



Peterson-Milbank
Program for Sustainable
Health Care Costs

Establishing the Target Methodology & Value



The process of setting a target represents an opportunity to educate, engage with stakeholders, and develop buy-in among payers and providers whose performance will be measured against the target.

States should strive to be clear and transparent about why the target is needed and the factors to consider in setting the target methodology and value. This section describes key steps in this activity.

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Identify a Target Methodology and Calculate the Value

The methodology used to determine the target value is critical in helping stakeholders, including the public, understand the policy and reasoning behind the target. For the most part, states have tied their targets to measures of the larger economy, so future health care cost growth does not exceed overall state economic growth, and to a measure of household finances such as income growth.

States have considered indicators that fall into three general categories:

1. **State economic output:** Such measures represent the total value of goods produced and services provided in a state during a defined period. Using this type of measure sets an expectation that health care costs should not grow faster than the state economy, and that state spending on health care should not take up a greater proportion of the state's overall spending in the future than it does currently.
2. **Inflation:** Inflation measures the decrease in the purchasing power of money, reflected as increases in prices consumers pay for goods and services. Using a measure of inflation signals that health care costs should not grow faster than the increase in the cost of goods and services, tying the target to consumers' experiences at the grocery store or shopping mall.
3. **Income or wages:** These measures represent the individual earnings of a state's population and the ability to afford to live in and purchase goods and services in the state. Tying the health care target to such measures puts health care in the context of individual and family experiences and signals that spending on health care should not take up a greater proportion of a family's budget than it currently does.

If a state chooses an economic indicator as its target methodology, it must then calculate the growth rate of that indicator to derive an initial target value. This can be done using historical or forecasted growth. While using historical growth reflects actual experience, it can be volatile from year to year. Alternatively, long-

term forecasted growth is estimated using historical experience but smooths out significant swings caused by short-lived economic booms or busts, which are poor predictors of future trends.

Before finalizing the target value, states should consider short- and long-term historical cost growth to ensure the target is reasonable and set at a level that would put appropriate downward pressure on cost growth. Some of the resources available to states to understand historical spending include the following:

- **All-payer claims database (APCD):** These databases include medical, pharmacy, and sometimes dental claims collected from private and public payers. For states that have an APCD, this is the best source for data on fully insured commercial, Medicare, and Medicaid claims spending, so long as the APCD has been tested and the data are clean and ready to use.
- **State employee health benefit experience:** For states that do not have an APCD, data from the state employee health plan can serve as a proxy for commercial market experience.
- **Medicaid Management Information System (MMIS):** States may choose to use claims data directly from their MMIS to understand Medicaid spending.
- **Insurer rate filing data:** In states that require submission of spending information as part of the rate review process, insurer rate filing data can be a source of trend information for commercial spending.
- **Publicly available research:** The Health Care Cost Institute, the Institute for Health Metrics and Evaluation, the State Health Expenditure Accounts, and FAIR Health provide national, regional, and/or state reports on cost growth.

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Determine the Target Duration and Any Adjustments to the Methodology or Value

If not previously determined through executive order or legislation, the state must decide how long to keep the target in place. States have set targets for periods ranging from four to 15 years. Four years is the minimum recommended length for the target policy because 10 to 14 months are needed after the end of a performance year to assess and publish performance against the target and to make changes in contracts or payment policies that could change cost growth trends.

States can also opt to adjust the target value, or the target methodology, when setting targets over multiple years. By adjusting the value, states can help providers and payers adjust to a target over time and accelerate the drive to reduce health care cost growth. For example, New Jersey based its target methodology on 25% potential gross state product (PGSP) and 75% median income, resulting in a target of 3.2%. New Jersey then used “add-on factors” to adjust the value to ease the transition for stakeholders. Nevada took a slightly different approach, which yielded similar results. Rather than adjusting the value of the target, Nevada adjusted the methodology itself over the course of five years. Nevada used a changing blend of forecasted median wage and PGSP, with increasing weight placed on forecasted median wage in future years. The aim was to signal that affordability is a state priority and that, over time, health care cost growth should more closely reflect individuals and families’ ability to purchase goods and services.

Monitor for Conditions That Might Call for Revisiting the Target Methodology or Value

States should view the target as a long-term policy. However, recognizing that the landscape and economic circumstances of a state may change significantly in ways that are difficult to predict (e.g., the COVID-19 public health emergency), states may opt to revisit the target methodology at intervals or in response to external circumstances. For example, Washington developed a provision that would allow it to consider changes to its target or target methodology in the event of extraordinary circumstances, including highly significant changes in the economy or health care system. Delaware, on the other hand, annually reviews the methodology.

The sharp rise in inflation in late 2021 that persisted through 2022 led some states to review their target values and methodologies. States can consider several options when deciding whether and how to update target methodologies and values based on such circumstances:

- Recalculate the value of future targets **using new inputs**.
- Revise the target **methodology**.
- Retain existing target values and **contextualize** short-term trends resulting from elevated inflation.

Resources

Data on Health Care Spending and Growth

- The Health Care Cost Institute's [Health Care Cost and Utilization Reports](#) examine trends in health care spending for individuals with employer-sponsored insurance. Users can explore spending by health care service category.
- The [National Health Expenditure Accounts](#) provide historical and projected spending on health care in the United States. Spending is presented by type of good or service (e.g., hospital care, retail prescription drugs) and source of funding (e.g., Medicare, Medicaid, private health insurance, out-of-pocket).
- The [State Health Expenditure Accounts](#) provide state level aggregate and per capita estimates of health spending for the Medicare, Medicaid, and private health insurance markets from 1991 to 2020.

Data on Economic Indicators That May Be Used to Determine the Target Methodology

- The Congressional Budget Office's [Budget and Economic Outlook Report](#) contains national data on potential labor force productivity and projected inflation that can be used as inputs to calculate PGSP.
- The Federal Reserve Bank of St. Louis' research data portal, [FRED](#), provides access to over 800,000 economic indicators that can be sorted by state or geographic region.

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To read the complete playbook, visit <https://www.milbank.org/publications/making-health-care-more-affordable-a-playbook-for-implementing-a-state-cost-growth-target>.