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Impact of the PPACA on Texas Business

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Key Points

- The health care law mandates employer-sponsored insurance coverage in an attempt to expand insurance coverage. However, its requirements will be a significant cost burden for Texas businesses.
- The Texas Comptroller's office estimates that from 2010 to 2019 Texas businesses will pay approximately $9.3 billion in penalties under the employer mandate.
- The health care law's small business tax credit is more likely to be an impediment to small business growth and hiring than a boon to employer-sponsored insurance.

Introduction

The Patient Protection and Affordable Care Act (PPACA) is an effort to mandate the purchase of comprehensive health insurance coverage for all Americans. In order to accomplish this goal, Congress enacted numerous requirements which will impose significant burdens on Texas business.[1]

Employer costs begin with the mandate, as defined by Sec. 1513 of PPACA, which requires employers to offer their employees a health insurance policy that meets the minimum essential health benefits established by the Secretary of Health and Human Services. If an employer does not offer such coverage, an annual maximum penalty of $2,000 for all employees after the first 30 employees is assessed.

Offering coverage, however, does not guarantee protection from the penalty. If the policy costs more than 8 percent of an employee's household income, and if the employee obtains insurance through a state exchange, the employer must still pay the penalty. If one or more employees qualify for and receive a subsidy in the state insurance exchange, then the employer is assessed the lesser of $2,000 for all employees beyond the first 30, or $3,000 for each employee that receives subsidies in the exchange.

Of course, the impact of this mandate is compounded by provisions in the health care law that will cause the cost of insurance to increase. With the average 2010 employer contribution to an individual health insurance policy at $4,508 and the average employer contribution to a family health insurance policy at $10,944,[2] the cost is already high enough. Faced with increasing costs, many employers may decide not to offer insurance, and opt to pay the fine.

The administrative burden associated with the employer mandate is also considerable. These costs will hit small businesses particularly hard as many do not have full-time human resources personnel to record, report, and ensure compliance with the mandate. The requirements include informing employees of the exchange, informing employees of their eligibility for tax credits contingent on the employer's plan options, evaluating employees' household income to ensure compliance, and reporting on compliance in offering health insurance. The smaller the business the greater is the burden of these administrative requirements.

These burdens are not, however, uniform for all businesses. The law differentiates between those businesses with fewer than 50 employees and those with more than 50 employees. The biggest difference between these two business sizes is that the employer mandate applies to the latter but not the former. This distinction creates a significant disincentive for growth for small businesses as they approach the 50 employee mark and consider the compliance costs that come with hiring the 51st employee.

The burdens of the health care law do not only fall on businesses. Employees of all business will be harmed as the increased marginal cost of hiring new employees will slow employment growth. Low-wage employees and employees of small business will likely be hit the hardest.

The health care law could shape the future of Texas economic development in such a way that only two types of businesses remain: those who stay small enough to be exempt and those large enough to afford it.

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The Employer Mandate

The employer mandate is one of the costly requirements in the health care law. Sec. 1513(a) of the health care law states:

> If any applicable large employer fails to offer to its full time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer sponsored plan … for any month, and at least one full-time employee under section 1411 of the [PPACA] as having enrolled for such month in a qualified health plan with respect to which an applicable premium tax credit or cost sharing reduction is allowed or paid with respect to the employee, then there is hereby imposed on the employer an assessable payment equal to the product of the applicable payment amount and the number of individuals employed by the employer as full-time employees during such month …The term 'applicable payment amount' means, with respect to any month, 1/12 of $2,000.[3]

Any business in Texas with more than 50 employees that does not offer the minimum essential coverage of health insurance is assessed a fine of $2,000 annually for each employee. It is important to note that Sec. 1513(c) (2) (D) exempts the first 30 employees for the penalty outlined in Sec. 1513(a). For example, if a Texas firm that has 100 employees under 400 percent of FPL does not offer coverage, the annual fee would be $2,000 per employee for 70 employees or $140,000 a year.

If a business *does* offer coverage they still have to comply with certain requirements. Sec. 1513(b) of the health care law states:

> If an applicable employer offers to its full-time employees (and their dependents) the opportunity to enroll in minimum essential coverage under an eligible employer sponsored plan … for any month, and 1 or more full-time employees of the applicable large employer has been certified to the employer under section 1411 of the [PPACA] as having enrolled for such a month in a qualified health plan with respect to which an applicable premium tax credit or cost sharing reduction is allowed or paid with respect to the employee, then there is hereby imposed on the employer an assessable payment amount equal to the product of the number of full time employees of the applicable large employer described for such month and an amount equal to 1/12 of $3,000. …
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> The aggregate amount of tax determined … with respect to all employees of an applicable large employer for any month shall not exceed the product of the applicable payment amount and the number of individuals employed by the employer as full time employees during such a month.[4]

In short, any large employer who offers coverage and whose employees obtain coverage through the exchange and are eligible for subsidies is assessed a penalty of the lesser of $2,000 per employee after the first 30 annually or $3,000 for each employee who receives subsidies in the exchange. The tax credits and cost sharing reductions in the health care law insurance exchange are applicable to the majority of employees as eligibility goes as high as 400 percent of the Federal Poverty Limit (FPL) or $88,200 a year for a family of four. For example, if a Texas firm with 100 employees offered coverage and 40 employees who are eligible for subsidies receive coverage in the exchange, the company would be assessed a penalty of $120,000 (40 employees x $3,000). The company's maximum allowable penalty would $140,000 (70 employees x $2,000).

In 2008, Texas had 123,027 private-sector businesses with 50 or more employees, employing a total of more than 5.4 million full-time workers. Of these businesses, 91.6 percent offered health insurance to their employees.[5] The state Comptroller's office estimates that from 2010 to 2019 Texas businesses will pay approximately $9.3 billion in penalties.[6] These penalties will be paid by companies that do not offer coverage or do not offer compliant coverage.

A business is not assessed a penalty for an employee that is offered an employer-sponsored insurance policy that meets the minimum essential benefits coverage and does not exceed 9.5 percent of the employee's household income. However, the cost of health insurance is significant. The average cost of a health insurance policy has doubled over the last decade.[7] In 2010, the average employer contribution to an individual health insurance policy in Texas was $3,951, and the average employer contribution to a family health insurance policy was $10,026.[8]

Sidebar: The Impact on Conner Industries

Businesses across the state are feeling the impact of the health care law, and Conner Industries is one in particular. Conner Industries is an industrial lumber and package company headquartered in Fort Worth, TX. Conner Industries has 450 employees but is defined as a small business under Small Business Administration guidelines. Conner Industries has a workforce that is largely made up of young, hourly wage, unskilled workers, and the production model is very hard to automate leaving manual labor a necessity. This puts Conner Industries in a tough position when it comes to compliance with the health care law.

Currently, Conner Industries offers full insurance coverage to approximately 140 employees, and they struggle to get the 75 percent participation rate required by health underwriters. The company currently has a fully insured plan but as early as the 2012-13 plan year will be forced to drop coverage or seek an undesirable self-funded plan in order to comply with ObamaCare's discrimination requirements. In the 1990s, insurance was offered to all employees, but most production line workers opted out due to the high costs.

Under the health care law, the company is required to offer minimum essential coverage, as defined by the law, or pay a fine of $2,000 per employee after the first 30. This leaves Conner Industries with three options:

1. Expand full coverage to all employees at an additional cost of $1.75 million annually.
2. Pay only the difference between the total premium cost and 4 percent to 9.5 percent of the employee's household income. This would cost over $1,000,000 each year not including the administrative costs of reporting and calculating household income for all 450 employees. They anticipate that many employees will find this unacceptable. This exposes the company to a $3,000 non-tax deductible penalty for each employee who rejects coverage.
3. No longer offer any insurance and pay a non-tax deductible $2,000 fine on all employees. This option would be $1,000,000 in new costs and penalties to the company and much more once the tax effect is considered.

Under any of these options all capital devoted to growth and capital improvements would now be dedicated to health care. The effect of this reduction is startling. For the cost of paying the penalty for not offering coverage, Conner Industries could start two new plants with 70-80 employees each year. The magnitude of these costs would also put vital credit lines in jeopardy further endangering the business.

Beyond the hard costs is the negative impact on Conner Industries' competitiveness. Conner Industries operates 11 plants in 8 states. Each of these plants is under 50 employees and would individually be exempt from the employer mandate. Smaller companies that can meet this threshold currently represent 76 percent of Conner Industries competition. Being able to meet customer needs in multiple locations gives Conner Industries a competitive advantage over single mill operators that would be lost. The advantage these competitors would have from being exempt from the employer mandate would be unbeatable.

"It gets worse because the business community knows this law isn't paid for. Who is going to pay for it?" said CEO of Conner Industries Grady Payne. "Until we know how this will get paid for, no one is moving forward with investments or expansion."

"It isn't just the Federal government, either," noted Mr. Payne. "It's the state as well. We know that most states do not have the money for their Medicaid obligations. Where is all this money going to come from? Until we know, we simply cannot move forward."

Mr. Payne said, "We want to be able to offer our employees health insurance, but the way to do that is to make it more affordable—not mandate it. If the law stands as is, we are going to have to reevaluate how we do business from this point forward. We certainly will not be able to expand and grow as we had planned before."

Conner Industries is a prime example of the type of adverse impact the health care law will have on Texas businesses. In Texas, the health care law will cost jobs, reduce investment, and stunt growth.

Table 1: Employer Mandate Costs

Employee Household Income	Maximum Employee Share	Average Remaining Employer Share for an Individual Policy ($5,429)	Average Remaining Employer Share for a Family Policy ($15,079)
$20,000	$1,900	$3,529	$13,179*
$30,000	$2,850	$2,579	$12,229
$40,000	$3,800	$1,629	$11,279
$50,000	$4,750	$679	$10,329
$60,000	$5,700	$0	$9,379
$70,000	$6,650	$0	$8,429
$80,000	$7,600	$0	$7,479
$90,000	$8,550	$0	$6,529
$100,000	$9,500	$0	$5,579

**A family of 3 or more making $20,000 would be eligible for Medicaid.*
Source: Author's calculations based on Kaiser Family Foundation, "Texas: Average Single Premium per Enrolled Employee for Employer Based Health Insurance, 2010." Statehealthfacts.org (accessed Dec. 2011).

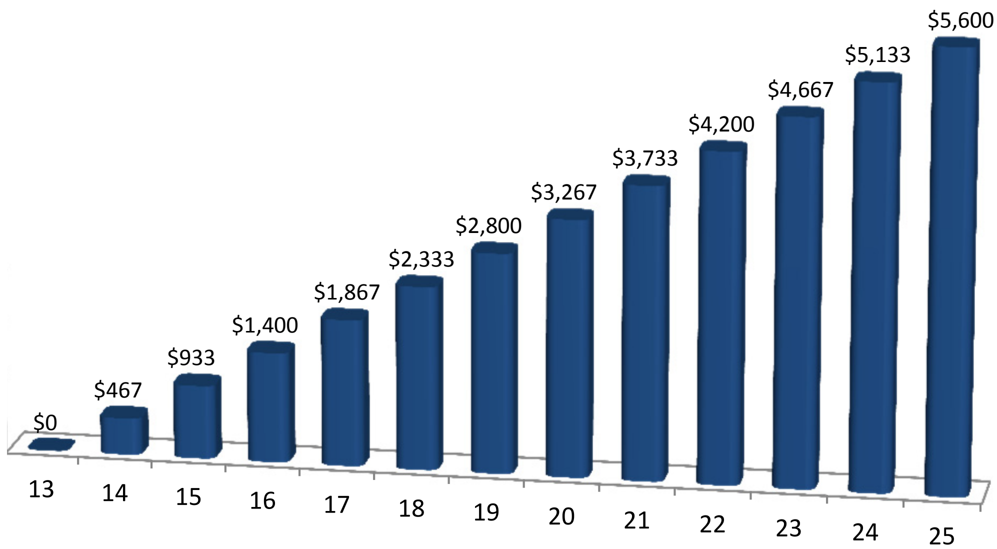
In 2010, if a Texas firm with 100 employees insured all of its employees with only individual policies it would cost $395,100 on average, far greater than the $140,000 maximum penalty. The cost of providing health insurance is high, and this makes the mandate expensive. The penalty is less expensive than the average cost of health insurance. This creates an incentive for companies to drop coverage and pay the penalty.

Furthermore, the cost of providing coverage is projected to increase. Per capita expenditures on health insurance are projected to increase from $8,327 in 2010 to $13,709 in 2020.[9] However, these estimates are conservative when estimating the compounding effect of the health insurance provisions in Title I of the health care law. One study estimates that community age-rating could raise costs on younger individuals by as much as 45 percent.[10] Because the penalties for not offering essential benefit coverage are linked to a percentage of income, businesses that employ low-wage workers will be hit the hardest. **Table 1** shows a breakdown of employer costs necessary for compliance based on income.

The high costs of the health care law do not only affect businesses. The additional costs for complying with the employer mandate also disproportionately affect low-wage workers. The impact of the marginal cost of providing health care coverage will be much greater when hiring low-wage workers, especially low-wage workers with families. As a result, there will be an incentive for employers to hire fewer low-wage workers, and when they do hire them, they will be more likely to hire unmarried workers with fewer dependents to keep their insurance costs lower.

Businesses with fewer than 50 employees are not subject to the employer mandate. Instead, small businesses with 25 employees or fewer are encouraged to provide coverage for their employees with a small business tax credit. From 2010 to 2014, the tax credit will be worth up to 35 percent of the employer's contribution to employee coverage. In 2014, employers will be eligible for a tax credit worth up to 50 percent of their contribution for two years. In order to qualify for the full tax credit in 2014, the employers must pay at least half of the cost of coverage, purchase insurance through a health benefits exchange, have no more than 10 employees, and have an average wage of $25,000. The amount of the tax credit is gradually reduced as the firm's average wage or workforce grows. This is a significant disincentive to hiring as each employee's marginal cost is increased by the reduction of the tax credit. **Figure 1** shows the marginal cost for a small business to hire employees.

Figure 1: Marginal Cost for Hiring Additional Workers



Source: National Center for Policy Analysis

The small business tax credit serves to shield small businesses from the true cost of health insurance under the health care law. This will reduce the benefits of a competitive marketplace, and weaken the price signals in the marketplace. Furthermore, the tax credit will do little to change behavior long term because the tax credit ends in 2017. This could create a disincentive to utilize the tax credit initially, or it could be an incentive to pick up insurance until 2017 and then drop it once the tax credit goes away.

An even greater impediment to growth and hiring for small businesses is the marginal cost of hiring the 50th employee and triggering the employee mandate. The minimum cost to a Texas business that did not previously offer coverage for hiring their 50th employee would be $40,000. For a low-wage worker making $20,000, this is a 200 percent marginal cost increase over the employee's base compensation for that one employee before considering new compliance costs. The marginal cost for small business is a disincentive to expansion over 50 employees.

Not all Texas businesses will be impacted by the employer mandate. If a firm offers health insurance that is compliant with the health care law little will change for them. Most large employers offer compliant coverage, and many medium size high-wage employers offer compliant coverage. The firms that will be impacted most will be small and medium size employers who do not offer coverage. Also, firms that employ low-wage workers will be impacted as it will be difficult to offer compliant coverage for less than 9.5 percent of a low-wage employee's household income.

Increasing health insurance costs combined with an individual mandate will squeeze Texas businesses increasingly over the next decade. In order to finance these new requirements businesses will have to go forego investment and growth and may be forced to close. The expanded coverage will come at the cost of business and job growth. An ineffective, complicated, short-term tax credit will further impede business growth. On top of the requirement to offer health insurance, businesses are faced with the administrative burden of doing so.

The Administrative Burden

Small businesses are not convinced that the health care law "will reduce paperwork and make the provision of health care less complex."[11] In fact, the law is more likely to add to the complexity of providing health care due to a number of administrative burdens. The administrative burdens include legal compliance, new reporting requirements for businesses to the IRS and their employees, regulatory compliance, and tax compliance.

Legal Compliance

The most basic burden of the health care law on business is the task of determining what they are legally obligated to comply with. The law is over 900 pages, and over 6,500 pages of regulations, notices, and corrections have been released since its passage, necessitating a comprehensive and costly legal analysis to ensure proper compliance.

Reporting Requirements

Under the health care law businesses are required to provide to their employees information on the existence of an insurance exchange and if their share of premiums is less than 60 percent of the total premium. A Free Choice Voucher may be offered to employees to purchase their own health care in the exchange, in lieu of a full coverage insurance plan. The employer must inform the employee of their Free Choice Voucher, if applicable, and if the employee purchases exchange insurance without a Free Choice Voucher he may lose his employer's contribution. Large employers must also provide to the IRS certification that they offered minimum essential coverage, the months it was available, the lowest cost plan available, and the identification of each employee that is enrolled in the plan. This is to be followed by a written statement to every employee that they have been identified in the certification reporting. These requirements may seem small but could amount to a noticeable reduction in time and resources devoted to doing business.

Household Income Verification

In order to be compliant in offering minimum essential coverage, employers must verify that the employee's share of the cost of insurance does not exceed 9.5 percent of his *household* income. This requires that an employer verify the worker's income along with the income of their spouse and any other outside income from investments unrelated to their work. The level of financial knowledge employers must gather from their employees is startling. Not only is this requirement overly burdensome to employers it also verges on an invasive violation of privacy for their employees.

Tax Compliance Burden

The health care law has 15 explicitly new or enhanced tax provisions in Title IX of the law. These penalties and tax provisions will be assessed through the IRS. In order to stay compliant with the IRS, businesses will be forced to coordinate with their insurance companies, their employees, the insurance exchange, the state government, and the federal government. This will require extensive accounting and reporting, and will necessitate human resources personnel with experience in employee wage and benefits accounting.

The Tax Burden

Medicare Tax

Under The health care law there is a 0.9 percent increase in the Medicare payroll tax assessed on couples making more than $250,000 each year. This raises the Medicare payroll tax from 2.9 percent to 3.8 percent for most self-employed couples. In 2007, sole proprietor firms numbered 38,083 in Texas. From 2010 to 2019, Texas citizens are expected to pay $13.2 billion in new taxes under the increased Medicare tax.[12] This reduces these individuals' ability to either expand their business or invest in others.

Health Savings Account (HSA) Tax

The health care law increases the taxes paid on non-medical purchases made from an HSA or Medical Savings Account (MSA). Previously the tax on these expenditures was 10 percent, but the health care law has raised this tax to 20 percent. The Comptroller's office estimates that this tax will cost Texans $113 million between 2010 and 2019. Again, this is $113 million no longer available for investment in the Texas economy.

Health Insurance Excise Tax

Beginning in 2014, the health insurance industry nationwide will be assessed a flat tax of $8 billion that increases annually to $14.3 billion in 2018. An insurance company's share of this tax will be based on their share of the insurance market. If the cost of this excise tax is passed on to consumers, it would adversely affect businesses providing this level of coverage through higher premiums.

Higher Premiums

Spending on private health insurance is expected to increase from 3 percent to 9 percent annually between now and 2020, according to the CMS actuary.[13] This increased spending on health insurance will be financed through premiums creating a larger burden on businesses providing insurance coverage. Health insurance costs are a primary concern to small business owners, and it will limit business owners' ability to attract talented employees and expand their business.

Sidebar: The Hispanic Entrepreneur

The recent census results showed a major increase in the Hispanic population in Texas. Hispanics accounted for 65 percent of our state's population growth since 2000.[14] This growth has not been limited to just population. Hispanic businesses have been increasing rapidly as well. Between 2002 and 2007 the number of Hispanic-owned firms increased from 319,340 to 447,486, a 40.1 percent increase.[15] In 2007, these Hispanic owned firms saw sales of $62.1 billion dollars.[16] Nationwide, Hispanic-owned firms are expected to increase revenue by 8 percent annually from 2005 to 2015.[17] There is no doubt that Hispanic business owners play a vital role in our state's economy.

Hispanic-owned firms are also overwhelmingly small businesses. In 2007, 97.5 percent of Hispanic-owned firms had fewer than 50 employees. These firms employed 60 percent of the employees of Hispanic-owned firms. By contrast, only 46 percent of employees in non-Hispanic-owned firms are employed by businesses with fewer than 50 employees. The growth in the Hispanic population and business ownership is not surprising because Hispanics have long been a larger portion of the Texas population than in other states.

However, their growth is outpacing other demographics. The state demographer projects that if migration rates hold their 2000-2007 rates, Hispanics will comprise a majority of the Texas population by 2015. If this population growth comes in tandem with economic growth as we have seen in the past, then Texas Hispanic business owners represent the future of the Texas economy. This makes repealing the health care law doubly important to the Hispanic entrepreneur. Because the employer mandate poses such a barrier to growth past 50 employees, Hispanic-owned firms are in greater danger than others by virtue of their current stage of development. The Hispanic-owned businesses are poised to lead the state's economic growth in the coming decades. However, because of their current size, the health care law threatens to bring this growth to a halt.

The impact of this tax will be felt especially by low-wage workers. This is of unique concern to Texas because the state has a high number of low and minimum wage workers. The health care law is more likely to cause them to *lose* their job than to gain coverage.

Conclusion

The Texas economy has been the most successful economy of all 50 states over the last decade. The state's low tax and low regulatory structure are a key driver of this economic success, but the health care law threatens the state's continued prosperity. The regulatory, tax, and administrative burdens posed by the health care law create a significant drag on business growth.

Much of this law is out of the state's legal authority, but Medicaid is not. Medicaid is unsustainable in the long term, and it needs reform. Texas has passed the Health Care Compact and multiple waiver requests seeking positive reforms. These policies have the possibility to afford Texas with great flexibility in administering our Medicaid program. However, until they are ratified or approved, they do not reduce the cost the state faces under the expanded Medicaid program in the health care law. The 2014-15 Medicaid budget will require an increase of almost 50 percent in General Revenue spending on Medicaid. The Legislature should reject any and all proposals to pay for this through higher taxes on our businesses.

Under the health care law, the employer mandate creates such a barrier at the 50 employee threshold that it is unlikely that most businesses will seek expansion to that size after 2014. The rising cost of business driven by compliance, employee coverage, and penalties will force medium size business to either merge with one another to gain economies of scale, sell their business to larger competitors, or shut down completely. The future of Texas business under the health care law is one in which small businesses stay small, large businesses stay large, and growth is muted. ✯

Endnotes

[1] Texas Comptroller of Public Accounts, *Diagnosis: Cost – An Initial Look at the Federal Health Care Legislation's Impact on Texas* (Combs, 2010).

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[3] Patient Protection and Affordable Care Act, Public Laws 111-148 & 111-152 (Consolidated), Sec. 1513 (a), (2010).

[4] Patient Protection and Affordable Care Act, Public Laws 111-148 & 111-152 (Consolidated), Sec. 1513 (b), (2010).

[5] Texas Comptroller of Public Accounts, *Diagnosis: Cost – An Initial Look at the Federal Health Care Legislation's Impact on Texas* (Combs, 2010).

[6] Ibid.

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