Consumer Watchdog

March 28, 2016

Insurance Commissioner Dave Jones
California Department of Insurance
300 Capitol Mall, 17th Floor
Sacramento, CA 95814

Re: Proposed merger of Anthem and Cigna

Dear Commissioner Jones:

Insurance industry consolidation has gone too far in California, costing consumers in the form of higher prices, reduced benefits, narrower networks and fewer choices. Any further contraction of the health insurance market will irreversibly harm consumers. Consumer Watchdog urges the Department of Insurance to use its statutory authority to reject the proposed merger of Anthem and Cigna as against the interests of California policyholders.

The Insurance Code gives the Insurance Commissioner the ability to deny a transaction if:

> Section 1215.2 … (2) The purchases, exchanges, mergers, or other acquisitions of control **would substantially lessen competition in insurance in this state** or create a monopoly therein;
>
> …(4) The plans or proposals which the acquiring person has to liquidate the insurer, to sell its assets, or to merge it with any person, or to make any other major change in its business or corporate structure or management, **are not fair and reasonable to policyholders**;

An Anthem-Cigna merger would eliminate the fifth-largest player from the health insurance marketplace, create a near-monopoly in the large employer self-insured market and decrease options for at least 16.8 million Californians. The proposed merger will unquestionably "substantially lessen competition in insurance in this state" and is "not fair and reasonable to policyholders."

Top Four Health Insurance Companies Will Become Even More Dominant

If Anthem and Cigna are allowed to merge in California, Anthem will leapfrog Kaiser to become the largest health insurer in the state. California's already-highly concentrated health insurance market will lose its fifth-largest player. And, California will be denied the possibility that one of the nation's largest health insurers – Cigna – could increase competition by expanding its presence in the market. And, with Anthem's enrollment at approximately 8.2 million, and Kaiser's at 7 million, the two next-largest players, Blue Shield (3.4 million) and Health Net (2.7 million), will be placed at an even greater competitive disadvantage.[1] Even without the merger, the top four insurers control 83% of the commercial market.[2]

Self-Insured Large Employers Will Have Less Options, Higher Prices

Large employers that self-insure account for nearly 20 percent of insured Californians. Anthem and Cigna control nearly equal portions of this market, also called Administrative Services Only, in which the insurers administer health plans that employers fund. Using 2013 numbers, an Anthem and Cigna merger would double Anthem's share of the self-insured market to 69 percent – or 3.8 million people.[3] (The total number of self-insured rose slightly in 2014, but the ratios remain similar.) Prices will inevitably go up for this group of large employers whose ability to shop around for competitive prices will be cut in half.

Nine California Regions – Population 16.8 Million – Are Among Nation's Hardest-Hit If Merger Is Approved

An American Medical Association (AMA) study of health insurance enrollment data uses the U.S. Department of Justice (USDOJ)/ Federal Trade Commission (FTC) Horizontal Merger Guidelines to identify markets where an Anthem-Cigna merger would enhance market power and reduce competition in the commercial market.

The USDOJ/FTC guidelines identify a merger that enhances market power as "likely to encourage one or more firms to raise price, reduce output, diminish innovation, or otherwise harm customers as a result of diminished competitive constraints or incentives." Outcomes can also include "reduced product quality, reduced product variety, [or] reduced service" and "may also make it more likely that the merged entity can profitably and effectively engage in exclusionary conduct."[4]

The AMA report identifies 9 California metropolitan areas as among the hardest hit in the nation, where the USDOJ/FTC guidelines conclude that the merger is likely to enhance market power. 16.8 million Californians live in these areas.[5] Just 14 states will see such a significant impact. The merger would potentially enhance market power in an additional 6 California metropolitan areas. Combined, the 15 metro areas are home to 33.3 million people and include every significant population center in California, except portions of the Central Valley.

Metropolitan areas where Anthem-Cigna merger will likely enhance market power (in order

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[1] December 2014 enrollment data. California Healthcare Foundation, "California Health Care Almanac," http://www.chcf.org/~/media/MEDIA%20LIBRARY%20Files/PDF/PDF%20Q/PDF%20QRGHealthInsurersEnrollment2016.pdf
[2] December 2013 enrollment data. California Healthcare Foundation, "California Health Care Almanac," http://www.chcf.org/publications/2015/02/data-viz-health-plans
[3] December 2013 enrollment data. California Healthcare Foundation, "California Health Care Almanac," http://www.chcf.org/publications/2015/02/data-viz-health-plans
[4] U.S. Department of Justice and the Federal Trade Commission, "Horizontal Merger Guidelines," August 2010. https://www.ftc.gov/sites/default/files/attachments/merger-review/100819hmg.pdf
[5] Bureau of Economic Analysis, Metropolitan Statistical Areas. https://www.bea.gov/regional/docs/msalist.cfm#C

of impact):

1) Santa Cruz-Watsonville
2) Santa Ana-Anaheim-Irvine
3) Santa Barbara-Santa Maria
4) Salinas
5) Oxnard-Thousand Oaks-Ventura
6) Los Angeles-Long Beach-Glendale
7) Bakersfield
8) El Centro
9) Modesto

Metropolitan areas where Anthem-Cigna merger will <u>potentially</u> enhance market power (in order of impact):

10) San Jose-Sunnyvale-Santa Clara
11) San Diego-Carlsbad-San Marcos
12) San Francisco-San Mateo-Redwood City
13) Riverside-San Bernardino-Ontario
14) Oakland-Fremont-Hayward
15) Sacramento-Arden-Arcade-Roseville

Since the AMA's study is based on 2013 enrollment data, we can only assume two years of increasing consolidation has made the situation worse, not better, for Californians.

California cannot exact enough promises or impose enough conditions to protect consumers from the higher prices, lower benefits, reduced choice and compromised services that are inevitable with another tightening of the market.

<u>The only way to prevent irreversible harm to California policyholders is to reject the Anthem-Cigna merger outright.</u> However, in the event that the Department chooses to approve the merger, we offer the following undertakings as a minimum level of consumer protection from the inevitable reduction of competition in California.

<u>Undertakings</u>

Unreasonable Rates & Wall Street

Anthem is responsible for at least $145 million in rate hikes that were deemed unreasonable by CDI or DMHC since 2013. As you know, California regulators have no authority to reject an excessive or unjustified rate increase. At the same time, Anthem Blue Cross has transferred more than $5.4 billion in dividends to its parent company since the 2004 Wellpoint/Anthem merger.[6] It is neither "fair" nor "reasonable" to continue sending profits out of state while imposing rate hikes on California policyholders, let alone unreasonable rate hikes Anthem refuses to be accountable for.

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[6] Anthem Annual Reports through 2014 and *Los Angeles Times*, "As Anthem Blue Cross sends profit to WellPoint, it plans hefty rate hikes for Californians," February 23, 2010.
http://ir.antheminc.com/phoenix.zhtml?c=130104&p=irol-reportsannual
http://articles.latimes.com/2010/feb/23/business/la-fi-anthem-cash23-2010feb23

- Anthem should commit to not implementing rate hikes that regulators find to be unreasonable.

- Anthem should be prohibited from upstreaming profits to its parent company while at the same time increasing premiums on California policyholders.

- Anthem should be required to disclose details of any administrative services payments to its parent company out of state, to allow the public to gauge whether such payments are made at fair rates or are inflated to hide upstreaming of California policyholder money to shareholders.

Executive Compensation
Anthem has a poor track record in California when it comes to mergers.

When Anthem and Wellpoint proposed to merge in 2004, WellPoint executives tried to walk away with $600 million from the deal. The Department of Insurance under then-Commissioner Garamendi blocked the merger, eventually approving it only after Anthem agreed to concessions including: reduced executive compensation, restrictions on underwriting practices, donations of $265 million to California state health programs, and an agreement that Blue Cross Life & Health customers would not pay for the merger through higher rates.

Even with a reduced compensation package, it was reported that WellPoint CEO Leonard Schaeffer and other executives received $265 million, and Anthem CEO Larry Glasscock was rewarded with a $42.5 million bonus for closing the deal. Anthem has also transferred more than $5.4 billion in dividends out of state as of December 2014.

In the Department's approval of the Health Net-Centene merger deal we were pleased that California policyholders will not be held responsible for executive bonuses, but troubled that severance payments in connection with the deal could still be billed to Californians. California policyholders should bear no part of the cost of an Anthem-Cigna merger, including departures required by any re-organization in the executive suite.

- Anthem should be prohibited from removing reserves from California or otherwise requiring California policyholders to pay for severance, retention or other compensation packages for executives in connection with the merger.

Networks
A Robert Wood Johnson Foundation/ Leonard Davis Institute of Health Economics study recently found that provider networks on Covered California are among the narrowest in the nation, with 75% of exchange plan networks including 25% or less of a region's doctors.[7] Network size has been rapidly shrinking outside the exchange as well.

Multiple insurers have misled California consumers about network size and composition,

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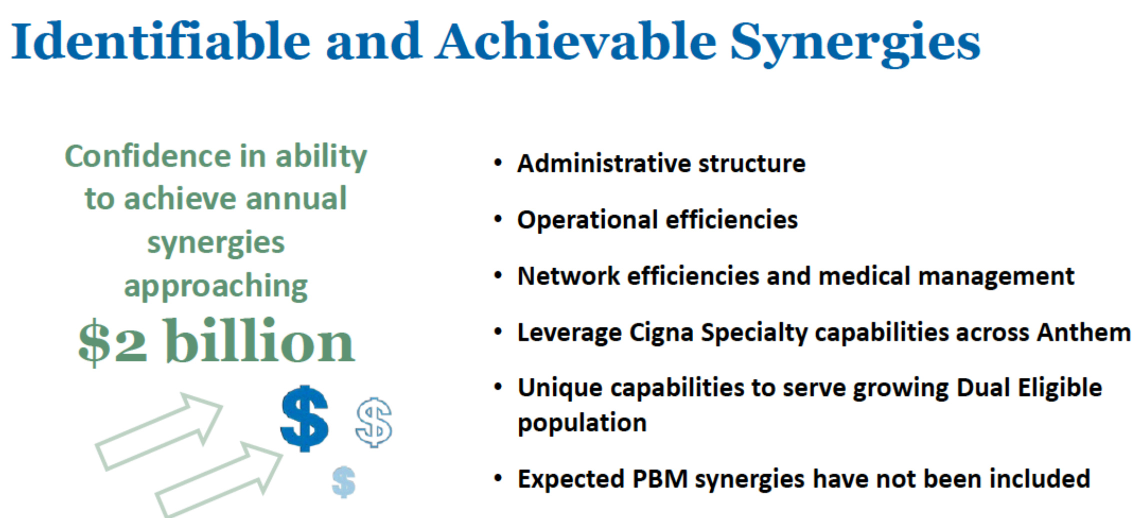
[7] Robert Wood Johnson Foundation, Leonard Davis Institute of Health Economics, "State Variation in Narrow Networks on the ACA Marketplaces," August 2015. http://ldi.upenn.edu/sites/default/files/rte/state-narrow-networks.pdf

and Anthem has been one of the worst offenders in provider directory errors and misrepresentations. A DMHC audit resulted in a $250,000 fine, and CDI implemented new network regulations.   Anthem's indifference even affected its most vulnerable members, with inaccurate Medi-Cal managed care provider directories highlighted in a June 2015 review by the California State Auditor.[8] Anthem Blue Cross of Fresno County was found to have the highest rate of inaccurate provider information of Medi-Cal plans studied.

Cigna has claimed that the merger will increase consumer access to an "enhanced" or "premier" network of hospitals, doctors and other providers. Yet nothing in Anthem's pitch to Wall Street investors identifies better networks or network expansion as a goal or outcome of the merger.[9] Instead, Anthem's investor pitch identifies "network efficiencies" as a key factor in $2 billion in anticipated cost-cutting annually under the merger. From the presentation:



Anthem should be required to resolve its network problems, not make them worse, as a condition of any merger approval.

- Anthem should immediately submit its provider networks to review for compliance with Department of Insurance network adequacy regulations.

- Anthem should commit to improving network size and composition for all plans that give customers access to less than 50% of providers in the area.

Public Accountability

- Anthem's filings with the Department of Insurance to prove its compliance with these undertakings should be public documents. Grants of confidentiality should only be

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[8] California Department of Health Care Services, "Improved Monitoring of Medi-Cal Managed Care Health Plans Is Necessary to Better Ensure Access to Care," June 2015. https://www.auditor.ca.gov/pdfs/reports/2014-134.pdf

[9] Anthem investor presentation, "Anthem-Cigna: A Compelling Combination," July 24, 2015. www.consumerwatchdog.org/resources/anthem_presentation.pdf

allowed sparingly, with explanation of the sensitive nature of the withheld documents, if at all.

- Anthem should be subject to steep penalties for violating any provision of these undertakings, and revocation of approval if there is a pattern of violations.

The number of uninsured Californians has fallen dramatically since the passage of the Affordable Care Act. Yet many low- and middle-income families continue to struggle to pay the costs of a commercial policy, let alone use their new health coverage, as deductibles soar and doctor and hospital networks shrink. A Kaiser Family Foundation/New York Times survey released in January showed that one-in-five working-age Americans ran into serious financial difficulties trying to pay medical bills despite being insured.[10] And California's success in signing up new Medi-Cal enrollees has made the simple act of finding a doctor who will accept Medi-Cal coverage a daunting task.

Historically, health insurance consolidation has not provided the benefits to consumers promised by merging companies. Even when mergers did achieve cost reductions, the savings went to companies, not consumers. We are aware of no study showing evidence of a merger resulting in reduced costs for consumers or better healthcare. Instead, we have evidence of an almost immediate 7 percent hike in premiums after the Aetna-Prudential merger in 1998, cut jobs and wages, reduced payments to healthcare providers and no quality improvements.[11] In another example, an additional 13.7 percent premium increase resulted after the 2008 United-Sierra merger in Nevada.[12]

The merger would make Anthem the largest health insurer in California history. That leap to $115 billion in annual revenue and claiming the lead position in the health insurance market are the merger benefits that Anthem is touting to Wall Street. Yet increasing the size of the few insurance giants that dominate the health insurance market can no longer be credibly sold as a benefit to consumers. California consumers deserve better. We have recommended undertakings in the event the Department approves the Anthem-Cigna merger. However, the only action that truly protects California policyholders is for the Department of Insurance to reject the Anthem-Cigna deal.

Sincerely,

Carmen Balber

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[10] Kaiser Family Foundation, New York Times, "The Burden of Medical Debt," January 5, 2016. http://kff.org/report-section/the-burden-of-medical-debt-introduction/

[11] Leemore Dafny, Mark Duggan, Subramaniam Ramanarayanan, "Paying a Premium on Your Premium," 2012 http://www.kellogg.northwestern.edu/faculty/dafny/personal/documents/publications/ms_2010_0837_0804.pdf

[12] Jose Guardado, David Emmons, Carol Kane, "The Price Effects of a Large Merger of Health Insurers: A Case Study of UnitedHealth-Sierra," 2013. http://www.hmpi.org/pdf/HMPI%20-%20Guardado,%20Emmons,%20Kane,%20Price%20Effects%20of%20a%20Larger%20Merger%20of%20Health%20Insurers.pdf