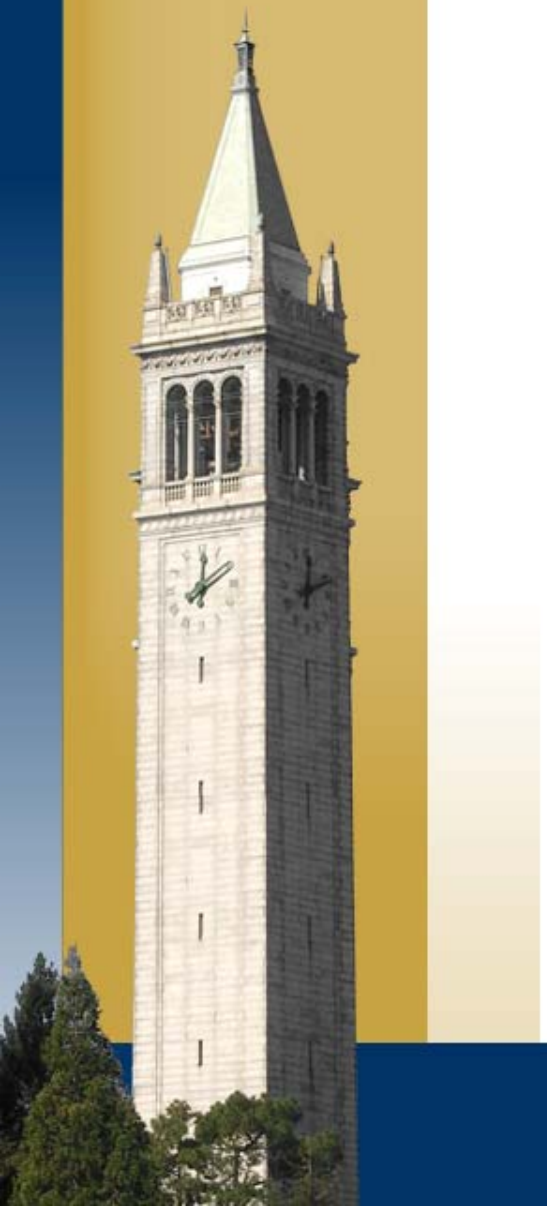

BERKELEY CENTER
FOR HEALTH TECHNOLOGY

Price Transparency Needs Reference Pricing Needs Bundled Pricing Needs Price Transparency

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Overview

- Love for and limits of price transparency
- Reference pricing explained
- The PERS reference pricing initiative
- Lessons and limits of the PERS initiative
- Implications for bundled pricing and transparency

Motherhood and Apple Pie

- We all believe in price transparency
  - Supports informed consumer choice
  - Gives incentives to providers to compete on price
  - Price pressure creates pressure to reduce costs
  - Consumer and market pressures for efficiency reduce need for top-down governmental regulation of prices
  - Everything else is on Facebook: why not prices?

Transparency of Irrational Prices Does not Rational Choices Make

- Health care prices are inscrutable and irrational. Making them transparent is good for jokes but not for choices
- For simple components of care, transparency of existing prices is okay
  - Flu shots, lasik, generic drugs
- But most health care is consumed as a course or episode of care, and it's the episode price that counts for the consumer
- We want the price of the car, not of the sparkplugs, transmission, drive chain
- Putting hospital chargemasters online?

Bundled Payment

- Medicare, Integrated Healthcare Association, Prometheus, and other good people have pioneered bundled payment
- It's been a hard slog, with little to show
- One major hurdle: Providers see no benefit to negotiating bundled payments, much less in making them transparent, since they would earn no new patients and the payers want to demand savings from bundling.
- Bundled payment without benefit re-design is a great idea no one adopts

The Importance of Insurance Benefit Re-Design

- Insurance has numerous important benefits
  - Improve access: improve health
  - Promote innovation: most diseases are too rare to justify R&D if only patients pay for care
- But comprehensive coverage has many faults
  - Moral hazard: over-use of unnecessary services
  - Discourage price-shopping by consumers, encourages aggressive pricing by suppliers
  - Creates culture whereby medicine is a “free” entitlement rather than a valuable scarce good
    - Backlash against governmental cost controls
    - Backlash against private cost controls

Targets: Prices and Quantities

- Cost sharing can target inappropriate services (quantities) or over-priced services (prices)
- Targeting inappropriate care is very volatile
  - Patients trust physicians, not insurers/employers
  - Backlash against capitation, prior authorization, cost effectiveness analysis, coverage policy, managed care, Obamacare
- Targeting high prices for health care is easier
  - Most people are used to shopping for low prices
  - There is a wide range of prices for similar medical services and products
- If consumers learn to shop for price, maybe they can learn to shop for appropriate care as well

Limits of Current Designs

- Annual deductible
  - Target low-cost primary/preventive services rather than high-cost specialty services
  - Arbitrary link to calendar year
- Coinsurance (%)
  - Exposes patient to only a % of cost or price
  - Limited by annual out-of-pocket maximum
- Copayments ($)
  - Same price is charged to consumer regardless of price charged to insurer
  - Copayment is small relative to price of specialty services

Reference Pricing

- Sponsor (employer, insurer) establishes a maximum contribution (reference price) it will make towards paying for a particular service/product
  - This RP limit is set at minimum or median of the prices charged by comparable providers
- Patient must pay full difference between the RP limit and the actual price charged by the provider
  - Patient payment is not limited by OOP max
  - Patient has good coverage for low priced options but full responsibility for choice
  - Note: Provider price is the negotiated “allowed charge” not the arbitrary list price

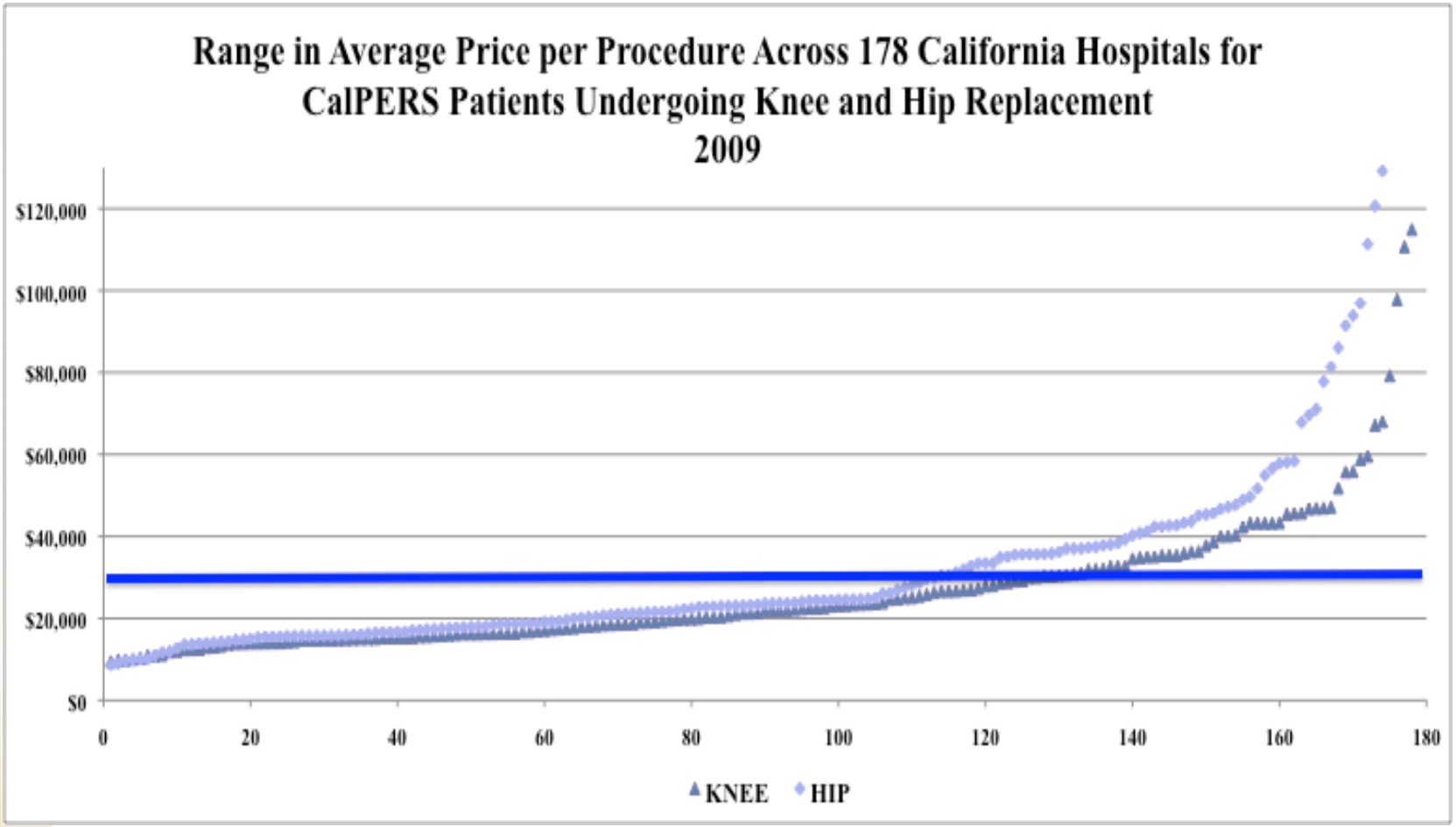
More on Reference Pricing

- Reference pricing is best applied to products/services where there is wide variation in price but only narrow variation in quality
  - Pharmaceuticals in Europe
  - Safeway: Lab tests, diagnostic imaging
  - PERS: high volume IP and OP surgeries
- It can be conceptualized as “reverse deductible”
- It can be conceptualized as a coverage exclusion rather than benefit limit or cost sharing
  - Advocates seek to avoid confrontation with federal “essential benefits” requirement as well as state insurance regulation (bans on excessive cost sharing)

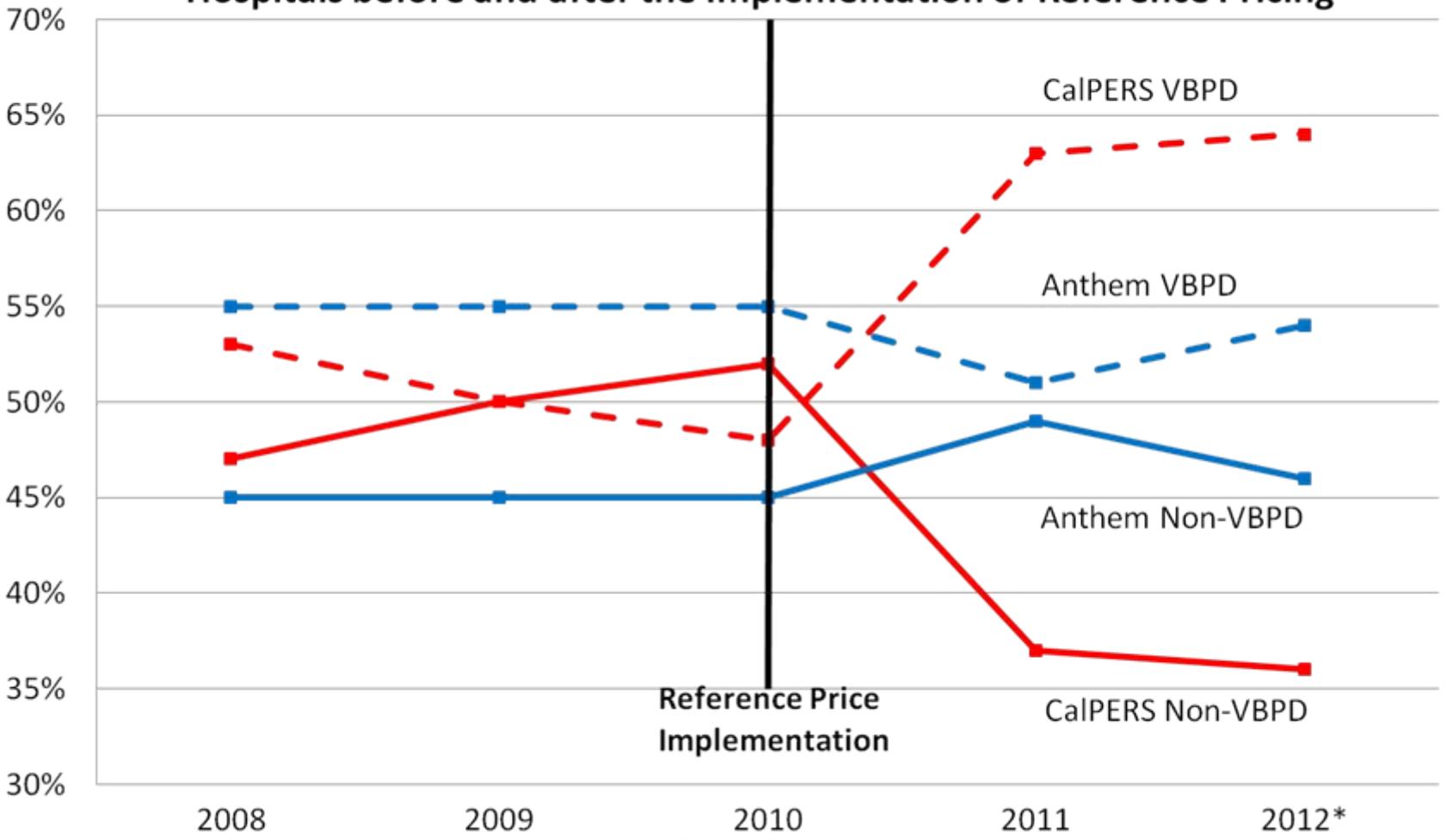
Reference Pricing for Orthopedic Surgery at PERS

- PERS covers 1.3M public employees, of which 450K are in self-insured PPO
- It was paying $20K to $120K for joint replacement
- In January 2011 established RP limit of $30K
- It identified 41 hospitals as “value-based purchasing design” facilities (charge less than $30K, geographic dispersion, score well on BCBSA quality metrics) and initiated employee communication strategy
- For HMO enrollees, it relied on narrow network rather than reference pricing

Variation in Hospital Prices

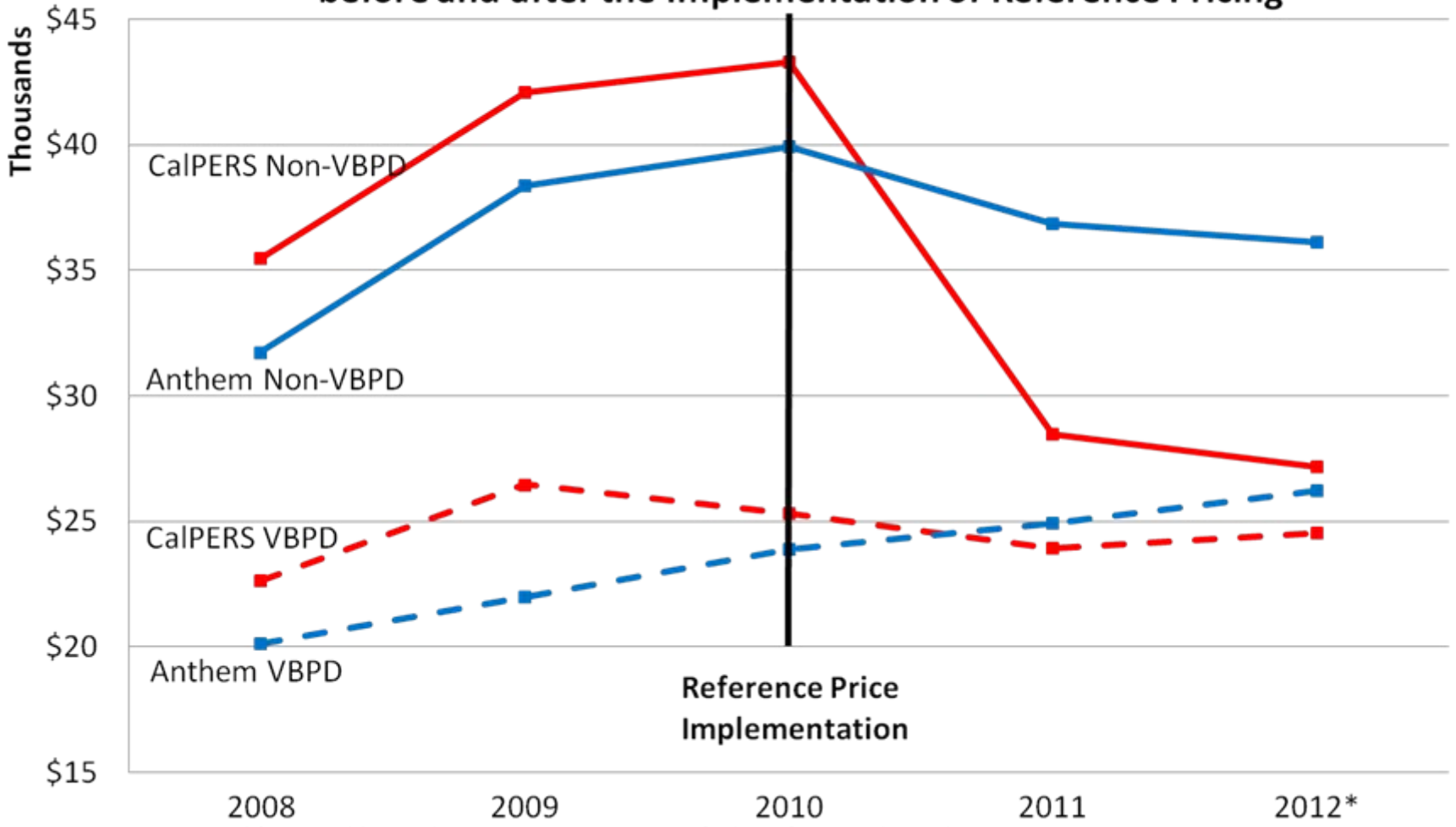


Percentage of Surgery Patients Choosing Low-Priced and High-Priced Hospitals before and after the Implementation of Reference Pricing



Source: California Public Employees Retirement System (CalPERS) and Anthem Blue Cross.
*Through September of 2012 only.

Prices for Knee and Hip Replacement Surgery in California Hospitals before and after the Implementation of Reference Pricing



Source: California Public Employees Retirement System (CalPERS) and Anthem Blue Cross.
All prices in 2011 dollars. VBPD : Value Based Purchasing Design. *Through September of 2012 only.

PERS Savings: Payments Compared to What Would have been Paid Without Reference Pricing

- **2011 : -19.6% ($2.8 million)**
- **2012 : -18.6% ($2.7 million)**
- **Cumulative savings: $5.5 million**
- **Additional cumulative consumer (enrollee) savings: $0.5 million**

Discussion of PERS Results

- **Reference pricing for high-cost surgery induces enrollees to use lower-priced facilities**
  - But the bigger effect is on hospital prices
  - This was probably an over-reaction by hospitals. In other applications, RP will have its greatest effect on consumer choices and market shares
- **The PERS results were achieved with only elementary 'transparency' (list of 41 hospitals). Real reference pricing would have required hospitals to negotiated bundled rates that were transparent to the patient.**
- **PERS is not seeking to expand reference pricing to full set of hospital services, but merely to ambulatory procedures it wishes to move from hospital-based to freestanding surgicenters**

Limits of Transparency

- **Price transparency is not a panacea for the ills of the health care system but:**
  - It helps support patients as shoppers for value
  - It can stimulate price competition among providers
  - It is consistent with our larger culture of sunshine, truth, honesty, and Facebook
- **But to transform health care it requires reference pricing and bundled payment**

Limits of Reference Pricing

- **Reference pricing is not a panacea but:**
  - It helps convert patients into shoppers for value
  - It stimulates price competition among providers
  - It may help change culture of medicine: from a free entitlement to be used without thought to a valuable social resource to be cherished and used with care
- **But to transform health care it requires price transparency and bundled pricing**

Limits of Bundled Payment

- **Bundled pricing is not a panacea but:**
  - It gives incentives to doctors and hospitals to work together for efficiency and cost reduction
  - It relieves insurers of burden of managing care
  - It allows payers to compare price with performance in establishing networks
- **But to transform health care, it requires price transparency and reference pricing**

Conclusion

- Price transparency will only support consumer choice if (1) consumers care about prices and (2) consumers can understand prices
- Reference pricing will only motivate consumer choice if (1) prices are transparent and (2) consumers can understand prices
- Bundled payment will only make prices understandable if it is adopted, and it will only be adopted if (1) consumers care about prices and (2) prices are transparent
- Ideally we enact all three simultaneously, but, realistically, we need to decide:
- Where to break into the circle?