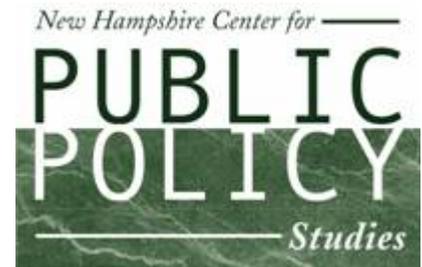


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Will the Real “Cost Drivers” Please Stand Up? The Problem of Identification

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About this Paper

This paper is one of a series of issue briefs published by the NH Center for Public Policy Studies on the broad topic of health-care finance and insuring the New Hampshire workforce. The Concord-based Endowment for Health has sponsored this work and this was first presented to the Endowment’s Citizens’ Roundtable in the fall of 2004.

Will the Real “Cost Drivers” Please Stand Up?

"There is always an easy solution to every human problem—neat, plausible and wrong."

H. L. Mencken

"I have yet to see any problem, however complicated, which, when you looked at it in the right way, did not become still more complicated."

Poul Anderson

"It's so much easier to suggest solutions when you don't know too much about the problem."

Malcolm Forbes

Health care costs have been climbing at double-digit rates in each of the past few years. Health care costs continue to grow faster than inflation and are annually consuming a larger portion of New Hampshire's overall economy. This spiraling cost results in a logical question: "What are the cost drivers that lie behind these increases?" The implication is that if we could describe a limited set of causes, then we might be able to propose policy interventions that would serve to limit future increases.

The literature on "cost drivers" in health care is extensive. While individual researchers seem to be convinced that their research has found the true "cost drivers," the larger picture is much more complex and less assuring. Different researchers come to quite different conclusions depending on how they approached the problem and what data they used as the basis of their analysis. Indeed, researchers don't even have a consistent definition of "cost driver."

I have reviewed dozens of research articles and news reports that have attempted to describe what is driving the cost of health care to ever increasing heights. From those materials I have created a classification of types of drivers that have been cited. This list is meant to be indicative, not exhaustive of all types identified in the literature.

Segment Drivers

Segments of the health care industry where spending has been increasing at the highest rates have been called "cost drivers." These tend to vary over relatively short time periods. Segments that have been identified most often in recent years are:

- In-patient hospital services;
- Out-patient hospital services;
- Outpatient care generally (including ambulatory surgery centers);
- Prescription drugs.

Cost Correlates

Measures that have been shown to be correlated to overall health care costs or correlated to the magnitude of differences in cost among states or regions have been called "cost drivers."

Because statistical correlation itself contains no proof of cause-and-effect, the term "cost driver,"

which conveys cause, is really inappropriate for these. Nevertheless, measures that have been so identified include:

- Proportion of population age 65 and older;
- Personal income;
- Physician-to-population ratio;
- HMO market penetration;
- Hospital missions and market structure (teaching, public, for-profit, etc.).

Demographic Drivers

Measures of the population, society, and general economy that appear to result in more spending on health care have been called “cost drivers.” These are at least one step removed from being a true cause because they assume a link to a health condition and need/willingness to spend.

Examples:

- Population increase generally;
- Increase in elderly population, especially those over 75;
- Increasing personal income.

Health Condition Drivers

Measures of illness or other health conditions that have changed over time in excess of general demographic trends have been called “cost drivers.” The need for a greater volume of services to meet the needs of individuals with these conditions may be offset by reduced needs for other conditions. Examples:

- Increased prevalence of diabetes;
- Increased prevalence of asthma;
- Increased diagnosis of mental disorders, (depression);
- Increased survival of infants with complex conditions;
- Increased prevalence of hypertension;
- Increasingly obese population.

Other Demand Drivers

There are aspects of demand for health care that are not directly the result of the demographics or health conditions. These other sources of demand have also been called “cost drivers.”

Examples:

- Request for care in ERs that should be elsewhere;
- Response to direct-to-consumer advertising of prescription drugs;
- Decline in effectiveness of older antibiotics.

Line Item Drivers

Increasing amounts actually being spent by health care providers in their operating budgets are perhaps the most direct and most easily quantifiable of “cost drivers.” Out of pocket spending by consumers can also be tracked. The accounting profession has a long history of making some of these these measurable. Examples:

- Aggregate wages paid by hospitals and other provider institutions
- Provider spending on new medical technology (capital and consumable)

- Consumer spending on new medical technology (primarily drugs)
- Malpractice costs (insurance or claims against self-insurance)
- Health insurance underwriting cycle: increasing company profits
- Increasing quantities of medication used per patient

Policy Drivers

Public policy and health system practice can contribute to the cost of health care in various ways. Each of the following has been proposed as a “cost driver:”

- Relaxed Certificate of Need (CON) – dwindling control of capital expenditures
- Retreat from tightly managed care (HMOs)
- Allowing merger of pharmaceutical companies
- Extended patent protections for drugs
- Allowing hospital consolidations that result in monopolies
- Increased cost-shifting from Medicare and Medicaid
- Administrative costs imposed by complex claims processing

The search for a small, easily described set of cost drivers is a fruitless endeavor. Each of the bulleted items above has been identified by some authority as an important “cost driver.” Certainly there are many others not contained in this list. To further complicate matters, as two researchers have correctly pointed out about a much smaller list, “...these individual factors interact with one another to make their collective stimulus much greater than the sum of their individual effects.”¹

The health care system is a web of institutions, laws, practices, technology, and human beings. Like a regional ecosystem, it is composed of distinct parts that are inter-related in complex ways. Changes in one part of the system are simultaneously the cause and the effect of changes in other parts of the system. Asking what its ultimate cost drivers may be is similar to asking what the ultimate drivers of the global weather system may be. There is no one satisfactory answer.

¹ Gabel, Jon & Karen Fitzner, “New Evidence to Explain Rising Healthcare Costs,” *The American Journal of Managed Care*, Volume 9, Special Issue 1, June 2003.

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