COMMITTEE ON FINANCE
NEWS RELEASE

Max Baucus, Chairman
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Hearing Statement of Senator Max Baucus (D-Mont.)
Regarding Health Benefits in the Tax Code

The Yale literature professor Peter Brooks once wrote: "We live immersed in narrative, recounting . . . our past actions, anticipating . . . our future projects, situating ourselves at the intersection of several stories not yet completed."

Here in this Committee, we have lived immersed in separate narratives, anticipating healthcare reform and tax reform. Today, we situate ourselves at the intersection of these two stories, not yet completed.

Today, we focus on tax subsidies for health benefits. As our healthcare and tax reform narratives progress, I expect that we will be hearing more and more about this particular story.

The tax code includes many provisions that affect health care — FSAs, HSAs, the TAA health care tax credit, and the deduction for medical expenses in excess of seven and a half percent of AGI — a virtual alphabet soup of provisions.

But the tax subsidy most relevant to today's hearing is the provision that one of our witnesses has called "the third largest government entitlement for health care." That is, the exclusion of employer-sponsored health benefits from individual taxation.

160 million Americans — three-fifths of the non-Medicare population — receive health benefits through the workplace. The tax code does not count the cost of this health insurance coverage as income. And as a result, the Federal Government receives $200 billion less revenue every year.

Economists have long recognized that the tax exclusion for health benefits is regressive. In 2004, nearly 27 percent of these tax expenditures accrued to families with annual incomes above $100,000 — although this group accounted for only about 14 percent of the population.

At the other end of the scale, only 28 percent of these tax expenditures went to families with incomes below $50,000 — although this group represented nearly 58 percent of households.

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Not only do higher income families receive more benefit due to their marginal tax rate — but they are also more likely to receive healthcare benefits from their employer.

Economists also tell us that the tax treatment of employer-sponsored health benefits creates an incentive for over-insurance. And they tell us that this incentive, in turn, promotes healthcare cost inflation.

The current system is a result of evolution dating back to World War II. We have the system that we do by chance, not by design. If we were designing a health system today, we would do things differently.

That said, we've also learned from past attempts at healthcare reform that too much disruption can backfire. Too much change for those who already have health coverage can cause a backlash.

And since a majority of Americans get their healthcare coverage through their employer, any changes to the current tax subsidy should be done carefully and deliberately. We need to have a full understanding of the advantages, disadvantages, and consequences.

Some have proposed transforming the current system into a system where individuals need to purchase their own insurance and employers no longer have a role. That would be no trivial matter. That might be too much change.

All of us here recognize that our system is unsustainable. We cannot continue on our current path. But we must strike a balance. We need to fix what's broken, without breaking what's working.

Thus tax subsidies for healthcare stand at the intersection of healthcare and tax reform. As we anticipate our future projects, let us think about what role these provisions will play in our unfolding narratives. Let us consider ways to change the system as much as appropriate, but not more so. And let us try to find a happy ending for our several stories, not yet completed.

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