The Washington Times

Book Review: Priceless

By: David Hogberg **July 11, 2012**

With the Supreme Court's recent decision on Obamacare, it's clear that the only solution to repealing the Affordable Care Act lies in the ballot box. But suppose Americans elect Mitt Romney as president and a Republican Congress in November and they follow through on their promise to repeal Obamacare. Then what? Although we will be rid of a legislative and bureaucratic nightmare, we still will be left with the same dysfunctional health care system that preceded it.

Getting to the free-market health care system we deserve requires first understanding what's wrong with the current system. In "Priceless: Curing the Health Care Crisis," health economist John C. Goodman explains the perverse incentives that plague our health care system. In short, the system penalizes us for doing the right things and rewards us for doing the wrong things. The reason is that we are caught in a system of third-party payment that insulates patients from the cost of their care and discourages health care providers from innovating in ways that lower the costs of care while improving its quality.

Mr. Goodman, who is president of the National Center for Policy Analysis, has written about health care for decades. He probably is known best for popularizing the concept of health savings accounts. "Priceless" arguably is his magnum opus, taking on a variety of subjects, including the quality and access problems of our system; the catastrophe that is Obamacare; and the reform of malpractice insurance, Medicare and Medicaid.

But in the context of the current election, "Priceless"proves most useful in explaining why our private health care markets don't work properly and how to fix them. Because of federal tax law, health insurance provided by an employer is tax-free. This, Mr. Goodman, notes, has "favored third-party insurance against individual self-insurance." Because health insurance is tax-free and wages are taxed at the marginal rate, employees have an incentive to put as many dollars of benefits as possible into health insurance. This has led to the notion of "ideal heath insurance," which Mr. Goodman says is insurance "with no deductible or co-payment, making medical care essentially free at the point of delivery."

But if health insurance pays for all of a patient's health expenses, the patient has an incentive "to overuse the system, essentially consuming health care until the last amount obtained has a value that approaches zero." If patients aren't paying more of their health expenses with their own money, "they're not likely to shop around for the best buy."

When patients don't shop around, health care "providers will not compete for patients based on price. They will have no economic incentive to keep costs low the way producers do in other markets." Rather, with an insurance company - i.e., a third-party payer - paying their bills, "the incentive of providers will be to maximize against the payment formulas in order to enhance their incomes."

That, in turn, incentivizes insurance companies to interfere with the doctor-patient relationship in an effort to restrain the amount of care that is used. Ideally, they are able to eliminate primarily unnecessary care. In practice, they go after low-hanging fruit that may or may be not be necessary care. In the process, insurance companies anger both doctors and patients.

To get out of this mess, Mr. Goodman says no change in public policy is "more important than giving patients more control over health care dollars." But will Republicans follow this principle? Mitt Romney does not inspire confidence. He wants to give individuals the same tax break for health insurance that employees get for buying it through their employer. That only will encourage individuals to buy more insurance than they need, putting more of their dollars under the control of a third-party insurer. In short, it will only exacerbate the problems with the current system.

If Mr. Romney and the rest of the GOP want to get reform right, they should champion Mr. Goodman's ideas. For starters, Mr. Goodman recommends getting rid of the employer-based tax exclusion for health insurance and replacing it with an individual $2,000 tax credit for health insurance. This would incentivize people to purchase health insurance that covers largely catastrophic costs. If the person spends less than $2,000, the difference is transferred to a health savings account to help pay for small health care expenses.

Mr. Goodman also advocates changing health savings accounts so that it is easier to save for health expenses. First, let anyone who wants an HSA have one, not just those who have high-deductible insurance, as is the case under current law. Second, the money people put into the HSAs is after-tax money, but withdrawals should be tax-free. This would have three important effects: First, it would encourage people to save more money for health expenses. Second, they would become direct purchasers of health care, comparing cost and value. Third, it would incentivize health care providers to innovate and find ways to lower the cost of care while improving quality.

In short, the market for health care would begin to look like the markets for most other services, with consumers in charge and providers competing to give them what they want and need. It's not too late for the Romney campaign to read "Priceless."

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