

MINUTES OF THE HOUSE TAXATION COMMITTEE

The meeting was called to order by Chairman Richard Carlson at 9:10 a.m. on March 5, 2010, in Room 783 of the Docking State Office Building.

All members were present except:

Representative Pat George- excused  
Representative Mario Goico- excused  
Representative Bill Light- excused  
Representative Melody McCray-Miller- excused  
Representative Larry Powell- excused  
Representative Sharon Schwartz- excused

Committee staff present:

Gordon Self, Office of the Revisor of Statutes  
Scott Wells, Office of the Revisor of Statutes  
Chris Courtwright, Kansas Legislative Research Department  
Brandon Riffel, Kansas Legislative Research Department  
Marla Morris, Committee Assistant

Conferees appearing before the Committee:

Representative Arlen Siegfroid  
Representative Milack Talia  
Ken Daniel, Topeka Independent Business Association  
Beverly Gossage, HSA Benefits Consulting  
Daniel S. Murray, National Federation of Independent Business-Kansas (NFIB)  
Richard Cram, Kansas Department of Revenue  
Linda Sheppard, Director of Accident and Health Division, Kansas Insurance Department

3/5/10

Others attending:

See attached list.

Chairman Carlson opened the hearing on:

**HB 2682 - Allowing employees to retain and receive contribution from employer on individual policies, requiring employer to provide cafeteria plan, and requiring administering carriers to provide health savings accounts and high deductible health plans**

Staff Scott Wells, Office of the Revisor of Statutes, briefed the Committee on **HB 2682**. The bill would allow a small employer who does not offer a group health insurance plan to contribute to the premium of an eligible employee's individually underwritten health benefit plan. The bill would allow eligible employees to retain the individually underwritten plan even if they are eligible to enroll in a small employer health benefit plan. The small employer could then establish a health reimbursement plan to contribute to the employee's individual plan. The employer would pay the employee the same amount that would have been contributed to the employer plan if the employee had elected to participate. The bill would allow a taxpayer to deduct from their federal income tax, the amounts paid for premiums for the taxpayer, taxpayer's spouse or dependents health insurance policy. He stood for questions.

Representative Arlen Siegfroid, addressed the Committee in support of **HB 2682** and the proposed balloon amendment. He stated the bill represents a modest, yet notable step for Kansans in providing affordable insurance coverage to small businesses and their employees (Attachment 1). He stood for questions.

Representative Milack Talia, supports **HB 2682** and asked the Committee to consider expanding the scope of the legislation allowing the employer to contribute to the premium of more types of health benefit plans for employees and applying this to all types and sizes of businesses (Attachment 2). He stood for questions.

Ken Daniel, Topeka Independent Business Association, supports **HB 2682**. He testified that Small Group Insurance Laws have caused damage to employees of small businesses (Attachment 3). Mr. Daniel feels **HB 2682** would accomplish the following:

CONTINUATION SHEET

Minutes of the House Taxation Committee at 9:00 a.m. on March 5, 2010, in Room 783 of the Docking State Office Building.

If an employer offers a Section 125 Plan, individuals can qualify and use it to obtain a tax-free treatment of their premium even if they own an individually-purchased insurance policy.

Employers can contribute to the premium costs for an employee's individually underwritten policy.

This at least takes a "baby step" toward tax equity for employees of small businesses.

Mr. Daniel stood for questions.

Beverly Gossage, HSA Benefits Consulting supports **HB 2682** and anticipates the following outcome with passage of the bill (Attachment 4):

More employers will contribute to premium.

More employees will become insured.

Employees will have more coverage options.

Employees will select policies with lower premiums.

No minimum number of participants will be an incentive for employers to provide assistance.

No minimum percentage of premium will be an incentive for employers to provide assistance.

Though no group plan is available, employees will choose to be insured through private policies for their portability and to receive the employer's contribution toward premium.

Formerly uninsured employees will discover the security in owning a personal policy.

Employers and employees will discover the convenience of personal policies.

Employers and employees will begin to see a tax savings.

Some employees will chose a personal policy because they can receive a state tax deductions.

Ms. Gossage proposed an amendment to **HB 2682** (Attachment 5). She stood for questions.

Daniel S. Murray, National Federation of Independent Business-Kansas (NFIB), supports **HB 2682**. The NFIB believes **HB 2682** will help slow the rising cost of insurance and reduce the number of uninsured Kansans by allowing small businesses and their employees more choice in the current small-group market (Attachment 6).

Richard Cram, Kansas Department of Revenue and Linda Sheppard, Director of Accident and Health Division, Kansas Insurance Department will return on Monday, March 8, 2010 to present their testimony in opposition to **HB 2682**.

Chairman Carlson directed the Committee to these proponents providing written only testimony on **HB 2682**:

Sandy Braden, Kansas Association of Health Underwriters (Attachment 7)

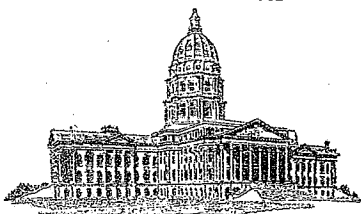
Tim Witsman, Wichita Independent Business Association (Attachment 8)

Chairman Carlson closed the hearing on **HB 2682**.

The next meeting is scheduled for March 8, 2010.

The meeting was adjourned at 10:45 a.m.





ARLEN H. SIEGFREID  
SPEAKER PRO TEM

March 5, 2010

House Bill 2682  
House Taxation Committee

Mr. Chairman and members of the committee,

I come before you today in support of HB 2682 and the balloon amendment being offered. As you are each aware, personal health insurance coverage is an issue of critical importance. While national legislation seeks to fundamentally alter the landscape of the healthcare and insurance industry, the bill before us today represents a modest, yet notable step for Kansans in providing affordable insurance coverage to small businesses and their employees.

Currently, small businesses, entrepreneurs, and farming operations not only face skyrocketing rates and premiums, but also restrictive rules regarding taxation of those policies and premiums. While the legislation before you is not the ultimate solution for small businesses, it's an important start.

By enabling businesses to attract employees and grow their companies, we not only improve the well being of the workers they hire, but also bolster the state's economy. Kansas businesses operate in an incredibly competitive environment. The simple ability to provide an affordable healthcare package is an important determinant in recruiting talented workers—which you'll find at the nucleus of any successful business, large or small.

These are the businesses and individuals we need to be not only protecting, but also incentivizing. They represent organic job growth in Kansas, and they need the ability to provide adequate and affordable care to potential employees. This legislation provides them with a rational tool to continue putting Kansans to work, and maintain reasonable rates for a basic job requirement in today's market.

I stand firmly in support of this legislation, as well as the balloon amendment, and encourage each of you vote yes on HB 2682.

Thank you.

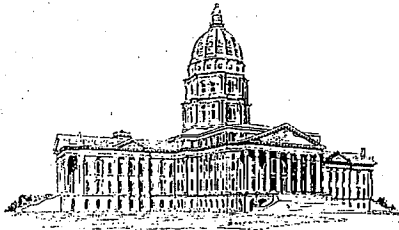
A handwritten signature in cursive script that reads "Arlen Siegfroid".

Rep. Arlen Siegfroid  
Speaker Pro Tem

House Taxation  
Date: 3-5-10  
Attachment: 1

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STATE OF KANSAS | 23RD DISTRICT

March 4, 2010

Chair Carlson, Vice-Chair King, Rep. Menghini, and Members of the Taxation Committee,

I would like to provide testimony in support of HB 2682. Allowing small business employers contribute to the premium of an eligible employee's individually underwritten health benefit plan has the potential to reduce the number of uninsured Kansans. However, I would like to humbly ask the committee to consider expanding the scope of this important legislation in two ways.

The first would be to allow the employer to contribute to the premium of more types of health benefit plans for employees. A consequence of this legislation would be to exclude an employee from receiving the employer-contribution if the employee declines to enroll in the employer health benefit plan and then enrolls in their spouse's health benefit plan. Expanding the types of health benefit plans employers can contribute to would provide more alternatives for health insurance coverage.

The second would be to apply this to all types and sizes of businesses, in addition to small businesses. I've heard stories from families that increases in health care costs cause big businesses to go into cost-cutting mode. What happens then is more of the health care costs are shifted to workers through decreased benefits and increased premiums, deductibles and co-pays. Including all types and sizes of businesses would enable more employee free choice for health care.

Some additional points for the committee to consider deal with safeguards for employees:

- Prohibiting the employer from arbitrarily reducing the employer-contribution if the employee elects to not enroll in the employer health benefit plan and
- Prohibiting employers from coercing employees to enroll in the employer health benefit plan.

This legislation is a good first step in reducing the number of uninsured Kansans. If more people are priced out of health insurance, our premiums will increase to pay for health care for the uninsured and hospitals will cut services. Please consider expanding and passing this important legislation and thank you for your consideration of this bill.

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March 5, 2010

TESTIMONY TO HOUSE TAXATION COMMITTEE  
ON HOUSE BILL 2682

Board Members

Tara Dimick, Chair  
*E<sup>2</sup> Communications*

Tom Anderson, MD  
*St. Francis Hospital*

Kevin Doel  
*TK Magazine*

Ping Enriquez  
*Ad Veritas Construction*

Rick Farrant  
*GreatLife Golf & Fitness*

Webb Garlinghouse  
*National Electronic Type*

Jim Hamilton, MD  
*Tallgrass Surgery*

Scott Hamilton, DDS  
*Dr. Hamilton & Wilson*

Scott Hughes  
*Silver Lake Bank*

Marc Johnson  
*Kennedy & Coe CPAs*

Rick Kendall  
*Kendall Construction*

David Lippe  
*MACI Publishing*

Larry Magill  
*KALA*

Rise Quinn  
*Lower's*

Tim Royer  
*Fidelity State Bank*

Marvin Spees  
*Capital City Oil*

Matt Strathman  
*Strathman Sales*

Director of Governmental  
Affairs

Ken Daniel  
*Midway Wholesale*

By Ken Daniel  
Chairman, Midway Wholesale  
Director of Governmental Affairs, Topeka Independent Business Assn.

*Kenneth L. Daniel is an unpaid volunteer lobbyist who advocates for Kansas small businesses. He is the Governmental Affairs Director of the Topeka Independent Business Association. He is publisher of KsSmallBiz.com, a small business e-newsletter and website. He is Chairman of the Board of Midway Wholesale, a business he founded in 1970.*

Mr. Chairman and members of the committee.

I would like to speak in support of House Bill 2682. We do have a balloon amendment we would like to offer.

In 2006 (latest available), there were 61,902 employer firms in Kansas. 52,600 of these were firms with 1-19 employees. According to the Kaiser Family Foundation, only 42% of employers with fewer than 20 employees offer group health insurance to their employees. This is down from 62% twenty years ago, and continues to decline.

At the same time, there were 183,600 non-employer firms – firms with no employees other than the owners.

These are the firms, along with their employees, that have the hardest time affording and getting health insurance, yet we continue to attempt to force them to pay higher premiums than almost all others and forbid their employers to help them pay for individual policies or include them in the federal government's tax-free Section 125 Cafeteria Plans.

In addition, there are nearly 60,000 farms in Kansas that are not included in these firms. The overwhelming majority of farms also have a hard time affording and maintaining health insurance coverage for the same reasons the non-farm businesses do.

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Furthermore, the employees of these firms have to pay higher taxes on their health benefits. Some employees of big businesses and unions pay no taxes at all on their health insurance benefits.

Following is a chart which shows the tax treatments on various forms of businesses. A more complete chart showing more forms of businesses follows as "Exhibit A".

<b>TAX TREATMENTS OF VARIOUS ASPECTS OF HEALTH INSURANCE</b>	<b>Policy owned by an individual or family.</b>	<b>Owners of sole proprietorship, partnership, Sub-S Corp, and key employees of Sub-S</b>	<b>Premiums for owners and employees of small "C" Corp, paid by the business.</b>	<b>Premiums for owners &amp; employees of large self-insured "C" Corp, paid by the business.</b>
Federal Income Taxable?	Yes	No	No	No
Section 125 Cafeteria Plan Prohibited?	Yes	Yes	No	No
Social Security Taxes Owed?	Yes	Yes	No	No
Medicare Taxes Owed	Yes	Yes	No	No
State Income Taxable?	Yes	No	No	No
Kansas Premiums Taxes Owed?	Yes	Yes	Yes	No
Required to Pay for 39 Kansas Mandates?	Yes	Yes	Yes	No
Required to Pay Into KS High Risk Fund?	Yes	Yes	Yes	No
Required to Pay for Bankrupt KS Insurers?	Yes	Yes	Yes	No

Small Group Insurance Laws have done great damage to the employees of small businesses, and continue to do so. House Bill 2682 is not a panacea, but it is a beginning. In summary, here is what this bill will accomplish:

- If an employer offers a Section 125 Plan, individuals can qualify and use it to obtain tax-free treatment of their premiums even if they own an individually-purchased insurance policy.
- Employers can contribute to the premium costs for an employee's individually underwritten policy.
- This at least takes a "baby step" toward tax equity for employees of small businesses.

I hope you will support HB2682. I'll be happy to answer any questions,

# EXHIBIT "A"

## TAX EQUITY: COMPARISON OF TAX TREATMENTS

Assumptions: Full-time only, ignore the 7.5% of adjusted gross income deduction

Note that in all of the following cases, Health Savings Accounts can be used to save some taxes.

### ITEMS IN RED ARE NOT TAXED

	Federal Income Taxable?	State Income Taxable?	Social Security Taxable?	Medicare (OASDI) Taxable?	Section 125 Forbidden?	Kansas Premiums Tax?	Pay into KS High Risk Fund?	Pay for Bankrupt KS Carriers
Premiums for policy owned by an individual or family	Yes	Yes	Yes	Yes	Yes	Yes	Yes	Yes
Premiums for policy for sole proprietor, paid with company money	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Premiums for policy paid by Sub-S corporation for an owner (Ditto for partnership partners, key employees of a Sub-S or partnership, highly-paid employees of a Sub-S or partnership.)	No	No	Yes	Yes	Yes	Yes	Yes	Yes
Premiums for policy paid by Sub-S or partnership for ordinary employee	No	No	No	No	No	Yes	Yes	Yes
Premiums for policy paid by "C" Corp for employees including owners	No	No	No	No	No	Yes	Yes	Yes
Benefits paid by self-insured "C" Corp for employees including owners	No	No	No	No	No	No	No	No
Benefits paid by self-insured Sub-S Corp for an employee	No	No	No	No	No	No	No	No
Benefits paid by self-insured Sub-S Corp for an owner, key employee, or highly-paid employee	Yes	Yes	Yes	Yes	Yes	No	No	No
Employee share of premiums paid toward employer plan. (If eligible, can use Section 125 to avoid all federal taxes.)	Yes	Yes	Yes	Yes	No	Yes	Yes	Yes
Employee share of benefit costs paid through self-insured employer. (If eligible, can use Section 125 to avoid all federal taxes.)	Yes	Yes	Yes	Yes	No	No	No	No



# HSA

Benefits Consulting

## Written Testimony to the Committee on Taxation

Date: March 5, 2010  
From: Beverly Gossage  
To: Mr. Chairman and Members of the Committee

Subject: HB 2682

### Introduction:

My name is Beverly Gossage and I am the Director of HSA Benefits Consulting. I serve on the health board for Kansas Policy Institute and am a research fellow for Show Me Institute. I am here today to give testimony on how HB 2682 can give small business employers and their employees a tax savings and can help cover the uninsured.

### Purpose:

The purpose of this bill is to permit employers of small businesses to contribute to an employee's individually purchased policy and to equalize the tax treatment for Kansans who purchase private health insurance.

### Information:

This bill would permit small employers to contribute to employees' individually selected policies through a health reimbursement arrangement with a defined contribution without these private plans being considered a small group health insurance plan. Under current Kansas legislation if an employer gives premium assistance toward these individual policies, they would be subject to such rules as group mandates and guaranteed issue which would drastically raise the rates of the premiums and no longer make them portable. This bill permits the employer to offer premium assistance without changing the fact that the policy is a personal, individually underwritten portable policy.

According to a Kaiser Foundation Study, in 2008 only 41.3 percent of small businesses in Kansas with fewer than 50 employees offered group health insurance. Insurance carriers tell us that even more employers have dropped coverage in 2009. Those who have dropped group health plans cite various reasons:

- 1) *Lack of time and personnel*

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Particularly in this economy, small business owners do not have a fulltime HR department to oversee the health insurance benefits. The employer is busy trying to run the company, make a profit, and keep employees on the payroll.

2) *High cost of group premiums*

State and federal mandates, guaranteed issue, community rating and the demographics of the group can lead to high premiums. Due to the small pool, if one person develops a severe health issue, everyone can experience significant rate increases at renewal.

3) *Employee participation requirements*

To avoid adverse selection, most carriers mandate that at least 50% of the full time eligible employees and 75% of employees without other group coverage be on the plan. Often expensive premiums and other factors can make it difficult to meet those participation percentages.

4) *Employer contribution requirements*

Carriers require that the employer pay at least 50% of the employee premium. As rates accelerate, employers find that they can't keep increasing this portion of their employees' compensation, so they drop the plan and might increase salaries in an attempt to stay competitive and keep employees. But they and the employees receive no tax deduction on that portion of salary which the employee could apply to purchasing a policy.

5) *Retention*

1 in 4 employees change jobs annually and go in and out of employer group plans. This can make it especially difficult for a small business to keep up with the paperwork and budget for insurance costs. At each annual renewal they could have a very different employee pool which could drastically affect the premium. When you have a pool of 5 people and one person leaves, you have changed the underwriting by 20%.

6) *Portability*

Kansas requires that employees be offered state continuation when they leave the plan. In many cases, employers must do the paperwork to offer the employees this option and monitor if the terminated employee has paid the full premium and is still on the plan. They must keep up with the ever changing subsidy renewals and legislation. Even then, group plans are only portable for a time until the employee has exhausted the continuation period.

In 2007 over 175,000 Kansans were covered by a private policy. The fact that most small business employers are not offering health insurance and the fact that we live in a mobile and global society has contributed to the growing number of Kansans who own an individual policy. Some businesses in Kansas hire employees who work remotely from other areas around the state. Finding a small group policy with a broad network to cover these employees can be daunting. This growing population with private policies is apparent in the number of group insurance carriers who have entered the individual marketplace in the past three years and now advertise these private policies on billboards, radio and television.

Yet, about 30 percent of workers in firms with fewer than 25 employees are still uninsured.

### **Expected outcome of HB 2682:**

- 1) More employers will *contribute to premium*.  
To stay competitive with employers that offer group health insurance, some employers who currently do not offer a group plan will be more likely to encourage employees to select a private health insurance policy to which they, the employer, can contribute and receive a tax deduction.
- 2) More employees will *become insured*.  
Employees will be more likely to purchase a policy if the employer contributes to the premium and they can receive a tax deduction on their premium.
- 3) Employees will have *more coverage options*.  
When a small business owner formerly offered a group plan, he most likely offered a single option. This bill gives employees more choices and they can act as a consumer, selecting the best policy for their needs.
- 4) Employees will select policies with *lower premiums*.  
When given free choice, many employees choose HSA qualified plans because the premiums are usually 35 percent to 40 percent lower than traditional plans and their out-of-pocket is capped. Employers and employees may contribute to the health savings account, providing tax free funds, (if contributions are made through a Cafeteria 125, the funds go in pretax) which grow with interest that the employee may accumulate to pay for future health care expenses and save for retirement if not used.
- 5) *No minimum number of participants* will be an incentive for employers to provide assistance.  
Employers not offering a group plan will offer premium assistance since they don't have to have a minimum number of employees participate.
- 6) *No minimum percentage of premium* will be an incentive for employers to provide assistance.  
Employers determine the amount that their budget can allow toward premium, as long as it is the same for employees in the same classification. For example, an employer may contribute \$100 toward premium for full time employees and perhaps he would want to put \$50 toward part time employees' health policies.
- 7) Though no group plan is available, employees will choose to be insured through private policies for their *portability* and to receive the employer's contribution toward premium. Employees will discover that their personal policy is portable and not the employer's plan. This ownership provides for more judicious utilization of the benefits and promotes wellness. No worries about losing a job meaning losing benefits.
- 8) Formerly uninsured employees will discover the *security* in owning a personal policy. If the employer drops his group plan, the employee with a private policy has the security of knowing that his policy is intact. For example: though it is not a group plan, his policy cannot be cancelled nor his rates increased due to his personal claims; his newborn babies can be added to his policy without going through underwriting within the first 31 days of

birth; and with many plans, his adult child could be transferred to an individual policy without going through underwriting, building a ladder of the insured.

- 9) Employers and employees will discover the *convenience* of personal policies. There is less hassle and an easier transition when a new employee is hired. He is not required to go through a waiting period to access health insurance or be made to complete a health carrier's application to be added to the company policy. Most carriers offer a list bill in which an employer may provide the convenience of payroll deduction and send one check to the carrier monthly for the employees who have selected policies from that carrier. When the employee leaves, he merely calls the carrier and starts paying his premium directly to the carrier.
  
- 10) Employers and employees will begin to see a *tax savings*. Through a premium-only cafeteria plan, the employees who have purchased individual health insurance will have a tax advantage on their portion of the premium, equalizing the tax discrimination. In addition, the employer will have a tax advantage by reimbursing his portion of the premium through the health reimbursement arrangement. This will give an incentive for the employer and employee to contribute to health insurance, covering more uninsured.
  
- 11) Some employees will choose a personal policy because they can receive a state tax deduction. Those employees whose employer chooses not to pay toward their premium or offer a Cafeteria 125, will still receive a state tax deduction on the premium of their personal policy through this bill.

As the popularity of individual plans has increased, the injustice of the tax system has become more pronounced. Federal legislation has been proposed to equalize the tax advantages given to those who purchase insurance through their employer's group plan, by eliminating both federal income taxes and employment taxes for individually purchased health insurance, thus allowing a reduction for health premiums in the federal Adjusted Gross Income. We are pleased that Kansas is not waiting for the federal government to establish a tax equalization proposal.

I have included a revision to the bill that consolidates new Sec 1 and new Sec 2, thus eliminating repetition and standardizing the provisions for small business employers. The revision also replaces the bill's definition of health reimbursement arrangement with the federal definition. We struck Sec. 3 and 4 because they mandate carriers to offer high deductible health plans, but the market dictates the options that the public want; therefore, carriers already offer them.

### **Conclusion**

Turning uninsured employees into insured consumers benefits all of Kansas. I urge you to support HB2682 because it is a common sense step toward equalizing the tax treatment of personal policies and will offer small businesses an option to provide premium assistance to their employees.

Attached please find:

-Documentation from the Kaiser Foundation

-Clarification from the Department of Treasury regarding employers paying toward individual health policies

-Op-ed from the Council for Affordable Health Insurance (CAHI)

-revised version of the bill (balloon version and easy to read version)

I will gladly respond to your questions.

**Kansas: Percent of Private Sector Establishments That Offer Health Insurance to Employees, by Firm Size, 2008**

Compare Kansas to:  United States

Percent of Private Sector Establishments That Offer Health Insurance to Employees, by Firm Size, 2008

Compare 

	KS %	US %
Firms with Fewer than 50 Employees	41.3%	43.2%
Firms with 50 Employees or More	96.8%	96.5%

[\(show/hide notes\)](#)

**Kansas: Health Insurance Coverage of Nonelderly 0-64, states (2007-2008), U.S. (2008)**

Compare Kansas to:  United States

Health Insurance Coverage of Nonelderly 0-64, states (2007-2008), U.S. (2008)

Compare 

	KS #	KS %	US #	US %
Employer	1,500,000	63.0%	156,860,100	59.7%
Individual	175,100	7.4%	13,823,100	5.3%
Medicaid	292,800	12.3%	39,256,200	14.9%
Other Public	78,500	3.3%	7,123,600	2.7%
Uninsured	334,800	14.1%	45,693,300	17.4%
Total	2,381,200	100.0%	262,756,400	100.0%

[\(show/hide notes\)](#)

August 10, 2007

## IRS Clarifies Use of Cafeteria Plans

The U.S. Treasury Department has just released a regulation that reiterates and clarifies certain tax provisions with regard to individually purchased health insurance, ensuring that many employees with access to an employer-provided cafeteria plan who buy their own health insurance can get a tax break, as do those who have employer-provided coverage.

"This is an important clarification," said Dr. Merrill Matthews, Executive Director of the Council for Affordable Health Insurance (CAHI), "because it helps to level the playing field on the tax treatment of health insurance."

The IRS regulations clarify that employees can pay their individual health insurance and life insurance premiums through a tax-favored cafeteria plan. Employees in an employer-provided group health insurance plan have always been able to do that. But some had questioned whether individuals working for an employer who did not provide health insurance could do the same thing. This isn't a new tax provision; the regulation simply provides clear guidance that employees are allowed to have their premiums payroll deducted from their paychecks. They can either be reimbursed directly or paid through a "list billing" arrangement, in which the employees buy individual health insurance policies using a payroll deduction plan.

"We have been calling on the IRS to make this clarification; it could be a big boost for the uninsured who work for small employers," said J.P. Wieske, CAHI's Director of State Affairs. "Employers who don't provide health insurance can still help their employees get coverage through a list bill arrangement. And now we know those employees can pay for their premiums tax free."

One of the reasons for the Connector, part of the new Massachusetts health insurance reform legislation, was to help employees buying individual health insurance get a tax break for that coverage through a cafeteria plan. This IRS clarification essentially eliminates the need for a Connector to achieve tax fairness.

For more information on list billing see CAHI's [One Solution for the Small Group Market](#). To see the August 6, 2007, *Federal Register* document outlining the clarification, see [Employee Benefits -- Cafeteria Plan; Proposed Rule](#)

1961-2 C.B. 25; 1961 IRB LEXIS 8, \*;  
REV. RUL. 61-146

Rev. Rul. 61-146

## SECTION 106. - CONTRIBUTIONS BY EMPLOYER TO ACCIDENT AND HEALTH PLANS

26 CFR 1.106-1: Contributions by employer to accident and health plans.

(Also Section 61; 1.61-1.)

*1961-2 C.B. 25; 1961 IRB LEXIS 8; REV. RUL. 61-146*

July, 1961

[\*1]

Reimbursements by an employer to his employees for his share of premiums for hospital and medical insurance for them may be considered as contributions by the employer to accident or health plans for his employees so as to result in the exclusion of such payments from the gross income of the employees under section 106 of the Internal Revenue Code of 1954.

Revenue Ruling 57-33, C.B. 1957-1, 303, distinguished.

Advice has been requested whether amounts paid by an employer, under the circumstances below, as his share of premiums for hospital and medical insurance for his employees are excludable from the gross income of the employees under *section 106 of the Internal Revenue Code of 1954*.

In the instant case, the employer pays a share of the premiums for hospital and medical insurance for his employees. For those employees who are covered by a group policy through their employment, the employer pays his share of the premium directly to the insurance company. For those employees who are not covered by the employer's group policy but have other types of hospital and medical insurance for which they pay the premiums directly to the insurers, the employer pays a part of such premiums [\*2] upon proof that the insurance is in force and is being paid for by the employees.

To facilitate payment of his share of the premiums paid directly by the employees to the insurers, the employer uses the following methods: (1) reimburses each employee directly once or twice a year for the employer's share of the insurance premiums upon proof of prior payment of the premiums by the employee; (2) issues to each employee a check payable to the particular employee's insurance company, the employee being obligated to turn over the check to the insurance company; or (3) issues a check as in method (2) except the check is made payable jointly to the insurance company and the employee.

Section 106 of the Code provides that gross income does not include 26 contributions by the employer to accident or health plans for compensation (through insurance or otherwise) to his employees for personal injuries or sickness.

*Section 1.106-1 of the Income Tax Regulations* provides that the employer may contribute to an accident or health plan either by paying the premium (or a portion of the premium) on a policy of accident or health insurance covering one or more of his employees, or by contributing [\*3] to a separate trust or fund, which provides accident or health benefits directly or through insurance to one or more of his employees.

In this case it is clear that in method (2) the employer is actually paying accident or health insurance premiums directly to the insurer of the particular employee, utilizing the employee as his agent for the delivery of the checks to the insurer. Method (3) is not substantially different, inasmuch as the employee there is obligated to turn the checks over to the insurer and can in no event divert the payments to other uses. Although method (1) involves direct payment to the employee, in practical effect it does not differ from methods (2) or (3), since proof is required by the employer that hospital and medical insurance is in force for the employee and that premiums for the period involved have been paid by the employee and because the employer's payment is stated to be in reimbursement for the employer's share of the insurance premiums.



1961-2 C.B. 25; 1961 IRB LEXIS 8, \*;  
REV. RUL. 61-146

Under the circumstances of this case, it is held that the amounts paid by the employer under methods (2) or (3) above constitute payments of premium or portions of premiums on policies of accident or health [\*4] insurance covering one or more employees within the meaning of section 1.106-1 of the regulations. Similarly, the payments under method (1) constitute employer payments of accident or health insurance premiums for employees if the payments are shown to be in reimbursement of premiums actually paid by the employees to the insurers. Accordingly, amounts paid as above are excludable from the gross income of the employees under section 106 of the Code.

Revenue Ruling 57-33, C.B. 1957-1, 303, holds that certain weekly payments made by employers direct to employees, pursuant to a union contract of employment, for the purpose of purchasing individual hospitalization and surgical insurance coverage, are "wages" for Federal employment tax purposes and are includible in the gross income of the employees.

Under the facts in that case, the employers had no accident or health plan of their own in effect and, with respect to the payments which they made direct to the employees, did not require an accounting either by the employees or the employees' union that the funds were expended in the acquisition of insurance coverage. *Revenue Ruling 57-33*, accordingly, is distinguishable from the instant [\*5] case. 27

HOUSE BILL No. 2682

By Committee on Taxation

9 AN ACT concerning insurance; relating to health insurance and taxation;
10 amending K.S.A. 2009 Supp. 40-2240 and 79-32,117 and repealing the
11 existing sections.

12
13 Be it enacted by the Legislature of the State of Kansas:

14 New Section 1. (a) A small employer who does not offer a group
15 health insurance plan may, through the establishment of a health reim-
16 bursement arrangement, contribute to the premium of an eligible em-
17 ployee's individually underwritten health benefit plan. The employee's
18 portion of the premium may be paid through a cafeteria plan as permitted
19 under 26 U.S.C. Section 125. The provisions of K.S.A. 40-2209b through
20 40-2209o, and amendments thereto, shall not apply to an employee who
21 retains such individually underwritten health insurance plan.

22 (b) As used in this section, "individualized health reimbursement ar-
23 rangement" means an arrangement by which a small employer contrib-
24 utes to the premium of an eligible employee's individually underwritten
25 health insurance plan.

26 New Sec. 2. An eligible employee may choose to retain their indi-
27 vidualy underwritten health insurance plan at the time such eligible em-
28 ployee is entitled to enroll in a small employer health benefit plan. If the
29 eligible employee retains their individually underwritten health insurance
30 plan, a small employer who offers a group health benefit plan may,
31 through the establishment of a health reimbursement arrangement, con-
32 tribute to the premium of an eligible employee's individually underwrit-
33 ten health insurance plan. The employer shall pay to the employee the
34 same amount the employer would have contributed to such employer's
35 health benefit plan had the employee elected to participate in the small
36 employer health benefit plan. The employee's portion of the premium
37 may be paid through a cafeteria plan as permitted under 26 U.S.C. Sec-
38 tion 125. The provisions of K.S.A. 40-2209b through 40-2209o, and
39 amendments thereto, shall not apply to an employee who retains such
40 individually underwritten health insurance plan.

41 New Sec. 3. (a) Beginning with the open enrollment period for the
42 2010 plan year, the administering carrier shall offer to all eligible em-
43 ployees the option of receiving health care coverage through a high de-

If a

contributes

insurance policy,
whether or not

policy. The amount
the employer pays
toward the premium
must be the same
percentage of
premium or up to
the same dollar
amount toward the
premium that the
employer pays
toward the health
insurance premium
of the other
employees of the
same classification.
An eligible
employee may
choose to retain an
individually
underwritten health
insurance policy at
the time such
eligible employees
are entitled to enroll
in a small employer
health benefit plan.

is
125, the
the employee's

an employer-
funded, tax
sheltered account
to reimburse
allowable medical
expenses, including
insurance
premiums.

1 ductible health plan and the establishment of a health savings account.  
2 Such option may be offered through a cafeteria plan permitted under 26  
3 U.S.C. Section 125.

4 (b) The administering carrier shall issue a request for proposals from  
5 companies interested in offering a high deductible health plan in con-  
6 nection with a health savings account.

7 (c) As used in this section, "carrier" means any insurance company,  
8 nonprofit medical and hospital service corporation, nonprofit optometric,  
9 dental and pharmacy service corporations, municipal group-funded pool,  
10 fraternal benefit society or health maintenance organization, as these  
11 terms are defined by the Kansas Statutes Annotated, and amendments  
12 thereto, that offers health benefit plans covering eligible employees of  
13 one or more small employers in this state.

14 ~~New Sec. 4. Any insurer who offers small group health benefit plans  
15 shall offer a high deductible health plan in conjunction with the estab-  
16 lishment of a health savings account.~~

17 Sec. 5. K.S.A. 2009 Supp. 40-2240 is hereby amended to read as  
18 follows: 40-2240. (a) Any small employer as defined in subsection (4) of  
19 K.S.A. 40-2209d, and amendments thereto, may establish a small em-  
20 ployer health benefit plan for the purpose of providing a health benefit  
21 plan as described in subsection (u) of K.S.A. 40-2209d, and amendments  
22 thereto, covering such employers' eligible employees and such employ-  
23 ees' family members. If an association or trust is used for such purposes,  
24 the association or trust may not condition eligibility or membership on  
25 the health status of members or employees.

26 (b) The commissioner shall provide assistance to employers desiring  
27 to organize and maintain any such benefit plan and may aid in the ac-  
28 quisition of the health care insurance by the small employer health benefit  
29 plan.

30 (c) *Any health benefit plan may:*

31 (1) *Be offered through a cafeteria plan authorized by 26 U.S.C. Sec-*  
32 *tion 125.*

33 (2) *Offer to all eligible individuals the option of receiving health care*  
34 *coverage through a high deductible plan and the establishment of a health*  
35 *savings account.*

36 (d) *For the purposes of this section, the term:*

37 (1) *"Health savings account" shall have the meaning ascribed to it in*  
38 *subsection (d) of 26 U.S.C. Section 223.*

39 (2) *"High deductible health plan" shall mean a policy or contract of*  
40 *health insurance or health care plan that meets the criteria established in*  
41 *subsection (c) of 26 U.S.C. Section 223 and any regulations promulgated*  
42 *thereunder.*

43 Sec. 6. K.S.A. 2009 Supp. 79-32,117 is hereby amended to read as

1 pursuant to K.S.A. 48-282, and amendments thereto, or pursuant to sec-  
2 tion 1 or section 2 of chapter 207 of the 2005 session laws of Kansas, and  
3 amendments thereto, to the extent that such death benefits are included  
4 in federal adjusted gross income of the taxpayer.

5 (xix) For the taxable year beginning after December 31, 2006,  
6 amounts received as benefits under the federal social security act which  
7 are included in federal adjusted gross income of a taxpayer with federal  
8 adjusted gross income of \$50,000 or less, whether such taxpayer's filing  
9 status is single, head of household, married filing separate or married  
10 filing jointly; and for all taxable years beginning after December 31, 2007,  
11 amounts received as benefits under the federal social security act which  
12 are included in federal adjusted gross income of a taxpayer with federal  
13 adjusted gross income of \$75,000 or less, whether such taxpayer's filing  
14 status is single, head of household, married filing separate or married  
15 filing jointly.

16 (xx) Amounts received by retired employees of Washburn university  
17 as retirement and pension benefits under the university's retirement plan.

18 (xxi) *For all taxable years beginning after December 31, 2009,*  
19 *amounts paid for health insurance premiums for any individual insurance*  
20 *policy primarily providing health care coverage for the taxpayer, the tax-*  
21 *payer's spouse or the taxpayer's dependents.*

individually  
underwritten,  
privately purchased  
health

22 (d) There shall be added to or subtracted from federal adjusted gross  
23 income the taxpayer's share, as beneficiary of an estate or trust, of the  
24 Kansas fiduciary adjustment determined under K.S.A. 79-32,135, and  
25 amendments thereto.

26 (e) The amount of modifications required to be made under this sec-  
27 tion by a partner which relates to items of income, gain, loss, deduction  
28 or credit of a partnership shall be determined under K.S.A. 79-32,131,  
29 and amendments thereto, to the extent that such items affect federal  
30 adjusted gross income of the partner.

31 Sec. 7. K.S.A. 2009 Supp. 40-2240 and 79-32,117 are hereby  
32 repealed.

33 Sec. 8. This act shall take effect and be in force from and after its  
34 publication in the statute book.

AN ACT concerning insurance; relating to health insurance and taxation; amending K.S.A. 2009 Supp. 40-2240 and 79-32,117 and repealing the existing sections.

*Be it enacted by the Legislature of the State of Kansas:*

New Section 1. (a) ~~If a small employer who does not offer a group health insurance plan may, through the establishment of a health reimbursement arrangement, contribute to the premium of an employee's individually underwritten health insurance benefit plan policy, whether or not the employee's portion of the premium may be is paid through a cafeteria plan as permitted under 26 U.S.C. Section 125, the provisions of K.S.A. 40-2209b through 40-2209o, and amendments thereto, shall not apply to an employee who retains such the employee's individually underwritten health insurance plan policy. The amount the employer pays toward premium must be the same percentage of premium or up to the same dollar amount toward premium that the employer pays toward the health insurance premium of the other employees of the same classification. An eligible employee may choose to retain an individually underwritten, health insurance policy at the time such eligible employees are entitled to enroll in a small employer health benefit plan.~~

(b) As used in this section, "~~individualized health reimbursement arrangement (HRA)~~" means an arrangement by which a small employer contributes to the premium of an eligible employee's individually underwritten health insurance plan. employer-funded, tax-sheltered account to reimburse allowable medical expenses, including health insurance premiums.

New Sec. 2. (incorporated into New Sec. 1) ~~An eligible employee may choose to retain their individually underwritten health insurance plan at the time such eligible employee is entitled to enroll in a small employer health benefit plan. If the eligible employee retains their individually underwritten health insurance plan, a small employer who offers a group health benefit plan may, through the establishment of a health reimbursement arrangement, contribute to the premium of an eligible employee's individually underwritten health insurance plan. The employer shall pay to the employee the same amount the employer would have contributed to such employer's health benefit plan had the employee elected to participate in the small employer health benefit plan. The employee's portion of the premium may be paid through a cafeteria plan as permitted under 26 U.S.C. Section 125. The provisions of K.S.A. 40-2209b through 40-2209o, and amendments thereto, shall not apply to an employee who retains such individually underwritten health insurance plan.~~

AN ACT concerning insurance; relating to health insurance and taxation; amending K.S.A. 2009 Supp. 40-2240 and 79-32,117 and repealing the existing sections.

*Be it enacted by the Legislature of the State of Kansas:*

New Section 1. (a) If a small employer, through the establishment of a health reimbursement arrangement, contributes to the premium of an employee's individually underwritten health insurance policy, whether or not the employee's portion of the premium is paid through a cafeteria plan as permitted 26 U.S.C. Section 125, the provisions of K.S.A. 40-2209b through 40-2209o, and amendments thereto, shall not apply to the employee's individually underwritten health insurance policy. The amount the employer pays toward premium must be the same percentage of premium or up to the same dollar amount toward premium that the employer pays toward the health insurance premium of the other employees of the same classification. An eligible employee may choose to retain an individually underwritten, health insurance policy at the time such eligible employees are entitled to enroll in a small employer health benefit plan.

(b) As used in this section, "health reimbursement arrangement (HRA)" means an employer-funded, tax-sheltered account to reimburse allowable medical expenses, including health insurance premiums.



The Voice of Small Business®

**House Taxation Committee**  
**Daniel S. Murray: State Director, NFIB-Kansas**  
**Testimony in Support of HB 2682**  
**March 5, 2010**

Mr. Chair, Members of the Committee: My name is Dan Murray and I am the State Director of the National Federation of Independent Business-Kansas. NFIB-KS is the leading small business association representing small and independent businesses. A nonprofit, nonpartisan organization founded in 1943, NFIB-KS represents the consensus views of its 4,000 members in Kansas. Thank you for the opportunity to comment on HB 2682.

Since 1986, the National Federation of Independent Business' members have said that healthcare costs are their No.1 concern. In a recent NFIB poll, nearly 81 percent of small business owners say that finding affordable healthcare for themselves and their employees is a challenge. Fifty percent of small business owners say they anticipate having difficulty keeping up with the cost of healthcare over the next four years. And, of the nearly 46 million Americans without healthcare, more than 26 million are small business owners, employees and their dependents.

Further, small businesses do not have the purchasing power and large pools to spread experience that big business does. In fact, small businesses, on average, pay about 18 percent more for health insurance than their larger counterparts for the same group of services. Such data suggests that small employers either pay more for the same services or receive less (in terms of services) for their health insurance. In either case, the point remains that health insurance is more expensive for small businesses.

Thus, with the rising cost of providing healthcare benefits, an increasing number of employers are looking for innovative ways to stretch their healthcare dollars. Additionally, many small businesses which do not currently offer health insurance benefits are looking for ways to actually provide insurance to their employees. As you know, health benefits are key tool to recruit and retain qualified employees. Many employers look to market-driven reforms aimed at empowering individuals and employees to become better consumers by giving them the freedom to choose how they are spending their healthcare dollars, including: health savings accounts (HSAs), health reimbursement arrangements (HRAs) and flexible spending accounts.

Very simply, HB 2682 allows small business employers which have HRAs to be able to contribute to the insurance premiums of their employees' individually underwritten health plans. The amount the employer contributes to the employees' individually underwritten health plan must be the same percentage of premium, or up to the same dollar amount, that the employer pays toward the health insurance premium of the other employees of the same classification. This arrangement will allow employees to maintain their individually underwritten plans if they prefer, and should benefit small employers because the contributions would be made to tax-sheltered HRAs.

In closing, we believe HB 2682 will help slow the rising cost of insurance and reduce the number of uninsured Kansans by allowing small businesses and their employees more choice in the current small-group market. NFIB asks that you support HB2682. Thank you for your time and consideration.

House Taxation

Date: 3-5-10

Attachment: 6

**Written Testimony in Support of HB2682**  
**By Sandy Braden, Gaches, Braden and Associates on behalf**  
**Of the Kansas Association of Health Underwriters**  
**House Taxation Committee**  
**Friday, March 5, 2010**

Thank you for the opportunity to provide written testimony in support of HB2682.

The Kansas Association of Health Underwriters supports any efforts of the Kansas legislature to improve the affordability of health insurance premiums for small businesses. HB2682 would accomplish this by providing the following:

- Allows an employer to contribute to an employee's individually owned health plan on a tax-deductible basis through an established cafeteria plan;
- Provide an option of a high benefit plan in conjunction with the establishment of a health savings plan.

Allowing an employer to contribute to an employee's purchase of his or her own individual insurance policy would be an incentive for the individual to purchase insurance and maintain the insurance they have, thus decreasing the number of uninsured. It will also improve the portability of insurance.

Additionally, HB2682 encourages the use of Health Savings Accounts. Use of the Health Savings Accounts will reduce the cost of health insurance for both employees and employers.

And one of the most effective ways to lower the cost of insurance for those with modest incomes is to provide individuals and families with a tax credit for the purchase of health insurance. The cost of the tax credit in this case would be offset in the long run through the savings in increases in health care costs.

The Kansas Association of Health Underwriters encourages the House Taxation Committee to support a health care reform program such as HB2682 that encourages competition and reduces the cost of private health insurance for all Kansans. This will assist the small group market needs added flexibility and incentives to better serve uninsured Kansans.

Sandy Braden  
Gaches, Braden and Associates  
825 S Kansas Suite 500  
Topeka, Kansas 66612  
785-233-4512

**House Taxation**  
**Date:** 3-5-10  
**Attachment:** 7



**Wichita Independent Business Association**

*THE VOICE OF INDEPENDENT BUSINESS*

**House Committee on Taxation  
Testimony in Support of HB 2682  
By: F. Tim Witsman**

**March 5, 2010**

Chairman Carlson and honorable committee members:

My name is Tim Witsman, and I am the President of the Wichita Independent Business Association (WIBA). As a representative of organizations charged with the mission to promote a strong business environment in Kansas, I am here as the voice for more than 1,000 business members from across the state of Kansas and can assure the rising cost of health care insurance is the top concern for our members. Thank you for the opportunity to submit written testimony in favor of HB 2682, which provides for small employers the option of contributing to the cost of an employee's individual policy through a Health Reimbursement Account (HRA).

The members of WIBA support HB 2682 because it proposes a tool that may be used by employers to assist their employees in obtaining health care insurance. HRA's, under current law, are attractive to employees because they deposit pre-tax dollars and use those dollars to pay for health care expenses. Under existing law, employers are denied the option of contributing dollars to employees HRA's that can be used to pay for individual policies. HB 2682 would remove this restriction and allow employers to deposit dollars into an employee's HRA account, affording the employee the benefit of leveraging both contributions towards the premium of an individual health care policy. HB 2682 will give employers and employees an additional choice, which we believe is what is needed in the health care arena. It also fosters additional individual choice and control over one's health care insurance, which we believe is a necessity in ultimately reducing health care costs.

There is concern that passage of this bill might circumvent the small group market and we would offer that this is a legitimate concern. However, we also recognize that if we are going to reduce the cost of health care, we need to be willing to try new approaches.

WIBA is committed to working with Kansas legislators to find market driven solutions that assist employers with providing health care to their employees and urge your support of HB 2682. We look forward to working with lawmakers in developing the best possible options and outcomes for all Kansans. Thank you for the opportunity to share our position with you.