



Health Care Reform

LEGISLATIVE BRIEF

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Tobacco Use Surcharge in 2014

Effective for 2014, the Affordable Care Act (ACA) allows health insurance issuers in the individual and small group markets to impose a tobacco use surcharge, within a ratio of 1.5 to 1. This means that, beginning in 2014, health insurance issuers in the individual and small group markets may vary insurance premiums based on a policyholder (or dependent's) tobacco use, up to 1.5 times the regular premium. In addition, issuers of qualified health plans (QHPs) offered through an Exchange may also impose up to a 1.5:1 tobacco use surcharge.

The tobacco use surcharge is part of the ACA's premium rating restrictions that apply for health insurance issuers in the individual and small group markets. The ACA's rating restrictions do not apply to grandfathered plans, large group plans or self-funded plans.

On Feb. 22, 2013, the Department of Health and Human Services (HHS) issued a [final rule](#) to implement the ACA's rating restrictions for health insurance premiums. The guidance in the final rule is effective for 2014 plan (or policy) years.

OVERVIEW OF THE TOBACCO USE SURCHARGE

A tobacco use surcharge is a variation in insurance premiums based on a policyholder's (or dependent's) tobacco use. Under the ACA, the premium rate charged by an issuer for non-grandfathered health insurance coverage offered in the individual or small group market may vary for tobacco use. However, the ACA limits this variation by not allowing insurance companies to charge those who use tobacco products more than 1.5 times the non-tobacco user's rate.

States have the option of reducing or eliminating the tobacco surcharge altogether. However, states that wished to establish tobacco rating bands more protective than the federal requirements were required to report this decision to HHS by March 29, 2013.

Issuers in the small group market may apply the tobacco rating factor only in connection with a wellness program that allows a tobacco user to avoid paying the full amount of the tobacco factor by participating in a tobacco cessation program. Additionally, the federally facilitated SHOP Exchanges (the Exchanges for small businesses) will not impose the tobacco surcharge at the time of initial enrollment (or re-enrollment) if the employee or dependent agrees to participate in a wellness program meeting specific standards, such as a tobacco cessation program.

Who Does the Tobacco Use Surcharge Apply To?

The final rule clarifies that issuers may vary rates for tobacco only based on individuals who may legally use tobacco under federal and state law. Thus, the tobacco surcharge does not apply to persons under 18 years of age. However, tobacco rating may vary by age (for example, lower tobacco use factor for younger individuals).

If a policyholder begins smoking after purchasing the policy, he or she would be subject to the tobacco surcharge when renewing the plan the following year. In contrast, if the policyholder successfully quits smoking after purchasing the policy, the insurance issuer is not required to lower the premium until renewal the following year.

Assuming coverage is purchased in a state that allows the tobacco surcharge, an insurer can adjust the premiums of health plans sold to small businesses based on the number of workers who use tobacco.

Tobacco Use Surcharge in 2014

If an enrollee provides false or incorrect information about his or her tobacco use, the final rule allows an issuer to retroactively apply the appropriate tobacco use rating factor to the enrollee's premium. However, the issuer may not rescind the coverage.

Definition of "Tobacco Use"

The final rule defines "tobacco use" as use of tobacco an average of four or more times per week within no longer than the past six months, including all tobacco products but excluding religious and ceremonial uses of tobacco. Tobacco use will be based on when a tobacco product was last used.

States can enact more consumer-protective definitions or look-back periods, or reduce or eliminate the tobacco surcharge altogether.

How Will the Tobacco Use Surcharge Be Applied?

The ACA requires any rating variation for tobacco use to be applied based on the portion of the premium attributed to the individual family member.

In the final rule, HHS directs issuers to use the per-member rating methodology in the small group market. According to HHS, per-member rating ensures compliance with the requirement that tobacco rating only be apportioned to an individual family member's premium, enhances employee choice inside the SHOP Exchanges and promotes the accuracy of the ACA's risk adjustment methodology.

States may require issuers to offer premiums based on average employee amounts where every employee in the group is charged the same premium. Also, according to HHS, the age bands, as implemented by the per-member-rating methodology, are consistent with the Age Discrimination in Employment Act of 1967 (or the ADEA).

Effect on Affordability for Purposes of the Individual Mandate

If the cost of health insurance, taking into account both a premium tax credit and the tobacco surcharge, exceeds 8 percent of an individual's household income, he or she will not be subject to an individual mandate penalty for failing to obtain insurance.

STATE LAWS

The health insurance market is mainly regulated at the state level. Each state may have its own laws to regulate how issuers set their premiums, and these laws can vary widely by state and by insurance market. The ACA's rating restrictions create minimum federal standards for varying rates in the individual and small group markets. In addition to the ACA, issuers will be required to comply with state laws that impose stricter rating standards.

TOBACCO USE SURCHARGE IN EXCHANGES

The ACA also includes a 50 percent allowable tobacco surcharge for qualified health plans sold through an Exchange. However, states can further limit or prohibit insurers from applying a tobacco surcharge.

The tobacco surcharge is not covered by premium tax credits. This means that, if an individual qualifies for a premium tax credit, the tax credit amount will be based on the premium before the tobacco surcharge is applied. As a result, individuals who use tobacco will be required to pay the full cost of the surcharge.