

Memorandum

To: Republican Leader John Boehner
From: Alex Brill, American Enterprise Institute
Date: November 6, 2009
RE: Healthcare Reform and Costs on Small Business

This memorandum provides a short comparison of the disparate expected impact on small businesses of H.R. 3962, the House Democrats' healthcare reform bill, and the amendment in the nature of a substitute that you have proposed. As described below, the Democratic bill will increase costs on small business. The Republican substitute will achieve a moderate decline in costs for small business owners and their employees through a decrease in insurance premiums.

As the Congressional Budget Office (CBO) noted in its analysis of your bill, "The average reductions [in private health insurance premiums] would be larger in the markets for small group and individually purchased policies, which are the focus of many of the legislation's provisions."ⁱ Specifically, the Republican substitute contains the following provisions that will reduce costs, particularly for small group insurance:

1. Allow the creation of association health plans (AHP) and allow states to establish interstate compacts with a unified regulatory structure;
2. Expand health savings accounts (HSAs);
3. Federal funding for small group market reinsurance programs operated by states;
4. Medical malpractice reform.

Health insurance costs have been identified as the most severe problem for small businessⁱⁱ and the higher insurance costs these firms face makes competing with larger firms more challenging. By removing regulatory barriers, expanding the qualified uses of tax-free HSA accounts, reducing the cost for insurers by facilitating reinsurance markets and reducing the threat from trial lawyers, the Republican substitute will reduce the cost of providing health insurance for small businesses. The result will be more workers will receive health insurance and the cost for that insurance will be less.

As CBO noted, "In the small group market...the amendment would lower average insurance premiums in 2016 by an estimated 7 percent to 10 percent compared with amounts under current law."

In contrast, the Democrats' legislation contains a number of provisions that will lead to higher costs for small businesses and individuals as a result of higher health insurance premiums and tax increases. Among the provisions that will adversely affect small businesses and their workers:

1. \$480 billion in additional taxes (2010-2019) as a result of a 5.4% surtax on incomes above \$500,000 (\$1 million for married filing jointly)ⁱⁱⁱ. This large tax hike would significantly discourage entrepreneurship among affected taxpayers.^{iv}
2. Excise taxes on medical devices, increased drug rebate and expansion of the drug rebate to "dual-eligibles" all of which will lead to higher healthcare prices and higher insurance premiums.^v
3. A mandate on employers, including most small employers, to provide insurance or pay a penalty tax to the government. \$135 billion in employer penalty payments will be collected 2010-2019.^{vi}

Discouraging small business activity and entrepreneurship is never a good idea. With 15.7 million unemployed workers, the right policy objectives are those that lower private health insurance premiums so

to allow more Americans to be able to afford coverage. The Republican substitute amendment, with policies that promote better risk pooling and reduce costs, achieves that goal.

ⁱ Elmendorf, Douglas. Letter to Honorable John A. Boehner from CBO Director Douglas Elmendorf, November 4, 2009.

ⁱⁱ Philips, B. and H. Wade. "Small Business Problems & Priorities." NFIB Research Foundation, June 2008.

ⁱⁱⁱ Joint Tax Committee, JCX-46-09, November 4, 2009.

^{iv} Bruce, D. and T. Gurley. "Taxes and Entrepreneurial Activity: An Empirical Investigation Using Longitudinal Tax Return Data." Small Business Administration. March 2005. See also Gentry, W. and R. G. Hubbard, "Tax Policy and Entry into Entrepreneurship" Williams College Working Paper, June 2004.

^v Brill, A. "Taxing the Sick: How 'Fees' in Healthcare Reform Hurt Patients." *AEI Tax Policy Outlook*, October 2009.

^{vi} JCT, JCX-46-09.