

Plan Management Navigator

Analytics For Health Plan Administration

September 2005

MEDICAID ADMINISTRATIVE EXPENSE COSTS – LOW AMOUNTS, LOW TREND, REPORTS SHERLOCK COMPANY

Sherlock Company recently published benchmarks for Medicaid plans. For Medicaid HMO, the median per member per month (PMPM) costs were \$17.92, while the Child Buy-in product had median costs of \$14.23 PMPM. Plans reported median PMPM costs of \$19.62 for all products in 2004. In other products, the plans reported costs ranging from \$11.18 for Commercial ASO to \$58.76 for Medicare Advantage.

Expressed as a percent of premiums or equivalents, Medicaid HMO administration was 11.58% for Medicaid HMO and 13.70% for Child Buy-in products. For insured comprehensive products costs ranged from 8.47% for Medicare Advantage to 16.61% for insured POS products. The growth in PMPM administrative costs remained moderate.

This is 2005's third universe of the *Sherlock Expense Evaluation Report (SEER)*, a series of benchmarks of performance metrics for health plans. In-depth financial metrics for each universe are complemented with extensive operational metrics.

This universe is comprised of seven plans focusing on Medicaid managed care products. On average approximately 55.6% of their business was in Medicaid managed care products. Firms committed to this segment tend to be deeply committed to medical management. The plans included in this study serve over 2.1 million people. In aggregate, 41.9% of the members and 59.3% of the revenues are from Medicaid products.

Expenses by Major Functional Category

Figure 1 reports administrative costs by principal functional group for all of the products sold by Medicaid-oriented health plans. These include costs that may not be borne by Medicaid products at all, especially certain marketing costs. (*SEER* itself segments costs by product line but also into many more functional areas.) The total PMPM cost was \$19.62.

Figure 1. Benchmarks for Medicaid Plans' Administrative Expenses
Cost Per Member Per Month - By Function, Total Products

	25th %	75th%	Median	σ /Mean
Marketing	\$1.26	\$5.07	\$4.32	70.24%
Medical/Provider Mgmt.	\$2.89	\$4.42	\$3.85	33.08%
Account/Membership Admin.	\$4.47	\$6.41	\$6.00	32.23%
Corporate Services	\$5.46	\$7.62	\$6.23	29.47%
Total Expenses	\$17.81	\$20.82	\$19.62	13.79%

Marketing expenses included Rating and Underwriting, Product Development / Market Research, Sales and Marketing, Commissions and Advertising and Promotion. These expenses represented \$4.32 of the total administrative costs. At the 75th percentile, these costs were \$5.07 but only \$1.26 at the 25th percentile.

Medical & Provider Management was composed of Provider Network Management and Services and Medical Management (including Quality Assurance and Wellness Programs). These expenses had a median value of \$3.85. At the 75th percentile, these costs were \$4.42, but were as low as \$2.89 at the 25th percentile. By

Dashboard Summary for July

For the trailing three months ended July 31, 2005, the twelve health plans in our Health Plan Dashboard reported revenue growth of 3.0%, with ASO/ASC growth of 34.8% and managed care revenue increased by only 0.0%. Membership declined by 9.3% for managed care but increased by 38.0% in the indemnity business. Managed care and ASO had price increases of 11.3% and 26.1%, respectively, while indemnity posted an increase of 5.7%.

Health benefits ratios overall increased by 0.4 percentage points, but increased by 1.8 and 1.9 percentage points for indemnity and managed care lines. The number of scripts per person increased by 0.2 to 8.9 on an annualized basis. E/R visits decreased by 11.9 to an annual rate of 255.1 per thousand and hospital days per thousand decreased by 1.2 days to 303.2 days per thousand.

Administrative expense to premium increased by 0.2 percentage points to 9.3% - per capita claims volumes increased while inquiries per member decreased. Staffing ratios increased by 0.62 FTEs to 17.5.

Information in our health plan dashboard is segmented by product. It is intended to complement the Sherlock Expense Evaluation Report in its brevity and timeliness. Please contact us regarding ordering information.

contrast, the Blue and Provider-Sponsored universes reported costs of \$2.83 PMPM and \$3.31, PMPM, respectively.

Account & Membership Administration represented \$6.00 per member per month of administrative expenses in 2004. This category of expenses includes many of the core functions of health plans such as Enrollment (including Membership and Billing), Customer Services, Information Systems and Claims (including Encounter Capture and Adjudication). Plans reported \$6.41 at the 75th percentile and \$4.47 at the 25th percentile.

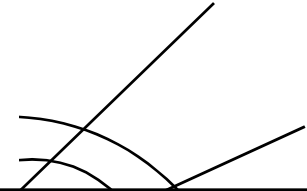
Corporate Services represented the final category. It included investments in HIPAA compliance as well as Finance and Accounting, Actuarial, Corporate Services (including Human Resources, Facilities, Legal and Regulatory, Corporate / Executive and Association Dues and Miscellaneous Business Taxes). These expenses collectively represented \$6.23 in administrative expenses. Fewer than 25% exceeded \$7.62 or were less than \$5.46. These expenses are more susceptible to economies of scale than other groups of functional expenses, in our view.

Expense Growth Exceedingly Moderate

Health plans serving the Medicaid market reported an increase in costs of 0.8% PMPM, excluding miscellaneous business taxes. This is especially impressive considering that last year the plans

reported a decrease in costs of 20.0%. In both cases, we held the universes constant for comparability.

We do not know whether these findings can be generalized across all Medicaid-oriented plans. On one hand, our health plans serve a significant portion of Medicaid beneficiaries, suggesting they may be representative. On the other hand, the health plans in our universe are likely to (a) be especially committed to improving their performance because of the commitment involved, and (b) employ Sherlock Company performance benchmarks to achieve this change. As the head of one association of health plans said to us recently, "You manage what you measure."



Expenses by Product

The products varied in their costs because they have different functional requirements. For instance, as previously noted, medical and provider service costs tend to be relatively high in plans with a significant commitment to pure managed care type products. The analysis of costs by product is included in Figures 2 and 3.

Figure 2. Benchmarks for Medicaid Plans' Administrative Expenses
Cost Per Member Per Month - By Product Line

	25th %	75th%	Median	σ/Mean
Commercial Insured				
HMO	\$21.52	\$31.37	\$25.90	26.62%
POS	\$29.50	\$32.14	\$31.67	9.22%
Indemnity & PPO	\$18.90	\$29.58	\$24.74	32.46%
Commerical ASO	\$9.62	\$12.65	\$11.18	23.68%
Medicare				
Advantage	\$57.04	\$60.49	\$58.76	8.31%
Medicaid				
HMO	\$15.68	\$20.78	\$17.92	32.75%
Child Buy-In	\$12.38	\$16.09	\$14.23	36.89%

Note: Medicare Cost product omitted due to only one respondent.

The Medicaid HMO product typically cost \$17.92 to administer, with 25% of the respondents reporting costs of \$15.68 or less, or \$20.78 or more. The median cost for the Child Buy-In product was \$14.23 PMPM, or \$12.38 at the 25th percentile and \$16.09 at the 75th percentile. Expressed as a percent of revenue the Medicaid HMO operated at 11.58% of premium, and the Child Buy-in product operated at 13.70% of premium.

Figure 3. Benchmarks for Medicaid Plans' Administrative Expenses
Costs as a Percent of Revenue - By Product Line

	25th %	75th %	Median	σ/Mean
Commercial Insured				
HMO	10.48%	15.93%	13.03%	25.63%
POS	14.81%	17.09%	16.61%	15.30%
Indemnity & PPO	9.53%	15.62%	12.71%	31.20%
Commerical ASO	88.75%	107.48%	92.54%	14.39%
Medicare				
Advantage	8.24%	8.69%	8.47%	7.49%
Medicaid				
HMO	8.15%	13.07%	11.58%	26.85%
Child Buy-In	13.04%	14.37%	13.70%	13.72%

Note: Medicare Cost product omitted due to only one respondent.

Among the other insured products, Medicare Advantage had the highest costs at \$58.76 PMPM. The commercial insured products had median values of \$25.90, \$31.67, and \$24.74 in the HMO, POS, and Indemnity / PPO respectively. The commercial ASO product cost \$11.18 PMPM to administer.

Expressed as a percent of revenue, administration also varied by product. Medicare Advantage had the lowest costs at 8.47% of revenue. Among the commercial insured products, POS had the highest costs at 16.61% of revenue, followed by HMO at 13.03% of revenue, and Indemnity & PPO at 12.71% of revenue. The Commercial ASO products sold by these plans have administrative costs of 92.54% of sales.

Medicaid Plans' Administrative Expenses Compared to Other Universes

The Medicaid-oriented plans exhibited lower median administrative costs associated with the Medicaid HMO product than Blue Cross Blue Shield with \$17.92 compared to \$20.27. Similarly, expressed as a percent of premium, these costs were 11.58% as against 11.82%. This advantage was enjoyed despite the fact that Blue Cross Blue

Shield Plans are typically much larger than Medicaid oriented plans. Specialization may play a role in enabling these Medicaid plans to administer the product for less. Advantages to specialization include know how and economies of scale. Put a different way, focused firms reduce the complexity associated with support of multiple products. This, we believe, can be especially troublesome in claims and information systems. Perhaps in recognition of this, we understand that AmeriChoice, the wholly-owned Medicaid business of UnitedHealth Group, operates relatively autonomously.

Background on Performance Benchmarks

Volume I (Financial Metrics) of *Sherlock Expense Evaluation Reports (SEER)* of Medicaid plans contains thousands of analyses of eight principle product areas and more than twenty five functional areas. Products include Medicaid HMO, and Child Buy-In, as well as commercial insured HMO, POS, and Indemnity & PPO. Other products include Commercial ASO, Medicare Advantage and Medicare Cost.

The benchmarks of the Medicaid plans are the third of several Sherlock Company benchmarks for the management of health plan performance issued in 2005. Other universes include Blue Cross Blue Shield, Provider-Sponsored plans, and Larger Plans. In aggregate, plans included in the *SEER* reports serve approximately one in five insured Americans.

In addition to the financial metrics, other performance metrics are included in a companion volume of operational metrics. These metrics include factors affecting functional area costs such as member use of the function, employee productivity, unit cost and staffing ratios. This volume also includes various drivers of such metrics as the extent to which these functions are performed electronically, quality measures, employee compensation analyses, and other function-specific measures. Volume II provides thousands of performance benchmarks on nine key functional areas, including marketing, customer service, claims, enrollment and provider relations. Examples include average cost per inquiry, average speed of answer and the average cost, speed and accuracy of processed claims. An extensive array of medical management and health care cost information is also provided.

SEER reports are the definitive benchmarks for health plan administration. They are critical tools to enhance operational performance and support strategic initiatives ranging from management of the product portfolio, vendor negotiations, outsourcing and business combinations.

