

**STATE of NEW HAMPSHIRE INSURANCE DEPARTMENT**

**Docket No.: INS 07-079-AP**

**In Re: Small Employer Health Reinsurance Pool:  
Request for approval of Amendments to the Plan of Operation  
And Certain other Board Actions**

**FINAL ORDER**

**INTRODUCTION**

RSA 420-K established a nonprofit entity to be known as the “New Hampshire Small Employer Health Reinsurance Pool”, (“the Pool”). The enabling legislation creating the Pool, SB125, passed during the 2005 session of the New Hampshire legislature. In addition to creating the reinsurance pool, this bill repealed health status as a small employer group health insurance rating factor and placed relatively narrow limits on the total variability in rates that health carriers may charge between groups that are expected to have high claims costs and groups expected to have low claims costs. This regulatory approach is known as modified community rating.

The primary goal of modified community rating is to keep health coverage affordable for small employer groups with high expected claims. The challenge for markets governed by some form of community rating is that groups with low expected claims costs have options other than participating in the community rated market. They can “self-insure,” that is, directly pay their own benefit costs and purchase stop loss insurance to cover benefit costs beyond a specified attachment point. Also, they can choose not to provide group health insurance benefits, and leave their employees to buy health insurance in the individual market or to go uninsured.

The rules for coverage purchased in the fully insured small group market are very different from the rules for coverage purchased by self-insured plans or for coverage purchased in the non-group market. Stop loss insurance plans and non-group plans are not required to be offered on a guaranteed issue basis; they may be rated based on health status; and the overall permitted rate variability is much greater. This sets up a potential dynamic in which small employer groups with low expected claims costs leave the community rated market for lower cost alternatives while groups with higher expected claims costs remain in the community rated market. This creates potential rate instability in the small group market as rates increase market wide due to an “adverse selection spiral.”

The primary purpose of the Pool is to promote rate stability in the small group market by setting up a mechanism to compensate for this disparity in market rules. Similar to the manner in which carriers are able to identify high risks in the other markets providing alternative options to small employers, carriers writing in the fully insured market utilize the standard health statement to identify high risks. Without the Pool, these costs would be borne entirely by the carrier’s

book of business. By ceding these identified risks to the reinsurance pool, the carrier is able to transfer these expected costs to a broader base that includes coverage written outside of the small group market. This means that the rates charged to the better risk groups written by the ceding carrier will include a much smaller adjustment to provide for the worse risk groups.

Moreover, the fully insured market in aggregate is further supported by assessing stop loss coverage purchased by the better risk groups that do opt out of the fully insured market. This helps to level the playing field between carriers who are able to utilize underwriting in the selection and pricing of risks with the carriers who are not able to utilize underwriting.

The pool's other purposes include reducing incentives for carriers to engage in risk selection and classification and enhancing competition by providing carriers with smaller blocks, e.g. carriers just entering the market, the ability to cede risks. Smaller carriers attempting to enter the market or to grow their block of business are otherwise disadvantaged by having a limited ability to spread risk in a cost effective way.

At issue in this proceeding is the Board's request for approval of amendments to its Plan of Operation for the Pool, as well as certain other Board actions. Under the statute, the Commissioner must approve amendments to the Plan to "assure the fair, reasonable, and equitable administration of the Pool, and provide for the sharing of Pool gains or losses on an equitable proportionate basis." (RSA 420-K:2 IV) The Plan means "the plan of operation of the small employer health reinsurance pool, including articles, bylaws and operating rules, procedures and policies approved by the commissioner and adopted by the pool." (RSA 420-K:1 VII) This is the first set of amendments proposed to the Plan of Operation that has been submitted since the original Plan was approved. (Department's Final Order, Docket No: INS 05-039-AP)

Throughout this order "the Plan" will be used to refer to the statutory definition, which includes the actual plan of operation document, as well as articles, bylaws and any operating rules, procedures and policies of the pool. "The Plan document" will refer to the document being used by the Board and titled by the Board as "Plan of Operation". The Commissioner has approval authority over everything in the Plan, as well as the Plan Document.

On October 24, 2007, a public hearing was held at the offices of the New Hampshire Insurance Department to provide the Board an opportunity to present its rationale for the proposed Plan amendments and take testimony from other interested parties.

## **FINDINGS AND RULINGS**

### **1. THE BOARD OF DIRECTORS**

The Members elected the following directors:

Beth Roberts	Harvard Pilgrim Health Care of New England
William Whitmore	Anthem Health Plans of New Hampshire

Chris Henderson	Patriot Healthcare
Chris Henchey	MVP Health Care
Jon Hendrickson	Symetra Life Insurance Company
Adam Rudin	CIGNA Life Insurance Company

The following Member Directors are small employer health carriers: Harvard Pilgrim Health Care of New England, Anthem Health Plans of New Hampshire, Patriot Healthcare, MVP Health Care, Symetra Life Insurance Company, CIGNA Life Insurance Company. Therefore at least 2/3 of the Member Directors represent small employer health carriers.

The following carriers write less than \$100,000,000 in net small employer health insurance premiums in New Hampshire: Patriot Healthcare and MVP Health Care. Therefore, at least one Member Director is a small employer health carrier with less than \$100,000,000 in net small employer health insurance premiums in this State.

I find that the slate of elected directors meets the statutory requirements and assures that members are fairly represented. The slate of elected directors is hereby APPROVED.

## 2. THE STANDARD REINSURANCE UNDERWRITING FORM

The board has approved a change to the standard reinsurance underwriting form extending the applicant authorization for the release of healthcare information in the last paragraph from 60 days to 12 months to permit the verification of the accuracy of the information on the form.

The amended standard reinsurance underwriting form is hereby APPROVED.

## 3. AMENDED AND RESTATED BYLAWS

The Board has revised their documents so that the Bylaws reflect governance issues and the Plan document is limited to operational matters. I find that the Amended and Restated Bylaws are consistent with the fair, reasonable and equitable administration of the Pool.

These Amended and Restated Bylaws are hereby APPROVED.

## 4. AMENDMENTS TO THE PLAN DOCUMENT

As required under RSA 420-K, the Board conducted an annual review of the Pool's Plan, including the Plan document, and approved various amendments to the Plan document. These amendments include deleting provisions that were duplicative with the Act, Articles or Bylaws; clarification of the calculation of certain time periods and language regarding the enhanced special assessment capabilities as amended by the Legislature.

Except as specified elsewhere in this Order, I find that the Plan document as amended is consistent with the fair, reasonable and equitable administration of the Pool. These amendments are hereby APPROVED.

5. THE 2008 PREMIUM RATES

The Board reviewed the Pool's standard health benefit plan and rating methodology and made no changes. The methodology for developing the premium rates also remained unchanged, although the actual rates reflect the four percent trend assumption included in that methodology.

The 2008 premium rates, which are based on the existing rating methodology, are hereby APPROVED.

6. THE REINSURANCE DEDUCTIBLE

Board Chair Roberts wrote, in a letter to me, dated October 3, 2007, "This is to inform you as a matter of courtesy that the Board has approved an increase in the [reinsurance] deductible applicable to ceding carriers from \$5,000 to \$50,000." The letter continues, "The Board notes that Section 5(II) of the Act empowers it to increase the deductible without the need for approval from you. Should you disagree with this statutory interpretation, then in the alternative the Board requests that you approve its increase of the Pool deductible to \$50,000."

Based on Staff recommendations, I structured the October 24<sup>th</sup> hearing to consider certain essential questions related to the Board's position.

1. Must the reinsurance deductible be in the Plan?
2. What is the Commissioner's authority with respect to approval of the reinsurance deductible?
3. Is the change from \$5,000 to \$50,000 consistent with the purposes of the pool?

For each of these questions, the Board retains its right to contest my findings.

A. THE QUESTION WHETHER THE REINSURANCE DEDUCTIBLE MUST BE IN THE PLAN.

The Plan sets forth the program's operating rules and procedures. It is the basis for carrier expectations. Carriers contemplating ceding risks are entitled to understand how the Pool adjudicates claims and calculates premiums.

The presence of a reinsurance deductible is a material component of the way claims are adjudicated. The presence of a deductible indicates that ceding carriers will be responsible for some level of claims costs before they can expect to be eligible for reimbursements from the Pool.

RSA 420-K:5 II requires that the Pool have a deductible in place. The Board's duty and authority, as delineated in statute, is to "periodically review" the deductible and make "upward" adjustments. Therefore, the Pool could not operate without a reinsurance deductible.

The Board argues, per statutory requirements, that there would have to be a reinsurance deductible regardless of whether it was referenced in the Plan. The argument continues that the Commissioner could not approve a proposal by the Board to have no reinsurance deductible. Therefore, since the statute's requirements trump the Plan's specifications, neither the Board nor the Commissioner have any authority with respect to whether a reinsurance deductible is part of the Plan. It need not be referenced in the Plan; the statute requires that a reinsurance deductible shall apply. The Board argues further that the level of the reinsurance deductible is a technical detail that need not be specified in the Plan document.

Whether the Plan document refers to the reinsurance deductible is not dispositive of the issue of my authority. The statute requires that a reinsurance deductible be applied during the claims adjudication process. The Plan includes "operating rules, procedures and policies" of the Pool. The reinsurance deductible, both its presence and its level, materially affect the operations of the Pool and therefore, must be considered part of the Plan.

It is of significance that the original Plan document includes the reinsurance deductible. Further, with these proposed amendments, the Board makes no proposals to remove references to the reinsurance deductible from the Plan document; and, notwithstanding the Board's legal arguments, would seem to concede that reference to the same must necessarily be in the Plan.

In order to ensure the fair, reasonable and equitable administration of the Pool, the Plan must be clear as to the presence and level of a reinsurance deductible. I find that the reinsurance deductible must be part of the Pool's Plan and that I have a statutory obligation to review and approve any proposed change to the reinsurance deductible.

**B. THE QUESTION WHETHER THE COMMISSIONER HAS AUTHORITY TO DISAPPROVE AN ADJUSTMENT TO THE REINSURANCE DEDUCTIBLE PROPOSED BY THE BOARD**

The Board argues that the statute is explicit relative to what the Commissioner is authorized to approve. RSA 420-K:5 II, the section speaking to the reinsurance deductible, states "the [reinsurance] deductible shall be periodically reviewed by the Board and may be adjusted upward as determined by the Board." There is no explicit reference to the Commissioner needing to approve these changes. Therefore, the Board concludes, these adjustments are within the sole discretion of the Board, and I have no authority with respect to changes in the reinsurance deductible level.

While the Board does acknowledge that the statute requires the Commissioner to approve changes to the Plan, it argues that changes in the reinsurance deductible have been expressly reserved for the Board. So, even if the level of the reinsurance deductible must be specified in the Plan, in the opinion of the Board, I am specifically barred from taking any non-approval action relative to it.

The statute does not explicitly state that the Board may adjust the reinsurance deductible without Commissioner approval. Further, given the Commissioner's explicit broad approval authority with respect to Plan amendments, it is illogical to conclude that changes to any Plan

element would be outside the scope of the Commissioner's authority. The statute simply places a requirement on the Board to annually review the reinsurance deductible and to adjust it as necessary.

Therefore, I find that adjustments to the level of the reinsurance deductible are subject to my review and approval.

C. THE QUESTION WHETHER THE PROPOSED CHANGE IN THE REINSURANCE DEDUCTIBLE IS CONSISTENT WITH THE POOL'S PURPOSE

The Chair writes in her letter dated October 3, 2007 describing recent actions taken by the Board that:

*Based on a report from NHSEHRP's legal counsel, the Board understands that one of the legislative purposes for the establishment of the Pool was to encourage small carriers to enter the market by spreading the risk of significant health expenses within a small employer group to the entire health insurance market. The New Hampshire General Court expressed an expectation that this would enhance competition and market stability, and perhaps result in the introduction of new health insurance products. A review of the Pool's performance to-date indicates that these legislative expectations have not yet been realized.*

The primary purpose of the Pool is to create some competitive balance between the self-insured or non-group option and the fully-insured small group option. Secondary purposes include reducing the incentive to engage in medical underwriting and enhancing competition by providing a facility for small carriers to cede risks.

Concerning the Pool's primary purpose, carriers writing stop loss insurance plans to self insured small employers have the benefit of using health status and claims experience information when encouraging small employers to convert their benefit program from fully-insured to self-insured. Non-group carriers enjoy similar advantages. These facts present small employer carriers writing fully-insured products with a significant anti-selection risk. Healthy small employers will be attracted out of the fully-insured market, causing rates to rise in the fully-insured market. The Pool provides a mechanism for carriers to identify the same predictable high cost insureds that a stop loss insurance carrier would be able to identify and to spread those costs across the entire health insurance market. The mechanism creates a subsidy to the small employer market carriers that helps to promote rate stability and prevent an anti-selection spiral.

With only one full year of experience available for review and study, it is difficult to tell how successful the Pool has been in stemming an anti-selection spiral, but statistics indicate that the Pool's performance is largely consistent with legislative expectations. The Pool provided reinsurance coverage for 838 ceded lives as of June, 2007. The average number of ceded lives insured each month during the Pool's last fiscal year of operations was 821. The Pool's

operational losses for FY 2007 were \$24.2 million. As the Pool's enabling legislation was being deliberated, the Department provided technical advice on the various legislative proposals. The Department's Fiscal Note Worksheet, FN 05-1049s, estimated that the Pool would provide coverage to approximately 769 lives and the operational losses would be about \$17.9 million. The Pool's operations, as measured in total, appear to be consistent with expectations.

During the legislative deliberations, policymakers paid attention to the aggregate impact on the State's health insurance markets. Little consideration was given to what the impact might be on each small employer health carrier. To date, one carrier, Anthem, has participated in the Pool to a much larger extent than any other carrier. Anthem has benefited from its high participation. Lisa Guertin, President of Anthem Blue Cross and Blue Shield of New Hampshire, testified that through its Pool participation, Anthem has been able to reduce its small group rates. No other carrier indicated that its participation in the Pool has yielded the same results.

Today, it seems that there is considerable concern shared by many of Anthem's competitors in the small employer health market that, through the Pool, they are, in effect, subsidizing Anthem. This fundamental concern has been couched in other terms. For example, Chairman Roberts writes:

*[I]n order to... slow the level of deficit of the Pool, the Board approved an increase in the deductible to \$50,000.*

But, in fact, as already indicated, the Pool's operational losses are consistent with the original expectations. The effect of the proposed change would be to set expected operational losses at one-tenth of its current level. Whereas, in the first year, operational losses were about \$24.2 million versus an expected \$17.9 million, the Board proposes a change that would reduce the anticipated loss to about \$2.4 million. This proposal does not slow the deficit of the Pool. It virtually eliminates the Pool.

I also heard concerns about utilizing a line of credit to finance the Pool's operations. Chris Henchey, Vice President of MVP Health Care New Hampshire, in his testimony, referred to this type of financing as 'accordion financing', and questioned whether such financing was appropriate for the mechanism. Yet, this type of financing is exactly what was contemplated when the legislation was passed. RSA 420-K:6 I specifically states that the assessment rate shall be determined at the close of each fiscal year and shall be based on the losses of the prior fiscal year.

The questions whether the level of the deficit is appropriate and whether accordion financing is appropriate are not questions for deliberation in this forum. Both the Board and I are bound by the statutory intent. Any proposed change that so materially alters the operations of the Pool undermines the original statutory intent. Therefore, a change in the deductible level of the magnitude being proposed is a matter for legislative determination.

In addition, it is of significance that the Board took this action despite the advice and counsel provided by its actuarial expert. The actuarial expert writes:

*We caution against making any dramatic changes in response to the poor first year. Despite the poor early experience, there are signs that things are turning around, and the losses incurred for the second and later years may not be as great as the first year. Ceding from the inforce book is no longer permitted (except on every third anniversary for groups with fewer than six employees). The loss ratio for the first part of 2007 is significantly better than the loss ratio for 2006. As the business matures and the experience becomes more credible, the combination of the line of credit and assessments is likely to become a more effective cashflow management tool.*

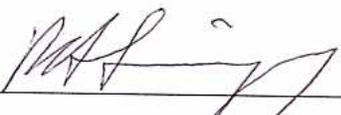
For all the above reasons, the change in the reinsurance deductible is hereby DISAPPROVED.

The Board shall provide the Department with a true and final copy of the documents approved herein, as they have been approved herein, on or before the close of business Friday, November 30, 2007.

SO ORDERED.

NEW HAMPSHIRE INSURANCE DEPARTMENT

Dated: November 20, 2007

  
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Roger A. Sevigny, Commissioner