

## **Statutory Issue Paper No. 100**

### **Health Care Delivery Assets—Supplies, Pharmaceuticals and Surgical Supplies, and Durable Medical Equipment**

#### **STATUS**

**Finalized June 23, 1998**

**Original SSAP and Current Authoritative Guidance: SSAP No. 73**

**Type of Issue:  
Health Entities**

#### **SUMMARY OF ISSUE**

1. This issue paper applies only to reporting entities which directly provide health care services to subscribers, members or policyholders. Such providers acquire and retain assets not directly addressed in current statutory guidelines. These assets, commonly referred to as “health care delivery assets”, are assets used in connection with the direct delivery of health care services in facilities owned or operated by the reporting entity and include supplies, pharmaceuticals and surgical supplies, and durable medical equipment.
2. The purpose of this issue paper is to establish statutory accounting principles for health care delivery assets—supplies, pharmaceuticals and surgical supplies, and durable medical equipment that are consistent with the Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy (Statement of Concepts).

#### **SUMMARY CONCLUSION**

3. Supplies, pharmaceuticals and surgical supplies, and durable medical equipment meet the definition of assets established in *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets* (Issue Paper No. 4). Pharmaceuticals and surgical supplies, and durable medical equipment held by reporting entities and used for the direct delivery of health care services are assets which are used to fulfill policyholder obligations within the meaning of Issue Paper No. 4 and are admitted assets to the extent that they conform to the requirements of this issue paper.
4. The reporting entity shall maintain a control system that provides for identification of quantities on hand and appropriate valuation (lower of cost or market) of supplies, pharmaceuticals and surgical supplies, and durable medical equipment.
5. Supplies except for pharmaceuticals and surgical supplies discussed in paragraph 6 (e.g., linens, uniforms and garments, food and other commodities, and housekeeping, maintenance, and office supplies) shall be nonadmitted assets.
6. Pharmaceutical and surgical supplies (e.g. drugs, surgical items (such as implants), and medical dressings) used directly in the treatment of medical conditions shall be admitted assets.
7. Durable medical equipment includes consumable or salable equipment such as wheelchairs, crutches and braces, that is generally classified as inventory, and is of a nature that it may be reused. Subscribers, members or policyholders may utilize durable medical equipment on a temporary basis and later return the equipment to the provider. The provider shall recognize the diminution in value, if any, as a result of use of such equipment.

8. In accordance with the reporting entity's capitalization policy, immaterial amounts of medical supplies, pharmaceuticals and surgical supplies, and durable medical equipment may be expensed when purchased.

## DISCUSSION

9. Supplies as defined in this issue paper are nonadmitted assets because they are consumed in the normal operations of a hospital or medical facility and would generally have limited or no value in the event of liquidation.

10. Pharmaceuticals and surgical supplies, and durable medical equipment are admitted assets as defined in this issue paper because they are used to fulfill benefit requirements, they are tightly controlled and the nature of such items would generally permit the recovery of costs upon liquidation.

11. This issue paper rejects the AICPA Audit and Accounting Guide: Health Care Organizations.

12. The statutory accounting principles established in this issue paper are consistent with the recognition concept in the Statement of Concepts which states:

The principal focus of solvency measurement is determination of financial condition through analysis of the balance sheet. However, protection of the policyholders can only be maintained through continued monitoring of the financial condition of the insurance enterprise. Operating performance is another indicator of an enterprise's ability to maintain itself as a going concern. Accordingly, the income statement is a secondary focus of statutory accounting and should not be diminished in importance to the extent contemplated by a liquidation basis of accounting.

The ability to meet policyholder obligations is predicated on the existence of readily marketable assets available when both current and future obligations are due. Assets having economic value other than those which can be used to fulfill policyholder obligations, or those assets which are unavailable due to encumbrances or other third party interests should not be recognized on the balance sheet but rather should be charged against surplus when acquired or when availability otherwise becomes questionable.

## RELEVANT STATUTORY ACCOUNTING AND GAAP GUIDANCE

### Statutory Accounting

13. The Health Maintenance Organization Model Act, dated July 1995 states the following:

#### Section 5. Powers of Health Maintenance Organizations

A. The powers of a health maintenance organization include, but are not limited to, the following:

- (1) The purchase, lease, construction, renovation, operation or maintenance of hospitals, medical facilities, or both, and their ancillary equipment, and property reasonably required for its principal office or for purposes necessary to the transaction of the business of the organization;

#### Section 12. Investments

With the exception of investments made in accordance with Section 5A(1), the funds of a health maintenance organization shall be invested only in accordance with [cite section of law or regulation implementing the NAIC Health Maintenance Organization Investment Guidelines.]

### **Generally Accepted Accounting Principles**

14. The AICPA Audit and Accounting Guide: Health Care Organizations states the following:

6.02. Supplies usually are not material to the financial position of health care organizations. However, because of the volume of supply transactions, they may materially affect operations. Supplies typically include medical and surgical supplies; pharmaceuticals; linens; uniforms, and garments; food and other commodities; and housekeeping, maintenance, and office supplies.

6.04. Accounting for property and equipment, supplies, and other assets of health care organizations is similar to that used by other business organizations.

### **Other Sources of Information**

15. The NAIC Survey on State Practice Regarding Admissibility of Health Care Delivery Assets dated January 1996 conducted by the Risk-Based Capital Task Force surveyed the state insurance departments that regulate HMOs to determine if and to what degree that they allow HMOs to admit health care delivery assets. Responses from 38 state insurance departments indicated that the vast majority admit such assets at book value. A number of state insurance departments noted that they do place varying limits on the amount of certain health care delivery assets that can be admitted. However, none of the respondent states indicated that they did not admit such assets.

## **RELEVANT LITERATURE**

### **Statutory Accounting**

- Statutory Accounting Principles Statement of Concepts and Statutory Hierarchy
- Health Maintenance Organization Model Act, dated July 1995
- *Issue Paper No. 4—Definition of Assets and Nonadmitted Assets*

### **Generally Accepted Accounting Principles**

- The AICPA Audit and Accounting Guide: Health Care Organizations

### **State Regulations**

- No additional guidance obtained from state statutes or regulations.

### **Other Sources of Information**

- NAIC Survey on State Practice Regarding Admissibility of Health Care Delivery Assets dated January 1996
- American Academy of Actuaries Report on Simplification of the Health Risk-Based Capital Formula dated June 1996

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