REPORT OF THE COMPTROLLER GENERAL OF THE UNITED STATES

Analysis Of Variations In Claims Processing Costs Of Fiscal Agents For The Civilian Health And Medical Program Of The Uniformed Services

Department of Defense

Wide variations exist in claims processing costs under cost-reimbursable contracts because of differences in administrative costs charged to the program, productivity and wages of claim processors, claim volumes, and other factors. Claims processing costs are higher than for Medicare and Medicaid partly because of smaller claim volumes, a complex claim form, and frequent program changes.

Corrective action is in process for the Civilian Health and Medical Program of the Uniformed Services, such as consolidation of fiscal agent operations to obtain benefits of large volume operations and use of competitively bid fixed price contracts. These and additional actions should be required under any new federally sponsored health insurance program to maximize performance and minimize claims processing costs of fiscal agents.

HRD-77-93

JUNE 8, 1977

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-133142

The Honorable Henry Jackson, Chairman
Permanent Subcommittee on Investigations
Committee on Governmental Affairs
United States Senate

Dear Mr. Chairman:

This report is in response to the Subcommittee's request of July 1, 1976, for a review of fiscal agents' variations in claims processing costs under the Civilian Health and Medical Program of the Uniformed Services. The report identifies the major reasons for the cost variations and identifies some factors, other than basic program differences, that cause claims processing costs for this program to be higher than those for Medicare and Medicaid.

In requesting this study, the Subcommittee suggested that the program's experience could serve as a model for a larger issue. We believe that the experience the Department of Defense has gained in working with this program's fiscal agents provides some important lessons for the future. Accordingly, the report contains recommendations to the Congress on specific actions that should be required under any new federally sponsored health insurance program to maximize performance and minimize fiscal agents' claims processing costs.

As your office requested, we did not obtain written comments from the Department of Defense on this report, but the contents were discussed with Department representatives.

Sincerely yours,

Elmer B. Staats

Comptroller General
of the United States

REPORT OF THE
COMPTROLLER GENERAL
OF THE UNITED STATES

ANALYSIS OF VARIATIONS IN CLAIMS PROCESSING COSTS OF FISCAL AGENTS FOR THE CIVILIAN HEALTH AND MEDICAL PROGRAM OF THE UNIFORMED SERVICES
Department of Defense

D I G E S T

From the beginning of the Civilian Health and Medical Program of the Uniformed Services in 1956, cost-reimbursable contracts were used exclusively until 1976 to obtain claims processing services of fiscal agents. Under these contracts, claim processing costs for the period April 1975 through March 1976 ranged from $3.50 to $11.31 a claim for the 44 fiscal agents processing physician claims and from $6.20 to $38.40 a claim for the 53 fiscal agents processing hospital claims. (See pp. 5 to 13.)

The most important reason for these different rates was the amount of fixed costs charged to the program. For example, occupancy costs at one fiscal agent were about $13 per square foot; at another, this cost was about $8 per square foot. Fixed costs ranged from 14 percent to 70 percent of the total per claim cost at the fiscal agents reviewed. (See pp. 20 to 22.)

Other important factors included the

--number of claims returned and rejected,

--rates of productivity,

--methods used to allocate costs,

--hourly wages of claims processing personnel, and

--volume of claims.

Differences in services provided by fiscal agents did not appear to be an important factor in the variances of claim rates. (See pp. 23 to 29.)

HRD-77-93

Generally claim rates were higher than for Medicare and Medicaid, partly because of factors other than basic differences in the programs. The low claims volume for the program resulted in manual processing; the large volumes of Medicare and Medicaid claims were processed with highly automated systems. Complex claim forms resulting in large numbers of returned and rejected claims and frequent benefit changes under the program lowered claims processors' productivity which also caused program rates to be higher. (See pp. 29 to 31.)

In administering cost-reimbursable contracts with fiscal agents, program officials had not established provisions for measuring performance acceptability, and the contracts did not contain incentives for cost control or efficiency. (See p. 35.)

Program officials who visited fiscal agents did not investigate reasons for rate variations. The Health, Education, and Welfare Audit Agency audits the contracts with fiscal agents, but was not assigned specific responsibility to investigate causes for claim rate variations and did not do so. (See pp. 36 and 37.)

Program officials began using fixed-price competitive bid contracts in 1976. These offer opportunities to lower claim rates by giving fiscal agents an incentive to control costs and perform more effectively. While the fiscal agent's performance under the first fixed-price contract proved unacceptable, cost savings and other advantages should outweigh any disadvantages if the competitive bid process is administered effectively. Program officials estimate administrative cost savings of approximately $1.9 million in the first 1-year period for the nine competitive bid contracts in effect as of December 1976. (See pp. 38 to 42.)

The Subcommittee on Investigations believed GAO should study the program's experience since the program could serve as a microcosm

of a larger issue. On the basis of this study's results, GAO recommends that, for any new federally sponsored health insurance program which will need services such as those provided by fiscal agents for the Civilian Health and Medical Program of the Uniformed Services, the Congress require:

--Consolidated fiscal agent operations to achieve large claim volumes and take maximum advantages of economies of scale.

--Simplified claim forms and, to the extent practical, standardized Government health insurance forms.

--Specifically defined program benefits and policies to avoid frequent program changes.

--Use of cost-reimbursable contracts only until reliable information is available on program specifications, fiscal agents' performance, and costs.

--Use of competitive bid fixed-price contracts as soon as reasonably precise specifications, performance data, and reliable cost information are available. (See pp. 43 to 44.)

At the request of the subcommittee, GAO did not obtain written comments from the Defense Department on this report, but the contents were discussed with Defense representatives.

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ABBREVIATIONS

BCA	Blue Cross Association
CHAMPUS	Civilian Health and Medical Program of the Uniformed Services
DOD	Department of Defense
GAO	General Accounting Office
HAS	Health Application Systems, Inc.
HEWAA	Department of Health, Education, and Welfare Audit Agency
OCHAMPUS	Office for the Civilian Health and Medical Program of the Uniformed Services
RFP	request for proposals

CHAPTER 1

INTRODUCTION

The Civilian Health and Medical Program of the Uniformed Services (CHAMPUS) provides financial assistance for medical care provided by civilian sources to dependents of active duty members, retirees and their dependents, and dependents of deceased members of the uniformed services. 1/ The program originated in 1956 with the Dependents' Medical Care Act (Public Law 84-569) and was expanded by the Military Medical Benefits Amendments of 1966 (Public Law 89-614).

CHAMPUS benefits are divided into two categories--basic and handicap benefits. Basic benefits apply to all beneficiaries and cover both inpatient and outpatient medical care, including such services as surgery, hospitalization, outpatient prescription drugs, X-rays, clinical laboratory tests, and psychiatric care. Handicap benefits apply only to spouses and children of active duty members and cover rehabilitative services and care for the moderately or severly mentally retarded or seriously physically handicapped persons.

Costs of care are shared by the Government and beneficiary. For basic benefits, dependents of active duty members pay a total of $25, or $4.10 a day, whichever is greater, for inpatient care; other beneficiaries pay 25 percent of total charges. For outpatient care, there is a deductible of $50 for each beneficiary ($100 maximum deductible for each family) each fiscal year, after which dependents of active duty members pay 20 percent and other beneficiaries pay 25 percent of the remaining charges. There is no limit on the Government payment under the basic program. For handicap benefits, active duty members pay a specified monthly amount, ranging from $25 to $250 depending on the rank of the active duty member, and the Government pays remaining charges up to $350 a month. Any charges exceeding these amounts are the responsiblity of the active duty member.

1/The "uniformed services" are the Army, the Navy, the Air Force, the Marine Corps, the Coast Guard, the commissioned corps of the Public Health Service, and the commissioned corps of the National Oceanic and Atmospheric Administration.

PROGRAM ADMINISTRATION

The program is administered by the Office for the Civilian Health and Medical Program of the Uniformed Services (OCHAMPUS), located at Fitzsimons Army Medical Center near Denver. OCHAMPUS is a field activity under the policy guidance and operational direction of the Assistant Secretary of Defense (Health Affairs).

OCHAMPUS has contracted with fiscal agents to process and pay claims for services provided beneficiaries. The fiscal agents (1) receive, process, and pay claims of physicians, hospitals, and other providers of authorized care, (2) educate the providers of care about the nature, scope, and special features of the program, and (3) assemble cost and statistical information.

Before 1976, all OCHAMPUS contracts with fiscal agents for processing and paying claims were cost reimbursable. Fiscal agents were generally reimbursed for administrative costs on a provisional-rate basis; that is, a specified amount for each claim paid, pending a final determination of the actual administrative costs incurred through audits by the Department of Health, Education, and Welfare Audit Agency (HEWAA). The provisional rates were subject to adjustment by mutual agreement of the fiscal agent and OCHAMPUS. OCHAMPUS required fiscal agents to report costs quarterly to identify any fiscal and operating problems.

For administration purposes, CHAMPUS is divided into hospital and physician components. Hospital claims include inpatient and some outpatient services, such as charges for laboratory work and X-rays done by hospital outpatient departments. Physician claims include claims for prescription drugs and handicap benefits. Claims may be submitted by and payments made to either beneficiaries or providers. In practice, virtually all hospital claims are submitted by the provider while some physician claims are submitted by beneficiaries.

In 1975, OCHAMPUS had contracts with two fiscal agents--the Blue Cross Association (BCA) and Mutual of Omaha--for paying hospital claims. BCA, through subcontracts with 52 Blue Cross plans (hereinafter also referred to as fiscal agents), paid claims in 33 States, the District of Columbia, and Puerto Rico; Mutual of Omaha paid hospital claims in the other 17 States, Canada, and Mexico. OCHAMPUS had contracts with 44 different fiscal agents in 1975 for processing physician claims. These fiscal agents were individual Blue Cross and Blue Shield plans, private insurance companies, and State

medical societies. Fifty-one Blue Cross plans processing CHAMPUS hospital claims also processed claims of institutional providers (such as hospitals and nursing homes) for the Medicare program administered by the Social Security Administration. Twenty-one of the 44 CHAMPUS fiscal agents processing physician claims also processed Medicare physician claims. Twelve of the CHAMPUS fiscal agents also processed Medicaid claims, and 11 of these processed Medicare claims.

In 1976 the Department of Defense (DOD) began converting to fixed-price contracts for processing CHAMPUS claims. The first contract covered a five-State area--California, Arizona, New Mexico, Nevada, and Texas--and was awarded on February 19, 1976, to Health Application Systems, Inc. (HAS). This contract covered processing hospital, physician, drug, and handicap claims. Nine additional fixed-price contracts for processing CHAMPUS claims in 16 States were awarded through November 1976. DOD plans to convert all contracts to fixed-price contracts as cost-reimbursable contracts expire.

CHAMPUS ADMINISTRATIVE COSTS

Administrative costs of fiscal agents and the average cost per claim (claim rate) for processing CHAMPUS claims for fiscal years 1970-76 are shown below:

Fiscal year	Administrative costs	Number of claims	Claim rate
1970	$ 6,352,023	1,299,626	$4.89
1971	10,663,094	1,951,128	5.47
1972	12,853,539	2,275,035	5.65
1973	15,180,372	2,578,040	5.89
1974	17,587,744	2,783,853	6.32
1975	21,582,720	3,166,353	6.82
1976	24,810,705	3,172,103	7.82

Administrative costs for OCHAMPUS (such as salaries) were budgeted at approximately $2.8 million in fiscal year 1976.

Total benefit payments for services provided beneficiaries under CHAMPUS and administrative costs (including OCHAMPUS) as a percentage of benefit payments for fiscal years 1972-76 are shown below:

Fiscal year	Benefit payments	Administrative costs as a percentage of benefit payments
	(millions)	
1972	$387.6	3.8
1973	433.2	3.9
1974	448.0	4.5
1975	a/508.0	4.7
1976	a/528.0	5.2

a/Estimated total costs since all costs for these years are not yet recorded. Costs are allocated to the year in which the medical services were provided rather than the year in which paid.

SCOPE OF REVIEW

As requested by the Permanent Subcommittee on Investigations, Senate Committee on Government Operations, our review was directed at determining the reasons for the wide variances in claims processing rates of CHAMPUS fiscal agents. Data on variances is given in chapter 2, and an assessment of the reasons for the variances is provided in chapter 3. Work was performed at OCHAMPUS (Denver), and at DOD's Office of CHAMPUS Policy and the Defense Supply Service in Washington, D.C. In addition, we visited Mutual of Omaha, BCA, seven Blue Cross hospital fiscal agents, and eight physician fiscal agents. We visited fiscal agents that had significant variations (high and low) in claim rates and volumes of claims processed who also processed claims for the Medicare and Medicaid programs. Fiscal agents visited and their participation in CHAMPUS, Medicare, and Medicaid programs are shown in appendix II.

We obtained information on services provided CHAMPUS and the cost allocation methods used in charging the cost of these services to CHAMPUS. We also identified factors which affected the CHAMPUS claim rate and obtained information on claims processing costs for Medicare and Medicaid for comparison with CHAMPUS. At OCHAMPUS, we obtained statistical information on fiscal agents and reviewed methods used in monitoring their cost and performance. At the Defense Supply Service and DOD's Office of CHAMPUS Policy, we obtained information on fixed-price contracts for processing CHAMPUS claims.

CHAPTER 2

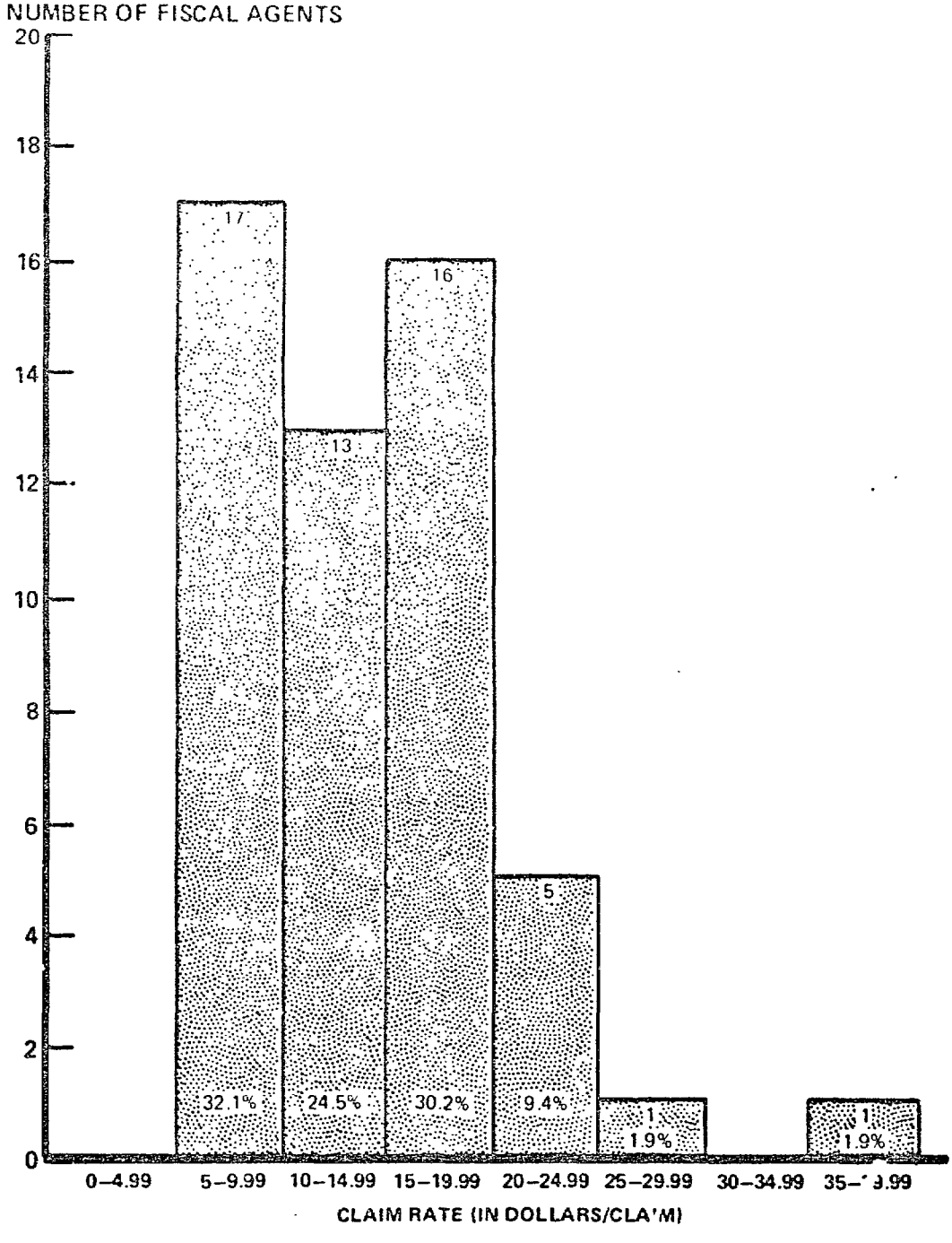
CHAMPUS CLAIM RATES AND VOLUMES VARY WIDELY UNDER COST-REIMBURSABLE CONTRACTS

The administrative costs for processing claims and the volume of claims processed vary widely among CHAMPUS fiscal agents. In addition, when compared to the Medicare and Medicaid rates, the CHAMPUS claim rate for a given fiscal agent is generally higher, partly for reasons other than basic differences in the programs. Further, the claim rate charged CHAMPUS often differs significantly from the average rate for all lines of a fiscal agent's business. The amounts allocated to individual administrative cost categories, such as excutive salaries and beneficiary services, also vary widely among fiscal agents.

HOSPITAL CLAIMS

During the period from April 1, 1975, to March 31, 1976, OCHAMPUS contracted for processing hospital claims with Mutual of Omaha and BCA. Mutual of Omaha handled all processing aspects, while BCA subcontracted with 52 local Blue Cross plans. These local plans processed slightly more than half the approximately 457,000 claims paid during the period; Mutual of Omaha paid the rest. Although both groups processed a similar volume of claims, Mutual of Omaha had a claim rate of $7.11 while BCA's overall claim rate was $16.81. The claim rates of the individual Blue Cross plans ranged from $6.20 to $38.40 with 48 plans having rates higher than Mutual of Omaha. (See app. III.) The following chart shows the distribution of hospital claim rates:

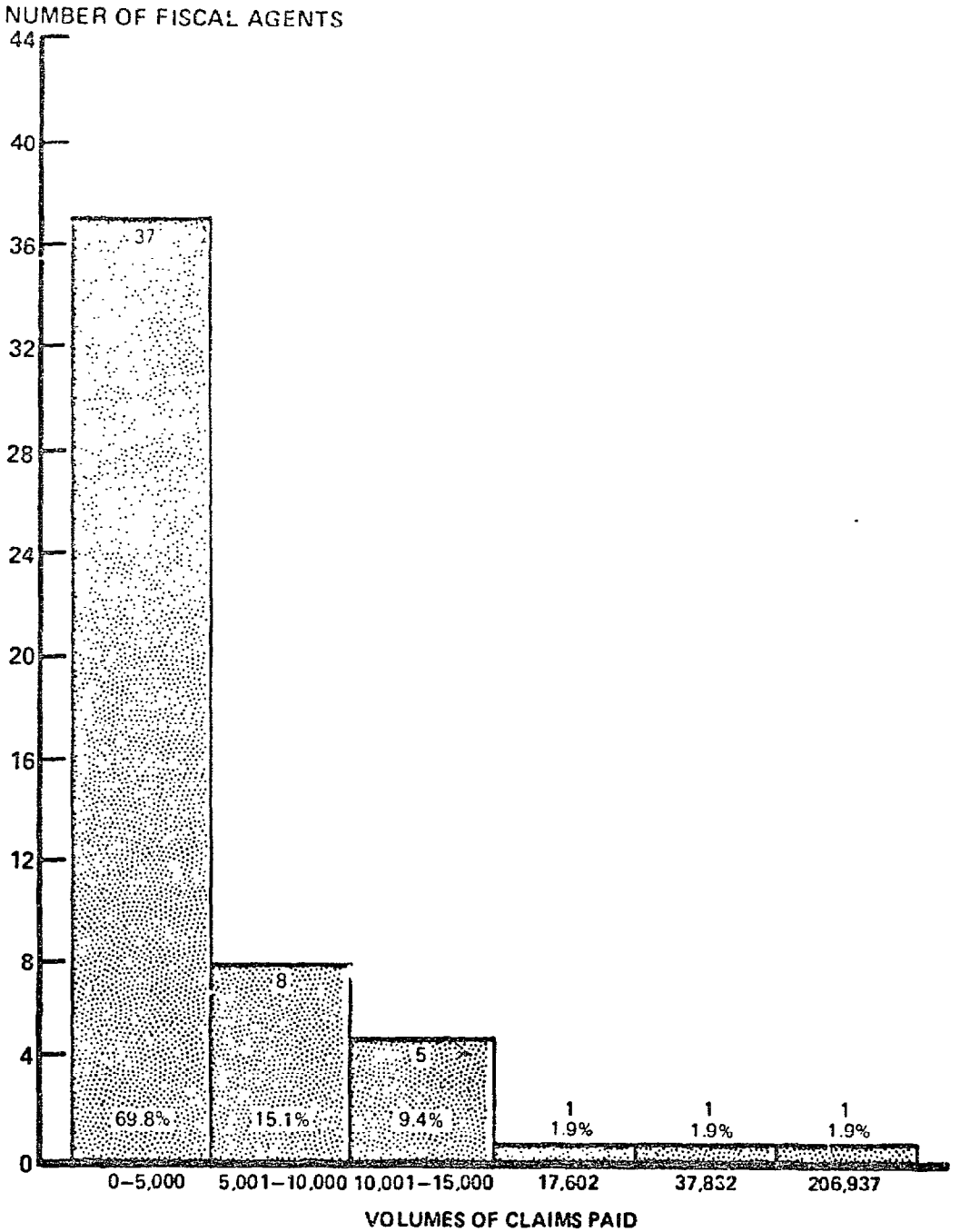
DISTRIBUTION OF HOSPITAL CLAIM RATES



The chart shows that about 87 percent of the hospital claim rates were between $5 and $20, while about 13 percent exceeded $20.

The range of hospital claim volumes, like claim rates, varied widely. Mutual of Omaha processed nearly 207,000 paid claims, while the 52 Blue Cross fiscal agents processed nearly 250,000 paid claims. The volumes for the Blue Cross fiscal agents ranged from 103 to more than 37,000 claims, with an average of 4,792. (See app. III.) The following chart shows the distribution of hospital claim volumes:

DISTRIBUTION OF HOSPITAL CLAIM VOLUMES

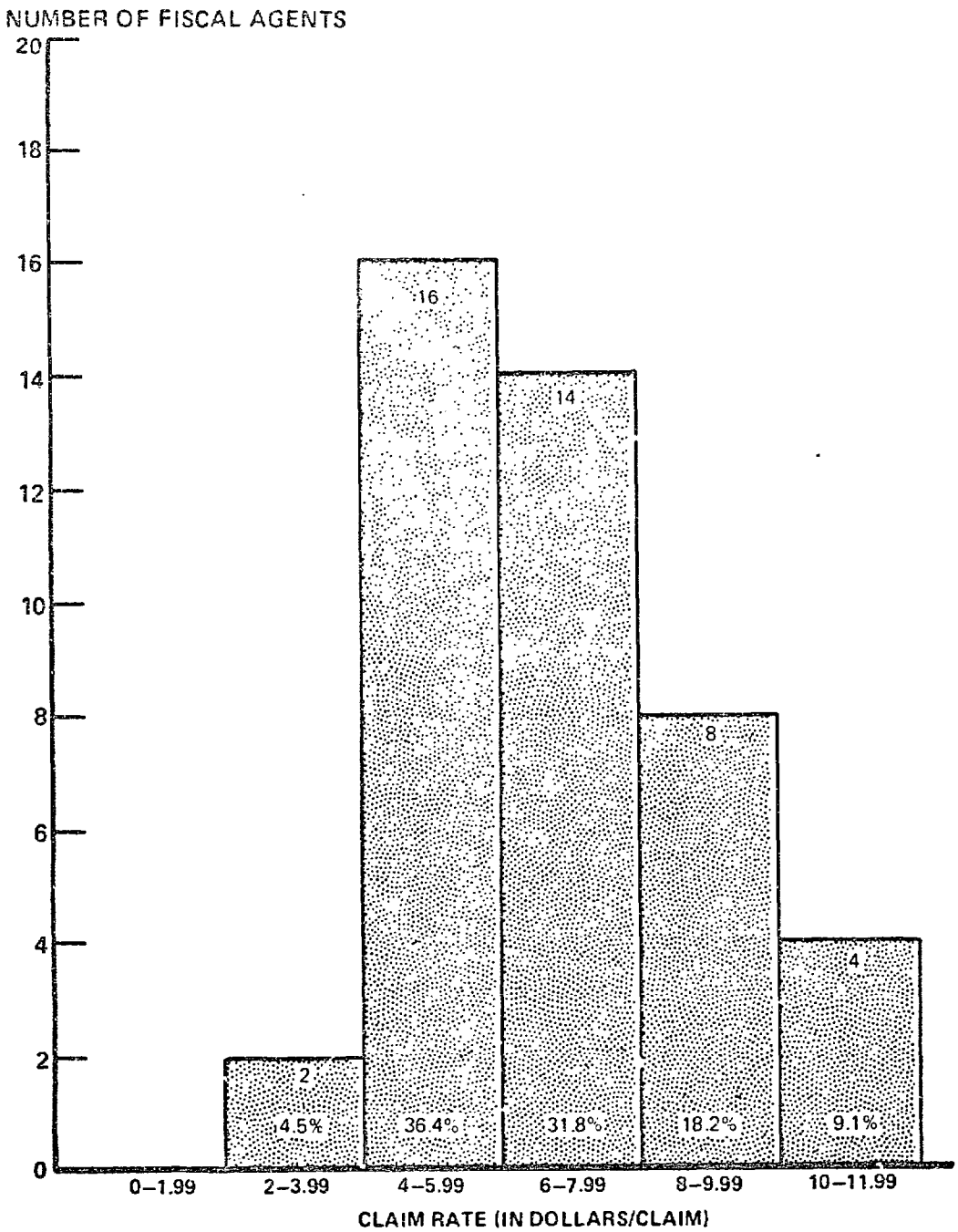


This chart shows that nearly 70 percent of the hospital fiscal agents paid less than 5,001 claims, and less than 6 percent of the fiscal agents paid more than 15,000 claims.

PHYSICIAN CLAIMS

A significant variation also exists in the CHAMPUS physician claim rates and volumes. For the period from April 1, 1975, to March 31, 1976, 44 fiscal agents averaged $6.77 per claim, with a range from $3.50 to $11.31. (See app. IV.) The following chart shows the distribution of physician claim rates:

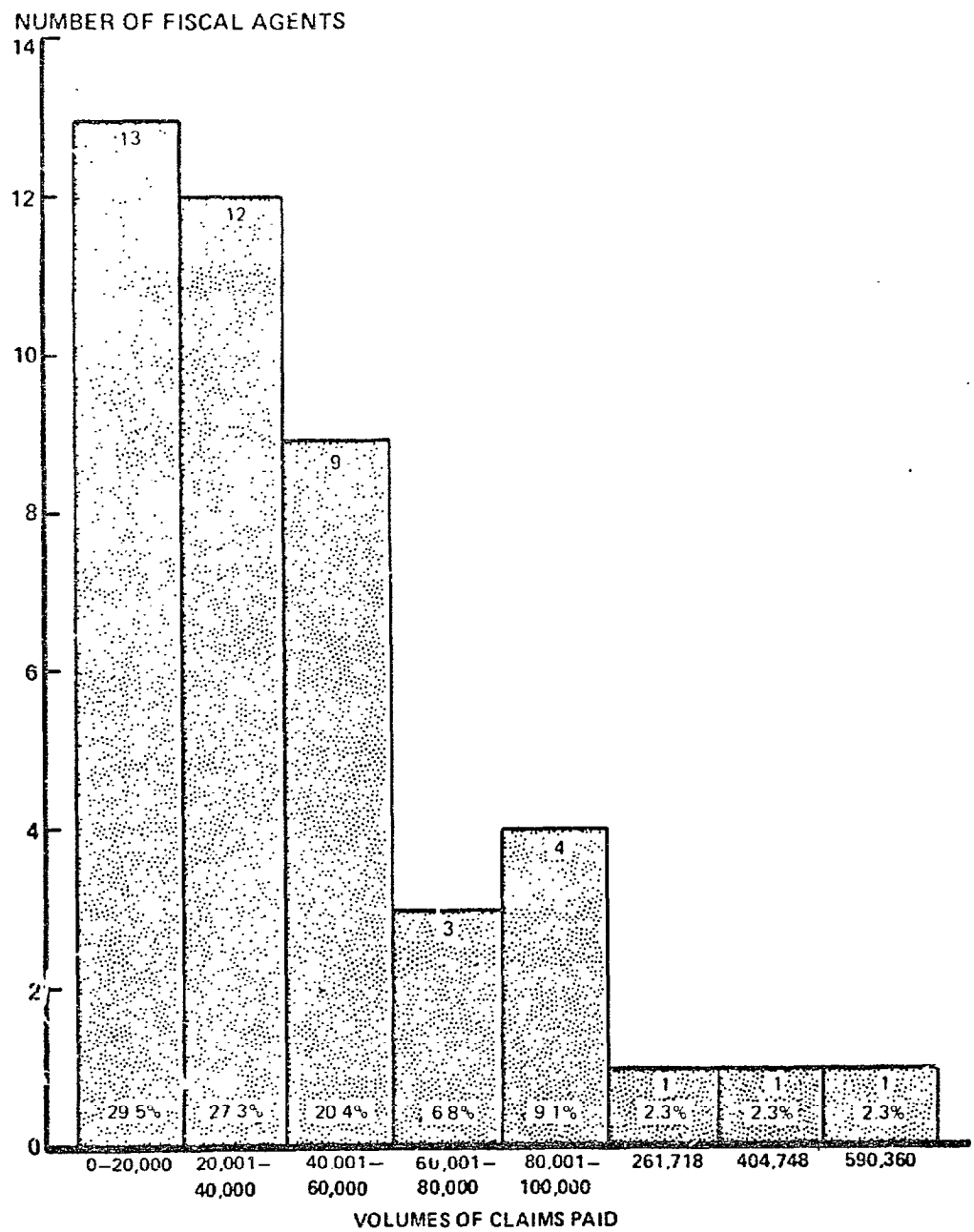
DISTRIBUTION OF PHYSICIAN CLAIM RATES



This chart shows that nearly 91 percent of the physician claim rates were between $2 and $10, while just over 9 percent exceeded $10.

During the same period, the claim volumes of these fiscal agents ranged from 4,875 to 590,360 claims, with an average of 62,885. (See app. IV.) While the average number of paid claims processed by physician fiscal agents is much higher than for hospital fiscal agents, only 10 of the 44 fiscal agents processed more than 62,885, or the average number of claims. These 10 fiscal agents processed nearly 65 percent of the total paid claims. The following chart shows the distribution of physician claim volumes:

DISTRIBUTION OF PHYSICIAN CLAIM VOLUMES



More than half the physician fiscal agents process less than 40,000 paid claims each, and less than 7 percent process over 100,000 paid claims each.

CHAMPUS CLAIM RATES GENERALLY EXCEED MEDICARE AND MEDICAID RATES

CHAMPUS, Medicare, and Medicaid claim rates are not directly comparable because of various program differences. For example, Medicare hospital claims may include a large number of outpatient claims which are relatively simple to process. Under Medicaid, claims are prepared by and paid to the provider of care and usually are for only one or a few items and are, therefore, easier to process and more likely to be prepared correctly. CHAMPUS physician claims may be prepared by and paid to beneficiaries, who are more likely to make errors and who also may submit claims for a number of expenses incurred over a period of time, thus taking longer and costing more to process. We did not attempt to quantify the effect of these factors on the following comparisons of claims processing costs or the comparison of productivity rates on pages 30 and 31.

Comparison of the CHAMPUS and Medicare claim rates, as they are normally computed, would be misleading because of the different bases used to compute claims volume. CHAMPUS divides administrative costs by paid claims to determine its reimbursement rate while Medicare uses the total of paid and rejected claims. To place both programs on a equal basis for comparison, we recomputed, as shown in the following schedule, the CHAMPUS rates for 13 of the fiscal agents we visited to reflect both paid and rejected claims.

CHAMPUS and Medicare Claim Rates
Year Ended March 31, 1976

Fiscal agents	CHAMPUS Paid claim rate	CHAMPUS Adjusted Claim rate	Medicare claim rate
Hospital:			
New Hampshire-Vermont Hospitalization Physician Service	$28.92	$27.97	a/$5.07
Colorado Hospital/ Medical Service	19.43	18.40	a/ 4.87
Blue Cross and Blue Shield of Maryland	12.57	12.34	a/ 4.17
Connecticut Blue Cross	10.53	9.88	a/ 5.00
Maine Blue Cross and Blue Shield	8.03	5.81	a/ 4.56
Blue Cross of Oregon	7.62	7.40	a/ 6.42
Mutual of Omaha	7.11	7.01	a/,b/ 7.41
Hawaii Medical Service Association	6.98	6.71	a/ 6.36
Average	$12.65	$11.94	$5.48
Physician:			
Colorado Hospital/ Medical Service	$10.80	$7.20	$3.10
New Hampshire-Vermont talization/ ician Service	10.44	8.33	2.58
ross and Blue Shield of Maryland	8.66	7.44	3.75
Mutual of Omaha	5.86	4.76	3.51
Arkansas Blue Cross and Blue Shield	4.82	4.02	2.67
Average	$ 8.12	$6.35	$3.12

a/Medicare rates include provider auditing costs, which add about $1 to the per claim processing cost of Blue Cross fiscal agents and a greater amount for Mutual of Omaha. CHAMPUS rates do not include a comparable cost.

b/The Mutual of Omaha Medicare rate includes costs for processing claims from skilled nursing facilities, which were more expensive to process than hospital claims.

The table shows that the adjusted CHAMPUS claim rate was higher than the Medicare rate for 12 of the 13 fiscal agents. The CHAMPUS average adjusted rates for both hospital and physician claims were twice as high as the Medicare average rates.

Only six of the fiscal agents visited processed Medicaid claims. Their respective rates are shown in the following table:

CHAMPUS and Medicaid claim rates
For year Ended March 31, 1975

Fiscal agents	CHAMPUS Paid claim rate	CHAMPUS Adjusted claim rate	Medicaid claim rate
Hospital:			
New Hampshire-Vermont Hospitalization/ Physician Service	$28.92	$27.97	$2.08
Colorado Hospital/ Medical Service	19.43	18.40	b/ 2.20
Hawaii Medical Service Association	6.98	a/ 6.98	b/1.04
Average	$18.44	$17.78	$1.77
Physician:			
Colorado Hospital/ Medical Service	$10.80	$7.20	b/$2.20
New Hampshire-Vermont Hospitalization/ Physician Service	10.44	8.33	.70
Hawaii Medical Service Association	3.50	a/ 3.50	b/ 1.04
Average	$ 8.25	$6.34	$1.31

a/Rate not adjusted because fiscal agent computes Medicaid claim rate on same basis as CHAMPUS; total administrative cost divided by paid claims.

b/Combined rate for both hospital and physician claims.

The adjusted average CHAMPUS hospital claim rate was over 10 times higher than the average Medicaid hospital claim rate, and the adjusted CHAMPUS physician claim rate was nearly 5 times higher than the average Medicaid physician claim rate.

CHAMPUS CLAIM RATES ARE GENERALLY HIGHER THAN TOTAL BUSINESS RATES

Wide variations exist between the claim rates charged CHAMPUS and the total business rates 1/ for nearly all CHAMPUS fiscal agents visited.

1/The total business claim rate of a fiscal agent is the total administrative costs for all lines of business divided by total volume of claims paid.

As shown in the following table, the CHAMPUS claim rate, in all but three cases, was higher than the fiscal agent's rate for total business:

CHAMPUS Portion Compared to Total Business

Fiscal agents	Claim rates (note a) Total business	CHAMPUS	Difference of rates	Percent of CHAMPUS to total business Volume	Costs
Hospital:					
New Hampshire-Vermont Hospitalization Physician Service	$6.61	$27.05	$20.44	0.4	1.8
Colorado Hospital Medical Service	8.11	16.00	7.89	.4	.9
Blue Cross and Blue Shield of Maryland	[illegible]	12.57	7.10	.3	.6
Connecticut Blue Cross	[illegible]	9.18	5.62	.1	.3
Maine Blue Cross and Blue Shield	[illegible]	6.78	-.54	.7	.7
Blue Cross of [illegible]	[illegible]	6.65	.55	.4	.4
Mutual of Omaha	[illegible]	[illegible]	.93	11.2	13.1
Hawaii Medical Service Association	[illegible]	6.99	4.95	.1	.3
Average difference between rates			$ 5.87		
Physicians:					
Colorado Hospital Medical Service	4.49	10.60	6.11	1.0	2.4
New Hampshire-Vermont Hospitalization Physician Service	[illegible]	[illegible]	8.04	.6	2.7
Blue Cross and Blue Shield of Maryland	[illegible]	8.66	4.87	.9	2.0
Mutual of Omaha (note b)	[illegible]	6.36	.93	11.2	13.1
Maine Blue Cross and Blue Shield	[illegible]	6.18	-.06	2.1	2.0
Oregon Physicians Service	5.44	[illegible]	-.92	7.0	5.8
Arkansas Blue Cross and Blue Shield	4.72	[illegible]	.10	2.0	2.0
Hawaii Medical Service Association	$ 2.03	3.50	1.48	.7	1.2
Average difference between rates			$2.57		

a/All rates are for calendar year 1975 except for Blue Cross and Blue Shield of Maryland, Hawaii Medical Service Association, and Arkansas Blue Cross and Blue Shield, which are for the 12-month period ended March 31, 1976.

b/Combined rates for both hospital and physician claims.

For hospital claims, the differences between these two rates ranged from -$.54 to $20.44, with an average difference of $5.87. For physician claims, the differences ranged from -$.92 to $8.04, with an average difference of $2.57.

CHARGES TO COST CATEGORIES DIFFER AMONG FISCAL AGENTS

Fiscal agents report their administrative costs to OCHAMPUS quarterly. The key cost categories for reporting, and the services performed and charged to each cost category are shown below:

Executive: Includes costs of corporate executives allocated to the CHAMPUS program.

Beneficiary services: Includes costs associated with responding to CHAMPUS-related letters and telephone calls, preparing explanations of benefits, answering walk-in inquiries, assisting beneficiaries in filling out forms, resolving billing problems, and providing educational literature. Five of the fiscal agents we visited did not charge costs to this category and two indicated that beneficiary services are charged to claims processing.

Claims processing: Includes costs associated with sorting mail, pulling files, checking claims forms for accuracy and completeness, coding and pricing claims, determining the reasonableness of charges, and keypunching claims for payment.

Professional relations: Includes costs associated with explaining the CHAMPUS program to providers, acting as a liaison with providers, determining the reasonableness of physician charges, publishing a newsletter, contracting with hospitals, maintaining contact with BCA, resolving fee disputes and claims problems, and reviewing hospital budgets.

Utilization review: Includes costs associated with evaluating the quality, quantity, promptness, or necessity of the medical services provided. Levels of review may include reviews by (1) a registered nurse, (2) a medical director or doctor, and (3) a medical society or team of consulting physicians. Not all fiscal agents perform all three levels of utilization review.

Financial: Includes costs related to accounting activities, internal audit, payroll, financial reporting, controlling accounts (ledgers), budgeting, and billing.

Data processing: Includes data processing costs associated with such functions as claim form edits and preparing checks and reports.

Office services: Includes cost of mail services, personnel, purchasing, supply, control records, cafeteria, photocopy/duplication, printing, building maintenance, microfilming, switchboard, and word processing.

Other: Includes provider relations, provider reimbursement, enrollment systems and programing, and field office administrative services. Only three fiscal agents visited charged costs to this category.

Claim rates charged to each of the above categories by fiscal agents visited, for the 12 months ended March 31, 1976, are shown in the following table:

Administrative Claim Rates by Cost Category (note a)

Fiscal agents	Total	Executive	Beneficiary services	Claims processing	Professional relations	Financial	Data processing	Office services	All other	Utilization review
Hospital:										
New Hampshire-Vermont Hospitalization/ Physician Service	$28.92	$0.86	$ 1.47	$12.10	$2.93	$ 1.22	$ 3.86	$ 4.49	-	-
Colorado Hospital/ Medical Service	19.43	.47	-	8.50	.47	1.	2.66	2.65	$ 3.46	-
Blue Cross and Blue Shield of Maryland	12.57	1.00	.06	6.16	.13	1.56	1.47	1.19	-	-
Connecticut Blue Cross	10.53	1.12	.03	4.95	.46	1.62	1.11	.25	-	-
Maine Blue Cross & Blue Shield	8.03	1.31	-	3.44	.09	.37	2.29	.53	-	-
Blue Cross of Oregon (note b)	7.62	1.01	-	6.18	-.19	-.12	-.02	- 15	.91	-
Mutual of Omaha	7.11	.35	.50	3.69	.17	.29	1.51	.62	-	-
Hawaii Medical Service Association	6.98	.33	-	5.07	.07	.76	.38	.37	-	-
Physician:										
Colorado Hospital/ Medical Service	10.80	.25	-	5.78	.37	.47	1 26	1 46		5 81
New Hampshire-Vermont Hospitalization/ Physician Service	10.44	.28	.60	5 63	.18	66	55	1 35		
Blue Cross and Blue Shield of Maryland	8.66	.43	.02	5 35	12	.58	1 17	.66		1.
Mutual of Omaha	5.86	.28	.41	3.04	.14	.24	1 26	.50	-	-
Maine Blue Cross and Blue Shield	5.64	.62	-	3.90	13	.25	39	.36		.61
Oregon Physician Service	5.60	.20	.13	3.78	.22	18	.53	.33	26	.18
Arkansas Blue Cross and Blue Shield	4.82	.22	.02	2.90	.26	.13	.59	.39	-	.14
Hawaii Medical Service Association	3.50	.32	-	2.61	.05	.19	.27	.06		-

a/Costs are unaudited and subject to adjustment. The sum of all cost category amounts may not equal the total claim rate due to rounding.

b/Negative figures represent adjustments to prior period estimates.

CHAPTER 3

FACTORS CONTRIBUTING TO DIFFERENCES IN CLAIM RATES CHARGED BY FISCAL AGENTS

Six factors appeared to have the greatest impact on claim rate variances among CHAMPUS fiscal agents. The factor having the greatest impact was the amount of fixed costs charged to CHAMPUS; other factors were differences among fiscal agents in numbers of returned and rejected claims, productivity rates, cost allocation systems used, hourly wages of claims processing personnel, and volumes of claims processed. Differences in services provided CHAMPUS by fiscal agents did not appear to be an important factor in claim rate variances.

In addition to the wide CHAMPUS claim rate variances among fiscal agents, CHAMPUS rates overall were generally higher than Medicare and Medicaid rates. While the programs are not directly comparable for the reasons cited on page 13, we believe that there are certain controllable factors which caused CHAMPUS claim rates to be considerably higher than Medicare and Medicaid rates. Small CHAMPUS volumes resulting in many fiscal agents being unable to take advantage of economies of scale was identified as one reason for the higher CHAMPUS rates. Most fiscal agents we visited processed CHAMPUS claims manually, while they processed Medicare and Medicaid claims with various degrees of automation. CHAMPUS claim rates were also higher than Medicare and Medicaid rates because many more CHAMPUS claims were returned due to errors in the more complex CHAMPUS claim form.

Studies of CHAMPUS claim rate variations by a management consulting firm and BCA indicated that many fiscal agents were unable to achieve economies of scale due to a small number of claims paid. BCA also reported that the claim rates varied among CHAMPUS fiscal agents because of differences in the allocation methods used and salaries paid claims processors.

REASONS FOR DIFFERENCES IN CHAMPUS CLAIM RATES

Factors affecting the claim rates were

--amounts of fixed costs to be allocated to all programs,

--numbers of returned and rejected claims,

--productivity rates,

--cost allocation methods,

--claims processors' hourly wages, and

--volumes of claims processed.

We did not find differences in services provided by fiscal agents to be a significant factor in claim rate variances. Although minor differences existed in services provided and some fiscal agents utilized computerized data processing systems more than others in paying claims, these factors had little impact on claim rates.

Amount of fixed costs

The total amount of fixed costs which fiscal agents must spread over all lines of business has a great effect on the CHAMPUS claim rates. Fixed costs, as we defined them, were those charged to CHAMPUS which would continue to be incurred if the fiscal agent no longer had the CHAMPUS contract. These costs are charged both directly and indirectly and are comprised of both personnel costs and such costs as those for buildings, equipment, and utilities. If two fiscal agents use the same allocation methods but have different total fixed costs, their charges to the CHAMPUS program will differ when all other variables are held constant. For example, we found one fiscal agent whose office occupancy cost per square foot was about $13; another's occupancy cost per square foot was about $8. Given similar allocation methods and paid claims volumes and holding all other variables constant, the cost per claim of the first fiscal agent will be higher than that of the second.

Generally, those fiscal agents charging the highest amount and highest percentage of fixed costs had higher than average CHAMPUS claim rates. For example, the New Hampshire-Vermont hospital fiscal agent, whose rate was the highest of all hospital fiscal agents, charged CHAMPUS with fixed costs of $20.24, or 70 percent of total costs of $28.92. However, the Hawaii hospital fiscal agent charged fixed costs of only $2.56, or 36.7 percent of its $6.98 in total costs.

The following table shows the fixed costs per claim incurred by the fiscal agents visited:

Relationship Between Fixed and Total Costs of
Selected CHAMPUS Fiscal Agents
For Year Ended March 31, 1976

Fiscal agents	Total administrative cost/claim	Fixed cost/claim	Percentage
Hospital:			
New Hampshire-Vermont Hospitalization/ Physician Service	$28.92	$20.24	70.0
Colorado Hospital/ Medical Services	19.43	15.74	79.6
Blue Cross and Blue Shield of Maryland	12.57	6.66	53.0
Connecticut Blue Cross	10.53	8.88	84.4
Maine Blue Cross and Blue Shield	8.03	6.24	77.7
Blue Cross of Oregon	7.62	2.97	39.0
Mutual of Omaha	7.11	3.2	45.0
Hawaii Medical Service Association	6.98	2.	36.7
Physician:			
Colorado Hospital/Medical Service	10.80	7.78	72.0
New Hampshire-Vermont Hospitalization/ Physician Service	10.44	6.25	60.0
Blue Cross and Blue Shield of Maryland	8.66	4.50	52.0
Mutual of Omaha	5.86	2.64	45.0
Maine Blue Cross and Blue Shield	5.64	3.62	64.2
Oregon Physician Service	5.60	(note a)	(note a)
Arkansas Blue Cross and Blue Shield	4.82	.68	14.1
Hawaii Medical Service Association	3.50	1.28	36.7

a/Not available.

Returned and rejected claims volumes

The percentage of claims returned and rejected by a fiscal agent can contribute to variances in claim rates among fiscal agents and increase total administrative costs. The volume of returned and rejected CHAMPUS claims varied among fiscal agents from about 12 to 73 percent of paid claims. Several fiscal agents with the higher rates also had higher percentages of returned and rejected claims.

Claims were returned or rejected for a number of reasons. The fiscal agents emphasized that causes of returned and rejected CHAMPUS claims included the claim form's complexity and frequent changes in CHAMPUS benefits. For example, the CHAMPUS regulation provides that a claim may be returned if it is not fully completed and does not contain at least 30 specified items of information. There have also been numerous deletions and revisions by DOD in recent years in benefit coverage to control costs and aline the program more closely with the legislation's intent. Claims are returned because data is missing, such as

--certification of other insurance,

--identification information,

--diagnosis and services provided,

--date of care,

--a statement that services are not available at a military facility,

--service or social security number, and

--signatures.

Many of the returned claims are resubmitted to the fiscal agent and later result in paid claims. Claims were also rejected because they were

--for a nonbenefit item,

--a duplicate,

--sent to the wrong fiscal agent,

--paid by other insurance, or

--for services not medically necessary.

These claims generally are not resubmitted for payment to the fiscal agent.

Claims processing productivity rates

The claims processors' productivity can affect claim rates. Although there were exceptions, fiscal agents with higher rates generally had lower productivity.

Productivity was defined as claims paid per claims processor per day. Claims processors' duties generally included determining the claim's completeness, reasonableness of charges, correlations between diagnosis and treatment, and whether services were for covered benefits. Assuming two fiscal agents pay their claims processors the same wages and one fiscal agent's processors turn out more paid claims than the other, the claims processing cost per claim of the more productive fiscal agent would be lower than that of the less productive fiscal agent. For example, the Hawaii hospital fiscal agent and the New Hampshire-Vermont hospital fiscal agent pay their claims processors about the same hourly salaries. However, each Hawaii hospital fiscal agent claims processor completes about 10 paid claims per day while each New Hampshire-Vermont hospital fiscal agent claims processor completes about 7 paid claims per day. The Hawaii hospital fiscal agent's higher productivity is reflected in its claims processing cost of $5.07 per claim compared to the New Hampshire-Vermont hospital fiscal agent's claims processing cost of $12.10 per claim. (See p. 19.)

New Hampshire-Vermont, which had the highest claim rate among hospital fiscal agents and one of the highest physician claim rates, was the least productive. The following table shows productivity of the physician and hospital fiscal agents visited:

Claims Processing Productivity

Fiscal agents	Productivity rate (note a)
Hospital:	
Mutual of Omaha	b/36.8
Colorado Hospital/Medical Services	29.4
Maine Blue Cross and Blue Shield	26.0
Blue Cross and Blue Shield of Maryland	18.3
Blue Cross of Oregon	15.5
Connecticut Blue Cross	11.7
Hawaii Medical Service Association	10.0
New Hampshire-Vermont Hospitalization/ Physician Service	6.6
Physician:	
Mutual of Omaha	b/36.8
Hawaii Medical Service Association	34.4
Arkansas Blue Cross and Blue Shield	34.0
Colorado Hospital/Medical Service	26.9
Blue Cross and Blue Shield of Maryland	23.8
Oregon Physician Service	21.1
Maine Blue Cross and Blue Shield	20.2
New Hampshire-Vermont Hospitalization/ Physician Service	15.7

a/Productivity is defined as claims paid per day divided by the average number of claims processors during FY 1976.

b/Combined Rate. Mutual of Omaha does not compute productivity rates separately for hospital and physician claims on the basis of average number of claims examiners.

Different cost allocation methods

Fiscal agents charged CHAMPUS directly for costs easily identified with the program. All other costs were allocated as indirect costs. The methods used to allocate indirect costs can greatly influence claim rates. The OCHAMPUS contracts with fiscal agents do not specify the allocation method to be used or set any limitations on the amounts that can be charged to CHAMPUS.

Fiscal agents visited were generally charging CHAMPUS directly for most costs in the claims processing category, and indirectly through various allocation methods for many costs

in the other eight administrative cost categories. (See pp. 17 and 18.) The percent of indirect costs allocated to CHAMPUS claims by the fiscal agents visited ranged from 6 to 85 percent of total costs. The most prevalent allocation methods used to charge different categories of indirect costs to CHAMPUS and a description of how indirect costs are calculated by each method is shown in appendix V. All fiscal agents we visited used more than one allocation method and several used as many as seven methods.

It is difficult to demonstrate the impact of different allocation methods on the claim rate in actual situations because of offsetting factors. For example, using the direct hours method would usually produce a higher charge to CHAMPUS if all other factors were equal. In practice, that effect may be offset by such factors as a small amount of fixed costs to be allocated or higher productivity. However, the following example shows how charges to the CHAMPUS program, for a given category of indirect costs, can vary greatly depending upon the allocation method:

	Direct hours allocation method	Claims volume allocation method
Total executive salaries to be allocated	$500,000	$500,000
CHAMPUS claim volume as a percent of total claim volume	1%	1%
CHAMPUS direct hours as a percent of total corporate hours	4%	4%
CHAMPUS claims processed	2,500	2,500
Executive salaries allocated to CHAMPUS	$ 20,000 ($500,000 x 4%)	$ 5,000 ($500,000 x 1%)
Executive salary costs charged to CHAMPUS per claim	$8.00	$2.00

The above example shows how the direct hours allocation method can produce higher costs to the CHAMPUS program. In comparison with other lines of a fiscal agent's business, CHAMPUS may be charged a relatively large number of direct hours since CHAMPUS claims processing is mostly manual. Consequently, use of the direct hours allocation method results in a larger base for the allocation of indirect charges to CHAMPUS.

Employee hourly wages

Another factor contributing to claim rate variances was employee wages. The average hourly salary of claims processors at the fiscal agents visited ranged from $2.94 to $5.73. Given similar productivity levels and all other factors remaining constant, fiscal agents paying higher hourly wages will be charging CHAMPUS more per claim than fiscal agents paying lower hourly wages. For example, the Oregon hospital fiscal agent and the Connecticut hospital fiscal agent have similar productivity levels; however, the Oregon hospital fiscal agent pays its claims processors an average of about $5.73 per hour, while the Connecticut hospital fiscal agent pays its claims processors an average of about $3.42 per hour. The difference in hourly wages is partly responsible for the Oregon hospital fiscal agent's charge in the claims processing category of $6.18 per claim and the Connecticut hospital fiscal agent's claims processing charge of $4.95 per claim. (See p. 19.)

Volume of claims processed

The hospital fiscal agents that processed a large volume of claims generally had the lower claim rates; however, a similar relationship was not evident among physician fiscal agents.

Fiscal agents that also processed Medicare and Medicaid claims cited higher claim volumes as one reason Medicare and Medicaid rates are lower than CHAMPUS. Seven of the 10 hospital fiscal agents who had the lowest claim rates ranked in the upper 50 percent of fiscal agents that had the largest number of claims paid.

Impact of specific factors on fiscal agents claim rates

Following are several examples of how the factors discussed above resulted in differences in claim rates between selected fiscal agents.

Mutual of Omaha's hospital claim rate of $7.11 was less than half the average rate of $16.81 for BCA and the 52 Blue Cross plans. Significant factors causing this difference were as follows:

--Mutual took advantage of economies of scale as it centrally processed almost as many hospital claims (206,937) as the 52 BCA fiscal agents combined (249,180); when considering both physician and hospital claims, Mutual processed many more claims (611,685). Mutual's

system is highly automated, whereas many BCA fiscal agent systems are primarily manual. Thirty-seven BCA fiscal agents processed less than 5,000 claims and one processed only 103 claims. Mutual's fixed costs were spread over a large volume, while the BCA fiscal agents' fixed costs had to be absorbed by relatively small volumes. Mutual's fixed cost per claim was $3.20, compared to an average of $9.04 per claim by the BCA fiscal agents visited.

--Blue Cross fiscal agents must work through BCA. BCA adds about $1.96 per claim to the overall claim rate, while Mutual and physician fiscal agents deal directly with OCHAMPUS. Services performed by BCA in this "middleman" role include claim edits (which duplicate edits performed by many of the BCA fiscal agents), compiling statistics, and preparing reports for OCHAMPUS.

--Mutual's average hourly salary was $3.44 for claims processors, while the BCA average was $4.23.

Contracting with BCA gives CHAMPUS the opportunity to obtain the same favorable rates on benefit payments that hospitals give Blue Cross plans. Plan agreements with hospitals generally provide for reimbursement formulas which adjust billed charges to costs, or cost plus a small percentage charge. BCA estimates that it saved CHAMPUS over $5.2 million in benefit payments in calendar year 1975, while total administrative charges under the BCA contract were about $3.5 million, of which BCA headquarters charged about $450,000. A BCA study, however, shows that these lower benefit rates could be offered CHAMPUS directly by the local Blue Cross plans without contracting through BCA.

The Hawaii fiscal agent's hospital claim rate of $6.98 was less than half the $19.43 claim rate charged by the Colorado hospital fiscal agent. Fixed cost was the major factor responsible for the claim rate difference. Hawaii's fixed cost per claim was $2.56 while Colorado's was $15.74. The Hawaii fiscal agent's philosophy is that Government health programs have helped the organization because the expanded claims volume justified the cost of mechanizing operations; this in turn benefits both its private and Government business. This fiscal agent charges the Government programs, in addition to direct costs, only those fixed costs easily identifiable as related to the program.

Analyses similar to those performed above could be used to explain claim rate variances between any two of the fiscal agents visited. We believe such variances are due to differences in amounts of fixed costs, volumes of returned and re-

jected claims, productivity, allocation systems, hourly salaries, and paid claims volume.

REASONS FOR CHAMPUS CLAIM RATES BEING HIGHER THAN MEDICARE AND MEDICAID RATES

Fiscal agents' lower claims volumes and lower productivity rates were the major reasons identified for CHAMPUS claim rates generally exceeding Medicare's. Fiscal agents generally had automated systems to handle the high volume of Medicare claims, while their systems to process CHAMPUS claims were primarily manual. The high Medicare claims volumes resulted in spreading fixed costs over a volume larger than under CHAMPUS.

According to fiscal agent officials visited, the CHAMPUS productivity rates were lower than Medicare because

--CHAMPUS claims processing is primarily manual,

--CHAMPUS claim forms are longer and more complex,

--CHAMPUS makes many more program changes, and

--turnover of CHAMPUS claims processors is more of a problem because of the many program changes and program complexity.

In addition, Medicare hospital claims may include a high volume of outpatient claims, which are easier to process than the hospital inpatient claims.

A comparison of CHAMPUS and Medicare productivity rates for fiscal agents visited is shown below:

CHAMPUS and Medicare
Productivity Rates (note a)

Fiscal agents	Daily productivity rates CHAMPUS	Medicare
Hospital:		
New Hampshire-Vermont Hospitalization/ Physician Service	5.8	17.0
Colorado Hospital/ Medical Service	11.8	19.8
Blue Cross and Blue Shield of Maryland	11.2	27.5
Connecticut Blue Cross	12.0	18.2
Maine Blue Cross and Blue Shield	17.0	21.1
Blue Cross of Oregon	15.3	16.6
Mutual of Omaha	18.2	b/12.6
Hawaii Medical Service Association	10.3	11.3
Physician:		
Colorado Hospital/Medical Service	21.9	25.3
New Hampshire-Vermont Hospitalization/ Physician Service	15.1	25.7
Blue Cross and Blue Shield of Maryland	15.4	25.0
Mutual of Omaha	16.8	18.6
Arkansas Blue Cross and Blue Shield	20.5	36.2

a/Productivity is defined as claims handled per person per day, considering all personnel in the claims processing unit, including mail clerks and secretaries as well as claims processors.

b/Mutual of Omaha's productivity rate for Medicare is not directly comparable to the CHAMPUS rate because it includes claims from skilled nursing facilities, which are more difficult to process than hospital claims.

Medicaid claim rates, as shown in chapter 2, were significantly lower than CHAMPUS rates for the CHAMPUS fiscal agents who also processed Medicaid claims. Higher productivity and claims volumes were also the predominant reasons for Medicaid rates being lower than CHAMPUS rates. The Colorado fiscal

agent processed over 800,000 Medicaid claims while processing only 45,190 CHAMPUS claims during the 12 months ended March 31, 1976. The Hawaii fiscal agent processed over 1 million Medicaid claims and only 27,339 CHAMPUS claims in the same period. Claims processing systems for Medicaid were much more automated than for CHAMPUS. Productivity differences between CHAMPUS and Medicaid in the two States are shown below:

	Daily Productivity Rate (note a)			
	CHAMPUS		MEDICAID	
	Hospital	Physician	Hospital	Medical
Colorado Hospital/ Medical Service	11.8	21.9	b/148	58.6
Hawaii Medical Service Association (note c)	8.5	25.8	d/92.1	

a/The productivity rates for the Colorado fiscal agent are based on all claims handled; the productivity rates for the Hawaii fiscal agent are based on paid claims only. Rates for both fiscal agents reflect the average number of all personnel in the claims processing units.

b/Many of the Medicaid hospital claims are processed completely by automation through direct computer linkups between a hospital and the fiscal agent.

c/The Hawaii fiscal agent's Medicaid claims include prescription drug claims, which are relatively easy to process. The CHAMPUS claims include claims from foreign countries, which may involve translation and converting charges into U.S. currency and, therefore, are relatively more difficult to process.

d/Combined.

STUDIES OF REASONS FOR CHAMPUS CLAIM RATE VARIANCES AND DIFFERENCES WITH MEDICARE CLAIM RATES

Studies have been performed by a management consulting firm for DOD and BCA to determine the reasons for claim rate variations among CHAMPUS fiscal agents.

Management consulting firm study

In a report dated August 29, 1975, a management consulting firm analyzed administrative costs of CHAMPUS fiscal agents.

Using data from quarterly cost proposals submitted by fiscal agents and OCHAMPUS reports, the firm presented findings separately for hospital and physician fiscal agents in two broad categories--(1) composition of administrative costs and (2) comparison of CHAMPUS claims processing costs with those of Medicare.

Hospital fiscal agents

Using 1974 figures, the report shows a range of costs for the Blue Cross plans from $4.04 to $19 per claim, with averages of $8.35 per claim and about 6,100 claims paid. The two plans with the highest claim rates had substantially less than the national average of paid claims, while the third highest plan was only slightly above average. In contrast, the seven plans with the highest paid claims volumes had claim rates of less than $7.50 (a $6 average). The study maintains that this supports an argument for economies of scale, allowing fiscal agents with large claims volumes to process claims at lower rates. This argument is further supported by data from Mutual of Omaha, which paid nearly 200,000 claims in 1974 at a cost of $5.95 each.

In an effort to identify common patterns among fiscal agents, the quarterly cost reports of eight Blue Cross plans and Mutual of Omaha were analyzed. Fiscal agents reported costs broken down into nine categories. It appeared that those fiscal agents who charged the highest percentage of their administrative costs to the claims processing category generally had lower claim rates. Efforts to correlate the data from the other eight cost categories did not show clear relationships between cost allocations and total costs.

A comparison of CHAMPUS claim rates and averages with the Medicare program showed that Medicare fiscal agents had both a lower average rate and a narrower range than CHAMPUS fiscal agents. Medicare had an average rate of $4.77 with a range from $2.46 to $8.70. The study made no attempt to explain the reasons for the differences between Medicare and CHAMPUS.

Physician fiscal agents

The claim rate and range for CHAMPUS physician fiscal agents for 1974 were lower than for CHAMPUS hospital fiscal agents. The average claim rate for the 46 physician fiscal agents was approximately $6, with only one being above $10. Eighty-seven percent of the fiscal agents had claim rates below $8, and the 10 largest fiscal agents (by paid claims volume) had an average claim rate of $5.81, or about $0.20

below the national average. The limited work done to determine any correlation between cost allocations and total costs for physician fiscal agents was inconclusive. The Medicare national average claim rate for carriers was $4.01 per claim, which is much lower than approximatley $6 per claim for CHAMPUS physician fiscal agents.

BCA study

In November and December 1975, BCA made a study to identify reasons for claim rates differences among its CHAMPUS subcontractors. Four plans were chosen for review based on a variety of factors, including claim rates and volumes. The plans were:

--Cheyenne, Wyoming (low rate-low volume);

--Youngstown, Ohio (high rate-low volume);

--Birmingham, Alabama (low rate-high volume); and

--Denver, Colorado (high rate-high volume).

The study identified several factors causing rate differences:

--Where there was a combined type of plan (Blue Cross and Blue Shield), the CHAMPUS claim rate was generally lower than for a plan with only one operation (Blue Cross). The conclusion was that a single operation was not able to spread overhead costs as much as a multiple plan.

--Claim rates and salaries were related. The ranking order of the four plans by claim rate is the same as for average monthly salaries paid to claims processors, personnel handling correspondence, and supervisors.

--Allocation methods used to distribute indirect costs can affect the cost of claims processing. One example given involved the allocation of space costs to the CHAMPUS program. While all four plans allocated facility and occupancy costs to cost centers on the basis of square footage occupied, the methods of further distributing costs to various lines of business varied among plans. The plan with the highest claim rate used a salary dollars method, while the one with the lowest used a paid claims ratio.

--Plans either undercharging or overcharging CHAMPUS also caused differences in claim rates. These instances were usually the result of accounting errors or a failure to recognize proper costs.

The BCA study concluded that no single factor can be isolated as being responsible for claim rate differences. Some factors affect claim costs more than others. The differences will probably continue until methods and standards for claims processing and cost accounting are established to hold claim rates at a uniform level.

CHAPTER 4

MONITORING CHAMPUS CLAIM RATES

Fiscal agent operations are monitored by the OCHAMPUS Contract Management Directorate. Fiscal agents are visited by contract performance review teams and the Department of Health, Education, and Welfare Audit Agency (HEWAA), which audits the CHAMPUS contracts with fiscal agents through an arrangement with DOD. These groups have made little effort to determine the reasons for variances in fiscal agents' claim rates or to identify methods for lowering administrative costs.

RESPONSIBILITIES FOR ADMINISTRATION OF CHAMPUS CONTRACTS

The OCHAMPUS Contract Management Directorate is responsible for negotiating contracts with fiscal agents, making interim payments for claims paid, and monitoring contractor performance. Cost-reimbursable contracts have been used since the program was established in 1956, and under these contracts wide variations in claim rates have existed for many years.

A July 1975 consultant's report on the feasibility of using fixed-price contracts cited several deficiencies with CHAMPUS cost-reimbursable contracts. These contracts, which varied little between fiscal agents, did not contain detailed work statements specifying the services to be performed, standards for measuring fiscal agent performance, or incentives for improving performance and controlling costs. Fiscal agents' performance was evaluated subjectively for the most part, through visits by the OCHAMPUS contract performance review team. OCHAMPUS personnel also were said to have had little training in procurement.

About 5 years ago, OCHAMPUS instituted a requirement for monthly and quarterly reporting by fiscal agents to help identify fiscal and operating problems. Fiscal agents provide information on administrative costs, paid claims volume, returned and rejected claims, and personnel processing claims. With this information, OCHAMPUS ranks all fiscal agents by claim rate and volume, makes comparisons on returned and rejected claims, and computes productivity.

The information showed wide variations in claim rates and productivity among fiscal agents. However, no action was taken to replace fiscal agents with high claim rates and low productivity until October 1975. At that time OCHAMPUS replaced the New Jersey physician fiscal agent, whose $13.95 claim rate was

the highest of all physician fiscal agents. Inefficiencies in that fiscal agent's claims processing operations were noted as early as July 1967, and the agent's claim rate after that time had been consistently high. However, more than 8 years passed before OCHAMPUS terminated the contract. An OCHAMPUS official stated that this was the only cost-reimbursable contract terminated for cause by OCHAMPUS.

The contract performance review team is responsible for evaluating fiscal agent performance and compliance with contract provisions. According to an OCHAMPUS official, teams of two generally spend 3 days with each fiscal agent and review such areas as

--claims processing and automated data processing operations,

--utilization review procedures,

--services provided to beneficiaries and providers,

--management and organization efficiency, and

--accounting and fiscal management.

Visits to fiscal agents are made at least once every 2 years and sometimes as frequently as twice a year. Performance review reports are prepared on the results of each visit. These reports give OCHAMPUS officials an indication of how fiscal agents are administering the program, but they do not explain why administrative costs may be comparatively high or indicate what could be done to lower costs. Letters to the fiscal agents summarize review findings and sometimes state that costs appear excessive, but no suggestions are given on how to reduce costs.

HEWAA AUDITS OF CHAMPUS COST-REIMBURSABLE CONTRACTS

HEWAA is responsible for audits of CHAMPUS contracts with fiscal agents. These audits, besides covering the allowability and reasonableness of benefit payments, cover the allowability, allocability, and reasonableness of proposed administrative costs. The auditors determine that the allocation method used by the fiscal agent is consistently applied to all lines of business, and that costs not allowed by the contract are not charged to CHAMPUS. However, an OCHAMPUS official said that HEWAA has not been assigned responsiblity for comparing fiscal agents' administrative costs to determine reasons for variances or identifying methods of lowering administrative costs.

HEWAA may disallow certain administrative costs because they are not allowable under CHAMPUS or because the fiscal agent's allocation methods are inconsistent. For example, under a recently completed contract with the Oregon physician fiscal agent, HEWAA questioned $4,447 of $525,789 in administrative costs because they were not properly allocable to CHAMPUS.

According to the OCHAMPUS Director, the audit function will be changed to make it responsive to the different requirements of fixed-price contracts.

CHAPTER 5

CONVERSION TO FIXED-PRICE CONTRACTS

OCHAMPUS is replacing its cost-reimbursable contracts with fixed-price contracts. This is expected to reduce administrative costs by stimulating competition and promoting efficiency among fiscal agents. However, effective performance monitoring will be necessary to make sure that the quality of claims review is not reduced through efforts to keep costs competitively low.

Although the fiscal agent's performance under the first fixed-price contract proved unacceptable, cost savings and other advantages of such contracts should outweigh the disadvantages if OCHAMPUS effectively administers the competitive bid process and contracts. This experience should demonstrate the necessity of strict adherence to basic principles of fixed-price contracting if the benefits of this type of contracting are to be fully realized.

IMPLEMENTATION OF FIXED-PRICE CONTRACTS

According to a Defense Supply Service memorandum, the decision to use fixed-price contracts for CHAMPUS fiscal agents was based on recommendations contained in a GAO report. 1/ Other reasons cited by DOD officials included recommendations contained in the July 1975 consultant's feasibility study done for DOD.

The study concluded that, with the use of a detailed specification (work statement), a standard for determining acceptable work, and a competitive fixed-price contract, contractor performance would increase in quality and decrease in overall cost to the Government.

For the first fixed-price CHAMPUS contract, DOD requested that the Defense Supply Service issue a request for proposals (RFP) for implementation and operation of a CHAMPUS fiscal intermediary system in the States of California, New Mexico, Arizona, Nevada, and Texas. A DOD review panel evaluated the six proposals recieved, and on February 19, 1976,

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1/"Management of the Civilian Health and Medical Program of the Uniformed Services Needs Improvement" (B-133142, Nov. 21, 1975).

awarded the contract to Health Application Systems, Inc. (HAS). HAS had the highest technical rating and bid the lowest unit price.

As of October 4, 1976, HAS had a backlog of over 230,000 claims, which was over three times the average backlog of former fiscal agents for the 12-month period ended March 31, 1976. At HAS's then current processing rate, it would have taken over 30 months to clear the backlog. In the opinion of OCHAMPUS officials, HAS did not comply with contract provisions to

--process claims promptly and accurately,

--obtain appropriate management and administrative information through production of timely and accurate reports,

--explain fully to providers and beneficiaries the disposition of all claims submitted by them for payment, and

--detect duplicate claims, overutilization, and other potential abuses.

On October 28, 1976, DOD decided not to renew the contract with HAS. The claims processing responsibilities of HAS were discontinued on November 14, 1976, and assumed by two other fiscal agents under cost-reimbursable contracts as an interim measure.

The OCHAMPUS Director stated that DOD officials decided in March 1976 that OCHAMPUS would issue RFPs and award fixed-price contracts in the future. As of December 6, 1976, OCHAMPUS had issued 14 RFPs covering 25 States, and awarded 9 contracts covering 16 States. OCHAMPUS estimated that fixed-price contracts will be in effect for all States by the end of 1977.

ADVANTAGES AND DISADVANTAGES OF FIXED-PRICE CONTRACTS

For the initial 1-year period for fixed-price contracts awarded as of December 6, 1976, OCHAMPUS estimates administrative cost savings of about $1.9 million over fiscal year 1976 costs. The following table shows the estimated savings by contract and compares the bid price per claim with the average fiscal year 1976 claim rate under cost-reimbursable contracts for the States covered by fixed-price contracts:

Projected Administrative Cost Savings
and Contractor Bid Data

Contract by areas	FY 1976 costs	Projected costs (note a)	Estimated savings	RFP bid price (note a)	Average FY 1976 claim rate
Washington Alaska Oregon	$1,240,162	$ 640,385	$ 599,777	$3.95	$7.65
Massachusetts Connecticut	700,716	526,893	174,523	3.89	6.85
Delaware Pennsylvania	573,060	356,545	216,515	5.14	6.25
Colorado	538,200	355,168	183,032	5.69	8.59
Michigan	527,958	272,271	255,687	5.45	10.57
Indiana Kentucky	483,365	412,320	71,045	4.08	4.83
New Hampshire Vermont Maine	428,007	191,529	236,478	4.19	9.36
Missouri	353,565	230,788	122,777	4.14	6.34
Maryland	269,566	194,119	75,447	7.03	9.76
	$5,114,599	$3,179,018	$1,935,581		

a/Projected costs and RFP bid price shown are for the same volume of claims as processed in FY 1976 for the given States.

The following table shows that former CHAMPUS fiscal agents with experience in processing both hospital and physician claims submitted bids for fixed-price contracts that were lower than their previous combined rate for both hospital and physician claims. The decrease may partially explained by the increased claims volume related to the bid price, particularly in the case of bidder 'A'. However, the 25-percent reduction in claim rate for bidder 'C' and the 47-percent reduction for bidder 'D' would not appear to be explained by the increases in volume of 13 percent and 18 percent, respectively.

Comparison of Cost-Reimbursable Contract Claim Rates With Fixed Price Contract Bid Prices of Selected Fiscal Agents

Bidder	Average RFP bid price	Former CHAMPUS claim rate	Average volumes of RFPs bid	Former CHAMPUS volume
A	$5.61	$ 6.28	745,830	611,685
B	7.05	12.01	66,740	45,190
C	7.08	9.41	30,725	27,207
D	5.42	10.24	59,960	50,727

The advantage most frequently cited by fiscal agents that we visited was that fixed-price contracts would reduce costs by stimulating competition and promoting efficiency. Many also believed, however, that the quality of claims review could suffer through efforts to keep costs competitively low.

In addition to cost savings, the OCHAMPUS Director stated that fixed-price contracts would produce the following advantages:

--Strong contractual commitments from fiscal agents to provide indepth, top quality claims processing, including high level peer and utilization review.

--Commitments from fiscal agents for improved management information systems.

--An opportunity for innovation in CHAMPUS administration and reimbursement.

Disadvantages of fixed-price contracts identified by the OCHAMPUS Director included:

--Some beneficiary inconvenience by changing to new fiscal agents.

--The risk of incurring poor performance from contractors inexperienced with CHAMPUS.

--The probability of short-term poor performance during contractor changeovers.

--An unstable, temporary relationship between the Government and some contractors.

--Reduced claims adjudication skill and experience when new fiscal agents take over.

The Director said the competitive process is the best way to prepare the private sector for national health insurance by helping new companies enter the industry and by encouraging improvements and refinements among older companies.

According to our analysis of Federal agency experience in contracting for various systems and services, 1/ the fixed-price contract places maximum risk on the contractor, and gives the contractor a maximum profit incentive to control costs and perform the contract effectively. The fixed-price contract is suitable for procurements when reasonably precise specifications are available for which sound cost estimates can be developed before procurement.

Cost-reimbursable contracts place less financial risk on the contractor and more risk on the Government than do fixed-price contracts. They are suitable when the cost of performance cannot be reasonably estimated. A consultant's study noted that cost-reimbursable contracts are most generally used to procure research and development because both parties are unable to define the effort required to do the work.

In comparison, CHAMPUS has been procuring fundamentally the same services through cost-reimbursable contracts for about 20 years. With such a lengthy procurement history, it is possible to detail the functions to be performed by the contractor and, therefore, reasonably estimate the cost.

1/"Lessons Learned About Acquiring Financial Management and Other Information Systems," August 1976, by the Comptroller General of the United States.

CHAPTER 6

CONCLUSIONS AND RECOMMENDATIONS TO THE CONGRESS

CONCLUSIONS

Six factors appeared to have the greatest impact on CHAMPUS claim rate variations and rates overall. The most significant factor in rate variation was the fixed cost amount charged CHAMPUS. The fiscal agents charging CHAMPUS high claim rates also charged high fixed costs.

Frequent CHAMPUS program changes and a complex claim form contributed to low claims processing productivity and high percentages of returned and rejected claims. Because of the large number of CHAMPUS fiscal agents and the low volumes of claims processed by many, CHAMPUS generally did not obtain advantages of economies of scale.

The CHAMPUS cost-reimbursable contracts, which resulted in wide variations in claim rates between fiscal agents, did not contain standards for measuring performance acceptability and offered no incentive for cost control or efficiency. In addition, the benefits of contracting through a middleman for processing hospital claims did not appear to justify the costs and added further variance in claim rates between the Blue Cross Association and Mutual of Omaha.

Services such as those provided by CHAMPUS fiscal agents will probably have to be procured for any national health insurance program. The use of competitively bid fixed-price contracts to obtain these services would appear to be advantageous. Cost-reimbursable contracts, however, may be preferable at the early stages of a new program until reasonably precise performance specifications and cost estimates are available.

RECOMMENDATIONS TO THE CONGRESS

In asking for this review, the Subcommittee stated that it is conducting an inquiry into contracting by Government agencies for fiscal agent services for health and welfare programs, and that the CHAMPUS experience could serve as a model of a larger issue.

We believe our study of the CHAMPUS experience with fiscal agents provides some important lessons that could be applied to any new federally sponsored health insurance programs.

Because of the CHAMPUS experience with cost-reimbursable contracts and the potential benefits of competitively bid fixed-price contracts, we recommend that, for any new federally sponsored health insurance programs which will need services such as those provided by CHAMPUS fiscal agents, the Congress require:

--Consolidated fiscal agent operations to achieve large claim volumes and take maximum advantage of economies of scale.

--Simplified claim forms, and to the extent possible, standardized Government health insurance claim forms.

--Well-defined program benefits and policies to avoid frequent program changes.

--Use of reimbursable contracts only until reliable information can be assembled on specifications, performance, and costs. The contracting process should require:

  a. Contracts that contain standards for acceptable cost accounting and cost allocation methods.

  b. Contracts to be specific about the nature and intensity of duties to be performed, and standards for measuring contractor performance acceptability.

  c. Direct contracting rather than subcontracting.

  d. A maximum acceptable cost rate. Costs exceeding this rate must be investigated and necessary corrective actions taken.

  e. Assignment of specific administrative responsibility for investigating fiscal agents not meeting performance standards and acceptable costs.

--Use of competitive bid fixed-price contracts as soon as reasonably precise specifications, performance data, and reliable cost information are available.

APPENDIX I

United States Senate

COMMITTEE ON GOVERNMENTAL OPERATIONS
SENATE PERMANENT SUBCOMMITTEE ON INVESTIGATIONS
(PURSUANT TO S. RES. 49, 94TH CONGRESS)
WASHINGTON, D.C. 20510

July 1, 1976

My dear Mr. Comptroller General:

The Permanent Subcommittee on Investigations is conducting a preliminary inquiry into contracting by government agencies for fiscal intermediary services for health and welfare programs.

From our experience, the Civilian Health and Medical Program for the Uniformed Services (CHAMPUS) offers us the best agency from which to begin a study of these services. It can serve as a microcosm of a larger issue.

Fiscal intermediaries for CHAMPUS reimbursement for physicians' services use the same forms across the country and yet there are wide variations in prices. For example, we understand that Blue Shield of Virginia, processes claims at Richmond for CHAMPUS claims from New Jersey as well as Virginia. We are curious as to why Virginia Blue Shield charges $4.25 per claim on 82,000 claims per year from Virginia, but $12.65 per claim for 26,500 claims from New Jersey.

For hospital claims, there are two primary contractors, each with about the same volume. Mutual of Omaha processes 212,500 claims at $7.12 each but Blue Cross Association charges $13.62 per claim on a volume of 255,000 claims.

We would like the General Accounting Office to conduct a review of these charges and provide the Subcommittee with a Statement of Facts about the issue. In the interest of time, we prefer that there be no review of your report by the concerns or government agency that may become the subjects of this review.

I would, however, like to point out that we want to structure [illegible] review so that it [illegible] be [illegible]. In short, those intermediaries [illegible] are se[illegible] [illegible] tails s[illegible] be providing services not only to [illegible], but [illegible] the [illegible]care pro[illegible] and, perhaps, Medicaid programs.

Thank you for your cooperation.

Sincerely yours,

[illegible]mm
Acting Chairman

The Honorable Elmer B. Staats
The Comptroller General

CHAMPUS FISCAL AGENTS AND SUBCONTRACTORS VISITED AND THEIR PARTICIPATION IN MEDICARE AND MEDICAID

Organization visited	CHAMPUS hospital		CHAMPUS physician fiscal agent	Medicare		Medicaid
	Fiscal agent	Subcontractor to BCA		Part A	Part B	
Blue Cross Association Chicago, Illinois	X					
Mutual of Omaha Omaha, Nebraska	X		X			
Arkansas Blue Cross and Blue Shield Little Rock, Arkansas			X	X	X	
Colorado Hospital/Medical Service Denver, Colorado		X	X	X	X	X
Connecticut Blue Cross North Haven, Connecticut		X		X		
Hawaii Medical Service Association Honolulu, Hawaii		X	X	X		X
Maine Blue Cross and Blue Shield Portland, Maine		X	X	X		
Blue Cross and Blue shield of Maryland Towson, Maryland		X	X	X	X	
New Hampshire-Vermont Hospitalization/ Physician Service Concord, New Hampshire		X	X	X	X	X
Blue Cross of Oregon Portland, Oregon		X		X		
Oregon Physicians' Service Portland, Oregon			X			

APPENDIX II

AVERAGE CLAIM RATES AND VOLUMES OF CHAMPUS HOSPITAL FISCAL AGENTS

For year ended March 31, 1976

Fiscal agent	Claim rate		Claim volume	
	Rank	Amount	Rank	Volume
BCA subcontractors				
Ohio-Lima	1	$38.40	51	156
New Hampshire/Vermont	2	28.92	26	2,872
Michigan	3	23.59	12	6,262
Utah	4	23.14	33	2,225
Virginia-Roanoke	5	21.91	40	1,340
District of Columbia	6	20.84	18	3,882
Puerto Rico	7	20.25	43	1,064
Colorado	8	19.43	11	6,355
New York-Syracuse	9	18.72	37	1,438
Ohio-Youngstown	10	17.72	45	729
Ohio-Cleveland	11	17.71	34	2,010
Ohio-Toledo	12	17.46	44	756
Kentucky	13	17.16	14	5,475
New Jersey	14	17.02	16	4,635
Ohio-Columbus	15	16.95	21	3,399
Delaware	16	16.48	46	575
Ohio-Canton	17	16.27	49	343
Pennsylvania-Allentown	18	16.20	50	297
New York City	19	16.05	17	4,235
Rhode Island	20	15.82	38	1,415
New York-Buffalo	21	15.73	41	1,279
New York-Watertown	22	15.66	48	402
Tennessee-Memphis	23	15.14	29	2,620
California-Los Angeles	24	14.83	1	37,832
Washington/Alaska	25	13.79	6	11,062
Pennsylvania-Philadelphia	26	13.08	31	2,361
Maryland	27	12.57	15	5,225
Pennsylvania-Pittsburgh	28	12.56	19	3,753
New Mexico	29	12.37	22	3,364
Ohio-Cincinnati	30	12.34	30	2,397
North Carolina	31	12.06	2	17,602
New York-Albany	32	11.84	35	1,897
Massachusetts	33	11.79	8	9,622
Idaho	34	11.04	32	2,283
California-Oakland	35	10.59	4	14,221
Connecticut	36	10.53	27	2,791
Mississippi	37	9.89	10	8,318
Virginia-Richmond	38	9.46	3	14,334

APPENDIX III

Fiscal agent	Claim rate Rank	Claim rate Amount	Claim volume Rank	Claim volume Volume
Pennsylvania-Wilkes-Barre	39	$ 9.40	42	1,199
Tennessee-Chattanooga	40	9.40	9	8,853
Wyoming	41	9.27	39	1,394
New York-Utica	42	9.00	36	1,622
Arizona (Nevada)	43	8.85	5	12,374
New York-Chautaugua	44	8.40	52	103
Maine	45	8.03	20	3,525
Montana	46	7.97	24	3,232
Oregon	47	7.62	13	5,490
West Virginia	48	7.59	23	3,328
Pennsylvania-Harrisburg	49	7.08	25	3,119
Hawaii	50	6.98	28	2,628
New York-Rochester	51	6.75	47	538
Alabama	52	6.20	7	10,949
Average rate and volume		14.85		4,792
BCA headquarters per claim rate		1.96		-
Total-BCA average per claim rate and total volume		16.81		249,180
Mutual of Omaha		7.11		206,937

AVERAGE CLAIM RATES AND VOLUMES OF CHAMPUS PHYSICIAN FISCAL AGENTS (note a)

For Year Ended March 31, 1976

Fiscal agent	Claim rate Rank (note b)	Claim rate Amount	Claim volume Rank	Claim volume volume
Nebraska	1	$11.31	30	20,587
Colorado	2	10.80	20	38,835
New Hampshire/Vermont	3	10.44	32	19,245
Utah	4	10.40	39	12,738
Delaware	5	9.34	41	5,793
Alaska	6	9.24	40	6,725
New York	7	9.15	8	78,172
District of Columbia	8	8.69	10	63,040
Maryland	9	8.66	29	21,982
Michigan	10	8.36	18	44,465
Kansas	11	8.35	22	31,630
Massachusetts	11	8.35	15	53,687
Iowa	12	7.87	35	15,979
Connecticut	13	7.76	38	14,165
Washington	14	7.67	7	83,129
California	15	7.61	1	590,360
New Mexico	16	7.25	27	23,952
North Dakota	16	7.25	44	4,673
Wisconsin	17	7.14	28	23,115
Kentucky	18	6.96	23	29,365
Tennessee	19	6.92	12	38,727
North Carolina	20	6.82	9	71,914
Georgia	21	6.63	5	87,449
West Virginia	22	6.57	34	18,575
Pennsylvania	23	6.42	11	59,773
Florida	24	6.00	3	261,718
Mutual of Omaha	25	5.86	2	404,748
Missouri	26	5.83	19	40,933
Oklahoma	27	5.79	14	55,917
Louisiana	28	5.66	16	49,776
Maine	29	5.64	31	20,009
Oregon	30	5.60	13	57,976
Nevada	31	5.51	33	17,899

a/Excludes Colorado Dental Service which processed only dental claims for the entire country.

b/Because some fiscal agents had the same claim rate, only 41 rankings are shown.

APPENDIX IV

Fiscal agent	Claim rate		Claim volume	
	Rank (note b)	Amount	Rank	volume
South Dakota	32	5.50	43	4,993
Arizona	33	5.32	6	86,983
Wyoming	34	5.29	42	5,451
Mississippi	35	5.19	21	37,314
Virginia	36	4.99	4	90,178
Minnesota	37	4.93	25	26,490
Arkansas	38	4.82	17	46,837
Idaho	39	4.73	37	14,539
Montana	39	4.73	36	14,660
Indiana	40	3.82	24	27,531
Hawaii	41	3.50	26	24,711
Average		$6.77		62,885

b/Because some fiscal agents had the same claim rate, only 41 rankings are shown.

METHODS USED TO ALLOCATE INDIRECT COSTS TO THE CHAMPUS PROGRAM

Claims volume	--	CHAMPUS claims volume as a percentage of total claims volume for all lines of business is mulitplied by the indirect costs to be allocated.
Labor dollars	--	CHAMPUS salaries and wages as a percentage of total salaries and wages is multiplied by the indirect costs to be allocated.
Direct hours	--	Direct hours charged to CHAMPUS as a percentage of direct hours charged to all lines of business is multiplied by indirect costs to be allocated.
Machine utilization	--	CHAMPUS utilization of data processing and office machines as a percentage of utilization by all lines of business is multiplied by indirect costs to be allocated.
Square footage	--	CHAMPUS square footage as a percentage of square footage occupied by all lines of business is multiplied by indirect costs to be allocated.
Mail volume	--	CHAMPUS mail handled as a percentage of total mail handled is multiplied by indirect costs to be allocated.
Number of personnel	--	CHAMPUS personnel as a percentage of total personnel is multiplied by the indirect costs to be allocated.