

WHAT'S BEHIND THOSE RISING HEALTH INSURANCE PREMIUMS?

by *Merrill Matthews, Ph.D.*

Health insurers have begun notifying policyholders of their (in the vast majority of cases) premium increases. That has led to a public debate about the size of those increases and whether and to what extent the Patient Protection and Affordable Care Act is responsible.

The problem with such assessments is that multiple factors, both health care related and even political, are affecting those premiums. Some of those variables are pushing premiums up and others down. Here's why:

ACTUARIAL ESTIMATES ARE AN EDUCATED GUESS

Actuaries set premiums for the upcoming year based on several factors, including the estimated ratio of sick and healthy people in a particular insurance pool, the kind of coverage policyholders want or have, the normal growth in health care costs, the impact of new federal and state government rules and regulations, and other factors.

The more years of experience actuaries have with a particular policy and the more stable the covered population, the easier it is to predict an appropriate premium. However, actuaries had ZERO experience with ACA's "metal plans" (Bronze, Silver, Gold and Platinum), plus the Department of Health and Human Services (HHS) and President Obama were making up or changing the rules as they went along—and still are.

More importantly, the ACA requires actuaries to abandon longstanding actuarial principles such as underwriting an applicant and assigning a premium based on the risk the person brings to the pool.

In short, actuaries were mostly guessing when they set their company's initial ACA premium rates. And the second year won't be much better.

FUTURE PREMIUMS CAN REFLECT PAST MISTAKES

If actuaries misprice policies one year, they may attempt to adjust for that mistake the next year, which could have a significant impact, up or down, on future premiums. So, for example, if some companies announced lower-than-average premium increases for 2015, it may be because they overpriced policies the first time—not because the ACA is holding costs down.

HHS HAS A 10 PERCENT RED-FLAG CAP

HHS Secretary Kathleen Sebelius had warned insurers that if they raised premiums more than 10 percent in one year, the agency would closely scrutinize their justifications. That's because such increases would undermine Obama's affordability promise.

Thus, it wasn't surprising when PricewaterhouseCoopers recently announced that average premium increases for 2015 appear to be in the 8 percent to 9 percent range in those states that have released that information. What insurer wants to antagonize heavy-handed regulators who can make its life, and business, miserable? Better to ask for an 8 percent increase two years, or more, in a row than 12 percent in one year.

POLITICIANS AND BUREAUCRATS ARE PRESSURING INSURERS TO KEEP PREMIUMS DOWN

We saw this in Massachusetts shortly after the passage of Romneycare. Health insurers asked for a premium increase and the state rejected the request. Governor Duval Patrick even leaned on the insurers to lower their rates—which they did.

Remember, Democrats who passed the ACA have a huge self-interest in making sure premiums are low—both for their reelection chances and because the government is on the hook to subsidize coverage for millions of Americans. The higher the premiums the more it costs the federal government (i.e., taxpayers)—and those who voted for the law. So expect the administration to use every tool at its disposal to try and force premiums lower.

SOME PEOPLE ARE STILL IN NONCOMPLIANT PLANS

In the confusion created by his waivers and postponements, Obama permitted people with plans that did not qualify under the ACA to keep them if their state insurance departments allowed it. Twenty-five states are allowing non-compliant plans to continue through 2015, and 21 through 2016. It appears that most of those plans will cost less than Obamacare-qualified plans.

Those non-qualified plans get lumped in with the qualified plans when assessing premium increases. The point is that the

existence of millions of non-qualified plans may be lowering the aggregate premium increase.

SOME STATES ALREADY HAD VERY HIGH RATES

Several states—e.g., New York, Massachusetts, New Jersey and several others—embraced many of the ACA's reforms in their individual health insurance markets years ago, like the requirement that health insurers selling in the individual market accept any applicant without medical underwriting. So the ACA may have had very little impact on their premiums, at least initially.

EASY PENALTY AVOIDANCE COULD AFFECT THE PARTICIPATION RATE

Reports recently said that exceptions and loopholes would allow perhaps as many as 90 percent of the uninsured to avoid paying the penalty for not having coverage.

If that estimate turns out to be accurate, look for a lot of young and healthy people to postpone getting coverage until they need it. That development could greatly increase the “adverse selection”—an unacceptably high percentage of sick people in the pool—which drives premiums up.

PERVERSE INCENTIVES BEHIND THE MEDICAL LOSS RATIO

The Obama administration is boasting that some policyholders are getting a check back from their health insurer—a result of the Medical Loss Ratio. The MLR provision says that insurers must spend a certain amount of their premiums—80 percent for smaller companies and 85 percent for large ones—paying claims. Thus, only 20 percent or 15 percent, respectively, can be used to pay administrative costs, commissions and profit.

Prior to the ACA, health insurers had an economic incentive to keep claims as low as possible; now they actually have an incentive to allow claims to rise because the more claims they pay the higher the premiums and the more money—in dollars, not percentage—they keep for administrative costs and profits.

LOWER PREMIUMS DON'T ALWAYS MEAN LOWER COSTS

There are a number of ways actuaries can adjust a policy in an effort to lower or maintain its premium level. They can raise the deductible, increase one or more copays, increase the level at which the insurer pays 100 percent of the costs, and narrow the network of providers, among other options—though all of these have to be done under the ACA's “actuarial equivalence” guidelines. In other words, actuaries can and do fine tune policies to keep premiums as low as possible, even when there is economic pressure to raise the premiums—or more precisely, because of upward economic pressures.

In addition, the ACA has three mechanisms intended to subsidize insurers that get a disproportionate share of expensive patients. Two of those mechanisms go away in a few years, which means premiums will likely rise significantly afterwards.

SHIFT TO HIGH DEDUCTIBLES WILL LOWER RATES

While most ACA provisions drive premiums up, some have the opposite effect. ACA premiums are so expensive that many participants are choosing very high deductible plans. Health Pocket Inc. found the average deductible for an individual in a Bronze plan was \$5,081, and \$10,386 for a family. It was \$2,907 for an individual in a Silver plan, and \$6,078 for a family.

That's actually a very positive step. High deductibles dramatically lower health care utilization and, just as importantly, they make patients cost-conscious and encourage them to seek value for their health care dollars. That practice puts downward pressure on premiums.

The irony is that shifting to high deductible coverage, in conjunction with a tax-free account like a Health Savings Account, has been part of every Republican plan for two decades. Most Democrats dislike high deductibles, and yet they are the ones responsible for driving so many Americans to high deductible plans.

CONCLUSION

There are multiple variables involved in setting premium rates, and trying to point to one or two insurers or states doesn't tell us much. The ACA's structure and disregard of actuarial principles will increase inefficiency and its inherent economic incentives will encourage more utilization, both of which will force health insurance premiums up, even as the government uses its political power to try and push them back down.

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