

**Frequently Asked Questions**  
**NO TAXES ON INJURED WORKERS:**  
**HB5545 (LaHood) and SB2989 (Schwertner) <sup>1</sup>**  
(revised 5-7-25)

- 1. Who supports this bill?** Many business and policy groups have voiced support, including but not limited to, Texas Conservative Coalition Research Institute (TCCRI), Texas Public Policy Foundation (TPPF), Texas Retailers Association, Association for Responsible Alternatives to Workers' Compensation (ARAWC), Walmart, Sysco, Jamak Fabrication, Owner Operator Services, Inc. (Texas McDonald's franchisees). This bill supports approximately 33,000 Texas employers that do have workers' compensation insurance and their injured workers covered by alternative injury benefit plans. <sup>2</sup>
- 2. What federal tax laws exempt workers' compensation and payments "in the nature of" workers' compensation from federal income and employment taxes?** See Attachment #2.
- 3. Will it be mandatory for employers to treat wage replacement benefits as tax-free?** No. As with all matters of state and federal taxation, employers should consult their accounting, legal and other advisers to independently determine whether to continue withholding and payment of federal income and employment taxes on such payments or rely on this new Texas law as authority to treat such payments as tax-free.
- 4. How will the bill's tax-free treatment be implemented?** When employers first began paying wage replacement benefits outside of the Texas workers' compensation system, adjustments were made to their HR policies, procedures and payroll systems to code such payments as disability benefits or "sick pay" (not for work performed) and taxable. That process has varied between companies and payroll systems. Likewise, if desired, employers can make adjustments to code wage replacement benefits as tax-free.
- 5. What position will the Internal Revenue Service take on this bill?** The IRS will likely be neutral and not challenge tax-free treatment under this bill because:
  - a. Wage replacement benefits under an injury benefit plan are for the exact same purpose and are calculated and administered in the exact same manner as wage replacement benefits under workers' compensation;
  - b. Legal precedent has established workers' compensation as a subject area of state control, and the Texas Legislature has authority to address what it considers to be a Texas workers' compensation law or "in the nature of" a Texas workers' compensation law;
  - c. This bill amends the Texas Workers' Compensation Act, not federal law; <sup>3</sup>
  - d. This bill aligns with and relies on the same concise, plain wording found in existing federal tax law; and

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<sup>1</sup> HB5545 and SB2989 are referred to herein as "the bill". The companion bills are at Attachment #1.

<sup>2</sup> [Employer Participation in the Texas Workers' Compensation System, 2022 Estimates](#), p. 13.

<sup>3</sup> This bill also will not be preempted by the Employee Retirement Income Security Act because it in no way adds to, subtracts from, or otherwise attempts to regulate or control any of the terms or administration of an ERISA plan.

e. The U.S. Supreme Court’s decision in 2024 to repeal the “Chevron doctrine” means that federal agencies, like the IRS, no longer have broad authority to create new rules and adopt statutory interpretations that depart from the plain wording of a statute.

- 6. What if the employer and injured worker disagree on the taxability of wage replacement benefits?** If the employer decides to withhold taxes but the injured employee wants to pursue tax-free treatment, the employee can work with his or her own advisers to determine whether and how to file with the IRS for a tax refund.
- 7. What are the fiscal and economic impacts of the bill on the State of Texas?** This bill will not cost the state anything and add approximately \$50 million back into the Texas economy every year, benefiting Texas businesses and families. <sup>4</sup>
- 8. Will the State of Texas lose money by not receiving the same unemployment taxes?** No, because state unemployment taxes should be paid only on wages for services performed – not wage replacement while an employee is unable to perform services; and state unemployment taxes only apply to the first \$9,000 of wages. Unemployment taxes will still be paid during a year because the average time missed from work under an injury benefit plan is only 3 weeks.
- 9. How will this bill affect the Texas workers’ compensation system?** It will have no impact whatsoever on workers’ compensation insurance companies, the Texas Division of Workers’ Compensation, or any employer or worker covered by the Texas workers’ compensation system. The current legislative penalty for not carrying workers’ comp is unchanged, with these employers remaining fully exposed to negligence liability claims by injured employees.
- 10. Why would workers’ comp insurance companies be neutral on or support this bill?** This is a mature Texas marketplace with very few employers moving in or out of the Texas workers’ compensation system, and there is no justification for punishing a large group of Texas employers for not purchasing workers’ compensation insurance by requiring they and their injured workers continue to pay unnecessary taxes to the federal government. With 100% of all governmental employers, virtually all of their vendors, and over 80% of all private employers in the State of Texas covered by workers’ compensation, no concern has been expressed that this bill will harm the state system or unfairly compete with a workers’ comp insurance company. Instead, a voluntary Texas workers’ compensation system and bills like this reflect a common-sense approach to supporting companies relocating their businesses to Texas; and most of those new Texas employers purchase workers’ compensation insurance. This tax issue will also be a non-factor in the decision of employers on whether to participate in Texas’ voluntary workers’ compensation system or sponsor an injury benefit program. When a nonsubscriber feasibility analysis is performed – considering all money spent on medical and wage replacement benefits, claim administration costs, attorney fees, insurance premiums, the cost of state and federal legal compliance, and negligence liability exposure – this tax issue will be lost in the rounding.

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<sup>4</sup> Economic Impact Analysis at Attachment #3.

# ATTACHMENT #1

89R19198 TYPED

By: LaHood

H.B. No. 5545

A BILL TO BE ENTITLED

AN ACT

relating to the consideration of wage replacement benefits in the nature of workers' compensation.

BE IT ENACTED BY THE LEGISLATURE OF THE STATE OF TEXAS:

SECTION 1. Subchapter A, Chapter 406, Labor Code, is amended by adding Section 406.0025 to read as follows:

Sec. 406.0025. CONSIDERATION OF WAGE REPLACEMENT BENEFITS IN THE NATURE OF WORKERS' COMPENSATION.

Wage replacement disability benefits paid by an employer that does not carry workers' compensation insurance to an employee who is unable to return to work due to an injury in the course and scope of employment are considered payments made under a statute in the nature of a workers' compensation statute solely for the purpose of being excluded from taxable income for federal income and employment tax purposes.

SECTION 2. The enactment of this Act is a clarification of existing law and does not imply that existing law may be construed as inconsistent with the law as amended by this Act.

SECTION 3. This Act takes effect September 1, 2025.

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**Attachment #2**  
**Federal Tax Laws at issue in**  
**HB5545 (LaHood) and SB2989 (Schwertner)**

**Income Taxes**

**Internal Revenue Code section 104**

(a) In general. Except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., expenses) for any prior taxable year, **gross income does not include—**

**(1) amounts received under workmen's compensation acts as compensation for personal injuries or sickness;**

**IRS Regulation: 26 CFR § 1.104-1 - Compensation for injuries or sickness.**

**(b) Amounts received under workmen's compensation acts.** Section 104(a)(1) excludes from gross income amounts which are received by an employee under a workmen's compensation act (such as the Longshoremen's and Harbor Workers' Compensation Act, 33 U.S.C., c. 18), or **under a statute in the nature of a workmen's compensation act** which provides compensation to employees for personal injuries or sickness incurred in the course of employment....

**Employment Taxes**

**IRS Regulation: 26 CFR § 31.3121(a)(2)-1 - Payments on account of sickness or accident disability, medical or hospitalization expenses, or death.**

(a) The term “wages” does not include the amount of any payment (including any amount paid by an employer for insurance or annuities, or into a fund, to provide for any such payment) made to, or on behalf of, an employee or any of his dependents **under a plan or system established by an employer which makes provision for his employees generally** (or for his employees generally and their dependents) **or for a class or classes of his employees** (or for a class or classes of his employees and their dependents), on account of—

(1) Sickness or **accident disability of an employee** or any of his dependents, only **if payment is received under a workers' compensation law...**

(d) Workers' compensation law.

(1) For purposes of paragraph (a)(1) of this section, **a payment made under a workers' compensation law includes a payment made pursuant to a statute in the nature of a workers' compensation act.**

**(e) Examples.** The following examples illustrate the principles of paragraph (d) of this section:

Example 1.

A local government employee is injured while performing work-related activities. The employee is not covered by the State workers' compensation law, but is covered by **a local government**

**ordinance that requires the local government to pay the employee's full salary when the employee is out of work as a result of an injury incurred while performing services for the local government.** The ordinance does not limit or otherwise affect the local government's liability to the employee for the work-related injury. The local ordinance is not a workers' compensation law, but it is in the nature of a workers' compensation act. Therefore, the salary the employee receives while out of work as a result of the work-related injury is **excluded from wages** under section 3121(a)(2)(A).

Example 2.

The facts are the same as in *Example 1* except that the local ordinance requires the employer to continue to pay the employee's full salary while the employee is unable to work due to an injury whether or not the injury is work-related. Thus, the local ordinance **does not limit benefits to instances of work-related disability.** A benefit paid under an ordinance that does not limit benefits to instances of work-related injuries is not a statute in the nature of a workers' compensation act. Therefore, the salary the injured employee receives from the employer while out of work is wages subject to FICA even though the employee's injury is work-related.

Example 3.

The facts are the same as in *Example 1* except that the local ordinance includes a rebuttable presumption that certain injuries, including any heart attack incurred by a firefighter or other law enforcement personnel is work-related. The presumption in the ordinance does not eliminate the requirement that the injury be work-related in order to entitle the injured worker to full salary. Therefore, the ordinance is a statute in the nature of a workers' compensation act, and the salary the injured employee receives pursuant to the ordinance is excluded from wages under section 3121(a)(2)(A).

(f) It is immaterial for purposes of this exclusion whether the amount or possibility of such benefit payments is taken into consideration in fixing the amount of an employee's remuneration or whether such payments are required, expressly or impliedly, by the contract of service.



**ATTACHMENT #3**  
**Economic Impact Analysis of**  
**HB5545 (LaHood) and SB2989 (Schwertner)**  
(revised 4-18-25)

As determined below, the annual economic impact of making currently taxable wage replacement disability payments to injured Texas workers non-taxable is **\$50 million**.

To assess the economic impact, we can calculate the potential tax savings for both employees and employers and apply an economic impact multiplier based on these reasonable assumptions developed in collaboration with nonsubscriber industry service providers managing over ten thousand injury claims annually:

1. Texas injury benefit plans process an average of 50,000 claims per year.
2. 30% of these claims involve lost time due to disability from on-the-job injuries, equating to 15,000 claims annually.
3. The average wage replacement benefit is \$1,200 per week, paid for three weeks.
4. For such short-term payments, we can (A) use the marginal federal income tax rate of 22% without regard to tiered rates or standard deductions, (B) use employment tax rates of 7.65% for the employer's portion and 7.65% for the employee's portion, and (C) assume no impact on state unemployment taxes paid by the employer on other wages received by the employee during the calendar year.
5. An economic impact multiplier of 2.5x.

**Step-by-Step Calculation:**

1. **Number of claims per year:**  $50,000 \times 30\% = 15,000$  claims
2. **Total annual wage replacement benefits:**  $15,000 \times 1,200 \times 3 = 54,000,000$

**Tax Savings:**

1. **Employer Employment Tax Savings:**  $54,000,000 \times 0.0765 = 4,131,000$
2. **Employee Income + Employment Tax Savings:**  
 $54,000,000 \times (0.22 + 0.0765) = 54,000,000 \times 0.2965 = 16,011,000$

**Economic Impact (with 2.5x multiplier):**

1. **Employer Impact:**  $4,131,000 \times 2.5 = 10,327,500$
2. **Employee Impact:**  $16,011,000 \times 2.5 = 40,027,500$
3. **Total Economic Impact:**  $10,327,500 + 40,027,500 = \underline{\underline{\$50,355,000}}$