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Evaluation of President Bush's Healthcare Plan

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On January 23rd, President Bush outlined a healthcare proposal in his State of the Union Address that aimed to address two major problems facing this country: 47 million uninsured citizens and the rising cost of healthcare. The president stated that the goal of his plan was to decrease reliance on government-sponsored programs while increasing access to private insurance. The proposal encourages Americans to take ownership of their health plans and make more informed medical choices.

The President's plan

President Bush's plan has two parts: a tax reform and a reallocation of federal funds. First, he calls for a restructuring of the tax code that would implement a standard deduction for the purchase of health insurance, regardless of its source (i.e. through an employer or the private market). Families would not pay payroll or income taxes on the first $15,000 of their compensation designated toward insurance coverage, and single people would not pay payroll or income tax on the first $7,500 of their compensation designated towards insurance coverage. Those whose insurance costs surpass the standard deduction would have to pay marginal taxes on the excess. To qualify for the tax deduction, the insurance plan obtained would have to offer maximum lifetime benefits of at least $700,000 and cover inpatient and outpatient services.

The President's proposal also creates the "Affordable Choices Initiative" which would reallocate federal funds that currently are directed toward Disproportionate Share Hospitals (DSH) (hospitals that care for a large number of uninsured or underinsured and Medicaid patients) to a state program that would pay premiums for basic, private insurance for the poor or the hard to insure. States would need to define basic benefits and then develop a subsidy program approved by the US Secretary of Health and Human Services.

The plan is budget neutral; it is designed to neither increase nor decrease tax revenues for ten years. The standard deduction is set to the Consumer Price Index (CPI) to control for inflation. As a result, it will grow at a much slower rate than insurance premium growth and healthcare spending. After the 10-year budget period, the tax reform is expected to increase income tax revenue, potentially reducing the deficit in the long run. If approved, the plan would be implemented in 2009.

How does the current system work?

Employer-based health insurance is a form of compensation that is not taxed by either payroll or income taxes. In order to attract workers, employers can offer generous health plans to their workers in lieu of higher salaries, and they are not taxed; the cost of providing health insurance can be deducted as a business expense. These tax exemptions on healthcare expenditures are effectively acting as a subsidy. The money that the federal and state government does *not* receive as a result of this tax break is known as a "health benefit tax expenditure." Federal and state health tax expenditures totaled $209.9 billion in 2004.[i] Fourteen percent of the population makes more than $100,000 yet this population accounts for 26.7% of all federal health tax expenditures.[ii]

Workers whose companies do not offer coverage, retirees without coverage and the unemployed who buy health insurance through the non-group private market all pay taxes without a deduction for their health insurance. People that obtain coverage through their jobs and self-employed individuals who buy coverage avoid paying these same taxes. However, when people pay more than 7.5% of their adjusted gross income (AGI) on healthcare, the excess amount is tax deductible.

How would the current system change under the President's plan? What would the impact be?

Under the President's proposal, health insurance would be considered taxable income for those employees with employer-sponsored coverage. They would now have to pay taxes on their wages plus their employer's contribution for health insurance. Employers would still be able to deduct their share of wages and benefits as they normally would deduct for compensation.

Eighty percent of employer-based policies cost less than the standard deduction outlined in Bush's proposal. Some people would experience no change in how much they pay in taxes. More than 100 million people would pay less in taxes.[iii] However, 20% of employer-based policies cost more than the President's proposed standard deduction. That means 30 million people stand to pay more in taxes unless they switch to a cheaper plan.

A family policy on the individual market is estimated at an average cost of $11,500[iv]. Under the new plan, the White House estimates that families who currently buy their own insurance would save $3,650 and families who currently do not have health insurance but decide to buy coverage under the President's plan would save $3,350 in taxes.

Under President Bush's proposal only those on Medicare would be able to claim a deduction if their health expenses are over 7.5% of their AGI. Also, Flexible Spending Accounts (FSAs) would no longer allow subscribers to pay for the employee portion of a premium or for out of pocket health expenses on a tax-free basis.[v]

Things to consider

The President's Affordable Choices Initiative gives the states the option to redirect DSH funds away from county and private hospitals that rely on those funds to care for indigent individuals or those without coverage. The money will be redirected into coverage for the uninsured, but if the state fails to provide adequate subsidies for those in need, there could be a funding shortage at hospitals that continue to provide care to those who are still unable to afford or obtain coverage. Providing more funding for programs like SCHIP or Medicaid would better assist low-income Americans obtain healthcare.

President Bush's plan aims to open up the private individual insurance market to more Americans. The assumption is that as more people join the market, prices will drop as the market becomes more saturated and regulates itself. Unfortunately, the individual market is plagued with high administrative costs and coverage exclusions for those who are older or who have chronic conditions. Without any sort of regulation of basic access to coverage or community-rated insurance plans, there is no guarantee that those seeking to purchase in the individual market will be able to buy and keep affordable coverage.

In 2005, 54.7% of Americans had employer-based health coverage, which is roughly 147 million people.[vi,vii] The reduction of the employment-based coverage tax break under the President's proposal might deter employers from providing coverage and thus erode the employer-based system. If some employers stop offering insurance and instead increase wages so their employees can buy individual insurance, this could possibly disrupt pre-existing risk pools, and high-risk individual employees may become uninsured. Workers with generous insurance plans are not necessarily wealthy individuals-often they are offered generous health coverage instead of higher wages. Many such individuals are in the 20% of those who would face higher taxes under the President's plan. Thus an increased financial burden may fall on some older and sicker employees who may be least able to afford it.

The President's proposed deduction is standard; those with health insurance get a deduction, regardless of the method used to obtain it. Even though the deduction is standard, what it is *worth* to you depends on your tax bracket. For example, if you are single and purchase a health insurance plan for $5,000 then the President's proposed $7,500 tax deduction would decrease your taxable income by $2,500. The higher your income tax bracket, the more you could save under the President's plan.

Tax Bracket	Savings from a $7,500 deduction
10%	$750
15%	$1,125
25%	$1,875
28%	$2,100
33%	$2,475
35%	$2,625

Those who do not pay income taxes because their earnings are below the tax threshold are not affected by the President's proposal; they would not benefit from the deduction because they do not pay income taxes. Fifty-five percent of the uninsured are in the 0% tax bracket, and 40% of the uninsured are in the 10-15% tax bracket.[viii]

There is concern that President Bush's proposal may create unfair incentives to purchase coverage through Health Savings Accounts (HSAs). By purchasing coverage through an HSA, individuals can use pre-tax dollars to purchase coverage and also get the standard $7,500 deduction. This may encourage tax "double dipping."

Would the proposal work?
The White House estimates that both aspects of the President's healthcare proposal would reduce the number of uninsured by 3-5 million people, but that still leaves at least 42 million without health insurance. President Bush's plan would cut taxes for roughly 100 million people and over the course of ten years is estimated to lower health spending by 0.5% of the GDP.[ix] The plan's emphasis on private individual insurance does increase the portability of insurance, but it does not make health insurance more affordable to most uninsured Americans.

One way to increase affordability for low wage workers is to offer a refundable tax credit, as President Bush has done in the past, instead of a deduction. Refundable tax credits can reach the 55% of the uninsured that have zero tax liability. President Bush has said that he is open to the idea of a refundable tax credit. Most federal legislators agree that the President's acknowledgement of the lack of affordable health insurance is an important first step, and they welcome his participation in a discussion that may begin to solve this nationwide problem.

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[i] Shiels & Haught, The Cost of Tax Exempt Health Benefits in 2004. Health Affairs-Web Exclusive, February 25, 2004.
http://www.healthaffairs.org/
[ii] ibid
[iii] Fact Sheet: Affordable, Accessible, and Flexible Health Coverage, The Office of the Press Secretary, January 22, 2007.
http://www.whitehouse.gov/infocus/healthcare/
[iv] Press Briefing on the President's State of the Union Health Care Initiative, The Office of the Press Secretary, January 22, 2007.
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[v] Burman, et al., The President's Health Insurance Proposal-A First Look. Tax Policy Center, January 23, 2007.
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[vi] President Bush Promotes New Health Care Plan, NewsHour with Jim Lehrer, Originally Aired January 25, 2007.
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[vii] Snapshot: California's Uninsured 2006, California HealthCare Foundation, 2006.
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[viii] Glied & Remler, The Effect of Health Savings Accounts on Health Insurance Coverage. The Commonwealth Fund, April 2005.
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