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LIP SERVICE BUT LITTLE ELSE: FAILURE OF THE SMALL BUSINESS HEALTH INSURANCE TAX CREDIT

HEARING

BEFORE THE

SUBCOMMITTEE ON ECONOMIC GROWTH, TAX AND CAPITAL ACCESS

OF THE

COMMITTEE ON SMALL BUSINESS
UNITED STATES
HOUSE OF REPRESENTATIVES

ONE HUNDRED FOURTEENTH CONGRESS

SECOND SESSION

HEARING HELD
MARCH 22, 2016

Small Business Committee Document Number 114–051
Available via the GPO Website: www.fdsys.gov

U.S. GOVERNMENT PUBLISHING OFFICE

99–544 WASHINGTON : 2016

For sale by the Superintendent of Documents, U.S. Government Publishing Office
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Questions for the Record:	
None.	
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None.	
Additional Material for the Record:	
None.	

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TUESDAY, MARCH 22, 2016

HOUSE OF REPRESENTATIVES,
COMMITTEE ON SMALL BUSINESS,
SUBCOMMITTEE ON ECONOMIC GROWTH,
TAX AND CAPITAL ACCESS,
Washington, DC.

The Subcommittee met, pursuant to call, at 10:00 a.m., in Room 2360, Rayburn House Office Building. Hon. Tim Huelskamp [Chairman of the Subcommittee] presiding.

Present: Representatives Huelskamp, Hanna, Kelly, and Chu.

Chairman HUELSKAMP. Good morning. Thank you all for being with us today. I call this hearing to order.

Six years ago tomorrow, the Patient Protection and Affordable Care Act of 2010, otherwise known as "Obamacare," was enacted. It imposed a host of new obligations and taxes on insurance companies, individuals, and employers, including small businesses. These new burdens included an individual mandate, which requires that most individuals have health insurance and an employer mandate, requiring that most employers provide health insurance for their employees. In both cases, noncompliance results in significant penalties. Fortunately, employers with fewer than 50 employees were exempted from the employer mandate. However, their employees are still subject to the individual mandate and must have insurance. As we all know, many businesses with more than 50 employees can hardly be termed large, yet those businesses are ineligible for the exemption.

In order to provide an incentive for the smallest of the small, those employers with fewer than 25 employees, to provide employee health insurance, a small business health insurance tax credit was included to offset the cost to the employer. Like so many other parts of Obamacare, this was another case of over-promise and under deliver. Multiple assessments, both during initial implementation and now today, years down the road, have made it abundantly clear the credit scheme is so cumbersome and poorly designed that it is largely ineffective. As the credit's useful life comes to a close, today's hearing will reevaluate its efficacy from several different perspectives.

I would like to thank our witnesses for coming today, and I look forward to your testimony. I now yield to Ranking Member Chu for her opening remarks.

Ms. CHU. Thank you, Mr. Chair.

Before the Affordable Care Act was enacted, the rising cost of health care was one of the biggest worries for small companies and their employees. The ACA introduced many substantial changes to the insurance market with the hopes of making quality health care affordable for small employers.

One way in which the ACA helped make health insurance more accessible to small companies was through the Small Business Health Care Tax Credit. The ACA provided $40 billion in tax assistance through the Small Business Health Care Tax Credit and was made available immediately upon its enactment. This credit aimed to make healthcare coverage attainable for the smallest of businesses. Research has shown that the fewer employees a company has, the less likely it is that the business offers health insurance. For example, businesses with between 3 and 9 employees only offer rates of 46 percent. This is a stark contrast from their larger counterparts with more than 50 employees that offers a rate of over 95 percent.

The tax credit was designed for businesses that are small. However, while the credit was originally estimated to support between 1.4 million to 4 million small employers, the use of the credit by small employers was much lower than projected. While final data on the use of the credit is still being collected and analyzed, the most current information shows its use to be low among eligible businesses.

Although there are some conflicting reports on the actual use of credit, the numbers are disappointing. For instance, the final IRS data for 2010 indicates 335,600 claims were made, but another report by the GAO found that only 170,300 small employers claimed the credit. But both show the same thing: few small businesses are taking advantage of a critical tax credit that would benefit them greatly.

Today's hearing serves as a way for us to examine the tax credit and learn what challenges faced small businesses attempting to use the credit. Most recently, the GAO concluded that nearly 168,000 employers claimed the credit in 2012. Despite few employers using the credit, nearly 1 million employees obtained employer-sponsored health coverage through businesses claiming the credit.

It is clear that the low adoption rates by small businesses were caused by numerous factors. The single greatest factor was the lack of awareness surrounding how the credit actually worked. The complexity of the calculations and requirements to be met were daunting for small employers with limited time and resources. Another challenge for small firms was meeting the stringent eligibility rules to be fully qualified for the credit. Strict salary requirements and employee counts had to be met. This added to the complexity and credit amount available. A final challenge was the delay in the Small Business Health Options Program, or SHOP Exchanges.

Despite these problems, small employers and the healthcare industry in general are experiencing some benefits. More workers are obtaining health coverage and are now able to start their own businesses or change jobs without fear of losing their insurance. Additionally, we have seen per capita healthcare spending grow at its lowest rate on record for any 3-year period, and the uninsured rate

drop. Premium rates are decreasing in some states and stabilizing in others. In fact, the average premium for employer-based family coverage grew a relatively modest 4.2 percent in 2015. This continues the trend of slow growth with the last 4 years accounting for the lowest growth rate since 1999. These lower rates are in part due to more competition in the market.

This hearing will show just how critical the tax credit was to small firms wishing to offer health coverage and highlight areas where improvements could have been made. We will hear today why expanding and improving and strengthening the credit should have been done while it mattered most to our small employers.

I would like to welcome all the witnesses and thank them for being here today. Thank you, and I yield back.

Chairman HUELSKAMP. Thank you.

If Committee members have an opening statement prepared, I ask that they be submitted for the record.

I would like to take a moment to explain the timing lights for each of our witnesses. You each have 5 minutes to deliver your testimony. The light will start out as green. When you have 1 minute remaining, the light will turn yellow. Finally, at the end of your 5 minutes, it will turn red. I ask that you try to adhere to this time limit.

Our first witness is James McTigue, Director of Strategic Issues at the GAO, overseeing their audits of the IRS on a wide range of issues relating to tax administration and policy. He has 25 years of GAO audit experience across a variety of agencies and programs. Mr. McTigue holds a bachelor's degree in economics from Brown University and master's degree in public and private management from the Yale School of Management. I appreciate you being with us today, Mr. McTigue, and you may begin.

STATEMENTS OF JAMES R. MCTIGUE, JR., DIRECTOR, STRATEGIC ISSUES, UNITED STATES GOVERNMENT ACCOUNTABILITY OFFICE; HAROLD JACKSON, EXECUTIVE CHAIRMAN, BUFFALO SUPPLY, INC.; HOLLY WADE, DIRECTOR, RESEARCH AND POLICY ANALYSIS, NFIB RESEARCH FOUNDATION; MICHAEL RICCO, QUALITY MANAGER, AEEC, LLC

STATEMENT OF JAMES R. MCTIGUE, JR.

Mr. MCTIGUE. Thank you, Mr. Chairman, Ranking Member Chu, Congressman Hanna. I am pleased to be here today to discuss our work on small employers' use of the health insurance tax credit.

The tax credit was established as part of the Patient Protection and Affordable Care Act to help small employers provide health insurance for their employees. Our findings indicate that use of the credit has continued to be lower than expected, limiting the effect of the credit on expanding health insurance coverage through small employers.

As we discussed in our 2012 report, small, low-wage employers historically have not offered insurance for three reasons. First, health insurance is expensive and drives up the cost of labor. Second, lower-wage employees generally prefer cash over benefits. And third, insurers of small employers face high costs and are less able

to pool risk across many employees. As a result, plans for small employers are likely to have higher premiums and fewer benefits.

Government estimates indicate that about 86 percent of employers who may have been eligible for the full credit and 76 percent who may have been eligible for a partial credit did not offer their employees health insurance in 2013. While government and industry estimates place the number of eligible employers somewhere between 1.4 and 4 million, only about 181,000 employers claimed the credit in 2014. This is down slightly from 2010 as shown in Figure 1 of my statement.

In our 2012 study, we identified four key reasons why small employers did not claim the credit based on interviews with groups representing small employers, tax preparers, insurance brokers, as well as discussion groups with small employers themselves. First, the amount of the credit is too small to influence employers to offer or maintain insurance. This is because few small employers actually qualify for the maximum credit since the credit is phased out to zero as the number of employees reach 25 full-time equivalents and average wages approach $52,000. And the credit is limited to the average premium in the small group market in the State.

In our report, we found that only about 17 percent of employers who claimed the credit in 2010 were eligible for the full amount. Usually, employers could not meet the average wage requirement. In fact, 68 percent did not qualify based on wages, even though they met the FTE requirement. Second, the credit can only be claimed for 2 consecutive years beginning in 2013. We found that employers may be reluctant to provide a benefit that they may have to take away later when the credit is no longer available and they are faced with higher costs for premiums. Third, GAO also found that the cost and complexity involved in claiming the credit was significant, deterring small employers from claiming it. For example, a major complaint that we heard had to do with the effort required to gather information on the number of hours worked for each employee in order to calculate full-time equivalence in the associated average annual wages. Tax preparers told us it could take 2 to 8 hours to gather the necessary information and that they spent 3 to 5 hours calculating the credit. Fourth, many small employers have also reported that they were unaware of the credit. In response, the IRS developed a communication strategy that includes written materials, a website, and outreach to interest groups. However, the effectiveness of this outreach is unknown.

Our 2012 report also discussed ways that the design of the credit could be altered to spur greater use of the credit. Options include increasing the amount of the full credit, the partial credit, or eliminating the State average premium cap. Other options would expand eligibility by increasing the FTE and wage limits for employers. And some options involve simplifying the credit calculation by using the number of employees and wage information already reported on the employer's tax return, or offering a flat credit amount per employee rather than a percentage. In recent years, Congress and the administration have proposed a number of changes to the credit as well. These include expanding the size of eligible employers, altering the phase-out rules, and allowing the credit to be claimed in more than 2 consecutive years.

In conclusion, expanding eligibility or increasing the amount of the credit may spur more small employers to claim the credit. However, these changes would increase the cost to the Federal Government.

Mr. Chairman, Ranking Member Chu, and members of the Subcommittee, this concludes my prepared remarks, and I would be happy to take any questions.

Chairman HUELSKAMP. Thank you, Mr. McTigue. I appreciate your testimony. We will have questions here shortly.

Next up, I am now pleased to welcome Harold Jackson, who is Executive Chairman of Buffalo Supply, Inc., located in Lafayette, Colorado, just to my west from Kansas. Buffalo Supply is a family-owned business that has been devoted to providing high-tech medical supplies and equipment to the Federal Government since its inception in 1983. Mr. Jackson joined the company in 1990. He is also an active member of the U.S. Chamber of Commerce, where he serves on the Small Business Council and the Government Procurement Subcouncil. He is also a longtime member of the Coalition for Government Procurement. I appreciate you being with us today, Mr. Jackson. You may begin.

STATEMENT OF HAROLD JACKSON

Mr. JACKSON. Thank you, Chairman, and Ranking Member Chu, distinguished members of the Committee. My name is Harold Jackson. I am the executive chairman of Buffalo Supply, a 20-employee small business located in Lafayette, Colorado. I am honored to speak to you today on behalf of the United States Chamber of Commerce.

Since 1983, our family-owned business has been devoted to providing high-tech medical equipment and supplies to Federal-funded facilities. We provide exceptional customer service, a deep level of expertise to our supply partners, and a high-quality workplace for our employees. We have 16 full-time and 4 part-time employees.

I understand most tax credits are designed to incent or change behavior. Let me be clear. We have always provided health insurance for our employees, but premiums have increased dramatically year after year, and we may not be able to continue to provide health insurance in the future. Because BSI is ineligible, the tax credit does not help me provide affordable coverage for my employees now, nor will it encourage me to continue so in the future. We may be forced to stop providing health insurance due to the escalating costs.

Over the years, we have changed carriers almost annually and explored different plan designs moving from PPO to high-deductible plans, and in the beginning, we covered the associated HSA contributions to cover the high deductible, but we had to reduce that from 100 percent coverage for our employees to 50 percent of the deductible, and now down to 0. We do pay 100 percent of the premiums for our employees and their dependents, but subject to higher family deductibles from $3,000 up to $5,000, and higher maximum out-of-pocket expenses up from $4,000 to $6,800. So we are paying more in premiums and our employees are paying more when they require medical services.

When Connect for Health Colorado opened its shop in 2015, I went online and tried to enroll. Unfortunately, the amount of information required in the online application process was incredible. Much of the information I did not have access to, such as dependents' and spouses' Social Security numbers, dates of birth, tobacco use. After 3 days of gathering this information and another 10 hours of entering it into the system, I could not review the plan options or see quotes, so I contacted the shop at their 800 number and I was told that we do not provide quotes to small businesses; that you would need to go through your insurance broker. Interestingly enough, when I called the insurance broker, he said, well, I will be happy to provide you with a quote, but it will not be through SHOP. They are way too much hassle for us to deal with. So the people they referred me to did not even want to use them.

Based on my experience, the SHOP requirement is an onerous hurdle in and of itself. The biggest hurdle though is the annual earnings cap of $50,000. I am certainly not a tax expert, but it would appear to me that we could improve it by first removing the requirement that small businesses go through SHOP. Second, increase average earnings cap. Third, make the credit available for more than 2 consecutive years. The bottom line is the tax credit needs to be easier for businesses to assess and the hoops need to be simplified. It seems like a big part of the problem is the rules for the tax credit are so confusing that small businesses cannot assess the benefit without hiring outside counsel. Ultimately, any changes should not only increase the tax benefit to help small businesses but must be simple and easily understood.

Thank you for this opportunity to testify, and I would be happy to answer any questions.

Chairman HUELSKAMP. Thank you, Mr. Jackson. I appreciate your testimony, and I am disappointed by your experience with SHOP, and hopefully, there will be some questions on that later.

Up next, I am pleased to welcome to the Subcommittee Holly Wade, who is the Director of Research and Policy Analysis at the NFIB. In that role, Ms. Wade oversees the foundation's publications, including the monthly "Small Business Economic Trend Survey and Small Business Problems and Priorities." She also provides in-depth analysis on public policy issues that impact our small businesses. She is a member of the National Association of Business Economics and the Department of Commerce's Industry Trade Advisory Committee on Small and Minority Business. Ms. Wade is a graduate of the University of Washington, with a degree in political science and sociology, and she has a master of public policy from the University of Denver. And I appreciate you being with us today, Ms. Wade. You may begin.

STATEMENT OF HOLLY WADE

Ms. WADE. Thank you. Good morning, Chairman Huelskamp, Ranking Member Chu, and members of the Subcommittee. Thank you for the opportunity to testify today. I am pleased to be here on behalf of the National Federation of Independent Businesses as the Committee discusses the Small Business Health Insurance Tax Credit.

Small business owners rank the cost of health insurance as their most severe problem in operating their business out of 75 potential issues, with 56 percent of small business owners finding it a critical problem. The high cost of health insurance is the main reasons owners do not offer employer-sponsored health insurance and the main reason owners discontinue providing the benefit. And for those offering, many owners annually confront the arduous task of adjusting profit expectations, insurance plans, cost sharing, and other mechanisms to help absorb the often erratic changes in total premium costs. The rising cost of health insurance has forced many small employers to rethink the viability of offering health insurance to their employees, especially during and in the wake of the Great Recession.

Since 2008, the offer rates for small businesses with fewer than 50 employees has dropped precipitously. Small business owners are far more hesitant to commit themselves to offering a long-term, high-cost benefit. The offer rates for this group have fallen over 10 percentage points from 43 percent offering in 2008 to 32 percent in 2014.

The Small Business Health Insurance Tax Credit was a targeted approach to help curb health insurance costs for offering small employers and was intended to provide an incentive for those that do not to start offering. However, the tax credit was largely ineffective in both fronts as its design is exceedingly restrictive, complicated, and only offers limited and temporary relief to a larger small business cost problem. To date, the tax credit has generally served as a windfall for the few small business owners who qualify and take the time or pay an accountant to file for it.

The ineffectiveness of the tax credit is largely due to four factors. The first and most limiting factor in claiming the tax credit is that eligibility was targeted to and most beneficial for those small businesses least likely to offer health insurance. Health insurance operates very significantly by employee size of firm and average wages. Those businesses with lower than average wages are more likely to compensate employees in cash and not benefits. Health insurance costs would significantly crowd out employee's take-home pay. Smaller small businesses are also less likely to offer health insurance and those factors vary from high administrative burdens, low take-up rates, and higher than average premium costs.

Second, the tax credit is exceedingly complicated to verify eligibility and claim the credit. The IRS estimates that recordkeeping requirements to claim the credit average just under 11 hours for most filers. The education component is estimated to take about an hour and a half. And finally, the time spent preparing and filing is estimated to take an average of 2 hours and 45 minutes. While most small employers use a tax preparer for their business, the cost associated with claiming the tax credit will deter many from going through the process in the first place. Since 2010, NFIB has received numerous complaints from small business owners regarding the complexity of the tax credit. Some owners called to say that even their tax preparer told them the credit was not the extra cost associated with determining eligibility and filing the paperwork.

Third, the tax credit is temporary. At most, the credit was available to small business owners for 6 years that they started claim-

ing the credit in 2010. Currently, small business owners can claim the credit for 2 years. Health insurance is a long-term benefit offered by employers to retain and recruit employees. Owners generally start offering the benefit when profits allow for the added cost. Profitability was an important factor in offering health insurance for 63 percent of newly offering firms. The tax credit is little relief in the long-term cost challenges small business owners face in offering health insurance.

And fourth, as of July 1, 2014, the Small Business Tax Credit is only available to qualifying businesses through the Small Business Health Options Program marketplaces. Most small employers purchase health insurance through an insurance agent and therefore, rely on the agent for suggesting health insurance options available to them. Only 13 percent of offering small businesses visited their SHOP Exchange, and of those offering and shopped, less than 1 percent purchased through the SHOP marketplace. Among nonoffering firms, 17 percent of small employers shopped for coverage through the SHOP Exchange. The vast majority of nonoffering firms did not select a plan through SHOP because the plans were too expensive.

The Small Business Health Insurance Tax Credit was too narrowly designed to be an effective cost-saving tool for small employers. The tax credit is now available to qualifying small business owners, small employers, for 5 years, and still very few businesses have benefited. But more importantly, health insurance costs continue to increase, and small business owners continue to struggle with their ability to afford offering the benefit.

I appreciate this opportunity to present NFIB's views and data on the effects of the Small Business Health Insurance Tax Credit, and I look forward to answering any questions you may have.

Chairman HUELSKAMP. Thank you, Ms. Wade. I appreciate your testimony. I look forward to questions and answers on that.

I am now pleased to yield to the Ranking Member of this Subcommittee so that she may introduce our final witness, Mr. Ricco.

Ms. CHU. Yes. It is my pleasure to introduce Mr. Michael Ricco, Quality Manager for AEEC, a minority and women-owned small business. AEEC provides IT, environmental, and engineering services to federal and commercial customers. Mr. Ricco has been with AEEC for over 2 years and oversees quality assurance and compliance for every department and Federal contract at the company. Additionally, Mr. Ricco is a facilitator and member of AEEC's management board. He holds a master of arts from Syracuse University and a bachelor of arts from the University of Arizona. As the manager of a women-owned business, he is testifying today on behalf of the U.S. Women's Chamber of Commerce, which represents 500,000 members, three-quarters of whom are small business owners and federal contractors. Welcome, Mr. Ricco.

Chairman HUELSKAMP. I thank the Ranking Member for that introduction. Mr. Ricco, you may begin.

STATEMENT OF MICHAEL RICCO

Mr. RICCO. Good morning, Chairman Huelskamp, Ranking Member Chu, and other Subcommittee members. Thank you for this opportunity to provide testimony before the Subcommittee on

Economic Growth, Tax, and Capital Access. My name is Michael Ricco. I am the quality manager for AEEC, a women and minority-owned small business located here in Reston, Virginia. Our president, Sangita Patil, wishes she could be here in person but she had a conflict.

AEEC is an award-winning, professional services organization offering top-quality technology, environmental, and engineering solutions to U.S. Federal Government and Fortune 50 customers since 1995. We support our customers' requirements and offer a range of customized solutions with the highest degree of honesty, integrity, and service excellence. We offer solutions that are efficient, appropriate, and worthy of investment. Our company is also a member of the U.S. Women's Chamber of Commerce. While I would like to testify today that my company has been able to benefit from the Small Business Health Care Tax Credit, that is, unfortunately, not the case because we are ineligible for the following reasons: First, we are ineligible because we have more than 25 employees. As this Subcommittee is well aware, there are many differing definitions of what a small business is, ranging from 50 to 100 to sometimes even 500 employees. The size standards for companies to use this health care tax credit is on the woefully low side and should be increased so that many more legitimate small businesses can take advantage of this tax credit.

Second, we are an IT company, and as such, our employees tend to earn higher salaries than many other employees working in small businesses nationwide. Therefore, we do not qualify because our workers on average make more than $50,000, which is the current cap as stated in the implementation language governing this credit. We question the fairness of this cap because in essence, it punishes our company for paying our employers a higher wage. This limitation in our view should be removed from the eligibility requirements of this tax credit.

Why do I say these changes should be made? Because AEEC would very much like to use this credit. Receiving a tax credit for up to 50 percent of our healthcare costs would certainly help us reduce our own costs. We all know, and as pointed out in the GAO report, plans for small employers are likely to have higher premiums, less coverage, and higher costs than plans for large employers, yet we, as a small business, want to do the right thing and provide healthcare coverage for our hardworking employees. AEEC has long provided healthcare coverage to all of our employees, and we go far beyond the minimum coverage now required by the Affordable Care Act. Our package would fall in the platinum or high gold range, so expanding the tax credit would go a long way to help us pay for premium increases and cover the additional compliance and reporting requirements that have come with the ACA.

Here is something else to consider. The expectations that would-be employees have for benefits coverage get higher with salary levels. For example, a cashier at a fast food restaurant might be thrilled getting any healthcare coverage, but a senior data architect expects to have a platinum healthcare package. This makes small businesses like ours among the most in need for a tax credit.

Finally, I would like to stress that although the ACA very much helps very small businesses with subsidies, large business benefit

from large pools that keep their costs down. It is the small businesses in the middle, particularly those between 50 and 100 employees, that would benefit the most from this health care tax credit. Therefore, I would ask this Subcommittee to consider making changes to this credit so that more small businesses that are so critical to our Nation's economy can be better able financially to pay for these healthcare costs.

Two changes I have already mentioned, increasing the eligibility threshold for the number of employees that work at a small business and removing the wage barrier that excludes so many businesses from eligibility. Two other reforms that we would recommend are increasing the credit so that it is more cost-effective for small businesses to actually use it and to make it last longer than 2 consecutive years.

Again, thank you for this opportunity to address this Subcommittee. AEEC is dedicated to providing our employees with the best healthcare coverage possible; yet, the fact remains that we are still a small business and these costs are quite high. We would urge this Subcommittee to put forth language that would make this important health care tax credit more accessible to the small businesses in our Nation that I would like to point out, on average, account for over 60 percent of all net new jobs created in this country.

I would be happy to answer any of your questions. Thank you.

Chairman HUELSKAMP. Thank you, Mr. Ricco, and other witnesses for your input. I will go ahead and open it up for questions. We have a few Subcommittee members here, but I will start.

First, Mr. McTigue, Mr. Jackson, I appreciate your testimony. Mr. McTigue, we have been given the number of employers that are participating. What is the number of actual employees that are receiving some additional coverage because of this credit at that level? Do you have that data?

Mr. MCTIGUE. Yes. The actual number of employees covered, it fluctuates year to year, but on average I would say it is around $800,000. So a larger number than the actual employers.

Chairman HUELSKAMP. Certainly. In terms of that, the estimates that you presented were on the employer level, and, of course, the estimates from the CBO were significantly higher than they have come in. The number of employees, did they actually identify how many they thought would be covered because of this at that employee level? Did they meet those estimates with the implementation? Do you have those figures?

Mr. MCTIGUE. I do not have the figures. I can provide them for the record, but I do know that the overall costs, the take-up rate of the credit was much lower than originally estimated by CBO and JCT. And it continues to be lower than the revised estimates.

Chairman HUELSKAMP. Yes, I appreciate that.

Mr. Jackson, you have given some insight, particularly your personal experience with your company and the limits working through the SHOP Exchange. Can you describe that a little bit more? You go to the SHOP. They ask for information you did not have, and then they refused to provide an estimate? I am just shocked that they would tell you, well, we do not provide estimates for small businesses. I assume in the State of Colorado, I see it is

a state-run exchange. Was small business not a focus at all? I mean, there are exchanges, one exchange for small business and the individual market. Can you describe that a little bit more for the Subcommittee, your experience with the SHOP in your State?

Mr. JACKSON. Well, my personal opinion is that it is more focused on the individual marketplace than it is the small business marketplace. And it would have been helpful if they just upfront said small businesses go to your broker to get a quote. But they allow you or keep asking you all this information about your employees, and they do not really tell you that ever. When you get to the end, I had to call them and say, well, I have entered all this data. Now where do I find the options, the policy options, and the quotes? And that is when they said, well, we do not really provide small businesses with quotes. So it was a very frustrating process. I would throw in that we have done everything, I think, reasonable and prudent possible to try to minimize our premiums, yet over the last 5 years they have still gone up over 25 percent, and we cannot—and even to do that, we are not in a small business program. I had to join a professional employer organization to get into another company's large insurance pool to keep our premiums as low as they were. The last small business quote I got, our premium increases were going to be something in the neighborhood of 70 percent one year to the next year.

Chairman HUELSKAMP. Ms. Wade, the experience of Mr. Jackson, is that what you are seeing across other states, even if it was a state-level exchange or a federally-facilitated exchange, partnership exchange? Is this similar to the story you are hearing across the various States?

Ms. WADE. It is a very common story that we are hearing from our members. And it is not, unfortunately, State specific. It is not size specific. They are all having a lot of frustrating circumstances in accessing SHOP, and looking to find more affordable health insurance for their employees. And if they are not offering insurance, finding a plan that would work for their business and for their employees. So yes, we are hearing many stories that are very similar to Mr. Jackson. And they are still coming in, unfortunately.

Chairman HUELSKAMP. Follow-up question for any of the witnesses who can answer this. The information that Mr. Jackson provided to the SHOP, extensive hours and hours, then chose to go elsewhere because he really had no choice to stay in the SHOP, what happens to that information?

Mr. JACKSON. That is an interesting question that I do not know the answer to because some of my people were, well, I will say semi-reluctant to provide me with the information, but I explained if they wanted health coverage, they really did not have a choice but to provide me with that information. I have no idea what happens to it, but I am concerned.

Chairman HUELSKAMP. Yes, so you asked for some information, they reluctantly provided it, you turned it over to the SHOP, and then you did not even sign up through that. That is something I would like to follow-up on for folks that might be able to answer that. So I appreciate that, Mr. Jackson.

I see I am out of time, and I will recognize our Ranking Member for her 5 minutes of questions.

Ms. CHU. Mr. Ricco, the Small Business Health Care Tax Credit was meant to incentivize small employers into offering health insurance. How do you feel the IRS worked with the business community to provide information about the credit, and was that outreach adequate?

Mr. RICCO. In our situation, it was adequate because it was very clear what the size standards were, 25 or fewer employees, average of $50,000 or less. If you could not hit those, there was no sense in looking further. So, for us and many other small businesses in our situation, we could tell right away we were not eligible. Now, that may not be the case for smaller businesses that would have; however, there was information out there and they could have reached out.

Ms. CHU. Well, talking about size standards, the tax code contains many different definitions of a small business and what a small business is depending on what section of the code we are discussing. This lack of uniformity certainly was highlighted by the ACA in its definition of a small business. This definition shaped which businesses were eligible for the tax incentives in offering health care. Mr. Ricco, what do you think would be a better size standard with regard to the ACA?

Mr. RICCO. Well, it certainly makes sense to have size standards, because small businesses are in much greater need for a tax credit than larger companies. However, I think it would have made a lot more sense to base if off of NAICS codes. The government already sets NAICS codes for every industry. If you want to be a Federal contractor, you have to fall into those. Every business knows what their NAICS codes are. It would not take any type of change to use that as the basis instead of this arbitrary 25 employee, $50,000 cap.

Ms. CHU. Mr. McTigue, what do you think of the size standards? What have you found to be a better size standard with regard to participation?

Mr. MCTIGUE. We did not look at what would necessarily be a better size standard. Obviously, there are tradeoffs associated with how you target a benefit, whether through the tax code or spending program. So expanding eligibility, expanding both on the FTE and average wage would have tradeoffs in terms of increasing the cost of the program or the tax credit to Federal Government, so those options have to be weighed. Complexity, as we have heard from all the witnesses, is a major issue. Reducing complexity can be achieved at relatively less cost, so that might be an option to pursue.

Ms. CHU. Let me ask about the different numbers to the analyses of the Small Business Health Care Tax Credit by the Treasury Inspector General of Tax Administration. The IRS and the GAO all concluded drastically different results for the use of this incentive. Mr. McTigue, can you walk me through why the GAO's numbers are much lower than those of the Treasury Inspector General of Tax Administration and the IRS for the 2010 claims?

Mr. MCTIGUE. Yes. For today's statement, for today's report, we reached out to the IRS and obtained the most recent data available. Those data do differ from what we originally reported in 2012 for the tax year 2010. Basically, it is an issue of more returns hav-

ing come in since we previously reported. Overall, the numbers are relatively low compared to the number of potentially eligible small employers. So I have not looked at the TIGTA numbers specifically. We can look at those and get back to you for the record, but again, I think you mentioned something in the order of $300,000 versus 181,000 that we reported today. Not a big difference compared to potentially eligible in the millions.

Ms. CHU. Do you plan to perform a final analysis using these numbers?

Mr. MCTIGUE. Not at this time. We would be happy to do so at the Committee's request.

Ms. CHU. Yes. I certainly would be interested in that.

Despite the low adoption rate, nearly 1 million employees whose employers claim the credit are benefiting from the ACA, but this is an increase from only 770,000 workers in 2010 and through fewer employers. Has the GAO studied whether these numbers are due to small employers hiring more employees or simply different businesses entirely who are claiming the credit?

Mr. MCTIGUE. We have not studied that issue. There are a number of factors that come into play. It could be the size of the company, companies coming in and out claiming the credit. As you are aware, the credit originally was available for up to 6 years when it was originally established. Beginning in 2013, it was only available for 2 years. Also, we mentioned one of the factors that we found was the lack of awareness, maybe part of the issue is companies becoming more aware of it and signing up for it.

Ms. CHU. Thank you. I yield back.

Chairman HUELSKAMP. Thank you. I would like to recognize Mr. Richard Hanna, who actually has personal experience in this arena. I look forward to your 5 minutes of questions.

Mr. HANNA. Thank you, Chairman.

The government is famous for unintended consequences, but there is something insidious about this. The time, the incentive to raise pay, the complexity, the fact that you went from 16 percent to 32 percent of companies that are not doing this or are not supplying it.

Mr. McTigue, Ms. Wade, is it possible that in this particular case this law is doing exactly what it was intended to do, and that is incentivize people to have insurance for a short period of time, but ultimately, create a marketplace where the real goal is to force everybody to provide insurance without really giving them any benefit? Maybe that sounds like a strange question, but it seems like there is nothing about this that is workable or working. If you really wanted people to get more insurance, this is not what you would design. None of us here would. So what do you think of that? I mean, it is my inference.

Mr. MCTIGUE. I think in terms of the Patient Protection and Affordable Care Act as, you know, a congressman in the United Sates, many people—the majority of people, the majority of workers receive their health insurance through their employers. I think it is something in the range of 55 percent of all employees receive through their employer or spouse's employer, something of that nature. Whether or not this was the best way or the most efficient way, the most equitable way to either incentivize small employers

to provide health insurance or have all individuals have some sort of health insurance coverage, you know, there are tradeoffs in terms of different ways of requiring that, delivering the service. I mentioned, you know, would a spending program be more efficient? You know, a direct subsidy as opposed to a tax credit. The small employer health tax credit is a small piece of a larger strategy to provide health insurance for all individuals.

Mr. HANNA. The bottom line is this is not working, and people are not incentivized to use it. And it is not producing the outcome it was intended. I mean, it is nice that more people have insurance, but on the margin you have to say it is a very small number compared to the number that it might be able to affect. If it were simpler, longer, maybe raise the number, I do not know. So this ought to be something you can look back and either decide to make it go away or fix it and make it cleaner. Ms. Wade? Anybody?

Ms. WADE. No, I absolutely agree. The tax credit is far too temporary and far too limiting to the people that are able to——

Mr. HANNA. The temporary part is what makes me think it is a little insidious because clearly people, you are not going backwards. You do not give somebody a pay raise effectively through insurance and then yank it back in 2 years. Any fool can project the cost of that out for however long you may think you have your average employee and say, you know, I am not doing that because in 10 years it is going to cost me 10 times or 5 times more. So I think the whole rule is suspect.

Ms. WADE. Absolutely. For small employers, offering health insurance is a very costly, long-term benefit that generally takes some time when they start their business to offer that. It is based on profitability, their certainty about where sales are projected to go in the near future. So offering the benefit is serious consideration for small business owners and for long-term.

Mr. HANNA. It looks like the government are trying to lock people into this without giving them an exit strategy or incentive that actually works in the real world. What do you think, Mr. McTigue?

Mr. MCTIGUE. I would just say that again it comes down to a tradeoff between the cost to the government and cost-sharing overall. Certainly, if we expanded the credit or made it permanent and offered it to more people, a lot more people would benefit. However, it would cost the government a lot more.

Mr. HANNA. You have to look at the goal though. If the goal is somewhere in between, right?

Mr. MCTIGUE. Exactly.

Mr. HANNA. I would wager that the government looked at this and said this is really expensive, and how can we limit it? So you do 2 years and a few other things that you have thrown in here, but the net result is not as many people are enjoying the outcome as we would like to have.

My time is expired. Thank you, Chairman.

Chairman HUELSKAMP. Thank you, Mr. Hanna. As Mr. Kelly prepares, I'd like to make a statement very quickly here.

I was not around when they passed this law, and it would be, I guess, fascinating to try to decide whether they really thought this would have an impact or was this kind of dropped in there and sounded good? In 2012, we had these discussions that it clearly was

not going to work. Here we are 4 years later, still coming to the same conclusion. That is very disappointing.

Next, I recognize Mr. Kelly, but he had his questions already all answered. I appreciate you coming here. It has been a very quick hearing discussing this.

I am going to spend a couple more minutes and leave questions for the other members as well. As we move forward, if we are really trying to incentivize and encourage small businesses, if you could devise that, Mr. Ricco, how would you devise that? Obviously, you want to take the cap off so it would not punish or penalize those who actually are paying maybe more than their competitors. In 1 minute, if you could just say how would you devise this and what would you change to make certain that it produces the effect to encourage our small businesses to provide a pretty expensive benefit for their employees. Mr. Ricco?

Mr. RICCO. Well, like I mentioned before, I would certainly do it by NAICS code or a similar mechanism. I would also get rid of the way that it is tied to the States with the amount that you can get back because that just adds another calculation that gets factored in for a small business to figure out how much money they are actually going to get back with a subsidy like that. You could also look at making a more uniform change that will help small businesses pay for the additional compliance and reporting costs that we have associated now that we have got to comply with these new mandates.

Chairman HUELSKAMP. Okay. Ms. Wade, any thoughts on the system, the Wade system if you put that together?

Ms. WADE. Certainly, expanding the population that would be eligible for the tax credit would be immensely helpful. But still, I would say that it is a temporary approach to a larger cost issue that small business owners are facing. Thirty percent increase on average for health insurance costs since 2008 when profits and earnings and wages have been fairly stagnant for the small business population is still a hefty hurdle for them to get across to offer and keep offering health insurance. So while the tax credit is helpful for those that can access it, it is not a particularly helpful solution for the broader small business population in offering and affording health insurance for their employees.

Chairman HUELSKAMP. Simply an additional cost of doing business and that might provide some benefits, but at the end of the day you still have to have enough business to cover that cost.

Mr. Jackson, personal experience? If you were looking out there and waved a magic wand, what would it look like?

Mr. JACKSON. Well, the increasing costs have been a major, major hurdle for us to continue providing our insurance, and certainly any way that we can devise a system that minimizes that cost, I am all in favor of. I would not be opposed to if you are going to have a cap, not make it an average cap for the employee but make it an employee-specific cap, so I know if I have 10 employees that make $48,000 I am going to get the credit. And if I have 10 that make $53,000, I am not going to get the credit for them. But make it simple and straightforward and untie it from States and all the other—if we meet the size standard and your employee

makes less than whatever the magic number is for the cap, then give the people the credit for it.

Chairman HUELSKAMP. Mr. McTigue, you have an interesting perspective and very insightful. I mean, 4 years ago sitting with businesses, particularly with the Chamber and say, hey, we knew this was not going to work, worse than we feared. How would you devise that, scrap it all together and replace it with what?

Mr. MCTIGUE. Well, I think one area that you have heard from all, the three other witnesses, to look at simplifying how a small employer goes about claiming the credit. As we mentioned in our statement, you could use wage and employee counter information that is already available. It might not be as precise as FTEs and average ages, but there is a tradeoff between precision and targeting and the cost and complexity of the burden on small employers to comply in order to claim the credit. Obviously, you want a design that allows the most people eligible, the largest number of eligible employers to access the credit. Otherwise, it is a very inefficient way to provide this benefit.

Chairman HUELSKAMP. Okay.

Mr. MCTIGUE. Mr. Chairman, if I could add for the record.

Chairman HUELSKAMP. Yes.

Mr. MCTIGUE. In response to Ms. Chu's question about the 360 employers reported by TIGTA. The TIGTA account actually included partnerships and S corporations which are basically pass-through entities, whereas the 181,000 employers that we testified to are real employers. So that accounts for the difference. Thank you.

Chairman HUELSKAMP. Thank you, Mr. McTigue, Mr. Jackson, Ms. Wade, and Mr. Ricco. I appreciate your testimony. I wish we would have a happy story today, and that is not the case. But thank you for being here.

As we know, the Small Business Health Insurance Tax Credit was created with a stated purpose of making it easier for small business owners to provide health benefits for their employees. The numbers in testimony show, however, that this credit simply did not deliver, and from what we have heard today, I believe we can see why. This credit proved to be complicated, confusing, and costly to implement. It is yet another broken promise to the small business community.

The Committee on Small Business remains dedicated to the interest of small businesses and their hardworking employees. It is our duty to ensure that America's entrepreneurs, job creators, and their employers are actually being helped, not simply being paid lip service.

I ask unanimous consent that the members have 5 legislative days to submit statements and supporting materials for the record.

Without objection, so ordered.

The hearing is now adjourned.

[Whereupon, at 10:55 a.m., the Subcommittee was adjourned.]

APPENDIX

United States Government Accountability Office

Testimony

Before the Subcommittee on Economic Growth, Tax and Capital Access, Committee on Small Business, House of Representatives

For Release on Delivery
Expected at 10:00 a.m. ET
Tuesday, March 22, 2016

SMALL EMPLOYER HEALTH TAX CREDIT

Limited Use Continues Due to Multiple Reasons

Statement of James R. McTigue, Jr.
Director, Strategic Issues

GAO-16-491T

GAO Highlights

Highlights of GAO-16-491T, a testimony before the Subcommittee on Economic Growth, Tax and Capital Access, Committee on Small Business, House of Representatives

Why GAO Did This Study

Many small employers do not offer health insurance. The Small Employer Health Insurance Tax Credit was established as part of the Patient Protection and Affordable Care Act to help eligible small employers—businesses or tax-exempt entities—provide health insurance for employees. The base of the credit is premiums paid or the average premium for an employer's state if premiums paid were higher. In 2016, for small businesses, the credit is 50 percent of the base unless the business had more than 10 FTE employees or paid average annual wages over $25,900.

This statement summarizes and updates GAO's prior work in May 2012, November 2014, and March 2015 on the extent to which the credit is claimed, any reasons that limit claims, and changes to the credit proposed by Congress and the administration. To conduct the updates, GAO reviewed 2013 and 2014 IRS data on credit claims and academic and government studies, and summarized proposed legislation related to the credit.

What GAO Recommends

GAO is not making recommendations in this testimony statement.

View GAO-16-491T. For more information, contact James R. McTigue, Jr. at (202) 512-9110 or mctiguej@gao.gov.

March 2016

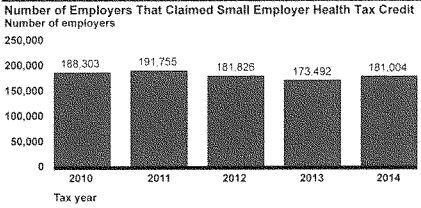
SMALL EMPLOYER HEALTH TAX CREDIT

Limited Use Continues Due to Multiple Reasons

What GAO Found

Claims of the small employer health tax credit have continued to be lower than thought eligible by government agency and small business group estimates, limiting the effect of the credit on expanding health insurance coverage through small employers. In 2014, about 181,000 employers claimed the credit, down somewhat from 2010 (see figure). These numbers are relatively low compared to the number of employers eligible for the credit. In 2012, GAO reported that selected estimates of the number of employers eligible ranged from about 1.4 million to 4 million. In 2010, claims totaled $468 million compared to initial estimates of $2 billion by the Congressional Budget Office and the Joint Committee on Taxation. Actual claims for the credit in 2013 and 2014 increased slightly to about $511 million and $541 million, respectively.

Number of Employers That Claimed Small Employer Health Tax Credit



Source: IRS. | GAO-16-491T

The small employer health tax credit has not been widely claimed for a variety of reasons, as GAO reported in May 2012. The maximum amount of the credit does not appear to be a large enough incentive for employers to offer or maintain insurance. Also, few small employers qualify for the maximum credit amount. For those employers who do claim the credit, the credit amount "phases out" to zero as employers employ up to 25 full time equivalent (FTE) employees at higher wages. The amount of the credit is also limited if premiums paid by an employer are more than the average premiums for the small group market in the employer's state. Furthermore, the credit can only be claimed for two consecutive years after 2013. GAO also found that the cost and complexity involved in claiming the tax credit was significant, deterring small employers from claiming it. Many small businesses have also reported that they were unaware of the credit. Even so, the Internal Revenue Service (IRS) had been taking steps since April 2010 to raise awareness about the credit and reduce the burden on taxpayers by offering tools to help taxpayers determine eligibility for the credit.

Congress and the administration have proposed a number of changes to the credit. These include expanding the size of eligible employers, altering the phase out rules, and allowing the credit to be claimed in more than two consecutive years. Amending the eligibility requirements or increasing the amount of the credit may allow more businesses to claim the credit. However, these changes would increase its cost to the federal government.

Chairman Huelskamp, Ranking Member Chu, and Members of the Subcommittee:

Thank you for the opportunity to discuss our work on small employers' use of the health tax credit.[1] The Small Employer Health Insurance Tax Credit was established as part of the Patient Protection and Affordable Care Act (PPACA) to help eligible small employers—businesses or tax-exempt entities—provide health insurance for employees. This testimony updates our work that showed seemingly low usage of the credit and some of the reasons for this low usage.

The Small Employer Health Insurance Tax Credit is generally available to eligible small employers and tax-exempt employers who have fewer than 25 full-time equivalent (FTE) employees with average annual wages that fall below a statutorily-specified cap.[2] For tax year 2016, the wage cap is $51,800.[3] These small employers must cover at least 50 percent of the cost of each of their employees' self-only health insurance coverage. The credit amount is a percentage of the employer's contributions to employees' health insurance premiums. The percentage varies according to the number of FTEs, average wage paid by the employer, and whether the employer is a for-profit or tax-exempt employer. The larger the average annual wage and the greater the number of FTEs, the lower the

[1]See GAO, *Small Employer Health Tax Credit: Factors Contributing to Low Use and Complexity*, GAO-12-549 (Washington, D.C.: May 14, 2012), GAO, *Small Business Health Insurance Exchanges: Low Initial Enrollment Likely due to Multiple, Evolving Factors*, GAO-15-58 (Washington, D.C.: Nov. 13, 2014), and GAO, *Private Health Insurance: Early Evidence Finds Premium Tax Credit Likely Contributed to Expanded Coverage, but Some Lack Access to Affordable Plans*, GAO-15-312 (Washington, D.C.: March 23, 2015).

[2]A tax-exempt eligible small employer is one that is exempt from federal income tax under section 501(a) and described in section 501(c) of the Internal Revenue Code. 26 C.F.R. §1.45R-1(a)(20). An eligible small employer can include businesses that are corporations in a controlled group of corporations, or members of an affiliated service group, as well as partnerships, sole proprietorships, cooperatives, and trusts. A sole proprietor is an individual who owns an unincorporated business but may employ others. Credit amounts claimed by partnerships and S corporations are to be passed through to their partners and shareholders, respectively, who may claim their portions of the credit on their individual income tax returns.

[3]To be eligible for the full credit, employers must have 10 or fewer FTEs with average wages below $25,900 in 2016. For 2010 to 2013, the wage cap to be an eligible employer was $50,000, with the full credit available for small employers with averages wages for FTEs at $25,000. Starting in 2014, the wage cap is adjusted for inflation each year using the Consumer Price Index–Urban.

credit percentage the small employer can claim, until the credit is entirely phased out. Beginning in 2014, small employers who qualify for the credit generally must purchase coverage through a Small Business Health Options Program (SHOP) exchange.[4] SHOP exchanges, as established under PPACA, are marketplaces where small employers can shop for and purchase health coverage for their employees. All health plans available through SHOP exchanges must meet certain federally required criteria, such as providing plans that offer minimum essential health benefits. Our 2014 report noted that a primary incentive for small employers to use SHOPs has been this tax credit.[5]

The vast majority of small employers do not offer health insurance to their employees. The Medical Expenditures Panel Survey (MEPS) estimates that 83 percent of employers who may be eligible for the full credit did not offer health insurance in 2010 and that 67 percent who could be eligible for a partial credit did not offer insurance.[6] As we discussed in our 2012 report, various factors have explained why small, low-wage employers historically tend not to offer health insurance. For example:

- For very low-wage employees, health insurance drives up total compensation costs.
- Low-wage employees generally prefer wages over insurance benefits. While employees pay income and employment taxes on wages, employees do not pay these taxes on premiums that employers pay for health insurance. However, the income tax exclusion is worth less to low-wage employees—being in a lower-income tax bracket—compared to those with higher wages.
- Insurers of small employers face higher-average fixed costs for billing and marketing and are less able to pool risk across many employees.

[4]IRS Notices 2014-6 and 2015-8 provide transition relief for certain small employers that cannot obtain coverage through a SHOP exchange because SHOP coverage is not available in their location. SHOP exchanges cover small employers with either 100 or fewer employees or 50 or fewer employees, as chosen by each state; this means that not all small employers as defined for SHOP purposes would be small enough to qualify for the credit.

[5]See GAO-15-58.

[6]MEPS is a set of large-scale surveys. MEPS is administered by the Agency for Healthcare Research and Quality in the Department of Health and Human Services. In a subsequent 2013 MEPS–Insurance Component, 34.8 percent of private-sector firms with fewer than 50 employees offered health insurance compared to 95.7 percent of firms with 50 or more employees in 2013.

As a result, plans for small employers are likely to have higher premiums, less coverage, and higher costs than plans for large employers.

This statement (1) describes the extent to which the credit is being claimed by smaller employers (2) describes the reasons, if any, limiting employer claims, and (3) summarizes legislative proposals on the credit. It is based on reports we issued from May 2012 through March 2015. Detailed information about the scope and methodology for this prior work can be found in each of these reports. Much of this statement discusses findings from our May 2012 report. For that report, we reviewed Internal Revenue Service (IRS) data on credit claims for tax year 2010. We interviewed IRS officials and subject-matter specialists from government, academia, research foundations, and think tanks. We also interviewed officials of groups representing employers, tax preparers, and insurance brokers, and worked with them to assemble discussion groups on the credit. Finally, we reviewed literature about the credit and health insurance as well as IRS documentation.

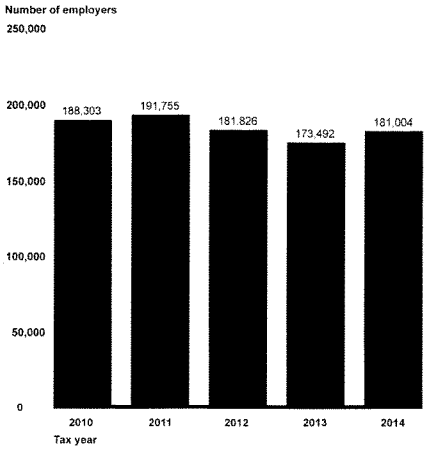
We updated selected data in this statement with 2013 and 2014 data from IRS on claims of the credit by small employers. To assess the reliability of the data, we reviewed the data and supporting documentation for obvious errors, reviewed our prior use of the data, and interviewed IRS officials about the data. We found the data to be sufficiently reliable for our purposes. We also reviewed academic and government studies about the tax credit, including reports from the Congressional Research Service and the Treasury Inspector General for Tax Administration, and a web page about the credit from the Taxpayer Advocate Service. We also summarized proposed legislation on the credit.

The work upon which this statement is based was conducted in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Fewer Small Employers Claimed the Credit Than Were Thought to Be Eligible

Claims of the small employer health tax credit have continued to be lower than thought eligible by government agency and small business group estimates, limiting the effect of the credit on expanding health insurance coverage through small employers. In 2014, about 181,000 employers claimed the credit, down somewhat from 2010 (see figure 1).

Figure 1: Number of Employers That Claimed Small Employer Health Tax Credit, Tax Years 2010 to 2014



Source: IRS | GAO-16-491T

Note: Data for 2014 are reported on a calendar-year basis. These data differ from those we reported in GAO-12-549 and GAO-15-312 because additional returns were processed for a given tax year after the data were compiled by IRS.

These numbers are relatively low compared to the number of employers thought eligible for the credit. In 2012, we reported that selected estimates of the number of employers eligible ranged from about 1.4 million to 4 million.[7] The Council of Economic Advisors estimated 4 million

[7]See GAO-12-549.

and the Small Business Administration (SBA) estimated 2.6 million.[8] Estimates made by small business groups included the Small Business Majority and the National Federation of Independent Businesses. Their estimates were 4 million and 1.4 million, respectively.[9]

A similar outcome is seen when the dollar value of credits claimed is compared to initial estimates. In 2010, claims totaled $468 million compared to initial estimates of $2 billion by the Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT). In March 2012, CBO and JCT estimated that the credit would cost $1 billion in 2012 and $21 billion from 2012 to 2021, down considerably from the original estimate of $5 billion and $40 billion, respectively.[10] The revised estimates appear overstated as well given that actual claims for the credit in 2013 and 2014 were about $511 million and $541 million, respectively.[11]

Small Employers Have Been Unlikely to Claim the Health Tax Credit for Various Reasons

Based on our interviews, discussion groups, and literature review conducted for the 2012 report, we found the small employer health tax credit has not provided a strong enough incentive for employers to begin to offer health insurance for various reasons, as discussed below.

Maximum Small Employer Credit Amount is Too Small

The maximum amount of the credit does not appear to be a large enough incentive to get employers to offer or maintain insurance. For example, the maximum amount is available to small businesses with 10 or fewer FTE employees that pay an average of $25,900 or less in wages in tax

[8]The Council of Economic Advisors, within the Executive Office of the President, is charged with offering objective advice on forming domestic and international economic policy. SBA is a government agency that offers a variety of programs and support services to help small businesses.

[9]It is important to recognize data limitations make these estimates rough. It is not possible to combine data from available sources on three basic eligibility rules for the credit—wages, FTEs, and health insurance—to closely match the rules. Further, limited data are available on the distribution of claim amounts for business entities.

[10]See GAO-12-549.

[11]Data from 2013 are on a tax year basis and 2014 data are on a calendar basis because only partial tax year 2014 data were available at the time of this report.

year 2016 (adjusted for inflation in future years).[12] Such an employer could be eligible for a credit worth up to 50 percent of the premiums paid.[13] These employers did not consider the maximum credit amount to generally be high enough, and the amount tended to be less than the maximum, as discussed below.

Few Small Employers Qualify for Maximum Small Employer Credit Amount

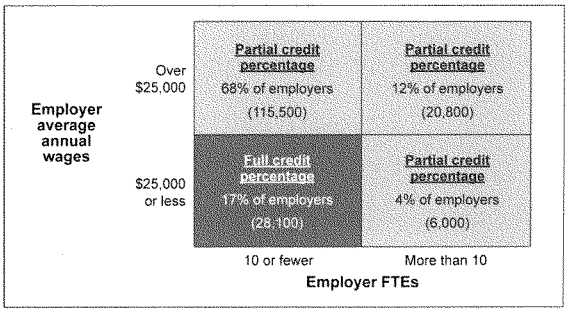
Most small employer credit claims are likely to be for less than the maximum credit percentage. To illustrate, our 2012 report analyzed how many of the approximately 170,300 small employers making claims for tax year 2010 could claim the full credit.[14] As figure 2 shows, only 28,100—17 percent—could use the full credit percentage. Usually, employers could not meet the average wage requirement to claim the full percentage, as 115,500—68 percent—did not qualify based on wages, but did meet the FTE requirement.

[12]Pursuant to the requirements of the Balanced Budget and Emergency Deficit Control Act of 1985, as amended, refund payments issued to certain small tax-exempt employers claiming the refundable portion of the Small Business Health Care Tax Credit under Internal Revenue Code Section 45R, are subject to sequestration. This means that refund payments processed on or after October 1, 2015, and on or before September 30, 2016, to a Section 45R applicant will be reduced by the fiscal year 2016 sequestration rate of 6.8 percent. The Congressional Budget Office estimates that a sequestration for fiscal year 2016 will not be required.

[13]Through 2013, small businesses received up to 35 percent and tax-exempt entities received up to 25 percent of their health insurance premium payments; these portions rose to 50 percent and 35 percent, respectively, in 2014.

[14]This amount differs from figure 1 because additional returns were processed for tax year 2010 since we initially reported this amount in GAO-12-549.

Figure 2: Percentage and Number of Small Employers Claiming the Full and Partial Credit Percentages, by FTE and Wage Requirements for the Credit, Tax Year 2010



Source: GAO analysis of IRS data on Form 8941. | GAO-16-491T

Note: This information is based on 170,300 small employer claims. This number has increased since our 2012 report because IRS later processed additional claims for tax year 2010. Numbers do not add to total because of rounding to the nearest hundred.

To the extent that a small employer qualifies to claim the credit, the employer may not be able to fully claim the credit amount for the tax year. For tax-exempt employers, the credit amount claimed cannot exceed the total amount of the employer's payroll taxes for the calendar year. For other small employers such as small businesses, the credit is not refundable but is limited to the actual income tax liability. If a small business had a year in which it ended up paying no taxes (i.e., it had no taxable income after accounting for all its other deductions and credits), then the small business tax credit could not be used for that year as there would be no income tax for the credit to reduce.[15]

[15]An unused credit amount can generally be carried back for 1 year and carried forward up to 20 years.

Certain Credit Design Features Reduce the Amount of Credit That Can Be Claimed

Credit Amount is "Phased Out"

The credit amount that can be claimed "phases out" to zero as employers employ up to 25 FTE employees at higher wages—up to an average of $51,800 for 2016. Table 1 shows the phasing out of the tax credit amount we calculated for a tax-exempt employer's contribution to health insurance in 2016. Table 2 shows the phasing out for other small employers in 2016.

Table 1: Phase out of the Credit as a Percentage of Employer Contributions to Premiums, Tax-Exempt Employers, 2016

Firm size (number of full-time equivalent employees)	Average wage					
	$25,900 and less	$30,000	$35,000	$40,000	$45,000	$51,800
10 and fewer	32.5%	27.3%	21.1%	14.8%	8.5%	0.0%
11	30.3%	25.2%	18.9%	12.6%	6.4%	0.0%
12	28.2%	23.0%	16.7%	10.5%	4.2%	0.0%
13	26.0%	20.8%	14.6%	8.3%	2.0%	0.0%
14	23.8%	18.7%	12.4%	6.1%	0.0%	0.0%
15	21.7%	16.5%	10.2%	4.0%	0.0%	0.0%
16	19.5%	14.4%	8.1%	1.8%	0.0%	0.0%
17	17.3%	12.2%	5.9%	0.0%	0.0%	0.0%
18	15.2%	10.0%	3.7%	0.0%	0.0%	0.0%
19	13.0%	7.9%	1.6%	0.0%	0.0%	0.0%
20	10.8%	5.7%	0.0%	0.0%	0.0%	0.0%
21	8.7%	3.5%	0.0%	0.0%	0.0%	0.0%
22	6.5%	1.4%	0.0%	0.0%	0.0%	0.0%
23	4.3%	0.0%	0.0%	0.0%	0.0%	0.0%
24	2.2%	0.0%	0.0%	0.0%	0.0%	0.0%
25	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

GAO analysis of the Patient Protection and Affordable Care Act. | GAO-16-491T

Note: The maximum credit for tax-exempt employers in 2016 is 32.5 percent, which is calculated by using the 2015 and 2016 budget sequester rates in the following formula: [((0.35)(1-0.073)(9)) + ((0.35)(1-0.68)(3))] / 12 =32.5 percent.

Table 2: Phase out of the Credit as a Percentage of Employer Contributions to Premiums, For-Profit Employers, 2016

Firm size (number of full-time equivalent employees)	Average wage					
	$25,900 and less	$30,000	$35,000	$40,000	$45,000	$51,800
10 and fewer	50.0%	42.1%	32.4%	22.8%	13.1%	0.0%
11	46.7%	38.8%	29.1%	19.4%	9.8%	0.0%
12	43.3%	35.4%	25.8%	16.1%	6.5%	0.0%
13	40.0%	32.1%	22.4%	12.8%	3.1%	0.0%
14	36.7%	28.8%	19.1%	9.4%	0.0%	0.0%
15	33.3%	25.4%	15.8%	6.1%	0.0%	0.0%
16	30.0%	22.1%	12.4%	2.8%	0.0%	0.0%
17	26.7%	18.8%	9.1%	0.0%	0.0%	0.0%
18	23.3%	15.4%	5.8%	0.0%	0.0%	0.0%
19	20.0%	12.1%	2.4%	0.0%	0.0%	0.0%
20	16.7%	8.8%	0.0%	0.0%	0.0%	0.0%
21	13.3%	5.4%	0.0%	0.0%	0.0%	0.0%
22	10.0%	2.1%	0.0%	0.0%	0.0%	0.0%
23	6.7%	0.0%	0.0%	0.0%	0.0%	0.0%
24	3.3%	0.0%	0.0%	0.0%	0.0%	0.0%
25	0.0%	0.0%	0.0%	0.0%	0.0%	0.0%

GAO analysis of the Patient Protection and Affordable Care Act. | GAO-16-491T

Notes: The maximum credit for for-profit employers is 50 percent in 2016.

Credit Amount is Reduced by State Average Premiums

The amount of the credit is also reduced if premiums paid by an employer are more than the average premiums for the small group market in the state in which the employer offers insurance. The credit percentage is multiplied by the allowable premium to calculate the dollar amount of credit claimed. For example, if the state average premium is $4,441 for a single employee, but a small employer in that state paid $5,000 for an employee's health premium, the credit would be calculated using the state average premium of $4,441 rather than the $5,000. According to IRS data, this cap reduced the credit for around 30 percent of employer claims as of 2012.

Credit is Temporary

Regardless of the allowable credit amount, small employers can claim the credit for just two consecutive years after 2013, which detracts from the incentive for small employers to begin offering coverage. Employers are

reluctant to provide a benefit to employees that would be at risk of being taken away later when the credit is no longer available. As of 2014, the two consecutive tax years for credit claims starts with the first year a qualified employer obtains coverage through a SHOP exchange. In other words, if a qualified employer first obtains coverage through a SHOP exchange in 2016, the credit would only be available to the employer in 2016 and in 2017. From 2010 through 2013, the credit was available to qualifying employers that purchased coverage in the small group market outside of SHOP exchanges, which were first established in 2014. Receipt of the credit for any years between 2010 and 2013 does not disqualify an employer from receiving the credit in 2014 and in subsequent years.

Costs and Complexity Deter Credit Claims

Small employers have not viewed the credit as a sufficient incentive to begin offering health insurance because the credit amount may not offset costs enough to justify the cost for health insurance premiums. In addition, our 2012 report described how small business owners generally do not want to spend the time or money to gather the necessary information to calculate the credit, given that the credit will likely be insubstantial. Tax preparers told us it could take 2 to 8 hours or possibly longer to gather the necessary information to calculate the credit and that the tax preparers spent, in general, 3 to 5 hours calculating the credit. To the extent that preparers did these tasks, small employers would generally incur additional cost for these services.

For example, a major complaint we heard in discussion groups with employers, tax preparers, and insurance brokers centered on gathering information on FTEs and the related health insurance premiums. Eligible employers reportedly did not have the number of hours worked for each employee readily available to calculate FTEs and their associated average annual wages nor did they have the required health insurance information for each employee readily available.

Our 2012 report also noted that the complexity involved in claiming the tax credit was significant, deterring small employers from claiming it. The complexity arises not only from the various data that must be recorded and collected (as just described), but also from the various eligibility requirements in the design of the credit and number of worksheets to be completed.

To determine eligibility requirements, exclusions from the definition of "employee" and from other rules make the calculations complex. For

calculating the number of FTEs and their wages, workers excluded from the definition of employee are seasonal workers (an employee who works no more than 120 days during the year), a self-employed individual, a 2 percent shareholder in an S-corporation, a 5 percent owner of an eligible small business, or someone who is related to or a dependent of these people. While seasonal workers are excluded from FTE counts, insurance premiums paid on their behalf count toward the tax credit. In determining premiums paid by the employer, the rules exclude employer contributions to health reimbursement arrangements, health flexible spending accounts, or health savings accounts. Similarly, an employer's premium payments exclude tobacco surcharges if an issuer charges higher premiums for tobacco users.

As for the complexity of the worksheets and paperwork to be completed to claim the credit, in 2012, tax preparers told us that they thought that IRS did the best it could with the Form 8941 given the credit's complexity.[16] IRS officials said they did not receive criticism about Form 8941 itself but did hear that the instructions and its seven worksheets were too long and cumbersome for some claimants and tax preparers. On its website, as of 2012, IRS tried to reduce the burden on taxpayers by offering "3 Simple Steps" as a screening tool to help taxpayers determine whether they might be eligible for the credit. However, to calculate the actual dollars that can be claimed, we found in 2012 that the three steps become 15 calculations, 11 of which are based on seven worksheets, some of which require multiple columns of information.

Given the effort involved to make a claim and the uncertainty about the credit amounts, our 2012 report discussed the view that having a way to quickly estimate employers' eligibility for the credit and the amount they might receive would help them decide whether the credit would be worth the effort. However, we also noted in 2012 that this would not reduce the complication of finding all the documentation needed to file Form 8941. Further, some employers may believe they are eligible based on a calculator, but then turn out to be ineligible, or find they are eligible for a smaller credit amount when they complete Form 8941 with all the required information.

[16]See IRS Form 8941, *Credit for Small Employer Health Insurance Premiums*.

IRS's Taxpayer Advocate Service developed a calculator in 2012 to quickly estimate an employer's eligibility, but this still requires gathering information such as wages, FTEs, and insurance plans. Our analysis showed that use of this tool peaked in March 2014 with 5,383 uses, and has declined since then, falling to less than 1,000 uses by February 2016.[17] The Centers for Medicare & Medicaid Services officials said they launched a SHOP Small Business Health Care Tax Credit Estimator on the federal exchange website in early 2014 to help employers determine if they qualify for the tax credit as well as the size of the credit they might receive.

Lack of Awareness May Contribute to Low Credit Claims, Although IRS Engaged in Significant Outreach

Many small businesses reported that they were unaware of the credit, as discussed in our 2012 report. The National Federation of Independent Businesses Research Foundation and the Kaiser Family Foundation both estimated that about half of small businesses were aware of the credit as of May 2011. The extent to which the lack of awareness prevented eligible employers from claiming the credit is unknown, particularly given other reasons for not claiming the credit. Further, a number of small business employers would not be eligible for the credit regardless of their awareness. Even if employers were unaware, their accountants or tax preparers may have been aware, but did not inform their clients because they did not believe their clients would qualify or because the credit amount would be very small.

To raise initial awareness of the credit, IRS conducted significant outreach, as discussed in our 2012 report. First, IRS developed a communication and outreach plan, written materials on the credit, a video, and a website. Second, IRS officials reached out to interest groups about the credit and developed a list of target audiences and presentation topics. IRS officials began speaking at events in April 2010 to discuss the credit and attended more than 1,500 in-person or web-based events from April 2010 to February 2012. Discussion of the credit at the events varied from being a portion of a presentation covering many topics to some events that focused on the credit.

[17]This number includes uses of a new tool, which started in May 2015. According to the Advocate's website, the tool helps to determine credit eligibility and estimate the amount, but does not determine whether the health insurance plan is eligible and which employees should be included in the credit estimation.

When we issued our 2012 report, IRS did not know whether its outreach efforts increased awareness of the credit or were otherwise cost effective. It would be challenging however to estimate the impact of IRS's outreach efforts on awareness with a rigorous methodology. As we reported in 2012, based on feedback they received, IRS officials told us they believe their efforts have been worthwhile and used this feedback to expand its outreach to include insurance brokers in 2012. IRS also issued a press release in 2014 to urge small employers to consider claiming the tax credit.

Addressing Factors and Expanding Credit Use Could Require Substantive Design Changes

Our 2012 report discussed ways that the design of the credit could be altered to spur use of the tax credit. Given that most small employers do not offer insurance and that the credit may be too small an incentive to convince employers to provide health insurance, we found that it may not be possible to significantly expand use of the credit without changing its design.

Amending the eligibility requirements or increasing the amount of the credit may allow more businesses to claim the credit, but as we noted in 2012, these changes would increase its cost to the federal government.[18] Options for changing the design of the credit include the following:

- increasing the amount of the full credit, the partial credit, or both;
- increasing the amount of the credit for some by eliminating state premium averages;
- expanding eligibility requirements by increasing the eligible number of FTEs and wage limit for employers to claim the partial credit, the full credit, or both; or
- simplifying the credit calculation by (1) using the number of employees and wage information already reported on the employer's tax return, which could reduce the amount of data gathering as well as credit calculations because eligibility would be based on the number of employees rather than FTEs; and (2) offering a flat credit amount per FTE (or per employee) rather than a percentage. A tradeoff inherent in these changes would be to reduce the precision in targeting the credit.

[18]The data limitations that made it difficult to estimate the number of businesses eligible for the current credit also make it difficult to estimate the impact of any design changes.

Administration and Legislative Proposals to Change the Design and Status of the Credit

The administration has offered proposals to alter the small employer health tax credit. The most recent proposal as of February 2016, would (1) expand eligible employers to include those with up to 50 FTEs; (2) begin the phase out at 20 FTEs; (3) provide for a more gradual phase-out based on average wage and number of employees; (4) eliminate the requirement that an employer make a uniform contribution for each employee (although nondiscrimination laws will still apply); and (5) eliminate the limit imposed by the area average premium.

Between 2011 and 2015, Congress has considered more than 20 bills on the small employer health tax credit. Many offered ways to expand usage of the credit. For example, the bills sought to increase the number of eligible small employers (e.g., allowing an employer to have 50 FTEs); changing the phase out formula; allowing the credit to be claimed in more than two consecutive years; increasing the average annual wage limitation; eliminating the requirement that employers contribute the same percentage of cost of each employee's health insurance; eliminating the cap limiting the credit amount to average premiums paid to a state health insurance exchange; and allowing a partial credit for health insurance purchased outside of SHOP exchanges. Some of these proposed bills restricted the use of the credit for abortion coverage. At least one would have eliminated the credit and a few offered alternatives to the credit.

In closing, the Small Employer Health Insurance Tax Credit was intended to offer an incentive for small, low-wage employers to provide health insurance. However, utilization of the credit has been lower than expected, with the available evidence suggesting that the design of the credit is a large part of the reason why. While the credit could be redesigned, such changes come with trade-offs. Changing the credit to expand eligibility or make it more generous would increase the revenue loss to the federal government.

Chairman Huelskamp, Ranking Member Chu, and members of the Subcommittee, this concludes my prepared remarks. I look forward to answering any questions that you may have at this time.

GAO Contact and Staff Acknowledgments

If you or your staff have any questions about this testimony, please contact James R. McTigue, Jr., Director, Tax Issues, Strategic Issues, (202) 512-9110 or mctiguej@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. GAO staff who made key contributions to this

testimony, or previous related work, are Tom Short, Assistant Director; Anna Bonelli, Amy Bowser, Leia Dickerson, Ed Nannenhorn, Robert Robinson, Cynthia Saunders, Lindsay Swenson, and Jason Vassilicos.

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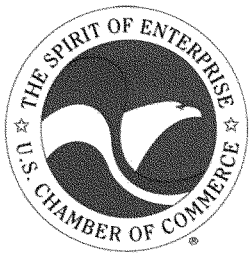

Statement of the U.S. Chamber of Commerce

ON: **"Lip Service but Little Else: Failure of the Small Business Health Insurance Tax Credit "**

TO: **THE HOUSE SMALL BUSINESS COMMITTEE'S SUBCOMMITTEE ON ECONOMIC GROWTH, TAX AND CAPITAL ACCESS**

DATE: **March 22, 2016**

The Chamber's mission is to advance human progress through an economic, political and social system based on individual freedom, incentive, initiative, opportunity and responsibility.

The U.S. Chamber of Commerce is the world's largest business federation representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations. The Chamber is dedicated to promoting, protecting, and defending America's free enterprise system.

More than 96% of Chamber member companies have fewer than 100 employees, and many of the nation's largest companies are also active members. We are therefore cognizant not only of the challenges facing smaller businesses, but also those facing the business community at large.

Besides representing a cross-section of the American business community with respect to the number of employees, major classifications of American business—e.g., manufacturing, retailing, services, construction, wholesalers, and finance—are represented. The Chamber has membership in all 50 states.

The Chamber's international reach is substantial as well. We believe that global interdependence provides opportunities, not threats. In addition to the American Chambers of Commerce abroad, an increasing number of our members engage in the export and import of both goods and services and have ongoing investment activities. The Chamber favors strengthened international competitiveness and opposes artificial U.S. and foreign barriers to international business.

Statement on

"Lip Service but Little Else:

Failure of the Small Business Health Insurance Tax Credit"

Submitted to

THE HOUSE SMALL BUSINESS COMMITTEE'S

SUBCOMMITTEE ON ECONOMIC GROWTH,

TAX AND CAPITAL ACCESS

on behalf of

U.S. CHAMBER OF COMMERCE

By

Harold Jackson

Executive Chairman

Buffalo Supply, Inc.

Lafayette, Colorado

March 22, 2016

Chairman Huelskamp, Ranking Member Chu and distinguished members of the Subcommittee, thank you for inviting me to testify before you today about my experiences with the small business health insurance tax credit. I hope that my testimony and remarks will help provide a concrete real life example as to the shortfalls of this premium tax credit which is unfortunately illusive to most small businesses. I understand that most tax credits are designed to incent or change behavior and - to be clear - we have always provided health insurance for our employees. But the fact is prices have increased so dramatically year after year that we may not be able to continue to provide health insurance in the future. Because we are ineligible, this tax credit does not help me in any way to provide affordable health coverage to my employees now. And unfortunately, it will not encourage me to do so in the future - if and when - I may be forced to stop offering insurance because of prohibitively escalating costs. Despite efforts to encourage employers to provide health insurance and bolster the small group and individual markets, this premium tax credit helps with neither goal. Instead, we are unable to mitigate increasing costs to our company and our employees as we strive to provide our Buffalo Supply family with health insurance.

My name is Harold Jackson. I am the Executive Chairman of Buffalo Supply, Inc., a 20-employee small business located in Lafayette, Colorado, specializing in federal contracting for medical

supplies and equipment. I am honored to speak with you today on behalf of the U.S. Chamber of Commerce. The U.S. Chamber of Commerce is the world's largest business federation, representing the interests of more than three million businesses and organizations of every size, sector, and region. As you might know, more than 96 percent of the Chamber's members are small businesses with 100 or fewer employees, just like mine, and 70 percent of which have 10 or fewer employees.

Company Background

Since 1983, our family-owned business has been devoted to providing high-tech medical supplies and high-tech medical equipment to the federal government. While our company has grown to be successful, we began in the basement of my brother Stonewall's home. With a strong belief that he could help companies understand the federal procurement process and bring value to federal customers, my brother established Buffalo Supply with originally just one supplier partner. Over the past 33 years, we have grown to be one of the top 20 federal contractors for medical supplies and equipment and are currently the exclusive small business federal distributor for many well-recognized brands, such as Integra Lifesciences, Stryker Spine, STERIS Corporation, and Bausch + Lomb Storz (to name a few). Today, we have 16 full-time employees and four part-time employees.

At Buffalo Supply, Inc. (BSI), we understand the complexities of federal contracting and work closely with our supplier partners to ensure that we are bringing high quality medical supplies and equipment to our Veterans and warfighters, while also helping our supplier partners remain compliant with all Federal Acquisition Regulations. We hold multiple FSS Contracts, ECAT and DAPA contracts, and Blanket Purchase Agreements (BPAs) to ensure that federal customers are able to purchase the products they need through their preferred contract platform.

BSI has numerous Federal Supply Schedule contracts with products to satisfy a wide variety of operating room and health care needs. Through our diligent work and extensive experience in the federal marketplace, BSI has developed a high level of expertise in helping federal institutions efficiently meet their objectives of providing high quality health care equipment at competitive prices. We primarily provide our goods and services to federal medical facilities, mainly within the Department of Veterans Affairs, Department of Defense, and Department of Health and Human Services.

We pride ourselves not only on providing exceptional customer service to our customers and a deep level of expertise to our supplier partners, but also on providing a high quality workplace for our employees. We spend a lot of time and effort in training our employees to stay up to date on changes to regulations, changes in the federal market, etc. When you call BSI, you always get a live person. Even if you ask for something we can't provide, we'll help you find it. We went to be the government buyers' partner in providing the products our vets and warfighters deserve, helping how-

ever we can. And to help us do this, we spent a lot of time and effort on hiring. It's extremely important to not just find people with the right education level and the skill levels, but also with the personality that will complement our organization—to keep the attitude positive and moving forward. We're a family at our small business—our average customer service rep has been with BSI for nearly 10 years.

Additionally, we also share the profits with the employees through bonus programs. If we grow the business to the projections, then everyone gets a couple hundred dollars a month in addition to their normal check—and it is amazing how that creates a positive attitude. At the end of the year there is an additional profit share program—we are all pulling towards the same cause and when the company is successful, each of our members should benefit.

While our primary measure of success is the happiness of our employees and our customers, we have been honored to receive some external praise as well. Colorado Biz Magazine named BSI as one of its top 10 small businesses to work for in Colorado. The DC-based Coalition for Government Procurement and the US General Services Administration gave BSI their "Excellence In Partnership - Most Innovative Small Business Award" for 2003.

Personally, I have served as an advisor for the University of Colorado, Denver School of Business for Entrepreneurship. I am an active member of: The U.S. Chamber of Commerce (where I serve on the Small Business Council and the Government Procurement Sub-Council); the Coalition for Government Procurement; and the NFIB Leadership Council of Colorado. In 2006, the Bush Administration appointed me to the Small Business Administration's Regulatory Fairness Board, where I served for two years. In 2012, I was honored by the Leadership Council of NFIB/Colorado as Colorado's Small Business Champion of the Year. On November 6, 2013, I received an award for a Lifetime of Service to Small Business. I am grateful for these accolades but recognize the company and our employees made all of this possible.

In my leisure time, I love to fill my days camping, "Jeeping," and as an amateur photographer. Once a year, I take off with my 4X4 crew and disappear into the wilderness of Utah and Arizona. I am eager to teach my grandson how to participate in all of these activities—if I can get my daughter Kara's permission.

Health Care: My Experience with Premium Increases

We have offered health care coverage to our employees for many, many years ever since we started hiring additional employees—probably back in 1990. Since then, providing health insurance to our workers has always been a priority—it is part of our culture and important for attracting and maintaining the best employees. But, it hasn't been easy, and in fact, each year it gets harder and harder for us financially.

As an employer committed to providing insurance to our employees and their families, our history with offering health insurance has been somewhat tumultuous. We try to shield our employees as much as possible to the challenges we have faced. For many years we provided our employees with health insurance coverage through a PPO plan, which allowed employees to pay a bit extra to go to out-of-network providers—giving them a greater level of choice.

We came to a point in the mid-2000s where we were growing quickly and insurance premiums were increasing so much that we had to try to find some new solutions. Health Savings Accounts, or HSAs, were new to the market place and we did a lot of research to understand if offering a High-Deductible Health Plan in conjunction with an HSA would be good for our employees. A few members in our management team volunteered to review their medical expenses for the previous year and compare how much they would have spent out-of-pocket with the two different types of plans. After reviewing the comparisons, we decided to offer an HDHP plan and fully fund our employees' HSAs to cover the cost of the associated HDHP's deductible. Unfortunately, as premiums have increased, our company's ability to fund the HSA to cover the associated HDHP's deductible has waned—at first down to 50% of the deductible and now to zero. However, we continue to pay 100% of the premiums for our employees and their dependents—which continues to make BSI stand out to job applicants.

In addition to changing plan types and HSA contributions, we have also had to change carriers, on average every 1-3 years. We have rotated between Anthem, United, Aetna and Rocky Mountain Health in an effort to find more affordable coverage.

Beyond changes in plan design and carriers, we have seen tremendous cost increases despite modest decreases in benefits. For example, in 2010 our average premium was under $12,840 annually for family coverage. This average premium skyrocketed to a $16,380 annual premium for family coverage this year (over a 25% increase). This increase accompanies less robust coverage. Now our health insurance plan has a higher family deductible (up from $3,000 to $5,000) and a new out-of-pocket maximum of $6,800—up from $4,000 in 2010. So we are paying more in premiums and sadly—our employees are also paying more when they need medical care and services.

My Limited Experience with the Elusive Small Business Premium Tax Credit

When the Colorado Exchange "Connect for Health Colorado" opened its Small Business Health Options Plan in 2015, I went online and tried to enroll. I learned through my colleagues at the U.S. Chamber and NFIB that small businesses with 25 or fewer employees may be eligible for a small business premium tax credit provided coverage was purchased through the SHOP. Unfortunately, the amount of information that the SHOP asked for in its on-line application process was incredible; much of the information requested—I didn't have. They wanted a lot of information about

spouses and dependents that we don't have or maintain—such as dependent's and spouse's Social Security numbers, dates of birth, and tobacco use. It took me two or three days to gather up this information. I spent about 10 hours entering this information into the system, after which I couldn't figure out how to review the plans available or get quotes.

I called the 800 number and they told me that they don't give quotes to small business. The SHOP representative said that I needed to go through a broker. When I called a broker, clearly he had heard from other businesses like me about the SHOP—even though SHOP referred me to him—he told me "I can get you a quote, but I don't want to go through the exchange, it's too much hassle."

I mention all of this because—as you know—the small business premium tax credit is only available to small businesses (those with 25 or fewer employees earning on average less than $50,000 per year) that purchase coverage for their employees on the SHOP. Clearly, based on my experience, this is an onerous "hoop" in and of itself as a requirement. Unfortunately, it is not the only hoop that makes the prospect of obtaining a small business tax credit elusive. The other—and bigger—hurdle for small businesses is the annual average earning cap. The average annual earning threshold is simply too low.

Possible Solutions/Improvements?

I do believe small businesses need help, both to encourage others (like we do) to provide health insurance and also to help those who (perhaps also like we) may one day find that they cannot continue to provide health insurance to their employees. I am certainly not a tax expert—although lord knows I pay taxes and wish I were—but it seems to me like there are several ways to make this tax credit more useful to small businesses.

- First, it should be available to small businesses that purchase coverage on or off the SHOP—this would level the playing field a bit.
- Second, the average earning level must be raised.
- Third, the tax credit should be available for more than 2 consecutive years.
- In any event, the benefit of this tax credit needs to be easier for businesses to assess and the hoops should be simplified for businesses to more easily satisfy.

Conclusion

I am proud of the company that my brother started and that we as a family have built. I am proud of the employees that we have—our broader family. I am concerned about the ability of our company and others around the country to continue to provide health insurance and I think this premium tax credit may be increasingly necessary to encourage companies to provide coverage—particularly

given the premium increases we continue to see year over year. Based on my experience, I think part of the problem is that the rules for the tax credit are so confusing that small businesses cannot assess benefit of the tax credit without hiring outside counsel. Ultimately, any changes should not only increase the tax benefit to help small businesses provide health insurance for their employees, but must be simple and easily understood. As my brothers and I transition our company to our children, I hope that they will be able to benefit from the struggles we have had in many areas and learn from our successes as well. Unfortunately, at this point, providing health insurance continues to be a struggle.

Thank you for this opportunity to testify, and I look forward to your questions.

TESTIMONY BEFORE THE UNITED STATES CONGRESS
ON BEHALF OF THE

NATIONAL FEDERATION OF INDEPENDENT BUSINESS

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Testimony of

Ms. Holly Wade,
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before the

Subcommittee on Economic Growth, Tax and Capital Access

on the subject of

Lip Service but Little Else: Failure of the Small Business Health Insurance Tax Credit

on the date of

March 22, 2016

Good morning Chairman Huelskamp, Ranking Member Chu and members of the Subcommittee on Economic Growth, Tax and Capital Access. Thank you for the opportunity to testify today. I am pleased to be here on behalf of the National Federation of Independent Business (NFIB) as the Committee discusses the small business health insurance tax credit.

Small business owners rank the cost of health insurance as their most severe problem in operating their business out of 75 potential issues, with 56 percent of small business owners finding it a "critical" problem.[1] The high cost of health insurance is the main reason owners do not offer employer-sponsored health insurance and the main reason owners discontinue providing the benefit. And for those offering, many owners annually confront the arduous task of adjusting profit expectations, insurance plans, cost-sharing and other mechanisms to help absorb often erratic changes in total premium costs.

The rising cost of health insurance has forced many small employers to rethink the viability of offering health insurance to their employees, especially during and in the wake of the great recession. Since 2008, the offer rate for small businesses with fewer than 50 employees has dropped precipitously. Small business owners are far more hesitant to committing themselves to offering a long term, high cost benefit. The offer rates for this group have fallen over 10 percentage points from 43 percent offering in 2008 to 32 percent in 2014.[2]

The small business health insurance tax credit was a targeted approach to help curb health insurance costs for offering small employers and was intended to provide an incentive for those that do not, to start offering. However, the tax credit was largely ineffective on both fronts as its design is exceedingly restrictive, complicated, and only offers limited and temporary relief to a larger small business cost problem. To date, the tax credit has generally served as a windfall for the few small business owners who quality and take the time, or pay an accountant, to file for it.

In 2010, the Congressional Budget Office (CBO) estimated the tax credit would provide $40 billion in cost relief for small business owners over 10 years. More recently, CBO has lowered the cost estimate to $10 billion over 10 years due to lower than expected utilization. NFIB initially estimated the eligible population of small business owners to be about 1.4 million. The Administration's estimate, which included non-offering firms, was 4 million.[3] IRS data reported that in 2010 just over 170,000 small businesses claimed the tax credit at a cost of $468 million, despite considerable outreach efforts by the IRS and other groups to raise awareness of the credit.[4]

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[1] Wade, Holly, *Small Business Problems and Priorities,* NFIB Research Foundation, August 2012.

[2] Source: Agency for Healthcare Research and Quality, Center for Financing, Access and Cost Trends. 2008-2014 Medical Expenditure Panel Survey-Insurance Component.

[3] Fact Sheet: Small Business Health Care Tax Credit, April 1, 2010. https://www.whitehouse.gov/the-press-office/fact-sheet-small-business-health-care-tax-credit.

[4] The IRS mailed 4.4 million postcards to small business owners informing them of the tax credit.

The ineffectiveness of the tax credit is largely due to four factors. The first, and most limiting, factor in claiming the tax credit is that eligibility was targeted to and most beneficial for those small businesses least likely to offer health insurance. Health insurance offer rates vary significantly by employee size of firm and average wages.[5] Those businesses with lower than average wages are more likely to compensate employees in cash and not benefits. Health insurance costs would significantly crowd out employees' take home pay. Smaller, small businesses are also less likely to offer health insurance and those factors vary from high administrative burdens, low take-up rates, and higher than average premiums.

Second, the tax credit is exceedingly complicated to verify eligibility and claim the credit. The IRS estimates that recordkeeping requirements to claim the credit average just under 11 hours for most filers. The education component is estimated to take about 1 1/2 hours. And finally the time spent preparing and filing is estimated to take an average of 2 hours and 46 minutes. While most small employers use a tax preparer for their business, the costs associated with claiming the tax credit will deter many from going through the process in the first place.

Since 2010, NFIB has received numerous complaints from small business owners regarding the complexity of the tax credit. Some owners called to say that even their tax preparer told them the credit was not worth the extra costs associated with determining eligibility and filling out the paperwork.

Third, the tax credit is temporary. At most, the credit was available to small business owners for six years if they started claiming the credit in 2010. Currently, small business owners can claim the credit for two years. Health insurance is a long term benefit offered by employers to retain and recruit employees. Owners generally start offering the benefit when profits allow for the added costs. Profitability was an important factor in offering health insurance for 63 percent of newly offering firms.[6] The tax credit is a little relief in the long term cost challenges small business owners face in offering health insurance.

And fourth, as of July 1, 2014, the small business tax credit is only available to qualifying businesses through the Small Business Health Options Program (SHOP) marketplaces. Most small employers purchase health insurance through an insurance agent and therefore rely on the agent for suggesting insurance options available to them. Only 13 percent of offering small businesses visited their SHOP exchange. And of those offering and shopped, less than 1 percent purchased through the SHOP marketplace. Among non-offering firms, 17 percent of small employers shopped for coverage through a SHOP exchange. The vast majority of non-offering firms did not select a plan through SHOP because the plans were too expensive.

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[5] Source: Agency for Healthcare Research and Quality, Center for Financing, Access and Cost Trends. 2008-2014 Medical Expenditure Panel Survey-Insurance Component.

[6] Dennis, WJ, Jr. (2014). Small Business's Introduction to the Affordable Car Act, Part II. NFIB Research Foundation: Washington, DC. http://www.nfib.com/assets/nfib-aca-study-2014.pdf.

The small business health insurance tax credit was too narrowly designed to be an effective cost savings tool for small employers. The tax credit has now been available to qualifying small employers for 5 years and still, very few businesses have benefited. But more importantly, health insurance costs continue to increase, and small business owners continue to struggle with their ability to afford offering the benefit.

I appreciate the opportunity to present NFIB's views and data on the effects of the small businesses health insurance tax credit. I look forward to answering any questions you might have.

Michael Ricco, Quality Manager, AEEC
on behalf of the
U.S. Women's Chamber of Commerce

Before the House Small Business Committee
Subcommittee on Economic Growth, Tax and Capital Access
for the Hearing
"Lip Service, But Little Else: Failure of the Small Business Health Insurance Tax Credit"
Wednesday, March 22, 2016, at 10:00 a.m.
Rayburn House Office Building, Room 2360

Good morning Chairman Huelskamp, Ranking Member Chu, and other Subcommittee members. Thank you for this opportunity to provide testimony before the Subcommittee on Economic Growth, Tax and Capital Access.

I am Michael Ricco, Quality Manager for AEEC—a women- and minority-owned small business located in Reston, VA. Our President—Sangita Patil—wishes she could be here in person, but she had a conflict. AEEC is an award-winning professional services organization offering top-quality technology, environmental, and engineering solutions to US Federal Government and Fortune 50 customers since 1995. We support our customers' requirements and offer a range of customized solutions with the highest degree of honesty, integrity, and service excellence. We offer solutions that are efficient, appropriate and worthy of the investment. Our company is also a member of the U.S. Women's Chamber of Commerce.

While I would like to testify today that my company has been able to benefit from the Small Business Health Care Tax Credit, that is unfortunately not the case because we are ineligible for the following reasons. First, we are ineligible because we have more than 25 employees. As this Subcommittee is well aware, there are many differing definitions of what a "small business" is—ranging from 50 to 100 to even 500 employees. The size standard for companies to use this health care tax credit is on the woefully low side and should be increased so that many more legitimate small businesses can take advantage of this tax credit.

Second, we are an IT company and as such our employees tend to earn higher salaries than many other employees working in small businesses nationwide. Therefore, we do not qualify because our workers on average make more than the $50,000 cap as stated in the implementation language governing this credit. We question the fairness of this cap because, in essence, it punishes our company for paying our employees a higher wage. This limitation, in our view, should be removed from the eligibility requirements of this tax credit.

Why do I say these changes could be made? Because AEEC would very much like to use this credit. Receiving a tax credit for up to 50 percent of our health care costs would certainly help us reduce costs. We all know and as pointed out in the GAO report, "plans for small employers are likely to have higher premiums, less coverage and higher costs than plans for large employers." Yet we, as a small business, want to do the right thing and provide health care coverage for our hard-working employees. AEEC has long provided health coverage to all of our employees and we go far beyond the minimum coverage now required by the Affordable Care Act. Our package would fall into the platinum or high-level gold range. So expanding the tax credit would go a long way to help us pay for these premium increases and cover our additional compliance and reporting requirements.

Here is something else to consider. The expectations that would-be employees have for benefits coverage get higher with salary levels. For example, a cashier at McDonald's is going to be thrilled with any health care coverage while a Senior Data Architect ex-

pects a platinum health. So small businesses like ours are among the most in need for a tax credit.

Finally I would like to stress that while the ACA very much helped very small businesses with subsidies and large businesses benefit from large pools that keep their costs down, it is the small businesses in middle—particularly those between 50-100 employees—that could benefit the most from this health care tax credit. Therefore, I would ask this Subcommittee to consider making changes to this credit so that more small businesses that are so critical to our nation's economy can be better able financially to pay these health care costs.

Two changes I already mentioned—increasing the eligibility threshold for number of employees that work at a small business and removing the wage barrier that excludes so many small businesses from eligibility. Two other reforms that we would recommend are increasing the credit so that it is more cost effective for small businesses to actually use it and to make it last longer than two consecutive tax years.

Again, thank you for this opportunity to address this Subcommittee. AEEC is dedicated to providing our employees with the best health care coverage possible. Yet the fact remains that we are still a small business and these costs are quite high. We would urge this Subcommittee to put forth language that would make this important health care tax credit more accessible to the small businesses in our nation that I would like to point out, on average, account for over 60 percent of all net new jobs created in this country.

I would be happy to answer any of your questions.