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Medicare Advantage and the Federal Budget

The House Budget Committee held a hearing last month on "Medicare Advantage and the Federal Budget." The purpose of the hearing was to develop a better understanding of the additional budgetary costs of Medicare Advantage under its current financing structure, who pays those costs, and who benefits. Below are some highlights of testimony from the hearing.

Medicare Advantage costs 12 percent more than traditional Medicare. Both the Congressional Budget Office (CBO) and the Medicare Payment Advisory Commission (MedPAC) estimate that payments to Medicare Advantage (MA) private plans are 12 percent higher than per-capita costs in traditional fee-for-service (FFS) Medicare. The extra costs occur because the MA payment structure is based on county-level benchmarks that exceed average fee-for-service spending in many places. CBO projects that setting the benchmarks equal to fee-for-service would save $150 billion over ten years.

There is no conclusive information on what MA enrollees get in exchange for the extra spending. The typical MA plan must provide enrollees with extra benefits or reduced cost-sharing. However, the extra benefits offered vary widely across plans. MedPAC Executive Director Mark Miller testified that there is no consistent data available on what benefits are actually being used by MA enrollees. And there is no evidence that enrollees experience better health outcomes under MA plans. "We do not have sufficient reporting requirements, given the amount of federal money that's going to these [plans], to see what works and what doesn't," CBO Director Peter Orszag said in his testimony. Not all of the 12 percent excess payment represents extra benefits. Some of it – although exactly how much is not publicly known – goes to marketing, profit, and other administrative costs.

Medicare Advantage is unlikely to ever produce budgetary savings. Supporters of the current system argue that overpayments are necessary to entice plans into the market, but that, over time, competition will lead to efficiencies and save the government money. Dr. Orszag testified, however, that under the current payment system, private plans on average would have to be able to provide basic Medicare benefits at about half the cost incurred in the FFS program before the government would save any money – an outcome he described as "implausible." Right now, private plans on average are providing basic Medicare benefits at 99 percent of the FFS cost.

Medicare Advantage is accelerating Medicare trust fund insolvency. Dr. Miller and Dr. Orszag noted that the excess payments to MA plans shorten the projected life of the Medicare hospital trust fund by two years.

Medicare Advantage is not a reliable form of protection from out-of-pocket costs. Beneficiaries can end up paying more in MA. Patricia Neuman, vice president and Medicare Policy Project director for the Henry J. Kaiser Family Foundation, showed in her testimony that an MA enrollee's out-of-pocket costs can vary widely and may exceed FFS out-of-pocket costs in some cases, depending on the MA plan and the enrollee's health circumstances. "It's clearly up to the individual beneficiary – the seniors – to choose which plan is going to end up saving them the most money. And, given the number of plans that are in their area and the wide variety of benefits, that could sometimes be a tall order," Dr. Neuman said. Robert Wah, a member of the American Medical Association Board of Trustees, said physicians and patients are besieged by fine-print details "that make it very hard to understand what they're signing up for." Dr. Miller said it is "somewhat concerning" that the government pays MA plans more than traditional FFS, and yet MA beneficiaries, depending on their health path, may still end up exposed to higher cost-sharing.

The testimony indicated that minority beneficiaries do not rely disproportionately on Medicare Advantage. Dr. Neuman testified that MA enrollment rates are similar for whites and African Americans. Hispanics are more likely to enroll in MA, but that is because the Hispanic population is concentrated in places like Florida and California with a high concentration of MA plans.

The testimony indicated that low-income beneficiaries do not rely disproportionately on Medicare Advantage. About half of all beneficiaries in MA as well as in traditional Medicare have annual incomes below $20,000. Medicaid is the primary source of supplemental assistance for low-income Medicare beneficiaries. Dr. Neuman pointed out that MA was not designed as a program for people with low incomes. A low-income MA beneficiary who becomes ill and needs medical care could end up with out-of-pocket costs that consume a significant share of income.

There are more targeted and effective ways to protect beneficiaries of modest incomes from out-of-pocket costs. A set of provisions collectively known as the Medicare Savings Program exists to help beneficiaries of modest means with out-of-pocket medical costs. The new prescription drug benefit also offers a low-income subsidy. Several witnesses suggested that if the policy goal is to protect low-income beneficiaries from out-of-pocket costs, expanding these programs would be a more effective use of funds than continuing to subsidize MA plans.

Taxpayers and traditional Medicare beneficiaries pay the added cost of Medicare Advantage. The 12 percent added cost for MA plans is borne by taxpayers and by all Medicare beneficiaries who pay Part B premiums. This subsidy raises questions of fairness. The majority of Medicare beneficiaries – four out of five – are not in MA plans. Many of them have modest incomes, Dr. Neuman noted, yet they pay higher Part B premiums (about $2 more per month) to support the MA payment system.

The current Medicare Advantage payment structure rewards inefficiency. The original intent of a private-plan option in Medicare was that private plans would have incentives to be more efficient than FFS Medicare, and they would use the savings from those efficiencies to offer extra benefits in order to attract enrollment. The MA payment mechanisms, however, "send signals inviting and rewarding inefficient plans," Dr. Miller said.

Private fee-for-service plans are the most expensive and least accountable category of Medicare Advantage. "Private fee-for-service plans may be the most striking example of what's wrong with the system," Dr. Miller said. These plans charge nine percent more than traditional Medicare to provide the basic FFS benefit, and then they receive additional money on top of that for extra benefits, for total payments that exceed Medicare FFS by 19 percent. And private fee-for-service plans are exempt from many of the reporting requirements that apply to other types of Medicare Advantage plans. Private fee-for-service is the fastest-growing sector of MA.