

# **Achieving Healthcare Cost Reductions Through Market Incentives**

**The Keys to Healthcare Cost Reduction Are:**

- **Universal Enrollment**
- **“Normalization” of the Health Insurance Market**

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# Achieving Healthcare Cost Reduction Through Market Incentives



## The Keys to Healthcare Cost Reduction are:

- **Universal enrollment**
- **“Normalization” of the health insurance market**

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Health insurance costs consistently rise faster than the rate of inflation, health benefits continue to shrink, expenditures for health insurance and medical services consume an ever greater portion of U.S. GDP, and an estimated 18,000 lives end prematurely each year simply because the United States lacks universal healthcare coverage.<sup>1-3 8</sup>

The healthcare systems of other nations of the Organization for Economic Cooperation and Development (OECD) have universal coverage and substantially lower healthcare costs. The main reason for this difference lies in their approach to health insurance.

Other nations approach health insurance as a “cost-redistribution” responsibility rather than as a financial “risk-mitigation” opportunity. Two features of these healthcare systems assist them in cost containment. One is simply universal enrollment; the other is “normalization” of the health insurance market.<sup>6</sup>

In spite of the moral imperative to save lives and improve health, meaningful changes have not occurred in the U.S. Cost containment has not been satisfactorily addressed because the U.S. lacks a universal coverage healthcare policy and the responsibilities of the health insurance industry have not been defined.

This Position Paper proposes that changes in the U.S. healthcare system without cost reduction will fail to protect U.S. industries or workers, and the keys to cost reduction are:

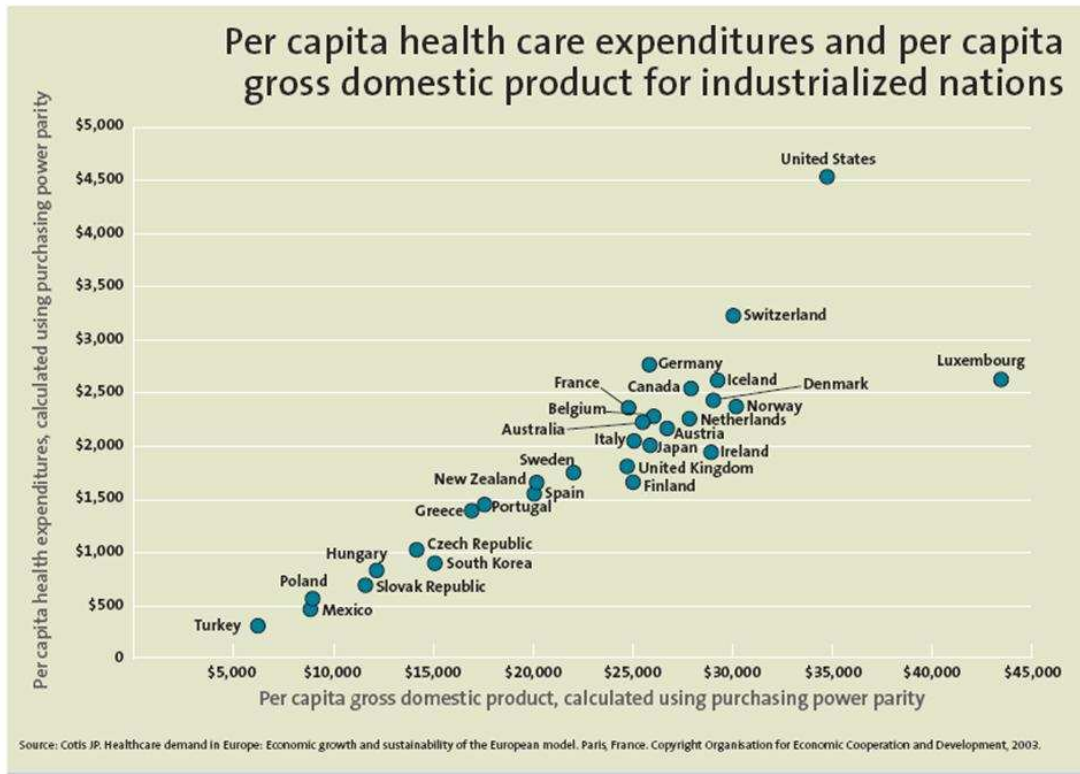
- Universal enrollment, and
- “Normalization” of the health insurance market.

## Relative Healthcare Costs:

### **How U.S. Industries and Workers Are Penalized Because of Healthcare Policy**

Figure 1 shows the relationship between per capita healthcare costs and per capita GDP for the thirty OECD member nations.<sup>5</sup>

Figure 1.



High U.S. healthcare costs threaten American industries and American jobs. Failure to reduce U.S. healthcare costs to levels comparable to other industrialized nations will only delay inevitable economic consequences.

Money spent inefficiently on medical services or health insurance cannot be spent on other productive industries. High corporate health insurance expenses drive outsourcing to foreign markets and threaten American jobs.

Thus the productivity of both individuals and corporations is hobbled. Workers with even minor pre-existing medical conditions cannot move to more productive opportunities for fear of losing health insurance.

The U.S. must lower healthcare costs to remain economically competitive in international markets.

### **Factors that Affect U.S. healthcare Costs:**

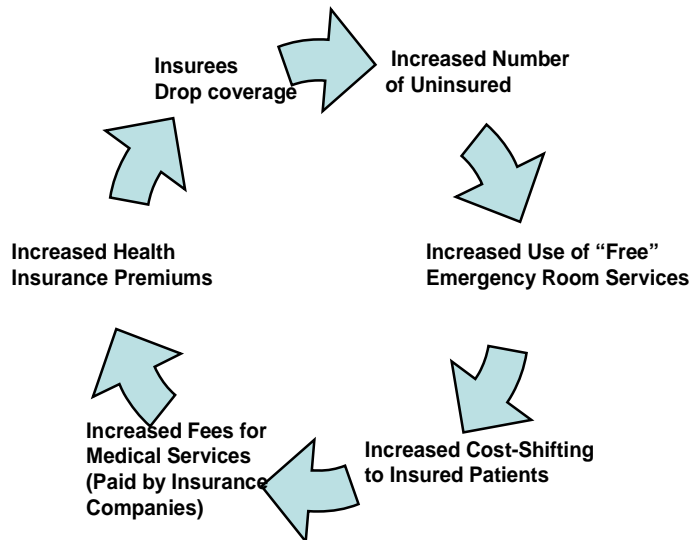
#### **The Un-Insurance Cycle**

Failure to achieve universal enrollment for healthcare drives up health insurance costs as well as costs for medical services. The following figure illustrates how a large

population of uninsured cyclically increases health insurance costs and increases the pool of uninsured.

Figure 2.

### **A Large Population of Un-insured Increases Health Insurance Premiums**



Emergency rooms are the most expensive source of medical services. When people without health insurance need medical services, the emergency room is often the only resource available. Hospitals are required by law to care for emergency patients. When uninsured patients cannot pay for these expensive services, the cost is shifted to the hospital patients who do have health insurance – “cost shifting.”

The result is that the fees for all medical services go up, insurance premiums rise, and some employers and individuals eventually drop health insurance coverage. This cycle continually increases the number of uninsured and further drives up the cost of premiums.

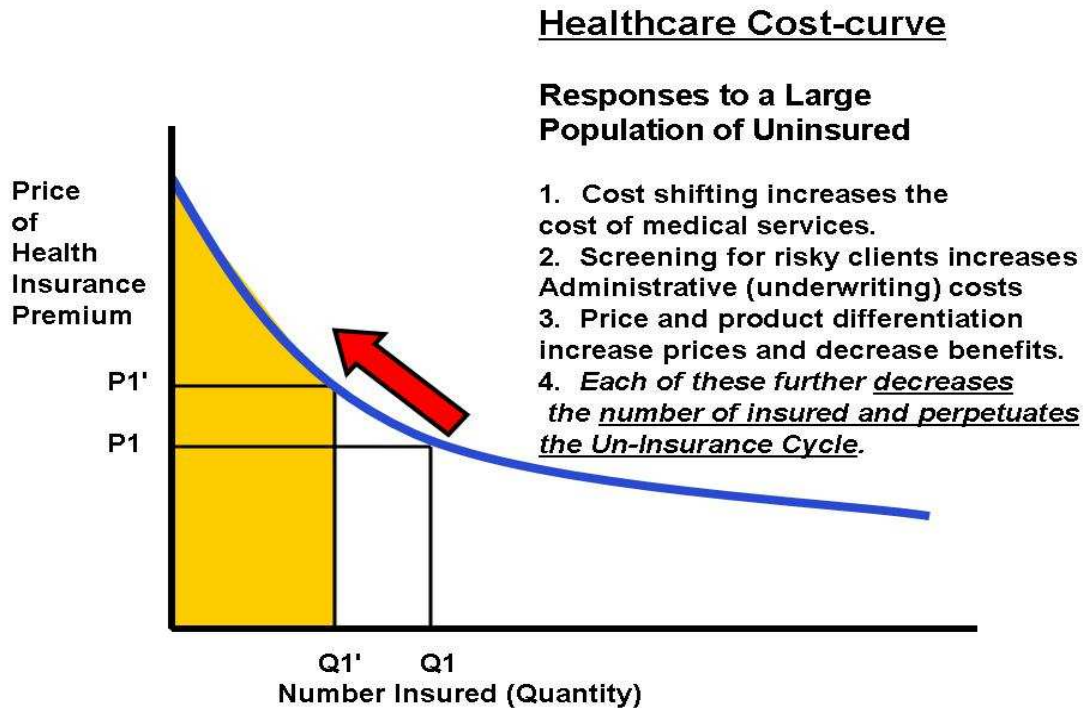
A policy of universal enrollment interrupts this cycle. Other member nations of the OECD do not have this cycle. Why? Because they already have universal enrollment.

If universal enrollment were implemented in the U.S., a direct benefit would fall to the population that already has health insurance. The insured population would no longer carry the inflated cost of caring for the uninsured in emergency rooms.

### **The Cost-Shift Penalty**

Figure 3 illustrates the relationship between the price of health insurance and increases in the number of uninsured.

Figure 3.



In an ideal world, there would be no uninsured. In that situation, the cost of health insurance would be at P1 and would cover the medical costs of the entire population, Q1. The total cost of medical care would be included in the rectangle defined by Q1 and P1.

Having a population without health insurance, however, changes the equilibrium state. As the number of uninsured increases, the number *with* health insurance shifts from Q1 toward Q1'. As more people become uninsured, fewer people are paying, but they are paying more. Fewer people still pay the same total cost of medical services. This is cost shifting.

Cost shifting drives up the cost of a health insurance premium. The total population does not change, but remains at Q1. The rate of illness in the population does not change and the total production of medical services changes very little, so the production curve moves very little. But with each pass through the Un-Insurance Cycle, an increasing number of uninsured people use the emergency room for so called “free” medical services.

Two things do change; 1) the number of people *with* insurance decreases (shifts from Q1 to Q1'), and 2) the price of a health insurance premium inevitably rises (from P1 to P1'). In Figure 3 the shaded area illustrates how revenues to accommodate cost shifting ultimately come from the insured population. For the insured population, the price of premiums is now higher than the cost of medical services received.

This increase in the price of health insurance premiums is comparable to a “tax” on health insurance. This hidden “tax”

- contributes to health insurance rates rising faster than inflation,
- is being paid only by people with health insurance,
- pays for “free” emergency room services for the uninsured,
- could be largely avoided with a National Policy of Universal Coverage.

Opponents of public funding for healthcare apparently prefer to pay this hidden “health insurance tax” rather than implement any form of “socialized” healthcare system. They oppose any healthcare system that gathers part of its revenues through other taxes. Thus the workers in America’s largest industries subsidize the emergency room care of America’s uninsured population.

But if other taxes did pay for public healthcare, the uninsured would be paying for at least part of their medical care, and the price of health insurance premiums could drop. The present system assures that insured workers will continue to pay for unpaid medical expenses through the Cost-Shift Penalty – a hidden “tax” on workers with health insurance.

*The first step to healthcare cost reduction is Universal Enrollment. Universal enrollment interrupts the Un-Insurance Cycle and reduces or eliminates the Cost-Shift Penalty.*

### **“Normalization” of the Health Insurance Market**

#### **Five Policies of Multi-payer Universal Enrollment Healthcare Systems**

It is important to remember that Universal Enrollment does not necessarily require full enrollment in a public healthcare system. Many nations have “hybrid” healthcare systems that provide for *both* a public healthcare plan and a private health insurance industry. Such systems are Multi-payer Universal Enrollment Healthcare Systems. These Multi-Payer Universal Healthcare Systems have proven to be more sustainable and typically provide better access than single payer systems.

Multi-Payer Universal Healthcare Systems (MUHS) have been around for decades. Many member nations of the Organization for Economic Cooperation and Development (OECD) already have this type of healthcare system. The hallmarks of MUHS are simple:

- Complementary roles for both public and private coverage, and
- Universal enrollment.

These combined public and private models with universal healthcare enrollment have proven capable of producing healthcare outcomes comparable to or better than the United States at an average per capita cost that is half the per capita cost of the United States model. (See Figure 1)

More than thirty per cent of people in over a third of member nations of the OECD receive primary coverage through private insurers.<sup>7</sup> Healthcare systems in the Netherlands, Japan, Switzerland, Germany, Australia and France all have complementary roles for both public coverage and private health insurance.

Although these systems were developed and matured independently, all these systems implement five policies that protect patients and define the role of private health insurance companies. C-MCGU is an acronym for the five policy instruments common to Multi-payer Universal. These policies are:

1. C- Choice between public and private coverage.
2. M- Mandatory universal enrollment
3. C- Community Ratings
4. G- Guaranteed issue
5. U- Uniform benefits

The policy instruments included in the acronym C-MCGU are typically considered “patient protection” policies. They do indeed protect patients who need medical services and healthcare coverage, but they do much more than this.

These policies also transform the health insurance market from a dysfunctional “failed” market to a “normal” market by building an environment of price-based competition. In some form or other, every successful multi-payer universal enrollment healthcare system addresses ALL these policies.

**C- Choice between public and private health coverage.** Having both a public not-for-profit plan and a private health insurance industry means the healthcare system as a whole retains the advantages of both. A public plan offers low administrative cost. A private health insurance industry supports innovation and new infrastructure in response to patient utilization patterns.

The key to cost containment is Choice - a choice that includes a publicly sponsored not-for-profit health insurance product with default enrollment. This is a matter of establishing a universal enrollment policy and allowing consumers to decide whether they will receive public or private coverage.

**M- Mandatory enrollment.** There are two ways to accomplish universal enrollment: Mandatory enrollment and Default enrollment. (The M in Mandatory enrollment fits the tidy acronym C-MCGU, but the real goal is Universal enrollment.) Several nationalized and single-payer systems accomplish universal enrollment with default enrollment policies. Others, the Multi-payer Universal Healthcare Systems, such as are found in the Netherlands, Germany, Australia and Switzerland, all have Mandatory enrollment policies.

All citizens not enrolled in the public coverage plan are required – by mandate – to enroll in private coverage plans and thus accomplish universal enrollment. Universal

enrollment accomplishes two goals: 1) it eliminates non-paying “free-riders” who use so called “free” emergency room services, and 2) universal enrollment substantially decreases the pressures (and administrative costs) placed on insurers by the phenomenon called “adverse selection.”

**C- Community ratings** assure that healthcare costs are distributed across the entire population. Every nationalized or single-payer system does this. Multi-payer universal enrollment healthcare systems implement this policy for both public and private plans. This does not only distribute the cost of medical care across the population; it also distributes the cost of medical services across a lifetime.

**G- Guaranteed issue** assures that those who most need medical services will have healthcare coverage. Nationalized and single payer systems guarantee enrollment. Multi-payer universal healthcare systems implement this policy for both public and private plans.

Without universal enrollment, guaranteed issue, and community rating, the specter of “adverse selection” will continue to dictate who is insurable and at what price.

**U- Uniformity of a minimum benefits package** accomplishes three goals: 1) a uniform Benefits package simplifies choices for insurers and clients alike, thereby facilitating knowledge of product and price; 2) it assures a fundamental level of care to everyone; and most importantly, 3) this policy "normalizes" the health insurance market.

Uniform benefits packages, when required of all insurers, prompts competition based on price and promotes efficiencies in management. When all insurers must offer the same minimum basic benefits package, the purchasers of health insurance may shop for insurance based on price. Price-based competition is a hallmark of competitive markets.

It cannot be over emphasized that ALL FIVE of these policy instruments must be addressed *together* in a successful Multi-payer Universal Healthcare System.

### **Reducing Healthcare Costs by Restoring a Competitive Health Insurance Market**

The essential characteristics of “normal” competitive markets are:

- Uniformity of product,
- Universal availability,
- Perfect knowledge of product and price,
- Easy entry to the marketplace,
- Price-based competition.

The above described five policy measures (C-MCGU) reinforce the essential characteristics of “normal” competitive markets. When these policies have been applied to health insurance, other nations have realized lower total healthcare costs. The

following table shows how corresponding policy instruments “normalize” health insurance markets.

Table 1.

Five Features of “Normal Markets”	Corresponding Policy Measure	Effects on Health Insurance Market
Uniform product	Uniform Minimum Benefits Package	Insurers compete on Price and Service
Universal availability	Guaranteed issue Mandatory enrollment	Availability assured; Reduced effects of Adverse Selection
Knowledge of product and price	Uniform Minimum Benefits Package	Uniform understandable “basic” policy
Competing providers	Assure a competitive number of insurers	Insurers compete on Price and Service;
Price-based competition	Community ratings Uniform Minimum Benefits Package	Insurance available at competitive prices

Under the above conditions, a universal enrollment policy tends to lower per capita healthcare costs.

Refer again to Figure 1. Nationalized and Single-payer healthcare systems are not the only systems that contain costs. Many nations with large health insurance industries also contain healthcare costs when these policy instruments are implemented.<sup>4</sup>

*The second step to healthcare cost reduction is “normalization” of the health insurance market.*

**Conclusion:**

TheCenter for Healthcare Policy Research and Analysis favors the Multi-payer Universal Healthcare System. Throughout the world these systems contain cost, provide healthcare outcomes as good as or better than the United States, and provide universal enrollment without waiting times. The policies that make these systems successful are adaptable to the circumstances of the U.S.

TheCenter for Health Care Policy Research and Analysis recommends the United States adopt a National Healthcare Policy with a Multi-payer Universal Enrollment Healthcare System.

Universal enrollment will interrupt the Un-Insurance Cycle and reduce the hidden “tax” in the Cost-Shift Penalty.

“Normalization” of the health insurance market will lower health insurance costs as well as protect patients’ access to healthcare coverage.

By addressing fundamental policies that reduce cost the United States can finally address the issues of saving lives and improving health.

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