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## **THE CASE FOR RETARGETING TAX SUBSIDIES TO BROADEN HEALTH CARE COVERAGE**

### **Shift from Employer-Based to Individual Health Insurance Would Extend Coverage, Improve Portability, and Reap Cost Savings**

ANNANDALE-ON-HUDSON, N.Y.--While market and budgetary discipline has slowed the rise in health care expenditures in recent years, this cost-cutting trend has also dimmed prospects for expanding health care coverage to the more than 40 million Americans without health insurance, according to Walter M. Cadette, senior fellow at The Jerome Levy Economics Institute. Cadette, author of a new Levy Institute Public Policy Brief on health care policy, contends that the nation must rethink the way it finances health care if coverage is to be extended to the growing ranks of the uninsured.

In *Prescription for Health Care Policy*, Cadette makes the case for retargeting tax subsidies to health care to expand coverage to the uninsured and to contain spiraling costs. He lays out the argument for transforming the tax exclusion of employment-based health insurance into an income-scaled tax credit for individuals to purchase basic but comprehensive health insurance.

"The tax-subsidized, employment-based health insurance that has made American medical care inordinately expensive and, in the process, exclusionary is now dated, linked to a model of the labor market that no longer reflects reality," Cadette says. "Not only are many low-income workers left out, those who benefit from employment-based health insurance are increasingly finding their freedom of choice restricted as employers seek to curb costs," he says, noting also that many who receive subsidies through the current system are those who are least in need. "A reasonable alternative--one that holds out promise of controlling costs as well as providing protection for the uninsured--is to require people to purchase health insurance as individuals, rather than as employees, and to subsidize that purchase as necessary" through a tax credit or other forms of subsidy for nontaxpayers, Cadette says.

While some would argue that a requirement to carry individual health insurance is burdensome, it is no more so than the requirement that all car owners carry liability insurance because an uninsured driver represents an unfair potential cost to everyone else on the road, Cadette says, adding that a mandate is not all that onerous if it is accompanied, as needed, by the financial resources to pay for it. "This mandate is less of a constraint on free choice today

than it would have been in an earlier time when employees had greater choice of medical insurance than they have now in the era of cost-cutting and HMOs," says Cadette.

A plan retargeting tax credits to individuals could be budget neutral, with \$80 billion of revenue now forgone through the tax exclusion freed up with the exclusion's elimination. "And such a program promises real economies in the use of medical care, because people are likely to shift to catastrophic policies when they have to use after-tax income to pay for any insurance costing more than the tax credit they receive," Cadette says.

Medicare could be integrated into an income-scaled tax credit plan, reflecting the principle that subsidies for health care should be based on need just as much for the elderly as for the population at large, says Cadette. Medicaid also could be fashioned as a tax-credit plan. "Such a plan would eliminate the disincentive to get a job, namely, the loss of health insurance benefits, that recipients now have," according to Cadette. "This so-called notch problem will have to be addressed if the nation is to make a serious effort to move people off welfare and into work."

A constituency for transforming the exclusion into an income-scaled tax-credit could be fashioned by stressing that individual insurance is the only truly portable insurance, as it cuts the link between health care and employment, Cadette says. A tax-credit plan provides health care security for most middle-income Americans at the same time that it provides for the uninsured poor.

Corporate America could also be part of the constituency for transforming the exclusion into a credit. While it has benefited from the exclusion, which is a way of leveraging compensation costs, it is not well served by the damage to employee morale that has come about because of the need to control health care costs, a need that is rooted in the tax-free way the nation has financed much of its health care, says Cadette. "Being 'the heavy' when employees feel deprived of needed care for themselves and their family is not a role Corporate America could possibly want." Business probably would retain a role in health insurance under a tax-credit plan--if not as a provider, as a sponsor. Retaining a role would foster employee welfare, yet end the hopelessly ambivalent position employers find themselves in as administrators of health insurance.

[Public Policy Brief No. 30, \*Prescription for Health Care Policy, The Case for Retargeting Tax Subsidies to Health Care\*, 1997](#)

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