EXECUTIVE DIRECTOR'S REPORT

Peter V. Lee, Executive Director | December 7, 2017 Board Meeting

PROTECTING CONSUMERS AND PROVIDING COMPETITIVE OPTIONS IN THE FACE OF CONTINUED FEDERAL UNCERTAINTY

THE INDIVIDUAL MARKET WAS STABILIZING IN PLAN YEAR 2017 – CALIFORNIA'S CONTINUED STABILITY WAS BECOMING THE NATIONAL NORM IN 2017

- Kaiser Family Foundation analysis of insurer financial data from the first six months of 2017 showed:
  - Individual market was stabilizing and on the path to insurer profitability.
  - 2017 rates were estimated to result in "medical loss ratios" of 77% for through the second quarter of 2017 (down from a high of 93% in the second quarter of 2015).

- S&P global market analysis found:
  - 2016 was the first year since the start of exchanges that Blue Cross/Blue Shield insurers nationally reported a gross profit (in aggregate) in the individual business line.

FEDERAL ACTIONS CAUSING UNCERTAINTY AND INSTABILITY FOR PLAN YEARS 2018 AND BEYOND

1. **Administration not making cost-sharing reductions (CSRs) payments beginning October 2017 and no legislative solution in place.**
   - **Potential consequence:** carriers ending participation in the individual market; increased costs to consumers and/or the federal government depending on how required CSR expenses are built into premiums.
   - **Mitigations in California:** build cost of CSRs into on-exchange silver premiums to keep carriers in the market and protect unsubsidized individual market from undue premium increases.
2. **Dramatic reductions in marketing investments in Federally Facilitated Marketplace (FFM) states.**
   - **Potential consequence:** reduction in enrollment particularly among healthy individuals who need to be actively sold on the value of coverage throughout the open enrollment period; carriers ending participation; higher premiums for unsubsidized.
   - **Mitigations in California:** Covered California marketing independent of federal decisions – continued evidence-based investments to promote enrollment and lower premiums.
3. **Open enrollment period cut by half for FFM states.**
   - **Potential consequence**: reduction in enrollment particularly among healthy individuals. Impact magnified by dramatic reduction in FFM marketing this year.
   - **Mitigations in California**: use state-flexibility to maintain three-month open enrollment period.
4. **Uncertainty among carriers about federal enforcement of individual shared responsibility penalty.**
   - **Potential consequence**: significant coverage losses and exodus of carriers from individual market if replacement policy is not enacted.
   - **Mitigations in California**: added a provision to contracts with qualified health plans to allow multiyear adjustments to their margins. Additional mitigations, to be determined.
5. **Executive order on new individual market products (association health plan and short-term limited duration insurance plans).**
   - **Potential consequence:** potential harm to risk pool by “siphoning off” good risk; return of low-value “gotcha” coverage.
   - **Mitigations in California**: to be determined.

EXAMPLES OF FEDERAL AND STATE OPTIONS TO PROVIDE STABILITY IN FACE OF UNCERTAINTY

Source of Uncertainty or Instability	National-level Mitigation Actions	State-level Mitigation Actions
Cost-sharing reductions not funded directly	• Reinstitute direct federal funding of CSRs • Provide direction to carriers on “best” way to build CSR funding into premiums	• Instruct carriers in how to build CSR funding into premiums (protecting unsubsidized consumers)
Reductions in federal marketing	• Augment federal marketing for balance of 2018 (SEP) and for future plan years • Carriers expand direct marketing	• Review marketing spend and augment as necessary for future plan years

EXAMPLES OF FEDERAL AND STATE OPTIONS TO PROVIDE STABILITY IN FACE OF UNCERTAINTY

Source of Uncertainty or Instability	National-level Mitigation Actions	State-level Mitigation Actions
Penalty elimination	• Aggressive marketing • Federal reinsurance to lower premium impact of worse risk mix • Impose substitute policies to foster new/continued enrollment (e.g., continuous coverage requirement or auto-enrollment)	• Aggressive marketing • Contractual provisions to allow plans to recoup losses in future years • State-level coverage requirement (e.g., penalty, continuous coverage requirement, auto-enrollment)
Short-term duration health plans and association health plans	N/A	• State regulatory action where possible • Contractual provisions to allow plans to recoup losses in future years

AFFORDABLE CARE ACT PENALTIES: THE BASICS AND HOW IT WORKS

- Starting in 2014, individuals must either:
  - Have health insurance coverage throughout the year;
  - Qualify for an exemption from coverage (people who are exempt because health care is "too expensive" – meaning coverage costs more than 8.05% of actual household income for 2018); OR
  - Pay a penalty when filing federal income tax returns.

- The penalty does the following:
  - Encourages consumers to shop for coverage.
  - On the margins, encourages people to purchase insurance who otherwise would not have without the penalty.
  - Penalizes those who do not purchase insurance which creates a consequence for incurring uncompensated care costs.

- The penalty in tax year 2017 for not having coverage is the higher of:
  - Flat dollar amount: $695 per adult ($347.50 per child; capped at $2,085 per household)
  - 2.5% of household income (capped at the average cost of bronze plan, which is $3,264 per year for an individual)

WHY THE PENALTY: COUNTERACT NATURAL BIASES AND ASSURANCE OF A GOOD RISK MIX

- Individuals with known health conditions in a market with no prohibition on excluding those with pre-existing coverage – will always be more likely to enroll – leading to a potentially very unhealthy risk pool.

- Natural biases lead consumers to perceive health insurance as something they do not need. Biases include:
  - Loss Aversion Bias
  - Temporal Discounting
  - Optimism Bias
  - Availability Bias
  - Status Quo Bias
  - Self-Efficacy

- The penalty is additional incentive to both shop and enroll, which in concert with subsidies and effective marketing, is targeted to overcome those barriers.

See "Marketing Matters: Lessons From California to Promote Stability and Lower Costs in National and State Individual Insurance Markets": http://hbex.coveredca.com/data-research/library/CoveredCA_Marketing_Matters_9-17

WHAT WE KNOW ABOUT THE EFFECTS OF THE PENALTY

- Reduces rate of uninsured by encouraging shopping and insurance take up.
- A higher enrollment of healthy individuals lowers premiums for unsubsidized individuals by fostering a better risk mix.
- Reduction in uncompensated care in hospitals lowers costs to those with employer-based coverage.
- Carriers more likely to participate in the individual market given bigger risk pool and less uncertainty.

THE PENALTY – BENEFITING THOSE "NUDGED" TO GET COVERAGE

- About 20 percent of an individual market insurance pool have ongoing care needs that have costs that vary widely, but are likely to exceed $10,000. These anticipated or likely costs relate to ongoing costs of care for individuals with chronic and/or other ongoing care needs – these people do NOT need a penalty to see the value of insurance.

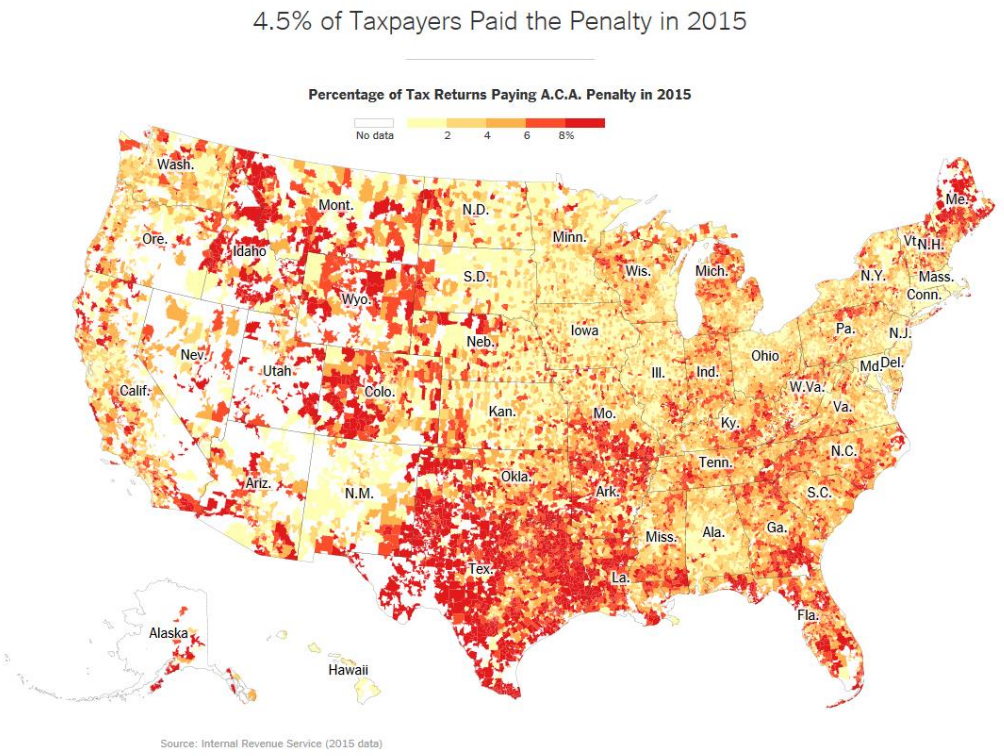
- About 10 percent of the individual market insurance pool may have unanticipated high-cost events – with health care costs of over $20,000. These could be accidents or diagnosis and treatment of newly appearing conditions. These events are precisely the sorts of large financial impacts for which insurance is intended, could easily exceed the maximum out-of-pocket.
  - Based on data from the marketplace Actuarial Value Calculator, which estimates actual average spending by a wide range of consumers in a standard population, there is a significant share of the insurance pool that will have care costs that exceed the Affordable Care Act's maximum out-of-pocket of $7,000 for an individual and $14,000 for a family.

WHAT IS KNOWN ABOUT WHO PAYS THE PENALTY AND GETS THE EXEMPTION?

- According to a New York Times analysis of Internal Revenue Service data, 6.7 million tax filers, or 4.5 percent, paid the penalty in 2015, which is down from 8.1 million in 2014. This figure is at the tax household level, which may be an individual or a whole family.
  - In California, about 4.4 percent of tax filers paid the penalty in 2015.

- Nationally, tax filers with income between $25,000 to $50,000 were the largest group paying the penalty. This group more often lacks access to employer-based coverage and has income that qualifies for premium subsidies. According to a Kaiser Family Foundation analysis, more than half (54% or 5.9 million) of the 10.7 million people who are uninsured and eligible to purchase an Affordable Care Act marketplace plan in 2018 could pay less in insurance premiums for a bronze plan than what they would owe under the penalty.

- Nationally, more than 12 million tax filers filed for and were exempt from the penalty in 2015, meaning that for every tax filer that paid the penalty, two were granted an exemption.



See more at: https://www.nytimes.com/interactive/2017/11/28/us/politics/obamacare-individual-mandate-penalty-maps.html

COVERED CALIFORNIA

TAX CUTS AND JOBS ACT: PROPOSED CHANGE TO INDIVIDUAL MANDATE

- The proposed Tax Cuts and Jobs Act seeks to “zero-out” the shared responsibility payment for individuals who fail to maintain minimum essential coverage, as follows:
  - Strikes the existing 2.5 percent and $695 requirements (including indexing), and inserts zero percent and $0, respectively.
  - Applies to months beginning **after December 31, 2018**.

ESTIMATES OF IMPACT OF PENALTY ELIMINATION OR REPEAL

- Range of national coverage estimates include 3 to 5 million additional uninsured by 2027 (S&P Global) to 13 million (Congressional Budget Office).

- PwC estimates from May 2016 for California forecast a five-year increase in uninsured by up to 300K from subsidized individuals dropping coverage and 480K unsubsidized individuals dropping coverage.

- While wide ranges of estimated impacts, we know:
  - Enrolled consumers find subsidies twice as important as the penalty.
  - Elimination of the penalty would result in decreased enrollment, higher premiums and potential withdrawal of health plans from the individual market.
  - Marketing matters, so impact in California is likely to be far less than in other states.

POLICY OPTIONS FOR OFFSETTING THE IMPACT OF PENALTY REMOVAL

- **Federal or state reinsurance**:
  - Current federal proposals are being considered to fund reinsurance for 2018 and 2019.
  - Reinsurance funding results in about one percent in premium decrease per billion dollars in funding.
  - The cost of reinsurance to the federal government is approximately 20% of the reinsurance cost, since the federal Advanced Premium Tax Credit is reduced.
  - The primary direct beneficiaries of reinsurance are those who do not receive a subsidy.

- **Marketing and outreach to effectively promote availability of subsidies:**
  - Consumers need to know that there are subsidies available to them. Research shows that significant resources are still required to encourage consumers who are subsidy-eligible to research the options available to them.
  - For most consumers, the affordability provided by subsidies is far more important to their enrollment decision than is the penalty.

- **State or federal requirements for continuous coverage and/or auto enrollment:**
  - Continuous coverage requirement could penalize consumers who do not maintain some minimum level of coverage throughout the year.
  - Auto-enrollment could automatically assign consumers to an individual market plan at points of transition in insurance status such as loss of employer-based coverage.

- **State-level individual mandate and penalty**

RESOURCES

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