Economic Impact Analysis
Virginia Department of Planning and Budget

12 VAC 5-408 – Regulations for the Certification of Quality Assurance of Managed Care Health Insurance Plan Licensees; Virginia Department of Health
June 11, 1999

The Department of Planning and Budget (DPB) has analyzed the economic impact of this proposed regulation in accordance with Section 9-6.14:7.1.G of the Administrative Process Act and Executive Order Number 25 (98). Section 9-6.14:7.1.G requires that such economic impact analyses include, but need not be limited to, the projected number of businesses or other entities to whom the regulation would apply, the identity of any localities and types of businesses or other entities particularly affected, the projected number of persons and employment positions to be affected, the projected costs to affected businesses or entities to implement or comply with the regulation, and the impact on the use and value of private property. The analysis presented below represents DPB's best estimate of these economic impacts.

Summary of the Proposed Regulation

This proposed regulation implements the requirements of SB712 (1998) requiring the Department of Health to establish a certification program for managed care health insurance providers (MCHIPs). MCHIPS are health care insurance plans that arrange for insured individuals to obtain their care mostly or entirely from health care providers (physicians, hospitals, etc.) under contract with or employed by the insurance organization. The intended purpose of the certification program is to require MCHIPs to satisfy a set of quality assurance standards. These standards do not, in most respects, specify what coverage must be offered by the MCHIPs.[1] Instead, they specify a set of procedures and standards of operation designed primarily to ensure that the insured parties receive the care that they are entitled to in their coverage contract. This is accomplished by a set of standards for keeping consumers informed and for managing information within the organization itself about the quality of services and

customer satisfaction. The standards include requirements for resolving and tracking consumer complaints.

These quality assurance standards reflect, in many respects, the standards for quality assurance used by national certification organizations. For example, for health maintenance organizations (HMOs), satisfying the accreditation standards of the National Committee for Quality Assurance (NCQA) will bring the HMO into compliance with most, if not all, of the requirements of this rule, although, the regulations do not allow satisfaction of the NCQA standards to substitute for compliance with the terms of the certification requirements and the certification review process.

The rules proposed here apply somewhat differently to the various types of MCHIPs. MCHIPs can be roughly categorized into three types: HMOs, preferred provider organizations (PPOs), and point of service providers (POS). The differences between these types of arrangements have to do with the contractual arrangements between the MCHIP and its providers and with the terms on which consumers can seek care outside of the MCHIPs contracted providers.

Estimated Economic Impact

The number of people enrolled in managed care programs has increased from 6 million people in 1976 to more that 70 million today. The significant penetration of managed care into the health care market has been credited by some with a substantial share of the reduction of the growth rate of medical expenses during the 1990s. Managed care programs reduce medical costs in a number of ways. First, large managed health care organizations are in a relatively strong bargaining position with respect to their suppliers and may be able to obtain price discounts. Second, MCHIPs reduce costs by writing contracts with providers (physicians and hospitals) that result in lower costs per procedure. Third, MCHIPs save money by reducing utilization through utilization review, health management for individuals, and preventive care.

The use of utilization review and the restrictions on which providers could provide care to the enrolled have led to an increasing number of complaints as the population enrolled in

[1] There are exceptions to this general statement. For example, the regulations specify maximum travel times for the

MCHIPs has expanded. The Virginia General Assembly responded by requiring that the Department of Health (VDH) establish regulations governing the quality of care of individuals covered by managed care plans. These proposed regulations attempt to allay the concerns about the quality of MCHIP care by requiring MCHIPs to have in place a set of quality assurance procedures. The rules also provide for periodic review of MCHIP compliance with the requirements. These include: grievance procedures, customer satisfaction assessment, accessibility assurance, preventive services, credentialing contract providers, informing enrollees and providers of policies, outcome-based measures of improved health outcomes, confidentiality assurance, and utilization review standards.

As mentioned earlier, these standards are similar to those established by national accrediting organizations. HMOs are required to meet all of these requirements. PPOs are exempt from some of the standards (particularly utilization review) if they are accredited by nationally recognized accreditation standards for PPOs.[2] These regulations only apply to a subset managed health plans, but the organizations that offer the covered plans also offer the non-covered plans in Virginia. Thus, all managed care organizations in Virginia are likely to be affected.

Costs

For MCHIPs not choosing to seek accreditation from one of the national organizations, the cost of complying with this regulation is probably somewhat less than the cost of complying with the national accreditation standards. MCHIPs that do choose to become accredited will probably find that these regulations will impose some additional expenses, partly because there are a few additional requirements and partly because the VDH will be conducting on-site reviews which will involve a commitment of MCHIP staff resources. The additional costs experienced by MCHIPs already satisfying the standards of the national accrediting organizations will be relatively modest.[3] For an organization not yet accredited, the costs may be considerable

insured to various types of health care facilities and services.

[2] Two such standards currently exist and are specifically listed in the regulation: (1) the American Accreditation Health Care Commission/Utilization Review Accreditation Commission (AAHCC/URAC), and (2) the Joint Commission on Accreditation of Healthcare Organizations' Accreditation Standards for Preferred Provider Organizations (JCAHO).

[3] The Virginia Association of Health Plans has argued that these rules are more burdensome than is required to accomplish the legislative intent. First, they impose a number of substantive standards for care in addition to the management systems envisioned in the legislation. Second, the rules could accomplish their intended purpose by

depending on how large the organization is and how far it is from meeting the accreditation standards. Putting these standards in place can be a very expensive proposition. Figures reported for the initial investment in accreditation range from $0.25 million to $1 million.[4] It is not possible at this writing to make a reliable estimate of gross compliance costs.

Surveys of MCHIPs indicate that most of them have some grievance procedures in place, many perform customer satisfaction surveys annually, many have explicit utilization review standards and procedures.[5] Since the actual distribution of costs are not known at this time, the aggregate gross cost of compliance of MCHIPs cannot be estimated at this time although it can reasonably be expected to be several million dollars for initial compliance by all 110 MCHIPs and some continuing elevated operating expenses in subsequent years.

As already indicated, this is the *gross* cost of compliance. Since these regulations are requiring a set of management practices that are only marginally different from the national private accreditation standards, and since a number of MCHIPs have already voluntarily sought and received accreditation, it may be assumed that there is some benefit to firms of receiving accreditation. Among the potential benefits are: improved customer satisfaction, improved health outcomes, improved public perception, and improved management information.[6] For those firms that had not in the past sought accreditation, it may be assumed that the benefits listed above were worth something but that that amount was less than the cost of achieving accreditation. Thus, to get the net cost of compliance, we must subtract off any incidental benefits of achieving compliance.[7] The magnitude of these offsetting benefits of compliance is probably not known with any degree of certainty even by the MCHIPs themselves. There are not, at this time, any publicly available estimates.

Estimating the cost of compliance is further complicated by the possibility that some MCHIPs may choose to substitute the VDH quality assurance certification for the certification

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allowing MCHIPs to be "deemed" to satisfy the standards if they have received accreditation. Finally, the Association argues that VDH is requiring the reporting of more information than is needed to accomplish the regulatory purpose.

[4] Personal conversations with Robert Hurley, Virginia Commonwealth University ($0.5 million), Nancy Hofheimer, VDH ($0.25 million), 6/10/99. Also, Mark Pratt and Lynn Warren of the Virginia Association of Health Care Plans (up to $1 million), 6/14/99.

[5] *Final Report: President's Advisory Commission on Consumer Protection and Quality in the Health Care Industry* (1998), See especially, Chapter 2. Available from: http://www.hcqualitycommission.gov/final.

[6] Personal conversation with Nancy Davenport-Ennis, National Patient Advocate Foundation.

they might have otherwise chosen to receive from the national accreditation organizations. If it is less costly to achieve VDH certification, and if firms can gain much of the public relations value from VDH as from private certification, then there may be some substitution. For MCHIPs that would have chosen national accreditation, the existence of these regulations could actually reduce costs.

However, since the national standards are somewhat more detailed than the VDH rules, there is the possibility that the VDH rules will not produce the same level of quality assurance as the national accreditation standards. VDH argues that their standards have been written to achieve the same level of quality assurance as the national standards. It is not possible, at this time, to make a useful estimate of the value of the impact of any substitution away from national standards that might occur due to this proposed regulation. Only actual experience after the implementation of the rules will allow an assessment of the net impact of these effects.

Whatever the magnitude of the cost increase the costs will be distributed between the complying organization and its customers. Nearly 85% of Americans with health insurance coverage are in managed care plans. These regulations only affect MCHIPs covering approximately one fifth of the Virginia population covered by managed care plans. However, representatives of the Virginia Association of Health Care Plans (VAHCP) have argued that these rules will actually affect virtually all MCHIPs in Virginia, because the plans covered by these proposed standards are offered by the same firms and organizations that offer the plans not covered. VAHCP argues that the VDH certification standards will involve organization-level changes rather than changes at the individual plan level. Given that this is true, it may be expected that most of the net costs of compliance will be passed on to customers since the regulations affect all providers.[8] If the customer is an employer, the employer may choose not to pass all of the costs along to its employees, however, it can be expected that some share of the net costs will be passed along to consumers. It is important to note that if a significant number of

[7] It has even been suggested that compliance with these rules could actually improve profits for MCHIPs. This is not likely to be a common occurrence since these firms had the option of doing the things required of this regulation voluntarily and chose not to do so.

[8] Should the VAHCP assertion not be true, then there is the potential that these regulations could induce some substitution away from covered plans toward non-covered plans. In that case, we would expect to see some of the costs of compliance paid by the organizations offering the MCHIPs. This is because the higher price-elasticity of demand for covered plans would force the providers to absorb some portion of cost increases. In general, however, we would expect that most of the increased costs will be directly passed on to consumers. It should also be noted that any substitution away from covered plans toward non-covered plans could affect the net costs or benefits ultimately achieved by these proposed rules.

insurers leave the Virginia market due to these rules, there could be some impact on the competitiveness of some health care markets resulting in some additional losses to consumers.

The demand for health insurance, as with other goods, depends on price. Therefore, it can be expected that any cost increases from complying with this regulation may result in some firms choosing to drop all or part of their employee health plan or some number of insured people choosing to drop their coverage. Since the magnitude of the cost increases is not known, no estimate can be provided for the likely number of people who will choose to drop coverage.

Benefit

The benefits of the proposed regulation arise from the potential for better health outcomes and for increases in consumer satisfaction.[9] A report prepared by the VDH[10] presents some focus group and survey data on customer satisfaction with managed care plans. It is not clear from the report that the level of consumer dissatisfaction in the managed care field is significantly different from consumer dissatisfaction in other services that people purchase. Nor is it necessarily true that consumer dissatisfaction is necessarily indicative of reduced health outcomes.

In order to assess the benefits of this regulation, we would need to have information on the differences in health outcomes (and satisfaction) for MCHIPs before and after the imposition of the rules. We would also need to know whether firms would have implemented any of the requirements of these standards without the promulgation of the regulations. If MCHIPs are in some way insulated from competitive pressures that would give more competitive firms incentive to improve their quality assurance management, then there may be significant gains from the imposition of these regulations. If, on the other hand, MCHIPs are in a more competitive environment, where a number of firms or organizations are competing for enrollees, then we would expect the gains from these regulations to be small.

In the absence of direct evidence on any of these issues, the magnitude of benefits resulting from this proposal cannot be estimated in any meaningful way. It cannot be known at this time whether this proposal will result in a net benefit or cost to the Virginia economy. Given the prevalence of uninsured individuals, it is very important that careful attention be given to

[9] Aside from the direct benefit to individuals of these effects, an indirect effect could be a reduction in the amount of litigation and other ancillary costs resulting from poor health outcomes and consumer dissatisfaction.

[10] *The Role of the Commonwealth in Monitoring and Improving the Quality of Care in Managed Care Plan: House Document No. 14 (1998)*. Virginia Department of Health. Richmond.

making sure that the benefits of this regulation are achieved at the lowest possible cost. Each addition to MCHIP costs should be assessed for whether the benefits of the added information or management process add significant value to the regulation.

Businesses and Entities Affected

This regulation affects approximately 110 managed care health insurance plans in Virginia.

Localities Particularly Affected

No localities are particularly affected by this regulation.

Projected Impact on Employment

This regulation will probably raise somewhat the cost of employer-provided health insurance. This may result in some shift in the mix of types of compensation received by Virginia workers, but will probably not have any significant net impact on the level of employment.

Effects on the Use and Value of Private Property

It is expected that most of the costs of this regulation will be passed on to employers and consumers. However, any portion of costs paid by for-profit health care firms could result in lower profits and hence a lower market value for the firm than would be the case in the absence of the regulation. This effect is not expected to be large.