

SUMMARY ANALYSIS OF AMENDED BILL

Author: Nunez/Perata Analyst: Anne Mazur Bill Number: ABX1 1
 Related Bills: See Prior Analysis Telephone: 845-5404 Amended Date: January 16, 2008
 Attorney: Patrick Kusiak Sponsor: _____

SUBJECT: Enforcement of Individual Health Care Mandate/Health Care Premium Refundable Credit/ Require Employers To Establish Section 125, Cafeteria Plans

- DEPARTMENT AMENDMENTS ACCEPTED. Amendments reflect suggestions of previous analysis of bill as introduced/amended _____.
- AMENDMENTS IMPACT REVENUE. A new revenue estimate is provided.
- AMENDMENTS DID NOT RESOLVE THE DEPARTMENTS CONCERNS stated in the previous analysis of bill as amended December 17, 2007.
- FURTHER AMENDMENTS NECESSARY.
- DEPARTMENT POSITION CHANGED TO _____.
- REMAINDER OF PREVIOUS ANALYSIS OF BILL AS AMENDED December 17, 2007 STILL APPLIES.
- OTHER – See comments below.

SUMMARY

This bill, which would be known as the Health Care Security and Cost Reduction Act, would do the following:

- Beginning July 1, 2010, require each California resident to be enrolled in and maintain at least the minimum health care coverage (individual mandate).
- Permit the Managed Risk Medical Insurance Board (MRMIB) to enter into an agreement with the Franchise Tax Board (FTB) to recoup any state funds advanced for health care coverage on behalf of noncompliant individuals.
- For taxable years 2010 through 2014, establish a refundable income tax credit based on the amount of health care premiums paid for individuals of a specified income class and state the intent of the Legislature to allow this credit to be advanceable.
- In addition, state the intent of the Legislature to enact a health care coverage income tax credit not to exceed \$50 million dollars annually, subject to an appropriation for certain individuals of a specified age.
- Beginning January 1, 2010, require certain employers to set up a cafeteria plan under Internal Revenue Code (IRC) section 125 (125 plan mandate).

Board Position:	Legislative Director	Date
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This bill would make other changes to several California Codes related to the health care program, including establishing the California Health Trust Fund to provide health care coverage and pay program expenses. Discussion in this analysis is limited to those provisions of the bill that affect the FTB.

SUMMARY OF AMENDMENTS

The January 16, 2008, amendments made the following changes to the health care premium credit:

- Expanded the definition of the term “premium for a plan from coverage choice category 3” to require that such a plan provide benefits including “prescription drugs, physician visits, and preventive services, including the services to manage chronic conditions, outside of any deductible.”
- Modified the definition of “qualified taxpayer” to indicate that an individual “enrolled in or eligible for health expenditures that may be credited against any required employer health care contribution” is not a qualified taxpayer.
- Revised language to indicate that “appropriate amounts” rather than “all amounts” in the California Health Trust Fund (Fund) to be transferred to FTB or MRMIB to recover funds expended to allow the credit as a credit against tax or refund or credit advance, if authorized.
- Made other substantive changes and nonsubstantive technical changes to health care-related provisions that would not impact the department.

A revised Implementation Considerations section is provided to reflect the amendments. The concern identified as #11 in the department's analysis of the bill as amended December 17, 2007, relating to transfers from the Fund, has been resolved. A new concern identified as #12 in this analysis is added relating to the definition of qualified taxpayer. The remainder of the analysis of the bill as amended December 17, 2007, continues to apply.

POSITION

Pending.

REFUNDABLE INCOME TAX CREDIT

ANALYSIS

IMPLEMENTATION CONSIDERATIONS

Department staff has identified the following implementation concerns. Department staff is available to work with the author's office to resolve these and other concerns that may be identified.

1. The bill would allow FTB to be reimbursed from the Health Care Trust Fund or General Fund for the aggregate amount of premium credits allowed only if appropriated. It appears that the bill intends that no premium credits be allowed unless an amount has first been appropriated for such credits. If there is no appropriation by the Legislature or in the annual Budget Act for the fiscal year in which the credit would be granted, FTB could not allow credits claimed. Lack of appropriation could result in a delay in processing all returns that claim the credit. Such delays may require payment of interest on any refunds due. It is also unclear how the credit would be administered if credits claimed exceeded the appropriated amount.
2. It is unclear whether departmental processes and systems would be subject to federal Health Insurance Portability and Accountability Act (HIPAA) requirements as a result of receipt of insurance premium data from MRMIB. An affirmative determination could significantly impact the department and, as noted below, substantially increase the department's costs to implement this proposal.
3. If it is intended that the credit be verified during initial personal income tax return processing, FTB would need premium data from MRMIB annually and as close to taxable year end as possible to minimize delay in issuing personal income tax refunds. In the alternative, returns claiming the credit prior to receiving data from MRMIB would be held, pending receipt of that information, until FTB has the historical experience to establish a reasonable threshold for allowing refunds during that period.
4. Refundable credits are susceptible to fraud. Resources would be necessary to detect and prevent fraud. Unlike the existing refundable child and dependent care credit, reliable third party information—from MRMIB—would presumably reduce fraud by increasing both detection and prevention. The risk of fraud would substantially increase if MRMIB is unable to provide the data necessary to verify upon initial processing the credits claimed.
5. At least two new lines would need to be added to individual tax returns to allow taxpayers to claim the credit and report any advances received, if authorized. Instructions would be added and a schedule or worksheet would be created to compute the credit. The addition of two lines may result in a 3-page return, which would increase annual costs as discussed, below, under Fiscal Impact.

6. Consistent with the law as it applies for refundable credits, any corrections to the credit in processing would be treated as a math error adjustment¹ and billed to the taxpayer. Taxpayers wishing to dispute the adjustment would be required to pay the amount owing and file a claim for refund.
7. Unless it is modified, fewer taxpayers would be able to use the user-friendly Form 540 2EZ, California Resident Income Tax Return, because it does not require AGI or other information necessary to process the credit.
8. Individuals included on an income tax return may not match the individuals included in a family for health care coverage purposes. For example, a taxpayer may be required to purchase insurance pursuant to divorce agreement for a family member that is appropriately not included on his or her income tax return, such as a child reported as a dependent on another taxpayer's return. Because FTB would administer this credit based on the individuals included on the return, it is unclear how these issues would be reconciled.
9. The bill provides that only health care premiums purchased through MRMIB — presumably for enrollment in California Cooperative Health Insurance Purchasing Program (Cal-CHIPP) — would be treated as a qualified premium. However, the bill also requires, as an option in a list, an individual to be eligible for the credit in order to be eligible to enroll in Cal-CHIPP. This would result in a circular, thus unadministrable, requirement.
10. The bill would authorize MRMIB to provide a report to FTB with specified health care information for each individual that purchases a health care plan through MRMIB. However, it does not authorize such information to be provided with respect to the dependents of the taxpayer for which health care was also purchased. In addition, FTB would need the age of each subscriber in order to apply the credit maximums. Such information would be necessary for the administration of the credit.
11. The bill would permit a penalty on tax return preparers for failure to be diligent in determining eligibility for the credit. The bill authorizes FTB to modify a federal due diligence penalty as needed through instructions or notices. It is suggested that the bill be amended to provide an Administrative Procedures Act (APA) waiver to prevent a likely APA challenge on grounds that such modifications constitute an underground regulation.

¹ An adjustment to a tax return balance due that is treated as a math error adjustment pursuant to applicable statutes is due upon notice and demand. A taxpayer may protest or appeal such an adjustment only after the adjustment amount is paid, at which point the taxpayer may file a claim for refund.

12. The bill would provide that a taxpayer with an employer-subsidized health plan or that is “enrolled in or eligible for health expenditures that may be credited against any required employer health care contribution” is not a qualified taxpayer. It is unclear what constitutes “health expenditures” or how they would be “credited” against any required employer health care contribution. Apparently, these terms and how they would be applied in this context is described in another proposal. It is suggested that these terms be defined by reference to prevent confusion.

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