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Commissioner David Jones
State of California Department of Insurance
300 Capitol Mall, Suite 1700
Sacramento, CA 95814

Re: Proposed Acquisition of Health Net Life Insurance Company by Centene Corporation

Dear Commissioner Jones,

I very much appreciate the opportunity to write on the potential impact of the proposed acquisition of Health Net Life Insurance Company by Centene Corporation on consumers and competition in California. I am a professor of law at the University of California Hastings College of the Law and the Associate Dean and Co-Director of the UCSF/UC Hastings Consortium on Law, Science and Health Policy. I have written and taught in the field of health law and policy for the last seven years. I am also the Co-Founder and Executive Editor of The Source on Healthcare Price and Competition, a free and independent academic website devoted to issues of health care prices, costs, and markets. In September 2015, I testified before the U.S. House of Representatives Judiciary Committee's Subcommittee on Regulatory Reform, Commercial and Antitrust Law regarding the potential impact of the proposed mergers of Aetna and Humana and Anthem and Cigna on consumers and competition in the U.S. health care system. My brief letter aims to provide insight to the consumer risks associated with health insurance mergers and put the potential merger of Centene and Health Net into a broader national context.

Introduction

The United States has experienced more than a 400 percent increase in total health care expenditures since 1990.¹ By 2014, health care expenditures exceeded \$3 trillion and represented 17.5 percent of our GDP. Private insurance premiums are at their highest levels in history (\$17,545 for the average family).² One of the reasons our health care costs so much is that we overpay for health care

¹ Center for Medicare and Medicaid Services, National Health Expenditures 2014, Aggregate and Per Capita Amounts available <https://www.cms.gov/research-statistics-data-and-systems/statistics-trends-and-reports/nationalhealthexpenddata/nhe-fact-sheet.html>.

² Kaiser Family Foundation and Health Research & Educational Trust, "2015 Survey of Employer Health Benefits," available at <http://kff.org/health-costs/report/2015-employer-health-benefits-survey/>; Health Cost Institute, 2013 Health Care Cost and Utilization Report, available at <http://www.healthcostinstitute.org/2013-health-care-cost-and-utilization-report>.

goods and services, in part due to price increases caused by consolidation in health care markets. After decades of increased consolidation in provider and insurer markets resulting in ever-escalating health insurance premiums and health care expenditures, consumers have begun to demand more accountability for health care costs from their providers, insurers, and policymakers. Reform efforts, big and small, have started to shift the playing field for providers and insurers and new alliances are being formed with a wide array of potential risks and benefits for consumers. I offer some considerations and data regarding recent health insurance mergers to inform your analysis of the potential risks to consumers from the transaction at hand.

Key Concerns for Consumers

The key risks for Californians associated with any health insurance merger are increased premiums and/or reductions in quality, competition, and innovation.

Increased Premiums

In terms of premiums, research has consistently found increased premiums in the wake of an insurance merger.³ The research on past insurance mergers reveals that insurers can and do exercise newly acquired market power by raising premiums.⁴ An examination of the 1999 Aetna and Prudential Health Care Insurance merger estimated that health insurance consolidation between 1998 and 2006 led to a 7 percent increase in large group health insurance premiums.⁵ Further, analysis of the UnitedHealth Group and Sierra Health Services merger increased the post-merger premiums in the Nevada markets by 13.7 percent, suggesting that the merging parties exploited the market power gained from the merger.⁶ When premiums go up, employers often pass the added costs through to employees in the form of reduced pay, higher cost sharing, or reduced benefits.⁷ Furthermore, early data from the individual health care marketplaces also support the inverse notion that increased competition among insurers is associated with lower premiums in the post-ACA landscape.⁸

Some have argued that the Medical Loss Ratio (“MLR”) will prevent consolidated insurers from increasing premiums. But, the MLR depends on competition to function. In markets that lack adequate competition, the MLR is gameable. Because it limits administrative costs to a percentage of total premiums, in the absence of sufficient competition, insurers in have an incentive to grant higher provider reimbursement rates, increase premiums, and thereby increase the value of their allowed

³ Leemore Dafny *et al.*, *Paying a Premium on Your Premium? Consolidation in the US Health Insurance Industry*, 102 AM. ECON. REV. 1161 (2012) (examination of the 1999 Aetna and Prudential Health Care Insurance merger estimating that health insurance consolidation between 1998 and 2006 led to a 7 percent increase in large group health insurance premiums). See also Jose R. Guardado *et al.*, *The Price Effects of a Large Merger of Health Insurers: A Case Study of UnitedHealth-Sierra*, 1 HEALTH MGMT., POL’Y & INNOVATION 16 (2013) (finding the UnitedHealth Group and Sierra Health Services merger increased the post-merger premiums in the Nevada markets by 13.7 percent, suggesting that the merging parties exploited the market power gained from the merger).

⁴ Leemore Dafny, *Are Health Insurance Markets Competitive?*, 100 AM. ECON. REV. 1399 (2010).

⁵ See *Paying a Premium on Your Premium? Consolidation in the US Health Insurance Industry*, *supra* note 4.

⁶ Jose R. Guardado *et al.*, *The Price Effects of a Large Merger of Health Insurers: A Case Study of UnitedHealth-Sierra*, 1 HEALTH MANAGEMENT, POL’Y & INNOVATION 16 (2013).

⁷ David W. Emmons & Jose R. Guardado, “Competition in Health Insurance: A Comprehensive Study of U.S. Markets,” AM. MED. ASS. 33 (2014).

⁸ See *id.* at 13; Leemore Dafny *et al.*, *More Insurers Lower Premiums: Evidence From Initial Pricing in the Health Insurance Marketplaces*, AM. J. OF HEALTH ECON. 53 (Winter 2014) (finding that the addition of one insurer would lower premiums by 5.4 percent, while adding every available insurer would lower rates by 11.1 percent); Michael J. Dickstein, *et al.*, *The Impact of Market Size and Composition on Health Insurance Premiums: Evidence from the First Year of the Affordable Care Act*, 105.5 AM. ECON. REV. 120 (2015) (estimating that an additional insurer in, a given ratings area, results in savings of nearly \$500 per person).

administrative percentage. Finally, the MLR does not apply to enrollees in self-insured plans, which make up over half of the private insurance market, leaving those consumers still at risk of premium increases.

Reductions in Quality and Innovation

Consumers may also be harmed by reductions in competition that hinder incentives to improve quality and innovate. Quality reduction in the insurance industry can take many forms: delayed or refused claims payment, poor responsiveness to customers, inadequate and poor quality provider networks, lack of access to claims information, and mishandling of appeals, to name a few. Examining whether the acquiring firm has a history of quality reduction following a merger or in markets in which it has considerable market share can be instructive.

Benefits from Market Leverage and Efficiencies:

Merging insurers sometimes argue that the merger will benefit consumers because (1) any gains in market power obtained by the new insurance entity will counterbalance gains in market leverage by providers; and (2) the merger will result in significant post-merger efficiencies. While some evidence exists to support a claim that increasing health insurers' market power enhances their ability to negotiate lower prices from dominant provider organizations, those lower prices only benefit consumers if there is sufficient competition in the market to incentivize the insurer to pass the savings through to consumers in the form of lower premiums.⁹ Unfortunately, no study has found that those savings have ever been passed on to consumers.¹⁰ The more typical result is that physicians make less money, and consumers still overpay for health care following an insurance merger. History also provides several examples of dominant insurers and providers joining forces to disadvantage rivals and increase premiums and reimbursement rates.¹¹ In other words, as antitrust and health care scholar Professor Thomas Greaney posits in his "Sumo Wrestler Theory Fallacy," when dominant insurers and dominant providers face off, the result may be "a handshake rather than an honest wrestling match."¹²

Second, in looking at any efficiencies promised to accompany the merger, it is essential to determine whether the merger is *necessary* to achieve those efficiencies, or whether the firms could achieve those same objectives on their own. In recent healthcare antitrust cases, proving that the claimed procompetitive efficiencies are merger-specific has proven challenging.¹³ I am confident that the California Department of Insurance will carefully analyze whether the proposed merger will enhance competition and is necessary to obtain Centene's claimed efficiencies.

Conclusion

⁹ Erin Trish and Bradley J. Herring, *Health Insurer Market Concentration and Bargaining Power*, 42 J. Health Econ. 104 (2015).

¹⁰ Leemore Dafny, "Health Insurance Industry Consolidation: What Do We Know From the Past, Is It Relevant In Light of the ACA, and What Should We Ask?" United States Senate Committee on the Judiciary, Subcommittee on Antitrust, Competition Policy, and Consumer Rights, Sept. 22, 2015 [hereinafter *Dafny Statement*] at 9, available at <http://www.judiciary.senate.gov/imo/media/doc/09-22-15%20Dafny%20Testimony%20Updated.pdf>.

¹¹ See, e.g., *West Penn Allegheny Health Sys., Inc. v. UPMC; Highmark, Inc.*, 627 F.3d 85 (3rd Cir. 2010) (In Allegheny County, PA, the dominant provider, the University of Pennsylvania Medical Center (UPMC), agreed to use its market power to prevent competitors of the dominant insurer, Highmark, from successfully entering or expanding in the Allegheny County market and, in exchange, Highmark agreed to use its position to strengthen UPMC and weaken its rivals); see also *Complaint, U.S. v. Blue Cross Blue Shield of Michigan*, 2:10-cv-15155 (E.D. Mich., 2010).

¹² Thomas L. Greaney, "The State of Competition in the Health Care Marketplace: The Patient Protection and Affordable Care Act's Impact on Competition," United States House of Representatives Committee on the Judiciary, Subcommittee on Regulatory Reform, Commercial and Antitrust Law, at 11, Sept. 10, 2015 [hereinafter *Greaney Statement*] available at http://judiciary.house.gov/_cache/files/0a0e88c8-0519-4a47-8fa8-4c2233c760c3/greaney-testimony.pdf.

¹³ *St. Alphonsus Med. Ctr.-Nampa Inc. v. St. Luke's Health Sys., Ltd.*, 778 F.3d 775, 791 (9th Cir. 2015).

Overall, consumers bear the brunt of the impacts of consolidation in health care in multiple ways. When provider prices increase from consolidation in the provider market, insurance premiums follow.¹⁴ When insurance markets consolidate, premiums also tend to increase.¹⁵ When premiums go up, employers pass the cost through to employees in the form of reduced pay, higher cost sharing, or reduced benefits.¹⁶ If past is not prologue, and merging insurance companies do pass through any beneficial price reductions obtained from providers, consumers can still be harmed by reductions in the quality and quantity of provider services.¹⁷ Further, consolidation may compromise opportunities to increase and sustain competition. Given the significant increase in consolidation in the health insurance and provider markets, both in California and throughout the United States, government agencies and antitrust enforcers should carefully analyze the significant long-term risks of any further concentration to consumers.

Thank you for your efforts and diligence in doing so.

Warmest regards,

A handwritten signature in black ink that reads "Jaime King". The signature is written in a cursive, flowing style.

Jaime King, J.D., Ph.D.

¹⁴ See *Competition Policy in Health Care Markets*, *supra* note 13; Richard Scheffler, E.R. Kessler, and M. Brandt, *Covered California: The Impact of Provider and Health Plan Market Power on Premiums*, J. OF HEALTH POLITIC, POL'Y & L. (forthcoming 2015).

¹⁵ Kate Ho & Robin S. Lee, *Insurer Competition in Health Care Markets*, NBER, Working Paper No. 19401 (Sept. 2013), available at <http://www.nber.org/papers/w19401>; See *Paying a Premium on Your Premium? Consolidation in the US Health Insurance Industry*, *supra* note 4.

¹⁶ See *Competition Policy in Health Care Markets*, *supra* note 7, at 33.

¹⁷ See Dafny Statement, *supra* note 5, at 10.