

Market Rules and Plan Participation: Adverse Selection and Role of Exchanges

Legislative Commission on Health Care Access:
Exchange Work Group

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Overview

- What is Adverse Selection
- Tools to Minimize Adverse Selection
- PPACA Provisions Regarding Adverse Selection
- Comparison General Roles for Exchange (see handout)



Adverse Selection

- The tendency of higher risk persons/groups to seek coverage more than less risky persons/groups
- The separation of risk into different insurance arrangements
- Typically results from information asymmetry
- Left unchecked, could lead to “death spiral”



Tools to Minimize Adverse Selection

- Medical Underwriting
- Mandatory Purchase
- Pre-existing Exclusions
- Waiting Periods
- Open Enrollment Periods



PPACA Exchange Adverse Selection Provisions

- **Why is adverse selection an issue for Exchanges:**
 - When characteristics of products offered inside vs outside a market/pool are different and lead to separation of risk. Situation can result in higher risk, higher premiums, and lower enrollment inside vs outside a market/pool that continues over time (death spiral).
 - Example: Purchasing pools enacted by many States in the 1990s (separate risk pools, different rules, and mobile population)
- **PPACA provisions to mitigate adverse selection with Exchanges:**
 - Single risk pool inside and outside Exchange
 - Minimum benefit level
 - Same rating/underwriting rules inside and outside Exchange
 - Same premium for same products offered inside and outside Exchange
 - Exchange subsidies
 - Risk adjustment inside and outside Exchange



PPACA Exchange Risk Pooling Provision

- Under PPACA, insurers must include individual market/small group products inside and outside an Exchange in the same risk pool.
- How could this work in the pricing of products:
 1. Base pricing for all products based on trend of whole market
 2. Adjust for product characteristics (benefits, provider network)
 3. Adjust for assumed risk selection and actual risk experience of individual products
 4. Adjust for modified community rating factors (age, geography, etc) and wellness discounts for individual enrollees
- If there are differences between an Exchange and the outside market related to these four areas, adverse selection could occur.



Potential for Exchange Adverse Selection

- 1. Base pricing for all products based on trend of whole market**
 - Issue: PPACA does not require insurers to participate inside and outside an Exchange. For example, insurers could have one subsidiary in an Exchange and another operating outside and avoid risk pooling provision.
- 2. Adjust for product characteristics (benefits, provider network)**
 - Issue: PPACA requires plans in an Exchange, but not the outside market, to be certified. Different rules for network adequacy could exist inside vs outside an Exchange and lead to risk segmentation.
- 3. Adjust for assumed risk selection and actual risk experience of individual products**
 - Issue: PPACA requires the same products inside and outside an Exchange to charge the same premium, but insurers do not have to offer the same plans inside and outside an Exchange. Different products inside vs outside Exchange could segment risk. Can potentially mitigate this problem by not allowing insurers to price based on assumed risk selection or actual risk experience of products.



General Exchange Roles

- **Facilitator:** Offers all products available in a market and applies certification rules to all products. Could use ratings or other incentives to guide consumers to high-value plans.
- **Selector:** Selects a limited number of plans/products that voluntarily want to participate based on criteria such as value. May or may not apply certification rules to all products.
- **Purchaser:** Uses a bidding process/negotiates with health plans that voluntarily want to participate. May or may not apply certification rules to all products.
- **See handout for comparison of general Exchange roles**

