GOVERNOR SCHWARZENEGGER'S HEALTH CARE PROPOSAL

The Governor's vision for health reform is an accessible, efficient, and affordable health care system that promotes a healthier California through prevention and wellness and universality of coverage. For the Governor's vision to be realized, health care reform must reflect a "systems" approach that incorporates three essential building blocks in an integrated manner. These building blocks are:

Prevention, health promotion, and wellness
Coverage for all Californians
Affordability and cost containment

A. PREVENTION, HEALTH PROMOTION, AND WELLNESS

Preventable disease and disability have a profound impact on the health of California residents and communities as well as on the continued growth in health care costs. An increased emphasis on disease prevention, health promotion and healthy lifestyles will improve health outcomes and help contain health care costs. To promote a healthier California and achieve long term cost containment, the Governor's action steps include:

Structuring benefits and providing incentives/rewards to promote prevention, wellness, and healthy lifestyles through the implementation of "Healthy Actions Incentives/Rewards" programs in both the public and private sectors: Implement "Healthy Action Incentives/Rewards" programs in both the public and private sectors to encourage the adoption of healthy behaviors. Californians who take personal responsibility to increase healthy practices and behaviors, thereby reducing their risk of chronic medical conditions and the incidence of infectious diseases, will benefit from participation in this groundbreaking program. The Healthy Action Rewards/Incentives program will reward Californians for participation in evidence-based practices and behaviors that have been shown to both reduce the burden of disease and are cost-effective. Individuals in public programs, such as Medi-Cal and Healthy Families, will earn rewards that may include gym memberships or weight management programs. Participants enrolled in commercial plans, including CalPERS, will earn rewards and incentives, including premium reductions, for engaging in healthy activities. The Governor's plan includes the creation of a new insurance subsidy pool administered by the Managed Risk Medical Insurance Board through which low-income adults will be provided with subsidized coverage. The pool's coverage will also include a Healthy Action Incentive/Rewards program. All health plans and insurers will be required to offer a health benefit package(s) that includes incentives/rewards programs, including premium reduction, in the event that an employer wishes to make them available to their employees. All of the Healthy Actions programs are linked to the completion of a Health Risk Assessment and follow-up doctor visit.

Establishing a national model for the prevention and treatment of diabetes: Over 2 million Californians currently have diabetes, and the number of Californians with diabetes is expected to double by 2025. Over one quarter of people with diabetes do not know they have the disease. To better prevent, target, and manage this high-cost chronic condition, Medi-Cal and the California Diabetes Program, in collaboration with community organizations, will jointly develop a comprehensive statewide initiative to institute proven interventions for pre-diabetes and diabetes screening, primary prevention, and self-management to reduce the number of people with diabetes or improve the health of those with the disease while reducing costly care within California's health care system.

Preventing medical errors and health care acquired infections: Medical errors and health care acquired infections unnecessarily compromise the health status of patients, lower health care quality and significantly contribute to health care costs. Patient harm due to such lapses causes an estimated 23,000 hospital deaths and untold numbers of injuries each year in California and costs over $4 billion annually. To combat this problem and significantly improve patient safety throughout California, the Governor will: (1) Require electronic prescribing by all providers and facilities by 2010 to substantially reduce adverse drug events; (2) Require new health care safety measures and reporting requirements in California's health facilities to reduce medical errors and hospital acquired infections by 10% over 4 years; (3) Call upon the leadership of California's health facilities to implement evidence-based measures to prevent harm to patients and provide state technical assistance; and (4) Create a university-based academic "re-engineering" curriculum designed to improve patient safety and streamline costs within the health care delivery system.

Reversing obesity trends through nation-leading innovative and comprehensive strategies: Obesity threatens to surpass tobacco as the leading cause of preventable death among Californians and costs the state $28.5 billion in health care costs, lost productivity, and workers' compensation. California can lead the nation in tackling obesity with the same success demonstrated in the state's anti-tobacco campaign. Based on the Governor's 10-Step Vision for a Healthy California, the Governor's proposal includes a sustained media campaign to encourage healthy choices; community-based activities to increase access to healthy food in stores and physical activity in schools and neighborhoods; employee wellness programs; and school-based strategies that engage the broader community in obesity prevention activities.

Continuing the battle against tobacco use: Smoking is the leading preventable cause of death in California. California has led the nation in effective smoking control activities, achieving the second lowest rate of smoking among adults in the nation. Still, an estimated 3.8 million adults and 200,000 youth smoke. California can maintain its leadership role in tobacco control and further reduce smoking rates by increasing access to cessation services offered through the highly effective California Smokers' Helpline and maximizing utilization of cessation benefits.

B. COVER ALL CALIFORNIANS

According to the UCLA California Health Interview Survey, 6.5 million Californians were uninsured at some point during last year, representing 20% of children and non-elderly adults. 75% of the uninsured were in working families, with the majority having no health coverage through their employers.

Addressing the "hidden tax" benefits everyone: A recent report by the New America Foundation estimated that a "hidden tax" on California health premiums has driven prices 10% higher to help cover the costs of caring for the state's large numbers of uninsured. The study indicated that this annual "hidden tax" is $1,186 per California family and $455 for individual health insurance policies. This tax is even higher when underpayments from government purchasers such as Medi-Cal are added in.

Source: Dobson, Allen et al. (2006). The Cost-Shift Payment 'Hydraulic': Foundation, History, And Implications. Health Affairs, 25, no. 1: 22-33.

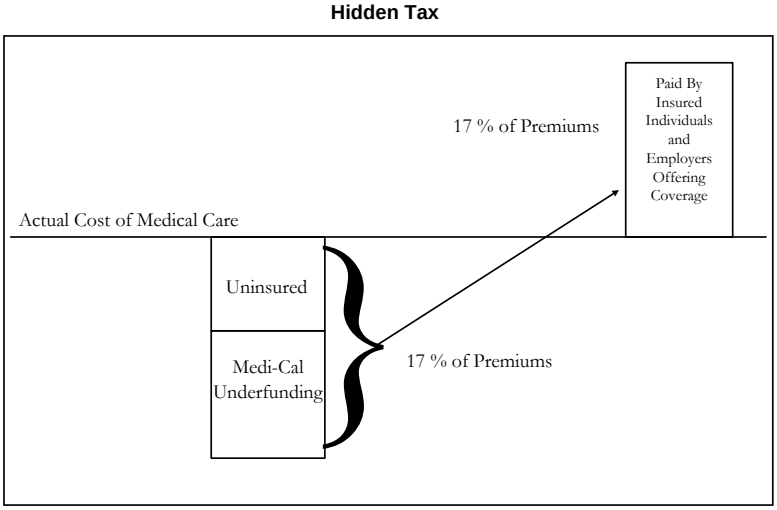

Figure 1: The effect of the "hidden tax" on insured individuals and employers offering coverage.

Ensuring availability of emergency rooms and trauma centers is essential: According to the Office of Statewide Health Planning and Development, 65 emergency rooms (ERs) in California have closed in the last decade. In Los Angeles County, one fifth of ERs have closed since 1995, leaving only 75 ERs open to the county's 10 million residents. A new study by the federal Centers for Disease Control and Prevention indicates that between 40% and 50% of emergency departments experienced overcrowding during 2003 and 2004. A major source of this overcrowding, especially in metropolitan areas, is the uninsured and persons who have problems accessing physicians through government programs such as Medi-Cal, which also contributes to emergency department and trauma center closures across California. As a result, the well-being and life of many Californians is threatened by longer drives to fewer ER facilities, longer waiting times, and compromised hospital capacity to cope with a major emergency, such as a disease outbreak or earthquake.

Availability of insurance affects not only the physical but the financial health of the community: A 2002 synthesis of 25 years of research on the uninsured conducted by the Kaiser Commission on Medicaid and the Uninsured found that the uninsured receive less preventive care, are diagnosed at more advanced stages of illness, have reduced annual earnings from work, and achieve reduced educational attainment. A National Institute of Medicine study indicated that the lack of insurance has resulted in a lost national economic productivity of $65 billion to $130 billion annually.

A February 2005 article in Health Affairs indicated that about half of the approximately 1.5 million American families that filed for bankruptcy in 2001 cited medical bills as the cause, which indicates that 1.9–2.2 million Americans (filers plus dependents) experienced bankruptcy

due to lack of funds for medical expenses. The lack of insurance and underinsurance (less comprehensive medical policies) were major contributors to the bankruptcies for the two years prior to 2005 as well. Numerous other articles have chronicled the sometimes catastrophic financial difficulties that individual families have encountered when facing uncovered health care costs.

To achieve coverage for all of California's uninsured, the Governor's action steps include:

Requiring all individuals to have a minimum level of coverage (individual mandate): Requiring people to carry coverage is the most effective strategy for fixing the broken health care system. The core problem for California is that those with insurance pay the cost of health care delivered to 6.5 million uninsured. Everyone must participate equally. An employer mandate will not achieve universal coverage because it fails to address the needs of part-time, seasonal, and unemployed uninsured Californians.

Providing low-income individuals affordable coverage: Low-income Californians will be provided expanded access to public programs, such as Medi-Cal and Healthy Families, and lower-income working residents will be provided financial assistance to help with the cost of coverage through a new state-administered purchasing pool.

Requiring insurers to issue health insurance: Insurers will be required to guarantee coverage, with limits on how much they can charge based on age or health status, so that all individuals have access to affordable products.

Increasing Medi-Cal rates significantly: To reduce the "hidden tax" associated with low Medi-Cal reimbursement and to encourage greater provider participation in the Medi-Cal program, Medi-Cal rates for providers, hospitals, and health plans will be increased.

Facilitating and enforcing the individual mandate: Systems will be established to facilitate enrollment of uninsured persons who use the health care system. Providers will play an important role in supporting enrollment by instituting such strategies as on-site enrollment at provider locations, as well as by underscoring the expectation that everyone present a coverage card at the point of service. In addition, the salary tax withholding and payment process with the Employment Development Department and the state income tax filing process will be utilized to promote compliance with the individual mandate.

<u>Coverage Proposal Overview</u>

6.5 million Californians are uninsured for all or part of a year; 4.8 million Californians are uninsured at any given time. The Governor's health care initiative identifies sufficient funds to cover all Californians through a variety of mechanisms. Jon Gruber, Ph.D., an MIT economist and health care expert, has assisted the Administration in estimating individual and employee behavior in the coverage model outlined below based upon coverage for all 4.8 million uninsured residents.

Coverage for uninsured children (approximately 750,000):

- All uninsured children below 300% of the federal poverty level (FPL), regardless of residency status, will be eligible for state-subsidized coverage. 220,000 uninsured

children below 100% of the FPL will enroll in Medi-Cal, while 250,000 uninsured children between 101-300% of the FPL will enroll in the Healthy Families Program.

- 210,000 uninsured children will enroll in employer-sponsored coverage and an additional 50,000 uninsured children above 300% of the FPL will be covered by private insurance by their parents or responsible adult. Parents of these children will be responsible for purchasing at least the minimum level of coverage for their children.

Coverage for uninsured adults (approximately 4.1 Million):

- 630,000 uninsured legal resident adults with incomes below 100% of the FPL will be eligible for and enroll in no-cost Medi-Cal. This population has little discretionary income and purchasing Medi-Cal is a cost-effective coverage option.
- Approximately 1.2 million uninsured legal resident adults with incomes between 100-250% of the FPL will be eligible for coverage through a state purchasing pool operated by the Managed Risk Medical Insurance Board. Approximately 1 million are expected to enroll with the remaining 200,000 opting for employer-sponsored coverage.
- Consistent with the principle of shared responsibility, the individual/family contribution toward the premium will be as follows:

  100-150%: 3% of gross income
  151-200%: 4% of gross income
  201-250%: 6% of gross income
- Approximately 1.1 million uninsured legal resident adults above 250% of the FPL will not receive a subsidy and will be required to purchase and maintain coverage under the individual mandate. Of this amount, 370,000 are expected to opt for employer-sponsored coverage and 730,000 are expected to purchase individual coverage.
- There are approximately 1 million uninsured persons without a "green card" (primarily undocumented persons and persons with temporary visas). Of this amount, approximately 40,000 are expected to opt for employer-sponsored coverage and 160,000 are expected to purchase individual coverage. The remaining 750,000 under 250% of the FPL are expected to receive health coverage provided, coordinated or arranged by county government in coordination, where applicable, with county and University of California hospitals. Counties would retain $1 billion in current funding (primarily for outpatient services) and county and UC hospitals will retain $1 billion in federal Disproportionate Share Hospital (DSH) funds and in addition, some "safety net" funds for primarily inpatient services. The state will also continue to fund emergency Medi-Cal which provides certain vital services such as prenatal care and maternity for this population.

Payment assistance will be available for low-income insured adults: In order to maintain equity for low-income persons who are already contributing towards the cost of their care, persons with individual or employer-sponsored coverage who are between 100-250% of the poverty level will be eligible for state financial assistance through the purchasing pool. Approximately 700,000 persons are expected to utilize this option. Persons with employer sponsored coverage are eligible for state financial assistance through the purchasing pool for the employee share of the premium only if the employer contributes to the cost of coverage for those employees.

Anti crowd-out provisions are included to provide a disincentive to employers and employees from dropping current coverage. These include the 4% employer "in-lieu" fee for non-offering employers with 10 or more employees, purchasing pool premium contribution levels which are slightly higher than employee-only premium contribution levels, and a proposed provision that

will be added to the Labor Code making it an unfair business practice for an employer to differentiate the employer premium contribution by class of employee, except pursuant to a collective bargaining agreement.

In order to establish a more organized system of state-subsidized coverage that simplifies the eligibility system and maintains family unity of coverage, a "bright line" will be established between the Medi-Cal program and other subsidized programs (except for pregnant women). This would affect 680,000 children and 215,000 adult Medi-Cal enrollees above 100% of the FPL who would switch coverage to either the Healthy Families Program or the purchasing pool.

Source: Governor Schwarzenegger's health care team.

California's Family Health Insurance Programs

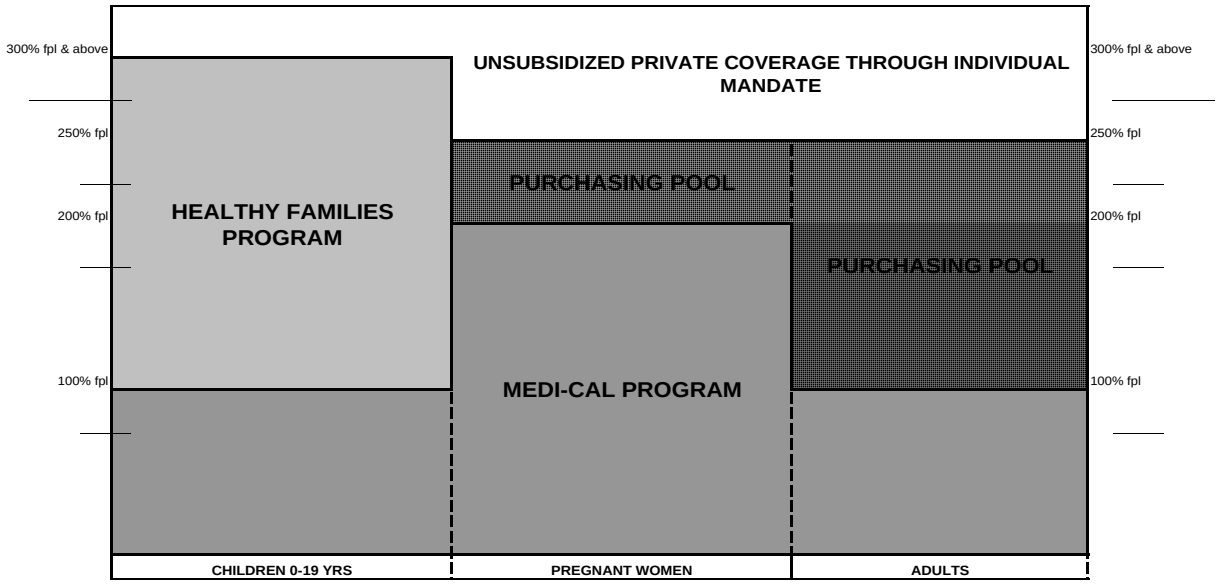

Figure 2: Proposed state coverage programs.

Everyone must maintain a minimum level of insurance:

- All Californians will be required to have health insurance coverage. Coverage must be substantial enough to protect families against catastrophic costs as well as minimize the "cost shift" that occurs when large numbers of persons are receiving care without paying the full cost of that care.
- The *minimum* health insurance benefit that must be maintained will be a $5,000 deductible plan with maximum out-of-pocket limits of $7,500 per person and $10,000 per family. For the majority of uninsured individuals, such coverage can be purchased today for $100 or less per month for an individual and $200 or less for two persons. Uninsured persons at any income level can purchase their own health coverage that meets the above requirement or, if income eligible, may obtain coverage with a state subsidy.
- Coverage through the new purchasing pool will fulfill an individual's obligation to obtain health coverage. The subsidized coverage through the purchasing pool is expected to be at the level of Knox-Keene medical benefits plus prescription drugs. Deductibles and/or co-payments that encourage the use of preventive benefits and discourage unnecessary use of emergency rooms will also be a part of the benefit package. The design of the subsidized benefit package will be the responsibility of MRMIB. Although dental and

vision benefits will not be included in the subsidized benefits, the pool will also offer non-subsidized products so that members can purchase richer benefits at their own expense. Persons between 100-250% FPL will have the option to purchase this subsidized coverage through the pool.

- Medi-Cal and Healthy Families Program benefits are expected to remain the same.
- Persons not eligible for a subsidy can purchase coverage that meets the minimum requirements in the private individual market. They can also access the mandated minimum $5,000 deductible product in the purchasing pool. Individuals will also be able to take advantage of the federal pre-tax premium deductions in either place if eligible.

Under shared responsibility, financing for expanded public programs, the subsidized health plan, increased Medi-Cal rates, and programs to promote prevention, health and wellness will be achieved through the following structure:

- Employers with 10 or more employees who choose not to offer health coverage will contribute an amount equal to 4% of payroll toward the cost of employees' health coverage.
- The plan will direct $10-$15 billion to hospitals and doctors, who will then return a portion of this coverage dividend associated with universal coverage; hospitals will contribute 4% of gross revenues and physicians will contribute 2% of gross revenues.
- The redirection of $2 billion in medically indigent care funding, which includes health care safety net, realignment, and other funding sources.
- Additional federal reimbursements for Healthy Families Program expansion, Medi-Cal rate increases, Medi-Cal coverage of parents as well as single adults through a Medi-Cal Section 1115 Waiver.

The proceeds from these revenue sources will be deposited into a newly established Health Care Services Fund. These funds will be segregated from the state general fund and will be the source for payment for health care coverage under the initiative.

Under the proposal, counties, county and University of California hospitals, will retain $2 billion in current funding for the uninsured. The State will continue to fund emergency Medi-Cal, which provides certain vital services, including emergency care, prenatal care and maternity services for this population.

C. AFFORDABILITY AND COST CONTAINMENT

Cost and coverage must be addressed together: without short- and long-term cost containment measures, the current system of health care delivery is not sustainable for employers and employees. With health care costs rising faster than general inflation, even more employers and employees will discontinue coverage and reliance on state health care programs will increase if health care affordability is not addressed. Cost containment becomes even more important with an individual mandate so individuals can afford to purchase and maintain comprehensive benefits.

Reduction of the "Hidden Tax:"

- When more Californians have coverage, providers will not need to continue loading their insurance charges with extra funds to make up for the cost of caring for those without coverage.
- Increased Medi-Cal reimbursement will further reduce the need of providers to shift uncompensated Medi-Cal costs to other payers.
- Employers will finally see an end to the annual premium cost-spikes they are currently experiencing. Providing health coverage to their employees will be more affordable.

Enhanced tax breaks for individuals and employers for the purchase of insurance:

- Align state tax laws with federal laws by allowing persons to make pre-tax contributions to individual health care insurance Health Savings Accounts.
- Require employers to establish "Section 125" plans so that employees can make tax-sheltered contributions to health insurance and save employers additional FICA contributions.

Enhance insurer and hospital efficiency:

- Require health plans (HMOs), insurers and hospitals to spend 85% of every dollar in premium and health spending on patient care.
- Revise the amount an insurer must pay a hospital when insured persons need treatment outside of their network so insurers will not need "defensive contracting" to protect against high daily rates from out-of-network providers.

Reduce regulatory barriers to more efficient health care delivery:

- Implement a new federal classification system for hospital construction and establish a new structural performance category to adopt a "worst first" system of hospital conformity to California's seismic safety requirements.
- Implement a "24-Hour Coverage" program that combines and coordinates the health care component of workers' compensation with traditional group health coverage. The proposed five-year pilot program for Cal-PERS (state and local agency employees) will ensure that health care services are delivered by the same set of providers used in the Cal-PERS managed care/HMO program for work and non-work-related health care. The private sector will be allowed to opt into the pilot.
- Remove statutory and regulatory barriers to expansion of lower-cost models of health care delivery such as retail-based medical clinics by making scope of practice changes for "physician extenders" such as nurse practitioners and physician assistants.

Reduce cost for delivering HMO products to employers and individuals:

- Review health/plan benefit, provider, and procedural mandates in order to reduce the cost of health care.
- Allow electronic submission of documents between insurers and their enrollees.
- Eliminate unnecessary health plan reporting requirements, such as the report on late grievances, antifraud, and arbitration reports, which are confusing and result in incomplete and/or not useful information.
- Streamline health insurance product approval.
- Develop a technology assessment process that will promote evidence-based care.

Prevention, health promotion, and wellness represent critical long-term cost containment strategies, as described above. Other key components for achieving long-term affordability include:

Health Information Technology (HIT): Health Information Technology offers great promise as one means to achieve more affordable, safe, and accessible health care for Californians while inside and outside of the state . Governor Schwarzenegger proposes the following action steps to advance the adoption of HIT throughout California:

- Providing state leadership and coordination by appointing a Deputy Secretary of HIT to lead and coordinate the state's HIT-related efforts to achieve 100% electronic health data exchange in the next 10 years.
- Improving patient safety through universal e-prescribing by 2010.
- Accelerating HIT by leveraging state purchasing, including support for uniform interoperability standards and HIT adoption, such as e-prescribing.
- Supporting consumer empowerment through use of standardized Personal Health Records (PHR) in the shorter-term within the public and private sectors that: are accessible via the internet and smart cards, are portable between health plans, and provide consumers with access to the core set of data in their PHR for their use and the use of their providers.
- At the county level, a pilot of an Electronic Medical Record system will be implemented, utilizing requirements under the Mental Health Services Act, creating an integrated network of care for mental health clients.
- Facilitating the use of innovative financing mechanisms, guided by a State HIT Financing Advisory Committee, to ensure the development of public/private partnerships and to meet capital needs for important HIT-related projects.
- Expanding broadband capabilities to facilitate the use of tele-medicine and tele-health, particularly in underserved areas throughout the state and stimulating the adoption of e-health technologies throughout the state through engagement of early tele-health adopters, communities in which they serve, technology firms, and community stakeholders.

Leverage state purchasing power through Medi-Cal:

- Increase Medi-Cal physician, hospital outpatient and inpatient, and health plan rates to promote a stable and sizeable provider network and assure continued timely access to health care for Medi-Cal beneficiaries and the broader population.
- Link future Medi-Cal provider and plan rate increases to specific performance improvements measures, including measuring and reporting quality information, improvements in health care efficiency and safety, and health information technology adoption.
- Pursue a Federal Medicaid 1115 waiver to maximize federal financing and support innovations in the financing and delivery of services through Medi-Cal. Such innovations can include the use of incentives and rewards for healthy behaviors, new strategies for diabetes prevention and management, adoption of health information technology, and strategies to rebalance the state's current system of long term care services in support of home and community-based services.

Enhance health care quality and efficiency:

- Provide a one-stop resource for information on health plan performance through the Office of the Patient Advocate website (www.opa.ca.gov) to increase the transparency of quality of care and access to other information to help inform consumers.
- Expand and strengthen the ability of the Office of Statewide Health Planning and Development to collect, integrate, and distribute data on health outcomes, costs, utilization, and pricing for use by providers, purchasers, and consumers so that additional health care data is available to inform and drive decision-making.
- Partner with private and public sector purchasers to promote the measurement and reporting of provider performance and the aggregation of data for quality improvement, pay for performance, and consumer choice.

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We have a social, economic, and moral imperative to fix California's broken health care system and improve health care for all. Health care reform is essential to a healthy, productive, and economically competitive California. The foundation of the Governor's plan to expand health coverage and contain costs is a shared responsibility. Just as society as a whole shares in the benefits of universal coverage and health care affordability, so too is there a shared responsibility to secure universal coverage and contain health care costs. Over the course of the next year, the Governor and his Administration will work collaboratively with the Legislature, employers, health care insurers, and providers, and all Californians to create a national model for health care.

Source: Governor Schwarzenegger's health care team.

State Fiscal Impact Summary
(Dollars in Millions)

COSTS	STATE	LOCAL	FEDERAL	TOTAL COSTS	INDIVIDUAL TAX REDUCTION	SAFETY NET CARE POOL[1]
Increased Medi-Cal/Healthy Families Program Coverage	$1,283		$1,357	$2,638		
Subsidy for Persons 100% -250% of FPL	$1,135		$1,135	$2,270		$542
Persons w/o Green Cards Provided Coverage by Counties		$1,000	$1,000	$2,000		
Prevention and Wellness Measures	$150		$150	$300		
Section 125 Tax Treatment (State Income Tax Reduction)	$900			$900	$900	
Section 125 Tax Treatment (Federal Income Tax and FICA Reduction)					$7,500	
Medi-Cal Rate Increase	$2,208		$1,832	$4,039		$224
TOTAL COSTS	**$5,675**	**$1,000**	**$5,474**	**$12,147**	**$8,400**	**$766**

REVENUES	
Employer 4% of Social Security Wages Payroll In-Lieu Fee (employers with <10 employees excluded)	$1,000
Provider Coverage Dividend (4% Gross Revenues from Hospitals and 2% from Physicians)	$3,472
County Funds Available from Relief of County Obligations	$1,000
Savings from the elimination of State Programs[2]	$203
TOTAL REVENUES	**$5,675**

NET SURPLUS/SHORTFALL	$0

[1] Safety Net Care pool funding is included in the federal fund cost column and is split out in this column to show how these funds are being used.
[2] The Access for Infants and Mothers program, Managed Risk Medical Insurance Program and Medi-Cal Share-of-Cost will no longer be needed.

Figure 3: Fiscal impact of Governor's proposal.