Virginia Health Reform Initiative

Virginia Health Insurance Market Overview and Adverse Selection Risk in the Exchange

July 15, 2011
Agenda

• Virginia Health Insurance Market Characteristics
• Actuarial Value
• Adverse Selection Risk
• Exchange Development and Market Structure/Regulation
• Key Structural Decisions
• PPACA Exchange Characteristics impacting Adverse Selection
• Policy Options for Minimizing Adverse Selection
• Insurance Rating Options
• Region Definitions and Market Rules
• Risk Adjustment
Virginia Market Characteristics

BOI data call

• Request from the Virginia BOI to health insurers operating in the Commonwealth

• Information requested included:
  - For each market segment:
    - enrollment
    - total premium revenue
    - average premiums
    - average member age
  - Additionally, for their top selling benefit plans:
    - benefit description
    - average premiums
    - standard single premiums
    - risk loads
    - denial rates (Individual plans)
Virginia Market Characteristics
BOI data call results

• Responses received from nearly all of insurers offering health coverage in the Individual and Small Group markets
  - 11 health plans offering Individual coverage
  - 12 health plans offering Small Group coverage

• Market share is highly concentrated in a few plans
  - Individual market: one health plan has over 3/4 of enrollees, top five health plans have over 95% of enrollees
  - Small Group market: one health plan has over 1/3 of enrollees, top five health plans have nearly 85% of enrollees
### Virginia Market Characteristics

**BOI data call results**

<table>
<thead>
<tr>
<th></th>
<th>Individual</th>
<th>Small Group (2-50)</th>
<th>Small Group (51-100)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Avg monthly subscribers</td>
<td>190,276</td>
<td>247,868</td>
<td>86,774</td>
</tr>
<tr>
<td>Avg monthly members</td>
<td>302,791</td>
<td>443,121</td>
<td>162,692</td>
</tr>
<tr>
<td>Avg members per subscriber</td>
<td>1.59</td>
<td>1.79</td>
<td>1.87</td>
</tr>
<tr>
<td>Avg monthly premium per</td>
<td>$226</td>
<td>$345</td>
<td>$313</td>
</tr>
<tr>
<td>member</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total premium</td>
<td>$821,051,851</td>
<td>$1,834,662,279</td>
<td>$611,625,808</td>
</tr>
<tr>
<td>Avg member age</td>
<td>34.0</td>
<td>35.8</td>
<td>33.9</td>
</tr>
</tbody>
</table>

- For Individual plans, reported application denial rates due to health status range from 7% to nearly 30%
Virginia Market Characteristics
Range of deductibles in top selling benefit plans

- Health plans were asked to provide info on up to 5 of their top selling benefit plans in each market segment

<table>
<thead>
<tr>
<th>In-network Medical Deductible</th>
<th>Individual</th>
<th>Small Group (2-50)</th>
</tr>
</thead>
<tbody>
<tr>
<td>$0</td>
<td>5%</td>
<td>60%</td>
</tr>
<tr>
<td>$100</td>
<td>2%</td>
<td>0%</td>
</tr>
<tr>
<td>$250-$500</td>
<td>14%</td>
<td>10%</td>
</tr>
<tr>
<td>$750-$1,200</td>
<td>7%</td>
<td>18%</td>
</tr>
<tr>
<td>$1,500-$1,750</td>
<td>0%</td>
<td>11%</td>
</tr>
<tr>
<td>$2,000-$2,500</td>
<td>62%</td>
<td>2%</td>
</tr>
<tr>
<td>$2,700-$3,750</td>
<td>1%</td>
<td>0%</td>
</tr>
<tr>
<td>$5,000-$10,000</td>
<td>8%</td>
<td>0%</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>Member-weighted Average Deductible</td>
<td>$2,161</td>
<td>$539</td>
</tr>
</tbody>
</table>
Virginia Market Characteristics
Single premiums of Individual plans in the market

<table>
<thead>
<tr>
<th>Age Band</th>
<th>Region 1</th>
<th>Region 2</th>
<th>Region 3</th>
<th>Region 4</th>
<th>Region 5</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Avg</td>
<td>Min</td>
<td>Max</td>
<td>Avg</td>
<td>Min</td>
</tr>
<tr>
<td>Child</td>
<td>$135</td>
<td>$60</td>
<td>$241</td>
<td>$132</td>
<td>$59</td>
</tr>
<tr>
<td>19-30</td>
<td>$148</td>
<td>$59</td>
<td>$310</td>
<td>$135</td>
<td>$75</td>
</tr>
<tr>
<td>31-40</td>
<td>$189</td>
<td>$79</td>
<td>$381</td>
<td>$175</td>
<td>$93</td>
</tr>
<tr>
<td>41-50</td>
<td>$246</td>
<td>$108</td>
<td>$537</td>
<td>$220</td>
<td>$122</td>
</tr>
<tr>
<td>51-60</td>
<td>$354</td>
<td>$158</td>
<td>$840</td>
<td>$307</td>
<td>$166</td>
</tr>
<tr>
<td>61-65</td>
<td>$470</td>
<td>$194</td>
<td>$1,168</td>
<td>$395</td>
<td>$203</td>
</tr>
</tbody>
</table>

- Nine companies with significant enrollment in Region 1, three in Regions 2 and 3, two in Regions 4 and 5
- Age-based premium ratios ranged from 2.7:1 to 7.0:1, most are well above 3:1
**Virginia Market Characteristics**

Single premiums of Small Group plans in the market

<table>
<thead>
<tr>
<th>Age Band</th>
<th>Region 1</th>
<th>Region 2</th>
<th>Region 3</th>
<th>Region 4</th>
<th>Region 5</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Avg</td>
<td>Min</td>
<td>Max</td>
<td>Avg</td>
<td>Min</td>
</tr>
<tr>
<td>Child</td>
<td>$231</td>
<td>$143</td>
<td>$536</td>
<td>$242</td>
<td>$140</td>
</tr>
<tr>
<td>19-30</td>
<td>$283</td>
<td>$208</td>
<td>$675</td>
<td>$300</td>
<td>$206</td>
</tr>
<tr>
<td>31-40</td>
<td>$392</td>
<td>$275</td>
<td>$822</td>
<td>$396</td>
<td>$272</td>
</tr>
<tr>
<td>41-50</td>
<td>$612</td>
<td>$411</td>
<td>$1,243</td>
<td>$613</td>
<td>$403</td>
</tr>
<tr>
<td>51-60</td>
<td>$844</td>
<td>$514</td>
<td>$1,695</td>
<td>$839</td>
<td>$504</td>
</tr>
</tbody>
</table>

- Nine companies with significant enrollment in Region 1, five in Region 2, seven in Regions 3 and 4, and six in Region 5
- Age-based premium ratios ranged from 3.1:1 to 6.6:1
Virginia Market Characteristics
Underwriting risk rating

<table>
<thead>
<tr>
<th>Risk Rating</th>
<th>Percent of Members</th>
<th>Individual</th>
<th>Small Group (2-50)</th>
</tr>
</thead>
<tbody>
<tr>
<td>&lt; 0.90</td>
<td>0.4%</td>
<td>40.8%</td>
<td></td>
</tr>
<tr>
<td>0.90 - 0.95</td>
<td>0.5%</td>
<td>12.1%</td>
<td></td>
</tr>
<tr>
<td>0.95 - 1.00</td>
<td>45.8%</td>
<td>9.8%</td>
<td></td>
</tr>
<tr>
<td>1.00 - 1.05</td>
<td>24.4%</td>
<td>15.7%</td>
<td></td>
</tr>
<tr>
<td>1.05 - 1.10</td>
<td>0.9%</td>
<td>4.9%</td>
<td></td>
</tr>
<tr>
<td>1.10 - 1.20</td>
<td>0.3%</td>
<td>6.7%</td>
<td></td>
</tr>
<tr>
<td>1.20 - 1.35</td>
<td>15.5%</td>
<td>5.2%</td>
<td></td>
</tr>
<tr>
<td>1.35 - 1.50</td>
<td>0.2%</td>
<td>2.8%</td>
<td></td>
</tr>
<tr>
<td>1.50 - 1.75</td>
<td>7.0%</td>
<td>1.3%</td>
<td></td>
</tr>
<tr>
<td>1.75 - 2.0</td>
<td>0.0%</td>
<td>0.7%</td>
<td></td>
</tr>
<tr>
<td>&gt; 2.0</td>
<td>4.9%</td>
<td>0.2%</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>100.0%</td>
<td>100.0%</td>
<td></td>
</tr>
</tbody>
</table>

- Risk rating is applied as an adjustment to the Standard rates
## Virginia Market Characteristics
Actuarial values of plans being sold today

<table>
<thead>
<tr>
<th>Actuarial Value</th>
<th>Member Distribution</th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Individual</td>
<td>Small Group (2-50)</td>
<td>Small Group (51-100)</td>
</tr>
<tr>
<td>40%-49.9%</td>
<td>1%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>50%-59.9%</td>
<td>38%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>60%-64.9%</td>
<td>30%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>65%-69.9%</td>
<td>3%</td>
<td>0%</td>
<td>0%</td>
</tr>
<tr>
<td>70%-74.9%</td>
<td>4%</td>
<td>6%</td>
<td>5%</td>
</tr>
<tr>
<td>75%-79.9%</td>
<td>17%</td>
<td>15%</td>
<td>10%</td>
</tr>
<tr>
<td>80%-84.9%</td>
<td>2%</td>
<td>55%</td>
<td>45%</td>
</tr>
<tr>
<td>85%-89.9%</td>
<td>6%</td>
<td>11%</td>
<td>9%</td>
</tr>
<tr>
<td>90%-94.9%</td>
<td>0%</td>
<td>9%</td>
<td>16%</td>
</tr>
<tr>
<td>95%-100%</td>
<td>0%</td>
<td>5%</td>
<td>14%</td>
</tr>
<tr>
<td>Total</td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
<tr>
<td>Average AV</td>
<td>65%</td>
<td>84%</td>
<td>86%</td>
</tr>
</tbody>
</table>
Actuarial values and PPACA

- PPACA defines minimum benefits and benefit levels based on actuarial value

<table>
<thead>
<tr>
<th>Benefit Level</th>
<th>Actuarial Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Platinum</td>
<td>90%</td>
</tr>
<tr>
<td>Gold</td>
<td>80%</td>
</tr>
<tr>
<td>Silver</td>
<td>70%</td>
</tr>
<tr>
<td>Bronze</td>
<td>60%</td>
</tr>
</tbody>
</table>

- Can be achieved through a wide range of possible cost sharing and benefit exclusion combinations, subject to essential benefit requirements
Actuarial Value and Actuarial Equivalence

• Definition of actuarial value:
  1. the **dollar value** of average benefits expected to be paid by the plan, or
  2. the **average share** of covered medical costs paid for by the health plan (PPACA uses this definition)
     ◦ AV under this definition does not reflect benefit exclusions, but
       PPACA essential benefits coverage must be considered
     ◦ Actuarial value allows broad comparisons of benefit plans but is not
       very helpful to individual consumers due to reliance on averages

• Benefit plans with the same actuarial value are “actuarially equivalent” but . . .
  - AE benefit plans will probably have different premiums
  - AE plans may cover different benefits or impose different limitations or cost sharing on specific benefits. Essential benefits coverage requirements will help limit differences.
Adverse Selection

- Adverse selection occurs when insurance pools become skewed towards those with high expected claims
  - Caused by the tendency for people to act in their own best interest when presented with coverage options
  - Increases costs for everyone in the pool

- If plans outside the exchange operate under different rules, healthy individuals and groups may purchase lower cost plans outside of the exchange and the exchange may evolve into a high risk pool that is unattractive to insurers and unaffordable for enrollees

- Risk adjustment is a tool that is used to correct for selection differences among health plans and benefit plans. PPACA also includes provisions for temporary risk corridors and individual market reinsurance.
Exchange development and market regulation/structure

• Development of exchanges must be done with consideration of broader insurance market regulation
• Differences between the exchange and external market will drive adverse selection
• The structure of the entire individual and small group market should be considered in the design of the exchange
Key Structural Decisions

Key structural decisions

• Should the state create separate or combined Individual and Small Business Health Options Program (SHOP) exchanges?

• Will external markets be permitted for individual and/or small group?

• What design elements and regulatory measures should be used to protect the exchange from insurance market risks such as adverse selection?
Characteristics of PPACA that could drive Adverse Selection

• Location of subsidies
  - Subsidies only available through exchange

• Initial entry from Temporary Federal High Risk Pool
  - In 2014, TFHRP ends and enrollees may enter the exchange

• Individual market reinsurance and risk corridors in early years are intended to mitigate these risks
Characteristics of PPACA that could drive Adverse Selection

• “Grandfathered” and self-insured plans may remain outside the exchange
  - Likely to have lower costs, but not likely to have significant impact
  - If larger groups join the exchange, impact will be greater

• Opportunity to offer less rich benefit plans outside the Exchange
  - Health plans participating in exchange must offer “Silver” and “Gold” coverage
  - Unless restricted, health plans outside exchange could drive adverse risk to the exchange by only offering “Bronze” coverage
Characteristics of PPACA that could reduce Adverse Selection

• PPACA requires common benefit designs in/out of exchange
  - Bronze, Silver, Gold, Platinum plans based on actuarial value
  - All plans must cover same minimum range of “Essential Benefits”
  - Same restrictions on annual/lifetime benefit limits
  - But variations in benefit coverage may still be allowable which could increase adverse selection risk
**Characteristics of PPACA that could reduce Adverse Selection**

- PPACA requires common pricing for same benefit design in/out of exchange
  - Same benefit designs at the same premium rate for a demographically similar population
  - Enrollee should not face a premium price difference, regardless of where the policy is purchased
  - But could a slightly different benefit design be offered at a very different price outside the exchange?
Characteristics of PPACA that could reduce Adverse Selection

• Prohibited in both markets:
  - Medical underwriting
  - Limiting coverage for people with pre-existing conditions
  - Rating for differences in health status
    ◦ Exceptions: tobacco use, wellness program participation

• Same basic market rules (GI, min LR, prices same in/out of Exchange)

• Same allowable premium variations:
  - Age (max 3:1 ratio)  - Individual v. Family
  - Geography  - Tobacco use (max 1.5:1 ratio)
  - Wellness program participation (max 30% discount)
Characteristics of PPACA that could reduce Adverse Selection

• Subsidies available only in the exchange, so low risk individuals seeking a subsidy will prefer the exchange

• Risk adjustment for all plans inside/outside exchange

• Risk pooling across health plan’s products offered inside/outside exchange
Policy Options for Minimizing Adverse Selection

Limit Open Enrollment Periods

• Advantages
  - Effective in reducing adverse selection driven by delaying purchase of insurance until needed
  - Easy to administer

• Disadvantages
  - Limited access to coverage if unexpected need arises
Policy Options for Minimizing Adverse Selection

Require exchange participation for a certain period of time

• Advantages
  - Reduces anti-selective behavior
  - Improves stability (reduces “churning”)

• Disadvantages
  - May be significant disincentive, especially during initial months
  - Difficult to enforce
Policy Options for Minimizing Adverse Selection

Limit ability to return to the exchange

• Advantages
  - Easy to administer

• Disadvantages
  - Difficult to enforce
  - Unfairly penalizes employees for their employer’s decisions
  - Higher premiums for returning individuals may not comply with PPACA rules
Policy Options for Minimizing Adverse Selection

Require minimum contribution and participation

• Advantages
  - Effectiveness

• Disadvantages
  - Contribution/participation rates need to be verified \(\rightarrow\) increase admin
  - Relatively high participation requirements to impact risk
  - Subsidies/tax credits may not be enough for affordability
  - Entire employer groups may be discouraged from participation
Policy Options for Minimizing Adverse Selection

**Limit coverage choices**

- **Advantages**
  - Encourages enrollees to consider long-term insurance needs and assess tradeoffs between higher cost-sharing and lower premiums

- **Disadvantages**
  - Does not consider changes in an individual’s circumstances
Policy Options for Minimizing Adverse Selection

Limit employer size to minimum allowed
✓ 2016: PPACA option to include groups of 51-100 employees
✓ 2017: PPACA option to include larger groups

• Advantages
  - Reduces the risk of adverse selection due to grandfathered and self-insured groups
  - Insurers not required to pool large groups for risk adjustment so this limitation reduces adverse selection risk

• Disadvantages
  - Reduces market power of exchange
  - Self-insured plans tend to be lower-risk groups
Policy Options for Minimizing Adverse Selection

Offer Individual/Small Group products only through exchange

• Advantages
  - Eliminates adverse selection between exchange/external market
  - Consumers have same choices and protections
  - Creates larger pool, with leveraging/purchasing power
  - Ability to standardize benefit design across product tiers
  - Simplified data collection/monitoring, improved trend/risk adjustment
  - Possible: improved negotiating power over provider payments, lower admin costs

• Disadvantages
  - Limits plan choice, constrains flexibility/innovation
  - Eliminates alternatives for grandfathered/self-insured plan enrollees
  - Undocumented immigrants may not be able to get coverage (PPACA prohibits from joining exchange)
Policy Options for Minimizing Adverse Selection

Retain two markets (in/out of exchange), with identical market rules

• Advantages
  - Greater consumer plan choice
  - Greater flexibility/innovation
  - Accommodates local/regional health plans
  - Provides options for grandfathered / self-insured / undocumented
  - Reduces potential for adverse selection

• Disadvantages
  - Less leverage/purchasing power
  - Reduced data collection/monitoring (effects quality of trend, risk adjustment)
  - Possible: higher administrative costs
Policy Options for Minimizing Adverse Selection

Require all licensed plans to sell in the Individual/Small Group market to offer Silver and Gold policies

- **Risk**
  - For low risk individuals, Bronze plans may be attractive due to lower premium
  - Insurers operating outside the exchange may choose to sell only lower value policies to attract preferred risks

- **Option**
  - Require all licensed health plans to offer policies at each tier level offered in the exchange, so there is no natural advantage to plans operating only outside of the exchange
Insurance Rating Options

• Age variation
  - Age-related healthcare cost variation generally exceeds allowed 3:1 premium ratio
  - Use of a narrower ratio will increase subsidization of older participants by younger participants
    ◦ Discourages younger individuals from enrolling
    ◦ Increases costs for the entire pool

• Individual v. Family Coverage
  - Since family size cannot be considered, there is increased risk from incorrect average family size assumptions
  - Consider establishing standardized individual/family premium ratio to minimize adverse selection
**Insurance Rating Options**

- **Tobacco use**
  - Difficult verifying whether an individual is not a tobacco user (typically self-reported)

- **Wellness program participation**
  - Benefits yet to be fully validated
    - Potential of reduced costs due to improved participant health
    - Potential positive selection effects from discounts
  - Requires documentation; verification difficult
  - May support Virginia’s long term health policy goals, regardless of whether there is an immediate cost impact
Region Definitions and Market Rules

Rating region definitions, network coverage and participation rules within regions can help address differential pricing and selection

- **Advantages of strict regional definitions**
  - Prevent manipulation of coverage areas for favorable selection
  - Clearly defines health plan competition and networks

- **Disadvantages of strict regional definitions**
  - May shut small/local plans out of individual and small group markets
  - Difficulty negotiating contracts with additional providers
  - Reduced competition; smaller plans may exit the market
Risk Adjustment

• PPACA: to mitigate risk differences among health plans participating in the exchange and between plans operating in and out of the exchange

• Risk adjustment design decisions likely left to states with guidance from HHS

• Decisions
  - Risk adjustment model or models to use
  - Risk measurement and risk adjustment periods
  - Level at which risk adjustment is applied (e.g., between Individual and Small Group, between benefit tiers)
  - Individual v. Group risk measurement
  - Implementation and phase-in timeline
Discussion