Testimony of the Hon. Tevi D. Troy, Ph.D.

House Committee on the Education and the Workforce
Subcommittee on Health, Employment, Labor, and Pensions

Hearing on

"Five Years of Broken Promises:
How the President's Health Care Law is Affecting America's Workplaces"

Tuesday, April 14, 2015

Mr. Chairman, Mr. Ranking Member, Members of the Committee,

My name is Tevi Troy, and I am the President of the American Health Policy Institute, adjunct fellow at Hudson Institute, and a former Deputy Secretary of the U.S. Department of Health and Human Services, as well as a former senior White House Domestic Policy Aide. The American Health Policy Institute is a 501(c)3 think tank dedicated to studying the issue of employer sponsored health insurance and highlighting the challenges employers face in offering care to their employees and their dependents. In addition to publishing a variety of studies on employer sponsored health insurance, the Institute also examines employer responses to these challenges and shares best practices from the most successful of these responses. These roles give the Institute a unique perspective on developments in employer sponsored health insurance, and enable it to make recommendations to both policymakers and business leaders regarding the future state of health care.

Today, I'd like to talk about the impact the Affordable Care Act's (ACA) high-cost excise tax is having on employer-sponsored health care, the cost of the ACA to employers, and the affordability of health care to employees. These three factors combined mean that there are likely big changes ahead in employer sponsored care, which is currently how 169 million Americans get their health coverage.

The ACA Cadillac Tax

Under the ACA, an excise tax on high-cost health plans, the so-called "Cadillac tax," takes effect in 2018. The potential impact of this tax is already driving employers to reassess their health care plans and reconsider their future role and approach in providing health care benefits. At the moment, the tax is forcing employers to reduce health care benefits to reduce their exposure to the tax. In the future, however, continued medical inflation and other factors beyond the control of employers and employees will make it very difficult for employers to avoid the tax.[1] Rising health care costs will make it more difficult for employers to provide affordable health care benefits to employees with each passing year, and the inexorable increases in health care costs will eventually cause Chevrolet benefit plans to be taxed as Cadillacs. That, in turn, will result in the burden of the excise tax falling on a significant number of American employees and their families.

Last November, the American Health Policy Institute published a study on "The Impact of the Health Care Excise Tax on U.S. Employees and Employers," which found:[2]

- From 2018 to 2024, the excise tax could cost 12.1 million employees an average of $1,050 in higher payroll and income taxes per year, *if* employers increase their taxable wages as they reduce the cost of health care benefits. Alternatively, these employees could see up to a $6,150 reduction in their health care benefits and little or no increase in their pay.

- Should employers increase the taxable wages of employees, something that is not clear in the current business cycle, a significant portion of the increase in take-home pay may be spent on higher out-of-pocket health care expenses as deductibles and out-of-pocket limits increase.

- Large employers subject to the excise tax in 2018 will pay an average of $1.0 million that year, and an average of $2.1 million per year from 2018 to 2024, *or over $2,700 per employee.*

- In 2018, the excise tax is anticipated to hit 17 percent of all American businesses, and 38 percent of large employers.

- Within twenty years, the impact of the excise tax will not be limited to just high value plans. By 2031, the cost of the average family health care plan is expected to hit the excise tax threshold.

Currently, the Congressional Budget Office (CBO) estimates the excise tax will result in approximately $3 billion in new taxes in 2018, $6 billion in 2019, $7 billion in 2020, and a total of $87 billion from 2018 to 2025.[3] According to previous CBO estimates, about 25 percent of the $87 billion, or about $22 billion, will come directly from employers, third party administrators (TPAs), and issuers.[4] The remaining 75 percent, or $65 billion from 2018 to 2025, will come from increased income and payroll tax revenue from the higher taxable wages employers are predicted to pay to offset the reduction in the health care benefits that is expected to occur because of the excise tax. As these numbers show, this tax is going to impose real costs on both employees and employers alike.

In January and February 2014, the American Health Policy Institute confidentially surveyed over 350 large companies that are members of the HR Policy Association to identify and quantify the direct costs of the ACA on large employers. Over 38 percent said they would be impacted by the excise tax in 2018 unless they made changes to their plan designs before then. Another recent analysis of large employer plans found 33 percent are likely to trigger the excise tax in 2018 and 58 percent would by 2022.

Many state and local government health care plans will also be impacted by the high-cost excise tax because they tend to offer more expensive health plans than private-sector employers. According to the Bureau of Labor Statistics, the cost of health insurance for state and local governments is more than two times the cost for private-sector employers ($5.05 per hour vs. $2.35 per hour), which suggests they are more than twice as likely to be impacted the high-cost excise tax. Unless public-sector health care benefits can be reduced to avoid the excise tax, state and local officials will either have to raise taxes or cut other services to pay the tax.

The excise tax is also expected to significantly impact the high-cost health care plans labor unions have bargained for over the years. Although nonunion employers may have the flexibility to adjust their health care benefits anytime between now and 2018, unionized employers will need to address potential excise tax costs in their upcoming contract negotiations to ensure contractual changes are in place to avoid or minimized the excise tax in the future.

As employers reduce the cost of their health care plans to avoid or minimize their exposure to the excise tax, employees are likely to have to pick up more of their health care costs out of their own pockets and find ways to reduce their own health care expenses. Although employers will continue to pick up the large majority of employee health care costs (71% of the premium for family coverage, or $12,011), employee deductibles, copayments, and out-of-pocket maximums will increase.

Excise tax costs in the range of $7 million to $78 million per large employer will not be overlooked by CEOs, CFOs, or Boards of Directors, especially when it is a non-deductable expense. In a recent survey, two-thirds of Chief Financial Officers said they are somewhat or very concerned they will trigger the excise tax based on their current plan designs and projected cost increases. More than four in ten (43 percent) said avoiding the tax is the top priority for their health care strategies in 2015.

The ACA's high-cost excise tax was intended to change employer health care plans and it is having its anticipated effect. Over time the only way for an employer to avoid the excise tax is to take steps to reduce the rate of increase in the company's health care costs to less than the increase in consumer prices and keep it there; and/or to modify the health care benefits the company offers to stay under the excise tax threshold. While 83 percent of large employers consider health benefits to be an important part of their employee attraction and retention strategy, at least 78 percent are changing their health care plans in response to the high-cost excise tax. According to a recent survey by the National Business Group on Health:

- 57 percent of employers are implementing or expanding account-based consumer driven health plans to minimize the impact of the excise tax;
- 53 percent are adding or expanding incentives for employees to participate in wellness programs;
- 42 percent are increasing employee cost sharing; and
- 30 percent are eliminating high cost plans.

Policymakers should recognize the cost of employer-provided care is increasing for a variety of reasons beyond the control of employers and employees, including the aging workforce, new medical technologies and drug therapies; and new mandates, taxes, fees and compliance burdens imposed by the ACA. The threat of the excise tax is driving employers to fundamentally reassess their plans in ways that will have a real impact on employees and their families. To avoid the inevitability of Chevrolet benefit plans eventually being taxed as Cadillacs, and to remove the potential negative impact that will have on employer sponsored health benefits, Congress should repeal the excise tax sooner rather than later.

The Marginal Cost of the ACA on Employer-Sponsored Health Care

Last year, an Institute study looked at direct costs to companies from the ACA's requirements, over and above projected employer health care cost trends without the ACA.[5] The study found that over the next decade:

- The cost of the ACA to large U.S. employers (10,000 or more employees) is estimated to be between *$4,800 to $5,900 per employee*;
- These large employers will see overall ACA- related cost hikes of between *$163 million and $200 million per employer, or an increase of 4.3 percent in 2016 and 8.4 percent in 2023 over and above what they would otherwise be spending; and*
- The total cost of the ACA to all large U.S. employers over the next ten years is estimated to be from *$151 billion to $186 billion*.

These cost hikes, combined with the fear of triggering the excise tax, are accelerating employer movement towards alternative models of health care delivery. Many have experimented with wellness programs, high deductible plans, and alternative forms of cost-sharing. These employer steps in reaction to the ACA will have a significant impact on the recipients if employer based care, namely employees, retirees and their dependents.

The Affordability of Employer Sponsored Plans

Under the ACA, large employers must offer affordable health care coverage to full-time employees. Coverage is deemed to be not "affordable" according to the ACA if the employee's share of the annual premium for self-only coverage is greater than 9.5 percent of their annual household income. An employer plan must cover at least 60 percent of total allowed costs to meet the ACA's minimum value requirement, and offer "substantial" coverage for in-patient hospitalization services or physician services (or both). Employer plans are also required to offer certain preventive care services on a no-cost basis to participants, and a range of additional benefits, such as the age-26 adult dependent coverage requirement and no annual or lifetime limits on essential health benefits.

The average employee share of the premium for employer sponsored family coverage cost less than 9.5 percent of family income for 82.8 percent adult-nonelderly private-sector employees with families (22.6 million).[6] However, the average employee premium for family coverage accounted for more than 9.5 percent of family income for 4.7 million employees (17.2 percent). Further, 10.4 million employees with families, or 38.1 percent, faced an average family premium *and* deductable that could consume 9.5 percent or more of their family income. Moreover, projections by the American Health Policy Institute show that by 2025, that 38 percent becomes 53 percent, creating a big problem for employers and employees alike.

The Affordability of ACA Public Exchange Plans

As employer sponsored plans become less affordable, it is not at all clear that the ACA exchanges can solve the affordability problem, either. In 2013, there were 137.4 million

nonelderly adult Americans with incomes above the federal poverty level that could potentially find the average cost of health insurance in the ACA public exchanges unaffordable depending on their income level. Although nearly all of these adults would find the average ACA premium for a silver plan costs less than 9.5 percent of their individual income, 105.5 million people, or 76.8 percent, face an average ACA premium *and* deductable that could consume more than 9.5 percent of their individual income.[7] The large number of people is due to the fact that the average deductible for an ACA silver plan was $3,030 for individuals with incomes above $28,725. Compared to the average employer plan, some of the most popular health care plans sold on the ACA's public exchanges have significantly higher deductibles and out-of-pocket expenses.

For the 20.2 million nonelderly adult Americans *with no health insurance* who might seek coverage on the public exchanges:

- 11.5 million (56.9 percent) faced an average ACA premium *and* deductable that could consume more than 9.5 percent of their individual income–for 7.4 million (36.6 percent), the average ACA premium *and* deductable could consume 15.5 percent or more of their individual income.

- 9.4 million (46.5 percent) of the 20.2 million nonelderly adult Americans with no health insurance would find the average employer sponsored coverage affordable and the average ACA plan unaffordable, while 8.8 million (43.6 percent) would the average ACA plan affordable and the average employer sponsored coverage unaffordable; 2.0 million would find both types of coverage unaffordable.

Although survey results suggest there is an affordability gap for middle income Americans purchasing coverage on the ACA exchanges, these results, which look at the combined affordability of the average ACA exchange premium and deductible after all the subsidies are taken into account, suggests affordability will be an issue for over three quarters of exchange participants.

We are facing a troubling cycle in the world of employer sponsored care. The combination of a creeping excise tax affecting more and more plans over time and the high marginal costs of the ACA to employers is driving employers to look at significant changes to their health care offerings. Some employers will exit the system, but we believe that more will look to make serious changes in approach. These employer based changes typically include more cost-sharing components as employers seek to avoid triggering the excise tax when it comes on line in 2018. The cost sharing then impacts the affordability of health care for employees, who will become unsatisfied with their employer sponsored care and look to Washington for answers.

Mr. Chairman, Mr. Ranking Member, Members of the Committee, I thank you for your time here today, and I look forward to any questions you may have.

[1] Robert H. Dobson and Stuart D. Rachlin, What does the ACA excise tax on high-cost plans actually tax?, Milliman, December 9, 2014.

[2] Tevi D. Troy and D. Mark Wilson, "The Impact of the Health Care Excise Tax on U.S. Employees and Employers," American Health Policy Institute, November 2014. Unless otherwise noted, the following data for this section of the testimony comes from this report.

[3] Congressional Budget Office, Insurance Coverage Provisions of the Affordable Care Act - CBO's March 2015 Baseline, Table 1, March 9, 2015.

[4] Congressional Budget Office, The Budget and Economic Outlook: 2015 to 2025, January 2015, pg. 124.

[5] Tevi D. Troy and D. Mark Wilson, "The Cost of the Affordable Care Act to Large Employers," American Health Policy Institute, April 2014. Unless otherwise noted, the following data for this section of the testimony comes from this report.

[6] Tevi D. Troy and D. Mark Wilson, "The Affordability of Employer Sponsored Care and the ACA Exchange Health Care Plans," American Health Policy Institute, February 2015. Unless otherwise noted, the following data for this section of the testimony comes from this report.

[7] *Id.*