

IN THE NEWS

Insurance Companies Look To Mergers To Remain Viable



JAN 26, 2011 — *Curt Nickisch*

In his State of the Union address, President Obama reiterated his goals for national health care reform. That new law is already playing out here in Massachusetts, where Tuesday two of the state's largest health insurance companies said they are looking at merging.

In their joint statement, Harvard Pilgrim Health Care and Tufts Health Plan talked about the cost of government mandates — translation: national health care reform. The new law caps insurance company spending.

"Meaning for every dollar they take in, 80 cents has to be spent on medical costs and only 20 cents can be used for profit and administration," said Steve Zaharuk, senior vice president at the rating company Moody's.

Zaharuk analyzes health insurance companies nationally, and says that 80/20 ratio is just one economic pressure coming from national health care reform. There's also the mandate to go to electronic health records.

"They have to update all their equipment to handle that, and that's a big investment of capital. And so some of these smaller companies really just can't afford it, so it's

almost forcing them to look to mergers or other partnerships to absorb that cost," Zaharuk said.

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National health care reform is not the only economic force pressuring insurance companies. They are increasingly squeezed on one side by consumers, who want to keep premiums and co-payments low, and on the other side by doctors and hospitals, who keep charging more and more. The economy hasn't been great either. When people lose their jobs, they lose their employer health plans.

So that's also why Harvard Pilgrim and Tufts Health think they are better off by merging. But consolidation is an unintended consequence of the new national health care law, Zaharuk said.

“Well, clearly, one of the tenets of health care reform was to increase competition,” he said.

And that’s not what would happen here with a merger.

“I don’t like the news,” said Chris Nadeau, who works for William Gallagher Associates, a company that represents employers as they buy health care coverage from these insurance companies.

But Nadeau thinks it’s inevitable. So until now, Nadeau has been able to go shopping around between the state’s three biggest insurance companies, Harvard Pilgrim and Tufts, and also Blue Cross Blue Shield Massachusetts.

“And I think having three markets has kept the carriers pretty aggressive and pretty competitive for the most part,” he said.

On the one hand, Nadeau’s worried about going from three big players to two, leading to less competition. But here’s why he thinks it may still help his clients: Nadeau knows that most of their money gets used by insurers to pay hospital and doctor bills. And so his best chance to keep those bills down is to have a strong insurance company that can negotiate good rates.

And they’ve often been hit by a hardball tactic, when a hospital threatens to drop an insurance company if they won’t pay them what they want. Nadeau said that’s harder to do when the insurance company is bigger.

“If they’re threatening to walk away from Tufts Health Plan with 750,000 members, that’s less painful for them if they walk away from a combined Harvard/Tufts that has 2 million members. So that just gives them more leverage at the table.”

And the more leverage the insurance company has, the more they can save customers like you and me.

So that’s the key question facing regulators who have to approve any merger. Is the consumer better off with a stronger insurance company? Or better off by having competition between more insurance companies?

Barbara Anthony is the Massachusetts Undersecretary for Consumer Affairs and Business Regulation, and she’s noncommittal on these questions.

“We will be looking to ensure that the merged company will further the interests of consumers in the health care marketplace in Massachusetts,” Anthony said. “And of course we’ll be looking to see whether that merged company is solvent and whether it is able to handle the needs of its current and future policy holders.”

“It’s a fine a line. I’m sure it’s going to be an interesting discussion the regulators will have,” Zaharuk said. “Bottom line is I’d rather have one less company but a stronger one, versus two weak ones. That argument might win the day.”

If it does, expect more of the smaller insurance companies to follow suit. After all, players like Fallon Community Health and BMC HealthNet are in the same boat with Harvard Pilgrim and Tufts Health Plan. They all face the same economic pressures, from national health care reform and from consumers who want to fight the rising cost of health care.

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Christopher Nadeau is a Principal at William Gallagher Associates (WGA) and head of the Employee Benefits Group. Mr. Nadeau has been a key figure in growing the practice to a strong organization of 50 employees with over 400 clients, and maintaining consistent annual growth. Mr. Nadeau counsels his department to develop and redesign employee benefits programs to match the corporate philosophy, long-term needs and objectives of their clients. He is also an industry leader on Healthcare reform and the cost impact and administrative burden on employers. He can be contacted at cnadeau@WGains.com or 617.640.0351.