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**FISCAL IMPACT STATEMENT**

**LS 7713**

**BILL NUMBER: SB 459**

**NOTE PREPARED: Mar 1, 2005**

**BILL AMENDED: Feb 28, 2005**

**SUBJECT:** Health Benefit Plan Credit.

**FIRST AUTHOR:** Sen. Dillon

**FIRST SPONSOR:** Rep. Leonard

**BILL STATUS:** As Passed Senate

**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:

Revenue Base (millions)	FY 2006	FY 2007	FY 2008	FY 2009
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	(1.0 M)	(1.0 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	(0.4 M)	0.2 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 FICA, and the employer's FICA and unemployment insurance tax payments. The employee's use of pretax dollars to pay for health insurance would decrease state individual income tax revenues. As a result, the bill does the following:

(1) Provides that insurance premiums paid with "pretax" dollars by employees participating in the health benefit plan must be added back to the employee's state Adjusted Gross Income (AGI) for the first two years after the health benefit plan is offered.

(2) Provides, after the first two years, that insurance premiums paid with “pretax dollars by employees whose annual income from the employer is \$80,000 or more must be added back to the employees AGI. If the employee’s income is \$40,000 but less than \$80,000, 50% of the insurance premiums paid with “pretax dollars by the employee must be added back to the employee’s AGI. If the employees income is less than \$40,000, the premiums paid by the employee with “pretax dollars do not have to be added back to the employee’s AGI.

*It is estimated that the impact of the exclusion of premium payments from AGI for employees with incomes less than \$80,000 could potentially reduce AGI tax revenue by about \$1 M annually.* This estimate is based on data relating to the distribution of certain health benefit coverage purchased at full-price for low, moderate, and high income taxpayers. The estimate also assumes that roughly 70% of the premiums paid for health plan coverage under this bill will be paid by employees with the 50% exclusion for premium payments (those with \$40,000-\$80,000 incomes) and employees with no exclusion for premium payments (those with incomes of \$80,000 and over).

The estimates are also 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:** (Revised) 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

first two years after the health benefit plan is offered. Therefore, the bill will have no impact on local option income tax revenues for these two years. After that, there are varying add back requirements depending upon the income of the employee (see Explanation of State Expenditures). This would decrease taxable income for some 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*. The Urban Institute, *Could Subsidizing COBRA Health Insurance Coverage Help Most Low-Income Unemployed?*

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