# Overview of the Cadillac Tax

Adam Solander, Member of the Firm
Epstein Becker Green
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# Cadillac Tax / Law of Unintended Consequences

- Revenue
  - As one of the Affordable Care Act's principal "pay-fors," the Cadillac tax was initially expected to raise $137 Billion in the first 10 years.
  - After examining recent cost trends in employer-sponsored health benefits, that estimate was revised, and now CBO expects the Cadillac tax will generate about $80 billion over the next 10 years
  - True cost next will reveal itself in the next 20 years

# Cadillac Tax / Law of Unintended Consequences

- Purpose/Debate
  - Health economists for some time have argued that rich benefit structures create price insensitivity in consumers who demand more and more expensive services
    - Consumers, plans, and providers need "skin" in the game for reform to work. Does the Cadillac tax achieve this?
- Opposition arguments: public exchange time bomb, employer ante at health reform table.

# Cadillac Tax / The Reality

- The Cadillac tax will affect fairly modest plans
- Depending upon source roughly half of employers will hit thresholds in 2018.
  - Much higher numbers in the next 10 years
  - State governments, unions, employers all subject to tax
- Takeaway: Plans can only reduce richness to a point.
  - Long term avoidance requires more than benefit buy downs.
- Takeaway: Because much of the Cadillac tax is statutory, legislation is likely needed to fix big ticket items.
  - Recent subregulatory guidance will allow employer feedback before regulations are issued similar to mandate
    - Beyond statute interpretation unlikely given recent case

# Cadillac Tax / The Basics

- Beginning in 2018, employer-sponsored plans will be subject to a 40 percent non-deductible excise tax on the dollar amount of coverage that exceeds certain specified thresholds.
  - Was originally slated to take effect in 2013 and original thresholds just indexed to 2018 dollars.
  - Why 2018…
- 2018 threshold for individual coverage is $10,200 and the threshold for family coverage is $27,500.
  - Adjusted by “health cost adjustment percentage”
  - Adjusted upwards for early retirees and individuals in high-risk professions
  - Indexed for inflation

# Cadillac Tax / How Does It Work?

- The Cadillac tax applies to the dollar amount that exceeds the specified threshold using the following formula:
  - "The aggregate cost of the applicable employer sponsored coverage of the employee for the month, over
  - An amount equal to 1/12 of the annual limitation for the calendar year in which the month occurs."

- Example: If an employer offered individual coverage that cost $12,000 per employee, the excess amount for a month would be calculated by ($12,000 / 12 months) − ($10,200 / 12) = $150. Therefore, the employer would be taxed 40 percent of $150, or $60 per employee per month. Over a year, the Cadillac tax liability per employee would be $720.

# Cadillac Tax / Thresholds: Health Cost Adjustment

- Thresholds Increased in 2018 for Health Cost Adjustment Percentage
- The health cost adjustment percentage is designed to increase the thresholds in the event that the actual growth in the cost of U.S. health care between 2010 and 2018 exceeds the projected growth for that period.
  - The health cost adjustment percentage is equal to 100 percent plus the excess (if any) of:
    - the percentage by which the per employee cost for providing coverage under the Blue Cross/Blue Shield standard benefit option under FEHBP for plan year 2018 (determined by using the benefit package for such coverage in 2010) exceeds such cost for plan year 2010;
    - over 55 percent.
- Example: If the cost of standard FEHBP coverage increases by 60 percent from 2010 to 2018, then the health cost adjustment percentage would be (60 percent − 55 percent) + 100 percent = 105 percent.

# Cadillac Tax / Thresholds:  Age and Gender Adjustment

- Thresholds increased for any taxable period by the Age and Gender Adjustment

- Is an amount equal to the excess (if any) of—
  - the premium cost of the Blue Cross/Blue Shield standard benefit option under the FEHBP Plan for the type of coverage provided such individual in such taxable period if priced for the age and gender characteristics of all employees of the individual's employer, over
  - the premium cost for the provision of such coverage under such option in such taxable period if priced for the age and gender characteristics of the national workforce.

- Example: If the cost of standard FEHBP coverage for the age and gender characteristics of the employer's workforce is $11,500 and the cost of standard FEHBP coverage for the age and gender characteristics of the national workforce is $10,500, then the age and gender adjustment would be $11,500 − $10,500 = $1,000.

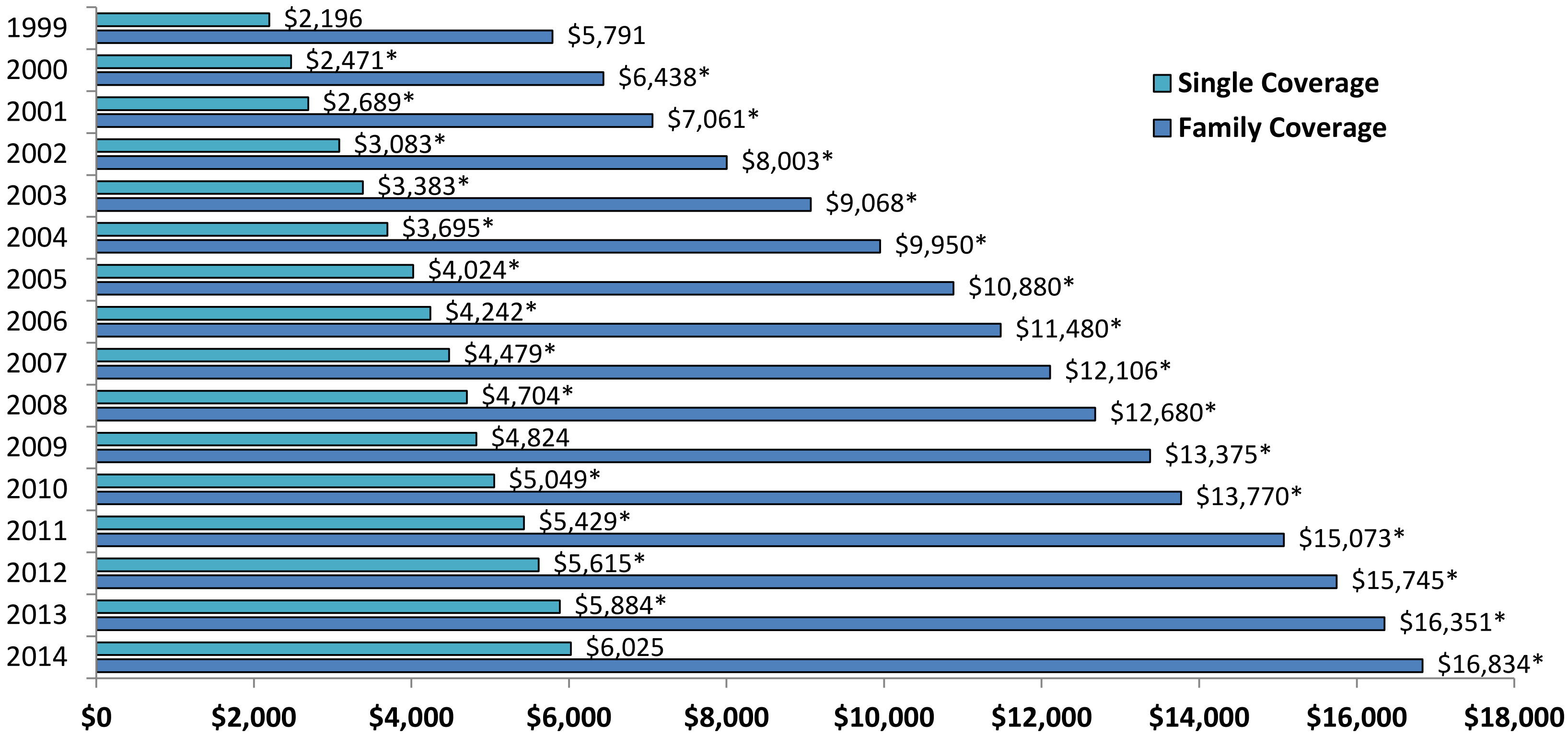
# Cadillac Tax / Thresholds: Retirees and High Risk Professions

- The thresholds are increased for individual qualified retirees or those who participate in a plan sponsored by an employer the majority of whose employees covered by the plan are engaged in a high-risk profession.
- Qualified Retirees: individuals over 55 who are not Medicare eligible and receiving employer- sponsored retiree health coverage.
  - High Risk Professions: Line workers; Law enforcement officers ; Fire protection personnel; Individuals who provide out-of-hospital emergency medical care (including EMTs, paramedics, and first-responders) ;Longshoremen; Construction, mining, agriculture (not including food processing), forestry, and fishing personnel; retirees with 20 years in these industries.
- In 2018 thresholds for Individual Coverage increased $1,650
- In 2018 threshold for Family Coverage increased $ 3,450

# Cadillac Tax / Thresholds: Indexing

- In 2019, thresholds are indexed for CPI–U, plus one percentage point, rounded to the nearest $50.
- Beginning in 2020, the threshold amounts are indexed to the CPI–U, rounded to the nearest $50.
- Medical inflation has historically risen faster than CPI-U
  - Holding everything constant plans will come closer to threshold by virtue of indexing
  - Holding everything constant if subject to the tax the amount will grow each year

# Average Annual Premiums for Single and Family Coverage 1999-2014




* Estimate is statistically different from estimate for the previous year shown (p<.05).

SOURCE: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2014.

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# Cadillac Tax / To Whom Does the Cadillac Tax Apply

- The ACA states that each “coverage provider” is responsible for payment of the tax.
  - In the context of insured group health plans, the coverage provider is the health insurance issuer.
  - For self-insured plans, the entity that administers the plan is the covered provider responsible for payment of the tax.
    - Regulations identify the plan sponsor
  - HSA contributions the coverage provider is the employer
  - Other coverage, the administrator
- While the penalties may technically apply to the health insurance issuer, the cost of the penalties will be passed down to the employer.

# Cadillac Tax / What Benefits are Included?

- The Cadillac Tax applies to "applicable employer-sponsored coverage."
- Applicable employer-sponsored coverage includes coverage under any group health plan made available to the employee by an employer which is excludable from the employee's gross income or would be excludable if it were employer-provided coverage.
  - Major medical coverage and coverage provided under account-based plans (e.g., FSAs and HSAs) are likely includable in the calculations.
  - Wellness likely includable if not excepted benefits
  - Coverage for long-term care, stand-alone vision and dental, and non-coordinated benefits (e.g., hospital indemnity) are exempt.
- Coverage treated as applicable employer- sponsored coverage without regard to whether the employer or employee pays for the coverage.

# Cadillac Tax / What Benefits are Included?

Account Based Plans:

- FSAs: Includes the employee's salary reduction and any employer contribution
- HSAs: Includes the employer contribution
  - Proposal to include employee pretax contributions as well
- HRA: Includes full amount of coverage purchased through an HRA
- Onsite Clinics: Unclear how cost is calculated

Other Benefits:

- Wellness and Telehealth: TBD and dependent upon structure

# Cadillac Tax / How is Cost Calculated

- The ACA says that the cost of coverage will be determined under rules similar to the rules used for calculating cost of coverage under COBRA.
  - The subregulatory guidance provides detailed methodologies for determining cost using COBRA rules
  - Proposal to allow for geographic differences

# Cadillac Tax / Employer Response

- A fight for our life:
  - Given the indexing issue if thresholds are hit it is unlikely that the most plans will continue to offer coverage.
    - Hard to justify increasing non-deductible business expenses that do not provide additional benefit to employees.
- At this point mostly compliance focused. Evaluation of plans starting.
- Reducing benefit richness
  - State benefit mandates
  - Recruitment and retention issues
  - Cadillac tax avoiding plans
    - More migration to HDHPs
    - Likely that only one benefit option will be offered
    - Lowest common denominator with stand-alone add on

# Cadillac Tax / Employer Response

- Value Based Purchasing/ Population Health Management
  - In its infancy for employers.
    - Most programs only include provider incentives
  - Takes time to bend the cost curve
  - Need market share to negotiate
- Provider Innovation
  - Looking to telehealth, and other non-traditional settings.

# Cadillac Tax / Congress to the Rescue???

- The Middle Class Health Benefits Tax Repeal Act
  - Would repeal the Cadillac Tax
  - Introduced by Joe Courtney (108 Co-Sponsors (mostly D's))
- The Patient Choice, Affordability, Responsibility, and Empowerment Act
  - Introduced by Burr, Hatch and Upton
  - Repeals Cadillac Tax and caps <u>employee</u> exclusion for employer-provided health care at $12,000; $30,000 for family
  - Indexed at CPI + 1

# Cadillac Tax / Congress to the Rescue???

- Legislative solution
  - Must maintain system transformative qualities
  - Must account for regulatory, geographic, and demographic characteristics of plans
  - Must be fiscally responsible

# Questions /

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**Adam Solander**

Member of the Firm
Asolander@ebglaw.com
202-861-1884