Health Care Savings at Medicare Rates

By Ron Howrigon

A recent report by the Kaiser Family Foundation calculated the potential savings produced by reimbursing all health care services at Medicare rates. The savings are staggering.

In 2021 employers and individuals will spend $859 billion on health care insurance and out of pocket expenses. The Kaiser Foundation calculated how much money these employers and individuals would save if private insurers used Medicare rates to pay hospitals, doctors and other health care providers, rather than the substantially higher rates they currently pay. KFF calculated that if private insurers paid for services at Medicare rates, it would save employers and individuals over $350 billion a year. That's a 41% reduction in cost. That's an average savings of $2,096 per year for adults and $1,033 for children. Just think about that for a moment. That means a family of four would save over $6,000 per year. This could go a long way toward helping small businesses in this country. These kinds of savings would make health care much more affordable and drive down the number of uninsured in America. For many low- and middle-income families, an extra $500 per month is life changing.

So, how do we make this happen? Why haven't our law makers already drafted the Medicare Payment Act? Is this a reason to push forward with Medicare for All?

Well, like all things in life, it's not that simple. While the savings are attractive and would solve a number of problems, they don't come without side effects. In this case, the cure is much worse than the disease. So, before you start spending your savings or calling your representative to demand action, you need to look at the whole story.

The first thing to keep in mind is one man's expense is another man's revenue. Reducing health care spending by 350 billion dollars by just reducing reimbursement rates means you are reducing the revenue for hospitals and physicians by that same $350 billion. Since a reimbursement rate reduction would not reduce any costs at hospitals or doctors' offices, this revenue reduction would drop right to the bottom line. "So, what?" you say, "Hospitals and doctors have been living high on the hog for too long. It's time for them to take a little haircut." While I can appreciate that emotion, what we are talking about is more than just a little haircut. Its more than a full head shaving. This kind of revenue reduction would have catastrophic impacts on the way health care is delivered in this country and would most likely make the whole system implode.

Let's assume that roughly half of the savings would come from hospitals and the other half from physicians. With that assumption in mind, let's look at how these reimbursement cuts would impact the average hospital and the average physician.

This country has around 6,000 hospitals. The average hospital has annual revenues of about $165 million a year. If our country's hospitals had to face reimbursement reductions of $175 billion a year, it would mean the average hospital would face a revenue reduction of over $29 million annually. That's a 17% reduction in revenue. The average hospital's operating margin in America is less than 2%. So, where are the hospitals going to come up with all this money? They would have to significantly cut costs - which means staffing, equipment etc. Honestly, many hospitals in rural areas would cease to exist and large metropolitan hospitals would have to cut expenses so drastically that the care you would receive wouldn't look anything like what you see today.

The hospital situation is the good news. Things are even worse when you look at what happens to physicians in this scenario. There are around 825,000 physicians in this country, actively practicing and providing direct patient care. If those physicians took a collective cut in revenue of 175 billion dollars a year, it works out to an average reduction of $212,000 per doctor. Again, since this reimbursement reduction wouldn't reduce their expenses at all, that means this reduction would come right out of the doctors' salaries. How much would a $212,000 annual pay cut hurt? Well, the average physician salary in 2021 is projected to be $281,000 a year. That means our average doctor in this scenario would take a 75% pay cut and only make $69,000. How many doctors do you think would continue to practice after a 75% pay cut? Remember, too, that almost half of these practicing physicians are over the age of 55 and would most likely retire before enduring that kind of reduction.

So, while the thought of saving $350 billion a year is enticing, it's not without its downside. In this case, the downside means that most doctors would be unwilling to work for that wage, and our hospitals would either shut down or be turned into something you might see in a third world country.

As the great Paul Harvey used to say, "And that's the rest of the story."