



GEORGETOWN UNIVERSITY

Health Policy Institute

May 10, 2006

Senator Edward Kennedy
527 Hart Senate Office Building
Washington, DC 20510

Dear Senator Kennedy:

This is a response to your request for an analysis of the proposed rating structure in the Manager's Amendment to S. 1955. This also addresses your question on how the proposed amendment compares with the current NAIC model law on small group rating.

In general, the proposed Manager's Amendment would not improve the bill. Under the new proposed rating structure there would be no new protections for consumers and a significant loss of existing state-based protections in the area of premiums. This loss of protections will adversely impact people with medical needs, older workers, and women of child-bearing years. This will also have a negative impact on "micro" groups (employers with fewer than 10 employees) because insurers will be allowed to charge these groups higher rates solely on the basis of the employer's size.

Here is a brief summary of how the proposed amendment would work:

Associations

- ✓ The amendment clarifies that associations certified as small business health plans (by the U.S. Department of Labor under Title I of the bill) would enjoy a complete carve-out from small group rating state pools in both adopting and non-adopting states. Each certified association would be allowed to have their own premium rate not tied to the rest of the small group market. This would segment the small group market. Assuming associations attract healthy businesses (there are many ways that the bill would allow associations to "cherry-pick" healthy people), any restrictions on rates in the rest of the small group market would be undermined. Rates between association coverage and coverage outside the association could vary broadly. For a discussion of this, please see attached paper "Health Insurance Regulation by States and the Federal Government: A Review of Current Approaches and Proposals for Change."
- ✓ In adopting states, the bill clarifies that premiums within an association may vary using the same standards that would apply in small group market (see discussion below). This would be at least 500% variation in rates for businesses covered by the association or if the state allows, variations in rates could be even greater.

- ✓ In non-adopting states, it is unclear whether the rating standards in the bill would even apply. If they apply, then a variation in premiums of 500% would be allowed for businesses covered by an association (so some employers would pay 5 times more than others for the same coverage within an association).

Small group market

- ✓ In adopting states, insurers are required to vary rates by at least 500% (called “total variation limit”). This means that states can allow insurers to have greater variations in rates. Using age, health, claims, and duration factors, variations of at least 300% are required. Note that insurers *must* use age, health, or both and may use duration and claims experience. The option is given to insurers. If a state wants to adopt this approach and become an “adopting state,” it must allow insurers to use age and health. This requirement essentially eliminates community rating and adjusted community rating by allowing insurers to adjust rates based on health. Allowable factors included in the 500% minimum required variation are: industry, geography, group size, participation rate, class of business, and wellness programs. Note that gender is not listed. The bill is unclear whether gender rating is prohibited or is added to the 500% variation.
 - At renewal, the same rules would apply. This means that premiums may increase at least by 500% if a small business has high claims the year before.
- ✓ In non-adopting states (generally states with greater protections for consumers), the language in the bill is ambiguous. The proposal says “The plan may not vary premium rates by more than [500%].” The term “plan” is not defined. If the term “plan” means an “insurer,” then one possible interpretation is that premium variations are limited to 500% (if insurers chose to follow this new federal standard). What is clear, however, is that adjusted community rating and pure community rating would be preempted.
 - Renewal rates would limited to trend plus 15% to reflect claims of small business.

Importantly, in non-adopting states insurers would have a choice of whether to follow a state’s existing laws or the new federal one. As a way of example, in DC, which has no rating laws, assuming DC chooses not to adopt the bill’s rating structure and is therefore a non-adopting state, insurers are not likely to use the rating restrictions in the bill.

The proposed rating structure varies significantly from the NAIC model law for small business health insurance premiums. By way of background, the National Association of Insurance Commissioners (NAIC) in the early 1990’s adopted and since replaced a model law that provided for rate bands that permit premium variation up to 200 percent based on health status. The old model, which is the basis for the original bill, allowed further premium variation based on age, gender, industry, small business group size, geography, and family composition. Rates based on adjustments for these factors had to be actuarially justified but were not limited except for industry, which was limited to a 15% variation. The old NAIC model act permitted a wide variation in rates, allowing for a price difference of 26 to 1, or more.¹ This means that for the same policy an insurer could charge a business or a person \$100 per month or \$2600 per month depending on risk and other factors. Higher rates under the model would be permitted as long as there was actuarial evidence to support wider variations.

Shortly after adopting its original model with rate bands, the NAIC replaced it with a model law for small groups that requires adjusted community rating, prohibiting premium surcharges based on health or other risk characteristics (like claims experience and durational rating). The current NAIC model act limits premium surcharges based on age to 200%; it prohibits insurers from varying small group premiums based on gender of people in the group or an employer's size.ⁱⁱ Today 12 states follow the current NAIC model act. Ten states require all insurers to use community rating or adjusted community rating for all small group policies. Two others, Michigan and Pennsylvania, require Blue Cross Blue Shield plans (their largest insurers) and HMOs to use adjusted community rating. The proposed amendment would preempt these state rating protections.

Please let me know if you need additional information. Thank you for the opportunity to address your questions.

Very truly yours,

A handwritten signature in blue ink that reads "Mila Kofman". The signature is written in a cursive, flowing style.

Mila Kofman, J.D.
Associate Research Professor

ⁱ NAIC Small Employer Health Insurance Availability Model Act adopted in 1990. For information on rate variations permissible under the model, see NAIC Guidance Manual in the Evaluation of Rating Manuals and Filings Concerning Small Employer and Individual Health Insurance.

ⁱⁱ "Small Employer Health Insurance Availability Model Act" NAIC, Model #118, *Model Laws, Regulations, and Guidelines*, 118-13 (2001).