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# STATE OF MINNESOTA

OFFICE OF THE COMMISSIONER

DEPARTMENT OF COMMERCE

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## THE MINNESOTA DEPARTMENT OF COMMERCE STUDY OF SMALL EMPLOYER HEALTH INSURANCE REFORM PRELIMINARY PROGRESS REPORT December 1, 1994

Pursuant to 1992 Minn. Laws Chap. 549  
— Sec. 24 1993 Minn. Laws Chap. 247 —  
Art. 2 Sec. 29

AN EQUAL OPPORTUNITY EMPLOYER

The Minnesota Department of Commerce is conducting a study of small employer health insurance reform and further rate band reductions as assigned by the legislature in Chapter 549 (1992) Article 2, Section 24. This report is the Department's preliminary progress report for the study, as required by the legislature. It includes a brief description of the study, as well as some preliminary results.

The Department's final report and recommendations are due to the legislature no later than April 1, 1995. As the results of our study may be useful to the legislature in its consideration of additional small employer market reforms during the 1995 session, such as the proposed rate band reductions, we are working to complete the study in advance of the due date. At this time, we anticipate completing the study and filing our final report and recommendations to the legislature in a January/February time frame.

APR 13 1995

### Description of the Study

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The legislature, in the 1992 Laws, has asked the Department of Commerce to study, report, and make recommendations on the following:

- the effects of Chapter 62L, the Minnesota small employer health benefit act, on the market for health benefit plans for small employers, and
- the desirability and feasibility of achieving the legislature's goal by phasing out the rate bands by July 1, 1997, according to a specified timetable.

The referenced goal of the legislature is the elimination of harmful effects in the small employer market such as substantial hardship and unfairness, unnecessary administrative costs, and adverse affects on the health of Minnesotans.

Attachment A includes Chapter 549 (1992), Article 2, Section 24.

*Chapter 62L, the Minnesota small employer health benefit act*, introduced significant reforms to Minnesota's small employer health insurance market. The major provisions of this chapter include:

- a guaranteed issue requirement,
- required offer of two defined plans (62L.05),
- elimination of coverage limitations for preexisting conditions,
- restrictions on premium rate variations from group to group ("rate bands"),
- the requirement that rates be filed and approved,
- minimum loss ratio standards, and
- creation of the Minnesota Health Care Reinsurance Association.

The Department is analyzing the effects of the Chapter 62L reforms on the number of small employer groups and members covered, the availability of coverage, affordability of and variation in premium rates, and other areas of Minnesota's small employer health insurance market. We are utilizing information and data from a variety of sources including small employer rate filings, several surveys of small employers being conducted by other Departments and private associations, and a survey of all small employer health carriers. Our "Small Employer Health Insurance Survey" has been distributed to all carriers identified as possibly having participated in the small

employer health insurance market anytime as recently as 1992. A copy of the survey is included as Attachment B.

Preliminary results suggest that the Chapter 62L reforms undertaken to date are achieving increases in coverage, access, and affordability in Minnesota's small employer health insurance market. To reiterate, the small employer reforms that have taken effect appear to be a public policy success. However, it's important to note, as the subsequent discussion points out, that some of the reforms that have not yet taken effect, principally "pure community rating", may stymie this success.

*The "rate bands"*, implemented on July 1, 1993 by the 1992 Laws Chapter 549 (1992), Article 2, Section 8 are restrictions on the variations in premium rates charged to small employers. There are two rate bands, the age rating band and the general premium rating bands. The age band limits the rate variation due to age between any two insured persons to +/- 50% of the index rate, which is a ratio of 3:1. The general premium rating band limits variation by other factors between any two groups to +/- 25% of the index rate, which is a ratio of 1.67:1. General premium variations may be based *only* on health status, claims experience, industry, and duration of coverage. In addition to the rating bands, Chapter 62L limits the variation of rates by geographic area and prohibits gender-based rating.

The result of phasing out the rate bands is "pure community rating". This is a rating method that accounts for family size, geographical area, and plan design as the only differentiating variables between employers and individuals. Under "pure community rating," rates do not vary by age, sex, or claims experience. The rates for groups with higher risk members decrease, and the rates for groups with lower risk members increase.

Chapter 625 of the 1994 Laws proposes a specified timetable of rate band reductions resulting in pure community rating on July 1, 1997. (This timetable is slightly different the specified timetable of Chapter 549 of the 1992 Laws, and is also included in Attachment A.) The proposed timetable of rate band reductions is not effective unless an effective date is specified in 1995 legislation. Our understanding is that the legislature intends to consider the advisability and feasibility of implementing the rate band reductions during the 1995 legislative session.

Our final report will include a discussion of rating practices in the small employer market, illustrations showing variations in expected costs by age and other variables, and analyses of both the impact of the current rate bands and the projected impact of phasing out the current rate bands.

### **Impact of Pure Community Rating, Preliminary Results**

As part of our study, we retained the actuarial consulting firm of Milliman & Robertson, Inc. (M&R) to model the impact of further rate band reductions on Minnesota's small employer health insurance marketplace. In addition to the rate band reductions described in Chapter 549 of the 1992 Laws, we defined several additional rating scenarios to be projected, such as the rate band reductions described in Chapter 625 of the 1994 Laws.

M&R constructed a model to project the impact of various rating limitations on the Minnesota small employer health insurance market. We have just received M&R's report and have not yet had a chance to analyze the model results nor to discuss the report with M&R. We are including

the initial results from M&R's model in this preliminary report. Further model results will be shown and explained in our final written report to the legislature.

M&R's model starts with an experience base of Minnesota small employer health insurance at June 30, 1994 and projects the market through mid-1998. The experience base was developed from enrollment and rate level data collected from six of the largest Minnesota small employer health carriers covering approximately 80% of the Minnesota small employer health insurance market. A description of M&R's model and of the requested data is included as Attachment C.

The model was used to project the impact of "pure community rating" on the Minnesota small employer health insurance market, under different scenarios including both the specified timetable of rate band reductions proposed in Chapter 625 of the 1994 Laws, and the specified timetable of rate band reductions described in Chapter 549 of the 1992 Laws.

**Under both timetables, "pure community rating" is projected to result in decreases in enrollment and increases in average premium rates.**

The total population enrolled in the size 2-29 Minnesota small employer health insurance market is projected to decline by 22% under the 1994 timetable or by 23% under the 1992 timetable. Another way to think about this statistic is that approximately 64,000 Minnesotans will have to find other coverage (self-insurance or individual policies) or go without.

A further consequence of this loss of enrollment is that the average premium rate for those remaining in the market will rise an additional 10% over and above other increases. For example, a sample group with a rate which is 20% below the current average rate (due to good experience and/or a younger group) will experience an 81% rate increase in four years. To illustrate, assume that this group has selected a benefit plan with an average monthly rate per person of \$100. The monthly rate per person currently paid by this group is thus \$80. Under "pure community rating", phased-in as proposed in the 1994 Laws, this group experiences a 37.50% rate increase above medical claim trend made up of:

- i) a 25% increase to bring the group's rate up to the current average rate of \$100, and
- ii) an additional 10% rate increase due to the increase in the average rate to \$110.

When claim trend equal to the growth limits is included, this group experiences an 81% rate increase. Assuming a January 1 renewal date, the sample group's monthly rate per person of \$80 in 1994 will rise to \$145 per person in 1998.

## Summary

Although our study is not yet complete, the preliminary work indicates that pure community rating will have an adverse impact on Minnesota's small employer health insurance market. We hope that both this preliminary information and the further analysis and results which will be included in our final report will be useful to the legislature when considering the appropriateness of the proposed phase out of the rate bands during the 1995 session.

## **Attachment A: Legislation**

### **1992 Laws, Chapter 549, Article 2, Sec. 24 [COMMISSIONER OF COMMERCE STUDY.]**

The commissioner of commerce shall study and provide a written report and recommendations to the legislature that analyze the effects of this article and future measures that the legislature could enact to achieve the purpose set forth in section 62L.01, subdivision 3. The commissioner shall study, report, and make recommendations on the following:

- (1) effects of this article on availability of coverage, average premium rates, variations in premium rates, the number of uninsured and underinsured residents of this state, the types of health benefit plans chosen by employers, and other effects on the market for health benefit plans for small employers;
- (2) the desirability and feasibility of achieving the goal stated in section 62L.01, subdivision 3, in the small employer market by means of the following timetable:
  - (i) as of July 1, 1995, a reduction of the age rating bands to 30 percent on each side of the index rate, accompanied by a proportional reduction of the general premium rating bands to 15 percent on each side of the index rate;
  - (ii) as of July 1, 1996, a reduction in the bands referenced in the preceding clause to 15 percent and 7.5 percent respectively; and
  - (iii) as of July 1, 1997, a ban on all rating bands; and
- (3) Any other aspects of the small employer market considered relevant by the commissioner.

The commissioner shall file the written report and recommendations with the legislature no later than April 1, 1995. The commissioner shall file with the legislature a written preliminary progress report no later than December 1, 1994.

### **1994 Laws, Chapter 625, Article 6, Sec. 3, Subd. 6. [LIMITS ON PREMIUM RATE VARIATIONS.]**

(a) Effective July 1, 1995, the premium variations permitted under sections 62A.65 and 62L.08 become:

- (1) for factors other than age and geography, 12.5 percent of the index rate; and
- (2) for age, 25 percent of the index rate.

(b) Effective July 1, 1996, the premium variations permitted under sections 62A.65 and 62L.08 become:

- (1) for factors other than age and geography, 7.5 percent of the index rate; and
- (2) for age, 15 percent of the index rate.

(c) Effective July 1, 1997, no health plan company shall offer, sell, issue, or renew a health plan, that is subject to section 62A.65 or 62L.08, for which the premium rate varies between covered persons on the basis of any factor other than:

- (1) for individual health plans, differences in benefits or benefit design, and for group health plans, actuarially valid differences in benefits or benefit design;
- (2) the number of persons to be covered by the health plan;
- (3) actuarially valid differences in expected costs between adults and children;
- (4) healthy lifestyle discounts authorized by statute; and
- (5) for individual health plans, geographic variations permitted under section 62A.65, and for group health plans, geographic variations permitted under section 62L.08.

### **1994 Laws, Chapter 625, Article 6, Sec. 3 Subd. 9. [CONTINGENCY; FUTURE LEGISLATION]**

This section, except for subdivision 7, paragraphs (b), (c), and (d), is not intended to be implemented prior to legislation enacted to achieve the objectives of sections 1, 5, 6, and 7. Subdivision 6 is not effective until an effective date is specified in 1995 legislation.

## **Attachment B: Small Employer Health Insurance Survey**

Small Employer  
Health Insurance Survey

Minnesota Department of Commerce  
133 East 7th Street  
St. Paul, Minnesota 55101

Complete survey & return to the above address by **September 26, 1994**. If you have any questions, contact Dorothy Petersen (612) 296-8949. Response is required pursuant to Minnesota Statute section 45.027.

Name of Health Carrier: \_\_\_\_\_

Address of Health Carrier: \_\_\_\_\_

Person Completing Survey: \_\_\_\_\_ Phone: \_\_\_\_\_

1. Please check whichever of the following applies:

- \_\_\_\_\_ A. Our company does not now and has not in the recent past (since July 1, 1992) participated in the "small employer market" as defined in Minnesota Statute section 62L.02 subdivision 27.
- \_\_\_\_\_ B. Our company has ceased (or has elected to cease, as provided under 62L.09) doing business in the Minnesota "small employer market" as of:  
(date) \_\_\_\_\_
- \_\_\_\_\_ C. Our company is currently participating in the "small employer market" as defined in Minnesota Statute section 62L.02 subdivision 27.

If the answer to Question 1 is "A", you need not complete the rest of the survey.

2. Does your company currently offer individual health plans (other than conversion plans) in Minnesota? \_\_\_\_\_
3. Please respond to the following about your Minnesota small employer business during the period July 1, 1992 to June 30, 1993 (the year prior to the effective date of Minnesota Statute chapter 62L).
- A. Number of Small Employer Groups as of June 30, 1993: \_\_\_\_\_
- B. Number of Certificate Holders (covered employees) as of June 30, 1993: \_\_\_\_\_
- C. Number of Covered Persons as of June 30, 1993: \_\_\_\_\_
- D. Total Gross Earned Premium for July 1, 1992 to December 31, 1992: \_\_\_\_\_
- E. Total Gross Earned Premium for January 1, 1993 to June 30, 1993: \_\_\_\_\_
- F. Number of Small Employer Groups as of June 30, 1993, which were new sales between July 1, 1992 and June 30, 1993: \_\_\_\_\_
4. Please respond to the following about your Minnesota small employer business during the period July 1, 1993 to June 30, 1994 (the first year under the provisions of Minnesota Statute chapter 62L).
- A. Number of Small Employer Groups as of June 30, 1994: \_\_\_\_\_
- B. Number of Certificate Holders (covered employees) as of June 30, 1994: \_\_\_\_\_
- C. Number of Covered Persons as of June 30, 1994: \_\_\_\_\_
- D. Total Gross Earned Premium for July 1, 1993 to December 31, 1993: \_\_\_\_\_
- E. Total Gross Earned Premium for January 1, 1994 to June 30, 1994: \_\_\_\_\_
- F. Number of Small Employer Groups as of June 30, 1994, which were new sales between July 1, 1993 and June 30, 1994: \_\_\_\_\_
5. Please respond to the following about small employer groups covered through an association in existence prior to July 1, 1993, with respect to small employers that were members of the association as of that date. (Note that under 62L.02 subdivision 26, these groups are not considered part of the small employer market.)
- A. Number of Small Employer Groups as of June 30, 1993: \_\_\_\_\_
- B. Number of Small Employer Groups as of June 30, 1994: \_\_\_\_\_

Where any responses represent estimates, please indicate.

## **Attachment C: M&R Model**

M&R's model starts with an experience base of Minnesota small employer health insurance at June 30, 1994. The experience base was developed from enrollment and rate level data collected from six of the largest Minnesota small employer health carriers, covering approximately 80% of the Minnesota small employer health insurance market. The following data was requested by the Department for a set of four employer size categories:

- Description of current rating methodology for insured small employer plans.
- Counts of insured small employer business by quarter of issue and by quarter of experience for 1991 through mid-1994.
- Sales of insured small employer business by quarter for 1991 through mid-1994.
- Lapses of insured small employer business by quarter for 1991 through mid-1994.
- Distributions of rate increases to insured small employers by quarter for 1991 through mid-1994, separately for the amount due to the rating bands.
- Distributions of group average rate variations due to the general premium variation, by quarter for mid-1993 through mid-1994, and separately for policies in their first policy year.
- Distributions of group average variations by level of age rate factor, by quarter for mid-1993 through mid-1994, and separately for policies in their first policy year.

The model divides the experience base of insured small employers into 1,080 cells in order to separately project the impact on each cell of phasing out the rate bands. The cells vary by number of employees, average age rating factor, and general rating factor. The model projects the rate changes, rate level, new business, lapsation and enrollment separately for each cell for each year until June 30, 1998. Each cell experiences rate increases or decreases due to the narrowing of the rate bands, and lapsation occurs that is correlated with the rate changes in the cell and the impact of premium subsidization among groups. In general, the groups lapsing from the market are lower cost groups which experience rate increases due to the rate bands. The lapsation thus results in an upward adjustment of the index rates to correspond to the change in average cost of the remaining total population in all cells. Upward adjustment of the index rates then results in additional lapsation.

For each year from mid-1993 through mid-1998 the model projects the following characteristics for the Minnesota small employer health insurance market: (1) average rate level in the market based on the changes in index rates, (2) the enrollment in the market based on the total of the enrollments in each cell, and (3) the distribution of rate changes (resulting from phasing out the rating bands) based on the rate change in each cell.