U.S. House of Representatives

Committee on Oversight and Government Reform

Darrell Issa (CA-49), Chairman

Examining the Administration's $2 billion ObamaCare Loan Guarantee Gamble: Two Case Studies of Political Influence Peddling and Millions of Taxpayer Dollars Wasted

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Executive Summary

The Committee's examination of ObamaCare's Consumer Operated and Oriented Plan (CO-OP) program reveals that the program has jeopardized up to $2 billion in federal taxpayer money. The ongoing oversight has uncovered numerous examples in which companies selected to receive CO-OP loans are plagued with legal and financial issues. The Committee's oversight has also shown that the companies receiving CO-OP loans oftentimes have strong political ties to the Obama Administration. The Committee's findings to date raise troubling questions, not only about the administration of the CO-OP loan program, but also about the effectiveness of ObamaCare implementation in general.

The ObamaCare CO-OP model is similar to the member-owned banking model of a credit union in the private sector. CO-OPs are intended to be nonprofit health insurers funded by their customers that provide care in the individual and small group markets. The key difference, however, is that unlike self-sufficient credit unions, the taxpayers foot the bill for the ObamaCare CO-OPs.

This Committee staff report profiles two organizations who received federal funding through the CO-OP program: the Freelancers Union, which sponsored three CO-OPs in New York, New Jersey, and Oregon; and the Consumer Health Coalition of Vermont. As detailed in this staff, Freelancers Union used its political influence to participate in the program despite being ineligible under the ObamaCare statute. Documents and information provided to the Committee show that Freelancers Union sought to benefit both financially and politically from its involvement in the CO-OP program. This report also presents the case of the Vermont Health CO-OP, which failed to receive the proper state licensure to sell insurance. The licensure denial opinion portrays the Vermont CO-OP as a dangerously insolvent and poorly managed entity.

The shortcomings evident from these two entities raise serious concerns about the overall viability of the CO-OP program. The Committee's ongoing oversight has identified instances in which HHS approved loans for companies with existing insolvency, personnel mismanagement, and legal issues. In addition, the Committee's oversight has uncovered evidence that some companies attempted to influence the Administration to modify program eligibility requirements in the statute. The Committee has discovered communications that demonstrate a politically cozy relationship between company executives and the Obama Administration.

The Committee's initial findings are eerily similar to the findings of the Committee's investigation into the Energy Department's $14.5 billion § 1705 loan program.[1] The recent bankruptcies of Solyndra, Beacon Power, and Abound Solar, which collectively received nearly $1 billion in loan guarantees under the § 1705 program, highlight the problems that occur when the government picks winners and losers. The shortcomings of ObamaCare CO-OPs

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[1] H. Cmte. on Oversight & Gov't Reform, *The Department of Energy's Disastrous Management of Loan Guarantee Programs*, 112th Cong. (2012).

demonstrate HHS's mismanagement of the CO-OP loan awarding process as well as serious deficiencies in the Administration's healthcare reform efforts as a whole.

This staff report presents the Committee's initial findings about the ObamaCare CO-OP program. This report demonstrates how HHS loan commitments through the CO-OP program expose taxpayers to excessive risk as these companies begin to offer coverage through the new health insurance marketplaces. Recognizing these concerns, Congress reduced funding for the program from $6 to $3.8 billion in April 2011. In January 2013, Congress rescinded further program funding, but not before the Department of Health and Human Services had approved $1.98 billion in low-interest CO-OP loans to 24 companies across the country. Because CO-OPs remain operative in the consumer insurance marketplace and billions of taxpayer dollars remain at risk, the Committee continues to receive information from the CO-OPs and will continue to conduct vigorous oversight of the program.

Initial Findings

- HHS's CO-OP loan program received bipartisan criticism from the beginning because the model was virtually untested in the health insurance marketplace and "adverse selection" meant it would be costly to administer. The Department of Health and Human Services therefore took a costly gamble by distributing $2 billion in taxpayer money to companies that were oftentimes hastily assembled and, according to experts, may not be able to attract the right balance of enrollees to keep premiums at reasonable levels.

- The solvency of the CO-OP loan program has been debated from the start. The Office of Management and Budget projects that taxpayers would lose 43 percent of loans offered through the program in its FY 2013 budget statement. In other words, the Administration's own assessment shows that taxpayers stand to lose $860 million from CMS's $2 billion investment into 24 CO-OPs across the country. Independent reviews of company applications conducted by an outside consultant and approved by CMS confirm the concerns that many CO-OPs have significant legal and financial issues.

- Under the plain language of the ObamaCare enacting legislation, Freelancers Union is ineligible to receive CO-OP program funding due to its subsidiary relationship with a for-profit insurance company. Freelancers Union, however, actively lobbied CMS to influence the drafting of regulations to qualify for CO-OP funds as a CO-OP sponsor.

- Freelancers Union sought to benefit financially and politically from its participation in the CO-OP program. Freelancers Union viewed its participation in the CO-OP program as beneficial to its goal of "power in markets" and "power in politics." Freelancers Union received at least $25 million, via its for-profit wholly owned subsidiary, as a result of its participation in the CO-OP program.

- Freelancers Union benefited from a cozy relationship with the Obama Administration. Freelancers Union interacted with White House officials frequently, even successfully appealing to the White House to arbitrate disputes with CMS.

- The Vermont Health CO-OP was not a financially viable business model. The state's Department of Financial Regulation denied the company licensure because its "unrealistic" budget and enrollment projections created a "high likelihood" that the company would become insolvent.

- Oversight from Vermont Health CO-OP's Board of Directors was lacking. The president of the Board had a conflict of interest and received excessive compensation. The Board itself also overly relied on CMS for guidance and oversight.

- The Vermont Health CO-OP actively lobbied Administration and state officials to find a way around the Affordable Care Act's requirements to operate without licensure.

Background: ObamaCare's risky CO-OP program

The provision of health insurance coverage through non-profit cooperatives emerged as the alternative to the "public option" during the debate over health care reform in 2009.[2] Senator Kent Conrad (D-ND) introduced the idea in June 2009 as "an alternative to for-profit insurance companies, so that there's a different delivery model for competition."[3] Health insurance cooperatives were added as a final piece of the Patient Protection and Affordable Care Act, which authorized $six billion in funding to establish non-profit health insurance issuers throughout the country by 2014.[4] The CO-OP concept meant private entities would serve the small and individual insurance markets both on and off of the new health insurance exchange marketplaces.[5]

The Centers for Medicare and Medicaid Services (CMS), a unit of the Department of Health and Human Services, administers two types of loans through the CO-OP program: start-up loans and solvency loans.[6] Start-up loans, repayable in five years, offer funding to assist with start-up activities associated with developing a CO-OP; solvency loans, repayable in 15 years, enable states to meet insurance solvency and reserve requirements.[7] To be eligible for funding, HHS determined that CO-OPs must be not-for-profit entities that meet state licensure requirements and that any applicant would be ineligible "if the organization or a related entity … was a health insurance issuer on July 16, 2009."[8]

The CO-OP loan program is part of the federal government's Direct Loan Program (DLP).[9] While DLP loans are inherently risky, the expected taxpayer loss through the CO-OP program is extraordinarily high. By the Administration's own projections, taxpayers should expect to lose over 40 percent of the amount of loans paid out through the CO-OP program.[10] Although CMS Administrator Marilyn Tavenner assured the Committee that the expected loss is a "loan subsidy rate," not an outright "default rate," she conceded that almost half of the 43.2 percent loss projection is because CO-OP loan interest rates are "below Treasury market rates."[11] This extraordinarily high default right makes the taxpayer-funded CO-OP loans incredibly risky.

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[2] *See, e.g.*, Stuart Butler, *COOP d'etat: An acronym does not a co-op make*, WASH. TIMES, (Sept. 24, 2009), http://www.washingtontimes.com/news/2009/sep/24/coop-detat-an-acronym-does-not-a-co-op-make/?page=1.
[3] Ken Strickland, *A new health-care option?*, NBC News (June 9, 2009), http://firstread.nbcnews.com/_news/2009/06/09/4431391-a-new-health-care-option.
[4] Patient Protection & Affordable Care Act, Pub. L. No. 111-148, 124 Stat. 119 (2010).
[5] *Id.*
[6] Office of Mgmt. & Budget, Exec. Office of the President, Budget of the U.S. Government, Fiscal Year 2013, Federal Credit Supplement, Table 1 (2012) [hereinafter Federal Credit Supplement].
[7] *Id.*
[8] Consumer Operated and Oriented Plan Program, 45 C.F.R. § 156 subpt. F (2011).
[9] Ctr. for Consumer Info. & Ins. Oversight, U.S. Dep't of Health & Human Servs., New Federal Loan Program Helps Nonprofits Create Customer-Driven Health Insurers (2012).
[10] Federal Credit Supplement, *supra* note 6.
[11] Letter from Marilyn Tavenner, then Acting Adm'r, Ctr. for Medicare & Medicaid Servs., to the Hon. Darrell Issa, Chairman, H. Comm. on Oversight & Gov't Reform (Feb. 12, 2013).

Bipartisan concerns about the CO-OP program

There are widespread concerns about the viability of the ObamaCare CO-OP program. Avik Roy, a Senior Fellow at the Manhattan Institute, has explained why the CO-OP program is designed to fail. He wrote:

> [T]he plans are prohibited from using the loans for marketing purposes. So there isn't an easy way for the plans to make consumers aware of them. The plans are prohibited from working with insurers already in operation, hence limiting their ability to gain from the experience of existing market players. The plans will have to enroll members and contract with providers—but unless they are able to enroll a good mix of healthy and sick people, they'll pay out more in claims than they take in premiums: the classic problem of adverse selection. Since healthy people have plenty of options already, it's sick people who will be most likely to sign up for the CO-OP plans.[12]

The CO-OP program received strong bipartisan opposition from its inception. For example, Senator John D. Rockefeller (D-WV) criticized the CO-OP program design in a letter to the Chairman and Ranking Member of the Senate Finance Committee in 2009. Senator Rockefeller wrote: "I believe it is irresponsible to invest over $6 billion in a concept that has not proven to provide quality, affordable health care."[13] Other experts agree. According to Dr. Roger Stark, a physician and health care policy analyst at the non-partisan Washington Policy Center, the CO-OP program is "playing political favorites in handing out the loans, and may be totally illegal in doing so."[14]

Due to these concerns and others, Congress cut funding for the CO-OP program from six billion to $3.8 billion in 2011.[15] The program ultimately dispensed $1.98 billion to 24 companies,[16] before the remainder returned to the general treasury as part of the January 2013 budget deal.[17] The taxpayer dollars already allocated are at considerable risk. A recent study shows that products offered by CO-OPs "are generally higher priced than those offered by more experienced health plans."[18] Adding to these concerns, although some CO-OPs have begun to

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[12] Avik Roy, *Six Solyndras: ObamaCare blows $3 billion on Faulty CO-OP Insurance Loans*, FORBES, May 30, 2012.

[13] Letter from John D. Rockefeller, Chairman, S. Comm. on Commerce, Sci., & Transp., to S. Comm. on Fin. Chairman Max Baucus and S. Comm. on Fin. Ranking Member Charles Grassley (Sept. 16, 2009).

[14] Kenneth Artz, *Obama Administration May Have Used CO-OP Grants to Reward Political Allies*, HEARTLAND INST. (June 29, 2012), http://news.heartland.org/newspaper-article/2012/06/29/obama-administration-may-have-used-co-op-grants-reward-political-allies.

[15] Dep't of Defense and Full-Year Continuing Appropriations Act, 2011, Pub. L. No. 112-10, § XXX, 125 Stat. 38 (2011).

[16] Ctr. for Consumer Info. & Ins. Oversight, *supra* note 9.

[17] Ninety percent of the unobligated balance of funds ($3.4 billion, $2.0 billion obligated) was rescinded as of the date of enactment of the American Taxpayer Relief Act of 2012.

[18] *AIS Survey Data: CO-OPs: Not Necessarily Priced for Competition on Exchanges*, AIS HEALTH WEEK, Nov. 4, 2013, *available at* http://aishealth.com/archive/nref110413-03.

report favorable enrollment, it is not clear that others will be as successful.[19] News reports indicate that the websites of several CO-OPs were "difficult to navigate and provided little understandable insurance information" on October 1 – the date that the ObamaCare exchanges went live.[20]

Deficiencies in HHS's awarding of CO-OP funding

In making award determinations, HHS retained consulting group Deloitte & Touche to review CO-OP loan applications, at an expense of $2.4 million.[21] CMS Administrator Tavenner assured the Committee that the CO-OP application process was "rigorous, objective, and independent to ensure the financial strength and sustainability of CO-OPs."[22] Documents reviewed by the Committee suggest otherwise.

Deloitte performed 113 reviews of applicants through seven funding rounds, scoring applicants on a scale of 100 based on compliance with the program's Funding Opportunity Announcement.[23] Applicants were scored mostly on the quality of their business plans, which included criteria such as qualifications of management and key personnel, budget narrative, and loan funding repayment strategies.[24] Information contained within the Deloitte reports raises serious questions and concerns about CMS's selection process for the CO-OP loan program. Although scores varied widely, CO-OPs that passed these reviews typically received a score of at least 70. Of the companies that passed these reviews as well as an additional review from a Committee within CMS, 24 companies were ultimately selected to receive program funding.[25]

Despite this testing, a review of these reports by Committee staff revealed that HHS funded many CO-OPs with structural, management and solvency issues.[26] Actuarial firm Milliman also conducted financial feasibility studies and business plan analyses for each CO-OP. Notably, Milliman published a study outlining several concerns that the ObamaCare CO-OPs could face, including "overstated assets," "fraud," "inadequate pricing and/or inadequate surplus" and "rapid growth."[27] This study is especially concerning because a survey of 16 CO-OPs conduct by the HHS Inspector General shows that 11 CO-OPs have already exceeded the

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[19] Allison Bell, *CO-OPs Start to Report Enrollment*, BENEFITS PRO (Jan. 14, 2014), http://www.benefitspro.com/2014/01/14/co-ops-start-to-report-enrollment.
[20] Richard Pollock, *Obamacare health insurance co-ops mostly not ready for opening day*, WASH. EXAMINER, Oct. 2, 2013.
[21] Richard Pollock, *ObamaCare co-ops being created behind closed doors*, WASH. EXAMINER, Feb. 5, 2013.
[22] Letter from Marilyn Tavenner, *supra* note 11.
[23] Ctr. for Consumer Info. & Ins. Oversight, U.S. Dep't of Health & Human Servs., *Consumer Operated and Oriented Plan [CO-OP] Program Amended Announcement Invitation to Apply*, Loan Funding Opportunity No.: 00-COO-11-001, CFDA: 93.545 (Dec. 9, 2011).
[24] *Id.* at 41-45.
[25] Letter from Marilyn Tavenner, *supra* note 11.
[26] Committee staff *in camera* review (Apr. 26, 2013).
[27] Troy J. Pritchett & Shelley Moss, *CO-OPs: Learning from History*, CO-OP POINT OF VIEW, Mar. 2012, http://publications.milliman.com/periodicals/co-op-point-of-view/pdfs/co-op-march-2012.pdf.

amount of their startup loans.[28] These independent assessments support the Committee's grave concern about the risk to taxpayer-funded CO-OP loans.

The Committee's oversight efforts

The Committee on Oversight and Government Reform began it's oversight of the CO-OP loan program in October 2012. The Committee initially inquired into the health and solvency of three Freelancers Union CO-OPs and a Nevada-based CO-OP due to concerns that the companies were ineligible to receive funding through the CO-OP program.[29] In late March 2013, the Committee expanded its oversight to examine additional companies.[30] In June 2013, after the Vermont Department of Financial Regulation denied the Vermont Health CO-OP a state health insurance license, the Committee requested information from the Vermont CO-OP.[31] Most recently, the Committee and Senator Coburn (R-OK), the Ranking Member of the Senate Committee on Homeland Security and Governmental Affairs, requested revised enrollment figures from all of the CO-OPs in light of the delayed launch of the Administration's HealthCare.gov website.[32]

During the Committee's oversight, the Committee has written HHS Secretary Kathleen Sebelius three letters requesting information about the CO-OP program.[33] Secretary Sebelius did not respond voluntarily to the Committee's requests. It was only after Chairman Issa issued a subpoena in June 2013 requiring the Department to comply with the Committee's oversight that HHS produced some responsive material.[34]

The information obtained by the Committee highlights many of the Committee's initial concerns about the CO-OP program. The Committee's examination has confirmed concerns about the financial viability of CO-OPs as well as the the qualifications of key executives. Furthermore, the Committee's examination shows that some loan recipients may have unduly influenced the final eligibility criteria and that key employees had close ties with senior Obama Administration officials. Although the full extent of realized losses from the CO-OP program

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[28] Office of Inspector Gen., Dep't of Health and Human Servs., CMS Awarded Consumer Operated and Oriented Plan Program Loans in Accordance with Federal Requirements, and Continued Oversight is Needed, Audit no. A-05-12-00043 (July 30, 2013).
[29] Letter from Reps. Darrell Issa, James Lankford and Jim Jordan, H. Comm. on Oversight & Gov't Reform, to Ms. Sara Horowitz, Freelancers Union & Mr. Thomas Zumtobel, Hospitality Health,(Oct. 2, 2013).
[30] *See, e.g.*, Richard Pollock*, ObamaCare's Solyndra? Oversight panel expands co-ops probe, renews document demand to HHS*, WASH. EXAMINER, Mar. 27, 2013.
[31] Letter from Reps. Darrell Issa, James Lankford and Jim Jordan, H. Comm. on Oversight & Gov't Reform, to Ms. Christine Oliver, CEO, Vt. Health CO-OP (June 18, 2013).
[32] Letters from Reps. Darrell Issa, Trey Gowdy, and Jim Jordan, H. Comm. on Oversight and Gov't Reform, and Sen. Tom Coburn, to 24 CO-OPs (Jan. 15, 2014).
[33] Letter from Reps. Darrell Issa and Trey Gowdy, H. Comm. on Oversight and Gov't Reform, to Kathleen Sebelius, Sec'y, Dep't of Health and Human Servs. (Oct 23, 2013); Letters from Reps. Darrell Issa, James Lankford and Jim Jordan, H. Comm. on Oversight and Gov't Reform, to Kathleen Sebelius, Sec'y, Dep't of Health and Human Servs (March 25, 2013; June, 4, 2013).
[34] SUBPOENA BY AUTHORITY OF THE HOUSE OF REPRESENTATIVES OF THE CONGRESS OF THE UNITED STATES OF AMERICA, to Honorable Kathleen Sebelius, served June 14, 2013.

will not be known for some time, the Committee's oversight into these companies reveals serious problems with the ObamaCare CO-OP program.

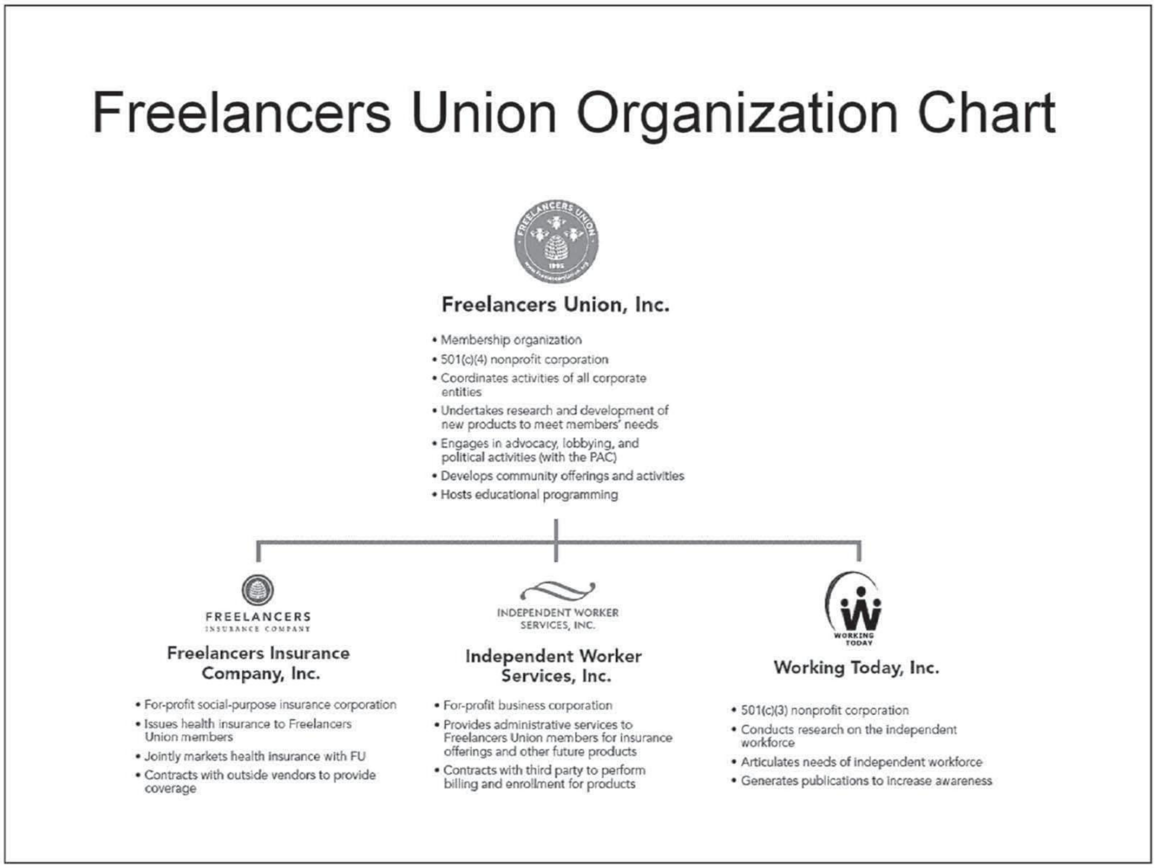
Case Study One: Freelancers Union CO-OPs

Freelancers Union, an association of independent workers headquartered in New York City, sponsored CO-OPs that received the largest three loans. HHS gave Freelancers Health Services Corporation, based in New York; Freelancers CO-OP of New Jersey; and Freelancers CO-OP of Oregon a total of $340 million in CO-OP loans on February 21, 2012.[35] The Committee has substantial reason to question why these three entities received such a substantial federal loan. The Committee's concerns include Freelancers Union's eligibility problems and its lobbying of CMS to participate in the program, Freelancers Union's apparent intention to benefit from the CO-OP program, Freelancers Union's use of political connections to achieve its goal, and serious questions about the solvency of Freelancers Union's CO-OPs.

Freelancers Union did not meet the statutory eligibility requirements for CO-OP funding

Documents and information provided to the Committee show that HHS violated the statute by awarding three loans to CO-OP sponsored by the Freelancers Union. Freelancers Union operates several subsidiaries: Freelancers Insurance Company (FIC), a for-profit insurance corporation providing health insurance to Freelancers Union members; Independent Worker Services (IWS), a for-profit business corporation providing administrative services to Freelancers Union members; and Working Today, a 501(c)(3) nonprofit corporation providing research on the "independent workforce."[36] Because Freelancers Union owns and operates a for-profit insurance provider, it is ineligible for CO-OP funding under the plain language of the statute.

[35] Ctr. for Consumer Info. & Ins. Oversight, *supra* note 9.
[36] Freelancers Union, "Freelancers Union Organization Chart" (transmitted May 17, 2012). [FREE111228-32]



Under Section 1322(c)(2)(a) of the Patient, Protection Affordable Care Act (also known as ObamaCare), entities may not receive direct loans through the CO-OP program if the organization or a *related entity* was a health insurance issuer prior to July 16, 2009.[37] The law further provides that only a non-profit organization may receive loans through the CO-OP program.[38] Facially, therefore, Freelancers is ineligible to participate in the CO-OP program. Freelancers Union has operated a for-profit insurance wholly owned subsidiary, FIC, since 2008.[39] Moreover, according to FIC's website, it is "a for-profit insurance company owned wholly by Freelancers Union."[40]

In response to the Committee's inquiry, counsel for Freelancers Union asserted that FIC is not a "related entity" of the CO-OPs. He asserted that because "no loans will be made by CMS to Freelancers Union" directly, Freelancers Union's ownership of FIC "does not bar the

[37] Patient Protection & Affordable Care Act, Pub. L. No. 111-148, § 1322(c)(2)(a), 124 Stat. 119 (2010).
[38] *Id.*
[39] Freelancers Union, History, http://www.freelancersunion.org/about/history.html (last visited Jan. 29, 2014).
[40] Freelancers Insurance Company, Freelancers Insurance Company to Begin Operating January 1, 2009 (Nov. 24, 2008), https://www.freelancersinsuranceco.com/fic/news/2008/11/.

three CO-OP plans from receiving CMS loans under the CO-OP program."[41] However, information obtained by the Committee reveals that strong, undeniable ties exist between the three CO-OPs, Freelancers Union, and its wholly owned subsidiaries.

The Committee learned during its oversight that Freelancers Union enjoys a close relationship with FIC and its other subsidiary entities. According to a document obtained by the Committee, Freelancers Union exerts considerable control over its subsidiaries, even to the point of "[c]oordinat[ing] activities of all corporate entities."[42] Freelancers Union and its subsidiaries share the same executives and Board members.[43] Sara Horowitz, the chief executive officer of Freelancers Union and its subsidiaries, testified during a transcribed interview that Freelancers Union also shares office space, employees, officers, and resources with its subsidiaries. She testified:

> Q Ms. Horowitz, you mentioned earlier that there were about 70 employees that report either directly or indirectly to you. Are those employees just for Freelancers Union or for Freelancers Union, IWS, Working Today, and FIC?
>
> A Yes, all.
>
> Q So 70 is for all four of those entities?
>
> A Yes.
>
> Q And do they all – do all the employees, are they – do they perform duties solely for one of the organizations, or are they – they all perform duties for different organizations?
>
> A So most are for all, and then there may be some that are, you know, particularly oriented to one thing.
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> Q Ms. Horowitz, the employees, the 70 employees we've discussed, do they share office space?
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> A Yes.

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[41] Letter from Ronald G. Blume, Manatt, Phelps & Phillips, to the Hon. Darrell Issa and Trey Gowdy, H. Comm. on Oversight & Gov't Reform (Nov. 15, 2012).

[42] Dep't of Health and Human Servs., *Patient Protection & Affordable Care Act; Establishment of Consumer Operated and Oriented Plan (CO-OP) Program*, 76 Fed. Reg. 77392-01 (Dec. 13, 2011) (final rule) (to be codified at 45 C.F.R. pt. 156).

[43] H. Comm. on Oversight & Gov't Reform, Transcribed Interview of Sara Horowitz, Freelancers Union, (Nov. 8, 2013) [hereinafter Horowitz Tr.].

Q Do they share office resources?

A What do you mean?

Q Computers, office supplies, that type of thing?

A Yes.[44]

This information makes it clear that Freelancers Union has a unified corporate structure and exerts total control over its subsidiaries. In addition, the Committee also learned that Freelancers Union sponsored the CO-OPs with the expectation that they would execute service contracts with IWS, a for-profit subsidiary of Freelancers Union.[45] An internal document envisions IWS as the central hub of several spokes, including Freelancers Union, FIC, and Freelancers Union-sponsored CO-OPs.[46] This close contractual relationship between the CO-OPs and IWS, which was envisioned when Freelancers Union submitted applications for the CO-OPs,[47] also strongly works against its statutory eligibility to participate in the program.

Under a commonsensical reading of the term, FIC is clearly a "related entity" to Freelancers Union. The entities share a close parent-subsidiary relationship. Freelancers Union coordinates the activities of FIC and the two entities share employees, office space, and office resources. Moreover, the Freelancers Union sponsored the CO-OPs with the intention of having a wholly owned subsidiary provide services to the CO-OPs. Under the plain language of the statute, therefore, Freelancers Union should be ineligible to participate in the CO-OP program because it is "related" to FIC – a for-profit insurance provider that existed prior to July 16, 2009.

Freelancers Union lobbied CMS to issue regulations to allow Freelancers Union to receive CO-OP funding

The Committee's investigation shows that Freelancers Union recognized its eligibility problem and sought a work-around to ensure that the organization would receive CO-OP funding. The lobbying effort was ultimately successful, as the Centers for Medicare and Medicaid Services issued a proposed rule that allowed Freelancers Union to "sponsor" CO-OPs.

Early in the CO-OP program, Freelancers Union recognized that under the plain language of ObamaCare, it was ineligible to participate due to its relationship with FIC. Freelancers Union CEO Sara Horowitz testified:

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[44] Horowitz Tr. at 47.
[45] *Id.*
[46] Freelancers Union, IWS Business Development Plan (June 2012). [FREE 66756- 67]
[47] Horowitz Tr. at 104.

Q Did you have concerns that potentially the law would mean that FIC, or Freelancers Union would be ineligible to sponsor the CO-OPs?

A I thought of it more as again thinking about the larger ACA and what would be all of the different regulations, how they would be interpreted, and it just wasn't clear to me how we would be able to participate.

Q And as a part of that, did you see the possibility that Freelancers Union or FIC would not be able to participate?

A Right, that FIC, I think it was pretty clear that FIC couldn't, and I wasn't sure.

Q Wasn't sure about what?

A Given how we are a Freelancers Union and/or mission, how we would be able to participate in the CO-OP program if at all.

Q Okay. In your opinion, ma'am, are Freelance Insurance Company and Freelancers Union related entities?

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A It's a – it's difficult for me to answer because if you are asking me in the sort of nonlegal sense, like are they related to one another, yes, they are related to one another. I don't know if there is like a legal term of art, and to that I just don't know.[48]

In one e-mail, an independent contractor hired to prepare Freelancers Union's CO-OP applications echoed Horowitz's concerns about Freelancers Union's eligibility, writing: "Here's the part about applicant eligibility that I'm just not sure about (the related insurer not being able to share the same CEO or any board of directors). . . . Though it certainly appears they wrote this section with orgs like Freelancers Union – with related insurance practices – in mind (to allow eligibility)."[49] This concern did not deter Freelancers Union.

Freelancers Union sought to influence the definitions of "related entity" and "sponsor" before HHS issued final regulations to allow these three CO-OPs to qualify for funding. Horowitz began speaking with Barbara Smith, the Associate Director of the CO-OP program at CMS, about the term "related entity." She testified:

Q And have you had occasion to interact with, communicate with HHS officials about the term "related entity"?

[48] *Id.*
[49] E-mail from Joe Kelly to Diallo Powell (July 19, 2011). [FREE023023-4]

A So Freelancers Union, for sure, yes. And so, yes.

Q And does that include you personally having communications or interactions with HHS officials?

A Yes.

Q Which officials?

A During the process in the early stages offering ideas of how we would want the CO-OP to be structured that would help with Freelancers Union and how we wanted to have things done, and that would be to Barbara Smith.[50]

In January 2011, Horowitz sent a letter to Smith detailing her "primary concern regarding Freelancers Union's eligibility to participate in the program, as well as a few solutions that may help overcome that barrier."[51] The attached proposals included various ideas to narrowly define "related entity" so that Freelancers Union's control of FIC would not bar it from participating in the CO-OP program.[52] In the comment to one proposal, Freelancers Union wrote: "This approach is narrow enough to exclude all entities except Freelancers Union, but may be problematic for just that reason."[53] During her transcribed interview, Horowitz testified that she sent the letter because she wanted to find a way for "Freelancers Union to be able to participate in the CO-OP program."[54]

In another e-mail three months later, Ms. Horowitz suggested that "HHS could exclude organizations that are exempt from federal taxation . . . from the definition of related entity. This solution . . . would allow organizations like Freelancers Union to participate in the program."[55] In March 2011, Horowitz formalized her suggestions, writing a letter to the GAO Advisory Board that outlined the issue following a public meeting on March 14.[56] Her lobbying worked. The final CO-OP regulation, issued in December 2011, included language that excluded related organizations such as Freelancers Union and Freelancers Insurance Company from the definition of "related entity."[57]

Freelancers Union continued to lobby CMS throughout the rulemaking process. In an e-mail on June 1, 2011, Melanie Nathanson, Freelancers Union's political consultant in

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[50] Horowitz Tr. at 112.
[51] Letter from Sara Horowitz to Barbara Smith (Jan. 21, 2011). [FREE038414]
[52] Freelancers Union, CO-OP Regulatory Suggestions and Questions. [FREE38415-9]
[53] *Id.*
[54] Horowitz Tr. at 117..
[55] E-mail from Sara Horowitz to Barbara Smith (March 22, 2011) [FREE17837]
[56] Letter from Sara Horowitz to Dr. Allen Freezor, Chair, Federal Advisory Board on CO-OPs (March 14, 2011), *available at* http://www.cms.gov/CCIIO/Resources/Files/Downloads/sara_horowitz_comments_03142011.pdf.
[57] Dep't of Health and Human Servs., *supra* note 42.

Washington, D.C., asked Barbara Smith to meet with Freelancers Union about its CO-OP plans. She wrote:

> I know you are in the middle of rule-making, but I thought it might be helpful to you and your team to hear from Sara and hers on the work they have been doing to get ready for the COOPs. . . . I know you and your team are weighing a variety of different policy options and I thought it might help you to hear what was happening on the ground . . . .[58]

When asked about why she sent this e-mail to Smith, Nathanson testified that the Advisory Board's recommendation emboldened Horowitz to secure Freelancers Union's participation in the CO-OP program. She testified:

> Well, when the advisory board issued its advice, and, you know, it was very clear that a sponsorship notion could be plausible, Sara pulled – got a team together. . . . So she began to do a lot of work in anticipation of potentially sponsoring five CO-OPs. And so we wanted – you know as well as I do, when the administration is in rulemaking they cannot say anything to you, but there is nothing to preclude anyone from coming in and sharing a point of view or sharing learning in the hopes that they will take that into account as they are writing their rules. And that's what this was.[59]

Nathanson testified that the meeting between CMS and Freelancers Union occurred on June 8, 2011.[60] Just a month later, on July 20, 2011, CMS issued the proposed regulation, including language allowing Freelancers Union to sponsor its CO-OPs.[61] The lobbying effort had worked.

Freelancers Union sought to benefit financially and politically from the CO-OP program

The Committee's oversight has revealed substantial evidence that Freelancers Union sought to benefit from its involvement in the ObamaCare CO-OP program. Documents and information suggest that Freelancers Union employees considered the financial and political benefit that would flow to the organization as a result of the CO-OP program. According to one document produced to the Committee, Freelancers Union sought to participate in the CO-OP

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[58] E-mail from Sara Horowitz to Anne Bollinger, Melanie Nathanson, Althea Erickson, (June 1, 2011). [FREE03865-6]
[59] H. Comm. on Oversight & Gov't Reform, Transcribed Interview of Melanie Nathanson, at 53-4 (Nov. 5, 2013).
[60] *Id.*
[61] Dep't of Health and Human Servs., *Patient Protection & Affordable Care Act; Establishment of Consumer Operated and Oriented Plan (CO-OP) Program,* 76 Fed. Reg. 43237-01 (Jul. 20, 2011) (proposed rule).

program to further the organization's "power in markets" and "power in politics."[62] Ultimately, Freelancers Union, via its wholly owned for-profit subsidiary, received millions of dollars of taxpayer funds.

Freelancers Union employees communicated openly about the Union's hope to benefit financially and politically from the CO-OPs. In an exchange on December 11, 2010, Althea Erickson, the Advocacy and Policy Director of Freelancers Union, e-mailed Noah Leff, the Chief Financial Strategist of Freelancers Union, about how to describe Freelancers Union's intended financial relationship with the CO-OPs. She wrote: "Defer to you as to what word you're using to describe moving money from the CO-OPs to FU. I used transfer, but I don't think that's right."[63] In response, Leff wrote: "The word I would use is flow, as in **'profits will flow from the CO-OPs to FU, the parent organization**,' or something like that."[64]

When asked about this e-mail during a transcribed interview, Erickson could not explain the distinction in how Freelancers Union described its financial relationship with the CO-OPs. She testified:

Q When you say, "Defer to you as to what word you're using to describe moving money from CO-OPs to FU," what does "FU" stand for?

A Freelancers Union.

Q And you say, "I used transfer, but I don't think that's right." Why were you struggling to determine what verb to use in that sentence?

A I don't honestly recall. I believe we were working on a document to present to Sara, but, you know, I don't recall.

Q Why did it matter to Sara whether or not you used the word "transfer" versus some other word?

A To be honest, I don't remember.

Q Okay. Maybe Mr. Leff's response will refresh your recollection. He then says, "The word I would use is flow, as in 'profits will flow from the CO-OPs to FU, the parent organization.'" So you have this discussion about whether you want to use the verb "transfer" or "flow." You have no idea why you were having that discussion?

[62] Independent Worker Servs., "IWS Business Development Plan: June 2012," (transmitted June 28, 2012). [FREE66756-67]
[63] E-mail from Althea Erickson to Noah Leff & Andrew Hunter (Dec. 11, 2010). [FREE 53602]
[64] E-mail from Noah Leff to Althea Erickson & Andrew Hunter (Dec. 11, 2010) (emphasis added). [FREE 53602]

A No, besides just using the right word in the right context for language that you're, you know, writing.

Q Sitting here today, with the knowledge you have now, does it seem like it would be important to you as to how to describe that, the relationship between profits from the CO-OPs and the parent organization?

A No. I'm not certain why that conversation happened. And I – this wasn't an external document, it was an internal document.[65]

Freelancers Union also apparently contemplated how it could benefit by using CO-OP funding to perform lobbying activities. In one exchange from December 2010, several Freelancers Union employees discussed how Freelancers Union could perform lobbying with CO-OP money, despite ObamaCare's express prohibition on using CO-OPs funds for that purpose. Andrew Hunter, a senior business analyst for the Union, wrote to Althea Erickson about how Freelancers Union could use CO-OP funds to advocate for Union priorities. He wrote: "We want to be able to use returns from the CO-OPs to advocate for our members in states where they are served now and served in the future. Example: We will push to get colonoscopy legislation passed in New Jersey . . . ."[66]

Erickson replied: "The bill not only prevents the co-ops from using federal $ to lobby, but the 501c(29) requirements prevent CO-OPs from doing any political activity at all, thought I'm not clear if they make a distinction between issue advocacy and 'political' activity. I think we could argue for issue advocacy with HHS."[67] She continued in a later e-mail: "**The more I think about it, the more I think all lobbying should remain in national FU**. Afterall, [*sic*] FIC doesn't lobby, FU does."[68] When asked about using CO-OP money for Freelancers Union priorities, Erickson testified: "That's not clear to me from this e-mail. Again, I don't remember writing it. I think this was more of a conceptual idea, you know, the profits from the CO-OPs helps sort of advance the mission of the overall whole."[69]

The Committee's oversight also shows that Freelancers Union sought to benefit financially from the CO-OP program by having its sponsored CO-OPs contract with Independent Worker Services (IWS), a wholly owned for-profit subsidiary of Freelancers Union. Sara Horowitz explained the CO-OPs' relationship with IWS during her transcribed interview. She testified:

Q At the time that Freelancers Union submitted the applications for CO-OPs, how did the union see the relationship between IWS and the CO-OPs?

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65 H. Comm. on Oversight & Gov't Reform, Transcribed Interview of Althea Erickson, (Oct. 30, 2013) [hereinafter Erickson Tr.].
66 E-mail from Althea Erickson to Andrew Hunter & Noah Leff (Dec. 11, 2010). [FREE 53598]
67 E-mail from Althea Erickson to Andrew Hunter & Noah Leff (Dec. 11, 2010). [FREE 116312]
68 E-mail from Althea Erickson to Andrew Hunter & Noah Leff (Dec. 11, 2010) (emphasis added). [FREE 53598]
69 Erickson Tr. at 80-1.

A The – it was modeled very much on the secondary CO-OPs and the agricultural CO-OPs in America that . . . help to group purchase, and sort of engage in higher level economic activity that bring efficiencies. And so that was the goal and the concept, and what we were hoping was that IWS would be able to do both things like helping to get one enrollment vendor so that the costs would be shared between the three or the technology infrastructure because technology is so expensive, if you could build one thing for three. And so that was one aspect of it. I would say kind of put that into the category of the driving the efficiencies in the business, and then the other was very much trying to make sure, as I spoke earlier about culture, and mission, and that you could have an ecosystem where there would be sort of in the modern way of talking about it like the double bottom line and making sure that the mission was just as important.

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Q I see. And IWS would provide services to each CO-OP?

A Right.

Q Would there be a contractual relationship between IWS and the CO-OPs? How would that work?

A Yes.

Q Between IWS and each CO-OP, or the CO-OPs collectively?

A Each CO-OP collectively. I don't think that – there would be no other way to do it, because they don't have – each three are independent CO-OPs. So, unless they independently formed their own organization, we were negotiating with them.[70]

Documents and information suggest that CMS raised questions about the close relationship between the CO-OPs and IWS. In one e-mail to Rick Koven, the interim CEO of the Freelancers CO-OP of Oregon (FCO), CMS expressed concern about not approving FCO's contract with IWS prior to its execution.[71] CMS prohibited the CO-OP from sending any funds to IWS until it could review the agreement.[72] Meeting notes of a November 2012 meeting between the Oregon CO-OP and IWS similarly reflect that "CMS concerned about: IWS agreement not approved by CMS prior to execution."[73]

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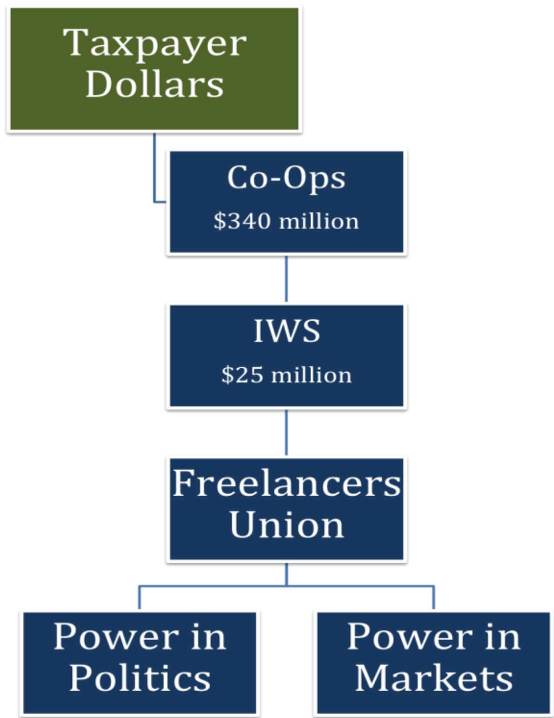
[70] Horowitz Tr. at 123-4.
[71] E-mail from Kevin Kendrick to Rick Koven (Nov. 7, 2012). [FREE 57674]
[72] *Id.*
[73] IWS FCO Meeting Notes (Nov. 9. 2012). [FREE 66410-1]

Freelancers Union, through its wholly owned subsidiary IWS, received a significant amount of taxpayer dollars from the CO-OP program. A memorandum prepared in November 2012 in response to CMS concerns about the Oregon CO-OP's contract with IWS indicated that of the $9 million allocated by CMS to the Freelancers Oregon CO-OP at that time, almost $5 million ended up with IWS.[74] Horowitz testified during her transcribed interview that the "total amount of disbursement between the [Freelancers Union-sponsored] CO-OPS to IWS is $25 million."[75] This acknowledgement confirms that Freelancers Union benefited tremendously – to the tune of $25 million of taxpayer funds – from its successful lobbying to participate in ObamaCare CO-OP program.

Figure 1: Freelancers Union: "Power in Politics" and "Power in Markets"



Freelancers Union benefited from its ties to the Obama Administration

The Committee's investigation also suggests that Freelancers Union used its close ties to the Obama Administration to ensure its participation in the ObamaCare CO-OP program. After CMS expressed reservations about the relationship between IWS and the Freelancers Union's CO-OPs, senior Freelancers Union officials appealed to the White House for its assistance. The Freelancers Union ties were so close to the White House that they closely coordinated with the Administration in response to congressional questions about the organization's CO-OP participation.

[74] Response to CMS Questions on FCO- IWS Agreement (Nov. 21, 2012) .[FREE 58048-5]
[75] Horowitz Tr. at 178.

During the CO-OP rulemaking process, Freelancers Union officials and representatives maintained fairly regular communications with Administration officials about CO-OP program developments. According to publicly available White House visitor logs, Sara Horowitz and Melanie Nathanson met with White House officials more than 30 times from March 2010 to late 2013.[76] In particular, Freelancers Union communicated with Elizabeth Fowler, a special assistant to the President for Health Care and Economic Policy and, according to Horowitz, "the person at the White House who was the most involved in the CO-OP program."[77]

On July 18, 2012, after CMS expressed concerns about Freelancers Union's use of IWS to service the CO-OPs, Horowitz e-mailed Nathanson, writing: "I think this calls for an SOS to Liz fowler and high level friends. They [CMS] will truly fuck with the IWS model – we are already seeing evidence of this. I want to start working on this now- can we set up meetings in dc?"[78] When asked about this e-mail, Horowitz testified that she wanted "to bring [the issue] up with people above Barbara Smith to start talking about it."[79] With respect to her concern about CMS disturbing the "IWS model," Horowitz continued: "I believe that we had a model that we put in our application . . . and we felt that the basic principles of it were being pushed away because there were things that CMS was looking to do that didn't make sense to us."[80]

Committee staff questioned Horowitz about Freelancers Union's need to elevate its concerns about the "IWS model" to the White House for assistance. She testified:

> Q And because you thought CMS was messing with the IWS model, you felt the need to go above them to the White House for assistance?
>
> A Well, to the person who was the point person [at the White House] on the CO-OPs, as well as to people at HHS. You know, I think that that's the right thing to do is when you have an issue, you raise it, you say what your concern is, especially if you want to see something succeed. You know, to me, the perfect way to make something not work is to not raise what your concerns are. And I think you do it in the light of day. You do it transparently, and if you can't do it, I could not call those people I don't have a relationship – Melanie has that relationship. There was no legislation pending. She was just helping us, you know.[81]

Freelancers Union's political connections paid off. Horowitz eventually spoke with Fowler and CMS officials. She described the meeting as "a very good meeting because we got

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[76] *Visitor Access Records*, THE WHITE HOUSE, http://www.whitehouse.gov/briefing-room/disclosures/visitor-records (last visited Feb. 3, 2014).
[77] Horowitz Tr. at XXX; *See also* David Leventhal & Anna Palmer, *PI SCOOP … FOWLER LEAVES WHITE HOUSE FOR JOHNSON & JOHNSON*, POLITICO (Dec. 4, 2012, 2:05 PM), http://www.politico.com/politicoinfluence/1212/politicoinfluence9596.html (last visited Feb. 3, 2014).
[78] *See, e.g.*, E-mail from Richard Swift to Sara Horowitz (July 18, 2012). [FREE114211]
[79] Horowitz Tr. at 206-8.
[80] *Id.*
[81] *Id.*

to kind of clear the air and I think I really got to hear from CMS about what their concerns were."[82]

Freelancers Union continued to utilize Fowler as a high-placed resource. On August 24, 2012, Melanie Nathanson e-mailed Fowler and other Administration officials, writing: "Sara Horowitz is coming to DC to meet with Senator Conrad to discuss the progress that is being made in standing up CO-OPs . . . . Sara is interested in sharing the same information with you that she is giving to Senator Conrad and would love to meet with you all . . . ."[83] After Fowler indicated that she may not make the meeting,[84] Nathanson responded: "Liz, I hate to not have you there. I will make sure you have all of Sara's materials!"[85]

Freelancers Union and the Administration also worked closely to defend the Union from criticism about its eligibility to participate in the CO-OP program. For instance, in February 2012, Freelancers Union's communications manager e-mailed CMS, writing: "I just got off the phone with Ellen in your shop. I wanted to make sure you saw this release from the House Ways and Means committee, attacking the eligibility of Freelancers Union on our coop [*sic*] sponsoring loans."[86] CMS responded by sending talking points about Freelancers Union's eligibility prepared for HHS Secretary Sebelius for an upcoming appearance before the Ways and Means Committee.[87] These talking points detailed how Secretary Sebelius would respond to questions about Freelancers Union's eligibility to participate in the CO-OP program.[88]

It is difficult to assess the precise degree to which Freelancers Union's political connections benefited the organization. Documents and information show a close and consistent relationship that Freelancers Union utilized to its advantage. In this respect, the evidence makes clear that Freelancers Union leveraged its political relationships to ensure that it could participate in the ObamaCare CO-OP program.

Serious questions exist about the viability of Freelancers Union CO-OPs

In addition to the Committee's findings about the manner in which Freelancers Union secured its participation in the CO-OP program, there are several reasons for concern about the fiscal state of Freelancers Union's three CO-OPs. According to recent press reports, Freelancers Union has a record as the "worst" health insurer in the New York state for customer service in

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[82] Horowitz Tr. at 212.
[83] E-mail from Melanie Nathanson to Michael Hash, Elizabeth Fowler, Yvette Fontenot, Chiquita Brooks-LaSure and Barbara Smith, (Aug. 24, 2012). [NH00049]
[84] E-mail from Melanie Nathanson to Elizabeth Fowler, (Aug. 24, 2012). [NH00209]
[85] E-mail from Melanie Nathanson to Richard Popper, (Aug. 24, 2012). [NH00323]
[86] E-mail from Dan Lavoie to Sara Horowitz and Althea Erickson, (Feb. 24, 2012). [FREEE 53588-90]
[87] E-mail from Dan Lavoie to Sara Horowitz and Althea Erickson, (Feb. 24, 2012). [FREEE 53588-89]
[88] *See, e.g.*, H. Comm. on Ways & Means, Obama Administration Continues to Use Health Care Overhaul to Reward Friends (Feb. 21, 2012), http://waysandmeans.house.gov/news/documentquery.aspx?DocumentTypeID=1624.

2011 and 2012 and has had reports of "growing consumer complaints."[89] In addition, Deloitte's independent reviews found several financial and legal concerns about the New York, New Jersey and Oregon CO-OPs. Deloitte noted that IWS "may be overburdened" due to its work with all Freelancer Union-sponsored CO-OPs,[90] and that the CO-OPs need "to perform due diligence . . . over Freelancers Union and IWS."[91] These concerns present serious questions about the long-term viability of the Freelancers Union CO-OPs.

Deloitte noted strong concerns about all three of Freelancers Union's sponsored CO-OPs. For instance, in regard to the New York CO-OP, the consultant noted that the CO-OP's "current [debt] ratio is too high compared to the industry benchmark . . . which may indicate that the applicant is holding too much cash in reserves or that they are over-stating assets."[92] Deloitte also noted that the CO-OP's "reliance on an integrated care model provided and driven by its vendor partners . . . needs . . . detailed plans to perform due diligence over . . . vendors and partners to include Freelancers Union and IWS."[93]

Deloitte noted that the Freelancers Union's New Jersey CO-OP faces competition from "strong . . . long-established" firms and it also predicted that the expenses of the CO-OP would "grow slightly faster . . . than revenues . . . which is a negative indicator of the CO-OP's ability to remain financially solvent in the long-term."[94] Deloitte's review found that Freelancers CO-OP of Oregon's executive team "does not have specific knowledge of the provider and insurance markets in the areas in which it proposes to operate . . . ."[95] Further, the consultant stated that revenue growth is "potentially too aggressive in relation to the applicant's forecasted growth in membership" and that the key weakness with the CO-OP is that they do not "have a strong existing base in Oregon."[96]

In light of these issues raised by Deloitte's independent review, the Committee is concerned about how the CO-OPs will responsibly utilize their taxpayer-funded loans. During her transcribed interview, Sara Horowitz could not provide the Committee with enrollment figures for each of the Freelancers Union-sponsored CO-OPs on November 8, 2013. The Committee has written to each of the three CO-OPs to determine how they are faring in the new ObamaCare exchanges. With millions of taxpayer dollars still at stake in the three CO-OPs

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[89] Richard Pollock, *Consumer complaints swirl around Obamacare's flagship health co-op in New York*, WASH. EXAMINER (Jan. 27, 2014), *available at* http://washingtonexaminer.com/consumer-complaints-swirl-around-obamacares-flagship-health-co-op-in-new-york/article/2542868.
[90] *See* Deloitte Consulting LLP's Freelancers Health Service Corporation's application review, submitted to CMS Jan. 13, 2012.
[91] *See* Deloitte Consulting LLP's Freelancers CO-OP of New Jersey application review, submitted to CMS Jan. 13, 2012.
[92] *See* Deloitte Consulting LLP's Freelancers Health Service Corporation's application review, submitted to CMS Jan. 13, 2012.
[93] *Id.*
[94] *See* Deloitte Consulting LLP's Freelancers CO-OP of New Jersey application review, submitted to CMS Jan. 13, 2012.
[95] *See* Deloitte Consulting LLP's Freelancers CO-OP of Oregon's application review, submitted to CMS Jan. 13, 2012.
[96] *Id.*

sponsored by Freelancers Union, the Committee will continue to closely oversee their health and viability. Unfortunately, none of the Freelancers CO-OPs have responded to the Committee's requests for this information.

Case Study 2: Vermont Health CO-OP

The Vermont Health CO-OP, incorporated as the Consumer Health Coalition of Vermont, received $33.8 million in CO-OP funding from HHS/CMS on June 22, 2012.[97] Three companies with health insurance experience in the state of Vermont – Vermont Managed Care, Inc.; Apex Benefit Services, Inc.; and Fleischer Jacobs Group – were to provide most operational services to the CO-OP.[98] However, the CO-OP never got off the ground. After a thorough eighteen-month review, the Vermont Department of Financial Regulation (DFR) ruled on May 22, 2013, that the CO-OP failed to meet licensure in the state, calling the application itself "fatally flawed."[99]

Following the DFR decision, CMS cut off loan disbursements to the company in May 2013.[100] In a letter dated September 16, 2013, CMS formally informed Vermont Health CO-OP CEO Christine Oliver to "forfeit all unused loan funds" due to "insurmountable obstacles" facing the CO-OP.[101] The decision meant that American taxpayers lost $4.5 million in startup funds for a CO-OP that had been approved by the Administration but that failed to meet even the most basic requirements for state licensure.[102]

Vermont Health CO-OP was unviable and showed "high risk" of insolvency

The Vermont DFR's examination of the Vermont Health CO-OP highlights serious problems with viability of the CO-OP – problems that apparently escaped CMS's review. The DFR found that the company's "liabilities and high proposed rates" would make it "extremely difficult for the CO-OP to remain solvent."[103] Namely, the DFR concluded that the CO-OP's proposed rates for "standard" plans were 15 percent higher, or approximately $73 more a month per plan, than comparable standard plans from competitors.[104] Given that its rates were "significantly less competitive" than initially calculated,[105] the DFR concluded the Vermont Health CO-OP's target enrollment number of 19,645 members in the first year was "unreasonable."[106]

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[97] Ctr. for Consumer Info. & Ins. Oversight, *supra*. note 8.
[98] Consumer Health Coalition of Vermont, Inc., Business Plan, at 7.
[99] State of Vt. Dep't of Fin. Regulation, *In the Matter of: Application by the Proposed Vermont Health CO-OP for a Certificate of Public Good and Certificate of Authority to Commence Business as a Domestic Mutual Insurance Company*, Docket No. 12-041-I (May 22, 2013).
[100] Anne Galloway, *Feds Terminate Loan Agreement with Vermont Health CO-OP*, VT DIGGER, Sept. 16, 2013.
[101] Nancy Remsen, *Vermont Health CO-OP gives up and dissolves*, BURLINGTON FREE PRESS, Sept. 16, 2013.
[102] Bob Kinzel, *Was Vt. Health COOP Undermined by Push for Single Payer?*, VT. PUB. RADIO, Sept. 18, 2013.
[103] State of Vt. Dep't of Fin. Regulation, *supra* note 99, at 12.
[104] *Id.* at 12.
[105] *Id.* at 12.
[106] Id. at 13.

The DFR concluded that the Vermont Health CO-OP would face cumulative losses during its first three years of operation. The CO-OP forecasted that it would lose "approximately $0.8 million cumulatively from 2014-2016," before becoming profitable in 2017.[107] The DFR found otherwise. Carefully examining the CO-OP's unrealistic budget and enrollment projections, the DFR found "a high risk that the CO-OP would be insolvent."[108] The DFR opinion explained:

> [E]ither the CO-OP's rates would be higher than competitors and enrollment would suffer as a result, or the CO-OP's rates would be competitive in the market and insufficient to cover obligations. In either scenario, it is unlikely the CO-OP would remain solvent.[109]

Adding to these concerns, according to the Vermont DFR, the formation of the CO-OP itself was problematic given the state's legal landscape. Specifically, the DFR noted that the formation of the CO-OP conflicts with the state's anticipated implementation of a single-payer system entitled "Green Mountain Care" in 2017, an event that the DFR found would effectively put the CO-OP out of business.[110] Thus, under the particular circumstances of the Vermont insurance industry, the creation of the Vermont Health CO-OP was inherently unviable and ultimately doomed to failure.

The CO-OP suffered from a lack of oversight, conflicts of interest, excessive compensation, and inexperience

The Vermont DFR also identified serious deficiencies in the makeup and actions of the Vermont Health CO-OP's Board of Directors and officers. The DRF decision denying licensure describes serious problems with the key executives' lack of oversight, conflicts of interest, excessive compensation, and inexperience with the health insurance.

According to the Vermont DFR, the Board members left oversight of the CO-OP up to CMS. Several Board members described to the DRF their "very passive role" in overseeing the CO-OP, instead deferring control to CMS, the CO-OP's CEO, and the Board's president.[111] The DFR expressly noted that "the oversight by CMS does not extend to matters of state law . . . and is not a substitute for oversight by the board."[112] Recognizing the risk associated with lax oversight, the DFR noted that the Board's inattention created "an enormous risk" for the standing-up of the Vermont Health CO-OP.[113]

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[107] *Id.* at 13.
[108] *Id.* at 13.
[109] *Id.* at 14.
[110] *Id.* at 26.
[111] *Id.* at 18.
[112] *Id.* at 21.
[113] *Id.* at 22.

In addition, the president of the Vermont Health CO-OP Board created a material conflict of interest that CMS and the CO-OP failed to recognize. Mitchell Fleischer served as the president of the Board and, according to DFR, "ha[d] been a driving force behind the CO-OP's formation and application to [the] DFR."[114] Fleischer simultaneously served as the president of Fleischer Jacobs & Associates, a Vermont-based insurance company.[115] The CO-OP Board allowed the CO-OP to enter into what DFR described as "an illegal no-bid contract" with Fleischer Jacobs "to be the exclusive agent for the CO-OP in soliciting applications for CO-OP products."[116] Although this contract was "reviewed and scrutinized by CMS," the federal agency apparently left this significant conflict of interest unresolved.

The Committee's oversight exposed CMS's failure to appreciate and resolve this significant conflict of interest. In an April 2013 e-mail to the Vermont DFR, Margaret Platzer, the General Counsel of the Vermont Health CO-OP, explained that the Fleischer Jacobs contract "was thoroughly vetted by CMS and their consultants, Deloitte, who had voiced questions related to the potential conflict."[117] In a June 2013 email exchange with Vermont Health CEO Christine Oliver, Robin Fisk, an attorney from Fisk Law office, also revealed that CMS has developed a "tolerance" for "certain conflicts of interest between CO-OPs and vendors…."[118] Ms. Fisk wrote: "I believe that during the loan approval process CMS developed a "tolerance" to certain conflicts of interest between CO-OPs and vendors, probably out of necessity due to the short time for getting the loans done. Obviously the Vt Department of Insurance is using a different standard…."[119] Although CMS appeared willing to ignore this serious problem, the Vermont DRF rightfully identified it as a "stark, ever-present conflict of interest" that "creates insurmountable risk for the CO-OP."[120]

Vermont Health CO-OP leaders also were paid excessively for their services. According to the Vermont DRF, Fleischer's annual salary as president of the CO-OP Board, a staggering $126,000, "eclipsed the salary of the chair of the board of Blue Cross Blue Shield of Vermont, a much larger nonprofit health insurance company, who is paid $28,900 per year."[121] The DFR noted that no evidence exists of discussions by the Board about Fleischer's "surprisingly high salary."[122] "The CO-OP's compensation packages," as found by the DFR, "exhibit a lack of oversight by the board of directors and an outsized influence by the president of the board."[123]

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[114] *Id.* at 18.
[115] According to Fleischer Jacobs' website, Mr. Jacobs has been President and CEO since 1988. *See* Fleischer Jacobs, Staff Directory, http://www.fjgfinancial.com/StaffDirectory/member/MitchFleischer (last visited Feb. 3, 2014).
[116] State of Vt. Dep't of Fin. Regulation, *supra* note 99, at 19.
[117] E-mail from Margaret Platzer to Ryan Chieffo (April 30, 2013). [VCH01455-6]
[118] E-mail from Robin Fisk to Christine Oliver, Margaret Platzer, Mitchell Fleischer (June 3, 2013). [VHC02629]
[119] *Id.*
[120] State of Vt. Dep't of Fin. Regulation, *supra* note 99.
[121] *Id.* at 19.
[122] *Id.* at 19.
[123] *Id.* at 19.

Adding to these concerns, certain Vermont Health executives were not well-qualified for their positions. The DFR found several "weaknesses related to financial responsibility, insurance experience and business qualifications" of the CO-OP's officers and directors.[124] The DFR concluded that key officers of Vermont Health "lack insurance experience and business qualifications commensurate with similar positions in similar entities."[125] Although CEO Christine Oliver had previous experience as a healthcare regulator,[126] the DFR found that she had no experience in operating a health insurance company. Given this inexperience, the DFR predicted that mismanagement could cause "compliance, reputational and financial risks."[127]

Vermont Health CO-OP sought to exert political influence to continue operations despite its licensing failure

Documents and information provided to the Committee indicate that Vermont Health CO-OP officials actively sought to provide insurance coverage without a state license. Section 1322(c)(5) of ObamaCare requires that a CO-OP "must meet all the State standards for licensure" that are required of other issuers.[128] As the Vermont Health CO-OP determined its program eligibility in light of DFR licensure concerns, key CO-OP leaders sought to exercise political influence to benefit the CO-OP.

On November 28, 2012, Fleischer e-mailed Barbara Smith, then associate director of the CO-OP program at CMS, thanking her for meeting with him about their CO-OP's licensure issues and asking if there was "anything else" she could suggest to help the CO-OP with the Vermont DFR.[129] In an e-mail about a month later, CO-OP CEO Oliver addressed the DFR's concerns, explaining that the state regulator had suggested that the CO-OP "prepare to enter the Exchange in 2015 instead of 2014."[130] Oliver commented: "This obviously does not work for us" because the Vermont Health CO-OP was "merely trying to find a path to the Exchange" without receiving licensure first.[131]

The Vermont Health CO-OP also sought to utilize state-level political influence. On December 20, 2012, Oliver wrote about a meeting with Vermont Governor Peter Shumlin, explaining that he had suggestions for how the CO-OP could proceed while their licensure was "pending."[132] On February 12, 2013, Oliver e-mailed Gary Cohen, a senior CMS official, writing: "You may recall that we discussed the potential for you or [CMS] Administrator Tavenner to send a letter to Governor Shulmin recognizing his efforts to stay up to date on the

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[124] *Id.* at 22.
[125] *Id.* at 23.
[126] Andrew Stein, *Vermont Health CO-OP Takes Shape in the Shadow of the ACA Exchange*, VT. DIGGER, Oct. 23, 2013.
[127] State of Vt. Dep't of Fin. Regulation, *supra* note 99, at 24.
[128] Dep't of Health and Human Servs., *supra* note 57.
[129] E-mail from Mitchell Fleischer to Barbara Smith (Nov. 28, 2012). [VHC00748-9]
[130] E-mail from Christine Oliver to Kathleen Scelzo (Dec. 17, 2012). [VHC00843-4]
[131] *Id.*
[132] E-mail from Christine Oliver to Kathleen Scelzo (Dec. 20, 2012). [VHC00854]

Vermont Health CO-OP as we move through the state exchange and licensure processes."[133] Oliver also informed Cohen that "a friend of the CO-OP with a connection to Secretary Sebelius may seek a separate letter from her."[134]

Following the release of DFR's licensure denial, Fleischer pleaded with CMS for leniency. In a May 23, 2013, e-mail, Fleischer wrote: "We have had a chance to review all the information. . . . I wanted you to have a little history because our DOI [Department of Insurance] painted a very unfair picture."[135] During this same time, the CO-OP leaders continued to meet with Governor Shumlin. In a May 28, 2013, e-mail to CMS, Oliver acknowledged having a meeting with the Governor the day before, writing: "He is supportive of CO-OPs generally but his Commissioner advised that we would be insolvent. We were very frank, and so was he. He seemed disappointed that we were not approved…."[136] This considerable political influence proved futile.

The story of the Vermont Health CO-OP is a cautionary tale of how excessive risk, serious conflicts of interest, and inexperience escaped the attention of CMS. If not for the diligent oversight of the Vermont Department of Financial Services, it is entirely possible that American taxpayers could have lost far more than $4.5 million. As a case study of one already-failed CO-OP, the Vermont Health CO-OP raises considerable concerns for the viability of the program in general.

Conclusion

The Committee's preliminary findings about ObamaCare's CO-OP loan program so far tell a story of waste and abuse. Similar to the Committee's concerns about the Department of Energy's §1705 loan program, the Committee has serious concerns about how the Administration chose to award nearly $2 billion in CO-OP funding. The case studies presented in this report paint an unflattering picture for the ObamaCare CO-OP program.

Freelancers Union, the sponsor of three CO-OPs, successfully lobbied the Administration to allow the Union to participate in the program despite its statutory ineligibility. Freelancers Union sought to use its involvement in the CO-OP program to propel its mission of "power in markets" and "power in politics." To this end, $25 million of taxpayer funds loaned to Freelancers Union-sponsored CO-OPs flowed from the CO-OPs to Freelancers Union's wholly owned subsidiary, Independent Workers Services. The fate of the Vermont Health CO-OP also tells a cautionary tale. Due to an unviable business model, mismanagement, poor governance, and conflicts of interest amongst Board members, the company failed to receive licensure to operate its insurance company. American taxpayers are on the hook for $4.5 million in unpaid loans due to bad business decisions and poor oversight by CMS.

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[133] E-mail from Christine Oliver to Gary Cohen (Feb. 12, 2013). [VHC01107]
[134] *Id.*
[135] E-mail from Mitchell Fleischer to Reed Cleary, Kevin Kendrick and Richard Popper, (May 23, 2013). [VHC01495-6]
[136] *Id.*

The Committee is not finished examining the ObamaCare CO-OP program. The Committee continues to review CO-OP information and data. In the weeks and months ahead, the Committee will continue its work to ensure that Congress and the American taxpayers have the requisite information to fully assess the true costs of the ObamaCare CO-OP program.