National Center for Policy Analysis

Handbook on State Health Care Reform

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Foreword by Jeb Bush

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Foreword

HEALTH CARE REFORM

Reforming health care is one of the great challenges facing our country today. Based on our experience, true transformational reform must begin in state capitols, not in the halls of Congress. States can introduce and vet a variety of reforms. Through a process of trial-and-error, state reforms can provide an empirical basis for comprehensive action by the federal government.

The *Handbook on State Health Care Reform* provides an in-depth examination and analysis of our health care system. It is a valuable resource and practical tool for guiding policy decisions to improve quality, expand access and control the escalating costs of health care. Even in states where reform is already underway, policymakers will benefit from the insights, advice and visionary approach to solutions outlined in the *Handbook*.

Rather than complicate an already complex problem, the *Handbook* focuses on universal principles of human nature and market forces. Individuals, with the advice of their doctors, make better health care decisions for themselves and their families than institutional bureaucracies. A freer and more transparent market for health care will produce the financial incentives for providers to improve health care to compete for patients. Consequently, empowering individuals with greater freedom to spend their health care dollars in a competitive marketplace will control costs better than regulatory limits mandated across the spectrum of services.

Countering critics of market-based reform who decry the profits currently earned in the health care industry, the authors point to the real culprit — the ability to earn rewards in a system that does not serve patients well. In this light, placing patients in charge of health spending is clearly the essential ingredient for empowering them to get what they want — quality care at a reasonable price. Using unequivocal examples, the *Handbook* pinpoints the obstacles embedded in today's health system and illuminates the exceptions that prove the potential in a market-based re-design. For example,

> "**Horse and Buggy Medical Care**…doctors and patients are still interacting in the same way as they did in the horse and buggy era…At last count, there were about 7,500 specific tasks Medicare pays for. Telephone consultations are not among them. Nor are email consultations or electronic record keeping. In general, when third parties pay by task there will always be valuable services not on the list of reimbursable activities. The incentives of physicians are to perform those tasks for which there is payment and avoid those tasks for which there is no payment."

> "**Health Care without Insurance**…Parkland (Hospital in Dallas) operates what Harvard Professor Regina Herzlinger has described in other contexts as a 'focused factory.' They are so good at delivering babies, they helped produce an internationally praised textbook on how to deliver babies and their methods are being copied in Britain and other countries…Were all of Parkland's 16,000 expectant mothers enrolled in Medicaid, or private insurance, however, the experience might be worse. Prenatal care delivered by nurses rather than doctors might not be allowed under many states' Medicaid rules. Ditto for deliveries performed by midwives. And under typical state insurance regulations, patients with private coverage would be encouraged to see OBGYNs (because of zero patient cost sharing), where the cost would be higher and the overall quality of the pregnancy/delivery episode might not be as good (because of fragmented care)."

The *Handbook on State Health Care Reform* successfully challenges the prevailing assumption that the only responsible reform for health care is more government, more centralized decision-making, more mandates and more third party payment. These authors provide a rational and practical alternative to this conventional viewpoint. Greater freedom and proven market principles will provide lasting access to affordable, quality health care.

Jeb Bush

Introduction

THE CASE FOR A NEW APPROACH TO HEALTH POLICY

Why another book on health care? Because no previous book actually shows how to solve the three most important health care problems: cost, quality and access to care.

Nor for that matter does any previous book tell how to reliably insure the uninsured, or make health insurance portable, or make the insurance marketplace functional rather than dysfunctional, or solve the problems of workers' compensation or medical malpractice, or reform Medicaid, or shore up the charity care safety net, or deal with innumerable other problems.

This book is a "how to" book. It is designed to help legislators, policy analysts, think tanks and other interested parties solve the very difficult problems of health policy. We don't claim to have all the answers, but we suspect there will be much of value here that readers have not seen before.

The problem of health care spending is by far the most serious U.S. domestic policy problem. Health care spending is on a course to crowd out every other government program at the local, state and federal levels. It is also on a course to crowd out everything else in the aver-age family budget. This problem will become progressively worse year by year until 2011, when the first of the baby boomers become eligible for Medicare. At that point, the severity of the problem will begin to soar.

As we are constantly reminded by the national news media, our health care system also has problems of quality and access to medical care. Moreover, in the face of escalating health care costs, the problems of quality and access are likely to get even worse. The way most other countries try to control costs is by denying patients access to the highest quality care.

Before considering solutions, however, let's first set the stage. There are three features of health policy everyone needs to understand to get properly oriented.

Number one, health care is far and away the most complex social system there is. In fact, it may be even more complex than all other social systems combined.

Number two, health policy has been the object of more studies than any other market or area of human activity. In fact, the number of health policy studies must exceed by several orders of magnitude whatever field of endeavor is in second place.

Number three, despite the huge volume of research, the large number of active researchers and the best of all possible motivations, health policy researchers have managed to produce hardly any truly workable solutions to the problems of cost, quality and access. They haven't solved the lesser problems either. Indeed, with each passing year, the problems only seem to get worse and the solutions seem to grow increasingly elusive.

So the first important question to ask about health policy is not, what is the solution to this problem or that? It is, why have so many very bright

people toiled for so long in so many different ways without finding serious solutions to much of anything?

We believe we know the answer to this question, and it marks the point of departure for this book.

All too often, health policy analysts take the problems as given — as natural and inevitable characteristics of health care delivery. Given this assumption, they seek solutions from the outside — usually in the form of government efforts to force the system to change. To control costs, the conventional solution is to artificially push down provider incomes or restrict access to new technology. To improve quality, the conventional solution is for government to dictate standards, in effect telling doctors how to practice medicine. To improve access, the conventional solution is to expand government-funded health care to more and more groups and to make health care free at the point of delivery.

These conventional solutions have been tried in other developed countries and to a large extent they have been tried in the United States as well.[1] It is probably no exaggeration to say they have not worked very well.

In contrast to the conventional approach, we do not take the most important problems in health care as natural or inevitable. They are instead the artificial byproduct of the systematic suppression of normal market forces — which took place over the course of the 20th century.[2] Further, the solution to these problems does not lie in top-down, government-imposed remedies. It instead lies in bottom-up liberation. In particular, we need to free people from institutions that prevent them from solving problems on their own.

The most common source of problems in our health care system is the fact that most of the time people do not bear the full costs of their bad decisions or realize the full benefits of their good ones. On the buyer side of the medical marketplace, this means that patients who wastefully overuse health care resources usually pay only a small fraction of the cost of that

waste. Conversely, patients who economize and avoid waste usually reap only a small fraction of the savings from their economizing.

On the provider side of the market, incentives are also distorted. In fact, health care providers rarely reap the benefits of being better at what they do. Consider that:

- In a normal market, producers compete vigorously to meet consumer needs; in fact, the more unmeet needs there are, the greater the producer opportunities.
- In a normal market, insurers price and manage risk; in fact, the more risk there is, the greater are the insurer's opportunities.
- In a normal market, firms compete based on price and quality; in fact price reductions and quality enhancements are the principal ways to attract customers and boost profits.

In health care, by contrast, these normal market processes are subverted:

- Providers, more often than not, try to avoid the sickest patients with the hardest cases — rather than compete to attract them.
- Health insurers, more often than not, try to avoid the riskiest customers rather than viewing them as market opportunities.
- Doctors, hospitals and other providers rarely compete for patients based on price or quality; in fact, they rarely compete at all, in any meaningful sense.

Yet these problems are not insolvable. One of the most amazing facts about our health care system is that for virtually every problem there are tangible, visible solutions — not hypotheticals, but real flesh and blood answers operating here and there, in diverse places.

For example, there are numerous examples of high-quality, low-cost health care in America — they are just not the norm. If we all got our health care at the Mayo Clinic, the nation's health care bill could be reduced by one-fourth and the quality of care would be improved. If everyone went

to Intermountain Healthcare in Utah, total spending would be reduced by one-third, again with higher quality.[3]

Not only does health not have to be expensive, there is no reason in principle why we should have to wait for it. In pharmacies, shopping malls and "big box" retailers around the country, people are getting high quality primary care at walk-in clinics for half the normal cost and with very little waiting.[4]

Nor does price and quality information have to be hidden. In the international marketplace hospitals routinely quote package prices for all manner of standard surgical procedures and publish quality data (including their mortality rates) as well. Furthermore, patients can get top quality care at a fraction of what it would cost at most U.S. hospitals.[5]

So how do we get from here to there? How do we take advantage of these examples of success and get the rest of the system to copy and improve on them?

Complex systems cannot be successfully managed, regulated or reformed from above. They are simply too complex. To have any hope of making such a system functional and workable, reform must start from below. Specifically:

- Hospitals that follow the procedures at Mayo or Intermountain should find that the change attracts customers and improves the bottom line; and, if this is not the case, we should ask: what public policy changes are needed to encourage that outcome?
- Primary care doctors who increase patient convenience, consult with patients by telephone or e-mail, keep patient records electronically and order prescriptions online should find such patient pleasing improvements boost their net income; and if that is not the case, what policy changes are needed to make it so?
- Hospitals that offer package prices, make public their quality data and compete for patients based on price and quality should find

these activities rewarding; and if not, how can we make them rewarding?

- Patients who find ways to economize by avoiding unnecessary procedures, comparing prices and shopping for drugs online in a national marketplace should find that smart shopping is good for the pocketbook; and if not, what can we do to change this feature of our system as well?

Ultimately, every problem in our health care system begins with perverse incentives faced by individuals — patients, doctors, nurses, hospital managers and others. Correcting the problems means changing those incentives.

The policy proposals advanced in this book will not by themselves solve any problems. Instead they will change the institutional environment. In so doing, they will liberate everyone in the system. Problems are ultimately solved by people. The best government can do is remove the legal obstacles that prevent people from doing just that. For example:

- Our solution to the problem of the uninsured is to allow people to take dollars now spent on free care — largely in hospital emergency rooms — and buy private health insurance instead.
- Our solution to the problem of people trapped in such government health programs as Medicaid and the State Children's Health Insurance Program (S-CHIP) is to allow them to apply those same dollars to private insurance instead.
- Our solution to the problem of lack of continuity of insurance and health care is to give employees and their employers access to personal and portable insurance.
- Our solution to the problem of quality is to allow doctors and hospitals to repackage and reprice their services under government health care payment systems — allowing them to gain financially from providing better care.

- Our solution to the problem of cost is to allow patients to control more of their own health care dollars, and to allow patients and providers to benefit from new arrangements that produce lower-cost, higher-quality care.
- Our solution to the problem of long-term care is to allow people to insure for this contingency in a way that does not cause complete asset depletion if they eventually have to rely on Medicaid.
- Our solution to the problem of Workers' Compensation is to give employers and employees access to integrated health and disability plans as well as other contractual opportunities.
- Our solution to the dysfunctional medical malpractice system is to give doctors and patients the opportunity to resolve tort liability issues by contract rather than in the courtroom.

None of these solutions involve telling people what to do. Instead, we propose in every case to lower barriers, remove restrictions, repeal laws and otherwise give people the freedom to solve problems using their intelligence, creativity and innovative abilities.

We are confident that, given the freedom to do so, 300 million Americans will find better answers to health care problems than any government agency.

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John C. Goodman

Notes

[1] For a comprehensive analysis of how the national health insurance systems of other countries have not solved the problems of cost, quality and access, see John C. Goodman, Gerald L. Musgrave and Devon M. Herrick, *Lives at Risk: Single-Payer National Health Insurance around the World* (Lanham, Md.: Rowman & Littlefield, 2004).

[2] To understand how markets were systematically suppressed in the twentieth century see John C. Goodman, *Regulation of Medical Care: Is the Price Too High* (San Francisco: Cato Institute, 1980); and the summary in John C. Goodman and Gerald L. Musgrave, *Patient Power: Solving America's Health Care Crisis* (Washington, D.C.: Cato Institute, 1992).

[3] John E. Wennberg et al., "The Care of Patients with Severe Chronic Illness: an Online Report on the Medicare Program by the Dartmouth Atlas Project," Dartmouth Atlas of Health Care, Center for the Evaluative Clinical Sciences, Dartmouth Medical School, 2006. Available at http://www.dartmouthatlas.org/atlases/2006_Chronic_Care_Atlas.pdf. Accessed February 19, 2007.

[4] Rik Kirkland, "Wal-Mart's RX for Health Care," *Fortune*, April 17, 2006.

[5] Devon M. Herrick, "Medical Tourism: Global Competition in Health Care," National Center for Policy Analysis, forthcoming.