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BEFORE THE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP
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Introductory Remarks

Good morning Chairwoman Snowe, Ranking Member Kerry, and members of the Committee. Thank you for inviting me to discuss Association Health Plans (AHPs) – a key component of the President's efforts to make quality, affordable health benefits available to all Americans. I applaud your leadership, Sen. Snowe, for focusing on the health care needs of small business employers and their employees by championing AHP legislation in the Senate. I support S. 406, the Small Business Health Fairness Act, and I look forward to continuing to work with you as the Senate considers this much-needed legislation.

Approximately 45 million Americans lack health insurance, and approximately 84 percent of the uninsured are in families headed by workers – with most working at firms with fewer than 100 employees. In fact, small firm workers and their families comprise more than 60 percent of the working uninsured.[1] To increase health insurance coverage, the President has proposed a comprehensive reform agenda that includes tax credits for the purchase of individual coverage, policies that encourage increased use of health savings accounts (HSAs), medical malpractice reform, and AHPs sponsored by trade and professional associations, as well as civic, religious and other community groups.

The Uninsured and Small Businesses

Although most working Americans receive health insurance from their employers, small firms with fewer than 100 employees find it particularly difficult to offer benefits. Just 46 percent of these small businesses offer insurance, compared to 98 percent of larger firms with more than 100 employees. The difficulties that small businesses face in trying to offer quality, affordable health insurance account for a significant part of America's uninsured.

We know that small employers want to offer health insurance to their workers and their families. Among 600 small businesses responding to a survey, less than one-third currently offer insurance, but about three-fourths said they would be "very" or "somewhat likely" to participate in an AHP that offered lower prices, more choices, or less paperwork. [2] Further, small business employees value health insurance. According to a recent survey, health insurance was ranked as "very important" by 89 percent of small business employees.[3]

AHPs are a central component of the President's overall plan for expanding access to health care. Your legislation, Sen. Snowe, is aimed squarely at the gap in coverage among small businesses, and to understand why your bill will have such a significant impact on reducing the uninsured, it's important to understand the barriers that prevent many small employers from offering coverage today.

Small Firms Face Numerous Barriers to Coverage

Cost is clearly the biggest barrier for small employers wishing to provide health benefits. For a variety of reasons, insurers typically charge small firms more per employee than large firms for comparable coverage. Small company premiums are 20 percent to 30 percent higher than those of large self-insured companies

with similar claims per covered employee.[4] Cost drivers include small businesses' higher fees for administration, insurance company marketing, and underwriting expenses, as well as adverse selection, and state regulatory burdens. Further, small firms that are able to offer coverage, are likely to offer less generous benefits and more of their premiums are consumed by administrative costs. In addition, vulnerability to insurance fraud leaves many small firms unsure about where to go for affordable, reliable coverage.

Small employers' costs are rising more rapidly than those of larger employers. Total costs per employee increased by 13.6 percent at firms with 3 to 24 employees in 2004, compared with 11.6 percent at the largest firms.[5] Employees in small businesses bear the brunt of these cost increases, according to a survey by the Blue Cross Blue Shield Association (BCBSA), the Employee Benefit Research Institute (EBRI), and the Consumer Health Education Council. Of the small businesses that changed their health benefits, 65 percent increased workers' copayments and deductibles, 30 percent raised the percentage of premiums paid by employees, and 29 percent cut back on the package of benefits offered.[6]

Employer Expenses: When a small firm decides to offer health insurance, it must undertake numerous administrative tasks, including identifying available insurance policies; comparing their prices, benefit packages and other features; assembling plan descriptions, enrollment materials and other forms; and educating and enrolling its workforce. Small firms must pay for these activities with typically fewer resources than large firms, and the cost of these activities for each covered employee is higher.

Insurance Company Expenses: According to the Government Accountability Office[7], insurers incur higher costs when providing health care coverage to small employers than to large employers. Insurers must market and distribute their

policies to a very large number of unconnected employers. They typically must compensate agents for each small policy sold or renewed. Some costs, such as the cost of collecting detailed medical histories for purposes of medical underwriting, are layered on each time an employer changes insurers – and smaller employers generally tend to change insurers more frequently.

Underwriting and Adverse Selection: Under current law, many small employers face higher premium costs based on insurers' underwriting practices. In underwriting an insurance policy, the insurer estimates its cost to insure the employer's workforce, by looking at the group's demographics, past claims experience, and/or health status and other factors. Small groups have few participants among whom to spread the risk, and, as a result, a few unhealthy workers or dependents will skew the claims experience and may force the employer to pay much higher premiums.

Faced with high premiums and limited budgets, small employers often share more of the costs with their employees than larger employers. In the worst-case scenario, healthy workers will balk at higher costs and may not accept the offer to purchase insurance, either obtaining private individual coverage or joining and increasing the ranks of the uninsured. When healthy workers give up health insurance, sponsored by a small employer, only higher-risk individuals remain, leading to a predictable spiral of ever-increasing premiums and declining coverage as the insured group becomes less and less healthy. The small-group market is particularly vulnerable to this situation.

State Regulatory Burdens: Some state laws further impede small employer coverage. Because some states have been very aggressive in regulating small-group markets, many insurance carriers have withdrawn from those markets, leaving employers with little choice in plan design or cost options. Five or fewer insurers control at least three-quarters of the small-group market in most states.

In some states, insurance for certain small firms is available only through a state-operated risk pool or from one insurance carrier.[8]

Additionally, small employers are sensitive to the cost of state benefit mandates (such as requiring coverage for hair transplants, or treatment provided by acupuncturists) that drive up the cost of the small group coverage. Such mandates are responsible for one of every five small employer decisions not to offer coverage.[9] Another study reported that mandates raise premiums by four to 13 percent, and that up to one-quarter of uninsured Americans lack insurance because of state mandates.[10]

Vulnerability to Fraud: Small employers and their employees are often victims of fraudulent schemes that promise low-cost health coverage. Many of these arrangements are multiple employer welfare arrangements (MEWAs). MEWAs are arrangements that provide health benefits to employees of two or more unrelated employers who are not parties to collective bargaining agreements. MEWAs are subject to a complex mix of state and federal laws and regulations. Unfortunately, unscrupulous promoters have exploited MEWAs' complex regulatory and oversight structure to operate Ponzi schemes that collect premiums but intentionally default on benefit obligations.

Any small businessperson who has been harmed by fraud will be wary of buying coverage again. And all small businesses are vulnerable to such schemes because the marketing can be persuasive and the price is often "too good to be true." Because of this, any new legislation aimed at expanding access to affordable health coverage must protect against this type of abuse and provide assurances to small businesses that the product is legitimate.

AHPs Address These Barriers to Coverage

Association Health Plans will have the effect of reducing these barriers to coverage. Small businesses would enjoy greater bargaining power, economies of scale, administrative efficiencies, and the benefits of a uniform regulatory structure. Federal certification demonstrating that legitimate and financially sound sponsors operate AHPs would provide small businesses with the assurance that the Department of Labor has determined that the organization offering coverage is not a "fly-by-night" operation, reducing the vulnerability of small businesses to fraud by providing secure, high quality, and affordable health benefits.

The AHP legislation provides a level playing field for small business by allowing small employers to join together through *bona fide* associations to purchase or provide health insurance coverage for their employees. Through the power of group purchasing, Sen. Snowe's legislation would give small firms many of the economic and legal advantages currently enjoyed by large companies and labor unions. The Administration also believes that quality affordable insurance could be expanded to many more Americans by further adopting the President's proposal to expand AHPs to civic and community groups. This would allow private, non-profit, multi-State entities outside the workplace, as well as small businesses, to offer affordable health coverage to their members and dependents.

Bargaining Power and Economies of Scale: By grouping small employers, as well as civic and community organizations, together to purchase coverage, AHPs will be able to act more like large employers and offer lower cost coverage to employers, employees and their families. If the AHP chooses to purchase insurance, it will be in a better position to negotiate with insurers regarding the terms and costs of coverage than a small employer acting individually. AHPs

will also enjoy economies of scale in the administration of plans. They will give insurers a vehicle to market and distribute policies to many small employers at once. By offering a well-selected and stable choice of policies to members, AHPs can help slow small employers' otherwise costly movements from one insurer to another.

Streamlined Regulation: AHPs will allow small businesses to enjoy the benefits of a more uniform regulatory system. For AHPs that offer fully insured coverage, state laws will govern the solvency requirements and other consumer protections, just as the states regulate insurance policies issued to group health plans today. However, insured AHPs will be able to offer a uniform benefits package nationwide, making it possible for employees to receive the same benefits regardless of where they live.

AHPs that offer self-insured coverage will be subject to a single, effective, national certification, solvency and oversight process that will be administered by the Department of Labor. Strict standards would be met to ensure solvency and protect consumers.

Pooling Risk: AHPs will help ensure small employers are not denied insurance coverage or priced out of the market due to the health of their employees. As a member of a *bona fide* association, even an employer with high claims experience would be offered the same coverage options as those offered to other employers within the AHP. Large AHPs can spread the risk of insuring unhealthy groups or individuals among a larger population of health risks.

Broader Choice of Coverage: Associations will be able to fashion coverage that best meets their members' needs, even choosing to offer more than one plan. By

offering broader choices, AHPs will encourage healthy small business members to purchase coverage and pay into the premium pool.

AHPs Will Reduce Costs and Cover the Uninsured

Cost Savings and Increased Coverage: Small businesses obtaining insurance through AHPs could lower premiums. According to the Congressional Budget Office (CBO),[11] the average savings would be 13 percent, and could be as much as 25 percent per employer. CBO further estimates that, because insurance will be more affordable, more small firms will be able to provide coverage to their employees and families. Even firms that already offer coverage could obtain lower-cost coverage through AHPs. According to CBO, as many as 2 million American workers and their families who are currently uninsured could obtain health benefits through AHPs.

Wide Availability and Greater Access: Numerous small business groups are eager to offer coverage and look forward to enactment of AHP legislation, including organizations such as the National Federation of Independent Business, United States Hispanic Chamber of Commerce, the American Farm Bureau Federation, and dozens of groups representing small businesses and professionals. The Small Business Survival Committee (SBSC), representing nearly 100 existing associations and employer groups, believes that coverage will increase dramatically. According to the SBSC, "AHPs will empower America's small employers with the tools needed to harness their entrepreneurial spirit and skills in providing working families with more health benefits, and more health plan choices, at affordable prices."

Ensuring AHPs Keep Their Promises: Strong DOL Oversight

The Department of Labor has extensive experience in regulating group health insurance and in combating insurance fraud. The Department of Labor currently administers Employee Retirement Income Security Act (ERISA) protections covering approximately 2.5 million private, job-based health plans and 135 million workers, retirees and their families. Of these, 300,000 plans covering 78 million individuals are self-insured, and therefore subject exclusively to DOL oversight. In addition, self-insured multiemployer plans (established and operated jointly by a union and two or more employers) are overseen exclusively by DOL. These plans cover more than 5 million participants, not counting their covered dependents.

Your legislation, Sen. Snowe, gives the Department new, but not unfamiliar, responsibilities with respect to Association Health Plans. I am confident that we can and will protect the workers in an AHP just as we currently protect the millions of workers in other kinds of group health plans. Rest assured, I will allocate the resources necessary to effectively carry out our AHP certification and oversight responsibilities with effective, efficient and timely regulation and enforcement. I am confident of our ability to administer the AHP program successfully.

Certification and Oversight: To ensure that unscrupulous promoters would not operate AHPs, only *bona fide* trade or industry associations that have been in operation for more than three years for purposes other than providing health benefits are allowed to sponsor an AHP. The Department will examine AHP sponsors and certify them only if they meet this standard, as well as applicable solvency and membership requirements.

Whether AHPs are self-funded or fully insured, the AHP may not offer benefits to a single worker until the Department of Labor certifies that the AHP complies with the strong protections in the law. And I can assure you, we will not issue such a certification until we are satisfied that the AHP will comply with the law and our regulations.

Safeguards Against Insolvency: The states will regulate the solvency of insurers selling insurance to an AHP, just as they currently do for group health plans. Thus, workers in a fully insured AHP will be guaranteed that the current protections against insolvency apply to their plans as well.

For self-funded AHPs, the bill establishes new, strict solvency requirements in Federal law. An AHP that offers self-insured coverage will be required to establish premium rates that are adequate to cover claims and to maintain adequate reserves, as determined by a qualified actuary. Self-insured AHPs will also be required to keep additional reserves on hand to cover unexpected losses, and to purchase both specific and aggregate stop loss insurance to cover unusually large claims. AHPs will be required to purchase indemnification insurance to ensure that claims are paid in the event of plan termination. Self-insured AHPs must pay annual fees to a fund administered by the Department that is used to ensure that indemnification policies remain in force for terminating plans.

Further, the legislation provides regulatory authority to the Department of Labor to expand upon these requirements to ensure that workers' health benefits provided through an AHP are secure.

Insurance Market Safeguards: AHP legislation includes provisions to ensure that AHPs result in stable, reliable markets for health insurance. Spreading risk

and costs across a large group of individuals is fundamental to effective health insurance. In the past, small group markets have sometimes been vulnerable to practices, such as adverse selection or "cherry picking," that segregate good risks from bad. Such practices can make insurance unaffordable or unavailable for small firms when employees or their families become seriously ill. To prevent cherry-picking, AHPs and participating employers will not be allowed to direct their higher-cost employees to the individual insurance market based on health status. AHPs must offer all available health policy options to all of the membership's employers and individuals. The proposed legislation also limits AHPs' ability to vary the premiums for their participating employers, including a general prohibition on rating based on health status.

ERISA, HIPAA and Other Laws: Like other group health plans, AHPs will be subject to the fiduciary requirements of ERISA, which set high standards of behavior for health plan sponsors. In particular, the Health Insurance Portability and Accountability Act (HIPAA) would apply to AHPs. Under HIPAA, group health plans are subject to portability, pre-existing condition, nondiscrimination, special enrollment, and renewability provisions. These provisions also will limit the opportunity for cherry-picking. Other federal health insurance requirements that provide consumer protections, such as COBRA, DOL's claims regulation, the Mental Health Parity Act, the Women's Health and Cancer Rights Act, and the Newborn's and Mother's Health Protection Act would apply to AHPs.

Strong DOL Enforcement and Education: The Department takes health care fraud very seriously, and pursues an active strategy of enforcement and education to combat it. We devote significant resources to enforcement efforts, and we have been effective in closing down fraudulent health plans and in recovering money for their victims. We also work to educate small employers,

alerting them to ways they can protect themselves and their employees from fraudulent health insurance schemes.

- **Enforcement:** The Department places a heavy emphasis on enforcing existing health laws and on working with state insurance departments and the National Association of Insurance Commissioners (NAIC) to protect workers and their families. In particular, EBSA is actively investigating and litigating issues connected with some MEWAs. The Department's primary goals are to shut down such scam artists quickly, to appoint independent plan fiduciaries in order to protect plan assets, and to recover money for victimized workers.

  To combat MEWA fraud and corruption, EBSA has implemented a two-pronged approach using both its civil and criminal enforcement authorities. Due to our enforcement efforts, more than $7 million was recovered in FY 2004 alone for innocent victims to assist them with unpaid medical bills. Most of the criminal MEWA investigations have been jointly conducted with other agencies including the Department's Office of the Inspector General, the FBI and the United States Postal Inspection Service. As of March 31, 2005, EBSA was pursuing 120 civil and 46 criminal investigations related to MEWA health fraud. From March 1, 2004, to the present, EBSA's criminal investigations into MEWA fraud have led to the indictment of 25 individuals in 8 cases.

  Examples demonstrating the level of fraud perpetrated by unscrupulous MEWA operators are numerous. In one recent prosecution, the Department obtained court orders to shut down an abusive MEWA called Employers Mutual, LLC, sixteen related entities, and the individuals who operate them. Employers Mutual offered health benefits in all fifty states

and the District of Columbia, with over 22,000 individuals enrolled in its plans. After collecting over $14 million in employer premiums, Employers Mutual paid less than $3 million in claims. Nearly fifty percent of the contributions were diverted to the personal accounts of the principals and to pay administrative expenses. Through our timely enforcement actions, an independent fiduciary was appointed and the court approved an orderly method of resolving unpaid medical providers' claims in order to protect the plan participants from being pursued by the health providers. In addition to this civil action, EBSA's criminal investigation of Employers Mutual led to the indictment of three individuals. The indictment alleges that the defendants committed fraud by, among other things, misappropriating premiums, including $1 million in payments to two fictitious vendors set up for the benefit of the defendants, and not paying most of the claims.

- **Education and Outreach:** Through our outreach, education and assistance programs, EBSA has made educating small employers a top priority. The Department provides guidance to small employers on how they can avoid purchasing health coverage from fraudulent MEWA operators. EBSA's website lists a series of anti-fraud publications, including *How to Protect Your Employees When Purchasing Health Insurance.* These tips, designed for small employers, offer important warning signs to consider when purchasing health coverage. Checking simple information can alert small employers to fraudulent schemes. The Department worked with dozens of small business groups to disseminate these tips to their members. I encourage interested small employers and employees to visit the EBSA website at www.dol.gov/ebsa/ or call EBSA's toll-free hotline at 1-866-444-EBSA (1-866-444-3272) for further information about protecting themselves against fraud.

Other materials published on the Department's website include a publication explaining current federal and state regulation of MEWAs, and guidance on what to do when health coverage offered by a MEWA is lost. EBSA has also issued numerous advisory opinions to assist state prosecutors and regulators in the enforcement of state insurance laws against MEWAs.

Conclusion

Thank you for the opportunity to testify today. Small business employers and employees are in critical need of new ways to increase health insurance coverage, and the Association Health Plan legislation pending before the Senate is a central part of a solution to this problem. President Bush strongly supports Association Health Plans for small businesses through trade and professional associations, as well as for other members of civic, religious and community based groups. I look forward to working with the members of Congress and this Committee to help pass and administer legislation that expands health insurance coverage for working Americans.

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[1] Department of Labor estimates of working families' health insurance status, based on the Census Bureau's annual March Current Population Survey.

[2] National Association for the Self Employed.

[3] Transamerica Center for Retirement Studies.

[4] Actuarial Research Corporation.

[5] Kaiser Family Foundation Employer Health Benefits 2004 Annual Survey.

[6] The 2002 Small Employer Health Benefits Survey.

[7] U.S. Government Accountability Office, *Private Health Insurance: Small Employers Continue to Face Challenges in Providing Coverage*, GAO-02-8; and *Private Health Insurance: Number and Market Share of Carriers in the Small Group Health Insurance Market*, GAO-02-536R.

[8] U.S. Government Accountability Office, Private Health Insurance: Small Employers Continue to Face Challenges in Providing Coverage, GAO-02-8; and Private Health Insurance: Number and Market Share of Carriers in the Small Group Health Insurance Market, GAO-02-536R.

[9] Gail A. Jensen and Jon Gabel, "State Mandated Benefits and the Small Firm's Decision to Offer Insurance," Journal of Regulatory Economics; 4:379-404 (1992).

[10] Gail A. Jensen and Michael A. Morrisey, Mandated Benefit Laws and Employer-Sponsored Health Insurance (Washington, D.C.: HIAA, 1999).

[11] Congressional Budget Office, *Increasing Small-Firm Health Insurance Coverage through Association Health Plans and Healthmarts*, January 2000.