

'Cadillac tax' on health benefits will hit middle class hardest

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Although both liberal and conservative economists have denounced the longstanding exemption of employment-based health benefits from taxes as tantamount to a "regressive" tax subsidy that unfairly favors the rich, and have lauded a provision of Affordable Care Act that will impose a hefty tax on costlier ("Cadillac") benefit packages, those who stand to be hit hardest by the new provision are middle-income families.

That's the chief finding of a new study by Drs. Steffie Woolhandler and David U. Himmelstein, professors of health policy and management at the City University of New York School of Public Health and lecturers in medicine at Harvard Medical School. Their research article was published this week in the *International Journal of Health Services*.

"Taxpayers should be paying directly for [health care](#) through Medicare-for-All, not indirectly through tax subsidies to private insurance.

However, removing the tax subsidies - as Obamacare will do - without setting Medicare-for-All in place is a step backwards. It's shameful that economists have provided cover for this tax that will hit middle-class families and largely spare the wealthy," said Woolhandler.

"Most Americans are covered by employment-based health insurance," Woolhandler and Himmelstein write. "Both employers' and employees' payments for such coverage are exempt from income and payroll taxes, an exemption that provided a tax subsidy of \$326.2 billion in 2015.

"For years, economists and [health policy](#) analysts have criticized these

subsidies on two grounds, claiming they (1) encourage over-insurance, resulting in the frivolous use of unneeded care, and (2) that the subsidies are regressive, that is, disproportionately benefiting the rich."

These claims, they say, lay behind the so-called Cadillac tax provision of the ACA, which would impose a 40 percent, nondeductible excise tax on employment-based plans that exceed \$10,200 for individuals or \$27,500 for family coverage in 2018 (now set to take effect in 2020).

Because the upper limit on the cost of such plans "will be indexed to overall inflation rather than to health care inflation (which is almost always faster), over time more and more employee groups will be hit by the tax, or by a cut in benefits to avoid it."

The authors note that the new tax provision has been sharply criticized by labor groups and some businesses.

To calculate the impact of the Cadillac tax on various segments of the U.S. population, the authors drew upon a key 2009 study by economist Jonathan Gruber, who helped design the tax, and data from the U.S. Census Bureau, the Robert Wood Johnson Foundation and the World Top Incomes Database. They break out the bulk of their findings by family income quintiles, with an accompanying table and chart.

As to the claim that new levy will make the tax subsidy less "regressive," the authors flatly deny it. They say that while it's true that the wealthiest segment of the U.S. population, e.g. the richest fifth, is currently receiving the largest subsidies in terms of absolute dollars (hence the claim that the subsidies are regressive), if one uses the standard economic definition of regressivity - based on share of income - it's clear that middle-income Americans stand to sustain the greatest financial harm.

"The tax subsidy is a big help for people with (2009) family incomes of \$38,550 to \$100,000, but not for those with lower or higher incomes," they write. As a result, the new tax on benefits "will hit the middle class hardest and spare the wealthy."

They add that eliminating the subsidies (and "over-insurance"), as the Cadillac tax aims to do, "has ripple effects that will disproportionately harm lower-income workers."

"Employers seeking to avoid the tax will probably increase copayments and deductibles. Even if most of the employers' premium savings were eventually passed on to workers as higher wages, the higher out-of-pocket costs would discourage most low-income families from seeking care - exacerbating inequalities in health and health care."

The authors also criticize other inequities that are built in to the Cadillac tax provision, and note "the glaring unfairness of levying the Cadillac [tax](#) based on the cost of benefits, rather than their richness."

In addition to their academic posts, Woolhandler and Himmelstein are co-founders of Physicians for a National Health Program, a nonprofit organization that advocates for single-payer national [health](#) insurance. PNHP had no role in funding or otherwise supporting their study.

More information: S. Woolhandler et al. The "Cadillac Tax" on Health Benefits in the United States Will Hit the Middle Class Hardest: Refuting the Myth That Health Benefit Tax Subsidies Are Regressive, *International Journal of Health Services* (2016). [DOI: 10.1177/0020731416637163](https://doi.org/10.1177/0020731416637163)

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