To: Senate Finance Committee

From: Phil Keller, Director of Insurance Regulation,
Department of Financial Regulation

Re: Summary of 3/20/18 testimony re Regulation 2009-02

I'd like to address very briefly the two questions the Committee chair posed about the Department's revisions to Regulation H-2009-2: (1) why the change and (2) what it does.

To answer the first question, in 2016 the Legislative Committee on Rules approved several changes to Rule 2009-2, which had already been in effect for seven years. One of the changes approved by the Committee was to conform the definition of small employer to the expanded definition of "small employer" in 33 V.S.A. 1811 that became effective on January 1, 2016. This meant changing the definition of "small employer" from an entity that employs a maximum of 50 employees to an entity that employs a maximum of 100 employees.

A second change approved by LCAR was to increase the minimum attachment points in the regulation to keep pace with medical inflation. Attachment points are dollar thresholds that limit an employer's financial responsibility for unexpectedly large claims.

The 2016 revision increased the aggregate annual attachment point for small employers from the greater of 120 percent of expected claims or $4,000 times the number of covered lives, which was the aggregate attachment point in the original 2009 regulation, to the greater of 120% of expected claims or $5,700 times the number of employees.

This 2016 revision proved to be problematic in practice, because for a small group of employers, especially employers with a young workforce and few dependents, the "$5,700 prong" has the effect of increasing the employer's aggregate attachment point to as much as 200 percent of expected claims, or even higher.

To give you a quick example, say you have a small employer with 50 employees, all of whom are relatively young. Say their expected health care claims for the year are $2,500 per employee or $125,000 for the entire group. If the employer's aggregate attachment point is

120% of expected claims, the employer will be on the hook for $150,000 in claims before its stop loss policy kicks in to protect it.

But if the employer's aggregate attachment point is "$5,700 times the number of employees", it will be on the hook for $285,000 in claims before its stop-loss insurance kicks in. It will, thus, be assuming almost twice the financial exposure that it would have at 120 per cent of expected claims.

That increased claims exposure is enough to force some small employers, especially ones with younger workforces and low profit margins, to drop their self-funded health plans. It means that they are going from bearing a majority of their employees' claims risk, as they do at the 120 percent threshold, to almost all of it.

We heard from a number of small employers that the ability to offer a self-insured plan was an important way to compete for and retain employees. But we also heard that they wouldn't be able to offer such plans if they had to shoulder almost all of the claims risk themselves.

That's the answer to why the change. To address the problem, we've eliminated the "$5,700 times the number of employees" prong and made the annual aggregate attachment point simply 120% of expected claims for all small employers, as it is in most states that regulate stop loss insurance. For large employers, the annual aggregate attachment point remains 110% of expected claims, as it always has been.

According to the actuarial study we conducted, if the aggregate attachment point is simplified to 120 percent of expected claims, the average small employer will still retain about 64% of its own claims risk, which is what the stop loss regulation is intended to accomplish. The regulation is intended to make self-funding a real financial commitment by the employer, but not to make it impossible.

We also asked our actuaries to look at whether making this change would have a negative impact on premiums on Vermont Health Connect. Their conclusion was that because the $5,700 prong had a negative impact on only a small number of employers, the number of healthy employees that would migrate to the exchange from groups that dropped coverage would be minimal and would affect rates on the exchange by less than 0.1 percent.

Finally, it's important to note that if the definition of small employer in the regulation is changed back to what it was prior to 2016, i.e., an entity with 1-50 employees, employers with 51-100 employees would go back to being considered a large group. This means that they would subject to an annual aggregate attachment point of 110% of expected claims, rather than the 120% attachment point contained in the proposed revision. Changing the definition of "small employer" back to what it was prior to 2016 would make it easier for entities with 51-100 employees to self-insure by reducing the amount of risk they are required to retain. By making self-insurance easier, such a change would thus actually increase the incentive for employers in that group to leave the Exchange and take their good risks with them.