THE FOUNDATION FOR TAXPAYER AND CONSUMER RIGHTS

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Thursday, January 10, 2007

Senator Sheila Kuehl
Chair, Senate Health Committee
State Capitol, Room 5108
Sacramento, CA 95814

RE: ABX1 1 – Oppose Mandatory Purchase of Private Health Insurance

We write to urge you and the Senate Health Committee to amend ABX1 1 to remove the mandatory purchase of private health insurance. The solution to the health care crisis is not to require Californians to buy private insurance policies they cannot afford and that provide no guarantee of coverage.

Speaker Núñez previously acknowledged the need for affordability protections in a mandatory purchase regime. Mr. Núñez pledged to put a limit on deductibles and co-pays and promised to exempt individuals from the mandate who would pay more the 6.5% of their annual income on health care costs, including insurance premiums and out-of-pocket costs.

But as you pointed out in your December 18 essay, under the current version of ABX1 1 even that protection has been discarded. There are no caps on premiums, no maximum deductibles, and no floor on benefits to protect consumers from being forced to buy bare-bones junk insurance that they cannot afford to use when they do fall ill.

A blanket 6.5% exemption has been replaced by an undefined "hardship" exemption to be determined on a case-by-case basis. The best that patients can hope for from such an exemption, if one is provided, is that they will be left uninsured. The inevitable delays and high cost to the state of making individual determinations are not addressed in ABX1 1.

Proponents argue that a provision in ABX1 1 to cap insurer overhead and profit at 15% will control costs. But absent regulation of premiums and out-of-pocket costs, this provision will actually drive up rates rather than control them. Insurers allowed to keep 15% of premiums will have incentives to pay providers more, and charge more, in order to keep more. See below.

Massachusetts' real-world experience offers the most striking indicator of what may happen in California. Proponents of the Massachusetts plan, including Jonathan Gruber of MIT (who also prepared the fiscal analysis for ABX1 1 and its precursors) predicted that comprehensive health insurance under Massachusetts reforms would cost about $200 a month,[1] but for many the cost is more than twice that amount. Insurers in Massachusetts have signaled their intention to seek double-digit price increases next year, though the state is asking for voluntary reductions.

[1] Julie Appleby, "Mass. residents face required coverage," *USA Today*. April 4, 2006.

The following points illustrate the deep faults of mandatory individual insurance purchase.

In general:

- Under ABX1 1 an employer must spend from 1% to 6.5% of payroll to buy insurance for employees. For large employers, 6.5% is about half their current health insurance spending. If the employer does not wish to continue offering insurance, the company may pay the same amount into a state fund, and employees would have to buy their insurance through the state fund with no cap on premiums and no floor on coverage. Unless the employer supplemented the mandatory 6.5% of payroll fee for employee insurance, the state pool would offer only a 20% premium price reduction to these supposedly "covered" employees. Given this, a family of four earning $85,000 per year (above 400% of poverty and thus ineligible for tax subsidies) that currently receives coverage from an employer may well see existing coverage exchanged for pool coverage that offers fewer benefits at a higher cost. With the cost of family health coverage through employers now averaging more than $12,000 a year, this could *increase* the family's share by $6,000 or more, on top of its current cost share. Self-employed individuals earning over 400% of poverty would have to pay full price for coverage. All individuals and families would bear the cost of future insurance premium increases while employers would be insulated from higher costs with a hard cap on what they must spend on health care.

- The proposed tax credits for families making from 250% to 400% of the poverty level are entirely insufficient to close the cost gap for those who must purchase their own insurance. This insufficiency would worsen every year because the tax credit would adjust only to the overall rate of inflation in California, while insurance premiums rise two to three times faster than the overall inflation rate each year.

    - Tax deductions are only provided if health care *premium* costs exceed 5.5% of income. No tax credit, nor *any other affordability protection*, would be available to the many consumers whose premium and out-of-pocket costs – deductibles and copays – together exceed 5.5% of income. It is unhelpful to have a tax credit for premiums if a patient cannot afford to go to the doctor because she cannot pay the deductible.

    - Year-end tax credits do not help patients afford monthly premiums when they are due. Each month, ABX1 1 will force many Californians into difficult choices between paying mortgages and buying coverage.

    - The tax credits are only available to people purchasing through the MRMIB pool. This limitation discriminates against those employed by small businesses ineligible to buy into MRMIB.

- The Foundation for Taxpayer and Consumer Rights supports the use of subsidies to provide access to health care for those who cannot afford coverage, but under ABX1 1, insurers would receive taxpayer funds with no accountability over the product they sell or the price they charge.

Specific hypothetical cases:

- **An individual 29-year-old waitress making $26,000 a year**, just over 250% of poverty level. Her age group does not qualify for the tax credit at all. At her age, a cruelly bare-bones Kaiser HMO policy is available today, if she is deemed perfectly healthy by the insurer, for $107 a month. That is just under 5% of her income. Doctor visits cost $30 each. But the deductible is $1,500 and the yearly out of pocket maximum is $5,000 per year. The annual premium and maximum out-of-pocket charge represents 12.6% of her income. Emergency room visits are not covered until the deductible is met. Nor are hospital stays. Even after the deductible is met, she is charged a $500 per day copay for hospitalization. A more comprehensive Kaiser policy, with copays of $200 a day for hospitalization and $25 for doctor visits, no deductible and a $2,500 annual out of pocket limit, is $206 a month. But that is nearly 10% of her income just for monthly premiums. If her employer opted to contribute to the MRMIB pool, and is big enough to do so – no small feat since many restaurants have less than $250,000 in payroll – she would receive only a $20 reduction on premiums for the base Kaiser policy.

    - The policy being considered under ABX1 1 as the "base policy," a Blue Cross plan with a $2,500 deductible and 30% coinsurance, would cost $116 month for the 29-year-old, 5.4% of income before deductibles and coinsurance – including deductibles, 15% of her income.

    - The same waitress, at age 43, could receive up to $76 a month in credits, but the more comprehensive Kaiser policy described above would cost $277 a month and the Blue Cross plan would cost $257 a month. She would be in the same untenable situation as the 29-year-old, with the probability of greater health care needs that would cost her the full deductible as well.

- **A retired couple, both age 62, with $50,000 yearly income**, about 375% of poverty level. The maximum tax subsidy for a couple of their age would be $674 a month. But the subsidy would be reduced to about $380 a month for this couple because the subsidy falls for every dollar of income above 300% of poverty. The subsidy would be available to defer premium costs for a policy above 5.5% of the couple's income—in this case, $229.00 a month. Adding $229 and $380, this couple would look for insurance costing up to $610 a month. A Blue Cross plan is listed on ehealthinsurance.com at a minimum of $606 a month for a perfectly healthy couple of that age in Los Angeles. Even if that were the actual cost, the policy carries a $5,800 family deductible, requires 40% copays and has an out-of-pocket limit of $11,800 per year. Only generic drugs are covered. For the Blue Cross $2500 deductible/30% copay plan, the couple would pay, after the tax subsidy, $655 per month. That's 15.7% of their income, before the high out-of-pocket payments. The retired couple would not eligible for the MRMIB pool 20% credit or the Section 125 plan.

    - A couple the same age making over $56,000 yearly would receive no tax subsidy at all. The same bare-bones policy would cost them 13% of income before the high deductible and copays.

- **A family of four with parents in late 30s, self-employed, making $85,000 a year.** The family, over 400% of the poverty level, does not qualify for a tax credit. The average current premium cost for families of four is slightly over $12,000 a year, according to the latest Kaiser Family Foundation survey. This family would not be eligible for the tax credit. Blue Cross advertises a family plan covering both maternity care and prescription drugs (the cheapest family plans do not) for $623 a month in Southern California, just over 9% of their income. But here's the catch: Almost nothing, including drugs, is covered until the $4,500 family deductible is met. Even covered items have a 50% copay. The out of pocket limit is $5,500. The policy will cost most families $10,000 to $12,000 a year anyway. The self-employed family is not eligible for the MRMIB pool 20% credit or the Section 125 plan.

    - The Blue Cross $2,500 deductible/30% copay plan would cost the family $606 a month, nearly the same as the plan described above, but its out-of-pocket limit would be $7,500 a year per person, $15,000 a year for the family. For even a moderate hospitalization, the family could pay the premium cost of $7,272 plus a $7,500 out of pocket limit and $2,000 in copays for other family members. Total: $16,772. That yearly amount would put many families into foreclosure or near-bankruptcy.

    - If the family were older, likely with parents in their 50s and children heading to college, the same plan would cost $957 a month.

Bottom line:

- None of the Californians described above would be entitled to an automatic exemption from insurance purchase, and none would qualify for the state-subsidized program that would strictly limit what they have to pay. All of them would be at the mercy of insurance companies that could raise their premium costs without limit, and/or reduce their benefits. There is no limit specified in the bill on deductibles or copays, and no limit on out of pocket costs.

- Without direct regulation of insurance premiums, the 15% cap on insurer overhead and profit in ABX1 1 will not control premium costs, subjecting California to the same price increases buffeting Massachusetts. Insurers will have no incentive to control costs and the state has no power to directly do so. Higher premiums increase the dollar amount of the insurers' 15% share, while their absolute costs remain the same. Doctors, hospitals and insurers will have common cause to raise rates at the expense of individuals and the state. The 85/15 requirement also encourages gaming of the system, for instance to define as "medical costs" such administrative functions as phone banks that handle billing questions. This puts upward pressure on premiums.

- Rate regulation, absent from ABX1 1, is the only proven curb on insurance costs. Since 1988, property and casualty insurance rate regulation under Proposition 103 has saved

California drivers $23 billion in premiums.[2] Our consumer group's challenges alone have saved Californians $800 million in auto, home, and medical malpractice premiums since 2003.[3] Under Proposition 103, auto and property/casualty insurers must justify premium increases to the elected insurance commissioner and receive approval before raising rates. At a minimum it should be recommended that provisions be added to ABX1 1 to require health insurers to abide by the same oversight. Auto insurance rate regulation has a proven record of success:

- California auto insurance premiums have declined by 7% since voters approved Prop 103 in 1988, while rates nationally have increased 47%.
- the fifteen years following the passage of Prop. 103, California fell from 2nd most expensive state for auto liability premiums in the country to 21st.
- At the same time, the stability of rate regulation has provided above-average profits for California insurers.[4]

➢ According to the Kaiser Family Foundation, insurance premiums have increased 78% since 2001, compared to a 19% increase in wages and a 17% increase in inflation. Yet the risk of similarly increasing costs appears not to have been factored into proponents' financing formula for ABX1 1.

➢ Beyond unaffordable premiums, the high out of pocket costs under this bill create a false promise that middle-class Californians will actually be able to afford health care. This is called "Mack truck" insurance: you use it only if you get run over by a truck.

The Massachusetts problem:

Proponents of the Massachusetts mandatory purchase of private insurance sold it on a promise of comprehensive health insurance for about $200 a month.

➢ In fact, premiums for health plans for a 55-year-old through the Massachusetts state pool reach up to $531 per month for the most basic required coverage. (Required coverage under the California law has not been defined). The same 55-year-old wishing to purchase more comprehensive coverage will pay up to $906 monthly.

➢ Massachusetts at least offers automatic exemptions based on income and premium costs. A Wall Street Journal editorial on January 7 noted that Massachusetts has already

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[2] *Why Not the Best? The Most Effective Auto Insurance Regulation in the Nation*, Consumer Federation of America, June 2001

[3] *Proposition 103's Impact On Auto Insurance Premiums in California, 15 Years of Insurance Reform*: 1989-2004, Foundation for Taxpayer and Consumer Rights (FTCR), available at: http://www.consumerwatchdog.org/insurance/pr/?postId=8011

[4] *State Average Expenditures for Personal Automobile Insurance* 1993-2004, National Association of Insurance Commissioners.

exempted almost 20% of uninsured adults who don't qualify for subsidies because the mandated insurance is too expensive. Many others who fail to qualify for exemptions are simply refusing to buy.

Real-life examples:

- **Ron Norton, Worcester, Mass,** healthy, 47. "I work full-time and more as an adjunct professor of radiology and data administrator at a community college, but I'm considered an independent contractor. Community colleges train many of the nurses and most of the allied medical professionals Massachusetts. Yet the state doesn't offer health care to 66% of the faculty because we're adjunct professors, not tenure track. After a few years of making about $21,000 as a teacher, I'm making more like $40,000 this year because I'm also doing an administrative job. So under the Massachusetts insurance law my family is not eligible for a subsidy. I'm 47 and have no health problems but the cheapest individual plan is $234, for $2808 a year. That premium is more than 6.8% of my gross salary. Including the $2000 deductible, health care costs will account for 12.7% of my income. After a few years of making $21,000 I'm trying to dig out of a hole. A lot of my students will be in a similar bind, buried in student debt even if they're making decent pay. Young families who took out adjustable mortgages and are now struggling to pay the increase will also suffer from the mandate. I've looked at trying to get an exemption from the state, but you pretty much have to ruin your credit rating first—prove you have unpaid bills, utilities turned off, a foreclosure notice, things like that. That's probably worse in the long run than paying the state fine against the uninsured. I'll pay the fine this year because it's just $220, but it would be at least $1,000 next year." *Interview, 1/03/2008.*

- **Lisa Poplaski, Pittsfield, Mass.,** married, late 40s: "Until last year we had health coverage through my husband's employer for about $300 a month with drug coverage. It was a good policy. But he lost that job and was out of work for 8 1/2 months and we used up our savings. He finally got another tech job but with no benefits. Now the state is forcing us to buy health insurance we can't afford. The only policy that would work for us, based on the state guidelines, costs about $720 a month without prescription drug coverage, excluding copayments. That's far more than our total medical expenses have been up to now. There were slightly cheaper premiums but with high deductibles, so they wouldn't actually be cheaper. Our income will be too high to get the subsidized coverage or an automatic exemption, but not enough to afford $720 a month. The state won't take into account our unemployment hardship this year or our loss of savings. You have to be practically homeless or in foreclosure before they'll give a waiver." *Interview, 12/10/2007.*

Unforeseen costs:

The only publicly available current analysis of ABX1 1, by Assembly committee staff, contains no predictions for either cost increases or expected revenue increases/decreases. Massachusetts, however, is already struggling to control much higher than expected costs. For instance:

- Massachusetts estimates that the cost of subsidized plans by the end of the first year, July 2008, will be $147 million, or 30%, over budget. A similar increase in California (with at least 12 times the number of uninsured), would be $1.75 billion.

- There are a higher-than-expected number of enrollees in subsidized care. Massachusetts' budget projected 136,000 participants; 178,000 new enrollees are expected by July 2008.[5] This indicates that estimates of the number of subsidy-eligible uninsured likely to enroll may be low in California as well.

- Massachusetts' costs are projected to increase up to an additional 14% next year.[6]

- Massachusetts' budget for that state's health care program was based on a low-ball number of the uninsured. The Massachusetts Department of Finance and Policy reported the number of uninsured Massachusetts residents to be 355,000 while the Blue Cross Blue Shield Foundation found that number to be 571,000. Other estimates put the number of uninsured between 500,000 to 650,000. Similarly, a recent analysis of ABX1 1 cited the number of California's uninsured to be 5.9 million while other independent researchers have consistently found that number to be between 6.5 and 7 million.

The fallacy of mandatory purchase:

- Proponents of mandatory purchase, a plan conceived by health insurance companies, say you cannot force insurers to sell policies to everyone if Californians are not required to buy them. There is no large-scale study or firm factual basis for this assertion, under conditions in which premium costs are controlled by regulation. The truth is that most people want to buy health insurance. Sick and well would join the new market if the product was affordable and those with trivial medical conditions were not excluded.

- Small employer groups of two or more have to be sold a policy today, regardless of employees' health condition. There is no gaming by employers and groups. The 7 million uninsured are largely well, working families who often flit in and out of coverage. They are trying, but they just cannot afford to stay insured. The insurers and the medical complex are the problem, not the uninsured.

Real Reform Without Mandatory Purchase of Insurance

The Foundation for Taxpayer and Consumer Rights has recommended throughout this debate a reform plan that addresses affordability and access to care, but does not mandate the purchase of private health policies. Elements of that reform plan include:

- Prohibits the state from requiring Californians without health insurance to purchase insurance.

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[5] Alice Dembner, "Success could put health plan in the red; Mass. program may come up $147m short," *Boston Globe*, Nov. 18, 2007.
[6] Commonwealth Connector staff report, Dec. 12, 2007.

- Requires health insurers to justify premium increases and get approval from state regulators for rate increases.
- Requires insurers to sell policies to anyone regardless of health condition.
- Limits the amount patients must pay out-of-pocket when they get sick.
- Allows any Californian to buy the same health coverage as that available to the governor, legislators and state employees.

Sincerely,

Jerry Planagan

Judy Dugan