Advising the Congress on Medicare issues

Realigning incentives in Medicare Part D

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MEDPAC

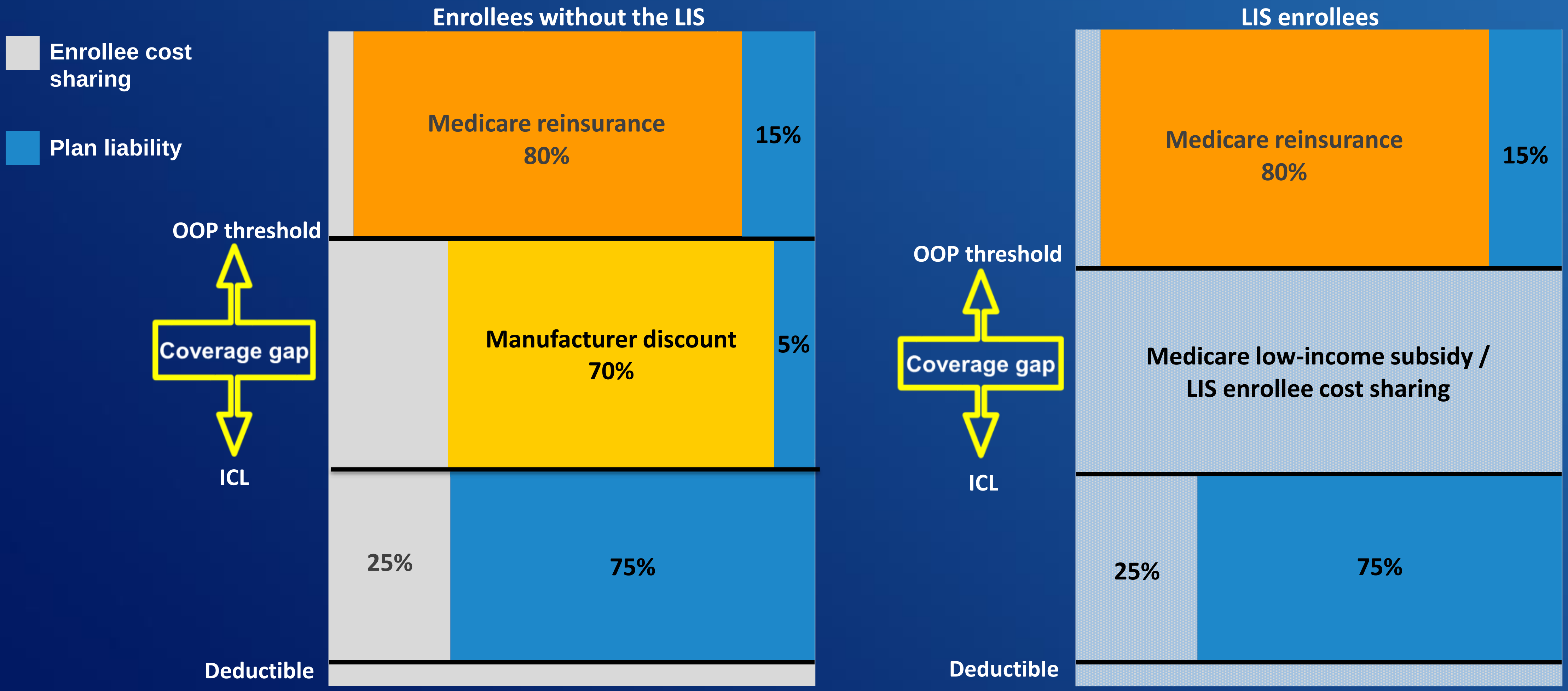
The Commission’s approach to Part D reform

- The Congress designed Part D to use a market-based approach
  - Wide choice among competing private plans
  - Plan sponsors have financial incentives and “commercial-like” tools to manage benefit spending
- Law restricts federal government from “interfering” in negotiations among plans, pharmacies, manufacturers
- Commission’s work to date has kept with this approach

Why Part D needs to be restructured

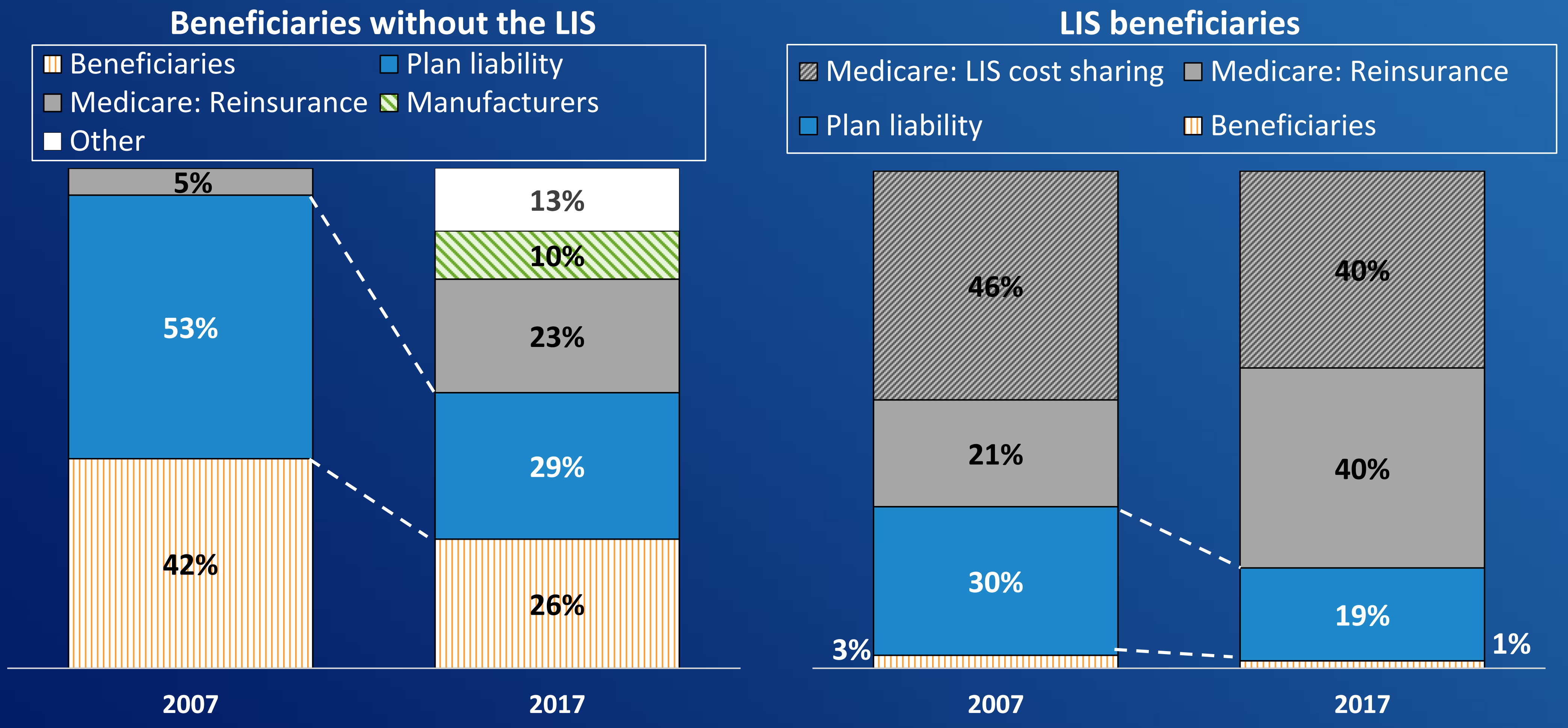
- Rapid growth in Medicare's cost-based payments
  - Medicare's reinsurance pays for 80% of catastrophic spending
  - Low-income subsidy (LIS) pays for nearly all cost sharing of LIS enrollees
- Part D's benefit design dampens incentives to manage spending
  - Coverage-gap discount distorts relative prices of brands to generics
  - Low plan liability in coverage gap and catastrophic phase
  - Manufacturer rebates can be larger than plan liability
- Program design may influence manufacturers' pricing and, in turn, affect:
  - Beneficiary coinsurance
  - Medicare program spending

Misaligned incentives in Part D



Notes: LIS (low-income subsidy), OOP (out-of-pocket), ICL (initial coverage limit). The coverage gap for non-LIS beneficiaries is depicted as it would apply to brand-name drugs and biologics.

Plans are currently responsible for a much smaller share of Part D costs than in 2007



Notes: LIS (low-income subsidy). Data are preliminary and subject to change. Percentage estimates reflect amounts in Part D prescription drug event data minus average rebates as reported by Medicare Trustees. Figures assume that the percentage reductions in total spending attributable to rebates do not systematically differ between enrollees with and without the LIS. “Other” includes spending paid by supplemental coverage other than from enhanced Part D plans.

Potential package of reforms

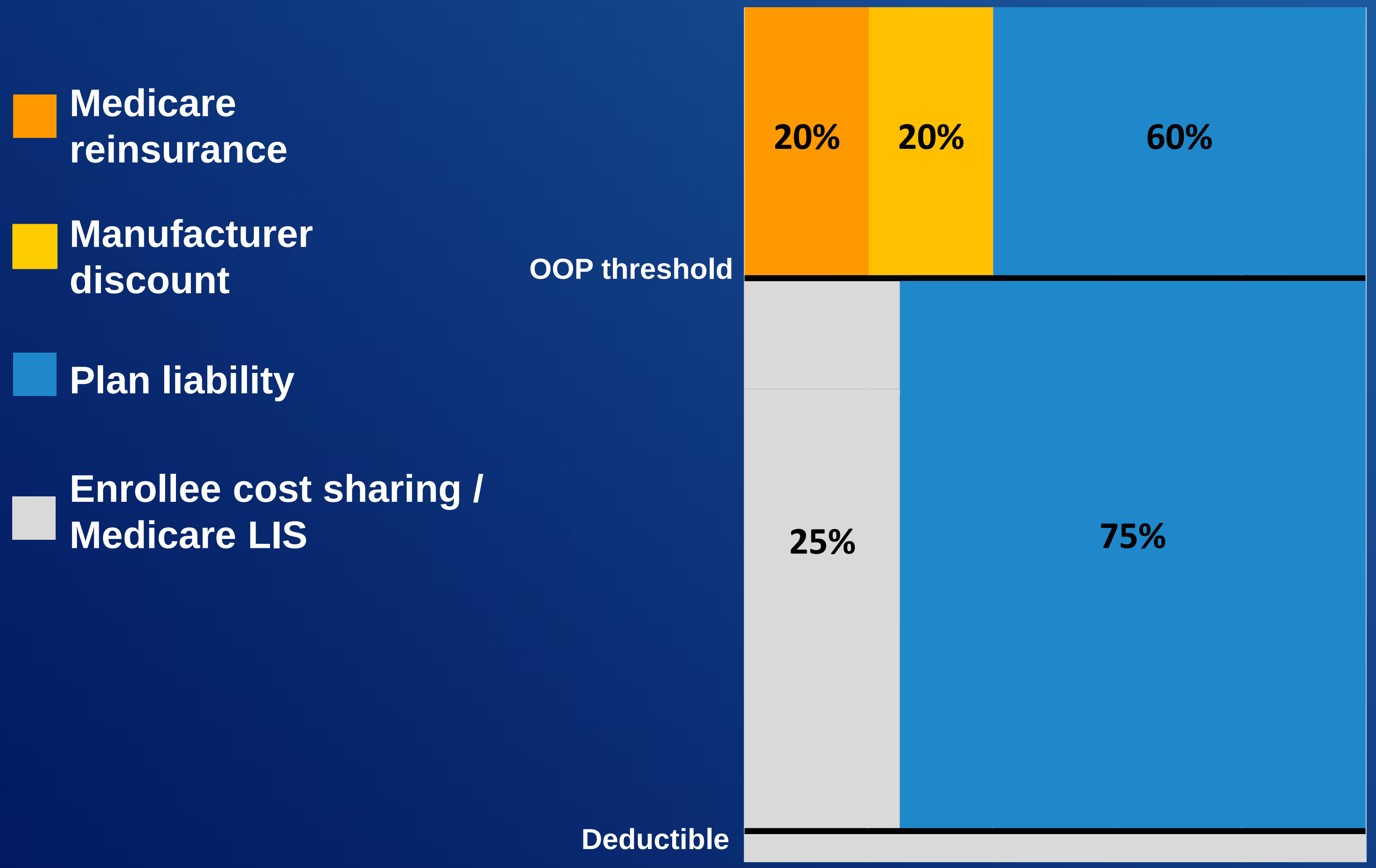
- Major components
  - Plans become responsible for 75% of spending between the deductible and OOP threshold
  - Restructure the catastrophic benefit to eliminate enrollee cost sharing and shift insurance risk from Medicare to plan sponsors and pharmaceutical manufacturers
- Restore risk-based capitated approach
- Eliminate program features that distort market incentives

Key elements of the restructured Part D benefit

	Current benefit	Restructured benefit
Phase-in period	n/a	4 years
Below OOP threshold		
Enrollee cost sharing between deductible and ICL	25%	25%
Plan liability between deductible and ICL	75%	75%
Coverage gap?	Yes	No
Brand manufacturer discount	70% in coverage gap	None
Projected OOP threshold in 2022	$3,100 ($7,100)*	$3,100
Total spending at OOP threshold	About $11,000	About $11,000
Above OOP threshold (catastrophic phase)		
Enrollee cost sharing	5%	0%
Medicare reinsurance	80%	20%
Plan liability	15%	80% for lower-price generics 60% for brands and high-priced generics
Manufacturer discount**	0%	20% for brands and high-priced generics

Notes: n/a (not applicable), LIS (low-income subsidy), OOP (out-of-pocket), ICL (initial coverage limit). *In 2022, a non-LIS beneficiary would pay about $3,100 of the $7,100 threshold and brand manufacturers would discount the remaining $4,000 in the coverage gap. **Applies to brand-name drugs, biologics, biosimilars, and certain high-priced generics.

How Part D would be restructured



Notes: OOP (out-of-pocket), LIS (low-income subsidy). The catastrophic phase (above the OOP threshold) is depicted as it would apply to brand-name drugs, biologics, biosimilars, and high-cost generics. For lower-priced generics, there would be no manufacturer discount and plans would have 80% liability in the catastrophic phase.

Related policy changes would help ensure a successful transition to a restructured benefit

- Phase in higher plan liability in catastrophic phase
- Recalibrate Part D's risk-adjustment model to ensure adequate payments and discourage plans from engaging in risk selection
- Temporarily make risk corridors more generous during the transition period
  - Reduce losses that plans bear fully before risk sharing starts
  - After risk sharing starts, increase share of losses covered by government

New tools would make it easier for Part D plans to manage drug spending

- Differentiate LIS cost sharing for preferred and nonpreferred drugs
- Allow plans to use a nonpreferred tier for specialty drugs
- Give plans greater flexibility in the protected drug classes
  - The Commission recommended removing antidepressants and immunosuppressants from protected classes (2016)
  - The Commission supported a CMS proposal to provide plans with additional tools to manage protected-class drug spending (2019)

Considerations for plans serving low-income beneficiaries and employer-sponsored plans

- Plans with heavy LIS enrollment will see larger increases in plan liability
  - Updates to Part D's risk-adjustment model should ensure that payment rates are adequate
  - Temporary changes to risk corridors should help smaller plans
- Employer group waiver plans (EGWPs) will receive fewer discounts due to the generosity of their coverage
  - EGWP sponsors should have sufficient lead time to make any needed changes to their benefit packages

Summary of Chairman’s draft recommendations

- Major components
  - Plans become responsible for 75% of spending between the deductible and OOP threshold
  - Provide complete financial protection to non-LIS enrollees
  - Restructure the catastrophic benefit to shift insurance risk from Medicare to plan sponsors and pharmaceutical manufacturers
  - Provide plans with more tools and flexibility to manage spending
- ►Restore risk-based capitated approach
- ►Eliminate program features that distort market incentives