Study Snapshot:

Hospital Pricing Under Medicare Advantage and Traditional Medicare

September 2015

key findings

- MA plans nominally pay only 100 to 105 percent of traditional Medicare rates and, in real economic terms, possibly less.
- Statutory and regulatory provisions limit out-of-network payments to traditional Medicare rates.
- MA plans face de facto budget constraints because of the need to compete with traditional Medicare and other plans.
- Market equilibrium permits relatively lower MA rates as long as commercial rates remain well above traditional Medicare rates.

The Question

How do Medicare Advantage plans and traditional Medicare compare on prices?

The policy community generally has assumed that Medicare Advantage (MA) plans negotiate hospital payment rates similar to those for commercial insurance products and well above those in traditional Medicare. However, recent research has suggested that MA plans in fact pay at or near traditional Medicare rates for both inpatient and outpatient hospital services. In a study funded by the Robert Wood Johnson Foundation,[1] Robert Berenson, M.D., Jonathan Sunshine, Ph.D., Emily Lawton, Urban Institute; and David Helms, Johns Hopkins Bloomberg School of Public Health, interviewed senior hospital and health plan executives to understand the negotiating dynamics between MA plans and hospitals, first to confirm that MA plans do pay hospitals at or near traditional Medicare payment rates and then to explain why. The researchers also sought to understand other aspects of contract negotiations between MA plans and hospitals that might guide possible restructuring efforts to reduce Medicare program spending. The full results of the study are available in *Health Affairs*.

The Implications

Medicare Advantage plans pay at or slightly more than 100 percent of the traditional Medicare payment for hospital services.

The study confirms earlier reports that MA plans and hospitals peg their MA payment rates not to commercial insurance rates but instead to rates used by traditional Medicare. There are three predominant, complementary explanations for the payment equivalence: statutory provisions that constrain out-of-network payments to traditional Medicare rates; de facto budget constraints faced by MA plans because of the need to compete with traditional Medicare and other MA plans; and a market "equilibrium" that permits relatively lower MA rates as long as commercial rates remain well above traditional Medicare rates. Accordingly, MA plans in fact do not face a significant price disadvantage compared to traditional Medicare for hospital care, which is the largest component of MA plans' payments. The study's findings suggest that letting MA plans benefit from traditional Medicare's administered pricing helps constrain MA plans' costs, thereby making MA a more advantageous option for Medicare beneficiaries. Consistent with these findings, the Congressional Budget Office recently concluded that maintaining the traditional Medicare program as a competing plan in the establishment of a premium support system for Medicare would boost federal savings partly because its rates to providers would hold down the rates paid by competing private insurers. Berenson, Sunshine, and colleagues conclude by suggesting that an upper limit on out-of-network billing might discipline commercial insurance market negotiations by providing a regulatory alternative to setting commercial rates themselves—an approach that is likely to be less intrusive and less resource-intensive.

Contact Us

For more information on the results from this grant, please contact the principal investigators Dr. Robert Berenson (rberenson@urban.org) or Dr. Jonathan Sunshine (jsunshine@urban.org) or call 202-223-5886.

[1] The Robert Wood Johnson Foundation's Changes in Health Care Financing and Organization (HCFO) initiative supports timely and policy-relevant health services research on health care policy, financing, and organizational issues.

If you would like to learn more about other HCFO-funded work, please contact: Bonnie J. Austin, HCFO Deputy Director | bonnie.austin@academyhealth.org

Robert Wood Johnson Foundation

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