Under the microscope

Powerful BlueCross BlueShield faces new challenges in changing health-care environment

"We're an in-state not-for-profit and one of the few that operates in a single state in the country. We have no interest to do anything else than be a not-for-profit"

— Ron Harr, BlueCross BlueShield VP

By KEITH RUSSELL
Staff Writer

CHATTANOOGA — For many of Steven Lawrence's customers, BlueCross BlueShield of Tennessee is to health insurance "what Kleenex is to facial tissue."

In other words, synonymous.

"I have lots of examples of people who, instead of asking, 'Who is your insurance with?' will ask, 'Who is your BlueCross and BlueShield with?' " said Lawrence, a health benefits consultant with the Gallatin-based firm W.E. Shaw & Associates. "There is definitely name recognition."

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▶ BlueCross BlueShield generates strong feelings, postive and negative.
On 4E

That recognition has followed Tennessee's BlueCross franchise for most of its history. Nearly 60 years after being founded in this city on the banks of the Tennessee River, BlueCross today provides four out of every 10 Tennesseans with commercial health insurance. A similar percentage of enrollees in TennCare, the state's health-care program for the poor, disabled and previously uninsured, have ID cards bearing the company's well-known cross and shield logos.

As BlueCross has learned in recent months, however, being the state's largest health insurer can attract a similar-sized share of scrutiny.

Since December, BlueCross has become embroiled in two high-profile contract disputes affecting the health benefits of hundreds of thousands of its Midstate customers. First, the insurer on Jan. 1 parted ways with a dozen hospitals in Middle Tennessee and the Chattanooga area owned by Nashville-based HCA Inc., the nation's largest for-profit hospital chain. Then on Feb. 14, the insurer saw a contract expire with Radiology Alliance, Nashville's biggest radiology practice and sole provider of radiology services at Saint Thomas and Baptist hospitals.

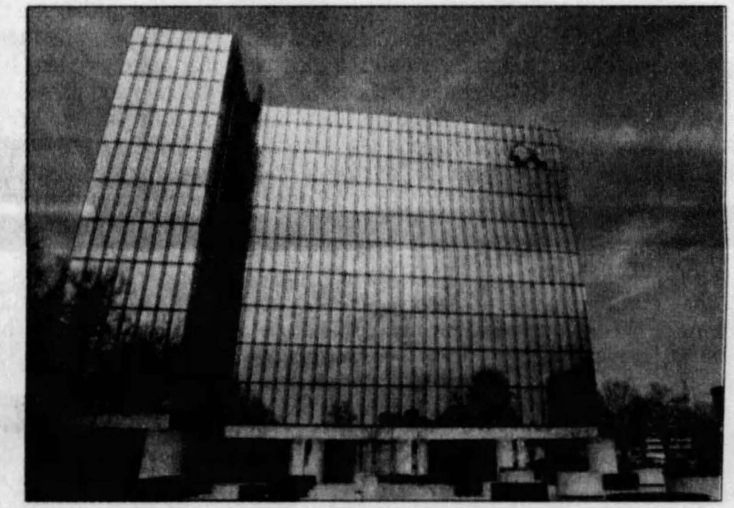
Neither dispute has caused any significant defections among its health plan customers. In fact, the company last week announced a 4.2% net growth in enrollment for the month of January among its commercial plans.

Nevertheless, the disputes have put BlueCross on the defensive.

Shortly after news broke of the contract dispute with Radiology Alliance, BlueCross quickly arranged a 60-day extension and promised to resume negotiations. The spat centers on the prices and terms under which BlueCross pays the practice to treat its health plan members.

On Thursday, meanwhile, BlueCross announced it would be open to mediation of its bitter dispute with HCA, which also

▶ Please see **BLUE, 4E**



BlueCross BlueShield has its headquarters in Chattanooga.

BlueCross BlueShield of Tennessee

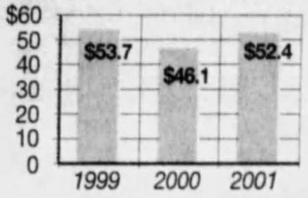
Headquarters: Chattanooga
Founded: 1945
Employees: 4,220
CEO: Vicky Gregg
Annual revenues (2001): $3.9 Billion
Commercial health plan members: 1.73 million

By the numbers

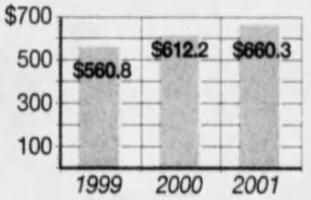
BlueCross BlueShield of Tennessee has managed to maintain its financial position as plan members faced double-digit premium increases in recent years.

Revenues *(in billions of dollars)*

Net income *(in millions of dollars)*

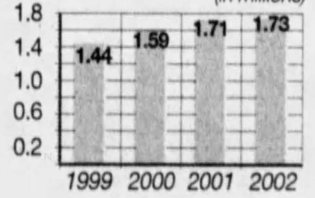


Reserves *(in millions of dollars)*



Commercial health plan members

(in millions)



SOURCE: BlueCross BlueShield of Tennessee

KENT TRAVIS / STAFF

Blue: Health insurer facing new challenges

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centers primarily on financial issues. HCA officials quickly said they too were open to the idea, though both sides were vague on details.

In interviews, officials with each company have said they believe the other side was more interested in making a point during the well-publicized impasse than they were in reaching a compromise. HCA officials contend BlueCross has singled out the company to show its members it is "doing something" about its rising premiums. BlueCross officials, in turn, question whether HCA was flexing its muscles to impress Wall Street of its ability to gain concessions from insurers, a strategy the company frequently highlights in its financial reports.

"When I talked with HCA, I never felt I was able to generate any common ground with them," said Vicky Gregg, BlueCross' recently appointed chief executive officer.

Even on this point, there is disagreement. "I thought we did have common ground," Paul Rutledge, president of HCA's Mid-America division, said when told of Gregg's remarks.

In many ways, health policy experts say Blues disputes with HCA and Radiology Alliance are part of a nationwide trend of increased tensions between insurers and health-care providers.

"It's not a thing exclusive to BlueCross," said Paul Ginsburg, president of the Center for Studying Health System Change, which two years ago began tracking such contract disputes.

BlueCross officials say the disagreements are the result of a multi-pronged effort to stem double-digit premium costs increases for their customers. Regardless, the disagreements have shined new light on an organization whose portrait is a study in contrasts.

Profitable not-for-profit

BlueCross BlueShield of Tennessee was conceived in 1944 by Roy McDonald, a Chattanooga civic leader and publisher of the *Chattanooga News-Free Press*, as a way to help pay for his employees' medical expenses. With McDonald's efforts, Tennessee joined a growing number of states in forming BlueCross and BlueShield health plans. Today, there are 43 organizations nationwide who belong to the national BlueCross and BlueShield Association, providing coverage to approximately 84 million Americans.

Growth has been a hallmark of Tennessee's BlueCross since its inception. Within its first year, the organization grew across the state to cover 105,000 members. Subsequent decades would see BlueCross build sizable market share in every Tennessee county, culminating with the Chattanooga organization's 1996 merger with BlueCross BlueShield of Memphis.

The growth has been to the benefit of the city of Chattanooga, where BlueCross employs 3,700 of its more than 4,200 statewide employees. The workers are spread among eight different sites around Chattanooga, including six downtown.

Nationally, each of the Blues operate independently of one another but are licensed by the national organization to ensure they meet certain quality and financial standards. They work cooperatively, however, agreeing to make their own provider networks available to other out-of-state BlueCross plans. The result is an expansive network insurance brokers say is especially attractive to large employers with multi-state operations.

Otherwise, the companies can differ widely, in geographic reach and corporate form. Recent years have seen a number of BlueCross plans across the country convert to for-profit status, partly to shore up dwindling cash reserves. Many of them have then sought to expand into other states. It is a tact Tennessee's BlueCross won't be following.

"We're an in-state not-for-profit and one of the few that operates in a single state in the country," said Ron Harr, Blue vice president in charge of government programs, including TennCare. "We have no interest to do anything else than be a not-for-profit."

At the same time, BlueCross officials are quick to point out two important ways they greatly differ from most not-for-profits. First, unlike not-for-profit hospitals, which are tax-exempt, BlueCross pays state and federal taxes. In 2001, the company paid more than $89 million in taxes, according to its annual report for that year.

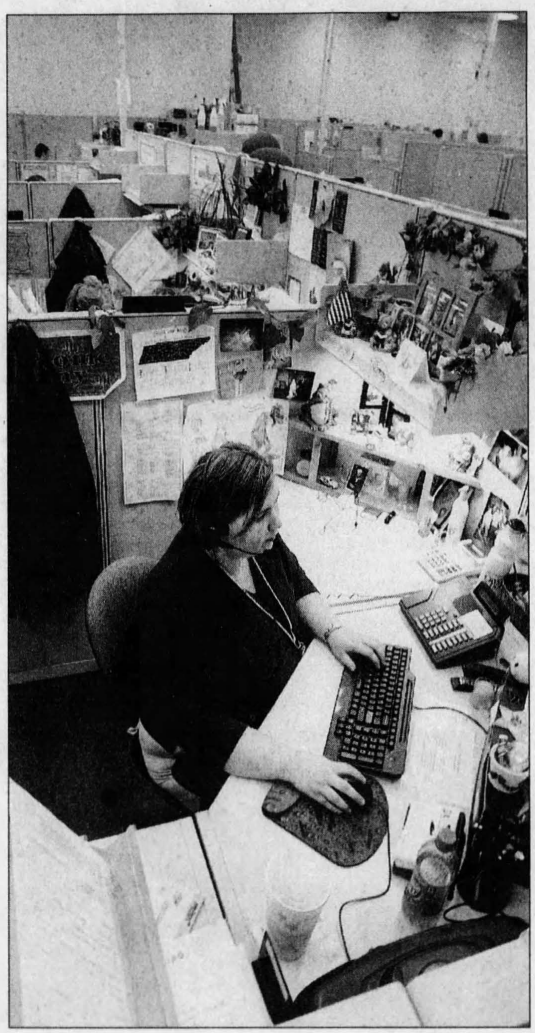
Second, the state law that created the local BlueCross included language requiring the company to maintain a 2.5% profit margin as reserves.

At the end of 2001, that "legally required reserve" had grown to $403 million. But BlueCross' actual reserves are much higher than that — $660 million at the end of 2001. They are the result of continued strong financial results that have seen BlueCross post net income of at least $50 million each year from 1999-2001. The company has yet to report its 2002 financial results, but officials say they expect profits to fall within a similar range.

Some providers have questioned the need to keep such reserves. But David Deal, BlueCross' chief financial officer, said the reserves ensure the company's financial stability. Besides serving as a sort of rainy day fund, it allows BlueCross to avoid borrowing money to fund capital expenditures — the company has zero long-term debt. Deal also notes that on a per-member basis, BlueCross' reserves are actually lower than they were 10 years ago.

Provider conflicts

The not-for-profit status does not keep BlueCross from competing as fiercely as its for-profit counterparts, said Gregg, who previously served as a top executive at Humana, the Louisville-based for-profit insurer.



GEORGE WALKER IV / STAFF

Jennifer Seay talks with a client at the BlueCross BlueShield headquarters in Chattanooga.

She said the differences between a not-for-profit such as BlueCross and a for-profit can be subtle and have more to do with ultimate goals than how those objectives are reached.

"There are similarities and there are differences," Gregg said, noting that a publicly traded insurer's primary obligation is ultimately to its shareholders. "That does drive a lot of things you do day in, day out," she added of for-profit status, drawing from her experience at Humana.

Even so, many providers caution against developing warm and fuzzy notions about BlueCross. Rather, they tell of a company that uses its considerable market power to force its will on doctors and hospitals.

"They are at a point where they don't have to negotiate with anybody," said Dr. Charles Eckstein, president of Urology Associates, one of Middle Tennessee's largest urology practices.

"The only people that have had success in two-way negotiations with them are the larger groups," Eckstein said. "And if BlueCross BlueShield can say no to HCA, they can say no to anybody. I think that troubles a lot of physicians and hospitals."

The strength of BlueCross can be seen in what has happened with programs for the state of Tennessee and Metro government in recent weeks.

Both governments have allowed thousands of their employees to switch to another insurance carrier in light of the HCA dispute. Still, the majority has stuck with BlueCross. Of 19,000 state employees with BlueCross insurance who live near one of HCA's Tennessee hospitals, state officials say only 280 have switched. Metro government officials say they expect only about 100 of 7,200 employees on BlueCross to move to an alternative HMO plan.

"At first there was a real surge of interest," said John Kennedy, Metro's assistant director of human resources, "because people weren't sure if this affected their relationship with their doctor.

"Once people understood what it really meant," Kennedy said, "it took some (wind) out of the sails."

Steven Coulter, BlueCross' chief medical officer, conceded that the insurer will inevitably pay more attention to larger provider groups, given their importance in maintaining a large-scale provider network. But he said such attention has little influence on the actual prices BlueCross seeks from its providers.

"From our perspective, what's fair for the goose is fair for the gander," Coulter said.

Many doctors have hard feelings these days about most insurance companies, said Russ Miller, spokesman for the Tennessee Medical Association. The organization last year filed a lawsuit against several insurance companies, including BlueCross, accusing them of "physician profiling," or penalizing doctors who provide treatment the companies believe might not be necessary. The companies also are accused of using computer programs to automatically reduce or reject some claims submitted by physicians.

BlueCross has denied the allegations and said it uses computer programs only to make sure claims are being paid properly, not to avoid paying them.

"That lawsuit came out of frustrations about insurers in general," Miller said. "BlueCross happened to be a target because they're the biggest."

At the same time, providers compliment BlueCross for its efficiency and ability to pay claims promptly.

In a recent TMA survey, BlueCross scored among the highest in terms of doctors' preferences among insurers.

"It's kind of a love-hate relationship," said Craig Becker, president of the Tennessee Hospital Association. "They love them because probably in terms of efficiency and paying bills on time they are one of the better ones. They hate them because they try to come in and beat hospitals down on rates."

Affordability concerns

As for the recent contract disputes, Becker attributes them primarily to lower payments to providers from government programs, particularly TennCare. He says the payments don't come close to covering providers' costs, so they are forced to seek increased payments from commercial insurance plans to make up the difference. The practice is known as cost-shifting.

"That's driving this more than anything else," Becker said. "They've got to cost-shift these dollars over, and hospitals have nowhere else to go but BlueCross."

BlueCross officials say they are sympathetic to providers' plight but point out that they confront their own pressures — from commercial health plan customers who can no longer afford rapidly rising insurance costs.

"This is not fun," Coulter said of the tougher talks with providers such as HCA. "We're trying to do what our customers want us to do, which is help control health-care costs."

Such costs have forced BlueCross, along with most other health insurers, to raise its premiums by double-digit rates since 1999. Buddy Shaw, Lawrence's business partner at broker W.E. Shaw, said such rising costs are at the forefront of employers' concerns.

"Holding the line on premiums is the main issue with employers," Shaw said.

The trend in premiums prompted BlueCross to investigate the exploding costs behind the increases in a series of white papers released last year. The papers cited cost-shifting as a key contributor, but noted several other factors as well, including increased utilization, rising drug costs, technology improvements and a rise in the mix of more costly treatments, such as having an MRI performed as opposed to a less expensive X-Ray.

In light of these findings, Coulter and other BlueCross executives say their approach to making health-care more affordable is being fought on multiple fronts. They include statewide ad campaigns designed to help consumers better understand how they can control health-care costs. The company has also introduced new features to its plans, such as tiered prescription drug benefits, that require members to pay more for choosing more expensive types of treatment.

Discussions with some providers also are more complex than the tough negotiations with HCA and Radiology Alliance might indicate. BlueCross is working with Vanderbilt Medical Group to find ways to reimburse its doctors for holding down costs while simultaneously improving patient outcomes. The initiative is designed to find a way to restructure the present fee-for-service compensation system for doctors, which Coulter said provides no incentives for doctors to hold down costs.

"The whole notion is let's try to get our incentives aligned," Coulter explained.

Dr. John Sergent, Vanderbilt's chief medical officer, said the two sides are still trying to agree on how that can best be done. But he said the efforts show him that patient care is a priority to BlueCross.

"Don't get me wrong, when they are on the other side of the table from you, they are very tough negotiators. There's no question about that," Sergent said. "On the other hand, I believe they have people there who are truly interested in improving the quality of care." ■

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