State-employee health benefits: Avoiding the ObamaCare 'Cadillac tax'

Naomi Lopez Bauman, Director of Health Policy

The problem: Under the Affordable Care Act, or ACA, the federal government imposes an excise tax on high-value, employer-provided health-insurance coverage, commonly referred to as "Cadillac" plans.[1] Originally scheduled to go into effect in 2013, the Obama administration has delayed levying the "Cadillac tax" until 2018.[2]

The value of some health-insurance plans for Illinois' active state employees and their dependents is so generous that it could trigger the ObamaCare "Cadillac tax" penalty, costing taxpayers $2 billion over the next 20 years, and another $1 billion for retiree health insurance.

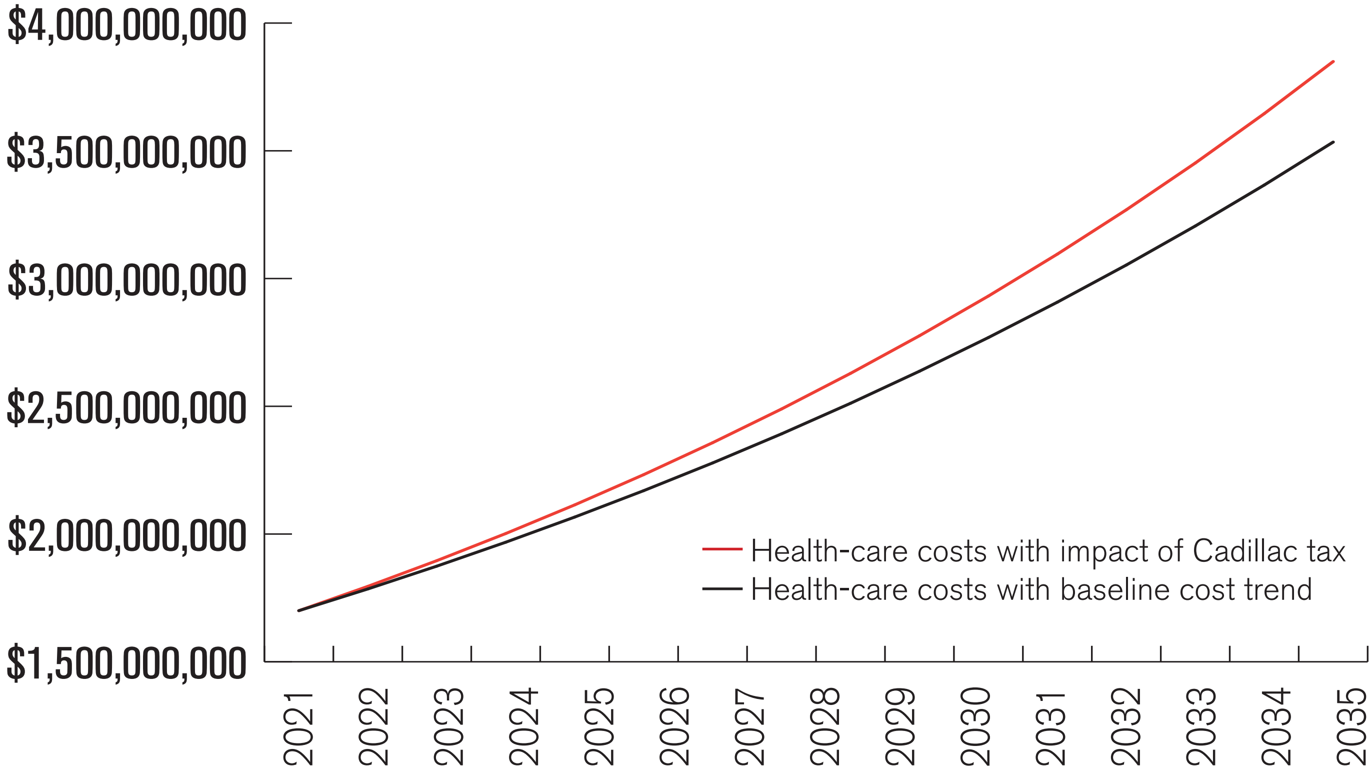
The Illinois Policy Institute has shown that the state's insurance offerings are not only out of line with what is offered in the private sector, but also that the Cadillac-tax penalty will further squeeze out spending on the state's priorities while offering no additional health benefits to government employees.[3]

Our solution: Illinois government should restructure its health-insurance offerings to be more in line with what is offered in the private sector, and in a way that does not trigger the federal tax penalty.

Why this works: The state is in the midst of a budget crisis. Taxpayers should not pay an unnecessary excise tax on state employees' health-insurance plans.

Budget impact of the Cadillac tax

Active state employee health-care costs with and without the Cadillac tax, 2020-2035*



Source: Author's calculations based on data from the Commission on Government Forecasting and Accountability and Gabriel Roeder Smith & Company

* Calculations assume a cost trend, or change in the cost of health care, of 5 percent. The impact trend, or the cost trend plus the impact of the new tax, is assumed to be 5.6 percent. The base cost was $1.7 billion beginning in 2020. See Gabriel Roeder Smith & Company, "Illinois State Employees Group Insurance Program, GASB no 45 Actuarial Valuation Report," June 30, 2013, p. 4 at cgfa.ilga.gov/Upload/SEGIP_GASB45_2013_Final.pdf for a brief discussion of the excise tax.

The problem

The Affordable Care Act, or ACA, commonly known as ObamaCare, imposes a steep excise tax, otherwise known as the "Cadillac tax," on the most generous employer-sponsored health-insurance plans. The purposes of the tax are to discourage lavish plans and generate federal revenue.

The state of Illinois offers high-value health-insurance coverage to state employees. High-value plans are those that offer coverage for most of a patient's medical claims, often having little or no deductible and low or no copays. The ACA imposes a 40 percent excise tax on employer plans beginning in 2018 with a value of more than $10,200 for an individual plan and $27,500 for a family plan. For health coverage provided through collective-bargaining agreements, the $27,500 threshold applies to both individual and family plans.[4]

The table below shows the value of Illinois government-worker health-insurance premiums for individuals and families.

Health-insurance premiums for Illinois government workers

Annual premiums (weighted), fiscal year 2015

Membership	Quality Care Health Plan	HMO (four plans)	Open Access Plan (two plans)
Active employee	$11,640	$8,316	$9,516
Active employee with two dependents	$16,800	$11,712	$13,956

Source: Commission on Government Forecasting and Accountability

The state's Quality Care Health Plan for an individual already exceeds the $10,200 threshold for individuals. And the Quality Care Health Plan that includes dependents could conceivably be the first plan to exceed the $27,500 family-plan threshold, when taking health-care inflation into account.[5]

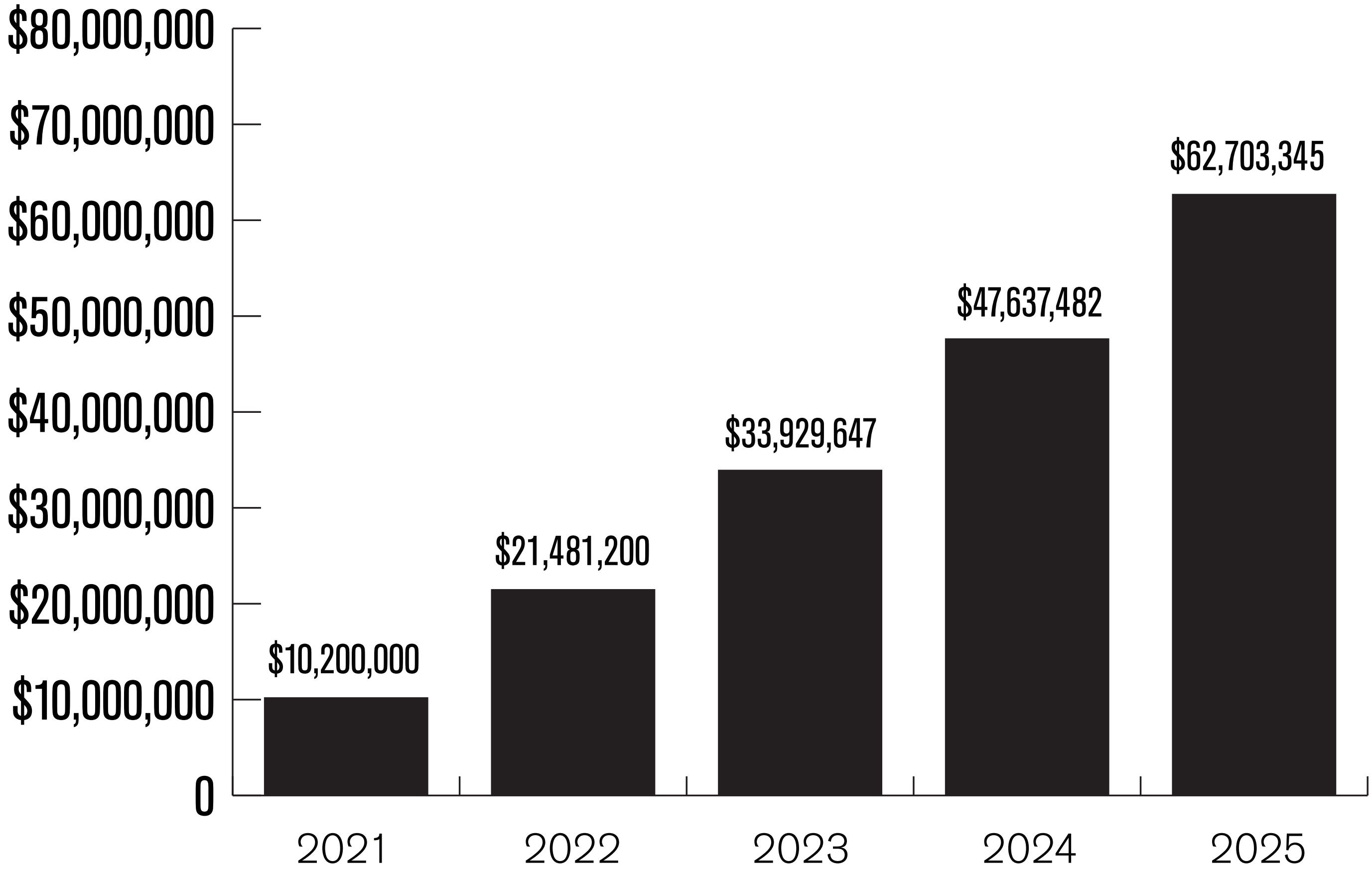
The Cadillac tax is scheduled to take effect in 2018. If the state continues to offer the current plan options, some state-employee health plans will be subject to this tax in the near term while other plans will trigger the excise tax in the long term.

That is because the allowable health-plan value is based on the inflation rate. Since the health-care inflation rate tends to outpace inflation for other goods and services,[6] over time, more and more plans are likely to be hit with this tax.

The cost to taxpayers as a result of this tax on health plans for active employees could total $2 billion through 2035.[7] This is the estimated difference between what the state will spend on active employee and dependent health-care coverage and what it state will spend once the Cadillac tax is added to the cost. While the tax is imposed on the health plan, these increased costs will likely be passed on to taxpayers and would offer no additional health benefits to state-government employees. More immediately, the cost of the Cadillac tax could total more than $175 million through 2025.[8]

Annual budget impact of the Cadillac tax: $175M by 2025

Active state employee health-care impact of the Cadillac tax, 2021-2025*



Author's calculations based on data from the Commission on Government Forecasting and Accountability and Gabriel Roeder Smith & Company

* Calculations assume a cost trend, or change in the cost of health care, of 5 percent. The impact trend, or the cost trend plus the impact of the new tax, is assumed to be 5.6 percent.

As it turns out, taxpayers may already be on the hook for the Cadillac tax on retiree health plans. At present, about 86,000 eligible retirees and 40,000 of their dependents can enroll in state-sponsored plans for full health benefits (for those under age 65) and supplemental coverage (for those 65 years and older) with an average contribution of 12 percent of the plan's total cost.[9] This is virtually unheard of in the private sector.

While the Illinois Supreme Court ruled in Kanerva v. Weems that retiree health benefits are a function of the pension system and therefore covered by the Illinois Constitution's pension clause, an upcoming ruling from the Illinois Supreme Court could determine whether those benefits are absolute or can be altered. Depending on the outcome of a legal challenge to changes to state-employee retiree pension benefits, Illinois taxpayers may be forced to fully shoulder another $1 billion through 2035 in Cadillac taxes on retiree health plans.[10]

Our solution

The primary purpose of the Affordable Care Act, or ACA, Cadillac tax is to upend generous employer-sponsored health plans. Instead of passing the cost of the Cadillac tax on to their employees, many private-sector employers are already offering less generous plan options to avoid the Cadillac tax entirely. The state of Illinois should follow suit rather than pass on the penalty cost to taxpayers, who are already shouldering the burden for expensive health insurance offered to state employees.

Health-insurance coverage similar to the "silver" tier plan, as defined by the ACA, could provide more modest benefits.

Every dollar the state spends on the Cadillac tax is money that cannot be directed toward actual health-care services for the state's neediest citizens. To ensure that taxpayer resources are directed to only the highest priorities, the state of Illinois should not offer health-insurance options to active employees that could trigger the ObamaCare Cadillac tax.

Should the state continue to offer these plans as an option, state employees should shoulder all of the costs imposed by the Cadillac tax.

Why this works

Illinois taxpayers cannot afford to shoulder the additional cost of the Cadillac tax, especially when these resources do nothing to improve patient care or health outcomes. Since health-care inflation tends to outpace inflation for other goods and services, more and more plans will become subject to this tax in the future. Avoiding this tax altogether or passing any additional costs resulting from the tax on to employees will ensure that Illinois taxpayers are not saddled with these additional costs.

Endnotes

[1] Health Affairs and Robert Wood Johnson Foundation, "Health Policy Brief: Excise tax on 'Cadillac' plans. To slow growing costs and finance and finance expanded coverage, the ACA imposes an excise tax on high-cost health plans to take effect in 2018," Sept. 12, 2013, p. 1 at healthaffairs.org/healthpolicybriefs/brief_pdfs/healthpolicybrief_99.pdf

[2] Ibid.

[3] Lopez Bauman, Naomi, "Budget Solutions 2016: State-employee health insurance: Opportunities for reform," Illinois Policy Institute, Feb. 11, 2105, at illinoispolicy.org/reports/budget-solutions-2016-state-employee-health-insurance-opportunities-for-reform/

[4] Troy, Tevi D. and Wilson, Mark D., "The Impact of the Health Care Excise Tax on U.S. Employees and Employers," American Health Policy Institute, 2014, p. 2 at americanhealthpolicy.org/Content/documents/resources/Excise_Tax_11102014.pdf

[5] Commission on Government Forecasting and Accountability, "FY 2015: Liabilities of the State Employees' Group Health Insurance Program," March 2014, p. 19 at cgfa.ilga.gov/Upload/FY2015GroupInsuranceReport.pdf

[6] Gabriel Roeder Smith & Company, "Illinois State Employees Group Insurance Program, GASB no 45 Actuarial Valuation Report," as of June 30, 2013, p. 4 at cgfa.ilga.gov/Upload/SEGIP_GASB45_2013_Final.pdf

[7] Health Affairs and Robert Wood Johnson Foundation, "Health Policy Brief: Excise tax on 'Cadillac' plans. To slow growing costs and finance and finance expanded coverage, the ACA imposes an excise tax on high-cost health plans to take effect in 2018," Sept. 12, 2013, p. 3 at healthaffairs.org/healthpolicybriefs/brief_pdfs/healthpolicybrief_99.pdf

[8] Author's calculations based on data from the Commission on Government Forecasting and Accountability and Gabriel Roeder Smith & Company. Calculations assume a health cost trend of 5 percent and an impact trend of 5.6 percent. The base cost was $1.7 billion beginning in 2020.

[9] Commission on Government Forecasting and Accountability, "FY 2015: Liabilities of the State Employees' Group Health Insurance Program," March 2014, pp. 8, 15 at cgfa.ilga.gov/Upload/FY2015GroupInsuranceReport.pdf

[10] Author's calculations based on data from the Commission on Government Forecasting and Accountability and Gabriel Roeder Smith & Company. Calculations assume a health cost trend of 5 percent and an impact trend of 5.6 percent. The base cost was $900 million beginning in 2020.