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Analysis of Selected Washington State Health Plan Rate Filings 2022 - 2024

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About the Author

Analysis Group is one of the largest international economics consulting firms, with more than 1,200 professionals across 14 offices in North America, Europe, and Asia. Since 1981, we have provided expertise in economics, finance, health care analytics, and strategy to top law firms, Fortune Global 500 companies, and government agencies worldwide.

Mr. Deal is a Managing Principal with Analysis Group and oversees all economic analyses in the Menlo Park, California office. Mr. Deal began his consulting career working for a consulting group from Harvard University, where he did his graduate training in Health Policy and Public Policy. Prior to joining Analysis Group, Mr. Deal spent several years in the early 1990s working as a senior consultant and manager with Arthur Andersen's Seattle office, where he worked with hospitals throughout the Pacific Northwest on a range of operational and strategic projects. Mr. Deal's current practice involves performing economic analyses across a wide variety of industries, including healthcare, insurance, finance, and technology.

Overview

In recent years, health insurers and health purchasers in Washington State have stated in their premium rate filings, public statements, and hearing testimony that hospital payment *rate increases* are the primary driver of increases to overall health care premiums and health care costs. Proposed legislation cites studies that generally attribute increases to health care costs to increased hospital leverage as a result of consolidation, but we are unaware of any study that quantifies or confirms that relationship for Washington State.

At the same time, regulators are aware that there are many factors driving proposed rate increases. For example, in its October 16, 2023 presentation to the House Health Care Committee, Office of the Insurance Commissioner (OIC) staff mentioned several cost drivers other than hospital unit price increases that had significantly affecting premiums, but staff had not quantified their specific impact on premiums. These factors included:

- Pent-up demand for elective procedures delayed during the public health emergency (higher utilization)
- Increases to the cost of prescription drugs, including increased off-label use
- Increases to administrative costs and general inflation
- Changes to what payments insurers are either owed or received under the Affordable Care Act (ACA) risk adjustment program
- The extent the insurer has high risk enrollees who incur high dollar claims.

In order to better understand the factors contributing to proposed rate increases, Analysis Group has been asked by the Washington State Hospital Association (WSHA) to review the health plan premium rate filing requests submitted by several of the largest health plans serving Washington State residents. The purpose of the analysis is to evaluate the relative contribution of various factors that can result in increasing healthcare premiums, of which hospital rate increases are one source.

This report presents the results of this analysis. We find that while hospital rate increases (increases in the unit cost of each service offered by a hospital) are a contributor, they are not the major driver of

health care cost increases leading to proposed rate increases, Instead, other factors such as increases in utilization (the number of services being provided), drug cost increases, and changes in insurer risk payments are collectively a larger contributor to proposed rate increases.

Background and Methodology

Health plans in Washington State are required to file an application for proposed rate increases with the Washington State OIC each year. These filings are posted and available on the OIC website (www. https://www.insurance.wa.gov/health-insurance-rate-increases). There may be multiple documents and hundreds of pages of actuarial and other information associated with each of the filings.

As part of these documents, health plans are required to list the factors that contribute to their proposed rate filing. These include the following:

- Changes in unit costs for medical services (hospital and professional services, such as physicians).
- Changes in utilization for medical services
- Changes in unit costs for prescription drugs
- Changes in utilization for prescription drugs
- Changes in risk adjustment payments based on the risk profile of the plan's enrollees
- Changes due to other factors

Medical services are reported as a single category, including both hospital and physician services. Where relevant, to separately estimate the unit cost and utilization changes for hospital and physician services components of medical services, Analysis Group used information in each rate filings showing the share of the medical services category due to hospital services and professional services for each insurer, as well as using reported changes in unit costs for physician services.

For this study, Analysis Group selected small group and where available, the individual filings of three of the largest health insurers in Washington State: United Healthcare, Aetna, and Premera Blue Cross for plan years 2022, 2023, and 2024. Where applicable, Analysis Group used approved overall rate increases where they differed from the overall proposed rate increases.

Summary of Major Findings

- While overall insurer premium increases were often greater than inflation, the changes in reported hospital unit costs were generally near the overall general inflation rate. (See Analysis 1) For most hospitals, the unit price increases have been lower than increases in the cost of providing hospital care, including labor costs of nursing and other staff.

- While increases to hospital payment rates were a contributing factor to increased premiums, other factors, such as expected increases to utilization, drug price increases, and changes in risk adjustment factors, cumulatively account for most of the premium rate increase. This was particularly true of the Premera individual plan filing, where the portion of the premium increase attributable to hospital payment rate increases was about 4 percent, less than a quarter of Premera's 17.2% total premium increase for 2024. (See Analysis 2)

- Total expenditures for hospital inpatient and outpatient services, which include both unit cost increases and changes in utilization, are reported by plans to be stable or declining as a proportion of expenditures for all medical services. While outpatient services have increased over time, this has been more than offset by decreases in inpatient expenditures, consistent with the view that hospitals have been transitioning care to the less expensive outpatient setting where possible. (See Analysis 3)

Presentation of Findings

Analysis 1: Hospital/Physician Unit Cost Increases by Year

In this first set of analyses, Analysis Group extracted from the rate filings the reported overall annual cost changes for Medical Care and Prescription Drugs. Overall annual cost changes are reported separately as changes in unit costs and changes in utilization. As discussed above, hospitals are not separately reported by health plans, and the Medical Care category is comprised primary of hospital and physician/other professional costs.

Each figure reports the overall increases in hospital/physician costs on the left side for each rate filing year from 2022 to 2024. The right side includes similar information for prescription drugs. Within each category and year, the unit cost increases are identified in the lower portion of each bar and the utilization increases are reported in the upper portion of each bar. For example, the United Healthcare Small Group 2024 rate filing reported a hospital/physician unit cost increase of 3.7 percent and a hospital/physician utilization-driven cost increase of 4.6 percent, for a total increases of over 8 percent. The 2024 prescription drug reported unit cost increase of 4.0 percent, and the prescription drug utilization-driven cost increase was 6.3 percent, resulting in an overall increase in prescription drug costs of over 10 percent.

Observations:

- For the Medical Care category, which includes hospital, physician, and other services (excluding pharmacy), utilization changes (increases in the use of services per member) is often as large (or nearly as large) a driver of cost increases as changes in unit costs.

- For the Medical Care category, increases in unit costs are generally lower than overall inflation in the Puget Sound area for the corresponding year.

- Unit cost increases for the Pharmacy category typically exceed unit cost increases for the Medical Care category.

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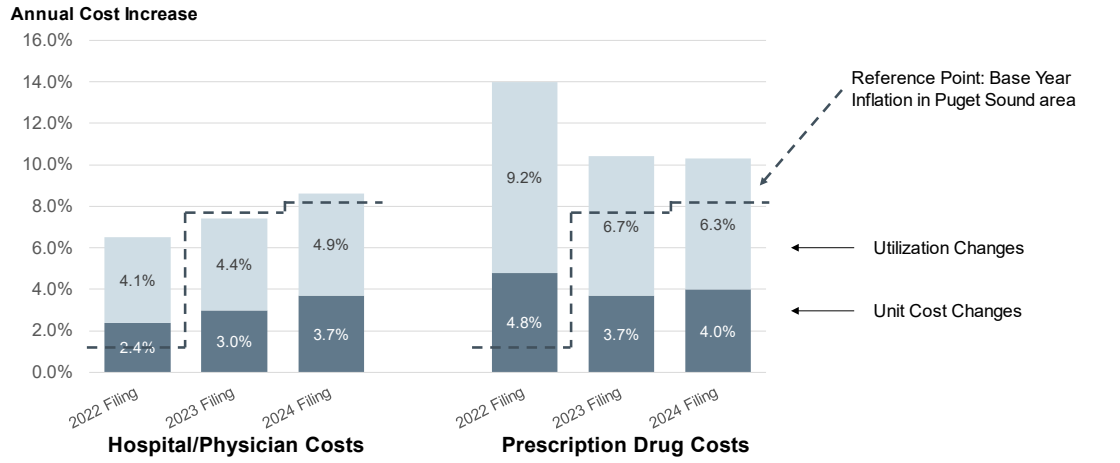
Cost Increases Included in United's OIC Small Group Rate Filings



Source: United Healthcare Insurance Company OIC Rate Filings, Actuarial Memorandum, 2022 – 2024.
Note: Base year inflation is defined as the 12 -month % change in the CPI for all Urban Consumers in the Seattle -Tacoma-Bellevue WA MSA, as of December two years prior to the filing year.

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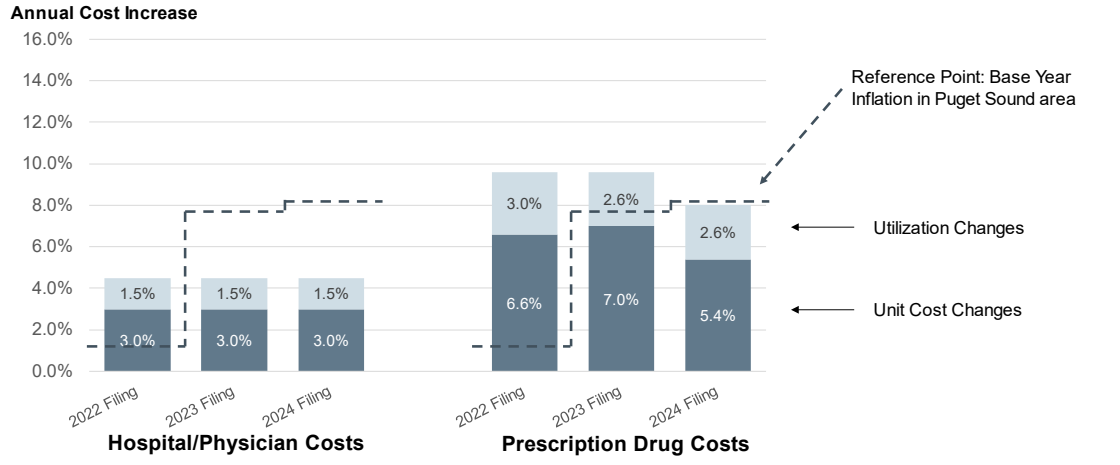
Cost Increases Included in Aetna's OIC Small Group Rate Filings



Source: Aetna OIC Rate Filings, Actuarial Memorandum, 2022 – 2024.
Note: Base year inflation is defined as the 12 -month % change in the CPI for all Urban Consumers in the Seattle -Tacoma-Bellevue WA MSA, as of December two years prior to the filing year.

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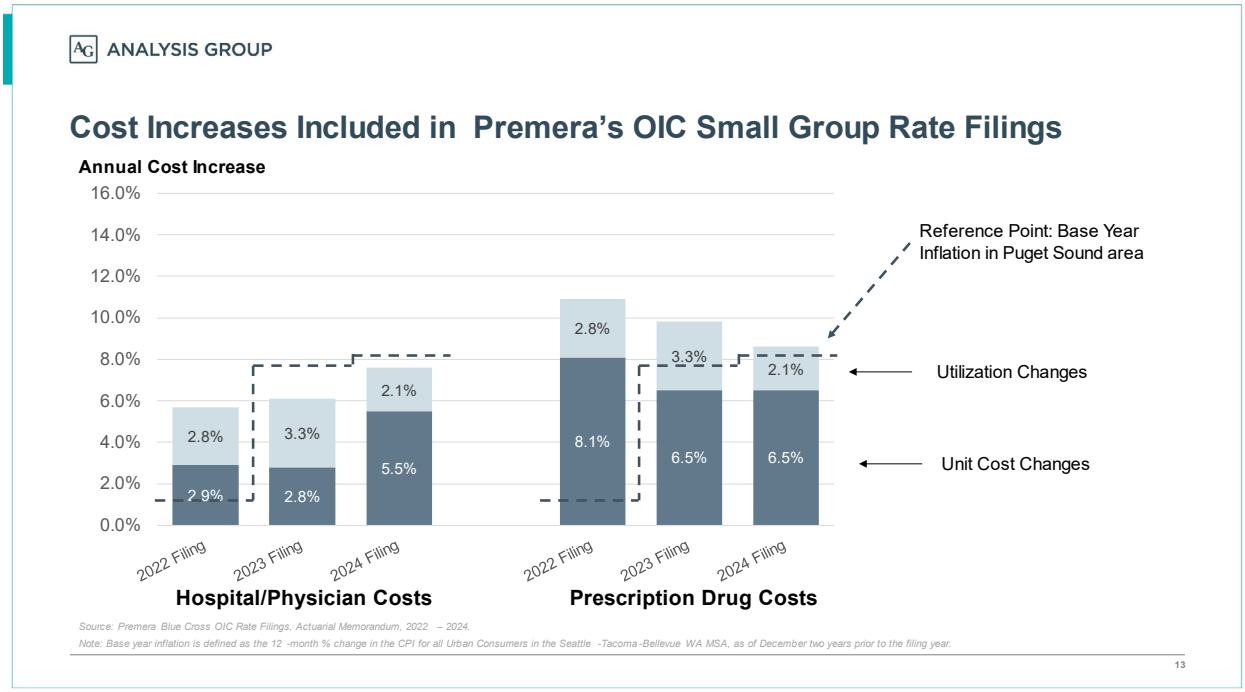

Analysis 2: Hospital Per Unit Cost Increases vs. Other Factors Contributing to Overall Premium Increases

The second analysis focuses on what the overall rate increase would have been if the only change in health plan costs had been the increase in hospital unit costs. This is then compared to the overall approved premium increases in order to illustrate the extent to which hospital unit price changes compare to all other factors. As an illustration, if hospital costs were 40 percent of a health plan's costs and hospital unit costs were reported to have increased by 4 percent, then hospital unit costs alone would result in an overall premium increase of 1.6 percent (40% of costs x 4% increase). If the overall rate increase were 8 percent, then all other factors would account for the remaining 6.4 percentage point increase in rates.

As discussed above, hospital unit cost increases are not separately reported under the Medical Care category. In order to estimate the hospital-specific unit price increase, Analysis Group used the reported overall unit cost increase for the category, the share of the category due to hospital costs, and national estimates of the unit cost increase for physician services. This results in an estimate of the unit cost increase for hospital services.

Observations:

- Hospital unit cost increases are generally a small portion of the overall rate increase for the health plans.

- For all of the plan/year combinations, hospital unit cost increases alone would have resulted in overall health plan rate increases ranging from less than one percent to a maximum of 4.3 percent.

- Hospital unit costs for 2024 were generally a larger component of overall premium increases compared to the smaller increases that were reported for 2022 and 2023. This would be consistent with an understanding of the contracting dynamics occurring during the Covid-19 emergency, where relatively few contracts were renegotiated by health insurers. Because health insurer contracts with hospitals are typically for multi-year periods, the increases for 2024 may reflect larger rate increases as a result of low increases for prior years, as well as expected increases to the costs of providing care going forward, such as increases labor costs.

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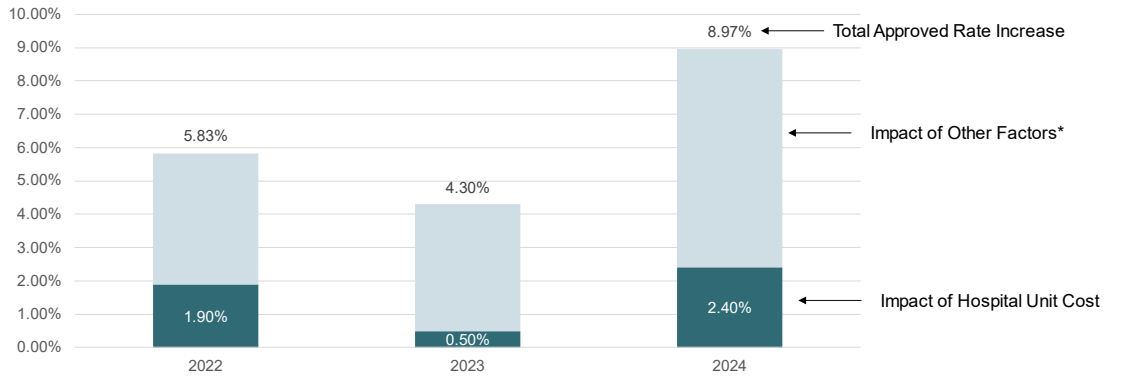
Approved Rate Increases: Impact of Hospital Unit Cost Changes and Other Factors

United Healthcare Small Group Plans



Note: Requested rate increases were 5.83% in 2022, 6.75% in 2023, and 8.97% in 2024.

* Other factors include the impact of changes in hospital utilization, physician and other outpatient unit prices and utiliza tion, member demographics, cost sharing, risk adjustment payments, administrative costs and profit expectations

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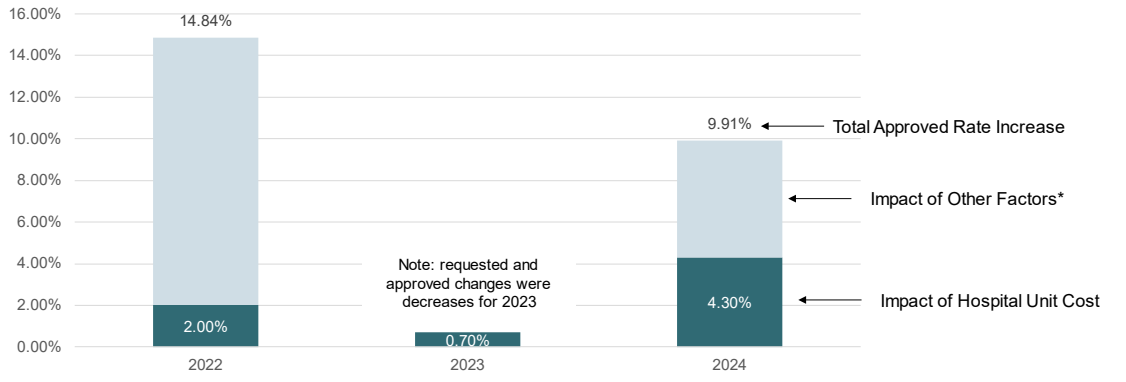
Approved Rate Increases: Impact of Hospital Unit Cost Changes and Other Factors

Aetna Small Group Plans



Note: Requested rate increases were 8.99% in 2022 and 7.43% in 2024. The overall rate increase was negative in 2023.

* Other factors include the impact of changes in hospital utilization, physician and other outpatient unit prices and utiliza tion, member demographics, cost sharing, risk adjustment payments, administrative costs and profit expectations

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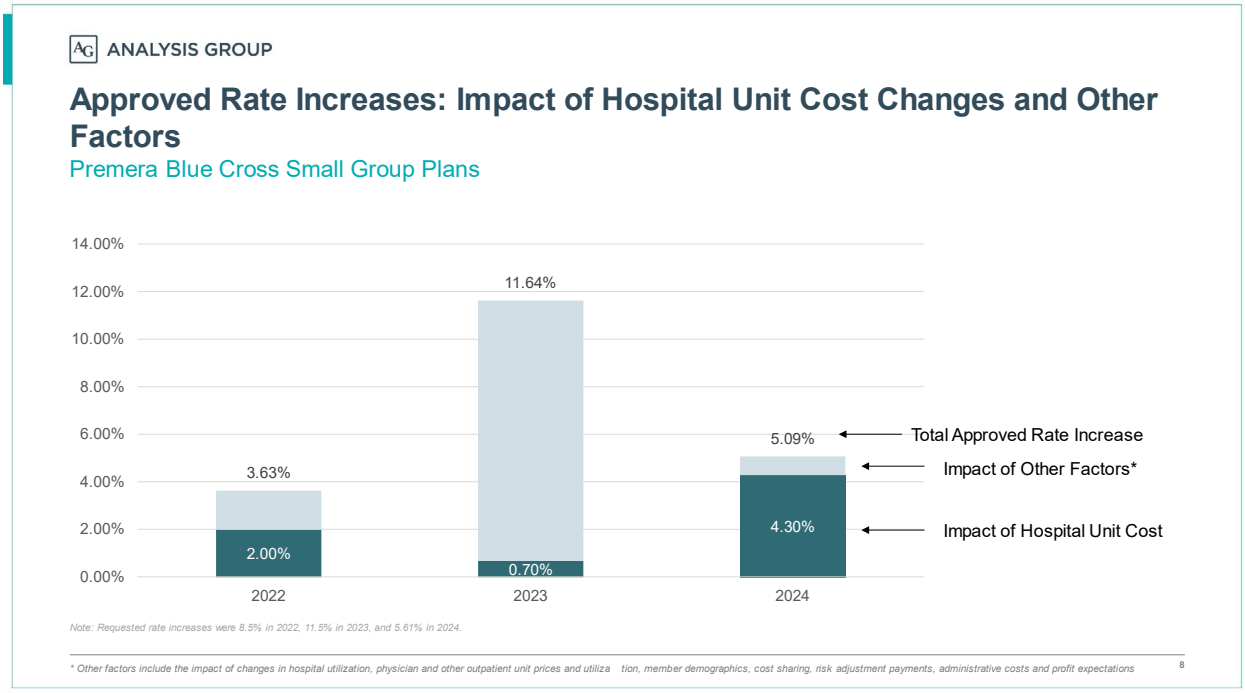

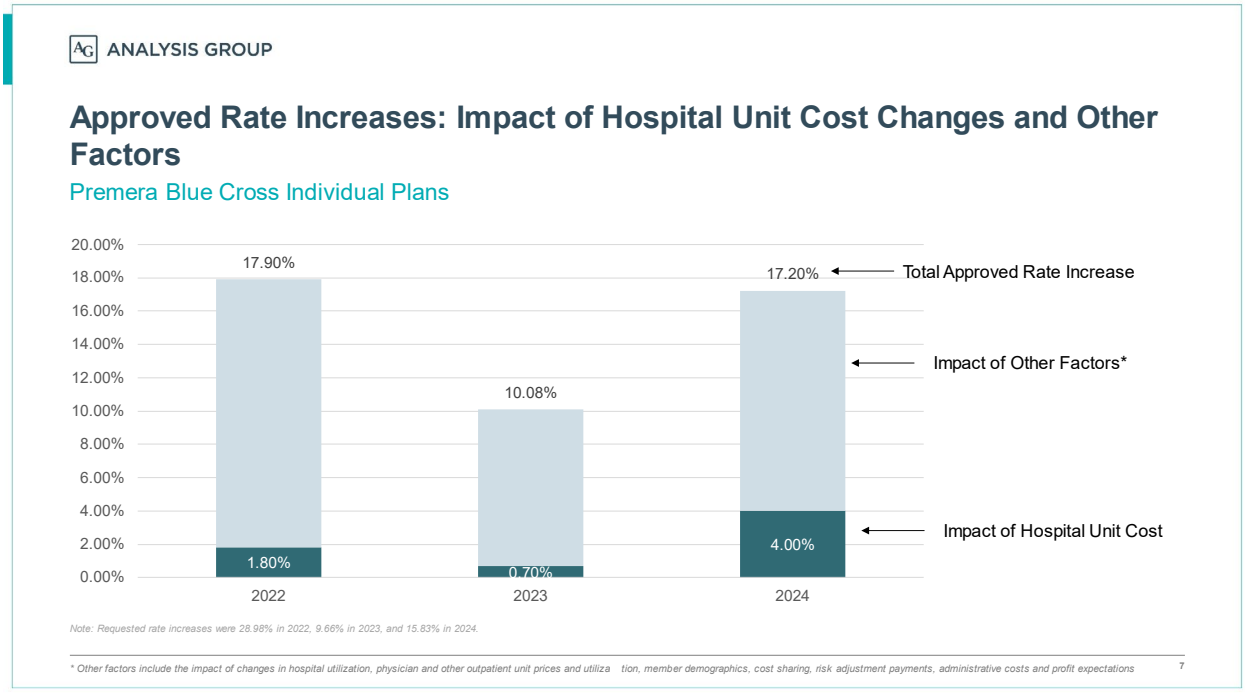

Analysis 3: Hospital Costs as a Share of Reported Overall Healthcare Costs (Premera Multi-Year Analysis)

The third analysis uses a longer data series as reported by Premera, dating back to 2014. This analysis provides a historical view of how hospital costs as a share of overall healthcare costs have changed for Premera over more than a decade.

The data are presented annually as a share of total healthcare costs, such that the total will always equal 100 percent. For example, in 2014 Premera reported that inpatient hospital services represented over a quarter of their total healthcare costs, with outpatient costs (primarily hospital

outpatient costs) representing another 25 percent. The remaining approximately 50 percent of costs were divided among physician/professional costs, other medical costs, and prescription drug costs.

By reviewing changes over time, one can observe overall changes in the categories of spending. While spending within each category will change as a result of the combination of unit cost changes and utilization changes, it is useful to understand the extent to which hospital costs have—or have not—become a larger share of overall spending.

Observations:

- Inpatient and outpatient spending as reported by Premera has declined over time, from approximately 51 percent of all healthcare spending in 2014 to approximately 45 percent in 2024.

- Inpatient spending has declined substantially, with outpatient spending increasing. This is consistent with an overall shift in healthcare from expensive inpatient settings to outpatient settings over time.