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To: ALL INTERESTED PARTIES

From: Department of Managed Health Care

The following is a brief summary of the comments and events that occurred during the Financial Solvency Standards Board (FSSB) meeting held on August 23, 2005.

I. Opening Remarks and Adoption of Meeting Minutes

Advisory Committee Chairperson Scott Syphax called the meeting to order at 10:00 A.M. The Board members unanimously approved minutes from the April 12, 2005 meeting.

II. SB 260 Regulations (Kevin Donohue)

The Office of Administrative Law approved our SB 260 regulations on August 9, 2005. The regulations became effective on September 9, 2005. First quarter reports were due November 15, 2005. These reports reflect business activity beginning July 1, 2005.

III. Presentations on the Growth of Consumer Driven Health Plans (CDHP) and Its Effects on California's Managed Care Delivery Model were provided.

A. Physician Group Perspective.

- From 2001 through 2004, there was an increase in PPO enrollment and a slight decrease for HMOs. Employer surveys indicate demand for consumer driven plans and Healthcare Saving Account (HSA) products will increase in the near future. Most applications for new health care products are being filed with the Department of Insurance (DOI) and not with Department of Managed Health Care (DMHC), suggesting a shift away from Knox-Keene HMOs. Employers are looking to shift costs through high deductible PPOs and fee-for-service systems.
- The delegated model does not currently have the ability to administer high deductible products.
- Health plans should be encouraged to develop new HMO products with higher levels of deductibles or higher levels of co-payment on the professional side and even deductibles on the institutional side, all in an effort to reduce the premium and remain competitive with PPO product offerings.

B. Broker Perspective.

- HSA is a tax-exempt trust or custodial account established exclusively for paying qualified medical expenses of the account beneficiary who, for the months for

which contributions are made to an HSA, is covered under a High Deductible Health Plan (HDHP).

- Tax Advantages of HSAs: Contributions are tax deductible. Contributions made by employers are not included in employee taxable income. Contributions are tax free when used for qualified medical expenses. Balance not spent rolls over on a tax-free basis, which can earn interest (similar to an IRA). The HSA is owned by the employee and remains the employees even after the employment relationship ends.
- How to Qualify for an HSA: need a qualified HDHP.
- Concern regarding funding for low or medium income employees, who may not participate due to competing financial obligations.

C. Provider Billing Perspective

- Providers have increased costs associated with insurance verification, benefits screening, collection of large deductibles, and an increase in account receivables and subsequent bad debt.
- The Risks: HDHP members may not have deductible set aside in an HSA or in savings of any form, which can result in enrollees not seeking care.
- Reimbursement complexity makes it difficult to estimate costs, especially for hospital providers.
- Increase in A/R Days for Providers. Patients are not required to abide by timely payment laws. Providers could require patients to pay up front, which could be problematic for high cost services.
- Patient deductibles for insurance companies that do not have contracts with providers will be based on full-billed charges.

D. Early Preliminary Data

- HSA Market is growing: In September 2004, there were 29 plans with a little over 400,000, by March of 2005 there were 99 plans with over a million enrollees. Clear trend for an increase in demand for these types of products.

E. Health Plan Perspective

- Market shift from HMO to PPO. From 01 through 04, there was an increase of PPO enrollment and a slight decrease of HMO. Employer surveys indicate that the number of enrollees in consumer directed health plans will dramatically increase in the near future.
- In California, high deductible products are somewhat problematic because the delegated model does not currently have the ability to administer deductibles.
- HMO v PPO Growth: From 2000 on, the growth rate in national health care expenditures is increasing at a greater rate than the consumer price index. This gap is increasing. HMOs became popular when the gap was narrowing.
- Cost increases are likely to continue, with some drivers being technology, hospital prices, and as well as an aging population.

- Employers have increased premiums and have increased the share that employees pay. In the future, employees will bear an increasing percentage of the cost of health care services.
- In order to meet market demands, there has recently been an increase in the number of types of products offered including Consumer Directed Health Plans, High Deductible Health Plans, and HSAs. Without these new types of products, employers may decide to forego coverage for their employees due to the continued increase in the cost of coverage.
- Mandated benefits, such as the ones in the Knox-Keene Act, increase the cost of coverage. Employers have options regarding the purchase of health care coverage. There is a "market" for regulatory oversight. Department of Insurance (DOI) regulation is less oriented to benefits than to the insurers' ability to meet financial obligations. If DOI establishes benefit levels similar to the benefit structure of Knox-Keene licensed plans, employers may switch to self-funded arrangements under ERISA, which has minimum requirements and may result in less comprehensive health care coverage for employees.

F. HSA Perspective

- Often, consumers do not understand how insurance works and are very much at risk of paying retail if billed at the point of care. Those who administer HSAs can review medical bills and can have extensive record keeping for their clients. They can also allow some directed investments, with HSAs looking like a medical IRA.
- Drivers include: overall increased healthcare cost; reducing the employer's cost/liability; encourage consumer cost-conscious behavior; employer interest in re-engineering health care and provider backlash against managed care. Providers, who do not want to be in managed care, want to be involved in a different kind of delivery mechanism.
- Benefit structure includes: high deductibles; maximum out-of-pocket; link to financial vehicles (HRAs, HSAs, FSAs); preventive care incentives; and individual choice.
- Funding options:

    - HRAs are health reimbursement accounts (regulated by the Department of Labor). The employer contributes to the account and owns the funds. The funds roll over, but the employee cannot take the funds when leaving the employer.
    - HSA is a health savings account that is regulated by the Internal Revenue Service. HSAs have certain tax advantages. Either the employee or employer can contribute, but the employee owns the funds. The funds roll over and the employee still owns the funds when leaving the employer. The funds can be invested. Annual contributions are limited to the amount of your HDHP deductible.
    - Flexible spending account, also regulated by the Department of Labor. Either the employee or the employer can contribute, but the employer owns

the funds. The funds do not roll over and the employee cannot take the funds when leaving the employer.

- The employer is shifting from being the primary purchaser to simply contributing financially to their employees' health coverage, and promoting self-service on the part of the consumer.
- Early Results with HRAs: Employers sponsoring CDHP with HRAs report a 50% decrease in overall medical spending.
- Consumers will be more involved in the decision process. Consumers will have financial incentive to control cost.

G. Consumer Perspective.

- Concern that a significant increase in co-pays or deductibles will result in patients skipping care or not filling prescriptions due to cost concerns, which could lead to more costly health care in the long term.
- This is a disproportionate impact on those needing chronic care. These new products shift costs to employees without a commensurate salary increase to offset the loss of benefits.

IV. Closing Remarks/Next Steps

The next meeting will be October 11, 2005 at the Burbank Hilton. (Note: The meeting was rescheduled for January 31, 2006, at the Burbank Hilton.)