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TO THE HOUSE COMMITTEE ON FINANCE

TWENTY-FOURTH LEGISLATURE
Regular Session of 2008

Monday, February 25, 2008
1:45 p.m.

TESTIMONY ON HOUSE BILL NO. 2256 HD 1 – RELATING TO INSURANCE

TO THE HONORABLE MARCUS C. OSHIRO, CHAIR, AND MEMBERS OF THE COMMITTEE:

My name is J.P. Schmidt, State Insurance Commissioner ("Commissioner"), testifying on behalf of the Department of Commerce and Consumer Affairs ("Department"). The Department opposes H. B. 2256, HD 1 which would weaken the anti-bundling provisions of the Insurance Code.

Under Hawaii Revised Statutes section 431:13-103(a)(4)(B), part of the unfair methods of competition and unfair and deceptive acts and practices in the business of insurance statute, insurance companies are prohibited from making the purchase of one class of insurance contingent upon the purchase of another class of insurance. This is known as the "anti-bundling" provision and is designed to protect consumers from an insurer who would seek to force consumers to purchase multiple types of insurance in order to buy a policy that they want to buy. The rule does not prohibit an insurer from offering different classes of insurance together in an attractively priced package. There is no violation if the consumer has the option of taking the package or just taking the insurance wanted. The law only prohibits an insurer from refusing to sell one policy unless another policy or other policies are also purchased.

In other words, under current law a health insurer could pair a life insurance policy with a health insurance policy and offer the package to consumers who are free to accept or reject the life insurance. The insurer can not demand that the consumer buy the life policy in order to get the health policy.

H. B. 2256, HD 1 would allow insurers with less than a 5% market share to require customers to purchase a bundle of insurance products as a condition of sale. The Insurance Division is aware of only one insurer engaging in this practice presently and that is the health insurer Hawaii Management Alliance Association ("HMAA"). Presently, HMAA requires sole proprietors to puchase not only health insurance related coverages such as vision and dental insurance, but also life insurance. The Insurance Division is moving to halt this practice. This bill seeks to reverse the Division's action.

Although this bill only applies to insurers with less than 5% market share, the issue is not market share, the issue is what the U.S. Supreme Court in *Jefferson Parish Hosp. Dist. No. 2 v. Hyde* called "market power", or "leverage".

In footnote 20, the court noted:

> FN20. .... "'Leverage' is loosely defined here as a supplier's ability to induce his customer for one product to buy a second product from him that would not otherwise be purchased solely on the merit of that second product." V P. Areeda & D. Turner, Antitrust Law ¶ 1134a at 202 (1980).
>
> *Jefferson Parish Hosp. Dist. No. 2 v. Hyde,* 466 U.S. 2, 14, 104 S.Ct. 1551, 1559 (U.S.La.,1984)

HMAA has that "leverage" – although it has a small share of the "accident and sickness insurance market", HMAA presently is essentially the only health insurer who offers group policies to sole proprietors.

HMAA portrays its practice of requiring the purchase of one, possibly undesired insurance product in order to purchase another desired insurance product as a customer benefit or a social good. The company characterizes the observation that this conduct is illegal as irrational, unfair and misleading. We are happy to submit that matter to the committee on the basis of the Attorney General's testimony, which

confirms that the practice is illegal. According to HMAA, the Department's concern over HMAA's practice of bundling products departs from 18 years of "practice and judicial precedent." In response we note first that in enforcing the law it is totally meaningless that HMAA has been violating the law for 18 years – that is no justification for being allowed to continue an unlawful practice. Second, the Insurance Division did not have a health branch 18 years ago or even 10 years ago and the reason that this matter was raised in 2006 and not sooner was that we received a complaint at that time from an HMAA member who objected to being forced to buy life and dental coverage from HMAA in order to purchase a health plan. During our investigation we discovered that 30 to 40% of prospective HMAA members objected to being forced to buy insurance coverage they didn't want. If any of those consumers had come to the Insurance Division earlier we would have moved to stop this practice earlier.

Contrary to HMAA's assertion, allowing this practice does not mean lower premiums for the consumer. In HMAA's case for example, HMAA got approximately $36,000 in "profit sharing" from the company issuing the life insurance policy that HMAA members were required to buy but, more significantly, an affiliated company of HMAA, AB & Associates, received $855,014 in commissions on the sale of this life insurance policy from 2001 to early 2006. AB & Associates is a for-profit company owned by the individuals who were officers of HMAA. This commission for placement of the life insurance did not benefit the consumer, did not benefit HMAA, and did not benefit HMAA's members. AB & Associates' commission in this transaction was 25% of the total premium, in other words, every year 25% of the premium that HMAA members pay for life insurance that they had no choice in purchasing goes to an HMAA for-profit affiliated company. This is an example of what can and does happen if bundling is allowed.

The anti-bundling rules are there to protect consumers; it would be bad policy to allow so called "small insurers" to use their market power to force consumers to take insurance they don't want or need. As noted above, evidence was presented that 30-

40% of HMAA's members objected to being required to buy insurance that they didn't want and requested to buy coverages separately.

This bill is being presented as beneficial to small business. Small business would truly benefit by amending the definition of "small employer" in HRS §431:2-201.5 to include sole proprietor and thus clarifying that sole proprietors are entitled to group health insurance.. That way they will get the same protections under our HIPAA conformity statute enjoyed by other small employers. We support the language in Senate Bill 2530 Relating to Health Insurance Help for Small Business which takes this approach.

We thank this Committee for this opportunity to testify and ask that this bill be held.

HMSA
Blue Cross
Blue Shield
of Hawaii

An Independent Licensee of the Blue Cross and Blue Shield Association

February 25, 2008

The Honorable Marcus Oshiro, Chair
The Honorable Marilyn Lee, Vice Chair
House Committee on Finance

Re: HB 2256 HD1 – Relating to Insurance

Dear Chair Oshiro, Vice Chair Lee and Members of the Committee:

The Hawaii Medical Service Association (HMSA) appreciates the opportunity to testify on HB 2256 HD1 which would exempt small health plans that occupy less than five per cent of the health care market from adhering to a portion of the Insurance Code dealing with unfair methods of competition and unfair or deceptive acts or practices. HMSA opposes this measure in its current form.

Unfortunately, the current language of this measure would allow health plans with less than a five percent share of the local market to engage in an activity that would be prohibited for many of the health plans in the state, including HMSA. We believe that this would create an unlevel playing field.

If it is the Committee's will to move this measure forward we would request a small amendment to narrow the definition in scope so as to only apply to specific products offered by a health plan. This would be accomplished by removing language which refers to a plan's market share so that Page 6, Lines 17 – 20 read as follows:

provided that this subparagraph shall not apply to any insurer subject to chapter 432 offering contracts for dental and vision insurance as a condition, agreement, or understanding to the new health insurance policy or renewal of a health insurance policy for those policies offered to an individual or sole proprietor under chapter 432;

This would ensure that this measure accomplishes its intended goal without affecting other plan offerings in the State. Thank you for the opportunity to testify on HB 2256 HD1.

Sincerely,

Jennifer Diesman
Director, Government Relations

HMAA
HAWAII MEDICAL ASSURANCE ASSOCIATION

BEFORE THE

HOUSE COMMITTEE ON FINANCE
Representative Marcus R. Oshiro, Chair
Representative Marilyn B. Lee, Vice Chair

HB 2256, HD 1 RELATING TO INSURANCE

TESTIMONY OF
JOHN HENRY FELIX
Chairman of the Board and Chief Executive Officer

February 25, 2008, 1:45 pm
State Capitol Conference Room 308

Chair Oshiro, Vice Chair Lee, and Committee Members:

My name is John Henry Felix, Chairman of the Board and Chief Executive Officer of Hawaii Medical Assurance Association (HMAA). HMAA **STRONGLY SUPPORTS** HB 2256, HD 1, which would enable small insurers that occupy less than five percent of the health insurance market to continue combining different types of health and sickness-related insurance benefits into a single unified policy. **HB 2256, HD 1 has been amended to limit its application to health insurers only, as reflected in the addition of the applicable statutory language "accident and health or sickness" insurers.**

I. Background to HMAA and the Need for this Bill

By way of background, HMAA is a non-profit mutual benefit society which provides health insurance to over 30,000 Hawaii residents. HMAA occupies about three percent of Hawaii's health insurance market. As a small insurer, HMAA takes special pride in providing health insurance to sole-proprietors and small businesses, a segment of Hawaii's market which has a difficult time obtaining affordable health related insurance.

HB 2256, HD 1 is intended to help self-employed workers and small businesses by continuing to allow broader coverage for less cost. This bill is necessary because the current administration has recently chosen to interpret Hawaii law in a different way than it has ever been interpreted by prior administrations, to prohibit the combination of drug and medical coverage, or the combination of medical, dental and drug coverage, or any other combination of health related coverages, into one insurance policy. Numerous Hawaii laws already permit the combination of various types of health

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coverages under one policy, and this should be encouraged, not discouraged, to help provide the broadest health coverage possible for Hawaii's residents.

II. The Insurance Commissioner's Departure from Practice and Judicial Precedent

Since its inception in 1989, HMAA's medical plans have always included life insurance, and its sole proprietor/independent contractor plans have always included medical, dental, vision, and prescription drug coverage.

Although prior Insurance Commissioners have accepted HMAA's practice for the last 18 years, the current administration has departed from those years of acceptance and deemed these combined benefits as a violation of state anti-tying laws. This administration is doing so even though the U.S. Supreme Court has made clear that a company with less than 30% market share has no coercive power in the marketplace and cannot violate federal anti-tying laws. *Jefferson Parish Hospital v. Hyde*, 466 U.S. 2 (1984). Consistent with the federal standard, HB 2256, HD 1 will encourage the existing practice by smaller accident and sickness insurers to "bundle" together different classes of insurance, such as health, dental, and vision, thereby continuing the State's historical acceptance of this practice by small insurers who lack coercive power in the marketplace. In these circumstances, bundling provides broader health care coverage in single unified policies, ultimately resulting in lower overall premiums, fostering greater competition within the Hawaii insurance marketplace, and providing consumers with greater flexibility, coverage and pricing options.

HB 2256, HD 1 codifies into Hawaii law the same rules applicable to similar federal anti-tying laws, though using a more conservative standard of 5% market share. HB 2256, HD 1 does not change the Prepaid Health Care Act in any way, but rather simply provides that HMAA's 18 year practice of providing broad, cost- effective benefits to Hawaii's smallest business groups is not an unfair insurance practice. Without passage of HB 2256, HD 1 hundreds of sole-proprietors, small businesses, and their families currently insured by HMAA could be forced to shop for more expensive individual policies with much less coverage.

III. Misleading Testimony Provided to Date

This bill, and its companion SB 2314, SD1 have come under irrational, unfair and at times outright false criticism to which I must respond so that this Committee may have the benefit of an accurate record.

A. False Testimony Regarding HMAA's Market Power

In prior testimony with respect to both bills, the Insurance Commissioner has repeatedly attempted to confuse the issue by claiming that HMAA has nearly one hundred percent (100%) of the "market" for accident and sickness insurance policies issued to sole proprietorships. *See e.g.,* Testimony of Insurance Commissioner dated February 14, 2008 re: H.B. No. 2256, H.D.1, at p. 2, and that HMAA therefore has "market power" even though HMAA has less than five percent (5%) of the market for accident and sickness insurance policies generally.

However, the Insurance Commissioner admits that "[o]ther insurers could sell group insurance to sole proprietors but they are not required to do so by law . . . so they don't." *Id.*, at p. 3. Plainly, if other insurers are free to sell group insurance to sole proprietors, HMAA cannot have any market power because if HMAA raises its premiums above competitive levels, other insurers would be free to start selling policies to sole proprietors. Thus, the Insurance Commissioner's claim that, on the one hand, HMAA has market power *vis a vis* sole proprietors, but, on the other hand, other insurers can sell group policies to sole proprietors, is contradictory and illogical.

In fact, HMAA does not control a majority of the sole proprietor / independent contractor market. HMAA currently covers 932 of these individuals. The annualized gross premium is currently $5.4 million out of HMAA's 2007 actual gross premium of $96 million. The premium is not significant, but the benefit to the sole proprietor/independent contractor is. *If HMAA were to cease offering this plan, the loss of premium would be equivalent to HMSA losing a single large group.*

The Attorney General's own testimony of February 14, 2008 stated "The sole proprietor market in Hawaii is not insignificant. According to the latest U.S. Census Bureau report (2004), 16,503 out of 31,605 Hawaii business, or 52%, have one to four employees." (emphasis added). *This would suggest that HMSA's Individual Business Plan, and not HMAA's plan that covers only 932 individuals, has the market share.*

Given the foregoing, and in light of the Insurance Commissioner's necessary concession that "[o]ther insurers could sell group insurance to sole proprietors," the attempt to impute market power to HMAA even though HMAA has less than a five percent (5%) market share must be rejected. Other insurers can sell group insurance to sole proprietors. If HMAA or another insurer offers bundled products that consumers do not want, other insurers can step in to offer products to satisfy that demand. This is how competitive markets work. If anything, the Insurance Commissioner's anti-bundling rules are anti-competitive because they prevent the development of bundled products in a competitive market by insurers who lack coercive market power.

B. False Testimony Regarding the Practice of Bundling

Also in prior testimony, the Insurance Commissioner asserted that HMAA is the only health insurer which bundles, stating "H.B. 2256 would allow insurers with less than a 5% market share to force consumers to purchase a bundle of insurance products as a condition of sale. The Insurance Division is aware of only one insurer engaging in this practice presently and that is the health insurer ....HMAA".

This statement is not true. HMSA's "Individual Business Plan" has been available to sole proprietors and independent contractors for the last decade. It, too, combines medical, drug, vision, dental, and life insurance in one plan. However, HMSA and other insurers elect to treat the sole proprietor and independent contractors as individuals for insurance purposes, and not as 'groups' protected by the Hawaii Prepaid Health Care Act.

This election by other insurers reduces benefits and imposes additional eligibility rules to the detriment of sole proprietors and independent contractors, including the ability to deny coverage and a 12-month waiting period before benefits begin for certain conditions, such as:

Aids and HIV	Reflux Disease
Alzheimer's Disease	Hearing Loss
ALS	Heart, blood, and blood vessel diseases
Anemia for congenital or hereditary blood disorders	Hepatitis other than Hepatitis A
Arthritis	High blood pressure
Asthma	Multiple sclerosis
Cancer	Osteoporosis
Cataracts	Pelvic inflammatory disease
Cerebral Palsy	Radiculopathy
Cirrhosis of the liver	Reconstructive surgery for a previous illness or injury
Chronic Obstructive Pulmonary Disease	Sleep Apnea
Cohn's Disease	Spinal disk problems
Diabetes	Surgery and services related to hemorrhoids, hernia, tonsils, adenoids, and varicose veins
Diverticulitis	Thyroid conditions
Dysfunctional uterine bleeding	Tuberculosis
Endometriosis	Ulcers
Fibromyalgia	Urinary Incontinence
Gall Bladders disease and gallstones	Transplants

HMAA protects the sole proprietors and independent contractors by electing to treat them as regular groups. This means that there is **no waiting period** before benefits begin. This has been HMAA's mission since its inception. It was formed specifically to give the 'little guy' as good or better benefits as so-called regular companies including the 'big guys'.

C. False Testimony Alleging Kick-Backs

In his prior testimony regarding both bills, the Insurance Commissioner has repeatedly alleged that HMAA "got a rebate, or "kick-back" if you will, from the life insurer of profits on the bundled life insurance." **This statement is an absolute falsehood.** HMAA's contract with Hartford Life insurance contains a *profit sharing* provision. This is *not* a rebate and *not* a 'kick-back'.

For policy year ended 1/31/02, HMAA received a profit sharing check in the amount of $34,909. This money went directly to the mutual benefit society, as recorded in HMAA's audited financial results. There have been no profit sharing payments since 2002.

HMAA's subscribers personally choose the beneficiary of their life insurance policy, whether it be a family member, child, grand child, or significant other. HMAA's life insurance benefits paid to consumers for policy years ending January 31 since 2002 have been:

$347,817
$419,208
$387,536
$467,358
$262,222
$540,000 for policy year ended January 31, 2007

for a total of $2.9 million.

These benefits have gone to families that in most cases had no other life insurance. It has made a substantial difference to the loved ones of HMAA subscribers. These benefits include all of payments to HMAA subscriber beneficiaries, and not just sole proprietors. Although the insurance division's testimony refers only to sole proprietors, it is on record as also opposing life insurance included in HMAA's medical plans for larger groups.

If the legislature eliminates this benefit for sole proprietors/independent contractors, the Division's likely next step is to also eliminate it for larger groups.

D. Misleading Testimony Regarding Benefits to Consumers

The Insurance Commissioner further claims that bundling will hurt the consumer because it will eliminate consumer choice and that any savings will be retained by HMAA. Specifically, in his prior testimony, the Commissioner represented that "[t]he Committee should understand that allowing this practice does not mean lower premiums for the insured."

This statement is also incorrect. HMAA's actuary, Thomas J Parciak, FSA, MAAA, of AON Consulting, has made the following analysis of the consequences of un-bundling:

> "For HMAA to unbundle their various product offerings, the premiums you would need to charge would increase from current levels, likely to a point of becoming prohibitively expense for this population.
>
> You would also need to seriously consider whether HMAA should continue to offer some of these products.... At all, as they have a very high likelihood of anti-selection [adverse selection] when offered separately.
>
> Finally, further fragmenting this already small population into coverage-specific groups would potentially jeopardize the credibility of the various groups for pricing purposes, making it very difficult for HMAA to effective price any of the coverages. This puts the viability of these Small Business Plan offerings into question."

This information was provided to the Insurance Division in 2006. And, the Commissioner knows that his position, if unchanged, will also require health plans to incur additional costs - that will be passed on to consumers - for administering numerous different policies instead of a unified policy. His actions will deprive Hawaii's businesses and employees low cost, broad coverage health policies, and will destroy cost efficiencies and lower prices that can result from combining broad health coverage within the same insurance policy.

E. Bundling of Life Insurance is Mandated by Current Law

For groups of two or more, HMAA's plan includes life insurance and accidental death and dismemberment benefits. The Division's insistence that these benefits be "unbundled" is contrary to existing Hawaii law, which requires mutual benefit societies to bundle life insurance if they choose to offer it:

431:10D-208. Mutual benefit society groups.

The lives of a group of individuals may be insured under a policy issued to a mutual benefit society, which shall be deemed the policyholder, to insure members of the society for the benefit of persons other than the society or any of its officials, subject to the following requirements:

. . .

(3) . . . a policy on which no part of the premium is to be derived from funds contributed by the insured members specifically for their insurance **must insure all eligible members**; [1]

. . .

(7) The amounts of insurance under the policy must be based upon some plan **precluding individual selection either by the members or by the society**.

See Haw. Rev. Stat. § 431:10D-208 (emphasis added). Plainly, the only reasonable interpretation of the statutory mandate that the insurer "must insure all eligible members" and must "offer the insurance in such a manner so as to "preclude[] individual selection either by the members or by the society" is to require that it be uniformly provided to all members, just as HMAA has been doing for years. The Division's position is squarely at odds with section 431:10D-208, and should be rejected accordingly.

Thank you for the opportunity to correct the record, and to testify on this matter of critical importance. HMAA **STRONGLY SUPPORTS** HB 2256, HD 1 and urges the passage of this measure.

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[1] HMAA pays for the life insurance from its reserves, not member premiums.

HOUSE COMMITTEE ON FINANCE

February 25, 2008

HB 2256, HD 1 Relating to Insurance

Chair Oshiro and members of the House Committee on Finance, I am Rick Tsujimura, representing State Farm Insurance Companies, a mutual company owned by its policyholders. State Farm has comments regarding House Bill 2256, HD 1 Relating to Insurance.

House Bill 2256, HD 1 Relating to Insurance is a companion measure to Senate Bill 2314, SD 1 Relating to Insurance. State Farm prefers the language that appears in the Senate companion bill and requests replacing the amendment on page 6 of House Bill 2256, HD 1 with the language that appears in Senate Bill 2314, SD 1 as follows:

> (B) Entering into any agreement on the condition, agreement, or understanding that a policy will not be issued or renewed unless the prospective insured contracts for another class or an additional policy of the same class of insurance with the same insurer; provided that this subparagraph shall not apply to any insurer subject to chapter 432 with less than five per cent of the health insurance market share offering contracts for dental and vision insurance as a condition, agreement, or understanding to the new health insurance policy or renewal of a health insurance policy under chapter 432;

Thank you for the opportunity to present this testimony.