Portability of Health Insurance: COBRA Expansions and Small Group Market Reform

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Issue Brief

- Proposals are currently being put forth to change the health care system incrementally. One area of proposed legislation addresses portability, which allows an individual to change insurers without being subjected to a new waiting period for preexisting conditions. These proposals, discussed in this *Issue Brief,* contain provisions to limit preexisting condition exclusions, guarantee access to health insurance, guarantee renewal of health insurance, allow individuals to contribute to medical savings accounts on a pretax basis, and change the current law under the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA). The proposals would affect insurers, employers, and insured individuals by potentially increasing the cost of providing and purchasing health insurance.

- Concern about the portability of health insurance primarily arises in situations where an individual is leaving, or would like to leave, a job. If health insurance is not offered by a prospective employer, if the worker must satisfy a waiting period before becoming eligible for coverage, if the benefits package offered through the prospective employer is less generous, or if the employee (or a dependent) has a medical condition that is considered a preexisting condition and would not be covered by the new plan, the employee may opt to remain with his or her current employer—a situation known as job lock.

- Expansions of COBRA may not have any effect on portability. Employers can charge up to 102 percent of the premium for COBRA coverage, making it unaffordable for many workers. Because cost is a major factor, if there is no reduction in cost (or health care cost inflation) there could be little or no increase in coverage.

- According to one survey, in 1994 average COBRA costs were $5,301 per COBRA covered worker, compared with $3,420 for active employees. Any expansion of COBRA would almost certainly increase employer cost for health insurance.

- Guaranteed issue and guaranteed renewal may have the effect of increasing average premiums if insurers and employers are forced to accept relatively unhealthy individuals. Many states have already enacted small group insurance market reforms. While it is still too early to measure the effects of these laws on health insurance coverage, anecdotal evidence indicates that there has been a movement of small firms out of the small group market.

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Introduction

Unlike the comprehensive health care reform proposals that Congress has considered in recent years, which would have significantly changed the financing and delivery of health care in the United States, proposals currently being put forth change the health care system incrementally. **One area of proposed legislation addresses the issue of health insurance portability. Portability allows an individual to change insurers without being subjected to a new waiting period for preexisting conditions.** These proposals would reform the market for individual and group health insurance. They contain provisions to limit preexisting condition exclusions, guarantee renewal of health insurance, guarantee access to health insurance, and change the current law under the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) (see box on definitions). In other words, the proposed legislation would increase individuals' opportunity to maintain health insurance as they move geographically or change jobs. These proposals would affect insurers, employers, and insured individuals by potentially increasing the cost of providing and purchasing health insurance. In addition, proposals have been introduced that would allow individuals to hold medical savings accounts (MSAs) on a pretax basis. MSAs would address the issue of portability and affordability of health insurance, but they might also introduce factors that could affect other aspects of the health care system (see box on MSAs).

Background Issues

Portability

Concern about the portability of health insurance primarily arises in situations where an individual is leaving, or would like to leave, a job. The circumstance can be one of completely withdrawing from the job market or wanting to move to a new employer. For example, portability could help alleviate the loss of insurance benefits when a worker is offered a new job that could alter his or her insurance status. If health insurance is not offered by a prospective employer, if the worker must satisfy a waiting period before becoming eligible for coverage, if the benefits

Definitions

Guaranteed issue (or access)—Requires insurers that offer coverage to make coverage available to any individual or group that applies, regardless of the health conditions of the individual or the individuals in that group.

Guaranteed renewal—Requires an insurer to renew coverage for an individual or group at the option of the covered individual or group. Typically, policies may be canceled or not renewed for nonpayment of premiums, fraud or misrepresentation, termination of the plan, or the failure of the plan sponsor to meet contribution or participation requirements.

Portability—Allows an individual to change insurers without being subjected to a new waiting period for preexisting conditions.

Preexisting condition exclusions—Mechanisms that insurers use to restrict an enrollee's access to health care benefits relating to an individual's previous medical condition. These waiting periods are typically 6 or 12 months; however, some preexisting medical conditions may be permanently excluded from coverage.

Medical Savings Accounts

Medical savings accounts (MSAs) can be viewed as savings accounts for uninsured health expenses and could be used in conjunction with catastrophic health insurance plans. Currently, employers offer MSAs on an after-tax basis, meaning any contributions made to the MSA by the employer and the employee are considered taxable income. As of June 1995, 13 states give tax-preferred status to MSA contributions, but MSA contributions are still subject to federal income taxation.

Several members of Congress have proposed allowing employers and individuals to contribute to a savings account on a pretax basis and roll over the unused funds at the end of the year. MSAs could address the issue of portability and affordability of health insurance. If MSAs were permitted to move with an individual from job to job, they could be used to finance health insurance premiums and health care expenses during periods of unemployment. They could also be used to finance health insurance premiums and health care expenses for workers whose employer does not offer health insurance. Individuals could use the accumulated funds in the MSA to pay COBRA premiums during a transition period to health insurance provided by a new employer. However, a number of issues arise concerning MSAs. The availability of these accounts could discourage the use of necessary care, introduce adverse selection, reduce participation in cost-effective managed care arrangements, and leave overall health care spending unchanged.[1]

[1] For more detail on medical savings account (MSA) design issues and a description of MSA legislation, see Paul Fronstin, "Medical Savings Accounts: Issues to Consider," EBRI Notes (July 1995): 1–7.

package offered through the prospective employer is less generous, or if the employee (or a dependent) has a medical condition that is considered a preexisting condition and would not be covered under the new plan, the employee may opt to remain with his or her current employer. This may result in "job lock," or in employees forgoing job opportunities that could potentially increase their productivity. In other words, workers may forgo job opportunities in which a better match between the worker and the employer would enable the worker to perform his or her job more effectively. For employers that want employees to leave or retire and for employees who would prefer to change jobs, job lock can be undesirable. **The original purpose of the coverage continuation provisions of COBRA was to assure workers an ability to maintain health insurance during a period of transition to other health insurance coverage.** However, many individuals who qualify for COBRA forgo the continued coverage because of its high price relative to their income. Employees cannot be charged more than 102 percent of the employer's average health insurance premium, which may be less than the employer's actual cost but more than the employee was used to paying for health insurance. Because COBRA requires individuals pay up to 102 percent of average cost, persons leaving jobs may not always take advantage of the insurance.

Small Group and Individual Markets

Concern over guaranteed issue and guaranteed renewal relates to the small group market and the individual market for health insurance. In the small group market, for example, many employers choose to forgo health insurance because of the relatively higher premiums when compared with premiums that large employers pay. In 1993, small firms paid $187 monthly per individual, on average, for a traditional fee-for-service health insurance plan, compared with $171 for large firms (Morrisey, Jensen, and Morlock, 1994). In addition, small firms may not have large enough profit margins to add health insurance to cash wages.

Much of the variation in premiums that small employers face is due to the insurers' underwriting practices. Each employer is generally charged a premium tied to its own work force. For example, in the small group market there is generally a health risk assessment undertaken for each employee. Thus the smaller the group, the larger the administrative cost component of total health cost. The premiums faced by small groups can be affected significantly by one person with health problems because there are few employees among whom to spread the cost, whereas larger groups are not as affected by a small number of high cost individuals because the average cost per individual drops as the group grows. As a result, average premiums for small groups will tend to be relatively higher than those for large groups. Considering the premium differences due to underwriting practices and administrative cost and the difference in the affordability of health insurance between small and large employers that is due to higher average profit levels in large firms, it is not surprising that the uninsured population is closely associated with small business. In 1993, 61.5 percent of all uninsured workers were either self-employed or

Limiting preexisting condition exclusions is one method that states have used to reduce job lock, yet there is no conclusive evidence assessing the impact of these laws on job mobility.

worked in firms with fewer than 100 workers (Snider and Fronstin, 1995). Guaranteed issue and guaranteed renewal would help to address the issue of stability of health insurance for small employers and individuals but might do little to affect average insurance costs. Because cost is a major factor in employers' decision to offer health insurance, if costs are not reduced, there may be little increase in insurance coverage among workers in small companies. In fact, guaranteed issue and renewal may have the effect of increasing premiums or decreasing coverage if insurers and employers are forced to accept relatively unhealthy individuals.

Job Lock

Job lock may occur either because a worker cannot get health insurance coverage through a prospective employer or because, while the worker can obtain coverage, his or her share of the premium is higher at the prospective job than it is at the current job; the benefits package is less generous; or selected conditions are not covered (i.e., a preexisting condition clause may discourage a worker from leaving the current job and health insurance plan to move to a new plan that does not cover a given health condition). Selected health reform proposals have assumed that disallowing or restricting preexisting condition clauses and making health insurance more portable and personal would lessen job lock.

Limiting preexisting condition exclusions is one method that states have used to reduce job lock, yet there is no conclusive evidence assessing the impact of these laws on job mobility. However, in the presence of COBRA, among plans that cover a preexisting condition following a waiting period, preexisting conditions are not necessarily the primary motivating factor behind individuals' decision not to change jobs. This is because individuals can continue their current coverage for a maximum of 18–36 months even after moving into a new job, as long as they are willing to pay 102 percent of the premium for their old health insurance. Thus, individuals could carry two plans until the waiting period is satisfied. In some cases though, the plan may not cover a preexisting condition at all—with or without a waiting period. Regardless of the existence of COBRA, cost, comprehensiveness of the benefit package, and availability of coverage remain important.

COBRA Basics

COBRA, as amended in legislation subsequent to its passage in 1985, requires employers with health insurance plans to offer continued access to group health insurance to qualified beneficiaries if they lose coverage under the plan as a result of a qualifying event. COBRA requires continued access for 18 months (or 29 months if the qualified beneficiary is disabled) for covered employees, spouses, and dependent children who lose coverage when a covered employee terminates employment (for reasons other than gross misconduct) or there is a reduction in his or her hours of employment. COBRA requires continued access for 36 months for spouses and dependent children who lose coverage as a result of a covered employee's death, divorce, or legal separation. In addition, spouses and dependent children qualify for continued access for 36 months if a covered employee becomes entitled to Medicare benefits.

Prior to enactment of the Omnibus Budget Reconciliation Act of 1989 (OBRA '89), coverage could be terminated prior to the end of the maximum required period if the qualified beneficiary became covered under another group health plan. However, OBRA '89 provides that COBRA need not terminate before the maximum period if the qualified beneficiary becomes covered under another group health plan that excludes or limits a

Table 1
Entitlement and Elections for Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA), Plan Years 1988-1994

Plan Year	Employees/Dependents Who Elected COBRA as a Percentage of Active Employees	Employees/Dependents Entitled to COBRA as a Percentage of Active Employees	Employees/Dependents Who Elected COBRA as a Percentage of Those Entitled
1988	1.70%	16.00%	11.20%
1989	2.60	9.20	28.50
1990	2.20	10.60	20.50
1991	1.60	12.06	13.23
1992	1.68	8.71	19.30
1993	2.86	14.54	19.64
1994	1.30	7.20	18.20

Source: Charles D. Spencer and Associates, Inc., "1995 COBRA Survey: Almost One in Five Elect Coverage, Cost is 155% of Actives' Cost," *Spencer's Research Reports* (August 25, 1995): 329.04.04-1–329.04-7.

preexisting condition.

The coverage offered must be identical to that available prior to the change in the worker's employment status. The qualifying employee or dependent may be required to pay up to 102 percent of the premium (disabled qualified beneficiaries may be required to pay up to 150 percent of the premium for months 19 through 29). At the end of the coverage period, the employer must offer conversion to an individual policy if the group plan includes a conversion privilege (an option required in some states).

Group health plans for public and private employers with fewer than 20 employees are excluded from these provisions, as are plans offered by churches (as defined in sec. 414(e) of the Internal Revenue Code (IRC)); the District of Columbia; or any territory, possession, or agency of the United States.

COBRA Survey Results

The original purpose of COBRA's coverage continuation provisions was to assure workers an ability to maintain health insurance during a period of transition to other coverage. Several surveys have been conducted regarding issues surrounding the use of COBRA. Some key results of the Charles D. Spencer & Associates, Inc. survey, conducted in the spring of each year, include the following:

- **Of the 14.5 percent of employees and dependents eligible for COBRA coverage, about one in five (18.2 percent) elected the coverage in 1994, down from 19.6 percent in 1993 and 19.3 percent in 1992, and a high of 28.5 percent in 1989** (table 1).
- Among all spouses and dependents eligible for coverage, 26.0 percent elected coverage in 1994, compared with 9.6 in 1993, 37 percent in 1992, 23.4 percent in 1991, 25 percent in 1990, and 36.6 percent in 1989. Among employees eligible for coverage, 16.2 percent elected coverage in 1994.
- Among the entire surveyed population, 1.3 percent of the active employee work force elected COBRA coverage in 1994, down from 2.9 percent in 1993 (table 1).
- Among all eligibles electing coverage, 21.9 percent were spouse/dependent elections in 1994 (4.4 percent selected coverage because of termination or reduction in hours, and 17.5 percent elected coverage because of death, divorce, or plan ineligibility). This is up from 15.9 percent in 1993 (table 2).
- **Average COBRA costs were $5,301, compared with $3,420 for active employees in surveyed health plans in 1994.** Thus, average continuation of coverage costs were 155 percent of the active employee claims costs. Large differences between active employee costs and COBRA costs have been typical since 1990, when average active employee costs were $2,769, compared with $4,208 for COBRA costs (chart 1).
- Costs of COBRA coverage to companies with employees electing coverage varies greatly. Data indicate that within the 1994 plan year, COBRA costs bore little relationship to active employee costs (chart 2). In 1993, the most common range (for 68 percent of responding companies) was between 102 percent and 200 percent of the average costs for an active employee. On the extreme end, 9 percent of responding employers had COBRA costs in excess of three times the cost of active employees. COBRA costs more closely resemble individual (as opposed to group) plan costs in that they are not consistent from year to year.
- For 18-month qualifying events, the average length of coverage was 10.3 months. For 36-month qualifying

Table 2
Reasons for Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA) Elections, Plan Years 1990–1994

Plan Year	Total Electing Coverage	Spouse/Dependent Election: Termination or reduction in hours	Spouse/Dependent Election: Death, divorce, plan ineligibility	Employee Election: Termination or reduction in hours
		(percentage)		
1990	100%	16.00%	7.60%	76.40%
1991	100	10.15	8.29	81.56
1992	100	15.00	13.50	71.50
1993	100	7.90	8.00	84.10
1994	100	4.40	17.50	78.00

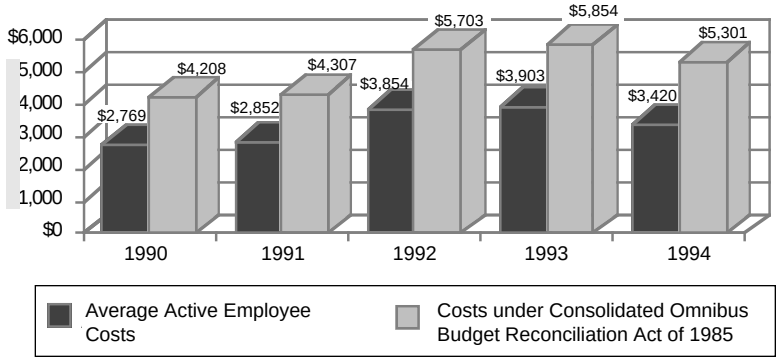
Source: Charles D. Spencer & Associates, Inc., "1994 COBRA Survey: One in Five Eligible Employees Takes COBRA; Employers Pay One-Third," *Spencer's Research Reports* (August 19, 1994): 329.04-1–329.04-6; and "1995 COBRA Survey: Almost One in Five Elect Coverage, Cost is 155% of Actives' Cost," *Spencer's Research Reports* (August 25, 1995): 329.04-1–329.04-7.

events, the average length of coverage was 25 months. Among individuals electing coverage, 1.6 percent converted to an individual policy.

- Difficulties surrounding COBRA coverage, according to surveyed employers, included adverse selection/claims costs (21 percent); difficulties in collecting premiums (30 percent); administrative difficulty such as paperwork and record-keeping (28 percent); excessive time for beneficiary response and tracking eligibility (17 percent); notification from continuee of election or change in status (18 percent); and lack of final rules and complexity of law (14 percent).

COBRA coverage can be considered advantageous for some employees. Consider the following example for a firm with a traditional fee-for-service health plan offered by Blue Cross/Blue Shield plan in the Washington, DC region for plan years starting on March 1, 1995. Under the health plan, the annual premium for a family plan is $10,859. However, the actuarial cost of the plan varies greatly across workers. The actuarial cost for workers under age 30 would be $4,524, and the actuarial cost for workers aged 55 and over would be $12,759. If a worker chooses COBRA coverage, the premium would be $11,076, or 102 percent of the annual premium faced by the employer. Young individuals would have an incentive to forgo COBRA coverage, while older workers would have an incentive to accept COBRA coverage. As a result, the COBRA coverage pool of insured workers is adversely selected—meaning only relatively older, relatively unhealthy individuals will choose COBRA coverage, and the cost of providing health insurance coverage will increase for all workers. If the firm is self-insured, it would receive $11,076 from each COBRA covered worker but would expect to pay $12,759 in claims for workers aged 55 and over and their families. If the firm's COBRA pool is adversely selected, it can expect to pay an even higher amount in health care claims, as evidenced by the Spencer survey. Even if a firm was able to require that COBRA beneficiaries pay 102 percent of their age-rated premium, the firm could pay an even greater amount in health care claims if the pool of COBRA beneficiaries was adversely selected. Older employees would prefer that employers use the average premium in determining COBRA costs, while employers and young employees would prefer to use age-adjusted premium levels.

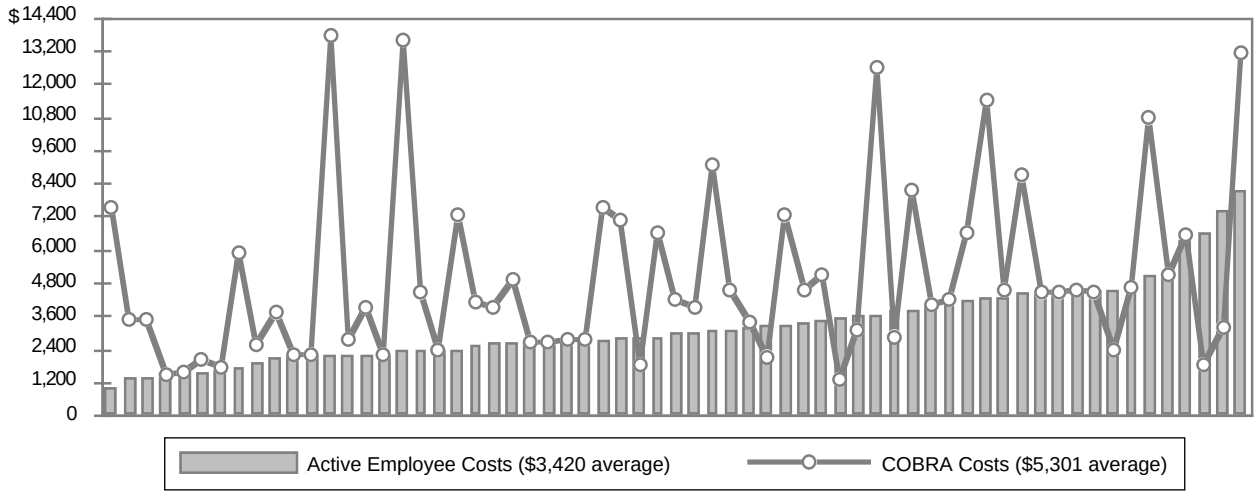
Chart 1
Five Years of Adverse Selection: Average Annual Costs per Participant, 1990–1994



Source: Charles D. Spencer and Associates, Inc., "1995 COBRA Survey: Almost One in Five Elect Coverage, Cost is 155% of Actives' Cost," *Spencer's Research Reports* (August 25, 1995): 329.04-1–329.04-7.

Many employers consider COBRA to be a costly mandate. Assuming that individuals electing COBRA coverage are a

Chart 2
COBRA Costs Compared with Active Employee Costs, 1994



Source: Charles D. Spencer & Associates, Inc., "1994 COBRA Survey: One in Five Eligible Employees Takes COBRA, Employers Pay One-Third," *Spencer's Research Reports* (August 19, 1994): 329.04-1–329.04-6.

relatively higher risk population than the general work force, any expansion in the current law that affects either the size of the firm covered under COBRA or the length of time that former employees could receive continuous coverage would almost certainly increase employer costs for health insurance. In addition, COBRA subsidies, as proposed by the Clinton administration (discussed in the Proposals section), would increase the percentage of eligible workers electing COBRA coverage, driving up the costs to employers. On the other hand, if employers are able to offer plans that are substantially similar to the current plan, with the primary difference being the level of the deductible, employees electing this type of COBRA coverage may be less costly to insure.

The Proposals

There are essentially three types of proposals to increase portability of health insurance: insurance market reforms, changes in the current COBRA law, and adoption of tax-preferred MSAs. Proposals intended to promote individual and group markets increase universal access by limiting preexisting condition exclusions and ending job lock by assuring continuous availability of coverage through an employer or insurer. Employer and individual health plans could not be canceled or denied renewability except in the case of nonpayment of premiums. Individuals would still be free to choose not to have a health insurance plan, and employers could still offer health benefits on a voluntary basis.

Proposals to change the current COBRA law would increase the length of time that continuous coverage could be offered through a former employer, increase the health insurance options former employees have to choose from, and/or provide subsidies to low income individuals who cannot afford COBRA premiums.

Proposals to establish tax-preferred MSAs would allow individuals covered by catastrophic health insurance to place money into a savings account on a tax-preferred basis. Money could be withdrawn from that account to cover medical expenses and nonmedical expenses; however, withdrawals for nonmedical expenses would be subject to income tax and a possible penalty tax. Thus, individuals would spend their own money (a combination of their own contributions and employer contributions to the account that becomes the employee's property) for the majority of health care services and would remain insured for major losses. Individuals could use the funds in these accounts to finance health insurance premiums during periods of unemployment and noncoverage during employment.

H.R. 1818: Proposed by Reps. Bill Archer (R-TX) and Andrew Jacobs (D-IN)

This bill would allow individuals who purchase catastrophic health plans to establish MSAs to help them save for expenses not covered by the plan. Combined individual and employer contributions

There are essentially three types of proposals to increase portability of health insurance: insurance market reforms, changes in the current COBRA law, and adoption of tax-preferred MSAs.

of up to $2,500 for single coverage and $5,000 for family coverage would be allowed on a pretax basis but could not exceed the amount of the health plan's deductible. MSAs would also be available to the self-employed and individuals not participating in the labor force. Pretax contributions would be permitted if the individual is covered by a high deductible health plan, with a deductible of at least $1,800 for single coverage or $3,600 for family coverage. Withdrawals from the MSA would be tax exempt if used for the purchase of qualified medical expenses as defined in IRC sec. 213(d) or the purchase of long-term care insurance, but they would be included in gross income and subject to a 10 percent penalty tax if used to purchase other goods or services. Earnings on the MSA would be taxed at the individual's personal income tax rate.

S. 1028: Proposed by Sens. Nancy Kassebaum (R-KS) and Edward Kennedy (D-MA)

This bill is the first major bipartisan health legislation to be introduced in the 104th Congress. It seeks to provide increased access to, and portability of, health care benefits. **Guaranteed availability of health insurance would be provided because insurers would not be allowed to decline to provide whole group insurance coverage to employers. Insurers and employers would not be permitted to establish eligibility, continuation, enrollment, or contribution requirements for participants based on health status, claims experience, medical history, receipt of health care, evidence of insurability, or disability.** Insured plans would also be guaranteed renewal at the option of the plan sponsor, except in the case of nonpayment of premiums, fraud or misrepresentation, termination of the plan, or the failure of the plan sponsor to meet contribution or participation requirements. Persons covered by health plans through the individual health insurance market would also be guaranteed renewal or continuation of coverage at their option.

This bill would limit preexisting condition exclusions to 12 months under group health plans. If an individual was covered previously, the exclusion period would be reduced by one month for every month of prior coverage. Preexisting conditions must have been treated or diagnosed within the previous six months, and pregnancy would not be treated as a preexisting condition. For individuals seeking coverage directly from an insurer, the insurer would not be permitted to establish eligibility, continuation, enrollment, or contribution requirements based on a participant's health status, claims experience, medical history, or evidence of insurability if the individual had previous coverage for at least 18 months.

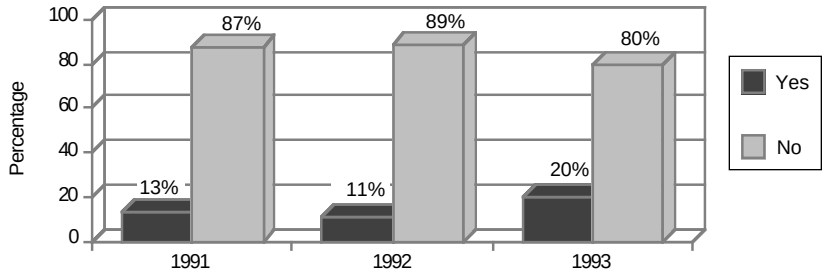
H.R. 1610: Proposed by Rep. William Thomas (R-CA)

Introduced by Rep. Thomas, chairman of the House Ways and Means Subcommittee on Health and cosponsored by all of the members of the subcommittee, H.R. 1610 would reduce waiting periods until preexisting conditions are covered if the individual had prior health insurance coverage. The preexisting condition limitation period would be reduced by one month for every month that the individual had health insurance coverage prior to obtaining the new health insurance coverage. This legislation would only affect individuals covered by group health insurance plans.

Some employers currently require new hires to wait a short period of time before they are eligible to be covered under the new health insurance plan. During this time, the worker does not receive employment-based health insurance benefits and is not required to pay health insurance premiums. The bill would not count these waiting periods as breaks in coverage. In addition, if a break in coverage is longer than 60 days, then prior health insurance coverage would not count toward the preexisting condition exclusion. This bill is designed to

Chart 3

Question 9: "Have you or a family member ever passed up a job opportunity or stayed in a job you would have preferred to leave solely because of health benefits?" 1991–1993



Source: Employee Benefit Research Institute/The Gallup Organization, Inc., *Public Attitudes on Benefit Trade Offs, 1991*, G-28 (Washington, DC: Employee Benefit Research Institute, December 1991); *Public Attitudes on Health Benefits, Part 1*, G-30 (Washington, DC: Employee Benefit Research Institute, February 1992); and *Public Attitudes on Health Benefits, 1993*, G-50 (Washington, DC: Employee Benefit Research Institute, November 1993).
Note: Asked of 1,000 individuals aged 18 or over from randomly generated telephone lists.

alleviate job lock for individuals with preexisting conditions who are uninsured for a short period of time.

The Clinton Administration Proposal

Under the administration's balanced budget proposal, subsidies would be offered to COBRA qualified beneficiaries with low income for six months. The subsidies would be available on a sliding scale basis determined by level of income. The proposal would also prohibit insurers from denying coverage to individuals with preexisting conditions. Insurers would be required to renew health insurance regardless of an individual's health status. However, premiums for health insurance would be allowed to vary with health status. The proposal also has provisions for guaranteed renewal and guaranteed access to health insurance coverage for individuals employed in small firms.

H.R. 1604: Proposed by Rep. Nancy Johnson (R-CT)

This bill would extend provisions of H.R. 1610 to the individual insurance market. **The bill would deny insurers the ability to establish or impose eligibility, continuation, or enrollment requirements for a qualifying individual based on factors directly related to the individual's health status, medical condition, claims experience, receipt of health care, medical history, disability, or evidence of insurability.** An individual would be considered qualified if he or she had previous coverage for at least six months and is not eligible for coverage under a group health plan. Preexisting conditions must have been either diagnosed or treated during the three-month period prior to application for insurance. Waiting periods for preexisting conditions would be limited to six months and would be reduced by the length of prior health insurance coverage. Preexisting condition limitations would not apply to the treatment of pregnancy. Insurers would be permitted to cancel or not renew a policy only in the event of nonpayment of premiums or fraud or misrepresentation.

S. 121: Proposed by Sen. Phil Gramm (R-TX)

This proposal would amend COBRA to allow employers to offer identical health insurance coverage with the only difference being the deductible. This legislation would allow employers to offer health plans with identical coverage with deductibles of $1,000 and $3,000. Penalty-free withdrawals from qualified retirement plans would also be allowed to pay for COBRA coverage. Employers and individuals would not be subject to cancellation or nonrenewal of health insurance coverage, except for certain reasons (i.e., failure to pay the premium). The bill would also allow individuals to establish MSAs with pretax income and allow individuals and the self-employed to fully deduct the cost of health insurance by 2001.

S. 715: Proposed by Sen. Alfonse D'Amato (R-NY)

Sen. D'Amato's proposal includes COBRA reforms, insurance reforms, and the establishment of tax-preferred MSAs. COBRA would be amended to cover firms with 2 or more employees, extend the period of coverage from 18 months to 36 months, allow employers to offer plans that are similar to the current plan, allow

Pending Legislation

H.R. 1818, Archer (R-TX)	Referred to Ways and Means Committee on 6/13/95. Hearing held 6/27/95. Attached to budget reconciliation on 9/18/95. Awaiting action on the House floor.
S. 1028, Kassebaum (R-KS)	Referred to Labor and Human Resources Committee on 7/13/95. Passed as amended by committee on 8/2/95.
H.R. 1610, Thomas (R-CA)	Referred to Ways and Means Committee 5/11/95.
H.R. 1604, Johnson (R-CT)	Referred to Ways and Means Committee 5/10/95.
H.R. 2220, Jacobs (D-IN)	Referred to Commerce, Economic and Educational Opportunities, and Ways and Means Committee on 8/4/95.
S. 715, D'Amato (R-NY)	Referred to Finance Committee 4/7/95.
S. 121, Gramm (R-TX)	Referred to Finance Committee 4/7/95.
Administration Proposal	Announced by President Clinton June 13 as part of the administration's balanced budget proposal. Not considered by Congress.

employers to offer plans with $1,000 or $3,000 deductibles, and guarantee conversion from group rated to individual rated insurance at the end of the coverage period.

This bill would reform the insurance market by guaranteeing that small groups could not have their policies canceled because of claims experience. The bill would also establish limits on rate increases for small employers. Preexisting condition waiting periods would be limited to 12 months, and those conditions would have to have been treated or diagnosed within the past 6 months. In addition, the preexisting condition waiting period would be reduced by one month for every month of previous continuous coverage. Portability would also be guaranteed for coverage obtained through the individual insurance market.

H.R. 2220: Proposed by Rep. Andrew Jacobs (D-IN)

This bill addresses the issues of portability, guaranteed renewal, guaranteed issue, and MSAs. First, **COBRA would be expanded to cover firms with two or more employees. Coverage could be continued under COBRA for up to 36 months for all beneficiaries. Employers could offer coverage that is substantially similar to the previous coverage, instead of identical to the previous coverage, and individuals could choose plans with $1,000 or $3,000 deductibles.** Conversion to individual coverage would be guaranteed at the end of 36 months without regard to preexisting conditions or medical history.

Employees covered by health plans in the small group market would be protected from cancellation or nonrenewal of their health insurance, except in the case of nonpayment of premium, fraud or misrepresentation, noncompliance with the plan's provisions, or departure of the insurer from the small group market in the state. Insurers providing health insurance in the small group market would not be permitted to refuse to provide coverage based solely on the nature of the employer's business or industry.

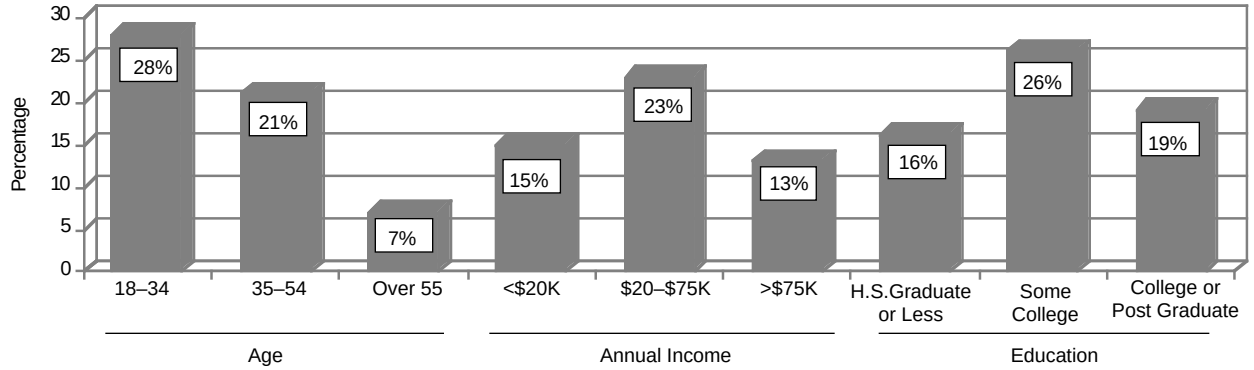
Portability of health insurance is addressed for small groups and individuals by limiting preexisting condition exclusions to 12 months. In order to be considered a preexisting condition, the medical condition must have been diagnosed or treated within the past six months. The exclusion period would be reduced by one month for every month of previous continuous coverage. Refer to the Pending Legislation box for details on the current status of each of the proposals previously discussed.

Reform Issues

Job lock is a primary motivation behind proposals to increase portability of health insurance. Researchers, policymakers, and the general public give varying estimates of the extensiveness of job lock. This section gives a brief overview of these estimates, evidence of the effectiveness of guaranteed issue and guaranteed renewal on job lock, and state reform efforts.

Chart 4

Question 9: Percentage of Individuals Who Responded Yes to, "Have you or a family member ever passed up a job opportunity or stayed in a job you would have preferred to leave solely because if health benefits?," by Age, Annual Income, and Educational Level, 1993



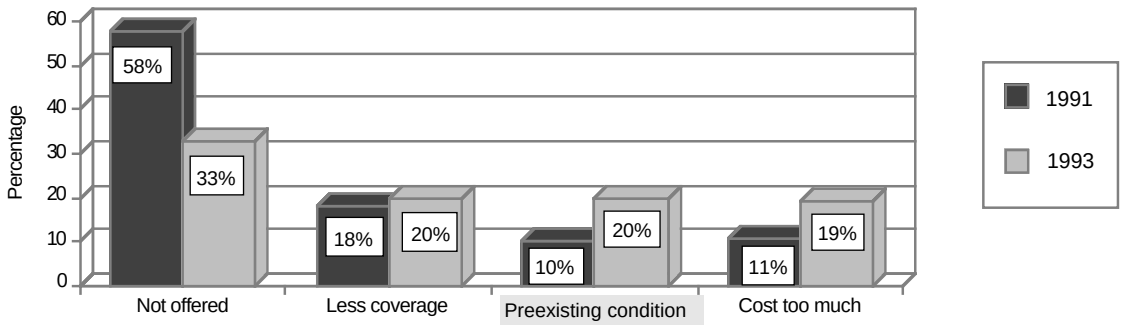
Source: Employee Benefit Research Institute/The Gallup Organization, Inc., *Public Attitudes on Health Benefits, 1993*, G-50 (Washington, DC: Employee Benefit Research Institute, November 1993).

Public Opinion

The Employee Benefit Research Institute (EBRI), in conjunction with The Gallup Organization, Inc., conducted several public opinion surveys regarding Americans' perspective on job lock between 1991 and 1993. **In 1993, 20 percent of surveyed Americans indicated they or a family member passed up a job opportunity based solely on health benefits, up from 11 percent in 1992 and 13 percent in 1991** (chart 3). Among age groups, 18–34 year olds were most likely to have passed up a job opportunity based solely on health benefits (28 percent). This compares with 21 percent among individuals aged 35–54 and 7 percent among individuals aged 55 and over (chart 4). Individuals with an annual income of $20,000–$75,000 were most likely to have passed up a job opportunity based solely on health insurance (23 percent) (chart 4). When asked in further detail the reason for not changing jobs based on health benefits, the reason most often cited was that health benefits were not offered by the prospective employer (58 percent in 1991) (chart 5). The likelihood of this reason declined to 33 percent in 1993 yet remained the most commonly cited reason. (COBRA would allow these individuals to maintain coverage if they are willing to pay up to 102 percent of the premium.) Among other

Chart 5

Question 10: "Which of the following best describes the reason you or your family member chose not to change jobs?," 1991 and 1993



Source: Employee Benefit Research Institute/The Gallup Organization, Inc., *Public Attitudes on Benefit Trade Offs, 1991*, G-28 (Washington, DC: Employee Benefit Research Institute, December 1991; and *Public Attitudes on Health Benefits, 1993*, G-50 (Washington, DC: Employee Benefit Research Institute, November 1993).
Note: The balance of reasons are the following: in 1991, other (3 percent); in 1993, other (4 percent); secure at present job (3 percent); and none of these reasons (1 percent).
Refer to charts 1 and 2 for the number of individuals who responded yes to the question, "Have you or a family member ever passed up a job opportunity or stayed in a job you would have preferred to leave solely because of health benefits?"

Table 3
Employment-Related Health Insurance and Job Mobility: Alternative Estimates of Job Lock in the United States

Study	Sample/Method	Magnitude of Job Lock
Mitchell (1982)	Wage earners 18–65 years of age from the Quality of Employment Survey in 1973 and 1977. Estimated a reduced form probit equation of likelihood of job change using baseline insurance status.	Probability of job change for men reduced by 4.24 percentage points.[a] Not statistically significant.
Madrian (1994)	1987 National Medical Expenditure Survey. Sample of married men aged 20–55. Used a probit estimate of the likelihood of job change to derive a "difference in the difference" estimator; examined three empirical tests for job lock.	Mobility rates reduced by 30 %–31% for those with employment-related coverage compared to those without such coverage; mobility rates reduced by 33%–37% for those married men with employment-related coverage and large families (proxy for medical care costs); mobility rates reduced by 67% for those with employment-related coverage and a pregnant wife (proxy for medical care costs). All statisticallysignificant.
Holtz-Eakin (1994)	1984 wave of the Panel Study of Income Dynamics. Sample of full-time workers aged 25–55. Derived a "difference in the difference" estimator for job changes over one- and three-year intervals.	For job changes during 1984–1985: mobility rates for married men reduced by 1.59 percentage points (result insignificant); rates for single women reduced by 1.06 percentage points insignificant); (job lock effects for other groups not found (wrong sign and insignificant). Results for three-year intervals insignificant.
Cooper and Monheit (1993)	1987 National Medical Expenditure Survey. Sample of wage earners aged 25–54. Predicted whether workers would gain or lose coverage on a new job and used the results in a structural probit model of job change. Compared their mobility rates to the mobility rates of workers whose insurance status was expected to remain the same.	Among workers likely to lose coverage: mobility for married men reduced by 24.8%; single men by 23%; married women by 34.7%; single women by 38.8%. Results significant for one- or two-tail tests.

Source: Alan C. Monheit, and Philip F. Cooper, "Health Insurance and Job Mobility: Theory and Evidence," *Industrial and Labor Relations Review* (October 1994): 68–85.
[a]This figure is based on Monheit and Coopers' computation based on coefficient and mean values reported by Mitchell (1982). Mitchell (1983) did not provide an explicit estimate of job lock.

reasons cited, having a preexisting condition showed the largest increase, rising from 10 percent in 1991 to 20 percent in 1993.

In addition to public opinion surveys, several studies have been conducted regarding job mobility and health insurance. The findings are mixed and do not uniformly support or refute the existence of job lock. Studies that do support the theory of job lock show wide variation in the magnitude of its effects based on demographic and employment-based characteristics. Findings from these studies are summarized in footnote 1 and in table 3.

[1] *Mitchel (1982 and 1983) conducted one of the first studies regarding the magnitude of job lock. Mitchell found evidence that the loss of a pension promise was a particularly strong deterrent to quitting. While Mitchell also found evidence that medical coverage deterred employees from quitting, it was at a fairly low level of reliability.*

Madrian (1993) and Cooper and Monheit (1993) provided the strongest evidence of job lock. Madrian estimates that job lock reduces the voluntary rate of those with employment-based health insurance by 25 percent, from 16 percent to 12 percent per year. Cooper and Monheit found that policyholders of employment-based health insurance were three and one-half times less likely to change jobs than uninsured workers. However, they did not find worker or dependent health conditions to be associated with job mobility.

Cooper and Monheit also indicate that mobility rates vary based on worker characteristics. Most likely to change jobs were younger workers with high hourly wage rates. The authors also indicate that married men who expected to lose coverage were 23 percent less likely to change jobs. Workers who were likely to gain coverage through a change in employment were 52 percent more likely to change jobs than those whose insurance prospects were not expected to change.

Madrian cites three factors to consider in evaluating the implications of job lock for economic efficiency: does job turnover result in a better match between workers and firms and thereby increase productivity; to the extent that job lock does lower porductivity, are loses temporary or permanent; and is job lock a benefit or cost for firms?

Gruber and Madrian (1994) found that state continuation of coverage mandates were successful in reducing job lock. They found that one year of continuous benefits was associated with a 10 percent increase in mobility among those with health insurance.

In a later publication, Monheit and Cooper (1994) found that job lock was present in the labor market but that the proportion of workers affected and the magnitude of the welfare loss was less than generally supposed.

Holtz-Eakin (1993) indicated that there was little evidence that health insurance provision interferes with job mobility. In his study of individuals who changed jobs as compared with those who did not, he found that, analyzing health insurance alone, there was a correlation between job mobility and health insurance. However, when looked at as part of a total compensation package, the importance of health insurance with regard to incentive to change jobs disappears.

Proposals that would establish guaranteed issue and guaranteed renewal may make access universal but are unlikely to achieve universal coverage or significantly increase coverage.

Guaranteed Issue and Guaranteed Renewal

Proposals that would establish guaranteed issue and guaranteed renewal may make access universal but are unlikely to achieve universal coverage or significantly increase coverage. Researchers evaluating the Robert Wood Johnson Foundation (RWJF) projects for the medically uninsured found that small employers' primary reason for not offering health insurance was the high cost of coverage: 85 percent of employers not offering coverage cited high premiums as an important reason (McLaughlin, 1991). Although the RWJF demonstration projects did not reform local small group insurance markets the way that their proposals would, the goals are similar: to stabilize the cost of insurance to small businesses and distribute these costs more equitably. However, only 17 percent of employers who had not previously offered insurance enrolled in even the most successful RWJF project targeted at small employers (McLaughlin, 1991). If the experience of these projects is any indication of what might happen nationally under the proposed reform initiatives, small group insurance market reform may result in a minority of employers choosing to purchase health insurance.

Changes in the insurance market might stabilize premiums somewhat, but the ability of individual groups to select the risks they associate with would likely result in continued segmentation of the risk pool. Small employers would probably continue to face higher premiums than larger employers, and individuals would continue to face higher costs than those who purchase health insurance in a group, as long as these reforms do little to address increases in health care cost inflation.

State Reform

Beginning in 1990, many states have taken the lead in attempting to reform the small group market for health insurance. **As of December 1994, 43 states have enacted legislation for guaranteed renewal, 38 states have enacted legislation for guaranteed issue, 41 states have enacted legislation for increased portability, and 39 states have enacted legislation that limits preexisting condition exclusions** (Markus, et al., 1995). These laws are based largely on the Small Employer Health Insurance Availability Model Act, developed and continually refined by the National Association of Insurance Commissioners.[2] In general, these laws affect firms with fewer than 25 or 50 employees, although some states include firms with as many as 100 workers. The purpose of these laws is to increase health insurance coverage and to reduce job lock; however, some states have been reporting unintended side effects. It is too early to measure the effects of these laws on levels of health insurance coverage and job lock, but anecdotal evidence indicates that, in some states, there is a movement of small firms out of the small group market for health insurance. Because states are limited in the area of health insurance reform under the Employee Retirement Income Security Act of 1974 (ERISA), which preempts state authority over self-insured health plans, these firms are choosing to self-insure, thereby circumventing the state laws. This not only has the effect of undermining the intent of the legislation but also runs the risk of increasing adverse selection in the small group health insurance market. In addition, states have been reporting an increase in the prevalence of small group associations that were formed for the purpose of purchasing health care services for their members.

Conclusion

Proposals to reform the health care system incrementally would expand COBRA,

[2] *For more information on the National Association of Insurance Commissioners' model, see U.S. General Accounting Office, 1995.*

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relax preexisting condition exclusions, guarantee access to health insurance, and/or guarantee renewal of health insurance for individuals and employees of small firms. Under many proposals, individuals would also be allowed to make pretax contributions to MSAs. These proposals are intended to make health insurance more portable and more affordable; however, they may have no effect whatsoever on health insurance premiums and health insurance coverage. In addition, employer and employee costs for health insurance and health care may increase and coverage may decrease.

Concern about the portability of health insurance primarily arises in situations where an individual is leaving, or would like to leave, a job. If health insurance is not offered by a prospective employer, if the worker must satisfy a waiting period before becoming eligible for coverage, if the benefits package offered through the prospective employer is less generous, or if the employee (or a dependent) has a medical condition that is considered a preexisting condition and would not be covered by the new plan, the employee may opt to remain with his or her current employer—a situation known as job lock. **Expansions in COBRA may not have any effect on portability. Employers can charge up to 102 percent of the premium for COBRA coverage, making COBRA coverage unaffordable for many workers. Because cost is a major factor, if there is no reduction in cost (or health care cost inflation) there could be little or no increase in coverage.** In addition, many employers consider COBRA to be a costly mandate. According to one survey, average COBRA costs were $5,301 per COBRA covered worker, compared with $3,420 for active employees. Any expansion of COBRA would almost certainly increase employer cost for health insurance.

Proposals that would establish guaranteed access and guaranteed renewal of health insurance for employers and individuals may do little to increase coverage and may, in fact, decrease coverage. Results from the RWJF demonstration projects indicate that small group insurance market reform may result in a minority of employers choosing to purchase health insurance. Guaranteed issue and guaranteed renewal may have the effect of increasing average premiums if insurers and employers are forced to accept relatively unhealthy individuals. Many states have already enacted small group insurance market reforms. While it is still too early to measure the effects of these laws on health insurance coverage, anecdotal evidence indicates that there has been a movement of small firms out of the small group market. These plans are choosing to self-insure, thereby circumventing the state law because of ERISA preemption. Some states have also noticed an increase in the prevalence of small group purchasing associations.

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