



# AMERICAN ACADEMY of ACTUARIES

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July 12, 2010

Office of Consumer Information and Insurance Oversight  
Department of Health and Human Services  
Attention: OCIO-4150-IFC  
P.O. Box 8016  
Baltimore, MD 21244

**Re: Dependent coverage to age 26—comments regarding interim final rule**

To Whom It May Concern –

On behalf of the American Academy of Actuaries’<sup>1</sup> Benefits and Eligibility Work Group, I appreciate this opportunity to provide comments to the Departments of Health and Human Services, the Treasury, and Labor on the recently released interim final rule on Sec. 2714 of the Public Health Service Act (PHSA). These regulations clarify issues related to the requirements for a plan or issuer offering dependent coverage of children to make such coverage available for children until they reach the age of 26.

Our comments are focused on three areas within the regulations that may cause some disruption in the individual and group markets and/or have a significant financial impact on insured costs. In addition, based on our reading of the regulations, it is unclear whether the financial impact of the issues discussed in this letter is reflected in the economic impact study performed by the departments. The three areas of concerns are: premium surcharges due to age, limiting coverage to dependents not eligible for employer-sponsored insurance (ESI), and the definition of “dependent.” These issues are described below.

## **Premium Surcharges Due to Age**

Section II. A. of the interim final rule states that “the terms of the plan or policy for dependent coverage **cannot vary based on the age of a child**, except for children age 26 or older. Examples illustrate that **surcharges for coverage of children under age 26 are not allowed** except where the surcharges apply regardless of the age of the child...” [emphasis added] Below we cite Sec.147.120 (e) *Example 1*.

Example 1. (i) Facts. A group health plan offers a choice of self-only or family health coverage. Dependent coverage is provided under family health coverage for children of participants who have not attained age 26. The plan imposes an additional premium surcharge for children who are older than age 18.

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<sup>1</sup> The American Academy of Actuaries is a 16,000-member professional association whose mission is to serve the public on behalf of the U.S. actuarial profession. The Academy assists public policymakers on all levels by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

(ii) Conclusion. In this *Example 1*, the plan violates the requirement of paragraph (d) of this section because the plan **varies the terms for dependent coverage of children based on age**. [emphasis added]

We believe the requirement, as well as *Example 1*, creates some unintended ambiguity. In particular, the conclusion under *Example 1* does not reference “surcharge,” thus leading to an alternative interpretation that age rating for dependents is no longer allowed. These regulations apply to both group and individual health insurance coverage. If age rating for dependents is not allowed, it would create rate disruption in the market. Age rating for dependents needs to be maintained so that the rates are reasonable in relation to the benefits provided. In the next paragraph, we describe current rating practice in the individual market and the effect of not allowing age rating for dependents.

In the individual market today, many carriers consider the age of the dependent when setting the family premium for policies. While the practice is predominant in the individual market, this practice also occurs in the group market. Standard risk premium rates typically vary by each age or age grouping. A carrier does this to be consistent with how it rates all other ages (i.e., to match premium rates with the expected medical expenses for the risk class of age). Expected medical expenses, at very young ages in particular, vary significantly from other ages of dependents; in practice, carriers have reflected this in higher standard premium rates for the youngest of dependents than for others. For example, claims costs for younger children (ages 0 to 2) are much higher than for children who are age 2 and older. Reflecting the age of dependents, when establishing premium rates for a family policy, more accurately reflects the true costs for each family. Eliminating this ability will require insurers to charge the same dependent rate to each family regardless of age. Since this varies from current practice, families with older children will likely see an increase in their premium, and families with very young children will likely see a decrease in their premium.

We request clarification on whether the intent of the regulations is to limit a plan’s ability to use age-based surcharges for these newly insured dependents (to age 26) as a means of discouraging them from electing to continue coverage under their parent’s plan. Since the regulations specifically prohibit a premium “surcharge” for dependent coverage, one interpretation is that the regulations allow the continuation of the practice of varying premiums for dependent coverage by age. In other words, as long as no extra surcharges are levied above and beyond current rating practices, age rating for dependents would be allowed. We suggest a revision of the regulations and relevant examples to remove any unintended ambiguity.

In the event the intent was to disallow age rating on dependents, other alternatives should be considered. One alternative would be to allow a carrier to continue the practice of charging premium rates by age; however, once the dependent reaches a particular age, the rates would remain constant. For example, the expected claim costs for individuals in their 20s do not vary significantly by age, which is consistent with current pricing practices for this age group. Thus, disruption in the market would be minimal.

## **Limiting Coverage to Dependents Not Eligible for Employer-Sponsored Insurance (ESI)**

The interim final rule states that a grandfathered health plan may exclude from coverage an adult child who has not attained age 26 only if the child is eligible to enroll in an employer-sponsored health plan other than his or her parent's group health plan.

Enabling currently insured young adults to shift coverage from their own policy to that of their parent's policy could create unintended adverse dynamics or uncertainty in the group market. We provide an example to demonstrate an unintended consequence of allowing young adults to make this shift.

Example: A group health plan offers a choice of self-only or family health coverage. Dependent coverage is provided under family health coverage for children of participants who have not attained age 26. Under this dependent tier structure, family premiums do not vary by the number of dependents. Therefore, a working adult child can be added to an existing family contract with no increase in premiums rates.

The magnitude of the loss in premium due to the addition of adult children will vary by the dependent rating structure offered.

What if the adult child is working full time at an employer that currently offers insurance but requires the employees to pay a portion of the premium? This adult child is currently enrolled in his or her employer's plan and paying a portion of the premium. However, the adult child will now be able to opt out of this plan and enroll under his or her parent's plan for free. It would be a wise economic decision for the young adult to elect to enroll under the parent's plan. What is the impact on the premium for his employer's plan?

Generally, most groups employ what is commonly called a "composite rating." In other words, there is a common rate for each dependent option for the group (i.e., a common single rate for all those who elect employee-only coverage, a common family rate for all those who elect employee-plus-dependents coverage.) In states in which age rating is allowed, the composite rates reflect the average age distribution of all employees. Therefore, the younger employers are subsidizing the older employers.

In this example, if the adult child were to withdraw from his or her employer's insurance program, the group's average age would increase, resulting in a higher premium rate for the rest of the group. Small employers are most susceptible to material increases due to young adults migrating to their parents' plans, because they have fewer employees over whom to spread the lost subsidy. However, even large employers could experience increases, depending on the distribution by age of their currently insured employees.

We have illustrated one scenario, but there are other scenarios depending on the structure of the dependent tier options under the parent's contract, as well as the individual circumstances of the family (i.e., if there are other siblings currently insured under the parent's policy). The opportunities for selection will vary by each of these scenarios. However, the situation cited in the above example is applicable for many groups.

One way to address these concerns is to allow both grandfathered and non-grandfathered plans to exclude an adult child who is eligible to participate in their employer's insurance plan.

### **Definition of Dependent**

The interim final regulations clarify that financial dependency, residency with participant/subscriber, student status, employment, and eligibility for other coverage may not be used to define a dependent. These are practices that carriers currently use to assist them in identifying dependents for insurance coverage. Since the definition of dependents is much broader in the regulations, we believe there is potential for significant anti-selection, especially prior to the implementation of the individual mandate requirement. There are strong incentives for individuals who need medical services to enroll in an insured plan by any means, setting up a system prone to misuse. Adoption of a definition for dependent that is difficult to verify could increase administrative costs and increase the likelihood for misuse. We believe this anti-selection issue will have a significant financial impact, especially in the first few years of implementation of the regulations.

### **Economic Impact**

The interim final rules included an economic impact of this portion of the law. However, there were insufficient disclosures of assumptions and methodologies for us to provide an independent review. It is unclear whether certain scenarios were taken into account in the economic impact calculation. Examples include, but are not limited to, the impact of the items discussed in this letter—namely, the upward pressure on rates and market disruption as a result of (1) age rating no longer being allowed; (2) the anti-selection effect of young adults currently enrolled or eligible for ESI moving to their parent's plans and paying a lower dependent rate; (3) the anti-selection effect of carriers' reduced ability to verify dependent eligibility. Furthermore, we believe it should be noted that the economic impact calculated in the interim final rule is an average, and the actual impact on individual carriers, employer groups, and/or individual insureds could vary significantly from this average and from one another. Therefore, without understanding the assumptions and methodologies used in the economic impact calculation, we are unable to comment on this analysis.

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We would appreciate the opportunity to discuss any of these items, including the assumptions and methodologies behind the economic impact section, with you at your convenience. If you have any questions or would like to discuss these items further, please contact Heather Jerbi, the Academy's senior health policy analyst (202.785.7869; [Jerbi@actuary.org](mailto:Jerbi@actuary.org)).

Sincerely,

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