Free Market Fix

by Joseph Slater

Health care in the United States is expensive and getting more expensive at a rapid rate. Currently, spending on health care in the United States accounts for approximately 17 percent of the Gross Domestic Product (GDP). In 2008, total health care expenditures were expected to increase by about 7 percent, or approximately twice the rate of inflation. Furthermore, the high cost of health care has made it unaffordable for 46 million Americans who are uninsured. High costs do not necessarily correlate to high quality care. Recent studies show that only 55 percent of adult patients receive recommended care.

How Do We Fix The System?

Fixing the U.S. health care system requires reducing the level of government intervention in the health care system, not increasing it. Effective reform will also necessitate making each individual insured aware of the costs she is incurring prior to consumption and to giving her incentive to make economic choices regarding offered services and to "police" the payments claimed by providers.

Four simple reforms could dramatically alter the U.S. health care system so that it would provide affordable, effective and universally available health care.

Fix The Tax Code

The tax code must be reformed to eliminate the incentive for employers to offer low cost-sharing, "rich" plan designs to their employees as tax-free benefits. The net result of these types of plans is that consumers care too little about the cost of health care at the point of service. Most proposals to remedy this problem are politically infeasible or economically insufficient to control health care spending. Fortunately, the Cato Institute put forth a reform that is politically and economically effective: so-called "Large" HSAs. Current HSAs would be transformed into Large HSAs by making the following three improvements:

1. Increase tax-free contribution limits dramatically so that the limits would meet or exceed the value of the vast majority of employees' tax free employer-sponsored health care coverage.
2. Eliminate the attendant high-deductible health plan (HDHP) requirement.
3. Allow HSA holders to spend their HSA funds on health care coverage of any type (i.e., varying coverage limits, varying product types, out-of-pocket, etc.) from any source (i.e., employer, individual plan, etc.) tax free.

Large HSAs would have to be implemented in concert with the elimination of all current health care tax breaks, including the current favorable treatment of employer-sponsor health care coverage. This is necessary so that the current cost of the employer-sponsored health coverage is returned immediately to employees' wages thus minimizing employee anxiety over the uncertainty of the new system.

Returning the value of employer-sponsored health coverage to individual employees' wages will make the large HSA concept work by giving individuals control over their health care spending while maintaining the value of their employer-sponsored coverage on a tax basis. Imagine a hypothetical individual who currently receives his health coverage through his employer. The total premium for this coverage is $6,000, of which he contributes $1,500. With a Large HSA, the employee would see the $4,500 his employer contributes in his wages. The employee could deposit the $6,000 into his HSA. Now the employee has complete control over and transparency regarding his health care spending choices. He may decide to stay with a version of his employer-sponsored plan. He may decide instead to purchase (tax-free, of course) a less-rich individual plan and keep the rest of his funds in his HSA to spend out-of-pocket as needed. Either way, the employee will now have "skin in the game" regarding the cost of his care. He

will learn to shop for the insurance coverage which best meets his needs and risk tolerance. He will also learn to seek value from his health care providers, as he no longer feels that his health care coverage is free or almost so.

Reform Health Insurance Regulations

The health insurance market needs to be liberated from the expensive and distorting effects of government regulations and mandates. This can be done by allowing individuals and groups to purchase out-of-state insurance plans, thus creating competition between states and putting pressure on regulators and lawmakers to remove assumedly well-intentioned, but excessively costly guaranteed issues, community rating laws and state mandates. The variance among state regulatory environments can make the premiums on a health insurance policy several times more expensive in one state than it would be in another. Economists have estimated that allowing individuals and groups to purchase insurance across state lines would eliminate 17 million people from the roles of the uninsured. When this approach is combined with the tax changes suggested above, as many as 24 million of the uninsured would become insured.

Open The Health Care Industry To Increased Competition

To provide the health care industry with the incentive to provide less expensive and more effective care, we need to reform laws that protect health care providers and facilities from competition. First, it is essential to eliminate state health care licensing laws to increase the number of physicians, nurse practitioners, and physician assistants providing care, while also allowing for increased competition among provider types. In spite of claims to the contrary, there are a large number of services, currently restricted to highly-trained and costly providers, which could be performed by lower cost provider types. For example, many studies have shown that midlevel clinicians, e.g. nurse practitioners, are just as effective at providing routine treatments as physicians. Removing the state licensing requirements would not make health care providers unaccountable for the quality of the care they provide. Instead, providers would work to prove their competence by demonstrating their effectiveness to consumers.

Second, state laws that require government approval of new medical facilities—so-called Certificate of Need laws (CON)—should be eliminated. Evidence suggests that even though CON laws are supposed to slow the increase of health care costs, their effect has been the opposite. In reality, CON laws increase the barriers to entry for new and more effective medical facilities, thus protecting existing facilities and systems from competition and reform. The ineffectiveness of CON laws led the federal government and several states to lift their CON mandate. Unfortunately, many states maintain their CON laws and some have even expanded them.

Malpractice Litigation Must Be Reformed

Medical malpractice lawsuits provide an important protection for health care consumers since the threat of being sued for medical malpractice provides an extra incentive for providers to limit negligence and fraud. Unfortunately, the medical liability system also interferes with the ability of providers to offer the best and most cost-effective care. Rather than increasing consumers' risk to medical malpractice —by limiting the actions of plaintiffs' counsel—providers and consumers, or insurers acting on the consumers' behalf, should be allowed to bargain for their own mutually beneficial medical malpractice liability levels in their health care services contract. Since the cost of medical malpractice liability insurance is directly reflected in the cost of health care services, allowing the marketplace to determine cost effective and sufficient liability levels would benefit providers and consumers alike. Currently, contracts that allow providers and consumers to agree on malpractice liability levels are illegal. Instead, liability levels are set uniformly by the court system at great cost to providers, insurers and consumers. Legislatures will need to act to make these contracts legal.

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A Health Care Market Instead Of A Health Care System

These basic reforms will transform the U.S. health care system into a thriving health care market. Health care consumers will now have the incentive to shop for the best insurance and bring pressure on providers to provide cost-effective and quality care. Insurance companies will be able to offer fair, adequate and affordable policies to consumers across the country. Providers of all types will be free from anti-competitive licensing requirements to offer their services in a less costly, yet consumer-satisfying manner. And finally, both providers and consumers will be free to decide cost-effective and mutually beneficial medical malpractice liability levels instead of having them imposed by the courts at their expense. Free of the damaging restraints of government intervention, the health care market will evolve to bring about less costly, more efficient and universally available health care.

What About Medicaid, Medicare, The Poor And The Chronically Ill?

The reforms outlined here will go a long way to making health care more amenable for the poor and chronically ill simply by making health care less costly and more effective. Additionally, a vibrant health care market will help reduce the cost and inefficiencies that currently plague Medicaid and Medicare. Improvements in health care delivery and health insurance operations will greatly advance the prospects of Medicare and Medicaid privatization since the providers and insurers will be able to apply new, effective tools to these programs. However, assistance to the poor and chronically ill not covered by any other program or private group insurance policy will still be necessary. Therefore, a voucher system that would allow people from these groups to purchase health care coverage from private insurers would be effective in ensuring that the no one goes without sufficient health care.

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