

# Health Care Reform:

## Looming fears mask unprecedented employer opportunities to mitigate costs, risks and reset total rewards

Employers have little hope that the Patient Protection and Affordable Care Act (PPACA) will help them achieve their top goals to decrease the health care cost trend and improve workforce health. But they remain committed to their role in providing employer-based coverage — at least for now. Indeed, most employers are convinced that health care reform will lead to increased costs and a stepped-up exodus from employer-provided retiree medical coverage, according to the findings of a May 2010 Towers Watson survey on health care reform.

Although employers appear to be bracing for the worst, they are just beginning to assess the broader impact of the law on their health benefit strategies and total rewards programs.

This survey of more than 650 mid- to senior-level benefit professionals provides a snapshot of how employers are responding to a host of health care reform challenges that have far-reaching implications for retention, recruitment, productivity, workforce planning, change management and every aspect of the evolving employer-employee deal.

### Employers' Forecast Is Grim for Achieving Top Three Goals

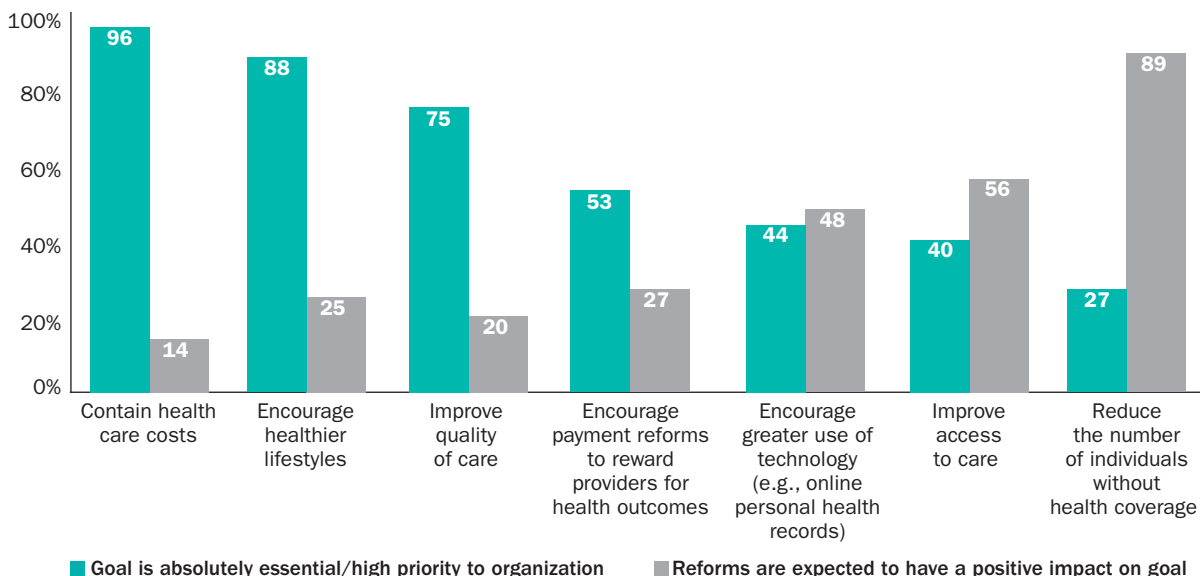
Employers' top three goals for health care reform are containing costs, encouraging healthier lifestyles and improving the quality of care. But as they look down the road to when health care reform is fully implemented, few employers think this legislation will achieve the goals that are most important to them. Specifically:

- A mere 14% of respondents think health care reform will help contain health care costs.
- Just 25% think health care reform will encourage healthier lifestyles.
- Only 20% believe health care reform will improve the quality of care.

Indeed, the overwhelming majority (90%) of employers believe health care reform will increase their organization's health care benefit costs.

Employers do see some benefits of the new legislation. Eighty-nine percent of respondents expect health care reform to have a positive impact on reducing the number of individuals without health coverage, and 56% predict it will improve access to care (*Figure 1*).

**Figure 1. Importance and Impact of Health Reform Goals**



## Beyond the Horizon: Employers Have Unprecedented Total Rewards Opportunities

By providing pre-65 retirees with access to health benefit coverage in the individual insurance market, health care reform may have a sweeping impact on many individuals who have been reluctant to retire. Yet nearly half of employers (48%) think these reforms will have no impact in supporting early retirement objectives for some employees (see sidebar, “Retiree Medical Benefits: An Accelerated Rush to the Exit?” on page 6).

Similarly, most employers predict these reforms will have no impact on their organization’s ability to achieve key workforce management goals such as improving productivity, attraction and retention, and providing a competitive reward package. Specifically,

“What employers may not have focused on yet is an unprecedented opportunity to reshape their deal with employees and their total rewards package overall.”

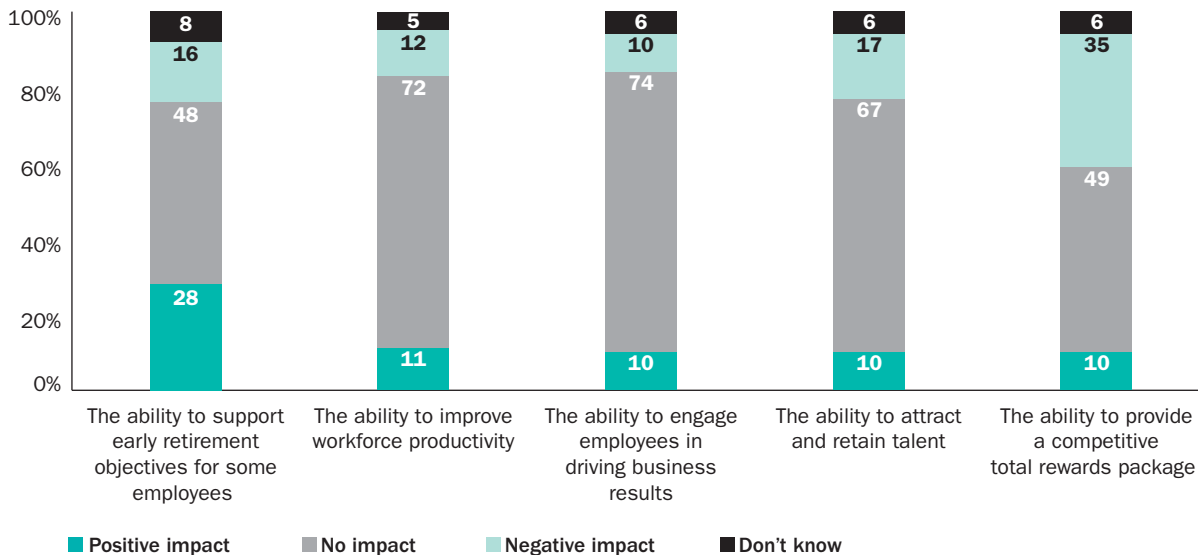
employers think health care reform will have no impact on these critical workforce management objectives (Figure 2):

- Improving workforce productivity (72%)
- Engaging employees in driving business results (74%)
- Attracting and retaining talent (67%)
- Providing a competitive total rewards package (49%)

What’s more, 35% believe that health care reform measures may even have a negative impact on their ability to provide a competitive total rewards package. What employers may not have focused on yet is an unprecedented opportunity to reshape their deal with employees and their total rewards package overall.

What these findings suggest is that respondents are just beginning to get their arms around this massive, highly complex legislation and have had little time to perform an in-depth analysis of its various business, benefit, workforce and total rewards implications. This limited insight may also be coloring the relatively high percentage of “don’t know” responses on key issues throughout this survey.

**Figure 2. Expected Impact on Organizations’ Workforce Management Objectives**



## Employer Actions

### Education Is Key

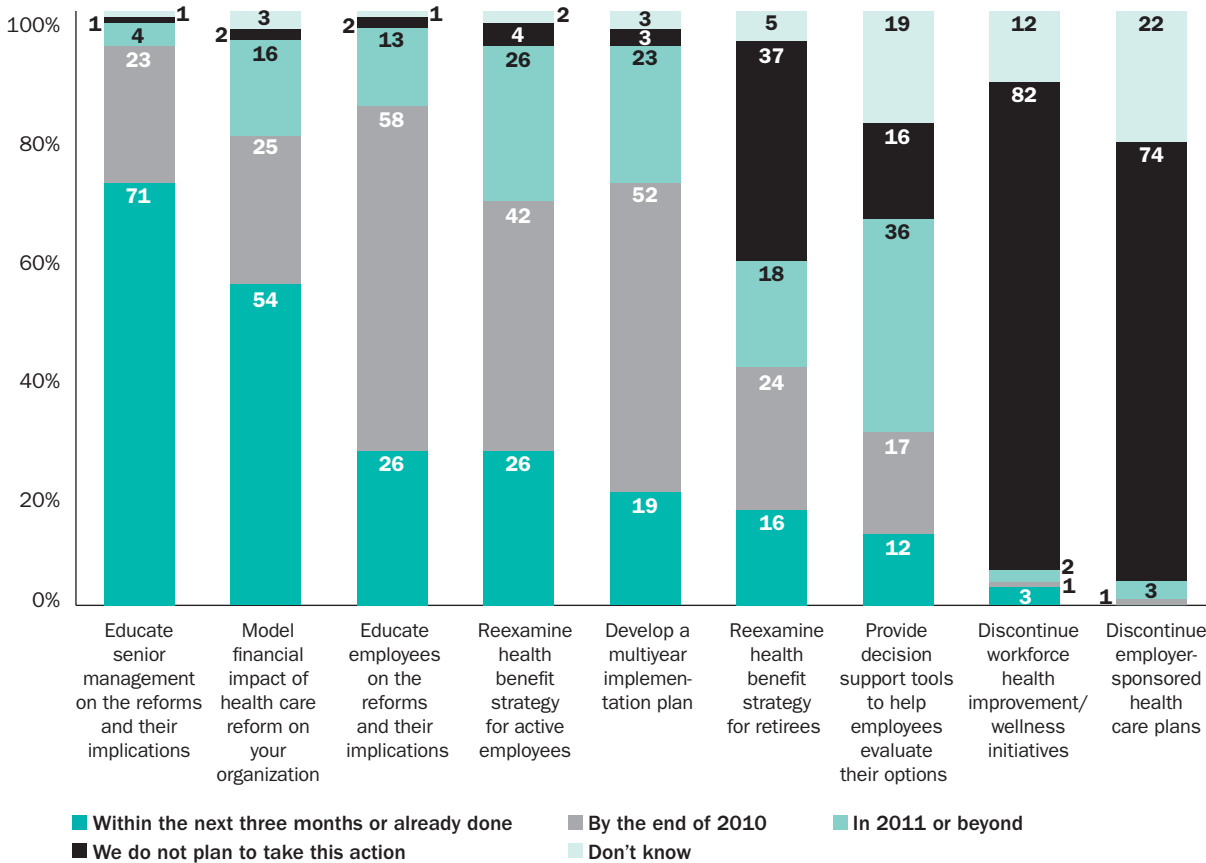
Now that health care reform is here to stay, respondents' most pressing short-term actions focus on educating senior management and employees on the reforms and their implications, and modeling the financial impact of health care reform on their organization (Figure 3).

By the end of 2010:

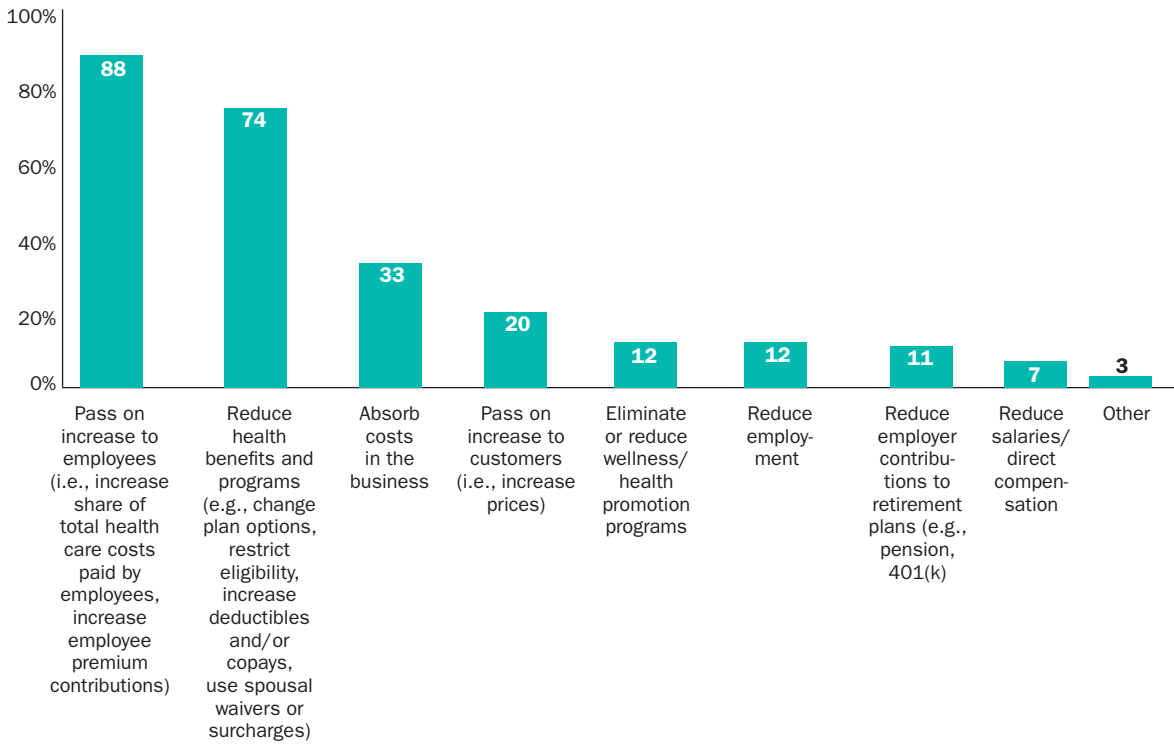
- 94% of employers plan to educate senior management on the reforms and their implications.
- 79% of employers plan to model the financial impact of health care reform on their organization.
- 84% of employers plan to educate employees on the reforms and their implications.
- 71% of employers plan to develop a multiyear implementation plan.
- 68% of employers plan to reexamine their health benefit strategy for active employees, versus 40% for retirees.

“Respondents’ most pressing short-term actions focus on educating senior management and employees on the reforms and their implications.”

**Figure 3. Organizations’ Likely Actions and Time Frames in Response to Health Care Reform**



**Figure 4. Likely Actions If Reform Increases Organization's Health Care Benefit Costs (multiple responses allowed)**



**A Broad Brushstroke of Employer Actions Is Anticipated — Depending on Costs**

The majority of employers anticipate that health care reform will increase their organization's health benefit costs. In response, most say they plan to pass on the increase to employees (88%) or reduce health benefits and programs (74%) (Figure 4).

On the other hand, if health care reform reduces costs, most employers would retain the savings (59%), pass the savings on to employees by reducing their total share of health care costs or premiums (49%) or offer enhanced wellness/health promotion programs (45%).

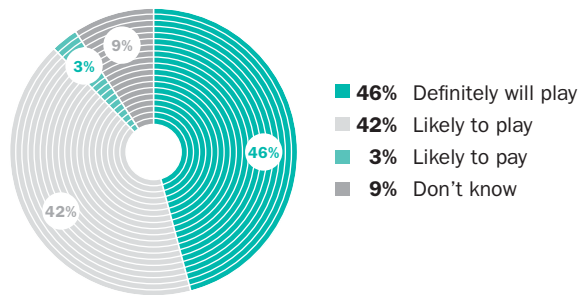
On a positive note, 82% of employers remain committed to their leadership role in creating a culture of health by providing workforce health improvement/wellness initiatives.

**Play-or-Pay Implications: Employers Say They Will Play, Not Pay**

Beginning in 2014, employers must offer minimal essential coverage to full-time employees or pay a penalty. When this provision takes hold, 88% of surveyed employers are either definitely, or likely, to play by continuing to provide health benefit coverage. But as the law's administrative and financial implications become clearer, employers can't rule out the possibility that their perspective may change (Figure 5).

“Beginning in 2014, employers must offer minimal essential coverage to full-time employees, or pay a penalty.”

**Figure 5. Likelihood That Organization Will Play or Pay**



### Reform Could Drive an Increase in Consumer-Driven Health Plans

Fifty-eight percent of employers surveyed believe health care reform will drive large employers to adopt replacement consumer-driven health plans (CDHP)\* for their active employees. These plans are being offered by an increasing number of employers to drive down costs and encourage employees to be more accountable for managing their health and the cost of their care.

On another note, 48% of respondents believe the PPACA will increase the number of large employers offering wellness programs and support, which is consistent with our findings throughout this survey that focus on initiatives aimed at decreasing costs and improving productivity by promoting prevention and employee health.

“Beginning in 2018, plans with group health coverage exceeding specified premium cost thresholds will be subject to an excise tax.”

### The Excise Tax Could Hit Many Employers

Beginning in 2018, plans with group health coverage exceeding specified premium cost thresholds will be subject to an excise tax.

Among employers with medical plans for active employees:

- Less than half (43%) believe they will be subject to an excise tax.
- 6% don't know whether they will subject to an excise tax.

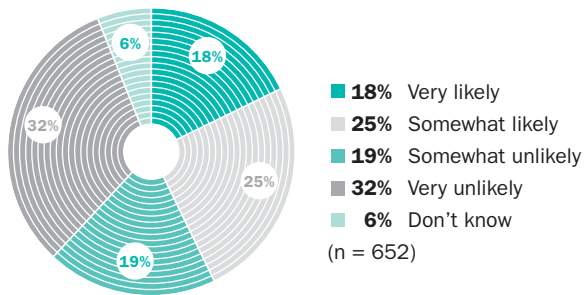
Among employers with medical plans for retirees:

- 34% believe they will be subject to an excise tax.
- 11% don't know whether they will be subject to an excise tax (Figure 6).

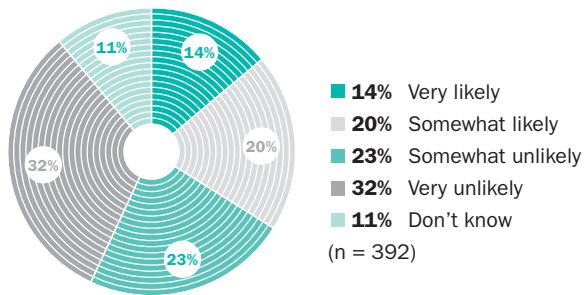
Employers have reason to be more concerned about this provision of the PPACA than indicated by their responses. Insight gleaned from our extensive research and client experience indicates that more than 60% of companies will reach the proposed excise tax on high-cost plans in 2018 if the current trend continues. Of equal concern, the adverse impact of legislated caps would increase over time. The good news is that employers can take actions now to delay hitting the excise threshold by up to five years (see “Health Care Reform Road Map: Areas of Focus,” on page 7).

Figure 6. Likelihood That Organization Will Be Subject to Excise Tax

#### Medical plans for active employees



#### Medical plans for retirees



Base: Those offering medical plans (n varies by plan)

\*Towers Watson defines a CDHP as a plan with a deductible offered together with a personal account — a health savings account (HSA) or health reimbursement arrangement (HRA) — that can be used to pay a portion of the medical expense not paid by the plan. A total replacement CDHP would mean the entire workforce would have only this plan option.

## Retiree Medical Benefits: An Accelerated Rush to the Exit?

Employer-sponsored retiree medical benefits have decreased in popularity in recent years as employers seek ways to control their health benefit costs. According to survey respondents, health care reform is likely to accelerate the employer exit. Today, only 45% of employers provide retiree medical benefits, and only 22% offer subsidized retiree coverage to future retirees joining the company as new hires, according to the Towers Watson 2010 Health Care Cost Survey, which was fielded before the passage of the PPACA.

Now that the bill has passed, 77% of respondents say there is likely to be either a moderate or significant decrease in the number of large employers offering employer-sponsored retiree medical benefits.

What's more, 58% say their own organization is likely to reexamine its health benefit strategy for retirees, with 40% doing so by the end of 2010 and another 18% planning to do so by 2011 or later. Finally, fully 43% say their organization is likely to eliminate or reduce retiree medical programs as a result of health care reform (Figure 7).

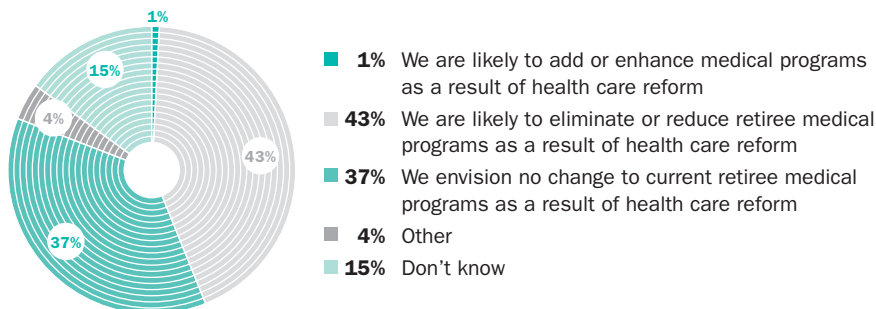
The anticipated increase in employer health care costs is likely driving this view as organizations start to consider areas where they can cut back on costs while having the least impact on their active employees. But other factors could also impact the decision to eliminate retiree health plans, including loss of the tax-free nature of the Medicare Part D Subsidy (Retiree Drug Subsidy) in 2013.

For companies that offer pre-65 retiree medical benefits, the PPACA may be a boon. If the legislation works as intended, the robust individual health insurance market that exists for Medicare-eligible retirees will extend to pre-65 retirees. That could allow employers to exit their sponsorship of retiree medical programs while still providing any desired financial subsidies to their retirees. By converting their current commitment into a reimbursement account and allowing retirees to choose how to spend it, employers can offer a subsidy while reducing their administrative costs.

There are other options as well. Employers that don't currently offer health savings accounts (HSA) could consider doing so, since an HSA offers a tax-effective way for active employees to save for retiree medical costs and for pre-Medicare retirees to pay for health care. A retiree medical savings account (RMSA) allows employees to accumulate unused health care funds provided through active employee plans and use them in retirement. Unfortunately, less than a third of respondents to our 2010 Health Care Cost Survey said they offer HSAs, and only 9% offer RMSAs.

For many employers, their current retiree medical plan offerings can be expensive. With the PPACA and options such as HSAs, there are new ways for employers to provide security for their employees in retirement without incurring the continuing high cost of a full retiree medical program.

**Figure 7. Organization's Likely Commitment to Retiree Health Strategy, Including Prescription Drug Coverage (post-health care reform)**



Base: Those offering retiree medical plans (n = 392)

## Health Care Reform Road Map: Areas of Focus

Health care reform presents a host of challenges for employers that go well beyond health benefit costs. However, there are a number of actions employers can take right now to mitigate risks and take advantage of newfound opportunities. Although there is no one-size-fits-all strategy, these are some initial actions employers may want to consider:

- **Know your numbers**

The implications of health care reform will be far reaching for cost management, talent management and productivity. To position themselves for the long term, employers need to model the financial implications, the myriad business scenarios and the impact of health care reform legislation on their current employee value proposition.

- **Keep abreast of evolving regulatory interpretation**

One of the most prominent features of the PPACA is its complexity and sheer volume. As a result, interpretive regulations to implement the law will be required for years to come. Keeping abreast of this evolving guidance and sharing the emerging implications with key stakeholders, including boards of directors and senior management, is critical.

- **Reevaluate your retiree medical strategy**

Consider anticipated health plan costs post-health care reform and the role of retiree medical in your total rewards program. For example, what is the appropriate role for your organization in light of opportunities that will be available in 2014? How might changes in the retiree medical offering impact other elements of total rewards?

- **Stave off the excise tax**

Data from the 2010 Towers Watson Health Care Cost Survey showed that top performers\* have the potential to stave off the excise tax threshold for roughly five years, or until 2023. Program design, including the use of CDHPs and other strategies to drive continued improvement in workforce health, are some of the tools employers are likely to use to keep costs at or below the medical cost component of the Consumer Price Index.

- **Keep up the momentum with your workforce health programs**

Most employers understand that strong workforce health will deliver a competitive advantage in a number of ways. For starters, there's a strong, demonstrated link between workforce health and a healthy bottom line. Even more striking is the correlation between senior management interest in employee well-being and employee engagement. According to research we've conducted over multiple years in countries around the globe, a vibrant

“Employers need to model the financial implications, the myriad business scenarios and the impact of health care reform legislation on their current employee value proposition.”

“culture of health” environment sends a strong message that senior leaders are concerned about employee well-being. Finally, engaged employees are far more likely to devote discretionary effort to their jobs, which in turn leads to performance improvement for the organization.

- **Prepare your organization for change**

Regardless of whether an employer decides to pay or play, successive waves of changes will be inevitable in the years to come — culminating with Open Enrollment in 2013, when the health care reform “big bang” will occur from a communication standpoint. This event will likely require significant effort to educate and engage employees. As with any major change initiative, people need to be involved in order to build acceptance and adjust behaviors. Proactive organizations will begin now to enlist support from leaders, solicit input from employees and build the communication infrastructure required to support this major change.

- **Take a holistic view of talent management opportunities**

Clearly, health benefit programs can play an important role in employee attraction, retention and engagement, to name just a few talent management issues. Health care reform presents unprecedented opportunities for employers to press the reset button on their total rewards proposition and employer-employee deal as they make critical choices about where to invest their benefit dollars, which is likely to have a ripple effect on the business overall.

## Looking Ahead

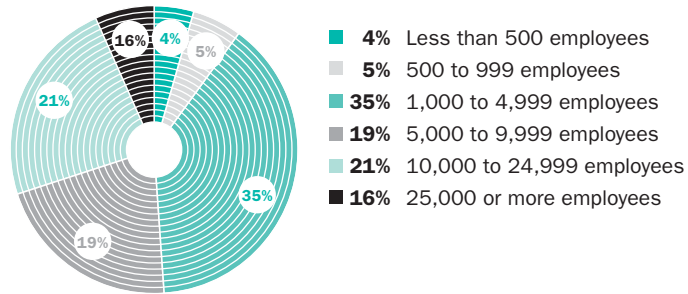
Although the jury is still out on how the many health care reform provisions will play out, one implication is increasingly clear: Employers need to respond quickly and thoughtfully by developing the necessary business planning, analytics modeling and decision support to stay in front of these complex issues. While the PPACA is fraught with challenges, it also presents employers with unparalleled opportunities to impact staffing and reward strategies, recruitment and retention, change management, and many other business issues that will have deep-seated and long-lasting implications for their organizations.

\*According to the 2010 Towers Watson Health Care Cost Survey, High-performing companies — the top tier of survey respondents — successfully hold cost increases at or below the medical cost component of the Consumer Price Index.

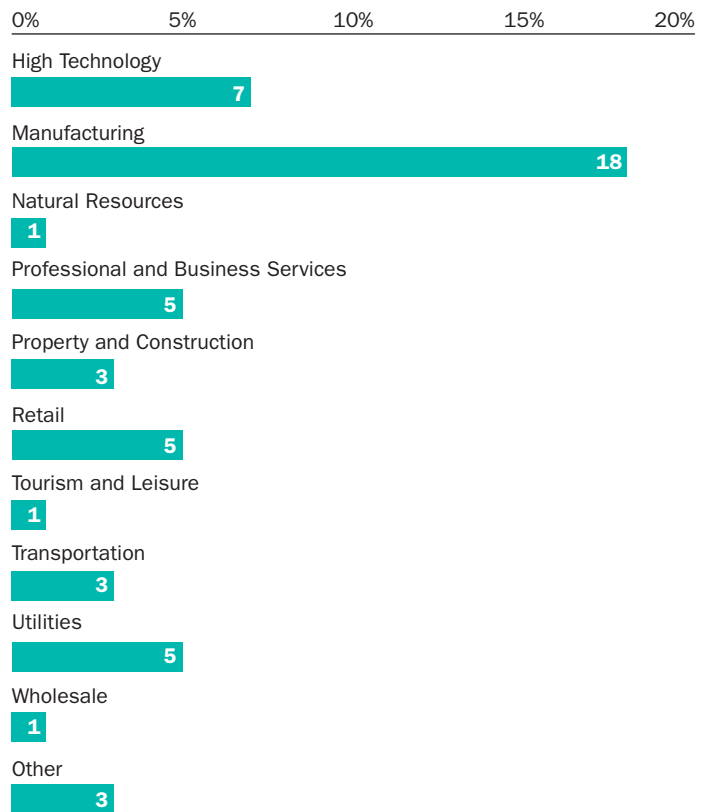
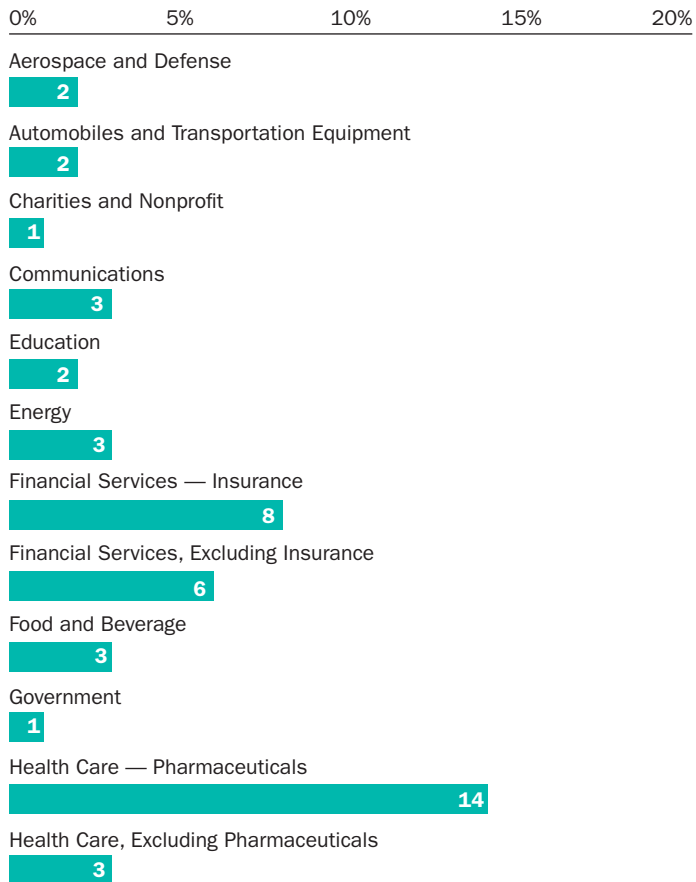
## About the Survey

This study captures the opinions of leading employers on key elements of the PPACA and their expected impact on organizations. The survey was conducted online between May 3 and May 10, and drew responses from 661 HR and business professionals working in midsize to large companies based in the United States across a broad cross section of industries.

## Organization Size (number of employees)



## Industry



## About Towers Watson

Towers Watson is a leading global professional services company that helps organizations improve performance through effective people, risk and financial management. With 14,000 associates around the world, we offer solutions in the areas of employee benefits, talent management, rewards, and risk and capital management.