



LEGISLATIVE BRIEF

Health Care Reform: Final Regulations Issued On Medical Loss Ratio

On Dec. 2, 2011, the Department of Health and Human Services (HHS) announced final regulations on the medical loss ratio (MLR) requirements under the health care reform law. The MLR requirements became effective on **Jan. 1, 2011**. They require health insurance issuers to spend **80 to 85 percent** of premium dollars on medical care and health care quality improvement, rather than administrative costs.

In December 2010, HHS issued interim final regulations on the MLR requirements, which became effective on Jan. 1, 2011. The final MLR regulations issued by HHS on Dec. 2, 2011, leave the 2010 regulations largely intact, but make some technical changes to how the MLR is calculated and how rebates are distributed. The final regulations become effective on **Jan. 1, 2012**.

This Legislative Brief summarizes the technical changes made by the final MLR regulations.

MLR CALCULATION

An issuer must calculate its MLR as a fraction. The numerator of the fraction is the amount of incurred claims paid plus expenses for health care quality improvement activities. The denominator is the premium revenue, minus federal or state taxes and licensing and regulatory fees.

The final regulations provide the following guidance on calculating the MLR:

- ICD-10 conversion costs up to 0.3 percent of an issuer's earned premium in the relevant state market may be considered health care quality improvement activities for each of the 2012 and 2013 reporting years. (The ICD-10 conversion involves updating medical code sets to comply with HIPAA's transaction standards for electronic health claims.)
- Issuers may deduct from earned premiums the higher of either the amount paid in state premium tax or actual community benefit expenditures up to the highest premium tax rate in the state.
- Adjustment factors may be used to calculate the MLR for expatriate plans and mini-med plans to take into account the higher administrative costs associated with these plans and to ensure that consumers do not lose coverage.

The final regulations do *not* reclassify how agent and broker commissions are treated when calculating the MLR. The final rules leave agent and broker commissions as an administrative expense that cannot be taken into account when calculating the MLR fraction.

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REBATES

Issuers that do not satisfy the MLR requirement must issue rebates to consumers starting in August 2012. The final regulations streamline the rebate requirements by generally requiring issuers to provide rebates to the group policyholder. Policyholders must use the rebates for the benefit of enrollees.

Rather than paying the rebates directly to enrollees, the final regulations permit policyholders to use the rebates to reduce the employee portion of the health plan premium. This method allows enrollees to have the benefit of the rebates without having to pay tax on the rebate amount. The final regulations also note that policyholders of ERISA plans will need to consider their fiduciary duties to plan participants when deciding how to use the rebates.

When issuers provide rebates, they must also provide a notice of the rebate to enrollees. The notice must provide information about the MLR and its purpose, the MLR standard, the issuer's MLR and the rebate provided. The final regulations request comments on whether issuers should provide information to enrollees on their MLR, even if they are not required to provide a rebate, and whether the notice should include information about the issuer's MLR for the prior year for comparison purposes.

MORE INFORMATION

More information on the MLR requirements, including the interim final regulations and final regulations, is available on HHS's website at: <http://cciio.cms.gov/programs/marketreforms/mlr/index.html>.

This Legislative Brief is not intended to be exhaustive nor should any discussion or opinions be construed as legal advice. Readers should contact legal counsel for legal advice.