



Testimony for

**THE UNITED STATES SENATE
FINANCE COMMITTEE**

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By

**Janet Stokes Trautwein, Director of Federal Policy Analysis
THE NATIONAL ASSOCIATION OF HEALTH
UNDERWRITERS
2000 North 14th Street, Suite 450
Arlington, VA 22201
(703) 276-3806
www.nahu.org**

Good afternoon. My name is Janet Stokes Trautwein. I am the Director of Federal Policy Analysis for the National Association of Health Underwriters. **The National Association of Health Underwriters** is an association of insurance professionals involved in the sale and service of health insurance, long-term care insurance, and related products, serving the insurance needs of over 100 million Americans. We have almost 17,000 members around the country. We appreciate this opportunity to present our comments regarding the rising number of uninsured Americans. NAHU has been a proponent of refundable health insurance tax credits to address the problem of the uninsured for more than a decade, and is pleased to have this opportunity to discuss the practical application of a tax credit with the members of this committee. We believe a refundable health insurance tax credit will provide a real solution to the problem of the uninsured in America by addressing affordability - the most basic component of access to health care.

The current estimate on the number of uninsured in this country is approximately 43 million people. That number represents an increase from a few years ago, despite numerous state and federal efforts to improve access. Over half of the 43 million uninsured Americans are the working poor or near poor, many of whom already have access to health insurance through an employer-sponsored plan.¹ Since employers already provide access to health plans and pay a significant portion of the premiums for many Americans, why do we have so many uninsured? The problem isn't access – it's affordability. **They just can't pay for it.**

This inability to pay has many causes. As we know, the United States government gives a tax break to people covered under their employer's health insurance plan. Health insurance premiums paid by an employer are not taxable as income to employees, even though many people consider employer-paid health insurance to be a part of compensation. Although this tax break has provided an excellent incentive for many people to become insured, it has also inadvertently created another problem – lack of tax equity. When an employer pays \$100 in tax-free health insurance premiums for an employee in a 30% tax bracket, it's worth \$30 to that employee. To another employee in a 15% tax bracket, it would be worth \$15, and for the low-income employee with no tax liability or the person who is self-employed or otherwise has no employer-sponsored plan available, the tax break is worth nothing. That's why many low-

income employees who must pay part of the cost of employer-sponsored health insurance coverage for themselves or their family have declined coverage. Most people in employer plans benefit from both the dollar amount of the employer contribution and the tax exemption on employer-sponsored health insurance premiums. Low-income individuals only benefit from the employer's contribution if they are able to pay their share of the remaining premium, and they don't benefit at all from the tax exemption. Increased deductibility of health plan premiums for the self-employed has helped and will help more as greater deductibility is phased in. Unfortunately, however, deductibility does nothing for the bulk of the uninsured – the working poor with no or very low tax liability.

People with no tax liability don't benefit from a deduction for two reasons. First, if they owe no taxes, there is nothing from which to deduct their premiums, even if the deduction was available without the requirement that a person itemize. Second, and probably more important for the working poor, a deduction or even a credit that is only available at the end of the year is of no value to them because they need the funds at the time their health insurance premium is due. They can't wait a year to be reimbursed, so they forego insurance entirely. That's why they are uninsured now.

Fortunately, there is a solution for this problem. A refundable, advanceable tax credit would allow individuals to receive their tax credit dollars monthly, when their premiums are due. This type of credit, advanced monthly and administered through the insurance company or the employer, provides the following benefits:

- It is simple to understand.
- It is almost impossible to abuse, since the insurance company or employer would certify that coverage was purchased.
- It enhances the effectiveness of COBRA's access mechanism by providing a means to pay COBRA or other health insurance premiums when people change jobs.
- It provides early retirees with needed dollars to help them purchase a health insurance policy.

¹ U.S. Census Bureau, 2000.

- Small employers who currently can't afford to provide a health insurance plan would, with the combination of the contribution they could provide and dollars provided to eligible employees through a health insurance tax credit, be more likely to offer a group health plan to workers.²

Tax Credits in Employer-Sponsored Plans

Some health insurance tax credit proposals do not allow a credit to be used in an employer-sponsored plan. A better solution is a health insurance tax credit designed to be used either to buy coverage in the individual health insurance market or to help an employee pay his or her share of premiums in an employer-sponsored plan. Most people are happy with the employer-based system, according to a 1999 survey by the Employee Benefits Research Institute, and many uninsured individuals already have high-quality employer-based coverage available to them. A recent NAHU survey of small employers shows that many small employers pay most or all of an employee's health insurance premium, but little or none of the cost of coverage for dependents. Allowing low-income employees to supplement their employer's contributions with a refundable tax credit would allow families to be insured together, which many employees prefer, and would provide the funds necessary to allow them to come up with "their share" of health insurance premiums. It would also address concerns from the business community, such as declining take up and shrinking pools, and would empower individuals to select their own place of purchase, rather than having it imposed on them by the government.

Another way to help employees pay their share of premiums would be to allow (but not require) advanceable Earned Income Tax Credit (EITC) dollars to be combined with health insurance tax credit dollars for eligible employees. Past concerns about whether or not adequate coverage would be purchased with EITC dollars would be addressed through the administration mechanisms of the health insurance tax credit, which require the purchase of HIPAA-creditable coverage, certified by either the employer or the insurance company.

Should a Tax Credit be Flat or a Percentage of Premiums?

² See NAHU survey of small employers, March 2001.

Some people claim that because the cost of individual health insurance is different for individuals of different ages and in different states, a flat credit is unfair and inflexible. It is true that health insurance costs are different for different populations. But a credit based on a percentage of premiums is difficult to administer because of these very differences. It is very important that a health insurance tax credit be advanced monthly, when premiums are due. This can be done through insurance carriers for those who purchase individual health insurance coverage as well as through the employer payroll process for those who purchase coverage in an employer-sponsored plan. If administration becomes too difficult, it won't be cost-effective for employers and insurers to handle this administration, and they will elect not to advance tax credits to individuals. This will result in the tax credit not being available to individuals and families until they file their tax return.

How Much Should the Tax Credit Be?

Over the years, NAHU has spent a considerable amount of time looking at the dollar amount of a health insurance tax credit. In doing so, we looked carefully at the amount of coverage that is currently financed by employers. Employers pay for much of the coverage that insures most people today. It is very important that in our zeal to do something about those without health insurance that we don't inadvertently discourage employer funding of coverage for those who are already insured today. For that reason, it is important that a health insurance tax credit be low enough so that it will not provide an incentive for employers to discontinue their financial contributions towards plans. At the same time, it is important that the credit be large enough to provide a meaningful incentive for people without access to an employer-sponsored plan to obtain coverage.

A credit in the range of \$1,000 for individuals and \$2000-\$2,500 for families is not large enough to cause an employer to stop providing coverage for employees, yet still provides a good base to finance coverage, even for employees purchasing coverage in the individual health

insurance market.³ We've attached as exhibits several comparisons of the cost of health insurance across the country. The first exhibit gives some examples of the types of health insurance coverage that are available to a single mother with two children for a contribution of about \$2,600 per year. This assumes she does not have an employer plan available and has a \$2,000 tax credit plus \$50 per month of her own money. We've also illustrated the costs of coverage in a second exhibit for a higher level of benefits. A third exhibit gives a sampling of group insurance costs for the same person. Keep in mind that coverage offered in employer-sponsored plans provides a significantly higher level of benefits in many cases than what is available in the individual market, in addition to being less expensive. The controlled access in employer plans is much more effective at keeping a balanced risk pool than the individual health insurance market. But a tax credit would bring new people into the individual health insurance pool and would over time encourage insurance companies to write individual health insurance policies geared to the size of the credit, offering more options and making it possible for low-income families to obtain coverage without paying much more than the credits available.

Is a \$1,000 Tax Credit (\$2,000 for a Family) Large Enough to Buy Reasonable Coverage?

Individuals without employer-sponsored health insurance currently must purchase coverage in the individual health insurance market entirely on their own. This is particularly hard for low-income employees who may have to choose between health insurance and groceries, and even employees who do have employer-sponsored coverage available may not be able to participate because they can't afford their share of the premiums. A health tax credit should be considered a base from which to build on the financing of health insurance coverage. It is not designed to take away the role of the employer in the financing of health insurance coverage, or to replace personal responsibility.⁴

What if Someone Doesn't Qualify for Coverage in the Individual Health Insurance Market due to a Health Condition?

³ The amount of the tax credit would periodically change to reflect increases or decreases in the COST of living, as reflected by the medical Consumer Price Index (CPI).

⁴ To get an idea what is available in the individual health insurance market, see "Individual Health Insurance Coverage options across the United States," March 2001, National Association of Health Underwriters.

In most states individual health insurance requires that a person be in relatively good health. If a person does not qualify for coverage based on their medical history, many states have a high-risk pool or some other mechanism to ensure that coverage is available. High-risk pools provide an affordable alternative for high-risk individuals who don't have access to employer-sponsored coverage and must purchase individual health insurance coverage. An exhibit illustrating the cost of coverage in a sampling of states with high-risk pools is attached. A refundable health insurance tax credit could help eligible high-risk individuals afford the cost of health insurance coverage in high-risk pools in the same way it would be used for others who purchase coverage through their employer's plan or through the regular individual health insurance market. In addition, states without any safety net for the medically uninsurable should be encouraged and provided with incentives to develop programs to ensure that coverage is available for these individuals.

Administering a Refundable Health Insurance Tax Credit

The Treasury Department would have primary responsibility for administering tax credit payments. The credit, while owned by the individual, would not be paid directly to the individual, but would be transmitted to an insurance company, employer, high-risk pool, or other organization maintaining the individual's insurance account. The credit could be used only for the payment of private insurance premiums, and could not exceed the total cost of the premiums. Only health plans eligible as creditable coverage under the Health Insurance Portability and Accountability Act of 1996 (HIPAA) would be eligible for credit payment. The credit would be available on a monthly prorated basis, in order to ensure the continuing availability of credit funds throughout the year, particularly in cases of job change, and to help protect against fraud.

In cases of employer-provided insurance, the monthly tax credit allocation can be handled as part of the regular withholding process. The credit would be shown as a specific line item on the pay stub. Federal income taxes withheld by the employer on behalf of employees would be reduced by the amount of the credit before being sent to the government.

For those individuals purchasing coverage in the individual health insurance market, the monthly tax credit allocation could be subtracted from the regular monthly health insurance premium due, with the insurance company using normal billing mechanisms for the balance, if any, of the premium. As with employer plans, insurance companies could reduce federal taxes owed by the amount of credits they had advanced to eligible individuals.

Economic Impact of a Health Insurance Tax Credit

A refundable health insurance tax credit for low-income individuals is an innovative way to achieve affordable health insurance coverage through the competitive private sector. A health insurance tax credit will help ensure that low-income Americans who have the greatest difficulty affording coverage will have a basic level of resources to purchase health insurance. The tax credit, by being available only for the purchase of private sector insurance, will allow a shift of low-income individuals from the very costly Medicaid program into private insurance plans. A health insurance tax credit would also help to lower the per capita cost of insurance, by reducing the amount of uncompensated care that is currently offset through cost shifting by health care providers to private sector insurance plans, and by substantially increasing the insurance base, spreading the cost over a wider number of people.

The Children's Health Insurance Program

A discussion of the uninsured would be incomplete without mention of the Children's Health Insurance Program. Many of NAHU's members have been invited to serve on state task forces and committees to assist in implementation and outreach for CHIP. They have consistently reported several shortcomings of the federal CHIP legislation, which they feel have impeded their states' ability to reach the largest number of uninsured children.

Under the Balanced Budget Act, states have a number of options for implementing plans most appropriate to the needs of their uninsured children. One of those options is to expand Medicaid. The other available options are centered in the private sector. One reason many of the

people who are already eligible for Medicaid today do not enroll is that they do not want the negative stigma associated with public assistance. Private sector programs can represent a transition from this stigma by allowing and encouraging people to embrace the concept of “self-help” as opposed to the expectation of government entitlement. As you know, this is a concept that has ramifications that extend far beyond the health insurance benefits provided by the plan. Congress wisely considered these private sector advantages and not only authorized states to develop private sector CHIP programs, but also allowed for children to be enrolled in the employer-based plans of their parents.

Unfortunately, due to some of the inflexible provisions that were also contained in the CHIP provisions of BBA, many states have been unable to adequately implement the full range of options allowed by the legislation. Even though it appears that states have a range of plan benefit options, that reality is virtually eliminated by the cost-sharing limitations contained in the legislation. Cost sharing is prohibited for children in families under 150% of the poverty level, and is limited to 5% of family income above that level. Unfortunately, cost sharing is defined to extend beyond premium to include co-payments and co-insurance.

A quick calculation of the maximum potential co-insurance liability of an “average” plan, such as might be offered to state employees, one of the plan prototypes allowed under the legislation, for example, would make that plan unacceptable. Under CHIP guidelines, the co-insurance responsibility alone would exceed the 5% maximum for many eligible participants. This requirement, along with certain mandated benefit requirements that were also included in the legislation, virtually forces states to use a benchmark plan based on Medicaid level benefits, which, we would point out, are far in excess of what the average child who is already insured enjoys today. Those parents who have already made the sacrifices necessary to see that their children are insured, many of whom are at an income level that would allow CHIP participation, are not eligible for CHIP funding because they are “already insured.” In addition, the message they are receiving as a result of exercising responsible behavior is that the plans under which their children are now insured aren’t good enough, because they may not meet the standards established under CHIP for uninsured children.

The other problem associated with the cost-sharing requirements is that because each employer plan is different, and the family income of each eligible child is different, a separate mathematical calculation is required for EACH participant, to be sure the 5% cost-sharing limitation is met for that particular plan and participant. Employer-sponsored coverage is often the easiest and most cost-effective option available for children and their families, and will allow families the opportunity to be enrolled together on the same employer-sponsored plan, but the separate calculation requirement makes plan administration unwieldy and expensive. For this reason it is unlikely that opportunities for participation in employer-sponsored plans will be aggressively pursued. This frustrating provision of the legislation is only worsened by a ruling by HCFA that employer plans where employers are paying less than 60% of the family premium are not eligible for participation in the CHIP program.⁵ Not only does this ruling by HCFA have no legislative basis, but surveys show that very few employers pay a significant part of the dependent premium, much less 60%.

Summary

A refundable health insurance tax credit represents a simple and realistic way to extend private health insurance coverage to those uninsured individuals and families who are most in need of assistance. It is fair and is easy to administer. It is a private sector solution to a difficult public problem. It gives people the tools to make their own decisions.

In addition to a tax credit, the Children's Health Insurance Program could be greatly improved and made available to many more eligible uninsured children if changes were made to the cost-sharing requirements of the CHIP program to define cost-sharing as premium cost-sharing only. It would also appear that HCFA's concerns about crowd-out are unwarranted at this time since many states have not been able to use their current allotment of CHIP dollars. The best safeguard against crowd-out would be to facilitate the use of employer-sponsored plans

⁵ Pending HHS Children's Health Insurance Program regulations may lessen this requirement slightly. HCFA's 60% employer contribution requirement was designed to avoid "crowd-out" which theoretically can occur when employers or employees drop the coverage they currently pay for in order to take advantage of government funding.

in the CHIP program.

The most important patient protection is the ability to afford health insurance coverage. Real access to health care and choice can't exist without the dollars required to buy a health plan.

I appreciate this opportunity to testify today and would be happy to answer any questions the committee may have.

Should you have any questions or if we might be of any additional assistance, please contact Janet Stokes Trautwein, Director of Federal Policy Analysis for NAHU, at (703) 276-3806, or jtrautwein@nahu.org.

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