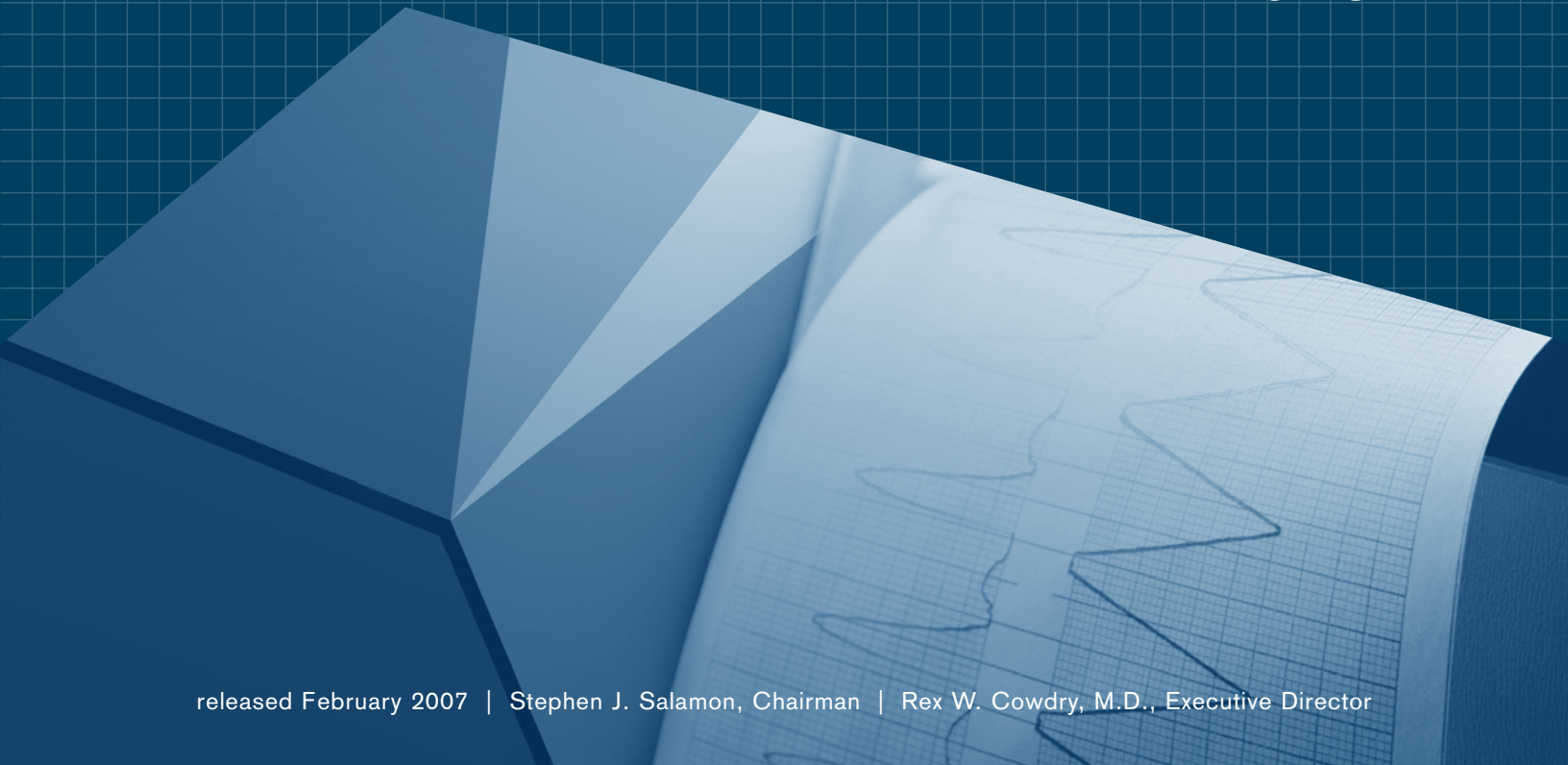
MARYLAND HEALTH CARE COMMISSION

experience from 2005

STATEHEALTHCARE EXPENDITURES



released February 2007 | Stephen J. Salamon, Chairman | Rex W. Cowdry, M.D., Executive Director

MARYLAND HEALTH CARE COMMISSION

Each year the Maryland Health Care Commission reports on the state's expenditures for health care services in accordance with Maryland law. Our goal is to provide reliable information about trends in health care expenditures to help inform health policy deliberations among health policy experts, health care professionals, executives, and legislators.

Maryland health care spending grew to $30.2 billion in 2005. The rate of overall growth in health care spending was 7 percent from 2004 to 2005, slightly below the trend from 2001 to 2005, which averaged 8 percent per year.

Per capita expenditures for health care in Maryland ($5,387) continue to be about 7 percent less than national per capita spending. From 2004 to 2005, per capita health care spending grew 6 percent, compared to the longer-term trend of 7 percent per year since 2001. The rate of growth in health care spending continues to surpass various measures of growth in the broader economy. For example, personal per capita income in Maryland increased at an average annual rate of only 4 percent from 2001 to 2005.

This marks the third consecutive year of slowing growth in health care spending, but consumers and purchasers have yet to see much relief from rising health care premiums. Premium increases have made the affordability of health insurance a challenge for more Maryland families and contributed to a rise in the number of uninsured Marylanders. The Maryland Health Care Commission recently reported that 780,000 nonelderly Marylanders lacked insurance coverage during 2004-2005, representing 16 percent of the nonelderly population, up from 13 percent in 2000-2001.

This is an exciting time in health care policy. States, payers, providers, and purchasers are crafting creative strategies to improve health care quality, to insure the uninsured, and to control health care costs. The Commission's mission is to provide reliable information and trustworthy analysis to help this process.

The report would not have been possible without the cooperation of other state agencies, the federal government, and private organizations that provided information. The Commission is grateful to these organizations for working closely with Commission staff to complete this study in time for the 2007 Session of the Maryland General Assembly.

Rex W. Cowdry, M.D.
Executive Director

MARYLAND HEALTH CARE COMMISSION

experience from 2005

STATEHEALTHCARE EXPENDITURES

released February 2007 | Stephen J. Salamon, Chairman | Rex W. Cowdry, M.D., Executive Director

CONTENTS

FIGURES AND TABLES

ACKNOWLEDGMENTS

THIS REPORT REQUIRED THE ASSISTANCE OF MANY INDIVIDUALS AND OFFICES IN STATE GOVERNMENT, PRIVATE INDUSTRY, AND FEDERAL GOVERNMENT. In particular, the Maryland Health Care Commission (MHCC) wishes to note special contributions from the following individuals and organizations. Tricia Roddy and Patricia Holcomb, Office of Planning, Development and Finance, Maryland Department of Health and Mental Hygiene (DHMH); Jeffrey Gruel, Office of Operations, Eligibility and Pharmacy, DHMH; and Babi Lamba, Center for Health Program Development and Management, University of Maryland-Baltimore County, provided Medicaid expenditure and enrollment information. Jim Johnson and Hank Fitzer, Budget Management Office, DHMH, and Walter Wirsching, Maryland Department of Corrections, supplied information on government spending, while Estelle Apelberg, Vital Statistics, DHMH, provided population statistics.

In constructing spending accounts of this complexity, the MHCC relied on estimates of private insurance expenditures supplied by Calvert Gorman of the Maryland Insurance Administration. As in previous years, Maribel Franey and Cheryl Sample at the Centers for Medicare & Medicaid Services (CMS) assisted MHCC with the data use agreements that are necessary before Medicare information can be released. Leroy McKnight in the federal government's Office of Personnel Management supplied information on federal employees' insurance coverage. Richard D. Barnett (TRICARE Management Activity) provided spending information on CHAMPUS/TRICARE programs, and Pat Kane at the Department of Veterans Affairs provided similar spending data on VA programs. Anne Martin of the Office of the Actuary at CMS provided estimates of expenditures for nontraditional Medicare programs. Charlotte Thompson of the Health Services Cost Review Commission provided estimates of hospital spending. Information from the Agency for Healthcare Research and Quality (AHRQ) Medical Expenditure Panel Survey (MEPS) was used in the estimation of private insurance allocations. Karen Beauregard, John Sommers, and Ray Kuntz at AHRQ provided advice on the use of the MEPS data files.

The development of the state health care expenditure analysis would not have been possible without the significant contributions of our consultants. This project was under the direction of Dr. Deborah Chollet, Mathematica Policy Research (MPR), Thomas Bell of Social & Scientific Systems, Inc. (SSS), and Sophie Nemirovsky of SSS. Dr. Eric Schone of MPR developed the estimation algorithms for private sector spending using the MEPS data, and Dr. Dean Farley of Ingenix/UHC provided quality assurance services for the

methodologies and the final estimates. Adrian Ndikumwami, Cynthia Saiontz-Martinez, Shelley Mullins, Sanee Maphungphong, and Po-Lun Chou at SSS provided programming support on the project. Priscilla Thompson and her staff of Solutions Technology, Incorporated, provided data collection and processing support. Beverly Valdez of SSS, with the assistance of Laura Spofford, Kate Bryan, and Joan Holleman, provided the graphic design and editorial services for the report.

SUMMARY

HOW MUCH DID MARYLAND SPEND FOR HEALTH CARE?

Total health care expenditures in Maryland grew 7 percent from 2004 to 2005, more slowly than the trend since 2001. From 2001 to 2005, total health care expenditures growth in Maryland averaged 8 percent per year.

Per capita, health care expenditures in Maryland continue to be less than the national average, although Maryland's expenditure growth has mirrored the national average. From 2004 to 2005, per capita health care expenditures in Maryland grew 6 percent, compared to the longer-term trend of 7 percent per year since 2001.

HOW WERE MARYLAND'S HEALTH CARE DOLLARS SPENT?

Hospital inpatient and outpatient care together represent the largest single category of health care expenditures in Maryland, accounting for more than one-third of total health care expenditures in 2005. Inpatient care accounted for 24 percent of total health care expenditures in 2005; outpatient care (including emergency room visits) accounted for 10 percent. Outpatient hospital care was the fastest growing category of expenditures in Maryland, growing 13 percent from 2004 to 2005.

Physician services and other professional services together comprise the next largest category of health care expenditures in Maryland. These services accounted for nearly 30 percent of total health care expenditures in 2005—16 percent for physician services and 13 percent for other professional services. From 2004 to 2005, expenditures for physician care grew more slowly than any other category of services except nursing home care: just 4 percent.

Three categories of expenditures account for nearly all of the balance of health care expenditures in Maryland: outpatient prescription drugs (14 percent of total expenditures in 2005); nursing home and home health care (12 percent), and the administrative and net cost of insurance (9 percent). Of these, expenditures for prescription drugs, home health care, and the administrative and net cost of insurance grew more rapidly than total spending growth from 2004 to 2005.

EXPENDITURES FOR HOSPITAL CARE Total expenditures for hospital care grew at an average annual rate of about 9 percent from 2001 to 2005—about 1 percent faster than for all health care spending. Over the five-year period, outpatient spending grew at an average annual rate of 10 percent, as fast as expenditures for prescription drugs and faster than all other categories except home health care services (14 percent). From 2004 to 2005, outpatient expenditure growth accelerated to 13 percent while inpatient expenditure growth slowed to 7 percent. Medicare is the single largest payer for hospital care in Maryland, followed by private insurance. Medicare and private insurance together financed 78 percent of the increase in expenditures for inpatient hospital care from 2001 to 2005, and 68 percent of the increase in expenditures for outpatient care. Medicaid's role in financing hospital care also has grown. In Maryland, Medicaid financed 23 percent of the increase in outpatient expenditures from 2001 to 2005 and 18 percent of the increase in inpatient expenditures.

EXPENDITURES FOR PRACTITIONER SERVICES Physician services accounted for more than half of all expenditures for practitioner services in Maryland (55 percent) in 2005. Expenditures for physician care grew at an average annual rate of 7 percent per year from 2001 to 2005, making this one of the slowest growing health care sectors over the five-year period. From 2004 to 2005, growth in expenditures for physician care further slowed to 4 percent.

As with hospital care, private insurance and Medicare are the principal sources of financing for physician services, respectively accounting for 51 percent and 26 percent of total expenditures in 2005. Together, they financed 76 percent of the growth in expenditures for physician care from 2001 to 2005. Medicaid expenditures for physician care also rose significantly, but they remained a relatively small part of total expenditures for physician services—financing 7 percent of total expenditures in 2005.

Consumer out-of-pocket expenditures and private insurance finance most expenditures for other professional services, and together accounted for more than half of the growth in these expenditures from 2001 to 2005.

EXPENDITURES FOR PRESCRIPTION DRUGS Mirroring national trends, the growth in total expenditures for prescription drugs slowed from an average annual increase of 10 percent from 2001 to 2005, to 8 percent from 2004 to 2005 in Maryland. Per capita, Marylanders continued to spend about 6 percent more for prescription drugs than the national average in 2005, generally in line with higher average personal income in the state.

Private insurance is the dominant payer for prescription drugs in Maryland, accounting for 46 percent of all expenditures for prescription drugs in 2005. However, consumers paid 34 percent of prescription drug expenditures out-of-pocket—a proportion that has remained stable since 2001. Since 2001, Medicaid has become a larger purchaser of prescription drugs in Maryland, financing (together with other much smaller state programs) 20 percent of all expenditures for prescription drugs in Maryland in 2005, compared with 17 percent in 2001.

EXPENDITURES FOR LONG-TERM CARE Nursing home care accounted for approximately two-thirds of the total expenditures for long-term care in 2005, while home health care accounted for approximately one-third. However, expenditures for home health care have increased faster, as Medicaid has expanded the use of waiver programs to encourage home and community-based care. From 2001 to 2005, expenditures for home health care increased more rapidly than any other health care category, growing at an annual rate of 14 percent, while nursing home care expenditures increased at an average annual rate of only 7 percent. From 2004 to 2005, the growth in spending for nursing home care dropped to about 4 percent.

Medicaid financed 45 percent of all expenditures for nursing home care and 60 percent of expenditures for home health care in 2005. Medicaid accounted for 35 percent of the increase in nursing home expenditures from 2001 to 2005, and 74 percent of the increase in expenditures for home health care.

Marylanders paid 28 percent of nursing home care expenditures and 18 percent of home health care expenditures out-of-pocket in 2005. Out-of-pocket spending accounted for 33 percent of the increase in expenditures for nursing home care from 2001 to 2005, and 18 percent of the increase in expenditures for home health care.

WHO PAID FOR MARYLAND'S HEALTH CARE?

Private insurance and consumer out-of-pocket payments finance most health care expenditures in Maryland. In 2005, private insurance financed 40 percent of all health care expenditures; 17 percent were paid out-of-pocket. Government programs financed the balance—including Medicare (21 percent), Medicaid (18 percent), and other government programs (4 percent). Taken together, public program expenditures accounted for a slightly larger percentage of all health care expenditures in 2005 (43 percent) than in 2001 (42 percent).

MEDICARE EXPENDITURES From 2004 to 2005, Medicare spending in Maryland increased 8 percent, compared with 9 percent nationally. More than 60 percent of Medicare expenditures in Maryland were associated with inpatient hospital care (48 percent) and outpatient care (13 percent). Hospital care accounted for a larger share of Medicare spending in 2005 (61 percent) than in 2001 (59 percent), while physician care accounted for a smaller share of Medicare expenditures (22 percent in 2001 versus 20 percent in 2005).

MEDICAID EXPENDITURES Between 2001 and 2005, Medicaid spending in Maryland grew faster than the national average—averaging 11 percent per year in Maryland, compared with 9 percent nationally. Nearly one-third of Medicaid expenditures in 2005 were for hospital care—including inpatient care (24 percent) and outpatient care (8 percent). The next largest block of Medicaid expenditures was for long-term care—including both nursing home care (19 percent) and home health care (13 percent). Overall, the percentage of Medicaid expenditures associated with institutional care (inpatient and nursing home care) has declined significantly; these expenditures accounted for 43 percent of Medicaid spending in 2005 compared with 51 percent in 2001.

Expenditures for prescription drugs are a relatively small but accelerating share of Medicaid expenditures (13 percent in 2005). Prescription drugs accounted for 18 percent of the growth in Medicaid spending from

2001 to 2005—just less than the share of expenditure growth associated with inpatient hospital care (20 percent) and home health care (19 percent).

PRIVATE INSURANCE EXPENDITURES Private insurance expenditures in Maryland grew at an average annual rate of 8 percent per year from 2001 to 2005, equal to the average annual growth rate from 2004 to 2005. In contrast, the growth in private insurance expenditures nationally averaged 9 percent per year from 2001 to 2005, but slowed to 7 percent from 2004 to 2005. On a per capita basis, private insurance expenditures in Maryland remained lower than the national average in 2005. Growth in inpatient hospital costs accounted for 25 percent of the growth in private insurance expenditures from 2001 to 2005, followed by growth in expenditures for physician services (19 percent), administration and net cost of insurance (19 percent), prescription drugs (17 percent), and hospital outpatient care (12 percent).

OUT-OF-POCKET EXPENDITURES From 2001 to 2005, out-of-pocket spending in Maryland increased at an average annual rate of 7 percent, compared with the national average of 6 percent. From 2004 to 2005, the growth in out-of-pocket expenditures in Maryland slowed to 6 percent, approximately the national average. Prescription drugs accounted for more than one-third (36 percent) of the increase in Marylanders' out-of-pocket expenditures for health care from 2001 to 2005—far outpacing the increase in out-of-pocket expenditures for any other service type. The increase in expenditures for physician and other professional services together accounted for 28 percent of increased out-of-pocket spending over that period, while increased expenditures for nursing home and home health care accounted for 21 percent. Out-of-pocket spending as a percentage of total spending in 2005 was 17 percent, unchanged from 2001.

OUTLOOK FOR 2007 THROUGH 2009

A third consecutive year of slower growth in total health care spending suggests there may be reason for optimism about future spending growth. However, significant reasons for concern remain. Health care costs remain high, and cost growth still exceeds the growth in wages and personal income—even as worker productivity has increased.

Pressure on upward movement of prices seems particularly strong for hospital and professional services. These sectors account for more than 60 percent of health care spending. While consumers may see continued slowing in prescription drug spending, the slowing trend may be largely attributable to the cycle in new drug applications rather than a moderating of demand.

The emergence of new technologies and the lowering of clinical thresholds for treatment increase both the volume and the cost of care. These drivers probably will remain significant features of the U.S. health care system for the foreseeable future. As they continue to drive the cost of care, they are also driving greater attention to measures that curb or avoid the use of care—including consumer information, cost-sharing, information systems that improve efficiency, the development of protocols for managing high-cost care, and greater attention to maintaining and improving population health.

STATE HEALTH CARE EXPENDITURES

THE MISSION OF THE MARYLAND HEALTH CARE COMMISSION (MHCC) INCLUDES THE DEVELOPMENT OF TIMELY AND ACCURATE INFORMATION FOR POLICYMAKERS, PURCHASERS, PROVIDERS, AND THE PUBLIC, IN ORDER TO PROMOTE INFORMED DECISIONMAKING. This report provides information about total and per capita health care expenditures by Maryland residents in 2005, and the distribution of expenditures by type of service and by source of payment. Expenditures in 2005 are compared with those in 2004, and also in 2001.

This year's report differs from those in previous years in two major ways. First, a longer time series is presented. Expenditures in 2001 as well as in 2004 were reestimated, using consistent methods and measures for the purpose of comparing with 2005 estimates. This longer time series provides greater perspective on changes in health care expenditures that we believe will be helpful to analysts and policymakers in understanding expenditure trends in Maryland. As with all continuing time series, the reestimates reflect both improvements in estimation methods and revisions in the underlying data. As a result, the 2001 and 2004 reestimates may differ from those published in earlier reports and should be regarded as improved estimates.

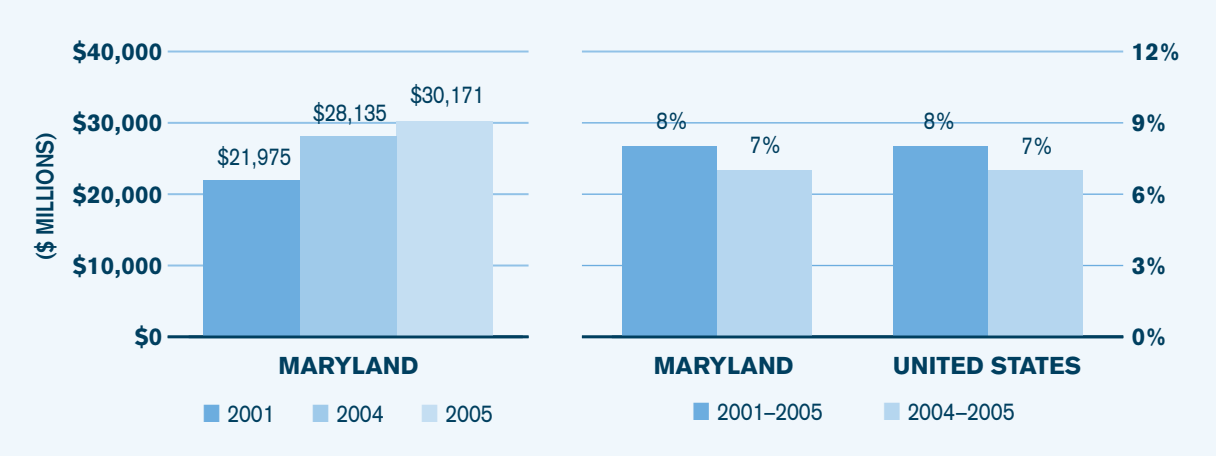
Second, the organization of information presented in the report is new. Estimates are presented separately by service type and by payer, with additional data provided in the body of the report compared to earlier years. The revised organization is intended to allow readers to refer to a single section to obtain information of interest, without needing to scan the entire report. As in past years, the data supporting all graphics are provided at the end of the report in a section of supporting tables. Because additional data are reported in the body of the report, the supporting tables are relatively brief. The methods and data sources for the Maryland and national estimates and the calculation of annual rates of change are described in the Methods section of this report.

HOW MUCH DID MARYLAND SPEND FOR HEALTH CARE?

In 2005, Maryland residents spent $30.2 billion for health care services, compared to $28.1 billion in 2004 and $22.0 billion in 2001 (Figure 1). Health care expenditures grew 7 percent from 2004 to 2005, more

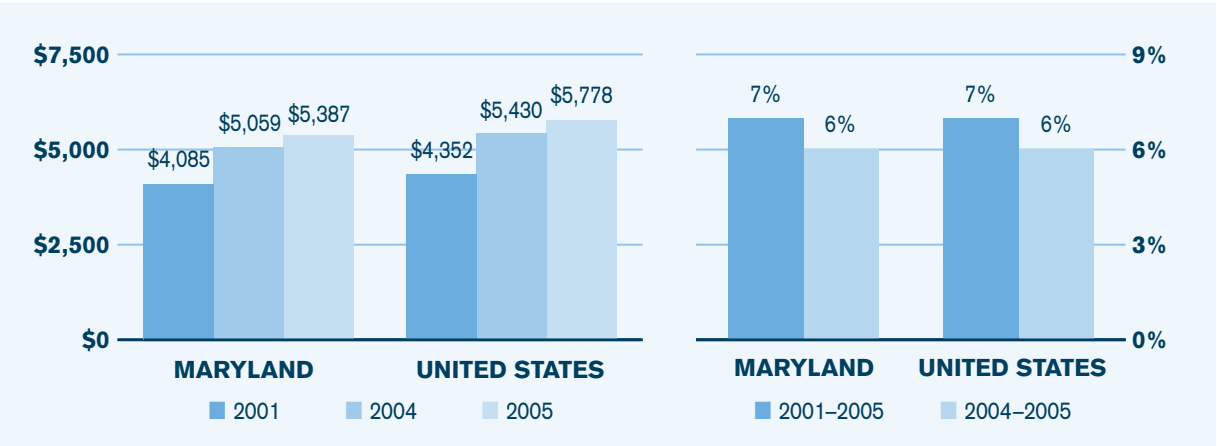
slowly than the trend since 2001. From 2001 to 2005, total health care expenditures growth in Maryland averaged 8 percent per year.

FIGURE 1: Estimated Health Care Expenditures and Rate of Growth



Per resident, health care expenditures in Maryland continue to be less than per capita expenditures nationally, although annual growth in per capita expenditures mirrors the rate of growth in per capita expenditures nationally. (Per capita expenditure growth rates are consistently lower than total expenditure growth rates due to increases in population.) In 2005, Marylanders spent an average of $5,387 per person for health care, about 7 percent less than the national average of $5,778 (Figure 2). From 2004 to 2005, per capita health care expenditures in Maryland grew 6 percent, compared to the longer-term trend of 7 percent per person per year since 2001. These rates of increase in Maryland equaled the national growth in per capita expenditures per year over the same periods.

FIGURE 2: Estimated Per Capita Health Care Expenditures and Rate of Growth, Maryland and U.S.



HOW WERE MARYLAND'S HEALTH CARE DOLLARS SPENT?

Hospital inpatient and outpatient hospital care together represent the largest single category of health care expenditures in Maryland, accounting for more than one-third of total health care expenditures in 2005. Inpatient care accounted for 24 percent of total health care expenditures in 2005; outpatient care (including emergency room visits) accounted for 10 percent of total health care expenditures (Table 1).

TABLE 1: Estimated Health Care Expenditures by Service Category in Maryland

SERVICE CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$21,975**	**100%**	**$28,135**	**100%**	**$30,171**	**100%**
Inpatient	5,268	24	6,863	24	7,364	24
Outpatient	1,998	9	2,634	9	2,973	10
Physician Services	3,771	17	4,730	17	4,917	16
Other Professional Services	3,300	15	3,765	13	3,995	13
Prescription Drugs	2,777	13	3,791	13	4,091	14
Nursing Home Care	1,760	8	2,205	8	2,290	8
Home Health Care	682	3	1,076	4	1,166	4
Other Services	494	2	643	2	662	2
Administration and Net Cost	1,924	9	2,428	9	2,713	9

Physician services and other professional services together comprise the next largest category of health care expenditures in Maryland. Together these services accounted for nearly 30 percent of total expenditures for health care in 2005—16 percent (physician services) and 13 percent (other professional services) of total expenditures, respectively.

Three categories of expenditures account for nearly all of the balance of health care expenditures in Maryland. Expenditures for outpatient prescription drugs accounted for 14 percent of total expenditures in 2005. Expenditures for long-term care services—including nursing home care (8 percent) and home health care (4 percent)—accounted for approximately 12 percent of total expenditures for health care. Finally, administrative cost and the net cost of insurance accounted for 9 percent of total health care expenditures in Maryland.

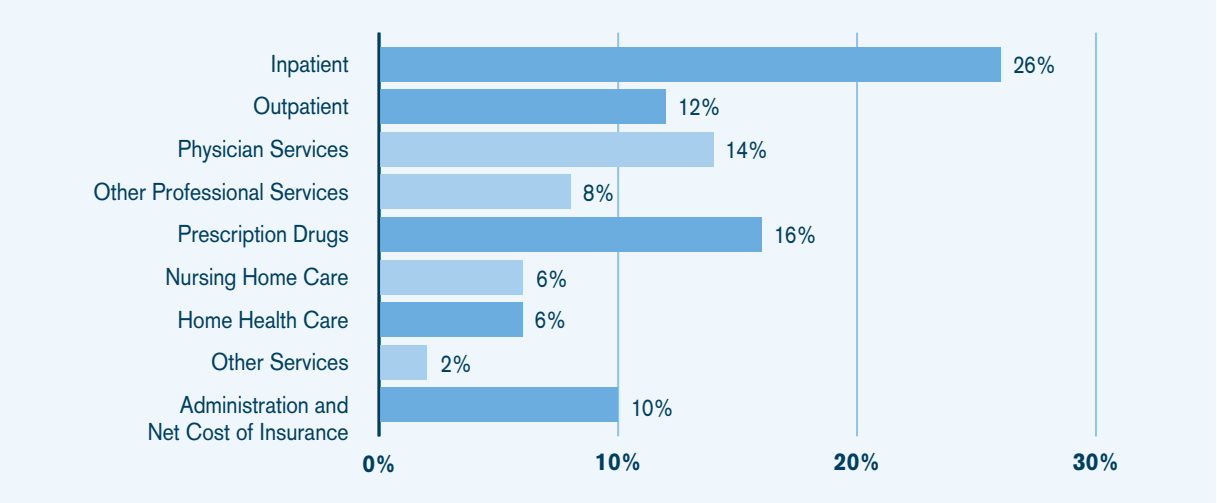
Since 2001, expenditures in three categories—outpatient hospital care, prescription drugs, and home health care—accounted for an increasing percentage of total expenditures in Maryland. Together, they represented a larger percentage of total expenditures in 2005 (28 percent) than in 2001 (25 percent). Conversely, expenditures for physician and other professional services together accounted for a smaller percentage of total expenditures in 2005 (29 percent) than in 2001 (32 percent).

Because inpatient hospital care is the largest single category of expenditures in Maryland, it typically accounts for a large share of the growth in total expenditures. From 2001 to 2005, growth in inpatient hospital care

costs accounted for 26 percent of the growth in total health care expenditures (Figure 3). Similarly, expenditures for physician care—also a large category of health care expenditures in Maryland—accounted for a relatively large share of the growth in spending from 2001 to 2005 (14 percent), although expenditures for physician care represented a slightly smaller percentage of total expenditures in 2005 (16 percent) than it had in 2001 (17 percent). In contrast, relatively fast growth in expenditures for prescription drugs (described later in this report) accounted for 16 percent of the growth in total health care expenditures from 2001 to 2005, and drove growth in the percentage of total expenditures devoted to prescription drugs (from 13 percent to 14 percent) as described above.

In general, private insurers, and to a lesser extent public programs such as Medicare and Medicaid, gauge acceptable levels of expenditures for administration and the net cost of insurance in direct proportion to medical costs paid. Aggregated across all third-party payers for health care in Maryland, these costs accounted for 9 percent of total expenditures in 2001 and 2005, and 10 percent of the growth in total health care expenditures in Maryland over this period.

FIGURE 3: Estimated Share of Increase in Health Care Expenditures by Service Category in Maryland, 2001–2005

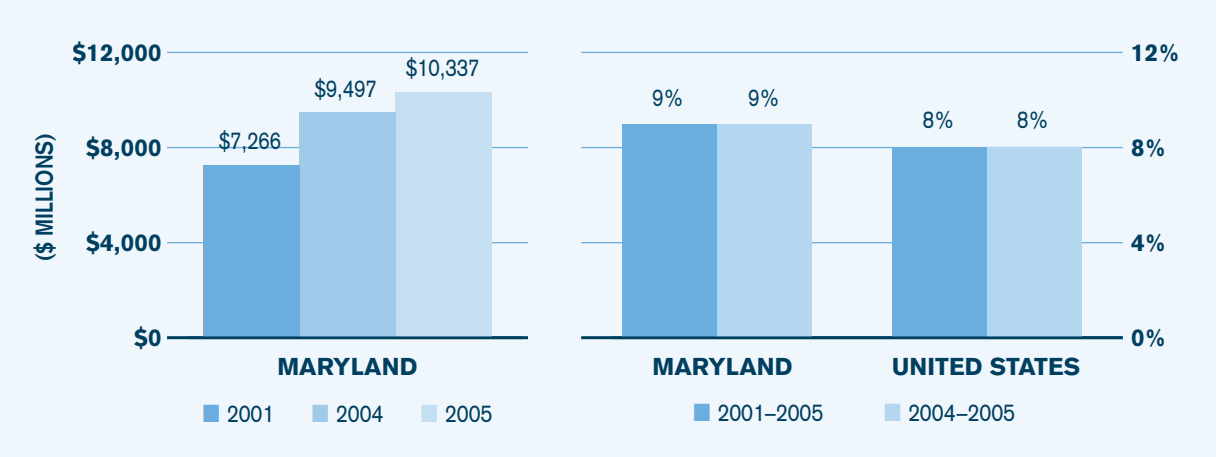


NOTE: Dark shading indicates services that have an increasing share of expenditures in 2005 from 2001. Light shading indicates services that have the same or decreasing share of expenditures in 2005 from 2001. Due to rounding, the increase or decrease in share of expenditures may not be reflected in Table 1 above.

EXPENDITURES FOR HOSPITAL CARE

Including both inpatient and outpatient services, Marylanders spent $10.3 billion for hospital care in 2005 (Figure 4). Total expenditures for hospital care grew at an average annual rate of about 9 percent from 2001 to 2005, continuing at 9 percent growth from 2004 to 2005. Since 2001, the average annual growth in total expenditures for hospital care in Maryland (9 percent) has exceeded the national average by 1 percentage point per year, although inpatient hospital rates in Maryland have risen more slowly than hospital rates nationally.[1]

FIGURE 4: Estimated Hospital Services Expenditures and Rate of Growth

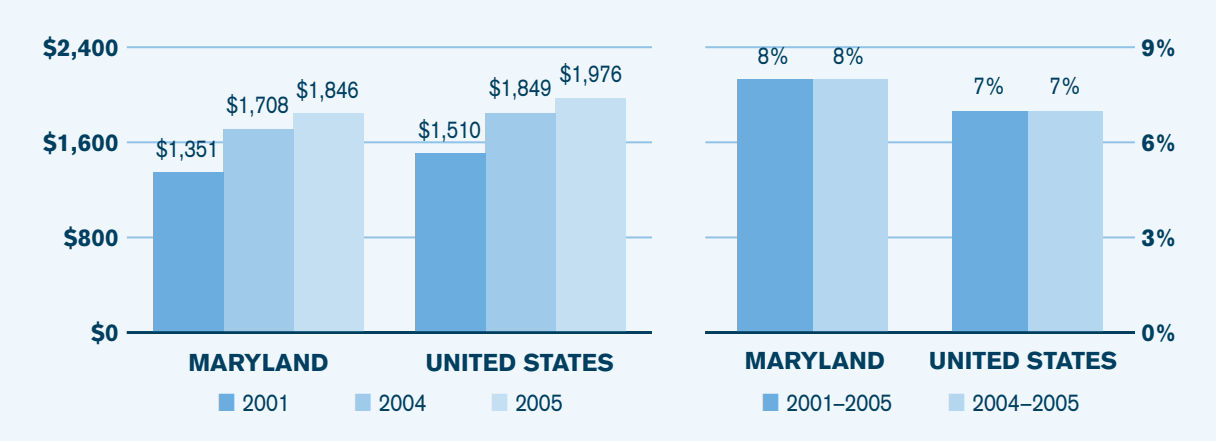


On a per capita basis, Marylanders spend less for hospital care than the national average. In 2005, Marylanders spent an average of $1,846 per person for inpatient and outpatient hospital care, about 7 percent less than the national average of $1,976 (Figure 5). At least in part, lower per capita spending in Maryland reflected much lower charges relative to hospital cost than the national average.[2] Still, the growth in per capita spending for hospital care in Maryland has outpaced the national average, gradually narrowing the difference between the level of per capita hospital spending in Maryland and the national average. From 2001 to 2005 (and also from 2004 to 2005), per capita spending for hospital care in Maryland grew at an average annual rate of 8 percent, compared with 7 percent nationally.

[1] Since 1971, the Maryland Health Services Cost Review Commission (HSCRC) has set the rates that hospitals may charge to any payer. In fiscal 2005 (including the first half of CY 2005), HSCRC increased inpatient and outpatient rates by 3.78 percent, including adjustments for intensity and inflation. In fiscal 2006 (including the second half of CY 2005), HSCRC increased inpatient and outpatient rates by 4.9 percent and 3.9 percent, respectively.

[2] In Maryland, the markup in hospital costs (i.e., the difference between hospital costs and charges) averaged 20 percent in fiscal 2005, while the average markup for hospitals nationally was 156 percent, according to data from the American Hospital Association. Maryland Health Services Cost Review Commission (August 2, 2006), *Disclosure of Hospital Financial and Statistical Data* (http://www.hscrc.state.md.us/financial_data_reports/documents/FinancialStatements/financial_disclosure_fy2005.pdf).

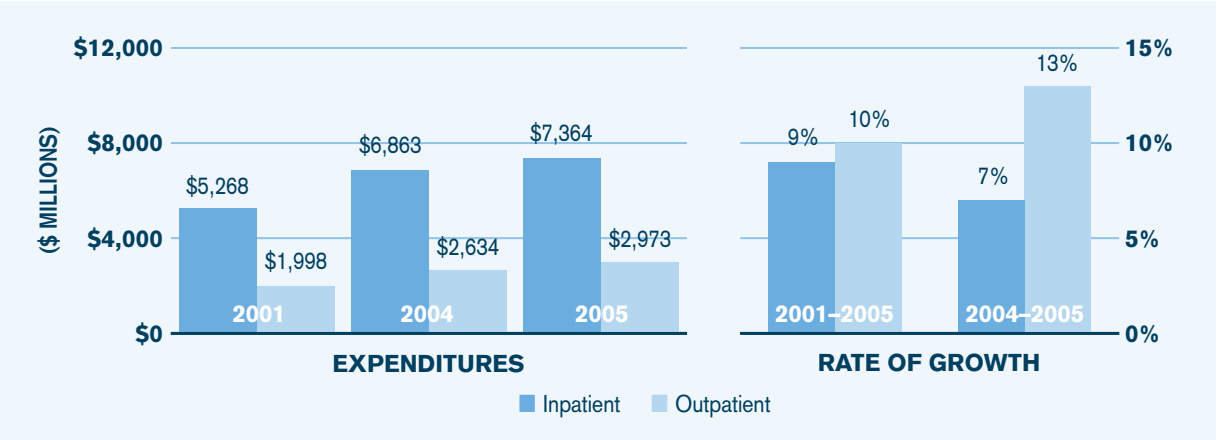
FIGURE 5: Estimated Per Capita Hospital Services Expenditures and Rate of Growth, Maryland and U.S.



Maryland's higher growth in per capita spending for hospital care may reflect the state's regulation of Medicare and Medicaid reimbursements—as well as charges to private insurers and self-pay patients. As in other states, the proportion of residents with private insurance coverage in Maryland has declined while enrollment in Medicaid, in particular, has increased.[3] As a result, public program reimbursements have accounted for a growing share of all providers' revenue, including hospital revenues. In other states, Medicaid reimbursement for hospital care is typically much lower than private insurer reimbursements. Thus, the growth in Medicaid enrollment has probably depressed growth in total expenditures for hospital care in other states—but not in Maryland, where hospital reimbursement rates are the same for all payers.[4]

While Marylanders spend more than twice as much for inpatient care as for outpatient care (in 2005, $7.4 billion versus less than $3.0 billion), expenditures for outpatient care have grown more rapidly. From 2001 to 2005, expenditures for inpatient care grew at an average annual rate of 9 percent, compared with 10 percent average annual growth in expenditures for outpatient care. From 2004 to 2005, the growth in inpatient expenditures dropped to 7 percent, as expenditures for outpatient care accelerated to 13 percent.

FIGURE 6: Estimated Inpatient and Outpatient Expenditures and Rate of Growth in Maryland

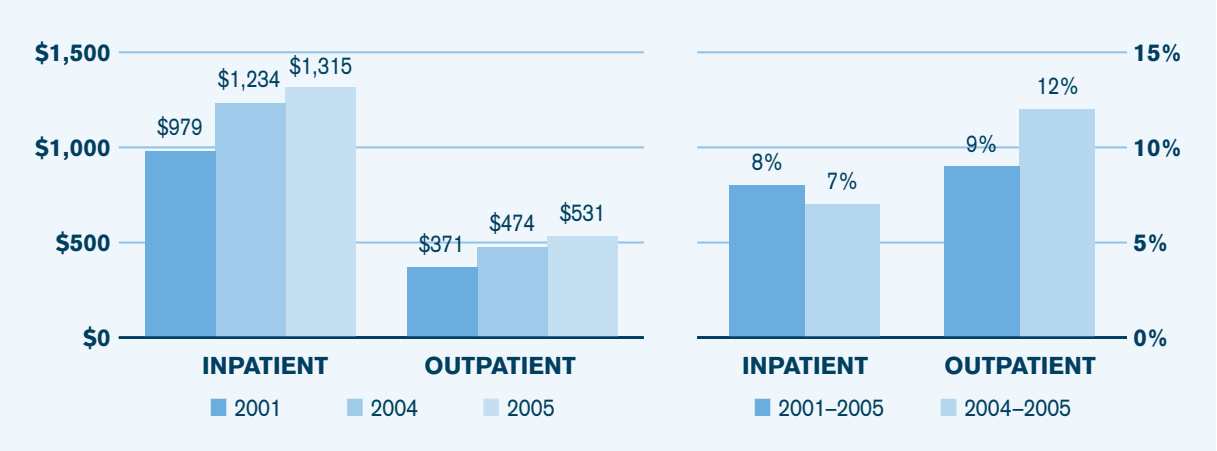


[3] Maryland Health Care Commission (2007a), *Health Insurance Coverage in Maryland Through 2005* (http://mhcc.maryland.gov/health_insurance/insurance_coverage/insurance_report_thru_2005.pdf).

[4] Increases in hospital rates provided through the rate-setting system also affect Medicaid expenditures. A 1-percent increase in inpatient hospital rates increases total Medicaid spending by about 0.24 percent, and a 1-percent increase in outpatient rates increases total Medicaid spending about 0.1 percent, all else being equal.

The pattern of expenditures per capita for inpatient and outpatient hospital care is similar to the pattern of total expenditures. While Marylanders spend substantially more per capita for inpatient care (in 2005, $1,315) than for outpatient care ($531), per capita expenditures for outpatient care have grown faster (Figure 7). Per capita expenditures for outpatient care grew at an average annual rate of 9 percent from 2001 to 2005, and by 12 percent from 2004 to 2005. In contrast, per capita expenditures for inpatient care grew at an average annual rate of 8 percent from 2001 to 2005, but slowed to 7 percent growth from 2004 to 2005.

FIGURE 7: Estimated Per Capita Inpatient and Outpatient Expenditures and Rate of Growth in Maryland



Medicare and private insurance are the largest payers for both inpatient and outpatient hospital care in Maryland. Medicare paid for 41 percent of all inpatient hospital care and 28 percent of all outpatient care provided to Marylanders in 2005 (Table 2). Private insurance financed a somewhat smaller share of inpatient care (37 percent), but nearly half of all outpatient care (46 percent) provided to Marylanders in 2005. Medicaid financed a smaller though still significant share of hospital care in Maryland—in 2005, 18 percent of inpatient care and 15 percent of outpatient care.

TABLE 2: Estimated Inpatient and Outpatient Expenditures by Source of Payment in Maryland

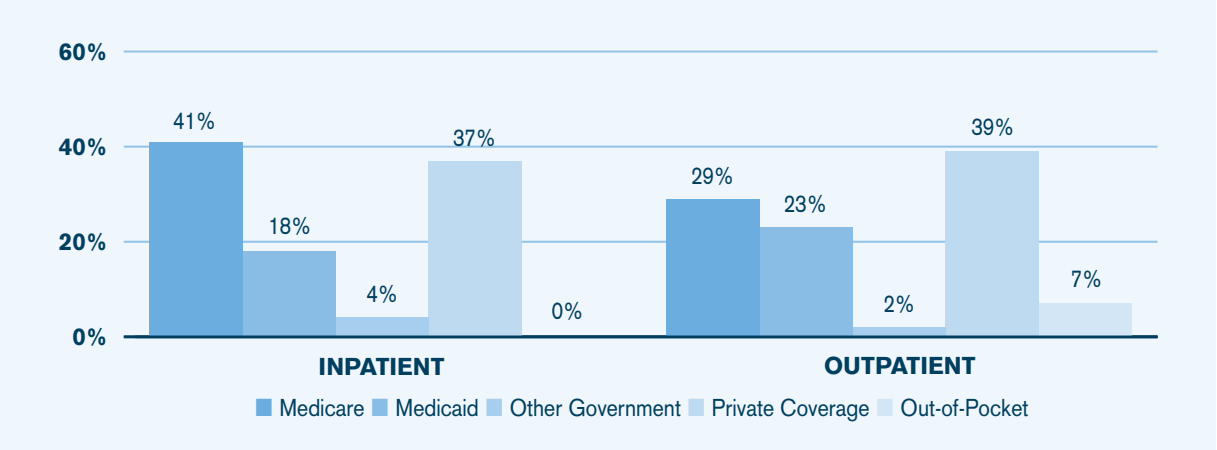
PAYER CATEGORY	INPATIENT						OUTPATIENT					
	2001		2004		2005		2001		2004		2005	
	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total
TOTALS	**$6,092**	**100%**	**$6,863**	**100%**	**$7,364**	**100%**	**$2,218**	**100%**	**$2,634**	**100%**	**$2,973**	**100%**
Medicare	2,288	41	2,802	41	3,014	41	621	28	756	29	838	28
Medicaid	1,026	18	1,266	18	1,330	18	311	11	382	15	453	15
Other Government	292	4	257	4	269	4	59	3	60	2	69	2
Private Coverage	2,426	36	2,482	36	2,690	37	1,039	50	1,223	46	1,374	46
Out-of-Pocket	60	1	56	1	60	1	188	8	213	8	240	8

Marylanders pay out-of-pocket a relatively small share of the cost of inpatient care (in 2005, just 1 percent), but a larger share of outpatient expenditures (8 percent). The larger share of outpatient care paid out-of-pocket reflects the typical structure of cost-sharing in private insurance plans and Medicare, as well as the uninsured population's greater use of hospital outpatient departments as a source of primary care.[5]

As the largest payers for hospital care in Maryland, Medicare and private insurance expenditures have accounted for a large share of the growth in expenditures. Medicare and private insurance financed approximately 78 percent of the increase in expenditures for inpatient hospital care from 2001 to 2005, and 68 percent of the increase in expenditures for outpatient care (Figure 8).

However, Medicaid expenditures for outpatient care, in particular, accounted for a disproportionate share of the growth in total outpatient expenditures—reflecting in part increases in program enrollment. In Maryland, Medicaid financed 23 percent of the increase in outpatient expenditures from 2001 to 2005 (and 18 percent of the increase in inpatient expenditures). As a result, Medicaid financed 15 percent of all outpatient care in Maryland in 2004 and 2005 (compared with 11 percent in 2001), while the share of outpatient care financed by private insurance declined commensurately—from 50 percent in 2001 to 46 percent in 2005.

FIGURE 8: Estimated Share of Increase in Inpatient and Outpatient Expenditures by Source of Payment in Maryland, 2001–2005



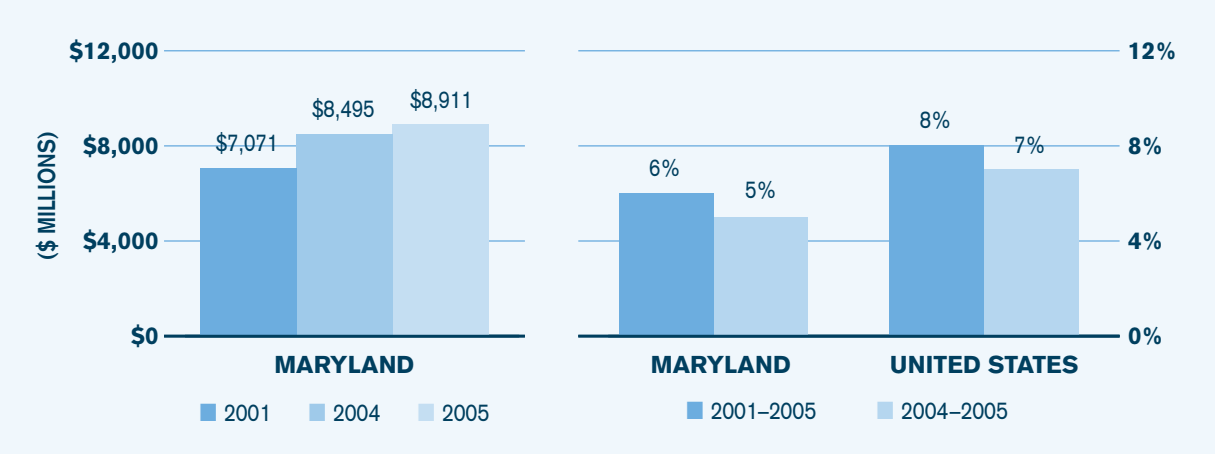
NOTE: 0% indicates < 0.5%.

[5] Maryland Health Care Commission (2007a), *op cit.*

EXPENDITURES FOR PRACTITIONER SERVICES

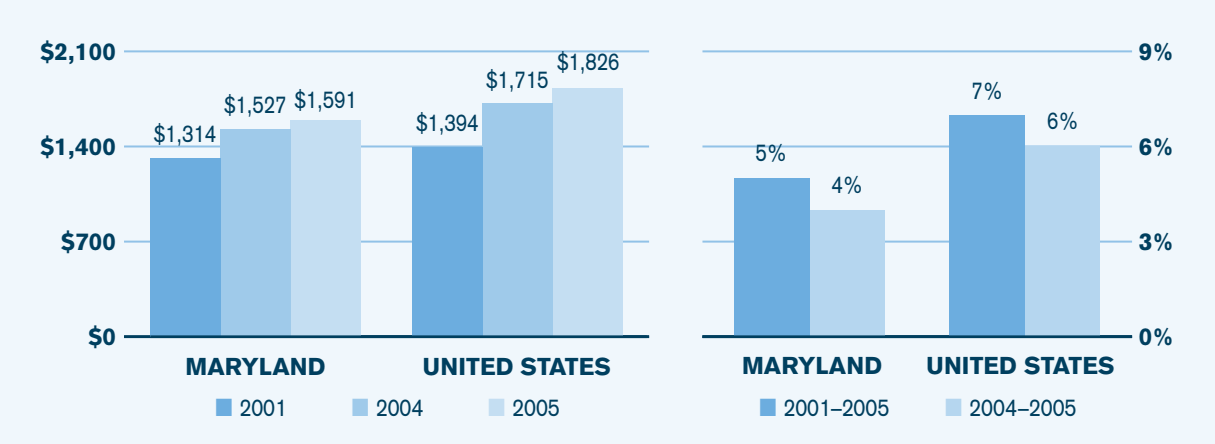
Marylanders spent approximately $8.9 billion for physician and other professional services in 2005—the latter including dental services; nonphysician vision services; occupational, physical, and other therapy services; nurse practitioner services; and chiropractic (Figure 9). In Maryland, total expenditures for practitioner services have grown more slowly than the national average: at an average annual rate of 6 percent from 2001 to 2005 (compared to the national average of 8 percent per year), and by 5 percent from 2004 to 2005 (compared to the national average of 7 percent).

FIGURE 9: Estimated Practitioner Services Expenditures and Rate of Growth



Per capita expenditures for practitioner services also are lower in Maryland ($1,591 in 2005) than the national average ($1,826) and, like total expenditures for practitioner services, have grown more slowly than the national trend (Figure 10). From 2001 to 2005, per capita expenditures for practitioner services in Maryland grew at an average rate of 5 percent per year, slowing to 4 percent from 2004 to 2005. In contrast, national per capita expenditures for practitioner services grew at an average annual rate of 7 percent from 2001 to 2005, and slowed to 6 percent from 2004 to 2005.

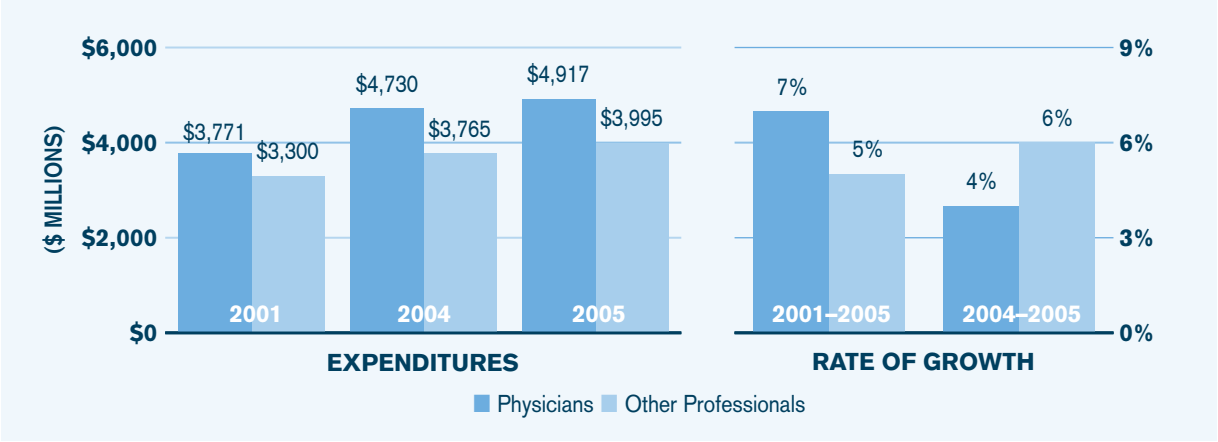
FIGURE 10: Estimated Per Capita Practitioner Services Expenditures and Rate of Growth, Maryland and U.S.



NOTE: 0% indicates < 0.5%.

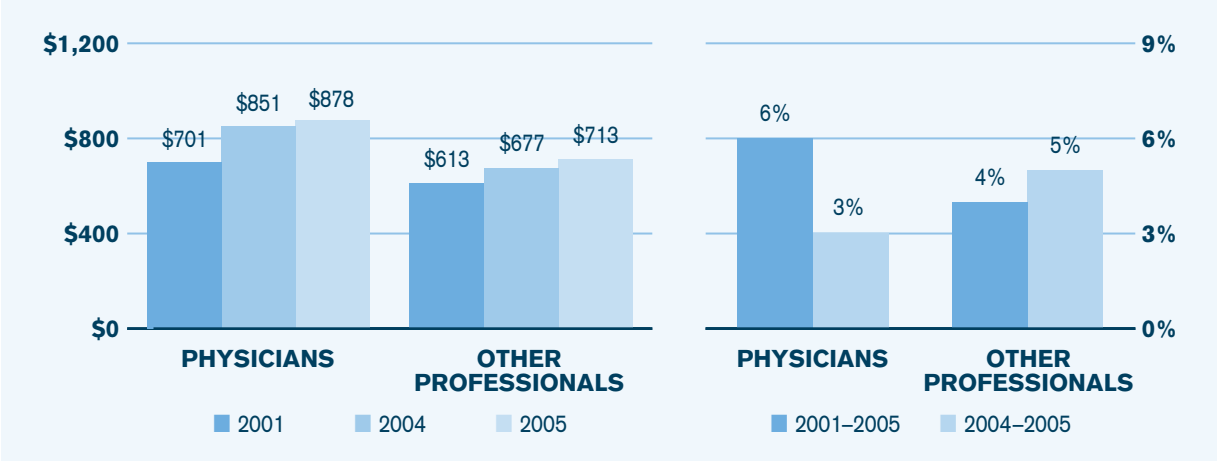
Physician services account for more than half of all expenditures for practitioner services in Maryland (in 2005, 55 percent). From 2001 to 2005, expenditures for physician care grew much faster than expenditures for other professional services—averaging 7 percent per year, compared to 5 percent for other professional services (Figure 11). However, from 2004 to 2005, spending for other professional services in Maryland accelerated (to 6 percent) while the growth in spending for physician services declined (to 4 percent). The slower growth in expenditures for physician services in 2005 occurred in the midst of significant controversy between physicians and insurers over payment for covered services.[6]

FIGURE 11: Estimated Physician and Other Professional Expenditures and Rate of Growth in Maryland



From 2001 to 2005, per capita spending for physician care grew at an average annual rate of 6 percent while per capita spending for other professional services grew at an average annual rate of 4 percent (Figure 12). Both growth rates reflected increases in the use of services as well as small increases in price. From 2004 to 2005, the growth in per capita spending slowed to 3 percent for physician care, but accelerated to 5 percent for other professional services.

FIGURE 12: Estimated Per Capita Physician and Other Professional Expenditures and Rate of Growth in Maryland



[6] In January 2005, the Supreme Court declined to hear an appeal filed by six national insurers in a bid to stop a class action lawsuit brought by more then 600,000 physicians who alleged that a number of companies—including United Healthcare, Aetna, Cigna, and others—underpaid them for treating patients, delaying or denying reimbursements and illegally rejecting claims for necessary medical treatments (Bloomberg/ Hartford Courant, January 11, 2005). The Blue Cross and Blue Shield Association was reported to be facing similar lawsuits from physicians disputing payment practices.

The primary sources of payment for physician care in Maryland are different than those for other professional services (Table 3). Private insurance is the dominant source of payment for physician care (accounting for 51 percent of total expenditures in 2005), followed by Medicare (26 percent). Marylanders financed just 13 percent of physician care out-of-pocket, and Medicaid and other government programs together financed just 10 percent of physician care in 2005.

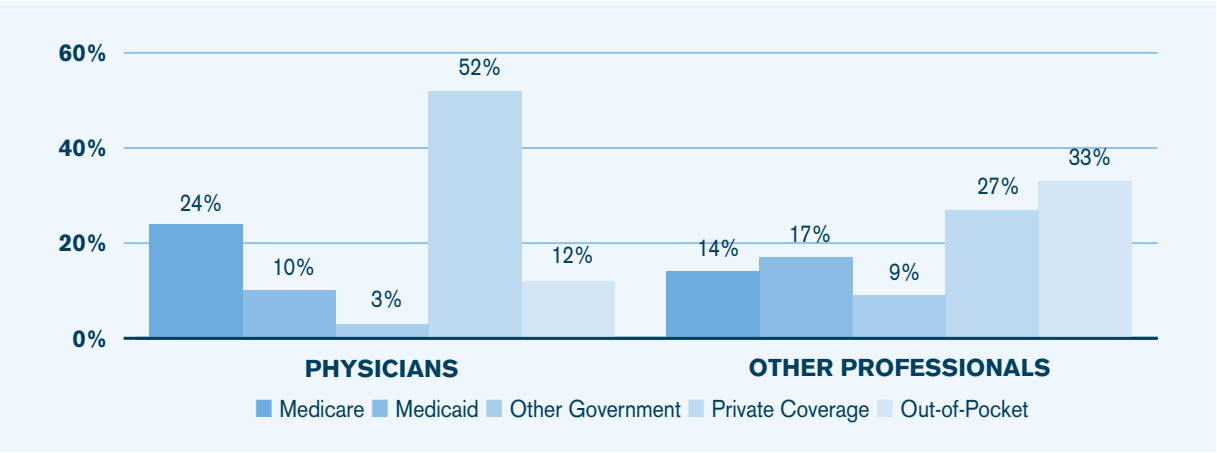
In contrast, out-of-pocket expenditures are the dominant source of payment for other professional services (accounting for 35 percent of total expenditures in 2005), followed closely by private insurance (32 percent). Medicaid and other government programs financed 25 percent of other professional services, while Medicare financed just 7 percent—although these programs may finance substantially larger proportions of some services in this category.

TABLE 3: Estimated Physician and Other Professional Expenditures by Source of Payment in Maryland

PAYER CATEGORY	PHYSICIANS						OTHER PROFESSIONALS					
	2001		2004		2005		2001		2004		2005	
	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total
TOTALS	**$3,771**	**100%**	**$4,730**	**100%**	**$4,917**	**100%**	**$3,300**	**100%**	**$3,765**	**100%**	**$3,995**	**100%**
Medicare	995	26	1,213	26	1,269	26	191	6	265	7	291	7
Medicaid	229	6	320	7	348	7	380	12	453	12	498	12
Other Government	107	3	137	3	137	3	445	13	505	13	509	13
Private Coverage	1,913	51	2,424	51	2,503	51	1,094	33	1,205	32	1,280	32
Out-of-Pocket	527	14	635	13	659	13	1,189	36	1,337	36	1,417	35

For both physician services and other professional services, the estimated share of total expenditures paid out-of-pocket declined slightly from 2001 to 2005, reflecting in part enrollment growth in Medicaid, which requires no cost-sharing. Medicaid has financed a growing share of physician services, though its share of total expenditures has remained relatively small—just 6 percent of total expenditures for physician care in 2001 and 7 percent in 2005. However, from 2001 to 2005, Medicaid accounted for 10 percent of the growth in expenditures for physician care. The dominant payers—private insurance and Medicare—respectively accounted for 52 percent and 24 percent of the growth in total expenditures (Figure 13).

FIGURE 13: Estimated Share of Increase in Physician and Other Professional Expenditures by Source of Payment in Maryland, 2001–2005

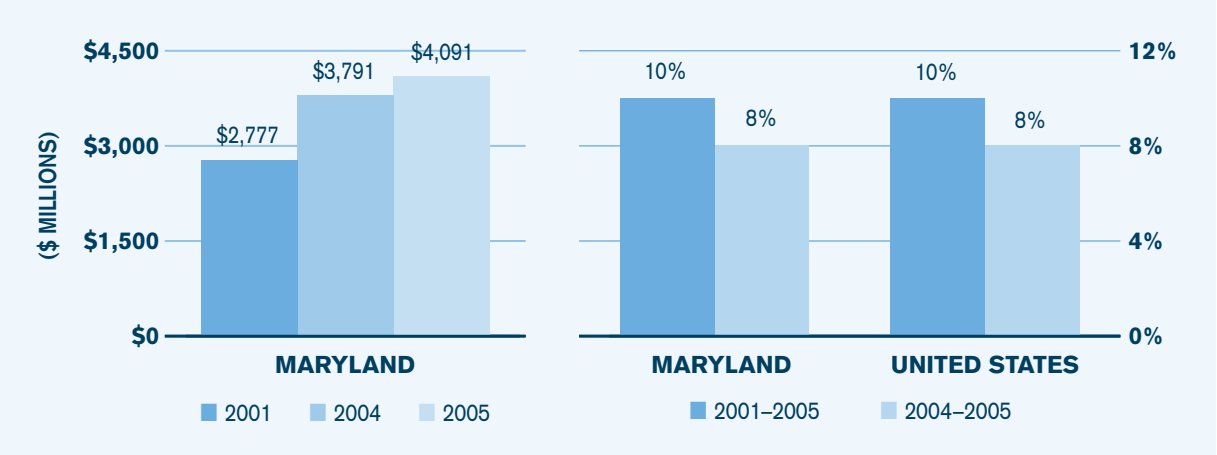


For other professional services, Medicare became a more important source of financing, although it too remained relatively small. Medicare expenditures grew from 6 percent of the total in 2001 to 7 percent in 2005—as both private insurance and out-of-pocket expenditures became slightly less important sources of payment. Increased Medicare expenditures accounted for 14 percent of the growth in total expenditures for other professional services from 2001 to 2005, while the dominant payers—consumer out-of-pocket expenditures and private insurance—accounted for 33 percent and 27 percent of the growth in total expenditures, respectively.

EXPENDITURES FOR PRESCRIPTION DRUGS

In 2005, Marylanders spent nearly $4.1 billion for outpatient prescription drugs (Figure 14). From 2001 to 2005, the growth in expenditures for prescription drugs in Maryland matched the national trend, increasing at an average annual rate of 10 percent per year. The growth in expenditures for prescription drugs slowed to 8 percent from 2004 to 2005 in Maryland and nationally, correlating with a number of national factors—including a decline in the introduction of new 'blockbuster drugs,' the conversion of a number of branded drugs to generic status, and purchaser demands for greater transparency in drug pricing.[7] In 2004 and 2005, drug price increases slowed from about 5 percent in the 2001-2003 period to about 3.5 percent.[8] Other factors also may have affected the use of prescription drugs and, therefore, the slower growth of expenditures in 2005—including tiered copayments and other measures to encourage substitution of generic or lower-cost drugs for higher-cost brand name drugs.

FIGURE 14: Estimated Prescription Drug Expenditures and Rate of Growth

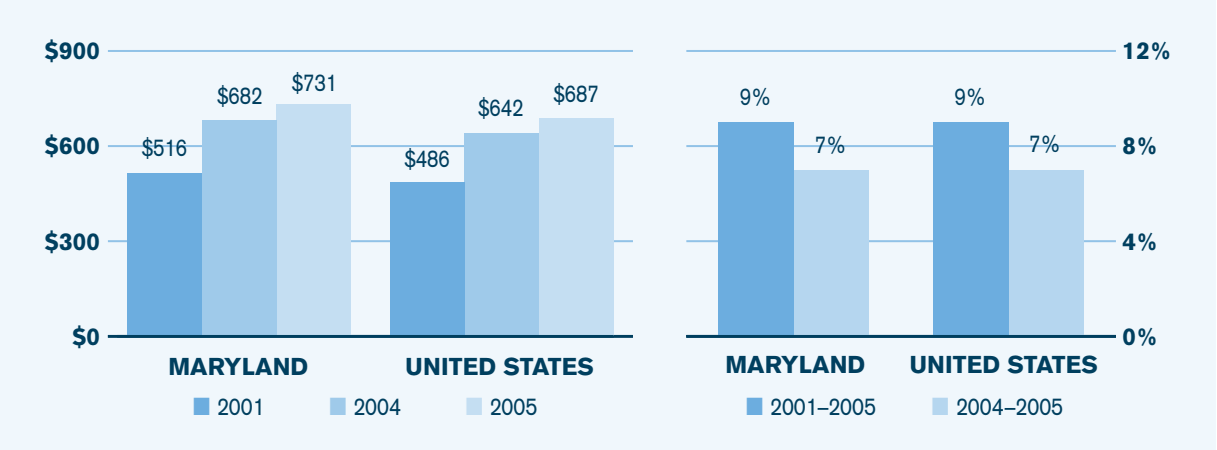


Per capita expenditures for prescription drugs in Maryland in 2005 ($731) continued to exceed the national average ($687) (Figure 15). Per capita, Marylanders spend about 6 percent more for prescription drugs than the national average. The growth in per capita spending for prescription drugs in Maryland (as with total expenditures for prescription drugs) has mirrored national trends, averaging 9 percent growth per year from 2001 to 2005 and slowing to 7 percent growth from 2004 to 2005.

[7] Safety concerns around the use of COX-2 inhibitors as well as antidepressants in children apparently contributed to the slowing of expenditures for prescription drugs. In Maryland, the use of COX-2 inhibitors among privately insured patients fell nearly 70 percent from 2004 to 2005. Maryland Health Care Commission (2007b), *Prescription Drug Use and Expenditures 2005: Trends Among Privately Insured Patients* (http://mhcc.maryland.gov/health_care_expenditures/exputildrug2003/pdfreport.pdf).

[8] Maryland Health Care Commission (2007b), *ibid.*

FIGURE 15: Estimated Per Capita Prescription Drug Expenditures and Rate of Growth, Maryland and U.S.



Private insurance is the dominant payer for prescription drugs in Maryland. In 2005, private insurance financed 46 percent of all expenditures for prescription drugs (Table 4). However, largely reflecting extensive cost-sharing for prescription drugs in insurance plans, consumers paid 34 percent of total expenditures for prescription drugs out-of-pocket in 2005, as they did in 2001 and 2004. The share of expenditures that is privately insured declined from 48 percent in 2001 to 46 percent in 2005, displaced by an increase in Medicaid expenditures. In both 2004 and 2005, Medicaid and other government programs together financed 20 percent of all expenditures for prescription drugs in Maryland, compared with 17 percent in 2001.

TABLE 4: Estimated Prescription Drug Expenditures by Source of Payment in Maryland

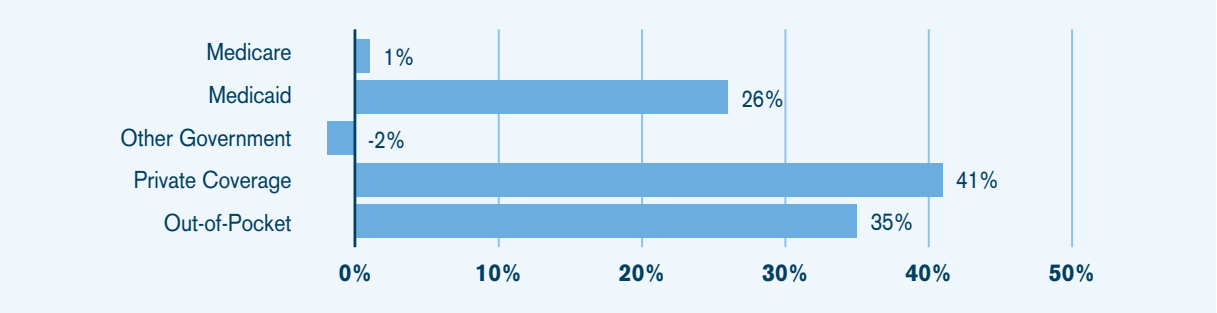
PAYER CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$2,777**	**100%**	**$3,791**	**100%**	**$4,091**	**100%**
Medicare	5	0	8	0	12	0
Medicaid	388	14	666	18	727	18
Other Government	94	3	67	2	67	2
Private Coverage	1,346	48	1,750	46	1,881	46
Out-of-Pocket	945	34	1,301	34	1,404	34

NOTE: 0% indicates < 0.5%.

As for all services, growth in expenditures among the dominant payers for prescription drugs—private insurers and consumers—explained most (taken together, 76 percent) of the growth in total expenditures from 2001 to 2005 (Figure 16). However, a decline in the private insurance share of prescription drugs is evident. While private insurers accounted for 48 percent of all expenditures for prescription drugs in 2001, they accounted for just 41 percent of the growth in expenditures through 2005.

In contrast, Medicaid—which accounted for just 14 percent of all expenditures for prescription drugs in 2001—accounted for 26 percent of the growth in prescription drug expenditures from 2001 to 2005.[9] In June 2005, the federal Centers for Medicare & Medicaid Services (CMS) approved Maryland's formation of a purchasing pool with Louisiana and West Virginia, in order to leverage Medicaid purchasing of prescription drugs over the states' combined 1.3 million Medicaid beneficiaries.

FIGURE 16: Estimated Share of Increase in Prescription Drug Expenditures by Source of Payment in Maryland, 2001–2005

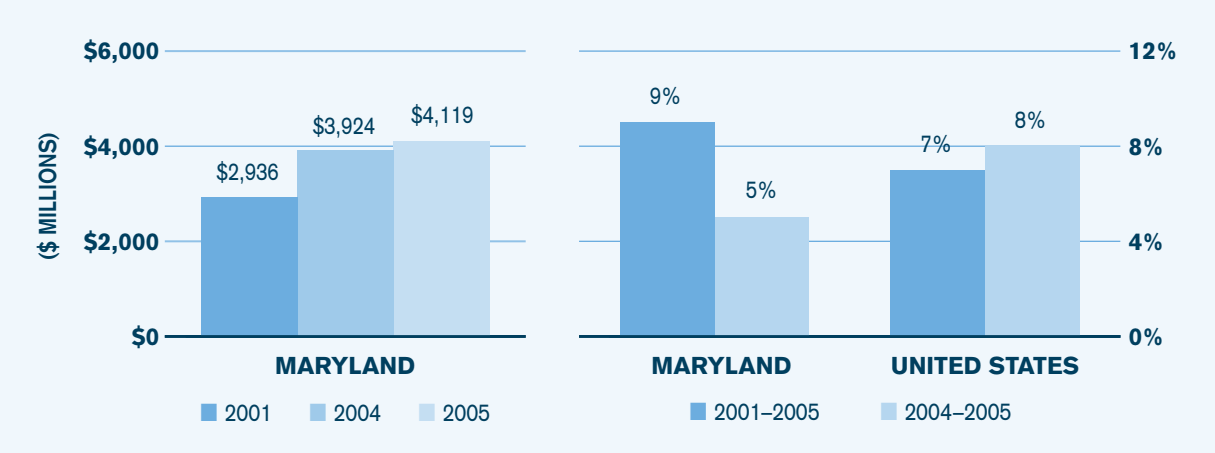


[9] A small percentage of this growth (1 to 2 percent) was associated with the transition of Maryland Pharmacy Assistance Program enrollees (in other government programs) into Medicaid since 2001.

EXPENDITURES FOR LONG-TERM CARE AND OTHER SERVICES

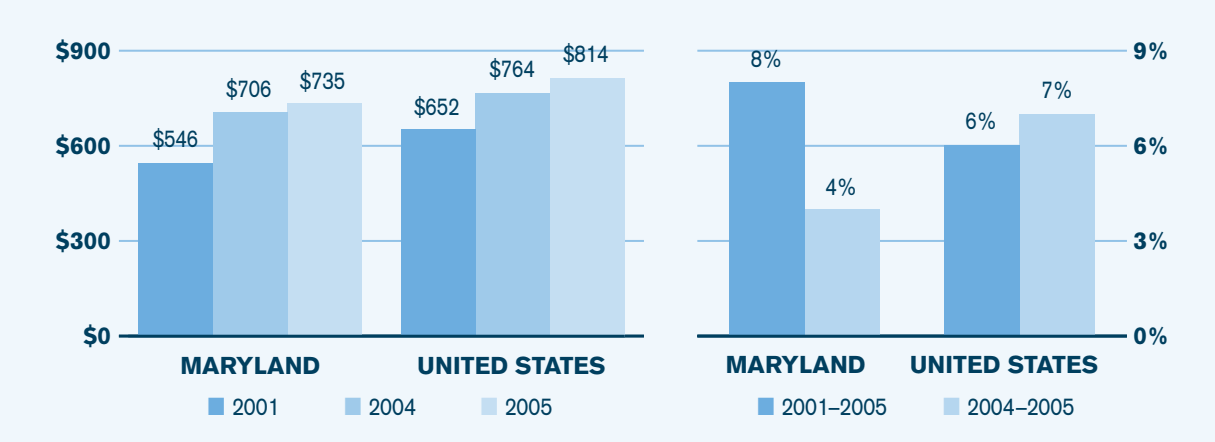
Expenditures for long-term care and other miscellaneous services in Maryland exceeded $4.1 billion in 2005 (Figure 17). Expenditures for long-term care—including nursing home and home health care expenditures—accounted for approximately 84 percent of the aggregate, nearly $3.5 billion in 2005. Expenditures for both long-term care and other services grew much faster in Maryland from 2001 to 2005 than the national trend, averaging 9 percent annual growth over those years compared with 7 percent nationally. However, by 2005, growth in these expenditures in Maryland slowed substantially, to just 5 percent, as expenditures nationally accelerated to 8 percent.

FIGURE 17: Estimated Long-Term Care and Other Services Expenditures and Rate of Growth



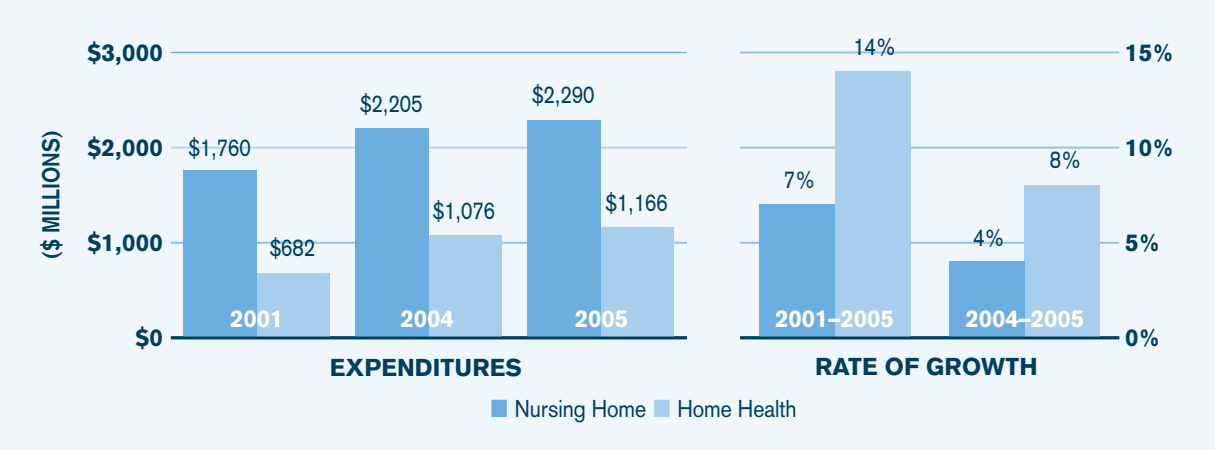
Per capita, Marylanders spent about 10 percent less for long-term care and other services than the national average in 2005—$735 compared with $814 (Figure 18). The slowing of growth in total spending for long-term care and other services in Maryland compared to the nation also is apparent on a per capita basis: per capita spending in Maryland slowed from the trend of 8 percent per year from 2001 to 2005, to just 4 percent from 2004 to 2005. In contrast, national per capita spending for these services increased from a trend of 6 percent per year from 2001 to 2005, to 7 percent from 2004 to 2005.

FIGURE 18: Estimated Per Capita Long-Term Care and Other Services Expenditures and Rate of Growth, Maryland and U.S.



Expenditures for nursing home care account for approximately two-thirds of total expenditures for long-term care in Maryland. In 2005, Marylanders spent nearly $2.3 billion for nursing home care and less than $1.2 billion for home health care services (Figure 19). However, expenditures for home health care services are growing relative to those for nursing home care, as Medicaid—the largest third-party payer for long-term care services in Maryland, as in other states—has attempted to help residents in need of long-term care services find them in the community.[10] As a result, expenditures for home health care in Maryland grew at an average rate of 14 percent per year from 2001 to 2005, and by 8 percent from 2004 to 2005. By comparison, nursing home expenditures have grown much more slowly—averaging 7 percent per year from 2001 to 2005, and just 4 percent from 2004 to 2005.

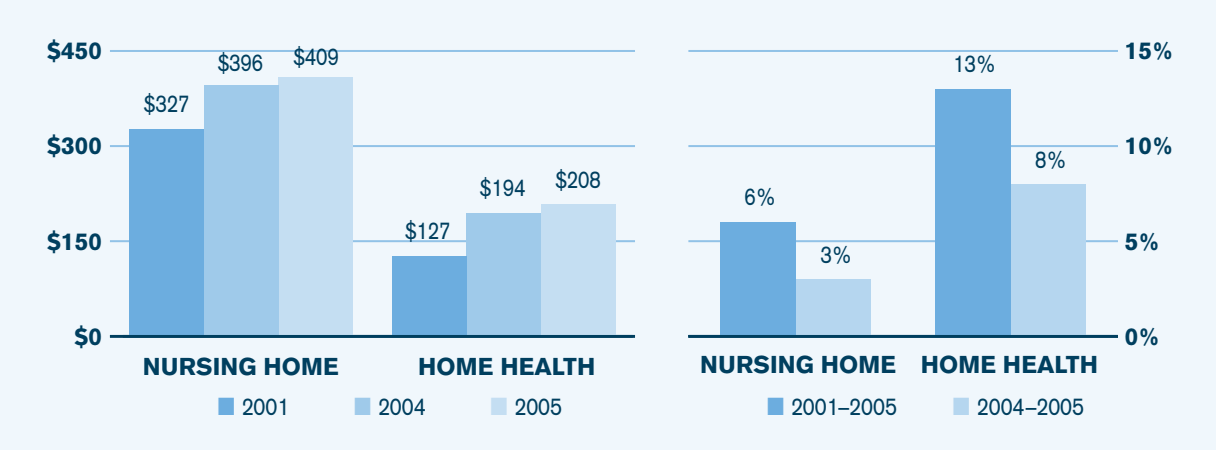
FIGURE 19: Estimated Nursing Home and Home Health Expenditures and Rate of Growth in Maryland



Per capita, Marylanders spent $409 for nursing home care in 2005, compared with $208 for home health care services (Figure 20). Expenditures per capita for home health care increased at an average annual rate of 13 percent per year from 2001 to 2005, compared with an average annual increase of just 6 percent for nursing home care. For both types of services, per capita expenditures slowed from 2004 to 2005—growing just 8 percent and 3 percent, respectively.

[10] Maryland Medicaid funds six waiver programs for home and community-based services that allow individuals in need of long-term care services to remain in a community setting, although the level of care they need warrants placement in a long-term care facility. Waiver programs also allow Medicaid to provide medical and qualified nonmedical services to medically fragile children, individuals with developmental disabilities, and individuals with traumatic brain injury. These programs served 14,300 people as of January 2005. In addition, the New Directions waiver for people with developmental disabilities was implemented in fiscal year 2006 (which includes the last 6 months of 2005), bringing the total number of waivers to seven. The total number of waiver slots continues to increase; as of January 2007, there were 16,200 waiver slots.

FIGURE 20: Estimated Per Capita Nursing Home and Home Health Expenditures and Rate of Growth in Maryland



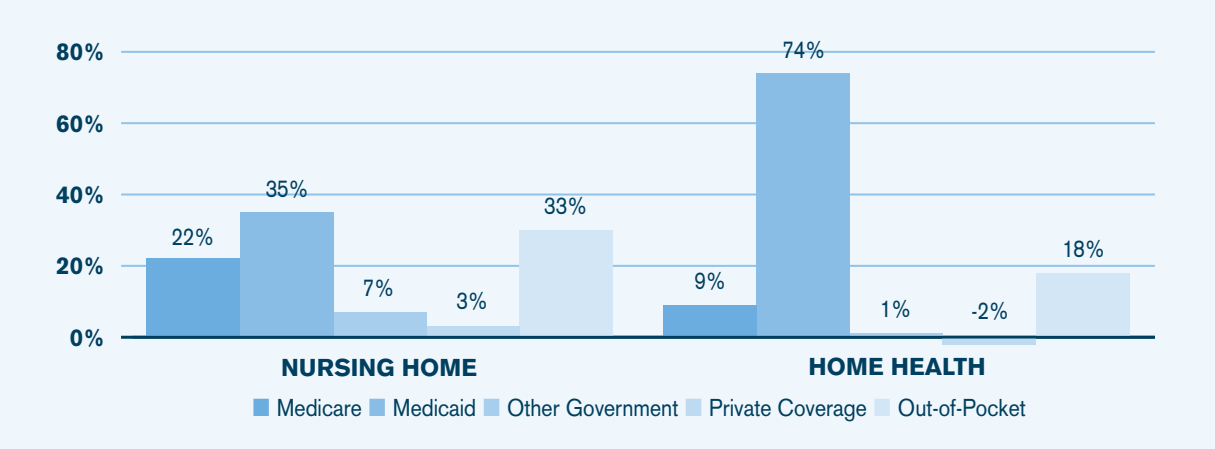
Medicaid is the largest source of payment for both nursing home and home health care in Maryland. In 2005, Medicaid financed 45 percent of all expenditures for nursing home care and 60 percent of expenditures for home health care (Table 5). Because Medicare finances either nursing home or home health care only as it relates to recovery from a hospitalization, it is a relatively minor payer for these services, notwithstanding the elderly and disabled populations that Medicare serves. In addition, private long-term care insurance is relatively rare, especially among the population that, by virtue of age or disability, is currently most likely to require these services. Thus, Marylanders finance a significant share of long-term care expenditures out-of-pocket. In 2005, Marylanders paid 28 percent of nursing home care expenditures out-of-pocket (compared with 27 percent in 2001) and 18 percent of home health care expenditures out-of-pocket (compared with 17 percent in 2001).

TABLE 5: Estimated Nursing Home and Home Health Expenditures by Source of Payment in Maryland

PAYER CATEGORY	NURSING HOME						HOME HEALTH					
	2001		2004		2005		2001		2004		2005	
	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total	Expenditure ($ millions)	Percent of Total
TOTALS	**$1,760**	**100%**	**$2,205**	**100%**	**$2,290**	**100%**	**$682**	**100%**	**$1,076**	**100%**	**$827**	**100%**
Medicare	264	15	345	16	383	17	129	19	148	14	131	15
Medicaid	853	48	1,010	46	1,041	45	336	49	643	60	425	60
Other Government	29	2	62	3	64	3	5	1	10	1	6	1
Private Coverage	135	8	148	7	151	7	97	14	85	8	124	7
Out-of-Pocket	478	27	640	29	652	28	116	17	190	18	141	18

Responding to the magnitude of uninsured long-term care expenditures and the correspondingly high probability that individuals who require long-term care will "spend down" to Medicaid eligibility, the federal Deficit Reduction Act of 2005 (DRA-05) authorized long-term care insurance partnerships that enable individuals who purchase qualifying long-term care insurance policies to retain a specified amount of assets and still qualify for Medicaid, provided they meet other Medicaid eligibility criteria—including income criteria.[11] Maryland is 1 among at least 21 states that enacted authorizing legislation in anticipation of this change in federal law—although in no state are these provisions likely to substantially affect out-of-pocket spending for long-term care services or spend-down to Medicaid eligibility in the near term. From 2001 to 2005, out-of-pocket spending accounted for 33 percent of the increase in expenditures for nursing home care and 18 percent of the increase in expenditures for home health care in Maryland (Figure 21). In contrast, Medicaid accounted for 35 percent of the increase in nursing home expenditures and 74 percent of the increase in expenditures for home health care.

FIGURE 21: Estimated Share of Increase in Nursing Home and Home Health Expenditures by Source of Payment in Maryland, 2001–2005



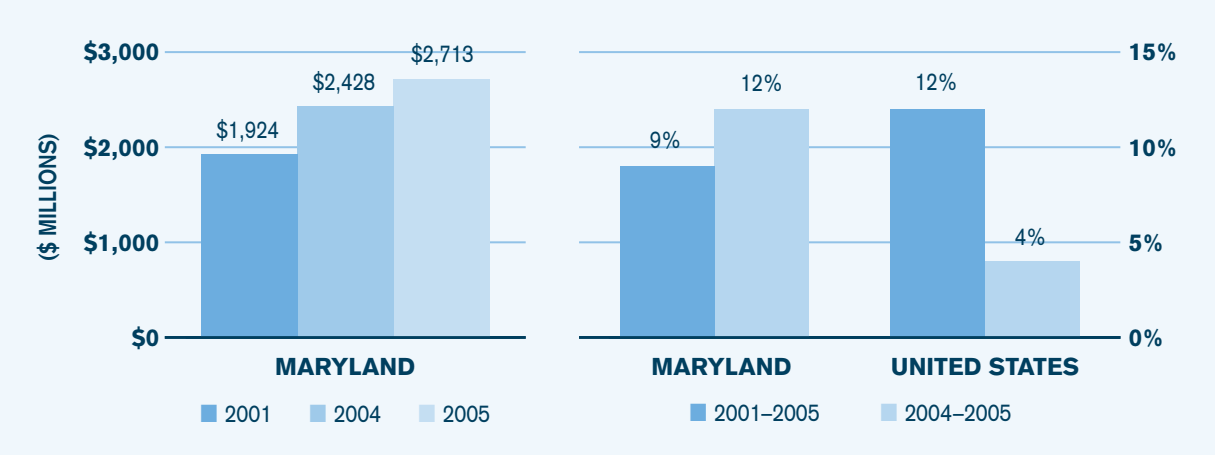
[11] E. Kassner (2006), *Long-Term Care Partnership Programs* (Washington, DC: AARP Public Policy Institute) (http://www.aarp.org/research/longtermcare/insurance/fs124_ltc_06.html).

EXPENDITURES FOR THE ADMINISTRATION AND NET COST OF INSURANCE

The administrative costs of insurance include the costs that both private insurers and public programs incur in enrolling and disenrolling participants and processing claims for health care services. The net cost of insurance includes only private insurers' profits, capital expenditures, additions to surplus, and assessments and taxes. In 2005, Marylanders spent $2.7 billion for the administration and net cost of private insurance and public insurance programs (Figure 22). From 2001 to 2005, these expenditures increased at an average annual rate of 9 percent, accelerating to 12 percent growth from 2004 to 2005. This pattern is markedly different than national trends: nationally, expenditures for the administration and net cost of insurance grew much faster over the 5-year period (averaging 12 percent per year), but slowed dramatically (to 4 percent) from 2004 to 2005.

Some (but certainly not all) of the faster growth of these expenses in Maryland may be related to removal of HMOs' exemption from the 2 percent state tax on premiums that non-HMO insurers pay. Since 2005, the additional revenue gained from the removal of this exemption is used to help subsidize the cost of medical malpractice premium rates and also to increase Medicaid payments.[12] [13]

FIGURE 22: Estimated Administration Expenditures and Net Cost of Insurance, and Rate of Growth

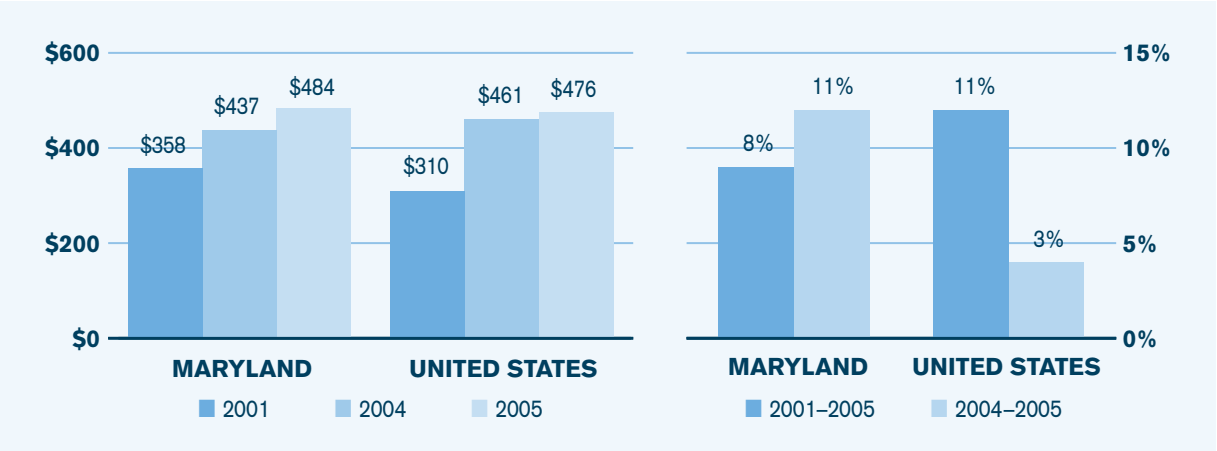


Reflecting the high growth of expenditures for the administration and net cost of insurance from 2004 to 2005, Marylanders paid more for the administration and net cost of insurance than the national average in 2005—$484 per capita for the administration and net cost of insurance, compared with $476 nationally (Figure 23). From 2004 to 2005, per capita expenditures for the administration and net cost of insurance in Maryland grew 11 percent compared with just 3 percent nationally, reversing the 2001-2005 trend of slower growth in Maryland.

[12] Medicaid started transitioning payment increases by procedure codes in 2005 with codes billed by obstetricians/gynecologists, neurosurgeons, and emergency medicine personnel, who generally face the highest malpractice insurance premiums. It is anticipated that Medicaid rates will equal 80 to 100 percent of Medicare fees for all specialties by 2009.

[13] Enacted in 2005, S.B. 831 also capped malpractice insurance rate increases for physicians at 5 percent in 2005. In addition, S.B. 831 capped noneconomic damages at $650,000 in most malpractice lawsuits and at $812,500 in cases that involve patient deaths.

FIGURE 23: Estimated Per Capita Administration Expenditures and Net Cost of Insurance, and Rate of Growth, Maryland and U.S.



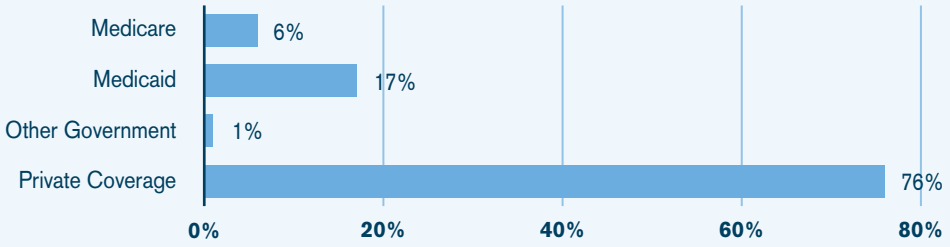
As in 2001 and 2004, private insurance accounted for the vast majority of expenditures for the administration and net cost of insurance in Maryland. In each year, 77 percent of these expenditures were associated with private insurance plans (Table 6). Medicaid expenditures for administration increased as a share of total expenditures for administration and the net cost of insurance combined—from 10 percent in 2001 to 12 percent in 2005. Over the same period, Medicaid enrollment in Maryland increased at an average annual rate of 3 percent per year (Table 14).

TABLE 6: Estimated Administration Expenditures and Net Cost of Insurance by Source of Payment in Maryland

PAYER CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$1,924**	**100%**	**$2,428**	**100%**	**$2,713**	**100%**
Medicare	166	9	193	8	210	8
Medicaid	183	10	258	11	320	12
Other Government	88	5	101	4	97	4
Private Coverage	1,488	77	1,877	77	2,086	77

Consistent with its high share of total expenditures for the administration and net cost of insurance, private insurance accounted for 76 percent of the growth in these expenditures from 2001 to 2005 (Figure 24). Medicaid accounted for 17 percent of the growth in these expenditures from 2001 to 2005, and Medicare accounted for 6 percent. For traditional Medicare and Medicaid, these expenditures are solely for administration.

FIGURE 24: Estimated Share of Increase in Administration Expenditures and Net Cost of Insurance by Source of Payment in Maryland, 2001–2005



WHO PAID FOR MARYLAND'S HEALTH CARE?

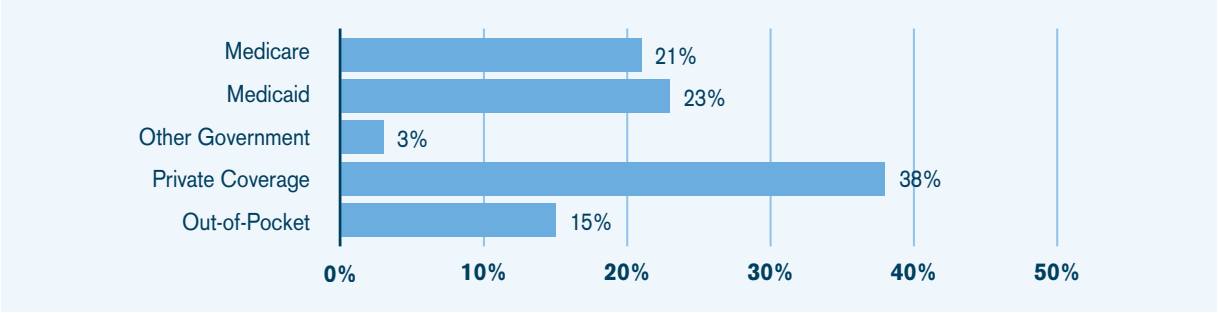
Private payers—either private insurance or consumer out-of-pocket payments—finance most health care expenditures in Maryland. In 2005, private insurance financed 40 percent of all health care expenditures; 17 percent were paid out-of-pocket (Table 7). Government programs financed the balance of expenditures for health care in Maryland. These programs included Medicare (which financed 21 percent of health care expenditures in 2005), Medicaid (18 percent), and other government programs (4 percent). Taken together, public program expenditures accounted for a slightly larger percentage of all health care expenditures in 2005 (43 percent) than in 2001 (42 percent).

TABLE 7: Estimated Health Care Expenditures by Source of Payment in Maryland

PAYER CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$21,975**	**100%**	**$28,135**	**100%**	**$30,171**	**100%**
Medicare	4,565	21	5,863	21	6,323	21
Medicaid	3,572	16	5,039	18	5,453	18
Other Government	1,028	5	1,217	4	1,242	4
Private Coverage	9,025	41	11,240	40	12,098	40
Out-of-Pocket	3,785	17	4,776	17	5,054	17

As the largest single category of health care financing in Maryland, the growth in privately insured expenditures for health care accounted for the largest share of the growth in health care expenditures from 2001 to 2005—38 percent (Figure 25). However, public programs—mainly Medicare and Medicaid—accounted for nearly half of the growth in health care expenditures (47 percent), with Medicaid accounting for a slightly larger share of total growth (23 percent) than Medicare (21 percent). Out-of-pocket spending grew at just less than the pace of health care spending as a whole—accounting for 17 percent of all health care expenditures in both 2001 and 2005, but 15 percent of the growth in total expenditures over that period.

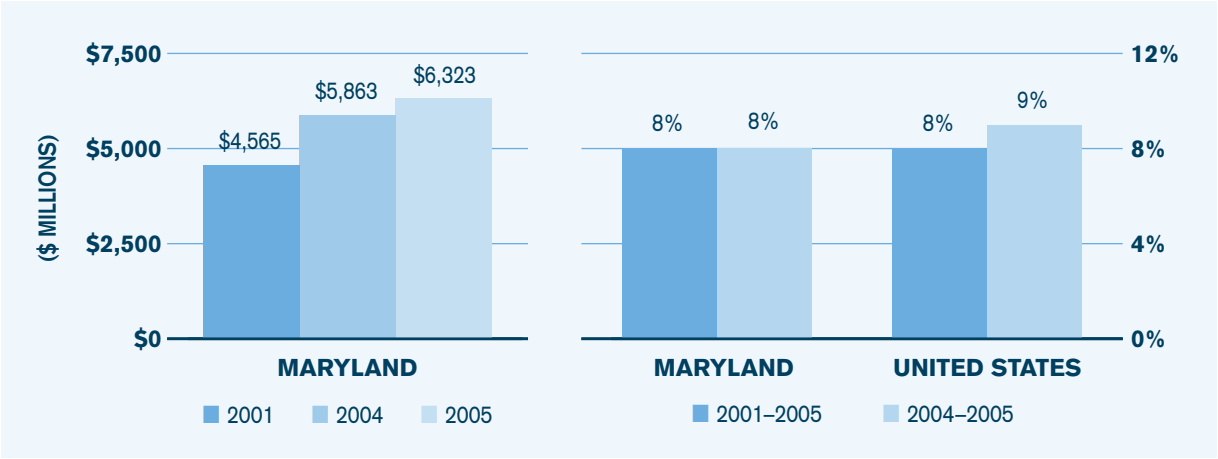
FIGURE 25: Estimated Share of Increase in Health Care Expenditures by Source of Payment in Maryland, 2001–2005



MEDICARE EXPENDITURES

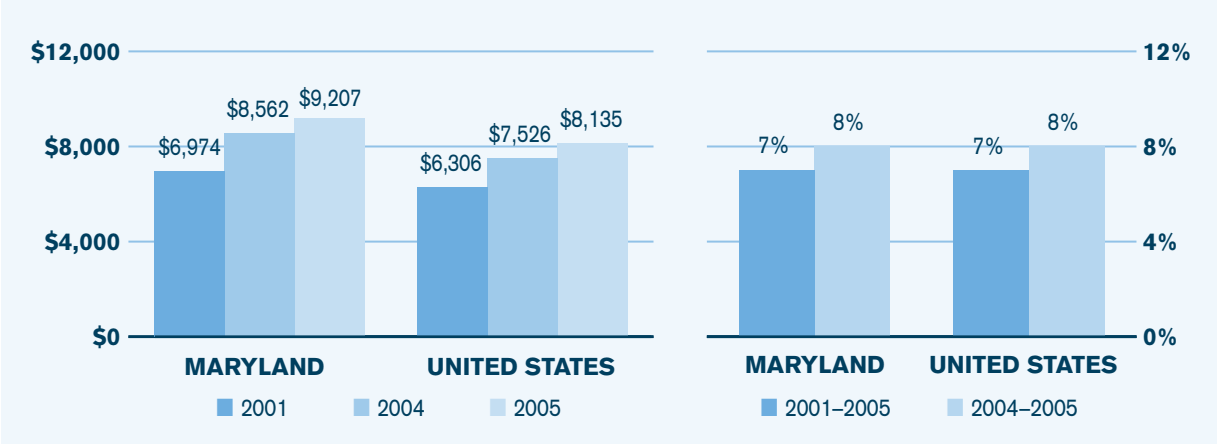
Medicare expenditures in Maryland reached $6.3 billion in 2005, having grown at an average rate of 8 percent per year since 2001—equal to the national trend (Figure 26). From 2004 to 2005, the growth in total Medicare spending in Maryland remained at 8 percent, compared with 9 percent growth in Medicare spending nationally. Medicare enrollment in Maryland also grew more slowly than enrollment nationally.

FIGURE 26: Estimated Medicare Expenditures and Rate of Growth



On a per enrollee basis, Medicare spent about 13 percent more for health care services in 2005 than the national average—$9,207 in Maryland compared with a national average of $8,135 (Figure 27). Growth in Medicare spending per enrollee in Maryland approximately equaled the national trend from 2001 to 2005, and also from 2004 to 2005.

FIGURE 27: Estimated Per Enrollee Medicare Expenditures and Rate of Growth, Maryland and U.S.



More than 60 percent of Medicare expenditures in Maryland are associated with hospital care. In both 2004 and 2005, inpatient care accounted for 48 percent of Medicare spending in Maryland, up from 47 percent in 2001 (Table 8). Outpatient care accounted for an additional 13 percent of all Medicare spending in Maryland, up from 12 percent in 2001. In contrast, spending for physician services declined from 22 percent of total Medicare expenditures in 2001 to 20 percent in 2005.

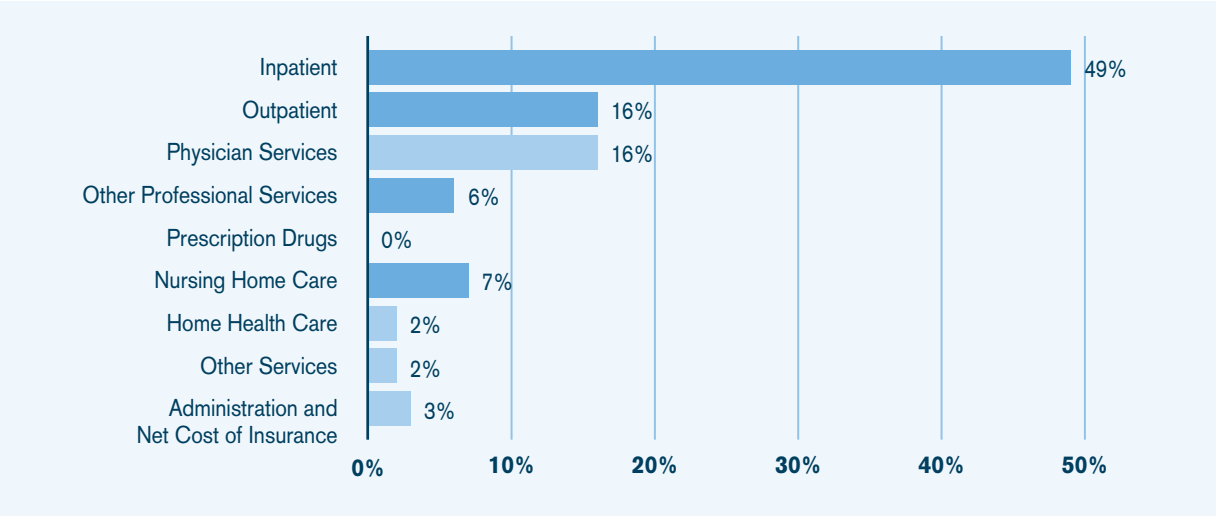
TABLE 8: Estimated Medicare Expenditures by Service Category in Maryland

SERVICE CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$4,565**	**100%**	**$5,863**	**100%**	**$6,323**	**100%**
Inpatient	2,157	47	2,802	48	3,014	48
Outpatient	558	12	756	13	838	13
Physician Services	995	22	1,213	21	1,269	20
Other Professional Services	191	4	265	5	291	5
Prescription Drugs	5	0	8	0	12	0
Nursing Home Care	264	6	345	6	383	6
Home Health Care	129	3	148	3	171	3
Other Services	99	2	133	2	136	2
Administration and Net Cost	166	4	193	3	210	3

NOTE: 0% indicates < 0.5%.

Expenditures for inpatient hospital care accounted for 49 percent of the growth in all Medicare expenditures in Maryland from 2001 to 2005 (Figure 28). By comparison, growth in expenditures for outpatient hospital care and physician services each accounted for 16 percent of the increase in Medicare expenditures.

FIGURE 28: Estimated Share of Increase in Medicare Expenditures by Service Category in Maryland, 2001–2005



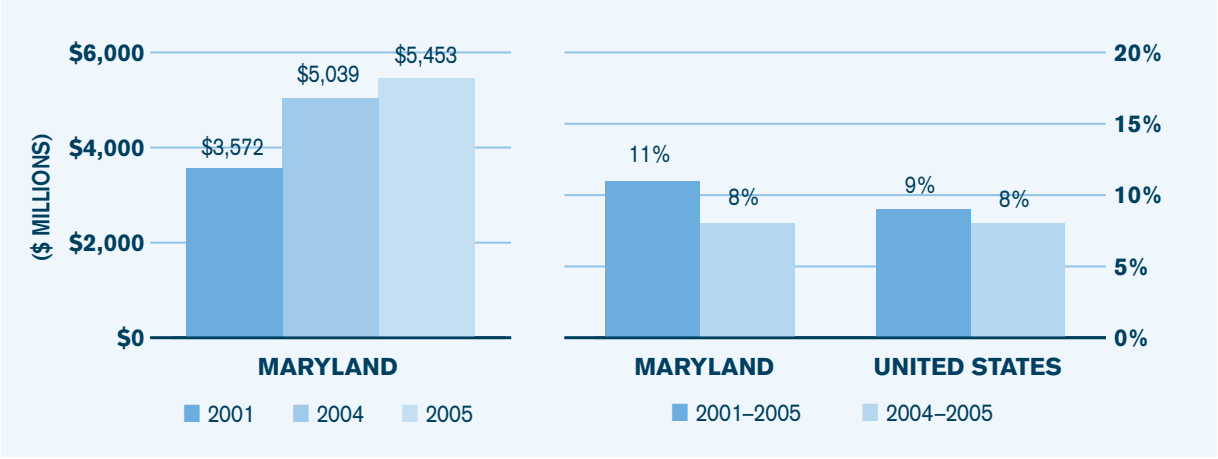
NOTE: Dark shading indicates services that have an increased share of expenditures in 2005 from 2001. Light shading indicates services that have the same or decreasing share of expenditures in 2005 from 2001. Due to rounding, the increase or decrease in share of expenditures may not be reflected in Table 8 above.

In Maryland and nationally, Medicare expenditures for prescription drugs were negligible in 2005, prior to implementation of Medicare Part D. In 2006, Medicare spending overall, and for prescription drugs in particular, is expected to rise significantly. Beneficiaries in Maryland enrolled in Part D and Medicare Advantage plans in significant numbers in late 2005 to qualify for the prescription drug benefits that became available as of January 1, 2006. As of January 1, 2006, the Maryland Pharmacy Assistance Program (MPAP) no longer provides pharmacy coverage to persons eligible for Part D benefits.

MEDICAID EXPENDITURES

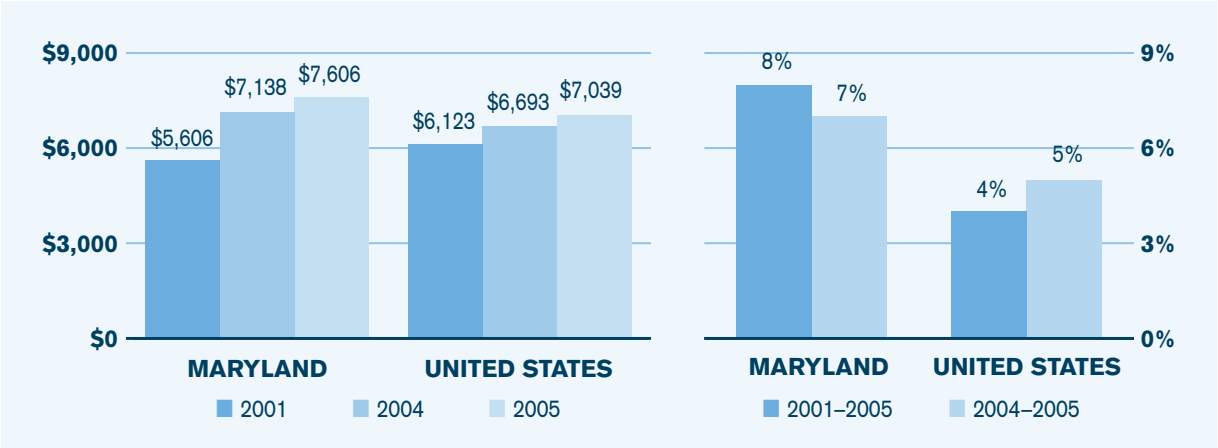
Medicaid expenditures in Maryland have grown d 2005, Medicaid spending in Maryland grew faster than the national average—averaging 11 percent per year in Maryland, compared with 9 percent nationally.

FIGURE 29: Estimated Medicaid Expenditures and Rate of Growth



While Medicaid enrollment has grown more slowly than the national average, costs per enrollee have grown faster. On a per enrollee basis, Medicaid expenditures in Maryland were about 8 percent higher than the national average in 2005—$7,606 in Maryland, compared with $7,039 nationally (Figure 30). From 2001 to 2005, per enrollee expenditures grew substantially faster than the national average—at 8 percent per year, compared with 4 percent nationally. The rate of growth in Maryland Medicaid expenditures per enrollee slowed to 7 percent from 2004 to 2005, but it continued to substantially exceed the growth in spending per Medicaid enrollee nationally (5 percent).

FIGURE 30: Estimated Per Enrollee Medicaid Expenditures and Rate of Growth, Maryland and U.S.



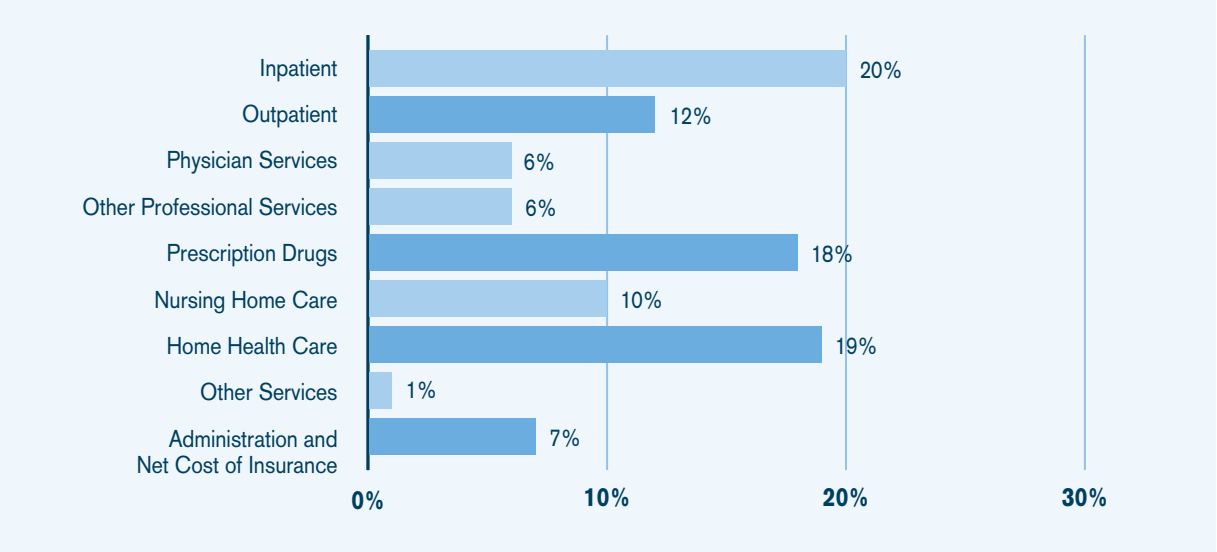
Nearly one-third of Medicaid expenditures in 2005 were for hospital care—including inpatient care (24 percent) and outpatient care (8 percent) (Table 9). The next largest block of Medicaid expenditures was for long-term care—including both nursing home care (19 percent) and home health care (13 percent). Overall, the share of Medicaid expenditures paid for institutional care in Maryland has declined significantly since 2001, when inpatient hospital care and nursing home care together accounted for 51 percent of Medicaid expenditures. In 2005, payments for institutional care accounted for 43 percent of Medicaid expenditures in Maryland.

TABLE 9: Estimated Medicaid Expenditures by Service Category in Maryland

SERVICE CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$3,572**	**100%**	**$5,039**	**100%**	**$5,453**	**100%**
Inpatient	953	27	1,266	25	1,330	24
Outpatient	226	6	382	8	453	8
Physician Services	229	6	320	6	348	6
Other Professional Services	380	11	453	9	498	9
Prescription Drugs	388	11	666	13	727	13
Nursing Home Care	853	24	1,010	20	1,041	19
Home Health Care	336	9	643	13	695	13
Other Services	23	1	41	1	42	1
Administration and Net Cost	183	5	258	5	320	6

While expenditures for prescription drugs remained a relatively small share of Medicaid expenditures in Maryland (13 percent), prescription drug expenditures account for a significant share of the growth in Medicaid spending. From 2001 to 2005, prescription drug expenditures accounted for 18 percent of the total growth in Medicaid spending in Maryland (Figure 31). By comparison, expenditures for inpatient hospital care and home health care, respectively, accounted for 20 percent and 19 percent of the increase in Medicaid spending from 2001 to 2005. To address the very fast growth in Medicaid expenditures for prescription drugs, Maryland obtained CMS approval in June 2005 to participate in a multistate supplement rebate pooling agreement with Louisiana and West Virginia in order to leverage Medicaid expenditures for prescription drugs for the states' combined 1.3 million Medicaid enrollees.

FIGURE 31: Estimated Share of Increase in Medicaid Expenditures by Service Category in Maryland, 2001–2005

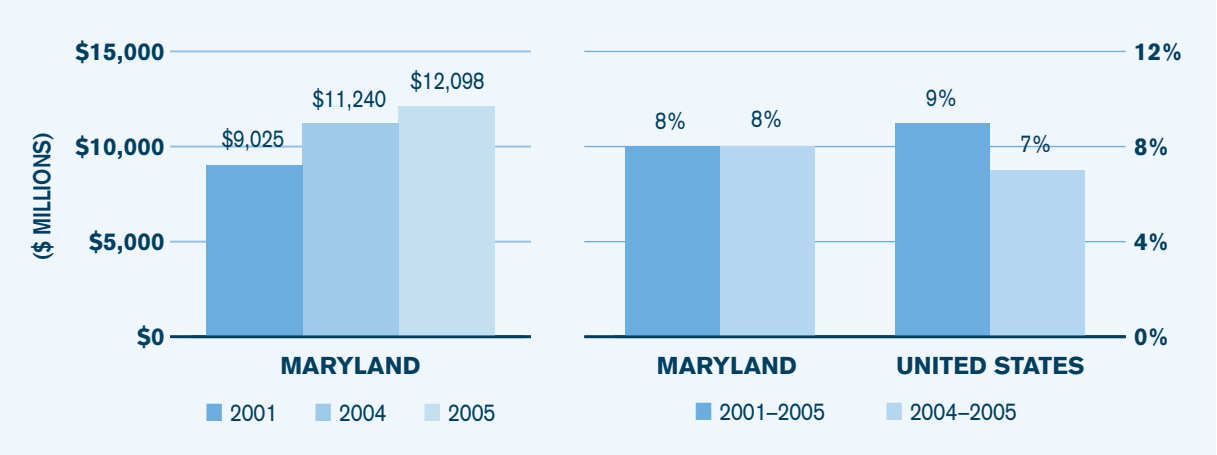


NOTE: Dark shading indicates services that have an increased share of expenditures in 2005 from 2001. Light shading indicates services that have the same or decreasing share of expenditures in 2005 from 2001. Due to rounding, the increase or decrease in share of expenditures may not be reflected in Table 9 above.

PRIVATE INSURANCE EXPENDITURES

Private insurers are the dominant payers for health care in Maryland. In 2005, private insurers in Maryland financed $12.1 billion in expenditures for health care (Figure 32). Private insurance expenditures in Maryland grew at an average annual rate of 8 percent per year from 2001 to 2005 and also from 2004 to 2005. In contrast, the growth in private insurance expenditures nationally averaged 9 percent per year from 2001 to 2005, but slowed to 7 percent from 2004 to 2005.

FIGURE 32: Estimated Private Insurance Expenditures and Rate of Growth

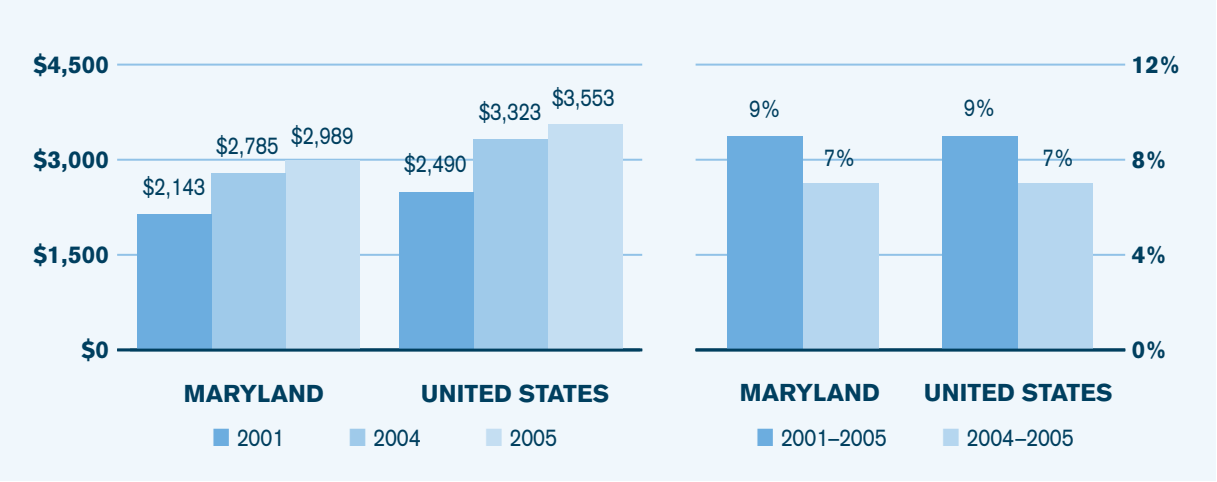


On a per capita basis, private insurance expenditures in Maryland remained lower than the national average in 2005 (Figure 33). This difference may reflect a number of factors—including privately insured payment and service utilization levels. In Maryland—and in contrast to national estimates—private sector rates in 2004 and 2005 were about equal to Medicare payment rates.[14] [15] Both the long-term trend and recent growth in per capita private insurance expenditures in Maryland mirrored the national average: private insurance expenditures increased at an average rate of 9 percent per year from 2001 to 2005, and slowed to 7 percent from 2004 to 2005.

[14] Maryland Health Care Commission (2005), *Practitioner Spending and Utilization Through 2004* (http://mhcc.maryland.gov/health_care_expenditures/exputil2005/report_web.pdf).

[15] The Medicare Payment Advisory Commission (MedPAC) estimated that Medicare payment rates for physician services were approximately 83 percent of private insurance rates for comparable services in 2004 (the most recent estimate available)—slightly higher than in 2002 and 2003 (81 percent), but lower than in 2001 (84 percent). MedPac (2006), *Report to the Congress: Medicare Payment Policy* (http://www.medpac.gov/publications/congressional_reports/Mar06_Ch02b.pdf).

FIGURE 33: Estimated Per Enrollee Private Insurance Expenditures and Rate of Growth, Maryland and U.S.



In 2005, three categories of services accounted for nearly 60 percent of private insurance expenditures in Maryland: inpatient hospital care (22 percent), physician services (21 percent), and prescription drugs (16 percent) (Table 10). However, the administration and net cost of private insurance accounted for 17 percent of private insurance expenditures in 2005, up from 16 percent in 2001 but nevertheless remarkably stable over the period. Stability in the net cost of private insurance—in contrast to the underwriting cycle that historically has characterized health insurance markets—may be one result of the growing concentration of insurers in Maryland and in other states, as well as the growing influence of for-profit insurers that prefer to avoid variation in their profits.[16]

TABLE 10: Estimated Private Insurance Expenditures by Service Category in Maryland

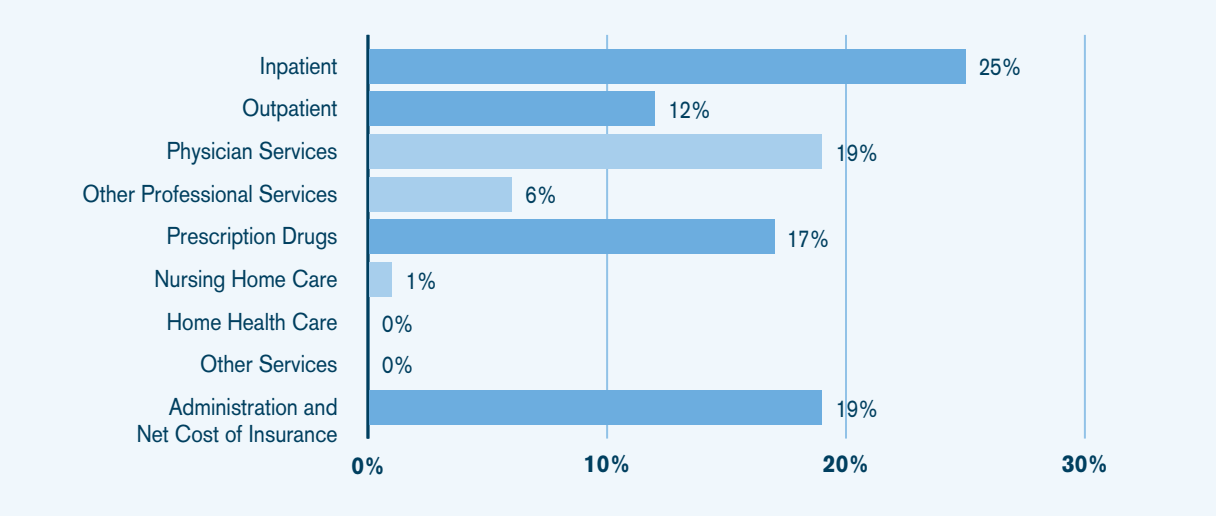
SERVICE CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$9,025**	**100%**	**$11,240**	**100%**	**$12,098**	**100%**
Inpatient	1,920	21	2,482	22	2,690	22
Outpatient	990	11	1,223	11	1,374	11
Physician Services	1,913	21	2,424	22	2,503	21
Other Professional Services	1,094	12	1,205	11	1,280	11
Prescription Drugs	1,346	15	1,750	16	1,881	16
Nursing Home Care	135	1	148	1	151	1
Home Health Care	97	1	85	1	87	1
Other Services	42	0	45	0	47	0
Administration and Net Cost	1,488	16	1,877	17	2,086	17

NOTE: 0% indicates < 0.5%.

[16] Maryland Health Care Commission (2005), *Spotlight on Maryland: Health Insurance Premiums, the Underwriting Cycle, and Carrier Surpluses* (http://mhcc.maryland.gov/spotlight/health_ins_prem_spotlight_ 0305.pdf).

The increase in private insurance expenditures from 2001 to 2005 is largely explained by increases in the cost of major covered services, as well as increases in expenditures for the administration and net cost of insurance. Growth in inpatient hospital costs accounted for 25 percent of the growth in private insurance expenditures from 2001 to 2005, followed by growth in expenditures for physician services (19 percent), administration and net cost of insurance (19 percent), prescription drugs (17 percent), and hospital outpatient care (12 percent) (Figure 34).

FIGURE 34: Estimated Share of Increase in Private Insurance Expenditures by Service Category in Maryland, 2001–2005

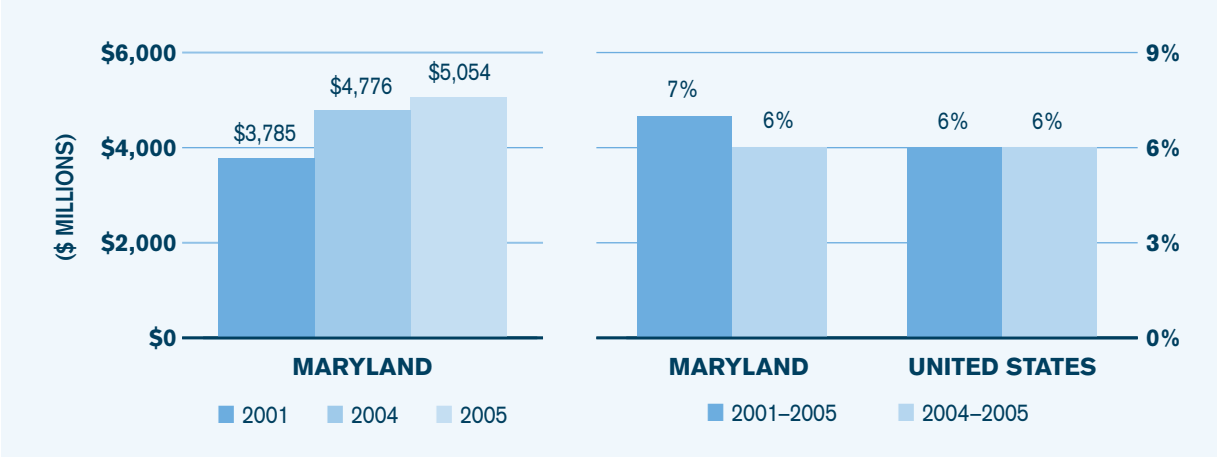


NOTE: Dark shading indicates services that have an increased share of expenditures in 2005 from 2001. Light shading indicates services that have the same or decreasing share of expenditures in 2005 from 2001. Due to rounding, the increase or decrease in share of expenditures may not be reflected in Table 10 above. 0% indicates < 0.5%.

OUT-OF-POCKET EXPENDITURES

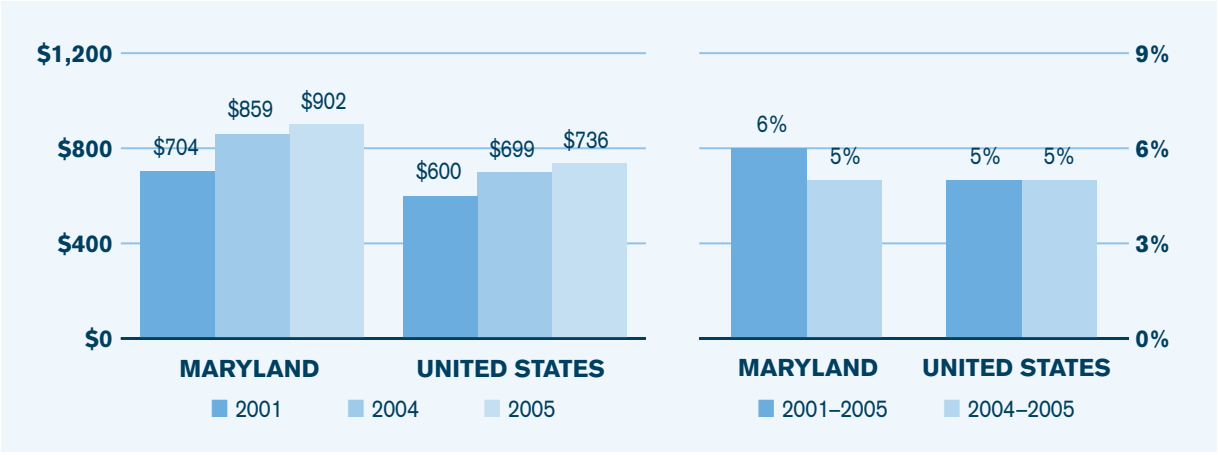
In 2005, Marylanders paid approximately $5.1 billion for health care out-of-pocket (Figure 35). From 2001 to 2005, the growth in out-of-pocket spending in Maryland exceeded the national average. During that period, total out-of-pocket expenditures increased at an average rate of 7 percent per year, compared with the national average of 6 percent per year. However, from 2004 to 2005, growth in out-of-pocket expenditures in Maryland slowed to 6 percent, approximately the national average. Much of the increase in out-of-pocket expenditures for health care is probably related to increased cost-sharing for insured services—especially prescription drugs—as well as gradual growth in the number of Marylanders who are uninsured. Additionally, the increasing popularity of services not covered by health insurance—such as laser eye surgery, plastic surgery, cosmetic dermatology, and cosmetic dentistry—have contributed to higher levels of out-of-pocket spending.

FIGURE 35: Estimated Out-of-Pocket Expenditures and Rate of Growth



On a per capita basis, Marylanders continue to spend substantially more out-of-pocket for health care than the national average. In 2005, Marylanders spent out-of-pocket approximately 23 percent more per capita than the national average, an average of $902 per person in Maryland compared with $736 nationally (Figure 36). Nevertheless, because personal income per capita in Maryland is nearly 22 percent above the national average, Marylanders spend approximately the same percent of their income on out-of-pocket spending (2 percent) as do other Americans.[17] Maryland's per capita out-of-pocket expenditures grew faster than the national average from 2001 to 2005 (by 6 percent per year, versus the national average of 5 percent per year), but dropped to the national average (5 percent) from 2004 to 2005. Similar to the nation as a whole, spending out-of-pocket for health care in Maryland has grown faster than per capita personal income. From 2001 to 2005, personal per capita income in Maryland increased at an average annual rate of 4 percent.[18]

FIGURE 36: Estimated Per Capita Out-of-Pocket Expenditures and Rate of Growth, Maryland and U.S.



[17] U.S. Department of Commerce, Bureau of Economic Analysis, *Annual State Personal Income*. (http://www.bea.gov/bea/regional/spi/).
[18] U.S. Department of Commerce, Bureau of Economic Analysis, *ibid*.

In Maryland, expenditures for prescription drugs and other professional services account for more than half of all out-of-pocket expenditures. In 2005, expenditures for prescription drugs and other professional services accounted for 56 percent of consumer out-of-pocket expenditures (Table 11). Hospital and physician services accounted for an additional 19 percent of out-of-pocket expenditures, while long-term care (nursing home and home health care) accounted for 17 percent.[19] Since 2001, expenditures for three types of services—outpatient hospital care, prescription drugs, and home health care—have increased as a percentage of out-of-pocket expenditures. Together, these services accounted for an additional 5 percent of total out-of-pocket expenditures in 2005 (37 percent) compared with 2001 (32 percent), while the relative amounts expended for physician services and other professional services declined.

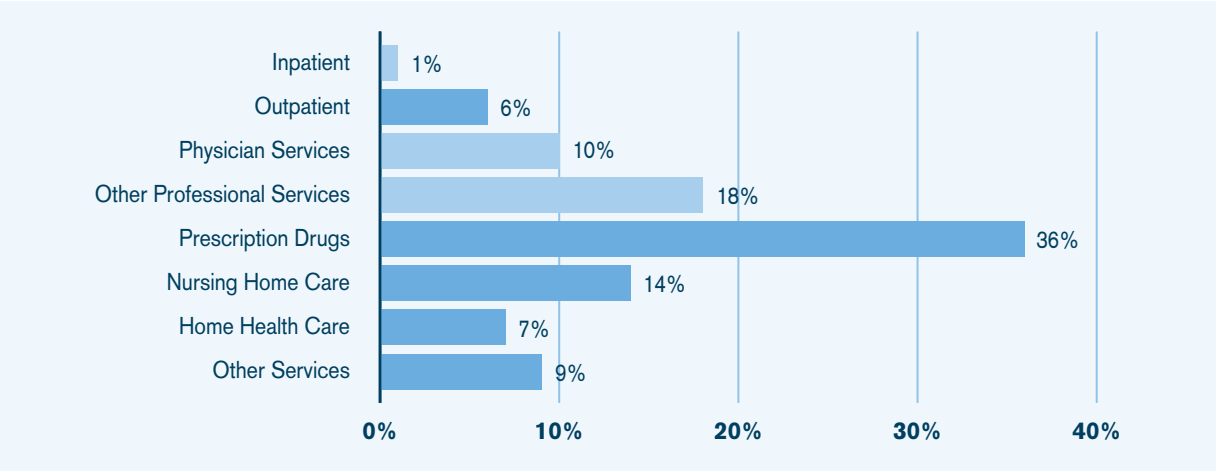
TABLE 11: Estimated Out-of-Pocket Expenditures by Service Category in Maryland

SERVICE CATEGORY	2001 Expenditures ($ millions)	2001 Percent of Total	2004 Expenditures ($ millions)	2004 Percent of Total	2005 Expenditures ($ millions)	2005 Percent of Total
TOTALS	**$3,785**	**100%**	**$4,776**	**100%**	**$5,054**	**100%**
Inpatient	52	1	56	1	60	1
Outpatient	169	4	213	4	240	5
Physician Services	527	14	635	13	659	13
Other Professional Services	1,189	31	1,337	28	1,417	28
Prescription Drugs	945	25	1,301	27	1,404	28
Nursing Home Care	478	13	640	13	652	13
Home Health Care	116	3	190	4	205	4
Other Services	309	8	405	8	417	8

Prescription drugs accounted for more than one-third (36 percent) of the increase in Marylanders' out-of-pocket expenditures for health care from 2001 to 2005—far outpacing the increase in out-of-pocket expenditures for any other service type (Figure 37). The increase in expenditures for physician and other professional services together accounted for 28 percent of increased out-of-pocket spending over that period, while increased expenditures for long-term care (nursing home and home health care) accounted for 21 percent.

[19] By convention, expenditures for health insurance (including administration and the net cost of insurance) are not included in out-of-pocket expenditures in order to avoid double-counting health expenditures.

FIGURE 37: Estimated Share of Increase in Out-of-Pocket Expenditures by Service Category in Maryland, 2001–2005



NOTE: Dark shading indicates services that have an increased share of expenditures in 2005 from 2001. Light shading indicates services that have the same or decreasing share of expenditures in 2005 from 2001. Due to rounding, the increase or decrease in share of expenditures may not be reflected in Table 11 above.

PROSPECTS FOR CHANGE: 2007 THROUGH 2009

A third consecutive year of slower growth in total health care spending suggests there may be reason for optimism about future spending growth. However, significant reasons for concern remain. First, health care costs remain high, and cost growth still exceeds growth in wages and personal income—even as worker productivity has increased. It is likely that health care costs will continue to depress income growth and burden private and public resources, causing further erosion of employer-based coverage, growing need for public insurance programs, and increasing reliance on safety net providers and uncompensated care.

All the factors that historically have driven health care expenditure increases largely remain in place. Most prominently, these include the emergence of new technologies and the lowering of clinical thresholds for care. Both increase the amount and typically also the cost of care that the population uses and will remain significant features of the U.S. health care system for the foreseeable future. However, while they are likely to continue to drive the cost of care, they also are driving increased attention to measures that curb or avoid the use of care—including consumer information, cost-sharing, information systems that improve efficiency, the development of protocols for managing high-cost care, and greater attention to maintaining and improving population health.

In the remainder of this section, factors that may affect spending from 2007 through 2009 are examined by sector and payer category.

HOSPITAL SERVICES Nationally, growth in the use of inpatient and outpatient hospital care more than offset slower growth in prices in 2005.[20] In Maryland, expenditures for hospital services grew faster than the national average, both overall and on a per capita basis. Under current forecasts developed by the Health Services Cost Review Commission (HSCRC), costs per case are expected to continue growing at 6 to 7 percent per year from 2007 to 2009.[21]

Hospital services are likely to remain a strong driver of health care spending in the state. If the current annual rate of growth in utilization continues (1.5 to 2.5 percent per year), the rate of growth in expenditures for inpatient hospital care in Maryland could reach 9 percent. Expenditures for outpatient care may continue to grow at an even faster rate—in 2005, nearly twice as fast as expenditures for inpatient care. Rising hospital costs reduce access to health care coverage by increasing the prices of private insurance and public programs.

New opportunities to constrain growth in expenditures for hospital services may be difficult to find. In April 2006, HSCRC reached a policy decision to widen by 1.1 percent the difference in case-mix adjusted costs per case in Maryland hospitals relative to the United States from 2007 through 2009. This now appears less likely to occur, as an updated forecast has suggested that the implementation of currently approved updates would increase case-mix adjusted costs more rapidly in Maryland than in the United States, causing Maryland cost performance relative to the United States to deteriorate. These increases also would drive higher spending in the Medicaid program, which, like other payers in Maryland, reimburses hospitals on the basis of HSCRC rates.

---

[20] A. Catlin et al. (2007), "National Health Spending in 2005: The Slowdown Continues." *Health Affairs* 26, no. 1 (2007): 142-153.

[21] Health Services Cost Review Commission, "Staff Recommendation Regarding FY 2006 Case Mix Distributions and Adjustments Related to the 1.0% Inpatient to Outpatient Shift", Baltimore Maryland, January 2007.

PRACTITIONER SERVICES Continued growth in expenditures for practitioner services could reappear as a major driver of total health care spending in the 2007 through 2009 time frame. In 2001 through 2005, spending for physician services grew about 6 percent annually, despite fee increases that averaged only about 1 percent annual growth in both the private sector and Medicare over that same period. Growing use of services per patient was the primary driver of the spending increase.[22] Had fee increases tracked with input costs (as measured by the Medicare Economic Index), fees would have increased by more than 12 percent from 2001 through 2005 as opposed to the cumulative 6 percent increase that MHCC has reported.[23] Recent evidence suggests that private payers and Medicare will be less able to hold the line on fee increases over the next several years.

Attempts by a major payer to reduce fees for advanced imaging services and complex surgeries met with stiff resistance in the summer of 2006, and physician groups have made reimbursement a top priority in their legislative agenda for 2007.[24] Although price increases in certain inputs such as professional liability expense have slowed, staffing and other practice expenses have continued to increase.[25] Many practices are looking at major investments in electronic medical records and clinical information systems, forming the foundation for a standard of specialty care.

In the public sector, widespread dissatisfaction exists with Medicare physician payment policies, particularly with the formula used to update physician fees. Changes to Medicare fee levels could trigger a significant increase in Medicare spending. But they also would have a cascading impact on Medicaid and private payers that directly or indirectly peg their fee schedules to the Medicare Fee Schedule. The Medicaid program in Maryland currently is raising professional fees, with the goal of reaching 80 to 100 percent of Medicare rates by 2009. As a result, growth in Medicare's physician payment fees would add upward pressure on Medicaid spending for physician services. Mechanisms to slow this spending, including pricing transparency, growth in value-oriented insurance products, financial reward of high performance by practices, and more effective management of chronically ill and vulnerable populations are unproven or just getting underway. If either legislation or market pressure reduces restraint on fees, physician services could drive higher health care spending.

PRESCRIPTION DRUG SPENDING In Maryland and the United States, weaker growth in expenditures for prescription drugs helped to constrain health care expenditure growth in 2005. Additional opportunities to constrain prescription drug expenditures are tied to patent expirations for brand name drugs, which allow for more generic substitutions. Ambien®, the leading sedative-hypnotic for insomnia treatment, lost its patent protection in late 2006, although a brand extension in the form of Ambien CR® could reduce possible savings. Generic versions of two leading statin drugs (Pravachol® and Zocor®) entered the market in 2005 and 2006. As statins are a leading cost driver for prescription drugs, generic statins offer consumers

[22] Maryland Health Care Commission (2006), *Practitioner Spending and Utilization Through 2004* (http://mhcc.maryland.gov/health_care_expenditures/exputil2005/report_web.pdf).

[23] Maryland Health Care Commission. (2006), *op cit.*

[24] M.W. Salganik (May 11,2006), "Doctors ask state probe of cuts in pay by CareFirst", *Baltimore Sun*, http://www.baltimoresun.com/news/health/bal-bz.doctors11may11,1,3903585.story.

[25] In contrast to average premium increases of 28 percent in 2004 and 33 percent in 2005, premiums in 2007 are expected to drop 8 percent, reflecting a decline in malpractice claims in Maryland and nationally. M.W. Salganik (December 15, 2006), "Physicians' Insurer to Lower Premiums," *Baltimore Sun* (http://www.baltimoresun.com/news/health/bal-bz.malpractice15dec15,1,5001683.story?page=2&cset=true&ctrack=1).

and purchasers new cost-saving opportunities. A generic version of Zoloft®, one of the most commonly prescribed drugs for the treatment of depression, will become available in 2007.

A slowdown in the number of drug approvals by the Food and Drug Administration (FDA) will further reduce growth in prescription drug spending. Recent recalls of several blockbuster drugs due to safety concerns has made the FDA more cautious in approving drugs. In 2005, the FDA approved 25 new molecular entities, down from 37 in 2004. New drugs slated for approval by the FDA in the next several years will likely have less of an impact on spending, as most will treat conditions that are already covered by one or more existing medications. The absence of new blockbusters (drugs with more than $1 billion in annual sales) will contribute to slowing the growth in overall prescription drug spending.

Limitations in Maryland law could have a modest impact on the growth in prescription spending. Insurers and HMOs that sell in the state are prohibited from offering enrollees incentives for use of mail-order pharmacies. Pharmacy benefit managers that operate mail-order pharmacies claim significant savings over retail store pharmacies. MHCC estimates that such savings might exist, but they may be smaller than claimed, in part because the retail store and mail-order segments of the prescription drug market are becoming more integrated.[26]

MEDICARE Important changes in Medicare include changes in the physician payment formula, prescription drugs expansion (Part D), and increased enrollment in managed care. Major changes to physician reimbursement seem inevitable, as concern about the willingness of the Congress to live with the Medicare Fee Schedule methodology has grown. However, the implementation of Medicare Part D, which finances a significant share of Medicare enrollees' expenditures for prescription drugs, may represent the single largest change in expenditure patterns in Maryland in 2006 and in coming years. As a result, out-of-pocket expenditures for prescription drugs—accounting for 34 percent of total expenditures for prescription drugs in Maryland in 2005—will drop substantially as Medicare expenditures rise. In addition, Medicaid spending, which historically has included significant payments for prescription drugs used by low-income elderly and disabled Medicare beneficiaries, will decline.

Increased enrollment in Medicare Advantage plans may affect expenditure patterns, although in Maryland enrollment in these plans remains relatively low. By December 2005, an estimated 4.3 percent of Medicare beneficiaries in Maryland had enrolled in Medicare Advantage plans, well below the national rate (12.5 percent), despite greater availability of Medicare Advantage plans in Maryland than in many states.[27] By

[26] A study on mail-order pharmacy use found that removing retail pharmacy parity protections in Maryland law would reduce insured patients' out-of-pocket expenditures by 2 percent to 6 percent, depending on whether payers mandated or merely offered incentives to use mail-order pharmacies. See *Mail-Order Purchase of Maintenance Drugs: Impact on Consumers, Payers, and Retail Pharmacies*, Maryland Health Care Commission, December 2005. http://mhcc.maryland.gov/legislative/mailorderrpt.pdf

[27] M. Gold and S. Peterson (July 2006). *Analysis of the Characteristics of Medicare Advantage Plan Participation*. Final report to the Assistant Secretary for Planning and Evaluation, U.S. Department of Health and Human Services. Washington, DC: Mathematica Policy Research, Inc.

November 2006, the percentage of Medicare beneficiaries enrolled in Medicare Advantage plans reached 4.5 percent in Maryland and 16.3 percent nationally.[28]

MEDICAID Spending under the Medicaid program increased at an annualized rate of 11 percent from 2001 to 2005, but by 8 percent from 2004 to 2005. The rate of growth in the Medicaid program has slowed in each of the past three years. A looming state budget deficit could further slow growth in the program over the next three years.

Actions by the federal government could reduce eligibility and lead to lower spending, although not necessarily for desirable reasons. New eligibility documentation requirements have been mandated under the federal Deficit Reduction Act of 2005 (DRA). Effective July 1, 2006, citizens applying for or renewing their Medicaid coverage must provide "satisfactory documentary evidence of citizenship or nationality."[29] No federal matching funds are available for services provided to individuals who declare they are citizens or nationals unless the state obtains satisfactory evidence of their citizenship or determines that they are subject to a statutory exemption that applies to individuals eligible for Supplemental Security Income and children in foster care. Virginia, New Hampshire, Wisconsin, Iowa, and Louisiana already have reported declines in enrollment. In Virginia, more than 12,000 children have dropped from Medicaid rolls since July 2006, although it is too early to determine if these declines are permanent or temporary.[30]

The Congress must reauthorize the State Children's Health Plan (SCHIP) in 2007. SCHIP has 6 million beneficiaries nationwide and is financed with a $5 billion annual allocation. Federal government estimates indicate that maintaining the current funding level could result in at least 1.5 million children losing coverage by 2012, but addressing the funding gap could cost an additional $13 billion to $15 billion over five years. If Congress fails to provide full funding for the program, Maryland would face the difficult choice of dropping coverage or financing a portion of the program with 100 percent state funds.

On the other side of the age spectrum, it seems likely that Medicaid spending for nursing home services will climb as the baby-boom population ages and the need for long-term care services grows. From 2001 to 2005, annual growth in Medicaid spending for nursing home care has been about 5 percent, although costs per patient have grown more rapidly. In anticipation of higher future total spending, the Medicaid administration has sought a 1915(c) waiver to modify the delivery of long-term care services, covering home and community-based services that individuals might need to avoid institutionalization. The Centers for Medicare & Medicaid Services (CMS) has not yet approved Maryland's waiver application. Without approval, it is likely that Medicaid spending for nursing home and hospital services will rise more rapidly than if the 1915(c) waiver were in place.

---

[28] The Kaiser Family Foundation Medicare Health and Prescription Drug Plan Tracker, forthcoming (www.kff.org). Mathematica Policy Research, Inc. analysis of CMS data available at http://www.cms.hhs.gov/PrescriptionDrugCovGenIn/02_EnrollmentData.asp. The calculation of November 2006 penetration was based on December 2005 estimates of the population eligible for Medicare, the most recent available.

[29] DRA and implementing federal regulations dictate that originals of a U.S. passport or a birth certificate are preferred documents, although a number of other documents may be permitted as a last resort.

[30] *USA Today*, Documentation rules for Medicaid penalize legal residents, some states say, January 9, 2007 Washington, DC.

Finally, in 2007, the Medicaid administration will seek removal of day limits on inpatient hospital care, leading to higher spending for hospital care. Because day limits establish maximum lengths of stay on Medicaid hospital stays, they push some of the cost of hospital services provided to Medicaid enrollees into uncompensated care. Conversely, as uncompensated care is rolled into hospital rates, other payers and Medicare absorb the expense of this Medicaid policy. However, while removing day limits will increase Medicaid spending, it probably will not increase total hospital spending as uncompensated care for Medicaid patients will decrease.

PRIVATE PAYERS Although the proportion of Marylanders with private health insurance coverage remains above the national average, it seems likely it will continue to erode in Maryland and nationally, absent a significant change in public policy to bolster employer-based coverage, individual coverage, or both. The percentage of the population under age 65 with private coverage has declined steadily—from 82 percent (averaged across 2000 and 2001) to 75 percent (2004-2005)—as employer-based coverage has declined.[31]

Among those with coverage, rising enrollment in high-deductible plans may also alter the level and distribution of privately insured health care expenditures. These products decrease the proportion of expenditures that private insurance pays and increase the proportion paid out-of-pocket for insured health care services.[32] Effective in 2007, increased limits on tax-exempt contributions and other provisions affecting health savings accounts (HSAs) may encourage higher-income Marylanders to consider HSA-qualified high-deductible plans in a new light.[33] However, these tax savings are less likely to appeal to individuals at lower income levels.

Concern about eroding coverage has sparked renewed interest in some states for requiring residents to purchase private health insurance or enroll in public programs. Significant reform has been enacted or proposed in a number of states (including Maine, Massachusetts, Vermont, Pennsylvania, and California) and developed incrementally in many others. These alterations could change the picture of private insurance significantly, and also the share of expenditure financed by private insurance. The formation of potentially significant new alliances between labor and large employers to direct attention to this problem demonstrates the growing urgency that both workers and employers place on resolving the problem of access to affordable coverage.[34]

---

[31] Maryland Health Care Commission (2007a), *op cit.*

[32] The Congress of the United States, Congressional Budget Office (December 2006), *Consumer-Directed Health Plans: Potential Effects on Health Care Spending and Outcomes* (http://www.cbo.gov/ftpdocs/77xx/doc7700/12-21-HealthPlans.pdf).

[33] The Tax Relief and Health Care Act of 2006 increased tax-deductible contributions to HSAs from the lesser of the plan's deductible or $2,700 (for single coverage, or $5,450 for family coverage). In 2007, contribution limits are $2,850 for single coverage or $5,650 for family coverage, even if the plan's deductible is less. In addition, the new law permits a one-time tax-exempt transfer of funds from a flexible spending account (FSA) or health reimbursement accounts (HRAs) to an HSA, as well as a one-time tax-exempt direct transfer of funds from an individual retirement account (IRA) to an HSA up to the HSA annual contribution limit. HSA distributions are tax-exempt, while funds in traditional IRAs are taxed as personal income when withdrawn.

[34] Michael Barbaro and Robert Pear, "Wal-Mart and a Union Unite, at Least on Health Policy," *New York Times*, New York, NY, February 8, 2007.

METHODS

The Methods section describes the data sources and methods used to produce the Maryland and national estimates provided in this report. This section includes three parts: first, a description of methods and sources for the Maryland expenditures, followed by methods and sources for national expenditures, and finally, the methods and sources used to produce enrollment estimates used in per capita estimates.

MARYLAND EXPENDITURES

MEDICARE Maryland Medicare expenditures are estimated separately for the Original Medicare program and the Medicare Advantage program, and then the two results are aggregated. Expenditures for Original Medicare are estimated from claims data provided by the Centers for Medicare & Medicaid Services (CMS). The claims data include information on expenditures by the type of service (service category). Claims expenditures are aggregated by service category. For the Medicare Advantage program, the Maryland Insurance Administration (MIA) provided total expenditures for Maryland residents by insurer. For a few small insurers, the expenditures are estimated based on their enrollment and the average monthly payment for all Medicare Advantage plans of the same type. Both the enrollment and payment information are available at the CMS Web site. Expenditures by insurer are aggregated and allotted to service categories based on estimates provided by CMS. Administration costs are estimated from the National Health Expenditure Accounts data (for Original Medicare) and from the MIA reports (for Medicare Advantage).

MEDICAID Maryland Medicaid expenditures are estimated from Management Information Systems (MMIS) reports by line item provided by the Maryland Department of Health and Mental Hygiene (DHMH). Medicaid HealthChoice premiums are allocated to service categories based on reports produced by DHMH using expenditure reports from the individual insurers. Administrative expenditures are provided by DHMH for the Medicaid Traditional program and the HealthChoice program.

OTHER GOVERNMENT Maryland expenditures for Other Government programs (Maryland public programs other than Medicaid, Department of Corrections, Veterans Administration, CHAMPUS/TRICARE) are collected directly from the administrators for the individual programs.

PRIVATE INSURANCE Maryland total expenditures for private insurance (including self-insurance) are produced in four steps:

1. From the MIA annual filings by insurers in Maryland, we estimate the amount of Direct Losses Incurred for Health Care, excluding the Federal Employees Health Benefits Program (FEHBP). This represents the amount of expenditures for insurers reporting to MIA for lives covered in Maryland (not residents of Maryland).

2. For FEHBP, we estimate expenditures from data received from the U.S. Office of Management and Budget.

3. We estimate expenditures of persons in self-insured firms using data from the Maryland Medical Care Data Base (MCDB), which is a claims-based system including a designation of self-insurance.

4. We estimate a NET adjustment that accounts for Maryland residents not covered in steps 1 and 2 because they work outside Maryland, minus non-Maryland residents included in steps 1 and 2. This adjustment is based on the estimates of persons working in Maryland and employed outside the state, and persons from outside Maryland who work in the state, obtained from the Census Bureau's American Community Survey.

Expenditures are allocated to service categories, applying a method for estimating state expenditures developed by the staff at the Agency for Healthcare Research and Quality (AHRQ) utilizing the Medical Expenditure Panel Survey (MEPS) data. These estimates from the MEPS are adjusted to the current year using the change in per capita expenditures from three sources: the Maryland Health Services Cost Review Commission for hospital categories; the MCDB for practitioner categories; and the MCDB prescription drug claims for the prescription drug category.

Administration and Net Cost of Insurance is estimated from the MIA annual filings data.

OUT-OF-POCKET Using MEPS data for a group of states selected as Maryland-like, an estimate of out-of-pocket to total expenditures is calculated by service category and insurance coverage/age category. This ratio is then weighted by the actual Maryland population (from the Current Population Survey) to produce a ratio of out-of-pocket expenditures to total expenditures. This ratio is used to develop an estimate of out-of-pocket expenditures among Maryland residents.

NATIONAL EXPENDITURES

Estimates for the nation shown in this report are estimated using the National Health Expenditure (NHE) accounts data estimates and projections by service category and payer. Data for 2001 and 2004 are estimated, and data for 2005 are projected. See http://www.cms.hhs.gov/NationalHealthExpendData/ for more infor-

mation on the National Health Expenditures projection data. The NHE categories are aggregated by the Maryland State Health Expenditures' payer and service categories for comparison to Maryland estimates in this report. Because of this aggregation, selected NHE categories/payers are excluded and therefore the totals may differ from total NHE account totals.

ENROLLMENTS/POPULATIONS

Populations for Maryland and the nation are from the Census Bureau's Population Estimates program (http://www.census.gov/popest/estimates.php). Medicare (http://www.cms.hhs.gov/MedicareEnrpts/) and Medicaid (http://www.cms.hhs.gov/MedicaidDataSourcesGenInfo/) enrollments are from the CMS Web site. Private insurance enrollment estimates are two-year averages from the Current Population Survey.

SUPPORTING TABLES

TABLE 12A: Health Care Expenditures in Maryland by Expenditure Component and Source of Payment, 2005

EXPENDITURE COMPONENTS	GOVERNMENT SECTOR					PRIVATE SECTOR		TOTAL EXPENDITURES
	Medicare	Medicaid Total	Medicaid Traditional	Medicaid HealthChoice	Other Government	Private Coverage	Out-of-Pocket	
TOTAL HEALTH EXPENDITURES	**$6,322,970**	**$5,453,451**	**$3,574,603**	**$1,878,848**	**$1,242,020**	**$12,098,490**	**$5,053,655**	**$30,170,585**
Hospital Services								
Inpatient	3,013,697	1,329,948	667,231	662,717	269,438	2,690,254	60,358	7,363,695
Outpatient	837,525	453,198	150,696	302,502	68,953	1,373,610	239,664	2,972,949
Physician Services	1,269,068	348,097	90,735	257,363	137,472	2,503,114	659,071	4,916,823
Other Professional Services	290,758	497,731	386,969	110,762	509,175	1,279,762	1,417,103	3,994,528
Prescription Drugs	11,962	727,168	523,060	204,108	67,434	1,880,529	1,404,024	4,091,117
Nursing Home Care	383,407	1,040,581	963,589	76,992	63,601	150,869	651,564	2,290,022
Home Health Care	170,811	694,628	694,628	n/a	8,637	87,098	205,247	1,166,421
Other Services	135,654	42,478	42,478	n/a	20,046	47,320	416,624	662,123
Administration and Net Cost of Insurance	210,089	319,621	55,216	264,405	97,263	2,085,934	n/a	2,712,906

TABLE 12B: Health Care Expenditures in Maryland by Expenditure Component and Source of Payment, 2004

EXPENDITURE COMPONENTS	GOVERNMENT SECTOR					PRIVATE SECTOR		TOTAL EXPENDITURES
	Medicare	Medicaid Total	Medicaid Traditional	Medicaid HealthChoice	Other Government	Private Coverage	Out-of-Pocket	
TOTAL HEALTH EXPENDITURES	**$5,863,143**	**$5,038,775**	**$3,384,848**	**$1,653,927**	**$1,217,457**	**$11,239,833**	**$4,776,178**	**$28,135,385**
Hospital Services								
Inpatient	2,802,398	1,266,134	661,187	604,946	256,637	2,481,814	56,053	6,863,035
Outpatient	755,967	382,391	135,727	246,664	59,801	1,223,262	212,519	2,633,939
Physician Services	1,213,069	320,187	85,362	234,825	137,064	2,424,317	635,453	4,730,090
Other Professional Services	264,731	452,586	354,837	97,749	504,911	1,205,451	1,336,901	3,764,579
Prescription Drugs	7,749	666,007	484,557	181,450	67,416	1,749,561	1,300,638	3,791,371
Nursing Home Care	345,139	1,009,903	924,763	85,140	61,848	148,078	639,865	2,204,833
Home Health Care	147,983	643,091	643,091	n/a	9,962	85,131	190,052	1,076,220
Other Services	133,075	40,567	40,567	n/a	19,196	45,302	404,698	642,838
Administration and Net Cost of Insurance	193,030	257,910	54,756	203,153	100,623	1,876,917	n/a	2,428,481

TABLE 12C: Health Care Expenditures in Maryland by Expenditure Component and Source of Payment, 2001

EXPENDITURE COMPONENTS	GOVERNMENT SECTOR					PRIVATE SECTOR		TOTAL EXPENDITURES
	Medicare	Medicaid Total	Medicaid Traditional	Medicaid HealthChoice	Other Government	Private Coverage	Out-of-Pocket	
TOTAL HEALTH EXPENDITURES	**$4,564,979**	**$3,571,701**	**$2,392,998**	**$1,178,704**	**$1,027,968**	**$9,024,571**	**$3,785,405**	**$21,974,625**
Hospital Services								
Inpatient	2,157,419	953,268	503,048	450,220	185,939	1,919,588	52,049	5,268,262
Outpatient	558,449	226,195	92,435	133,760	54,109	990,005	169,000	1,997,758
Physician Services	995,269	228,873	52,454	176,420	107,308	1,912,536	526,918	3,770,905
Other Professional Services	190,526	380,454	311,189	69,265	445,226	1,094,429	1,189,444	3,300,078
Prescription Drugs	5,346	387,507	256,949	130,557	93,777	1,346,058	944,804	2,777,492
Nursing Home Care	264,115	853,361	764,895	88,466	29,034	135,252	477,977	1,759,739
Home Health Care	128,855	335,619	335,619	n/a	4,744	96,657	116,404	682,279
Other Services	99,476	23,372	23,372	n/a	20,090	42,495	308,808	494,241
Administration and Net Cost of Insurance	165,526	183,052	53,037	130,016	87,742	1,487,550	n/a	1,923,871

TABLE 13A: Rate of Growth in Health Care Expenditures in Maryland by Expenditure Component and Source of Payment, 2004–2005

EXPENDITURE COMPONENTS	GOVERNMENT SECTOR			PRIVATE SECTOR		TOTAL EXPENDITURES
	Medicare	Medicaid	Other Government	Private Coverage	Out-of-Pocket	
TOTAL HEALTH EXPENDITURES	**7.8%**	**8.2%**	**2.0%**	**7.6%**	**5.8%**	**7.2%**
Hospital Services						
Inpatient	7.5	5.0	5.0	8.4	7.7	7.3
Outpatient	10.8	18.5	15.3	12.3	12.8	12.9
Physician Services	4.6	8.7	0.3	3.3	3.7	3.9
Other Professional Services	9.8	10.0	0.8	6.2	6.0	6.1
Prescription Drugs	54.4	9.2	0.0	7.5	7.9	7.9
Nursing Home Care	11.1	3.0	2.8	1.9	1.8	3.9
Home Health Care	15.4	8.0	-13.3	2.3	8.0	8.4
Other Services	1.9	4.7	4.4	4.5	2.9	3.0
Administration and Net Cost of Insurance	8.8	23.9	-3.3	11.1	n/a	11.7

TABLE 13B: Rate of Growth in Health Care Expenditures in Maryland by Expenditure Component and Source of Payment, 2001–2005

EXPENDITURE COMPONENTS	GOVERNMENT SECTOR			PRIVATE SECTOR		TOTAL EXPENDITURES
	Medicare	Medicaid	Other Government	Private Coverage	Out-of-Pocket	
TOTAL HEALTH EXPENDITURES	**8.5%**	**11.2%**	**4.8%**	**7.6%**	**7.5%**	**8.2%**
Hospital Services						
Inpatient	8.7	8.7	9.7	8.8	3.8	8.7
Outpatient	10.7	19.0	6.2	8.5	9.1	10.4
Physician Services	6.3	11.1	6.4	7.0	5.8	6.9
Other Professional Services	11.1	6.9	3.4	4.0	4.5	4.9
Prescription Drugs	22.3	17.0	-7.9	8.7	10.4	10.2
Nursing Home Care	9.8	5.1	21.7	2.8	8.1	6.8
Home Health Care	7.3	19.9	16.2	-2.6	15.2	14.3
Other Services	8.1	16.1	-0.1	2.7	7.8	7.6
Administration and Net Cost of Insurance	6.1	15.0	2.6	8.8	n/a	9.0

TABLE 14: Enrollment and Populations, and Rate of Growth, Maryland and U.S., 2001, 2004, 2005

MARYLAND	2001	2004	2005	2001–2005	2004–2005
Population	5,379,591	5,561,332	5,600,388	1.0%	0.7%
Medicare Enrollees	654,607	684,795	686,746	1.2	0.3
Medicaid Enrollees	637,084	705,914	717,040	3.0	1.6
Private Insurance Enrollees	4,211,876	4,036,117	4,048,084	-1.0	0.3
UNITED STATES	**2001**	**2004**	**2005**	**2001–2005**	**2004–2005**
Population	285,107,923	293,656,842	296,410,404	1.0%	0.9%
Medicare Enrollees	39,149,152	40,792,298	41,003,057	1.2	0.5
Medicaid Enrollees	36,795,699	43,728,180	44,776,664	5.0	2.4
Private Insurance Enrollees	199,865,125	198,172,361	198,828,346	-0.1	0.3

4160 Patterson Avenue
Baltimore, Maryland 21215

Phone: 410-764-3570
Fax: 410-358-1236
www.mhcc.maryland.gov