



South Carolina Department of Insurance

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MARK SANFORD
Governor

SCOTT H. RICHARDSON
Director of Insurance

July 15, 2010

The Honorable Kathleen Sebelius, Secretary
U.S. Department of Health & Human Services
200 Independence Avenue, SW
Washington, D.C. 20201

Re: Individual Market Medical Loss Ratio Waiver

Dear Secretary Sebelius:

Thank you for your leadership as our nation makes the important transitions in our health insurance marketplaces required by the Affordable Care Act (the Act). The State of South Carolina has always emphasized providing affordable, meaningful health insurance to its citizens that is backed by solvent, well managed health insurers and health maintenance organizations (HMOs). As a part of its regulatory responsibilities, the Department of Insurance monitors the insurance market and attempts to address issues related to the availability and affordability of insurance products for South Carolina's consumers. The health insurance market is no exception. South Carolina has introduced a number of legislative reforms intended to increase the availability of health insurance products at reasonable prices. The Act has been passed by Congress with the same basic objective.

In reviewing the provisions of the Act, it has come to our attention that some provisions may have an unintended, deleterious impact on the consumers of this state. If implemented as currently proposed, the 80% medical loss ratio requirement will not increase consumer choice in health insurance products or make coverage more affordable or readily available. As you know, the health insurance marketplace differs among the states. The Act takes this variation into account and allows state-by-state waivers to minimize disruption in the existing individual markets as we make the transition to the exchange-based markets in 2014.

Accordingly, South Carolina requests a waiver of the 80% minimum medical loss ratio requirement for individual health insurance policies offered in South Carolina until 2014 in accordance with Section 2718 of the Public Health Service Act. *See* Patient Protection and Affordable Care Act Section 1001(5) and Section 10101(f). To avoid the potential problem of consumers not being able to find health insurance coverage at affordable prices, we propose to phase in the 80% loss ratio requirement and would respectfully request that the following minimum medical loss ratio requirements be substituted as the applicable loss ratios for the State of South Carolina: 65% in 2011, 70% in 2012, 75% in 2013, and 80% in 2014 and thereafter. The reasons that support gradually phasing in the minimum loss ratio requirements follow.

I. Current Rate Filing and Guaranteed Loss Ratio Requirements

Under South Carolina law, individual health insurance rates must be filed with the Department of Insurance (DOI) in one of two ways. First, the rates must be filed for prior approval by the DOI with justification for the proposed rate increase. The DOI has the right to request additional data and to reject the rate increase. Second, the health insurance issuer must file new rates with a loss ratio guarantee. If the loss ratios for the

products in the filing fail to meet the guaranteed loss ratio, the issuer must refund premium in the subsequent year so that the guarantee is met. *See* S.C. Code Ann. § 38-71-310(E) (2002). In all cases, the DOI uses the National Association of Insurance Commissioners' (NAIC) *Guidelines for Filing of Rates for Individual Health Insurance Forms* to determine the minimum acceptable loss ratio for health insurance products. For comprehensive health insurance products, this minimum medical loss ratio is 55%, depending on the renewability clause stated in the contract. In South Carolina, the medical loss ratio is defined as the ratio of incurred claims to earned premiums.

II. Underwriting and Its Impact on Loss Ratios

Moreover, South Carolina law allows issuers to underwrite new applicants for health insurance coverage. An individual may be accepted as a standard risk, offered a higher rate based on their health status, offered a policy with a condition rider based on their health status, or rejected for coverage by the health insurance issuer. Health insurance that is underwritten in this way demonstrates significant variation in loss ratios based on the duration of the policy as the effect of the underwriting process wears off as the duration lengthens. Individuals in their first year of coverage typically have an average loss ratio that is significantly less than the average loss ratio for individuals who have had coverage for three or more years. The durational mix of an issuer's block of business significantly affects its average loss ratio for its entire block. Suddenly implementing a new, significantly higher minimum medical loss ratio would have a very different impact on different health insurance companies based upon the durational mix of their blocks of business even if every other aspect of how those companies do business is identical.

III. Commissions and Their Impact on Loss Ratios

Most individual health insurance is sold through insurance producers (i.e., agents) in South Carolina. Health insurance issuers must include the commissions paid to producers in their health insurance rates. Competition between the state's issuers requires each issuer to maintain an adequate commission arrangement for producers. The transition to an 80% minimum medical loss ratio will require changes in these commission arrangements. Since some of the current arrangements are contractual between the health insurance issuer and the producer, it will take time for changes in the commission arrangements to have a full impact on the aggregate level of commissions paid by an issuer.

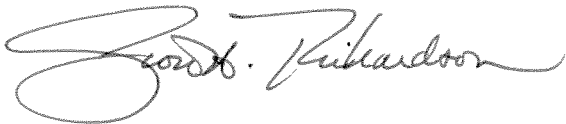
IV. Insurance Availability Issues

Absent a waiver, the South Carolina Department of Insurance believes that the new federal minimum medical loss ratio will create disruption in our individual health insurance market. This will have a disparate impact on smaller carriers and could cause a decrease in competition as carriers exit the marketplace, thus resulting in less consumer choice. We believe that health insurance issuers can make a transition from the existing requirements to the new requirements, but that the transition should be phased in to allow issuers the time to make the necessary adjustments, encourage them to stay in the market, and to minimize the potential market disruptions. If issuers are not allowed a period of transition from the current South Carolina requirements to the new federal requirements in 2014, consumers will not be able to find coverage and will be denied the choice the Act was intended to create. While we have not received reports of market exits from major carriers, we are increasingly concerned that some of our smaller carriers will exit the market, making health insurance less available and affordable. This will likely result in the complete domination of the market by one or two carriers. This is not our understanding of the purpose of the Act nor do we believe that it is in the best interest of South Carolinians.

Therefore, we would ask for approval of our waiver request and plan for gradually phasing in the minimum medical loss ratio requirements. Based upon the information set forth above, we believe you will agree with our determination that implementing an 80% minimum medical loss ratio for individual products before 2014 will destabilize the South Carolina individual health insurance marketplace and hurt consumers. As noted above, we request that the following minimum medical loss ratio requirements be substituted for the state of South Carolina: 65% in 2011, 70% in 2012, 75% in 2013, and 80% in 2014 and thereafter.

Thank you for your consideration of this request. Please feel free to contact me at (803) 737-6805 or Leslie Jones, the Department's chief actuary, at (843) 577-3413 if you have any questions.

Sincerely,

A handwritten signature in cursive script that reads "Scott Richardson". The signature is written in black ink and is positioned above the printed name and title.

Scott Richardson, CPCU
Director