

Income Tax Credit for Small Business Health Benefits

-An Analysis-

This paper assesses a proposal to provide an \$800 annual state income tax credit per employee to businesses with 10 or fewer employees if they offer health care coverage to their full-time workers and pay at least 50 percent of the premium.

Currently, just under 24,000 Idaho businesses have payrolls of 10 or fewer. Those businesses employ a total of just over 81,500 people.

Based on responses to the state's fringe benefit survey and other data, only 13.5 percent of the employees are enrolled in health insurance programs with their employers.

Under the proposed incentive legislation, those employers combined would automatically receive \$8.8 million in credits without changing their compensation policies. That would be a reduction in income tax revenue to the state general fund.

The cost of the credit would rise should the incentive encourage other employers to provide health insurance coverage and pay at least 50 percent of the premium.

It is, however, extremely difficult to determine whether this legislation will result in significantly more small business employees becoming insured. The insurance premium share can still be prohibitive for certain business budgets. The Bureau of Labor Statistics estimated that during the third quarter of 2006 employers in the Mountain Region of the United States, which includes Idaho, paid on average \$1.56 an hour for health insurance for their workers, an annual cost of \$3,244.80 for a full-time employee.

Additionally, the impact on the first year might be pronounced only to decline in following years if employers drop insurance coverage because premium inflation has eroded the value of a fixed \$800 tax credit.

To avoid the possibility of eroding participation by employers as premiums escalate, this tax credit could be indexed to the cost of inflation or another measure of value depreciation to avoid the credit becoming obsolete and irrelevant.

Alternatively, if the \$800 is indexed to a measure of value depreciation, the \$800 in 2007 will increase year after year, boosting the impact on general fund revenues whether additional employees are offered health coverage at 50 percent or less of the premiums by their employers.

Detail Information

Total employers with 10 or fewer full-time employees: 23,886
Total full-time employees: 81,520

Commerce & Labor estimates 55.6 percent, or 13,281, of these employers currently offer health insurance benefits and pay at least 50 percent of the premium for the 32,282 people they employ. The best estimate is that only 34 percent of those full-time employees, 10,976, actually take advantage of the benefit. That group represents 13.5 percent of the total small business payroll of 81,520.

Financial Impact of the Small Business Health Insurance Tax Credit

Employees already enrolled in plans qualifying for the credit – about two of every 15 – would automatically earn their employers \$8,780,800 in state income tax credits

If the tax incentive results in doubling the employee insurance coverage to four of every 15 employees, the additional credits worth \$8,780,800 would increase the total cost of the incentive to \$17,561,600. That would raise small business employee health insurance coverage to 27 percent.

Since the current level of health coverage by small employers has been achieved without this proposed tax incentive, providing an \$800 per employee credit to double existing coverage levels essentially translates into a cost to the state general fund of \$1,600 per employee added to the employer health coverage rolls.

Should all eligible employers revise compensation policies to qualify for the tax credit, the assumption is that the number of employees enrolling would remain about the same as it currently is at 34 percent. That would mean the number of employees participating in plans qualifying for the incentive would total 27,716, and the cost of the tax credit to the state would total \$22,172,800 at the current levels of employment.

Salvador Vazquez
Research and Analysis Supervisor
January 2007

Source: Compiled from the Idaho Fringe Benefits Survey and employment data. Idaho Commerce & Labor.