STATE OF HAWAI'I
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DEPT. COMM. NO. 73

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The Honorable Shan S. Tsutsui
President of the Senate
State Capitol, Room 409
Honolulu, Hawai'i 96813

The Honorable Calvin K.Y. Say
Speaker of the House of Representatives
State Capitol, Room 431
Honolulu, Hawai'i 96813

Dear Mr. President and Mr. Speaker:

This letter responds to the Legislature's request for an analysis on the effects of Act 227, Session Laws of Hawai'i (SLH) 2008, relating to insurance, to be repealed on June 30, 2011. We also analyzed the effects of Act 120 of the same legislative session, since it also relates to insurance and affects the same group of small businesses with no employees—sole proprietors and independent contractors.

Background

On September 6, 2005, Sumi U.C. Sylva filed a complaint against the Hawaii Management Alliance Association, currently doing business as the Hawaii Medical Assurance Association (HMAA), with the Department of Commerce and Consumer Affairs (DCCA). Sylva had requested that HMAA allow her to purchase health insurance without requiring her to purchase life and dental insurance as well. The insurer refused the request, replying that health insurance for its small business plans for sole proprietors was not available "unbundled." Larger client groups are not required by HMAA to purchase bundled insurance products. At the time, the 1974 Prepaid Health Care Act, which requires most employers to provide health insurance to employees working 20 hours or more, did not apply to businesses that had no employees such as self-employed individuals, or to sole proprietors, which are businesses owned and managed by a single individual. HMAA was the only insurer offering group health insurance policies to sole proprietor businesses.

In 2005, the insurer acknowledged that it had been requiring customers to buy bundled insurance, a practice it had engaged in since 1989. It also argued that allowing single employee groups to pick and choose among parts of a plan would inevitably raise plan costs. However, on September 7, 2007, the Insurance Division concluded that HMAA's bundling practice violated

Section 431:13-103(a)(4)(b), Hawai‘i Revised Statutes (HRS), and was an unfair method of competition and an unfair business practice under Section 431:13-102, HRS. On October 5, 2007, HMAA appealed the agency's decision before the Circuit Court of the First Circuit.

Act 227 and Act 120 enacted

Senate Bill No. 2314, Senate Draft 1, House Draft 2, Conference Draft 1 (S.B. No. 2314, S.D.1, H.D.2, C.D.1), was drafted in response to the above-mentioned enforcement action by the state insurance commissioner against HMAA and became law on July 8, 2008, as Act 227. Act 227 authorizes the Insurance Division to allow broader combinations of health insurance benefits by allowing an exception to the definition of boycott, coercion or intimidation, anti-competitive business practices banned in Chapter 431, HRS. Specifically, Act 227 provides a temporary exemption for accident and health insurers with less than 5 percent of the health insurance market share, so they can bundle different types of benefits in a single policy. According to Act 227, bundling, "provides broader health care coverage in single unified policies, ultimately resulting in lower overall premiums, fostering greater competition within Hawai‘i insurance marketplace, and providing consumers with greater flexibility, coverage, and pricing options." Act 227 is scheduled to sunset on June 30, 2011.

In testimony opposing S.B. No. 2314, S.D.1, H.D.1, the insurance commissioner objected to the bill enacted as Act 227, because HMAA's health plan is sold as a mandatory package. The commissioner testified that: "The anti-bundling rules are there to protect consumers; it would be bad policy to allow health insurers to use their market power to force consumers to take insurance they don't want or need." The commissioner instead expressed support for legislation that would make sole proprietors eligible for group coverage. The attorney general also opposed the bill for similar reasons, favoring consumer choice.

In testimony supporting its long standing practice, HMAA's chairman of the board and chief executive officer testified that allowing insurers to continue bundling different classes of insurance, such as health, dental, and vision, provides broader health care coverage, would result in lower overall premiums, fosters greater competition, and provides consumers with greater flexibility, coverage, and pricing options.

Less than two months before Act 227 took effect, Act 120 became law, requiring group health insurers to offer small group health plans to self-employed individuals properly registered with DCCA. The law also allows the state insurance commissioner to exempt some insurers from offering small group health plans based on certain criteria. While Act 120 does not have a stated purpose per se, according to testimony submitted by the state insurance commissioner in support of House Bill No. 2224, House Draft 1, Senate Draft 1 (H.B. No. 2224, H.D. 1, S.D. 1) the bill would help reduce the number of uninsured sole proprietors in Hawai‘i. In addition, the Senate Judiciary and Labor Committee's standing committee report for H.B. No. 2224, H.D. 1, S.D. 2 (the version that became law) stated the bill's purpose was to increase accessibility to health insurance for self-employed individuals, who otherwise could not obtain health insurance if they are not incorporated. Act 120 is scheduled to sunset on July 1, 2013.

Table 1
Timeline of Events Relating to Act 227 and Act 120

Sept. 6, 2005	Sept. 7, 2007	Oct. 5, 2007	July 1, 2008	July 8, 2008	Oct. 2, 2008
Consumer complaint lodged against HMAA by Sumi U.C. Sylva.	HMAA bundling found to violate law.	HMAA appeals to the First Circuit Court.	Act 120 takes effect.	Act 227 takes effect.	Sylva case is dismissed with prejudice.

Source: Office of the Auditor

Act 227: minimal impact on the insurance market

Based on market figures compiled by the state Insurance Division, four insurers are eligible for the Act 227 exemption: HMAA, the University Health Alliance, Ohana Health, and EverCare Hawai'i. Of these only HMAA utilizes the exemption tying health insurance with life insurance into a single policy sold to sole proprietors and small businesses. Since their market shares are equal to or greater than 5 percent, the Hawaii Medical Service Association (HMSA), Hawai'i's largest health insurer, and Kaiser Permanente Hawai'i and AlohaCare, which are a distant second and third in market share respectively, are not eligible for the exemption.

Prior to the enactment of Act 227, HMAA reported having 932 sole proprietor and small business plan health insurance policies that were bundled with life, prescription drug, dental, and vision insurance. Those policies generated $5.4 million in annual premiums. As of November 9, 2010, HMAA reported that it had sold an additional 308 sole proprietor and small business bundled policies. Despite those sales, HMAA's current sole proprietor and small business plan membership is now 815, a decrease of 13 percent. However, these policies accounted for higher premiums of $7.4 million a year.

Act 120: an increase in group health insurance to the self-employed

We found that since the passage of Act 120, access to group rate health insurance to sole proprietors has increased overall giving these small businesses with no employees more of a choice. Act 120 is spurring insurers such as HMSA and Kaiser to sell group rate health insurance to self-employed individuals and sole proprietors. For example, in 2010, HMSA and

Kaiser have a total of 463 enrollees in sole proprietor plans. This is in addition to HMAA's 815 enrollees in sole proprietor and small business plans as shown in Table 2.

In effect, HMSA and Kaiser have filled some of the need to help sole proprietors and small businesses obtain affordable health related insurance identified by HMAA when it advocated for Act 227. Moreover, HMSA believes that since Act 120 has made access to health care coverage uniformly available to small employers, the provisions of Act 227 are unnecessary. However, we note that Act 120 sunsets on July 1, 2013.

Table 2
Sole Proprietor Group-Rate Policies in Effect in 2010

Insurer	Sole Proprietor Policies
HMAA	815 as of Nov. 9, 2010
HMSA	405 as of Sept. 30, 2010
Kaiser	58 as of Oct. 27, 2010

Source: Office of the Auditor

HMAA may no longer qualify for Act 227's exemption

Act 227 does not specify how market share compliance is to be determined. The Insurance Division has not adopted administrative rules relating to Act 227, so there are no criteria for determining whether HMAA's market share has reached 5 percent. Currently, the Insurance Division is tracking compliance based on the number of members.

If market share is to be measured by the number of members, HMAA may soon be ineligible to bundle policies due to its acquisition of the fully insured health insurance membership of Summerlin Life and Health Insurance Company announced in April 2010. In 2009, HMAA and Summerlin separately reported a total of 48,018 members to the Insurance Division, 5 percent of the overall market. However, HMAA's actual market share may be smaller because the Insurance Division's figures exclude an estimated 10 percent of policies administered by out-of-state health insurers. On September 30, 2010, HMAA reported having 41,970 members.

Table 3
2009 Health Provider Market Share Based on Members

Company	Members	Market Share (percent)
Hawaii Medical Service Association	565,904	58.7
Kaiser Permanente	223,795	23.2
AlohaCare	71,688	7.4
University Health Alliance	30,493	3.2
Hawaii Medical Assurance Association	25,770	2.7
Ohana Health Plan	23,344	2.4
Summerlin	22,248	2.3
EverCare Hawai'i	N/A	N/A

Source: Insurance Division

If Act 227 were to sunset, the Insurance Division has no intention of requiring HMAA to unbundle tied policies sold prior to and during the exemption period. However, the division said it would investigate consumer complaints against HMAA, if the law is repealed. The insurer continues to dispute the State's legal position and would likely pursue remedies such as legislative action and litigation to retain its ability to bundle policies.

Recommendation

We found that Act 227, SLH 2008, has had a minimal effect on insurers' ability to sell health insurance and sole proprietors' access to health insurance. Furthermore, we found that Act 120, SLH 2008, enacted two months before Act 227, has increased health insurance access and choice for small businesses with no employees and sole proprietors. Therefore, we recommend Act 227, SLH 2008, be allowed to sunset on June 30, 2011.

Please do not hesitate to contact me should you have any questions.

Sincerely,

Marion M. Higa

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State Auditor