

Pa.'s largest health insurers talk merger

Independence Blue Cross of Philadelphia and Highmark Inc. of Pittsburgh said a combination could happen by September.

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July 14, 2006

Talks between Independence Blue Cross of Philadelphia and Highmark Inc. of Pittsburgh could result in a plan to merge Pennsylvania's two largest health insurers by September.

"If this thing comes together, we're thinking maybe Labor Day," said M. Walter D'Alessio, chairman of Independence's board, which includes 35 Philadelphia-area business, professional and labor union leaders. "These are large and complicated companies with lots of moving parts."

"There are discussions going on," but there has been no merger vote at Highmark, although a decision is likely "in two to three months," said Bill George, a Highmark board member and head of the Pennsylvania AFL-CIO labor union federation, whose members also hold several seats on the Independence board.

The companies have talked about mergers before without reaching agreement. "Both companies understand" they need to work together "to grow their business, achieve economies of scale, and improve their customer service," Highmark spokesman Michael Weinstein said.

"We regularly talk with Highmark" and other insurers, Independence spokeswoman Elizabeth Williams said. The two companies have collaborated on state-sponsored health insurance for the working poor and for low-income children and Medicare Part D drug-prescription coverage for the elderly, she noted.

Weinstein and Williams had no comment on how the combined Blues might operate or the impact a merger could have on employers, workers, doctors and hospitals.

Highmark and Independence belong to the national network of nonprofit "Blue" insurance cooperatives that dates to the 1930s.

In Pennsylvania, Highmark was originally a "Blue Shield" company, managing relationships with physicians, while the other Pennsylvania-based "Blue Cross" companies, including Independence, focused on hospitals. Over the years, those lines have blurred.

Independence collected about 28 percent of Pennsylvania's \$28 billion in yearly health insurance premiums thanks to its dominant market share around Philadelphia, according to the state insurance department's most recent figures, which date to 2004. Highmark was right behind with about 27 percent, in western and central counties. Overall, Highmark's out-of-state operations make it a bigger company than Independence.

Blue Cross/Blue Shield affiliates in California, Michigan, and other states have consolidated to compete with well-funded private insurers.

Even as the number of insured workers has dropped in Pennsylvania in recent years, the Pennsylvania Blue plans say they have faced increased competition.

Aetna Inc., which is based in Connecticut but operates much of its health insurance business from offices in Montgomery County, says its health maintenance organizations and preferred provider organizations now represent 30 percent of the "commercially insured population in the Philly area," according to spokesman Walter Cherniak Jr.

Insurance brokers say a merger could lead to back-office consolidation and less paperwork for middlemen and employers. But Independence and Highmark also have to please politicians, regulators, and constituents worried about merger-related job and service cuts. Independence employs about 9,500 people in the Philadelphia area, ranking with The Vanguard Group Inc., Merck & Co. Inc., and other major leading employers.

"You can operate out of two cities," D'Alessio said, perhaps with Philadelphia specializing in "traditional plans" while Pittsburgh handles vision, dental and other specialized businesses.

Separately, George, the AFL-CIO official, called for regional, not centralized, operations. "It would be ludicrous to move everything to Pittsburgh or to Philly," he said. If they were perceived to be abandoning either home market, he said, "Aetna and United Health would eat [the Blues] alive."

Tom Knox, a former insurance and banking executive and current candidate for mayor of Philadelphia, questioned the value of a Blue-on-Blue merger. He said the companies would do better selling out to expansion-minded for-profit companies like Aetna or United Healthcare. Knox was formerly an official of United Healthcare.

Ten years ago, Aetna spent \$8.9 billion to buy U.S. Healthcare Inc., a Blue Bell insurance company. But now that it is one of the nation's biggest health insurers, Aetna hasn't shown interest in buying more members, preferring to go after specialized products and markets, spokesman Alfred Laberge said. United Healthcare's chief executive officer for Pennsylvania, Thomas Pappas, could not be reached for comment.

Knox, state officials, and insurance industry executives say a final conversion of the Blues to for-profit status could enable the Commonwealth of Pennsylvania to extract a payment that could be applied to coverage of the uninsured or other public-health purposes. Knox estimated that the potential value of such a payment could top \$3 billion, given the size of the plans.

Independence Blue Cross board member Patrick J. Eiding, who heads the Philadelphia Central Labor Council of the AFL-CIO, and three other Independence board members said talks with Highmark have been progressing.

Eiding said he would like to see any resulting company remain a nonprofit. "People criticize IBC," he said, "but there's a lot of things they can do that you don't get when it's a regular business."

Philadelphia lawyer Don P. Foster, a partner in the Klehr, Harrison, Harvey, Branzburg & Ellers law firm and a member of the Highmark board's executive committee, sees a possible merger as a good competitive move. "To the extent that a greater critical mass could be developed in the Blues in Pennsylvania, it would be better," Foster said. "I think it's good for Pennsylvania, good for the members."

Philadelphia's city-funded consumer advocate, Lance Haver, said he expected to oppose any Blue Cross merger that reduced the companies' nonprofit obligations. But, he said, many public-health activists likely would agree to a merger if it resulted in greater funding for covering the uninsured.

"Health insurance should be done on a nonprofit basis," Haver said. "Blue Cross was founded to be a nonprofit cooperative. That's how you best meet everyone's needs. That's the goal when you're nonprofit. A for-profit company's goal is different - it's to create profit for the owners."