

MINUTES
SENATE LOCAL GOVERNMENT & TAXATION COMMITTEE

DATE: Thursday, March 13, 2014
TIME: 3:00 P.M.
PLACE: Room WW53
MEMBERS PRESENT: Chairman Siddoway, Vice Chairman Rice, Senators Hill, McKenzie, Johnson, Vick, Bayer, Werk and Lacey
ABSENT/ EXCUSED: None
NOTE: The sign-in sheet, testimonies and other related materials will be retained with the minutes in the committee's office until the end of the session and will then be located on file with the minutes in the Legislative Services Library.

CONVENED: **Chairman Siddoway** called the meeting of the Senate Local Government and Taxation Committee (Committee) to order at 3:01 p.m.
Without objection, **Chairman Siddoway** reordered the agenda to accommodate a request from the presenter who needed to make an out of town appointment.

H 595 **Chairman Siddoway** welcomed Representative Brandon Hixon to the podium to present **H 595** relating to income taxes and contributions to medical savings accounts. **Representative Hixon** outlined the provisions of the bill.
Representative Hixon said the sole purpose of this important legislation is to empower all citizens of Idaho by encouraging them and their employers to contribute to their privately held Idaho Medical Savings Account (MSA) to utilize as a hedge against high health care costs. He said these changes are brought forth to update the severely outdated MSA statute that was enacted in 1995. He said Idaho MSAs are individual accounts that are held at private institutions across Idaho for the purpose of saving for medical expenses. They are not the same as Federal Archer MSAs, as this is Idaho's own sovereign program.
Representative Hixon said upon passage in 1995, the annual contribution limit set forth was \$2,000 per person. He said these contributions and the interest earned on them are tax deductible for state purposes. The money can accrue year over year and need not be exhausted at the end of each year, and contributions can be made by individuals or employers. He said the contributions can be used for eligible medical expenses in accordance with Internal Revenue Service Code Section 213(d), eligible medical expenses, including physician visits, insurance premiums, deductibles, copays, contact lenses and eye glasses, to some over-the-counter drugs, prescriptions and much more.
Representative Hixon next outlined the changes being made to this law and why. He said the first change removes the outdated cap of \$2,000 per person and raises it to \$20,000. He said this is necessary because health care costs have seen enormous increases statewide, noting that even Idahoans with good insurance coverage often end up with large bills after a procedure. He said, "In my mind, an average Idahoan cannot afford the high cost of health care any longer, and removing this cap allows for them to accrue and save tax free money to help pay for necessary medical expenses."

Representative Hixon said the next change gives an incentive to all Idaho employers to start contributing to their employees' MSAs, by giving the employer a 10 percent tax credit and allowing them to roll that credit over for up to 15 years. The credits are not refundable.

Representative Hixon said his thought behind the change is to encourage Idaho companies to contribute to these accounts, putting the money back in the hands of the people to save for and combat high health care costs. He said businesses small and large have felt the crunch of high costs associated with health care in recent years. He said employees are the most important thing to any business, and this will give them an incentive and very useful tool that will ultimately result in happier and healthier employees who will begin constructing a financial safety net for medical costs.

Representative Hixon said the last change ensures that if a person in Idaho seeks State assistance for medical reasons, such as from the CAT Fund, that person's MSA must first be exhausted before receiving assistance. He said the reason for this is that in the event someone's employer or an individual has contributed to these accounts and they have accrued an amount of tax free savings, it is good taxpayer friendly policy to require the use of these funds first before assistance is rendered.

In closing, **Representative Hixon** said he would summarize his feelings about why the changes are needed. He said he feels one of the biggest issues people face in Idaho today is the high cost of health care and the detriment it places every day on hard working Idaho families. He said Idaho is near the bottom of the states in per capita wages, and that when combined with health care cost increases that seem to have no plateau or ceiling, this is a recipe for bankruptcy for Idaho residents. He said in fact, 50 percent of all bankruptcy cases in Idaho are medical-related.

Representative Hixon said the underlying premise of this legislation is to give Idahoans some much needed buying power for health care expenses, noting it will not fix the high cost of health care, but rather give Idahoans an extra tool against them. He said "most of us" were taught the importance of saving our money, and this legislation perpetuates that idea for some of the biggest costs we face every day - medical costs. He said many Idaho families are just one major medical procedure away from bankruptcy, and this legislation will ease that burden. He said it covers the entire spectrum of Idaho's population. He said older people who may have higher medical costs can put more money in to help ease those costs, while younger working people have an opportunity to start saving and can use the money to pay regular costs, while saving more and more in case they need extra for a major procedure.

Representative Hixon said it is his hope that as Idahoans use this tool, that it may help inject some free market shopping for people that now have buying power from their savings accounts. He said, "Remember that money talks, and if someone has cash to bring to the table, I would hope that it would be a powerful negotiation tool for them to use, as well."

Representative Hixon said one other good side effect this bill may bring forth will be that the interest that the financial institutions holding these MSAs have will increase significantly because the cap has been raised. He said right now, many institutions have stopped this program because of the current \$2,000 cap. He said he hopes the Committee sees the value of what these changes will accomplish for Idaho families and he asked for their affirmative vote.

Senator Werk asked how this legislation interacts with the federal statute, and if the tax credit is only for the State. **Representative Hixon** replied that is correct, the tax savings is for State purposes only. He said people can use medical expenses on a federal level to deduct from federal tax, but they must meet federal requirements. He said he thinks double-dipping would be minimal from that. He said this is also the opinion of the Idaho State Tax Commission (Commission).

Senator Werk asked if there are compatible and incompatible accounts and accounting of these credits and benefits between federal and state requirements, and how is the Commission going to be able to incorporate this legislation when handling those returns that may have differences. **Representative Hixon** asked the Chairman for permission to read an email from the Commission regarding Senator Werk's question. The Chairman granted permission, and **Representative Hixon** read the following:

"From: Alan Pack, Tax Policy Specialist, Idaho State Tax Commission; Sent: Thursday, March 13, 2014 2:29 p.m.; To: Representative Brandon Hixon; Cc: Michael Chakarun; Subject: Idaho MSA" – "Representative Hixon, Idaho's MSA does create a double dip situation, i.e. an individual can claim medical expenses as itemized deductions and also get a deduction for contributing to an Idaho MSA. This is how it has always been with the Idaho MSA contributions. However, with the increase in the percentage of federal adjusted gross income (10%) the number of individuals that will be able to claim medical expenses as itemized deductions will be severely limited. Only those with major or catastrophic medical occurrences will be able to itemize their medical expenses. There are still two classes of individuals that retain the 7.5% limitation for medical expenses, those being lower income and people age 65 and older. We do not think the double dip situation occurs very often." "Alan Pack • Tax Policy Specialist Idaho State Tax Commission • Tax Policy"

Senator Werk asked for clarification on the amount in the Fiscal Note. He asked if the \$4 million figure was per week, per month, per year or over ten years.

Representative Hixon replied that the \$4 million is the amount of the fiscal impact that the Commission provided based on current holdings with MSAs. He said originally there was no cap placed on this, so when a \$20,000 cap is placed, that is the amount the Commission came up with. He said it would be a potential tax liability down the road. **Senator Werk** asked again if it is a \$4 million per year liability once this kicks in. **Representative Hixon** said he is double checking, and he said he believes it would be per year.

Chairman Siddoway welcomed Elizabeth Criner of the Idaho State Dental Association (ISDA) to the podium to testify. She said the ISDA is supportive of **H 595**. **Ms. Criner** called the Committee's attention to a letter from the ISDA's legislative committee chairman, Dr. Steve Bruce, that outlines their position on this issue (see attachment 1). She said that many people in small business do not have dental policies today. She said even in her own business Veritas, employees are better off putting money aside each month rather than purchasing a policy, because it doesn't cover as much out of pocket as other types of health care policies might. **Ms. Criner** said in looking at current restrictions of MSAs, a \$2,000 cap could be a single critical oral health event. She said that is why she is in support of raising that cap and giving consumers another tool in the toolbox to help finance their oral health care needs. She said she always likes to promote that oral health is as important to general health as anything else. **Ms. Criner** asked the Committee to support the legislation.

Chairman Siddoway invited Suzanne Budge, representing the National Federation of Independent Business (NFIB), to the podium to testify. **Ms. Budge** said the NFIB has long supported flexibility for employers with businesses who have fewer than 50 employees for self-funding and high deductibles and maximum flexibility at every level. She said a colleague of hers was involved in writing the initial legislation in 1995 on behalf of farmers in the small group market. She said Idaho was leading the vanguard for this type of approach for medical funding to support self-employed people before it was popular or even included in federal law. She said MSAs did come at the federal level which improved the tax situation, but the State level is still a significantly helpful tool for those who self insure and pay those dental bills and medical costs. **Ms. Budge** noted that she personally uses MSAs to help cover medical and dental costs. She said the NFIB supports this bill and any other legislation that provides flexibility in this arena.

Chairman Siddoway invited Representative Hixon to return to the podium. **Representative Hixon** said, "What this bill boils down to is putting money back in the hands of the people in the state of Idaho so they can have a fighting chance against high health care costs." He said these are increases that are seen year over year over year with no plateaus, but yet higher still. He said he realizes this is an investment of \$4 million per year, but he thinks the return on that investment given to Idaho citizens would be very great. He said this would be a benefit to every Idaho citizen, not just one group or another, which he thinks makes for good legislation and good public policy. **Representative Hixon** asked the Committee to send it to the floor with a do pass recommendation.

Chairman Siddoway asked if Representative Hixon has worked with anyone on this bill in the Senate who would be the sponsor on the Senate side.

Representative Hixon answered no.

Senator Hill commented that he wanted to commend Representatives Hixon and Wood who worked on this bill. He said he thinks it has some good advantages in encouraging people to save for medical expenses, which keeps medical expenses down when people pay for them out of pocket instead of through insurance. He said at the same time, he feels the need to let the Committee know that he has three concerns, and will leave it to the Committee to determine the best policy. He said he will share his concerns in reverse order of importance. **Senator Hill** said his first concern is that he has spent 13 years here trying to simplify the tax code, but more and more differences are added between state and federal returns. He noted that this is not a new difference, because MSAs already exist, but this is a larger amount. He said hopefully it will get used more.

Senator Hill said another concern he has is about the point of trying to promote a free market system, but this bill offers a 10 percent credit to employers who contribute to the MSA. That would mean that not only do they get an income tax deduction for it, but they get a 10 percent credit as well. He said employers don't get a 10 percent credit for offering health insurance to their employees. He said therefore, in essence, the bill tries to influence and tell them what is the best way to insure their employees. He said employers are getting an additional incentive for the MSA not available for insurance premiums, and in a way letting them double dip by letting them have a credit as well.

Senator Hill said his biggest concern is about fairness. He shared an example that he worked through recently with Michael Chakarun of the Commission, who was also present in the audience if correction is needed in this example.

Senator Hill said a taxpayer has \$100,000 in earnings and puts \$20,000 into an MSA and gets a tax deduction on their State return. Then that year, or another year, (it really doesn't matter) he has \$20,000 in medical expenses paid with this account. He said when they itemize their deductions, most taxpayers have to reduce the medical deduction by 10 percent of their adjusted gross income. In this example, that would mean 10 percent of \$100,000 which would be \$10,000 to reduce. This means on his itemized deductions, there is a \$20,000 expense, which needs to be reduced by \$10,000, resulting in a \$10,000 deduction on his itemized deductions. In addition, he said, he still gets to deduct the \$20,000 he put into the MSA.

Senator Hill said that by pushing that through the MSA, and paying for the same expenses, all of a sudden he has a \$30,000 deduction for a \$20,000 cash outlay. He said that might be a good policy the Committee may want to allow, but he said it's a struggle for him. He said he wants everyone to understand how this all works so they can make their best judgment.

Vice Chairman Rice asked Senator Hill if that \$10,000 itemized deduction on the federal return flows through and shows up on the State return. **Senator Hill** said yes, and confirmed with **Mr. Chakarun** in the audience, who also said yes, that is right.

Senator Werk stated, "We want to be fair to all taxpayers if we can." He said if this starts to double, triple, and quadruple dip, then it gets to be difficult. He asked how this analysis changes for a taxpayer who makes only \$30,000 and does not get the same amount of deductions and somehow magically comes up with \$20,000 over the years to put in one of these accounts. On the other end, what if someone earns \$500,000. He asked if this bill benefits a higher income person more than it benefits a lower income person.

Senator Hill commented that it is hard to go through every scenario in his mind, but it seems the benefit would be opposite, because a very high income person with \$500,000 in earnings can only deduct medical expenses to the extent they exceed \$50,000, which is 10 percent of their earnings. In addition, he said, when a taxpayer is in that high level, their itemized deductions start to phase out. In that high income case, the only way that taxpayer will get to deduct medical expenses would be through the MSA, and they could only deduct it once because they're not getting the itemized deduction because they're not over the threshold or it's being phased out, or both.

Vice Chairman Rice asked Senator Hill about the discussion in which a taxpayer puts \$20,000 in during one year, and deduct it and then they have the \$20,000 expense, then they maybe get an additional \$10,000 deduction. He asked what if, under current law, they put in \$2,000, then \$2,000, then \$2,000 over the years until there was \$20,000 in the account. He asked what happens when there is then a \$20,000 expense, would the taxpayer - under current law - get the \$20,000 and the \$10,000 deductions. **Senator Hill** answered yes, they would, and that is the same problem that exists now. He said they can double dip with what they have now. The difference is the magnitude of the dipping.

Senator Werk said he assumes the level at which the cap is set on an annual basis only impacts the issue from the standpoint of the level at which it happens. He said if instead of \$20,000, the decision was that \$10,000 was a more reasonable level, the same kind of effect would still happen, but the accrued tax benefits would be that much less.

Senator Hill said he thinks so, noting that he gave an example for simple math, not to exaggerate the issue. He said depending on the person's income level, whether or not they itemize, and what they itemize, they still may not qualify to use the \$10,000 in the itemization. He said the nice thing about MSAs is they allow taxpayers to deduct expenses off the top, whether or not they itemize, whether or not they go over the limit for medical threshold.

Senator Hill said it is a good plan, but he wishes the federal law would catch up to the amount. He said if it were a federal point, then it would go all the way through, but the federal returns do not allow a deduction on the front end and also on the Schedule A, so there is not a double dip, nor is there a difference between the two returns that need to be kept track of, nor a 10 percent credit that needs to be calculated on a separate sheet over and keep track of for future use, and other complications. He said he really doesn't want to discourage someone who thinks this is a good idea, but he believes everyone should have all the information when making a decision. He said it has some good points, but he probably won't support the bill.

Senator Vick asked Representative Hixon how he arrived at the \$20,000 amount in this bill. **Representative Hixon** answered there was no magical formula by which he came up with that number. He said when he presented it originally, there was no cap. The Committee decided it would be best at \$20,000.

Senator Werk said he appreciates the discussion and he sees the merit of the bill. He thanked the dental representatives for attending. He said he appreciates Representative Hixon's efforts through the process. He said there are two aspects with which he is uncomfortable, including the 10 percent credit on the employer's side. He said when there is an incentive like that, it tends to skew behavior to offer one thing over another, when there may or may not be a benefit. He said that gives him pause. He said he is also uncomfortable with the jump from \$2,000 to \$20,000.

Senator Werk said he would like to amend the bill and remove the 10 percent employer credit and put the cap at \$10,000 as a more doable jump.

MOTION: **Senator Werk** moved, seconded by **Senator Hill**, to send **H 595** to the 14th Order for possible amendment.

DISCUSSION: **Senator Hill** said he would feel better about something different, but he doesn't know if he will support it after it's amended either. He said if it gives the Committee more assurance, he'll support the motion so it can get to the floor so the whole body could eventually vote on it.

ROLL CALL VOTE: **Chairman Siddoway** called for a roll call vote. **Senators Hill, McKenzie, Johnson, Bayer, Werk** and **Lacey** voted aye. **Chairman Siddoway, Vice Chairman Rice** and **Senator Vick** voted nay. The motion carried.

Chairman Siddoway thanked Representative Hixon and requested he work on a proposal for amendments to resolve concerns and to find a Senate sponsor for the bill.

H 602 **Chairman Siddoway** welcomed Bill Roden, representing the Coeur d'Alene Tribe, to the podium to present **H 602**, relating to income tax to add a clause to **H 384**.

Mr. Roden said he **H 602** is a measure advised by the Legislative Services Office (LSO) to make an adjustment to **H 384** which has already passed the Senate, the House and was signed into law by the Governor.

He said **H 384** corrected a situation with relation to income earned by an Indian tribal member employed on a reservation that was not his own. He said there was no objection to the bill. He said the bill had a retroactive clause to January 1, 2013. He said LSO advised him that there is case law that if there was not an emergency clause, it could invalidate the retroactive provision. He said for that reason, LSO suggested returning with this bill to include an emergency clause to correct the problem.

MOTION: **Senator McKenzie** moved, seconded by **Senator Werk**, to send **H 602** to the floor with a **do pass** recommendation.

DISCUSSION: In discussion, **Vice Chairman Rice** commented that he also does not see the need for this bill as the Commission would already be stopped because it was party to the lawsuit and so would be bound by the decision of the judge and would be bound by the decision of the U.S. Supreme Court. He said it doesn't hurt to do this bill, just to be sure.

The motion carried by **voice vote**. **Chairman Siddoway** noted that Vice Chairman Rice carried the initial bill on the floor and would carry this one as well.

H 370 **Chairman Siddoway** welcomed Michael Chakarun, Tax Policy Manager with the Idaho State Tax Commission (Commission) to the podium to present **H 370**, relating to cigarette taxes. **Mr. Chakarun** said this bill is a technical correction relating to the tobacco tax.

Mr. Chakarun said the first change amends Idaho Code § 63-2511 to eliminate a reference to vending machine operators. Cigarettes cannot be sold from vending machines so this language is no longer needed. The second change relates to collection and enforcement, Sections § 63-2516 and § 63-2563. He noted these sections have many references back to the collection and enforcement provisions of the Income Tax Act. This is done in the product tax statutes to avoid duplicating language. The income tax collection and enforcement statutes make reference to taxable year but cigarette and tobacco use monthly taxable periods. This bill adds language to clarify that any reference to taxable year in the Income Tax Act enforcement statutes shall be considered a taxable period in the cigarette and tobacco tax statutes. The proposed language is consistent with the language used in the collection and enforcement statutes for beer in Idaho Code § 23-1050A, and for wine in Idaho Code § 23-1322A. Those changes to Idaho Code were added in 1984.

Chairman Siddoway pointed out to the Committee that the Secretary had put the minutes from the previous discussion for the Committee to reference. He said he hopes Mr. Chakarun's explanation alleviates the Committee's concerns from the initial presentation. **Vice Chairman Rice** said he appreciates and prefers using the language taxable period rather than taxable month.

MOTION: **Senator Lacey** moved, seconded by **Senator Bayer**, to send **H 370** to the floor with a **do pass** recommendation. The motion carried by **voice vote**.

H 541 **Chairman Siddoway** welcomed Phil McGrane, Chief Deputy Clerk with Ada County Clerks, to the podium to present **H 541**, relating to county records to allow for the photographic or digital storage of records. **Mr. McGrane** said the purpose of this bill is to update and modernize the code to allow counties to digitize their public records and then dispose of the paper. He said the language used in this bill was taken from the city code which was updated in 2009 to allow cities to do this very thing. He said one distinction that differs from the city code is that this bill also includes permanent records.

Mr. McGrane said that allows all records at the county level to be digitized. He said many of the most important records have already been digitized by specific statues, such as land records. He said they no longer keep any paper records. He said court records have already been digitized for quite some time. He said this bill will include all other records like vouchers, receipts, and items that become public record when they are created. **Mr. McGrane** said the Idaho Association of Counties supports this legislation.

Mr. McGrane said the reason this came about is that a few years ago Ada County was looking to purchase a multimillion dollar building to store paper records because they had amassed so much paper. He said the office came together and realized they should invest tax dollars more wisely. He said by storing items digitally, they consolidate and do not spend nearly as much to manage those records. He said the benefit is the documents are more accessible to the public. He said one can imagine sifting through numerous volumes of records is not the same as searching on a computer. He said this will also manage the security of the documents much longer. **Mr. McGrane** asked the Committee to move this forward with a do pass recommendation.

Senator Johnson asked why the legislation doesn't recommend a format for digital storage. **Mr. McGrane** said the standard practice is to use tif images. He said it doesn't matter if software changes because tif images can always be read because of the management of them. He said the records retention people at each of the counties handle them, and this works for them.

Senator McKenzie said he thinks this is a good idea and makes records safer. He said digital records are easier to maintain, backup and store offsite, whereas paper records are easily destroyed if there's a fire. He said the courts have done this for a while, and he does it with his own practice that otherwise would have a ton of paper. He thinks it's a cost effective and secure measure.

MOTION: **Senator McKenzie** moved, seconded by **Vice Chairman Rice**, to send **H 451** to the floor with a **do pass** recommendation. Motion carried by **voice vote**.

ADJOURNED: There being no further business, **Chairman Siddoway** adjourned the meeting at 3:50 p.m.

Senator Siddoway
Chair

Christy Stansell
Secretary