

Plan Management Navigator

Analytics for Health Plan Administration



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BLUE CROSS BLUE SHIELD BENCHMARKS: 2013 IS THE BASELINE YEAR

Costs increase by 6.2% due to Information Systems, Commissions and Customer Services

2013 is the Baseline Year

The 2014 Sherlock Benchmarks reflect the first effects of the Affordable Care Act. While no membership had yet enrolled through the state or federal exchanges, Blue Cross Blue Shield plans nevertheless incurred its costs.

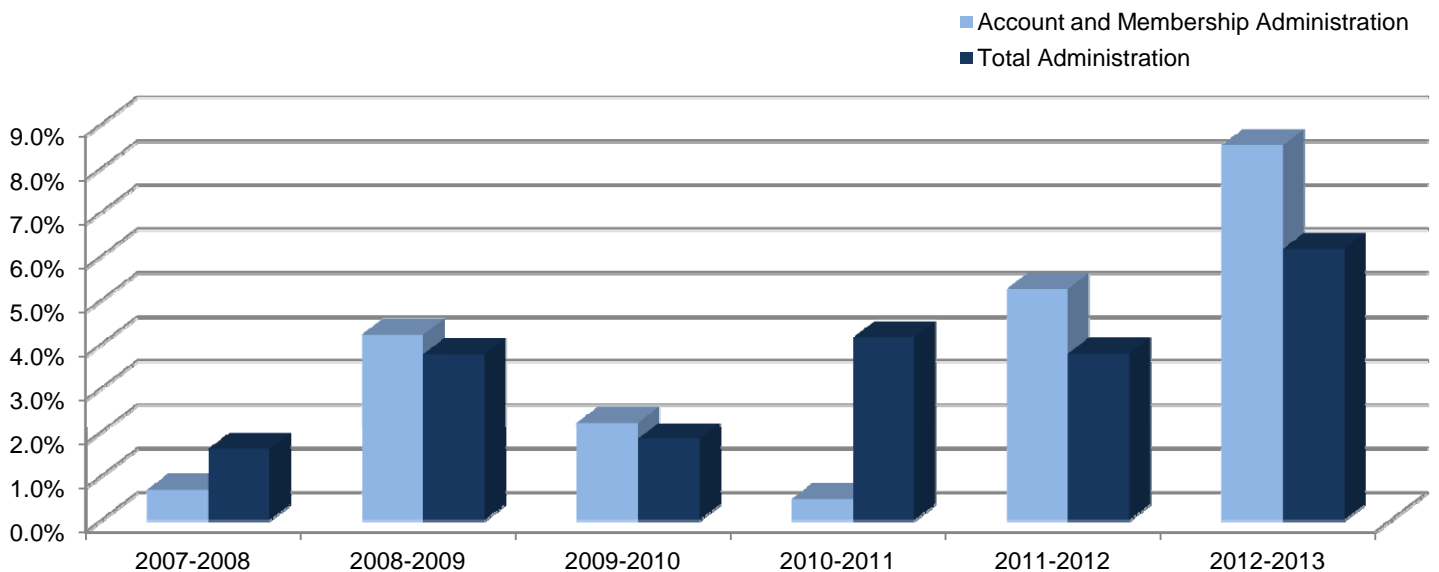
Some of these costs have been characterized by one participating Blue Cross Blue Shield Plan as “bulge” costs. That is, they reflected one-time costs to assist customers in understanding new products sold through exchanges and explain coverage changes to existing customers. Examples of higher costs are found in Customer Services and broker Commissions.

Costs were also higher to develop new products and prepare the infrastructure for the reformed market of the Affordable Care Act. These included increases in Actuarial and Information Systems.

Since these drivers are (hopefully) unique, and cost optimization will inevitably be a priority because of market and ACA-related MLR rules, we think that this year’s results may in the future be viewed as an inflection point. Accordingly, the 2013 results will be considered the baseline costs for health insurers in future comparisons.

The cost increase is readily apparent. Figure 1 shows that the administrative cost

Figure 1. Sherlock Benchmark Summary
Blue Cross Blue Shield Rates of Change for Account and Membership Administration and Total Administration, Constant Mix



trends for Blue Cross Blue Shield participating plans as reflected in the 2014 Sherlock Benchmarking Study. PMPM rates of growth were 6.2% for Total expenses (in dark blue), a sharp increase from recent years.

Account and Membership Administration (in light blue) surged by 8.5%, 60% higher than last year, and double the rate of growth in the next highest year of the six year comparison. The comparisons in Figure 1 should be understood as “real” increases. That is, they eliminate the effect of changes in the product mix such as the continuing growth of highly-demanding Medicare Advantage in the product portfolios of these health plans.

So, what happened?

The 2014 Sherlock Benchmarks of Blue Cross Blue Shield Plans (also called *Sherlock Expense Evaluation Report* or *SEER*) reflect the changes noted above. These increases, reflect PMPM increases and costs stemming from membership whose care and administrative needs changed between the periods. Overall as-reported costs increased by 7.3% up from 5.1% last year. Pharmacy, Mental Health and ICD-10 expenses are included as part of the total in this presentation.

For convenience of analysis, we group various functional areas into clusters, and standardize for the size of the health plans by expressing expenses on a per member basis. Clusters are comprised of functions listed, without subcategories, in Appendix C. All rates of change, including in Figure 1, are calculated using plans that have participated during both comparison years. All values exclude investment and non-operating income and expense, income taxes and miscellaneous business taxes.

Account and Membership Administration soared by 8.9%, the highest in the past six years. This was chiefly due to a surge in Information Systems and Customer Services costs. (Pharmacy, Mental Health and ICD-10 costs are included

Figure 2. Sherlock Benchmark Summary
Blue Cross Blue Shield Median Changes in Per Member Per Month Expenses

Functional Area	2012 Data		2013 Data	
	As Reported	Constant Mix	As Reported	Constant Mix
Sales and Marketing	7.7%	6.9%	8.1%	8.9%
Medical and Provider Managemε	4.2%	3.5%	5.7%	4.5%
Account and Membership Admin	5.0%	5.3%	8.9%	8.5%
Corporate Services	-2.7%	-2.6%	4.2%	4.5%
Total Expenses	5.1%	3.8%	7.3%	6.2%

in the Account and Membership Administration cluster.) They muted the effect of the growth of these expenses, which would have been 9.6% without them.

Sales and Marketing also increased by 8.1%, the fastest rate in the past five years. Advertising costs increased at high double-digit rates. Again, this surge may have been required to educate customers and preserve share in an environment in flux. Continuing a trend from 2012, broker Commission costs also increased; while its increase was the slowest of the Sales and Marketing functions, the magnitude of the cost itself makes it the most important factor in the total increase of the cluster. Internal Sales cost growth, like commissions, was relatively modest. Rating and Underwriting and Marketing cost growth greatly exceeded the cluster's cost trends, possibly related to adaptation to the required new product designs and a shift in favor of Medicare. HCC costs are classified as Rating and Underwriting by our panel. Membership among continuing plans grew at median rate of 1.2%. While most Plans grew, several Plans had sharp declines. Overall, this growth is an improvement over last year's decline in membership and reflects an economy that is slowly recovering. The mix shifted in favor of Insured Indemnity/PPO and Medicare Advantage.

Medical and Provider Management cost trends were higher than last year, 5.7% versus 4.2%, with Provider Network Management and Services having trend above average for the past several years.

Corporate Services costs increased by 4.2% with Corporate Executive and Governance posting a below trend increase in per member costs. Actuarial was sharply higher and the increase in Corporate Services was the most rapid in the past five years.

Setting aside mix, what happened?

In 2013, the average percent of members served by Medicare Advantage products among continuing Plans increased by 0.2 percentage points to 3.0%. Because they were more expensive to serve, the mix change in effect amplified the growth in administrative expenses. Without this and other mix change effects, cost increases would have been the 7.3% mentioned earlier. Accordingly, we consider the mix-adjusted increase, 6.2% in 2013, to be the "real" increase in costs. (We calculate this as the differences between last year's costs weighted by this year's product mix for continuously participating Plans.)

While it is strictly speaking inappropriate to employ median values in doing calculations, dividing the constant mix increase by the as-reported increase implies that the change in business mix was responsible for 1.1 percentage points of the overall PMPM increase. The effect of business mix was especially important in amplifying the reported increases in Rating and Underwriting, Enrollment and Corporate Services.

Again, the total increase was higher than the 3.8% increase last year although, considering the magnitude of the changes in the health care system, this is lower than perhaps could have been anticipated. However, declines in growth in administrative costs for Pharmacy, Mental Health and ICD-10 expenses muted this growth. Without these factors, costs would have increased by 7.7%.

Account and Membership Administration climbed by 8.5% and, like the as-reported results, was the highest in the past six years. Trends were muted by the specialized activities noted above and, excluding them, costs would have increased by 8.9%. Information Systems costs increased at a high double-digit rate, followed by a Customer Service increase at a low double-digit rate. Claims increased by less than 1%, continuing a long-standing trend of modest growth. Enrollment costs increased above its historic pace.

As with the as-reported comparisons, Sales and Marketing also increased, and at 8.9%, it was the fastest rate in the past five years. Advertising costs increased at high double-digit rates, nearly doubling last year's rate of growth. On a constant mix basis, broker Commission costs increased at their fastest rate since 2009. While Rating and Underwriting growth slowed from 2012, it continued faster than the long-term trend. Marketing growth and Sales growth were both similar to last year's paces.

Medical and Provider Management cost trends accelerated over last year, 4.5% versus 3.5%. Provider Network Management and Services was above the long-term trend.

Corporate Services costs increased by 4.5%, higher than last year's decline, and higher than trend in this volatile cluster. Actuarial was much higher at low double-digit rates. While Corporate Executive and Governance posted a small increase in per member costs, the increase was half of recent year trends. Finance and Accounting increased over last year but still grew slower than trend. The Corporate Services function accelerated from 2012, and was above the long-term trend.

Administrative Expenses for Blue Cross Blue Shield Plans were \$30.53

The costs to administer comprehensive products for Blue Cross Blue Shield Plans was \$30.53, 4.3% higher than last year's reported costs of \$29.25. Last year's values are shown in Appendix A. The numbers are not perfectly comparable; while both universes contain 19 plans, three of the Plans turned over, so that 84% of the Plans were the same as last year.

Because of the high comparability, some of the earlier comments are paralleled when the comparing the values of the two universes over the two years. Thus, the sharp constant universe increase in Sales and Marketing compares with the 12% increase to \$8.09 PMPM. Similarly, Account and Membership

costs increased, as did the values for 2013 compared with the values for 2012. The relationships are less close in the other clusters. The moderate growth in Medical and Provider Management compares with the slight decline to \$4.05 PMPM in 2013. The similarly moderate growth in Corporate Services also compares with the slight decline to \$4.44.

Another notable change is the increased clustering of values. The total coefficient of variation is 24% down from 25% last year. This is underscored by the fact that the Corporate Services cluster's coefficient of variation declined 20 percentage points to 31%. The other coefficients of variation declined or remained effectively the same.

Similarly, the differences between the 75th percentile and the 25th percentile values also declined. The difference in these percentiles for Total costs declined by \$0.86. Sales and Marketing fell by \$0.74 and Corporate Services declined by \$0.72. By contrast, Account and Membership Administration increased. It is possible that increased clustering captures increasing adoption of best practices by participating Plans.

Administrative Costs in Each Product Maintained Their Relative Relationships

The Blue Cross Blue Shield Plans that participated in the Sherlock Benchmarking study offered products in 2013 maintained their historic directional cost relationships with one another. Insured products were more expensive than ASO products, Medicaid cost less than commercial insured products and Medicare cost twice the per member costs of the closest Commercial equivalent, Commercial HMO Insured.

But the differences between insured and ASO products expanded sharply. While last year they ranged from \$12-16 PMPM, this year they are in the \$18-19

Figure 3. Sherlock Benchmark Summary
Blue Cross Blue Shield Costs by Functional Area Cluster, 2013 Data
Per Member Per Month

Functional Area	25th Percentile	75th Percentile	Median	Coefficient of Variation
Sales and Marketing	\$7.29	\$10.15	\$8.09	36%
Medical and Provider Management	3.42	4.99	4.05	27%
Account and Membership Administration	11.02	15.60	13.94	25%
Corporate Services	4.03	5.85	4.44	31%
Total Expenses	\$27.44	\$36.14	\$30.53	24%

range. Notably, the increase was due to higher costs for Insured products which in all cases increased more rapidly than for their ASO counterparts. As an example of the change in insured product costs this year, individual product costs were \$46.93 compared with a median cost of \$40.53 in 2012. This seems to be due almost entirely to Information Systems and Sales costs in 2013 that were sharply higher than for 2012, a predictable response to the adaptation requirements of ACA.

Over the long term, this trend could continue. There are said to be pricing, tax and other advantages under the Affordable Care Act that can make self-insurance increasingly attractive to employee benefit plans. Since the groups that are the largest are the ones most able to self-insure, what remains are the smaller groups. Smaller groups have higher per member Sales and Marketing and Enrollment costs than the larger groups that may exit the insured market.

The mix of commercial business that was individual was substantially unchanged, approximately 8%, and the average percent of Commercial Blue Cross Blue Shield members that are served through ASO arrangements remained about the same, about 52%.

Figure 4. Sherlock Benchmark Summary
Blue Cross Blue Shield Costs by Product, 2013 Data
Per Member Per Month

Product	25th Percentile	75th Percentile	Median	Coefficient of Variation
Commercial HMO				
Insured	\$39.57	\$43.63	\$41.69	21%
ASO / ASC	\$20.51	\$29.43	\$22.39	26%
Commercial POS				
Insured	\$30.54	\$39.07	\$37.79	19%
ASO / ASC	\$18.51	\$26.97	\$19.99	36%
Indemnity & PPO				
Insured	\$31.14	\$45.49	\$42.39	27%
ASO / ASC	\$19.37	\$25.79	\$24.38	28%
FEP	\$14.40	\$23.47	\$18.24	35%
Medicare Advantage	\$73.68	\$107.23	\$79.28	26%
Medicaid	\$23.58	\$23.58	\$23.58	NM
Medicare Supplemental	\$23.23	\$34.92	\$32.44	34%
Comprehensive Total	\$27.44	\$36.14	\$30.53	24%
Stand-Alone Medicare Part D	\$13.54	\$19.43	\$17.66	26%
Stand Alone Dental	\$2.42	\$4.18	\$3.26	85%

Administrative Expense for Blue Cross Blue Shield plans was only 8.7% of Premiums

Administrative expenses were 8.7% of premiums in 2013, less than the 8.9% reported last year. This seems to be the result of cost management efforts. Notably, administrative expense to premium ratios declined or were flat in five of the six commercial products. If participation in Sherlock Benchmarking studies is indicative Blue Cross Blue Shield Plan commitment to cost management on the grounds that you manage what you measure, it only makes sense that their administrative expenses grow more slowly than health care costs. Since health care costs dominate the build-up to premium rates, this results in administrative expenses declining as a percent of premiums.

By weighting product cost ratios by 2013 and 2012 product mixes, we ruled a possible alternative explanation, that changing product mix differences were responsible.

Note that ASO/ASC percents are always lower than their insured equivalents, and by 4.6 percentage points in the case of the Plans' dominant Indemnity & PPO product. (We employ our calculations of premiums equivalent [fees plus health

Figure 5. Sherlock Benchmark Summary
Blue Cross Blue Shield Costs by Product, 2013 Data
Percent of Premium Equivalents

Product	25th Percentile	75th Percentile	Median	Coefficient of Variation
Commercial HMO				
Insured	9.1%	11.0%	10.7%	19%
ASO / ASC	6.9%	8.3%	7.4%	29%
Commercial POS				
Insured	8.0%	17.7%	10.3%	76%
ASO / ASC	5.2%	6.2%	5.6%	46%
Indemnity & PPO				
Insured	9.0%	13.7%	11.9%	26%
ASO / ASC	6.3%	8.0%	7.3%	21%
FEP	3.8%	5.6%	4.6%	27%
Medicare Advantage	8.0%	13.1%	10.5%	33%
Medicaid	9.3%	9.3%	9.3%	NM
Medicare Supplemental	13.3%	18.3%	17.1%	28%
Comprehensive Total	7.7%	10.2%	8.7%	18%
Stand-Alone Medicare Part D	10.9%	16.4%	13.7%	39%
Stand Alone Dental	12.1%	19.8%	17.4%	44%

benefits] here.) As noted previously, ASO/ASC costs less to administer because of lower marketing and enrollment costs.

Medicare Advantage has often in the past been a contributor to lower administrative expense to premium ratios but not in recent years for Blue Cross Blue Shield plans. Medicare membership increased at a median rate of 6.1% in 2013 and a mean rate of 14.7% among continuously participating plans.

By the same token, Medicare Supplemental membership fell by 0.5% on average. This product comprised a median share of 4.2% of members, a 0.1 percentage point decline. This product has a very high administrative cost to premium ratio because many of the administrative activities relate to health care costs that are borne by regular Medicare.

The Composition of Expenses also Shifted

As previously noted, administrative expenses fell 0.2 percentage points relative to premiums to 8.7%. (Last year's results are in Appendix B.) Plans' sharp increase in the percent of premiums devoted to Sales and Marketing were more than offset by declines in the percents committed to Medical and Provider Management, Account and Membership Administration and Corporate Services.

This largely comports with the trends discussed earlier. On a constant mix basis, Sales and Marketing costs surged in 2013. The Corporate Services and Medical and Provider Management changes seem to follow from Figure 2 since PMPM growth are below the total in 2013.

More puzzling is the 0.1 percentage point decline in both Account and Membership Administration in the face of the sharp growth of this cluster shown in Figures 1 and 2. It is important to recognize that Figures 6 and Appendix B are snapshots while Figures 1 and 2 shows changes year over year.

Figure 6. Sherlock Benchmark Summary

Blue Cross Blue Shield Costs by Functional Area Cluster, 2013 Data
Percent of Premium Equivalents

Functional Area	25th Percentile	75th Percentile	Median	Coefficient of Variation
Sales and Marketing	1.8%	2.8%	2.4%	37%
Medical and Provider Management	1.0%	1.3%	1.1%	23%
Account and Membership Administration	3.5%	4.5%	3.9%	19%
Corporate Services	1.2%	1.7%	1.3%	26%
Total Expenses	7.7%	10.2%	8.7%	18%

The snapshots contain different health plans whereas the rate of change shows continuing plans. As it happens, each of the three plans that left the panel were replaced by others that had lower ratios to premium equivalents for Account and Membership Administration. Also, several continuous participants posted declines in their ratios.

About the Sherlock Benchmarks and the Blue Cross Blue Shield Universe

These results are excerpted from the Blue Cross Blue Shield edition of the 2014 *Sherlock Expense Evaluation Report*. The results are based on our detailed surveys of 2013 operating parameters of 19 Blue Cross Blue Shield Plans. Accordingly much more information is available by licensing the Sherlock Benchmarks. We hope you will not hesitate to contact us (sherlock@sherlockco.com) if you are interested in licensing these materials or if we can answer any further questions.

Including all of our benchmarks, in each of the 17 years of our analyses, those published in 2014 will comprise the experience of approximately 660 health plan years. We also have universes of Independent / Provider-Sponsored Plans, Larger Health Plans, Medicare Advantage Plans and Medicaid Plans. Later this month, we will publish results on the Independent / Provider-Sponsored Plans and we will be reporting on the results of other universes in the months that follow.

The Blue universe consists of approximately one-half of all primary licensees of U.S. Blue Cross Blue Shield Plans. They represent approximately 60% of the revenues of single state Blue Cross Blue Shield Plans. Plans participating in our benchmarking studies served more than 29 million people with comprehensive insurance, of which approximately 14 million or 83% were commercial. Of the commercial members, 58.2% were served under some form of self-insurance arrangement.

Medicare Advantage, offered by 11 Plans, comprised 3.5% of their total comprehensive membership. In six of the Plans, Medicare Advantage comprised 18% or more their total revenues, and in 9 cases, their Medicare Advantage revenues exceeded their historically important Medicare Supplemental revenues. Combining all of this universe's revenues, those from Medicare Advantage comprised nearly four times that of Medicare Supplemental.

Appendix A. Sherlock Benchmark Summary

Blue Cross Blue Shield Costs by Functional Area Cluster, 2012 Data
Per Member Per Month

Functional Area	25th Percentile	75th Percentile	Median	Coefficient of Variation
Sales and Marketing	\$6.66	\$10.26	\$7.24	38%
Medical and Provider Management	3.57	5.31	4.12	34%
Account and Membership Administration	10.87	14.47	13.39	24%
Corporate Services	3.61	6.16	4.52	51%
Total Expenses	\$26.10	\$35.66	\$29.25	25%

Appendix B. Sherlock Benchmark Summary

Blue Cross Blue Shield Costs by Functional Area Cluster, 2012 Data
Percent of Premium Equivalents

Functional Area	25th Percentile	75th Percentile	Median	Coefficient of Variation
Sales and Marketing	1.8%	3.0%	2.2%	39%
Medical and Provider Management	1.0%	1.4%	1.3%	33%
Account and Membership Administration	3.5%	4.4%	4.0%	20%
Corporate Services	1.2%	2.0%	1.4%	43%
Total Expenses	8.0%	10.6%	8.9%	21%

Appendix C. Sherlock Benchmark Summary

Major Functions Included in Each Administrative Expense Cluster

Sales & Marketing

Rating and Underwriting
Marketing
Sales
Commissions (external)
Advertising and Promotion

Account & Membership Administration

Enrollment / Membership / Billing
Customer Services
Claim and Encounter Capture and Adjudication
Total IS Expenditures (as expensed)

Provider & Medical Management

Provider Network Mgmt and Services
Med. Mgmt / Q.A. / Wellness

Corporate Services

Finance and Accounting
Actuarial
Corporate Services Function
Corporate Executive and Governance
Association Dues and License/Filing Fees