Premiums and Stability in the Individual Health Insurance Market

The Effects of Young Adult Enrollment and Subsidies

Key findings:

- Eliminating the Affordable Care Act’s premium tax credits would substantially increase premiums and reduce overall enrollment in the individual market.
- Reduced enrollment of young adults in the individual health insurance market would lead to modest premium increases.
- Alternative types of subsidies—such as vouchers—could cause premiums to become more sensitive to the age mix of enrollees.
- Eliminating the individual mandate would cause small increases in premiums but large declines in enrollment.

The Affordable Care Act (ACA) established new online markets for obtaining health insurance known as “Marketplaces.” The law requires insurers in the Marketplaces to offer coverage to all eligible buyers. To keep insurance affordable, insurers need to spread risk across a broad pool of individuals, including healthier young adults, to offset the costs of older and sicker enrollees. In theory, low levels of young adult enrollment could cause insurers to raise premiums, which could in turn price an ever-increasing number of buyers out of the market. In the worst-case scenario, this would lead to a “death spiral” in which the market collapses from high premiums and dwindling enrollment.

However, the ACA has built-in mechanisms to buffer the effects of lower-than-expected enrollment by young adults (see sidebar). The ACA also encourages participation by younger adults and healthier populations of all ages by including a “carrot”—subsidies in the form of tax credits for lower-income individuals—and a “stick”—the individual mandate, which requires all adults to have coverage or pay a fine.

Given these provisions, how sensitive are premiums to the share of young adults enrolled in the Marketplaces? What role do other mechanisms, such as premium tax credits, play in ensuring market stability? How would changes—such as a shift to voucher-type subsidies or eliminating subsidies altogether—affect the enrollment of young adults? To address these questions, RAND researchers used the Comprehensive Assessment of Reform Efforts (COMPARE) microsimulation model to estimate the effect of changes in young adult enrollment on premium prices in the individual market, taking into account the ACA’s buffering mechanisms.

Reduced Enrollment of Young Adults in the Individual Market Translates into Slight Premium Increases

In a baseline scenario for 2015, the RAND COMPARE simulation suggests that 27 percent of enrollees in the individual market would be young adults between ages 18 and 34. If this share were to fall, premiums would rise modestly. The team estimated that a 1 percentage point reduction in the share of young adults is associated with an increase of less than half of 1 percent (Figure 1). The modest effect size is driven partly by the ACA’s tax credits, which create an incentive for some young adults who are eligible for subsidies to remain in the individual market even if other young adults—including a mix of those eligible for subsidies and those not—drop out. In addition, the spending data used as input to COMPARE suggest that, for most enrollees of all ages, premium payments are enough to cover the costs of health care claims, an effect that is boosted by the age rating provisions of the ACA.

This research highlight summarizes RAND Health research reported in the following publication:
Eliminating Tax Credits Would Substantially Reduce Enrollment and Increase Premiums

Eliminating premium tax credits for lower-income enrollees would disrupt the individual market. All enrollees would be required to pay the full cost of premiums. The research team estimated that, if this happened, premiums would rise nearly 45 percent and enrollment would fall by nearly 70 percent (see table). This effect is driven by the fact that higher-risk individuals are likely to sign up for coverage regardless of whether they are eligible for tax credits, whereas lower-risk individuals—including those from the “young invincible” population—often need incentives to sign up. When they do, they improve the risk pool and help contain the price of premiums.

Alternative Types of Subsidies—Such as Vouchers—Could Cause Markets to Become More Sensitive to Age Mix

The analysis also examined the effect of the ACA’s premium tax credits, which cap individual spending on health insurance premiums as a percentage of income, up to the price of the second-least-expensive silver plan in an individual’s rating area. This design protects enrollees against rising premiums because, once an individual’s required contribution is met, any additional premium cost is paid by the federal government. If this design were changed to an alternative structure—such as a voucher for a fixed dollar amount or a fixed percentage contribution—then the individual market would likely become more sensitive to the share of young adult enrollees. For example, if enrollees were given a fixed-dollar voucher to buy insurance, then a 1 percentage point reduction in the share of young adults in the market would be associated with an
increase in premiums of roughly three-quarters of 1 percent (Figure 2). This is true even if we set the initial voucher amounts so that they are equivalent to the premium tax credit amounts predicted by the model at baseline.

**Eliminating the Individual Mandate Would Cause Modest Increases in Premiums but Large Declines in the Number of Insured**

Without the mandate, the overall number of people enrolled in the individual market would fall by nearly 20 percent, from 19.8 to 15.8 million. The number of young adults would decline from 5.4 million (27 percent of those enrolled) to 3.9 million (24.8 percent of those enrolled), and premiums would rise by about 7 percent. The sharp decline in enrollment in this scenario suggests that the individual mandate is important to achieving the ACA’s goal of universal coverage.

**Conclusions**

Many of the mechanisms included in the ACA help provide stability across shifts in the enrollee age mix. In particular, premium tax credits, which encourage participation and guard against financial shocks from rising premiums, play an important role in stabilizing the individual market. Without the ACA’s premium tax credits, the RAND COMPARE model estimates large premium increases and dramatic declines in Marketplace enrollment.
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