



ISSUE Brief

Premium Stabilization Programs: How Reinsurance, Risk Corridors, and Risk Adjustment Protect Consumers

TWEETS

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- 3 interconnected programs - reinsurance, risk corridors, risk adjustment - protect consumers by stabilizing premiums
- In Medicare Part D, three risk mitigation programs created a thriving market that provides choices for consumers
- Issue Brief: Changes to reinsurance, risk corridors, risk adjustment will disrupt the market & increase premiums

KEY TAKEAWAYS



Three interconnected risk mitigation

programs - reinsurance, risk corridors, and risk adjustment - protect consumers from market volatility and help keep coverage affordable.



These programs were used successfully in

Medicare Part D to help create a thriving market noted for its highly competitive nature and choices for consumers.



Changes to how these programs work will disrupt

the market and lead to higher costs for consumers.

Background

Consumers benefit when the cost of health coverage is stable. Three programs are in place to help protect consumers by stabilizing premiums in the reformed health insurance marketplace created by the Affordable Care Act (ACA). Two of these programs (Reinsurance and Risk Corridors) provide much needed premium stability for consumers in the first three years of the law’s implementation. The third program (Risk Adjustment) is designed to permanently protect against adverse selection.

Together, these three programs—commonly known as the “3Rs”—have helped create a more stable and predictable environment for consumers purchasing health insurance coverage. The American Academy of Actuaries noted that the 3Rs facilitate “competition based on efficient care management and quality rather than risk selection.”¹ Similar programs successfully mitigated risk among private plans offered under Medicare. The 3Rs serve the same purpose for the ACA’s market reforms by creating confidence in the new marketplaces and stability in premiums for consumers.

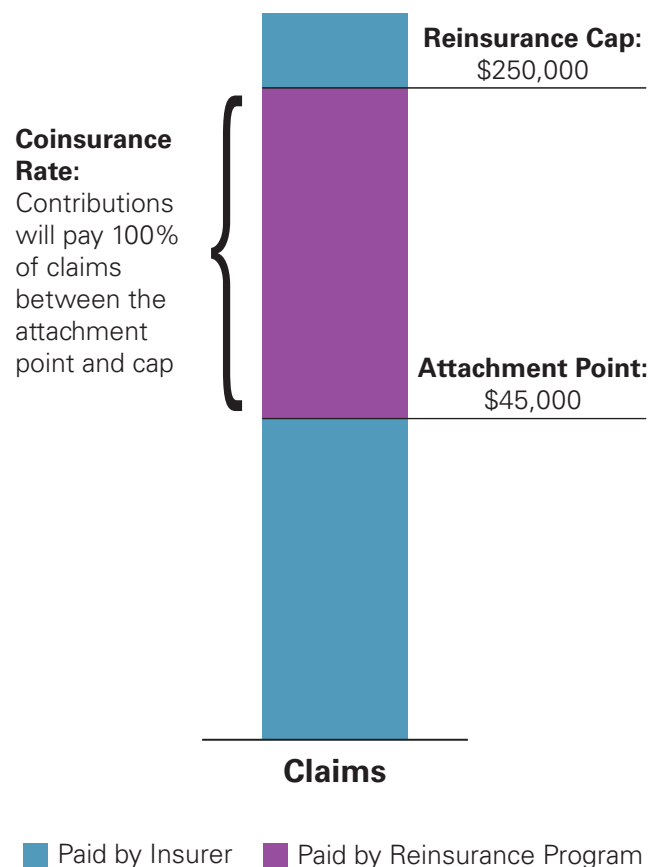
A Closer Look: How Do the 3Rs Work?

Reinsurance Program (2014-2016)

For each of the first three years of the ACA’s reformed marketplace, the law established a reinsurance fund used to cover a portion of the costs for individuals with very high medical expenses. Health plans provide funding for the program by contributing a set amount of money for each year of operation. In 2014, plan contributions totaled approximately \$9.7 billion, with just over \$7.9 billion paid out in reinsurance-eligible claims. The excess funds from 2014 will be used to cover high-cost claims in subsequent years. The program is set to collect \$6 billion and \$4 billion for the 2015 and 2016 benefit years, respectively.

After the close of the benefit year, the reinsurance program reimburses health plans for funds already spent on individuals with high medical spending, based on specific parameters. For 2014, the program paid for 100% of the medical costs between \$45,000 and \$250,000 for individuals in reinsurance-eligible plans (Figure 1).

Figure 1: 2014 Reinsurance Payment Parameters



The reinsurance program is helping health plans meet the needs of high-cost enrollees while making individual market premiums more affordable for consumers. The Department of Health and Human Services (HHS) estimated that the reinsurance program reduced premiums in the individual market in 2014 by 10%-15%, a higher rate reduction than would have occurred absent the program.² The magnitude of this effect will be muted in 2015 and 2016 because of lower reinsurance funding, thereby increasing premium rates as compared to the previous year.³

Federal Risk Corridors Program (2014-2016)

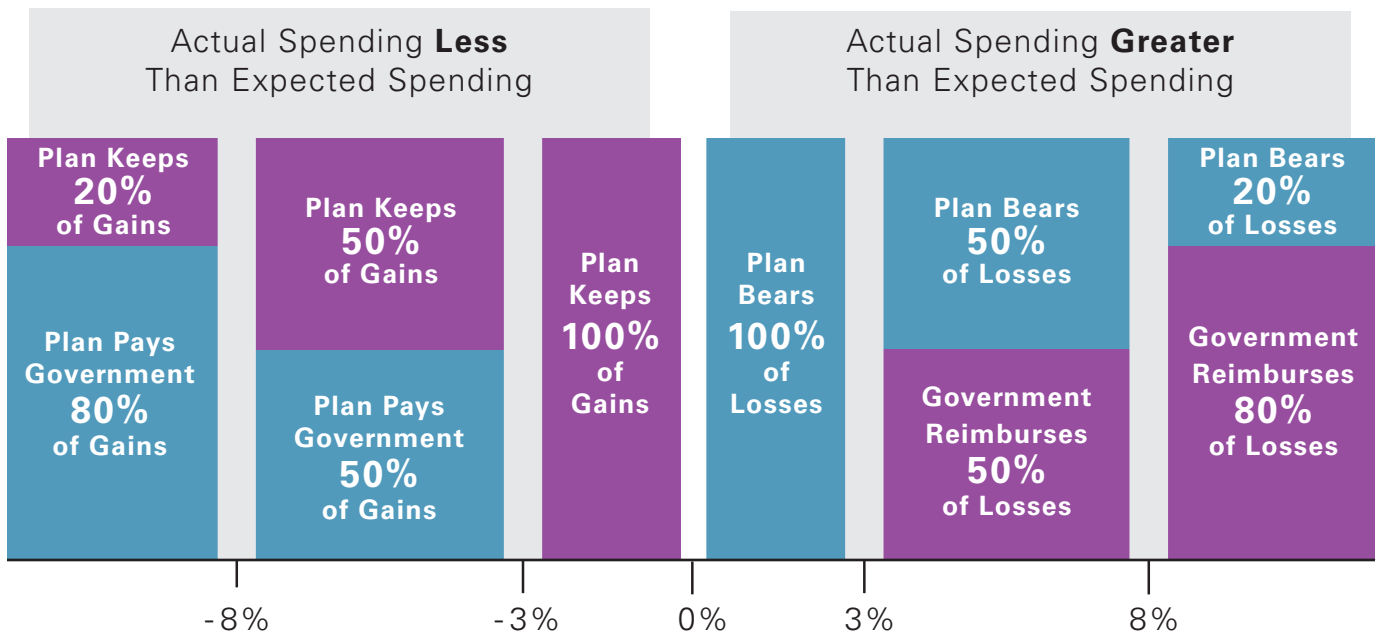
New benefit mandates, regulatory requirements, and the ACA's broad insurance reforms dramatically transformed the insurance marketplace in 2014. Although health plans made assumptions about the cost of coverage in this new market, it will take time for health plans to accurately predict how this new population will use health care services. The risk

corridors program was meant to limit volatility in the individual and small group markets during this transition, resulting in a more stable marketplace and options for consumers that accurately reflect the cost of coverage.

Under the statutory parameters of the risk corridors program, qualified health plans (QHPs) and the federal government share in the risk associated with the uncertainty of the new marketplace. If the amount a health plan collects in premiums exceeds their medical expenses by a certain amount, the plan will make a payment to the federal government. If premiums fall short of this target, the risk corridors program transfers a portion of this shortfall to the health plan (Figure 2).

Like the reinsurance program, the risk corridors program is designed to ease the transition between the old and new marketplace and help stabilize premiums for consumers. As health plans gain more experience setting premiums in this new market over time, the protections provided by risk corridors will become less critical for protecting market stability.

Figure 2: Difference Between Actual Medical Spending and Expected Medical Spending (as a percentage of expected medical spending)



Source: American Academy of Actuaries. Fact Sheet: ACA Risk-Sharing Mechanisms – The 3Rs (Risk Adjustment, Risk Corridors, and Reinsurance) Explained. December 2013.

After health plans finalized premiums and opened 2014 plans for enrollment, two developments altered assumptions about the risk pool of the reformed market and the structure of the risk corridors program. The first development was the transitional guidance, released in November 2013, allowing individuals to remain on their pre-ACA policies. In some markets, consumers could still be enrolled in these plans well into 2017. Changing the rules after premiums had already been set for 2014 introduced substantial uncertainty about the population that would ultimately enroll in ACA plans. To the extent that fewer young and healthy individuals chose to purchase coverage in a particular market due to these changes, health plans' would need to revisit their assumptions about the cost of coverage.

Second, Section 227 of the Consolidated and Further Continuing Appropriations Act of 2015, which was signed into law on December 16, 2014, prevents HHS from using taxpayer funds, including transferring funds from either the Hospital Insurance Trust Fund or the Supplemental Medical Insurance Trust Fund, for purposes of making payments to health plans under the risk corridors program.

Risk Adjustment Program (2014 and Subsequent Years)

The ACA's risk adjustment program is designed to spread risk among health plans to prevent problems associated with adverse selection. Under this program, health plans that enroll disproportionately higher risk populations (such as individuals with chronic conditions) will receive payments from plans that enroll lower-risk populations. Payments and transfers are only between health plans and do not involve federal funds. The risk adjustment program applies to individual and small group plans, both inside and outside of the Exchanges.

By spreading risk across all health plans in a state, risk adjustment promotes market stability as it protects consumers with complex medical conditions. Preventing adverse selection will lead to a more robust marketplace and more affordable coverage options for consumers.

First Year Results

On June 30, 2015, HHS released a report with state-level, health plan-specific data related to risk adjustment and reinsurance payments and charges for the 2014 benefit year.⁴ The report also included summary level data on both programs, including aggregate reinsurance metrics and the number of issuers participating in the risk adjustment program. Based on data from the first year of the reinsurance and risk adjustment, HHS noted that both these programs are working as intended – helping provide coverage to individuals with chronic conditions and protecting against adverse selection.

Preliminary estimates of nationwide 2014 risk corridors payments and charges were released on October 1, 2015. HHS will collect \$362 million from those health plans with less than expected medical spending. Under the parameters of the risk corridors calculation, HHS would pay out \$2.87 billion to those health plans with greater than expected medical spending. However, HHS will pay approximately 12.6% of the requested risk corridors payments. HHS stated that it will use collections from program years 2015 and 2016 for the remaining 2014 funds.

Health plans began receiving payments or invoices for charges under the 3Rs in September 2015 as part of the established monthly payment cycle for advance premium tax credits (APTC), cost-sharing reductions (CSR), and Exchange user fees. Payments and charges under the risk corridors program will be included as part of this payment cycle beginning in late 2015.

Precedent of Federal Risk Mitigation Programs: Medicare Part D

The federal government has employed mechanisms under several health coverage programs to promote a stable and competitive market. One such example is the Medicare prescription drug program (Medicare Part D), which may allow beneficiaries to enroll in prescription drug plans offered by private Part D sponsors.

Medicare Part D includes similar versions of the three risk mitigation programs under the ACA. All three programs are permanent features of the Part D program.

- The Centers for Medicare & Medicaid Services (CMS) provides reinsurance payments to Part D sponsors when a beneficiary’s prescription drug costs reach a catastrophic threshold, providing additional support to sponsors with high-cost enrollees.
- CMS administers a risk corridor program in which Part D sponsors share risk above and below predetermined payment-to-cost ratio thresholds established by law. The risk corridors have broadened over time, meaning Part D sponsors are more likely to be at full risk than they were during the initial years of the program.
- CMS reimburses Part D sponsors on a risk-adjusted basis that provides payments to Part D plans that enroll more individuals with complex conditions. This more accurately reflects the cost of addressing these beneficiaries’ health care needs. A similar system is used to risk adjust payments to Medicare Advantage plans.

Together, these programs have been instrumental in the creation of a new insurance market noted for its highly competitive nature and choices for consumers.

The Importance of the 3Rs

Health plans price their insurance policies based on a set of assumptions about the people who will enroll in coverage and an understanding of how the different parts of the ACA – including the 3Rs – interact. Changes to either these assumptions or understandings after premiums have already been set can have a profoundly disruptive impact on the market. The 3Rs are already working to create a more stable and affordable market for consumers.

Recommendation

Stable, affordable coverage for consumers depends on adequate funding of the 3Rs. It is critical that Congress and HHS ensure that the programs work as designed and consumers are protected.

End Notes

- 1 American Academy of Actuaries. Research Brief: Design and Implementation Considerations of ACA Risk-Mitigation Programs. June 4, 2012. http://www.actuary.org/files/A A A-SOA _research_brief_on_3R s_060412.pdf.
- 2 77 FR 73199, December 7, 2012.
- 3 The program will pay at least 50 percent of the costs between \$45,000 and \$250,000 in 2015 and at least 50 percent of costs between \$90,000 and \$250,000 in 2016. The American Academy of Actuaries estimates lower reinsurance funding in 2016 will likely reduce premiums by about 4 to 6 percent, compared to a reduction of 10 to 14 percent in 2014, and 6 to 11 percent in 2015. (American Academy of Actuaries Issue Brief: Driver of 2016 Health Insurance Premium Changes. August 2015. Available at: http://actuary.org/files/ Drivers_2016_Premiums_080515.pdf).
- 4 Available at: <http://www.cms.gov/CCIIO/Programs-and-Initiatives/Premium-Stabilization-Programs/Downloads/RI-RA-Report-Draft-6-30-15.pdf>

Related Topic

A Consumer Guide to Understanding Health Plan Networks, AHIP Foundation



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