Developments Affecting Health Care Spending and What Can Be Done

Paul B. Ginsburg, Ph.D.
President, HSC and Research Director, NIHCR

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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
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
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
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
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
Limited Network Benefit Designs

• Growth in limited network designs in small group market
• Barriers to tiered networks in many areas
  – Recent Massachusetts legislation
Opportunities to Slow Rising Spending
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
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
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
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?
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?
Potential Rate Setting Approaches

• 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