

## RESEARCH SUMMARY

## The Hidden Subsidy of the Affordable Care Act

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The expansion of Medicaid under the Affordable Care Act (ACA) allowed state policymakers to shift the program's costs to the federal government by reclassifying enrollees. In "The Hidden Subsidy of the Affordable Care Act," Liam Sigaud, Markus Bjoerkheim, and Vitor Melo show how this strategic reclassification contributed to the growth of Medicaid and underscores the need for better-designed incentives to ensure the program can effectively support Americans in need.

### Medicaid Expansion and Enrollee Reclassification

Medicaid is the single largest source of health insurance in the United States. It provides coverage to an estimated 85 million people and costs the federal government and states approximately \$750 billion per year. Under the ACA, Medicaid coverage was expanded to millions of new adults.

States that opted to expand Medicaid received enhanced federal matching for newly covered individuals and could save up to 100 percent of the costs on those previously enrolled by reclassifying them as part of the newly eligible group. Given that Medicaid expenditures represent about one-fifth of states' general fund expenditures on average, reclassifications could constitute a substantial hidden subsidy from the federal government to the states.

### Estimating the Impact of Enrollment Changes

In some cases, the reclassifications of Medicaid enrollees that occurred were permitted under the ACA and other federal rules. But in other cases, states may have deliberately reclassified enrollees in violation of federal law. Irrespective of their legal status, such reclassifications are financially attractive to states and have had substantial—if different—fiscal implications for states and the federal government.

- **Federal:** The federal government distributed \$52.9 billion to states from 2014 to 2019 as a result of enrollee reclassifications, including \$8.3 billion in 2019 alone. Reclassifications increased federal costs by 18.2 percent.
- **States:** Despite larger-than-expected enrollment, the fiscal impact of Medicaid expansion has been small for states. Indeed, for some of them, Medicaid expansion appears to have been a net fiscal benefit. The hidden subsidy from the ACA helped states offset the direct costs of expansion.

### **Realigning Incentives for the States**

Examining the fiscal effects of Medicaid expansion suggests state policymakers are sensitive to incentives created through the program's joint financing structure. Accounting for such strategic behavior by states is crucial to accurately predict the effects of policy changes to Medicaid and similar federal/state programs. More stringent monitoring of states' enrollment practices, as well as use of federal block grants or other alternative financing methods, could mitigate this kind of outcome.