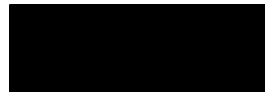


Defining Markets in the Health Insurance Industry

NATIONAL ECONOMIC
RESEARCH ASSOCIATES

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Consulting Economists

The Historic View

- **Pre-1999**
 - **Geographic Market: at least Statewide, even National**
 - **Product Market: Self- and Fully-Insured**
All Products: Indemnity, PPO & HMO

- **June 1999 – Aetna-Prudential Consent**
 - **Geographic Market: MSA level...Dallas and Houston**
 - **Product Market: Fully-Insured HMO and HMO-based POS only**

- **Post-1999**
 - **No new precedents**

Can an MSA be a Relevant Geographic Market?

- **Local health care delivery through local provider networks used to support the MSA as the geographic market**
- **Licensure for managed care plans requires physician and hospital networks. Generally only a single license is needed to operate statewide.**
 - **Typically, must notify regulator of additions to provider network to assure coverage before expanded plan is marketed**

But...

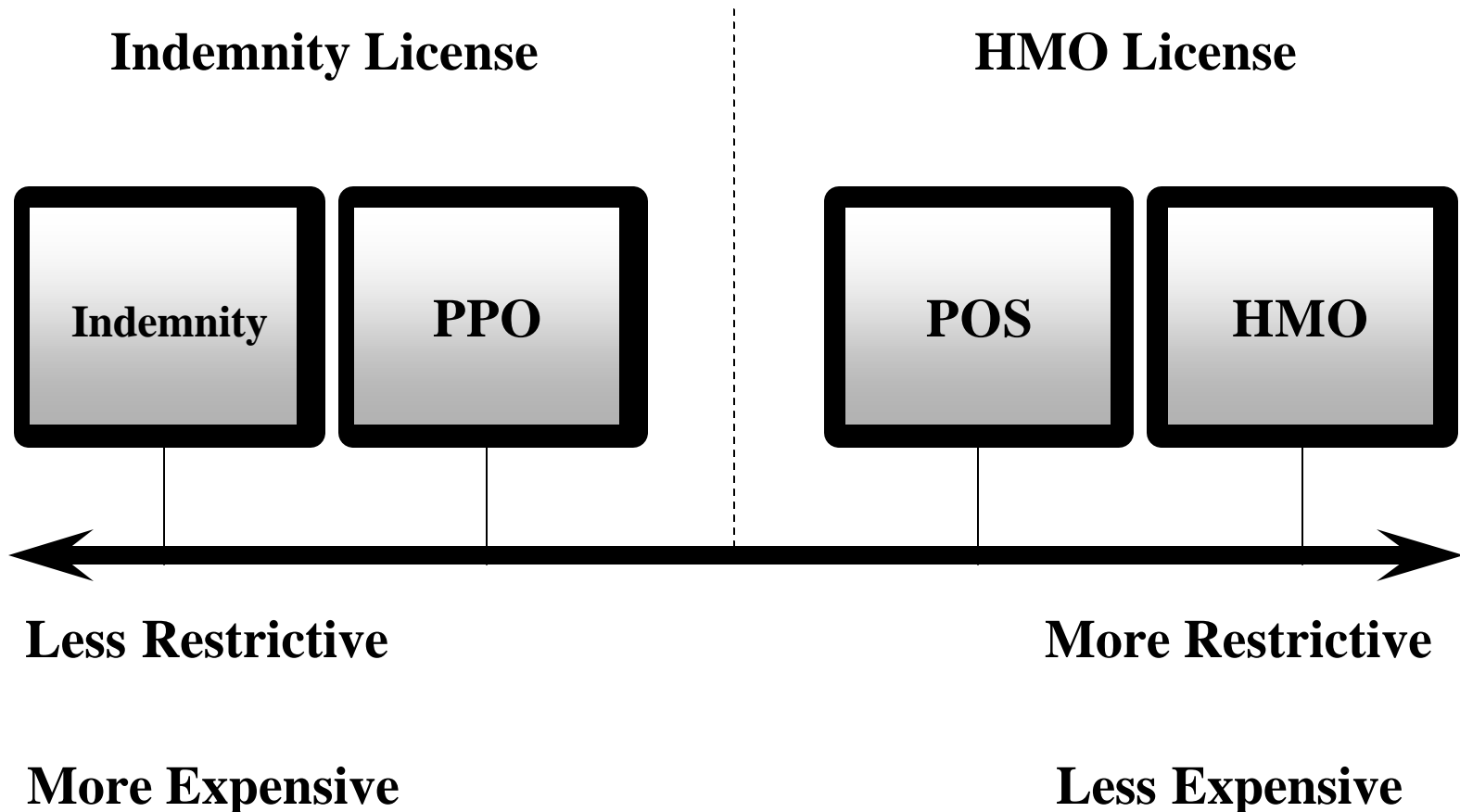
- **Ease of geographic expansion makes supply substitution important to defining the relevant market**

Do Self-Insured Plans Compete with Fully-Insured Plans?

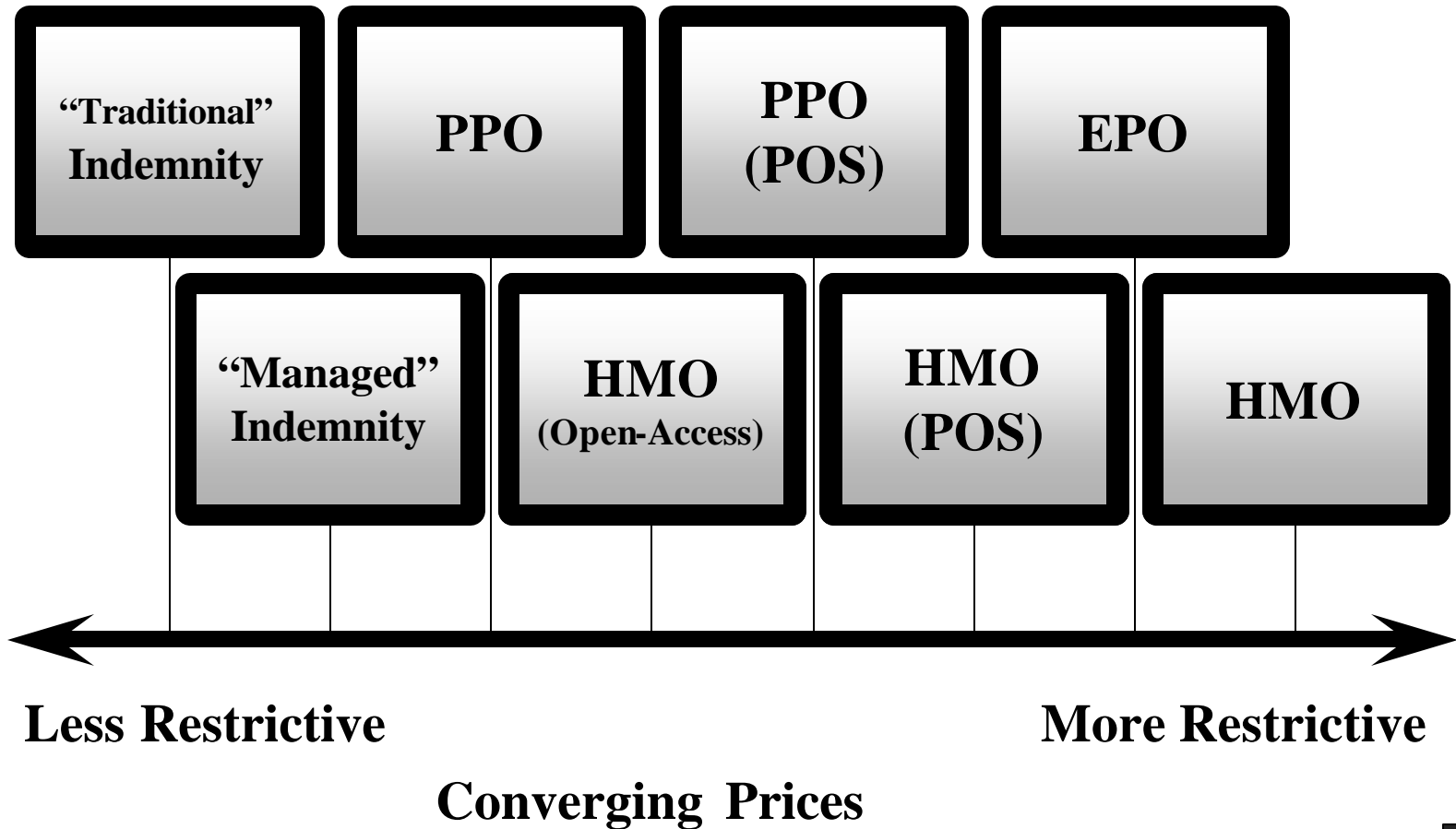
- **Employees generally do not know funding source**
- **Most large insurers offer fully-insured and self-insured plans**
 - **Indemnity, PPO, POS and HMO plans can be self- or fully-insured**
- **Local TPAs generally available to offer services, with rental networks available**
- **In most cases, employers have choice of fully-insured and self-insured plans**
 - **Individual and small group segments are usually highly regulated**

Do PPOs Compete with HMOs?

The Health Insurance Product Continuum



The Health Insurance Product Continuum



Do PPOs Compete with HMOs?

- **To test the proposition, DOJ used choice-modeling in Dallas and Houston to derive an elasticity**
 - **Obtained data from competing health plans and employers, which allowed them to study the choices made by employers and employees**
 - **Estimated elasticities less than -3**
 - **With low margins, critical elasticity close to -6**
 - **So, DOJ concluded that HMOs and PPOs were in separate markets**

Do PPOs Compete with HMOs?

- **NERA simulation**
 - **Test whether a proper model needs both benefit design and employee contribution**
 - **In simulation, with both factors omitted we obtained an estimated elasticity below -1**
 - **Accounting for choice and benefit design brought the elasticity estimate close to the known elasticity from the simulated data of -11**
 - **Conclusion: missing data creates a bias toward challenging the merger**

Do PPOs Compete with HMOs?

- **Analysis of Mercer data**
 - **National survey of employers**
 - **Includes limited information on benefits and employee contribution**
 - **Elasticity estimates are consistent with conclusion that PPO, POS and HMO plans are all in same market**
 - **Nested logit grouped HMOs and PPOs together**

Do PPOs Compete with HMOs?

- **Yes, generally speaking the empirical evidence supports the conclusion that HMOs and PPOs compete and are therefore in the same relevant market**
- **Moreover, the world has changed...**

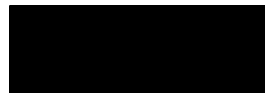
Where are We Now?

- **The DOJ has been asking the right questions**
- **The tools that were used in 1999 are still the right tools to use today**
- **The key to studying all three questions is to look at how the health plans, employers and employees switch, when presented with opportunities**
- **Finally, any analysis today must look at new products that may emerge as a result of the managed care backlash.**

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END OF PRESENTATION

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