

FRESH Thinking
Funding of Comprehensive Healthcare
October 18 & 19, 2007

Shoven Presentation

- Health Policy Problem statistics are well known
- Two essential elements for universal coverage
 - Subsidization of the poor
 - Compulsion
- Who are the uninsured?
 - Poor, sick/disabled (preexisting conditions), difficult to reach, low users, gamblers, and free riders
 - More than half are young (18-34)
- Myth of “shared responsibility”
 - Fails basic incidence analysis (taxpayers/consumers)
- Myth of “government assistance for middle class”
 - There aren't enough of the rich to subsidize the middle class
- Current funding of Medicare and Medicaid
 - Medicare Part A funded mostly by a dedicated tax
 - Medicare Part B and D funded partly by general revenue and premiums
 - Medicaid funded by general revenue
- Examples of the disadvantages of general revenue financing
 - Financial problems of system concentrate on SS and Medicare Part A, ignore things that can draw on general revenues
 - Introduction of Part D was basically “free” to the taxpayer because no taxes were increased
- Advantages of dedicated tax
 - Basically like a price system (taxes are the price for health)
 - Discussion of whether to increase expenditure is a good one
 - Budget discipline on healthcare
 - Replaces the current standard of provision of health care with one that only provides care that we can afford
- Choices for a Dedicated Tax
 - Need for a lot of revenue limits choices to taxes with a broad base
 - Candidates: personal income, consumption, etc.
 - Mandates
- Consumption v. Income Taxes
 - Consumption causes less distortions
 - Other already known issues
- VAT v. Sales Tax
 - Close relatives
 - More than 40 states already have sales taxes
 - VAT is the one unused broad based tax available to the federal government
 - VAT financed universal health vouchers would be very progressive
 - Tax is regressive, but benefit is progressive
- Other alternatives
 - Payroll tax: already taken by SS
 - Corporate tax: terrible idea. Inefficient, unknown incidence, hidden
 - Tax expenditures: lack of salience a drawback from their point of view
 - Income based user charges: amount to taxes. Low income already face high marginal tax rates.
- Mandates
 - Individual, employer and insurance
 - Incidence analysis makes employer mandates similar to individual mandates
 - Insurance companies leave the business when they are faced with mandates
 - Mandates provide compulsion but fail subsidization
- VAT financed vouchers – are they more distortionary?
 - Existing arrangement is already distortionary

- Bundled product (job and insurance) is unnatural
- Incidence of employer provided insurance
 - Workers collectively bear the burden
 - Not widely understood
- VAT also introduces distortions
 - Work-leisure
 - Actual VAT wouldn't cover all consumption
- Case study
- Winners from VAT financed health care
 - Poor
 - Difficult to reach
 - Basically those who are uninsured today
- Summary
 - Need budget discipline
 - Myths of shared responsibility and assisting the middle class
 - Advantages of tax dedication
 - Distortions of employment based health insurance with tax subsidy

Alan Auerbach

- Good paper to start from
- Anecdote about incidence discussion being true in the long run
- Need to address the question of non-citizens
 - This is especially true in a place like CA
- What one means by universal health care?
 - Issue of grouping
- The paper is talking about universal health insurance and not universal care
 - Political argument as to why we need universal insurance is that a program targeted at the poor is a poor program
 - Transfer of middle class into new scheme
- What makes the politics of health care different from economics of health care?
 - For economists the best system is quite easy to decide
 - But there is heterogeneity in preferences and that is where politics comes in
- Incidence issue
 - People don't understand this concept
 - We need to take advantage of the fact that people don't understand incidence → this is why we target employers
- Misunderstanding of costs and benefits
 - People don't know/understand current costs
 - Making things free isn't that relevant as a result
- Preferences are unknown
 - People don't know what they want
 - People don't understand probabilities
- Dedicated taxes
 - Have to be careful in how you're choosing the tax
 - Chose a tax that will rise more slowly than current rates of health care cost increases
 - Subject to the vagaries of a particular tax
- Distortions to the labor system
 - The current system has a lot of distortions
 - People are making discrete choices among jobs not according to hours worked
 - To some extent the marginal distortion under the current system is lower than under a payroll taxes
 - Need to take account of this more carefully

Peter Fisher

- Really liked this paper
- Framework → too little / too much of health care in different sectors
- Need to make people understand true costs of health care

- Corporate taxes are bad
- Need to understand transition costs better
- Any device to discipline is a good thing
- He doesn't see Congress adopting consumption tax and not using it for other things

Chris Jennings

- Is for anything that covers everyone
- Myth of shared responsibility is a political reality
 - Labor folks want a higher contribution from employers → they don't get it, but that means it is real
- Is using employers that horrific if that is the only way to get funding?
- Market the good outcomes and not the financing mechanisms to the public
- Middle class → need to tell them that they are getting more (security, choice, etc.)
 - Can't tell people that it won't cost them anything either
- Part B and Part A expenditures are rising around the same rate, irrespective of tax dedication
- SCHIP expansion failed and it had a dedicated tax
- The final solution will be a lot of different pieces (savings from technology, etc.)
 - People will start with other things before they talk about taxes
- Discussion of financing is the easiest way to kill healthcare reform
 - But the stakeholders who usually use this argument are not using this as much
- GOP is starting to get on board
 - But won't like VAT unless it gets rid of income tax

Alice Rivlin

- Really likes the paper
- Problem is how we will finance care and not just how we finance the uninsured
- Thinks that we need a new tax source at the federal level irrespective of healthcare reform because of growth in Medicare and Medicaid expenditures
- Payroll tax is a bad idea
- Income tax is already used
- Could consider a new energy tax to force energy efficiency
 - But not sure about magnitude and long term sufficiency
- Sales tax is least distorting
 - Would need to cut a deal with the states on sharing and collection
- Dedication of tax
 - Dedicated taxes historically fuel expenditures, look at gas tax and highway expenditure (too high)
 - Payroll tax for SS and Medicare has proven all too easy to raise and allowed too much generosity in SS and Medicare
 - 1983 is an example of a dedicated tax forcing a difficult decision
 - Part D is an example of a difficult decision not happening
 - PayGo rules going by the wayside were a main driver behind that
- Bigger problem is not only financing but creation of entitlement
 - Won't be traded off among other priorities
 - Once it is set it will be put off to the side in terms of tough decisions
- When you couple an ageing population and healthcare entitlement you can create a huge storm
 - A dedicated tax that is easy to raise, will compound problem
- What she would do?
 - Add VAT to federal taxes
 - Share it with the states
 - Add it to general revenue
 - Restrain costs as per Emmanuel/Fuchs
 - Enact firm budget rules to limit expenditure (PayGo)
 - Periodic reconsideration of plan
- In the end it comes down to political will

Discussion

- Dedicated tax issue
 - With VAT the most expenditures will grow is GDP growth
 - What is the expenditure that it is tied to?
 - With healthcare everyone is a beneficiary
 - Healthcare is different than highways, won't see what happened with gas tax in this case
 - Budget limit of a dedicated tax may not be necessary if cost reductions are implemented
 - Delivery system is the problem not the financing scheme; this is where savings can be achieved
 - Changing accounting methods (to force accounting for future costs) achieves much of the discipline of dedicated tax
 - This is already done elsewhere and is of no help (Medicare)
 - Who is paying this tax?
 - Dedication is part of solution of cost control
 - Can PayGo achieve the same result?
 - Dedication isn't really a tax it is a set expenditure
 - Dedication exposes the tax chosen to political attack, hiding in the general fund avoids that avenue
 - Dedication = transparency
- VAT
 - Need to address regressivity
 - Rebate?
 - Not really if the benefit is broad
 - Rate of growth is limited by general economic expansion
 - Accelerating growth would garner political debate
 - Work incentives
 - Pairs up well with dedication because current generation pays for its own expenditures unlike payroll tax
 - Could be the political killer with the GOP
- Incrementalism vs. Revolution
 - Reischauer doesn't believe a huge fix can happen in his lifetime
 - Current system is very difficult to get out of → incrementalism is the only way
 - Changes in US happen in spurts not increments
 - Are we at critical juncture?
 - Healthcare is getting worse at an incremental rate → incrementalism is best way to deal with this, impetus for big change is not there
 - Doing small things means you don't need a big tax
- Incidence of current scheme
 - Won't get immediate salary benefit with new system
- Medicare/Medicaid
 - Paper is missing the biggest effect of this type of reform: getting rid of Medicare and Medicaid will create a lot of money for the government (federal and state)
 - What do we do with the systems if we do a big change?
- Transition
 - Critical unaddressed issue
 - Need to address issue of winners and losers among health care providers
 - Do we buy out the \$500 billion paid by employers to the insurance companies
- Selling the idea to policy makers
 - The predicate for doing something big is to make the long term debt real for people
 - Attaching tax to healthcare may make it more tenable
 - Don't hold out for the best, get something done
 - Unions need to be on board unlike in the past
 - Clinton plan was not set when it came forward
 - Packaging is more important than incrementalism/big change debate
 - Focus on quality and long term cost containment (tie to GDP growth)

- But people don't understand quality
 - People equate price with quality
 - Think of this as single insurer and not single payer
 - Government will not be paying providers directly
 - VAT is more progressive than a payroll tax
 - Need better framing of what we are reforming
 - People are worried about health security
 - A lot of people today are happy with their own delivery system but unhappy with the system overall
- Employers
 - Starting to move on healthcare today, could help spur change
 - Myth of shared responsibility is reality for employers, why not use this to fund healthcare?
- CA is instructive
 - Entrenched groups that support the poor are opposed to reforms
 - Labor is lynchpin
 - Governor talking about whole system and not just insurance part
 - Branding is critical
- Stagnant wages
 - A big problem currently, benefits eat up wages
- Covering the uninsured
 - This goes back to incrementalism debate, do we really need to change the whole system
 - People equate covering the uninsured with health care reform
 - Obama/Edwards want to change system but media focuses on covering the uninsured
- Big discussion on delivery system
- Last thoughts
 - What is the most effective way of bringing about a budget constraint?
 - Tax dedication or PayGo/Caps will work
 - Problem is that eventually there may not be enough money, and the advantage of vouchers might be to create competition to provide some care
 - Perpetuating the myths is not useful
 - But may be necessary
 - Insurance companies gear their plans towards the least costly plan → this is a voucher plan
 - This isn't a case where better information will help, the system will cost more if we move to it, the more people know about it, the less likely they are to buy into it
 - Capital markets will punish those who do not solve health care costs
 - The sell cannot be the financing, it has to be the outputs
 - Have to keep the states in the mix
 - Their financing is getting worse

Oberlander Paper

- He read Fuchs paper as what we should do; his paper is about what *can* be done
- Economics doesn't matter much in the end; substance is rarely the pivotal
- Political feasibility
- Context
 - The status quo isn't great but cannot be underestimated politically
 - There are lots of taxes and revenues coming in
 - People receiving this money are happy and have a vested interest
 - Tax politics
 - A completely new tax isn't easy to do
 - Expiration of Bush tax cuts is looming
 - There has been a big decline in the faith in government

- Undocumented immigrants issue in healthcare
- PayGo
 - Makes it harder to fund reform
- Limited presidential power, fragmentation, 60 votes in the Senate
 - Not easy to get anything through
- Menu
 - There is a huge gap between people and the realities of healthcare
 - Limiting the funding to taxing the wealthy, while more palatable, probably wouldn't have enough money
 - Something incremental may be more feasible
- Employer mandate
 - Historically employer mandates have been the vehicle for universal healthcare
 - There is strong support for having employers pay
 - People are used to this
 - Irrespective of substantive problems, it is probably easier to use
- VAT
 - Seems like a good idea
 - We don't import good ideas from other countries
 - Not sure you can fund all of healthcare for the VAT
 - Easy to pillory
- Dedicated Funding
 - History of split financing Medicare A/B
 - Part A came from social insurance movement
 - Part B came from Wilbur Mills because he did not like payroll taxes
 - There have been more years where costs for Part B have gone up faster than Part A (CMS)
 - Canadian experience now is that there is no empirical link between cost control and dedicated financing
- Conclusions
 - "No easy answers" and "it depends"
 - Thinks that the employer system is a good frame to build on because 160 million people have coverage through their employers
 - People are happy with their health insurance
 - There could be a third way: take the employer dollars and change the locus of decision making
 - This is what the Clintons tried to do
 - Current proposals are "faith based" in terms of cost controls
 - Everything has to go right in order to get healthcare reform to work by 2009
 - Has to be based on employer mandate

Allen Auerbach

- He took from this paper that healthcare reform can't happen
- It would be helpful to distinguish between that which is fundamental and that which is ephemeral in the political world
 - People's perceptions can change
- Would like to understand the politics of capping costs better. Why wouldn't they work?
- Found the discussion about different countries to be interesting
 - But ultimately need to look at the US; just because other people can do it, you can't really learn much from them for cultural reasons
- A universal system change can allow us to hide the ball (that people have to pay more)
 - An add on system to cover the uninsured is explicit about increasing costs

Peter Fisher

- Was surprised at the 50/50 conclusion that followed a glib paper
- Absolute likelihood may be low, but different combinations may work
- The bond market won't solve the problem for us
 - Debt doesn't frighten people; look at Japan

- Previous work on truck, airline, and telecom deregulation shows us where we need to be in terms of beltway consensus
 - Healthcare is still dominated by the battle of the plans not a desire to change
- Need to choose a few ideas to focus on and isolate lobbyists
- Can you get the one big change that can pay dividends?
 - Voucher plan has this by hallowing out Medicare
- John's conclusions
 - Patchwork → yes, good place to start
 - Building on employer based system → won't work, can't get employer mandate to work, balance sheets already out of whack
 - Can see building on employer system only in terms of administering the reform not being fundamental aspect of it
 - Cost controls → yes, they will never fully get us there

Chris Jennings

- Found this to be a great paper
- Agrees with the conclusion
 - Have to pick your time right and pick your poison
- Found the low percentage of tax as % of GDP interesting
- PayGo challenge is tough, but necessary
- Congressional issues are true
 - What is different is who is in the chairmanship positions today than in 1993
 - Good relationships between chair and ranking members in the relevant committees
- Financing is not what we are selling but the whole package
- Tax exclusion reforms
 - Was mishandled by Bush
 - But there is some movement here
 - Don't take this off the table entirely, Democrats
- Employer mandate
 - All of the existing reform plans have this feature, even if it isn't talked about
 - There can't be a small business component because of politics
 - It will be on the table only out of equity not as a revenue raiser
- Maybe there is some possibility to an energy tax
- Sin taxes are a no go
- Deficit spending won't work with Democrats because of current politics
- This will be debate of the 2008 presidential campaign along with tax cut extension

Alice Rivlin

- Enjoyed reading this paper
- Yes it is hard to increase taxes, but it is equally difficult to decrease benefits
 - Tax and spending are intermingled
- The future of Medicare/Medicaid is very tenuous
- The expiring tax cuts are not a good source for funding healthcare
- Reforms that we are considering will require a new PayGo baseline
- Bush opened the door on the exclusion by saying a refundable credit could be funded by rolling it back
 - This is on track to be a voucher
 - Doesn't see why this couldn't work
- Major focus has to be spending restraint
- She isn't sure that debt limit is infinite

Discussion

- Incrementalism vs. Big Change
 - Won't get this in normal times, will need a major crisis
 - A crisis won't necessarily prompt dealing with healthcare
 - Mega-reform excites a lot of parties
- Dedication

- Comparing Parts A and B of Medicare to analyze the effectiveness of dedicated taxes as control, there is too much shifting between the two parts
- 3 Gs that are difficult to deal with
 - Generosity
 - Different in the costs of health insurance and the benefits
 - Geography
 - Plans cost differently in different places
 - There is no variation in the current tax code, it will be difficult to implement
 - Group
 - Composition of the group varies
- Medicare
 - Doesn't do a good job implementing innovations
 - Changing financing could help change this
 - The politics of Medicare expansion are impossible
 - Medicare does change things (the way we structure payments to hospitals)
 - Medicare is the driver in healthcare reform
 - MediGap issue
 - Payment scheme is part of the problem
 - Medicare has market power that allows it to set non-market prices
- Political climate
 - Anti-tax sentiment is a symptom of generalized preference for limited government
 - People don't trust government
 - Old people do
 - But in 2008 there is a chance not because of uninsured but because current system is broken
 - Like the idea of a series of hearings in House and Senate and how the current healthcare system is bad
 - But this has been done
 - Anything we will name will have a downside
 - Lots of political support for exclusion
 - Leadership
 - There could be a sea change
 - New individuals (Baucus and Grassley)
- Implementation of reform
 - Risk adjustment and vouchers is very difficult to do right
 - Difference between health insurance and health care
 - Need constraints into the future
 - Hard to get something when you are taking something away
 - The net impact is a takeaway
 - This is hard enough to do on its own, seems implausible to add tax reform and getting rid of Medicare/Medicaid at the same time
 - The issue about hearings and getting momentum is timing
 - Right now could be the right time
 - Have the hearings on why the status quo is unsustainable
 - These should be non-solution drive hearings
 - Match funding with reform
 - A lot of criticism is on funding piece alone
 - Delivery system reform is critical
- Selling reform
 - Covering other people's children doesn't sell
 - Wage suppression doesn't sell
 - Paying for better system has resonance
 - People know they can't get something for nothing
- Conjunction of tax credit and voucher plan
 - How do you make it work?
 - It is a transformation of one type of tax expenditure into another

- Refundable tax credit is a horror
 - Doesn't this turn into a voucher
- Scoring of voucher and credit is different
- Employers
 - People are getting more than just insurance from the employer
 - Trusted agent
 - Simplify administratively
 - They are financially linked as well
 - It is possible to remove the third part, the financial link, and still have them provide the other functions
 - This could allow the financing and the other roles to be separated
 - There are logical roles for them to be trusted agents
- Stealth incrementalist idea
 - Open up Medicare to those who don't have health through an employer
 - Medicare is less generous than FHEP
 - Age band the premiums, with some geographic adjustment eliminated over time
 - Medicare would be loosened up to pursue reforms
 - Open it up after a few years to employers to fully buy in all of their employees
 - Next, tax all insurance policies and begin subsidizing people who are in this based on income
- There was quite a bit of discussion on individual proposals that appeared to be somewhat unrelated
 - Creating a Medicare based system for a small segment of the population (Part E for Everyone)
- Last thoughts
 - Mistrust in government is an oversimplification
 - People trust government on healthcare in all things other than delivery
 - Question is what you can create that can be transferred over to an independent entity (like FedReserve)
 - Medicare has a major role to play in making the system more efficient
 - If we can get advocates to get behind a plan this is doable
 - You really can't separate the question of funding and what you are delivering
 - The current debate has too much of separation
 - Need to insulate government from provision of care
 - Socialize the insurance and not the care
 - Need a FedReserve like body to set standards and what is covered at the first tier
 - Need an entity of government but not part of the administration
 - You won't be able to make a truly independent agency
 - Whoever creates it controls it
 - Transition is going to be massively complex
 - Just look at Part D
 - Get Bob, Chris and Zeke together to get from incrementalism to big idea
 - Setting the rules for insurance is important
 - Medicare Part E
 - There are a lot of hurdles to get this
 - Evidenced based medicine is not a cure-all
 - Need to change the incentives
 - Pay or play / or nothing
 - Notion of incrementalism should be to chart the road in the right direction of the ultimate solution
 - Idea of separation from politics is important
 - Perfecting financing is not enough, need to deal with delivery also