

*A Guide to*

# State Health Care Reform

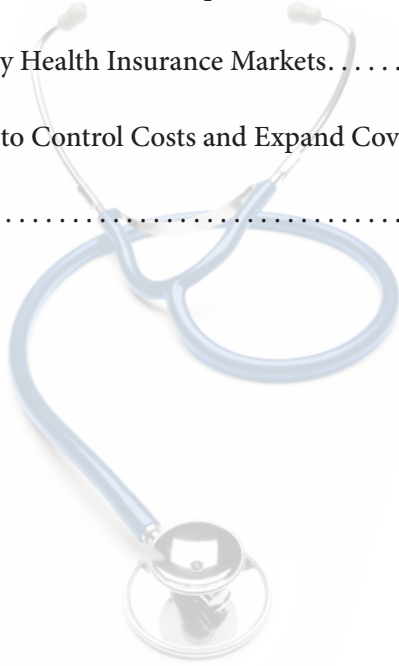


Center for Health Policy Studies

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## *Introduction*

# **An American Solution to the Health Care Crisis**

Over the past half-century, the federal government and other institutions have increasingly taken control of every American's health care. It is time to restore that control to individuals and families, both as patients and as consumers. This will require a uniquely American solution to our health care crisis—a solution that can and should arise from the states.

States have a crucial role in ensuring that every American has the opportunity and the ability to choose the health insurance and medical care that offers the best value for their health care dollars. For too long, key health care decisions have been made for patients by someone else, often employers or the government. Too often, this has meant that the interests of others are given priority over the needs of patients. It is only when individuals and families are able to choose *for themselves* among competing private insurance plans that health insurers and health care providers will have the right incentives to provide patients with better products and better results at better prices.

An essential characteristic of American health care reform must be that any reform respects the diversity and autonomy of the states. Significant variations exist among states, not only in geography and demographics, but also in how their health insurance markets and

medical delivery systems are organized and financed. The states must be permitted to retain and exercise their authority to customize solutions to meet their citizens' particular circumstances and needs.

Federal action is needed to reform the tax treatment of health insurance so that people without access to adequate employment-based insurance get the same tax breaks as those who do have such coverage. At the same time, the states, which are the principal regulators of health insurance, need to undertake reforms in their markets that increase consumer choice, expand access to more coverage options, and create true portability of insurance that allows for greater continuity of care.

States license and regulate health care providers and are much better positioned than the federal government to promote value-focused competition in health insurance and medical care by fostering transparency of information about price, quality, and outcomes. States also administer two joint federal-state programs: Medicaid and the State Children's Health Insurance Program (SCHIP). This means that they have the ability to manage those programs in ways that extend the benefits of patient empowerment and improved quality of care to their most disadvantaged residents.

In health care policy, Washington policymakers are inevitably drawn to top-down, old-fashioned centralized decision-making that vests concentrated authority in some bureau, board, or commission. The inevitable result of such an approach is the creation of a closed system that is characterized by a high degree of uniformity and restricted options with a limited capacity for innovation and change.

Such an approach is utterly incompatible with the reality that prevails in a large and diverse nation of 300 million persons, where health insurance markets and prevailing patterns of medical practice, as well as economic, social, and demographic patterns, are often radically different. Massachusetts, for example, has the highest health care costs in the nation, and Utah has the lowest; but both have embarked on

profoundly consequential health care reforms. State authorities are keenly aware of these differences and are best able to cope with their greatest challenges—especially the best ways to secure affordable and quality care for their poorest and most vulnerable citizens, who face the greatest difficulties in getting it.

There is no simple solution that is equally applicable to all states in the Union. For this reason, successful health care reform should encourage bottom-up solutions, allow for a diversity of approaches, and promote real innovation in the financing and delivery of care.

Imaginative state officials have ample authority to undertake historic reform and, in so doing, to provide their fellow citizens in other states with fruitful examples of real progress and fulfill the states' historical role as "laboratories of democracy." There is no reason for state officials to delay real reform on the ground, waiting for Washington to make such decisions for them with additional strings attached to federal dollars.

In this Guide, you will find a concise summary of actions needed to achieve patient-centered health reform and lists of publications with The Heritage Foundation's detailed research and policy guidance on each topic.



# A Federalist Approach: Encourage State Innovation

The regulation of insurance in the private sector has primarily been, and should remain, a state function. It makes sense for Washington to set only broad parameters and goals and for the states to propose and implement the best ways to arrange health insurance. Even if it were possible to create an arrangement that had the same effect from Manhattan to rural Alabama, innovations and changing conditions would quickly render it ineffective in parts of the country.

State experimentation with health insurance market reform should be encouraged as an important instrument for policy improvement. Several bipartisan bills before Congress use a federalist approach to encouraging state innovation in health care. Although these bills vary in their details, they share core elements:

- Congress should establish broad, measurable goals for increasing health care coverage while using funds more effectively and should also establish protections for vulnerable populations.
- Congress should enact a “policy toolbox” of federal reforms or programs that, while not required, would be available to states. The aim would be a package of federal initiatives and legislative waivers that represented the political spectrum on health care in Congress.

- States should offer innovative proposals to achieve the agreed goals, utilizing selected federal toolbox items and state initiatives. An independent commission would select a slate of proposals that would be implemented, subject to an up-or-down vote in Congress.
- Using the principle of pay for performance, states would receive funding according to an agreed timeline for achieving the agreed goals in the proposal.

### ***Heritage Research and Policy Recommendations***

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# Use Patient-Centered Reform Principles

Patient-centered health care reform requires the introduction of free-market principles of consumer choice and competition into a patient-centered system. Legislative changes should shift the locus of decision-making to *individuals and families*, and they, not insurers or the government or employers, should control the flow of health care dollars.

The fundamental objective of this shift is to maximize value for individuals and families so that they receive more benefit and better results for their health care dollars, both as patients and as consumers buying health insurance. Only when individuals choose and own their own health insurance will the other actors in the system, including health plans and providers, have the right incentives to deliver better value in the form of improved results at lower prices.

Patient-centered, consumer-driven health care reform legislation should embody six key principles:

- **Individuals are the key decision-makers in the health care system.** Individuals should control the flow of health care dollars.
- **Individuals buy and own their own health insurance coverage.** Most Americans do not own their health insurance; their employers or government officials own it. As a result, Americans



lose coverage as they change between jobs or government assistance programs. In a reformed system, individuals would choose and own their own health insurance.

- **The role of government is limited.** Government should make and enforce rules that create a level playing field for free-market forces and should avoid any actions that pick winners and losers.
- **Individuals have a wide range of coverage choices.** Suppliers of medical goods and services, including health plans, should enter and exit the health care market freely.
- **Prices are transparent.** Individuals should know the prices of the health insurance plan or the medical goods and services that they are buying so that they can compare the value that they receive for their money.
- **Individuals have the periodic opportunity to change health coverage.** Individuals should have the ability to pick a new health plan on predictable terms. They should not be locked into past decisions and deprived of the opportunity to make future choices.

### ***Heritage Research and Policy Recommendations***

Haislmaier, Edmund F., “Health Care Reform: Design Principles for a Patient-Centered, Consumer-Based Market,” Heritage Foundation *WebMemo* No. 2128, April 23, 2008, at <http://www.heritage.org/Research/HealthCare/bg2128.cfm>.

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# Create 21st Century Health Insurance Markets

State policymakers can redesign state health insurance markets to promote personal ownership of health plans and enable individuals and families to keep coverage regardless of employment changes, combine health premium payments from multiple employers, and benefit from federal tax advantages.

Americans get unlimited federal tax breaks for the purchase of health insurance if they receive that coverage through their workplace. Workers who buy health coverage outside of the employer-based system often have to pay for health insurance coverage with after-tax dollars and cope with high administrative costs and inflexible government mandates. With these extra costs, plans purchased outside of work can cost 40 percent to 50 percent more.

Another problem with the federal tax code is that it promotes health insurance that sticks to jobs and is not portable. The majority of uninsured are in and out of coverage, usually due to changes in their job situations, having access to insurance and then losing it.

## ***Benefits of Defined-Contribution Health Insurance Markets***

State establishment of a defined-contribution health insurance option for employers, administered through a state health insurance exchange,

is a solution that gives individuals and families the opportunity to secure the health plans of their choice without losing tax benefits, even while changing jobs. Such innovative state health insurance reforms offer solutions to many problems commonly found in current health insurance markets.

- **They reduce bureaucracy and create one-stop shopping.** A health insurance exchange serves as a market organizer and central clearinghouse for the buying and selling of health insurance and for managing related information and financial transactions.
- **They lower administrative burdens on business and increase employers' flexibility in offering health benefits.** An exchange can perform the administrative functions associated with individuals choosing and paying for health insurance, can give employers greater options for providing access to health care for employees, and can give employees expanded plan choices.
- **They provide better coverage for more people.** Like the current employer system, insurance would be guaranteed issued and would not be individually underwritten, and benefits would not diminish if health status declined.
- **They enable you to pick a plan and take it with you.** Employees, not employers, would buy their health care coverage with pre-tax dollars, would own their own health plans, and would take their plans from job to job without losing the generous tax benefits of conventional employer-based coverage.

### ***Recommended State Actions***

- **Create** a statewide health insurance market that allows defined contributions toward health care coverage.
- **Use** the state's power to regulate commercial insurance to create a new hybrid insurance market for employer-sponsored coverage through plans that are individually chosen and owned by workers.

- **Charter** a health insurance exchange as the market organizer for the new arrangement. Employers can then voluntarily sign up to designate the exchange (and all of the insurance products sold through it) as their employer group “plan” for their workers.
- **Administer** premium support for public health assistance programs through the exchange to low-income residents.
- **Consider** implementing non-subsidized health insurance risk-transfer arrangements to spread risk among insurers. While risk-transfer arrangements do not directly reduce general health care costs, they can create a more smoothly functioning health insurance market by equitably redistributing the costs of a small number of expensive cases or individuals across a broader population.

### ***Heritage Research and Policy Recommendations***

The Heritage Foundation, Health Insurance Exchange Model Bill, available by request to [ed.haislmaier@heritage.org](mailto:ed.haislmaier@heritage.org).

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# Improve Medicaid to Control Costs and Expand Coverage

Through their power to affect both supply and demand, state officials play critical roles in determining the cost of health care.

- States affect the supply of health care by licensing health care professionals; regulating health insurance markets; and controlling the development and expansion of health care services and infrastructure such as hospitals, long-term care facilities, nursing homes, and diagnostic centers through regional planning mechanisms (e.g., certificate of public need).
- States influence the demand for health care by determining eligibility for public programs, setting reimbursement rates for doctors and hospitals, and mandating health benefits, procedures, and treatments.

State policymakers can do a great deal to control costs, improve coverage, and restructure the financing and delivery of health care in their states. The simple reforms outlined below offer many benefits, including some unexpected ones.

For example, enabling Medicaid and State Children's Health Insurance Program recipients to use private health plans of their own choosing can result in more appropriate care and reduced costs to the state and the private sector. How? Families move on and off of public

assistance programs. Supporting them in the private sector will lead to increased portability and thus greater continuity of care. Fewer gaps in coverage will help to reduce costs. Private coverage will expand access and thus reduce inappropriate and costly provision of care at hospital emergency departments.

In 2004, the emergency department visit rate for Medicaid and SCHIP patients was four times the rate for patients with private health insurance. When more than one family member is eligible for assistance, private family coverage is likely to be less expensive than the cost of covering each member individually through Medicaid or SCHIP. By moving the millions of healthy Medicaid and SCHIP beneficiaries back into the private health insurance pool, states can help to reverse the detrimental effects of “crowd out” and stabilize costs for everyone.

### ***Recommended State Actions***

Within current law, state policymakers can take several needed actions. Specifically, they can:

- **Create a premium-support system for Medicaid and SCHIP recipients.** Working in conjunction with reforms in the health insurance market, premium support will enable families to enter or re-enter private insurance markets. Premium-support systems direct government payment to a private health plan of the recipient’s choice.
- **Redirect government funds from institutions to individuals.** There are several ways to achieve this goal. For example, Medicaid supplemental funding could be transformed into a fund for personal health insurance coverage. Government health care funding could be used to help individuals and families buy their own health insurance, and be redirected proportionately from health care institutions that otherwise would receive such funds to defray the costs of caring for the uninsured in emergency rooms.

Additionally, “cash and counseling” demonstration projects that provide long-term supportive services for the disabled and elderly have demonstrated increased access to services, improved patient care, and increased patient satisfaction, all without any increase in the risk of fraud. States can adopt such programs of self-direction as part of overall Medicaid reform through a simple state plan amendment process.

- **Reform health insurance markets.** State policymakers, who have an enormous amount of authority over state health insurance markets, can restructure these markets, reduce excessive benefit mandates and regulation, and foster competition both within the state and across state lines with statewide health insurance exchanges and interstate health insurance plans. States can administer premium support for public health assistance programs that benefit low-income residents through a statewide health insurance exchange.

### ***Heritage Research and Policy Recommendations***

The Heritage Foundation, Medicaid Premium Assistance Model Bill, available by request to [dennis.smith@heritage.org](mailto:dennis.smith@heritage.org).

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# Conclusion

Washington is embroiled in a major debate that could lead to far-reaching changes in America's health care system. But regardless of how this debate progresses, the nation's governors and state legislators have their own enormous opportunities to make hugely consequential reforms that would expand health insurance coverage and improve the quality of health care while empowering individuals and families to control the flow of health care dollars.

The ultimate objective of a sound health policy should be reinforcement of the traditional doctor-patient relationship in which doctors are in control of the delivery of care and patients are in control of the financing of care.

State officials can enact far-reaching reforms of their private health insurance markets that will enable all residents to secure affordable coverage while undertaking significant reforms of their Medicaid and SCHIP programs that will enable beneficiaries of those programs to secure better care through health plans of their choice and reduce their dependence on hospital emergency rooms for routine care. By pursuing serious reform, states can become the centers of innovation in American health care.

Americans will improve their health care system. They will do so largely because of the historical capacity for policy innovation that has been a hallmark of America's unique constitutional order—the Founding Fathers' wise division of authority between the states and the national government. All that is required is the political will and imagination to tackle the task.



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# Leadership *for* America

## HEALTH CARE

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