



Testimony of Covered California Executive Director Peter V. Lee
To the Joint Hearing of the Senate and Assembly Committees on Health
Assessing the Operational Impacts of the Insurance Rate Public Justification and
Accountability Act

July 2, 2014

Introduction:

Senator Hernandez, Assemblymember Pan and Members –

Covered California has been working on an analysis of the potential operational impacts of the Insurance Rate Public Justification and Accountability Act to help us prepare if it is enacted and to inform the public of its potential impacts on us. We welcome this opportunity to share some of our initial thoughts on the proposal.

To begin this review, we developed an outline of potential operational issues and questions that we posted on our website and presented to our board last month along with a request for public comment. We've also had discussions with Department of Managed Health Care, Consumer Watchdog, Health Access, the California Association of Health Plans, as well as individuals with expertise in various aspects of the issue.

In late May, we reached out to the Department of Insurance to schedule a meeting to discuss the implementation issues. We are now scheduled to meet on July 17th, the earliest date the Department of Insurance is available.

We are continuing our work to develop a more comprehensive analysis of the initiative and this hearing will help inform our ongoing analysis.

At the outset of my testimony, I would note three things.

First, the scope of our analysis is limited: Covered California is not assessing the potential public policy implications – positive or negative – of the initiative. Rather, we are focused solely on how it will impact what we do, and how it will affect our role in implementing the Affordable Care Act in California.

Second, we are not experts about how Proposition 103 has been implemented for property and casualty insurance. What we do know is that the health insurance marketplace is different. For example, in property and casualty insurance, there is no Open Enrollment period; no one-year rate lock for offered products in that year; no federal subsidies; and no exchange to negotiate the best value on behalf of consumers.

We also understand that the proposal for rate regulation in California with its processes for third party intervention and judicial review is different than that of other states that have implemented prior approval for rates in concert with the Affordable Care Act.

Third, there are many uncertainties as to how the initiative would be implemented – as there always are in any new proposal. We are doing our best to better understand how it would work, and how it could affect our operations.

Covered California's Role in the New Marketplace

In 2010, the passage of the Affordable Care Act and California's legislation to implement it here fundamentally changed the way health insurance is sold in the individual and small group markets. We now have a marketplace that is governed by new rules intended to protect consumers. This includes requirements for guaranteed issue so insurers cannot deny coverage for someone with a pre-existing condition along with a three month open enrollment period; Medical Loss Ratio standards that cap how much insurers spend on non-medical costs; dual oversight process with the DMHC and Department of Insurance that includes a rate review process for those insurers each regulator oversees; federal premium assistance to help make coverage and cost sharing more affordable for low income individuals and the expansion of Medi-Cal; standardized benefits so consumers can compare products on an "apples to apples" basis; and risk adjustment & reinsurance policies to protect the risk pool of health plans that enroll more than their proportional share of sicker, more costly enrollees.

Covered California - California's Exchange – is also something that's new, and it's at the center of the insurance marketplace. What makes Covered California particularly unique is the authority to be an active purchaser – a responsibility that very few Exchanges throughout the country have. As an active purchaser and negotiator, our mission is to obtain the best value for our consumers.

Affordability and lower rates are a critical priority, but our objective as an active purchaser goes beyond rates. We look at a portfolio of attributes that make the new marketplace work for consumers. This includes consideration of federal subsidies; having a range of competitive plan choices in every region of the state; establishing standardized benefits and cost sharing to consumers in Covered California AND in the individual market outside of Covered California's exchange. As an active purchaser, we are able to standardize benefits and cost sharing; assure a choice of plans and appropriate provider networks; and support a longer term, so-called "triple aim" strategy to contain costs, improve quality and population health outcomes.

To operationalize these objectives, specific timelines must be met to allow health insurance products to be offered when open enrollment begins. For 2015, the plan year begins on January 1, but open enrollment begins this fall – on November 15, 2014 and ends on February 15, 2015. By this September, health plan rates need to be locked in for the full year as required by state and federal law. The process for getting ready is complex and requires considerable planning. For example: Plans need to be reviewed

and certified, rates must be approved, data must be loaded and formatted into the California Health Eligibility, Enrollment and Retention System (CalHEERS), marketing materials need to be developed, and our sales force – thousands of agents and enrollment counselors and staff - need to be trained. Once a rate is locked in for the benefit year, it cannot be changed or adjusted until the following open enrollment period.

In looking back over the past 12 months, we are proud of what we have accomplished. We have worked with thousands of Californians across that state to enroll over 1 million Californians in competitive, affordable plans through Covered California and many more who are insured because of our state's expansion of Medi-Cal. We have a strong foundation to build on for the future. Based on our experience and preliminary analysis, we can share some insight as to how the initiative might affect our operations and the consumers we serve.

Potential of the Initiative to Have Significant Impact to Covered California

Based on our preliminary review and discussion with a range of stakeholders, we think that there would likely not be immediate impacts on Covered California for the 2015 year. This assuming the initiative would not apply to rates already submitted to the regulators for the 2015 plan year, although, under the initiative, plans may be subject to subsequent judicial review of rates, not only for 2015, but back as early as 2012. If a health plan's rates were found to be excessive, the insurer could be ordered to rebate the difference.

The areas in which there may be significant potential impacts to Covered California and the consumers we serve are in the following four areas:

1) Covered California's Role as an Active Purchaser Could Be Undermined.

Covered California's ability to negotiate with health plans to achieve its "triple aim" objectives could be undermined to the extent insurers believe Department of Insurance would "second-guess" the rate they negotiated with Covered California. Rates are important – but in our role at Covered California as an active purchaser, we seek to consider more. According to Consumer Watchdog, the initiative proponent, rates would be the only factor subject to change under the new rate regulation process. However, a review that looked only at rates could give less weight to considerations of quality and improved health outcomes, key elements of Covered California's approach to achieving better quality, better health outcomes, and lower cost. These are also elements that are central to the broader oversight and monitoring functions of Department of Managed Health Care and California Department of Insurance as insurance regulators. To the extent the new rate review process overlays a primary focus on rates, it may fail to include broader factors that have been negotiated by Covered California and reflected in the proposed rate. For example, provider

networks and rates are interconnected in negotiations with health plan. If the proposed ballot initiative were to pass, it is unclear how a health plan would treat a demand by Covered California to expand a network's offerings when the issuer knows that its rates may yet be determined by a subsequent negotiation with the Department of Insurance, a possible intervenor or the prospect of a third-party seeking judicial review.

Part of this concern comes from what we believe to be uncertainty about the scope of the initiative. We are advised by the initiative's proponents that it is focused primarily on rates. But as drafted, rates are defined very broadly to include "anything that affects charges including benefits, premiums, base rates, underwriting relativities, premium financing, co-pays deductibles." Given that rates are the product of a range of factors, including networks, utilization review processes, quality initiatives and others – it is hard to see how regulation of rates would not (1) create an opportunity for those who disagree with Covered California's active purchasing role to use regulatory and judicial processes to challenge rates under the broad definition; or (2) lead to timing challenges if the Department of Managed Health Care must re-review licensure, benefit design and other elements that are changed through negotiations with the Department of Insurance.

- 2) **Timing & Process of Review Could Impact Availability of Plans for Open Enrollment.** Prop 103 rate approval timelines as now practiced in property and casualty insurance settings would not work in the health insurance marketplace. This is because the time to approval can take too long – especially if there is an intervenor challenge. If a proposed rate increase is over 7%, an intervenor would be entitled to a mandatory hearing and possible judicial review. We now have a 60 day window for rate review – and we might be able to buy a little more time for rate review on the back end if we start our plan certification process a little sooner. But the time tables for public hearings along with the intervenor processes could take much longer for resolution – up to 180 days or more after the filing of a rate change application with California Department of Insurance. That could leave rates in a state of limbo where the rate isn't approved and can't be used for open enrollment.

We have been told that regulations could be enacted to dramatically abbreviate the Prop 103 calendar so that a decision would be reached to meet Covered California's deadlines. However, any regulations would still need to comply with state law and federal requirements. Specifically, timelines that would be largely consistent with those that exist could be met by the following paths:

- (1) The Department of Insurance could find rates that are less than 7% acceptable;
- (2) The Department of Insurance could reject a proposed rate and allow the health plan to sell its product at the prior year rate – with no adjustment;

- (3) The Department of Insurance could negotiate a rate increase below the 7% threshold; or
- (4) If the proposed rate increase exceeds 7% and a member of the public intervenes, the intervenor would be entitled to a mandatory hearing. If the hearing upholds the rate increase and the intervenor seeks judicial review, it is possible that the new rate could still be offered while the judicial process continues with the potential of a plan being required to rebate any amounts found to be excessive by the court.

Based on past history, health insurance rate increases have frequently exceeded the 7% threshold.

Assuming that the Department of Insurance institutes a rate regulation process that provides for finality of rates in time to put insurance products on the market for open enrollment, the impact of any third-party intervening and seeking judicial review is a potential wild card that requires additional review. In addition, the timing of subsequent regulatory review on the part of Department of Managed Health Care to the extent there are changes in a plans operations beyond its rates requires further review.

3) If a plan's rate increase is rejected, but the plan STAYS in the market, there could be impacts on consumers based on changes to federal subsidies.

For almost 90% of those who enroll through Covered California, their "insurance premium" is the product of both the premium and the amount they receive as a federal subsidy through the "Advanced Premium Tax Credit."

In the event that a carrier has its proposed premium increase rejected and the plan accepts a default rate (same as prior year's rate or negotiated to be less than the 7% hearing and judicial review threshold), the impact on an individual consumer depends on the plan chosen by that consumer and the price position of that plan relative to other plans in that rating region. For example: a lower rate could be good news for a consumer in a plan that had a small or no rate increase. But the impact on consumers in other plans in that region is more complicated to assess. For example, if a hypothetical plan's new rate set a lower floor, there's the risk that federal subsidies would slide downward, diminishing the purchasing power of low income consumers as their tax credit dropped. How much of a reduction in the tax credit consumers would face would depend on: (1) the relative price position of the carriers in that market; (2) what plan and product a consumer had selected; and (3) that consumer's income and eligibility for the tax subsidy.

While the tax subsidy could be reduced based on lower than anticipated rates, consumers can always change plans during open enrollment to avail themselves of a lower cost plan. This change, however, could have the effect of increased

movement and confusion of consumers; some consumers paying more to remain in the plans they'd chosen previously; and more volatility of prices among plans.

4) **Risk of Withdrawal of a Plan.** If an adequate rate is not approved for that year, a health plan could decide to withdraw from the market. The business decision to withdraw could potentially be for a particular region or from the individual market entirely. While we cannot predict the likelihood of plans withdrawing from all or part of the market, this is a real potential impact:

- For smaller, regional health plans, their capacity to absorb losses over a year may be limited as is their willingness to accept too much risk and uncertainty.
- Larger plans may have greater capacity to tolerate short term losses, but could decide to withdraw from certain higher cost regions.
- In either case, given the Medical Loss Ratio rules, plans would have very limited ability to "make up" losses incurred in future years.

The impact of a withdrawal would depend on the plan or plans that withdrew, but would affect consumers' choice of plans and could result in consumers facing the need to change providers.

Conclusion

Covered California is proud of what we've accomplished as part of the broad fabric of elements of the Affordable Care Act that have expanded health insurance coverage and implemented an array of new rules and processes on the health insurance market.

The proposed Rate Regulation Act would put into play a new set of processes that would have a range of potential impacts on Covered California and the consumers we serve. The scope and nature of those impacts is difficult to define and in many ways the only thing we can be sure of is the uncertainty of the ultimate effects on the products consumers will have available to them, the potential impacts on tax subsidies, and on how insurers are regulated, monitored and overseen in the emerging era of the Affordable Care Act.

We look forward to gaining greater clarity on the potential impacts of the Act and, if enacted, assuring it would be implemented in ways that would as much as possible complement Covered California's role as an active purchaser on behalf of California's consumers.