



**Covered California Analysis of the Insurance Rate Public
Justification & Accountability Act
Proposition 45**

**Presentation by
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The following document summarizes the analysis by Covered California of the Insurance Rate Public Justification and Accountability Act (Proposition 45) presented at the August 21, 2014 meeting of the Covered California Board of Directors.

Overview:

Proposition 45 could have a significant detrimental impact on Covered California's operations, based on a plain reading of the Act, its broad definition of "rates," and the rights of intervenors as implemented under Proposition 103. The scope and nature of these impacts – either mitigating the potential harms or making them worse – are subject to the interpretation and implementation of the Act by an elected Commissioner and potentially the courts.

Context and Process:

As part of its responsibility to inform the Board and the public of the potential impact of Proposition 45 on its operations, and to respond to requests from the legislature, Covered California conducted an analysis of Proposition 45.

A list of initial questions related to Proposition 45 was presented to the Board and to the public at the June 19, 2014 Board meeting in order to identify the scope of the analysis. These questions focused on operational impacts, not on the policy merits of Proposition 45 or rate regulation generally. Subsequently, Covered California's Executive Director testified at a joint legislative hearing of the Senate Health Committee and the Assembly Health Committee, indicating tentative areas of uncertainty and possible concerns based on a preliminary analysis of the initiative.

Meetings Held and Feedback Received: In the course of conducting its analysis, staff met with the following entities:

- Insurance Commissioner
- Department of Managed Health Care
- Consumer Watchdog (proponents)
- California Association of Health Plans
- Health Access and other consumer advocates

In addition to these meetings, staff reviewed the testimony of the Insurance Commissioner, the Department of Managed Health Care, and others who testified or provided material at the July 2, 2014 joint legislative hearing. Covered California also received detailed responses from the Insurance Commissioner that responded to both the initial questions outlined on June 19th and the follow-up questions which arose after meeting with the Commissioner. In addition, Covered California reviewed 6 written comments received from the public at large, as well as testimony provided during public comment at Board meetings. Input from these meetings, and other communications, comments and materials, along with independent research, have all informed Covered California staff of the potential impacts of Proposition 45 on Covered California and the continued uncertainty regarding how the Act may be implemented. The testimony provided at the joint legislative hearing, and the letters and written material provided to Covered California were posted with the Covered California board meeting material on August 21, 2014.

Summary of Proposition 45 Key Elements:

Prior Approval: Under Proposition 45, all health filings in the individual or small group markets would be subject to approval under the Proposition 103 framework (specifically, Cal. Insurance Code §§ 1861.03(a) and (b) and 1861.04 through 1861.14). The Proposition 103 statutory framework includes the requirement for rates to receive prior approval by the Commissioner before a rate can take effect: “No rate shall be approved or remain in effect which is excessive, inadequate, unfairly discriminatory, or otherwise in violation of this chapter.” *Cal. Insurance Code § 1861.05(a)*. Additionally, the initiative applies to all rates proposed or in effect as of November 6, 2012, with transitional period for rates in effect on January 1, 2014.

Review by Two Regulators: Proposition 45 (and the requirement for prior approval) applies to all individual and small group health filings in California, regardless of whether the carrier or its insurance product is otherwise regulated by the Department of Managed Health Care (DMHC). Thus, for plans also under DMHC jurisdiction and subject both to rate review (without the authority to order new rates) as well as an array of other regulatory approvals before a product can be offered in the market, the proposed ballot initiative would require review by two regulators.

Definition of Rates: The proposed ballot initiative defines “rates” to include: “[B]enefits, premiums, [...] co-payments, coinsurance, deductibles, [...] and any other out of pocket costs of the policyholder.” *Initiative proposed Cal. Insurance Code § 1861.17(g)(2)*.

Hearings & Public Participation by Intervenors: Proposition 45 would apply the Proposition 103 statutory framework for rate review hearings. Under Cal. Insurance Code § 1861.05(c), for any rate change application over 7%, the Commissioner must hold hearing upon timely request by intervenor, subject to due process requirements.

Analysis:

Covered California has assessed the implications of the Proposition 45 (the “Act”) as drafted on our operations – with consolidation of rate regulation under one of two regulators, an intervenor process and building on the Proposition 103 structure – not how rate regulation under other proposals could impact Covered California’s goals and approach as an active purchaser.

Following the feedback received and research conducted, Covered California focused its analysis on five key aspects of potential impact on Covered California in the

implementation of Proposition 45: 1) Covered California's role as an active purchaser; 2) Timeline for open enrollment with potential intervenors and review by two regulators; 3) Risk of withdrawal of a plan; 4) Effect on plans in 2015; and 5) Impact to federal subsidies for consumers.

What follows is a summary of Covered California's analysis for each area.

1) *Covered California's Role as an Active Purchaser:*

Covered California seeks to negotiate with health plans to achieve our "triple aim" strategy to lower costs, improve quality, and improve health outcomes, while assuring a good choice of plans for consumers. The plain language of the Act provides for a very broad interpretation of the factors that could be considered as part of rate regulation, including "anything that affects the charges associated with health insurance." How networks, broader quality improvements, and other factors would be considered by CDI would be subject to the department's regulations and potentially judicial interpretation. Covered California's role as an active purchaser could be significantly undermined if health plans negotiating with Covered California are reluctant to consider or negotiate on factors other than price because of uncertainty about the subsequent price that will be approved (or ordered) by CDI.

2) *Timeline for Open Enrollment with Potential Intervenors and Review by Two Regulators:*

Timelines for final decision on rates under the initiative depend largely on the regulations CDI would issue and the interaction between CDI and DMHC. If for any reason a new rate were not approved in time for open enrollment, plans would "default" to the old rate for the entire next year. A timely completed review is essential to ensure that plans can rely on their new rates for the annual open enrollment period and the subsequent plan year.

In assessing the likely impact of Proposition 45 to the timely approval of rates, staff have identified some critical uncertainties:

- a. Regulations to determine review and hearing processes would need to be established. Current timelines under Proposition 103 would provide significant disruption to the offering of plans for the annual open enrollment. While CDI has noted that it could either establish timelines or Covered California could require submission of rates at "whatever time is required" to meet deadlines, it has not elaborated on how that would be accomplished consistent with the due process requirements of the Administrative Procedures Act (which require formal hearing process rights for intervenors).

- b. Furthermore, it is uncertain how future Commissioners might impose different timelines and it is unclear to what extent DMHC reviews could occur concurrent to CDI's review, or would need to wait until after CDI's processes are completed. This is particularly important where CDI's review would lead to changes by the plan of core elements required for DMHC's regulatory oversight (e.g., network adequacy, benefit designs).

3) *Risk of Withdrawal of a Plan:*

One risk that Covered California needs to be concerned about is the potential of health plans withdrawing in advance of or during the rate regulation process. The risk of plan withdrawal is uncertain. CDI has stated an intent to only order a rate that is both "not excessive" and also "adequate," which should mean that carriers would not face dramatic losses based on regulated rate reductions. How plans might respond to rate regulation in the individual market, however, remains uncertain. To the extent a mandatory intervenor hearing process is unresolved in time to meet the open enrollment deadline, a plan's proposed rate could not go forward. In addition, to the extent a the rate ordered by CDI was considered "too low" by a plan, a plan might evaluate potential losses and consider mitigation strategies that could include withdrawal from some or all rating regions in the individual market.

4) *Effect on Plans in 2015:*

Under the Act, CDI has the ability to conduct retrospective review of rates on all plans from 2012 through 2015. In the event there is a rate regulation finding that the rate was too high, plans could be required to pay rebates to the affected consumers. Rate changes filed for 2015 would be "deemed approved" because the rates for 2015 would have been filed more than 60 days prior to enactment of the Act.

5) *Impact to Federal Subsidies for Consumers:*

Almost 90% of Covered California's consumers receive federal subsidies to reduce their net premiums. The amount of the tax credits and the resulting net price to the consumer is based on the relationship between plan prices in a given region. The impact of a rate regulation action lowering or raising rates would have a direct effect on the consumer enrolled in that plan – having their rate increased or decreased. For consumers in other plans, if the rate change sets a new "second lowest silver" plan, some consumers could see their costs increase due to the adjustment of the prices used for the tax credit calculation and the potential reduction of the purchasing power of the tax credits. While these impacts are possible and could be disruptive relative to Covered California's marketing and operations, they are not different in kind from what can and does

happen when plans bid rates that change their price position relative to other plans in a given region.

In summary, at this time, based on a plain reading of the Act, its broad definition of “rates,” and the rights of intervenors as implemented under Proposition 103, there could be significant detrimental impact on Covered California’s operations. The scope and nature of these impacts – either mitigating the potential harms or making them worse – are subject to the interpretation and implementation of the Act by an elected Commissioner and potentially the courts. The potential impact of the Act on Covered California are significant, but the scope and shape of those impacts are and will be uncertain.