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Beyond SCHIP: A Serious Proposal to Reduce Uninsurance

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The Senate debate on SCHIP reauthorization is, in fact, a debate on the future direction of health care policy. In one direction is greater government control over the financing and delivery of medical care; in the other is greater personal freedom for individuals and families that empowers them to choose the health care options that they want and trust. Leading the way toward freedom are the five senators—Richard Burr (R–NC), Bob Corker (R–TN), Tom Coburn (R–OK), Elizabeth Dole (R–NC), and Mel Martinez (R–FL)—who are sponsors of the Every American Insured Health Act (S. 1886). This bold and innovative proposal would reduce the number of uninsured by an estimated 24 million by eliminating the unfairness of the federal tax treatment for health insurance, providing tax relief for individuals and families in a budget-neutral fashion and promoting reform of state health insurance markets to make coverage more affordable. Though a revolutionary break from the status quo, the legislation embodies an approach to reform that has been vigorously championed for decades by prominent health care economists and policy analysts, liberal and conservative alike.

The Two Pillars of Comprehensive Reform. The Senate reform proposal has two main components; they are distinct but inseparable means of expanding patient choice and encouraging robust competition in the sector of the American economy where it is most conspicuously lacking.

1. Replacement of the Current Tax Regime with a National Health Care Tax Credit. The bill would replace the existing tax exclusion for health insurance with a national system of health care tax credits. This is an entirely new tax policy, and working Americans and their families would be treated equally for the purpose of securing health insurance coverage.[1] Individuals and families would receive a standard tax credit to purchase health insurance: $2,160 for an individual and $5,400 for a family.[2] For low-income individuals and families, the credit would be refundable, meaning that these persons would receive the credit whether or not they file income taxes. Employers would still be able to deduct the provision of health insurance for employees as a regular cost of doing business, as they do today. Because the national tax credit program would replace the existing employee tax exclusion for health insurance, the Senate sponsors say that the legislation would be budget neutral over 10 years.

The existing federal tax regime for health care ties favorable tax benefits for the purchase of health insurance almost exclusively to the place of work, making access to coverage an accident of employment. The professional literature—as well as independent academic and government studies—on the deficiencies of the current system is voluminous: It undermines

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portability of coverage; it fuels health care inflation; it distorts the health insurance markets; it is inequitable and profoundly regressive; and it undercuts the free market forces of consumer choice and competition in the health care system.[3] That is why there has been growing bipartisan support for a tax credit strategy to reduce the number of uninsured.[4]

There is no effective way to resolve these many problems short of overhauling federal tax treatment of health care while providing help to low-income persons to enter the private market. As Professor Regina Herzlinger of the Harvard Business School has explained:

> The academic health policy wonks and Beltway crowd will hold press conferences and write papers about tax neutrality, and interest groups will lobby to gain some tax advantage. But the debate boils down to two approaches: a tax deduction or a tax credit for my expenditures. The only difference between the two approaches is that the deduction is worth more to someone who is in a high tax bracket, while the value of the tax credit is independent of the tax bracket. [5]

The cost of health insurance varies radically from state to state and largely reflects the underlying costs of health care in the state. Under the Burr bill, in the event that an individual or family buys a health insurance plan that costs less than the value of the credit, the difference would be deposited into the individual's tax free health spending account, such as an HSA or an MSA.

2. State Health Insurance Market Reform. States regulate health insurance markets, and these markets are often dysfunctional. They are balkanized under special interest-driven law and complex regulations, with distinct sets of rules governing separate individual and group markets; they are increasingly uncompetitive, largely as the result of the relentless growth of oligopolistic concentrations of market power by a few geographically dominant insurance carriers; and they are over-regulated, overburdened by complex and costly insurance rules and, according to the Council for Affordable Insurance, more than 1,800 specific provider and benefit mandates nationwide.

Unlike other Senate proposals, the Burr bill would not displace existing state regulation or impose yet another layer of federal regulation on top of existing state regulation. Rather, the bill would create new incentives for state officials to reform their health insurance markets and make health insurance more affordable and flexible. The bill would accomplish this by tying the eligibility of states' low-income residents for the refundable federal tax credit to state health insurance market reform.

In pursuing state reform, state officials would have several options available to them. But the key provision is that, in order to secure the refundable tax credits, they must change state law and regulation to allow individuals and families to take advantage of an affordable health insurance option. In this case, an affordable health option would be a low-cost plan with an average premium that does not exceed 6 percent of the state's median income.

In addition, states could establish new high-risk pools or reinsurance mechanisms to cope with adverse selection in the state markets. Another pooling option open to state officials would be to create a statewide health insurance exchange, sub-

1. For those enrolled in Medicare, Medicaid, the Veterans Administration system, and Tricare, their coverage would not change, and they would not be eligible for the credit.
2. This is in today's dollars. The credit amounts would be annually adjusted based on a blended index of the Consumer Price Index and the rate of medical inflation.
3. A broad spectrum of health policy analysts, from those at the American Enterprise Institute and the Heritage Foundation to those at the Urban Institute and the New America Foundation, have supported using a refundable tax credit to reduce the number of uninsured. For an excellent overview of the issue, see Grace Marie Arnett (ed.), *Empowering Health Care Consumers Through Tax Reform*, (Anne Arbor: University of Michigan Press, 1999).
4. Recent political supporters of using a refundable tax credit as a means to reduce the number of the uninsured include President George W. Bush, Senator John Kerry (D–MA), Senator Robert Bennett (R–UT), and Senator Ron Wyden (D–OR).
5. Regina Herzlinger, *Who Killed Health Care?* (New York: McGraw Hill, 2007), pp. 163–164.

ject to certification by the Secretary of Health and Human Services, to cover more state residents and to offer individuals and families the ability to secure the health insurance of their choice.[6]

With regard to statewide health insurance exchanges, the Senate bill is not prescriptive; the details would be left up to state officials. The bill broadly defines the functions of a statewide exchange: to ease access of low-income persons getting the refundable credit; to enroll eligible persons and provide health plan information; and to develop and apply methods to reduce adverse selection or provide for more equitable distribution of risk. A statewide exchange could also serve as a mechanism for individuals enrolled in Medicaid or SCHIP to get private health insurance. The bill also provides that states may enter into interstate compacts to establish multi-state pooling arrangements to spread risk and make insurance portable and more affordable among their citizens.

More importantly, the Senate bill specifies that any statewide health insurance exchange must be open to any willing health plan licensed in the state that wishes to compete for consumers dollars; that the exchange may not be a vehicle for imposing any new benefit mandates; and the exchange may not be a vehicle for imposing price controls or premium caps on health plans, thus preventing the exchange from evolving into a regulatory agency.

Conclusion. The Senate debate on SCHIP is pivotal for the future of American health care. There are, at the end of the day, only two basic directions in health care: greater government control or more personal freedom for individual and families choosing the health care they trust in a robust and competitive health care economy.

If Congress decides to go down the road toward SCHIP expansion, it means that more Americans will be dependent on government for their health care; taxpayers will be burdened by higher levels of government spending and increased taxation; and more Americans will lose their private health care coverage because of the "crowd-out" that accompanies government expansion.

If Congress decides instead to expand personal choice for individuals and families, it would unleash the powerful forces of the market economy to reduce health care costs, improve the quality of care, and increase patient satisfaction and family control. The Every American Insured Health Act is a visionary proposal that would change the federal tax treatment of health insurance, enabling millions of Americans to secure private coverage through health care tax credits, while harnessing the power of state innovation to make health benefit options more affordable and flexible in state health insurance markets. Beyond comprehensive tax reform, Congress should also consider other creative ways to finance refundable tax credits for low-income families, including the use of existing government funding for various programs such as SCHIP to expand coverage of choice for low-income families.

The Senate debate on SCHIP is an opportunity to go beyond the standard rhetoric on the uninsured and act to address the problem. At the end of this debate, not one child in any American family should lose existing private coverage because of congressional incompetence or indifference.

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6. Under the terms of the bill, a low-income person would not be eligible to secure coverage under a statewide health insurance exchange if they are enrolled in an employer group health plan, Medicare, military health care, or the Federal Employees Health Benefits Program.