A Competitive Bidding Approach to Medicare Reform

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Organization of our talk

1. Goals and assumptions
2. What is competitive bidding?
3. Effects
   - Quality of care
   - Medicare savings
   - Financial effects on beneficiaries
4. Conclusion

I. Goals and Assumptions

What competitive bidding can accomplish

1. Aligns the price Medicare pays with the underlying costs for efficient plans to produce it
   - To degree possible, reveals actual costs
2. Savings – possibly a lot, depending on how it's designed
3. Preserves the entitlement benefit at no added premium (at least one option in every county)
4. Preserves the traditional Fee-for-Service (FFS) program, though under price competition with MA plans
   - All health plans, including FFS, submit bids
5. Relatively easy to implement – Medicare already doing virtually all that's required

If competitive bidding is so wonderful, why don't we have it already?

- Medicare has tried to have it!
  - Since 1980: ~10 efforts to demonstrate/phase-in competitive bidding for some part of Medicare benefit, including MA plans
  - Almost all have failed
  - Not due to practical problems or failure to save money – all demos that took bids provided/promised savings
  - Political opposition has been the key obstacle to competitive bidding
  - Overcome recently on DME (still vulnerable) and Part D
- Was proposed by Democratic and Republican administrations
- But killed by Democrats and Republicans in Congress
  - Abetted by courts (lawsuits brought by health plans and providers)
- The only reason we're having this conversation today – Medicare's difficult financial situation may override political opposition to true competitive bidding for health plans

Key assumptions

1. Medicare is a *defined benefit* program
2. The government should buy that benefit at the economical cost of producing it in each market area
3. The entitlement should be to the benefit, not to a particular plan that offers it
   - Traditional FFS and MA plans treated equally
   - The "overpayment" critique applies to both FFS and MA plans
4. Provision must be made for poor beneficiaries
   - Give targeted help to the people who need it most
   - Competitive bidding is compatible with almost any scheme of assistance to needy beneficiaries.

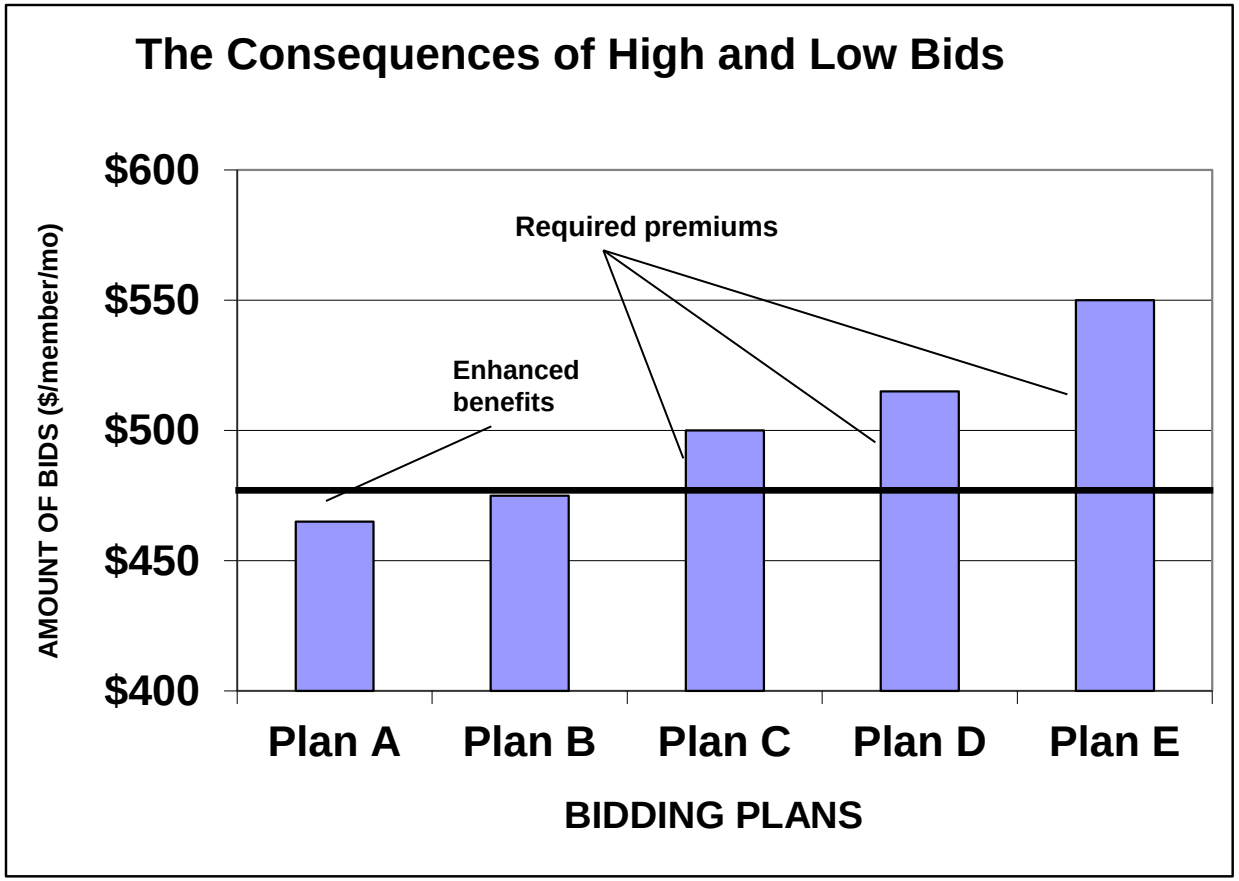
II. What Is Competitive Bidding?

How does competitive bidding work?

- In competitive bidding, Medicare does a set of familiar things
  - Qualifies bidders
  - Takes bids for cost of the statutory "entitlement" benefits for a "standard" enrollee
    - FFS 'bid' = average FFS cost of care per county
  - Pegs its contribution to some function of the bids
    - E.g. lowest bid or 2nd lowest bid or median or….
  - Risk adjusts payments
- Note: does <u>not</u> exclude any plans (unlike bidding model for durable medical equipment)

Then what happens? Competitive Bidding in One Picture

- **HMOs and traditional Medicare submit bids on the entitlement benefit package**
- **Use the bids to determine a "Benchmark Price" (e.g. the second lowest bid)**
- **Leave it to consumers to decide if more expensive plans are "worth it"**



The only realistic way to discover the cost of providing the Medicare benefit

- With administrative alternatives (e.g. current benchmarks for MA plans) information about the costs of care flows
  - from the government – knows very little about actual MA costs
  - to health plans – know as much as is possible to know
- Competitive bidding *changes the source* of cost information
  - MA plans tell the government how much it costs them to care for Medicare beneficiaries. FFS bid simply computed.
  - Bids are used to establish the benchmark price
  - The system rewards low bids and penalizes high bids → encourages more honest bids
- This homily from Economics 100 remains the most compelling justification for competitive bidding
  - Even if Medicare were not in financial distress: why pay more than efficient quality plans – public or private – can offer?

Distinguishing this proposal from others

1. **Proposals ("premium support," others) vary in how they treat traditional Medicare, i.e., the public FFS program**
   - Does the bidding program envision an important role for FFS in Medicare?
   - Is FFS included in the bidding, or does bidding only apply to MA plans?

Our proposal: FFS is a bidding plan <u>and</u> a key to the system

- Need a mixed system of public and private plans.
- FFS
  - can offset provider market power in bidding in some areas
  - has universal availability – a bidder in every service area

2. Is the proposal for a defined benefit or a defined contribution?

- Premium support programs often include caps on the government payment
  - – e.g., GDP per-capita growth + 0.5 %pts
  - The "benchmark" is the lower of the cap or plan bids.
- Result : shifts to beneficiaries, providers, and others the risk of cost growth over the cap

Our proposal: defined benefit

- Benchmark based on the bids, not a cap
- For <u>all</u> beneficiaries: at least some option(s) provide the entitlement benefit for no added premium
- But: no cap means no certainty of a limit

III. The Effects of Competitive Bidding

- Quality of care
- Medicare savings
- Financial effects on beneficiaries

Quality: no evidence of change

- No evidence that quality of care would suffer in shifting from traditional Medicare to MA plan
- The bidding contract could be a platform for enhanced quality monitoring (there may be good reasons for this)
  - Note DME competitive bidding: enhanced qualification

Savings from competitive bidding

- Calculated savings from a fully-implemented competitive bidding system (Feldman, Coulam, and Dowd, 2012)
  - Used very conservative assumptions
- The results compared to ACA:
  - 5.6 percent savings
  - $339 billion 10-year savings through 2020
- If FFS is excluded from the bidding, savings are substantially reduced (~75 percent less)
- These savings come from somewhere → effects on beneficiaries (won't address effects on providers)

Figure 1: Changes in Payments for FFS and MA Enrollees (assuming no one chooses different plan)

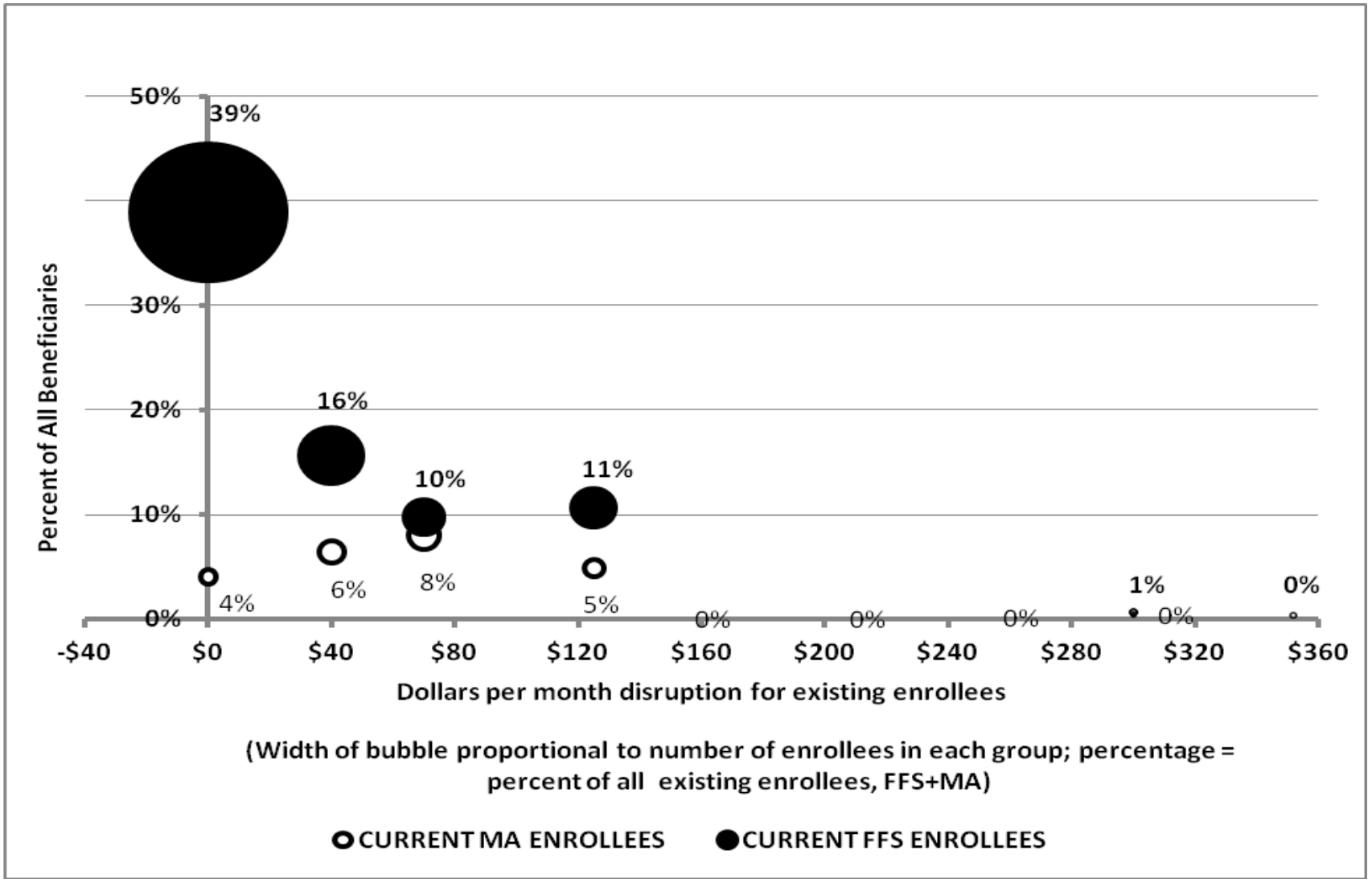


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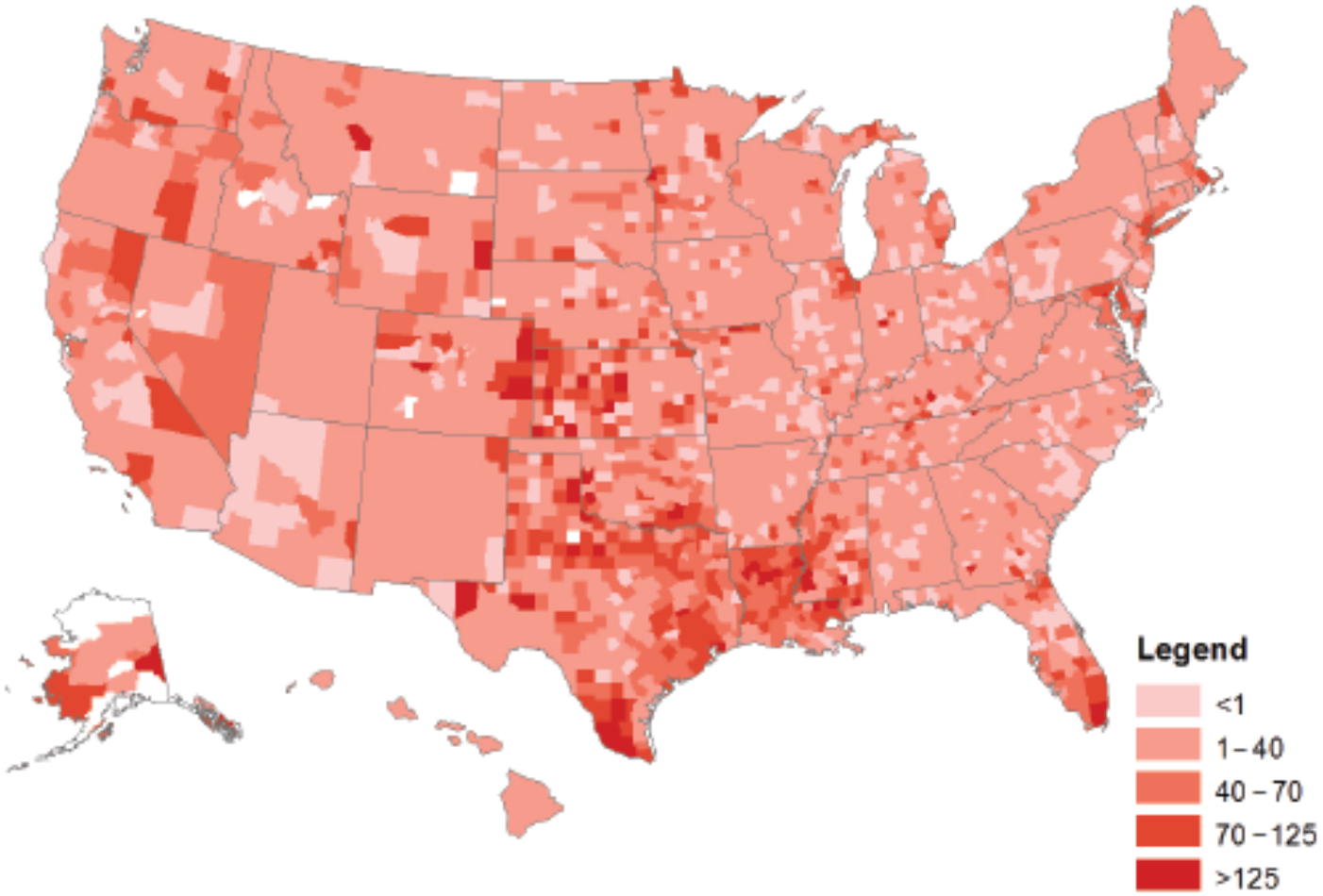
Figure 2.

ENROLLMENT-WEIGHTED (FFS + MA) PAYMENT CHANGES FROM BIDDING



SOURCE: Authors' calculations.

Financial effects on beneficiaries #1: Some traditional FFS enrollees pay premium to stay in FFS

- If FFS a "high" bidder, have to pay out-of-pocket premiums to remain in traditional Medicare
- BUT: traditional FFS may be in a better position to compete than is casually assumed
  - Feldman, Coulam, and Dowd (2012): traditional FFS is the low bidder in counties in which 50 percent of beneficiaries live.
  - Implication: correspondingly fewer enrollees have to pay premium to stay in FFS

Financial effects on beneficiaries # 1: Enrollees in Traditional FFS Medicare [continued]

- Some evidence: most FFS enrollees in high FFS areas would opt to pay higher premiums to stay in FFS → "financial disruption"
- Low-income beneficiaries are most likely to leave FFS, although many already have left
- High FFS bids aren't only a bad
  - Private plans realize they can gain enrollment by submitting low bids
  - The result: lower bids, greater Medicare savings, and more free benefits for beneficiaries

Financial effects on beneficiaries #2: 4 of 5 private plan enrollees pay to stay in MA and to maintain current benefits

- Loss of 'free' benefits – especially where plans overpaid
- Private plans offer these benefits because they are paid more than the cost of traditional Medicare (and more than their costs)
  - ACA reduced this overpayment versus FFS to 7 percent
  - Competitive bidding would complete this reduction – indeed, go further where plan bids < FFS
- Discussion needed about transition arrangements – to avoid abrupt loss of benefits, given reasonable beneficiary expectations

Financial effects on beneficiaries #3: The special case of low-income beneficiaries

- Low income beneficiaries will be affected in both ways:
  - They will lose “free” benefits in former high payment areas
  - They might have to change health plans, to avoid paying an additional premium
- But: use targeted assistance to protect low income beneficiaries where needed
  - There are precedents
  - The cost: reduces savings

IV. Conclusion

Conclusion: what are the alternatives to our proposal?

- The alternatives aren't great
  - Arbitrary cuts → burden on providers, beneficiaries, others
  - Payment reform (e.g., VBP, ACOs): promising, but untested
  - Bidding with payment caps (premium support): puts the risk of cost growth on beneficiaries, providers
  - Bidding without FFS: saves much less money, makes system less competitive

Competitive bidding with FFS/without a cap is a better solution

1. Saves more money
   - Reduces overpayments (to FFS and MA) in a defensible way
   - Without the disadvantages – or the certainties – of a cap
2. No evidence of an effect on quality
3. Defends the defined entitlement benefit, at no added premium for beneficiaries
4. Effects on beneficiaries amenable to transition methods and targeted assistance to low-income beneficiaries
5. Preserves the traditional FFS program, though under price competition
6. Is a tested, administratively feasible approach

Final points

- Is consistent with other reforms being contemplated
  - Does not block the way to quality bonuses, value-based purchasing, ACOs, etc.
- Is the right place to end up – it gets the prices right!
  - Though far from the complete solution
- Don't minimize the extent of the reform
  - Recognize reasonable beneficiary needs and expectations to buffer the transition to reform

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