

Comments for the Record
United States House of Representatives
Committee on Ways and Means
Hearing on the Tax Ramifications of the Supreme Court's Ruling
on the Democrats' Health Care Law
Tuesday, July 10, 2012, 10:30 AM
by Michael G. Bindner
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Chairman Davis and Ranking Member Levin, thank you for the opportunity to submit my comments on this topic. We must note that because the law is actually part of the U.S. Code, it applies to all of us. As we pointed out in March, it is based on a model signed by the Republican Governor of Massachusetts and designed by the conservative leaning Heritage Foundation. The tax ramifications of the law being ruled constitutional go much beyond the impact of the taxing power to the viability of the mandate as written and the impact of the ruling that states who do not chose to participate in the expansion of Medicaid can do so without losing all Medicaid funding.

In our March comments, here is how we addressed the taxing power in relation to the law:

Before even considering the constitutionality of mandates under the Commerce Clause, the Supreme Court will examine if the mandate penalty is actually a tax and if it is a tax, whether consideration of this issue is even ripe. The Center for Fiscal Equity has always believed that this penalty is, in fact, a tax, and that the Court will likely quickly rule that it is and that further consideration of its constitutionality must wait until the tax is collected, leaving all other issues in abeyance until that occurs – although, frankly, it would be an act of judicial malpractice to let clients go forward on a what would be a Quixotic quest against the taxing power to bring this up again.

That is the first hurdle and it is the out that the Court is looking for to avoid the complicated constitutional question. The second is that the dollars funding the public relations campaign against the law are not brought out because the donors object to the mandate, but because the non-wage income payroll taxes which will take effect soon are costing rich people money - especially since there are no offsets to paying them or passing the cost to customers - essentially turning these taxes into a VAT. Indeed, a VAT would be less objectionable than keeping these taxes in place, because the burden is more broadly shared, more visible and refundable at the border.

It seems that we were mostly right on this issue, although we should have foreseen that the Court would not invoke the Anti-Injunction Act because the taxing power to do the mandate was not challenged, merely the use of the Commerce Clause. Any such challenge could be made, but it will not be ripe until this portion of the law takes effect, which is cold comfort to those who funded the legal challenge who will commence paying taxes on non-wage income at the beginning of the next calendar year. Among those commenting on the issue, we suspect our analysis was likely one of the best predictions, so we marvel at the fact that we have not been invited to testify on this issue.

As to the impact of the decision on the taxing power, we are given to understand that this decision relies on existing precedent, *United States v. New York* (*citation omitted*) so this does not break any new ground in the interpretation to lay and collect income tax, which is plenary as it is.

We also considered the Medicaid question. We missed this one by a mile, as demonstrated below:

As an aside, the objection to using the threat of loss of federal funding to enforce Medicaid reforms is a long objection of so called “Federalists” (who are in truth, states rights supporters, which is something different) has never gained much traction, from using highway funding to enforce the 55 mile per hour speed limit to using the same funding to force a 21 year old drinking age. It is an unsophisticated objection. I made the same argument in Iowa Model legislature when in High School – contending that the clause prohibiting differing regulations of commerce or revenue applied. Any first year law student or historian will point out that this clause applies to international trade, not the regulation of interstate commerce or the use of intergovernmental funds. We suspect that the Court has likely allowed it to be argued to kill this argument once and for all. To expect either a radical rethinking of the Commerce Clause or intergovernmental funding requirements will occur at this time is the legal equivalent of believing in unicorns.

While this precedent has nothing to do with the taxing power under the *Constitution*, it will likely make the eventual federalization of the entire Medicaid program all the more likely, along with a shift to consumption taxes to fund health care generally, rather than reliance on a combination of personal income taxes, the health insurance exclusion to corporate income taxes and the Hospital Insurance payroll tax.

We believed at the time that opposition to the Law had nothing to do with mandates, the Commerce Clause or Medicaid funding. The real reason conservative major donors don't like the law is the funding mechanism for much of reform. Wealthy donors were and are writing checks because of provisions creating additional taxes on un-earned income that fix Medicare Part A funding and fund other health care reform, essentially turning the Hospital Insurance Tax into a Value Added Tax with an exemption on profits paid to the 98%. Fighting for repeal on this basis, however, would only be politically unpopular.

Only judicial repeal of the whole law would have stopped this tax hike. While this might be possible under reconciliation, we believe that a point of order will be enforced against it in the Senate, so any reform that busts the budget is unlikely, especially provisions which repeal the new non-wage income tax. As much of the new tax was designed to make Medicare Part A viable, we find no logical ground to repeal it unless replaced by a broader consumption tax. As we stated in March:

Note that whenever this tax applies to those whose holding operate in less than a perfectly competitive market, in other words to most commerce in 21st century America, the costs will likely be passed to the consumer and it would be more honest to simply enact a Value Added Tax or VAT-like Net Business Receipts Tax (which is proposed below).

Our prior testimony on the adequacy of mandates is as applicable now as it was in March, if not more so. We believe that the stock market priced in repeal and may react negatively to the prospect of guaranteed issue and community rating. The Committee ignores these predictions at their own peril. As we stated previously:

We will now return to the question of the adequacy of mandates. The key issue for the future of health care consolidation is the impact of pre-existing condition reforms on the market for health insurance. Mandates under the Affordable Care Act (ACA) may be inadequate to keep people from dropping insurance - and will certainly not work if the mandate is rejected altogether for constitutional reasons.

If people start dropping insurance until they get sick – which is rational given the weakness of mandates – then private health insurance will require a bailout into an effective single payer system. The only way to stop this from happening is to enact a subsidized public option for those with pre-existing conditions while repealing mandates and pre-existing condition reforms.

In the event that Congress does nothing and private sector health insurance is lost, the prospects for premium support to replace the current Medicare program is lost as well. Premium support, as proposed by Chairman Ryan, also will not work if the ACA is repealed, since without the ACA, pre-existing condition protections and insurance exchanges eliminate the guarantee to seniors necessary for reform to succeed. Meanwhile, under a public option without pre-existing condition reforms, because seniors would be in the group of those who could not normally get insurance in the private market, the premium support solution would ultimately do nothing to fix Medicare's funding problem.

Resorting to single-payer catastrophic insurance with health savings accounts (another Republican proposal) would not work as advertised, as health care is not a normal good. People will obtain health care upon doctor recommendations, regardless of their ability to pay. Providers will then shoulder the burden of waiting for health savings account balances to accumulate – further encouraging provider consolidation. Existing trends toward provider consolidation will exacerbate these problems, because patients will lack options once they are in a network, giving funders little option other than paying up as demanded.

Shifting to more public funding of health care in response to future events is neither good nor bad. Rather, the success of such funding depends upon its adequacy and its impact on the quality of care – with inadequate funding and quality being related. For example, Medicare provider cuts under current law have been suspended for over a decade, the consequence of which is adequate care. By way of comparison, Medicaid provider cuts have been strictly enforced, which has caused most providers to no longer see Medicaid patients, driving them to hospital emergency rooms and free clinics with long waiting periods to get care.

Ultimately, fixing health care reform will require more funding, probably some kind of employer payroll or net business receipts tax – which would also fund the shortfall in Medicare and Medicaid (and take over most of their public revenue funding). We will now move to an analysis of funding options and their impact on patient care and cost control.

The committee well understands the ins and outs of increasing the payroll tax, so (we) will confine (our) remarks to a fuller explanation of Net Business Receipts Taxes (NBRT). Its base is similar to a Value Added Tax (VAT), but not identical.

Unlike a VAT, an NBRT would not be visible on receipts and should not be zero rated at the border – nor should it be applied to imports. While both collect from consumers, the unit of analysis for the NBRT should be the business rather than the transaction. As such, its application should be universal – covering both public companies who currently file business income taxes and private companies who currently file their business expenses on individual returns.

The key difference between the two taxes is that the NBRT should be the vehicle for distributing tax benefits for families, particularly the Child Tax Credit, the Dependent Care Credit and the Health Insurance Exclusion, as well as any recently enacted credits or subsidies under the ACA. In the event the ACA is reformed, any additional subsidies or taxes should be taken against this tax (to pay for a public option or provide for catastrophic care and Health Savings Accounts and/or Flexible Spending Accounts).

If cost savings under an NBRT, allow companies to offer services privately to both employees and retirees in exchange for a substantial tax benefit. Employers who fund catastrophic care would get an even higher benefit, with the proviso that any care so provided be superior to the care available through Medicaid. Making employers responsible for most costs and for all cost savings allows them to use some market power to get lower rates, but no so much that the free market is destroyed. The ability to exercise market power, with a requirement that services provided in lieu of public services be superior, will improve the quality of patient care.

This proposal is probably the most promising way to decrease health care costs from their current upward spiral – as employers who would be financially responsible for this care through taxes would have a real incentive to limit spending in a way that individual taxpayers simply do not have the means or incentive to exercise. While not all employers would participate, those who do would dramatically alter the market. In addition, a kind of beneficiary exchange could be established so that participating employers might trade credits for the funding of former employees who retired elsewhere, so that no one must pay unduly for the medical costs of workers who spent the majority of their careers in the service of other employers.

Employer provided health care will also reverse the trend toward market consolidation among providers. The extent to which firms hire doctors as staff and seek provider relationships with providers of hospital and specialty care is the extent to which the forces of consolidation are overcome by buyers with enough market power to insist on alternatives, with better care among the criteria for provider selection.

The NBRT would replace disability insurance, hospital insurance, the corporate income tax, business income taxation through the personal income tax and the mid range of personal income tax collection, effectively lowering personal income taxes by 25% in most brackets. Note that collection of this tax would lead to a reduction of gross wages, but not necessarily net wages – although larger families would receive a large wage bump, while wealthier families and childless families would likely receive a somewhat lower net wage due to loss of some tax subsidies and because reductions in income to make up for an increased tax benefit for families will likely be skewed to higher incomes. For this reason, a higher minimum wage is necessary so that lower wage workers are compensated with more than just their child tax benefits.

Thank you for the opportunity to address the committee. We are, of course, available for direct testimony or to answer questions by members and staff.

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