“Private” Exchanges

What Are They?

And What Issues Do They Present?

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The Drivers of Health Care Reform?

- Reform Insurance Laws
  - Mandate certain insurance standards.
    - For example, “Essential Health Benefits” and “Actuarial Value.”
- Coverage - Priority #1
  - Expand Medicaid.
  - Provide premium subsidies to help low- to middle-income people purchase health insurance.
    - The new Exchanges created under PPACA became the mechanism through which these subsidies could be accessed.

The Exchange Under PPACA

- The original intent of the Exchange created under PPACA was not to deliver the subsidies, but rather to serve as a *marketplace*.
  - It was believed that the Exchange would reduce administrative costs.
  - In addition, it was believed that the Exchange would attract multiple insurance carriers, which would promote competition.
  - Achieving these two goals could translate into lower premiums.
- Early on in the drafting process, it was “private” exchanges that served as the model, not the Massachusetts Connector.

What Is a Private Exchange?

- Private exchanges have been in existence even before the enactment of PPACA, although new private exchange models are being developed post-PPACA.
- What makes private exchanges unique is their use of creative, interactive technology.
  - For example, every private exchange utilizes an on-line web portal that allows the health care consumer to shop from among a wide-variety of insurance products.
- In general, private exchanges employ uniform, standardized descriptions of the various insurance products offered through the web-site, and the interactive technology allows the consumer to educate themselves about the different types of plan designs and compare prices.
- At its core, private exchanges offer a consumer-friendly way to purchase health insurance.

What Is a Private Exchange?

- Currently, private exchanges sell health insurance to (1) individuals and families in the individual health insurance market, (2) employees of employers, and (3) retiree populations seeking Medicare supplemental coverage.
- In the case of a private exchange that services the individual market, there is generally 1 private exchange model.
- When it comes to selling insurance to employees, there are currently 4 different models.

Private Exchange in the Individual Market

- These private exchanges are brokers that sell health insurance on-line.
- What distinguishes the private exchanges from other brokers is the use of creative technology to sell insurance products to health care consumers.

Policy Implications for Private Exchanges in the Individual Market

- Interestingly, private exchanges in the individual market will NOT compete with the "individual" Exchange created under PPACA.
- Why? As the law is currently written, low- to middle-income consumers purchasing insurance through these private exchanges will *not* be eligible for a subsidy for health insurance.
  - Because in addition to being eligible for a subsidy based on income, the consumer MUST purchase insurance through a governmental agency or a non-profit entity (i.e., the Exchange created under PPACA).
- However, the law may be clarified through, for example, regulations of State law, where a private exchange that meets certain conditions may be "deemed" an Exchange for the purposes of the subsidies.
  - Here, a private exchange would serve as an extension of the Exchange created under PPACA.

Private Exchange For Employees – Model #1

- There are also private exchanges that service the "group" health insurance market.
- These private exchanges sell fully-insured "group health plans" to employers with as few as 2 employees to employers with 3,500 employees.
  - These private exchanges also offer plans to employers that self-insure their employees' health risks (i.e., a self-funded plan), although this is not their primary market.
- Under this model, employees may choose from a wide-variety of plans (e.g., 10 to 20 plans), ranging from a high-cost sharing plan to a low- or no-cost-sharing plan.
  - This is a significant departure from current practice, where employers only offer 1 or 2 plan options.
  - This model promotes "employee choice."

Private Exchange For Employees – Model #1

- Under this model, the employer funds the purchase of insurance through a health reimbursement arrangement (“HRA”) or a notional bookkeeping account.
- These private exchanges also offer human resource-related services to the employer, where in essence, the employer “outsources” its HR functions to the private exchange.
- In addition to major medical plans, this model also offers supplemental insurance products (e.g., hospitalization, disease, or indmenity coverage).
- Finally, these private exchanges offer “recommendation technology.”
  - Here, the health care consumer is asked a series of questions. The technology synthesizes the answers to these questions – along with any claims data (if available) – with the insurance products offered, and recommends an insurance package that may best fit the consumer’s needs.

Private Exchange for Employees – Model #2

- Another private exchange model that offers insurance to employees enables the employer to allow its employees to purchase plans in the individual health insurance market (as opposed to the “group” market).
- Under this model, the employer funds an HRA that an employee may use to purchase individual market health insurance.
  - In this case, although the employee is purchasing an individual plan, the employee uses tax-preferred dollars instead of after-tax.
- These private exchanges also offer human resource-related functions to the employer.
  - For example, the private exchange will administer the HRA or provide call-center and other claims administration services.
- Finally, these private exchanges offer “recommendation technology.”

Private Exchange For Employees – Model #3

- Another type of private exchange that has recently been developed services large employers (with 1,000 or more employees) in the “group” market.
- Under this model, the private exchange establishes a “platform” and allows insurance carriers to offer certain plan designs that employees may choose from.
- In the case where the employer self-insures its employees’ own health risks (i.e., a self-funded plan), in general, the insurance carrier administers the medical claims incurred by employees and the employer pays the medical claims out of its general assets.
- In the case where the large employer purchases a fully-insured product, this private exchange will operate in a manner similar to other private exchanges.

“Defined Contribution” Approach

- In addition to the technology and services that these 3 models offer, what makes these private exchanges unique is their use of a “defined contribution” approach.
  - A defined contribution approach is similar to a 401(k) retirement plan where employers contribute set amounts of money toward employees’ health insurance coverage.
- In each of these models, employers decide how much they want to spend on health insurance each year, and they set aside these amounts in some sort of funding vehicle (e.g., an HRA or a notional account).
  - Advantages of this approach include allowing the employer to better manage their health care costs from year-to-year by deciding the rate at which their contributions will increase.
  - Another advantage is the employer relieves itself of the burden of choosing plan options to offer each year.
  - Instead, employees are free to choose from among a wide-array of health plans with the specified dollars allocated to them by their employer.

Who Runs Private Exchanges for Employees?

- Models #1 and #2 have traditionally been owned an operated by brokers.
- However, recently, insurance carriers are establishing their own private exchanges that mirror these models or they are investing heavily in the existing models (i.e., the carriers are essentially purchasing the private exchange's platform and technology).
- In the case of a private exchange servicing large employers with 1,000 or more employees, large benefit consulting firms are taking the lead in running this type of private exchange.

Policy Implications for Private Exchanges for Employees

- Will private exchanges for employees compete with the SHOP Exchange created under PPACA?
  - No, in the case of private exchanges that service large fully-insured or self-funded plans (e.g., Model #3).
  - Most likely, in the case of private exchanges that sell fully-insured products to employers with 100 or fewer employees (e.g., Model #1).
  - Most likely, in the case of private exchanges that enable employers to allow their employees to purchase plans in the individual health insurance market (e.g., Model #2).

Policy Implications for Private Exchanges for Employees

- Will private exchanges for employees result in adverse selection in a State's insurance markets?
  - It is unclear, but PPACA includes two new requirements that should mitigate any adverse selection.
    - *Same Risk Pools* – Under PPACA, individuals purchasing insurance in the individual market inside OR outside of the Exchange are part of the same risk pool (pooled by carrier). Same is true for employees purchasing insurance inside OR outside of the SHOP Exchange in the small group market (i.e., the employees are part of the same risk pool (pooled by carrier) no matter where they purchase their health insurance).
    - *Risk-Adjustment* – In addition, PPACA requires States to establish a risk-adjustment mechanism to compensate insurance carriers that end up insuring high-risk employees.

Policy Implications for Private Exchanges for Employees

- How will a private exchange promote competition?
  - Private exchanges in the individual market will be able to offer multiple carriers generally without the risk of adverse selection.
  - However, in the case of a private exchange that sells insurance in the "group" market – and also promotes "employee choice" – multiple carriers may result in adverse selection.
    - This is largely the reason why we see brokers that run a private exchange contract with one or two insurance carriers that negotiate the best deal with the private exchange. Here, there should still be competition among insurance carriers, but this competition will be at the broker level, not at the consumer level.
    - In the case of an insurance carrier that owns, or is a dominant investor in, the private exchange, the insurance carrier will generally be the only company offering insurance plans to consumers. Here, there will be little or no competition among carriers.
  - In the case of a private exchange for large employers, if enough lives purchase through the private exchange, multiple carriers may participate, but only if there are participation minimums.

Other Policy Implications

- Currently, private exchanges that enable employers to allow their employees to purchase insurance in the individual health insurance market can only operate in a limited number of States because although an employee is purchasing an individual plan, the plan is considered a “group health plan.”
  - HIPAA prohibits a “group health plan” from being medically underwritten, which carriers are permitted do in most States, at least until 2014.
- In 2014, PPACA prohibits insurance carriers from underwriting individual market plans based on health status.
  - In theory, this change in the law will allow more employers to allow their employees to purchase plans in the individual market, which should open up more markets for this model.

Other Policy Implications

- If this model becomes popular among small employers in 2014 and beyond, the risk pool that the employee will be part of may be critical.
  - For example, if employees who would otherwise be in the small group market are considered part of the individual market on account of coverage under an individual plan, the risk pools in one or both markets may be skewed.
- But, States may be able to resolve this issue by merging its individual and small group markets.

Private Exchange Offering Medicare-Supplemental Coverage

- Another private exchange that has been in existence for a number of years allows public and private sector employers with retiree populations to continue to offer health care coverage even when their retirees become Medicare-eligible.
  - Under this model, the private exchange helps employers transition their retirees from group health plans to Medicare Advantage, Medicare Part D, and other Medicare-supplemental plans.
  - Like other private exchanges, this model allows employers to fund the purchase of the Medicare supplemental-type plans through an HRA.
  - This model utilizes creative, interactive technology that allows the retirees to shop from among a wide-variety of products offered by multiple insurance carriers.

Private Exchange Distribution Channel

- Finally, a public-private exchange is being developed in Florida.
- While the Florida Health Insurance Exchange generally differs from private exchanges – because it does not provide the same services, rather, it will allow small employers to simply shop for coverage offered by participating carriers through a web-site – this exchange will operate independent of the Exchange created under PPACA.

The Future?

- Are private exchanges the future?
  - As health care costs continue to rise, more and more individuals are likely to look to private exchanges.
    - Why? Because private exchanges provide a consumer-friendly way to choose a health plan.
  - In the case of employers, it is likely that private exchanges will help those employers who want to hold on to employer-sponsored coverage to continue to provide such coverage.
    - Why? Because of the advantages we discussed: (1) employers can better manage costs, (2) employees are able to choose their health insurance as opposed to employers deciding on plan options every year, and (3) the customer service found only in a private exchange.
- Even if PPACA is modified or halted by a Supreme Court decision or the 2012 elections, private exchanges will play a critical role in the future of health care.

Questions?

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