



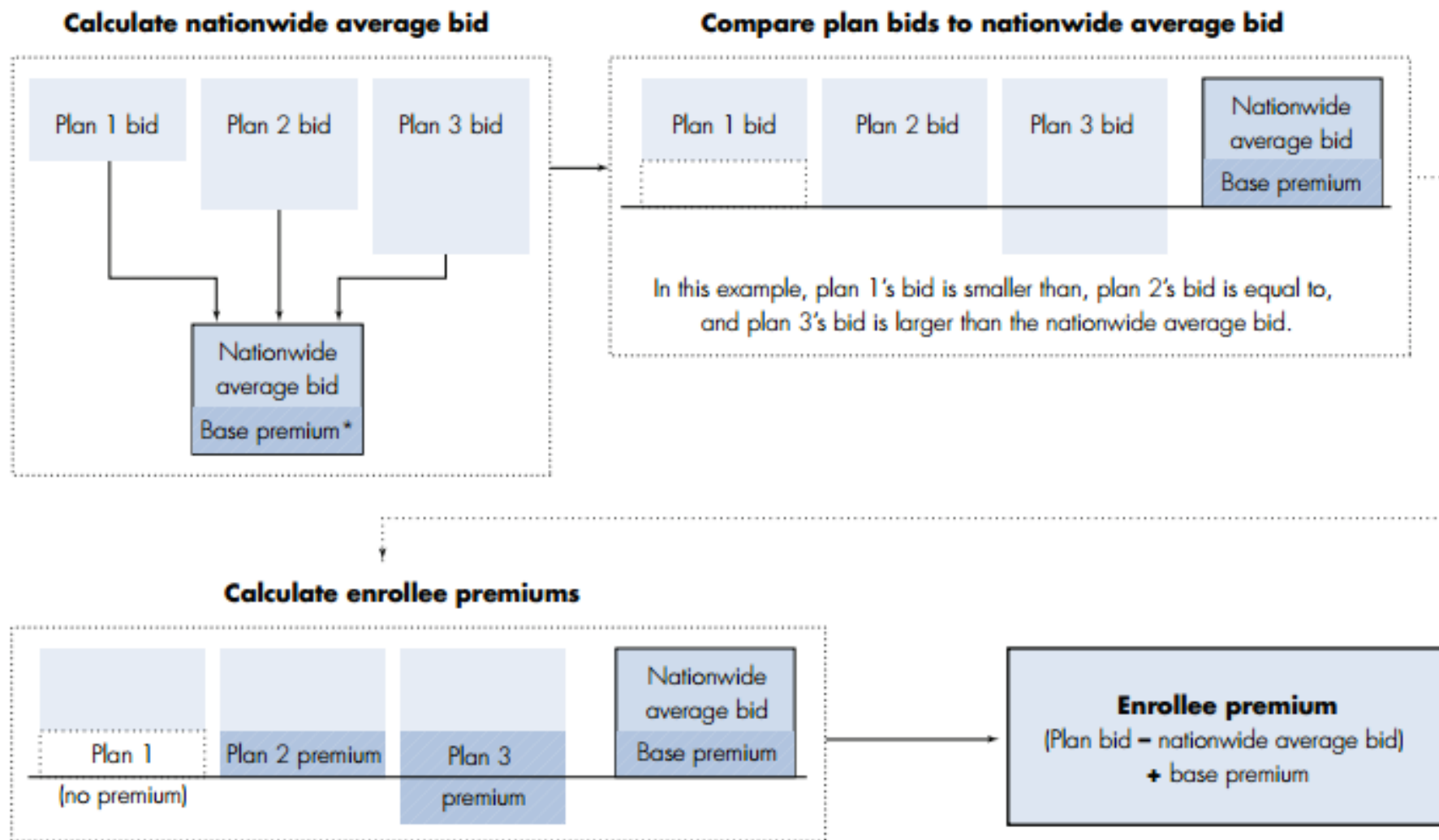
Congressional Budget Office

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Competition and Bids in Medicare's Prescription Drug Program

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Design of the Part D Program for Standard Beneficiaries



*Base premium is a share of the nationwide average bid. It equals the nationwide average times a factor with a numerator of 25.5% and a denominator of 100% minus CMS's estimate of aggregate plan revenues for Part D benefits that they receive through federal individual reinsurance subsidies.

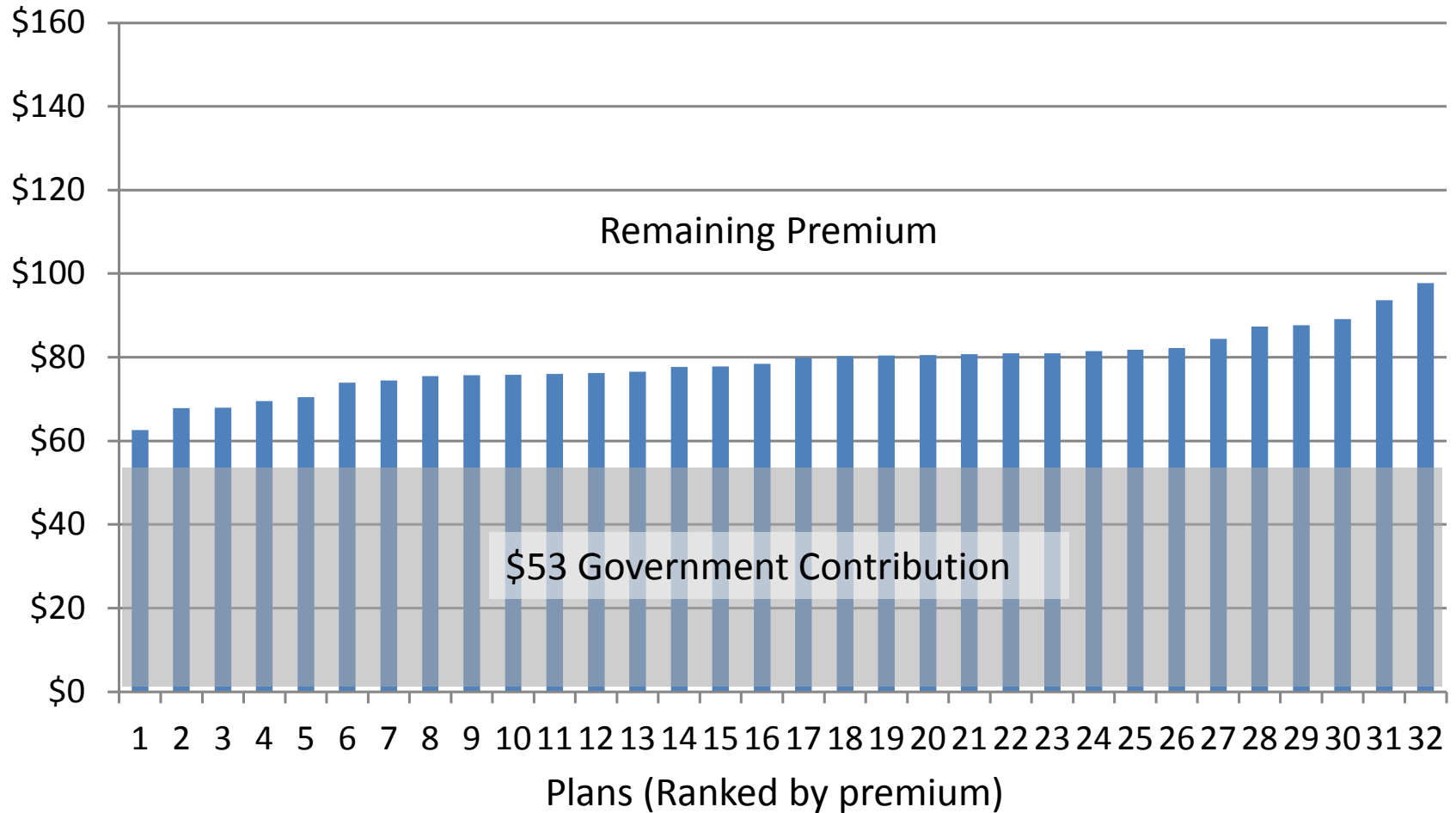
Source: MedPAC, "Part D Payment System" (October 2011)

Incentives That Underlie Bids by Plan Sponsors

- Beneficiaries tend to select plans with lower premiums from among those offered
 - Beneficiaries have been found to place significant weight on the premium in selecting a plan (Abaluck and Gruber, 2011)
 - Within the FFS population, about 60 percent of beneficiaries chose a plan within \$6 per month of the lowest premium plan (avg premium was \$27, ranging from \$10 to \$72 in 2008)
- Beneficiaries tend to change plans if the premium of their plan increases relative to the premiums of other available plans
 - Between 20 percent and 25 percent of Medicare FFS beneficiaries select a new plan each year
 - About half of those beneficiaries are new to the program and the other half are switching from within the program (new plan sponsor or same plan sponsor but new plan)

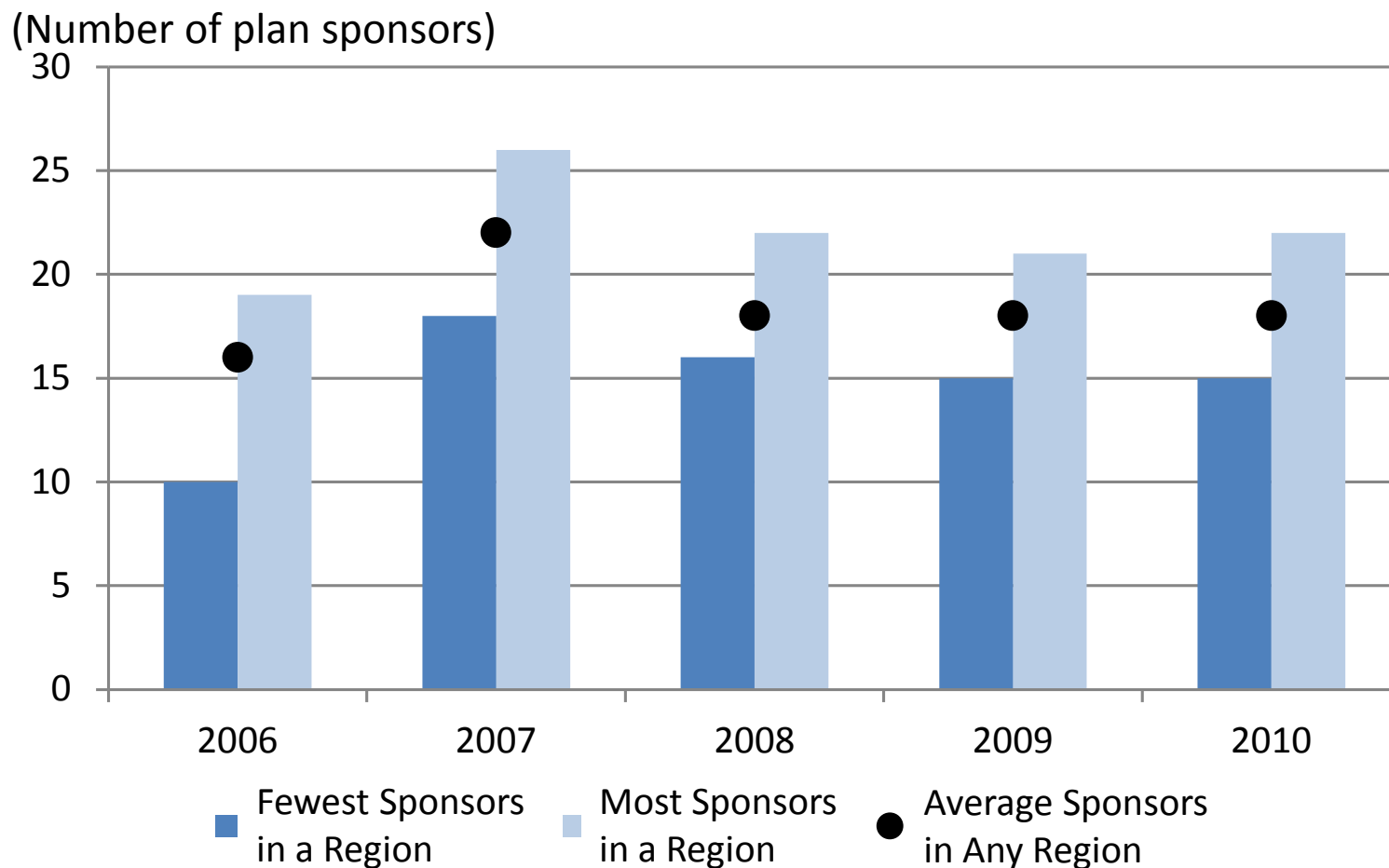
Part D is Designed to Encourage Plans to Compete on the Premium

New York (Region 3, 2007 basic bids)



Part D Market Concentration and Average Premium

Summary Statistics



National
Average
Monthly Bid

\$92.30

\$80.43

\$80.52

\$84.33

\$88.33

Sources: CBO and CMS annual Release of Part D National Average Monthly Bid Amounts



Identifying the Relationship Between Competition and Bids

■ Background

- Most plan sponsors are present in only a single region
 - In 2007: 19 plan sponsors in at least 30 regions; 9 plan sponsors in 2 to 29 regions; 34 plan sponsors in 1 region
 - In 2010: 15 plan sponsors in at least 30 regions; 6 plan sponsors in 2 to 29 regions; 29 plan sponsors in 1 region

■ Strategy

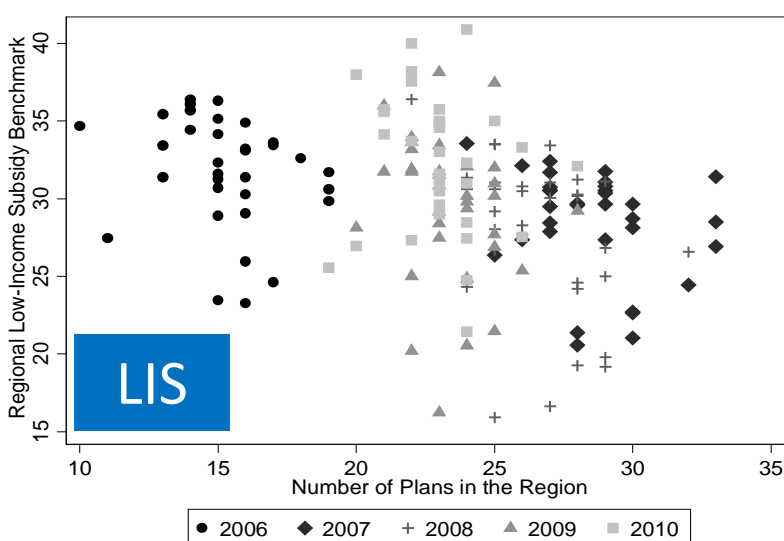
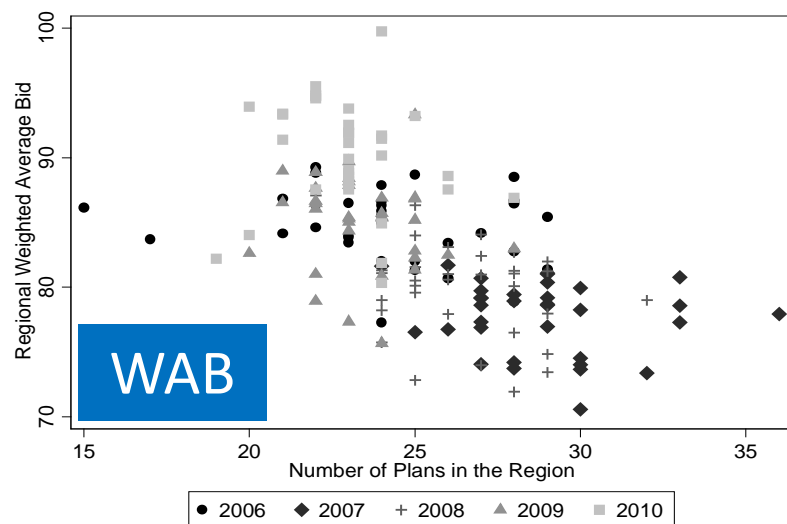
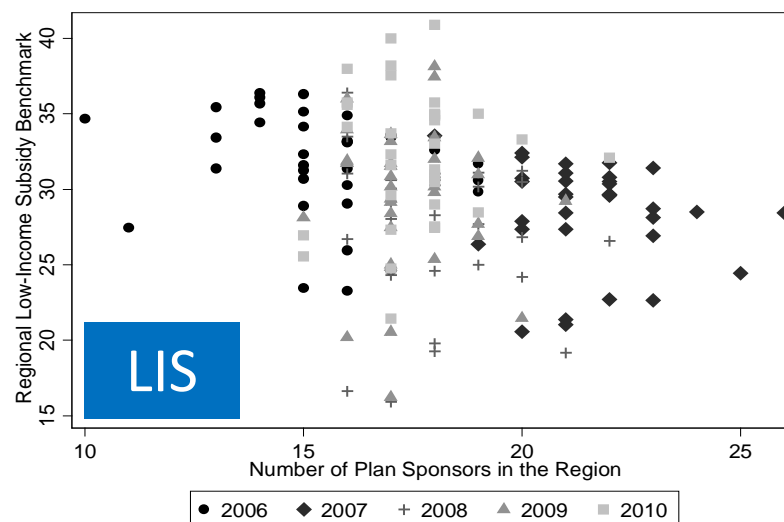
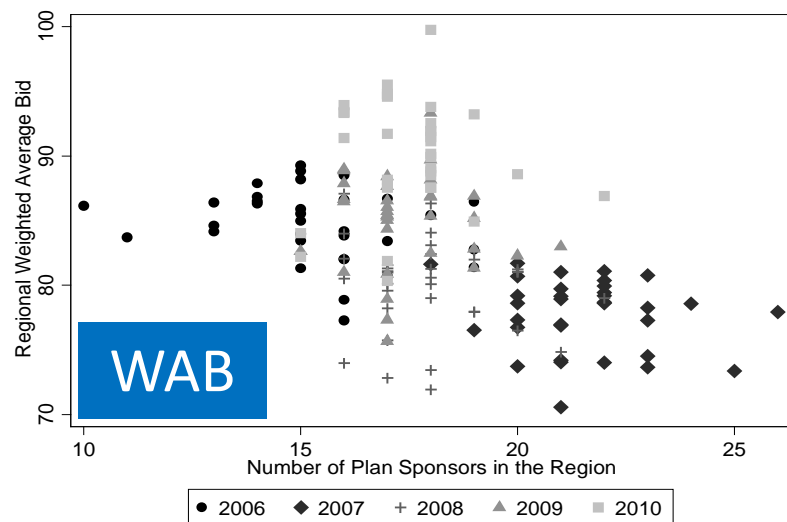
- Compare the bids of multi-region sponsors across regions within year
- Compare bids within region across years
- Control for region, year, sponsor, and various interactions
 - This approach places little weight on bids of plan sponsors only present in a single region (and no weight if the plan sponsor only offers one basic plan in that region)

The Number of Competing Sponsors Varied Across Region and Year

- Between 2006 and 2010, some plan sponsors entered the market for the first time or expanded into new regions
 - National plans: 3 new plan sponsors; 2 closed the year after launch; That initially represented 102 new competitors (34 regions x 3 plan sponsors)
 - Regional plans: 14 plan sponsors launched a PDP in the year or two after launching an MAPD; That represents 19 new competitors (14 plan sponsors x 1.3 regions per sponsor on average)
- Between 2006 and 2010, some plan sponsors exited the market
 - 8 plan sponsors were acquired by another plan sponsor; there was a loss of 105 competitors
 - 11 plan sponsors with low enrollment exited without sale; there was a loss of 77 competitors

Lower Bids Submitted in Regions With More Competition

Preliminary results



Lower Bids Submitted in Regions With More Competition (cont.)

Preliminary results

Dependent Variable	(1) bid	(2) bid	(3) bid	(4) bid
No. Plan Sponsors	-0.49** [0.20]	-0.25 [0.26]	-0.54** [0.22]	-0.40*** [0.13]
No. Plans		-0.25 [0.16]		
Region Controls	X	X	X	
Year Controls	X	X	X	X
Sponsor Controls	X	X		
Observations	4,276	4,276	4,276	4,276
R2	0.51	0.51	0.32	0.28
Adjusted R2	0.49	0.49	0.31	
F-statistic	57.3	56.1	137.1	133.4

Note: Robust standard errors in brackets * p<0.10; ** p<0.05; *** p<0.01; variables used describe conditions in previous year (i.e., the year relevant to when the firm was submitting its bids)

Lower Bids Submitted in Regions With More Competition (cont.)

Preliminary results

- Between 2007 and 2010, more plan sponsors are correlated with a lower low-income benchmark
- Between 2007 and 2010, each additional plan sponsor in a region is correlated with a reduction in the average bid for that region of about half a percent
 - The effect is slightly larger when there are fewer plan sponsors and smaller when there are more plan sponsors

Some Factors Reduce the Role of Competition

■ Determination of benchmarks

- National benchmarks are set to maintain incentive for plan sponsors to submit low bids
- Low-income subsidy benchmarks are established based on regional enrollment; Some large plan sponsors could unilaterally influence the benchmark if they increased their bid

■ Catastrophic coverage

- Reimbursement based on 80 percent of actual costs and not estimated costs reduces incentives to maintain low costs

Some Factors Reduce the Role of Competition

■ The low-income subsidy program

- The assignment of some low-income beneficiaries to plans reduces the incentive for plan sponsors to bid low because the number of new beneficiaries assigned is not dependent on how low the plan sponsor bids (as long as it maintains a premium below the benchmark)
- Plan sponsors wanting low-income beneficiaries have little incentive to reduce their bid below their estimate of the benchmark
- Other plan sponsors avoid auto-assignment by bidding such that their premium is above the benchmark

Summary

- Beneficiaries place weight on the premium and tend to migrate toward low-premium plans
- The design of the program generally motivates plan sponsors to submit low bids
- The market has experienced a net exit of plan sponsors since 2007, which has generally allowed bids to increase slightly
- Some rules of the program reduce the incentive for plan sponsors to submit low bids