

The Equity Effect of Universal Health Care

A Guide to Reducing Income and Wealth Gaps through Public Health Care Financing

Universal health care, or Medicare for All, seeks to provide health care as a right and a public good to all residents. This requires taking health care out of the market and financing it publicly, through the tax system. Everyone gets the care they need, regardless of how much money they have.

Task forces in California, Oregon and Washington are planning a transition to universal health care, as are the presidential candidates supporting a national Medicare for All program. But they are faced with fear-mongering about tax hikes, fueled by a reluctance among both advocates and legislative champions to openly discuss financing issues. This brief takes a different approach. While it is true that most revenue would come from re-directing existing funding streams, we look at who would be paying the taxes replacing premiums and out-of-pocket costs. We conclude that at a time when wealth is transferred upwards at record levels, universal health care would lead to a more equitable sharing of wealth and income.

Universal health care financing: from “*how much*” to “*who pays*”

Universal health care advocacy has long relied on talking about cost savings. That’s because all evidence shows that publicly financed health care will reduce costs. Yet the truly powerful message remains hidden: whose costs? That the health system will be cheaper in the aggregate is hardly meaningful to people if it is unclear who will benefit. What really matters is that a publicly financed system will reverse who pays for it. In the current market-based system, people with health issues and those with low and moderate incomes are most burdened by health care costs. The wealthy, on the other hand, spend much less of their income on health care. Universal health care flips this relationship between health and wealth: payments would be independent of health status but increase with wealth and income. By changing how we pay for health care, we can increase economic equity.

The equity effect of universal health care

In a universal, publicly financed health care system, most of us will spend a smaller share of our income on health care, while only the wealthy will contribute more. All studies point to this equity effect, but what makes it possible? Simply put, public financing eliminates the set dollar amounts we pay for premiums, deductibles and out-of-pocket costs, and replaces these with tax rates proportional to our income (or wealth, or consumption, depending on what is being taxed). Instead of paying a fixed amount, we contribute a percentage of our income, which means those who earn more, will pay more. This reverses the current distribution of health care payments: in the market system, the more money a household makes, the less they pay for health care as a share of their income. In a universal, public system, this regressive financing model will become progressive: those with more money need to contribute more. Although the degree of progressivity will depend on the tax design, the overall effect will be a shift toward greater distributional equity. The following examples illustrate this.

The first chart, reflecting a proposal by RAND for financing universal health care in Oregon, shows that a universal public system will turn a regressive payment curve into a progressive one. While the existing system has poor and middle income families pay the largest share of their incomes on health care, the universal public system flips who pays for health care: the more income a household has, the more they would pay. In this proposal for Oregon, this payment would be in the form of income and payroll taxes. How big this equity effect is — the degree of progressivity — depends on how health care

taxes are designed. The second chart illustrates PERI's projections for universal health care in California. Poorer and low income households would pay much less in the universal system, whereas wealthy households would pay more than they do now. Yet the proposed tax mix — sales and gross receipt taxes — produces a near flat line rather than a progressive curve. This means most people would pay a similar share for health care, despite their different incomes and wealth. This is the effect of taxes based on consumption. Everyone — poor and rich — has to pay the same tax on a purchase they make, regardless of their income or wealth.

Treating the smallest businesses equitably

Businesses can also benefit from the equity effect of universal, publicly financed health care. The third chart illustrates how health care payments made by different size companies would be more progressive in a national Medicare For All system, compared to the current employer-sponsored insurance model. In these two scenarios, small businesses would pay significantly less, while large corporations would pay more. The extent to which small businesses would benefit depends on the type of tax, coupled with the extent of bottom exemptions: in this particular model (Chart 3) a gross receipts tax (GRT) appears more progressive than a payroll tax. Further, small businesses that currently do not offer insurance — not shown in the chart — would see no change with a GRT (which includes a larger bottom exemption), but a slight increase with a payroll tax. However, this model does not take into account that the costs of a GRT tend to be passed on to consumers.

Advancing racial and gender equity

Equity effects would also benefit population groups that are particularly impacted by fiscal, economic and health care injustice. Public financing for universal health care creates a positive distributional effect for people of color and women, increasing their net disposable incomes. While racial health disparities are widely recognized, racial income disparities caused by regressive health care payments have received less attention. As people of color tend to be overrepresented among lower-income households, they are disproportionately affected by regressive financing. Further, they are more likely to be under- and uninsured, which tends to increase out-of-pocket costs. Similarly, women, and especially women of color, are more likely to have lower incomes, which means high premiums and cost-sharing affect them more than men. A greater share of women's income goes toward out-of-pocket costs, also because women have greater health care needs. Universal, publicly financed health care would end this unjust distribution of costs burdening people of color and women.

Which types of taxes have the greatest potential for maximizing equity?

Universal, publicly financed health care increases the progressivity of health care payments across income groups. This means it redistributes disposable income from higher to lower-income households, and from white households to families of color.

Yet there are significant differences in how big this equity effect is, depending on the type of taxes chosen. To illustrate these differences Table 1 provides an overview and equity assessment of the main financing proposals put forward in states that are or have been considering universal health care bills, and of a financing proposal for a national Medical for All program. Based on the studies we reviewed, Table 1 summarizes the proposed tax structures and their projected distributional impacts on households and businesses. This comparison shows that when the financing design of universal health care includes the following features, it will maximize equity.

- **Taxes that target the wealthy directly**, such as taxes on financial and physical assets, and on capital income, will redistribute wealth from richer to poorer households. Options include a new health tax on wealth, increased tax rates on unearned income, including capital gains, and higher top marginal income tax rates. New York's universal health care bill mandates health care taxes on unearned income.
- **Graduated tax rates** that increase with income will ensure that taxpayers contribute according to their ability. Although flat tax rates would be better than fixed premiums, as people who earn or buy

more would pay more, they are regressive in so far as a higher share of poorer families' income would go toward health care payments. New York and Oregon's bills mandate some form of graduated taxes.

- **Exemptions for poorer households** or for necessary goods can mitigate the impact of otherwise flat or regressive taxes. Several proposals include exemptions targeted at Medicaid beneficiaries and low-income people more generally. However, some of these measures, particularly tax credits for poor people, may be politically unstable, as they are easily revoked if attacked as special provisions for certain groups.
- **A highly progressive tax structure that applies to everyone** would be more sustainable in the long run. Ultimately, a regressive tax (e.g. a tax on consumption rather than income) does not advance redistribution, even with exemptions or credits. The sales tax proposed in California curtails the equity effects of universal health care, as seen in comparison with the federal proposal, which uses a wealth tax to counterbalance the sales tax's regressive effects.
- **Businesses must not be let off the hook** when moving from employer-sponsored insurance (which currently covers over half the non-elderly population) to publicly financed health care. Capturing existing employer contributions is a key reason for the popularity of payroll taxes in current financing proposals. New York's bill mandates a graduated payroll tax with employers paying 80% and workers 20%. Yet employers tend to shift the cost of their premium share onto workers by reducing wages. Once businesses save costs with universal health care, positive wage effects are expected, but this is unlikely to happen automatically. The Oregon study suggests wage passbacks during the transition period. A more permanent incentive for increasing wages was proposed by Vermont's Healthcare Is a Human Right campaign, which designed a payroll tax that uses wage disparity as a factor in setting tax rates. A gross receipts tax with a generous bottom exemption could be a progressive alternative to a standard payroll tax, according to PERI's calculations, especially since it avoids employment disincentives. Yet a GRT may simply shift the burden from businesses to consumers (rather than from businesses to workers).
- **Equity concerns apply to businesses too.** If small businesses are disproportionately burdened, as in the flat payroll tax proposal by Vermont's governor, the financing of universal health care may be jeopardized. Taxes on businesses require graduated tax rates starting a zero or bottom exemptions.

Addressing transition challenges through equitable financing

Many proposals contain pro-active solutions to some of the sticky financing questions that can affect the transition to universal health care. As we have seen in Vermont at the end of 2014, an ill-advised financing plan that does not work for the majority of people and businesses can slow down or even derail universal health care. Here are some ideas on how an equity focus can help:

- **Sharing universal health care savings equitably:** savings for businesses must translate into savings for workers. Oregon's proposal seeks to address this through wage passbacks to workers.
- **Incentivizing positive wage effects for workers:** Vermont's HCHR campaign proposed a tax on wage disparity to boost median wages while avoid hiring disincentives. Since then, a new transparency rule requiring the disclosure of the CEO-worker pay ratio has spurred wage equity related tax initiatives. Portland, Oregon, now imposes a surtax on companies whose CEOs earn more than 100 times the median worker pay, and Bernie Sanders has proposed a corporate tax based on compensation ratio at the federal level.
- **Holding Medicaid recipients harmless:** A tax threshold, tax exemption or tax credit can ensure that people who are too poor to pay premiums now are not subject to paying taxes in the universal system. If the financing mix includes a sales (or gross receipts) tax, a tax credit should also be extended to low- and moderate income **seniors**. Although seniors would no longer pay Medicare premiums and out-of-pocket costs, a tax on consumption would cause an unexpected burden, especially for those seniors who have already paid payroll taxes into the current Medicare system.
- **Protecting the smallest businesses:** A payroll or gross receipts tax threshold or bottom exemption can ensure that small businesses (e.g. those with up to 10 workers, 60% of which do not currently offer coverage) and the self-employed do not face a sudden and disproportionate increase in costs.

What are wealth taxes?

Wealth taxes, also referred to as net worth taxes, are applied on a recurring basis to the value of personal financial assets, such as stocks, financial securities, and trusts, and can also include taxes on the value of physical assets, such as luxury goods and real estate. The threshold of a wealth tax is typically set very high, so that only millionaires or billionaires are affected. Wealth taxes are different from taxes on the non-wage income derived from the sale of financial assets (i.e. capital gains) and from estate and inheritance taxes. These taxes are imposed on the transfer of wealth, whereas wealth taxes apply to the possession of wealth. Nevertheless, all of these taxes are targeted at individuals with great wealth, which means they contribute directly to redistributing resources downwards and to narrowing the wealth gap.

What are consumption taxes?

Taxes levied on the consumption of goods and services include sales taxes as well as excise taxes on alcohol, tobacco and gasoline (sometimes referred to as sin taxes). In most other countries, value-added taxes (VAT) are more common than sales taxes. VAT is collected on the value added to a good or service throughout the supply chain, rather than solely at the final point of sale. The result, however, is the same: the tax is passed on to the consumer. A different but related approach is to tax the gross receipts or revenue of a business. This is technically a business rather than a consumption tax, but it is also passed on to the consumer. All of these taxes tend to be regressive, as they impose a flat tax rate and do not take account of ability to pay.

How to maximize universal health care's impact on economic equity: Five recommendations for advocates

1. Include explicit financing principles in universal health care bills, including parameters for tax design and distributional outcomes.
2. Ensure that financing proposals are intentional about redistributing income and wealth from richer to poorer households. The tax structure should be progressive for both people and businesses.
3. Ensure that corporations contribute according to their ability and pass on savings to workers.
4. Use the equity effect of publicly financed health care as an advocacy talking point and connect this with demands for reducing wealth and income inequality. An equitable financing design can enhance the political feasibility of universal health care, as the Vermont experience shows (which largely faltered due to a flat tax proposal).
5. Don't be afraid of "disruption": shifting health care out of the market is an important and necessary structural transformation. A timid financing design that mirrors current premium or tax conventions risks perpetuating the same unjust fiscal policies that have facilitated economic inequity in the first place. Many current tax rules benefit the wealthy. By shifting the resourcing of a major public good — health care — to the wealthy, we can change that injustice.

Studies referenced in Table 1:

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Table 1: Comparison of Universal Health Care Financing Proposals

	Type of tax	Notable features	Distributional effects	Equity focus?
National Medicare 4 All (PERI study)	Taxes on payroll, sales & wealth (real and financial assets); capital gains tax increase	Necessities excluded from sales tax. Tax credit for Medicaid population. Bottom exemptions for other taxes (all flat). During transition to payroll tax, employer premiums remain but are cut by 8%.	All except top 20% of households would pay less than under the existing system. All except very large businesses would pay less.	Progressive, although the focus is on even (over equitable) distribution of savings. No financing guidance in bills.
California (PERI study)	Taxes on sales & gross receipts	Necessities excluded from sales tax. Tax credit for Medicaid population. Bottom exemption from gross receipts tax.	Top 20% of households would pay slightly more, others less. Businesses would pay less, especially small businesses currently offering coverage.	Mildly progressive. Focus is on even (over equitable) distribution of savings. No financing guidance in universal health care or study commission bills.
New York (Friedman & RAND studies)	Taxes on payroll & unearned income (interest, dividends, capital gains)	Payroll tax is graduated, has no cap, employer pays 80%. Bottom tax bracket is exempted from both taxes.	All (Friedman) or most (RAND) poor, low and middle income households would pay less; the wealthy would pay significantly more.	Progressive. Type of taxes and equity goal is built into universal health care bill; actual tax schedule would set degree of progressivity.
Oregon (RAND study)	Taxes on payroll & earned income	Small businesses (90% of employers) exempted from flat payroll tax. Transitional "wage passbacks" from employers to workers.	All households under 400% FPL would pay significantly less. Higher incomes would pay more.	Progressive. Universal health care and task force bills include progressivity principle.
Vermont (Governor's 2014 proposal)	Payroll taxes and premiums	Premium has sliding scale "on-ramp" but is flat for middle incomes and capped at the top. Payroll taxes are flat.	90% of households would benefit from net income increases. Small businesses would pay significantly more.	Progressive and regressive elements. No equity focus, despite equity principle in universal health care law.
Vermont (HCHR proposal)	Taxes on payroll, earned & unearned income	Payroll tax is on wage disparity rather than wages. Tax rates depend on wage ratio and business size. Income taxes are not capped and have bottom exemptions.	Low and middle income families would pay less, and the wealthy would pay more, also compared to the Governor's proposal. Small businesses would pay much less than large employers.	Highly progressive. Focus is on reducing income inequity directly and indirectly, including equity between businesses.
Washington (Friedman study)	Taxes on payroll, earned, unearned & corporate income; plus premium	Bottom exemption from taxes (all of which are flat). Premium is sliding scale at bottom end.	Targeted at middle class, no changes for poorer or wealthier households, although top 1% would pay more. Benefits businesses with expensive existing coverage.	Mildly progressive. Universal health care bill suggests employer assessments and individual premiums, though work group bill does not.