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This Just In...

RETHINKING CASH BALANCE PLANS

## Rethinking Cash Balance Plans

 Short-term disability (STD) claims jumped tenfold over the last decade, due in large part to obesity, according to findings by UnumProvident researchers. Analysts found a 4,000 percent increase in syndromes that are primarily symptom-based, such as fibromyalgia and chronic fatigue syndrome. The study also revealed substantial increases in hypertension and diabetes (100 percent), musculoskeletal disorders (78 percent), cancer (63 percent), back disorders (46 percent) and cardiovascular disease (17 percent). The National Business Group on Health attributes to obesity some 39 million lost work days, 239 million restricted activity days and 63 million physician visits.

 Workplace legal training programs do more than help companies avoid costly litigation. While there is ample evidence that legal training enables companies to avert costly lawsuits, the greatest financial benefit lies elsewhere, according to *The Business Review*.

By teaching techniques for avoiding workplace harassment and discrimination, training programs create a more harmonious workplace, resulting in lower employee turnover and higher productivity. For most companies, low productivity and high absenteeism represent a far greater expense than legal exposure. Replacing competent workers typically costs two or three times their annual salary.

Cash balance plans became popular with employers in the 1980s and 1990s as traditional defined benefit plans became more costly to administer and fund. Cash balance plans currently account for about 25 percent of all participants in defined benefit plans and 40 percent of all assets invested in defined benefit plans, according to the Federal Reserve Board. Lately, however, cash balance plans have received some negative press. What exactly is a cash balance plan and what do you need to know if you want to implement one?



### What are cash balance plans?

Cash balance plans are defined benefit plans that derive their name from the way they define the benefit amount available at retirement. Other, more traditional, defined benefit plans use a complex formula based on pay and longevity to determine retirement benefits. But a cash balance plan defines the retirement benefit simply as the balance in that employee's retirement account.

Cash balance plans also share characteristics with defined contribution plans, such as 401(k)s. In a cash balance plan, the participant earns compensation credits, based on a percentage of pay, and interest credits. Compensation credits end when a participant's employment ends; interest credits continue until the participant takes retirement benefits.

Cash balance plans differ from 401(k)s in that the employer makes all contributions, which accrue in a hypothetical account for each plan participant. And although the employer can earn interest on cash balance plan funds while they accrue, any investment gains or losses do not affect the retirement benefit available. The employer assumes all investment risk.

### Employer benefits

Companies can realize substantial cost savings with cash balance plans, since benefits are based on average career earnings, while benefits under a traditional plan are based on the average of the employees' highest salary over three or five years. The cash balance design allows employers to shrink long-term pension debt while still providing benefits. Since the plan sponsor makes



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# Managing Prescription Drug Costs

If you want to address the most rapidly growing portion of the increase in health care costs, take a closer look at your company's prescription drug benefit. Prescription drugs currently account for more than 15 percent of all corporate health care spending. And costs related to drug benefits are expected to continue to rise at a staggering pace. By understanding what's behind these cost hikes, employers can take steps to reduce expenditures while keeping employees satisfied with their benefits.

The Kaiser Family Foundation identified three main factors driving the increases in prescription drug spending: manufacturers' price increases, changes in the types of drugs used, and higher drug utilization generally. Each factor requires a different employer response, and may include moving beyond cost-shifting to employees, which employers have often considered the path of least resistance.

**1 Pricing.** Manufacturers' rising prices account for nearly one-quarter of recent health care cost hikes. The easiest way for companies to mitigate rising prescription costs is to require employees to absorb more of the expense. Increases in employee premiums and hikes in deductible amounts and copayments are proven employer-to-employee cost-shifting techniques.

The tiering of copayments – based on whether the drug is generic, branded and/or part of the plan formulary – is a relatively new cost containment technique that's beginning to yield cost savings. But even these differences in copayments do not reflect the vast difference in the underlying costs of these drugs. So some companies are moving from copayments to coinsurance, which requires the patient to pay a percentage of the total charge. For smaller employers who may not share in manufacturers' rebates, coinsurance offers a viable savings solution.

**2 New generations of drugs.** Newer and more expensive drugs are supplanting older, cheaper drugs as a first line of care. These drugs account for around 28 percent of the increase in the cost of prescription drug benefits. Dealing with this issue requires benefit designs that encourage employees to use older and less costly drugs if they are the therapeutic equivalents of newer ones. Plans should also allow newer drugs to be used only when older drugs are shown to be ineffective.

**3 Utilization.** The number of prescriptions filled has been growing 6 percent a year over the last decade, and will continue to rise as the population ages and more medications emerge to treat chronic conditions. This trend is linked to about 48 percent of the overall increase in prescription drug benefit costs.



Companies can tackle the utilization issue by implementing more comprehensive disease management protocols to help workers find the simplest, least costly treatments that are effective. Increasingly, employers are adding disease management and wellness programs to their benefits packages to help stem the costs of more expensive hospitalizations and procedures.

## Beyond cost shifting

Traditionally, smaller companies have worked with insurance brokers and health insurance companies that offer comprehensive plans with prescription drug benefits. But even smaller companies may benefit from a “carve out” that separates the prescription benefits out of a health package and turning to a prescription benefit manager (PBM) to manage drug benefits.

Proponents claim that PBMs give employers access to more affordable drugs through deeply discounted retail and mail-order delivery channels. PBMs also contract with manufacturers to obtain rebates that can be passed on to clients. While the marketplace is dominated by a handful of large players that account for 80 percent of the market, a number of PBMs specialize in working with smaller companies. Groups of small companies working together can obtain even better rebates and discounts on both branded and generic drugs.

While PBM pricing is often more transparent than insurance company pricing, a PBM's financial interests may not always align with those of their clients. Some PBMs retain the difference between the discount applied to the client's invoice and the actual amount reimbursed to the retail pharmacy. With mail-order purchases, certain PBMs rely on their market power to generate revenue by purchasing volume-based brand and generic drugs at a deeper discount than the prices clients pay. Clearly, vendor management can help keep a lid on costs.

Whether your company is large or small, now is a good time evaluate current provider relationships and explore options for managing those relationships. Companies can significantly reduce prescription drug benefit costs by negotiating terms and monitoring performance of PBMs or insurance companies. Finally, keep communicating with your employees about the cost issues and their health care plan options.

For more information on prescription drug benefits, please call us. □

# Disease Management

## Promoting Wellness and Saving Money

Even as medical benefits shrink, disease management programs are expanding as part of, or in addition to, traditional health plans. The reason is simple: employers view disease management as an effective way to control soaring costs. Just five years ago, a relatively small percentage of employers were implementing the programs; today most companies see disease management as a competitive issue, if not a necessity.

Approaches to disease management vary, with companies using mailings, the Internet, home monitoring equipment and direct phone calls to reach clients. Typically, a nurse works with the patient to help promote positive lifestyle changes and ensure compliance. The nurse also coordinates with the primary physician and other providers to ensure that established guidelines for specific diseases are being followed. Patients also can call the nurses if they have questions about their plan of care, although the nurses don't diagnose conditions.

If you are considering including disease management in your company's benefits package, here are some guidelines to consider:

**Early intervention.** Studies reveal that only a small fraction of patients with major chronic conditions are responsible for the majority of health care costs. Proponents of disease management programs maintain that the demands of the sick person can be mitigated by optimizing care early on in the illness. It is relatively inexpensive to attend to the mundane needs of a diabetic who regularly monitors the disease, but expenses of an uncontrolled condition can skyrocket with complications, such as blindness, kidney transplants and heart attacks.

Through early patient identification, education, nursing support and care coordination, disease management reduces the number of inpatient admissions and emergency-room visits. It helps avoid or minimize complications and improves the employee-patient's quality of life.

**More diseases, more people.** Until recently, most disease management programs covered just a few major chronic conditions—usually heart disease, asthma and diabetes. Now many programs cover a dozen or more ailments, including depression and other mental illnesses.

What all these diseases have in common is that they require lifelong management and account for about half of all health care costs, according to American Healthways, the nation's largest disease management provider. By keeping these patients as healthy as possible, disease management creates a win-win situation, since as health improves, savings improve.

**Costs.** A recent Hewitt survey found that almost two-thirds of employers say that disease management has helped control their health-care expenditures, with an approximate 2-to-1 or higher return on invest-

ment. Cost depends on which conditions are covered, how the program is structured, and whether fees are based on the total number of employees or the number of enrolled participants. Average annual costs range from \$5 to \$12 per employee/per condition, according to Watson Wyatt consulting.

Employers are identifying the most prevalent and high-cost conditions and choosing the specific disease management program that best fits their workforce profile. By examining their health insurance and pharmaceutical claims and evaluating their employee population, employers can custom-design packages that not only cover more ailments, but also serve employees who aren't sick but may be at risk. This results in a more broadly cast net, with programs morphing from disease management to "population health."

**Resistance.** Some doctors and consumer groups criticize disease management, because they say it can undermine the doctor-patient relationship or make it harder for people to get coverage for chronic diseases. Because disease management companies often work for insurance companies and not doctors, some doctors believe guidance given by disease management nurses may conflict with the doctor's advice.

Disease management nurses follow professional standards of care, but sometimes a doctor might need to deviate from guidelines based on the individual patient's needs and circumstances. The conflicting advice confuses patients, who end up calling their doctors, asking them to explain the difference.

Despite such concerns, proponents say that within the next three to four years, companies likely will begin using predictive computer models to analyze a person's risk factors for disease and set up programs



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contributions that are evenly spread out over an employee's time with the company, employers often enjoy greater cash flow predictability and funding options.

## Employee benefits

For younger workers and those who tend to job-hop, the steady accruals under a cash balance plan might provide higher benefits than a traditional plan, which rewards longevity. Cash balance plans are also simple for new employees to understand—their retirement benefit equals the account balance—whereas figuring benefits under a traditional pension requires complex calculations.

Cash balance plans also offer participants more flexibility than traditional defined benefit plans. For example, a participant with an account balance of \$100,000 at retirement could roll that amount into an annuity, which would pay a certain amount every year for life. Alternatively, some plans allow participants to receive the retirement benefit as a lump sum, as long as the spouse consents. Some plans also permit vested participants to take a lump sum payment if they terminate employment before reaching retirement age. Traditional defined benefit pension plans seldom offer this feature.

## Beware conversions

An employer might have no problems implementing a new cash balance plan, but a “conversion” could cause problems. Since 1995, one-fifth of large companies have converted their traditional defined-benefit pension plans into cash balance plans. This has caused concerns among those nearing retirement and their advocates. When a conversion occurs, all benefits accrued under the traditional plan are protected and cannot be reduced. For some employees close to retirement, however, the cash balance conversion may upset future earnings expectations. This change in expectations has led to accusations of age discrimination against employers who have converted their pension plans.

## The IBM ruling

In 2003, a federal court in Illinois found that IBM's cash balance plan – and by implication all such plans – discriminated against older workers, because the same credit would buy a much bigger retirement annuity for a younger employee than for an older one. The ruling alarmed other corporations and administrators who fear exposure to similar lawsuits.

At the end of September, IBM agreed to a \$320 million settlement to compensate current and former employees for lost pension benefits.

But the settlement leaves unresolved claims that IBM intends to appeal, including the fundamental age discrimination claim. Under the settlement, IBM's liability in the case will be capped at an additional \$1.4 billion if the ruling is upheld on appeal. Experts contend that an appeals court ruling against IBM would jeopardize over a thousand pension plans. Some pension observers believe that Congress needs to resolve the controversy in a way that protects older workers and clarifies the legal status of cash balance plans.

The House passed a bill in late September that, if enacted, would prohibit the U.S. Treasury Department from trying to use regulations to overturn the IBM ruling. The measure followed a series of proposed Treasury rules that affirmed the basic design of cash balance plans as non-discriminatory. But under a five-year “hold harmless” period, companies could convert to a cash balance plan and be shielded from age-discrimination claims if the cash balance plan guarantees that current workers start out with at least the present value of the traditional plan. Any future earnings would be based on the new plan.

Opponents of the House measure warn that the bill would undermine pension schemes generally by discouraging businesses from sponsoring additional defined benefits plans. While the Senate has been working on developing a consensus between employers and participant groups, no tangible results have emerged.

So for now, most employers are putting plans to convert traditional pensions to cash balance plans on hold. Instead, companies and pension observers are looking to the next Congress for clarification on the legality of conversions and efforts to craft new rules for them. Stay tuned. □

## DISEASE – continued from Page 3

in which nurses and dietitians encourage people to avoid those risks and stay healthy.

**Disease management vendors.** As employers seek more comprehensive health care packages tailored to their specific workforce needs, many are contracting directly with disease management vendors rather than working through their medical plan or pharmacy benefit administrator.

To provide comprehensive offerings in both sickness and health, vendors may partner or subcontract with other specialty providers. Such partnerships are organized around a single “care concierge,” who serves as a focal point. This allows a partnership of vendors to serve participants, but the employee and employer deal with only one company. Such vendors are attempting to become one-stop shops not only for monitoring diseases but also for health and utilization management.

This focus on health — not just on disease — helps companies seeking a coordinated approach that integrates lifestyle and wellness as well as sickness prevention. In this context, disease management programs are a good investment, not only from a financial standpoint, but also for employee health, productivity and performance. And that's great news for the bottom line. For more information on incorporating disease management into your group health benefit plan, please call us. □



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