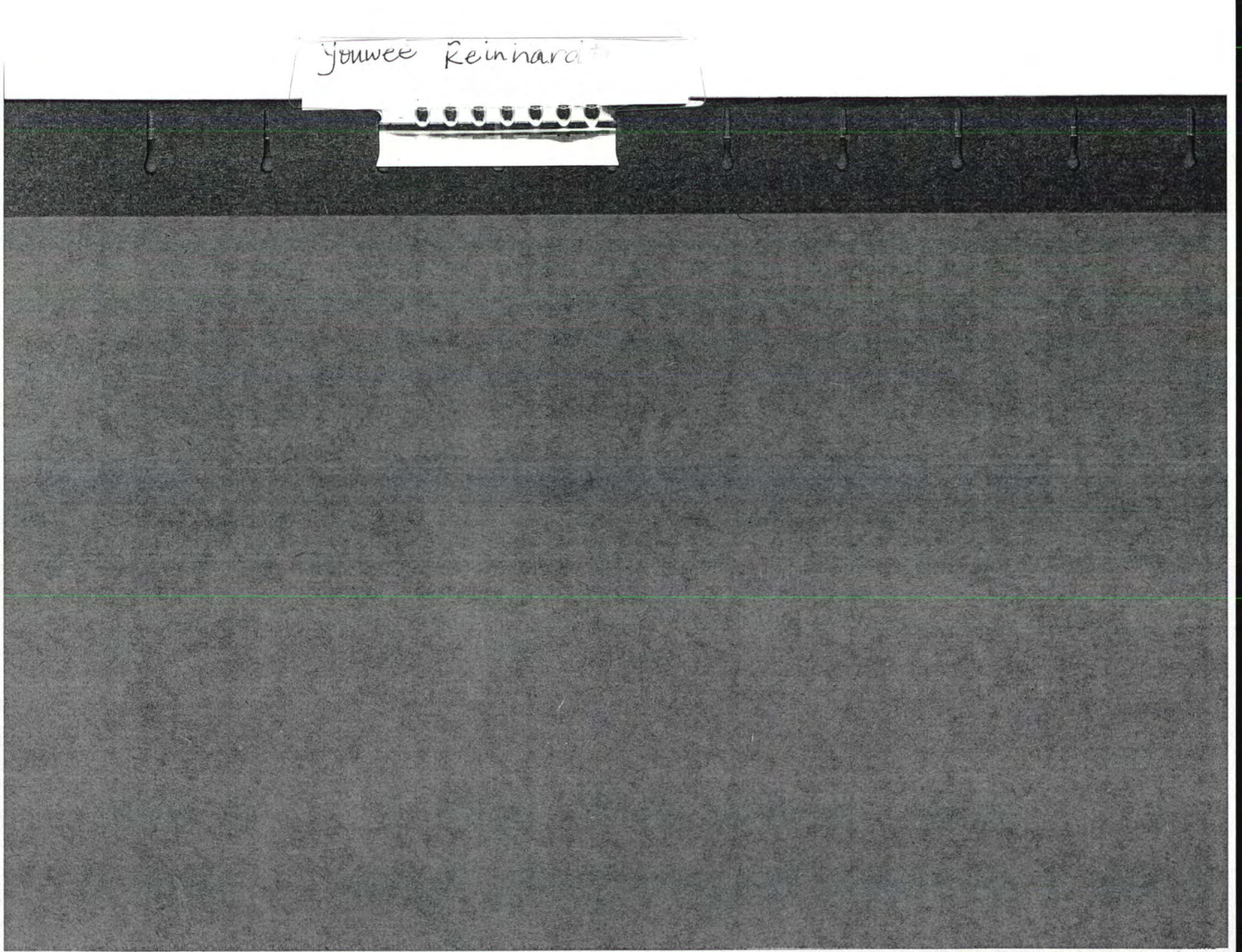
Jouwee Reinhardt

An after-dinner talk.

from Uwe Reinhardt

dear Uwe
Rhinehardt
heath care

# For a Fistful of Dollars:

## Health Reform through Bounty Hunting

starring

Youwee Reinhardt

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Clint Eastwood

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Clint
Eastwood

# FOR A FISTFUL OF DOLLARS:
# Health Reform through Bounty Hunting

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## SUMMARY OF PRESENTATION

There are but two ways to control a nation's spending on health care: (1) government controls on prices and utilization, or (2) raw competition on the basis of insurance premiums and the prices charged by doctors, hospitals and other providers of care. As our recent debate on health reform has shown, Americans are unwilling to countenance the first approach. That leaves only the second alternative: an approach best called "private-sector bounty hunting."

In this emerging wild-west scenario, doctors, hospitals and the manufacturers of health products play the role of "economic outlaws." Their raids on the treasuries of private employers during the 1980s so outraged these major payers for health care that they sought help from a rough bunch of "bounty hunters"--the executives of the burgeoning HMO industry. The employers give the "bounty hunters" a flat annual capitation per insured employee, along with the license to go after the "economic outlaws" in any which way they can, as long as the employees remain satisfied with the health care received through this process. The government's *Medicare* and *Medicaid* programs are now beginning to switch to this system as well.

The "bounty hunters" carry a two-barreled shotgun into this "hunt." One barrel consists of the large pools of insured that the "bounty hunters" amass through their marketing blitzes. Merely by threatening to divert parts of these pools from individual doctors, hospitals and health manufacturers, the "bounty hunters" can extract huge price concessions from these frightened providers. The second barrel consists of the vast computer systems by which the "bounty hunters" monitor and control the doctors and hospitals within their territory (i.e., within their networks). With swift frontier justice, the "bounty hunters" drive from their territory any provider whose statistical practice profile is deemed wanting on clinical or economic grounds.

To be sure, along with the handsome "bounty" earned by the "hunters," their massive advertising campaigns and their micro-management of health care do eat up sizeable chunks of the capitation premiums they collect from business and government (up to 30%). But those chunks are not a new burden on premium payers; they are carved out of the incomes of the providers of health care. The premiums paid by business and government, which rose at double-digit rates in the 1980s, have now been stabilized, and many are even decreasing. From the payers' perspective, then, competition evidently *has* been productive, at least so far.

That the "hunted" see it differently is not surprising. Nor should these latterday "desperados" be surprised, however, that they now find themselves backed into the health-sector's O.K. Corral. By opposing any other form of cost control for so long, they literally invited these private-sector "bounty hunters" onto their turf, did they not?

Alas, some innocent bystanders will be hit in this shoot-out, for the private-sector "bounty hunters" are unlikely to absorb the famous "cost shift" by which charitable doctors and hospitals have hitherto been able to finance catastrophic health insurance for the nation's uninsured simply through higher prices to private payers. But the demise of that hidden tax system will help flush the chronic problem of the uninsured into the open, where it can no longer be ignored, thus forcing our politicians to confront it more forthrightly than they have in the past.

## First a Riddle for Health Policy Wonks:

What do ...

Saddam Hussein,

the AMA,

the Ph. RMA and

the HIMA

have in common?

(For the answer, stay to the end.)

# Health Reform through Bounty Hunting

I. A Brief History of U.S. Health Reform

A. President Johnson and the Blue-Eyed U.C.R. Wonders

B. President Nixon and the Happy Price Fixers

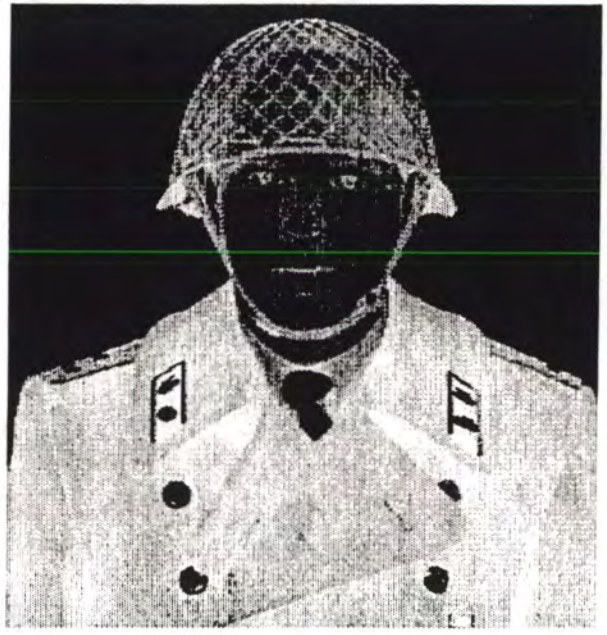
C. President Ford and the Toothless-Tiger Planners

D. President Carter and the "Voluntary Effort"

E. President Reagan and the Grim Apparatchiks

# Reagan Health-Care Apparatchiks

## Enforcing Centrally-Administered Prices for the Medicare Program



**It is a supreme irony that it was President Reagan, of all people, who introduced centrally (federally) administered prices into American health care. I am referring here to the flat fees per medical case (per *"diagnostically-related group"* or "*DRG*") that, since 1983, have been set unilaterally by the Federal government for its Medicare program and applied to virtually *all* hospitals in the United States. Usually, one finds such centrally administered-price regimes only in purely socialized health systems, such as England's or those of the former socialist nations.**

**This seemingly odd circumstance is but one more illustration of what may be called the "China Syndrome" in health care: Just as only a Republican president could have afforded politically to open a dialogue with Communist China in the late 1960s, so can only Republicans afford politically to impose certain regulatory strictures (such as price controls or spending caps) on all or parts of the American health system.**

## Health-Care Bounty Hunter:

C.E.O. of Apex Health Plan (AHP), Inc.

Highly efficient and a smart marketer, U.S. Healthcare is a Wall Street darling. But what happens as politicians and bureaucrats intrude on the health care system?

# Abramson to Clinton: Thanks, but no thanks

By Robert Lenzner

THE NEW YORK metropolitan area is being inundated with television commercials featuring the signature songs of show business stars like Gene Kelly and Louis Armstrong. What are they peddling? Health care for as little as $2 a doctor's visit.

Welcome to the new era, where medical care is marketed like soap or cars by Philadelphia-based U.S. Healthcare, Inc., one of the largest health maintenance organizations (HMOs). Sign up with U.S. Healthcare, print ads promise, and you'll get such freebies as free cancer screenings, 100%-covered X rays and lab tests, and emergency coverage anywhere in the world.

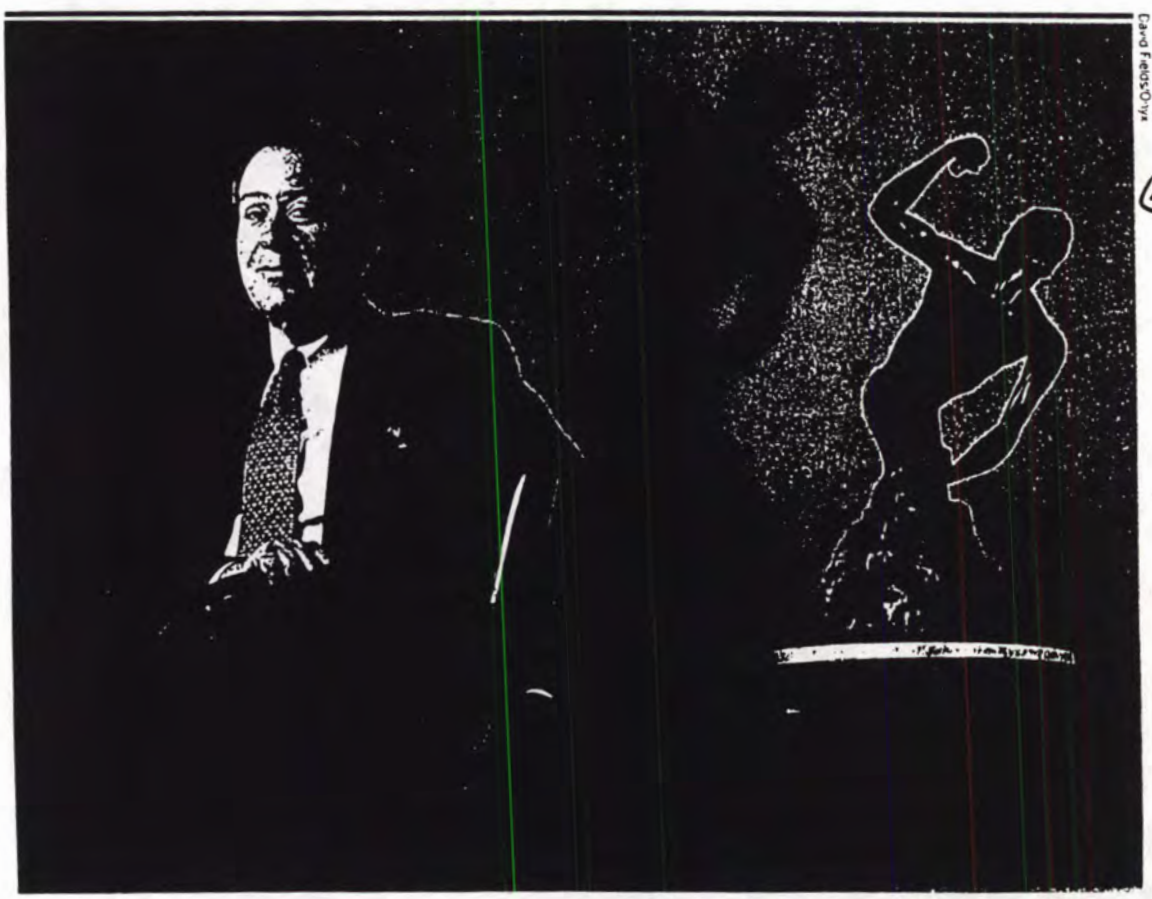
With smart marketing, low prices and efficient delivery, U.S. Healthcare's profits over the past five years have zoomed from $3.6 million to over $200 million, on revenues of $2.2 billion.

U.S. Healthcare's unusually rich margin of profit stems from its ability to negotiate tough deals with doctors and hospitals and other providers. With average per-person monthly premiums of $138.86, U.S. Healthcare runs medical care costs per insured of only $99.55, giving it a ratio of medical costs to premiums of just 72%. Compare that with about 77% for Oxford Health Plans or 85% for Cigna HealthCare.

All of which would seem to guarantee U.S. Healthcare a profitable position no matter what political compromise emerges from the Clinton White House's grandiose plans. But that doesn't mean that Leonard Abramson, U.S. Healthcare's chief executive officer, is happy about the idea.

Abramson feels that the plan Hillary Clinton presented will "open up legitimate enterprises to political influence." The health alliances the Clintons are looking to create mean too many political appointees and too much bureaucracy, he says: "This is a perverse socialism."

Under the Clinton plan, the regional health alliances would collect



Leonard Abramson, chief executive officer **We only need HMOs, not the "perverse socialism" of Clinton health alliances.**

the premiums from employers and patients, and then pay the money over to U.S. Healthcare. Right now, U.S. Healthcare has no interference at all as the middleman that collects the premiums from patients and pays the doctors.

Abramson's argument—self-serving, of course, but reasonable—is that the nation has all the health care reform it needs in the Health Maintenance Organization Act of 1973, under which U.S. Healthcare and many other for-profit and not-for-profit organizations operate.

U.S. Healthcare, he points out, avidly pursues capitation, the concept of prepaying doctors and other providers a predictable monthly stipend for each member patient enrolled with them. In U.S. Healthcare's case each doctor in the system has about 300 to 1,000 patients.

A typical primary care doctor enrolled in U.S. Healthcare as a participating provider can count on earning $125,000 to $175,000 a year. For this he or she must take on a heavy patient load but needn't worry about where the money for the next malpractice insurance premium payment is coming from. U.S. Healthcare has also reduced medical specialist prices by 10% to 15%. It has cut hospital utilization by 10% to 20%, by decreasing length of stays and doing away with what it believes are unnecessary treatments such as some cesarean sections.

Part of its cost-cutting methodology derives from well-organized programs of preventive medicine. U.S. Healthcare provides high-risk pregnant women with early access to expert prenatal care. This helps reduce the risk of premature, low-birth-weight babies.

U.S. Healthcare tries to identify potential breast cancer at an early stage by urging that every woman member reaching the age of 40 go for a free mammogram. By catching the appearance of irregular growths early on, U.S. Healthcare believes that it avoids having to pay for more complicated and costly surgical procedures later on.

The HMO also uses the drawing power of its member base to pressure hospitals into lowering the cost of complicated medical procedures. Liver transplants, which ordinarily cost around $500,000, are contracted for at rates of between $135,000 and $375,000.

Because of its hard-nosed approach to the medical profession, U.S. Healthcare isn't always popular with it. Medical professionals express concern that the quality of services may suffer where cutting costs has the highest priority. Kathleen Galvin-Flack, vice president for managed care at Presbyterian Hospital, says U.S. Healthcare is "the most controversial HMO" in New York. She objects to the way U.S. Healthcare does business: She says it often refuses to pay enough to simply cover the cost of hospital services. "They're extremely unresponsive," Galvin-Flack says. "They say, 'This is our fee schedule. Take it or leave it. Otherwise, we will take our patients over to New York Hospital.' "

Does this hard line on costs lead to corner-cutting? David Cohen, chief aide to Philadelphia Mayor Edward Rendell, says: "There have been literally no complaints" about U.S. Healthcare's handling of about 3,500 municipal employees. Cohen says that budgeted medical health costs for the city of Philadelphia have fallen from $167 million in fiscal 1992 to $136.5 million in fiscal 1993.

For all its impressive marketing and financial skills, U.S. Healthcare still faces tough competition. In Philadelphia, U.S. Healthcare's main market, Keystone Health Plan East is biting into U.S. Healthcare's market share. "Our membership growth is three times theirs over the past 2½ years. That is because of our hospital network, the connection with Blue Cross and the ability to offer employers national coverage," says John Daddis, Keystone's chief operating officer.

U.S. Healthcare is going to face some intense competition from other HMOs as well. Oxford Health Plans, another fast-growing publicly owned HMO, is promoting a more flexible but costlier plan that includes the option of using doctors outside the Oxford network.

And there are insurance giants, desperately trying to shift their high-cost indemnity medical plans to cheaper HMOs. Cigna, for example, guided by former U.S. Healthcare senior executive Dr. Michael Stocker, is making the transition from an insurance provider to a powerful HMO company.

To make life even more complicated for outfits like U.S. Healthcare, New York State insurance regulators are trying to keep a lid on U.S. Healthcare's freedom to raise premiums, according to David Simon, U.S. Healthcare senior vice president and

Costas Nicolaides, chief financial officer (left); David Simon, principal legal officer

**Widening margins between medical costs and member premiums equals a hot stock.**

**Now Back to our Riddle for Health Policy Wonks:**

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What do ...

Saddam Hussein,

the AMA,

the Ph. RMA and

the HIMA

have in common?

## Answer to our Riddle

They always aim their guns
in the wrong direction.

They're shooting away at Hillary Clinton,
all the while being taken to the cleaners
by savvy private-sector Bounty Hunters.

**MAZEL TOV!**

**(Chinese for "Congratulation")**

## Concluding Observation:

It is common knowledge that

1. Germans are the most humorless people on earth

2. Economics is the most dismal science on earth

**Proposition:**

The behavior of the American health system is such that, even when a German-born economist describes that system, it comes across as funnier than hell.