Health Care Law Subsidies: A Tale of Two Cities

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The 2010 health care law will conjure up a strange brew of inequities as it comes to a boil in 2014. The mechanistic, one-size-fits-all health insurance subsidies, for example, will generate serious questions about the law's fairness. By ignoring the enormous regional disparities in cost of living, the subsidies effectively penalize those in more expensive localities and reward those in lower-cost areas. Additionally, the law biases the subsidies toward those with larger families.

This inequity arises because of a three-part structure at the core of the Patient Protection and Affordable Care Act (PPACA). First, PPACA requires individuals to purchase health insurance (or to pay penalties for not doing so). Second, another provision draws a mathematical line between those households with access to "affordable" insurance and those without such access. Third, the law offers premium tax credits (subsidies) to households lacking options meeting the affordability standards. To qualify for subsidies, the household's income must be below 400 percent of the Federal Poverty Level (FPL), and insurance premiums that the household pays must exceed 9.5 percent of the employee's income. A household meeting these two standards can obtain the subsidies and purchase insurance in the exchanges set to open in 2014.

To understand the problem, let's focus on two siblings – one in New York City and one in Abilene, Texas. Both own small businesses.

New York sister, Texas brother

The New Yorker is single and has a new business that earns her $45,000 in its first year of operation. To put this in perspective, this amount is almost exactly what a beginning schoolteacher earns in New York. With high taxes, food prices, and apartment rents, $45,000 in New York City only buys a Spartan life in a cramped apartment.

The Texan is married, has three children, and earns $100,000 a year at his 15-year-old business. He and his family live in a roomy house with a swimming pool. In Abilene, $100,000 buys a very cozy life. An unscientific Google search suggests that most of Abilene's attorneys earn less than our business owner.

In 2014, sitting at the Thanksgiving table, the sister complains to her brother about the heavy burden of health insurance. The brother mentions that he bought insurance in the new exchange and received federal subsidies because the law deems health insurance unaffordable for him and his family. The sister is surprised – and irritated – since she was told that her income is too high to qualify for subsidies.

Here's the explanation. To get a health insurance subsidy, a household's income must be less than 400% of FPL *for a given size of household*. The guidelines have separate dollar figures for Alaska and Hawaii, but no regional variation within the 48 contiguous states. In those 48 states, 400% of FPL for a household of one person is currently $43,560; for a household of five people, the figure is $104,680. The sister earns more than $43,560, so she cannot receive subsidies. Her brother earns less than $104,680, so he may qualify.

To obtain the subsidies, the Texan's insurance would have to cost more than 9.5 percent of household income – $9,500 in this case. An October 2011 Kaiser Family Foundation survey reported that, across the

U.S., average 2011 individual and family policies cost, respectively, $5,429 (up 8 percent from 2010) and $15,073 (up 9 percent from 2010). We can say with near certainty that the New Yorker's individual policy will cost more than 9.5 percent of her income ($4,275). It's not important to this blog piece, but given the high cost of health care in New York, the sister's unsubsidized individual policy might even cost more than her wealthier brother's subsidized family policy.

In a different context, New York Senator Charles Schumer recently declared a proposed income tax provision to be unacceptable because it effectively treats households across America as "rich" if they earn more than $250,000 a year. Schumer said, "$250,000 makes you really rich in Mississippi but it doesn't make you rich at all in New York and there ought to be some kind of scale based on the cost of living on how much you pay." One can apply Schumer's logic to PPACA's subsidies. Doing so, however, would open quite a few new cans of worms.

When families gather in 2014, PPACA's fairness will be questioned around many a dinner table. In that year, members of Congress from high cost-of-living areas are likely to hear quite a few of those questions from displeased constituents.