

Rhetoric vs. Reality: Comparing Public and Private Health Care Administrative Costs

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March 1994

Executive Summary

Government programs incur significantly more administrative costs than private insurance in providing health benefits. For every administrative dollar spent by the private insurance industry, government spends \$1.66. That is the conclusion of this study by the Council for Affordable Health Insurance.

The review of Medicare and Medicaid expenses was prompted by the often repeated claim that government has lower administrative costs than does the private health insurance industry. The proponents of that view conclude that large amounts of money could be saved if government administered health benefits for the entire country.

The Council's findings are to the contrary:

- * Medicare and Medicaid spend 26.9 cents for every dollar of benefits versus 16.2 cents for private insurance.
- * The claims of greater efficiency for government programs are based on numbers that omit many of the true costs of administration by the government.
- * Government's true costs for administering Medicare and Medicaid are spread through all three branches of the federal and state governments and their numerous departments. These "hidden" costs have not been attributed to health care until this study.

The Council reviewed federal and state government budgets and allocated costs for departments in proportion to their time and resources spent on Medicaid and Medicare.

Private industry costs are based on the *SimuCare* national health care data base developed in 1993 by Milliman & Robertson, Inc.

The Council's report is a guidepost in the current debate on health care reform. Private industry should be looked to for the most cost effective administration in the health care field.

Introduction

A major focus of the current debate on health care reform is the cost of delivering medical services. Supporters of single-payer and managed competition systems point to the administrative costs of the insurance industry as a wasteful use of health care dollars.

Medicaid and Medicare are often cited for their administrative costs of 5% and 2%, respectively. In comparison, private insurance reports an industry cost average of between 12% and 20%.

The Council for Affordable Health Insurance undertook this study in order to make a realistic comparison of the efficiency of government health programs and private health insurance.

Contrary to the assertion that government has much lower administrative costs than the private insurance industry, in an "apples-to-apples" comparison, government spends more than half again as much (66% more) to provide a dollar of Medicare and Medicaid benefits as private insurance spends to provide a dollar of health insurance benefits.¹

The Council has found that government masks the true cost of financing health services to senior citizens on Medicare and to poor Americans on Medicaid. These expenses are hidden under the complex and bureaucratic reporting and tracking systems used by government.

Central to this study is the recognition that there are more costs in running the Medicare and Medicaid programs than just paying benefits. For example, the legislative and executive branches devote time and resources to the management and direction of these programs: passing laws, writing regulations, holding hearings, commissioning studies and the like. The judicial branch expends resources resolving the legal questions surrounding Medicare and Medicaid. In addition, the costs of programs and activities benefiting Medicare and Medicaid exist in a number of other federal budget categories including Education and Training, Labor and The National Institutes of Health.

¹Traditionally, private insurance expenses are reported as a relationship to premiums paid ("loss ratio"). Since government programs do not have premiums as the sole source of funding, it is necessary in this issue brief to refer to administrative costs as a percentage of benefits paid.

Beyond Medicare and Medicaid program and activity costs, government operates at a deficit and issues debt to fund operations. Paying interest on that debt represents an enormous cost to government. A portion of the interest must be allocated to the Medicare and Medicaid programs since debt enables government to provide such programs.

This study estimates the actual administrative costs of Medicare and Medicaid and compares that data to the costs of the private insurance industry. The study involved extensive analysis of the 1993 budgets of the federal government, and the state of California as well as the 1992 Statistical Abstract of the United States. This report does not measure or consider the administrative costs borne by providers or the time and paperwork borne by patients in dealing with either the public or private system.