

Overview of Key Tax Provisions of Health Care Reform Acts (HR3590 and HR4872)

The health care reform acts, HR3590 and HR4872, make sweeping changes to key individual and business tax provisions, most of which have delayed effective dates. Below is a summary of these provisions.

Individual Provisions

1. [Adoption credit](#)
2. [Flexible Spending Account \(FSA\) / Health Savings Account \(HSA\) reimbursable expenses](#)
3. [HSA distributions](#)
4. [FSA contribution maximum](#)
5. [Medical expenses deduction \(Schedule A\)](#)
6. [Medicare Tax](#)
7. [Additional tax on net investment income](#)
8. [Compliance implications of not obtaining minimum required health care coverage](#)

Business Provisions

1. [Small business health care premium credit](#)
2. [Excise tax on indoor tanning](#)
3. [Employer reporting of employer-paid health insurance premiums](#)
4. [Certain employers required to provide health care coverage to employees](#)
5. [Compliance penalty for not providing required health care \(Play or Pay implications\)](#)
6. [Excise tax on high-cost health plans](#)

Items that are or may be a tax return event are circled.

Individual Provisions

Effective CY2010 (TS2011)

1. **Adoption credit.** Increases the 2010 adoption credit to \$13,170 (up from the \$12,170 originally scheduled for 2010) and makes the credit fully refundable.
 - Under prior law the credit is nonrefundable, and any unused portion of the credit was carried over for up to five years. (Any unused carry forward amount from 2009 is refundable in 2010.)
 - The bill also postpones the sunset of the adoption credit increase included in EGTRRA one year to 12/31/2011. The 2011 maximum credit is \$13,360 in 2011.

Effective CY2011 (TS2012)

2. **Flexible Spending Account (FSA) / Health Savings Account (HSA) reimbursable expenses.** Beginning in 2011, medications require a prescription to be reimbursable through a flexible spending account or health savings account.
 - As a result, over-the-counter drugs such as OTC allergy medications must have a doctor's prescription to be qualified expenses for HSA or FSA purposes. Insulin and medical devices (such as crutches) do not require a prescription.
3. **HSA distributions.** Increases the penalty for nonqualified distributions from a health savings account to 20% (currently set at 10% for 2010.)

Effective CY2012 (TS2013)

- Nothing in the new law becomes effective in 2012.

Effective CY2013 (TS2014)

4. **FSA contribution maximum.** Contributions to FSAs are limited to \$2,500 (generally set at \$5,000).
 - The limitation is adjusted for inflation after 2013.
5. **Medical expense deduction (Schedule A).** Increases the threshold for deducting medical expenses to 10% beginning in 2013 (currently set at 7.5% of AGI for 2010).
 - Through 2016, the 7.5% AGI limitation is unchanged if at least one taxpayer on the return is age 65 or older by the end of the year.

6. **Medicare tax.** Increases the employee portion of Medicare tax by 0.9% to 2.35% (currently set at 1.45%) for earned income in excess of \$200,000 (\$250,000 for joint filers).
- Any tax not collected by the employer (paid through withholding) must be paid by the employee via the income tax return.
 - Applies to self-employment income as well.
 - No deduction is allowed for the excise tax paid.
7. **Additional tax on net investment income.** High income taxpayers will be subject to a new 3.8% tax on net investment income.
- The tax is limited to the lesser of: 3.8% times
 - (1) Net investment income or
 - (2) MAGI minus applicable threshold.
 - The applicable threshold is \$250,000, for joint filers, \$125,000 MFS, and \$200,000 for other filers.
 - The tax does not apply to net income from active trades or businesses conducted by a sole proprietor, partnership, C corporation, or S corporation. The tax does apply to a passive activities and investments of working capital in a sole proprietorship or pass-through entity.
 - The tax will be paid on the filed tax return.

Effective CY2014 (TS2015)

8. **Compliance implications of not obtaining minimum required health care coverage.** Beginning in 2014, if an individual chooses not to purchase health care coverage (and is required to do so), they will pay a penalty, in the form of an additional tax per individual required to be covered.
- The amount is phased in starting in the year 2014 (\$95 in 2014, \$325 in 2015, \$695 in 2016). For dependents that are required to be covered, the penalty is equal to one-half of the stated amounts.
 - In 2016, the penalty is the greater of 2% of income or \$695, but it is limited to an amount equal to the national average premium for minimum level coverage times an applicable % (1% for 2014, 2% for 2015, 2.5% for 2016 and later years).
 - The additional tax related to this penalty may not be offset by a credit on the tax return.
 - Certain individuals are exempt from this tax (e.g. Native Americans, insurance costs >8% of household income)
 - Individuals are exempt from the requirement for months they are incarcerated, not legally present in the United States or maintain a religious exemption to self-employment tax and adhere to the tenets of the sect.
 - Individuals residing outside of the United States are deemed to maintain minimum essential coverage.
 - Dependents are not required to obtain coverage as they are to be covered by the insurance obtained by the taxpayer(s) for whom they are a dependent.
 - An exception to the penalty may apply if the individual was without health care for less than 90 days.
 - Individuals required to obtain health insurance must complete an "information return" to substantiate health care coverage likely in a form similar to a Form 1099 information reporting document.

Note: To facilitate compliance in obtaining health care coverage, individuals with incomes below 400% of the poverty level who purchase insurance through an exchange will qualify for a subsidy to help cover the cost of the insurance. Generally, the subsidy is received via a reduction in the premium paid to the insurance company. A true up on the tax return will be required if the taxpayer receives too large a subsidy (paid back as an additional tax) or too little subsidy (claimed as a refundable credit). Subsidies or credits received under the program are disregarded for purposes of determining eligibility for Federal or Federally-assisted programs such as Medicaid.

Business Provisions

Effective CY2010 (TS2011)

1. **Small business health care premium credit.** A qualified small employer (25 or fewer full-time equivalent (FTE) employees or less with an average annual employee payroll of \$50,000 or less) that pays health insurance premiums on behalf of its employees will qualify for a credit.
 - To determine the number of FTE employees for purposes of the credit, total regular (non-overtime) hours worked by employees who worked more than 120 days during the year (whether FT, part-time, or seasonal) is divided by 2,080.
 - To determine the average annual employee payroll, only wages and fringe benefits subject to FICA are included. Wages paid to seasonal workers (those that worked 120 days or less during a cyclical / seasonal busy time of year for the business) are not counted.
 - For calendar years 2010-2013, the credit equals the lesser of:
 - (1) 35% of nonelective contributions to the health care plan or
 - (2) 35% of nonelective contributions that would have been contributed had the health care plan premiums equaled the small group market premiums in the rating area in which the employee enrolls for coverage.
 - After 2013, the credit percentage increases to 50%.
 - After 2013, the credit is only available for insurance purchased through the exchange and for a maximum of two consecutive years.
 - Employers with 10 or fewer FTE employees and average annual wages up to \$25,000 get 100% of credit. The credit phases out
 - (1) for each FTE employee over 10 and
 - (2) to the extent average annual employee payroll exceeds \$25,000.
 - Sole proprietors, partners, 2% shareholders of an S Corporation, and 5% owners of the employer are not treated as employees for purposes of this credit.
 - Generally, 501(c) tax-exempt organizations with 25 or fewer FTE employees qualify for a 25% credit (35% after 2013).
 - The \$50,000 wage threshold is adjusted for inflation after 2013.
2. **Excise tax on indoor tanning.** A 10% tax would apply to indoor tanning procedures on or after 7/1/10.
 - The tax does not apply to phototherapy performed by a licensed medical professional.
 - The tax is collected from customers at the time of payment for the service. If the business does not collect the tax, the business is liable for the tax.
 - The tax must be paid in quarterly. The method by which the payment is made will be determined by the IRS (probably in a manner similar to sales and excise tax reporting).

Effective CY2011 (TS2012) and CY2012 (TS2013)

3. **Employer reporting of employer-paid health insurance premiums.** Beginning in 2011, employers have the option to report the dollar amount of employer-paid health insurance premiums paid for each employee in their W-2s. The amount will be shown on the W-2 as a nontaxable employer fringe benefit. Starting in 2012, the reporting requirement is mandatory.

Effective CY2013 (TS2014)

- Nothing in the new law becomes effective in 2013.

Effective CY2014 (TS2015)

4. **Certain employers required to provide health care coverage to employees.** Employers with at least 50 employees must provide health care coverage to its full-time employees and pay at least 60% of the premium cost.

- An employer is not treated as employing more than 50 people if:
 - 1) The workforce equals 50 or more employees for 120 days or less during the year, and
 - 2) Those who are employed during the 120 day period, in 1 above, were seasonal workers.
- A seasonal worker is one who works 120 days or less per year during a seasonally busy time of year.
- Definition of a FT employee is an employee who works at least 30 hours per week.
- In determining the number of FT workers in any month, the total regular (non-overtime) hours worked during the month by part-time (PT) workers is divided by 120 and the resulting number is added to the number of FT workers. Note: The 120 divisor equals 30 hour work week times 4 work weeks in a month.

Example: During the month of June, 2014, Simsbury Corp. has 45 FT employees and 15 PT employees. The PT employees work a total of 1200 regular hours during the month.

The 15 PT employees are the equivalent of 10 FT employees ($1200 \div 120$). Simsbury is considered to have 55 ($45 + 10$) FT employees for the month of June.

- After 2013, construction industry employers with at least 5 FT employees during the preceding calendar year and an annual payroll exceeding \$250,000 would be required to offer coverage.
- Important: Employers who have less than 50 employees are NOT required to provide health insurance to their employees.

5. **Compliance penalty for not providing required health care (Play or Pay Implications).** If a qualified employer does not provide minimum health insurance coverage *and* at least one FT employee has been certified as enrolled in a subsidized health plan (considered a certified employee) the employer is subject to an excise tax calculated on a monthly basis equal to:

(FT employees – 30) x \$2,000 divided by 12.

- If the employer provides a health care plan but pays less than 60% of the premiums or the plan is determined to be unaffordable by one or more employees *and* at least one FT employee has been certified as enrolled in a subsidized health plan (considered a certified employee), the monthly excise tax is equal to the lower of:

(1) The number of certified employees times \$3,000 divided by 12, or

(2) (FT employees – 30) x \$2,000 divided by 12.

Effective CY2015 (TS2016) through CY2017 (TS2018)

- Nothing in the new law becomes effective in 2015-2017.

Effective CY2018 (TS2019)

6. **Excise tax on high-cost health plans.** A 40% nondeductible excise tax will be assessed on coverage exceeding \$10,200 for individual annual coverage and \$27,500 for family coverage
- Increases the threshold amounts for individuals age 55 or older or in high risk industry workers to \$11,850 for individual coverage and \$31,950 for family coverage.
 - Although the tax is assessed on the issuer of the insurance, it is likely that the cost will be passed down to the employer or insured individual via higher premiums (which would in turn increase the excise tax) or reduced benefits.