

The Potential for Crowd Out Due to CHIP: Results from a Survey of 450 Employers

by Harriette B. Fox and Margaret A. McManus

As states design their new plans under the Children's Health Insurance Program (CHIP), nearly all are attempting to address the problem of crowd out — the substitution of publicly subsidized health insurance coverage for coverage purchased through the workplace. Crowd out can occur as a result of employers deciding to discontinue coverage for child dependents or as a result of employees electing to drop employer-based coverage for a child in favor of a less costly public option.

To understand employers' likely responses to CHIP, the Maternal and Child Health Policy Research Center contracted with the firm of Lake, Sosin, Snell, Perry, and Associates to conduct a telephone survey¹ of 450 businesses nationwide.² The sample consisted of an equal distribution of small, medium, and large businesses; was regionally stratified; and assured a significant proportion of businesses most likely to employ low and moderate wage workers. The survey, which was conducted in January 1998 and was part of a larger study of employer-based coverage of dependent children, was designed to obtain information relevant to actions that employers might take to force or encourage crowd out.

To date, little research has been conducted on crowd out that is relevant to the CHIP program. Five major analyses of national data sets have addressed crowd out as a consequence of Medicaid expansions for children between the late 1980s and the early or mid 1990s, but none has examined crowd out as a result of newer public health insurance programs predominately enrolling children in families with incomes well above the poverty level and often involving premium and other charges. Using various

methodologies, these studies found some evidence of crowd out for a population of primarily poor and near-poor children. The three studies using cross-sectional data from the Current Population Survey (CPS) found crowd-out rates — the proportion of new Medicaid enrollees who previously had employer-based coverage — of 15,³ 17,⁴ and 22⁵ percent but were unable to adequately account for either the erosion of private health insurance occurring independent of Medicaid expansions or the episodic nature of private coverage among low wage workers. The two studies using panel survey data from the National Longitudinal Study of Youth (NLSY), which permits a tracking of particular individuals over time, found rates of 14.5⁶ and 16 percent.^{7, 8} One additional study based on a telephone survey of participants in MinnesotaCare, a state-subsidized program for families with incomes up to 275 percent of poverty, found seven percent of families gave up private insurance to obtain subsidized coverage — despite strict requirements for periods of uninsurance and lack of access to affordable coverage.⁹ Neither this nor the national studies, however, consider the quality or cost of private insurance dropped.

Survey Findings

Our survey found that the vast majority of employers today offer health insurance coverage for dependent children. Ninety-four percent of survey respondents report that they make such coverage available. Yet a sizeable proportion, particularly small companies and those in the south and west, offer dependent coverage that is costly to employees. As many as 21 percent of businesses pay 35 percent or less of the premium cost of health insurance for their employees' dependents, while an additional 16 percent contribute between 36 percent and 60 percent.

Employers that do not offer any coverage for dependent children are far more likely to be small firms and to have employees who earn between \$13,000 and \$27,000.

When employers who offer coverage were asked “if publicly subsidized health insurance coverage were made available for uninsured children of families with low and moderate incomes (between \$16,000 and \$32,000 for a family of three),¹⁰ would your company drop its health insurance for employees’ dependent children,”¹¹ 87 percent said they would not, while seven percent said they would eliminate coverage, and another five percent said they would consider it.¹² However, the seven percent who would discontinue coverage fell to three percent when the respondent was told that children would be required to go without coverage for a period of three months, and to one percent when told that children would be required to go without coverage for six months. And, with a 12-month period of uninsurance required, the percent of employers reporting that they would discontinue coverage for dependent children was virtually nil.

Employers most likely to report that they would either drop or consider dropping dependent coverage with the advent of publicly subsidized insurance for low and moderate income children are those that are small. In addition, although our sample size for firms offering coverage of different values was relatively small and our findings therefore preliminary, our survey suggests firms that currently provide fewer benefits and impose greater cost-sharing requirements may be more likely than other firms to drop or consider dropping dependent coverage.

Among the 88 percent of employers who responded that they would not discontinue or consider discontinuing dependent coverage if publicly subsidized coverage became available, 14 percent reported that they would

institute one or more other changes. These would have the effect of reducing the value of coverage for children and encouraging their families to choose the CHIP option. Nine percent would increase the employee’s premium contribution for dependent coverage, 13 percent would increase cost-sharing requirements, and six percent would decrease covered services. Although almost a quarter of those who would increase employee costs for dependent coverage if subsidized coverage were available had stated earlier in the survey that they anticipated increasing the

cost of dependent coverage in the coming year, no employer stated that they expected to decrease benefits.

A surprisingly small proportion of employers seemed to know about CHIP at the time of our survey. Sixty-eight percent were not aware that federal funds

were available to states to finance subsidized health insurance for children with low and moderate incomes. Small employers and those whose workforce was composed primarily of clerical and sales employees were the least informed. It is interesting to note, however, that those who were aware of CHIP were

somewhat less likely than other employers to report that they would drop or consider dropping dependent coverage for children.

State Policy Implications

Our survey findings suggest that only a small proportion of companies are likely to drop dependent coverage in response to CHIP, while a somewhat larger segment is likely to take steps that would make private coverage less attractive. Our findings also suggest that since employers informed about CHIP were less likely to report that they would drop or even consider dropping dependent coverage and their responses may be more predictive of actual employer behavior, expected

Effects of Period of Uninsurance on Employer’s Decision to Drop Coverage

- Would drop dependent coverage 7%
- BUT if period of uninsurance is required, would drop dependent coverage:
 - 3 months 3%
 - 6 months 1%
 - 12 months 0%

Employer Responses to CHIP

- Would drop dependent coverage 7%
- Would consider dropping coverage 5%
- Would not drop or consider dropping but would increase the cost or decrease the value of dependent coverage 12%

declines in the availability of dependent coverage might be slightly smaller. However, at the same time, our survey did not capture other pertinent employer actions that might foster crowd out, such as the increasing use of flexible benefit options and the offering of financial incentives to discourage employees from purchasing coverage for children.

States concerned about crowd out may want to consider a variety of strategies to reduce it. One strategy is for a state to require that children be uninsured for a specified period of time. Such a policy would not only deter families from dropping coverage for a dependent child but, as our survey findings show, it would also deter an employer from eliminating coverage for all child dependents. A state could require that a child be uninsured for a specified period of time — perhaps three months for children in families with incomes up to 200 percent of the poverty level and longer for children at higher income levels — and possibly also require a somewhat longer period of time during which a child had to be ineligible for employer-based coverage. However, a state presumably would want to establish special exemptions for children who had lost coverage through no fault of their own. For example, exemptions could be established for children who became ineligible for Medicaid, whose employer-based coverage was discontinued, or whose parent was terminated from employment. A state might also want to permit a much shorter period of uninsurance for children deemed to have been “underinsured” — thereby making adequate coverage quickly available to all potentially eligible children without penalizing those whose families had purchased particularly expensive or limited coverage. Our finding that 21 percent of employers contribute 35 percent or less of the cost of dependent coverage for their employees suggests underinsurance may be a significant problem for some children. A state’s criteria for underinsurance could be any health insurance that provided a lesser benefit package or required more cost sharing than the state CHIP plan or it could be more restrictive.

Another strategy is for states to take steps to prevent employers from eliminating or reducing coverage for children who would be eligible for CHIP if they were uninsured. This might be accomplished by amending the state tax code to provide financial penalties (or discontinue deductions for employer contributions to employee health coverage) for businesses that drop or substantially reduce the value of health insurance coverage for child dependents to encourage CHIP enrollment.¹³ It might

also be accomplished by amending the state labor code, as California has done, to make it an unfair labor practice for employers to “change coverage or change the cost of coverage” to get employees to enroll their children in CHIP.¹⁴ However, state legislation of this type needs to be mindful of ERISA’s preemption of state regulation of self-insured health coverage available through the workplace.¹⁵

A third strategy for preventing crowd out is for states to purchase or assist families in purchasing dependent coverage that is available to them but unaffordable. The intent is to maintain private employer financing of children’s health insurance that meets the standards for benchmark or benchmark-equivalent coverage. However, according to HCFA, if state policies are not appropriately structured, this strategy could have the effect of encouraging families to discontinue employer-based coverage for a child in order to obtain lower cost CHIP coverage. For this reason, the agency has issued guidance for states suggesting that they require a period of uninsurance of at least six, but no more than 12 months; only subsidize coverage for which employers contribute at least 60 percent; and require families to contribute the same premium amount they would otherwise contribute under a state child health insurance plan. The state would pay the residual premium amount, provided that it did not exceed the subsidy that would otherwise have been paid for the child.¹⁶

Endnotes

- ¹ The survey was managed by Michael Perry and Evan Stark.
- ² We defined small businesses as those with 10 to 99 employees, medium-sized businesses as those with 99 to 1,000 employees, and large businesses as those with more than 1,000 employees.
- ³ Shore-Sheppard LD: *Stemming the Tide: The Effect of Expanding Eligibility on Health Insurance Coverage*. Pittsburgh, PA: University of Pittsburgh. Manuscript submitted for publication, November 1997. This study revises an earlier study by the same author which found no evidence of crowd out. The rate we report here is the revised estimate for the period between 1988 and 1993. The author also provides a crowd-out estimate of 41 percent for the period between 1988 and 1995. However, this estimate may be subject to error due to changes in questions, coding, and sampling that occurred in the March 1995 CPS. These questions relate to private health insurance, Medicaid, and state-specific health insurance programs for uninsured individuals. For a more detailed discussion of the CPS changes, see Swartz K: *Changes in the 1995 Current Population Survey and Estimates of Health Insurance Coverage*. *Inquiry*. 34:70-79, Spring 1997.

- ⁴ Dubay LC and Kenney GM: The Effects of Medicaid Expansions on Insurance Coverage of Children. *The Future of Children*. 6:152-161, 1996.
- ⁵ Cutler DM and Gruber J: Medicaid and Private Insurance: Evidence and Implications. *Health Affairs*. 16:194-200, 1997. This rate includes both women and children. When Cutler and Gruber estimated crowd out as the share of the decline in private insurance that constituted a substitution of Medicaid, instead of the share in the increase in Medicaid coverage that constituted a substitution of private coverage, they reported a crowd-out rate of 15 percent. Cutler and Gruber also estimated a child-specific crowd-out rate of 32 percent; however, this rate only provides a very gross estimate of the number of children who lost private coverage over those who enrolled in Medicaid as a result of the expansions.
- ⁶ Yazici EY and Kaestner R: Medicaid Expansions and the Crowding Out of Private Health Insurance. New York: Baruch College. Manuscript submitted for publication, January 1998. This study revises an earlier study by Yazici which found no evidence of crowd out.
- ⁷ Thorpe KE and Florence CS: Health Insurance Among Children: The Role of Expanded Medicaid Coverage. New Orleans, LA: Tulane University. Paper prepared for the Commonwealth Fund, November 1997.
- ⁸ It is important to note that the five studies listed above vary with respect to the child population studied. The Yazici and Kaestner study and the Shore-Sheppard study reported crowd out for those newly enrolled Medicaid children who were made eligible as a result of the Medicaid expansions. The Dubay and Kenney study and Thorpe and Florence study reported crowd out for all newly enrolled Medicaid children, those made eligible as a result of the Medicaid expansions and those who were regular Medicaid-eligibles. Cutler and Gruber report a separate crowd-out rate for all newly enrolled Medicaid recipients.
- ⁹ Call KT et al: Who is Still Uninsured in Minnesota? *Journal of the American Medical Association*. 278:1191-1195, 1997.
- ¹⁰ Although the CHIP legislation (Title XXI of the Social Security Act) refers to children in families with incomes up to 200 percent of poverty as being "low income," we chose in surveying employers to use the term "low and moderate income" so that they would not automatically assume we were talking only about children living at or below the poverty level. For this reason, we also gave a specific range of income amounts for a family of three.
- ¹¹ The survey asked a hypothetical question. We recognize that our findings may not reflect actual employer behavior.
- ¹² One percent of the sample refused to answer.
- ¹³ The federal tax code contains a requirement that could discourage at least some employers from dropping or reducing coverage for the child dependents of low wage workers who would be potentially eligible for CHIP. It requires non-discrimination among employees of different wages with respect to the health benefits they receive. However, the provision only pertains to employers who self-insure (not those who purchase health insurance), and it has numerous exemptions. It exempts employees who have not completed three years of service, employees under the age of 25, part-time employees, and employees not included in a collective agreement. 26 U.S.C. 105 (h).
- ¹⁴ Section 4.4.3 of California's State Child Health Plan under Title XXI of the Social Security Act.
- ¹⁵ ERISA is the federal Employee Retirement Income Security Act. Even though there is very little substantive regulation of health plans in ERISA, ERISA has a very broad preemption clause that prevents states from issuing any law that "relates to an employee benefit plan." ERISA contains one exception to this broad preemption; it permits the states to regulate the business of insurance, which includes health insurance purchased by an employer from an insurance company. Nevertheless, ERISA preempts states from regulating self-insured health insurance contracts. 29 U.S.C. section 1144 (a).
- ¹⁶ HCFA has also called on states pursuing employer subsidies to assess the cost effectiveness of their strategy by evaluating the level of substitution taking place. Health Care Financing Administration guidance dated February 13, 1998.

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