June 21, 2024

Mark Ghaly, MD
Chair, Health Care Affordability Board
1215 O St.
Sacramento, CA 95814

Subject: **Comments Following the May 2024 Health Care Affordability Meeting**
(Submitted via Email to Megan Brubaker)

Dear Dr. Ghaly:

Californians rely on hospitals for lifesaving care in their time of greatest need. California's hospitals recognize that accessible, affordable care is out of reach for too many patients and stand ready to work with the Office of Health Care Affordability (OHCA) and other stakeholders to transform our health care system into one that best serves patients. On behalf of more than 400 hospital and health system members, the California Hospital Association (CHA) appreciates the opportunity to comment on the May Health Care Affordability Board meeting.

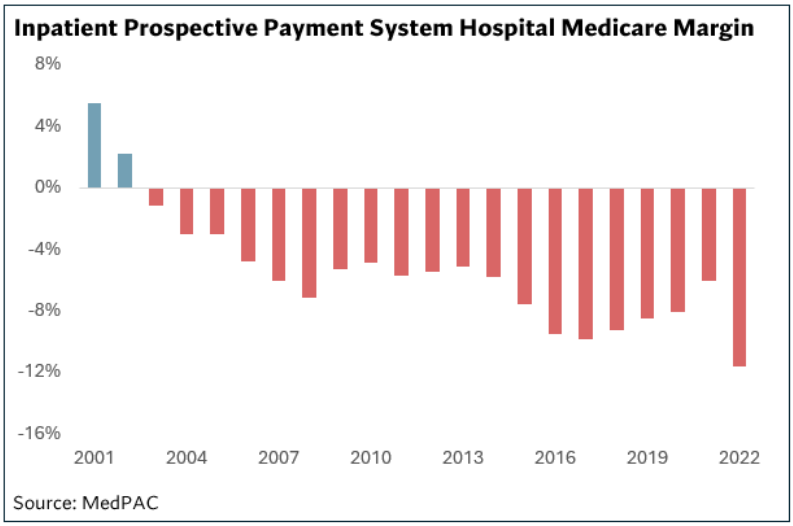
New Research and Developments Should Inform OHCA's Approach

National Projections Place Health Care Spending Growth Ahead of the Spending Target. This month, actuaries at the Centers for Medicare & Medicaid Services (CMS) released updated national health expenditure (NHE) projections, which provide a fresh look at recent health care spending trends and an updated outlook for expected expenditures over the next decade.[1] The updated data underscore the divergence between OHCA's spending target of 3% to 3.5% over the next five years and what economic and demographic fundamentals indicate will be the likely pace of future health care spending growth. Nationally, federal actuaries and forecasters expect per capita health care spending to grow by between 4.8% and 5.8% while California's approved statewide spending target is in place — meaning statewide health care spending, if comparable to national trends (which historically has been the case), is likely to be more than 50% higher than the state spending target. In addition to revealing the gap between

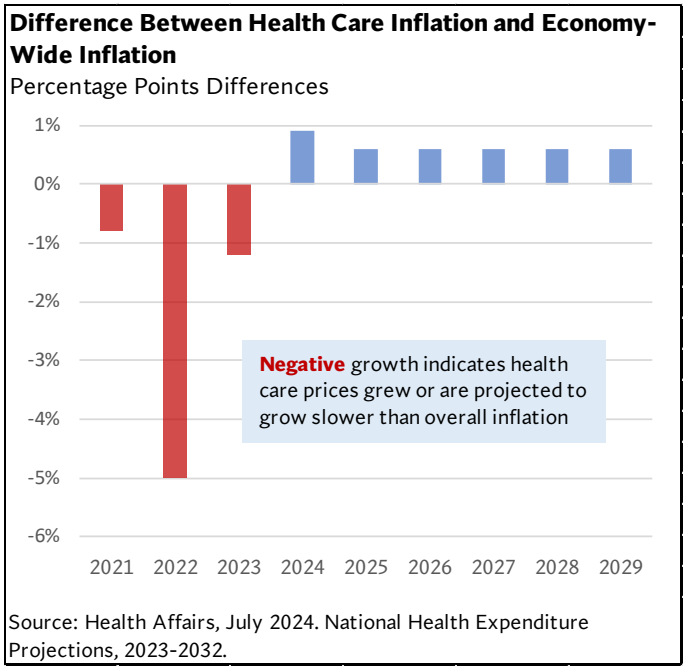
[1] Fiore, J. et al. (2024) National Health Expenditure Projections, 2023–32: Payer Trends Diverge As Pandemic-Related Policies Fade. Health Affairs. https://www.healthaffairs.org/doi/pdf/10.1377/hlthaff.2024.00469

projected trends and the state's goals, the CMS projections discuss the drivers of health care spending both over the past several years and as anticipated in the next decade.

- **Aging and Higher Demand for Care.** Demographic changes are a major factor behind CMS' updated projections, finding that population aging will drive increased demand for care and shifts in coverage from private health insurance to Medicare. Between 2024 and 2032, CMS projects Medicare enrollment to grow by 17%, Medicaid enrollment to grow by 5%, and private coverage to drop by 2%. The shift from private to public coverage, combined with the yawning disparity between private and public payment levels, will severely test hospitals and other providers, forcing them to increase capacity while simultaneously planning for enormous drops in reimbursement. As the figure above shows, Medicare inpatient reimbursement last came in above cost in 2002, and since has declined to more than 12% less than cost in 2022. The shortfall of Medicare payments is even more severe in California, where hospitals only receive 73 cents for every dollar of care they provide to Medicare patients.



- **Price Growth to Make Up for Recent Revenue Shortfalls.** Updated CMS data for 2021 through 2023 show that health care prices grew much slower than prices in the broader economy. Most notably, in 2022, general price inflation was 7.1% while that for health care services came in at just 2.3%. Despite low growth in patient revenues over the last three years, health care input costs grew closer to (if not in excess of) overall inflation, creating a growing financial imbalance between health care providers' revenues and costs. As the figure on the left shows, CMS expects this imbalance to correct over the next decade, with health care prices growing moderately faster than overall inflation.



CMS' choice of health care inflation measures cannot be ignored. First, unlike the most well-known inflation measure — the consumer price index — the health

care inflation measure used by CMS includes all payers, not just private plans and the uninsured. By including all payers, CMS avoids painting an overstated and misleading picture of health care inflation, as has been done by other researchers (and previously shared by OHCA). Despite these advantages, CMS' figures still likely overstate health care inflation given the well-documented deficiencies in appropriately adjusting for quality improvements for medical care broadly[2] and hospital care specifically.[3] These quality improvements, stemming from the introduction and dissemination of new technologies, advances in best safety practices, and improved screening and diagnosis, mean that the extra dollars spent on health care are buying more and more health improvements every year. By failing to appropriately capture these improvements, CMS' and other measures of health care inflation fail to properly reflect the value of the health care patients receive. Going forward, OHCA should carefully consider the tradeoffs and shortcomings of different measures of inflation when assessing health care spending growth.

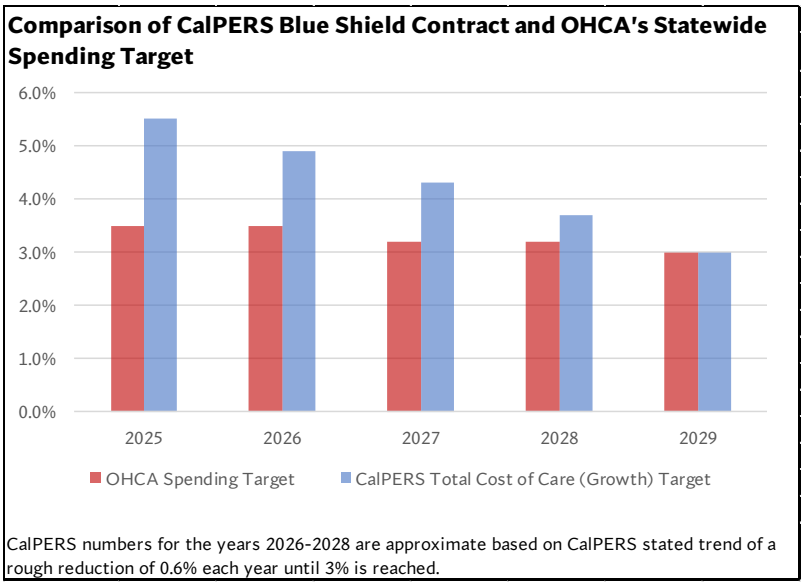
- **Stable Shares of Spending by Major Category of Service.** CMS expects the share of total spending going to hospitals, physicians and clinics, and prescription drugs to remain relatively stable due to similar growth rates for each category of service.
- **Increased Share of Gross Domestic Product (GDP) Going to Health Care.** CMS projects health care spending to grow faster than economic growth, resulting in the share of GDP going to health care growing from 17.3% to 19.7% by 2032. This is attributable to the aging population, increased demand for health care as incomes rise, and price increases to close the gap that rose during the pandemic between general price inflation and health care price inflation (discussed above).
- **Anticipated Coverage Losses Will Reduce Spending.** CMS anticipates a 2 percentage point increase in the percent of the population that is uninsured, largely due to the continuous coverage requirement in Medicaid and the scheduled expiration of enhanced federal subsidies for individual market coverage. These coverage reductions are expected to temper future health care spending increases, but for the wrong reason — families without coverage will be less likely to seek timely, preventive health care services. California must work to avoid this outcome, which would temporarily reduce spending at the expense of Californians' long-term health. This would only add to the affordability crisis as sicker patients seek acute care services that could have been avoided.

What Lessons Can Be Drawn from Recent CalPERS Contract? Earlier this month, CalPERS announced a new contract with Blue Shield of California starting in 2025 aimed at improving affordability, quality, and equity for state employees and retirees enrolled in the insurer's preferred provider organization plan. Specifically, the contract:

- Sets a total cost of care growth target starting at 5.5% in 2025 and ramping down to 3% in 2029
- Places $464 million at risk if the insurer does not meet the contract's affordability and quality goals
- Adds a new partnership with Included Health, a provider of virtual care and navigation services

[2] Dunn, A., Hall, A. and Dauda, S. (2022), Are Medical Care Prices Still Declining? A Re-Examination Based on Cost-Effectiveness Studies. Econometrica, 90: 859-886. https://doi.org/10.3982/ECTA17635
[3] Matsumoto, B. (2021), Producing Quality Adjusted Hospital Price Indexes. U.S. Bureau of Labor Statistics, Working Paper. https://www.bls.gov/osmr/research-papers/2021/pdf/ec210090.pdf

The new CalPERS contract presents a great opportunity to learn how the state and its selected vendor aim to realize OHCA's goals. Accordingly, the OHCA board should dedicate time to learning more about the new CalPERS contract, including:



- How the cost growth targets were set and how Blue Shield expects to meet the ambitious targets
- How improved care coordination is expected to improve health outcomes
- The details of the at-risk payments
- The exclusion of pharmacy costs from the target
- The treatment of high-cost outliers
- Other interesting facets of CalPERS' innovative approach to contracting

While exploring the contract design on its own will be illuminating, the OHCA board should monitor performance over the full life of the contract to draw lessons about how OHCA — and the health care field at large — can best achieve our shared affordability goals.

Alternative Payment Model (APM) Goals Are Bold and Will Require Ongoing Monitoring

OHCA is currently considering standards for promoting the adoption of APMs, with a goal of more closely tying payment methodologies to quality outcomes. While the goals behind this effort are worthy, OHCA should continue to consider how its APM adoption goals fit alongside its other activities and monitor for unintended consequences. Such factors and questions to consider include:

- To what extent is California ahead of other states in the adoption of APMs? How would this affect the state's ability to realize additional savings from the spread of APMs?
- How might providers' capacities to adopt APMs differ? (Small providers, for example, often lack the scale and financial wherewithal to implement risk-based payments.)
- How might OHCA's rules related to market oversight impair providers' efforts to improve clinical integration? What impact would this chilling effect have on the state's ability to meet its APM goals?
- Would patients seek to avoid health insurance products that extensively incorporate APMs, if the plans limit patients' choice of providers and/or ability to obtain the care they need?

Conclusion

OHCA must plan for the health care system Californians need and deserve. The state must address affordability challenges while meaningfully and measurably improving access to high-quality, equitable, and innovative care. As work toward that multi-faceted goal progresses, California's hospitals are eager to help the OHCA board more fully understand the ever-changing health care landscape. We are grateful for the opportunity to comment and look forward to continued collaboration on this important work.

Sincerely,

Ben Johnson
Vice President, Policy

cc: Elizabeth Landsberg, Director, Department of Health Care Access and Information
Vishaal Pegany, Deputy Director, Office of Health Care Affordability
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Dr. Sandra Hernández
Dr. Richard Kronick
Ian Lewis
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