Sage Policy Group, Inc.

20,000 Direct Jobs in Maryland: The Economic Impact of Maryland's Health Insurance Brokerage/Underwriting Industry

Submitted by:

Sage Policy Group, Inc.

On behalf of:

The Health Insurance Buyers and Brokers Coalition of Maryland

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Executive Summary

Introduction

The enactment of federal healthcare reform legislation in March 2010 defines a series of actions that will presumably be implemented through 2014, although final adjustments will not take effect until 2018. These actions range widely from preventing insurance companies from dropping coverage for individuals who become sick to increasing Medicare compensation for primary care physicians.

The most fundamental actions created with the passage of this legislation relate to the expansion of health insurance coverage for the uninsured. By 2014 almost all Americans will have to obtain health insurance or pay a fine if they choose not to do so. In order to facilitate the enrollment of the uninsured, states are required to open health insurance exchanges by 2014. These exchanges are subject to regulation by the states, which have wide latitude in their design in their implementation of the health insurance exchange requirement.

Critically, one of the issues regarding formation and implication of these state-based exchanges is the extent to which they will take advantage of the capacity that current exists among a network of typically small businesses that support the insurance market by educating purchasers of health insurance products and providing support and advocacy to covered individuals and employees in the claims process and benefits administration. Maryland's health underwriters have played a critical role in the state's health insurance industry to date and this role is likely to become even more prominent during this period of healthcare reform and adjustment unless the State adopts public policy that effectively ignores this pre-existing capacity.

From an economic perspective, the health brokerage/underwriting industry directly accounts for between 20,000 and 23,000 jobs in Maryland and supports approximately 1.2 additional jobs for every direct job. Therefore, when multiplier effects are properly considered, health brokerage/underwriting supports at least 44,000 jobs in Maryland and as many as 51,000 jobs as shown in Exhibit E-1.

Exhibit E-1. Employment impacts of Maryland's health brokerage/underwriting industry (full-time and part-time jobs)

Range of number of health underwriting professionals	*Direct Impacts*	*Indirect Impacts*	*Induced Impacts*	*Total*
20,000	20,000	12,132	12,016	44,147
21,500	21,500	13,042	12,917	47,458
23,000	23,000	13,952	13,818	50,769
Sources: Sage, IMPLAN				

Moreover, the health brokerage/underwriting industry provides high quality employment with the average annual compensation for direct health underwriting jobs exceeding $73,000. This

translates into direct annual compensation for the industry's workers estimated to range from $1.5 billion to $1.7 billion. When the income of those additional jobs supported by the health brokerage/underwriting industry is included, the total annual compensation for all workers supported by the industry is estimated to range from $2.7 billion to $3.1 billion, or roughly $60,000/job. See Exhibit E-2.

Exhibit E-2. Income impacts of Maryland's health brokerage/underwriting industry (millions of 2010 dollars)

Range of number of health underwriting professionals	*Direct Impacts*	*Indirect Impacts*	*Induced Impacts*	*Total*
20,000	$1,467	$663	$534	$2,663
21,500	$1,577	$712	$574	$2,863
23,000	$1,687	$762	$614	$3,063
Sources: Sage, IMPLAN				

Healthcare reform and its goal of reducing the number of uninsured will place demands on Maryland to create a health insurance exchange to facilitate the enrollment of uninsured individuals and small groups into insurance policies. This exchange will be housed in a website that is intended to make purchasing health insurance as uncomplicated as possible.

Existing Capacity can Save the State Millions of Dollars

The simplicity of ordering insurance online will necessitate highly complex and expensive software, computer programming, and related equipment and facilities. Fortunately in Maryland, the capabilities to create such an exchange are already in operation and are part of the ongoing business capabilities of the state's third party administrators (TPAs) and wholesalers, known collectively as intermediaries, specialized firms within the health underwriting industry. These companies have invested tens of millions of dollars into developing, refining, maintaining, and updating websites and the information technology infrastructure that the state's health insurance exchange will need. Moreover, this existing capability allows these companies to realize substantial economies of scale when adding large numbers of new customers to the existing infrastructure.

Total investments made by Maryland's intermediaries in existing information technology infrastructure to support existing market participants are estimated at **$57 million**. This investment is dominated by software design and development and website design and development, which account for over 90 percent of these costs. Remaining costs are attributable to the facilities and equipment required to support this information technology infrastructure.

Over time, the intermediaries have invested substantially more than this in information technology. The $57 million estimate is the cost to replicate the existing technology – a cost that the State could either choose to endure or avoid. The annual operational costs for websites and

related information technology are estimated at **$10 million** and include costs related to maintaining software and programming. In the rapidly changing world of information technology, simply maintaining the status quo guarantees obsolescence. Consequently, the intermediaries invest about **$9 million** annually in capital improvements to assure that this technology maintains its currency.

To buttress the website and other technology that is the online health insurance exchange, there will need to be a customer service capability to handle the extraordinary volume of inevitable questions and inquiries that health insurance coverage will entail. Creating this capability involves a substantial investment in facilities and equipment and, of course, in training and developing the people who provide this service. The intermediaries have invested an estimated **$25 million** in creating this customer service capability. Once in place, customer service costs the intermediaries **$47 million** in annual operating expenses. Intermediaries handle about 1.6 million phone calls and about 20 million email inquiries annually. These figures do not include the innumerable calls and emails handled by independent brokers. Given that most of these costs are for staff, there are relatively modest, but still significant annual capital improvement costs of **$1 million** to maintain facilities and equipment.

Any new exchange that failed to take advantage of this capacity would have to replicate in full that which already exists at substantial costs. *Sage's analysis indicates that the existing health brokerage industry in Maryland has invested at least **$150 million** in existing capacity.*

I. Contributions of Health Brokers/Underwriters to Maryland's Economy

Defining the Industry

Health brokers/underwriters encompass health insurance agents, brokers, intermediaries, consultants and benefit professionals. Collectively, this industry is referred to as "the brokers" by public officials, clients, and many others. The common purpose of these professionals is to assist employers and individuals in their efforts to obtain the best health insurance coverage at the most affordable price all the while recognizing the struggle clients face to balance the desire to purchase high-quality and comprehensive health coverage with the reality of rapidly escalating medical care costs. After the sale, health underwriters provide administrative service and support for insurance policies and help clients with claims issues and other questions.[1,2]

A fundamental source of information that is helpful in understanding the dimensions of the brokerage/underwriting industry is the Maryland Insurance Administration (MIA), the agency with regulatory authority over the insurance industry in the state. Among its responsibilities is the licensing of insurance brokers and agents, and insurance advisors as well as firms employing insurance professionals. These licenses are a requirement for anyone wishing to do business in the state, both Maryland-based companies and residents as well as companies located elsewhere and individuals residing outside Maryland.

The MIA regularly updates its database of licensed insurance professionals and firms. As of October 18, 2010, almost 25,000 Maryland residents were licensed producers (i.e. brokers and agents) for life, health, and variable insurance not including a small number of Maryland residents who were licensed advisors. Over 2,000 Maryland-based insurance firms were licensed by MIA. An even greater number of nonresident producers and firms were also licensed by the State of Maryland. Exhibit 1 summarizes these statistics.

Exhibit 1. Life, health, and variable insurance professionals and firms licensed in Maryland

	Producers	*Advisers*	*Total licenses*	*Producer Firms*
Resident	24,963	188	25,151	2,017
Nonresident	53,557	90	53,647	3,430
Total	78,520	278	78,798	5,447
Source: Maryland Insurance Administration				

As an economic description of brokers in Maryland, MIA license data have several confounding factors. One, the existence of a license does not necessarily mean that an individual is actively engaged in work. Some licenses are likely held by individuals who have retired or have changed careers. The number of Maryland license holders then represents an upper limit on the number of agents, brokers and advisers. Two, the data on insurance professionals includes those involved in health insurance as well as life and variable insurance activities. In many cases, the

[1] "About BAHU," www.baltimoreahu.org/about.htm
[2] "About NAHU," www.marylandahu.com/

same individual provides services in all these areas. In some cases, these producers may not be involved in the health insurance side of the business at all. Thus, the number of health underwriters is almost certainly smaller than the number of licenses shown in Exhibit 1. Finally, some individuals have licenses as producers and as advisers. As a result, the total number of resident licenses (i.e. 25,151 licenses) may not accurately represent the total number of active brokers; although it does represent a number of active licenses.

There are several standard published sources of descriptive information that allow for an understanding of the economic status and significance of the brokerage/underwriting industry in Maryland. The most important of these are reports by the U.S. Bureau of the Census and reports by the U.S. Bureau of Labor Statistics. Because these data sources use different methods including censuses, surveys, and data reported by employers to various agencies, the data they report are not identical. These government data sources are also used by private companies to compile economic statistics. From these various sources it is possible to construct a basic understanding of the business establishments, employment, income, and business revenue associated with health underwriters in Maryland.

In reviewing these data, it is important to distinguish between those who work as employees of insurance firms and those who are self-employed. Businesses with employees account for approximately 98 percent of all jobs in the country.[3] As a result, some standard data sources concentrate on these employer business establishments and ignore self-employment. Certain industries, however, have relatively high concentrations of self-employed persons. Insurance is one of these industries; thus, any examination of the health underwriting industry must carefully consider these self-employed persons.

The following discussion reviews standard sources of data on the brokerage/underwriting industry. All these data sources use the North American Industry Classification System (NAICS) to categorize data. The discussion is based on the code for agencies, brokerages, and other insurance related activities (specifically code 5242).[4] The MIA license data are included as a benchmark for employment and business establishments. It should be noted that the NAICS data include those involved with property and casualty insurance while the MIA data presented below exclude these activities. (MIA has separate listings for producers and firms involved in property and casualty insurance.)

Exhibit 2 provides data on business establishments (i.e. unique locations) for insurance agencies, brokerages, and other insurance services. Insurance carriers (e.g., CareFirst, Aetna) are not included in these data. The data on employer establishments are relatively consistent from the

[3] www.bls.gov/cew/peoplebox.

[4] Code 5242 includes agents, brokers, third party administrators, and those providing insurance services, including advisory services and insurance ratemaking services, on a contract or fee basis (except insurance agencies and brokerages, claims adjusting, and third party administration). Insurance carriers fall under code 5241 and are not included in 5242.

various sources ranging from a high of 2,376 establishments in the 2007 Economic Census to a low of 2,017 establishments licensed by the MIA in 2010. This may indicate a reduction in the number of establishments in recent years although the fact that the MIA data excludes property and casualty establishments that are included in the other sources makes this conclusion unreliable.

Establishments for self-employed persons are defined by the Census Bureau as the tax returns of self-employed persons. The locations of these establishments may be commercial offices or home offices. Essentially establishments for the self-employed are a count of the number of self-employed individuals who are insurance agents, brokers, and other related professionals. The two data sources for these establishments are consistent at just over 6,100 establishments. As noted, these business establishments may and, most likely, do offer health, life, and variable insurance services, not just health insurance services.

Exhibit 2. Estimates of health brokerage/underwriting establishments

Data source	*Establishments with employees*	*Establishments of self-employed persons*	*Total establishments*
2007 Economic Census	2,376	6,111	8,487
2008 County Business Patterns	2,272	N.A.	N.A.
2008 Nonemployer Statistics	N.A.	6,137	N.A.
2008 Quarterly Census of Employment and Wages	2,282	N.A.	N.A.
2010 Maryland Insurance Administration	2,017	N.A.	N.A.
Sources: U.S. Census Bureau, U.S. Bureau of Labor Statistics, Maryland Insurance Administration			

Given that the MIA license data represent an upper bound on health, life, and variable insurance firms and establishments and that other data sources include all types of insurance, an estimate of approximately 2,000 employer firms actively involved in health underwriting is reasonable. This figure does not include the establishments of self-employed persons.

Employment in the health brokerage/underwriting industry is also subject to some uncertainty given the different reporting methods used by standard data sources. The number of employees of the roughly 2,000 employer firms in this sector of the insurance industry ranges from 15,384 (Bureau of Labor Statistics) to 16,770 (Census Bureau). A distinctive characteristic of this employment is that the industry includes a high proportion of self-employed persons. Indeed, the two available estimates indicate that more than 6,100 insurance professionals are self-employed. Total employment also shows a range from not quite 20,000 (IMPLAN) to almost 23,000 (Census Bureau). Both of these employment estimates are below the total of over 25,000 licenses issued by the Maryland Insurance Administration to health, life, and variable insurance professionals. See Exhibit 3.

Exhibit 3. Estimates of health brokerage/underwriting employment

Data source	*Employees*	*Self-employed persons*	*Total employment*
2007 Economic Census	16,770	6,111	22,881
2008 County Business Patterns	16,340	N.A.	N.A.
2008 Nonemployer Statistics	N.A.	6,137	N.A.
2008 Quarterly Census of Employment and Wages	15,384	N.A.	N.A.
2008 IMPLAN	N.A.	N.A.	19,973
2010 Maryland Insurance Administration (1)	N.A.	N.A.	25,151

Note. (1) MIA data are licenses for health, life, and variable insurance professionals and include some individuals with more than one license, thus overestimate total employment in this part of the industry.
Sources: U.S. Census Bureau, U.S. Bureau of Labor Statistics, IMPLAN, Maryland Insurance Administration

As noted several times, the MIA data on licenses include professionals in life and variable insurance activities who may not also be involved in health insurance. Moreover, the existence of a license does not necessarily mean active engagement in work. Consequently, the total number of brokers in Maryland is most likely in the range of 20,000 to 23,000. Because of the inclusion of all types of insurance agents, brokers, and related professionals in these estimates, the lower end of this range—20,000 professionals—is a more conservative estimate of health underwriting employment in Maryland.

The income (e.g., wages, salaries, commissions) of these professionals is estimated by government agencies and private companies, but is subject to the kinds of caveats that apply to enumerating firms and workers. All these estimates are presented in the source materials in either 2007 or 2008 dollars. To allow for direct comparisons and for greater clarity, these values have been converted to 2010 dollars as shown in Exhibit 4.[5] Not all sources of employment and firm/establishment data provide data on payrolls or compensation. Of the government sources that provide compensation data, none provide data regarding income for the self-employed although some provide data on sales and revenue for the self-employed, which is discussed later in this report.

[5] Conversion to 2010 dollars was done using the Employment Cost Index of the U.S. Bureau of Labor Statistics. This index measures the change in the cost of labor, including benefits such as health insurance, free from the influence of employment shifts among occupations and industries.

Exhibit 4. Estimates of health brokerage/underwriting payrolls and compensation (millions of 2010 dollars)

Data source	*Employees*	*Self-employed*	*Proprietors*	*Total*
2007 Economic Census	$1,035	N.A.	N.A.	N.A.
2008 County Business Patterns	$1,055	N.A.	N.A.	N.A.
2008 Nonemployer Statistics	N.A.	N.A.	N.A.	N.A.
2008 Quarterly Census of Employment and Wages	$1,047	N.A.	N.A.	N.A.
2008 IMPLAN	$1,369		$96	$1,465
Sources: U.S. Census Bureau, U.S. Bureau of Labor Statistics, IMPLAN				

As shown in Exhibit 4, the three estimates of payroll for employees are in virtual agreement, ranging from $1,035 million to $1,055 million in 2010 dollars. This compensation is for individuals employed at the approximately 2,000 insurance firms and establishments in Maryland. Missing from these values is the income earned by the self-employed as well as other types of proprietors' income such as the profits of business owners. IMPLAN provides estimates of these other types of income.[6] As a result, the IMPLAN estimate of total compensation approaches $1.5 billion and, as would be expected, is well above the value of payroll for employees.

While the IMPLAN estimate of total compensation is 40 percent higher than the payroll estimates shown in Exhibit 4, the per worker compensation from these different sources falls within a much narrower range. Compensation per employee ranges from almost $62,000 to just over $68,000 based on estimates from the Census Bureau and the Bureau of Labor Statistics. The IMPLAN per worker value is significantly higher at over $73,000, but this includes self-employed workers, business owners' profits, and other items not included in the lower values. See Exhibit 5.

Exhibit 5. Estimates of health brokerage/underwriting compensation per worker (2010 dollars)

Data source	*Employees*	*Self-employed*	*Proprietors*
2007 Economic Census	$61,727	N.A.	N.A.
2008 County Business Patterns	$64,578	N.A.	N.A.
2008 Nonemployer Statistics	N.A.	N.A.	N.A.
2008 Quarterly Census of Employment and Wages	$68,062	N.A.	N.A.
2008 IMPLAN	$73,336		
Sources: U.S. Census Bureau, U.S. Bureau of Labor Statistics, IMPLAN			

[6] IMPLAN is a proprietary source of economic data such as employment, income, and business sales. It is also the industry standard for estimating the impacts of economic activity.

Estimates of total revenue or sales generated by brokers in Maryland are available from Census Bureau documents and from IMPLAN. Two estimates of revenue for self-employed professionals are consistent and range from $349 million to $364 million in 2010 dollars. Only the Economic Census estimates revenue for employer firms ($2.8 billion), while IMPLAN only provides only a summary value for revenue of employer firms and the self-employed. Consequently, there are two estimates of the total revenue for this segment of the insurance industry in Maryland. In 2010 dollars, these estimates are quite consistent and range from $3.1 billion to $3.2 billion as shown in Exhibit 6.

Exhibit 6. Estimates of health brokerage/underwriting sales and revenue (millions of 2010 dollars)

Data source	*Employer firms*	*Self-employed*	*Total*
2007 Economic Census	$2,774	$364	$3,138
2008 County Business Patterns	N.A.	N.A.	N.A.
2008 Nonemployer Statistics	N.A.	$349	N.A.
2008 Quarterly Census of Employment and Wages	N.A.	N.A.	N.A.
2008 IMPLAN	N.A.	N.A.	$3,246
Sources: U.S. Census Bureau, U.S. Bureau of Labor Statistics, IMPLAN			

Multiplier Effects and Total Economic Impacts of the Health Brokerage/Underwriting Industry

The 20,000 or more health underwriting professionals and the 2,000 insurance firms in Maryland create economic opportunities for other parts of the state's business community. In conducting their work, these workers and firms require a range of goods and services in order to operate. These requirements from utility services for offices to computers and office equipment create new demands for other Maryland businesses who are suppliers to the underwriting industry. The revenue these suppliers receive from the insurance industry is used to support their own workers and payroll and also to buy the goods and services from other Maryland businesses that they need to operate. This cascading series of purchases in the supply chain is considered the indirect impact of the underwriting industry.

When Maryland's brokers and the indirect workers supported by the underwriting professionals spend their incomes in the Maryland economy, they create another set of impacts that are termed induced impacts. These impacts are typically defined as the consumer-oriented goods and services provided by retail, service, and other local businesses and include haircuts and home mortgages, groceries and birthday gifts along with thousands of other goods and services.

These indirect and induced impacts when added to the direct impacts of the health brokerage/underwriting industry constitute the total contribution that the industry makes to the Maryland economy. This contribution can be measured in terms of employment, income, and business sales.

Given the difficulty in pinning down a specific number of brokers in Maryland, the following discussion of the industry's impacts presents a range of impacts based on the estimate that there are likely to be 20,000 to 23,000 workers in Maryland's health brokerage/underwriting industry.

For every job in the health brokerage/underwriting industry, there are approximately 1.2 jobs resulting from the indirect and induced impacts. Thus, at the lower end of the estimated range of 20,000 brokers in Maryland there are an estimated 24,147 additional jobs supported by these brokers making a total of 44,147 jobs in the state related to 20,000 health brokerage/underwriting jobs. At the upper end of the estimated range of health brokerage/underwriting jobs—23,000 professionals in Maryland, there are a total of almost 51,000 jobs in the state that are supported by the health brokerage/underwriting industry.

Exhibit 7 provides more detailed information on the employment impacts associated with the health brokerage/underwriting industry for a range of estimates of the number of health brokerage/underwriting professionals. Direct impacts are the health brokerage/underwriting jobs themselves, indirect impacts are jobs in the supply chain for the health brokerage/underwriting industry, and induced impacts result from the household spending of the direct and indirect workers. These jobs include a mix of mostly full-time and some part-time workers.

Exhibit 7. Employment impacts of Maryland's health brokerage/underwriting industry (full-time and part-time jobs)

Range of number of health underwriting professionals	*Direct Impacts*	*Indirect Impacts*	*Induced Impacts*	*Total*
20,000	20,000	12,132	12,016	44,147
21,500	21,500	13,042	12,917	47,458
23,000	23,000	13,952	13,818	50,769
Sources: Sage, IMPLAN				

The annual income associated with these jobs is substantial. Exhibit 8 summarizes the income for brokers (direct impacts), the brokers' supply chain (indirect impacts), and the consumer-oriented businesses that serve workers at health brokerage/underwriting firms and their supply chain. Income for brokers ranges from a total of $1.5 billion to $1.7 billion. The estimated total income for all workers supported by the health brokerage/underwriting industry ranges from $2.7 billion to over $3 billion statewide. Brokers tend to fit neatly within the middle and upper middle classes. On average, the income per worker in the health underwriting industry exceeds $73,000 and is 25 percent higher than the average for all workers in Maryland, though this higher average compensation can be viewed largely as a return to educational attainment.

Exhibit 8. Income impacts of Maryland's health underwriting industry
(millions of 2010 dollars)

Range of number of health underwriting professionals	*Direct Impacts*	*Indirect Impacts*	*Induced Impacts*	*Total*
20,000	$1,467	$663	$534	$2,663
21,500	$1,577	$712	$574	$2,863
23,000	$1,687	$762	$614	$3,063
Sources: Sage, IMPLAN				

The annual business sales impacts of the health brokerage/underwriting industry are presented in Exhibit 9. As with the previous tables, these estimated impacts are based on a total number of brokers ranging from 20,000 to 23,000. Business sales for health underwriting professionals (direct impacts) encompasses sales both to employer firms (i.e. businesses with employees) and to individual proprietors. These direct impacts range from $3.3 billion to $3.7 billion. When the sales of suppliers (indirect impacts) and consumer-oriented businesses (induced impacts) are added to the business sales of the health brokerage/underwriting industry itself, total impacts for business sales range from $6.5 billion to $7.5 billion.

Exhibit 9. Business sales impacts of Maryland's health brokerage/underwriting industry
(millions of 2010 dollars)

Range of number of health underwriting professionals	*Direct Impacts*	*Indirect Impacts*	*Induced Impacts*	*Total*
20,000	$3,250	$1,643	$1,630	$6,523
21,500	$3,494	$1,766	$1,752	$7,013
23,000	$3,738	$1,890	$1,874	$7,502
Sources: Sage, IMPLAN				

The health brokerage/underwriting industry represents a significant share of the total Maryland economy. As much as 1.5 percent of the total state economy is supported by the health brokerage/underwriting industry. One in every 70 jobs in the state is supported by the industry.

II. Creation of a Health Insurance Exchange

A New Federal Mandate

A major initiative under the new federal healthcare reform legislation is a requirement that states create health insurance exchanges that can facilitate the expansion of insurance coverage to those who are uninsured. In the study team's view, health insurance exchanges are the most critical element of existing federal legislation regarding meeting the basic goal of healthcare reform, which is to enroll the uninsured.

A few states have recently created health insurance exchanges. While the number of states is few, they include states (e.g., Massachusetts and Utah) with strikingly different demographic characteristics and philosophies regarding these exchanges. Before the 2010 federal reforms, Massachusetts took an approach that includes state policies on minimal requirements for policies offered to residents and a requirement that policies offered through the exchange be categorized into groups of similar benefits relative to costs. Utah has taken a more hands-off approach, essentially providing a lightly regulated platform for insurance carriers interested in doing business in the state.[7] In part, this report represents the successor to a 2010 study conducted in 2010 entitled *A Health Insurance Exchange for Maryland? Comparing Massachusetts and Maryland* by Robert L. Carey and Dr. Jonathan M. Gruber. That report concluded that Maryland's transition to a statewide health insurance exchange could be less onerous than Massachusetts' transition because of the presence of capable and sophisticated private sector intermediaries in Maryland.

Websites are the most visible element of these exchanges. Backing up these websites is software that allows for gathering of information on available plans, comparing alternatives, selecting a specific plan, and applying for the selected plan. The Massachusetts exchange can help individuals enroll in Medicaid and other public health programs. It also supports the process of subsidizing insurance coverage for those who are eligible.

In addition to the information technology that enables the websites, the exchanges involve a customer service component that addresses the inevitable questions, concerns, and complaints that arise. This component requires not only call centers for telephone inquiries, but also the capacity to respond to email, written, and other types of communication.

These exchanges must be operational by January 2014. The federal government will evaluate the progress states have made as of January 1, 2013 and the federal government is required to operate exchanges for states unable or unwilling to do so.

[7] A discussion of the Massachusetts and Utah health insurance exchanges can be found in "Healthcare overhaul depends on states' insurance exchanges," Robert Pear, *The New York Times*, October 24, 2010.

Investments that Can Support the Mandated Maryland Health Insurance Exchange

A basic question for the State of Maryland is how best to implement this health insurance exchange requirement. While the state will need to define a basic approach that best meets the needs of Marylanders, there is an unavoidable need for the basic infrastructure for health insurance distribution that will serve the needs of individuals and small groups in the state.

Maryland is in a particularly fortunate position relative to the development and operation of the federally mandated statewide health insurance exchange. Existing insurance organizations known as third party administrators (TPAs) and wholesalers serve the small group (i.e. employers with two to 50 employees) and individual insurance market in Maryland. These companies, the TPAs and wholesalers, also known as intermediaries, provide a vital link between insurance carriers and the brokers who deal directly with small businesses and individuals and often also work directly with small businesses and individuals (e.g., implementing the billing function) once policies are in place.

The small businesses and individuals served by intermediaries are the same market that is the focus of health insurance exchanges. Currently, the intermediaries serve over 225,000 individuals and almost 50,000 small groups.

A recent report on small group health insurance in Maryland by the Maryland Healthcare Commission found that the average small employer had eight covered employees in 2007, a modest decrease from the average of 8.4 covered employees in 1999.[8] Assuming that the average employer in 2010 has approximately eight covered employees, then the total number of policies among customers of the Maryland intermediaries is over 625,000 (225,000 individuals + roughly 400,000 covered within small group policies). These policies include those that cover only the employee, those covering the employee and some dependents, and some policies that cover all members of the employee's family.

There are very limited data regarding the distribution of policies among these options although the Maryland Healthcare Commission report indicated that the coverage of dependents declined from 1999 to 2007. Based on data from Maryland's intermediaries, estimates of the average number of individuals covered by each policy range from roughly 1.25 to 2.5 persons. If this range is narrowed to approximately 1.5 to 2 persons per policy, then these 625,000 policies provide health insurance to as few as 950,000 Marylanders or as many as 1.25 million Marylanders (see Exhibit 10).

[8] Maryland Healthcare Commission, "Small Group Market Report," presentation to Joint Committee on Healthcare Delivery and Financing, October 14, 2008

Exhibit 10. Estimated number of Marylanders covered by intermediaries

	Estimated number of policies	People covered at 1.5 persons covered per policy	People covered at 2 persons covered per policy
Coverage through Maryland intermediaries	625,000	950,000	1,250,000

Note. Maryland households average 2.6 persons.
Sources: Maryland intermediaries, Maryland Healthcare Commission, Maryland Department of Planning

This range of persons per policy (i.e., 1.5 to 2 persons) is the rough equivalent of assuming that at the low end of the range two-thirds of policies cover individuals and one-third cover the typical Maryland household of 2.6 persons. At the high end of the range, approximately two persons per policy is the equivalent of one-third of policies covering individuals and two-third covering typical Maryland households.

The extent of this service provided to Maryland residents through the intermediaries can be compared to the estimated number of Marylanders—793,000 in 2009—who are uninsured. The year-to-year change in the number of uninsured has been somewhat volatile recently; however, the number of uninsured has increased only about 2 percent since the State expanded Medicaid and other public health programs in 2006.[9]

Thus, in recent years, Maryland has had about a relatively consistent number of not quite 800,000 residents who lack private health insurance or other health benefits. This number is about 65 percent to 85 percent of the number of Marylanders who are now served by the state's intermediaries.

The cornerstone of the brokers' business is customer service. The volume of this service is remarkable and an indicator of the types of service that any Maryland health insurance exchange must provide. The medical system is inherently complex and often deals with matters that can be fraught with anxiety. Necessarily, health insurance brokers must deal with these complexities and concerns by establishing a robust customer service capability.

The intermediaries offer different levels and types of services to their customers, including services related to billing, claims, and other activities. In some cases, intermediaries provide a wide range of services while in others they provide more limited services and refer customers to insurance carriers for some services. One larger intermediary provides services related to Medicare and Medicaid, for example, while the others do not. As a result, the volume of communications for each intermediary varies considerably and reflects the levels and types of services provided. Total communications events handled by the intermediaries do, however,

[9] Scott Graham, "Census: Maryland uninsured rate rose 14 percent in 2009," *Baltimore Business Journal*, September 16, 2010

provide a guide to the level of effort that any Maryland health exchange should be prepared to deliver.

As noted in Exhibit 11, intermediaries handle about 1.6 million phone calls and about 20 million email inquiries annually. The average phone call can require 3 to 4 minutes of time while certain email responses can take considerably longer. The intermediaries also respond to other forms of communication (e.g., website generated questions, comments handwritten on invoices). Because at least a significant share of the population that will be served by a health insurance exchange is likely to be relatively unfamiliar with health insurance, there is every likelihood that customer service demands will be considerable and will undoubtedly be an important aspect of the exchange's services.

Exhibit 11. Customer service activities

Type of communications	*Millions of events*
Phone calls	1.6
Email	20
Source: Maryland intermediaries	

Another fundamental service typically provided by the intermediaries is billing. This includes not only monthly and other routine invoicing of customers and payments to providers, but also a continuous updating of customer records as addresses change, small group members are added or deleted, and other needs to change records arise. The intermediaries currently undertake over 5 million of these individual billing transactions annually.

The intermediaries already have the basic information technology infrastructure in place that could support a Maryland health insurance exchange. Intermediaries also provide a range of services that are essentially the same as those provided by existing health insurance exchanges, including information on existing policies, the capacity to enroll individuals and small groups, ongoing administrative support for policy holders (e.g., billing of policy holders, payment of insurance providers), and customer service. Maryland's intermediaries have experience with the types of split payment issues (e.g., partial payment by the policy holder and partial payment by an employer or former employer) that will be part and parcel of the subsidies that are mandated by health reform legislation.[10]

In particular, the intermediaries have developed websites undergirded by customized software that provide comprehensive information on health insurance policies available to individuals and small groups. The intermediaries have used this information technology to work with health underwriters in Maryland (i.e. insurance agents and brokers) who in turn work with small groups

[10] The capabilities of Maryland's intermediaries and their ability to take on the functions of a health insurance exchange are explored in the report, "A health insurance exchange for Maryland? Comparing Massachusetts and Maryland" which was prepared by Robert L. Carey and Jonathan M. Gruber, Ph.D. for the Maryland Association of Health Underwriters and the National Association of Insurance and Financial Advisors of Maryland.

and individuals. The technology is readily adaptable to use directly by individuals and, in fact, the intermediaries have considered extending access to these websites to the public.

The intermediaries' investment in this technology infrastructure has been considerable and is indicative of the level of investment that the development of a Maryland health insurance exchange will entail. As noted in Exhibit 12, investments by Maryland's intermediaries in the existing information technology infrastructure is estimated at $57 million. This cost is dominated by software design and development and website design and development, which account for over 90 percent of these costs. Remaining costs are attributable to the facilities and equipment required to support this information technology infrastructure. Over time, the intermediaries have invested substantially more than this in information technology. The $57 million estimate is the cost to replicate the existing technology. The annual operational costs for websites and related information technology are estimated at $10 million and include costs related to maintaining software and programming. In the rapidly changing world of information technology, simply maintaining the status quo guarantees obsolescence. Consequently, the intermediaries invest about $9 million annually in capital improvements to assure that this technology maintains its currency. The basic lesson of this experience is that to create from scratch the information technology that would be a platform for Maryland's health insurance exchange would require investing tens of millions of dollars and then supplying millions of dollars for annual operating costs and additional millions of dollars in annual capital improvements.

Exhibit 12. Information technology investments and costs related to a health insurance exchange

Type of cost	*Value in millions*
Investment Cost	$57
Annual Operational Cost	$10
Annual Capital Improvement Cost	$9
Source: Maryland intermediaries	

To buttress the website and other technology that is the online health insurance exchange, there will need to be a customer service capability to handle the extraordinary volume of inevitable questions and inquiries that health insurance coverage will entail. Creating this capability involves a substantial investment in facilities and equipment and, of course, in training and developing the people who provide this service. The intermediaries have invested an estimated $25 million in creating this customer service capability. Once in place, customer service costs the intermediaries $47 million in annual operating expenses. Given that most of these costs are for staff, there are relatively modest, but still significant annual capital improvement costs of $1 million to maintain facilities and equipment. Exhibit 13 summarizes the investment and annual costs that the intermediaries current customer service operations require.

Exhibit 13. Customer service investments and costs related to a health insurance exchange (millions of dollars)

Type of cost	*Value in millions*
Investment Cost	$25
Annual Operational Cost	$47
Annual Capital Improvement Cost	$1
Source: Maryland intermediaries	

Because the intermediaries already serve a substantial share of the individual and small group market in Maryland and have developed robust infrastructure to support that service, adding new customers comes at a relatively modest cost. The total number of uninsured Marylanders is known. The number of new customers that health reform would bring to a Maryland health insurance exchange, however, is unknown. Some currently uninsured would likely become members of a small group while others would be individual policy holders. The coverage of dependents would presumably fall under either the option of group coverage or individual coverage.

Because of these unknowns, the intermediaries were surveyed by the study team regarding the cost of upgrading the website and associated information technology to add an additional 10,000 customers as well as the annual cost associated with providing services to 10,000 new customers. Not surprisingly, the principal cost of adding new customers would be the ongoing provision of customer service, an inherently staff laden cost. On the other hand, the cost of expanding website and other technology to handle added customers was considered very modest.

There are also many undefined characteristics of a Maryland health exchange that could affect costs (e.g., whether the health exchange would provide billing services or customer services for claims). Nevertheless, based on cost estimates from the intermediaries, the marginal cost of adding 10,000 new customers is a fraction of the average cost they have incurred in creating the basic infrastructure of a health insurance exchange. Expanding the basic web-based technology for another 10,000 customers would only cost 5 to 10 percent of the average cost of creating that technology. Supporting those new policy holders with ongoing customer services would cost perhaps 35 percent to 65 percent of the average cost of current customer service capabilities. This cost would depend on the actual mix of individuals and small groups, the volume of customer service demands from this group relative to the volume of demands from the current customer base, and other factors. Moreover, there may be certain cost hurdles for several hundred thousand new customers compared to 10,000 new customers. Still, because the intermediaries know this market and its requirements, there are significant, almost certainly substantial, economies of scale that apply to adding new customers that make this expansion particularly cost effective. See Exhibit 14.

Exhibit 14. Marginal cost to add 10,000 additional customers

Cost element	*Marginal cost as share of average cost*
Website investments	5 - 10 percent
Customer service annual operating costs	35 - 65 percent
Source: Maryland intermediaries	

Healthcare reform and its goal of reducing the number of uninsured will place demands on Maryland to create a health insurance exchange to facilitate the enrollment of uninsured individuals and small groups into insurance policies. The capabilities to create such an exchange are already in operation in Maryland and are part of the ongoing business capabilities of the state's intermediaries. These companies have invested tens of millions of dollars into developing, refining, maintaining, and updating the information technology infrastructure that the state's health insurance exchange will need. Moreover, this capability allows these companies to realize substantial economies of scale when adding large numbers of new customers.

Thus, while Maryland needs to make basic policy decisions about how a health insurance exchange will operate and what its particular capacities will be, the state can turn to the health underwriting industry to readily convert these policies and procedures into a functional exchange. Existing and proven industry capabilities will greatly facilitate the launching of such an exchange in a timely and economic manner.

Conclusion

Maryland is home to a vibrant health brokerage/underwriting industry. This industry is dominated by small businesses though there are also several larger players associated with substantial technological prowess and investment. Roughly 30 percent of industry employment is comprised of solo practitioners. The Sage study team estimates that the industry directly employs more than 20,000 employees and supports directly and indirectly more than 50,000 jobs in Maryland associated with roughly $3 billion in income. This translates into $60,000/job.

The State of Maryland is presently contemplating how to implement a healthcare reform-mandated state-based insurance exchange. This report suggests that the health underwriting industry already possesses much of the technology, personnel and capacity to support this exchange, which essentially would be a website available to the public featuring insurance options, pricing and other details.

Investments made by Maryland's intermediaries in existing information technology infrastructure to support existing market participants are estimated at $57 million. This cost is dominated by software design and development and website design and development, which account for over 90 percent of these costs. Remaining costs are attributable to the facilities and equipment required to support this information technology infrastructure.

Over time, the intermediaries have invested substantially more than this in information technology. The $57 million estimate is the cost to replicate the existing technology – a cost that the State could either choose to endure or avoid. The annual operational costs for websites and related information technology are estimated at $10 million and include costs related to maintaining software and programming. In the rapidly changing world of information technology, simply maintaining the status quo guarantees obsolescence. Consequently, the intermediaries invest about $9 million annually in capital improvements to assure that this technology maintains its currency.

To buttress the website and other technology that is the online health insurance exchange, there will need to be a customer service capability to handle the extraordinary volume of inevitable questions and inquiries that health insurance coverage will entail. Creating this capability involves a substantial investment in facilities and equipment and, of course, in training and developing the people who provide this service. The intermediaries have invested an estimated $25 million in creating this customer service capability.

Once in place, customer service costs the intermediaries $47 million in annual operating expenses. Intermediaries handle about 1.6 million phone calls and about 20 million email inquiries annually. The average phone call can require 3 to 4 minutes of time while certain email responses can take considerably longer. The intermediaries also respond to other forms of communication (e.g., website generated questions, comments handwritten on invoices). Because

at least a significant share of the population that will be served by a health insurance exchange is likely to be relatively unfamiliar with health insurance, there is every likelihood that customer service demands will be considerable and will undoubtedly be an important aspect of the exchange's services. Given that most of these costs are for staff, there are relatively modest, but still significant annual capital improvement costs of $1 million to maintain facilities and equipment.

Sage has identified at least $150 million in private sector investment that handles health brokerage and insurance services in Maryland on a daily basis. This is likely a significant underestimate of total capital expenditures given that it is virtually impossible to calculate the capital investments made over time by independent brokers. Based on this existing intermediary capacity, it is estimated that the State could avoid tens of millions of dollars in one-time and ongoing expenditures by making appropriate use of existing Maryland-based private sector capabilities.

Notes on data sources.

Maryland Insurance Administration. The MIA licenses insurance professionals as a part of its regulatory responsibilities. On a weekly basis, the MIA updates its lists of licensees. The lists noted below are available at the MIA website (www.mdinsurance.state.md.us).

- Active Resident Individual Producers with Life, Health and Variable
- Active Non-resident Individual Producers with Life, Health and Variable
- Active Resident Individual Producers with Property and Casualty
- Active Non-resident Individual Producers with Property and Casualty
- Active Firms with Life, Health and Variable
- Active Firms with Property and Casualty
- Active Individuals and Firms with Title
- Active Adviser with Adviser Life/Health, Adviser Property/Casualty and Adviser Variable
- Active Surplus Line Brokers and Adjusters

Minnesota IMPLAN Group, Inc., IMPLAN The industry-standard source of input-output analysis, IMPLAN uses federal government data sources (e.g., QCEW, CBP) to compile information for the U.S., states, and sub-state jurisdictions. IMPLAN's models of state and local economies can be used to examine the relationships and interdependencies among industries.

Third party administrators (TPAs). One of two types of insurance companies along with wholesalers that act as intermediaries between carriers, brokers, and customers. Maryland has three major TPAs which provide services that are closely aligned to those required by the federally mandated health insurance exchange. These companies─Benefit Mall, Group Benefit Services, and Kelly & Associates Insurance Group─have provided the data used to estimate the investment and ongoing costs associated with websites and customer service functions that they currently provide. These two functions are central to the required health insurance exchange.

U.S. Bureau of the Census, County Business Patterns Data are extracted from the Business Register (BR) which contains the Census Bureau's most complete, current, and consistent data for U.S. business establishments. The BR is updated continuously and incorporates data from Census Bureau economic censuses and current business surveys, quarterly and annual Federal income and payroll tax records, and other Department of Commerce and Federal statistics and administrative records programs.

U.S. Bureau of the Census, Economic Census Firms in the economic census and related programs are divided into those sent report forms and those not sent report forms. For most economic census sectors and programs, all large- and medium-size firms and all multi-establishment firms were sent report forms to be completed for each of their establishments and returned to the Census Bureau.

For most sectors and programs, report forms were also mailed to a sample of small employers. These include single-establishment firms with payroll below a specified cutoff. This cutoff varies by economic census sector, industry and geography. However, for most very small firms, data from existing administrative records of other federal agencies were used instead. These records provide basic information for the business, including data on sales, payroll, number of employees, legal form of organization and other statistics.

All data for firms with no paid employees during the year (also known as "nonemployers") were obtained from administrative records of other federal agencies. Data for nonemployers are not included in the reports from the economic census but are released in the annual *Nonemployer Statistics* series.

U.S. Bureau of Labor Statistics, QCEW The Quarterly Census of Employment and Wages (QCEW**)** program publishes a quarterly count of employment and wages reported by employers covering 98 percent of U.S. jobs, available at the county, MSA, state and national levels by industry.

Jobs that are exempt or otherwise not covered by unemployment insurance are not included in the QCEW tabulations. In 2001, in the private sector, this was approximately 0.1 million wage and salary agricultural employees, 1.2 million self-employed farmers, 8.6 million self-employed nonagricultural workers, 0.4 million domestic workers, and 0.1 million unpaid family workers. A further group of excluded private sector workers were the 0.2 million workers covered by the railroad unemployment insurance system. Additionally about 0.7 million State and local government workers were also excluded. Certain types of nonprofit employers, such as religious organizations, are given a choice of coverage or exclusion in a number of States, so data for their employees were reported to a limited degree.

Wholesalers. One of two types of insurance companies along with TPAs that act as intermediaries between carriers, brokers, and customers. Maryland has four wholesalers which, like TPAs, provide services that are closely aligned to those required by the federally mandated health insurance exchange. These companies─CBIZ MT Donahoe & Associates, Potomac Basin Group Associates, LLC, Insurance Marketing Center, Inc., Employee Benefits Incorporation of America ─ were surveyed for the investment and ongoing costs associated with websites and customer service functions that they currently provide. These two functions are central to the required health insurance exchange. While wholesalers function similarly to TPAs, they tend to serve smaller customer bases.