Plan Management Navigator
Analytics for Health Plan Administration

Healthcare Analysts

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Three Models for Health Plan Strategic Planning

The *Sherlock Benchmarks* are frequently used to manage health plan administrative costs. Their granularity helps pinpoint and prioritize cost variances.

In addition, the analyses and values posted on the Sherlock Company website provide useful initial insights for strategic decisions. Drawn from analyses published in the *Plan Management Navigator*, our website contains models that may help your plan answer three questions:

1. How do my health plan's per-member costs compare with the norms of a peer group that resembles my plan and offers a similar product mix?
2. How do economies of scale affect the expenses of each cluster of administrative functions, and how does this compare with the Benchmarks?
3. In the event of a sudden change in membership, what will be the short-term effect on costs?

Benchmark Calculator

This model facilitates comparisons between a health plan's costs and those of its peers. By supplying a plan's product mix and closest health plan industry segment, the model shows an expected PMPM value and the plan's variance from the norm.

For each product the plan offers, enter its membership and select the closest matching universe. Product segmentation is important because per-member costs vary greatly between products. For example, Medicare Advantage costs more than Insured HMO, and commercial insured products cost more than similar ASO products.

To reflect differences in operating styles, you may also select the most appropriate universe for each product. This recognizes that industry segments differ in their strategies, resulting in different expense commitments. For instance, many Independent/Provider–Sponsored plans have a managed care background, giving rise to a high commitment to medical management activities. The values shown in the Benchmark Calculator are derived from *Plan Management Navigators* available on our website.

Economies of Scale

Economies of scale arise from fixed costs within business expense structures, including health plans. Functions such as Information Systems, Finance and Accounting, and Actuarial often have a high proportion of fixed costs.

Economies of scale can be observed in both the long term and the short term:

- **Long-term scale:** measured using a cross-sectional analysis of PMPM health plan costs and membership. Rates of change are not measured.
- **Short-term scale:** measured by calculating rates of change in each plan's membership and expenses. Actual levels of membership and expenses are not measured.

It is often said that all costs are variable in the long term and fixed in the short term. This aphorism is essentially definitional. Since costs are mainly fixed in the short term but more variable in the long term, the slopes of short-term economies of scale tend to be steeper. This implies that sudden short-term changes in membership result in more rapid changes in per-member expenses than long-term differences in membership.

In the following charts, we illustrate this. The regressions show steeper slopes for short-term changes in scale (–1.2846 in Figure 2) compared with long-term differences in scale (–0.1118 in Figure 1)*. In both figures, the dependent variable is the rate of change in per-member Account and Membership Administration expenses, while the independent variable is percent changes in membership. The same 23 plans were used in each analysis, and we excluded no plans from the sets.

Again, the slope of cost changes relative to membership changes is steeper in the short term than in the long term. Because cross-sectional analysis (Figure 1) compares plans of different sizes at a single point in time, it does not measure year-to-year changes. Instead, it expresses scale as rates of change for comparison with short term scale. Expressed in this way, the differences we see across plans of different sizes approximate how a single plan's costs would shift if it achieved scale over many years, during which expenses become variable.

* How we calculated long-term scale for this comparison may be a qualification of this analysis. The long-term scale study is a cross-sectional analysis of per-member costs and membership among participating plans. By contrast, the short-term study is based on rates of change in membership and PMPM expenses between two years. To compare the two, we expressed differences in plan membership and expenses as rates of change, with each plan's values calculated as the percent difference between its membership and expenses relative to the next smallest plan.

Figure 1. Plan Management Navigator
Three Applications For Strategic Planning
Long-Term Scale Change in Membership and Change in PMPM Expenses

$R^2 = 0.0422$
P-Value = 0.3469
Slope =-0.1118

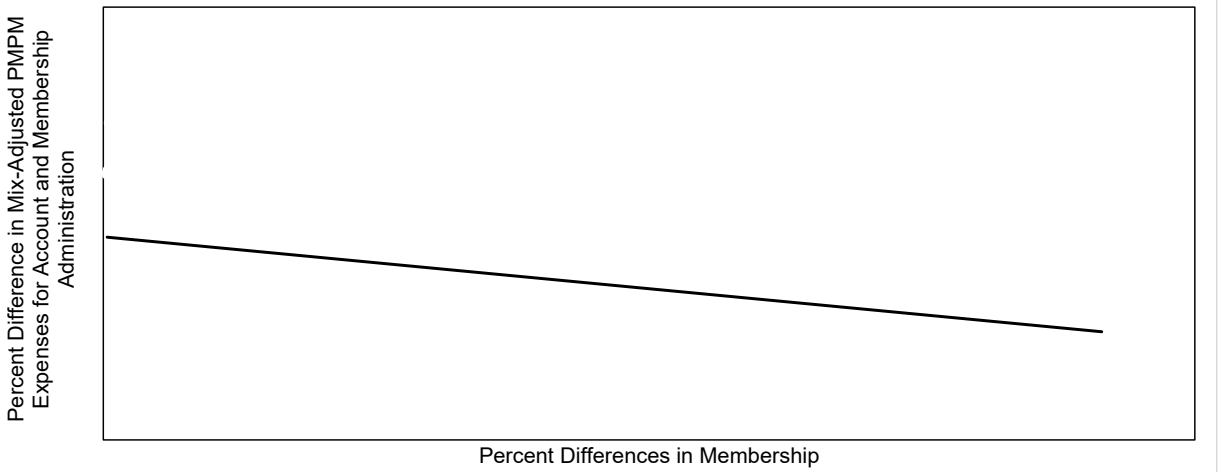
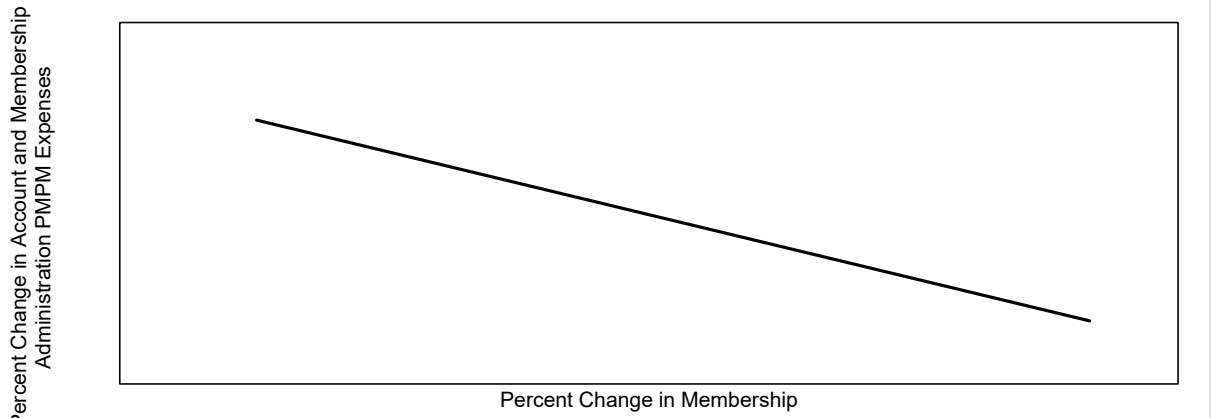


Figure 2. Plan Management Navigator
Three Applications for Strategic Planning
Short-Term Scale: Change in Membership and Change in PMPM Expenses

$R^2 = 0.3234$
P-Value = 0.0046
Slope = -1.2846



Long-Term Scale

This model estimates the effect of economies of scale on each cluster of expenses for health plans. By entering a PMPM cost and a long-term increase in scale (as a percent), new PMPMs are calculated to reflect the difference.

Although only a minority of expenses show statistically significant economies of scale—and the slopes are shallow—larger health plans can still benefit from scale effects in administrative expenses.

Expense estimates may be calculated in total or by clusters of functions: Sales and Marketing, Medical and Provider Management, Account and Membership Administration, and Corporate Services.

The scale slopes are derived from point-in-time, cross-sectional analyses based on cost information from 2024. These slopes are based on results from plans ranging from hundreds of thousands to millions of members, with few having fewer than 100,000 members.

Short-Term Scale

The short-term scale model quantifies the possible effect of changes in a health plan's membership growth rate on its expense growth rate, and thus on PMPM costs.

This model was developed by summarizing a longitudinal study of the relationship between membership growth and administrative expense growth over one year—a period in which costs that may be variable in the long term often behave as fixed. Cost and membership information is from 2023 and 2024.

To apply the modeled relationships to a health plan, supply its PMPM costs, base membership growth rate, baseline PMPM cost growth, and new membership growth. The resulting rates of change derived from the study are then applied to PMPM costs for any of the four clusters of expenses and/or for the total. The clusters are Sales and Marketing, Medical and Provider Management, Account and Membership Administration, and Corporate Services.

Qualifications

We hope these models are helpful. They should be considered alongside other information, including your health plan's unique circumstances. Many of the slopes in the scale studies do not achieve statistical significance. P-values and R^2 values are shown in the Appendices for each model.