

Kaiser earnings are up 30%

HMO slowed growth rate of its costs

By Victoria Colliver
CHRONICLE STAFF WRITER

Kaiser Permanente's health plan and hospitals posted solid earnings in 2006, with net income up 30 percent over the previous year, the health maintenance organization reported Thursday.

Oakland's Kaiser said it earned \$1.3 billion last year compared with \$1 billion in 2005. Revenue increased to \$34.4 billion from \$31.1 billion.

At the same time, the HMO's 2006 operating margin was a relatively modest 2.8 percent, up slightly from the 2.6 percent margin recorded in 2005. Operating margin, a key measure of the financial performance of a hospital system, had hit a robust 5 percent in prior years.

In the quarter ended Dec. 31, Kaiser posted net income of \$215 million and operating reve-

nue of \$8.7 billion, swinging from a loss of \$211 million and revenue of \$7.9 billion in the fourth quarter of 2005.

The gain in earnings for the year was due in part to slowing the growth rate of costs, Chief Financial Officer Kathy Lancaster said in a statement.

Kaiser's financial improvement came despite a series of problems. During 2006, Kaiser faced a crisis that led to the closure of its Northern California kidney-transplant program. After allegations of mismanagement in the program, state and federal regulators conducted investigations and levied fines.

Meanwhile, the HMO faced breakdowns in its nearly \$4 billion electronic medical information system. Concerns over outages in the system, called Health-Connect, prompted the state Department of Managed Health Care to request that Kaiser provide the agency with information on backup procedures. The department is evaluating Kaiser's response, spokeswoman Lynne Randolph said.

In addition, Kaiser had to make

heavy outlays to meet earthquake-safety standards and expand its network of hospitals and other facilities. Capital spending grew to \$2.8 billion in 2006 from \$2.5 billion the previous year.

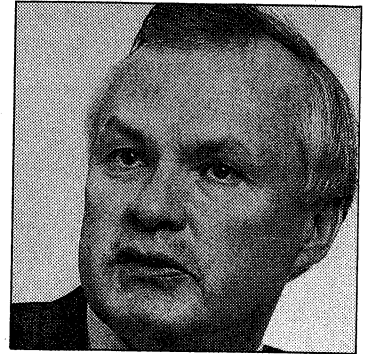
Despite the challenges, Kaiser officials characterized 2006 as a positive year.

"We are on our way to completing the largest civilian deployment of electronic health records in the world and constructing new hospitals and clinics to meet the growing demand for our services," said Kaiser's chief executive, George Halvorson, in a statement. "When you put it all together, Kaiser is well positioned to meet the challenges facing health care."

Halvorson had warned late last year that if Kaiser didn't curb spending it could incur billions in losses in future years due to high operating costs and decreasing reimbursement from Medicare and other sources.

Kaiser's generally healthy financial report prompted some industry experts to question its recent premium increases.

Kaiser's message to employers "was they needed the increases to



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George Halvorson had warned about cutting Kaiser spending.

maintain their financial health and painted a pretty pessimistic picture of the future," said Charles Rosson, senior vice president at Woodruff-Sawyer & Co. in San Francisco, an insurance brokerage and consulting firm. "I would hope this means they've addressed whatever financial concerns they have and their future rate increases will be more in line with the marketplace."

E-mail Victoria Colliver at vcolliver@sfchronicle.com.