

A TAX ON WORKING FAMILY BENEFITS

The Senate health reform bill (H.R. 3590) would tax health plans worth more than \$8,500 per year for individuals and \$23,000 per year for families. For workers in high-risk occupations and retirees 55 or older, the bill would tax plans worth more than \$9,850 for individuals and \$26,000 for families. In 17 high-cost states, the tax thresholds would be increased by 20 percent in 2013, 10 percent in 2014, and 5 percent in 2015.

This would amount to an enormous tax on middle class health benefits. A benefits tax is the wrong way to finance health care reform.

The Benefits Tax Is Designed to Hit More and More Lower-Cost Plans Over Time

- The benefits tax would affect 19 percent of workers with employer-provided health coverage in 2016, according to the Congressional Budget Office (CBO).¹
- Similarly, the international benefits consulting firm Mercer estimates that the tax would hit a fifth of all employers after it becomes effective in 2013.²
- However, more and more workers and employers would be affected in subsequent years, because the dollar threshold at which the tax applies would rise at a much slower rate than plan costs are expected to rise.
- CBO projects that revenues resulting from the tax would increase by 10-15 percent every year in the second decade after the tax takes effect.³
- The benefits tax is designed to hit more and more lower cost plans over time, and it would hit union and non-union plans alike.

High Cost ≠ “Cadillac” Benefits

- The benefits tax would affect many plans that have relatively high costs for reasons that have nothing to do with generous benefits.
- According to Mercer partner Linda Havlin, “It’s important to note that not all the plans that would be subject to the tax are particularly generous. There are other factors besides plan design that drive up cost.”⁴
- In fact, according to a recent study published by the prestigious journal *Health Affairs*, only 3.7 percent of the variation in the cost of family plans can be explained by benefit design, and only 6.1 percent of cost variation can be

¹ CBO, Letter to Sen. Bayh, Nov. 30, 2009, at p. 25. <http://www.cbo.gov/ftpdocs/107xx/doc10781/11-30-Premiums.pdf>

² Mercer, “Majority of Employers Would Reduce Health Benefits to Avoid Proposed Excise Tax,” Dec. 3 2009. <http://www.kaiserhealthnews.org/Stories/2009/December/02/cadillac-tax-cost.aspx>.

³ CBO, Letter to Sen. Baucus, Oct. 7, 2009, at p. 11. http://www.cbo.gov/ftpdocs/106xx/doc10642/10-7-Baucus_letter.pdf

⁴ Mercer, “Majority of Employers Would Reduce Health Benefits to Avoid Proposed Excise Tax,” Dec. 3 2009.

explained by benefit design plus plan type (HMO, PPO, POS, or high-deductible).⁵

- The same study found that two powerful variables explaining variation in premiums among health plans are the industry in which a plan sponsor operates (which may capture characteristics such as health status) and the cost of medical inputs in particular geographical areas, both of which are beyond a plan sponsor's control.
- Similarly, according to the actuarial consulting firm Milliman, "whether someone hits the [excise tax] ceiling is not so much driven by benefit richness as it is by age, gender, profession, health status, and the geography of the covered population."⁶

The Impact on Workers

- For a minority of affected workers, the benefits tax would mean higher premiums, as insurers increase premiums by the amount of the tax.⁷
- For the majority of affected workers, the benefits tax would mean higher out-of-pocket costs, as employers avoid the tax by offering health plans that increase cost sharing and cover fewer services.⁸
- According to a Mercer survey of 465 health plan sponsors, 63 percent say they would cut covered benefits to avoid paying the excise tax, 23 percent would maintain their current plan and pass along the tax to their employees, and only 2 percent would absorb the new tax themselves.⁹
- Also according to the Mercer survey, 7 percent of employer would terminate affected plans in response to the tax. Of small employers, which typically offer only one health plan, 9 percent would terminate their plans, potentially forcing employees into the individual market.¹⁰
- CBO concludes that the benefits tax would reduce premiums by reducing the amount of health insurance coverage purchased.¹¹ According to CBO, increasing cost sharing would reduce premiums both directly and indirectly.¹²
- CBO estimates that affected plans would reduce premiums by an average of 9 to 12 percent in 2016. This figure is an indication of the extent to which plans

⁵ Jon Gabel, Jeremy Pickreign, Roland McDevitt, Thomas Briggs, "Taxing Cadillac Plans May Produce Chevy Results," Health Affairs (Dec. 3, 2009). <http://content.healthaffairs.org/cgi/reprint/hlthaff.2008.0430v1?maxtoshow=&HITS=10&hits=10&RESULTFORMAT=&author1=gabel&andorexactfulltext=and&searchid=1&FIRSTINDEX=0&resourcetype=HWCIT>

⁶ Robert Dobson, "No Room to Stand," Milliman Health Reform Briefing Paper (Sept. 2009) (referring to previous version of the excise tax). <http://www.milliman.com/perspective/healthreform/pdfs/no-room-to-stand.pdf>

⁷ CBO, Letter to Senator Bayh, Nov. 30, 2009, at p. 25.

⁸ *Ibid.*

⁹ Mercer, "Majority of Employers Would Reduce Health Benefits to Avoid Proposed Excise Tax," Dec. 3 2009).

¹⁰ *Ibid.*

¹¹ CBO, Letter to Senator Bayh, Nov. 30, 2009, at p. 9.

¹² CBO, Letter to Senator Bayh, Nov. 30, 2009, at p. 25.

would have to reduce coverage to bring their premiums below the tax threshold. It does not represent a reduction in the price of insurance for a given amount of coverage, but rather a reduction in the amount of coverage.

- Professors Joseph White and Timothy Jost write that “the excise tax is simply a fall-back cost-control method that targets beneficiaries: if health care costs rise too quickly, the federal government will slash health insurance benefits for people in the employer-based system, even if costs are high because of the need for care.”¹³

A Benefit Cut Is Not “Keeping What You Have”

- The benefits tax is designed to force more and more plans over time to increase out of pocket costs for beneficiaries, in hopes that beneficiaries will utilize fewer health care services.
- The tax would raise health care costs for some of the most vulnerable workers—workers in small firms, workers in firms with sicker employees, and workers in firms with older employees.
- The benefits tax would thus violate one of the fundamental commitments of health care reform: that workers should be able to keep the health care coverage they have now.

A Benefit Cut Is Not “Win-Win” For Workers

- Advocates for the benefits tax argue that it would be a “win-win” for workers, on the assumption that employers will immediately increase wages for all affected beneficiaries to compensate them on a dollar-for-dollar basis for the reduction in their benefits.
- However, the Mercer survey of 465 health plan sponsors found that “less than a fifth of respondents (16 percent) say they would convert their cost savings into higher pay.”¹⁴
- This finding is consistent with another recent survey of 433 human resources and benefits executives, which found that only 9 percent would increase salaries and direct compensation if health care reform reduced costs to their organization, while 78 percent would retain savings in the business and 23 percent would pass on savings to customers.¹⁵
- It is especially unlikely that retirees whose benefits are cut to avoid the tax would see any corresponding increase in wages.

¹³ Joseph White and Timothy Jost, “Cadillacs or Ambulances? The Senate Tax on ‘Excessive Benefits’” Healthaffairs.org (Dec. 3, 2009). <http://healthaffairs.org/blog/2009/12/03/cadillacs-or-ambulances-the-senate-tax-on-excessive-benefits/>.

¹⁴ Mercer, “Majority of Employers Would Reduce Health Benefits to Avoid Proposed Excise Tax,” Dec. 3 2009).

¹⁵ Towers Perrin, “Employers Put Cost at the Top of Health Care Reform Priority List,” Sept. 17, 2009. http://www.towersperrin.com/tp/showdctmdoc.jsp?url=Master_Brand_2/USA/Press_Releases/2009/20090917/2009_09_17.htm&country=global

“Bending the Cost Curve”

- Advocates for the excise tax also argue that it is essential to “bend the curve” of health care costs and expenditures. However, a recent report by the Commonwealth Fund found that “there is little empirical evidence that such a tax would have a substantial effect on health care spending.”¹⁶
- When the Commonwealth Fund asked health care opinion leaders to rate the effectiveness of nine system reforms contained in the House and Senate health care bills, the benefits tax was ranked last.¹⁷
- Increasing out-of-pocket costs for workers may actually lead consumers to forgo necessary care and make counterproductive health care decisions.¹⁸
- The key to reining in health care spending is to get providers to deliver care in more cost-effective ways.¹⁹

Reform Health Care Without Taxing Benefits

- The U.S. House’s bill pays for health care reform through a surtax on the very wealthiest earners, who benefited so much from Bush-era tax cuts, not through a benefits tax. The House bill gets it right.

¹⁶ The Commonwealth Fund, “Starting on the Path to a High Performance Health System: an Analysis of Health System Reform Provisions of House of Representatives and Senate Health Reform Bills,” Nov. 2009.

http://www.commonwealthfund.org/~media/Files/Publications/Fund%20Report/2009/Nov/Analysis%20of%20Health%20System%20Reform/Davis_BillsSystemReform_Exec%20Summ_cah.pdf

¹⁷ *Ibid.* (However, a majority nevertheless did support the tax.)

¹⁸ Michael Chernew and Joseph Newhouse, “What Does the RAND Health Insurance Experiment Tell Us About the Impact of Patient Cost Sharing and Health Outcomes,” *American Journal of Managed Care* (July 2008); Bruce Vladeck and Thomas Rice, “Market Failure and the Failure of Discourse: Facing Up to the Power of Sellers,” *Health Affairs*, vol. 28, no. 5 (2009); Joseph White and Timothy Jost, “Cadillacs or Ambulances? The Senate Tax on ‘Excessive Benefits’” *Healthaffairs.org* (Dec. 3, 2009), <http://healthaffairs.org/blog/2009/12/03/cadillacs-or-ambulances-the-senate-tax-on-excessive-benefits/>.

¹⁹ The Commonwealth Fund, “Starting on the Path to a High Performance Health System: an Analysis of Health System Reform Provisions of House of Representatives and Senate Health Reform Bills,” Nov. 2009.