Factors Impacting Health Care Affordability

Information about the drivers of health care costs from Anthem Blue Cross and Blue Shield for New Hampshire customers, accounts, officials and opinion leaders
Rising Health Care Costs

Why Health Care Costs are Rising Today

Introduction

The growing national anxiety about health care costs is not surprising. Historically, concerns over the cost of health care follow a downturn in the economy. With the U.S. economy still sputtering, spiraling prescription drug expenses, escalating payments to medical professionals, and a hospital building boom are projected to increase 2003 health care premiums, on the average, 15 to 20 percent. This is in stark contrast to the overall inflation rate, which from 1997 to 1999 averaged only 2.0 percent. Despite year-to-year increases in health care premiums since 1993, more employers than ever are offering health care to their employees. But as they pay more, employers also are asking employees to bear more of the costs. The result is that workers across the country will pay between $189 and $463 more for health insurance this year. As a result, many employees will opt out of coverage for themselves or their families and will join the ranks of the 43 million Americans who are uninsured.

When American consumers look at the escalating cost of health care, they frequently forget that the problem is not new; it has been with us for more than 30 years. The only exception was in the early 1990s, when growth in health care costs slowed. Several factors were responsible, including the movement toward HMOs and PPOs and a shift away from inpatient hospital procedures to outpatient care. According to industry economists, health care costs started to shift upward again in the latter part of the decade when the soaring economy made labor markets tight, and consumers wanted no restrictions on their access to health care services. Employers asked health insurers to concentrate more on products that were not so tightly managed, and this contributed to the rise in health care costs.

Payment Trends

Growth in health care costs is reflected in recent premium increases, which are now outpacing medical prices.

Average Annual Premium Contribution: 1993-2001

<table>
<thead>
<tr>
<th>Year</th>
<th>Single Coverage</th>
<th>Family Coverage</th>
</tr>
</thead>
<tbody>
<tr>
<td>1993</td>
<td>$2,600</td>
<td>$4,600</td>
</tr>
<tr>
<td>1996</td>
<td>$3,114</td>
<td>$4,299</td>
</tr>
<tr>
<td>2000</td>
<td>$3,664</td>
<td>$5,520</td>
</tr>
<tr>
<td>2001</td>
<td>$4,200</td>
<td>$6,918</td>
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Source: Kaiser Family Foundation/Health Research and Educational Trust, Employer Health Benefits Survey, 2001
Today, the health care marketplace is growing increasingly more complex and expensive. In fact, we spend nearly four times as much on health care as we do national defense.\(^5\)

A report released in 2002 by the Centers for Medicare and Medicaid Services (CMS) indicated that health care spending will balloon to $2.8 trillion annually by 2011, with the projected rate of increase for 2001 being 40 percent greater than the increase in 2000. For consumers, the best recourse is to understand that there is no "villain" to blame — despite what is portrayed regularly in the news media and in popular entertainment venues. Rather, each sector of the health care industry must be held accountable and better define the economics of care.

In reality, multiple factors are responsible for increasing the cost of health care, including a key driver — new technology, an aging population, lifestyle choices, ever-increasing customer demands for new treatments, direct-to-consumer advertising of pharmaceuticals, cost shifting, legislative mandates, and a stripping away of the cost-saving tools of managed care.\(^6\)

To help you to better understand the drivers of health care costs and how these dollars are spent, each is described in the following sections.

Anthem Blue Cross and Blue Shield works hard to hold down premium costs for its customers and members through innovative product designs; investments in information technology; collaboration with physicians and hospitals to help ensure the delivery of quality, cost effective care; and disease management programs targeted at chronic conditions such as diabetes and asthma. Other initiatives encourage healthy lifestyles among members. However, providing ongoing access to high-quality health care for all Americans is a societal problem and a challenge for all of us. The first step in resolving this complex issue is to understand it better.

### Understanding Health Care Inflation

The past 30 years have seen steady cost increases in excess of the growth of the rest of the economy: health care’s share of the gross domestic product (GDP) — just 5 percent in 1960-stood at 13.2 percent in 2001.\(^7\) The year 2000 saw the fastest acceleration of health care spending in 12 years in this country, marking the end of an era of reasonable health care cost growth, according to a January 2002 report released by the CMS National Health Statistics Group. The report found that health care spending grew 7.2 percent, to $1.3 trillion — the largest jump in a decade and the second consecutive year that health care spending growth outpaced GDP growth — a true signal that the nine-year stability in which health care spending grew in tandem with the GDP is over.
Health care is a major economic force in this country and among the most difficult to understand for consumers. The majority of health care costs are paid through private insurance or government programs such as Medicaid and Medicare. Spending was fairly evenly split between the government and the private sector in the mid-1990s, but reduced payments to providers by Medicare and Medicaid led to an increase in cost shifting. This impacts the price of medical services because different people pay different prices that may, or may not, reflect the true cost of the services. For example, Medicaid and Medicare often pay health care providers less than the cost of a particular service or procedure. These under-compensated costs then are borne by those who have private health insurance, or self-fund their health care expenses. Below are just some of the averages of health care costs in the United States since the mid-1990s.

Health Care Cost Trends

Health expenditures represent the largest sector in the U.S. economy.

![Graph showing components of GDP]

Source: Bureau of Economic Analysis, 2001

Most Expensive Hospital Procedures

<table>
<thead>
<tr>
<th>National Statistics</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dollars</td>
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Note: Figures are average charges for hospital stays involving these procedures and they exclude auxiliary procedures.
Health Care Dollar Increases for New Hampshire

Hospital Costs

According to the federal Center for Medicare and Medicaid Services (CMS), total personal health care spending in New Hampshire rose from $2,029 billion to $4,658 billion in the decade between 1988 and 1998, far outstripping both inflation and population growth. In 1998, nearly 35 cents of every health insurance dollar paid in New Hampshire went toward hospital costs.9 In contrast, hospital spending nationally by the year 2000 accounted for the largest portion of medical cost increases — 43 percent. For the first time in a decade, hospital-spending growth outpaced growth in prescription drug spending.10

Reasons for the cost increases over the last decade at both the state and national levels included the enhanced bargaining power of hospitals with insurers and labor shortages, especially for pharmacists and registered nurses. To manage the labor shortages, hospitals offered signing bonuses and higher wages. Additionally, the dollar shortfalls caused by reduced Medicaid and Medicare reimbursements to hospitals caused cost shifting to occur to the private payor market.

Teaching hospitals, with their unique set of services, new technology, training programs and indigent care, are other drivers behind rising hospital costs. Historically, new technology has brought us more weapons to fight disease and injury. While that is good news, it comes with a high price tag. Consumers are not only using more services such as CT scans and MRIs, but they are more costly. The challenges are to decide which new technology adds value and to encourage the most appropriate use of these technologies.

Recent research by the Blue Cross and Blue Shield Association and the consulting firm of PricewaterhouseCoopers suggests that new technology may account for nearly a third of projected increases in U.S. health care spending during the next several years.

Additionally, there is the growing “medical arms race” in this country — where hospitals not only purchase expensive pieces of medical equipment, but also build freestanding facilities such as heart, cancer or ambulatory surgical centers to gain a marketplace advantage. This yields increased fees and not only drives up the cost of health care for communities, but health insurance premiums.

Physician Costs

The share of health care dollars paid to New Hampshire physicians and other medical professionals by insurers was 30.2 percent in 1998.11 Overall, payroll expenses primarily drive physicians’ fees. In 1986, those expenses nationally averaged $67,000 for self-employed physicians. By 1997, this number jumped to $144,000.12 From a national perspective, increases in spending for doctors and other clinical professionals in 2001 accounted for one-quarter of the boost in health care spending.13

The number of specialists also increased over the last four decades, accounting for much of the growth in the physician population. Specialists’ real income growth doubled that of primary care physicians between 1986 and 1996 as indicated in the following chart. As with hospitals, physician groups also have increased bargaining power with payors and are demanding higher reimbursements.
Another key factor is malpractice insurance. A portion of the rise in physician fees is attributable to more of a willingness to pursue malpractice action against doctors on the part of patients, the size of these court awards, and the resulting medical malpractice insurance rate increases. Some physicians have seen their malpractice premiums increase from 20 percent to 100 percent. These premiums can run more than $100,000 annually for certain specialties such as obstetricians and gynecologists, eclipsing what a physician may spend on rent and utilities. According to the consulting firm of Tilhinghast-Towers Perrin, physicians can expect between an 8 and 18 percent premium increase this year for malpractice insurance.

Prescription Drugs

Approximately, 11.6 percent of every health insurance dollar in New Hampshire in 1998 was for prescription drugs, an increase of 14.2 percent from the previous year. Nationally, prescription drug expenditures grew 17.3 percent last year, the sixth consecutive year of double-digit growth. During the past 20 years, there has been a substantial and steady increase in total pharmaceutical spending by public and private payors. The price of prescription drugs is affected by increased utilization, direct-to-consumer advertising, patients switching from generics or older medications to newer, high-cost drugs, new strength/dosage forms and price inflation.
While new drugs enhance the quality of life for us and play an essential role in advancing medicine, they come at a high price. The cost of researching, developing and marketing a new drug, including advertising and promotion costs, is factored into the consumer price of a branded drug. In the United States, these prices are considerably higher than in Canada, Mexico or Europe. Costs for branded anti-depressants and anti-psychotics are six times higher in the U.S. than in European countries. The cost of a month’s supply of the most commonly prescribed anti-depressant in the United States is $123.38 — more than triple the amount charged in Canada and Spain. A 1999 Boston University study concluded that Americans could save $16.2 billion annually if U.S. drug prices were brought in line with the level paid in Canada. Put another way — Americans subsidize the rest of the world for the research and development of blockbuster drugs.

**Other Health Care Cost Drivers**

While rising outpatient, hospital and pharmaceutical expenses are driving costs and the premium structure upward, there are other contributing factors. Legislative mandates for benefit coverage, administrative expenses, unhealthy lifestyle choices, and the baby boom generation entering into a life stage of increasing health costs and higher utilization all contribute to the health care cost spiral.

**Aging Population**

Over the next 10 years, the first wave of baby boomers will turn 65, and by 2020 the over-65 population will grow by 50 percent. Elderly people tend to use many more medical services due to chronic health conditions such as diabetes or heart disease. For example, this age group made 19 percent more visits to specialists in 1999 as compared to those in the 18 to 44 age range. With more people demanding more medical services, new ways must be designed to keep health care costs affordable.

**Lifestyle Choices**

Another problem is lifestyle factors that range from inactivity and obesity to smoking. Unfortunately, despite the increased public awareness on the values of proper diet and healthy, lifestyle choices, not all Americans are heeding the message. Obesity is one of the most common medical problems in the United States and a risk factor for illnesses such as hypertension, diabetes, degenerative arthritis and heart attack. Treatment of obesity and diseases directly related to it accounts for 5 to 7 percent of total health care costs annually.

**Administrative Costs**

Interestingly, administrative costs for health plans increased at lower rates than actual health care costs over the past decade. Administrative costs are those dollars not directly paid to providers for health care services. Nationally, nearly 85 cents out of every dollar is spent on hospital, prescription, physician and other medical costs in this country.
Mandates and Government Regulations

Coverage mandates and government regulation represent $10 billion of the overall increase in health premiums, or 15 percent. According to the National Center for Policy Analysis, there were eight mandated health insurance benefits in 1965 across all state lines. Today, there are nearly 1,500 in this country and another 600 new mandates are proposed by legislatures nationwide. While these mandates are well intentioned, when added to the benefit portfolio of a health insurance plan, they cause premium costs to go up for purchasers.

There also are “other requirements” — which have nothing to do with the delivery of medical services, but impact the cost of care. These include legislation that health plans must accept any medical professional who wants to be in their networks, prompt pay legislation and the Health Insurance Portability and Accountability Act (HIPAA) to name a few. The Congressional Budget Office predicts that the proposed federal Patients’ Bill of Rights, which would allow patients to sue insurers, could increase health care costs an additional 3 percent. Granted, most mandated coverage legislation is well intended, but it takes away from employers and individuals the option to voluntarily choose these benefits.

What Can We Do to Keep Health Care Affordable?

Health care costs are driven in part by advances in technology applied to an aging population with a social infrastructure that rejects the notion of rationing care. The issue of rising costs has not changed significantly over the past decades, and it has been exacerbated by the third-party payor system that insulates consumers from the actual cost of their health care. The resulting dilemma: Patients are not always rational, economic consumers of health care; providers have minimal accountability for rising costs; payors, challenged by the managed care backlash, search for ways to stabilize premium costs; and the government has failed to find a workable solution to this problem.

As a nation, it is increasingly difficult to protect consumer demands for choice and affordability until we clearly understand what drives health care costs. Self-education is the first step toward learning the real cost of medical services as well as the best way for consumers to get the care that is necessary to stay healthy. As this crisis continues to evolve, it is the collective responsibility of the industry along with government and consumers to hold down costs and find a lasting solution to health care inflation.

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3 2002 Segal Health Plan Cost Trend Survey
4 Blue Facts: Health Care Cost Campaign BCBSA
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6 Centers for Medicare and Medicaid Services, March 12, 2002
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9 U.S. Department of Health and Human Services, Agency for Health Care Research and Quality
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16 Medical Benefits, The Escalating Cost of Prescription Drug Coverage, June, 1999
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18 Centers for Medicare and Medicaid Services, Office of the Actuary, National Health Statistic Group
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