

Analysis: Section 125 Plans and a Virginia Health Insurance Exchange

Presented to the:

Joint Commission on Health Care

September 4, 2008

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Agenda

- Study Background
- Section 125 Plans
- Health Insurance Exchange
- Other Issues
 - Access to Health Insurance Options
 - Update: Riverside Share Program
 - Update: Maryland Health Insurance Partnership
- Policy Options

Organizations Contacted

- Agency for Healthcare Research and Quality
- Anthem
- Asset Protection Group, Inc.
- BB&T Insurance Services, Inc.
- Benefit Solutions Inc.
- Connecticut Business and Industry Association
- Connecticut General Assembly Office of Legislative Research
- Independent Insurance Agents of Virginia
- Internal Revenue Service
- Iowa Insurance Division
- JLARC
- Maryland Health Care Commission
- Massachusetts Commonwealth Connector
- Massachusetts Joint Committee on Health Care Financing
- Minnesota Department of Health
- Missouri Joint Committee on Legislative Research
- National Conference of State Legislators
- National Federation of Independent Businesses
- Office of the Secretary for Health and Human Resources
- Rhode Island Office of the Health Insurance Commissioner
- Riverside Health System
- State Corporation Commission
- Total Administrative Services Corporation
- Virginia Association of Health Underwriters
- Virginia Attorney General's Office
- Virginia Commonwealth University
- Virginia Association of Health Plans
- Virginia Chamber of Commerce
- Virginia Department of Business Assistance
- Virginia Department of Health
- Virginia Department of Tax
- Virginia Employment Commission
- Virginia Farm Bureau
- Virginia Health Underwriters Association
- Virginia Local Commissioner's of Revenue
- Your Benefits Partner

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Study Background

Health Insurance Affordability Is the Primary Barrier

- Estimates range from 9% - 15.5%
 - 632,000 – 1 million non-elderly Virginians
- “Affordability is the primary barrier to obtaining health insurance”
 - JLARC health insurance study finding

Source: Options for Extending Health Insurance to Uninsured Virginians, Slide 4 and 5, JLARC, December 11, 2006 5

Employers Have Been a Primary Source of Working Non-Elderly Obtaining Health Insurance

60% of firms offered health insurance in 2006; down from 69% in 2000

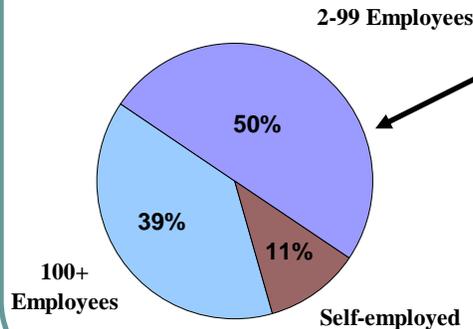
- Approximately 77% of covered employees pay 0% - 50% of premium costs (2006)
- Virginia health insurers often require significant employer contribution for small group plans
 - frequently 50% of premium

| # Employees | % Offering Health Benefits (2006) |
|------------------|-----------------------------------|
| 3 to 9 | 45% |
| 10 to 24 | 76% |
| 25 to 49 | 83% |
| 50 to 199 | 94% |
| 200 or more | 99% |
| All Firms | 60% |

Sources: KFF/HRET 2007 Employer Health Benefits Survey and discussion with Virginia Association of Health Plans 6

50% of the Working Uninsured Work for Smaller Employers

Distribution of Uninsured In Working Families



Uninsured employees that work in smaller businesses (2-99 employees) account for 50% of Virginia's working uninsured

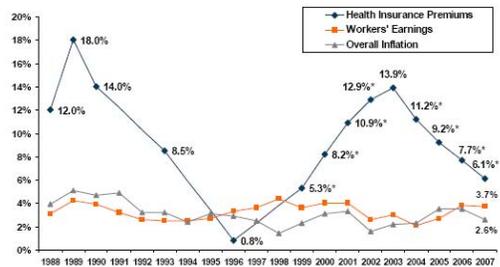
Note: Only 48% of small employers (2-50) offer health insurance to their employees

Source: *Options for Extending Health Insurance to Uninsured Virginians*, JLARC, December 11, 2006

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Health Insurance Premiums Continue to Increase

Exhibit 1: Increases in Health Insurance Premiums Compared to Other Indicators, 1988-2007



- Premiums are rising at a slowing rate
- Rate of increase is still greater than workers' earning increases

*Estimate is statistically different from estimate for the previous year shown (p<.05). No statistical tests are conducted for years prior to 1999.
 Note: Data on premium increases reflect the cost of health insurance premiums for a family of four. The average premium increase is weighted by covered workers.
 Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2007; KPMG Survey of Employer-Sponsored Health Benefits, 1990, 1996; The Health Insurance Association of America (HIAA), 1989, 1999, 1990; Bureau of Labor Statistics, Consumer Price Index, U.S. City Average of Annual Inflation (April to April), 1988-2007; Bureau of Labor Statistics, Seasonally Adjusted Data from the Current Employment Statistics Survey, 1988-2007 (April to April).

Sources: Kaiser Family Foundation and Health Research Educational Trust, *Employer Health Benefits* (2007) Catlin, et al., *National Health Spending In 2005: The Slowdown Continues*, *Health Affairs* 26 (1): 142 (2007)

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Background: Health Care Costs Study

- JCHC recommended in 2008 JCHC study the advisability of:
 - i) establishing a Virginia health insurance exchange targeted for small businesses,
 - ii) increasing employer adoption of Section 125 plans, and
 - iii) any other health insurance issues as deemed appropriate.

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Section 125 Plans

Section 125 Plans Defined

- Enables employees to purchase health insurance policies with pre-tax dollars
 - Refer to Section 125 of the U.S. Internal Revenue Code
 - Group Plans (with or without employer contribution)
- Employee savings can be 25%-40% per dollar contributed towards health insurance
 - FICA (Social Security and Medicare payroll tax), federal and state income taxes
- Employers can decrease tax liability by decreasing its payroll tax if employees contribute to their health care premiums

Source: States use 'Cafeteria plans' to expand health insurance coverage, Cauchi NCSL Health Program, September 2008

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About Section 125 Plans

- Employers which do not offer health insurance are not benefited as there would be no reduction in payroll taxes paid
- Not all entities and individuals can participate including:
 - Self-employed individuals
 - Partners in a partnership
 - Outside directors, limited partners and members in an Limited Liability Corporations (LLCs)

Source: Section 125 Flexible Benefit Plans, Benefit Solutions.

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Section 125 Plans Are Not Helpful When

- Low-income employees do not make enough to afford health insurance
 - Less than 200% of the Federal Poverty Guideline
- Employers that pay 100% of the employees' premiums are not benefited by setting up a plan
 - No payroll tax for employers or employees to deduct from wages or salary

Sources: Interviews with representatives from Independent Insurance Agents of Virginia and Virginia Health Insurance Underwriters, August 2008.

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Types of Section 125 Plans

- Section 125 plans can address
 - Premium Only Plans
 - Flexible Spending Accounts (FSA)
 - Medical Expenses
 - Dependent Care Expenses
 - Full Flexible Benefit Plan with Benefit Credits

Focus of the Presentation is increasing employer adoption of Section 125 - Premium Only Plans

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Section 125 Plan Requirements

- Plan must delineate:
 - Description of the benefits that may be elected
 - Eligibility rules
 - Method, timing and irrevocability of participant elections
 - Manner of any employer contribution
 - Maximum amount of employer and employee contributions under the plan
 - The Plan Year
- Plan must be adopted by employer

Source: Helping Your Employees Connect to Good Health: Section 125 Plan Handbook for Employers, Massachusetts Commonwealth Connector, Version 2.0 (July 1, 2007)

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Section 125 Effect on Premium Cost: Employee Illustration # 1

Individual earning \$50,000 Annually (~\$24/hour) = 409% of Federal Poverty Guidelines

| | Single |
|--|--------------|
| VA Small Group avg. monthly premium (2006) | \$ 246 |
| Payroll deduction amount (through 125 plan) | \$ 246 |
| Reduction in FICA tax → 7.65% | \$ 19 |
| Reduction in federal tax liability → 18% | \$ 44 |
| Reduction in VA state tax liability → 9.2% | \$ 13 |
| Net premium cost to employee (including after tax-savings) | \$ 170 |
| Total Monthly Tax Savings → 31% | \$ 76 |

Sources: Internal Revenue Service and Virginia Department of Taxation

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Section 125 Effect on Premium Cost: Employee Illustration # 2

Married Worker with Two Children earning \$70,000 Annually
(~\$33.65/hour) = 339% of Federal Poverty Guidelines

| | | Family of 4 |
|---|--|------------------------|
| VA Small Group avg. monthly premium (2006) | | \$ 645 |
| Payroll deduction amount (through 125 plan) | | \$ 645 |
| Reduction in FICA tax → 7.65% | | \$ 49 |
| Reduction in federal tax liability → 15% | | \$ 97 |
| Reduction in VA state tax liability → 5.4% | | \$ 35 |
| Net premium cost to employee (including after tax-savings) | | \$ 464 |
| Total Monthly Tax Savings → 39% | | \$ 181 |

Sources: Internal Revenue Service and Virginia Department of Taxation

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Section 125 Effect on Premium Cost: Employee Illustration # 3

Married Worker with Two Children earning \$50,000 Annually
(~\$25/hour) = 235% of Federal Poverty Guidelines

| | | Family of 4 |
|---|--|------------------------|
| VA Small Group avg. monthly premium (2006) | | \$ 645 |
| Payroll deduction amount (through 125 plan) | | \$ 645 |
| Reduction in FICA tax → 7.65% | | \$ 49 |
| Reduction in federal tax liability → 13% | | \$ 87 |
| Reduction in VA state tax liability → 5.2% | | \$ 33 |
| Net premium cost to employee (including after tax-savings) | | \$ 476 |
| Total Monthly Tax Savings → 39% | | \$ 169 |

Sources: Internal Revenue Service and Virginia Department of Taxation

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Section 125 Effect on Premium Cost: Employer Illustration # 1

Small firm with 10 employees has an annual payroll cost of \$500,000

| | \$ 125 Plan w/o POP | \$ 125 Plan w/ POP |
|---|------------------------|-----------------------|
| Annual Payroll | \$ 500,000 | \$ 500,000 |
| Employee payroll deduction amounts (VA small group premium average (2006) – 5 single and 5 families of 4) | \$ 0 | \$ 53,460 |
| Taxable Payroll → | \$ 500,000 | \$ 446,540 |
| Annual Social Security Tax Rate 7.65% | | |
| Annual Social Security Tax → | \$ 38,250 | \$ 34,160 |
| Employer Annual Tax Savings with Section 125 Plan | | \$ 4,090 |

Source: Internal Revenue Service

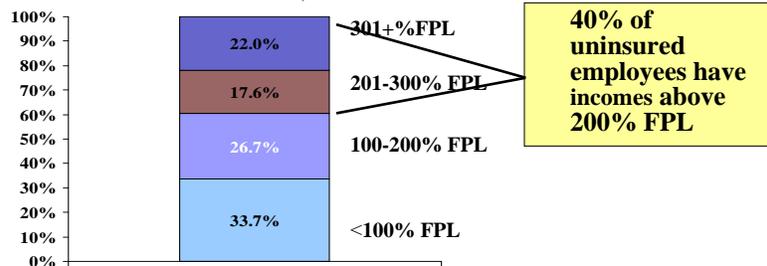
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Which Employees Would Be Affected?

- Employees that can afford and purchase health insurance policies can be assisted

Note: 200% FPL is a lower-end affordability threshold

Virginia Uninsured by Federal Poverty Level (FPL) (2005 & 2006)



Source: Profile of Virginia's Uninsured, Urban Institute Presentation to Governor's Health Reform Commission, Health Care Access Workgroup, December 7, 2006

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Virginia Small Businesses Are Much Less Likely to Offer Pretax Savings

| Employers Offering Health Coverage w/o Pretax Savings | # of Employees | |
|---|----------------|-----|
| | Less than 50 | 50+ |
| % of Employers | 68% | 8% |
| % of Employees Enrolled | 52% | 5% |

| | |
|-------------------|-------------------|
| 291,000 employees | 139,000 employees |
|-------------------|-------------------|

Arrows point from the 291,000 and 139,000 employee counts to the 52% and 5% enrollment percentages in the table above.

Note: If employer pays 100% of health insurance cost then there is no need for a Section 125 plan

Source: Unpublished estimates for Virginia provided by the Agency for Healthcare Research and Quality

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Why Haven't More Businesses Adopted Section 125 Plans

- Employer lack of knowledge
- Perception of:
 - Significant increased administrative burden
 - Cost
 - Time it takes to learn and develop plans
- Not all business owners can receive pretax benefits toward their premiums
- Tax consequences if plan not correctly set-up

Sources: Interviews with representatives from Independent Insurance Agents of Virginia, Virginia Association of Health Plans, and Virginia Health Insurance Underwriters, August 2008.

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Potential Benefits of 125 Plans

- Section 125 plans can be set up for as little as \$100
- Profits can increase for employers that offer health insurance
- Employee health insurance costs can be reduced
- Increased health insurance adoption can improve health of employer's workforce
- Many parties can assist in creation of plans:
 - Health insurance brokers
 - Health insurers
 - Third-party administrators
 - CPAs
 - Attorneys

Sources: Interviews with representatives from Independent Insurance Agents of Virginia, Virginia Association of Health Plans, and Virginia Health Insurance Underwriters, August 2008.

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Initiatives in Other States

- Massachusetts – requires employers with 11 or more employees to offer at least a “premium only” Section 125 plan
 - Tax consequence if the employer does not contribute a portion to employee health insurance
 - State created document detailing how to set up plan with sample form
- Rhode Island – requires use of Section 125 plans for employers with 25 or more employees
 - No requirement for employers to contribute to the plans

Source: States use 'Cafeteria plans' to expand health insurance coverage, Cauchi NCSL Health Program, September 2008

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Initiatives in Other States

- Minnesota –employers affirm that they have read about Section 125 Plans or have a Section 125 Plan in place
- Iowa – Commissioner of Insurance required to assist small employers with implementing and administering Section 125 plans through information on website

Source: States use 'Cafeteria plans' to expand health insurance coverage, Cauchi NCSL Health Program, September 2008

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Possible Avenues to Encourage Section 125 Plan Adoption

- Websites
 - Virginia Business Portal
 - Business One-Stop - Virginia Department of Business Assistance
 - Virginia Health Information (VHI)
 - InsureMoreVirginians - Department of Health
 - Bureau of Insurance – State Corporation Commission
- Agencies that can assist small businesses regarding health insurance
 - Department of Business Assistance
 - Bureau of Insurance
 - Department of Health
- Professionals that serve small businesses
 - Brokers
 - Insurers
 - Third-party administrators
 - CPAs
 - Attorneys

Sources: Interviews with representatives from Independent Insurance Agents of Virginia, Virginia Association of Health Plans, and Virginia Health Insurance Underwriters, August 2008.

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Methods to Increase the Adoption of Section 125 Plans

- Amend the *Code of Virginia* to mandate that employers offer a Section 125 Plan if all of the following provisions are met:
 - 11 or more full-time employees,
 - Group health insurance is offered, and
 - Employee pays some part of the health insurance premium
 - (Option 2)
- Provide Section 125 Plan information to employers on state website, information may include:
 - Brief document highlighting Section 125 Plan benefits
 - Detailed document with Section 125 Plan requirements and adoption details
 - Detailed document with Section 125 Plan requirements and adoption details with sample Section 125 Plan adoption forms
 - (Options 3, 4 and 5)

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Methods to Increase the Adoption of Section 125 Plans (Continued)

- Amend the *Code of Virginia* to require employers with 11 or more full-time employees to affirm either:
 - Employer has read the state-created document regarding Section 125 Plans, or
 - Employer has a Section 125 Plan
 - (Option 6)
- Consider including Section 125 plan information on the State's health insurance broker examination.
 - (Option 7)

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Methods to Increase the Adoption of Section 125 Plans (Continued)

- Work to increase adoption through awareness of Section 125 Plans through public-private partnership with:
 - Virginia Chamber of Commerce Newsletter
 - National Federation of Independent Businesses – Area Action Council meetings
 - (*Options 7 and 8*)

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Health Insurance Exchange

Health Insurance Exchange Benefits and Types

- **BENEFITS:** Exchanges' goals are:
 - Promote competition
 - Provide consumers a single access point for:
 - A wide variety of high-quality of health insurance products
 - Understandable and complete information of products
- **TYPES:** Exchanges may:
 - Be a state or private entity
 - Be of large or small scope
 - Apply to either the individual or small group insurance market, or both
- Other state insurance reforms have occurred in concert with the creation of a health insurance exchange to further its ability to execute its role

Source: Health Insurance Exchange Study, Minnesota Department of Health, February 2008,

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Functions of a Health Insurance Exchange

- Single point of:
 - access to multiple insurance products
 - payment to multiple health insurers
- Exchange Does Not purchase policies
- Employees are allowed to choose best health insurance product for their situation, if other reforms are in place

Source: Health Insurance Exchange Study, Minnesota Department of Health, February 2008,

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Functions of a Health Insurance Exchange (Continued)

- Limited health benefits administration provided for employers
- Exchange may allow for:
 - Decreased premium cost by increasing competition between insurers
 - Individuals with multiple employers combine employer contributions toward health insurance

Source: Health Insurance Exchange Study, Minnesota Department of Health, February 2008.

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Current Health Insurance Exchanges

States with Exchanges:

Connecticut, Massachusetts, Washington



Massachusetts Role for Its Exchange

- Promote cost-effective high quality plan
- Decrease administrative health benefits burden for smaller business
- Facilitate pretax premium purchases through Section 125 plans

Sources: State Coverage Initiatives website at statecoverage.net and an interview with Sara Nolan, Senior Researcher, *Massachusetts Joint Committee on Health Care Financing*, August 2008.

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Establishing a Health Insurance Exchange is a Significant Investment

- An organization (public or private) would need to take on the administrative role of:
 - Deciding which insurers may offer products
 - Deciding types and standards of product offerings
 - Advising employers and employees on health products offered
 - Monthly billing to employers for insurance premiums
 - Payment of policy premiums to insurers

Initial Operational Cost of Massachusetts Exchange
\$25 Million (2006)

Sources: Health Insurance Exchange Study, Minnesota Department of Health, February 2008, and an Interview with Sara Nolan, Senior Researcher, Massachusetts Joint Committee on Health Care Financing, August 2008.

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Health Insurance Exchanges Are Costly and May Not Decrease Premium Costs

Implications for Creating an Exchange in Virginia

Substantial state funding needed

Premium rates may not decrease

Initial appropriation was \$25 million for exchange in Massachusetts

Virginia's Small-group health plan premiums were ranked 3rd least expensive in the U.S (2006)

Source: American Health Insurance Plans' Center for Policy and Research, *Small Group Health Insurance in 2006*, September 2006.

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Other Issues

Finding All Health Insurance Options

- There is no place employers can go to consistently find all of the health insurance options in their area
- Market Breakdown: Some employers are not aware/misinformed of health insurance options

Enhancing Consumer Avenues to Virginia's Health Insurance Options

Remedy: Establish website listing of health insurers that offer coverage by locality with contact information

- Workgroup to develop website:
 - National Federation of Independent Businesses
 - Virginia Association of Health Plans
 - Virginia Association of Health Underwriters
 - Virginia Chamber of Commerce
 - Virginia Department of Health
 - Virginia Department of Business Assistance
 - Virginia Health Information (VHI)
 - (*Option 10*)

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Riverside Share Program for the Working Uninsured

- Riverside Health System Foundation donated \$1 million over two years
 - \$100 per individual per month
 - Can serve 500 individuals
 - Working with Anthem to include HMO products
- Plan Specifics
 - Employee pays 1/3 of health insurance cost
 - Employer could not have offered insurance in the last 6 months
 - Employee's income is \leq 200% FPL
 - Open to employee and spouse
 - Children can be enrolled in FAMIS

Source: Interview with Sally Hartman, Vice President, Riverside Health System, August 2008.

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Maryland Health Insurance Partnership

Partnership Facts

- Employer assistance:
 - up to 50% of the premium cost
- Expected enrollment
 - 1500 employers
- Year 1 appropriation
 - \$15 million
- Enrollment starts September 9th
- Coverage begins October 1st

Employer Requirements

- 2-9 employees
- Did not offer insurance in previous 12 months
- Average employee wage
 - under \$50,000
- Must have Section 125 Plan

Source: Interview with Nicole Stallings, Maryland Health Care Commission, August 2008.

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Policy Options

Policy Options

Option 1: Take no action

Option 2: Amend the *Code of Virginia* to mandate that employers offer a Section 125 Plan if all of the following provisions are met:

- 11 or more full-time employees,
- Group health insurance is offered, and
- Employee pays some part of the health insurance premium

Note: No requirement for employers to provide health insurance or contribute to plan premiums.

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Policy Options

Option 3: Request by letter of the Chairman that the Department of Human Resources Management (DHRM) in consultation with the Department of Business Assistance (VDBA) create a:

- Brief electronic document that highlights Section 125 benefits to post on the VDBA website and on Virginia's business portal website.

Option 4: Request by letter of the Chairman that the Department of Human Resources Management in consultation with the Department of Business Assistance (VDBA) create a:

- Detailed electronic document that highlights Section 125 benefits; requirements for adoption; and COBRA, ERISA and HIPPA implications for posting on the VDBA website and on Virginia's business portal website.

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Policy Options

Option 5: Request by letter of the Chairman that the Department of Human Resources Management in consultation with the Department of Business Assistance (VDBA) create a:

- Detailed electronic document that highlights Section 125 benefits; requirements for adoption; COBRA, ERISA, and HIPPA implications; and a simple Section 125 plan form for posting on the VDBA website and on Virginia's business portal website.

Option 6: Amend the *Code of Virginia* to require that employers affirm on the Virginia Department of Taxation Form VA-6 that:

- Employer has a Section 125 Plan, or
- Employer has read the State-created document regarding Section 125 Plans.

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Policy Options

Option 7: Request by letter of the Chairman that the State Corporation Commission consider and report to JCHC on including Section 125 Plan information on both the Health and the Life & Annuity & Health insurance examinations.

Option 8: Request by letter of the Chairman that the Virginia Chamber of Commerce inform its membership of Section 125 Plans and associated benefits through its newsletter.

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Policy Options

- **Option 9:** Request by letter of the Chairman that the National Federation of Independent Businesses/Virginia include Section 125 Plans as part of the Federation's Area Action Council meetings with small businesses.

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Policy Options

- **Option 10:** Include in the 2009 workplan, that the Joint Commission convene a workgroup to compile information needed for an informational website on health insurers to be hosted by Virginia Health Information (VHI) with appropriate linkages on other state websites.
 - The workgroup to develop the website should include:
 - National Federation of Independent Businesses
 - Virginia Association of Health Plans
 - Virginia Association of Health Underwriters
 - Virginia Chamber of Commerce
 - Virginia Department of Health
 - Virginia Department of Business Assistance
 - Virginia Health Information.

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Public Comments

- Written public comments on the proposed options may be submitted to JCHC by close of business on October 6, 2008.
- Comments may be submitted via:
 - E-mail: sareid@leg.state.va.us
 - Fax: 804-786-5538
 - Mail: Joint Commission on Health Care
P.O. Box 1322
Richmond, Virginia 23218
- Comments will be summarized and presented to JCHC during its October 23rd meeting.