A not-for-profit health and tax policy research organization

Testimony before the U.S. House of Representatives
Committee on Education and the Workforce
Subcommittee on Health, Employment, Labor, and Pensions

Rep. Phil Roe, Chairman
Rep. Robert Andrews, Ranking Member

Hearing on

Regulations, Costs, and Uncertainty in Employer Provided Health Care
October 13, 2011

Testimony presented by
Grace-Marie Turner
President, Galen Institute

Regulations, Costs, and Uncertainty in Employer Provided Health Care: Saving Jobs from PPACA's Harmful Regulations

Committee on Education and the Workforce
Subcommittee on Health, Employment, Labor, and Pensions
Testimony by
Grace-Marie Turner, Galen Institute

Executive summary

- The unemployment rate is stuck at 9.1 percent, and there is good reason to believe that PPACA is a major contributor to the jobs picture. Employers fear the costs, mandates, and regulations of hiring new workers as a result of PPACA.

- While most companies initially hoped they would be able to preserve much of their existing group health plans under the new grandfather provisions of the law, a survey by Aon Hewitt Consulting found almost all will not. The administration's own estimates indicate most employers will not be able to maintain grandfathered status.

- The grandfathering rules box employers into a corner. They cannot make changes, other than minor modifications, to their health plans to keep costs down without being forced to comply with expensive PPACA regulations that increase their health costs.

- Health costs are directly related to creation of new jobs. Higher health costs put additional pressures on the employer's bottom line and increase the cost of hiring new workers, in turn discouraging job creation. This is bad news for the economy and for unemployed workers.

- Many people argue that PPACA's restrictions are necessary to keep employers from cutting benefits or imposing higher health costs onto their employees. But employees actually pay the price for rising health costs.

- A recent RAND study found that most of the pay increases that employees have received over the last ten years have been consumed by health costs. The typical family had just $95 a month more to devote to non-health spending in 2009 than a decade earlier. Had the rate of health care cost growth kept pace with general inflation, the family would have had $545 more per month in spendable income — a difference of $5,400 per year.

- PPACA already is having a direct impact on jobs in the health broker industry because of misguided regulations concerning the Medical Loss Ratio requirements in the law.

- Health costs are a jobs issue. It is in the interest of both employers and employees to keep health costs down, and the grandfathering and MLR regulations issued by HHS restrict their ability to do that.

Regulations, Costs, and Uncertainty in Employer Provided Health Care: Saving Jobs from PPACA's Harmful Regulations

Committee on Education and the Workforce
Subcommittee on Health, Employment, Labor, and Pensions
October 13, 2011
By Grace-Marie Turner, Galen Institute

Thank you Chairman Roe, Ranking Member Andrews, and members of the Committee for the opportunity to testify today about the impact of regulations on costs and uncertainty in employer-provided health coverage and particularly the impact of provisions in the Patient Protection and Affordable Care Act (PPACA) on employers, employees, and job creation in America.

Impact on job creation

PPACA's potential impact on jobs and the economy has been the subject of debate and controversy from the start. The president promised it would be a boon to both; former Speaker Nancy Pelosi said the law would create 400,000 jobs "almost immediately." Others argued, however, that the law's costs and mandates would make businesses much *less* likely to hire new workers.

That debate should now be over.

The Heritage Foundation's James Sherk, a senior policy analyst in labor economics, recently released a paper[1] comparing the rate of net job growth before and after PPACA's passage in March of 2010. The findings show that job creation came to a virtual halt after the health law was enacted.

The low point of the recession came in January 2009, when U.S. employers shed 841,000 jobs in just that one month. But the economy slowly started to recover over the next 15 months; private employers began hiring workers at an average rate of 67,600 per month (net of layoffs). The economy's high point came with the April 2010 report, when 229,000 jobs were added.

But the health law was signed into law in late March, and the hiring freeze began. In the following months, the economy added an average of just 6,500 net private sector jobs per month — less than a tenth of the pre-ObamaCare average.

This doesn't prove that the health law is a major cause of the problem. But there is no question that the jobs recovery stalled after ObamaCare passed, with no new jobs created in August and unemployment stuck at 9.1 percent. There's good reason to believe that the health law is a major contributor to the hiring halt.

In a recent U.S. Chamber of Commerce study, 33 percent of business owners cited uncertainties about the health law as either the biggest or second-biggest reason they're not hiring new workers.

Those findings were backed up by the words of Dennis Lockhart, president of the Federal Reserve Bank of Atlanta, in a speech: "We've frequently heard strong comments to the effect of 'My company won't hire a single additional worker until we know what health-insurance costs are going to be.' "[2]

The health law discourages hiring in several ways. First, it adds unknown costs to hiring new workers. Companies already must consider the cost of taxes for Social Security, Medicare, unemployment insurance, and workers' compensation when hiring new staff. Combined with health benefits, these costs explain why a $50,000-a-year employee costs a company $62,500 to $70,000 (according to MIT business professor Joseph Hadzima).[3] The health law will add new costs by forcing employers to either provide workers with expensive, government-approved insurance or pay a fine. Employers anticipating these costs are simply unwilling to add new workers.

The health law also discourages small businesses from becoming mid-size businesses because the mandate to provide insurance kicks in once you reach 50 or more employees. This is profoundly wrongheaded. Small business is the engine for job growth in America, but a recent survey found that 70 percent have no plans to increase hiring in the next year.

As for those companies that already have 50 or more workers, the burden of having to buy expensive government-approved policies or pay penalties discourages them from hiring all but essential staff. Indeed, larger companies are doing everything they can to pare back on entry-level jobs and are using automation to avoid the added cost of mandatory health insurance for lower-income workers. McDonald's and CVS drug stores, among many other large companies, are replacing some human order-takers and cashiers with electronic systems.

This especially hurts entry-level would-be workers who need jobs so they can get the skills to enter the workforce. Is it any surprise that teen unemployment has now hit 25 percent? The jobs they need are evaporating because of the president's health overhaul law.

Employees pay the price of higher health costs

Many people argue that the PPACA's regulations are necessary to keep employers from cutting benefits or imposing higher and higher health costs onto their employees. But employees actually pay the price for these higher health costs.

The cost of health coverage is part of employee compensation. A recent RAND study found that most of the pay increases that employees have received over the last ten years have been consumed by health costs.

Between 1999 and 2009, a median-income family of four that received health insurance through an employer saw their real annual earnings rise from $76,000 to $99,000 over the ten year period. But nearly all that gain was consumed by rising health care costs, according to the paper by David Auerbach and Arthur Kellermann of RAND. [4]

After taking into account the price increases for other goods and services, they said the typical family had just $95 a month more to devote to non-health spending in 2009 than they had a decade earlier. By contrast, the authors say that if the rate of health care cost growth had not exceeded general inflation, the family would have had $545 more per month in spendable income instead of $95 — a difference of $5,400 per year. Workers are paying the price for higher health costs.

Many companies have introduced plans that engage their employees as partners in managing health costs, giving them more control over health care and health spending decisions. These companies have had success in holding down health cost increases. A 2011 survey for the National Business Group on Health on "purchasing value in health care" found that companies that offered account-based health plans, such as Health Savings Accounts or Health Reimbursement Arrangements, had coverage costs that were $900 lower than average for employee-only coverage and $2,885 lower for Preferred Provider and Point of Service (PPO/POS) plans.[5] "The cost of [account-based health plan] coverage is considerably more affordable than either PPO/POS plan or HMO plan coverage in 2011," the survey found. These premium savings benefit both employers and employees.

The number of people with HSA/HDHP (high-deductible health plan) coverage rose to more than 11.4 million in January 2011, up from 10 million in January 2010, 8 million in January 2009, and 6 million in January 2008.[6]

Of course consumer-directed plans are only one option of the wide array of policy choices offered in the private marketplace. But many employees and employers value this choice. Flexibility, rather than the top-down regulations PPACA is imposing, is essential for employers and employees to find ways to hold down health costs.

Grandfathered health plans

Many employers said that assurances their health plans would be "grandfathered" was a key reason that led to their support or to their taking a neutral stance on passage of the PPACA.

People who have and value their health coverage were also reassured. Surveys have shown that 88 percent of Americans are satisfied with their health coverage.[7] While most companies initially hoped they would be able to preserve much of their existing group health plans under the new grandfather provisions, a survey by Aon Hewitt Consulting found almost all will not.[8]

"If you like your health insurance, you can keep your health insurance," the president repeatedly promised. Even administration experts now admit this promise will not be kept. The Department of Health and Human Services expects that, by 2013, between one-third and two-thirds of the 133 million people with coverage through large employers will lose their grandfathered status. And up to 80 percent of the 43 million people in small employer plans will lose their grandfathered protection. Up to 70 percent of those with coverage in the individual market would be forced to comply with expensive new federal rules within a year.[9] Few of them are likely to lose coverage in the short term, but most will lose the coverage they have now.

The grandfathering rules box employers into a corner. They cannot make changes, other than minor modifications, to their health plans to keep costs down without being forced to comply with expensive PPACA regulations that increase their health costs.

Health costs are the issue

The human resources consulting firm Towers Watson released a survey of large employers regarding health costs.[10] Seven out of ten of the employers surveyed expect to lose grandfathered health status in 2012 — subjecting them to all of the new regulations and mandates under the new health law. Of even greater concern, nearly three in ten employers (29 percent) are unsure

whether or not they will continue offering coverage to their current workers after all of the provisions of the new health law take effect.

Towers Watson reports that overall health plan costs are projected to rise at a 5.9 percent rate in 2012, continuing to rise faster than the rate of overall inflation. Because of rising health insurance costs and the other cost pressures that employers face, a majority of firms say they will be forced to increase the employee share of premiums in 2012. Only one percent of firms say they will be able to decrease the employee share of premium contributions next year.

Health costs are directly related to creation of new jobs. Employers continue to face a fragile economy. Higher health costs put additional pressures on their bottom line and increase the cost of hiring new workers, in turn discouraging job creation. This is bad news for the economy and for unemployed workers.

What all employers must cover

Under the Affordable Care Act, all health plans — whether or not they are grandfathered plans — were required to provide certain benefits for plan years starting after September 23, 2010, including:[11]

- Restrictions on lifetime limits on coverage for all plans. Starting in 2014, insurance plans must provide coverage without imposing any annual or lifetime limits on the amount paid to individual beneficiaries. During the transition years between now and 2014, however, insurance firms can impose annual limits, subject to HHS rules. The HHS regulations issued last June dictated how high these limits must be. In 2011, insurance companies can

continue to impose an annual limit, but it must be at least $750,000 per enrollee. In 2012, the limit will have to be at least $1.25 million, and in 2013, $2 million. In 2014 there can be no limit on payouts for any individual's care.[12] This is the particular regulation that has led to at least 1,578 waivers being issued by HHS, primarily covering limited benefit plans offered by employers such as McDonald's who said the higher cost could force them to drop the coverage altogether.[13]

- No rescissions. Plans may not rescind coverage after enrolling a participant, except in the case of fraud or limited circumstances.
- No coverage exclusions for children under age 19 with pre-existing conditions, and no pre-existing condition exclusions for anyone starting in 2014.[14]
- Group health plans that provide dependent coverage are required to extend coverage to adult children up to age 26 with no conditions on dependency.

A recent employer survey said that 28 percent of employers believe that compliance with PPACA rules already is increasing their health cost.[15]

Restrictions on plans hoping to keep grandfathered status

What do plans have to do in order to maintain their grandfathered status? A Health and Human Services Department fact sheet describes the restrictions.[16]

Compared to policies in effect on March 23, 2010, employers:

- cannot significantly cut or reduce benefits
- cannot raise co-insurance charges

- cannot significantly raise co-payment charges
- cannot significantly raise deductibles
- cannot significantly lower employer contributions
- cannot add or tighten an annual limit on what the insurer pays
- cannot change insurance companies. (This rule was later amended to allow employers to switch insurance carriers as long as the overall structure of the coverage does not violate other rules for maintaining grandfathered plan status. The amended rule specifically directs that the new insurance carrier must precisely match the same terms of coverage that were previously in place.)

These rules mean, for example, that health plans and employers with plans in effect on March 23, 2010, lose their exempt — or grandfathered — status if they were to raise co-payments by the greater of $5 or a medical inflation rate plus 15 percent. Deductibles couldn't go up more than medical inflation plus 15 percent. In addition, employers couldn't cut the amount of the premium that they contribute by more than 5 percent.

Plans that lose their grandfathered status become subject to all of the requirements in PPACA, including first-dollar coverage for preventive care, required coverage for certain clinical trials, quality reporting requirements, and implementation of internal and external appeals processes.

A survey by Aon Hewitt Consulting found that ninety percent of companies said they anticipate losing grandfathered status by 2014, with the majority expecting to do so in the next two years. The study found that among those companies with self-insured plans, 51 percent expect to first

lose grandfathered status in 2011 and another 21 percent expect to lose it in 2012. The survey found that "Most employers would rather have the flexibility to change their benefit programs than be restricted to the limited modifications allowed under the new law."[17]

Why employers need flexibility

The employment-based health system in the United States has evolved from decisions made during World War II that gave favored status to health insurance offered through the workplace. Our system of employer-based health insurance is underpinned by generous tax incentives that allow employers to deduct the cost of health insurance as a part of their employee compensation costs and through a separate tax provision that shields the value of the policy from being taxed as income to the worker. These dual tax incentives have provided strong incentives for people to get their health insurance at work and have led to the system in which 158 million Americans get health insurance through the workplace.

Employers work very hard to find the balance in keeping the cost of health insurance as low as possible while offering the benefits that employees want and need. Part of the way they are able to do this is by seeking bids from competing insurers and amending and adjusting benefit structures. But under the grandfathering rules, employers are very limited in their ability to adjust current benefits without losing their grandfathered status. This also means they are limited in what they can do to help keep costs down.

The U.S. Chamber of Commerce, the largest U.S. business advocacy group, presented written comments on the grandfathering rules in August 2010, saying its first concern is with the

restriction on cost-sharing. "By so severely restricting changes in cost-sharing, the regulations will effectively force plans to lose grandfathered status in order to remain solvent," the Chamber wrote.[18]

Medical Loss Ratio regulations as job killers

PPACA already is having a direct impact on jobs in the health broker industry. Janet Trautwein, Executive Vice President and CEO of the National Association of Health Underwriters (NAHU), reported in recent testimony before the House Energy and Commerce Subcommittee on Health that "the economic outlook for many health insurance agents and brokers across the country continues to be bleak. As health insurance companies renew and revise their agent and broker contracts for the coming year, it is clear that the financial situation for many of these business owners is getting worse."[19]

She reported that: "NAHU recently surveyed its members and found that 21 percent of independent health insurance agency owners have been forced to downsize their businesses, including laying off employees. Twenty-six percent have also had to reduce the services they provide to their clients … Five percent of respondents who were not principals in their agencies have already lost their jobs due to producer revenue reductions caused by the MLR regulation, and agency owners report that if their compensation continues to plummet more job loss will follow."

The main reason for this is a rule imposed by the Department of Health and Human Services involving the Medical Loss Ratio (MLR) which mandates that health insurance carriers spend 85

percent of their premiums for large groups and 80 percent of their premiums for individual and small group policies on direct medical care.

The HHS rule requires health plans to treat independent agent and broker compensation as part of health plan administrative costs — even though they aren't employed by health insurance carriers. Brokers and agents run their own businesses, hire their own employees, and pay all of their own office expenses, working for their clients to find the best and most affordable health insurance, usually from a range of health carriers.

None of the compensation goes to the health insurer, yet HHS rules require that it be counted against the insurer's allowable administrative cost.

Agents bring a great deal of value to their clients, yet this clumsy rule is shoving them aside. Not only do they help individuals and small businesses find the most appropriate and affordable policy from many competing carriers, but they also help companies find and establish wellness and disease-management programs and navigate the often-complex claims process. They are a crucial element in the equation of helping businesses find the most appropriate and affordable health policies for their employees.

Agents and brokers often act as an external human resources department for companies. Many smaller companies do not even have an HR department so, as the Congressional Budget Office has noted, agents and brokers often "handle the responsibilities that larger firms generally

delegate to their human resources departments — such as finding plans and negotiating premiums, providing information about the selected plans, and processing enrollees."

Janet Trautwein testified that NAHU "members are spending significant amounts of time educating their clients about the new law's provisions and helping them comply with its resulting regulations. Regardless of what the final outcome of PPACA may be, the need for licensed, trained professionals to help individuals, employers and employees with their health insurance needs will always be there. So we need to make sure this industry survives." She made it clear that "PPACA-related regulations … are costing American jobs and hindering American business owners every single day. In every state, as a direct result of the new law's MLR provisions, agency owners are reporting that they are reducing services to their clients, cutting benefits and eliminating jobs just to stay in business. In some instances, they are simply closing their doors." NAHU recommends "eliminating independent producer commissions from the MLR calculation," adding that this "will go a long way toward providing uniform and needed relief to all health insurance markets — and the consumers who reside within them — during the transitional period as PPACA requirements are fully implemented over the next three years."

Relief from the grandfathering regulation

It is in the interest of both employers and employees to keep health costs down, and the MLR and grandfathering regulations issued by HHS are just two examples of rules that are restricting their ability to do that. Health costs and jobs are at stake.

I understand that legislation is being drafted to reverse the interim final regulation issued by HHS addressing grandfathering. Reversing this regulation would give employers the flexibility

they need to manage their health costs and find the balance between health costs, wages, and hiring new workers. In addition, Reps. Mike Rogers and John Barrow of Georgia have introduced legislation, the Access to Professional Health Insurance Advisors Act of 2011, to remove independent health insurance producer commissions from what is currently defined as premiums for MLR calculation.

Chairman Roe, your leadership on health reform issues is particularly important because of your experience as a physician and because you have first-hand experience with the damage of government-controlled health care through TennCare. Your support for repeal of the Independent Payment Advisory Board is both important and relevant. You have made it very clear in your work that you believe health care is best provided when doctors and patients — not Washington bureaucrats — are in charge of decisions. It is fortunate that Drs. Bucshon, DesJarlais, and Heck are also serving with you on this committee to provide physician leadership in Congress to restore the proper control over health care decisions to doctors and patients.

Thank you for the opportunity to testify today, and I will be happy to answer your questions.

ENDNOTES

[1] James Sherk, "Economic Recovery Stalled After ObamaCare Passed," The Heritage Foundation, July 19, 2011, http://thf_media.s3.amazonaws.com/2011/pdf/wm3316.pdf.

[2] Dennis Lockhart, "Business Feedback on Today's Labor Market," Federal Reserve Bank of Atlanta, November 11, 2010, http://www.frbatlanta.org/news/speeches/lockhart_111110.cfm.

[3] Joseph G. Hadzima, Jr., "How Much Does an Employee Cost?" *Boston Business Journal*, http://web.mit.edu/e-club/hadzima/pdf/how-much-does-an-employee-cost.pdf.

[4] David I. Auerbach and Arthur L. Kellermann, "A Decade Of Health Care Cost Growth Has Wiped Out Real Income Gains For An Average US Family," *Health Affairs*, September 2011, http://content.healthaffairs.org/content/30/9/1630.abstract.

[5] "Shaping Health Care Strategy in a Post-Reform Environment: 2011 16th Annual Towers Watson/National Business Group on Health Employer Survey on Purchasing Value in Health Care," Towers Watson/National Business Group on Health, March 2011, http://www.towerswatson.com/assets/pdf/3946/TowersWatson-NBGH-2011-NA-2010-18560-v8.pdf.

[6] "January 2011 Census Shows 11.4 Million People Covered by Health Savings Account/High-Deductible Health Plans (HSA/HDHPs)," America's Health Insurance Plans, June 2011, http://www.ahipresearch.org/pdfs/HSA2011.pdf.

[7] Ruth Helman and Paul Fronstin, "2010 Health Confidence Survey: Health Reform Does Not Increase Confidence in the Health Care System," Employee Benefit Research Institute, September 2010, http://www.ebri.org/pdf/surveys/hcs/2010/ebri-notes-09-2010-hcs-rspm.pdf.

[8] "Employer Reaction to Health Care Reform: Grandfathered Status Survey," Aon Hewitt, August 2010, http://www.aon.com/attachments/Employer_Reaction_HC_Reform_GF_SC.pdf.

[9] "Fact Sheet: Keeping the Health Plan You Have: The Affordable Care Act and 'Grandfathered' Health Plans," U.S. Department of Health and Human Services, HealthReform.gov, Accessed September 13, 2011, http://www.healthreform.gov/newsroom/keeping_the_health_plan_you_have.html.

[10] "Employers Committed to Offering Health Care Benefits Today; Concerned About Viability of Insurance Exchanges," Towers Watson, August 24, 2011, http://www.towerswatson.com/press/5328.

[11] "Fact Sheet: Keeping the Health Plan You Have: The Affordable Care Act and 'Grandfathered' Health Plans," U.S. Department of Health and Human Services, HealthReform.gov, Accessed September 13, 2011, http://www.healthreform.gov/newsroom/keeping_the_health_plan_you_have.html.

[12] John Hoff and John E. Calfee, "The Contradictions of ObamaCare," *The American*, February 10, 2011, http://www.american.com/archive/2011/february/the-contradictions-of-obamacare.

[13] "Annual Limits Policy: Protecting Consumers, Maintaining Options, and Building a Bridge to 2014," The Center for Consumer Information & Insurance Oversight, Accessed September 13, 2011, http://cciio.cms.gov/resources/files/approved_applications_for_waiver.html.

[14] PPACA was misdrafted, and the law did not explicitly require insurers, starting last year, to sell health insurance to families with children under age 19 who have pre-existing conditions. But health plans told Department of Health and Human Services Secretary Kathleen Sebelius they would voluntarily comply with the HHS rules requiring them to cover these children. For more information: Robert Pear, "Insurers to Comply With Rules on Children," *The New York Times*, March 30, 2010, http://www.nytimes.com/2010/03/31/health/policy/31health.html.

[15] "US employer health plan enrollment up 2% under PPACA's dependent eligibility rule," Mercer LLC, August 1, 2011, http://www.mercer.com/press-releases/1421820.

[16] "Fact Sheet: Keeping the Health Plan You Have: The Affordable Care Act and 'Grandfathered' Health Plans," U.S. Department of Health and Human Services, HealthReform.gov, Accessed September 13, 2011, http://www.healthreform.gov/newsroom/keeping_the_health_plan_you_have.html.

[17] "Employer Reaction to Health Care Reform: Grandfathered Status Survey," Aon Hewitt, August 2010, http://www.aon.com/attachments/Employer_Reaction_HC_Reform_GF_SC.pdf.

[18] "Comments on the Grandfathered Health Plan Status Regulations," U.S. Chamber of Commerce, August 16, 2011, http://www.uschamber.com/issues/comments/2010/comments-grandfathered-health-plan-status-regulations.

[19] Janet Trautwein, Testimony for the United States House of Representatives Committee on Energy and Commerce Subcommittee on Health Hearing "Cutting the Red Tape: Saving Jobs from PPACA's Harmful Regulations," September 15, 2011, http://republicans.energycommerce.house.gov/Media/file/Hearings/Health/091511/Trautwein.pdf.