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Will Federal Health Legislation Cause the Deficit to Soar?

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The health care plan approved by the Senate Finance Committee is supposed to reduce budget deficits over 10 years by $81 billion, according to the Congressional Budget Office.[1] Similarly, the House version of health legislation would reduce 10-year deficits by $104 billion, according to the CBO.[2] Supporters of these health care proposals thus argue that the plans are fiscally responsible.

However, enacting a $1 trillion entitlement program would greatly increase the burden of government spending. In addition, promises of lower deficits are a triumph of hope over experience. Government forecasters have a very poor track record of predicting costs. More realistic assumptions suggest that health legislation could easily push up 10-year deficits by $600 billion.

Government-run health care will cost more than the politicians are telling us. The tax increases will not collect as much money as the politicians think. And, to put it mildly, promises of future spending restraint are naïve. The following are some of the reasons why current federal health proposals will mean not just more spending and higher taxes, but also larger deficits and added debt.

1. The Senate plan would increase federal spending by nearly $900 billion, while the House plan would increase spending by more than $1.2 trillion, according to the CBO. These estimates are far too low because they do not properly measure how people and businesses change their behavior in response to government handouts.

2. Errors in forecasts by the Congressional Budget Office and Joint Committee on Taxation could have large fiscal implications. If revenues and offsets are 25 percent below the forecast and spending is 50 percent higher than estimated, the 10-year deficits will be $602 billion to $860 billion higher.

3. There are incentives for companies to dump their health plans since workers will then get more take-home pay and be able to obtain health insurance using subsides and handouts from the government. This will dramatically increase budgetary costs.

4. The spending estimates are far too low because they do not recognize that politicians in the future will be tempted to expand subsidies as part of routine vote-buying behavior, similar to what happened with Medicare and Medicaid.

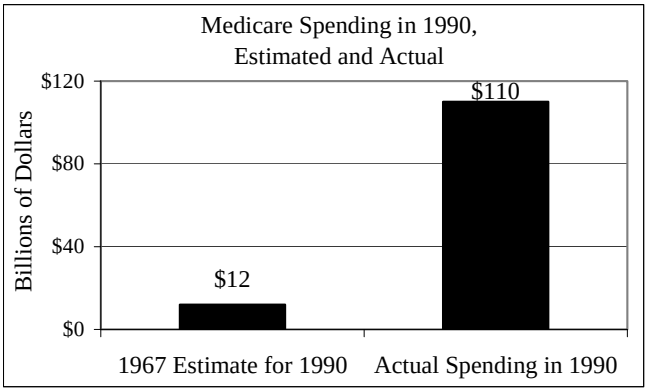
5. Future savings in the Senate plan are based on unrealistic gimmicks such as a “Medicare Commission” and a “Failsafe Budgeting Mechanism.” These absurd ploys share one thing in common—a hollow commitment to be frugal in the future while spending more today.

6. Even the savings that might be real—such as reductions in Medicare payment rates for physicians’ services in the Senate plan—are pushed off into the future, where they can be cancelled by politicians seeking to curry favor with key constituencies.

7. Much of the new spending is “backloaded,” meaning that it does not take effect for several years. This makes the long-run costs appear deceptively low. More than 90 percent of the spending in the Senate plan takes place in the second five years of the 10-year projection, and more than 84 percent of the spending in the House plan is also in the last five years.

8. Outlays in both plans will be climbing by about 8 percent annually toward the end of the 10-year period, much faster than growth in the overall economy.[3]

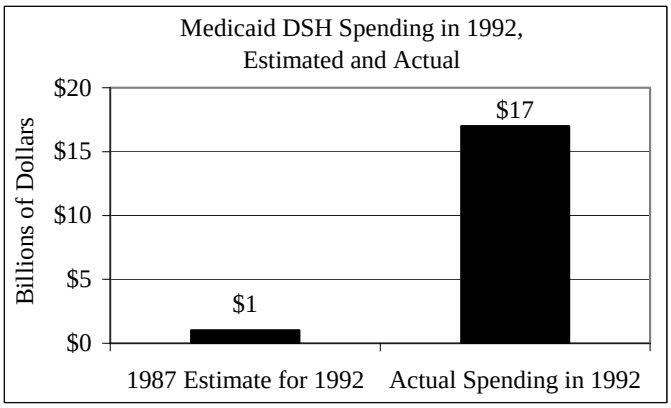
9. The federal government's ability to predict healthcare spending leaves much to be desired. When Medicare was created in the 1960s, the long-range forecasts estimated that the program would cost about $12 billion by 1990. It ended up actually costing $110 billion that year, or nine times more than expected.[4]



Source: Joint Economic Committee.

10. When Medicaid was created in 1965, it was supposed to be a very small program with annual expenditures of about $1 billion.[5] It has now become a huge $280 billion per year burden for federal taxpayers.

11. Medicaid's disproportionate share hospital (DSH) program is a sobering example. Created in 1987 to subsidize hospitals with large numbers of uninsured patients, the program was supposed to cost $1 billion in 1992, but actually cost a staggering $17 billion.[6]



Source: Joint Economic Committee.

12. The Medicare Catastrophic Coverage of 1988 was repealed after less than two years, in part because some provisions were already projected to cost six times more than originally forecast.[7]

13. The tax provisions in the health proposals will impose considerable damage while raising less revenue than expected. The House legislation will supposedly raise more than $460 billion from higher income tax rates, but actual collections would likely be far smaller because of reduced incentives to earn income and increased incentives to avoid and evade taxes.

14. The Senate plan has big tax increases on high-cost insurance policies, medical devices, and health insurance providers. However, a substantial share of those projected revenues would evaporate as businesses and consumers alter their behavior to protect themselves from the taxes.

15. With the phase-out of insurance subsidies in some plans, taxpayers with modest incomes will face marginal tax rates of nearly 70 percent, a staggering penalty on upward mobility that will hinder overall economic performance.[8]

16. To add insult to injury, the Internal Revenue Service would get new enforcement powers to determine if people have acceptable (in the eyes of politicians and bureaucrats) health insurance.

Deficits and debt will skyrocket if government-run healthcare is expanded. This will happen if either the House or Senate plan becomes law. Big increases in federal spending and higher taxes are a bleak combination that would substantially slow U.S. economic growth.

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[1] Congressional Budget Office, letter to Senator Max Baucus (D-MT), October 7, 2009.
[2] Congressional Budget Office, letter to Representative Charles Rangel (D-NY), October 29, 2009.
[3] Congressional Budget Office, letter to Senator Max Baucus (D-MT), October 7, 2009.
[4] Joint Economic Committee, "Are Health Care Reform Cost Estimates Reliable?" July 31, 2009. The JEC cites 1967 testimony by Robert J. Myers.
[5] Clay Chandler, "Health Care Costs a Long-Term Headache," *Washington Post*, October 17, 1993.
[6] Joint Economic Committee, "Are Health Care Reform Cost Estimates Reliable?" July 31, 2009.
[7] Marilyn Moon, "The Rise and Fall of the Medicare Catastrophic Coverage Act," *National Tax Journal* 43, no. 3 (September 1990).
[8] Greg Mankiw, "Marginal Tax Rates from Health Reform," October 10, 2009.