

## **Re: Dealing with Health Care Reform's New Tax Laws: The Health Care and Education Reconciliation Act of 2010**

Dear Client:

Now that Congress has passed a landmark health care reform package, much work needs to be done in dealing with new requirements. While the end result of the legislative process is necessarily health care related, the tax law plays a major role in its implementation. 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.

**Two new laws.** Health care reform is actually made up of two new laws: the Patient Protection and Affordable Care Act of 2010 and the Health Care and Education Reconciliation Act of 2010. The Patient Protection Act was crafted largely in the Senate and sets out the general framework of health care reform. The Reconciliation Act was prepared in the House to modify the Patient Protection Act, 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.

**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. Initially, we would advise taking particular note of the following highlights:

- \* Individuals who earn more than \$200,000 for the year (\$250,000 for married couples) will be paying an additional 0.9 percent in Hospital Insurance (Medicare) tax, starting in 2013;
- \* Individuals whose adjusted gross income for the year exceeds \$200,000 (\$250,000 for joint filers), whether from wages or otherwise, will also be paying an additional 3.8 percent Medicare tax on net investment income, starting in 2013;
- \* Employers with 50 or more employees generally will be required to provide a minimum level of health insurance for their employees or pay a penalty per employee, starting in 2014;
- \* Small employers with no more than 25 employees are entitled to up to a 35 percent tax credit on the cost of providing health insurance for employees, starting immediately in 2010;
- \* Most individuals will be required to obtain health insurance or be subject to a penalty tax starting in 2014;
- \* Tax credits to subsidize the cost of health insurance premiums will be available to individuals earning up to 400 percent of the poverty level, starting in 2014;
- \* Health flexible savings arrangement (FSA) dollars will be limited to prescription medications with some exceptions after 2010, along with placing a \$2,500 annual cap on expenses covered under health FSAs, starting in 2013;
- \* 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 will be 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.

***Tax incentives.*** Among a handful of tax incentives provided under the new health-care reform package, two are particularly notable at this time: (1) the ability of parents to cover adult children up to age 27 under their tax-qualified employer-provided health plans, starting immediately for plans that elect to beat the mandatory post-September 22 year deadline for doing so; and (2) the unveiling of a simplified cafeteria plan specifically tailored to small businesses, starting in 2011.

***Exchanges.*** The health care reform package requires each state to establish an exchange by 2014 to help individuals and qualified employers obtain coverage. Coverage will be offered at various levels. Qualified individuals may be eligible for premium assistance tax credits, cost-sharing or vouchers to help pay for coverage through an insurance exchange. An individual's income, whether or not coverage is provided by his or her employer, will all be taken into account when determining if the individual qualifies for a premium assistance tax credit, cost-sharing or voucher.

***IRS guidance.*** Over the course of the next few months, the IRS and other federal agencies will be filling in details on how to comply with all the provisions under the massive health care reform package. The IRS is expected to issue guidance soon on the provisions with effective dates in 2010 and 2011.

Our office will be staying on top of all developments, with an eye toward how to best maximize results under the new law for our clients. We are prepared to advise our clients on all compliance rules and tax-reduction opportunities that undoubtedly will arise. In the meantime, if you have any questions about the new law, please do not hesitate to call our office.

Sincerely yours,

Gordon Fleck and Barbara Uhlich