

## 7. FINANCING SOURCES AND THE PRINCIPLE OF EQUITY

### PROGRESSIVE INCOME TAXES

Taxes on income are direct and progressive, which allow the equitable sharing of responsibility for financing the healthcare system based on people's ability to pay. The HCHR Campaign proposed a progressive income tax for healthcare in our 2012 report, after reviewing evidence of different tax systems across the world. An income tax's positive effect on equity can be enhanced by designing a progressive tax *structure*, in which the tax rate increases as income increases, so that higher income earners pay a greater proportion of their income than lower income earners. This can also be accomplished by taking into account a breadth of *different types of income*, for example through specifically taxing income sources generally found in high income populations, such as non-wage income from stocks, derivatives and other capital gains. Our proposal pursues a combination of both strategies; a progressive income tax structure up to a certain income threshold, coupled with a tax on unearned income to capture revenue beyond that threshold.

### **TAX ON EARNED INCOME**

The Governor's proposed income tax, which he called a "public premium", has progressive elements, such as a sliding scale between 138% and 400% of the Federal Poverty Level (FPL), and an exemption for individuals below 138% FPL. But it is also designed to benefit high-income earners by capping the amount of income subject to the tax. This regressive element can be seen in the shape of the tax curve, which becomes flat after it reaches 400% of the FPL and remains at 9.5% until the contribution reaches a cap of \$27,500. At this point, a household's actual tax payment stays at \$27,500, regardless of increases in income level. In effect, this creates a regressive tax rate that decreases as income increases.

The HCHR campaign's proposal eliminates this cap on contributions by the wealthy, based on the principle that wealthy households should pay according to ability, just as low and middle income families do. But eliminating the cap does not resolve the issue of the flat 9.5% tax and its implications for equity. Therefore, we propose a wealth tax on unearned income (discussed in the following section) that ensures that wealthy earners pay according to ability rather than according to an arbitrary flat tax.

The HCHR campaign's progressive tax curve was designed with the principle of equity in mind, using the following parameters:

1. Any household below 138% of the FPL is excluded from the income tax. This population qualifies for Medicaid, and is similarly excluded from the Governor's tax proposal.
2. There should be no exceptions in the form of capped contributions for high-income earners.
3. The tax should be designed to provide a sliding scale "on-ramp" for as many low and middle-income households as possible, with only higher income earners paying the maximum tax rate. Our target was that at least 75% of Vermont's population would be taxed on the sliding scale ramp and that no more than 25% would pay the maximum tax.

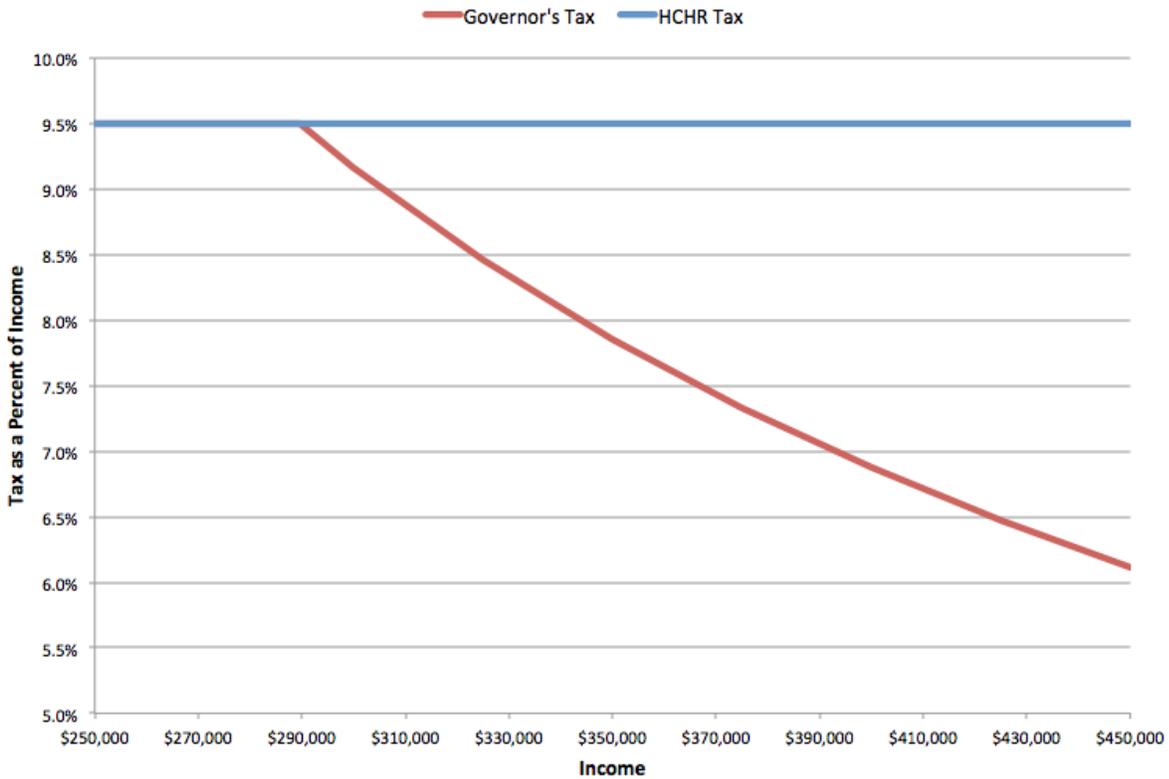
In order to make sure that low and middle-income families do not bear a disproportionate burden of healthcare costs, our proposed income tax starts with a 1% tax rate for households at 138% of the FPL, and reaches 9.5% at 523% of the FPL. All households above 523% of the FPL pay a tax of 9.5% on their household income.

Figure 2 shows how the HCHR tax provides relief for low and middle-income families relative to the Governor's proposal. Figure 3 shows the impact of removing the cap on the wealthiest households.

Figure 2. Governor's and HCHR Income Tax Curve for a Low- and a Middle-Income Household



Figure 3. Governor's and HCHR Income Tax Curve for a High Income Household



## Benefitting Low and Middle Income Families

The HCHR Campaign's income tax is designed to benefit low and middle income families:

- 76% percent of Vermont's population will be taxed at less than 9% of their income
- 65% of Vermont's residents will pay less than under the Governor's scenario
- People under 500% FPL<sup>46</sup> pay between 4% and 10% of their income on healthcare costs, whereas they would pay between 11% and 16% without a transition to GMC
- A family whose total income is \$50,000 will pay an average 40% less in healthcare costs than without GMC.<sup>47</sup>

## Generating Sufficient Revenue

Table 6. Revenue Estimates

<b>Total Revenue Generated by HCHR Income Tax</b>	<b>\$1,121,893,647</b>
Revenue Generated in Governor's Model	<b>\$1,097,000,000<sup>48</sup></b>
Difference	<b>\$24,893,647</b>

The HCHR Campaign's proposal generates a comparable amount of revenue to the Governor's proposal, when adjusted for the same populations (Table 6). As seen in Table 7, our proposal generates more revenue from higher income households, while forgoing revenue from lower and middle-income families. Through these changes, we are able to create a more equitable tax while generating similar revenue for GMC.

Table 7. Revenue Impact of Equity Features

Removing Cap	<b>+ \$131,385,433</b>
Flattening Curve	<b>-106,491,786</b>

(See Appendix A for *Methodology*)

## ***TAX ON UNEARNED INCOME***

The principle of equity requires that low- and middle-income people pay proportionally less of their income on healthcare costs than the wealthy. In the current healthcare system, the opposite is the case.<sup>49</sup> Our sliding scale income tax model changes this by progressively increasing tax rates in proportion to income. Yet we do not propose to increase the tax rate any further once the 9.5% threshold has been reached at 523% FPL; instead, the tax rate for people earning above that threshold stays flat (although we remove the Governor's cap on high earners).

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<sup>46</sup> Not counting the Medicaid population

<sup>47</sup> Comparing income tax and OOP contributions under GMC to premium and OOP contributions without GMC Scenario without GMC comes from RAND report projected figures for cost of healthcare for individuals under 65 in 2017.

<sup>48</sup> For comparison purposes to the HCHR scenario, this figure does not include contributions from out-of-state residents.

<sup>49</sup> Eibner et al., *The Economic Incidence of Healthcare Spending in Vermont*, January 2015.

To ensure that the very wealthy contribute based on their ability, we proposed in our 2012 report a wealth tax on assets, independent of income flows. We investigated existing wealth tax regimes in comparable settings (in Switzerland, where a wealth tax is levied at state level; and in Iceland, which has a comparable population size to Vermont), and estimated that a Vermont wealth tax could yield around \$88 million if applied in a similar way.<sup>50</sup> Yet we also flagged the lack of available data on taxable assets, and therefore do not have the necessary information to take our proposal further at this time. Instead, we propose two steps to increase the progressivity of Vermont’s income tax structure.

Repeal of capital gains exclusion

The first essential step to improving tax equity between the very wealthy and the rest of the population is to remove a tax loophole that disproportionately benefits those with great wealth. We propose, as we did in our 2012 report, to repeal the capital gains tax exclusion, which, according to the most recent figures, cost the state \$17.3 million.<sup>51</sup> This would increase the income tax base for funding the healthcare system and other essential public goods. In 2012, over \$7.8 million of this tax expenditure went to the very wealthy with incomes greater than \$1 million. The top 6% of taxpayers received almost 60% of this special tax benefit, which makes it highly inequitable. Vermont is one of only nine states that allows for this preferential treatment of certain forms of capital gains<sup>52</sup>; the principle of equity requires that this tax benefit be removed.

A tax on non-wage income

A new tax on unearned or non-wage income will ensure that those with substantial wealth contribute to GMC based on their ability. We propose a tax rate of 5% on non-wage income from stocks, dividends, capital gains, interest, and on the trading of stocks and derivatives. To design this tax in a progressive way, we extend a sliding scale credit to all tax filers with non-wage income under \$200k. Only unearned income above the credit amount will be taxed.<sup>53</sup>

Table 8. Tax credits for non-wage income

Total household income	Credit
Under \$25,000	\$5,000
\$25,000 to under \$50,000	\$4,000
\$50,000 to under \$75,000	\$3,000
\$75,000 to under \$100,000	\$2,000
\$100,000 to under \$200,000	\$1,000
\$200,000 or above	\$0

For example, for a household whose total income is between \$50,000 and \$75,000 the first \$3000 of non-wage income is tax exempt.

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<sup>50</sup> Healthcare Is a Human Right Campaign, “A Wealth Tax for Vermont? A Brief Look at International Examples,” August 2014.  
<sup>51</sup> Legislative Joint Fiscal Office, *Vermont Tax Expenditures: 2015 Biennial Report* (Vermont Department of Taxes, January 2015), 85.  
<sup>52</sup> Institute on Taxation and Economic Policy, *Who Pays? A Distributional Analysis of the Tax System in All 50 States*, January 2015.  
<sup>53</sup> The credit is not a reimbursement; the credit amount marks the threshold after which the tax takes effect.

We project that a tax on non-wage income, designed in this way, will generate annual revenue of \$97,335,100, and that 77% of this revenue will come from tax filers with incomes greater than \$200,000. A household with less than \$50,000 in total income would, on average, have no non-wage tax obligation, according to our projection.

Table 9. Average per person non-wage income tax obligation

<b>Total household income</b>	<b>Average per household tax obligation on non-wage income</b>
Under \$25,000	\$0
\$25,000 to \$50,000	\$0
\$50,000 to \$75,000	\$10
\$75,000 to \$100,000	\$152
\$100,000 to \$200,000	\$578
\$200,000 or above	\$9,002

## PAYROLL TAXES FOR UNIVERSAL HEALTHCARE

Employers currently pay around 80% of private health insurance premiums.<sup>54</sup> In Green Mountain Care, these premium payments will no longer be necessary, as all employees will be eligible for publicly financed healthcare. Instead, businesses will contribute to the universal healthcare system, paying their share toward funding an essential public good that ensures the health of their employees.

The principle of equity applies to businesses as well as individuals. Once healthcare is decoupled from employment and financed through taxation, businesses contribute according to their ability to pay, which is best measured by profits or surplus revenue generated. In theory, corporate income taxes would be the most equitable way to ensure that business contributions are sensitive to ability to pay. The HCHR campaign explored the feasibility of using corporate income taxes in our 2012 report, yet we found that only a minority of businesses are subject to corporate income tax, that loopholes were numerous and that tax avoidance was a significant problem. For these reasons, we concluded that unless Vermont implemented comprehensive corporate tax reforms, corporate income tax would not be an equitable, stable and sufficient mechanism for ensuring that businesses contribute to healthcare financing.<sup>55</sup> Instead we proposed a progressive payroll tax for businesses, levied on employers only, not employees.

In his report, Governor Shumlin likewise suggested a payroll tax on employers only. Yet with a proposed flat tax rate of 11.5% for all businesses, capped at wages for any individual employee in excess of \$200,000, the Governor’s plan failed to account for businesses’ ability to pay, which turned into a major obstacle for proceeding with universal healthcare financing. Large businesses, and those with high executive compensation,

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<sup>54</sup> University of Massachusetts Medical School Center for Health Law and Economics, and, and Wakely Consulting Group, Inc., *State of Vermont Health Care Financing Plan Beginning Calendar Year 2017 Analysis*.

<sup>55</sup> Healthcare is a Human Right Campaign, *Toward Equitable Financing of Green Mountain Care*, December 2012, p. 11-14.

would do significantly better under the Governor's plan than the smallest of businesses. The Governor's report concluded that the transition costs for small businesses that currently do not provide health insurance would be too high, and he dismissed scenarios for gradually transitioning businesses to the same flat rate as too costly.

The HCHR Campaign proposes a different payroll tax approach. We noted in our 2012 report the inequity of charging small businesses the same tax rate as large corporations. We also noted that a payroll tax could lead to a depression of wages. To mitigate these challenges, we proposed the idea of a graduated tax that takes into account business size as well as wage disparity.<sup>56</sup>

Based on these goals, we have now developed a payroll tax model that generates sufficient revenue for financing GMC while protecting small businesses and preventing negative wage effects. Payroll tax rates will be lower for small businesses and businesses with low wage disparity, and higher for larger corporations and those that have a greater top to bottom wage ratio. Specifically, our proposed tax model will ensure that businesses pay according to their ability in the following ways:

1. A sliding scale tax rate from 1% to 20%, increasing with company size and wage ratio of top-tier salaries to bottom-tier salaries.
2. Nine size-based tax categories, from businesses with 4 or fewer employees to more than 1000 employees.
3. A wage ratio that measures the discrepancy between the wages of the top 1% (i.e. management and CEOs) and the average wage of the bottom 50% of workers. If a company's wage ratio is greater than average, the company will pay a higher tax than others in its size category, if its wage ratio is lower than average, the company will pay less.

The principle of equity is the guiding factor for this proposal. Only if businesses are actually able to pay without experiencing challenges to their financial viability, and only if they are encouraged to raise rather than depress the wages of those earning the least, will a payroll tax financing mechanism be beneficial for Vermont. A payroll tax graduated by business size and wage gap will meet this standard in the following ways:

1. The tax obligation increases with business size, measured in the number of full-time equivalent employees (FTE). This gives relief for small businesses and ensures that large corporations and large public employers pay what they can. Large employers' current payment for health insurance premiums indicates their ability to pay; the majority of businesses that do not offer insurance are small.
2. The tax obligation decreases with greater wage equality. This will prevent negative wage effects and incentivizes income equality.
  - a. Introducing wage ratio as a variable in tax obligations prevents the lowering of worker wages. If a company seeks to pass the cost of the tax onto their employees by reducing wages of the bottom 50% of workers (but not executives), their wage ratio "rating" will get worse and result in a higher tax rate. If a company seeks to pass the cost of the tax onto *all* workers (including executives) by reducing everyone's wages (and thus maintain the same wage ratio), their tax contribution will be lowered through a decrease in payroll size, but not a decrease in their tax rate. In other words, a company may want to reduce their payroll size in order to reduce their tax contribution (an inevitable incentive produced by any payroll tax), but the wage ratio rating prevents the lowering of the wages of only the bottom 50% of workers as a way to achieve this goal.
  - b. The wage ratio model provides an incentive for increasing equity between workers' and CEO's wages, as a company's tax obligation will be reduced if CEO wages are lowered or workers' wages raised.

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<sup>56</sup> Healthcare is a Human Right Campaign, *Toward Equitable Financing of Green Mountain Care*, December 2012, p.16.

- c. The inclusion of the wage ratio in our payroll tax model reduces the risk that a business would reduce its size solely to decrease its tax rate, because company size has less weight in our model than in a graduated tax model based only on size. Similarly, companies would be disincentivized to lay off workers from the bottom 50 % of earners, as this would increase the company’s wage ratio and thereby its tax rate. A company could only effectively reduce its tax obligations by laying off the top 1% wage earners. Similarly, the inclusion of the wage ratio factor helps mitigate against hiring disincentives created by the size factor.

Modeling Results

We have modeled various payroll tax scenarios using industry level wage and size data. Based on the modeling outputs, we recommend a company level payroll tax formula that results in the following average tax rates.

The smallest businesses (1 to 4 workers) receive a size credit – a credit that results in a zero tax obligation for the business if each employee receives the same wage. However, on average, our model shows that those smallest businesses do not have equal wages across the board and therefore, despite the size credit, will pay a payroll tax of around 4%. This means that over 60% of Vermont businesses would have an average tax obligation of 4%, determined solely by the gap between the wages of the top 1% and bottom 50% of wage earners. All businesses under 50 employees - the vast majority of Vermont businesses - would pay a lower tax rate than under the Governor’s proposal. Our model suggests that the top end of the tax scale would be occupied by companies with over 1000 employees and public sector employers, as well as mid-size and large companies with high wage discrepancies. To ensure predictability of tax obligations, and to avoid large tax burdens, we have capped the tax rate at 20%. According to the model, some mid-size as well as large companies benefit from this cap, as their high wage gaps would otherwise take them beyond a 20% tax rate.

Table 10. Distribution of businesses and average tax rate by business size, 2017

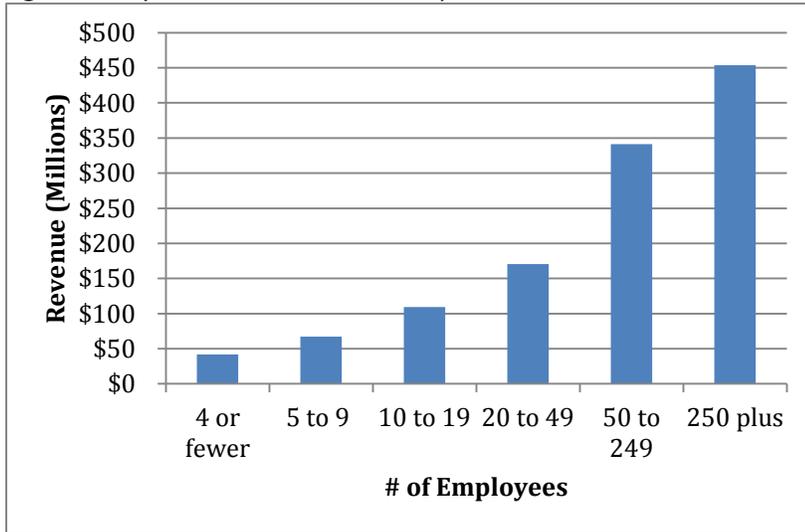
<b>Business size</b>	4 or fewer workers	5 to 9 workers	10 to 19 workers	20 to 49 workers	50 to 99 workers	100 to 249 workers	250 to 499 workers	500 to 999 workers	1,000 plus workers	Gov’t
<b>Average tax rate</b>	4.10%	7.72%	9.88%	10.68%	12.32%	14.41%	15.74%	16.96%	19.81%	20%
<b>% of private businesses</b>	60.49%	18.04%	11.28%	6.94%	1.88%	1.03%	0.18%	0.11%	0.06%	N/A

Table 11. GMC payroll tax rates, 2017 – Governor’s proposal and HCHR proposal

<b>Business Size</b>	4 or fewer workers	5 to 9 workers	10 to 19 workers	20 to 49 workers	50 to 99 workers	100 to 249 workers	250 to 499 workers	500 to 999 workers	1,000 plus workers
<b>Gov’s payroll tax proposal</b>	11.5%	11.5%	11.5%	11.5%	11.5%	11.5%	11.5%	11.5%	11.5%
<b>HCHR payroll tax proposal</b>	4.10%	7.72%	9.88%	10.68%	12.32%	14.41%	15.74%	16.96%	19.81%
<b>Difference Gov. &amp; HCHR</b>	-7.40%	-3.78%	-1.62%	-0.82%	0.82%	2.91%	4.24%	5.46%	8.31%

In our simulation at industry level, these average tax rates yield \$1,605,110,481 in revenue. The modeling inputs can be changed to produce different rates and different revenue projections as needed. It is important to note that this model is designed for the purpose of predicting revenue only. We do not propose to set tax rates by size and/or wage ratio categories; instead, each business will calculate its own actual rate, based on the formula provided.

Figure 4. Payroll tax contributions of private businesses



Payroll tax calculator

Our modeling produces an equitable tax formula that raises sufficient revenue by giving similar weight to size and wage ratio variables.

Payroll tax amount per employee:  $r \times w + i$

Wage ratio  $r$  = average wage of the top 1% of wage earners divided by the average wage of the bottom 50% of wage earners. The wage ratio cannot be smaller than 1 ( $r \geq 1$ ). If  $r$  equals 1, this means everyone employed by a business earns the same wage.

$w = 650$ ;  $i =$  see table below

FTE	1-4	5-9	10-19	20-49	50-99	100-249	250-499	500-999	1000+	Gov't
	-650	-300	300	800	1750	3000	6250	7500	12,000	10,000

The values of the coefficients  $w$  and  $i$  have been set based on our modeling outputs. Below we have also tested the formula with sample companies.

Comparing modeling data with sample companies

Below are three sample scenarios that illustrate how the payroll tax formula would be applied by individual companies.

#### Company 1:

A very small company with 3 employees. The highest wage earner has a salary of \$60k, the other two employees each earn \$40k.

Wage ratio: 60/40:  $r=1.5$

$1.5 * 650 + (-650) = \$325$  per person. This company pays \$975 payroll tax per year - a tax rate of 0.7%.

#### Company 2:

A small company with 6 employees. Its CEO gets paid \$150k, the director makes \$100k and four workers get paid \$50k.

Wage ratio: 150/50:  $r = 3$

$3 * 650 + (-300) = \$1,650$  pp, to a total of \$9,900 per year. Since its total payroll is \$450,000, this company's tax rate is 2.2%.

#### Company 3:

A mid-sized company with 75 employees. The CEO gets paid \$150k, the bottom 50% of workers receive an average wage of \$29,737. The wage ratio is 5.04.

$5.04 * 650 + 1750 = \$5,029$  pp, to a total of \$377,157 per year. This company's total payroll is \$3,300,000, which means its tax rate is 11.43%.

In these examples, companies 1 and 2 – both small businesses under 10 employees - pay tax rates below the modeled average. We assume that the modeling outputs tend to overestimate tax rates for small size businesses, which are likely to have a much lower wage ratio than larger companies. In our modeling, we were limited to industry level data, which is likely to produce higher wage ratio estimates than company level data, especially for smaller businesses. Although we made adjustments to the modeling inputs to address this issue, it is possible that tax yields from small businesses will be lower in reality than in our model, unless the wage ratio coefficient beta is adjusted upwards. That said, small businesses contribute only a small part of the overall tax revenue (see Figure 4), and we explicitly designed the model to benefit small businesses with excellent wage ratios.

The state also has the option to produce an accurate and updated revenue projection by conducting a data survey prior to implementation of GMC, asking all businesses subject to the payroll tax to submit their calculated tax rates for review. This “trial run” would enable an accurate revenue forecast for the first year of implementation.

(See Appendix C for Methodology)

## STATE AND FEDERAL FUNDING SOURCES

Significant funding for Green Mountain Care will come from existing state and federal sources, including from Affordable Care Act (ACA) premium subsidies once Vermont obtains a Section 1332 waiver that enables the dissolution of Vermont Health Connect. For the purposes of this report, we mostly accepted the funding projections listed in the Governor's report when calculating state and federal revenues for GMC, even though it appears that not all available state and federal funds were included in the Administration's estimates. While some state Medicaid funding streams are explicitly listed,<sup>57</sup> many others are not, and we are unable to ascertain

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<sup>57</sup> Shumlin et al., *Green Mountain Care: A Comprehensive Model for Building Vermont's Universal Healthcare System* Appendix, Table F-1.1.

whether these have been deliberately omitted, and if so, for what reasons. We reiterate our concern with the lack of transparency in the Administration's processing of primary data, which makes it difficult to discern how existing state funds are accounted for.

We estimate that additional existing state and federal funds are likely to be available for incorporation into GMC, yet in lieu of firm evidence, we opt to accept the Governor's conservative estimates. We do, however, have a different proposal for one identified source of state funding, Vermont's various provider taxes.

### **PROVIDER TAXES**

The Governor's report proposes to eliminate five provider taxes (specified at 33 V.S.A. §1953-55b), which are projected to generate \$ 152,058,604 in 2016 (Appendix Table F-1.2). We agree with the Administration that these taxes are – and have, in fact, always been - largely circular;<sup>58</sup> however, we propose a phasing out period, tied to the establishment of an effective hospital and pharmaceuticals rate setting system.

Specifically, we propose to maintain the assessment on hospitals and the very small assessment on pharmaceuticals, which together are projected to generate \$131,950,013 in 2016, until effective price controls are in place. Since the Governor's proposal is not fully transparent about its assumptions regarding the baseline costs of health services in GMC, such as what price control mechanisms are incorporated into the projected 4% annual cost inflation rate, we cannot be confident that effective rate setting for the cost of services, as set forth in 18 V.S.A § 9376 (b), is included in the calculation of GMC cost trends. The UMass/Wakely report recommended reducing current commercial insurance rates from 155% to 105% of Medicare rates.<sup>59</sup> No set rates are specified in the Governor's report; rather, it appears that baseline and projected costs continue to be based on existing prices charged by hospitals and pharmaceutical companies, especially those in near monopoly market positions.

In this context, eliminating these two taxes without setting reasonable rates for services supplied under GMC would effectively result in a windfall for hospitals at the expense of the health system as a whole. Until an all-payer rate setting system is fully operational and results in effective price controls for health services, we propose maintaining existing checks and balances with the hospital and pharmaceuticals tax. Once prices start getting under control, these two taxes can be phased out.

## **8. RESULTS AND RECOMMENDATIONS**

This report has put forward a concrete financing plan for Green Mountain Care and presented new evidence for the economic feasibility of a state-based universal, publicly financed healthcare system. By taking the blueprint provided by Vermont's Governor and addressing the challenges raised in his report, we created solutions that demonstrate the viability of GMC.

Our plan builds a comprehensive healthcare system that vastly improves access to care for all Vermont residents, beyond the Governor's proposals, and lays out additional scenarios for a phased implementation of meeting all healthcare needs of all people in the state. Importantly, our plan guarantees that this system will be financed in an equitable way, thus giving immense relief to low- and middle-income people who are currently

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<sup>58</sup> Shumlin et al., *Green Mountain Care: A Comprehensive Model for Building Vermont's Universal Healthcare System*, p.37.

<sup>59</sup> University of Massachusetts Medical School Center for Health Law and Economics, and, and Wakely Consulting Group, Inc., *State of Vermont Health Care Financing Plan Beginning Calendar Year 2017 Analysis*. p.25.

burdened with disproportionately high healthcare costs. Even the Governor’s report showed that 9 in 10 families will benefit financially from public healthcare financing;<sup>60</sup> our more progressive income tax proposal creates further savings in healthcare costs for low- and middle income families.

At the heart of our financing plan is an equitable payroll tax for businesses that solves the Governor’s main conundrum: how to ensure that businesses pay into the system based on their ability. By graduating the tax based on business size and wage discrepancy, we designed an equitable tax that is affordable for all businesses.

Finally, our plan greatly increases transparency, accountability and participation in the healthcare system by moving responsibility for administering healthcare as a public good to a public corporation, the Green Mountain Care Board.

This financing plan shows that the small state of Vermont, despite legal and financial challenges, can adopt an equitably financed healthcare system that provides universal care as a public good, accountable to the people. This can be done in a financially sustainable way, as our balance sheet shows, especially if reforms within the healthcare delivery system, which are not fully reflected in these figures, start taking shape.

Our financing plan improves the GMC Fund’s fiscal position in 2017 by over \$200 million compared to the Governor’s proposal. While we do not have access to the econometric model that enabled the Governor to trend these projections forward until 2021, this sizable initial surplus creates a solid basis for maintaining a positive fiscal position in the longer term. Compared to the failing current healthcare system, which is projected to consume a growing part of people’s incomes and of state spending, a publicly financed alternative is the only rational solution.

Table 11. Comparison of GMC Balance Sheets, in millions, 2017

	<b>Governor</b>	<b>HCHR</b>
<b>Spending</b>		
Cost of GMC Services and Operation	<b>-4,340</b>	<b>-4,354</b>
<b>Revenue</b>		
<b>Federal Funding</b>		
Federal Medicaid Match	1,310	1,310
Federal ACA Waiver Funding	106	106
<b>State Funding</b>		
State Medicaid	344	344
Hospital & Pharma Tax	--	132
<b>New Revenue Needed</b>	<b>-2,580</b>	<b>-2,462</b>
Payroll Tax	1,510	1,605
Income Tax	1,247	1,122
Non-wage income tax	--	97
<b>GMC Fund Fiscal Position</b>	<b>177</b>	<b>362</b>

<sup>60</sup> Shumlin et al., *Green Mountain Care: A Comprehensive Model for Building Vermont’s Universal Healthcare System*, December 30, 2014, p. 54.

Our financing plan achieves this sound fiscal position even with providing additional health services and giving out-of-pocket cost relief to seniors. The tables below show detailed cost and revenue estimates for Green Mountain Care.

Table 12. GMC cost projection, in millions, 2017

<b>GMC services</b> (excludes out-of pocket)	
GMC Primary (Residents, Non-Medicaid)	1,971
GMC Medicaid Primary	1,126
State Medicaid Fixed Costs	680
Medicaid Dual Eligible	259
Employer Sponsored Insurance Wrap	28
Dental, vision, hearing	195
Medicare Affordability Credit	48
<b>Total Cost</b>	<b>4,307</b>
<b>State Operations Cost</b>	
Insurance reserves	146.2
Insurance reserves from BCBS	(132)
Health Care Innovation Spending	23
Contingency	10
<b>Total GMC Annual Cost</b>	<b>4,354</b>

Table 13. GMC revenue projection, in millions, 2017

<b>Federal Funds</b>	
Federal: Medicaid Match	1,310
Federal: ACA Waiver Funds	106
<b>Total Federal Funds</b>	<b>1,416</b>
<b>Existing State Funds</b>	
State Medicaid Revenue	344
Hospital & Pharma Tax	132
<b>New GMC Taxes</b>	
GMC Payroll Tax	1,605
GMC Income Tax	1,122
GMC Non-wage Income Tax	97
<b>TOTAL State Funds</b>	<b>3,300</b>
<b>TOTAL GMC REVENUES</b>	<b>4,716</b>

In summary, our plan's main additional costs consist of \$195 million for adult dental, vision and hearing care, and \$45 million for a Medicare Affordability Credit to give out-of-pocket cost relief to seniors. Our plan's main additional revenue centers are an extra \$105 million from a more equitable payroll tax, \$97 million from a wealth tax on unearned income, along with maintaining at least a portion of the provider tax until all-payer rate setting produces effective cost controls. As stated in chapters 5 and 6, additional cost savings should be implemented through measures such as rate setting, drug price negotiation and a public administration system. Yet in keeping with conservative projections, we have refrained from changing the Governor's estimate of GMC administrative overhead (at 7%) and growth in system costs (4%).

## PHASE-IN OF SYSTEM IMPROVEMENTS AND EXPANSIONS

The plan outlined in this report is designed as the baseline for implementing GMC by 2017. In chapters 3 and 4 we showed scenarios for increasing the universality of the system, both in terms of people included and health services provided. We consider these expansions essential steps toward building a truly universal system. Some of these steps require legal permission; others simply need better data to produce cost and revenue projections. We recommend taking the following phase-in steps:

1. Extend dental, vision and hearing services to Medicare recipients: this can be done immediately upon obtaining a cost estimate and designing a financial contribution mechanism for Medicare recipients.
2. Implement a fuller Medicare wrap-around approach that replaces our proposed out-of-pocket credit.
3. Ensure that savings measures, such as all payer rate setting, moving away from fee-for-service, drug price negotiation, malpractice reform, etc. are implemented swiftly.
4. Increase GMC's actuarial value to 100% A/V.
5. Include residents from other states in GMC if they work in Vermont.
6. Obtain a federal Medicare waiver and include the Medicare population in GMC.
7. Incorporate Workers' Compensation into GMC.
8. Include long-term care in GMC.

## 10. CONCLUSION

Vermont has the ability and obligation to implement a universal, publicly financed healthcare system by 2017, as set out by state law enacted in 2011. The HCHR Campaign's financing plan improves upon the Governor's proposal with a more equitable solution for businesses' contribution to the healthcare system, thus making payroll financing economically feasible. Our plan sets GMC on a solid financial footing, with a \$362 million surplus in 2017, and guarantees access to comprehensive healthcare for all Vermont residents. By transitioning from private, market-based insurance to public financing of universal care, it flips the way we pay for care: people will contribute based on their ability, so that low- and middle-income people pay a smaller share of their income on healthcare than the wealthy – the opposite of the current system.

Vermont cannot afford to maintain a dysfunctional market-based insurance system that fails to provide adequate access to care and has unsustainable rates of cost growth. Fundamental changes are needed to ensure that healthcare financing and delivery systems serve the people of Vermont, realize their right to health and advance equity. Those changes cannot be made in a piecemeal fashion, as all components of a healthcare system are interconnected. Guided by years of studies, reports, modeling and projections, Vermont is ready to implement a public financing plan for GMC, and we submit our proposal for serious consideration. Only by providing healthcare as a public good, equitably financed and publicly administered, can Vermont finally realize the promise of ensuring the human right to healthcare for all.

## APPENDIX A: MEDICARE METHODOLOGY

### Assumptions:

- 128,739 of Medicare recipients in Vermont are above 138% of the FPL and not dual eligible, therefore qualifying for GMC secondary coverage according to the UMass/Wakely Report<sup>61</sup>
- The distribution of individuals at various percentages of FPL is the same for the Medicare population as it is for the population described in the RAND report. Following this assumption, roughly 60% of the Medicare population is between 138% and 523% of the FPL, or 80% of those who qualify for wrap coverage are between 138% and 523% of the FPL. Therefore, 96,554 Medicare recipients will receive the Medicare Affordability Credit on a sliding scale.
- The Medicare population is evenly distributed between 138% and 523% FPL, and the average recipient will receive the average level of support -- 100% of out-of-pocket savings seen by Green Mountain Care recipients.

### Calculating Cost:

Average Medicare Affordability Credit X Qualifying Population  
\$497 X 96,554= \$47,998,066

### *ALTERNATIVE PROPOSAL 1*

Raising the actuarial value (AV) of the Medicare population from the average to 94% to match the Green Mountain Care population.

**Assumptions:** The average Medicare recipient receives coverage at an actuarial value of ~85%.

The extra cost of bringing Medicare recipient from ~85% AV to ~94% AV is \$80 PMPM<sup>62</sup>, which is \$960 per year. According to the Governor's projection, the Medicare population will be 140,000 in 2017. Therefore, the total annualized cost of this proposal is \$134,400,000.

### *ALTERNATIVE PROPOSAL 2*

Raising the AV of the Medicare population from the average to 100% AV.

### **Assumptions:**

- 1) The average Medicare recipient receives coverage at an actuarial value of ~85%
- 2) Medicare population in 2017: 140,000

The extra cost of bringing Medicare recipients from ~85% AV to ~100% AV is \$132 per member per month<sup>63</sup>. Therefore, the total annualized cost of this proposal is \$222,284,160.

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<sup>61</sup> Ibid.

<sup>62</sup> Cost extrapolated from table in Shumlin et al., *Green Mountain Care: A Comprehensive Model for Building Vermont's Universal Healthcare System*, Appendix B-10.

<sup>63</sup> Ibid.

## APPENDIX B: INCOME TAX METHODOLOGY

Our income tax design mirrors the income tax scenarios put forth by the Governor. The appendix to the Governor’s report includes 14 “Alternative Financing Concepts”, some of which with similar features to ours, including flattening the ramp of the tax curve and excluding out-of-state residents<sup>64</sup>. However, the exact combination of measures to increase equity, as put forward above, are not among the Governor’s modeled scenarios. With access to the model used for the Governor’s projections, calculating the revenue generated by our proposed income tax would be straightforward and require minimal effort. In the absence of access to this model, we developed our own methodology for calculating the expected income tax revenue, as described below.

### DESIGNING THE TAX CURVE

#### Determining the Federal Poverty Level for 2017

For the purposes of this report, the FPL for 2017 was calculated based on projections from the RAND report, which forecasts that 100% of the FPL will be a household income of \$12,506 for a single individual and \$25,559 for a family of four<sup>65</sup>. From those data points, calculations were made to determine the salary at 138% FPL and 523% FPL for various household sizes.

Table 1: Projected household incomes at 100% FPL

% FPL	Household Size	Income
100%	1	\$12,506 <sup>66</sup>
100%	2	\$16,857
100%	3	\$21,208
100%	4	\$25,559 <sup>67</sup>
100%	5	\$29,909

#### Vermont Population and the Federal Poverty Level

Roughly 75% of Vermont’s population is below 523% of the FPL. We used this as a guideline for determining the point at which the income tax should reach its maximum level of 9.5%.

#### Household Income and Tax Rates

Knowing the household income start and end points of the tax, the equation for a straight line was used to generate multiple points along the tax curve and create a guide for tax rates for various households at various income levels.

Table 2. Guide for determining individualized tax based on household size, household income, and universal healthcare tax rates<sup>1</sup>

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<sup>64</sup> Shumlin et al., *Green Mountain Care: A Comprehensive Model for Building Vermont’s Universal Healthcare System*, Appendix F–3.

<sup>65</sup> Eibner et al., *The Economic Incidence of Healthcare Spending in Vermont*, 12.

<sup>66</sup> Ibid.

<sup>67</sup> Ibid.

Tax Rate (% of income)	Taxable Income: 1 Person Household	Taxable Income 2 Person Household	Taxable Income 3 Person Household	Taxable Income 4 Person Household	Taxable Income 5 Person Household
0% if taxable income is below:	\$17,258	\$23,262	\$29,267	\$35,271	\$41,275
1% if taxable income is above: <b>but below:</b>	\$17,258 <b>\$22,917</b>	\$23,262 <b>\$30,890</b>	\$29,267 <b>\$38,863</b>	\$35,271 <b>\$46,836</b>	\$41,275 <b>\$54,809</b>
2% if taxable income is above: <b>but below:</b>	\$22,917 <b>\$28,576</b>	\$30,890 <b>\$38,518</b>	\$38,863 <b>\$48,460</b>	\$46,836 <b>\$58,401</b>	\$54,809 <b>\$68,343</b>
3% if taxable income is above: <b>but below:</b>	\$28,576 <b>\$34,235</b>	\$38,518 <b>\$46,146</b>	\$48,460 <b>\$58,056</b>	\$58,401 <b>\$69,966</b>	\$68,343 <b>\$81,877</b>
4% If taxable income is above: <b>but below:</b>	\$34,235 <b>\$39,894</b>	\$46,146 <b>\$53,773</b>	\$58,056 <b>\$67,653</b>	\$69,966 <b>\$81,532</b>	\$81,877 <b>\$95,411</b>
5% If taxable income is above: <b>but below:</b>	\$39,894 <b>\$45,553</b>	\$53,773 <b>\$61,401</b>	\$67,653 <b>\$77,249</b>	\$81,532 <b>\$93,097</b>	\$95,411 <b>\$108,945</b>
6% If taxable income is above: <b>but below:</b>	\$45,553 <b>\$51,212</b>	\$61,401 <b>\$69,029</b>	\$77,249 <b>\$86,845</b>	\$93,097 <b>\$104,662</b>	\$108,945 <b>\$122,479</b>
7% If taxable income is above: <b>but below:</b>	\$51,212 <b>\$56,871</b>	\$69,029 <b>\$76,657</b>	\$86,845 <b>\$96,442</b>	\$104,662 <b>\$116,227</b>	\$122,479 <b>\$136,013</b>
8% If taxable income is above: <b>but below:</b>	\$56,871 <b>\$62,530</b>	\$76,657 <b>\$84,284</b>	\$96,442 <b>\$106,038</b>	\$116,227 <b>\$127,793</b>	\$136,013 <b>\$149,547</b>
9% If taxable income is above: <b>but below:</b>	\$62,530 <b>\$65,359</b>	\$84,284 <b>\$88,098</b>	\$106,038 <b>\$110,837</b>	\$127,793 <b>\$133,575</b>	\$149,547 <b>\$156,314</b>
9.5% if taxable income is above:	\$65,359	\$88,098	\$110,837	\$133,575	\$156,314

## CALCULATING REVENUE

### Selecting a Revenue Base

The earned income tax was applied to the state total Adjusted Gross Income in Vermont, as was the Governor's projection, for tax returns representing individuals under 65 in 2013<sup>68</sup>. This particular tax base excludes the Medicare population and out-of-state residents.

### Determining Average Household Size

<sup>68</sup> Vermont Tax Department, "2013 Vermont Personal Income Tax Returns- Individuals Under Age 65," December 2014.

Average household size, for the purpose of determining income in relation to the start and end points of the tax curve (138% FPL and 523% FPL), was calculated with the following equation:

$$\begin{aligned} & \text{(Total Vermont in-state returns under 65 in 2012} \\ & \text{+ Total count of dependents for all ages in 2012 in Vermont)} \\ & \text{/Total Vermont in-state returns under 65 in 2012} \\ & \text{= Average Household of 1.58 individuals} \end{aligned}$$

2012 figures<sup>69</sup> were used because figures for number of dependents were not available for Vermont in 2013. All dependents were attributed to tax filers under 65, based on the assumption that a majority of the dependents would be on tax returns of filers under 65.

$$(255,589 \text{ returns} + 148,160 \text{ dependents}) / 255,589 \text{ returns} = 1.58 \text{ individuals}$$

**Determining Income Targets for Household of 1.58**

Income for a household of 1.58 at 100% FPL was determined by adding .58 of the difference in income between a household of 1 and a household of 2 at 100% FPL to the income for a household of 1 at 100% FPL. Then, this figure was multiplied by 1.38 to find income for a household at 138% FPL, \$20,741. Similarly, the income at 100% FPL was multiplied by 5.23 to determine the income at 523% FPL.

Table 3.

<b>% FPL</b>	<b>Household Size</b>	<b>Income</b>
138%	1.58	\$20,741
523%	1.58	\$78,548

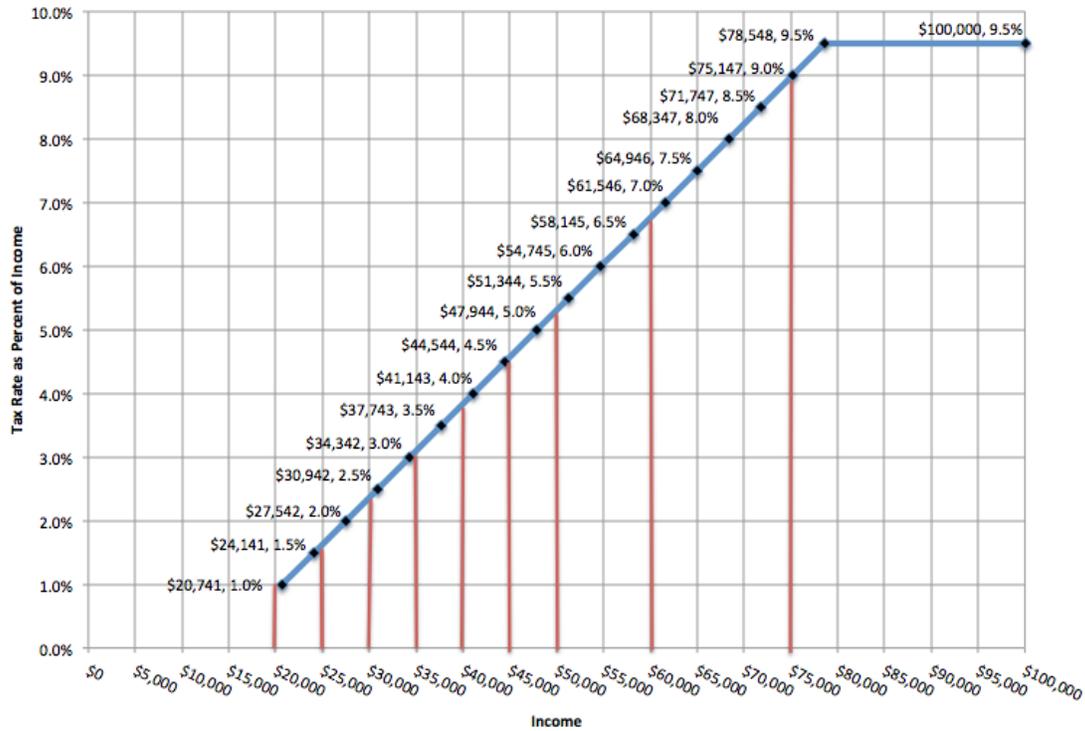
**AGI at Various Income Levels**

Vermont income tax returns report AGI in income classes. The following figure shows the Vermont Tax Return income ranges as they correspond with a HCHR tax curve designed for a household of 1.58.

Figure 1. Tax rate as a percentage of income for a household of 1.58 and AGI Income Ranges

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<sup>69</sup> Vermont Tax Department, “2012 Vermont Personal Income Tax Returns- Individuals Under Age 65,” December 2013.



\*Vertical lines represent the delineations between income classes as defined by Vermont Tax Returns.

With the assumption that income is distributed evenly within income classes, tax rates were applied to each income range based on averages of the tax rates present in each income range. The following table shows the average rate at which each income class is taxed for the purpose of taxing total income in that range, and the revenue generated from each income class. Note, this procedure is for generating a total revenue estimate for the income tax, and therefore deals with a “synthetic” household of 1.58 individuals. For individuals to determine their personal tax rates, Table X shows tax rates, household income, and household size.

Table 4. Income tax rate and income class

Income Range	Tax	Income Range	Tax
0.01-4999	0	50000-59999	6.00%
5000-9999	0	60000-74999	7.75%
10000-14999	0	75000-99999	9.25%
15000-19999	0	100000-124999	9.50%
20000-24999	1.25%	125000-149999	9.50%
25000-29999	2.00%	150000-199999	9.50%
30000-34999	2.75%	200000-299999	9.50%

35000-39999	3.50%	300000-499999	9.50%
40000-44999	4.25%	500000-999999	9.50%
45000-49999	5.00%	1000000	9.50%

Table 5. Total income tax revenue generated by income class

Income Class	Revenue	Income Class	Revenue
0.01-4999	0	50000-59999	\$55,516,656.48
5000-9999	0	60000-74999	\$101,381,308.10
10000-14999	0	75000-99999	\$186,716,392.08
15000-19999	0	100000-124999	\$141,695,916.96
20000-24999	4882791.65	125000-149999	\$89,758,419.84
25000-29999	\$9,244,170.70	150000-199999	\$102,037,011.67
30000-34999	\$13,991,647.64	200000-299999	\$88,573,657.17
35000-39999	\$17,584,925.30	300000-499999	\$63,420,222.55
40000-44999	\$20,679,530.19	500000-999999	\$48,017,942.00
45000-49999	\$23,271,291.15	1000000 and over	\$90,258,618.69
		<b>Total</b>	<b>\$1,057,030,502.15</b>

### Inflation Rate

Various inflation rates were considered for the purposes of inflating the 2013 tax base to reflect 2017 income. Ultimately, a conservative inflation rate of 1.5% was selected to most closely approximate the Governor's projection; higher inflation rates would have yielded more revenue than the estimates shown in the Governor's scenarios. In the absence of access to the model that the Administration used to estimate revenue for 2017, we replicated the Governor's curve based on the data points provided in his proposal: a tax that starts at 2.5% at 138% FPL and flattens out at 9.5% at 400% FPL, with a cap at a contribution of \$27,500. Using our methodology, the revenue estimate for this curve is \$1,038,687,998 in 2013. Since we used in-state AGI to generate this revenue estimate, and we know that the Governor's proposal includes commuters, we expanded this number (in state revenue accounts only for 88% of the total revenue generated in the Governor's model) to \$1,180,327,270. This figure, inflated by 1.5% each year between 2013 and 2017 is \$1,252,756,343, which brings us close to the Governor's revenue estimate. Therefore, we inflated our revenue estimate of \$1,057,030,502 by the same 1.5% annually to reach our Total Revenue Generated: **\$1,121,893,647**, in effect replicating any income base impacts present in the Governor's model that we could not otherwise account for.

## APPENDIX C: PAYROLL TAX METHODOLOGY

Our payroll tax model is based on three data sets: the Covered Employment and Wages table and the Size of Establishment by Industry table, both produced by the Quarterly Census of Employment and Wages (QCEW), available from the Vermont Department of Labor<sup>70</sup>; and Occupational Employment Statistics Research Estimates for wage distribution by industry, available for Vermont from the Bureau of Labor Statistics<sup>71</sup>. All data sets use the North American Industry Classification System (NAICS) to group industries. We used 2013 data, the most recent year with complete datasets.

After merging those datasets, we modeled wage ratios for eight different industries to approximate wage ratios at company level. We used the mean wages within the bottom 10<sup>th</sup>, 25<sup>th</sup>, 50<sup>th</sup>, 75<sup>th</sup> and 90<sup>th</sup> percentiles to extrapolate the wages of the top one percentile, fitting a third order polynomial to those percentiles to replicate the expected wage distribution up to the top 1% of wage earners. We restrained the polynomial at the bottom end to avoid dropping below minimum wage. We obtained wage ratios for these eight industries ranging from 3.98 (in construction) to 5.68 (in retail).

We assigned pre-determined wage ratios to another 10 industries, at levels that reflected our assumption that industry-wide wage ratios are likely to be higher than company-level ratios (because they include the lowest earners and the highest earners across the whole industry as opposed to within a given company). One remaining industry and state and local government were assigned the average ratio of 4.87. Government data proved challenging to integrate; first, because it is not differentiated into size categories; and second, because the education sector is reported within an industry category, rather than, as in the Governor's report, as the "municipal government" sector. This may have led to underestimating the tax obligation of the public education sector, and to overestimating the tax rate of other government employers. We did not allocate any tax obligation to the federal government.

Keeping within the parameters of our data sources, the tax base we use to project revenue is smaller than our preferred tax base. The data includes only establishments subject to the Vermont Unemployment Compensation Law, whereas our preference would be to include every employer subject to withholding tax, which would generate additional revenue.

Unlike the Governor's model, we do not cap the tax for wages in excess of \$200,000k, but we do cap the overall tax rate at 20%. To trend 2013 payroll data forward to 2017, we applied the same 2.48% payroll inflation rate used by the Administration.

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<sup>70</sup> <http://www.vtmi.info/indnaics.htm#industry>

<sup>71</sup> [http://www.bls.gov/oes/2012/may/oes\\_research\\_estimates\\_2012.htm](http://www.bls.gov/oes/2012/may/oes_research_estimates_2012.htm)