IBDeditorials.com

Obama's Tax Flip-Flop On Health Benefits

By MICHAEL D. TANNER | Posted Friday, July 10, 2009 4:20 PM PT

The campaign ad was ominous: "John McCain would make you pay income tax on your health insurance benefits. Taxing health benefits for the first time ever."

So warned candidate Barack Obama less than a year ago. In ads and speeches, Obama went on to predict the horrific fallout of McCain's proposal: financial hardship and millions dumped from employer-provided health plans.

Today, spokesmen for President Obama are saying a tax on employer-provided health benefits wouldn't be such a bad thing after all.

Roughly 163 million Americans receive health insurance through their employer. While actually a form of compensation, the value of the employer's contribution to that insurance is not taxed under the federal income or payroll taxes.

This exclusion is a solidly middle-class tax benefit. More than 70% of middle-income, nonelderly Americans have employer-based health coverage. And about half of people with employer-based coverage have family income of less than $75,000.

Now, in a desperate search for $1 trillion to $2 trillion to pay for Obama's medical insurance reform plan, congressional Democrats are considering proposals to limit or repeal this tax exclusion. And the Obama administration says it may go along.

This reversal is far more than a simple case of hypocrisy or jettisoning a campaign promise once it becomes inconvenient.

The McCain proposal that candidate Obama so viciously attacked was part of a plan to shift the overall system toward market-based individual coverage. While it was true that McCain would have eliminated the exclusion for employer-provided health benefits, letting them be taxed like ordinary income, he would have given workers a tax credit for purchasing health insurance on their own or through an employer.

The result would have been that most workers would pay the same or less in taxes, with health markets more efficient and coverage more portable.

The proposals now discussed are nothing more than a naked grab for more tax money. There would be no offsetting tax credit. Workers would simply pay more taxes — a lot more taxes.

For example, if the income-tax exclusion were repealed, it would impose a $2.3 trillion tax increase over 10 years.

On average, employers pay $8,824 for a worker's insurance. Assuming tax rates of 10% to 38%, that means workers could expect to pay from $882 to $3,353 annually in additional taxes. Those with more expensive health plans, such as unionized auto workers, would face even bigger tax hikes.

Rather than fully repealing the exemption, Congress likely will put a cap on the tax exclusion. It would eliminate the income and payroll tax exclusion only for insurance plans with an above-average value or for workers with incomes above a certain level.

The problem is that, while more politically palatable, such a partial repeal of the exclusion wouldn't raise nearly enough money to pay for medical insurance reform. Eliminating the exclusion only for insurance plans with an above-average value would raise only $165 billion over 10 years.

And all this is only one of the middle-class tax increases Congress is considering to pay the enormous cost of the president's plan. Payroll tax hikes, a value-added tax, income tax surcharges, even taxes on beer and soft drinks are all on the table.

In the words of humorist P.J. O'Rourke: "If you think health care is expensive now — just wait until it's free."

Congress seems determined to pass medical insurance reform no matter what the price. And if the president has to break a few campaign promises and tax the American middle class, the path he is on indicates he is willing to pay up.

Whether middle-class Americans are is a different story.

Tanner is a senior fellow at the Cato Institute and co-author of "Healthy Competition: What's Holding Back Health Care and How to Free It."
