

Health Insurance: Small is the New Large

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Annie L. Mach, Analyst in Health Care Financing (amach@crs.loc.gov, 7-7825)

Background

The group health insurance market is divided into large- and small-group markets. Historically, employers with 50 or fewer employees were considered small and could purchase health insurance coverage in the small-group market. The Patient Protection and Affordable Care Act (ACA; [P.L. 111-148](#), as amended) expands the definition of small employer to include employers with 100 or fewer employees. States must implement the expanded definition for plan years beginning in 2016 and have the option of implementing the expanded definition prior to 2016.

No states have yet implemented the expanded definition. As described in greater detail by the [American Academy of Actuaries](#), the change in the definition has potential implications for employers with 51-100 employees and for current small employers.

Potential Implications for Employers with 51-100 Employees

State and federal requirements do not always apply uniformly to the small- and large-group markets. Employers that move from the large-group market to the small-group market will likely see the effects of the different requirements in the types of coverage available and in the cost of coverage. Discussing the differences in state requirements is beyond the scope of this report, but some federal requirements are noted below.

[Fully insured plans](#) offered in the small-group market must cover the [essential health benefits \(EHB\)](#), and they must comply with [minimum actuarial value requirements](#). Because of these requirements, the small-group plans may have more generous benefits and less flexibility with respect to plan design as compared to the large-group plans. Additionally, small-group plans must comply with federal [rating restrictions](#). These restrictions limit how plans can vary premiums to four factors: self-only or family enrollment; geographic rating area; tobacco use; and age. In the absence of these rating restrictions in the large-group market, [plans have typically used additional factors](#)—such as the employer's medical claims history and industry—to develop premiums.

If employers see increased costs and administrative burdens in the small-group market, some employers may self-insure rather than purchase a small-group plan. Self-insured plans, regardless of the size of the employer, [do not have to comply with state health insurance requirements](#) and are required to comply with [fewer federal requirements](#). An employer's cost to self-insure is closely related to the collective health status and demographics of its workforce, and employers with low-risk employees may have more incentive to self-insure. If employers employing low-risk individuals opt out of the small-group market, the majority of new entrants to the market could be high-risk individuals. The effect could be increased costs of coverage in the small-group market.

It is also possible that some employers may choose to drop coverage rather than purchase coverage in the small-group market or self-insure. This option seems less likely for employers with 51-100 employees, as these employers will be subject to the [ACA employer mandate](#) beginning in 2016.

Potential Implications for Employers with 50 or Fewer Employees

The ACA applies a [single risk pool requirement](#) to the small-group market. Under this requirement, a health insurance

issuer must consider all enrollees in small-group plans offered by the issuer in a state to be members of a single risk pool. This requirement means that an issuer must consider the medical claims experience of enrollees in all small-group plans offered by the issuer when developing rates.

The change in the definition of small employer will bring new employers to the small-group risk pool, and small-group rates will change to reflect the new entrants into the market. Whether the new employers cause rates to increase or decrease—and by what magnitude—[depends on the number of new employers and their mix of risks](#). For instance, if a majority of the employees of the new entrants are older individuals who use a lot of health care services, the addition of these entrants to the small-group pool could cause rates to increase for all small-group market plans. The American Academy of Actuaries asserts that while the new entrants could also cause rates to decline, [factors causing rates to increase are likely to dominate](#).

If small employers see increased rates, some may self-insure or stop offering coverage. Self-insurance is generally less common among smaller employers, but small employers may pursue the self-insurance option provided it is permitted under state regulations. Small employers also may choose to not offer coverage, particularly if the employer is not subject to the [ACA employer mandate](#).

Potential Delay in Implementation

In March 2014, the [Centers for Medicare & Medicaid Services](#) extended a [transitional policy](#) to address the potential cancellation of health plans that did not comply with certain ACA requirements effective in 2014. Pursuant to the policy, state insurance commissioners could choose whether to enforce compliance with specified ACA requirements that apply to non-group and small-group plans. In states allowing the transitional policy, issuers could choose to renew coverage for enrollees in their current non-group and small-group plans. Pursuant to the extended policy, coverage renewed for a plan year between January 1, 2014, and October 1, 2016, does not have to comply with certain ACA requirements.

In states allowing the transitional policy, issuers may permit employers with 51-100 employees to renew their current large-group policies on or before October 1, 2016. These renewed policies do not have to comply with the ACA requirements that apply to the small-group market, such as covering the EHB. This provision has the effect of delaying implementation of the change in the definition of employer. According to the Commonwealth Fund, 34 states have [issued guidance](#) allowing employers with 51-100 employees to renew their policies and effectively continue to have large-group coverage into 2017.

Legislative Activity

Legislation introduced in the House ([H.R. 1624](#)) and the Senate ([S. 1099](#)) would redefine *small employer* as one with 50 or fewer employees and give states the option to expand the definition to include employers with up to 100 employees.