



MEDICAID-ORIENTED PLANS' ADMINISTRATIVE EXPENSE BENCHMARKS AVAILABLE

Summary

Per member administrative cost growth declined from 11.3% in 2006 to 7.2% in 2007. Adjusted to eliminate the effect of changes in plans' product mixes, per member administrative expense growth decreased from 3.9% in 2006 to 3.8% in 2007. Administrative expenses comprised 9.3% of premium equivalents in 2007.

The administrative expenses of Medicaid plans participating in our performance benchmarking study was \$24.30, but varied greatly by product. Excluding marketing, the median total costs were \$19.34.

For their Medicaid products, the median total PMPM costs were \$21.17, or \$18.10 excluding the costs of marketing. By contrast, these plans reported administrative expenses of \$104.75 for Medicare Special Needs Plans (SNPs) and \$19.86 for Child Buy-In products. Results on other products are reflected in the following sections.

Expressed as a percent of premium equivalents, administrative costs for Medicaid products were 9.4%, or 8.2% after excluding marketing. In 2007, the Medicare Special Needs Plans (SNP) administrative expenses were 4.3% of premium equivalents, the lowest such ratio, followed by Commercial ASO at 6.2%. Medicaid Child Buy-In costs, with a median value of \$19.86, had median expenses of 22.6% of premiums. We reflect the results for the other products in subsequent sections.

All values in this article exclude investment and non-operating income and expense, income taxes and miscellaneous business taxes. "Core Expenses" exclude marketing costs as marketing is prohibited for Medicaid products in many states. These results are excerpts from our 2008 *Sherlock Expense Evaluation Report*, comprising 2007 data.

Calculation of Mix Adjusted Rates of Expense Growth

To make useful comparisons between administrative expenses, it is helpful to eliminate the effects of product mix differences. This is helpful both between organizations with different product mixes and also between periods.

Accordingly, in comparing expenses between periods, to make this adjustment by holding constant the product mix between the two years. To do this, since Provider-Sponsored plans report to us by product, we reweight their expenses so that the product mix existing in the prior period is the same as in the current. We then recalculate the rates of change based on these reweighted estimates.

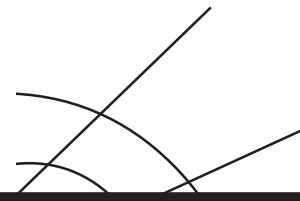
Administrative Costs and Trends

For convenience, we group total administrative expenses into clusters, and standardize for size by expressing expenses on a per member or percent of revenue basis. Values and rates of change for these clusters Medicaid plans and overall are shown in Figures 1 and 2. Appendix A provides values for all plans participating in 2007, and comprises 2006 data.

Medical & Provider Management was composed of Provider Network Management and Services and Medical Management (including Quality Assurance and Wellness Programs). These expenses increased to a median value of \$6.19, up 9.1%. This cluster's cost actually increased by

Figure 1. Medicaid Benchmark Summary
Medicaid Costs by Functional Area Cluster, 2007 Data
Per Member Per Month

	25th PCTL	75th PCTL	Median	σ / Mean
Provider & Medical Management	\$4.73	\$6.70	\$6.19	25.5%
Account & Mem. Administration	7.07	9.34	7.72	30.2%
Corporate Services	1.99	6.20	5.00	87.3%
Subtotal: Core Functions	\$17.25	\$21.40	\$19.34	19.7%
Marketing	1.89	7.16	2.98	80.5%
Total	\$22.10	\$27.39	\$24.30	27.9%



only 0.6% on a constant product mix basis. At the 75th percentile, these costs were \$6.70, but were as low as \$4.73 at the 25th percentile. The expenses for Medical & Provider Management are sensitive to the mix of products that are offered. For example, products such as Medicaid as Medicare Advantage tend to require a higher commitment to this function.

Account & Membership Administration represented \$7.72 per member per month of administrative expenses in 2007, up 15.3% from last year. This category of expenses includes many of the core functions such as Enrollment (including Membership and Billing), Customer Services, Information Systems and Claims (including Encounter Capture and Adjudication). Plans reported \$9.34 at the 75th percentile and \$7.07 at the 25th percentile. The fastest growing area was the Information Systems area, followed by Claim and Encounter Capture and Adjudication expenses.

Holding constant and adjusting for product mix, the Account and Membership Administration cluster increased by 7.9%, up from an increase of 6.4% in 2006. On this adjusted basis, Information Systems costs were still the fastest growing area, but Enrollment Membership and Billing functional area's costs decreased by 10.7%.

Corporate Services included Finance and Accounting, Actuarial, Corporate Services (including Human Resources, Facilities, Legal and Regulatory and Corporate / Executive and Association Dues). These expenses collectively represented \$5.00 PMPM administrative expenses. In 2007, this functional area increased 4.5%, as reported, and increased by 3.9% on a constant product mix basis. Fewer than 25 percent exceeded \$6.20 or were less than \$1.99. These expenses are more susceptible to economies of scale than other groups of functional expenses, based on numerous analyses we have performed over the years.

Core Expenses, that is, total expenses excluding marketing and miscellaneous business taxes, were also calculated. This may facilitate a more ready comparison between the plans, since marketing for Medicaid may not be performed in certain states. The median total expenses excluding marketing and miscellaneous business taxes was \$19.34. The plans' value at the 25th percentile was \$17.25 and at the 75th percentile was \$21.40.

Marketing represented the final expense category. It includes the expenses of Rating and Underwriting, Product Development / Market Research, Sales and Marketing, Commissions and Advertising and Promotion. These expenses represented a median of \$2.98 of the total administrative costs and grew by 6.0% PMPM. (All rates of change hold constant the universe of participants.) At the 75th percentile, these costs were \$7.16, but only \$1.89 at the 25th percentile. On a constant product mix basis, PMPM costs increased by only 3.5% in 2007, compared with 7.3% in 2006.

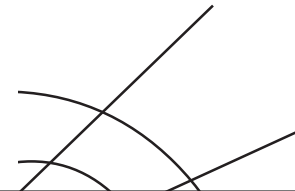
Accounting for Costs as a Percent of Premium Equivalents

Notwithstanding its important drawbacks, health plans and others often express administrative costs as a percent of premiums. As shown in Figure 3, overall, administrative expenses were 9.3% of premium equivalents for comprehensive products sold by Medicaid plans. The 25th percentile value was 8.0% and the value at the 75th percentile was 11.5%. Comparing these results to those in Appendix B, administrative expenses were 0.9 percentage points higher as a percent of premium equivalents.

The value at the 25th percentile for Medical and Provider Services costs was 1.9% of premiums, while the 2.7% of premium equivalents represented the 75th percentile. The

Figure 2. Medicaid Benchmark Summary
 Medicaid Percent Change in Costs by Functional Area Cluster

	2006 Data		2007 Data	
	Percent Change	Percent Change Mix-Adjusted	Percent Change	Percent Change, Mix-Adjusted
Provider & Medical Management	36.1%	23.6%	9.1%	0.6%
Account & Mem. Administration	18.5%	6.4%	15.3%	7.9%
Corporate Services	15.1%	-14.3%	4.5%	3.9%
Subtotal: Core Functions	16.6%	1.8%	8.2%	-6.4%
Marketing	18.3%	7.3%	6.0%	3.5%
Total	11.3%	3.9%	7.2%	3.8%



median value, 2.1%, was 0.1 percentage point higher than the 2.0% posted last year.

The expenses associated with Account and Membership Administration were 3.3% of premium equivalents, 0.5 percentage points higher than last year. The value at the 25th percentile was 2.2% of premium equivalents and 4.1% of premium equivalents at the 75th percentile.

Calculation of Premium Equivalents

Administrative services relationships, comprising nearly one-quarter of commercial members for the plans in the Medicaid universe, play havoc with the intuitive notion that administrative expenses expressed as a percent is a proportion of the premium dollar. That is because such ASO relationships are billed to employers only for the administrative services that they provide, rather than for the cost of care which are borne by the self-insured groups. Since each of the plans submits the health care expenses for the self-insured groups (which they know since they process self-insured claims), by adding this amount to the administrative service fees actually billed, we are able to estimate the premium equivalents of the ASO arrangements.

Note that, as with premiums, fees charged to ASO/ASC clients reflect a profit assumption. Therefore to estimate premium equivalents it is appropriate to add the fees rather than the administrative expenses to estimate premium equivalents in a way that is most directly comparable with the insured business.

The median proportion of premium equivalents due to Corporate Services was 2.2%, 0.1 percentage points more than last year. Twenty five percent of plans had values below 0.4% of premium equivalents or above 2.6% of premium equivalents in 2007.

At the 25th percentile for Core Expenses, costs were 5.3% of premiums, while costs were 9.1% at the 75th percentile. The median value for these expenses were 8.0% of premiums equivalents in 2007, which is 0.9 percentage points higher than last year.

Marketing costs comprised 1.5% of premium equivalents, with the 25th percentile value was 0.8% and the value at the 75th percentile was 1.7%. The comparable median percent in 2006 was 0.6% or 0.8 percentage points higher than for 2007.

Administrative Expenses by Product

All participants in our benchmarking studies segment their costs by product as well as by forty-six functional areas. Overall the resources consumed in these products are reflected in varying administrative expenses that differ quite sharply between the various products. Our participants normally have quite robust activity-based costing systems to facilitate this. For example of how this is done, members in Medicare Advantage products tend to submit more claims than members in Medicaid products so their costs per member are accordingly higher. More directly, ASO products have lower overall costs than their insured counterparts since ASO arrangements are normally sought by larger groups that tend to be less costly to market to.

Medicaid HMO cost \$21.16 PMPM, while Family Buy-In was \$19.86. Child Buy-In had the highest cost among Medicaid products sold by our panel, \$22.25 PMPM.

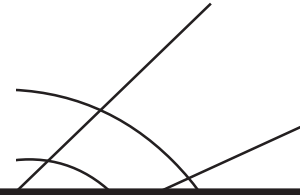
Figure 3. Medicaid Benchmark Summary

Medicaid Costs by Functional Area Cluster, as a Percent Premiums or Equivalents, 2007 Data

Percent of Premium Equivalents

	25th PCTL	75th PCTL	Median	σ / Mean
Provider & Medical Management	1.9%	2.7%	2.1%	28.3%
Account & Mem. Administration	2.2%	4.1%	3.3%	53.6%
Corporate Services	0.4%	2.6%	2.2%	94.6%
Subtotal: Core Functions	5.3%	9.1%	8.0%	42.9%
Marketing	0.8%	1.7%	1.5%	48.2%
Total	8.0%	11.5%	9.3%	28.2%





Treatment of Marketing and Miscellaneous Business Taxes in Metrics

States vary in their regulations with respect to enrollment in private Medicaid health plans. In 2008, according to the Kaiser Family Foundation, four additional states mandated enrollment requirements for Medicaid with seven more states planned for 2009. By contrast, voluntary enrollees have the option to choose an HMO, a primary care case manager (PCCM), or stay in a fee-for-service system. This increasing move to mandatory enrollment has an effect on marketing costs for plans.

Because of these differences, marketing expenses vary from state to state, with some permitting and some severely restricting marketing efforts. Therefore, it is helpful to eliminate marketing from comparisons to facilitate comparability across states.

Miscellaneous business taxes also vary state to state, which diminishes comparability among firms. Because of this, we calculated total expenses less miscellaneous business taxes to help eliminate non-operating differences.

Of the Commercial Insured products, Indemnity & PPO had the highest cost at \$32.83, while POS expenses were \$25.67, the lowest. Commercial HMO cost \$28.43 and Commercial ASO cost \$16.09 in 2007.

Medicare SNP had the highest PMPM administrative costs for products sold by this universe at \$104.75 while Medicare Advantage incurred administrative costs of \$66.74 PMPM.

These adjusted numbers can also be analyzed relative to their premium or equivalents. Expressed as a percent, Medicaid HMO had administrative costs for Medicaid products were 9.4%. The Child Buy-In product had the highest cost with 22.6%, as a percent of premium, while the Family Buy-In was 11.2% of premiums.

Medicare Advantage had a cost of 8.0% of premium equivalents, while Medicare SNP cost 4.3% of premium.

Commercial Insured POS had the lowest administrative expenses as a percent of premiums at 8.9% and Commercial HMO had 9.7% of premiums. Indemnity and PPO Insured and Commercial ASO were 13.3% and 6.2% of premium equivalents, respectively.

Figure 4. Medicaid Benchmark Summary

Medicaid Costs by Product, 2007 Data

Per Member Per Month

	25th PCTL	75th PCTL	Median	σ/ Mean
HMO	\$24.66	\$30.01	\$28.43	25.5%
POS	25.67	25.67	25.67	NM
Indemnity & PPO	29.70	35.96	32.83	27.0%
Total Comm. Ins.	24.66	30.46	26.97	25.8%
ASO	15.62	16.56	16.09	8.3%
Total Commercial	22.66	26.37	24.66	27.8%
Medicare Advantage	52.40	70.33	66.74	31.9%
Medicare SNP	81.21	105.21	104.75	30.7%
Medicare Total	57.44	78.32	76.44	35.5%
Medicaid HMO	17.97	23.47	21.16	30.0%
Medicaid Child Buy-In	16.65	20.87	19.86	24.0%
Medicaid Family Buy-In	19.42	22.57	22.25	16.9%
Medicaid Total	17.70	23.50	21.17	30.3%
Comprehensive Total	\$22.10	\$27.39	\$24.30	27.9%
Medicare Part D	\$28.83	\$36.01	\$32.42	31.3%



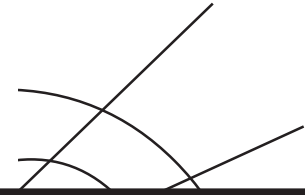


Figure 5. Medicaid Benchmark Summary

Medicaid Costs by Product, 2007 Data

Percent of Premium Equivalents

	25th PCTL	75th PCTL	Median	σ / Mean
HMO	9.0%	10.2%	9.7%	25.2%
POS	8.9%	8.9%	8.9%	NM
Indemnity & PPO	11.4%	15.2%	13.3%	40.7%
Total Comm. Ins.	9.4%	10.6%	9.7%	25.1%
ASO	6.1%	6.3%	6.2%	4.3%
Total Commercial	8.1%	9.7%	9.5%	26.1%
Medicare Advantage	6.1%	8.1%	8.0%	32.6%
Medicare SNP	4.1%	5.9%	4.3%	38.6%
Medicare Total	5.3%	7.1%	6.4%	29.1%
Medicaid HMO	8.1%	12.5%	9.4%	34.1%
Medicaid Child Buy-In	15.9%	24.9%	22.6%	47.3%
Medicaid Family Buy-In	8.0%	12.3%	11.2%	45.2%
Medicaid Total	8.1%	12.5%	9.4%	34.8%
Comprehensive Total	8.0%	11.5%	9.3%	28.2%
Medicare Part D	19.0%	31.8%	25.4%	71.5%

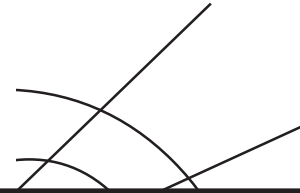
Figure 6. Medicaid Benchmark Summary

Medicaid Characteristics by Universe, 2007 Data

	Medicaid	Indep. / Prov. Sponsored	BCBS	Combined Universes*
Core Costs PMPM				
25th PCTL	\$14.55	\$17.85	\$18.51	\$17.08
Median	17.72	19.80	18.73	18.58
75th PCTL	\$19.30	\$24.96	\$19.83	\$20.18
σ / Mean	49.4%	32.2%	21.6%	27.0%
Core Costs as a Percent of Premiums				
25th PCTL	6.0%	6.4%	8.3%	7.1%
Median	8.2%	7.4%	8.7%	8.9%
75th PCTL	10.1%	10.0%	9.0%	10.1%
σ / Mean	54.4%	40.2%	23.9%	33.9%
Total Costs PMPM				
25th PCTL	\$17.97	\$22.10	\$19.45	\$19.32
Median	21.16	24.65	19.94	22.03
75th PCTL	\$23.47	\$26.95	\$23.68	\$24.91
σ / Mean	30.0%	33.6%	20.9%	23.4%
Total Costs as a Percent of Premiums				
25th PCTL	8.1%	6.9%	8.7%	8.3%
Median	9.4%	9.0%	9.3%	9.5%
75th PCTL	12.5%	11.2%	11.3%	12.4%
σ / Mean	34.1%	51.6%	24.1%	35.1%
Plans Offering Medicaid	8	5	5	16
Medicaid Members	979,997	339,997	498,623	1,666,405
Total Compr. Members	1,672,124	4,009,971	30,742,114	35,770,689

* Two firms included in two universes, are excluded from combined figures.





Other Universes

Because of the demands of our survey process, not all health plans are capable of submitting reliable information for this survey. Since so many of the health plans focused on Medicaid are relatively small, this necessarily leads to a relatively small universe.

On the other hand, a number of Blue Cross Blue Shield Plans and Independent / Provider-Sponsored plans participating in other universes also offer Medicaid. Medicaid membership in these two universes were 498,623 members and 339,997 members, respectively, so that the combined universe of plans for which comparable data is available totals 1,666,405 members.

Recall that each of the universes segments its costs by product, as well as by functional area. We acknowledge that some differences between the different universes, such as scale or the effect of differing products with which Medicaid costs are shared, was not entirely eliminated. Notwithstanding, the results remain remarkably similar across universes. This suggests both the strength of the activity based accounting systems as the dearth of economies of scale.

Background of SEER and Medicaid

Our participation includes 8 Medicaid plans, serving 1.7 million members with comprehensive products. Of the 8 plans, 5 were participants in 2007 and 6, or 75.0%, have three or more years of participation in Sherlock Company benchmarks, contributing to a "practice effect" on the accuracy of data submitted by participants. This is our fifth consecutive annual edition.

Cost comparisons are based on the results for plans that participated in each of the comparison years. PMPM values are actual for all plans the universes. We employed median values throughout this process as the best measure of central tendency.

Overall, our benchmarks in 2008 will comprise the experience of approximately 340 health plan years. We also have universes of Blue Cross Blue Shield Plans, Larger Health Plans, Independent/Provider-Sponsored plans and Medicare Advantage plans. We have completed an analysis of Blue Cross Blue Shield Plans, Provider-Sponsored plans and will be reporting on the Medicare results in the next month or so.

Appendix A. Medicaid Benchmark Summary

Medicaid Costs by Functional Area Cluster, 2006 Data
Per Member Per Month

	25th PCTL	75th PCTL	Median	σ / Mean
Provider & Medical Management	\$4.02	\$6.63	\$5.93	36.6%
Account & Mem. Administration	5.54	8.10	5.76	33.4%
Corporate Services	5.21	6.91	5.77	34.6%
Subtotal: Core Functions	\$15.20	\$20.13	\$18.52	29.2%
Marketing	0.88	3.91	1.20	110.0%
Total	\$16.19	\$27.41	\$20.97	37.7%

Appendix B. Medicaid Benchmark Summary

Medicaid Costs by Functional Area Cluster, as a Percent Premiums or Equivalents, 2006 Data
Percent of Premium Equivalents

	25th PCTL	75th PCTL	Median	σ / Mean
Provider & Medical Management	1.6%	2.6%	2.0%	27.7%
Account & Mem. Administration	2.3%	3.2%	2.8%	30.6%
Corporate Services	1.6%	3.0%	2.1%	41.8%
Subtotal: Core Functions	6.0%	8.7%	7.1%	28.5%
Marketing	0.4%	1.5%	0.6%	83.2%
Total	6.6%	9.9%	8.3%	25.3%