The Policy Debate on Government Sponsored Health Care Reinsurance Mechanisms
Colorado's Proposal and a Look at the New York and Arizona Models

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Introduction

Recently many states have explored the idea of creating reinsurance programs to reduce costs of health care coverage for the "working poor" and small businesses and thereby reduce the number of individuals without medical coverage. The principle supporting government backed reinsurance programs is to allow insurers to reduce the excess reserves and surplus that they must hold, and subsequently build into premiums, in order to protect against exceptionally large claims.[1] Although less than one percent of the U.S. population has annual medical expenses above $50,000, those individuals account for roughly 28 percent of the country's medical spending.[2] Consequently, proponents argue reinsurance programs that either spread the risk or assume part of the risk can have a large impact on premium levels. However, structuring and implementing a program in an individual state raises myriad issues and obstacles.

Colorado's Proposal: "Healthy Business Healthy People"

During the 2005 legislative session, the Colorado General Assembly considered legislation intended to create more affordable health care for individuals and businesses. It is estimated that Colorado has 746,000 medically uninsured.[3] Senate Bill 05-237, "Healthy Business Healthy People," was modeled after the plan implemented in New York, "Healthy New York"[4] ("HNY"). Like the New York plan, Colorado's proposed legislation would have created a state subsidized reinsurance mechanism for participants' health care costs.

The impetus for the legislation was stated in the Legislative Declaration to Senate Bill 05-237, which provides as follows:

1) All Colorado citizens deserve to have access to affordable, comprehensive health insurance and quality health care;

2) Individuals, families, and small businesses deserve to have predictable, stable costs for health care from one year to the next;

3) Small businesses are the backbone of our economy and must not be asked to disproportionately bear the burden of providing health insurance;

4) Between 1996 and 2002, small business health insurance premiums increased more than eighty percent, both nationally and in Colorado;

5) Less than fifty percent of Colorado small businesses offer health insurance;

6) Most low-income working Coloradans who are not offered health insurance at the workplace and who have preexisting conditions cannot obtain coverage in the private market and cannot afford the high cost of coverage made available to uninsurable individuals through the CoverColorado program;

7) Reinsurance policies have been proven to lower the cost of insurance for small employers, by providing additional coverage for those at highest risk;

8) The purpose of this part 7 is to make standardized, low-cost health insurance contracts available to qualifying small employers and qualifying individuals as defined in this part 7. This part 7 is designed to encourage small employers to offer health insurance coverage to their employees and also to make affordable coverage available to uninsured individuals whose employers do not provide group health insurance.[5]

Colorado's "Healthy Business Healthy People" would have required an insurer to pay for claims under $5,000 and over $75,000, while the state government fund would cover expenses in between those amounts.[6] Eligibility requirements were designed to fit the local Colorado market, and qualifying businesses in Colorado had to have 10 or fewer eligible employees with 30 percent of them earning $28,000 or less.[7] The Legislation mandated participation by all carriers in the "small group"[8] market – HMOs, PPOs and indemnity carriers.[9] Funding for the reinsurance mechanism would be $15 million per year.[10] The program could not be funded unless Colorado voters approved Referendum C in the 2005 general election.[11]

The ultimate effectiveness of the "Colorado's Healthy Business Healthy People" proposal in fulfilling the legislative goal was unclear. Detractors claimed the bill was too premature as it preceded the passage of Referendum C, which would create the 15 million dollar reinsurance pool. Some alleged that it was "'an obvious advertising strategy' to convince voters to approve Referendum C."[12] There were insufficient mechanisms in place to assure that the costs of the program would not be greater than the available funds. Additionally, there were managed care effectiveness concerns regarding Colorado's inclusion of PPO's and Indemnity plans in the proposal as opposed to limiting the program to HMO's, as did HNY. Other differences, between the New York health insurance environment and that in Colorado, created uncertainties regarding achieving any of the success that resulted from implementing the reinsurance program in New York.

Advocates, on the other hand, recognized the critical need to provide affordable healthcare to small businesses and the working poor and to reduce the burden on emergency care providers that the uninsured use as their source of primary medical care. They maintained that adoption of the plan would lower medical costs for everyone in Colorado.

Ultimately, the "Healthy Business Healthy People" legislation failed to pass, in major part due to the fundamental need to carefully plan and tailor such a program to the unique aspects of Colorado's health insurance environment.

Other States' Efforts

The issues raised in Colorado this past session are being discussed nationwide as states struggle to help manage the costs of health care. Both New York and Arizona have established reinsurance mechanisms funded by state money. "Healthy New York"[13] (HNY), an excess-of-loss plan, and Arizona's "Healthcare Group of Arizona"[14] (HCG), an aggregate stop-loss program, have realized success making health coverage more affordable for more people in their states.[15]

New York

"The Healthy New York" program was designed to be an affordable alternative for small businesses and individuals who in the past have been unable to afford insurance in the commercial market.[16] The state of New York acts as the re-insurer for costs that exceed $5,000 but are below $75,000.[17] Qualifying businesses must have 50 or fewer eligible employees with 30 percent of those employees earning $32,000 or less.[18] Additionally, the program offers coverage to individuals whose gross household income meets the income guidelines of the program.[19] In New York, the state protects insurers from the high costs incurred by any one individual. In essence, HNY establishes a reservoir fund to pay for catastrophic cases. Dedicated funding levels for the program were $89.4 million in calendar year 2003, $49.2 million in 2004, and $44 million for the first half of 2005. Any amounts not used are carried over to subsequent years. It is estimated that total stop-loss reimbursement for 2003 will be approximately $13 million.[20]

The premiums initially offered under HNY (in January 2001) were about half those for individuals in the regular direct-pay, individual market in New York, and were between 15 and 30 percent lower than premiums of comparable policies for small firms.[21] During the second year of the program, premiums dropped another 6 percent and finally resulted in a premium decline of 17 percent.[22] As of May 2005, HNY had 92,368 individuals enrolled.[23] It is estimated that there are 3 million uninsured New York citizens.[24]

"HNY" continues to evolve and modifications are being sought in additional areas. The 2004 year end report is a valuable source of information on demographics, contains survey results of both provider and consumer perceptions, and also contains data on all aspects of the program - including suggested changes in several areas.[25]

Arizona

Healthcare Group of Arizona provides coverage for the risk that a large number of enrollees will have above-average health care expenses.[26] The Arizona plan does not necessarily focus on catastrophic costs but rather the higher-than-average expenses of all the enrollees.[27] Healthcare Group of Arizona (HCG) was created to provide affordable and accessible health care coverage to small businesses with 50 or fewer employees and political subdivisions within the State of Arizona.[28]

"HCG" is a public–private partnership between Arizona Health Care Cost Containment System (AHCCCS, the state's Medicaid agency) and two private health plans. It offers a small business an HMO product that is administered by AHCCCS and exempt from state insurance regulations for commercial plans. Employers and employees share the full cost of premiums. However, the state subsidizes the program covering a portion of claims above $20,000 and less than $100,000, and purchases catastrophic reinsurance coverage for claims above $100,000. Health plans are reimbursed for losses.

"HCG" has been successful in attracting participants and lowering health care costs. In 2001, the total subsidy for "HCG" was $8 million per year.[29] Expenses were eventually cut and by 2004 this subsidy was reduced to $4 million.[30] As of July 2005, approximately 15,000 workers and dependents were enrolled.[31] Of the 3,816 businesses participating, 92 percent are firms with one to three employees."[32] There are approximately 933,500 medically uninsured in Arizona.[33] Demographic data for "HCG" is updated monthly by "HCG".[34]

"HCG" is also a program that continues to evolve. The program is introducing diverse customized benefits packages, enhancing the provider network, and implementing a new marketing campaign that may include wellness programs with member reward incentives. The program also is trying to attract the participation of enough health plans to offer choice and diversity of arrangements for enrollees. Proposed legislation would allow more flexibility in contracting with health plans and specialized provider networks, dropping a previous state requirement that only plans participating in Medicaid may be offered by "HCG".[35]

Policy Arguments

Government funded health reinsurance mechanisms remain controversial and policymakers nationwide continue to debate their efficacy. Advocates, generally point to the following in support of such plans:

- "By reducing insurance carriers' exposure to large number of very high claims, [reinsurance programs] remove much of the need for per capita premiums in the individual and small group markets to be priced so much higher than those in larger groups."[36]
- Reinsurance programs allow states to "ease protections against adverse selection in a reinsured health insurance purchasing program-and widen access to the subsidies that the program offers-by balancing program rules and market rules."[37]
- "If carriers' risk of very high costs could be reduced, they would have far less incentive to use screening mechanisms to risk-select enrollees."[38] Such reduction is possible with reinsurance plans.
- Under reinsurance plans "the burden of the high expenditures of a few people will be quite small for any one person. This reduces the likelihood that people who have nongroup coverage will drop it if anyone with very high expenditures enrolls with their carrier."[39]
- State reinsurance plans help nongroup health insurance markets spread the costs of very high-cost persons.[40]

- Reinsurance programs can be useful in states with varying market rules. Such plans can address issues of both affordability and access.[41]

Skeptics of state reinsurance plans argue the following:

- "Even with reinsurance, state health insurance purchasing programs are vulnerable to adverse selection when they attempt to do what the market does not."[42]

- The government would most likely have to assume the costs associated with serving as a reinsurer, which could be high if the rate reduction is to be sufficient to induce substantial numbers of previously uninsured individuals to buy coverage.[43]

- Carriers are not totally protected if claims for high-cost enrollees exceed the available reinsurance funds.[44] In addition, reinsurance does not eliminate the risk that a single carrier may have a disproportionate share of claims above the maximum attachment point. In the event that this occurs, carriers might request higher premiums to recoup their losses.[45]

- Difficult decisions regarding which benefits to include as being eligible for reinsurance would have to be made, and sophisticated simulation models are needed to determine the costs of reinsurance designs.[46]

Conclusion

Scant amount of academic research exists regarding these various reinsurance programs and whether or not they can successfully lower health care costs. As a result, the jury is still out. States must be mindful of variants among health care delivery systems across the country. Such differences make it nearly impossible to simply export one state reinsurance program to another state absent some modifications.

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1 Mr. Ferm wishes to thank his associate, Beth Dickhaus, for her assistance with this article.
[2] Chollet, D., Cohn, D., & Martinez-Vidal, E., *More Answers on Reinsurance*, STATE COVERAGE INITIATIVES, Vol. VI, No. 2, 1, June 2005.
[2] Swartz, K., *Reinsurance: How States Can Make Health Coverage More Affordable for Employers and Workers*, THE COMMONWEALTH FUND – NARVARD SCHOOL OF PUBLIC HEALTH, 1, July 2005.
[3] Colorado: Population Distribution by Insurance Status, state data 2002-03, U.S. 2003, Henry J. Kaiser Family Foundation.
[4] N.Y. Ins. Law §§4326 & 4327; *See also*, http://www.ins.state.ny.us/website2/hny/english/hny.htm and Swartz, K. *supra* at note 2.
[5] Senate Bill 05-237, Amended 2nd Reading, May 2, 2005, proposed C.R.S § 10-8-702,
[6] *Id*. at proposed C.R.S. § 10-8-708(2)(b).
[7] *Id*. at proposed C.R.S. § 10-8-703 (11) & (12).
[8] In Colorado, a small group is essentially defined as an employer with 50 or fewer employees C.R.S. § 10-16-102(40)(a).
[9] *Supra*, note 5 at proposed C.R.S. § 10-16-105(16)(b).
[10] Colorado Legislative Council Staff, Fiscal Note to SB 05-237.
[11] Referendum C, a legislative referendum placed on the ballot by the passage of Colorado House Bill 05-1194 would alter a Colorado constitutional provision commonly known as "TABOR." TABOR limits the amount of money the state may spend each year. It limits the annual increase for some state revenue to inflation plus the percentage change in state population. Any money collected above this limit is refunded to taxpayers, unless the voters allow the state to spend it. Referendum C asks voters if the state may spend the money it collects above the limit. Colorado Legislative Council, *2005 Blue Book Analysis.* Available at: http://www.leg.state.co.us/lcs/0506initrefr.nsf/89fb842d0401c52087256cbc00650696/deb289c855a0758987256ffc006efc97?OpenDocument.
[12] Ashby, C., *Senate Republicans Attack Small Business Health Insurance Bill,* THE PUEBLO CHIEFTAIN ONLINE, May 4, 2005.

[13] Supra note 5.
[14] Arizona Revised Statutes §§ 36-2912 to 36-2912.02. *See also*, http://www.healthcaregroupaz.com and Swartz, K. *supra*, note 2.
[15] Swartz K., *supra*, note 2.
[16] N.Y. Ins. Law § 4326(a)
[17] Chollet, D., *The Role of Reinsurance in State Efforts to Expand Coverage*, STATE COVERAGE INITIATIVES ISSUE BRIEF, October 2004.
[18] N.Y. Ins. Law § 4326(c)(1)
[19] N.Y. Ins. Law § 4326(c)(3)
[20] *Report on the Healthy New York Program 2004*, December 31, 2004, Available at: http://www.ins.state.ny.us/website2/hny/reports/hnyepp2004.pdf
[21] Swartz K., *Healthy New York: Making Insurance More Affordable for Low-Income Workers*, HARVARD SCHOOL OF PUBLIC HEALTH -THE COMMONWEALTH FUND, vii, November 2001.
[22] *Supra*, note 20 at I –3.
[23] *Supra*, note 2 at 5.
[24] New York: Population Distribution by Insurance Status, state data 2002-03, U.S. 2003, Henry J. Kaiser Family Foundation.
[25] *Supra*, Note 20
[26] Swartz, K. *supra*, note 2 at 9.
[27] *Id*.
[28] http://www.healthcaregroupaz.com/FAQS.asp
[29] *Affordable Health Care for Small Business – A Plan to Meet the Need*, HEALTHCARE GROUP OF ARIZONA, 4 (2004). Available at: http://www.healthcaregroupaz.com/reports.asp
[30] *Id*.
[31] http://www.healthcaregroupaz.com/reports.asp
[32] The Commonwealth Fund. *See*, http://www.cmwf.org/tools/tools_show.htm?doc_id=235064
[33] Arizona: Population Distribution by Insurance Status, state data 2002-03, U.S. 2003, Henry J. Kaiser Family Foundation.
[34] Health Care Group of Arizona*, supra*, note 31.
[35] The Commonwealth Fund, s*upra,* note 32.
[36] Chollet, s*upra*, note 17.
[37] *Id.*
[38] Swartz K., *Government as Reinsurer for Very-High-Cost-Persons in Non-Group Health Insurance Markets*, HEALTH AFFAIRS, October 2002.
[39] *Id*.
[40]*Id*.
[41] Chollet, *Supra* note 17.
[42] *Id*.
[43] Swartz, *Supra* note 38.
[44] Swartz, *Supra* note 21.
[45] *Id*.
[46] Swartz, *Supra* note 38.
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