

**ENHANCING PROFITABILITY THROUGH PAYER, PRODUCT,
AND PRICING STRATEGIES**

BDC ADVISORS, LLC POINT OF VIEW

Managed Care Contracting departments in most Care Delivery Systems have developed strong tactical interfaces with payers. However, a need exists to elevate decision-making around managed care business to address broader strategic issues critical for successful participation in managed care, including:

- Market positioning
- Physician network design
- Clinical integration
- Pricing strategy

Significant opportunities exist to increase revenues through thoughtful, multidisciplinary, and strategic approaches to managed care participation. Therefore, Care Delivery System Senior Management Teams should reexamine overall payer, pricing, and product strategies.

Presented herein is an illustration of an integrated Care Delivery System located in a mature managed care market that executed a disciplined managed care strategy which increased managed care revenues by 17% to 22% over a two year period. This new strategy improved profitability, market share growth, and data interfaces with payers and reduced inpatient days.

ILLUSTRATIVE CASE EXAMPLE¹

Actions

- Reduced number of commercial contracts to three plans
- Reduced number of Medicare Risk contracts to one plan
- Developed new non-risk commercial product with one payer
- Renegotiated all existing HMO and PPO contracts
- Reduced or eliminated pharmacy risk and out-of-network risk from all contracts
- Launched clinical differentiation strategy
- Limited provider panel for risk contracts
- Implemented budgets for all contracts
- Returned to shared risk arrangements with several health plans
- Tightened medical management processes
- Adjusted physician compensation under risk contracts
- Established contractual performance benchmarks for information reporting



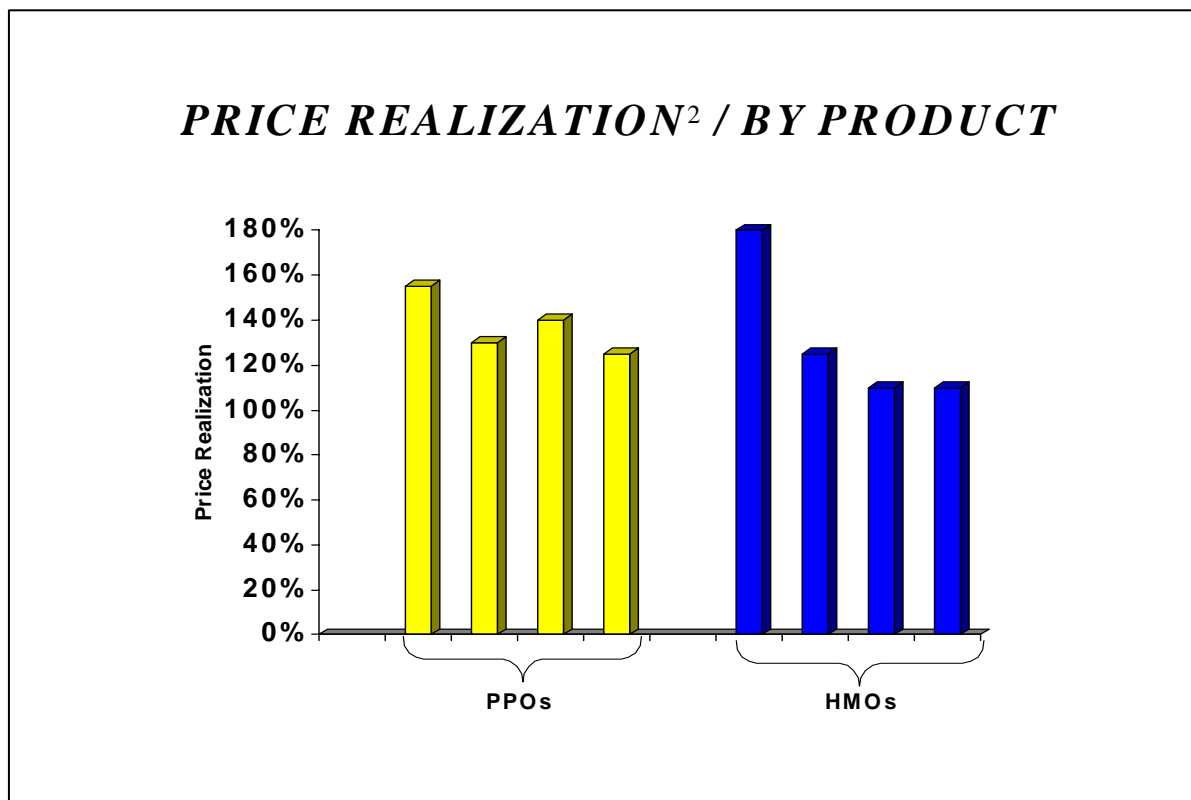
Impact

- Introduced pricing discipline in market
 - 22% increase in reimbursement on commercial business
 - 17% increase in reimbursement on Medicare Risk business
 - 9% price increase in all non-risk contracts
- Expanded market share in commercial segment
- Influenced evolution of managed care products within market
- Introduced pricing discipline in market
- Supported differentiation between risk and non-risk products in market
- Incentivized utilization management
- Reduced inpatient utilization by 10% to 15%
- Improved data interface with health plans
- Provided physicians with the information required to manage “at risk” enrollees

¹ Illustrative case example represents a composite of BDC Advisors, LLC client experiences from markets and systems in western, midwestern, and eastern states.

BACKGROUND

Physician Hospital Care Delivery System (“PHCDS”) operates in a consolidated, highly penetrated managed care market that is served by a number of provider systems and several major payers, including a Blue Cross plan and several for-profit health plans. Over 40% of the commercial population is enrolled in a managed care product, and over 20% of the senior population is enrolled in a Medicare Risk product. Prior to execution of a new managed care strategy by PHCDS, there was limited distinction (from the consumer perspective) between the HMO and PPO product benefits. Further, as shown below, limited variation in pricing existed for HMO and PPO products.



PHCDS COMPETITIVE POSITION AND ORIGINAL STRATEGY

PHCDS occupied a competitive market position between a low-cost provider system and a high-end provider. In order to maintain and grow market share, PHCDS adopted a strategy to

² Price realization is a comparative measure of performance against Medicare FFS reimbursement. For example, a DRG payment would equal 100% of Medicare FFS reimbursement. All payer contracts were normalized as a percentage of Medicare FFS reimbursement in order to complete the price realization analysis.

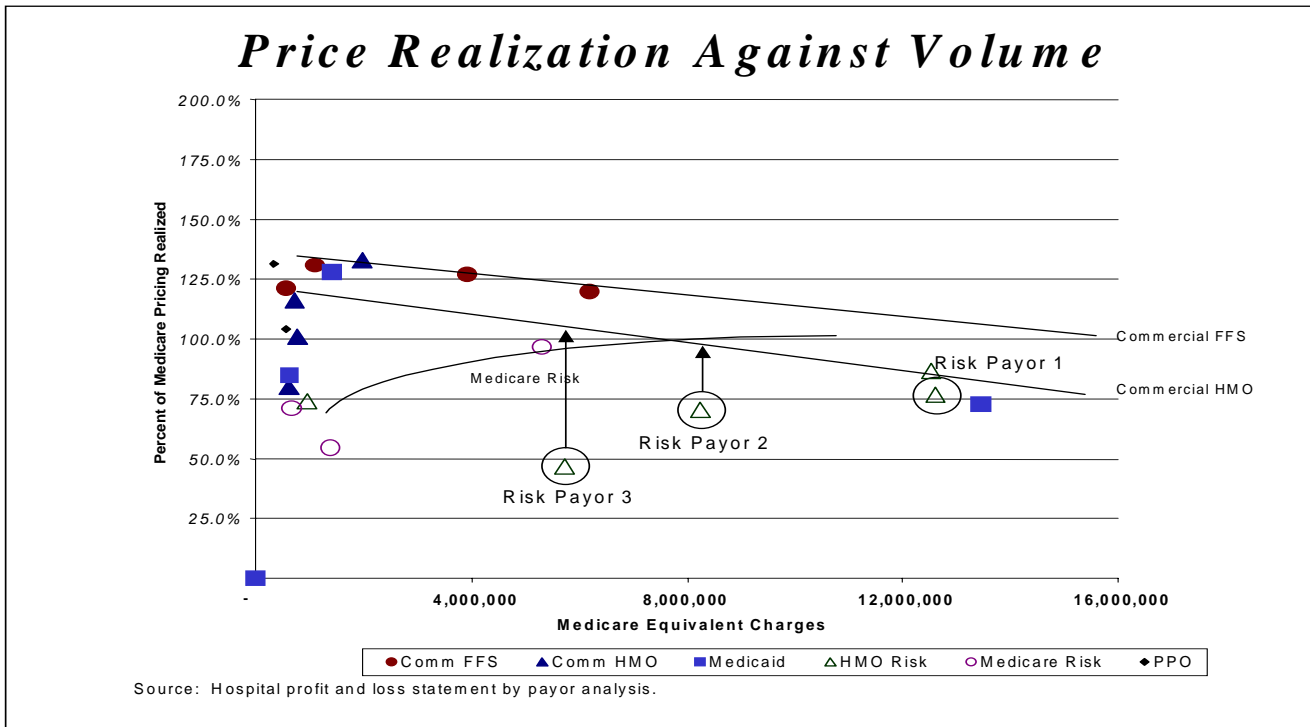
compete on the basis of cost with the low-cost competition. The strategy involved accepting and managing globally capitated “at-risk” products. An extensive physician education program was developed and launched. Simultaneously, reimbursement, risk sharing, care delivery, and data monitoring and reporting systems were developed and implemented. Within a short time, PHCDS was responsible for managing over 100,000 enrollees through several “at risk” commercial contracts. Unfavorable financial performance resulted.

INTERNAL DIAGNOSTIC PROFILE

PHCDS identified the need to complete a diagnosis of its performance under the above strategy and identified the following results:

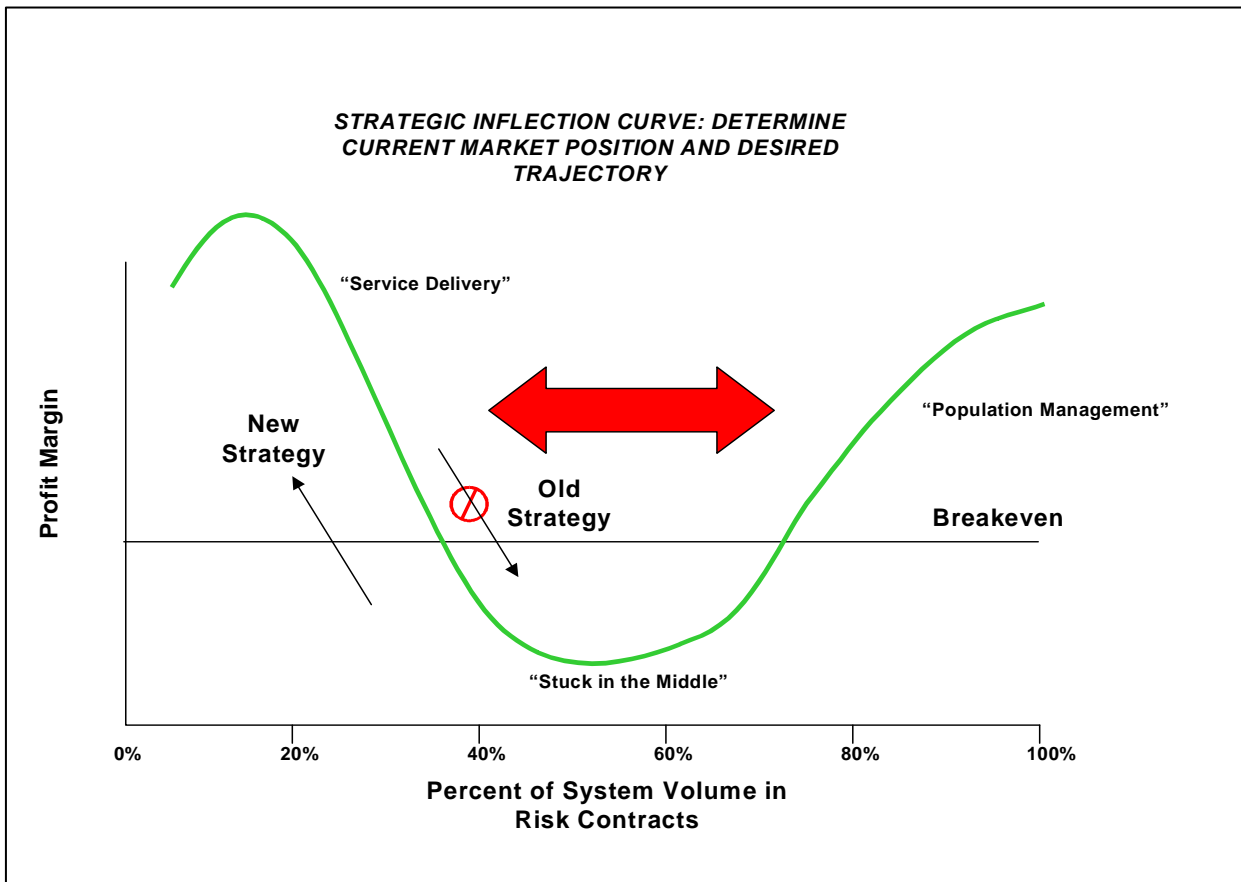
Performance Driver	Finding
Health Plan Contractual and Operational Relationship	<ul style="list-style-type: none"> • Poor match of rate and benefit design on most contracts • Non-performance by health plans related to non-delegated services • No penalties to health plans for non-performance of non-delegated services • Acceptance of risk by PHCDS with no ability to manage
Network Design	<ul style="list-style-type: none"> • Broad network (PHO structure) for all products
Reimbursement and Risk Sharing Systems	<ul style="list-style-type: none"> • PCP capitation with withholds • Specialist fee-for-service with withholds • Hospital per diems
Care Delivery Systems	<ul style="list-style-type: none"> • Strong performance for in-network providers • Extensive out-of-network (in-area) leakage • Heavy pharmacy losses
Data Monitoring and Reporting Systems	<ul style="list-style-type: none"> • Untimely, inaccurate health plan reporting • Strong internal database systems under development

PHCDS also analyzed its price realization for individual contracts against the revenue of each contract. Deep discounting was being provided for HMO products, despite the lack of product differentiation from PPO products. Additionally, opportunities for improved pricing discipline were identified. For example, several small PPO health plans were receiving high discounts for minimal volume. Furthermore, it became apparent that health plans that were delivering higher price realization were being disadvantaged in the market by the deep discounting that was being offered to HMOs.



MANAGING MARKET EVOLUTION

As shown in the diagram, PHCDS determined that under its present volume of at-risk business, it was achieving suboptimal financial performance. PHCDS determined that it could profitably manage at-risk contracts, but doing so would require the aggressive conversion of most of its volume to risk (and, consequently, supporting market conversion to risk) and an aggressive reduction in fixed costs. Since neither condition for profitability was deemed feasible, PHCDS determined to revise its strategy and move volume back to non-risk reimbursement through the series of actions identified at the outset of this article.



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For additional information on Payer, Product, and Pricing Strategies, please contact Rick Wesslund at (415) 247-1030 or via electronic mail at rwesslund@bdcadvisors.com.