SB 1431 Attacks Self-Insurance Option, Creates Unwanted "Exchange Protection Act" and Invites ERISA Preemption Challenge

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Some folks at CAHU have asked me why I decided to come out of my "Happy Has-Been" retirement status (referring to my no longer sitting on a CAHU or NAHU Board of Directors) to write an article… Well, I have serious concerns and thoughts on this bill, and I wanted to share them, and I'm hoping that members will still read what I have to say! So, on that note, SB 1431 in its current form is an unfair, unnecessary and unwanted bill… unless, of course, you would profit from the beloved California Exchange, scheduled for launch in the very near future, with or without PPACA on the federal level.

On April 25, the California Senate's Health Committee passed through SB 1431, a Stop-Loss Insurance Coverage bill (De Leon), with a 5-3 vote along party lines, with 3 republicans opposing and 5 democrats supporting. I was indeed there to watch the testimonies of the supporters and opposition. As a witness, I felt as though the decisions were already made before anyone presented their statements; the chairman and majority of the committee members were already prepared with their yes votes, and nothing was going to stop them. As no "Appropriations" are necessary, this bill will head straight to the Senate Floor…

And now, as I've just put the finishing touches on this article, I have been informed that *the bill was amended on May 1, and it's even worse than before! Changes to the bill now make it retroactive to January 1, 2012, so it's vital that our members know about this now!*

SB 1431 was introduced by Senator De Leon (and sponsored by Insurance Commissioner Jones) on February 24, 2012, and amended in the Senate on April 9, 2012, and now later amended on May 1. Its purpose, according to the Senate Committee on Health, is to "establish minimum attachment points for stop-loss policies to self-insured employers in the small group market", to "require guarantee issue for employees and dependents and guaranteed renewabililty of the policy for the small employer".

This bill, in my opinion, clearly attempts to eliminate competition for the California Exchange, by virtually eliminating the option for self-insurance in the small group market in California. It is currently being nicknamed " The Exchange Protection Act" by prominent members of CAHU and SIIA (phrase coined by CAHU and NAHU's own David Fear, Sr.). As you'll see below, this bill has provoked action from the Self Insurance Institute of America, and if it is signed into law, it is likely California will be engaged in an expensive ERISA Preemption lawsuit.

Organizations supporting the bill in Sacramento at the hearing included Blue Shield of California, California Physician Groups, Consumer Federation of America, Health Access California, SEIU California, and the Department of Insurance (Dave Jones, Insurance Commissioner, the Bill Sponsor). Opposing organizations included California Association of Health Underwriters (CAHU), California Chamber of Commerce, National Federation of Independent Business (NFIB), Self-Insurance Institute of America (SIIA), and Southwest California Legislative Council.

What SB 1431 Would Do

SB 1431 would require a minimum specific stop-loss deductible of $95,000 per person, and an aggregate attachment point of $19,000 per individual for employers with 50 or fewer employees. This means that a small employer would have to incur $95,000 in claims before seeking reimbursement from the stop-loss carrier, for each individual. Those attachment points basically eliminate the option to self-insure, even if you have an excellent

candidate for self-insurance. In addition, those employers who have been self-insured at lower specific and aggregate attachment points for many years would likely lose the option in the future, as they likely would not be able to afford the additional risks. I personally have two clients in that position, should this bill be signed into law. One has successfully maintained a $45,000 specific stop-loss policy (which started as low as $20,000 over 20 years ago), and the other, a $50,000 specific (which started out at $25,000). The latter was, incidentally, a larger group that reduced in size due to the economy and a merger, and is now just under 50 lives. If this bill become law, it is conceivable that they would have to terminate their self-insured plan, even after years of success, with little notice, and have to pay run-out claims (claims incurred during the plan year that are paid after the plan year ends) after the plan is forced to terminate, for a period of three to six months, plus incur the simultaneous costs of purchasing a fully insured plan for their employees; one with likely lower benefit levels and higher costs than their current self-insured plans. *In essence, they would pay double for about six months…* Why/how, please tell me, does this possibly make sense? And now, with the May 1 amendments, how will that work? My clients aren't the only ones that had stop-loss placed since January 1, 2012, and all of them now are at risk. How do you retroactively make something illegal that was sold and implemented months before the bill was signed into law?

I reached out to fellow CAHU and NAHU colleague David Fear, Sr. recently, and asked for some of his thoughts on SB 1431. I asked Dave "As a past president of CAHU and NAHU, and a former Legislative Chair and Leg Council member, you've seen your share of legislative battles. How do you think SB 1431 measures up, and how serious of a situation do you see this as for California employers?" Dave responded, " I think SB-1431 is an important issue for two reasons: First, it's about the State's indirect regulation of self-insured plans for a specific segment of employers. There are long standing court rulings that clearly indicate the States cannot do this. Employers of ALL SIZES should be concerned about this attempt. Second, this measure is an attempt by the Insurance Commissioner to 'protect' the soon-to-be-operational California State Health Benefit Exchange from perceived adverse selection by healthy small employers who may opt to self-insure their benefits and would force them to only purchase fully insured products, primarily through the Exchange."

ERISA and Self-Insurance

Since the passage of the Employee Retirement Income Security Act (ERISA) in 1974, qualified employers of all sizes have successfully self-funded their group health plans. According to the Self-insurance Institute of America, in 2010, 77 million workers and their dependents were covered by self-insured plans, which represents about one third of the private health care marketplace. Employers have sought the help of professional service providers, such as third party administrators (TPA's), specialized brokers, competitive networks of providers, pharmacy benefit managers, utilization review and case management firms, and others to assist them in creating and maintaining a viable and well cost-contained health plan. The most critical component of self-insurance, however, is medical stop-loss. This coverage provides a financial reimbursement mechanism for claims in excess of pre-determined risk thresholds. *SB 1431 imposes new regulatory restrictions on such stop-loss coverage that would in essence disallow this funding option for small employers*. With SB 1431, in most cases, employers would not be allowed to retain stop-loss coverage at levels and terms consistent with their financial risk transfer philosophies and needs.

A very important distinction that should be made is that stop-loss carriers do not pay for individual health care claims, as erroneously stated in SB 1431. Stop-loss coverage reimburses the employer/plan sponsor for claims. SB 1431, according to SIIA, has some erroneous assumptions. "It's important to be clear" stated Mike Ferguson, COO of SIIA, " that self-insured employers are financially responsible for all eligible health care claims, so it's not accurate to say [as stated in SB 1431] that an employer's financial liability is 'capped' at the stop-loss attachment levels. To put a finer point on it, stop-loss carriers do not pay individual health care claims."

ERISA Preemption

ERISA prohibits states from imposing regulations that affect the administration of self-insured group health plans. Because SB 1431 would restrict employer risk transfer arrangements, this directly affects plan administration and is therefore a likely violation of ERISA, and would invite an ERISA preemption challenge. The Self-Insurance Institute of America (SIIA) has stated that it is prepared to make that legal challenge.

One of the key testimonies on April 25 was that of Mike Ferguson, COO of SIIA, as well as a long-term friend and colleague of mine. When I first became aware of the bill contents and the hearing date, in large part due to Dave Fear, former CAHU and NAHU President, my first reaction was to contact Mike and ask SIIA to get involved. SIIA's role in legislative and lobbying activity across the nation on self-insurance issue is unprecedented. "SIIA has been the recognized leader on representing the legislative/regulatory interests of self-insured employers and their business partners for more than 30 years, " stated Mike Ferguson. " Most of our focus has been at the federal level, but we do get involved at the state level as hot issues arise." *Obviously, California's SB 1431 quickly became a hot issue*.

Mike flew in from the east coast the morning of the hearing to testify, and flew back that night. When asked why SIIA decided to get involved in the SB 1431 issue, Mike's response was "We have been highly engaged for some time on developments related to stop-loss insurance regulation because this threatens the ability of employers to self-insure. Clearly SB 1431 would have that effect in California, and it is high profile state so we have determined that a robust opposition effort is necessary." Just how robust and how necessary? *Enough to talk lawsuit…*

SIIA went on record with the California Senate Health Committee, informing them that they (SIIA) would consider initiating a legal battle in this state, as this is a prominent, high profile state. How serious is SIIA about this? "Very serious, " Mike replied. "There clearly is a legal argument that the regulation proposed by SB 1431 'relates to' self-insured ERISA plans and is therefore preempted by federal law. The open questions are 1) how strong is this argument, and 2) will our industry financially support what would be a very costly litigation effort. We are having internal discussion about both of those questions and expect to comment more as soon as we comfortable with the answers."

In SIIA's written testimony, they stated that "It is well established that state mandated benefit laws do not apply to ERISA self-insured plans. This is because such laws are preempted – or superseded-by federal law. The mandated attachment points of SB 1431 are also preempted. Simply stated," Mike continued, "this is because they affect the terms and conditions of ERISA regulated employee benefit plans."

Also part of Mike's testimony: "The rationale that attachment points can be regulated as 'insurance' is based on an inaccurate assumption that ERISA's 'savings' clause, which exempts state insurance regulation from federal preemption, permits such regulation. This legal analysis has been consistently rejected by federal courts- and the U.S. Supreme Court has declined to review."

"State laws that focus on what is known as the 'business of insurance' typically oversee the financial ability – or solvency- of carriers to pay claims. Such regulation also applies to market conduct, consumer rights, claims appeals and disclosure requirements." The testimony continued: "While some states have attempted to regulate stop-loss within its insurance oversight role, the courts have rejected such attempts that impose requirements when they relate to self-insured group health plans."

"There is no question," Mike continued, "that SB 1431's provisions would impact impermissibly on benefit risk structure, terms and conditions, and administration of ERISA plans. These provisions affect the fundamental

underlying benefit structure of self-insured plans – they clearly 'relate' to ERISA plans – the critical prerequisite to a federal preemption challenge. For these reasons, SIIA has concluded that legislation would not withstand a legal challenge."

SIIA has been involved in lawsuits in other states on ERISA issues… I asked Mike to confirm their previous successes in those states, as well as other state actions they are currently involved in. "SIIA has previously [litigated]successfully in the states of Florida and Texas in Federal Court over ERISA preemption issues and we currently have litigation pending against the state of Michigan. While none of these cases involved the same issues has California, it demonstrates the association's willingness to push aggressively back in court should states overstep their authority."

The Senate Health Committee Analysis referred to about 15 other states with stop-loss regulations. I asked Mike his thoughts on this. "You stated in your testimony to the California Senate Health Committee on Wednesday that the other states mentioned in the bill's analysis (by the committee) that have passed similar legislation may have passed laws, but that doesn't mean they are legal, and could be challenged in federal court. Would you like to comment on that?" Mike, indeed, did comment. "Sure. At the risk of contradicting my previous answer, regulations imposed by other states to dictate attachment levels simply have not been challenged in court. We'd like to have the opportunity to do so contingent on supporting legal advice and financial resources."

Other supporters seem to agree in large part to what we are saying, and added further detail and testimony. The California Chamber of Commerce, combined with National Federation of Independent Business, for example, in its letter of opposition (dated April 18, 2012), stated that they opposed SB 1431 because "it will severely limit small employers opportunity to select the most appropriate, affordable health care coverage to their employees as self-insurance. The bill proposes to regulate stop-loss insurance for small employers, most notably to require the employer to bear an unreasonable level of claims cost before stop-loss coverage applies."

Further, Marti Fisher from Cal Chamber states "The author and sponsor claim that allowing small employers to self-insure will cause insurers to only cover healthy workforces, taking them out of the Exchange, leading to adverse selection and a death spiral in the Exchange. This implication is illogical. A 'healthy' workforce is a snapshot, not necessarily a stable factor going forward. Populations deemed 'healthier' can still experience significant high dollar claims on day one due to unexpected medical events. Furthermore, the U.S. Bureau of Labor Statistics finds that employee turnover can be as high as 38 percent in some industries. The claims experience today for that workforce may be dramatically different next year due to employee turnover."

California Chamber of Commerce and NFIB also referred to a 2011 study and modeling, in which they stated that "Health Affairs[1] concludes that limiting self-insurance for small business will reduce enrollment in the exchanges somewhat, but without substantially affecting exchange premiums. The research further finds that removing the option to self-insure will cause fewer small employers to offer coverage to employees." They stated also that a RAND[2] study in 2012 came to similar conclusions, that the phenomenon of a 'death spiral' – extreme premium growth leading healthier workers to drop out, and thus to ever-higher premiums for those who remain- caused by changes in stop-loss availability, as not observed…. Furthermore, results found no major differences in benefit generosity between self-insured and fully insured plans or to a major threat of adverse selection in the small-group market after the ACA is fully implemented. *Without clear evidence of adverse risk selection within the fully insured small group market, limiting stop-loss coverage and its availability is a solution in search of a problem."*

[1] Health Affairs February 2012 "Small Firms Actions in Two Areas, and Exchange Premium and Enrollment Impact"
[2] RAND Corporation August, 2011 "Employer Self-Insurance Decisions and the Implications of the Patient Protection and Affordable Care Act as modified by the Health Care and Education Reconciliation Act of 2010 (ACA).

I say “AMEN” to the Chamber and NFIB…

Why Self-Insurance?

As a long-term self-insurance specialist, spanning over more than two decades, I have successfully administered , then later placed as a broker, a number of self- insured plans here in California. I have been involved in every aspect, from bidding stop-loss coverage, to managing TPA’s paying claims, to writing plan documents and SPD’s, to analyzing the claims experience and making recommendations for plan design to assist employers in creating and maintaining the most cost-effective, competitive health benefit plans in the market. In all these years, I have never seen such a blatant attack on a successful funding option.

While self-insurance is not for every employer, it provides a viable option for some; particularly those with strong balance sheets, stable workforces, healthy employees and dependents, those with employees in multiple states and those who wish to offer uniformity to their employees. Employers who self-insure are allowed plan design flexibility (but are subject to ERISA requirements), and a long term cost management mechanism. Self-insurance is a funding option that offers affordable coverage at a time that California employers have experienced rising health insurance costs, and many small and medium size businesses struggle to provide health coverage at all…

In my recent conversation with Dave Fear, Sr, we talked about our mutual history of working with self-insured plans. I asked Dave “Like me, you’ve done a lot of self-funding in your agency production years. How big of a threat do you feel SB 1431 is to the small group market?” Dave responded, “ For the past two years as employers of all sizes have carefully read the provisions of PPACA, they begin to see that come 2014 the rules for their fully insured plans are going to be very different from the current market: Compressed rate bands and elimination of all risk adjustment to name two of these provisions. Naturally they are going to look at their individual businesses and determine if there is a more efficient way to provide health care benefits for their employees, given the fact that the Federal Law is going to drive them into community rated pools that are going to be expensive and will provide no incentive for innovative plan designs which are a hallmark of the private benefit system of the United States.”

Employers have always enjoyed the freedom to choose their funding arrangements and make their own decisions regarding their risk and funding mechanisms. I asked Dave how much he thinks this bill, if it were to become law, would change their ability to control employers’ own destiny and choices? “ For employers with less than 51 employees, they will effectively have to ‘self-insure’ most of their risk, because specific stop-loss levels will be dictated by the law, currently proposed at $95,000 per person. Additionally, aggregate stop-loss attachment points will be set at a minimum of $19,000 per employee per year. This is *way* too much liability for a small employer to assume.”

I continued to converse with Dave on his thoughts. “Do you think the specific and aggregate thresholds included in SB 1431 would be acceptable to the small group market, and if not, why?” Dave responded, “ Absolutely not and the Insurance Commissioner knows this – he’s really trying to drive small employers to exclusively provide their health benefits through fully insured methods and specifically through the soon-to-be-operational Exchange. Most small employers are willing to look into self-funding if they have reasonable stop-loss levels such as $20,000 for specific and $5,000 for aggregate. By the way, the NAIC model for this very situation are at those two levels, yet the Commissioner wants to set this much higher than the recommended NAIC levels.”

Would this bill really change the small group market?

I asked Dave Fear how he felt SB 1431 would change the small group market in California. "It would eliminate self-funding as a viable option for employers with fewer than 51 employees. They will be forced to buy fully insured plans and perhaps 'partially self-fund' by using more expensive High Deductible Health Plans such as those for Health Reimbursement Arrangements. These products are, for the most part, much more expensive than specific and aggregate stop-loss products on the street today."

I asked further: "How do you think SB 1431 would affect the current competitiveness of the health insurance marketplace?" Dave replied, "Any time you eliminate an option available in the market, you drive up the price of remaining choices: I don't think health insurance will be any different than other products which have seen diminished competition."

The California Chamber of Commerce/NFIB stated in its opposition letter, when discussing PPACA's intent, "The Act was adopted to ensure that everyone has access to affordable health care. To that end, the Act envisions a number of different vehicles for individuals and companies to obtain coverage, and different ways to provide coverage. For example, the Act authorizes the creation of Consumer Operated and Oriented Plans (co-ops), Accountable Care Organizations (ACO), Direct Primary Care Medical Home Plans, grandfathered plans, as well as a variety of public programs in addition to the individual exchange, the SHOP exchange, and the market outside the exchange... Furthermore, current law was not eliminated and continues to provide for self-insurance. The above-listed organizations believe that this variety of alternatives allows consumers – and employers - to choose the method most appropriate for them in obtaining health care."

How do you think the excess loss/stop-loss carriers in California will react to this bill if it becomes law? Dave Fear shared his thoughts. " I'm not sure. Hopefully they will remain in the market but some may say 'ok we just won't offer our normal suite of products to employers with less than 51 employees'. By the way, I believe that definition of small employer will change from 2 to 50 to 1 to 100 in 2014. Thus I would assume that the provisions of SB-1431 will extend on up to employers with up to 100 employees by that time. Thus, I think "mid-sized" employers (51-100) would be concerned about this bill too, since it may end up applying to them in 2014."

I asked Dave why he thought the Senate Health Committee members want to pass this bill… He replied, "I don't know, you would have to ask them. I noted that the bill passed out of committee on a straight party line vote, 5 Democrats in support and 3 Republicans in opposition. The employer community appealed to members of the committee to oppose the measure and it would appear that they chose *not* to heed the request of the employer community in this regard."

Should our members and employers, and other organizations join the fight?

Is this an issue CAHU members should get up in arms for? David Fear, Sr. believes it is. **"** Yes, we should fight for the right of our clients to select the type of health benefit program that best meets their needs. This measure pretty much kills the self-funded option for employers with 50 or fewer employees."

And what about the rest of the market, the brokers, the TPAs, the business associates? "It is really important for everyone involved in the self-insurance industry to get and stay engaged as there are some powerful interest groups that would be happy if self-insurance just went away" stated Mike Ferguson of SIIA. "To keep up to date on the latest SB 1431 developments, I would suggest people check out www.facebook.com/Defeat1431."

Personally, I would ask that CAHU members participate in the Call to Action and possible Operation Shouts on this issue. We need grassroots actions, which we are quite good at in this association. In addition, I would suggest they perhaps consider helping fill the legal battle coffers. A small donation to the SIIA Legal Defense Fund would be a

few dollars well spent. There are times when many associations and organizations need to fight together. I ask you to consider joining the fight to preserve a viable and competitive option to small employers.

So, I guess the "Happy Has-Been" is back! Please help us in fighting this fight. With your help, we can succeed.

Author's Note: You can reach Dorothy Cociu at Advanced Benefit Consulting & Insurance Services, Inc., 714 693 9754, ext 3#, or by email at dmcociu@advancedbenefitconsulting.com. If you'd like to get more involved, please refer to the Facebook page set up by SIIA for our California fight at www.facebook.com/Defeat1431. *Also,* ***if you'd like to make a donation to help in the legal fight, please donate to SIIA Legal Defense Fund, and send it to SIIA, P.O. Box 1237, Simpsonville, SC 29681.*** *Every little bit will help. If we all donate a small amount, we can help SIIA help us. CAHU and NAHU are not organizations prepared to participate in a legal battle. But the CAHU Board is in support of SIIA's efforts and activities on our behalf.*

References: Senate Bill 1431, February 24, 2012, Senate Bill 1431, Amended April 9, 2012 and Amended Mary 1, 2012, Senate Committee on Health, Analysis, Consultant Trueworthy, April 11, 2012, for Hearing Date April 11, 2012, Testimony SIIA, April 25, 2012, California Chamber of Commerce/National Federation of Independent Business, Memo to Members of Senate Health Committee, Subject: SB 1431 (DeLeon) Stop-Loss Insurance Coverage Scheduled for Hearing- April 25, 2012, Oppose.

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