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Employer Adoption of Private Exchanges Lower than Projected

In 2014, the *Patient Protection and Affordable Care Act* (ACA) established a *public exchange* for government-sponsored health insurance,[1] significantly altering the landscape of the health insurance market. In addition to this paradigm shift in government-sponsored healthcare insurance, private insurance providers are moving toward this exchange system, which provides a choice among many different health insurance plans. *Private exchanges* are similar to *public exchanges* in that they purport to offer low-cost plans to beneficiaries; however, *private exchanges* differ from *public exchanges* in that the insurance is offered by the employer to the employee.[2] Qualities that are common across private exchanges include: (1) employee choice; (2) employer subsidies; (3) ancillary products (e.g., dental and vision); (4) online enrollment; and, (5) administrative benefits.[3] Approximately 8 million people are currently enrolled in a private exchange, which represents a growth of 35 percent from 2015.[4] Although the prevalence of private exchanges is increasing, adoption rates for private exchanges have decelerated since 2013.[5] This *Health Capital Topics* article will discuss the benefits and consequences of utilizing a private exchange and the state of private exchange adoption nationwide.

The development of private exchanges stems from the unsustainable design and delivery models of traditional employer-based health insurance plans with defined benefits.[6] For instance, traditional plans will become more expensive as healthcare costs rise from a projected *national healthcare expenditures* (NHE) growth of 4.9 percent in 2016[7] to an average of 5.9 percent annual growth in the period from 2016 to 2024.[8] Second, given the expanding ubiquity of digital technology, employees expect the abundance of choices and digital accessibility to which they have become accustomed in everyday life – characteristics that are not common in traditional health insurance plans.[9] Third, regulations continue to impose an administrative and financial burden on employers.[10]

Private exchanges are a potential remedy to this burden placed upon employers operating traditional healthcare insurance plans. For instance, private exchanges may reduce costs by enhancing the bargaining power that companies have over insurers. According to Towers Watson, one of the largest private exchange operators by total number of covered individuals,[11] companies participating in their exchange have managed to decelerate the overall growth in healthcare costs because the exchange enhances a company's leverage to negotiate with insurers.[12] Another benefit of private exchanges is increased employee choice;[13] given the option of various monthly costs and deductibles, employees may be willing to make individual tradeoffs between cost and provider access.[14] Consequently, private exchanges may increase *adverse selection* because an individual who anticipates incurring high healthcare expenses may decide to purchase a plan with a high premium and a low deductible through the private exchange. Inversely, if an individual does not anticipate incurring healthcare expenses, he or she might opt for a plan with a low premium and a high deductible.[15] In addition, private exchanges may remove some of the employer burden of operating employee health insurance plans by outsourcing many administrative tasks (e.g., decision-support tools and customer service) to the exchange providers.[16] Finally, by increasing competition within the market through a variety of health insurance plans, private exchanges could potentially improve cost predictability and transparency.[17]

Given the possible benefits of private exchanges, industry analysts initially forecasted significant growth in the utilization of private exchanges;[18] however, growth has been slower than expected.[19] As mentioned earlier, although the number of people enrolled in a health insurance plan through a private exchange increased 35 percent from 2015,[20] the annual growth rate of private exchange adoption has slowed significantly since 2013.[21] For example, approximately 35 percent of employers in 2014 evaluated private exchanges as a source for offering employee health insurance, but only 6.7 percent of employers reported engaging in the same process during 2016.[22] Further, most of the growth in private exchanges is driven by midsize companies,[23] while adoption rates among employers with greater than 2,500 employees remains lethargic.[24] The low rate of healthcare inflation may contribute to slower adoption among large companies[25] because size affords these businesses leverage over health insurers to sustain benefit levels in the face of modest cost increases.[26] In contrast, small to mid-sized companies do not possess the leverage to avoid healthcare cost increases, creating incentive to utilize a private exchange to reduce costs.

Lack of information regarding the effectiveness and implementation process of private exchanges may also be contributing to the slowing adoption rates. First, the

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impact of private exchanges on the total cost of healthcare remains unclear.[27] Private exchange operators can obfuscate healthcare cost and quality data, thereby complicating the evaluation process for employers seeking to adopt a private exchange.[28] Second, transitioning to a private exchange may require substantial employer resources that discourage adoption, such as the administrative burden of preparing for the transition – a process that could take up to 12 months.[29] Third, since private exchanges are relatively new and untested, employers are concerned about a potential loss of plan support and fewer benefits offered to their employees should they abandon traditional health insurance plans.[30] Lastly, the substantial overlap of health insurance providers within private exchange platforms could reduce overall competition in the market and potentially limit the cost savings that render private exchanges as an attractive option.[31]

Despite an initial optimistic forecast for the future of private exchanges, adoption rates have decelerated in recent years. Although private exchanges have the potential to offer benefits, such as increased competition and lower health insurance costs, the ability of private exchanges to actualize these benefits remains unclear. Therefore, a lack of information regarding the effectiveness of private exchanges may deter employers from offering insurance through a private exchange platform. Moving forward, attention should be paid to the impact of private exchanges on healthcare costs as the market continues to evolve.

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