The Excise-Tax on High Cost Health Plans

Paul Fronstin, Ph.D.
Director, Health Research and Education Program
Employee Benefit Research Institute
Washington, DC

Copyright© - Employee Benefit Research Institute Education and Research Fund, 1978-2015. All rights reserved.

The information contained herein is not to be construed as an attempt to provide legal, accounting, actuarial, or other such professional advice. Permission to copy or print a personal use copy of this material is hereby granted and brief quotations for the purposes of news reporting and education are permitted. Otherwise, no part of this material may be used or reproduced without permission in writing from EBRI- Erf.
Excise Tax on High Cost Health Plans: “Cadillac Tax”

- Beginning in 2018, nondeductible 40% excise tax on the total cost (employer & employee shares) of coverage exceeding $10,200 (employee-only coverage) or $27,500 (family)
- Higher thresholds of $1,650/$3,450 for early retirees & high risk professions
- Adjustments for age & gender of workers
- Aggregate value includes employer and worker contributions to FSAs, HRAs, and HSAs
- Cost or pre- and post-65 retirees may be combined
- IRS released previews (Notices 2015-16 & 2015-52) of possible regulations, but regs not yet released, so questions remain on how adjustments will be determined
Goal of the Tax

• To mitigate against the rising cost of health care
• To generate tax revenue to pay for other provisions in the ACA
Goal of the Tax

- To mitigate against the rising cost of health care
  - Employers are expected to reduce comprehensiveness of health benefit
  - Should lead to a reduction in use of health care services and health insurance premiums

- To generate tax revenue to pay for other provisions in the ACA
  - JCT estimates $91 billion in tax revenue between 2016 and 2025
  - 25% of revenue from excise tax receipts
  - 75% of revenue from higher worker (taxable) wages
What Did We Learn from IRS Notices?

- Cost of coverage calculated separately for employee-only coverage and other-than-self-only coverage
  - Implication: Employers have incentive to drop spousal coverage

- Coverage for on-site medical clinics must be included (unless providing only de minimis care)
  - Implication: Less incentive to provide such a benefit.

- Employee contributions to HSAs made through pre-tax payroll deduction included. Employee contributions to HSAs made outside of payroll are not counted.
  - Implication: Employers have less incentive to allow pre-tax employee contributions to HSAs through payroll. Employers may allow post-tax employee contributions through payroll.
Why Use a Cadillac Tax?

• Assumption that workers over-insure because they prefer non-taxable health coverage to taxable wages
• Workers over-insure because premiums are not included in taxable income, whereas out-of-pocket spending on health care services is not 100% tax deductible
• Over-insurance leads to higher use of health care services, which drives up premiums and makes coverage less affordable
• Cadillac tax expected to:
  • Reduce comprehensiveness of health benefits
  • Reduce use of health care services
  • Reduce health care costs and premiums
  • Increase worker wages
  • Overall decline in demand for health care services reduces price of health care outside group market
Implications of Higher Cost Sharing

RAND Health Insurance Experiment
- Cost sharing is a blunt instrument
- Both inappropriate/ineffective and appropriate/effective use of health care services were affected.
- Inconsistent findings related to health status, but few adverse health effects

CDHP research
- Reduced use of certain health care services…
  - outpatient visits and prescription drug fills
  - recommended cancer screenings
  - medication adherence among people with hypertension, high cholesterol, and diabetes
- Increase in emergency department visits
Issues Related to the Wage-Benefit Trade-Off

- There is evidence for and against the trade-off
- Research focuses on impact of rising health costs on worker wages
- One study on impact of decreasing health costs on worker wages
- Economic environment matters when it comes to enabling or precluding trade-off
- Strength of economy and unemployment rates matter
- Even if worker wages do not increase, tax revenue will likely materialize to pay for other parts of ACA
  - For example, corporate profits are taxable
Prospects for Repeal

- Rep. Guinta (R-NH) introduced legislation in Feb. 2015 with 28 Republican co-sponsors. Currently has 110 co-sponsors.
- Rep. Joe Courtney (D-CT) introduced similar legislation in May, with 71 co-sponsors, inc. 3 Republicans.
- Sen. Heller (D-NV) has introduced legislation with 17 co-sponsors.
- Presidential candidate Hillary Clinton has voiced support for repeal.
- Speaker of the House Ryan (R-WI) introduced legislation for repeal, which passed on Oct. 23.
- Sen. Reid (D-NV) & Rep. Pelosi (D-CA) working since spring 2015 to repeal the tax
Repeal Hurdles

• $91 billion in tax revenue
• Congress might pay for repeal with some other form of limitation on the tax preference
• Repeal legislation could be loaded up with other provisions, which might not enjoy bi-partisan support
• President Obama may veto any repeal legislation
• “Doc-fix” could have been a vehicle, but there was no agreement on what appeared to be low hanging fruit (ie full-time worker definition & tax on medical devices)
• Repeal in 2019??