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Reinsurance and the Federal Government

One percent of the population accounts for about 28 percent of all medical expenses. That's a $50,000 threshold (the top 2 percent have a $30,000 threshold).

That fact has led some to suggest that if the government were to pick up part or all of the costs of the small percentage of people responsible for much of the health care spending — in essence, becoming the national reinsurer — premiums would decline and health insurance coverage would increase.

Proposals that would make the government the national health reinsurer aren't new. They go back to President Dwight Eisenhower. And the government currently acts as a reinsurer in some areas of property and casualty insurance, the secondary mortgage market and in parts of the Medicare program.

However, national health reinsurance proposals are finding new support, from Democrats and even some Republicans. Is a federal health reinsurance program an idea whose time has come?

The Federal Government as Reinsurer. The federal government has been involved in sponsoring or assuming excess risk in a number of areas for more than half century. Many are familiar with the government's role in the property and casualty areas.

Property and Casualty Reinsurance:

- **Disaster Relief (1950)** — A fund allowing the president to decide which disasters qualify.
- **National Flood Insurance Program (1968)** — Led to a federal effort to identify the nature and extent of flooding risk in various areas as well as provide a private market for flood insurance.
- **Disaster Relief Act (1970)** — Expanded previous law to include grants for temporary housing and legal services.
- **National Flood Insurance Program** — The program was placed under the Federal Emergency Management Agency (FEMA) in 1978 and became an all-federal program. It was restructured in 1983 as a federal-private program. Insurers sell and service flood insurance policies while the federal government holds all the risk.
- **Terrorism Risk Insurance Act of 2002 (TRIA)** — Enacted after 9/11. The federal government pays 90 percent of the cost of any terrorist attack after losses exceed $10 billion.

  Of course, the concern in the property and casualty industry is that a catastrophe — whether natural or by terrorists — could affect thousands and even millions of people and billions of dollars in property. Health insurers, by contrast, are usually dealing with a relatively small number of people whose costs run under $1 million, and not billions of dollars.

Medicare:

- **Prospective Payment System (1983-84)** — Outlier payments for higher-than-expected hospital costs and/or length of stay. Medicare pays hospitals 80 percent of costs above an outlier threshold.
- **Medicare Reform Proposal (1990)** — Proposed (not passed) outlier pool funded from the Medicare trust fund that would have paid 45 percent of the cost of HMO Medicare enrollees with expenditures above $50,000.
- **Medicare Modernization Act (2003)** — Created "risk corridors." If an insurer has an individual with expenses in excess of a complicated cost formula, the Centers for Medicare and Medicaid Services (CMS) provides a reinsurance payment.

Reinsurance Industry vs. Federal Government

Service	Reinsurance Industry	Federal Government
Financial (ceding all or part of the risk)	Yes	Yes
Integrated Reinsurance Programs	Yes	No
Medical Management Support Services	Yes	No
Acute/Chronic Medical Management	Yes	No
HMO Insurer Insolvency Coverage	Yes	No
Transplant Networks	Yes	No
High Risk Pregnancies & Infants Program	Yes	No
High Cost Drug Discounts	Yes	No

Proposed Federal Reinsurance Legislation. The notion of a federal reinsurance mechanism for high health care costs is not a new idea. However, proposals have dramatically increased in the past few years.

Eisenhower Administration — Proposed to deal with the private sector's risk-adverse behavior in health insurance by creating a government-sponsored reinsurance program analogous to the Federal Housing Authority. The Nixon administration also looked at a somewhat similar proposal.

The Health Care Refinancing Act of 1996 — This legislation from Sen. Jim Jeffords (R-VT) established a Federal Health Reinsurance Corporation (a wholly owned government corporation) to provide reinsurance limited to a list of reimbursable events as determined by the Corporation.

The Better Health Act of 2003 — Medical malpractice legislation from Sens. Dick Durbin (D-IL) and Lindsey Graham (R-SC) containing provisions that would have instructed the Department of Treasury to study the establishment of a Federal Reinsurance Fund to be used for reinsuring malpractice costs.

Presidential Candidate Sen. John Kerry's (D-MA) Election-Year Health Reinsurance Proposal (2004) — The federal government would reimburse employer insurance plans for 75 percent of per-person costs that exceeded $50,000 a year. Two independent analyses found the policy could reduce annual premiums by 10 percent. However, an American Enterprise Institute study estimated the proposal would cost $573 billion over 10 years. Emory University health economist Ken Thorpe estimated the cost at $257 billion over 10 years — although he also claims it would have saved businesses and employees $288 billion in premiums.

New England Journal of Medicine Article by Senate Majority Leader Bill Frist (R-TN) (January 2005) — Sen. Frist's proposal discussed a new national publicly chartered, privately run "Healthy Mae" program. Healthy Mae was supposed to help insurers more broadly share risk and reduce administrative costs by creating a secondary market for health insurance, just as Fannie Mae does for home mortgages. One goal was to make health insurance, particularly in the individual market, more stable and affordable. No legislation was introduced.

Small Employers Health Benefits Program Act of 2006 (S.2510) — This legislation, introduced by Sens. Dick Durbin (D-IL) and Blanche Lincoln (D-AR) would have established a national health insurance program to offer private health benefits to small business employees. It also included tax credits for small employers who contributed a significant share of certain employees' premiums. And the federal government would establish and operate a reinsurance fund to cover up to 80 percent of the amount in claims exceeding $50,000.

Other Calls for Federal Reinsurance. In addition to proposals recommended or introduced by lawmakers, other groups have thrown their support behind federal reinsurance efforts. For example:

- Families USA recently sponsored a nationwide call that featured Harvard School of Public Policy economist Katherine Swartz to discuss her latest book, *Reinsuring Health* (June 2006), in which she concludes: "The economy and society as a whole have gained in untold ways from the stability in these markets brought about by government assumption of their greatest risks. The same could be true of health insurance markets."
- In addition, the three major U.S. automakers, struggling under very high employee health insurance costs, have asked the government for help. One proposed solution would be for the government to take on the high-cost patients, in essence becoming a reinsurer.

Other articles, conferences and white papers continue to appear from a number of organizations and health policy experts calling on the federal government to step into reinsurance.

But Why? Overlooked in the growing calls for the federal government to become the national reinsurer is the question why? There is a private health reinsurance industry that works very well, and it functions very differently from the property and casualty reinsurance industry, where a terrorist attack could lead to astronomical claims and the insolvency of the industry. This is not the case in the health reinsurance sector. Private reinsurers have invested heavily to provide additional medical management support services which improve the quality of care for those with chronic illnesses and catastrophic injuries — and save hundreds of millions of dollars in the process. There is no danger of default in this reinsurance sector, like that in property and casualty.

While reform proponents claim that health insurance premiums would go down if the federal government picked up the largest bills, those costs would simply be shifted to taxpayers. There are no real "savings." Premiums would simply be paid to the federal government instead of a health reinsurer. Moreover, since the federal government would not engage in chronic and catastrophic medical case management as effectively as private sector reinsurers, a federal reinsurance program would likely increase health care spending and reduce the quality of care in the long run.

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