

# Plan Management Navigator

## *Analytics for Health Plan Administration*



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### INDEPENDENT/PROVIDER-SPONSORED ADMINISTRATIVE COST TRENDS: THE FULL IMPACT OF THE AFFORDABLE CARE ACT

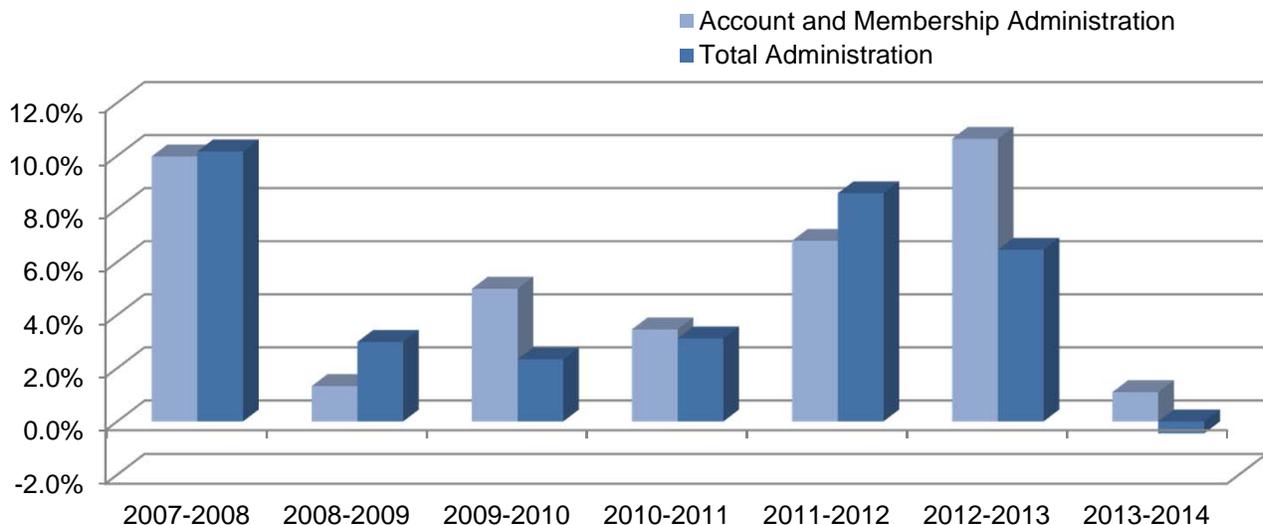
Like Blue Cross Blue Shield Plans, Independent / Provider-Sponsored plans in 2014 were dramatically affected by the first year's effects of the Affordable Care Act. Administrative expenses before Miscellaneous Business Taxes, after eliminating the effect of product mix changes, actually declined at a median rate of 0.4% on a PMPM basis. This is down from an increase of 6.5% in 2013 and is the lowest in at least the last seven years.

Account and Membership Administration was similarly low, declining to 1.1% PMPM growth from 10.6% in the prior year. This rate was the lowest since before 2008.

Every cluster of expenses posted declines in the median rate of growth except Corporate Services, whose growth was effectively flat. Sales and Marketing costs declined, their slowest rate since at least 2009. Medical and Provider Management grew at the slowest rate since 2010. Account and Membership Administration was sharply lower as discussed above.

While the product mix of these organizations changed, the trends overall and by cluster varied by degrees, not direction, even if the effect of mix was not eliminated. Corporate Services, however, accelerated on an as-reported basis. Administrative expenses, excluding Miscellaneous Business Taxes, totaled \$42.14 PMPM.

**Figure 1. Sherlock Benchmark Summary**  
 IPS Rates of Change for Account and Membership Administration and Total Administration, Constant Mix



While not included in the administrative expenses under managerial control that are the central focus of this analysis, Miscellaneous Business Taxes are burdens that must be covered by the premiums and fees charged by health plans. Including the effect of a 922% increase in Miscellaneous Business Taxes, administrative costs overall increased by 11.1%.

### *Miscellaneous Business Taxes*

The explosion in taxes was the result of the first year of taxes associated with the Affordable Care Act. These are the Patient Centered Outcome Research Institute Fees (or Comparative Effectiveness Research Fee), the Transitional Reinsurance Fee, the Risk Adjuster User Fee, the Exchange User Fee and the Annual Fee on Health Insurers.

Continuously reporting plans posted median Miscellaneous Business Taxes of \$4.82 in 2014, equating to approximately \$0.47 PMPM in 2013. This is an increase of approximately \$4.35. That increase in taxes is more than two-thirds the cost of Medical and Provider Management cluster of functions, shown in Figure 3.

Costs varied by product. The median costs for Insured Commercial products was \$9.74. For Commercial ASO, the median value was \$0.02.

### *“Real” Trends*

When we calculate our rates of change, we are careful to include only those plans that participate in both measurement years. Otherwise, we would conflate the effect of the introduction of high or low cost organizations with actual trends.

**Figure 2. Sherlock Benchmark Summary**

Independent / Provider-Sponsored Median Changes in Per Member Per Month Expenses

<b>Functional Area</b>	<b>2013 Data</b>		<b>2014 Data</b>	
	<b>As Reported</b>	<b>Constant Mix</b>	<b>As Reported</b>	<b>Constant Mix</b>
Sales and Marketing	2.8%	4.4%	-3.3%	-3.4%
Medical and Provider Management	7.0%	3.3%	5.4%	2.3%
Account and Membership Administration	7.5%	10.6%	-0.6%	1.1%
Corporate Services	-0.3%	0.6%	1.9%	0.6%
<b>Total Expenses</b>	<b>6.8%</b>	<b>6.5%</b>	<b>-2.3%</b>	<b>-0.4%</b>

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We go one step further when we calculate Constant Mix trends. Since each product offered by a health plan has different costs, a change in product mix can also distort the actual trend in costs. For instance, Medicare Advantage members require more customer inquiries, representatives and costs, so a change in product mix in favor of Medicare Advantage would increase total PMPM costs irrespective of the underlying trends in the inputs.

A more realistic way of looking at cost trends eliminates the effect of the change in product mix. Happily, each of the plans submits all of their costs segmented by product. So it is easy to eliminate this product mix effect - we reweight the continuously participating plan costs so that the prior year's product mix matches that of the current year. Unless noted otherwise, this analysis will focus on the constant mix rates of change.

## **Account and Membership Administration**

Account and Membership Administration growth declined far more than any of the other clusters. Growth decreased from last year's trend of 10.6% to 1.1%, the lowest rate of growth since 2011. This seems to have mainly been powered by a decline in Information Systems growth, from the low double-digit rate to very low single digits. In every year since 2011, these plans' PMPM costs for Information Systems have increased at double-digit rates. Bouncing back from the heavy development in prior years, Application Acquisition and Development costs actually *declined* sharply.

Unlike Blue Cross Blue Shield Plans, Enrollment/Membership/Billing continued the decrease of the prior two years.

The rate of growth in Claims and Encounter Capture and Adjudication also decreased, to low single digits from low double digits in the prior year. However, the growth in COB and Subrogation was especially rapid. In two of the last five years, PMPM costs for the Claims function actually decreased. This may reflect a trend towards automation, though more muted than evident with Blue Cross Blue Shield Plans: While PMPM costs for Claims function costs are 18% higher since 2009, they are 51% higher for Information Systems.

The sole exception to the moderating trend was that Customer Services expenses, which accelerated over 2013 changes. Cost trends were the second highest increase in the past five years. Printed materials costs declined. The Affordable Care Act's effects may well be seen here: since nearly all commercial members had new products, customer inquiries may have required higher levels of staffing.

As-reported results had a similar but not identical pattern. The Enrollment trend was up but Customer Services cost trend was down.

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## Sales and Marketing

Sales and Marketing's costs declined at a median rate 3.4% versus an increase of 4.4% last year. The median rates of increase for most functions in this cluster (which includes Rating and Underwriting, Marketing, Sales, External Broker Commissions and Advertising and Promotion) declined. The exceptions were Commissions and Sales, both of which increased.

The declines in Rating and Underwriting and Advertising and Promotion was in high double-digits for both. The magnitude of both were unprecedented since at least 2003. The increase in Sales and Marketing were both in low single digits. The Marketing cost decline was in low single digits.

Broker Commissions grew in line with historic trends and Sales growth was the second highest over the past five years.

### MIX SHIFT

Membership increased in 2014 versus 2013 at a median rate of 8.3% and a mean rate of 8.0%. Medicaid product growth was particularly robust, increasing at a median rate of 18.0%. Products sold to seniors were also robust with the Medicare products increasing at median rate of 4.8%. This growth was evident in Medicare SNP, Medicare Advantage and Medicare Cost, in that order. Medicare Supplemental grew at a median rate of 3.7%.

By contrast, Commercial increased at a median rate of 2.4%. While ASO increased by 5.5%, commercial insured decreased at a median rate of 2.0%.

While Commercial's share declined (especially the insured share), Medicare was slightly higher and Medicaid increased.

### IMPLICATIONS OF MIX SHIFT

Populations have needs that plans incur costs to respond to. The increased importance of Medicaid and Medicare versus Commercial means that the Medical Management as-reported trend exceeds that of the constant-mix trend.

The Affordable Care Act's role in the Commercial market is highlighted by the fact that while Account and Membership Administration uniquely increased faster in the constant mix comparison, the Customer Service function was the only one that had faster growth on a constant mix basis.

In general, however, Figure 2 shows that cost trends are lower when the effect of the change of mix is eliminated.

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## Medical and Provider Management

This cluster's cost growth declined to the lowest level since at least 2010. Medical and Provider Management costs grew at a median rate 1.1% versus an increase of 10.6% last year.

The growth in Medical Management sharply decreased and, since this function dominates the cluster, this led to an overall reduction in trend. Medical Management cost growth was its lowest since at least before 2010. Disease Management expenses actually declined, year over year. (In our Benchmarks, all medical management costs are included in administrative expenses even if they are classified as Quality Improvement Activities for Medical Loss Ratio calculations.)

By contrast, Provider Network Management and Services growth increased. The focus of the increase appeared to be in Other Provider Network Management and Services. Activities in this function include Provider Audit / Billing Validation and such activities as provider reporting, provider report cards and orientation and on-going education.

As might be expected from the shift away from Commercial, in favor of Medicare and Medicaid, health plan administrative costs for this function grew less rapidly on a constant mix than an as-reported basis.

## Corporate Services

The costs in the cluster of Corporate Services increased by 0.6% PMPM, driven in large part by the 1.2% decline in the Corporate Services function and the 7.1% decline in Actuarial.

The rate of growth in Finance and Accounting declined to low single digits from high double digits in the prior year. Base Finance and Accounting costs declined but Credit Card fees were sharply higher.

The Legal function was substantially unchanged. Notably, Compliance costs were lower. Along with Human Resources and Credit Card Fees, Other Legal was the only sub-function that increased. Imaging and Other Corporate Services costs also trended lower.

## Miscellaneous Business Taxes

As noted previously, the trends for administrative costs within the control of plan managers tended to be very low, matched only in 2006. But their 11.1% growth after inclusion of the Miscellaneous Business Taxes was unprecedented since at least before 2010. The reason for the surge was that Miscellaneous Business Taxes increased by 922%, largely due to the Affordable Care Act.

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This surge in taxes comports with a detailed look at the ACA-related taxes these companies actually paid in 2014. Based on the plans that reported details, these increased costs are overwhelmingly Transitional Reinsurance Fee and the Annual Fee on Health Insurers. Additionally, plans were subject to Exchange User Fee if they had exchange members.

The cost of the Transitional Reinsurance Fee was \$5.27 per commercial insured member per month. The cost of the Annual Fee on Health Insurers (excluding ASO members) was at least 2% of premiums PMPM. Assuming premiums of \$400 PMPM this fee would equal \$8.00 PMPM. The Exchange User Fee was approximately \$7.00 PMPM. Of the plans reporting, a median of 7.7% of Commercial members were in public exchanges. Since these taxes do not apply to all members, a median cost of \$4.99 PMPM was incurred.

### *A Few Outliers*

The plans that participate in Sherlock Benchmarks each operate independently and operate in accordance with their own strategic decisions. Figure 2 shows median changes, and we think that medians are a better representation of the central tendencies because they mute the effect of outliers.

There were some outliers though. (We mean this only in actual performance. We scrub to eliminate the effect of reporting outliers.)

The subcategory of Rating and Underwriting that pertains to everything other than Hierarchical Condition Categories was especially volatile with one of the plans reporting increases of hundreds of percent notwithstanding that 11 of the 16 reported declines.

The Charitable Contribution subcategory was volatile as well. Only 10 of the plans reported and six reported a decline. But one reported an increase of hundreds of percent.

10 of the 16 continuing plans reported declines in Actuarial. But the generally declining trend included organizations with 50% increases and 50% decreases.

Corporate Executive and Governance cost trends were all over the map. This area also includes management consulting services that can be episodic.

The Billing sub-function of Enrollment/ Membership / Billing had a very broad range of increases. The Credit Card Fees also varied quite a bit between the plans.

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## *Administrative Expenses PMPM, by Cluster and in Total*

As noted above, we summarize the administrative costs of Independent / Provider-Sponsored plans into four clusters. In Figure 3, however, costs are reported for all of the plans rather than for the continuing plans.

Overall, administrative expenses excluding Miscellaneous Business Taxes totaled \$42.14 PMPM. The costs were 9.2% higher than reported in 2013, as shown in Appendix A on the last page. This is a far higher increase than either the as-reported or the constant mix growth. Mix likely comprised 2.5 percentage points of this increase, real growth offset 0.4 percentage points, the changes in the universe likely comprised 5.8 percentage points and 1.2 percentage points remain unexplained.

The addition of the five new plans makes it difficult to map relationships between the rates of change of continuing plans, in Figure 2, and the change from Figure 3 and Appendix A. As noted above, the addition of the five new plans appear to have made the universe's costs approximately 5.8% higher than had they included only the sixteen plans from the prior year. Notably, the average participation of the 16 continuously participating plans was 7.2 years, as compared with 4.2 years for the plans that did not. While other causes are also possible, this is consistent with the aphorism that "you manage what you measure."

In order of size, the clusters are Account and Membership Administration, Sales and Marketing, Corporate Services and Medical and Provider Management.

Account and Membership Administration's high cost weight, combined with the precipitous decline in the rate of growth, makes its change especially important to the overall trend. Note that it is larger than Provider Network Management and Services and Corporate Services, combined, and is 40% larger than Sales and Marketing. The costs for this cluster had a median value of \$16.03 PMPM.

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### **Figure 3. Sherlock Benchmark Summary**

Independent / Provider-Sponsored Costs by Functional Area Cluster, 2014 Data

*Per Member Per Month*

<b>Functional Area</b>	<b>25th Percentile</b>	<b>Median</b>	<b>75th Percentile</b>	<b>Coefficient of Variation</b>
Sales and Marketing	\$9.08	\$11.49	\$11.92	34%
Medical and Provider Management	5.34	6.48	8.85	34%
Account and Membership Administration	13.39	16.03	18.77	39%
Corporate Services	5.23	6.70	8.01	31%
<b>Total Expenses</b>	<b>\$33.82</b>	<b>\$42.14</b>	<b>\$45.81</b>	<b>27%</b>

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Sales and Marketing is the second largest cluster of functions. Among continuously participating plans, the costs actually declined and, at \$11.49, the cost increase of 6.4% are lower than the increase in median total costs of 9.2%.

The Corporate Services cluster of functions costs, which had a median value of \$6.70 PMPM, was small compared with most other clusters. They were 8.6% higher than reported for 2013.

Medical and Provider Management costs, the smallest cluster, was only a modest 1.7% higher than reported last year. The median PMPM costs for this cluster was \$6.48.

The values tended to cluster more in 2014 versus 2013. The coefficient of variation fell from 28% in 2013 to 27%. This seems to be largely due to the increased clustering in the Account and Membership Administration cluster of expenses, from 44% last year to 39% in the current year. While Corporate Services also became slightly more clustered both Medical and Provider Management and Sales and Marketing became more disbursed.

### *Costs by Product*

We report health plan administrative costs segmented by products as well as by function. This is important since the products' costs are very different. For instance, the PMPM Sales and Marketing costs for Insured Commercial Products greatly exceed that of their Insured counterparts because the group size is typically much greater. In other words, distribution systems costs are spread over a larger population, explaining why Indemnity and PPO Insured, at \$44.87 PMPM, costs double that of the \$22.03 PMPM for ASO products. Similarly, Medicare Advantage costs, at \$83.60 PMPM tend to be higher than Commercial HMO Insured of \$44.93 since administrative activities are driven in part by the underlying health care cost requirements of the enrolled seniors versus the under 65 population.

Medicare SNP is the most expensive product at \$139.03 PMPM, followed by Medicare Advantage and Medicare Cost, while commercial ASO costs least among comprehensive products. Medicaid products were relatively low cost at close to \$30.00 PMPM.

*To aid readers in the use of this analysis, we have also posted this content in the form of an application on our website: [sherlockco.com/calculator](http://sherlockco.com/calculator). While few organizations actually operate with entirely separate staff and other costs for each product, by using this model, you can actually apply the values in Figure 4 (see next page) to your membership to estimate what your enterprise administrative costs would be if you operated at the median values for each of your products. If you insert your actual administrative costs, the model also provides a PMPM and percent comparison.*

## Costs by Product, in Percent

Administrative expenses comprised 9.2% of premiums for Independent / Provider-Sponsored plans in 2014. While Medicare SNP was the highest cost product on a PMPM basis, it was below average, at 8.9%, compared with all comprehensive products. Medicare Advantage was average, with administrative expenses at 9.2%. (See Figure 5 on next page.)

ASO product costs were low at 6.2%. (We employ “premium equivalents” as the denominator of these products sold to self-insured groups.) All of the Commercial Insured products were more expensive than average by this metric.

Both Medicare Supplemental and Medicare Cost were relatively high cost products at 13.7% and 18.6% median values, respectively. While many of these activities incurred in providing this product were similar to those of other products sold to seniors, the revenue denominator does not include a build-up from all their health benefits – after all, regular Medicare is primary for Medicare Supplemental and beneficiaries of Cost products Part A (Hospital Insurance) services are covered through Original Medicare.

### Figure 4. Sherlock Benchmark Summary

Independent / Provider-Sponsored Costs by Product, 2014 Data

Per Member Per Month

Product	25th Percentile	Median	75th Percentile	Coefficient of Variation
<b>Commercial Insured</b>				
HMO	\$35.08	\$44.93	\$52.06	32%
POS	\$32.86	\$43.93	\$50.67	37%
Indemnity & PPO	\$39.77	\$44.87	\$55.51	29%
Commercial ASO	\$17.99	\$22.03	\$25.80	31%
<b>Medicare</b>				
Advantage	\$70.09	\$83.60	\$110.14	46%
SNP	\$135.81	\$139.03	\$173.64	41%
Cost	\$45.94	\$49.86	\$53.78	22%
<b>Medicaid</b>				
HMO	\$18.90	\$29.57	\$35.74	39%
CHIP	\$16.42	\$29.74	\$41.82	50%
Medicare Supplemental	\$32.35	\$41.66	\$48.55	40%
<b>Comprehensive Total</b>	<b>\$33.82</b>	<b>\$42.14</b>	<b>\$45.81</b>	<b>27%</b>
Stand-Alone Medicare Part D	\$13.47	\$21.83	\$32.42	64%

## *Cluster Costs in Percent, by Cluster and in Total*

Administrative costs comprised 9.2% of the premiums, calculated on a premium equivalent basis. This was lower than the 9.7% reported last year. While Corporate Services increased as a percent of premiums, all other clusters of functions declined or were flat. It appears that the prominence of Medicare products in the growth of these organizations contributed to the decline of the administrative expense ratio. (see Figure 6 on next page)

The order of importance of the clusters was similar to the PMPM medians in Figure 3, with Account and Membership Administration highest and Medical and Provider Management lowest.

The coefficients of variation were, in total and in most clusters, lower than their PMPM counterparts. Our participation is in all regions so it is possible that differences in costs of living between the plans were muted by the percent of premiums approach.

### **Figure 5. Sherlock Benchmark Summary**

Independent / Provider-Sponsored Costs by Product, 2014 Data  
*Percent of Premium Equivalents*

<b>Product</b>	<b>25th Percentile</b>	<b>Median</b>	<b>75th Percentile</b>	<b>Coefficient of Variation</b>
<b>Commercial Insured</b>				
HMO	9.0%	10.6%	12.1%	27%
POS	8.7%	9.1%	11.5%	29%
Indemnity & PPO	11.4%	13.2%	14.4%	23%
<b>Commercial ASO</b>				
	5.1%	6.2%	6.6%	19%
<b>Medicare</b>				
Advantage	7.8%	9.2%	11.9%	51%
SNP	4.6%	8.4%	11.5%	71%
Cost	13.0%	13.7%	14.3%	14%
<b>Medicaid</b>				
HMO	7.8%	8.6%	10.0%	27%
CHIP	11.5%	14.7%	17.5%	40%
<b>Medicare Supplemental</b>				
	17.1%	18.6%	21.0%	51%
<b>Comprehensive Total</b>	<b>8.4%</b>	<b>9.2%</b>	<b>10.5%</b>	<b>21%</b>
<b>Stand-Alone Medicare Part D</b>				
	10.7%	15.0%	20.6%	57%

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## About the Sherlock Benchmarks and the Independent / Provider-Sponsored Universe

These results are excerpted from the Independent / Provider - Sponsored edition of the 2015 *Sherlock Expense Evaluation Report*. The results are based on our detailed surveys of 2014 operating parameters of 21 Independent / Provider-Sponsored plans. Accordingly, much more information is available by licensing the Sherlock Benchmarks. We hope you will not hesitate to contact us ([sherlock@sherlockco.com](mailto:sherlock@sherlockco.com)) if you are interested in licensing these materials or if we can answer any further questions about them or this *Navigator*.

Including all of Sherlock Benchmarks, those published in 2015 will comprise the experience of approximately 700 health plan years. We also have universes of Blue Cross Blue Shield Plans, Larger Health Plans, Medicare Advantage Plans and Medicaid Plans. We will be reporting on the results of other universes in the months that follow.

The 21 Independent / Provider-Sponsored health plans collectively serve 9.5 million members with comprehensive products. They also served 110,000 under stand-alone Part D. Because they average 450,000 members, they include a very high proportion of the leading health plans of this type.

Collectively, Commercial Insured comprised 53% of membership, with ASO comprising an additional 19% for a total of 71% Commercial. Various Medicare products comprised 11% of membership and various Medicaid products comprised an additional 17%. Medicaid products were chiefly Medicaid HMO, as opposed to CHIP, of which 86% were low income or TANF.

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### Figure 6. Sherlock Benchmark Summary

Independent / Provider-Sponsored Costs by Functional Area Cluster, 2014 Data

Percent of Premium Equivalent

Functional Area	25th Percentile	Median	75th Percentile	Coefficient of Variation
Sales and Marketing	2.2%	2.5%	2.9%	34%
Medical and Provider Management	1.3%	1.4%	2.0%	29%
Account and Membership Administration	3.1%	3.7%	4.5%	30%
Corporate Services	2.0%	2.3%	2.7%	28%
<b>Total Expenses</b>	8.4%	9.2%	10.5%	21%

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## Appendix A. Sherlock Benchmark Summary

### Independent / Provider-Sponsored Costs by Functional Area Cluster, 2013 Data

*Per Member Per Month*

<b>Functional Area</b>	<b>25th Percentile</b>	<b>Median</b>	<b>75th Percentile</b>	<b>Coefficient of Variation</b>
Sales and Marketing	\$8.78	\$10.80	\$12.87	31%
Medical and Provider Management	5.37	6.38	7.84	31%
Account and Membership Administration	11.23	15.29	18.32	44%
Corporate Services	4.87	6.16	8.22	32%
<b>Total Expenses</b>	<b>32.12</b>	<b>38.59</b>	<b>48.58</b>	<b>28%</b>

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## Appendix B. Sherlock Benchmark Summary

### Independent / Provider-Sponsored Costs by Functional Area Cluster, 2013 Data

*Percent of Premium Equivalents*

<b>Functional Area</b>	<b>25th Percentile</b>	<b>Median</b>	<b>75th Percentile</b>	<b>Coefficient of Variation</b>
Sales and Marketing	2.4%	2.8%	3.1%	33%
Medical and Provider Management	1.3%	1.7%	1.8%	20%
Account and Membership Administration	3.0%	3.7%	4.9%	36%
Corporate Services	1.2%	1.6%	1.9%	28%
<b>Total Expenses</b>	<b>8.5%</b>	<b>9.7%</b>	<b>10.6%</b>	<b>22%</b>

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## Appendix C. Sherlock Benchmark Summary

### Major Functions Included in Each Administrative Expense Cluster

#### **Sales & Marketing**

Rating and Underwriting  
Marketing  
Sales  
External Broker Commissions  
Advertising and Promotion

#### **Provider & Medical Management**

Provider Network Management and Services  
Medical Management / Quality Assurance / Wellness

#### **Account & Membership Administration**

Enrollment / Membership / Billing  
Customer Services  
Claim and Encounter Capture and Adjudication  
Information Systems Expenses

#### **Corporate Services**

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