

WORKING PAPER

Executive Summary

OCTOBER 2009, WP# 2009-24

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MEDICARE PART D AND THE FINANCIAL PROTECTION OF THE ELDERLY

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The Medicare Modernization Act of 2003, better known as the legislation that added the Part D prescription drug benefit to the Medicare program, represents the single most significant expansion of public insurance programs in the U.S. in the past 40 years. Despite the size and importance of this new program, however, we know very little about its effectiveness, which can be measured along several dimensions. A primary dimension is the success of this program in providing financial security. In this paper, we evaluate the gain in financial protection provided by the Part D program. We do so using the 2002-6 waves of the Medical Expenditure Panel Survey (MEPS), before and right after the implementation of this program. These rich survey data contain information not only on insurance coverage, but also prescription drug expenditures by source of payment, including out-of-pocket. This allows us to carefully model the impact of the Part D program on the distribution of expenditure risk. Our primary findings are:

- Under Part D, elderly prescription drug coverage increased by 12 percentage points, a dramatic rise. However, this figure represents only between one-quarter and one-third of elders who received public coverage.
- Part D to a large extent crowded out of other forms of prescription drug coverage, with our best estimates at 75% crowd-out.
- Prescription drug spending rose dramatically among the elderly; our central estimates suggest that there was an overall increase of \$1,100 per year spent on drugs as a result of Part D.
- Part D spending crowded out other sources of spending by 33-50%, the bulk of which came from private insurance plans.
- The large increase in drug spending was driven by a large increase not in the fraction of elderly taking prescription drugs (the extensive margin), but instead the number of prescriptions filled (the intensive margin). In particular, elderly under Part D filled on average 7 more prescriptions per year, a roughly 30% increase.
- Part D led to only a modest decline in out-of-pocket drug spending, and that this decline was concentrated in the top of the expenditure distribution.

- There is little evidence that the reduction in out-of-pocket drug spending was offset by increases in other out-of-pocket medical spending.
- Our estimates suggest that the welfare gains from the increased insurance provided by Part D were relatively small.

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