

Purpose

Average Cost Based Reimbursement Plans pervade intra- and inter-organizational health care financing throughout the world. These mechanisms are primarily, rather than incidentally, risk transfer agreements, frequently a form of unregulated reinsurance for nominal health care insurers. This report focuses on the consequences of risk transfers to professional caregivers (PCs), that place PCs in the roles of insurers rather than providers, seriously upsetting the balance between these two roles, compromising PC financial stability, service quality, and provider-consumer relationships by greatly increasing overall financial risk for PCs and their patients...

Comparison of Insurer v. Provider Risk

Risk = Probability of a Loss Greater than Loss Ratio
Due to Size Differentials Between Insurer and Provider

<u>Loss Ratio</u>	<u>Insurer Risk</u>	<u>Provider Risk</u>	<u>Relative Risk</u>
0.85	0.500	0.500	1.000
0.86	0.421	0.482	1.146
0.87	0.345	0.464	1.348
0.88	0.274	0.447	1.629
0.89	0.212	0.429	2.025
0.90	0.159	0.412	2.594
0.91	0.115	0.394	3.426
0.92	0.081	0.377	4.670
0.93	0.055	0.360	6.574
0.94	0.036	0.344	9.565
0.95	0.023	0.327	14.389
0.96	0.014	0.311	22.396
0.97	0.008	0.296	36.078
0.98	0.005	0.281	60.176
0.99	0.003	0.266	103.955
1.00	0.001	0.251	186.054

Portfolio transfer = 1/20th of insurers

Different risk characteristics based on normal sampling distribution

Financial failure risk is higher because of undercapitalization, timing, bonus plans

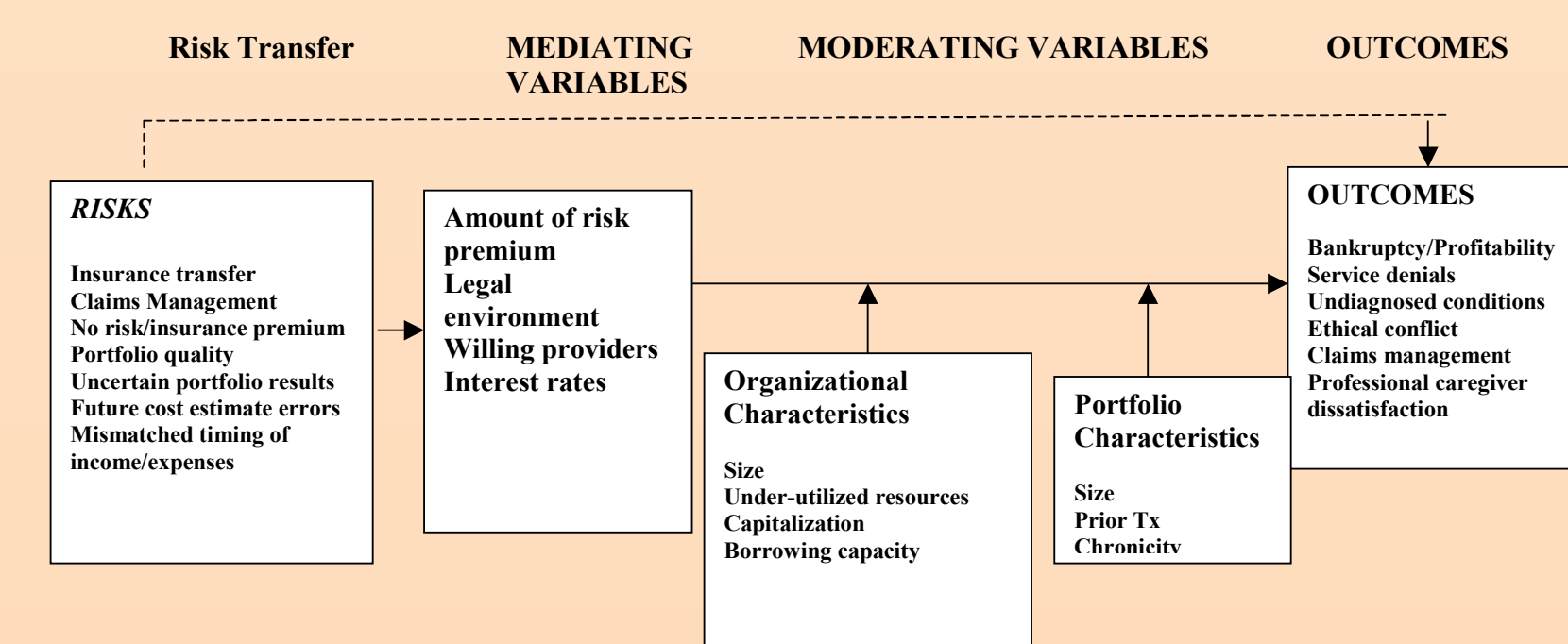
Average Cost Based Reimbursement and Risk Theory: Implications for Health Care Policy and Practice

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Model of ACBRP Impact



Overall Findings

Capital and Income: PCs that accept insurance risks are under-funded, undercapitalized, inadequately resourced for the insurance business, unregulated for insurance, and unable to benefit from actuarial and underwriting expertise. Policy aggregators that transfer such risks avoid insurance risk, compete unfairly with true insurers, and through differential knowledge of insurance and risk theory, advantage themselves at the expense of providers and consumers.

Risk Management: Premiums provided to PCs are inadequate compensation for the insurance risk assumed, transferring risk to patients. Inadequate premiums implies that reinsurance is not viable as a risk management strategy for PCs. Delays in payments further exacerbate PC's financial experience as do compensation plans that kick in when least needed – when losses are low. ACBRPs violate fundamental principles of risk theory and insurance – eliminating the essential social benefit of insurance.

Legal and Ethical Issues: Largely unregulated insurance transfers, with no specific accounting standards, inadequate regulation and oversight, result in ethical conflicts, violated consumer trust, inadequate and unreliable service delivery, as well as substantial risk of white collar crime in the form of denial of services.

How are Average Cost Based Reimbursement Plans and Traditional Insurance Similar and Different

	ACBRP	INSURANCE
Capital and Income		
Amount	Nonexistent for PCs	Varies by state
Form	None	Secure Investments/Cash
Oversight	None	SAP/GAAP/FASB
Investment expertise	Little	Substantial
Usual source of profits	Service delivery	Premiums and investments
Risk Management		
Loss Premium	Yes	Yes
Expense Premium	Yes	Yes
Risk Premium	None	Yes
Risk management expertise	None	Actuaries/Underwriters
Overall Risk	Increases	Decreases
Who really bears the risk	Patients	Contracted Providers
Who is the real insurer	Professional caregivers	Insurance company
Reinsurance	Further depletes premium	Calculated in premium
Consequences of large losses	Unanticipated – Bankruptcy, takeovers and consolidations	Anticipated/Managed
Time value of money 1		Substantial investment income potential
Time value of money 2	Costs precede income	Premium available for secure investments
Results	Substantial premium withheld	Highly predictable
Profitability due to inefficiency	Highly unpredictable Unproven assumption	Profitability due to LLN and CLT, risk spread, actuarial, underwriting, and financial expertise
Legal and Ethical Issues		
Regulation	None	State and Federal laws/regs
Accounting Requirements	None	SAP/GAAP/FASB
Contract Law/Case Law	Emergent	Substantial
Rights of consumers	Unclear	Substantial
Ethical issues of service provision	Inherent role conflicts	Dispassionate/Imperfect
Duties	Pt v pt, self v pt, family v pt	Duty to contractees
Non-performance of duties	Difficult to detect and pursue	Much oversight and case law

Average Cost Based Reimbursement Plans

Capitation contracts, Diagnosis Related Groups plans, Preferred Provider agreements, Managed Care, Unrealistic budgeting constraints in highly variable units such as nursing.

Whereas product line operating characteristics are good models in manufacturing, especially in assembly line operations, the inherent variability in health care settings, particularly when patients are already known ill makes such approaches injurious rather than helpful, since they assume higher levels of rationality and predictability than apply.

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Conclusions

PCs cannot perform the functions of trusted informants and care provision and the insurance underwriting and claims management functions implicit in insurance risk assumption.

Proper compensation, including risk premiums will cost more than aggregators can charge.

Reinsurance further depletes loss premiums while paying reinsurers to assume the risks PCs should not have accepted.

A high index of suspicion of unethical actions should be presumed in such relationships – rather than a low index of suspicion. Wolves should not provide security for lambs.

Implications

Unregulated risk transfers to PCs should be prohibited under extant insurance law. Hidden insurance transfers in politically supported finance plans must be examined as insurance transfers – even within organizations. The consequences of PC insurance risk assumption: financial, ethical, criminal, must be explored and documented

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