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POLICY BRIEF

Proposed Regulations Could Limit Access to Affordable Health Coverage for Workers' Children and Family Members

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Key Findings

The Patient Protection and Affordable Care Act (ACA) is designed to offer premium subsidies to help eligible individuals and their families purchase insurance coverage when affordable job-based coverage is not available. However, the law is unclear on how this affordability protection is applied in those instances where self-only coverage offered by an employer is affordable but family coverage is not. Regulations recently proposed by the Department of the Treasury would make family members ineligible for subsidized coverage in the exchange if an employee is offered affordable self-only coverage by an employer, even if family coverage is unaffordable.[1] This could have significant financial consequences for low- and moderate- income families that fall in this gap.[2] Using an alternative interpretation of the law could allow the entire family to enter the exchange when family coverage is unaffordable, which would broaden access to coverage. However, this option has been cited as cost prohibitive.[3] In this brief we consider a middle ground alternative that would base eligibility for the individual worker on the cost of self-only coverage, but would use the additional cost to the employee for family coverage as the basis for determining affordability and eligibility for subsidies for the remaining family members. We find that:

- **Under the middle ground alternative scenario an additional 144,000 Californians would qualify for and use premium subsidies in the California Health Benefit Exchange, half of whom are children.**

- **Less than 1 percent of those with employer-based coverage would move to subsidized coverage in the California Health Benefit Exchange as a result of having unaffordable coverage on the job.**

Background

To improve access to health insurance for low- and middle-income families, starting in 2014, under the ACA, subsidies will be provided to workers earning less than 400 percent of the federal poverty level (currently $89,400 for a family of four) to buy health insurance through state-run health insurance exchanges. Individuals will not be eligible for these premium subsidies if they are offered "minimum essential coverage" by their employer that costs less than 9.5 percent of the employee's household income. Workers who are offered insurance that exceeds this affordability threshold, however, will be eligible for a subsidy to purchase insurance in their state exchange.

The language of the ACA is unclear on whether family members of employees would be eligible for premium subsidies in cases where an employee is offered *affordable self-only coverage* (i.e., the individual premium share is under 9.5 percent of household income) but *unaffordable family coverage.* Draft regulations released in August 2011 by the Department of the Treasury propose that:

> "…for both employees and others (such as spouses or dependents) who are eligible to enroll in employer-sponsored coverage by reason of their relationship to an employee (related individuals), the coverage is unaffordable if the required contribution for "self-only" coverage (as opposed to family coverage or other coverage applicable to multiple individuals) exceeds 9.5 percent of household income."[4]

In other words, under the Treasury's proposed interpretation, if self-only coverage costs less than 9.5 percent of household income, then both employees and their family members are ineligible for premium subsidies in the health insurance exchanges—regardless of whether or not the cost of family coverage exceeds the 9.5 percent threshold for affordability.

Treasury takes a different interpretation of the affordability protections as they relate to the individual mandate. Here they state that future regulations are "expected to provide that the affordability test for purposes of applying the individual responsibility requirement to related individuals is based on the employee's required contribution for employer-sponsored family coverage."[5] Thus, while family members would not be eligible for subsidized coverage in the exchange even if the cost of family coverage exceeds the affordability threshold, they would be exempted from the individual mandate.

In this paper, we compare the impacts on access to affordable coverage and subsidy costs of the draft Treasury regulations and an alternative interpretation of the statute that separates the affordability determination for the worker and their family members. In those instances where an employee's self-only coverage is affordable but family coverage is unaffordable, the employee would not be eligible for subsidies in the exchange, but the family members would be eligible. This alternative interpretation provides for a compromise between the proposed regulations and a third possible interpretation that would allow employees as well as family members to enroll in subsidized coverage in the exchange if family coverage is unaffordable, regardless of whether or not self-only coverage is affordable.

While legal analysis is outside of the scope of this paper, the Center on Budget and Policy Priorities suggests that this middle ground interpretation reflects a better reading of the statute and is consistent with Congress's intent.[6]

Enrollment in Exchange Differs Slightly Under Alternate Affordability Interpretations

Using a micro-simulation developed by UC Berkeley and UCLA to estimate the impact of health care reforms on California, we analyzed the impact of two different interpretations of affordability:

SCENARIO 1:

In Scenario 1, eligibility for subsidies in the health care exchange, for both employees and their families, is based on the cost of self-only coverage. In those instances where self-only coverage is less than 9.5 percent of household income, neither the employee nor his or her family members will be eligible for subsidies in the exchange, regardless of the cost of family coverage. Scenario 1 is based on the Treasury's proposed regulations.

SCENARIO 2:

Scenario 2 is called the "middle ground alternative" and is based on the proposed regulations for the individual mandate. In Scenario 2, subsidy eligibility for employees would be based on the affordability of self-only coverage, and subsidy eligibility for additional family members would be based on the cost of family coverage.

If the cost of self-only coverage is less than 9.5 percent of household income, but the cost of family coverage is greater than 9.5 percent of household income, then family members—but not the employees themselves—would be eligible for subsidized coverage in the exchange.

Scenario 2 is still narrower than the broadest interpretation, which would allow employees, along with family members, to qualify for exchange subsidies when family coverage is unaffordable, even if self-only coverage is affordable.

Our results indicate that the number of Californians who would obtain subsidized coverage through the health care exchange would be less than 10 percent of those currently insured through job-based coverage, under either of these scenarios. Also, less than 1 percent of those covered through an employer would move to subsidized exchange coverage in California. This finding is consistent regardless of whether or not family members offered unaffordable job-based coverage are allowed access to subsidized coverage in the exchange.

Under the proposed regulations (Scenario 1), 1.46 million Californians would have subsidized coverage in the exchange in 2019 (Table 1, page 4). Under Scenario 2, this would increase by 144,000 to 1.60 million

Table 1. Comparison of Alternative Affordability Interpretations: Number of Californians Receiving Subsidies in Exchange, 2019

	Scenario 1: Proposed Regulations	Scenario 2: Middle Ground Alternative
Total population, ages 0–64 years	35,812,000	35,812,000
Total population in subsidized exchange	1,456,000	1,600,000
Percentage in the subsidized exchange	4.1%	4.5%

Source: UCB–UCLA Micro-simulation model.

Scenario 1: Workers' and family members' exchange eligibility based on cost of self-only coverage.

Scenario 2: Workers' exchange eligibility based on cost of self-only coverage, family members' eligibility based on cost of family coverage.

in 2019, a 10 percent increase over Scenario 1. Of the 144,000 additional family members with subsidized coverage in the exchange in California under Scenario 2, we estimate that 73,000 (51 percent) would be children.

We also found that only a small group of people are projected to move from job-based coverage to the subsidized health care exchange in either scenario. The vast majority of Californians receiving subsidized coverage in the exchange in 2019 would have been previously uninsured or enrolled in coverage through the individual market.

Under Scenario 1, we find that only 46,000 of the 19.3 million California employees and family members with job-based coverage would be eligible for the exchange, would have a financial advantage in switching to the exchange, and would ultimately chose to make the switch. Many of those who are eligible for subsidized coverage in the exchange would receive no financial benefit from switching, due to the difference in tax treatment and lower benefit levels offered in the subsidized exchange compared to employer-based coverage. Under Scenario 2, we estimate that 112,000 Californians would drop job-based coverage and move to the subsidized exchange (Table 2, page 5).

Further consideration of actual processes of employer and employee decision making suggests that our estimates of the differences between the two scenarios may be higher than what will be observed in practice. Our micro-simulation model is not able to take into account other important behaviors that could reduce the difference in outcomes between the two scenarios. For example, we would expect some sorting between workers and firms based on health needs. If workers are worse off taking a job with an employer that offers unaffordable family coverage, they may be less likely to seek out employment with firms that provide insurance benefits where much of the premium share is passed on to the worker. While there are serious limitations in job-mobility for low-wage workers, sorting can be expected to reduce the coverage differences between the two options.

Table 2. Comparison of Alternative Affordability Interpretations: Number of Californians Switching from Job-based Coverage to Subsidized Exchange, 2019

	Scenario 1: Proposed Regulations	Scenario 2: Middle Ground Alternative
Total population with job-based coverage whose employers maintain coverage, ages 0–64 years	19,320,000	19,313,000
Total population whose employers maintain coverage but who switch to the subsidized exchange	46,000	112,000
Percentage switching to the subsidized exchange	0.2%	0.6%

Source: UCB–UCLA Micro-simulation model.

Scenario 1: Workers' and family members' exchange eligibility based on cost of self-only coverage.

Scenario 2: Workers' exchange eligibility based on cost of self-only coverage, family members' eligibility based on cost of family coverage.

Exchange Enrollees are Younger and Higher Income Under the Middle Ground Alternative

We analyzed how the age and income demographics of the exchange population would vary under the alternative interpretations. Individuals expected to shift into the exchange under Scenario 2 would be younger on average than those in the exchange under Scenario 1: In the first scenario, 0 to 18 year-olds would make up 9.6 percent of the total exchange population, but those under 18 years would make up more than half (50.9 percent) of the additional exchange participants under Scenario 2 (Table 3, page 6). These children are in families with incomes between 250 percent and 400 percent of the federal poverty level (FPL) and do not qualify for Healthy Families (California's Children's Health Insurance Program, or CHIP). Overall, the group that would shift into the exchange under Scenario 2 is more likely to be between 200 percent and 400 percent FPL (65 percent) than the exchange population as a whole under Scenario 1 (56.3 percent). The combined effect of lower age and higher income would result in both a significantly lower average cost for health insurance and lower average subsidies than in the exchange overall.

Other Researchers' Recent Estimates of the Affordability of Alternative Models Were Too High

Our estimates of the amount of switching from job-based coverage to coverage in the exchange are substantially lower than another recent estimate from Burkhauser, Lyons, and Simmons (2011a), who analyzed the impact of various affordability scenarios on coverage on a national level. Their analysis is based on a broader interpretation of affordability than the ones we examine here. In their scenarios, the individual employee and family members are all eligible for coverage in the exchange if family coverage costs more than 9.5 percent of income, even if self-only coverage is less than 9.5 percent of income. This is the "third possible interpretation" we referred to above (page 2), and it casts a far wider net than either Scenario 1 or Scenario 2. Burkhauser et al. argue that employers would have an incentive to increase

Table 3. Age Profile of Exchange Population under Alternative Scenarios, 2019

Age	Total under Scenario 1	Move from ESI to Exchange under Scenario 2
0–18 years	9.6%	50.9%
19–29 years	26.0%	14.9%
30–44 years	25.2%	15.2%
45–54 years	20.3%	13.4%
55–64 years	18.9%	5.6%
Total	100.0%	100.0%

Source: UCB–UCLA Micro-simulation model.
Scenario 1: Workers' and family members' exchange eligibility based on cost of self-only coverage.
Scenario 2: Workers' exchange eligibility based on cost of self-only coverage, family members' eligibility based on cost of family coverage.

employee premium contributions for family coverage to enable their lower-wage employers to receive subsidized coverage in the exchange, while their higher-wage employees continue to access family coverage through the employer using pre-tax dollars. Their estimates presume all employers would adjust their compensation and benefit plans in this manner.

It is highly unlikely that all employers would shift their cost sharing as dramatically as projected by Burkhauser et al. Their analysis assumes that employers would maintain the same spending on compensation for each employee, but shift a greater share into wages for those who drop coverage and move into the exchange. In practice this may be difficult for many employers to do, particularly in the short- to medium-run. Employers are not likely to set different direct pay rates for workers with families and workers without families (even as they effectively do so currently through benefits). Employers may also be reluctant to create incentives that would cause healthier workers to leave job-based coverage. As the authors note, if employers are not able to take the savings that accrue from not paying for some employees' health insurance, and pass those savings onto the employees in the form of higher wages, it would reduce the incentive to opt for coverage in the exchange.

The creation of the State Children's Health Insurance Programs (SCHIP) in 1997 to 1999 offers a relevant point of comparison. With access to health insurance available for children in families with incomes as high as 250 percent of FPL in certain states, employers faced a similar incentive to shift a greater share of the cost for children's coverage onto employees in order to encourage the employees to drop their children from their health insurance policy and enroll them in CHIP instead. Research by several economists indicated that firms did not stop offering coverage to their employees, but may have been more likely to increase the employee share of premiums for family coverage. However, one study found that the difference in take-up due to this extra cost, while statistically significant, was fairly small. In the simulation exercise, in firms where 20 percent of the employees were eligible for public programs only 1 percent of workers dropped their CHIP-eligible children from employer-based coverage. Even among

firms with a vast majority (70 percent) of employees who were eligible for public programs, only 6 percent of workers dropped coverage for their children and enrolled them in CHIP.[7]

To examine this issue, we tested a maximum cost-shift scenario (Scenario 3) in our micro-simulation model. Scenario 3 is the same as Scenario 2, except that it assumes that all employers increase premium cost-sharing for family coverage to 50 percent and decrease cost-sharing of single coverage to 0 percent.

We found that the number of Californians with subsidized coverage in the exchange in 2019 would increase by an additional 262,000 to 1.86 million under Scenario 3. An estimated 140,000 additional Californians who currently have job-based coverage through a parent or spouse would be projected to shift to the subsidized exchange.

Not only would the level of coverage vary between Scenarios 2 and 3, but the average subsidy amount would also vary because the composition of exchange enrollees would differ under each scenario. An estimated 50.9 percent of the individuals who would move into the exchange under Scenario 2 and 54.2 percent who would move into the exchange under Scenario 3 are children in families between 250 percent and 400 percent FPL. As a result, the additional exchange population is both younger and higher income than the average exchange population as a whole, and would thus require significantly smaller subsidies on average. We estimate that the average annual subsidy for additional participants under Scenario 2 would be $2,600 per person in 2019. Those who would move to the exchange under Scenario 3, with employers shifting the cost of family premiums onto workers, would qualify for even lower subsidies on average: $1,700 per person in 2019.

We estimate that in 2019 the cost difference of the alternative interpretations of affordability would range from $380 million in Scenario 2 to $820 million in Scenario 3, depending on the degree of the employer shift in premium costs. This range is well below the potential costs projected by Burkhauser et al. (2011a).

The differences between our estimates and those of Burkhauser et al. are due to the combination of a more modest interpretation of affordability and the application of more realistic behavioral models to employer and employee decision making:

- Burkhauser et al. assume that both employees and their family members would be eligible for coverage in the exchange in instances where the cost of family coverage is greater than 9.5 percent of income; we assume that in these cases individual employees would not be eligible for subsidized coverage in the exchange, but their family members would be.

- Burkhauser et al. note that differences between the quality of coverage in the exchange and coverage offered on the job will affect employees' decisions, but do not include these differences in their cost calculation. The average actuarial value for employer-sponsored plans is 83 percent[8] compared to 70 percent for subsidized exchange plans, with greater cost-sharing subsidies for people with lower incomes. The difference in value is taken into account in our employee behavioral model.

- Burkhauser et al. assume individuals will switch away from job-based coverage regardless of the magnitude of the savings. We model switching as a function of the magnitude of the savings.

Importantly, in another version of the same paper, Burkhauser et al. (2011b) note that their analysis is "stylized" and cannot be compared to estimates from the Congressional Budget Office or other micro-simulation models because it does not allow for other behavioral changes.[9]

Conclusion

We tested the impact of alternative proposals for the affordability standard using our micro-simulation model of the California insurance market under health reform. We found that:

- Allowing family members without affordable job-based coverage access to subsidized coverage in the exchange would increase enrollment in the exchange by an amount equal to less than 1 percent of the non-elderly California population.

- Half of those excluded from subsidies under the currently proposed Treasury regulations are children.

- Only a small portion of the population would move from job-based coverage to subsidized exchange coverage, regardless of whether or not family members who are offered unaffordable job-based coverage are allowed access to subsidized coverage in the exchange.

- Individuals who would be expected to shift from job-based coverage under the middle ground alternative of affordability would be younger and have higher income on average than the exchange as a whole, improving the risk pool.

California contains 12 percent of the U.S. population under age 65. If our estimates for California hold for the nation as a whole, the narrow interpretation of affordability used in Treasury's draft regulations could have consequences for more than one million people nationwide. A greater share of children would be affected in those states with lower eligibility levels for state Children's Health Insurance Programs (CHIP), while a lower share of children would be affected in those states with higher eligibility levels for CHIP.

To ensure that the final rule carries out the coverage goals of the ACA and does not create undue financial burdens on working families, we recommend that an employee's family members be eligible for subsidized coverage in the exchange if the cost to the employee of covering the family is greater than 9.5 percent of household income and the family members do not have offers of minimum essential coverage elsewhere, as in our Scenario 2 above.

This recommendation is consistent with a plain language interpretation of the Affordable Care Act, and would provide affordable coverage to an estimated 144,000 Californians, nearly half of whom are children. Our analysis shows that the cost of implementing this recommendation would be significantly less than previous analyses suggest.

Appendix: Overview of Micro-Simulation Model

To test how alternative affordability interpretations would impact exchange eligibility in California, we used our Micro-Simulation Model for Consumer Health Spending and Affordability. The model was developed by the UC Berkeley Center for Labor Research and Education and the UCLA Center for Health Policy Research, with funding from The California Endowment. It is currently being used in California to inform decisions by the California Health Benefit Exchange and to estimate the impact of the ACA on a variety of demographic groups, employers, and employees.

The micro-simulation model is built on three core datasets: The Medical Expenditure Panel Survey Household Component (MEPS-HC), the California Health Interview Survey (CHIS), and the California Employer Health Benefits Survey (CEHBS). Use of CHIS and the CEHBS allowed for adjustments to the MEPS that provide a California-specific model of the impact of the ACA. The model uses the Confidential CHIS file to integrate undocumented status and legal residency for individuals. This allows for individual-level behavioral predictions for the undocumented population, rather than adjusting for them in aggregate based on existing results, as has been done in other modeling efforts nationwide.

The model reweights respondents in the MEPS-HC using the CHIS data to represent California's population. The respondents are then separated into workers and their dependents/spouses. The workers are matched to synthetic firms from the CEHBS based upon wage distribution, firm size, and other characteristics. These synthetic firms then choose to participate in different aspects of the ACA, such as taking up coverage or dropping coverage. These decisions, once made by the firm and linked to each employee and their families, allow for individual probabilities to be assigned for insurance choices depending on family characteristics such as household income, availability of other coverage options, and documentation status.

Endnotes

[1] Health Insurance Premium Tax Credit, Treasury REG-131491-10, 76 Fed. Reg. at 50935 (proposed August 17, 2011) (to be codified at 26 C.F.R. pt. 1).

[2] Larry Levitt and Gary Claxton, "Measuring the Affordability of Employer Health Coverage," The Henry J. Kaiser Family Foundation, *Notes on Health Insurance and Reform,* August 24, 2011, http://healthreform.kff.org/notes-on-health-insurance-and-reform/2011/august/measuring-the-affordability-of-employer-health-coverage.aspx (accessed December 10, 2011).

[3] Richard Burkhauser, Sean Lyons, and Kosali Simon, "An Offer You Can't Refuse: Estimating the Coverage Effects of the 2010 Affordable Care Act," Employment Policies Institute, July 2011.

[4] Treasury REG-131491-10 at 50935.

[5] Treasury REG-131491-10 at 50935.

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[9] Richard Burkhauser, Sean Lyon, and Kosali Simon, "The Importance of the Meaning and Measurement of 'Affordable' in the Affordable Care Act," NBER Working Paper No. 17279, August 2011.

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