PHC4 fyi

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"The Blues Divorce" Revisited

Capital Blue Cross (CBC) and Highmark/Pennsylvania Blue Shield (PBS) are in the midst of separating their operations after more than 60 years of joint marketing and administration of medical claims. In August 2001, PHC4 reported on several questions that purchasers had asked about "The Blues Divorce" and the future of health insurance in Central Pennsylvania. This *FYI* will review some of those issues, discuss what has happened since then, and mention some emerging issues and questions purchasers are asking today.

- CBC is a non-profit company that previously contracted with hospitals and related providers, while PBS is a non-profit firm that has contracted with doctors and other medical service professionals in Central Pennsylvania. As of April 1, 2002 each company has begun to offer both hospital and physician coverage to potential customers.
- The Central Pennsylvania market is estimated to include more than 1.4 million members the two companies have jointly served in the past. As contracts come up for renewal, the firms are gradually allowing joint contracts to lapse, and are competing against each other as well as other insurance carriers. Within another year or so PBS and CBC plan to be entirely separated.
- CBC CEO Jim Mead notes that most of his firm's customers are not asking for product changes, therefore CBC is mainly offering some product enhancements. PBS CEO John Brouse says his firm is offering some wholly new products in Central Pennsylvania. Some purchasers believe the firms' product offerings appear similar.
- Purchasers, who generally benefit from competition in the marketplace, are asking whether it is possible to contain personnel costs in the new environment? Will the two companies add personnel? PBS says it is increasing staffing in response to its marketplace growth. CBC says its staff level will not change. Both say the quality of their services will not change.
- For the first time, the two Blues have begun separate advertising campaigns in Central Pennsylvania; purchasers are asking about the impact of these new marketing campaigns on premium costs.
- Some purchasers say they would like additional details about prescription drug coverage.
- Some purchasers are asking whether the level of provider reimbursements is increasing?
- In January 2002, CBC filed a petition with the state Insurance Department challenging PBS's right to offer both physician and hospital services in Central Pennsylvania. In February, the state Insurance Department dismissed the CBC petition. CBC has appealed the dismissal to Commonwealth Court, where the matter is now pending.
- The implications for Keystone Health Plan Central (KHPC), an HMO jointly owned by PBS and CBC, remain unclear. Both Mr. Brouse and Mr. Mead say there is no agreement about KHPC at this time. The settlement options include one firm buying out the other's share, or both firms selling to a third party. KHPC operates as a wholly owned subsidiary of CBC and PBS, and its operations are not expected to change in the near term.

Other issues have emerged that are of interest to Central Pennsylvania residents and purchasers. These include the implications of the CBC/PBS split for *Security 65* Medicare Supplemental members, and a change in community rating for small employer groups.

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Security 65 - The break-up affects some 90,000 customers over the age of 65, who have *Security 65* Medicare Supplemental coverage. On May 9, PBS and CBC jointly announced a plan that will have each firm covering half of the *Security 65* customers. The Pennsylvania Insurance Department, which helped devise the plan, said the *Security 65* customers will see no change in their coverage, and will continue to have access to the same doctors. In effect, they are treated as if the two companies had stayed together. Customers will be randomly assigned to the two companies and the firms will try not to split up spouses or families. According to a joint CBC and PBS press release, those enrolled in *Security 65* will not see any immediate change in their premiums, at least through December 31, 2002. After that, the firms can increase rates.

While the *Security 65* change does not go into effect until July 1, 2002, enrollees will receive a letter in May outlining the transition plan. A second letter will be sent before the end of September telling members which company they are assigned to and outlining their options. Members will have several opportunities during the next two years to change companies.

Insurance rating for small employer groups – When determining the premiums for small employer groups of 2 to 50 employees, the Blues have historically used *community rating*. With community rating, the risk is spread equally across an entire community without factoring in characteristics such as age or sex. Since the average risk is the same for all members of the community, all employer groups in the community pay the same insurance premium rate regardless of how often the group utilizes the health care system. For example, even if an employer has a younger workforce, and the employees are likely to be healthier and to use fewer health care services, the premiums charged to the group would be the same as the premiums charged an employer of an older workforce.

Community rating *by class*, often called *demographic rating,* uses additional *demographic* factors to determine premium rates. These demographic factors take into account the composition of the employer group including the age and sex of the employees. In turn, premiums charged to a group with an older population would reflect the likely use of increased health care services. Beyond the age and sex of the group, insurers may include other factors in the premium rates to adjust for the employer's industry-type and the average contract size (e.g., the number of single contracts versus family contracts).

PBS recently decided to implement community rating *by class* (demographic rating). Whether or not this significant change is due to the split, PBS indicates the change was necessary in order to compete with commercial insurers who already use community rating by class. PBS reports that they have been using community rating by class in other parts of the state for years, thereby offering groups with better demographic characteristics a more competitive premium rate. Once PBS made the decision to use demographic rating factors in Central Pennsylvania, CBC says it had to follow suit to stay competitive.

Mr. Mead says he realizes the timing for the change might be inopportune. He recognizes that purchasers might think that the shift to demographic rating is a primary motivation of the two companies — to increase premium revenues. But CBC and PBS report that the community rating by class does not increase their overall revenues. According to both organizations, other factors such as increased utilization and cost of health care services have an impact on premiums. If it were not for these other factors, both firms say premiums would not be increasing.

The Pennsylvania Insurance Department confirms that overall rates will be rising 10-15% this year, regardless of structural changes in the marketplace. With demographic factors added, some price changes for small employers could be larger. This might be a difficult pill for purchasers to swallow, particularly since some groups have already faced significant premium increases on contracts beginning April 1, 2002, or may see large rate hikes soon.

The effects of the change to demographic rating or community rating by class have not yet been fully determined, nor are they likely to be widely understood by the general public for some time. Some purchasers say they have received lower premium prices; some say premium rates are significantly higher. As competition heats up, there may or may not be good pricing opportunities available. Whether prices will be contained in future years is a subject of speculation. *Purchasers might wish to familiarize themselves with their pricing options and obtain quotes from as many insurers as possible as early as possible.*

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