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Wrong Incentives for Low-Income Workers?

By Meghan McCarthy **Monday, January 24, 2011**

Beyond the House floor rhetoric over the "job killing" health care law, one potential problem identified by conservative thinkers is the "perverse" incentives for low-income workers through the law's insurance exchange subsidies. John Goodman, president of the National Center for Policy Analysis, told a Capitol Hill panel last week that the subsidies could push low-income workers to seek employment at companies that do not offer health insurance coverage. The thinking is that low-income employees stand to gain far more in savings through government subsidies on the exchanges than with the tax-free premium contributions they'd get if they stay on employer-sponsored coverage.

The health care law covers a certain amount of individuals and families' premiums and medical costs on the health insurance exchanges, provided they make 400 percent of the federal poverty line or less and are not offered employer-sponsored health insurance that is comprehensive and affordable.

Do you think the law's current schedule of subsidies will have to be reworked to avoid a movement of low-income workers to employers without health insurance? Will this make the health care law more expensive than estimated?

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An Employee's Point of View

By John C. Goodman

President and CEO, National Center for Policy Analysis, and Kellye Wright Fellow

Look at it from the employee's point of view. The new law says that an employee must have insurance costing, say, $15,000 for family coverage in 2016. Remembering that employee benefits are a dollar-for-dollar substitute for

wages, that implies that a previously uninsured $30,000-a-year worker will get a 50% cut in pay. Further, the only help this worker will get from Uncle Sam will be the ability of the employer to pay the premiums with pretax dollars. That's worth about $2,000. On the other hand, if this worker can get the same insurance through the newly created health insurance exchange, the federal government will pay almost all the premium and reimburse most out-of-pocket expenses to boot. The Congressional Budget office estimates the total subsidy is worth more than $19,000.

It follows that every worker in his right mind at this income level is going to want to work for a firm that does not offer health insurance and pays cash wages instead. Yes, this employer will have to pay a $2,000 fine. But the fine is well worth the opportunity to obtain a $19,000 benefit.

Now consider a $100,000-a-year worker. This employee will get no subsidy in the exchange. But insurance premiums paid by the employee will avoid a 15.3% payroll (FICA) tax, a 25% federal income tax and, say, a 5% state and local income tax. So at work, Uncle Sam is prepared to pay almost half the cost of this employee's health insurance. It follows that any worker in his right mind at this income level will want to work for a company that does offer health insurance.

In competition for labor, therefore, companies and entire industries will reorganize. Low-income workers will congregate in companies that do not provide insurance; high-income employees will work for firms that do provide it. Firms that ignore these worker preferences will not survive.

This implies two bad results: (1) much higher burdens for taxpayers as millions more take advantage of the subsidies than the Congressional Budget Office (CBO) has predicted and (2) an entire economy whose structure is based not on sound economics, but on gaming an irrational subsidy system.