

Insurance Industry News

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HMO Regulation Update

Elsewhere in this month's edition we focus on the managed care industry and its struggle with costs and an aging population. Our managed care friends, and in particular HMO's, now face increasing scrutiny by regulators such as the National Association of Insurance Commissioners (NAIC).

The NAIC released data last summer, which, although just a little self-serving in tone (as they stress the need to exercise their duty to protect us all from the big bad HMO's), contains information of interest to all those who follow the development of managed care in the U.S. We've summarized some of this important information below.

1998 NAIC Statement Changes

Those HMO's that file with NAIC will need to file their "blanks" differently in the future, with respect to two important points:

(a) Investment Schedules: Schedules A through DB have been added to the HMO statement to make it more consistent with statements filed by life/health and property/casualty insurers. These schedules will allow more detailed reporting regarding the purchase or sale of investments throughout the year.

(b) Risk-Based Capital Requirements: New exhibits have been added to record underwriting information and to re-capture data according to risk-based capital calculations. (Beginning with year-end 1998, HMO's will be required to complete the "Managed Care Organizations Risk-Based Capital Formula." During the past few years the NAIC has urged HMO's to complete sample formulas in order to assist in the development of an industry-sensitive formula and set of guidelines.)

Size of the Market

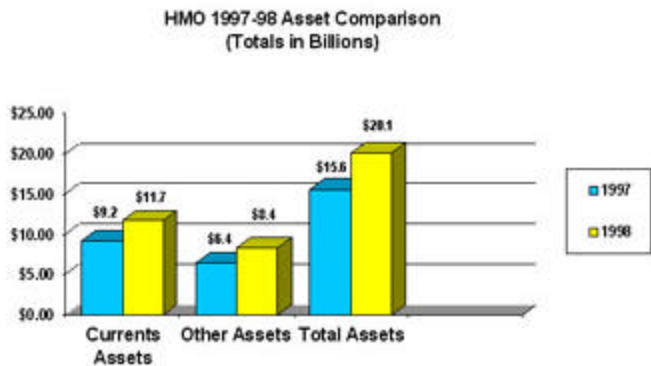
According to the NAIC data for 1998, the 481 HMO's which filed NAIC annual statements now represent a significant national data profile. (It's also important to note that currently not all HMO's file annual financial statements with the NAIC.) We've excerpted some of this information, which we think may be of interest to Mason's directors.

The following chart provides an asset comparison using 1997 and



HMO's and Regulators -- Keeping Track of the Numbers

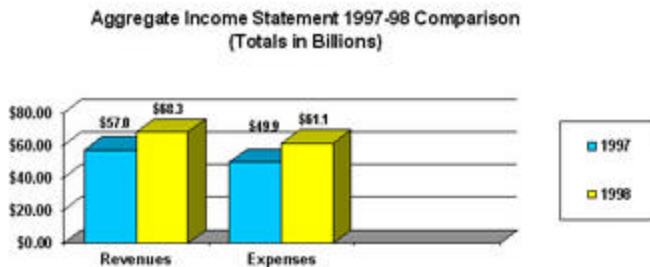
1998 data for these 481 HMO's, in three key areas.



With regard to the aggregate liabilities of this group of 481, we see a market continuing to develop conservatively, and with increases in net worth.



When we look at an aggregate income statement for this group of 481, we perhaps begin to see the reason for the need for upward rate action in many states. We also begin to see, I think, the impact of losses from such areas as the Medicare business and other initiatives which HMO's have recently undertaken, with varying degrees of success.



Well, so far, so good. However, what's not included in these numbers is a \$700 million collective industry net loss in 1997 among these 481 HMO's, which grew to \$1.2 billion in 1998, and is predicted to exceed \$2 billion in 1999 for this same group. With regard to the issue of profits, we believe that the systematic assault, state by state, on the ERISA pre-emption for HMO's will force some organizations to assume larger retentions or deductibles for professional and other liability insurance coverages in order to keep the cost of these coverages down; and that this fact, coupled with expected consumer and legislative assaults in the areas of patient rights and quality of care, is going to make it more expensive to operate an HMO in the future. What's becoming clear though, is that on a combined basis, the NAIC data points to a product which, in general, is underpriced. This is, of course, a serious problem in any business.

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