

Health Care Spending Slowdown: The Consumer Paradox

Executive Summary

Dobson | DaVanzo

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Submitted by:
Dobson | DaVanzo

Al Dobson, Ph.D.
Gregory Berger, M.P.P.
Kevin Reuter
Phap-Hoa Luu, M.B.A.
Joan E. DaVanzo, Ph.D., M.S.W.

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In recent reports we have outlined the continuing historic slowdown in the growth rate of health care spending driven in large part by emerging structural changes in the health care system.^{1,2} Recent evidence suggests that the cost curve has continued to bend, with health care spending **declining** in the first quarter of 2014. Despite this continuing trend in health care spending growth, consumers are increasingly concerned that they are ever-more financially burdened by spending on their own health care.

This consumer perception is largely a factor of the “new normal” being established through health insurance, which includes:

- Benefit plan designs, used by employers and insurers to shift greater financial risk to consumers through higher out-of-pocket spending (i.e., deductibles, co-payments, and co-insurance); and
- Health insurance premiums, which continue to rise faster than the average person’s income.

This trend of growth in out-of-pocket spending combined with increases in health insurance premiums that outpace increases in wages is not sustainable over the long term, and harms both patients and providers. However, the slowing growth of national health care spending has eased this burden to some degree, and if it continues, will ultimately benefit consumers. The savings from the health care spending slowdown have been and will continue to be passed onto consumers through lower costs than would otherwise have been the case and greater value in the services they use.

A shift to value (rather than volume) based payment is a key factor driving spending growth reductions. Payers and providers are transitioning to structural changes in delivery and payment arrangements that are beginning to show reduced spending and higher quality (e.g., fewer hospital readmissions). To support these efforts, providers are making large

Consumer spending on health care grew at its slowest rate in over three decades in the fourth quarter of 2014, yet consumers experience increases in health insurance premiums and out-of-pocket spending that continue to outpace increases in wages.

¹ Dobson, A., DaVanzo, J., Berger, G., Reuter, K. (2013). Structural Changes Drive Health Care Spending Slowdown: Implications for Medicare Policy and Deficit Reduction. Vienna, VA: Dobson | DaVanzo.

² Dobson, A., DaVanzo, J., Berger, G., Reuter, K. (2014). Do Structural Changes Drive Health Care Spending Slowdown? New Evidence. Updated Implications for Medicare Policy and Deficit Reduction. Vienna, VA: Dobson | DaVanzo.

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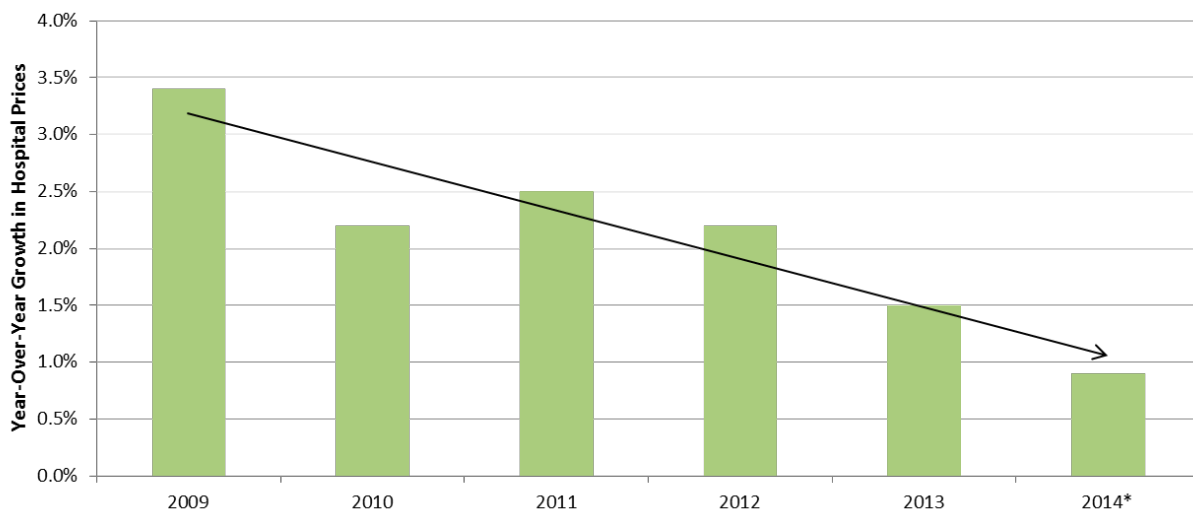
investments in cost reductions, developing new care and business models, provider partnerships, and data systems that allow them real-time feedback to influence clinical and administrative decisions. The development of a stronger health care infrastructure able to provide high quality, affordable care to the aging American population is reliant upon health care providers continuing to support this transition. Therefore, policymakers should not get in the way of the innovations currently in place or under development; as the cost-curve continues to bend, both consumers and payers will benefit from reduced spending on health care and from a vastly improved health care system. Abrupt changes to health care policy at this point could bring unintended consequences.

Key Findings

In the first quarter of 2014, new evidence emerged that the sustained health care spending slowdown has continued even as Medicaid coverage expands and the state-based and federal health insurance marketplaces launch. For example:

- In the first quarter of 2014, consumer spending on health care **declined** by 1.4%, representing the largest decline in over 30 years, and 7.0 percentage points lower than the 5.6% increase in the fourth quarter of 2013³ (see Exhibit 1 for additional evidence on hospital price growth)

Exhibit 1: Year-over-Year Percent Change in Hospital Prices (2009-2014)



Source: Dobson | DaVanzo analysis of Bureau of Labor Statistics data. Note: Annual growth rates calculated from December to December of each year.*2014 growth rate calculated from December 2013 to June 2014.

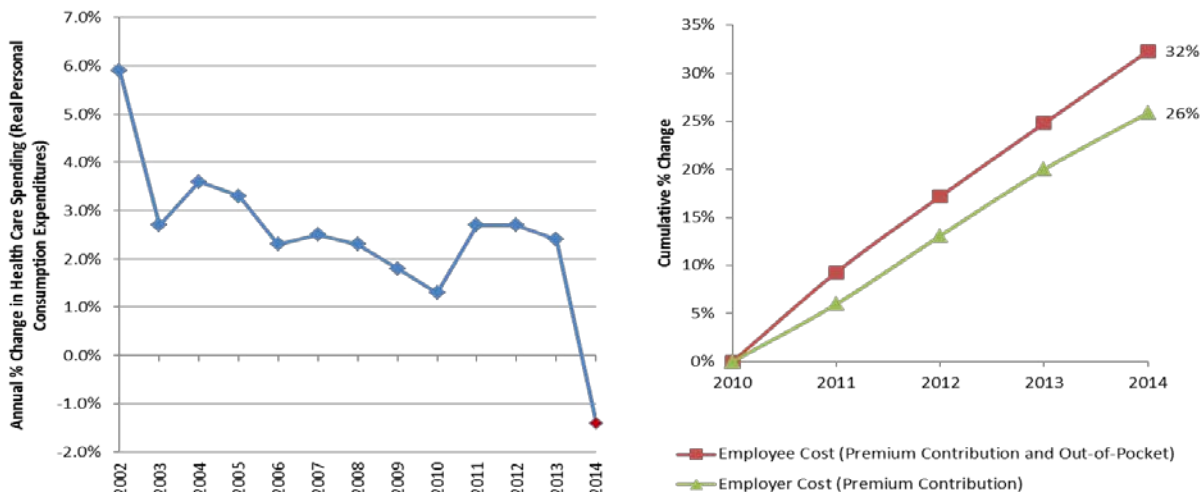
³ Bureau of Economic Analysis. Real Personal Consumption Expenditure Data.

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However, paradoxically, consumers perceive that their health care spending is increasing more than usual. This perception is largely a result of spending on their health care increasing faster than personal income combined with a continuing redesign of their health insurance benefits, which shifts more of the cost burden onto consumers:

- Almost 60% of Americans think that health care costs have been growing faster than usual in recent years⁴, and more than 70% of consumers attribute responsibility for their perceived high and rising costs to health insurance companies⁵
- Total premiums have increased substantially over the past decade, from 14.9% to 21.6% of median household income between 2003 and 2012⁶
- Employee contributions to premiums and out-of-pocket spending have risen 23% faster than employee costs since 2009 (32% in cumulative growth vs. 26%)⁷ (see Exhibit 2)

Exhibit 2: Annual Percent Change in Health Care Spending (2002-2014) and Cumulative Change in Employer and Employee Health Care Costs (2010-2014)



Source: Dobson | DaVanzo analysis of Bureau of Economic Analysis data and 2014 Milliman Medical Index. Note: Real personal consumption expenditures consist of the actual and imputed expenditures of households and are adjusted for inflation. The Milliman Medical Index is an actuarial analysis of the projected total cost of health care for a hypothetical family of four covered by an employer-sponsored preferred provider organization (PPO) plan.

⁴ Altman D., "Health Cost Growth Is Down, or Not. It Depends on Who You Ask", Kaiser Family Foundation, March 2014. Almost 60% of the respondents said that health care cost for the nation have been growing faster than usual in recent years, less than 30% thought the costs have been the same, and just 4% responded that they have been slower than usual. No one said that health care costs were going down.

⁵ Altarum Institute, Survey of Consumer Health Care Opinions, Fall 2013.

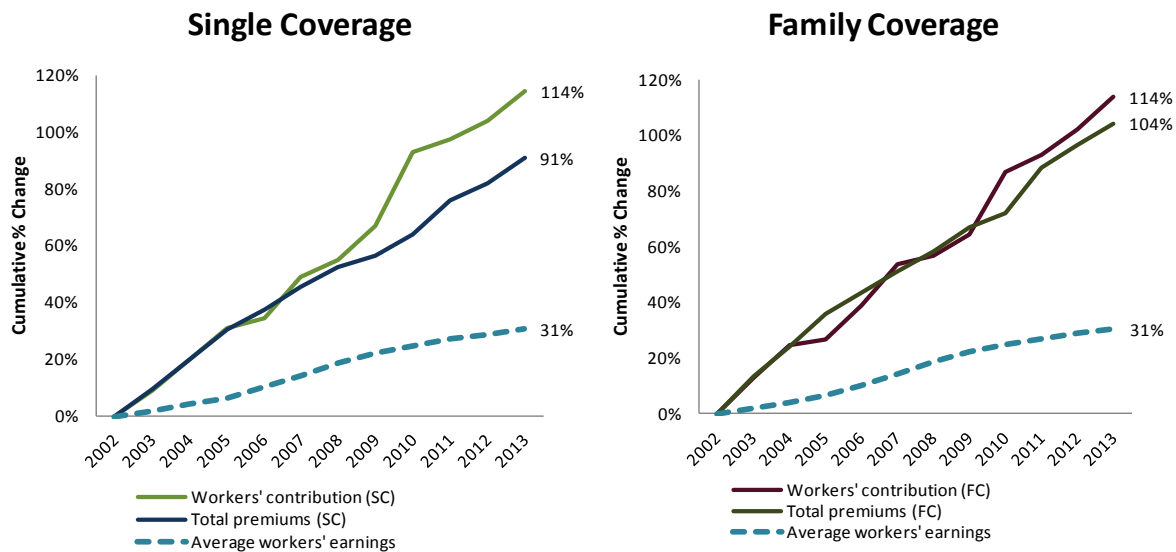
⁶ Schoen C, Hayes S.L., Collins S.R., Lippa J.A., and Radley D.C., America's Underinsured, A State-by-State Look of Health Insurance Affordability Prior to the New Coverage Expansion, The Commonwealth Fund, March 2014.

⁷ Milliman Medical Index, 2014.

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- Cumulative growth in workers' contributions to premiums between 2002 and 2013 was 114%, approximately four times higher than growth in workers' average income (31%)⁸ (see Exhibit 3)

Exhibit 3: Cumulative Growth in Workers' Contribution to Premiums, Total Premiums, and Average Worker Income, Single and Family Coverage (2002-2013)



Source: Dobson | DaVanzo analysis of Kaiser Family Foundation's Employer Benefits, 2013 Survey, and CMS OACT National Health Expenditures. Note: SC= single coverage, FC= family coverage.

- Deductibles for family coverage increased more than 75% from 2006 and 2013 (from \$1,034 to \$1,854), while enrollment in plans with a deductible increased to 81% in 2013⁹
- The percentage of workers enrolled in high-deductible plans (\$1,000 or more) has increased more than five times over the past decade, from 4% in 2006 to 26% in 2014
- Overall, employees' premium contributions and out-of-pocket expenses per capita have grown by 42% over the past five years, from \$6,824 in 2009 to \$9,695 in 2014¹⁰

⁸ Data for total premiums and workers' contributions are from Kaiser Family Foundation, Employer Benefits Survey, 2013; Data for workers' earnings are from the Bureau of Labor Statistics.

⁹ Kaiser Family Foundation, Employer Benefits Surveys, 2006-2013. Deductible rates for single coverage increased from \$584 in 2006 to \$1,135 in 2013, with an increase, respectively, from 55% to 78% in enrollment of covered workers in plans with deductibles. Rates for family coverage increased from \$1,034 in 2006 to \$1,854 in 2013.

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As consumers, payers, and providers all adjust to the structural changes taking hold in health care payment and delivery as well as the new health insurance market status quo—which represents higher patient cost-sharing and therefore a higher financial burden on the consumer—policymakers need to be mindful of potential unintended consequences.

Payers and providers are both adjusting to a “new normal” in the marketplace through a variety of multi-year strategies aimed at improving quality, reducing costs, and minimizing financial risk within the evolving regulatory framework. Additional interventions or blunt policymaking, rather than allowing the market to respond to current reform efforts, could interfere with the system. For example:

- ***Interrupting access to care:*** Within the context of existing uncertainty, increasing bad debt related to the expansion of high deductible health plans or eroding the predictability of government reimbursement for services could cause providers to lose their capital reserves and/or face solvency issues. This could also lead to providers cutting services, leaving individuals with difficulties accessing care including delayed procedures, increased travel time, and longer wait times, or even closing facilities.
- ***Inhibiting advancement in the health care system:*** Providers have invested in redesigning care and business models to improve quality while also decreasing costs to patients (e.g., accountable care organizations, bundled payments). Hospitals and other providers have made and need to continue making investments in health information technology, clinical integration, developing best practices, and care reengineering to manage care outside of their four walls. Without capital reserves to support these efforts, some of which are required by regulation—such as meaningful use of electronic medical records—providers may lack the ability to devote substantial and sustained resources to fund these investments.

Both payers (including employers) and providers have prepared multi-year transition plans to adjust their business models, and require some level of predictability and capital reserves. Major disruptions to the operating environment for providers, payers and/or employers may generate uncertainty, which ultimately could flow down to consumers in the form of higher premium contributions and out-of-pocket spending.

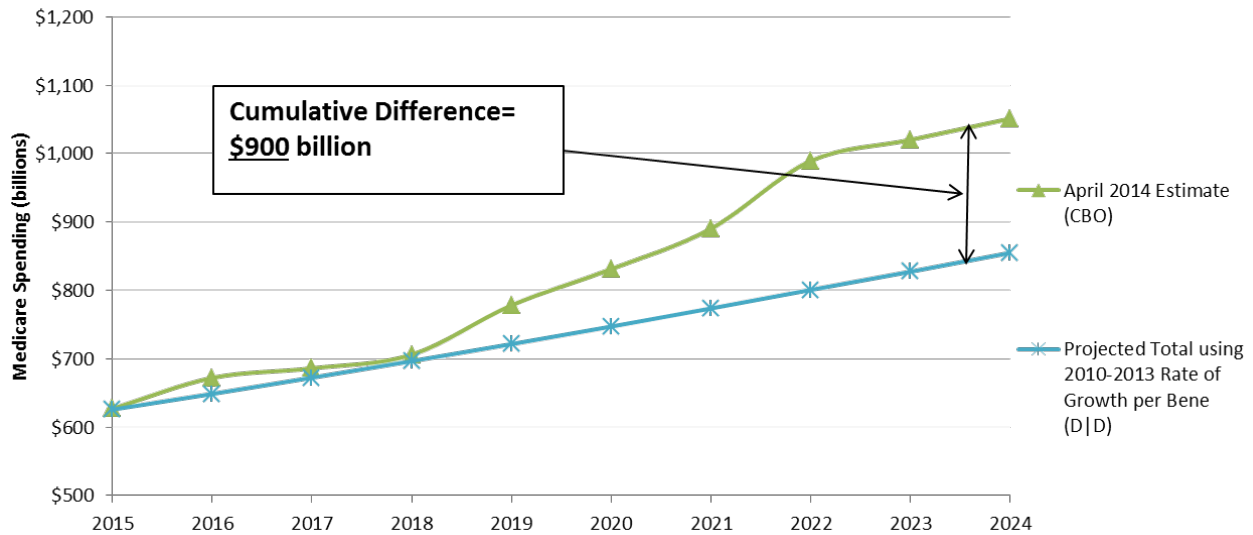
Preserving the current climate is equally important to realizing future savings in Medicare. As projected by Dobson | DaVanzo, if the 2010-2013 rate of spending per Medicare

¹⁰ Despite increases in the absolute dollar amount spent by consumers out-of-pocket, out-of-pocket spending as a percent of total health care spending has remained relatively constant at slightly over 16% since 2009 (Dobson | DaVanzo analysis of Health Care Cost and Utilization Report, 2012).

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beneficiary continues over the next decade, Medicare could realize projected savings of \$900 billion beyond that which CBO projects through 2024 (see Exhibit 4).¹¹

Exhibit 4: Projected Aggregate Medicare Savings (2015-2024) based on CBO April 2014 Baseline (billions)



Note: D|D is Dobson | DaVanzo. For detailed methodology see: Dobson, A., DaVanzo, J., Berger, G., Reuter, K. (2014). Do Structural Changes Drive Health Care Spending Slowdown? New Evidence. Updated Implications for Medicare Policy and Deficit Reduction. Vienna, VA: Dobson | DaVanzo. The average growth rate from 2010-2013 was calculated using CBO estimates of total Medicare expenditures from 2010-2013 (reported in the April 2014 CBO baseline estimate) divided by the number of Medicare beneficiaries in each year as reported in the 2013 Medicare Trustees report.

Therefore, it is prudent for policymakers to allow the health care marketplace to continue adapting, innovating, and implementing the structural changes already underway; as the cost-curve continues to bend, both payers and consumers will ultimately benefit both from reduced spending on health care and from a vastly improved health care system.

¹¹ Dobson, A., DaVanzo, J., Berger, G., Reuter, K. (2014). Do Structural Changes Drive Health Care Spending Slowdown? New Evidence. Updated Implications for Medicare Policy and Deficit Reduction. Vienna, VA: Dobson | DaVanzo.