

What We Can Do About Rising Healthcare Costs

A Special Report from the Blue Cross and Blue Shield Association

“Everybody talks about the weather, but nobody does anything about it.”

-Attributed to Mark Twain

Unlike the weather, we can do something about keeping healthcare affordable and reducing the number of uninsured Americans – if, as a nation, we are willing to work together to find lasting solutions. In fact, the 42 Blue Cross and Blue Shield Plans across the country – which collectively provide coverage for nearly one-in-three Americans – are already at work building stronger relationships with employers, consumers, physicians and hospitals to meet the healthcare needs in their local markets.

Many of us thought the healthcare cost storm had abated in the mid-1990s, when for a while managed care seemed to have brought an end to double-digit healthcare increases.

But rising healthcare costs are back with a vengeance. Last year, Americans faced premium increases of 15 to 25 percent – a trend that is expected to continue for the next several years.

Let’s not fool ourselves. It isn’t simply government or employers that bear the burden of our nation’s \$1.5 trillion medical bill. We all do. It comes directly out of our pockets and paychecks. Rising healthcare costs reduce wages and take-home pay. They also reduce company profits and make it more difficult for American firms to compete in the global marketplace.

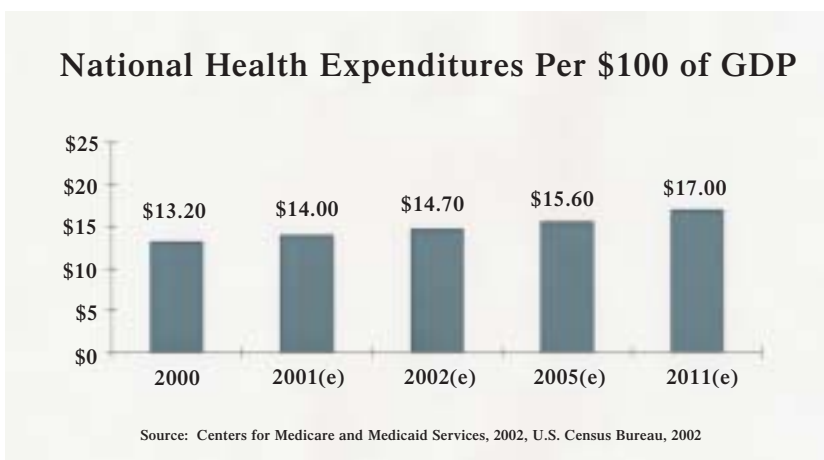
So it’s up to all of us to be better informed about how our healthcare dollars are being spent, using the

same vigilance we apply to our household budgets, children’s college savings and retirement plans.

Today, Americans spend nearly \$15 out of every \$100 on healthcare. According to government forecasts, by 2011 we’ll be spending almost \$17 from every \$100 on health. As

healthcare in this country than any other sector of our economy – including food, housing, automobiles and national defense.

A more sensible way to finding real, lasting solutions is to unearth the key drivers behind rising costs and prioritize steps



a nation, how much we spend on healthcare has been documented widely. How well those healthcare dollars are being invested, however, is the focus of a national, multi-year campaign by the Blue Cross and Blue Shield companies on behalf of the more than 84 million Americans they serve.

“... we need to work together to keep healthcare affordable.”

There are two ways to approach the issue of healthcare affordability. The first option would be to try to take it all on at once. This would be an almost impossible task considering we spend more on

for keeping healthcare affordable and improving access for the millions of Americans who have no healthcare coverage at all.

Finding lasting solutions is not going to be easy. But we need to work together to keep healthcare affordable.

Health insurers cannot do it alone. Hospitals and physicians cannot do it alone either.

It is going to take the healthcare finance expertise of the insurance industry, the healthcare delivery expertise of physicians, hospitals and other providers, and an emphasis on quality outcomes and

value to the patient to make the difference in keeping healthcare affordable.

But it starts with a clear understanding of why these costs are rising so fast.

In this special report, we will examine the real forces behind double-digit healthcare cost increases.

Then we will look at innovative approaches individual Blue Cross and Blue Shield companies are taking to reduce medical errors, improve clinical outcomes and protect customers' health – and their pocketbooks.

Keeping healthcare affordable is the top priority for the Blue Cross and Blue Shield System. This report is an important step in helping to lead a national partnership with consumers, employers, physicians, hospitals, pharmaceutical companies and the government to assure healthcare remains affordable and accessible.

What's Behind the Rise?

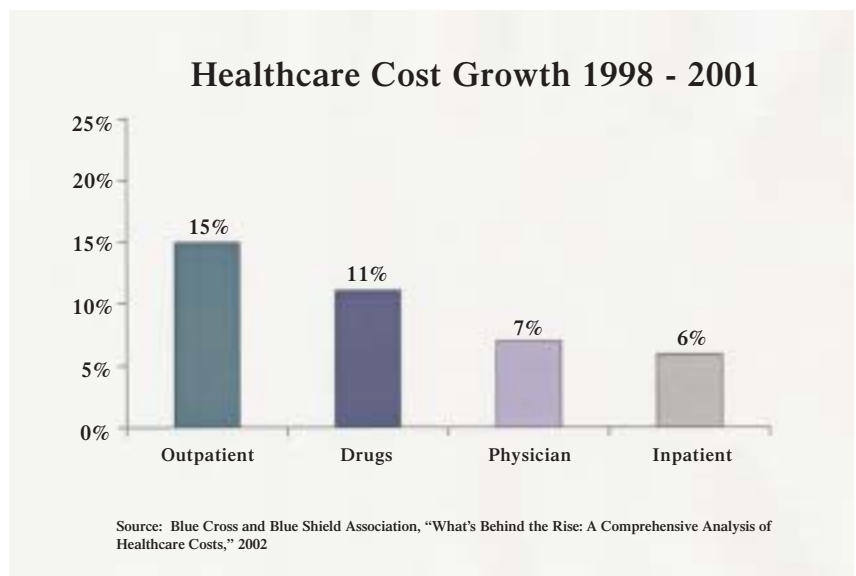
The Blue Cross and Blue Shield Association recently released a series of research studies representing the most current

and comprehensive assessment of the reasons why health costs once again are rising as much as five times faster than the costs of almost everything else we purchase.

The research was conducted by some of the nation's top healthcare economists from the University of

healthcare economy. That year, however, pharmaceutical costs were outpaced by the more rapid growth of outpatient hospital spending, which rose 15 percent.

Does this mean that we have overcome the difficulties associated with skyrocketing drug costs?



Southern California, The Lewin Group and HealthShare Technology, Inc., which performed independent studies to determine the key cost drivers behind hospital inpatient, outpatient and physician costs.

What they found may surprise you.

We all have read a great deal in recent years about the high costs of prescription medicines. Until 2001, pharmaceutical costs were growing faster than any other part of the

Hardly. Prescription drug coverage remains one of our country's most difficult challenges – especially for our aging and Medicare populations who depend heavily on life-enhancing or life-supporting drugs.

Because of the continued shift to higher cost drugs, the increased number of prescriptions being written and the overall increase in the price of drugs, pharmacy costs continue to increase at about 11



percent a year – or about four times the rate of inflation.

It may be surprising to you that the fastest growing part of our country’s ballooning medical bill is not pharmaceuticals, but rather, the cost of hospital services. In reality, 51 percent of everything we spend on healthcare goes to hospital outpatient and inpatient services. In fact, hospital inpatient costs have had a more

significant impact on healthcare expenditures than either prescription drugs or outpatient services. Researchers from the University of Southern California determined that the cost of inpatient hospital services grew by nearly 6 percent annually from 1998 to 2001 – roughly twice the rate of inflation. Even though this rate of growth is much smaller than that of pharmaceuticals (11 percent) and outpatient hospital services (15 percent), due to its sheer size,

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inpatient hospital costs represent 34 percent of the total dollars spent in these three sectors.

Comparatively, according to national health economists from the Lewin Group, the rate of growth for physician services is currently about 7 percent.

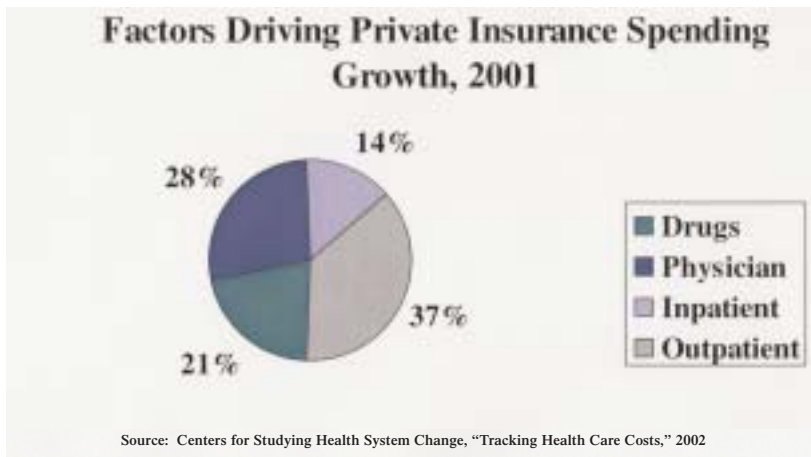
To know the rate of growth and how much we are spending overall on our healthcare is important. But to begin making choices based on what is and what is not adding value to our healthcare system, we first must have a better understanding of the forces driving up healthcare costs.

Based on the results from one of the largest combined public and private sector sample of healthcare cost data ever studied, the Blue

Cross and Blue Shield Association identified three factors that – while not the only drivers of healthcare costs – represent an opportunity to begin prioritizing our efforts to help keep healthcare affordable. These factors include the impact of:

- increased use of new and duplicate technology
- current hospital and physician market structures, including construction, consolidation and facility expansion
- rising labor costs – including the growing nursing shortage.

As these factors impact the cost of physician services, researchers found that 11 percent of the growth in physician cost is related





to technology with 15 percent of cost increases attributed to the current provider market structure. The growth in the number of physicians accounted for 7 percent of cost increases – with the number of specialist physicians increasing by 23 percent and the number of primary care physicians increasing just 3 percent.

Physicians represent the portal through which almost all patient care begins. By and large, no prescription, no test, no treatment is given without the direction of a physician. The patient-physician relationship is the most important part of our healthcare delivery system.

So while the rate of growth for the cost of physician services may seem considerably less than that of prescription drugs and hospital inpatient and outpatient services, we cannot discount the influence physicians have in directing care – including ordering tests and writing

prescriptions – as it relates to the increase in overall healthcare costs.

As we discuss ways of keeping healthcare affordable, new technology and new medication are always on the horizon. These scientific breakthroughs may mean a cure or earlier detection for a deadly disease. They may also mean treatment for crippling ailments that have kept some people in our society from leading normal, pain-free lives.

But advances in medical science will mean little if we cannot afford them.

We can, however, maintain the pipeline of new medical technology and prescription drugs, but only if we as a society can transform our healthcare system into one that adds value to patient care, quality and clinical outcomes.

Seeds of this transformation are already at work in our country today. Countless organizations are

promoting improved quality and value to the patient as a consumer of healthcare services, including The Washington Business Group on Health's Institute on Healthcare Costs and Solutions and the Council for Affordable Quality Healthcare to name a few.

National and local initiatives such as these with Blue Cross and Blue Shield companies from around the country as active partners – represent the beginning of the next generation of American healthcare: affordable, improved quality and increased access.

Today, with hospital costs consuming the largest part of our healthcare dollar and growing at a rate not seen for nearly a decade, it is imperative that we use this collective ingenuity to address the three key factors driving hospital inpatient and outpatient costs: the overuse of new and duplicative technology, the impact of hospital restructuring, including consolidation, new construction and facility

Key Drivers Behind Rising Hospital Costs, 2001			
Inpatient Hospital Costs		Outpatient Hospital Costs	
Labor	20%	Market Structure	35%
Technology	19%	Technology	18%
Market Structure	18%	Physician & Specialist Supply	11%

Source: Blue Cross and Blue Shield Association, "What's Behind the Rise: A Comprehensive Analysis of Healthcare Costs," 2002

expansion, and the labor shortage – particularly the growing nursing shortage.

Medical Technology

What some have described as a medical arms race, in which hospitals and outpatient facilities compete to purchase the latest technology, is having a tremendous impact on the cost of hospital care.

Nearly 20 percent of the rise in hospital inpatient costs is due to technology – 18 percent in outpatient settings.

For example, Kansas has 47 MRI facilities across the state. Michigan, with four times the population of Kansas, has 48 MRI facilities. According to national statistics prorated to the state's population, 19 would be a more appropriate number of MRI facilities.



The number of MRI facilities is not the full story in Kansas, however. Duplication of services is also a tremendous problem. A patient may have an MRI in one part of the state and travel to another part of the state – perhaps to an academic medical facility – for treatment where a second MRI is typically done.

To help reduce the number of unnecessary or duplicative MRIs, Blue Cross and Blue Shield of Kansas is working with the state's hospital and physician associations to establish reasonable protocols for when and how MRIs should be used.

MRIs are just one example of how technology has given us the opportunity to diagnose and treat illnesses earlier. But without a value-based consensus on how best to deploy and use these great advances in medical care, we will

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continue down the path of increased healthcare costs and reduced access to care.

Market Structure

The intense restructuring of the hospital market is compounding the impact of this problem.



Eighteen percent of the rise in hospital inpatient costs is related to market restructuring, including consolidation. Research shows that every 1-percent increase in market share due to consolidation is leading to a 2-percent increase in inpatient expenditures.

Similarly, 35 percent of the increase in outpatient costs is directly related to the provider market structure, including the

expansion of freestanding diagnostic and surgical facilities.

We all realize that to stay competitive and viable in our communities hospitals must upgrade their facilities and keep pace with the latest medical technology. But do we need to

have open MRIs or rapid CT scans located next door to one another?

Labor, Nursing and Quality

Labor costs are the single largest portion of hospital expenses. In particular, the growing nursing shortage in the United States will continue to put upward pressure on wages paid by hospitals. Finding ways to recruit and retain nurses is an important linchpin in keeping healthcare affordable and improving the quality of care we receive.

Nearly \$3 billion annually could be saved by reducing the number of unfavorable outcomes to the level of the nation's best performing hospitals. To achieve this, we must also recognize the important role nurses play in increasing the quality of clinical care as well as their impact on healthcare costs.



Keeping Healthcare Affordable - A Top Priority

Across the United States, Blue Cross and Blue Shield companies are offering customers innovative products and services that help stretch healthcare premium dollars – in some cases, making it possible for small employers to buy coverage for their workers for the first time – or to avoid dropping group coverage altogether.

Healthcare affordability is a major problem for small businesses and the millions of people who work for them. More than 15 million people working for companies with fewer than 100 employees have no healthcare coverage.

New Products and Services

In response, Blue Cross and Blue Shield companies across the country are offering innovative new benefit products specially designed for

small businesses struggling to provide healthcare coverage to their employees.

In Louisiana, for example, where nearly one-fourth of small businesses do not offer health benefits to their employees, Blue Cross and Blue Shield of Louisiana has introduced its trueBlue plan, which features premium savings near 30 percent by offering members separate deductibles for hospital services (both inpatient and outpatient) and for prescription drugs.

Consumer Choice

In response to consumer demand for more choices in coverage and premiums, several Blue Cross and Blue Shield companies have introduced products that provide choices in coverage-type and provider selection. These are accompanied by varying premium and co-payment costs to reflect choices made by consumers.

For example, Blue Cross and Blue Shield of Massachusetts has introduced its Tri-Blue plan that allows employers to offer employees a choice of three plans with varying prices and benefits. Employees can choose to pay more and receive

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more first-dollar coverage, or opt for higher cost-sharing but lower monthly premiums.

Blue Cross of California's Flexscape allows small businesses that pay \$80, \$100 or more per-employee per-month to offer employees a selection of health insurance plans with varying levels of cost. Employees choose the one

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they like and use pre-tax dollars to pay the remaining premium or for non-covered benefits.

Blue Shield of California, recognizing that some hospitals are more expensive than others, recently introduced a “network choice” program for small and mid-sized groups and individuals that allows members to avoid additional copayments or coinsurance by getting services at Blue Shield-preferred hospitals. More than 80 percent of all Blue Shield-affiliated hospitals are in the preferred category. Patients can still go to the other affiliated hospitals, but their out-of-pocket costs are higher.

Reducing Administrative Burdens

Blue Cross and Blue Shield companies are streamlining their own claims handling procedures to reduce administrative costs and make the business side of healthcare function more smoothly. BlueCross BlueShield of South Carolina, for instance, enables both members and physicians to access benefit information 24 hours a day over the Internet, including eligibility, deductibles, referrals, claims payment status as well as a two-year claims history for consumers.

Blue Cross and Blue Shield of Illinois now offers a computer link between physicians' offices and the company's system. The benefit: physicians can get claims resolved immediately instead of the days or

weeks it took to resolve disputes under previous payment systems.

Reaching Out to Consumers

Blue Cross and Blue Shield companies also are stepping up efforts to help the more than 84 million members they serve to better understand how their choices can make a difference in keeping healthcare affordable. From lifestyle choices to understanding the value of generic drugs, Blue Cross and Blue Shield companies are at the forefront of healthcare consumer education and advocacy.

For example, Highmark Blue Cross and Blue Shield has launched an aggressive campaign to help raise awareness among constituents in its Pittsburgh-area market that FDA-approved generic drugs offer the same quality as their name-brand counterparts but at a fraction of the price.

Blue Cross Blue Shield of Michigan's generics campaign provides consumers with a comparison of brand versus generic drug prices via its corporate Web site. The Michigan Blues also reward pharmacists who increase their generic fill rates.

Blue Cross and Blue Shield of Oklahoma is reaching out to employers and consumers with a



public service program to help Oklahomans better understand what's driving healthcare costs in the state and how their choices can

make a difference in keeping healthcare affordable.

These are just a few of the many Blue Cross and Blue Shield Plan initiatives going on all across the country. In addition, the Blue Cross and Blue Shield System is joining forces nationally with leading foundations, consumer and business groups to continue raising awareness and understanding of the impact of rising healthcare costs.

Keeping healthcare affordable, reducing the number of uninsured Americans and improving the quality of care we receive are top priorities for all of us. There is nothing more important in life

than safeguarding the health of loved ones and arranging the best care for them if and when they do become sick.

The Blue Cross and Blue Shield System is honored to be among the leading voices dedicated to improving healthcare affordability and access to care. It's a tremendous challenge. But we believe we need to start now to work together to keep healthcare affordable.

To find out more about what's behind the rise in healthcare costs or to receive a copy of our research, visit us at BCBS.com. You also can find additional materials and receive weekly updates about rising healthcare costs and key health policy issues at BCBSHealthIssues.com.



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