

# Preserve and Protect

## ***How Public Sector Employers Can Provide Excellent Benefits While Controlling Costs***

***Benefits at Work Series***

**A Colonial Life White Paper**

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# Executive Summary

All employers — whether in the public or private sector — face unprecedented challenges when it comes to meeting employee expectations and finding ways to control health care costs. Cost increases for health insurance and employee benefits continue to set records for all sectors of the U.S. economy. Premiums for family health insurance coverage increased 113 percent from 2001 to 2011<sup>1</sup> and are expected to rise 5 percent to 7 percent in 2012.<sup>2</sup>

Public sector employers face additional challenges. With revenue shortfalls and increased public scrutiny, it's no surprise the vast majority of government employers are looking for options to reduce benefits costs.<sup>3</sup> Public sector employee benefits have become a politically charged target in an era where all government spending is under close examination.

Yet governments have historically used generous health insurance and benefits packages to hire and retain quality employees. As a result, public sector workers have made long-term decisions based on their expectations that these benefits will continue. This means their employers must be careful how they manage this necessary and potentially frightening cultural shift to maintain employee satisfaction and productivity. And indeed, most government employers aren't planning to eliminate health benefits<sup>4</sup> — but they *are* looking at their options.

Change in employee health benefits is inevitable, but it can be managed and even used to improve employee relations. Government employers have access to many proven solutions to control and even reduce costs while continuing to offer a strong benefits package.

This white paper draws on several studies that demonstrate the effectiveness of multiple strategies for public employers to save money while preserving the value of their benefits packages. These include greater participation in pretax benefits and Section 125 programs, wellness initiatives, partnering for improved benefits communication and education, adding voluntary benefits, and implementing a dependent verification process.

**Government employers have access to many proven solutions to control and even reduce costs while continuing to offer a strong benefits package.**

# Rising Health Insurance Costs Collide with Falling Revenues

An aging population, advances in medical technology, more expensive medications and other factors have all driven up the cost of health care — and health insurance. According to a report by the Kaiser Family Foundation, employers paid an average annual premium of \$15,073 for family coverage in 2011, an increase of 9 percent over the previous year.<sup>5</sup> The same report found the cost of family coverage has doubled since 2001.<sup>6</sup> City governments spend an estimated \$30 billion a year on employee health benefits.<sup>7</sup>

**Family coverage annual premium 2010 – 2011**



*Source: Kaiser Family Foundation, September 2011*

**Cost of family insurance coverage doubled in last decade**



Planned and potential changes in health care laws make the future uncertain. Although federal health care reform legislation attempts to control insurance costs, making some screenings mandatory and adding coverage for adult children may instead lead to higher costs. What's more, some experts predict the price of medical care will continue to climb.<sup>8</sup> And no matter what happens, health care costs for public sector employers are too high to sustain.

State and local governments are already facing significant financial stress from the most recent recession, exacerbating the need to control benefits costs. Their revenues declined 22.1 percent from 2008 to 2009. Taxes represent the largest source of general revenue for both state and local governments — nearly half of general revenue at the state level and 40 percent for local governments. State and local governments saw those tax collections decline 4.5 percent from 2008 to 2009. Meanwhile, expenditures increased 4.6 percent, and indebtedness increased 5.1 percent for state and local governments during the same time period. Local governments were especially hard-hit, accounting for 61 percent of the total indebtedness. Higher unemployment contributed significantly to the problem: State and local government spending on unemployment compensation jumped 86 percent from 2008 to 2009.<sup>9</sup>

And a change in fortune is not yet in sight. Although property tax receipts nationwide actually increased slightly in 2009, they generally lag real estate assessments from one to several years. That means recent declines in property tax assessments may not be reflected for several data cycles.

Declining revenue streams and rising costs make health benefits management more difficult than ever for government employers. The good news is cost-containment strategies are readily available, proven to work, and can be implemented at no direct cost to the employer.

**City governments spend an estimated \$30 billion a year on employee health benefits.**

# Proven Strategies for Cost Containment

## Wellness initiatives

Wellness initiatives are employer efforts to improve the overall health of employees, and sometimes dependents, with the goal of decreasing health care costs and increasing productivity. They can take many forms, from on-site fitness centers, to nutritional counseling, to employer-subsidized gym memberships and employer-sponsored events. Other initiatives include health risk assessments such as lifestyle questionnaires and biometric evaluations, self-help educational materials, individual counseling and behavior modification programs. Some initiatives focus on one aspect of health, such as weight loss, smoking cessation or fitness.

Weight loss is a frequent goal of wellness initiatives, and with good reason. Two-thirds of adults are overweight, resulting in 36 percent higher spending on health care and 77 percent higher spending on medications than those with a healthy weight.<sup>10</sup> Workers who are above normal weight and have three or more chronic health conditions report an average of 3.5 unhealthy days per month, which translates into 42 days per year. Unhealthy workers' absenteeism costs our economy \$153 billion.<sup>11</sup> Presenteeism — employees who come to work while unwell — also negatively affects productivity and morale.

## Measuring results

Wellness initiatives work, and the results can be measured in:

- Fewer sick days
- Reduced occurrences of preventable chronic conditions
- More positive work environment
- Increased productivity
- Higher employee retention rate due to improved morale<sup>12</sup>

**Estimates show a return of three-to-one or higher for every dollar invested in a wellness program.**

Results also can be measured directly on the bottom line. Estimates from different studies vary but consistently show a return of three-to-one or higher for every dollar invested in a wellness program. One study of return on investment for large employers with more than 1,000 employees showed an average return of \$3.27 over a three-year period for every dollar spent.<sup>13</sup> Another study showed employer savings on health insurance costs as high as \$6 per dollar invested.<sup>14</sup>

"Public employers clearly see benefits that help them maintain a healthy and productive workforce can also be effective strategies for controlling their benefits costs," said Anne Spray Kinney, director of research and consulting for the Government Finance Officers Association.

## Case Study

The City of Lewiston, Maine, implemented a wellness program for its 443 employees in 2006. The city consequently saw its health insurance premiums decrease by \$786,757 through 2008. From 2007 through 2010, health insurance premiums increased an average of 3.3 percent, well below the national average.

*Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.*

## Making wellness work

Wellness programs are generating a lot of enthusiasm among both public and private employers. Wellness-related initiatives were among the top cost-control strategies implemented by employers in a recent survey of government financial officers. Nearly 80 percent of survey respondents have added wellness initiatives to their benefits program, and 90 percent of those recommend them to others; nearly two-thirds recommend them strongly.<sup>15</sup> That aligns with a Society for Human Resource Management report showing 75 percent of employers supply their workforce with wellness resources and information.<sup>16</sup> However, 58 percent of employers report low engagement as the greatest obstacle to the success of their wellness initiatives.<sup>17</sup>

### Wellness initiatives are among top cost-control strategies used by employers



Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.

Two factors are at work here. The first is whether the wellness program is a good fit for the employee population. The second is the critical role of effective communication and education to drive employee engagement and participation in a wellness program.

- **Good fit.** Employers should first assess the particular health risks of their workforce. Biometric evaluations, claims analysis and employee surveys should provide a window into what types of health risks any wellness initiative needs to address. After examining the most common types of claims, most common predictive factors and highest-cost diseases, employers can then develop a focused program designed to reduce the occurrences of these targeted health claims.
- **Communication.** Employers can partner with workplace benefits providers that have the experience and skills to effectively communicate with and educate the workforce about wellness initiatives. This drives up participation rates and generates the enthusiasm needed for the program's success.

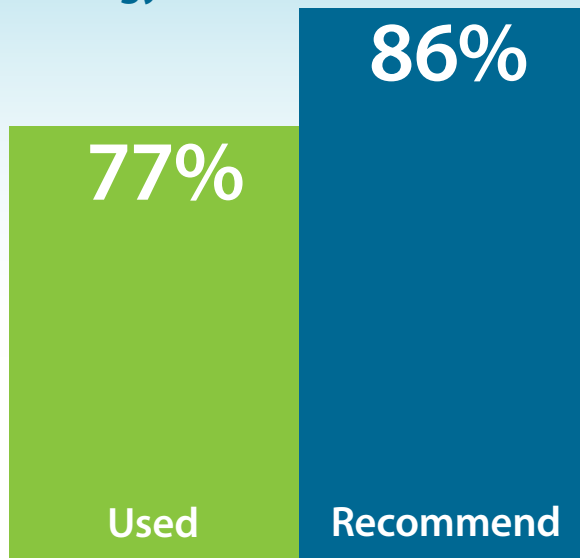
## Pretax benefits/Section 125 participation

Equaling wellness programs as a highly implemented and recommended cost-control strategy in the recent government financial officers survey was establishing Section 125 plans and maximizing employees' participation in pretax benefits programs. More than three quarters — 77 percent — of employers surveyed say they offer pretax benefit plans, and 86 percent of those recommend this option.<sup>18</sup> In fact, at 73 percent highly recommended, it was the most enthusiastically endorsed strategy of the survey options, and only 3 percent were unlikely to recommend it.

Pretaxing benefits gives employees the option to buy qualified insurance coverage with before-tax dollars. This has the effect of making coverage more affordable by reducing the taxable portion of employees' pay, so they pay lower income taxes. Section 125 plans allow employees to make before-tax contributions to personal spending accounts that can be used for qualifying health care or child care expenses. Because they reduce the employer's overall payroll, these plans also can reduce the employer's payroll taxes, including FICA, Social Security and Medicare matching taxes.

Like wellness programs, pretaxing of insurance purchases and flexible spending account contributions must be effectively communicated to employees during the enrollment process so they understand, appreciate and participate in these programs. A benefits partner that can demonstrate the value to employees through customized salary illustrations and benefits statements can help drive stronger participation and higher cost savings. This is best accomplished through individual, face-to-face enrollment meetings with each employee.

### Pretaxing benefits/Section 125 participation widely used and highly rated as cost-control strategy



Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.

### Case Study

A North Carolina community college with about 1,000 employees streamlined its benefits enrollment and enhanced communication of its flexible spending account, increasing participation by 68 percent. This created more than \$100,000 in tax savings for employees and \$26,000 in FICA savings for the college.

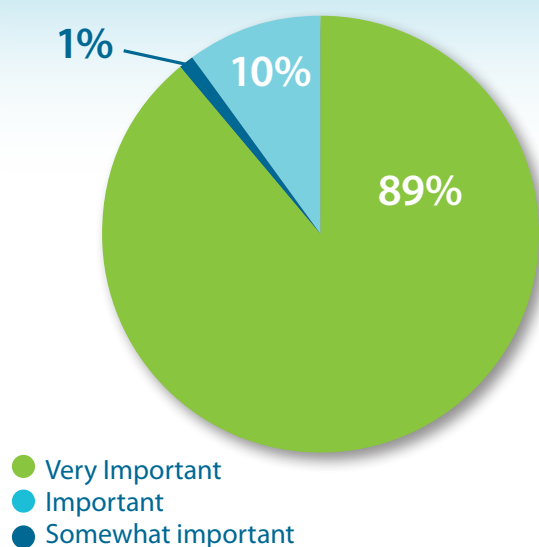
Source: Colonial Life customer case study.

## Benefits communication and education

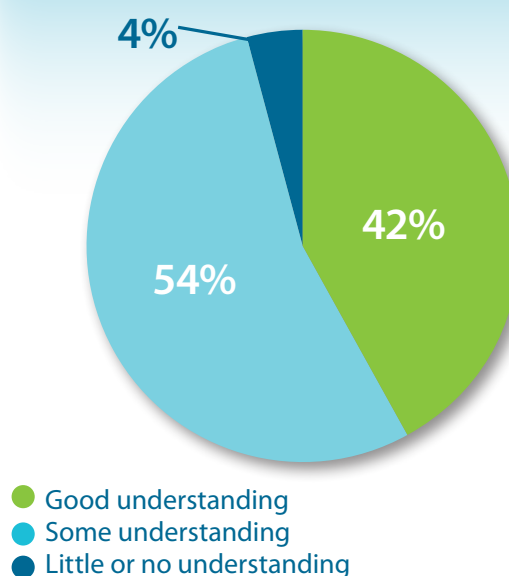
When dealing with a cultural change as fundamental as remaking the benefits that have been in place for a generation, effective communication and education about these changes are vital to the program's implementation and success. Employees who have survived layoffs, rumors of layoffs, news about falling revenues and cutbacks in services will be apprehensive and suspicious about changes, especially if these changes could affect the financial security of their families. In some cases, the benefits package is so long-standing and entrenched, it's seen as an entitlement.

Public sector human resources managers almost unanimously agree it's important for employees to understand their benefits and appreciate their employers' investment in them. In a recent survey of members of the International Public Management Association for Human Resources, 89 percent of respondents say it's *very* important. However, like their counterparts in commercial industries, they don't think their employees actually do understand their benefits. Just over half — 54 percent — think their employees have *some* understanding, and only 42 percent say their employees have a *good* understanding.<sup>19</sup>

### How important is it for employees to understand benefits?



### How well do employees understand benefits?



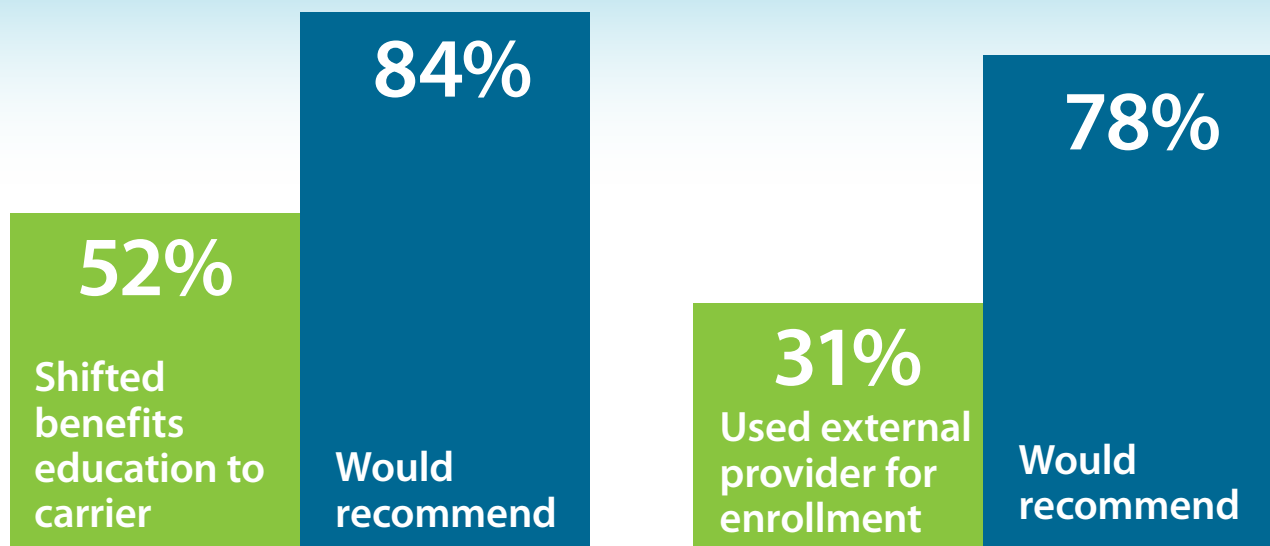
Source: International Public Management Association for Human Resources survey, September 2011.

Employers need to reach out to employees individually to educate them about the value of their benefits plan, or the whole workforce may react to changes with hostility. At the same time, few public employers are equipped to handle benefits communication themselves. However, employers can transfer the cost of benefits plan communication to their benefits suppliers. They also can outsource an enrollment system and open enrollment management rather than maintaining a system and processing responsibilities fully in-house. Best of all, these services are available at no direct cost to the employer from some benefits providers.

Although this shift to external resources for benefits communication and enrollment responsibilities is well-recommended by those using it, it's not yet widely implemented. In the government financial officers survey, only 31 percent of employers were using an external service provider for benefits enrollment and 52 percent had shifted benefits education and communication expense to suppliers. However, 78 percent of those who outsourced enrollment would recommend it, and 84 percent recommended using a benefits carrier to handle benefits education and communication.<sup>20</sup>



## External support for education and enrollment is underused but highly recommended by employers



Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.

One strategy is to educate employees about the value of their benefits so they better appreciate the investment the employer is making and the true costs of their benefits, not just their out-of-pocket portion. A popular tool for this kind of communication is a benefits statement. Benefits are a significant piece of employee compensation, yet most employees don't understand the value of what they are receiving. A benefits statement lists the benefits available to the employee and their monetary value. In addition, group and individual meetings held near enrollment can supplement the written statement, giving employers the opportunity to explain benefits in person and make sure employees understand what is available.

Benefits communication should be built into the enrollment process itself. Employers can use their benefits provider for all aspects of enrollment including publicizing it, educating employees about their choices and what to expect in the upcoming enrollment, meeting one-on-one with employees, answering questions, verifying contact and eligibility information, and maintaining and managing the system.

### Case Study

The City of Montgomery, Ala., has 2,750 employees spread out in 59 locations, but a small human resources staff. The city partnered with a full-service employee benefits provider to plan and deliver an extensive communication and enrollment plan including one-to-one benefits counseling sessions, group meetings, emails, customized benefits booklets, website content and daily enrollment reports to the HR team. As a result, 86 percent of employees met individually with a benefits counselor, the number of flexible spending account participants tripled and employee awareness and understanding of the benefits package was increased.

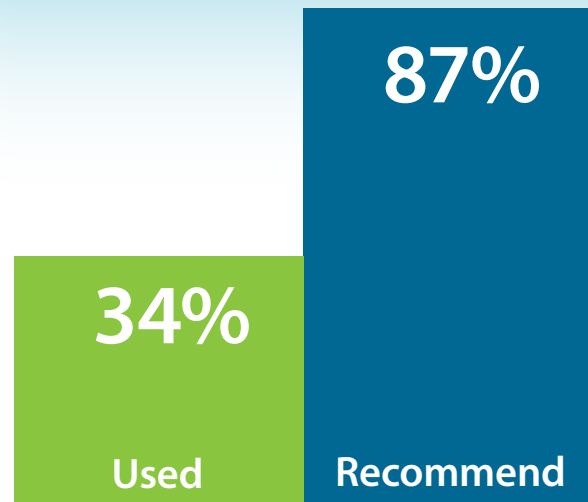
Source: Colonial Life customer case study.

## Voluntary benefits

One underutilized solution to the public sector's benefits problem is to move noncore benefits to employee-paid voluntary benefits. This option allows employees access to expanded benefits options to meet their unique family situations, and coverage is typically more affordable than they could obtain themselves outside the workplace. Moving some benefits to voluntary coverage also can support a health plan design strategy by helping alleviate some of the potential for employees to experience higher out-of-pocket costs associated with higher deductible and co-insurance requirements that may be part of the new core benefits plan. At the same time, there is no direct cost to the employer because employees choose and pay for the coverage they want.

This strategy is another example of a change that fewer employers have yet to implement, but those who do give it very high marks. Only about a third of employers in the government financial officers study said they have moved noncore benefits to employee-paid voluntary coverage. However, 87 percent of those employers recommended this strategy, and 70 percent recommended it strongly.<sup>21</sup>

Moving noncore benefits to employee-paid voluntary is one of most highly recommended strategies



Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.

## Typical voluntary benefits

**Disability insurance.** Helps protect employees' most valuable asset: their income. This insurance replaces a portion of an employee's income to help offset the financial losses that may result when an employee is disabled.

**Life insurance.** Coverage may include term, whole or universal life.

**Hospital confinement indemnity insurance.** Helps fill the gaps in most major medical coverage and helps provide benefits for a covered hospital stay. Benefits can be used for medical or nonmedical expenses.

**Specified disease.** Designed to supplement major medical coverage to help with the high cost of cancer and critical illness treatment. This coverage can help pay for the nonmedical expenses that can decimate a family's savings, such as for travel, child care and loss of income while in treatment.

**Accident insurance.** Helps protect against significant medical and nonmedical out-of-pocket expenses for accidental injuries not covered by most major medical insurance.

# Dependent verification

Providing insurance coverage for dependents who are no longer eligible drives up the costs for public sector employers. While some cases of covering dependents who are no longer eligible are simply a misunderstanding by employees who fail to remove these dependents from their plans, others may be less innocent. Fraud does exist: Federal investigators reportedly found and recovered more than \$4 billion in health care fraud in 2011 alone.<sup>22</sup>

Health plan audits can reveal a significant number of ineligible participants, including dependents who are over age or who aren't blood relatives or a spouse. Also, former employees may not have been removed from the plan.

Yet, for most public employers, dependent verification is a costly and unproductive use of scarce resources if they try to implement it themselves. Some benefits providers offer dependent verification services free of charge annually as part of the enrollment process, making sure public sector employers aren't paying for coverage for people who aren't legitimately qualified. The potential cost savings offered by this free dependent verification can be considerable.

**Some benefits providers offer dependent verification services free of charge as part of the enrollment process.**

## Case Studies

The City of Dallas experienced a projected \$1.1 million dollars in medical claim savings as a result of a dependent verification process.

The City of Montgomery, Ala., realized a potential annual savings of more than \$1.3 million when it discovered nearly 9 percent of covered dependents — 288 people — were ineligible for benefits coverage.

Smaller governments can also realize savings. Upon an initial audit, a town of 20,000 people found \$20,000 in potential savings on an annual \$1.2 million budget for employee health benefits.

*Sources: Colonial Life customer case studies; Government Finance Officers Association, "Containing Health Care Costs," 2011.*

## Other strategies

Surveys of public employers show they're using several other strategies to contain benefits costs, but few are being implemented by a strong majority, and of those, few are strongly recommended to their colleagues. Further, many of these strategies can have significant negative impacts on employees that might be avoided by using other cost-control methods.

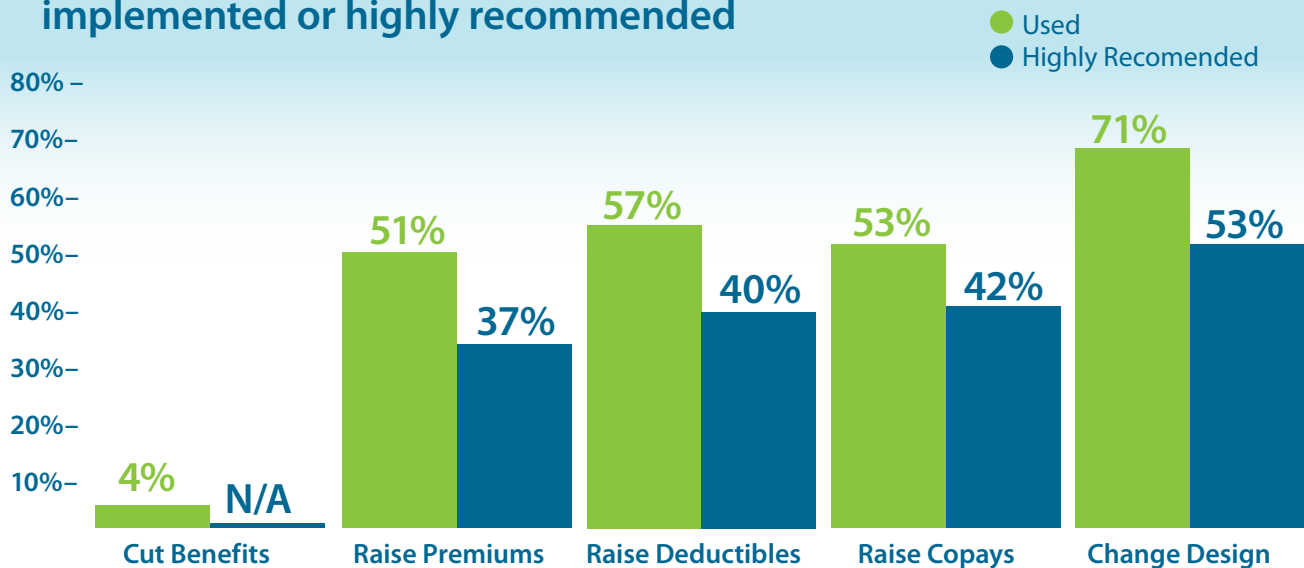
**Eliminating benefits.** This might seem like the simplest and easiest way to cut costs, but government employers are avoiding this strategy. Only 4 percent of respondents in the government financial officers survey say they're eliminating health benefits, such as dental, vision or family coverage for active employees.<sup>23</sup> The recent International Public Management Association for Human Resources survey showed only 14 percent of respondents plan to eliminate some benefits within the next year.<sup>24</sup>

**Increasing health insurance premiums.** Half of the government financial officers survey respondents reported using this strategy, but only 37 percent highly recommend it.<sup>25</sup> A slightly larger percentage — 64 percent — of IPMA-HR survey respondents said they planned to increase employees' premiums within the next year.<sup>26</sup>

**Increasing health insurance deductible or co-payments.** This strategy was reported to be in use or planned for use within the next year by just over half of the government financial officers survey respondents<sup>27</sup> and even fewer — 45 percent — of the IPMA-HR survey respondents.<sup>28</sup>

**Changing the health plan design.** This strategy includes carving out pharmacy benefits, expanding the use of generic drugs, implementing health savings accounts, tightening provider networks and implementing disease management. Although it was the fourth most-popular strategy in the government financial officers survey, implemented by 71 percent of respondents, it received a lukewarm evaluation. Only about half of those who made this change would recommend it to others.<sup>29</sup>

### Other cost control strategies not widely implemented or highly recommended



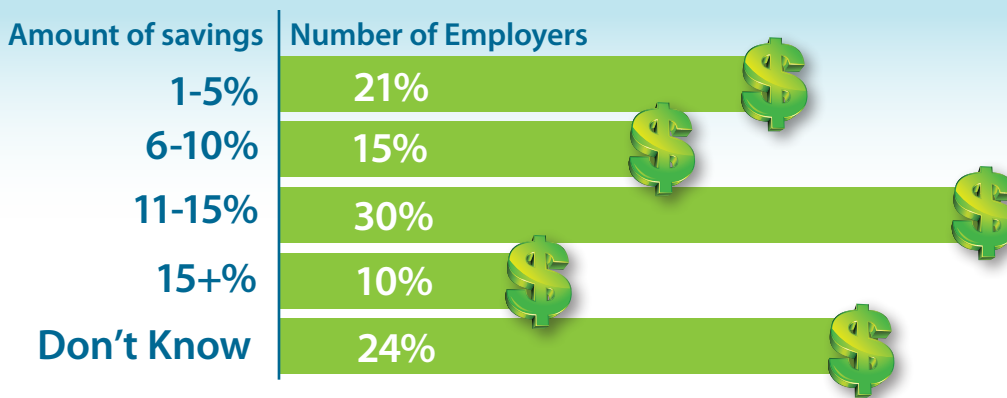
Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.

# Dollars and Sense: Cost Savings on Benefits

City governments nationwide collectively spend an estimated \$30 billion a year on employee health benefits.<sup>30</sup> The recent government financial officers survey showed more than half saved at least 6 percent on their benefits during a two-year period by implementing some of the cost-control strategies mentioned in this white paper, and 40 percent saved more than 10 percent during that time period.<sup>31</sup> Based on aggregate spending by municipalities, even a modest 3 percent annual savings on health benefits costs would represent \$900 million in savings. That's close to \$1 billion that municipal governments could funnel back into underfunded programs to prevent reductions in staffing and service levels.

As remarkable as this figure is, another revealed by the government financial officers survey is almost more startling: A quarter of respondents who implemented cost-containment strategies don't know how much they saved. This lack of awareness may point out a need for public employers to get help capturing and quantifying their potential savings — another opportunity they may be able to realize through an effective partnership with an employee benefits provider.

## City government savings on health benefits in most successful two-year period using cost-management strategies



Source: Government Finance Officers Association, "Containing Health Care Costs," 2011.

## Selecting a Benefits Partner to Help Implement Change

The solutions recommended in this paper can help public sector employers and elected officials, as well as their private sector counterparts, make the smart choices and changes their benefits plans need for long-term sustainability. However, success can still be elusive. *How* employers make the necessary changes is just as important as the changes themselves. The right employee benefits partner can make the difference between success and failure. Factors to consider when evaluating an employee benefits partner include:

- Experience in public sector business
- Proven track record of success
- One-to-one benefits counseling and enrollment capabilities
- Comprehensive package of products and services
- Excellent service reputation validated externally

# Taking Advantage of Proven Solutions and Support

Health care costs continue to rise, and health insurance keeps the pace. Even with predicted government caps on the rate of insurance increases, costs are already too high to manage for many employers. Public sector employers — who face the added challenge of communicating with a work force accustomed to exceptional benefits — now must find ways to keep these employees satisfied while changing, reducing or cost-shifting those benefits.

Fortunately, solutions to these problems have been implemented with proven success in both the public and private sectors. Employers can save money and preserve the value of their benefits packages by carefully selecting the most effective combination of strategies for their situations and needs, including enlisting the often-free support of qualified benefits providers.

“Focusing on the right cost-saving measures could have a significant impact on the bottom line while minimizing the impact on employees,” says Tom Cochran, chief executive officer and executive director of the U.S. Conference of Mayors. “Thoughtful implementation of strategies appropriate for each employer can help them continue to offer a stable benefits package in a more financially sustainable way.”

By considering factors such as the organization’s size, political environment, cost management goals, impact on employee health and access to care, employers can select from a range of options with the potential to significantly impact their health benefits costs, now and for years to come.

**“Focusing on the right cost-saving measures could have a significant impact on the bottom line while minimizing the impact on employees.”**

*Tom Cochran  
Chief Executive Officer and Executive Director  
U.S. Conference of Mayors*

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# About Colonial Life

Colonial Life & Accident Insurance Company is a market leader in providing insurance benefits for employees and their families through the workplace, along with individual benefits education, advanced yet simple-to-use enrollment technology and quality personal service.

Colonial Life offers disability, life and supplemental accident and health insurance policies in 49 states and the District of Columbia. Similar policies, if approved, are underwritten in New York by a Colonial Life affiliate, The Paul Revere Life Insurance Company. Colonial Life is based in Columbia, S.C., and is a subsidiary of Unum Group.

For more information on voluntary benefits, cost-containment solutions or benefits communication and enrollment support, call Colonial Life at (803) 798-7000 or visit **coloniallife.com**.