CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Providing Insights that Contribute to Better Health Policy

Health Plan – Hospital Contracting in Today's Marketplace

Statement of Bradley C. Strunk

FTC/DOJ Hearings on Health Care and Competition Law and Policy

March 27, 2003

Key Points

- Trends in reimbursement rates to providers have accelerated
- Hospitals regained significant leverage over plans
- But some signs that balance of power might be shifting again

CENTER for STUDYING HEALTH SYSTEM CHANGE

Center for Studying Health System Change (HSC)

- Research on changes in the organization and delivery of care – and their impact on people
  - Objective information for policy makers
  - Funded by The Robert Wood Johnson Foundation

- Emphasis on health care markets

- www.hschange.org

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

CTS Site Visits

- Insight into changing market trends
- Visit 12 randomly selected sites every two years
- Currently finishing up 4th round of visits
- Conduct 70-100 interviews in each site, including a broad cross section of local health system leaders
- “Triangulate” results

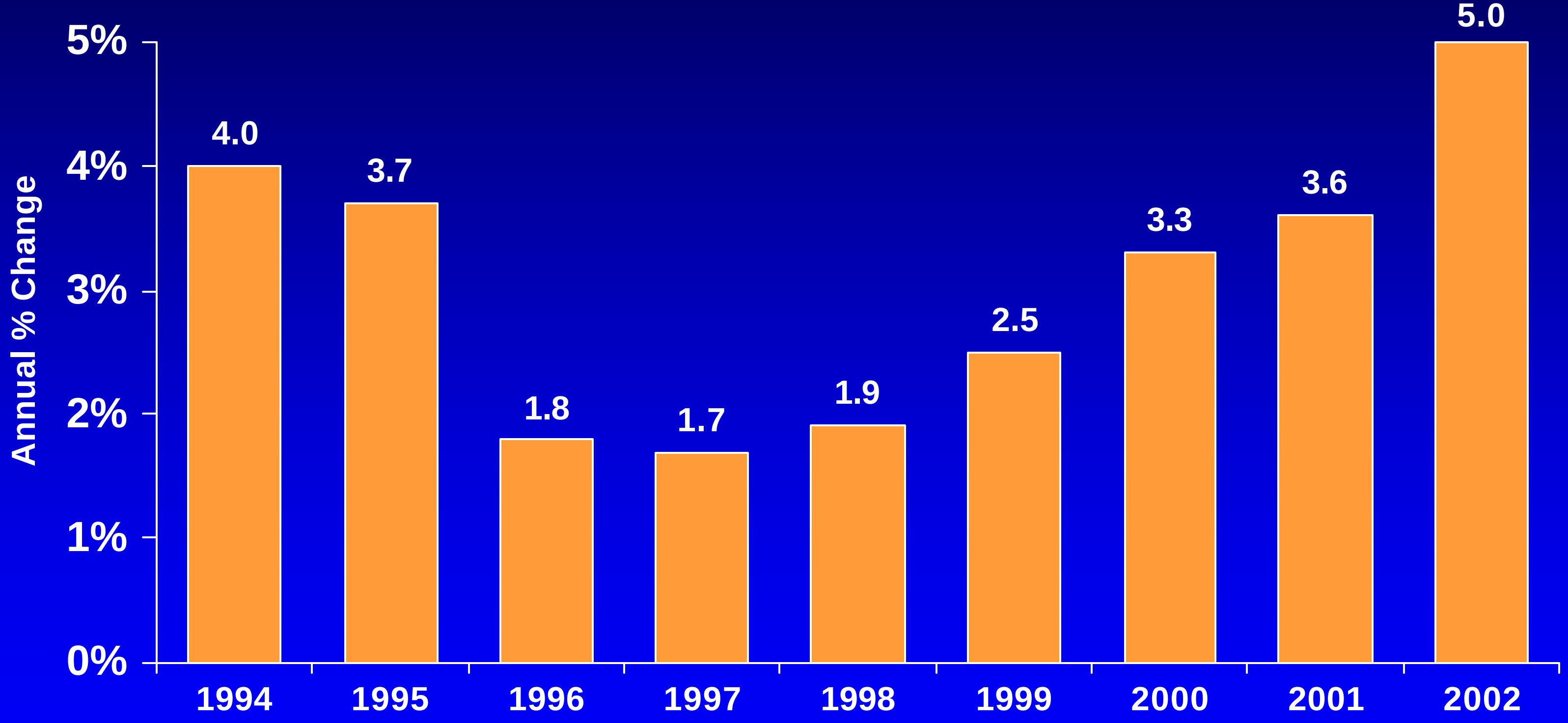
CENTER for STUDYING HEALTH SYSTEM CHANGE

Community Tracking Study (CTS) Sites

- Site visits and surveys
- Survey only

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Trend in Hospital Prices



Source: *U.S. Department of Commerce, Bureau of Labor Statistics' "All other payers" Producer Price Index For General Medical and Surgical Hospitals*

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Negotiating Leverage is Dynamic

CENTER for STUDYING HEALTH SYSTEM CHANGE

Contracting Environment Favored Plans in Mid 1990s

- Employers viewed managed care/HMOs as solution to rapid cost growth of early 1990s
- Widespread expectation among hospitals that narrow network products, utilization mgmt, capitation would become the norm
- Hospitals agreed to steep discounts in exchange for promises of higher volume

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Hospitals' Response to Rise of Managed Care

- Consolidation – system/network building
  - Horizontal
  - Vertical – less prevalent but important where present

- Branding – creating "must-have" status

- Solidify geographic niche

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Contracting Environment Shifted to Favoring Hospitals at Turn of Decade

- Managed care backlash from consumers
  - Disdainful of managed care restrictions
  - Demand choice of providers
- Economic boom and tight labor markets
- New capacity constraints emerged in some markets

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Pressures on Hospitals

- Medicare margins declined since 1997 (BBA)

- Operating cost pressures
  - Nursing shortage driving up wage rates
  - Prescription drug costs growing rapidly
  - Market-specific pressures

CENTER for STUDYING HEALTH SYSTEM CHANGE

Hospitals Push Aggressively for Rate Increases

- Securing better rates by using various approaches to negotiation
  - Terminate-to-negotiate
  - Leveraging the system
  - Appeals to the public
- Contract showdowns and network instability result

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Health Plan Response

- Tiered hospital network products
  - Viability varies across markets
  - Limited penetration at this time
- Quality incentives to providers
- Some development of Exclusive Provider Organization (EPO) products

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Contracting Environment Continues to Evolve in 2003

- Health insurance premiums increased by double digit rate for 3rd straight year
- Economic downturn that started in 2001 continues
  - Recession not as bad as that of early 1990s, though
- Employers increasing patient cost sharing
- Consumers could develop a renewed appetite for narrow provider network products if they are cheaper

CENTER *for* STUDYING HEALTH SYSTEM CHANGE

Current Balance of Power

- Hospitals remain willing to take contract negotiations to the brink…
- …but outcomes of negotiations are more variable
- Some employers becoming more supportive of plans
- Seeing fewer showdowns played out in public, so outcomes often unclear

CENTER *for* STUDYING HEALTH SYSTEM CHANGE