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MEDICARE ADVANTAGE 2004 PAYMENT INCREASES RESULTING FROM THE MEDICARE MODERNIZATION ACT

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As part of the Medicare Modernization Act (MMA), Medicare Advantage (formerly Medicare+Choice, or “M+C”) health plans will receive payments over and above what they were slated to receive in 2004. The original rate increase, announced by CMS in May 2003, will remain in effect for January-February 2004. The higher payments are intended to help stabilize Medicare Advantage, in which recent drops in enrollment have been prompted largely by two factors: the withdrawal of health plans from the program and higher monthly premiums and cost sharing in plans that have stayed. Payments will continue to be set at the county level.

More specifically, the bill requires plans to use the additional payments to (1) reduce enrollee premiums or cost sharing, (2) enhance benefits, (3) stabilize provider networks and/or (4) put the dollars in a stabilization fund for use later in order to offset potential future premium increases or benefit cuts. And although information on how plans are actually using the funds is not yet available, many plans have indicated that they plan to reduce monthly premiums or cost sharing. Since plans must use stabilization funds by the end of 2005, they may be reluctant to use that option.

The analysis presented here examines the distributional effects of the MMA-mandated increases across Medicare beneficiaries, private plan enrollees, and U.S. counties.

How the MMA Changed 2004 Payment Rates

The MMA changed the methodology used to calculate county payment rates in 2004 and 2005 as a prelude to full implementation of the bill in 2006. Before the bill was passed, plans received the greatest of three county payment rate increases:

- *A floor payment* (there was an urban floor of \$591.78 and a rural floor of \$535.42)
- *A minimum update of two percent over the previous year's rate*

- *A blended rate*, which depended on the growth in fee-for-service expenditures both locally and nationally. The blended rate increase, however, had to be budget neutral, and plans were only eligible for blended rate increases in 2000.

Under the MMA, plans are eligible for the highest of *four* payment rates, calculated as follows:

- *A floor payment* (the urban floor has been increased to \$613.89, and the rural floor, to \$555.42)
- *100 percent of average fee-for-service costs* in the county¹
- *A minimum update over the 2003 payment rate* equal to the greater of 2 percent or the national growth rate percentage (6.3 percent for 2004)
- *A blended payment rate update* that depends on the growth in fee-for-service expenditures locally and nationally. For 2004, the availability of the blended payment rate is not subject to budget-neutrality provisions.

In 2005, plans will be paid the same rate as 2004 updated by either two percent or the national growth rate, whichever is higher.

MMA Impact on 2004 Rates

Overall, the MMA raised the average payment, weighted by M+C enrollment in September 2003, from \$620.32 in 2003 to \$640.25 for January–February 2004 and to \$687.82 for March–December 2004 (Table 1). Information is based on the demographic payment rates, which account for 70 percent of total plan payment rates in 2004.²

*The total difference is a 10.9 percent increase over 2003 levels and a 7.4 percent increase over the increase originally slated for 2004.*³ Plans in counties receiving the new 100 percent of

¹ The 100 percent of average fee-for-service costs excludes Medicare payments to providers for direct medical education (DME), but includes spending for indirect medical education (IME). The estimate was also to include spending for Medicare beneficiaries in Department of Defense and Veteran’s Administration programs. However, CMS could not obtain data to implement this adjustment, so DoD and VA spending adjustments are not included in the 2004 estimates of fee-for-service spending.

² Risk-adjusted payment rates which account for 30 percent of plan payment, are heavily variable by plan based on each plan’s risk profile. Since the risk profiles of plans are not available, it is difficult to make any estimates of risk-adjusted payments. However, a limited discussion of risk payments is included later.

³ The 10.9 percent figure differs from the 10.6 percent reported by the Centers for Medicare & Medicaid Services (CMS) because the agency’s number is an average across counties in which a private plan operates, whereas the 10.9 percent weights by county enrollment in MA.

Table 1
Medicare Advantage Payment Rate Increase Information
 (Information presented for demographic payment rates only)

Rate Category	Average 2004		Payment Increase -- 2003 to Jan- Feb 2004		Payment Increase -- Jan- Feb 2004 to Mar-Dec 2004		Total Payment Increase -- 2003 to Mar-Dec 2004		Total Dollar Increase -- 2003 to Mar-Dec 2004	
	Payment (Jan-Feb)	Payment (Mar-Dec)	Feb 2004	Mar-Dec 2004	Mar-Dec 2004	Mar-Dec 2004	Feb 2004	Mar-Dec 2004	Mar-Dec 2004	2004
Overall	\$620.32	\$640.25	3.2%	7.4%	10.9%	\$19.93	\$47.57	\$67.50		
Blended Payment Increase	\$608.10	\$623.67	2.6%	7.0%	9.8%	\$15.57	\$43.81	\$59.38		
Rural Floor	\$499.80	\$524.74	5.0%	3.6%	8.8%	\$24.94	\$19.13	\$44.07		
Urban Floor	\$563.84	\$591.80	5.0%	3.7%	8.9%	\$27.96	\$22.09	\$50.05		
Minimum Update	\$717.47	\$733.25	2.2%	4.0%	6.3%	\$15.78	\$18.67	\$45.22		
100% Fee-For-Service	\$618.60	\$635.91	2.8%	12.1%	15.3%	\$17.31	\$77.11	\$94.42		

SOURCE: Mathematica analysis of CMS Medicare Advantage 2004 Rate Files.

NOTES: Information excludes counties in Guam and the Virgin Islands, but includes Puerto Rico. All data were weighted by the number of M+C enrollees in a county in September 2003. Data presented includes only demographic payment rates, which account for

fee-for-service rate will get the largest payment increase, both as a percentage of 2003 payments (15 percent) and as a total dollar amount (\$94 per month). The increase also represents an average additional 12.1 percent more than the January-February 2004 rates. Forty-one percent of Medicare enrollees were residents of such counties in September 2003.

In all counties, Medicare Advantage rates as of March 2004 will average 107 percent of average fee-for-service costs (Table 2).

About 7 percent of the people enrolled in M+C in September 2003 live in counties that will receive blended payment rates beginning March 2004. The average rate in these counties will therefore be 111 percent of the county's average fee-for-service Medicare expenditures. Roughly 4 percent of people enrolled in M+C in September 2003 live in counties receiving a rural floor payment, and 26 percent live in counties receiving an urban floor payment. These "floor counties" have the highest payment rates relative to fee-for-service costs, at 121 percent (rural floor) and 117 percent (urban floor) of fee-for-service costs. Twenty-two percent of M+C enrollees live counties that will receive a minimum update in payments, which according to the MMA, is the national growth rate percentage, or 6.3 percent in 2004. Payment rates in these counties average 105 percent of fee-for-service costs. The remaining 41 percent of enrollees live in counties that will earn the newly established 100 percent of fee-for-service payment rate. These counties will average 102 percent of fee-for-service costs because indirect medical expenditures (IME) are counted in the Medicare Advantage 100 percent of fee-for-service payment rate even though IME are made directly to providers.

Geographic Variation in Rate Increases

The minimum increase in payment rates received by any county was 3.6 percent over the January-February 2004 rate and 6.3 percent over 2003 payment rate.

Tables 3 and 4 show the distribution of Medicare beneficiaries, M+C enrollees, and counties by percentage increase in monthly payment rates from both the January-February 2004 and the 2003 rates.

Table 5 presents the revised payment rates for 2004 in relation to county fee-for-service costs. Most private plan enrollees (55 percent) live in counties where the new Medicare Advantage rates range from 100 percent to 105 percent of the average county fee-for-service cost. However, certain counties in which enrollment is somewhat significant will be paid considerably more than fee-for-service costs under the new payment system. Some of these counties are:

- In Fresno County, California, plans will be paid 124 percent of fee-for-service costs. About 20,000 Medicare beneficiaries were enrolled in M+C in Fresno in September 2003.
- In Marion County, Oregon, plans will be paid 128 percent of fee-for-service costs. About 18,500 Medicare beneficiaries were enrolled in M+C in Marion County in September 2003.

Table 2
Medicare Beneficiaries, Medicare Advantage Enrollees and U.S. Counties by Type of MA Payment Rate, March-December 2004

Rate Category	Number of Medicare Beneficiaries		Percent of Medicare Beneficiaries		Number of M+C Enrollees		Percent of M+C Enrollees		Number of Counties		Percent of Counties		Average Rate Compared to FFS*
Overall	42,100,179		100.0%		5,304,232		100.0%		3,223		100.0%		107.3%
Blended Payment Increase	1,713,984		4.1%		389,248		7.3%		93		2.9%		111.3%
Rural Floor	7,894,730		18.8%		216,815		4.1%		1,614		50.1%		121.0%
Urban Floor	11,607,311		27.6%		1,379,730		26.0%		538		16.7%		116.6%
Minimum Update	5,199,731		12.4%		1,158,118		21.8%		141		4.4%		105.4%
100% Fee-For-Service	15,684,423		37.3%		2,160,321		40.7%		837		26.0%		102.3%

SOURCE: Mathematica analysis of CMS Medicare Advantage 2004 Rate Files.

NOTES: Information excludes counties in Guam and the Virgin Islands, but includes Puerto Rico. Data may be different than that presented by CMS because of differences in counties included in the analysis. Data presented on comparison to fee-for-service rates includes only demographic payment rates, which account for 70 percent of plan payments in 2004. Fee-For-Service rates were adjusted to account for double counting of Indirect Medical Expenditures (IME) in Medicare Advantage payment rates.

*Data weighted by M+C enrollees in September 2003.

**Distribution of Medicare Beneficiaries, M+C/Medicare Advantage Enrollees, and Counties,
by Percent of Payment Increase**

Table 3
Payment Increase From Jan-Feb 2004 Rates to Mar-Dec 2004 Rates

	Number of Beneficiaries	Percent of Beneficiaries	Number of Enrollees	Percent of Enrollees	Number of Counties	Percent of Counties
Total	42,100,179	100.0%	5,304,232	100.0%	3,223	100.0%
3.60%	18,744,200	44.5%	1,584,122	29.9%	2,016	62.6%
3.7% -- 6.7%	9,168,224	21.8%	1,723,062	32.5%	406	12.6%
6.8% -- 10.0%	4,136,887	9.8%	651,602	12.3%	174	5.4%
10.1% -- 15.0%	5,057,559	12.0%	725,475	13.7%	344	10.7%
15.1% -- 25%	4,238,712	10.1%	570,364	10.8%	208	6.5%
25.1% +	754,597	1.8%	49,607	0.9%	75	2.3%

SOURCE: Mathematica analysis of CMS Medicare Advantage 2004 Rate Files.

NOTES: Information excludes counties in Guam and the Virgin Islands, but includes Puerto Rico. Data presented includes only demographic payment rates, which account for 70 percent of plan payments in 2004.

Table 4
Payment Increase from 2003 Rates to Mar-Dec 2004 Rates

	Number of Beneficiaries	Percent of Beneficiaries	Number of Enrollees	Percent of Enrollees	Number of Counties	Percent of Counties
Total	42,100,179	100.0%	5,304,232	100.0%	3,223	100.0%
6.30%	5,199,731	12.4%	1,158,118	21.8%	141	4.4%
6.4% -- 8.8%	20,105,802	47.8%	1,859,594	35.1%	2,096	65.0%
8.9% -- 15.0%	8,548,792	20.3%	1,337,775	25.2%	399	12.4%
15.1% -- 25.0%	6,760,340	16.1%	851,756	16.1%	452	14.0%
25.1% -- 40.0%	1,293,310	3.1%	78,781	1.5%	120	3.7%
40.1% +	192,204	0.5%	18,208	0.3%	15	0.5%

SOURCE: Mathematica analysis of CMS Medicare Advantage 2004 Rate Files.

NOTES: Information excludes counties in Guam and the Virgin Islands, but includes Puerto Rico. Data presented includes only demographic payment rates, which account for 70 percent of plan payments in 2004.

Table 5
Mar-Dec 2004 Payment Rates in Relation to Fee-For-Service Costs

	Number of Beneficiaries	Percent of Beneficiaries	Number of Enrollees	Percent of Enrollees	Number of Counties	Percent of Counties
Total	42,100,179	100.0%	5,304,232	100.0%	3,220	100.0%
100.0% -- 105.0%	19,676,207	46.7%	2,903,909	54.7%	1,118	34.7%
105.1% -- 109.9%	7,233,543	17.2%	1,002,194	18.9%	407	12.6%
110.0% -- 119.9%	7,598,813	18.0%	743,857	14.0%	687	21.3%
120.0% -- 129.9%	4,460,289	10.6%	337,674	6.4%	517	16.1%
130.0% -- 139.9%	1,910,511	4.5%	223,734	4.2%	264	8.2%
140.0% -- 149.9%	706,304	1.7%	63,753	1.2%	137	4.3%
150.0% -- 159.9%	220,912	0.5%	12,761	0.2%	52	1.6%
160.0% -- 169.9%	181,804	0.4%	9,974	0.2%	21	0.7%
170.0% -- 179.9%	103,719	0.2%	5,821	0.1%	13	0.4%
180.0% -- 189.9%	6,374	0.0%	555	0.0%	1	0.0%
190.0% -- 199.9%	1,703	0.0%	0	0.0%	3	0.1%

SOURCE: Mathematica analysis of CMS Medicare Advantage 2004 Rate Files.

NOTES: Information excludes counties in Guam and the Virgin Islands, but includes Puerto Rico. Data presented includes only demographic payment rates, which account for 70 percent of plan payments in 2004. Fee-For-Service average expenditures were adjusted to account for double counting of Indirect Medical Expenditures (IME) in Medicare Advantage payment rates.

- In Clark County, Washington, plans will be paid 132 percent of fee-for-service costs. About 16,700 Medicare beneficiaries were enrolled in M+C in Clark County in September 2003.
- In San Francisco County, California, plans will be paid 132 percent of fee-for-service costs. About 35,500 Medicare beneficiaries were enrolled in M+C in San Francisco County in September 2003.
- In Honolulu County, plans will be paid 144 percent of fee-for-service costs. About 43,100 Medicare beneficiaries were enrolled in M+C in Honolulu County in September 2003.
- In Puerto Rico, the M+C plan will be paid 160 percent to 180 percent of fee-for-service costs in many areas in Puerto Rico. About 29,400 Medicare beneficiaries were enrolled in M+C in Puerto Rico in September 2003.

Table 6 shows the actual dollar differences between the March–December 2004 rates and the January–February 2004 rates. The minimum increase in any county payment rate was \$11.35 per member per month. About one-third of enrollees live in counties where the payment rate will increase by \$11.35 to \$25.00 per month, and another third live in counties where the increase will range from \$25.01 to \$50.00 per member per month. Some counties that have significant private plan enrollment will get much larger payment increases in terms of actual

Table 6
Dollar Increase in Payment Rates from Jan-Feb 2004 to Mar-Dec 2004

	Number of Eligibles	Percent of Eligibles	Number of Enrollees	Percent of Enrollees	Number of Counties	Percent of Counties
\$11.35 -- \$25.00	20,384,260	48.4%	1,861,278	35.1%	2,149	66.7%
\$25.01 -- \$50.00	9,721,460	23.1%	1,809,558	34.1%	386	12.0%
\$50.01 -- \$75.00	4,208,795	10.0%	515,481	9.7%	215	6.7%
\$75.01 -- \$100.00	4,117,860	9.8%	731,319	13.8%	272	8.4%
\$100.01 -- \$125.00	1,549,845	3.7%	160,250	3.0%	86	2.7%
\$125.01 -- \$150.00	1,487,182	3.5%	177,217	3.3%	57	1.8%
\$150.01 -- \$175.00	253,368	0.6%	22,779	0.4%	29	0.9%
\$175.01 +	377,409	0.9%	26,350	0.5%	29	0.9%

SOURCE: Mathematica analysis of CMS Medicare Advantage 2004 Rate Files.

NOTES: Information excludes counties in Guam and the Virgin Islands, but includes Puerto Rico. Data presented includes only demographic payment rates, which account for 70 percent of plan payments in 2004.

dollars as a result of the MMA. Most of these counties, listed below, were eligible for the new 100 percent of fee-for-service payment.

- In Clark County, Nevada, plans will receive an additional \$117 per member per month. About 67,200 Medicare beneficiaries were enrolled in M+C in Clark County in September 2003.
- In Delaware County, Pennsylvania, plans will receive an additional \$138 per member per month. About 29,600 Medicare beneficiaries were enrolled in M+C in Delaware County in September 2003.
- In Palm Beach County, Florida, plans will receive an additional \$146 per member per month. About 66,500 Medicare beneficiaries were enrolled in M+C in Palm Beach County in September 2003.
- In Nassau County, New York, plans will receive an additional \$149 per member per month. About 26,300 Medicare beneficiaries were enrolled in M+C in Nassau County in September 2003.
- In Belmont County, Ohio, plans will receive an additional \$171 per member per month. About 4,700 Medicare beneficiaries were enrolled in M+C in Belmont County in September 2003.
- In Ocean County, New Jersey, plans will receive an additional \$249 per member per month. About 11,800 Medicare beneficiaries were enrolled in M+C in Ocean County in September 2003.

- The largest payment increase is in Saint Bernard County, Louisiana, where health plans will receive an additional \$310 per member per month. About 2,700 Medicare beneficiaries were enrolled in M+C in Saint Bernard County in September 2003.

At least some of these counties receiving large dollar increases have been affected by plan withdrawals in the last five years. Plans in these areas have argued that they could not compete because of payment rates well below Medicare fee-for-service costs. While the dollar amount increases in these counties are large, the new rates reflect payment much closer to fee-for-service costs than in other areas, for instance floor payment counties.

Risk Payments

In addition to the changes in the base demographic rates, CMS used the opportunity of issuing new rates to update the risk rates as well. As part of the new risk adjustment system, 30 percent of plan payments in 2004 will be adjusted according to each health plan's risk profile, compared with just 10 percent in 2003. *In aggregate, the impact of risk adjustment will be to increase the average premium increase by about 0.9 percent because CMS decided to implement the adjuster on a budget neutral basis (i.e. to maintain total aggregate spending in the MA sector as the distribution of payments was modified based on risk. More detail is provided below on the calculations.)*

Data on the risk profiles of individual plans are not available, so it is difficult to present information on risk payments. However, Figure 1 presents the average monthly demographic and risk payments nationwide to M+C/Medicare Advantage plans in 2003, January–February 2004, and March–December 2004. The risk payments are based on the demographic rate, a county re-scaling factor, and a plan's risk profile.

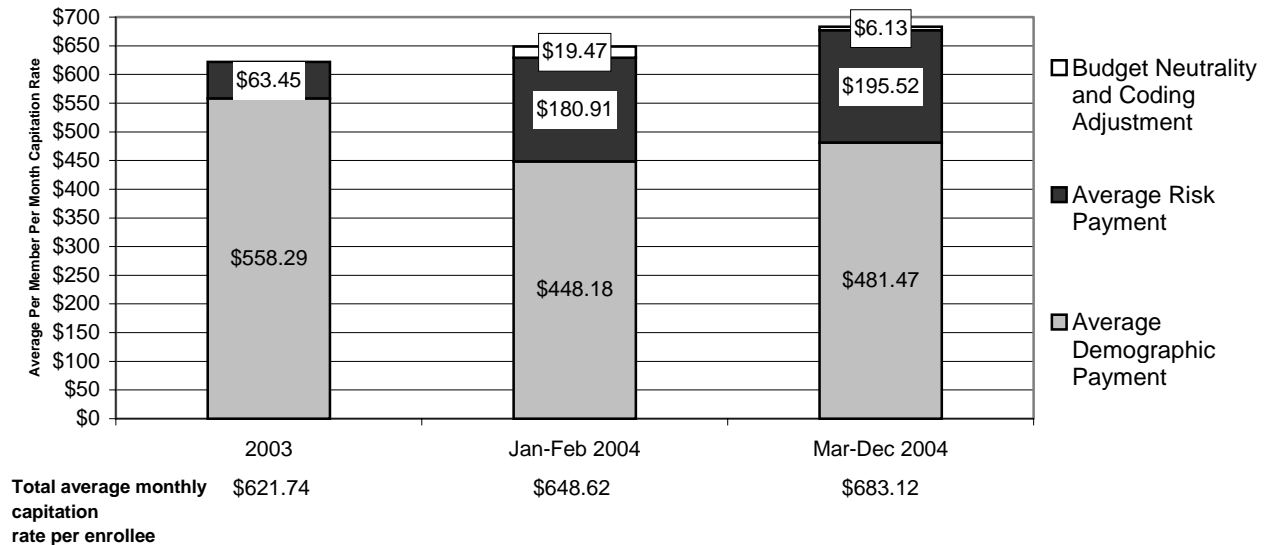
In 2003, payments based on plan demographics accounted for an average \$558.29 in monthly payments to health plans. Risk payments added another \$63.45,⁴ bringing the total to \$621.74. In 2003, payments to health plans were composed of 90 percent of a plan's demographic rate and 10 percent of its risk-adjusted rate. By comparison, total payments to plans in 2004 are 70 percent demographic and 30 percent risk-based, as CMS went forward with its new risk adjustment system. Also in 2004, CMS added an adjustment for risk adjustment budget neutrality.⁵ This adjustment added approximately 10.8 percent to risk payments or 3.6 percent to overall payments in the original January-February 2004 rates.

For the January-February period, the average demographic payment is \$448.18. Under the risk formula, the average plan received \$180.81 in payments that they would have received without the adjustments for risk adjustment budget neutrality. The adjustment added another \$19.47 to the risk-based payment, bringing the average total payment to \$648.56.

⁴ The total payments are based on a risk score of 1.0 for all plans. Actual CMS payments to health plans will differ according to the risk scores of individual plans.

⁵ A full discussion of the risk adjustment budget neutrality adjustment is in the "Data Sources and Methods" section.

Figure 1
Average Demographic and Risk Payments to Medicare+Choice/Medicare Advantage Plans in 2003/2004



SOURCE: MPR analysis of CMS data files.

NOTES: In 2003, risk payments represented 10 percent of a plan's total payment. In 2004, risk payments account for 30 percent of payment. The budget neutrality adjustment was applied to 2004 rates only. The adjustment was updated for the March-December time period to 3.1 percent from 10.8 percent in January-February. Individual plan payments will vary greatly from these amounts to reflect each plan's risk profile. Data is weighted by September 2003 M+C enrollment.

When CMS announced the new demographic rates for 2004, the agency used the opportunity to include more thorough data to modify its adjustment for risk adjustment budget neutrality. For March-December, the risk adjustment budget neutrality factor will be reduced to 3.1 percent of risk payments, or 0.9 percent of total payments.

Under the revised payment methodology, the average March-December 2004 demographic payment will rise to \$481.47. The risk payment will also rise to \$195.52 because of the increase in the demographic base. However, the update to the risk adjustment budget neutrality factor means plans get a smaller bump, just \$6.13 from that payment. The total average payment for March-December 2004 will be \$683.12.

About the Data

Unless otherwise stated, the data presented in this analysis are weighted by M+C enrollment in September 2003. Therefore, the average payment rates represent the average payment paid to a plan on behalf of a M+C enrollee. In addition to the MMA-mandated rate increases, CMS updated a few other factors that help determine health plan payment rates. First, the national growth rate percentage was updated from 3.7 percent to 6.3 percent, which will be reflected in the March-December 2004 rates. This change raises the minimum payment increase and affects plan payments in floor and blend counties. CMS also modified the risk adjustment budget neutrality factor, which accounts for the difference in health status between private health plan enrollees and fee-for-service Medicare beneficiaries to 3.13 percent from 10.76 percent.

Data Sources and Methods

Data on health plan payment rates and average fee-for-service costs are based on CMS's 2003 Medicare+Choice ratebook, the 2004 Medicare+Choice ratebook (for January-February information), and the 2004 Medicare Advantage ratebook (for March-December information). All three are available on the CMS website at www.cms.hhs.gov/healthplans/rates/default.asp. Information on M+C enrollment and eligible Medicare beneficiaries by county is from CMS's September 2003 State/County Market Penetration file, available on the the agency's website at www.cms.hhs.gov/healthplans/statistics/mpsct/.

Estimates of fee-for-service spending in each county were based on the 100 percent of fee-for-service rates for each county specified in the 2004 Medicare Advantage ratebook. However, these rates were adjusted to remove the IME payment included in the 100 percent Medicare Advantage rates by subtracting 65 percent of the carve-out.

Risk payments are determined by a number of factors. For the March-December 2004 period:

Risk payment = .3(Demographic rate x County Rescaling Factor x (1.0829/1.05) x Health Plan's Risk Profile)

The 1.0829/1.05 factor is a new adjustment as of 2004. The 1.0829 adjustment accounts for favorable selection into M+C plans⁶ and the 1/1.05 accounts for the fact that fee-for-service providers in 2003 code differently than they did in 1999. Together, these adjustments add 3.13 percent to risk payments, or 0.94 percent to total payments.⁷

Because information on plans' risk profiles is not available, our estimates of risk payment assume a risk score of 1.0.

⁶ In the January-February 2004 rates, CMS used a 1.163 adjustment for favorable selection. However, that adjustment was based on data from a selection of health plans, while the updated adjustment uses data from all health plans.

⁷ Since risk payments are 30 percent of total payments, the effect of the adjustment is 0.3 x 3.13, which equals 0.94