



## Forum Session Meeting Announcement

**Friday, September 23, 2005**  
11:45am — Lunch  
12:15pm–2:00pm — Discussion

# Location, Location, Location: Market Characteristics and Private Payer Health Care Spending

### A Discussion Featuring:

**Christine Brudevold, MPH, PhD**  
*Assistant Director*  
Government Accountability Office

### With Comments From:

**Joseph R. Antos, PhD**  
*Resident Scholar*  
American Enterprise Institute

**Robert Berenson, MD**  
*Senior Fellow*  
Urban Institute

**Michael A. Morrisey, MA, PhD**  
*Professor and Director*  
Lister Hill Center for Health Policy  
University of Alabama at Birmingham

### Location

**Reserve Officers Association  
of the United States**  
One Constitution Avenue, NE  
Congressional Hall of Honor  
Fifth Floor  
(Across from the Dirksen Senate  
Office Building)

### Registration Required

Space is limited. Please respond  
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# Location, Location, Location: Market Characteristics and Private Payer Health Care Spending

## OVERVIEW

*This Forum session will highlight a soon-to-be released Government Accountability Office (GAO) report on geographic variation in hospital and physician prices paid by private health plans. This study expands the research on geographic variation in health care spending by adding information on the market area factors that affect the price of services. After a summary of the report, a panel of health policy experts will discuss the implications of the GAO findings in the context of other market research and draw out its implications for health policy.*

## SESSION

Health care spending varies dramatically across geographic areas with little rhyme or reason.<sup>1</sup> Variation in Medicare spending per beneficiary is primarily determined by differences in the use of services, not in the prices Medicare pays for services. Private payer spending variation, however, reflects differences in both components of expenditures: service use and price per service. Unlike Medicare, private payers negotiate prices with local providers. Sometimes the providers call the shots in these negotiations, and sometimes the payers have the final say in establishing the prices. How this ultimately affects spending is just beginning to be explored.

As policymakers continue to grapple with ways to control health care spending growth, both the use and price of services will be targets for change. The geographic variation in these components of health care spending may offer important insights into how health care markets work and how markets affect health care spending. Understanding the determinants of the use and price of services may also provide clues about the possible consequences of policies to influence spending growth—particularly as more Medicare beneficiaries receive health care through private plans, as envisioned in the Medicare Prescription Drug, Improvement and Modernization Act (MMA) of 2003.

Of the two components of expenditures, research on Medicare utilization is rather extensive. The Medicare Payment Advisory Commission (MedPAC) found that spending per Medicare beneficiary averaged about \$400 more in the highest spending state than in the lowest spending state.<sup>2</sup> The higher spending was due to unexplained differences in the use of services. Other research looking at small area variations, conducted by

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Wennberg and colleagues, found that service use was higher in areas with more hospital capacity and that use of discretionary services was more variable than that of well established treatments.<sup>3</sup> Even though higher use translated into higher spending, it did not necessarily contribute to improved quality of care.

Understanding the other component of expenditures, price variation, is more difficult because the data are harder to come by. Evidence indicates that prices are higher where hospitals have more clout in negotiating with payers and lower where hospitals face greater competition.<sup>4</sup> Competition may also affect physician fees. Private insurers pay higher physician fees in areas with lower overall wage levels, possibly because there were fewer competing physicians.<sup>5</sup> These analyses point to the interaction between local market dynamics and private health care spending.

### **Variation in Private Payers' Health Care Prices**

An analysis published in 2004 by the Government Accountability Office (GAO) examined the contribution of both service use and price to geographic differences in spending for private payers.<sup>6</sup> Congressman Paul Ryan (R-WI) asked GAO to examine geographic variation in health care spending because of reports from his district that insurers faced higher prices in Milwaukee than in similarly situated areas. GAO used claims data from the largest national insurers participating in the Federal Employees Health Benefits Program (FEHBP) to conduct its analysis.

Health care spending for federal employees under 65 who were insured through FEHBP varied by more than 110 percent across metropolitan areas in 2001. The average price of an inpatient stay was approximately 250 percent higher in the highest priced metropolitan area than in the lowest—even after adjusting for differences in area wages, patient mix, and severity of cases. The average price of a physician visit varied by about 100 percent from the highest to the lowest priced area.

Key stakeholders in higher priced areas thought the high prices were needed to offset losses due to uncompensated care and low public payer rates. The analysis, however, found no support for this assertion. Market forces, such as competition among providers and presence of capitated managed care plans, however, often marked the differences between higher and lower-priced areas. Areas with fewer providers tended to have the highest health care prices because insurers had to contract with all or almost all area providers.

The forthcoming GAO report, which will be available at the Forum session, expands on the 2004 report by providing national data on price and spending variation and analyses of the factors that contribute to that variation. Christine Brudevold, assistant director on the Medicare Payments Team, will present the findings from the GAO report. Her presentation will be followed by comments from Joseph Antos, resident scholar

at the American Enterprise Institute; Robert Berenson, senior fellow at the Urban Institute; and Michael Morrissey, professor, University of Alabama at Birmingham.

## KEY QUESTIONS

- What factors are related to the variation in prices for inpatient hospital services? Physician visits? Why would different factors affect hospital prices and physician prices?
- What is the relation between the price of care and the utilization of care for hospital services? For physician services? Why would this relation differ?
- How can market dynamics best be used to control prices? To control utilization? How are these market dynamics likely to change over time?
- What do geographic differences in prices imply about Medicare fee-for-service payment policies? Medicare Advantage payment policies?
- What is the role of anti-trust enforcement policies in controlling spending? What would be the effect of stronger anti-trust enforcement?
- How does the variation in prices affect consumers? Can consumer-driven health care products affect market dynamics?

## SPEAKERS

**Christine Brudevold, MPH, PhD**, is an assistant director on the Medicare Payments Team at the Government Accountability Office (GAO). She spearheaded GAO's work on geographic variations in private sector spending.

**Joseph R. Antos, PhD**, is a resident scholar at the American Enterprise Institute (AEI), where he works on health policy, including Medicare reform, the regulation of private health insurance, and challenges facing the uninsured. Prior to that, he was assistant director for health and human resources at the Congressional Budget Office.

**Robert Berenson, MD**, is a senior fellow at the Urban Institute. He has practiced medicine; served in two administrations, where he was in charge of Medicare payment policy and managed care contracting; and managed a successful preferred provider organization.

**Michael A. Morrissey, MA, PhD**, is a professor and director at the Lister Hill Center for Health Policy at the University of Alabama at Birmingham, with secondary faculty appointments in the Department of Economics, the Department of Health Services Administration, and the Department of Sociology. His research has focused on managed care, employer-sponsored health insurance, hospital markets, health care finance, and the effects of payment systems.

## ENDNOTES

1. See "Variations Revisited," *Health Affairs*, Web Exclusives, October 7, 2004; available at <http://content.healthaffairs.org/cgi/content/full/hlthaff.var.5/DC1>.
2. Medicare Payment Advisory Commission. *Report to the Congress: Variation and Innovation in Medicare*, June 2003; available at [www.medpac.gov/publications/congressional\\_reports/June03\\_Entire\\_Report.pdf](http://www.medpac.gov/publications/congressional_reports/June03_Entire_Report.pdf).
3. John E. Wennberg *et al.*, *The Dartmouth Atlas of Health Care in the United States* (Hanover, NH: Dartmouth Medical School, 1999; and John E. Wennberg, Elliot S. Fisher, and J. S. Skinner, "Geography and the Debate over Medicare Reform," *Health Affairs*, Web Exclusives (February 13, 2002); available at <http://content.healthaffairs.org/cgi/reprint/hlthaff.w2.96v1>.
4. Cory Capps and David Dranove, "Hospital Consolidation and Negotiated PPO Prices," *Health Affairs*, 23, no. 2 (March/April 2004): 175–181.
5. Dyckman & Associates, *Survey of Health Plans Concerning Physician Fees and Payment Methodology*, August 2003; available at [www.medpac.gov/publications/contractor\\_reports/Aug03\\_PhysPaySurvey\(cont\)Rpt.pdf](http://www.medpac.gov/publications/contractor_reports/Aug03_PhysPaySurvey(cont)Rpt.pdf).
6. U.S. Government Accountability Office (GAO), *Milwaukee Health Care Spending Compared to Other Metropolitan Areas: Geographic Variation in Spending for Enrollees in the Federal Employees Health Benefits Program*, GAO-04-1000R, August 18, 2004; available at [www.gao.gov/new.items/d041000r.pdf](http://www.gao.gov/new.items/d041000r.pdf).



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