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May 23, 2008

Thomas J. Hoerger, Ph.D.
Senior Fellow, RTI International
3040 Cornwallis Road
Post Office Box 12194
Research Triangle Park, NC 27709-2194

Dear Dr. Hoerger:

As a follow up to the Ways and Means Health Subcommittee Hearing on DME Competitive Bidding on Tuesday, May 6, 2008; please respond to the following Questions for the Record.

Questions from Rep. Sam Johnson

(1) From your experience with the implementation of the demonstration project, do you believe CMS was able to successfully implement the demonstration project in the two cities? What were some of the implementation issues that were identified in this demonstration? How were they rectified in the demonstration project and were the lessons learned applied to the roll out of Round 1?

(2) The major concerns we are hearing from suppliers surround the submission of financial disclosure documents. Did you encounter any of these types of problems in the demonstration project? Any advice on how to rectify the current predicament CMS finds themselves in?

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(1) From your experience with the implementation of the demonstration project, do you believe CMS was able to successfully implement the demonstration project in the two cities? What were some of the implementation issues that were identified in this demonstration? How were they rectified in the demonstration project and were the lessons learned applied to the roll out of Round 1?
(2) The major concerns we are hearing from suppliers surround the submission of financial disclosure documents. Did you encounter any of these types of problems in the demonstration project? Any advice on how to rectify the current predicament CMS finds themselves in?

Responses

(1) Based on our evaluation, we concluded that CMS was able to successfully implement the demonstration project in the two sites. As noted in the Executive Summary of our Final Evaluation Report,

- "From an operational standpoint, CMS and [its contractor] Palmetto GBA were able to successfully implement the demonstration project. The project team was able to effectively solicit, collect, and evaluate bids; educate suppliers, referral agents, and beneficiaries; monitor quality and behavior; and administer claims throughout the demonstration.

- Although the overall implementation was successful, not everything went perfectly. A flaw in the weighting system used to evaluate bids in Round 1 of the Polk County demonstration led to higher prices in the surgical dressings category. In San Antonio, CMS delayed the start of the demonstration by 1 month, and delivery of the demonstration directories was delayed until very close to the actual starting date.

- Such problems were relatively minor and reflect one of the benefits of conducting demonstration projects: the ability to learn from the demonstration and apply the lessons if the demonstrated system is adopted on a wider scale. CMS modified the bid weights before Round 2 bidding in Polk County, and the Round 2 prices of surgical dressings declined. Similarly, the delays in San Antonio signaled the importance of including adequate time to evaluate bids and approve winners and the need to provide timely delivery of demonstration directories."

More broadly, we concluded that the overall impacts of the demonstration were largely positive. Again quoting from the Executive Summary of the Final Evaluation Report:

"Based on our evaluation, we believe that the overall impacts of the demonstration were largely positive. Competitive bidding produced lower prices, leading to lower allowed charges for the Medicare program and beneficiaries. We found that the demonstration had relatively little effect on beneficiary access, quality, and product selection. Beneficiaries remained as satisfied with their DMEPOS suppliers during the demonstration as they were before the demonstration. There is a cost to implementing the demonstration, but the estimated reductions in program expenditures exceeded the estimated costs of implementation. By definition, if the demonstration reduced allowed charges, supplier revenues had to fall, and that result will likely be viewed as a negative impact by suppliers in general. Still, the demonstration produced the expected results among suppliers; demonstration suppliers gained market share as a group, while nondemonstration suppliers lost market share."

Although I was not involved in the evaluation of bids and selection of winners for the current program, I believe that most of the lessons from the demonstration were incorporated in the design of the program. The original timeline for bidding and selection of winners in the program allowed sufficient time for notification of winners and the timely delivery of supplier directories. However, delays in the announcement of winners may have pushed back the delivery of supplier directories.

(2) Our evaluation team did not directly review the financial documents submitted by bidders during the demonstration project (they were reviewed by the implementation contractor's Bid Evaluation Panel and CMS staff). However, from our evaluation, we are aware that assessing financial status was challenging in the demonstration project. Overall, the assessments resulted in a relatively wide range of scores ranging from poor (scores less than 70 out of 100) and average (70-79 points) to good (80-89 points) and excellent (>90 points). Suppliers in the financially competitive range with quality ratings of good to excellent were selected with no conditions. Several suppliers in the financially competitive range with average quality rankings were selected conditionally; these suppliers were required to meet specific conditions to become demonstration suppliers. In San Antonio, seven suppliers were not initially selected as demonstration suppliers. Under demonstration rules, these suppliers were allowed to file for reconsideration. Six suppliers did so, and ultimately five achieved demonstration status after providing supplemental information and/or correcting deficiencies.

Collecting and assessing financial information under the program rules is even more challenging because (a) the volume of bids is much higher in the program because more sites are included, and (b) the legislation requires that contracts cannot be awarded to suppliers that fail to meet financial requirements. Financial documents are generally large and variable in format; consequently, they cannot easily be loaded into a single automated format that can be tested electronically for completeness and accuracy. I suspect that the large number of bids led to the decision to not notify bidders who did not

submit all of the required documents, while the legislative requirement led to these bids being disqualified.

There are several options for rectifying the current situation:

(a) The CBIC could notify all suppliers who have not submitted complete financial documents.

(b) The CBIC could conduct a preliminary ranking of bids and contact any suppliers who are likely to be in the competitive range but have incomplete financial documents. These suppliers would be given a short time to provide financial documentation (or show that they had previously submitted the documentation). The initial competitive range would be based on capacity estimates for those suppliers with full financial documentation; therefore, the competitive range might be reduced as the notified suppliers provided their documentation.

(c) CMS could simplify the requirements for financial documentation, creating specific forms that could be automatically verified for completion. However, it might be difficult to confirm that the information included is correct.

(d) CMS could make no changes, and rely on the first round experience convincing suppliers to take greater care in submitting the financial documents.

Of these options, I believe that (b) would best balance fair treatment for suppliers with administrative burden.

A remaining conceptual issue is whether there is enough evidence linking the required financial information to the ability of suppliers to stay in business for the duration of the contract. The point of the financial requirements is to ensure that CMS contracts with suppliers who will not go out of business. Although it is plausible that the financial variables are associated with future performance, we don't have clear evidence on how strong the association is: For example, if a supplier's financials are "poor", we don't know whether its probability of going out of business during the next 3 years is closer to 100% (clearly warranting disqualification), 50% (disqualification is questionable), or 20% (probably not warranting disqualification). Until we have better information on the relationship between the financial variables and bankruptcy, it might be better to allow such suppliers to receive contracts, but discount their estimates of capacity. This would lead to more suppliers receiving contracts.