

## Case Study: How A Cash Incentive Strategy Can Dramatically Reduce Health Plan Costs For Any Employer That Offers Their Employees A Generous Health Plan

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Employer Z has an employer contribution of 90%. Their health plan also has very low deductibles and co-pays which makes it a very attractive health plan. Employer Z has 500 employees and the average employee salary is \$40,000 per year. Their employees can either choose individual coverage or family coverage, and no employees are uninsured.

Out of their 500 employees, 200 are unmarried and 300 are married. Out of the 300 married employees, 230 of them have a working spouse that has access to a health plan where they work. These 230 employees could enroll their family in their spouse's health plan (i.e., opt out) if they wanted to. When an employer offers a very generous health plan, very few of their "potential opt outs" will opt out. For simplicity, let's assume that none of the 230 "potential opt outs" opted out of this very generous health plan. The other 70 married employees either have a spouse that doesn't work, or their spouse has a job but they don't have access to a health plan where they work, so these 70 families can't opt out. A summary appears below:

	<u>Employees In The Health Plan</u>
200 Unmarried Employees That "Can't Opt Out"	200 With Individual Coverage
300 Married Employees	
230 That Could Opt Out If They Wanted To ("Potential Opt Outs")	
All 230 Didn't Opt Out	230 With Family Coverage
70 That "Can't Opt Out"	<u>70</u> With Family Coverage
	500 Employees In The Health Plan

Let's assume that the health plan's total annual cost **for their next plan year** will be \$7,000 for individual coverage and \$20,000 for family coverage. Therefore, employer Z's total annual cost next year will be \$7,400,000 **under the status quo**. (i.e.,  $(200 \times \$7,000) + (300 \times \$20,000) = \$7,400,000$ )

**Fairness would dictate** that employer Z should only have half of their 230 "potential opt outs" in their health plan which is 115. Since all 230 "potential opt outs" are in their health plan, employer Z is covering 115 "extra" families. This results in health plan costs that are **\$2,300,000 higher than what's considered fair** assuming that the total annual cost of each family is \$20,000. Therefore, employer Z's health plan costs in their next plan year will be **45% higher than what fairness would dictate under the status quo** (i.e., \$7,400,000 versus \$5,100,000).

There are many strategies that employer Z can use to dramatically reduce or potentially nearly eliminate this huge "extra cost". Now, we'll examine a simple strategy that they could use starting at the beginning of their next plan year. Any generous employer could use this strategy whether their health plan is self-funded, fully insured, or experience rated.

**Starting next year**, employer Z will offer their employees \$4,000 if they enroll their family in their spouse's health plan. They'll receive this \$4,000 every year that they remain in their spouse's health plan. Although there are many considerations involved when a family is deciding on which of the two health plans they should be in, \$4,000 per year is an attractive offer since the average salary of employer Z's employees is only \$40,000 per year. (Most employers that offer cash incentives only offer their employees \$1,000 or \$2,000 which won't generate many new opt outs. On the other hand, some employers offer \$6,000 or more.)

Let's assume that 70 of the 230 who didn't opt out decide to take advantage of this \$4,000 offer and opt out next year. Therefore, employer Z will have 430 employees in their health plan next year.

200 Employees With Individual Coverage That Obviously Can't Opt Out  
160 Employees With Family Coverage That Could Have Opted Out But Didn't  
70 Employees With Family Coverage That Can't Opt Out  
430 Employees In The Health Plan

Let's assume that the 70 new opt outs are **30% less costly** than the 160 that could have opted out but didn't because families with existing medical problems rarely opt out of their current health plan. Therefore, the total annual cost associated with the 70 new opt outs WOULD HAVE BEEN \$15,407 PER FAMILY IF THEY STAYED IN EMPLOYER Z's HEALTH PLAN (which they didn't), and the total annual cost of the 160 that could have opted out of employer Z's health plan but didn't will be \$22,010 per family. (NOTE: The weighted average of the 70 families at \$15,407 and the 160 families at \$22,010 is \$20,000. Also note that \$15,407 is 30% less than \$22,010.)

Here's the calculation:

$$\begin{aligned}160 Y + 70 (.70 Y) &= 230 \times \$20,000 \\209 Y &= \$4,600,000 \\ \text{So, } Y &= \$22,010 \\ \text{And } .70 Y &= \$15,407\end{aligned}$$

Therefore, employer Z's total cost next year (ignoring the cash incentives that must be paid) will be:

$$(200 \times \$7,000) + (160 \times \$22,010) + (70 \times \$20,000) = \$6,321,600$$

However, employer Z must pay \$4,000 to each of the 70 new opt outs. This amounts to a \$280,000 expense which makes the health plan's total annual cost (after cash incentives are paid) equal to \$6,601,600. This \$6,601,600 is **\$798,400 less** than the \$7,400,000 that their total health plan costs would have been if there were no opt outs next year which represents a **10.8% cost savings**.

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We have a seminar called "Highly Effective Cost-Control Strategies" that's primarily intended for brokers and employers that have a self-funded (or a partially self-funded) health plan which we offer once a year. The topic that's examined above is just one of the many types of highly effective cost-control strategies that we examine during this ground-breaking seminar. Check out our "Upcoming Seminars" section on the home page to get all the details regarding this seminar and to find out when it will be offered. If this seminar isn't currently scheduled, you can send us an email at [smsnow@smsnow.com](mailto:smsnow@smsnow.com) and we'll notify you when we have scheduled this seminar.

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