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Developments Affecting Health Care Spending and What Can Be Done

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Key Factors behind Rising Costs (1)

- Extensive third party payment
  - Encouraged by tax expenditure
- Predominance of fee for service payment
  - Lack of incentives for efficient delivery
  - Penalties for reengineering delivery

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Key Factors behind Rising Costs (2)

- Advancing technology
  - Much improves outcomes
  - But some is overused
  - And some unproven technology in broad use
- Increasing obesity
- Aging
  - But its role is modest

Recent Developments Relevant to Cost Trend

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Deeper Penetration of Consumer-Driven Health Plans

- Recent shift by smaller employers
- Few larger employers have gone to total replacement
  - Indianapolis an exception
- But focus on lower premiums—not on consumerism
- Increasing deductibles in PPOs and HMOs

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Hospital Geographic Expansion Strategies

- Seeking privately-insured patients
- Part of “service-line” strategies
- Outpatient and ED facilities as well as inpatient
- New facilities or acquiring existing

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Physician Employment by Hospitals (1)

- Rapidly developing trend
- Attractive in current payment environment
  - Also position for future integration of delivery

Physician Employment by Hospitals (2)

- Short-term implications for payers
  - Higher private payment rates
  - Higher Medicare/Medicaid rates
  - Potential for higher volume
- Potential to increase primary care supply in an area

Increasing Provider Leverage

- Leverage is very variable—by market and by provider
  - Market (submarket) consolidation, provider size, reputation
  - Small physician practices lack leverage
- More aggressive use of leverage over time

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Limited Network Benefit Designs

- Growth in limited network designs in small group market
- Barriers to tiered networks in many areas
  - Recent Massachusetts legislation

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Opportunities to Slow Rising Spending

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Provider Payment Reform (1)

- Replacing FFS by blending it with capitation and per episode payment
- Enthusiasm in provider and payer sectors
- But important development process ahead
- Coordinating payment method changes with improved delivery

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Provider Payment Reform (2)

- Coordinating payers
  - Public sector leadership
    - Critical mass and credibility
    - But highly constrained environment
  - Private sector leadership
    - Lack of critical mass in some markets
    - Coordination challenging

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Consumer Price Incentives

- Continuing trend in employer-based coverage
  - "Cadillac" tax likely to accelerate it
- But no developments in Medicare
  - Continuing implicit subsidy to Medigap
  - Medicare Advantage plans cannot have more cost sharing than Medicare
  - Addressable with premium support

Prices for Services--Market Approaches

- Benefit design with incentives to choose more efficient providers
  - High deductible plans do little at present
    - Need to steer patients before they reach deductible
  - Tiered networks
  - Limited networks
- Can regulation support market approaches?

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What if Market Approaches Do Not Succeed?

- Some markets already too consolidated for competition
- Powerful providers can resist tiered networks
- Potential for implementation of health reform to increase “cost shifting”
- Would employers advocate rate setting?

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Potential Rate Setting Approaches (1)

- State approach more likely than federal
- Likely to focus on nongovernment payers
  - Control over Medicaid budgets
- Need to address variation in prices as well as trend

Potential Rate Setting Approaches (2)

- Opportunity and challenge of fostering payment reform
  - Coordinate private payer (and perhaps public payer) approaches
  - Allow for review and approval of innovative contracting