COVID-19's Expected Impact on Healthcare Costs

Changes ahead for employers in 2021 & beyond

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KEY CONSIDERATIONS FOR HEALTHCARE COSTS IN 2021

2020 healthcare costs cannot be used as a baseline due to COVID-19 and changes in member behavior without well-considered adjustments.

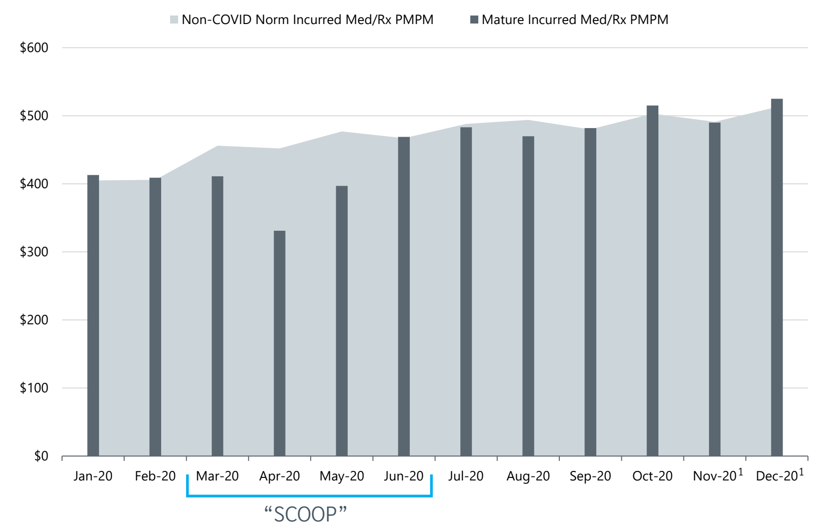
The impact of new COVID-19-related costs on budget projections for 2021 and beyond need to be carefully evaluated.

COVID-19 has inserted new complexities into employer healthcare plan budgeting and cost projections. Based on data analytics from Infolock®, Lockton's propriety data platform, we are seeing new trends for potential increases and decreases that can help employers prepare for what comes next.

Prior to the pandemic, analysis of Infolock data indicated that many employers faced annual cost increases of about 5%. As we entered 2020, many employers had generally based their planning on this 5% or so cost increase over their 2019, pre-COVID-19 costs.

But in early 2020, the world changed. As we shifted to the COVID-19 time period, a new pattern emerged when the world locked down, and claims costs and trend went down with it. We saw a "pandemic scoop" — or a gap between what actually happened and what would have normally happened — that is largely attributable to care avoidance.

2020 ACTUAL INCURRED COMPARED TO NON-COVID NORMATIVE MED/RX PMPM



[1] Estimates

Across Lockton's client base, on average, 2020 came in lower than what prior experience would have suggested, and many clients will see their annual incurred claims finish nearly 5% lower than what they planned for in their 2020 budgets. We define expected as "what if COVID-19 never happened" or the "non-COVID-19 normative" baseline.

As we look at the pandemic's impact to claims, these are relative to a certain baseline. Usually, this baseline is the prior year, but since 2020 was so unusual, for our projections, we have assumed pre-COVID-19 claims kept trending at around the 5% level each year. We also have COVID projection models that use developing Infolock data to inform our assumptions.

As a reminder, the estimates that follow are high level and normative — an employer may have different results due to industry, age mix, geography and other factors.

Likely cost increases

COVID-19 testing, treatments & vaccines

In 2020, we saw the joint impact of growing testing capacity in the U.S. coupled with infection waves. The allowed charge per COVID-19 diagnostic test settled near $100 per test, and our data indicated most tests that went through a plan were performed in an office setting or lab.

In 2021, we expect **COVID-19 diagnostic testing** to continue to add upward pressure to plans. Our current projection estimates assume about a 1.0%-1.5% impact to a typical plan this year and continuation into 2022 depends largely on the path of the virus and vaccination efforts.

The costs for **treating COVID-19** run the spectrum from mild to severe. Based on 2020 data for our client population, over 95% of members with a COVID-19 diagnosis who interacted with the medical system had outpatient treatment. Less than 5% had an inpatient stay with a five-day average stay, and less than 1% went on to the ICU with a more costly 20-day average stay.

Our projection estimates for COVID-19 treatment costs indicate about a 0.5%-1.0% impact to a typical plan in 2021, with most of that driven by inpatient and ICU stays. The continuation of this impact into 2022 depends on the virus and vaccination efforts, which if successful, will mitigate the incidence and severity/cost of COVID-19 infections.

The costs for **COVID-19 vaccines** will continue to unfold in 2021. Key drivers are the cost of the vaccine and how many members ultimately receive the vaccine. The federal government is expected to cover most of the ingredient costs of the vaccine in 2021, so plan costs should be $0. Administration costs may vary based on whether the shot requires one or two doses, the Center for Medicare & Medicaid Services benchmark administrative cost (which is evolving) and whether an administrative charge was assessed. For example, if the vaccine was administered through a city or county vaccine event, this cost may not run through a plan.

After making assumptions about the number of members who receive the vaccine in 2021, as well as the administrative costs, our current projection estimates indicate about a 0.5%-1.0% impact to a typical plan. The continuation of this impact into 2022 depends on unknowns such as the degree of ongoing ingredient cost subsidy and the ongoing need for regular COVID-19 booster shots, like annual flu shots.

Impact of extended COBRA and/or COBRA subsidization

The government's COVID-19-related actions may indirectly apply upward pressure to some self-funded employer plans. The March 2021 American Rescue Plan Act (ARPA) included a provision for fully subsidized COBRA coverage for certain employees subject to involuntary termination. COBRA claimants have a reputation for costing more than a typical active member, and we see in our data that a typical COBRA member costs over twice as much as an active member, as unhealthy members are more motivated to pay the associated costly COBRA premiums. "Free" COBRA coverage will incentivize more people to elect COBRA and may create additional cost pressures for employers.

Some good news is that our sensitivity modeling indicates that, on average[2], most employers should expect only a modest impact of 0.0%-0.5%, with only employers that have engaged in larger layoffs tending toward the higher amount. How does that happen? "Free" coverage can incentivize relatively more healthy members to elect COBRA, which brings the total COBRA claims costs closer the total COBRA premiums collected.

[2] A word of caution: The average cost does not fully capture the volatility risk of an unexpected large COBRA claimant on the plan for an employer. Stop loss policies should be reviewed for coverage and high-cost claims management mitigation strategies employed in these cases.

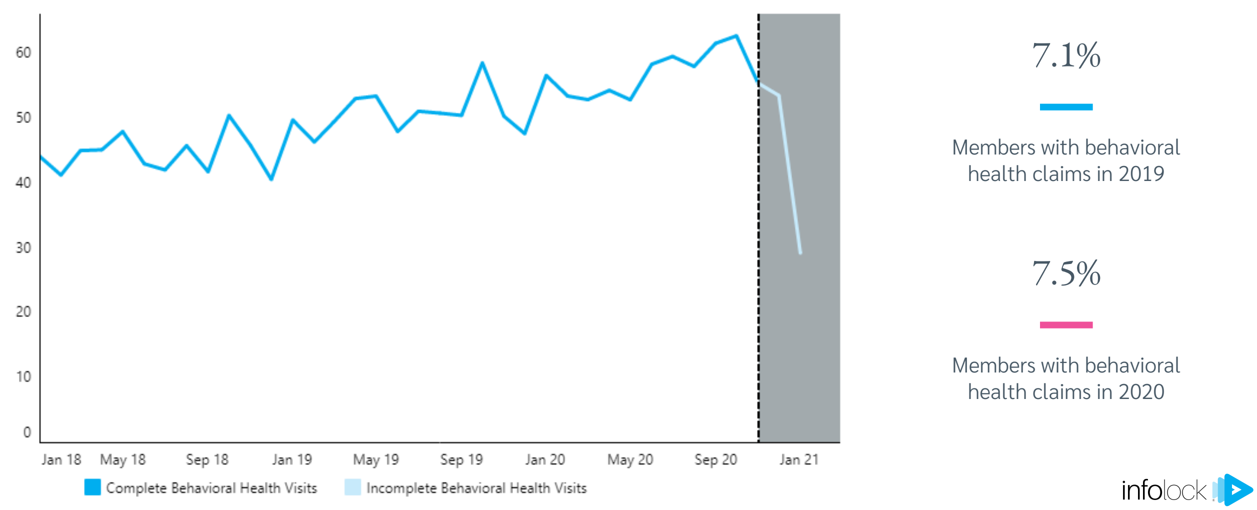
Increases in mental health & behavioral health claims

Economic uncertainty, fear of COVID-19 and social isolation have been stressful to employees and their families. Mental health and behavioral health claims increased over the course of 2020 and are expected to continue into 2021 and possibly beyond.

In our Infolock data, we see evidence of utilization changes in behavioral health visits, specifically in telehealth claims. Prior to COVID-19, upper respiratory symptoms were some of the most frequent diagnoses for virtual visits. During COVID-19, the proportion of telehealth visits associated with a mental health diagnosis more than doubled.

PROFESSIONAL UTILIZATION CHANGE — BEHAVIORAL HEALTH VISITS PER 1,000 MEMBERS

Unlike many other services, mental health and behavioral health claims steadily increased over the course of 2020



Elevated mental health and behavioral health claim activity is expected to add upward pressure to plans in 2021. Our current projection estimates indicate about a 0.0%-0.5% impact to a typical plan over a non-COVID norm and this may continue into 2022.

Less certain cost increases

Will missed preventive care lead to health deterioration?

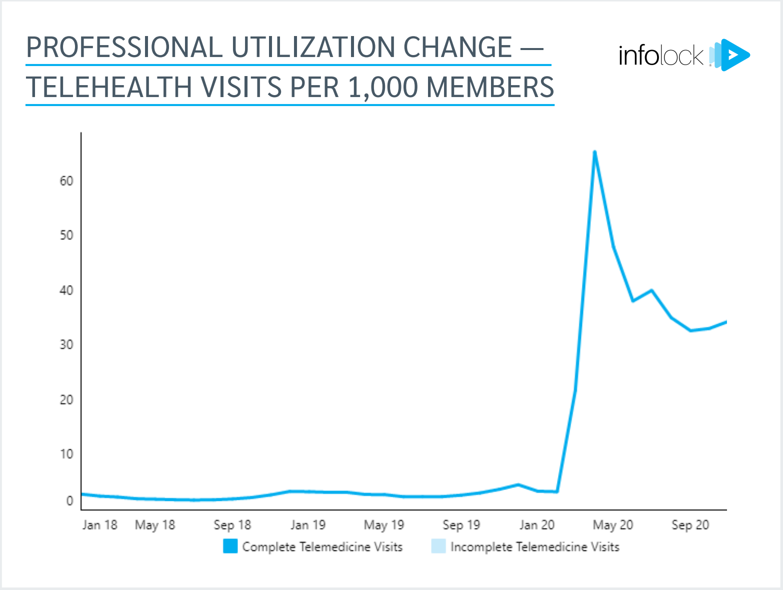
Some less certain increases will continue to unfold over time. Closures and member healthcare avoidance meant preventive care utilization dropped in 2020, with less than 50% of members receiving recommended cancer screenings. Because of this, missed preventive care in 2020 may contribute to a general deterioration of member health in the future, which may translate into upward trend pressure. We also do not yet know the long-term implications of COVID-19 infection.

Likely cost decreases

Members shift to telehealth

COVID-19 has ushered in a new era for telehealth that likely creates downward pressure on future costs. Typically, telehealth claims are more cost-efficient, particularly in lieu of an emergency room visit. Our Infolock data showed a dramatic spike in telehealth claims over spring 2020 that appears to be settling into a new, higher utilization pattern.

This shift is expected to provide some slight relief to trend and our modeling indicates a modest drop in claims of 0.25% or less.



Less certain cost decreases

Semi-permanent, ongoing avoidance of care is a possibility

General member reluctance to seek or elect care may continue to depress trends in the near term. As an example, a sustained decrease in outpatient utilization and ER utilization of 5%-10% could reduce spend by 1.5%-3.0%.

While some of this reluctance may ebb over time, it is possible there are potentially lasting member behavior changes that will continue to decrease trend over time. One example is lower emergency room (ER) utilization. In 2020, we saw a notable drop in ER usage over the spring 2020, followed by an ongoing lower steady state in the summer, fall and winter. While some avoided ER use could be of concern, a positive statistic is that potentially avoidable ER visits were down in 2020. To the extent this change continues in the future, it may also help to lower trend in future years.

COST IMPACT CONSIDERATIONS

POTENTIAL INCREASES & DECREASES	
COVID-19 testing	+
COVID-19 treatment	+
COVID-19 vaccines	+
Impact of extended COBRA and/or COBRA subsidization	+
Increases in mental health and behavioral health claims	+
Members shift to telehealth	−
Semi-permanent, ongoing avoidance of care	−

Cost estimates cannot be added together as they are not mutually exclusive.

One thing that is clear about trend and cost projections during COVID-19 is underwriting or claims projection methods that worked in the past will not necessarily work in the future.

It will be critical for employer plan sponsors to understand the what and why behind these data adjustments in their cost projections for 2021 and 2022. Lockton's actuaries and analysts have established best practices in underwriting during times of COVID-19, evolving the practice as data and circumstances evolve over this dynamic period.

Your Lockton consultant can work with you to navigate the shifting landscape and address better plan and employee health outcomes in a post-COVID-19 world.

UNCOMMONLY INDEPENDENT

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