REFORMING MEDICARE

Option: Increase Supplemental Plan Costs and Reduce Coverage

Even with Medicare coverage, seniors are often left with significant health care costs, so many people purchase supplemental private insurance coverage (such as Medigap plans) to reduce their out-of-pocket expenses. One proposal would charge more for certain types of supplemental plans, such as those that cover all costs so seniors incur no out-of-pocket expenses themselves. Other proposals would limit what Medigap supplemental insurance plans will cover. For instance, they could prevent Medigap from covering the first $500 of a Medicare beneficiary's out-of-pocket costs, and only cover 50 percent of the remaining charges.

Argument for:
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Argument against:
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Most Medicare beneficiaries have health insurance coverage in addition to Medicare. Some coverage comes from previous employers and some from Medicaid. Roughly one Medicare beneficiary in six buys private insurance themselves, called Medigap. The reason people want such coverage is straightforward: There are gaps in Medicare coverage. The Hospital Insurance deductible is large. Medicare does not cover all of the cost of very long stays in a hospital or a nursing home, and beyond a certain point Medicare stops paying altogether. The cost of lengthy illnesses can be financially crushing, despite Medicare benefits.

So, what is the problem? The problem is not that people want to and are able to buy additional coverage. People should be free to use their own money to protect themselves from financial risk. But the price for such coverage should accurately reflect the expected cost of the added protection. At present it does not.

The additional insurance that Medicare enrollees buy increases the use of Medicare-covered services but covers only covers only part of the cost of this increased service use. Taxpayers pay the rest. For example, a person may stay a bit longer in a skilled nursing home if supplemental insurance covers the $144.50 daily copayment for stays longer than 20 days. Many supplemental insurance plans cover the copayment for the added days. But the copayments do not cover the full costs of the additional days, and Medicare covers the rest.
No one believes that people should be prevented from buying supplemental coverage altogether. But many are worried because current policies increase overall Medicare spending. Some reform proposals would change Medigap by raising the amount that Medicare enrollees must pay themselves and reducing what Medicare pays, especially at the beginning of an episode of illness. All such proposals would maintain or improve protection in one way—by placing a hard cap on total out-of-pocket expenses. This change would also reduce the price of Medigap insurance. Dual eligibles—those Medicare beneficiaries who also qualify for Medicaid (a government program for people with low incomes)—and those covered by supplemental insurance from previous employers would be unaffected. People who do not use many Medicare services would gain from such a shift, as they would save more from lowered Medigap premiums than the increase in what they would spend directly for medical services. But heavy users of Medicare services would see an increase in their total medical costs.

If some cuts in Medicare spending prove to be necessary in order to keep the Medicare program financially sound, limits on how Medigap insurance pays for services, in addition to those in current law, would have the side benefit of lowering Medigap premiums and might deter some people from using services that produce few benefits. But no reduction will be painless.

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It would be unwise to increase the premium amounts for Medicare supplemental insurance, such as Medigap, or to decrease the amount of coverage available to enrollees under these policies. There is no evidence that these reforms would deter Medicare beneficiaries from using unnecessary health care services. Further, Medigap reform proposals in particular have an unfair effect on lower-income Medicare enrollees and those in poor health.

About 20 percent of Medicare beneficiaries purchase some type of Medigap plan to help cover Medicare cost-sharing. A majority of these policies (59 percent) provide “first dollar” coverage, which protects enrollees from having to incur any out-of-pocket costs for Medicare services in exchange for a monthly premium. Supplemental insurance programs like Medigap make health care expenses more predictable and therefore easier to manage on a fixed income.

Critics say that generous Medicare supplemental policies, such as first dollar Medigap plans, encourage Medicare beneficiaries to use more and sometimes unnecessary health care services. Proposals to reform Medigap and other supplemental private insurance would require beneficiaries who purchase these plans to pay more for services, or tax the purchase of these first dollar plans.

There is, however, limited evidence to support the claim that first dollar coverage results in an increase in unnecessary use of services. In fact, there is some evidence that beneficiaries without supplemental coverage are more likely to postpone medically necessary services in order to avoid Medicare cost-sharing requirements. Furthermore, some studies found that when health plans increase cost-sharing, it particularly affects those who are sicker and poorer, as these are the individuals who are most likely to postpone or avoid seeking care. This delay of care could lead to more expensive health problems in the longer term, particularly for those with chronic conditions.
If the concern is overutilization and unnecessary use of health care services, there are less burdensome and more direct ways to address the problem. Many beneficiaries are not in a position to determine whether a service is necessary or not, and they should not be placed in a position of having to decide based on their ability to pay.

Finally, there is an equity issue inherent in proposals that target Medigap without reforming other forms of supplemental coverage. Beneficiaries who purchase Medigap coverage are less likely to have access to other forms of supplemental coverage, such as employer-sponsored insurance or Medicaid. Most Medigap reform proposals do not include similar premium and cost-sharing restrictions on these other types of supplemental coverage. This would place Medigap enrollees at an unfair financial disadvantage when it comes to affording supplemental insurance or covering Medicare out-of-pocket costs.

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Avalere Health, LLC is a leading advisory company focused on health care business strategy and public policy.