How the 2017 Tax Reform Act May Impact Healthcare Costs and Spending

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The 2017 Tax Reform Act, formerly known as H.R.1 the Tax Cuts and Jobs Act, was signed into law by President Trump on December 22, 2017. This politically charged bill first passed the Senate by a strict party line vote of 51-48 and passed the House by a final vote of 224-201. No Democrats voted for the bill in either the Senate or the House. Republicans were eager to pass the bill, claiming that families would see an average of $2,200 cut from their annual taxes.[1] The most controversial part of the bill pertains to the elimination of the Affordable Care Act's financial penalty for individuals failing to obtain healthcare insurance. This post discusses the effect of this repeal on health insurance markets and explores other ways the bill may affect healthcare.

The Affordable Care Act (ACA) required qualified individuals to pay a penalty if they failed to obtain healthcare coverage. This penalty has come to be known as the individual mandate. By 2015, qualified individuals who did not obtain coverage were forced to pay the higher amount of either 2.5% of their annual income or $695.[2] The 2017 Tax Reform Act eliminated these financial penalties for failure to obtain insurance. The amendments made by this section will apply beginning January 1, 2019. The Supreme Court's decision in National Federation of Independent Business v. Sebelius defining the individual mandate as a tax enabled Republicans to strike the ACA's individual mandate via a change in the tax law. (*See* National Federation of Independent Business v. Sebelius). All other parts of the ACA remain in force. The federal government is still required to help pay premiums for people with low income, and insurers are unable to deny coverage or raise premiums for patients who have preexisting conditions. Additionally, adults may continue on their parents' insurance plans until they are 26, and the millions of people who became eligible for Medicaid under the ACA's expansion may keep their insurance.

The Republican party considers the Tax Reform Act a major victory and believes that reductions in insurance coverage are not concerning because these reductions would be voluntary.[3] The party has long echoed the sentiment that families should be able to make decisions about what type of coverage they want and what works for them. Republicans have also expressed their beliefs that individuals choosing to forgo coverage bear the full cost of their decision. The party cites evidence that eliminating the mandate may save the government approximately $338 billion over the next ten years.[4] The savings result from a decrease in government subsidies to people who will drop insurance and from anticipated cuts to Medicaid and Medicare, which will reduce the number of government insurance beneficiaries. These efforts, however, will require additional legislation.

Despite Republican thinking, decisions by individuals to forgo insurance affect not only themselves, but also impact the health insurance market. According to the Congressional Budget Office (CBO), repealing the individual mandate will reduce insurance coverage by approximately 13 million people by 2027 and raise insurance premiums by an additional 10 percent. Without the mandate, healthy individuals that do not qualify for Medicaid and are not covered through their employer may exit the insurance markets, creating a sicker and poorer insurance pool. Often, healthy individuals, more specifically healthy younger individuals, tend to undervalue insurance coverage. For many in this population, the savings from upfront costs from foregoing healthcare coverage outweigh the potential benefits the coverage may provide, because they perceive themselves to be less likely to need the care in the future. If healthy and younger people exit the insurance market, they shift the costs to the populations that do pay for health insurance. Healthcare expenses will rise because uninsured populations do not seek preventative care and wait to receive care until they are really sick. This pattern leads to more visits to emergency rooms, which leads to higher medical costs. Patients who are uncovered and need emergency treatment still receive treatment even if they are unable to pay. In 2017, the average hospital bill for the uninsured was $34,953, an amount that is unaffordable to most people.[5] Because many uninsured patients are unable to fully pay their hospital bill, these costs shift to hospitals, governments, and insurance consumers. Without a stable and balanced insurance pool, premiums will rise.

The repeal of the individual mandate and consequent increase in insurance premiums are causing some Republicans to push for bipartisan fixes to help stabilize insurance markets. Senator Susan Collins (R-ME) voted for the tax bill after receiving verbal commitments from President Trump and Senate Majority Leader Mitch McConnell to pass two bipartisan bills aimed at counteracting premium increases resulting from the repeal of the individual mandate. One of the bills, known as the Alexander-Murray bill, funds cost sharing reduction (CSR) payments to insurers. The second bill written by Collins and Senator Nelson (D-FL) establishes a reinsurance pool to pay for some patients' claims and sets aside $10.5 billion over the next two years. Despite McConnell's original promise to push these bills through Congress in December 2017, they have received stiff opposition in the House. Speaker of the House Paul Ryan has stated that he is not bound by McConnell's agreements.[6] Supporters of these measures suggest attaching the bills to a spending agreement that lawmakers will vote on sometime before January 19.

In addition to health insurance changes, healthcare costs and markets may be impacted in other ways. The new tax bill allows taxpayers to deduct up to 60 percent of the taxpayer's contribution base for such year – nearly double the amount previously allowed. Many nonprofit and charitable health organizations fear that this change may lead to a decline in personal donations to their organizations. Estimates by the Joint Committee on Taxation project that this expansion could result in a $95 billion decline in the value of charitable deductions claimed on tax returns in 2018.[7] Democrats also voiced their opposition for the bill, fearing that it would increase the federal deficit. In fact, the CBO projected that the tax bill will raise federal deficit by $1.7 trillion over the next ten years.[8] This may be the tax bill's greatest threat. An increased federal deficit often reduces federal spending. Since Medicaid and Medicare programs account for 30% of federal spending, they are likely targets for future reductions, such as increasing the age of Medicare eligibility or creating spending caps per beneficiary.[9] As the tax bill on its own will not create these effects, Congress may pass additional legislation in attempt to mitigate the growing federal deficit. Stay tuned for more information regarding the tax reform's impact on healthcare costs!

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[3] Matthew Fiedler, *Repealing the Individual Mandate Would Do Substantial Harm*, The Brookings Institute (Nov. 21, 2017), https://www.brookings.edu/blog/up-front/2017/11/21/repealing-the-individual-mandate-would-do-substantial-harm/.

[4] Tami Luhby and Lauren Fox, *Axing Obamacare Individual Mandate Would Save $338 Billion: CBO*, CNN Money (Nov. 8, 2017) http://money.cnn.com/2017/11/08/news/economy/tax-reform-individual-mandate-cbo/index.html?iid=EL.

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[8] Nash Jenkins, *The Republican Tax Plan Would Add $1.7 Trillion to Federal Deficits*, Time (Nov. 8, 2017), http://time.com/5015271/republican-tax-plan-deficits-trillion/.

[9] David Blumenthal, *How the New U.S. Tax Plan Will Affect Health Care*, Harv. Bus. Rev. (Dec. 19, 2017), https://hbr.org/2017/12/how-the-new-u-s-tax-plan-will-affect-health-care.