AMERICAN ACADEMY *of* ACTUARIES

November 23, 2009

The Honorable Tom Harkin, Chairman
U.S. Senate Committee on Health, Education, Labor and Pensions
428 Senate Dirksen Office Building
Washington, DC 20510

The Honorable Max Baucus, Chairman
U.S. Senate Committee on Finance
219 Senate Dirksen Office Building
Washington, DC 20510

Dear Senators Harkin and Baucus –

On behalf of the American Academy of Actuaries'[1] Health Practice Council, I would like to offer the following comments in response to your request for information related to the effect of "grandfather provisions" within the recently-introduced *Patient Protection and Affordable Care Act*. With the proposed implementation of a number of insurance market reforms, including implementation of guaranteed issue, prohibition of rating based on health status, and the narrowing of age bands, some have expressed concerns about the potential for "rate shock," defined as individuals experiencing significantly higher premiums in the reformed market.

The *Patient Protection and Affordable Care Act* contains a number of provisions related to the grandfathering of coverage for individuals who wish to keep their existing coverage. The legislation would grandfather coverage (individual and group plan policies) in which the individual is enrolled at enactment; retain the same rating rules for grandfathered coverage (i.e., new market reforms would not apply); allow for the renewal of that coverage, limited to the individual and their dependents; and allow group health plans in effect on the date of enactment to enroll new employees and dependents. Furthermore, under the individual mandate to be established by this legislation, grandfathered coverage would be considered "minimum essential coverage."

To the extent that proposed market reform provisions could result in significant premium increases for individuals with existing coverage (sometimes referred to as "rate shock"), the grandfather provisions included in the *Patient Protection and Affordable Care Act* would insulate individuals with existing coverage from experiencing that rate shock.

Individuals and small-group employees who currently have health insurance would be able to choose between their existing coverage and coverage through the new system. In most states, the market rules under which the existing grandfathered policies were priced and sold would be very

[1] The American Academy of Actuaries is a professional association with over 16,000 members, whose mission is to assist public policymakers by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

different from those of the new system. As a result, some individuals and small employers will find coverage under the new system less expensive, while others will find it more expensive, compared to what they currently pay. In general, the differences in rating rules would tend to make the new system more attractive to older and less healthy individuals and groups, while younger and healthier individuals would be more likely to find their existing policies more affordable.

Thus, there will be economic incentives for older individuals and individuals who have "substandard" premiums in the current individual market to drop out of their existing grandfathered plans. Younger individuals and individuals with "preferred" premiums will have incentives to remain in their grandfathered plan. As older and less healthy individuals leave the pool of grandfathered policies, these blocks of grandfathered policies could experience premium increases lower than medical trend. However, over time these blocks would likely shrink due to attrition, meaning that administrative expenses would have to be distributed over a smaller pool. In addition, policyholders in these blocks will age, and some will develop serious health conditions. These factors will tend to create upward pressure on premiums.

The presence of the new, guaranteed issue market ensures that no one would be confined to a grandfathered policy. This should mitigate any rate spirals; as premiums for grandfathered policies rise to the level of the new market, policyholders would move to avoid further premium increases.

If you have any questions or would like to discuss these comments further, please feel free to contact Heather Jerbi, the Academy's senior health policy analyst, at 202.785.7869 or Jerbi@actuary.org.

Sincerely,

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Vice President, Health Practice Council
American Academy of Actuaries