WHAT A CANADIAN-STYLE HEALTH CARE SYSTEM WOULD COST U.S. EMPLOYERS AND EMPLOYEES

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EXECUTIVE SUMMARY

In the auto industry and elsewhere, corporate leaders are calling for national health insurance. They mistakenly believe that they can turn over the cost of their employee health care plans to the U.S. taxpayer. What they forget is that they also pay taxes. Under national health insurance, the nation's largest companies and their employees would pay more in national health insurance taxes than they currently pay for private health insurance.

A national health insurance program similar to Canada's would require at least $339 billion in new taxes, making the United States one of the most heavily taxed among countries with whom we compete in international trade.

- If the program were funded by a payroll tax, the payroll tax rate would rise from its current level of 15 percent to at least 29 percent.

- If it were funded by an income tax, the current income tax rate would increase by at least 14 percentage points, and the highest rate would rise from 33 percent to 47 percent.

- If it were funded by a consumption tax, the price of everything we buy would increase by almost 10 percent, relative to our income.

These are the tax rates needed to pay for national health insurance for workers and their families. If new health benefits were created for the elderly or for low income people now covered by Medicaid, tax rates would move still even higher. These estimates also assume health care costs remain at their current level. Any rise in health care spending — which is virtually inevitable — would require even more tax revenue.

Under national health insurance, the high-wage industries would pay above-average taxes, even though their workers would receive the average national health insurance benefit. For example:

- On the average, the auto industry would pay about $5,641 per employee under a national health insurance payroll tax.

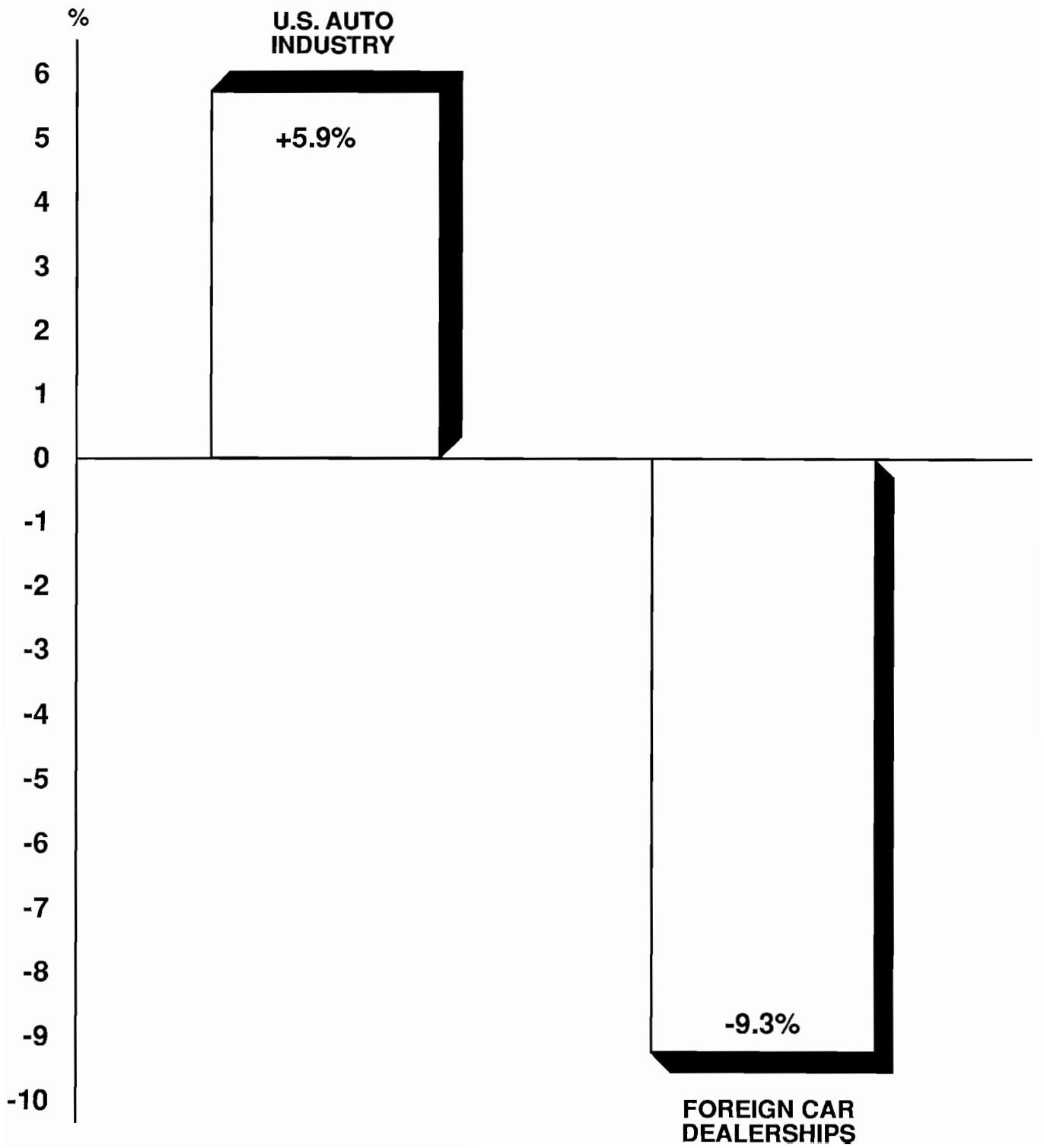
- Add the loss of the current deduction for private health insurance and the total cost rises to $6,824 per auto worker.

- Since the industry now pays only $3,055 for private health insurance, under national health insurance the cost of health care for auto workers would more than double.

Those industries with below-average wages would pay below-average national health insurance taxes and would experience a financial gain under national health insurance. Ironically, some of those industries are in the distribution chain of direct competitors of the manufacturing industries which are calling for a government health care plan. Other things equal, for example, foreign auto dealerships would gain a substantial cost advantage over domestic auto producers.

National health insurance would cripple our ability to compete in international markets. This is because national health insurance involves a redistribution of income among producers in different industries. On the whole, national health insurance would impose extra taxes on U.S. exporting industries and use the proceeds of those taxes to subsidize health care in the importing, marketing and service industries.

HOW NATIONAL HEALTH INSURANCE WILL AFFECT COSTS OF PRODUCTION



INTRODUCTION[1]

One reason why national health insurance is popular in other countries is that the taxes collected to pay for the program are often hidden or disguised. As a result, most people believe they are getting a benefit paid for by someone else.[2]

A similar phenomenon is occurring in the United States, where executives of some large companies have expressed the belief that they could shift the cost of employer-provided health insurance to "others" through government-provided health insurance. Many point to Canada's health care system as a model to be copied. Advocates of national health insurance frequently overlook two facts:

- Paying for national health insurance will require broad-based taxes such as a payroll tax, an income tax or a consumption (value-added) tax, and industries with highly-paid workers will pay proportionately more in taxes.

- Companies with generous health care plans currently receive large tax subsidies because of the deductibility of health insurance costs — subsidies that would vanish under a government-funded health care system.

Once they account for the loss of current tax subsidies and the probable effects of new taxes needed to pay for national health insurance, many U.S. employers will find that the cost to them of national health insurance is *greater* than their current health care costs. For example, under almost any reasonable set of assumptions *the automobile industry will pay more than twice as much for national health insurance as it now pays for private health insurance.*

ASSUMPTIONS USED FOR COST ANALYSIS

Because the implications for employers are so shocking, we have deliberately based our calculations on very conservative assumptions. These are assumptions that are most favorable to the case for national health insurance. What follows is a brief summary.

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[1]This paper is part of an ongoing health policy project being conducted by the National Center for Policy Analysis. Aldona Robbins is Vice-President of Fiscal Associates and a Senior Fellow of the NCPA. Gary Robbins is President of Fiscal Associates and a Senior Fellow of the NCPA.

[2]For example, in Britain the national health insurance payroll tax covers only about 5 percent of the actual cost of operating the British National Health Service. Polls show that a majority of Britons believe that this tax pays for the entire program. Thus the British public underestimates what it pays for national health insurance by a factor of 20. See John C. Goodman, *National Health Care in Great Britain: Lessons for the USA* (Dallas, Texas: Fisher Institute, 1980), p. 203.

Definition of National Health Insurance. Under a system of national health insurance, patients receive health care services free at the point of consumption and pay for the program in their role as taxpayers.[3]

Assumptions About the Consumption of Health Care Services. We assume that, under national health insurance, people will continue to receive the same level of health care benefits they now enjoy. Contrary to the experience of other countries, we assume that there will be no surge in demand or dramatic increase in health care costs after national health insurance is adopted.

Assumptions About the Effects of New Taxes. Despite the fact that national health insurance will impose a large tax burden on the economy, we assume no change in the willingness of workers to work and no change in the nation's output of goods and services.

Assumptions About Medicare and Medicaid. We assume that the new program applies only to the nonelderly population not now on Medicaid. Although it is politically unrealistic, we assume no increase in Medicare and Medicaid spending.

Assumptions About Access to Health Care and the Quality of Health Care. Despite contrary evidence from other countries, we assume no change in the quality of health care services or in access to health care. Thus we assume people will not seek to opt out of the system and purchase private health insurance as they do in Britain and other countries.

Assumptions About the Cost of National Health Insurance. We assume initially that the health care system experiences no change in efficiency, so that the cost of insuring an individual through the public sector will be the same as it is in the private sector. We then assume that the public system becomes more efficient than the current system, despite contrary evidence from countries with national health insurance programs.

Assumptions About Who Bears the Cost of National Health Insurance. National health insurance will involve the loss of a current tax subsidy for private health insurance and the payment of new taxes to finance the new system. As an economic principle, the employees will ultimately bear the cost of these changes. Initially, however, the program can be structured so that it attempts to impose the entire cost on either employers or employees. Accordingly, we consider both financing alternatives.

[3]Under Canada's system of national health insurance, for example, all Canadians receive complete coverage for hospital and physicians' services without deductibles or copayments.

Employees Held Harmless: Under this regime, the system is structured so that employees have the same aftertax real income (minus the average out-of-pocket medical expenses) as they have under the current system.[4] On the average, employees neither gain nor lose financially as a result of the switch to national health insurance.[5]

Employers Held Harmless: Under this regime, the system is structured so that employers have no higher labor costs than they currently have. Employers neither gain nor lose financially as a result of the introduction of national health insurance.

As an example of this distinction, consider the incidence of the new taxes needed to finance national health insurance. If employees are held harmless, the excess burden of the new taxes (national health insurance taxes minus national health insurance benefits) will fall totally on employers. Conversely, if employers are held harmless, the excess burden of the new taxes will be borne by workers.

These two methods of adjusting to the new system — employees or employers held harmless — may be regarded as two extreme bargaining positions that will be brought to the negotiating table both in the economic and in the political marketplace. Undoubtedly, the final outcome will rest somewhere between these extremes.

NATIONAL HEALTH INSURANCE WOULD REQUIRE A MINIMUM OF $339.3 BILLION IN NEW TAXES

Using the assumptions enumerated above, we are prepared to calculate the cost of national health insurance. That cost is equal to the total amount of health care costs currently incurred by employers, plus all out-of-pocket costs currently incurred by individuals, plus the cost of health insurance for the currently uninsured. As Table I shows, this cost would be $387.8 billion in 1989 — an amount equal to almost one-third of the current federal budget.

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[4]Under the current system, employees have out-of-pocket medical expenses. Under national health insurance, these expenses will be paid by the government. As a result, if the workers' aftertax wages are reduced by the amount of current average out-of-pocket medical expenses, they will be no worse off or better off than they are under the current system.

[5]In making these calculations, we assume that public insurance is just as valuable as private insurance and that a national health insurance policy has a value to workers of $3,300 on the average. See Appendix A for the derivation of this number.

TABLE I

NATIONAL HEALTH INSURANCE COSTS IN 1989[1]

1989 Employer Health Payments	$156.9
1989 Out-of-Pocket Health Payments Plus Other Health Insurance[2]	230.9
Total Expenditures[3]	$387.8

[1]Refers to the nonelderly, non-Medicaid population.

[2]Includes payments made under health insurance policies purchased by individuals as well as unreimbursed care provided to the currently uninsured. About $58 billion of this amount represents the cost of insuring the currently uninsured.

[3]Equal to about $3,300 per worker, which is a weighted average of single and family coverage.

Source: Appendix A.

TABLE II

TAX RATES NEEDED TO FINANCE NATIONAL HEALTH INSURANCE[1]

Tax	Employees Held Harmless	Employers Held Harmless
Payroll Tax[2]	13.86%	14.99%
Income Tax[2]	14.42%	15.67%
Consumption Tax	9.75%	9.75%

[1]See Appendix A for an explanation of the tax bases.

[2]These rates differ in the two cases because there will be a difference in the tax base, depending on how much employee wages are increased after the abolition of employer-provided health insurance.

Of the $387.8 billion total cost, we assume that approximately $48.5 billion will be financed through an increase in income and FICA (Social Security) taxes because money wages will increase to offset the abolition of a fringe benefit (employer-provided health insurance). Private health insurance provided by an employer is part of the total compensation package which workers receive. Health insurance is an alternative to higher money wages. Since under national health insurance private health insurance will no longer be necessary, it is reasonable to assume that employees will receive wage increases equal to the present cost of health insurance. Unlike private health insurance fringe benefits, however, money wages are subject to income and FICA taxes. Even if employers did not increase the wages of workers, but instead kept the savings from the abolition of private health insurance as an addition to company profits, the government would still collect more tax revenue in the form of additional corporate income tax payments. Consider, for example, the case of the automobile industry:

- On the average, automobile companies spend about $3,055 per worker for health care under some of the most lavish health insurance plans found anywhere, and none of it is taxed.

- In the absence of any need for private health insurance, if the auto companies increased employee wages by $3,055, the federal government would collect as much as $1,323 per worker in additional income and payroll taxes.[6]

- On the other hand, if the auto companies tried to keep the $3,055 per worker as profit, about $1,039 would go for additional corporate income taxes.

After adjusting for the increased revenues the government would receive through the abolition of national health insurance, we calculate that an additional $339 billion would be needed to pay for national health insurance. This sum would have to be financed through new taxes.

[6]Assumes the worker is in the 28 percent income tax bracket and below the Social Security wage ceiling.

THREE GENERAL TAX OPTIONS: PAYROLL, INCOME OR VALUE-ADDED TAXES

Because the cost of national health insurance is so large, it is realistic to expect that it will be financed through a broad-based tax: a payroll tax, an income tax or a consumption (value-added) tax.[7] Table II shows what tax rates will be necessary in order to fund the program under each of the three.

- If the program is funded by a payroll tax, the payroll tax rate will rise from its current level of 15 percent to a rate of at least 29 percent.
- If the program is funded by an income tax, the income tax rate will increase by at least 14 percentage points, and the highest rate will rise from 33 percent to 47 percent.[8]
- If the program is funded by a value-added tax, the price of almost everything we buy will increase by almost 10 percent, relative to our income.

To see what these tax rates would mean for American families, consider the effects of financing national health insurance with a payroll tax.

- For low-income workers, who currently pay no income taxes, the amount of taxes paid would double — from the current payroll tax which takes 15.3 percent of income to 30.3 percent of income.
- For workers who are currently in the 15 percent income tax bracket, the marginal tax rate would increase by 50 percent — rising from a combined (income and payroll tax) marginal tax rate of 30.3 percent to a rate of 45.3 percent.
- Workers who are currently in the 28 percent income tax bracket would see their combined marginal tax rate rise to 58.6 percent, with the government taking more than half of each additional dollar earned.

In general, the cost of national health insurance to any particular industry will be highest if the program is financed by a payroll tax. For the most part, under a payroll tax those who receive the benefits of national health insurance (the under-age-65 working population) will be paying the costs of those benefits. If the program is financed with an income tax, elderly taxpayers covered by Medicare will pay part of the cost of the new program, even though they receive no additional benefits under our assumptions. With a consumption tax, part of the cost of the program will also be borne by people covered by Medicaid, even though these people also will receive no additional benefits.

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[7]Canada uses a combination of all three taxes. See Employee Benefit Research Institute, "Canada's Health Care System: Lessons for the United States?" EBRI Issue Brief No. 90, May 1989, pp. 2-3. Recently, Canada's federal government proposed a 9 percent consumption tax on all goods and services to help meet its growing budget crisis. This would be on top of provincial sales taxes that can go as high as 12 percent. Middle-income taxpayers pay a base income tax rate of 26 percent before provincial taxes, which add half as much again to the burden. See "Ducks Fly North," *Wall Street Journal,* December 26, 1989, p. A8.

[8]For taxpayers in the 15 percent income tax bracket, the income tax rate would rise to 29 percent. For taxpayers in the 28 percent tax bracket, the income tax rate would rise to 42 percent.

NATIONAL HEALTH INSURANCE WILL MORE THAN DOUBLE HEALTH CARE COSTS IN THE AUTO INDUSTRY

The cost of national health insurance will not be spread equally over all sectors of the American economy. Instead, some industries will incur large losses while others will gain.

- Other things equal, the more generous an industry's current health care benefits the more it will lose under the switch to national health insurance because of the loss of tax subsidies for current employer-provided health insurance.

- Other things equal, the more highly paid the work force, the more an industry will lose under national health insurance because the burden of taxes needed to pay for national health insurance rises with income.

Take the auto industry, for example.

Effects of a Payroll Tax in the Auto Industry. As Tables III and IV show, the auto industry will pay about $6,800 per worker in additional taxes as a result of national health insurance funded by a payroll tax. Yet the value of national health insurance is only $3,300. As a result:

- The auto industry will pay about $3,500 more in taxes than it will receive in benefits under the new health care scheme.

- Since the cost of employer-provided health insurance currently is about $3,055, this means that national health insurance will cost the industry more than twice as much as the current cost of private insurance.

Under the worker-held-harmless scenario, the employer increases the worker's salary in order to compensate both for the loss of the private health insurance fringe benefit and for the new taxes on the higher salary. The employer also bears the cost of the excess burden of the national health insurance payroll tax. After these changes are made, the employee is no better off or worse off than before. The employer's health care costs have more than doubled, however, rising from the current level of $3,055 to $6,579 per worker.

Under the employer-held-harmless scenario, employees receive a salary equal to the value of their lost private health insurance fringe benefit. This salary is reduced by the amount of the employer's FICA tax on the salary increase, however. Employees must also bear the full burden of the income and employer FICA tax on their salary increase plus the new national health insurance payroll tax. After these changes are made, auto workers will have the same health care benefits they now have, but their taxes will have increased by $3,491 per worker. If the value of employer-provided health insurance is regarded as a substitute for money wages, then the cost of health insurance for the average worker will have more than doubled, rising from $3,055 to $6,546.

Effects of an Income Tax in the Auto Industry. Table V shows the cost of national health insurance for auto workers under each of the three types of broad-based taxes. As explained above, an income tax has a lower cost per worker than a payroll tax and the consumption tax has the lowest cost of all three because of the differences in the taxpayer base. This does not mean that the payroll tax is the most expensive in terms of total costs of production, however. An income tax, for example, reaches holders of capital and will cause the service price of capital to rise. As a result, the initial impact on the cost of production will be quite high.[9] As Table VI shows, the impact of the income tax on total costs of production will be more than twice as great as the impact of a payroll tax.

Effects of a Consumption Tax in the Auto Industry. In the case of a consumption tax, Table II shows that an across-the-board value-added tax rate of 9.75 percent will be required in all industries. In the automobile industry, however, the rate will be 11.6 percent and will include costs of compensating auto workers for the losses they sustain in the switching to the new system. Our method of analysis examines the initial attempt to impose the tax on a particular group of taxpayers. In the case of a value-added tax, we assume that industries will initially try to impose the cost of this tax on consumers by raising their prices. As an economic principle, however, it will be impossible for all firms to raise their prices by 10 percent because consumers will not have 10 percent additional income to pay those prices. Ultimately, therefore, a value-added tax will be borne not by consumers but by people in their role as suppliers of labor and capital.

[9]In general, a tax on capital has a much more severe impact on input prices than a tax on labor. For example, a 13 percentage point increase in the income tax rate will increase the tax rate on capital by about 50 percent. If the aftertax rate of return on capital is to be held constant (as economic theory and historical evidence suggest), this implies a 25 percent increase in the service price of capital for employers.

TABLE III

NEW TAXES UNDER NATIONAL HEALTH INSURANCE FOR AN AUTOMOBILE WORKER[1]

(NHI Funded by a Payroll Tax)

	Employee Held Harmless	Employer Held Harmless
Loss of Tax Subsidy for Private Insurance:		
Increase in FICA Tax	$592	$428
Increase in Income Tax	591	427
NHI Payroll Tax[2]	5,641	5,936
Total Tax Burden	$6,824	$6,791

[1]Based on an initial salary of $36,760 — the average salary currently paid to auto workers assumes the worker is in the 15 percent federal income tax bracket. The new salary varies depending on whether employers or employees are held harmless.

[2]Equal to the new salary times the payroll tax rates presented in Table II.

TABLE IV

NET COST OF NATIONAL HEALTH INSURANCE FOR AN AUTOMOBILE WORKER

(NHI Funded by a Payroll Tax)

	Employee Held Harmless	Employer Held Harmless
Loss of Tax Subsidy for Private Insurance[1]	$1,183	$855
Excess of NHI Payroll Tax over NHI Benefits[2]	2,341	2,636
Total Net Cost	$3,524	$3,491

[1]From Table III.

[2]The benefit of national health insurance is assumed to be $3,300. The relevant payroll tax rates are presented in Table II.

TABLE V

INCREASE IN HEALTH CARE COSTS IN THE AUTO INDUSTRY UNDER NATIONAL HEALTH INSURANCE (Per Production Worker)

Tax	Employee Held Harmless	Employer Held Harmless
Payroll Tax	+$3,524	+$3,491
Income Tax	+$3,019	+$2,962
Consumption Tax	+$1,018	+$687

TABLE VI

COST OF NATIONAL HEALTH INSURANCE AS A PERCENT OF TOTAL PRODUCTION COSTS IN THE AUTO INDUSTRY

Tax	Employee Held Harmless	Employer Held Harmless
Payroll Tax	5.9%	5.9%
Income Tax	12.6%	13.3%
Consumption Tax	11.6%	11.6%

NATIONAL HEALTH INSURANCE WOULD BE ESPECIALLY COSTLY TO U.S. MANUFACTURING INDUSTRIES

National health involves much more than government provision of health care. As taxes are raised to pay for national health insurance, an enormous amount of redistribution of income will take place. As we have seen, workers in some industries will pay more in taxes than the value of their national health insurance benefits while workers in other industries will pay less.

Because the manufacturing sector of our economy tends to pay above-average wages and provide above-average (tax subsidized) private health insurance benefits, this sector will be especially hard hit by a program of national health insurance. As Table VII shows:[10]

- Among those manufacturing industries that will be hardest hit financially by national health insurance, the additional cost per employee (over and above any national health insurance benefit) ranges from $1,500 to more than $3,500 per employee.

- In motor vehicle and equipment manufacturing, telecommunications, primary metals and chemical manufacturing, the total additional cost to the industry will exceed one billion dollars.

- In mining, automobile manufacturing, computer services and data processing, the total loss to the industry is just under one billion dollars.

[10]A complete listing of the gains and losses by industry, under three different types of taxes, is presented in Appendix B.

TABLE VII

WINNERS AND LOSERS UNDER NATIONAL HEALTH INSURANCE: SELECTED INDUSTRIES[1]

Industries That Lose	Initial Change in Cost Per Production Worker	Increase in Total Production Costs[2]	
		Amount	Percent
Motor Vehicles and Car Bodies (Mfg.)*	+ $3,523	$951,914,600	4.11%
Tires and Inner Tubes (Mfg.)*	+ $3,242	$211,378,400	6.18%
Petroleum and Coal Products (Mfg.)	+ $3,203	$350,728,500	0.90%
Tobacco Manufactures	+ $2,793	$98,034,300	0.55%
Photographic Equip. and Supplies (Mfg.)	+ $2,490	$125,745,000	3.43%
Telephone Communications (Non mfg.)	+ $2,254	$1,485,386,000	1.19%
Primary Metal Industries (Mfg.)	+ $2,007	$1,215,238,500	2.89%
Chemicals and Allied Products (Mfg.)	+ $1,939	$1,206,251,700	1.35%
Mining (Non mfg.)	+ $1,901	$977,114,000	0.99%
Computer and Data Processing Services (Non mfg.)*	+ $1,609	$949,149,100	3.85%

Industries That Win	Initial Change in Cost Per Production Worker	Decrease in Total Production Costs	
		Amount	Percent
Retail Trade (Non mfg.)	- $1,488	$25,989,408,000	5.26%
Hotels and Other Lodging Places	- $1,387	$2,007,543,800	4.85%
Amusement and Recreation Services	- $1,346	$1,339,539,200	4.83%
Personal Services	- $1,280	$896,256,000	2.25%
Apparel and Other Textile Products (Mfg.)	- $1,161	$1,081,703,700	4.16%
Leather and Leather Products (Mfg.)	- $738	$87,969,600	2.30%
Banking	- $670	$852,508,000	0.87%
Credit Agencies Other than Banks	- $486	$331,014,600	1.68%
Textile Mill Products (Mfg.)	- $417	$264,544,800	1.14%
Auto Repair Services and Garages	- $411	$305,619,600	0.68%

[1]National health insurance tax burden minus health insurance benefits. The calculations presented here assume that the excess burden of national health insurance is borne by employers and that national health insurance is funded by a payroll tax. Similar calculations were done assuming that the full burden falls on workers and produce similar results.

[2]Based on the contribution to gross national product (GNP) in each industry. Industry GNP for 1987 was taken from the *Survey of Current Business*, July, 1988, Table 6.1, and adjusted to 1989 levels using the growth in overall GNP between 1987 and 1989. The asterisk (*) indicates an estimated industry GNP using the share of that industry's production workers in that of the larger industry group. For example, motor vehicles and car bodies account for 40 percent of the larger industry group, motor vehicles and equipment.

Source: Appendix B.

WHY SOME INDUSTRIES WILL GAIN FINANCIALLY UNDER NATIONAL HEALTH INSURANCE

In contrast to the auto industry, some industries actually will gain as a result of national health insurance. These are industries which currently provide small health insurance benefits and thus receive little tax subsidy for health insurance. Because they tend to have below-average wages, they will pay below-average payroll taxes. Table VII lists some industries that will gain the most under national health insurance. As the Table shows:

- The retail trade sector will receive a national health insurance subsidy equal to $26 billion.

- In hotels and lodging, amusement and recreation services, and in the apparel and textile industries, the total industry subsidy will exceed one billion.

Indeed, it is ironic that industries with the most generous health care benefits and the greatest inclination to seek government relief will be hurt the most by national health insurance, while industries providing meager health care benefits will gain the most.

Consider a national health insurance annual benefit of $3,300 per worker financed by a payroll tax with a 15 percent tax rate. For an industry with an average wage of $10,000, the average national health insurance tax will be $1,500. Compared with a $3,300 benefit, this industry will gain $1,800 per worker. On the other hand, an industry with an average wage of $30,000 will pay an annual tax of $4,500 and will lose $1,200 per worker.

Effects on Retail Trade. As an example of an industry which gains from national health insurance, consider the retail trade sector of the economy. As Table IX shows:

- The average loss of health insurance tax subsidy in retail trade is about $300 and the average national health insurance tax is about $1,800.

- Since the average national health insurance benefit is $3,300, the industry gains $1,488 per worker.

As in previous examples, Table IX presents the results in terms of the employee-held harmless and employer-held-harmless assumptions. In this case, however, when the employee is held harmless (neither gaining or losing), the employer realizes the full gain of $1,488 as a result of the introduction of national health insurance. While at first glance it may seem improbable that the employer would reap any of the gain. However, employers who provide little or no health insurance benefits currently are at a disadvantage in the competition for labor. Other things equal, they must pay higher wages. With the introduction of national health insurance, they will be able to lower their wages and still attract employees.

Auto Industry vs. Foreign Car Dealership. It is interesting in this respect to contrast the expected consequences of national health insurance for the U.S. auto industry with the consequences for a foreign car dealership. As Table X shows, if the dealership exhibits the characteristics of the average retail employer, it will experience a reduction in payroll and production costs and gain a competitive advantage over its domestic competitors.

TABLE IX

NET BENEFIT OF NATIONAL HEALTH INSURANCE FOR A WORKER IN RETAIL TRADE

(NHI Funded by a Payroll Tax)

	Employee Held Harmless	Employer Held Harmless
Loss of Tax Subsidy for Private Insurance:	- $ 307	- $221
Excess of NHI Benefits over NHI Payroll Tax	+ $1,795	+ $1,714
Net Benefit	+$1,488	+$1,493

TABLE X

THE U.S. AUTO INDUSTRY VS. FOREIGN AUTO DEALERSHIPS UNDER NATIONAL HEALTH INSURANCE

(Employees Held Harmless)

Cost of National Health Insurance Per Production Worker

Tax	Auto Industry	Foreign Car Dealerships
Payroll Tax	+ $3,524	- $1,488
Income Tax	+ $3,019	- $2,520
Consumption Tax	+ $1,018	- $2,074

Cost of National Health Insurance as a Percent of Total Production Costs

Tax	Auto Industry	Foreign Car Dealerships
Payroll Tax	+ 5.9%	- 9.3%
Income Tax	+ 12.6%	- 8.2%
Consumption Tax	+ 11.6%	- 4.5%

CONTROLLING HEALTH CARE COSTS UNDER NATIONAL HEALTH INSURANCE

Implicit in the call for national health insurance is the belief that the government would do a better job of controlling costs than the private sector. Yet the evidence suggests that government involvement in health care is not part of the solution but part of the problem.

- Personal health care expenditures as a percent of GNP have grown at a *faster rate* since Medicare and Medicaid came into existence.[11]

- Government programs have exacerbated the increase in medical inflation, which is twice that for other goods and services. Since the enactment of Medicare and Medicaid in 1965, 67 cents of each health care dollar has been consumed by inflation.[12]

- Government projections have seriously underestimated the costs of new health care programs. In 1972, Medicare coverage for kidney dialysis and transplants was budgeted at $100 million, but first-year costs were 233 percent greater than estimated. Today Medicare spends $1.1 billion on the program.[13]

- Only eight months into the new Medicare Catastrophic Coverage program, government analysts raised their estimates of the program's first-five-year costs from $30 billion to between $45 and $55 billion.[14]

- Medicare's Prospective Payment System (PPS) has been hailed as an effective way of controlling inpatient hospital costs. Since PPS, however, Medicare outpatient expenditures have exploded.[15]

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[11]Rates of growth were calculated using statistics in U.S. Department of Health and Human Services, *Health, United States 1988* (Hyattsville, MD: DHHS, March 1989), Table 96, p. 150.

[12]From 1948 to 1987, about 50 cents of each additional dollar of health care spending was consumed by inflation. See Aldona Robbins and Gary Robbins, "Mandating Health Insurance," *Economic Policy Bulletin,* No. 39, Institute for Research on the Economics of Taxation, Washington, DC, July 8, 1987, p. 21. For an estimate since 1965, see *Health, United States 1988,* Table 100, p. 154.

[13]Paul Craig Roberts and Aldona Robbins, "At the Heart of Medicare's Woes," *Wall Street Journal,* November 22, 1985.

[14]Bacon, Kenneth H., "Catastrophic Medicare Insurance Plan Generates Skyrocketing Cost Overruns," *Wall Street Journal,* September, 18, 1989, p. A18.

[15]Part B benefits have grown from $19.6 billion in 1984 to $38.8 billion in 1989, a 98 percent increase. Moreover, the share of outpatient hospital payments has grown from 15 percent of Part B expenditures in 1984 to 19 percent in 1989. See The Board of Trustees, Federal Supplementary Medical Insurance Trust Fund, *1989 Annual Report of the Board of Trustees of the Federal Supplementary Medical Insurance Trust Fund,* Washington, DC, April 1989, Table 76, p. 30 and Table A1, p. 46.

- The federal government, the nation's largest single employer, has not been effective in controlling its own health insurance costs. Federal budget projections show federal employee health insurance costs doubling between 1987 and 1991 — an annual increase of 20 percent.[16]

- Nor has the federal government been an effective hospital administrator. The average length of stay at federally-owned Veterans Administration hospitals is twice as long as that of private, proprietary hospitals for the same procedures.[17]

It is true that countries with national health insurance spend less on health care than does the U.S. Canada spends about 8.5 percent of its GDP on health and Britain about 6.2 percent, far less than the U.S. at 11 percent. However, other countries typically spend less on health care not because they are more efficient but because they deny patients services which are routinely available in the U.S.[18]

Effects of Reducing Health Care Spending by 8 Percent. For the moment, however, assume that switching to national health insurance would bring about an 8 percent reduction in costs — a reduction equal to about $31 billion — and ignore the fact that no national health insurance scheme has ever brought down health care costs.[19] Financing national health insurance would still require a payroll tax increase on the order of 13 percentage points, an income tax rate increase on the order of 13.5 percentage points or a consumption tax on the order of 9 percent. As Table XI shows, the costs of production in the durable manufacturing sector would still increase by 2 percent to 7 percent.

Effects of Reducing Health Care Spending by 23 Percent. Table XII shows the increase in health care costs and the cost of goods in the durable manufacturing sector if U.S. health care spending were constrained to be 8.5 percent of GNP, as is the case with Canada. This would require a 23 percent reduction in current health care spending and might be achieved by extensive health care rationing. Constraining health care spending in this way reduces by $90 billion the amount of new taxes needed to finance national health insurance. However, while they would pay lower taxes, the production employees in durable manufacturing would also receive a smaller national health insurance benefit. The combined effect of lower taxes and the reduced value of health benefits leads to only slightly lower costs per auto worker than in the case of no reduction in health care spending.

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[16]Executive Office of the President, *Budget of the U.S. Government,* Fiscal Year 1991, Washington, DC, 1990, p. A-1074.

[17]Cotton M. Lindsay, *Veterans Administration Hospitals: A Economic Analysis of Government Enterprise* (Washington, DC: American Enterprise Institute, 1975), p. 47.

[18]See Goodman, *National Health Care in Great Britain*; John Goodman and Gerald Musgrave, "Health Care for the Elderly: The Nightmare in Our Future," NCPA Policy Report No. 130, National Center for Policy Analysis, October 1987; and John Goodman and Gerald Musgrave, *Solving America's Health Care Crisis* (Washington, DC: Cato Institute, 1990), forthcoming.

[19]Health experts claim that financial management, marketing and duplicative administration add 8 cents to every health care dollar.

TABLE XI

COST OF NATIONAL HEALTH INSURANCE IN DURABLE GOODS MANUFACTURING ASSUMING AN 8 PERCENT REDUCTION IN HEALTH CARE COSTS

	Increase in Costs Per Production Worker	
	Employee Held Harmless	Employer Held Harmless
Payroll Tax	+ $833	+ $802
Income Tax	+ $145	+ $61
Consumption Tax	- $613	- $836

	Increase in Cost of Production	
	Employee Held Harmless	Employer Held Harmless
Payroll Tax	2.2%	2.1%
Income Tax	7.1%	7.7%
Consumption Tax	7.1%	7.1%

TABLE XII

COST OF NATIONAL HEALTH INSURANCE IN DURABLE GOODS MANUFACTURING IF HEALTH CARE COSTS WERE REDUCED TO 8.5 PERCENT OF GNP

	Increase in Costs Per Production Worker	
	Employee Held Harmless	Employer Held Harmless
Payroll Tax	+ $959	+ $934
Income Tax	+ $405	+ $327
Consumption Tax	- $206	- $429

	Increase in Cost of Production	
	Employee Held Harmless	Employer Held Harmless
Payroll Tax	2.5%	2.4%
Income Tax	6.3%	6.7%
Consumption Tax	6.6%	6.5%

NATIONAL HEALTH INSURANCE WOULD HURT AMERICA'S ABILITY TO COMPETE IN INTERNATIONAL MARKETS

A commonly held view in the U.S. business community is that health care costs in this country make U.S. products less competitive in the international marketplace. An example of this view is the frequently repeated assertion that health care costs add $700 to the price of every U.S. automobile. This statement is often followed by the assertion that American automobile manufacturers would be more competitive internationally under national health insurance. Both assertions are wrong.

Health Care and Competitiveness. There is no evidence whatever that private health insurance costs add anything to the price of an automobile — or of any other product. Health insurance is simply one element in the total compensation package of auto workers, a fringe benefit provided in lieu of money wages. Over the last two decades, fringe benefits for most American workers have grown steadily in real terms, while money wages have grown little, reflecting the preference of employees for nontaxed benefits over taxed money wages.

What workers are paid depends on what they produce, not what they consume. The fact that Americans spend a greater proportion of their income on health care and a smaller proportion on other goods and services does not put us at a competitive disadvantage relative to other countries.[20] As Table XIII shows,

- The Japanese spend a greater proportion of their income on food, but that doesn't mean that food consumption adds to the price of a Japanese car.
- The Canadians spend a greater proportion of their income on education, but that doesn't mean that education adds to the price of Canadian lumber.

These differences in consumption patterns merely reflect differences in consumer preferences and the relative prices of consumer products.

Taxes and Competitiveness. Although health care expenditures by themselves do not affect the competitiveness of U.S. exports in international markets, national health insurance would affect our ability to compete. This is because national health insurance involves not only the purchase of health care but also a redistribution of income among producers in different industries. On the whole:

- A national health insurance system would impose extra taxes on U.S. exporting industries and use the proceeds of those taxes to subsidize other industries.
- The industries which would receive subsidies are those which contribute mostly to domestic rather than international markets.
- The industries which would be penalized are the manufacturing industries which provide most of our exports.

National health insurance would raise the costs of our export goods and lower marketing costs in the U.S. for our foreign competitors. Far from making auto producers more competitive

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[20]See Uwe Reinhardt, "Health Care Spending and American Competitiveness," *Health Affairs*, Winter 1989, pp. 5-21.

in international markets, national health insurance would raise auto production costs relative to foreign rivals and make the industry less competitive.

Despite the fact that one-third of our federal budget goes to defense spending, a burden not equaled by our trading partners, taxes are still lower in the U.S. than in most other developed countries. As Table XIV shows, only Japan currently has a tax burden as low as ours. Were we to adopt a program of national health insurance, the U.S. tax burden would approach that of Britain and West Germany, and would be one of the highest among our trading partners. That additional burden would have a major impact on our ability to compete.

TABLE XIII

SELECTED CONSUMPTION EXPENDITURES[1] FOR MAJOR U.S. TRADING PARTNERS, 1986

	Food	Medical Care	Education	Housing and Fuel
Canada	11%	5%	12 %	21%
Japan	16%	10%	8 %	17%
United Kingdom	12%	8%	6 %	17%
West Germany	12%	13%	6 %	18%
United States	13%	14%	8 %	18%

[1]Expressed as a percent of total consumption expenditures.

Source: Figures derived using consumption data from the Organization for Economic Co-operation and Development.

TABLE XIV

TAXES AS A PERCENT OF GROSS DOMESTIC PRODUCT FOR MAJOR U.S. TRADING PARTNERS, 1986

	Taxes as a Percent of GDP
Canada	33%
Japan	29%
United Kingdom	39%
West Germany	38%
United States	29%
United States with National Health Insurance	36%

Source: Organization for Economic Co-operation and Development.

A FURTHER NOTE ON THE CONSERVATISM OF THE ASSUMPTIONS USED IN THIS REPORT

It is important to note again that the very conservative cost estimates used in this report put national health insurance in its most favorable light. Making more realistic assumptions would lead to even more pessimistic results. For example, it is almost certain that Medicare beneficiaries would be included in a program of national health insurance (add $30 to $40 billion) and it is highly likely that long-term care for the elderly would be tacked on as well (add $60 to $70 billion). It is also virtually certain that national health insurance would lead to a surge in demand for health care (add at least $50 billion), as has been the case in every other country. Thus only a modest move toward more realistic assumptions could add $150 billion to our estimate of the total costs of national health insurance.

NOTE: Nothing written here should be construed as necessarily reflecting the views of the National Center for Policy Analysis or as an attempt to aid or hinder the passage of any bill before Congress.

APPENDIX A

DESCRIPTION OF THE ESTIMATION METHOD

The Current Cost of Health Insurance Through the Workplace

Most nonelderly Americans obtain private health insurance through the workplace. In 1987, $120.1 billion of the $154.7 billion in private insurance premiums, or 78 percent, was contributed by employers on behalf of employees.[1] We estimate that employer-provided health care costs amounted to $157 billion in 1989.

Employees spend about the same amount out-of-pocket. In 1987, of the $438.9 billion spent on personal health care, private insurance covered $136 billion, direct payment from individuals covered $127.9 billion and government funds covered the remaining $169.6 billion.[2] Government funds go primarily to the elderly via Medicare and to the poor via Medicaid.

Health insurance coverage and costs vary by industry. Table 1 contains information on the earnings, employment and health care costs of production workers by industry. The information on the average weekly earnings and the number of production workers employed by industry are from the U.S. Department of Labor's Bureau of Labor Statistics establishment survey for July 1989.[3] Estimated average annual earnings were calculated by multiplying by 52.

The estimates of health care costs by industry are based on the U.S. Chamber of Commerce's *Employee Benefits: 1988 Edition*, which contains survey data from benefit year 1987. The employer health care costs were constructed by using the Chamber's reported health costs as a percent of payroll for each industry times the estimated average annual production worker earnings.

We estimated the 1989 average health care cost per production worker in the private nonagricultural sector to be $1,335. Health care costs range from $793 in retail trade to $3,231 in transportation and public utilities.

Average employer-provided health care costs vary across industries because of the generosity of the benefits and the percentage of workers covered. For example, only 48.6 percent of workers are covered in personal services industries whereas 88.1 percent are covered in manufacturing.[4]

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[1] *Survey of Current Business*, Vol. 69, No. 7, July 1989, Table 6.13; and Division of National Cost Estimates, Office of the Actuary, Health Care Financing Administration, "National Health Expenditures, 1986-2000," *Health Care Financing Review*, Vol. 8, No. 4, Summer 1987, Table 14, p. 27.

[2] *Health Care Financing Review*, Summer 1987, Table 14, p.27.

[3] U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings*, Vol. 36, No. 8, August 1989.

[4] Employee Benefit Research Institute, "A Profile of the Nonelderly Population without Health Insurance," *EBRI Issue Brief*, No. 66, May 1987, Table 12.

TABLE A-1

EARNINGS AND HEALTH CARE COSTS OF PRODUCTION WORKERS

Industry	Average Weekly Earnings	Number of Employees on Payroll (thous)	Estimated Average Annual Earnings	1989 Estimated Employer Health Care Per Employee
Total private nonagricultural	$333.38	74,317	$17,336	$1,335
Mining	$558.11	514	$29,022	$2,083
Construction	$502.74	4,305	$26,142	$1,876
Manufacturing				
Durable Goods	$457.87	7,760	$23,809	$2,065
Nondurable Goods	$390.51	5,732	$20,307	$1,580
Transportation & public utilities	$493.81	4,801	$25,678	$2,231
Wholesale trade	$392.43	5,049	$20,406	$1,644
Retail trade	$189.22	17,466	$9,839	$793
Finance, insurance & real estate	$339.03	4,988	$17,630	$1,066
Services	$302.80	23,702	$15,746	$1,130

Three Methods to Estimating Average National Health Expenses

National health insurance would cover the health expenditures of all Americans, regardless of age, income and other characteristics. Currently, the government sector pays 40.6 percent of the $550 billion in national health expenditures. Medicare and Medicaid account for most of these expenditures. This analysis assumes that national health insurance would use the tax revenues which now support Medicare and Medicaid to pay for the medical benefits of the elderly and the poor.

The remaining group, the non-aged, non-poor population would require a new financing system. The first step is to estimate the value of current insurance to workers in order to assess the costs and benefits of switching to an alternative financing scheme. Because there is not sufficient information to estimate directly the average health expenditure per employee by industry, we developed three independent methods to estimate indirectly the economy-wide average value of health insurance to workers.

Method 1: Gross-Up of Employer Insurance

Most employees (96 percent of employees of large firms and 74 percent of employees of small firms) obtain health insurance through the workplace.[5] The Health Care Financing Administration estimates that the percentage of total health expenses paid by private health insurance and direct out-of-pocket expenses are approximately the same.[6] Thus the $157 billion in employer health insurance contributions would be matched by another $157 billion in employee out-of-pocket expenditures.

The total expenditure of $314 billion would not include the 31 to 37 million Americans without health insurance. According to Senator Edward Kennedy, requiring employers to purchase coverage for 17 million uninsured workers and their families would add $22 billion to the cost for employers.[7] Costs for the remaining uninsured, those who are not workers or their dependents, would amount to another $7 billion.[8] Using the above relationship of private health insurance to personal health care expenditures, the total would have to include an additional $60 billion for a grand total of $374 billion spent for health care for the nonelderly.

Method 2: Ratio of Employer Expenditures

The Health Care Financing Administration estimates that private sources paid $268.5 billion for health care in 1986.[9] The Commerce Department reports that employers paid $115.3 billion of that amount.[10] In other words, employers paid 43 percent of all private expenses. Thus the $157 billion in employer health expenses we estimated for 1989 would translate into $364.9 in total private expenses. Adding the employer expenses which were used above for the uninsured, the estimated total expense would be $394 billion.

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[5]Employee Benefit Research Institute, *Employee Benefit Notes*, Washington, DC, December 1989, Vol. 10, No. 12, Table 3.

[6]National Center for Health Statistics: *Health, United States, 1988*, DHHS Pub. No. (PHS) 89-1232. Public Health Service, Washington. U.S. Government Printing Office, March 1989, Table 106, p. 160.

[7]Spencer, Rich, "Expanded Health Insurance Proposed," *Washington Post*, April 13, 1989, p. A20. Senator Kennedy claims that the cost of insurance for each covered worker and family would be $1,619, but the employer would pay only $1,295.

[8]Assuming 34 million uninsured, there would still be 11 million people not covered through the workplace. Assuming two people to a family, the cost would be 5.5 million times $1,295, or $7.1 billion.

[9]*Health, United States*, Table 105, p. 159.

[10]U.S. Department of Commerce, *Survey of Current Business*, Washington, DC, July 1989, Table 6.13, p. 83.

Method 3: Highest Reported Average Expenditure

The information in Table A-1 provides a third estimate of the average expenditure per employee. The employee benefits firm, A. Foster Higgins & Co., Inc., reports that surveyed employers who provided almost complete medical coverage for their employees spent an average of $3,366 per employee in 1989.[11] This amount corresponds closely to the $3,278 for the tires and inner tubes industry that we estimated using the U.S. Chamber of Commerce survey data. Table A-2 shows detailed estimates for selected manufacturing industries, and Table A-3 shows estimates for nonmanufacturing industries.

[11] "Medical Insurance Costs Climb 20%," *Washington Times*, January 30, 1990, C-1.

TABLE A-2

EARNINGS AND HEALTH CARE COSTS OF PRODUCTION WORKERS

Industry	Average Weekly Earnings	Number of Employees on Payroll (thous)	Estimated Average Annual Earnings	1989 Estimated Employer Health Care/ Employee
Manufacturing	$429.08	13,492	$22,312	$1,742
Durable goods	$457.87	7,760	$23,809	$2,065
Lumber & wood products	$357.94	654	$18,613	$1,570
Furniture & fixtures	$323.05	424	$16,799	$1,417
Stone, clay & glass products	$457.52	481	$23,791	$2,337
Primary metal industries	$533.46	606	$27,740	$2,585
Fabricated metal products	$437.85	11,081	$22,768	$2,035
Machinery, except electrical	$482.23	1,309	$25,076	$1,894
Office & computing machines	$466.07	155	$24,236	$1,831
Electronic computing equipment	$463.01	129	$24,077	$1,819
Electrical & electronic equipment	$423.50	1,198	$22,022	$1,608
Transportation equipment	$581.49	1,290	$30,237	$2,513
Motor vehicles & equipment	$611.46	674	$31,796	$2,642
Motor vehicles & car bodies	$706.92	270	$36,760	$3,055
Instruments & related products	$423.33	431	$22,013	$1,913
Photographic equip. & supplies	$593.01	51	$30,837	$2,679
Miscellaneous manufacturing	$324.26	287	$16,862	$1,465
Nondurable goods	$390.51	5,732	$20,307	$1,580
Food & kindred products	$390.51	1,192	$20,307	$1,585
Tobacco manufactures	$641.07	35	$33,336	$2,602
Textile mill products	$318.24	634	$16,548	$1,042

Apparel & other textile products	$236.11	932	$12,278	$773
Paper & allied products	$515.27	531	$26,794	$2,260
Printing & publishing	$401.68	895	$20,887	$1,552
Periodicals	$419.97	48	$21,838	$1,622
Chemicals & allied products	$551.23	622	$28,664	$2,238
Drugs	$522.44	108	$27,167	$2,121
Pharmaceutical preparations	$514.95	89	$26,777	$2,090
Petroleum & coal products	$684.28	110	$35,583	$2,778
Rubber & misc. plastics products	$390.10	662	$20,285	$1,967
Tires & inner tubes	$650.26	65	$33,814	$3,278
Leather & leather products	$254.65	119	$13,242	$1,284

Source: Figures derived from the U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings*, August 1989, and U.S. Chamber of Commerce, *Employee Benefits: 1988 Edition*.

TABLE A-3

EARNINGS AND HEALTH CARE COSTS OF PRODUCTION WORKERS

Industry	Average Weekly Earnings	Number of Employees on Payroll (thous)	Estimated Average Annual Earnings	1989 Estimated Employer Health Care/ Employee
Mining	$558.11	514	$29,022	$2,083
Construction	$502.74	4,305	$26,142	$1,876
Transportation & public utilities	$493.81	4,801	$25,67	$2,231
Communication	$518.48	981	$26,961	$2,342
Telecommunications	$568.84	659	$29,580	$2,570
Wholesale trade	$392.43	5,049	$20,406	$1,644
Durable goods	$406.84	2,967	$21,156	$1,705
Nondurable goods	$371.76	2,082	$19,332	$1,558
Retail trade	$189.22	17,466	$9,839	$793
General merchandise stores	$186.93	2,252	$9,720	$783
Department stores	$193.77	1,872	$10,076	$520
Finance, insurance & real estate	$339.03	4,988	$17,630	$1,066
Banking	$292.74	1,272	$15,222	$920
Credit agencies other than banks	$313.17	681	$16,285	$984
Insurance carriers	$395.86	978	$20,585	$1,322
Services	$302.80	23,702	$15,746	$1,130
Hotels & other lodging places	$205.30	1,447	$10,676	$766
Personal services	$216.72	700	$11,269	$809
Business services	$322.11	4,966	$16,750	$1,202
Computer & data processing svc.	$526.78	590	$27,393	$1,966
Auto repair services & garages	$310.06	744	$16,123	$1,157

Automotive repair shops	**$355.58**	**430**	**$18,490**	**$1,327**
Miscellaneous repair services	**$376.65**	**296**	**$19,586**	**$1,406**
Motion pictures	**$355.21**	**228**	**$18,471**	**$1,326**
Amusement & recreation services	**$209.67**	**995**	**$10,903**	**$783**
Health services	**$314.92**	**6,797**	**$16,376**	**$1,196**
Legal services	**$468.36**	**760**	**$24,355**	**$1,748**
Miscellaneous services	**$494.80**	**1,168**	**$25,730**	**$1,847**
Engineering & architectural svc.	**$540.36**	**636**	**$28,099**	**$2,017**
Accting, auditing & bookkeeping	**$413.09**	**390**	**$21,481**	**$1,542**

Source: Figures derived from the U.S. Department of Labor, Bureau of Labor Statistics, *Employment and Earnings*, August 1989, and U.S. Chamber of Commerce, *Employee Benefits: 1988 Edition.*

Using $3,366 per employee as an estimate of the average total expenditure per worker translates into an aggregate employee cost of $382.1 billion.[12] The $374 billion from method I implies an average expense of $3,200 per employee, and the $394 billion implies an average of $3,368. Because all three estimates are close, we decided to use $3,300 as an average employee medical expense for the study. Table A-4 recaps the major components of current national health expenses, adjusted to cover the uninsured.

[12]There were 117.5 million workers in 1989, of which, 100.5 were covered by health insurance..

TABLE A-4

NATIONAL HEALTH COSTS IN 1989
(in billions)

1989 Employer Health Payments	$156.9
Employer Coverage for the Uninsured	29.1
Out-of-pocket Health Payments	201.8
TOTAL EXPENDITURES	$387.8

Current Tax Subsidies for Employer-Provided Health Care

The federal government currently reduces the cost of health insurance purchased through employers by almost $50 billion. The exclusion of employer contributions for medical insurance premiums and medical care from federal income tax is worth about $28 billion in 1989.[13] Foregone social security payroll tax revenues amount to $20 billion.[14] Table A-5 shows the tax subsidies and the net cost which would have to be financed by a national health insurance plan.

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[13]Executive Office of the President, Office of Management and Budget, *Special Analyses, Budget of the United States Government, Fiscal Year 1989*, Washington, DC 1989, Table G-2, p. G-44. We have translated the $27.7 billion for fiscal year 1989 into $28.2 billion for calendar year 1989.

[14]About 86 percent of U.S. wages and salaries are above the social security wage ceiling and, therefore, not subject to FICA tax. The foregone FICA tax revenues due to employer-provided health insurance equals ($157 billion x 0.86 x 0.1502).

TABLE A-5

NATIONAL HEALTH SUBSIDIES IN 1989

Current Tax Subsidies	**48.5**
Income taxes	**28.2**
FICA taxes	**20.3**
NET NEW NHI FINANCING	**$339.3**

These costs would have to be paid with revenues raised via payroll taxes, personal income taxes, corporate income taxes, national sales or consumption taxes, or some combination of the four. Each mechanism would impact differently on specific industries and the U.S. economy in general.

NHI Tax Bases and Rates

Financing NHI expenditures of $339.3 billion would require the following payroll, income and consumption tax rates. There are slightly different tax bases and therefore rates, depending upon whether the firm or worker pays, because the amount of taxable money wages differs.

The payroll tax base is the taxable social security wage base under Alternative II- A from the 1989 Social Security Trustees' Report ($2,275 billion), plus the additional money wages from cashing out health benefits.[15]

The income tax base is taxable income from the 1987 Statistics of Income, adjusted to 1989 by using the square of the rate of growth in U.S. personal income between 1987 and 1988. Added to the income tax base are the money wages from cashing out health benefits.[16]

The consumption tax base is personal consumption expenditures in 1988, adjusted to 1989 by using its growth rate between 1987 and 1988.[17] The bases are the same for both alternatives.

Table A-6 shows the tax base and the rate necessary to finance each of the alternatives considered.

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[15]The Board of Trustees, Federal Old-Age and Survivors Insurance and Disability Insurance Trust Fund, *1989 Annual Report of the Board of Trustees Federal Old-Age and Survivors Insurance and Disability Insurance Trust Fund*, Washington, DC, April 1989, Table F1.

[16]Internal Revenue Service, Statistics of Income Bulletin Fall 1989, Washington, DC 1988, p 76.

[17]*Survey of Current Business*, July 1989, Table 1.1, p. 40.

TABLE A-6

TAX BASES AND RATES TO FINANCE NHI
(Dollar amounts in millions)

	FIRM PAYS		WORKER PAYS	
	Base	Rate	Base	Rate
Payroll	$ 2,448	13.86%	$2,399	14.99%
Income	2,353	14.42%	2,296	15.67%
Consumption	3,481	9.75%	3,481	9.75%

Effects of Different Taxes on the Cost of Goods

Overall, national health insurance would raise the cost of U.S. goods between 4 and 10 percent, depending upon the type of tax. The estimates by industry are constructed by separately estimating the impact of each type of tax on the price of the factors of production, and in the case of the consumption tax, on sales price.

The cost of goods impact of the payroll tax is constructed by remembering that workers supply their labor based on the aftertax compensation they receive. An increase (or decrease) in the aftertax compensation would represent a shift in the supply of labor. The new price of labor (ignoring quantity adjustments) would change by the same amount as payroll costs. Because historically labor costs represent two-thirds of total production costs, the payroll tax would change the costs of goods by two-thirds of the change in labor costs.

The income tax alternative follows the same method for the labor component of the production process. An income tax, however, also affects the cost of financing capital. Owners and suppliers of capital will demand a higher capital payment because of the new tax. The cost of capital, therefore, will increase by one over one minus the additional tax. Because capital accounts for one-third of production costs, the income tax adds one-third of the increase in the capital cost component plus two-thirds of the labor cost change to the cost of goods.

The consumption tax directly increases the cost of goods sold by the amount of the tax increase.

APPENDIX B

CHANGE IN HEALTH CARE COSTS AND COST OF PRODUCTION BY INDUSTRY AND TYPE OF TAX, ASSUMING EMPLOYEE IS HELD HARMLESS

	PAYROLL TAX		INCOME TAX		CONSUMPTION TAX	
Industry	Payroll Change	Cost of Goods	Payroll Change	Cost of Goods	Payroll Change	Cost of Goods
All workers	$343	1.1%	-$477	6.1%	-$993	6.3%
Total Nonproduction workers	$1,179	2.8%	$474	8.7%	-$541	8.3%
Total private nonagricultural workers	-$143	-0.5%	-$1,029	3.9%	-$1,256	4.8%
Mining	$1,901	4.1%	$1,243	10.2%	$24	9.7%
Construction	$1,385	3.3%	$670	9.2%	-$338	8.9%
Manufacturing	$778	2.2%	-$10	7.5%	-$689	7.7%
Durable goods	$1,168	3.0%	$411	8.6%	-$423	8.6%
Nondurable goods	$409	1.2%	-$419	6.3%	-$916	6.7%
Transportation & public utilities	$1,521	3.6%	$801	9.5%	-$204	9.2%
Wholesale trade	$459	1.4%	-$366	6.4%	-$878	6.8%
Retail trade	-$1,488	-9.3%	-$2,520	-8,2%	-$2,074	-4.5%
Finance, insurance & real estate	-$254	-0.9%	-$1,136	3.5%	-$1,361	4.4%
Services	-$478	-1.9%	-$1,396	2.0%	-$1,471	3.4%
Manufacturing	$778	2.2%	-$10	7.5%	-$689	7.7%
Durable goods	$1,168	3.0%	$411	8.6%	-$423	8.6%
Lumber & wood products	$168	0.6%	-$692	5.3%	-$1,047	6.0%
Furniture & fixtures	-$170	-0.6%	-$1,065	3.7%	-$1,256	4.7%
Stone, clay & glass products	$1,320	3.4%	$564	9.0%	-$295	8.9%
Primary metal industries	$2,007	4.4%	$1,328	10.5%	$118	10.0%
Fabricated metal products	$1,007	2.7%	$230	8.2%	-$515	8.2%
Machinery, except electrical	$1,247	3.1%	$513	8.8%	-$409	8.6%
Office & computing equip.	$1,095	2.8%	$344	8.4%	-$502	8.3%
Electronic computing equip.	$1,066	2.7%	$312	8.4%	-$520	8.3%
Electrical & electronic equip.	$662	1.9%	-$133	7.2%	-$774	7.4%
Transportation equip.	$2,313	4.7%	$1,681	11.0%	$271	10.4%
Motor vehicles & equip.	$2,602	5.0%	$2,001	11.4%	$450	10.7%
Motor vehicles & car bodies	$3,523	5.9%	$3,020	12.6%	$1,018	11.6%
Instruments & related products	$833	2.3%	$40	7.7%	-$630	7.8%
Photographic equip. & supplies	$2,490	5.0%	$1,871	11.3%	$395	10.6%
Miscellaneous manufacturing	-$134	-0.5%	-$1,028	3.8%	-$1,229	4.8%
Nondurable goods	$409	1.2%	-$419	6.3%	-$916	6.7%
Food & kindred products	$411	1.3%	-$416	6.3%	-$913	6.7%
Tobacco manufactures	$2,793	5,2%	$2,220	11.7%	$546	10.9%
Textile mill products	-$417	-1.6%	-$1,320	2.6%	-$1,453	3.7%
Apparel & other textile products	-$1,161	-5.9%	-$2,147	-3.4%	-$1,901	-0.9%
Paper & allied products	$1,693	3.9%	$993	9.8%	-$107	9.5%
Printing & publishing	$473	1.4%	-$344	6.5%	-$886	6.9%
Periodicals	$645	1.8%	-$153	7.1%	-$781	7.3%

Industry	PAYROLL TAX		INCOME TAX		CONSUMPTION TAX	
	Payroll Change	Cost of Goods	Payroll Change	Cost of Goods	Payroll Change	Cost of Goods
Chemicals & allied products	$1,939	4.2%	$1,275	10.3%	$23	9.8%
Drugs	$1,665	3.8%	$972	9.8%	-$145	9.4%
Pharmaceutical preparations	$1,594	3.7%	$893	9.6%	-$189	9.3%
Petroleum & coal products	$3,203	5.6%	$2,675	12.2%	$798	11.3%
Rubber & misc. plastics products	$624	1.9%	-$201	7.0%	-$734	7.3%
Tires & inner tubes	$3,242	5.8%	$2,683	12.4%	$903	11.5%
Leather & leather products	-$738	-3.4%	-$1,702	-0.3%	-$1,586	1.8%
Transportation & public utilities	$1,521	3.6%	$801	9.5%	-$204	9.2%
Communication	$1,762	4.0%	$1,067	10.0%	-$55	9.6%
Telephone Communications	$2,254	4.7%	$1,610	10.9%	$249	10.3%
Wholesale trade	$459	1.4%	-$366	6.4%	-$878	6.8%
Durable goods	$597	1.7%	-$214	6.9%	-$793	7.2%
Nondurable goods	$261	0.8%	-$586	5.7%	-$999	6.2%
Retail trade	-$1,488	-9.3%	-$2,520	-8.2%	-$2,074	-4.5%
General merchandise stores	-$1,510	-9.6%	-$2,544	-8.6%	-$2,088	-4.8%
Department stores	-$1,609	-10.1%	-$2,639	-9.0%	-$2,186	-5.3%
Finance, insurance & real estate	-$254	-0.9%	-$1,136	3.5%	-$1,361	4.4%
Banking	-$670	-2.8%	-$1,599	1.0%	-$1,610	2.4%
Credit agencies other than banks	-$486	-1.9%	-$1,395	2.2%	-$1,500	3.4%
Insurance carriers	$301	0.9%	-$523	6.0%	-$1,018	6.3%
Services	-$478	-1.9%	-$1,396	2.0%	-$1,471	3.4%
Hotels & other lodging places	-$1,387	-8.1%	-$2,404	-6.4%	-$2,024	-3.2%
Personal services	-$1,280	-7.1%	-$2,286	-5.1%	-$1,959	-2.1%
Business services	-$298	-1.1%	-$1,196	3.1%	-$1,362	4.2%
Computer & data process. svc.	$1,609	3.7%	$919	9.6%	-$202	9.2%
Auto repair, services & garages	-$411	-1.6%	-$1,321	2.5%	-$1,430	3.7%
Automotive repair shops	$14	0.0%	-$850	4.7%	-$1,172	5.4%
Miscellaneous repair services	$210	0.7%	-$633	5.5%	-$1,053	6.1%
Motion pictures	$10	0.0%	-$854	4.7%	-$1,174	5.4%
Amusement & recreation svc.	-$1,346	-7.7%	-$2,358	-5.9%	-$1,999	-2.8%
Health services	-$354	-1.3%	-$1,259	2.8%	-$1,393	3.9%
Legal services	$1,065	2.7%	$315	8.4%	-$533	8.3%
Miscellaneous services	$1,311	3.2%	$588	9.0%	-$383	8.7%
Engin. & architectural services	$1,735	3.8%	$1,059	9.9%	-$125	9.4%
Accting, auditing & bookkeeping	$549	1.6%	-$256	6.8%	-$846	7.1%