Here's to Your Health

Law firms can battle high medical insurance costs by pursuing options that increase claims savings and lower premiums and adjudication costs.

BY JIM EDHOLM

Law firms can face subtle "discrimination" related to overcharging for health insurance premiums. Given the importance of attracting and retaining good personnel, minimizing these costs can give a firm a key advantage in the hiring market.

Why are some organizations overcharged? Law firms may overpay because of:

- **Location**. Many major law firms are in metropolitan areas, which generally have higher premium costs than their clients' suburban locations.
- **Demographics**. White-collar professionals, particularly partners, tend to work beyond the Medicare age. Rates are based on the group's employees' average age, so law firms' rates may be older than those for other employers.
- **Claims experience**. Above a certain size, the group's own claim history drives its rates, but on average white-collar groups, especially attorneys, consume more health care than blue-collar groups. Therefore, carriers "rate up" the groups accordingly. This is offset somewhat by well-educated groups of people living healthier lives.
- **Psychographics**. This has nothing to do with "law-firms-because-they're-law-firms" and everything to do with "law-firms-because-of-whom-they-hire." To deliver quality service and representation, you must hire capable people. Individuals of this caliber expect and can get excellent benefits – If not from your firm, then from your competitors. Because of this, law firms tend to have very rich benefits, particularly health insurance, which in turn leads to unintentional, de facto discrimination in the form of higher premiums.

Jim Edholm , *President,* BUSINESS BENEFITS INSURANCE

Because health insurance for law firms is expensive – but still crucial to retaining top talent – you'll need to employ all the tools at your disposal to get the most bang for your buck. A Health Reimbursement Arrangement or Health Savings Account could be the key weapon in your arsenal.

Most of us are familiar with the Pareto Principle – the tendency for 20 percent of something to generate 80 percent of something else. The usual example is illustrated by positive outcomes: 20 percent of your firm's clients generate 80 percent of billings.

But the principle is also true for negative factors. The percentages may vary, but using the Pareto Principle we can stipulate that 80 percent of administrative costs are attributable to 20 percent of the *dollar value* of health insurance claims. That may sound counter-intuitive, but in fact it costs about as much to administer a small claim as it does a large one.

Take, for example, a doctor visit. Probable cost: about $100. One incident, one adjudication, one processing fee. Compare that to a colonoscopy: One incident, two adjudications (hospital and surgeon), two processing fees. The cost, however, is about $1,600.

If those were the only two claims, the smaller would account for about 6 percent of the medical costs ($100 out of $1,700), but 33 percent of the administrative costs (one fee out of three). This underscores two factors:

1. Common, frequent, simple procedures cost as much to adjudicate and process as do more costly *but also simple* procedures, and
2. As the complexity and cost of procedures increase geometrically, the cost to process the claims increases only arithmetically.

Therefore, the least expensive procedures – accounting for perhaps 20 percent of claims dollars – account for as much as 80 percent of administrative costs. A rich, first-dollar health plan has significantly higher administrative costs than do other, less generous plans.

'MONEY VELOCITY'

Then there's "money velocity." Carriers pay all claims incurred during a contract period, irrespective of when they're presented for payment. A larger claim takes 60 to 90 days from the date the claim is incurred until it's billed, adjudicated, and the check is processed and clears the bank. Even small claims (doctor visits, simple x-rays, etc) may take 30 to 45 days.

The carrier must pay bills when presented – even if your company has moved on to another carrier. Reserves are built up to cover that eventuality, and that's not easy in a low-deductible, first-dollar plan. Money moves out about as fast as it's moving in; there's a high "money velocity."

But with a larger, up-front deductible plan, the carrier can accumulate the reserve dollars while the employee pays for initial claims. The result is counter-intuitive: The high-deductible plan is often less expensive *by an amount that exceeds the seeming savings attributable to the deductible*.

Because of the claims savings, lower adjudication costs, and easier accumulation of reserves, the plan price can drop by more than would seem likely. And many carriers prefer higher-deductible plans and actively discourage the purchase of rich, front-end plans via artificially high pricing.

GOOD BENEFITS AT LOWER COST

Which brings us back to you: the legal professional who is trying to manage your firm's costs. Stuck between an employee base that expects rich benefits and a carrier that's prohibitively pricing such plans, what's your law firm to do?

Well, you can grit your teeth, raise your fees, and muddle through… or you can take advantage of the carriers' inducements and give your employees good benefits while improving your firm's bottom line.

Here's the basic concept: Share with your carrier the risk inherent in a higher- deductible plan, and use the premium savings to advance your agenda and reward your employees. There are two basic methods for the average-sized firm (fewer than 100 to 150 employees): the Health Reimbursement Arrangement (HRA) and the Health Savings Account (HSA).

Let's examine how each works, but keep in mind that health insurance is a very fragmented business, and plan selections may differ throughout the United States. Still, the concept is similar everywhere. Find a capable broker or benefits consultant who can generate illustrative examples for your area.

UNDERSTANDING HRAS

An HRA is generally much like other plans, but with a significant deductible for some services. If most plans in your area have doctor co-pays, so will your HRA. The same applies to prescription drug cards.

The difference is in expensive but infrequent items such as hospital stays, surgery (inpatient or outpatient), and diagnostic procedures such as MRIs, CAT scans or PET scans. Those more expensive items are subject to a deductible, so the employee pays that cost before the carrier participates. Because the carrier both delays payment and pays a lower fraction of the procedure's cost, premiums for such a plan are lower. You decide whether you want to pass the premium savings to the employees (lower premiums in exchange for higher risk) or keep the savings and reimburse the employee some or all of his or her deductible.

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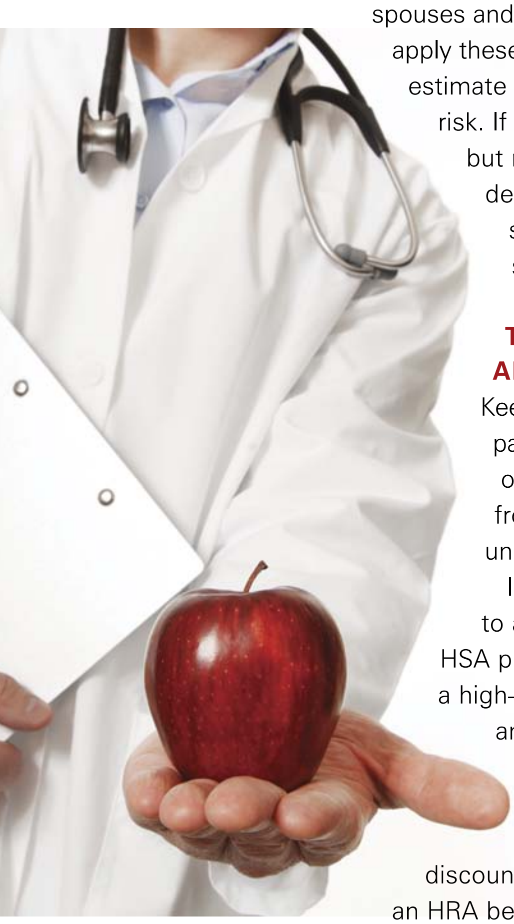
To help you make that decision, here's what one carrier found. On average, during a plan year:

- 22 percent of insureds will have an emergency room visit,
- One in 16 will be admitted to the hospital,
- One in eight will have an outpatient surgery,
- One in six will have an MRI, and
- One in five will have a CAT scan.

By tallying your employee count (including spouses and children), you can apply these percentages to estimate your reimbursement risk. If you keep the savings but reimburse the deductibles, the firm's savings may be significant.



THE HSA ALTERNATIVE

Keep in mind, however, that partners and LLC owners are prohibited from being reimbursed under an HRA.

Instead, you may want to adopt an HSA. A true HSA plan has two parts: a high-deductible health plan and a Health Savings Account from which claims can be paid. First, the premium discount is greater than under an HRA because nothing (except preventive expenses) can be paid by the carrier until the insured hits his or her deductible. The carrier pays less and, therefore, charges a lower premium.

Secondly, deposits made into the HSA savings portion are triply tax-blessed. They are deductible when the deposit is made (by either the employer or the employee), they accumulate and earn without taxes, and the withdrawals – if made to cover legitimate medical expenses – are income tax free when withdrawn.

In addition, *any taxpayer*, including partners and LLC owners (although it's a bit more arduous for them), is eligible to deposit money in the HSA. The savings can be substantial. In a recent Massachusetts plan, a 30-plus employee law firm achieved the following:

- Fully funded the HSA (i.e., deposited cash equal to the full amount of the deductible throughout the year),
- Paid for the entire premium portion of the plan, and
- Saved – after the full cost of the HSA deposit and the full cost of the premium –17.8 percent of the current premium, *without changing either the carrier or the employee contribution*.

This firm's benefits were particularly rich, so its savings were more dramatic than most. However, another firm with a more plebian plan (higher co-pays for doctor, surgery and hospital) was able to improve the benefits via full-funding of the HSA, while still saving the partnership 4.4 percent and improving the partners' tax picture. So, even less-than-stratospheric benefit plans can still bank savings.

BENEFITS TO EMPLOYEES

How likely is an employee to benefit from a fully-funded HSA? Pretty likely. One Massachusetts carrier found that 61 percent of singles would spend less than half of the typical HSA deductible. So, 61 percent of the single employees would have half or more of their deposits remaining at the end of the plan year.

The carrier also found that 40 percent of families would spend less than half of the family deductible, so they, too, would profit from the fully funded HSA. It's important to remember that even if nothing is left in the HSA account, the employee is no worse off than currently. After all, how much do employees get back from the carrier now when their claims are low?

Law firms should also seriously consider fully funding the deposit. An HSA is a new, unfamiliar vehicle, and employees are reluctant to embrace change, especially when lacking an incentive. It always helps if the HSA lily is gilded with a full-funding program in the first year.

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LEARNMORE

Want to learn more about health insurance for law firms? The *ALA Guide to Salary and Benefits Administration*, available in the *ALA Management Encyclopedia*, discusses related issues in-depth. When the costs associated with hiring staff are combined with an increasingly challenging economy and job market, it becomes clear that many of the old rules of compensation and benefits administration no longer apply. Learn much more in this article, available at *www.alaenyclopedia.org* via individual article purchase or subscription to the complete *Encyclopedia*.

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Jim Edholm is President of Business Benefits Insurance, an employee benefits planning firm in Andover, Massachusetts. Request his complimentary, no-obligation report – *How Attorneys Can Lower Healthcare Costs, Maintain Benefits and Put Cash in Employees' and Partners' Hands* – by e-mailing *JimEd@bbibenefits.com*.