Employer Provision of Health Insurance

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Economics 156/256
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Sources of Coverage: under 65 population

<table>
<thead>
<tr>
<th>(percentage)</th>
<th>1987</th>
<th>1998</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total population</td>
<td>100.0%</td>
<td>100.0%</td>
</tr>
<tr>
<td>Employment-based coverage</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Own name</td>
<td>33.8</td>
<td>33.1</td>
</tr>
<tr>
<td>Dependent coverage</td>
<td>35.4</td>
<td>31.7</td>
</tr>
<tr>
<td>Individually purchased</td>
<td>6.7</td>
<td>6.5</td>
</tr>
<tr>
<td>Public</td>
<td>13.3</td>
<td>14.3</td>
</tr>
<tr>
<td>No health insurance</td>
<td>14.8</td>
<td>18.4</td>
</tr>
</tbody>
</table>

Notes: From EBRI (2002)
Health Insurance Loading

\[ \text{premium} = (1 + L) E(B) \]

\[ L = \text{Loading} \]

\[ E(B) = \text{Expected Benefits} \]
Estimates of Loading by Group Size

Table 10.3  Typical Loading by Group Size

<table>
<thead>
<tr>
<th>Number of Employees</th>
<th>Loading Fee (as a % of benefits)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Individual policies</td>
<td>60-80%</td>
</tr>
<tr>
<td>Small Groups (1-10)</td>
<td>30-40%</td>
</tr>
<tr>
<td>Moderate Groups (11-100)</td>
<td>20-30%</td>
</tr>
<tr>
<td>Medium Groups (100-200)</td>
<td>15-20%</td>
</tr>
<tr>
<td>Large Groups (201-1000)</td>
<td>8-15%</td>
</tr>
<tr>
<td>Very Large Groups (&gt;1,000)</td>
<td>5-8%</td>
</tr>
</tbody>
</table>

Source: Phelps (1997)
Tax treatment lowers the price of insurance

<table>
<thead>
<tr>
<th></th>
<th>Marginal tax rate= 28%</th>
<th>After-tax purchase</th>
<th>Pre-tax purchase</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Wage</td>
<td>$1000</td>
<td>1000</td>
<td></td>
</tr>
<tr>
<td>Pre-tax premium</td>
<td>-</td>
<td>50</td>
<td></td>
</tr>
<tr>
<td>Tax Payment</td>
<td>280</td>
<td>266</td>
<td></td>
</tr>
<tr>
<td>Net Cash Wage</td>
<td>720</td>
<td>684</td>
<td></td>
</tr>
<tr>
<td>After-tax premium</td>
<td>50</td>
<td>-</td>
<td></td>
</tr>
<tr>
<td>Take Home Pay</td>
<td>670</td>
<td>684</td>
<td></td>
</tr>
</tbody>
</table>
Is the Subsidy Equitable?

Average Federal Health Benefits Tax Expenditure, 1998

Sheils and Hogan (1999)
Insurance Status by Household Income

Increases the quantity of health insurance purchased
The role of the employer in the purchase of health insurance
Who bears the cost of employer-sponsored coverage?
Do employers make “good” choices for workers?

Cash wages

Insurance

W₁

O  I₀  I₁

A
What if workers vary in their preferences for health insurance?
Barriers to Offering Choice

• Favorable tax treatment is contingent upon meeting non-discrimination requirements
• Fixed costs of offering multiple plans
  – Administrative costs
  – Loading
Note: Nationwide, there are about 6,290,665 firms with 3-199 workers and 85,448 with 200+ workers.


^ Estimate is statistically different (p<0.1) from the previous year shown: 2000-2002.

Percentage of Employers Providing a Choice of Health Plans, by Firm Size, 2002

- **All Firm Sizes**
  - One Plan: 2%
  - Two Plans: 92%
- **All Small Firms** (3-199 Workers)
  - One Plan: 2%
  - Two Plans: 93%
- **Midsize Firms*** (200-999 Workers)
  - One Plan: 5%
  - Two Plans: 25%
- **Large Firms*** (1,000-4,999 Workers)
  - One Plan: 23%
  - Two Plans: 48%
- **Jumbo Firms*** (5,000 or More Workers)
  - One Plan: 28%
  - Two Plans: 66%

* Distribution is statistically different from All Firms.

Percentage of Covered Workers With a Choice of Conventional, HMO, PPO, or POS Plans, 1988-2002


^ Information was not obtained for POS plans in 1988.

Average Monthly Worker Contribution, 1988-2002


Percentage of Premium Paid by Covered Workers, 1988-2002

Labor Market Distortions

• Anecdotal evidence of job lock:
  – 11-30% of individuals report that they or a family member have remained in a job at some time because they did not want to lose health insurance coverage.

• Types of job lock
  – Job to job mobility
  – Self-employment decisions
  – Delaying retirement
# Empirical Evidence

<table>
<thead>
<tr>
<th>Value of health insurance</th>
<th>No</th>
<th>Yes</th>
</tr>
</thead>
<tbody>
<tr>
<td>High</td>
<td>$M_{00}$</td>
<td>$M_{10}$</td>
</tr>
<tr>
<td>Low</td>
<td>$M_{01}$</td>
<td>$M_{11}$</td>
</tr>
</tbody>
</table>

Test 1: $(M_1 - M_0)$

Test 2: $(M_{10} - M_{00}) - (M_{11} - M_{01})$
Summary

• The purchase of employment-based health insurance is highly subsidized, particularly for high income workers and their families.

• On average, the incidence of health insurance premiums falls on workers, not firms.

• Employers have incentives to respond to the preferences of their workers when choosing health insurance.