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Commentary

Playing Good Cop, Bad Cop

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President Obama campaigned hard for universal health insurance last fall, and is now feeling the pressure to deliver on it. In drawing up the legislative details, his administration provided the broad goals and principles. Meanwhile, the Democrats in Congress--who are, at least theoretically, able to ignore Republicans' preferences--employed a classic "good cop/bad cop" routine. This leaves the voters to subject the proposed legislation to closer scrutiny during coming weeks.

It has become clear that this health care "reform" effort is being driven by something other than the real and urgent need to reduce the nation's growing health care costs. The Congressional Budget Office recently declared that the administration's proposed mechanism for controlling health care costs--a Medicare Advisory Committee "on steroids"--would likely be ineffective.

What, then, explains the enormous political push to cover the uninsured? The customary justification for extending such coverage is that so many Americans simply cannot afford health insurance. Partly, this is the result of government regulations that cause segmented insurance markets. Moreover, in most insurance markets, those facing a low risk of loss prefer to forgo insurance coverage at average premium rates. It's no surprise, therefore, that a large segment of the uninsured are young individuals that are much less likely to experience health problems.

One explanation of the drive toward mandatory health insurance is the need to reinforce funding for Medicare, which is rapidly running out of revenues. The young will consume relatively few medical services, but their mandated coverage would provide a rationale for additional taxes. This is very similar to how Social Security's finances were buttressed repeatedly--by expanding coverage to additional occupations and population groups. It's the reason why the leadership of retiree lobbies is maintaining silence despite the possibility that the new program will introduce cuts in Medicare benefits.

The Democrats followed a standard maneuver to push forward their legislation in the House of Representatives. "Bad cop" Democrats first released a "tri-committee" health care reform bill packed with large and inefficient subsidies. The Congressional Budget Office's scored the proposal's net cost at a staggering $1 trillion over its standard 10-year budget-scoring window--through 2019. That almost derailed the entire effort. Thereupon, good cop Democrats--the "Blue Dogs"--stepped in to compel their liberal colleagues into shaving $100 billion from the initial proposal.

Note that, according to the proposed legislation, mandatory health insurance coverage will commence in 2013. Calculations based on information from the Centers of Medicare and Medicaid Services indicates that the program's true "10-year" net cost would become almost $2 trillion through the year 2022. That is, adding just another three years to the CBO's budget window doubles the net cost.

Taking an even longer view, we calculate that the permanent program would add $13.6 trillion to the federal government's total unfunded obligations in today's dollars. That is, the government would need to have that amount in the bank today, invested at interest, to fully finance the new program's subsidy costs as they come due. Social Security and Medicare actuaries estimate that these two programs' unfunded obligations under today's policies exceed $100 trillion (not billion) in today's dollars.

One way of financing the proposed health care mandate would be for the government to impose a large, uniform insurance premium on new enrollees, regardless of their health risks or needs. A similar approach failed miserably in Massachusetts, which now must find new resources to close its resulting budget gap. The Obama approach would impose those costs on rich individuals and high earners.

Unfortunately, funding the entire new long-term obligations by taxing the rich won't work. Based on data from the Urban-Brooking Tax Policy Center, households earning more than $200,000 per year bear an effective average income tax rate of 21.7% (total taxes at regular rates divided by total AGI). Requiring them to bear, permanently, an additional $13.6 trillion tax

liability would increase their effective average income tax rate to 32.5%.

But that assumes that their incomes would remain at current inflation-adjusted levels, which is surely incorrect. It's well established that higher tax rates--and especially the steep increase required here--would reduce those taxpayers' incentives to work and earn, create and expand businesses, hire workers and so on. That means an even higher tax increase will be needed, and the nation's long-term growth potential would be eroded.

The White House has emphatically countered recent hints from top administration officials that middle class taxes may have to be increased to control exploding federal budget deficits. That means the final health care legislation will likely involve significant medical regulations on patient choices, smaller medical reimbursements for providers and steeper premium increases for those already insured. But, over the long haul, we will be forced to contemplate similar changes given how significantly underfunded Medicare is already. Although we need to reduce health care costs, the entitlement expansion that Democratic lawmakers are proposing would only increase health care subsidies and push costs further upward. As voters closely examine these implications of the new mandatory health insurance program, public support is likely to evaporate--as it should.

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