



## Why McCain has the best health-care plan

**His is the only one of the candidate proposals that has a chance of getting medical costs under control. An argument for some free-market sanity.**

By Shawn Tully, editor-at-large  
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**Fellow Americans, choose your revolution.** One way or another, we're getting a new health-care system. The old one is obviously broken. The U.S. now has 47 million uninsured, and costs are out of control. The Department of Health and Human Services predicts that if things continue as they are, health spending will almost double by 2017 to \$4.3 trillion, or one-fifth of GDP, vs. 16% today.

The crisis has gotten so severe that fixing the system is no longer a partisan issue. Everyone understands that something has to change, and fast. In this presidential race, both sides are proposing radical fixes that would totally transform the way health care is delivered and paid for in America. Both the Democrats and the Republicans embrace the same goals: John McCain, Barack Obama, and Hillary Clinton are all putting forth ways of making health care affordable for every American and stopping a disastrous escalation in costs. Both sides also envision a world where employers play a much smaller role in medical benefits. The differences, of course, are in the way each candidate intends to reach those laudable goals. In essence, McCain wants to create a kind of national insurance market that shoves more decision-making power into the hands of consumers; the Democrats are aiming for a Medicare-like federal superprogram. (We'll stick with the "Democrat" label in this story. The nominee status was still unclear at press time, and, intraparty sniping notwithstanding, the Clinton and Obama plans are extremely similar.)

So far, the press and public haven't paid much attention to the implications of these dueling visions. This stuff is complicated, and the most revolutionary provisions are buried deep in jargon-filled position papers. But parsing the plans is worth the work: This issue is crucial to America's economic future, and the differences between McCain and the Democrats are profound.

Who has the best plan? Both have huge flaws, but on balance McCain's is better.

McCain's main pillar is the elimination of a tax break that employees receive if their employer provides their health care. That may not sound like a shocker, but it is. The exclusion dates from World War II, when the federal government imposed controls on wages, but allowed companies to compete for workers by offering tax-free health benefits in lieu of pay. The law is largely responsible for the nightmarish patchwork of corporate-provided medical plans we enjoy so much today. Employees and their unions demanded richer and richer packages,

and employers complied, since they could buy far more benefits for their employees than workers could buy with after-tax dollars on their own. Americans have paid a steep price, however, by sacrificing their raises as corporate insurance bills exploded, never more so than now.

McCain suggests that we junk all that. Say you're earning \$100,000 a year and your company provides about \$9,000 toward your \$12,000 family premium, which is about average. Today you're taxed only on the \$100,000. Under McCain's plan, you'd also pay on the \$9,000. That could mean an extra \$3,000 or so in federal taxes alone. To compensate for the extra levy, McCain would provide a \$2,500 federal tax rebate for individuals and \$5,000 per family, meaning a family would simply subtract \$5,000 from its tax bill, the equivalent of a big cash payment.

Here's where it gets interesting. Employers would no longer be able to buy more health care with \$9,000 of their employees' money than the workers could buy on their own. The *raison d'être* for corporate health benefits would vanish. Employers have another compelling reason to pass the ball to the employee: While wages are rising around 3% a year, their health-care costs are growing at three times that rate. "I predict that most companies would stop paying for health care in three to four years," says Robert Laszewski, a consultant who works with corporate benefits managers. Hence, an employer that pays \$9,000 for your benefits would simply pack an extra \$9,000 a year into your paycheck. (Why? Because in a competitive labor market, companies would have to hand over that cash to employees or risk losing them.) So you'd have \$6,000 after tax, plus the \$5,000 family credit, to buy insurance. That's \$11,000 in new cash that employees can set aside for health care.

So what types of policies would they buy? Employees (and their families) with corporate plans - about 150 million Americans - would probably rush toward high-deductible, low-premium insurance, and use what's left over to pay cash for routine procedures. They would couple those high-deductible policies with Health Savings Accounts, which allow families to put away up to \$5,800 a year, before taxes, for medical expenses. Those plans cost about \$10,000. That's not a huge saving from the typical \$12,000 corporate plan, but it's a start. More than four million Americans already have HSAs, and the McCain plan would make portable, high-deductible plans the product of choice for a new generation of healthcare consumers.

Besides eliminating the employer exclusion, McCain's plan boasts another nice feature. It would allow consumers to choose an insurance plan that suits their stage of life. If you're young and healthy, for example, you probably want the cheapest plan you can get. If you're 45 and have four dependents, maybe you want something a bit more expensive and generous. Nine states, including New York, California, and Texas already require that as many as 50 benefits be covered, a list that ranges from *in vitro* fertilization to mental health services to prescription drugs. These requirements increase the cost of insurance; they're a major reason young people have dropped their coverage. Under the McCain plan, insurers in any state would be free to offer the plans with a vast variety of deductibles, co-pays and benefits. UnitedHealthcare and Blue Cross/Blue Shield plans already provide a menu of packages tailored to groups as varied as Gen Xers and retirees.

The problem with McCain's approach - and it is a huge problem - is that McCain ventures so far toward total laissez-faire liberty that he risks leaving the poor and sick behind. Here's why. Perhaps his most drastic proposal is allowing the same insurance products to be sold across state lines. That seems to make sense, and maybe it does: Look what interstate banking has done for pricing and choice in financial services. But in health care, the upheaval would be so brutal that it scares even the most ardent free-marketer. Many states have some form of what policy wonks call "community rating." Under pure community rating, insurers must charge all customers the same premium no matter whether they're 20 or 55, or whether they have cancer or are models of good health. McCain is targeting community rating for good reason. It forces the young and healthy to pay far more than their actual cost by making them subsidize the elderly and sick. Like the mandated benefits, it's pushed millions of Americans in their 20s to drop their health insurance.

But under the McCain plan, states with no restrictions - Pennsylvania, for example - could sell policies for 25-year-olds that cost around \$1,200 a year, one-third the price in New York. Young New Yorkers would drop their plans in favor of Pennsylvania providers, forcing New York insurers to jack up premiums for people in their 50s or early 60s, who need those rich, community-rated plans that cover as many procedures as possible - but who no longer benefit from the excessive premiums paid by the youngsters. It gets worse. Anyone with cancer, diabetes, or other pre-existing conditions will see their premiums multiply too.

To his credit, McCain does have a plan for relatively young, low-income Americans who can't afford insurance. "We would increase the tax credit according to income so that poor families could buy insurance," says Douglas Holtz-Eakin, McCain's policy director. But McCain sorely lacks a plan for people in their 50s without corporate benefits, and Americans with pre-existing conditions, who would be brutally stripped of coverage if insurance crosses state lines. "For his plan to work, McCain has to tell us how he would deal with the old and sick," says Jon Gruber, an MIT economist. "If McCain doesn't tax the healthy to pay for pre-existing conditions, as happens under community rating, he has to tax the taxpayer. That means his plan will require huge subsidies he's not talking about."

**Now for the Democrats.** The core of their plan is a "pay or play" option for employers. Large companies would have the choice of either providing benefits for workers or dropping their coverage. If they chose the latter, they would pay a mandatory payroll tax to support a new government-administered system. That system would have two parts: a Medicare-like public program, and a menu of private options similar to the generous plans available to U.S. government employees today. Workers who are self-employed or lack insurance would go straight into one of these two options. Low-income Americans would receive federal subsidies to purchase the premiums.

In practice, the system would quickly swell the ranks of Americans with government-paid health care. Remember, health-care costs are rising far faster than wages, so companies have a strong incentive to pay the tax and erase that rapidly growing burden from the books. It's also likely that the government plan will offer better benefits than many, or perhaps most, corporate plans. In fact, the Democrats call for rich standard benefits packages based on the plan offered to federal employees. Those packages would have deductibles of just \$300 and offer prescription drugs, mental health benefits, and "spinal manipulations" (i.e., chiropractic

services), among a cornucopia of other benefits. As a result, the federal plan, potentially packed with new benefits pushed for by lobbyists for various medical specialties, will quickly cause an exodus from employer plans.

The standard benefits package isn't just a bad idea because it will substantially raise the cost to taxpayers. It will also make it virtually impossible for Americans to buy insurance tailored to their needs. Suppose you're one of those 25-year-olds. You probably don't want to spring for a full-blown plan that covers old-age diseases like Alzheimer's and would rather save some money and go with a low-premium, high-deductible plan. But the Democrat approach requires that any competing plans be "actuarially equivalent" (Clinton's term) to the federal employee plan - which translates as a generous minimum standard for health insurance. "With that mandate, you rule out high-deductible plans," says Gruber. "It would make it very difficult to design one that would qualify."

The Democrat proposals have some additional drawbacks. First, the Dems want to heavily regulate the insurance industry by limiting everything from profits to marketing expenses. If the earning power of insurers is determined by federal regulators, their pricing will be too, and thus they will evolve into the equivalent of public utilities. Would you rather have medical prices set by fiat or by nationwide market competition?

Second, the Democrat plan exacerbates the fundamental problem in the American health-care system, which is that no one has any incentive to care about price. (How much is that MRI center charging for your ankle scan? Who cares? Just hand over the \$50 co-pay and never you mind.) Creating a huge new medical superstructure would shift far more spending to third-party providers, chiefly the federal government, giving consumers even less incentive to concern themselves with the price of an MRI - or any other service, from an elective wart-removal procedure to a life-saving heart bypass. "The Clinton and Obama plans would enormously increase total health-care spending, but disguise the extra costs by shifting them to taxpayers," says John Sheils of the Lewin Group, a research firm that does statistical modeling for health-care plans.

Despite all that, the Democrats' plan probably beats McCain's if you're scoring on political viability. Their program doesn't involve anything that smacks of a cut in benefits, and it's just easier to win with largesse.

But on economic merits, McCain wins. For all its problems, at least it puts the consumer in charge. Would that create a world where we're forced to dicker with heart surgeons? No. It will create a world where health care is treated as the precious resource that it is, rather than a costless entitlement; where nationwide competition pushes down the price of catastrophic care and consumers focus their attention and budgets on what's really crucial to their health. That's an important first step. The price of health care is never going to get under control until patients get what they deserve: the right to be customers too.

*Christopher Tkaczyk contributed to this article.*