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HOUSE WAYS AND MEANS OFFSET FOR REPEALING AFFORDABLE CARE ACT'S TAX REPORTING REQUIREMENT WOULD WEAKEN HEALTH REFORM

by Judith Solomon

On February 17, both the House Ways and Means Committee and the full Senate approved legislation to repeal a provision of the health reform law — usually referred to as the 1099 tax reporting requirement — that is designed to raise revenue by improving compliance with the nation's tax laws. The full House will consider its version of the bill this week.

The Ways and Means Committee declined to use the same "offset" as the Senate bill to pay for the cost of repealing this provision.[1] (Repealing the reporting requirement would cause a loss of $21.9 billion in revenue over ten years, according to the Joint Committee on Taxation, because tax avoidance and tax cheating would remain at higher levels rather than being reduced.) The Ways and Means Committee's offset would seriously weaken health reform by imposing large tax penalties on substantial numbers of people who received subsidies to purchase coverage in the health insurance exchanges.

As a result, the offset would discourage many people with modest incomes from applying for subsidies in the first place and lead more of them to remain uninsured instead (and pay a modest penalty for failing to have insurance). Those who elected not to purchase coverage would predominantly be people who thought they could risk going without coverage because they are in good health. As a consequence, the pool of people who enroll in the exchanges would consist, on average, of less-healthy individuals than would otherwise be the case — which would push up premiums for policies available through the exchanges and thereby depress exchange enrollment further. The Ways and Means provision also likely would fuel backlash against the health reform law on the part of lower-middle income families and individuals who purchased coverage and then found themselves owing large sums to the Internal Revenue Service.

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[1] The Senate bill would offset the costs of repealing the 1099 provision by directing the Office of Management and Budget to rescind (or cancel the use of) $44 billion in funds that Congress previously provided but that have not yet been "obligated" for expenditure. Another difference between the two bills is that the Ways and Means bill also would repeal a separate provision of law requiring landlords to report on rental property expenses. This provision helped to pay for a small business lending law enacted in September 2010. Repealing it would cost $2.8 billion over ten years, according to the Joint Committee on Taxation.

For these reasons, the Ways and Means offset would increase the chances that health reform would not survive the political challenges that lie ahead — and would work less well if it did survive.

Background: The Affordable Care Act's Year-End Reconciliation Provision

The Affordable Care Act (ACA) contains a mechanism to reconcile the subsidies (or premium credits) that people receive over the course of a year to help them buy coverage in the exchanges with the final amount of the premium credit for which they turn out to qualify, based on their final income for the year. If, when taxpayers file their tax returns, the amount of the premium credits they received during the year exceeds the final amount for which they are found to have qualified, they will be required to pay some or all of the difference back to the IRS — even if they received premium credits for only part of the year when their income was low, and the credits they received accurately reflected their income in those months.

In crafting the ACA, Congress recognized that this year-end "tax reconciliation" procedure differed dramatically from how other means-tested programs work and could have serious unintended consequences. Eligibility for other means-tested programs such as Medicaid and food stamps is based on a household's *current* income; if a household whose low income during the first part of the year qualifies it for benefits then obtains a job (or a higher-paying job) that makes it ineligible for benefits for the rest of the year, it is not required to pay back the assistance it received during the months it was poor.

In contrast, under the ACA, a household that receives a subsidy to help it buy insurance for the first half of the year and then finds a job and ceases to receive a subsidy — and enrolls in employer coverage instead — could be required to repay all or a substantial part of its subsidy at tax filing time because its income for the year as a whole would be higher than its annualized rate of income in the period during which it received the subsidies. Similarly, a family that loses its job, income, and employer-based health coverage in the middle of a year would be able to receive a subsidy to help it purchase coverage for the remainder of the year — but could then be made to pay much or all of the subsidy back at tax time, even if it is still unemployed and has little or no assets.

To address these serious problems — which would likely discourage substantial numbers of people from accepting subsidies in the first place and likely lead many of them to elect to remain uninsured, thereby undermining the purpose of the law — the ACA limited the amount that families can be made to pay back at tax time. If a family's income for the year as a whole was below 400 percent of the poverty line, the family would not be required to repay more than $400 in subsidies. (Separate provisions of the ACA provide for a full set of enforcement actions, including substantial fines, to be taken against households that received excess premium credits due to misrepresentation or fraud.)

The ACA provision had a significant weakness, however: a huge "cliff" at 400 percent of the poverty line. Someone whose income ended up at 399 percent of the poverty line would owe a maximum of $400 in repayments, while someone whose income ended up at 401 percent of the poverty line would be required to repay the entire amount of premium subsidies they received for the year, which could total thousands of dollars.

Congress Significantly Increased Repayment Caps in December Legislation

Congress sharply raised this $400 cap in December to offset the cost of extending relief from scheduled cuts in Medicare payments to physicians in 2011. That legislation doubled or tripled the $400 cap for some families and increased it for others by as much as six times, depending on the family's income for the year. In a positive change, the legislation also eliminated the cliff at 400 percent of the poverty line by phasing the cap out between 400 percent and 500 percent of the poverty line. (See the table.)

Current Caps on Repayments		
Income as a percentage of the poverty line	**Cap on liability for individuals**	**Cap on liability for families**
Less than 200%	$300	$600
At least 200 but less than 250%	$500	$1,000
At least 250 but less than 300%	$750	$1,500
At least 300 but less than 350%	$1,000	$2,000
At least 350 but less than 400%	$1,250	$2,500
At least 400 but less than 450%	$1,500	$3,000
At least 450 but less than 500%	$1,750	$3,500
Above 500%	No cap — repay entire subsidy	No cap — repay entire subsidy

As a result of the December legislation, if the subsidy amount for which a family is found to have qualified for the prior year (based on its final income for the year as a whole) exceeds the subsidy that it received, then:

- The family will have to repay as much as $1,500 in subsidies if its income for the year ends up between 250 percent and 300 percent of the poverty line (between $46,325 and $55,590 for a family of three in 2011).
- The family will have to repay up to $2,000 if its income ends up between 300 percent and 350 percent of the poverty line.
- The family will have to repay up to $2,500 if its income for the year ends up between 350 percent and 400 percent of the poverty line.

These repayment amounts will, of course, be in addition to the premiums these households already paid for the months that they purchased coverage through the exchange. For example, a family of four earning 250 percent of the poverty line (about $56,000 a year) would contribute $372 a month — $4,464 on an annual basis — toward its premium.

Ways and Means Committee Provision Would Require Even Larger Repayments

The Ways and Means bill would go much further, raising the caps on repayment for many moderate-income families and eliminating them entirely for families with annual incomes between 400 percent and 500 percent of the poverty line.

Families with incomes between 200 percent and 250 percent of the poverty line would pay up to $1,500 (rather than $1,000), while those with incomes between 300 percent and 350 percent of poverty would pay up to $2,500 (rather than $2,000). Those whose annual incomes ended above 400 percent of poverty, even by a very small amount, would owe the entire subsidy they received.

Older people would end up owing more at tax time than younger people because they receive higher subsidies to reflect the higher premiums they pay for coverage. (Under the ACA, older people can be charged up to three times as much as younger people.) Similarly, people who receive higher subsidies because they live in areas of the country where coverage costs more would also owe more at tax time.

The following examples show how the Ways and Means bill would affect different families and individuals:

- Consider a 60-year-old individual who is working part-time at the start of the year, with earnings at about 250 percent of the poverty line (about $27,000 a year), who purchases coverage in the exchange with the help of a subsidy. In July, she finds full-time work with job-based coverage and ceases to receive a subsidy. At tax time, her income for the year as a whole is slightly above 400 percent of the poverty line (about $44,000 a year). Under current law, she would have to repay $1,500; under the Ways and Means bill, she would have to repay her entire subsidy — over $3,500.

- Or consider a family of four with two working spouses — one of whom is age 55 — that has income between 350 percent and 400 percent of the poverty line. Because one spouse is 55, the premium for this family's insurance is nearly $20,000; the family receives a subsidy that reduces its share of the premium to $8,600, still a very large amount. One of the spouses then receives a year-end bonus of a few thousand dollars, which pushes its income modestly over 400 percent of poverty for the year. Under current law, the family would owe $3,000 to the IRS; under the Ways and Means bill, it would owe $11,200.[2]

- Consider also a younger household of four with income at 225 percent of the poverty line that receives a subsidy for the first six months of the year. The subsidy amount accurately reflects the family's income over this period. At the start of July, an unemployed family member obtains a job with family coverage, so the household terminates its exchange coverage. When the household files its tax return, its income for the year is modestly over 400 percent of the poverty line. Under current law, this family would have to pay back up to $3,000; under the Ways and Means bill, it would have to repay every dollar it received to help it purchase coverage in the first half of the year — likely over $4,500 — even though the family was fully eligible for that assistance during that period and couldn't have afforded insurance without it.

- Another example involves a family whose main breadwinner earns significantly above 400 percent of the poverty line but loses his job and health coverage in the fall, dropping the family's income to 200 percent of poverty for the remainder of the year. The family applies for subsidies so it can purchase coverage in the exchange. But if the family is told it probably will have to repay every dollar in assistance it receives because its income for the year likely will end up slightly above 400 percent of poverty, the family will be forced to choose between being

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[2] This example is adapted from a Kaiser Family Foundation analysis. "Reconciliation of Advance Payments for Health Insurance Subsidies," February 2011.

Justification Advanced for Ways and Means Provision Overstates Case

In justifying its new offset, the Ways and Means Committee majority has argued that under the ACA, eligibility for premium subsidies will be based on "financial information that is two years old" and, because incomes can change in the interim, "many households will receive thousands of dollars in health care subsidies to which they are not actually entitled."[1] This claim rests on a mistaken characterization of how the premium subsidies are likely to work.

Under the ACA, an individual applying for a premium subsidy is required to provide his or her most recent tax return. Someone applying in late 2013 for a premium subsidy for 2014 would provide his or her tax return for 2012; this is the basis for the Ways and Means Committee's reference to two-year-old tax information. But the ACA does not limit the health insurance exchanges to using *only* the prior-tax year return in determining households' eligibility for subsidies. The ACA envisions that such information will be supplemented by current income data when a household's income has changed. The Act requires the Secretary of Health and Human Services to develop procedures to take changes in circumstances into account when determining eligibility for, and the amount of, premium credits that a household receives during the year. Accordingly, the forthcoming federal rules governing the premium subsidies are expected to direct that the exchanges collect and use more current income information when a household's income or other household circumstances have changed significantly. Other means-tested programs have performed this task for years.

A heavy-handed provision like that in the Ways and Means bill — which, as this analysis shows, would impair the success of health reform and reduce the effectiveness of the exchanges — thus is not necessary to address changes in income that have occurred since the filing of a household's prior-year tax return.

[1]Committee on Ways and Means, "Overview of H.R. 4 and H.R.__."
http://republicans.waysandmeans.house.gov/UploadedFiles/Overview_HR_and_HR_____.pdf.

uninsured for the rest of the year and repaying a large sum at tax time even though its breadwinner may still be unemployed and the family may be unable to afford such a payment. One of the purposes of health reform was to help families such as this avoid becoming uninsured if the breadwinner lost his or her job; the Ways and Means provision undercuts that purpose of the law.

- Finally, consider a family with a self-employed individual who receives a subsidy based on estimated income of 350 percent of the poverty line. At the end of the year, the family's income unexpectedly rises due to increased demand at Christmas for the products that the self-employed individual makes. As a result, the family's income for the year ends up modestly over 400 percent of poverty. Under current law, this family's liability would be capped at $3,000; under the Ways and Means bill, would have to pay back more than $5,000 at tax time.

Ways and Means Provision Would Penalize Families and Discourage Participation in Exchanges

The current repayment requirements already pose a risk. When potential applicants for premium credits learn that they may be required to pay back substantial sums, a significant number of them may decide against enrolling. In addition, people who played by the rules and received a correct subsidy amount based on their income at the time — and who ceased to receive *any* subsidy once they landed a job (or a better job, or when their income rose for other reasons) — are likely to feel aggrieved when they are compelled to pay as much as several thousand dollars to the IRS when they file their tax return.

The current repayment requirements, as increased by the December legislation, are thus at the edge of what represents sound and sustainable policy. *Substantially increasing* the required repayment amounts, as the Ways and Means bill would do, would be extremely ill-advised. It would penalize and cause hardship to large numbers of modest-income families who have done everything they are supposed to do and have received subsidies that accurately reflected their needs and circumstances during the period they got that assistance. The Ways and Means provision would require them to repay very large sums because their income during the months they did *not* receive a subsidy, such as after they found a job, significantly exceeded their income during the months they did receive assistance.

As noted, people applying for subsidies will have to be informed in advance about the possibility that they could be required to pay back large amounts, and this will lead some people who are in good health to elect to remain uninsured (and pay a penalty) rather than pay a substantial amount for their share of the premiums *and* risk owing much more at tax time. Substantially increasing the repayment amounts would surely lead more people to decline coverage and thereby make the exchanges less viable. It would discourage participation in the exchanges by many of the very people the law was intended to help, such as those who are laid off and lose job-based coverage in the middle of a year. And it could fuel backlash against the health reform law (which might be one of the provision's intended purposes).