California Raises the Bar for Risk-Bearing Entities

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The Knox-Keene Health Care Service Plan Act of 1975 (the "Knox-Keene Act") is the set of laws or statutes passed by the California State Legislature to regulate health care service plans, including health maintenance organizations (HMOs) within the state. The California Department of Managed Health Care (DMHC) adopted a regulation in June 2019 that defines various types of risks that entities assume, including health care providers, and establishes that any entity assuming "global risk" must obtain a Knox-Keene license or receive an exemption. The DMHC established a phase-in period in which entities could apply for and automatically receive an exemption request through June 30, 2020. The deadline was later delayed until December 31, 2020 and subsequently delayed again until a currently unknown effective date of a forthcoming amendment to the DMHC General Licensure Regulation. The DMHC expects the new effective date to be in late 2021 or early 2022. If a DMHC-licensed health plan is a party to the contract, the exemption would apply for the entire term of the contract. If a DMHC-licensed health plan is not a party to the contract, the exemption is valid for the earlier of: 1) two years from the date the DMHC grants the exemption; and 2) the renewal or amendment of the contract.

Background

Recent trends in the healthcare industry are moving towards more healthcare providers taking on risk as well as larger amounts of risk. Specific regulations vary by state and line of business, among other items. Normally, however, healthcare risk is regulated for the health insurer by requiring them to obtain a license, hold a constant minimum amount of capital, and consistently file their financials for review of solvency and anti-competitiveness. Downstream health care providers are not generally held to the same types of regulation and scrutiny. As these risk-sharing arrangements become more widespread throughout the industry and across the nation, regulatory agencies are beginning to impose new rules governing these downstream entities. The DMHC of California is one of the first state agencies to pass this type of regulation on risk-taking entities, and it would not be surprising for other states and agencies to eventually follow suit.

What is the regulation and who does it affect?

This new regulation will require all health care providers that engage in "global risk" arrangements to apply for either a Knox-Keene license or an exemption from the DHMC. According to the DMHC, "global risk" has been defined as accepting a prepaid or periodic charge from or on behalf of enrollees

in return for the assumption of both professional and institutional risk. Professional risk is defined to include the cost of providing licensed professional services to a plan member, while institutional risk means the cost associated with providing hospital services, whether inpatient or outpatient. Providers that assume only professional risk are excluded from the new regulation.

The regulation applies to any contract entered into, amended, or renewed on or after July 1, 2019 by an entity that:

1) Does not have a Knox-Keene Act license, or is not licensed as an insurer by the California Department of Insurance (CDI); and,

2) Assumes any amount of global risk on a pre-paid or periodic basis, including a payment at the end of a contract term.

The regulation applies to contracts that involve only “upside” risk, as well as contracts that involve both “upside” and “downside” risk.

The following types of contracting arrangements do not need to be filed with the DMHC and are exempt from the guidance at this time:

- Bundled Payments
- Case Rates
- Diagnosis-Related Group (DRG) Payments
- Contracts for professional services provided in a hospital emergency department
- Per diem payments pursuant to which the provider (typically a hospital and/or provider group) assumes financial responsibility for providing or arranging for all services associated with an episode of care. In exchange for the bundled payment, the hospital/provider agrees to provide or arrange for all necessary care, including hospital services, professional services, and other attendant medical services, associated with the episode.
- Agreements between a DMHC-licensed health plan and a provider for professional capitation-only where, under the Division of Financial Responsibility (DOFR), the provider assumes financial responsibility for professional services that may be provided in a hospital facility (e.g., radiation therapy, hemodialysis, chemotherapy, amniocentesis, imaging services) but the provider does not share in any savings or losses the hospital may incur.

Entities do not need to submit their contracts pursuant to which they participate in a CMS Accountable Care Organization (ACO). Entities that assume global risk in which all of the consumers impacted by the global risk arrangements are covered by a CDI-licensed insurer are also exempt.

Knox-Keene application process

Entities wishing to obtain a Knox-Keene license will need to apply to the DMHC and provide a wealth of information such as service area, provider lists, provider contracts, organizational charts, quality of care processes, grievance procedures, and other administrative information. Entities must provide financial statements including Tangible Net Equity calculations. Projected financials are also required and must be accompanied by an actuarial report detailing the assumptions and data used for the projection. Lastly, there is an application fee that can range as high as $25,000. After submitting an application, it can take up to 18 months to receive approval.

How do exemptions work?

To be excluded from the license application process, one must submit a collection of financial statements and other necessary information to be considered. This information includes:

- Financial statements related to applicant's viability;
- The total percentage of annualized income of institutional risk the applicant will assume;
- The contract(s) for the assumption of risk;
- The estimated number of subscribers and enrollees;
- The geographic service area under consideration; and
- Any other information the applicant believes to be appropriate or relevant for the Department to consider.

Within 30 days of the request, the DMHC will make a decision based on specific factors. As long as the action of exclusion isn't detrimental to subscribers, enrollees or other persons regulated under the Knox-Keene Act, they are likely to be granted the request.

What is the solution?

If you are interested in applying for a Knox-Keene license, Wakely is fully equipped to assist! Please contact Jackson Hall at Jackson.Hall@wakely.com or Conor Clarkson at Conor.Clarkson@wakely.com with any questions or to follow up on any of the concepts presented here. For more information on the application process, you can also visit https://www.dmhc.ca.gov/licensingreporting/healthplanlicensing.aspx.

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