

## The MA health reform and other issues

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## Gruber: three key issues for any reform

- Pooling
  - Need way to organize health care other than need
  - Otherwise -- “adverse selection”
  - Problem: current system leaves out small firms
- Affordability
  - Median family income is \$61K
  - Avg plan is \$12K for a family of 4 (1/5 of income)
- Mandates – no way to generate 100% coverage without them

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## MA Reform: Romney

- Most ambitious state reform to date. Passed April 12, 2006
- Many features but.....
- Two that generate the most heat:
  - Individual mandate, required by law to carry insurance
  - Firm Mandates – must provide insurance or fined \$295
- Most unique: Connector

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## Primary characteristics of MA plan

- People < 300% FPL can purchase state run insurance at subsidized rates
  - Commonwealth care
  - <150% get free insurance
  - Children up to 300% enrolled through SCHIP
- Connector
  - Central market for insurance
  - For people 300%+ of FPL
  - people not in groups can purchase at group rates
  - Community rated – all people pay the same

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- Individual mandate
  - Must own qualified insurance or face fine
  - 1<sup>st</sup> year: fine was \$219
  - 2008: Fine 50% of insurance plan for your geographic area, up to \$912
  - Can file hardship exemption (2% not subject to fine)
- Section 125 plans
  - Firms not offering insurance must set up ability for workers to purchase insurance in pre-tax \$

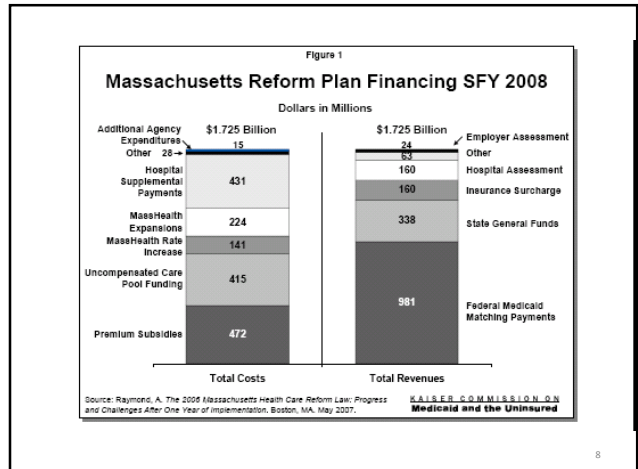
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- Firm mandate
  - Applied to firms w/ > 11 employees
  - Must provide insurance or face annual fine of \$295

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- ### Important question about MA reform
- If mandate people have insurance, what also must be established? From policy perspective, why is this difficult?
  - Why MA?
  - Can it be exported to other states?
  - What has happened to HI costs in MA since reform?
    - What has happened to the state budget during this time?

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### Long, *Health Affairs*, 2008

- Two surveys of adults 18-64 in MA
  - Before: Fall 2006, 3,101 respondents
  - After: Fall 2007, 2,938 respondents
- Compared insurance rates over time

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#### EXHIBIT 2 Impact Of Health Reform On The Health Insurance Status Of Adults (Ages 18-64) In Massachusetts, 2006 And 2007

	Unadjusted Impact		2007-2006 simple difference	Regression- adjusted Impact
	Fall 2006	Fall 2007		
<b>All adults (N = 5,835)</b>				
Uninsured	13.0%	7.1%	-5.8***	-5.6***
Had employer coverage	66.6	69.3	2.6*	2.5**
Had other insurance	20.4	23.6	3.2**	2.9**
Ever uninsured in past year	18.8	14.5	-4.3***	-3.8***
<b>Adults with family income less than 300% of poverty (n = 2,702)</b>				
Uninsured	23.8	12.9	-10.9***	-10.5***
Had employer coverage	37.7	42.3	4.7	4.9**
Had other insurance	38.5	44.8	6.3**	5.9***
Ever uninsured in past year	35.1	24.4	-10.7***	-10.2***

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### Long, Stockley, and Yemane, *AER*

- Use data from the Current Population Survey
- Sample 18-64 year olds
- Compare 2005/06 with 2007 for MA versus all other states
  - Difference in difference model
  - Adds secular trend in outcomes -- what would have happened in the absence of the intervention

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TABLE 1—ESTIMATES OF THE IMPACTS OF HEALTH REFORM ON INSURANCE COVERAGE, BY INCOME

	Pre-post estimates	DD estimates
<b>All adults</b>	N = 6,210	N = 27,481
Uninsured	-6.5***	-6.6***
ESI coverage	1.7	3.1*
Other coverage	4.9***	3.5**
<b>Higher-income adults</b>	N = 3,982	N = 25,253
Uninsured	-0.2	-0.2
ESI coverage	0.8	0.4
Other coverage	-0.7	-0.1
<b>Lower-income adults</b>	N = 2,228	N = 23,499
Uninsured	-17.1***	-17.3***
ESI coverage	3.9	5.6*
Other coverage	13.1***	11.7***

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## Replacing EPHI

- Tax preferred status of EPHI has some advantages
  - Increased coverage
  - Reduces adverse selection
- Problems
  - Encourages more extensive insurance packages
  - Generates readily identifiable uninsured
  - Tax inequality

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- Problem: EPHI has encouraged rapid growth of costs
- Now, insurance expensive
- If we eliminate tax preferred status, will make insurance prohibitively expensive
- How can maintain subsidy with less distortions but one that subsidizes HI?

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## Tax credits

- Replace tax-free EPHI with tax credit
- Tax credit – benefit paid to workers through the tax system
- In most cases, refundable –Reimbursed after income taxes are calculated – even if you owe money
- Example: Earned income tax credit

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## Popular proposal

- Part of McCain's presidential platform
- Outlined as option by Cutler and Dranove in class readings
- Common component of some current proposals before Congress

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### Basic outline

- Families received average of \$4000 tax benefit from EPHI (family plan)
- Only available to those w/ EPHI and lowers the cost of insurance
- Elim. Tax preferred status and replace w/ tax credit of \$4000 for couples.
- Benefits: subsidizes insurance, does not distort market for insurance as much, available to people with coverage not from employers

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### Another example: What is after tax cost of HI from FEDS only

- A family w/ \$70,000 in taxable income
- 36.5% marginal tax rate
  - 25% federal
  - 7.65% Social Security and Medicare
  - 32.65% marginal rate in total (FEDERAL ONLY)
- Suppose they receive a \$12,000 policy
- If HI were a taxable benefit, they would be subject to an additional \$3918 in federal taxes

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### Example

- Family of 4 with \$90,000 in labor earnings, no other income
- Have EPHI valued at \$12,000
- Have no deductions (i.e., do not own a home) so they take the standard deduction

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### Tax rates, married filing jointly

- **Income refers to taxable income: Adjusted gross income minus deductions**
- **10%** on income between \$0 and \$16,700
- **15%** on income between \$16,700 and \$67,900; *plus* \$1,670
- **25%** on income between \$67,900 and \$137,050; *plus* \$9,350
- **28%** on income between \$137,050 and \$208,850; *plus* \$26,637.50
- **33%** on income between \$208,850 and \$372,950; *plus* \$46,741.50
- **35%** on income over \$372,950; *plus* \$100,894.50

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### Federal taxes with tax preferred EPHI

• Income	\$90,000
• - standard deductions	<u>-\$18,700</u>
• Taxable income (TI)	\$71,300
• Federal Income Taxes on TI	\$10,200
• +SS/Medicare taxes (7.65%)*	<u>\$ 6,885</u>
• Total federal taxes	\$17,085

\*These taxes are on all \$90,000 in taxable income

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### HI is taxable but with refundable credit

• Income (\$90K + \$12,000 HI)	\$102,000
• - standard deductions	<u>-\$18,700</u>
• Taxable income	\$83,300
• Federal Income Taxes	\$13,200
• +SS/Medicare taxes (7.65%)	<u>\$ 7,803</u>
• Total federal taxes	\$21,003
• - tax credit	<u>\$ 4,000</u>
• Total	\$17,003

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### What will this do to demand for HI?

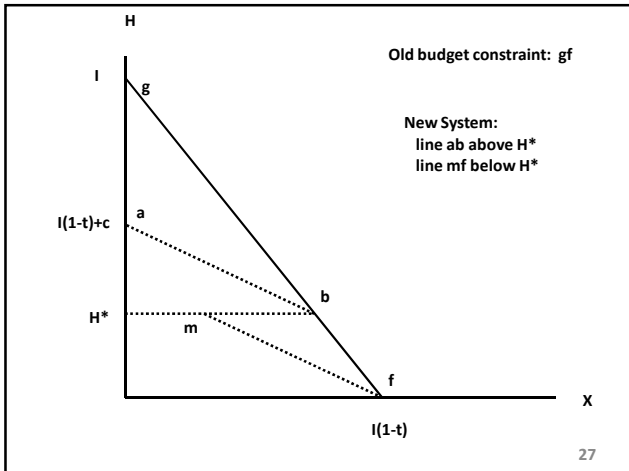
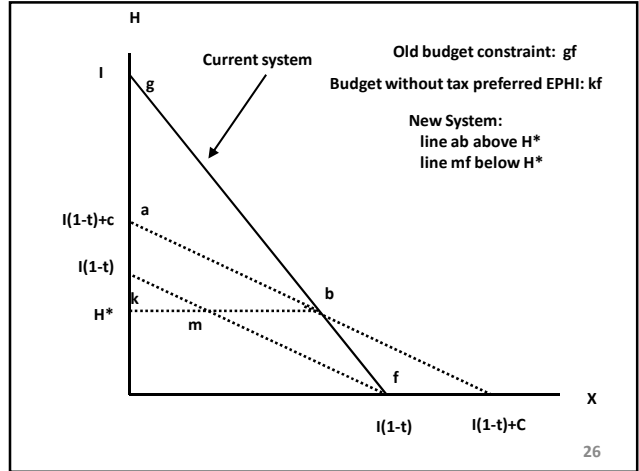
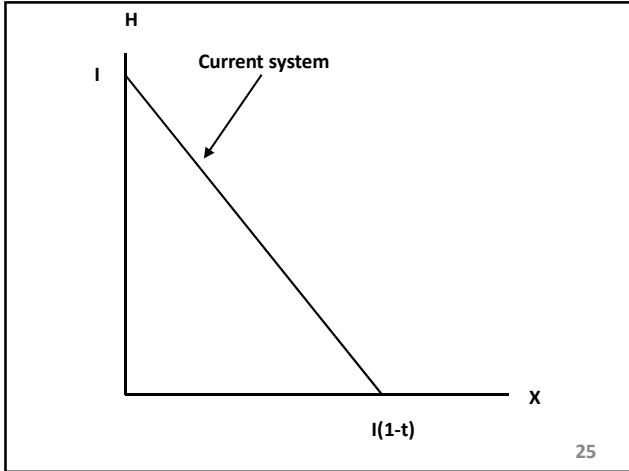
- Max utility by consuming
  - Health insurance (H)
  - All other goods (X)
- Original budget constraint
  - Income I with proportional tax rate t
  - EPHI is tax preferred (not subject to a tax)
$$I(1-t) = x + H(1-t)$$

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### New system

- H is no longer tax preferred
- But, if have qualified H, receive tax credit (C)
  - $H > H^*$  to receive credit
- Assume have qualified health insurance
- $I(1-t) + C = X+H$

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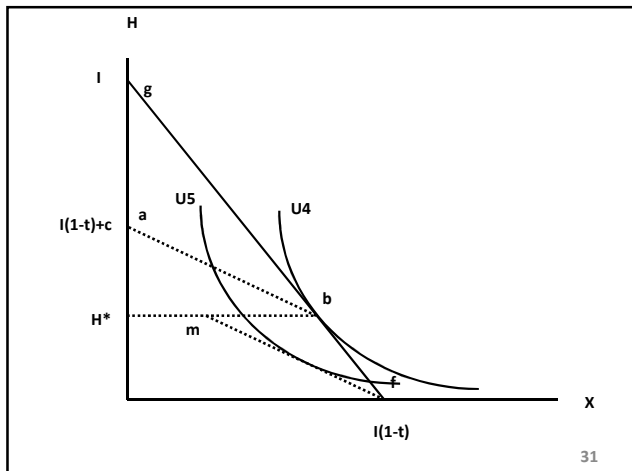
- What is the impact on demand for HI
- Consider area above  $H^*$
  - First – what are the income/substitution effects
  - Sub effects are easiest – price of HI has increase, so demand should fall
  - Look at previous graph, what has happened to the budget constraint for  $H > H^*$ ? What does this mean about relative incomes?
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### Consider second case

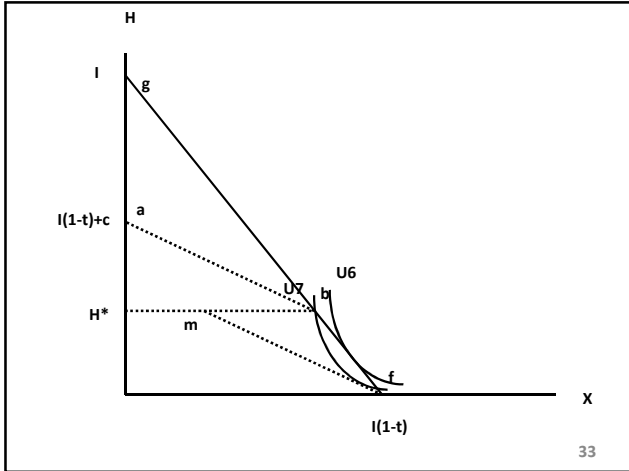
- Person already at breakeven point B
- What will they do?
- Original utility maximizing bundle is at U4
- Will they move to U5?

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- Consider someone who is maximizing at some level below the break even point,  $H^*$
- Call this U6

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### Some questions about tax credits?

- How effective are tax credits for low income people?
- What must be defined by the FEDS if they institute a tax credit? What problems does that generate?

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