What Accounts for the Growth in Private Health Insurance Spending?

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EXECUTIVE SUMMARY

Hospital care is the largest contributor to commercial health insurance spending growth, accounting for 42% of the increase since 2016. The growth in spending due to hospitals is more than twice that of the growth due to physician services and administrative costs, and ten times that of prescription drugs and nursing care. Efforts to control spending should consider how drivers of spending growth are linked to better patient care and chronic disease management.

WHAT ACCOUNTS FOR THE GROWTH IN PRIVATE HEALTH INSURANCE SPENDING?

Health spending growth is determined by both how much a health insurer is spending on medical care services (price and utilization) and the health plan’s administrative spending (operational costs and profits). This analysis determined the leading drivers of increased spending in the private market using the 2016-2018 National Health Expenditures (NHE) data reported by the Centers for Medicare & Medicaid Services (CMS). The drivers of spending growth were calculated based on the change in spending over the most recent two years attributable to each category of care relative to the change in overall spending.

Between 2016 and 2018, private insurance spending increased by $101 billion overall. Of that total, hospital spending grew by nearly $43 billion. At the same time, the $21.3 billion increase in spending on plan administration costs and profits outpaced spending on physician and clinical services by $650 million. Spending on retail and non-retail prescription drugs grew by $3.6 billion over the same time.* In terms of proportionate share of the total growth in private insurance spending, hospital services dominated, accounting for 42% of overall spending growth, followed by spending on plan administrative expenses and profits at 21%. Total spending on prescription drugs accounted for 4% of the growth in spending.

* Please see Notes below for details on calculation of prescription drug spending and adjustments made to other sectors to deduct spending on prescription drugs administered in the hospital or a physician’s office and include those totals in total spending on prescription drugs.
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Table 1. Increase in Private Health Care Spending, 2016-2018 by Source of Spending

<table>
<thead>
<tr>
<th>PRIVATE HEALTH INSURANCE PLAN SPENDING BY CATEGORY</th>
<th>2016-2018 SPENDING GROWTH (IN BILLIONS)</th>
<th>PROPORTIONATE SHARE OF OVERALL SPENDING GROWTH 2016-2018</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Spending</td>
<td>$101.30</td>
<td>100%</td>
</tr>
<tr>
<td>Hospital Services</td>
<td>$42.72</td>
<td>42%</td>
</tr>
<tr>
<td>Health Plan Profits and Administrative Costs</td>
<td>$21.26</td>
<td>21%</td>
</tr>
<tr>
<td>Physician and Clinical Services</td>
<td>$20.61</td>
<td>21%</td>
</tr>
<tr>
<td>Total Prescription Drugs</td>
<td>$3.58</td>
<td>4%</td>
</tr>
<tr>
<td>Nursing Care Facilities</td>
<td>$3.00</td>
<td>3%</td>
</tr>
<tr>
<td>Home Health</td>
<td>$0.79</td>
<td>1%</td>
</tr>
<tr>
<td>Other</td>
<td>$9.34</td>
<td>9%</td>
</tr>
</tbody>
</table>

THE ROLES OF HOSPITAL MARKET POWER AND CHRONIC DISEASE

An underlying source of the rise in overall health plan spending is the growth in the prevalence of chronic disease in general and of multiple chronic conditions in particular. Six in ten U.S. adults have at least one chronic condition, and more than four in ten adults have two or more chronic conditions. II Between 2016 and 2030, chronic disease is projected to cost the U.S. $42 trillion. IIii Hospital spending, the dominant driver of spending growth, can be better controlled by avoiding unnecessary visits through better management and prevention of chronic disease. For example, spending $1 on medicines for adherent patients with congestive heart failure, high blood pressure, diabetes or high cholesterol can generate $3 to $10 in savings on emergency room visits and hospitalizations. IV

Not only is the prevalence of chronic disease increasing, increases in the prevalence of multiple chronic conditions has a multiplier effect on costs. Research has shown that 15% of the growth in spending between 1987 and 2011 was associated with the rising prevalence of chronically ill patients. V In terms of dollar impact on private insurance spending, the number of chronic conditions had the largest effect on spending increase. Compared to annual medical spending for adults with no chronic conditions treated, adults with one chronic condition incurred nearly $2,080 more spending; those with two conditions had nearly $3,000 more; and adults with five or more chronic conditions spent an additional $8,250 more. And yet more patients go untreated or sub optimally treated.

This analysis also supports growing empirical evidence that hospital care is the largest driver of private market health care cost growth. VI Research suggests that hospital prices are the primary driver of spending growth, evident by wide variation in prices and significant mark-ups relative to Medicare and physician services. VII Increasing consolidation of the provider market suggests that the trend in cost growth is unlikely to improve. In fact, a new study by the Health Care Cost Institute (HCCI) reported that more than 70% of hospital metro markets are highly concentrated. VIII Hospital market power and pricing must be addressed to rein in spending growth in the private market.

Another critical finding of this analysis is that one-fifth of the growth in spending is not attributable to direct patient care. We found that administrative costs account for 21% of the growth in spending, equal to that of physician spending growth and seven times that of prescription drugs and nursing care. Reducing spending on excessive administrative costs offers one of the most practical opportunities to control costs without negatively affecting quality of care.

CONCLUSION

As efforts to control cost growth in the private market are explored, it will be critical to consider how drivers of spending growth are linked to chronic disease prevention and management and whether care quality is compromised. Between 2016 and 2018, the growth in spending due to hospitals was more than twice that of the growth due to physician services and administrative costs, and ten times that of prescription drugs and nursing care. These spending patterns reflect more investment in administrative costs and disease complications in the hospital after they’ve occurred then disease prevention and management.

Cost containment efforts such as the persistent rise in shifting costs back to patients through higher cost sharing is likely counterproductive among those who need consistent access to treatment and routine primary care to manage their conditions. Cost sharing should be lower, not higher for these individuals. Reducing the incidence and prevalence of chronic disease should be at the forefront of making health care less expensive.
NOTES

Using CMS NHE data, all service categories but prescription drug spending were defined using the CMS categories. For prescription drug spending, the CMS data measure retail drug spending (spending at outlets that directly serve patients) and account for non-retail drugs administered in hospitals, nursing homes, outpatient clinics, and home health care agencies in the spending totals for these outlets. To combine retail and non-retail drug spending into a single measure, we relied on previous analyses by the Altarum Institute. We estimate non-retail private insurance drug spending using the ratio of non-retail to total drug spending on a national level (about 30%). The estimated dollar amount for non-retail prescription drug spending was subtracted from the NHE hospital, physician and clinic, nursing home spending totals estimated by the Altarum study.

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3 What is the Impact of Chronic Disease on America? Partnership to Fight Chronic Disease. Available at https://www.fightchronicdisease.org/sites/default/files/pfcd_blocks/PFCD_US.FactSheet_FINAL1%20%282%29.pdf


6 UnitedHealth Group. Confronting the High Cost of Hospital Prices. Available at: https://www.unitedhealthgroup.com/newsroom/posts/2019-08-12-confronting-high-hospital-prices.html


8 Health Care Cost Institute. Healthy Marketplace Index. Available at: https://healthcostinstitute.org/research/hmi/hmi-interactive