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WHAT IS DRIVING PRICE VARIATION IN PRIVATE HEALTH INSURANCE?

Why This Study Is Important

Considerable prior work has examined geographic variation in Medicare spending, but much less is known about spending variation for people with private health insurance. This study uses extensive claims data from three large private insurers to provide a national picture of private-sector spending and pricing variation and to delve into the reasons for this variation.

What This Study Found

- Risk-adjusted spending per privately insured beneficiary varies by a factor of more than three across hospital referral regions, driven almost equally by variation in quantity and variation in prices.
- Private insurers' prices for specific services vary substantially across markets, across hospitals within markets and even within hospitals. Variation in how much different private insurers pay the same hospital for the same procedure suggests the relative bargaining power of insurers and hospitals plays a role in price determination.
- Hospital and insurer market structures are significantly associated with price variation. Overall prices are 12 percent higher for monopoly hospitals than for hospitals with four or more competitors. Conversely, a ten-percentage-point increase in the collective market share of the study insurers was associated with 7 percent lower hospital prices in the market.
- Market structure is also associated with the type of contracts negotiated between hospitals and insurers. Monopoly hospitals are more likely to obtain contracts that expose them to less financial risk or that reimburse at more lucrative rates. Hospitals facing greater insurer concentration are more likely to receive prospective reimbursement tied to Medicare rates.
- Hospital prices increased after mergers, with the largest increases seen for merging facilities in closer proximity. Merging hospitals within 5 miles of one another experienced post-merger price increases of 6 percent; no significant price increases were observed for merging facilities located more than 25 miles apart.

What These Findings Mean

The significant variation in prices observed across and within markets suggests that policies aimed at steering privately insured patients to lower-priced providers could reduce health care spending. At the same time, having hospitals bear more risk for the costs of the care they provide could help to improve production efficiency. Hospitals with greater market power relative to insurers would be better able to resist these efforts. Policymakers need to continue to monitor hospital market power and seek to protect against hospital mergers that could harm consumer welfare.

More About This Study

The data used for this study include the amounts actually paid to hospitals and unique hospital identifiers, permitting analysis of price variation within and across hospitals and markets as well as characterization of the contract mechanisms each insurer used to reimburse each hospital. Price measures included an overall case-mix-adjusted price index for each hospital and hospital- and contract-level prices for seven specific services. The unique hospital identifiers were used to link the claims with other hospital- and market-level data, characterize market structure and identify hospital mergers over time. Cross-sectional regressions examined the relationship between prices and contract arrangements and hospital and insurer market structures. Difference-in-difference analyses examined changes in hospital prices after a merger, relative to price trends at non-merging hospitals.

Cooper Z, Craig, SV, Gaynor M, and Van Reenen J. "The Price Ain't Right? Hospital Prices and Health Spending on the Privately Insured." *Quarterly Journal of Economics*, published online September 4, 2018.

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