



Why Health Care Costs Are Rising

In simplest terms, spending on health care is the product of two factors: **price** and **utilization**.

- **Prices** charged by hospitals, physicians, drug companies and other health care providers have risen dramatically – more than the cost of goods and services in general (inflation).
- **Utilization** is way up. Despite rising prices, demand is high. More of us are using health care services more often, for more conditions – including some that were not even treated in the past.

| The Critical Equation | | | | |
|-----------------------|---|-------------|---|---------|
| Price | X | Utilization | = | Expense |

Why are medical prices going up, and why are we using more care? Here's where things get complicated. Experts differ in their conclusions about what – or who – is *most* to blame, but there's widespread agreement that certain cost drivers are at work.

Key Cost Drivers

Americans' lifestyle choices are partly to blame. Unhealthy eating, lack of exercise, smoking, not getting enough sleep, alcohol abuse all put us at higher risk for a host of costly illnesses including heart disease, diabetes, cancer, arthritis and more. Rising obesity rates – in adults *and children* – suggest health care costs will continue their upward climb. About 17% of children and teens in the USA are obese with nearly the same percentage on the brink of becoming so. Extra pounds put children at an increased risk of developing type 2 diabetes, high cholesterol, heart disease and other expensive health problems for their lifetime. (Source: Nanci Hellmich, USA Today, September 13, 2006.)

Advances in medical technology have led to amazing breakthrough treatments. The research and development costs behind these new technologies must be recovered somewhere – typically through the general cost of medical goods and services. And we're all paying the high price. Still, Americans want the latest treatment at their disposal, whether it means an expensive bone marrow transplant that may be yet unproven as treatment, or a heart bypass operation at age 85. Our society's devotion to technological discoveries ensures that costs will continue to rise. No matter what employers do to manage costs, the impact of technology on spending will continue.

Prescription drug costs are rising even faster than medical care overall. Some of the most exciting – and most expensive – developments in medical care involve prescription drugs. Many claim that direct-to-consumer drug ads are prompting patients to request the newest (most expensive) brand-name drug, even when a generic or over-the-counter drug may work just as well. Another concern is that drug ads rarely mention the lifestyle changes or other, non-drug solutions, which are often just as important as drug therapy in improving outcomes. For example, a patient may resist when his physician insists on discussing a low-fat diet, stress management, or allergen avoidance rather than writing a prescription. In one study, up to half of patients said they would feel disappointed, and 15% would consider switching doctors, if their doctor refused a request for an advertised drug. (Source: Richard L. Kravitz, MD, MSPH, Director, Center for Health Services Research in Primary Care, University of California Davis, *JAMA*, November 1, 2000, Vol. 284, No. 17.)

Whatever the reason, employees' usage of prescription drugs has significantly increased recent years and is expected to continue rising.

Did You Know?

The prescription drug industry spends more than \$5 billion annually to support 59 million sales rep visits to doctors and hospitals, including giving gifts to physicians.

Source: Michael A. Steinman, M.D., San Francisco Veterans Affairs Medical Center and University of California, San Francisco. Reprinted in *JAMA*, November 2000 Vol. 284, #17.

Key Cost Drivers, continued

An aging population needs more care. From 1992 to 2002, the older U.S. population (age 65+) increased more than 10%, to 35.6 million. By the year 2030, the older population will more than double to 71.5 million. Not only that, the 85+ population is projected to increase from 4.6 million in 2002 to 9.6 million in 2030. **Source:** U.S. Department of Health and Human Services, Administration on Aging, <http://www.aoa.gov/prof/Statistics/profile/2003/2.asp>.

What's the significance of these statistics? Often, as people age, health problems increase.. There are more people getting treatment for the types of one-time problems that accompany middle age, such as gallbladder surgery. Just as important, more people now need ongoing care for the types of chronic conditions that may develop with age, such as back problems or adult-onset diabetes. Often, that treatment includes expensive prescription drugs.

The costs associated with older people will not diminish anytime soon. Today's youngest Baby Boomers will still be in the workforce 20 years from now. As a demographic group, their health costs will balloon as they age and use medicine to live long, active lives. Advances in health care are part of the reason we're living longer, which in turn is driving our national health care spending even higher.

Legal mandates and a litigation-prone society have raised the risk of liability for many players in the health care system. That leads to higher malpractice insurance premiums, which in turn drives up doctor and hospital fees.

Consolidation in the health care marketplace means less competition. That gives employers less leverage to negotiate favorable pricing. As a result of consolidation, many health care systems have transitioned services from a not-for-profit to for-profit status, adding the cost of "profit" to medical charges. In addition, there continues to be a great deal of opportunity to streamline the wide range of administrative processes used today in order to eliminate waste from the system.

Governmental factors also play a role in health care cost inflation. Hospitals and doctors receive limited reimbursement from Medicare and Medicaid for patients in those systems. To keep operating at a profit, they must recover those "losses" through the prices they charge paying patients, most of whom have coverage from their employers. Ultimately, it's the employer and covered employees who end up footing the bill for the uninsured.

Did You Know?

Approximately 20% to 30% of health care treatments are unnecessary. Millions of patients receive unnecessary treatments each year, leading to complications, reduced productivity, and significantly higher costs.

Source: The National Forum for Health Care Quality Measurement and Reporting.