

# Dirigo Watch

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## The Savings Offset Payment: Dirigo Health's Questionable Funding Strategy by Tarren Bragdon

The most politically-charged aspect of the Dirigo Health initiative is the funding mechanism called the Savings Offset Payment (SOP) tax. The funding mechanism is initiated when the Dirigo Health Agency makes a determination of how much the Dirigo Health initiative has "saved" Maine's healthcare system. Then, the SOP tax is levied to "recover" those savings from individuals with private health insurance.

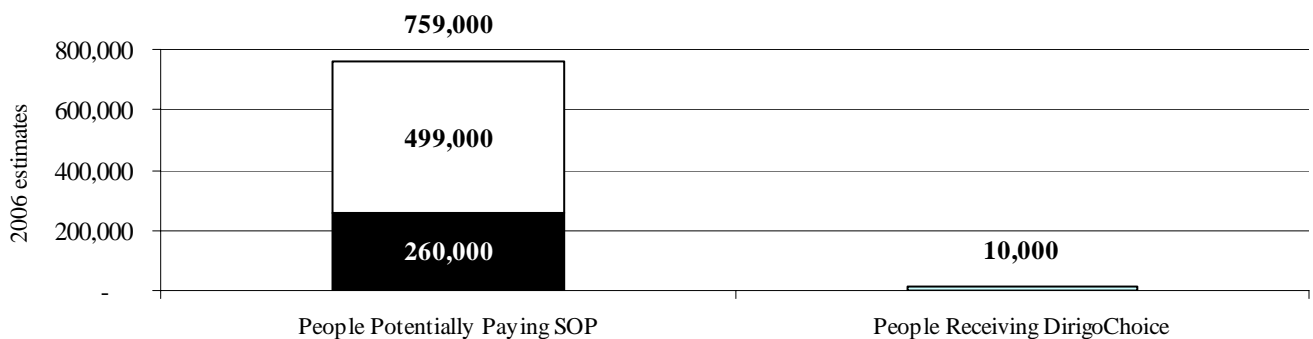
Since the summer of 2003, Dirigo Health has been funded using one-time federal funds of \$53 million.[1] Now that initial funding is running out, creating a budget hole for the Dirigo Health initiative. Effective January 1, 2006, that funding gap was filled by the SOP tax.

In October 2005, the Superintendent of Insurance certified that the Dirigo Health initiative "saved" Maine's healthcare system \$43.7 million. In November 2005, the Dirigo Health Board of Directors voted 4 to 1 to assess a 2.408 percent SOP tax. The SOP tax functions similarly to an excise tax; a 2.4% surcharge is added to all paid health-care claims.

The SOP tax exemplifies the problems inherent in the Dirigo Health Initiative:

- Consumers are not seeing the health "savings" despite the Superintendent's ruling.
- The SOP tax reaches up to 759,000 Mainers, while funding DirigoChoice that reaches only 10,000 Mainers.
- Without the SOP tax, Dirigo Health would be forced to compete against Medicaid, education and other priorities for scarce State General Fund dollars. In this fiscal fight, Dirigo Health will likely lose.
- If insurers pass along the SOP tax to policyholders, then Maine individuals, small businesses and large companies will face cost increases of \$70 per individual or \$200 per family per year to fund Dirigo Health.
- If insurers are forced to bear the burden of the SOP tax, as envisioned in LD 1935, the very financial viability of Maine's entire private health insurance market is in doubt.

**Chart 1: Number of SOP Payers Compared to DirigoChoice Recipients**



Sources: Dirigo Health Agency, U.S. Census Bureau, MHPC Calculations

■ Number of people making less than 300% of poverty with private health insurance.

**Consumers Not Seeing the Health Savings.**

The whole concept that there have been savings resulting from Dirigo Health is questionable. Currently, several health insurers and the Maine State Chamber of Commerce are suing the State, in part over the savings methodology.

A consultant hired by the State Chamber tested the formulas that the Dirigo Health Agency used to calculate the hospital-generated savings from Dirigo by using data from New Hampshire hospitals. New Hampshire does not have Dirigo Health regulations and, therefore, should not show any “savings.” Nevertheless, Dirigo’s formulas showed \$45 million in savings for New Hampshire hospitals.[2] This illogical result raises questions about the accuracy of the savings that resulted from Dirigo Health.

Additionally, the average person may not “feel” that there have been savings. Individual Anthem BC/BS insurance policyholders—almost 36,000 Mainers or 83% of the individual market[3]—just had a 16% premium increase for 2006 prior to the SOP tax (on \$2,250-\$10,000 deductible policies).[4]

The savings are also a tough sell to health insurance consumers because, by the Superintendent’s own admission, the major driver of the savings is not the DirigoChoice program. In fact, as Table 1 below shows, 94% of “savings” (\$41 million) are not from Dirigo Choice—yet DirigoChoice requires almost 100% of the SOP tax funding.

**The SOP Tax Impacts up to 759,000 Mainers.**

The SOP tax potentially reaches everyone with private health insurance. According to the U.S. Census Bureau, up to 759,000 Maine individuals potentially are impacted by the SOP tax, as they have private coverage.[7]

The SOP tax hits the poor to subsidize the middle class. Again, according to the U.S. Census Bureau, 260,000 Mainers have private health insurance yet also have incomes low enough to be on DirigoChoice (below 300% of poverty or \$58,000 a year for a family of four). These 260,000 Mainers will pay the SOP tax so that people who may make more than they do can have subsidized coverage. For example, a family of four with private health insurance earning \$40,000 could be subject to the SOP tax to subsidize a family of four on DirigoChoice earning \$58,000.

DirigoChoice, which receives almost all of the SOP tax funding, will reach only 10,000 people in 2006--see Chart 1.

The SOP tax hits all small businesses but exempts certain large companies. If a large company is self-insured (self-administered) or uses an out of state insurer, they don’t pay the SOP tax. The SOP tax creates an incentive to large Maine businesses to switch to an out-of-state insurance administrator. In a sense, the message to large Maine businesses is: move your health benefit out of Maine and save thousands. Such an action could result in hundreds of lost jobs at Maine insurers, and also, reduce the funding-base of the SOP tax.

**Table 1**  
**Analysis of Savings Deemed Reasonably Supported**  
**by Superintendent of Insurance**

	<b>BOI Deemed Reasonably Supported Savings [5]</b>	<b>Cost to State Taxpayers[6]</b>	<b>Return on Investment (ROI) of Taxpayer Money</b>
Hospital Savings Initiatives	\$33.7 million	\$0 (voluntarily by Maine hospitals)	Infinite
Uninsured Savings Initiatives from DirigoChoice	\$2.7 million	\$27 million (est. through 12/2005)	-90%
Health Care Provider Fee Savings Initiatives through Medicaid	\$7.3 million	\$7.3 million (paid by taxpayers in FY2006 Medicaid budget)	0%
<b>Total</b>	<b>\$43.7 million</b>	<b>\$33.3 million</b>	

Source: Maine Bureau of Insurance, MHPC calculations.

**The SOP Tax Will Cost about \$70 per Individual or \$200 per Family Per Year**

Based on current law, the SOP tax will increase health insurance premiums on Mainers by about two percent. In dollar terms, the SOP tax will increase the average annual premium by approximately \$70 for a Maine individual, or \$200 for a Maine family.[8] This tax comes on top of the two percent premium tax Mainers already pay on all non-HMO health insurance products. The SOP tax adds to this existing tax burden on health premiums.

Ironically, the higher cost associated with the tax will increase the number of Maine people without private insurance, making the SOP tax seemingly in conflict with the goals of Dirigo Health. A one percent increase in health insurance premiums is estimated to result in 1,250 Maine people dropping health insurance coverage. Therefore, the SOP tax could cause up to 2,500 Maine people to become uninsured.[9]

**LD 1935 Could Significantly Impact Maine’s Private Insurance Market**

The reality of the SOP tax has raised concern among businesses, insurers and members of the public who will be responsible for paying the tax. In an attempt to deflect this concern, Senator John Martin (D-Aroostook County) introduced LD 1935 – An Act to Protect Health Insurance Consumers.[10] The bill had a public hearing on February 14, 2006 and is scheduled to be voted on in early March by the Maine State Legislature’s Joint Standing Committee on Insurance and Financial Services.

If LD 1935 is passed, insurers will not be allowed to pass along the costs of the SOP tax to policyholders which could make it

more difficult for an insurer to be financially viable in the Maine market. The SOP tax is effectively a huge tax increase on Maine insurers. The three major Maine insurers would face 161-375 percent increases in state and local taxes.[11] See Chart 2 and Table 2. Considered it another way, if LD 1935 is passed, the SOP tax will become a large “effective state corporate income tax” on insurers. Maine insurers will face an “effective state corporate income” tax of 11-40 percent of profits on top of the 36 percent federal corporate income tax they already pay.[12] See Chart 3 and Table 2.

The legislation is inherently discriminatory against one industry. Such legislation would be analogous to the Legislature passing a bill that would prevent gas stations from passing along the gas tax to consumers.

**Final thoughts – from Dirigo Health to Disco Health**

Maine policymakers should be more focused on reducing the costs of private health insurance for Maine individuals and businesses. That goal will not be accomplished through the SOP tax. The SOP tax means higher premiums or, if LD 1935 is passed, a potential death-blow to the financial viability of Maine’s private health insurance market. However, without the SOP tax, the funding of Dirigo Health is questionable if the program has to compete for funding in the State General Fund.

Maine policymakers should examine the 47 states that have a higher rate of lower-income adults with private insurance. How are these states able to make private health insurance an affordable option? Dirigo is Latin for “I lead.” Maybe, Dirigo Health should focus less on “I lead” and focus more on “I learn,” which in Latin is ‘Disco.’

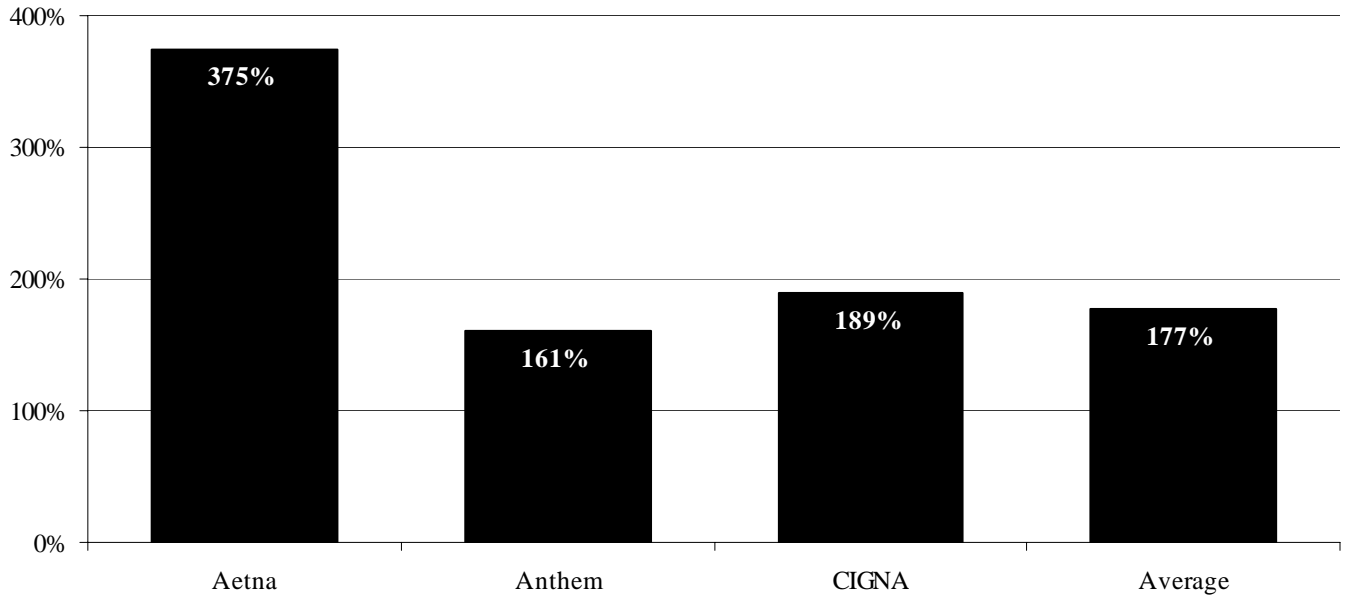
**Table 2**  
**Analysis of Impact of Savings Offset Payment on Three Largest Maine Insurers**

*(2004 figures, latest available)*

Company	Aetna	Anthem (with Maine Partners)	CIGNA	Total	% of Total
Average Number of Members	47,197	301,343	23,530	372,070	
Revenue	\$172,588,439	\$901,944,887	\$86,922,467	\$1,161,455,793	100%
Medical Claims	\$140,539,716	\$757,104,772	\$63,979,362	\$961,623,850	84%
Administrative Costs	\$23,180,120	\$99,414,681	\$8,716,215	\$131,311,016	11%
State and Local Taxes Paid (included in admin)	\$903,141	\$11,336,557	\$815,030	\$13,054,728	1%
Profit - Underwriting Gains	\$8,868,603	\$45,747,623	\$14,226,890	\$68,843,116	6%
Savings Offset Payment (2.408% of claims)	\$3,384,196	\$18,231,083	\$1,540,623	\$23,155,902	2%
SOP as % increase in State and Local Taxes	375%	161%	189%	177%	
SOP as % of Profit	38.20%	39.90%	10.80%	33.60%	
Estimated Federal Corporate Income Tax	35.50%	35.50%	35.50%	35.50%	
Total Effective Income Tax (estimated)	73.70%	75.40%	46.30%	69.10%	

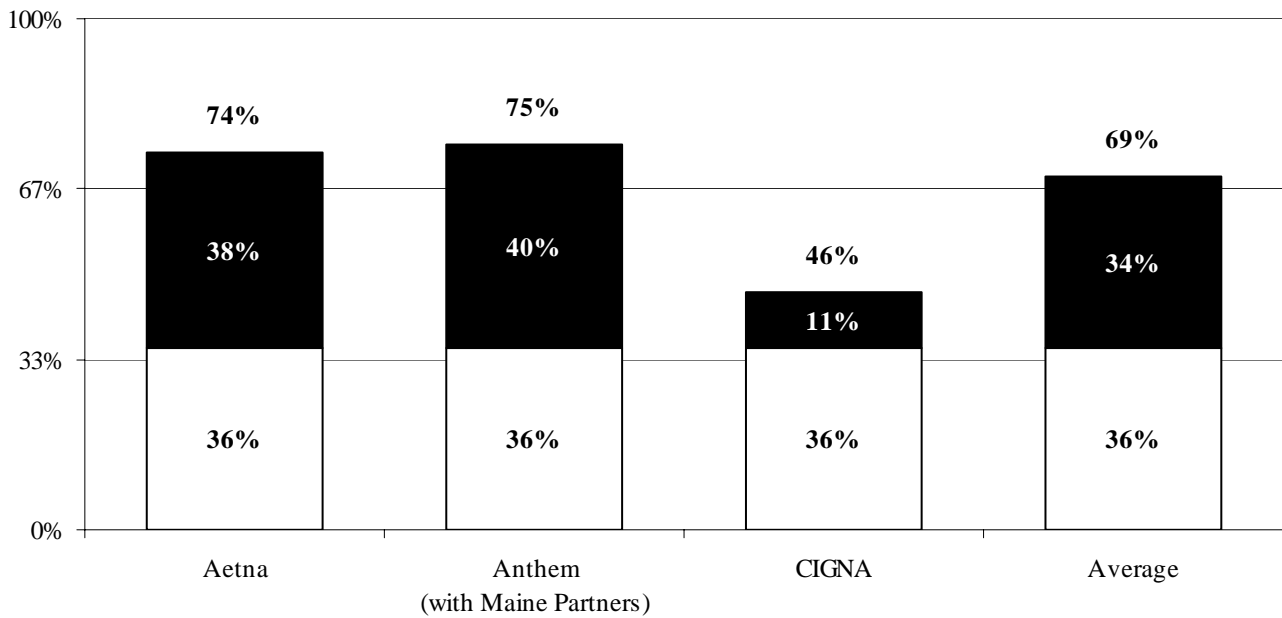
Source: Maine Bureau of Insurance, MHPC calculations.

**Chart 2: SOP as Percent Increase in Insurers' State & Local Taxes**  
*(based on 2004 figures)*



Source: Bureau of Insurance, MHPC calculations (with Maine Partners)

**Chart 3: SOP as Percent of Insurers' Profit [13]**  
*(based on 2004 figures)*



Source: Bureau of Insurance, MHPC calculations

□ Estimated Federal Corporate Income Tax

■ SOP as % of Profit

**Notes**

1. This money was provided to the State as Federal fiscal relief in 2003.
2. Stiles, Esq. William. "Filing to Maine Superintendent of Insurance." October 21, 2005. Exhibit 5. [http://www.mainechamber.org/pdf/Dirigo%20Working%20Group/Sheils%20\(The%20Lewin%20Group\)%20Testimony.pdf](http://www.mainechamber.org/pdf/Dirigo%20Working%20Group/Sheils%20(The%20Lewin%20Group)%20Testimony.pdf)
3. Maine Bureau of Insurance. MARKET SNAPSHOT: INDIVIDUAL MARKET. September 30, 2005. [http://www.state.me.us/pfr/ins/Snapshot\\_individual.htm](http://www.state.me.us/pfr/ins/Snapshot_individual.htm)
4. Anthem communication to policyholders. January 25, 2006.
5. Maine Superintendent of Insurance Alessandro A. Iuppa. REVIEW OF AGGREGATE MEASURABLE COST SAVINGS DETERMINED BY DIRIGO HEALTH FOR THE FIRST ASSESSMENT YEAR. October 29, 2005. [www.state.me.us/pfr/ins/ins05700Dirigo.htm](http://www.state.me.us/pfr/ins/ins05700Dirigo.htm)
6. Maine Legislature's Office of Fiscal and Program Review. 2004-2005 Dirigo Health Fund Status (dated 10/17/05) and 2006-2007 Dirigo Health Fund – Budgeted Status (dated 10/18/05) for spending through September 30, 2005. Author's calculations for full year figure.
7. All figures from US Census Bureau based on three-year average for Maine for 2002-2004. [www.Census.gov](http://www.Census.gov). Counting only those 0-64 years of age, those 65+ are on Medicare.
8. Kaiser Family Foundation. 2003 Maine premium figures for employer-based coverage. [www.StateHealthFacts.org](http://www.StateHealthFacts.org).
9. Stiles, Esq., Page 15.
10. Sponsored by Senator John Martin (D-Aroostook). LD 1935 – An Act to Protect Health Insurance Consumers.
11. <http://janus.state.me.us/legis/LawMakerWeb/externalsiteframe.asp?ID=280020051&LD=1935&Type=1&SessionID=6>
12. Based on 2004 figures received from the Maine Bureau of Insurance calculated with a 2.408% SOP on all 2004 claims paid.
13. Profits means underwriting gains, based on Maine Bureau of Insurance 2004 data for large, small and individual insurance plans sold in Maine by the noted insurers.

**Methodology**

For taxpayer costs resulting from Dirigo Health "savings," MHPC used reported expenditures for the Dirigo Health Agency for calendar year 2005.

For calculated cost and effect of the SOP, MHPC used reported medical claims paid, state and local taxes paid, total administrative expenses and underwriting gain for the three largest Maine insurers for 2004, the latest figures available, as reported to the Maine Bureau of Insurance. To calculate the SOP tax, a 2.408 percent rate for all medical claims paid was applied.

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DirigoWatch is a quarterly publication of The Maine Heritage Policy Center that provides research, updates and commentary on the state-run Dirigo Health initiative. All information is from sources considered reliable, but may be subject to inaccuracies, omissions, and modifications.

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