



MANAGED CARE

Research Brief

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SASB's industry brief provides a summary of the material sustainability issues that are likely to impact shareholder value. The issues identified within are industry specific, and reflect how the associated companies rely on environmental, social, and human capital. Further, the brief identifies material sustainability issues that pertain to business model and innovation, and governance. SASB adheres to the U.S. Supreme Court definition of materiality, defined as "presenting a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." To identify material sustainability issues, SASB's research team examines three types of evidence; evidence of interest, evidence of financial impact, and forward looking impact. The research reflected within this document was conducted by SASB and an initial version of the document served as an input for the Industry Working Groups to evaluate the materiality of industry issues and potential accounting metrics. The industry brief is not the disclosure standard, but rather is intended to provide background context and evidence for the material sustainability issues that SASB identified for the given industry. SASB takes sole responsibility for errors and omissions.

Related Documents

- [Health Care Sustainability Accounting Standards](#)
- [Industry Working Group Participants](#)
- [SASB Conceptual Framework](#)
- [Example of Integrated Disclosure in Form 10-K](#)

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MATERIAL SUSTAINABILITY ISSUES

Environmental Capital

- Climate Change Impacts on Human Health

Social Capital

- Access to Coverage
- Customer Privacy and Technology Standards

Human Capital

Business Model and Innovation

- Improved Outcomes

Governance

- Plan Performance
- Pricing Transparency and Plan Literacy

INDUSTRY SUMMARY

The managed care industry offers health insurance products for commercial, Medicare, and Medicaid members. For commercial customers, managed care companies pay for health care benefits in return for premiums. Companies also provide administrative services and network access for self-funded insurance plans.¹

Enrollment in managed care has traditionally been correlated with employment rates, while revenues are driven by medical-cost inflation. The Patient Protection and Affordable Care Act will expand the number of insured individuals over the next several years and will create increasing demand for services in this industry. Additional enrollment, coupled with an aging population that is entering Medicare eligibility, and competition between companies for economies of scale will create downward pricing pressure and continue to drive consolidation in the managed care industry. These factors will place further importance on the ability of managed care companies to maintain strong relationships with health care providers. Value will also be linked to new policies that tie performance to compensation in managed care.

¹ A list of the top five companies by revenue appears in Appendix I

The managed care industry provides a necessary and public good. However, the industry has contributed to a situation in which an estimated 60 percent of all personal bankruptcies in the United States are associated with extraordinary unpaid medical expenses, while 75 percent of those cases involved individuals who had health insurance coverage. Recent legislation attempts to address this imbalance and will therefore further align the interests of society with those of long-term investors by emphasizing how non-financial forms of capital contribute to market value. More specifically, the management of environmental, social, and human capital will increasingly affect traditional valuation by impacting revenue, assets, liabilities, and cost of capital. The ability of companies to manage these issues while also addressing the associated risks and opportunities through governance will be strong indicators of management quality and long-term value.

To ensure that shareholders are able to evaluate these factors, managed care companies should report on the material sustainability risks and opportunities that may affect value in the near and long term. Enhanced reporting will provide stakeholders with a more holistic (and comparable) view of performance that includes both positive and negative externalities and the non-financial forms of capital that managed care companies rely on to create long-term value.

The sustainability issues that will drive competitiveness within the managed care industry include:

- Addressing the increased health costs associated with climate change
- Facilitating access to coverage and health care as provided for by the Patient Protection and Affordable Care Act
- Ensuring the privacy of enrollee information
- Focusing on wellness programs and preventative care through new pricing structures and incentives
- Managing the key elements of plan performance as determined by the Five Star Quality Rating program
- Improving benefit, payment, and pricing transparency

The extent to which these sustainability factors impact value will become increasingly apparent as the legislative and regulatory environment continues to evolve and increased emphasis is placed on access, reduced costs, performance, and improved efficiency.

LEGISLATIVE AND REGULATORY TRENDS IN THE MANAGED CARE INDUSTRY

The legislative environment that governs the managed care industry continues to evolve. The following section provides a brief summary of key developments that are likely to impact value and to further amplify the importance of sustainability performance.

The Patient Protection and Affordable Care Act (PPACA) is expected to benefit the industry by expanding health insurance to an estimated 26 million people.^{ii,2} In addition, managed care companies will have the opportunity to solicit new contracts for their private Medicaid plans. The expansion of Medicaid eligibility is expected to bring an estimated \$38 billion in added revenues to the industry. Performance-based incentives from the Centers for Medicare and Medicaid Services will provide further opportunities for growth. However, companies in the managed care industry will also face new challenges associated with the PPACA.

The PPACA will be funded by a combination of cuts in Medicare and Medicaid reimbursement, and increased taxes on individuals, corporations, and the health industry, including an annual fee of \$60 billion which will be imposed on health insurance providers. In addition, managed care companies will compete in health insurance exchanges designed to encourage consumers to compare policies and premiums, which is expected to lead to increased competition and reduced costs. Finally, medical loss ratios will require companies to spend at least 80 percent of all premium dollars on health care services and quality improvement.

SUSTAINABILITY RISKS AND OPPORTUNITIES

Recent legislative efforts have focused on increased access, improved efficiency and transparency, and reduced costs to consumers. As a result, companies will not be able to maximize financial capital unless material sustainability issues are addressed as well. Managed Care companies that are able to navigate legislative and societal expectations, while addressing all forms of capital will be better positioned to protect shareholder value in the long run.

The following section provides a brief description of how the managed care industry depends on each form of capital, and outlines the specific sustainability issues that will drive performance including: evidence of materiality, value impact, and timing. Tables indicating the type of evidence gathered to demonstrate materiality for each issue, and the recommended disclosure framework appear in Appendix II and III. An analysis of the current state of reporting on material sustainability issues in the managed care industry appears in Appendix IV.

² Estimates range between 26 and 30 million for the number of people will become insured under the PPACA.

ENVIRONMENTAL CAPITAL

Relative to other industries, managed care companies do not engage in activities that have a direct impact on the environment, nor do they have a material dependence on natural resources. However, the industry will face challenges associated with the human health impacts of climate change.

Climate Change Impacts on Human Health

An increase in extreme weather events associated with climate change could have significant health impacts. These events coupled with the potential spread of infectious diseases, and food and water scarcity are likely to present material implications for the managed care industry through an increase in covered medical expenses.

Evidence

A 2011 study in Health Affairs found that future health costs due to climate change will be significant. Specifically, the study estimated that the health care costs associated with six climate related events between 2000 and 2009 were \$740 million. This estimate reflects more than 760,000 encounters with the health care system.ⁱⁱⁱ

WellPoint reports that “if the United States were to experience widespread bioterrorism or other attacks, large-scale natural disasters in our concentrated coverage areas or a large-scale pandemic or epidemic, our covered medical expenses could rise and we could experience a material adverse effect on our business, cash flows, financial condition and result of operations or, in the event of extreme circumstances our viability could be threatened.”

Value Impact and Timing

An increase in the frequency of extreme weather events has the potential to impact costs and liabilities by generating additional covered medical expenses. In addition, the associated risks could lead to an increased cost of capital.

SOCIAL CAPITAL

Managed care companies generate significant revenue through participation in government sponsored insurance programs. Subsequently, there is an expectation that companies in this industry provide access to services while maintaining the security of sensitive patient information. Companies that are able to ensure performance in these areas of social capital will be well positioned to enhance value.

Access to Coverage

Although the Patient Protection and Affordable Care Act (PPACA) will increase the number of insured individuals, the Congressional Budget Office estimates that 30 million nonelderly people will remain uninsured in 2023. The PPACA will require that managed care companies cover all applicants regardless of health status, gender, or pre-existing conditions. Increased demand will pressure firms to address their medical cost ratio, while maintaining access to coverage.

Evidence

A study published in the *Annals of Family Medicine* indicates that if health insurance premiums and wages continue to grow at current rates, family health insurance premiums will equal 50 percent of household incomes by the year 2021.^{iv} Further, studies indicate that increases in health care costs have driven overall health spending rather than changes in service or utilization.^v

In 2013, managed care companies were required to pay an estimated \$500 million in total rebates to more than 8.5 million individuals as a result of medical loss ratio provision of the PPACA.^{vi}

Value Impact and Timing

Rising health care costs and an expanding pool of insured individuals present opportunities for managed care companies to develop innovative solutions and pricing structures that reduce costs, increase enrollment, and provide additional revenue.

Customer Privacy and Technology Standards

The Health Insurance Portability and Accountability Act (HIPAA) requires health plans to comply with various requirements relating to the use, disclosure, storage, and transmission of patient health information. Further, companies in this industry are required to develop policies and technical safeguards to protect patient health information. A failure to comply with these evolving standards, which include new provisions established under the Health Information Technology for Economic and Clinical Health Act, can lead to significant civil and criminal penalties.

Evidence

Recent trends suggest that the government is increasing its enforcement of HIPAA's privacy and security provisions. In addition, the government continues to encourage the adoption of new technologies that will aid in ensuring privacy while reducing the administrative costs associated with information processing.

In 2012, BlueCross BlueShield of Tennessee agreed to pay \$1.5 million to the Department of Health and Human Services for a HIPAA violation. The settlement resulted from an incident in which unencrypted computer hard drives with protected health information were stolen from a facility in Tennessee. The company spent an additional \$17 million to investigate and resolve the incident.^{vii}

Value Impact and Timing

Breaches of customer privacy have the potential to result in fines, decreased consumer confidence and lower enrollment numbers. Poor performance in this area could impact profits and liabilities.

HUMAN CAPITAL

Managed care companies rely on human capital to maintain value. However, relative to other industries in the health care sector, these companies do not face specific and material risks or opportunities associated with human capital.

BUSINESS MODEL AND INNOVATION

Managed care companies operate in an evolving sector. As the current legislative framework continues to reward companies that demonstrate improved outcomes, the ability to manage performance in this area will be a critical indicator of corporate value.

Improved Outcomes

Managed care companies have the opportunity to create shareholder and societal value by working to improve the health of enrollees. The Patient Protection and Affordable Care Act places increased emphasis on health outcomes through provisions that require health plans to provide coverage for preventive services without cost to members. Further, the Act established the Five Star Quality Rating System for Medicare Advantage Plans. This rating system ties federal reimbursement rates for Medicare Advantage carriers and bonus payments to performance on five domain areas, including specific outcome based measures. Subsequently managed care companies that are able to improve the health of enrollees will be better positioned to protect shareholder value.

Evidence

Recent studies indicate that obese men incur \$1,152 dollars in additional medical costs per year, while obese women have additional expenses of \$3,613.^{viii} Rising rates of obesity and other preventable illnesses add significant expenses to the managed care industry. Companies that are able to support or reward better outcomes can achieve significant savings and improve shareholder value. In particular, this transition can be achieved through the adoption of a capitated model in which incentives to keep customers healthy are aligned with efforts to lower costs.

For example, Cigna offers a health risk assessment tool to help customers determine if they would benefit from wellness and behavioral modification programs. Individuals subsequently have access to health coaches who can help inform decisions.

Value Impact and Timing

Efforts to improve the health of consumers can lead to reduced covered medical costs and increased margins for companies in the managed care industry. Strong performance in this area is likely to increase profits and reduce liabilities.

GOVERNANCE

An evolving legislative and regulatory environment, downward pricing pressure, and competition in the managed care industry increase the importance of strong governance. Management structures must be able to negotiate shifts in policy while ensuring plan performance, pricing transparency, and plan literacy. Information on these aspects of governance is essential for shareholders to understand management quality and a company's ability to protect value.

Plan Performance

Managed care companies must manage performance in areas such as responsiveness, complaints, voluntary disenrollment, and customer service in order to maintain competitiveness. Under the Five Star Quality Rating System for Medicare Advantage Plans, performance on key plan performance metrics will be factored into federal reimbursement rates and bonus payments for Medicare Advantage carriers.³ The ratings will assess performance in the following five domains: staying healthy via preventive services such as screenings and vaccines; managing chronic conditions; ratings of plan responsiveness and care; complaints,

³ The rating system is based on five existing rating programs: Healthcare Effectiveness Data and Information Set (HEDIS), Consumer Assessment of Healthcare Providers and Systems (CAHPS), Centers for Medicare and Medicaid Services (CMS), Health Outcome Survey (HOS), and Independent Review Entity (IRE).

appeals, and voluntary disenrollment; and telephone customer service. Disclosure on key indicators related to these issue areas will allow shareholders to understand how managed care companies are ensuring corporate value.

Evidence

Managed care companies that achieve three or more stars on the Five Star Quality Rating System received bonus payments from federal programs beginning in 2012. As of 2015, these bonuses will be issued to plans receiving four or five stars. Further, five star plans have the ability to recruit customers throughout the year instead of being limited by the normal enrollment period.

UnitedHealth reports that “although we are dedicating substantial resources to improving our quality scores and star ratings, if we are unable to significantly increase the level of membership in plans with a rating of 4 stars or higher for the 2015 payment year, our 2015 results of operations and cash flows could be adversely impacted.”

Value Impact and Timing

Plan performance has the potential to impact profits and intangible assets. Companies that achieve high quality ratings will have the opportunity to increase revenues and assets through increased enrollment.

Pricing Transparency and Plan Literacy

Managed care companies can create value through effective communication and transparency. The Patient Protection and Affordable Care Act strengthens that link by requiring that all health plans provide a uniform summary of benefits and coverage for enrollees and applicants. Companies will also be required to provide two examples of typical out-of-pocket costs for common medical events. Performance in this area will contribute to value as companies compete for new applicants in state-based exchanges.

Evidence

Since the PPACA limits competition based on risk selection, managed care companies will be incentivized to compete on the basis of the quality of care that enrollees receive. This will place additional emphasis on a plan’s ability to communicate cost structures and other information.

Value Impact and Timing

Firms that are able to adhere to federal requirements relating to transparency and literacy will be better positioned to avoid fines and to attract new enrollees, thereby impacting both profits and liabilities.

SASB INDUSTRY WATCH LIST

The following section provides a brief description of sustainability issues that did not meet SASB's materiality threshold at present, but could have a material impact on the managed care industry in the future.

Integration of Environmental and Social Factors in Investment Management

Managed care companies are responsible for the capital preservation of premium revenue equivalent to expected policy payouts. Subsequently, companies must be able to maintain long-term asset-liability parity. As large asset owners, the managed care industry could face increasing pressure to account for the environmental and social impacts of these investments. Failure to address these issues could lead to diminished returns and limit a company's ability to issue payments for covered medical costs.

APPENDIX I: Top Five Companies by Revenue | Managed Care

- UnitedHealth Group Inc.
- WellPoint Inc.
- Humana Inc.
- Aetna Inc.
- Cigna Corp.

APPENDIX II: Evidence of Materiality | Managed Care

The following table provides a summary of the evidence of materiality for each issue in the managed care industry.

MATERIAL SUSTAINABILITY ISSUES		EVIDENCE OF INTEREST					EVIDENCE OF FINANCIAL IMPACT				FORWARD-LOOKING IMPACT			
		MM	IWGs		Other	EI	Revenue / Cost	Asset/ Liability	Cost of Capital	EFI	Probability	Magnitude	Timing	FLI
			%	Priority										
ENVIRONMENTAL CAPITAL	Climate Change Impacts on Human Health	20%	-	-	•	Low	•	•	•	Low	•	•	Near	Yes
	Access to Coverage	55%	90%	2		High	•			Med				
SOCIAL CAPITAL	Customer Privacy and Technology Standards	35%	90%	5	•	Med	•	•		Low	•	•	Near	Yes
	Improved Outcomes	80%	80%	1		High	•	•		High	•	•	Near	Yes
GOVERNANCE	Plan Performance	53%	100%	4		Med	•	•		High	•	•	Near	Yes
	Pricing Transparency and Plan Literacy	95%	90%	3		Med	•	•		Low				

EMERGING SUSTAINABILITY ISSUES		EVIDENCE OF INTEREST					EVIDENCE OF FINANCIAL IMPACT				FORWARD-LOOKING IMPACT			
		MM	IWGs		Other	EI	Revenue / Cost	Asset/ Liability	Cost of Capital	EFI	Probability	Magnitude	Timing	FLI
			%	Priority										
GOVERNANCE	Integration of ES Factors in Investment Management	-	-	-		Low		•		Low	•	•	Near	Yes

MM: Materiality Map, a percentile score of the relative importance of the issue among SASB's initial list of 43 generic sustainability issues. The score is based on the frequency of relevant keywords in documents (i.e., 10-Ks, shareholder resolutions, legal news, news articles, and corporate sustainability reports) that are available on the Bloomberg terminal for the industry's publicly listed companies.

IWGs: SASB Industry Working Groups

%: The percentage of IWG participants that found the issue to be material. (-) denotes that the issue was added after the IWG was convened.

Priority: Average ranking of the issue in terms of importance. One denotes the most material issue. (-) denotes that the issue was added after the IWG was convened.

Other: Other evidence of interest including: in-depth 10-k analysis, shareholder resolutions, corporate sustainability reports, traditional financial analysis, impending regulation, and academic studies. This is primarily used in cases where the issue was added after the IWG or the issue received lower MM and IWG scores. However, this test is also used in some cases where there is significant additional evidence of interest.

EI: Evidence of Interest, a subjective assessment based on quantitative and qualitative findings.

EFI: Evidence of Financial Impact, a subjective assessment based on quantitative and qualitative findings.

FLI: Forward Looking Impact, a subjective assessment on the presence of a material forward-looking impact

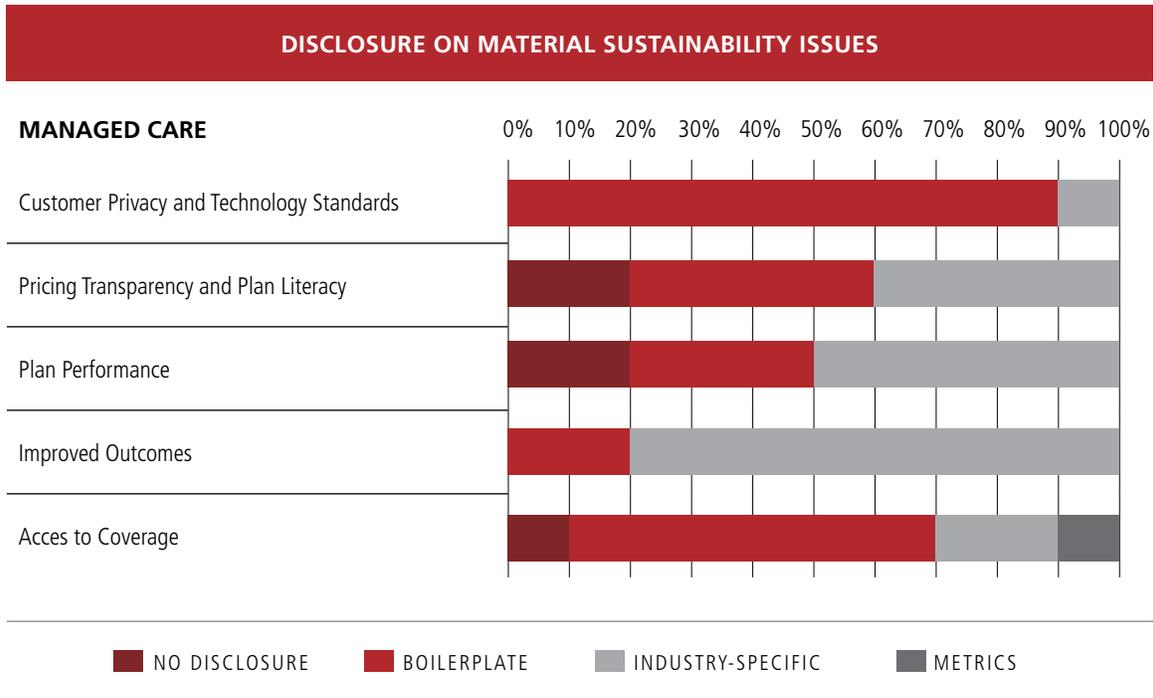
APPENDIX III: Sustainability Accounting Metrics | Managed Care

The following table provides a list of sustainability issues and the associated accounting metrics for the managed care industry.

TOPIC	CODE	ACCOUNTING METRIC
Access to Coverage	HC0303-01	Medical Loss Ratio (MLR) = medical costs as percentage of premium revenue.
	HC0303-02	Rebates accrued and rebates paid due to non-compliance with Section 2718 of the Patient Protection and Affordable Care Act for Medical Loss Ratio (i.e., the "80/20 Rule").
	HC0303-03	Percentage of proposed rate increases receiving "not unreasonable" designation from Health and Human Services (HHS) review or state review (where it is authorized to conduct the review).
Improved Outcomes	HC0303-04	Percentage of enrollees in wellness programs by type: diet & nutrition, exercise, stress management & mental health, smoking or alcohol cessation, or other.
	HC0303-05	Coverage of preventive services: (1) Total coverage (\$) for preventive health services with no cost sharing for the enrollees including that which is required by the Patient Protection and Affordable Care Act; (2) Total coverage (\$) for preventive health services requiring cost-sharing by the enrollee, including the percentage of the cost of services covered by the registrant; and (3) Percentage of enrollees receiving Initial Preventive Physical Examination (IPEE) or annual wellness visit (AWV).
	HC0303-06	Number of customers receiving care from Accountable Care Organizations or enrolled in Patient-Centered Medical Home programs.
Plan Performance	HC0303-07	Mean Medicare Advantage plan rating (1–5 stars) for each of the following plan types: HMO, local PPO, regional PPO, PFFS, and SNP.
	HC0303-08	Enrollee retention rate by plan type, including HMO, local PPO, regional PPO, PFFS, and SNP.
	HC0303-09	Percentage of claims denied that were appealed by customers and ultimately reversed.
	HC0303-10	Grievance rate per 10,000 enrollees.
Pricing Transparency and Plan Literacy	HC0303-11	JD Power & Associates members' rating on "Information and Communication."
	HC0303-12	Description of policies and practices related to clarity in pricing and coverage, including health care literacy programs.
Customer Privacy and Technology Standards	HC0303-13	Description of legal and regulatory fines and settlements related to Health Insurance Portability and Accountability Act of 1996 (HIPAA) Privacy and Security Rules violations or The Health Information Technology for Economic and Clinical Health (HITECH) Act violations. Dollar amount of fines and settlements and a description of corrective actions implemented in response to events.
	HC0303-14	Discussion of implementation of technology and management standards to maintain security, privacy, and availability of customer data. Number of breaches of customer data security, including the number of HIPAA-mandated breach notifications.
Climate Change Impacts on Human Health	HC0303-15	Description of the strategy to address the effects of climate change on business operations and how climate change is incorporated into risk models. Discussion of specific risks presented by changes in the geographic incidence, morbidity, and mortality of illnesses and diseases.

APPENDIX IV: Analysis of 10-K Disclosures | Managed Care

The following graph demonstrates an aggregate assessment of how the top ten companies in the managed care industry are currently reporting on material sustainability issues in the Form 10-K. The analysis was completed prior to the finalization of the issues, so the graph does not reflect disclosure on all issues.



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