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For fiscal health, end a tax exclusion: Christopher Swann

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-- Christopher Swann is a Reuters columnist. The views expressed are his own --
By Christopher Swann
NEW YORK, June 16 (Reuters) - President Obama's sales pitch for his healthcare plan rests on both humanitarian and financial appeals. Not only will he extend coverage to America's uninsured but he will help stem the ruinous rise in costs. On the first count he is convincing. On the second count much less so. Indeed the president opposes the most effective method of curbing healthcare inflation -- eliminating the employer-healthcare tax exclusion. This highly inefficient tax code lies at the heart of many of the woes of the U.S. health system and the country's fiscal disarray. Taking an axe to this tax break would be a step in the right direction.

The tax exemption on employer sponsored health insurance causes two big problems. First, it is the biggest exclusion in the tax code, costing around $150 billion a year -- twice the amount surrendered because of the mortgage-interest deduction. And it makes Americans remarkably insensitive to the price of medical services by creating the illusion that they are spending someone else's money.

As a result, Americans fiercely resist any effort to introduce more efficiency and have a penchant for unnecessary procedures. If you believe the Dartmouth Atlas of Healthcare, as much as 30 percent of U.S. medical spending may do nothing to improve health. A recent McKinsey study found that the United States spent nearly $650 billion more on healthcare than peer OECD countries, "even adjusting for wealth".

The costly idiosyncrasy has become perhaps the biggest menace to the nation's financial stability. Since America spends about 17 percent of national income on health -- compared with an OECD average of 9 percent -- rising costs pack a heavier economic punch. Health already consumes around a fifth of the U.S. federal budget and that is even before you take into account the monster tax exclusion. According to Obama's budget, the combined cost of Medicare and Medicaid alone is expected to double from $687 billion in 2009 to $1.34 trillion by 2019. During his presidential bid Obama spoke against even trimming the employer-healthcare tax deduction. He should reverse this stance. Some political cover for a volte face has been offered by Senator Max Baucus, chairman of the Finance Committee. By capping the tax free employer contribution at $13,000 a year for a family of four, the senator's proposal would raise about $420 billion over the coming decade -- a significant portion of the $1 trillion bill for covering the uninsured. Aside from sending a powerful signal of fiscal rectitude to the bond markets, it would also start to introduce much needed price-sensitivity into the U.S. system. Congress and the President should go further. Phasing out the employer tax exemption altogether and replacing it with an individual credit would be best of all. "If individuals rather than companies were allowed to shop for insurance, they would be more discerning and cost conscious," says Chris Edwards at the Cato Institute. Medical inflation can either be curbed by powerful government intervention or market pressure.

Obama seems to be choosing neither.
(Edited by David Evans)