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## BCBS Study Shows Low Health Plan Administrative Costs

*John Commins, for HealthLeaders Media, August 14, 2009*

Private health plans' administrative costs averaged 9% of premiums across all policies sold and are well below "vastly overstated" estimates offered by proponents of a government-run public plan, according to a new study paid for by the Blue Cross Blue Shield Association.

A consumers' rights group disputes the findings.

[The report](#), written by Sherlock Company, states that previous studies showing that private health plans' administrative costs are two to three times higher than actual costs are based on old estimates that don't reflect changes in industry practices, including advances in electronic processing.

"Prior reports rely on outdated, decades-old estimates from when claims were paper-based and today's electronic processes were in their infancy," says Douglas B. Sherlock, president of the Sherlock Company. "This report demonstrates that health plan administrative costs have been vastly overstated." The study reviewed 36 health plans—mostly Blues—participating in benchmarking studies in 2008.

Advocates for a public plan maintain that the higher administrative expenses for private plans are one reason why a public plan is needed. Health insurance industry officials say the Sherlock study undermines that claim.

"Some elements of healthcare reform can help reduce administrative costs, if done right. For example, state-based health insurance exchanges can make it easier for people to purchase health insurance and simplify administrative functions," says Scott P. Serota, president/CEO of the Blue Cross and Blue Shield Association.

The Sherlock report also claims that private plans perform the administrative functions that Medicare performs for \$12.51 per member per month, compared to \$13.19 per month for Medicare, and that private plans perform more administrative functions than traditional Medicare, including care coordination and wellness programs.

However, Cathy Schoen, senior vice president The Commonwealth Fund, says the Sherlock study is narrowly drawn. "It focused more on the Blues than the whole industry and it is focusing just on what it narrowly calls the administrative costs, not profit margins," Schoen says. "When you talk about the share of the premium that is not being paid out in benefits, it's both administrative and profits."

She says corporate reports from larger companies like Aetna and UnitedHealthcare show pretax profits in the 6% range in 2008, and administrative costs as a share of operating revenue running in the 15%-16% range. "UnitedHealth, out of all the revenue it took in, the

amount it paid out was only 82%. So 18% was not paid out in medical benefits. In 2007, it was 19%," Schoen says.

She says the Blues also don't count the average 5% commission that businesses usually pay the agents who write the insurance contract as administrative costs. "That is on top of the Blues' marketing costs. From the employer's perspective, that agent fee is part of it. But the Blues' don't count it because they don't pay the agent. The customer pays it though," she says.

Schoen says public and private health plans in the United States average about \$600 per person a year for insurance administrative costs, compared with an average of about \$200 for many countries in Europe. "Nine percent would be considered high in every country outside the United States. Fifteen percent would be considered unbelievable," she says.

A [recent Commonwealth Fund study](#) claims the cost of administering the U.S. healthcare system totaled nearly \$156 billion in 2007, and that figure is expected to double—reaching \$315 billion—by 2018. In addition, the study claims that costs incurred by physicians in their transactions with health plans are estimated to be as high as \$31 billion a year.

About 12.4%—or \$96 billion—of the \$775 billion in privately insured healthcare spending went for administrative costs in 2007. That \$96 billion—representing what insurance companies received in premiums, minus what was paid in medical claims—included claims processing, advertising, sales commissions, underwriting, and other administrative functions; net additions to reserves; rate credits and dividends; premium taxes; and profits, the Commonwealth study claims.

By contrast, about 6.1%—or \$60 billion—of the \$974 billion in public program healthcare spending went for administrative costs in 2007, the Commonwealth report claimed. That includes federal, state, and local governments' administrative costs for public health programs, such as Medicare, Medicaid, and the State Children's Health Insurance Program. Medicare prescription drug coverage, provided by private plans, has high administrative costs, but is included in public program administration figures. Private Medicare Part D plans averaged 11.3% in administrative costs as a share of total drug spending, the Commonwealth study added.

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[Back](#)