

# ACA Repeal and Replacement

March 9, 2017

*Special Report*

## HIGHLIGHTS

- Immediate “Repeal” of Individual/Employer Mandates
- Many Other Changes Start 2018
- New Age-Based Credit
- Repeal of NII Tax
- Expanded Health Savings Accounts
- Excise Tax On High-Dollar Health Plans Delayed Until 2025
- Pre-Existing Conditions Rule Retained
- Flexible-Spending Rules Loosened

## INSIDE

Tax Provisions.....	1
Individual and Employer Mandate Penalties .....	1
Net Investment Income Tax .....	2
Additional Medicare Tax .....	2
Tax Credits .....	3
New Refundable Credit for Health Insurance Coverage.....	3
Other Provisions.....	4
Medical Expense Deduction .....	4
Health Savings Accounts.....	5

## House GOP Proposes To Eliminate Most ACA Taxes; Some Coverage/Credit Benefits Remain

House Republicans have unveiled a repeal and replacement plan for the Affordable Care Act (ACA). The GOP’s American Health Care Act (AHCA) would eliminate most of the ACA’s taxes, including the penalties connected with the individual and employer mandates, the net investment income (NII) tax and the Additional Medicare tax. Left in place, although delayed, would be the excise tax on high-dollar health plans. Also left in place, would be a number of non-tax provisions related to scope of coverage, benefits and children – including allowing dependents to continue staying on their parents’ plan until age 26, prohibiting health insurers from denying coverage or raising rates to patients based on pre-existing conditions, and forbidding lifetime limits on insurance coverage.

The House GOP plan has been rejected by Democrats. Some Republicans have said the plan does not go far enough in repealing all of the ACA. As March moves forward, a vote on the House floor is eventually expected.

***IMPACT.** Under the House GOP proposal, the ACA would not be repealed in its entirety at one instance. Republicans in Congress plan to use the budget reconciliation process to repeal and replace the ACA. The rules for reconciliation are very complex and beyond the scope of this Briefing. Because of reconciliation and other considerations, some ACA provisions would be repealed over time or delayed. The process would continue into 2020 and beyond.*

***IMPACT.** The House GOP’s American Health Care Act and the budget reconciliation process is just one avenue that Republicans intend to use to repeal and replace the ACA. Republicans also plan to roll back and/or undo ACA regulations through administrative actions, particularly at the U.S. Department of Health and Human Services (HHS), and use regular order to pass other ACA repeal and replacement bills.*

***COMMENT.** This Briefing is intended to present a high-level overview of the House GOP proposal, focusing on the tax provisions. The GOP proposal also encompasses changes to Medicaid and other many other non-tax provisions. As the GOP proposal moves through the House, there may be changes to the tax and non-tax provisions. There could also be changes in the Senate down the road.*

## TAX PROVISIONS

The ACA contains a number of tax provisions, put in place to encourage compliance or help offset the cost of the health care reform. The House GOP plan would repeal all of the ACA’s tax provisions with one exception. The House GOP plan delays the excise tax on high-dollar health plans until 2025.

### Individual and Employer Mandate Penalties

One key to the ACA’s overall hope for success was to have as many individuals as possible covered by health insurance in an effort

to spread the risk and lower the costs. Part of this goal was to be achieved through credits and other incentives; as well as through a penalty structure by way of the individual and employer mandates.

These mandates would be repealed under the House GOP plan, effective for months beginning after December 31, 2015 by retroactively reducing the penalties to zero.

**IMPACT.** *To discourage healthy individuals on insurance plans from leaving, which would tend to drive overall premiums up, the House GOP plan would amend the ACA market reforms to permit insurance companies to impose up to a 30 percent premium penalty for up to a year on those who let their insurance lapse. This change, along with permission to raise premiums for older individuals and lower them for younger, is designed as a substitute for the individual mandate. There is some question whether these provisions would survive a Senate filibuster.*

**Net Investment Income Tax**

The Net Investment Income Tax (NII tax) on individuals equals 3.8 percent of the lesser of net investment income for the tax year, or the excess, if any of the individual’s modified adjusted gross income (MAGI) for the tax year, over the threshold amount. The threshold amounts are \$250,000 in the case of a taxpayer making a joint return or a surviving spouse, \$125,000 in the case of a married taxpayer filing a separate return,

and \$200,000 in any other case. The House GOP plan would repeal the NII tax effective for tax years beginning after December 31, 2017.

“The House GOP plan would repeal all of the ACA’s tax provisions with one exception.... [it] delays the excise tax on high-dollar health plans until 2025.”

**IMPACT.** *The NII tax is expansive in its reach. Repeal would mean the loss of significant tax revenue. According to the Joint Committee on Taxation, repeal of the NII tax would cost approximately \$158 billion over 10 years. Repeal of the Additional Medicare tax (discussed below) would cost approximately \$117 billion over 10 years.*

**IMPACT.** *Capital gains, a major component of NII, are targeted for a significant tax rate reduction under tax reform that is proposed for consideration later this year. The likely effective date for tax change will also be starting in 2018, the same as NII tax repeal. As a result, strategies to defer investment income into 2018 should begin to be considered.*

**Additional Medicare Tax**

Closely-related to the NII tax is the 0.9 percent Additional Medicare tax on employee compensation and self-employment income above certain threshold amounts (the same as for the NII tax). The House GOP plan would repeal the Additional Medicare tax effective for remuneration received and tax years beginning after December 31, 2017.

**Excise Tax on High-Dollar Health Plans**

When the aggregate cost of qualified employer-sponsored health insurance coverage (known as “Cadillac plans”) exceeds certain dollar amounts, the ACA imposes a 40 percent excise tax. In 2015, Congress delayed for two years, 2016 and 2017, the excise tax, which had been scheduled to apply to tax years beginning after December 21, 2017. The House GOP plan would effectively delay the tax until 2025, in coordination with budget reconciliation requirements.

**IMPACT.** *This delayed tax might be one of the sleeper provisions in this bill as far as impact to employers. “High-dollar” plans by 2025 are predicted to cover more than half of all employer-provided plans. According to the Congressional Research Service, the excise tax is projected to be imposed on plans that cost more than \$10,080 for single health plans and \$29,100 for family plans.*

**IMPACT.** *The Joint Committee on Taxation (JCT) released a partial estimate of the legislation on March 7. Repealing the ACA’s taxes, as well as delaying the “Cadillac” tax until 2025, would result in a federal revenue loss of over \$500 billion, according to preliminary figures. A full estimate by the JCT was not released. The CBO score is expected to include counterbalancing revenue estimates.*

**Medical Device Excise Tax**

The ACA imposes a 2.3 percent excise tax on the sale of certain medical devices. In

	ACA	AHCA
Individuals	Mandate: Taxpayers must either maintain coverage or pay a penalty unless exempt	Incentive: Beginning in 2019, taxpayers who go longer than 63 days in the past year without continuous coverage may be charged a penalty of 30% of their premium for the first 12 months of coverage
Employers	Mandate: Qualified employers must either provide affordable, minimum value coverage or pay a penalty	No mandate or incentive

2015, Congress approved a moratorium on the excise tax for two years (2016 and 2017). The House GOP plan would repeal the medical device tax effective for sales of qualified medical devices after December 31, 2017.

**Excise Tax on Tanning Services**

Amounts paid for indoor tanning services are subject to a 10 percent excise tax, the first tax under the ACA to go into effect immediately in 2010. The House GOP plan would repeal the excise tax on tanning services effective for qualified tanning services performed after December 31, 2017.

**Health Insurance Provider Fee**

The ACA imposes a fee on health insurance providers. In 2015, Congress imposed a moratorium on the fee for one year (2017). The House GOP plan repeals the fee with respect to calendar years beginning after December 31, 2017.

**TAX CREDITS**

The ACA created a number of tax credits to help offset the cost of health insurance coverage for individuals and small employers. The House GOP plan repeals these individual and employer credits but creates a new refundable credit for health insurance.

**New Refundable Credit for Health Insurance Coverage**

The House GOP bill would repeal the Code Sec. 36B premium assistance tax credit and create an advanceable, refundable tax credit for individuals to purchase state-approved, major medical health insurance and unsubsidized COBRA coverage. Coverage must meet specified essential standards. Eligible individuals must not have access to government health insurance programs or an offer of health insurance from any employer. The credits would be adjusted by age:

Under age 30 .....	\$2,000
Between 30-39 .....	\$2,500
Between 40-49 .....	\$3,000
Between 50-59 .....	\$3,500
Over age 60.....	\$4,000

Total age-based credits for any family would be capped at \$14,000. The credits and cap would be inflation adjusted. The credits are available in full for those making \$75,000 or less each year (\$150,000 for joint filers) and phase out by \$100 for every additional \$1,000 income.

*IMPACT. Despite the income caps, critics of the bill have raised the concern that many lower-income individuals would not receive as much premium assistance with this new credit as they did under*

*the ACA. Concern has also been raised over not considering the varying cost of insurance dependent upon geographic area. Note that the credit is not available for abortion coverage except when the woman's life is at risk.*

**COMMENT.** *Before repeal of the Code Sec. 36B credit, the House GOP plan would make some modifications to the credit, such as allowing use of the credit for "catastrophic only" plans.*

A program of simplified reporting on Form W-2s to verify an offer of coverage will be established. This reporting will phase out the current reporting scheme under Code Sec. 6056.

*IMPACT. Although employers would be subject to less reporting under the proposed ACA repeal-and-replace bill, state jurisdictions may require stepped up reporting to monitor health insurance more oriented toward states, individual markets and state-run pools.*

*IMPACT. Premiums would not be required to be constant irrespective of age—insurance companies would be permitted to charge up to five times as much for older insureds. Critics contend that this credit will not fully offset the rise in premiums that would be faced by older individuals.*

*IMPACT. Because of procedural restrictions on a reconciliation bill, Congress cannot repeal the current employer reporting requirements under the ACA. However, the Treasury Secretary would be authorized to not enforce the ACA reporting when it is not needed for tax purposes.*

**Code Sec. 45R Small Employer Credit**

Qualified small employers are currently eligible for a tax credit if they offer health insurance to their employees. The House GOP plan would repeal the Code Sec. 45R small employer credit generally, but only effective for tax years beginning after December 31, 2019 (after 2018 if the health plan includes coverage for elective abortions).

Taxes	ACA	AHCA – Repeal Effective Date
Tanning Tax	10 percent sales tax on indoor tanning services	2018
Medical Device Tax	2.3 percent excise tax on the sale of certain medical devices	December 31, 2017
Net Investment Income Tax	3.8 percent to certain net investment income of individuals, estates, and trusts with income above certain amounts	2018
Branded Prescription Drug Fee	Annual fee on certain brand pharmaceutical manufacturers	December 31, 2017
Health Insurance Provider Fee	Annual fee imposed on certain health insurers	December 31, 2017
Additional Medicare Tax	0.9 percent of an employee's wages or a self-employed individual's self-employment income	2018

Shortly after the House GOP plan was unveiled, HHS Secretary Tom Price described it as a “work in progress.” This could signal possible changes down the road. President Trump said that this legislation is “phase 1” and that “Our wonderful new healthcare bill is out for review and negotiation.” Vice President Mike Pence, too, weighed in, saying that he and the President believes the American Health Care Act is the framework for moving forward. “We are open to improvements in the legislative process... but this is the bill, and the President supports the American Healthcare Act.”

## OTHER PROVISIONS

Included in the House GOP plan are a number of other provisions, impacting the medical expense deduction, health savings accounts and more.

**COMMENT.** *The House GOP plan does not repeal codification of the economic substance doctrine or the Patient Centered Outcomes Research Institute (PCORI) fee.*

### Medical Expense Deduction

The ACA revised the threshold to claim an itemized deduction for unreimbursed medical expenses from 7.5 percent of adjusted gross income (AGI) to 10 percent of AGI for tax years beginning after December 31, 2012. However, the ACA included special rules for individuals (or their spouses) age 65 and older. The House GOP bill returns the medical expense deduction to its pre-ACA parameters, effective starting in 2018. Individuals age 65 and older, however, would return to the 7.5 percent AGI level starting retroactively to January 1, 2017.

**IMPACT.** *The ACA only changed the medical expense deduction for purposes of regular tax. The ACA left untouched the rules for the medical expense deduction for alternative minimum tax*

*(AMT) purposes. Taxpayers should also be aware of a provision in upcoming tax reform proposals that would increase the standard deduction significantly and, therefore, not warrant itemizing deductions—including for medical expenses—for many more taxpayers.*

### Health Flexible Spending Arrangements

The ACA limits contributions to health flexible spending arrangements (health FSAs) to \$2,500 (adjusted for inflation). The House GOP plan would repeal this limitation, starting in 2018.

### Over-the-Counter Medicines

Generally, expenses for health FSAs and similar arrangements incurred for a medicine or drug are treated as a reimbursement for a medical expense only if the medicine or drug is a prescribed drug or insulin. The House GOP plan would eliminate this rule, which the GOP refers to as a “tax on over-the-counter medications,” for distributions after December 31, 2017.

**IMPACT.** *Many FSAs allow either a carryover of \$500 unused amounts into the next year or use of account balances through March 15 of the following year. In either*

*case, at least a portion of FSA contributions during 2017 may therefore be used in 2018 for over-the-counter medicines or drugs.*

### Remuneration

Under the ACA, the allowable deduction for applicable individual remuneration and deferred deduction remuneration attributable to services performed by applicable individuals that is otherwise deductible by a covered health insurance provider is limited to \$500,000. The House GOP plan would repeal this provision effective for tax years beginning after December 31, 2017.

### Retiree Drug Subsidy

The House GOP plan would re-instate the business-expense deduction by employers for the value for providing retiree prescription drug subsidies without deduction for the amount of any federal subsidy, including Medicare Part D. This re-instatement would apply for tax years beginning after December 31, 2017.

### Branded Prescription Drug Fee

The ACA imposes an annual fee on each covered entity engaged in the business of manufacturing or importing branded prescription drugs. The House GOP plan would repeal the branded prescription drug fee.

	ACA	AHCA
Tax on Health Savings Accounts	20% tax on distributions from HSAs or Archer MSAs that are not used for qualified medical expenses	10% tax on distributions from HSAs (15% tax on Archer MSAs) that are not used for qualified medical expenses after December 31, 2017
Maximum Contribution Limit to HSAs	\$3,400 for self-only coverage, \$6,750 for family coverage in 2017	\$6,550 for self-only coverage, \$13,100 for family coverage starting in 2018
HSA Catch-Up Contributions	Each spouse may make catch-up contributions to their own HSA account	Both spouses may make contributions to one HSA starting in 2018
Medical Expenses Incurred Before HSA was Established	HSA is treated as established on the day it is actually established	If an HSA is established during the 60 day period beginning on the date that an individual's coverage under a HDHP begins, then HSA treated as having been established on date coverage under the HDHP begins starting in 2018

## Health Savings Accounts

The House GOP plan would increase the annual limit on aggregate health savings account (HSA) contributions to equal the sum of the maximum of the sum of the annual deductible and out-of-pocket expenses permitted under a high deductible plan. As a result, the basic limit would be at least \$6,550 for self-only coverage and \$13,100 for family coverage, beginning in 2018.

**IMPACT.** *This provision would nearly double the amount that may be contributed to an HSA in 2017, which is \$3,400 for individuals and \$6,750 for families.*

Also starting in 2018, both spouses would effectively be allowed to make a catch-up contribution to a single HSA.

Also starting in 2018, HSA withdrawals would be able to be used to pay qualified medical expenses incurred up to 60-days before the HSA is established by treating coverage as beginning on the date that an individual's coverage under a high deductible health plan begins.

**IMPACT.** *Distributions from health savings accounts (HSAs) and Archer medical savings accounts (MSAs) not used to cover qualified medical expenses have been subject to an additional 20 percent tax as well as being included in taxable income. The House GOP plan would revert the 20 percent tax back to 10 percent for HSAs and*

*15 percent for MSAs, effective for distributions made after December 31, 2017.*

**COMMENT.** *According to House Speaker Paul Ryan, R-Wisc., the ACA repeal and replacement process will consist of three distinct phases. The bill being passed through budget reconciliation is phase 1. Next, Health and Human Service Secretary Tom Price will “deregulate the marketplace to lower costs and stabilize the market,” Ryan said. Finally, the House will have “phase 3” bills to address certain issues that are not permitted to be passed through reconciliation because of budget rules, according to Ryan. Association health plans and interstate coverage are two of the issues Ryan expects to address in subsequent legislation, which will require 60 votes in the Senate.*