



## Health Care Reform: What Does It Cost and Who Pays?

### Introduction

Health care reform legislation will carry a huge price tag – around \$940 billion over ten years – but it will reduce the federal deficit by \$132 billion, according to the Congressional Budget Office (CBO).

On an annual basis, though, what will it cost, who will pay, and who will save? This paper looks at the law when fully implemented, and attempts to answer that question.

### How Health Reform Will Change Coverage

Because most of the new coverage provisions and insurance exchanges don't begin until 2014, CBO projects that it will be 2016 before coverage changes dramatically. The result is a change in coverage for the non-elderly population as follows:

	Number of People Insured		
	2010	2016	Increase/(Decrease)
Medicaid and CHIP	35 million	52 million	17 million
Employer-provided insurance	162 million	159 million	(3 million)
Individual and Other Insurance	29 million	24 million	(5 million)
Exchange-purchased insurance	none	21 million	21 million

As a result, the number of uninsured people will decrease between 2010 and 2016 by 30 million, from 52 million to 22 million.

### What will this cost?

While these costs will phase-in over the next decade, by 2019 the coverage provisions in health reform will result in an annual cost of \$217 billion, in three categories:

Medicaid and CHIP	\$98 billion
Consumer Insurance Subsidies	\$115 billion
Small Employer Tax Credits	\$4 billion

Medicaid and CHIP costs are direct payments to be made by state governments on behalf of low income people (in 2019 the Federal Government will be reimbursing 90% of these new costs). Consumer insurance subsidies will be provided as Federal tax reductions for taxpayers with household income up to 400% of poverty who buy health insurance. Small employer tax credits will be provided to “mom and pop” businesses that offer insurance to employees. These will generally benefit employers with 25 or fewer employees who provide insurance and whose average salary is less than \$50,000.

### Significant New Taxes and Major Spending Decreases in the Reform Law

The Federal Government provided for nearly \$230 billion of revenue as of 2019 to cover the \$217 billion in costs, resulting in a net deficit reduction in 2019 of \$12 billion (which is a portion

of the total deficit reduction over the next ten years combined of \$132 billion). Approximately half of these dollars will come from new taxes and fees, and the other half from spending cuts.

### ***New Taxes and Fees on Individuals and Businesses***

New taxes and fees will add up to \$109 million, or around half of what is needed to pay for the reforms. Of these, four of the most important account for \$35 million. They are:

- Penalty payments by uninsured individuals who choose not to buy insurance will raise \$3 billion a year. These fines begin in 2014 and 2015, and in 2016 and thereafter will be 2.5% of income (e.g., \$1,083 for an individual making \$43,320).
- Penalty payments by businesses will raise \$10 billion a year. These will be paid by employers with more than 50 employees who choose not to provide health insurance to employees and instead pay a fine of \$2000 per worker each year if any worker receives federal subsidies to purchase health insurance.
- Starting in 2018, there will be a 40% excise tax on high premium insurance plans (over \$27,500 for families and \$10,200 for individuals), which will raise \$20 billion in 2019.

Some other provisions related to individuals that will generate significant additional revenue include:

- An increased Medicare tax of 0.9% and a new Medicare tax of 3.8% on both earned and unearned income for people earning above \$200,000 (individuals) and \$250,000 (families), beginning in 2013.
- A new 10% excise tax on indoor tanning services, which goes into effect in 2010.
- Raising the percentage after which people can deduct medical expenses from their taxes from 7.5% to 10% of Adjusted Gross Income (this will take effect for non-elders in 2013, and for elders in 2016).
- Limiting health flexible spending arrangements in cafeteria plans to \$2,500, beginning in 2013.

Some other provisions related to corporations that will generate significant additional revenue include:

- Imposing an annual fee on health insurance providers that will raise \$14.3 billion in 2018 when fully implemented. (This begins in 2014.)
- Imposing an annual fee on importers and manufacturers of branded drugs that will eventually settle in at almost \$3 billion annually by 2019. (This begins in 2011.)
- Imposing a 2.3% excise tax on manufacturers and importers of some medical devices. (This begins in 2013.)

### ***Non-Coverage Provisions Generally Reduce Spending***

Most of the remaining dollars needed for health reform will come from cuts in Federal spending for health care that will add up to over \$118 billion in 2019. Among the most significant are:

- Revisions to Medicare market basket updates, which will result in over \$40 billion of annual savings by 2019. “Market baskets” are projections of future Medicare payments based on both the cost and configuration of services in a current year and how these are expected to change over time. Savings to Medicare means that payments to hospitals and other providers will be reduced, either because it is believed that costs will go down for some procedures, or less expensive procedures and services will be substituted for them, or a combination of both.
- Reductions in Medicare Advantage payments of over \$26 billion per year as of 2019. These are payments made to insurance companies, not individuals. The companies will also be required to pay out at least 85 cents in benefits for every dollar in premiums taken in.
- Payment adjustments to home health care providers, which will result in \$5 billion in savings by 2016 growing to over \$10 billion by 2019.
- Reductions in Medicaid prescription drug payments to drug companies of \$5 billion or more as of 2017.
- Reductions of \$5 billion each in both Medicare and Medicaid “Disproportionate Share Hospital” payments as of 2018. These will be borne by hospitals that have traditionally had high volumes of lower-income patients. The Federal Government expects that as more people are insured, there will be less need for these payments.
- An adjustment to the calculation of Medicare Part B premiums, which will result in almost \$5 billion of annual savings by 2019.
- Reducing the Medicare Part D premium subsidy for higher income individuals that will result in savings of more than \$2 billion by 2019.
- Readmission rate reductions for hospitals of \$1 billion or more as of 2015. This is intended to penalize hospitals that discharge people early who then need to be re-admitted.

### **Which Households Benefit from Reform? Lower and Lower-to-Middle Income**

In light of this list of new taxes, other revenues, and spending cuts, who will benefit? Because nearly all of these spending cuts and most of the new taxes will impact businesses, some individuals and households will benefit the most.

First, households making up to \$29,327 for a family of four, or up to 133% of poverty, will save all of their insurance costs because they will be covered by Medicaid and/or CHIP, with free coverage of children likely continuing to extend to 200% of poverty or more.

Second, households making up to 400% of poverty (\$43,320 for an individual, \$88,200 for a family of four in 2010) will also save, because their health insurance premiums will be subsidized by the government, usually significantly. In 2016, the average Exchange subsidy is estimated by the CBO to be \$5,300. Here are two examples of how the subsidy will be calculated:

- Families of four earning \$88,200 (400% of poverty) will have their insurance premium capped at \$8,379 annually, or 9.5% of income. If their plan costs \$1,115 per month, or \$13,375 per year, then their subsidy will be \$4,996.

- An individual earning \$21,660 (200% of poverty) will have his or her insurance premium capped at \$1,365, or 6.3% of income. If the plan costs \$402 per month or \$4,824 per year, then his or her subsidy will be \$3,459.

Third, Medicare Gap coverage will benefit people in the Medicare Part D Donut Hole, and while the initial payment in 2010 will be up to \$250 for those in the Donut Hole, the total coverage subsidy will grow to \$1,300 or more for Medicare recipients with high drug costs in 2019.

### **Which Households Pay More for Reform? Upper Income With Cadillac Plans**

Even with a lower cost plan, households in the upper income range –above \$200,000 for an individual and \$250,000 for a family, will pay more because they will pay a higher Medicare tax on earned income and a new Medicare tax on unearned income. How much more they pay depends on how much unearned income they have – those with more will pay a greater amount of new taxes because they already pay a tax on earned income.

Starting in 2018, the Cadillac health plan excise tax could also increase insurance costs for a segment of the population that cuts across income levels and enjoys comprehensive health coverage, but because that tax is delayed for eight years, it is hard to predict just how many plans and people will be affected by it at that time.

All households, regardless of income, that refuse to buy insurance will also pay, because they will be subjected to a new 2.5% penalty tax on income.

### **Which Households Neither Gain Nor Lose from Reform? The Insured Middle**

Households in the middle and upper middle income brackets which, depending on family size, begin in the \$50,000 to \$100,000 range and continue up to the \$200,000 to \$250,000 range will neither gain nor lose unless they have a high-cost plan.

### **Conclusion**

Because the federal deficit is not projected to increase as a result of tax reform, by itself reform requires no new general income tax increases in addition to the provisions that are in the law. However, certain tax increases that are built into the law will affect wealthier households more than others, and reductions in payments to health care providers that are built into the bill could be passed along to individual consumers in the form of higher fees for health services and higher insurance premiums (though there are some protections built into the law to prevent this). The subsidies being offered to people at lower and middle income levels will result in a lowering of their cost of insurance, and the closing of the Medicare Donut Hole will lower out-of-pocket drug costs for many recipients of Medicare.

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