Beginning in 2014, the Patient Protection and Affordable Care Act (PPACA) imposes a health insurance tax (HIT) on the fully-insured market that serves most small-business employers and those who purchase policies individually.

**Insurers will write the checks, but consumers and small businesses will bear the burden.** Section 9010 of PPACA and Section 1406 of the Reconciliation Act (which modified PPACA) refer to the HIT an “annual fee on health insurers.” Formally, then, insurers will write the checks to cover the HIT.

However, the Congressional Budget Office (CBO) advised Congress that the HIT “would be largely passed through to consumers in the form of higher premiums for private coverage.” This observation has been confirmed by statements from the Office of the Actuary at the Centers for Medicare and Medicaid Services (CMS) and by the Joint Committee on Taxation (JCT) of Congress.

The HIT will fall on most of the country’s 5.8 million small businesses and 15 million self-employed individuals. But the tax mostly bypasses big businesses, unions, and governments. CBO said, “Self-insured plans would be mostly exempt from the fee on health insurance providers, and since large firms are more likely to self-insure, that fee would result in smaller percentage increases in average premiums for large firms than it would for small firms and for nongroup coverage.”

The HIT raises premiums for small businesses, but not for big businesses. This will reduce employment and wages in the small-business sector. NFIB forecasts that the HIT will reduce private sector employment by 146,000 to 262,000 jobs in 2021, with 59 percent of those losses falling on small business.

The HIT has an unusual structure. The HIT is a fixed-dollar amount distributed across health insurance providers: $8 billion in 2014, $11.3 billion in 2015-2016, $13.9 billion in 2017, and $14.3 billion in 2018. After 2018, the HIT rises according to an index based on net premium growth.

The total HIT obligation is divided among insurers according to a formula based on each insurer’s net premiums. An insurer’s tax base equals its net premiums minus the first $25 million and 50% of the second $25 million. Nationally, an insurer’s HIT equals its portion of the total base times the total HIT for that year.

For non-profit insurers, only 50% of the net premiums are taxed. Plans that receive more than 80% of their premiums from government programs for the poor, elderly, and disabled under titles XVIII, XIX, and XXI of the Social Security Act are exempt altogether.

If some businesses drop coverage or switch from fully-insured to self-insured, those remaining in the fully-insured market will have to absorb the tax bill of those firms who have left.

In addition, the HIT includes a tax on a tax. Insurers will pass the HIT along to purchasers as higher premiums. In turn, those premium increases will enter into the index and raise the tax in later years.

The HIT is one of the biggest taxes in PPACA. Over the first decade (2014-2023), this provision increases taxes by $102 billion. During the second decade, the total tax impact will likely be $200-300 billion.

The HIT’s full magnitude will become apparent in the second decade (2021-2030), with ten full years of a premium-indexed, fully-implemented HIT. The magnitude is difficult to forecast, but $200-300 billion is plausible. (See the 6/14/11 entry here.) The exact amount depends both on how rapidly premiums rise and on how the law’s arcane index translates those premium increases into HIT increases.
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As Douglas Holtz-Eakin explained, the corporate income tax will amplify the HIT’s total impact on purchasers by an extra 54%. Example: (1) if an insurer responds to a $1,000,000 HIT by raising premiums by $1,000,000, it will incur an extra $350,000 in corporate income taxes (35% x $1,000,000). Its after-tax profits will drop by $350,000. (2) If, instead, the insurer raises purchasers’ premiums by $1,538,462, the corporate tax will rise by $538,462 (=35% x $1,538,462) and the insurer will have completely offset the HIT. Thus, Holtz-Eakin argues, an $87.4 billion first-decade HIT will likely result in premium increases of $134.6 billion (=154% x $87.4 billion) to small businesses and individuals.

A Milliman report noted that the HIT will also produce liabilities for state government budgets. Medicaid managed care programs generally purchase insurance in the fully-insured market, so they, too, will have to pay the HIT. Including the corporate income tax interaction described above, Milliman estimates that the HIT will raise Medicaid managed care premiums by 1.5%-1.6% nationwide, with some states’ costs rising by 2.5%.

NFIB is leading a coalition to repeal the Health Insurance Tax. You can find more information on the HIT at the coalition’s website at www.StopTheHIT.com.