

What's Ahead on the Trail? – The Economic Forecast for Independent Hospitals

State of the Union 2017

Health Care Advisory Board

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What's Ahead on the Trail? – The Economic Forecast for Independent Hospitals

State of the Union 2017

The best practices are the ones that work for **you.**SM

 research

 technology

 consulting

ROAD MAP

6

- 1 Unpacking the Political Process
 - 2 The Next Era of Health Reform
 - 3 Adapting Provider Strategy to New Market Realities
-

Health Care Squarely in the Hands of the GOP

Congress, Executive Branch, and Majority of States Now in Republican Control

33/50

Republican Governors

32/50

Republican-Led
Legislatures



Image: © 2017, United States Department of State

52/100

Senate Republicans

241/435

House Republicans



Majority of Americans Hold GOP Responsible for Health Care

64%

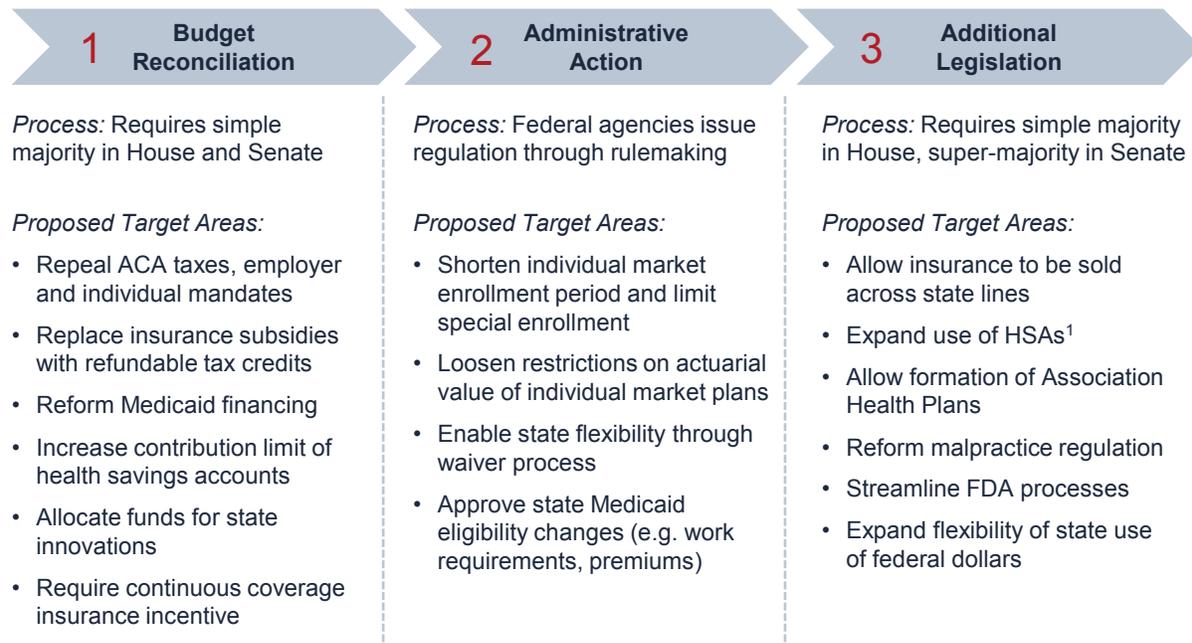
Individuals who believe "President Trump and Republicans in Congress are now in control of the government and they are responsible for any problems with the ACA going forward."¹

1) Telephone survey of 1,171 adults age 18+ living in the US.

An Ambitious Three Part Agenda

GOP Laid Out Three Phases to Health Care Reform

A Three-Staged Approach to Repeal and Replace the ACA

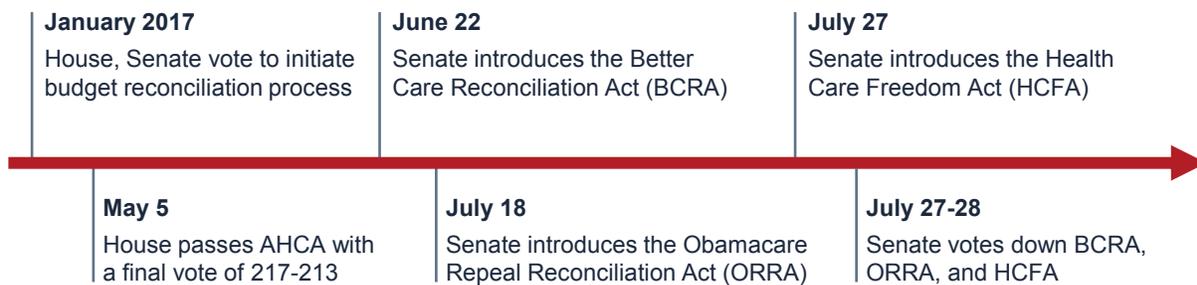


1) Health Savings Accounts.

Easier Said Than Done

GOP Budget Reconciliation Bill Stalls

House, Senate Iterate on Repeal Strategy



1) Restores funding in 2018 in non-expansion states and 2020 in expansion states.
 2) Block grant option only available for traditional adult and children populations.
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Source: House Ways and Means Committee, available at: <https://waysandmeans.house.gov/american-health-care-act/>; House Energy and Commerce Committee, available at: <https://energycommerce.house.gov/news-center/press-releases/energy-and-commerce-republicans-release-legislation-repeal-and-replace/>; Health Care Advisory Board interviews and analysis.

Conservative Principles Driving Repeal Legislation

Reconciliation Bills Target Individual Market, Medicaid, and Taxes

	ACA	AHCA	BCRA	ORRA	HCFA	
Individual Insurance Market	Premium subsidies	✓	✓	✓	✗	✓
	Cost-sharing reduction payments	✓	✗	✗	✗	✓
	Guaranteed essential health benefits	✓	✗	✗	✓	✓
	Health status underwriting	✗	✓	✗	✗	✗
	Individual mandate penalties	✓	✗	✗	✗	✗
Medicaid	Medicaid expansion enhanced match	✓	✗	✗	✗	✓
	Per-capita spending limits	✗	✓	✓	✗	✗
	Block grant option	✗	✓	✓	✗	✗
	Optional work requirements	✗	✓	✓	✗	✗
Taxes	"Cadillac" tax	✓	✓	✓	✓	✓
	Taxes on high-earners, investment income, executive compensation	✓	✗	✓	✗	✓
	Medical devices tax	✓	✗	✗	✗	✗
	Other ACA taxes	✓	✗	✗	✗	✓
Payment Reform	Creates or preserves CMMI	✓	✓	✓	✓	✓
	Advances or does not repeal Medicare payment reform	✓	✓	✓	✓	✓

Source: Restoring Americans' Healthcare Freedom Reconciliation Act, H.R. 3762, 114th Congress, 2015; Patient Protection and Affordable Care Act, H.R. 3590, 111th Congress, 2010; American Health Care Act, H.R. 1628, 115th Congress, 2017; Better Care Reconciliation Act, H.R. 1628, 115th Congress, 2017; Health Care Advisory Board interviews and analysis.

Future of Repeal Legislation Now Unclear

Ready to Move On From Repeal-and-Replace?

“

Senate Leadership Ready to Move on to Other Priorities

“This is clearly a disappointing moment...I regret that our efforts simply were not enough...we look forward to colleagues on the other side suggesting what they in mind [for health care]...**now it is time to move on...**”

Senate Majority Leader Mitch McConnell (R-KY), July 27th statement before the Senate

“Until there’s something that can get us 50...**I think we’ve had our vote and we’re moving on to tax reform.** Everybody wanted to give...the bipartisan approach a chance. People not have that opportunity.”

Sen. John Thune (R-SD), Republican Conference Chairman

Three Potential Legislative Paths Forward

1



Senate Republicans Renew Effort

2



Bipartisan Health Reform Effort

3



GOP Shifts Focus to Non-ACA Legislation

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Source: Nather, D. and Baker, S. "Axios Vitals," *Axios*, Aug. 1, 2017; Davis, S. and Montanaro, D. "McCain Votes No, Dealing Potential Death Blow to Republican Health Care Efforts," *NPR*, July 27, 2017; Health Care Advisory Board interviews and analysis.

Regulatory Agenda Taking Center Stage

Administration Has Considerable Leeway to Alter ACA Trajectory

Meet the Key Players

HHS Secretary: Tom Price



Image: © 2007, District Office of Tom Price

- Six-term Representative from Georgia; retired orthopedic surgeon
- Sponsor of the Empowering Patients First Act
- Confirmed by 52-47 vote

CMS Administrator: Seema Verma



Image: © 2017, CMS

- National health policy consultant from Indiana
- Helped shape Medicaid expansion in IN, OH, KY, TN
- Confirmed by 55-43 vote

Potential Administrative Actions

- End cost-sharing reduction payments
- Delay Cadillac Tax
- Eliminate, delay, or modify Innovation Center programs (e.g., CJR¹)
- Reduce enforcement of insurance mandates
- Narrow scope of essential health benefits
- Allow Medicaid eligibility, cost-sharing reform through 1115 waivers

ACA Leaves Enormous Amount to the Secretary's Discretion

1442

Times the ACA says “the secretary shall” or “the secretary may”

1) Comprehensive Joint Replacement.

Individual Market at a Crossroads

While Some Participants Falter, Others Renewing Commitment

Certain Insurers and States Struggling

aetna No longer selling exchange plans in 2018; expects to lose \$200M on exchange business

HUMANA Plans to withdraw from exchanges in 2018; stands to lose \$45M in 2017

Iowa Two major carriers weighing departure; would leave 15,600 without insurance

25% Increase in counties with only one insurer in 2017

But Market Showing Signs of Stabilization

“Looking forward, we expect insurers, on average, to get close to break-even margins in this segment in 2017... **If the market continues unaffected... we expect 2018... to be one of gradual improvement with more insurers reporting positive (albeit low single-digit) margins.**”

Standard and Poor's analysis of 32 BCBS insurers with exchange plans

“Insurer Centene Commits to Shaky ACA Exchanges for 2018”

“Centene Corp.'s exchange enrollment has swelled 74% since last year, up to nearly 1.2 million people”

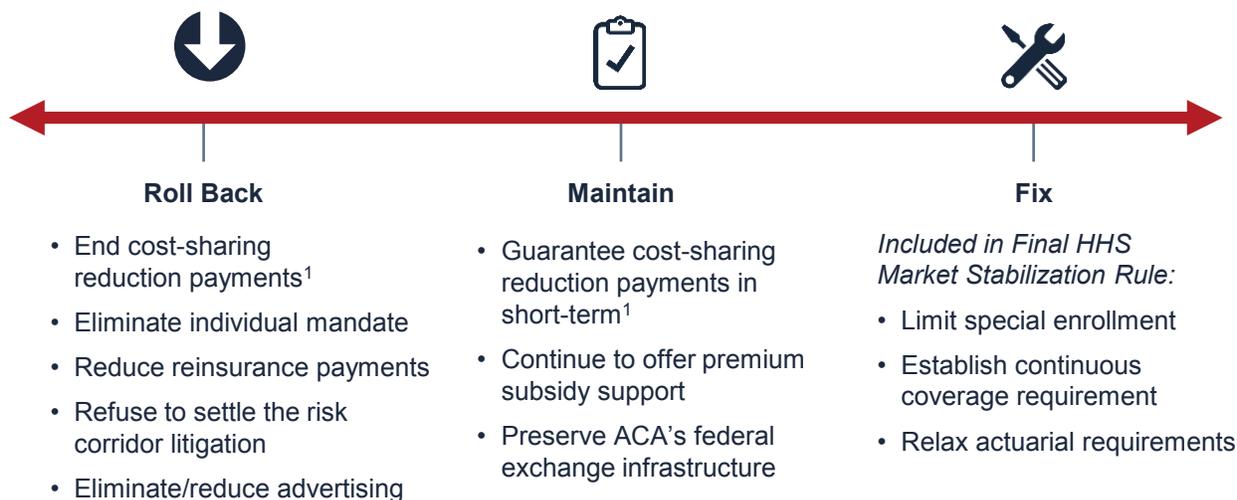
Source: Castellucci, M., “Iowa likely to have no insurers selling on exchanges for 2018,” *Modern Healthcare*, May 4, 2017; Cancryn, A., “Humana becomes first major insurer to quit Obamacare exchanges,” *Politico*, Feb. 14, 2017; Cox, C. et al., “2017 Premium Changes and Insurer Participation in the Affordable Care Act's Health Insurance Marketplaces,” *KFF*, Oct. 24, 2016; S&P, “The US ACA Individual Market Showed Progress in 2016, But Still Needs Time to Mature,” April 7, 2017; Murphy, T., “Insurer Centene Commits to Shaky ACA Exchanges for 2018,” *ABC News*, April 25, 2017; Livingston, S., “Aetna bails on ACA exchanges,” *Modern Healthcare*, May 10, 2017; Health Care Advisory Board interviews and analysis.

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Public Exchanges Hang in the Balance

Future of Public Exchanges May Depend on GOP Actions and Inactions

Administration Has a Spectrum of Options for How to Manage Exchanges



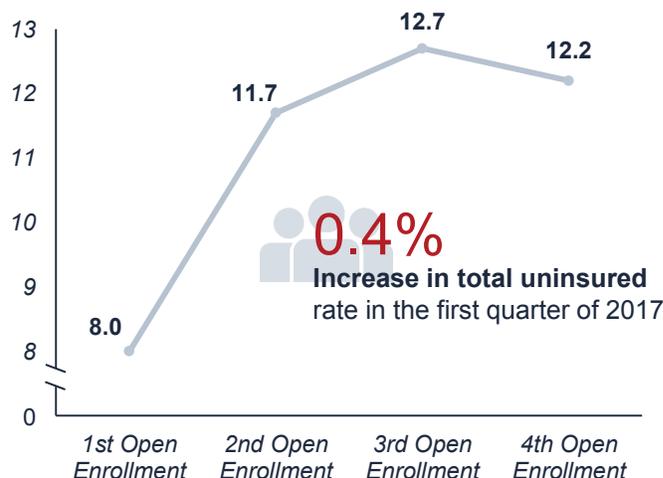
1) Subsidies ruled unconstitutional by district judge in May 2016; ruling stayed additional 90 days at Trump administration request, May 22, 2017.

New Administration Already Impacting Enrollment

Coverage on Public Exchanges Dips Following Change in Administration

Exchange Enrollment Numbers Fall for First Time

Enrollees in ACA Marketplaces
In Millions



Administration’s Decision to Pull Advertising Hurt Enrollment Down Homestretch

“Just **367,260 people** signed up for coverage in the final two weeks of [2017] enrollment on the federal exchange...**compared to more than 700,000 plan selections** in the last week of 2016 enrollment.”

CNBC News

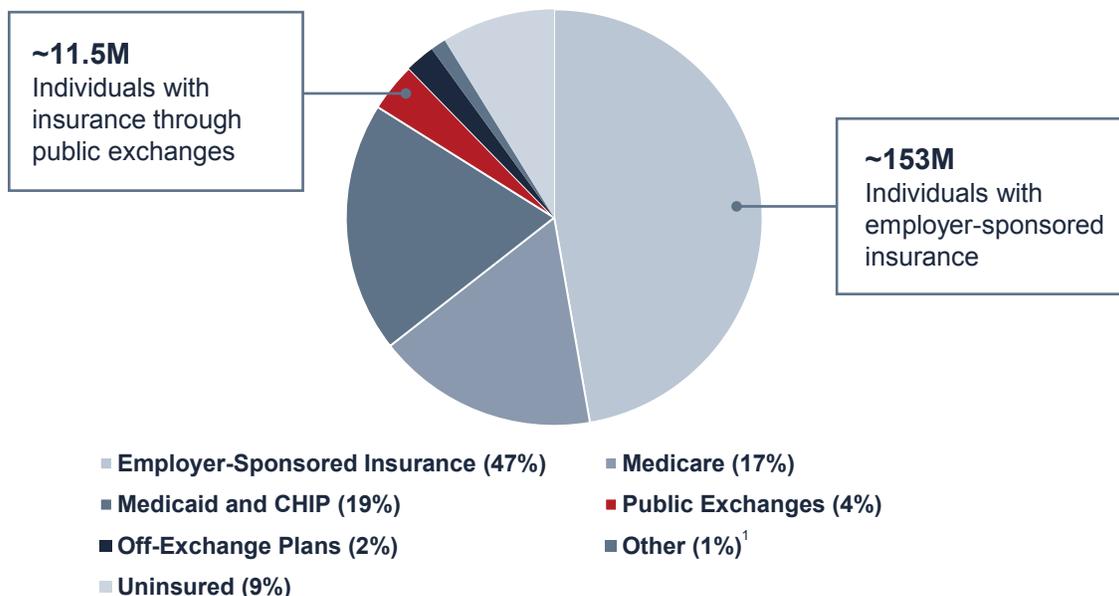
Source: Rudowitz, R., "Medicaid Enrollment & Spending Growth: FY 2016 & 2017," *KFF*, Oct. 13, 2016; Levitt, L., et al., "Assessing ACA Marketplace Enrollment," *KFF*, March 4, 2016; CMS, "Health Insurance Marketplaces 2017 Open Enrollment Period Final Enrollment Report: Nov. 1, 2016-Jan. 31, 2017," March 15, 2017; Mangan, D., "Obamacare enrollment drops in face of Trump repeal effort: More than 9 million people signed up on federal exchange," *CNBC*, Feb. 3, 2017; Mangan, D., "Sabotage: Trump administration reportedly kills Obamacare ads for HealthCare.gov with less than week to go in open enrollment," *CNBC*, Jan. 26, 2017; Health Care Advisory Board interviews and analysis.

For Providers, a Relatively Limited Impact

Despite Political Significance, Exchanges Only a Small Segment of Market

Approximate Coverage of US Population by Payer Sector

As of March 2016



1) Student, IHS, CH+.

Source: Gaba, C., "Healthcare Coverage Breakout for the Entire U.S. Population in 1 Chart," *ACA Signups.net*, March 28, 2016, available at: <http://acasignups.net/16/04/18/show-your-work-healthcare-coverage-breakout-entire-us-population-1-chart>; Health Care Advisory Board interviews and analysis.

Confronting a Larger Problem

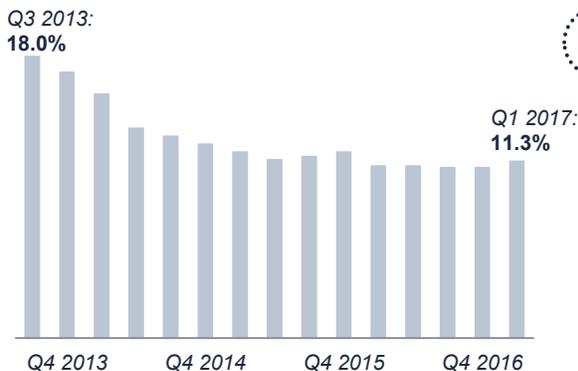
Last Era of Health Reform Expanded Coverage and Increased Spending

Coverage Expansion to Millions...

22M

HHS estimate of adults who **gained coverage** as a result of the ACA

US Adult Uninsured Rate



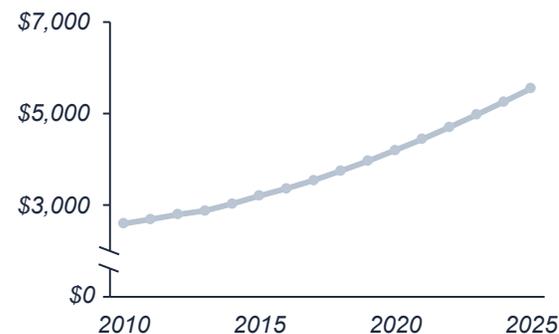
...Drove Spike in Health Care Spending

\$44.6B

Estimate of **increase in hospitals' net income** due to new coverage under the ACA, 2014-2016

National Health Expenditures

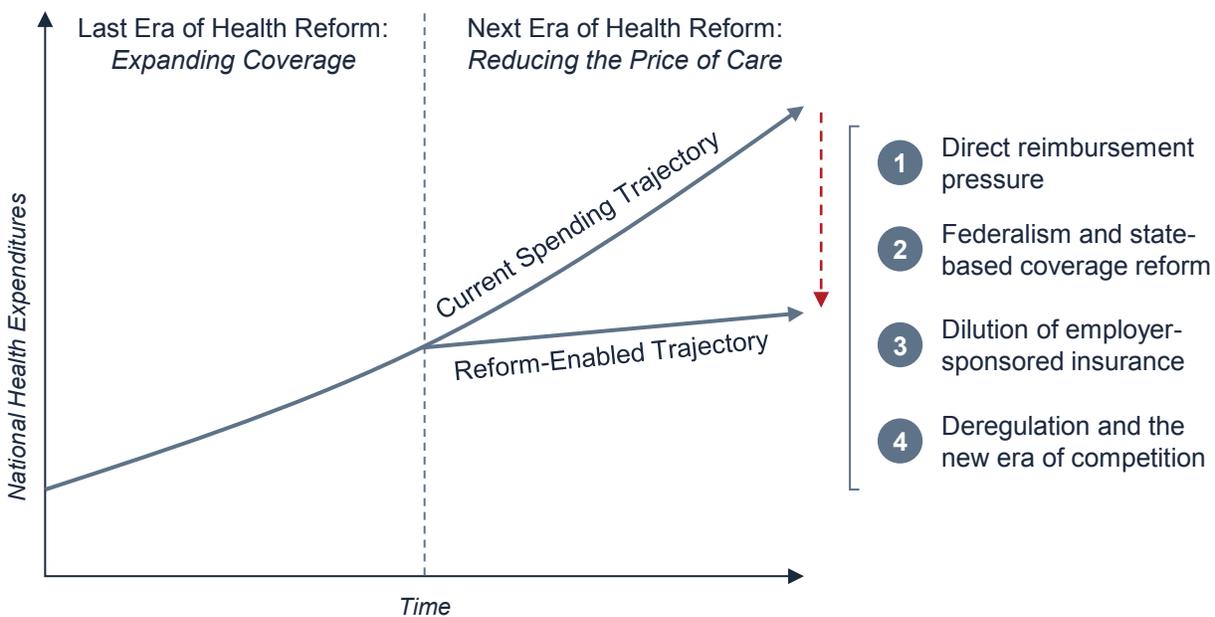
Actual Spend FY2010-2015, Projected FY2016-2025, in billions



Source: CMS, National Health Expenditures, available at: www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/NationalHealthExpendData/NationalHealthAccountsHistorical.html; Gallup, "US Uninsured Rate Edges Up Slightly," April 10, 2017, available at: www.gallup.com/poll/208196/uninsured-rate-edges-up-slightly.aspx; MedPAC, "Report to Congress on Medicare Payment Policy," March 2017, available at: www.medpac.gov/docs/default-source/reports/mar17_entirereport.pdf?sfvrsn=0; Dobson, A. et al., "Estimating the Impact of Repealing the Affordable Care Act on Hospitals," *Dobson DeVanzo & Associates*, Dec. 6, 2016; Health Care Advisory Board interviews and analysis.

The Next Era of Health Care Reform

Four Key Forces Shaping the Next Era of Reform



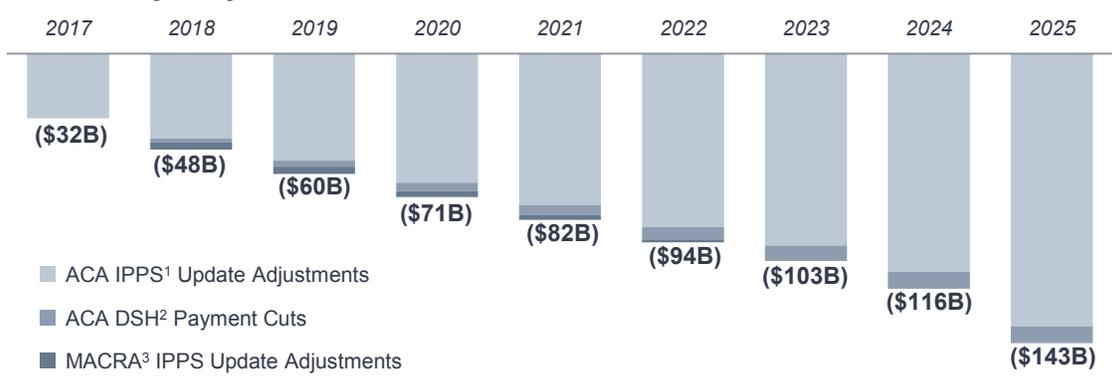
- 1 Unpacking the Political Process
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Force #1: Direct reimbursement pressure

Guess What's Not Getting Repealed

Even Under Repeal, Majority of Obama-Era Cuts Would Have Remained

“Productivity” Adjustments and Other Cuts



No Subtlety Here

“Providers should compare ACO earnings not with what they could earn in today’s fee-for-service payment environment but **with what they could expect to earn in the future if they didn’t participate in such alternative payment models.**”

CMS Officials

1) Inpatient Prospective Payment System; year-over-year estimates based on CBO total projected payment reductions, 2016-2025.
 2) Disproportionate Share Hospital; repealed for non-expansion states under BCRA.
 3) Medicare Access and CHIP Reauthorization Act.
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Source: CBO, Budgetary and Economic Effects of Repealing the Affordable Care Act, June 2015; CBO, “Letter to the Honorable John Boehner Providing an Estimate for H.R. 6079, The Repeal of Obamacare Act,” July 24, 2012; CBO, “Cost Estimate and Supplemental Analyses for H.R. 2, the Medicare Access and CHIP Reauthorization Act of 2015; The Daily Briefing, “How to Understand Last Week’s Big Budget Deal,” November 2, 2015; Budget of the United States Government (Proposed) FY 2016; Pham H, et al., “Medicare’s Vision for Delivery-System Reform – The Role of ACOs,” *New England Journal of Medicine*, September 10, 2015; Health Care Advisory Board interviews and analysis.

No Relief Ahead

New Administration Continuing to Pursue Cost Cutting Goals

House Budget Proposal Would Make Substantial, Additional Medicare Cuts



Hospital 340B Program Also Attracting Scrutiny

Number of Hospitals Participating in 340B



2018 OPPS Proposed Rule to Cut 340B Payments



1) Excludes drugs on pass-through and vaccines.

Source: Kodjak, A., "EpiPen Manufacturer Says It Will Help With Out-Of-Pocket Costs," *NPR*, Aug. 2016; Nather, D., "Trump's Health Care Plan Takes (another) Page from the Democrats," *STAT*, March, 2016; CMS; Health Care Advisory Board interviews and analysis.

Payment Reform Marches On

With MACRA¹ Underway, 2017 a Pivotal Year

Bipartisan Support Guarantees Continued Implementation



Physician Leaders Praise Transition Year

"[These] actions help give physicians a fair shot in the first year of MACRA implementation. This is the flexibility that physicians were seeking all along."

*Dr. Andrew Gurman,
President of the AMA*

2017 MIPS² Reporting Structure

- 1 Clinicians report all MIPS-required data for at least 90 days and are eligible to receive the full bonus
- 2 Clinicians report more than one measure for at least 90 days and are eligible to receive a smaller bonus
- 3 Clinicians report any data for any period of time and receive no positive or negative adjustment in payment

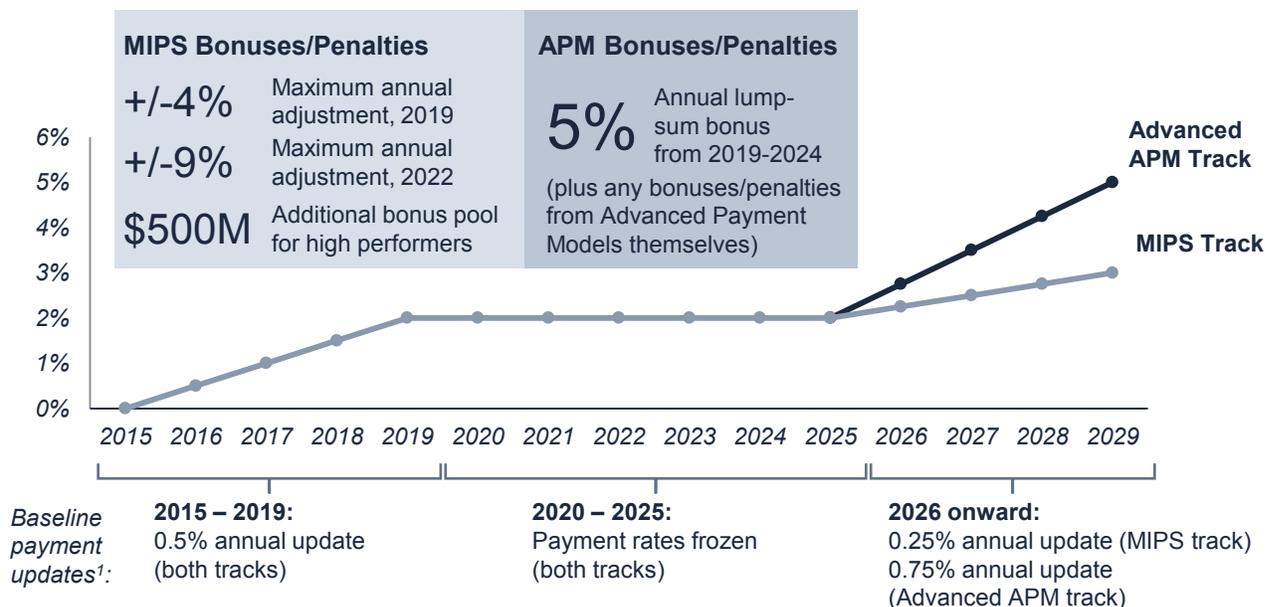
1) Medicare Access and CHIP Reauthorization Act.
 2) The Merit-based Incentive Payment System.

Source: Centers for Medicare and Medicaid Services; Dickson, V., "CMS will give providers flexibility on MACRA requirements," *Modern Healthcare*, September 2016; Health Care Advisory Board interviews and analysis.

MACRA Dealing Physicians in on Risk

Greater Payment Updates, Bonuses Depend on Payment Migration

Annual Provider Payment Adjustments



1) Relative to 2015 payment.

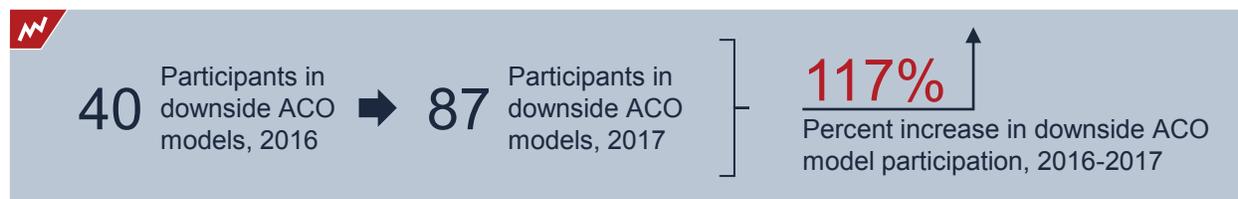
Source: The Medicare Access and CHIP Reauthorization Act of 2015; CMS, Merit-Based Incentive Payment System (MIPS) and Alternative Payment Model (APM) Incentive under the Physician Fee Schedule, and Criteria for Physician-Focused Payment Models, April 25, 2016; Health Care Advisory Board interviews and analysis.

Changing the Calculus Around ACO Participation

MACRA Already Moving the Dial on Participation in Downside Models

Model Selection Determines MACRA Track Qualification

MIPS Not in an ACO or other APM; will receive MIPS payment adjustment 428 Participants ¹	MSSP Track 1 Maximum share rate of 50% 428 Participants ¹	MSSP Track 1+ Fixed loss rate of 30%; Maximum share rate of 50% Begins in 2018	MSSP Track 2 Maximum share/loss rate of 60% 6 Participants	MSSP Track 3 Maximum share/loss rate of 75% 36 Participants	NGACO² Choice of 80% or 100% share/loss rate 45 Participants
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1) As of January 2017.
 2) Next Generation ACO.

Source: NAACOS, "NAACOS ACO Comparison Chart", October 2016, available at: <https://naacos.com/pdf/RevisedSummaryACO-ComparisonChart021916v2.pdf>; CMS, "Next Generation Accountable Care Organization Model (NGACO Model)," January 11, 2016, available at: www.cms.gov; CMS, "2016 Medicare Shared Savings Program Organizations," October 2016, available at: <https://data.cms.gov/ACO/Medicare-Shared-Savings-Program-Accountable-Care-Only>; Health Care Advisory Board interviews and analysis.

Future of Bundled Payments In Question

CMS Poised to Iterate on Voluntary Programs, Scale Back Mandatory Ones



Cardiac EPMS¹ Cancelled

- **Mandatory** bundling for CABG and AMI², originally slated to go into effect July 2017
- Proposed rule released on August 15th would cancel programs entirely



CJR³ Scaled Back

- **Mandatory** bundling for hip and knee replacements, originally in 67 markets
- Proposed rule would make participation in 33 markets voluntary, cancel planned expansion to SHFFT⁴



What's Next for BPCI¹?

- **Optional** bundling program; providers may opt into any of 48 different conditions across four risk models
- Current Models 2, 3, and 4 extended through September 30th, 2018

“

GOP Historically Opposed to CMS's Mandatory Models

“**CMMI has overstepped its authority** and there are real-life implications—both medical and constitutional. That's why we're demanding CMMI cease all current and future mandatory models.”

Letter from GOP Lawmakers, including current HHS Sec. Tom Price to CMS, September 2016

1) Episode Payment Models.

2) Coronary artery bypass graft and acute myocardial infarction; MS-DRGs: 280-282; 246-251; 231-236

3) Comprehensive Joint Replacement.

4) Surgical hip/femur fracture treatment; MS-DRGs: 480-482.

5) Bundled Payments for Care Improvement.

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Source: Jankowski, G., "The New "Price" of U.S. Health Care: The Future of Value-based Reimbursement Under President-elect Trump and Tom Price," *JDSUPRA*, Jan. 10, 2017; Dickson, V., "Hospitals call on Trump administration to end mandatory bundled pay programs," *Modern Healthcare*, April 24, 2017; Centers for Medicare and Medicaid Services; Health Care Advisory Board interviews and analysis.

Impact of Price Cuts and Payment Reform Adds Up

Medicare Payment Cuts Threatening Future Margins

CBO Analysis of Impact of Medicare Payment Cuts¹

60%

Projected increase in the share of hospitals with negative profit margins by 2025²

(0.2%)

Projected average hospital profit margin in 2025²



MACRA Poised to Further Exacerbate Financial Pressures

RAND Analysis of Change in Utilization and Spending Under MACRA³

(\$22B)

Spending decrease in "medium-prospectiveness⁴" scenario

(\$250B)

Spending decrease in "high-prospectiveness⁴" scenario



1) Focusing on 3,000 acute care hospitals subject to ACA's Medicare payment cuts.

2) Assuming hospitals continue at 2016 levels of productivity.

3) RAND Corp. Projections, April 7, 2017.

4) Model factors in changes in physician behavior and potential financial gains/losses for providers if they increase/decrease their level of financial risk.

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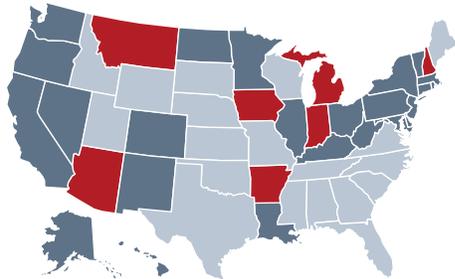
Source: CBO, Projecting Hospitals' Profit Margins Under Several Illustrative Scenarios: Working Paper 2016-04, Sep. 8, 2016; Hussey, P. et al., "The Medicare Access And CHIP Reauthorization Act: Effects On Medicare Payment Policy And Spending," *Health Affairs*, April 7, 2017; Health Care Advisory Board interviews and analysis.

Federal Medicaid Funding Set to Phase Down

ACA's Medicaid Cuts Poised to Take Effect Beginning in 2017

31 States and DC Have Approved Expansion

As of March 2017



■ Participating ■ Expansion by Waiver ■ Not Currently Participating

\$68B Federal spending on Medicaid expansion population, FY2015

\$4.3B State spending on Medicaid expansion population, FY2015

Impending Federal Cuts to Safety Net Spending Threaten Stability

Federal Matching Rate for Expansion Population



\$43B Cut to federal Medicaid DSH payments, 2018-2026

31 States face revenue shortfalls, Jan. 2017

“Medicaid could make up close to half of Louisiana's state budget”
 “We can't control our costs. We're growing out of control,” said state Rep. John Schroder, R-Covington.”

Source: Mitchell, A., "Medicaid's Federal Medical Assistance Percentage (FMAP)," *Congressional Research Service*, Feb. 9, 2016; Maness, R., "Thirty-One States Face Revenue Shortfalls for the 2017 Fiscal Year," *Multi-State*, Jan. 3, 2017; O' Donoghue, J., "Medicaid could make up close to half of Louisiana's state budget," *nola.com*, April 5, 2017; Mitchell, A., "Medicaid Disproportionate Share Hospital Payments," *Congressional Research Service*, June 17, 2016; Health Care Advisory Board interviews and analysis.

Waivers Offer Opportunity for Funding and Innovation

States Using Waivers to Drive Three Major Types of Medicaid Reform



1 Payer-Led Managed Care

- Section 1932 and 1915 waivers, some 1115
- Implemented in 39 states
- Controls state spending by shifting beneficiaries to managed care with per-capita spending limits and/or home-based care alternatives



2 Consumer-Driven Insurance Design

- Section 1115 waivers
- Implemented in 7 states
- Allows states to change Medicaid coverage and eligibility options, often implementing more conservative features (e.g. beneficiary cost-sharing requirements)



3 Provider-Focused Delivery Reform

- Section 1115 waivers, notably DSRIP¹ waivers
- Implemented in 16 states
- States receive federal dollars upfront; commit to delivery and/or payment reform that will save federal government money in long-term

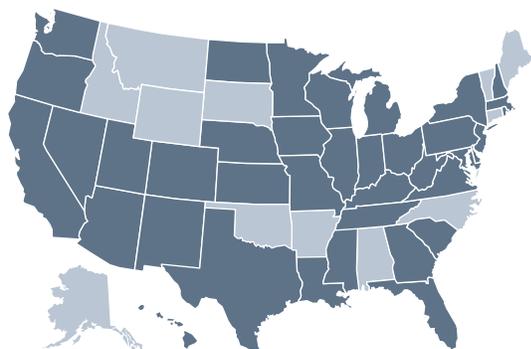
1) Delivery System Reform Incentive Payment.

Source: Kaiser Family Foundation, "Medicaid Enrollment in Managed Care by Plan Type," 2014; Medicaid.gov, "State Waiver List," available at: www.medicaid.gov/medicaid/section-1115-demo/demonstration-and-waiver-list/waivers_faceted.html; Health Care Advisory Board interviews and analysis.

Medicaid Managed Care Reaching Its Limits

39 States and DC Have At Least One Medicaid Managed Care Organization

As of September 2016



■ MCOs¹ ■ No MCOs¹

58% Increase in MCO enrollment in 19 expansion states, Dec. 2013-Sep. 2016

Implications of Medicaid Managed Care for Providers

 Continued payment rate cuts

 Increased opportunity for provider-sponsored health plans

“ [The number of Medicaid beneficiaries covered by insurers] is staggering. It’s nearly a quarter of the population, [but] **the easy growth is over.**”

*Ari Gottlieb,
Director Health Industries Payer
Strategy, PwC Advisory*

1) Capitated Medicaid managed care organizations.

Source: KFF, “Total Medicaid MCOs,” Sep. 2016. <http://kff.org/medicaid/state-indicator/total-medicaid-mcos/?currentTimeframe=0&sortModel=%7B%22colId%22:%22Location%22,%22sort%22:%22asc%22%7D>; Demko, P. “Insurance industry profits booming under Obamacare,” *Politico*, May 1, 2017; Health Care Advisory Board interviews and analysis.

Indiana Tests Medicaid Coverage Reform

Injecting Consumer-Driven Principles Into Medicaid Market

 **Case in Brief: Healthy Indiana Plan**

- Section 1115 Medicaid expansion-enabled model modifying traditional program elements implemented in 2015
- Includes enrollee premiums, co-pays, incentives for preventive services, 2 plan tiers, and penalties for non-payment
- Providers reimbursed at Medicare rates to encourage provider acceptance of Medicaid
- 73% of eligible Medicaid beneficiaries participated in 2015, the first year

HIP¹ Attempts to Encourage Three Behaviors:

- 1 **Taking Personal Responsibility**
 - Requires monthly contributions to “POWER” health savings account; failure to pay results in reduced benefits
 - No retroactive coverage
- 2 **Using Preventative Services**
 - Free preventative services
 - POWER account balances roll over if beneficiaries access these services
 - Higher copays for use of ED in a non-emergency situation
- 3 **Staying on Employer-Sponsored Coverage**
 - HIP Link program offers Medicaid-eligible individuals with employer-sponsored insurance a state-funded POWER account with \$4,000 to cover out-of-pocket expenses

1) Healthy Indiana Plan.

Source: Harper, J., “With the Healthy Indiana Plan up for renewal, is the Medicaid expansion experiment working?” *MedCity News*, Feb. 28, 2017; “State Waivers List,” www.medicaid.gov/medicaid/section-1115-demo/demonstration-and-waiver-list/waivers_faceted.html; Health Care Advisory Board interviews and analysis.

Mixed Results in First Year of Healthy Indiana Plan

Challenges with Cost, Complexity Somewhat Offset by Coverage Expansion

First-Year Results

60% Of enrollees **were previously uninsured** or became eligible due to a change in income

75% Members that remained in the program for a year who **accessed preventative care**

46K Applicants earning above the FPL¹ **were never enrolled** because they didn't make their first payment², Feb. 2015-Nov. 2016

13K Beneficiaries were **disenrolled after failing to pay**, Feb. 2015-Nov. 2016

Key Takeaways

Program Impact

- ▶ Significantly expanded number of individuals with coverage
- ▶ Not yet clear if POWER accounts truly encourage enrollees to shop for the highest value providers and services

Provider Response

- ▶ Employed navigators to assist eligible resident with enrollment

Future Plans

- ▶ In February 2017, officials filed to extend the waiver through 2021, with the addition of voluntary job-related services

1) Federal poverty level.

2) Either because they had not heard of a POWER account or because they could not afford the payment.

Source: Pradhan, R., "Indiana Medicaid expansion blocks out thousands, report finds," *Politico*, May 2, 2017; Harper, J., "With the Healthy Indiana Plan up for renewal, is the Medicaid expansion experiment working?" *MedCity News*, Feb. 28, 2017; The Lewin Group, Inc., "Indiana Healthy Indiana Plan 2.0: Interim Evaluation Report," July 2016, available at: www.medicaid.gov/Medicaid-CHIP-Program-Information/By-Topics/Waivers/1115/downloads/in/Healthy-Indiana-Plan-2/in-healthy-indiana-plan-support-20-interim-evl-rpt-07062016.pdf; Health Care Advisory Board interviews and analysis.

Following in Indiana's Footsteps

New Proposals Even More Expansive than HIP¹

Key Components of Select State Medicaid Waiver Requests Further Embrace Conservative Aims

			Amending current Medicaid expansion			Not expanding Medicaid	
		Indiana ²	Arizona ³	Ohio	Kentucky	Maine	Wisconsin
Eligibility and Enrollment	Coverage conditional on first premium payment	✗	✓	✗	✗	✓	✗
	Waives retroactive eligibility	✓	✗	✗	✗	✓	✗
	Work requirements	✓	✓	✓	✓	✓	✓
	Substance abuse screening and testing	✗	✗	✗	✗	✗	✓
	Time limit on coverage	✗	✓	✗	✗	✗	✓
Cost Sharing	Coverage or select benefits conditional on continued premium payments	✓	✓	✓	✓	✓	✓
	Healthy behavior incentives	✓	✓	✓	✓	✓	✓
Benefits	Waive non-emergency medical transportation	✓	✗	✗	✓	✓	✗

1) Healthy Indiana Plan.

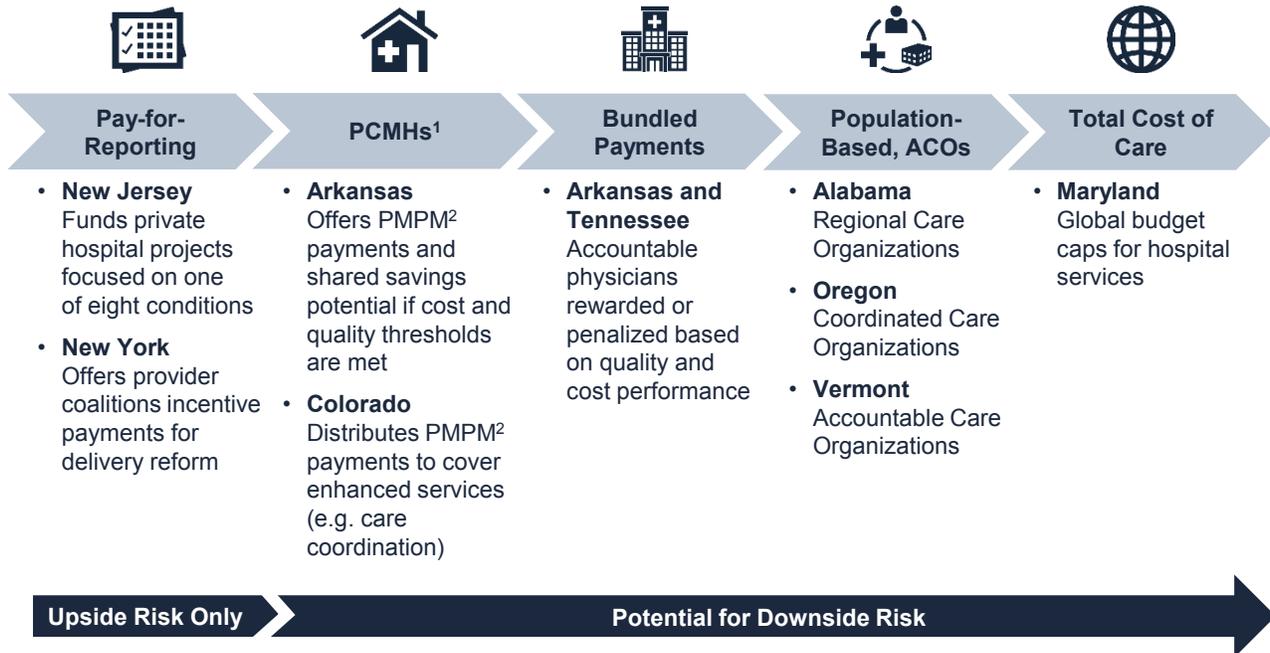
2) Original waiver approved by CMS without work requirements, planning to apply to add them as of May 24, 2017.

3) Already has approval for premiums, healthy behavior incentives.

Source: Musumeci, M. et al., "Proposed Medicaid Section 1115 Waivers in Maine and Wisconsin," *KFF*, May 10, 2017; Musumeci, M. et al., "Key Themes in Section 1115 Medicaid Expansion Waivers," *KFF*, Mar. 14, 2017; Wisconsin DHS, "Section 1115 Demonstration Waiver-BadgerCare Reform," April 25, 2017, available at: www.dhs.wisconsin.gov/badgercareplus/waivers-cla.htm; Arkansas Governor, "Governor Hutchinson to Seek Changes to Arkansas Works Waiver, Legislation Needed," March 3, 2017, available at: <http://governor.arkansas.gov/press-releases/detail/governor-hutchinson-to-seek-changes-to-arkansas-works-waiver-legislation-ne>; Dickson, V., "Maine joins the throng seeking Medicaid work requirements," *Modern Healthcare*, April 26, 2017; Health Care Advisory Board interviews and analysis.

Payment Reform an Increasingly Popular Strategy

State Demonstrations Span Value-Based Payment Spectrum



1) Patient Centered Medical Homes.
2) Per-Member Per-Month.

Delivery Waivers Offer Most Opportunity for Providers

An Alternative to Cuts to Coverage and Reimbursement

Items to Watch For

- Will more comprehensive data on cost, savings, and quality from existing demonstrations be forthcoming?
- How will the Trump administration assess new and renewal waiver proposals?
- Will more commercial payers get involved in these demonstrations?
- Will CMMI create a third round of State Innovation Model (SIM) grants?

Provider Considerations

- Take advantage of money available from current demonstrations to fund new initiatives or ongoing projects
- Leverage model parameters to enhance value-based care capabilities; align incentives across distinct Medicaid, uninsured enrollment groups; and prepare for population health under MACRA
- Proactively engage with state officials to participate in shaping and improving program structure

1) The Medicare Access and CHIP Reauthorization Act of 2015.

Employer Health Spending Continues to Grow

Employer Health Benefits Clearly Not a Legislative Target



“Cadillac Tax” Delayed

- 40% excise tax assessed on employee health benefit spend exceeding \$10,200 for individuals, \$27,500 for families
- Originally proposed in ACA to begin in 2018; effective date postponed to 2020



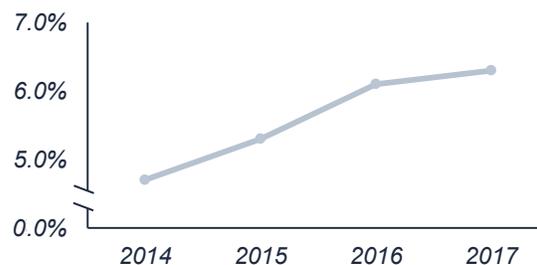
Cap on Tax Exclusions Dropped

- Limit on existing tax exclusions for employer contributions to health plans
- Model proposed in “A Better Way,” absent from House’s AHCA and Senate’s BCRA

Even Without Regulatory Pressure, Employers Still Have a Cost Problem

~47% US population covered by employer-sponsored insurance

Average Annual Growth Rate Among Private Business’s Health Expenditures FY 2014-2017



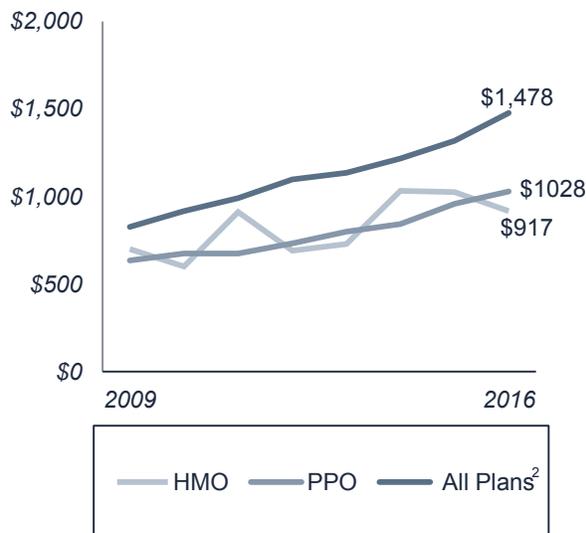
Source: Gaba, C., “Healthcare Coverage Breakout for the Entire U.S. Population in 1 Chart,” *ACASingups.net*, March 28, 2016, available at: <http://acasingups.net/16/04/18/show-your-work-healthcare-coverage-breakout-entire-us-population-1-chart>; US Bureau of Labor Statistics, “Employee Tenure Summary,” September 2016; Berman, R., “Why Some Conservatives Are Unhappy About Obamacare Cuts,” *The Atlantic*, Dec. 17, 2015; Health Care Advisory Board interviews and analysis.

Cost-Shifting Remains the Dominant Response

Migration to High Deductible Health Plans Well Underway

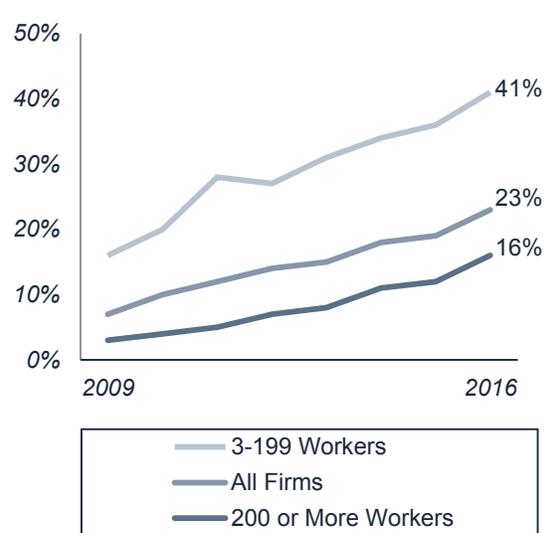
ESI Average Deductible for Single Coverage¹

By Plan Type, 2009-2015



Percentage of Covered Workers with Annual Deductible of \$2,000 or More³

By Firm Size, 2009-2016



1) Among covered workers with a general annual health plan deductible.

2) Includes HDHP/SO.

3) For single coverage.

Source: KFF, “2016 Employer Health Benefits Survey,” available at: <http://kff.org/health-costs/report/2016-employer-health-benefits-survey/>; Health Care Advisory Board interviews and analysis.

Cost-Shifting Reaching Its Limits

Employers Increasingly Looking to Supplement Cost-Shifting Strategies

Cost Shifting Causing Consumers to Forgo Care, Increasing Bad Debt...

Spending Reductions Following Implementation of HDHPs



Increasing Bad Debt as Consumers Face Growing Financial Exposure



...But Not Incentivizing Shopping

“ [We found] that spending reductions are entirely due to outright reductions in quantity. We found no evidence of consumers learning to price shop after two years in [a HDHP].”

The National Bureau of Economic Research

“ Consumers want to make better choices. They want to save money. They just want someone else to do the work and show them how.”

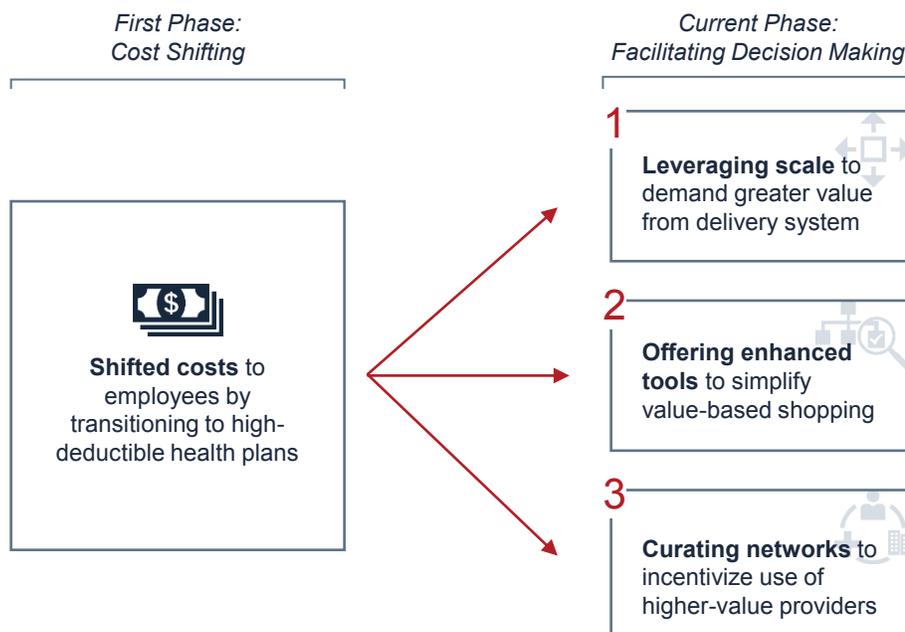
Chief Innovation Officer, Global Benefits Consulting Firm

Source: DiJulia, B. et al., "Data Note: Americans' Challenges with Health Care Costs," KFF, March 2, 2017; Brot-Goldberg, Z. et al., "What Does a Deductible Do? The Impact of Cost-Sharing on Health Care Prices, Quantities, and Spending Dynamics," The National Bureau of Economic Research, October 2015; Altman D, "Health-Care Deductibles Climbing Out of Reach," *Wall Street Journal*, March 11, 2015; KFF, "2016 Employer Health Benefits Survey," available at: <http://kff.org/health-costs/report/2016-employer-health-benefits-survey/>; Health Care Advisory Board interviews and analysis.

New Tools Aim to Facilitate Consumer Shopping

Helping Employees Make High-Value Choices

Employers Entering a New Era of Health Benefits Strategy



Using Scale to Incentivize Transformation

Employer Coalition Demanding Greater Value



**HEALTH
TRANSFORMATION
ALLIANCE**

Select Founding Members

- American Express
- American Water
- BNSF
- Coca-Cola
- DuPont
- HCA
- IBM
- Ingersoll Rand
- International Paper
- Lincoln Financial
- Macy's
- Marriott
- NextEra Energy
- Pitney Bowes

\$14B Annual health spending

4M Covered lives

HTA's First Priority Areas



Prescription Drug Purchasing

- Three-year contract with CVS and OptumRX
- Members receive full transparency on rebates/discounts, ability to audit fees, and participation in formulary decision-making



Data and Analytics

- Contract with IBM Watson Health
- Will aggregate and analyze claims data to better-understand impact of medical interventions and wellness initiatives



Narrow Network Curation

- Partnering with Cigna and UnitedHealthcare
- Payers will build high-value networks for Type II Diabetes, joint replacements, and back pain in Dallas, Phoenix, and Chicago

Source: Sanicola, L., "The Health Transformation Alliance: Can Employers Help Solve the Problem?" *Huffpost*, April 27, 2017; Walker, J., "Alliance of companies announce plans to lower their health-care costs," *Wall Street Journal*, Mar. 6, 2017; Pharmaceutical Commerce, "Health Transformation Alliance sets its 2017 agenda," April 4, 2017; Health Care Advisory Board interviews and analysis.

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Engagement Tools Simplify Shopping Process

Personalized Support Helps Facilitate Decision-Making

Technologies Span a Variety of Engagement Mediums

Aggregator Platforms

Integrated interfaces that aggregate all health benefits related tools and resources



Example: Jiff

Increased use rates of price transparency tool by 62% within two months for Activision Blizzard

Customized Messaging

Communication platforms that use predictive analytics to tailor messaging



Example: Evoke Health

Increased flu vaccine rates by 4% among high-risk employees at a large, Midwest utility company

Concierge Navigation

Phone- or web-based service that provides access to a dedicated health navigator



Example: Accolade

Improves health care outcomes and engagement (e.g. 98% consumer satisfaction, 3% reduction in ED visits) across clients

Source: Milkman, K. et al., "Using implementation intentions prompts to enhance influenza vaccination rates," *PNAS*, June 28, 2011; Evoke Health, <http://www.evivehealth.com/>; Accolade, <https://www.accolade.com/solution/>; Jiff, <https://www.jiff.com/>; Health Care Advisory Board interviews and analysis.

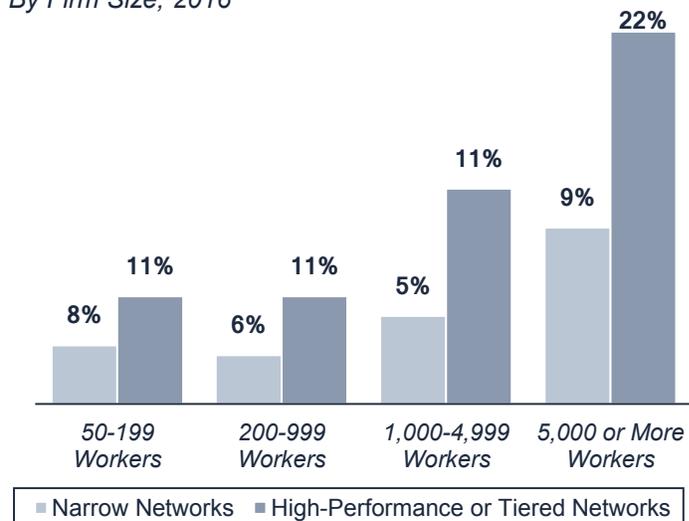
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Others Curating Through Network Design

High-Performing Networks Most Prevalent Among Large Employers

Percentage of Firms With Health Plans Offering a Narrow Network, High-performance Network, or Tiered Network

By Firm Size, 2016



Even More Companies Poised to Join the Trend

46%

Of employers surveyed¹ in Q1 2016 are considering implementing value-based plan designs or high-performance networks in 2017

1) PwC's 2016 Health and Well-being Touchstone Survey; includes 1,100 employers from 37 industries across the US.

Source: Murphy, B., "PwC: 46% of employers consider move to high-performance networks," *Beckers*, June 21, 2016; Hall, M. et al., "Narrow Provider Networks for Employer Plans," *Employee Benefit Research Institute*, Dec. 14, 2016; Health Care Advisory Board interviews and analysis.

Force #4: Deregulation and the new era of competition

Regulatory Reform a Centerpiece of the GOP Agenda

White House, HHS, Congress Looking to Scale Back Regulations



White House

Executive Orders to-date include:

- January 20th order to "[minimize] the economic burden" of the ACA
- January 30th order requiring at least two regulations be identified for elimination for each new regulation issued
- February 24th "Enforcing the Regulatory Reform Agenda" order requiring every federal agency to create Regulatory Reform Task Force



HHS/CMS

RFIs on reducing regulatory burden included in:

- 2018 inpatient prospective payment system (IPPS) rule
- Standalone RFI on reducing the regulatory burdens of the ACA; comments were due on July 12
- The proposed outpatient prospective payment system (OPPS) rule for 2018; comments due on September 11
- The proposed physician fee schedule (PFS) rule for 2018; comments due on September 11



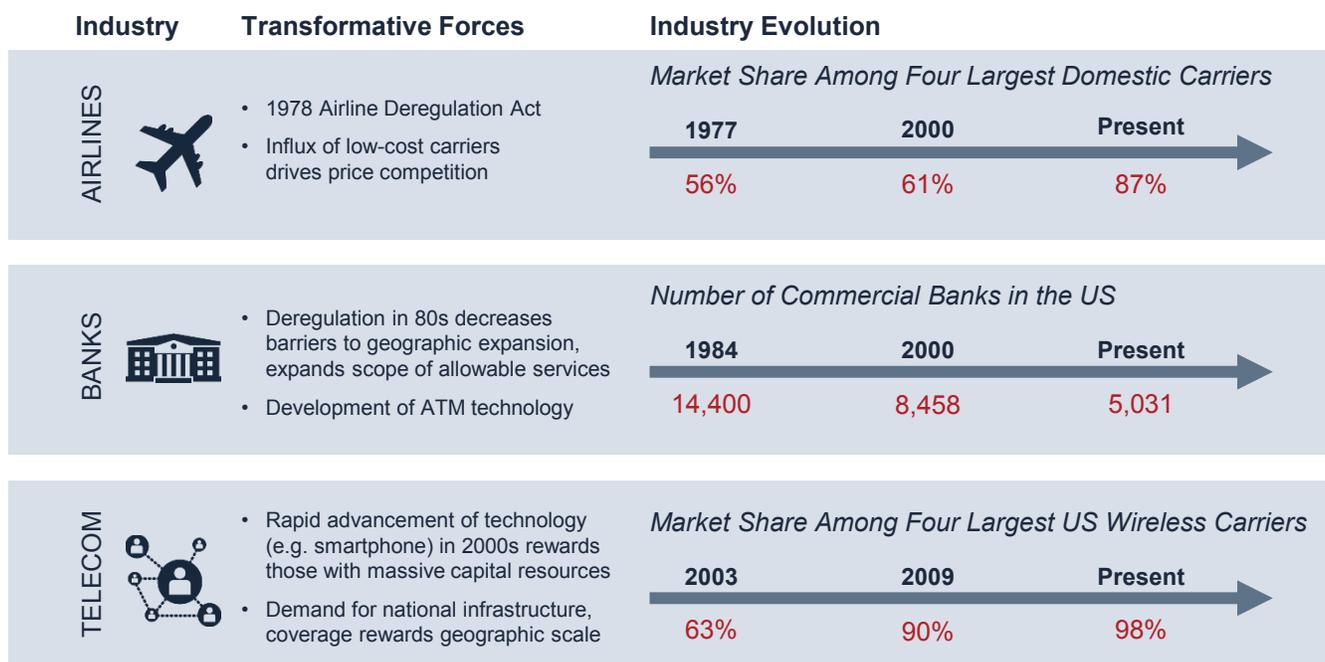
Congress

Medicare Red Tape Relief Project seeks to:

- Deliver relief from regulations that "impede innovation, drive up costs, and ultimately stand in the way of delivering better care for Medicare beneficiaries"
- Request feedback from stakeholders to identify opportunities
- Host stakeholder roundtables
- Drive Congressional action based on the stakeholder input efforts

Not an Altogether Unfamiliar Story

Market Forces, Regulatory Changes Have Driven Rapid Transformation in Other Sectors



Source: FRED Economic Research, "Commercial Banks in the United States," April 2017, available at: <https://fred.stlouisfed.org/series/USNUM>; Metzler, J., "6 years after the iPhone launched, just 4 big carriers are left standing," *Venture Beat*, July 8, 2013; Health Care Advisory Board interviews and analysis.

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Value to Consumers Paramount

Consolidation and Scale Deliver End-User Value in Other Industries



- Lower prices:** After adjusting for inflation, airline prices have declined by 50% since 1978
- Superior delivery model:** Increase in number of routes, fare classes has made flying more accessible



- Upgraded infrastructure:** Number of branches grew from 53,000 in 1980 to 71,000 by the end of 1998; digital banking now on the rise
- Superior delivery model:** Wider range of products and services (e.g. types of accounts, personal finance)



- Lower prices:** Cost of wireless voice service per minute has declined by more than 30% since 1993
- Upgraded infrastructure:** National networks now ubiquitous, enabling affordable long-distance calls

Imperatives for Health Systems



Reduce Prices
Bring down both unit cost and total cost of care



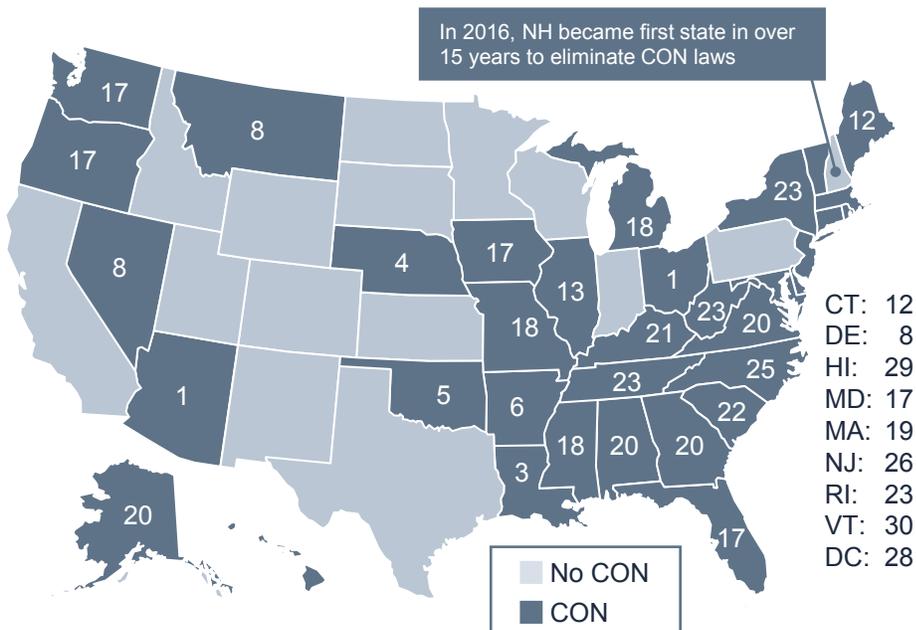
Improve Delivery Model
Make care more convenient and consumer-focused



Upgrade Infrastructure
Use scale to improve and expand asset base

States Renewing Push to Eliminate CON Laws

State of CON Laws, 2016



28
States with CON laws for ASCs

15
States with no CON laws

2
States that introduced bills to eliminate CON in 2017

New Administration Encouraging the Trend

2018's Outpatient Payment Proposal Promotes Lower Acuity Settings

Total Knee Arthroplasty (TKA) to be Reimbursed in the Outpatient Space

\$12,380.78
Inpatient Reimbursement¹

↓

\$9,912.69
Outpatient Reimbursement²

20%
Reduction in TKA reimbursement

48%
Average percentage of Medicare TKA cases per organization that are potentially eligible to be performed in outpatient setting³

Non-Excepted Hospital Outpatient Clinic Reimbursement Rate to be Cut in Half

Proposed CY2018 Rates
Percentage of HOPPS Reimbursed by Setting

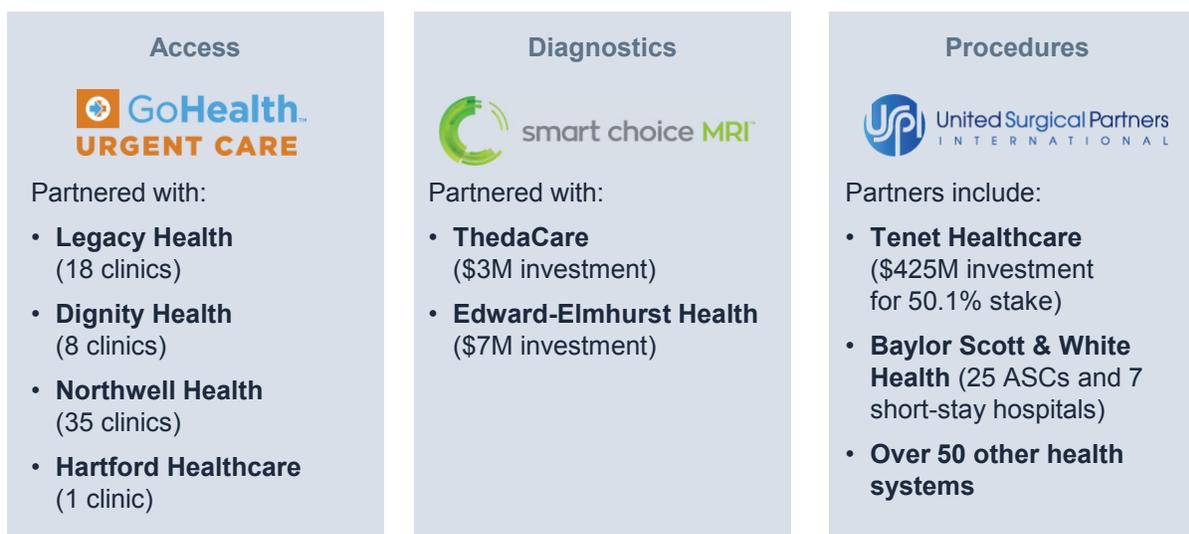
Setting	Percentage of HOPPS Reimbursed
Excepted HOPDs	100%
ASCs	55%
Non-Excepted HOPDs	25%
Physician Offices	25%

CY 2017 non-expected provider rate: 50%

1) Proposed rate for FY2018.
 2) Proposed rate for CY 2018.
 3) Analysis of MEDPAR inpatient Medicare claims from FY 2016 per six-digit Medicare CCN. Analysis reviewed cases assigned MS-DRG 469 or 470 with a TKA primary procedure code for distinct Medicare CCN. Cases with MS-DRG 470 were considered eligible to shift outpatient if the patient did not fulfill any of the exclusion criteria listed above. Please note that this is a generous analysis of eligibility, as other patient criteria not present in claims data (e.g., preference for no hospital stay; post-operative presence of a caregiver in patient's home) also impact whether a case should be performed outpatient.

Innovators Doubling Down on Ambulatory Care

Meeting Demands of Market Requires New Forms of Partnership



“Smart Choice MRI shares our vision to put patients and consumers at the center of the health care experience. **We sometimes collaborate with competitors in the best interests of consumers.**”

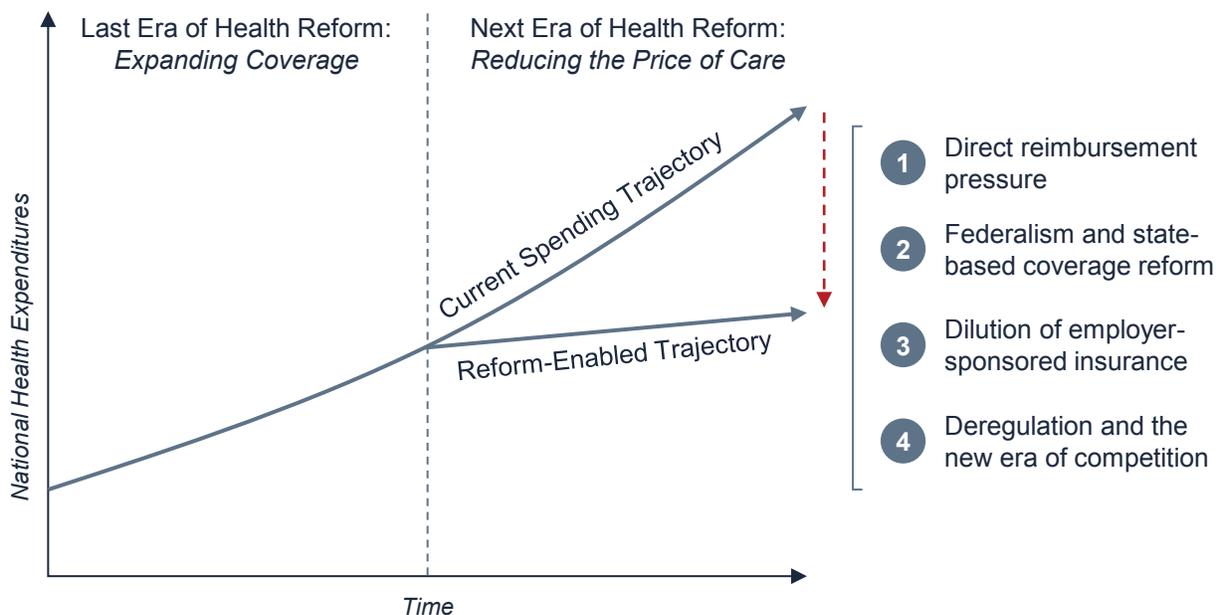
Keith Livingston, SVP of Systems of Care Support, ThedaCare

Source: GoHealth, <https://www.gohealthuc.com>, accessed May 2017; ThedaCare, “ThedaCare Invests in Smart Choice MRI,” February 2016; Edward-Elmhurst Health, “Edward-Elmhurst Health invests \$7 million in Smart Choice MRI,” May 2016; Modern Healthcare, “Tenet makes big ambulatory play with deal for majority United Surgical Partners stake,” March 2015; United Surgical Partners International, available at: <http://www.uspi.com/partners.aspx>, accessed May 2017; Health Care Advisory Board interviews and analysis.

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The Next Era of Health Care Reform

Four Key Forces Shaping the Next Era of Reform



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Source: Health Care Advisory Board interviews and analysis.

The “Checking in on Granny” Economy

Health Care Forced to Confront a Larger Societal Issue

From the Factory Floor...



Image: © 1942, Howard R. Hollem

...To the Rocking Chair

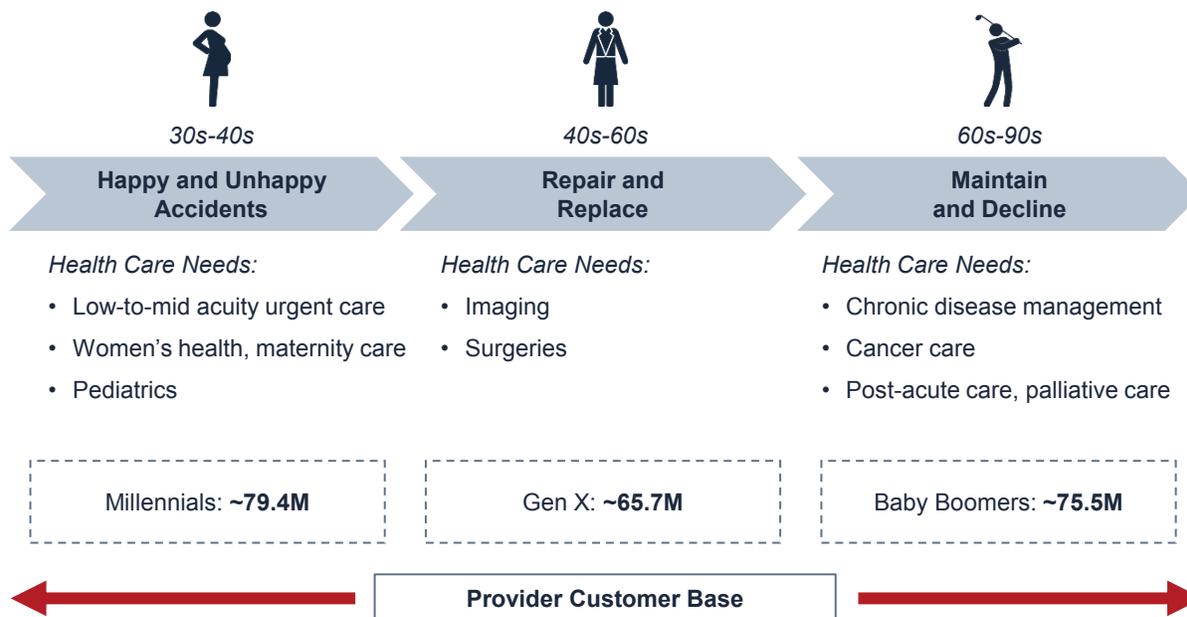


Image: © 2012, Lisay



Demanding an Entirely Different Set of Services

Retirees, Millennials Have Vastly Different Demands From Middle-Aged



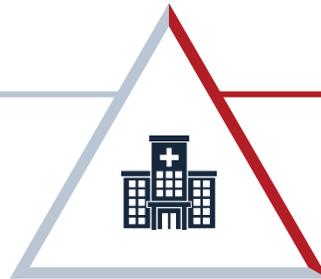
Delivery Model at a Crossroads

Reimbursement Model and Customer Needs Shifting Simultaneously

Yesterday's Model:

Privately-Reimbursed Procedural Care

Largest patient base comprised of commercially-insured, middle-aged patients in need of imaging services and surgeries



Today's Model:

Publicly-Reimbursed Medical Care

Patients covered by Medicare or HDHPs, in need of medical management, low-acuity preventive care

1

Unpacking the Political Process

2

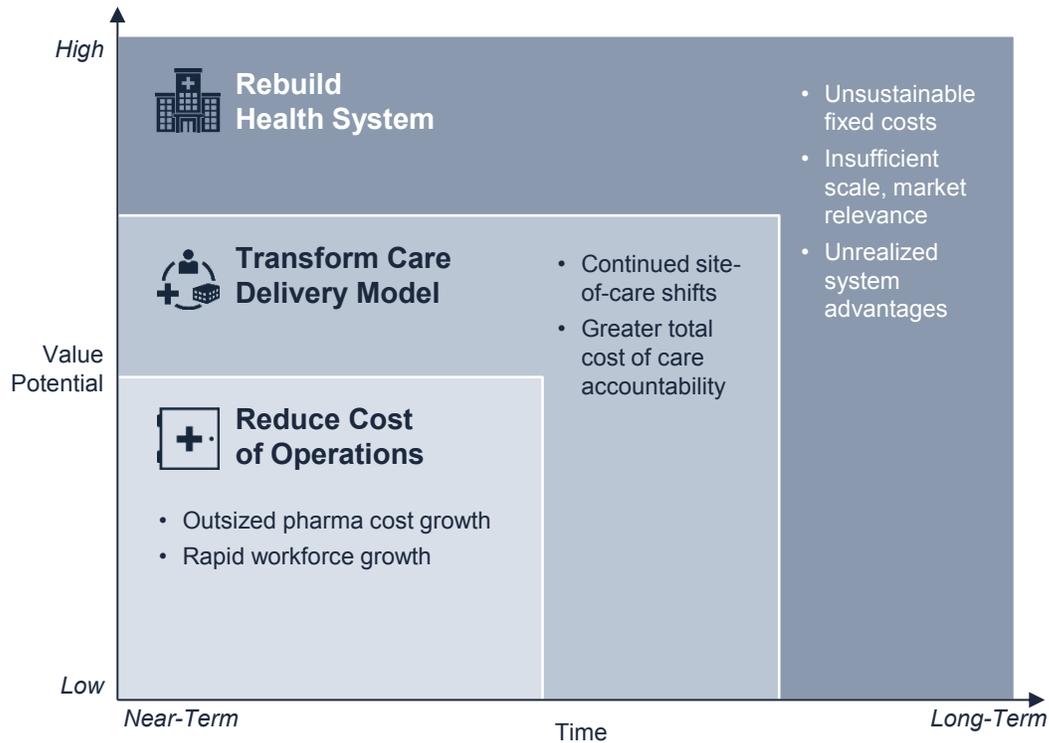
The Next Era of Health Reform

3

Adapting Provider Strategy to New Market Realities

Our Leadership Challenge

Delivery System Transformation Central to Future Success



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Source: Health Care Advisory Board interviews and analysis.

Expense Growth Inhibiting Price Flexibility

As Drivers of Unit Cost Shift, Expenses Continue to Rise

Major Cost Drivers Evolving

PAST ▶

PRESENT



“Over the next year, **rising labor and pharmaceutical costs** will continue to pressure the expense growth rate.”

Beth Wexler, VP, Moody's Investors Service

Pharma Costs Dominating the News



“I think it will be huge...**Almost all of it is profit** and I think we will get three years of that or more. Should be a very handsome investment for all of us.”

*Martin Shkreli, Former CEO
Turing Pharmaceuticals*



Bipartisan Alarm

“Over the last several years, Mylan Pharmaceuticals has **increased the price of EpiPens by more than 400%. That's outrageous.**”

*Sen. Amy Klobuchar
D-Minnesota*

“I am a very pro-business Republican, yet **I am really sickened by what I've heard about [the EpiPen] situation.** Nobody can really earn or deserve that much money.”

*Rep. John Duncan
R-Tennessee*

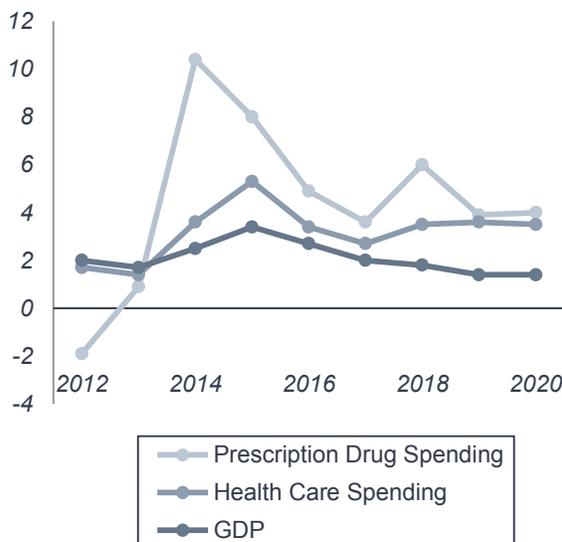
Source: Kodjak, A., "A Peek Inside Turing Pharmaceuticals: Another \$7.2 Million. Pow!" *NPR*, Feb. 2016; Scott, E., "Cost of EpiPen: 'One senator's daughter is Mylan CEO, another's needs drugs,'" *CNN Politics*, Aug. 2016; Langreth, R. et al., "Free Market Republicans Turn on Mylan, Say EpiPen Went Too Far," *Bloomberg*, Sept. 2016; Health Care Advisory Board interviews and analysis.

Beyond the Headlines, A Much Broader Problem

Pharma Spending on the Rise Across the Board

Drug Spending Growth Outpacing Broader Health Care Spending and Overall Economy

Annual Change



A Rapidly Growing Line Item

14.8%

Change in **brand drug prices** in 2015

\$435.3B

Projected **drug spending** in 2020

“The U.S. healthcare system spent **\$373.9 billion on drugs in 2014** — **13.1% more than it did the previous year** and the highest rate of spending growth since 2001.”

Forbes

Source: Centers for Medicare & Medicaid Services, Office of the Actuary; Weintraub, A., "Growth in Drug Spend Is Hitting a 13-Year High. Note to Pharma: Innovation Pays," *Forbes*, April 2015; Dennis, B., "Prescription Drug Prices Jumped More than 10% in 2015, Analysis Finds," *The Washington Post*, January 2015; Health Care Advisory Board interviews and analysis.

No Easy Policy Solutions

Despite Rhetoric, Limited Consensus on Policy Response

Radical Solutions Proposed on Campaign Trail



Allow Medicare to negotiate prices



Allow foreign drug imports

"We're the largest buyer of drugs in the world and yet we don't bid properly. We're going to start bidding and we're going to save billions of dollars over a period of time."

*President-Elect Donald Trump
Press Conference, January 11th, 201*



Draft Executive Order Takes Softer Approach



Scaling back 340B program



Value-based drug pricing



Extending patent life for drugs overseas



Reforming regulatory landscape



Expediting generic drug approvals

1) Excludes drugs on pass-through and vaccines.

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Source: Kodjak, A., "EpiPen Manufacturer Says It Will Help With Out-Of-Pocket Costs," *NPR*, Aug. 2016; Nather, D., "Trump's Health Care Plan Takes (another) Page from the Democrats," *STAT*, March, 2016; Health Care Advisory Board interviews and analysis.

Focus Leadership on Actionable Opportunities

Pharma Costs Require C-Suite Attention

1



Reining in Employee Health Spend

- How actively do we manage our outpatient formulary?
- Are we collecting and utilizing data on prescriber variation patterns?

2



Commercializing Pharmacy Management Expertise

- Have we expanded our health plan to outside entities?
- Have we initiated conversations with retail pharmacies?

3



Managing Prescription Costs for At-Risk Contracts

- Are pharmacists integrated in our clinical care teams?
- Is medication reconciliation being performed at all transitions of care?

4



Evaluating the Opportunity for Specialty Pharmacy

- Have we evaluated our eligible patient population and their drug coverage?
- Have we created a strategy to manage limited distribution drugs?



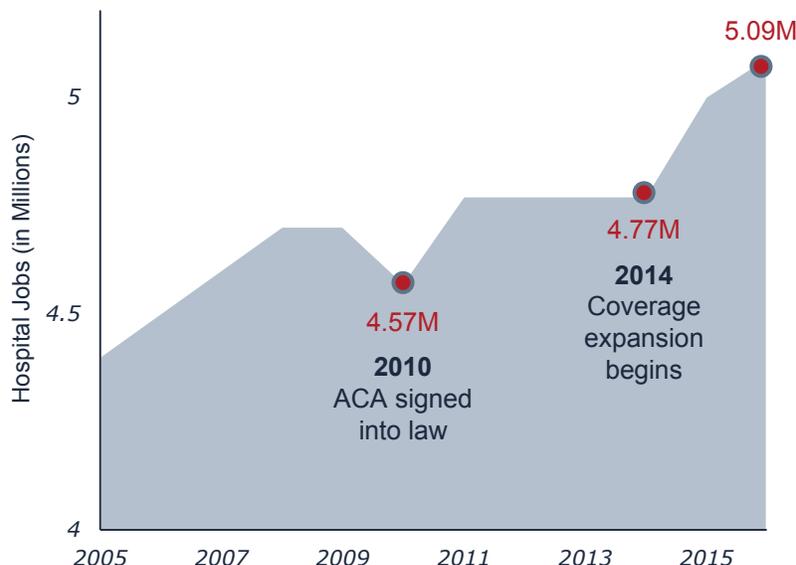
To explore these topics in more depth, members can watch our on-demand webconference:

["5 Things CEOs Need to Know About Pharmacy"](#)

Labor Force Reaches Unprecedented Heights

Job Growth Rises to Meet Demands of Reform, Coverage Expansion

Hospital Jobs in Millions, By Year



“More people—15.5 million—now work in health care than live in the state of Ohio... Based on job numbers, no sector is healthier than health care.”

Politico

Competition for Physician Assets Heating Up

Physicians Have Growing Number of Alternatives to Employment

Four Main Alternatives to Health System Employment

<p>1</p> <p>Large Independent Groups</p> <p>25% Growth in median medical group size, 2013-2015</p> <p>35% Physicians currently part of a group of 100 or more</p>	<p>2</p> <p>National Practice Companies</p> <p>PRIVIA MEDICAL GROUP EmCare MEDNAX TEAMHealth.</p> <p>\$400M Venture investment in Privia for care delivery innovation, primary care expansion, 2016</p>	<p>3</p> <p>Private Equity Firms</p> <p>3-5 years Common investment duration for private equity firm</p> <p>\$250M Invested by equity firm Summit Partners in DuPage Medical Group, a 459 physician multi-specialty group in Illinois</p>	<p>4</p> <p>Health Plans</p> <p>75 UnitedHealthcare® Markets for which United subsidiary Optum aims to provide primary care and ambulatory services</p> <p>40% Surveyed independent groups who reported interest in acquisition by health plans</p>
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Health Care's Incurable "Cost Disease"?

Labor-Intensive Industries Struggle to Reduce Costs



Theory in Brief: William Baumol's "Cost Disease"

- Productivity in labor-intensive service industries grows much more slowly than the overall economy
- Wages must grow with the overall economy to maintain talent
- This combination increases costs and reduces return on investment

“The number of players, the number of instruments, the amount of time it took to ‘produce’ a Mozart quartet in the 18th century will not have changed one whit two centuries later.”

Sen. Daniel Patrick Moynihan presenting Baumol's work to the Senate Finance Committee

Industries Plagued by Seemingly Unavoidable Cost Growth



Image: © 2014, Robert and Talbot Trudeau



Image: © 2008, U.S. Navy

Source: Lee, T., "William Baumol, whose famous economic theory explains the modern world has died," *Vox*, May 4, 2017; Will, G., "An old 'disease' that could help lawmakers understand today's health-care debate," *The Washington Post*, May 17, 2017; Health Care Advisory Board interviews and analysis.

Reconsidering the Reliance on Costly Human Capital

Translating Labor-Intensive Services into Discrete Goods



From the Concert Hall...

- Highly skilled symphony orchestra
- Unique occurrences

→
Evolution of technology and consumer expectations



...To the Living Room

- Individually accessible concert recording
- Infinitely repeatable



From the Operating Room...

- Technically skilled, hands-on surgery team
- Procedure-focused encounter

→
Evolution of technology and consumer needs



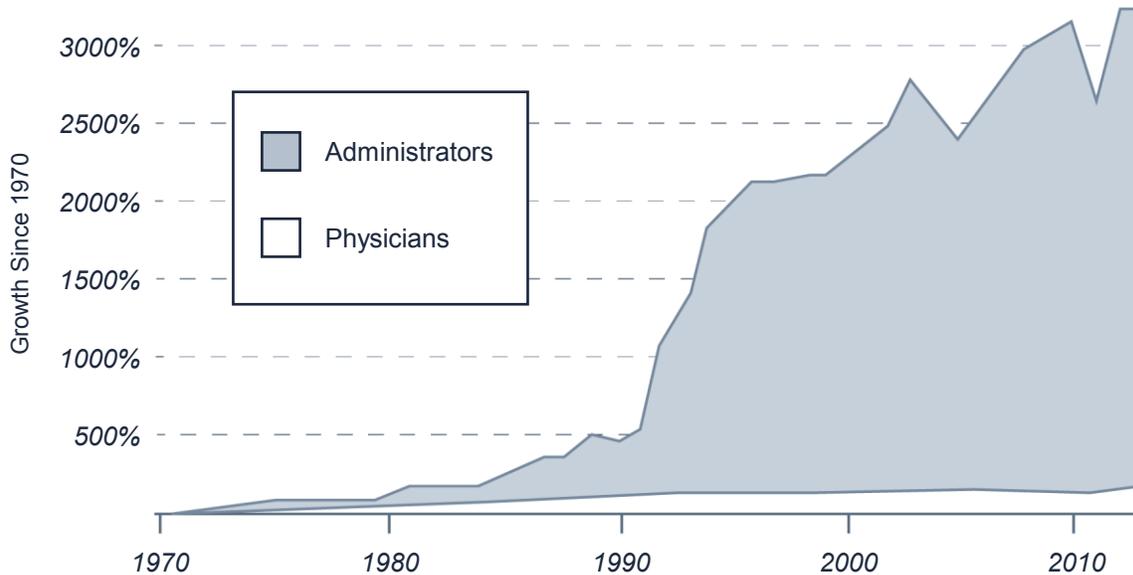
...To the Patient's Bed

- Diagnosing physician and hands-on nursing team
- Ongoing care management

Administrator, Cure Thyself

Clinical Workforce Only a Small Piece of the Puzzle

Growth of Physicians and Administrators¹, 1970-2013



1) Spans three occupational categories: management, non-financial administrative support, and financial administrative support.
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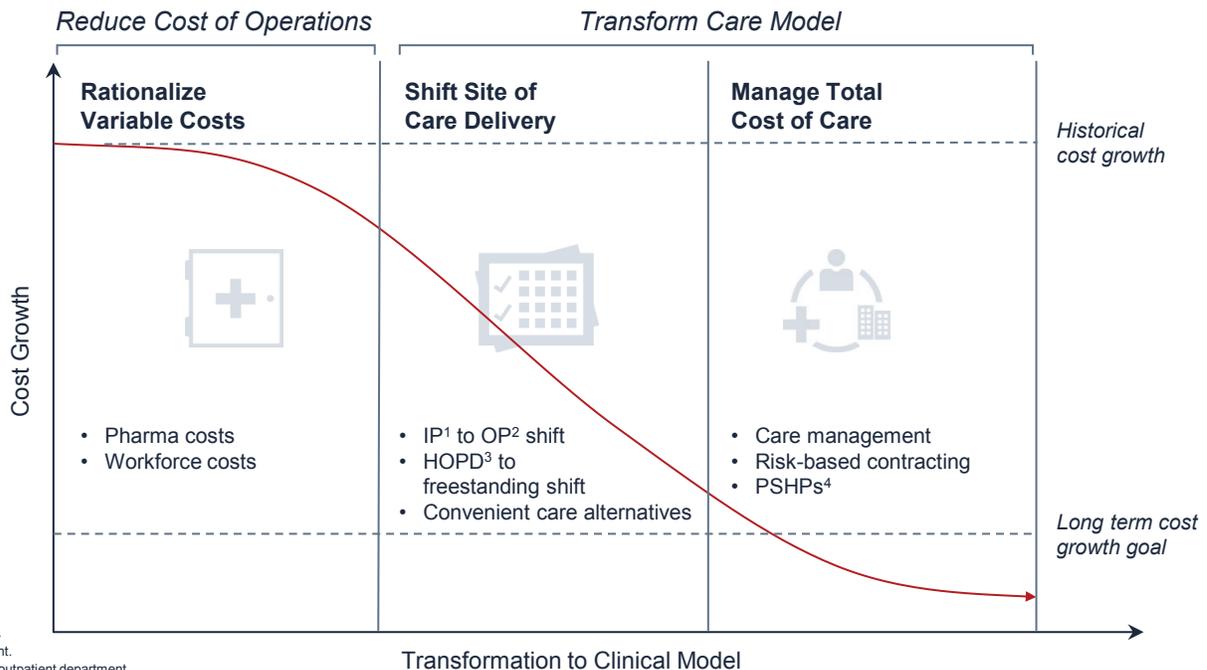
Source: Woolhandler, S, Himmelstein, DU. The National Health Program Slide-Show Guide. Center for National Health Program Studies, Cambridge, MA, 2014; Health Care Advisory Board interviews and analysis.

Transform Care Model

Improving Cost Structure Only the First Step

Future Demands Transformation of Care Model

Outlook for Cost Control



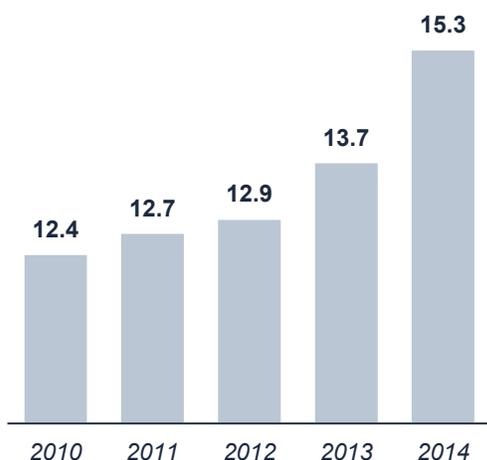
1) Inpatient.
2) Outpatient.
3) Hospital outpatient department.
4) Provider sponsored health plan.

Providers Move Up the Value Chain

But Health Plan Ownership Entails Distinct Challenges

Growth in PSHP¹ Enrollment

Millions



Far From a Slam-Dunk Investment

Modern Healthcare

“Health Systems With Insurance Operations Stumble in 2015”



“Catholic Health Initiatives to Divest Health Plan Operations”



“Neighborhood Health Plan Batters Partners HealthCare’s Finances in 2014”



“Mountain States Terminating CrestPoint Health Insurance Plans for Employees, Medicare Advantage”

1) Provider sponsored health plan.

Source: Avalere, “Medicare Advantage: 2016 National Snapshot,” May, 2016; Health Care Advisory Board interviews and analysis.

Payers and Providers Find Common Ground

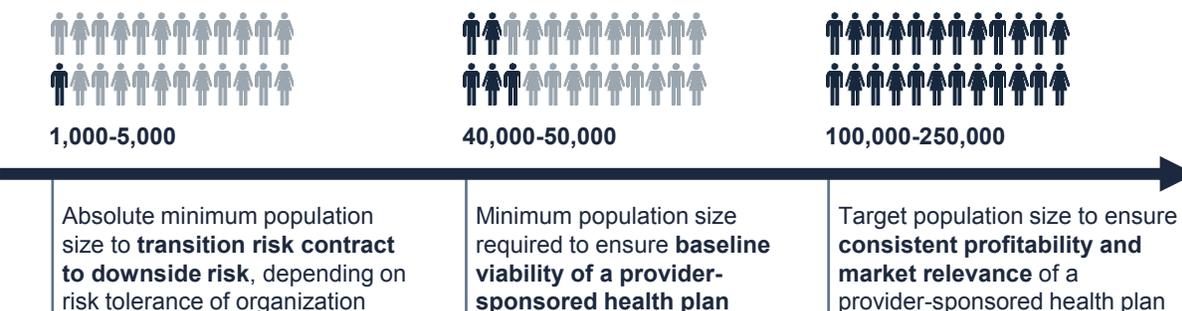
Health Insurance Partnerships, Joint Ventures Increasingly Common

 <p>Offers range of “accountable care solutions” from delegated risk to co-branding and joint ventures</p>  <p>4 Joint venture agreements with providers as of 2017</p> 	 <p>Launched CareAllies Inc. to help providers, including those launching their own plans, transition to value-based care</p>  <p>2 Joint venture agreements with providers as of 2016</p> 	 <p>Partnering with providers in select markets; after launching Vivity in 2014, expanded to Wisconsin in 2016</p>  <p>2 Joint venture agreements with providers as of 2016</p> 
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Source: Aetna, available at: news.aetna.com, accessed May 2017; Cigna, “Cigna launches new company to deliver proven systems, capabilities and management services to more health care providers,” June 2016; Modern Healthcare, “Anthem, Aurora Health Care plan joint insurance venture,” April 2016; Health Care Advisory Board interviews and analysis.

Risk Demands Substantial Scale

Benchmarks Heard in the Research



1) Based on 15.56% of anticipated annual health expenditures; assumes annual per-capita health expenditure of \$5,141.

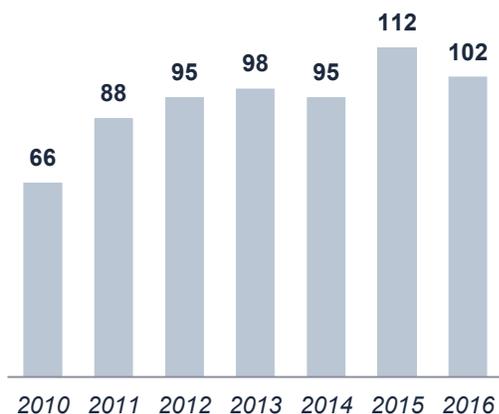
Source: Deloitte, "Provider-sponsored health plans: Positioned to win the health insurance market shift," 2015; American Academy of Actuaries and the Society of Actuaries, 2009; Health Care Cost Institute, "2015 Health Care Cost and Utilization Report," 2016; Health Care Advisory Board interviews and analysis.

Rebuild Health System

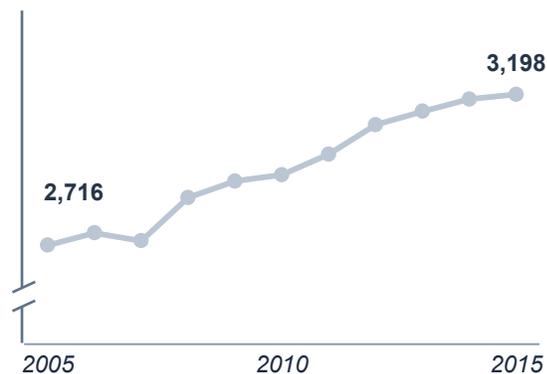
No Shortage of M&A Activity

Providers Actively Building Scale Through Consolidation

Hospital M&A Activity
Total Deal Volume



Number of Hospitals Part of a Health System



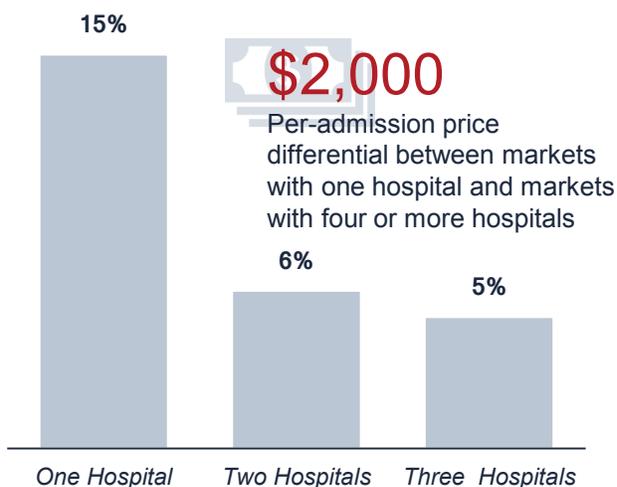
Source: Kaufmann Hall, *Hospital Merger and Acquisition Activity Continues Upward Momentum, According to Kaufmann Hall Analysis*, available at: www.kaufmannhall.com.; American Hospital Association, "2016 Chartbook: Trends Affecting Hospitals and Health Systems", available at: www.aha.org; Health Care Advisory Board interviews and analysis.

Not Exactly Delivering on the Value Proposition

Horizontal, Vertical Consolidation Have Added Cost to the System

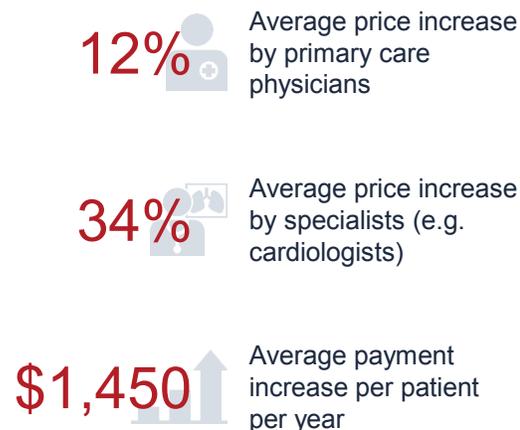
Reduced Hospital Competition Significantly Correlated with Increased Price

Percent Increase in Hospital Price Compared to Markets with Four or More Hospitals



Physician-Hospital Integration also Driving Up Prices

Physicians Practice Prices Increase After Health System Acquisition



Source: Evans, M., "Data suggest hospital consolidation drives higher prices for privately insured," *Modern Healthcare*, Dec. 15, 2015; AHIP, "Data Brief: Impact of Hospital Consolidation on Health Insurance Premiums," June 2015; Neprash, H. et al., "Association of Financial Integration Between Physicians and Hospitals With Commercial Health Care Prices," *JAMA Internal Medicine*, Dec. 2015; Health Care Advisory Board interviews and analysis.

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Lack of "Systemness" Often to Blame

Excess Capacity Remains Despite Consolidation and Utilization Declines

Fragmentation Evident Among Key Constituencies...



Facility-level Executives
Local leaders focused on maximizing performance of separate, often competing "fiefdoms"



Physician Workforce
Twin cultures of individualism, tribalism persist despite stronger contractual alignment



Frontline Staff
Rank-and-file workers unaware of, disengaged from system priorities

...And in Concrete Manifestations of Sub-par Performance

Operational inefficiency

\$190B Health care costs attributed to excess administrative costs

Unjustified clinical variation

1,200 days Extra inpatient LOS due to unjustified variation in total hip & knee replacements for typical¹ health system

Overgrown portfolios

1 in 3 Markets² with average inpatient occupancy rates under 50%

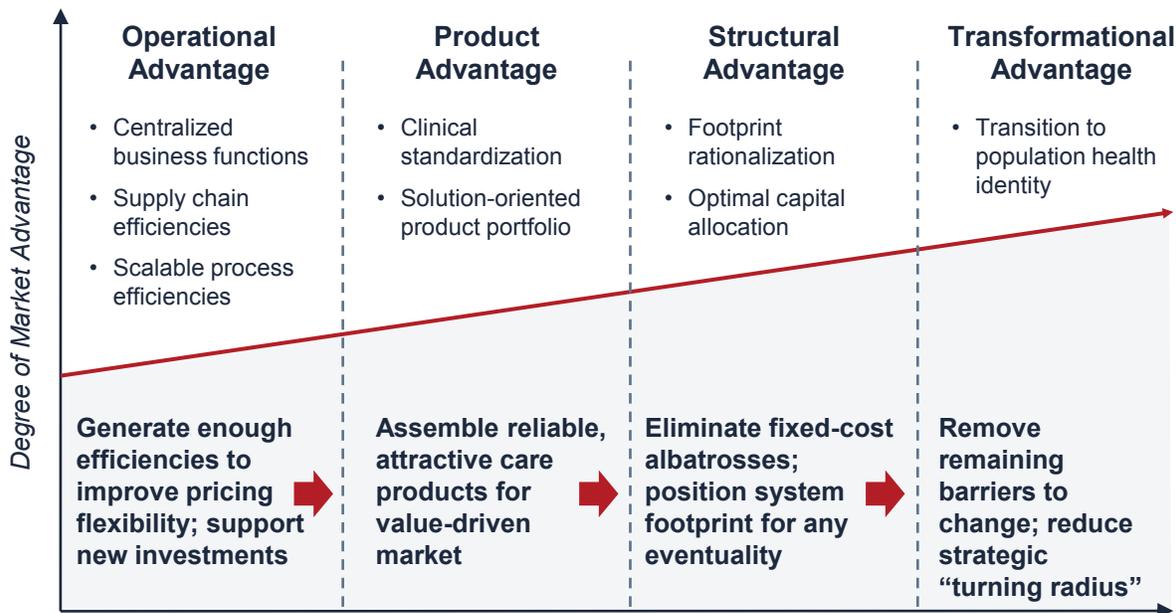
Sluggish response to market stimuli

25% Hospitals and health systems reporting no plans for total cost of care contracts before 2018

Source: MedPac, "Report to the Congress: Medicare Payment Policy," March 2014, http://www.medpac.gov/documents/reports/mar14_ch03.pdf?sfvrsn=0; Smith M, "Best Care at Lower Cost: The Path to Continuously Learning Health Care in America," 2013, <http://www.nap.edu/catalog/13444/best-care-at-lower-cost-the-path-to-continuously-learning>; Advisory Board analysis of Crimson Continuum of Care data, Physician Executive Council and Health Care Advisory Board, "The 'Systemness' Challenge in Quality and Safety" (Forthcoming, 2015); Health Care Advisory Board interviews and analysis.

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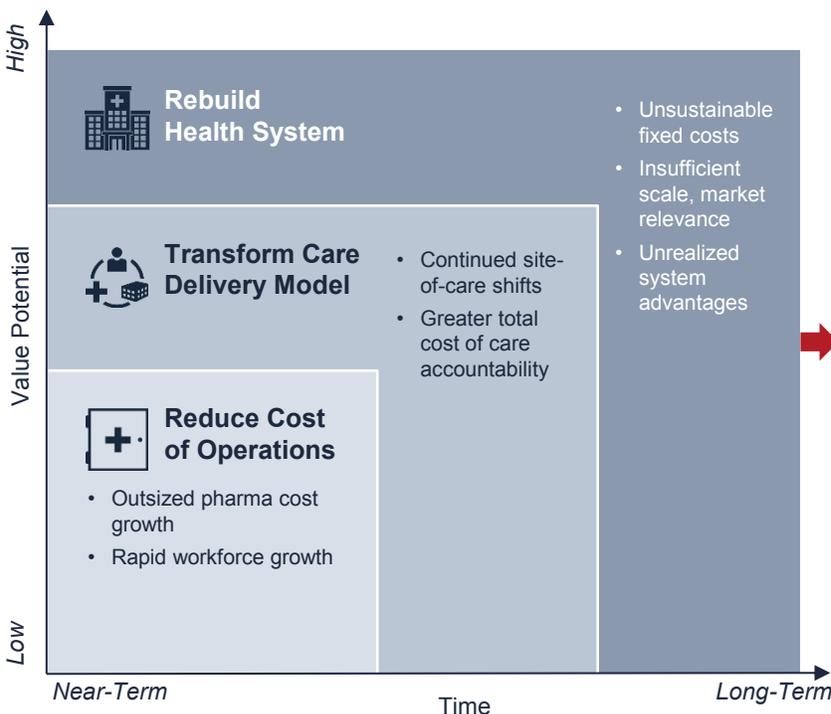
True Systems Able to Weather Any Storm



Our Leadership Challenge

Radical Delivery System Transformation Central to Future Success

Strategic Challenges



Strategic Imperatives

1. Identify opportunities to inflect pharma spending
2. Eliminate unwarranted care variation
3. Rightsize and reconfigure the clinical workforce
4. Expand to new sites of care
5. Reevaluate risk strategy, transition path
6. Reallocate services across the system
7. Eliminate excess capacity
8. Capitalize on internal advantages of scale
9. Embrace radical growth strategies



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