The Changing Regulatory Landscape for Stop Loss Insurance

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EDITORIAL NOTE: Commentary offered by the authors does not necessarily represent the views of SIIA.

Recent developments at the federal and state levels of government, taken together, portend changes in the regulation of stop loss insurance, which could lead more and more small and mid-size firms to self-insure than ever before. Although neither state nor federal officials keep comprehensive statistics on self-insurance, it appears to be growing in popularity as a feasible option. A recent study by the Employee Benefits Research institute indicates that nearly 60% of private sector workers were in self-insured health plans in 2011, up from approximately 40% in 1998 and 1999.

Background

Although stop loss insurance is not addressed in the Patient Protection and Affordable Care Act of 2010 (the "Affordable Care Act or "ACA"), the National Association of Insurance Commissioners ("NAIC") recently reviewed proposed action with regard to the regulation of stop loss insurance. The NAIC adopted a Stop Loss Insurance Model Act (#92) (the "Model Act") in 1995, which was amended in 1999 to clarify that the law applied only to insurers and did not impose obligations on employer benefit plans directly. In essence, the Model Act provides certain minimum standards for stop loss insurance coverage. Specifically, it prohibits an insurer from issuing a stop loss insurance policy that has an annual attachment point for claims incurred per individual which is lower than $20,000; has an annual aggregate attachment point (for groups of fifty or fewer) that is lower than the greater of:

1. $4,000 times the number of group members
2. 120 percent of expected claims or
3. $20,000;

has an annual aggregate attachment point for groups of fifty or more that is lower than 120 percent of expected claims; or provides direct coverage of health care expenses for an individual. These minimum standards ensure that the plan sponsor

retains some of the risk in providing health benefits to its employees, rather than transferring all or most of the risk to a stop loss insurer.

The Model Act was only adopted in its entirety by three states (Minnesota, New Hampshire, and Vermont). Other states have adopted certain parts of the Model Law only, or have chosen to regulate stop loss insurance through other ways. For example, New York and Oregon have banned stop-loss insurance for any firms with fewer than fifty workers. Many other states have standards similar to those in the Model Act, but allow attachment points below $20,000.

So much time has passed since 1995 that the intended effect of the standards in the original Model Act has been minimized in today's medical care environment. The obsolescence of the 1995 NAIC standards means, as a practical matter, that self-insured plans bear less relative risk, even in the few states where the Model Act was adopted. Accordingly, today, self-insured products with stop loss insurance or reinsurance that are marketed to small firms closely resemble high-deductible fully-insured plans, but are not subject to many state insurance regulations applicable to fully-insured plans pursuant to the federal Employee Retirement Income Security Act of 1974 ("ERISA"). ERISA states that multistate employers that offer a self-insured plan are not required to cover health care services for state-mandated benefits, as fully-insured plans are.

Additionally, certain provisions of the Affordable Care Act are also presumably incentivizing small employers to self-insure rather than to participate in the state-based insurance exchanges.

Federal Developments

While it is well settled that ERISA insulates multistate employee benefit plans from state regulation, the Affordable Care Act does not define what a self-insured plan is. Absent a definition, there is no clear legislative guidance in ACA as to what a self-insured plan is. More clear, however, is which parts of ACA do not apply to self-insured plans.

First and foremost, self-insured plans are not subject to ACA's essential benefit requirement, otherwise known as the "employer mandate," which requires employers to provide certain essential health insurance coverages to their employees. These essential benefits include health services such as maternity, mental health, and prescription drug benefits.

In addition, self-insured plans are not subject to ACA's risk adjustment or risk pooling requirements. Accordingly, a self-insured plan can price its small group coverage to reflect the group's claims history or medical status or by age, gender, or other factors. In contrast, fully-insured plans, under ACA, can only vary premiums by the average age of the employees, the presence of a wellness program, and tobacco use.

Additionally, self-insured plans are not required to pay the annual fee that insurers are required to pay on fully-insured products pursuant to Section 1343 of ACA. However, self-insured plans are required to contribute to the transitional reinsurance program from 2014 through 2016 created by Section 1341 of ACA, and confirmed in Final Rules promulgated by the Department of Health and Human Services in March 2013.

It bears noting that ACA only applies to employers with 50 or more employees. Smaller organizations, with 49 or fewer employees, do not need to comply with these new Affordable Care Act requirements, regardless of whether they are self-insured or not.

Developments at the State Level

In July 2012, the NAIC's ERISA (B) Working Group circulated a set of draft guideline amendments to the Model Act, as amended, which would have essentially tripled the recommended stop loss insurance attachment minimums adopted in 1995. The new standards had been developed by the NAIC's Health Actuarial Task Force and were intended to update the 1995 standards to reflect today's economic realities.

Those speaking in favor of the updated standards at the NAIC's Fall 2012 meeting argued that they would maintain a level playing field and establish reasonable expectations on stop loss insurance attachment points. They also said the updated standards would be important because they provide an alternative path for state-based regulation of health insurance, most of which is preempted by ERISA. They asserted that if stop loss attachment points are unregulated, a high percentage of small groups are likely to self-insure, which would raise premiums noticeably in the small group market. On the other hand, if the recommended higher attachment points were to be adopted, that risk disappears.

Opponents argued that the Model Law is largely irrelevant since it has been adopted in so few states. They also opposed the updated standards on the basis that they would close doors to options for small employers who are already facing tough choices; that the new standards were not actuarially sound; that they were unnecessary; and that an increase in self-insurance by small groups would not result in adverse selection against fully-insured plans or the insurance exchanges. Rather, it was suggested that self-insured plans were meant to operate alongside fully-insured plans.

The adverse selection argument advanced by supporters of, higher self insurance attachment points is based on the projection that if the current attachment points remain at their existing levels, employers with young and healthy employees will self-insure until they encounter unexpected losses, at which time they will quickly switch to a public insurance exchange. However, others argue that even though young people do not usually have some of the health conditions that older populations have, young people still have family medical histories, pre-existing conditions, and are more prone to accidents and to take maternity leave. In addition, some advocate that there are substantial administrative costs associated with switching from one type of health plan to another, making it less likely for all but the smallest employers to switch back and forth from one plan to another.

Ultimately, the NAIC's proposed updates narrowly failed to pass at the NAIC's November 2012 meeting. At the NAIC's Spring 2013 meeting, the ERISA Working Group announced that it is working on a white paper to further explore the potential impact of regulation of small employer self-insurance on the small group market beginning in 2014.

In addition to the NAIC Model Act activity on stop loss insurance, there has been a recent flurry of proposed state legislation designed to regulate stop-loss insurance.

In California, Senate Bill 161, if it passes, will lower the attachment points currently set forth in California law for all stop loss insurance policies issued on or after January 1, 2014. It would change the individual attachment point from $95,000 to $65,000. The aggregate attachment point would need to be the greater of one of the following:

1. $13,000 times the total number of covered employees (down from $19,000 times the total number of covered employees)
2. One hundred twenty percent of expected claims; or
3. $65,000 (down from $95,000).

This bill was still making its way through the legislative process as of press time.

A bill passed in Colorado would require stop loss insurers to make

annual filings with the Colorado Commissioner of Insurance with information including the following:

1. Total number and average group size of stop loss health insurance policies sold to employer groups with the following numbers of employees: less than 10; 11-25; 26-50; 50-100; or the number of lives covered in Colorado for each of these specified group sizes.
2. The mean and median attachment points by these specified group sizes.
3. The source of prior coverage for these specified group sizes.
4. The smallest group size covered and insurer minimum group size requirements.

The Colorado Commissioner would collect such data for the year s2013-2018 and make the information publicly available. Stop loss insurers would also be required to file an actuarial certification annually.

The bill would create an individual attachment point of $30,000 (just $10,000 more than the current Model Act standard but half of the proposed new NAIC standard). It would also impose an aggregate attachment point that is the greater of (1) $4,000 times the number of group members; (2) 120 percent of expected claims; or (3) $30,000. The Insurance Commissioner would be allowed to change these dollar amounts, by rule, based upon changes to the Consumer Price Index for the Denver metropolitan area. The bill has passed in the Colorado House of Representatives and the Colorado Senate but has not yet been signed into law by the Governor.

Utah's Small Employer Stop-Loss Insurer Act, which was enacted earlier this year, applies only to groups with 50 or fewer employees and sets the attachment point at $10,000. It also contains a provision requiring stop-loss insurers to pay claims incurred but not reported if the plan terminates. The new legislation also prohibits lasering, the practice of setting higher specific deductibles for plan members with pre-existing conditions.

In Rhode Island, if HB 5459 is enacted, the attachment points would be set at $20,000 for an individual or 120% of expected claims in the

aggregate. It would also require stop loss insurers to file an annual actuarial certification as to their compliance with the law.

The Minnesota Legislature also considered restricting the availability of stop loss insurance in their state, but decided not to take any action during this year's legislative session. Similarly, the New Jersey Department of Banking and Insurance had also considered proposed regulations in recent years, but decided not to move forward.

Conclusion

The maintenance of the status quo vis-à-vis stop loss insurance at the NAIC level, combined with new proposed state laws that either lower current attachment point levels, or establish them at nominal amounts, and the ACA incentivizing self-insurance but not regulating it, portends the trend of less regulation of stop loss insurance. Of course, we will need to wait and see what the final impact is on the small group health insurance market when many of the ACA provisions become effective on January 1, 2014. ■

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