

*Medicare Prospective Payment and
the Shaping of U.S. Health Care*

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For Ben and Ellen Mayes R. M.

To my mother, Clare Berenson R. A. B.

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The origins of this book, ironically, are rooted in a rejection. Back in 2001 or early 2002, I submitted a manuscript on Medicare's payment policy for hospitals to the *Journal of Health Politics, Policy, and Law*. Like most manuscript submissions, mine had as many weaknesses as strengths and needed substantial revisions. Fortunately, though, the reviewers' stinging (yet accurate) criticisms came with a very helpful and lengthy letter by the journal's editor at the time, Mark Peterson. All scholars should be so lucky to receive constructive suggestions that create a comprehensive road map for improvement. It took a day or two to digest all of the literature references and recommendations for additional research (namely, personal interviews with key policy makers) that he suggested. But the first few interviews I conducted—with Representative Pete Stark, former House Ways and Means Committee chair Dan Rostenkowski, former Ways and Means Committee staff member David Abernethy, former Senate Finance Committee staff member Lisa Potetz, former ProPAC chair Stuart Altman, and former House Ways and Means Committee ranking minority member Bill Gradison—led to more than sixty additional interviews and the discovery of how and why Medicare payment policy has significantly influenced the delivery, organization, and financing of U.S. health care.

Subsequently, the *Journal of Policy History* accepted a new and improved version of my manuscript, after its reviewers strengthened it even more. And the journal article later became the inspiration for this book-length examination of Medicare payment reforms, which Bob Berenson graciously agreed to help me write after we collaborated on an article on cost shifting for *Health Affairs* in 2003, with Jason Lee and Anne Gauthier at AcademyHealth. My first thanks, therefore, go to Mark Peterson and the editors at the *Journal of Policy History* for their time and patience with my scholarship.

An earlier and truncated version of Chapters 1 and 2 appeared in the *Journal of the History of Medicine and Allied Sciences* (2006) under the title "The Origins, Develop-

ment, and Passage of Medicare's Revolutionary Prospective Payment System." An older draft of Chapters 3 and 4 appeared in the *Journal of Policy History* (2004) under the title "Causal Chains and Cost Shifting: How Medicare's Rescue Triggered the Managed Care Revolution." Portions of Chapter 6 appeared in *Health Economics, Policy, and Law* (2006), in an article entitled "Pursuing Cost Containment in a Pluralistic Payer Environment," and portions of Chapter 7 appeared in the *Journal of Health Law* (2005) in an article entitled "Medicare and America's Health Care System in Transition: From the Death of Managed Care to the Medicare Modernization Act of 2003 and Beyond." I am grateful to these journals' editors for allowing me to use these works in this present volume.

This book would not exist were it not for the generosity of numerous policy makers who allowed me to interview them at length. Their names are listed in the appendix. I am indebted to all of them for providing me with an insider's perspective on how Medicare payment reforms were developed, implemented, and adjusted over time, as well as how they interacted with other parts of the U.S. health care system. A number of individuals, in particular, shared hours with me or even allowed me to interview them more than once: Jack Ashby, Sheila Burke, Allen Dobson, Paul Ginsburg, Stuart Guterman, William Hsiao, Linda Magno, James Mongan, Jack Owen, Leon Panetta, Julian Pettengill, Rick Pollack, Robert Reischauer, Tom Scully, Bruce Vladeck, and Gail Wilensky.

I have benefited greatly from the friendship, mentoring, and scholarship of a number of individuals, including Henry Abraham, Ed Berkowitz, Farasat Bokhari, Martha Derthick, John Echeverri-Gent, Ken Elzinga, Dan Fox, Dan Gitterman, Colleen Grogan, Jacob Hacker, Allan Horwitz, Bob Hurley, Carol Mershon, Jim Morone, Jon Oberlander, David O'Brien, Tom Oliver, Larry Sabato, Richard Scheffler, Herman Schwartz, and Deborah Stone. My progress in academia has been due, in part, to their support and encouragement. This book began as a research project at the University of California, Berkeley, School of Public Health, under a National Institute of Health postdoctoral traineeship. Since then, it has been supported by generous faculty research grants and a junior research leave from the University of Richmond.

It has been my good fortune to be a member of the Department of Political Science at the University of Richmond, where I have enjoyed the company of a kind and nurturing group of colleagues: Sheila Carapico, Akiba Covitz, Jennifer Erkulwater, Art Gunlicks, Jimmy Kandeh, Melissa Labonte, John Outland, Dan Palazzolo, Tracy Roof, Andrea Simpson, Pat Thiel, Yamina Truda, Vincent Wang, Ellis West, and John Whelan. I have also enjoyed the intellectual stimulation and friendship of numerous students with a significant interest in health care, many of whom have taken my U.S. Health Care Policy and Politics course: Casey Abare, Cecelia Ackerman (who tran-

scribed several interviews), Jon Alpern, Scott Annett, Ryan Babiuch (who transcribed several interviews), Megan Bailey, Amanda Biddle, Kelly Billig, Becky Brenner, Justin Burk, Ruthie Byrne, Drew Callison, Elise Carlin, Nicole Conner, Tom Cosgrove, Randy De Martino, Abbie Emerson (who transcribed several interviews), Emily Fellin, Paul Gardner, Adam Greenblatt, Deborah Hendryx, Matt Hitchcock, Taylor Hubbard, Jake Kayser, Faith Keck, Allison Kirk, Jackie Knupp, Dave Larkin, Marcie Lipper, Christine Livingston, Bill Longley, Emily Newman, Brian Pagels, Justin Pells, Roger Revell, John Rosato, Andrew Ryan, Kristin Schmidt, Jaime Settle, Lauren Skiles, Matt Summers, Jason Sutton, Meredith Stewart, Jeff Vergales, Chris Wellington, Conrad Williams, Matt Williams, and Kathryn Winslow.

Bob Berenson and I owe enormous debts of gratitude to David Colby, Tim Jost, David Smith, and Tom Weill, and to Joe White, who was the official reviewer for the Johns Hopkins University Press. All of them read either the penultimate or ultimate chapter drafts of our book. Their comments, criticisms, and suggestions for revision took months to address, and they may not agree with all of our final arguments and observations, but their reviews dramatically improved the overall quality of our book. Any errors that remain—particularly after their close critiques—are solely our fault.

I wish to thank the Johns Hopkins University Press for helping us make this book come to fruition. Wendy Harris has been a superb editor. I greatly appreciate and am thankful to her for believing in this project when it was only an idea on a few pages of paper. Special thanks as well to Susan Lantz and Brendan Coyne for working with our final manuscript drafts and for their very helpful recommendations for improvement.

Finally, this book is dedicated to my family. My parents, Ben and Ellen Mayes, are two of the people I admire most in life. I literally cannot thank them enough for their love and support. My brother, David, and his wife, Erika, have been an inspiration to me on many occasions, and I am exceedingly grateful to them. I consider my in-laws, Pat and David Gilpatric, to be two of my best friends. And my wife Jennifer and our two boys Timothy and Benjamin are the biggest joys in my life.

R. M.

I was pleased when Rick Mayes asked me to join in this collaboration to explain the importance of prospective payment in Medicare. After all, he had already done most of the heavy lifting by interviewing scores of individuals who had left important imprints on the Medicare program. He had the history down—all I needed to do, as a policy wonk working at the Urban Institute, was help him make sense of that history.

That I should be in a position to offer up policy remedies for Medicare could be

viewed as surprising. Certainly it is to me. For most of my professional career, I practiced medicine and as a general internist saw more than my share of Medicare patients. But learning how to code and bill Medicare for my services (and sometimes complain about inadequate payments) is not the proper preparation for understanding the various elements—fiscal, political, operational, and, yes, clinical—that must be factored into payment policy decisions. Rather, it was the three years I spent in what was then proudly called the Health Care Financing Administration as a senior political appointee in the Clinton administration that I developed my interest in and perspectives about Medicare payment policies.

That opportunity came pretty much out of the blue, so my first acknowledgment must go to Nancy-Ann DeParle, the HCFA administrator who hired me to run the Center for Health Plans and Providers, which was then the place from which all Medicare payment policy flowed. I also thank Mike Hash, Carol Cronin, and Kathy King, who also were political appointees during my HCFA tenure and provided much-appreciated collegiality and support as we collectively fought against Republican efforts to dismantle the traditional Medicare program. That fight continues.

I learned most of what I know about how Medicare works generally, and about prospective payment specifically, from the dedicated and hardworking career civil servants I had the privilege to work with at the center. Here, there is room to acknowledge only the senior leadership, but I benefited from contact with remarkable expertise throughout the agency. In no particular order, I want to thank Kathy Buto, Tom Hoyer, Tom Gustafson, Barbara Wynn, Stuart Streimer, Gary Bailey, Sharon Arnold, and Parashar Patel, most of whom have moved on to other jobs in other places but who gave their best to making Medicare the successful program it is, while helping me get through the day.

I have had three tours of duty working in the federal government—from the bowels of the Parklawn Building with Community Health Centers, to the rarified air of the Old Executive Office Building as a member of the Carter White House Domestic Policy Staff, to riding the I-95 corridor between Baltimore and D.C. while serving in HCFA. These have been the best three jobs I've had. I hope my contribution to Rick's book demonstrates that along the way I've learned the importance of federal government programs and the respect owed to the staff who administer them.

R. A. B.

ACRONYMS

AAPCC	adjusted average per capita costs
AHA	American Hospital Association
AMA	American Medical Association
ASCs	ambulatory surgery centers
ASIM	American Society of Internal Medicine
BBA	Balanced Budget Act of 1997
CABG	coronary artery bypass grafting
CBO	Congressional Budget Office
CDHC	consumer-directed health care
CHA	Connecticut Hospital Association
CMS	Centers for Medicare and Medicaid Services
COBRA	Consolidated Omnibus Reconciliation Act of 1985
CON	certificate of need
CPR	customary, prevailing, and reasonable
DSH	disproportionate share hospitals
DRGs	diagnosis-related groups
ERISA	Employee Retirement Income Security Act
ESP	Economic Stabilization Program
FAH	Federation of American Hospitals
FEHBP	Federal Employees Health Benefits Program
GAO	Government Accountability Office
GDP	gross domestic product
HCFA	Health Care Financing Administration
HCFPA	Health Care Facilities and Planning Act
HHS	Health and Human Services
HI	Hospital Insurance (trust fund)
HIAA	Health Insurance Association of America

HIPAA	Health Insurance Portability and Accountability Act
HMO	health maintenance organization
ICFs	intermediate care facilities
IPAs	independent practice associations
LPNs	licensed practical nurses
M + C	Medicare + Choice
MAACs	maximum allowable actual charges
MedPAC	Medicare Payment Advisory Commission
MEI	Medicare Economic Index
MMA	Medicare Prescription Drug, Improvement, and Modernization Act
MSAs	medical savings accounts
OASI	Old Age and Survivors Insurance (trust fund)
OMB	Office of Management and Budget
PHOs	physician-hospital organizations
POS	point of service plan
PPO	preferred provider organization
PPRC	Physician Payment Review Commission
PPS	prospective payment system
ProPAC	Prospective Payment Assessment Commission
PSROs	professional standards review organizations
RBRVS	resource-based relative-value scale
RNs	registered nurses
RUC	Relative-Value Scale Update Committee
SCHIP	State Children's Health Insurance Program
SGR	sustainable growth rate
SHARE	Standard Hospital Accounting and Rate Evaluation
SMI	Supplementary Medical Insurance (trust fund)
SNFs	skilled nursing facilities
SSA	Social Security Administration
TEFRA	Tax Equity and Fiscal Responsibility Act
UCR	usual, customary, and reasonable
VE	voluntary effort
VPS	volume performance standard
WHO	World Health Organization

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