Breaking Down Health Reform's Grandfather Clause:

New Rules May Hamstring Employers' Ability to Innovate Existing Plans…Unless Healthcare Performance Management Principles are Implemented

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Executive Summary

The grandfather clause is a provision in the Patient Protection and Affordable Care Act that seeks to keep a key promise made to citizens by the Obama administration: "If you like your health care plan, you can keep your health care plan." But interim final rules handed down by the Department of Health and Human Services (HHS) and other federal agencies June 17, 2010, appear likely to frustrate the intent of the law and hamstring employers' ability to offer the best coverage options in a cost-effective manner. In adopting an overly restrictive interpretation of the grandfather clause, the rules essentially diminish employer flexibility to make plan design changes by tying allowable changes to current plan structures.

In this report, we examine the grandfather clause, the new HHS rules that will govern its implementation and the likely impact on employer health plans. We also will address some factors organizations should consider when deciding whether or not the benefit of retaining grandfather status outweighs making certain plan design changes and how Healthcare Performance Management (HPM) technology can help them operate more cost-effectively.[i]

Inside the Interim Grandfather Rules

When Congress included the grandfather clause in the health reform law, it did so to allow employers to maintain current health plans that meet their employees' needs. But the June 17, 2010, rules issued to clarify how it would work severely limit changes that may be made on a grandfathered plan and appear to have muddied the waters somewhat.

New plans and those that lose grandfathered status, defined as non-grandfather plans, are subject to a larger set of requirements than grandfathered plans. Beginning for plan years after September 23, 2010, non-grandfathered plans must adhere to significant additional requirements including:

- 100 percent coverage of preventive care;
- Broader employee choice of providers and emergency care coverage;
- More extensive internal appeals and external review process;
- New non-discrimination rules; and
- New reporting requirements.

While the new law requires all existing health plans – insured and self-insured – to provide a whole host of new benefits to participants, plans that existed on March 23, 2010, are exempt from these additional requirements and regulations. Even though the law is silent on how plans lose grandfather status, plans will lose status if they choose to reduce benefits significantly, increase out-of-pocket employee cost sharing beyond allowable limits, or reduce employer contributions. Plans that make such changes will be considered non-grandfathered plans.[ii]

All health plans – grandfathered or not – must provide certain mandated benefits to participants for plan years starting on or after September 23, 2010. These federal mandates include:

- No lifetime limits on coverage,
- Plans can't drop members if they get sick or have made an unintentional mistake on their applications; and
- Parents' insurance coverage is extended to their adult children up to age 26.

Additionally, employer-based plans – grandfathered or not – must not deny coverage to children with pre-existing conditions or adopt restricted annual coverage limits below levels to be specified in future regulations – and annual limits are prohibited completely after 2014.

According to HHS documents, grandfathered health plans will be able to make certain routine changes to their policies and still keep their status – as long as the changes "do not significantly alter the level of benefits." Allowable changes include prescribed inflation-based rate adjustments, new

benefits, "modest" adjustments to existing benefits, adoption of new consumer protections and changes to comply with other state or federal laws.

"The rule … will allow employers to make routine and modest adjustments to co-payments, deductibles and employer contributions to their employees' premiums without forfeiting grandfather status," Labor Secretary Hilda Solis said in a statement. "This flexibility will encourage employers to continue offering health coverage to their employees and help to ensure coverage for all Americans."

Employer comments to HHS have noted that the final rules should be modified to provide grandfathered plans flexibility to make changes that advance cost control measures as well as pro-innovation changes. They state that grandfather plans must be open to innovation by providing incentives for wellness activities, rewarding high quality providers, and incorporating evidence-based medical treatments into plans. Plans should be able to make changes that reflect availability of less expensive generics, more effective treatment options and technological developments without losing grandfather status.

Cone Of Uncertainty

The impact of the health reform law and regulations on employer provided health insurance could be likened to that of a major hurricane on small barrier islands. And for employers, who must foot the bill and still keep their bottom line buoyant, the "cone of uncertainty" surrounding implementation of the rules looms large. The U.S. Chamber of Commerce, the world's largest business federation, opined in mid-August comments to HHS that the new grandfather rules are "inconsistent with the fundamental principles of health reform."

In a letter commenting on the rulemaking, the Chamber said the restrictions on making changes to cost sharing, policy issuers, the incorporation of wellness programs and plan election structure were troubling.

"Not only do the regulations frustrate the Administration's laudable promises to those covered by existing plans in the individual and group market, but they also undercut the admirable principles of health reform and far exceed the statutory language that authorizes their very promulgation," the Chamber said. Additionally, the group sought clarifications on key procedural issues such as how a plan can lose its grandfather status or why new disclosure requirements were necessary.[iii]

Employers Pessimistic About Remaining Grandfathered

The uncertainty created by these interim rules already is having a chilling effect on companies' plans to seek grandfather status. A new survey by Hewitt Associates, a global human resources consulting and outsourcing company, shows that nine out of ten companies surveyed anticipate losing their grandfathered status by 2014, with the majority expecting to do so in the

next two years.[iv]

Ken Sperling, leader of Hewitt's Health Management practice said, "Employers reviewing their existing health care strategies in light of reform are focused on answering two questions:

- What changes do I need or want to make to my health care plans; and
- How can I make them without significantly increasing costs?"

Hewitt's survey of 466 companies representing 6.9 million employees found that most companies expect to lose grandfather status because of health plan design changes (72 percent) and/or changes to company subsidy levels (39 percent).

Companies also cited consolidation of health plans (16 percent), changes to insurance carriers (16 percent) and union negotiations (15 percent) as additional reasons. A full 77 percent of companies said that recently released guidance on preventive care did not impact their decision to maintain grandfathered status.

"After assessing the grandfather provision, large companies realize they already comply with many of the requirements of non-grandfathered plans," Sperling said.

"So the changes they'll need to make aren't likely to add a significant cost or administrative burden. Most large employers would rather have the flexibility to change their benefit programs than be tied down to the limited modifications allowed under the new law."

Hewitt's survey found that of those companies with self-insured plans, most (51 percent) expect to first lose grandfather status in 2011 and another 21 percent plan to lose status in 2012. This timing is similar for companies with fully insured medical plans, with the vast majority expecting to lose status in 2011 (46 percent) or 2012 (18 percent). A government mid-range estimate is that one-third of large employer plans in 2012 and 45 percent in 2013 will have lost grandfather status.[v]

Better Alternatives

One of the realities about the health reform law is that – as it's currently structured -- it will have little impact on lowering the cost of healthcare. If anything, the administrative provisions and some of the mandates actually will increase costs -- in some cases substantially.

Two of the many specific new mandates illustrate the costly administrative burdens that will be faced by non-grandfathered plans. ERISA self-funded non-grandfathered plans, for example, must comply with a new federal external claims review process --not now required under ERISA -- that requires disputed claims to be reviewed by three independent review

organizations at plan expense.

A new federal mandate requiring preventive services to be covered with no cost sharing for non-grandfathered plans will increase costs for plans that need to add coverage or eliminate cost sharing provisions. While the long-term cost implications are uncertain, it will depend in large part to what extent the cost of providing the mandated coverage can be offset from prevention and early detection of certain conditions.

Although organizations ultimately will decide for themselves what is in their best interest, simply – and prematurely – abandoning the idea of grandfathering an existing health plan may be short sighted.

Here's why: health costs in 2011 are projected to increase by nine percent, a number that doesn't take into account additional costs associated with the health reform law.[vi]

These costs could add three to five percent to the existing projected increases and there are no apparent sure answers at this stage as to how to defray those double-digit increases.

Some employers are considering the traditional strategy of passing higher health costs on to employees and/or reducing benefits.

To do this, those companies now will have to amend their plans, which likely will make them ineligible for grandfather status -- and vulnerable to a wide range of costly new federal mandates.

Still, it may be ill-advised for a company that had a plan in place prior to March 23, 2010, to make a premature decision about surrendering its grandfather status.

Federal agencies are expected to issue revised final rules as well as administrative guidance other than in the form of regulations once their review of comments is completed. Several employer groups including the self-insurance industry fought very hard to include the grandfather provision, which does not expire, in the law.

Perhaps the most significant advantage for grandfathered plans is their immunity from the "essential benefit" provisions, which are codified in the law, but which will be defined by rule.

There are huge advantages to maintaining grandfathered status in the long run because it avoids numerous costly mandates, allows companies to keep their existing plans and provides significant flexibility for companies to self-insure. The rules eliminate the flexibility of self-insured plans to tailor and customize their benefit plans, undermining the agility that accounts for their popularity.

About fifty-nine percent of all people covered in private plans are in self-

insured plans, and that number has been growing; it has increased from 44 percent in 1999. Self-insurance has become a better option for employers looking for cost control.[vii]

Self-insured plans also have the advantage that the employer can control of its own claims data, which enables it to apply technology based on analysis and predictive modeling of that claims data. What this means is that self-insured employers can get a better grip on the trends in their health plan and take proactive, strategic action to intervene with effective outreach programs. They can obtain actionable workforce health risk information that helps them avert some of the catastrophic claims that account for a huge amount of the cost of the plan.

HPM: A Game-changing Approach

In this time of great change and uncertainty, employers can take steps to reduce plan costs and more effectively manage their health programs to offset any projected increased costs that could ensue by retaining their grandfather status. Healthcare Performance Management (HPM) is a game-changing approach to holding the costs of an employer's health plan in check.

By adopting an HPM strategy, plan sponsors integrate the business discipline of performance management into their company health plan's operations. In so doing, they are able to manage their health plans with data, analytics and metrics -- just like many manage other aspects of their business. The strategy can be implemented by licensing available software from HPM software developers on a per-member, per-month basis.

The savings can be significant. For example, a suburban Philadelphia township found that health costs were draining the general fund. It used HPM principles to analyze its workforce health risk -- potentially the source of the highest costs to its self-insured plan.

Pharmacy claims data were used to conduct an overview of health patterns and warning signs. Using that data, the township implemented targeted workforce educational programs including a smoking cessation program, a weight management program, and offered incentives for employees to enroll in an exercise program.

The township offered points, which were used as deductions from employee financial contributions to the health plan. Employees also began using a HPM on-line portal to communicate with caregivers, pharmacies, and providers to review medications, claims, track spending and manage incentives**.**

A key objective of this strategy was to get employees more involved in their own healthcare and cost containment. The outcome was significant: by the end of the first year, 26 percent of high and moderate risk employees were

working with care managers — up from five percent before the incentive program was in place. The company expects to reduce health costs by $500,000 or more annually.

This is only one example of how an organization can not only reduce the costs of its health plan, but also improve health outcomes in its workforce – all in a manner that does not adversely impact its grandfather status.

Conclusion:

The grandfather rule is based upon the political promise that individuals who currently are covered in the insurance or self-insured environments within healthcare will be able to keep their current plans intact. The early speculation of what that really means has now been clarified with the release of the June 17, 2010, interim rules.

At this point, companies need to evaluate the impact of grandfathering on their plan. Since there is no "sunset provision" on the grandfather clause, this status will allow employers to keep their current plans indefinitely instead of becoming subject to the more administratively burdensome non-grandfather framework. That may turn out to be a huge advantage when costly new mandates start to kick in three years from now in 2014 and could outweigh any perceived short-term benefits of surrendering grandfather status.

As written, the interim rules restrict the flexibility of companies to make traditional changes -- within reasonable parameters -- to existing plans, at least if they want to retain their grandfather status. Companies may need to seek out and evaluate other cost optimization strategies to take up the slack.

Enter Healthcare Performance Management (HPM), a new paradigm that incorporates the use of technology to manage plan performance. Just like other aspects of enterprise management, HPM is critical to helping organizations retain and benefit from grandfather status, which is a key to preserving the private employment-based health insurance system, reducing costs, and improving health outcomes.

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About the HPM Institute

The Healthcare Performance Management Institute (HPM Institute) is a research and education organization dedicated to promoting the use of business technology and management principles that deliver better and more cost-effective healthcare benefits for employers who cover their employees. The institute's mission is to introduce and develop the new corporate discipline, HPM, a technology-enabled business strategy that tackles the challenge of controlling healthcare costs and quality in much the same way that enterprises have optimized customer relations, supply chain management and enterprise resource management. HPM provides C-level executives with visibility and control over company healthcare benefits spending trends and risk-management postures, while protecting individual employee privacy. For more information, visit www.hpminstitute.org.

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END NOTES

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