

*Health Care and
Pharmaceutical Cost Drivers
and Regional Cost Variation*

*Regulatory Strategies,
Options and Solutions*

CIPR Research Brief



National Association of
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Health Care and Pharmaceutical Cost Drivers and Regional Cost Variation

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This CIPR Research Brief is based on the following three papers to be published as the second part of the CIPR Study: Rising Health Care Costs Drivers, Challenges and Solutions.

Addressing High Health Care Cost Drivers—A Critical Role for Regulators

By Joel White, President, Council for Affordable Health Coverage and
Paul Hewitt, Senior Consulting Economist, Council for Affordable Health Coverage

Regional Cost Variation and the Collaborative Path to Affordability

By Ellen Gagnon, Executive Director, Healthcare Affordability, Network for Regional Healthcare Improvement

Prescription Drug Cost Drivers

By Susan Pantely, Principal and Consulting Actuary, Milliman
and co-chairperson, Prescription Drug Work Group, American Academy of Actuaries

In this CIPR Research Brief we provide a summary of key points made in these papers with a focus on highlighting potential insurance regulatory solutions discussed by the authors. For more details please see the papers with the page references provided in this brief where possible. The full study is available on the CIPR website (cipr.naic.org). The views expressed in this publication are those of the authors. They do not represent the views of NAIC, its officers or members. All information contained in this document is obtained from sources believed by the NAIC to be accurate and reliable. Because of the possibility of human or mechanical error as well as other factors, however, such information is provided "as is" without warranty of any kind.

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Health Care and Pharmaceutical Cost Drivers and Regional Cost Variation

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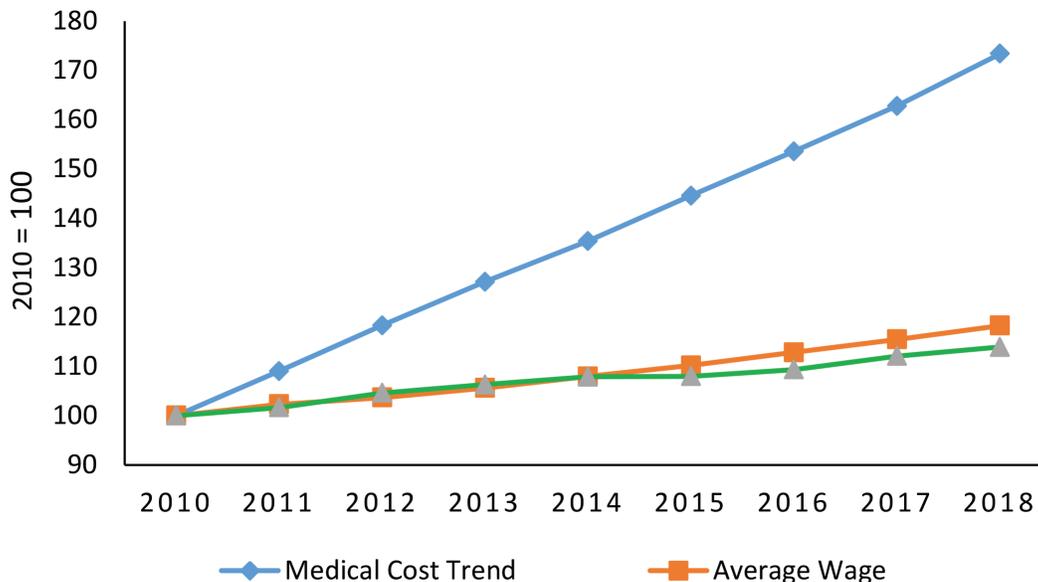
Increasing Costs and their Impacts

- Overall health care costs are growing at higher rate than both productivity and wages (see Figure 1).
- Increasing costs include insurance premiums and deductibles.
- Rising health care costs pose significant issues for consumers, employers, insurers and governments.
- Private health insurance premiums for any level of coverage are the same for all insureds, regardless of income.

- Private health insurance costs have more than doubled as a percentage of household incomes since 2000.
- During 2000-2015, at the fifth earnings decile, real hourly compensation rose by \$3.69, while premiums went up \$4.46.
- Rising health care costs have a disproportionate impact on lower-income households.
- A potential outcome from these rising costs is that consumers would end up using less health care (necessary and unnecessary) but also paying more for it—not positive for long-term health outcomes and future costs.

Figure 1: Medical Cost Trend is Increasing Faster than Wages and Inflation (2010 – 2018)

Source: PricewaterhouseCoopers, Census, BLS, CAHC Calculations





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Key Cost Drivers

- Unit price growth is the leading driver of rising overall health care costs. Trends in utilization and disease prevalence are important but less dominant factors.
 - Utilization and unit price per pharmaceutical script have contributed about equally to growth in prescription drug spending.
- During 2012-2016, commercial inpatient spending per person grew 24.3%, even as utilization fell 12.9%. Had prices not gone up, inpatient spending might have fallen by 37%. Similarly, outpatient spending grew 17.7% while utilization fell 0.5% (See Figure 1A in Appendix).
 - Most health care sectors are seeing costs grow at roughly the same rates. Factors driving up prices in the drug sector are different than those in health services.
 - Hospital and professional services (physician, dental, other health practitioners and clinical services) consume nearly 59 cents of every health dollar exerting the most influence on cost inflation (See Figure 2A in Appendix).
 - In recent years, prescription drug cost trends have at times exceeded medical cost trends driven primarily by the price and utilization of specialty drugs.

Other Factors Driving Health Care Costs

Macro Factors

Increasing market concentration in the health care sector may be driving pricing power (see Figure 4A in Appendix).

93% of hospital markets in metropolitan areas tend to be highly concentrated.

Many consumers may be unable to benefit from price competition.

Market Factors

Lack of pricing information on health care services and prescription drugs.

Increasing reliance on expensive specialized care and the decline of primary care.

Complex and opaque prescription drug supply chain.

Pharmaceutical patent and exclusivity rights restrict the use of more affordable generics.

Other Factors

Unnecessary utilization, administrative costs and waste.

Disease prevalence and aging population.

Taxes and regulation.

Fee-for-service payment system where providers are compensated for the number and type of services they perform.



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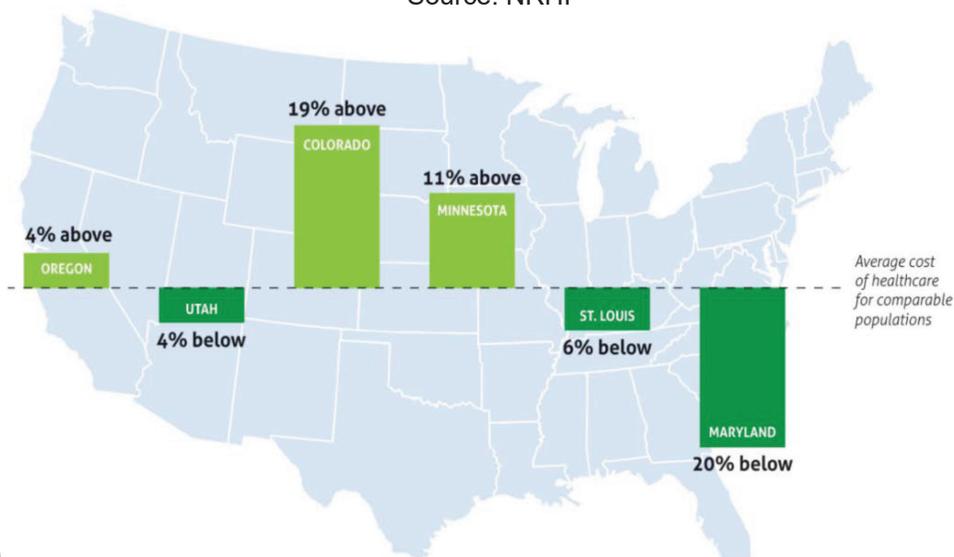
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Regional Cost Variation

- Despite overall cost increases, prices, care delivery, utilization patterns and population health tend to vary across states and within states across markets. These variations can drive differences in costs. (see Figure 2).
 - Although price is the driver of both higher and lower health care costs in some regions, utilization makes the difference in others.
 - Understanding difference in price, cost and resource use gives stakeholders a framework to consider the roles of policies, demographics and market factors in containing health care costs.
- Regional differences are measured using the primary Total Cost Index and its two components, the Resource Use Index and the Price Index. These indices help understand where to look for the underlying causes of these cost differentials.
 - Most regions tend to have the same higher price and/or higher utilization service lines year over year. Consistency in year-over-year total cost of care results reflect regional norms in care delivery and pricing.
 - Pharmacy pricing showed the least variability. This is largely a result of the influence of a few, large pharmacy benefit managers and pharmaceutical manufacturers' national pricing policies.
 - In each of the three years, Maryland was the lowest cost of the regions. In the most recent year, the total cost index varied from 20% below the benchmark for Maryland, to 19% above the benchmark for Colorado, the highest cost region.

Figure 2: Variation in Underlying Drivers of Health Care Costs Across Regions

Source: NRHI





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Policy Options and Solutions

Direct Regulatory Action

While there are no silver bullets for reining in health care costs, the authors of these three CIPR papers have highlighted a number of possible steps that could be taken by state insurance regulators if their resources and legislative mandate allow to help reduce spending and, by extension, insurance premiums and cost sharing.

- The rate review process can provide an opportunity for state insurance regulators to examine pricing and underlying assumptions (see *"Addressing High Health Care Cost Drivers—A Critical Role for Regulators,"* p.13)
- Through the review process regulators could also evaluate interventions to address high underlying costs and wasteful spending. While there is regulatory scrutiny on expenses directly under a health plan's control, such as administration expense and expected enrollee mix, regulators could also focus on the price of medical services and products.
- State insurance regulators could increase transparency on the medical costs driving premium and cost sharing rate increases. Such public disclosure and transparency can broaden the consensus about how best to rein in medical inflation.
- Plan filings can be used as a basis of consumer information to disclose to the public the key drivers of cost increases, including what portion of premium goes toward services, drugs and devices, administrative expenses, mandates and taxes. Unit prices of course are also an important metric.
- Hospitals and other providers can augment this data with relevant information regarding their input costs.
Examples of state review approaches can be found in "Addressing High Health Care Cost Drivers—A Critical Role for Regulators," p. 14
- Additional steps state insurance regulators could take in their plan approval process to encourage greater consumer value:
 - o Encourage value-based insurance designs
 - o Encourage creativity in network design
 - o Reward healthy behaviors and health literacy
 - o Consider flexible benefit designs
- For prescription drugs, moving to paying for value instead of volume could control rising prices and improve outcomes (see *"Prescription Drug Cost Drivers,"* p. 48).



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Indirect Regulatory Action

State insurance regulators can take several indirect actions as informed truth-tellers in their community by providing evidence on health care cost drivers and solutions. They can support action in concert with other decision makers, such as state legislatures and governors, to actually lower costs (see *“Addressing High Health Care Cost Drivers—A Critical Role for Regulators,”* pages 15-18 and *“Prescription Drug Cost Drivers,”* pages 48-55).

- Support the development of state data infrastructure. Data on price and utilization can help all payers target their initiatives to maximally impact cost.
- Support reporting on high cost and/or high prevalence conditions. Measurements over time by chronic condition may provide meaningful insights to better understand the interaction of medical and prescription drug costs.
- Offer transparency tools to assist consumers in choosing wisely across health care providers.
- Promote regulation of direct to consumer drug advertising. Providing consumers with more information on drugs, costs, and alternatives may be valuable educational material. Additional and higher visibility disclosures in the advertisements may moderate utilization.
- Provide payers with more leverage in markets where provider consolidation has resulted in uncompetitive oligopoly or monopoly.
 - o Ban uncompetitive practices such as anti-tiering, anti-steering, most-favored-nation and other contract clauses contributing to cost escalation.
 - o Support the development of upper payment limits in areas where competition is non-existent. Creating a similar upper payment limit for all private health plans would be straightforward and affect all local markets nearly equally.
 - o Examine provider licensing and scope of practice rules. Such a policy could improve patient access and promote provider competition and lower costs and prices.



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State Actions and Initiatives

The following are some of the recent actions states have taken to combat high prescription drug trends (see *“Prescription Drug Cost Drivers”* page 47-48).

- Price transparency and controls
 - o Six states have passed legislation requiring drug manufacturers to justify price increases over certain thresholds.
 - o Some states have explored imposing penalties if the price increases are excessive.
 - o Several states have implemented laws aimed at more transparency regarding prescription drug rebates and other concessions.
 - Prescription drug imports
 - o Vermont has become the first state to pass a drug importation bill to import wholesale prescription drugs from Canada.
 - Promote generic drugs
 - o Maine implemented legislation requiring brand name manufacturers to make samples of drugs available to generic drug manufacturers with the intention of shortening time until a generic becomes available.
- Efforts by Network for Regional Healthcare Improvement members to achieve better quality and affordable health care (see *“Regional Cost Variation and the Collaborative Path to Affordability,”* pages 27-28).
- In Oregon, HealthInsight Oregon has been sharing information on the total cost of care, including price and utilization, with state policymakers, providers and insurers for several years. The legislature has convened a number of workgroups to address health care cost components.
 - The Colorado Center for Improving Value in Health Care (CIVHC) has provided the state legislature and other stakeholders with data and information to help understand how the cost of care in Colorado compares to other states and promote policy changes to impact those costs.
 - The state of Maryland has operated the nation’s only all-payer hospital rate regulation program for about 35 years. State agencies have noted the results from this project suggest the model is having a positive impact for the commercially-insured.
 - Better Health Partnership, the Regional Healthcare Improvement Collaborative (RHIC) serving Cleveland and its surrounding communities, combined clinical data with data on social determinants of health, such as insurance type, race/ethnicity, language preference, education, and household income. The goals were to increase care coordination for complex patients and improve cost-effective primary care.



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Appendix

Figure 1A: Changes in Private, Commercial Health Spending, by Category (2012 – 2016)

Source: Health Care Cost Institute, Health Care Cost and Utilization Report, 2016

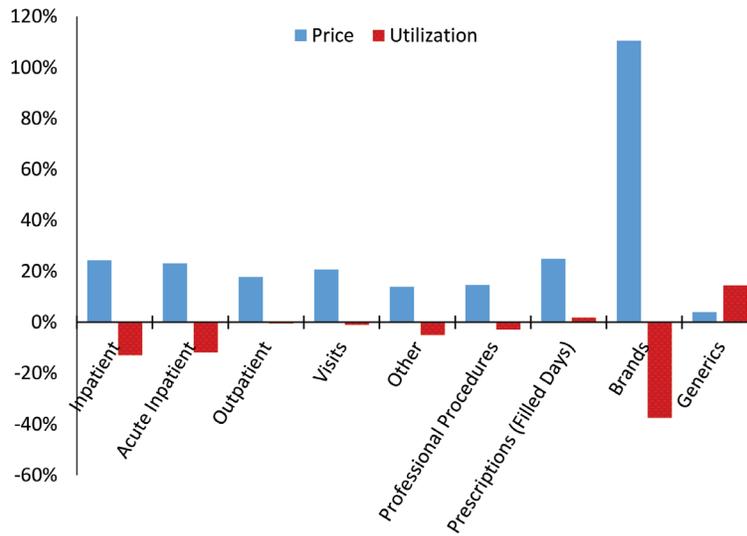
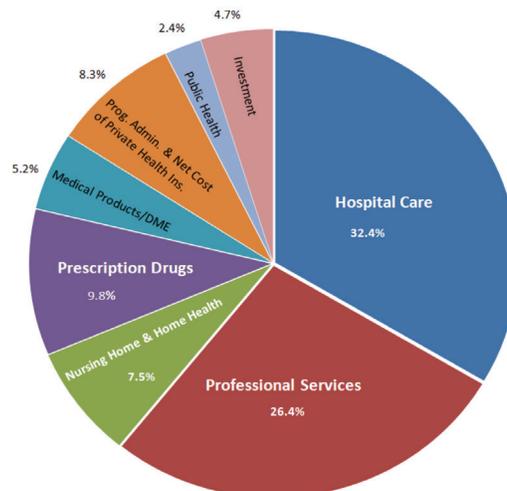


Figure 2A: Composition of Health Care Spending, 2017

Source: Centers for Medicare and Medicaid Services





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Figure 3A: Untangling the Cost Drivers

Source: NRHI

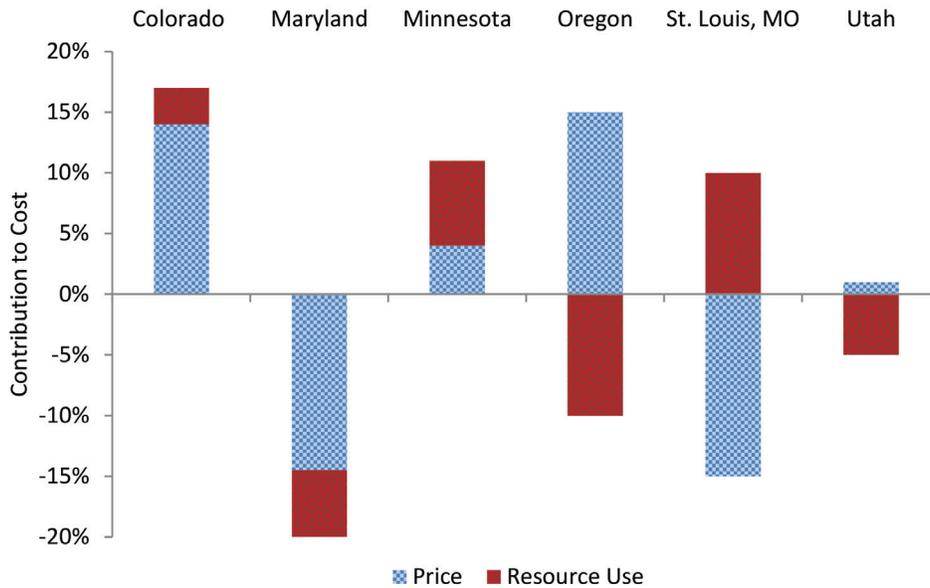


Figure 4A: Percentages of Metropolitan Areas with Highly Concentrated Markets (2010-2016)

Source: B. D. Fulton, Health Affairs, Sept. 2017

