

No Consensus on Health Insurance Exchanges *Congress Should Rely on States and Consider Health Insurance Premium Accounts*

by Peter J. Nelson, J.D.

SUMMARY

A health insurance exchange is often reported as one of the few key congressional health care proposals with bipartisan support.

Whatever bipartisan support people perceive is illusory. The fact is, conservatives and liberals support very different versions of an exchange. Conservatives hope to sidestep regulatory burdens with an exchange, while liberals hope to add regulatory burdens. This insight makes it difficult to believe that Democrats and Republicans will come to a fully bipartisan consensus.

Without consensus, the federal government should empower states to experiment with competing types of exchanges or even other alternatives.

Health insurance premium accounts are one alternative that states should consider. A health insurance premium account would be a trust fund that aggregates financial contributions from individuals, employers, government subsidies, tax credits, and possibly relatives or charities. These accounts provide a more narrowly focused (and less disruptive) alternative to an exchange and offer a number of powerful advantages.

- First, it would create brand new opportunities for people to receive financial support to buy health insurance.
- Second, it would help equalize the treatment of health care expenses under the tax code.
- Third, it would set the groundwork for a truly functional and competitive individual insurance market.
- Fourth, it would expand choice for workers who were formerly limited to their employer's take-it-or-leave-it small group plan.
- Finally, health plans purchased through the premium account would be portable from job-to-job.

Introduction

A health insurance exchange is a key component in almost every health care proposal before Congress. In general, an exchange creates a new marketplace for health insurance that offers people more choices, better products, and a simpler shopping experience than today's often dysfunctional individual and small group insurance markets.

Ezra Klein at the *Washington Post* calls the exchange the “most important aspect of health reform.” Stanford Professor Alain Enthoven—the man behind the original exchange concept—calls it “one of the key factors of the ultimate plan's success or failure.”

Nonetheless, it receives only scant attention in the press and from politicians. Why the inattention? Two reasons: First, many perceive bipartisan support for the idea and, second, where opposition exists, it's not the often hot-headed headline-grabbing opposition voiced at town hall meetings and protests.

It's time for the press, politicians and the loyal opposition to quit sidestepping the debate over the exchange. Whatever bipartisan support people perceive is illusory. There are stark differences between conservative and liberal conceptions of an exchange, and the American public deserves to be fully informed on the issue before politicians adopt a reform that might remake the entire health insurance market. This paper outlines those differences and recommends ways to move beyond them. Without consensus, Congress should rely on states to experiment with the exchange concept. Furthermore, there is at least one less disruptive alternative to an exchange for states to test: A health insurance premium account can offer similar services without any controversial add-ons.

Where the left and right differ

Support for an exchange is not nearly as bipartisan as the press and others report. That said, it's not hard to see why people perceive bipartisanship. Both the conservative Heritage Foundation and the liberal Center for American Progress actively promote them. Also, variations on an exchange exist in leading health care proposals from both Democrats and Republicans.

Furthermore, there is some general agreement on the core idea. For most people, an exchange creates a new marketplace for health insurance that serves people who traditionally lack access to a good health plan.

However, beyond this core idea, differences quickly surface as policymakers start building the exchange and detailing what it will actually do. In this way, an exchange is sort of like the Mr. Potato Head of health reforms. Everyone agrees that he's a potato, but start adding appendages and facial features, and he can look quite different depending on who's playing with him. Similarly, various functions can be affixed to an exchange and it will look very different depending on who does the affixing.

Conservatives keep the exchange simple. First, it's an insurance premium payment aggregator that brings together funding from workers, their employers, and possibly the government. This is an important function for anyone without access to adequate employer-sponsored coverage because it creates the opportunity to get financial support to pay insurance premiums from multiple sources while receiving tax advantages like someone with generous employer coverage. Second, the exchange provides administrative services to help workers shop and apply for plans. These are the two essentials.

More liberal variations on the exchange build on these essentials and affix a variety of other functions, including premium negotiator, insurance regulator, public plan distributor, benefit designer, insurance marketer, price and quality data collector, risk adjuster, and Medicaid eligibility evaluator. Though some people on the right might be sympathetic to the last two items on this list, the remaining functions add substantial regulatory powers that most conservatives adamantly oppose.

The root of the disagreement

These differences stem from the fact that each side uses the exchange to fix a different problem.

From the conservative view, an exchange fixes a *regulatory failure*. Federal regulations tend to encourage one-size-fits-all employer-based group health plans at the expense of a competitive insurance market for portable individual plans. Further, poorly designed state regulations often drive healthy people out of the individual market, making those markets unstable and costly. The exchange helps free the insurance market from these regulatory burdens, making it more competitive and giving individuals the power to afford and control their own policies.

The left, however, relies on the exchange to fix a *market failure*. In this view, markets make shopping for health plans too complicated, and insurers cannot be trusted to provide adequate coverage or to provide coverage at all. Furthermore, the left holds that the unique characteristics of the insurance market— asymmetric information, conflicts of interest, and uneven bargaining positions—will always lead to market failure. The exchange then acts as a powerful regulator to protect consumers from insurers' inevitable excesses.

Irreconcilable differences?

Knowing the problems conservatives and liberals hope to fix reveals that their underlying intentions for the exchange are diametrically opposed. Conservatives hope to sidestep or eliminate regulatory burdens, while liberals hope to add regulatory burdens. This insight makes it difficult to believe that Democrats and Republicans will come to a fully bipartisan consensus on any exchange.

Indeed, the differences in the various Democratic and Republican proposals in Congress appear irreconcilable. The Republican House proposal leaves out the exchange altogether. Another Republican bill, the Patients' Choice Act, includes only a bare-bones state-based exchange, and it is voluntary. In contrast, the Democratic House Tri-Committee bill and the Senate HELP committee bill include what Thomas Miller, a resident fellow with the American Enterprise Institute, calls a "full-strength version." Miller, blogging at the health policy journal *Health Affairs*, explains that this full-strength version "would provide the essential regulatory connective tissue to keep the embryonic Obama plan alive and growing." Unlike the Patients' Choice Act, this would be a national exchange, which, according to Miller, "ultimately aims to route all significant health care choices through a centralized political toll booth." Obviously, a new centralized regulator is a deal breaker for Republicans.

However, differences may not be entirely irreconcilable. The recently released Senate Finance Committee bill suggests the possibility for consensus with at least a handful of Republicans. According to the chairman's mark, the exchange would be state-based and focused on providing administrative services, such as help with health plan enrollment and tax credit applications. The bill even envisions allowing for multiple exchanges to compete.

This exchange looks far more like the voluntary version in the Patients' Choice Act.

Empower states to experiment, especially when no consensus exists

As a general rule, federal health care reform should depend on states to work out details. Our current predicament is a testament to the folly of relying on the federal government's regulatory expertise. When the federal government details the rules, they might as well be chiseling commandments in granite. Once a reform resides in the federal code, there's little chance to cure unintended consequences or test other promising solutions. Indeed, many of our current problems—e.g., inequitable tax advantages, fragmented markets, unaccountable insurers, and perverse payment incentives—were laid down in the federal code decades ago, and congressional gridlock forestalls any fixes.

States do not experience the same policy inertia that afflicts Washington D.C. Failed efforts at health reform get corrected or dialed back relatively quickly at the state level. When state policies go off track, state budgets usually can't afford to maintain the status quo, and politicians—more locally accountable than their federal counterparts—can't easily ignore constituent complaints. Consider Maine. In 2003, Maine embarked on a universal health care reform effort—Dirigo Health—and, since then, has cycled through three different methods to fund the reform. Maine started with a complicated fluctuating assessment on insurance claims based on estimated health system savings, then moved to a tax on soda and beer, and, finally, imposed a flat surcharge on insurance premiums.

Health care reform is exceedingly complex and, with health care accounting for 18 percent of the economy, the consequences of cementing the wrong policy would be devastating. As laboratories of democracy, states can subject reforms to real-world tests before letting them launch nationwide. Reforms like an exchange that lack consensus pose an even greater risk of failing—someone's idea must be wrong—which makes it even more important to subject them to real-world testing.

Also, some policies may not work nationwide. What works well in one state may work less well in another. A State Coverage Initiative Issue Brief drew lessons from Rhode Island's efforts to develop an exchange and found that "the range of options to consider for an exchange can vary based on key characteristics of the state's insurance markets," including "individual and small group market structure and effectiveness, declining employer-sponsored coverage, and the state's fiscal condition." The brief offered this concluding lesson for other states: "Given the economic situation in many states, consideration of a more narrow reform – one focused on a core set of goals with a more limited exchange infrastructure may make the most sense at this time."

State experimentation has already begun in Massachusetts and Utah. Massachusetts is testing out the full-strength exchange, while Utah is pursuing a more bare-bones approach. It remains to be seen whether either of these approaches is worthwhile. The reality is, the exchange may be entirely unnecessary in states with well-functioning insurance markets. Due to differences among states, states should be free to pursue or not pursue an exchange or pursue something altogether different.

Health Insurance Premium Accounts: An alternative

As just noted, researchers who studied Rhode Island's reform efforts conclude that a more narrowly focused exchange might be better for many states. States should also consider creating *health insurance premium accounts* as an even more narrowly focused (and less disruptive) alternative to an exchange. These accounts can serve the same premium aggregator function as an exchange, without any of the controversial add-ons.

A health insurance premium account would be a trust fund that aggregates financial contributions from individuals, employers, government subsidies, tax credits, and possibly relatives or charities. Contributions to a premium account would be tax deductible or, if an employer made the contribution, excluded from income the same way premium payments are excluded today. The trust arrangement would require that the funds first be used to pay the account holder's insurance premium. After the premium was paid, the trust arrangement would direct any excess funds into a separate health insurance reserve account. (The idea for this account is borrowed from the Patients' Choice Act.) This second account would then be used to pay for any qualified medical expenses, much like a health savings account.

This relatively simple arrangement offers a number of powerful advantages.

- First, it would create brand new opportunities for people to receive financial support to buy health insurance. Many small employers that can't afford to offer a group health plan or don't offer coverage to part-time workers would be willing to contribute to premium accounts. A worker with two part-time jobs could actually come from

multiple employers. The account would also be a natural repository for government subsidies or tax credits. Further, because the account would have strict rules for the disbursement of funds, relatives and charities, who often worry whether gifts are put to their intended use, could be confident that contributions would be directed to the individual's health care.

- Second, it would help equalize the treatment of health care expenses under the tax code, which would make health insurance more affordable for anyone without access to employer-sponsored group health insurance.
- Third, it would set the groundwork for a truly functional and competitive individual insurance market by increasing the pool of people in the market. The pool would increase as more people were able to afford coverage and as many small employers shifted their workers away from dysfunctional small group markets to individual markets.
- Fourth, it would expand choice for workers who were formerly limited to their employer's take-it-or-leave-it small group plan. Also, choice could be expanded for Medicaid enrollees if the premium account were coordinated with government subsidies.
- Finally, health plans purchased through the premium account would be portable from job-to-job, even when employers funded the premium.

Because premium accounts provide the same premium aggregator function as exchanges, it is not surprising that they share many of the same advantages. Importantly, all of these advantages come without the complexity or

controversy of creating a new insurance market or piling on new federal regulations. This result should attract broader bipartisan support from state lawmakers than the exchange.

Conclusion

Months ago, politicians drew lines in the sand over the public plan option, insurance coverage mandates, and other controversial components of health care reform. This greatly helped define what was at stake, which served to educate and engage the public. Despite sharp differences, no similar line has been drawn over health insurance exchange proposals, and, as a result, both the politicians and the public remain ill-informed. It's time to start delineating where people stand.

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