

**ENGROSSED HOUSE BILL NO. 1087 TESTIMONY**

**Presented by:**        **Jon Godfread**  
                              **Insurance Commissioner**  
                              **North Dakota Insurance Department**

**Before:**                **Industry Business and Labor Committee**  
                              **Senator Jerry Klein, Chairman**

**Date:**                 **March 3<sup>rd</sup>, 2021**

Good Afternoon Chairman Klein and members of the Senate IBL committee. I am Jon Godfread, North Dakota Insurance Commissioner.

Engrossed House Bill 1087 is seeking to reauthorize North Dakota's Reinsurance program. This program was established last session and created an invisible reinsurance program for North Dakota's individual health insurance marketplace. The approach of invisible reinsurance allows enrollees to remain in the individual market with their current plan and carrier, while a portion of their claims are reimbursed by the reinsurance pool. The enrollee is not aware that their claim is being paid by the reinsurance pool meaning there is no effect on the enrollee as the task of ceding claims to the reinsurance pool is completed on the back end of the process and is without consequence to the enrollee. Last session, the 66<sup>th</sup> Legislative Assembly approved this program for plan

years 2020 and 2021. This program was approved with overwhelming support, with only one legislator voting against this program. At the time, the Legislature put a sunset on the program, effectively ending the program at the end of 2021. Engrossed House Bill 1087 seeks to remove that sunset and continue this program into the plan years for 2022, 2023 and beyond.

As a reminder, for plan years 2020 and 2021, the reinsurance program will cover 75% of claims between \$100,000 and \$1,000,000. The enrollee's health insurer will cover the remaining 25%. We have realized **rate reductions from this program of 20%** for the individual market for the 2020 plan year. This resulted in approximately \$43M of savings to North Dakota consumers.

Due to the events surrounding 2020 and the lack of utilization, we have been able to also keep rates even (still reflecting those 20% reductions) for individual health insurance plans in 2021. These reductions have been especially helpful for North Dakota's farmers, ranchers, and small business owners as these individuals generally cannot access small and large group health insurance markets and are therefore required to purchase their health insurance on the much more costly individual market.

When we established program, we worked with an actuarial firm, NovaRest, who estimated the reinsurance program's cost. NovaRest

estimated the federal government will be funding more than half of the amount with the money this reinsurance program will save the federal government. This money is known as “federal pass through” money. The federal government made the formulas they use to calculate the federal funding amount available to the public, and NovaRest used these formulas in calculating the cost. Typically, we get our preliminary federal pass through estimate in January with the official number coming in April. I am happy to report that as of last week, we were informed by the federal government that our federal pass through dollars for 2021 are projected at \$14,683,761.

In 2020, we received \$21,488,350 of federal pass through dollars and we assessed the carriers a total of \$21,988,170 from July 1, 2019 through June 30, 2020. We have since paused the assessments on the carriers, a point I will cover in more detail in a moment.

For 2021, we are projecting the pass-through funding from the Federal Government to be \$14,683,761, and the projected claims for 2021 to be approximately \$26,000,000. Meaning the state share of the reinsurance program for 2021 is estimated at \$11,316,239. With these projections along with the reduced claims we saw in 2020 we have paused the assessments and are currently projecting with our current reserves in the RAND program that we will not need to assess our carriers for 2021.

After consultation with the CMS and the Federal Government as well as our contracted actuary, we have determined that the numbers that were projected for RAND were inaccurate. Some of this was a result of a new federal formula which has now been shared with the states, some of this is due to COVID, but the bulk of it is due to now having experience in this area and a better of understanding of the program. Essentially our projections were too high. An example, for 2021, our original projections for the full cost of the program was \$50M, approximately \$25M from federal pass through and \$25M from state funds. Given our new projections, the cost of the program is \$26M, \$14.7M from the federal pass through and \$11.3M from state funds.

Our projections were high as we did not want to risk underfunding a new program, but this illustrates the difficulties in projecting the costs going forward into the 2022 and 2023 plan years. We are continuing to work on the fiscal note to this bill, as currently it dramatically overstates our actual experience with the reinsurance program in 2020.

As you may remember in order to raise the state share of the program funding we assess the insurance companies doing business in our state and they in turn are allowed to deduct the amount of money they are assessed from the premium taxes they owe to the state, which will result in future reduced revenues for the state. To date the carriers have taken

\$16,976,918 in premium tax credits of the total \$21,988,170 that was assessed during the '19-'21 biennium.

The fiscal note reflects the reduction in premium tax revenue due to the ability of the carriers to take a tax credit on any assessments to fund RAND, the expenditure of \$21,500,000 (which should now be changed to \$14,683,761) covers the federal pass dollars through received under the waiver, and an appropriation of \$200,000 out of the funds already in RAND to cover the cost of a study regarding private reinsurance.

For the 2021 plan year we do not anticipate the need to conduct assessments. This is a result of the 2020 plan year, and the reduced utilization we saw. Our actual numbers for 2020 are still pending, but the number of claims actually ceded to the reinsurance program were well below our projections. Based on the preliminary claims numbers we have received to date from our carriers, the 2020 federal pass through dollars we received will likely cover the entire amount due for the 2020 plan year leaving RAND with a reserve balance of approximately \$22,000,000. Given that reserve balance along with the additional federal pass through dollars we anticipate receiving in 2021, we are confident we can pause the assessments to our carriers through 2021. This would reduce our assessments for both this current biennium and the '21-'23 biennium. The fiscal note currently attached to this bill is an

overestimated worst-case scenario. We have prepared a new fiscal note which accounts for the expected reduction in reinsurance payable in 2021. This new note shows an estimated reduction in general fund dollars of \$17,547,170 in the '21-'23 biennium and \$27,346,309 for the '23-'25 biennium, but in the end the estimates for the next biennium will be just that, an estimate. The increase for the '23-'25 biennium is due to the state's fiscal year starting on July 1 while the plan year for a health insurance policy typically begins on January 1.

House Bill 1087 as proposed also asks for some changes I would like to point out:

1. Section 3 of the bill on page 8, lines 13 -15, requests the authority to develop an amendment to our existing 1332 waiver. I will cover that in more detail later, but this is where we would ask for the authority to go back and amend our existing waiver.
2. Section 7 of the bill on page 11, lines 3-4; would clarify that an insurer writing less than \$100,000 annually in group health benefits plan premiums is exempt from assessments. This amount is modeled after CHAND as assessing carriers that write less than \$100,000 creates unnecessary additional work for both the Department and the carrier do the immateriality of the assessment.

3. Section 12 of the bill, on page 13 lines 16-19 would provide authorization for the Reinsurance Association of North Dakota to use the federal pass through dollars to procure third party reinsurance for the associations portion of eligible claims. We conducted an analysis of procuring third party reinsurance as a part of our larger health care cost study.

#### Third Party Reinsurance Program:

To supplement the cost-saving efforts of the 1332 waiver program, we have proposed evaluating purchasing private reinsurance to further reduce costs for individual taxpayers participating in the State's healthcare marketplace. Private reinsurance can assist in driving down/stabilizing rates and preventing spikes while providing consistency for taxpayers/users. For example, Aon, a private reinsurer, has proposed such a system, which is shown in Appendix A.

Using reinsurance to transfer the budgetary/program volatility, creates immediate opportunities for the State of North Dakota including:

- Transferring volatility away from the existing RAND program into the private market
- Reducing the future "known, unknowns", thereby allowing greater funding flexibility with the safety and security of knowing that protection is in place in the event of a higher-than-normal claims year

- Providing stability in rates from payers as a pre-arranged amount of funding is known
- Predictable cash flows for insurers and the state as there is no need, once coverage is purchased, to adjust the reimbursement levels to carriers based on higher-than-expected claim numbers and amounts
- Adjudication and claims processing is handled by the reinsurer, removing some of the operations of running the program in house

In addition, given the current Covid-19 health crisis there is likely to be further pressure on the individual health market. According to a recent Kaiser Family Foundation report, “It is likely that the most significant impacts of the coronavirus outbreak and economic crisis on the individual market will not be evident nationally until data from the second and third quarters of 2020 become available.” These solutions can help mitigate impacts stemming from the global pandemic. I have attached more information to my testimony going through the analysis we have completed on this program.

4. Section 13 of the bill, on page 13, lines 22 – 26 is a continuing appropriation, which was added by the House, related to the federal pass through funding received under our 1332 waiver. During 2020 an oversight was discovered regarding the ability to spend said federal pass through funding. This oversight was not noted during the



legislative process or by OMB. This resulted in the Department seeking approval from the Emergency Commission in order to spend the 2020 federal pass through funding. This was approved unanimously by the Emergency Commission at its June 30, 2020 meeting.

Section 13 of this bill seeks to make any federal funding received under our approved 1332 waiver a continuing appropriation. We are asking for this continuing appropriation for a few reasons. First, the amount of federal funding received is not static. It can and will change every year based on the number of individuals insured in the individual market. As this number changes each year, we are unable to ask for a known number and in the case of requesting less than gets awarded it would necessitate the Department having to go to the Emergency Commission potentially on a yearly basis.

Second, if our request comes in higher than awarded our budget is therefore inflated. These dollars are truly a pass through and can only be used to administer RAND. Any federal dollars not spent are rolled over to the next calendar year. We believe having this continuing appropriation is reasonable and will help cut down on administrative burdens to both this body and the Department.

5. Section 14 of the bill, on page 13 lines 25-31, we are asking for \$200,000 of the RAND reserves to study the possibility of combining the individual health insurance marketplace with the small group health insurance marketplace. We believe there may be value in combining those markets for North Dakota, and in doing so, our small group market would be able to receive the benefits of the reinsurance program, which should reduce rates for our small employers who purchase coverage through the small group market.

One final point, I have also included a document that outlines the discussion we had with the House Appropriations committee and does a nice job of summarizing, where the money is going, where it has gone, and how we got here.

As you can see this program has been successful, it has had a significant impact on North Dakotans who purchase their health insurance through the individual marketplace, and with the changes we are proposing, we believe we can continue this program and expand the benefits to the small group marketplace.

For these reasons, I would encourage a favorable recommendation for House Bill 1087, and I am happy to attempt to answer any questions you may have.

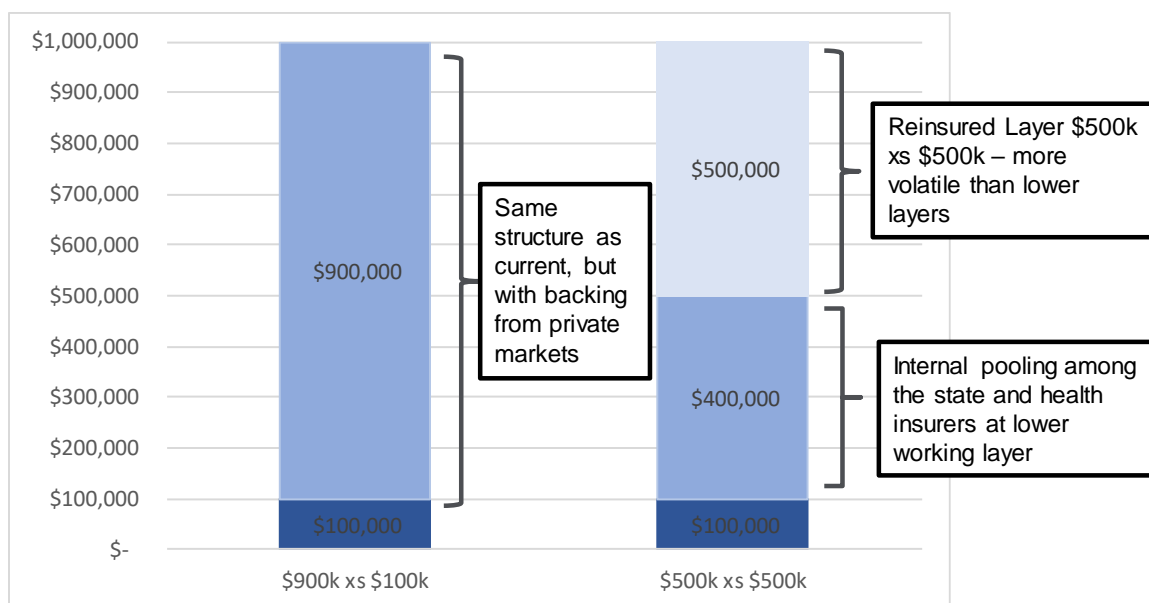
### Third-Party Reinsurance – Appendix A:

In conjunction with our health care cost study, we also looked at potential solutions around layering of a private third-party reinsurance program for our existing reinsurance program. HB 1087 would authorize us to further develop and study this idea and with positive results implement the program.

When considering the existing Reinsurance Association of North Dakota (RAND) program, there are two main structural options to consider.

#### Excess of Loss

- Provides recoveries after a pre-determined amount of loss
- Smooths results in excess of pre-determined attachment point



## Aggregate Stop Loss

- Provides recoveries after a pre-determined amount of loss in a defined/determined time period
- Coverage ensures the aggregation of numerous claims do not drain the financial reserves of the risk-bearer/entity



### **How much would this cost?**

*We modeled various scenarios using stochastic and deterministic models, we also used market data to derive pricing.*

Using available data collected for the initial 1332 Waiver Process to illustrate a few structural and pricing options that would make sense given the current RAND structure. In evaluating solutions for North Dakota our overarching motivation is to maximize coverage, deliver fast payment, and provide clear benefit to the users of the RAND program.

Projected claims costs were derived from North Dakota's 2017 year. In order to secure pricing from the reinsurance markets, typically 3-5 years of data is required, however we believe this 12-month snapshot provides enough information to draw preliminary conclusions.

Pricing is provided on a 100% experience basis and blended with national market data to provide more credibility to the block of business. It is illustrated on a per member per month basis.

Our analysis is based on following general market underwriting methodologies used across the reinsurance industry to develop a likely premium. Since North Dakota would be transferring the volatility to the market, the amount of money allocated to reinsurance claims in one particular year does not have to be as conservative as what may be traditionally allocated to a self-funded plan. Because RAND is a newly formed self-insured reinsurance program, it is not surprising that additional conservatism was included in the preliminary (NovaRest) actuarial analysis.

#### Claims Projections:

	75% Coinsurance	
Source	\$900k xs \$100k	\$500k xs \$500k
Nova Rest	\$106.68	
Market	\$67.27	\$8.18
Aon - Deterministic	\$58.53	\$4.38
Aon - Stochastic	\$58.82	\$4.65

#### Pricing Options:

*XOL Pricing by layer	Premium
1. \$900k xs \$100k	\$70.58
2. \$500k xs \$500k	\$5.58
*Agg Pricing	
1. 110% of expected	\$27.64
2. 120% of expected	\$20.61
3. 130% of expected	\$14.58

#### Key Takeaways:

- Based on the 2017 claims year costs there are indications that meaningful cost savings can be achieved by a private reinsurance purchase
- Claims costs can be shifted to the private market for less dollars than they are being funded for in the existing program, leaving additional funding to further stabilize rates and pay for the private purchase

- We can transfer claims to the private market for .65-.85 cents on the dollar (this is based on only one claims year and we would need 3-5 years to fully validate this with third party capital)
- The structures presented would provide more program certainty to payers allowing for greater flexibility in rate pricing
- While the premium payments for the State of North Dakota may be higher than the claims cost in some years, high claims years will counterbalance the years where the state ends in a negative net position
- As an example, 1 in 20 years the reinsurer is projected to lose \$20.57 per member per month, paying \$1.30 to the state for every \$1 the state pays in premium

<b>Return Period (1 in X years)</b>	<b>Losses (PMPM)</b>	<b>Reinsurer Position (PMPM)</b>
Average	\$58.82	\$11.76
5	\$72.34	-\$1.76
20	\$91.14	-\$20.57
40	\$99.22	-\$28.64

Considerations for Next Steps:

In order to procure formal pricing from the market, additional information is needed.

<b>Reinsurance Parameters</b>	<b>Key Considerations</b>
Data Required (last 3-5 years)	<ul style="list-style-type: none"> <li>- Membership Data</li> <li>- Claims Triangles</li> <li>- Large Claim Loss Data</li> <li>- Plan Design Changes (Historical and Proposed)</li> </ul>
Attachment Point	<ul style="list-style-type: none"> <li>- Attachment points can allow for any corridor, both overlapping what is being offered or just covering a piece</li> <li>- To reduce total cost coinsurance can be included which will reduce the reimbursement by a percentage for each claim</li> </ul>
How Much “Limit” to Purchase	<ul style="list-style-type: none"> <li>- Often relatively small incremental premium to purchase higher limit</li> <li>- Markets will cap the limit they offer based on their risk tolerance</li> </ul>
Contractual Considerations	<ul style="list-style-type: none"> <li>- If the State of North Dakota does not cede the entire \$900k xs \$100k layer to the reinsurance market, arrangements will be needed to administer the pooling layer</li> <li>- Additional analysis will be required to confidently opine on the contractual structure between the State of North Dakota reinsurance program and the reinsurers</li> </ul>

### **Who would provide this backstop?**

*Reinsurance companies are the providers of this protection and have been active participants in the health market for several years.*

There is a significant market appetite for health exposure. There are several highly rated counterparties that will be interested in an excess of loss or aggregate structure as these are the main vehicles used to transfer volatility in the space.

While the amount of data available is limited there are indications that meaningful cost savings can be achieved by RAND purchasing third-party reinsurance from the private market. As with any reinsurance contract there are years when the cost of the third-party reinsurance contract may be higher than the claims costs, however, high claims costs years will counter-balance this. By shifting claims costs from RAND to the private market this will potentially lead to a reduction in RAND funding needs from the state while providing stability to the health insurance market in North Dakota.

Reinsurance is used globally by insurers both large and small. As noted above, reinsurance can provide stability and consistency to the ceding entity by smoothing out the peaks and valleys that can and inevitably do occur. The health insurance world is not immune from these peaks and valleys as we have seen during 2020 and RAND has helped. By exploring the option of third-party reinsurance RAND too can take advantage of this stability and consistency in its results.