

## New Federal Rating Rules

The Patient Protection and Affordable Care Act (“PPACA”) includes new federal rules limiting the extent to which insurance companies can impose premium surcharges on individuals and small businesses based on such factors as health status, age, tobacco use and gender.<sup>1</sup> Traditionally, this practice has been regulated by the states, with wide variations in how much insurers are allowed to adjust rates.

### Background

Starting January 1, 2014, insurance companies must adhere to minimum premium rating rules for individuals and small businesses.

Health plans will be allowed to adjust premiums only for the following factors:

- Self-only or family enrollment;
- Geographic area<sup>2</sup>;
- Age (except the rate cannot vary by more than 3 to 1 for adults)<sup>3</sup>; and
- Tobacco use (except the rate cannot vary by more than 1.5 to 1).<sup>4</sup>

Other factors traditionally used by plans to charge higher rates, such as health status and gender, will no longer be allowed.<sup>5</sup>

Most states have enacted some rating reforms in the small group market, prohibiting or restricting the ability of insurers to charge higher premiums based on health status or the risk of having future medical claims. And some states have enacted similar laws for the individual market. Currently, states that require rating reforms fall into three categories [see also Appendix A]:

- Rating band states. These states limit insurers’ ability to base premiums on health status by establishing a range or “band,” so that the highest rate can be no more than some multiple of the lowest rate. Usually, additional adjustments (or surcharges) may be applied to the premium for other demographic factors — such as age, gender, or geography — although in a few states, these demographic adjustments are also limited by the rate band. Rate bands for insurers to spread some risk more broadly across all policyholders, but they still allow for wide variation in rates.

<sup>1</sup> PPACA § 1201, adding Public Health Service Act (PHSA) § 2701.

<sup>2</sup> States have the authority to determine the geographic rating area in their state, but the Department of Health and Human Services (HHS) can review the state determinations to ensure they’re “adequate.” If they’re not found adequate, the Department can establish the rating area (§ 2701(a)(2)(B)).

<sup>3</sup> The National Association of Insurance Commissioners (NAIC) is required to develop a set of permissible age bands for rating purposes (§ 2701(a)(3)).

<sup>4</sup> § 2701(a)(1)(A).

<sup>5</sup> § 2701(a)(1)(B).

- Community rating states. A few states require insurers to charge the same premium to everyone on the same plan in the same community. No adjustments in rates are allowed for health status or demographic factors.
- Adjusted community rating states: Under this form of rating, each insurer has to set a single rate for the plan, but can adjust (surcharge) that premium for specific applicants based on demographic characteristics (such as age). Insurers are not, however, allowed to adjust rates charged to an individual based on claims experience or the health status of an individual.

In states with unregulated markets, studies have found that sicker, older enrollees pay as much as 9 times more for the same policy.<sup>6</sup>

### *Examples: Premiums in an unregulated insurance market*

*Emily is a 56-year-old widow and breast cancer survivor. She exercises three times a week and doesn't smoke. Her friend's son, **William**, is 22 and has never had a major health problem, but he drives recklessly. Emily and William apply for the same health insurance policy that includes a \$500 deductible and \$20 co-payment per physician office visit. Emily is accepted, but she is quoted a premium price of \$24,000 per year. William, on the other hand, is asked to pay just \$2700 per year in premiums.*

Starting in 2014, plans in all states will have to meet the new federal standards and cancer patients and others with high health costs will no longer face higher premiums because of their health condition (although they may be charged more because of their age, or if they smoke). The new federal standards set a floor, so states that wish to retain or enact a tougher standard may do so.

## Issues to Consider

### Higher Rates for Some

The new rating rules in PPACA will have the effect of redistributing the amount of premiums paid by individuals and small businesses. This means that many healthy individuals and groups will pay more than they have been, and those who are sicker will pay less. For example, where states have enacted community rating, studies have shown higher average premiums in those markets.<sup>7</sup> However, any potential increase in premiums under PPACA should be moderated somewhat by the influx of more healthy and young people into the risk pool as a result of the individual mandate.<sup>8</sup>

<sup>6</sup> Pollitz, Karen, et al, "How Accessible is Individual Health Insurance for Consumers in Less than Perfect Health?" Kaiser Family Foundation, June 2001, available at [www.kff.org](http://www.kff.org).

<sup>7</sup> See Monheit, Alan C. and Joel C. Cantor, eds. State Health Insurance Market Reform: Towards Inclusive and Sustainable Health Insurance Markets. New York: 2004.

<sup>8</sup> PPACA includes a requirement that all individuals carry insurance coverage (§ 1501, adding Chapt. 48 to Subtitle D of the Internal Revenue Code). This is critical to the success of the insurance reforms, such as guaranteed issue, the ban on pre-existing condition exclusions, and the rating rules. Without an individual mandate, healthy people would be able to game the system by waiting until they get sick and then buying coverage. The only way to avoid this problem, and keep rates affordable for everyone, is to make everybody carry insurance even when they are healthy.

### ***Example: Premium rates under the new rating rules***

*Emily once again applies for the exact same insurance policy as her friend's son William. William is quoted a premium price of \$4500 per year, and Emily will be charged \$12,000 in premiums for the year.*

## **Adverse Selection**

PPACA requires plans that sell to individuals and small businesses to adhere to the new rating rules, and these rating rules apply to plans both in and out of the new exchanges.<sup>9</sup> However, “grandfathered”<sup>10</sup> plans and plans in the large group and self-insured markets will not have to comply with these rules, as well as a number of the other new market reforms.<sup>11</sup> This could result in adverse selection against plans subject to the new rating and other market rules, because their premiums will likely be higher than those of exempted plans. As a result, healthy individuals and employers with healthy, younger workforces will have strong incentives to keep their costs lower by hanging on to grandfather status or becoming self-insured. For older, sicker individuals and workforces, premiums will be more affordable (and coverage will likely be more comprehensive) in plans subject to the rating rules. If left unchecked, the resulting separation of healthier enrollees from sicker enrollees could cause unaffordable premium increases for people in the plans that are subject to the rating rules.

## **Enforcement**

States have long had the responsibility to regulate and enforce insurance market rating rules. PPACA represents a new partnership between the federal government and state insurance regulators in coordinating activities to ensure that plans comply with the new market protections, including the rating rules. PPACA provides federal authority to enforce the new rules for both individual and group coverage.<sup>12</sup>

If a state lacks the capacity or the willingness to enforce the law, then the federal government must step in. To do so effectively, the federal agencies will need to work closely with the states to monitor insurance industry behavior, verify states’ enforcement of the law, and address compliance problems as they arise. However, the federal government does not currently have the resources or staffing it needs to fulfill its enforcement obligations under the law. If there is weak enforcement of the law, some insurance companies could take advantage of consumers, particularly those with costly health conditions, with little or no risk of sanction.

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<sup>9</sup> § 1201, adding PHSA § 2701(a)(1).

<sup>10</sup> Existing plans may continue to offer coverage as grandfathered plans in the individual and group markets. Enrollment is limited to those enrolled in the plans prior to March 23, 2010 (the date of PPACA’s enactment) and their families, or new employees and their families in employer-sponsored coverage. Enrollees can stay on their grandfathered policy indefinitely (§ 1251).

<sup>11</sup> Other reforms that do not apply to grandfathered and self-insured plans include: essential benefits package, coverage for cancer clinical trials, internal and external appeals, and limits on annual cost-sharing exposure.

<sup>12</sup> § 1321(c)(2), renumbering current PHSA § 2722 as § 2736.

## Conclusion

PPACA's provisions providing more regulation of premium rates and the redistribution of costs will help make insurance coverage more affordable for cancer patients and their families. However, insurance companies will still be allowed to charge significantly more to older individuals and those who smoke. And some individuals in grandfathered plans, or who work for large and self-insured employers, will not receive the same rating protections. Lastly, all of the insurance market rules provided under PPACA, including the new rating limits, must be adequately monitored and enforced through an unprecedented state-federal partnership.

## Appendix A

Individual Market Rating Rules				
State	Access Mechanism	Health Status Adjustments	Gender Adjustments	Age Adjustments
AL	n/a (HIPAA-only HRP)	✓	✓	✓
AK	HRP	✓	✓	✓
AZ	n/a	✓	✓	✓
AR	HRP	✓	✓	✓
CA	HRP	✓	Prohibited	✓
CO	HRP	✓	Prohibited	✓
CT	HRP	✓	✓	✓
DE	n/a	✓	✓	✓
DC	n/a	✓	✓	✓
FL	n/a (HRP closed)	✓	✓	✓
GA	n/a	✓	✓	✓
HI	n/a	✓	✓	✓
ID	Other*	3:1	✓	✓
IL	HRP	✓	✓	✓
IN	HRP	✓	✓	✓
IA	HRP	2:1	1.3: for demographic factors	
KS	HRP	✓	✓	✓
KY	HRP	2:1	5:1 for age, gender and area combined	
LA	HRP	2:1	✓	✓
ME	GI	Prohibited	Prohibited	2.5:1 for age, and area combined (1.5:1 for area)*
MD	HRP	✓	✓	✓
MA	GI	Prohibited	Prohibited	2:1 for age and other specified factors combined
MI	GI from Blue Plan	Commercial Carriers: ✓ BCBS Plan: Prohibited	✓	✓
MN	HRP	1.67:1 for health status, tobacco use and occupation	Prohibited	3:1
MS	HRP	✓	✓	✓
MO	HRP	✓	✓	✓
MT	HRP	✓	Prohibited	✓
NE	HRP	✓	✓	✓
NV	n/a	2.63:1	✓	✓
NH	HRP	1.5:1	Prohibited	4:1
NJ	GI	Prohibited	Prohibited	3.5:1
NM	HRP	2.5:1 for health status, age, gender, area and tobacco use. 1.5:1 for gender within age brackets in 2010; phasing down to a prohibition on gender rating by 2014. [Rates for individuals up to age 19, and ages 19-25 are outside of these bands]		
NY	GI	Prohibited	Prohibited	Prohibited
NC	HRP	✓	✓	✓
ND	HRP	5:1	Prohibited	✓
OH	Other*	✓ <sup>13</sup>	✓	✓

<sup>13</sup> The following health status rating limits apply in Ohio, but only to capped open enrollment program enrollees: 2:1 in 2010-2011 and 1.5:1 starting in 2012, with the latter limit going into effect only if the market-wide average MLR for the entire individual market increases by no more than 5.25% as a result of the open enrollment law

Individual Market Rating Rules				
State	Access Mechanism	Health Status Adjustments	Gender Adjustments	Age Adjustments
OK	HRP	✓	✓	✓
OR	HRP	Prohibited	Prohibited	✓
PA	GI from Blue Plans	Commercial Carriers: ✓ BCBS Plans: Prohibited for certain products	✓	✓
RI	Other*	✓	✓	✓
SC	HRP	✓	✓	✓
SD	n/a (HIPAA-only HRP)	2.5:1	✓	5:1
TN	HRP	✓	✓	✓
TX	HRP	✓	✓	✓
UT	HRP*	1.86:1 (within a class)	✓	✓
VT	GI	Prohibited	Prohibited	BCBS Plan: Prohibited Commercial Carriers: 1.5:1
VA	GI from Blue Plan	✓	✓	✓
WA	HRP*	Prohibited	Prohibited	3.75:1 for age and other specified factors combined
WV	HRP	1.3:1	✓	✓
WI	HRP	✓	✓	✓
WY	HRP	✓	✓	✓
<b>Totals</b>	<ul style="list-style-type: none"> <li>- 5 states have guaranteed issue (GI)</li> <li>- 31 states have high risk pools (HRPs) open to all (34 states total have HRPS)</li> <li>- 3 states have Blue Plan guaranteed issue</li> <li>- 3 states have other access mechanisms</li> <li>- 8 states have no access mechanism</li> </ul>	<ul style="list-style-type: none"> <li>- 7 states prohibit use of health status rating</li> <li>- 13 states limit use of health status rating within bands</li> </ul>	<ul style="list-style-type: none"> <li>- 14 states prohibit gender rating [New Mexico, which is phasing out gender rating, is included in this category.]</li> <li>- 2 states limit use of gender rating within bands</li> </ul>	<ul style="list-style-type: none"> <li>- 1 state prohibits age rating</li> <li>- 11 states limit use of age rating within bands</li> </ul>

Source: Blue Cross Blue Shield Association

- Current rating rules in Maine, which became effective 7-1-09, expanded the total rating band from 1.5:1 to 2.5:1 and allow adjustments within that band for age and area only. Insurers must demonstrate that rates under the new rules do not exceed rates that would have existed under the prior, 1.5:1 rules (which also allowed adjustments for industry/occupation).

**Notes:**

- (1) Guaranteed issue is abbreviated as "GI" and high risk pools are abbreviated as "HRPs." States with asterisks have access mechanisms with more unusual features. These include: (a) Idaho ensures that those not offered private coverage can receive coverage through a virtual pool that contains significant reinsurance; (b) Ohio has annual open enrollment periods during which products must be guaranteed issue up to certain enrollment caps; (c) Rhode Island requires that individual market insurers have an annual open enrollment period, but in practice only the Blue Plan participates in the individual market and is subject to this requirement; and (d) Utah and Washington State have hybrid access systems under which some individuals are offered private coverage and all other individuals are offered high risk pool coverage.
- (2) A "✓" means that rating adjustments must be justified by actuaries.
- (3) Rate adjustments may be permitted based on factors in addition to those discussed in this chart, for example, tobacco use, geographic area, etc. Rating adjustments for these factors have been noted in this chart where they are part of combined rate bands with health status, gender, and age factors.
- (4) HIPAA requires that all individual market coverage be guaranteed renewable.
- (5) Massachusetts pools all individuals (not just self-employed persons) with small employers.
- (6) Generally, limits on health status adjustments reflect restriction on use of health status within a class of business.

## Small Group Market Rating Rules

State	Group Size*	Health Status Adjustments	Gender Adjustments	Age Adjustments
AL	2-50	1.67:1	✓	4:1
AK	2-50	2.08:1	✓	✓
AZ	2-50	4:1 for health status and industry combined	✓	✓
AR	2-25	1.67:1	✓	✓
CA	2-50	1.22:1	Prohibited	✓
CO	1-50	Prohibited	Prohibited	✓
CT	1-50	Prohibited	✓	✓
DE	1-50	2.08:1	1.1:1 for gender and area combined	✓
DC	2-50	✓	✓	✓
FL	1-50	1.35:1 (with additional adjustments permitted for one-life groups)	✓	✓
GA	2-50	1.67:1	✓	✓
HI	2-50	✓	✓	✓
ID	2-50	3:1	✓	✓
IL	2-50	1.67:1	✓	✓
IN	2-50	2.08:1	✓	✓
IA	2-50	1.67:1	✓	✓
KS	2-50	1.67:1	✓	✓
KY	2-50	3:1	5:1 band for age, gender and industry combined	
LA	2-50	2:1	✓	✓
ME	1-50	Prohibited	Prohibited	1.5:1 for age, industry and area combined
MD	2-50	Limited health status rating permitted for uninsured small employers; modified community rating required for all other coverage	Prohibited	2.8:1 for age and area combined
MA	1-50	Prohibited	Prohibited	2:1 for age and other specified factors combined
MI	2-50	Commercial Carriers: 1.45:1 within an area for health status, industry, age, and group size combined BCBS Plan and HMOs: Prohibited	Prohibited	Commercial Carriers: 1.45:1 includes age BCBS Plan and HMOs: 1.35:1 for industry and age combined (within an area)
MN	2-50	1.67:1	Prohibited	3:1
MS	1-50	1.67:1	✓	✓
MO	2-50	2.08:1	✓	✓
MT	2-50	1.67:1	Prohibited	✓
NE	2-50	1.67:1	✓	✓
NV	2-50	1.86:1	✓	✓
NH	1-50	Prohibited	Prohibited	3.5:1 band for age, group size, and industry combined
NJ	2-50	Prohibited	2:1 for age, gender and area combined	
NM	2-50	1.5:1	1.2:1 within a given age group	2.5:1
NY	2-50	Prohibited	Prohibited	Prohibited
NC	1-50	1.67:1	✓	✓
ND	2-25	4:1 for all factors, including age and health status (1.5:1)	Prohibited	Included in overall 4:1 band
OH	2-50	2.33:1 plus an additional "low claims discount"	✓	✓
OK	2-50	1.67:1	✓	✓
OR	2-50	Expected claims experience can be factored in, up to 5% of a group's annual premium (cannot be cumulative year to year), as follows:	Prohibited	3:1 for age and other specified factors combined

Small Group Market Rating Rules				
State	Group Size*	Health Status Adjustments	Gender Adjustments	Age Adjustments
		<ul style="list-style-type: none"> <li>Groups of 26-50: The 5% factor may be applied outside the 3:1 band (see column to right)</li> <li>Groups 2-25: The 5% factor can be applied only within the 3:1 rate band</li> </ul>		
PA	2-50	Commercial Carriers: ✓ BCBS Plans and HMOs: 1.35:1 for any factor beyond those in a carrier's approved rates	✓	✓
RI	1-50	Prohibited	Overall cap of 4:1 for age, gender, and wellness/disease management	
SC	2-50	1.67:1	✓	✓
SD	2-50	1.67:1	✓	3:1
TN	3-25	2.08:1	✓	✓
TX	2-50	1.67:1	✓	✓
UT	2-50	1.86:1	✓	✓
VT	1-50	Prohibited	Prohibited	Prohibited
VA	2-50	1.5:1 (applies only to essential and standard plans, which rarely are purchased in practice)	✓	✓
WA	2-50	Prohibited	Prohibited	3.75:1
WV	2-50	1.86:1	✓	✓
WI	2-50	1.86:1	✓	✓
WY	2-50	2.08:1	✓	✓
<b>Totals</b>		<ul style="list-style-type: none"> <li>11 states prohibit use of health status rating</li> <li>39 states limit use of health status rating within bands</li> </ul>	<ul style="list-style-type: none"> <li>14 states prohibit gender rating</li> <li>5 states limit use of gender rating within bands</li> </ul>	<ul style="list-style-type: none"> <li>2 states prohibit age rating</li> <li>15 states limit use of age rating within bands</li> </ul>

Source: Blue Cross Blue Shield Association

**Notes:**

- (1) A "✓" means that rating adjustments must be justified by actuaries.
- (2) Rate adjustments may be permitted based on factors in addition to those discussed in this chart, for example, tobacco use, geographic area, etc. Rating adjustments for these factors have been noted in this chart where they are part of combined rate bands with health status, gender, and age factors.
- (3) HIPAA requires that all coverage be guaranteed issue and guaranteed renewable for groups of 2-50. In Arkansas and Tennessee, small group rating rules apply to groups of 2-25 and 3-25, respectively.
- (4) Colorado, Connecticut, Delaware, Florida, Maine, Mississippi, New Hampshire, North Carolina, Rhode Island, and Vermont pool self-employed persons with small employers. Massachusetts pools all individuals (not just self-employed persons) with small employers.
- (5) Generally, limits on health status adjustments reflect restriction on use of health status within a class of business.

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