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COMMENT

RE-THINKING HEALTH INSURANCE

Hans Biebl*

In May 2009, while promoting the legislation that would become the Patient Protection and Affordable Care Act (PPACA),¹ President Obama said that rising health care costs threatened the balance sheets of both the federal government and private enterprise.² He noted that any increase in health care spending consumes funds that “companies could be using to innovate and to grow, making it harder for them to compete around the world.”³ Despite the rancorous debate that surrounded this health care legislation and which culminated with the Supreme Court’s decision in *National Federation of Independent Businesses*,⁴ the PPACA was not a radical piece of legislation. It did not address the fundamental function that health insurance plays in American society. Reform in health insurance must begin with treating health insurance more like fire insurance. In other words, health insurance should function more as a means to indemnify against catastrophic financial loss and less as a means to pay for routine medical care. By treating health insurance like other types of insurance that are carried for risk protection, the runaway medical bills that imperil American government and business can be constrained. This Comment first offers a survey of spending on health care in the United States. Next, it discusses the inefficiencies of Americans using health insurance to pay for routine medical expenses. Finally, this Comment proposes the elimination of government subsidies for employer-sponsored health insurance, which would create incentives for individuals to

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1. Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

2. See Press Release, President Barack Obama, Remarks by the President on Reforming the Health Care System to Reduce Costs (MAY 11, 2009), <http://www.whitehouse.gov/the-press-office/remarks-president-reforming-health-care-system-reduce-costs>.

3. *Id.*

4. 132 S. Ct. 2566 (2012).

become healthier while also lowering their health care expenditures.

Nationwide spending on health care was \$2.7 trillion in 2011.⁵ This amounts to 17.9 percent of GDP.⁶ The good news, if there is any, is that health spending only increased 3.9 percent in 2011.⁷ This is “the same as in 2009 and 2010 — the lowest annual rates recorded in the 52 years the government has been collecting such data.”⁸ Although a low rate of health spending growth is encouraging, the medical results that the health system achieves with such high spending are not. First, on average, adults in the United States die earlier than adults in other high-income nations.⁹ Second, the health system suffers from such widespread waste that one study estimates that 30 percent of all health care expenditures pay for unnecessary or inefficiently delivered services.¹⁰ Taken together, this data suggests that Americans need to reduce their need for health care and also make better choices about how to consume health services once the need for medical care arises.

The American health system misuses health insurance. Corporations and the United States government provide health insurance that pays for the costs of routine medical care. Employers do this primarily because employer-paid health insurance plans are subsidized by the federal government.¹¹ Employers can deduct expenditures on health insurance

5. HEALTH CARE EXPENDITURES DATA, (Jan. 2012), available at <http://www.cms.gov/Research-Statistics-Data-and-Systems/Statistics-Trends-and-Reports/Reports/NationalHealthExpendData/Downloads/highlights.pdf>.

6. Robert Pear, *Growth of Health Spending Stays Low*, N.Y. TIMES (Jan. 7, 2013), <http://www.nytimes.com/2013/01/08/us/health-spending-growth-stays-low-for-third-straight-year.html>.

7. *Id.*

8. *Id.*

9. See *Americans Have Worse Health Than People in Other High-Income Countries; Health Disadvantage Is Pervasive Across Age and Socio-Economic Groups*, NAT'L ACADEMIES (Jan. 9, 2013), <http://www8.nationalacademies.org/onpinews/newsitem.aspx?RecordID=13497>.

10. See Annie Lowrey, *Study of U.S. Health Care System Finds Both Waste and Opportunity to Improve*, N.Y. TIMES (Sept. 11, 2012), <http://www.nytimes.com/2012/09/12/health/policy/waste-and-promise-seen-in-us-health-care-system.html>.

11. See 26 I.R.C. § 106 (2006). Similarly, a variety of pre-tax arrangements exist that allow individuals to fund other out-of-pocket health expenditures that may not be covered by insurance, including 26 I.R.C. § 125 for health care flex plans and 26 I.R.C. § 223 for health savings accounts.

premiums for employees as a business expense, and the health insurance that the employee receives is treated as a fringe benefit, not compensation. The employee does not pay social security tax or income tax on the compensatory benefit of the health insurance. As a result, employees have come to expect their employers to pay for their health care. In 2012, approximately 55 percent of Americans working in private industry had employer-sponsored health care plans.¹² Because of the federal subsidy, companies have little incentive to control health care costs. Individual consumers in turn have little incentive to consume health care cheaply or wisely because they do not pay for it. But if health insurance were not used to cover routine medical expenses and instead paid only for high cost procedures, both companies and consumers would take responsibility for lowering health care costs. Medical insurance, if used like fire insurance for a house, would be a financial backstop against the catastrophic loss of an asset that is too costly to replace. Properly conceived, health insurance is a policy with a low premium and a high deductible that will cover medical expenses for high-cost procedures.¹³ High deductible insurance plans align the incentives of consumers, companies, and the federal government. These insurance plans ensure that consumers will spend health dollars carefully and take low-cost preventative measures that can delay or obviate the need for medical care.

The first step in reforming health care is to remove the tax subsidy for employer-sponsored health insurance.¹⁴ This will force consumers to take responsibility for their health care choices and will eliminate the current spendthrift attitude that consumers display in their health choices.¹⁵ For example, a recent study

12. See Brian Mauersberger, *Tracking Employment-Based Health Benefits in Changing Times*, BUREAU OF LABOR STATISTICS (Jan. 27, 2012), available at <http://www.bls.gov/opub/cw/c/cm20120125ar01p1.htm>.

13. Of course, annual physician visits and other preventative care measures such as flu shots are included in high deductible health insurance policies.

14. The removal of a preferred tax treatment for employer-sponsored health insurance plans will surely be met with some resistance by employers. Employers, however, will not be affected. If all employers are treated equally under the proposed plan, no employer will have an advantage over another.

15. Whole Foods Market Inc. has had success with a program that incentivizes its employees to spend health care dollars carefully. Whole Foods deposits \$1,800 into employees' Personal Wellness Accounts and allows employees to spend that money as they see fit. At the same time, the deductible on the employee insurance plan is \$2,500. This encourages employees to monitor their health care costs. Furthermore, money not spent

suggests that as many as 40 percent of physicians acquiesce to a patient's request for a brand-name drug when a suitable generic alternative is available.¹⁶

The elimination of a tax-subsidized health system also fixes the system's unfair treatment of workers who do not have employer-sponsored insurance. For the 55 percent of Americans (virtually all employed by large businesses) who enjoy tax-free employer provided health insurance, their contribution to their health insurance premium is generally funded through a pre-tax mechanism, such as an employer-sponsored Section 125 flex plan.¹⁷ Similarly, self-employed professionals and business owners can claim 100 percent of their health insurance as a pre-Adjusted Gross Income deduction in their Form 1040.¹⁸ This gives these individuals a significant tax advantage compared to people who do not have employer-provided health insurance. Those without employer-provided coverage face entirely nondeductible insurance costs.¹⁹ Moreover, self-employed small business owners who incur a tax loss are precluded from using the pre-AGI deduction due to an income limitation.²⁰ As a result, workers employed by small companies often do not have the tax advantages of workers employed by large corporations.

In an environment without subsidized health insurance, consumers will take preventative measures. When consumers know that they are financially responsible for a large deductible for future medical care, they will engage in healthier behavior. In other words, some of the moral hazard that pervades the present system will be removed. The final step is therefore to change consumer attitudes towards health insurance. Consumers must

from the Personal Wellness Accounts rolls over to subsequent years. See John Mackey, *The Whole Foods Alternative to ObamaCare*, WALL ST. J. (Aug. 11, 2009), <http://online.wsj.com/article/SB10001424052970204251404574342170072865070.html>.

16. Eric G. Campbell et al., *Physician Acquiescence to Patient Demands for Brand-Name Drugs: Results of a National Survey of Physicians*, JAMA INTERNAL MED. (Jan. 7, 2013), available at <http://archinte.jamanetwork.com/article.aspx?articleid=1555818#qundefined>.

17. See 26 I.R.C. § 125 (2006).

18. See 26 I.R.C. § 162(1).

19. Technically, they may claim their health insurance as an itemized deduction medical cost, but, for 2012, insurance premiums and other medical expenses are only deductible to the extent they exceed 7.5 percent of Adjusted Gross Income. See 26 I.R.C. § 213(a).

20. See 26 I.R.C. § 162(1)(2)(A).

understand that low premium, high deductible plans that are not subsidized by the federal government will benefit individuals in the long run because these plans encourage healthier lifestyles. Everyone ultimately wins because aggregate national spending on health care will be lowered as individuals make both financially informed and healthier choices. To address the fiscal challenge that health care presents to the United States government and American companies, the health care system itself needs to innovate and grow. Incremental change will not bring about the transformation that will lower costs and increase quality. Only a radical change can do that, and that change begins by re-examining the role insurance plays in health care.