SUBJECT: Alternatives to an Employer Mandate

Summary: The best alternative to an "employer mandate" is an "individual mandate". Think about it as we do automobile insurance. Everyone who owns an automobile is required to have auto insurance; it's illegal to drive without it. We obtain this "universal automobile coverage" without an employer mandate. It is done entirely through an "individual mandate" to purchase insurance. The same principle could be applied to health insurance. In fact, several health proposals have individual mandates and achieve universal coverage, including the Chafee Bill, the Heritage Foundation proposal (the Nickles bill), and the American Enterprise Institute proposal (not introduced in Congress).

Outline

I. Individual mandates can guarantee universal coverage.

II. There are several other common objections to individual mandates, that are also false:

1. They cost too much.
2. They are too difficult to administer.
3. They will induce employers to stop paying for insurance.

III. In addition, individual mandates have several attractions:

1. They target subsidy dollars better.
2. They avoid economic distortions that employer mandates create.

The remainder of this memorandum walks through these issues.

I. Obtaining Universal Coverage

Once big new taxes (e.g., value-added taxes) are ruled out, there are two ways to obtain universal health insurance:

- *Employer Mandate:* Require employers to pay some of the cost of insurance coupled with a requirement that individuals pay the rest; or
- *Individual Mandate:* Require individuals to pay for insurance, with employers free to contribute as they choose and families paying the rest.

Both plans obtain universal coverage (because they force people to buy insurance); the only difference between them is whether employers are mandated to pay for insurance or not. Indeed, the two plans in every other feature are very similar:

Comparison of Clinton Plan and Individual Mandate

	Clinton Plan	Individual Mandate
Family Requirement	Must have insurance	Must have insurance
Payment From:		
1. Employers	*Required payment*	*Optional payment*
2. Families	The remainder (20% share plus non-worker payments)	The remainder
3. Government	Subsidy based on family income and firm wages	Subsidy based on family income
Net Effect	**Families obtain health insurance through employer and family payments**	**Families obtain health insurance through employer and family payments**

Example: A "perfect example" of an individual mandate is automobile insurance. All families with cars are required to have insurance. Employers can pay for auto insurance if they choose (although few do because there is no tax benefit to doing so). Families must pay the difference between the insurance cost and what their employer pays. The net effect (if compliance were 100%) is that everyone would have automobile insurance, and there would be no employer mandate.

There are several ways to implement an individual mandate for health insurance. Here is the way most consistent with the Clinton Plan:

	Action	Comparison
1.	Employers and employees decide how much the employer will contribute to health insurance. (In families with multiple workers, one or both employers can choose to pay.)	Clinton Plan has fixed payment.
2.	If remaining family payments are owed, the family designates which employer is to withhold these payments. Non-workers pay directly.	Same as Clinton Plan.
3.	Family files a form indicating how payments will be made, and whether subsidies are applicable.	Same as Clinton Plan.
4.	Payments from employers, families, and the government are made to the health alliance. Family chooses health plan.	Same as Clinton Plan.

A second way to run the system is to have families receive a voucher for health insurance from the government, with payments for the voucher based on the family's income.

A third way to run the system is to have tax credits for the purchase of health insurance. The credit amount phases out as the family's income increases. The credits are refundable so that families receive the full value of them even if they pay no taxes. (This is the mechanism in the Nickles Plan, for instance.)

Here are some examples of how different families would compare under the Clinton Plan and an individual mandate.

Comparison of Payments Under Clinton Plan and Individual Mandate

Family	Clinton Plan	Individual Mandate
Two Workers	Each employer pays $2,479 Family pays $872	Employers pay up to $4,360 Family pays the remainder
One Worker	Employer pays $2,479 Family pays $872	Employer pays up to $4,360 Family pays the remainder
Non-worker	Family pays non-worker premium of $2,479 Family pays $872	Family owes $4,360

II. Objections to an Individual Mandate

There are three common objections made about individual mandates. Neither of these objections is necessarily true.

Objection 1: Individual mandates cost the government too much money.

Fact: Preliminary calculations suggest that an individual mandate costs no more than an employer mandate. This is because low-income families and their employers are already receiving substantial subsidies under the Clinton Plan. These subsidies can be kept the same in total and redirected to more needy families under an individual mandate.

Consider a family with $15,000 annual income and whose health insurance cost is $4,360, or 29 percent of income.

Payments and Subsidies Under the Clinton Plan

Payments		Subsidies	
Family Payment:	$450 (3%)	Family:	$422 (2.8%)
Employer Payment:	$1,185 (7.9%)	Employer:	$2,303 (15.4%)
Total Payments:	$1,635 (10.9%)	Total:	$2,725 (18.1%)

The family pays about 11 percent of income for health insurance. The average for poor families in the Clinton Plan is about 12 percent. Thus, an individual mandate that limited total payments for each worker (employer plus family payments) to about 12 percent of income would cost about the same as the Clinton Plan. A program which subsidized only family payments would cost less. Subsidies of both of these forms can easily be devised.

Objection 2: Individual mandates are impossible to administer.

Fact: If mandatory withholding of health insurance premiums is required under an individual mandate, the administrative burden in the two systems seems comparable. In fact, an individual mandate is easier to administer in some parts.

There are possible administrative functions that might have to occur in any health insurance system:

Administrative Action	Difficulty
Collecting money from employers	Easy
Coordinating among multiple employers within a family (e.g., which employer is supposed to be paying)	Moderate
Reconciling family income and insurance payments at end of year	Difficult
Collecting money from families	Very difficult (without mandatory withholding)

Clearly, the optimal individual mandate would run as much of the payment as possible through the employer, to avoid having to collect from families. (Indeed, the compliance rate for automobile insurance would be much higher if we had mandatory withholding of auto insurance payments.) In an individual mandate with mandatory withholding, the administrative burden is comparable -- both would have to coordinate family payments among employers, would have to reconcile income and subsidies, and would have to collect from non-workers.

In fact, the individual mandate is easier in at least one dimension. Under the Clinton Plan, the government has to know how many months a family is employed, to determine if non-worker payments are due. This is not required under an individual mandate because all that matters is total annual income, not the distribution of that income between wages and other sources.

Objection 3: Individual mandates will encourage employers to drop coverage.

Fact: If subsidies are given on all payments for health insurance (employer and family) and there is any tax preference left for employer payments, there will be no incentives created to drop payment. Further, there are measures that can be taken to minimize the risk of dropped coverage.

On the issue of the financial incentives to drop coverage, consider the following questions:

Question	Yes	No
Are subsidies given on employer payments as well as family payments?	Neutral between paying or not	Subsidies increase if coverage is dropped
Is there any tax preference for employer payments (even at the lowest cost plan)?	Incentive for employers to pay	Neutral between paying or not

It is clearly possible to design a system where employers will still have financial incentives to pay for health insurance (allow subsidies for employer payments and some tax preference). It is also possible to design systems where there are incentives for employers to drop coverage (subsidize only family payments and allow no tax preference). These two questions can be part of the policy design process, however. Note that the Cooper and Chafee plans subsidize payments only if the family makes them, and thus have some incentive to drop coverage. This is potentially a problem with these plans.

As additional protection against employers dropping coverage, there are two other proposals that can be made:

- All employers are required to tell their employees annually what they are paying for their health insurance. If the employer drops coverage, the employee has the right to demand this amount as additional wages.
- For a period of 5 years, employers are prohibited from dropping coverage if they current provide it (maintenance of effort).

III. Attractions of an Individual Mandate

The attractions of an individual mandate stem from the fact that employer subsidies are given based on the worker's wage and the average wage of the firm, not the family's income:

Payment for Workers In Different Firms

	Low Wage Firm (7.9% cap)	High Wage Firm (no cap)
$10,000 per year worker	$790	$2,479
$50,000 per year worker	$3,950	$2,479

There are two points to note about these differences.

Issue	Equity Considerations	Economic Considerations
Low-wage workers who work in high wage firms do not receive a subsidy (e.g., the $2,479 payment)	These workers are "just as deserving" as workers in low-wage firms, and therefore should receive a subsidy	• Possible adverse employment effects (small but possible) • **Large incentive to contract out services of low-wage workers so they receive a subsidy (outsourcing)**

The individual mandate subsidizes all families on the basis of family income, not the wage of the firm they work in, so this is not an issue.

Low-wage workers in families with high incomes may receive a subsidy if they are employed in a high-wage firm (e.g., the $790 payment)	These workers are not really deserving of a subsidy (family is rich)	No large economic effects

The individual mandate avoids this subsidy because the family would have too much income to quality.