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HEALTH INSURANCE

How Health Care Reform May Affect State Regulation

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SUMMARY

The Congress is currently debating several health care reform proposals that could fundamentally change the health insurance marketplace. Most health care reform proposals look to states to play an active role in implementing and enforcing new requirements on private health insurers. This role may require states to perform new regulatory tasks and regulate new organizations.

We conducted a questionnaire survey of the insurance departments of all 50 states and the District of Columbia and visited insurance departments in seven states. We found that states try to protect consumers through a variety of regulatory activities--performance of solvency, rate and policy form reviews, and resolution of consumer complaints. State insurance departments' roles in regulating health insurance are affected by their state's legal framework and business regulation philosophy. The resources state legislatures allocate to their insurance departments and the proportion the department dedicates to regulating health insurance vary widely among states.

The health care reform proposals we reviewed provide few details on how various provisions will actually be carried out by states. As a result, state insurance department responsibilities and activities under health reform are uncertain and subject to debate--even among state regulators. The administration's proposal authorizes planning and start-up grants to help states implement any new activities, while another proposal would provide grants to states to establish purchasing cooperatives.

States will continue to play an important role in protecting health insurance consumers under reform. Their responsibilities could become more complex as new requirements are imposed. A reform plan should clearly specify what states are expected to do to carry out their new responsibilities. These expectations need to recognize the wide variation in state insurance departments' existing legal authorities, regulatory activities and resources, and the actions needed to ensure that states have the tools to enforce new requirements on health insurers.

Mr. Chairman and Members of the Subcommittee:

We are pleased to be here today to summarize our work on states' regulation of health insurance, conducted at your request. We are also looking at how states regulatory role may be affected by the various health care reform proposals currently being discussed in the Congress.

In response to concerns about the implications of health care reform on the enforcement roles and responsibilities of state insurance departments, we conducted a questionnaire survey of the insurance departments of all 50 states and the District of Columbia. We also visited insurance departments in seven states--California, Colorado, Illinois, New York, Texas, Vermont, and Virginia[1]--and met with representatives of the National Association of Insurance Commissioners and the insurance industry.

My testimony today will focus on (1) the portion of the health insurance market currently regulated by state insurance departments, (2) the budget and staff resources state insurance departments commit to regulating health insurance, and (3) the key activities insurance departments perform. I will also discuss our observations on how several health care reform proposals might affect the activities of states and their insurance departments.

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[1]We selected these states because they included both large and small insurance departments in different geographic regions and included states that had undertaken state health insurance reform.

INSURANCE DEPARTMENTS' ROLE IN REGULATING HEALTH INSURANCE IS LIMITED

State insurance departments' oversight has generally been limited to a portion of the private insurance market. Only about 24 percent of the United States' national health expenditures is paid for through health insurers that are currently regulated by state insurance departments. Another 34 percent of health care dollars is paid out-of-pocket by individuals or through self-insured employer health plans that are regulated by the Department of Labor under the Employee Retirement Income Security Act of 1974. The remaining 42 percent of health care expenditures is funded and regulated by the federal government through programs such as Medicare and jointly by federal and state agencies for programs such as Medicaid.

RESOURCES COMMITTED TO HEALTH INSURANCE REGULATION VARY WIDELY

State insurance departments are responsible for regulating many different types of insurance, including health, life, auto, and homeowners and other property and casualty insurance. Thus, the departments' resources are spread over a wide range of insurance products. Our study found that, on average, state insurance departments devoted about 24 percent of their 1991 resources to regulating health insurance. However, estimates of individual

states' resource commitments to health insurance regulation varied widely, ranging from 4 to 57 percent of insurance department budgets.

Of the states responding to our survey, 28 estimated that the number of full-time-equivalent staff involved in regulating health insurance ranged from 1 to 153, with a median of 18 staff members.[2] Nine of these 28 states estimated that they had less than 10 full time staff involved in regulating health insurance,[3] and 22 state insurance departments said they were not able to estimate the number of full-time staff involved in regulating health insurance.

Some states we visited had recently enacted reforms to improve the availability and affordability of health insurance to small groups. Insurance department officials said these reforms assigned them new responsibilities that placed an increasing strain on their resources. Typically, these reforms have imposed new restrictions that limit how health insurers set premium rates and medically screen applicants.[4] Implementing these new reforms has increased state insurance department workloads in several areas, including

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[2]It is difficult for states to estimate the number of staff that oversee a particular type of insurance because state insurance departments are typically organized by regulatory activity--not line of business.

[3]The nine states were Delaware, Idaho, Louisiana, New Hampshire, New Mexico, Rhode Island, South Dakota, Vermont, and Wyoming.

[4]Access to Health Insurance: State Efforts to Assist Small Businesses (GAO/HRD-92-20, May 14, 1992).

preparing new regulations and ensuring compliance with new policy and rate provisions.

STATES PERFORM SEVERAL KEY REGULATORY ACTIVITIES

State insurance regulators face particular challenges in protecting consumers from insurer failures, excessive premiums, unfair policy provisions, and unscrupulous insurer business practices. Any one of these problems could be financially devastating to policyholders. States try to protect consumers through a number of activities. Depending on the particular state's regulatory philosophy and the level of resources devoted to health insurance regulation, we found that departments perform these activities in a variety of ways.

Monitoring Insurer Financial Solvency

The principal goal of all state insurance departments is to protect consumers by monitoring the solvency of insurance companies and quickly resolving the problems of financially troubled insurers. To monitor insurer solvency, state insurance departments typically perform annual reviews of insurers' financial data and conduct on-site financial exams of insurers about every 3 to 5 years.

Effectively monitoring insurer financial solvency is a complex and difficult task, in part because insurance regulators must often rely on financial information submitted by the insurer and CPA audit reports of insurer financial statements. A company experiencing financial trouble could hide its true condition from regulators by submitting misleading or false financial information. Such was the case in New York in which, according to a recent report, Empire Blue Cross and Blue Shield--the nation's largest nonprofit insurer--submitted inaccurate financial data to state regulators for years and used the data to justify the need for state insurance reforms. Although the New York State insurance department ranks second in expenditures and third in staffing among all state insurance departments, it did not identify Empire's inaccurate filings.

Reviewing Health Insurance Premium Rates

In addition to solvency monitoring, most state insurance departments attempt to protect consumers from excessive rates by reviewing health insurance premiums. We found that states' approaches to regulating health insurance premium rates differ. Some states require detailed rate submissions, which the insurance department reviews prior to approving or disapproving the requested rates. Others states do not routinely receive health insurance

rate information from insurers or do not have authority to regulate insurance premiums.

States face a particular challenge in balancing consumer interest in affordable insurance with insurance companies' need to collect sufficient premiums to pay future claims. There is little consensus among insurance regulators about how best to manage these competing demands.

New Jersey regulators faced this dilemma in 1992 when they had to weigh policyholders' need for affordable health insurance against Blue Cross Blue Shield of New Jersey's request for a major rate increase to stay solvent. The regulators acknowledged that they approved a smaller rate increase than the plan requested in order to ensure that the plan's premiums remained affordable. The regulators said that their decision to limit the rate increase denied the financially troubled plan an estimated $38 million in revenue that could have bolstered its reserve position.

Reviewing Health Insurance Policies

Insurance regulators also review health insurance policies because they are often complex and difficult for consumers to understand. States ensure that policies comply with state laws, which often include provisions such as readability, required coverages, prohibited exclusions and a number of administrative requirements.

States do this in several ways. For example, Texas uses a detailed checklist and reads each policy form line-by-line before it can be used. In contrast, insurance regulators in Colorado only require that the insurer certify that the form complies with all state laws and regulations.

Investigating Consumer Complaints and Insurer Market Practices

Finally, insurance consumers are vulnerable to unscrupulous practices by insurance companies, such as high-pressure sales practices, improperly denied claims, unfair discrimination, and improper denial of coverage. States we visited routinely used consumer complaints to help identify problem insurers. To protect against these unfair practices, insurance departments investigate consumers' complaints regarding health insurers. In addition, most states perform market conduct exams to review the marketing, underwriting, rating, and claims payment practices of health insurers.

In 1991, health insurance complaints comprised about 37 percent of the approximately 344,000 consumer complaints received by 45 insurance departments. The other five states did not distinguish health insurance complaints from other insurance complaints in their tracking system. Our survey found that 38 states believe

that the number of health insurance complaints has increased in recent years.

HOW HEALTH CARE REFORM WILL AFFECT STATES IS UNCLEAR

Most health care reform proposals look to states to play an active role in implementing and enforcing new requirements on private health insurers. This role may require states to perform new regulatory tasks and regulate new organizations.

We reviewed the administration's and several other health care reform proposals to identify how they may impact the states and their insurance departments. We found that the proposals provide few details on how various provisions will actually be carried out. Moreover, the manner in which state insurance department responsibilities and activities may change under health reform is extremely uncertain and still being debated--even among state regulators. Finally, the administration's proposal authorizes planning and start-up grants to help states implement any new activities, while another proposal would provide grants to states to establish purchasing cooperatives.

The proposals we reviewed prescribe some role for states in establishing standards for health insurance plan solvency. But it is unclear from the proposals what types of solvency standards

states would use, or how they might differ from the existing state by state standards that apply to various types of insurers and health maintenance organizations. These proposals also provide for a health plan's revenue to be adjusted for the expected utilization of health services by the plan's enrollees, but they do not indicate how risk adjustment requirements would be monitored. To further protect policyholders and providers in the event of a health plan failure, the administration's proposal also requires states to ensure that a guaranty fund exists. However, it is unclear whether this would be a new fund or an extension of the life/health guaranty funds that currently exist in most states.

If risk adjustment provisions are not implemented, the administration's proposal provides a role for states in establishing reinsurance programs. Another proposal assigns the responsibility for monitoring the reinsurance market for health plans to a national commission. Again, these proposals do not address if or how states would monitor reinsurance programs.

The proposals we reviewed all require the use of community rating in determining the premium rates for plan enrollees. The proposals primarily assign the responsibility for implementing these provisions to health alliances or purchasing cooperatives, rather than the states.

The reform proposals would require health insurance plans to offer a standard medical benefits package with no medical underwriting. While all states currently review policy forms in some manner, the administration proposal is unclear about whether the states would continue to review policy forms for compliance with these requirements, and other proposals do not address the monitoring role. The administration proposal asks states to ensure that plans are actually providing the benefits promised, while other proposals do not address this issue.

Finally, most proposals we reviewed would move the handling of consumer complaints from state insurance departments to the health alliances or purchasing cooperatives. One proposal may require the states to share the responsibility with the health purchasing cooperatives. The administration proposal also assigns responsibility for monitoring advertising to the health alliances, while the other proposals are silent in this area.

CONCLUSIONS

Although there is still much uncertainty about the final outcome of the health care reform debate, it may involve fundamental changes in the health insurance industry. States will continue to play an important role in protecting health insurance consumers. However, this role could be more complex as new responsibilities are imposed on states. A reform plan should clearly specify what states are

expected to do to carry out their new responsibilities. These expectations need to consider the wide variation in state insurance departments' existing legal authorities, regulatory activities and resources, and what actions need to be taken to ensure that the states have the necessary tools to enforce new requirements on health insurers.

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Mr. Chairman, this concludes my prepared statement. We would be happy to answer any questions you may have.

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