Commentary on Gross and Laugesen

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In 2003, several of us wrote a paper titled "It's the Prices, Stupid: Why the United States Is So Different from Other Countries" (Anderson et al. 2003). The paper compared the "real" resources used to deliver health care in the United States with those in other industrialized countries and found that the United States had fewer hospital beds, nurses, and physicians per capita than most other industrialized countries. We concluded the higher spending must be attributable to the higher prices in the United States.

The article by Tal Gross and Miriam J. Laugesen in this special issue examines many of the explanations that have been offered to explain why United States has higher prices than the other countries. With the possible exception of rent-seeking behavior (discussed below), the authors are correct that these are not viable explanations. This raises the question, what other factors could explain the higher prices in the United States?

Private insurers pay substantially higher prices for hospital, physician, and pharmaceutical services than public insurers. In some localities the difference is 20 percent, and in others it is over 100 percent; the national average is close to 50 percent (MedPAC 2017). The important question is, why are private insurers willing to pay such higher prices for similar goods and services?

One commonly offered explanation is cost shifting. However, this argument does not hold up under further scrutiny. Hospitals and physicians will spend all the money they are given, and it is the amount of revenue that determines their costs. So if the private sector pays 50 percent more than the public sector, and the public and private sectors each provide half of

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the revenues, then the costs will be 25 percentage points higher than what the public sector pays and 25 percentage points lower than what the private sector pays. There is no exogenous determination of cost—cost is a function of revenue.

The question becomes, Why is the private sector willing to pay these higher prices? It is unlikely that they are willingly subsidizing the public sector. One possibility is conflict of interest. Many corporations also provide health care services, so while they want to control spending for their employee benefits, they do not want to control spending for the health products they provide. A look at the Fortune 50 shows that many of them have a role in providing health services.

Another possibility is that no single company has the market power to lower health care prices in their community. Berkshire Hathaway, J. P. Morgan Chase, and Amazon recently announced an effort to control health spending. However, none of them alone has sufficient market power in its community to push down prices to public-sector levels. For large employers, health insurers are paid administrative services fees only, so they do not have a reason to control prices.

If the United States is going to be able to lower health care prices, it needs to start with corporations working collaboratively to control prices. A single corporation or even three powerful companies cannot lower prices alone. Surprisingly, price has not been a priority for corporate America. Corporations are concerned about the price of the widgets they buy, but not the prices they pay for health care. Consortia of corporations such as Pacific Business Group on Health and National Business Group on Health have focused more on reducing volumes and waste or enhancing value rather than lowering prices.

Another possibility is government action. In the 1970s, many states had all payer rate-setting programs because private insurers supported them as a way to control prices. These programs went out of favor with the advent of Medicare Prospective Payment system (Anderson 1991). Given the apparent inability of corporations to control health care prices, perhaps a second look at all-payer rate setting is appropriate. It has worked in Maryland since the early 1970s, and hospitals in Maryland have good bond ratings and quality of care (Murray 2009). Because of the way the Medicare waiver is structured, the rate of increase is based on the level of increase in Medicare spending, so there is no incentive to lower prices more than necessary to meet the target.

As the article by Gross and Laugesen suggests, rent seeking is a very difficult challenge. The hospitals, physicians, nursing homes, and pharmaceutical

companies are effective in arguing for high prices. The important question is, what entity is focused on lowering prices? It is hard to identify a political/economic entity that has made high price its priority. If the United States is going to lower health spending by lowering prices, it will be necessary to have a champion. Because of the price differential, it needs to be the corporations that are paying the high prices.

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