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Executive Summary

No. 1445 June 1, 2001

# WHY ADOPTING THE "COMMON GROUND" HEALTH CARE PROPOSAL WOULD BE A COSTLY MISTAKE

*ROBERT E. MOFFIT, PH.D.*

The Health Insurance Association of America (HIAA), a large trade association, and Families USA, a grassroots organization long associated with campaigns for sharply expanding the government role in health care, have agreed on a proposal to reduce the number of America's uninsured. The HIAA–Families USA "Common Ground proposal" recommends expanding the State Children's Health Insurance Program (S–CHIP) and Medicaid to include lower-income working adults and their families. It also recommends a new set of tax breaks for employers who cover previously uninsured workers who meet strict income eligibility criteria.

The Common Ground proposal has special relevance for Congress, since the fiscal year (FY) 2002 budget resolution sets aside $28 billion over three years to deal with the growing problem of the uninsured. Congress needs to deal with this issue, but it does not need to exacerbate the health care system's many problems by further eroding patient choice and control—which is exactly what the Common Ground proposal would do. This proposal represents flawed health care policy for a number of reasons.

1. **Its requirements would be difficult for businesses to implement.** To provide insurance coverage to their uninsured workers and receive a tax credit, employers would have to verify that workers meet the precise eligibility criteria. This is particularly problematic for small businesses that do not employ personnel to administer health insurance; taxpayers could subsidize the "wrong" workers. Employers also would be forced to gather an unreasonable amount of personal information on household income to verify a worker's eligibility. This would greatly increase their regulatory burden.

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2. **It relies on the relatively inefficient small employer system.** Small-business insurance pools have high administrative costs and limited or nonexistent personal choice of plans and benefits, making small firms poor vehicles for a serious expansion of health insurance.

3. **It reinforces flaws in the current employer-based system that spur patient dissatisfaction.**

The proposal preserves outdated federal tax policies that frustrate patient choice and genuine competition by distorting markets, driving up costs, and encouraging a steady erosion of patient control.

4. **It would significantly expand Medicaid.** The incentives in the proposal, as well as the compliance burden connected with its tax credit component, could encourage firms with a disproportionately large number of lower-income employees to cease offering health insurance. The effect would be further contraction of the private health insurance market as Medicaid expands.

5. **It would lay the groundwork for greater government control of health care.** By significantly expanding Medicaid and consolidating, to the extent practical, employer and insurance industry restrictions on health care decisions, the proposal would increase government's role in the delivery of health care. Employer restrictions invite government intervention. The next step would likely be government mandates on employers to provide insurance, with government specifying the treatments or procedures included in the approved benefits package.

**Building on a Real Consensus.** In sharp contrast to the Common Ground proposal, President George W. Bush would design a system that "puts a priority on access to health care without telling Americans what doctors they have to see or what coverage they must choose. Many working Americans do not have health care coverage, so we will help them buy their own insurance with refundable tax credits."

Within the broader health care policy community, there is strong bipartisan agreement that tax relief for individuals is a far better approach than expanding government programs. Small businesses also overwhelmingly support a system of tax credits that go directly to individuals and families, rather than a system based on new government reporting requirements that would increase their paperwork and administrative burdens. To build on this growing bipartisan consensus, Congress should work with the President to:

- **Create a system of refundable tax credits to expand health coverage.** Providing individual tax relief for insurance would help millions of Americans who need coverage. It would enable individuals to choose the kinds of plans, benefits, and doctors that best suit their family needs. It would promote personal control and ownership of insurance policies, including policies sponsored by associations or fraternal and faith-based organizations.

- **Allow S–CHIP funds to be used for tax credits and vouchers for the purchase of private health insurance.** Legislative report language accompanying the S–CHIP provisions of the Balanced Budget Act of 1997 encourages states to explore "innovative means" to expand health coverage. Such means should include the use of tax credits and vouchers to extend private coverage to children. The President and Congress can make technical adjustments in the law to facilitate the use of this option.

- **Reject incremental steps that lead to an increase in government or even employer control over health care decisions.** Most Americans, with the assistance of their doctors, want more, not less, personal control over sensitive health care decisions.

Enabling individuals and families to control their own health insurance coverage and giving assistance directly to those who need help the most would greatly improve America's health care system. The Common Ground proposal would increase employment-based coverage of the uninsured only if enough employers think it is worth the effort to obtain the new tax credit. Regardless of what private companies do, however, government-subsidized health care would expand, and an already ailing private health insurance market would contract even further and aggravate the problems that plague today's system, including the steady erosion of control by patients over the most sensitive decisions affecting their lives. Congress and the Bush Administration can do much better.

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*ROBERT E. MOFFIT, PH.D.*

Executives of the Health Insurance Association of America (HIAA), a large trade association, and Families USA, a grassroots organization long associated with campaigns for sharply expanding the government role in health care,[1] recently agreed on a proposal to reduce the number of uninsured in America. Not surprisingly, the agreement between these strange bedfellows proposes a major expansion of government health programs coupled with new tax breaks for business.[2] Specifically, the so-called Common Ground proposal would expand the State Children's Health Insurance Program (S–CHIP) and Medicaid to include lower-income working adults and their families. It also would give tax breaks to employers who cover previously uninsured workers,[3] while making employers responsible for determining whether low-income employees meet the strict income eligibility criteria.[4]

It is likely that Congress will address the issue of the uninsured this year, and it is crucial that this be done correctly. In the fiscal year (FY) 2002 budget resolution, Senate negotiators have set aside $28 billion over three years to cope with the problem of the uninsured.[5] The President and a bipartisan group in Congress have proposed a progressive tax credit

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1. According to a report in *The Wall Street Journal*, Families USA is "a nonpartisan but progressive public policy organization that was a major booster of the Clinton health care agenda." See Rhonda L. Rundle and Shailagh Murray, "The Have-Nots," *The Wall Street Journal*, February 21, 2001, p. R7.
2. The American Hospital Association, the nation's largest hospital trade association, has joined HIAA and Families USA in promoting the Common Ground proposal.
3. For a detailed explanation of the proposal, see Charles N. Kahn III and Ronald F. Pollack, "Building a Consensus for Expanding Health Coverage," *Health Affairs*, Vol. 20, No. 1 (January/February 2001), pp. 1–9. Kahn is president of HIAA, and Pollack is executive director of Families USA.
4. Curiously, even though small employers would carry a substantial burden in making the Common Ground proposal work, the National Federation of Independent Business (NFIB), the nation's largest association of small-business owners, was not consulted during development of the substance of the HIAA–Families USA proposal.

approach to expand patient choice and private plan options.

The Common Ground proposal, however, takes the opposite approach to reducing the number of uninsured. It represents flawed health care policy for a number of reasons.

- **Its requirements would be difficult for businesses to implement.** In order to provide insurance coverage to their uninsured workers and receive a tax credit, employers will have to verify that workers meet precise eligibility criteria. Mistakes could cause employers, as well as their employees, to run afoul of the Internal Revenue Service or other authorities. This is particularly problematic for small businesses that do not employ personnel to administer health insurance. The tax credit could become economically inefficient, and taxpayers could end up subsidizing the "wrong" workers. Moreover, employers would be forced to gather an unreasonable amount of personal information on household income to verify a worker's eligibility. Such a measure would greatly increase the burden on businesses to comply with government regulations.
- **It relies on the relatively inefficient small employer system.** Large corporate employers do a relatively good job of controlling administrative costs associated with health coverage, providing choice, and promoting economic efficiency in premium pricing and pooling. The same cannot be said of small employers, even though this is where disproportionately large numbers of the uninsured are concentrated. Among these employers, insurance pools are obviously small, administrative costs are high, and personal choice of plans and benefits is limited or nonexistent.[6] Small firms are among the least suitable vehicles for implementing a serious expansion of health insurance.
- **It reinforces flaws in the current system that spur patient dissatisfaction**. The proposal preserves the outdated federal tax policies that govern today's employer-based health insurance system. Such policies frustrate patient choice and genuine market competition by distorting health insurance markets, driving up health care costs, and encouraging a steady erosion of patient control.
- **It promotes a significant expansion of Medicaid.** Under this proposal, most low-income people would be consigned to Medicaid, the federal–state program that currently provides coverage for poor and indigent citizens. Most working people do not want to be in Medicaid for the simple reason that it provides inferior health care coverage; but the incentives embodied in the Common Ground proposal, as well as the compliance burden connected with the administration of its tax credit component, could encourage firms with a disproportionately large number of lower-income employees to cease offering health insurance. The likely result: further contraction of the private health care market as many of these workers and their families enroll in Medicaid, their only option.
- **It would lay the groundwork for greater government control of health care.** Government accounts for almost half of all direct spending on health care in the United States, largely through Medicare and Medicaid. By significantly expanding Medicaid and consolidating, to the extent practical, employer and insurance industry restrictions on health care decisions, the proposal would increase government's role in the health care system. As evidenced by the

5. The provision adopted by both the House and Senate is included in H. Con. Res. 83, the Concurrent Resolution Establishing the Congressional Budget for the United States Government. The $28 billion set-aside was based on a proposal offered by Senators Gordon Smith (R–OR) and Ron Wyden (D–OR). For an account of its adoption, see Julie Rovner, "Conferees Resolve Their Differences on Uninsured Plan," *Congress Daily*, May 3, 2001.
6. For a comparison of the strengths and weaknesses of large and small firms in offering health insurance, see Stuart M. Butler, Ph.D., "How Health Tax Credits for Families Would Supplement Employment-Based Coverage," Heritage Foundation *Backgrounder* No. 1420, March 16, 2001, pp. 2–5.

> continuing debate over "patient's bill of rights" proposals, employer restrictions on patient choices invite further government intervention in and regulation of health plan operations. Moreover, if the employer tax credit turns out to be unworkable, the next step is likely to be even more generous government subsidies to employers along with a mandate that they provide insurance. Government mandates for health insurance invariably require standardization of benefits, with government bureaucrats specifying what treatments or procedures will be included in the package.

It is hard to see how the political dynamics set in motion by this proposal would lead to anything resembling free markets or a more modest level of consumer choice and competition in the existing system. As recent surveys show, small businesses overwhelmingly support a system of individual tax credits that go directly to individuals and families, rather than a business tax credit that increases their paperwork and administrative burdens.[7]

**The President's Alternative.** In sharp contrast to the Common Ground proposal, President George W. Bush would design a system that addresses the problem of uninsurance with individual refundable tax credits. As the President explains,

> My budget puts a priority on access to health care without telling Americans what doctors they have to see or what coverage they must choose. Many working Americans do not have health care coverage, so we will help them buy their own insurance with refundable tax credits.[8]

On this issue, the President is building on genuine bipartisan political consensus that the profound inequities in the current tax treatment of employer-based health insurance contribute to uninsurance. There is broad recognition that the primary remedy would be to channel tax relief for the purchase of insurance directly to individuals and families, not simply to their employers. During the 106th Congress, for example, Members from both political parties sponsored several major individual tax credit proposals. Within the broader health care policy community, there is a similarly strong bipartisan agreement that tax relief for individuals is the better approach.[9]

Congress should build on this consensus. To address the problem of the uninsured, it should:

- **Create a system of refundable tax credits to expand health coverage.** Providing individual tax relief for insurance would help millions of Americans who need coverage. It would enable individuals to choose the kinds of plans, benefits, and doctors that best suit their families' needs. It would promote personal control and ownership of insurance policies, including policies sponsored by associations or fraternal and faith-based organizations. And it would reduce or eliminate the distortions and inequities in the current health insurance market, particularly those created by the federal tax treatment of health insurance.

7. See Steven Brostoff, "Small Employers Support Tax Credit for Health Insurance: NAHU Survey," *National Underwriter Life and Health–Financial Services*, Vol. 105, No. 13 (March 26, 2001).
8. President George W. Bush, "Address to the Nation," February 27, 2001.
9. For an extensive treatment of the relationships between health care and tax policy, see Grace-Marie Arnett, ed., *Empowering Health Care Consumers Through Tax Reform* (Ann Arbor: University of Michigan Press, 1999). Beyond The Heritage Foundation and various professional associations such as the American Medical Association and the National Health Underwriters Association, supporters of individual tax credits to reduce the number of uninsured include analysts from the American Enterprise Institute; the Center for Strategic and International Studies; the Galen Institute; the Progressive Policy Institute (research arm of the Democratic Leadership Council); the Urban Institute; and the National Center for Policy Analysis. Regardless of other ideological or political differences, there is firm agreement among this broad spectrum of analysts that every American family should be able to benefit from direct tax relief for the purchase of health insurance, including relief through refundable tax credits.

- **Allow S–CHIP funds to be used for tax credits and vouchers for the purchase of private health insurance.** States can obtain federal funds to finance expansions of their Medicaid programs to cover uninsured children, but legislative report language accompanying the S–CHIP provisions of the Balanced Budget Act of 1997 encourages them to explore "innovative means" to expand coverage. This would include the use of tax credits and vouchers to extend coverage to children.[10]
- **Reject incremental steps that lead to an increase in government or even employer control over health care decisions.** Most Americans, with the assistance of their doctors, want more personal control over sensitive health care decisions, not less control. The debate over a "patient's bill of rights" is largely attributable to the continuing frustration of Americans who have little or no choice over their plans and benefits.

If Members of Congress want to build on the growing bipartisan consensus on health care policy, they should pursue policies that give tax relief to individuals and families for the purchase of health insurance.

## THE COMMON GROUND PROPOSAL

The agreement between the Health Insurance Association of America and Families USA proposes a major expansion of government health programs. The three primary elements of this Common Ground proposal are:

1. **A major expansion of Medicaid.** Medicaid is a joint federal–state welfare program that is designed to provide health care coverage to the poor and indigent. Beyond basic federal guidelines, eligibility for the program, which currently costs more than $200 billion a year, is determined by the states. Of the estimated 34 million persons covered by Medicaid, 18 million are children.

   Under the Common Ground proposal, Medicaid would be expanded to cover all persons with annual incomes below 133 percent of the official federal poverty line, or about $18,820 for a family of three.[11] In a departure from current eligibility rules, it would base eligibility for Medicaid solely on a person's income; it would apply to parents, children, or childless adults. Proponents have not supplied a numerical estimate of how many people would be added to the program by this provision, but the number would undoubtedly be large. To guarantee funding for the states, Medicaid federal matching funds would be increased to "well in excess" of the level provided under the current funding formula.[12] Funding would be phased in over time.

2. **Expansion of S–CHIP coverage to adults.** One of the Clinton Administration's most significant health care initiatives was the State Children's Health Insurance Program (S–CHIP), a $24 billion program focused on uninsured children. Created in 1997, S–CHIP today provides health care coverage for 2.2 million children. Many states provide this coverage through their Medicaid programs.

   Under the Common Ground proposal, states at their discretion could expand S–CHIP or Medicaid to cover all adults, without exception, with incomes between 133 percent and 200 percent of the federal poverty line.[13] States already can offer such coverage to children under S–CHIP; the proposal would expand that coverage to adults. Because many states are using Medicaid already to provide S–CHIP coverage, eligibility for adults based on income

10. Under this legislation, a state could set up a tax credit option in its employee health plan, which could serve as a "benchmark" plan for offering similar coverage under S–CHIP. In 1997, Congress authorized a total of $24 billion for the program over five years.
11. Kahn and Pollack, "Building a Consensus for Expanding Health Coverage," p. 6.
12. *Ibid.*
13. *Ibid.*

would promote another large Medicaid expansion. The expansion of eligibility would be matched by an increased federal contribution to either program. Representatives William M. Thomas (R–CA), Chairman of the House Ways and Means Committee, and Jim McCrery (R–LA) report that the Common Ground proposal would increase the total number of Americans covered by Medicaid by 50 percent and add another $25 billion per year to the Medicaid budget.[14]

3. **Additional health insurance tax breaks for businesses.** Federal law provides unlimited tax relief for both workers and companies that provide health insurance. For workers, the tax break is in the form of an exclusion of employer-paid benefits from taxable compensation; for employers, it is a tax deduction of health insurance benefits as a cost of doing business.

   The Common Ground proposal would create a new tax break in the form of tax credits for employers, not employees. Any firm that pays a larger share of the premium for workers with incomes between 133 percent and 200 percent of the federal poverty level than it pays for other employees would get a non-refundable tax credit. Federal poverty determinations are based on family income. According to the authors of the Common Ground proposal, a business that pays 70 percent of premiums for all workers and decides to pay all or part of the remaining 30 percent for low-income workers would receive a tax credit for that additional amount. Specifically,

   > The employer tax credit would be available only to companies that make contributions to their health plans commensurate with the contribution levels of similarly situated employers. To ensure that this facet of our proposal strengthens existing coverage, the legislation would seek to secure, not weaken, current employer coverage and contributions that workers receive through their jobs.[15]

## WHY "COMMON GROUND" IS BAD HEALTH POLICY

The initial support for the Common Ground proposal stems from the desire of most policymakers to reduce the number of uninsured Americans. Today, roughly 43 million Americans lack health coverage at any given time, depending on how they are enumerated.[16]

While there is nearly universal agreement on the need to reduce sharply the number of the uninsured, and while many proposals before Congress are designed to do so, the Common Ground proposal is not the right approach. Among the many reasons:

1. **It would impose unworkable and inappropriate requirements on employers.** Any employer who wants to receive the tax credit would have to take on the added responsibility of investigating and verifying an employee's family income to see whether it meets the eligibility requirements. This is the only way to make sure that the firm qualifies to collect the credit. It is, of course, quite conceivable that an employee could have a wage rate that equals an income that falls between 133 percent and 200 percent of poverty but an overall family income that is above or below the income eligibility range.

   For the tax credit option to be efficient, employers would have to make sure that the

14. Representatives William M. Thomas and Jim McCrery, "Give Individuals the Resources to Choose," "Dear Colleague" letter, U.S. House of Representatives, December 1, 2000.
15. Kahn and Pollack, "Building a Consensus for Expanding Health Coverage," p. 7.
16. There is solid evidence that the official Census Bureau figure is inflated. For example, in a December 1999 presentation to congressional staff at a seminar hosted by The Heritage Foundation in Annapolis, Maryland, the Lewin Group noted that too many American citizens covered by Medicaid are included erroneously in the official Census number of the uninsured. The actual number of the uninsured is still lower if one controls for illegal aliens.

"right" persons were being insured: that they were, in other words, eligible for coverage. Employers would have to match income with eligibility standards by undertaking an accurate collection of family income data in order to comply with the tax credit requirements. This raises both administrative and new privacy concerns. Presumably, employers would also want to make doubly sure that their determinations of eligibility are correct to avoid unpleasant audits by the Internal Revenue Service.

The idea of promoting insurance coverage through public subsidies to small employers is not new. In recent years, several states have tried to subsidize employer-sponsored insurance to expand coverage for children under S–CHIP. In a recent study of these state efforts conducted for the Academy for Health Services Research and Health Policy, Linda Schofield, a health policy research consultant to the Academy, observes that

> The common commitment among these states to leverage private sector funds through ESI (employer sponsored insurance) was matched in each state by a high degree of cooperation and enthusiasm amongst employers. Unfortunately, the bottom line results of these efforts, to reduce the numbers of uninsured children through an eminently and widely politically embraced public private partnership approach, have been discouraging.[17]

Perhaps even more directly relevant to the infrastructure created under the Common Ground proposal is the experience of the Kansas Business Health Partnership. Created under a new Kansas law, the program is another example of efforts to broaden coverage through government subsidies to employers. But the Kansas project is burdened with practical infirmities, including a reluctance on the part of small firms to take on the added responsibilities of participating in the effort and the added problem of how to make sure that government funds reach the right employees. As noted in a recent report on the Kansas initiative in *The Wall Street Journal*, "Another challenge is to avoid paying subsidies to businesses and their workers who are already insured and don't qualify for help under the program rules."[18]

The authors of the Common Ground proposal conspicuously ignore what small employers *do* want in health care tax credit policy: for their employees to have health insurance coverage and for that coverage to be extended through a new system of individual tax credits that go directly to the workers and their families. According to a recent survey sponsored by the National Association of Health Underwriters,

- 84 percent of small employers support a tax credit to help lower-income employees buy employer-sponsored health insurance;
- 76 percent support an individual tax credit without regard to whether it would be applicable to employer-sponsored coverage; and
- 71 percent said they would cooperate in the administration of a program of individual tax credits for the purchase of employer-sponsored coverage.[19]

Many small employers realize, of course, that they do not enjoy the economies of scale or the efficiency of administration that are routinely taken for granted by large employers who offer health insurance coverage to large numbers of employees.

17. Academy for Health Services Research and Health Policy, *Employer Buy-in Programs: How Four States Subsidize Employer-Sponsored Insurance*, March 2001, p. 1, at *http://www.academyhealth.org*.

18. Rundle and Murray, "The Have-Nots."

19. Brostoff, "Small Employers Support Tax Credit for Health Insurance."

2. **It would move more Americans into Medicaid instead of getting more Americans off Medicaid and into private health insurance.** Advocates of the Common Ground proposal clearly believe that building on existing structures, including employment-based health insurance and government health programs, is a reasonable way to reduce the large number of uninsured. S–CHIP, for example, is popular with governors and with bipartisan majorities in Congress. Though it rarely gets the kind of attention from federal policymakers that is routinely showered on the Medicare program, Medicaid is popular among liberal policy analysts who appreciate its potential for expanding government's role in health care, or who believe that Medicaid or Medicaid-managed care is a sound program for dealing with the health care problems of poor people.

   The authors of the Common Ground proposal employ positive rhetoric about the possibilities of expanding Medicaid coverage but overlook the profound shortcomings of Medicaid as a health care delivery system. Medicaid, a welfare program, is a programmatic mess. In 23 states, Medicaid budgets are currently "out of balance."[20] The program has huge and growing costs; it delivers poor quality care; and doctors and hospitals do not like having to deal with the Medicaid bureaucracies at the federal and state levels to obtain reimbursement under the program's low reimbursement rates. These rates, of course, affect access to care; the government, by setting them at its own discretion, would be determining how much and what quality of care the newly enrolled millions would get. Price controls impose costs on consumers.

   There is solid evidence that, compared with those enrolled in private health insurance, Medicaid patients have a more difficult time getting the services they need when they need them.[21] Today, if given the opportunity, not many Americans would drop private health insurance to sign up voluntarily for Medicaid. Nonetheless, in sharp contrast to a progressive system of refundable tax credits as proposed by President Bush and leading Members of Congress in both political parties, the Common Ground approach would close off reasonable options for private health insurance for such lower-income Americans and lock them into the Medicaid program. Thus, these Americans would be denied choice, flexibility, and variety in their health plan offerings—the very features that would accompany an individual tax credit approach.

   Enrolling more Americans in solid private health insurance is clearly preferable to increasing the Medicaid rolls. Under the Common Ground proposal, however, there literally would be no way out for individuals and families forced into Medicaid. As Representatives Thomas and McCrery observe,

   > Instead of empowering individuals with the wherewithal to choose the health plan that best suits their needs, it empowers others—employers and HCFA [the Health Care Financing Administration] and state governments—to make these choices for them.[22]

   A good health policy would get more Americans out of Medicaid and into superior private

20. For a discussion of this Medicaid resource problem and related matters, see National Health Policy Forum, "Perspectives on the Financial Underpinnings of the Health Care Safety Net: No Margin, No Mission," *Forum Session*, George Washington University, June 2001, p. 2. The original citation for Medicaid's budgetary problems in the states is from Pamela Belluck, "Free Spending in Flush Times Is Coming Back to Haunt States," *The New York Times*, March 9, 2001, p. A14.
21. See, for example, Medicaid Access Study Group, "Access of Medicaid Recipients to Outpatient Care," *The New England Journal of Medicine*, Vol. 330, No. 20 (May 19, 1994), pp. 1426–1430; see also Robert W. Derlet, M.D., and Donna Kinser, M.D., correspondence, *The New England Journal of Medicine,* Vol. 331, No. 13 (September 29, 1994), pp. 877–878.
22. Thomas and McCrery, "Dear Colleague" letter.

health insurance. The Common Ground proposal would do exactly the opposite.

3. **It would further contract the private health insurance market by encouraging employers to drop coverage for workers who qualify for the expanded Medicaid program.** The private health insurance market would become smaller and less involved in what is supposed to be one of its primary functions: the management of insurance risk. The Common Ground proposal would discourage, not encourage, expanded coverage through the private sector. A major reason: If an entire class of Americans is automatically eligible for coverage under a government welfare program, there is less incentive for employers to cover them and incur the burden of compliance even in exchange for the tax credit. An employer with a workforce that is disproportionately made up of low-income employees will have even less incentive to continue coverage.

   The authors of the Common Ground proposal anticipated this problem. They argue that

   > For all aspects of the proposal, the substitution of taxpayer funds for coverage already provided through private spending ("crowding out") must be minimized. Since crowding out occurs more frequently among higher income populations, it is best to first focus expansion efforts on those with incomes below 200 percent of the federal poverty level.[23]

   Curiously, the authors of the Common Ground proposal seem to discount the problem of crowding out for lower-income persons with private health insurance. Consider the case of children under the age of 19 in households with incomes below 200 percent of the federal poverty level. According to data compiled by health policy analysts with the American Association of Retired Persons (AARP), the nation's largest senior citizens organization, 56.7 percent of such children in Utah are covered under employer-based plans. In South Dakota, it is 44.5 percent; in Maine, 43.3 percent; and in the District of Columbia, which ranks dead last with employer-based insurance coverage for such children, 20.7 percent are covered by employer-based plans.[24]

   Based on studies of previous Medicaid expansions, there is solid reason to believe that the Common Ground proposal would have similar consequences: a crowding out of private coverage. For example, David Cutler of Harvard University and Jonathan Gruber of the Massachusetts Institute of Technology found that Medicaid expansions accompanied a 15 percent reduction in private insurance between 1987 and 1992.[25] Similarly, Lisa Dubay and Genevieve Kenney of the Urban Institute found that Medicaid expansions for persons under the poverty line had little appreciable effect on employer-based coverage; but for pregnant women with incomes between 100 percent and 185 percent of poverty, Medicaid expansions correlated with a significant decline in private employer-based coverage.[26]

23. Kahn and Pollack, "Building a Consensus for Expanding Health Coverage," p. 4.
24. See American Association of Retired Persons, *Reforming The Health Care System: State Profiles 1999* (Washington D.C.: AARP Public Policy Institute, 1999). The percentages are based on 1995–1997 data. Comparatively, in Utah, South Dakota, and Maine, respectively, 14.9 percent, 24 percent, and 21.1 percent of these lower-income children are on Medicaid; in the District of Columbia, which ranks first in the nation in Medicaid coverage for children in this category, the number is 55.2 percent. Potentially, the chief effect of the Common Ground proposal would be to enable the rest of America to "catch up" with the District of Columbia.
25. David Cutler and Jonathan Gruber, "Medicaid and Private Insurance: Evidence and Implications," *Health Affairs*, January/February 1997, pp. 196–198.
26. Cited in Rick Curtis and Ann Page, "Improving Health Care Coverage for Low Income Children and Pregnant Women: Public and Employer Financed Coverage Relations," *Solutions*, Institute for Health Policy, December 17, 1996, p. 10.

The Common Ground proposal would push Medicaid's already high health care costs even higher, forcing taxpayers to pick up the increasingly larger bill. Given the incentives embodied in the proposal, its likely effect would be to sharpen segmentation of the working population based on income and, possibly, health status. In recent years, tight labor markets, among other things, have slowed the trend toward higher cost-sharing among workers enrolled in employer-based plans. With sharp premium increases in employer-based insurance, that is likely to change. Private insurance for employees who could afford the expected higher cost-sharing that accompanies employment-based coverage could retain coverage, while the same level of cost-sharing would discourage low-income employees from enrolling. As a result, more lower-income employees would end up in Medicaid at taxpayer expense.

4. **It would preserve outdated relations between consumers and insurance companies at the expense of consumer control.** The authors of the Common Ground proposal correctly point out that low-income persons often have difficulty purchasing private health insurance in today's insurance market. They also correctly point out that, to an overwhelming extent, privately insured Americans get their health care coverage through the place of work and that Americans who enjoy such coverage feel "comfortable" with it.

This is largely true, but this line of argument overlooks the nature of the dissatisfaction with current health insurance arrangements, now firmly dominated by bureaucratic managed care plans.[27] This serious dissatisfaction, particularly the unease caused by the loss of control by both doctors and patients, sparked intense congressional interest in legislation establishing a "patient's bill of rights" characterized by a quantum leap in direct federal regulation of health insurance markets in the states, as well as broader avenues for litigation over health benefits. Much of this popular dissatisfaction is rooted in the absence of patient choice. Existing professional literature on the subject strongly suggests a positive relationship between patient satisfaction and patient choice of plans.[28] Moreover, as officials of the American Medical Association observe, most employees who change plans today do so involuntarily and have to find a new doctor, and only 17 percent of all employment-based insurance arrangements allow employees to choose plans.[29] Only two out of five working adults have a choice of two or more plans.[30]

With the right policy, Congress can set in motion the dynamics of choice and competition. With a new system of individual tax cred-

27. For example, some recent polling results compiled by *The Wall Street Journal*, based on surveys conducted by the Harris organization and the Henry J. Kaiser Family Foundation/Harvard School of Public Health, reveal that 63 percent of respondents believe HMOs and other managed care plans make it harder for the sick to see specialists. In terms of overall satisfaction, during 2000, only 14 percent of respondents said that the health care system works pretty well and only minor changes are necessary; but 53 percent said that fundamental changes are necessary, and 29 percent responded that policymakers need to rebuild it completely. See "Can the System Be Fixed?" Special Report on Medicine and Health, *The Wall Street Journal*, February 21, 2001, p. R3.

28. For an excellent account of the relationship between patient choice and satisfaction, see Karen Davis and Cathy Schoen, "Managed Care, Choice and Patient Satisfaction," The Commonwealth Fund, August 1997, at *http://www.cmwf.org/programs/health-care/satis.asp* (accessed May 22, 2001). The authors found that employees with a choice of health plans are "less likely" to report dissatisfaction with their plans, with the physicians in their plans, or with the care they received in their plans.

29. American Medical Association, *Choosing Health Insurance that Best Meets Your Needs: A Proposal from the AMA* (American Medical Association Health Policy Group, 1999), pp. 1–2.

30. Karen Davis, "Employees Lack Options Among Health Plans," *Briefing Note*, The Commonwealth Foundation, August 1997, p. 1.

its—preferably refundable tax credits—not only would policymakers secure more reliable financing, but they would encourage long-term health insurance contracts between health plans and consumers, thus reducing churning in the market and helping to stabilize premiums. Since the consumer, under an individual tax credit system, is also a directly paying customer, insurance companies would also have a powerful interest in retaining the relationship.

5. **It would preserve outdated and inefficient insurance pooling arrangements.** The authors of the Common Ground proposal also overgeneralize about the efficiencies of employment group purchasing and the contributions of these purchasing and pooling arrangements to the affordability of health insurance.[31] Large employer-based insurance arrangements work very well in this respect; smaller companies do much less well because their pools are, by definition, artificially small. When one employee gets seriously sick, the premium rates for the small group soar.

   One of the advantages of an individual tax credit approach to the problem of the uninsured is that it can contribute to the creation of very large national pools. Large pools, coupled with expanded coverage of mostly younger and healthier uninsured populations, would exert a downward pressure on average claims costs. As Norman Ture and Stephen Entin, economists with the Institute for Research on the Economics of Taxation, have observed,

   > Large individual-based pools would make it possible for private insurers to handle people with higher risk factors than at present. The pools would contain enough such people to make their claims conform closely to the national average for people with those risk characteristics and would enable the company to charge an actuarially fair risk premium without fear of exposure to an extraordinary level of claims. Consequently, some people currently classified as uninsurable would be insurable in a broader risk pool.[32]

6. **It would lay the groundwork for even greater government control of America's health care system.** Although the Common Ground proposal undoubtedly would reduce the number of uninsured, it would also significantly advance government control of the health care system. By reinforcing the current federal and state tax treatment of employer-based health coverage, it would allow insurance companies, managed care networks, or employers to remain the key decisionmakers in determining the benefits available to workers and their families. What kinds of plans, benefits, doctors, or medical treatments are available, and how and under what circumstances providers will be reimbursed, are major questions and involve decisions that usually are made at only one decision point: the contractual agreement between employers, as purchasers of insurance, and their agents, the health insurance executives. This type of arrangement, in which the decision points are clearly and tightly confined, makes it supremely easy for government officials to regulate and control this sector of the economy. In fact, it is why the health care sector is already one of the most highly regulated sectors of American economic life. Patients, as consumers of the services, are not and cannot be the key decisionmakers in such an arrangement.

   The Common Ground approach would exacerbate this loss of patient control over health care decisions and the concomitant growth of government power in the system. Today, roughly half of all health care spending in the United

31. Kahn and Pollack, "Building a Consensus for Expanding Health Coverage," p. 3.

32. Norman B. Ture and Stephen Entin, "Health Care Reform: Why Not Try Real Insurance?" in Arnett, *Empowering Health Care Consumers Through Tax Reform*, p. 128.

States is directly attributable to government, particularly large government-run programs such as Medicare, Medicaid, and public health programs. If more and more lower-income individuals automatically become eligible for Medicaid coverage, the government share of the health care sector of the economy will increase significantly. Perhaps more than any other group of Americans, Medicaid patients are dependent on the policy decisions of government officials. As a practical matter, they have little or no recourse if they do not get the benefits they need or the quality of care they deserve. Nor can they sue government officials for those benefits, even when they are denied benefits formally "guaranteed" under Medicaid law.[33]

Under the Common Ground proposal, health insurance companies would have an opportunity to benefit from new contracts with employers that seek the tax credit. But they would also be retreating from the historic opportunity to cover millions of Americans through a superior system of individual tax credits in a market characterized by consumer choice and competition. Worse, they most likely would find themselves operating in an even more heavily regulated environment.

For employers that wish to take advantage of the short-term benefits of tax breaks for covering the uninsured, there will be new administrative burdens. Within this new regulatory environment, partially sweetened by a new business tax credit, it will be even more difficult for employers to resist the reintroduction of employer mandates to purchase health insurance coverage for employees. That was the core financing component of the failed 1993 Clinton health plan that small employers resisted so stoutly.

Longtime advocates of national health insurance understand the politically appealing aspects of the Common Ground proposal. For example, AFL–CIO President John Sweeney hails the agreement as an "important step" toward "building consensus" on federal policies to deal with the problem of those who are without insurance, and Senator Edward Kennedy (D–MA) praises the Common Ground proposal as an indication that "bipartisan cooperation" on this issue is possible.[34] From a public relations standpoint, the agreement between HIAA and Families USA is a politically attractive alliance of industry executives and a top liberal health care lobbying organization. Regardless of the public relations attractiveness of this tactical alliance, however, the strategic consequence of the joint effort will be a significant increase in government control of the health care sector of the economy.

7. **It would undercut real, comprehensive, market-based health care reform designed to expand consumer choice and private competition.** As noted above, a broad-based intellectual consensus has developed among economists, political scientists, and health policy analysts—liberals and conservatives alike—that the central problem with the America's health insurance market is the federal tax treatment of health insurance.

   The current tax treatment of health insurance confines Americans almost exclusively to employer-based health insurance. It under-

33. This has been reaffirmed in a recent federal court case, *Westside Mothers* v. *Haveman* (2001), in which U.S. District Court Judge Robert H. Cleland ruled that Medicaid patients may not sue state officials to force them to provide medical benefits "guaranteed" under Medicaid law. For an account of the far-reaching significance of this case, see Robert Pear, "Ruling in Michigan Bars Suits Against State Over Medicaid," *The New York Times*, May 13, 2001, at *http://www.nytimes.com/2001/05/13/national/13MEDI.html?searchpv=day01* (accessed May 21, 2001).

34. Senator Kennedy, for example, is described in *The Wall Street Journal* as a "diehard health reformer." But he is a "convert" to the cause of "incrementalism": "'His goal remains comprehensive health insurance reform, but in the current political reality, he decided that this step by step approach is the best way to achieve that,' says Jim Manley, Senator Kennedy's spokesman." Rundle and Murray, "The Have-Nots."

mines portability, consumer choice, and competition; it hides the true cost of health care; and it is dramatically regressive as tax policy: Low-income people get literally nothing; the tax breaks are heavily tilted toward the upper end of the income scale. Hardly any arrangement could be more discouraging to the expansion of private health insurance coverage. Congress should not reinforce this system. It should look for ways to develop a parallel system of tax treatment of health insurance, at the very least for persons who do not or cannot get health insurance outside of the place of work. Such a system should be based on refundable individual tax credits.

## THE BETTER APPROACH TO HEALTH POLICY REFORM

Members of Congress, working with the Bush Administration, have an historic opportunity to change the terms of the national health care debate, reverse the dynamics of the health care policy, reduce the numbers of uninsured, and put more direct control of health care decisionmaking into the hands of individuals and families. Specifically, they can:

1. **Create a system of refundable tax credits to expand health coverage.** President George W. Bush and a growing number of Senators and Representatives of both parties agree on the need to provide tax incentives—in the form of tax credits or subsidies—for Americans who do not have health insurance through the place of work to buy their own coverage. They are proposing a variety of plans with different levels of subsidies for individual and family coverage. For example, Representatives Richard Armey (R–TX) and William Lipinski (D–IL) are sponsoring the Fair Care for the Uninsured Act of 2001 (H.R. 1331), with tax credits of $1,000 per person up to $3,000 per family; Representative Nancy Johnson (R–CT) is sponsoring the Health Insurance Affordability and Equity Act (H.R. 1181), which would provide a tax credit of $1,500 per person and $3,000 per family; and Senator James Jeffords (I–VT) is sponsoring a bill (S. 590) to provide $1,000 for an individual and $2,500 for a family, with lesser amounts for employees already enrolled in an employer subsidized plan. Tax credits, depending on their structure, can make coverage affordable for millions of Americans.[35]

   The objective of such a policy initiative is not just to broaden access to coverage or to expand insurance coverage, but also to expand personal freedom and give people a real choice of options in an open and competitive market. Such a system, grounded in patient satisfaction, would reward high-quality health care services and reimburse doctors, hospitals, and other providers for providing better value for consumers' dollars.

   There is a genuine and broad consensus on this policy objective, and a rich diversity of alternatives on how to achieve it. While most analysts agree that to be effective, tax credits or subsidies should target low-income persons, the structure of these credits could vary.

   - Tax credits could be fixed or vary with income or health care costs or health risk.
   - Tax credits could be combined with new health insurance arrangements that are designed to minimize the problems of risk selection, such as large risk insurance pools or innovative reinsurance arrangements.
   - Tax credits could also be combined with employment-based insurance or association plans; employers could serve as brokers of insurance options in competing pools or as agents to sign up workers and their families for competing plans.[36]

35. On tax credits and the affordability of health insurance, see James Frogue, "Recent Survey Points to Affordable Individual Health Insurance," Heritage Foundation *Executive Memorandum* No. 740, April 17, 2001.

36. See Butler, "How Health Tax Credits for Families Would Supplement Employment-Based Coverage."

Not only would there be greater efficiencies, driven by consumer demand, in a market in which individuals and families make the key decisions over cost and coverage, but there would also be a superior system of health care delivery in which the watchwords would be quality and patient satisfaction.

2. **Allow S–CHIP funds to be used for individual tax credits.** As part of the Balanced Budget Act of 1997, Congress authorized the creation of the $24 billion State Children's Health Insurance Program (S–CHIP) to expand insurance coverage for millions of children not covered by health insurance. The conventional approach of state officials has been simply to enroll eligible children in the troubled Medicaid program; but the authors of the S–CHIP legislation, in their conference report language, encouraged state policymakers to use S–CHIP funds for tax credits or vouchers for the purchase of insurance.[37] HCFA, under the Clinton Administration, did not encourage such tax credit options, and developing an ambitious tax credit program under S–CHIP still presents some technical difficulties. That said, however, there is no reason why the Bush Administration cannot encourage such state policies and press for remedial legislation to facilitate an expansion of that option for innovative state officials.

3. **Reject any incremental step that leads to an increase in government or even employer control of health care decisions.** Most Americans, with the assistance of their doctors, want to make their own sensitive health care decisions. The frustration of individuals and families who have little or no choice of plans or benefits in the employment-based system is largely feeding the debate over a "patient's bill of rights." Unfortunately, Congress has refused to address this central issue.

The Common Ground proposal is the latest in a series of health care initiatives since the ill-fated Clinton plan of 1993 that have been designed to concentrate decisionmaking in the hands of government officials. Many of the Clinton plan's strongest advocates have adopted an "incremental" approach to achieve their objective, and the legislative process has achieved tiresome predictability: After all-night negotiations, Members produce huge bills packed with impenetrable provisions on the finer points of health policy that virtually no one reads before they go to the floor for a vote. Press releases are issued praising how the bills resolve or improve some flaw in the current system. But any honest reading of the fine print shows that the consequences of their incremental "reforms" will be to make the health care system more controlled, managed, or run by government, accompanied by major increases in health care costs, regulation, and paperwork. Congress and the Administration can break this cycle.

## CONCLUSION

For congressional liberals favoring government-run health care and shortsighted health insurance executives, the Common Ground proposal is mutually beneficial. The former would get a major Medicaid expansion, which takes another giant step toward their objective: a single-payer system of national health insurance. And not only would more health care coverage be under direct government control, but insurance executives would enter fresh contracts and avoid the risk management associated with low-income populations.

But the Common Ground transaction also has losers: American taxpayers, individuals and families, the people who could benefit from an alternative health policy that would expand private coverage with refundable tax credits for the purchase of private health insurance. America's health

37. For an explanation of how this can be accomplished at the state level, see James Frogue, "How Governors Can Help Children Get Private Health Insurance," Heritage Foundation *Executive Memorandum* No. 591, April 27, 1999; see also Carrie J. Gavora, "Kidcare Implementation: A Helpful Guide for the States," Heritage Foundation *F.Y.I.* No. 168, December 31, 1997.

care system is not static; it is constantly and rapidly evolving, and different policy decisions governing the system have different dynamics. Therefore, every specific health proposal should be judged against the overall objective: a quality health care system that all Americans deserve based on personal choice and market competition. The question for Congress is whether to provide Americans with a system that is controlled by government officials or one that is controlled by individuals and families as consumers and patients. Specific policy proposals invariably will move in one direction or the other.

The President and Congress can make a strong case for personal freedom. Instead of locking Americans into outdated and restrictive third-party systems, President Bush and Members of Congress can adopt an approach that parallels the current employment-based system by channeling tax breaks directly to individuals and families who lack health insurance, giving them the freedom to make the key decisions. Such an approach, giving assistance directly to those who need help the most, would change America's health care system for the better; but the key to reform is changing the current tax treatment of health insurance.

Most of the key components of the Common Ground proposal are a novel reconfiguration of old policy recommendations for changing the existing framework. If enacted into law, the proposal's policies might expand employment-based coverage of the uninsured, but only if enough employers think it is worth the effort to obtain the new tax credit. Regardless of what private companies do, however, government-subsidized health care would expand, and an already ailing private health insurance market would contract even further and aggravate the problems that plague today's system, including the steady erosion of control by patients over the most sensitive decisions affecting their lives. Congress and the Bush Administration can do much better.

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