



pmi health group

Employee healthcare in the credit crunch

An FD's guide on how to keep a lid on rising medical insurance premiums in an uncertain economic climate

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How will the credit crunch affect corporate private healthcare schemes?

The onset of the 'credit crunch' and subsequent economic downturn has caused many organisations to review their expenditure. Employees' salaries and associated benefits form a substantial portion of a company's costs.

Whilst pay reviews have been limited to below inflation increases the cost of medical insurance has continued to rise at a much greater rate. With expenditure under such close scrutiny Chief Executives, Managing Directors and in particular, Finance Directors are starting to question the value of this benefit.

Employers have two main motivations for providing private medical insurance to their staff:

- as an aid to recruitment and
- retention as part of an employee benefits package or to form part of an overall employee healthcare strategy.

Medical insurance costs in the large corporate sector are driven directly by claims made in the preceding years and the assessment of the future risk.

Although there is little evidence to suggest that the actual incidence of claims is increasing, what is apparent is that there is an upward trend in the value of the claims made. This is borne out by the rise in the average cost of a claim which has a direct impact on premiums in subsequent years.

Why are claims costs rising?

Medical treatment is costing more

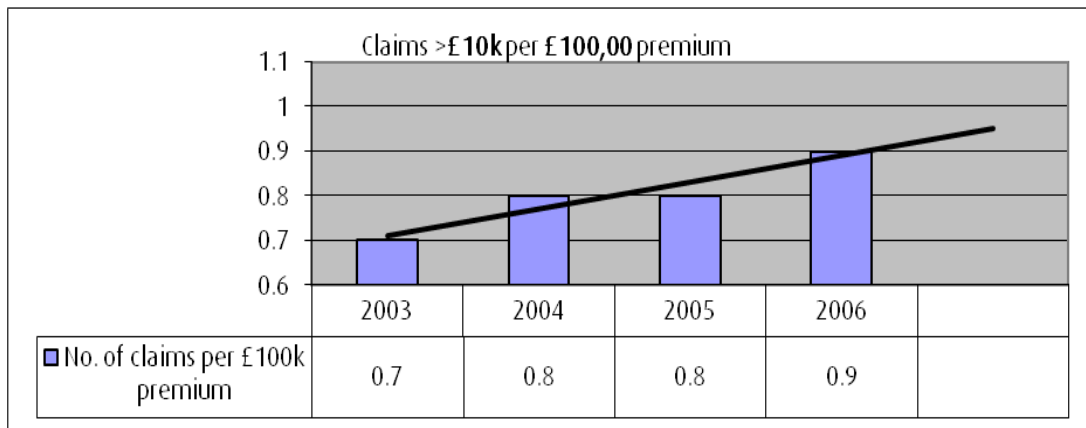
In 2003 a claim on a medical insurance policy would be regarded as high if it exceeded £10,000. Claims of this scale would include complex surgery, such as a coronary artery bypass graft or treatment for cancer that necessitated a combined chemotherapeutic and radiological approach.

The last two years have seen many more claims exceeding the notional £10k threshold, with claims over £50,000 becoming more common. This is largely, although not exclusively, due to the introduction of new chemotherapy drugs which are costly and not always freely available from the NHS.

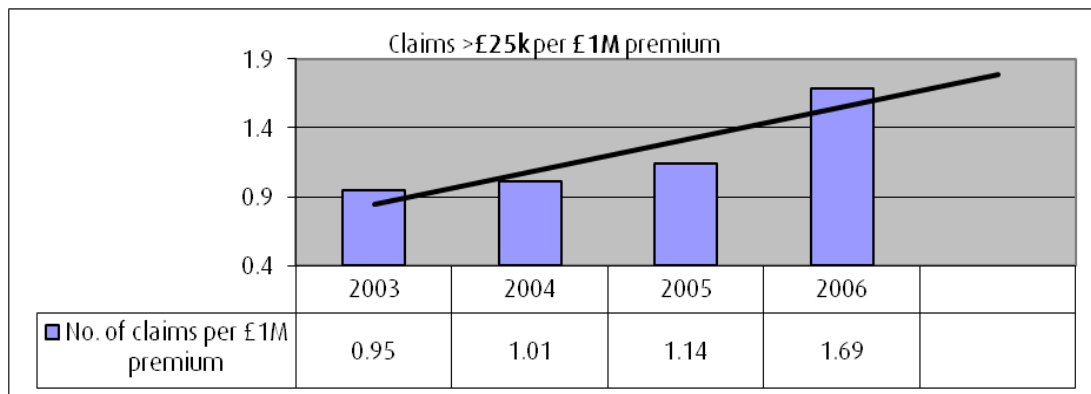
Research undertaken by PMI Health Group has identified that claims exceeding £25k increased by 69% in the period between 2003 and 2006 and the incidence of claims with treatment costs in excess of £50,000 have risen by 450%. The highest single claim recorded in the research data peaked in 2006 at a £110,000.

There is no evidence to suggest that high claims will do anything other than continue to rise at a rate that may well take employers and the medical insurance industry by surprise.

It has been established that for each £100,000 an employer spends on their medical insurance premium there is a strong likelihood of the occurrence of one claim over £10,000. The graph below shows that the probability has increased from 0.7 claims per £100k premium in 2003 to 0.9 in 2006. The graph is projected forward to 2007 to reach 0.95, although this may be too conservative an estimate.



When analyzing claims that have exceeded £25,000 the incidence has been quantified using £1m premium. The graph demonstrates that in 2003 approximately 1 claim over £25,000 occurred per £1m premium, this rate almost doubling in the projection for 2007.

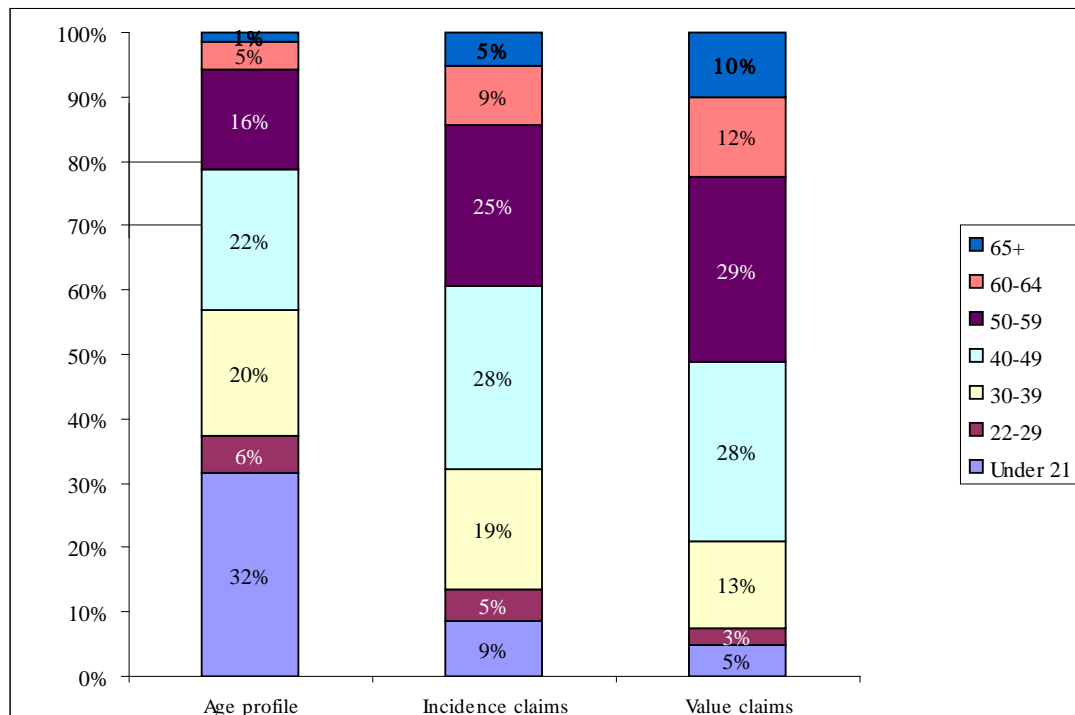


More people are working for longer

The age of the membership of a medical insurance scheme is a significant factor in the claims experience. Those policies with an ageing membership or a large number of retirees will present a greater risk than schemes with a younger, healthier profile.

The chart below shows a typical medical insurance scheme membership breakdown. Members and dependants under 40 present the most favourable risk – they make up 58% of the membership and account for 33% of the claims incidence and only 21% of the claims value. This group will generally make low cost claims.

The position deteriorates considerably in the 50+ age bands. Making up 22% of membership, they account for 39% of the claims incidence and over half (51%) of the claims spend.



The economic climate is changing

Changes in the economy have had a negative impact on many businesses. This is leading to an extremely cautious approach to expenditure being adopted and in some cases costs are being reduced through redundancy programmes.

More claims due to stress...

Financial uncertainty clearly places a strain on individuals and increases the reported levels of stress. Although stress may be the underlying causative factor, claims manifest themselves in a number of different ways, for example investigations and treatment of gastric and cardiac disorders become more prevalent.

Higher claims due to redundancy...

However, employees under threat of redundancy may be reluctant to have medical treatment as they perceive any sickness absence could be detrimental to their ongoing job security and new claims may fall until the point that redundancy notices are issued. Thereafter staff who are under notice will ensure that they claim for medical conditions before the entitlement to the benefit is lost, pushing up claims to an artificially high level.

How is your medical insurance scheme performing?

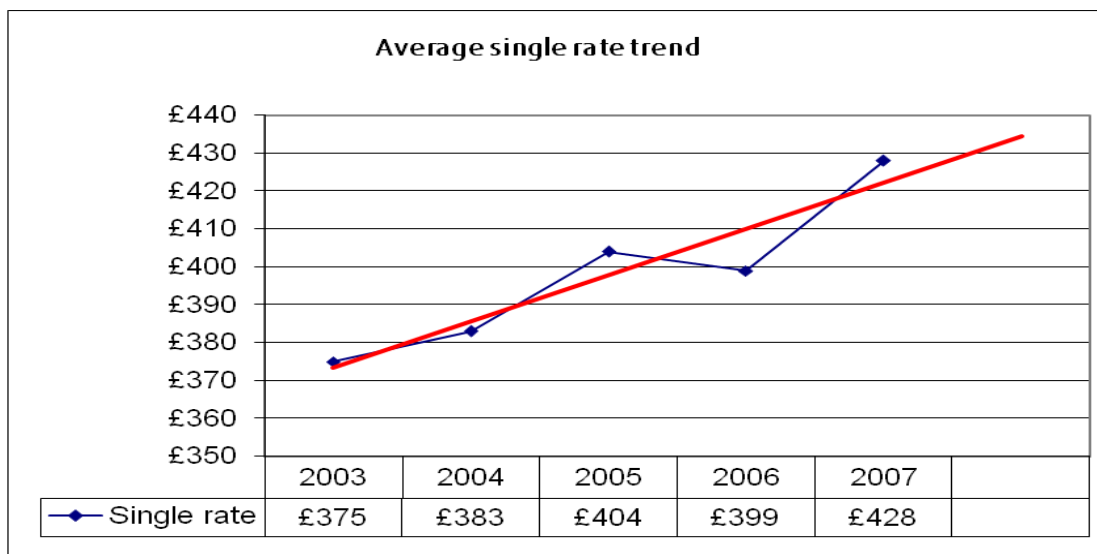
Insurers and the market generally quote a figure between 9 and 11% for annual medical inflation. Whilst this may be accurate in relation to voluntary and individual business, the figure for corporate insurance differs significantly.

The industry analysts Laing & Buisson have quantified the actual figures for each year.

2003-04	2004-05	2005-06	2006-07
4.8%	3.3%	5.0%	2.8%

In reviewing the performance of an experience rated medical insurance scheme the single rate cost is the most commonly referred to figure. This is the calculated cost of cover for a single member and is used throughout the industry to compare scheme pricing. It is also the figure declared to HMRC as taxable benefit.

The single rate is used by employers, insurers and brokers to assess the percentage price change of a contract. This is a more accurate method than using the gross premium which is affected by fluctuations in membership.



The graph above shows the average single rate based upon a representative sample of insurers and schemes nationwide. The red trendline, based on historic performance, plots the increase in single rate. This is projected forward in 2008 to be £434 on average, an increase of 1.4%. However this is too conservative – the single average rate for 2008 to date stands at £442, suggesting that inflationary increase of at least 3.3% should be expected. This reflects the rising cost of claims and the need for realistic pricing of contracts.

How do I control my premiums? 8 steps to better risk management

Limitless options exist to control claims costs but these need to be balanced against devaluing the benefit and negating the very reason for medical insurance to be offered to employees. Some practical measures for managing your healthcare risk are outlined below.

1. **Knowledge is power: review your claims data carefully.** Ask your HR team to undertake a review of claims made and the benefit structure of your medical insurance policy. This will help you to understand if there were any opportunities to control claims costs e.g. by negotiation with providers or amendments to the benefit structure to reduce risk. A professional adviser should be able to help with this.
2. **Identify negative trends and possible routes of action.** Analysis of claims will also highlight if there are any common patterns or trends. Where a cluster of claims exist, for example treatment for bad backs, further investigation may reveal the need for manual handling training and occupational health advice.
3. **Introduce on-site support.** Consider having an on-site physiotherapist. A quarter of all medical insurance claims relate to musculo-skeletal problems. Easy access to this service for employees saves time and cost.
4. **Remind employees that they are spending their own company's money.** Brand the medical insurance scheme to your organisation, not the insurer. This is beneficial in two respects: firstly, employees appreciate that you are providing a valuable benefit and secondly, it is more apparent that it is not just 'the insurer's money' that is being spent.
5. **Introduce limits on joining periods.** Good membership management can help you to protect your healthcare scheme: give employees the opportunity to join once each year reducing the likelihood of staff joining just to make a claim, remove scheme leavers immediately and have a separate arrangement for retirees to limit the impact on the claims experience.

6. **Educate your staff in the benefits of a combined NHS/private approach.** Help employees and dependants to understand when to use medical insurance. Acute, non-life threatening conditions fall within the scope of the private sector. Long-standing medical problems, often referred to as 'chronic' illnesses, such as diabetes are well catered for by primary care services within the NHS. Where treatment is required urgently for a life-threatening condition, the NHS should be the first choice. Promoting a combination of NHS and private treatment ensures that patients receive cost effective and appropriate care.
7. **Make the most of the benefits you pay for.** Look at all the employee benefits you provide and identify any areas of overlap e.g. in addition to your Employee Assistance Programme, counselling may also be provided by the medical insurer.
8. **Employ expert support to manage the value and volume of claims for you.** It is well worth investing in the services of a specialist claims management team, ideally manned by qualified nurses, who will act as the first point of contact for employees making a claim and assess each employee's needs as early as possible. They can also recommend appropriate treatment using a combination of both NHS and private medical options. The flexible approach ensures employees return to work or receive treatment as early as possible and via the most cost effective route.