Health Care Costs: Does Maine Have a Problem and What Should We Do About It?

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What is the Problem?

There is a growing sense of crisis associated with the cost of health care services as reflected in rapidly increasing insurance premiums, larger out of pocket expenditures for consumers, and expanding shortfalls in the State's budget. The impact of this crisis has included a reduction in the number of insurance companies providing health insurance in Maine, an increase in the number of businesses (and especially smaller businesses) that no longer provide health insurance, and a growing number of citizens eligible for Medicaid coverage.

This policy brief examines the factors contributing to the rise in health care costs, the implications of cost increases, and potential solutions.

How Much Does Maine Spend on Health Care?

In 2001, health care spending in Maine is estimated to be in excess of $5 billion dollars. Health care represents approximately 14% of the state's gross state product. Total annual spending in Maine amounts to over $4,000 per person.

Maine has experienced a high rate of growth in spending in the last decade with per capita spending rising by 25% from 1995 to 1998.

Approximately, three-quarters of this spending (or nearly $4 billion dollars) is borne by someone other than the consumer at the time he or she receives services. These payers include public programs, like Medicare and Medicaid, as well as private, employer-based insurance plans.
Is Spending Too High in Maine?

While $5 billion dollars is a lot of money, there are also many examples where additional expenditures for health care may be warranted. The question, therefore, is not whether $5+ billion is too high, or too low. Instead, the reasonableness of this amount must be assessed in a comparative context; that is, what can Maine afford given the national and global environment within which it competes?

When compared to the United States, health care spending in Maine represents a larger share of the gross domestic product. Moreover, the rate of growth in health care spending in Maine has been greater than in the rest of New England and the United States and has exceeded the growth in personal income in the state.

Why is Spending Increasing?

Health care spending is the product of the prices we pay for health services and the amount of service we use. And while simple demographics - the aging of the population - are certainly contributory factors, both unit prices and utilization are rising faster than would be indicated by demographics. There are many factors that contribute to this rising demand. For example, the increased demand for and use of complex and expensive services such as cardiac catheterization and heart surgery are associated with the increased availability of these services. Similarly, the increased availability and use of expensive pharmaceuticals have contributed to making the rise in spending for prescription drugs a major driver of increased public and private health care spending in recent years. And while technological and pharmaceutical advances have resulted in some savings (i.e., less inpatient hospitalizations for certain conditions), the net impact has certainly contributed to greater overall spending.

The increased use of services is also attributable to the relatively few financial barriers to the use of services. Most privately and publicly insured consumers are still able to freely use health care services with little out of pocket cost. Unlike other goods and services, the reasonableness of a specific service cost is not tested by conventional market disciplines. For most privately insured Mainers, cost sensitivity is introduced only indirectly through premium contributions to their employer based insurance plans. While effective for protecting consumers against catastrophic health care expenses, present financing arrangements provide no connection between the service cost and quality and the demand for health care services.

Medical inflation continues to exceed general inflation, despite efforts by employers and health plans to change the patterns of use, increase quality, and reduce price increases through greater competition. Most health care providers continue to compete for patient on services, rather than on cost and quality of services.

Health care presents some unique market challenges. It is often very difficult to reliably predict the set of products or services associated with an episode of medical care treatment and consequently the expected and reasonable costs. A newly diagnosed diabetic will enter a course of treatment that is likely to be continuous with little probability that a “cure” will be achieved. What is a reasonably defined episode of care? What is the predictable set of services associated with the defined episode of care? Can these definitions of episode as well as service set be consistently applied to all newly identified diabetics? Only when these questions are answered can one establish, predict and compare the total charges of the provider (and costs to the payer) associated with a specific, presenting morbidity.
Prices and costs in the health care system are also distorted and increased by what is known as "cost-shifting". All producers of goods and services have a business cost associated with bad debt, uncollectible accounts and discounts. These costs are recovered in the prices established for other customers. In the case of health care, it is the magnitude and variety of cost shifting between different payers that create a significant policy labyrinth. In 1999, costs associated with bad debt and charity care exceeded $163 million dollars. These expenditures are largely generated by persons without any insurance arrangements who present themselves for care, usually in the most expensive setting and usually in acute medical need. Most of these expenditures are shifted to non government payers. It is estimated that these expenditures represent about 8 percent of the total expenditures by Maine residents with private insurance.

Fee discounts imposed by government payers (Medicare and Medicaid) are another critical source of cost shifting in the health care system. Large, private purchasers and insurance plans also contribute to cost shifting to the extent that fee discounts are provided in exchange for certain business concessions.

While private payers are usually identified as being cost shifted "against", there are examples where the opposite is true. Benefit limits for mental health, substance abuse and long term care are often established by private insurance plans. If a consumer requires these services beyond those provided by private insurance plan, that consumer will often become Medicaid eligible, effectively shifting the service costs for this individual from a private to public payer.

The Implications of Increased Health Care Spending

Payers, policymakers and others often question the efficiency of present system costs. There is little relationship in Maine and in the nation between the level of our investments in the health care system and the health of the population. We know that Americans in general and Mainers in particular are not healthier than citizens of other modern industrial countries which allocate proportionally fewer resources to health care than we do. Indeed, there is evidence that the citizenry's health status is higher in these other countries. This suggests that the American health care system is inefficient and wasteful in allocating health care resources. The absence of coordinated planning is often referenced as an example of this inefficiency and was often mentioned in the recent controversy associated with establishing new cardiac services in the state. The varied administrative requirements associated with multiple private and public payment programs also contribute to the system's inefficiency.

Rapidly rising health care costs represent a growing burden for employers and individuals whose increased premiums for health insurance are far outstripping the growth in business revenue and profits, or individual income. For public programs such as Medicaid and Medicare, increasing health care costs are placing significant strains on state federal budgets.

As policymakers struggle to allocate limited resources among health and non-health priorities (such as education), the data implicitly suggest that health care enjoys a higher priority among Maine citizens than other goods and services. But because most health costs are not borne directly by the consumer, they represent an "overhead" associated with living and working in Maine; an overhead measured in terms of taxes and business operating costs that is greater than other states within the U.S. and nations.
Significantly, it has been also observed that health care is also an important component of our state’s and national economies and represents an important source of economic growth. Some argue as well that there is no reason why spending a higher percentage of our gross domestic product on health care is necessarily a problem as health care tends to be a desirable (e.g. good wages) industry.

Are There Solutions to Rising Health Care Costs?

Through the nineties, managed care was the foundation for a variety of private and public policy initiatives aimed at controlling health care costs. At its core, managed care required providers to assume accountability for clinical as well as resource allocation decisions. Consumers were promised more comprehensive benefits in exchange for restraints on their access to care. Managed care replaced a regulatory framework that characterized policy in the seventies and eighties and focused on centralized planning, price setting, and consumer cost sharing at the time services were provided.

Recent increases in health care costs suggest that managed care is no longer effective. Although health care cost increases abetted during the mid-1990’s, cost containment gains have not been sustainable largely because of the difficulties of imposing a competitive market structure on the health care system.

Unfortunately there are no "silver bullets" for addressing the problem of health care costs. In the absence of a system-wide strategy, employers and health plans are employing a variety of cost containment approaches in the design of their health benefit programs. These include requiring greater premium cost-sharing and co-insurance from employees, introducing preferred provider programs, and/or restructuring their contributions to employee health benefit programs in ways that require employees to be more cost-conscious in the choice of health plans and in their use of health services. In the face of burgeoning state and federal budget deficits, public programs are reducing costs by limiting or reducing their payments to providers and by introducing cost containment programs similar to those adopted by the private sector.

The problem of health care costs begs for a more rational system for policymakers and citizens to begin making difficult allocation decisions and reapply past approaches, such as greater consumer engagement, medical management, regulation and the like; this time with hopefully better resolve as well as better understanding of the effectiveness and limitations associated with each approach.