Design Considerations - Payroll Tax
For Discussion Only - Updated: 04/15/2008

Overall Value Proposition	Instituting a payroll tax with a credit offers the opportunity to acknowledge those employers who are already contributing to the system and to start to quantify and reduce the cost shift. Employers are already paying for the cost shift, but by making it explicit, the system is more transparent, and the state can use the revenue from the payroll tax for federal match. The revenue from the payroll tax could be used to extend coverage to those who are not covered by their employer, and revenue from the health services transaction tax could be used to increase access to care for those in public programs through coverage expansions and increased provider reimbursement. Those employers currently providing coverage would be recognized for their contribution.

Design Elements	Options	Policy Considerations		Straw Proposal
		Pro	Con	
General Tax Payers	1) Employers 2) Employers and employees	1) Recognizes that employees will likely need to pay a portion of insurance costs anyway under individual mandate. Employers would often spread burden across family types, etc. 2) Appears to split tax burden explicitly between employees and employers (actual burden is determined by relative elasticities of demand for and supply of labor)	1) Theory that employers will reduce wages to offset tax burden anyway, so better to make more explicit; May lead employers to increase use of independent contractors 2) Individuals are required to purchase insurance so may pay twice in a sense; potentially undermines employer-based system	**Employers**
Exemptions	1) Small employers (0-10 employees or < $200,000 payroll?) 2) Self employed? 3) Start ups?	1) Small employers may have lower profit margins and less able to absorb costs; may stymie entrepreneurial spirit 2) Same arguments as small employer exemption + they are already purchasing insurance for themselves + they don't have payroll 3) Same arguments as small employer exemption+ No exceptions could discourage people from initiating new enterprises to begin with	1) Less broad based with exemptions; Small employers represent many of the employers not offering insurance now; Big impact on revenue collection; All employers pay workers comp, etc., why exempt from this?; Gives small employers a competitive advantage over slightly larger employers 2) Many of the arguments for small employers- plus fairness of helping pay for subsidies to modest income self-employed (why should employers and/or their workers do so); 3) Many of the arguments for small employers	**No exemptions** Propose treating small businesses and start-ups as any other employer, allowing them access to the same credits and deductions as well. Do not impose additional tax on self-employed. *Fall-back position:* exempt small employers with small payrolls and start-ups for their first year.

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Tax Base	1) Only on Social Security payroll 2) Entire payroll 3) Some point in between? (E.g. small percentage across total wages in all firms, higher % on SS earnings with credit for health spending	1) Focuses burden of tax more on employers who may not be providing insurance (i.e., larger employers are more likely to be already offering insurance); follows argument of capping SS income tax that benefits paid correlate to benefits received 2) To extent high wage employers pay fee rather than increase own-plan spending, more redistributive/ progressive 3) May be good combination of "fair share" and progressive burden—virtually all employers have at least some workers ineligible for employer plan and would qualify for state subsidy; very small across-all-employer fee should be more than offset by reduced cost-shift. It may be possible to set the tax base such that the tax rate is below some desired level and the amount raised (roughly) equals the amount needed	1) Less redistributive; increases tax paid by smaller employers 2) More tax income from employers who are already providing insurance; Could not yield additional revenue if "irresistible incentive" to increase spending on employer plan for own workers (inflationary and potential ERISA problem); amount of tax could be very high from uniformly high-wage firms 3) Those employers who do cover virtually all of their workers would still have to pay more	**Entire payroll, no cap** More progressive than lump sum tax or a cap on Social Security
Tax rate	1) Flat % of payroll 2) Graduate % by size of employer 3) Lump sum based on spending per employee	1) Easy to calculate and administer; progressive 2) More sensitive to relative vulnerability/ volatility of micro employer income 3) Easy to calculate and administer	1) May be overly burdensome on some very small fragile employers with volatile income streams 2) More administratively difficult; requires determining tiers or cut off points without much gain in policy objectives 3) Ties tax to benefits received per employee, regardless of income level; more regressive than % of payroll, burden on small, low-wage employers.	**A flat % of payroll**

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Credit Amount	1) Full credit 2) credit but small base/residual fee for all employers 3) No credit	1) Clearer argument; stronger incentive to provide insurance 2) Raise more revenue and/or allows reduced rate paid by pay employers. Some "fair share" contribution from all employers for their modest income workers ineligible for employer plan/ on publicly subsidized coverage 3) Eliminates any ERISA concerns; Clear; strong revenue raiser	1) Either reduces available revenue or requires higher payments by non-offering employers to reach revenue goals 2) Requires employers who are already providing insurance to pay additional amount 3) Same as #2, except much larger payments required of these employers	**Credit available for offering employers** o Dollar-for-dollar credit for spending on health services up to 95% of the tax rate
Credit Eligibility	1) Must pay certain % of payroll on health services (being modeled) 2) Must spend certain amount on health services per employee 3) Two-tier test combining #1 & #2 (being modeled)	1) Easy to calculate; progressive 2) Provides incentive to provide coverage for part-time employees 3) Way to combine ability to do a partial credit with some level of simplicity while providing incentive for coverage of (or "fair share" payment for) part-time employees.	1) Doesn't necessarily provide incentive for employers to provide coverage (or "fair share" payroll tax) for part-time employees 2) More difficult to calculate and explain than #1 3) More difficult to calculate and explain than #1	**Two-tier test** Credit available for employers spending on health services for employees x% of payroll on health services for employees AND demonstrating they spend a certain amount per employee *Further discussion required.*
Administration	Tax forms	Relatively simple	Complexity depends on the policy choices outlined above	**Tax forms**