

SPECIAL REPORT

July 2016



Benfield

ARTHUR J. GALLAGHER & CO.

Employer Market

HEALTHCARE
REFORM
& PRIVATE
EXCHANGES

Benfield | Arthur J. Gallagher & Co., St. Louis, MO 63119
© Benfield, a division of Gallagher Benefit Services, Inc.
All rights reserved. Published 2016
Printed in the United States of America

This Report is licensed only to the original party licensed by Benfield, a division of Gallagher Benefit Services, Inc. (respectively the "Licensee" and "Benfield-Gallagher") and is subject to a binding license agreement between Licensee and Benfield-Gallagher. Benfield-Gallagher continues to retain title to and ownership of this Report. All copies and portions of this Report, in any form, belong to Benfield-Gallagher, which retains all rights not expressly granted. Licensee is entitled to use this Report solely for its own internal business purposes and is prohibited from modifying, translating, or otherwise creating derivative works based on this Report. Licensee is further prohibited from licensing, selling, leasing, distributing, lending or otherwise transferring this Report to any third party. Licensee may not make any copies of Benfield-Gallagher Reports except for internal distribution purposes as described and agreed to in the license agreement provided that all such copies are reproduced with and incorporate all of Benfield-Gallagher's protective notices, including this and all copyright notices. Nothing in this Report and/or license agreement applicable thereto constitute a waiver of Benfield-Gallagher's rights under United States Copyright law or any other law.

This information has been obtained from sources which Benfield-Gallagher believes to be reliable but we do not guarantee the accuracy or completeness of this information.

SPECIAL REPORT

July 2016



Benfield

ARTHUR J. GALLAGHER & CO.

Employer Market

HEALTHCARE
REFORM
& PRIVATE
EXCHANGES

TABLE OF CONTENTS

EXECUTIVE SUMMARY	8
INTRODUCTION	15
WHY EMPLOYERS	17
HEALTHCARE REFORM OVERVIEW.....	20
EMPLOYER HEALTH BENEFIT COVERAGE STRATEGY.....	28
Active Employee Healthcare Benefit Actions	30
TOP EMPLOYER BENEFIT MANAGEMENT APPROACHES.....	38
Consumer-Directed Health Plans	38
Consumer-Directed Account Offerings (HRA & HSA).....	41
Impact of ACA on Cost and Cost Sharing	45
Cadillac Tax	48
HEALTHCARE REFORM IMPACT ON RETIREE COVERAGE	57
Employers Offering Retiree Benefits	57
Timeline of Retiree Provisions.....	58
Retiree Healthcare Benefit Trend	62
Retiree Health Coverage Decision Making	63
Pre-65 Retiree Healthcare Benefit Actions	64
Post-65 Retiree Healthcare Benefit Actions	70
RDS vs. EGWP	76
PRIVATE HEALTH INSURANCE EXCHANGES	79
PRIVATE EXCHANGE INTRODUCTION.....	80
I. PRIVATE EXCHANGE LANDSCAPE.....	81
Employer Adoption Projections by Year	81
Private Exchange Enrollment Estimates and Projections	84
Outcomes	87
Differentiation among Private Exchange Operators	93
Known Employers Enrolled in a Private Exchange	96
II. EMPLOYER PERSPECTIVES ON PRIVATE EXCHANGES FOR ACTIVE EMPLOYEES	98
Employer Evaluation of Private Exchanges	98
III. EMPLOYER PERSPECTIVES ON PRIVATE EXCHANGES FOR PRE-65 AND POST-65 RETIREES.....	108
Pre-65 Retirees and Private Exchanges.....	109
Post-65 Retirees and Private Exchanges	110
GLOSSARY	116
APPENDIX.....	119

LIST OF FIGURES

Figure 1	Employer Implementation Timeline	20
Figure 2	Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2016	31
Figure 3	Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2017 <i>(planning or seriously considering)</i>	32
Figure 4	Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2018 <i>(planning or seriously considering)</i>	33
Figure 5	Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2019 <i>(planning or seriously considering)</i>	34
Figure 6	Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2020 <i>(planning or seriously considering)</i>	35
Figure 7	Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2016–2020	36
Figure 8	Non-Jumbo Employer Healthcare Benefit Approach for Active Employees and Dependents: 2016–2020	37
Figure 9	Employers Offering Consumer-Directed Health Plans: 2011–2020	39
Figure 10	Estimated Lives Covered by a CDHP in 2016–2020 <i>(in millions)</i>	40
Figure 11	Preventive Drug Coverage in CDHPs with HSAs	42
Figure 12	Pharmacy Benefit Coverage in CDHPs with HRAs	44
Figure 13	Perspectives on Employee Health Benefits Cost Sharing Strategy	47
Figure 14	Employers With Benefit Offerings That Will Trigger the Cadillac Tax	51
Figure 15	Organizational View of the Cadillac Tax	52
Figure 16	Four Employer Perspectives on the Cadillac Tax and Reactions to the 2-Year Delay	53
Figure 17	Employers' Approach to the Cadillac Excise Tax	54
Figure 18	Strategies for Minimizing or Avoiding the 2020 Cadillac Tax	55
Figure 19	Jumbo Employers (5,000+ Employees) Offering a Medical or Rx Benefit for Pre-65 and Post-65 Retirees	57
Figure 20	Employer Implementation Timeline: Retiree Provisions	58
Figure 21	Employers with 500+ Employees Offering Retiree Health Plans	62
Figure 22	Stakeholder Influence on Retiree Health Coverage Decisions	63
Figure 23	Pre-65 Retiree Healthcare Benefit Actions: 2016	64
Figure 24	Pre-65 Retiree Healthcare Benefit Actions: 2017	65
Figure 25	Pre-65 Retiree Healthcare Benefit Actions: 2018	66
Figure 26	Pre-65 Retiree Healthcare Benefit Actions: 2019	67
Figure 27	Pre-65 Retiree Healthcare Benefit Actions: 2020	68
Figure 28	Pre-65 Retiree Healthcare Benefit Actions: 2016–2020	69
Figure 29	Post-65 Retiree Healthcare Benefit Actions: 2016	70
Figure 30	Post-65 Retiree Healthcare Benefit Actions: 2017	71
Figure 31	Post-65 Retiree Healthcare Benefit Actions: 2018	72
Figure 32	Post-65 Retiree Healthcare Benefit Actions: 2019	73
Figure 33	Post-65 Retiree Healthcare Benefit Actions: 2020	74
Figure 34	Post-65 Retiree Healthcare Benefit Actions: 2016–2020	75
Figure 35	RDS and PDP-EGWP Enrollment by Year	77
Figure 36	Employers Utilizing or Seriously Considering Utilization of Private Exchanges for Active Employees	81

Figure 37 Jumbo Employers Seriously Considering a Private Exchange for Active Employees and Dependents by 2020: By Industry 83

Figure 38 Private Exchange Enrollment Estimates: 2014–2020 (*in millions*) 85

Figure 39 Private Exchange Enrollment Estimates: Non-Jumbo vs. Jumbo Employees (*in millions*) 86

Figure 40 Health Savings Account (HSA) Growth Projections: Exchange vs. Traditional Channels 89

Figure 41 Average Member Deductibles Before and After Private Exchange Implementation 90

Figure 42 HSA Participation Before and After Private Exchange (*Gallagher Marketplace*) 91

Figure 43 Tiers of Private Exchange Focus 93

Figure 44 Spectrum of Private Exchange Approaches 94

Figure 45 Known Employers Enrolled in Mercer and Other Exchanges 96

Figure 46 Known Employers Enrolled in Aon and Xerox (Buck) Exchange 97

Figure 47 Known Employers Enrolled in Towers Watson Exchange 97

Figure 48 Types of Private Exchanges Employers Have Evaluated for Active Employees and Dependents 98

Figure 49 Specific Private Exchanges Employers Have Evaluated for Active Employees and Dependents 99

Figure 50 Stakeholder Influence in Decision to Move or Not Move to a Private Exchange for Active Employees 100

Figure 51 Jumbo Employer Agreement that Private Exchanges Offer the Listed Benefit 101

Figure 52 Critical and Influential Factors in Employer’s Decision to Move Active Employees and Dependents to a Private Exchange 103

Figure 53 Top Reasons Jumbo Employers are NOT Currently Participating in a Private Exchange for Active Employees (*ranking top 3*) 105

Figure 54 Top Reasons Non-Jumbo Employers are NOT Currently Participating in a Private Exchange for Active Employees (*ranking top 3*) 107

Figure 55 Retiree Coverage: Employers Offering Retiree Health Plans 108

Figure 56 Employers Participating in or Planning or Seriously Considering Participation in Private Exchanges for Pre-65 Retirees 109

Figure 57 Employers Participating in or Planning or Seriously Considering Participation in Private Exchanges for Post-65 Retirees 111

Figure 58 Post-65 Retiree Enrollment by Private Exchange 112

Figure 59 Funding of Post-65 Retiree Benefits in a Private Exchange 112

Figure 60 Top Factors Influencing Organization’s Decision to Shift Post-65 Retirees Health Benefits to a Private Exchange (*percentage ranking 1st, 2nd or 3rd*) 113

Figure 61 Private Exchanges Employers Have Evaluated for Post-65 Retirees 114

Figure 62 Top Reasons Employers are NOT Currently Participating in a Private Exchange for Post-65 Retirees (*percentage ranking 1st, 2nd or 3rd*) 115

LIST OF TABLES

Table A	Description of Health Reimbursement Arrangements (HRAs) & Health Savings Accounts (HSAs)	41
Table B	Congressional Budget Estimates of Excise Tax Payments (<i>in billions of dollars</i>)	50
Table C	Collectively Bargained Health Plans vs. Employer-Based Plans	56
Table D	Retiree Drug Subsidy vs. Employer Group Waiver Plans	76
Table E	Example of Employer Cost Savings under RDS vs. EGWP in the Coverage Gap	78
Table F	Non-Jumbo Employers: Last Year vs. Current Private Exchange Adoption Projections (<i>percentage of employers seriously considering or planning to use private exchange for active lives</i>)	84
Table G	Jumbo Employers: Last Year vs. Current Private Exchange Adoption Projections (<i>percentage of employers seriously considering or planning to use private exchange for active lives</i>)	84
Table H	Recent Private Exchange Innovations	95
Table J	Medicare Market Overview	110

LIST OF APPENDIX FIGURES

Figure A1	Breakdown of Research Participants	121
Figure A2	Breakdown of Employer Size	121
Figure A3	Jumbo Employer Participant Panel	122
Figure A4	State Exchange Enrollment	123
Figure A5	State Decisions for Creating Health Insurance Exchanges	124
Figure A6	Jumbo Employer Research Participants	125

INTRODUCTION

The 6th annual Employer Healthcare Reform and Private Exchanges report details the impact of ACA on employer health and pharmacy benefit offerings, plans and priorities. It features a comprehensive private exchange overview, including employer interest and adoption for active employees and retirees.

Key Report Topics Include:

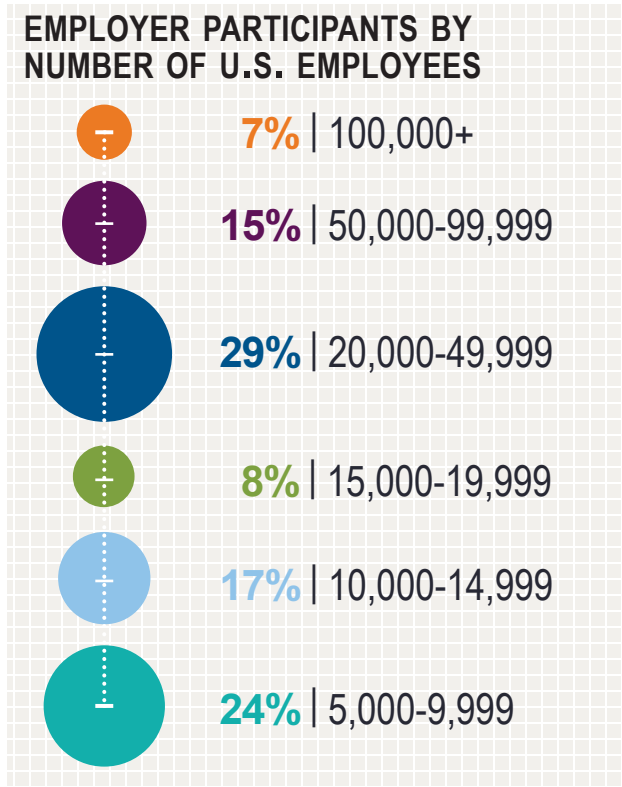
- Current and future plans for provision of active, pre-65 and post-65 retiree healthcare benefits for years 2016, 2017, 2018, 2019 and 2020
- Impact of ACA on Rx and medical benefit strategies, offerings, costs and cost sharing
- Preparations for and impact of the Cadillac excise tax
- Employer decision making factors related to evaluation and adoption of private exchanges
- Private exchange outcomes and participating employers
- Differentiation among major benefit consultant-run private exchange operators

Findings include results from a survey of 106 jumbo employers (5,000+ employees) and 52 non-jumbo employers (50-4,999 employees) fielded in February/March 2016. Respondents were key decision makers within their organization including VPs and Directors of Benefits and Corporate Medical Directors. Further qualitative insights were gathered via interviews with employers and private exchange operators.

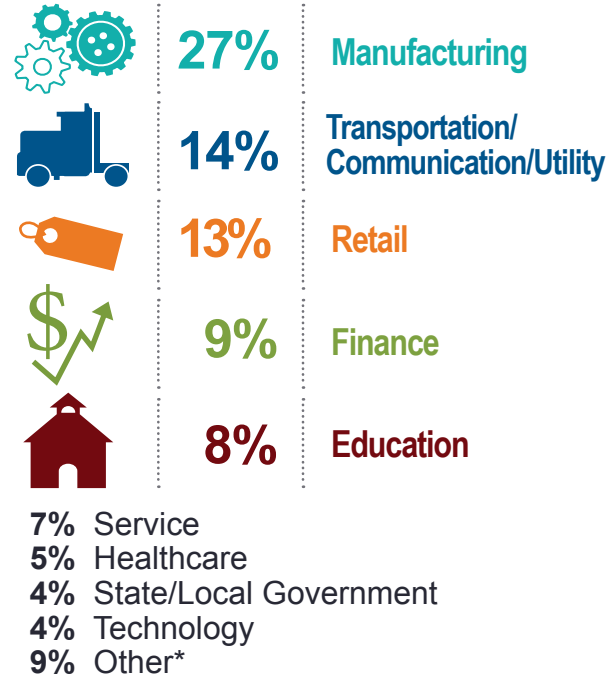
We encourage you to contact Sarah Daley, Research Director, at 314-968-0011 x 203 or sarah_daley@ajg.com with questions and comments as you review the report or to schedule a presentation of findings.

Jumbo Employer Participant Panel

106 SURVEYS | 11 INTERVIEWS | 3.7 MILLION COVERED U.S. LIVES



INDUSTRY

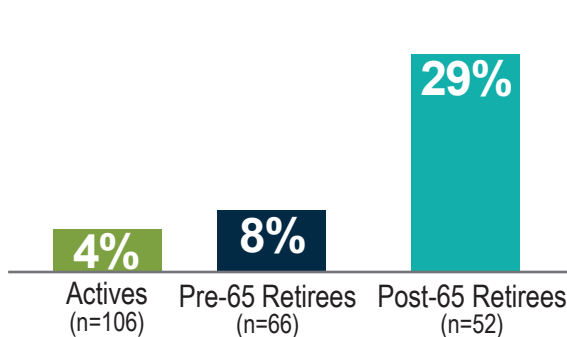


*Other includes: Agriculture, Energy, Fire/Security, Gaming/Hospitality, Media/Entertainment, Professional Services

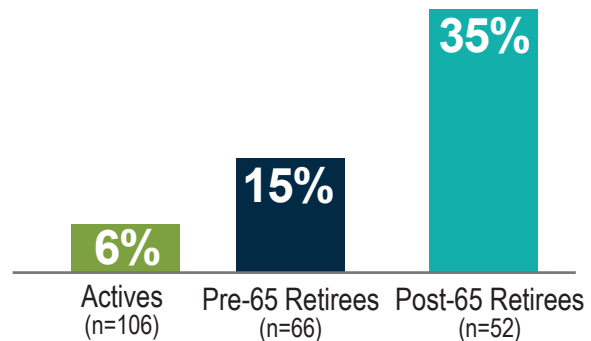
EMPLOYER RESPONDENT ORGANIZATIONAL POSITION



CURRENT PARTICIPATION IN A PRIVATE EXCHANGE



PROJECTED PARTICIPATION IN A PRIVATE EXCHANGE BY 2017



See Appendix for information on non-jumbo employer respondents.

Cadillac Tax

The so called “Cadillac tax” is a 40% excise tax that is applied to health insurance costs exceeding \$10,200 for single and \$27,500 for family coverage. The limits for pre-65 retirees are slightly higher—\$11,850 for single and \$30,950 for family coverage. Initially slated to take effect in 2018, the U.S. Congress passed a two-year postponement of the tax, now scheduled to be implemented in 2020. The threshold values will be updated prior to implementation and indexed for inflation in subsequent years.

The tax calculation includes:

- Annual insurance premiums paid by both the employer and employee
- Health savings account (HSA) and flexible spending account (FSA) contributions from the employer and pre-tax contributions from the employee
- Employer contributions to a health reimbursement arrangement (HRA)
- Cost of care received through employer on-site medical clinics providing more than de minimis care (benefit is too small to reasonably account for)
- Executive physicals



Pushing Back on HSA & FSA Cadillac Tax Rules

There is a movement underway, driven by a number of employer groups (including SHRM, American Bankers Association, ERIC and Business Roundtable) to exclude employee contributions to HSAs and FSAs from the Cadillac tax calculation. One reason cited is that employers have no control over employee contributions to these accounts, and employees can take them with them if they switch companies.

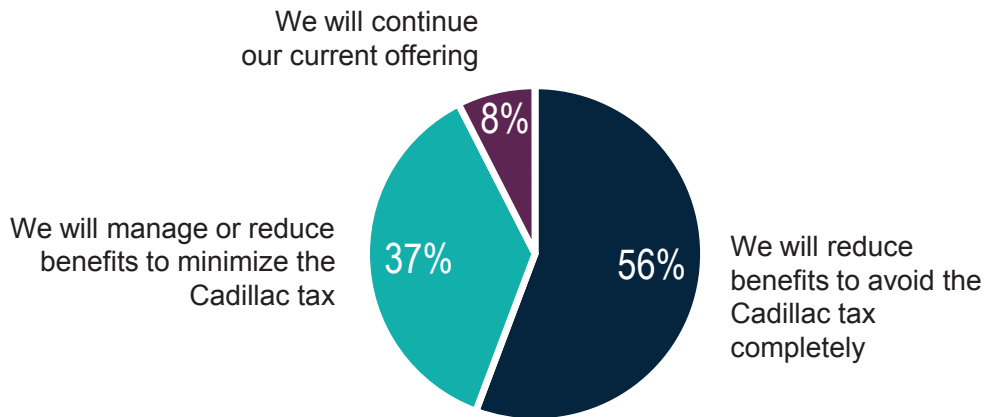
These groups fear that if employee contributions to HSAs and FSAs are counted toward the taxable value of plans, employers will stop offering and promoting them, leaving employees with high deductibles and no savings. The U.S. Treasury Department has pushed back, saying that this exclusion would require a statutory change to ACA, but employer groups have contended that the IRS can issue regulations without a change in the law.

In **March of 2016**, Representative Charles Boustany (R-LA) introduced the Health Savings Protection Act (H.R. 4832). By amending current tax code, this bill calls for the exemption of contributions to HSAs and FSAs when measuring value of employer-sponsored health benefits against the excise tax threshold. As of May 2016, there was bipartisan support offered by two cosponsors of the bill.

Employers' Approach to the Cadillac Tax

Employers were asked to describe their approach to the Cadillac excise tax (Figure 17). Similar to last year, the majority of employers will reduce their benefit offerings to avoid the Cadillac tax completely (56% this year, 60% last year). Thirty-seven percent of respondents (compared to 30% in 2015) will reduce benefits to minimize the amount of Cadillac tax for which their organization is responsible. Similar to last year, 8% of respondents (vs. 10% in 2015) indicated that their organization will continue their current offerings, and triggering the excise tax does not impact their decision making.

Figure 17: Employers' Approach to the Cadillac Excise Tax



n=106 Jumbo Employers
 Source: Benfield, a division of Gallagher Benefit Services, Inc. 2016 Healthcare Reform & Private Exchanges.

“If the Cadillac provision stays and it does kick in in 2020, it will significantly impact us because we have a very robust executive medical plan, and we have plan offerings right now that before adjusting for trend will bump right up against that trigger point. If that happens, that’s going to cause a major change. Although, if you’re looking at what’s going on politically it’s really an open question on whether that’s going to even survive.” – Benefits Manager, Employer

“Most employers are already looking for how we can cut back, and some of us did in ’16 because nothing was happening with appeal or delay at the time plan design decisions were made.” – VP of Global Benefits, Employer

I. PRIVATE EXCHANGE LANDSCAPE

This section begins with a look at private exchange market share and annual adoption projections. Then, we present findings specific to outcomes-to-date and differentiation among private exchange operators.

Employer Adoption Projections by Year

Figure 36 illustrates the percentage of employer respondents using or seriously considering a private exchange for active employees. Non-jumbo (50-4,999 employees) and jumbo (5,000+ employees) employers have different patterns in their plans for private exchange adoption.

Non-Jumbo: A modest but growing number of non-jumbo employers are using a private exchange in 2016 (8%, up from 6% in 2015 and 0% in 2014). Those planning or seriously considering a private exchange between 2017 and 2020 tops out at 15%. This is a decline in interest from last year's projections of 32% seriously considering a private exchange by 2018.

Jumbo: Just 4% of jumbo employers currently use a private exchange for actives. However, serious consideration jumps substantially between 2017 and 2020. Only 6% are considering a private exchange for 2017, but the number grows to 23% by 2020.

Arthur J. Gallagher's 2016 Benefits Strategy & Benchmarking Survey of employers found greatest current and projected private exchange uptake among small employers:

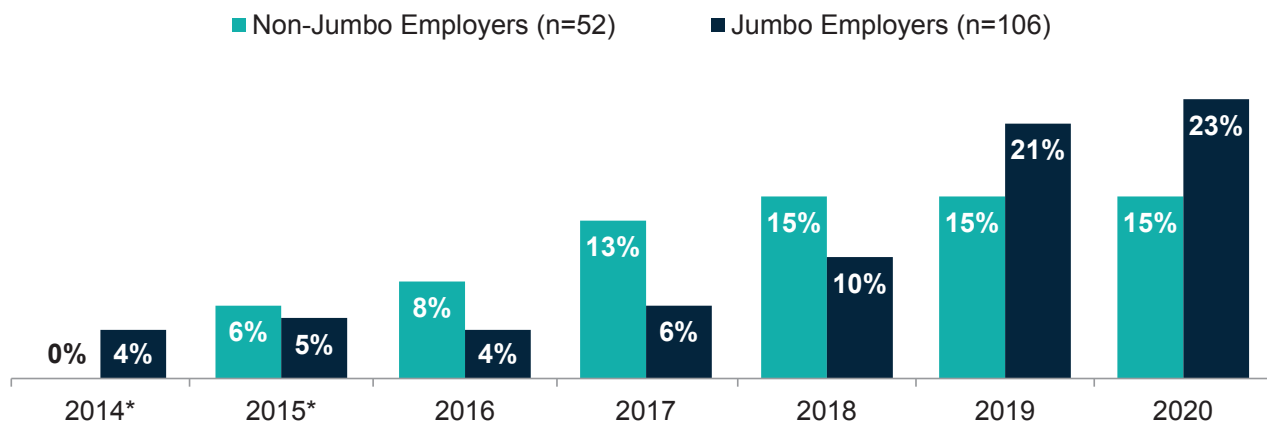
**Private Exchange Utilization:
Current & Planned (within 2 years)**

- Under 100 employees: 5% Current, +7% Planned
- 100-499 employees: 3% Current, +11% Planned
- 500-999 employees: 3% Current, +8% Planned
- 1,000+ employees: 1% Current, +6% Planned

OVERALL: 4% Current, +9% Planned

n=2324 Employers
Source: Arthur J. Gallagher & Co.

Figure 36: Employers Utilizing or Seriously Considering Utilization of Private Exchanges for Active Employees



2014-2016 percentages reflect actual enrollment
 *Non-Jumbo Employers: 2014 n=115; 2015 n=50; Jumbo Employers: 2014 & 2015 n=111
 Key: Non-Jumbo Employer=50-4,999 employees; Jumbo Employer=5,000+ employees
 Source: Benfield, a division of Gallagher Benefit Services, Inc. 2016 Healthcare Reform & Private Exchanges.