DEPARTMENT OF TAXATION
2005 Fiscal Impact Statement

1. **Patron** Benjamin J. Lambert III

2. **Bill Number** SB 1255
   House of Origin:
   X **Introduced**
   ___ **Substitute**
   ___ **Engrossed**

   Second House:
   ___ **In Committee**
   ___ **Substitute**
   ___ **Enrolled**

3. **Committee** Senate Finance

4. **Title** Income Tax: Employer Tax Credit for Health Insurance Premiums or Health Savings Accounts Premiums

5. **Summary/Purpose:**

This bill would provide a tax credit against the corporate or individual income tax for employers who pay for at least one-half of the annual health insurance premiums for each employee or who make an annual contribution to the employee's health savings account equal to one-half of the amount in the account. The credit would be equal to the lesser of the amount paid during the taxable year in premiums or contributions, or $500 per employee.

In addition, a credit would be available to an employer who paid at least ten percent of the annual health insurance premium for an employee's dependent. This credit would be equal to the lesser of the actual amount paid or $100 and would only be available for one dependent per employee.

These credits would be available to employers with businesses having 50 or fewer full-time employees. The total amount of credits available to each employer annually would be limited to $30,000; and any tax credit not used for the taxable year could be carried over for the next three years or until the full amount of the credit was used, whichever is sooner.

This bill would be effective for taxable years beginning on or after January 1, 2006.

6. **No Fiscal Impact or Fiscal Impact Estimates are:** Preliminary. (See Line 8.)

6a. Expenditure Impact:

Fiscal Year	***Dollars***	***Fund***
2004-05	$0	GF
2005-06	$27,600	GF
2006-07	$161,592	GF
2007-08	$10,550	GF
2008-09	$10,866	GF
2009-10	$11,193	GF
2010-11	$11,529	GF

7. **Budget amendment necessary:** Yes.
   ITEM(S): <u>284 and 286, Department of Taxation</u>

8. **Fiscal implications:**

   The Department would incur administrative costs of $27,600 for FY 2006, $161,592 for FY 2007, $10,550 for FY 2008, $10,866 for FY 2009, $11,193 for FY 2010, and $11,529 for FY 2011 for forms and systems modifications.

   The revenue impact of this bill is unknown, but is expected to be substantial. In 2002, there were 113,016 businesses with fifty or fewer employees, with an average of 6 employees per business. Out of those businesses, 26,518 offer at least one insurance plan that requires no employee contribution and potentially qualify for the $500 credit. Another 14,271 businesses offer at least one insurance plan that requires no employee contribution for family coverage and potentially qualify for the $100 credit. If all of these employers claim both credits, there would be an annual negative revenue impact of $93 million. In addition, 450,032 employees work in firms where some type of health insurance is offered. If all of their employers also qualified for the maximum credit amounts, the annual revenue loss would be $270 million.

9. **Specific agency or political subdivisions affected:**

   Department of Taxation

10. **Technical amendment necessary:** No

11. **Other comments:**

    <u>General</u>

    In 2003, the federal government passed legislation allowing for the creation of health savings accounts ("HSA"), which are tax-sheltered savings accounts earmarked for medical purposes. Taxpayers must be covered by a High Deductible Health Plan (HDHP) is order to qualify for an HSA. In general, an HDHP is an inexpensive health insurance plan that does not pay for the first several thousand dollars of health care expenses.

    A taxpayer must have a minimum HDHP deductible of at least $1,000 for self-coverage or $2,000 for family coverage in order to open an HSA. In addition, annual out-of-pocket expenses, including deductibles and co-pays, cannot exceed $5,100 for self-coverage or $10,200 for family coverage.

    The amount that can be contributed to an HSA is limited. The annual contribution to an HSA cannot exceed the deductible of the HDHP. In addition, for 2005, the amount cannot exceed $2,650 for self-coverage or $5,240 for a family. Those over 55 may make special catch-up contributions. Contributions made to HSAs may be deducted on the federal income tax return as an above-the-line deduction or employees may choose to make a pre-tax contribution if their employers offer "cafeteria" plans. Thus, these contributions are also not included in Virginia taxable income.

Federal Treatment

Federal law allows businesses to deduct premiums paid for health insurance as a business expense. Contributions made to an employee's health savings account are also allowed to be deducted as a business expense. These contributions, however, must be within the prescribed limits, as discussed above.

Proposal

This bill would create two income tax credits for employers. The first would be for employers who pay for at least one-half of the total annual health insurance premiums for each employee. An employer would also qualify if he made an annual contribution to an employee's health savings account equal to one-half of the amount in such account. The amount of this credit would be equal to the amount paid for premiums or contributed by the employer during the taxable year or $500 per employee, whichever was less.

The second credit would be for employers who pay at least ten percent of the annual health insurance premium for an employee's dependent. This credit would be available for one dependent per employee and would be equal to the lesser of the amount paid for the employee's dependent or $100.

Both of the proposed credits would only be available to employers with businesses employing fifty or fewer employees and would only be available to the extent that the employer did not claim a deduction for federal income tax purposes for the amount of the premium costs or contributions. The total amount of these credits allowed to each employer would not be allowed to exceed $30,000. If an employer were not able to use a credit during the taxable year, he would be allowed to carry over the credit for the next three taxable years of until the full credit was used, whichever was sooner.

In order to claim these credits, this bill would require employers to attach proof of payment of the premium costs or contributions to his income tax return.

This bill would be effective for taxable years beginning on or after January 1, 2006.

Other Legislation

House Bill 2513 and **Senate Bill 1041** would allow an individual or a corporate income tax credit to taxpayers who operate businesses in the Commonwealth and who provide benefits packages to employees, which include long-term care insurance. The amount of the credit would be equal to ten percent of the long-term care insurance premiums incurred during the taxable year. However, the total amount of the credit would not be allowed to exceed $5,000 or $100 per employee, whichever is less.

House Bill 2864 would provide an individual income tax credit for health insurance premiums and health savings accounts contributions paid by an individual for him or his dependents during the taxable year. The amount of the credit would be limited to $1,000.

Senate Bill 1097 would require the Department of Taxation and the State Corporation Commission to amend the Virginia Medical Savings Account Plan and provides several criteria for the new plan, which would be called the Virginia Health Saving Account Plan. The Department and the Commission would be required to present the new plan to various General Assembly committees by January 1, 2006.

cc : Secretary of Finance

Date: 1/24/2005 AMS
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