In this issue:

Hurdles ahead as Ways and Means approves PPACA repeal-and-replacement bill

House Republican taxwriters this week advanced the revenue portion of legislation intended to repeal major pieces of the Patient Protection and Affordable Care Act of 2010 (PPACA) and replace it with a system aimed at facilitating the purchase of health insurance on the individual market through refundable tax credits and liberalized rules for tax-favored health savings accounts (HSAs).

The Ways and Means package was approved strictly along party lines in the early hours of March 9 following a lengthy mark-up punctuated by debate and roll call votes on dozens of Democratic "message" amendments that were generally rejected as nongermane.

The revenue provisions will ultimately be merged with nontax repeal-and-replace legislation approved by the House Energy and Commerce Committee (also on March 9) and congressional leaders plan to move the combined bill under budget reconciliation rules that would allow it to be passed in the House and Senate without the support of Democrats, who have been and are expected to remain united in opposition.

But the plan, formally known as the American Health Care Act (AHCA), faces procedural and political hurdles. Procedurally, GOP leaders currently lack critical information from the Congressional Budget Office (CBO) that will help determine if the plan complies with budget reconciliation rules. Politically, backers of the plan will have to find a way to address complaints from conservative Republicans in both chambers who believe that it too closely resembles the law they want to eliminate and from more moderate Republican lawmakers who are concerned about changes to Medicaid and the impact the plan will have on those who obtained insurance coverage through the Affordable Care Act.

Most PPACA tax provisions repealed

As approved by the Ways and Means Committee, the plan would effectively repeal the PPACA's individual and employer mandates by reducing the penalty for noncompliance to zero for months after December 31, 2015. However, a new rule would require insurance companies to impose a surcharge on policy premiums of up to 30 percent in the case of individuals who fail to maintain continuous coverage over a specified timeframe.

Business provisions: The AHCA also would repeal most of the business taxes enacted under the Affordable Care Act, generally effective for months beginning after December 31, 2017. These include the:

- Annual fee on US health insurance providers allocated based on net premiums for US health risks;
- Annual fee on manufacturers and importers of branded drugs;
- 2.3 percent excise tax on manufacturers and importers of certain medical devices; and
- The $500,000 deduction limitation on taxable remuneration to officers, employees, directors, and service providers of covered health insurance providers.

The measure also would reinstate the deduction for expenses allocable to the Medicare Part D subsidy, which was eliminated under the PPACA.

Individual provisions: On the individual side, the AHCA would eliminate the:

- 3.8 percent Medicare contribution on certain unearned income of individuals with adjusted gross income over $250,000 for joint filers ($200,000 for single filers);
- Additional 0.9 percent Medicare hospital insurance tax on wages over $250,000 for joint filers ($200,000 for single filers);
- Increased floor (10 percent of adjusted gross income) for claiming the itemized deduction for medical expenses;
- 10 percent excise tax on indoor tanning services;
- So-called "medicine cabinet tax," which provides that the purchase of over-the-counter drugs is not a qualified expense for purposes of rules governing HSAs and flexible spending accounts;
- Increased (20 percent) penalty for nonqualified distributions from an HSA or an Archer medical savings account; and
- The $2,500 limitation (indexed) on annual salary-reduction contributions to health flexible spending accounts in cafeteria plans.

Repeal of these provisions generally would be effective for months after December 31, 2017.

Delayed Cadillac tax: The AHCA would retain the so-called "Cadillac" tax – a 40 percent excise tax levied at the insurance company level on employer-provided plans that exceed a certain premium threshold. Under current law, implementation of the tax is delayed until 2020. The AHCA further delays implementation until 2025.

An earlier draft bill that was circulating in the tax community late last month called for repealing the Cadillac tax and replacing it with a cap on the tax exclusion for employer-provided health insurance – a proposal that a number of lawmakers found problematic. (For prior coverage, see *Tax News & Views*, Vol. 18, No. 8, Mar. 3, 2017.)
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170303_1.html

Economic substance doctrine remains: One Affordable Care Act revenue raiser left untouched in the AHCA is the "economic substance" doctrine, codified in section 7701(o), which generally requires taxpayers to show that a transaction changed their economic position in a meaningful way apart from the federal income tax effects and that they had a substantial nontax business purpose for entering into a transaction. It also imposes a strict liability penalty on understatements attributable to transactions determined to lack economic substance. (The penalty varies depending on whether or not the transaction was disclosed.)

The economic substance doctrine was retained largely at the behest of Senate Finance Committee member Charles Grassley, R-Iowa, who was a prime mover in getting it enacted into law. Grassley reportedly told congressional GOP leaders he would not support a PPACA repeal package that eliminated the provision.

Incentives to purchase insurance

The AHCA would create a system of refundable, age-adjusted credits to replace the Affordable Care Act's premium assistance credits for low-income households. Under the AHCA, individuals not insured by an employer or government program (such as Medicare or Medicaid) would receive a monthly credit at an annualized rate ranging from $2,000 (for eligible individuals under 30), increasing by $500 for every 10 years of age, up to $4,000 (for individuals over 60). The maximum family credit would be $14,000 per year, calculated taking into account the five oldest credit-eligible family members.

The credit amount would begin to phase out for individuals earning over $75,000 and couples earning over $150,000. (The refundable credit included in the prior draft bill did not include an income-based phase-out, an omission that led some lawmakers to object that the credit would be available to wealthy individuals.)

The credit would be paid in advance on a monthly basis to taxpayers so that they could then use it to buy whatever insurance they like. (Rules for administering the credit have yet to be developed.)

The credit program would take effect on January 1, 2020.

HSA enhancements: Several provisions would expand access to and increase the flexibility of HSAs – tax-preferred savings accounts which, when used in conjunction with a high-deductible health insurance plan, allow individuals to pay for qualifying out-of-pocket health care expenses "using tax-free dollars." These include:

- Increasing the maximum HSA contribution limit to the combined amount of the plan's deductible and out-of-pocket contribution requirement;
- Allowing both spouses to make catch-up contributions to the same HSA; and
- Providing an administrative fix to allow certain expenses incurred after a taxpayer purchases an eligible high-deductible insurance plan, but before the taxpayer establishes an HSA, to be treated as eligible expenses under the HSA.

These provisions generally would take effect after December 31, 2017.

A side-by-side comparison of tax provisions in the PPACA and the AHCA is available from Deloitte Tax LLP.
URL: http://newsletters.usdbriefs.com/2017/Tax/TNV/170310_1suppA.pdf

Cost savings through Medicaid changes

The Joint Committee on Taxation staff, estimates that the AHCA's tax provisions – repealing the Affordable Care Act revenue offsets, adding the new refundable tax credit, and enhancing the HSA rules – would reduce federal receipts by a total of nearly $600 billion over 10 years. The price tag prompted Ways and Means Democrats to criticize the proposal during the mark-up as a tax cut for the large businesses and the wealthy – a characterization Republicans on the panel rejected.

Cost estimates for repeal of the individual and employer mandates and certain other provisions will be provided by the Congressional Budget Office. Democrats at the Ways and Means mark-up repeatedly complained that it was not appropriate to consider the AHCA without a complete score from the CBO and unsuccessfully offered amendments that would have delayed further action on the bill until CBO estimates became available.

Although the Ways and Means package does not include new tax offsets, it would achieve some cost savings by freezing new enrollment under the Affordable Care Act's Medicaid expansion (which 31 states accepted, including a number with Republican governors) after 2019. For non-expansion beneficiaries, beginning in 2020 the government would institute a Medicaid policy known as "per capita caps" – where the federal share of Medicaid spending in a particular state would not be open-ended, but rather limited to a set dollar amount based on that state's Medicaid population.

CBO score could be critical to AHCA's future

The fact that the AHCA components put forward by the Ways and Means and Energy and Commerce committees have not yet received a cost estimate from the CBO could prove critical in determining whether the plan can be advanced under the budget reconciliation process.

Provided certain strict budgetary and procedural rules are met, legislation moved under reconciliation can be passed with a simple majority in both chambers, making it a potentially powerful tool for Republicans, who control 52 seats in the Senate – 8 shy of the 60 votes normally required to advance legislation in that chamber under regular order.

Byrd Rule restrictions: Among the procedural and budgetary rules governing the reconciliation process – sometimes collectively referred to as "Byrd Rules," named after the late Sen. Robert Byrd, D-W.Va. – are a prohibition against legislation that would increase the deficit in any year beyond the budget window (which is typically 10 years) and a separate rule designed to block provisions that are deemed to have no effect on the federal budget, or whose effect is "merely incidental" to the underlying policy.

These two budgetary restrictions on the reconciliation process have been codified into law and apply on a provision-by-provision basis. They are enforced through points of order, which can be waived in the Senate with a three-fifths majority (that is, generally 60 votes); but because Democrats are not expected to lend any support to the PPACA repeal-and-replace effort, compliance with these rules is in essence a prerequisite for passage of the AHCA.

But without a CBO assessment of the AHCA's projected budgetary effects it remains difficult to know whether the entire bill could be successfully moved under the fast-track procedural protections.

For instance, unlike a previous PPACA repeal bill that congressional Republicans introduced in 2015 and successfully moved under reconciliation in early 2016 (and which President Obama subsequently vetoed), the AHCA also includes significant "replace" provisions in the form of new refundable tax credits and expanded HSA rules. These new provisions could make compliance with the Byrd Rule prohibition against long-term deficit increases more difficult, at least relative to the earlier bill which was focused solely on repeal. (For coverage of the prior repeal bill, see *Tax News & Views*, Vol. 17, No. 2, Jan. 8, 2016.)
URL: http://newsletters.usdbriefs.com/2016/Tax/TNV/160108_1.html

The AHCA also includes new insurance market reforms – for example, a requirement that insurers assess a surcharge on individuals who do not maintain continuous coverage, and a relaxation of current law limits on how much older Americans can be charged for health coverage relative to their younger peers – and it is unclear whether the CBO would determine them to have an impact on the federal budget.

For his part, House Speaker Paul Ryan, R-Wis., expressed confidence March 9 that the legislation is fully compliant with the rules of budget reconciliation – while also acknowledging some of the policy trade-offs that come with the process.

"Members realize this is a once in a lifetime opportunity, so naturally people are saying, 'I'd love to have this in there,' and what people are learning is, this reconciliation stuff is pretty tight," Ryan said. "[T]his bill is written so that it can't be filibustered."

Coverage numbers could cause political concerns: The forthcoming analysis from the CBO will likely also include projections of how many individuals may gain or lose health coverage under the plan – statistics that could significantly impact the politics of moving the bill through Congress. (Ways and Means Committee Democrats repeatedly raised the issue of coverage levels under the AHCA as a potential source of concern during their mark-up.)

Score likely available soon: Republican leaders have indicated that CBO's analysis may be made released the week of March 13.

Fissures in GOP support?

Even if the legislation is ultimately determined to be compliant with budget reconciliation rules, there are questions as to whether Republicans will be able to cobble together the simple majorities they would need to move it through the House and Senate.

Despite the initial view by many that repealing and replacing the PPACA would be a relatively smooth – and speedy – process (given GOP control of the House, the Senate, and the White House) significant political hurdles have emerged that leave the final outcome uncertain. While congressional Republicans are in near-universal agreement on the “repeal” component of the process, there is far less harmony around tax and nontax elements of the “replace” piece.

Obamacare 2.0?: Declaring it simply a repackaging of the current system – and dubbing it Obamacare Lite or Obamacare 2.0 – a number of the most conservative Republicans in both chambers have panned the current House proposal, including Sens. Rand Paul of Kentucky and Mike Lee of Utah, Rep. Jim Jordan of Ohio (who co-founded the 30-member-strong House Freedom Caucus), and Rep. David Brat of Virginia, who came to the House in 2014 by surprisingly toppling then-Majority Leader Eric Cantor.

Jordan compared the current House repeal-and-replace proposal unfavorably to the GOP’s repeal-only bill that President Obama vetoed early last year.

“Keep the Cadillac tax in place? Keep Medicaid in place until 2020? We didn’t have Medicaid expansion in the bill we sent to President Obama, but we have it in the one we send to President Trump? That makes no sense to me,” Jordan told *The Washington Post* on March 7. To emphasize his point, Jordan this week reintroduced the earlier repeal-only legislation.

Republican Study Committee members have also rejected the AHCA’s refundable tax credit as a new entitlement program.

Brat told *Politico* on March 6 that “[Speaker] Paul Ryan has always said the entire rationale for this bill is to bend the cost curve down and so far I have seen no evidence that this bill will bring the cost curve down.”

Across the Capitol, Mike Lee tweeted the day before the House mark-ups that “[t]his isn’t the #Obamacare repeal bill we’ve been waiting for. It’s a missed opportunity and step in wrong direction.”

And Republican Sen. Tom Cotton of Arkansas bluntly weighed in with his own tweets on March 9, after the Ways and Means vote: “House health-care bill can’t pass Senate [without] major changes. To my friends in House: pause, start over. Get it right, don’t get it fast.”

The measure also has its critics among some moderate Senate Republicans, including Susan Collins of Maine and Lisa Murkowski of Alaska, who have expressed concern about the bill’s potential to cut off funding for Planned Parenthood.

Thin margin for error: With no Democrats expected to support the legislation and Republicans able to lose only 2 votes in the Senate and 21 in the House, such statements of opposition raise the stakes for GOP leaders. The Trump administration has gone into “full sell mode,” according to White House press secretary Sean Spicer. Health and Human Services Secretary Tom Price, OMB Director Mick Mulvaney, Vice President Mike Pence, and President Trump himself have all been meeting with Republican critics of the bill, seeking to assuage their concerns and hinting at the potential for changes in the legislation as it makes its way through Congress.

Rand Paul has interpreted the administration’s outreach effort as a clear sign that it is open to revising the legislation.

“[It] is unknown what the product will be, but I promise you the White House, the cabinet and everybody else assumes there will be a negotiation or they wouldn’t be making all these phone calls and arranging all these appointments with conservatives in the House and Senate,” he told the *Conservative Tribune*.

As part of their whip effort, administration officials, House Speaker Ryan, and other Republican leaders are emphasizing that this week’s action is simply the first of three phases in the repeal-and-replace process, necessary because of the strict reconciliation rules. As they describe it, the AHCA will repeal the Affordable Care Act’s mandate, taxes, and spending and “begin to rebuild” within the parameters of reconciliation instructions. This will be followed by Health and Human Services Secretary Price deregulating the marketplace to provide stability, increased choices, and lower costs, which in turn will be followed by the passage of “conservative-minded bills to allow shopping [for insurance coverage] across state lines, medical liability reform, and more.” The bills in this third phase will likely include policy changes not permissible under reconciliation rules and will not be protected from filibuster in the Senate.

Despite this explanation, David McIntosh, president of the conservative advocacy group Club for Growth, told *The Washington Post* on March 8 that his group still opposes the House plan. Other influential conservative organizations, including Heritage Action of America (the advocacy arm of the Heritage Foundation) and FreedomWorks, continue to rally against the bill, as well.

Timing: House GOP leaders hope to move the AHCA legislation through the chamber this month. Senate Majority Leader Mitch McConnell of Kentucky has indicated he will bring a House-passed bill to the Senate floor for a vote as soon as possible, without Senate committee hearings or significant amendments. If all goes according to leadership's plans, this would happen before Congress departs for a two-week recess on April 7 and would prevent the bill from being unfinished business when members return to their home states.

Although he did not address issues of timing, Sean Spicer was adamant in his March 9 press briefing that the AHCA will be enacted into law.

"This bill will land on the president's desk. He will sign it," Spicer said.

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