

## **A NEW APPROACH TO EAP PRICING**

by Tom Farris, Ph.D.

Most EAP services historically have been priced on a capitated (per employee per month, or PEPM) basis. This pricing structure, unfortunately, has contributed to the commoditization of the EAP industry. By commoditization, I mean that there is little perceived difference in quality among EAP vendors and, therefore, purchasing decisions are made almost exclusively on the basis of price.

The problem with capitation is that it creates a financial incentive for the EAP to provide as little service as possible. The fewer the number of cases seen, the less the EAP will spend to service the contract and the more money it will make. Of course, an EAP with little or no utilization isn't really worth much because it doesn't help address any of the underlying issues that might be cutting into worker productivity and the employer's bottom line.

Many employers, however, prefer a capitated pricing structure. Not only is capitation inexpensive, it provides a consistent budget for EAP services and forces the EAP to take the financial risk for the program.

For the past several years, EAPs have been dramatically lowering prices in an attempt to gain market share. Even more alarming, EAPs sometimes are being included at "no charge" if an employer purchases a disability plan or other service from an insurance company. In such instances, the cost of the EAP is absorbed into the other insurance product. These "free" EAPs do little to promote their programs because any kind of utilization would erode their already slim profit margins.

Purchasers, in turn, have contributed to the commoditization problem by demanding low premiums and not holding EAPs accountable for achieving results. In addition, many benefits managers and human resources staff who make purchasing decisions don't place the same importance on EAPs that they place on health plans, dental plans, 401(k)s, etc. EAPs are less expensive than pension and benefits programs, so purchasing an EAP becomes a relatively insignificant decision compared to choosing, say, a health plan. It is not surprising, then, that purchasers might simply pick the EAP with the lowest bid, plug this cost into a budget, and forget about it.

### Measuring the Value of an EAP

As EA professionals, we are passionate about our services and our ability to positively affect organizations. Our challenge during the sales process is to convince the purchaser that an EAP is not "just another benefit" but a vital strategic partner that produces a significant return on investment if properly promoted. We need to make the purchaser understand that an EAP can be overpriced at \$1.00 PEPM or a tremendous value at \$3.00 PEPM, depending on the outcomes it achieves.

In my view, an EAP should be judged on program results, not simply on price. The key metrics for an EAP are the numbers, types, and outcomes for:

- Clinical cases;
- Management consultations;
- Management referrals;
- Organizational interventions (e.g., critical incident response, executive coaching, training, etc.);
- Work/life cases; and
- Account management activities.

Since there is no agreed-upon standard for reporting EAP utilization, it is difficult for employers to make an “apples to apples” comparison among programs. Many low-cost EAPs create the appearance of a highly utilized program by counting routine phone calls and Web hits. Utilization reports often are presented in a convoluted format, making it even more difficult for an employer to understand how the EAP is affecting (or not affecting) the work organization’s health and productivity.

While a detailed discussion of utilization reporting is beyond the scope of this article, it does not need to be an overly complex issue. EAPs need to report clearly on each type of activity--clinical cases, work/life cases, management consultations, and so on. A single utilization number cannot meaningfully capture the variety of services an EAP provides or the breadth and depth of its impact. Employers need to be educated about the meaning and effect of utilization in each program activity, so utilization reports must be concise and easy to understand.

*An EAP can only make a case that its services are superior to those of a competitor (and therefore not a commodity) when a purchaser understands and appropriately values the different elements that comprise EAP utilization.* This is the key to creating an EAP pricing model that does not have the incentive problems that are inherent with capitation. EAPs need to be financially rewarded--not penalized--for generating utilization and solving costly problems on behalf of the employer.

### Value-Based Pricing

Value-based pricing is a concept that ties an EAP’s fee to its accomplishments and utilization, thus creating an incentive for the EAP to be proactive and significantly affect an organization’s health and productivity. If utilization is low, the employer pays less; if the EAP is successful in generating cases, the employer pays more. There are several value-based pricing models, of which this article will examine three.

**Per-visit model.** In this model, an employer is billed for each clinical visit and each work/life case. The rate billed for these services is marked up 50 to 60 percent above the actual cost. All account management services are built into a “per visit” rate; critical incident response, training, and other services can be included in the per-visit rate or billed on a fee-for-service basis.

**Hybrid model.** The hybrid model incorporates a “per clinical visit” fee plus a relatively low PEPM fee that includes costs for account management and work/life services. Critical incident response, training, and other services can be built into the PEPM fee or billed on a fee-for-service basis. The “per clinical visit” fee is marked up 15 to 25 percent above the average

actual cost of a visit. The monthly capitated fee can be set at a fairly low level, depending on the services included in the fee.

**Target range model.** The target range model features a PEPM fee plus a utilization adjustment fee. The PEPM fee is relatively low and includes all account management services plus clinical, work/life, and management consultation services up to modest predetermined utilization targets. The PEPM fee may also include critical incident response, training, and other services. The utilization adjustment fee is paid only if actual utilization exceeds the utilization targets set for clinical, work/life, and management consultations.

An example may help illustrate the target range model. A company with 2,000 employees implements a three-visit EAP with a PEPM fee of \$1.35. The utilization targets and utilization adjustments are as follows:

| Type of Case        | Utilization Targets (Percentage) | Utilization Targets (Number of Cases) | Utilization Adjustment Fee |
|---------------------|----------------------------------|---------------------------------------|----------------------------|
| Clinical            | 3%                               | 60                                    | \$220 per case             |
| Work / Life         | 1%                               | 20                                    | \$110 per case             |
| Management Consults | 0.25%                            | 5                                     | \$250 per case             |

In the first year, the EAP achieves the following utilization levels:

| Type of Case        | Actual Utilization | Number of Cases (Total) | Number of Cases Over Target | Utilization Adjustments * |
|---------------------|--------------------|-------------------------|-----------------------------|---------------------------|
| Clinical            | 6%                 | 120                     | 60                          | \$13,200                  |
| Work / Life         | 2%                 | 40                      | 20                          | \$2,200                   |
| Management Consults | 0.5%               | 10                      | 5                           | \$1,250                   |

\* This amount is derived by multiplying the number of cases over the target range by the “per case” utilization adjustment amount.

These utilization levels would be considered successful by most EA professionals and are above industry standards. The financial results for the first year are as follows:

|                            |          |
|----------------------------|----------|
| PEPM Fee                   | \$32,400 |
| Utilization Adjustment Fee | \$16,650 |
| Total Annual Fee           | \$49,050 |
| PEPM Equivalent            | \$2.04   |

## Advantages and Disadvantages

The per-visit and hybrid models have the advantage of being simple for purchasers to understand and for the EAP to administer. The disadvantage is that they do not set utilization goals. The target range model, meanwhile, has the advantage of accurately capturing the different categories of service provided by the EAP. By linking a fee with each of the major categories of work, it provides the EAP an opportunity to highlight its accomplishments. The disadvantage of this model is that it is more complicated to understand and administer.

The target range and hybrid models also have the advantage of featuring a low PEPM fee that, in all likelihood, will be less than the PEPM fees submitted by other vendors. The downside is that these models (indeed, all value-based models) are difficult for purchasers to compare with traditional capitated fees. Also, whereas traditional capitated models place all of the financial risk on the EAP, value-based models essentially share the risk between the EAP and employer.

Many employers are wary of value-based models because they necessarily involve a variable rate, which makes it difficult to set a fixed budget for EAP services. One solution is to set a maximum annual cap that the program cannot exceed. This allows the employer to pay only for services it actually uses and ensures that costs won't spiral out of control.

From the EAP's perspective, hitting the cap is not necessarily a bad thing. The EAP will have generated significant utilization and, thus, will have plenty of data to support its need to raise the cap when its contract is due for renewal. An EAP with a multi-year contract can even specify in the agreement that if the cap is reached during any year, it will be raised to a predetermined level for the following year. This approach manages the financial risk for both the EAP and the employer.

The cap should be set at a level that assumes the program will be utilized extensively, but not so extensively that the cap probably will not be reached. The purchaser, in all likelihood, will be comparing the cap to traditional capitated rates proposed by other EAPs. In my experience, the maximum cap can be set 10 to 25 percent higher than the average of the competitors' capitated rates.

## Creating a Financial Incentive

From the employer's perspective, value-based pricing models are attractive because if utilization is low or average, the cost for the EAP will be less than that of others bidding on the program. If utilization is high, on the other hand, it indicates that the program is actually solving problems and producing value. The employer will pay slightly more, but is still protected by the annual cap.

Value-based pricing models can help EAPs resist the commoditization quagmire that threatens our industry. These models create a financial incentive for an EAP to accomplish its fundamental mission--helping employees resolve personal problems that affect their work performance. A well-utilized EAP, in turn, produces a significant return on investment for the employer. If nothing else, offering value-based pricing as an alternative to capitated pricing creates an opportunity during the sales process to discuss an employer's goals for its EAP and the EAP's true value proposition.

*Tom Farris is chief operating officer of Claremont Partners, Inc.*