How much in the way of kudos does President Bush deserve over his latest health care proposal? Some have decried the quick negative response of the democrats to the president's proposal. Is the criticism fair?

The president's proposal would replace the current open-ended tax exemption for employer-sponsored health insurance with a flat standard deduction for buying at least catastrophic coverage through an employer or a private individual policy.

Economists dislike the current tax subsidy, which increases with higher employer contributions and is greatest for those with the highest incomes. It's a subsidy for the purchase of overly generous insurance plans that encourage the overuse of medical services, driving up spending. And it mainly goes toward the purchase of coverage for those who are most likely to buy it no matter what—high-income people—while giving little help to those who need it the most, people with low incomes.

The president's proposal would set annual limits for the level of spending subsidized, which is good. But this new proposal does nothing to address the second complaint—that the subsidy is upside down to begin with.

So should we give the president half credit? No. The first problem has waned over time relative to the second. When economists first recognized the perverse incentives associated with excluding employer premiums from taxation, most health insurance was based on fee-for-service, and premiums were not nearly as high (even adjusted for inflation).

With annual premium growth far outpacing earnings and inflation, workers and employers no longer seek such generous coverage; they trim benefits and increase cost-sharing to keep premiums affordable. Meanwhile, the number of uninsured Americans climbs, and most among their ranks would receive little to nothing from the president's proposal.

The president's proposal would also end the difference between the tax treatment that employer-based insurance gets compared with individually purchased coverage. Economists love leveling the playing field, but in the case of health insurance, removing this advantage over policies individuals purchase on the open market will prompt some employers to stop offering insurance.

Young and healthy workers may save money by buying insurance on their own, and that market would be happy to serve them. But in most states, the insurers will pull up the welcome mat for older and less healthy workers. For these more vulnerable workers, the options aren't pretty: insurance could be impossible to come by at any price in most states, premiums could be substantially higher, or care for an individual's particular health conditions could be excluded from coverage. Nothing in the president's proposal guarantees that these currently insured individuals would have affordable, accessible, and adequate insurance post-reform.

The president's approaches to reform have consistently emphasized moving individuals into coverage with higher deductibles and lower benefits—intending to rein in systemwide spending by making individuals feel the financial bite when using services. If premiums go down because people use less care, the thinking goes, more people can afford coverage and the number of uninsured will fall. But this ignores a key fact at the heart of why our system is so costly.

Most health care spending is on a small percentage of individuals with very high medical costs. That means to dramatically cut costs, we'd have to reduce spending in the range well above even the higher deductibles the president would like to see. These costs are attributable to people with chronic and other serious conditions and are largely driven by the use of advanced medical technologies. The president's assumption that overly insured individuals are the problem behind premium growth and the number of uninsured is just plain wrong.

One component of the president's plan holds some promise, however. It would allow states to redirect government funds currently going to hospitals and use them to expand coverage for the poor, if states act. These provisions could help shore up the availability of care for low-income people, particularly if combined...
with a progressive tax credit instead of the proposed standard deduction.

Without a tax credit, however, the federal funds available to states are not sufficient to meet their needs. Even then, the availability of what is being offered is completely dependent on states’ ability and willingness to enact serious reforms. In states that do not, this plan offers little to those who need it most—those with the greatest medical needs and the low-income.

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