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# The Obama Health Care Budget: Hopeful Savings and Costly Change

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The President's $634 billion "down payment" on health care reform in his proposed budget depends on raising taxes and saving money largely through administrative payment changes in existing entitlement programs. That is not exactly fundamental reform.

**Down Payment or Unknown Costs.** President Barack Obama's budget sets aside $634 billion over 10 years in a health care reserve fund, which is earmarked for the enactment of unspecified policies intended to bring down costs and expand coverage. The President's budget outlines in broad terms the methods his Administration will employ to secure the projected $634 billion "down payment," but its true costs are still unknown. The budget narrative even says that "additional funding will be needed."

According to media reports, experts believe that the actual cost of his health plan is likely to be much higher, perhaps exceeding $1 trillion over 10 years. This, unfortunately, follows a familiar pattern: The actual costs of health care proposals are invariably higher than the original government projections.

**Key Provisions in the Health Care Budget:**

- *Higher Taxes.* The President is proposing tax increases on those making over $250,000 annually, and this revenue is projected to finance approximately half of the projected health care spending, an estimated $318 billion. The mechanism would limit the itemized tax deductions for these citizens, including mortgage interest deductions and charitable contributions. This would constitute a massive tax increase on these taxpayers, on top of the soon-to-expire Bush tax cuts.

  Tax policy is where health reform should start. It is therefore disappointing that the Obama Administration neglects to reform the most regressive feature of the federal tax code: the existing federal tax exclusion for health insurance. This unlimited tax break for persons enrolled in employer-based health care coverage distorts health insurance markets, undercuts consumer choice and competition, and fuels higher health care costs. In that respect, the budget proposal ignores a fundamental area of tax policy where there is an enormous intellectual consensus on the need for real change, even among economists who have advised the President.

- *Medicare Private Plan Payment Changes.* The Administration proposes cutting payments to Medicare Advantage plans. These plans are increasingly popular, enrolling one out of five senior citizens, and they provide richer and more varied packages of benefits than available under traditional Medicare. The Administration's estimate of overpayment to these plans is based on the inherently flawed payment formulas of the traditional Medicare system.

This paper, in its entirety, can be found at:
*www.heritage.org/Research/HealthCare/wm2314.cfm*

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The Administration would replace the current Medicare Advantage payment with a new "competitive bidding" model for private health plans to participate in Medicare. According to press reports, private plans would submit bids and Medicare would pay the plans based on some average of these bids.

Much depends on the details of the process. If the process is a way for the government to pick "winners and losers" (like the Defense Department procurement process) that would deny other private options for Medicare beneficiaries, it would be a direct assault on personal choice and market competition. If the plan is designed as a way of establishing a more rational benchmark payment and allowing beneficiaries to pick the plan of their choice—paying extra for richer health plans or picking less expensive health plans and keeping the savings—it would be an improvement. Even better, the Administration could include traditional Medicare, with appropriate modifications, in the competitive bidding process.

- *Medicare Prescription Drug Premiums.* The Obama Administration proposes to apply the same income-based subsidy policy for physician and outpatient services to prescription drug coverage. Under this proposal, higher-income seniors would pay higher premiums than lower-income seniors for Medicare Part D prescription drug coverage, just as they do under Medicare Part B. Income-relating Medicare subsidies, as the President has proposed, is sound policy and compatible with a broader structural change in Medicare.
- *Medicaid Prescription Drug Payment.* The Administration proposes increasing and extending Medicaid rebates for prescription drugs paid by the drug companies to the Medicaid programs. It amounts to a tax on pharmaceutical companies who offer prescription drugs in Medicaid, where drugs for the poor and the indigent are already restricted by tough formularies. It will shift more costs for drug purchases to private sector insurance. Changes in Medicaid payment formulas do not amount to Medicaid reform.
- *Medicare Payment Changes.* The Administration also calls for a variety of other payment changes designed to promote efficiency, accountability, and quality. Systemic delivery reforms, such as "pay for performance" (where physician and hospital reimbursement are tied to compliance with government practice guidelines), are intended to result in securing better value for dollars. That may not necessarily hold true, however, for some patients, and it is sure to encourage "gaming" for bonuses at the expense of others. Recalibrating the existing payment formulas for providers and medical services, however, only perpetuates the false notion that government officials can secure economic value outside of the free market. Worse, continuing to consolidate such decision-making in Washington will only exacerbate the political manipulation of the Medicare system by health care lobbyists working on behalf of special interests.

  These administrative payment changes are minor and, in and of themselves, do not amount to fundamental Medicare reform. That can be accomplished only by changing Medicare financing from a defined benefit to a defined contribution system, where consumers are making decisions based on the performance of medical professionals in providing them the personalized care they want and need.
- *Medicaid Family Planning.* The Obama Administration's budget would also expand the availability of Medicaid family planning funding. These family planning provisions already undermine parental authority by allowing children of any income level to qualify for family planning benefits without parental approval. Instead, Congress and the Administration should take active steps to reduce the vulnerability of the $350 billion Medicaid program to fraud and abuse.
- *Prescription Drug Re-Importation.* The Obama Administration also signaled new efforts to allow for the purchase and importation of prescription drugs from other countries. This is a flawed policy. Even if the federal government could guarantee the safety of these drugs, the Congressional Research Service has concluded that it would save less than 1 percent of America's spending on prescription drugs.

**Little Patient Empowerment.** President Obama's health care budget proposal is large but surprisingly


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unimaginative. It depends on old-fashioned, populist, "soak the rich" tax hikes combined with technocratic tinkering with administrative payment and new software in anticipation of program savings. It does very little to change America's flawed public and private third-party payment arrangements, where value is secured for "payers," not individual patients. If the President wants to affect real change—and secure value for individual patients rather than third party payers—he should take concrete steps to transfer direct control over health care dollars and decisions to individuals and families.

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