



Employer-Sponsored Health Insurance Tax Exclusion

Center Forward Basics

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Overview

Employer-sponsored health insurance (ESI) is a cornerstone of the U.S. healthcare system, providing coverage to approximately 60% of non-elderly Americans. A significant factor contributing to the prevalence of ESI is the current tax exclusion for employer-provided health benefits, commonly referred to as "**employer exclusion.**" This policy allows employer contributions toward employee health insurance premiums to be excluded from employees' taxable income, resulting in substantial tax savings for both parties. Understanding the mechanics, utilization, and implications of employer exclusion is essential for comprehending its role in the U.S. healthcare landscape.

In this Basic, we examine employer exclusion as a workplace benefit, its role in tax policy, financial trade-offs, and the potential effects of its altering or elimination.

Mechanics of the Employer Exclusion

Under the employer exclusion, the portion of health insurance premiums paid by employers is not considered taxable income for employees. Additionally, employees' contributions to their health insurance premiums are often made **pre-tax**, reducing their taxable income. Employers also benefit by deducting their premium contributions as a business expense, lowering their overall tax liability. This system incentivizes businesses to offer comprehensive health insurance coverage and makes it more affordable for employees.

Utilization by Employers and Employees

Employers leverage the exclusion to offer comprehensive health benefits as part of compensation packages, enhancing their ability to attract and retain talent. Employees benefit from reduced taxable income and access to employer-negotiated health plans, often providing better coverage options and lower premiums than individual market plans. Since most large companies offer ESI, this model has become the standard for healthcare coverage in the U.S. Furthermore, the National Institute of Health has conducted studies on the link between economic performance and health insurance. The study shows a correlation leading many to believe employees having health insurance leads to a healthier, and more productive workforce.

Potential Consequences of Changing the Exclusion

Removing or capping employer exclusion could have far-reaching effects. Employees might experience increased taxable income, increasing tax

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Center Forward brings together members of Congress, not-for profits, academic experts, trade associations, corporations and unions to find common ground. Our mission: to give centrist allies the information they need to craft common sense solutions, and provide those allies the support they need to turn those ideas into results.

In order to meet our challenges we need to put aside the partisan bickering that has gridlocked Washington and come together to find common sense solutions.

For more information, please visit www.center-forward.org

Key Definitions:

- **Employer-Sponsored Insurance (ESI):** Health insurance coverage provided to employees and their families through employers
- **Employer Exclusion:** A tax provision allowing employer-paid health insurance premiums to be excluded from employees' taxable income
- **Pre-Tax Contributions:** Employee contributions to health insurance premiums made before income tax is applied
- **Cadillac Tax:** A now-repealed excise tax on high-cost employer-sponsored health plans
- **Self-Insured Plans:** Employer health plans

burdens, and potentially making employer-sponsored insurance less attractive. Employers could reconsider offering health benefits, resulting in decreased ESI coverage rates. This shift might drive more individuals to seek insurance through government programs or the individual market, potentially increasing public expenditures and destabilizing existing insurance pools. The change may also increase the uninsured rate, which would increase uncompensated care costs for hospitals and other health care providers.

Cost Implications

While the employer exclusion provides tax advantages, it also represents a significant expenditure for the federal government. Estimates suggest the exclusion results in substantial revenue losses annually due to forgone tax collections. Critics argue the exclusion disproportionately benefits higher-income individuals who are more likely to have access to generous employer-sponsored plans, potentially exacerbating income inequality. Additionally, some analysts contend the exclusion contributes to rising healthcare costs by insulating employees from the true cost of their insurance, leading to overutilization of medical services.

Perspectives from Key Stakeholders

Organizations such as the U.S. Chamber of Commerce emphasize the value of employer exclusion in maintaining affordable and comprehensive health coverage for employees. They argue altering the exclusion could disrupt the employer-based insurance system, which many workers prefer and rely upon.

Some policy analysts and economists advocate reforming the exclusion to address its regressive nature and the substantial impact on federal revenues. Proposals include capping the exclusion to limit benefits for high-cost plans or replacing it with alternative tax incentives that promote equity and cost-effectiveness.

Labor unions and employee advocates often support employer exclusion, viewing it as a critical component of worker compensation. They caution changes to the exclusion could lead to reduced benefits or increased costs for employees, particularly in unionized industries where health benefits are a key aspect of collective bargaining agreements.

Conclusion

The employer exclusion for health insurance premiums plays a pivotal role in shaping the U.S. healthcare system by incentivizing employer-sponsored coverage and protecting the broader healthcare delivery system from uncompensated care. While it offers clear benefits to employers and employees, it also presents challenges related to federal revenue losses and potential inequities. Any policy considerations regarding the modification or elimination of the exclusion must carefully weigh the potential economic and social impacts to ensure changes do not inadvertently undermine the accessibility and affordability of health insurance for American workers.

where the employer assumes the financial risk of providing healthcare benefits rather than from a carrier

- **Affordable Care Act Marketplace:** The federally or state-run exchanges where individuals can purchase health insurance plans
- **Tax Expenditures:** Revenue losses to the government resulting from tax exclusions, deductions, or credits

Key Statistics:

- 155 million Americans receive health insurance through their employer
- The employer exclusion costs the federal government an estimated \$300 billion annually in lost tax revenue
- 83% of large employers offer health insurance coverage to their employees
- Employees with employer-sponsored coverage contribute an average of 17% of their premium costs, while employers cover the rest
- 53% of small businesses (fewer than 50 employees) offer health benefits
- Higher-income workers are four times more likely to receive employer-sponsored insurance than lower-income workers
- A strong correlation with a coefficient 0.429 was found between health insurance and economic performance
- Over 80% of the uninsured are in families within 400% of the federal poverty line

Links to Other Resources

- Alliance to Fight for Healthcare: [Advanced Employer Provided Coverage](#)
- Alliance to Fight for Healthcare: [Public Opinion Polling](#)
- Alliance to Fight for Healthcare: [Effects on Cost](#)
- Bipartisan Policy Center: [Paying the 2025 Tax Bill - Employer Sponsored Health Insurance](#)
- Benefits Pro: [Unions, Business Groups Warn Congress Against Touching Group Health Tax Rules](#)
- CATO Institute: [Report to the Department of Government Efficiency](#)
- Chamber of Commerce: [The Origins and Growth of Employer Provided Insurance](#)
- Chamber of Commerce: [American Employers Underscore Value of Employer Exclusion in Delivering Affordable, Robust Health Care](#)
- Chamber of Commerce: [New Poll of American Workers](#)
- Employee Benefit Research Institute: [Trends in Self-Insured Health Coverage - ERISA at 50](#)
- Kaiser Family Foundation: [Employer-Sponsored Health Insurance 101](#)
- Kaiser Family Foundation: [Key Facts about the Uninsured Populations](#)
- National Institute of Health: [The Relationship Between Health Insurance and Economic Performance](#)
- Wall Street Journal: [GOP Takes Control, Headed for a Fiscal Cliff](#)