Selected Small Group Market Issues and Recommendations

Key Takeaways

- The Affordable Care Act (ACA) offers states the option of merging the individual and small group markets for the purpose of risk pooling. The Technical Advisory Group (TAG) **recommends that the small group and individual markets maintain separate risk pools at this time.** No change is required to North Carolina statute to implement this recommendation.

- The ACA requires that North Carolina's small group market be expanded to employers with 100 or fewer employees by 2016, but offers states the option of expanding the definition prior to 2016. The TAG **recommends the small group market definition remain at 50 or fewer employees until required to change in 2016.** No change is required to North Carolina statute to implement this recommendation.

- The current methodology for counting employees for the purpose of determining employer group size (small or large) under North Carolina law differs from the methodology in the ACA. The TAG **recommends that North Carolina align the methodology for determining employer group size with the ACA effective January 1, 2014**. This change should be reflected in North Carolina statute.

- North Carolina currently allows all sole proprietors to participate in the small group market, while the ACA provides that sole proprietors with no employees (or whose only employee is a spouse) are not eligible to purchase coverage through the Small Business Health Options Program (SHOP). The TAG **recommends that North Carolina's treatment of sole proprietors align with the ACA effective January 1, 2014, allowing sole proprietors with no employees to be eligible for individual but not small group market coverage.** This change should be reflected in North Carolina statute.

- The ACA requires the Exchange to provide employers the option to offer their employees multiple plans within a single metal level. The TAG **recommends that employers should not be prohibited from restricting employee choice of plans to one or more specific plan(s) within a single metal level in the SHOP Exchange.** The TAG also recommends further consideration of the extent to which the employer should be allowed to offer expanded choice. This change should be reflected in North Carolina statute.

- Federal guidance under the ACA gives Exchanges the option of establishing a uniform minimum employee participation requirement as a condition of small businesses participating in the SHOP. The TAG **recommends the establishment of a minimum participation requirement in the SHOP to mitigate adverse selection, and that the Exchange board, in consultation with the North Carolina Department of Insurance, be granted the authority to determine the SHOP participation requirement.** This change should be reflected in North Carolina statute.

Issue #1: Merging of Risk in the Individual and Small Group Markets

Under the ACA, North Carolina has the option of merging the individual and small group markets for the purpose of risk pooling. Merging the risk pools does not require insurers to participate in both markets or offer the same products, nor does it impact whether the individual and small group markets are administered as a single or separate Exchanges. Instead, merging the risk pools would require insurers to set individual and small group premium rates based on the combined claims experience of their individual and small group policies.

The primary benefit of merger is to spread risk across a larger number of subscribers, thereby reducing variation in pricing and creating greater rate stability. However, because participants in the individual market in North Carolina are expected to be less healthy, on average, than their counterparts with small group coverage, merging the two markets would have differential impacts across the two markets. In short, merger is likely to lower premiums for individuals on average, while increasing premiums for small employers.

The current variation in risk profiles is likely to decrease over time as the ACA's insurance reforms and tax subsidies are implemented. For example, the ACA mandates guaranteed issue in the individual market, which requires insurers to offer coverage to individuals irrespective of health status. The ACA also provides tax subsidies to eligible participants in the individual market, which is likely to entice healthier individuals to participate. Finally, the ACA eliminates experience rating in the individual and small group market in North Carolina. North Carolina statute currently allows insurers to rate small groups up or down by twenty-five percent based on claims experience, which reduces premiums for employers with healthier employees. These changes are likely to cause the current differences in risk (and price) between individual and small group participants to decrease over time. It is possible that as these changes occur, merger may become a more viable option.

Milliman projects that merging would prompt small group subscribers to drop coverage, ultimately reducing the number of insured in the merged market by 130,676, or 9% in 2016.[1]

Based on these considerations, the TAG recommends that the individual and small group markets remain separate risk pools at this time. In addition, the TAG recommends that the North Carolina Department of Insurance (NC DOI) revisit market merger after the ACA is fully implemented and the impact on the markets is known.

[1] Milliman, North Carolina Health Benefit Exchange Study, July 18, 2011.

Issue #2: Expanding the Definition of the Small Group Market Prior to 2016

North Carolina law currently defines small employers as businesses that have no more than 50 eligible employees.[2] The ACA requires states to define small employers as businesses with 100 or fewer employees by 2016. However, states have the option to expand the definition of small employers prior to 2016.

Expanding the definition of the small group market requires that groups of 51 to 100 employees, both in and out of the Exchange, be subjected to the same rating requirements as groups of under 50 employees, including guaranteed issue and a prohibition on experience-based rating. This will be a significant change for this market. Similar to market merger, expanding the definition of the small group market prior to 2016 will likely cause premiums to rise for healthy groups, while premiums will fall for less healthy groups. It is likely that the result would be an increase in self insurance among the healthiest groups, leading to even higher premium in the insured market.

The TAG concluded that the market should be given time to adjust to the reforms implemented in 2014 and therefore recommends that the definition of the small group market remain the same until change is required in 2016.

Issue #3: Reconciling the Methodology for Determining Employer Group Size

The ACA methodology for counting employees for the purpose of determining employer group size differs from the current methodology in North Carolina statute. While North Carolina counts each full-time person with a work week of 30 or more hours as an employee, the ACA determines the group size by averaging the total number of employees on business days during the preceding calendar year. The United States Department of Health and Human Services (HHS) has indicated that it may address the methodology for counting employees in more detail in future rule-making.

Adopting the ACA definition is likely to increase the number of countable employees for most employers. Thus, employers with just below 50 full-time employees may no longer qualify as a small group. However, most small groups have significantly fewer than 50 employees, and therefore the number of groups impacted by this change would be a small percent of the market.

The TAG recommends that North Carolina align the methodology for determining employer group size with the ACA, effective January 1, 2014 and that grandfathered groups should be protected from any adverse consequences stemming from the changed counting methodology. To the extent that the federal government offers states flexibility in counting employees, the TAG further recommends that North Carolina align its methodology with federal rules. The TAG found it desirable to have as little variation as possible in the methodology for counting employees across markets, between states for multi-state insurers, and between the state/federal definition in order to reduce complexity and administrative burden.

[2] N.C.G.S. § 58-50-110(22)

Issue# 4: Reconciling the Definition of Sole Proprietors

While North Carolina law currently permits all sole proprietors to be treated as small groups, federal regulations interpret the ACA as excluding sole proprietors with no employees other than a spouse from SHOP eligibility. North Carolina is one of eleven states that currently allows all sole proprietors to purchase small group coverage. In North Carolina this policy is driven by the desire to ensure sole proprietors are subject to guaranteed issue which currently only exists in the small group market. However, beginning in 2014, the ACA requires guaranteed issue in the individual market while excluding sole proprietors with no employees other than a spouse from SHOP eligibility. While some sole proprietors may be negatively impacted by this change (individual coverage is likely to be more expensive than small group for sole proprietors on average), TAG insurer participants observed that the number of those impacted likely will be relatively small. Insurers also noted that moving sole proprietors into the individual market could improve rates for small groups since sole proprietors who seek coverage often are less healthy.

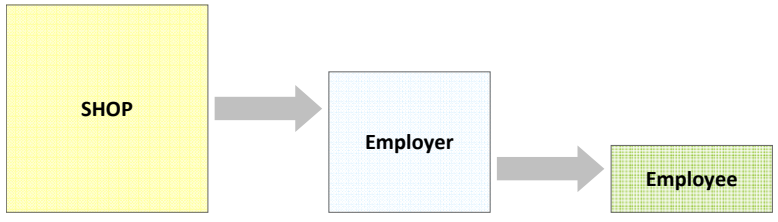
Thus, the TAG recommends that North Carolina align the sole proprietor definition with the SHOP approach, effective January 1, 2014 and that grandfathered groups should be protected from any adverse consequences stemming from the change. Similar to the previous recommendation, to the extent that the federal government offers states flexibility in the treatment of sole proprietors, the TAG further recommends that North Carolina seek to align its definition with federal rules.

Issue #5: Determining Choice in SHOP

The ACA requires that employers be offered an "employee choice" model within the SHOP. Under this model, the employer is able to pick a metal level (platinum, gold, silver, or bronze) within which employees may choose any plan offered by the SHOP. The metal level determines the average level of cost sharing required by the consumer. The ACA allows states to supplement this model with other models in which the employer offers more or fewer choices to employees. The TAG recommends that employers should be able to offer fewer choices, including offering a single plan as is common in the market today.

Currently in the small group market, employers often offer employees a single health insurance plan. The TAG considered the impact of broadening employee choice on rates. Insurers noted that the more choice granted to employees across metal levels, the greater risk of adverse selection, and the greater the need for insurers to increase premium rates to offset this effect. The TAG also discussed whether choice models that are more

Interaction between SHOP, Employer and Employees



- Must permit employers the option of offering a single benefit level
- May offer employers other options—with either more or less choice than above

- Choose among the options the SHOP offers

- Signs up for a plan based on the option the employer selected
- May have many choices or one choice

expansive than ACA requirements, but more limiting than allowing choice across all metal levels, might be effective, such as expanding employee choice to two contiguous coverage levels.

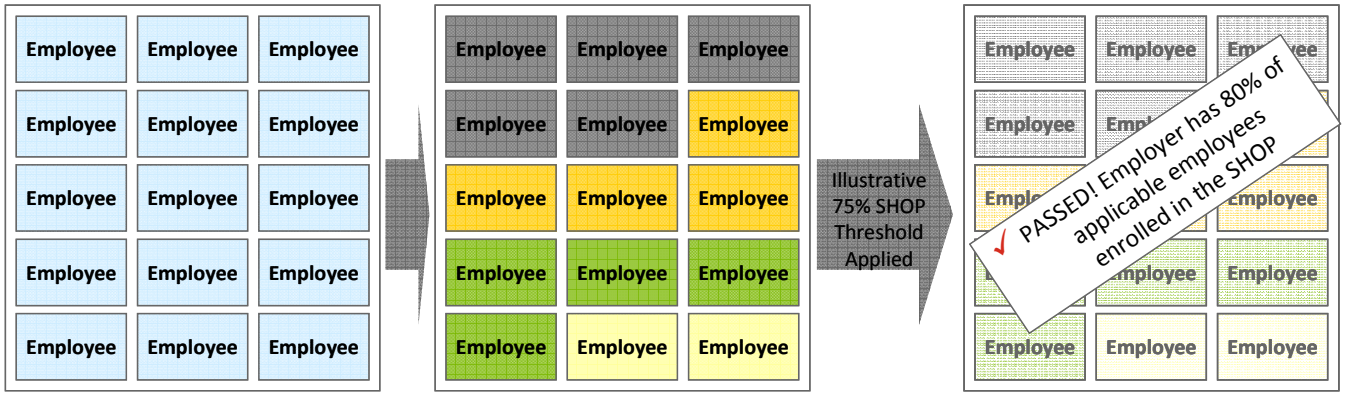
The TAG reached consensus that employers should not be prohibited from restricting employee choice of plans to one or more specific plans within a single metal level. Such an option is consistent with the ACA. It also reflects the way the market currently operates and would be seamless for employers who want to purchase coverage in the same way through the SHOP.

The TAG did not reach consensus regarding the extent to which employers should be allowed to expand choice beyond the ACA mandate, primarily due to concerns about the impact that adverse selection would have on premium costs. The TAG did not reach consensus on how much flexibility to grant the SHOP in designing employers/employee choice models versus what should be legislatively mandated. The issue of expanding employer choice may be discussed more in future TAG meetings.

Issue #6: Group Participation Requirement in the SHOP Exchange

Federal regulations issued pursuant to the ACA give Exchanges the option of establishing a uniform minimum employee participation requirement for small businesses participating in the SHOP. The minimum requirement must be the same across SHOP participating employers and be based on participation in the SHOP, not on the number of individuals enrolled in any particular plan or insurer. The number of employees participating in the SHOP generally is determined based on the number of employees without qualifying existing coverage.[3]

Example of SHOP Participation Requirement



- Small employer has 15 employees
- Purchases health insurance through the SHOP
- Gives employees the choice of a metal level

= 5 employees are covered either under Medicare, Medicaid or a spouse's plan

= 4 employees select Plan A

= 4 employees select Plan B

= 2 employees elect to not pay for coverage; take penalty

- **Since 5 employees have other coverage options, 8 out of 10 (80%) eligible employees are enrolled in SHOP**
- **Basic Plan A and Basic Plan B each have 4 out of 10 enrolled (40%)**

[3] "Qualifying existing coverage" generally means benefits or coverage provided under: (i) Medicare, Medicaid, and other government funded programs; or (ii) an employer based health insurance or health benefit arrangement, including a self insured plan, that provides benefits similar to or in excess of benefits provided under the basic health care plan.

Current North Carolina statute allows insurers to impose "reasonable employer participation" requirements on small employers applying for coverage, which may not vary based on the health benefit plan involved. This minimum participation requirement is determined on an insurer-by-insurer basis and can vary based on employer size. Insurers must follow North Carolina law when determining qualifying existing coverage, and they have the ability to refuse to issue coverage to groups or to non-renew or discontinue coverage if an employer falls below the insurer-defined participation rate.

Establishing a participation requirement in the SHOP may help mitigate adverse selection in the SHOP that could result when employers are permitted to seek coverage for only a few sick employees. However, doing so may also exclude some employers who cannot persuade a sufficient number of their employees to participate. The impact of this exclusion is at least in part mitigated by the availability of individual coverage in the Exchange. Individuals whose employers do not offer coverage due to a failure to meet participation requirements would be able to seek individual coverage and have access to subsidies, if qualified, through the Exchange.

Adverse selection could also occur between the SHOP and the small group market outside the Exchange if participation requirements are different in the two markets. For example, if SHOP participation requirements are lower than in the market outside the Exchange, employers seeking coverage inside the Exchange may tend to have employees who are sicker, on average, and adverse selection could occur.

Based on these considerations, the TAG recommends that North Carolina have an employer participation requirement in the SHOP to reduce adverse selection. The TAG concluded that the Exchange board, in consultation with the NC DOI, should be granted the authority to determine the SHOP participation requirement.

The TAG also recommends that the NC DOI actively monitor participation requirements inside and outside of the SHOP to determine whether adverse selection or other unintended consequences are occurring between the Exchange and non-Exchange markets. If the decision is made to align employer participation requirements across the SHOP and non-SHOP markets, the TAG agreed that the NC DOI is the appropriate entity to determine that participation requirement.

About the Market Reform Technical Advisory Group (TAG)

The TAG is comprised of representatives of insurers, agents, academia, hospitals, providers, business and consumers who reside in North Carolina and have knowledge of North Carolina's health care system and marketplace. The TAG considers and makes recommendations on each issue after a review of applicable State and federal laws, relevant literature, national stakeholder recommendations, and pending or passed legislation in other states.

The TAG evaluates the market reform policy options under consideration by assessing the extent to which they: expand coverage; improve affordability of coverage; provide high-value coverage options in the Exchange; empower consumers to make informed choices; support predictability for market stakeholders, competition among plans and long-term sustainability of the Exchange; support innovations in benefit design, payment and care delivery that can control costs and improve the quality of care; and facilitate improved health outcomes for North Carolinians. The TAG acknowledges that tension exists between these values and seeks to provide policy recommendations that are best aligned with the overall public interest, while ensuring the continued strength and viability of the State marketplace.

The purpose of the TAG is to develop options and considerations and to identify areas of consensus to inform the recommendations to the North Carolina General Assembly (NCGA) on ACA-related market reforms. The TAG was convened pursuant to North Carolina Session Law 2011-391, which authorized the Commissioner of Insurance to study insurance-related provisions of the ACA and any other matters it deems necessary to successful compliance with the provisions of the ACA and related regulations.

For more information on the TAG go to: http://www.ncdoi.com/lh/LH_Health_Care_Reform_ACA.aspx