Kibble & Prentice
A USI Company

HEALTH CARE REFORM UPDATE
February 23, 2010

PRESIDENT UNVEILS A REVISED HEALTH CARE REFORM PROPOSAL

President Obama has revealed his revised health care reform proposal on the White House website in anticipation of the upcoming Health Care Summit. The proposal is available at http://www.whitehouse.gov/health-care-meeting. At first read, it appears to follow the previously approved Senate bill with some important concessions to objections raised by House Democrats. The proposal does not appear to address any of the objections raised by Republicans. It is estimated to cost close to $1 trillion over ten years. There is already discussion amongst Washington insiders that the proposal is intended to set the stage for an attempt to push through a full-scale health care reform initiative using a series of political and parliamentary maneuvers, including the reconciliation process in the Senate. Reconciliation, which is reserved for budgetary matters, only requires a simple majority, although it is a complicated procedure that may require 60 votes on certain procedural questions.

Briefly, key differences in the President's proposal from the existing Senate-passed bill include:

- A softening of the tax on so-called "Cadillac Plans," apparently to overcome objections from House Democrats and their supporters in organized labor;
- An increase in the subsidies for lower-income individuals to obtain coverage under the state-based Exchanges that will serve as the marketplace for individuals and small groups to obtain health care coverage;
- Elimination of the special deals offered to certain states in regard to the costs of Medicaid expansion – but with concessions to all of the states that will soften the increased cost;
- Closing of the so-called "donut hole" in the Medicare Part D prescription drug program; and
- A national commission that will have some control over rate increases by insurers – an attempt to provide some "national" flavor to the Exchanges.

These changes will clearly add to the overall cost of health care reform. To help offset these additional costs, the President's proposal includes certain measures that will increase funding for the program, including:

- Increases in the penalties on employers that do not provide health care benefits to their employees if any of their employees receive a subsidy to purchase coverage under an Exchange;

- An extension of the Medicare payroll tax to the investment income of wealthier Americans;

- A modest increase in the amounts that will be paid by the pharmaceutical industry; and

- Expanded cuts in Medicare, both through direct cuts to programs such as Medicare Advantage and by tighter control of rate levels set by the government.

The President's Revised Proposal

The President's proposal strikes a compromise between the previously passed Senate and House versions of health care reform. By adopting a modified version of the Senate bill, the President appears to have taken the public plan option off of the table. At the same time, his proposal for comprehensive and systemic change with a significant price tag is likely to be the subject of much debate in future deliberations on this measure.

Discussed in more detail below are key components of the President's proposal, including items that will impact employer-sponsored health programs.

- **Elimination of special deals on Medicaid expansion.** The proposal eliminates the so-called "Cornhusker Kickback" which exempted Nebraska from the cost impact of Medicaid expansion, as well as certain other special deals. Instead, it offers 100% relief for all states from 2014 through 2017 for the cost of newly- eligible individuals. This level of support phases out to 90% in 2020 and thereafter. The proposal also increases matching funds for those states that have already borne a higher cost through their own Medicaid expansion.

- **Expanding individual subsidies.** The proposal lowers the threshold for the premium credits that will subsidize the purchase of health care insurance for certain lower income individuals and improves cost sharing assistance, moving these provisions closer to the House version. Like the House bill, it also indexes the premium credits for inflation.

- **Easing the tax on "Cadillac Plans."** The President's proposal changes the effective date of the excise tax on high cost plans from 2013 to 2018. The annual premium threshold for all plans is raised from $8,500 for single

coverage to $10,200. For families, the amount is increased from $23,000 to $27,500. These amounts are indexed for inflation and, in the event health costs rise unexpectedly between now and 2018, the thresholds may be adjusted automatically. The proposal also appears to remove premiums associated with dental and vision coverage as potentially taxable benefits. It also permits adjustments for firms where costs are higher due to age or gender and retains the adjustment for high-risk occupations.

- **Tightening the protections for grandfathered plans.** The Senate bill includes certain "grandfathering" provisions to ensure that individuals who like their current coverage can keep it, a key tenet of Obama's health reform goals. Generally, the Senate bill allows existing employer-sponsored programs to be grandfathered until some change to the coverage is made (e.g. a change in the carrier, deductible or cost-sharing). The President's proposal will continue grandfathering with certain conditions. Within months of enactment, the proposal will require that plans cover adult children up to age 26. By 2014, grandfathered plans will be prohibited from imposing annual/lifetime limits and pre-existing condition exclusions and from discriminating in favor of highly compensated individuals. By 2018, grandfathered plans will be required to cover preventive services with no cost sharing.

- **Changes in the penalties for the individual mandate.** Both bills require individuals to obtain health care coverage and will impose penalties on those without coverage once the Exchanges are established (2014 in the Senate bill). The proposal adopts the Senate bill's flat dollar approach, but reduces the penalty amount ($695, as opposed to $750, once the penalty is fully phased in by 2016). The alternative maximum penalty, once fully phased in, is 2.5% based on a percentage of income, as proposed in the House bill. The proposal also adopts the House bill's use of the individual income tax filing threshold to qualify for the exemption from the penalty, as opposed to the Federal poverty level used in the Senate bill.

- **Increases in the employer penalty.** Consistent with the Senate bill, the proposal does not impose a mandate on employers to provide coverage, but does assess penalties if the workers of certain larger employers (more than 50 employees) receive tax-payer funded subsidies under the Exchanges. The proposal appears to increase the penalty imposed on an employer who does not offer health insurance coverage. In this case, if at least one employee receives a premium tax credit, the employer would be assessed a fee of $2,000 per full-time employee. This is an increase from the $750 per full-time employee penalty under the Senate bill, but is about a third less than the penalty contained in the House bill. The proposal provides some relief by allowing the first 30 workers to be subtracted from the total fee assessment. The proposal also removes employees in a waiting period from the

calculation of the penalty, but does maintain the 90-day limit on the length of any waiting period beginning in 2014.[1]

- **Expanded Medicare tax on investment income of high income taxpayers.** The Senate's 0.9% increase in the Medicare payroll tax for high income workers ($200,000/single filer and $250,000/joint filer) is supported by the President. His proposal expands on the Senate's framework and suggests a 2.9% Medicare payroll tax on income from interest, dividends, annuities, royalties, rents and certain other non-passive income.

- **Closing the Part D "Donut Hole".** The proposal provides a $250 rebate to Medicare beneficiaries who hit the donut hole in 2010 (as opposed to provisions in both the House and Senate bills that would have raised the threshold for the donut hole by $500). The donut hole is the gap in coverage for out-of-pocket spending between $2,830 and $4,550. The gap in coverage is phased out by 2020.

- **Increased assistance for community health centers.** The proposal increases the Senate bill's funding of community health centers from $7 billion to $11 billion, closely approaching the $12 billion in the House bill.

- **Federal oversight of insurance premium increases.** The Senate bill provides for review of insurer rating practices. The President's proposal calls for the establishment of a national Health Insurance Rate Authority to monitor the rate review process in the Senate bill. This proposal will likely involve the new authority in rate review enforcement and rate setting or rate increase limitations.

- **CLASS Act:** Both the House and Senate bills include the Community Living Assistance Services and Support Act (CLASS Act). This is a voluntary, privately funded, long-term care services insurance program. Employees are offered a voluntary payroll deduction to purchase coverage that will provide a cash benefit should the employee become disabled. The President proposes strengthening the provisions of the Senate version of this program to protect its financial viability over the long term.

What's Next

The President's proposal is sure to be the centerpiece for debate at the upcoming Health Reform Summit. Whether it is truly intended to be a catalyst for bipartisan debate or a clever political move that will put opponents of comprehensive health care reform on the defensive is yet to be seen. Already, there is significant

[1] There does not appear to be a change to the current penalties under the Senate bill when an employer with more than 50 employees provides health insurance coverage that is not affordable. In this case, if a full-time employee receives a premium tax credit under an Exchange, the employer may be assessed the lesser of $3,000 for each employee receiving the tax credit or $750 for each full-time employee. In this scenario, it is not clear whether an employer may subtract the first 30 workers from the penalty payment calculation. Additional guidance is needed.

discussion of post-Summit game plans that will expedite the proposal through Congress, perhaps by the end of March. This scenario would involve a combination of the already passed Senate bill and a "sidecar" bill that contains the changes to the Senate bill necessary to conform to the President's proposal. The sidecar bill would be fast-tracked in the House as a budget bill and would be sent to the Senate for passage under the Senate reconciliation process for budget matters. If the bill is approved by the Senate Parliamentarian (the official interpreter of Senate rules and parliamentary procedure), it would then proceed to a simple majority vote. If passed, the House would then vote to approve the original Senate bill and the President would then sign both measures together, resulting in a comprehensive health care reform package that looks like the President's new proposed program.

There are a great many variables in this scenario. The reconciliation process in the Senate is procedurally complicated. Also, the sidecar would need to attract enough support in the House to accomplish quick passage. Some House Democrats may have concerns over how a "yes" vote on such a large overall package will play to their constituents in the upcoming November elections. The same factors could affect the thinking of some Senators, as well. The use of reconciliation in the Senate to accomplish such a large reform initiative will most likely be a point of contention.

Attention will now turn to the televised Summit on February 25th. What happens there and how those events are perceived by the nation and evaluated by the political pundits will largely determine the future course of events for health care reform. We will continue to monitor these developments and provide you with timely updates.

Disclaimer Statement:
These materials are produced by Kibble & Prentice for educational purposes only. Certain information contained in these materials is considered proprietary information created by Kibble & Prentice and/or their licensed and appointed insurance carriers. Such information shall not be used in any way, directly or indirectly, detrimental to Kibble & Prentice and/or their affiliates.

Neither Kibble & Prentice nor any of its respective representatives or advisors has made or makes any representation or warranty, expressed or implied, as to the accuracy or completeness of these materials. Neither Kibble & Prentice nor their respective representatives or advisors shall have any liability resulting from the use of these Materials or any errors or omission therein. These materials provide general information for the use of our clients, potential clients, or that of our clients' legal and tax advisors.

IRS Circular 230 Disclosure: Kibble & Prentice Holding Co. and its affiliates do not provide tax advice. Accordingly, any discussion of U.S. tax matters contained herein (including any attachments) is not intended or written to be used, and cannot be used, in connection with the promotion, marketing or recommendation by anyone unaffiliated with Kibble & Prentice Holding Co. of any of the matters addressed herein or for the purpose of avoiding U.S. tax-related penalties. Also, the information contained in this document should not be construed as medical or legal advice.

Copyright © 2010 Kibble & Prentice Holding Company. All Rights Reserved.