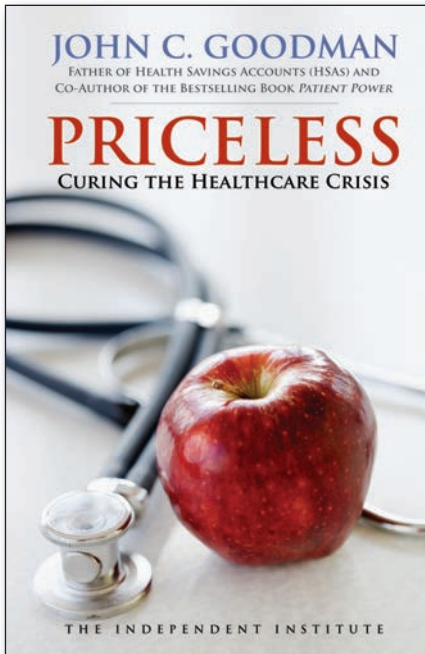


PRICELESS

Curing the Healthcare Crisis

BY JOHN C. GOODMAN



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Book Highlights

The problems in American healthcare are likely to get worse—much worse—before politicians get around to making them better.

- With the advent of the Affordable Care Act (ACA) perverse incentives will be set in place nationwide. Tens of thousands of employees will leave their employer plans and enter a no-man's land where the healthy will be desirable and the sick will be vulnerable. Those with serious health problems will find that they no longer have an employer who acts as a protector and defender. Their problems will be made worse by inexorable government pressure on the health plans to keep premiums from rising, so as to contain the expense of the taxpayer-funded premium subsidies.
- ACA will not control costs. The Affordable Care Act is relying on dozens of pilot programs and demonstration projects to find better ways of delivering care. The results have been disappointing. Further, we will still be left with a system in which no one—no patient, doctor, employer, insurer or government official—will be choosing between healthcare and other uses of money. And if no one is making those choices, healthcare spending will keep rising in the future with all the relentless persistence it has shown in the past.
- ACA may reduce access to care for our most vulnerable populations. The 32 million newly insured will try to double their consumption of healthcare and middle- and upper-middle-income families will have more generous coverage than they have now, but there will be no increase in supply. As the rationing problems escalate, those with private coverage will surely outbid people paying Medicaid rates for doctor services and hospital beds.

What would a better approach to American healthcare reform look like?

- A large portion of our healthcare dollars would be placed in Health Savings Accounts that we individually own and control. Patients would pay for most primary care, most chronic care, most discretionary care and extra out-of-network costs from these accounts.
- Doctors would advise patients on how to manage their health dollars as well as their care. They would be free to act as agents of their patients rather than of third-party payers.
- Insurance companies would specialize in the business of insurance—that is, pricing and managing risk—and leave the management of healthcare to doctors and patients.
- Employers would be free to buy individually owned insurance for their employees. They would offer a monetary contribution to be applied to the health-insurance premiums of each employee, each pay period. Most would have no more involvement in the employee's health plans than they have in their employee's 401(k) portfolio.
- Patients with chronic conditions would be empowered to manage their own care, achieving results as good or better than under traditional care. They would also manage the money that pays for that care.
- Individuals would be allowed to insure against pre-existing conditions, so they could switch health plans without financial penalty. Health plans would have incentives to compete for all potential enrollees, regardless of health condition.



The American healthcare system is plagued with problems that arise because we are trapped. Virtually all of us—patients, doctors, nurses, hospital administrators, employers, and employees—are locked into a system fraught with perverse incentives that raise the cost of healthcare, reduce its quality, and make care less accessible than it should be.

Unfortunately, conventional thinking about how to fix those problems is marred by two false beliefs. The first is the idea that to make healthcare accessible it must be free at

the point of delivery. The second is the idea that to make health insurance fair, premiums should not reflect real risks. Both ideas are the reason no one ever faces a real price for anything in the medical marketplace.

In *Priceless: Curing the Healthcare Crisis*, John C. Goodman demonstrates how these and other false beliefs eliminated normal market forces from American healthcare, making it almost impossible to solve problems the way they are solved in other markets. Relying on a common-sense understanding of how markets work, Goodman offers an unconventional diagnosis that allows him to think outside the box and propose dozens of bold reforms that would liberate patients and caregivers from the trap of a third-party payment system that stands in the way of affordable, high-quality healthcare.

A New Approach to Health Policy

The healthcare system, according to Goodman, is a “complex system.” Its gargantuan size and countless subtle intricacies make it impossible for anyone to understand how it works in every detail.

Like the economy as a whole, our healthcare system is far too complex to manage from above. But unlike a free market, American healthcare lacks a genuine price system, the mechanism that coordinates the actions of buyers and sellers in other markets. Instead, due to decades of government intervention, American healthcare is dominated by unwieldy third-party bureaucracies (insurance companies, employers, and the government) and by arbitrary payment formulas that have none of the helpful properties of market prices.

Because normal market forces have been systematically suppressed, everyone in the healthcare system faces perverse incentives that make our problems worse. Since healthcare is largely free at the point of delivery, patients are encouraged to over-consume it. Doctors are in danger of becoming agents of third-party payers, rather than agents of their patients. They are increasingly encouraged to practice “cookbook” medicine, rather than to find creative ways to improve quality and reduce costs. Employers face perverse incentives to hire the healthy and avoid the unhealthy. Health insurance companies in the soon-to-be-created

health insurance exchanges will face perverse incentives to over-provide care to the healthy and under-provide to the sick.

Four Core Problems

As in other developed countries, perverse incentives in healthcare have created problems of cost, quality, access, and lack of real insurance, Goodman explains.

Costs have escalated largely because the overwhelming bulk of payments to physicians and hospitals comes from third-party payers. For every dollar that patients spend at a doctor’s office, on average only ten cents comes out of their own pockets. This huge gap creates incentives to consume healthcare up to the point where the extra benefit is worth to patients only ten cents for every dollar paid on their behalf. In addition, healthcare providers have incentives not to search for ways to reduce prices, as producers in other markets do, but to exploit third-party payment formulas.

Quality of care also suffers. By one estimate, adverse medical events kill as many as 187,000 patients each year, and non-lethal mistakes cause an estimated six million injuries per year. Quality varies considerably from provider to provider and is unrelated to what we spend. Why, then, don’t the better hospitals compete more on quality, as producers in other markets do? Again, the incentive structure of the third-party system is to blame. When providers do not compete for patients based on price they don’t compete on quality either.

The problem of access to healthcare is widely misunderstood. For most people the obstacle isn’t so much the price of care in terms of money, it’s the price in terms of time (the time it takes to schedule and wait for a medical appointment, the time needed to travel to and from it, and so on). This “time price” of care is more burdensome for people with less income than for those with high levels of income. Unfortunately, most healthcare programs designed to eliminate the money price of care cause the “time price” of care to be much higher than it would have been.

Unlike casualty insurers, health insurers rarely tell potential customers that they need their product to help them in the event of a medical catastrophe. Instead they tend to advertise the services that healthy people want, such as wellness checkups, preventive

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care, and exercise facilities. Why? Because the health-insurance market is an artificial market in which the product offered is not real insurance. It more resembles prepayment for the consumption of healthcare.

Affordable Care Act

The Patient Protection and Affordable Care Act (ACA) is a Rube Goldberg contraption, the result of a special-interest feeding frenzy. Its individual mandates will force us to buy something whose cost is rising faster than our incomes and will eventually crowd out every other form of consumption. Its bizarre system of employer mandates (including a \$6-an-hour health minimum wage) and away-from-work subsidies will eventually force a complete restructuring of American industry.

It also creates perverse incentives. Its health insurance exchanges, for example, give insurers incentives to over-provide to healthy enrollees and under-provide to unhealthy ones.

ACA will leave our social-safety net in tatters as the demand for medical services outstrips the supply. It will create severe problems of access to care for the elderly and the disabled as Medicare payments are cut. By 2020, Medicare nationwide will pay doctors and hospitals less than what Medicaid pays, and by the time today's college students reach retirement, Medicare will be one-third gone.

Which changes are needed most to turn an unworkable health reform effort into genuine health reform? Goodman offers several ideas, including replacement of the bizarre system of subsidies and penalties with a uniform, refundable tax credit (say, \$2,500 for every adult and \$8,000 for a family of four) to fund the core insurance he wants everyone to have.

Goodman also argues that the insurance mandate should be dropped. If people choose to remain uninsured, their unclaimed tax credit could go to a local safety-net institution and used when the uninsured cannot pay their medical bills.

Reforms that Work

Goodman also offers a host of ideas that, if adopted, would enable doctors and patients to use their intelligence and creativity to make the changes needed to create access to low-cost, high-quality healthcare. Doctors, for example, would be free to repackage and re-price their services in patient-pleasing ways, rather than conform to the dictates of third-party-payer bureaucracies.

The widespread adoption of Health Savings Accounts would cut costs by 30 percent or more. Individuals would be responsible for their own primary care, most diagnostic tests, and inexpensive outpatient care. Insurers would pay for inpatient care by using a value-based purchasing approach, under which the insurer pays only the amount that will cover low-cost, high-quality care and patients pay the full extra cost if they choose to patronize other providers.

Medicare could be reformed in several ways. The perverse incentives for doctors to provide care that is too costly, too risky, and inappropriate could be eliminated. We could also reduce the misallocation of medical skills that arises from Medicare overpaying for some skills and underpaying for others. Doctors should be able to get paid in different ways so long as the cost to the taxpayer falls and the quality of care increases.

Medicaid perpetuates a two-tier health-care system—an inferior one for the poor and a better one for everyone else. Ideally,

Medicaid would be abolished and the savings would go to subsidize private insurance for low-income families. If that is too radical for the body politic, there are other alternatives. For example, Medicaid could get out of the business of dictating prices and instead oversee a Health Stamp program, fashioned after the Food Stamp program. Enrollees would be free to add their own money to the value of the stamps and purchase services in the larger medical marketplace. Low-income families on Medicaid could then compete on a level playing field with other patients for healthcare resources.

Patient safety could be improved. One way that Goodman discusses is to create an alternative to malpractice litigation: allow patients, doctors and hospitals to enter into voluntary, no-fault contracts. In return for foregoing their common-law rights to litigate, patients would be assured that if they experience an adverse outcome for a reason other than the medical condition for which they seek care (whether or not malpractice is involved), the provider institution will write them a check, without lawyers, without depositions, without judges and juries—no questions asked.

After discussing these and many other promising reforms, *Priceless* concludes with a discussion of two principles that must be applied in order to significantly improve the markets for healthcare and health insurance. First, prices must be allowed to reflect marginal social costs, where possible through the operation of market competition. Second, health insurance premiums should be able to reflect real risks in a market that enables people to insure against the onset of pre-existing conditions. The adoption of these principles would help enormously to bring about higher quality healthcare at an affordable cost.

What others are saying about *Priceless*...

“John Goodman is a highly influential health policy analyst whose ideas are always provocative and simply can't be ignored. He is right on target when he notes that future solutions to unsustainable health-cost growth must convince consumers and patients that they gain from those reforms.”

—**C. Eugene Steuerle**, Institute Fellow and Richard B. Fisher Chair, Urban Institute

“I have been following John Goodman's health policy ideas for as long as I've been on Capitol Hill. John's latest effort, *Priceless*:

Curing the Health Care Crisis, makes it abundantly clear why he is a source of wisdom, insight, and innovative thinking.”

—**Paul Ryan**, U.S. Congressman; Chairman, House Budget Committee

“John Goodman's analysis is incisive and compelling. The insight and innovative thinking in *Priceless* will be invaluable in avoiding the harms of government-run healthcare.”

—**Steve Forbes**, Chairman and Editor-in-Chief, Forbes Media

What others are saying about *Priceless*...

“John Goodman has long been the clearest and most insightful healthcare thinker we have. . . it’s time we acted on his common sense, fact-based wisdom in *Priceless*.”

—**Mitch Daniels**, Governor of Indiana

“There’s no question that today’s health care system is littered with distorted incentives and what John Goodman calls dysfunctionality. *Priceless* is a call to arms to do something about it.”

—**Peter Orszag**, former Director, Congressional Budget Office

“John Goodman’s terrific book *Priceless* . . . offers a breath of fresh air in a tired healthcare debate that demonstrates that markets enjoy their greatest advantage in complex settings that call for imaginative solutions that no government system can deliver.”

—**Richard A. Epstein**, Laurence A. Tisch Professor of Law, New York University

“John Goodman, widely known as the father of health savings accounts, is as provocative and controversial as ever in his new book, *Priceless*. His prescription for fixing what ails American health care is to free consumers to seek the health care that best suits their needs and to free physicians and hospital administra-

tors to provide the best, lowest cost care they can by getting rid of the constraints and disincentives provided by insurance companies and public payers.”

—**Gail R. Wilensky**, former Administrator, Centers for Medicare and Medicaid Services; Senior Fellow, Project Hope

“John Goodman’s book *Priceless* provides more good thinking from the person who taught us that incentives matter.”

—**Michael O. Leavitt**, former Secretary, U.S. Department of Health and Human Services

“*Priceless* is an important contribution to a market-friendly approach to reforming health care.”

—**Martin S. Feldstein**, President Emeritus, National Bureau of Economic Research; George F. Baker Professor of Economics, Harvard University

“If liberal commentators wish to sharpen their claws, there is no better stone on which to do it than John Goodman’s book *Priceless*.”

—**Uwe E. Reinhardt**, James Madison Professor of Political Economy, Princeton University

About the Author



John C. Goodman is Senior Fellow at the Independent Institute. Dr. Goodman has been President and Kellye Wright Fellow in Health Care at the National Center for Policy Analysis and editor of *Health Policy Blog*, the premier health care blog on the Internet where pro-market, pro-private-sector solutions to healthcare problems are routinely examined and debated by top health policy experts throughout the country. *The Wall Street Journal* and the *National Journal*, among other media, have called him the “Father of Health Savings Accounts.”

He is frequently invited to testify before Congress on healthcare reform, and he is the author of more than fifty studies on health policy, retirement reform and tax issues plus nine books, including *Lives at Risk: Single Payer National Health Insurance Around the World* (with Gerald Musgrave and Devon Herrick); *Leaving Women Behind: Modern Families, Outdated Laws* (with Kimberley A. Strassel and Celeste Colgan); and the trailblazing *Patient Power: Solving America’s Health Care Crisis*, which sold more than 300,000 copies. His other books include *The Handbook on State Health Care Reform*, *National Health Care in Great Britain: Lessons for the U.S.A.*, *Economics of Public Policy: The Micro View* (with Edwin Dolan), *Fighting the War of Ideas in Latin America*, and *Privatization*.

He received his Ph.D. in economics from Columbia University, and he has taught and completed research at Columbia University, Stanford University, Dartmouth College, Southern Methodist University, and the University of Dallas.

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