Arnold Ventures

Setting Medicare on a Fiscally Sustainable Path for Future Generations

PROBLEM: The Medicare program faces long-term fiscal challenges. Medicare spending has been increasing due to rising per capita health care costs and the aging of the baby boomer generation, which is leading to higher enrollment in Medicare. It is projected to consume nearly one-fifth of the federal budget in the next decade. This puts pressure on Medicare beneficiaries, who must pay higher premiums, and on taxpayers. In addition, Medicare's Hospital Insurance trust fund is projected to be insolvent by 2026. At that point, Medicare will not be able to fully cover its spending for hospital stays, skilled nursing facilities, hospice, and some home health care services for its beneficiaries.

SOLUTIONS: Congress should take a balanced approach to improving Medicare's fiscal sustainability challenges by addressing the three areas highlighted below. Achieving long-term sustainability will likely require a mix of spending reductions and new revenues. Enacting reforms that slow the growth of Medicare spending and strengthen the program's financing will also help extend the life of the Hospital Insurance trust fund in many cases.

1 Reduce overpayments and ensure efficient payments to traditional Medicare providers

Traditional Medicare operates on a fee-for-service basis that provides little incentive to ensure Medicare beneficiaries are receiving efficient, high-value care. Payments to certain providers also far exceed the cost of providing care. Congress should address overpayments to providers and align payment incentives across providers and service settings to encourage efficient care delivery in the lowest cost setting.

2 Reduce overpayments and improve competition among Medicare Advantage (MA) plans:

Medicare Advantage (MA) plans provide an alternative to traditional fee-for-service Medicare. In the MA program, Medicare pays private insurance plans to coordinate and manage health care coverage for its beneficiaries. While initially intended to be more efficient, Medicare has a history of paying MA plans more than fee-for-service. Solutions include addressing areas of excessive payments to MA plan and reforms to drive greater competition among plans.

3 Strengthen Medicare financing through revenue increases

Medicare's Hospital Insurance trust fund is primarily financed through payroll taxes. However, as the U.S. population ages and costs rise, Medicare's current financing is unequipped to handle the increased demand. Congress should consider raising additional revenue dedicated to the Medicare trust fund, including by closing tax loopholes.

1. REDUCE OVERPAYMENTS AND ENSURE EFFICIENT PAYMENTS TO PROVIDERS

Post-Acute Care (PAC)

- **Establish a unified payment system for post-acute care** providers to align payment incentives across providers and ensure that payments are based on the most appropriate, cost-effective site of care given a patient's characteristics. Currently, there is substantial overlap in the patients treated in different post-acute care settings, and consequentially, Medicare pays different amounts for similar patients.
- **Reduce excessive payments to post-acute care providers** by lowering or eliminating their payment rate updates to better align PAC provider payments with their costs. It is estimated that in some PAC settings, Medicare payments average over 11% higher than costs.
- **Reduce the hospice aggregate cap and eliminate the payment rate update** to reduce overpayments to hospice providers, who regularly have high aggregate Medicare margins.

Hospitals

- **Pay outpatient hospital departments the same Medicare rate as physician offices** for services that can safely be performed in a lower cost setting. This ensures that Medicare is not paying a higher price for the same service based on setting alone and reduces provider incentives to vertically consolidate.
- **Reduce and reform payments for Graduate Medical Education (GME)** to better align GME with the costs associated with teaching and require more accountability from its recipients for achieving education and training goals. Currently, federal payments for GME considerably exceed hospitals' actual teaching costs.
- **Reduce Medicare's coverage of bad debt** that occurs when Medicare pays additional dollars to cover services that were not paid in full by the beneficiary or other health payer.

Prescription Drugs

- **Lower the cost of prescription drugs in Medicare** by implementing a variety of proposals aimed at reducing Medicare spending in Parts B and D. Please refer to the Arnold Ventures Policy Focus: Drug Pricing for specific policy options.

2. REDUCE OVERPAYMENTS AND IMPROVE COMPETITION AMONG MEDICARE ADVANTAGE (MA) PLANS

Overpayments to MA Plans

- **Reform the quality bonus program** that allows a substantial majority of plans to qualify for bonuses and is financed by additional Medicare dollars, unlike quality incentive programs in traditional Medicare. An alternative to the current system could be a budget neutral program that redistributes quality bonuses/penalties among plans.
- **Improve risk-coding adjustments in MA** to fully account for the coding differential between MA plans. Evidence suggests that MA plans often engage in aggressive risk coding that makes MA beneficiaries appear sicker than similar beneficiaries in traditional Medicare, resulting in overpayments to plans.

Competition in MA

- **Implement competitive bidding among MA plans** and determine payments to plans based on the bids of other MA plans. This would increase price competition among plans and encourage them to offer higher quality, lower cost plans.

3. STRENGTHEN MEDICARE FINANCING THROUGH REVENUE INCREASES

Revenue Options

- **Close tax loopholes and subject all personal income to Medicare taxes** to ensure that all income for qualifying individuals is subject to either the Medicare payroll tax or the net investment income tax, improving the equity of Medicare taxes across income/wealth levels and types of income.
- **Eliminate the employer-sponsored insurance exclusion for the Medicare payroll tax** to increase the amount of income subject to Medicare payroll tax and limit incentives for companies to offer inefficiently generous health plans due to the open-ended tax subsidy.
- **Raise the Medicare payroll tax** rate to increase revenue financing the Medicare trust fund, which has been increasing at a slower rate than Medicare outlays.

Additional Policies:

- **Modify Medicare's benefit design** by replacing the current Part A and Part B fee-for-service (FFS) benefit structure with one that includes an out-of-pocket maximum and simplifies deductibles and coinsurance to encourage efficient service use and protect beneficiaries from high out-of-pocket costs.
- **Discourage the purchase of Medigap plans** through an additional charge on supplemental insurance or prohibit Medigap plans from providing first-dollar coverage to discourage unnecessary service utilization.