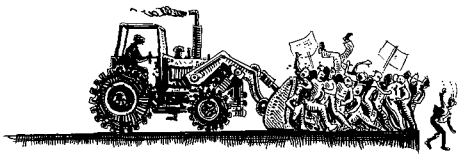

Taking Health Savings Into Account

HSAs are already solving our health policy problems.

by Peter Ferrara

BACK OFF, BARACK OBAMA. A conservative, free market health policy idea developed almost 30 years ago has taken off in the marketplace in recent years, embraced by workers, patients, and employers. That breakthrough concept is already doing what Obama claims his socialized medicine knockoff would do: reducing health costs, expanding coverage, and reducing the number of uninsured. Instead of the health care rationing that would inevitably accompany Obamacare, this policy gives Americans maximum freedom to choose and control their own health care.

The idea is Health Savings Accounts (HSAs), which I helped launch in the early 1980s, but which was mostly developed and advanced over the years by longtime National Center for Policy Analysis president John Goodman. HSAs were designed to counter the central economic problem of our health care system: the perverse incentives created by third-party payment, whether through government health programs or private insurance.

Incentives to Control Costs

WHEN GOVERNMENT OR an insurance company pays the bills, patients have no incentive to control costs. Instead of consuming health care until marginal benefits equal marginal costs, as in an efficient market, the patient with third-party payment will consume health care until the net benefit is zero. In other words, the patient has every incentive to consume health care until it literally hurts. This creates exploding health costs, which translate into rapidly rising insurance premiums and runaway government spending.

The concept behind HSAs is an insurance policy with a high annual deductible, in the range of $2,000 to $6,000 in today's products (the higher the better, as we'll see). The insight that Goodman had was that such high deductibles reduce the cost of the insurance so much that the savings mostly cover the deductible in the first year. After one healthy year with few or no medical expenses, the patient has more than enough in the account to cover all expenses below the deductible.

The HSA funds would earn interest tax-free and roll over year after year to be used for health expenses in later years. Any HSA funds used for health care expenses would also be tax-free. In retirement, remaining HSA funds could be withdrawn for any purpose, subject to ordinary tax if not used for health care. This mirrors the tax treatment provided for employer-provided health insurance, equalizing the playing field for HSAs.

HSAs transform the incentives of third-party payment. For all but catastrophic health expenses, the patient is essentially using his own money for health care. Whatever he doesn't spend he can keep. So the patient will try to avoid unnecessary care and look for less expensive care and alternatives for what he does need. This will work the best to the extent the patient can pay himself a reward at the end of the year out of whatever HSA funds he doesn't spend that year on health care, for then it will be most like his own money. He'd be making a complete

one-to-one trade-off between spending on health care and on other goods and services. Such transformed incentives would short circuit rapidly rising health costs.

Patient Power and the Market

GOODMAN ALSO HAD THE INSIGHT that HSAs give the patient complete freedom to decide what health care to spend his money on. It can be on regular checkups, preventive care or diagnostics, dental care, vision care, and any alternative medicine the patient desires but health insurance won't cover. This makes HSAs both empowering and liberating. Goodman came up with the term "patient power" as a theme for free market health reform.

Federal legislation providing for HSAs was adopted by the Republican congressional majorities in the 1990s and improved over the years. In recent years, market penetration of HSAs has exploded, as workers, patients, and employers have increasingly chosen HSAs for their coverage.

According to the annual census conducted by the Center for Policy and Research of America's Health Insurance Plans (AHIP), those with HSA or similar high-deductible plans increased by 21.5 percent from 2008 to 2009, after increasing by 35.5 percent from 2007 to 2008 and by 40.6 percent from 2006 to 2007. In 2008, 20 percent of employers with 500 or more employees offered such plans, up from 14 percent in 2007. Such plans also represented 31 percent of new coverage issued in the small group market. Overall, almost 12 million Americans now enjoy such coverage, with $9.2 billion in HSA deposits, projected to grow to $16 billion in 2010. Enrollment in such plans may well exceed HMO enrollment this year. Greg Scandlen, director of Consumers for Health Care Choices at the Heartland Institute, says, "Virtually the entire individual market is in high-deductible plans these days."

Employers also offer Health Reimbursement Accounts (HRAs), which are very similar to HSAs. The employer contributes all the money to an HRA, and retains control over it, but the employee is still free to use it for the health care he wants. About 20 percent of the privately insured population is now covered by HSAs, HRAs, or similar high-deductible coverage.

A six-year study by Aetna found that growth in health costs for companies with at least half of their workforce enrolled in such plans has been cut by more than 50 percent. Similar results were found for federal employees choosing HSAs over standard coverage. WellPoint and Cigna report no increase in costs for their HSA plans from 2007 to 2008. Similar programs offered by the American Postal Workers Union and the Government Employees Health Association experienced no increase in premiums for four years running.

The premiums for HSAs run 20 to 30 percent lower than for other insurance coverage, even with substantial funds contributed to savings in the HSA account. HSAs have consequently proven very effective in signing up the formerly uninsured. Merrill Matthews, director of the Council for Affordable Health Insurance (CAHI), reports that 33 to 40 percent of those with HSAs were previously uninsured.

The concept behind HSAs is an insurance policy with a high annual deductible, in the range of $2,000 to $6,000.

But this promising market innovation is endangered by Obama's heavy-handed government takeover of health care. Under Obama's proposed plan, employers are required to provide, and workers are required to obtain, health insurance approved by the government. Obama's bureaucrats are unlikely to approve high-deductible HSAs as an acceptable health plan. Liberal Democrats are incapable of following the economic reasoning regarding the problem of third-party payment, and how HSAs would counter that problem. Moreover, low-cost HSAs would likely be the one attractive alternative to the government-subsidized public option and so run counter to the liberal-left dream of forcing everyone into one government health plan ("Medicare for All"). So the government bureaucracy is likely to nix HSAs once it gets the power to do so.

Indeed, the House bill includes a provision making the purchase of individual insurance illegal. That would prevent all future purchases of individual HSA plans, forcing all individual purchasers into the government-run public option.

Free Market Alternatives to Obamacare

OBAMA'S GOVERNMENT TAKEOVER of health care is completely unnecessary. HSAs and related measures can serve as the foundation for a comprehensive free market alternative that will actually reduce costs, unlike Obama's centralized

bureaucracy and welfare plan, while also providing a true safety net for the uninsured, so that no one will suffer without essential health care.

Besides HSAs, a second component of a comprehensive alternative plan should be state uninsurable risk pools. The majority of states already have such uninsurable risk pools. The uninsured who become too sick to buy private health insurance can turn to their state's risk pool for coverage. They are charged premiums for such coverage based on their ability to pay. Each state then subsidizes its uninsurable risk pool to ensure that it can cover all costs.

Trying to force all people into the same market risk pools through such policies as guaranteed issue and community rating simply ruins health insurance for the general public, making it too expensive and sharply increasing the number of uninsured as a result.

Few people become truly uninsurable because of their health conditions. But trying to force these people into the same market risk pools as everyone else through such policies as guaranteed issue (requiring insurers to accept all applicants for coverage regardless of health condition) and community rating (requiring insurers to charge everyone the same regardless of health condition) simply ruins health insurance for the general public, making it too expensive and sharply increasing the number of uninsured as a result. Providing for the uninsurable separately through their own pool is consequently a much better policy.

A third component of the comprehensive alternative package should be Medicaid reform. It should be based on the enormously successful 1996 reform of the old Aid to Families with Dependent Children program (AFDC). That reform sent the federal share of spending for the program back to each state in a finite block grant, freeing each state to create a new welfare program based on work.

The old program was based on a matching spending formula, with the federal government spending more on the program the more each state spent. This only encouraged states to sign up more and more people for AFDC welfare. The 1996 reforms ended this practice. If costs for the program rose in a state, the state had to pay for the added costs itself. If the state saved money through innovation and finding work for those on the program, it could keep the savings. The results were spectacular. Within a couple of years, the old AFDC welfare rolls were reduced nationally by nearly 60 percent.

Medicaid reform should follow the same model. The current federal matching formula would be replaced by one of finite block grants to each state, to be used for a completely redesigned Medicaid program in each state. States could then better serve the poor by using the program to provide vouchers for the purchase of private insurance, enabling the poor to enjoy the same health coverage as the middle class. Poor families would then be free to choose the health insurance coverage they prefer, including health savings accounts. The vouchers should be subject to a work requirement for the able-bodied, just as with modernized AFDC.

Each state's voters would be free to decide how much assistance for the purchase of health insurance they wanted to provide at what income levels. The poor should be assured of enough assistance to purchase at least basic, essential coverage, so no one would have to go uninsured because they didn't have enough money.

Another component of reform would be for federal and state governments to reduce the costs of health insurance by repealing all requirements for guaranteed issue and community rating, which Medicaid vouchers and state uninsurable risk pools render completely unnecessary and counterproductive.

Further market reforms would be included in a comprehensive alternative to Obamacare as well. This would be the agenda of a truly forward-looking president and political party, rather than Obama's throwback to the socialized medicine failures of the last century. These free market alternatives are based on policies and practices that have already been shown to work. If our country is to experience genuine health care reform, this is where the public-policy debate of the future should focus.

Peter Ferrara *is Director of Entitlement and Budget Policy for the Institute for Policy Innovation. He served in the White House Office of Policy Development under President Reagan, and as Associate Deputy Attorney General of the United States under the first President Bush.*

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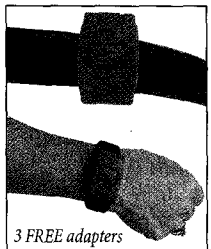

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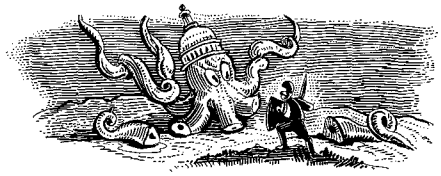

Can We Do Without Relativity?

by Tom Bethell

SOMETHING TELLS ME THAT MY NEW BOOK—*Questioning Einstein: Is Relativity Necessary?*—is unlikely to be reviewed. So I shall say something about it here. I have been working on it on and off for years, and it is based on the original work of a good friend of mine, Petr Beckmann. A Czech immigrant who taught electrical engineering at the University of Colorado, he wrote a brilliant book called *Einstein Plus Two.* But it was also difficult—written in the language of mathematical physics. I interviewed him at length, and told him I would write a simpler version. Then, too soon, he died (in 1993). I was able to finish the book with the help of Howard Hayden, who taught physics at the University of Connecticut and who became convinced that Beckmann's criticisms of relativity were right.

Most people know little about relativity theory, but we recognize that it was highly influential and that Einstein's theory somehow rewrote the laws of physics. It is divided into two parts, the special theory (1905) and the more difficult general theory (1916). The generally accepted view is that the special theory has been proven over and over again, while the general theory perhaps can be questioned and retested. In Beckmann's theory, this is more or less reversed. The general theory gives the right answers but by a complicated and roundabout route. Meanwhile a simpler path lay at hand. But the special theory may have to be discarded because the logical consequences of its postulates do not correspond to experimental results.

Here's one way of looking at the subject. We've all heard of the equation $E = mc^2$, saying that the energy of a body is proportional to its mass. It was derived by Einstein using relativity theory. Less well known is that it was derived by him again later, without relativity. He called the later version his "elementary derivation." Relativity wasn't necessary to derive the most famous equation in physics.

Beckmann extends that way of looking at the issue across the board. The physical facts that seem to demand relativity can be explained by classical physics. That is the argument of my book. It is written without math and in plain English; only a few technical terms need to be explained.

It was the Michelson-Morley experiment of 1887, conducted in Cleveland, Ohio, that led to the theory of relativity. If you don't know about that key experiment, then you will after reading my book. (The claim that this experiment led to relativity has lately been challenged, but for decades it was the standard view and I believe it should be still. The dispute does not affect Beckmann's more basic revision of relativity.)

Light is a wave form and so it was widely assumed in the 1880s that there must be a medium for it to wave in. It was called the ether, and it was believed to fill all of space uniformly. As the earth orbited the sun, its passage through the ether should have been detected by the instrument that Albert Michelson had perfected, the interferometer. But no such effect was observed.

Einstein responded with the theory of relativity, positing that the speed of light is a constant and that the ether didn't exist at all. This would explain the Michelson-Morley null result, but then came the general theory, the observed bending of starlight passing close by the sun and the slowing of light as