

Rating and Underwriting: Individual Health Insurance

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Individual (Non-Group) Health Insurance

- Status Quo (“SQ”):
 - 17 million covered individuals in 2007
 - Most states:
 - Do not require Guaranteed Issue (GI)
 - Do not restrict pre-existing condition exclusions
 - Do not limit premium variation to any significant degree

SQ: Categories of Non-Group Insurance

- Individually underwritten policies
- Federally guaranteed issue policies (If you lose your job)
 - COBRA continuation policies
 - Most with ESI qualify for either 18 or 36 months
 - Premium is 102% of average total premium for employer's plans
 - HIPAA continuation policies
 - Available within 63 days after COBRA period ends
 - Benefit/plan types are highly limited, but no health restrictions
 - Wide variation in premiums
 - High risk pools only in some states (rather than these policies)

Individual Health Insurance Issues

- “Mixed bag” of premiums and coverage
 - Initial underwriting effective in eliminating likely high cost applicants
 - Lower premiums for best risks
 - High variance in premiums
 - » Age/gender factors may be in a 6:1 range or more
 - » Rate-ups for those with certain conditions can increase premiums to 250% of “standard premiums” for persons of same age
 - » Total may vary by factor of 10x (or more)
 - Most individuals choose higher deductible plans to further reduce premiums
 - Other actions may result in high premium increases for renewing policy holders

Individual Health Insurance Issues

- Pre-existing condition exclusions and “post-claims” underwriting may limit coverage
- Rescission of policies
 - If an insurer finds the policyholder lied or withheld medical history, it may cancel the policy
 - Some insurers under fire for canceling policies over “minor” mistakes by applicants
- Administrative costs are high (30-35% of premium) relative to other coverage types
 - Sales and commission expense are large portion

SQ: Underwriting

- In most states, each person is tightly underwritten at issue for health conditions:
 - Generally an “expandable” set of +/-10 basic health questions; more questions asked about specific conditions, if any
 - “Have you seen a doctor?”
 - “Do you have a heart condition?”
 - Four possible outcomes:
 - Accept at standard (low) premiums
 - Add a “rate-up” to premiums for existing conditions
 - Exclude specified pre-existing conditions from coverage for some period
 - Decline coverage

SQ: Underwriting

- Premiums at issue of policy:
 - “Standard” premiums typically based on age, gender, geographic area, tobacco use (known as case characteristics)
 - 20% to 30% of applications getting a **modified** offer---Percentage depends on:
 - How much agent pre-screening occurs
 - Whether insurer uses only rate-ups or exclusions
 - Premiums can reflect either:
 - Rate-ups only
 - Exclusion of pre-existing conditions, or
 - Both

SQ: Underwriting

- Healthy individuals (e.g., recent college grads) have low, age-rated standard premiums
- Rate-up individuals might pay as little as 10% more or up to 250% of “standard” premiums
 - Rate-ups generally less than 150% as insurers more likely to deny coverage
- Pre-existing condition individuals might pay lower rates, but not have coverage for specified conditions
 - Insurers have differing standards
 - Some might allow a minor condition, while others would exclude coverage
- In comparison, COBRA premiums might be higher at most typical employers for employees younger than age 50

Rating Rules in Some States

Rating Bands

- Some states (mostly in the Northeast) restrict the ability to rate for health risk and case characteristics (age, gender, geographic area or tobacco use)
- A few states restrict rates for only case characteristics, but not necessarily for health rate-ups
- A few states have restrictions on maximum rate-ups

Survey of State Rate Restrictions

- Only half of surveyed states have restrictions on ranges of rates or rate increases
 - Range by age -- from 1:1 to 5:1
 - Range by rating area -- from 0.8:1 to 5:1
 - Health status, including smoking -- some +/-35%, some 1.5:1, one at 15% variance
 - Rate increase limits -- “trend + 20%,” “trend+15%+age change,” “No more than 25% from all sources”
- Some states do not have jurisdiction on premium rates for out-of-state master policies
 - Little rate regulation of these policies

Source: American Academy of Actuaries Rate Filing Task Force, Appendix F, May 12, 2004

Renewal Premiums

- Policies are Guaranteed Renewable, so can't be canceled
- Generally, all policies in the same block are rated together
 - A “block” of policies is usually a group of enrollees of various ages in the same product, same issue period (e.g., 3-5 year span) and perhaps the same region
 - All policies will increase for block's trend, plus additional increase for “deductible leveraging” as paid claims increase faster than trend due to effect of big deductible on remaining claims
 - Premiums are usually age-rated and increase every year for this factor also
 - “Wearing off” of underwriting (regression to the mean) may also add to increase over 3-5 years, if block is not replenished with new policies
- Most states prohibit “re-underwriting,” giving higher rate increases to some with lower increases to the healthiest

Glossary of Insurance Terms

- **Active Life Reserves** -- funds held by an insurer that recognize lifetime total costs of a policy. In early years after policy issue, paid claims are low but Active Life Reserves are set up to assure premium stability in later years with high paid claims.
- **“Block of Policies”** -- a group of enrollees of various ages in the same product, same issue period (e.g., 3-5 years) and perhaps the same region.
- **“Deductible Leveraging”** -- because cost increases apply to all claim costs, the amount of paid claims minus a “frozen” deductible will increase at a faster rate than just the rate of growth of all services only.

Glossary of Insurance Terms

- Incurred Claims
 - For group policies, generally paid claims plus claims “in the pipeline” for payment
 - For non-group policies, paid claims + “in the pipeline” claims + Active Life Reserves
- Medical Loss Ratios -- the ratio of health claims (without admin) to premium paid
- Paid Claims -- only actual health claims for services paid in the reporting period