HEALTH POLICY MEMO

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The Facts about Prior Approval of Health Insurance Premium Rates

Without state intervention, health insurance companies can and often do charge very high premiums to individuals and small businesses, and they spend an embarrassingly low proportion of the premium dollars they collect on health care services. In the face of double-digit increases in health insurance premiums, insurance companies should be required to demonstrate that their premium rate increases are reasonable and necessary, and that they are not retaining an excessive margin for profit and administration.

Most states address these issues by regulating insurance company premium rate increases. They use a system called prior approval, in which insurance companies must submit proposed premium rate increases to state regulators for approval. Under prior approval, insurance companies are required to file documents with the state showing their proposed premium increases and explaining why the expected costs of medical claims, administration, and other expenses justify the higher premiums. The state department of insurance then verifies that the new rates are not excessive or discriminatory. The insurer cannot actually begin charging the proposed rates until the state's department of insurance approves them. (Some states have a system known as file and use, which allows insurance companies to increase premium rates for policyholders and make those increases effective immediately without first having to justify the increases to insurance regulators.)

Insurance companies complain that the prior approval process is burdensome, but evidence from states that enforce these regulations clearly demonstrates that they are good for health care consumers and that they do not cause the negative consequences that insurance companies cite. We discuss several insurance industry myths about the consequences of prior approval below.

Insurance Industry Myth: **Prior approval will cause some insurers to leave the health insurance market, a trend known as "carrier flight."**

Fact: **Prior approval does not drive health insurance companies out of a state's market.**

The same health insurers that operate in states that do not review premiums also operate in many other states that do have prior approval requirements. Minnesota, which has had prior approval in place since 1993, argues that, while it has been one of the most aggressive states in regulating health insurers, it has a vibrant, competitive individual health insurance market with plenty of carriers and stronger-than-average individual enrollment.[1]

With prior approval already in place in most states—and cropping up in a handful of new states every year—insurers are running out of states to flee to. In fact, as shown in the table on page 2, the majority of states have prior approval requirements for at least some insurers or in specific markets.[2]

States with Prior Approval

	Individual Market	Small Group Market	Other Health Insurance Market
Alaska			Nonprofit Blue Cross Blue Shield plans
Arkansas	✓		
Colorado [a]	✓	✓	
Connecticut	✓	✓	Medicare supplemental policies are reviewed prior to premium rate increases.
Florida	✓	✓	
Georgia	✓ (some products)	✓ (some products)	
Hawaii			All managed care products
Indiana	✓	✓	
Iowa	✓		
Kansas	✓	✓	
Maine	✓	✓	
Maryland	✓	✓	
Michigan	✓		Nonprofit Blue Cross Blue Shield plans and HMOs
Minnesota [b]	✓	✓	
Mississippi [c]	✓	✓	
Nevada	✓		HMOs
New Hampshire	✓	✓	
New Mexico	✓	✓	
New York			HMOs. For other carriers, prior approval is required for new filings only. Carriers may file and use rate increases.
North Carolina	✓		
North Dakota	✓	✓	
Ohio	✓ (some products)		
Oklahoma		✓	
Oregon	✓	✓	
Rhode Island	✓	✓	
South Carolina	✓		
South Dakota	✓		
Tennessee	✓	✓	
Texas			Any increase in excess of 50% over a 12-month period requires actuarial justification to be filed. Initial rates and rate increases are filed for approval for Medicare supplemental coverage.
Vermont	✓	✓	
Virginia	✓		Medicare supplemental and long-term care insurance
Washington	✓	✓	
Wisconsin	✓	✓	

[a] Colorado's legislature enacted a law in May 2008 that introduces prior approval to the individual and small group markets. The bill passed too late to be reported in *Failing Grades: State Consumer Protections in the Individual Health Insurance Market*

[b] Minnesota regulators report that, although the law does not require carriers to submit rates for approval prior to using them, all insurers in fact submit rates to the Department of Insurance and wait for its approval. According to regulators, this is in part because the rate bands and restrictions are complicated, but also because the carriers would like to avoid the public embarrassment of correcting rates after imposing them because they are adjusted or disapproved by regulators.

[c] According to state regulators, Mississippi is a prior approval state. However, statutes and regulations appear to limit regulators' review and approval powers.

Insurance Industry Myth: **Prior approval will make health insurance more expensive.**

Fact: **Requiring prior approval of premium increases is an effective way to keep premium rates and premium increases at reasonable levels.**

In contrast to what health insurers say, insurance regulators in states with prior approval report that the measure helps keep premium rates and premium increases reasonable:

- **Indiana** regulators estimate that they negotiate lower premium increases about 50 percent of the time.
- In **Iowa**, regulators have negotiated down about 30 percent of requested premium increases since January 2007. The rates that were approved after insurers reduced their proposed increases were, on average, 40 percent lower.
- A **Maryland** insurer kept its premiums artificially low for two consecutive years and then requested a 46 percent increase, according to state regulators. The state denied that high increase and won in court when the insurance company challenged its decision. Regulators there report that they reduce about half of all proposed premium increases that come in.
- **New Hampshire** regulators negotiated with an insurer to bring a proposed 100 percent increase down to 12.5 percent.
- **North Dakota** regulators worked with insurers to bring down about 37 percent of the proposed premium increases (also known as rate filings) that have come in since the beginning of 2007.
- **Ohio** regulators report that they often negotiate with health insurers for lower premium rates, or they require a reduction in proposed rates, as part of the prior approval process.
- **Tennessee** regulators report that they often negotiate reductions in premiums or deny premium rate increases. Before Tennessee began its rigorous rate review process, insurers were charging higher rates for their products in Tennessee than they were in many other states. By using prior approval, Tennessee has curtailed that practice. For example, the state has denied insurer requests to increase premiums by 25 percent and 32 percent when insurers' rates in Tennessee were already 33 percent higher than the rates they charged in other states.
- **Vermont** insurance regulators estimate that they deny proposed premium rate increases or negotiate with insurers for lower rate increases about 75 percent of the time.
- **Washington** had a prior approval process in place from the early 1990s until 2000. It was repealed in 2000 as part of a deal with insurers. Not surprisingly, premiums rose steeply after that, and consumers complained to the Washington Office of the Insurance Commissioner. But without prior approval regulations, the Insurance Commissioner's office was unable to determine if the premium increases were always justified.

  Because of these concerns, the legislature considered reinstating prior approval in 2007. The insurance industry assured lawmakers that the measure was excessive and unnecessary. However, as soon as the prior approval bill died, the state's largest insurer in the individual health insurance market hit policyholders with 20 and 40 percent rate increases even though the company was already making lots of money in the individual market (20 percent of the premium dollars that the insurer collected the previous year went to profits).[3, 4]

During the 2008 legislative session, Washington legislators enacted a bill to reinstate prior approval in the individual health insurance market. Regulators report that since the law was enacted, they've already received two significant rate filings that will have to be negotiated down.

Insurance Industry Myth: **Prior approval will delay the introduction of innovative new products into the market.**

Fact: **Prior approval prevents insurance companies from offering artificially low premiums for a new policy to attract members, then later increasing premiums rapidly.**

Regulators from many states with prior approval requirements say that they are valuable in preventing insurers from gaming the market. For example, without prior approval, insurance companies often introduce a product into the market with lower-than-average premiums to attract new policyholders. Then, a short time later, they raise prices on these products significantly. In another example, in some states, insurers increase premiums more than once a year. Consumers, who purchase coverage with the expectation that they won't face steep premium increases in the near future (much less within the year), then drop their coverage, which often causes insurance companies to raise premiums for the remaining policyholders even further. This type of gaming is harmful to both consumers and insurers. State insurance regulators say that prior approval not only helps them to protect consumers, but it also helps ensure that insurance companies stay solvent and charge premiums that are sustainable.

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[1] These statements are based on an interview with the Minnesota Director of Health Policy and the Life and Health Actuary in February 2008. According to Kaiser State Health Facts, 8 percent of Minnesota residents have individual health insurance coverage, compared to 5 percent nationwide. Kaiser State Health Facts, *Health Insurance Coverage of Nonelderly, 0-64, States (2005-2006), U.S. (2006)*, available online at http://www.statehealthfacts.org/comparetable.jsp?ind=126&cat=3&sub=39&yr=1&typ=2, accessed on June 10, 2008.

[2] Based on Families USA's 50-state survey conducted for *Failing Grades: State Consumer Protections in the Individual Health Insurance Market* (June 2008), available online at www.familiesusa.org. The survey question asked, "Does state law require the department of insurance to review premium increases before they go into effect (prior approval)? If yes, does it apply to all products in the individual and small group markets?" Some states reported that they have prior approval requirements other than those in the individual and small group health insurance markets, while others may not have. Therefore, our table may not reflect all states' prior approval requirements.

[3] Chris McGann, "Senate Approves Bill Giving State Power to Review Insurance Rate Hikes," *Seattle Post-Intelligencer*, January 31, 2008.

[4] Mike Kriedler, Insurance Commissioner, Washington State, *Open Letter to Washington State Legislature*, January 23, 2008, available online at http://www.insurance.wa.gov/legislative/documents/Kreidler%20ltr%20to%20Legislature%201-23-08.pdf.