



## ISSUE BRIEF

June 2012

# How does Medicare value-based purchasing work?

## Takeaways:

- The U.S. health care system still largely pays for the volume of health care services provided rather than the value of that care to patients. Medicare is undertaking several initiatives to coax the system toward paying for value.
- One such initiative is Medicare's Value-Based Purchasing Program, created under the Affordable Care Act of 2010 to reward hospitals when they meet certain standards for delivering high-quality care to patients.
- Paying for value is difficult. Policy-makers struggle with whether to use process or outcome measures, among other issues.

## PAYING FOR REPORTING

Medicare and most other U.S. insurers are volume-based purchasers; they pay based on the number of health care services provided regardless of the quality of the care. Over the past decade, however, Medicare has been laying the groundwork to become a value-based purchaser of health care services. One important step in this transition is accurately measuring the value of care. To this end, in 2002 Medicare began voluntarily collecting data from hospitals on selected measures of quality, such as whether hospitals provided certain treatments to

patients for heart attacks, heart failure, or pneumonia. In 2004, Medicare made data reporting mandatory and imposed financial penalties for failure to comply. This approach is known as pay-for-reporting. Since 2005 quality data have been publicly available on the Hospital Compare website at <http://www.hospitalcompare.hhs.gov>. However, until this year, hospitals' actual performance on quality measures has had no effect on the amount Medicare pays to providers for treating patients.

## PAYING FOR PERFORMANCE

Under the new Hospital Value-Based Purchasing (VBP) Program required by the Affordable Care Act, Medicare will shift from just paying for reporting to paying for performance and value. Starting October 1, 2012, Medicare payments to all hospitals will be reduced by 1 percent to create a funding pool for incentive payments, which will be distributed based on performance on selected quality measures.

Whether the program actually improves patient care will depend on its design, including which measures are selected, the performance requirements, and how well performance calculations take into account the severity of each patient's condition.

## VALUE-BASED PURCHASING IN HOSPITALS

In the first year of the hospital VBP program (October 2012 to October 2013), Medicare will base payments on measures in two domains: (1) clinical process of care: whether heart attack, heart failure, pneumonia and certain surgical patients received

recommended care; and (2) patient experience of care: how patients felt about the communication with doctors and nurses, responsiveness of staff and the conditions at the hospital. These measures are among those that hospitals are already tracking under the pay-for-reporting system. Medicare will look at both the hospital's achievement—how well it performs compared to other hospitals and its improvement—how its current scores compare to its earlier scores. This two-pronged approach balances the concerns of different types of hospitals. High-performing hospitals want to be rewarded for leading the pack, and safety-net hospitals serving disadvantaged populations want their improvements recognized even if their scores are modest.

Hospitals contribute equally to the VBP program funding but some hospitals will receive less back in incentive payments. To maximize payments, hospitals have to figure out how to make meaningful improvements in processes and procedures. Such changes are not always easy to identify and implement but almost always require additional resources. As a result, financially disadvantaged hospitals may have greater difficulty making needed changes. Even hospitals with significant resources have found it challenging to achieve improvement goals.

## PROCESS VS. OUTCOME MEASURES

Many of the measures tracked under pay-for-reporting and VBP are process measures that assess compliance with treatment guidelines—are patients getting the care experts recommend? Critics call this “cookbook medicine” and say it restricts the ability of doctors to tailor care for individual patients and that these measures do not always correlate with improved health outcomes. Process measures are used, in part, because they are the easiest standards to quantify and track.

The Centers for Medicare and Medicaid Services (CMS) acknowledges that process measures have

drawbacks and plans to move to outcome-based measures soon. Outcome measures are more difficult to develop, because it is hard to isolate the effect of a particular intervention on a particular patient. For the second year of the VBP program, CMS has included new outcome measures related to patient mortality and is decreasing the reliance on process measures.

- **Appropriate incentives** CMS has a methodology for identifying and retiring measures that are “topped out”—on which hospitals have little room to improve performance—but hospitals have still raised concerns that they are being asked to strive for perfect compliance on many measures. For example, in 11 of the 12 clinical process-of-care measures, the achievement threshold is 90 percent or greater. Use of measures on which hospitals are already performing well has been criticized because it shifts the focus and resources from areas where greater improvement is still needed.
- **Exploring different approaches** The VBP program is one of several initiatives by CMS to reform traditional Medicare with the goal of improving patient care. Other projects include bundled or episode-based payments, global capitated payments, and shared savings between Medicare and accountable care organizations. In addition, CMS is a member of the Partnership for Patients, which brings together stakeholders to improve the safety and reliability of hospital care.

## WANT TO KNOW MORE?

- [\*Pursuing Perfection: Raising the Bar for Health Care Performance \(RWJF\)\*](#)
- [\*Open Door Forum: Hospital Value-Based Purchasing \(CMS\)\*](#)