

Medicaid Value-based Purchasing: What Is It & Why Does It Matter?

Medicaid Directors are reorienting the health care system to deliver better care and lower costs through “value-based purchasing” initiatives. These efforts are seeking to address historical fragmentation in the health care delivery system and ensure the sustainability of the Medicaid program. States are ideally positioned to lead these innovations – in partnership with consumers, providers and other payers – to meet the needs of the local community. These efforts are beginning to show early signs of success at reversing the trajectory of health care cost growth and improving the health care delivery system.

The following resource, which was developed with support from The Commonwealth Fund, provides foundational information about Medicaid value-based purchasing and the role of the federal/state partnership in ensuring the success of this state-led innovation.

What is Medicaid “value-based purchasing” and “alternative payment models”? *Medicaid value-based purchasing* is often considered any activity that a state Medicaid program undertakes to hold a provider or contracted managed care organization accountable for the costs and quality of the care they provide or pay for. Frequently, this refers to state Medicaid activities to implement alternative payment models. *Alternative payment models* change the way Medicaid programs pay providers;¹ instead of paying on a fee-for-service basis (which rewards the volume of care delivered), these models seek to incentivize value. Alternative payment models can be implemented in all types of Medicaid delivery systems, including fee-for-service Medicaid programs and in Medicaid managed care.

Why are states pursuing value-based purchasing?

States, like other stakeholders, recognize that rising costs of health care in the United States are unsustainable. The rapid growth in health care costs is especially problematic for state Medicaid programs, which serve the nation’s most complex and high-need populations, such as adults and

Key Definitions

Value-based purchasing – Generally considered any activity a state Medicaid program undertakes to hold a provider or a managed care organization accountable for the costs and quality of care they provide or pay for.

Alternative payment model – Often defined as a strategy that changes the way Medicaid providers are paid, moving away from fee-for-service payment (which rewards volume), to methods of payment that incentivize value.

¹ Alternative payment models may also be used with entities that share provider and health plan characteristics, including accountable care organizations.

children with disabilities, individuals with long-term services and support needs, and those with serious and persistent mental illness.

States also recognize that longstanding fee-for-service payment to providers has been responsible for a lack of coordination in the delivery system and poor health outcomes. It incentivizes providers to deliver a high volume of services, without financial rewards for coordinating a patient's care. This has resulted in duplication of services and fragmented care delivery, especially for Medicaid beneficiaries with the most complex physical and behavioral health needs.

Value-based purchasing initiatives seek to re-align financial incentives to reward providers for delivering coordinated, high-quality care for beneficiaries. The financial incentives also seek to promote value, meaning payment is tied to improving performance and health outcomes while also containing cost growth.

What are the most common types of Medicaid alternative payment models? The National Association of Medicaid Directors and Bailit Health Purchasing surveyed Medicaid Directors in 2015 (with support from The Commonwealth Fund) to better understand the types of alternative payment models Medicaid programs are implementing. While these models differ significantly by state, this study found that the most common types of approaches include:

- **Additional payments in support of delivery system reform.** Supplemental payments are made to a provider or group of providers for infrastructure, quality measurement and reporting. These programs most often support Health Home or Patient-centered Medical Home programs. They may also include a shared savings component, making providers eligible to receive a percentage of the net savings realized as a result of their efforts. Many state Medicaid programs are pursuing this type of model, such as Idaho, Oklahoma and Michigan.
- **Episode-based payment programs.** An identified provider or group of providers is held accountable for quality and total cost of care for specific procedures or events (such as asthma exacerbation or childbirth). There are opportunities for shared savings predicated on quality performance. Arkansas initially pioneered this approach, which has also been implemented in Ohio and Tennessee.
- **Population-based payment models.** A targeted expenditure is established for a population (Total Cost of Care) and a provider or group of providers are held responsible for quality and cost based on that targeted expenditure. In some instances, this model is applied to entities that share health plan and provider characteristics. This model usually includes an opportunity for providers to earn shared savings and may also include shared financial risk. Minnesota, Massachusetts and Rhode Island are a just a few of the states using this type of approach.

What role does the federal/state partnership play in state-led value-based purchasing?

Medicaid is jointly financed by states and the federal government, and states operate their Medicaid program in accordance with federal rules and regulations. This makes a strong federal/state partnership critical to the success of state-led value-based purchasing. Key aspects of the partnership include:

- **Ensuring federal rules, regulations, and oversight processes incentivize and encourage the use of value-based purchasing.** These rules and processes have the potential to encourage or discourage state-led value-based purchasing. For example, federal oversight processes (i.e., review of waivers,

state plan amendments, and managed care contracts and rates) could streamline state implementation of value-based purchasing. This would further facilitate state advancement of these innovations. In addition, state input in the creation of federal rules and regulations can ensure new regulations do not create unintended barriers to innovation.

- **Providing ongoing federal investment in the state reform infrastructure.** Successful state-led innovation requires time and sustained investment for states, in partnership with plans and providers, to build the complex infrastructure necessary to support reform. Medicaid's federal partners have provided key investments to help states build the infrastructure needed to transform the health care system, including through the State Innovation Model program. Ongoing investment will further accelerate the success of this state-led innovation.
- **Pursuing broad alignment between Medicare and Medicaid value-based purchasing to minimize duplication and provider confusion.** Medicare and Medicaid programs are moving along parallel tracks to transform the health care system. Without a deliberate effort to achieve broad alignment in value-based purchasing strategies, there is a risk that these efforts will diverge, causing provider confusion and duplication of effort. States and federal policymakers have begun to partner to address this concern through a series of in-person and virtual conversations. Continuing to strengthen the federal/state partnership will be critical especially as CMS implements Medicare value-based payment models under the Medicare Access and CHIP Reauthorization Act.

How do we know that state-led value-based purchasing is working? Widespread progress is being made to develop the infrastructure for reform, which is an essential foundation of success. Early evaluations are also starting to show signs that state-led reform is improving health outcomes and containing costs, including in places like Colorado, Missouri and Oregon.² But it is important to recognize that even the most advanced payment reform efforts have only had a few years of experience, and it will take time to realize the full potential of this innovation.

What resources are available about Medicaid value-based purchasing? The following resources provide additional information about how and why state Medicaid programs are transforming the health care system through value-based purchasing.

- [The Role of State Medicaid Programs in Improving the Value of the Health Care System](#). National Association of Medicaid Directors & Bailit Health Purchasing. March 24, 2016.
- [Value-based Purchasing in Medicare and Medicaid: Areas of Intersection and Opportunities for Future Alignment](#). National Association of Medicaid Directors. June 13, 2016.
- [Perspectives on Innovation: A State Medicaid Approach to Evaluation](#). National Association of Medicaid Directors. March 30, 2015.

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² [Accountable Care Collaborative 2014 Annual Report](#). Colorado Department of Health Care Policy and Financing. [Progress Report: Missouri CMHC Healthcare Homes](#). MO HealthNet. 2013. [Oregon's Health System Transformation 2015 Performance Report](#), Oregon Health Authority. June 23, 2016.