



Texas Department of Insurance

Commissioner of Insurance, Mail Code 113-1C
333 Guadalupe • P. O. Box 149104, Austin, Texas 78714-9104
512-463-6464 telephone • 512-475-2005 fax • www.tdi.state.tx.us

December 7, 2010

The Honorable Kathleen Sebelius, Secretary
U.S. Department of Health & Human Services
200 Independence Avenue, SW
Washington, D.C. 20201

RE: Medical Loss Ratio Transition Period

Dear Secretary Sebelius:

As you prepare to implement the interim final regulation relating to the Medical Loss Ratio (MLR) provisions of the Patient Protection and Affordable Care Act (PPACA), I would like to take this opportunity to thank you for taking the needs of the individual market into consideration by incorporating into the interim regulation a process for temporarily adjusting the required MLR. I would also like to urge you to reconsider allowing for a broader phase in period than is contemplated in the interim regulation that would enable a smooth transition into the new regulatory market, and doing so on a national scale.

Phasing in MLR requirements for the individual market will minimize some of the unintended destabilizations that might result from an abrupt shift in a volatile market. However, the individual market does not exist in a vacuum. Failing to address other areas of the insurance market that will be impacted by the new MLR requirements could still lead to destabilization of the individual market. The experience and expertise with respect to insurance of employers in the small group market and individuals, along with the number of insureds, are very similar. Those similarities are acknowledged by PPACA, which even contemplates the possible merger of the two markets in the Exchange system.

Allowing for a broader transition period that not only contemplates the impact on the individual market, but also on the small group market would allow companies to adapt their expense structure and better position the market for success after 2014. Not permitting a broad enough transition will hobble the companies that serve both markets, ultimately destabilizing the individual market. This is especially important to take into consideration given the goals of PPACA concerning assurance of consumer choice through Exchanges.

I believe that the U.S. Department of Health and Human Services has authority to implement a broader transition than is addressed in the interim regulation. The Public Health Service Act (PHSA) Section 2718(b)(1)(A)(ii) provides an MLR of 80 percent for both the small group and individual market, addressing them together, and notes that "the Secretary may adjust such percentage with respect to a State if the Secretary determines that the application of such 80 percent may destabilize the individual market." This provision requires the Secretary to focus on the individual market in watching for destabilization, but it does not limit the Secretary in determining which market the 80 percent can be adjusted for if there is a risk to the individual market. Therefore, the Secretary is given broad authority to adjust the MLR for both the small group and individual market if such adjustment is necessary to avoid the risk of destabilization in the individual market. Had Congress intended to limit the ability of the Secretary to protect the individual market, it could easily have addressed the MLR for the small group and individual markets separately or expressly limited the Secretary to only adjusting the MLR for the individual market. Instead, as drafted, the PHSA Section 2718(b)(1)(A)(ii) appears to acknowledge the interconnectedness of the two markets and gives the Secretary the ability to protect the individual market from destabilization that can result from this interconnectedness.

Additionally, while the interim regulation only contemplates adjusting the MLR on a state-by-state basis, I urge you to give further consideration to applying a national phase in of the MLR requirements. In limiting the MLR adjustment process to individual states, the preamble of the interim regulation focuses on the language in the PHSA Section 2718(b)(1)(A)(ii) that permits the Secretary to "adjust such percentage with respect to a State." The interpretation of this specific provision is accurate in this respect, however such analysis ignores the additional authority given the Secretary by Congress. The PHSA Section 2718(d) states that "The Secretary may adjust the rates described in subsection (b) if the Secretary determines appropriate on account of the volatility of the individual market due to the establishment of State Exchanges." This provision does not restrict the Secretary to adjusting the rates only for individual states, so it is not necessary that such a restriction be built into the regulation. Since the establishment of Exchanges will be a nationwide process, the Secretary should consider the volatility of the individual market in the nation as a whole and should not be limited to addressing that volatility only on a state-by-state basis.

In accordance with the reading of the PHSA Section 2718 addressed above, I request that you consider implementing a phased in MLR requirement to apply to both individual and small group health insurance, and to apply this transition on a nationwide basis over a six year period. I propose a transition that would begin with individual and small group carriers achieving 75 percent of the full 80 percent MLR requirement, incrementally working toward achieving 100 percent of the full 80 percent requirement by 2016, according to the following schedule:

Plan Year	Percent of MLR Goal Achieved
2011	75%
2012	80%
2013	85%
2014	90%
2015	95%
2016	100%

Implementation of the above transitional loss ratios would:

- minimize potential destabilization in the individual market;
- maintain adequate participation by health insurance issuers in all markets;
- preserve continued competition in the health insurance market;
- provide value for consumers; and
- protect consumer choice.

As noted above, I envision this as a nationwide approach. However, this request to allow a phased in transition of the MLR requirement for both the group and individual market is specifically necessary for Texas.

The Texas health insurance market is unique. Unlike some states served by a small number of issuers, the Texas individual, small group and large group market consists of a total of 132 domestic and foreign issuers, including an appreciable number of smaller issuers. However, Texas is an expansive state with a broad range of regional and population variations that do not have uniform opportunities for choice in coverage overall. Additionally, PHSA Section 2718 assumes the existence of new infrastructure and market regulations that will not be in place when the MLR is initially implemented. The transitional nature of significant market reforms in PPACA necessitates clear steps to ensure a similar transition period for the MLR requirement that does not cause instability and disruption in the marketplace.

Individual Market Implications

In Texas, individual coverage is provided on an underwritten, guaranteed renewable basis. Plans are typically priced on a lifetime loss ratio basis targeting 55 to 60 percent. The significant shift from a lifetime loss ratio to applying an annual 80 percent MLR standard could result in market destabilization. Some of the potential implications include:

- Some issuers may remain in the market but lack an effective distribution channel due to their need to significantly lower their distribution costs to meet the 80 percent MLR standard.
- Many insurance agents and brokers could discontinue selling individual health insurance if issuers materially decrease agent compensation for that product. This could inhibit consumers' access to the individual market in the years prior to the introduction of insurance Exchanges and limit the availability of people with knowledge about health insurance to assist consumers once Exchanges are implemented.
- Other issuers may decide that it is more advantageous for their long-term solvency to stop selling individual comprehensive medical insurance products, and may move to issuing short-term, limited duration coverage or hospital indemnity or other fixed indemnity insurance, which are not subject to the requirements of PPACA. While these products may appear more reasonably priced to consumers, ultimately they will not benefit consumers needing comprehensive coverage.
- To the extent that issuers withdraw from their currently in-force business, it may be difficult for their former policyholders to find new individual coverage in the transition period prior to 2014. Those with pre-existing conditions will not have access to the federal Pre-existing Condition Insurance Plan and, under Texas law, would have to pay 200 percent of the standard market rate to participate in the Texas Health Pool.
- In addition, in the current market environment where issuers are not offering child-only policies and where family policies are being rated up if children under 19 are included, currently insured consumers may become uninsured.

Small Group Market Implications

The same threat of market destabilization exists for smaller issuers in the small employer market. The risk characteristics, administrative costs and even acquisition costs of business for employer groups with a very small number of employees are similar to related costs in the individual market. Smaller issuers may find their claim costs, expenses and rebates during the next few years substantially higher than anticipated premiums. This may erode solvency stability for some carriers. In addition, insurance investors may require that these issuers withdraw from unprofitable business. This could result in:

- a loss of issuers marketing small group health products;
- decreased or lost consumer access to comparable product offerings due to the reduction or elimination of marketing channels;
- the possibility of material change to or withdrawal from existing coverage; and
- the potential for increased volatility in premium rates.

In addition, special circumstances surround the operating expenses of smaller issuers. These circumstances impact these issuers' ability to meet the MLR requirement initially, including:

- Smaller issuers have substantially higher operating expenses and acquisition costs. Maintaining an MLR formula that ignores these higher costs and imposes rebate

requirements without reference to the overall profitability of the business and without time for adjustments may result in smaller issuers being forced out of the market.

- Issuers must spread fixed costs associated with obtaining and maintaining business over the number of policies in force. For smaller issuers, this means that fixed expenses are a higher percentage of premium revenue per policy than is the case for larger issuers. Many of these issuers also have contracts in place with agents and brokers for business already on their books and cannot unilaterally change those contracts. This puts smaller issuers at an extreme disadvantage relative to large issuers with respect to meeting the MLR thresholds.

Legal Analysis of Statutes

There is a two step inquiry that is followed in determining whether a federal agency's interpretation of a statute is valid.¹ First is the question of whether Congress has directly decided the precise question at issue, and second is the question of whether the agency's interpretation of the statute is reasonable.²

In this instance, Congress has not directly decided the question at issue, which is "What approach should the U.S. Department of Health and Human Services take to address the impact of the new medical loss ratio requirements on the group and individual market, including the impact on agents and brokers that serve that market and consumers who receive their health coverage through that market?" Congress clearly leaves it to the U.S. Department of Health and Human Services to address this issue. Specifically, the PPACA provides:

- That the Secretary may adjust the percentage with respect to a State if the Secretary determines that application of the 80 percent medical loss ratio may destabilize the individual market in the State; and
- That the Secretary may adjust the medical loss ratio if the secretary determines appropriate on account of the volatility of the individual market due to the establishment of State Exchanges.

To make a reasonable interpretation of a statute, it is necessary to read the law as a whole and avoid a construction of the law that would lead to absurd results. This is a longstanding canon of construction applied by courts in interpreting statutes, and has also been referred to as a newly emerging canon in regulatory law.³ Based on this principle, in addition to looking at the provision that requires adoption of medical loss ratio requirements, the U.S. Department of Health and Human Services should consider the statutory requirements concerning State Exchanges. In addition, it is a longstanding tenet to harmonize statutes to prevent unintended consequences. Such harmonization will, in this case, not only to prevent market disruption, but also to ensure the success of the State Exchange.

The Employee Retirement Income Security Act (ERISA) became law in 1974. While Congress primarily sought to remedy improper funding by employers of retirement (pension) benefits when it passed ERISA, Congress also allowed employers to standardize welfare benefit plans (primarily health benefits) for their employees. Large employers can very easily add mere cents in pretax payroll deductions to each of their employees in their large risk pool in order to properly fund additional employees, or consultants, whose primary duty is to design, implement, and pay for welfare benefit plans. Such employees and consultants have garnered a great deal of expertise in employment benefit law that is simply not available to the small/individual market at the same cost per employee. Since small employers and individuals generally have fewer

¹ *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984).

² *Id.*

³ Cass R. Sunstein, *Avoiding Absurdity? A New Canon in Regulatory Law*, 32 ENVTL. L. REP. 11,126 (2002).

employees, or consultants, available to them, they have a greater reliance on agents and brokers to guide them.

One section in the PPACA addressing Exchanges, Section 1312, relating to "Consumer Choice," clearly needs to be taken into consideration in adopting medical loss ratio requirements. Subsection (e) of this section addresses enrollment through agents or brokers, and it calls for the Secretary of the U.S. Department of Health and Human Services to establish procedures under which a state may allow agents or brokers to enroll individuals and employers in qualified health plans as soon as those plans are offered through an exchange and to assist individuals in applying for premium tax credits and cost-sharing reductions for plans sold through an exchange. However, if *knowledgeable and experienced* agents and brokers are driven out of the market now due to the adoption of an inflexible MLR methodology in the small employer market, they will not be around to fulfill their role of serving small employers or individuals in the Exchange system as envisioned by the PPACA.

Thank you for your consideration. I look forward to continuing this discussion with you and am available to answer any questions you may have. In addition to this letter, the Texas Department of Insurance anticipates submitting written comments on the interim final regulations.

Sincerely,

A handwritten signature in black ink, appearing to read "Mike Geeslin". The signature is fluid and cursive, with a long horizontal stroke at the end.

Mike Geeslin
Commissioner of Insurance