CLIENT LETTER
Dealing with Health Care Reform's Tax Laws

Dear Client:

Many of the most far-reaching provisions of the health care reform law passed in 2010 are scheduled to take effect after 2013. As 2014 approaches, much work needs to be done in dealing with all of the requirements for individuals, businesses and others. The tax law plays a major role in implementation of health care reform. From the tax credits and subsidies used to expand health coverage, to the many penalties, fees and surtaxes designed to pay for it, the Tax Code is front and center.

Background. Health care reform is actually made up of two new laws: the Patient Protection and Affordable Care Act (PPACA) and the Health Care and Education Reconciliation Act (HCERA). The PPACA was crafted largely in the Senate and sets out the general framework of health care reform. The HCERA was prepared in the House to modify the PPACA, especially in the areas of tax credits and cost sharing for individuals to help make coverage more affordable. Common features to both laws are delayed effective dates for many of the provisions, which make strategic planning all that more important.

U.S. Supreme Court. Immediately after Congress passed health care reform, several states challenged its constitutionality in the federal courts. In 2011, the Supreme Court agreed to hear the dispute. The justices heard several days of oral arguments in March 2012 and announced their decision on June 28, 2012. The Supreme Court, in a 5–4 ruling, upheld health care reform (except for certain provisions affecting the expansion of Medicaid). Writing for the majority, Justice Roberts explained that the controversial individual mandate was within Congress' constitutional power to tax.

New taxes and penalties. Viewing the historic health care reform package from the context of the Tax Code, many new taxes and penalties stand out immediately above the rest. It is also important to remember many provisions have different effective dates.

Highlights include:

- Higher income taxpayers (individuals who earn more than $200,000 for the year; $250,000 for married couples) will pay an additional 0.9 percent in Hospital Insurance (Medicare) tax, starting in 2013;

- Beginning in 2013, the new Net Investment Income (NII) 3.8 percent surtax generally applies to the lesser of NII or the amount of modified adjusted gross income above a threshold amount ($200,000 for single taxpayers, $250,000 for married couples filing a joint return, and $125,000 for married couples filing separate returns).
- Large employers (generally employers with 50 or more full-time employees) may be liable for a shared responsibility payment if they do not offer coverage or if the coverage is deemed unaffordable (this so-called "employer mandate" goes into effect in 2015, following a one-year postponement announced by the IRS in July 2013);

Small employers (generally employers with no more than 25 employees) may qualify for a tax credit to help offset the cost of providing health insurance to employees;

- Young adults may remain on their parents' health insurance plans through age 26;
- The health care reform package extends the income tax exclusion to any employee's child who has not attained age 27 as of the end of the tax year;
- Many individuals will be required to obtain health insurance or be subject to a penalty tax starting in 2014 (this is the so-called "individual mandate");
- Tax credits to subsidize the cost of health insurance premiums will be available to qualified individuals, starting in 2014;
- Health flexible savings arrangement (FSA) dollars are limited to prescription medications with some exceptions after 2010, along with a $2,500 annual cap on expenses covered under health FSAs, after 2012;
- A 40 percent excise tax will be imposed on high-cost, "Cadillac" employer-sponsored health coverage, starting in 2018;
- Fees will be imposed on the pharmaceutical industry and health insurance providers, starting in 2011 and 2014, respectively;
- An excise tax is imposed on medical device manufacturers after 2012; and
- Limits on tax-subsidized medical expenses will be imposed by raising the itemized medical expense deduction floor for regular tax purposes from 7.5 percent to 10 percent, generally starting in 2013 with a temporary exception for senior citizens.

Exchanges. The health care reform package provides for state insurance exchanges by 2014 to help individuals and qualified employers obtain coverage. The federal government will operate exchanges in states that do not create their own exchanges. Coverage will be offered at various levels. Qualified individuals may be eligible for premium assistance tax credits to help pay for coverage through an insurance exchange. In May 2013, the U.S. Department of Labor (DOL) provided model notices for employers that do not offer a health plan and for employers that offer insurance to some or all of their employees. Employers may use one of the models, as applicable, or a modified version that meets content requirements, DOL explained.

IRS guidance. The IRS and other federal agencies have issued a plethora of guidance for how to comply with the provisions of the health care reform package. This growing body of guidance has included the tax treatment of certain adult children covered under a parent's employer health plan; cost-sharing for preventative services by certain religious employers; eligibility of certain over the counter drugs and medicines for tax-free reimbursement; W-2 reporting; requirements for tax-exempt hospitals; and the format and requirements for providers or insurers with respect to the summary of benefits and coverage.

Sincerely yours,
LA FIRST TAX & FINANCIAL SERVICES