

The Daily Dish

A Lesson in Budget Driving Policy

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Eakinomics: A Lesson in Budget Driving Policy

Imagine you were designing the insurance policy for, say, an Affordable Care Act (ACA) exchange participant. You would charge a premium and in exchange there would be a deductible — an initial cost borne entirely by the beneficiary to control overuse of discretionary procedures. There might also be a region of total spending in which the beneficiary paid coinsurance — a fraction of every dollar — to provide incentives for choosing low-cost providers and efficient use of providers. And there would probably be a catastrophic maximum, an amount above which the insurance company paid all or nearly all of the additional costs.

If you were the insurance company, you might worry about the losses that came with unexpectedly expensive patients. If so, you might want to purchase re-insurance — essentially insurance for insurance companies — to cover a portion of the catastrophic losses.

Finally, if you were the government you might have an interest in keeping premiums down to encourage broad coverage. If so, you could provide subsidies to purchasers of insurance. You might also offer reinsurance to the insurers, which would lower their cost exposure and reduce premiums — and might encourage more insurer participation and, thus, better competition.

Indeed, we saw all of these considerations in the design of the ACA exchange policies.

Which brings us to the Medicare Part D program — insurance against the cost of outpatient prescription drugs for seniors. It featured a subsidized premium and an initial coverage amount that included deductibles and co-pays. And it had a catastrophic limit above which the beneficiary paid only 5 percent of the costs of additional drugs. Finally, the federal government provided reinsurance and picked up 80 percent of the remaining 95 percent,

leaving only 15 percent of the costs for insurers.

But as an accident of its passage, Part D originally featured the "donut hole" — a interim region in which the beneficiary paid the full cost of the drugs (essentially 100 percent coinsurance) until hitting the catastrophic limit. In passing the ACA, the government decided to limit the exposure of beneficiaries in the donut hole by 50 percent — but not by requiring insurers to pick up half the cost. That strategy would have pushed up premiums and, thus, the subsidies needed to keep insurance affordable. (It would, however, have given insurers strong incentives to bargain for cheaper drugs.) Instead, the ACA required drug manufacturers to provide a 50 percent discount for those in the donut hole. It was the equivalent of asking doctors to work for half price for exchange participants who had moderate health expenses — something that is very difficult to envision happening. As it turns out, the government also paid a significant portion of the cost on behalf of low-income individuals, so the ACA provision nicely shifted some of this cost onto the drug manufacturers.

The odd nature of the evolution of the Part D design was highlighted by AAF's Tara O'Neill Hayes discussion of a feature included in the Bipartisan Budget Act of 2018. The exposure of beneficiaries in the Part D donut hole was supposed to decline to 30 percent in 2019 — meaning that 50 percent came from manufacturer discounts, 20 percent from insurers, and 30 percent coinsurance. Under the Act — at least as it was originally introduced in the Senate — this was changed to only 25 percent from the beneficiary and only 5 percent from the insurers, but manufacturers will pay 70 percent.

From a first principles point of view, it seems odd that anyone other than the patient, insurer, and government are involved in the financing arrangements. It seems even odder that the policy design has the insurer on the hook for more (15 percent) of the catastrophic costs than the moderate/donut hole costs (5 percent). But it all make perfect sense when one realizes that forcing pharmaceutical companies to fork over another 20 percent pushes more of the low-income subsidy off the government books (down to 25 percent from 30), shifts 15 percent off insurers (down to 5 percent) which modestly lowers premiums and subsidies, and thus saves the government $10 billion. It is a classic case of budgetary imperatives overriding policy principles.