

ONE HUNDRED TWELFTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
2125 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515-6115

Majority (202) 225-2927
Minority (202) 225-3641

April 24, 2012

Ms. Marilyn Tavenner
Acting Administrator
Centers for Medicare and Medicaid Services
7500 Security Boulevard
Baltimore, MD 21244-1850

Dear Acting Administrator Tavenner:

Pursuant to Rules X and XI of the U.S. House of Representatives, the Committee on Energy and Commerce is examining the implementation of the Consumer Operated and Oriented Plan (CO-OP).

The CO-OP program was authorized in Section 1322 of the Patient Protection and Affordable Care Act (P.L. 111-148) to create nonprofit health insurance issuers to offer qualified health care plans to individuals and small groups in the States. The Department of Health and Human Services (HHS) awards loans to the States to (1) fund start-up costs, and (2) to meet State solvency requirements. A net total of \$3.4 billion has been appropriated to fund these loans. As required by the Federal Credit Reform Act of 1990, the CO-OP program must estimate its subsidy and administrative costs up front.

In accordance with Budget Circular A-11, the Office of Management and Budget (OMB) estimated the subsidy percentage for the CO-OP program (see the President's Budget Appendix for Fiscal Year 2013):

Description \$ in millions	2012 est.	2013 est.	Total 2012-13 est.
Loan Levels:			
Startup Loans	\$675	\$195	\$870
Solvency Loans	4,950	1,430	6,380
Total	\$5,625	\$1,625	\$7,250
Loan Subsidy %:			
Startup Loans	37.51	37.66	
Solvency Loans	43.99	43.78	
Average Total	43.21	43.05	
Subsidy Budget Authority:			
Startup Loans	\$253	\$73	\$326
Solvency Loans	2,178	626	2,804
Total	\$2,431	\$699	\$3,130

As the above table indicates, the loan subsidy percentage, or expected losses percentage, is about 43 percent of the face amount of \$7.25 billion for all the loans. For the amounts detailed to be spent in the loan subsidy part of the CO-OP program (see table), the amount of expected losses is estimated to be about \$3.1 billion of the \$3.4 billion appropriated (91 percent). These losses exceed the estimate HHS presented in its proposed rule, (see Federal Register, July 20, 2011), that showed 35 percent of the Solvency Loans and 40 percent of the Startup Loans would be expected to default. Unfortunately, HHS did not present the dollar amount of the expected losses to compare to the figures in the President's Budget Appendix which showed a 91 percent expected loss in the amount authorized for the loan subsidy program.

On December 13, 2011, HHS issued final rules on the CO-OP program (45 CFR 156). The 15-member CO-OP Program Advisory Board, appointed on June 23, 2010, to make recommendations on awarding loans, issued its public report on April 15, 2011. The Board recommended four major principles for awarding loans which were incorporated in the final rules as follows:

1. Consumer operation, control, and focus must be the salient features of the CO-OP and must be sustained over time.
2. Solvency and the financial stability of coverage should be maintained and promoted.
3. CO-OPs should encourage care coordination, quality and efficiency to the extent feasible in local provider and health plan markets.
4. Initial loans should be rolled out as expeditiously as possible so that CO-OPs can compete in the exchanges in the critical first open enrollment period.

CO-OP plans must meet the same standards under State law as any other health insurer, including State solvency and reserve requirements. Section 1322(b)(3) of PPACA states that the standards for the repayment of loans awarded under the CO-OP program must take into consideration “any appropriate State reserve requirements, solvency regulations, and requisite surplus note arrangements that must be constructed in a State.”

Moreover, HHS recognized that a loan is typically considered a liability, and given that solvency loans must be repaid over a 15-year period, there is a risk that State insurance regulators may treat solvency loans issued by HHS “as debt, rather than capital that would satisfy State solvency and reserve requirements.” 76 Fed. Reg. 77392, 77403. Thus, HHS acknowledged that solvency loans may have to be structured as “surplus notes”, as they are the only types of loans that State insurance regulators will recognize as assets rather than debt.” This is because in terms of CO-OP solvency, the surplus notes could appear as an asset on the CO-OP balance sheets, rather than the debt that they actually are.

To date, the Centers for Medicare and Medicaid Services (CMS) has awarded 10 organizations -- offering coverage in 10 States -- over \$845 million in start-up and solvency loans to help them establish private, non-profit, consumer-governed health insurance plans. Each of these States, to some extent, permits mutual insurance companies to issue” surplus notes.” However, according to the National Association of Mutual Insurance Companies, surplus notes are regarded by investors “as relatively high risk since they are both unsecured and subordinated to the interests of the policyholders.” (See Focus on The Future Options For the Mutual Insurance Company – Pursuing Change: The Alternatives, posted March 25, 2010, <http://www.namic.org/Home/ReadArticle/86935b7a-bb05-45b5-b6ab-cc78c144cf93>.)

Because the CO-OP regulation does not specify any collateral for the loans, and, as mentioned above, holders of surplus notes are usually at the bottom rung in terms of priority if an insurer goes into rehabilitation or liquidation, the Federal taxpayer would be among the last in line for repayment should a CO-OP experience financial distress.

The potential losses to federal taxpayers are not the only concern. Past instances of insurer insolvency demonstrate the severe negative impact on the insurance markets. For example, the Government Accountability Office (GAO) found that, between January 1988 and June 1991, the financial mismanagement and insolvency of multiple employer welfare arrangements left at least 398,000 participants and their beneficiaries with over \$123 million in unpaid claims and many other participants without insurance. (See GAO Report No. GAO/HRD-92-40, “Employee Benefits: States Need Labor’s Help Regulating Multiple Employer Welfare Arrangements,” March 1992.)

Finally, we are concerned that HHS is awarding loans to entities that do not meet the statutory requirements for eligibility in this program. PPACA Section 1322 (c)(2)(A) disqualifies an organization or a related entity that provided health insurance prior to July 16, 2009. Nevertheless, three of the HHS loans went to recipients sponsored by the Freelancers Union, whose members own a for-profit corporation, the Freelancers Insurance Company (FIC), established in 2008. Since FIC may be considered a related entity that provided health insurance

prior to July 16, 2009, this raises a question about the independence of the Freelancer Union – sponsored entities from an ineligible, related entity.

To assist the Committee’s oversight of the CO-OP program, please provide by May 8, 2012, the following documents:

1. All documents related to “surplus notes” in connection with the CO-OP program.
2. All documents related to the loan applications submitted since December 11, 2011, including detailed business plans and schedules for operations, financial assessments, information relating to the expertise of the proposed management team, and information on the proposed management team’s assessment of the business market and proposed state markets.
3. All documents between December 11, 2011, and February 21, 2012, related to the decision to grant or deny loans.
4. All documents relating to HHS interpretation of the statutory requirements for eligibility in the CO-OP program.
5. All documents relating to HHS and/or CMS communication with the State Departments of Insurance in the 10 States where the loan recipients to date intend to operate.

We also request that you provide written answers to the following questions by May 8, 2012:

6. What loan review process has been established to review loan applications and perform due diligence before loan award?
7. What procedures are being taken to prevent fraud, waste and abuse?
8. What factors resulted in a 43 percent subsidy percentage which are estimated to cost the taxpayers \$3.1 billion for FY 2012 and 2013 or 91 percent of the \$3.4 billion authorized for the program?
9. What startup and solvency problems are envisioned for the new CO-OP insurers?
10. Because of the high loan subsidies, to what extent will CO-OP insurers have an unfair competitive advantage over private-sector insurers?
11. Have any of the loans awarded by HHS been structured as “surplus notes”? If so, which ones? Under some State insurance laws, neither principal nor interest may be repaid without department of insurance approval. Do the repayment schedules take into account that neither HHS nor the CO-OP will have any control over whether/when interest payments or principal payments are made back to the surplus note holder? If the State

department of insurance refuses to permit the CO-OP to repay HHS due to solvency, stability or other financial concerns, what will HHS do?

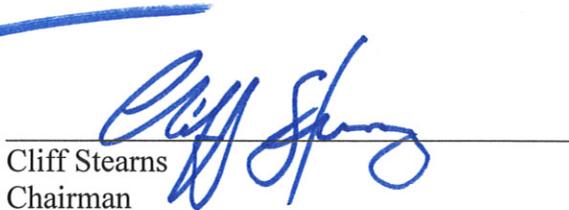
12. How many applicants for CO-OP loans were denied an award? Were any of the loan recipients previously denied?
13. What criteria were used by HHS to grant the loans announced so far in 2012? Did HHS receive and evaluate applications in the absence of final regulations?
14. How did HHS determine that the loan recipients had a high probability of becoming financially viable? What criteria were used to make this determination? Did the threshold of probable financial viability change from application to application?
15. In monitoring the performance of loan recipients will HHS:
 - review State financial examinations and seek information from state regulators?
 - review provider complaints regarding prompt payments?
 - review consumer complaints?
 - compare actual experience to the business plan for enrollments, premium revenue, medical costs, utilization, and net income?
16. What action(s) has HHS taken to ensure that the loans are repaid?
17. If a loan recipient cannot pay its claims, does HHS expect that State guaranty associations, and therefore other insurers in the CO-OP's State, will have to pay at least a portion of the unpaid claims to its policyholders? What is the cost-shifting impact on the other insurers in the State and the premiums they charge to their policyholders?
18. What action(s) has HHS taken to protect policyholders whose CO-OP has become insolvent? How will HHS ensure that their claims are paid? How will HHS ensure that the providers contracting with CO-OPs who become insolvent are paid?

An attachment to this letter provides additional information about how to respond to the Committee's request. If you have any questions regarding this request, please contact the Committee staff at (202) 225-2927.

Sincerely,



Fred Upton
Chairman



Cliff Stearns
Chairman
Subcommittee on Oversight and Investigations



Joseph R. Pitts
Chairman
Subcommittee on Health



Marsha Blackburn
Vice Chairman
Subcommittee on Commerce, Manufacturing,
and Trade

Attachment

cc: The Honorable Henry A. Waxman, Ranking Member

The Honorable Diana DeGette, Ranking Member
Subcommittee on Oversight and Investigations

The Honorable Frank Pallone, Jr., Ranking Member
Subcommittee on Health

RESPONDING TO COMMITTEE DOCUMENT REQUESTS

In responding to the document request, please apply the instructions and definitions set forth below:

INSTRUCTIONS

1. In complying with this request, you should produce all responsive documents that are in your possession, custody, or control or otherwise available to you, regardless of whether the documents are possessed directly by you.
2. Documents responsive to the request should not be destroyed, modified, removed, transferred, or otherwise made inaccessible to the Committee.
3. In the event that any entity, organization, or individual named in the request has been, or is currently, known by any other name, the request should be read also to include such other names under that alternative identification.
4. Each document should be produced in a form that may be copied by standard copying machines.
5. When you produce documents, you should identify the paragraph(s) and/or clause(s) in the Committee's request to which the document responds.
6. Documents produced pursuant to this request should be produced in the order in which they appear in your files and should not be rearranged. Any documents that are stapled, clipped, or otherwise fastened together should not be separated. Documents produced in response to this request should be produced together with copies of file labels, dividers, or identifying markers with which they were associated when this request was issued. Indicate the office or division and person from whose files each document was produced.
7. Each folder and box should be numbered, and a description of the contents of each folder and box, including the paragraph(s) and/or clause(s) of the request to which the documents are responsive, should be provided in an accompanying index.
8. Responsive documents must be produced regardless of whether any other person or entity possesses non-identical or identical copies of the same document.
9. The Committee requests electronic documents in addition to paper productions. If any of the requested information is available in machine-readable or electronic form (such as on a computer server, hard drive, CD, DVD, back up tape, or removable computer media such as thumb drives, flash drives, memory cards, and external hard drives), you should immediately consult with Committee staff to determine the appropriate format in which to produce the information. Documents produced in electronic format should be organized, identified, and indexed electronically in a manner comparable to the organizational structure called for in (6) and (7) above.

10. If any document responsive to this request was, but no longer is, in your possession, custody, or control, or has been placed into the possession, custody, or control of any third party and cannot be provided in response to this request, you should identify the document (stating its date, author, subject and recipients) and explain the circumstances under which the document ceased to be in your possession, custody, or control, or was placed in the possession, custody, or control of a third party.

11. If any document responsive to this request was, but no longer is, in your possession, custody or control, state:

- a. how the document was disposed of;
- b. the name, current address, and telephone number of the person who currently has possession, custody or control over the document;
- c. the date of disposition;
- d. the name, current address, and telephone number of each person who authorized said disposition or who had or has knowledge of said disposition.

12. If any document responsive to this request cannot be located, describe with particularity the efforts made to locate the document and the specific reason for its disappearance, destruction or unavailability.

13. If a date or other descriptive detail set forth in this request referring to a document, communication, meeting, or other event is inaccurate, but the actual date or other descriptive detail is known to you or is otherwise apparent from the context of the request, you should produce all documents which would be responsive as if the date or other descriptive detail were correct.

14. The request is continuing in nature and applies to any newly discovered document, regardless of the date of its creation. Any document not produced because it has not been located or discovered by the return date should be produced immediately upon location or discovery subsequent thereto.

15. All documents should be bates-stamped sequentially and produced sequentially. In a cover letter to accompany your response, you should include a total page count for the entire production, including both hard copy and electronic documents.

16. Two sets of the documents should be delivered to the Committee, one set to the majority staff in Room 316 of the Ford House Office Building and one set to the minority staff in Room 564 of the Ford House Office Building. You should consult with Committee majority staff regarding the method of delivery prior to sending any materials.

17. In the event that a responsive document is withheld on any basis, including a claim of privilege, you should provide the following information concerning any such document: (a) the reason the document is not being produced; (b) the type of document; (c) the general subject matter; (d) the date, author and addressee; (e) the relationship of the author and addressee to each

other; and (f) any other description necessary to identify the document and to explain the basis for not producing the document. If a claimed privilege applies to only a portion of any document, that portion only should be withheld and the remainder of the document should be produced. As used herein, "claim of privilege" includes, but is not limited to, any claim that a document either may or must be withheld from production pursuant to any statute, rule, or regulation.

18. If the request cannot be complied with in full, it should be complied with to the extent possible, which should include an explanation of why full compliance is not possible.

19. Upon completion of the document production, you should submit a written certification, signed by you or your counsel, stating that: (1) a diligent search has been completed of all documents in your possession, custody, or control which reasonably could contain responsive documents; (2) documents responsive to the request have not been destroyed, modified, removed, transferred, or otherwise made inaccessible to the Committee since the date of receiving the Committee's request or in anticipation of receiving the Committee's request, and (3) all documents identified during the search that are responsive have been produced to the Committee, identified in a privilege log provided to the Committee, as described in (17) above, or identified as provided in (10), (11) or (12) above.

DEFINITIONS

1. The term "document" means any written, recorded, or graphic matter of any nature whatsoever, regardless of how recorded, and whether original or copy, including but not limited to, the following: memoranda, reports, expense reports, books, manuals, instructions, financial reports, working papers, records, notes, letters, notices, confirmations, telegrams, receipts, appraisals, pamphlets, magazines, newspapers, prospectuses, interoffice and intra-office communications, electronic mail ("e-mail"), instant messages, calendars, contracts, cables, notations of any type of conversation, telephone call, meeting or other communication, bulletins, printed matter, computer printouts, invoices, transcripts, diaries, analyses, returns, summaries, minutes, bills, accounts, estimates, projections, comparisons, messages, correspondence, press releases, circulars, financial statements, reviews, opinions, offers, studies and investigations, questionnaires and surveys, power point presentations, spreadsheets, and work sheets. The term "document" includes all drafts, preliminary versions, alterations, modifications, revisions, changes, and amendments to the foregoing, as well as any attachments or appendices thereto. The term "document" also means any graphic or oral records or representations of any kind (including, without limitation, photographs, charts, graphs, voice mails, microfiche, microfilm, videotapes, recordings, and motion pictures), electronic and mechanical records or representations of any kind (including, without limitation, tapes, cassettes, disks, computer server files, computer hard drive files, CDs, DVDs, back up tape, memory sticks, recordings, and removable computer media such as thumb drives, flash drives, memory cards, and external hard drives), and other written, printed, typed, or other graphic or recorded matter of any kind or nature, however produced or reproduced, and whether preserved in writing, film, tape, electronic format, disk, videotape or otherwise. A document bearing any notation not part of the original text is considered to be a separate document. A draft or non-identical copy is a separate document within the meaning of this term.

2. The term "documents in your possession, custody or control" means (a) documents that are in your possession, custody, or control, whether held by you or your past or present agents, employees, or representatives acting on your behalf; (b) documents that you have a legal right to obtain, that you have a right to copy, or to which you have access; and (c) documents that have been placed in the possession, custody, or control of any third party.

3. The term "communication" means each manner or means of disclosure, transmission, or exchange of information, in the form of facts, ideas, opinions, inquiries, or otherwise, regardless of means utilized, whether oral, electronic, by document or otherwise, and whether face-to-face, in a meeting, by telephone, mail, e-mail, instant message, discussion, release, personal delivery, or otherwise.

4. The terms "and" and "or" should be construed broadly and either conjunctively or disjunctively as necessary to bring within the scope of this request any information which might otherwise be construed to be outside its scope. The singular includes the plural number, and vice versa. The masculine includes the feminine and neuter genders.

5. The terms "person" or "persons" mean natural persons, firms, partnerships, associations, limited liability corporations and companies, limited liability partnerships, corporations, subsidiaries, divisions, departments, joint ventures, proprietorships, syndicates, other legal, business or government entities, or any other organization or group of persons, and all subsidiaries, affiliates, divisions, departments, branches, and other units thereof.

6. The terms "referring" or "relating," with respect to any given subject, mean anything that constitutes, contains, embodies, reflects, identifies, states, refers to, deals with, or is in any manner whatsoever pertinent to that subject.

7. The terms "you" or "your" mean and refers to

For government recipients:

"You" or "your" means and refers to you as a natural person and the United States and any of its agencies, offices, subdivisions, entities, officials, administrators, employees, attorneys, agents, advisors, consultants, staff, or any other persons acting on your behalf or under your control or direction; and includes any other person(s) defined in the document request letter.