

Government Pays Growing Share Of Health Costs

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WASHINGTON -- As pressure grows for the government to pick up more of the nation's health-care tab, new data show its contribution is already at 45% and is expected to approach 50% within 10 years.

The government's widening role in financing health care stems from the recent expansion of Medicare to include prescription drugs, the growth of relatively new initiatives like the State Children's Health Insurance Program, increased spending by enrollees in programs like Medicaid -- which covers many of the sickest patients -- and cutbacks in employer-sponsored health coverage.

Overall, health spending in the U.S. is expected to double to \$4.1 trillion by 2016, consuming 20% of the nation's gross domestic product, up from the current 16%, according to a new federal study. By then, the study predicts, the government will be paying 48.7% of the nation's health-care bill, up from 38% in 1970 and 40% in 1990.

The stark projections come amid increasing ferment over health care in the states and Washington. They could bolster the argument of some analysts that the U.S. is creeping toward a single-payer system in a disorganized, piecemeal way. Under such a system, the government essentially pays for health care and covers the cost by collecting taxes and premiums.

In any case, the changing landscape has already prompted some insurers to rethink their growth strategies, at least in the short term, focusing more on the government end of the market.

"We are moving incrementally away from traditional sources of insurance, such as employer-based coverage, to a system comprising more federal and state government-provided health care," said the study's authors, who work for the agency that runs Medicare, the federal health program for the elderly and disabled. Their projections are being published today in the journal *Health Affairs*.

Health care has moved to the fore of public debate recently, as several states have followed Massachusetts's lead in fashioning plans to cover uninsured residents through a combination of subsidies and new state pools designed to make it easier for individuals to buy insurance. In Washington, meanwhile, lawmakers across the political spectrum are discussing the importance of expanding coverage for children, and many Democratic lawmakers, as well as diverse coalitions of businesses, insurers and health-care advocates, are talking up the need for universal coverage.

But there are sharp differences about how to get to universal coverage, and especially how to pay for it.

Some advocates of a free-market approach warn that the U.S. is nearing a tipping point in the debate between publicly financed and privately financed health care, and urge the White House to press its market-friendly approach now -- before the 2008 elections. They fear a new Democratic president might press for more government-centered solutions.

Indeed, Democratic presidential contenders have pledged to make helping the uninsured a focal point of their campaigns.

Medicare's drug benefit, introduced in January 2006, increased the program's share of the nation's prescription-drug spending to 22% last year from 2% in 2005. The drug benefit, though subsidized by the federal government, is offered through private insurers. Those private plans come in two types: stand-alone prescription-drug plans, which supplement traditional Medicare, and managed-care plans called Medicare Advantage, which cover other benefits as well as drugs.

Humana Inc., one of the biggest providers of the new drug benefit, has made no bones about becoming more government-focused. In the run-up to the drug benefit's launch, Chief Executive Michael McCallister declared that Humana would "get very heavily weighted toward the government space in terms of earnings over the next couple of years."

Humana threw itself into the new market by manning its own kiosks in Wal-Mart stores across the country, hiring an army of sales agents and contracting with State Farm Insurance Co. to help sell the drug plans. By the end of last year, 4.5 million Medicare beneficiaries were getting their drug benefits through Humana. That includes one million people who signed up for Humana's Medicare Advantage plans, which are even more profitable for the company.

Earlier this month, Humana said its heavy bet on Medicare helped its fourth-quarter net income more than double to \$155 million. Its pretax profit from government business alone more than tripled.

Robert Berenson, senior fellow at the Urban Institute's health-care center, said the projected rise in health spending in coming years means that the government should organize various parties -- including public and private payers, employers, workers, providers and consumers -- to discuss ways to curb costs and reform the system.

"We need some kind of comprehensive approach to control costs" that goes beyond merely shifting costs among the payers, Dr. Berenson said. Among the reform options he said should be discussed are a single-payer, government-run system; an expansion of Medicare to cover younger people, starting with 55- to 64-year-olds; and new limits on the use of high-tech medical equipment.

Joseph Antos, a health analyst at the American Enterprise Institute, a conservative think tank, said the new pressures facing the government "translate into a big political question: Can we continue on with the program the way it is now, given continuing demand by the baby-boomer generation?" With Medicare covering more people, the current public-private health system will

eventually be primarily a public-health system, and "at some point Medicare will be the largest system," Mr. Antos said.

A lot of "volatility" underlies the overall growth rate in health-care spending, including shifts in whether public or private sources are paying the bills, said John Poisal, who wrote the report with colleagues at the Office of the Actuary at the federal Centers for Medicare and Medicaid Services.

"We will continue to face tough questions about how we finance our health care bill," he said. Americans' out-of-pocket spending is expected to grow to \$440.8 billion by 2016 from \$250.6 billion last year.

According to the study's projections, Medicare spending grew by 22% to \$418 billion in 2006, up from \$342 billion in 2005. The study said the growth would slow to 6.5% this year, due to scheduled cuts in payments to physicians and smaller payment increases to Medicare Advantage plans. But because Congress has already reversed the cuts in physician payments for this year, the actual growth rate will likely be higher. The authors also assume that by 2016, 32% of those eligible will be enrolled in Medicare Advantage plans, up from 13.5% in 2005.

Federal and state spending on Medicaid last year was estimated at \$313.5 billion, roughly the same as in 2005. Medicare now provides drug benefits for low-income Medicaid enrollees, resulting in a 36% decrease in Medicaid drug spending in 2006. Medicaid spending in several other areas, such as hospitals and physicians, is also expected to grow at a slower pace, because of slower enrollment and state cost-cutting. But spending on some categories will grow sharply. The growth rate for home health spending, for example, was an estimated 20% for 2006, compared with 14% in 2005.

Meanwhile, spending growth by private insurance was estimated to have slowed from a peak of 9.5% in 2001 to a low of 4.7% in 2006.

With little overall growth in commercial or private health insurance, other insurers have sought to tap the market for government-financed health care. That strategy has driven some of **UnitedHealth Group Inc.**'s biggest deals in recent years.

In 2002, UnitedHealth bought AmeriChoice Corp., a big Medicaid plan provider, for \$560 million, to become one of the biggest players in that market. In 2005, it purchased PacifiCare Health Systems Inc., one of the biggest Medicare players, for \$8.1 billion just ahead of the launch of the new drug benefit. It also campaigned hard to win a deal to sell AARP-branded drug plans. UnitedHealth currently has 5.74 million Medicare drug-plan members, more than any other insurer.

Drug companies also have profited from the drug benefit. In the first seven months of 2006, prescriptions funded by Medicare drug plans accounted for nearly 9% of medicines bought in retail pharmacies, according to Verispan LLC, a Yardley, Pa., firm that collects prescription data.

One of the biggest winners was **Bristol-Myers Squibb Co.** Nearly 14% of U.S. retail prescriptions for its drugs, particularly the popular blood thinner Plavix, were financed by the Medicare drug benefit during that period, according to Verispan. Medicare-funded prescriptions

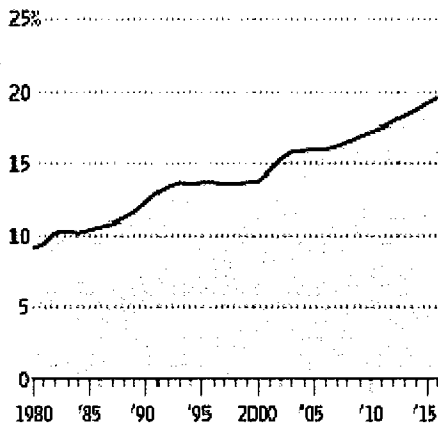
accounted for more than 10% of AstraZeneca PLC's and Merck & Co.'s retail prescriptions as well.

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Intensive Increases

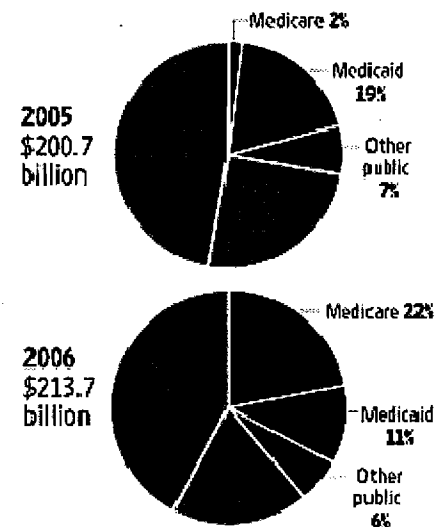
U.S. health-care spending is expected to double in the next decade to \$4.1 trillion, or nearly 20% of the general economy. The Medicare drug benefit introduced in 2006 changed the distribution of drug spending among payers.

National health spending as a percentage of GDP



Source: Centers for Medicare and Medicaid Services

Prescription-drug spending by payer



MEDICAL BILL

- **The Background:** U.S. health-care spending is expected to double to \$4 trillion in a decade, consuming a growing share of the economy.
- **What's at Stake:** How the government, private payers and consumers divvy up the rising health-care bills.
- **The Bottom Line:** Amid debate on paying for health care, the government already is taking a larger and larger share.