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Defined Contribution Health-Care Plans Benefit Consumers, Employers, Physicans and Insurance Companies

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Health care is heading for the “perfect storm.” The confluence of skyrocketing health-care costs and a slowing economy threatens to destroy the quality and accessibility of health care for all Texans.

Beginning in the mid-1960s, lavish health-care funding led to decades of unrestrained spending, followed by desperate but unsuccessful attempts to contain costs. While managed care temporarily tamed expenditures in the 1990s, doctors and patients paid the price with denials, delays and inconveniences that were sometimes medically, personally, politically and economically harmful.

By the late 1990s, negative press, contentious litigation, and restrictive legislation eroded the effectiveness of cost-containment strategies. The major cost-cutting tools (utilization review, provider fee concessions, incentives, and the like) are largely played out. The hefty profits that permitted premiums to stabilize in the mid-90s are gone. Costly new technologies are steadily emerging, and patients, insulated from their costs and sometimes backed by courts, continue to demand them. Health plans hike premiums regularly to maintain quality and remain solvent. As the economy remains sluggish, employers, particularly smaller firms, are pressed between the options of cutting back on benefits, increasing the employee share of costs or eliminating benefits entirely.

Health care is now at a crossroads. Everything points to higher costs. Easy cost cuts are long gone. This crossroads offers policy leaders the opportunity to resolve problems that have affected the state’s health-care systems for many years by reshaping how health care is financed and delivered.

Health care is now dominated by defined benefits plans. Under this traditional approach, an employer or institutional purchaser determines what range of services will be covered and then seeks or creates a plan that will provide those services for a set price.

Defined benefit plans are driven by employers, the insurance carrier and health-care provider, while patients play a walk-on role as recipients of others’ decisions. Defined benefit plans offer consumers no opportunity to decide about the types of care they ought to be permitted to have and are worth buying.

Defined contribution plans, in contrast, are consumer-driven, as well as cost-contained. In defined contribution plans, the employer determines up front how much it will spend for health care, provides an array of options from which beneficiaries can choose, and then defines its own contribution. Employees are free to choose a plan that is costlier than the employer’s contribution by paying out-of-pocket.

There are endless varieties of defined contribution plans. Some provide a Flexible Spending Account in which employees set aside their own pre-tax money to cover health-care expenses. In others, the employer fills a personal health account on which the employee can draw to purchase catastrophic insurance and, below that, to cover the daily costs of routine care. Many of these plans allow employees to use the funds to cobble together a health plan tailored to the individual's own needs. Some allow an individual to assemble his own provider panel, co-pay expectations and covered services. Monies unused during one year may be rolled over for use in future years in certain defined contribution plans.

For a consumer, defined contribution plans confer broad control of one's health care, allowing each person to decide which services are worth purchasing, at what price, from which provider and how to manage the money in his health care account to promote prudent purchasing of the health care he values. Assuming that the dedicated health account is sufficient to cover most routine expenses, plus purchase a catastrophic plan, even an otherwise impecunious patient need not forgo ordinary care on account of cost. In many instances, preventive services can be covered, first dollar, so that they need not be foregone because an illness or injury consumes available funds. Defined contribution plans also can offer employees more continuity across job changes because they are often highly portable.

For an employer, defined contribution plans enable companies to provide benefits to workers at a predictable and limited cost. Employee satisfaction rises as workers are empowered to make their own health care decisions using their own spending accounts.

For the health provider, defined contribution plans enable physicians to focus on patient care and receive prompt payment for services. When patients are empowered to make their own decisions, there is no need for the physician to engage in expensive claims-processing procedures, eligibility determinations, utilization review or appeals following denials of coverage. Patients can simply present a debit card to the health-care provider, and payment is instant. The relationship between physician and patient is strengthened when there are no insidious incentives for physicians to withhold care.

For the health insurance company, defined contribution plans offer cost savings and limit risk of insolvency. Claims administration is minimized when patients control payment for services. Opportunities for fraud are greatly reduced. When third parties cover the expenses and bills are breathtakingly complex, patients have little reason to scrutinize bills. When health plans no longer need to govern myriad small expenses, they are free to focus on costly care for people with serious illness or injury.

The last decade's extraordinary turbulence offers some important lessons for policy leaders. It has become clear that most doctors do not make good business people, and most business people do not make good doctors. It is also clear that the vitality of health care depends on responsible and engaged consumers. Defined contribution plans offer shelter from the impending storm.

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