



PERSPECTIVES FOR THE NEW ADMINISTRATION

Health Care:  
Don't Forget Saving  
Families \$2,500

*By Hanns Kuttner*

Hudson Institute



# Health Care: Don't Forget Saving Families \$2,500

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*President-elect Obama offered a concrete proposal to save the typical family \$2,500 on medical expenditures. Measuring progress towards that goal requires statistics the federal government does not currently calculate. In addition to providing new measures, the federal government should help those who have health insurance through employers understand just how much that coverage costs.*



**D**uring the Presidential campaign, Senator Obama promised he would save the typical American family up to \$2,500 a year on medical expenditures. How will the Obama administration measure and communicate its progress toward that goal?

None of our current statistics reports how much a typical American family currently spends on health care. Tasking the Bureau of Labor Statistics with producing a regular, more comprehensive report on health care expenditures would address this problem. Secondly, most Americans do not have a way to understand the true costs of their own health care. Legislation to add more information to the W-2

form would help inform the public about what their employers are spending on their health care premiums.

## Improving the government's statistical methodology

**D**espite improvements in our ability to measure such concepts as unemployment, poverty, and the gross domestic product, our current techniques for measuring medical expenditures remain inadequate to the task required of them. None of the data series regularly released by the federal government will allow an assessment of how well the Obama administration is doing to fulfill the commitment to reduce the typical family's health care expenditures.

Three areas in particular require a closer look and better statistical methodology. The first is the definition of "expenditures." Out-of-pocket costs are only part of what we spend on health care. This leaves out of the equation an important number, third-party expenditures such as the portion of insurance premiums paid by employers.

The second area that must be clarified in order to measure potential savings by families is the definition of the "typical family." The statistics from government sources homogenize very different family circumstances into a single average.

Third, we must be sure that we are comparing apples to apples. In looking at health care premiums paid by families and employers, we must be aware of variations in coverage. Lower premiums can reflect more efficiency or less coverage.

## Problems with the existing survey methods

**T**he most recent figures from the Bureau of Labor Statistics (BLS) in the Consumer Expenditure Survey show that in 2006 the average family's health care expenditures were \$2,766. Of that amount, \$1,465 was for health insurance, \$670 for medical services, \$514 for drugs, and \$117 for medical supplies. Total expenditures across all families using this measure were \$326.7 billion.

The BLS figures, however, get medical spending wrong by counting only out-of-pocket expenditures and ignoring money spent by employers on health care insurance premiums. The usefulness of these figures is also limited by the way the average is reported, for it includes single people living alone and families with children, young people and the elderly, those who obtain public coverage that requires no annual premium and those who buy coverage directly from insurers,

## PERSPECTIVES FOR THE NEW ADMINISTRATION

those who were uninsured and those who had HMOs with minimal cost-sharing.

A more useful study of typical family medical expenditures would require more detailed information about spending, both by families and on their behalf. It would also offer perspectives on families in different circumstances, including family size, insurance coverage, and age, to allow views of many “typical” families.

A better statistical approach comes from the National Health Accounts (NHA). This series, produced by a team at the Department of Health and Human Services (HHS), provides a consistent way of measuring the resources that go to health care services across the economy, public and private, out of pocket and through third parties. The NHA total for health expenditures in the United States for 2006 was \$2.1 trillion.

The problem with the NHA number, however, is that it is in the wrong units. President-elect Obama’s call was for savings of up to \$2,500 per family. We need dollars per family, not total dollars. Getting into the right units is more complex than looking up the number of families and dividing total spending by the number of families. This is because “total expenditures” include spending on behalf of a large number of Americans who do not have insurance through an employer, such as those enrolled in Medicare and Medicaid.

Among those with coverage through an employer, moreover, the employer contribution to the cost of their health insurance premium likely accounts for a majority of their expenditures. Any measure of spending by the typical family that omits this source is unhelpful in tracking progress toward lowering costs.

Premiums are only part of the story. The growth rate in premiums has been slowing in recent years. Part of this could be because health costs have grown at a slower rate. It also reflects changes in what health insurance covers. One way to reduce premiums is to cover less. Higher co-payments and deductibles lower premiums but also shift expenditures from premiums to out-of-pocket payments. Any benefit consultant could show an employer how to reduce premiums by \$2,500 by increasing co-payments and deductibles, but that is not what President-elect Obama had in mind.

The best government survey at present, the Medical Expenditure Panel Survey (MEPS) produced by HHS only gets part of the story. When looking at families, the MEPS simply counts expenses, whether paid out of pocket or by a third party. For 2005, among families whose members are under age 65 and had private insurance, 88 percent had some expense, and among those who did, mean expenses were \$3,290 per person. Without knowing how much those families paid for premiums, either directly or through an employer, we won’t be able to track the progress of policies designed to lower costs for consumers. Something very different, however, is clearly needed to measure progress towards the Obama goal.

## Recommendations for improved reporting

**T**he Obama administration should institute a new, regular report on trends in health costs at the family level. This report will tell us something that current releases do not: how much typical families spend on health costs, including premiums paid for health insurance—directly by consumers and indirectly by employers—and amounts spent out of pocket. This report, which could rely on data collected through the MEPS, should utilize both descriptive and analytical approaches. On the descriptive side, how much did total expenditures rise for a variety of family and coverage types? How much was paid out of pocket and how much was paid by third parties? On the analytical side, how much of the change consisted of changes in prices? How much can be explained by changes in the use of existing services? How much is due to the introduction of new and relatively new treatments, technologies, and services?

A new statistical series on trends in health costs at the family level would be the primary tool for assessing progress towards President-elect Obama's goal of saving the typical family \$2,500 per year in health care costs. Several bureaus in the executive branch would be capable of providing this research. One is the Department of Labor's Bureau of Labor Statistics (BLS), the federal agency responsible for such statistical series as the consumer price index. Another is the Department of Commerce's Bureau of Economic Analysis (BEA). Much of the necessary survey data resides at HHS.

HHS, however, lacks expertise in assembling price indices, a very technical area. This project should go where the experts are. It is easier to bring data to the experts than experts to the data. Either BLS or BEA are probably better equipped to analyze the data than any office within HHS. BLS, in particular, has the deepest bench in devising price indices that disentangle changes in prices and changes in quality.

## Helping consumers understand the true costs

**A**s long as Americans think of their health care expenditures as the amount they spend out of pocket, the Obama commitment to save the typical family up to \$2,500 is doomed. If a family were to rely on the \$2,766 figure reported by the BLS for 2006, they may well think that if the Obama plan works out, there won't be much left for them to pay.

Fewer than one-tenth of Americans with private health insurance write checks directly to insurance companies, as opposed to having the premiums paid by their

## PERSPECTIVES FOR THE NEW ADMINISTRATION

employers and/or deducted from paychecks. Yet these are the only individuals who truly appreciate how much they spend on health care. The rest of us are hard pressed to know more than what we pay as co-payments and deductibles.

For the public to better understand the true costs of health care, those of us with coverage through an employer need to know how much our coverage costs. Some employers already make an effort to convey to employees their total compensation package, including the employer contribution to the health insurance premium. However, such reporting is voluntary and not widespread.

The current W-2 form that employers provide to employees does not convey enough information. While the employer's contribution to the cost of health benefits is a form of compensation, the amount is not subject to taxation. Thus "wages, tips, other compensation" as reported on the W-2 does not include health insurance premiums.

The W-2 form needs an additional box to report how much the employer has contributed towards the employee's health insurance premium: "Health insurance—not taxed." This box should include the amount of an employer's contribution to an employee's health insurance plan. Seeing this amount will give consumers a new appreciation of how much health insurance costs. The Obama administration should support legislation to add this box to the W-2 form.

This new box on the W-2 form would not have tax implications. However, there could be enormous complexities for employers in calculating the "Health insurance—not taxed" box. Even before the law changes to require the reporting of how much the employer contributes to health insurance, the IRS could begin to develop simple guidelines for calculating the amount to report. One place to begin would be a one-step calculation: total health benefits costs divided by total covered employees. More complex calculations, taking into account variation in cost between individual and family coverage, plan cost variation where employers offer more than one plan, and variation across location, could be done, but the purpose of the new box on the W-2 is to educate employees about the cost of their health benefits, not to employ accountants and benefits consultants. The IRS guidelines should therefore err on the side of simplicity.

Saving families up to \$2,500 in health care costs is an audacious goal. We won't know how much progress we are making towards that goal until we can answer the question, "Savings from what?" ■

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PERSPECTIVES FOR THE NEW ADMINISTRATION



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