

The Impact of Sen. John Kerry's Health Care Proposal on Health Care Costs

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Overview

Unrelenting health care cost increases, growth in the ranks of the uninsured and problems with the quality of care all continue to put enormous pressure on U.S. consumers, employers and others affected by the health care system.

Sen. John Kerry has proposed a health care initiative including provisions that will reduce overall health care costs while expanding health coverage and improving the quality of care.

I have previously estimated the Kerry health care initiatives overall would reduce the growth in health care spending and produce approximately \$300 billion in federal savings alone over the next 10 years (www.sph.emory.edu/hpm/thorpe/kerry4-4-04final1.htm).

In this paper, I focus on the additional employer/health plan savings and increased coverage for uninsured workers arising from the Kerry proposal to establish a federal stop-loss health care pool. As shown in the analysis beginning on page 2, this proposal would reduce the cost of private health insurance for employers and employees by another \$288 billion over the next 10 years.

Looking broadly at its impact, the Kerry health plan lowers the costs of private health insurance in a number of ways, including:¹

Reimbursing health plans for high-cost cases (the federal stop-loss or premium rebate pool). Under the Kerry stop-loss health care pool,

the federal government would reimburse eligible health plans (including self-insured plans) for 75 percent of catastrophic, high-cost cases. The pool is designed to reduce the cost of health care by approximately 10 percent.

Constraining the growth in prescription drug spending. The Kerry plan would require the secretary of Health and Human Services to negotiate prices with drug companies on behalf of Medicare recipients. This would have the residual effect of setting a trend in pricing for all other purchasers. The plan would also require transparency rules (for example, concerning rebates from manufacturers) for pharmacy benefit managers (PBMs) that do business with the federal government. The plan also invests in comparative effectiveness research that provides purchasers with the type of independent clinical information they need to leverage the best medications at the best prices on behalf of their clients. As it does this, the plan also promotes policies that will accelerate access to and use of quality generic drugs as well as to increase bulk purchasing of drugs at the state level.

Cutting health care administrative costs. Approximately 30 to 40 percent of health care transactions still rely on paper claims, which can cost \$5 to \$20 per transaction depending on the level of claims adjudication involved. Use of electronic claims that automatically adjudicate can cost as little as 50 cents per claim. Moving all health care transactions from a paper to an electronic platform would reduce health care spending.

Encouraging disease management programs.

Chronic diseases such as congestive heart failure, diabetes and hypertension are expensive and are key factors responsible for the growth in health care spending. These three conditions alone account for nearly 30 percent of health care spending.

Overall, spending on chronic disease may account for 80 percent of total spending in the Medicare program alone.² The Kerry proposal would encourage the broader use of disease management in public and private health insurance. Disease management (appropriately structured) in many cases has been found to reduce the cost of health insurance.³

Achieving savings through the reduction of uncompensated care burdens.

As health coverage substantially expands under the Kerry proposal, the need for special payments for uncompensated care associated with the previously larger number of uninsured will decline. Conservatively, savings that can be expected reach \$88 billion over the next 10 years.

Reducing the costs of malpractice. The Kerry health care plan seeks to reduce the frequency of frivolous malpractice claims and generally eliminate the use of punitive damages in medical liability cases.

I have estimated the potential savings associated with the bulk of these proposals elsewhere (see www.sph.emory.edu/hpm/thorpe/kerry4-4-04final1.htm).

Policy Rationale for a Public Stop-Loss Pool

The rising cost of health care, and what to do about it, is one of our most important health policy issues. Most current proposals for reducing health care costs would take time to implement and take several years to produce savings. In contrast, a federal stop-loss pool would generate immediate savings while longer-term cost control approaches are developed and implemented.

Stop-loss pools also play an important role in the insurance market. Health insurance premiums are

based on the average claims experience of those in a particular risk pool. The variance in health conditions among individuals leads to enormous and highly skewed differences in claims experience.

Most health care spending is generated by relatively few individuals. This distribution of spending creates strong incentives for health plans to segment people into different pools through underwriting and other administrative tools where possible to avoid these risks or drop them from coverage altogether. These administrative costs increase the costs of health insurance. Reducing the variation in claims in small groups would reduce the risk facing plans and the risk associated with providing (particularly small) employers health insurance.

Administrative costs are lower in larger insurance pools. One approach for reducing administrative costs facing smaller groups is to lower the costs associated with underwriting and reduce the risk facing health plans when insuring small insurance pools. One way to lower these costs is through the use of stop-loss pools. These pools reduce the risk facing health plans by reducing the variation in health care costs they would otherwise face. For instance, a stop-loss plan that pays 75 percent of claims above a catastrophic threshold would, on average, reduce the variance (variation) in claims costs by more than 50 percent. Based on the target reduction in health premiums of 10 percent, the threshold would work out to be \$30,000 in 2006 and \$50,000 in 2013. This is a substantial reduction in risk facing health plans that would translate into lower health insurance premiums. Thus, developing approaches for reducing health plan risk associated with high-cost cases can mitigate risk selection and potentially reduce administrative costs.

Lower administrative costs would reduce the overall cost of health insurance. Approaches such as a federal stop-loss pool should improve the efficiency and performance of our health care system. In short, a federal stop-loss pool is designed to achieve several goals:

a. Reduce health plan risk by reducing the variance in claims and ensuring greater cost

predictability for businesses and plans. Stop-loss pools along the lines proposed by Sen. Kerry could reduce the variance in claims experience by 50 to 60 percent per year, a significant reduction in risk facing private health plans today.

b. Reduce administrative costs and incentives to underwrite and screen enrollees, risk-select and segment populations.

c. Spread the burden of high-costs patients from a relatively small number of workers in each plan to a broader population base.

d. Allow higher risk patients to have broader choices of health plans (through the Federal Employee Health Benefits pools), the same as lower risk patients.

e. Reduce the disincentives to hire and retain older workers or those with disabilities who can and do make extraordinary contributions to the workforce.

A federal stop-loss pool in the health insurance market is not a new role for the federal government in the private insurance market. Indeed, the federal government currently assumes the risk for high-cost cases in several other private markets. For instance, the Federal Emergency Management Agency (FEMA) plays a key role in providing financial assistance for the private sector (households and businesses) facing catastrophic losses. Most recently, the federal government will assume 90 percent of the costs over \$10 billion associated with a terrorist attack—a key federal stop-loss role designed to reduce private insurance risk.

Impact of Sen. Kerry's Federal Stop-Loss Pool on Health Insurance Premiums

Methods

The Kerry health care plan establishes federal stop-loss payments (from a premium-rebate pool) that pay (on average) about 10 percent of the cost of insurance for eligible employers.⁴

To be eligible for the stop-loss payments under the plan, employers must meet three conditions. First, they must cover all workers in their firms. Second, employers must encourage the introduction of disease management programs as a part of their health plans. Third, as they meet the first two criteria, employers must illustrate how they will share in the savings in a manner that benefits workers and employers alike.

I assumed that employers would participate in the stop-loss pool if the costs of covering currently uninsured workers were less than the anticipated benefit, i.e., the expected savings from the Kerry stop-loss health care pool. The tables below reflect the annual expected savings accruing to health plans for employers participating in the Kerry stop-loss health care pool, the costs employers would incur to cover uninsured workers and the numbers of workers newly receiving health coverage. The net benefit (savings) for employers is the difference between their contributions to cover otherwise uninsured workers and the rebates they receive from the Kerry stop-loss health care pool.

Results

The results displayed in the following tables assume the plan is fully implemented in 2005. When fully implemented, the Kerry health care plan would provide nearly \$35 billion per year in premium rebate (stop-loss) payments to employers to reduce the cost of health insurance. Employers that voluntarily participate in the Kerry stop-loss health care pool are expected to provide health care to all their workers. Providing such coverage is projected to cost about \$8.2 billion, but the overall reduced costs/greater affordability would produce an estimated net benefit to employers of \$26.6 billion (see Table 1).

Overall, the Kerry health care plan could extend coverage to 26.7 million currently uninsured Americans. The stop-loss aspect of the plan would potentially extend insurance to about 3 million currently uninsured.⁵

Savings for several industries could be quite substantial under the Kerry health care plan. For

instance, the cost of health insurance provided in manufacturing firms could, on balance, decline by \$5.7 billion on an annual basis. Similarly, the costs of health insurance provided to state and local workers could, on balance, decline by \$5.6 billion per year. Table 1 provides a more detailed presentation of the Kerry stop-loss payment and savings by industry.

Table 2 presents illustrative savings under the Kerry health care stop-loss pool for an average firm with 25, 100 and 1,000 workers. Of course, actual savings will vary within these groups and across

industries. As shown in the table, a typical firm with 25 employees would save approximately \$4,190 per year; a firm of 100 would save \$25,530; and a firm of 1,000 would save nearly \$275,000 on health care spending.

Table 3 displays the impact of the Kerry health care plan by state. Under the Kerry stop-loss health care pool, employers' health insurance costs would decrease by \$4 billion in California, by \$2 billion in New York and by more than \$1 billion per state in Florida, Illinois, Michigan, Ohio, Pennsylvania, New Jersey, Georgia, North Carolina and Texas.

¹The specific provisions that would reduce the overall level of federal health care spending by about \$300 billion over the next 10 years are outlined in my recent study found at the website listed in the text. In addition, the stop-loss pool would reduce the cost of private health insurance by about \$288 billion over the 10-year period.

²For the noninstitutionalized population. Estimates from the Medical Expenditure Panel Survey, 2000.

³American Association of Health Plans/HIAA, *Cost Savings of Disease Management Programs: Report on a Study of Health Plans*, Washington, D.C., November 2003.

⁴The stop-loss plan is designed to reduce premiums by an average of 10 percent. Each year an appropriate attachment point (for example, a dollar figure such as \$50,000) would be selected to produce these savings.

⁵Some of these newly insured—about 1 million—are likely to be covered through other components of the Kerry proposal. Thus the estimates here are an upper estimate of the costs incurred by employers to qualify for the stop-loss pool.

Table 1.
Annual Employer Benefit (\$\$ Savings) Under Kerry Stop-Loss Health Care Pool

Industry and Firm Size	\$ In Millions			
	Kerry Stop-Loss Payments to Employers	Employer Costs to Covering Uninsured Workers	Number of Workers Gaining Coverage	Net Benefit to Employers (\$\$ Savings)
ALL INDUSTRIES				
<24	\$1,746.9	\$1,246.1	457,231	\$500.8
25-99	\$4,174.6	\$1,513.1	562,260	\$2,661.6
100-499	\$6,931.8	\$1,754.5	660,736	\$5,177.3
500-999	\$2,767.6	\$498.2	178,785	\$2,269.4
1,000+	\$19,222.9	\$3,236.3	1,244,154	\$15,986.6
Total	\$34,843.9	\$8,248.2	3,103,166	\$26,595.7
MANUFACTURING				
<24	\$309.9	\$249.3	84,300	\$60.5
25-99	\$1,016.5	\$415.9	145,100	\$600.6
100-499	\$1,602.8	\$330.1	114,832	\$1,272.7
500-999	\$628.4	\$49.3	21,547	\$579.0
1,000+	\$3,520.5	\$268.8	95,879	\$3,251.7
Total	\$7,078.1	\$1,313.5	461,658	\$5,764.6
CONSTRUCTION				
<24	\$234.4	\$140.7	58,352	\$93.7
25-99	\$642.4	\$272.7	99,025	\$369.6
100-499	\$466.0	\$174.2	69,476	\$291.9
Total	\$1,342.8	\$587.6	226,853	\$755.2
TRANSPORTATION/COMMUNICATION				
<24	\$120.3	\$113.9	41,312	\$6.4
25-99	\$220.5	\$86.3	29,460	\$134.2
100-499	\$279.0	\$166.1	49,024	\$112.9
500-999	\$89.2	\$31.9	8,955	\$57.3
1,000+	\$1,644.7	\$276.9	86,943	\$1,367.7
Total	\$2,353.7	\$675.1	215,694	\$1,678.6
WHOLESALE				
<24	\$29.4	\$21.7	9,409	\$7.7
25-99	\$138.1	\$52.3	22,029	\$85.8
100-499	\$297.2	\$53.0	16,004	\$244.3
500-999	\$121.0	\$27.9	8,547	\$93.1
1,000+	\$384.2	\$92.8	32,999	\$291.4
Total	\$969.9	\$247.6	88,988	\$722.3

Industry and Firm Size	Kerry Stop-Loss Payments to Employers	Employer Costs to Covering Uninsured Workers	Number of Workers Gaining Coverage	Net Benefit to Employers (\$\$ Savings)
FINANCIAL/INSURANCE/REAL ESTATE				
<24	\$75.8	\$45.1	15,025	\$30.7
25-99	\$315.6	\$126.0	43,855	\$189.6
100-499	\$610.2	\$150.4	61,229	\$459.8
500-999	\$294.9	\$43.8	21,066	\$251.1
1,000+	\$2,455.4	\$499.3	206,513	\$1,956.1
Total	\$3,752.0	\$864.5	347,688	\$2,887.5
RETAIL				
<24	\$184.6	\$121.4	46,202	\$63.2
25-99	\$446.8	\$126.9	61,724	\$319.9
100-499	\$456.0	\$95.2	39,153	\$360.9
500-999	\$157.7	\$77.9	30,496	\$79.8
1,000+	\$1,757.5	\$709.2	297,797	\$1,048.3
Total	\$3,002.7	\$1,130.6	475,372	\$1,872.1
PROFESSIONAL SERVICES				
<24	\$339.0	\$265.7	94,186	\$73.3
25-99	\$641.2	\$175.5	68,855	\$465.8
100-499	\$1,004.7	\$272.4	90,317	\$732.4
500-999	\$379.4	\$109.6	32,851	\$269.8
1,000+	\$1,660.0	\$344.0	142,159	\$1,316.0
Total	\$4,024.3	\$1,167.1	428,367	\$2,857.2
OTHER SERVICES				
<24	\$414.6	\$254.2	99,966	\$160.4
25-99	\$505.9	\$174.9	60,690	\$331.1
100-499	\$1,185.0	\$441.5	194,916	\$743.6
500-999	\$522.6	\$83.8	28,722	\$438.8
1,000+	\$3,224.0	\$467.9	174,406	\$2,756.1
Total	\$5,852.2	\$1,422.3	558,700	\$4,429.9
STATE AND LOCAL WORKERS				
<24	\$6.4	\$2.8	990	\$3.6
25-99	\$199.2	\$64.9	23,311	\$134.4
100-499	\$1,030.7	\$71.8	25,787	\$958.9
500-999	\$574.5	\$74.0	26,601	\$500.5
1,000+	\$4,576.6	\$577.3	207,458	\$3,999.3
Total	\$6,387.4	\$790.7	284,147	\$5,596.7
AGRICULTURE/FISHERIES				
<24	\$32.5	\$31.4	7,489	\$1.1
25-99	\$48.3	\$17.8	8,210	\$30.5
Total	\$80.8	\$49.2	15,699	\$31.6

Table 2.
Examples of Employer Annual Benefit (\$\$ Savings)
Under Kerry Stop-Loss Health Care Pool, by Firm Size

	25	Firm Size* 100	1000
Total Spending 2005	\$99,625	\$415,000	\$4,330,000
Total Spending 2006	\$107,500	\$448,000	\$4,676,400
Total Spending 2006 with Kerry Plan	\$103,310	\$422,470	\$4,403,610
Savings	\$4,190	\$25,530	\$272,790

* Average for all firms. Results will vary by industry and within firm category.

Table 3.
Total Employer Benefit (\$\$ Savings) by State Under Kerry Stop-Loss Health Pool

\$ In Millions

State	Kerry Stop-Loss Payments to Employers	Employer Costs to Covering Uninsured Workers	Number of Workers Gaining Coverage	Net Benefit to Employers (\$\$ Savings)
Alabama	\$537.9	\$107.1	43,994	\$430.8
Alaska	\$75.9	\$35.1	9,985	\$40.8
Arizona	\$563.4	\$151.3	45,821	\$412.1
Arkansas	\$282.1	\$60.0	22,437	\$222.1
California	\$4,055.5	\$1,087.1	453,208	\$2,968.4
Colorado	\$561.7	\$176.2	65,626	\$385.5
Connecticut	\$424.7	\$90.5	26,446	\$334.2
Delaware	\$106.0	\$12.2	4,879	\$93.7
District of Columbia	\$90.5	\$15.5	6,460	\$75.0
Florida	\$1,699.6	\$579.5	205,558	\$1,120.1
Georgia	\$1,172.8	\$229.4	106,635	\$943.4
Hawaii	\$137.0	\$26.5	8,472	\$110.5
Idaho	\$151.5	\$38.4	14,074	\$113.0
Illinois	\$1,598.7	\$380.4	127,161	\$1,218.3
Indiana	\$832.9	\$148.9	62,353	\$684.0
Iowa	\$396.7	\$48.1	25,204	\$348.6
Kansas	\$331.6	\$37.7	15,774	\$293.9
Kentucky	\$515.8	\$83.6	32,864	\$432.2
Louisiana	\$451.4	\$147.7	74,212	\$303.7
Maine	\$150.1	\$39.2	13,955	\$110.9
Maryland	\$733.1	\$162.6	70,904	\$570.6
Massachusetts	\$804.4	\$163.9	61,870	\$640.5
Michigan	\$1,258.6	\$199.4	82,213	\$1,059.2
Minnesota	\$752.1	\$127.6	50,013	\$624.5
Mississippi	\$336.5	\$93.4	40,246	\$243.1
Missouri	\$731.4	\$98.4	35,990	\$633.0
Montana	\$83.9	\$24.3	7,383	\$59.5
Nebraska	\$210.5	\$45.4	17,605	\$165.1
Nevada	\$287.8	\$84.2	29,962	\$203.6
New Hampshire	\$168.7	\$21.7	8,380	\$147.0
New Jersey	\$1,105.8	\$344.2	109,188	\$761.6
New Mexico	\$182.3	\$66.5	28,231	\$115.7
New York	\$2,172.2	\$573.0	188,941	\$1,599.2
North Carolina	\$1,100.7	\$209.5	74,371	\$891.2
North Dakota	\$71.8	\$13.8	5,427	\$58.0
Ohio	\$1,496.9	\$296.4	116,943	\$1,200.5
Oklahoma	\$384.8	\$89.0	36,047	\$295.8

State	Kerry Stop-Loss Payments to Employers	Employer Costs to Covering Uninsured Workers	Number of Workers Gaining Coverage	Net Benefit to Employers (\$ Savings)
Oregon	\$412.7	\$99.6	38,943	\$313.1
Pennsylvania	\$1,501.3	\$276.9	102,934	\$1,224.4
Rhode Island	\$125.4	\$26.5	10,830	\$98.9
South Carolina	\$500.0	\$78.0	31,722	\$421.9
South Dakota	\$92.9	\$29.7	9,517	\$63.1
Tennessee	\$694.3	\$185.9	57,247	\$508.3
Texas	\$2,528.9	\$862.1	311,096	\$1,666.7
Utah	\$254.9	\$87.5	31,567	\$167.5
Vermont	\$74.1	\$10.4	3,577	\$63.7
Virginia	\$918.0	\$167.4	61,836	\$750.6
Washington	\$769.8	\$141.0	51,132	\$628.8
West Virginia	\$172.1	\$44.2	18,584	\$127.9
Wisconsin	\$723.7	\$115.1	39,469	\$608.6
Wyoming	\$58.6	\$16.0	5,876	\$42.6
Total	\$34,843.9	\$8,248.2	3,103,166	\$26,595.7