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Two Obamacare Mandates That Dramatically Expand The Internal Revenue Service's Power

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Much of the talk in the news this week regards the appalling scandal involving IRS targeting of conservative non-profit groups. So it's worth noting that Obamacare dramatically expands the authority and the scope of the Internal Revenue Service. Two provisions in particular will require thousands of new IRS agents, and billions in funding, to enforce: the law's individual mandate, forcing most Americans to buy government-approved health insurance; and its employer mandate, forcing most employers to take money out of workers' paychecks to purchase costly health insurance on their behalf. Here's why these two provisions are so intrusive, and why the only solution to the problems they create is to repeal them.

Many people are exempt from the individual mandate

Obamacare requires the IRS to enforce the individual mandate. So let's first review the precise details of how the individual mandate works. It turns out that many people are exempt from the mandate, and so the IRS has to know a lot about you in order to decide whether you are in compliance with it.

The individual mandate, or what Section 1501 of the Affordable Care Act calls the "shared responsibility for health care," requires individuals to maintain "minimum essential coverage" or pay a "penalty" (a penalty which Supreme Court Chief Justice John Roberts generously transmogrified into a "tax").

The mandate is phased in over a three-year period. In 2014, the fine for noncompliance is 1 percent of adjusted gross income, or $95, whichever is greater. In 2015, the fine is 2 percent of AGI, or $325, whichever is greater. In 2016 and thereafter, it's 2.5 percent of AGI or $695, whichever is greater.

Several groups are exempted from the mandate, including: (1) "a member of a recognized religious sect" that has a moral objection to health insurance; (2) "health care sharing ministries" in which a group of religious believers pool their resources to fund medical expenses, so long as that group has been in continuous existence since 1999; (3) illegal immigrants; (4) incarcerated individuals; and (5) members of Indian tribes.

Individuals who fall below certain income thresholds are exempt from the mandate's fines. Anyone below 138 percent of the federal poverty level (in 2013, $15,856 for an individual, or $32,499 for a family of four) is exempt from the mandate.

In addition, anyone whose "required contribution for coverage…exceeds 8 percent of such individual's household income" is exempt. What is a "required contribution? It's either (1) the portion of an employer-sponsored insurance plan that is paid directly by the individual for self-only coverage; or (2) the premium for the "lowest cost bronze plan available…through the Exchange in the State," minus the subsidies that the individual would receive from the federal government.

To make that less abstract: the average insurance plan covering a single individual costs around $5,500. If you're paying for that entire cost yourself, you're exempt from the mandate if your income is below $68,750. If your employer is paying half the cost on your behalf, then you're exempt from the mandate if your income is below $34,375.

So, in reality, only upper-income individuals are subject to the mandate; in addition, most people who get coverage through their employers are effectively required to take it.

As a practical matter, what this means is the individual mandate is actually quite weak. The typical uninsured person is a young, healthy individual making less than $50,000 a year whose employer doesn't offer health insurance. That individual will be exempt from the individual mandate in the average state.

The employer mandate incentivizes "unaffordable" coverage

Section 1513 of the Affordable Care Act covers "shared responsibility for employers regarding health coverage." The law requires that every employer with 50 or more "full-time employees" offer "minimum essential coverage" in an "affordable" manner. Employees that don't comply, if that non-compliance results in at least one worker accepting Obamacare exchange subsidies, face steep fines.

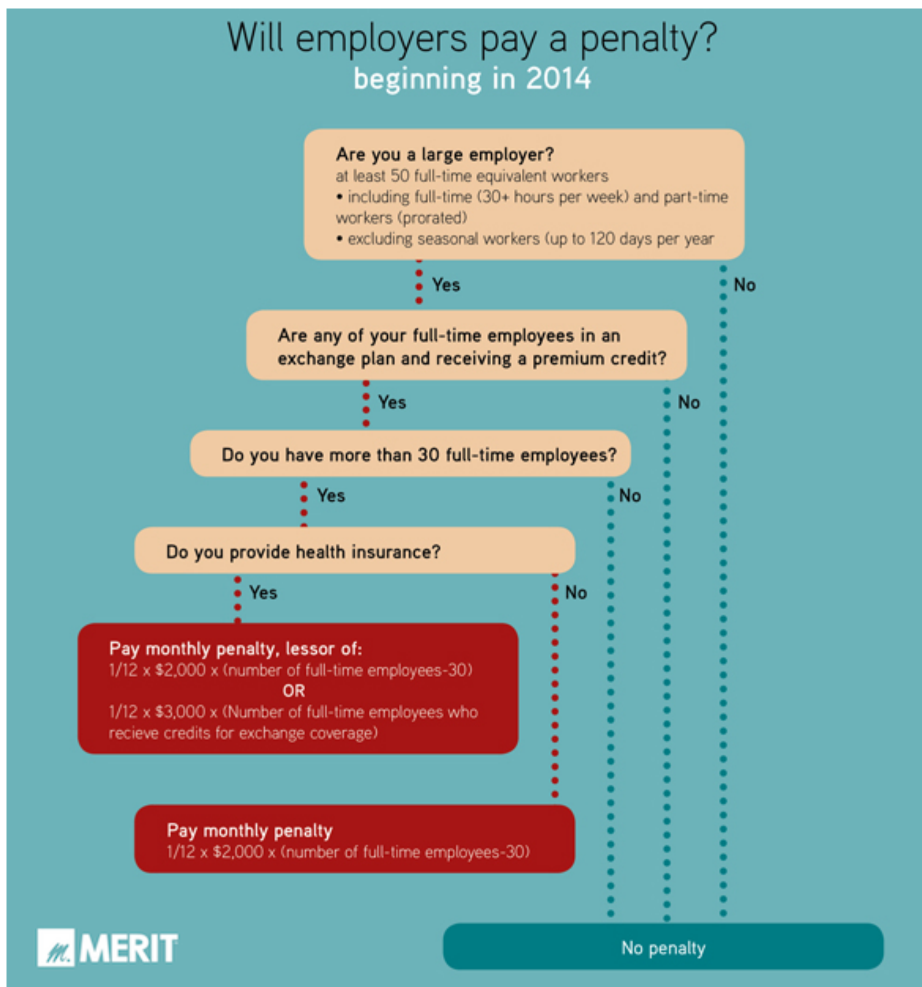
A "full-time employee" is someone who works at least 120 hours per month, or about 30 hours a week. Importantly, employers will also have to add up the total hours worked by part-timers, and divide by 120, to count toward that total. So, for example, three employees who each work 80 hours a week would count as two full-time employees (240 total hours divided by two). For this reason, employers who restrict their workers to 29 hours a week may not successfully evade the employer mandate.

"Minimum essential coverage" is defined in part by the law and in part by lengthy regulations issued by the Department of Health and Human Services. As to "affordability," employers must offer plans that, for those between 100 and 400 percent of the federal poverty level, do not require the worker to pay more than 9.5 percent of his household income. In addition, the plan must have an actuarial value of at least 60 percent (i.e., the expected insurance payout relative to deductibles, co-pays, and the like).

The penalty is triggered if at least one employee seeks federal exchange subsidies instead of gaining insurance form his employer. In that case, the employer will have to pay a non-tax-deductible fine of $2,000 times (the number of full-time employees – 30).

If the employer does offer a health plan, but it isn't "affordable" to all workers or fails to meet the "minimum essential coverage" requirements, then the employer pays the lesser of the fine described above, or $3,000 times the number of full-time employees receiving exchange subsidies.

What does this mean in reality? It means that employers have an incentive to offer coverage that is either "unaffordable" according to Obamacare or that fails to meet the law's "minimum essential requirements." That way, the employer pays a penalty only for those workers who gain subsidized coverage on the exchanges. So the best way for employers to "dump" coverage onto the exchanges is not by offering no coverage at all, but by offering coverage that doesn't meet Obamacare's requirements.



How these mandates expands IRS' power—and your employers'

Now that you know the details of the individual and employer mandates, you can see why the IRS needs to hire thousands of additional agents in order to enforce them.

To enforce the individual mandate, the IRS needs to know whether or not you have purchased insurance this year. It will also need to know the specific insurance policy you have, in order to ensure that it meets Obamacare's "minimum essential coverage" requirement.

To enforce the employer mandate, the IRS needs the same information from employers in terms of the specific policies employers purchase for their workers, and also the hours worked by every part-time employee. In addition, your employer will need to know what your household income is, in order to ensure that the coverage it offers you is "affordable" to you by the law's definition.

Some conservatives are raising the alarm: can a politicized IRS handle these duties in a non-partisan way? Or will your health records get leaked by the agency? Indeed, the IRS is subject to a class-action lawsuit in California, alleging that the IRS has improperly obtained personal medical records for 10 million individuals in that state, without a warrant.

Others are suggesting that the duty to enforce the individual and employer mandates be taken out of IRS' hands and moved into another agency. But, to me, this doesn't make much sense. Do we really want another government agency to have sensitive information about our incomes and our insurance policies?

The only viable solution to this problem is to repeal the employer mandate altogether, and to replace the individual mandate with something else, like a limited open enrollment period, that does not require expanding the power and the authority of the IRS.

Repealing the employer mandate will give employers additional incentive to dump workers onto Obamacare's exchanges. But, in my view, this is on balance a good thing, because it will mean that individuals can shop for insurance themselves, something that economists of all stripes support.

I continue to believe that it is unlikely at this stage that Republicans will be able to repeal Obamacare as a whole. But they could do much to improve our health-care system, and much to contain the power of the IRS, by repealing two of its most offensive mandates.

UPDATE: The Wall Street Journal has an excellent piece today expanding on what I discuss above—the ability of employers to partially evade the employer mandate by offering "bare-bones health plans" that fail Obamacare's tests of affordability and actuarial value:

Employers are increasingly recognizing they may be able to avoid certain penalties under the federal health law by offering very limited plans that can lack key benefits such as hospital coverage.

Benefits advisers and insurance brokers—bucking a commonly held expectation that the law would broadly enrich benefits—are pitching these low-benefit plans around the country. They cover minimal requirements such as preventive services, but often little more. Some of the plans wouldn't cover surgery, X-rays or prenatal care at all. Others will be paired with limited packages to cover additional services, for instance, $100 a day for a hospital visit.

Federal officials say this type of plan, in concept, would appear to qualify as acceptable minimum coverage under the law, and let most employers avoid an across-the-workforce $2,000-per-worker penalty for firms that offer nothing. Employers could still face other penalties they anticipate would be far less costly.

It is unclear how many employers will adopt the strategy, but a handful of companies have signed on and an industry is sprouting around the tactic. More than a dozen brokers and benefit-administrators in 10 states said they were discussing the strategy with their clients…

The idea that such plans would be allowable under the law has emerged only recently. Some benefits advisers still feel they could face regulatory uncertainty. The law requires employers with 50 or more workers to offer coverage to their workers or pay a penalty. Many employers and benefits experts have understood the rules to require robust insurance, covering a list of "essential" benefits such as mental-health services and a high percentage of workers' overall costs. Many employers, particularly in low-wage industries, worry about whether they—or their workers—can afford it.

But a close reading of the rules makes it clear that those mandates affect only plans sponsored by insurers that are sold to small businesses and individuals, federal officials confirm. That affects only about 30 million of the more than 160 million people with private insurance, including 19 million people covered by employers, according to a Citigroup Inc. report. Larger employers, generally with more than 50 workers, need cover only preventive services, without a lifetime or annual dollar-value limit, in order to avoid the across-the-workforce penalty.

Such policies would generally cost far less to provide than paying the penalty or providing more comprehensive benefits, say benefit-services firms. Some low-benefit plans would cost employers between $40 and $100 monthly per employee, according to benefit firms' estimates.

"For certain organizations, it may be an ideal solution to minimize the cost of opting out," said David Ellis, chief executive of Youngtown, Ariz.-based LifeStream Complete Senior Living, which employs about 350 workers, including low-wage housekeepers and kitchen staff. Mr. Ellis, who was recently pitched a low-benefit plan, said it is one option the firm may consider to lower costs and still comply with the law, he said.

Administration officials confirmed in interviews that the skinny plans, in concept, would be sufficient to avoid the across-the-workforce penalty. Several expressed surprise that employers would consider the approach.

"We wouldn't have anticipated that there'd be demand for these types of band-aid plans in 2014," said Robert Kocher, a former White House health adviser who helped shepherd the law. "Our expectation was that employers would offer high quality insurance." Part of the problem: lawmakers left vague the definition of employer-sponsored coverage, opening the door to unexpected interpretations, say people involved in drafting the law…

San Antonio-based Bill Miller Bar-B-Q, a 4,200-worker chain, will replace its own mini-med with a new, skinny plan in July and will aim to price the plan at less than $50 a month, about the same as the current policy, said Barbara Newman, the chain's controller. The new plan will have no dollar limits on benefits, but will cover only preventive services, six annual doctors' visits and generic drugs. X-rays and tests at a local urgent care chain will also be covered. It wouldn't cover surgeries or hospital stays.

Because the coverage is limited, workers who need richer benefits can still go to the exchanges, where plans would likely be cheaper than a more robust plan Bill Miller has historically offered to management and that costs more than $200 per month. The chain plans to pay the $3,000 penalty for each worker who gets an exchange-plan subsidy.