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SECOND OPINION

Employers Turn To Alternative For Insuring Staff

Despite Legal Concerns, Workers Are Encouraged To Use Individual Policies

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PARK CITY, Utah -- Many small businesses have trouble providing health coverage because the costs of paying benefits for a handful of ailing employees drive up the premiums for their entire staffs.

Now an entrepreneur in Utah, relying on a wrinkle in U.S. tax law, thinks he has found a way around the problem. His idea: Employers should stop providing group health insurance and help employees get individual policies instead.

Paul Zane Pilzer, founder of Zane Benefits, discusses the pros of health reimbursement arrangements or HRAs over group health insurance. Kelsey Hubbard has the interview.

Paul Zane Pilzer, a 53-year-old economist, occasional rabbi and author of books like "God Wants You to Be Rich," isn't just concocting theories. His sales method has drawn interest from insurance giant **UnitedHealth Group** Inc. His company, Zane Benefits LLC, has signed up more than 300 employers covering around 3,000 people since opening in March 2006. A company led by America Online founder Steve Case and a unit of **Wal-Mart Stores** Inc. have teamed up to market the idea to small business.

Mr. Pilzer is among a growing number of people -- politicians, policy makers and others -- scrambling to find alternatives to the U.S. system of employer-provided insurance. Some merely want to fix a system that leaves millions uninsured; others are looking for ways to profit from patching together the system.

None of the solutions so far is perfect, but Mr. Pilzer's is gaining traction. Critics say his plan doesn't take account of those people who can't get individual coverage because of previous or existing illnesses. Mr. Pilzer says they can get help from their state or other sources. With many companies dropping group coverage, "we believe something is better than nothing," says Bryce Williams, chief executive at a subsidiary of Mr. Case's company involved in the marketing.

Critics say the concept violates the fundamental principle of health insurance: that the well help pay for the coverage of the sick. "It's poor public policy," says Greg Matis, counsel for SelectHealth, a Utah insurer that won't cover workers this way. "Here it will only be healthy people who get individual policies, and the ones who need coverage the most -- the highest-risk people -- will be left holding the bag."

But Mr. Pilzer believes it's better for individuals to buy their own health-insurance policies because, under state and federal laws, the policies can't be terminated for health reasons. By contrast, workers who lose group coverage when they're laid off or change jobs may not be able to replace it. He also contends that, with individual policies, consumers pay only for the benefits they want, avoiding the bells and whistles in employer plans that drive up health costs.

Paul Zane Pilzer

"I feel I'm doing God's work switching people from group plans to individual insurance," he says.

He likens his philosophy to the shift in recent decades to 401(k) retirement plans, where employers provide tax-deferred dollars and it's up to employees to invest them. "Employers will be relieved of a crushing moral and financial obligation that they should never have taken on in the first place," he says. Some say Mr. Pilzer's setup violates a federal law requiring that employers offer coverage to everybody or nobody. Texas insurance regulators have warned employers not to try the idea, saying it discriminates against sicker workers.

"I think this is blatantly illegal," says Mila Kofman, an associate professor at the Georgetown University Health Policy Institute and a former Labor Department official. "I would not advise any employer to do this."

Mr. Pilzer calls his plan legal, and so far the federal government hasn't said anything to the contrary. The Department of Labor says it is aware of the controversy and is consulting with other parts of the federal government over possible clarification of the rules.

According to the Kaiser Family Foundation, 60% of businesses offered health benefits in 2005, down from 69% in 2000. Employer premiums for family coverage rose 81% since 2000 to $11,480 annually.

The tax wrinkle used by Mr. Pilzer involves something called a health reimbursement arrangement, or HRA. Employers set aside a certain sum every month, say $200, that employees can use for health expenses. The employer can write off the expense for tax purposes, just like traditional health benefits, and the money doesn't count as taxable income for the employee.

The tax advantages of HRAs resemble the better-known health savings accounts, or HSAs. Both plans are sometimes used by large employers that offer comprehensive benefits and want to supplement it by giving employees tax-free dollars for noncovered medical costs.

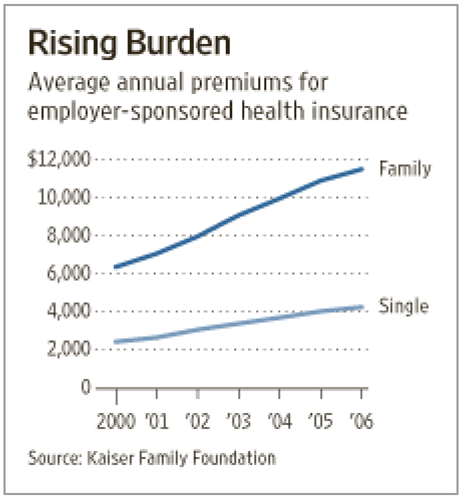
The key difference is that employees can use the money in an HRA, but generally not an HSA, to buy health insurance. That's why an HRA can be used not just to supplement health insurance but also to buy it.

At a business with generally healthy employees, an HRA plan, in effect, allows the owner to cover a good chunk of most people's insurance bills at a fraction of the cost of a traditional group insurance plan. The idea is especially attractive to small businesses that don't have the leverage to drive a good bargain for group coverage.

Helen Griffin, owner of IT Pros in Overland Park, Kan., was fed up with soaring premiums her insurer was demanding. The technology firm this year began offering a $100-a-month HRA allowance, plus an additional $200 a month for workers with a spouse and children.

Ms. Griffin says all five of her full-time employees were able to find individual coverage. She and her husband paid a combined $330 a month for their policies, down from $800 a month paid by the company when the business had a group plan. Businesses with only a handful of employees often pay high group premiums, because insurers must accept all employees and they keep rates high to protect against large claims.

"The biggest thing for us: No more increases," says Ms. Griffin, referring to her previous group plan.



Critics say a system like the one at IT Pros encourages employees to pick a bare-bones policy with low premiums that may exclude coverage for pre-existing conditions, maternity care, or other major medical needs.

The setup is attractive to some insurance companies worried about losing business as employers drop coverage. Like traditional group coverage, the HRA is a mechanism for companies' money to get pumped into insurance premiums. But with individual coverage, insurers are allowed, in most states, to weed out sick people likely to rack up big bills. An industry survey in 2004 found about a quarter of people 55 to 64 get rejected for individual coverage, above the overall average of 13%.

UnitedHealth is encouraging hundreds of its independent agents to take an online course offered by Mr. Pilzer's Zane Benefits to learn how to market individual plans at companies with HRAs. Zane Benefits isn't an insurer. It earns about $10 a month per worker administering plans for companies. Workers typically buy insurance with their own money, then submit paperwork to Zane to get reimbursed with HRA money.

Sam's Club, the warehouse chain of Wal-Mart, has been selling HRA-based plans to small businesses since January 2006 in a tie-up with Extend Health Inc., a company started by Mr. Pilzer that is now part of Mr. Case's Revolution Health Group LLC. Patricc Quinn, director of travel and nonfinancial services for Sam's Club, declined to say how many employers have signed up, but he said response has been strong.

"It's a very simple model going back to individual health insurance, something that fits small businesses better than group insurance," says Mr. Quinn. "Members don't believe it. It's too good to be true."

Barnett Well Services LP in Cresson, Texas, joined the Sam's Club program in April 2006. The oil-industry trucking firm says group insurance was too expensive at $420 a month per employee. Instead, each of the 28 workers gets $100 a month of HRA money to put toward insurance premiums or, if they prefer, other medical expenses.

A former Citibank vice president, real-estate developer and professor at New York University, Mr. Pilzer says he earned his first $10 million before age 30. His books include "Other People's Money," about the savings-and-loan crisis. He now lives in the resort town of Park City, Utah, and says he has occasionally served as a rabbi at bar mitzvahs and weddings. He helped found Park City's first synagogue.

Mr. Pilzer says he became interested in pursuing health care as a business in late 1999 when his wife became pregnant with their first child. (They now have four children, ages 2 to 6.) During the pregnancy, he lost insurance he had held through a board position. When he called an agent to buy his own policy, he was surprised to find premiums for a healthy family like his were just $220 a month.

With help from some investors, he started a company to explore the insurance market. It began to take off as Internal Revenue Service rulings in 2002 and 2005 clarified that HRA money could be used to buy insurance. In October 2005, he sold a controlling stake in his company to Mr. Case's group, and started Zane Benefits the next year after a noncompete agreement expired.

Small-business owner Jennifer Morgan was captivated by an interview Mr. Pilzer gave on the Christian Broadcasting Network, during which he told host Pat Robertson about HRAs and a book he had written called "The New Health Insurance Solution."

Ms. Morgan's business, MGI Morgan General Mechanical Group Inc., which builds and services generators, pump stations and fuel tanks, has 40 full-time employees and annual revenue of nearly $9 million. The Deerfield Beach, Fla., company's group health premiums shot up 24% in 2005, and the cost of family coverage grew to nearly $1,000 a month -- of which the company could cover only about $200. Ms. Morgan assigned the problem to her human-resources director -- her daughter, Jessica.

Jennifer and Jessica Morgan

After marking pages of Mr. Pilzer's book with Post-it notes, Jessica Morgan tried to set up HRAs. Several insurance agents told her it was illegal. Undeterred, she typed Mr. Pilzer's name in an Internet search late last year, found Zane Benefits and signed up for the HRA program. So far, eight employees have gone the HRA route, enabling them to get reimbursed for individual coverage. The Morgans still offer a group health plan from UnitedHealth, but may cancel it at renewal next year.

The younger Ms. Morgan, who is 28, found an individual policy from UnitedHealth's Golden Rule Insurance Co. that costs $123 a month -- less than the $150 she's entitled to through the HRA. She can use the $27 a month left over for other medical expenses. "I'm making money every month on my health insurance," she says. "I'm making out like a bandit."

Randi Pendleton, a 28-year-old in accounts payable, is also pleased at her savings on an individual plan. Previously, it had nagged at her that she was paying high premiums even though she's in good health. "A lot of people in the group plan are not as healthy. Is that affecting my policy and what it costs?" Ms. Pendleton says. "That is something I've thought about."

If MGI dumps its group plan, one person who could be in a pinch is the elder Ms. Morgan, 52, whose health isn't as good as her daughter's. She was hospitalized in October 2005 with high blood pressure and now takes medication for the condition. What's more, she says someone erroneously wrote on her medical chart that she suffered from an aortic aneurysm. She has received a letter from her doctor setting the record straight, and believes she would qualify for an individual policy.

Richard Schulz, 62, manager of MGI's generator division, had three stents implanted in April 2006 after tests found blockages in his blood vessels. "Too bad for me this wasn't around 25 years ago," Mr.

limits		single or $5,650 for a family
Unspent funds	Rollover yearly, subject to employer limit	Unlimited rollover
Premium reimbursement	Yes	Generally no
Interest accrual	No	Yes

Source: Internal Revenue Service

Schulz says of the HRA idea. "I'm not sure I would qualify now." He would face the prospect of going uninsured, except that his wife can get group coverage through her employer.

Thirty-four states have a high-risk pool for people who can't get insurance because of illness, but the premiums can be up to double the usual rate. The Florida high-risk pool has been closed to new enrollment since 1991 owing to a lack of funding.

In Texas, workers are ineligible for last-resort insurance if their employer offers an HRA. Jennifer Ahrens, associate commissioner of the state insurance department, says people with existing conditions "would be locked out of insurance completely" if a company dropped group coverage in favor of an HRA. Because of the barriers in Texas, Extend Health and Zane Benefits have stopped marketing HRA reimbursement for health insurance there.

Mr. Pilzer acknowledges there are holes in the government safety net, but he accuses Texas regulators of making matters worse by trying to shield higher-priced group policies from competition. The state's rules are "total price protection for brokers selling group insurance," he says. "It's a joke."

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