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Insurers Are Overestimating Costs, Lowering Rebates Owed to Policyholders

MHE Staff

A recent study from American Accounting Association finds health insurance companies are overestimating costs associated with patient care to avoid triggering rebate provisions in the Affordable Care Act (ACA).

According to Andrew Van Buskirk, co-author of the study and an associate professor of accounting at Ohio State University, the more likely companies were forced to issue refunds to policyholders, the more likely those companies would overestimate forthcoming costs. This would then allow them to reduce or avoid paying the refunds.

Language in the ACA is most likely to blame. The ACA requires insurers to spend at least 80% of their premium revenue on policyholder benefits – such as paying claims. If insurers don't, they're required to refund the difference to their policyholders. From 2011-2017, insurers refunded approximately \$4 billion to policyholders, according to the study.

To track insurance costs and revenues, the ACA requires health insurers to file annual reports of their premiums, estimated claims, and a relative measure of claims to premiums called the "medical loss ratio," or MLR. Each year's MLR includes claims that have been paid and an estimate of claims the company will have to pay in the future for an event that already happened.

Insurance companies base each reported MLR on a rolling three-year average. For example, the MLR report for 2018 includes claims estimates from 2016, 2017 and 2018. The most recent report's figures would include estimated and realized costs related to events that took place in 2018. However, the figures reported in 2018 for the 2016 year should include fewer estimates and more paid costs, making the older estimates more accurate.

Found by researchers were estimates were overstated in situations where more accurate estimates would have triggered higher rebate payments.

"We estimate that about 14% of insurers engage in strategic overestimation, costing policyholders hundreds of millions of dollars in unpaid rebates," says Evan Eastman, co-

author of the study and an assistant professor of risk management and insurance at Florida State University.

David Eckles, co-author of the study and a professor of risk management and insurance at the University of Georgia, said if you create an incentive, companies are going to respond to it.

"In this case, that means overestimating costs to avoid paying rebates. Regulators could limit those incentives by focusing solely on paid costs each year, or by incorporating a clawback provision to account for previously overestimated costs," Eckles said.

"Accounting-based regulation can be a powerful tool," Van Buskirk says. "But the lack of ACA provisions to prevent manipulation, and the lack of oversight, limits the effectiveness of this regulation."