

1. Employer-Sponsored Health Insurance: Are Employers Good Agents for Their Employees?

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EMPLOYERS IN THE UNITED STATES PROVIDE MANY welfare-type benefits, such as life insurance, disability insurance, health insurance, and pensions, to their employees. These benefits make up an increasing share of overall employee compensation, defined as comprising wages and salaries, voluntary benefits, and legally required benefits (payments to the Medicare and Social Security trust funds and workers' compensation insurance) (Ehrenberg and Smith 1988; Wiatrowski 1999). Economists argue that employees effectively pay for most of their nonwage benefits through lower wages (Ehrenberg and Smith 1988). They also argue the view that the employer serves as the employee's agent in purchasing pension, health, and other welfare benefits (Acs and Steuerle 1996).

In the economic literature, an agent is defined as one acting on the behalf of another, who is referred to as the principal (Besanko, Dranove, and Shanley 1996). Agents may act for the principal when he or she lacks the skills, the expertise, or the scale to perform tasks efficiently or to make decisions independently. Analysts point out that many employees view their employer's agency role favorably because employers can negotiate better terms when purchasing goods, such as health insurance and other

employment benefits, than employees can obtain on their own (Acs and Steuerle 1996). Analysts, of course, also remind us that the current tax laws provide strong financial incentives for employers to offer health insurance (Pauly 1986; 1997).

Health insurance is one of the most important of these welfare-type benefits: 90 percent of the nonelderly with private health insurance are covered through employer-sponsored health plans (National Center for Health Statistics 1997; Fronstin 1998). Employers decide whether to offer health insurance, and if they do, they select the plan(s) and their provisions. As the restrictions on access to physicians and hospitals that have accompanied the advent of managed care increase, the decisions of employers concerning health insurance offerings are likely to become more important to employees. Under traditional insurance plans, employers' decisions influenced the costs of employees' premiums and their out-of-pocket expenses for care. Under the prevailing models of managed care, employers' decisions influence not only those costs but also the network of available health care providers and the process for accessing care. Thus, an assessment of the current changes in the U.S. health care system must take into account how employers perform as agents. Dranove and White (1999) stressed this point when they argued that assessing the welfare implications of these changes depends on whether "employers who make most of these decisions *fully account for the preferences of their employees.*"

More literature is being written about the trends in employer-sponsored health insurance offerings and the identification of best practices used by leading corporations (such as Xerox and Ford Motor Company), employer groups, and coalitions (such as the Pacific Business Group on Health) (Coulter, Fabius, Hecksher, et al. 1998; Xakellis, McGlynn, and Ginsinger 1998; Maxwell, Briscoe, Davidson, et al. 1998; Rice, Desmond, and Pourat 1999; Cooper and Schone 1999; Schauffler, Brown, and Milstein 1999). A considerable amount of research has addressed employees' satisfaction with their health plans and with the services they receive under those plans (Davis and Schoen 1997; Gawande, Blendon, Brodie, et al. 1998). Although the relationship between employers and employees in purchasing health insurance does not strictly conform to a principal-agent model, it nevertheless provides a framework for informing the debate about this question. Very little research has focused specifically on the agency relationship between the employer and the employee.

How well do employers perform as agents for their employees in selecting health insurance plans? Economists would argue that employers are likely to act effectively as agents because, if they do not, they will ultimately bear the cost of that ineffectiveness in higher total compensation costs and/or greater employee turnover (Ehrenberg and Smith 1988; Kaufman 1989). Although this may be true over the long term, it seems likely that during periods of fast, significant change, as exemplified in the rapid restructuring of the health care delivery and financing system that is now taking place, the potential for deviation from traditional expectations is considerable. Certainly, the backlash against managed care suggests that people are very concerned about current trends (Blendon, Brodie, Benson, et al. 1998). For this reason, we were motivated to assess how well employers perform as agents in the short term.

We believe that if employers are effective agents for their employees, the following conditions should hold:

- Employers understand their employees' health plan preferences.
- Employers incorporate employee preferences into their health plan designs.
- Employees value their employer's agency role in purchasing health insurance benefits.

We also posit that if employers are effective agents, they should establish mechanisms for soliciting and understanding their employees' preferences and provide useful information to their employees about their health insurance offerings. We will examine the extent to which these conditions hold true in a small sample of large employers.

Data and Methods

Overview

The data for this study were collected as part of a larger project that examined how employers make decisions about health plan options. Three types of information collected during this project are presented here:

1. the results of structured interviews with senior human resource managers at selected employers
2. the findings from employee focus groups that were conducted at a subset of these employers

3. an overview of employer-supplied information on health insurance choices

Identification of Employers to Be Interviewed

We interviewed large employers in Pittsburgh and Cleveland between February, 1997, and April, 1998. These two metropolitan areas have relatively similar population demographics and economic activity. We defined a large employer as one with more than 800 local employees. We focused on local employment because we were interested in identifying firms large enough to achieve bargaining power in the regional health insurance market. We selected employers in four industry categories: banking and financial services; manufacturing; education; and hospitals. We excluded retail businesses, such as department stores, because, despite their large workforces, many of their employees were not offered health insurance benefits. We also excluded public employers. Firms were selected from rosters of regional employers supplied by local chambers of commerce and regional business groups.

We interviewed a total of 40 firms: 23 in the Pittsburgh metropolitan statistical area (MSA) and 17 in the Cleveland MSA. Table 1 lists the number of employers in each category and their average number of local employees.

Interviews with Senior Managers

After obtaining informed consent, a project investigator conducted a structured interview with the individual identified by the employer as being primarily responsible for designing the firm's health insurance

TABLE 1
Employers Interviewed by Size and Industrial Group

Industry group	Number of employers	Average local employment
Hospitals	11	3,010
Banking/service	9	7,700
Manufacturing	16	2,570
Education	4	4,300
Total	40	4,020

offerings. In most cases, this was the vice president of human resources or the manager of employee benefits, although more than one person participated in several of the interviews. The interview was designed to solicit detailed information on how the employers choose their health insurance offerings. Respondents were asked to select from a list of health plan characteristics the four that they consider critical to the firm's health plan package. They were also asked to identify the most—and the least—important characteristics from a list that included choice of insurer, choice of providers, quality of care, the geographic network of providers, availability of specific services, and cost (both to the firm and to the employee). Later in the interview, respondents were asked to rank a similar set of health plan characteristics according to the importance assigned to them by their employees. Specifically, they were asked to score the importance of each characteristic on a scale of 1 (least important to their employees) to 5 (most important). Respondents were also asked whether they track employees' preferences through systematic procedures like employee meetings, formal complaint systems, employee surveys, and focus groups.

Employee Focus Groups

We conducted focus groups of employees to discover their preferences and opinions about health insurance options. They took place between January and August, 1998, at 5 of the 40 participating firms. Of the 40 employers interviewed, 15 refused to allow us to conduct focus groups with their employees, most frequently because of concerns about raising employee expectations in the context of upcoming insurance enrollment periods and union negotiations. Focus groups were conducted with employees from two universities, one health care system, one banking–financial services firm, and a high-technology manufacturer.

The human resources department of the five consenting employers notified all nonunion employees of the possibility of being solicited to participate in a focus group. Employees other than those in top management and human resources were randomly selected from company directories and contacted by a study investigator by telephone at their workplace. To be eligible to participate, employees had to be enrolled in a health insurance plan offered by their employer. Of the 428 individuals contacted, 325 either did not wish to participate or were not currently enrolled in their employer's health insurance plan. We screened

potential participants to ensure that each focus group would contain a mixture of participants by age, sex, and children living at home. Two focus groups of seven to twelve participants were held at each of five firms, for a total of ten focus groups. The same investigator led each 90-minute focus group. Informed consent was obtained and participants received a small cash payment.

The focus groups were convened to achieve certain goals:

1. identify the characteristics of health insurance plans that mattered most to employees
2. assess employees' impressions of which plan characteristics mattered most to their employers
3. summarize the employees' experiences with their health plans
4. explore employees' opinions about selecting their own health insurance plans in the market

In order to achieve the first and second goals, participants were asked to rank a list of health plan characteristics (similar to those shown the employers) by their relative importance (very important, important, not important) to them. They were also asked to identify the single most important and the single least important characteristic on the list. Standard focus-group procedures were used to address each characteristic (Knodel 1993).

Information on Health Benefit Plans

We asked each firm for copies of all informational materials on health insurance offerings that were distributed to their employees during the previous three years, and we received material from 38 of the 40 employers in the study. We examined these materials to see if they contained any of the following items: a comprehensive listing of plan benefits; a chart comparing the different plans being offered; a glossary of terms; examples of how the plans would work under different circumstances; administrative procedures for filing claims; lists of covered and noncovered services; and a worksheet to aid in signing up for a plan.

Analytical Methods

The exploratory nature of our study and its small sample size did not permit us to test hypotheses; we focus instead on describing our findings.

Results

We organize the results by first describing the types of insurance plans offered by employers and then looking at the preferences for plans expressed by the employee focus-group participants. Turning to employers, we first discuss the methods they use to track employees' preferences and look at their perceptions of employee preferences. We then assess the extent to which employers incorporate employees' plan preferences. Next, we examine the nature of the information that employers provide regarding their health plan selection. Finally, we return to the employees and solicit their views on whether they want their employers to continue to act as their agents. In presenting the results, we do not distinguish between the Pittsburgh and the Cleveland firms because the measures we studied did not differ in any meaningful way between the two markets.

Overview of Health Insurance Offerings by Sample Employers

The majority of the employers (93 percent) gave their employees some choice among health plans: fifteen employers offered five or more plans; seven offered four plans; eight offered three plans; seven offered two plans; and only three offered just a single plan. Most of the plans (81 percent) fell into the managed care category. Sixteen employers (40 percent) offered at least one fee-for-service plan, twenty-nine offered at least one HMO, and thirty-eight offered at least one point-of-service/preferred provider organization (POS/PPO) plan. Plans with the same benefit structure, but whose deductible and copayment options differed, were counted as multiple plans. The managed care plans in the two regions were predominantly independent provider association (IPA) models, organized so that a health plan or insurance company contracts with independent physicians to form its provider network.

Employee Preferences

Table 2 reports employees' expressed preferences regarding health plan characteristics. Over 60 percent of the focus-group participants rated either access to specific providers or quality of care as the most important factor. It is likely that, in the view of employees, these two aspects capture the same attribute because, during the discussions, the participants

TABLE 2
 Characteristics of Health Plans That Employee Focus Groups
 Identified as Important^a

Health plan characteristics	Most important ^b	Least important
Having choice among products (i.e., HMO, POS)	1	6
Having choice among insurers	7	24
<i>Specific providers in plan</i>	30	5
Amount of employee premium	11	5
Patient cost sharing (deductibles, copays)	3	12
Having preventive services covered	3	6
Range of covered services	13	2
<i>Quality of care</i>	30	0
HMO accreditation	0	26

^aThere were 88 participants.

^bSome participants identified more than one most or one least important factor; rather than omitting responses from those participants, all are included.

clearly stated that they considered quality to be a function of the specific provider, not of the plan. Only a small proportion of participants listed other characteristics as “most important.” Clearly, employees thought the least important factors were having a choice among insurers and HMO accreditation. Approximately 30 percent of employees said that being able to choose among insurance companies was least important to them, and the same proportion indicated that they viewed accreditation of HMO plans as least critical.

Employers’ Understanding of Employees’ Preferences Regarding Health Plans

How Employers Track Employee Preferences. Thirty-nine of the 40 employers interviewed (98 percent) claimed that their firm used at least one of four specified methods (employee meetings, complaints, employee surveys, and focus groups) to obtain information on employee preferences and concerns about health insurance: 26 (65 percent) used formal employee meetings; 26 firms (65 percent) used employee complaints; 29 (73 percent) used employee survey results; and 23 (48 percent) used focus groups. Perhaps more significant is the fact that 37 of these 40

TABLE 3
Insurance Options That Employers Believe Matter
to Their Employees^a

Options	Mean	Min–Max
Specific insurers or managed care companies	2.85	1–5
Choice among insurers	3.03	1–5
Type of insurance product (i.e., HMO, POS/PPO, indemnity)	3.90	1–5
<i>Access to specific providers</i>	4.70	3–5
Out-of-pocket cost of care (deductibles and coinsurance)	4.50	1–5
Employee portion of insurance premium	4.43	3–5
Dependent portion of insurance premium	4.38	3–5
Overall package of benefits	4.01	2–5
Perceived quality of care	4.09	1–5
<i>HMO accreditation</i>	1.76	1–3

^aMean scores presented: score based on ranking from 1 (least important) to 5 (most important).

firms used at least one of the firm-initiated methods (surveys, formal meetings, or focus groups) for collecting such information, and only one firm did not solicit employee opinions in any organized way.

Employers' Perceptions of Employee Preferences. Table 3 provides data on the specific characteristics of health plans that employers believe matter to their employees. Clearly, access to specific providers heads the list, closely followed by the cost to employees—in the form of their share of health insurance premiums and their direct out-of-pocket payments for the use of medical care. Quality of care ranks next in importance. However, employers noted during the interviews that employees consider access to specific providers and quality to be closely related because they view quality as a function of the care given by specific providers rather than as a plan attribute. Employers indicated that HMO accreditation status is the plan attribute least valued by their employees.

Consistency between Employers and Employees. The firms we studied differed in their views of what was important to their employees, and their employees also held different opinions about what was important in health plans. However, in comparing the views of employers and employees in the five firms where we conducted focus groups, we found that all employers rated access to specific providers and quality of care

as most important to their employees. These perceptions coincided with the reports of the employee focus groups. When asked what was least important to their employees, these five employers cited either HMO accreditation or choice of insurer, duplicating exactly the responses of their employees in the focus groups. Based on this evidence, we conclude that the opinions of employers and employees in these five firms about the relative importance of plan attributes to employees were highly consistent.

Employer Incorporation of Employee Preferences

Given that employers understand what is important to employees in health insurance plans, how do they act based on that information? Although it is not possible to determine employers' motives from an examination of their health insurance offerings, we can look for evidence of consistency between employers' stated beliefs about what is important to their employees and the types of health insurance plans they offer to them.

From table 3, we see that employers believe that their employees value access to specific providers. Thirty-nine of the 40 employers rated this characteristic 4 or 5 on a 5-point scale (with 5 being most important). Additionally, employers expressed the belief that their employees were concerned about the cost of health insurance to employers (no employer rated this below a 3). We cannot observe the cost of health insurance options to employers in this study, but we can observe the range of choice among plans offered to employees. Employers can accommodate employee preferences for access to providers by offering several plans. The majority of the employers in this study (93 percent) did offer some choice among health plans. Another means of providing access to specific providers is to offer a PPO or POS plan. Ninety-five percent of the employers offered a PPO/POS plan, and most of these were based on an expansive network of providers. This suggests that the employers we studied do take employee preferences into account when selecting health insurance options to offer them.

Employer Health Plan Information

Most employers in this sample gave their employees some choice among plans. However, employees only benefit from choice if they are supplied with good information on these plans so they can make informed

decisions. Of the 38 employers who compiled and distributed informational material to their employees, 36 offered a choice among plans. Most of those employers (94 percent) provided a chart detailing the benefits available under each plan, but only 69 percent prepared a chart containing information on all offered plans so employees could easily compare them. In addition, 56 percent of the employers included worksheets and examples so that employees could estimate their own anticipated medical care costs. Although all the plan descriptions provided general information on benefits, only 72 percent listed the services covered by each plan, and only 61 percent listed the services that were explicitly excluded from coverage. Employers did provide information on the participating providers.

None of the employers in this study provided information on HMO quality, plan performance as measured by the Health Plan Employer Data and Information Set (HEDIS), or results of satisfaction surveys of plan members. Furthermore, employers did not provide any information on the quality of the network providers, although information on hospitals was available in both geographic regions. The Cleveland Health Quality Choice project extensively publicized the information it had compiled on hospital quality in the Cleveland area, and the Pennsylvania Health Care Cost Containment Council disseminated its findings on the quality of Pittsburgh hospitals.

Employees' Valuation of the Employer's Agency Role

Employees were asked if they would prefer to choose their own health insurance plan, independently of their employer, in much the same way that individuals choose auto insurance. Overwhelmingly, employees wanted to retain their employer as their agent in the selection of health insurance plans (Lave, Peele, Black, et al. 1999). The focus-group participants gave several reasons for not wanting to act as their own agents, which can be classified into three categories: lack of individual bargaining power; complexity of the market; and the employer's advocacy role. These are discussed in more detail below.

Most of the focus-group participants believed that their employers brought substantial bargaining power to the health insurance market and were able to purchase health insurance plans at lower prices than employees would be able to obtain for themselves. Most employees expressed

the opinion that their employers were far more knowledgeable about health insurance plans and were much better equipped to sort through the plans and options than they were individually. Although employees did not want to undertake the task of gathering and studying huge volumes of information about available plans and their relative prices, they did want to retain some degree of choice. Most wanted the employer to narrow the choice to a few plans and then permit employees to choose the one they preferred from that menu. Finally, many employees did not want to negotiate with insurers to obtain the benefits they felt they were entitled to under the plans they had selected. Several indicated that their employers assisted them in voicing their complaints to insurers. Although we did not ask employees explicitly if they were satisfied with their health insurance offerings, we believe that their nearly unanimous agreement about having the employers continue to select their health insurance offerings indicated reasonable satisfaction with the current plans they were being offered.

It is noteworthy that employees expressed a strong desire to have their employer act as their agent in the health insurance market, despite their expressed, nearly complete, agreement that their employers were most interested in decreasing the firms' costs. Employees correctly assessed their employers' interest in minimizing these costs. Employers in this sample overwhelming (98 percent) rated decreasing the cost of health plans to the firm as extremely important.

Discussion

In the United States today, there is some interest in reducing or eliminating the employers' role as the major provider of health insurance (Pauly 1997; American Medical Association 1998; Consensus Group 1998). Some observers have argued that a major problem with the present system is that the employer, not the individual, owns the health insurance policy (Gavora 1997). However, if employers are serving as effective agents for employees, then this criticism becomes less relevant.

We argued that if employers were effective agents for their employees, then the following conditions should hold: employers should understand their employees' health plan preferences; employers should incorporate those preferences into their health plan designs; and employees should value their employers' agency role in purchasing health insurance benefits.

The information we have presented suggests that these three conditions were essentially realized in our sample of large employers. First, the majority of the employers interviewed had established mechanisms for soliciting information from their employees about their health insurance preferences. We observed that, at least in the firms from which we obtained information on both employees and employers, the employers understood their workers' preferences. Second, employers do appear to incorporate employees' preferences into their plan benefit design, although the data supporting this observation are more tenuous. Most employees valued being able to choose among providers, and most employers in this study often offered their employees a selection of plans that allowed wide provider choice. Finally, employees of the firms that we were able to study valued the firms' agency role and did not want to become their own agents.

The main division between the values of employees and employers is over the issue of costs. Almost all employers (98 percent) told us that cost was either the most—or among the most—important of all the factors influencing their selection of health plans. Quality of the providers was the next most valued feature: 70 percent of the employers rated it one of the four salient factors that they considered when evaluating health plans. All focus-group participants expressed the belief that cost was the most influential factor in their employer's choice of plans. However, it is to be expected that agents would focus on costs. Employers could be expected to seek out plans that incorporate employee preferences at the best price, acting as value-conscious agents for their employees. Hence, it is not inappropriate for employers to be concerned about cost.

It must be pointed out, however, that although employers can act as effective agents for most of their employees, some employees may not be satisfied with the arrangement. Particularly in the case of health insurance, the structure of plans can vary widely in terms of benefit coverage, copayments, provider networks, and other aspects of coverage. Individuals who are very sick, or who have very sick dependents, may prefer different plan features and financial arrangements. However, several employers in this study commented that the reason they offered their employees a choice among health plans was because their employees had different preferences. The employers pointed out that their low-wage employees might prefer a plan with low premiums and limited out-of-pocket expenses (such as an HMO), even if it constrained provider choice, whereas professional and senior management personnel might prefer to

maintain broad provider choice, even if they had to pay more out of their own pockets. Thus, the employers acknowledged that no one plan would answer the needs of all their employees.

Although the number of firms examined for this study was small, those that we looked at were representative of companies that hire large number of employees in local markets in Cleveland and Pittsburgh. They are also likely to be representative of many large companies throughout the country. In 1998, the majority of large firms offered health insurance, and most of these companies offered more than three plans (Gabel and Hurst 1988). In addition, a national survey of companies with more than 200 employees found that 93 percent of them intervened to help their employees resolve complaints with their health plans (Henry J. Kaiser Family Foundation 1998). This is a role that the employers in our sample assumed: our focus-group participants noted that their employers often helped them to negotiate with health insurance companies.

The results of the focus groups must be interpreted against the fact that participating employees did not constitute a random sample but were employed in firms that allowed us access to them. They were employees who agreed to participate, who were not union members, and who elected to obtain their insurance through their employer, rather than turning to another source, such as a plan offered through a spouse's employer. We cannot assess the nature of the bias that may result from this selection. We do know that the participants had higher than average rates of health care use: in the past year, 19 percent reported that they or their family members had three or fewer visits, 32 percent reported four to six visits, and 49 percent reported seven or more visits. However, we would expect that people who chose to participate in focus groups about health insurance offerings might be more dissatisfied than those who refused to do so. This expectation was reinforced when many of the focus-group participants thanked the facilitator for giving them an opportunity to air their grievances. However, we believe that their views are representative of a large proportion of employees in the United States. The Employer Benefit Research Institute (EBRI) has just conducted a national survey of employees to assess their satisfaction with their current mix of health insurance benefits and wages, and to determine whether they would opt out of the employment-based insurance if given the choice (Fronstin 1999). The majority of the respondents (69 percent) were satisfied with the mix of wages and insurance benefits. Some (20 percent) preferred higher health benefits and lower wages, whereas others (8 percent)

preferred higher wages and lower health benefits. Under current tax laws, the majority (75 percent) preferred the current employment-based system to receiving higher wages and purchasing health insurance on their own. However, many indicated that if the tax laws were changed to provide full deductibility of health insurance expenses, they would prefer to take higher wages and purchase their own premiums. Nevertheless, even in this situation, most employees said they would prefer to stay in an employer-based system.

Conclusions

The evidence from this study indicates that large employers perform reasonably well as agents for their individual employees in the health insurance market. Employers do seem to provide a valued service and contribute to individual employees' welfare by purchasing their health insurance. Although the employers in this study understood their employees' preferences and provided services that were valued by their employees, it should be noted that this study was restricted to a small sample of large employers. We expect that these findings would apply to many large employers, but we do not know whether the results hold true for individuals employed by small firms. The acid test for the value of the employer as agent could be whether individual employees would be better off if they purchased their insurance plans directly, even if tax incentives were equalized. The evidence from this study, along with the results of the EBRI survey, indicates that employees do not believe they would be better off without their employer's agency. Thus, it is likely that many employees will want their employers to continue acting as their agents in the health insurance market.

However, the fact that a significant number of employers may act as good agents for their employees does not mean that this arrangement is without serious flaws. To take a simple example, a low-wage worker may prefer more wages in lieu of health benefits. Therefore, a firm that employs predominately low-wage earners may not offer any health insurance plans. In this case, the firm would be acting as a reasonable agent for the majority of the employees, but the outcome would be that many employees in that firm would be uninsured. Furthermore, the role of the employer as an agent in the health insurance market is missing entirely for unemployed and self-employed individuals. However, as policy

makers act to modify the health care system, they need to recognize the important agency role that employers play in the health insurance market and the value that many employees place on this role.

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