Incentives in US health care bill for employers to drop coverage

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There are growing indications that many US companies will drop health care coverage for their employees as a result of the health care overhaul voted into law earlier this year. Under the Patient Protection and Affordable Care Act (PPACA), whose major provisions begin to take effect in 2014, employers may find it more profitable to eliminate health care benefits altogether.

The main incentive for dumping coverage is that the fines imposed on companies for not providing health care coverage would be more than offset by the savings from eliminating it. As health care costs continue to rise—as they are projected to do—the incentive for dropping coverage will be even greater.

When the health care bill was being debated in Congress, the Congressional Budget Office projected that about 3 million people, a relatively small number, would lose their employer-sponsored health plans as a result of the legislation. It now appears that this was a considerable underestimation, and that many employers are weighing the options of eliminating coverage for their workers.

Paul Keckley, executive director of the Deloitte Center for Health Solutions, told the Raleigh, North Carolina-based *News & Observer*, “I don’t think you are going to hear anybody publicly say, ‘We’ve made a decision to drop insurance.’ What we are hearing in our meetings is, ‘We don’t want to be the first one to drop benefits, but we would be the fast second.’ We are hearing that a lot.”

Under PPACA, beginning in 2014 people will be required to purchase health care coverage on insurance “exchanges” if they are not covered through their employer or do not qualify for Medicare, Medicaid or other government programs. The penalties imposed for not having coverage will eventually rise to as high as 2 percent of income for everyone except the most impoverished.

Many people buying coverage on these exchanges will receive federal subsidies, according to income. For example, a 45-year-old purchasing insurance for a family of four with an annual income of $90,000 would qualify for a subsidy of 40 percent of the family’s insurance costs; the same family with an income of $50,000 would get a subsidy of 76 percent of the costs.

Employers with 50 or more employees would pay a penalty of about $2,000 per worker for failure to provide health care coverage. But with health care costs averaging $9,028 per worker this year, and expected to rise sharply over the next five years, it would be far more cost-effective for employers to eliminate the coverage and force their workers to fend for themselves on the insurance exchanges.

In an October 21 opinion piece in the *Wall Street Journal*, Philip Bredesen, the Democratic Governor of Tennessee, provided an example of how this might play out in practice. In 2014, Tennessee would have about 40,000 direct employees participating in the state’s health plan. If the state dropped coverage for these employees, and compensated them for the increased costs of purchasing insurance on the exchange, the state would incur estimated costs of $114 million.

The state would also be fined approximately $86 million for not providing insurance, for a total of about $200 million in increased costs. However, if Tennessee kept its existing insurance plan for its workers, the cost would be about $346 million. The state would therefore reduce its annual costs by some $146 million by dropping coverage for its employees and shifting them onto the insurance exchange.

Bredesen adds: “Local government will find eliminating all coverage particularly attractive, as many of them are small and will thus incur minor or no penalties; many have health plans that will not meet the minimum benefit threshold, and so they’ll see a substantial and unavoidable increase in cost if they continue providing benefits under the new federal rules.”

It should be noted that under Bredesen's hypothetical scenario, Tennessee would compensate employees so that they would not suffer financially as a direct result of being dropped from coverage. In reality, employers would be under no obligation to provide such compensation.

Another provision of the health care bill projected to influence employers to either shift a greater share of health costs onto workers or drop coverage altogether is the "Cadillac tax" on higher-cost insurance plans that offer more comprehensive coverage. Beginning in 2018, plans valued over $10,200 annually for an individual or $27,500 for a family will be taxed at a 40 percent rate for the value above these limits.

A spokesman for aircraft manufacturer Boeing told the *News & Observer* that concerns over the impending tax were one of the reasons the corporation just announced a 50 percent increase in insurance deductibles for its workers. Other companies with higher-cost plans are expected to either reduce benefits, shift costs to their employees, or dump coverage outright.

Obama administration officials contend that the provisions of the health care bill will not drive employers to drop coverage in large numbers. Jason Furman, an economic adviser to the president, stated, "The absolute certainty about the Affordable Care Act is that for many, many employers who cover millions of people, it increases the incentives for them to offer coverage."

Erin Shields, a spokesman for the Senate Finance Committee, which was involved in drafting details of the legislation, commented, "It is clearly cheaper for employers to continue providing coverage." She said that employers would lose the tax deduction for workers' health care costs if they dropped coverage, and that they would likely have to pay workers more in wages to compensate for eliminating the benefits and keep them on the job.

There is no evidence to support such a claim. With the official jobless rate hovering around 10 percent nationally, companies are far more likely to cut wages and benefits than increase them. Employers are already shifting the rising costs of health care coverage onto their workforces in the form of higher premiums, deductibles and co-payments.

Beginning in 2014, people cannot be denied coverage based on preexisting conditions, and insurers cannot place a lifetime cap on benefits, but there are no real mechanisms in the health care legislation to control what the for-profit insurers can charge. This is true for coverage provided by employers and for policies offered for purchase on the insurance exchanges, which include no government-run option.

Health care costs for large companies are expected to rise by about 8.8 percent next year, up from an average of $9,028 per worker this year to $9,821 in 2011. Smaller companies can expect even bigger increases. Businesses will pass more of these costs onto employees.

In addition to raising premiums, deductibles and co-payments, some companies are increasing "user fees" for visits to doctors or the emergency room. More companies are also charging fees or penalties to cover an employee's spouse if the spouse has access to coverage through his or her employer.

Other companies are eliminating co-pays and replacing them with "co-insurance," where instead of paying a set amount of $10 or $20 for a doctor visit, the insured would be required to pay a percentage of the bill, e.g., 20 percent. Another strategy of businesses is to replace their present health care plans with high-deductible policies referred to as "consumer-driven plans." Under these plans, the potential financial liability is so high that people are discouraged from seeking treatment.

According to research by the Corporate Leadership Council, by 2016 health care costs will have risen to the point where it will make far more financial sense for companies to eliminate health care coverage for their employees than keep it. Workers in the retail industry will be particularly vulnerable, as it will be more costly for employers to comply with the requirements of the health care legislation than pay the fine.