THE POWER of ACTUARIAL VALUE

The Power to Change Conversations

A New Word for an Old Idea

When visiting a pediatrician, young children are weighed, measured, and told where they stand compared to others.

"58th percentile" she might say. Similarly, actuarial value provides brokers and employers a measure to start the conversation and frame the topic on the stature of their plan compared to others.

"Actuarial Value" is a new word for an old idea. It's simply the measure of the "richness" of a plan design. That is, what proportion of cost are passed to participants as deductibles and co-pays and what proportion is paid by the plan? If a change in deductible is worth 3%, for example, then the actuarial value (and the expected claims) has changed by 3%. Changing plan designs to keep up with inflation and dampen renewal increases is sometimes an annual event. However, determining the plan change value has been cumbersome – either ask the carrier for numerous options, use a table of pre-packaged prices for various plans, or, use the clumsy and difficult federal calculator.

The fourth option, re-computing the entire claim data set under a different plan design seems accurate and impressive, but can be very misleading since the claims mix is erratic year to year, especially for smaller employers. Last year's claims are generally not the best estimator of next year's claims. Claim re-compute models look backward, actuarial models look forward.

> The value of plan design changes has always been of interest at renewal time for employers.

"But there's much more"

The phrase "Actuarial Value" embedded in the 2010 Affordable Care Act raised awareness and interest in this concept. Plans with a minimum Actuarial Value of 60% were considered sufficient to avoid penalties. Beyond any insurance reform laws, the ability for brokers and employers to make side-by-side comparisons of health insurance plans — based on their actuarial value — provides great strategic advantage for plan modeling and financial planning of employee benefit plans.

But there's much more. The mathematics of actuarial value opens opportunities for brokers, advisors, employers, and even ancillary vendors such as bankers and accountants to make useful observations and advice. It's the measure nobody else uses that can make you look smarter than the other guy. Everybody likes to look smart.

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- Imagine an accountant that says to an employer, *"did you know your plan is richer than 85% of my other clients. Is that what you intended?"*
- Imagine a broker that says, *"Aetna is offering a 9% discount for this plan design change and we think it is worth 5%, so take the deal."*
- Imagine a consultant telling a self funded employer, *"your high option is actually less value than your low option"*. (This happens!)
- Imagine the HR Director telling the CFO, *"we are not charging employees enough for Option A based on its actuarial value"*.

Actuarial value can elevate plan design conversations to a strategic level through benchmarking to a broader book of business. How does an employer compare to peers? So much of plan design in place across employers in America is simply inertia, legacy, and happenstance. Can any employer explain why they have what they have, other than a jouncy road of changes year after year going back decades perhaps?

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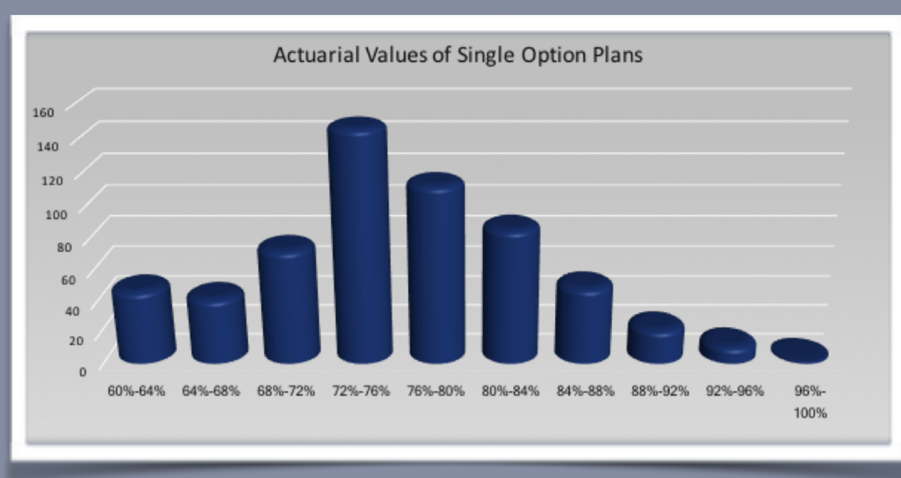
Employers have simply not had an easy way to benchmark the strength of their plan design and think about whether their plan offerings fit their employee benefit goals. A strategic approach for a broker is to lay out all their clients into a grid, show each employer where they stand, and ask the employer where they would like to be compared to others. Imagine a broker doing this for a prospect? Impressive.

QUINTILE	1	2	3	4	5
From	60%	70.2%	74.2%	77.6%	81.5%
To	70.1%	74.1%	77.5%	81.4%	97%

A STRATEGIC APPROACH FOR A BROKER IS TO LAY OUT ALL THEIR CLIENTS INTO A GRID, AND THEN SHOW EACH EMPLOYER HOW THEY COMPARE

Suppose the CFO wants to cut plan richness to save money, but the HR department wants to have competitive benefits. The actuarial value grid across all employers gives everybody an anchor and reference point in which to have a better discussion.

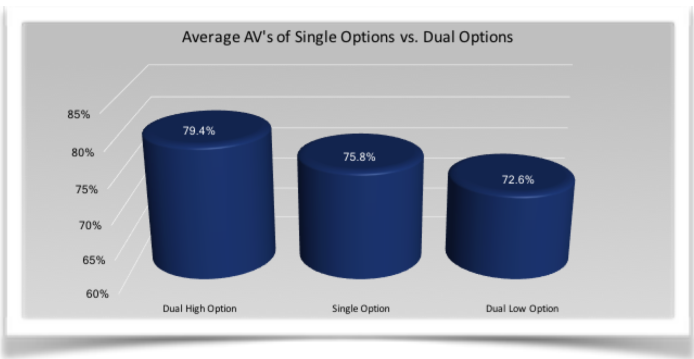


For example, the graph shows the plans offered by single option employers (from about 600 employers in our data base). The average, we call the "center of gravity", is about 76%. Percentiles or quintiles are easily drawn from these figures.

Dual and Triple Option Plans

We would expect to see employers offering multiple plan options to have a higher value option than an employer offering just one plan and we do.

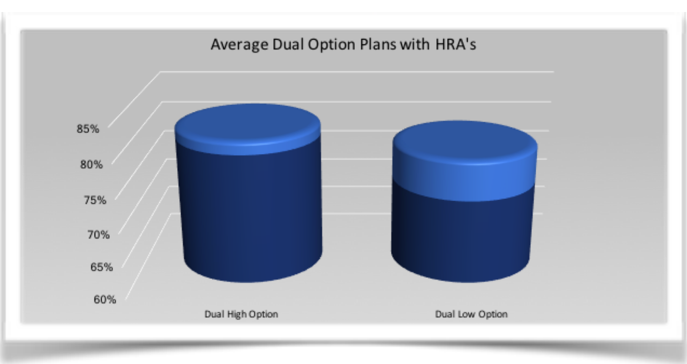
Similarly, the lower options of a multi-plan offering tend to be of less value than the single plan offer. The picture that emerges of a dual option employer is offering two plans that straddle the market average.



We see the average spread of a two option employer is about 6.8%, from 79.4% score for the high option to 72.6% score for the low option. The three option spreads are 84.1%, 78.4%, 71.9%.

You can see how such simple comparative information can immediately frame the debate for an employer in a much more meaningful way than in the past. The employer now knows where they sit compared to others. The distance between plan options has a frame of reference. The CFO might be able to cut costs and the HR people are still happy. Or vice versa. And the broker or advisor looks like a hero.

HRA Actuarial Values



Our data presented lacks the HRA/HSA designs that often accounts for the gap between plan options. A broker with their own block of business, or association survey, or chamber survey, could gather this data as well by bringing in the frequency and Actuarial Value impact of self-directed account values. Wow! We might find the gap between high option and low option is cut in half in cases where the low option includes an HRA.

Many HRA COBRA rate techniques in the market are questionable. That is, there are many non-actuarial methods being used to tack on COBRA values for HRA/HSA plans. Actuarial value is the correct way to settle this issue instead of the benchmarks and estimates and erroneous methods in common use. A good actuarial value calculator provides those answers.

Actuarial Value	81.4%
HRA Value	2.8%

Benefit Surveys

Actuarial Value can make plan design surveys obsolete – at least the part that tries to compare plan design elements of deductible, copay, and coinsurance components. For anyone who has ever tried this, a traditional plan design survey that tries to tabulate all the elements of plan design in a meaningful way is quite cumbersome. Table after table of comparisons of each plan design component (deductible, PCP co-pay, ER co-pay, coinsurance, out-P surgery, etc., etc.) leave the reader bewildered how they actually compare with others. Actuarial value has the power to sum it all up in one number.

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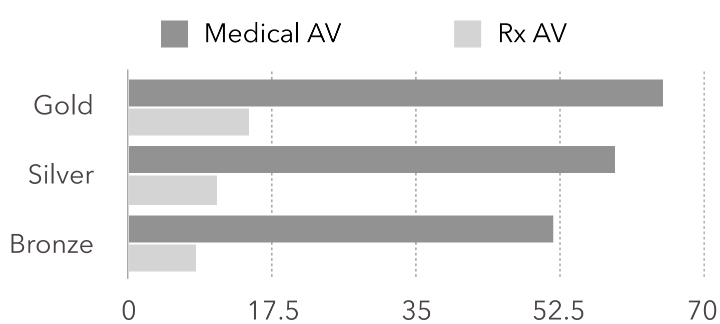
Simply scoring actuarial value of a large batch of plans is so much quicker and easier and more powerful. Even Rx benefits can be scored with actuarial value for a comparison with solely that component of benefits (see below). So can HRA or HSA. The first thing an employer needs to know is, "where do I sit compared to others?" Nothing could be simpler than saying, "*here's where you are, here's where everyone else is*".



Participant Out of Pocket Measures

For those concerned with participant out-of-pocket burdens, actuarial value provides an estimator of what employee costs might be. A comparison with actual employee out of pocket costs in the prior period would provide a surrogate measure of relative morbidity of the employee choice of plans. It's always interesting to see if sicker employees are stacking into the richer plans as expected. Actuarial Value scores provide the required base line to measure this.

Another interesting thought would be to help employees understand what they are buying. For example an employer may offer two plans with similar actuarial values. One plan may have a high upfront deductible for all services and the other plan may have copays for primary care, but less rich benefits when specialty services are utilized. Employees can then choose the plan that provides them with the most value based on their expected utilization. Without knowing the actuarial value, employees may see the copay plan as a better option, but may cost them more in the long run due to known family medical conditions.

Plan Design Details

Another window opened by actuarial value is the ability to quantify why a plan design structure didn't give the results expected.

Employers often overestimate the value of a copay or deductible. If a broker wants to look impressive, imagine these answers:

- *"That copay only effects about 2.5% of your costs so it wasn't worth much."*
- *"The plan has so many copays that the deductible only effects 45% of the costs."*
- *"Raising the Emergency Room copay is expected to impact about 42 visits for this population."*

With transparency, one can see the components of Actuarial Value broken down by the elements of plan design.

Full Value	100.0%
Deductible	16.2%
Coinsurance	4.9%
Copays	5.4%
Actuarial Value	73.5%

Actuarial Value calculators could be a secret weapon for brokers and others to differentiate their practice and gain competitive advantage on others – until the others catch up. Someday, we may all wonder how we got along without our desktop actuarial value calculator.

Contribution Health

Contribution Health helps employers manage the high cost and complexity of providing employee benefits by offering specialty actuarial, software, and compliance services for risk management, data analysis, legal compliance, and stop loss purchasing strategies. We work with licensed producers and brokers, human resources consultants, ACO's, risk pools, and third party administrators as their behind-the-scenes employee benefit subject matter experts providing compliance and actuarial services.

Contribution Health is the developer of www.freeactuarialvalue.com

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Contribution Health