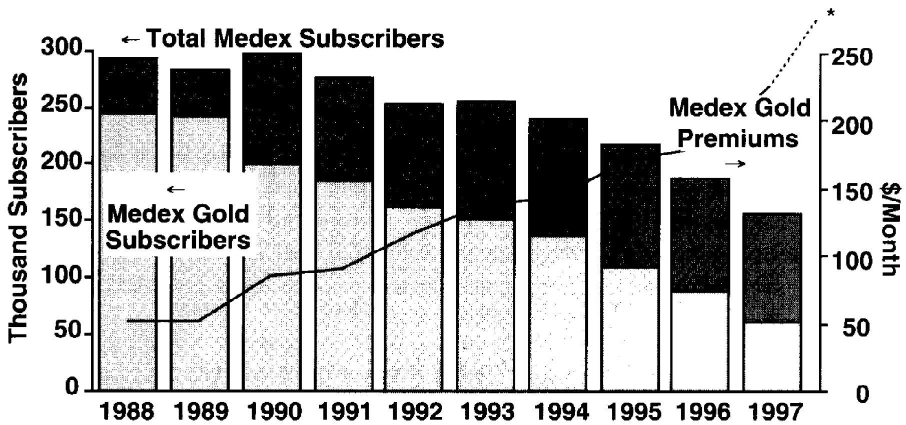
The Death Spiral: suscribers and premiums for medigap insurance

Medex medigap insurance for the elderly, Blue Cross Blue/Shield of Massachusetts



Source: Boston Globe, 20 January 1998, A1.

* proposed rate for 1998 of $278/month

Medex Gold covers unlimited prescription drugs with a small copayment. Other Medex plans limit total benefits.
From *Business Dynamics, Systems Thinking and Modeling for a Complex World*, 2000, p.177

Health Care Dynamics

http://www.exponentialimprovement.com/cms/HealthCareDyn.shtml

The death spiral of our current, fundamentally free-market-based, health care system is due to our focus on the individual, rather than the whole. Here are the reasons.

Adverse selection: Healthy people take the risk that they can do without insurance, leaving the less healthy in the system. Premiums rise and again the most healthy, as well as many who just can't afford it, drop out. The rising premiums and increasing dropouts of the healthiest is a reinforcing feedback that causes a death spiral.

Adverse selection causes havoc in a market economy because of asymmetric information, in this case because the buyers know their health situation better than the sellers. The understanding of this phenomenon is so important that those who developed it were awarded the Nobel Prize in 2001.

Unfortunately an awareness of its impacts has not sufficiently worked its way into the political realm. It explains why an insurance-based prescription drug proposal would fail. People who know they don't have as much need for prescription drugs will drop out ... and the death spiral begins.

Health Care Dynamics (cont'd)

Though adverse selection is the fundamental driver of system failure, other effects accelerate it.

Dropouts get sick: Some take a risk, betting they won't get sick, and don't get insured. Others simply can't afford it. Some lose the bet and get sick. The logical outcome in a pure free market system would be to just let them sicken and die. Thankfully, for the most part, our society is unwilling to do so. They often get some kind of government-funded care with many going to emergency rooms for treatment. The costs, some excessive, are passed on to the public in higher taxes, and to businesses in higher premiums, as much as 15 percent higher.* The higher taxes and higher premiums to businesses cause even more people to drop, or be dropped from, coverage. This reinforces the death spiral.

Loss of positive externalities: We don't take advantage of them. For example, when you spend money on your heath care, it benefits me. First, because I'm less likely to get sick, and, second, because if we work together, I'm going to be more efficient when you're in good health. Therefore, the result is higher premiums, and less income to pay them, when everyone isn't covered.

Short-term orientation: Even though it's a lot more efficient to prevent health problems than it is to treat them once people get sick, all companies, including HMOs, find it difficult to spend now for lower costs in the future. It's much faster and easier to deny care, to save now by not spending on prevention. People denied care often sue, which drives up costs. And, according to a 1999 Institute of Medicine report, "To err is human," two studies show that between 44,000 and 98,000 hospitalized Americans die each year due to medical mistakes. This costs lives and also results in lawsuits. So instead of driving costs down by prevention and providing adequate care, our system now drives them up due to the higher costs of treating people after they get sick and legal expenses.

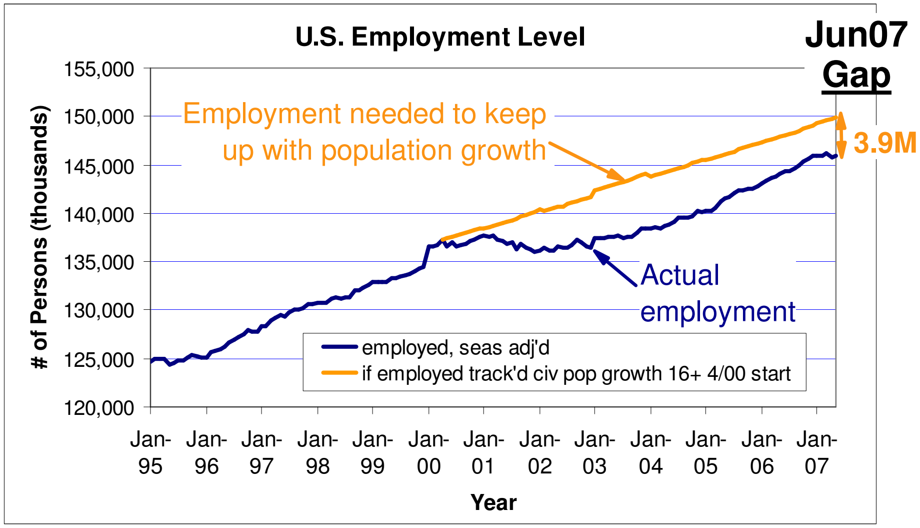
Unfortunately, there's a current push to cover up the root causes of the legal problems by taking the determination of lawsuit awards away from juries, who hear all the evidence, and impose one-size-fits-all caps on awards.

In summary, adverse selection, costs being passed on to the public in taxes and to businesses in higher premiums, not taking advantage of positive externalities of health care, a lack of emphasis on prevention, denying coverage, and medical mistakes are causing the death spiral of our health care system.

The market is a powerful mechanism and it works well to solve many, many problems. But **there are problems for which only collective, government-based solutions will suffice and for which individualistic, market-based solutions are doomed to fail.** Health care is just one example.

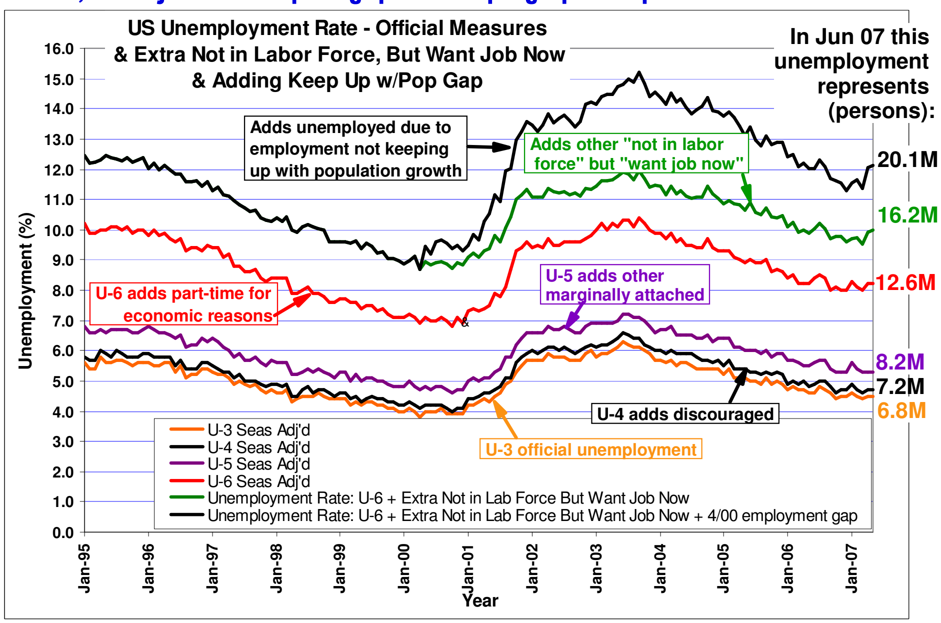
US Employment Level, Actual & Needed

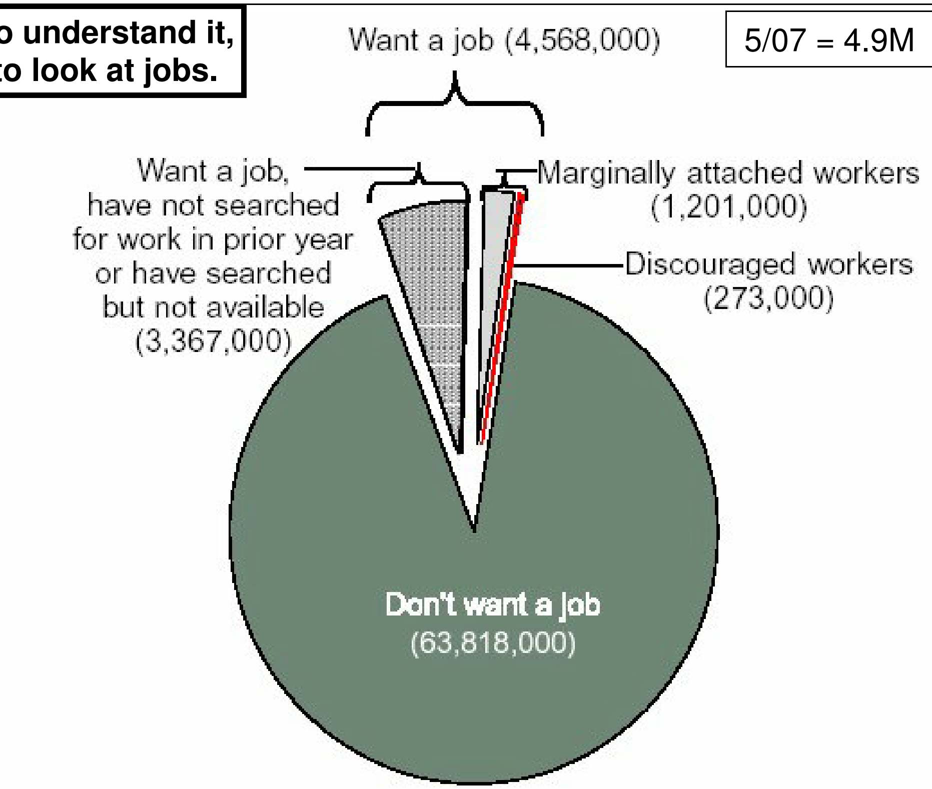
TABOR: To understand it, we have to look at jobs.



Employment has not kept up with population growth.

US Unemployment - Official Measures + Considered "Not in labor force, want job now" + plus gap not keeping up w/Pop Growth





SOURCE: Bureau of Labor Statistics, Current Population Survey

Persons considered not in the labor force, with 1999 annual averages

An Orwellian Category: "Not in labor force, Persons who currently want a job"

Marginally attached workers are persons who currently are neither working nor looking for work but indicate that they want and are available for a job and have looked for work sometime in the recent past.

Discouraged workers, a subset of the marginally attached, have given a job-market related reason for not currently looking for a job.

Other Want a job: Want a job have not searched for work in prior year or have searched but not available

Persons employed part time for economic reasons are those who want and are available for full-time work but have had to settle for a part-time schedule.

Note: None of this considers the Underemployed. True Slack: 20 - 30%

Why is real unemployment at 12%? Answer: Federal Reserve policy.

The Federal Reserve only allows so many jobs to be created and promotes worker insecurity to hold down inflation. Don't believe it?

Testimony of Chairman Alan Greenspan, February 26, 1997

> ... although I do not doubt that all these factors [I have reviewed] are relevant, I would be surprised if they were nearly as important as job insecurity. ... **restraint on compensation** increases has been evident for a few years now and **appears to be mainly the consequence of greater worker insecurity**.
>
> ... **suppressed wage cost growth as a consequence of job insecurity can be carried only so far**. At some point, **the tradeoff of subdued wage growth for job security has to come to an end. ...**
>
> ... The Bureau of Labor Statistics reports that people were somewhat more willing to quit their jobs to seek other employment in January than previously.
>
> ... Given the lags with which monetary policy affects the economy, however, we cannot rule out a situation in which a **preemptive policy tightening may become appropriate before any sign of actual higher inflation becomes evident. ...**

The Fed depends on job insecurity to control inflation and frets it might end. It's difficult to be happy when insecure, so <u>this policy is not at all consistent with the recognition in the Declaration of Independence of a right to the "pursuit of Happiness."</u>

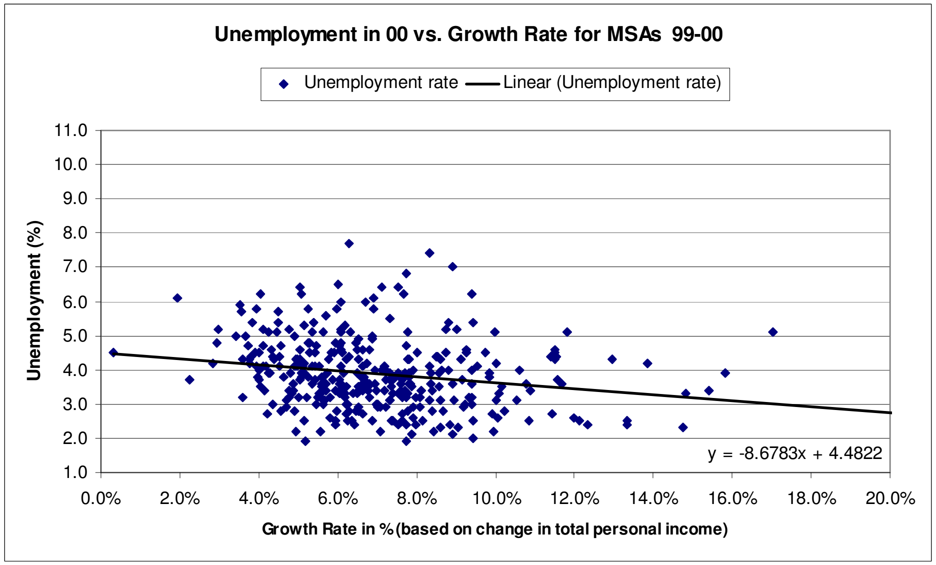
Testimony of Chairman Alan Greenspan, July 22, 1997

> ... the perceived quicker pace of application of our newer technologies ... has brought with it a heightened sense of job insecurity and, as a consequence, subdued wage gains. ... last February, **polls indicated** that despite the significant fall in the unemployment rate, **the proportion of workers in larger establishments fearful of being laid off rose from 25 percent in 1991 to 46 percent by 1996**. It should not have been ... unexpected that **the number of workers voluntarily leaving their jobs to seek other employment has not risen in this period of tight labor markets.**
>
> ... **at some point workers might no longer be willing to restrain wage gains for added security,** at which time accelerating unit labor costs could begin to press on profit margins and prices, **should monetary policy be too accommodative. ...**

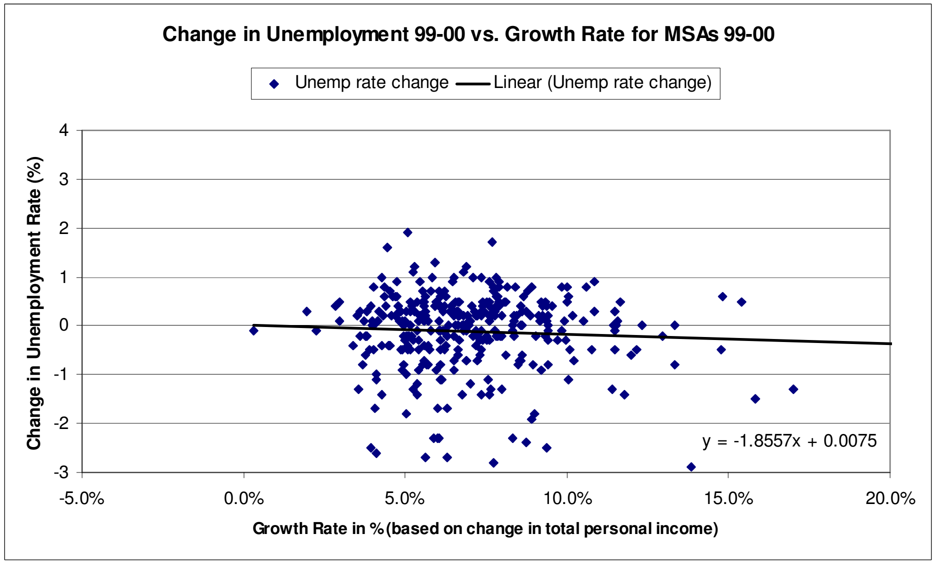
So if workers want a larger share of the economic pie, then the Fed pursues less "accommodative" monetary policy to slow the economy, increase unemployment, and increase worker insecurity. <u>Being so insecure that one is afraid to seek other employment is not consistent with the recognition in the Declaration of Independence of a right to Liberty</u>.

So what's going on? The Fed allows unemployment to only fall so low ... if it falls "too low," the Fed raises interest rates to "cool the economy." This means that, nationally, only so many jobs are allowed.

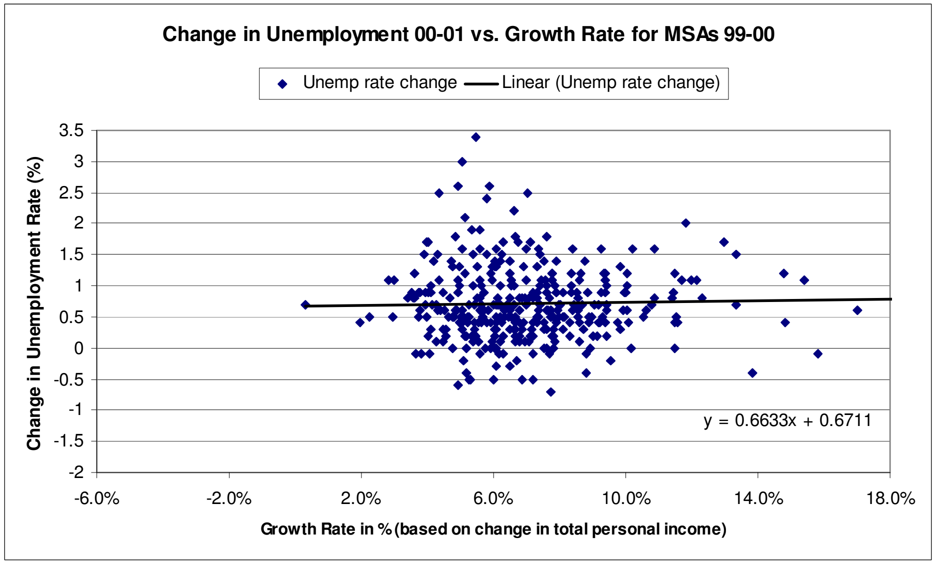
**Don't believe it? This graph shows:
a 10% faster growth appears to reduce unemployment by about 1%,
but a 10% faster growth in any region would be unsustainable.**



... and there is little, if any, *<u>change</u>* in unemployment in fast-growing areas



... and a reduction in unemployment doesn't show up a year later, either.



So what's this mean? Growth doesn't "create jobs," it only rearranges them. People leave slow-growing areas to go to fast-growing areas.

Because there aren't enough jobs, regions must compete for the jobs that are allowed. They compete with lower taxes and less regulation (more costs socialized onto the public). Years later, this leaves regions without enough tax dollars to pay for infrastructure.

Governments pass, or attempt to pass, the costs onto the public by increasing taxes. But the public rebels and passes laws like Gallagher and TABOR. Alas, the growth has already happened, so if you don't pay in taxes, you pay by getting stuck in traffic and hitting potholes. Bummer.

The Trouble with TABOR [Published, slightly edited, in The Denver Post as "In a hole? Stop digging" on 3/10/05]

Backers applaud TABOR: It cuts "wasteful government spending." Opponents assail TABOR: It limits "needed government services." But TABOR isn't the solution to, nor the cause of, our problems. Here's why.

Cities and counties approve new growth. While taxes and fees provide near term revenue for government services, they're insufficient to cover long term costs (roads, schools, prisons, etc.). But we don't feel the increased infrastructure load for years; it takes time to build and occupy new development.

Taxes may offset what government spends on infrastructure, but what's spent doesn't maintain levels of service. Examine any new development traffic report; you'll find the level of service is degraded even after developer “improvements.” As long term costs arise, governments raise property and sales taxes to pay for them. Because government does the raising of taxes, taxpayers are led to believe the problem is "wasteful government." Based on that belief, they've voted for laws like Gallagher and TABOR, instead of recognizing that insufficient taxes and fees on new development are responsible.

To increase revenue, growth proponents advocate more growth to "increase the tax base." Trouble is, that growth also doesn't cover long term costs; even more growth is "needed." This "doing what feels good in the short term, but is harmful over the long term" is called "addiction." This "addiction to growth" is very much like "addiction to drugs."

Infrastructure backlogs are a national problem. In September 2003, the American Society of Civil Engineers updated its "report card” on the nation’s infrastructure estimating a $1.6 trillion investment is required over the next five years. The rate of increase is 9.25%/year, many times inflation.

As infrastructure backlogs grows, eventually even growth industries support tax increases for roads to increase the area accessible for development. Note their support is for taxes on the general population, not for impact fees and taxes on the industries that primarily profit from growth (e.g., developers, home builders, banks, utilities, road builders, newspapers, etc.). In the literature on growth, these industries are called the "growth machine" because they're informally and naturally organized by shared profit motives.

It's not in the financial interest of growth industries to acknowledge this dynamic. Even those who really believe that "growth is good" find the dynamic difficult to recognize. Their belief is confirmed by the initial increase in revenue. When costs are displaced in time and space (e.g., Fountain Creek drainage erosion), they're easy to ignore.

So what to do?

When you find yourself in a hole, the first thing to do is stop digging. In this case, determine the rate at which short- and long-term infrastructure costs are accumulated and collect impact fees to offset the marginal (not average) costs of growth. Hear the screaming?

The second, increase property taxes to drain the overall backlog. More screaming! Though growth industries have primarily benefited, it's too late to recoup the subsidies.

The trouble with TABOR is that approving development with TABOR is like charging a credit card and then not paying the bill. It locks the barn door after the horse has been stolen. It's misguided public policy that contributes to the government dysfunction the "Doug Bruces" complain about.

Not paying the bill is somewhat justified. It's sent to the wrong people: all taxpayers rather than to growth industries. The costs of growth are externalized onto the public at large rather than paid by those who profit. Such negative externalities allow companies to privatize profits and socialize costs. Those who praise "the market" should know that internalizing the costs is important: unless market prices fully capture the costs, the market cannot correctly allocate resources or properly inform purchase decisions.

Economic conservatives decry redistributing income, no matter the social good; but they have no problem with redistributing costs, no matter the social harm. So let's not beat around the bush. Those who oppose impact fees and excise taxes on new development are as much socialists as those they batter with the "socialist" label. They're socialists on the cost side ... and hypocrites, too.