Should Public, Private Health Plans Compete?

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Let's assume President Barack Obama keeps his campaign promise to create a parallel system for health insurance. Those who don't get insurance through an employer would have the opportunity to buy insurance through a government-run exchange. Details on how the exchange would work are murky, and the clearer they become the worse the whole idea sounds.

But that's not the worst problem. The deal-killing issue is whether one of the plans in the exchange will be a government plan.

Two questions jump to mind immediately. What would it mean for a public plan to compete with a private plan? Why would anyone want that to happen?

Let's consider each of these in turn.

Uneven Playing Field

For competition to work, both competitors must be on a level playing field. In thinking about what this might look like, some people point to the current arrangement under which private Medicare Advantage plans offer seniors an alternative to participation in conventional Medicare. The trouble with this analogy is the playing field is in no sense level.

As an entitlement program, conventional Medicare has a blank check drawn on the U.S. Treasury. No matter how sick a senior gets, no matter how many resources are used in treatment, no matter how high the costs mount, Medicare can always count on the Treasury to pay the bills. No such blank check is available to private plans.

On a level playing field, every player has the same chance to succeed or fail. This means the (risk-adjusted) premium to be paid on behalf of every potential enrollee is fixed in advance. The only way a plan can get income is by attracting the enrollees along with their premium payments.

But if every plan's revenues are determined only by their success in attracting enrollees, every plan can potentially fail. If public plans can fail just as private plans can, they are "public" in name only and in reality indistinguishable from private plans.

Asymmetrical Enforcement

There are other issues to be resolved in creating a level playing field. The law must be the same for all players. You cannot allow the public plan to use the monopsonistic power of government to push down provider fees and have them set by force of law while the private players must pay market rates. If the public plan is entitled to pay Medicare rates, private plans must have that same option as well.

A level playing field means the public plan would have no advantage either with respect

to generating revenues or controlling costs. But that means the public plan is not really "public" in any meaningful sense of the word. It would be just one more plan.

Powerful Hand of Government

That leads us to the second question. The only rational reason anyone would want a public plan to compete with private ones is the belief a public plan might (by reason of its publicness) be able to accomplish something private plans could not. But what would that something be?

To appreciate the difficulty, consider that in most places Medicare is administered by Blue Cross. But Blue Cross is also a private insurer in the commercial insurance market. Is there any reason to believe Blue Cross (when running Medicare) can do something for the government that it cannot do just as well or better for the private sector (when acting as a private insurer)?

Similarly, most women and children covered by Medicaid are in plans administered by private insurers. Is there any reason to think UnitedHealthcare or Aetna can do something for Medicaid (in their role as Medicaid contractors) they cannot do as well or better in their role as private insurers?

In all these cases, the answer must be no. An entity doesn't get better or worse at something just because it exchanges its private hat for a public hat, or vice versa.

Crowding Out Private Insurance

It's hard to escape the conclusion that advocates of public/private competition are really rooting for a public-only health care system.

As a test of this hypothesis, consider the expansion of the State Children's Health Insurance Plan, which Congress passed in January. It's estimated up to four million children will be added to the program as a result of the expansion, with half of those dropping private insurance coverage to take advantage of free insurance from government.

In their private plans, these children were able to see almost any doctor or go to any facility. Yet since most SCHIP plans pay Medicaid rates, treatment options in the public plan will be limited.

Not only are taxpayers getting hit with the cost of the program, but in half the cases access to care is going to worsen.

If we really believe in public/private competition, why not allow the new money to follow the child? Let SCHIP programs across the country compete with employer plans and private insurance. Given a cost of about $2,000 per child, if a family chooses SCHIP, SCHIP gets the money. If a private plan is chosen, the money goes to the private plan.

If proponents are sincere in their desire to foster public/private competition, let's try it with SCHIP and see how well it works.