STOP Bad Ideas

A series examining proposals that could move private insurance in the wrong direction

Too Little, Too Late:
Why a $1,000 Tax Credit Won't Help the Uninsured

Currently, a record-high 45.8 million Americans lack health insurance coverage[1]—an increase of more than 4.5 million people since 2001.[2] As the ranks of the uninsured grow, policy makers are pursuing a wide range of options for helping the uninsured.

Who Are the Uninsured?

Contrary to popular belief, most people without insurance come from hard-working families. In fact, about 80 percent of the uninsured are in families where at least one member works full- or part-time.* Unfortunately, despite their high rate of employment, most of the uninsured work in low-wage jobs that not only fail to offer employer-based health insurance, but they also pay too little to cover the price of even the cheapest and least comprehensive private market policies. After paying for basic necessities like housing, utilities, and food, the average family of four living in poverty has only $215 a year left over for everything else, including health care. With such tight budgets, it's unfortunate but understandable that 60 percent of people living below poverty don't have any kind of health insurance.**

* Families USA, *One in Three: Non-Elderly Americans without Health Insurance, 2002-2003* (Washington: Families USA, June 2004).

** Families USA, *Cost-Sharing in Medicaid: It's Not about "Skin in the Game"—It's about Lives on the Line* (Washington: Families USA, September 2005).

The President's Proposal: A Tax Credit

Every year since 2001, President Bush has proposed a $1,000 tax credit to help uninsured, low-income people purchase health insurance in the individual market (the President's tax credit cannot be used to help pay the cost of employer-based coverage).[3] The Administration claims that the tax credit proposal will make health coverage affordable for the uninsured and thus will reduce the number of Americans without health insurance, but the evidence refutes these claims.

Tax Credit Justified by Questionable Studies

When the tax credit was first introduced, the President's Council of Economic Advisers made two key claims about its likely impact.

- First, they asserted that, in most cases, the tax credit would cover half the cost of a standard policy sold in the individual market.[4] But this assertion rested on a faulty study conducted by a private company that sells individual market health insurance online.[5] This study determined the cost of a standard policy by averaging premiums for people who actually purchased policies; it did not include premiums for those who were rejected for coverage or who were unable to buy because they couldn't afford the policy. The most that can be concluded from their methodology is that the $1,000 tax credit would have subsidized half the cost of premiums for the healthiest, most insurable people—those who were able to purchase coverage without benefit of a tax credit. The true, average cost of a standard policy for the uninsured would be much higher and, thus, a $1,000 tax credit would cover much less than half the cost.
- Second, the Council of Economic Advisers claimed that the tax credit would significantly expand health insurance coverage, enabling about four-fifths of the currently uninsured (85 percent) to purchase policies.[6] This claim also withers under scrutiny. An August 2005 report by the nonpartisan Congressional Budget Office (CBO) directly contradicts the Council of Economic Advisers. The CBO found that a subsidy of 50 percent of the premium cost (a much more generous subsidy than that proposed by the President) would increase uninsured workers' participation rate in the individual market by a mere 3.5 percent.[7] The President's tax subsidy, which is significantly lower, would obviously have a much smaller impact on participation rates.
- Furthermore, the assertion that the President's tax credit would enable up to 85 percent of the uninsured to purchase policies is drawn from a report that did not cover the President's proposal. Instead, this report surveyed a range of tax credit subsidy proposals that could be used to purchase employer-based coverage and that were not limited to the flawed individual market. In fact, the authors of that report strongly recommend that any tax credit be available for both individual and employer-based coverage. [8]

Tax Credit Tied to Flawed Individual Market

- Insurance premiums in the individual market are likely to be much higher than premiums in the employer-based market. Families USA has found, for example, that a healthy, non-smoking, 55-year-old woman can expect to pay $5,780 a year for a policy (if she can even find a company that will sell her a plan).[9] Yet the President's tax credit cannot be used to help pay the cost of more affordable employer-based insurance when such coverage is available.

- The insurance market for individual policies discriminates against older and sicker workers—those who are most likely to need insurance. In almost every state, the individual insurance market allows insurance companies to charge older and sicker people much higher premiums and to exclude coverage for many critical benefits. Worse, insurance companies are allowed to prevent individuals from purchasing individual coverage, either by setting premium prices so high that they are unaffordable or by refusing outright to sell a policy to a particular individual.
- Unless a tax credit is coupled with stringent reform of the individual insurance market, many of those who are in greatest need of coverage will be unable to find a suitable policy—with or without a tax credit.

Tax Credits Don't Make Insurance Affordable

- The majority of the uninsured have low incomes: One-third of the uninsured earn less than $25,000 a year, and another one-third earn between $25,000 and $50,000 a year.[10]
- In the employer-based insurance market, the average policy for an individual increased in price by 52 percent from 2000 to 2004 (from $2,424 to $3,695 annually),[11] compared to a 9.7 percent general inflation rate for all consumer goods over the same period.[12] Since 2000, the price of health insurance premiums has increased five times faster than the rate of inflation. Despite this inflation, the President has not proposed an increase in his $1,000 tax credit. Over time, spiraling health insurance costs will make the $1,000 tax credit increasingly inadequate.
- The President's Council of Economic Advisors points out that the tax credit is intended to help low-income people purchase " . . . (plans) which are not 'first dollar' plans but which . . . have per person deductibles of $1,000 for individuals and $2,000 per family . . . "[13]—hardly affordable deductibles for the very low-income individuals and families who are eligible for the President's full tax credit.[14]

Conclusion

Clearly, the President's proposed tax credit would be of little, if any, help to our nation's 45.8 million uninsured. It isn't big enough to cover the cost of health insurance, and it forces people to buy coverage in the individual market, which penalizes people for being old or sick. For working families living in poverty who have almost no money to spend after they pay for basic necessities like housing and food, the tax credit is not a solution—it is a sad smoke and mirrors act that keeps the nation from examining more feasible strategies that might help the uninsured gain health security.

Endnotes

[1] Carmen DeNavas-Walt, Bernadette D. Proctor, and Cheryl Hill Lee, *Income, Poverty, and Health Insurance Coverage in the United States: 2004* (Washington: U.S. Census Bureau, August 2005).

[2] Robert J. Mills, *Health Insurance Coverage: 2001* (Washington: U.S. Census Bureau, September 2002).

[3] Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2002 Tax Relief Proposals* (Washington: Department of the Treasury, April 2001). The proposed tax credit would be for an amount of up to $1,000 for low-income individuals and up to $3,000 for low-income families. It would only be available to those who do not have insurance coverage through their employers and who are not eligible for Medicaid.

[4] Council of Economic Advisers, *Health Insurance Credits* (Washington: Council of Economic Advisers, February 14, 2002), p. 7, available online at http://www.whitehouse.gov/cea/HealthCredit_Feb02wp.pdf, accessed on September 13, 2005.

[5] Council of Economic Advisers, *Health Insurance Credits* (Washington: Council of Economic Advisers, February 14, 2002), p. 7, available online at http://www.whitehouse.gov/cea/HealthCredit_Feb02wp.pdf, accessed on September 13, 2005. Citing www.ehealthinsurance.com/ehealthinsurance/eHealth2.pdf (access date not provided).

[6] Ibid.

[7] Congressional Budget Office, *The Price Sensitivity of Demand for Nongroup Health Insurance* (Washington: Congressional Budget Office, August 2005), available online at http://www.cbo.gov/ftpdocs/66xx/doc6620/08-24-HealthInsurance.pdf, accessed on September 13, 2005.

[8] The President's tax credit proposal can be used only in the individual market. The Council of Economic Advisors cites Mark Pauley and Bradley Herring, "Expanding Coverage Via Tax Credits: Trade-Offs And Outcomes," *Health Affairs*, Vol. 30, No. 1, January-February 2001. Pauley and Herring write on page 21, "Today's individual insurance market (as we have discussed elsewhere) is sorely in need of improvement, especially in terms of cost, ease of enrollment, and continuation of coverage…. The economies associated with group choice of plan and group billing available in the group setting are not easily extended to a market in which persons choose individually whether to be insured, what plan to take, whether to pay premiums and whether they should complain."

[9] Families USA, *A 10-Foot Rope for a 40-Foot Hole: Tax Credits for the Uninsured, 2004 Update* (Washington: Families USA, November 2004).

[10] *Health Insurance Coverage in the United States* (Washington: U.S. Census Bureau, 2002).

[11] Inflation in the costs of premiums was calculated directly by comparing the average costs of premiums for a single policy in the employer-based insurance market in 2000 to the same data for 2004. The average price of premiums in 2000 is taken from the following: Kaiser Family Foundation, *Employer Health Benefits 2000*, Summary of Findings (Washington: Kaiser Family Foundation, September 2000), available online at http://www.kff.org/insurance/loader.cfm?url=/commonspot/security/getfile.cfm&PageID=13525, accessed on September 13, 2005. The average price of premiums in 2004 is taken from the following: Kaiser Family Foundation, *Trends and Indicators in the Changing Healthcare Marketplace*, Section 3: Health Insurance Premiums (Washington: Kaiser Family Foundation, February 2, 2005), available online at http://www.kff.org/insurance/7031/ti2004-3-set.cfm, accessed on September 13, 2005.

[12] Kaiser Family Foundation, *Employer Health Benefits 2004 Annual Survey*, Summary of Findings (Washington: Kaiser Family Foundation, September 2004), available online at http://www.kff.org/insurance/7148/summary/index.cfm, accessed on September 13, 2005.

[13] Council of Economic Advisers, *Health Insurance Credits*, op. cit.

[14] The President's full tax credit subsidy is only available to individuals with annual incomes below $15,000 and families with incomes below $25,000.

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