DO HEALTH INSURANCE REFORMS BOOST DEMAND FOR OLDER WORKERS BY SES?

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Introduction

Working longer is an effective way for individuals to improve their retirement security, but a critical question is whether employers will hire and retain them. This concern is especially acute for less-educated workers, who often hold middle-skill jobs that are at greater risk of disappearing.[1]

One potential way to boost the prospects of older workers is to reduce the cost to companies of employing them. For example, some policy experts have proposed making Medicare the primary payer for older workers' health care costs or eliminating their Social Security payroll taxes.[2] And European countries have tried wage subsidies.[3]

This *brief*, based on the results of a recent paper, considers a policy that has already been tried in the United States.[4] In the 1990s, nearly every state gradually imposed restrictions on how much employer-sponsored health insurance premiums can vary across small firms based on the characteristics of their workers. Prior to these regulations, a small firm that hired even one additional older worker ran the risk of higher premiums for all of its workers. The regulations made premiums less – or, in some states, not at all – dependent on the age or health composition of a firm's employee pool, thereby reducing the

cost of older workers. This *brief* examines whether the regulations improved labor market outcomes for older workers, by education, particularly at the small firms directly affected by the regulations.

The discussion proceeds as follows. The first section provides background on the premium restrictions. The second section describes the data and methodology used for the analysis. The third section presents the results. The final section concludes that while the earnings gap between workers in large and small firms did shrink, especially for workers with only a high school degree, the premium restrictions did little to increase employment for older workers.

Health Insurance Premium Regulations

While insurers are generally unable to vary employer-sponsored health insurance premiums among the workers at any single firm, premiums historically could vary substantially from firm to firm, with the highest premiums for companies employing older and less healthy workers. This pricing regime put small firms at a particular disadvantage. At a large

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employer, the cost of hiring an additional "high-risk" worker would be spread among many employees. But at a small firm, the cost of that high-risk worker would raise every worker's premium, burdening the employer and/or the other employees.

Following the recommendations of the National Association of Insurance Commissioners, states began to pass legislation in the early 1990s restricting the ability of health insurers in the small-group market, in which smaller employers bought coverage, to vary their premiums by the characteristics of the firms' employees. Between 1990 and 1994, 45 states passed some form of restriction on premium setting.

The degree of restriction varied across states and over time. Some states adopted "community rating" policies that prohibit insurers from varying premium costs for different firms due to their employees' characteristics. Only a few states passed "pure" community rating policies that forced insurers to charge every small employer in the state the same average per-enrollee cost. Most states with community rating adopted "modified" policies, which prohibit the use of underwriting based on health status but permit premium variation for other group characteristics such as age and gender.

Instead of community rating, the majority of states adopted rate-band policies, which allow the insurer to vary premiums within an acceptable range; for example, a rate-band ratio of 3:1 restricts the highest group premium to three times the rate of the least expensive policy. The rate-band ratios varied across states and were adjusted periodically by state legislatures, until the Affordable Care Act (ACA) standardized the difference between firms with older and younger employee pools at 3:1 starting in 2014.[5]

The state-by-state adoption of premium-setting restrictions provides a good setting for a natural experiment. Most previous analyses have focused on whether these regulations reduced health insurance coverage for younger, healthier workers.[6] The few studies that have examined their impact on labor market outcomes did not focus on older workers, who are most likely to be affected.[7]

Data and Methodology

The analysis uses data on individuals ages 25-61 from the *Current Population Survey* for 1989-2013. The outcomes of interest are: 1) an indicator for whether the individual is employed; 2) an indicator for whether

the worker is with a small firm (fewer than 100 workers);[8] and 3) real annual earnings. The data include other important personal characteristics, notably educational attainment, which is a proxy for socioeconomic status. The education measure is defined as less than high school, high school, some college, and college graduate. The results are presented separately by these categories.

The study also compiled a comprehensive dataset on small-group premium restrictions by state and over time. The variable of interest is the strength of a state's rate bands, which proscribe the maximum ratio of premiums for firms with unhealthy policyholders relative to firms with healthy policyholders. A rate-band ratio of 1 (1:1), i.e. community rating, is the most restrictive policy because premiums do not vary by the health composition of a firm's employees. A rate-band ratio of 0 indicates that the state has no rate band law, and is therefore the least restrictive. States with rate bands in between are assigned the reciprocal of their ratio; that is, a state where premiums can be 4 times higher in unhealthier firms (a 4:1 ratio) is given the value of 0.25.

No state had any restriction as of 1989, but the regulations came quickly thereafter: by 1991, 17 states had adopted some restriction. By 1995, 46 states had a restriction in place, and most were strong restrictions – that is, 1.86:1 or lower. Subsequently, some states relaxed their restrictions, though many strong regulations remained in place just before rate bands were standardized by the ACA (see Figure 1 for each state's status as of 2013).

FIGURE 1. PREMIUM RESTRICTIONS BY STATE, 2013

☐ Weak
■ Strong
■ Community rating
▨ Data not available
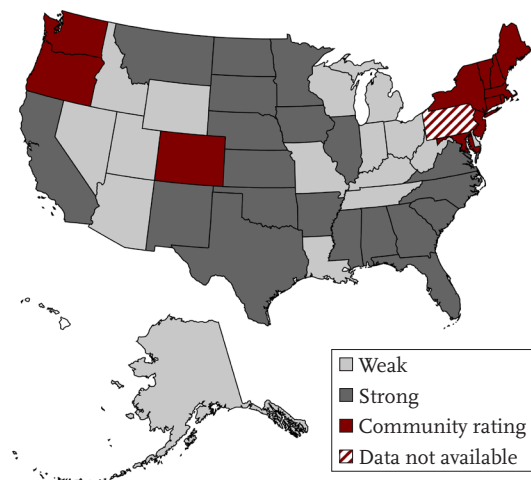
Source: Rutledge and Crawford (2016).

The analysis estimates regressions for each labor market outcome as a function of the rate-band ratio, an indicator for workers ages 50 or older, and the interaction of these two variables. The earnings regression also includes interactions with a "small firm" indicator. Finally, each model controls for standard personal demographic characteristics, the state unemployment rate in the given year, and state and year fixed effects.

Results

By reducing the cost of providing health insurance for older workers, the premium restrictions were expected to increase their employment at the small firms affected by the law. In addition, the restrictions were also expected to increase older workers' earnings at small firms, because lower health premiums could allow employers to pass on the savings to workers in the form of higher wages.[9] The restrictions were not expected to increase employment or earnings in larger firms, whose insurance premiums were not affected by the regulations.

Employment

Figure 2 shows the employment rate by rate band strength, age, and firm size, as predicted from the regression estimates.[10] The red portion of the bars

FIGURE 2. PREDICTED EMPLOYMENT RATE BY RATE BAND STRENGTH, AGE, AND FIRM SIZE

Note: "Community rating" refers to a 1:1 rate-band ratio, "Strong" ratios are between 1.2:1 and 1.67:1, and "Weak" ratios are between 1.86:1 and 4:1.
Source: Authors' estimates from the U.S. Census Bureau, *Current Population Survey* (CPS), 1989-2013.

represents the predicted probability of working in a small firm. The gray portion is the predicted probability of working in a large firm; though this outcome is not expected to be influenced by the premium restrictions, it helps to establish whether large-firm employment was changing at the same time for older workers (ages 50-61) vs. prime-age workers (ages 25-49). The full height of each bar is the predicted probability of being employed overall.

Contrary to the expectation that small-firm employment would increase, all employment rates – both overall and in small firms – look virtually the same, no matter the strength of the premium restriction. The left panel of Figure 2 indicates that the overall employment rate (as predicted from the regression results) for older individuals barely increases as the strength of the premium restrictions increases: from 69 percent with no rate band to 72 percent with community rating. Small-firm employment among individuals 50 and older increases by even less. Prime-age individuals effectively saw no change in small-firm employment or overall employment, which means that older workers did not see any *relative* increase either. Thus, the reforms did not appear to improve older workers' prospects of being employed at all, even at the small firms that would be most concerned about how expensive these workers are to insure.

Earnings

Unlike employment, both prime-age and older workers – especially those in small firms – do appear to be paid more in states with stronger premium restrictions (see Figure 3 on the next page). But, contrary to expectations, older workers do not appear to benefit much more than prime-age workers.

In general, workers at large firms earn more on average than workers at small firms, and the gap is especially large for older workers. But the premium regulations made older workers, in concept, more attractive to small firms, who could then afford to offer them higher wages. Indeed, the results indicate that the gap between earnings at large and small firms closes by more in states with stricter premium restrictions. In states with no premium restrictions, workers ages 50-61 earn about $13,400 less in small firms than in large firms. That difference falls steadily as insurance premiums become more restricted; in states with community rating, the large-small firm earnings gap is only $9,980, 26 percent less than in unrestricted states.
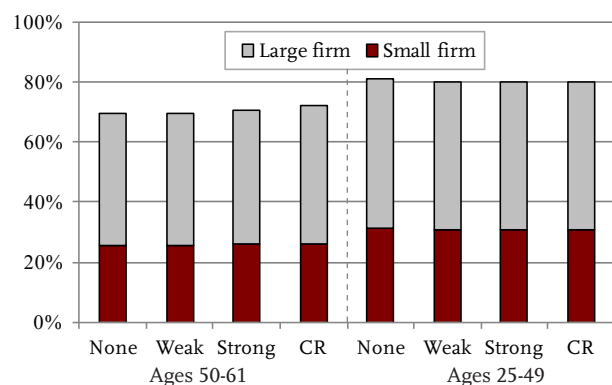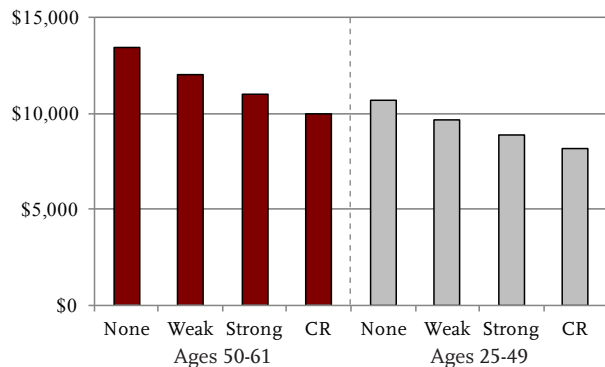
FIGURE 3. PREDICTED GAP BETWEEN AVERAGE LARGE AND SMALL FIRM EARNINGS, BY RATE-BAND STRENGTH AND WORKER AGE, IN 2013 DOLLARS

Note: "Community rating" refers to a 1:1 rate-band ratio, "Strong" ratios are between 1.2:1 and 1.67:1, and "Weak" ratios are between 1.86:1 and 4:1.
Source: Authors' estimates from the 1989-2013 CPS.

The large-small firm earnings gap also falls for prime-age workers, however: from $10,670 with no premium restrictions to $8,150 with community rating. Because the initial gap is smaller for prime-age workers in all rate-band categories, the percentage change – 23 percent – is almost equal to the one seen by older workers, and the difference in the policy's ef-

fect between the two age groups is not statistically significant. The fact that prime-age workers – whose job prospects at small firms were less likely to have been reduced by concerns about their effect on the firms' health insurance costs – also benefited may indicate that firms decided to use any savings from older workers' lower health premiums to raise salaries for *all* of their employees. But it may also indicate that small-firm earnings increased in stricter-regulated states for other reasons.

Results by Education

The results in Figure 4 indicate that the socioeconomic group that most benefits from premium-setting restrictions is high school graduates. Older high school graduates working in small firms see a statistically significant increase in their earnings (6.1 percent), all else equal, when their state moves from no rate band restriction to (pure or modified) community rating. Individuals with college experience also see increasing earnings – though of a lesser magnitude and statistically insignificant – when community rating is adopted.

Otherwise, the results do not provide much evidence that the policies were effective. No group saw the expected improvement in small-firm employment. High school dropouts actually saw the earnings gap between large- and small-firm workers increase,

FIGURE 4. ESTIMATED EFFECT OF ADOPTING COMMUNITY RATING ON LABOR MARKET OUTCOMES FOR INDIVIDUALS AGES 50-61, BY EDUCATION
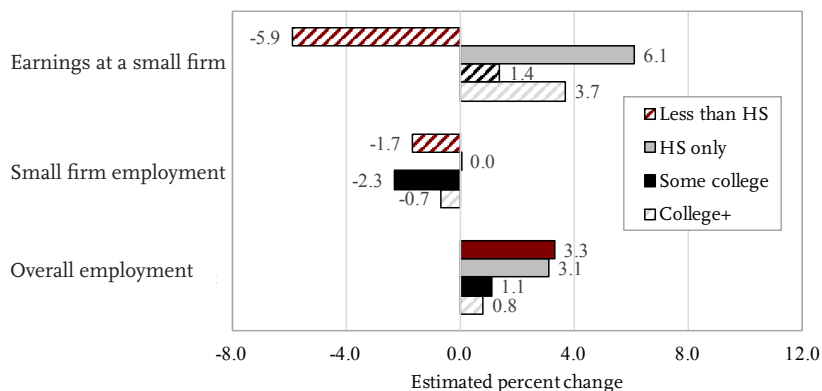
Note: Solid bars are statistically significant at least at the 10-percent level.
Source: Authors' estimates from the 1989-2013 CPS.

contrary to expectations. College graduates had no statistically significant change in employment or the earnings gap.

Conclusion

The labor supply of older workers is increasing, but they cannot work longer if jobs are not available to them. Tighter regulation of health insurance premiums for less healthy workers in the small-group market should have benefited older workers, allowing them greater employment opportunities in small firms, but the small-firm employment increase was minuscule. The earnings gap between large and small firms did shrink in states with stronger premium restrictions, but older workers did not see greater increases than younger workers, who stood to benefit, at most, indirectly. The earnings gap shrunk the most for high school graduates, but no education group saw statistically significant increases in small-firm employment.

These results suggest that indirectly reducing the cost of hiring older workers – by restricting their health insurance premiums – does not improve the labor market outcomes of any socioeconomic group. Instead, policymakers may want to consider trying more direct measures, perhaps by eliminating payroll taxes for older workers and their employers.

Endnotes

1 Autor (2014).

2 Goda, Shoven, and Slavov (2007, 2009).

3 The results of the subsidy policies have been mixed; see Huttunen, Pirttilä, and Uusitalo (2010); Boockmann et al. (2007); Schunemann, Lechner, and Wunsch (2011); Garcia-Perez and Sanz (2009); and Eppel and Mahringer (2012).

4 Rutledge and Crawford (2016).

5 The American Health Care Act of 2017, proposed by Republicans in the House of Representatives, would raise this ratio to 5:1.

6 Buchmueller and DiNardo (2002) and Adams (2007) find some evidence of adverse selection because the policies forced insurers to charge more to younger, healthier workers, which made insurance less attractive to this group.

7 Kapur (2003, 2004); Kaestner and Simon (2002).

8 Though most premium restrictions define the small-group market as applying to firms with 50 employees or fewer, the data do not allow for identifying firms of that size consistently over time.

9 Younger workers who were unhealthy could also benefit, but the data lack health status information until 1995, by which time most states had already adopted the premium restrictions.

10 The estimates are from a multinomial logit regression, where the outcomes are: 1) working at a large firm (the base outcome); 2) working at a small firm; and 3) not working. Results are similar in individual regressions examining employment (vs. not working) or small firm employment (vs. large firm employment).

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