

## Analyzing Health Care Reform's Impact on Working Households: A New Methodology

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In 2005, the Vermont Children's Forum and the Public Assets Institute released "Earning More, Losing Ground."<sup>1</sup> This report shows how Vermont's minimum wage failed to keep pace with cost increases for working Vermonters' basic needs during the five-year period 1999 to 2003. The analysis also revealed that because of the way income taxes and public benefits are structured, low-income working families – those earning less than the amount needed for basic needs -- are penalized for earning more money.

According to the report, "The single biggest cost increase was health insurance, which doubled over the five-year period, accounting for about 25% of 2003 basic household expenses."<sup>2</sup> As Vermont policymakers search for solutions to stem the rapidly increasing health insurance costs and ensure that all Vermonters have access to health care, it is important to be able to analyze the impact of potential health care reform options on Vermont households' economic momentum.

**Economic momentum** refers to a household's ability to get ahead financially. A household that earns more money and has more money to pay its bills has economic momentum. Policies now in place penalize low income Vermonters who earn more money, frustrating their economic momentum.

This report unveils a new methodology to evaluate the impact of any new health insurance plan on the economic momentum of low-income working households. It then uses this new analytical tool to evaluate Catamount Health, the health insurance plan included in Vermont's Health Care

Affordability Act of 2006, on households that are eligible for this plan.

### *Methodology*

This analysis tracks a household's gross wages from the minimum wage level up to the amount needed to pay for basic needs. At each increment of gross wages, above the minimum wage, the analysis calculates the effective income after paying for health care and the gap between effective income and the amount needed for that household's remaining basic needs.

A household's **effective income** is the combination of after-tax wages plus public benefits that allow the household to provide for its basic needs. It is called "effective" income because the household might never see all of the income as cash, but instead have access to a benefit, such as heating fuel, that satisfies a basic need. A benefit that eliminates a cost can be thought of as increasing the effective income for the household.

Similarly, an essential cost such as health care can be thought of as reducing the household's effective income. In order to compare the impact of various health insurance plans on the ability of a household to get ahead economically, this analysis looks at what the household will have remaining to pay for its other needs, assuming it first pays for health care. For any given health insurance plan, the analysis assumes the household will pay the necessary premiums and out-of-pocket costs for an assumed level of health care services. The amount a household pays for health care varies based on the household income because of various

public programs, including public insurance and premium subsidies. Therefore, public programs that cover more of these costs effectively increase the household income available to meet other needs.

The methodology for this analysis has three basic components:

1. **Basic Needs Budget After Paying for Health Care.** This is calculated by subtracting all health care costs (premiums and out-of-pocket costs) from the Basic Needs Budget. Basic Needs Budgets, prepared in many states, document the cost of meeting basic needs for various household configurations (e.g., one-adult, one-child household; one-adult, two-children household; etc.).
2. **Effective Income After Paying for Health Care.** Although the cost of basic needs after paying for health care is the same for a given household configuration regardless of wages, the ability of the household to meet those needs depends on wages, taxes and public assistance. To calculate the effective income available to meet the household's remaining needs at each gross wage increment, the analysis starts with the annual gross wage amount, then:
  - a. Subtracts state and federal income taxes,
  - b. Adds any other public assistance the household may be eligible for to help meet its remaining basic needs, then
  - c. Subtracts the amount paid by the household for:
    - i. health insurance premiums, and
    - ii. all out-of-pocket costs for the household's assumed level of health care services, which is based on actual services used (median by age group) as reported by MEPS<sup>3</sup>. This number is adjusted for the actual coverage provided by the insurance policy being analyzed to calculate the out-of-pocket costs of the household.
3. **Risk.** An important variable in evaluating any health insurance plan is the extent of the household's financial risk should they experience higher than median health care costs in the case of severe illness or accident. To estimate these costs, this analysis uses the same MEPS data but chooses the 90th percentile, by age group. Any costs not covered by the insurance or managed care plan must be paid by the household. As this extra cost would reduce the household's ability to meet its remaining basic needs, it is subtracted from the Effective Income After Paying for Health Care and is shown in the chart as a separate "risk" category.

### Charts

The following analysis shows two charts that use this methodology for a household with one adult and one dependent child: Chart A is the existing situation in Vermont for 2004 (the most recent available data) and Chart B assumes that the household had access to Catamount Health in 2004. The charts illustrate the impact of Catamount Health on both the economic momentum for the household and the annual gross wages needed to pay for basic needs. The x-axis (bottom) shows the household's annual gross wages and the y-axis (left) is the effective income levels. Starting with the minimum wage<sup>4</sup> level on the left, as gross wages increase, the chart tracks the household's effective income after paying for health care that is available to pay for the remaining basic needs.

The three basic components described above are shown in the charts as follows:

1. **Basic Needs Budget After Paying for Health Care** is shown with the straight horizontal blue line at the top of the chart.
2. **Effective Income After Paying for Health Care** is shown as the light blue area at the bottom of the chart.

3. **Risk** is shown as the white area (above the light blue area). This area reflects the range of possible extra health care costs for this household due to extraordinary illness or accident.

The **gap** between the amount needed for basic needs and the household's effective income is shown as the dark blue area in the chart. The gap is increased by the shaded red area for those households that face health care costs related to severe illness or accident.

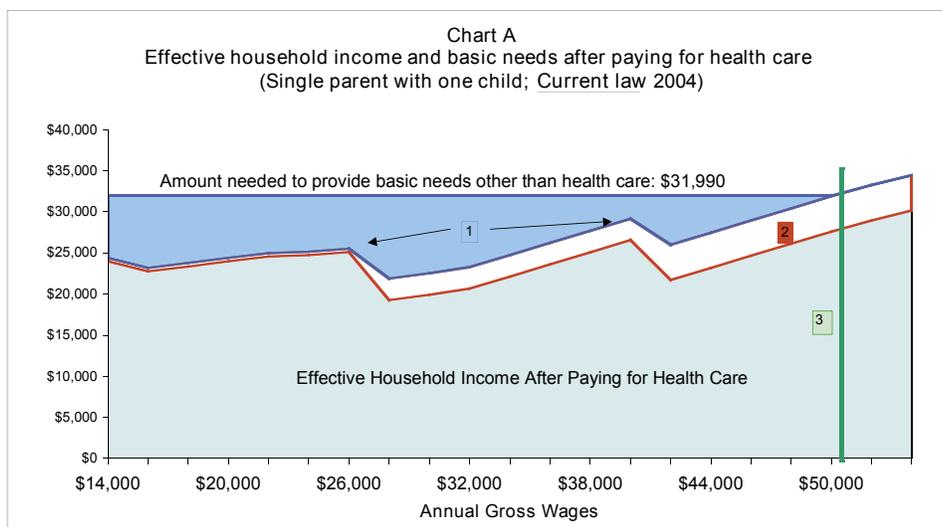
Chart A shows serious bumps in the road for low-wage earners trying to meet basic needs. This household would need annual gross wages of about \$50,000 to meet basic needs if family members are healthy. If they have serious health problems, they would need to gross \$57,000 to pay their bills.

**1A** The blue line shows the effective income (including public assistance) available to a household after paying for typical health care expenses and taxes. The line is lower on the left, where the household's gross wages are \$14,040 (minimum wage) and higher on the right where the household's gross wages are \$54,000. The dark blue area above the line shows the gap between the income available and what is needed to meet the household's remaining basic needs.

There are three "cliffs" where the household loses effective income by earning more money. The first cliff at \$14,040 gross wages is slight but real and is the result of loss of Foodstamps. The other two, related to health care, are much more dramatic. The first results from the adult no longer qualifying for VHAP between \$24,000 and \$26,000 annual gross wages and the second from the child no longer qualifying for Dr. Dynasaur between \$38,000 and \$40,000 annual gross.

**2A** The red line traces the effective household income for a household with high health care expenses resulting from severe illness or accident. This household would have less effective income because of higher out of pocket costs, depending on the type of health insurance coverage they have. With high health care expenses, the two large cliffs become steeper requiring much higher gross wages to meet basic needs. The white area between the red and blue lines is the "risk" zone, showing the amount that a household needs to put aside for deductibles and co-payments in the event of illness.

**3A** The vertical green line shows the point where the effective household income after paying for health care is enough to cover all other basic needs (\$50,130 gross wages). If the household has high out-of-pocket health care expenses due to severe illness or accident, an additional \$6890 in gross wages would be needed to meet basic needs (where the red line reaches the basic needs line).



Using the same analysis, let's look at Chart B to see what happens to this household had Catamount Health been in place in 2004. The chart shows that this household would have fewer obstacles to earning enough to pay for basic needs and less financial risk should illness or accident strike. Gross wages of about \$48,000 would have been sufficient to pay for all household expenses (\$50,000 if the household faced severe illness or accident).

**1B** For this household, shifting to Catamount Health substantially reduces the gap (dark blue area) between basic needs and effective household income. Also, because the Catamount Health premium subsidy picks up where VHAP<sup>5</sup> leaves off, the big cliff at \$24,440 gross wages disappears, rewarding higher wages with higher effective income. The second cliff at \$39,000 remains, however, because the child no longer qualifies for Dr. Dynasaur and the adult no longer receives a subsidy to help pay for the Catamount premium.

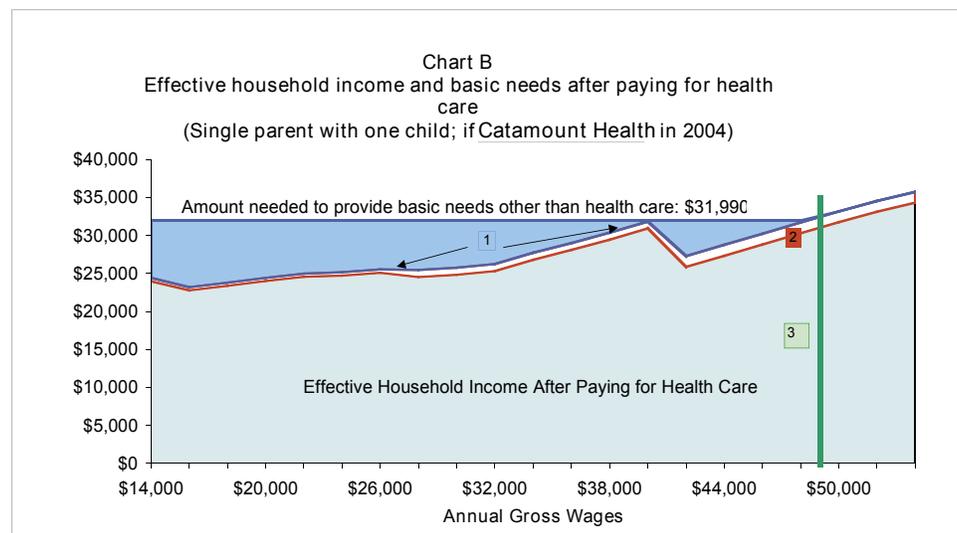
**2B** The "risk" area related to high deductibles and co-payments, is also greatly reduced for this household because Catamount Health requires lower out-of-pocket costs.

**3B** This household has nearly enough to meet basic needs at a gross income of \$39,000. However, if the household's gross wages increase above \$39,000, the child will no longer be eligible for Dr. Dynasaur and the adult will no longer be eligible for Catamount Health's premium subsidy. After losing eligibility for these programs, the household must earn gross wages of \$48,375 to meet basic needs with \$1925 more needed if the household faces severe illness or accident.

### Catamount Health Analysis

Catamount Health would have had the following effects in 2004 on the economic momentum of a qualifying household with one working adult and one child:

- Elimination of the significant cliff at \$24-26,000 gross wages, so that from \$16,000 to \$39,000 gross wages, this household would have more money for basic needs with each additional dollar earned.
- Ability to pay for basic needs with less in gross wages than under current law -- \$48,375 with Catamount compared to \$50,130 under current law.
- Less financial risk than current law because of reduced deductibles and co-payments. This household would need additional gross wages of \$1925 to meet basic needs if severe illness or accident strikes compared with \$6,890 under current law.



### *Catamount Health Recommendations*

1. Catamount Health would better assist this working household by extending the sliding-scale premium subsidy above the 300% of poverty cap that the plan currently includes. This would create a smooth economic path to earning enough to pay for basic needs.
2. Eligibility rules should be changed to allow more Vermonters to qualify for Catamount Health. Because eligibility is restricted to those who were on VHAP or were uninsured for at least one year, the benefits of Catamount Health are not available to most Vermonters.

### Methodology and Assumptions:

1. The household characteristics, the determination of basic needs, and the calculation of the cost of meeting those needs are consistent with the 2004 Basic Needs Budget produced by the Joint Fiscal Office in January, 2005 with the following exceptions:

- o This study assumes the household does not have employer-assisted health insurance and receives VHAP and Dr. Dynasaur (Vermont's health insurance for children under 18) if eligible, and a Blue Cross Blue Shield program if not eligible for a public program. The BCBS program has a premium of \$348 per person, a co-pay of \$20, a deductible of \$3000, and an out-of-pocket maximum of \$6000.

- o This study documents the out-of-pocket costs for a household with typical medical expenses and for a household with high medical expenses. For the typical household, the median total medical expenditure for the age group of each household member was derived from the 2003 Medical Expenditure Panel Survey of the Agency for Health care Research and Quality. Each type of expenditure was then compared to the applicable health insurance policy to calculate what percentage of it, if any, the household would pay for. For the household with high medical costs, the calculation began with total expenditures at the 90th percentile for the age group. The out-of-pocket costs are not "maximum" as they are below the maximum out-of-pocket for the BCBS policy, but the 90th percentile was chosen to show a reasonable risk a household faces should an accident or serious illness occur.

- o In the JFO study, the amount the household is expected to put into "savings" is calculated as a percent of income. In this study, the savings amount is frozen in order to isolate the effects of health care costs and benefits.

- o The JFO study calculates two basic needs budgets for each family configuration: one for an urban household and one for a rural household. This study uses a weighted average (18% urban, 82% rural) to reflect the urban/rural split in the state.

2. Effective Income after paying for health care is calculated as: gross wages minus taxes plus public assistance minus health care costs.
3. This report looks at the effect of the Catamount Health insurance program—not the effect of all the provisions of the 2006 Act.
4. The premiums for VHAP and Dr. Dynasaur are those in the Act even though they would not have been in effect in 2004.
5. The subsidized Catamount premiums for households with incomes less than 300% of poverty are those in the Act, even though they would not have been in effect in 2004. The premium for Catamount for households with incomes greater than 300% of poverty is estimated to be \$300 per person. As the cost of Catamount is unknown at this point, this is a rough estimate based on some information provided to the Legislature: BCBS quoted \$423 per person in 2006. This amount is reduced by roughly 30% to account for a reimbursement difference.
6. Hospital free care policies are not considered. It is assumed the household will be billed for the full amount.
7. Public Assistance as used in the analysis includes Reach up, Foodstamps, Child Care Subsidy, Low Income Home Energy Assistance Program (LIHEAP), Telephone Lifeline, Federal EITC, VT EITC, Renter's rebate, and State and Federal Child Credits and Dependent Care Credits.
8. Information needed to compare a health care plan other than Catamount Health or to look at a different household configuration:
  - Premium and/or health care tax paid by the household
  - Deductible
  - Co-pay
  - Co-insurance
  - Out-of-pocket maximum
  - Eligibility requirements and/or income limits

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#### End Notes

<sup>1</sup> *Earning More, Losing Ground -- A trend analysis of Vermont's minimum wage, public assistance, and the cost of basic needs* (1999-2003); Vermont Children's Forum with the Public Assets Institute; February 1, 2005; Report is available for download at [www.publicassets.org](http://www.publicassets.org).

<sup>2</sup> *Ibid.*, p.14

<sup>3</sup> Medical Expenditure Panel Survey of the Agency for Healthcare Research and Quality, U.S. Dept. of Health and Human Services, [www.meps.ahrq.gov](http://www.meps.ahrq.gov)

<sup>4</sup> Vermont's minimum wage in 2004 was \$6.75/hour or \$14,040/year.

<sup>5</sup> Vermont Health Access Plan

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