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TO: Interested Parties

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RE: The Hybrid: A Public Plan Alternative for Harry and Louise

Whether health care reform should include a "public plan" is an issue that now threatens to fracture the emerging consensus on health reform. If left unresolved, the debate over a public plan could derail the broader reform agenda while other pressing issues central to reform are put on hold.

The proponents of a public plan seek the right goals—to broaden access and lower costs. But there is a very real danger that an overly intrusive public plan can ultimately undermine these very goals and destabilize the private-sector coverage that middle-class Americans—i.e., Harry and Louise—depend on and are largely satisfied with.

In addition, reformers have already won key concessions from the health care industry. A public plan was meant to ensure, for example, that Americans could no longer be denied health coverage or have premiums increased because of a pre-existing condition. The insurance industry has now agreed to those reforms. A public plan was meant to drive costs down. The health care industry and stakeholders have pledged to reduce spending by $2 trillion over the next ten years.

But while a heavy hand from government might be destructive, the invisible hand of the market is also not enough. There's no question that the health insurance market needs reform and that for too many middle-class Americans, health care coverage is too unstable. Only 64% of working-age citizens enjoy the "gold standard" of continuous, private-sector coverage, while the remainder has experienced gaps in coverage or relied on government coverage in whole or in part.[1]

This memo describes a hybrid plan that combines the strength of the public and private sectors and that can appeal to both a wide range of progressive policymakers and the middle class. This plan has four elements:

- An explicit rejection of price controls and rate-setting on medical services and products;
- A level playing field that preserves and enhances a vibrant and robust private insurance industry with market-based competition;
- An assurance of stable coverage for the middle class, meaning that reform will not force people to change plans; and
- Mechanisms to ensure private-sector cost-containment, in conjunction with the health care industry's pledge to achieve the $2 trillion in savings over ten years .

What the Hybrid Plan Can Do

Like a hybrid car, the hybrid plan would have two sources of power: the public and private sectors. Its goal would be to energize and enhance market competition, not replace it. And it would aim to raise the bar in improving health insurance for average Americans, including by strengthening the stability of the private sector insurance market that most Americans rely on. As a health insurance plan whose shareholders are the American public, the hybrid would be intended to serve the public's interest. But it would also use the power of competition in the private sector to shape and prove its value to those Americans who wish to choose it.

We see three potential functions for the hybrid plan:

(1) Lead by example in payment reforms and pro-consumer business practices, thereby creating incentives for the insurance industry to modernize certain practices without using the blunt instrument of regulation.

(2) Enhance coverage stability for the middle class by providing a back-stop option if private coverage is unavailable.

(3) Help serve to encourage industry efforts to contain costs.

At the same time, the hybrid should remain limited in scope. After all, it's an experiment. It has no precedent in the current health care system, and it is critical that it not undermine a key promise of reform that people will be able to keep their own insurance. It is not a gateway toward a single-payer system, which is by definition highly disruptive. Nor should it drive up the cost of private insurance for Harry and Louise by shifting the cost of health care to the private sector.

Four Elements of a Hybrid Plan

1. An explicit rejection of price controls and rate-setting

First and foremost, the hybrid firmly and explicitly rejects Medicare-style price controls and rate-setting that would require doctors and hospitals participating in the public plan to accept Medicare's below-market prices. Instead, the hybrid plan would negotiate rates with hospitals, doctors, and other suppliers just like private insurers currently do in the health care marketplace.

Substantively, a firm and public rejection of price controls and rate-setting could be pivotal to the success of health care reform more generally. In fact, health care has advanced as far as it has today compared to1994 in part because progressives have not generally been espousing price controls as the key to controlling costs. Employers fear that price controls would shift costs to them. Providers would have concerns of their own. Insurance companies believe price controls will eliminate the role of competition and choice in health care. And because of their heavy-handedness and rigidity, price controls also eliminate the public plan's incentives to innovate and lead with best practices.

Politically, such a move would also enable policymakers to present the plan for

government involvement in the marketplace in a new and more appealing light. The threat of price controls is at the heart of the conservative critique—now getting louder—on a "government takeover" of health care and the "rationing" of medical care. By taking price controls off the table, progressives can effectively defang this attack while also demonstrating that a government-sponsored plan without price controls and rate-setting *is* possible.

2. A level playing field

The marketplace should welcome competition, not fear it. But at the same time, the competition should be fair. Private plans should not be required to compete with one hand tied behind their back. In order to help lead market reform, the hybrid plan should be wholly part of the market and subject to its rules, rather than being given special treatment or allowed to use its government mandate to rig the market in its favor.

Several measures, including some outlined by Senator Schumer, can help ensure a level playing field. Critical pieces should include:

- Preventing the government from using provider participation in Medicare or other public programs as a stick to compel them to participate in the public plan.
- Separating the administration of the plan from the regulation of the insurance market.
- Requiring that the plan follow the same insurance regulations and benefit requirements as private plans.
- Requiring the plan to establish a reserve fund in the same way that private plans are required to do so now.
- Requiring the plan to be self-financed.
- Providing the same health care insurance subsidies to people who enroll in a public or private health plan.

Other mandatory features should include:

- Limiting the hybrid plan to certain market segments – those employed in small businesses with 10 employees or less, those in the individual market, and those who lack insurance. Another option might to limit the geographic scope of the plan in its initial phases until its worth is demonstrated.
- Making any federal bailout of the hybrid in the event of a bankruptcy or shortfall subject to procedural hurdles such as a supermajority vote requirement in Congress (in addition to the self-financing requirement).
- Allow the hybrid to be privately administered in the same way that Medicare is now administered by contract through private insurance companies.

- Require the hybrid to follow private plan standards for a complete network of providers, marketing rules, and patient appeals of claim denials.
- Subjecting the plan to the same state premium taxes that private insurers pay.

And to address concerns that the hybrid will need to rely on existing Medicare provider rules to get itself off the ground, the plan could instead receive a small amount of start-up capital that it would have to repay.

Key Policy Proposals

- Explicit rejection of price controls and rate-setting
- A level playing field on taxes, regulations and administration
- Limited participation to certain market segments (e.g. small group and individual)
- Required supermajority approval for federal bailout of the public plan (in addition to self-financing)
- Automatic sunset after four years unless the plan can demonstrate solid financial performance and positive impacts on market stability
- Mandatory accreditation or evaluation of providers, plans and other stakeholders to ensure private sector cost containment if targets are not met

3. Stability for Americans in their current coverage

A third element of the hybrid is an assurance to the middle class that their current coverage will remain stable. Harry and Louise must feel confident in knowing not just that their employers won't be dropping their existing coverage in favor of the public plan but that the goal of the public plan is to help stabilize the private market for the middle class.

The way to do this would be to subject the plan to a "reverse trigger," i.e. an *automatic sunset* after four years unless two requirements are met: (1) a rigorous review by an independent commission (similar to what Congress has done in the past for base closings) determines that the plan is on solid financial footing and has had a positive impact on the private insurance market; *and* (2) Congress proactively reauthorizes the plan. If both requirements are not met, the public plan would be privatized so that none of its enrollees would lose their coverage.

As we've noted before, the hybrid plan should be an experiment, and this approach ensures that the burden of proof rests on the plan to prove that it can have a

positive impact on the marketplace and on the quality of Americans' coverage.

4. Cost-containment measures

The final element of the hybrid approach is to encourage the health care industry's unprecedented efforts to collectively restrain costs. This involves extending the hybrid strategy beyond the hybrid itself and into the whole market for health care.

In exchange for a hybrid plan that eschews price controls, industry should be encouraged to deliver on their pledge to reduce the annual growth rate in health care costs by 1.5 percentage points. The 28-page letter from the leaders of the health care industry released on June 1, 2009 offers a variety of solid proposals that demonstrate how a bold combination of public cooperation and private competition can reduce medical inflation.

While no industry sector should be held accountable for the failings of other sectors, each player should be held accountable for its share of the commitment to reducing costs. One potential mechanism for doing so might be a requirement that all health insurance plans and providers to be rated –i.e. "accredited"—for quality and cost if the industry's savings targets are not met.[2]

These cost and quality ratings could then in turn be used to sort out high-quality, low-cost plans and providers from poor performers.[3] For example, these scores could become part of the criteria for plans that want to participate in any health insurance exchanges that are created as a part of reform. Alternatively, subsidies could be linked to performance. Finally, health plans would be allowed to exclude low-scoring providers from their networks (even if state laws currently provide otherwise).

Because this approach is based on competition, not price controls, to bring down costs, it could prove to be much more palatable to stakeholders than the threat of a public plan modeled on Medicare. (The hybrid plan would, of course, also be subject to the accreditation requirement in order to ensure a level playing field.)

Conclusion

In a June 2 letter to Senators Baucus and Kennedy, President Obama drew a line in the sand in support of a "public plan." As his letter stated, "I strongly believe that Americans should have the choice of a public health insurance option operating alongside private plans. This will give them a better range of choices, make the health care market more competitive, and keep insurance companies honest."

The framework we offer here should govern any and all variations on a government plan that are included in the final reform package, regardless of whether Congress chooses a fallback structure or a side-by-side structure. A price-controlled plan—even as a fallback—has the potential to defeat the broader purposes of reform by eroding choice and competition.

On the other hand, a well-crafted hybrid option—whether as a fallback or as a side-by-side—can help to further the goals of reform in broadening access, lowering costs and strengthening the stability of coverage for middle class Americans who expect and rely on private-sector insurance.

Progressives who believe in both the power of markets and of government to work together in bettering the lives of the middle-class should embrace the notion of a hybrid plan that can energize and enhance the current market.

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[1] Anne Kim, Stephen J. Rose and David B. Kendall, *Checking Up on Harry and Louise: The Health Care Coverage Experiences of the Middle Class*, May 2009, available at http://www.thirdway.org/products/209

[2] Health plans, for example, could be required to be evaluated and rated for cost and quality by the National Committee for Quality Assurance (NCQA), which currently offers a widely-respected voluntary accreditation program for health plans. Accreditation could also be asked of providers, who would be required to participate in an accreditation process and report their scores for both quality and efficiency.

[3] At the state level, mandatory accreditation has proven to be highly effective. In Wisconsin, for example, the state has cut costs for state employees in the Madison region by 30 percent below the highest cost regions in the state.3 The state defines three tiers of plans based on price and quality and pegs the base reimbursement for all health plans at the level of the tier 1 plans, which have the highest quality and lowest price. State employees can choose lower quality plans from the other two tiers, but they must pay for part of the higher price.