PERSONAL MEDICAL ACCOUNTS: AN ALTERNATIVE TO COMPULSORY HEALTH INSURANCE

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This article explains how personal medical accounts can offer a better guarantee against sickness and privation to the poor in the United States and all nations struggling under compulsory health insurance schemes.

This article proceeds as follows. The first section describes the advantages of personal medical accounts. The second and third sections draw on the experience of the United States to demonstrate the importance of innovation in saving lives and making medical care available to the poor, and how compulsory health insurance blocks such innovation. The fourth section describes how to design personal medical accounts, and a final section concludes.

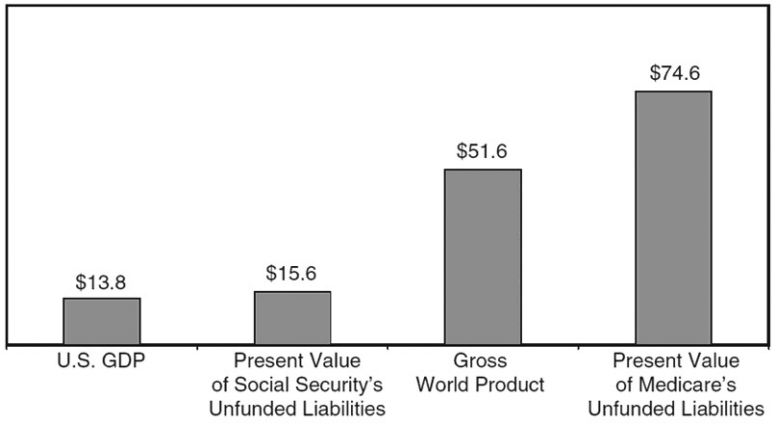
I. Advantages of personal medical accounts

In November of this year, Chile will celebrate the 30th anniversary of its Social Security reforms, which privatized the largest single government program in Chile by creating a system of personal retirement accounts. I am reliably informed, by my Cato Institute colleague José Piñera, that those reforms have been a resounding success.

We in the United States, in contrast, face an enormous problem with our state-run pension system, known as Social Security. That program has an unfunded liability larger than our annual economic output (see Figure No. 1). The United States should follow the path Chile has blazed: personal retirement accounts expand human freedom, improve economic performance, and fund what are currently unfunded commitments to the elderly.

FIGURE NO. 1

MEDICARE´S UNFUNDED LIABILITIES COMPARED WITH OTHER MEASURES, 2007
(IN USD TRILLIONS)



SOURCE: MICHAEL F. CANNON AND MICHAEL D. TANNER, HEALTHY COMPETITION: WHAT'S HOLDING BACK HEALTH CARE AND HOW TO FREE IT (WASHINGTON: CATO INSTITUTE, 2007).

The United States' state-run health insurance program for the elderly – known as Medicare – presents a much larger problem. Medicare's fiscal imbalance[2] is nearly six times greater than Social Security's. As I will explain, Medicare creates additional problems for the sick, whether elderly or non-elderly, by increasing the cost of medical care and reducing the quality of care.

Reforming the U.S. Medicare program and other compulsory health insurance schemes with personal medical accounts offers a number of advantages. Personal medical accounts are advantageous for many of the same reasons as the personal retirement and unemployment accounts adopted in Chile. They respect the workers' fundamental human right to control the fruits of their labor and the decisions affecting them and their families. Personal accounts expand the "investing class," create new opportunities for financial institutions, and broaden the political constituency for sound economic policies. They help lift families out of poverty by letting workers pass unspent balances to their heirs.

2 *See: http://www.cato.org/pub_display.php?pub_id=4556*

Personal medical accounts are advantageous for another, equally important reason. The price controls and other regulations that inevitably accompany compulsory health insurance schemes block innovations that improve the quality of medical care and bring medical care within the reach of low-income workers. By eliminating these harmful government controls, personal medical accounts will enable better medical care for the average worker and the poor. Put simply, *personal medical accounts offer a better guarantee against sickness and privation than any compulsory or state-managed system*. Since this is perhaps the most important and the least appreciated benefit of personal medical accounts, it will be the focus of my remarks.

II. Innovation

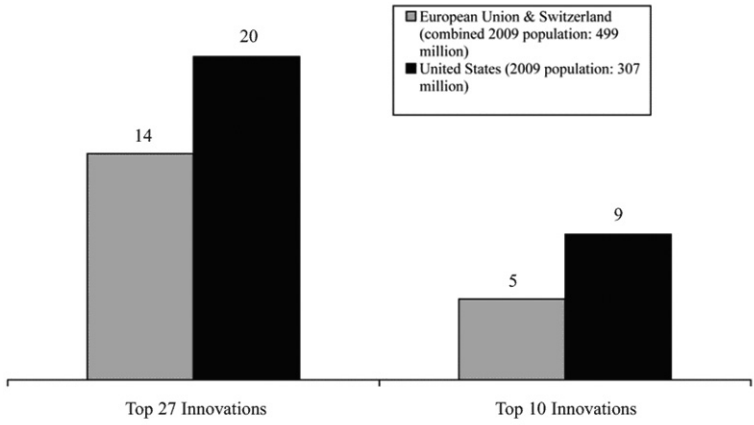
To support this claim, I will draw from the experience of the United States. Let me be clear: I do not offer the United States as a model of how to design a health care market. Contrary to international opinion, the United States emphatically does not have a free market in health care. Before this year, the U.S. health care sector was more than half-socialized; President Obama has merely socialized the rest. But because the United States' health care sector was perhaps less socialized than those of other advanced nations, it offers a glimpse into the marvelous innovations that a truly free market would create.

New Treatments

Patients worldwide suffer because there are no treatments for their illness. The United States develops most of the beneficial new medical treatments produced in the world because, more than any other nation, the United States allows innovators to profit by saving lives.

FIGURE NO. 2

TOP MEDICAL INNOVATIONS BY COUNTRY OF ORIGIN, 1975-2000



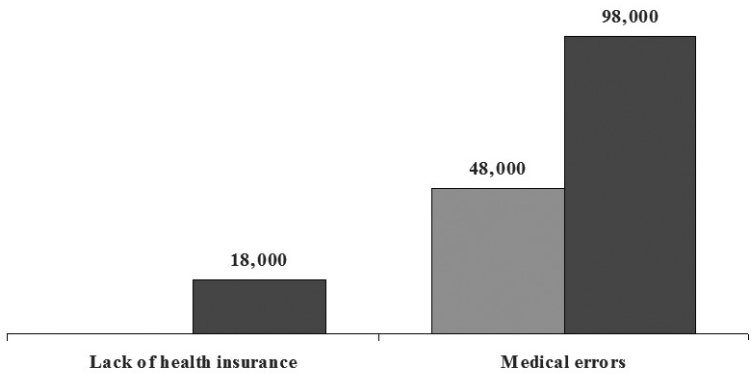
SOURCE: GLEN WHITMAN AND RAYMOND RAAD, "BENDING THE PRODUCTIVITY CURVE: WHY AMERICA LEADS THE WORLD IN MEDICAL INNOVATION," CATO INSTITUTE POLICY ANALYSIS NO. 654, NOVEMBER 18, 2009.

Figure No. 2 shows the top medical innovations from the past 40 years by country of origin. The United States has produced more than the whole of Europe. Some of these innovations include magnetic resonance imaging and computed tomography scanners (CT scanners); angiotensin-converting enzyme (ACE) inhibitors, used in the treatment of hypertension and congestive heart failure; balloon angioplasty; statins to lower cholesterol levels; mammography; and coronary artery bypass graft (CABG) surgery. These innovations were developed in whole or in part in the United States, and have been improving the lives of people around the world.

Error Reduction

Other patients suffer because medicine is too often unsafe. A leading research organization in the United States estimates that 20,000 Americans die each year because they lack health insurance. The same research organization estimates that as many as *five times* that number of Americans die each year due to medical errors (see Figure No. 3).

FIGURE NO. 3
ANNUAL PREVENTABLE DEATHS, UNITED STATES



SOURCE: INSTITUTE OF MEDICINE, UNITED STATES.

Entrepreneurs in the United States have developed private health insurance medical plans that discourage medical errors.

Secure Health Insurance

Decades ago, private health insurance companies in the United States developed innovative products that protect workers from the cost of medical care *and* protect them from high health insurance premiums when they become ill. The private sector is close to developing health insurance products that go further by enabling insurance companies to compete to cover the sickest patients, rather than avoid them.

Greater Accessibility

Entrepreneurs in the United States are developing new ways of making medical care and health insurance less costly, such as substituting lower-cost nurses for physicians and lower-cost general practitioners for specialists where appropriate. These innovations also include health insurance plans that keep premiums low by avoiding unnecessary services.

Electronic Medical Records, Coordinated Care And Effectiveness Research

Additional examples of private-sector innovation include: electronic medical records, which make medical care safer and more convenient; health systems where doctors improve quality by coordinating the services they provide to shared patients; and research on the effectiveness of medical treatments, which helps patients avoid unnecessary services and get the best available treatments.

III. Compulsory Health Insurance Blocks Innovation

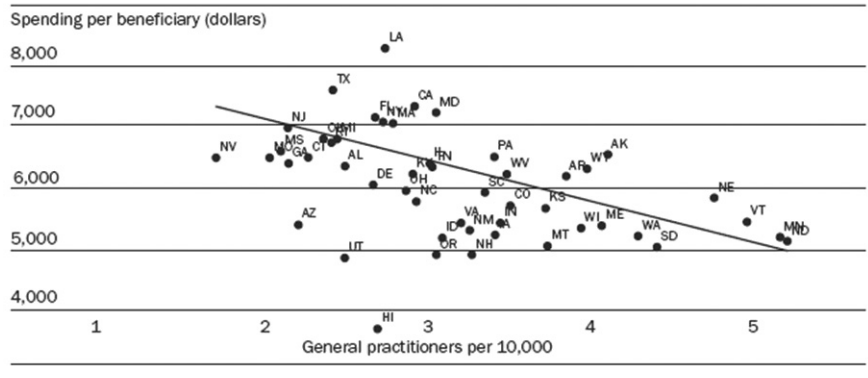
Patients in my country and in yours suffer because the price controls and other regulations that inevitably accompany compulsory health insurance schemes block these and other innovations.

Price Controls

Research in the United States shows that having a high proportion of general practitioners reduces Medicare spending (see Figure No. 4) and increases the quality of health care for Medicare patients (see Figure No. 5).

FIGURE NO. 4

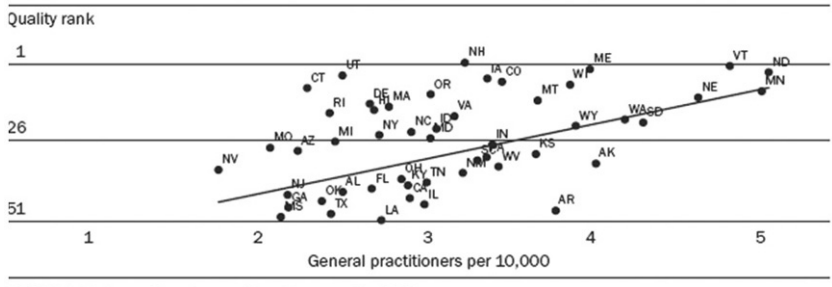
RELATIONSHIP BETWEEN PROVIDER WORKFORCE AND MEDICARE SPENDING: GENERAL PRACTITIONERS PER 10,000 AND SPENDING PER BENEFICIARY IN 2000



SOURCE: KATE BAICKER AND AMITABH CHANDRA, "MEDICARE SPENDING, THE PHYSICIAN WORKFORCE, AND BENEFICIARIES' QUALITY OF CARE," HEALTH AFFAIRS WEB EXCLUSIVE (APRIL 2004): W4-184 - W4-197.

FIGURE NO. 5

RELATIONSHIP BETWEEN PROVIDER WORKFORCE AND QUALITY: GENERAL PRACTITIONERS PER 10,000 AND QUALITY RANK IN 2000

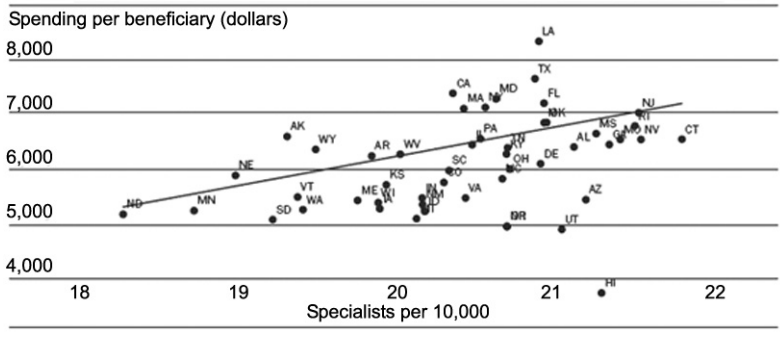


SOURCE: KATE BAICKER AND AMITABH CHANDRA, "MEDICARE SPENDING, THE PHYSICIAN WORKFORCE, AND BENEFICIARIES' QUALITY OF CARE," HEALTH AFFAIRS WEB EXCLUSIVE (APRIL 2004): W4-184 - W4-197.

Yet the U.S. Medicare program's price controls encourage doctors to become specialists, rather than general practitioners—even though research shows that a high proportion of specialists increases Medicare spending (see Figure No. 6) and reduces quality (see Figure No. 7).

FIGURE NO. 6

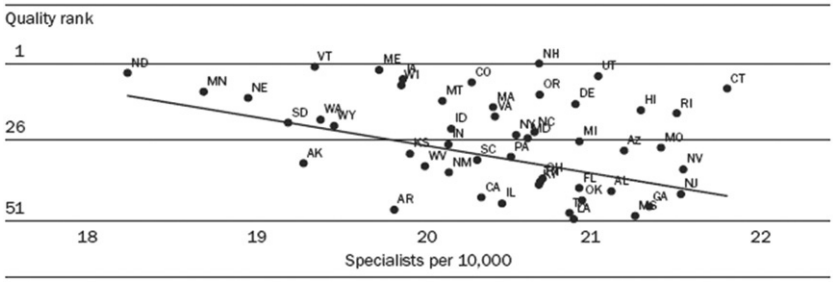
RELATIONSHIP BETWEEN PROVIDER WORKFORCE AND MEDICARE SPENDING: SPECIALISTS PER 10,000 AND SPENDING PER BENEFICIARY IN 2000



SOURCE: KATE BAICKER AND AMITABH CHANDRA, "MEDICARE SPENDING, THE PHYSICIAN WORKFORCE, AND BENEFICIARIES' QUALITY OF CARE," HEALTH AFFAIRS WEB EXCLUSIVE (APRIL 2004): W4-184 - W4-197.

FIGURE NO. 7

RELATIONSHIP BETWEEN PROVIDER WORKFORCE AND QUALITY: SPECIALISTS PER 10,000 AND QUALITY RANK IN 2000



SOURCE: KATE BAICKER AND AMITABH CHANDRA, "MEDICARE SPENDING, THE PHYSICIAN WORKFORCE, AND BENEFICIARIES' QUALITY OF CARE," HEALTH AFFAIRS WEB EXCLUSIVE (APRIL 2004): W4-184 - W4-197.

Medicare is the largest purchaser of medical care in the world. These harmful effects of Medicare's price controls therefore spill over into the private market place, increasing the cost and reducing the quality of care for privately insured patients as well.

Compulsory health insurance schemes guarantee access to medical care, but government price controls undermine that guarantee. A 12-year-old American boy named Deamonte Driver died in 2007 essentially because the U.S. Medicaid program set its prices so low that his mother could not find a dentist.

In nations with private insurance, governments impose price controls that force insurance companies to sell insurance for USD 5,000 even if a person costs USD 10,000 to insure. That creates a USD 5,000 incentive for insurers to avoid, mistreat, and dump the sick, often by denying them care. That is what happened to a 14-year-old girl in the United States named Shelby Rogers, who has spinal muscular atrophy. Shelby is so weak, she needs a nurse to turn her in bed at night and help her with other daily tasks. But her insurance company stopped paying for round-the-clock nursing care because that benefit attracted too many sick people. Those government price controls block the innovative products that would have private insurance companies competing to serve her.

Exchange Controls

The U.S. Medicare program's payment systems are de *facto* exchange controls that penalize health care providers who innovate by coordinating care, or using electronic medical records, or conducting effectiveness research, or reducing medical errors. Medicare is the driving force behind the epidemic of medical errors in the United States.

These controls render medical care more costly and deprive societies of resources that could be used to provide medical care to the needy. President Obama has brought even more of the U.S. market under the dominion of government price and exchange controls, however, because they are necessary under his state-run system.

IV. Designing Personal Medical Accounts

Personal medical accounts offer a better guarantee against sickness and privation because they can avoid government price and exchange controls, and thereby permit innovation to make medical care of ever-increasing quality available to ever-increasing numbers of workers.

A well-designed system of personal medical accounts would reduce each worker's tax burden by a percentage of income sufficient for the median wage earner to fund health insurance both now and in retirement. Those former tax payments would fund each worker's account. Chile is an example: workers must pay seven percent of their taxable salary to either a state plan (FONASA) or to a private insurance company (ISAPRE). Workers would invest their savings under rules similar to those that exist for personal retirement or unemployment accounts.

Workers would use their personal medical accounts to purchase health insurance, or to purchase medical care directly. Withdrawals for non-medical expenses would be penalized or prohibited. The difficulty of delineating between "medical expenses" and "non-medical expenses" will inevitably be messy. In the United States, we have an analogue to personal medical accounts that we call health savings accounts (HSAs); President Obama has just moved some medical expenses from the favored to the unfavored category. But this regulatory process is less distortionary than having the state decide what services health insurance must cover.

The financial institutions that manage personal medical accounts could be the same institutions that manage pensions, which already have experience in this area. These institutions would have the additional duty, however, of verifying that withdrawals are for approved medical expenses.

Importantly, a well-designed system would not require workers to purchase health insurance. This feature is controversial, but crucial. Preserving the workers' freedom to save their money, rather than purchase health insurance, is essential to make health insurance affordable for low-income workers. *Preserving the freedom to save forces insurance companies to compete with banks and other financial institutions for workers' savings.* That places enormous pressure on insurance companies to reduce the cost of health insurance. The freedom not to purchase health insurance is therefore most important to the poorest workers, because it brings the price of health insurance within their reach.

Requiring workers to purchase health insurance increases the cost of insurance because governments inevitably force workers to purchase more and more insurance coverage. In the United States and other nations, the entire medical sector lobbies governments to require workers to purchase more comprehensive insurance, because such insurance channels more money to the medical sector. Specific health care providers likewise seek to force workers to purchase insurance that covers the goods and services that they provide.

The freedom to save ensures that workers will receive value for their insurance premiums, because it preserves the workers' right to refuse insurance if they consider it a bad deal.

No doubt some workers will use this freedom to make poor decisions. Some will not purchase health insurance, and then will fall ill and not have enough savings to meet their medical expenses. I believe this problem will be small, for two reasons. First, health insurance will be less expensive, leading most workers to purchase it. Second, the very workers who might avoid health insurance will build up considerable savings in their personal medical accounts. They will want to protect those savings from the cost of illness. The way to protect those savings is to purchase health insurance.

Preserving the people's freedom not to purchase health insurance will do far less harm than giving the state the power to force people to purchase health insurance.

V. Conclusion

In designing health care markets, perfection is not an option. Under any system, whether state-run or the free market, some patients will inevitably fall through the cracks.

Personal medical accounts can help fill in those cracks by enabling innovations that improve medical care and bring it within reach of the poor. Yes, some will not earn enough to provide for themselves. And when we are free to make our own decisions, a small number of people will make poor decisions. I believe we have a moral duty to

care for patients who could not or would not provide for themselves. Personal medical accounts will make it easier for us to meet that moral duty.

Under compulsory health insurance schemes, those cracks widen, and more people fall through. Price and exchange controls block innovation. Governments waste resources on low-value medical care. Some would describe these as the unavoidable costs of creating an equitable society. But those wasted resources do not purchase solidarity. They purchase sickness and poverty.

If we seek to save lives, if we wish to bring medical care within reach of the sick and the poor, if we want to lift the poor out of poverty, then our task is to restore the workers' fundamental human rights and use personal medical accounts to let them control the fruits of their labor. Let the workers own what they have earned. Let them make their medical decisions free from coercive constraints, with all the benefits that innovation and competitive markets offer. Nations laboring under compulsory health insurance schemes should evaluate replacing those systems with personal investment accounts for medical purposes.