Recommendation Form for the 2015 Transition to Employee Choice Due to HHS June 2, 2014 for FF-SHOP States

Instructions: Please fill out the following form and attach your recommendation for a one year transition to employee choice including an evidence-based assessment of the full landscape of the small group market in your State.

State: New Jersey

Insurance Commissioner (signature): 

Please adequately explain that it is in your expert judgment, based on a documented assessment of the full landscape of the small group market in your State that the 2015 Transition to Employee Choice would be in the best interest of small employers and their employees and dependents, given the likelihood that implementing employee choice would cause issuers to price their products and plans higher than they would otherwise price them. Please base your recommendation on discussions with those issuers expected to participate in the SHOP, including naming those issuers, and keep your recommendations specific to 2015 since this is a one year transitional policy.

See attached letter dated June 2, 2014

State of New Jersey
DEPARTMENT OF BANKING AND INSURANCE
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CHRIS CHRISTIE
Governor

KIM GUADAGNO
Lt. Governor

KENNETH E. KOBYLOWSKI
Commissioner

June 2, 2014

The Honorable Kathleen Sebelius, Secretary
U. S. Department of Health and Human Services
200 Independence Ave, SW
Washington, DC 20201

Sent via electronic mail to: shop@cms.hhs.gov

Re: Recommendation for the 2015 Transition to Employee Choice

Dear Secretary Sebelius:

Thank you for the opportunity to provide my recommendation on this important issue. It is my expert recommendation that not implementing employee choice in 2015 would be in the best interests of the New Jersey small group market employers, employees, and dependents. An explanation of the process I employed as well as the information I considered prior to reaching this conclusion is given below.

I requested and received input from the six carriers currently offering small employer coverage in New Jersey as well as from the employer community to meet the requirements of 45 CFR 155.705(b)(3)(vi) that any consideration include the "full landscape of the small group market" in New Jersey. Of the six carriers currently offering small employer coverage in New Jersey, three carriers currently participate in the SHOP. It is important to note that the Department has a long history of seeking input from carriers and has found the information to be helpful and reliable. You may recall that New Jersey was able to develop an acceptable proposal and provide coverage in our pre-existing condition insurance plan (PCIP), NJ Protect, because of the same type of cooperation and assistance provided by two of our carriers, both of which are participating in the SHOP.

The majority of the carriers expressed strong support for not implementing employee choice in 2015. These carriers expressed significant concern with the adverse selection they expect to experience with an employee choice model. Carriers further noted that New Jersey's small employer rates could increase to the level of individual rates as a result of the adverse selection associated with individuals choosing among plans with differences in cost-sharing, network composition, and PCP selection and/or referral requirements. Carriers noted that the existing employer choice model appropriately addresses this type of selection.

Horizon Blue Cross Blue Shield is one of the carriers currently participating in the SHOP as well as outside the SHOP. As a member of the Blue Cross Blue Shield Association, Horizon received

and shared a May 28, 2014 memorandum prepared by the actuarial firm Oliver Wyman. A copy of this memorandum is attached for your reference. This memorandum refers to a 2012 study by the Wakely Consulting Group that estimated that "employee choice allowing for selection across issuers within a metal tier would have an adverse selection impact of 0.5% for those exercising the option." The memorandum quotes the Wakely report as stating "... none of the ACA's risk adjustment programs aim to protect against Market Adverse Selection in the SHOP Exchange." Please note that memorandum provides additional comments with respect to a broader employee choice model than the metal tier model that is being proposed for 2015. The memorandum suggests an increase in administrative costs associated with employee choice and the resultant impact on premiums. According to the memorandum, health plan actuaries generally indicated that the impact of employee choice on SHOP premiums would be an increase in the range of 2% to 4%.

We also asked the New Jersey carriers for estimates as to the cost associated with implementing employee choice. It is important to note that while the SHOP currently limits employers to a single plan, employers buying small employer coverage outside the SHOP enjoy the opportunity to purchase more than one plan from the same carrier. Thus, a small employer may buy both a PPO and an HMO and the employees may select the one they prefer.

A carrier that is currently participating in the SHOP, as well as outside the SHOP, provided the following observations:

> In the Small Group market, employers that offer dual-option products had 1.5% to 4.5% higher MLR than employers that offer single product choice. This result is consistent year-after-year based on a three year analysis.
>
> In the Large Group market, selection effects from multi-option offerings are consistent with that of the Small Group market. Employers that offer two options have, on average, 1.5% higher per person costs than those that offer a single option; and employers that offer three or more options have, on average, 4% higher per person costs.
>
> Based on this evidence, New Jersey should expect that products on the SHOP will be priced higher with an employee choice option than if New Jersey opted for the 2015 Transition to Employee Choice.

A national carrier that is not currently participating in the SHOP but is widely selected by employers purchasing small employer coverage provided the following observations:

> Employee choice will increase premium or inhibit the purchase of a plan. The carrier believes employee choice amongst significantly different plan designs causes selection risk and drives increased medical costs. Generally people with ongoing medical conditions or anticipated elective procedures will choose more expensive benefit coverage plans while those anticipating minimal medical cost will choose lower premium, lesser benefit plans. The carrier's analysis suggests that when there is an approximately thirty-five percent (35%) difference in price between plans offered, there is a corollary overall medical cost increase of about six percent (6%). Therefore, the carrier expects an approximately six percent (6%) higher medical cost will result on SHOP if employee choice is allowed. Since index rates have to be the same on and off

the marketplace, SHOP carriers would have to estimate SHOP penetration and build in overall medical costs and premiums appropriately.

As you may be aware, New Jersey has more than 20 years of experience with a small employer market that has required guaranteed issue, guaranteed renewability, modified community rating, 80% MLR and standard plan designs. During this more than two decade period we allowed selection very similar to the employee choice model. The 75% participation requirement could be satisfied by employers that applied for coverage from multiple carriers with each employee potentially selecting coverage from a different carrier. The term used to describe this opportunity was "slice." Thus, an employer with five employees could buy policies from five different carriers. New Jersey abandoned this model in 2010 following comments from the carriers participating in the small employer market that they experienced severe adverse selection. I have excerpted sections from the small employer Board meeting minutes that address the concerns with "slice."

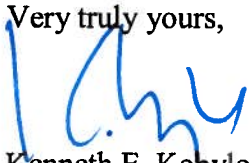
> "… speaking on behalf of the New Jersey Association of Health Underwriters (NJAHU), stated that NJAHU appreciates the carrier's concerns with small employers having the ability to purchase multiple plans from multiple carriers and thus would support a change in Board policy that would limit small employers to the purchase of multiple plans through a single carrier."

> "… stated that there is evidence that "slice" business (where employees of a small employer have the opportunity to select from among multiple plans) poses an underwriting concern."

Having carefully considered all of the information I received, and based on my expert judgment, I have determined that not implementing employee choice in 2015 would be in the best interests of New Jersey's small employers and their employees and dependents given the potential for adverse selection, additionally increased premiums and higher administrative costs.

Again, I appreciate the opportunity to provide my recommendation and I look forward to hearing your decision.

Very truly yours,



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MEMO

TO: BlueCross BlueShield Association

DATE: May 28, 2014

FROM: Kurt Giesa, FSA, MAAA

SUBJECT: Opt Out of Employer Choice on SHOP Exchanges for 2015: Sources and Evidence of Adverse Selection

COPY: Beth Fritchen, Karen Bender

Background

The recently finalized regulation on Exchange and Market Standards for 2015 and Beyond provides states with the ability to petition their SHOP (or HHS in the case of an FF-SHOP) to opt out of employee choice for 2015. A SHOP's decision not to implement employee choice in 2015 must be based on a written recommendation by the state insurance commissioner.[1] Such a recommendation must explain that it is the Commissioner's "expert judgment," based on a documented assessment of the full landscape of the small group market, that not implementing employee choice would be in the best interest of small business, given the likelihood that implementing employee choice would cause issuers to price products and plans higher in 2015 due to issuers' beliefs about adverse selection. The recommendation must be based on concrete evidence, including but not limited to discussions with issuers expected to participate in SHOP in 2015 (§155.705).

Employee choice will lead to higher overall costs for small employers, due to adverse selection and higher administrative costs in most markets. These costs will be borne by all small employers that purchase insurance, regardless of whether they participate in SHOP because HHS rules require these costs to be spread across the SHOP issuer's entire small employer pool. In light of the higher costs of employee choice and implementation risks for all parties, states may find that opting out of SHOP employee choice would be in the best interest of small employers in 2015.

Evidence of Adverse Selection

Our review of the literature and discussions with health plan actuaries indicate that there is reasonable evidence that implementing employee choice would cause issuers to price products and plans higher in 2015 due to adverse selection. We estimate that employee choice could add 2% to 4% to the cost of coverage in the SHOP exchange, depending on the degree of choice in the model implemented.

[1] States must use the following form to opt-out: http://www.cms.gov/CCIIO/Programs-and-Initiatives/Consumer-Support-and-Information/Downloads/State-Application-for-the-2015-Transition-to-Employee-Choice.pdf

CMS requires that a Commissioner's recommendation to opt out of employee choice in 2015 must be based on "concrete evidence," but the Rule does not specify the criteria that will be used to assess the evidence submitted – other than requiring Commissioners to include discussions with issuers expected to participate in the state SHOP in 2015.

Given that employee choice would be a new requirement in 2015, and the experience of employee choice in other states is still unknown[2], the available evidence for issuers and regulators will need to be based on information from health plans with prior experience with employee choice products and prior research. Even CMS recognized that concerns about the newness of employee choice could lead to more conservative pricing:

> "We recognize that some State Insurance Commissioners and issuers have concerns about the potential for adverse selection in the small group market due to employee choice, given that this will be a new feature in many markets and issuers at this point in time may feel that they do not have sufficient data available concerning expected enrollee risk in an employee choice environment. This may lead issuers to price products and plans more conservatively than they otherwise would price, even taking into account premium stabilization programs and other considerations."

Evidence Commissioners could submit includes prior reports from plan actuaries, prior research, or statements from exchanges that have already evaluated the potential for higher costs as a result of adverse selection in an employee choice environment:

- **Estimates from health plan actuaries**
  - Oliver Wyman collected information from eight Blue Cross and Blue Shield plans participating in SHOP. These plans generally indicated that the impact of employee choice on SHOP premiums would be an increase in the range of 2% to 4%.

- **Reports commissioned by states and other stakeholders**
  - A 2012 study by the Wakely Consulting Group for the Robert Woods Johnson Foundation[3] estimated that employee choice allowing for selection across issuers within a metal tier would have an adverse selection impact of 0.5% for those exercising the option, while full employee choice would have an adverse selection impact of 4.5% for those exercising the option.

    The Wakley Consulting Group's 2012 report on employee choice noted:
    "...none of the ACA's risk adjustment programs aim to protect against Market Adverse

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[2] Only a small number of states are attempting to implement employee choice SHOPs with mixed success for 2014 and those programs are so new that no claims data is available to evaluate adverse selection.

[3] "Design Considerations in Structuring Employee Choice for SHOP Exchange," Wakely Consulting Group for the Robert Woods Johnson Foundation, December 2012, http://www.rwjf.org/content/dam/farm/reports/issue_briefs/2012/rwjf403432

Selection in the SHOP Exchange. Offering employee choice, particularly the choice of different AV levels, will increase the potential for adverse selection against the entire market. The healthier members (with low service needs) will gravitate toward leaner plans, resulting in a loss of premium dollars relative to their utilized medical services. The sicker members (with high service needs) will gravitate toward richer plans, resulting in a gain of premium dollars that is not adequate relative to the increased use of medical services." (pg. 5)

- In Colorado, a letter from the Colorado Association of Health Plans found the following: *"Based on an internal study on the impact of adverse selection, we estimate that allowing employee choice between two adjacent metal tiers would increase total costs by around 3%. This impact would be much larger if the gap been plans is even wider (i.e., non-adjacent metal tiers)."* [4]

- **Statement by state Exchanges regarding adverse selection impacts of employee choice in SHOP**
  - Colorado: In regard to Absolute Employee Choice, the COHBE Health Plan Advisory Group stated:
    "There is too much potential adverse selection in this option. One estimate shows that the adverse selection component of this option would raise premiums 10-15% across the board for all plans. States that have allowed this option typically have active purchaser Exchange models and are structured around the Exchange picking plans." (pg. 5)[5]

  - California:
    "Employee choice within the SHOP Exchanges creates a paradox. Employee choice is one of the most attractive features of a SHOP Exchange, and it allows employees to choose products that best suit their needs rather than pooling them together. Yet it is this precise dynamic of high utilizers splitting off from their groups that exacerbates selection issues in ways that may create serious risks for these marketplaces. What this suggests is that to the extent that individual choice is more pervasive post-PPACA, adverse selection may be a more troubling rather than less troubling issue for exchanges as well as the broader insurance marketplace." (pg. 7)[6]

Administrative Costs

Implementing an employee choice SHOP could increase administrative costs that would have to be factored into premiums. Investments by health plans to support the marketplaces have been in the millions to tens of millions of dollars. The manual workarounds for the Federal SHOP, which abandoned its plans to implement automated enrollment for the 2014 benefit year late in 2013, have been costly.

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[4] http://connectforhealthco.com/wpfb-file/20-actuarial-feedback-on-choice.pdf

[5] Appendix 3 for the Colorado Exchange Employer & Employee Choice Policy Decision

[6] "Building Successful SHOP Exchanges: Lessons from the California Experience" Lessons from PAC Advantage

While a large portion of the administrative costs associated with the Exchange and employee choice is related to IT costs and administrative procedures, there are other administrative costs issuers will incur. Specifically, issuers will need to spend additional resources educating agents, small employers and now employees on enrollment procedures, available choices, explanation of benefit differences, potentially network differences, etc. Previously, only the small employer made these decisions.

Given low enrollment, states need to consider the cost-benefit trade-off for SHOP. Enrollment in employee choice SHOPs is generally less than 1% of total small group enrollment based on data available. At the same time, the costs for implementing employee choice must be spread across all small employers covered by an issuer based on HHS pricing requirements for the single risk pool.

Implementation Risks

There is uncertainty in the industry regarding whether the SHOP will be able to meet its goal of employee choice for 2015. Employee choice raises the risks of implementation because it limits the ability of the issuer to perform much of the maintenance or servicing, since the relationship with the employer is severed. A last minute delay in implementation of employee choice would be disruptive to states, issuers and small employers.

Opting out of employee choice could also reduce implementation risks for small employers, issuers and states. It would allow the federal government to test and implement SHOP on a smaller scale in a smaller number of states. This could also be in the best interests of small employers. Small employers who initially attempted to sign up with SHOP for 2014 had to restart enrollment once SHOP could not automate enrollment for 2014. It is clearly in the best interest of small employers to avoid such disruption.

As an example of the difficulty associated with implementing employee choice, we offer the fact that composite premium rating will not be allowed in Federally-facilitated SHOPs in situations involving employee choice.[7]

Potential Effect on Provider Networks

Allowing plan selection at the employee level may have the effect of reducing provider choice on the SHOP. Employees with lower health care needs are more likely to select narrow networks. In theory, the risk adjustment system should compensate issuers offering broader networks, to the extent they suffer from adverse selection, but the HHS risk adjuster is new and untested, and the extent to which it compensates issuers for adverse selection is unknown. Further we note that California's early version of the SHOP, PacAdvantage, included risk adjustment, but by the end of its existence in 2006,

[7] §156.285(a)(4)(ii)

narrow network plans were dominant and it was no longer viable for the lone issuer of PPO plans to remain in the market.[8]

Conclusion

Employee choice will lead to higher overall costs for small employers, due to adverse selection and higher administrative costs in most markets. These costs will be borne by all small employers that purchase insurance from an issuer, regardless of whether the employer participates in SHOP because HHS rules require these costs to be spread across the SHOP issuer's entire small employer pool. In light of the higher costs of employee choice and implementation risks for all parties, states may find that opting out of SHOP employee choice would be in the best interest of small employers in 2015.

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[8] Marie-Anne Hogarth, "Closure of PacAdvantage limits employers' options," *San Francisco Business Times*, November 26, 2006, http://www.bizjournals.com/eastbay/stories/2006/11/27/story3.html?page=all