



# EXPANDING THE RISK ADJUSTER

## Managing Risk to Stabilize the Small Group Market

A Utah Health Policy Project Fact Sheet

September 2009

### SUMMARY

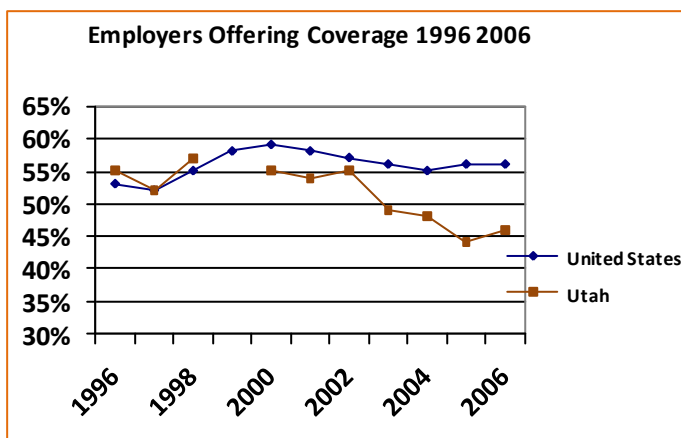
Enacted in 2009, HB188 (Health System Reform – Insurance Market) created a new defined contribution market, a cornerstone of Utah’s health system reforms. To stabilize costs and ensure the long term sustainability of the new market HB188 also created a risk adjuster to spread risk more efficiently across all insurers. Yet this mechanism is currently limited in its scope – to the ‘Exchange’ market – when in reality it could be instrumental in helping *all* small employers maintain their investment in health benefits.

It is no secret that Utah’s small businesses are struggling to provide health care coverage. A recent survey of Utah small businesses reported that 88% of the small businesses not offering health insurance say they can’t afford to, while 79% of those who *do* offer it say they are really struggling to do so.<sup>i</sup> Small businesses lack the buying power of big employers, so they pay more for health benefits than they can handle. Worst of all, they are unable to plan from year to year because premium increases are so unpredictable. If one employee becomes sick or has an accident, a small employer can be completely priced out of the health insurance market.

**If Utah’s objective is to stabilize the private market so it functions as the main platform for reforms, then the risk adjuster created in HB188 must be expanded to the entire small group market.**

### BACKGROUND

Over the past decade the number of Utah employers offering health insurance *decreased by almost 9%*, with the bulk of cuts coming from small business.<sup>ii</sup>



### PROMISING PRACTICES

*New Jersey* is looking at a reinsurance mechanism to manage risk within a new combined small and non-group market. Actuarial estimates show that 5,000 more people would be able to obtain insurance if the proposed program is implemented.

*Washington* passed legislation last year to design a reinsurance program for its small and non-group markets.

Created in 1990, *Connecticut’s* nonprofit Small Employer Health Reinsurance Pool has been successful in at least two ways:

1. stimulating market competition by ensuring that small insurers can compete in the market
2. allowing businesses to continue providing benefits by making premiums affordable.

All health plans in Connecticut must participate in the program, but each plan decides whether it or the pool will take on the risk for the person or the group. Premiums are then paid by the insurer on individuals or groups that will be reinsured.

Created in 2001, *Healthy New York* is a government subsidized HMO program for small businesses, sole proprietors, and previously uninsured low-wage individuals. By setting an appropriate *attachment point* (point in claims costs where reinsurance kicks in), insurers have been able to **lower premiums by 17%**. Funds are collected through assessments on premiums and other state funds.

With the main focus of Utah’s reform efforts on the private market, **our top priority must be to slow the erosion of small business health care coverage.** One proven way to do this is through a risk adjustment mechanism, such as reinsurance. Given that most of the erosion of small business coverage is linked to difficulties around affordability, reforms must include proven methods for managing risk. One accident or sick employee in a given year can cause small businesses premiums to rise by as much as 25%.<sup>iii</sup> In Utah, premiums for employer-sponsored health insurance increased 74% for families and 50% for individuals from 1996 to 2006.<sup>iv</sup> This trend is unsustainable, especially in the current economic climate. **By stabilizing premium increases through a reinsurance mechanism, small businesses will be able to plan for their health care costs.**

## WHY INCLUDE THE ENTIRE SMALL GROUP MARKET?

While a risk adjuster is currently being developed for the defined contribution market, its main function is to stabilize risk for insurers, not the participating businesses. Further, the pool is limited to the defined contribution market. **Yet to most effectively spread risk and avoid adverse selection, the risk adjuster must be extended as far as possible.<sup>v</sup>**

States with reinsurance pools use them to manage risk not only for health insurance companies, but for individuals with pre-existing health conditions and groups with high-risk individuals. **According to the Heritage Foundation, reinsurance can facilitate comprehensive reforms by creating a smoother-functioning health insurance market.<sup>vi</sup>**

**A reinsurance mechanism that includes the entire small group market, inside and outside the Exchange, will curb the significant spikes in premiums that force small businesses to drop or reduce coverage.** Currently a small percentage of the population utilizes the majority of health care dollars. Only 3% of the population uses half of the health care dollars, and 13% use almost 80% of the dollars (*see table at right*). All it takes is one high cost claimant to price a small group right out of the market. Yet, if these high costs are spread over a larger group, then one high claim will not have such a significant impact.

**Including the entire small group market both inside and outside the Exchange will help small business plan for future increases and thus stabilize the private market.**

Claims	Members	%	Dollars	%
Over \$100,000	204	.11%	\$53,200,000	11%
Over \$50,000	445	.24%	\$48,400,000	10%
Over \$25,000	1,112	.6%	\$59,000,000	12.2%
Over 10,000	3,670	1.98%	\$84,600,000	17.5%
Over \$5,000	7,266	3.92%	\$79,800,000	16.5%
Over \$2,500	10,714	5.78%	\$58,500,000	12.1%
Less than \$2,500	161,948	87.37%	\$100,100,000	20.7%
<b>TOTAL:</b>	<b>185,359</b>	<b>100%</b>	<b>\$483,600,000</b>	<b>100%</b>

*\*Public Employee Health Plan, Twelve Month Claims Distribution June 2008.*

## CONCLUSION

As Utah moves to a consumer-centered health insurance market where consumers and small groups are given a broad choice of health plans, it will be essential to create a robust risk adjuster. Reinsurance pools have been successfully implemented in many states to stabilize the private market by leveling the playing field for insurers so they can focus on managing wellness. **Protect small businesses and strengthen the foundation for a consumer-driven market by expanding the reinsurance mechanism within the risk adjuster to the entire small group market.**

<sup>i</sup> Small Business Majority, *Utah Small Business Healthcare Survey*. July 2009.

<sup>ii</sup> Medical Expenditure Panel Survey, 1996-2006.

<sup>iii</sup> *How are Insurance Rates Regulated? A Guide to Underwriting Laws in Utah & Policy Recommendations*. Utah Health Policy Project Issue Brief, January 2009.

<sup>iv</sup> *At the Brink: Trends in America's Uninsured*, Robert Wood Johnson Foundation and State Health Access Data Assistance Center, March 2009.

<sup>v</sup> Haislmaier, Edmund F. *State Health Care Reform: A Brief Guide to Risk Adjustment in Consumer-Driven Health Insurance Markets*. Heritage Foundation, No. 2166, August 1, 2008.

<sup>vi</sup> Haislmaier, Edmund F., *State Health Care Reform: The Benefits and Limits of "Reinsurance"*. Heritage Foundation WebMemo No. 1568, July 26, 2007.