

Public Option vs. Co-ops: The Bottom Line for Consumers

SUMMARY

Two new health insurance options are being debated as part of national health reform: a public insurance plan or health care cooperatives. According to the proposals, both options would operate within a market that contains important new insurance reforms that protect consumers. For example, new rules would require all insurers cover pre-existing medical conditions and set minimum standards for coverage. However, these reforms don't go far enough. New insurance options are also needed to provide consumers with better choices and to inject meaningful competition into health insurance markets. Which proposed option is best for consumers? The bottom line is that the larger size of the public plan option may make it only option that provides the market "clout" needed to operate as a strong competitor that could help hold down premium costs and inspire private insurers to expand their consumer focus.

Why Do We Need A New Type Of Insurer?

In order to give consumers more choices and to inject meaningful price competition into health insurance markets, policymakers are debating the introduction of a new type of insurance competitor that would compete side-by-side with private insurance options. The overarching goals are to drive down health care costs and make today's insurers more responsive to consumers.

As legislators on both sides of the aisle acknowledge, American's health care system is in crisis.¹ For decades, health care costs have been increasing at twice the rate of inflation, and consuming an ever larger share of our nation's economy. Rapidly escalating health care costs means little real growth in our paychecks as employers divert earnings to pay soaring health care premiums for their workers. Even people who are happy with their current coverage will not stay content for long, given steadily shrinking benefits.

Many believe that these soaring costs reflect, at least in part, an absence of real competition in many health insurance markets. Many health insurance markets have just one or two dominant competitors, and these insurers may lack the

incentive to negotiate aggressively with providers.² Many of these insurers are publicly traded, for-profit companies whose focus on short-term earnings may not always dovetail with the needs of their policyholders or the larger objective of reining in health care costs. The proposed solution: a new type of competitor.

Public Plan or Co-ops?

The two concepts being considered are that of a public insurance plan and health care cooperatives or co-ops. As Table 1 shows, the two proposals have many common features: both are non-profit entities, both require start-up funds but must pay for operations out of premium funds after that.³ Doctors and hospitals participate in the network voluntarily, and consumer enrollment is also voluntary. Both would operate on a “level playing field” with private insurers, with the goal of enhancing competition so it benefits consumers, not causing the withdrawal of private insurance options.

The key differences between the two proposals have to do with the scale of their operation and who would lead them. As envisioned by the U.S. House of Representatives, the proposed public plan would operate at the national level. The U.S. Secretary of Health and Human Services would oversee the plan, although administrative expenses would be paid out of premiums, not by taxpayers.

While a national co-op is a theoretical possibility, the current proposal being considered centers around smaller entities – either state or regional co-ops.⁴ By definition, the co-ops would be owned by their members (i.e. the policyholders). These policyholders would elect a governing board which, in turn, would hire the co-op’s leadership. The federal government would play no role in directly managing the co-ops.

TABLE 1 – OVERVIEW OF PUBLIC PLAN AND CO-OP OPTIONS

	Public Insurance Plan Option	Health Care Co-ops
Similarities	<ul style="list-style-type: none"> • Enrollment is optional; consumers have the choice of the new option or private insurers. • No government funding after start-up. Administration, medical claims and contributions to reserves must be paid out of the premiums collected. • Doctors and hospitals participate voluntarily. • Must comply with same rules as private insurers, including guarantee issue, benefit standards, provider network adequacy, and consumer protections. • Must be non-profit. • May contract out certain duties (like claims administration) to private companies, although both entities must keep the insurance function, that is, they bear the risk for their members' claims. 	
Differences		
Size:	National	Regional or State-based. Proponents suggest that a minimum size of 500,000 members would be needed to successfully compete and negotiate with providers.
Business Structure:	The Secretary of HHS operates the non-profit, public plan, although administrative expenses are paid out of premiums, not by taxpayers.	Federally-chartered co-ops would be non-profit, and operated to the benefit of policyholders (like mutual health insurance companies today). Policyholders (members) would elect a governing board which in turn hires the co-op's leadership.
Insurance Model:	The House proposal calls for the plan to be set up like a PPO (the most common type of private insurance) with preferred and non-preferred providers.	Health care co-ops operating today are set up as HMOs in which hospitals are owned by the insurer and doctors are salaried employees. Co-ops can also be set up to operate as PPOs.
Provider Payments:	The House proposal calls for provider payments to be based on Medicare payments, plus 5%, for the first three years. Thereafter, provider payments would be negotiated with the goal of establishing rates that ensure adequate access for patients, yet make use of payment innovations designed to curb rising health costs.	Provider payments would be negotiated using a process similar to that used by private insurers today. Ability to negotiate favorable rates or introduce payment innovations would presumably depend on the size of the policyholder population.
Repayment of start-up funds:	Federally-provided start-up money would be repaid out of future premiums over a 10-year period.	Some of the initial start-up money would take the form of grants, implying no taxpayer repayment. Other seed money would take the form of loans.
Reserve Requirements:	The House proposal calls for premium rates to include an amount for a "contingency" margin but the required level of reserves may differ from that specified by states.	Co-ops would be subject to the same reserve requirements as other insurers (determined at the state level).
Sources	"America's Affordable Health Choices Act," draft legislative language released by selected committees in the House of Representatives, July 31, 2009.	"Framework For Comprehensive Health Reform" released by the Senate Finance Committee, September 9, 2009.

How Would Consumers Fare Under the Two Options?

Consumers Union has developed a list of criteria that are important to consumers to see how the two proposed approaches stack up.

1. CAN I JOIN EVEN IF I HAVE A PRE-EXISTING CONDITION?

Public Insurance Plan Option	Health Care Co-op Option
Yes. New rules would require all insurers (public and private) to accept all applicants.	Yes. Both options are the same in this respect.

2. CAN I GET COMPREHENSIVE COVERAGE?

Public Insurance Plan Option	Health Care Co-op Option
Yes. New rules would require that all insurers (public and private) comply with minimum coverage standards. These standards haven't been completely specified but they are expected to cover a comprehensive array of services (doctors, hospitals, prescription drugs, etc). There will be cost-sharing but the share to be paid by the patient hasn't been decided. Insurers will retain some flexibility in their benefit designs.	Yes. Both options are the same in this respect.

3. AM I REQUIRED TO JOIN?

Public Insurance Plan Option	Health Care Co-op Option
No. There would be a new requirement that everyone have coverage, unless they can show they can't afford it. But people will continue to have the choice of private insurance options, in addition to the public plan, to comply with that requirement.	No. Both options are the same in this respect.

4. WILL THE COVERAGE BE AFFORDABLE?

Public Insurance Plan Option	Health Care Co-op Option
<p>Likely. The large size of the proposed public option gives it the leverage needed to negotiate aggressively with providers (doctors and hospitals). New price transparency and a creditable market presence would provide incentives for private insurers to match these prices. The proposed legislation charges the public plan with ensuring “affordable, high quality coverage.”</p> <p>In addition, families with income below a certain threshold would qualify for premium “credits” that would further lower the cost of the coverage. These credits could be applied to the public plan or to private coverage sold in the new “exchange.”⁵</p>	<p>Maybe. Affordable co-op coverage is less certain because the track record for small insurance competitors suggests that co-ops may be too small to negotiate favorable payment arrangements with providers.⁶</p> <p>However, under either option, families with income below a certain threshold would qualify for premium “credits” that would further lower the cost of the coverage. These credits could be applied to co-op coverage or to private coverage sold in the new “exchange.”</p>

5. IF I MOVE, CAN MY INSURANCE GO WITH ME?

Public Insurance Plan Option	Health Care Co-op Option
<p>Maybe. If a national public plan is implemented, the coverage would be available no matter where you lived in the country.⁷ In your new area, you would have the choice of a public plan and private options.</p>	<p>No. If you move outside the coverage area of the co-op, you would have to enroll in new coverage. In your new area, you would have the choice of private insurance options, but there might not be a co-op option. Co-op formation is voluntary, and there might not be one in every part of the country.</p>

6. WHAT INCENTIVES MAKE THESE PLANS ACCOUNTABLE TO CONSUMERS?

Public Insurance Plan Option	Health Care Co-op Option
<p>The proposal calls for the public insurance plan to ensure “choice, competition, and stability of affordable, high-quality coverage through out the United States.” The proposal also</p>	<p>Co-ops, by design, are operated to the benefit of their members. However, a co-operative business model is not a guarantee of sound, responsive leadership.⁸ As experience is gained</p>

creates an Ombudsman charged with resolving policyholder problems and communicating plan information.	with this option, it is possible that aggressive oversight may be needed to protect policyholders, given the voluntary nature of member oversight.
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7. WILL THIS INSURANCE BE THERE IN THE FUTURE?

Public Insurance Plan Option	Health Care Co-op Option
<p>Likely. The large size of the public option provides it with a basis for being viable over the long run. However, any insurance competitor will have to offer competitive insurance products in order to attract and keep a reasonable share of the insured population. If the public plan fails to do so, there are no provisions for a federal rescue.</p> <p>Additionally, the federal operation of the public plan would prohibit it from “converting” to a private company or being acquired by a private competitor.</p>	<p>Maybe. Past experience shows that small, co-operative approaches to health insurance have had difficulty surviving over the long run.⁹ Many mutual health insurance companies (an identical type of entity) found they couldn’t raise sufficient capital and they “de-mutualized” in order to become bigger and better able to compete with large, private insurers. In turn, many of these former mutuals later merged with private, for-profit insurers.</p> <p>A handful of co-ops have survived over a long period and are generally well regarded by their policyholders.¹⁰</p>

Bottom Line for Consumers

As discussed above, the two options, public plan and co-ops, have several common attributes intended to provide new value for consumers. However, for consumers to realize these potential benefits, the new insurance competitor must be a viable entity that can survive over the long run.

The bottom line is that consumers will need a large, permanent competitor if they are to realize the benefits of a truly competitive health insurance market. The public plan, with its national scope and greater stability, seems more likely to fit this bill.

If the proposed co-ops are too small to negotiate the “best deals” with the doctors and hospitals that will serve in the plan’s network, they will be unable to survive in the long run. Indeed, they may not form at all if the potential operators reach the same conclusion. Experts note that there are very high barriers to entering health insurance markets and almost no new insurance plans have formed in recent years.¹¹

Furthermore, the new competitor must have a big share of the market if they are to introduce the payment innovations and other reforms designed to improve the delivery of care and control costs. System-wide cost containment is a key goal of health care reform.

Another concern is that large, private insurers will try to attract the healthiest enrollees, enabling that insurer to offer lower premiums. Any new competitor must have the expertise and depth of reserves to counter this sort of competition.¹² Co-ops rely on the voluntary and mutual co-operation of their members. While these members aren't responsible for the day-to-day decision-making, they are responsible for ensuring that their organization's leadership operates in a manner consistent with their mission, yet is expert enough to compete successfully with very large, sophisticated, and well-funded private insurers. Finding this type of talent, in quantities sufficient to run multiple co-ops around the country, would be a challenge.

It is worth noting that the presence of a federally-operated public plan doesn't preclude the formation of co-ops. Current law permits the formation of these entities and the proposed legislation specifically permits them as well. To the extent that communities have the market environment, provider endorsement, and leadership needed for success, co-ops can still be formed to the benefit of consumers.

This report was prepared by Lynn Quincy and Kathy Talkington.

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ENDNOTES

- ¹ Policymakers acknowledge that other reforms are also needed: lower and moderate income families must have financial help to purchase coverage; all coverage should meet some minimum standards to ensure that it covers needed care and provides sufficient financial protection for families. Critically, the proposals would ensure that—no matter where they buy their coverage—people can't be denied coverage due to pre-existing medical conditions or be charged more. These changes would greatly expand the availability of affordable health insurance coverage.
- ² American Medical Association, *Competition in Health Insurance: A Comprehensive Study of U.S. Markets: 2008 Update*.
- ³ Our source for public plan details is the "America's Affordable Health Choices Act," draft legislative language released by selected committees in the House of Representatives. Co-op details are from the "Framework For Comprehensive Health Reform" released by the Senate Finance Committee September 9, 2009 (<http://finance.senate.gov/press/Bpress/2009press/prb090909.pdf>) and a description of the co-op proposal from Senator Conrad's website (http://conrad.senate.gov/issues/statements/healthcare/090813_coop_QA.cfm)
- ⁴ In order to make the co-ops large enough to be viable, but not too cumbersome, Senator Conrad has propose a co-op model that sets up a national entity with state affiliates, and the further flexibility so those states can have regional pools. (Post, Klein, June 11, 2009)
- ⁵ All of the health reform proposals call for a new health insurance store, often called a health insurance exchange or health benefits gateway. "Shoppers" can choose from among several health insurance options arrayed "side-by-side." The Exchange may take on a variety of other duties including: establish health plan standards, enrollment, billing, and other administrative functions, administer coverage subsidies, and respond to consumer grievances.
- ⁶ Consumers Union, *Health Care Co-ops: Many Challenges*, September 2009.
- ⁷ In order to offer the same coverage on the same terms to everyone in all states, the state-based regulation that exists today would need to change. The health reform proposals create a health insurance "exchange" that standardizes the rules facing insurers. In addition to nationwide rules requiring guaranteed issue, within the exchange there would be an "essential" benefit package with some limits on the permitted variation over and above this floor. Insurers would still have some flexibility in benefit design and states would retain the ability to require stronger consumer protections and/or benefit packages.
- ⁸ For example, credits unions (another form of co-op) have suffered from embezzlement just like their for-profit counterparts.
- ⁹ Consumers Union, *Health Care Co-ops: Many Challenges*, September 2009.
- ¹⁰ Consumers Union, *Health Care Co-ops: Many Challenges*, September 2009.
- ¹¹ American Medical Association, *Competition in Health Insurance: A Comprehensive Study of U.S. Markets: 2007 Update*.
- ¹² The proposals contain what is known as "risk adjustment" provisions. These provisions are designed to transfer monies from health plans that enroll healthier-than-average populations to those that enroll sicker-than-average populations, thus minimizing the incentive to compete based on attracting the healthiest enrollees. Most experts agree they don't work perfectly.