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Health Security Act

Under the Health Security Act:

- o Employers pay 80 percent of average premium. Families pay no more than 20 percent of premium.

- o Many employers and individuals pay less, since premiums are capped at 7.9 percent of payroll for businesses with less than 5,000 workers, and 3.9 percent of income for households under $40,000.

- o Additional subsidies cap small firm payments at lower levels. Firms with 75 or fewer workers are capped at 3.5 percent to 7.9 percent of payroll, depending on firm size and average wage.

- o Firms with more than 5,000 employees who are outside the alliance pay an assessment equal to 1 percent of payroll.

Financing of Health Care Reform has Several Key Levers:

- o Employer and Individual Shares
- o The Structure of Employer Subsidies (Total vs. Individual Wage Cap)
- o Firm Size in Alliances (or Community Rated Pool)
- o Benefits Package
- o Cost Containment
- o Treatment of Small Business

Employer and Individual Shares

- o Under Health Security Act, employers pay 80 percent of premium; workers pay 20 percent.

- o Many employers and individuals pay less, since premiums are capped at 7.9 percent of payroll for businesses, and 3.9 percent of income for households under $40,000.

- o Employer burden could be reduced below 80 percent, with workers making up difference. Increasing worker burden could require additional subsidies to individuals.

Total vs. Individual Wage Cap

- o HSA caps employer premium payments at 7.9 percent of total payroll.

- o Basing the employer subsidy cap on each individual's wages -- rather than total payroll -- would better target subsidies to lower income workers and reduce costs of HSA.

Size of Alliances (Community Rated Pool)

- HSA has a community rated pool for workers in firms with under 5,000 employees. Firms and workers in pool get federal subsidies.

- Firms with over 5,000 employees can stay out of community pool, but are assessed 1 percent of payroll.

- Reducing community pool firm-size threshold below 5,000 cuts costs by:

  - exempting firms above 1,000 from receiving employer subsidies.

  - requiring firms above 1,000 to pay corporate assessment. leave out?

Generosity of Benefits Package

- HSA benefit package equals median benefits package for Fortune 500 companies.

- Benefits package savings would result from:

  - reducing ~~benefits~~ services covered in the standard plan; or

  - increasing cost sharing by the individual.

Rate of Growth of Health Care Costs

- o HSA would slow growth of health costs through streamlined administration and other improvements.

- o HSA premium caps are a backstop to competition. With the HSA caps, healthcare spending grows at average annual rate of 7.0 7.1 percent from 1996 through 2004. Without reform, spending would grow 8.5 % annually.

- o Cost containment also requires that initial premium gives windfall of uncompensated care to businesses and consumers, not to health industry.

- o While relaxing HSA growth rates isn't too expensive, failing to constrain initial premium would increase costs dramatically.

Treatment of Small Business

- HSA subsidies reduce employer share of premium payments for small businesses, who pay as little as 3.5 percent of payroll.

- Further small firm relief could be provided through:

  - Additional subsidies,

  - Lowering small firm's employer share below 80 percent, or

  - Eliminating small firm employer requirement.

- Eliminating employer requirement:

  - Increases premiums for larger employers.

  - Imposes individual mandate on workers in exempt businesses.

  - Increases likelihood that large firms would splinter.

  - Creates huge cliff effect on hiring.

  - Increases administrative burdens.

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PROTECTING SMALL BUSINESSES

There are three approaches to providing greater protection to small businesses:

A. Providing larger discounts to small businesses.

This approach would require small businesses to pay less. Employees would be held harmless, but the federal government would pay more.

B. Requiring small businesses to pay a lower share of the premium than larger businesses.

This approach would require small businesses to pay less. Employees would be required to pay more -- potentially subject to discounts.

C. Exempting small businesses altogether from the requirement to contribute towards coverage.

This approach would require small businesses to pay nothing. Employees would pay more -- potentially subject to discounts -- and some costs would be shifted to larger employers.

CONCERNS

Protecting small businesses raises a number of structural concerns:

- **Risk of outsourcing** (larger firms splintering into smaller, lower wage firms)
- **Administrative complexity**
- **Equity**
- **Maintenance of effort**
- **Cliffs** (which require businesses that make small changes in size or payroll to pay substantially more towards health coverage)

RISK OF OUTSOURCING

- Under the HSA, all firms with 5,000 or fewer workers are eligible for subsidies. But small businesses are eligible for greater subsidies based on their size and average wage level.

- This structure creates an incentive to "outsource."

    - Outsourcing would occur when a larger employer splinters off a smaller, lower wage workforce in order to take advantage of the small business subsidies.

    - For example, a larger firm could choose to use an outside janitorial service rather than hiring janitors directly. Since the outside janitorial service could take advantage of small business subsidies, it would be less expensive for all concerned.

- Further protections for small businesses -- which would generate greater differentials between the requirements for small firms and the requirements for larger firms -- would tend to exacerbate this problem.

- The danger of outsourcing is that it would increase the cost of subsidies to the federal government. And while we can try to estimate the effects, they are likely to be quite unpredictable, leaving the federal government financially at risk.

ADMINISTRATIVE COMPLEXITY

- The HSA was designed to minimize the administrative complexity and paperwork for the system, and particularly for employers.

  In particular, because all working families are guaranteed an 80% contribution towards health coverage, the system requires very little tracking of families to determine how much they have to pay.

- Any proposal that requires a differential contribution for small and large businesses -- for example, if small firms were exempted altogether -- would inevitably make the system more complex.

  - It increases the administrative burden on employers and on the system, because it requires tracking a family across employers to determine the family's appropriate share of the premium.

  - It also requires a more complicated mechanism to share costs equitably across employers for families with two wage earners.

EQUITY

Requiring smaller employers to contribute less than larger employers raises a number of important equity concerns:

- Under some approaches, it means that expenses for large employers rise.

  This is because many families have two wage earners, one working for a small employer and the other for a larger employer. Exempting small employers means that larger employers continue to bear the full cost for the family, including the spouse working for a small employer.

- It means that worker would have to pay more or less for health coverage depending on whether he or she was working for a large firm or a small firm.

- It means that two employers in the same business -- e.g. a large restaurant and a small restaurant -- would not be competing on an equal footing.

MAINTENANCE OF EFFORT

- Today, on average, employers who pay for health coverage for their workers contribute from 80 to 86 percent of the cost of the premiums. The HSA builds on the current system, requiring employers to contribute 80 percent towards the cost of the premium for their workers.

- Small businesses could be assisted through a lower requirement -- e.g. a 50 percent requirement, or no requirement at all.

- In all likelihood, many small firms that currently contribute towards health coverage would continue to do so -- that is, they would "maintain effort."

  - If they are providing coverage today, and we do not change the tax code, they may very well continue to contribute.

  - But if subsidies are provided to lower and moderate wage workers, firms may drop coverage.

- Even if maintenance of effort is likely to occur, many people are likely to fear that their employers will drop coverage if the requirement for small businesses is lowered to 50% or to nothing.

CLIFFS

When small businesses are treated better, for example by giving them subsidies that large businesses don't enjoy or by exempting them from a mandate, incentives are created to modify their employment decisions to take maximum advantage of the government subsidies.

- For example, assume firms with 10 or less employees are exempted from an employer mandate. Cliff problems arise when such a firm decides to hire an eleventh employee and thereby become subjected to the rules that apply to all other firms.

  The marginal cost for a firm with 10 workers of hiring an additioanl worker is not only the cost of that worker's salary but also the cost of providing health insurance to all 11 workers.

  Consequently, exemptions from the mandate based on employer size create even larger disincentives for firms to hire additional workers.

- While that marginal cost will be less if the firm is heavily subsidized, the marginal cost, i.e. the cliff, can still be several thousand dollars depending on how generosity of the subsidies.