



Recommendations on Affordability of Health Plan Premiums

Increasing health care costs across the nation have caused health insurance premiums to rise significantly. This increase has been due to a variety of factors, including technological advances, pharmaceuticals, and an aging population. These cost-drivers of health care are often magnified by state regulation that decreases competition or stifles creativity and innovation. If this trend continues, employer-based coverage and the financial participation of employers will be eroded. Already, employers have been forced to shift increased premium expenses to employees in the form of higher cost sharing. In addition, health insurance carriers have left many unprofitable service areas and as a result, employers and individuals have a reduced choice of health insurance plans, particularly in rural areas. A variety of ideas either separately or in combination could be implemented at the federal level to address specific market issues that impact affordability of premiums. One of these ideas is the concept of state reinsurance pools.

Reinsurance Pools

Insurance carriers who operate in the small employer health insurance market currently pool similar small employers together in each of the states where they do business. Although they may be allowed some limited initial pricing flexibility based on underwriting of each small employer, and even though they are pooling many small employers together, it is often difficult to adequately spread the risk for individuals with significant health problems. The result is higher claims for the whole “pool” of small employers, which in turn results in higher premiums for all small employers.

In the individual health insurance market in the majority of states, insurance carriers can underwrite based on health status, and can decline to issue coverage on the sickest of individuals. This keeps rates affordable in the individual market, absent other regulations that impact premiums. Those who are turned down for coverage can obtain coverage in a state high-risk pool in thirty-two states, and most other states have some other mechanism to guarantee coverage to those with significant health conditions. A key element of these mechanisms is that the sickest individuals are pooled separately from those that are healthy.¹

¹ States that guarantee issue all individual health insurance policies do not pool sick individuals apart from those who are healthy, but prices are significantly higher for all individuals in those states.

HIPAA does not allow this type of high-risk pool arrangement in the small employer market, even though the small employer market shares many of the characteristics of the individual market. HIPAA does not allow individuals to be excluded from a group, or rated separately based on their individual health status. For this reason, each small employer's claims, including the claims from high-risk individuals, are included when calculating the total claims expense incurred for the whole "pool" of small employer business. This claims cost is the largest component of small employer health insurance premiums.

One way to mitigate the risk of less healthy individuals without violating HIPAA is through a small employer reinsurance pool. This is not a purchasing pool, but rather a pool set up at the state level strictly to handle the financial side of insuring high-risk individuals. Small employers purchase coverage through carriers as they normally do, but when a carrier initially underwrites a case, they purchase extra reinsurance coverage on the unhealthiest risks from a state reinsurance pool. This is transparent to the covered individual, who continues to receive benefits exactly the same as all other members of the employer group. If claims on the individual exceed a certain level, the reinsurance pool reimburses the carrier for their losses above that level. The carriers continue to retain a small part of the risk at that point, to ensure that incentives to control claims cost are retained.

Today there are nineteen active reinsurance pools, and another eleven pools that are either inactive or in the proposal stage. Reinsurance pools are currently funded by premiums paid by participating carriers. Up until this time, reinsurance pool success has been marginal in terms of its ability to produce cost savings in a given state market, primarily due to the size of current pools. The main reason for this is that the pools are largely voluntary and small. Many large carriers have decided not to participate in the pools, because they felt they were large enough to absorb more risk, or because they had already developed their own source of internal or external reinsurance. Their feeling was that they had no need to pay premiums to a reinsurance pool. So, some, but not all, carriers in a market participate in the current state reinsurance pools. For this reason, the pools have been small, with fewer participants to share in the cost of the reinsurance. As a result, savings have been less than they would have been in a larger pool, and the cost of reinsurance passed back to consumers has been greater than it would have been with more participation by more and larger carriers with more risks to reinsure.

Making participation in reinsurance pools mandatory is not the answer, and would at best only be a partial help anyway. It would appear from the premium rate increases we have seen from carriers of all sizes that the larger carriers have not been able to adequately handle the risk of unhealthy individuals in small employer groups on their own either. Because claims cost has increased, the cost of reinsurance has increased, both for carriers participating in the reinsurance pools in existence today and for larger carriers pursuing reinsurance on their own.

What is needed first is a means of enticing all players in a state small employer market to participate in the state's reinsurance pool. If all carriers participated in state reinsurance pools, more unhealthy risks would be removed from the "regular" small employer pools maintained by each carrier, and the cost of coverage would go down for small employers. However, due to the characteristics of the small employer market, even if all carriers participated in the reinsurance pool, there would still be a cost for reinsurance premiums to the carriers. This cost would be passed back to consumers. A real incentive that would significantly reduce the cost of coverage to small employers would do so by removing the cost of reinsurance premiums from carriers participating in a state's small employer reinsurance pool. Rather than a slight reduction and a rearranging of premium, this would completely remove a cost component now included in health insurance premium calculations and could significantly reduce the cost of coverage to small employers.

If the federal government subsidized small employer reinsurance pool premiums, this would remove part of the cost of coverage currently paid by small employers today. The amount of savings would depend on the amount of subsidy provided by the government. There are many degrees of unhealthy individuals. Reinsuring more of them would result in lower premiums to small employers but greater cost to the federal government. In any event, regardless of the standard set for what level of unhealthy individuals would go to the pools, the bottom line is that if there was a federal subsidy equal to the cost of a carrier's reinsurance premiums, the reinsurance costs would never trickle back to the cost of coverage paid by the small employer. This would reduce the cost of coverage to small employers, reduce the cost of the employee's share of the cost of coverage, and encourage more small employers to offer coverage to their employees.

This would seem an appropriate role for the government, and one that is consistent with other roles appropriately taken on by government. It would mean that the federal government would be subsidizing the cost of coverage for those who are sick. It would not create a new government-run bureaucracy, but merely provide financial assistance on behalf of those who most need help. The government would subsidize reinsurance premiums, but not become the reinsurer itself. It would bolster the private system, and make coverage more affordable for all small employers.

This type of system would also be fairly simple to initiate. Nineteen states already have pools that could easily be modified to work with this system. The NAIC already has a reinsurance pool model that with minor modifications would work in the scenario described and most of the pools in operation today are based on that model. Many other states with inactive models could simply activate the pools they already have "on the shelf." In fact, it is not overly ambitious to estimate that twenty-eight to thirty pools could begin this operation with the pool model they have, and that another twenty to twenty-two could adopt a modified NAIC model. With federal subsidies on the table, a state's incentive to move forward would be strong. The federal subsidies could be provided quarterly or annually to "qualified pools" based on their net losses and these

subsidies would be used to either reduce or eliminate assessments and premiums to small employer carriers participating in the pool. The federal subsidies could be disbursed through the Treasury Department, or through HHS/CMS like the high-risk pool grant money is currently being distributed.

Some Democratic candidates have suggested that reinsurance coverage only be provided to participants in government-sponsored purchasing pools. This is not necessary, would create an unlevel playing field by subsidizing only a portion of the small employer market, waste unnecessary time while the purchasing pools are developed, and create unnecessary bureaucracy on an unproven entity. Any reinsurance subsidy considered should be universal across a market segment (all small groups for example) or not used at all, otherwise ultimately access to affordable coverage could be reduced, rather than increased.

Tax Credits

It is highly recommended that a reinsurance pool concept be combined with a refundable tax credit to help low-income employees pay their share of the cost of coverage. Because small employers often can't afford to pay as much of the premium as larger employers, participation by lower income employees can be a problem. This results in adverse selection where a disproportionate number of participants with significant health conditions participate and the lower income employees in fairly good health elect not to participate due to the cost. This is a typical small employer problem and actually exacerbates the cost issue in the small employer market. Providing financial help in the form of a refundable advanceable tax credit to help them pay their share will help them afford coverage, but will also contribute to the overall health of the small employer pool by bringing more healthy individuals into the insurance pool. The credit should also be made available to individuals who don't have access to employer-sponsored coverage. The tax credit would be administered through the Treasury Department using the advancement mechanism developed for the TAA program. It would not have the purchasing option restrictions otherwise contained in TAA.

High-risk Pools

High-risk pools provide an important safety net for people with catastrophic medical conditions who do not have access to employer-based group health insurance, such as early retirees, self-employed individuals, and employees of businesses that do not offer health insurance coverage. In addition, in most states, high-risk pools serve as the guaranteed-issue purchasing option for individuals who wish to exercise their federal group-to-individual health insurance portability rights as provided by the federal Health Insurance Portability and Accountability Act of 1996. And in thirteen states, the high-risk pool also is available as a purchasing option for individuals who are eligible for the 65 percent federal health insurance tax credit provided by the federal Trade Adjustment Assistance Act of 2002. High-risk pools are an extremely important market stabilizer for

both the individual and small group markets and prevent the need to game the system to qualify for other sources of guaranteed coverage.

Continuing and increasing federal funding to state high-risk pools is highly advisable. In this discussion of the small employer market, it should be noted that many very small “groups” are actually families with one sick family member who should be individual market buyers but have instead sought group coverage because of its guarantee issue provisions. This type of adverse selection is another factor that impacts small group premiums. If adequate outlets for individuals with health conditions exist in both individual and small group markets, it won’t be necessary for these small groups to seek group coverage when the appropriate vehicle is the individual health insurance market.

On March 6, 2003, Congressman Edolphus Towns (D-NY) introduced HR1110 to expand federal funding to high-risk pools to 2009, increasing the funding each year to 75,000,000 and changing the formula from one based on the number of uninsured to one based on the number of enrollees in the pool.

On April 5, 2004, Senators Judd Gregg (R-NH) and Max Baucus (D-MT) introduced S2283, a preferable version. In addition to increasing the funding to 75,000,000 per year through 2009, it also changes the formula to one that gives 50% of the funds equally to each eligible pool, and the remaining 50% split equally based on number of uninsured and number of pool participants. Additionally, it extends the deadline for the use of seed money for the establishment of new pools, and modifies the requirement that a qualified pool be used for HIPAA eligibles to also allow a state to qualify if they have some other alternative mechanism allowable under HIPAA.

A House companion to the Gregg/Baucus bill would be very helpful. These bills generally have bipartisan support and could easily pass in 2004 with the right support.