

**Analysis of the Economic Impact of Competitive Bidding on the DME Market:
A One Year Update**
By: Brian O’Roark, PhD

SUMMARY OF FINDINGS

Overview

- **Competitive bidding reduces the number of sellers and thereby reduces competition.** Since competition is characterized by many sellers, the laudable objective of reducing healthcare costs through competition is compromised under this program.
- **Competitive bidding concentrates market power, which creates regional oligopolies and reduces quality of patient care.** Primary among economic concerns: by eliminating nine out of ten suppliers in the market for durable medical equipment (DME), the industry would become more concentrated. The initial bid results from 2008 confirmed the fears economists have in placing market power in the hands of very few firms, including reduced service and quality of, and access to, patient care.
- **The Centers for Medicare and Medicaid Services (CMS), the federal agency that oversees Medicare, misunderstands the structure of the market.** This lead to an undesirable economic outcome where CMS benefits at the expense of both the DME market and the true consumers, patients, who are worse off because of this plan.
- **The competitive bidding program forces an unsustainable business model on the DME industry.** Ninety percent of providers were excluded from participating because they could not meet the bid. Those who qualify are forced to sustain prices for three years—an untenable position for any business.

Consumer (Patient) Impact

- With cost as the primary determining factor, competitive bidding forces consumers to utilize providers with less experience or providers that do not even have current operations near the patients’ home areas.
- During the competitive bidding trials, it was reported that over half of referrals to contracted suppliers resulted in turning down the order for various reasons related to a firm’s inability to service patients.
- During the competitive bidding trials, nearly 40% of companies awarded DME contracts for Pittsburgh-area patients were located outside of Pennsylvania.
- Had the competitive bidding program continued, homecare providers would have had no choice but to cut service, lengthen patient response times and give up providing some equipment altogether. Contracts were also awarded to unlicensed providers, which would have violated state standards.

- Providing services to Medicare may not be worth the expense to many DME firms, and, as a result these providers may decide to pull out of the program, leaving the neediest patients without service, or sub-standard service.
- Reducing supply will produce undesirable outcomes. DME firms who lose the bidding may go out of business or be forced to reduce the quality of their products and services. Patients will experience lower quality and less service. Finally, and surprisingly, CMS will also lose out because more patients will be hospitalized or forced into long term care as a result.
- In a normal market, when service and quality of care decline, new homecare providers would enter the market to fill the void. The Medicare bidding program makes this impossible because it eliminates existing competitors and stops new firms from opening.
- Reduced access and declining quality of care under competitive bidding will force patients into institutionalized care. This will lead to higher long-term costs for Medicare.
- The Medicare bidding scheme creates the potential for forcing patients that require more than a single DME item to utilize multiple providers. This redundancy would lead to more costs – not to Medicare, but to the patient.
- The bidding program ignores anticipated increases in demand that are projected as baby-boomers' needs for DME increase. This will lead to one of two outcomes:
 - First, there will be tremendous shortages of quality service due to the reduced number of DME suppliers.
 - Second, when the initial bid period ends, future DME prices will be much higher because there will be fewer providers and thus no competitive forces to temper those increases.
- Studies have shown, and CMS has acknowledged, that homecare is preferred by patients and seniors, and it has the potential to be less costly than institutional care.

DME Market Impact

- In any other market, such an attempt to restrict supply would be soundly defeated under the anti-trust laws of the United States.
- CMS has placed winning homecare providers in the unusual position that they must guarantee sustained prices for three years. In business, no firm can succeed by locking in prices for this long.
- An even more unusual aspect of the three-year guarantee is that it comes at the retail end of the market. Retailers have no control over the costs of manufacturing the products they sell or transportation costs.

- While CMS has touted the results of the first competitive bidding program (during which small businesses won 70 percent of the contracts) as showing that the program benefits small business, the only thing these results show is that CMS *severely misjudged the marketplace*. Prior to the program's initiation, CMS anticipated that 70 percent of contracts would be awarded to *large* firms – the exact *opposite* of what actually happened.
- A possible reason why the results of the program differed from expectations is that small firms are more likely to take risks to retain a portion of their business. Thus, in a form of self-preservation, they are willing to bid low simply to stay in the game.
- Small or large firms aside, there would have been a **total reduction of 90% in the number of sellers of durable medical equipment in the included MSAs (CMS 2008 Round 1 bid data)**.
- Because Medicare is the dominant buyer for a significant portion of the DME customer base, its bidding program resulted in *artificially* deflating prices, which will drive firms out of business. This puts even bid winners substantially at risk, and leads to reduced benefits for all parties involved.
- The introduction of this kind of program is generally justified by a perceived market failure. However, CMS has not demonstrated any major problems with the current market state. Prior to the bidding program, there did not appear to be any ground swell of discontent about the service provided by DME firms, nor was there a record of complaints about consumer prices, especially given that Medicare already controls price.
- One group that *would* benefit from competitive bidding is private insurance firms. Medicare reimbursement rates are the gold standard and the basis for reimbursement by all other forms of health insurance. An artificial lowering of Medicare rates is immediately followed by a lowering of all others. As Medicare price schedules fall, insurance firms' costs fall with them. And while insurance firms will enjoy bigger profits, DME suppliers will be driven out of business as the cost of supplying products and services exceeds the reimbursement rate. This will lead to reduced care for millions of seniors and patients.