Cato Blog Post – June 2015

One Consequence of King v. Burwell

Some say that today's decision maintains business as usual for Obamacare, taxpayers and consumers. The Supreme Court upheld the subsidies (also known as the Premium Tax Credit) to consumers in the 34 states that rely on the federal exchange. Proponents of these subsidies argue they help keep health insurance affordable.

The subsidies lower the out-of-pocket cost to consumers who get them, but at what cost? Consider a 64-year-old consumer in Hialeah, Florida (one of the largest areas impacted by King v. Burwell) who is receiving the maximum subsidy of $7,488 per year. Of the 87 plans offered in the marketplace, 16 entail zero cost to the consumer. Premiums for these "free" plans range from $6,300 to $7,200. There is no incentive for the consumer to shop prudently from these 16 plans. The consumer does not get to keep any unused subsidy, creating incentives to choose health plans with additional features of only marginal value. The taxpayer – not the consumer – picks up the cost of the imprudent choices.

In addition to discouraging shopping based on plan value, the premium tax credit offers a set of perverse incentives, especially on the decision to earn more than 400% of the poverty line and on reporting your income for the upcoming year.

Today's decision may very well mean business as usual, but there are serious economic issues with how the subsidy is set up.

Aaron Yelowitz is an associate professor in economics at University of Kentucky and a Visiting Scholar at Cato Institute.