

The Costs and Benefits of Monitoring Providers: Evidence from Medicare Audits*

Maggie Shi [†]

September 2021

Abstract

Governments often outsource services to third parties and subsequently monitor them to deter wasteful spending, but monitoring can be costly. I study monitoring within Medicare, where expenditure on unnecessary care is a major source of waste. Using novel data on a large auditing program, I find that hospitals respond to monitoring by reducing admissions, but incur substantial compliance costs to do so. Patients denied admission due to monitoring are not harmed, suggesting that the marginal admission was unnecessary. But for every \$1,000 in savings to Medicare, hospitals incur \$173 in compliance costs. Taken together, increased monitoring is welfare-improving in the long run as the savings outweigh the costs.

*I gratefully acknowledge fellowship support from the Agency for Healthcare Research and Quality (#R36HS027715-01). All errors are my own.

[†]Department of Economics, Columbia University. m.shi@columbia.edu