



When It Comes to Health Insurance, Federal Dollars Support More Than ACA Plans

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February 23, 2026 By Julie Appleby and KFF Health News

Subsidies. Love 'em or hate them, they dominated the news during the Affordable Care Act's sign-up season, and their reduction is now hitting many enrollees in the pocketbook.

While lawmakers continue to disagree on a way forward, [and the politics of affordability](#) keeps the issue front and center, it would be understandable to think these are the only taxpayer-funded health insurance subsidies in the U.S. system.

But [that would be wrong](#).

"The vast majority of people with health insurance [get some kind of federal subsidy](#) for it, from Medicaid to Medicare to the ACA to employer-sponsored insurance," said Larry Levitt, executive vice president for health policy at KFF, a health information nonprofit that includes KFF Health News.

These broad taxpayer supports are rarely discussed, though, as they apply to work-based coverage. So, let's take a look.

Adding Up the Tax Breaks

[Nearly half](#) of the more than [\\$1.1 trillion in annual spending](#) on Medicare, the second-largest program in the federal budget behind Social Security, comes from general federal funds. The rest comes from payroll taxes and the monthly premiums paid by enrollees, who number [more than 66 million](#).

Medicaid — the nation's largest health insurer, covering more than 70 million low-income people — costs [more than \\$918 billion](#) annually. It's jointly financed by the federal government (65%) and states (35%).

For both programs, expenses are partially funded with taxpayer dollars. A less obvious form of federal support comes through employer-sponsored health coverage. Here, the impact on the federal bottom line is less visible, as hundreds of billions of dollars never reach the U.S. Treasury because it takes the form of tax breaks for employers and workers.

“It’s a world apart from Medicare, Medicaid, and Obamacare — from the government writing checks to people,” said Michael Cannon, director of health policy studies at the libertarian Cato Institute.

Job-based insurance provides coverage for [at least 154 million people](#) under age 65. (By comparison, about 23 million people enrolled in Affordable Care Act plans for this year, generally because they don’t have job-based insurance. Extending the enhanced ACA subsidies that expired at the end of 2025 [would cost about \\$350 billion](#) over a decade, or roughly \$35 billion annually.)

In fact, contributions to employer-sponsored health plans are the single-largest “exclusion” — a tax policy that allows certain income to be exempt from taxes — in the federal budget. For this fiscal year, the [estimated amount is \\$451 billion](#), according to the Joint Committee on Taxation and the Congressional Budget Office.

The money employers spend to offer health coverage to their employees can be written off as a business expense. And workers who receive this benefit don’t have to pay income or payroll taxes on its value.

[Those tax savings can be worth hundreds](#) or even thousands of dollars a year for workers. The amount varies, with the biggest breaks going to those with the most expensive health plans and those whose wages put them in the upper tax brackets. Contributions to health savings accounts [are among other tax breaks](#) related to health insurance.

But the exclusion can be a difficult concept for insured workers to wrap their heads around, as most employees still contribute a portion of their pay to health coverage.

Even though they’re not taxed on that, “it doesn’t necessarily feel like a subsidy to people,” Levitt said. “They do feel like they’re paying.”

Baked Into the Tax System

The tax treatment evolved along with work-based health insurance policies in the U.S., fueled during World War II, when wage and price controls spurred interest in offering health coverage to lure workers. It was enacted into tax law in 1954.

Backers, which often include labor unions and employers, say it encourages companies to offer health insurance, as most large companies do. Because of the cost, smaller companies are less likely to do so, even with the tax incentive. Also, for workers, getting \$1 of health care coverage is worth more than an extra dollar in wages, which would be taxed and, thus, worth less.

Opponents of the tax break, however, note the lost revenue to the Treasury and that the tax

exclusion, according to some economists, leads employers and workers to choose the most generous — and expensive — health insurance offered, which they say drives up health care spending. The tax break benefits wealthier workers more than those in lower-income tax brackets, and economists also say the amounts employers pay for health insurance might otherwise be spent on boosting workers' wages.

While there is currently no pending legislation to modify the tax break, the growing federal deficit has some [employer groups worried](#) the policy will change. Benefit experts say the outcome would vary.

"It's not clear that it would wind up in increased wages for everyone," said KFF's Levitt. "Some workers have more negotiating leverage than others."

[Decades of efforts](#) to cap or eliminate the exclusion have all failed.

"It's had a bipartisan target on its back for 40 years," said Paul Fronstin, a director at the Employee Benefit Research Institute, a private, nonprofit, nonpartisan organization.

Any change, however, "would raise some revenue, but it's also a tax increase for workers," Fronstin noted. "What would that mean, if their taxes go up? Do wages go up because they're not getting the same tax breaks? There will be winners and losers in that equation."

Still, because job-based coverage is the way so many Americans get health insurance, some policy experts warn that eliminating or even lowering the exclusion could remove an incentive for employers to offer coverage. While some employers would likely keep offering coverage even without the tax break — because it is a benefit that helps attract and retain workers — it is a huge expense, so others might drop it. Average family premiums cost an employer nearly \$27,000 last year, [according to KFF](#).

"These are businesses, which weigh the costs of offering insurance, which have gone up dramatically," said Elizabeth Mitchell, CEO of the [Purchaser Business Group on Health](#), an organization of large public and private employers that offer health insurance to their workers. "If there's not some sort of tax incentive, I would expect them to revisit whether they would bear those costs."

Cannon, of the Cato Institute, considers the tax policy bad because it takes choice away from workers, who might rather have increased wages, even if they are taxed. Those additional wages, he argues, could then be invested in tax-advantaged health savings accounts, used to pay medical costs.

Under the current tax break approach, "you are effectively saying let the employer control a huge chunk of your earnings and enroll in the plan the employer chooses," he argues.

Employers counter by saying they are better able to negotiate higher-quality, lower-cost health insurance packages than individuals could on their own.

Mitchell, at the employer group, said, “It is challenging for an enormous employer to negotiate fair prices with the large consolidated systems. So it’s hard to imagine how an individual would be able to navigate our current system.”

She also disputes arguments that the tax break leads to higher health care prices, driven by overly generous employer plans that lead insured workers to use more health services.

“That’s a tired economic theory that doesn’t apply in health care,” she said. “People don’t shop for health care because they want more of it. They use health care because they need it. It’s fundamentally different.”

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