What *Drives* the Growing Cost of Health Care?

Slowing the growth of health care costs is essential to ensuring a sustainable health care system. While the growth in health spending in the U.S. has slowed in recent years, to its lowest point in decades, this cost growth has not reversed itself and health care spending remains a significant portion of household incomes and government budgets.

Total health care spending in the U.S. reached $2.8 trillion in 2012, and the share of the gross domestic product (GDP) devoted to health care spending was 17.2 percent. That means more than one out of every six dollars goes to health care. Notwithstanding the recent slowdown in health spending growth, it is crucial to explore options that could help sustain that slowdown and further reduce cost growth.

The Affordable Care Act has taken some steps to reduce health care costs, but more needs to be done. The American Academy Actuaries, under the leadership of its Health Practice Council, is undertaking an initiative to examine health care cost growth and explore options that can reduce spending growth over the long term while at the same time focusing reform efforts on achieving cost-effective and high-quality care. To ensure a sustainable health care system, health care cost growth must be addressed.

Payment structures reward more tests and procedures

Most common payment systems to doctors and hospitals today reward more care, and more intensive care, but not necessarily better-quality care. In this environment, doctors and hospitals have little financial incentive to provide the most cost-effective care, and their reimbursements are not wholly tied to treatment outcomes.

More expensive medical technology

Technology and pharmaceutical advances have brought breakthroughs that have vastly improved Americans' life expectancies and quality of life. But often these advancements require more expensive equipment and procedures, and can lead to additional high-cost services. Unlike consumer technology, most medical technology doesn't dramatically drop in price over time. Additionally, some new technologies and treatments may not show much improvement over older treatments yet they may increase costs.

Less healthy lifestyles can increase medical service needs

Americans have cut down on smoking, but lack of exercise and poor eating habits have led to higher obesity and diabetes rates. Poor lifestyle choices increase the need and utilization of health services, especially to manage chronic conditions.

Lower out-of-pocket costs lead to more health care services

Most health insurance programs sponsored by the government or employers cover a

HEALTH CARE FAST FACTS

$2.8 trillion
U.S. health care spending in 2012

3.7%
Increase in spending in 2012

$8,915
Average health care spending per person in 2012

$1,048
Average out-of-pocket expenses in 2012

Who picks up the national tab
28% U.S. households
26% federal government
21% private businesses
18% state, local governments

Source: Centers for Medicare and Medicaid Services

comprehensive set of medical services that result in low out-of-pocket costs for patients. Since consumers pay only a fraction of their total costs – unless the service falls outside of their insurance coverage – this leads to increased utilization of medical services.

Broader provider networks limit discounts

Broader networks of providers offer consumers more choice. However, having broader networks can limit an insurer's ability to negotiate provider discounts because they cannot impose efficiency standards or direct a larger share of members to a narrower set of providers. Narrower networks can help manage cost increases, but that has to be balanced with the ability for consumers to have adequate provider access.

Primary care provider shortage leads to greater use of specialists

The U.S. had an average of 80 primary care doctors per 100,000 people nationwide in 2010 and only 68 per 100,000 in rural areas. This limited number of primary care doctors has led to individuals turning to specialists or other high-cost settings for routine care, even though the cost for the same service can be higher.

Various approaches are being explored in attempts to lower both the cost and utilization of medical services. Some of these will be addressed in upcoming Academy papers, which will analyze various options to slow the growth in health care spending and the many trade-offs that will be needed to balance high-quality health care with lowering costs.

- Comparative-effectiveness research can refocus the health care delivery system on the value of care received as a way to reduce spending on treatments and services that don't provide better health care outcomes.

- Patient-centered medical home (PCMH) and Accountable Care Organizations (ACOs) can provide more coordinated care through a personal physician or group of physicians, such as those affiliated with the same hospital, that would be responsible for improving the quality and controlling the costs of their patients' care.

- Benefit-design features, such as charging a lower copayment for an urgent care visit than an emergency room visit, could be changed to encourage care at lower-cost settings.

- Value Based Insurance Design (VBID) is an approach that would tailor cost sharing for certain treatments and services to individuals' specific needs, which provides incentives to use higher-value services and discourage lower-value services.

- Wellness and disease-management programs have been developed to encourage healthy lifestyle changes and manage the chronic conditions in efforts to contain overall health care costs.

Additional Resources from the American Academy of Actuaries

Examining the Health Care Equation: New Models of Care Delivery
http://www.actuary.org/files/Care_Delivery_IB_040414.pdf

An Actuarial Perspective on Accountable Care Organizations
http://actuary.org/files/ACO_IB_UPDATE_Final_121912.pdf

Value-Based Insurance Design
http://actuary.org/files/publications/value_based_insurance_design_june2009.pdf