Vermont Legislative Joint Fiscal Office

One Baldwin Street • Montpelier, VT 05633-5701 • (802) 828-2295 • Fax: (802) 828-2483

ISSUE BRIEF

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Prepared by: Joyce Manchester

The Cadillac Tax: An Excise Tax on High-Value Health Insurance Plans

Summary

The "Cadillac tax" is a federal excise tax on high-value health insurance plans beginning in 2018. The 40-percent excise tax applies to the value of health benefits over a certain threshold, equal to $10,200 for individual plans and $27,500 for family plans in 2018 and indexed in later years. JFO estimates that many Vermonters, and most State employees, have insurance plans that will be subject to the tax in 2018. Some employers will likely modify their plans or shift the tax to their employees in order to prevent their costs from increasing substantially.

Based on current plan design and Vermont's share of the national economy, JFO estimates that the aggregate excise tax bill in Vermont could be between $9 million and $24 million in 2018 and $40 million or more in 2023. All individual and family plans offered to State employees in 2015 are projected to be subject to the tax in 2018, imposing a new tax of about $6.8 million on the State government or its employees in the absence of changes in plan choice and design. In addition, JFO projects that one of the six individual and family plans offered to Vermont school employees through VEHI would be subject to the tax at the start of 2018. Revenues from the excise tax will partially offset the federal costs of the Affordable Care Act.

What is the Cadillac tax?

To slow growing costs for health care and finance expanded coverage, the Affordable Care Act (ACA) imposes an excise tax on high-value health insurance plans. The excise tax will take effect in calendar year 2018, thereby affecting one-half of the State of Vermont's fiscal year 2018. Health insurance issuers and sponsors of self-funded group health plans will be assessed an excise tax on the value of any benefits provided to employees that exceed a predetermined threshold. The media has labeled the tax the "Cadillac tax."

The excise tax will be imposed on the "excess benefit," defined as the cost of coverage for health benefits that exceeds the annual limit of $10,200 for self-only coverage and $27,500 for self and spouse or family coverage. The tax rate is 40 percent. The annual limit or threshold will be adjusted for individuals in high-risk professions, such as law enforcement, and may also be adjusted by age and gender. For example, the limits may be higher ($11,850 single, $30,950 self and spouse or family) for employers with a disproportionately older population. Analysts expect that more specific regulations will be forthcoming from the IRS. The threshold will increase by the rate of general inflation plus one percent in 2019 and 2020, and by the rate of general inflation in each year beyond 2020. It will be rounded to the nearest $50. Historically, the rate of health care inflation has exceeded the rate of general inflation, suggesting that more plans will become subject to the tax over time. Revenues from the excise tax will partially offset the federal costs of the Affordable Care Act.

The cost of coverage subject to the tax is more expansive than just the total premium. It also includes employer contributions to a health reimbursement account (HRA), employer and employee contributions to a health flexible spending account (FSA), and employer and employee salary reduction contributions to a health savings account (HSA). In this Issue Brief, we look only at the total premium and therefore likely underestimate the reach of the tax.

For self-funded plans, the "COBRA equivalent" will be used to determine the cost of coverage. In those cases, the cost of coverage is determined by the amount the employer would charge individuals on COBRA who no longer work for the employer but have the right to pay the full cost of the health insurance that was previously paid in part by their employer. Again, forthcoming regulations will set the exact rules for determining the COBRA rate and how the tax will be paid.

Some analysts are concerned that the administrative costs associated with the new excise tax could be quite high. Reporting requirements could be complex, especially for employers that have HRA, FSA, or HSA plans that will be included in the taxable amount. JFO has not estimated the implications of those costs.

How will the excise tax affect Vermonters in general and Vermont State employees, school employees, and people who buy health insurance on the exchange in particular?

Some Vermonters in the private sector may have health insurance plans that would be subject to the excise tax, but we have not yet obtained data on those plans. At the same time, most Vermont State employees and school employees will have plans that are subject to the tax in 2018 or several years thereafter. In addition, Vermonters who obtain platinum plans on the health insurance exchange through their employers will face the tax early in the next decade.

To get a ballpark figure of the new tax burden statewide in Vermont stemming from the excise tax on high-value health insurance plans, we turn to nationwide estimates from the Congressional Budget Office (CBO). CBO assumed that some employers will reduce the value of their plans to avoid the tax, but others will simply pay it. The estimates suggest that $5 billion will be collected nationwide through the Cadillac tax in fiscal year 2018. That sum would grow to $22 billion in fiscal year 2023. Vermont generally accounts for 0.18 percent of U.S. economic activity,[1] suggesting that insurance companies and self-insured employers would pay about $9 million in 2018 on behalf of Vermonters who have high-value health insurance policies. That estimate for Vermont may be low given the prevalence of higher value plans in the State. For example, a Pew report on state employee health plan spending in 2013 finds that Vermont State employees have the fifth highest average total premium in the country. Based on the national estimates, the excise tax levy for Vermont is estimated to reach $40 million in 2023.

The contractor who modeled Green Mountain Care for the Governor's office estimated that Vermonters would pay $24 million in Cadillac tax payments in 2018 under current law (State of Vermont 2014). That estimate assumed no change in behavior among employees or employers and grew premiums and plans as they existed in 2014 to 2018-2021.[2] A reasonable estimate of the burden of the Cadillac tax on Vermonters in 2018 probably lies between $9 million and $24 million. The contractor estimated $38 million in 2021 under current law, suggesting an amount that exceeds $40 million in 2023.

Impact on Vermont State Employees. Information on premium amounts and enrollment for Vermont State employees and retirees under age 65 offers insight on how the Cadillac tax could affect public plans. For 2015, Vermont State employees and retirees may choose one of two health insurance plans.[3] Based on the announced 2015 premium amounts, the Total Choice Plan for both individuals and families would be subject to the excise tax in 2015 if it were already in effect. JFO estimates that both the Total Choice Plan and the SelectCare POS Plan for individuals and families would be subject to the excise tax in 2018 (see Table 1).[4] For example, the Total Choice plan for individuals is projected to be subject to the excise tax on about $3,500 of excess benefits, resulting in a tax of about $1,400. The excess benefit in the SelectCare family plan is projected to be about $4,000, for a tax of about $1,600. Given the distribution of individual and family plans in Total Choice and SelectCare POS plans in 2014, the total excise tax for all State employees could be about $6.8 million in 2018.

[1] Data from the Bureau of Economic Analysis show that Vermont GDP has been approximately 0.18 percent of U.S. GDP in recent years.

[2] The contractor's estimates are on pg. 5 of the Green Mountain Care Final Report Data Appendix, available at: http://hcr.vermont.gov/sites/hcr/files/2014/GMCReport2014/ECON%20MODELING%20OUTPUT%20FOR%20GMC%20REPORT.pdf. Premiums in future years increase with the preliminary consensus annual growth rates for non-Medicare, non-Medicaid health care costs developed by the Administration, RAND, and JFO. The projected trend for 2015 through 2017 is 6.2 percent, 6.1 percent, and 7.7 percent, respectively. The administration assumed a growth rate of 5.6% in 2018 and average growth of 5.1 percent from 2017 to 2021.

[3] Three plans were offered until 2015, but as a result of collective bargaining between the State and Vermont State Employees' Association in 2014, the State Employees' Health Plan will no longer offer the option of the HealthGuard PPO Plan.

[4] Premiums in future years increase with the preliminary consensus annual growth rates for non-Medicare, non-Medicaid health care costs developed by the Administration, RAND, and JFO. The projected trend for 2015 through 2018 is 6.2 percent, 6.1 percent, 7.7 percent, and 6.6 percent, respectively. For years beyond 2018, the consensus trend is 6.25 percent. See "Preliminary Consensus Health Care Spending Trends," October 28, 2014. http://www.leg.state.vt.us/jfo/healthcare/health_spending_trend_memo_final.pdf.

Impact on Vermont School Employees. Active school employees and retired school employees under age 65 covered by the Vermont Education Health Initiative (VEHI) may choose one of six health insurance plans. Using premium amounts for the 2015–2016 school year, JFO estimates that one of the six plans for individuals and families would be subject to the tax in the first half of calendar year 2018; four of the plans for individuals and families, including the most popular plan, would be subject to the tax in the second half of fiscal year 2021 (see Table 2).

Table 1.
Premiums for VT State Employees

	Annual Total Premium in 2015	Annual Total Premium in 2018	Annual Limit in 2018	Excess Benefit in 2018	Excise Tax Liability in 2018
Total Choice Plan					
One Person	$11,257	$13,661	$10,200	$3,461	$1,384
Two Person	$22,513	$27,321	$27,500	N.A.	N.A.
Family	$30,956	$37,566	$27,500	$10,066	$4,026
SelectCare POS Plan					
One Person	$9,421	$11,433	$10,200	$1,233	$493
Two Person	$18,842	$22,865	$27,500	N.A.	N.A.
Family	$25,907	$31,440	$27,500	$3,940	$1,576

Notes: Total premiums are assumed to grow with the preliminary consensus trends.
Gray = estimated to be subject to excise tax

Table 2. Updated February 12, 2015.
Vermont Education Health Initiative (VEHI), Estimated Annual Premiums, Managed Parity Plans

	2015-16 (actual)		**2017-18**		**2020-21**	
	Single	Family	Single	Family	Single	Family
Dual Option: VHP	$8,370	$22,056	$9,565	$25,203	$11,521	$30,359
Dual Option: $300 Comp Plan	$8,370	$22,056	$9,565	$25,203	$11,521	$30,359
JY	$9,396	$24,916	$10,737	$28,471	$12,934	$34,295
$1200 Comp Plan	$6,696	$17,647	$7,651	$20,165	$9,217	$24,290
$1800 CDHP (HSavA)	$6,696	$17,647	$7,651	$20,165	$9,217	$24,290
$100 Comp Plan	$8,629	$22,837	$9,861	$26,096	$11,878	$31,434
THRESHOLD	*NA*	*NA*	*$10,200*	*$27,500*	*$11,100*	*$29,950*

Notes: Total premiums are assumed to grow with the preliminary consensus trends.
Gray = estimated to be subject to excise tax

Impact on Vermonters Who Obtain Employer-Sponsored Insurance through the Exchange. For Vermonters who obtain employer-sponsored health insurance on the exchange, only the platinum plans are expected to be subject to the excise tax over the next decade or so. Platinum plans offer more generous coverage than silver, gold, or bronze plans and would be more likely to exceed the annual limits for the excise tax. Neither the BlueCross BlueShield of Vermont (BCBSVT) platinum plans nor the MVP platinum plans for individuals and families in Vermont would be subject to the tax in 2018, JFO estimates (see Table 3). In 2020, the MVP platinum family plan is expected to exceed the annual limit, and both BCBSVT and MVP platinum plans for individuals and families would exceed the annual limits by 2022.

Table 3.
Estimated Annual Premiums for Platinum Plans Sold on the Exchange

	2015	2018	2020	2022
BCBSVT				
Single	$7,490	$9,090	$10,295	$11,622
Family	$21,047	$25,542	$28,929	$32,659
MVP				
Single	$7,761	$9,419	$10,668	$12,043
Family	$21,809	$26,466	$29,976	$33,840
Estimated thresholds for the Excise Tax				
Single	N.A.	$10,200	$10,850	$11,350
Family	N.A.	$27,500	$29,250	$30,650

Notes: Total premiums are assumed to grow with the preliminary consensus trends.
Gray = estimated to be subject to excise tax

What level of awareness exists in the public sector regarding the Cadillac tax?

Awareness of the new excise tax on high-value health insurance plans is gaining steam, and some organizations that oversee health insurance plans for public employees are already planning for its impending implementation.

For example, officials in both State government and the Vermont State Employees' Association know about the coming excise tax and recognize the need to take it into account when they begin bargaining the next contract for State employees in the fall of 2015. That contract negotiation will determine the benefit package for State employees between July 2016 and June 2018 and will therefore include plans that could be subject to the new tax in calendar year 2018.

VEHI is using an outside benefits consultant to help navigate the costs and implications of the new excise tax on high-value tax plans and awaits further guidance from the federal government.

The Vermont League of Cities and Towns is aware that a few of their cities as well as many employees of smaller towns who purchase platinum plans on the exchange will face the new excise tax. All employers with 50 or fewer employees currently use the exchange to purchase health insurance for their employees, with the vast majority purchasing platinum plans. Town governments with 50 or fewer employees fall into this category. By 2016, all towns with 100 or fewer employees will use the exchange. At that time, it is likely that only the largest cities in Vermont will maintain their own self-insured health insurance plans. In 2018 when the excise tax goes into effect, the excise tax as it applies to employer-sponsored platinum plans on the exchange could affect a number of Vermont cities and towns.

Around the country, some state and local governments have already indicated a need to take action. The New York Times noted in 2013 that cities and towns across the country are pushing municipal unions to accept cheaper health benefits in anticipation of the Cadillac tax. If municipalities and unions can reduce their health care costs, perhaps by increasing the amounts employees are required to pay in out-of-pocket expenses and increasing their deductibles, they may avoid the excise tax; if they cannot, the price of the tax in 2018 could be substantial.

In New Jersey, Governor Chris Christie has warned that taxpayers will have to pay $261 million for public employee health benefits that exceed the threshold in 2018. The Cadillac tax is expected to reach $837 million in that State four years later.

A blog entry by Physicians for a National Health Program suggests that "cities including New York and Boston, and school districts from Westchester County, N.Y., to Orange County, Calif., are warning unions that if they cannot figure out how to rein in health care costs now, the price when the tax goes into effect will be steep, threatening raises and even jobs."

How is the private sector responding to the Cadillac tax?

Some private employers are already taking actions to mitigate the cost of the Cadillac tax. Because health care costs are expected to rise more rapidly than the annual limits for the excise tax in the future, a growing number of health insurance plans likely will be subject to the tax in years beyond 2018. Many analysts believe that the response by employers to the Cadillac tax will be mixed. Some employers will pay the new tax to maintain their high-value health insurance plans, perhaps passing along some of the added cost to their employees. Other employers will take actions to reduce the generosity of their plans to avoid payment of the new tax.

A couple of recent surveys of private employers provide details on how employers are responding to the new excise tax. In general, high-value plans could be cut back by increasing deductibles and co-pays and limiting reimbursement amounts through the use of networks or other structures that change the delivery of health care. Alternatively, employers could keep their high-value plans and pass along some or all of the new excise tax to employees or stop offering health insurance at the workplace because the exchange is available.

A recent analysis of large U.S. employers by Towers Watson finds that roughly one-half of large U.S. employers will be hit with the excise tax in 2018; by 2023, 82 percent of all plans, public and private, will likely be impacted by the Cadillac tax. According to the survey, private employers are planning either to reduce the cost of their plans explicitly, pass on the tax to their employees, or give employees a stipend of taxable dollars and encourage them to purchase coverage through a public or private insurance exchange.

Another recent survey by Aon Hewitt finds that 68 percent of the 317 employers interviewed expect the excise tax to affect at least one or the majority of their current health plans by 2023. When asked about future actions they are likely to consider in order to minimize their exposure to the tax, employers reported that they are likely or highly likely to consider the following actions:

- Reduce plan design richness through higher out-of-pocket member share (79 percent)
- Adopt cost control strategies, such as reference-based pricing and a narrow provider network (40 percent)
- Restructure coverage tiers to align with tax threshold ratios (37 percent)
- Limit FSA, HSA, and/or HRA contributions counted against the thresholds (31 percent)
- Limit buy-up options for employees (26 percent)
- Move to a private health exchange (16 percent)

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