Demonizing the Insurance Industry Is Not the Answer

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In a last ditch effort to cram their health care reform package through Congress, Democrats have ramped up their demonization of private health insurers. They blame an alleged lack of competition in health insurance for all sorts of ills – from higher premiums to insurers denying coverage based on pre-existing conditions or dropping people who get sick.

According to the White House blog last week: “the insurers’ monopoly is so strong that they can continue to jack up rates as much as they like.” In The New York Times on Friday, Paul Krugman attacks what he calls the “vileness” of profit driven insurance companies. These arguments are echoed in Congress. In an ostensible effort to promote competition, the House recently passed legislation to exclude health insurance from the partial anti-trust exemption for the “business of insurance.” The 39 percent premium increase by Anthem Blue Cross for its individual (non-group) policyholders in California is continually touted as evidence of this monopoly power.

But what are the facts of this alleged monopoly power? Despite claims that it produces huge profits, health insurers’ profits generally average 3-5 percent of premiums. During the first nine months of 2009, profit margins were just 2.4 percent.

In his health care address to Congress last fall, Mr. Obama claimed: "Unfortunately, in 34 states, 75% of the insurance market is controlled by five or fewer companies. In Alabama, just one company controls almost 90% of the market. Without competition, the price of insurance goes up and the quality goes down." Likewise, on February 23, White House Press Secretary Robert Gibbs cited an American Medical Association study showing: “that 94 percent of the U.S. health insurance markets were highly concentrated.”

Yet, both the president's and AMA’s numbers are misleading as they look at less than half of the insurance market. About 55 percent of those insured receive their insurance from a “self-insured” employer, where the employer acts as the insurer, rather than from a traditional insurance company. These “self-insured” employers often hire other firms, including insurance companies, to help administer the plans (they handle the paperwork and form networks with doctors and hospitals). While employees often naturally think that the insurance company named on their insurance cards is providing the coverage, employers determine the details of coverage – from benefits to what premium the employee contributes – and they are responsible for putting aside money to cover employee medical costs.

The self-insured market consists of thousands of employers acting as insurance providers and competing for workers based on the salary they pay and the benefits they offer. Over 900 companies handle the administration of self-insured plans, with fees typically running three to eight percent of the total cost of insurance, depending on the employer’s size.

To see the difference this makes, take the president’s worst-case example of Alabama. The largest insurance company, Blue Cross/ Blue Shield of Alabama, accounts for 83 percent of the “fully insured” market, as opposed to self-insured employer plans. The fully insured market is therefore highly concentrated. But 57 percent of those
insured in Alabama get their coverage through thousands of employer self-funded plans. Blue Cross/Blue Shield of Alabama thus has only 36 percent of the total insurance market. The next largest insurance company in the state, Health Choice, has just 5 percent of the fully insured market, or 2.2 percent of the entire market.

Thus, it would be hard for Blue Cross/Blue Shield of Alabama to engage in price gouging, even if it wanted to, as many customers could turn to other insurers or more often, self-insure. In addition, the company is a non-profit entity, and its “profits” typically equal about 1 percent of its premiums. Or take the president’s claim that in the 34 most concentrated states, five or fewer companies control 75 percent of the insurance market. Given that self-insured firms cover over half of the people insured in those states, the total market share for the largest five insurers would average closer to 30 percent than 75 percent.

Allowing competition across state borders would be helpful, but the benefit has nothing to do with monopoly power -- it would allow more efficient insurance companies to expand. Many companies self-insure precisely to avoid state regulations that raise costs. Self-insurance is not regulated by the states but only comes under what has been, up to now, less restrictive federal rules.

As for the current anti-trust exemption for insurance companies, it likely promotes pro-competitive activity. Small insurers and employers use data on medical claims collected from many employers and health insurers to project the cost of providing health benefits. Small operations particularly benefit from sharing data because they do not have enough policyholders or employees to accurately forecast costs. While it is uncertain whether the existing anti-trust exemption is necessary to permit these activities, repealing it might lead to some data sharing activities being challenged, raising costs and leading small operations to stop providing coverage.

So, if insurance monopolies aren’t responsible for the higher premiums, what is? Regulation is a significant part of the problem. Take the 39 percent increase in insurance premiums from California’s Anthem Blue Cross. That state’s regulations make some people who buy insurance heavily subsidize others in the individual insurance market. Young people pay more than what it costs to insure them and older people pay less. The same discrimination occurs broadly between healthy and not so healthy people. What this government-imposed pricing has meant is that many healthier people decided to stop buying health insurance, leaving fewer people to subsidize the high cost, riskier policies and raising everyone’s rates.

A survey conducted jointly by the Kaiser Family Foundation, ABC News and USA Today, released in October 2006, found that 93 percent of insured Americans who had recently suffered a serious illness were satisfied with their health care. The survey questions in this poll were also asked of uninsured Americans, and Harris/Decima TeleVox asked them of Canadians covered by their government system. Uninsured Americans, not surprisingly, were not as satisfied as people who have insurance. Nonetheless, 70 percent of the uninsured who indicated their level of satisfaction said they were either "satisfied" or "very satisfied" with their health care, and only 17.5 percent said they were "very dissatisfied." Canadians are much less happy with their health care compared to insured Americans and just slightly more satisfied than uninsured Americans.

Few industries have as many competitors as health insurance. Despite President Obama’s distorted data, monopoly power isn’t the problem. Government mandates are the problem. Health insurance will only become more expensive if Obamacare becomes law.

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