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# HEALTH COVERAGE EXPANSION IN CALIFORNIA: WHAT CAN CONSUMERS AFFORD TO SPEND?

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## INTRODUCTION

Health reform proposals under consideration in Sacramento would require consumers, employers, providers, and government to share responsibility for the cost of expanding health coverage. However, given that affordability is the primary obstacle to insurance coverage for the majority of the uninsured,[i] consumers' share of the burden must be considered in light of their ability to pay.

In the current policy environment, affordability comes into play in several provisions of the Governor's Health Care Proposal (GHCP) and Assembly Bill 8 (AB 8). Both proposals would require low- and moderate-income families to contribute to insurance obtained through a purchasing pool. In addition, AB 8 would establish conditions for mandatory take-up of coverage offered through a pool, while the governor's individual mandate would create a minimum insurance requirement so that all Californians without coverage through their employer, or through public programs, would have to purchase coverage on the individual market.

One way of benchmarking affordability is to look at current healthcare spending, which provides an accurate picture of what consumers are willing and able to pay. We use data from the national Medical Expenditure Panel Survey (MEPS) – an annual set of large-scale surveys of families and individuals, their medical providers, and employers – to calculate the proportion of earnings Californians of various income levels are currently allocating to health care expenses.

The population we will focus on includes residents under the age of 65 who purchase health insurance coverage through a group, such as an employer, union or association, as well as residents who purchase health insurance through the individual market.[ii] In addition, we exclude Californians at or under the poverty level because both major reform proposals would extend Medi-Cal coverage to such individuals.

In 2005, roughly 18 million residents with incomes above the federal poverty line (FPL) had employment-based coverage while 2 million obtained coverage through the individual market. As the below table indicates, source of health insurance varies by income level.

### Table 1: Source of Insurance Coverage by Income for the Non-elderly in California (Percent and Size of Population), 2005

| | 101-200% FPL | 201-250% FPL | 251-300% FPL | 301-400% FPL | Over 400% FPL |
|---|---|---|---|---|---|
| **Employer-Based** | | | | | |
| Percent | 32.6% | 55.2% | 66.7% | 74.2% | 82.7% |
| Population | 2,026,000 | 1,178,000 | 1,261,000 | 2,824,000 | 10,900,000 |
| **Non Employer-Based (Individual)** | | | | | |
| Percent | 3.9% | 6.8% | 7.6% | 7.1% | 8.5% |
| Population | 243,000 | 144,000 | 144,000 | 270,000 | 1,121,000 |
| **Public** | | | | | |
| Percent | 36.7% | 19.6% | 13.6% | 8.0% | 3.0% |
| Population | 228,000 | 420,000 | 258,000 | 304,000 | 401,000 |
| **Uninsured** | | | | | |
| Percent | 26.8% | 18.4% | 12.1% | 10.7% | 5.8% |
| Population | 1,664,000 | 394,000 | 230,000 | 406,000 | 765,000 |
| **Total** | | | | | |
| Percent | 100% | 100% | 100% | 100% | 100% |
| Population | 4,161,000 | 2,136,000 | 1,893,000 | 3,804,000 | 13,220,000 |

Source: UC Berkeley Labor Center Analysis of 2005 California Health Interview Survey Data

Health care spending differs by source of coverage (employer-based versus non-employer-based), with consumers who purchase insurance through the individual market (outside of an employer or trade union group) spending more on health care than their counterparts who have coverage through their place of employment. This discrepancy holds true across all income categories. Those insured in the individual market likely pay more in total expenditures because they: (1) do not benefit from employer contributions to the cost of premiums, (2) pay significantly more in coverage-related administrative costs,[iii] (3) lack negotiating power with insurers which reduces their ability to obtain volume discounts, and (4) are charged more for insurance if they are at risk for expensive health care needs.

As Table 2 illustrates, families making between 251% to 300% of the FPL ($40,601 to $48,700 for a family of three) who obtained insurance through their employer spent 5.3% of their income on premium contributions and out-of-pocket spending. However, families in the same income group but insured through the individual market would spend 8.1% of their family income on premium and out-of-pocket expenses. This difference of 2.8% (or $1,344 for a family of three making $48,000) is primarily attributable to much higher premium contributions and slightly higher out-of-pocket spending levels, which are likely due to higher co-pays and deductibles.[iv]

Intuitively, the burden of health care costs is greater for households with lower incomes – the median proportion of family income spent on health care decreases as earnings increase.

Notably, out-of-pocket costs[v] represent a significant, but sometimes overlooked, portion of health care spending. This is especially true for lower-income residents and for those who purchase their coverage through the individual market.

### Table 2: Median Spending on Employee Share of Premiums and Out-of-pocket Costs as a Proportion of Total Family Income by Coverage Type, 2007

| | 101-200% FPL | 201-250% FPL | 251-300% FPL | 301-400% FPL | Over 300% FPL | Over 400% FPL | All Income Groups |
|---|---|---|---|---|---|---|---|
| **Employer-Based Coverage** | | | | | | | |
| Out-of-pocket | 1.7% | 1.1% | 1.1% | 0.9% | 0.6% | 0.6% | 0.8% |
| Premium | 4.2% | 2.7% | 2.8% | 1.7% | 1.0% | 0.9% | 1.4% |
| Total Spending | 7.3% | 4.7% | 5.3% | 3.2% | 2.2% | 2.0% | 2.9% |
| **Non-Employer-Based Coverage** | | | | | | | |
| Out-of-pocket | 2.2% | 1.4% | 1.7% | 1.6% | 1.0% | 0.7% | 1.4% |
| Premium | 11.0% | 10.5% | 5.0% | 4.6% | 3.5% | 3.3% | 4.7% |
| Total Spending | 12.0% | 10.5% | 8.1% | 7.0% | 5.0% | 4.6% | 6.8% |

While it is useful to focus on median or "typical" spending, this estimate does not capture the range of the spending distribution. Indeed, for some households, spending is well above median levels and consumes a large proportion of family income, particularly for those with incomes below 300% FPL and for those who purchase coverage in the individual market.

The difference in the distribution of spending between the employment-based and non-employment-based markets largely reflects demographic and risk-pooling differences between these two markets. Premiums and coverage on the individual market are tailored to individual risk using medical underwriting – insurers use characteristics such as health status, age, region, and medical history to price coverage. However, in the employment-based market, risk is shared across the employee group and premiums do not vary by individual health status. Given this difference, coverage in the individual market is significantly more expensive for older and sicker patients, which creates greater extremes in spending than would be found in the group market. Furthermore, Californians with individual health insurance tend to have less generous coverage than those with

employment-based insurance, which leads to greater exposure to high spending.[vi]

The variability in price and comprehensiveness of individual coverage is reflected in Table 4. Total spending for all income groups ranges from 1.4% in the 10th percentile to 26.4% in the 90th percentile and may exceed 45.7% for those in the 90th percentile of the 101-200% FPL income group. In contrast, variability in spending is much smaller for Californians with employment-based coverage (Table 3); total spending for all income groups ranges between 0.2% in the 10th percentile and 12% in the 90th percentile and may exceed 24.5% for those in the 90th percentile of the 101-200% FPL income group.

### Table 3: Proportion of Total Family Income Spent on Employee Share of Premiums and Out-of-pocket Costs, Employer Based, 2007

| | 101-200% FPL | 201-250% FPL | 251-300% FPL | 301-400% FPL | Over 300% FPL | Over 400% FPL | All Income Groups |
|---|---|---|---|---|---|---|---|
| **Out-of-Pocket** | | | | | | | |
| Median | 1.7% | 1.1% | 1.1% | 0.9% | 0.6% | 0.6% | 0.8% |
| 10th percentile | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| 25th percentile | 0.4% | 0.4% | 0.4% | 0.3% | 0.2% | 0.2% | 0.2% |
| 75th percentile | 4.1% | 2.8% | 2.7% | 2.3% | 1.7% | 1.5% | 2.1% |
| 90th percentile | 10.7% | 6.9% | 5.8% | 4.9% | 3.7% | 3.2% | 4.8% |
| **Premium** | | | | | | | |
| Median | 4.2% | 2.7% | 2.8% | 1.7% | 1.0% | 0.9% | 1.4% |
| 10th percentile | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| 25th percentile | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% | 0.0% |
| 75th percentile | 9.6% | 5.2% | 6.1% | 3.5% | 2.8% | 2.5% | 3.8% |
| 90th percentile | 16.7% | 10.5% | 11.4% | 6.1% | 5.5% | 4.9% | 8.1% |
| **Total Spending (Out-of-Pocket + Premiums)** | | | | | | | |
| Median | 7.3% | 4.7% | 5.3% | 3.2% | 2.2% | 2.0% | 2.9% |
| 10th percentile | 0.7% | 0.5% | 0.3% | 0.2% | 0.2% | 0.2% | 0.2% |
| 25th percentile | 2.6% | 2.1% | 1.6% | 1.3% | 0.9% | 0.8% | 1.0% |
| 75th percentile | 14.7% | 8.8% | 9.1% | 6.1% | 4.6% | 4.1% | 6.3% |
| 90th percentile | 24.5% | 15.7% | 15.1% | 10.2% | 8.1% | 7.2% | 12.0% |

### Table 4: Proportion of Total Family Income Spent on Out-of-pocket Costs, Non-Employer Based, 2007

| | 101-200% FPL | 201-250% FPL | 251-300% FPL | 301-400% FPL | Over 300% FPL | Over 400% FPL | All Income Groups |
|---|---|---|---|---|---|---|---|
| **Out-of-Pocket** | | | | | | | |
| Median | 2.2% | 1.4% | 1.7% | 1.6% | 1.0% | 0.7% | 1.4% |
| 10th percentile | 0.1% | 0.1% | 0.0% | 0.1% | 0.1% | 0.1% | 0.1% |
| 25th percentile | 0.6% | 0.6% | 0.3% | 0.5% | 0.3% | 0.2% | 0.3% |
| 75th percentile | 6.7% | 2.4% | 5.9% | 3.3% | 2.5% | 2.2% | 3.3% |
| 90th percentile | 10.7% | 9.8% | 9.7% | 8.0% | 6.1% | 5.9% | 8.5% |
| **Premium** | | | | | | | |
| Median | 11.0% | 10.5% | 5.0% | 4.6% | 3.5% | 3.3% | 4.7% |
| 10th percentile | 0.0% | 0.0% | 0.0% | 0.2% | 0.7% | 0.8% | 0.0% |
| 25th percentile | 5.2% | 0.0% | 2.2% | 2.2% | 1.7% | 1.7% | 1.8% |
| 75th percentile | 21.5% | 16.7% | 7.6% | 8.9% | 6.7% | 5.4% | 10.6% |
| 90th percentile | 33.1% | 23.6% | 20.7% | 13.7% | 11.1% | 9.8% | 19.4% |
| **Total Spending (Out-of-Pocket + Premiums)** | | | | | | | |
| Median | 12.0% | 10.5% | 8.1% | 7.0% | 5.0% | 4.6% | 6.8% |
| 10th percentile | 0.6% | 0.6% | 2.3% | 1.1% | 1.5% | 1.6% | 1.4% |
| 25th percentile | 7.0% | 1.7% | 4.8% | 3.7% | 2.8% | 2.7% | 3.0% |
| 75th percentile | 30.5% | 18.3% | 12.4% | 14.0% | 9.7% | 7.5% | 14.0% |
| 90th percentile | 45.7% | 33.2% | 30.4% | 19.1% | 16.7% | 12.4% | 26.4% |

## DISCUSSION

Health care proposals should take into account what Californians currently spend on health care. As this analysis reveals, health care currently represents a significant expense for lower and middle-income workers (families with incomes less than 300% of FPL), especially if they purchase coverage through the individual market.

The Governor's proposal has affordability protection for families up to 250% of FPL, but our analysis suggests that affordability protection may be necessary at even higher levels of income. For example, under the Governor's plan, families with incomes from 201-250% of FPL will have premium expenditures capped at 6% of family income if they purchase insurance through the pool. But families at 251-300% of FPL will not have the same protection, though one quarter of California families in this category who have coverage through the individual market spend more than 7.5% of income on premiums alone, while one in ten of families in this category spend more than 20% of income on premiums.

The contribution of out-of-pocket costs to total health care spending warrants further attention. Consumers today are paying a greater share of not only premium costs, but all health care costs. Approximately 41% of large employers (200 or more workers) in California reported that they were very likely to increase the amount employees pay for health insurance premiums in 2007, and another 28 percent said they were somewhat likely to do so.[vii] Parallel increases have occurred in deductibles for single PPO coverage since 2000. While 85% of employees faced a deductible of less

than $500 in 2000, only 69% did in 2006. The same trend holds true for out-of-pocket maximums. The proportion of California workers in PPOs with an out-of-pocket maximum of less than $1,500 has declined from 44% in 2000 to 21% in 2006.[viii]

Meanwhile, a new generation of products known as consumer-driven or high-deductible health plans (HDHP) have been gaining market share. These plans offer lower premiums in exchange for higher deductibles ($1,000 or more) and higher out-of-pocket limits. HDHPs are a recent innovation,[ix] yet just 4 years after their introduction, 16 percent of California employers now offer one.

Any individual coverage mandate or requirement for employees to take-up coverage should include standards for affordability. Such standards should take into account both premium and out-of-pocket expenditures. Without affordability standards on both premium and out-of-pocket expenditures, families could find they are required to purchase coverage they cannot afford to use. A mandate to purchase coverage without subsidies or affordability protections could have an adverse economic effect on many moderate income families.

## APPENDIX

To view additional information about the methodology and data set used in this analysis, please see Appendix A for this report at: http://laborcenter.berkeley.edu or at http://healthpolicy.ucla.edu.

## METHODOLOGY

The estimates in this Policy Brief were derived from Medical Expenditure Panel Survey (MEPS) Household component data for 2002 to 2004. This survey collects data on health care expenditures, insurance coverage, and other important health care issues. In order to approximate health care spending levels and income levels for Californians in 2007, only the western subset of the MEPS data was used.

The data on direct out-of-pocket spending and family income were inflated using the 2007 Medical Care Services CPI-U. The health care insurance premium data were inflated using the California HealthCare Foundation (CHCF) and Center for Studying Health System Change (CSHSC) 2006 *Employer Health Benefits Survey* to approximate the increase in premium costs to 2007 dollars. The methods used in this analysis were partially based on the approach used in a recent report using MEPS data to approximate the affordability of health insurance in Massachusetts[x] and mirror the approach used in a recent report by the California Budget Project and UCLA Center for Health Policy Research.[xi]

To estimate the actual number of individuals in California impacted by the proposed reforms, we used 2005 California Health Interview Survey (CHIS) data. CHIS is a population-based survey with over 45,000 household responses that collects data on health insurance coverage, family income, health status, disease condition, and various other health-related issues.

## AUTHOR INFORMATION

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## END NOTES

[i] Dubay, L., et al., *The Uninsured And The Affordability Of Health Insurance Coverage*. Health Affairs, January/February 2007; 26(1): w22-w30.

[ii] The non employment based insurance category includes individuals and families that purchased insurance in the private market by themselves or through purchasing pools. This indicates that they did not have access to premium subsidies that would be provided by most employers.

[iii] Pauly, M., and Percy, A., *Cost and performance: a comparison of the individual and group health insurance markets*. Journal of Health Politics, Policy, and Law, 2000. 25: p. 9-26.

[iv] Pollitz, K., and Sorian, R., *Ensuring Health Security: Is the Individual Market Ready for Prime Time?* Health Affairs Web Exclusive, October 23, 2002. http://content.healthaffairs.org/cgi/content/full/hlthaff.w2.372v1/DC1; Buntin, M., et al., *Trends and Variability in Individual Insurance Products.* Health Affairs Web Exclusive, September 24, 2003. http://content.healthaffairs.org/cgi/content/full/hlthaff.w3.449v1/DC1.

[v] Consumer health care spending in the MEPS survey includes two components: premium costs and out of pocket costs which include expenses such as co-payments, coinsurance, and deductible requirements. Out-of-pocket spending includes expenses paid by the user or other family member to hospitals, physicians, other health care providers (including dental and home health care), and pharmacies. Over-the-counter drugs, institutionalized care, and cosmetic surgery were not included.

[vi] Kaiser Family Foundation, *Update on Individual Health Insurance,* 2004; Kaiser Family Foundation, *How Accessible is Individual Health Insurance for Consumer in Less-Than-Perfect Health?* 2001; Pollitz, K., and Sorian, R., *Ensuring Health Security: Is the Individual Market Ready for Prime Time?* Health Affairs Web Exclusive, October 23, 2002. http://content.healthaffairs.org/cgi/content/full/hlthaff.w2.372v1/DC1;

[vii] California Health Care Foundation, *California Employer Health Benefits Survey,* November 2006.

[viii] Ibid.

[ix] Ibid.

[x] Holohan, J., et al., *Setting a Standard of Affordability for Health Insurance Coverage in Massachusetts*. The Urban Institute. http://www.mass.gov/Qhic/docs/Urban%20Institute%20Affordability%20Report%20(08-06).pdf

[xi] Carroll, D., et al, *What Does It Take for a Family to Afford to Pay for Health Care?* UCLA Center for Health Policy Research, 2007.