



# Large Employers Evaluate Risk-Adjustment Tools for Purchasing Health Insurance

## Developing and applying risk-adjustment tools

### SUMMARY

From 1993 to 1997, the Pacific Business Group on Health, San Francisco, tested the predictive power and practical application of several risk-assessment tools used by large employers that offer their employees a choice of two or more health plans.

Information on competing health care plans is vital to employers. For example, if employers know whether one plan's enrollees are sicker and consequently use more services—they can accurately assess whether that plan is priced higher because sicker employees have selected it or because the plan is less efficient.

This project was part of the Robert Wood Johnson Foundation (RWJF) national program *Changes in Health Care Financing and Organization* (HCFO) (for more information see the [Program Results Report](#)).

### Key Findings

- Using the risk assessment technique that relies solely on employee demographic information, the investigators found that neither the largest companies nor the lowest risk companies had the best prices.
- They also determined that the addition of employee health status information improves the precision of risk assessment models.

### Key Results

- Member companies used these results to collectively negotiate with 15 HMOs throughout California, requesting that each HMO submit a single bid for the whole group.
- Through pooling their volume and risk, the companies achieved 1995 rates that were 5 to 10 percent lower than their 1994 rates.

## **Funding**

RWJF supported the project with a grant of \$614,323 between June 1993 and March 1997.

## **THE PROBLEM**

Information on competing health care plans is vital to employers, the primary purchasers of health insurance. For example, if employers know the relative risk of enrollees in any given health plan—whether one plan's enrollees are sicker and consequently use more services—they can accurately assess whether a plan is priced higher because sicker employees have selected the plan or because the plan is less efficient. Employers can then use this information to negotiate better prices, fairly compensate plans with relatively high-risk enrollees, and direct employees to the most efficient and appropriate plans.

## **THE PROJECT**

This study, which was directed by the Bay Area Business Group on Health (BBGH), a nonprofit business health coalition headquartered in San Francisco, tested the predictive power and practical application of several risk assessment tools used by large employers who offer their employees a choice of two or more health plans. Additional funding for this project was provided by BBGH, Kaiser Permanente Northwest, and the University of California-San Francisco.

The risk-assessment techniques studied included: use of demographics alone (e.g., age, sex, family status), use of demographics and employee-reported health status, and use of demographics and employer personnel file socioeconomic information (e.g., income, education, job classification). BBGH member companies used the risk-assessment tools in their negotiations with health plans and to calculate employee premium contributions.

## **FINDINGS**

Using the risk-assessment technique that relies solely on employee demographic information, the investigators found that neither the largest companies nor the lowest risk companies had the best prices. While some of the price variation was attributable to utilization differences, most was based on the historical relationship between the employer and the health plan, or other arbitrary factors.

Based on their overall analysis, the investigators determined that the addition of employee health status information—over and above commonly used demographic information—improves the precision of risk assessment models. However, they noted that the constraints associated with conducting surveys to gather health status information

(e.g., costs, time, bias) may bring into question the "real-world" acceptance and application of such a model.

## Results

BBGH member companies collectively negotiated with 15 HMOs throughout California, requesting that each HMO submit a single bid for the whole group. Through pooling their volume and risk, the companies achieved 1995 rates that were 5 to 10 percent lower than their 1994 rates.

## Communications

An article was published in the Winter 1995 issue of *Health Affairs*.

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