Answers to Questions Asked by Congressman Pickle

Regarding Employee Benefits and the Tax Code

Submitted by the

Employee Benefit Research Institute

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List of Questions

1. We need to understand the relationship between private pensions, Social Security and individual effort plans such as IRAs. We need to understand what happens to one of these when a change is made in one of the others.

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11. Are the existing tax incentives for benefits such as health care, life insurance, day care, educational assistance, and cafeteria plans effective in encouraging employers to provide these benefits to a broad cross section of employees at a lower total cost than if the Government provided the benefit directly, if
How will tax laws that encourage employers to provide employee benefits affect compensation planning?

Will tax incentives for employer-provided employee benefits affect potential employees' choice of employment?
I. **We need to understand the relationship between private pensions, Social Security and individual effort plans such as IRAs. We need to understand what happens to one of these when a change is made in one of the others.**

- Social Security, employer-sponsored pensions and Individual Retirement Accounts (IRAs) are complementary, working together to assure retirement incomes. They are not perfect substitutes in terms of benefit delivery, but change in one would effect public pressures for, support for, and confidence in the others.

- Social Security provides a floor of protection on a redistributional basis, with lower earners receiving proportionally greater benefits. Many of those who rely most heavily on Social Security do not have high enough incomes to allow savings, and their work is such that they are unlikely to have employer sponsored retirement plans. Social Security is a pay as you go program. Research indicates that it has no effect, or a negative effect, on aggregate national savings.

- Employer-sponsored plans provide another form of "forced" savings that represents a tier of income above Social Security. Among employers with more than 250 employees these programs are almost universal. Among smaller employers they are not. For a significant portion of the population these advance funded programs represent their only real savings. As a result, research indicates that each dollar contributed to a pension increases aggregate national savings by at least 35 cents.

- IRAs are a vehicle for voluntary savings. They are used by 17 million persons as compared to over 50 million with pension coverage. Over 13 million IRA holders also have pension coverage.

- There are also differences in what these programs provide, or must provide, under current law. These differences affect the degree to which employer sponsored plans and IRAs "compliment" Social Security in terms of retirement income provision.

- Social Security only pays benefits as a stream of monthly benefits.

- Employer sponsored plans are of two types (1) those that only pay benefits as a stream of monthly benefits--most defined benefit plans and some defined contribution plans such as TIAA-CREF--and (2) those that make one time "lump-sum" payments at change of employment or at retirement age and thus may or may not produce retirement income--most defined contribution plans.

- IRAs allow the money to be withdrawn at any time with the payment of a small payment and after age 59 and 1/2 allow it to be removed as a lump-sum.
2. What is the relationship between private health plans and Medicare? If private health plans are taxed to help finance Medicare now, will it eventually result in greater demands on the Medicare system in the future?

- Employer sponsored health programs provide risk protection to most workers and their dependents. Research indicates that taxation of these programs might lead to a reduction in coverage. This in turn could produce significant pressure for a government program to complement present health programs for the poor (Medicaid) and the elderly (Medicare). Employers also increasingly are providing health insurance for retirees to supplement Medicare. Were these programs eliminated it could increase long-term costs of Medicare due to a reduction in wellness.

- Proposals for major tax reform, therefore, need to be carefully scrutinized. To the degree the full taxation of these programs as income rests on the assumption that they will continue to exist, research indicates that for millions of workers, they will not. Further, taxation could lead to an unintended age discrimination effect if health insurance were given an income value equal to the benefit provided, which would increase dramatically with age.

3. What are the appropriate employee benefits that should enjoy favorable tax treatment? What level of tax exempt or tax deferred benefits is acceptable in light of the Federal Government's revenue needs?

- Employee benefits should enjoy favorable tax treatment if they provide a benefit that the government would otherwise be required by public sentiment to provide; if it is provided more cost effectively by the employer than it could be by the government; if it serves a human resources objective that is to the advantage of the government and can most effectively be achieved through the employer; if it serves an economic advantage to the government that can be achieved most effectively through the employer; if it achieves a social objective such as allowing women to more readily enter the workforce and can most effectively be provided through the employer; if it allows U.S. employers to more effectively compete internationally; etc.

- Different employee benefits test vary differently against these criteria. For an analysis of such a question benefits should be clearly differentiated and can be classified into at least nine categories:

   1) legally required benefits (including employer contributions to Social Security, Medicare, unemployment insurance and workers' compensation insurance);

   2) discretionary benefits that are fully taxable (primarily, payment for time not worked);
3) discretionary benefits that provide retirement income as a stream of payments and for which taxes are deferred until benefits are received (including employer contributions to defined benefit pension plans and to defined contribution plans which require payment in the form of an annuity);

4) discretionary benefits that insure the employee against financial risks and are tax exempt (including employer contributions to health, life, and disability insurance plans);

5) discretionary benefits that provide for the deferral of salary until termination of employment, generally pay benefits as a lump sum, and for which taxes are deferred until benefits are received (including contributions to some profit sharing plans, to money purchase plans and ESOPs);

6) discretionary benefits that provide for the deferral of salary until special needs arise (loans and hardship), or until termination of employment, generally pay benefits as a lump sum, and for which taxes are deferred until benefits are received (including contributions to some profit sharing plans, thrift-savings plans, and salary reduction plans);

7) discretionary "reimbursement account" benefit programs that have been legally allowed since 1978 which allow employees to have reimbursement accounts--funded by the employer or through salary reduction--to pay expenses that fall into "statutory benefit" areas and are tax exempt (including health care reimbursement, child care reimbursement, etc.), with a further analytic break between those which allow salary reduction and those which don't;

8) discretionary benefits that help the employee meet special needs and are tax exempt (including employer contributions to child care and legal plans); and

9) discretionary benefits that have traditionally been called fringes and are intended to meet employer needs and are tax exempt (including employer provision of purchase discounts, job site cafeterias, special bonuses and awards, van pools, clubs, and parking).

*Only after the question is answered regarding which of these benefits meet the criteria set above for justification of favorable tax treatment can the revenue level issue be approached. All available evidence, for example, indicates that the retirement, life, health and disability benefits now provided far exceed the value of the government revenue loss. In other words, policy change should more readily be based on the question of whether the programs are meeting objectives the Congress supports, not on the revenue issue per-se.*
4. If certain compensation is not taxed, does Congress have to increase the tax rate on taxable compensation? Who benefits from that shifting of tax burdens?

- If certain compensation is not taxed at all like tax exempt insurance costs or on a deferred basis like retirement and savings programs, then to raise a given amount of revenue tax rates would have to be higher if behavioral change is not involved. This is the greatest problem with tax expenditure estimates, they assume no change in behavior when a change in the tax law takes place. On the other hand, if taxing otherwise non-taxed compensation--in this case exempt benefits--leads to larger government programs, then tax rates might in fact be lower than they would otherwise be were all compensation taxed.

- Were tax rates higher because of the exclusion or deferral of tax on benefits, however, a 1982 Treasury Department analysis undertaken for the Joint Economic Committee indicates that the burden would fall across the income spectrum on the same relative basis if benefits were valued as they are today. It is important to note, however, that the valuation of health insurance would likely change if taxed. The effect of this would fall most heavily on older workers at all income levels. This is because the true value of health insurance increases significantly as an individual ages, as evidenced by expenditure levels under the Medicare program.

5. How should we deal with tax-deferred compensation as opposed to tax-exempt compensation?

- All forms of benefits should be evaluated against their ability to meet policy goals. Tax expenditure numbers for all programs should be considered in context of the warnings contained in the budget, however, and tax-deferrals should be carefully considered in terms of the amount of tax savings eventually repaid to the government: over 80 percent in nominal dollar terms and over 70 percent in real dollar terms. This means that long-term tax subsidies are much smaller than the current year budget number implies for tax-deferred benefits.

- Estimates assume no other changes in the tax laws and estimates assume no change in taxpayer behavior if the law is changed--even if this is the only provision changed.

- Economists refer to this as "partial equilibrium" analysis. This means that most behavioral change is assumed away so that rough estimates are possible. As a result, these estimates suffer as guides to policy. Therefore, they must be used with great care. Analysis cannot, for example, legitimately use the numbers to indicate that elimination of favorable employee benefit tax provisions would produce $X of additional revenue for the fiscal or $X for the use of such programs as Social Security, health insurance for the unemployed, or Medicare.
6. Which income groups and what kind of employees benefit from different forms of employee benefits?

- Benefits are now provided across the income distribution. In medium and large establishments, coverage for major employee benefits such as retirement, health, life and disability is nearly universal. Employee benefits are now a mainstay of the middle-income worker's economic security, building savings as well as providing hazard protection.

- **Employer pensions**: Of all full-time employees in medium and large establishments, 82 percent are covered by a pension plan. Small firms, for numerous economic reasons, do not sponsor plans as uniformly. In 1981 the President's Commission on Pension Policy concluded that this could only be changed by mandating plans or by offering tax credits. As firms grow, however, they do add retirement programs. Among employees in all establishments who were covered by pensions in 1983, nearly 28 million (or 59.0 percent) earned less than $20,000. Pensions redistribute wealth to favor those at the lower end of the income scale who do not tend to save much out of current income. According to recent EBRI supported research, accumulated pension benefits constitute the major form of financial savings for more than half of all persons with pension coverage. More than 50 percent of the labor force reported no savings income in 1983. This group's average income was $9,651, just under half the average income of those reporting some asset income. Almost half of the group reporting little or no savings income were covered by an employer pension. Not all retirement benefits exhibit the same income distribution patterns, however. In particular, statutory provisions aimed at encouraging individual provision for retirement differ considerably. While 59 percent of pension participants earn less than $20,000, 46.5 percent of individual retirement account (IRA) holders and 34.8 percent of those participating in Section 401(k) plans fell into this income group. Section 401(k) plans in particular follow a different income distribution from both IRAs and employer-sponsored plans. More than half of Section 401(k) plan participants earn between $20,000 and $50,000, compared with under 50 percent for both IRAs and employer-sponsored plans.

- **Health insurance**: Of all full-time employees in medium and large establishments, virtually all are covered by health and by life insurance plans. Among all employees with employer-provided health coverage in 1982, 57.3 million (or 68.6 percent) earned less than $20,000, and 28.6 percent earned between $20,000 and $50,000. About 35 percent of all spending on health care that does not pass through government programs is now made through employer-sponsored plans. Fewer than 3 percent of pension and health insurance participants earn more than $50,000.
Increased savings: Pensions both increase and reallocate total savings. If pension contributions were received as cash income, total saving would decrease. The drop, moreover, would be relatively greater among lower- and moderate-income employees. While nonpension financial saving is concentrated among relatively high-income individuals, pensions are distributed broadly among income groups.

Pensions also change the distribution of saving among investment vehicles. Nonpension saving consists primarily of liquid saving deposits and investments in owner-occupied homes or other consumer durables. Pension funds, in contrast, are invested in securities that finance productive capacity and employment. Pension funds have grown to be the single largest supplier of investment funds to financial markets. At a time when unmet capital financing needs are emerging throughout the economy, the fact that pension funds provide long-term capital gives them an important role in economic policy.

Increased retirement income: The availability of a pension often means the difference between subsistence and the ability to maintain pre-retirement living standards in retirement. Recent EBRI research projects that over the next forty years real retirement incomes will more than double. The average annual retirement income for those reaching age sixty-five in the 1980s is projected to be $13,376 per household in 1983 dollars. It is expected to increase to $26,802 for those retiring between 2010 and 2019. Average employer pension benefits will increase from $5,315 for those retiring in the 1980s to $12,417 for those retiring between 2010 and 2019. The proportion of new retiree households receiving pension income will grow from 37 percent in the 1980s to 71 percent by 2019.

Tax payments by retirees will reflect this income growth. Pension beneficiaries retiring in the 1980s will pay an average of $15,808 in taxes (1983 dollars) on their benefits over the course of their retirement. Pension beneficiaries retiring between 2010 and 2019, in contrast, will pay an average of $44,672 in taxes (1983 dollars) on pension benefits during their retirement.

Retirees not only receive larger retirement incomes as a result of employer pensions, but their benefits are more secure due to legally mandated advance funding. This security is all the more important as debates over the fiscal stability of the Social Security system continue. Social Security benefits and employer pension benefits complement each other. As pension benefits increase, Social Security benefits become a smaller share of retirement income. If public policy continues to encourage increased pension coverage and benefit levels, the pension system could reduce the pressure for ever-increasing Social Security benefits.
7. What effect would the various tax reform or tax simplification plans such as the flat tax or modified flat tax or the value added tax have on employee benefits?

- The average taxpayer demanding tax reform because of a perception that the tax system is unfair does not see basic employee benefits as a tax abuse. Rather, both employers and employees see these benefits as part of the social contract that defines how individuals provide for themselves, their families, and their future. This social contract and related tax benefits includes the majority of the U.S. labor force. The distribution of benefit-related tax benefits among income groups reflects the distribution of coverage and participation. In 1981, employees earning between $15,000 and $50,000 received 71.8 percent of all health-related tax preferences, 64.5 percent of all pension-related tax preferences, and 67.5 percent of all insurance-related preferences. This group pays 51 percent of total federal taxes. By comparison, this income group received 64.2 percent of tax benefits related to homeownership. Employee benefits are less of a luxury than owning your own home.

- One of the most important consequences of tax reform proposals that seek to restructure the tax system for the average taxpayer would be to change the tax treatment of employer contributions for employee benefits.

- For workers with employee benefits there would be many implementation and transition issues in major tax reform. These could be formidable, and even predicting them involves some uncertainty about the reactions of employers, employees, insurers and other providers of benefits. This uncertainty arises from the fact that the availability of tax incentives for employee benefits has influenced how plans are provided and designed. For example, because employee benefits are purchased on a group basis, employers and employees can benefit from economies of scale. Therefore, a dollar spent on employee benefits by an employer buys more than would the same dollar spent by an individual. In the absence of tax incentives encouraging employer provision, the administrative structures that make group purchases cost-effective may never have been developed.

- Alternative treatments for employee benefits that have been proposed include:
  - Including benefit contributions in the employee's adjusted gross income;
  - Eliminating employer deductions for benefit contributions;
  - Capping the share of total compensation that can be provided in the form of tax-favored employee benefits;
  - Imposing an excise tax on the employer's benefit contributions; and
• **Imposing a value-added or national sales tax.**

• **Including benefit contributions in the employee's adjusted gross income:** most plans do not determine the costs of employee benefits on the basis of the characteristics of the individual for whom protection is being provided. These pricing structures are reasonable from employer's viewpoint given current tax treatment, since the total cost of insuring the employer's work force is not affected by the allocation of these costs among the members of the covered population. They are irrelevant to the employee who cares only about the total amount of insurance provided, and not about how the cost of this insurance is billed to the employer.

If employer contributions for benefits were taxed to the employee, the entire pricing and cost allocation structure of benefit plans could have to be revised to allocate contributions appropriately among individuals. While the average price of providing employee benefits to various employees may be uniform, the underlying cost of benefits differs widely according to the employee's age under all major benefits. Benefits for younger employees are less costly because these employees generally have lower health insurance claims, disability rates, and mortality rates. The adjustments that would be required would vary across benefits.

**Pensions:** actuarial methods used in defined-benefit pension plans do not generally allocate contributions or projected benefits to individuals, determining them instead for an employee cohort based on aggregate forecasts of that cohort's future demographic and economic experience. If defined-benefit pension costs were allocated among individuals, it would become clear that financing a given retirement benefit requires a lower contribution for a younger employee than for one closer to retirement age. The contribution for the younger employee can accrue interest over a longer period of time, while the same benefit increment for an older employee has to be financed primarily out of employer contributions.

Pension costs in a defined-benefit plan may therefore be ten times as high for an employee at age sixty as at age thirty. Attributing an average pension contribution to each employee would create serious inequities. Older employees would be undercredited, while younger employees would be overcredited. To the extent that older employees earn more and are taxed at a higher rate than younger employees, this inequity would be compounded.

**Health insurance:** employer contributions to finance health insurance are similarly based on the total cost of insuring a particular employee group. Underlying costs for health insurance can be twice as high at age sixty as they are at age thirty. Similarly, the underlying cost of providing health insurance for women of child-bearing age is higher than the cost of insuring young, single men. In short, the average price of most employee benefits is much
higher than the cost of providing benefits to some individuals and much lower for others.

If employer contributions for benefits were included in the tax base, they might be treated in the same way that the Internal Revenue Code now treats employer-paid life insurance premiums for coverage in excess of $50,000. These premiums are currently included in the tax base. The cost of life insurance varies according to the individual's age. For example, at age thirty, the cost of providing life insurance worth an individual's annual salary is 17 percent as large as it is at age forty-five, while at age sixty this cost is nearly four times as large.

To avoid the inequities that would arise if all individuals were taxed on an average cost of insurance, Treasury regulations prescribe the amount of premiums to be recognized as income for individuals on the basis of age (in five-year brackets) and coverage levels. The Treasury tables use blended actuarial assumptions for men and women based on the proportions of men and women in the group of employees with coverage over $50,000 in value.

To achieve an equitable distribution of tax liability, a schedule like that governing the tax treatment of life insurance would probably have to be developed for all employee benefits. Given the Supreme Court's decision in the Arizona v. Norris case, such tables would probably not be differentiated by sex. Such tables could, however, be differentiated by age, family status, or both. Family status could be used to predict health insurance claims under plans that offer maternity or dependents' benefits.

Effects of taxing benefits: the effects of taxing benefits would vary among benefits and would depend on whether or not individuals chose to continue their coverage. If pension accruals were taxed on a current basis, saving would almost certainly decline, and would decline disproportionately among those at lower income levels who do not tend to save out of current income.

To avoid the added tax liability, many low- and moderate-income individuals would choose to do without health and other types of insurance. Research conducted by the Employee Benefit Research Institute (EBRI) and others indicates that income determines whether or not people without employer-provided health coverage purchase such coverage themselves. If employers did not provide health coverage, most low-income workers would not purchase private health insurance. Since most people covered by an employer health plan are members of low- and middle-income families, employer-provided health benefits probably substantially raise rates of private health insurance coverage throughout the nonelderly population.

For those who chose to continue their insurance coverage, the impact of a tax on health insurance premiums would be regressive. While
Employer contributions for health insurance are independent of employee earnings. As a result, the value of employer-provided coverage is a larger share of total compensation at lower income levels and the added tax payment of low-income workers would be a larger share of their income than at higher income levels. EBRI tabulations of data produced by the Congressional Budget Office (CBO) indicate that under the Administration's proposal to cap the amount of health insurance premiums that an employee can receive tax-free, those with the lowest incomes would pay more than six times as much tax as a percent of income as those with incomes above $50,000.

The flatter rate structure of some major tax reform proposals would exacerbate this regressively. Under current-law rates, the progressivity of the tax schedule offsets the effect on tax liability of the declining share of health insurance in compensation at higher income levels.

In short, whatever the criterion used for determining the cost of each employee's cost of benefits, if it targeted those individuals likely to have the highest incidence of claims, it would also target those most likely to need insurance. Since those most likely to become sick, disabled, or die would face the highest tax liability, taxing employer contributions for benefits would impose tax liability in inverse proportion to ability to pay.

Another potential effect of taxing employee benefits to the individual could be to increase the attractiveness of flexible compensation or cafeteria plans. Under flexible compensation plans, employees can elect various levels of coverage under the major types of employee benefit plans. An employee choosing a less-generous health insurance plan, for example, can "spend" the employer's cost savings on added life insurance, vacation days, or other benefits. All employees--except for those who chronically guessed wrong about their need for health insurance or other benefits--would segregate themselves into plans according to the expected value of their claims. While this is the fundamental principle behind flexible compensation plans, many employers sponsoring these plans now price the high-cost insurance options at less than the value of the claims expected under them to maintain a reasonable risk pool of participants under each option. If employees were being taxed on the value of employer contributions, however, such subsidies would probably have to stop, since they would mean that low-risk employees would be paying the tax bill for higher-risk persons. If all persons chose plans priced at the expected value of their claims, the risk-sharing inherent in group insurance plans would be eliminated.

- Eliminating employer deductions for employee benefits: some of these distributional problems would not accompany major tax reform proposals that would include nonpension employee benefits in the tax base by eliminating employer tax deductions for them. The value-added tax
could have this effect, depending on how it was designed, and some versions of the consumption tax would provide for this.

Faced with such a provision, employers who now offer benefits would probably cut them back and those who do not would probably not institute them. Some employers who offer benefits might eliminate them or continue to offer them with full employee payment.

Others might forego improving their benefit packages, while still others might institute or increase employee contributions, deductibles, or copayments where appropriate. Employers are already working to reduce their benefit costs; including benefits in the tax base would clearly accelerate this process but at a social cost.

The greatest impact of proposals to eliminate employer deductions for benefits would probably be on those employees who are not now covered. Most employees without benefit coverage tend to be in smaller firms and at lower income levels. As small and new firms grow and become profitable, they are more likely to incur the financial commitment involved in establishing employee benefit plans. Removing the tax deductions for employee benefits would probably make this commitment uneconomical.

- **Capping employee benefits as a share of total compensation**: another alternative that has received some attention in tax policy debates, though not necessarily in the context of major tax reform, is establishing a limit on the share of total compensation that can be provided in the form of tax-favored employee benefits. Benefits provided in excess of this amount would be subject to payroll tax, income tax, or both. Under alternative proposals, the cap could cover contributions for all benefits, or pensions, welfare benefits, and so-called "fringe" benefits could all be capped separately.

Such an approach could raise its own set of problems. For example, an employer with a mature, long-tenure work force could be put at a competitive disadvantage compared with an employer with a younger work force, even if the benefits in the two firms were identical. Furthermore, a cap could act as a target that firms with less-generous benefit plans would feel compelled to meet to maintain their competitive positions. The efforts of such employers to catch up could offset the effects on employers whose benefits exceeded the cap. Such a system could also be difficult to implement for non-profit or public-sector employers, neither of which pay business profit taxes.

- **An excise tax on benefits**: rather than capping benefits as a share of compensation, the Treasury in 1983 proposed imposition of an excise tax on all tax-favored benefits, whatever their level. This would avoid creating a target benefit level for employers to reach. An excise tax, however, would have the same effect on benefits as eliminating employer deductions for benefit contributions. Employers
now offering benefits would cut them back, while those without benefits would probably not institute them. The only difference between the two options would be in the tax rates they would impose. If an excise tax carried lower rates than the corporate or business taxes the firm might be paying, then the incentives to eliminate benefits would not be as strong.

- **A value-added or national sales tax**: instituting a value-added tax would not have the same effect as a tax levied specifically on benefits. Any tax levied at different stages of production would be neutral between wages and benefits as a form of compensation, assuming that both were subject to the tax, and thus would not change employer and employee preferences.

8. **Should the tax law encourage employers to provide employee benefits; and if so, which benefits or services should be encouraged, and what type and level of tax incentive is appropriate?**

- The United States has always had a commitment to economic security for workers and retirees. Social Security with its income, health and disability components combines with workers compensation laws and unemployment compensation laws as an expression of public commitment. These social programs work with employer-sponsored programs to protect workers against significant health and economic risks. The government has established programs like Medicaid to take care of those without the employer protection, and it has provided tax incentives to encourage employer provision for the rest of the population.

- The tax incentive approach allows programs to be designed to accommodate very different workforces, geographic conditions, and employee preferences, while still carrying out the federal government's social support agenda. Unless the nation decides to step back from its commitment to economic security, tax incentives will be essential to benefit provision. The testimony sets out nine categories that now receive favorable tax treatment that can be evaluated.

9. **What conditions or restrictions are appropriate on tax incentives to encourage employers to provide employee benefits?**

- As a provider and encourager of benefits and economic security the government takes steps to assure that promised benefits are delivered, that all workers have access, and that expense is defined. This suggests funding requirements, nondiscrimination provisions, and percentage or dollar limits on employee benefits to control "tax subsidies or tax expenditures". It must be stressed, however, that the present system of benefit delivery would change if tax treatment changed.
10. **Are the existing rules concerning employee benefits sufficient to ensure that all employees benefit fairly from the tax incentives?**

- The data presented in this testimony provides a clear yes to this question.

11. **Are the existing tax incentives for benefits such as health care, life insurance, day care, educational assistance, and cafeteria plans effective in encouraging employers to provide these benefits to a broad cross section of employees at a lower total cost than if the Government provided the benefit directly, if employers provided the benefits on a taxable basis, or employees purchased these benefits on their own?**

- The first half of the question is easy to answer: benefits are being made available on a broad cross section basis. The second half of the question gets more complicated. And it is important that sound benefits be incorporated into this answer as well as cost. Note: employee benefits can accommodate different workers uniquely and can accommodate different geographic sections of the country; regressive taxation would result from the taxation of benefits where benefit cost is the same across the income stream (health, etc.); coverage gaps would be created if the employer chose to drop programs when taxed or also if employees chose to not purchase coverage. Finally, all available research indicates that the present system is the most cost effective and equitable method available to deliver the form and level of benefits now being provided.

12. **How will tax laws that encourage employers to provide employee benefits affect compensation planning?**

- Research and experience show that economic security benefits will be provided more readily in the presence of tax incentives. The presence of these incentives, along with qualification requirements, assures provision across the income spectrum. It encourages total compensation planning.

13. **Will tax incentives for employer-provided employee benefits affect potential employees' choice of employment?**

- The answer to this question is yes; the effect on behavior increases as workers grow older.
Numerous research projects sponsored by EBRI deal with these issues in greater detail. Examples are provided below.


*In smaller plans, the cost of providing health insurance for the marginal employee is based on the average costs of insuring the insured population of that community. In larger plans, the cost of insuring the marginal employee is based on the average cost of insuring the population represented by that employer's work force. While these two methods would be likely to yield different insurance costs for any given employee, under either method the cost of insuring that employee does not represent the cost of that employee's expected claims.

*For a thorough discussion of health insurance see Deborah J. Chollet, *Employer-Provided Health Benefits: Coverage, Provisions, and Policy Issues* (Washington, D.C.: Employee Benefit Research Institute, 1984), p. 94. An EBRI simulation of private health insurance suggests that 56 to 87 percent of all covered workers with 1979 family income less than $15,000 would not have purchased private health insurance, if an employer had not offered and contributed to their health insurance plan.

*For a discussion of employer efforts to reduce health care costs, see "Controlling the Cost of Health Care: Recent Trends in Employee Health Plan Design," EBRI *Issue Brief* no. 23, October, 1983.