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TESTIMONY

Federal Subsidies for Health Insurance and Policies to Reduce the Prices Paid by Commercial Insurers

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Chairman Guthrie, Ranking Member Eshoo, and Members of the Subcommittee, I appreciate the opportunity to appear before you today. In consultation with Committee staff, I have focused this statement on federal subsidies for health insurance coverage, the growth of those subsidies, and policy approaches that could reduce health insurance subsidies and the budget deficit.

How Do Federal Subsidies for Health Insurance Affect the Budget?

The federal government subsidizes health insurance for most of the U.S. population through Medicare, Medicaid, and various tax provisions. Those provisions include allowing employers and employees to exclude payments for health insurance premiums from income and payroll taxes and providing premium tax credits that reduce what people pay for coverage through the marketplaces established under the Affordable Care Act (ACA). The Congressional Budget Office projected that in fiscal year 2023, those subsidies would amount to a net $1.8 trillion, equal to 7.0 percent of the nation's gross domestic product (GDP).[1]

Federal subsidies for health insurance are projected to total $25.0 trillion over the next 10 years. That total includes $11.7 trillion for Medicare, $6.3 trillion for Medicaid and the Children's Health Insurance Program (CHIP), $5.3 trillion for employment-based coverage, and $1.1 trillion for the nongroup marketplaces established under the ACA and the Basic Health Program.[2]

Partly because of those subsidies, federal outlays are projected to grow faster than revenues over the next three decades, leading to ever-larger deficits. CBO projects that under current law, outlays for major federal health programs would increase from 5.8 percent of GDP in 2023 to 8.6 percent in 2053. At the same time, rising premiums for employment-based coverage would reduce the share of employees' compensation subject to taxes and decrease federal revenues.[3]

What Factors Contribute to the Growth of Federal Subsidies for Medicare and Employment-Based Insurance?

Federal subsidies for Medicare and employment-based insurance are projected to increase as a percentage of GDP from 2023 to 2033. The size of those subsidies depends on two factors: the average subsidy per enrollee and the number of enrollees. For Medicare, CBO projects that under current law, the average subsidy per enrollee would grow by 5 percent a year, on average, and enrollment would grow by 2 percent a year, on average. For employment-based insurance, the average federal subsidy per enrollee would grow by 7 percent a year, on average, and enrollment would grow by less than half a percent a year, on average.[4]

Subsidies per enrollee depend on the quantity and intensity of services provided, the prices paid to providers, and the share of costs subsidized by the federal government. Average subsidies grow at different rates for different sources of insurance coverage. Part of the reason is that the prices that commercial health insurers pay providers tend to rise faster than the prices paid by government programs such as Medicare and Medicaid, whose prices are generally set administratively. CBO estimated that between 2013 and 2018, the prices paid by commercial insurers with employment-based or nongroup plans grew by an average of 2.7 percent a year, whereas the prices paid by the Medicare fee-for-service (FFS) program grew by an average of 1.3 percent a year.[5]

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1. Congressional Budget Office, *Federal Subsidies for Health Insurance: 2023 to 2033* (September 2023), www.cbo.gov/publication/59273.

2. Other federal subsidies are projected to total $0.6 trillion over the 2024–2033 period. They include subsidies for people with supplemental or partial coverage that, on its own, would not provide financial protection against major medical expenses and thus would not meet CBO's definition of health insurance. They also include the value of the tax exclusion associated with Medicare wraparound coverage provided to former employees, Medicare spending on enrollees who receive only Part A or Part B benefits, and Medicaid spending on enrollees who receive partial benefits (such as beneficiaries who are also eligible for Medicare, for whom Medicaid pays only Medicare premiums or cost sharing). See Congressional Budget Office, *Federal Subsidies for Health Insurance: 2023 to 2033* (September 2023), p. 3, www.cbo.gov/publication/59273.

3. Outlays for major federal health programs consist of outlays for Medicare (net of premiums and other offsetting receipts), Medicaid, and CHIP, as well as subsidies for health insurance purchased through the marketplaces established under the ACA and related spending. See Congressional Budget Office, *The 2023 Long-Term Budget Outlook* (June 2023), www.cbo.gov/publication/59014.

4. Congressional Budget Office, *Federal Subsidies for Health Insurance: 2023 to 2033* (September 2023), p. 10, www.cbo.gov/publication/59273.

5. Congressional Budget Office, *The Prices That Commercial Health Insurers and Medicare Pay for Hospitals' and Physicians' Services* (January 2022), p. 1, www.cbo.gov/publication/57422.

What Factors Lead to the Higher Prices That Commercial Insurers Pay Providers?

Besides growing faster, the average prices that commercial insurers pay for hospitals' and physicians' services have historically been higher than the prices paid by the Medicare FFS program.[6] Those higher prices result from several factors. Primary among them are the market power of providers and the limited sensitivity of consumers and employers to the prices that insurers pay providers. Limited price sensitivity on the part of insurers also contributes to high prices, but it mainly results from price insensitivity among consumers and employers.[7]

Government policies can reduce the prices paid by commercial insurers by targeting the factors that contribute to high prices, although many of the underlying causes of those factors are not amenable to change by legislative action. In CBO's assessment, a comprehensive set of policies that promoted price transparency would lead to very small price reductions (between 0.1 percent and 1 percent), and a comprehensive set of policies that promoted competition among providers would lead to small price reductions (more than 1 percent to 3 percent). Moderate to large price reductions (3 percent to 5 percent or more) would be possible under policies that capped the level or growth of prices paid to providers.[8]

What Are the Budgetary Effects of Reducing the Higher Prices That Commercial Insurers Pay Providers?

Policies that would lower the prices that commercial insurers pay providers would reduce the federal budget deficit. And because subsidies for commercial insurance represent a significant portion of federal spending, even small reductions in commercial insurers' prices would result in sizable deficit reduction.

CBO analyzed an illustrative policy that would lower prices for hospitals' and physicians' services by 1 percent and found that it would shrink the deficit in 2032 by $4.8 billion, mainly by reducing federal subsidies for employment-based insurance. CBO expects that reductions in prices for hospitals' and physicians' services would reduce premiums for employment-based plans, which in turn would increase employees' taxable wages and federal revenues.[9]

6. Congressional Budget Office, *The Prices That Commercial Health Insurers and Medicare Pay for Hospitals' and Physicians' Services* (January 2022), pp. 5–6, www.cbo.gov/publication/57422.

7. Congressional Budget Office, *Policy Approaches to Reduce What Commercial Insurers Pay for Hospitals' and Physicians' Services* (September 2022), pp. 7–12, www.cbo.gov/publication/58222.

8. Ibid., Chapter 2.

9. Ibid., pp. 35–37.

Michael Cohen and Chapin White prepared this testimony, with contributions from Joyce Shin and with guidance from Berna Demiralp, Tamara Hayford, and Sarah Masi. In keeping with CBO's mandate to provide objective, impartial analysis, this testimony makes no recommendations. Jeffrey Kling reviewed the testimony, Christian Howlett edited it, and R. L. Rebach prepared it for publication. The testimony is available at www.cbo.gov/publication/59917.