DIRECT MANAGED CARE CONTRACTING

Everything You Always Needed to Know About Employer-Owned Networks*

***That Your Carrier, PPO, or HMO Never Told You**

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What exactly is direct managed care contracting?
Direct managed care contracting is an "outside-the-box" approach to managed care in which a self-funded employer contracts directly with hospitals and physicians to be network providers for the employer's managed care plan. Direct employer-owned networks create a true "buyer/seller" relationship between employer and provider that eliminates the managed care middleman. As a vital alternative to conventional HMO and PPO networks, direct contracting can reduce health plan costs and service problems, while giving employees access to the network providers they want everywhere they need them.

What kind of employer is the best candidate for direct contracting?
Major employers that offer (or want to offer) managed care benefits to geographically dispersed employees through a self-insured health plan are good candidates for direct contracting. Employers who have employees concentrated in outlying areas or in communities where commercial managed care networks are limited, inadequate, or unavailable also make good candidates. Employers whose existing HMO and/or PPO networks are not *consistently* demonstrating good service or strong savings are some of the *best* candidates for direct contracting.

What size employers benefit most from direct contracting?
While any size company can contract with doctors or hospitals, direct contracting appears most effective for employers who have larger numbers of employees relative to the size of the communities in which those employees reside. As such, an employer with 50 or 75 employees in a small town may be considered a "large" local employer, while 250 or 500 employees may be considered "large" in a more moderately-sized community. The point is that companies with a limited number of employees can often gain *considerable* leverage with local medical providers, leverage that can have an immediate impact on containing claims fund expenditures and reducing overall plan costs. Direct provider networks have been successfully established in many areas of the country in which the contracting employer had relatively limited employee populations.

With so many managed care networks already available, why contract directly with providers?
HMOs, PPOs, and other managed care companies simply cannot provide network access everywhere it is needed. Where networks *are* available, they may be deficient in the number or geographic distribution of doctors or hospitals, and may have difficulties in obtaining and maintaining provider agreements with the doctors who are most popular with employees. Ready-made networks are usually "take-it-or-leave-it" propositions, too, with few, if any, options for network customization to suit an employer's specific needs. Double-digit rate increases, network

instability, and deteriorating customer service are forcing many employers to seek out alternatives to conventional managed care. From every perspective, direct contracting can often represent the best alternative available.

Is direct contracting effective in metropolitan areas already served by HMOs and PPOs?

It depends. Most metropolitan areas have several or more commercial managed care networks. Unfortunately, many metropolitan HMO and PPO networks have experienced operational or financial difficulties; encountered instability and attrition among contracted providers; raised premiums or network access fees to unreasonable levels; or failed to demonstrate true bottom-line savings to their employer clients. Direct provider agreements address many of the problems and shortcomings that affect commercial networks and put control of the provider network squarely in the hands of the employer. Even where there are many commercial managed care choices, direct contracting should *always* be considered as an alternative.

What if employees are spread out in limited numbers among many locations?

Direct contracting can be ideally suited for limited numbers of employees spread among many locations. Instead of adding an entire HMO or PPO network in each area, an employer can contract directly with specific doctors and hospitals employees already use or want to use. This eliminates local network access fees and the need to administer yet another HMO or PPO network.

Are medical providers really interested in directly contracting with employers?

Contrary to what employers may be told by carriers, HMOs, and PPOs, doctors and hospitals are usually *quite* interested in direct contracting. While these same doctors and hospitals may show little interest in commercial managed care agreements, they *do* increasingly understand the value of doing business *directly* with local employers, regardless of the actual number of employees involved. Because of the "win-win" nature of direct agreements, providers have little or nothing to lose and much to gain from doing business directly, even when there are few employees and limited patient dollars.

When is it <u>not</u> worthwhile to directly contract with providers?

If an existing HMO or PPO network is delivering on its promises of cost-containment and client service, and if employees are satisfied, it may not be worthwhile to directly contract with providers. Direct contracting is not intended to replace those networks that are *truly* working in the best interests of the employer and employees. Considering the costs and time necessary to develop a direct network, it may be better to keep a network that's doing its job very well rather than to replace it with a direct network.

My company's carrier (or managed care vendor) is supposedly developing networks in smaller cities and rural areas, so why not wait?

From the perspective of a lot of employers, network development by carriers, PPOs, and HMOs seems to be taking place everywhere *except* where the employer needs it. In an effort to placate clients, commercial managed care companies often promise future development of networks in specific areas (or alignment with existing local networks) and suggest that their clients wait. But, unless those arrangements hold the potential for adequate member revenue and profits, network development may actually never take place. Carriers, PPOs, and HMOs typically don't base network development on individual client needs, but rather on their own financial objectives and the *aggregate* needs of their client-base. Rather than wait for vague promises of network development to materialize, direct networks can be developed quickly and cost effectively, specific to the employer's *own* needs and those of its employees, when and where those networks are needed.

Why do PPOs and HMOs say that providers in outlying areas, who won't contract with them, won't contract with anyone?

Many doctors and hospitals in outlying areas, wary of disadvantageous agreements often pushed upon them by commercial managed care companies, do tend to resist managed care contracting. In contrast, the direct contracting approach quickly demonstrates to providers the fundamental differences between commercial agreements and direct agreements, and the inherent advantages of doing business *directly* with employers. Once they're offered the mutually advantageous "win-win" direct agreements, most providers actually welcome the opportunity to contract with employers. Direct contracting has actually proven to be quite attractive to medical providers in outlying areas, including many providers who might otherwise reject agreements offered them by commercial managed care organizations.

My company's employees live in outlying areas serviced by only one hospital and a limited number of physicians who will get the patients anyway. Why would providers in those areas sign direct agreements?

They sign because it's a good business decision. Even though providers in outlying areas may get the patients anyway, most doctors and hospitals realize that employers in their communities simply *can't* offer managed care to employees without a network of participating providers. Signing a direct agreement establishes a working business relationship between provider and employer, one that has definite advantages for the provider. In consideration for a discount or reduced fee, direct agreements generally provide for quicker reimbursements, higher benefit payment levels, and better access to the ultimate payer (the employer). Doing business directly with employers in their own town is also a gesture of good community relations for any physician, medical group, or hospital to demonstrate.

If providers are so willing to negotiate, why doesn't my managed care vendor have a network there?

Your carrier or managed care vendor may have tried and failed to negotiate agreements with providers, or may not have attempted it at all. The truth is, that as the differences and distinctions between commercial managed care and direct contracting become better understood by providers, those providers will generally embrace the concept of direct agreements. But they may never change their opinion of conventional managed care.

With provider sentiment against managed care running high, why would doctors and hospitals welcome a direct agreement?

Providers welcome direct agreements for the very reason that they are not like conventional managed care agreements. Physicians have complained for years about the often-adversarial agreements and disadvantageous reimbursement terms they've been forced to accept by carriers, HMOs, and PPOs. This has created a largely negative perception of managed care in general and contracts in particular. Direct agreements represent the opportunity to do business directly with the employer, who is both health plan sponsor and payer, and avoid the overly controlling managed care middlemen who many providers have grown to disdain. The fair reimbursements, reasonable contractual terms, and "win-win" nature of the whole direct contracting process are a refreshing change for most providers. Many hospitals and doctors have expressed the sentiment that they would gladly exchange their commercial managed care agreements for direct agreements with the same employers that those carriers, HMOs, and PPOs otherwise represent.

Does direct contracting mean my company will own the network?
Yes, though ownership essentially means owning the contracts with the providers, who, in turn, deliver the medical care as participating providers in the employer's network.

Isn't A. J. Lester & Associates the middleman?
No. Direct managed care contracting eliminates the need for a middleman. A.J. Lester & Associates is never a party to any of the contracts, but simply negotiates the direct agreements on behalf of our corporate clients with medical providers. We're paid directly by our clients for developing their direct networks and receive no remuneration from the providers with whom we negotiate agreements.

Are the direct networks "remarketed" to other employers or managed care plans?
No. Each directly contracted network is owned by the employer itself and is intended for the exclusive use of the employees and dependents covered by the employer's health plan. In essence, each network is customized to the needs of the employer and is maintained for the specific use of eligible plan participants.

Who writes the contracts and sets up the financial terms of the agreements?
A.J. Lester & Associates has spent years refining the contractual and financial terms to assure that direct agreements can be negotiated quickly and successfully with medical providers. While the formulation of financial terms for reimbursing providers across many networks can be complex, we have developed proprietary pricing methodologies that can be successfully used in any given geographic area. These contracts and reimbursement terms consistently work because they equitably meet the providers' needs and expectations, without compromising the interests of the employer or the hard-dollar savings achieved for them.

Who handles the actual contract negotiation and development of the network?
Since A.J. Lester & Associates has successfully negotiated tens of thousands of direct agreements, we understand what it takes to handle the process quickly, efficiently, and with maximum impact. Whether contracting with a single physician in private practice; a medical group of hundreds of multi-specialty physicians; a small rural hospital; or a regional hospital system, we handle all facets of network development to create a strong business relationship between the employer <u>and</u> the providers who ultimately comprise their networks.

How is it determined which providers will comprise the network?
Depending on the number of employees, and the size and distribution of the medical community, each network is configured to provide an adequate number of hospitals, primary care physicians, and specialists to meet the needs of employees and dependents. Direct networks are built around the doctors and hospitals employees already use or prefer to use. By examining utilization data to determine which providers have been historically used by employees; deciding which additional specialties are necessary for the network; and by asking employees which providers they want, the

network can be configured with a high degree of certainty that employees will be satisfied with the selection of doctors and hospitals. Ultimately, however, it is the employer who decides on the size and composition of the network. This customized approach may be impossible for commercial managed care networks to accomplish because they must configure their networks based on the broad aggregate needs of many employers, not just the specific needs of one.

Who handles the ongoing management of the networks?

Once direct agreements are in place, and the necessary provider information regarding the employer's networks have been provided to the claims administrator, some employers choose to either handle network maintenance in-house or have their claims administrator handle it. A.J. Lester & Associates also handles network maintenance for major employers whose direct networks we've developed. Since direct agreements are non-adversarial, unobtrusive, and self-renewing, once they are in place, contracts can continue indefinitely with minimal maintenance along the way.

Will my current carrier, TPA, or managed care company process claims for direct networks?

Processing claims and administering benefits for employer-owned provider networks are *well within* the technical/systems capabilities of most carriers, TPAs, and MCOs. Though most prefer for clients to use the available networks *they* own, lease, and/or market, some claims administrators are responding to client demand by administering direct networks. By acknowledging that commercial networks don't *always* meet client needs and by paying claims for direct networks, progressive claims administrators can help clients to both contain costs and offer managed care benefits to more employees in more locations. Ask your carrier, TPA, or managed care company if they will administer claims for your direct networks. If they can't (or won't), there are lots of options for finding a claims administrator that can.

Are direct contracts stable? How often do they need to be re-negotiated?

When direct agreements are designed and negotiated with the proper expertise, to be non-adversarial, fair, and mutually beneficial to both parties, those agreements are the most stable and long-lived contracts available to employers and providers. Because they're "win-win" agreements, once they're negotiated, they generally stay firmly in place, automatically renewing annually, with little necessity to re-negotiate terms during the life of the agreement.

What kind of fixed cost savings can direct contracting produce?

The biggest, most immediate fixed cost savings are the elimination of per-employee-per-month (PEPM) access fees. Because PPO network access fees recur month after month for years on end, the fixed costs of PPO networks can be substantial. With direct contracting, after initial network development costs, the employer *owns* the network so there are no recurring PEPM access fees. Ultimately, fixed cost savings can be estimated by factoring the number of covered employees by the number of years the network will be in place and comparing it to the costs of accessing a PPO network for the same number of employees during the same time period.

How much money can direct contracting save my company's claims fund?

Savings are influenced by many factors, including the number of employees; size and number of networks; health plan design; and contractual terms and discounts negotiated with providers. Though savings vary from employer to employer, a well-designed and developed direct network should produce savings of 15-40%, or more, on total claims fund expenditures, especially when such networks are implemented in areas where employees previously had little or no managed care network access. For employers with multi-million dollar health plan claim funds, direct contracting has the proven potential to create millions of dollars in savings each year. In direct contracting, there are no middlemen to obfuscate savings estimates and all financial and contractual terms are always *fully disclosed* to both parties. As a result, potential savings can be realistically projected and reported, without the need to inflate or embellish the actual savings achieved.

How much does direct contracting cost?

The cost of developing direct networks is a function of the number and complexity of provider contracts negotiated. To maintain objectivity and to fairly account for *every* aspect of the direct contracting process, it is recommended that network development be based upon a flat hourly consulting fee. Return on investment to the employer from a successfully developed direct network can average $20 (or more) in savings for every $1 spent on the actual network development.

About A.J. Lester & Associates, Inc.

A.J. Lester & Associates, Inc. is a health care benefits consulting firm founded by Howard "A.J." Lester with the vision of helping change the face of managed care in this country by facilitating direct agreements between major employers and medical providers.

With over twenty-five years in the health benefits field, A.J. Lester's credentials include his work with the managed care subsidiaries of two major insurance carriers and many years as a consultant for one of the world's largest benefits consulting firms. Over the past ten years, A.J. has specialized in direct managed care contracting, working on behalf of such major corporate clients as SYSCO Corporation, Perdue Farms Incorporated, Parker Hannifin Corporation, Global Marine Corporation, and Blue Bell Creameries, L.P. A.J. has negotiated direct agreements with tens of thousands of physicians and hundreds of hospitals across 35 states.

A.J. Lester & Associates is committed to service excellence and to improving the quality of the business relationship between the employer and medical provider, the true "buyer" and "seller" in the managed care equation. By addressing the real needs of both parties in a positive way, A.J. Lester & Associates has helped facilitate strong and mutually beneficial networks that have stood the test of time and have successfully fulfilled the true objectives of managed care for both employers and providers throughout the country.

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