

**Potential Impact of Health Reform on the
Cost of Private Health Insurance Coverage**

PRICEWATERHOUSECOOPERS 

October 2009

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Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Table of Contents

| | |
|---|-----|
| Executive Summary | E-1 |
| Introduction | 1 |
| Private Health Insurance Coverage | 2 |
| Issue A - Insurance Market Reforms Without a Strong, Workable Coverage Requirement..... | 2 |
| Issue B - Excise Tax on "Cadillac Plans" | 5 |
| Issue C - Increased Cost Shifting..... | 10 |
| Issue D - Assessments on Health Sector Entities | 12 |
| Interaction of the Issues | 12 |

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Key Findings

- Health reform could have a significant impact on the cost of private health insurance coverage.
- There are four provisions included in the Senate Finance Committee proposal that could increase private health insurance premiums above the levels projected under current law:
 - Insurance market reforms coupled with a weak coverage requirement,
 - A new tax on high-cost health care plans,
 - Cost-shifting as a result of cuts to Medicare, and
 - New taxes on several health care sectors.
- The overall impact of these provisions will be to increase the cost of private insurance coverage for individuals, families, and businesses above what these costs would be in the absence of reform.
- On average, the cost of private health insurance coverage will increase:
 - 26 percent between 2009 and 2013 under the current system and by 40 percent during this same period if these four provisions are implemented.
 - 50 percent between 2009 and 2016 under the current system and by 73 percent during this same period if these four provisions are implemented.
 - 79 percent between 2009 and 2019 under the current system and by 111 percent during this same period if these four provisions are implemented.

Executive Summary

Private healthcare costs are anticipated to grow over the next decade by approximately 6 percent per year under current law, which is more than double the expected growth in the Consumer Price Index of approximately 2.5 percent per year.¹ Controlling the growth in these costs will require restructuring and realigning the incentives in the system.² While the healthcare reform packages take steps in this direction, a major focus of the current legislation is on expanding insurance coverage. These reforms propose to make insurance more widespread by providing new subsidies for the uninsured and those with lower incomes by reforming the health insurance market.

America's Health Insurance Plans engaged PricewaterhouseCoopers (PwC) to examine the impact of four components of the health reform bill being proposed by the Senate Finance Committee as

¹ The 6 percent increase is consistent with the per capita growth rate in total health expenditures as detailed in the National Health Expenditure Accounts, Projected total health expenditures 2010 to 2018. The Blue Chip Consensus expects inflation to average 2.5 percent over the same period.

² PwC has previously estimated that structural reforms, such as improved wellness and prevention, disease management, value based payment reform, improvements in health information technology, comparative effectiveness and malpractice reform, could mitigate growth in healthcare costs by between 0.5 and 1.0 percent per year after an initial investment period. See PricewaterhouseCoopers "A Review of AHIP Savings Estimates" in Appendix to AHIP, "A Shared Responsibility," 2008.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

introduced. These include:

- Insurance market reforms and consumer protections that would raise health insurance premiums for individuals and families if the reforms are not coupled with an effective coverage requirement.
- An excise tax on employer-sponsored high value health plans (or "Cadillac plans") that in a few years could also raise premiums for some moderate value plans.
- Cuts in payment rates in public programs that could increase cost shifting to private sector businesses and consumers. These changes are expected to more than offset the potential reduction in cost shifting resulting from providing coverage to the uninsured.
- New taxes on health sector entities that are likely to be passed through to consumers.

The increases in private health insurance coverage described above would be on top of the underlying growth in medical costs over the coming period.

This analysis shows that the cost of the average family coverage is approximately \$12,300 today and could be expected to increase to approximately:

- \$15,500 in 2013 under current law and to \$17,200 if these provisions are implemented.
- \$18,400 in 2016 under current law and to \$21,300 if these provisions are implemented.
- \$21,900 in 2019 under current law and to \$25,900 if these provisions are implemented.

This analysis shows that the cost of the average single coverage is \$4,600 today and could be expected to increase to:

- \$5,800 in 2013 under current law and to \$6,400 if these provisions are implemented.
- \$6,900 in 2016 under current law and to \$7,900 if these provisions are implemented.
- \$8,200 in 2019 under current law and to \$9,700 if these provisions are implemented.

The charts below outline the impact of these provisions on premiums for both single coverage (chart 1) and family coverage (chart 2). The bottom line illustrates the cost growth in premiums for the entire private health insurance sector³ taking into account medical growth and inflation. The top line illustrates the cost growth in premiums after adding the impact of these Senate Finance Committee provisions⁴.

³ This is a weighted average of the individual, small group, large group and self-funded markets.

⁴ Impact assumes payment of tax on high-value plans, full cost-shifting of cuts to public programs, and full pass-through of new industry taxes.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Chart 1: Average premiums for single coverage are estimated to be about \$4,800 in 2010, will increase to approximately \$8,200 in 2019 in the absence of reform and could increase to \$9,700 if these reforms become law.

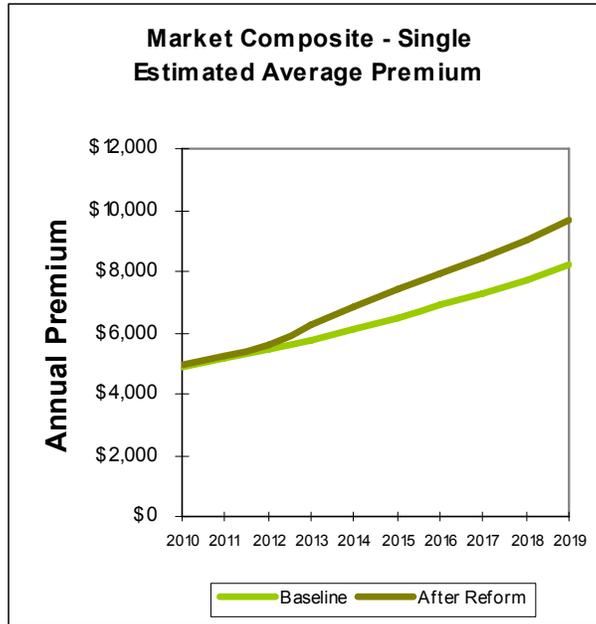
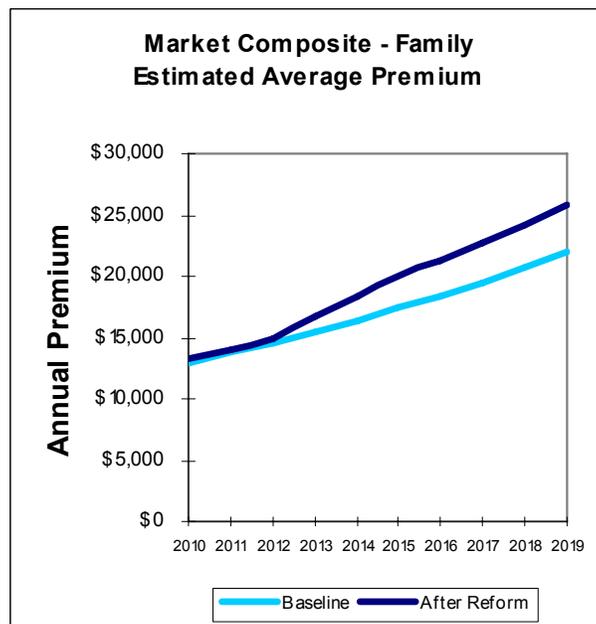


Chart 2: Premiums for family coverage will increase from about \$13,000 in 2010 to approximately \$21,900 in 2019 in the absence of reform and \$26,000 if these reforms become law.



Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

As the above charts illustrate, by 2019 the cost of single coverage is expected to increase by \$1,500 more than it would under the current system and the cost of family coverage is expected to increase by \$4,000 more than it would under the current system. This amounts to an additional 18 percent increase in premiums by 2019. The overall 18 percent increase is a composite of increases by market segment as follows:

- 49% increase for the non-group (individual) market;
- 28% increase for small employers (those firms with fewer than 50 employees);
- 11% increase for large employers with insured coverage; and,
- 9% increase for self-insured employers.

The overall impact of these provisions will be to increase the cost of private health insurance coverage for individuals, families, and businesses. The net impact of these increases on households would include the impact of these increases and the new subsidies provided under the bill.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Introduction

The health care reform debate has focused on three main issues: providing affordable coverage to the uninsured, promoting quality healthcare, and "bending the cost curve", or slowing the growth of healthcare spending. While complementary in some cases, these goals can also conflict. Efforts to increase coverage and promote quality could lead to a more efficient healthcare sector, but they could also lead to increased growth in costs if implemented without a full appreciation of the downstream impact on cost of health insurance coverage. Analyzing the overall impact of these reform efforts requires an evaluation from all perspectives. America's Health Insurance Plans engaged PricewaterhouseCoopers (PwC) to examine the potential impact of certain provisions of health reform bills on the cost of private health insurance coverage.

Private healthcare costs are anticipated to grow over the next decade by approximately 6 percent per year under current law, which is more than double the expected growth in the Consumer Price Index of approximately 2.5 percent per year.⁵ Controlling the growth in these costs will require restructuring and realigning the incentives in the system.⁶ While the healthcare reform packages take steps in this direction, a major focus of the current legislation is on expanding insurance coverage. These reforms propose to make insurance more widespread by providing new subsidies for the uninsured and those with lower incomes.

This report focuses on several key provisions that are part of current health reform proposals that would have a significant impact on the premiums for private health insurance coverage, including:

- Insurance market reforms and consumer protections that would raise health insurance premiums for individuals and families if the reforms are not coupled with an effective coverage requirement.
- An excise tax on employer-sponsored high value health plans (or "Cadillac plans") that could raise premiums for many private consumers.
- Cuts in payment rates in public programs that could increase cost shifting to private sector businesses and consumers. These changes are expected to more than offset the potential reduction in cost shifting resulting from providing coverage to the uninsured.
- New taxes on health sector entities that are likely to be passed through to consumers.

Collectively these provisions would raise the premiums for private health insurance coverage.

The reform packages under consideration have other provisions that we have not included in this analysis. We have not estimated the impact of the new subsidies on the net insurance cost to households. Also, if other provisions in health care reform are successful in lowering costs over the long term, those improvements would offset some of the impacts we have estimated.

⁵ The 6 percent increase is consistent with the per capita growth rate in total health expenditures as detailed in the National Health Expenditure Accounts, Projected total health expenditures 2010 to 2018. The Blue Chip Consensus expects inflation to average 2.5 percent over the same period.

⁶ PwC has previously estimated that structural reforms, such as improved wellness and prevention, disease management, value based payment reform, improvements in health information technology, comparative effectiveness and malpractice reform, could mitigate growth in healthcare costs by between 0.5 and 1.0 percent per year after an initial investment period. See PricewaterhouseCoopers "A Review of AHIP Savings Estimates" in Appendix to AHIP, "A Shared Responsibility," 2008.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Private Health Insurance Coverage

Private health insurance coverage is spread across several different segments. The majority of the U.S. population receives coverage through employers. Large employers either purchase coverage on behalf of employees at a regional or national level from health insurance companies, or self-insure, sometimes using a health insurance company as a plan administrator. The small group market includes small employers purchasing insurance in local markets. Individuals without employer-provided insurance purchase plans obtained in local markets.

Health reform targets many of its insurance reforms to the small group and individually purchased markets. These markets are expected to serve as the vehicle to provide new coverage to the previously uninsured and replacement coverage to others interested in new plans. However, the market reforms that are part of the current reform proposals could affect the ability of this market to provide attractive insurance plans.

The large group market would also be impacted by health reform, as cost shifting, new health sector taxes, and an excise tax on high value plans lead to higher costs.

Given that the majority of the US population is covered by some form of private insurance, the impact of these health reform provisions could affect the health insurance of most Americans.

Issue A - Insurance Market Reforms Without a Strong, Workable Coverage Requirement

There are three major components to insurance market reforms and consumer protections – guaranteed issue regardless of a pre-existing condition, rating reform and the individual coverage requirement. There is also an array of benefit options intended to offer affordable choices to meet diverse consumer needs. These elements interact to produce varying impacts on premium rates, depending on the segment of the population being analyzed. Additionally, the strength of the individual coverage requirement is critical in determining the impact of the other elements.

In this section of our report, we have reviewed and relied on extensive modeling by the Hay Group, an actuarial and benefits consulting firm. The results highlight the potential impact of proposed health care reform proposals on the non-group (individual) market. The Hay Group's analysis shows major increases in premium levels resulting from the proposed insurance reforms.

The root cause of the impact is the combination of several key factors:

- A weak individual coverage requirement, coupled with a guarantee issue requirement, no pre-existing condition limits and no rating based on health status;
- The impact of limiting the differential between age bands in rating, which can increase costs substantially for younger individuals;
- New minimum benefit requirements that may require people to buy coverage that is more expensive than options to which they have current access⁷; and
- Allowing more and more individuals to "opt-out" of coverage based on a standard that will be increasingly difficult to meet as premiums increase due to the factors listed above.

⁷ Under the Senate Finance Committee proposal, benefit plans at the "Bronze" level (generally the lowest cost tier available) must have an actuarial value of approximately 65%. In Massachusetts, benefit plans in the lowest cost Bronze level must have an actuarial value of roughly 56%. Congressional Research Service, Setting and Valuing Health Insurance Benefits, p. 1, April 6, 2009.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

The modeling results summarized in the table below show the impact of the guarantee issue requirement coupled with a low, weak or no individual coverage requirement. In states that allow underwriting of individuals (45 states plus the District of Columbia), premiums could increase by approximately 41% to 59% on average by 2016, depending on the strength of the individual coverage requirement⁸. These increases would take several years to be fully realized, but would begin to rise as unhealthy or sick individuals began to purchase coverage, while younger, healthier individuals decided it was less expensive for them to forego coverage without consequence or consideration of the impact of the overall pool.

| Estimated Change in Average Market Premium With Low or Weak Mandate | |
|--|--------|
| Individual in Underwritten States | 41-54% |

These figures assume the presence of temporary risk spreading mechanism or "reinsurance" to ensure that the costs of high risk individuals are spread across plans in an equitable way. Without this assumption, average premium increases listed above would range from 47-62%. The scenarios depicted in the model all assume premium assistance that attempts to follow the structure set out in the Senate Finance Committee's Mark called "America's Healthy Future Act".

In the Senate Finance proposal, the rate band restrictions⁹ would result in a maximum spread in rates by age to a 4-to-1 ratio. This ratio would further increase costs for younger individuals while reducing costs for older individuals. However, this reduction in costs for older individuals in underwritten states would be more than offset by the 41% to 54% increase in average premiums mentioned above. In the underwritten states, the combined impact of guarantee issue and rate band restrictions could be expected to result in an increase in premiums of 59% to 63% for 18-24 year olds while older individuals aged 60-64 could be expected to see increases in the 33% to 37% range assuming a low or weak mandate and a maximum 4-to-1 rate band ratio.

| Estimated Change in Market Premium by Age Band in Underwritten States Assuming Low or Weak Mandate and a Maximum 4-to-1 Rate Band Ratio | |
|--|--------|
| Age 18-24 | 59-63% |
| Age 40-44 | 48-52% |
| Age 60-64 | 33-37% |

In addition, there are several factors that could contribute further to the premium increases likely to result from these reforms and potentially threaten to create premium spirals. These include:

- A lack of coordination between the implementation of new market rules and the phase-in of the individual coverage requirement. While the new market rules are implemented in full in Year 1, the individual coverage requirement is delayed and then phased in gradually. Once the

⁸ 5 states are guarantee issue states and they already have average premiums significantly in excess of those available in underwritten states. Other states may offer a "carrier of last resort". In states that already require guarantee issue, rates could actually be reduced by 16% to 22%, as more people enter those markets due to the additional premium subsidies provided under reform. Nonetheless, since the majority of states are not guarantee issue, the average increase across the entire individual market could still be more than 40 percent by 2016 under the weak mandate.

⁹ A rate band restriction limits the difference in how much one person pays versus another person based on a set factors including age.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

penalties for lack of coverage are fully phased in, they are estimated to be less than 10 percent of the average cost of coverage resulting in a relatively low incentive for individuals who are healthy to buy insurance.

- Because there is no coverage requirement in Year 1, we would anticipate significant adverse selection to occur in the existing market, increasing premiums for those who have coverage today. Higher premiums will result in more individuals being exempted from the coverage requirement. Once the requirement is implemented, the penalties will be phased in, so that they will not reach full effectiveness for several years. This lack of coordination increases the likelihood of a premium spiral that “gets ahead” of the coverage requirement which, with the combination of an income-based opt-out and low penalties, may further reduce the incentive for those who are healthy to buy coverage. This may then cause an increase in premiums for those with coverage today.
- Proposals to further compress age bands will likely increase the cost of coverage for younger individuals and make it less likely that they will obtain coverage. As fewer and fewer young people come into the system, overall premiums will increase for everyone.
- New excise tax provisions on various industries that are likely to raise average premiums in the market as discussed below. The non-deductibility of the excise tax further increases the effective impact of the tax leading to further increases on health insurance premiums.

Small Group

Small group rates will also be impacted by these changes. Small employers face an affordability challenge today in offering health care coverage to their employees. Virtually all of the bills being considered by Congress would apply the same rating rules to small employers that would ultimately apply to the non-group market, whether provided in or outside a health insurance exchange. Additionally, these market reforms include minimum and tiered benefit requirements¹⁰.

All health reform bills pending before the Congress would create health insurance exchanges. Current proposals appear to contemplate a structure whereby small employers could make a defined contribution on behalf of their employees seeking coverage in the exchange. Those employees could then choose between competing health plans offerings within a benefit tier. Given that the rating rules in the exchange and benefit levels would ultimately be uniform, and that existing employer groups may be disaggregating by requiring individuals to pick their own plan, it is unclear to what extent premiums in the exchange would differ for individuals accessing the exchange on their own versus individuals accessing the exchange through their employer¹¹.

The proposed reforms applicable specifically to small group coverage are projected to lead to significant increases in premiums for most small businesses. While the requirement to offer coverage on a “guarantee issue” basis is already required under federal law in the group market the proposal to prohibit any premium variation between groups based on claims experience or health status will likely impact coverage in many states. This reflects the fact that most states (39) already limit by how much health plans can vary premiums between different small businesses based on the claims experience or health

¹⁰ Unless subject to “grandfathering,” small businesses offering coverage not meeting the newly established “minimum creditable coverage” would need to “buy up” their coverage. In addition to establishing a minimum actuarial value of 65%, the proposal being considered by the Senate Finance Committee would require coverage of all benefit mandates whether required at the state or federal level.

¹¹ This point is borne out by CBO estimates which project premiums for plans offered in the exchange, without distinguishing between whether those premiums are for individuals accessing coverage through the exchange on their own or through their employer.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

status of the group. They do not, however, prohibit rating based on the group's experience altogether¹². In addition, prohibiting a small business's own experience from being taken into account in establishing premium rates will tend to raise rates significantly for the majority of small businesses.

In addition, the income based premium credits are only available to individuals and families purchasing coverage through the new insurance exchanges – they are not available to employees (and their families) receiving coverage through an employer except under limited circumstances¹³. The effect of this structure might be to weaken incentives for maintaining small group coverage, leading to a shift towards individual purchase through the new exchanges. The level of premiums for coverage offered through the exchange for individuals (which under the Senate Finance Committee proposal would be the same as outside the exchange) would likely impact the amount of take up expected in the exchange.

The combined impact on small group premiums, assuming employers did not reduce benefits to offset increased costs is estimated at 13% to 15% on average or roughly \$1,200 per individual and \$3,200 per family based on projected rates for 2013¹⁴. It should be noted that the impact of proposed health care reforms on small businesses assumes the retention of a distinct small group market. If certain policy changes such as those discussed caused small firms to shift to individually purchased coverage through the exchange, the results could be different than estimated.

Issue B - Excise Tax on "Cadillac Plans"

As one of the revenue enhancements to support health reform, the Senate Finance Committee is considering an excise tax on employer-sponsored high-value health plans, or "Cadillac plans".¹⁵ Besides raising revenue, this excise tax is intended to discourage the proliferation of plans with minimal cost sharing. Many believe that if a plan were to be subject to the tax, efforts would be made to eliminate benefits or increase cost sharing in order to avoid the 40 percent excise tax. The excise tax is based on a flat dollar threshold of \$8,000 for individuals and \$21,000 for families. Healthcare costs and consequently premiums tend to vary by many factors including geography, age, morbidity and whether additional health benefits are offered (e.g. dental, vision, flexible spending accounts). In addition, since those thresholds are intended to be indexed by CPI plus 1 percent, they are not expected to keep up with health care costs, which are assumed to grow by 6 percent in the future.

¹² The most common permitted level of variation between small businesses based on claims experience or health status is +/- 25% on initial issue of the policy and +/-15% on policy renewal.

¹³ Under the Senate Finance Committee legislation, an employee who is offered coverage that does not have an actuarial value of at least 65 percent or who is offered unaffordable coverage by their employer can be eligible for the tax credit.

¹⁴ These estimates would also increase by approximately 7% if "groups of one" remained in the small group market. In addition, these projections assume that small businesses that found these increases due to health reform too much to bear would stop offering coverage. If this assumption proved wrong, the average increase for all small businesses would be higher.

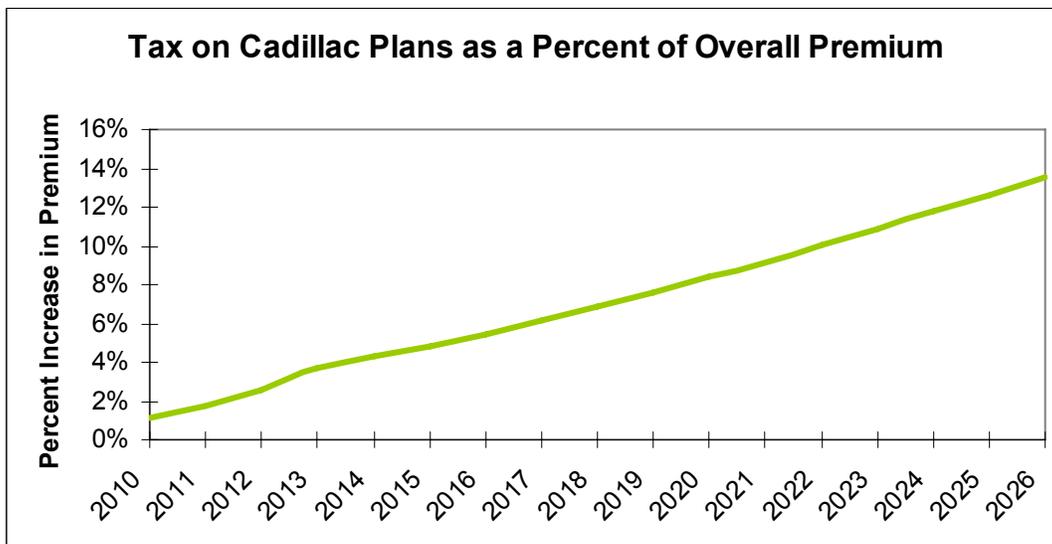
¹⁵ As recorded in the Senate Finance Committee's, "America's Healthy Future Act of 2009," as amended and released on October 2, 2009. The Act imposes a 40 percent excise tax on insurers "if the aggregate value of employer-sponsored health coverage for an employee exceeds a threshold amount." The threshold amounts will start at \$8,000 for individual coverage and \$21,000 for family coverage in 2013, and will be grown each year at the consumer price index for all urban consumers plus one percent. The thresholds are increased for employees in "high risk professions," which include law enforcement officers, firefighters, members of rescue squads or ambulance crew, and individuals engaged in the construction, mining, agriculture, forestry, and fishing industries. PricewaterhouseCoopers did not consider the increased thresholds for high risk professions for the purposes of this analysis. For the 17 highest healthcare costs states, the thresholds will be increased by 20 percent in 2013, 10 percent in 2014, and 5 percent in 2015 to provide transition relief.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

PwC performed two separate analyses of the impact of the excise tax on "Cadillac plans". First, we looked at a distribution of COBRA rates¹⁶ for large employers to determine how many plans can reasonably expect to be affected by the tax and when they would be affected. In addition, benefits such as dental coverage and flexible account contributions made by enrollees would also be included in determining the excise tax, as would any cost shifting or other health cost changes caused by reform.

We have estimated the potential impact of the tax on premiums. Although we expect employers to respond to the tax by restructuring their benefits to avoid it, we demonstrate the impact assuming it is applied. As the threshold is indexed to CPI-U which has generally been lower than medical trend, it is expected that many plans that currently have premium rates that are beneath the threshold will ultimately reach it.

The tax on Cadillac plans will only apply to plans that exceed the thresholds in a given year. However, in order to illustrate the impact of the tax on health plan expenditures as a whole, we have estimated that the tax will add an average of 5% to Large and Small Group insurance premiums in 2016. The estimated impact of the tax on Cadillac plans on premiums over time is shown in the following chart:



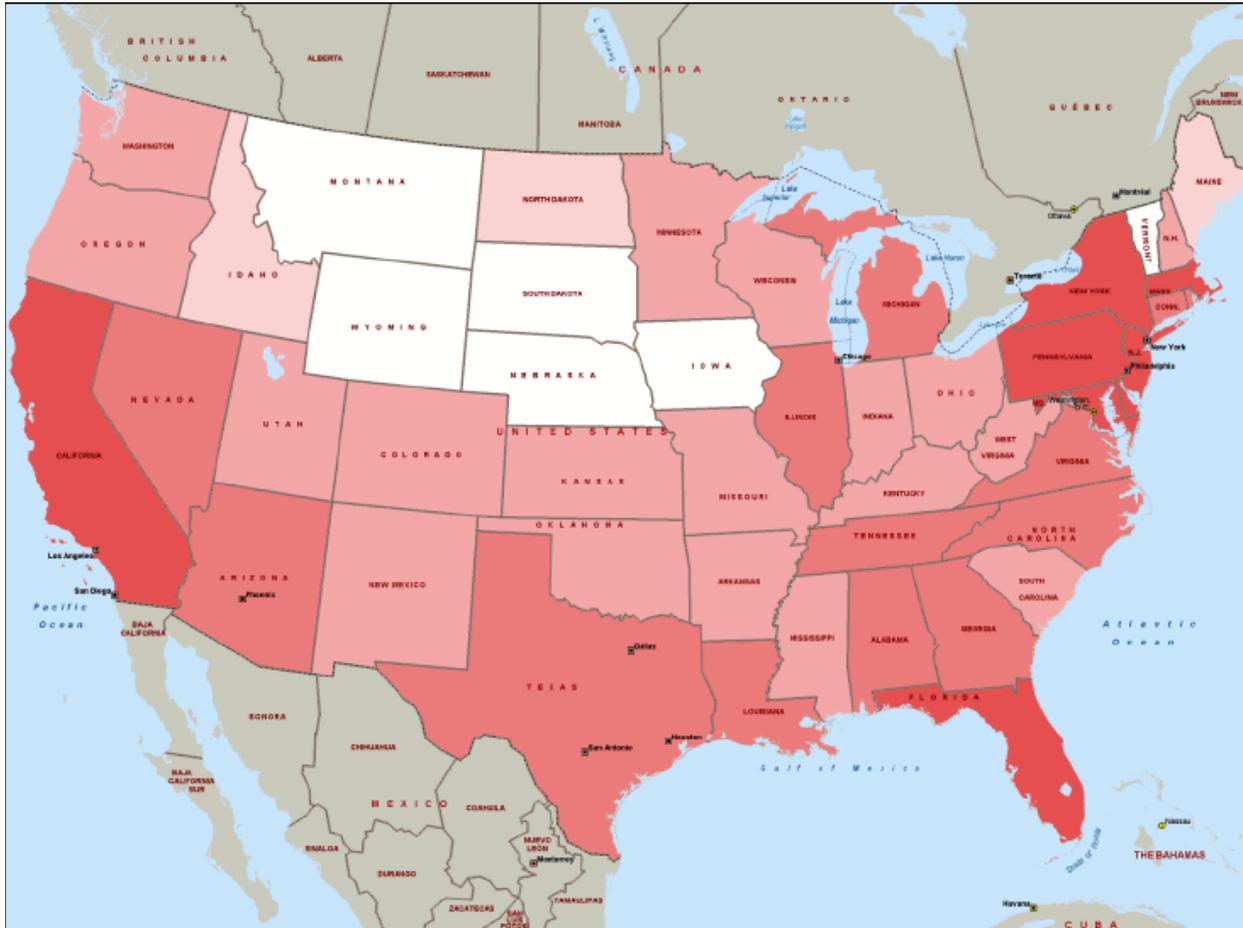
PwC also examined the impact of the excise tax on the mandated plans expected to be offered under the state health insurance exchanges detailed in the Senate Finance Committee Bill.¹⁷ We estimate that in many metropolitan areas, which tend to have higher than average medical costs, the lowest option plan (Bronze Plan) would be considered a "Cadillac plan" as early as 2016. By 2016 at least one of the mandated plans will be considered a "Cadillac plan" and be subject to the 40 percent excise tax in 17 of 50 states. By 2019 at least one of the mandated plans will be considered a "Cadillac plan" and be subject to the 40 percent excise tax in 24 of 50 states.

¹⁶ 2009 COBRA rates for approximately 300 large companies were analyzed from the PwC Touchstone Survey and evaluated against the parameters of the excise taxes. An adjustment was made to remove the 2% administrative load. A copy of the results of the 2009 PwC Touchstone Survey can be obtained at: <http://www.pwc.com/us/en/healthcare/publications/pwc-health-and-well-being-touchstone-survey-results.jhtml>

¹⁷ Based on "baseline" assumptions (6 percent annual trend; 15 percent supplemental load for additional benefits, age, morbidity and other factors)

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Plans Exceeding "Cadillac Plan" Threshold in 2019 by State (@ 8% Trend)



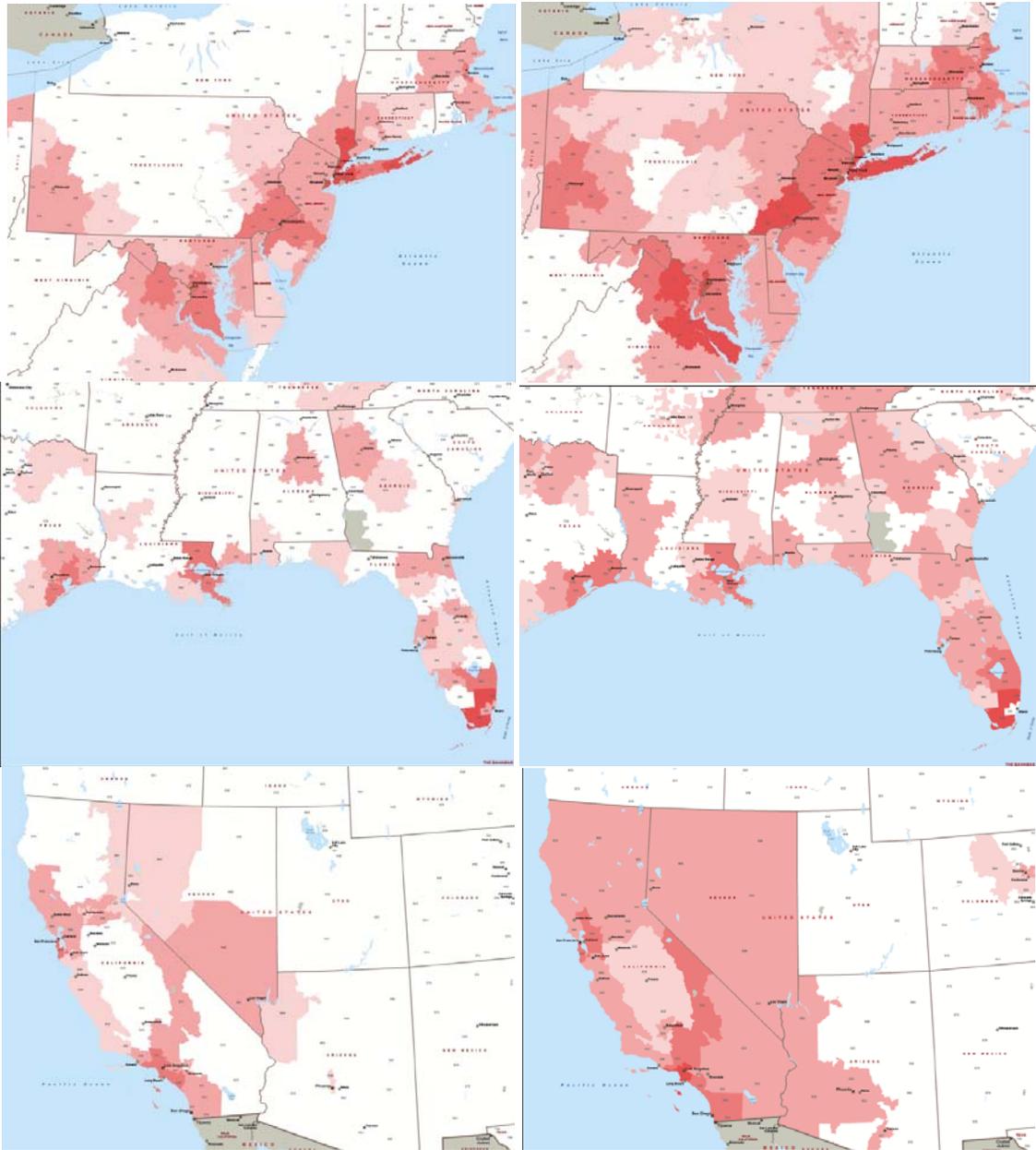
In addition, even in the short run, state averages are not indicative of the magnitude of the impact. For example, the following charts highlight the impact of the excise tax in 2016 and 2019 for several areas of the country. The metropolitan areas are impacted much more quickly than the secondary areas.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Plans Exceeding "Cadillac Plan" Threshold by Local Area (@ 6% Trend)

2016

2019



Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Issue C - Increased Cost Shifting

Today, certain costs (e.g., hospital expenses) are shifted to the private sector (employers and consumers) as some participants in the system pay less than their share of the cost of their care. Public programs such as Medicare and Medicaid reimburse less than the cost of care for hospitals services.¹⁸ In addition, the uninsured or underinsured may not be able to cover the full cost of care, and this cost is then also transferred to the private market.

The initial hope of health reform was that by improving coverage of the currently uninsured, a significant percentage of uncompensated care would be eliminated. This is still anticipated to happen. However, the cost shift "gains" from decreasing the numbers of uninsured now appear to be more than offset by the losses from proposed cutbacks in Medicare and Medicaid spending allocated to the hospital sector.¹⁹

It should also be noted that the impact of covering the uninsured may be different in communities constrained by limited hospital capacity. In those communities, covering the uninsured could actually increase cost-shifting if the newly insured increase demand for healthcare services and the overall mix of hospital patients migrates towards lower paying government programs.

The net impact is likely to result in an increase in cost shifting which translates into a 0.8 percent average annual increase in the private sector spending between 2010 and 2019, or \$145 on average per year for family coverage in a large group plan (and \$55 for single coverage). We note that this cost burden ramps up over the projection period, with an average annual increase in health costs of 1.2 percent over the second five-year period. We assume that this increased cost to the private sector will ultimately impact the cost of coverage for individuals and businesses in both the insured and self-insured market. As a result, premium costs for large group plans will be \$37 higher each year between 2010 and 2014 for family coverage (\$14 for single coverage), and \$255 higher each year between 2015 and 2019 (\$96 for single coverage).

¹⁸ American Hospital Association, "Trend Watch Chartbook 2009."

¹⁹ This evaluation is based on the Medicare payment cuts as detailed in the Senate Finance Committee's Chairman's mark (as amended) released on October 2, 2009. There are similar but not identical payment changes reflected in the Senate Health Education Labor and Pension (HELP) Committee bill, the "Affordable Health Choices Act" dated July 15, 2009 and the House Tri-Committee bill, "America's Affordable Health Choices Act" (H.R. 3200) dated July 14, 2009.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

| Average Impact of Cost Shift on Insurance Premiums * | | | |
|---|------------------|------------------|------------------|
| | <u>2010-2014</u> | <u>2015-2019</u> | <u>2010-2019</u> |
| Percent Impact on Premiums | | | |
| Reductions in Uncompensated Care | -0.4% | -1.4% | -1.0% |
| Cuts in Medicare/Medicaid Reimbursements | <u>0.6%</u> | <u>2.6%</u> | <u>1.7%</u> |
| Net Impact on Premium Spending | 0.2% | 1.2% | 0.8% |
| Average Annual Impact on Group Premiums | | | |
| Annual Impact on Individuals | \$14 | \$96 | \$55 |
| Annual Impact on Families | \$37 | \$255 | \$145 |

* Note: assumes full cost-shifting over the period. If only a portion of costs are shifted to private payers, the figures would be correspondingly smaller in absolute value.
Sources: PricewaterhouseCoopers' Touchstone Survey and calculations and CBO analysis of Baucus Mark, September 22, 2009

The House Tri-Committee legislation and the Senate HELP bill include a government-sponsored insurance option that would compete with private insurers in health insurance exchanges. Since government-sponsored programs have traditionally paid providers less than the private sector, as enrollment in a government-run plan increases, hospital revenue margins may decrease and consequently accelerate further cost shift. This would likely lead to increasing payment differentials between the public and private payers and the potential for further spiraling as private sector enrollees, facing continuously higher premiums leave the market²⁰.

²⁰ According to an analysis by Dobson Davanzo, LLC, payment to cost ratio increases could more than double the cost shift effect on premiums. They estimate the increase in the proportion of annual premiums that are due to cost-shift to increase from \$1,512 to a range of \$3, 375 to \$5,200. (<http://content.healthaffairs.org/cgi/reprint/hlthaff.28.w1013v1>)

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Issue D - Assessments on Health Sector Entities

As Congress seeks to finance coverage subsidies for low income individuals and small business, some bills are now targeting specific sectors of the health industry. The Senate Finance Committee legislation imposes new fees on certain providers: a \$6.7 billion annual fee on health insurance companies, a \$2.3 billion annual fee on pharmaceutical manufacturers, and a \$4 billion annual fee on medical device companies. All of these assessments would increase the underlying cost structure of each of these segments in the health sector and, as CBO has indicated, will likely be passed back to enrollees in the form of higher premiums.

We estimate that these fees will raise annual insurance premiums by 2.5 percent for individual, small group, and large group plans over the 2010 to 2019 period, assuming they are fully passed through to patients. Self-insured employers would avoid the tax on health insurers since it is based on insurance premiums and thus self-insured plans would see a 0.3 percent increase in costs. As the fees are fixed in nominal terms, the percentage impact would decline each year. The average cost of a family plan would increase by almost \$487 each year, while costs in the self-insured market would increase by \$64 per year on average.

| Average Impact of New Assessments | | | |
|--|-------------------------|-------------------------|-------------------------|
| | <u>2010-2014</u> | <u>2015-2019</u> | <u>2010-2019</u> |
| <i>Percent Impact on Premiums</i> | | | |
| Insured | 3.0% | 2.2% | 2.5% |
| Self-Insured | 0.4% | 0.3% | 0.3% |
| <i>Average Annual Impact on Group Family Premiums</i> | | | |
| Insured | \$487 | \$487 | \$487 |
| Self-Insured | \$65 | \$63 | \$64 |

Note: Nondeductible taxes have been grossed up to cover the associated taxes on the passed-through amounts assuming a 35 percent marginal federal tax rate and an average insurance premium tax of 2 percent.

Sources: PricewaterhouseCoopers' Touchstone Survey and calculations and CBO analysis of Baucus Mark, September 22, 2009.

This cost differential between group plans and self-insured plans is a key factor in the movement of many employers to self-insurance. Any increase in the differential, such as the proposed new tax on insurers would be expected to further increase this movement. The calculations above assume that 25 percent of the Large Group category switches to the Self-Insured category.

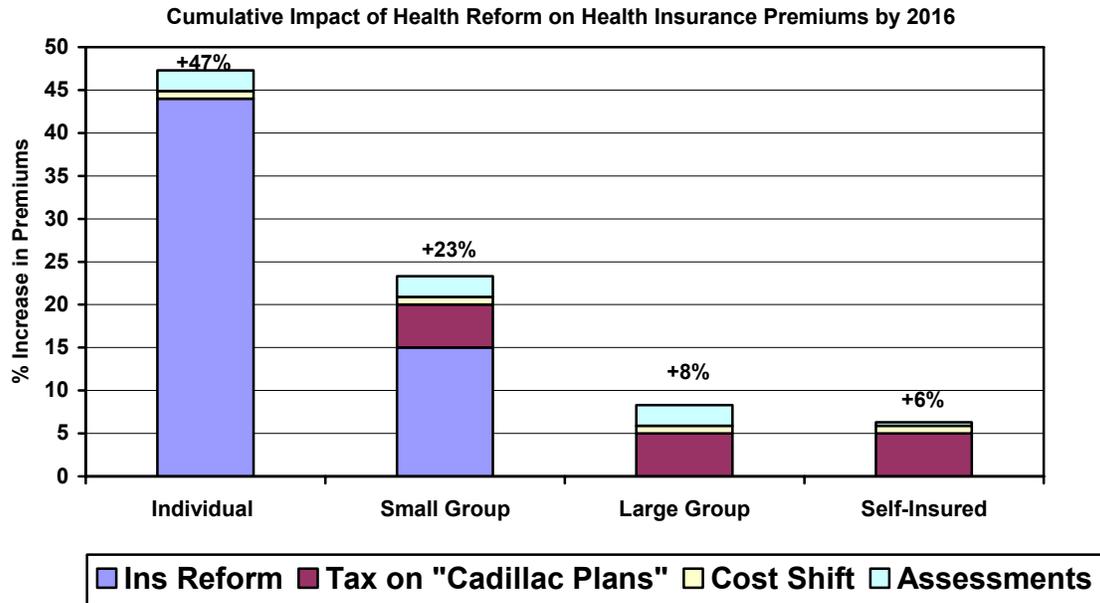
Interaction of the Issues

The interaction of all of these issues accelerates the impact on individuals and businesses. For example, the cost shifting and assessments described above will accelerate the application of the tax on high value plans.

We have allocated these spending increases to the different segments of the health insurance market. Reform could increase premium costs by significant amounts. Premiums for plans purchased in the

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

individual market in 2016 could rise in cost by 47 percent on average over premiums projected in 2016 in the absence of health reform. Other segments would also see significant increases.



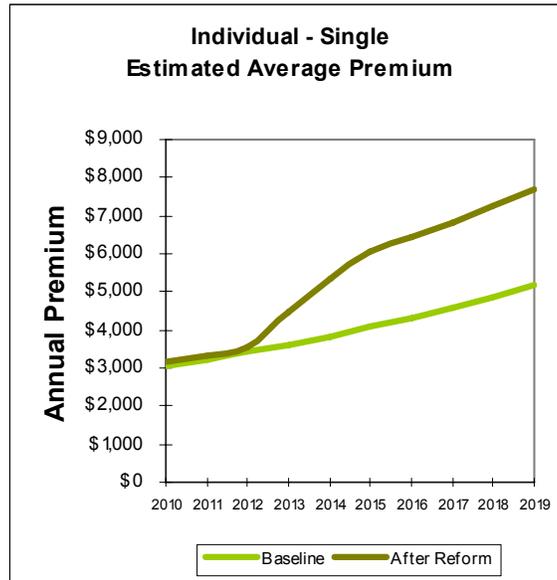
These increases are on top of normal healthcare trend and further serve to increase the cost of private health insurance coverage.

Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

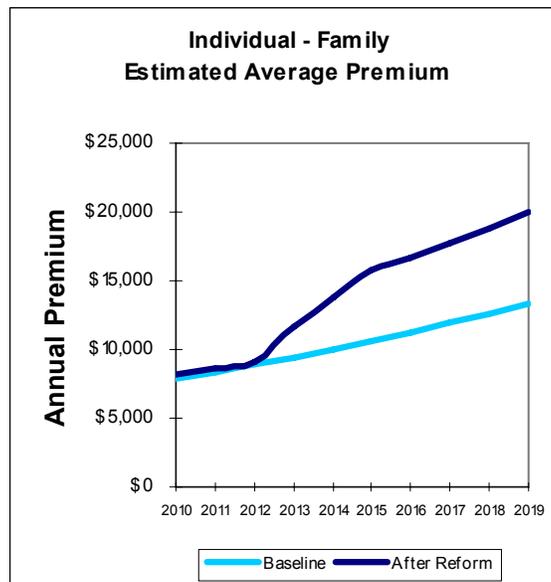
The charts that follow reflect the impact of reforms by market over time²¹.

Individual Market:

Single - Premiums for an individual purchasing insurance in the non-group market that are estimated to average about \$3,000 in 2010, will increase to approximately \$5,200 in 2019 in the absence of reform and will increase to \$7,800 if these reforms become law.



Family - Premiums for a family purchasing insurance in the non-group market will increase from about \$7,900 in 2010, will increase to approximately \$13,400 in 2019 in the absence of reform and \$20,000 if these reforms become law.

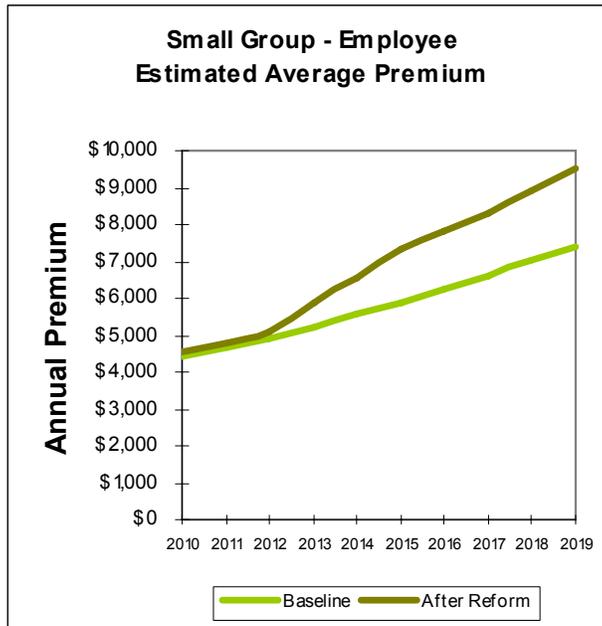


²¹ Impacts assume payment of tax on high-value plans, cost-shifting of cuts to public programs, and full pass-through of industry taxes

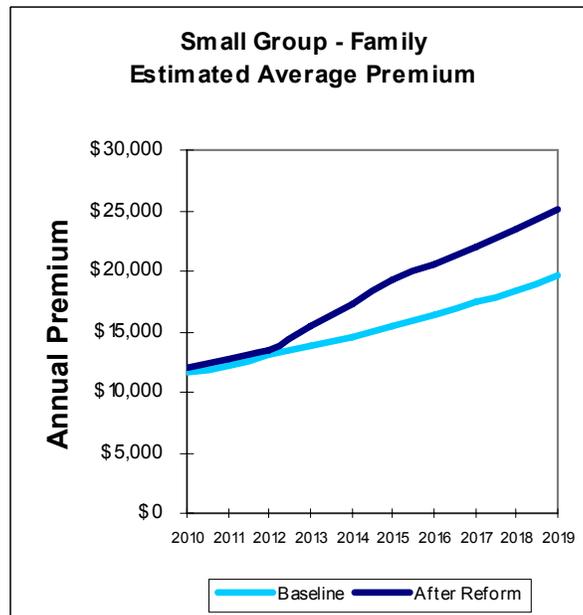
Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Small Group:

Single - Premiums in the small group market for employee coverage that are estimated to be about \$4,400 in 2010, will increase to approximately \$7,400 in 2019 in the absence of reform and will increase to \$9,500 if these reforms become law.



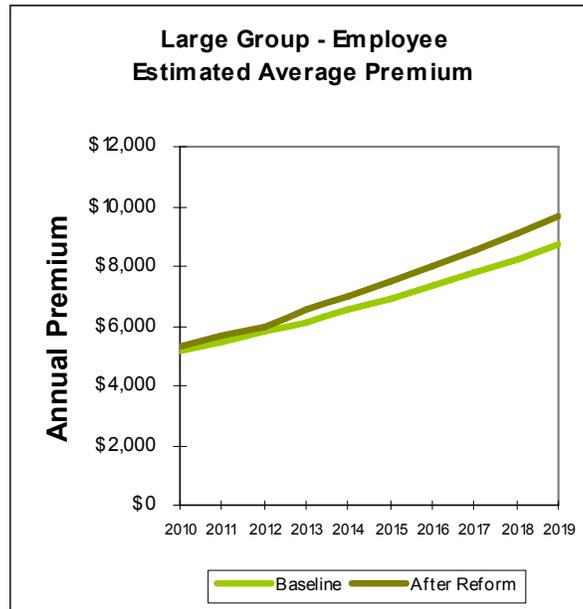
Family - Premiums in the small group market for family coverage will increase from an average of about \$11,600 in 2010 to approximately \$19,600 in 2019 in the absence of reform and to approximately \$25,000 if these reforms become law.



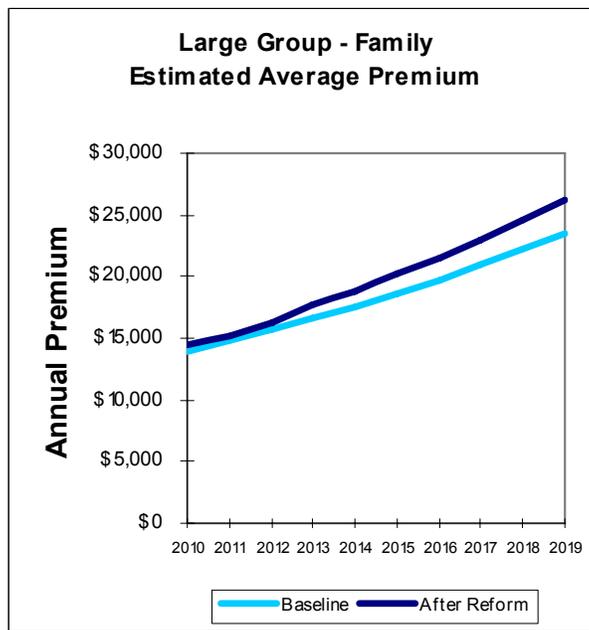
Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Large Group:

Single - Premiums in the large group insurance market for employee coverage that are estimated to be about \$5,200 in 2010, will increase to approximately \$8,700 in 2019 in the absence of reform and will increase to \$9,700 if these reforms become law.



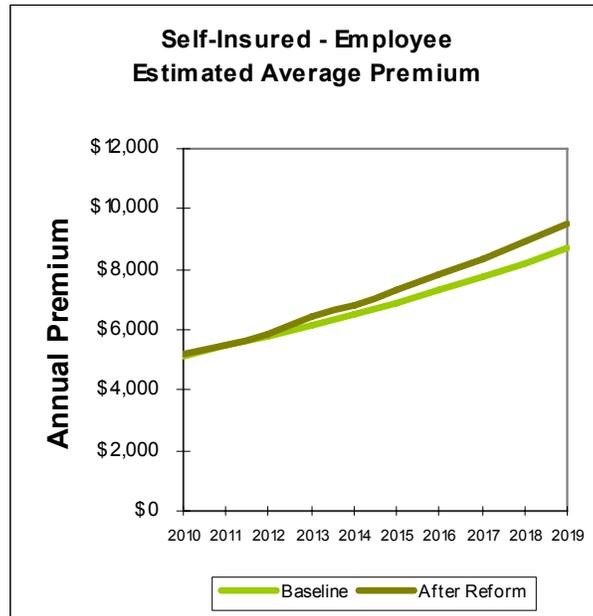
Family - Premiums in the large group market for family coverage will increase from average of about \$13,900 in 2010 to approximately \$23,500 in 2019 in the absence of reform and \$26,200 if these reforms become law.



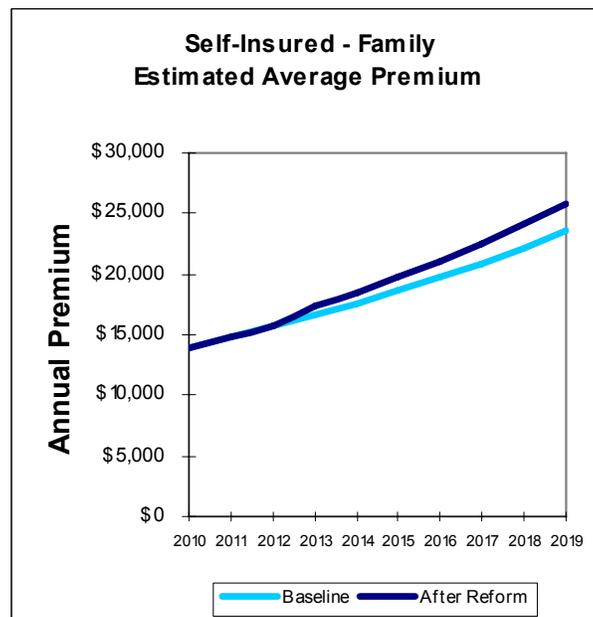
Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Self-Insured:

Single - Premiums²² in the large group self-insured market for employee coverage that are estimated to be about \$5,200 in 2010, will increase to approximately \$8,700 in 2019 in the absence of reform and will increase to \$9,500 if the reforms are passed.



Family - Premiums in the large group market for family coverage will increase from average of about \$13,900 in 2010 to approximately \$23,500 in 2019 in the absence of reform and \$25,700 if these reforms become law.

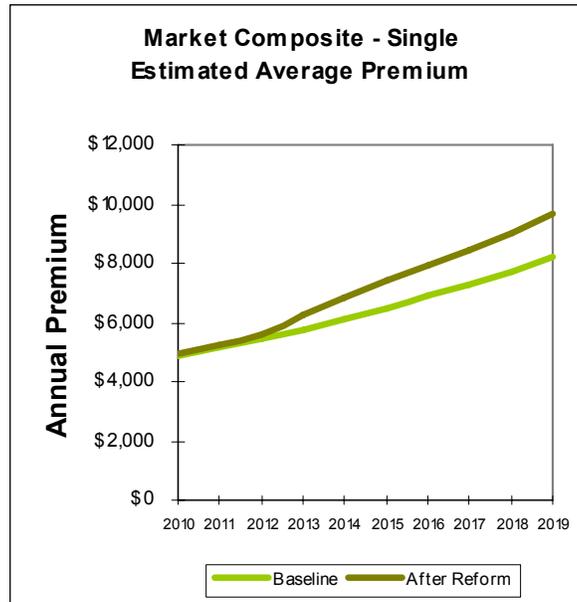


²² For self-insured employers, "premiums" refers to "premium equivalents" composed of incurred benefits plus related administrative expenses.

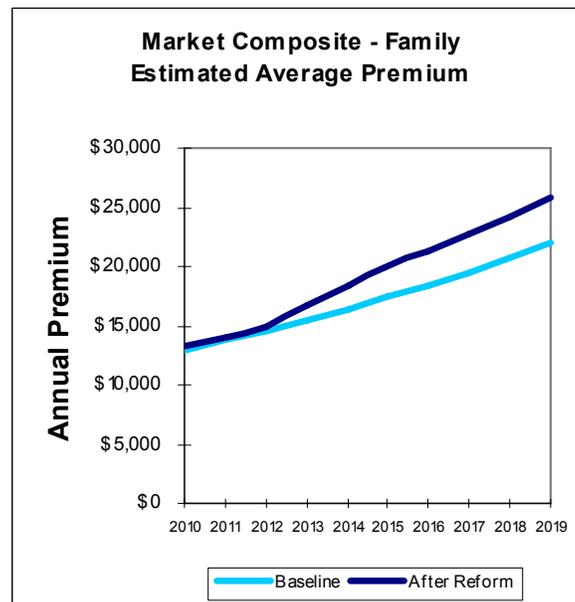
Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

Market Composite:

Single -- Average premiums for an individual that are estimated to be about \$4,800 in 2010, will increase to approximately \$8,200 in 2019 in the absence of reform and will increase to \$9,700 in 2019 if these reforms become law.



Family -- Premiums for a family purchasing insurance in the private market will increase from about \$13,000 in 2010 to approximately \$22,000 in 2019 in the absence of reform and to approximately \$26,000 in 2019 if these reforms become law.



Potential Impact of Health Reform on the Cost of Private Health Insurance Coverage

As the above charts illustrate, by 2019 the cost of single coverage is expected to increase by \$1,500 more than it would under the current system and the cost of family coverage is expected to increase by \$4,000 more than it would under the current system. This amounts to an additional 18 percent increase in the cost of health insurance coverage by 2019.

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