At the 2008 Annual Meeting, the House of Delegates adopted as amended the recommendations contained in Council on Medical Service Report 8, “Standardizing AMA Policy on the Tax Treatment of Health Insurance.” Recommendation 16 amended the report and called for the American Medical Association (AMA) to study the effect of changing the tax system from the deductibility of health care “expenses” to the deductibility of “insurance premiums” on self-insured employers and report back to the House of Delegates at the 2008 Interim Meeting. Recommendation 16 raised concerns with other recommendations of Council on Medical Service Report 8-A-08, which were adopted by the House, that amended several AMA policies by replacing the term “health expense coverage” with “health insurance.”

The Board of Trustees referred the requested study to the Council on Medical Service for a report back to the House at the 2008 Interim Meeting. This report, which is provided for the information of the House, clarifies the intent and expected impact of substituting the language “health expense coverage” with “health insurance” in AMA policy as adopted by the House of Delegates in June. It also clarifies any misunderstanding regarding whether Council on Medical Service Report 8-A-08 created new policy regarding the tax treatment of health insurance.

BACKGROUND

The tax treatment of health insurance as it currently exists, and as it would exist under the AMA proposal to expand health insurance coverage and choice, have recently been described in the following AMA publications and reports:

- Council on Medical Service Report 8-I-08, “The Tax Treatment of HSAs,” also currently before the House; and
- A series of AMA advocacy publications, which were distributed to the House at the 2008 Annual Meeting and are available at www.VoiceForTheUninsured.org.

For the past decade, the AMA has advocated expanding health insurance coverage and choice by replacing the existing employee income tax exclusion for employer-sponsored coverage with individual tax credits for health insurance that are refundable, inversely related to income, and applicable to coverage of the recipient’s choice, whether job-related or not. Specifically, Council on Medical Service Report 9-A-98, established 17 principles fostering individually owned health insurance. Following is the ninth of these 17 principles:
That AMA policy express a preference for replacement of the present exclusion from employees’ taxable income of employer-provided health expense coverage with a tax credit for individuals equal to a percentage of the total amount spent for health expense coverage by the individual and/or his/her employer, up to a specified actuarial value or “cap” in coverage so as to discourage over-insurance. (Recommendation 9 of Council on Medical Service Report 9-A-98).

Over the past decade, the policy established by this recommendation has been modified. Most recently, the reference to “health expense coverage” was updated and clarified by Council Report 8-A-08. However, support for replacing the employee income tax exclusion with tax credits has remained a core principle (Policy H-165.920[11], AMA Policy Database). The AMA reform proposal would redirect the estimated $125 billion annual government subsidy for private coverage toward those most likely to be uninsured i.e. those with lower incomes, while also expanding individual choice by leveling the playing field between employer-sponsored insurance and individually purchased insurance.

For purposes of both the current and proposed tax treatment of health insurance, it does not matter whether coverage takes the form of a fully insured or a self-insured health plan. Most employers with 100 or more employees, and some smaller firms, “self-insure” as provided for under the Employee Retirement Income Security Act of 1974 (ERISA). Rather than paying premiums to an insurer to assume responsibility for employees’ covered health care expenses, employers with ERISA plans bear the financial risk of covering their employees themselves, relying on insurers simply as third-party administrators to assist with claims management and similar activities. Employers who offer a choice of health plans may offer both fully insured and ERISA plans. All employer-sponsored health plans are subject to basic federal standards regarding fiduciary responsibility, patient information access, due process and appeals, and accessibility of coverage, but self-insured ERISA plans are exempt from many state regulations. The majority of people with employer-sponsored health insurance are enrolled in ERISA plans. Regardless of whether a health care plan is fully insured or self-insured by the employer, employer expenditures on employees’ health care coverage are currently excluded from the insured employee’s federal income tax. Employer expenditures on employees’ health care coverage are also currently deductible by the employer as a business expense, and would continue to be so under the reformed tax treatment of health insurance proposed by the AMA.

Under the AMA reform proposal, for purposes of taxes, there would be no distinction between fully insured and self-insured health plans, and employer-paid defined contributions toward employee-purchased coverage (Policy H-169.920[3a]). In all cases, the employer’s costs for employee coverage would become subject to the employee’s federal income tax, the individual could apply any tax credit toward the coverage, and, as noted, the employer could continue to deduct such outlays as a business expense. Finally, as noted in Council on Medical Service Report 8-I-08, “The Tax Treatment of Health Savings Accounts,” also before the House at this meeting, current AMA policy regards both components of a health savings account (HSA), the traditional health plan and the individual savings account, as “health insurance” for tax purposes. AMA principles for structuring tax credits (Policy H-165.865[11i]) make it clear that HSA coverage should qualify for the same tax treatment as other forms of health insurance coverage. Specifically, tax credits could be used to pay premiums for an HSA-qualified high-deductible health plan or to make contributions to an associated HSA account.
DISCUSSION

The Council appreciates the opportunity to further articulate the intent and implications of modifications to AMA policy discussed in Council on Medical Service Report 8-A-08. Recommendation 16 of the report called for the study of the effect of changing the tax system from the deductibility of health care “expenses” to the deductibility of “insurance premiums,” with special attention to the impact on self-insured employers. The Council notes that the recommendations of Council Report 8-A-08, which were adopted by the House of Delegates, do not call for a change in the types of health-related expenses that are tax deductible, nor do they call for the addition of the term “premiums,” as suggested by Recommendation 16. Rather, the linguistic modifications improve the clarity of long-standing AMA policy, and do not represent a shift in policy. As Council Report 8-A-08 states, the term “health insurance” is preferable to “health expense coverage” because it is widely used and understood, with substantially the same meaning.

Specifically, the Council believes that the effect of these modifications was to clarify long-standing AMA policy supporting replacement of the employee income tax exclusion of employer-provided health benefits with appropriately structured tax credits applicable to coverage of the recipient’s choice. These proposed changes in the tax treatment of health insurance are central to achieving the AMA reform objectives of redirecting the estimated $125 billion annual government subsidy for private coverage toward those most likely to be uninsured, i.e., those with lower incomes, while also expanding individual choice by leveling the playing field between employer-sponsored insurance and individually purchased insurance.

References for this report are available from the AMA Division of Socioeconomic Policy Development.