

# BENEFIT

## *Plan Developments*



A monthly report covering plan design and legislative changes

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## Health Care To Become The Most Expensive Employee Benefit

Health insurance will soon replace pensions as the most costly type of employee benefit, according to a newly released study by the Employee Benefit Research Institute (EBRI). But a further EBRI study indicated that, while many employers are considering adopting consumer-directed health plans to control costs, these high-deductible plans often fail to meet the needs of employees.

Based on an analysis of federal data, the EBRI study on the cost of employee benefits found that, in 2004, retirement plan expenditures represented 47.1% of employers' total spending on benefits, while health care accounted for 43.2% of spending. By contrast, researchers noted, health care benefits made up 38.3% of total benefit outlays in 1990 and 26.7% in 1980.

When spending on mandatory benefits such as Social Security and

Medicare were excluded, health care spending was found to be even higher. In 2004, 57.4% of spending by employers for voluntary benefits was for health care, compared with 41.2% for retirement plans. The study found that the shift in spending on voluntary benefits took place

between 1980 and 1990: health insurance premiums represented 36.0% of voluntary benefits expenditures in 1980, and that share rose to 52.1% by 1990.

While the bulk of employee compensation remained in the form of wages and salaries, benefits expenditures comprised an increasing share of compensation outlays during the period studied. Benefits expenditures accounted for just 5% of total compensation in 1950, but they had risen to 19% by 2004, according to the report. Over the same period, the percentage of compensation that took the form of health care benefits jumped from 0.5% to 8%.

In another study, sponsored by EBRI and the Commonwealth Fund, researchers looked at employee response to high-deductible health plans (HDHPs) and consumer-directed health plans (CDHPs), new forms of health coverage designed to lower health care costs for employers

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by giving employees greater responsibility for their health care expenditures.

HDHPs have deductibles of \$1,000 or more for individuals and \$2,000 or more for families. HDHPs combined with tax-advantaged savings accounts, usually Health Savings Accounts (HSAs) or Health Reimbursement Arrangements (HRAs), are known as CDHPs. Contributions to CDHP accounts, which may be provided by employees and/or employers, are to be used to pay for health care not covered by the HDHP.

The national survey of participants in various types of health plans found that those enrolled in CDHPs and HDHPs tend to be less satisfied with their health coverage than individuals with comprehensive insurance: 63% of respondents with comprehensive health insurance said they were extremely or very satisfied with their health plans, compared with 42% of CDHP participants and 33% of HDHP participants. Moreover, only 46% of CDHP enrollees and 30% of HDHP participants indicated they were extremely or very likely to stay with their current health plans if given the opportunity to switch, compared with 60% of participants in comprehensive plans.

The survey also found that, on average, consumer-driven and high-deductible plan participants devote a larger share of their incomes to health care costs than comprehensive plan participants. Results showed 42% of respondents with CDHPs and 31% of those with HDHPs—but only 12% of respondents with comprehensive plans—reported spending 5% or more of their incomes on out-of-pocket health care costs and insurance premiums.

The prospect of having to pay for health care does appear to make participants more cost-conscious, but it may also discourage them from seeking needed care, the survey further revealed. Some 70% of CDHP enrollees and 60% of HDHP participants strongly or somewhat agreed that they considered costs when deciding whether to see a doctor or fill a prescription, compared with 40% of comprehensive plan partici-

pants. In addition, 35% of individuals with CDHPs and 31% of those with HDHPs said they had delayed or avoided obtaining care, compared with 17% of comprehensive plan enrollees. Participants with chronic health conditions or incomes below \$50,000 were especially likely to forgo care, the survey found.

Karen Davis, president of the Commonwealth Fund, said, “These findings provide evidence that high-deductible and consumer-driven plans may undermine the two basic purposes of health insurance: to reduce financial barriers to needed care and protect against high out-of-pocket cost burdens for patients. Enrollees with low incomes or with health problems are particularly vulnerable to spending a high proportion of income on medical expenses under these types of plans.”

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## IBM Enhances 401(k) While Freezing Pension Plan

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IBM announced in January it would freeze its defined benefit pension plan, but it softened the blow to employees by introducing a substantially enhanced 401(k) plan. The move was seen as further evidence that the shift from defined benefit to defined contribution plans is accelerating among large U.S. employers, including financially stable companies with well-funded pension plans like IBM.

The company said employees would stop accruing benefits in its defined benefit plan on December 31, 2007 and would retain only the benefits earned based on salary and service as of that date. The changes would not apply to current retirees or employees who retire before the start of 2008.

At the same time, IBM said it was redesigning its 401(k) plan to make it one of the most generous in corporate America. Under the enhanced plan,

current pension plan participants would receive company-funded 401(k) contributions equaling up to 10% of their annual salaries, with 6% paid in the form of dollar-for-dollar matching contributions and 1% to 4% made as automatic contributions. To ensure full participation in the 401(k) plan, the company said it would open accounts to receive the automatic contributions even for employees who do not contribute their own money.

IBM had announced previously that all U.S. employees hired after January 1, 2005 would be enrolled in the company's 401(k) plan. The company reported that, at the end of 2005, its defined benefit plan was fully funded in excess of the projected benefit obligation, with more than \$48 billion in assets. Its 401(k) plan, with \$26 billion in assets, was the largest in the country. More than 90% of IBM's U.S. employees participate in the 401(k) plan, the company noted, with 88% of participants contributing at least 6% of pay.

Explaining the reasons behind the move, Randy MacDonald, IBM senior vice president, human resources, said, "In recent years, IBM has been following a global strategy to move toward defined contribution retirement plans for both existing employees and new hires. These changes are consistent with this direction and will give us more predictable retirement plan costs, along with benefits that remain ahead of—but more in line with—our competitors."

MacDonald added that, by altering its retirement benefit offerings, IBM expected to better control retirement plan expenses, while preserving earned benefits and providing employees with "a leading-edge 401(k) plan that will be one of the richest in the country and a standard in the United States." MacDonald also acknowledged that recent moves by the U.S. lawmakers and regulators to tighten the funding and reporting requirements on defined benefit plan sponsors played a role in the company's decision to freeze its traditional pension plan.

A number of companies in ailing sectors, such as the airline and steel industries, have terminated their pension plans due to acute funding shortfalls. But other U.S. employers not facing severe financial difficulties have recently announced plans to halt accruals or close their defined benefit pension plans to new employees, including Verizon, Motorola, and Lockheed-Martin.

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## Unions Promote Legislation Forcing Large Employers To Pay For Health Benefits

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The AFL-CIO has announced it is putting pressure on lawmakers in 33 states to pursue legislation requiring large employers, including Wal-Mart, to provide health insurance to employees or contribute to Medicaid expenses.

The AFL-CIO, a federation of unions representing nine million workers, launched its "Fair Share Health Care" campaign on January 5. The organization said it is working with state legislators to introduce and pass laws that would force large employers to offer their workers affordable health care benefits or contribute a percentage of payroll to state-sponsored funds that would provide benefits to the uninsured. The 1.8-million member Service Employees International Union has a similar initiative, "Americans for Health Care."

AFL-CIO President John Sweeney said, "We cannot afford to stand by and wait for the federal government to take action on these issues critical to working families—and we won't."

Citing a Commonwealth Fund study, Sweeney said more than one-quarter of workers in companies with 500 or more employees lack employer-provided health insurance.



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Among the campaign's main battle-grounds is Maryland, where legislators were expected to override Gov. Robert Ehrlich's veto of a bill that would require companies with more than 10,000 employees to spend a minimum of 8% of payroll on health care benefits or contribute to Maryland's health insurance program for the poor. Wal-Mart is currently the only company in Maryland that would be affected by the bill.

While the state bills vary, most proposals mandate that employers above a certain size commit between 8% and 11% of their payrolls to health care benefits or pay an equivalent amount to a state fund that would subsidize insurance coverage for low-income workers. The AFL-CIO said it would also focus on legislative efforts in states including Colorado, Connecticut, Wisconsin, Iowa, Georgia, Michigan, and Washington.

Bruce Josten, the U.S. Chamber of Commerce's executive vice president for government affairs, criticized the Maryland initiative. "States should be exploring ways to lower health care costs and help small business owners gain access to affordable, quality care rather than wasting time on half measures like this that ignore the reality of the health care crisis in this country," Josten said.

The Chamber also pointed out that forcing large employers to pay for a specified amount of health care benefits may violate the federal Employment Retirement Income Security Act (ERISA).

Proponents of the unions' approach argue that—far from creating a less competitive business environment—laws that lead to increased health insurance coverage rates among a state's residents should lower premium costs for companies currently providing health care benefits and reduce the burden on state taxpayers.

"Businesses that play fair and provide health care for their workers are forced to shell out over \$30 billion to cover those other businesses' workers," Sweeney asserted. "That's in addition to

the estimated \$150 billion they spend on their own workers' health care costs. Meanwhile, Medicaid's skyrocketing costs are being driven even higher by profitable employers who tell their workers to sign up for the program rather than give them health care."

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## U.S. Health Spending Accounted For 16% Of GDP In 2004

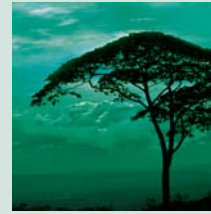
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Health care spending represented 16% of the U.S. economy in 2004, the highest share on record, according to an article by economists from the Centers for Medicare and Medicaid Services published in the January issue of *Health Affairs*. Growth in national health spending slowed to a rate of 7.9% in 2004, but reached a total of \$1.87 trillion, or \$6,280 per capita, the report said.

Researchers largely attributed the lower growth rate, down from 8.2% in 2003, to cost-saving efforts by employers and health plans, which included encouraging the use of generic drugs and mail-order services, as well as the introduction of higher co-payments. The figures showed, however, that outlays for doctors' services and hospital care continued to increase at rates comparable to previous years.

Spending on prescription drugs rose 8.2% in 2004, compared with nearly double that rate five years ago, the article said. But because pharmaceutical expenditures made up just 11% of overall health care consumption, this reduction failed to prevent an increase in health expenditures that was well above the 2004 overall inflation rate of 2.7%.

The report also noted that, as health care became more expensive, employers appeared to be shifting a greater share of premium costs on to employees, with companies cutting their premium contributions for workers by 1.3% in 2004.




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