IRET Congressional Advisory

INSTITUTE FOR RESEARCH ON THE ECONOMICS OF TAXATION

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SCHIP RETURNS FOR ANOTHER VOTE

The State Children's Health Insurance Program (SCHIP) is coming up for another vote. Two efforts in 2007 to reauthorize and significantly expand the program were successfully vetoed by President Bush. (H.R. 976 was vetoed October 3, and a slightly scaled back version, H.R. 3963, was vetoed December 12.) Following the second veto, SCHIP was given a simple extension at full funding of existing coverage levels through early March of 2009 (in H.R. 3584, passed and signed into law on December 21, 2007). Now, the Congressional leadership is gearing up for another attempt to pass something like H.R. 3963.

SCHIP was originally designed to provide insurance for children in families with incomes up to twice the poverty level. The targeted families had income too high to qualify for Medicaid, but not high enough to make insurance readily affordable.

Many states requested and were granted waivers to expand coverage to children in families with incomes up to 300 percent or 350 percent of poverty. Some states included large numbers of adults in their programs. These states have covered additional populations even though they have not fully enrolled the children in the original target group of poorer families. A number of states overspent their allotments due to their more generous eligibility rules, and have received matching funds from Congress to help cover the over-runs.

The President had proposed a 20% increase in SCHIP, from $20 billion to $25 billion, over five years. The Bush request was enough to fully fund a renewal of the SCHIP program at a level that would fully cover health cost inflation and the rising number of children in the originally qualifying income categories (families with income up to 200% of poverty).

By contrast, the second of the vetoed Congressional plans would have more than doubled the size of the program, expanding it by $35 billion over five years (from $25 billion to $60 billion). It would have paid for a broad inclusion of an additional 4 million children of middle-income families (up to 300% of poverty, or nearly $62,000 for a family of four). To address some of the President's concerns, it would have prohibited use of SCHIP money for families with income above 300 percent of poverty; removed childless adults, other than pregnant women, from the program; and would have required a Government Accountability Office study and subsequent efforts by the states to "determine best practices" to prevent the substitution of SCHIP for private coverage. ("Study" to "determine best practices" does not equal "adopt and successfully implement".)

The Congressional Budget Office (CBO) estimated that of every additional 100 children enrolled in SCHIP under the Congressional expansion proposal, between 25 and 50 of them would be switching from private insurance. Some would be switched out of their parents' employer-provided plans, and some from their parent's individual insurance plans. This "crowding out" of private coverage would shift the cost of the insurance from private wallets to the public purse.

To hold the five-year estimate to a $35 billion increase, Congress implausibly assumed that the additional spending on the program would drop by about 75% in 2012, forcing all the new entrants and most of those covered by the original program off the rolls.

The main funding mechanism in H.R. 3963 was a nasty, regressive tobacco tax hike that would hurt low-income families, including families currently receiving SCHIP assistance. It would raise the federal cigarette tax by $0.61 per pack hike (from $0.39 to $1, or a 156% increase), and impose similar or higher tax hikes on other tobacco products. (The tax on cigars would rise by 6,000%, from just under 5 cents to $3 per cigar!) Low-income individuals are far more likely to be smokers than middle- and high-income individuals, and for those who do smoke, people with lower incomes spend a higher percentage of their incomes on cigarettes and the associated tax than do people with higher incomes.

Who would lose and who would win from the SCHIP expansion and the tobacco taxes? Low income families already covered by SCHIP would either gain nothing or lose. They would have the same real health benefits as now, but would face a stiff hike in their tobacco taxes (if they are smokers) to pay for covering the new higher income enrollees. The tax would offset about a third of what the poorest families now receive from having a child in the program. Middle-income families who do not smoke would get the full benefit of the expansion. People who smoke but have no children and have nothing to do with SCHIP would lose the most.

Insofar as SCHIP is a welfare program, it should be funded by broad-based taxes at least loosely related to ability to pay. Instead, the tobacco tax provisions are a discriminatory hit against people with no rational connection to the problem being funded. Insofar as SCHIP is a social mandate, it should not involve subsidizing middle-income families who can afford to pay their own way. If parents need to trim other spending to pay for the insurance, what they cut back on should be left up to them. Singling out smoking, as opposed to any other greater-than-subsistence-level consumption, is "Big Brother knows best" at its worst.

The bill is still too focused on extending an expensive federal subsidy to families that can pay for insurance and who mostly have insurance already. At a time of increasing federal deficits, it is doubtful that the additional $35 billion in outlays can be justified. The expansion of SCHIP would drag millions of participants into state-directed programs for no good reason. Rather than put millions more children into a government-run insurance program, we should reform the tax treatment of health insurance to encourage and enable more families to get private coverage that is not dependent on one’s place of employment. The funding mechanism in this bill is not sensible tax policy. The bill deserves yet another veto.

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