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Health Reform: Is Tax on 'Cadillac' Plans Fair?

By THE ASSOCIATED PRESS

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Schoolteacher Kinzi Blair makes only $46,000 a year, but she has what many would consider a ''Cadillac'' health plan, now targeted for a big tax increase by health reformers.

She has $10 copays and no deductible. She gets generic prescription drugs for $10. Her plan covers mental health counseling, organ transplants, acupuncture. It covers speech therapy for preschoolers and in vitro fertilization.

Sound pretty good?

It surely must to millions of Americans who pay high deductibles, hundreds of dollars for prescription drugs or who have no insurance at all. Blair's circumstance illustrates the debate over taxes and fairness when it comes to health reform.

''For me, it's security,'' Blair says. ''I'm thankful I'm in a job where there is health insurance.''

Taxing plans like hers is unfair, says Blair, a kindergarten teacher in San Jose, Calif. Like 57 percent of Americans surveyed in a recent Associated Press poll, she favors a new income tax on wealthy Americans, which the House would impose in its bill to pay for expanding insurance coverage to millions.

But the Senate takes a different approach, including an unprecedented tax on the health insurance of people like Blair. The Senate plan would also increase the Medicare payroll tax for high-income Americans and tax elective cosmetic surgery.

The tax on high-dollar health plans would hit only a few very wealthy Americans and many more in the middle class, experts agree. But it also might bring down health care costs by discouraging companies from offering coverage with so many benefits.

Whatever method is chosen to pay for health reform, Congress and President Barack Obama must persuade Americans about its fairness. When it comes to taxes, Americans are hard to convince.

The Senate Democrats' bill, unveiled last week, would impose a 40 percent tax on insurance premiums above $8,500 for an individual and $23,000 for a family. Those thresholds represent the total paid by both employer and employee.

Blair's premiums cost $11,000 so her insurance company would be taxed 40 percent of the premium that exceeds $8,500 -- a total tax of $1,000.

The Senate bill also would increase the Medicare payroll tax to 1.95 percent on income over $200,000 a year for individuals and $250,000 for couples.

Most Americans don't know whether the tax on health plan premiums would hit them or not, says John Desser, a health policy adviser to John McCain during his presidential campaigns who now coordinates public policy for eHealth Inc., an online marketer of health insurance.

''I don't think most American have any idea what the cost of their premiums is. And I don't think most Americans know that the cost of their insurance could go up as a result of this legislation because we're making it more fair for people who have been treated unfairly in this system,'' Desser says.

The idea is that taxing high-cost health plans would discourage unnecessary health spending and pay for reform out of the health care system itself.

Blair's health plan would be taxed under the Cadillac tax proposal. Here's how her plan stacks up with an average one:

Blair's annual premium (paid entirely by her employer): $11,000.

Average U.S. premium for employer-sponsored individual plans (usually split between worker and employer): $4,824.

Blair's annual deductible: $0.

Average U.S. deductible for HMO plans: $699.

Blair's office visit copay: $10.

Average U.S. copay: $20.

The numbers cited above for employer-sponsored plans don't reflect people who buy their own health insurance. They usually buy plans with high deductibles, around $2,000, and low monthly premiums -- that's the only way many people whose employers don't provide health benefits can afford insurance at all.

Many Americans never think about the fact that health insurance premiums are now tax-free by law. Employers don't pay taxes on what they contribute, nor do workers pay taxes on their portion of premiums. And self-employed workers can take a deduction for their premiums.

Tax-exempt health insurance is an accident of history. During World War II, the government froze wages, so employers lured workers with health benefits. Employers' contributions were made tax exempt. Congress later made sure the tax exemption became law.

The system has led to ''bloated'' health benefits for some with coverage for ''in vitro fertilization, marriage counseling and acupuncture,'' says economist John Goodman of the National Center for Policy Analysis. The Dallas-based conservative think tank favors private solutions over government involvement.

Taxing wealthy Americans to pay for health care -- as the House bill would do -- is bad for the economy, Goodman said, because it would take money out of the system that could be used to invest in growing businesses.

Goodman doesn't like the Senate's proposed tax, either. He'd rather give everyone the same lump sum tax credit for core health insurance, as John McCain proposed when he was running for president, and let people use their taxed income to buy more insurance if they chose.

''The big mistake that Obama made in all of this is not explaining that we have a big mess on our hands and we ought to solve it in a way that, as much as possible, treats everybody the same,'' Goodman says.

One of the arguments for the Cadillac tax is that companies would spend their money to pay higher wages instead of providing rich benefits. Or so the thinking goes.

''The notion that there will be a corresponding increase in wages? You walk into a teachers' lounge or a break room in a factory and say that, you get laughed out of there. Maybe they'd chase you out of there,'' says Rep. Joe Courtney, D-Conn.

The House bill includes a 5.4 percent tax on individuals making more than $500,000 and families making more than $1 million. Courtney says that's the fair way to pay for reform.

''This is a slice of American society that has gotten a very good ride over the past 10 years,'' Courtney said.

Higher health insurance premiums in the Northeast have made many of Courtney's constituents potentially subject to the Cadillac tax. The Senate Finance proposal adjusts for some regional differences, but the adjustment is ''feeble'' and expires too soon, Courtney said. And he doesn't think a higher threshold for firefighters and others in risky jobs is high enough.

Losers would include small businesses and companies with older workers, says Paul Fronstin, director of health research for the nonpartisan Employee Benefit Research Institute. Small businesses lack purchasing power and older workers drive up the cost of health premiums.

But the Cadillac tax does raise revenue, Fronstin says, ''and it has to come from someplace if you want to pay for health reform.''

Tax analysts for Congress say the 40 percent tax on very generous health plans likely would be passed on to consumers, in Blair's case raising her annual premiums by $1,000.

Or perhaps her benefits would be cut instead and she'd have a higher deductible and higher copays. She recently spent $50 on an emergency room copay after she sprained her ankle slipping in the dark on a phone book that had been delivered to her porch.

Blair was grateful then she had insurance. The ankle sprain reminded her what it was like to be uninsured when she was a preschool teacher in her 20s. She was afraid to go inline skating with friends back then.

''Is it going to get to the same point where I'm worried I can't go to the emergency room?'' she says about rising premiums and copays.

She says she doesn't know the answers or what lawmakers should do. Is it possible to rebuild a health insurance system without some degree of tax unfairness? Or is somebody going to get hurt, no matter what, so that uninsured people, like she once was, can get coverage?

"It's definitely a fairness issue," she says.