



# **Budget Control Act: Potential Impact of Automatic Spending Reduction Procedures on Health Reform Spending**

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## Summary

The Budget Control Act of 2011 (BCA; P.L. 112-25) established new budget enforcement mechanisms for reducing the federal deficit by at least \$2.1 trillion over the 10-year period FY2012-FY2021. The BCA placed statutory limits, or caps, on discretionary spending for each of those 10 fiscal years, which will save an estimated \$0.9 trillion during that period. In addition, it created a Joint Select Committee on Deficit Reduction (Joint Committee) with instructions to develop legislation to reduce the federal deficit by at least another \$1.5 trillion through FY2021. If Congress and the President are unable to enact a Joint Committee bill by January 15, 2012, that reduces the deficit by at least \$1.2 trillion over the period FY2012-FY2021, then automatic annual spending reductions would be triggered beginning in FY2013. They would be achieved by lowering the caps on discretionary spending and by an automatic across-the-board cancellation of budgetary resources (i.e., spending cuts) for nonexempt direct spending programs—a process known as sequestration.

The potential impact of spending reductions triggered by the BCA on health reform spending under the Patient Protection and Affordable Care Act (ACA) would appear to be somewhat limited. ACA sought to increase access to affordable health insurance by expanding the Medicaid program and by restructuring the private health insurance market. It set minimum standards for private insurance coverage, created a mandate for most U.S. residents to obtain coverage, and provided for the establishment by 2014 of state-based insurance exchanges for the purchase of health insurance through which certain individuals and families will be able to receive federal subsidies to reduce the cost of purchasing that coverage. The law included direct spending to subsidize the purchase of health insurance coverage through the exchanges, as well as increased outlays for the Medicaid expansion. Under the rules governing sequestration, Medicaid spending would be exempt from any reduction, and cuts to Medicare would be capped at 2%.

ACA also included numerous mandatory appropriations that provide billions of dollars to support temporary programs to increase coverage and funding for targeted groups, provide funds to states to plan and establish exchanges, and support many other research and demonstration programs and activities. These appropriations would, in general, be subject to direct spending reductions under a sequestration order. However, for any given fiscal year in which sequestration was ordered, only new budget authority for that year (including advance appropriations that first become available for obligation in that year) would be reduced. Unobligated balances carried over from previous fiscal years would be exempt from sequestration.

ACA is likely to affect discretionary spending subject to the annual appropriations process. The law reauthorized appropriations for numerous existing discretionary grant programs and activities authorized under the Public Health Service Act, permanently reauthorized funding for the Indian Health Service (IHS), and created a number of new grant programs and provided for each an authorization of appropriations. In addition, the Congressional Budget Office projected that both the Department of Health and Human Services and the Internal Revenue Service will incur substantial costs to implement the policies and programs established by ACA. Those costs will have to be funded largely through the annual appropriations process. Most of the ACA-related discretionary spending would be subject to automatic spending reductions triggered by the BCA. Under the sequestration rules, however, any reduction in funding for community health centers and the IHS would be capped at 2%.

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## Introduction

The Budget Control Act of 2011 (BCA), which was enacted on August 2, 2011,<sup>1</sup> was the product of negotiations between the President and Congress to raise the nation's debt ceiling and avoid the federal government reaching its borrowing limit. The BCA authorized an increase in the debt limit of at least \$2.1 trillion (and up to \$2.4 trillion) in three installments. Congress can block the second and third installments by passing a joint resolution disapproving the debt limit increase and overriding an expected presidential veto, an outcome that is considered extremely unlikely.

In addition, the BCA established a process for reducing the federal deficit by at least \$2.1 trillion over the 10-year period FY2012-FY2021. First, the law placed statutory limits, or caps, on discretionary spending for each of the next 10 fiscal years.<sup>2</sup> For FY2012 and FY2013, separate caps for security and nonsecurity spending will be in effect.<sup>3</sup> For each of the remaining eight fiscal years (i.e., FY2014-FY2021), a single cap will apply to total discretionary spending. The Congressional Budget Office (CBO) estimated that these discretionary spending limits, which grow by approximately 2% each year, will reduce federal spending by \$917 billion between FY2012 and FY2021, compared to the projected level of spending if annual appropriations were to grow at the rate of inflation.<sup>4</sup>

Second, the BCA created a Joint Select Committee on Deficit Reduction (Joint Committee), composed of an equal number of Democrats and Republicans from the House and Senate. The Joint Committee was instructed to develop legislation to reduce the federal deficit by at least another \$1.5 trillion through FY2021.<sup>5</sup> It has until November 23, 2011, to approve a bill and have it considered by the House and Senate under special procedures that prevent amendments and limit debate in both chambers. If Congress and the President, for whatever reason, fail to enact a Joint Committee bill reducing the deficit by at least \$1.2 trillion over the period FY2012-FY2021, then automatic annual spending reductions would be triggered beginning in FY2013.

The spending reductions would be equally divided between defense spending and all other spending (i.e., nondefense spending).<sup>6</sup> The amount of reduction required in each category would then be divided proportionately between discretionary spending and mandatory spending (also known as direct spending).<sup>7</sup> The reductions would be achieved (1) by lowering the annual caps on

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<sup>1</sup> P.L. 112-25, 125 Stat. 240. For a more detailed examination of all the provisions in the BCA, see CRS Report R41965, *The Budget Control Act of 2011*, by Bill Heniff Jr., Elizabeth Rybicki, and Shannon M. Mahan.

<sup>2</sup> Discretionary spending refers to outlays from budget authority (i.e., the authority to incur financial obligations that result in government expenditures) that is provided in and controlled by the annual appropriations acts.

<sup>3</sup> Security spending comprises discretionary appropriations for the Department of Defense, the Department of Homeland Security, the Department of Veterans Affairs, and other related activities. Nonsecurity spending comprises all discretionary appropriations not included in the security category.

<sup>4</sup> U.S. Congressional Budget Office, *Analysis of Budget Control Act*, August 1, 2011. Available at <http://www.cbo.gov/ftpdocs/123xx/doc12357/BudgetControlActAug1.pdf>.

<sup>5</sup> The BCA placed no specific policy restrictions or requirements on the Joint Committee. The committee could recommend changes in federal revenues, spending, or both.

<sup>6</sup> As discussed later in this report, the annual discretionary spending caps for FY2012-FY2021 would be revised if automatic spending reductions were triggered. The overall discretionary spending limit for each fiscal year would remain unchanged, but that amount would be divided between defense discretionary spending and all other (i.e., nondefense) discretionary spending.

<sup>7</sup> Mandatory, or direct, spending generally refers to budget authority that is provided in laws other than the annual appropriations acts. Mandatory spending includes entitlement authority (e.g., Medicare, Social Security).

discretionary spending for FY2014-FY2021, and (2) by an automatic across-the-board cancellation of budgetary resources (i.e., spending cuts)—a process known as sequestration—for discretionary spending in FY2013 and for nonexempt direct spending programs over the FY2013-FY2021 period.

## **Health Reform Spending**

There is considerable interest in how automatic spending reductions triggered by the BCA would affect implementation of the Patient Protection and Affordable Care Act (ACA), the health reform law enacted in March 2010.<sup>8</sup> Among its many provisions, ACA restructured the private health insurance market, set minimum standards for health coverage, created a mandate for most U.S. residents to obtain health insurance coverage, and provided for the establishment by 2014 of state-based insurance exchanges for the purchase of private health insurance through which certain individuals and families will be able to receive federal subsidies to reduce the cost of purchasing that coverage. The new law also expanded eligibility for Medicaid; amended the Medicare program in ways that are intended to reduce the growth in Medicare spending that had been projected under preexisting law; imposed an excise tax on insurance plans found to have high premiums; and made numerous other changes to the tax code, Medicare, Medicaid, the Children's Health Insurance Program (CHIP), and many other federal programs.<sup>9</sup>

ACA is projected to have a significant impact on federal direct spending and revenues. The law included direct spending to subsidize the purchase of health insurance coverage through the exchanges, as well as increased outlays for the expansion of the Medicaid program. ACA also included numerous mandatory appropriations to fund temporary programs to increase access and funding for targeted groups, provide funding to states to plan and establish exchanges, and support many other research and demonstration programs and activities. The costs of expanding public and private health insurance coverage and other spending are offset by revenues from new taxes and fees, and by savings from payment and health care delivery system reforms designed to slow the growth in spending on Medicare and other federal health care programs.

Implementing ACA also is likely to affect discretionary spending that is subject to the annual appropriations process. The law established numerous new grant programs and provided for each an authorization of appropriations. It also reauthorized appropriations for many existing grant programs. While the authorization of appropriations for most of these programs expired prior to ACA's enactment, typically they continued to receive an annual appropriation.

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<sup>8</sup> ACA was signed into law on March 23, 2010 (P.L. 111-148, 124 Stat. 119). A week later, on March 30, 2011, the President signed the Health Care and Education Reconciliation Act (HCERA; P.L. 111-152, 124 Stat. 1029), which amended multiple health care and revenue provisions in ACA. Several other bills that were subsequently enacted during the 111<sup>th</sup> Congress made more targeted changes to specific ACA provisions. All references to ACA in this report refer to the law as amended. Note that previous CRS reports on the Patient Protection and Affordable Care Act used the acronym PPACA to refer to the law. CRS is now using the more common acronym ACA.

<sup>9</sup> More information on the ACA provisions may be found in the following CRS products: CRS Report R41664, *PPACA: A Brief Overview of the Law, Implementation, and Legal Challenges*, by Hinda Chaikind et al.; CRS Report R41210, *Medicaid and the State Children's Health Insurance Program (CHIP) Provisions in PPACA: Summary and Timeline*, by Evelyne P. Baumrucker et al.; CRS Report R41196, *Medicare Provisions in the Patient Protection and Affordable Care Act (PPACA): Summary and Timeline*, coordinated by Patricia A. Davis; and CRS Report R41278, *Public Health, Workforce, Quality, and Related Provisions in PPACA: Summary and Timeline*, coordinated by C. Stephen Redhead and Erin D. Williams.

## **Report Roadmap**

This report examines how automatic spending reductions triggered by the BCA might affect health reform implementation under ACA. If such a process were triggered, it must be emphasized that the details of its execution would depend in large measure on the statutory interpretations and actions of the Office of Management and Budget (OMB). Each year, OMB would be responsible for determining the proportional allocation of required cuts to discretionary and nonexempt direct spending in both the defense and nondefense categories. It would also have exclusive authority in applying the exemptions and special rules related to sequestration.

The report is divided into two sections. The first section provides an overview of ACA and describes the budgetary effects of its insurance coverage and other key spending provisions, based on CBO's most recent 10-year budget estimates. The second section discusses which of those provisions would likely be subject to, or exempt from, BCA spending reductions. A summary of that discussion appears in **Table 1** at the end of the report. This product will be updated to reflect important legislative and other developments.

## **Patient Protection and Affordable Care Act**

The primary goal of ACA is to increase access to affordable health insurance for the millions of Americans without coverage and make health insurance more affordable for those already covered. In addition, ACA makes numerous changes in the way health care is financed, organized, and delivered. These provisions are intended to slow the growth in health care costs and improve the quality of care by aligning payment incentives to increase efficiency and achieve savings; organizing care delivery systems to promote accountable, patient-centered, and coordinated care; and establishing benchmarks for better health outcomes.

While most of the major provisions of the law do not take effect until 2014, some provisions are already in place, and others are to be phased in over the next few years.

### **Coverage Expansions and Market Reforms Prior to 2014**

ACA created several temporary programs to increase access and funding for targeted groups. They include (1) temporary high-risk pools for uninsured individuals with preexisting conditions; (2) a reinsurance program to reimburse employers for a portion of the health insurance claims' costs for their 55- to 64-year-old retirees; and (3) small business tax credits for small employers with fewer than 25 full-time equivalents (FTEs) and average annual wages below \$50,000 that choose to offer health insurance.

In addition, several of ACA's private insurance market reforms have taken effect. Health plans may not impose lifetime limits on the dollar value of essential benefits, rescind coverage (except in cases of fraud), or deny coverage to children up to age 19 based on a preexisting condition. Also, young adults up to age 26 generally must be allowed to remain on their parents' plans. Finally, plans must cover recommended preventive services and immunizations without any cost-sharing.

## **Coverage Expansions and Market Reforms Beginning in 2014**

The major expansion and reform provisions in ACA take effect in 2014. State Medicaid programs will be required to expand coverage to all eligible non-pregnant, nonelderly legal residents with incomes up to 133% of the federal poverty level (FPL). The federal government will initially cover all the costs for this group, with the federal matching percentage phased down to 90% of the costs by 2020. The law requires states to maintain the current CHIP structure through FY2019, and extends CHIP appropriations through FY2015.<sup>10</sup>

Also beginning in 2014, states are expected to establish health insurance exchanges through which eligible individuals and small employers will be able to purchase coverage from private health insurance plans offering standardized benefit and cost-sharing packages. In 2017, states may allow larger employers to purchase health insurance through the exchanges, but are not required to do so. The Secretary of Health and Human Services (HHS) will establish exchanges in states that do not create their own approved exchange. Refundable tax credits will be available to individuals and families with incomes between 133% and 400% of the FPL to help offset the cost of purchasing insurance coverage through the exchanges. In addition, certain individuals and families receiving the premium credit will be eligible for a subsidy to lower their cost-sharing (i.e., out-of-pocket costs such as deductibles and co-pays).

Federal health insurance requirements are further expanded in 2014, with no annual limits on the dollar value of essential benefits and no exclusions for preexisting conditions allowed regardless of age. Plans offered within the exchanges and certain other plans must meet essential benefit standards, requiring them to cover emergency services, hospital care, physician services, preventive care, prescription drugs, and mental health and substance use disorder treatment, among other specified services. Premiums may vary by limited amounts, but only based on age, family size, geographic area, and tobacco use. Finally, plans must sell and renew policies to all individuals and may not discriminate based on health status.

Most U.S. citizens and legal residents will be required to have insurance. Those who remain uninsured may have to pay a penalty. As plans will no longer be able to restrict coverage of individuals with health problems, ACA's individual insurance mandate is intended to ensure that healthy individuals participate in the insurance market rather than waiting until they need health care services. Increasing the number of healthy persons in the risk pool helps spread the risk.

ACA requires employers with more than 200 full-time employees that offer health insurance benefits to automatically enroll new employees in a coverage plan, though employees must be given adequate notice and the opportunity to opt out. Employers with 50 or more full-time employees that have at least one employee who is enrolled in an exchange plan and receiving a premium tax credit may be subject to penalties, whether or not they provide health insurance coverage to their employees.<sup>11</sup>

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<sup>10</sup> For more details on ACA's changes to the Medicaid and CHIP programs, see CRS Report R41210, *Medicaid and the State Children's Health Insurance Program (CHIP) Provisions in PPACA: Summary and Timeline*, by Evelyne P. Baumrucker et al.

<sup>11</sup> For more details on the employer penalties, see CRS Report R41159, *Summary of Potential Employer Penalties Under the Patient Protection and Affordable Care Act (PPACA)*, by David Newman.

## **Estimated Impact and Costs of Coverage Expansions**

The Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT) estimated that ACA will increase the number of nonelderly Americans with health insurance by about 34 million in 2021. The share of legal nonelderly U.S. residents with insurance coverage in 2021 will be about 95%. Expansion of the Medicaid and CHIP programs is expected to attract 17 million additional enrollees that year, accounting for roughly half of the increase in coverage. The other half is due to an increase in private health insurance coverage. An estimated 24 million people will purchase their own coverage through insurance exchanges in 2021. However, about 7 million fewer people will purchase individual coverage directly from insurers or obtain coverage through their employers, resulting in a net increase in the number of people with private insurance coverage of about 17 million.<sup>12</sup>

CBO and JCT's February 2011 baseline projections of the federal budgetary effects of ACA estimated that insurance coverage expansion will result in gross costs of \$1,390 billion over the 10-year period FY2012-FY2021. Gross costs include the exchange subsidies and related spending, increased spending on Medicaid and CHIP, and tax credits for certain small employers. CBO and JCT further estimated that those costs will be partially offset by an estimated \$348 billion from penalties paid by uninsured individuals and employers, an excise tax on high-premium insurance plans, and net savings from other effects that coverage expansion is expected to have on tax revenues and outlays. Thus, CBO and JCT projected in the February 2011 baseline that ACA's insurance coverage provisions will result in net costs of \$1,042 billion over the FY2012-FY2021 period.<sup>13</sup>

The net costs of coverage expansion under ACA are more than covered by (1) new revenue sources from taxes and fees (other than those related to insurance coverage, mentioned above); and (2) direct spending savings from payment and delivery system reform provisions that are designed to slow the rate of growth of federal health care spending, primarily for Medicare, and improve outcomes and the quality of care. In the February 2011 baseline, CBO and JCT projected that the new revenues and direct spending savings—described briefly below—will total \$1,252 billion over the 10-year period FY2012-FY2021. Based on those projections, CBO and JCT estimated that ACA implementation will reduce federal deficits by \$210 billion over the FY2012-FY2021 period.<sup>14</sup>

Note that CBO and JCT have provided revised March 2011 baseline projections of the costs of insurance coverage expansion under ACA, but have not yet revised the February 2011 estimates of the law's offsetting revenues and direct spending savings. The March 2011 baseline projected gross costs of \$1,445 billion and net costs of \$1,131 billion for insurance coverage expansion over the 10-year period FY2012-FY2021.<sup>15</sup> The discussion of the potential impact of automatic spending reductions on insurance coverage expansion in the final section of this report uses the March 2011 cost estimates.

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<sup>12</sup> U.S. Congress, House Committee on Energy and Commerce, Subcommittee on Health, "CBO's Analysis of the Major Health Care Legislation Enacted in March 2010," Statement of Douglas W. Elmendorf, Director, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., March 30, 2011. Available at <http://www.cbo.gov/ftpdocs/121xx/doc12119/03-30-HealthCareLegislation.pdf>. See Table 3.

<sup>13</sup> Ibid., see Table 1.

<sup>14</sup> Ibid., see Table 1.

<sup>15</sup> Ibid., see Table 1.

## Revenues

The increase in revenues, totaling an estimated \$520 billion over the period FY2012-FY2021, is achieved largely by raising taxes on high-income households and by imposing fees on insurers and on manufacturers and importers of pharmaceuticals and medical devices.<sup>16</sup>

## Savings from Payment and Delivery System Reforms

ACA included numerous Medicare payment provisions intended to reduce the rate of growth in spending. They include reductions in Medicare Advantage (MA) plan payments and a lowering of the annual payment update for hospitals and certain other providers.<sup>17</sup> ACA established an Independent Payment Advisory Board (IPAB) to make recommendations for achieving specific Medicare spending reductions if costs exceed a target growth rate. IPAB's recommendations will take effect unless Congress overrides them, in which case Congress would be responsible for achieving the same level of savings.<sup>18</sup> Also, ACA provided tools to help reduce fraud, waste, and abuse in both Medicare and Medicaid.

Other provisions establish pilot, demonstration, and grant programs to test integrated models of care, including accountable care organizations (ACOs), medical homes that provide coordinated care for high-need individuals, and bundling payments for acute-care episodes (including hospitalization and follow-up care). ACA created the Center for Medicare and Medicaid Innovation (CMMI) to pilot payment and service delivery models, primarily for Medicare and Medicaid beneficiaries. The law also established new pay-for-reporting and pay-for-performance programs within Medicare that will pay providers based on the reporting of, or performance on, selected quality measures.

Additionally, ACA created incentives for promoting primary care and prevention; for example, by increasing primary care payment rates under Medicare and Medicaid, covering some preventive services without cost-sharing, and funding community-based prevention and employer wellness programs, among other things. The law increased funding for community health centers and the National Health Service Corps to expand access to primary care services in rural and medically underserved areas and reduce health disparities. Finally, ACA required the HHS Secretary to develop a national strategy for health care quality to improve care delivery, patient outcomes, and population health.

Overall, CBO estimated that the health care payment and delivery system reform provisions in ACA will result in a net reduction in direct health care spending of \$732 billion over the period FY2012-FY2021.<sup>19</sup>

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<sup>16</sup> Ibid., see Table 1. For more information about the revenue provisions in ACA, see CRS Report R41128, *Health-Related Revenue Provisions in the Patient Protection and Affordable Care Act (PPACA)*, by Janemarie Mulvey.

<sup>17</sup> For more information about the Medicare provisions in ACA, see CRS Report R41196, *Medicare Provisions in the Patient Protection and Affordable Care Act (PPACA): Summary and Timeline*, coordinated by Patricia A. Davis.

<sup>18</sup> For more information about IPAB, see CRS Report R41511, *The Independent Payment Advisory Board*, by David Newman and Christopher M. Davis.

<sup>19</sup> U.S. Congress, House Committee on Energy and Commerce, Subcommittee on Health, "CBO's Analysis of the Major Health Care Legislation Enacted in March 2010," Statement of Douglas W. Elmendorf, Director, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., March 30, 2011. Available at <http://www.cbo.gov/ftpdocs/121xx/doc12119/03-30-HealthCareLegislation.pdf>. See Table 1.

## Impact of Automatic Spending Reductions on Health Reform

As noted in the introduction to this report, the Joint Committee is charged with introducing legislation that would reduce the federal budget deficit by a total of at least \$1.5 trillion over the period FY2012-FY2021. However, if Joint Committee legislation estimated to produce at least \$1.2 trillion in deficit reduction is not enacted by January 15, 2012, then automatic procedures for cutting both discretionary and mandatory (direct) spending will take effect. Failure to enact any such legislation would trigger automatic spending reductions totaling \$1.2 trillion (including an allowance for reduced interest payments on the debt). Enactment of Joint Committee legislation estimated to produce less than \$1.2 trillion in deficit reduction would trigger automatic cuts to make up the difference.

The automatic spending reductions would take the form of equal cuts (in dollar terms) in defense and nondefense spending for each fiscal year over the period FY2013-FY2021. The annual amount of spending cuts required in each of these two categories would be divided proportionately between discretionary and nonexempt direct spending. Direct spending reductions—both defense and nondefense—would be executed through sequestration (i.e., an across-the-board cancellation of budgetary resources). Importantly, the BCA exempts many direct spending programs from sequestration and places a 2% limit on cuts to most Medicare spending.

Discretionary spending reductions in FY2013 also would be achieved through a sequestration of appropriations. However, for each of the remaining fiscal years (i.e., FY2014-FY2021), discretionary spending reductions would be achieved through a downward adjustment of the statutory spending limits.<sup>20</sup>

The sequestration process was first established in 1985 by the Balanced Budget and Emergency Deficit Control Act (BBEDCA), commonly known as the Gramm-Rudman-Hollings Act.<sup>21</sup> Initially, sequestration was tied to annual maximum deficit targets. If the budget deficit exceeded those target levels, then automatic across-the-board spending cuts would be triggered. The BBEDCA has been amended several times, notably by the Budget Enforcement Act of 1990,<sup>22</sup> which tied sequestration to new statutory spending limits, and most recently by the BCA. As already noted, the sequestration process is subject to exemptions and special rules, which are specified in Sections 255 and 256, respectively, of the BBEDCA.<sup>23</sup> Several of those provisions relate to health spending under ACA and are discussed below.

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<sup>20</sup> As already noted (see footnote 6), the annual discretionary spending caps for FY2012-FY2021 would be revised if automatic spending reductions were triggered. The overall discretionary spending limit for each fiscal year would remain unchanged, but that amount would be divided between defense discretionary spending and all other (i.e., nondefense) discretionary spending. Discretionary spending reductions, whether by sequestration (FY2013) or through a downward adjustment of the revised spending caps (FY2014-FY2021), would be applied to both spending categories.

<sup>21</sup> P.L. 99-177, Title II, 99 Stat. 1038.

<sup>22</sup> P.L. 101-508, Title XIII, 104 Stat. 1388-573.

<sup>23</sup> For an overview of the BBEDCA exemptions and special rules, see CRS Report R42050, *Budget “Sequestration” and Selected Program Exemptions and Special Rules*, coordinated by Karen Spar.

## Insurance Coverage Expansion

It appears that most of ACA's projected spending on expanding insurance coverage would not be subject to sequestration in the event that spending reductions are triggered under the BCA. First, the Medicaid and CHIP programs are both exempt from a sequestration order.<sup>24</sup> According to CBO's March 2011 estimate, Medicaid and CHIP outlays account for \$627 billion, or 43%, of the gross costs of \$1,445 billion for coverage expansion over the FY2012-FY2021 period (see **Table 1**).<sup>25</sup>

Second, the refundable tax credits available to individuals and families with incomes between 133% and 400% of the FPL for purchasing insurance coverage through the exchanges also would likely be exempt from a sequestration order.<sup>26</sup> These premium tax credits have the effect of limiting the cost of purchasing coverage to a specified percentage of income. According to CBO's March 2011 estimate, the premium tax credits account for approximately \$653 billion (84%) of ACA's total exchange subsidies and related spending of \$777 billion over the FY2012-FY2021 period (see **Table 1**), which represents about 54% of the \$1,445 billion in gross costs for coverage expansion.<sup>27</sup>

In addition to the premium tax credits for purchasing coverage through an exchange, certain individuals and families receiving the credits are also eligible for coverage with lower cost-sharing (i.e., out-of-pocket costs such as deductibles and co-pays) than otherwise required under the law. This is achieved through a cost-sharing subsidy, which is paid directly to the insurer to cover the extra costs associated with lower patient cost-sharing. The cost-sharing subsidies would presumably be subject to a sequestration order.<sup>28</sup> According to CBO, they account for an additional \$117 billion (15%) of ACA's exchange subsidies and related spending over the FY2012-FY2021 period (see **Table 1**).<sup>29</sup>

Finally, the tax credits available to certain small employers to offset the cost of purchasing health insurance for their employees also would presumably be subject to a sequestration order.<sup>30</sup> These

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<sup>24</sup> Low-income programs, including Medicaid and CHIP, that are exempt from sequestration are listed in BBEDCA Section 255(h). 2 U.S.C. §905(h).

<sup>25</sup> U.S. Congress, House Committee on Energy and Commerce, Subcommittee on Health, "CBO's Analysis of the Major Health Care Legislation Enacted in March 2010," Statement of Douglas W. Elmendorf, Director, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., March 30, 2011. Available at <http://www.cbo.gov/ftpdocs/121xx/doc12119/03-30-HealthCareLegislation.pdf>. See Table 2.

<sup>26</sup> While the ACA premium tax credits are not specifically exempted from sequestration, BBEDCA Section 255(d) provides a general exemption for refundable individual tax credits. It reads as follows: "Payments to individuals made pursuant to provisions of the Internal Revenue Code of 1986 establishing refundable tax credits shall be exempt from reduction under any order issued under this part." 2 U.S.C. §905(d).

<sup>27</sup> U.S. Congress, House Committee on Energy and Commerce, Subcommittee on Health, "CBO's Analysis of the Major Health Care Legislation Enacted in March 2010," Statement of Douglas W. Elmendorf, Director, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., March 30, 2011. Available at <http://www.cbo.gov/ftpdocs/121xx/doc12119/03-30-HealthCareLegislation.pdf>. See Table 2.

<sup>28</sup> The impact of such an order is unclear. ACA entitles certain low-income exchange enrollees to coverage with reduced cost-sharing and requires the participating insurers to provide that coverage. Sequestration would not change that requirement. In the event of a sequestration order, insurers presumably would still have to provide required coverage to qualifying enrollees but they would not receive the full subsidy to cover their increased costs.

<sup>29</sup> <http://www.cbo.gov/budget/factsheets/2011b/HealthInsuranceExchanges.pdf>.

<sup>30</sup> Among the programs and activities listed as being exempt from a sequestration order, BBEDCA Section 255 includes payments to individuals in the form of tax credits (see previous footnote). It does not include small employer (continued...)

credits are available to for-profit and nonprofit employers with fewer than 25 FTEs and average annual wages of less than \$50,000.<sup>31</sup> According to CBO's March 2011 estimate, they are projected to cost \$41 billion over the FY2012-FY2021 period, or about 3% of the \$1,445 billion in gross costs for coverage expansion (see **Table 1**).<sup>32</sup>

In general, federal administrative expenses are subject to sequestration, regardless of whether they are incurred in connection with a program or activity that is otherwise exempt or subject to a special rule.<sup>33</sup> Thus, while the ACA refundable tax credits may be exempt from sequestration, the federal administrative expenses associated with the program would not be exempt. However, federal payments to state and local governments that match or reimburse these governments for their administrative costs are not considered federal administrative expenses and are subject to sequestration, but only to the extent that the relevant federal program is subject to sequestration.<sup>34</sup> For example, federal payments to state Medicaid programs for administrative costs would be exempt from sequestration because the Medicaid program as a whole is exempt.

## **Mandatory Appropriations**

ACA included numerous mandatory appropriations that provide billions of dollars to support new and existing grant programs and other activities. Many of the provisions are annual appropriations of specified amounts for one or more fiscal years. A few of them are multiple-year appropriations, in which the amount appropriated is available for obligation for a definite period of time in excess of one fiscal year (e.g., for the period FY2011-FY2014). Often the provision includes additional language stating that the funds are to remain available "until expended" or "without fiscal year limitation."

Among the more significant appropriations, ACA created a \$1 billion fund to help pay for the law's implementation, and provided billions of dollars for the following temporary programs for targeted groups: (1) \$5 billion for the Pre-Existing Condition Insurance Plan (PCIP), a temporary insurance program to provide health insurance coverage for uninsured individuals with a preexisting condition; (2) \$5 billion for a temporary reinsurance program to reimburse employers for a portion of the costs of providing health benefits to early retirees aged 55-64; and (3) \$6 billion for the Consumer Operated and Oriented Plan (CO-OP) program, to establish temporary health insurance cooperatives.<sup>35</sup> ACA included money for states to plan and establish health insurance exchanges. The law also provided \$10 billion for the FY2011-FY2019 period (and \$10 billion for each subsequent 10-year period) for the CMMI to test and implement innovative

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(...continued)

tax credits.

<sup>31</sup> For more details on the small employer tax credit, see CRS Report R41158, *Summary of Small Business Health Insurance Tax Credit Under the Patient Protection and Affordable Care Act (ACA)*, by David Newman and Hinda Chaikind.

<sup>32</sup> U.S. Congress, House Committee on Energy and Commerce, Subcommittee on Health, "CBO's Analysis of the Major Health Care Legislation Enacted in March 2010," Statement of Douglas W. Elmendorf, Director, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., March 30, 2011. Available at <http://www.cbo.gov/ftpdocs/121xx/doc12119/03-30-HealthCareLegislation.pdf>. See Table 2.

<sup>33</sup> BBEDCA Section 256(h)(1), 2 U.S.C. §906(h)(1).

<sup>34</sup> BBEDCA Section 256(h)(3), 2 U.S.C. §906(h)(3).

<sup>35</sup> Section 1857 of the Department of Defense and Full-Year Continuing Appropriations Act, 2011 (P.L. 112-10, 125 Stat. 38) cancelled \$2.2 billion of the \$6 billion appropriation for the CO-OP program.

payment and service delivery models, and funded an independent board (i.e., IPAB) to provide Congress with proposals for reducing Medicare cost growth and improving quality of care for Medicare beneficiaries.

In addition, ACA appropriated \$2.4 billion for maternal and child health programs and established three multi-billion dollar funds. First, the Community Health Center Fund (CHCF) will provide a total of \$11 billion over five years (FY2011-FY2015) in supplemental funding for community health center operations and the National Health Service Corps. (A separate appropriation provided \$1.5 billion for health center construction and renovation.) Second, the Patient-Centered Outcomes Research Trust Fund (PCORTF) will support comparative effectiveness research through FY2019 with a mix of appropriations and fund transfers. Finally, the Prevention and Public Health Fund (PPHF), for which an annual appropriation is provided in perpetuity, is intended to support prevention, wellness, and other public health-related programs and activities authorized under the Public Health Service Act (PHSA). Overall, ACA includes more than \$100 billion in direct appropriations over the 10-year period FY2012-FY2021 (see **Table 1**).<sup>36</sup>

Some of the appropriations in ACA are included in CBO and JCT's estimate of the costs of coverage expansion (e.g., funding for high-risk pools for individuals with preexisting conditions). All the remaining amounts—including funding for community health centers, health workforce programs, and public health activities—are captured in CBO's overall estimate of the impact of the law's payment and delivery system reform provisions on direct spending.

The mandatory appropriations in ACA would, in general, be subject to direct spending reductions under a sequestration order. However, for any given fiscal year in which sequestration was ordered, only new budget authority for that year (including advance appropriations that first become available for obligation in that year) would be reduced. Unobligated balances (non-defense only) carried over from previous fiscal years are exempt from a sequestration order.<sup>37</sup> Thus, an FY2013 sequestration order to reduce direct spending would not apply to unobligated ACA funds that had been appropriated in a prior fiscal year (i.e., FY2010-FY2012) and were still available for obligation.

The exemption for unobligated balances carried over from prior fiscal years is a potentially important one that would apply to a number of ACA appropriations. As already mentioned, the appropriation provision often specifies that the funds are to remain available “until expended” or “without fiscal year limitation.” One example is the PCIP program to provide health insurance coverage for eligible individuals who have been uninsured for six months and have a preexisting condition. The program terminates on January 1, 2014. ACA appropriated \$5 billion in FY2010, to remain available without fiscal year limitation, to pay claims against the PCIP that are in excess of the premiums collected from enrollees. Any unobligated PCIP funds in FY2013 would be exempt from sequestration.<sup>38</sup>

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<sup>36</sup> For more details on all of ACA's mandatory appropriations, see CRS Report R41301, *Appropriations and Fund Transfers in the Patient Protection and Affordable Care Act (PPACA)*, by C. Stephen Redhead.

<sup>37</sup> An exemption for non-defense unobligated balances is provided in BBEDCA Section 255(e). It reads as follows: “Unobligated balances of budget authority carried over from prior fiscal years, except balances in the defense category, shall be exempt from reduction under any order issued under this part.” 2 U.S.C. §905(e).

<sup>38</sup> Table 2 in CRS Report R41301, *Appropriations and Fund Transfers in the Patient Protection and Affordable Care Act (PPACA)*, shows all the ACA appropriations by fiscal year over the period FY2010-FY2019 and, for each provision, indicates whether the funds are to remain available for an indefinite period of time (i.e., until expended, or without fiscal year limitation), subject to any requirement that the program terminate on a specific date.

## Discretionary Spending

ACA implementation will affect not only direct spending and revenues but also discretionary spending that is subject to the annual appropriations process. The law reauthorized appropriations for numerous existing discretionary grant programs and activities authorized under the PHSA, and permanently reauthorized appropriations for programs and services provided by the Indian Health Service (IHS). While the authorizations of appropriations for most programs had expired prior to their reauthorization in ACA, most of them continued to receive an annual appropriation. ACA also created a number of new grant programs and provided for each an authorization of appropriations.<sup>39</sup>

Funding for all these discretionary programs depends on actions taken by congressional appropriators, a process that may lead to greater or smaller amounts than the sums authorized by ACA. With Congress now operating under BCA's discretionary spending limits, it may prove difficult to secure funding for new programs and activities. Even maintaining current funding levels for existing programs with an established appropriations history may prove a challenge under growing pressure to reduce federal discretionary spending.

CBO estimated that ACA's discretionary spending provisions, if fully funded by future appropriations acts, would result in appropriations of almost \$100 billion over the period FY2012-FY2021 (see **Table 1**). However, most of that funding—about \$85 billion—would be for programs that were in existence prior to, and were reauthorized by, ACA; namely, the National Health Service Corps, the health centers program, and the IHS.<sup>40</sup>

In addition, CBO projected that both HHS and the Internal Revenue Service (IRS) will incur substantial costs to implement the policies and programs established by ACA. Most of these costs will have to be funded through the appropriations process. CBO estimated that the costs to the IRS of implementing the eligibility determination, documentation, and verification processes for premium and cost-sharing subsidies will probably total between \$5 billion and \$10 billion over 10 years. It further estimated that the costs to HHS for implementing the changes in Medicare, Medicaid, and CHIP, as well as some of the reforms to the private insurance market, will require similar amounts over 10 years.<sup>41</sup>

Most of the discretionary spending arising from authorizations of appropriations in ACA would be subject to automatic spending reductions triggered by the BCA. As noted earlier, discretionary spending reductions in FY2013 would be achieved through a sequestration of appropriations, whereas reductions in later years (i.e., FY2014-FY2021) would be achieved through a downward adjustment of the revised statutory spending limits. Lowering the annual spending limits would make it that much more of a challenge to maintain funding levels for existing programs. Under

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<sup>39</sup> For more details on all of ACA's discretionary spending provisions, see CRS Report R41390, *Discretionary Funding in the Patient Protection and Affordable Care Act (PPACA)*, coordinated by C. Stephen Redhead.

<sup>40</sup> U.S. Congress, House Committee on Energy and Commerce, Subcommittee on Health, "CBO's Analysis of the Major Health Care Legislation Enacted in March 2010," Statement of Douglas W. Elmendorf, Director, 112<sup>th</sup> Cong., 1<sup>st</sup> sess., March 30, 2011. Available at <http://www.cbo.gov/ftpdocs/121xx/doc12119/03-30-HealthCareLegislation.pdf>. See p. 16.

<sup>41</sup> *Ibid.*, see p. 15. Section 1105 of the Health Care and Education Reconciliation Act established a Health Insurance Reform Implementation Fund (HIRIF) within HHS and appropriated \$1 billion to the Fund to implement ACA. CBO's estimates of the amount of discretionary funding necessary to implement ACA are in addition to the funding provided to the HIRIF.

the BBEDCA sequestration rules, however, any reduction in funding for community health centers and the IHS would be capped at 2%.<sup>42</sup>

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<sup>42</sup> BBEDCA Section 256(e), 2 U.S.C. §906(e). This subsection identifies the health centers program (i.e., PHSA Section 330), which is administered by the Health Resources and Services Administration (HRSA), using the budget account identification number that applies to HRSA and all its discretionary programs and activities. But ACA, in addition to reauthorizing discretionary funding for the health centers program, provides a mandatory appropriation of \$9.5 billion over five years (FY2011-FY2015) in supplemental funds for the program through the CHCF. While any BCA-triggered reduction in discretionary spending for the health centers program would clearly be subject to the 2% cap, it would appear that the mandatory funds would not be affected by the cap. However, OMB might decide to subject both the discretionary and mandatory funds for health centers to the 2% cap, as both sources of funding are being used for the same program, notwithstanding the fact that the mandatory funds represent direct spending and are identified in the budget by a separate account number.

**Table 1. Impact of BCA's Automatic Spending Reduction Procedures on Health Reform Spending Under ACA**

Type of Spending	Estimated Cost FY2012-FY2021 (\$ billions)	Potential Impact of Spending Reductions
<b>Insurance Coverage Expansion</b>		
Medicaid/CHIP	\$627 <sup>a</sup>	The Medicaid and CHIP programs would both be exempt from a sequestration order. <sup>b</sup>
Premium tax credit	\$653 <sup>a</sup>	The refundable tax credits available to individuals and families with incomes between 133% and 400% of the federal poverty level to offset the cost of purchasing insurance coverage through the exchanges would likely be exempt from a sequestration order. <sup>c</sup>
Cost-sharing subsidy	\$117 <sup>a</sup>	The cost-sharing subsidies available to certain individuals and families receiving the premium tax credit would presumably be subject to a sequestration order.
Small employer tax credit	\$41 <sup>a</sup>	The tax credits available to certain small businesses and small tax-exempt organizations to offset the cost of covering their employees would presumably be subject to a sequestration order. <sup>d</sup>
<b>Mandatory Appropriations</b>	>\$100 <sup>e</sup>	The mandatory appropriations in ACA would, in general, be subject to direct spending reductions under a sequestration order. However, for any given fiscal year in which sequestration was ordered, only new budget authority for that year (including advance appropriations that first become available for obligation in that year) would be reduced. Unobligated balances carried over from previous fiscal years would be exempt from a sequestration order. <sup>f</sup>
<b>Discretionary Spending</b>	≈\$100 <sup>g</sup>	Most of the discretionary spending arising from authorizations of appropriations in ACA would be subject to automatic spending reductions. Discretionary spending reductions in FY2013 would be achieved through a sequestration of appropriations, whereas reductions in later years (i.e., FY2014-FY2021) would be achieved through a downward adjustment of the revised discretionary spending limits. Under the BBEDCA sequestration rules, however, any reduction in funding for health centers and the Indian Health Service would be capped at 2%. <sup>h</sup>

**Source:** Table prepared by the Congressional Research Service based on the text of the Patient Protection and Affordable Care Act (ACA, as amended), the Budget Control Act (BCA), and the Balanced Budget and Emergency Deficit Control Act (BBEDCA, as amended).

- a. CBO's March 2011 baseline projections of federal spending on ACA's insurance coverage provisions.
- b. Medicaid and CHIP are among the exempted low-income programs listed in BBEDCA Section 255(h).
- c. While the ACA premium tax credits are not specifically exempted from sequestration, BBEDCA Section 255(d) provides a general exemption for refundable individual tax credits.
- d. BBEDCA Section 255 does not include small employer tax credits among the list of programs and activities that are exempt from sequestration.
- e. It is not possible to determine the total amount appropriated by ACA over the period FY2012-FY2021. Several appropriations are for unspecified amounts (i.e., such sums as may be necessary) or contingent upon a formula or revenues from industry fees. For more details on all of ACA's mandatory appropriations, see CRS Report R41301, *Appropriations and Fund Transfers in the Patient Protection and Affordable Care Act (PPACA)*, by C. Stephen Redhead.

- f. An exemption for non-defense unobligated balances is provided in BBEDCA Section 255(e).
- g. This figure is CBO's estimate assuming that all ACA's discretionary spending provisions are fully funded by future appropriations acts. For more details on all of ACA's discretionary spending provisions, see CRS Report R41390, *Discretionary Funding in the Patient Protection and Affordable Care Act (PPACA)*, coordinated by C. Stephen Redhead.
- h. See footnote 42.

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