



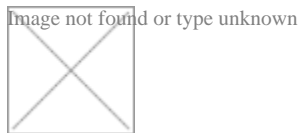
Weekly Checkup

Reference Pricing: A Possible Payment Model

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In the search for the holy grail of health care cost containment, economists and policy wonks have offered up a pricing structure referred to as “reference pricing.” Insurance providers set a reference price for a particular procedure and agree to reimburse hospital charges incurred up to that price. If beneficiaries chose to seek more expensive treatment, they will be responsible for paying the additional amount out of pocket. The policy is especially appealing for its emphasis on price transparency and price-conscious health care.

Already tested with some success in the California Public Employees Retirement System, we examine how this reference pricing might be implemented in Medicare.^[1] Since the policy is more effective in the context of elective, non-emergency procedures, we examine the application of reference pricing to hip and knee replacement surgeries.^[2] The chart below shows the distribution of prices charged to Medicare by hospitals providing 10 or more major joint replacements during 2011. The charges ranged from \$7,500 to \$30,000, but roughly half of all procedures were performed for less than \$10,000.^[3] If Medicare were to implement a \$10,000 reference price, it could reduce spending on knee and hip replacement surgeries by over \$1 million.



^[1] This example simplifies significant geographic and demographic variation that would need to be taken into account when designing a nationwide reference price.