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The UK Shouldn't Copy The U.S. with Tax Breaks for Employer-Funded Healthcare

Ryan Bourne

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Jeremy Hunt's aim to forge a healthier British workforce is commendable. Yet his purported solution — offering tax breaks for employers providing health services — would risk lower wages, higher healthcare prices, more strains on NHS staffing capacity and disproportionate subsidies to large corporations, with no guarantee of improving health outcomes.

The chancellor is said to be considering a corporation tax "super-deduction" to encourage businesses to provide their workers with flu jabs, health check-ups and screenings. If it operates along the lines of the previous 130 per cent super-deduction allowance for investment, companies providing such services would be able to deduct more than this spending's cost from their taxable profit. For every £100 spent on health services, a company could subtract an extra £30 from their tax base compared with today. Given the 25 per cent corporation tax rate, their profit tax bill would fall by £7.50.

The obvious effect of this incentive is that firms would provide more qualifying health services. If certain health investments that enhance their workers' productivity become viable, this might come from new spending. More generally, we'd expect the financial incentive to encourage businesses to offer workers lower pay in favour of more benefits-in-kind.

Basic economics shows how this can destroy value. Suppose an employee values a health check-up at £180. If it costs the employer £200 to purchase at present, but £185 with the super-deduction, the employer would be more likely to provide this benefit. Yet this is inefficient: something with a market cost of £200 will be consumed despite being valued at far less by its recipient.

To encourage employees to demand these services, Hunt therefore is also mulling whether to tax these benefits-in-kind less heavily when received as income. This personal tax advantage would make workplace health benefits more valuable than before, on a pound-for-pound basis, compared with cash wages or an employee spending their own money on healthcare. It therefore acts as a subsidy to employer health benefits as remuneration.

This type of “tax subsidy” underpins the American model for private health insurance — a system that Michael Cannon, my Cato Institute colleague, calls the “original sin of healthcare policy” there. In the United States this personal tax exemption has stoked demand for healthcare, creating a damaging cycle of overconsumption and high prices. It shackles employees to their jobs, hindering worker mobility, while bribing workers to purchase coverage that is more likely to drop them when they are sick.

Does Hunt genuinely want to lead Britain in that direction? Companies already have strong incentives, remember, to offer cost-effective health services that make their workforce more productive. By offering subsidies beyond this, profitable businesses are being tempted to expand such services even when they don’t improve health.

Then there are the unintended consequences. The super-deduction would hand out a profit windfall to businesses and individuals who already offer physical and mental health services — an outright waste of funds. It’ll also invite an endless quarrel over what counts as a qualifying service. Flu shots, health check-ups, physical therapy and mental health evaluations might be straightforward to justify, but how about gym sessions, weight loss programmes and other therapy? Businesses will test the boundaries, sparking a contest of evasion and enforcement with HM Revenue & Customs.

Hunt might well argue that improving occupational health would yield broader societal benefits, justifying this new distortion between firms and workers. If people work longer, more productively, paying higher taxes, then pressure on the NHS and the long-run public finances might be eased. With government healthcare spending projected to soar from 9 per cent to approximately 15 per cent of GDP over the next half-century, we could use all the help we can get.

Yet America’s experience should cause us to pause: despite its tax incentives for private provision, it spends way more on healthcare than elsewhere, with an unhealthy population. Nor is it clear how much immediate relief subsidised private services would bring the NHS here. These carrots are supposed to improve health directly, leading to fewer workers retiring early or getting sick, freeing up NHS capacity to deal with backlogs and the long-term sick.

It seems plausible, however, that stoking health service demand through new tax breaks will crowd out some existing NHS capacity, particularly in the short term. After all, who will provide these extra services? Reports suggest the government wants retiring NHS doctors and nurses to take up private sector roles. But what if existing NHS staff are also enticed, exacerbating the strains of labour shortages?

Even if the government is right that more taxpayer support for worker health is desirable, tax breaks to businesses miss whole chunks of the population. Stuart Adam, a tax expert at the Institute for Fiscal Studies, says: “One question I’d ask is: do we want this to be something that’s specific to employer provision for employees?” He points out that the business-centric approach naturally excludes from subsidies the self-employed, those not working or employees funding their own healthcare.

Implementing the super-deduction through the corporation tax code also means the scale of subsidy is rather arbitrarily determined by the entity's corporation tax rate. "Right now," Adam says, "we have a lower corporation tax rate for small companies. And so we'd be giving weaker incentives to smaller companies, stronger incentives for the intermediate-sized companies . . . and no incentive at all for partnerships, non-profit organisations or public sector employers."

Right now, for every thirteen people working, one person is estimated to be long-term sick. A healthier population, achieved through relieving mental health problems or back and neck pain, is clearly desirable. But one only has to look to America to see the corrosive effects of hidden subsidies to encourage employer-led healthcare. There must be a better way.

Ryan Bourne occupies the R. Evan Scharf Chair for the Public Understanding of Economics at Cato and is the author of the recent book Economics In One Virus. *He has written on numerous economic issues, including fiscal policy, inequality, minimum wages, infrastructure spending, the cost of living and rent control*.