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Navigating Cost-Sharing Reduction Subsidy Defunding

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As part of the Affordable Care Act (ACA), carriers in the individual market are required by law to offer silver plans to eligible individuals with richer benefits than a standard silver plan, with the requirement that the carrier must charge the same premium as the standard plan. These richer benefit plans for lower-income enrollees are referred to as cost-sharing reduction variant (CSR) plans. Before October 2017, carriers used to be refunded by the federal government for the increased benefits offered in the CSR plans; however, the Trump administration ended these subsidies. As a result, issuers needed to account for the additional benefits in their premiums moving forward. This paper will examine why CSR defunding produces pricing uncertainty and how regulators can possibly alleviate these risks.

A standard silver plan has a federal actuarial value (AV) of approximately 70 percent, meaning that on average, the plan pays 70 percent of the medical costs, while the enrollees pay 30 percent. Enrollees in the income-based CSR plans will generally pay fewer out-of-pocket expenses than a standard silver plan. There are three types income-based CSR variants with AVs of 73 percent, 87 percent, and 94 percent (see Table 1). Eligibility for each of the cost-sharing variants depends on an enrollee's income, defined as the family's income in relation to the federal poverty level (FPL).[1] In 2017, CSR enrollees represented approximately 60 percent of the overall exchange population, as the enhanced cost sharing was a major driver of enrollment.[2]

Table 1
Enrollment in CSR Plans by Eligible Income (2017)

Eligible Income (FPL)	Corresponding CSR Variant AV	Percent of Eligible Enrollees in CSR Plan
200%–250%	73%	71%
150%–200%	87%	85%
100%–150%	94%	91%

Based on 2017 Open Enrollment report, limited to *Healthcare.gov* states.

THE NEW WORLD: COST-SHARING SUBSIDIES NO LONGER REIMBURSED BY THE FEDERAL GOVERNMENT

In October 2017, the Trump administration stopped funding carriers for the CSR plans. Consequently, the CSR liability was transferred from the government to the carrier and, therefore, has to be considered in the carrier's premiums.

The lack of CSR funding creates the following pricing risks:

- Increased sensitivity to how a product will be competitively positioned, as small differences in premiums could yield large liability changes.
- Increased need to understand premium differences among the metal levels given the increased chance for metal shifting.

While we do not explore it in this article, carriers need to understand how risk adjustment may differ as a result of these two pricing risks.

WHAT HAVE CARRIERS DONE TO ACCOUNT FOR THE UNFUNDED CSR LIABILITY?

In 2018, many carriers adjusted their premiums to account for the increased CSR liability (except when disallowed by state regulators). The methodology on how plans were loaded varied, but the two primary methods were as follows:

- Carriers loaded the CSR liability onto on-exchange silver premiums but not onto any other metal levels.[3]
- Carriers loaded premiums across all metals,[4] on and off exchange, to account for the CSR liability.

For 2019 pricing, the vast majority of states instructed carriers to load on-exchange silver plans. When carriers loaded only on-exchange silver premiums to cover the CSR liability, there were two related effects. First, the advance premium tax credit (APTC) increased, which provided APTC-eligible consumers with more APTC dollars. This increase in silver premiums, relative to other metal levels, allowed consumers to have lower premiums if they purchased a non-silver plan. In effect, this meant that bronze and gold net premiums were often lower for subsidy-eligible enrollees.[5] This resulted in some consumers shifting from silver to bronze or gold. As shown in Table 2, the increase in APTC subsidies made a substantial impact on a consumer's decision to select a silver plan, particularly if the consumer was not eligible for an 87 percent or 94 percent CSR plan.

Table 2
Enrollment in Silver Plans by FPL (2017, 2018)

Enrollee Income (FPL)	Percent of Enrollees That Enrolled in Silver (2017)	Percent of Enrollees That Enrolled in Silver (2018)
250%–400%	53%	35%
200%–250%	71%	53%
150%–200%	85%	79%
100%–150%	91%	89%

Based on 2017 and 2018 Open Enrollment report, limited to *Healthcare.gov* states.

UNDERSTANDING THE PRICING UNCERTAINTY INTRODUCED BY CSR LOADING

To illustrate the pricing risk that loading premiums to cover the CSR liability creates, we have created a simplified market. The market has the following conditions:

- There are two carriers.
- Both carriers have identical plan designs and networks.
- The carriers assumed they would maintain their CSR and non-CSR historical enrollment when pricing.
- Policyholders purchased the plan with the lowest premium available to them.

Table 3 shows what would happen if Carrier A had filed a premium rate of $511[6] per member per month (PMPM) and Carrier B had filed a premium rate of $646[7] PMPM. All policyholders, assuming they act rationally, would select Carrier A's plan.

As you can see, Carrier A had a shortfall of $68 PMPM, since only $511 PMPM was received for the expected $579 PMPM in claim liabilities. In addition, Carrier B had no enrollees, which may result in Carrier B exiting the market or pricing aggressively in future years to gain enrollment. While this scenario is illustrative and arguably extreme, it does highlight a key feature of the individual market: Slight differences in premiums can produce large differences in enrollment and profitability.

This example is further complicated by the fact that the pricing differences between the second-lowest-cost silver and other metal levels could also cause metal shifting. For example, if the lowest-cost gold plan were cheaper than the second-lowest-cost

Table 3
CSR Loading in a Two Carrier, One Metal Market, With Rationale Policyholders

Metal Tier	Insurer	Member Months	Premium for Silver 70%	CSR Liability	Premium Charged	Funding Surplus
Silver 70%	Carrier A	100	$500	$0	$511	$11
Silver 73%	Carrier A	100	$500	$21	$511	($11)
Silver 87%	Carrier A	100	$500	$121	$511	($111)
Silver 94%	Carrier A	100	$500	$171	$511	($161)
Composite*	Carrier A	400	$500	$79	$511	($68)
Composite	Carrier B	0	n/a	n/a	n/a	n/a
Composite	Total	400	$500	$79	$511	($68)

*Calculated on a per member per month basis.

silver, there could be significant migration into gold plans (thus increasing plan liability).

Finally, the additional plan liability due to CSR defunding exacerbates the underlying dynamic of the individual market. In theory, risk adjustment is expected to somewhat compensate carriers for differences in anticipated liability; however, the ACA risk adjustment program assumes in aggregate that issuers have priced sufficient premiums to cover aggregate claims, which may not be the case if plans misprice for CSR defunding.

The impact of CSR liability loading will take some time to be fully understood and could result in differing levels of profitability based on a carrier's membership mix. This is something that both carriers and regulators should understand when reviewing financial results.

HOW COULD REGULATORS MITIGATE THE PRICING RISK?

Consideration of only loading silver on-exhange plans and leaving other plans unaffected could result in the following benefits:

- Allowing subsidy-ineligible enrollees to access an affordable silver plan off exchange.[8]
- Increasing the APTC credit for all policyholders on exchange.
- Avoiding an increase in cost to other metal levels.
- Reducing the incentive for member disenrollment.
- Helping maintain the overall risk-pool health.

It is important to note that the loading of CSR liabilities only onto on-exchange silver plans does produce some pricing uncertainties that could be mitigated by regulators. Three alternatives that regulators could consider follow.

Alternative 1: Quantify and Modify the Risk Adjustment CSR Load

Risk adjustment is designed to compensate carriers for actuarial risk. However, the ACA risk adjustment model was designed before the defunding of CSR payments. CMS could study to what extent the current model is appropriately compensating carriers in this new world. To the extent that CSR variant plans are being under- or overcompensated, the methodology should be updated. Given the time lags involved in updating the risk adjustment methodology, additional steps may be necessary for the short term.

Alternative 2: Allow for the Filing of Multiple CSR Liability Loads

A regulator could allow carriers in the market to file what their premium load would be based on their final competitive positioning. Although this places greater burden on regulators and carriers, it may be an alternative to ensure adequate premiums. For example, a regulator could ask carriers to submit all of the following with their rate filing:

- CSR load if the lowest silver.
- CSR load if the second-lowest (benchmark) silver.[9]
- CSR load if more than 10 percent above the benchmark.[10]
- Any other condition(s) prescribed by the regulator.

Based on the submissions, regulators could select pricing to maintain appropriate premium levels for expected claims costs.

Alternative 3: Prescribe the CSR Load

Regulators could instruct all carriers to load silver premiums by a fixed percentage, removing uncertainty and creating a level playing field when filing rates. The percentage used would have to be state specific and require somewhat advanced projections to account for morbidity and metal shifting. By ensuring sufficient premiums, it is more likely that risk adjustment will effectively compensate issuers given that, in aggregate, premiums will be sufficient for the statewide liability.

CONCLUSION

Early financial results appeared favorable for carriers in 2018; Fiedler suggests that carriers will earn positive underwriting

profit margins of 10.5 percent of premium, up from 1.2 percent in 2017.[11] However, premiums could be lower if some uncertainty were reduced. We believe one of the sources of this uncertainty is CSR loading. This article highlighted some of the issues that CSR loading causes issuers and how regulators can further mitigate pricing risks for their states.

The pricing risk from CSR loading remained when pricing 2019 premiums, but for pricing 2020 premiums, regulators may be better prepared to implement alternative methods to mitigate the pricing risks that CSR defunding creates. More research could be completed to better understand the implications of CSR defunding; in the meantime, we hope this paper creates a better understanding of the risks caused by CSR defunding and potential solutions. ■

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ENDNOTES

1 Carriers must also provide cost-sharing reduction plan variants for American Indians or Alaska Natives, regardless of income. For purposes of this paper CSR variant will refer only to income-based CSR variant.

2 Based on the 2017 Open Enrollment report, limited to states without a state-based exchange (SBE). SBEs do not report their CSR plan statistics to a federal database in the federal report used in this analysis. Some SBE states do make this information available through their exchange.

3 There was a variation of this loading in which states required a "substantially similar" off-exchange plan that did not get the premium load.

4 The inclusion or exclusion of catastrophic in all metals varied by state.

5 Assuming a bronze premium is $250 without APTC applied, if your APTC increased from $200 to $240 because of silver loading, your bronze premium would decrease from $50 to $10, further incentivizing buying bronze if you are relatively healthy.

6 Based on historical enrollment, assumed mix 50 percent Silver 70 percent and 50 percent Silver 73 percent.

7 Based on historical enrollment, assumed mix 50 percent Silver 87 percent and 50 percent Silver 94 percent.

8 Assuming stand-alone off-exchange silver plans are offered.

9 The benchmark plan or the plan at which APTC amounts are determined. Technically the benchmark plan is set as the Essential Health Benefits portion of a premium. Regulators would need to take this distinction into account.

10 Ten percent is an arbitrary number but, market dependent, could be when a plan starts becoming uncompetitive. As plans vary in network breadth, carrier reputation, county availability and other factors, there is certainly not a one-size-fits-all solution.

11 Fiedler, Matt. How would individual market premiums change in 2019 in a stable policy environment? *Brookings Institution*, August 1, 2018, *https://www.brookings.edu/research/how-would-individual-market-premiums-change-in-2019-in-a-stable-policy-environment/* (accessed December 20, 2018).