Department of Legislative Services

Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE

House Bill 279 (Delegate Costa, *et al.*)
Ways and Means

Income Tax - Subtraction Modification for Contributions to Health Savings Account

---

This bill creates a subtraction modification under the State income tax for an employer who contributes to the Health Savings Accounts (HSAs) of its employees. The amount of the subtraction modification is 40% of the amount contributed. In order to qualify, the employer is required to contribute at least $500 and comply with applicable contribution rules as stated under Sections 125 and 4980G of the Internal Revenue Code.

The bill takes effect July 1, 2005 and applies to tax years 2005 and beyond.

Fiscal Summary

State Effect: The extent of any State revenue decrease depends on the number of businesses that contribute to HSAs and the amount contributed. Under one set of assumptions, State revenues could decrease by approximately $1.1 million annually beginning in FY 2006. No effect on expenditures.

Local Effect: Local income tax revenues would decrease by approximately 3.1% of the State subtraction modification taken in each year. Based on the assumptions above, local income tax revenues could decrease by approximately $705,000 annually beginning in FY 2006. No effect on expenditures.

Small Business Effect: Potential meaningful.

Analysis

Current Law: No similar State subtraction modification exists.

Background: The federal Medical Prescription Drug, Improvement, and Modernization Act of 2003 (P.L. 108-173) provides that workers with high-deductible health insurance can make pre-tax contributions to HSAs of up to $2,600 each year ($5,150) to cover health care costs. Any amount paid or distributed out of an HSA which is used exclusively to pay the qualified medical expenses of any account beneficiary cannot be included in gross income. HSAs may be set up beginning January 1, 2004. Unlike flexible spending accounts, HSA balances can be rolled over from year to year. In order to qualify for an HSA, an individual must be covered by a high-deductible health plan and not also covered under a nonhigh deductible plan. A high-deductible plan is defined as a plan that has at least a $1,000 annual deductible for self-only coverage and a $2,000 deductible for family coverage. These amounts are indexed for inflation.

According to a nationwide survey conducted in 2004 by Mercer Human Resource Consulting, 19% of all companies said they were very likely to offer high-deductible plans by 2006. An additional 54% said they were somewhat likely. Due to small business' relative inability to absorb increased health care costs relative to larger companies, it is estimated companies that offer high-deductible plans are small businesses.

State Revenues: The actual cost of the bill, which cannot be reliably estimated at this time, depends on the number of businesses that contribute to HSAs and the amount contributed.

However, *for illustrative purposes only,* general fund revenues could decrease by approximately $1.1 million in fiscal 2006. This estimated is based on the following facts and assumptions:

- in 2003 approximately 51,000 Maryland small businesses provided health insurance coverage to approximately 253,000 individuals;
- it is estimated that 60% of these small businesses offer high-deductible health insurance;
- of the small businesses that offer high-deductible health insurance, 50% provide funds into employees' HSAs;
- the average employer contribution per employee is $750; and
- the subtraction modification will be taken against the personal income tax.

It is estimated the revenue losses resulting from larger businesses is minimal. To the extent that larger businesses offer HSAs, revenue losses would be greater than estimated.

Small Business Impact: Small businesses that contribute to HSAs and claim the subtraction modification would benefit.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Bureau of Labor Statistics, U.S. Census Bureau, Maryland Insurance Health Care Commission, Department of Legislative Services

Fiscal Note History: First Reader - February 22, 2005
mam/hlb

Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510