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**FISCAL IMPACT STATEMENT**

**LS 7713**

**BILL NUMBER:** SB 459

**NOTE PREPARED:** Feb 24, 2005

**BILL AMENDED:**

**SUBJECT:** Health benefit plan credit.

**FIRST AUTHOR:** Sen. Dillon

**BILL STATUS:** CR Adopted - 1<sup>st</sup> House

**FIRST SPONSOR:**

**FUNDS AFFECTED:**  **GENERAL**  
 **DEDICATED**  
 **FEDERAL**

**IMPACT:** State & Local

**Summary of Legislation:** The bill allows certain employers to take a tax credit related to making a health benefit plan available to the employers' employees.

**Effective Date:** July 1, 2005.

**Summary of Net State Impact:** (Revised) The estimated net impact of the bill is summarized in the table below:

<b>Revenue Base (millions)</b>	<b>FY 2006</b>	<b>FY 2007</b>	<b>FY 2008</b>	<b>FY 2009</b>
Adjusted Gross Income Tax				
Employer Health Benefit Plan Tax Credit	(0.6 M)	(0.6 M)	(0.6 M)	0
Employee Health Benefit Plan Premium Exclusion	0	0	(3.7 M)	(3.7 M)
Insurance Premiums Tax	1.2 M	1.2 M	1.2 M	1.2 M
Net Revenue Gain (Loss)	0.6 M	0.6 M	(3.1 M)	(2.5 M)

**Explanation of State Expenditures:** The Department of State Revenue (DOR) would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to incorporate this tax credit. The DOR's current level of resources should be sufficient to implement these changes.

**Explanation of State Revenues:** (Revised) A health benefit credit equal to \$50 per enrolled worker and capped at \$2,500 for employers (with 10 or more workers) providing health benefits to their employees for the first time will decrease Adjusted Gross Income Tax and Financial Institutions Tax liabilities for businesses during the two years of the credit and in following years as the carryforward is used.

The bill could also increase Insurance Premiums Tax revenues as more insurance policies are underwritten in the state. For the first two years that an employee participates in the health benefit plan, there will be no effect on the state Adjusted Gross Income Tax liabilities of individuals. The increase in Insurance Premium Tax revenues may partially mitigate the decrease in AGI tax liabilities, the extent to which will be determined by the amount of existing Insurance Premium Tax credits that health insurance companies currently take and carry forward.

The following assumptions are used to calculate the estimates: (1) All businesses currently not offering health benefits offer them and take the credit; (2) 10% of a business's employees participate in the health benefit plan.

**Adjusted Gross Income Tax Impact:** The bill establishes a credit for employers with 10 or more workers that offer at least one health benefit plan to employees for the first time. The credit is equal to the lesser of \$2,500 or \$50 for each enrolled employee and can be taken for two years. An employer claiming the credit must offer health insurance for at least 24 consecutive months after the taxable year in which the health insurance plan is initially offered. The bill contains a "claw-back" provision where employers who fail to meet this requirement have to pay back the tax credit. The credit is nonrefundable, but unused credit may be carried forward to subsequent years. The tax credit may not be carried back to previous years. In addition, the bill requires that an employer claiming the credit notify employees who participate in the health benefit plan of the amount of the employee's eligible benefits that are included in the employee's state adjusted gross income for the first and subsequent taxable year after the employer takes the credit. Eligible benefits are the total amount of health insurance premiums withheld from the employee's federal adjusted gross income. The credit is available beginning January 1, 2006.

The impact of this bill is a function of the number of employers with 10 or more workers currently not providing a health benefit plan to employees that choose to offer a health benefit plan and take the tax credit.

Recent survey results suggest that in 2003 there were approximately 7,585 Indiana businesses with 10 or more employees that did not offer a health benefit plan. Of these businesses, a number of them would have sufficient tax liability to take the full credit in a given year. *The employer tax credit is estimated to decrease the income tax liabilities of businesses by \$0.6 M in FY 2006 and FY 2007.* The carryforward for each year is estimated to total \$0.3 M. The carryforward could potentially be used in FY 2008.

The bill requires that the health benefit plan established by employers satisfy the requirements of Section 125 of the IRS Code. This section of the IRS Code allows employees (and employers) to pay their share of insurance premiums with pre-tax dollars which reduces the employee's taxable income and employer's FICA and unemployment insurance payments. The employee's use of pretax dollars to pay for health insurance would decrease state individual income tax revenues, therefore the bill requires that insurance premiums of employees who participate in the health benefit plan be included in the employee's state Adjusted Gross Income for two years. *After two years, the premiums are not added back to state AGI which will decrease individual AGI tax revenues by approximately \$3.7 M per year.* This estimate is based on the following assumptions: (1) employers offering a health benefit plan for the first time as a result of the bill would require participating employees to pay all or a substantial portion of the insurance premium, which would reduce the participation

rate among employees. A 10% participation rate is used to calculate the estimates. (2) Employees pay health insurance premiums with pre-tax dollars, and employers do not pay a portion of the premium.

Revenue from the corporate AGI tax and the Financial Institutions Tax is deposited in the state General Fund. Eighty-six percent of the revenue from the individual AGI Tax is deposited in the state General Fund, and 14% is deposited in the Property Tax Replacement Fund.

***Insurance Premiums Tax Impact:*** The bill could increase revenue from the Insurance Premiums Tax as health insurance premiums written in Indiana increase. According to a recent survey, the average annual premium cost for health insurance is \$3,383 for single coverage and \$9,068 for family coverage. *The potential increase in the Insurance Premiums Tax would be approximately \$1.2 M per year.* The estimates are based on the assumptions that 10% of employees participate in the health benefit plan of employers offering the plan for the first time and workers participating in the health benefit plans are currently uninsured or not insured by another policy. A 10% employee participation rate may be conservative given that recent survey results suggest that over 84% of workers in firms offering health benefits participate in the health plan. In Indiana, approximately 12.3% of covered employees enroll in HMO plans, which do not pay the Insurance Premiums Tax. This is accounted for in these estimates.

*Note:* Information on the Insurance Premium Tax liability of health insurance companies operating in Indiana is unknown. Due to the magnitude of existing tax credits available to health insurance companies operating in Indiana and the carryforward of these credits, the increase in Insurance Premium Tax revenues from the proposed credit is likely to be lower than anticipated.

The Insurance Premiums Tax is deposited in the state General Fund.

### **Explanation of Local Expenditures:**

**Explanation of Local Revenues:** The bill requires that the employees of employers claiming the health benefit plan tax credit add back the value of the employee's health benefit contribution to AGI for the taxable year in which the employer offers health benefits and the following year. Therefore, the bill will have no impact on local option income tax revenues for these two years. After the first two years, the employee's health benefit contribution is not added back to AGI. This would decrease taxable income for these employees. As a result, counties imposing a local option income tax (CAGIT, COIT, CEDIT) would experience an indeterminable decrease in revenue from these taxes beginning two years after businesses have taken the credit.

**State Agencies Affected:** Department of State Revenue.

**Local Agencies Affected:** Counties with local option income taxes (third and subsequent years after the health benefit credit is taken).

**Information Sources:** Kaiser Family Foundation, *Employer Health Benefits 2003 Annual Survey*, available at <http://www.kff.org/insurance/ehbs2003-5-set.cfm>; and *State Health Facts Online* available at <http://www.statehealthfacts.kff.org/>; OFMA Corporate Income Tax database; Bureau of the Census, *County Business Patterns*.

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