

# 2010 Tax Legislation

Patient Protection and Affordable Care  
Health Care Reconciliation  
HIRE

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- Patient Protection and Affordable Care Act (P.L. 111-148)
- Health Care and Education Reconciliation Act of 2010 (P.O. 111-152)
- Hiring Incentives to Restore Employment ("HIRE") Act (P.L. 111-147)
- American Jobs and Closing Tax Loopholes Act (HR 4213, May 2010)



# Health Care Reform

# Two Acts – A Framework

- Patient Protection and Affordable Care Act, signed March 23, 2010
- Health Care and Education Affordability Reconciliation Act, signed March 30, 2010
- Combine for over 2,000 pages
- Much more to come – regulations, guidance

- Individual v. Group Health Plan
- Grandfathered v. New Plan
  - Grandfathered? In existence at 3/23/10, no changes required other than some mandated benefits
  - No material modification allowed – we don't know what this means, waiting for guidance
  - Something you want to keep – for instance, no nondiscrimination testing

- Escape:
  - Coverage of preventive care
  - Nondiscrimination rules
  - Claims appeal procedures
  - Transparency requirements
  - Ensuring quality of care
  - Fair health insurance premiums
  - Prohibition on discrimination against providers
  - Cost sharing limitations
  - Requirement to provide essential benefits
  - Participation in clinical trials

# The Changes Start Today

- Small Employer Tax Credit
- Early Retiree Reinsurance Program - \$5 billion available, employers are lining up, application available by June 23 from HHS

# Simple Cafeteria Plan - 2011

- Eligible employer – employs on average 100 or fewer in either of the preceding two years
- Can grow up to 200 employees
- Uniform contributions – not less than 2%
- Eligibility – 1,000 hours in prior year, unless under age 21, less than 1 YOS, covered by CBA
- Free pass on nondiscrimination testing and concentration of benefits

- Over-The-Counter items no longer reimbursable without a prescription
- Impact on FSA, HRA and HSA
- Most cafeteria plans will need to be amended – look for a reference to 213(d) rather than 213(a)
- Failure to amend to 213(a) would make all benefits taxable to all employees

- Credit and exclusion amount increased from \$10,000 to \$13,170
- Was set to decrease to \$5,000
- Changed to a refundable credit
- Sunset now 12/31/2011 was 2010

- Community Living Assistance Services and Supports Act
- National Voluntary LTC program – employers that enroll responsible for monthly payroll deduction
- Auto-enroll employees with an opt-out
- Secretary to establish an actuarial sound program

- Expected premium - \$125 -150/month, nominal for FPL and students
- 5 year vesting period
- Benefit – not less than \$50/day, scaled to functionability
- Unable to perform 2 or 3 ADLs: eating, toileting, transferring, bathing, dressing, continence
- No lifetime cap

- Slowly closing the donut hole
  - No coverage for prescription drugs between \$2,830 and \$4,550
  - For 2010, \$250 rebate for those incurring donut hole expenses
  - For 2011, sliding coinsurance for generics and brand names, negotiated prices coming
- Medicare Part C or Medicare Advantage plans – these are private plans reimbursements will be reduced

- The excise tax for paying nonqualified costs is increased to 20%

# Dependent Coverage Expanded - 2011

- Plan years beginning on or after 9/23/2010
- Only about 14% of plans are early adopters
- Through age 26, even if married
- No more imputed income concerns
- Grandfathered plans until 2014 – only if child is not eligible for other coverage
- Health plans may start pricing per head
- Estimated to add 1,250,000 young adults
- Children can be a son, daughter, adopted child, stepchild or eligible foster child

# No More Lifetime/Annual Caps - 2011

- Applies to all plans
- For plan years prior to 2014 some reasonable restrictions - HHS to define essential health benefits
- Can still limit days of treatment, number of visits

# Nondiscrimination Testing - 2011

- Currently, only applies to self-insured plans
- Only for new plans not grandfathered plans
- Cannot discriminate as to eligibility and level of benefits
- HCE – top 25% of all employees
- Failure results in taxable benefits
- Other – 409A? 4980D?

- But immediate impact today – terminating employee entitled to request early issuance
- Report the aggregate cost of coverage under the plans, monthly calculation of coverage – COBRA cost, IRS to issue regs on valuation
- Plans included: medical, prescription, executive physicals, on-site/near-site clinics providing more than first-aid care, dental and vision if not stand-alone
- Cost of coverage under FSA/HSA, specific disease or hospital indemnity plan excluded (AFLAC)
- Required for employees, but seems to apply to retirees and those on COBRA, such as a terminnee or surviving spouse

- No more preexisting condition exclusion for all plans
- For children under age 19 on 9/23/2010
- For all adults in 2014

# Automatic Enrollment

- For employers of 200 or more
- Auto-enroll unless employee opts out
- When? By regulation

- Limited to \$2,500 each year
- Indexed for inflation
- Previously no cap
- Family typically participated in just one plan

- To avoid a penalty, individuals must have acceptable coverage from one of the following sources:
  - Employer-sponsored plan (including a grandfathered plan)
  - An individual policy (purchased through a private insurer or through an Exchange)
  - Government program (Medicare, Medicaid, Veterans, CHIP)
- Those without coverage face the greater of a dollar penalty or a percentage of household income penalty
  - Dollar penalty equals  $\frac{1}{2}$  of the amount listed below for each uninsured dependent under the age of 18
  - Total dollar penalty for a family is capped at 300% of the normal penalty

## Individuals (Cont.)

Year	\$ Penalty	% Penalty
2014	95	1.0
2015	325	2.0
2016 and after	695 as indexed	2.5

- Large Employers ( $\geq 50$  EEs) that do not offer health coverage and have at least one FT EE who receives premium tax credit must pay a penalty
- \$2,000 per FT EE (excludes the first 30 EEs)
- Offer health coverage and have at least one FT EE who receives a premium tax credit because employment-related health coverage is not adequate or affordable (plan covers less than 60% of costs or EE's contribution to ER coverage  $> 9.5\%$  of household income) must pay the lesser of:
  - \$3,000 per employee who is receiving a premium tax credit, or
  - \$2,000 for each FT EE
- Small Employers ( $< 50$  EEs) are exempt from penalties
- For “pay or play” purposes, full time employees are those who work 30 or more hours per week
- ER assessments are not tax deductible
- Vouchers

- Estimated 38% of plans do not provide reasonable cost insurance
- Estimated 60% of large employer plans will be impacted by the Cadillac tax

- Even the average plan will have difficulties
- Assume a 7.5% cost trend without the cost escalators of health care reform
- Every dollar over taxed at 40%

Classification	2008 Cost	2018 Projected Cost	FSA Addition (\$2,500)	Cadillac Tax Threshold
Single	\$4,386	\$11,450	\$11,540	\$10,200
Family	\$12,298	\$25,350	\$27,870	\$27,500

# Other Premium Pressures - 2013

- Implementation of X12 5010 transaction standards
- Implementation of ICD-10 code sets
- Expands diagnosis and procedure codes from 24,000 to 155,000
- Increased administrative expenses, billing errors, and auditing

# Small Employer Health Insurance Credit

## *Effective 2010*

- Allows eligible small employers to claim a 35% credit (25% in the case of tax-exempt employers) for premiums paid toward health coverage for its employees in tax years beginning 2010 through 2013. These percents increase to 50% and 35%, respectively, in 2014.
- An eligible small employer is an employer that has no more than 25 full-time employees and the average annual compensation of these employees is not greater than \$50,000.
- The credit is reduced by 6.6667% for each full-time employee in excess of 10 employees and by 4% for each \$1,000 that average annual compensation paid to the employee exceeds \$25,000.
- After 2013, employer must participate in an insurance exchange to be eligible for credit.

# Small Employer Health Credit (Cont.)

## *Effective 2010*

- Must pay at least 50% of premium for all employees and the percentage must be uniform among all employees, except for during the year 2010
- Steps in determining credit
  - Determine number of employees
  - Determine number of hours of service by those employees
  - Calculate number of employer's FTEs
  - Determine average annual wages paid per FTE
  - Determine premium taken into account
- Effective for tax year 2010; See Notice 2010-44

- Example: For the 2010 taxable year, a taxable small employer has 12 FTEs and average annual wages of \$30,000. The employer pays \$96,000 in health insurance premiums for its employees and meets all other requirements for the credit.
- The amount of the credit is calculated as follows:
- The initial amount of the credit determined before any reduction:  $(35\% \times \$96,000) = \$33,600$ .
- Credit reduction for FTEs in excess of 10:  $(\$33,600 \times 2/15) = \$4,480$ .
- Credit reduction for wages in excess of \$25,000:  $(\$33,600 \times \$5,000/\$25,000) = \$6,720$ .
- Total credit reduction:  $(\$4,480 + \$6,720) = \$11,200$ .
- Total 2010 tax credit equals \$22,400.

# Medicare Tax On High Income Taxpayers

## *Effective 2013*

- Generally, an additional 0.9% Medicare tax is imposed on the wages and self-employment income of certain high-income taxpayers received with respect to employment for tax years beginning after December 31, 2012.
- The additional Medicare tax is imposed on every taxpayer (other than a corporation, estate or trust) who receives wages or self-employment income in excess of \$200,000 (\$250,000 in the case of a joint return, \$125,000 in the case of a married taxpayer filing separately). The additional Medicare tax increases the employee portion to 2.35% or a total Medicare rate of 3.8%.

# Medicare Tax on Investment Income

## *Effective 2013*

- Effective for tax years beginning after December 31, 2012, a 3.8% Medicare tax is imposed on the lesser of an individual's net investment income for the tax year or modified AGI in excess of \$200,000 (\$250,000 in the case of joint filers and surviving spouses, and \$125,000 in the case of a married taxpayer filing separately.)
- Net investment income is the excess of the sum of the following items less any otherwise allowable deductions properly allocable to such income or gain:
  - Gross income from interest, dividends, annuities, royalties and rents unless such income derived is in the ordinary course of any trade or business (unless such trade or business is a passive activity of the taxpayer or involves trading in financial instruments and commodities);
  - Other gross income from any passive trade or business; and
  - Net gain included in computing taxable income that is attributable to the disposition of property other than property held in any active trade or business.

# Itemized Deductions For Medical Expenses

## *Effective 2013*

- For tax years beginning after December 31, 2012, the threshold to claim an itemized deduction for unreimbursed medical expenses is increased from 7.5% of AGI to 10% AGI for regular income tax purposes
- Effective 2013

# Health Care Coverage Reporting

## *Effective 2014*

- Any person who provides minimum essential health care coverage to an individual during a calendar year is required to file an information return. Such person is also required to furnish a written statement to the individual with respect to whom information is reported, detailing the contents of the information return submitted to the IRS.
- Large employers (defined as having more than 50 employees) or any employer offering minimum coverage will have to file an information return disclosing the type of insurance offered to its employees and other required information.

# Additional Hospital Reporting Requirements

## *Effective March 23, 2010 & March 23, 2012*

- New section 501(r) imposes additional requirements on hospital organization that are currently described in 501(c)(3) of the Code as exempt from federal income tax. The new rules are effective for tax years beginning after March 23, 2010 (except for the community needs assessment, which isn't effective until March 23, 2012).
- The four new requirements are:
  - community needs assessment;
  - adoption of a financial assistance policy;
  - limitation on charges; and
  - certain billing and collection practices.

- Exemption from employers portion of Social Security tax for a qualified individuals employment from 3/18/2010 through 12/31/2010
- Employer can also claim a credit of up to \$1,000 for retaining a newly hired worker for at least 52 consecutive weeks
- Qualified Individual:
  - Begins employment after 2/3/2010 and before 1/1/2011
  - Certifies by signed affidavit under penalties of perjury that they have not been employed for more than 40 hours during the previous 60-day period
  - Is not hired to replace another employee unless the other employee voluntarily quit or was fired with cause
  - Is not related to the employer in any way that would make him or her ineligible for the Work Opportunity Credit

# Code Sec. 179 Expense Election for 2010

- The increased Code Sec. 179 expense allowance provided for tax years beginning in 2008 and 2009 is extended one additional year. Thus, for the years beginning in 2010, the Code Sec. 179 dollar limitation is \$250,000, and the investment limitation is \$800,000.

# Economic Substance Doctrine

## *Effective 3/30/2010*

- Codified in IRC 7701 (o) (1)
- For any transaction to which the economic substance doctrine is relevant, such transaction will only be treated as having economic substance if, apart from the federal income tax effects, it changes in a meaningful way the taxpayer's economic position, and the taxpayer has a substantial purpose for entering into the transaction

# Economic Substance Doctrine (Cont.)

*Effective 3/30/2010*

- The codified standard clarifies that the economic substance doctrine involves a conjunctive analysis requiring an inquiry regarding the objective effects of the transaction on the taxpayer's economic position, as well as an inquiry regarding the taxpayer's subjective motives for engaging in the transaction
- The profit potential will be considered
- Applies to transactions entered into after 3/30/10

- Sales of medical devices
  - Tax of 2.3% of the price of medical devices sold by manufacturer or importer
  - “Medical device” is any item regulated by the FDA as defined in 21 USC 321 and intended for humans (not eyeglasses, contacts or hearing aids)
  - Effective after 12/31/12
- Indoor Tanning
  - 10% tax
  - Effective 7/1/10
  - Membership fees

# Reporting Requirements on Payments to Corporations

*Effective after 12/31/11*

- Exceptions to Form 1099 reporting eliminated
- All payments made by a payor to a corporation totaling \$600 or more annually must be reported on a Form 1099
- Tax-exempt entities are exempted
- Effective as to payments after 12/31/11

# American Jobs and Closing Tax Loophole Act of 2010

*Effective after 12/31/10*

- Reinstates through 2010 the research credit
- Reinstates through 2010 the five-year recovery period for certain farm machinery and equipment
- Extends through 2010 the election to take an itemized deduction for sales tax in lieu of income tax
- Extends through 2010, the additional standard deduction for real estate taxes
- For 2010, taxpayers can take the above the line deduction for qualified education expenses

# American Jobs and Closing Tax Loophole Act of 2010 (Cont.)

- Extends through 2010 the \$250 above the line deduction for school teacher's business expenses
- Extends through 2010 the 50% first year depreciation deduction for replacement property made in a Presidentially declared disaster area
- WOTC for Hurricane Katrina employees hired from 8/29/09 to 8/28/10
- Up to \$100,000 of charitable distributions from IRA's allowed through 2010

# American Jobs and Closing Tax Loophole Act of 2010 (Cont.)

- Taxation of carried interest
  - Would prevent investment fund managers from paying taxes at capital gains rates on investment management services income received as carried interest in an investment fund
  - To the extent that carried interest reflects a return on invested capital, the bill would continue to tax carried interest at capital gain tax rates
  - To the extent that carried interest does not reflect a return on invested capital, the bill would require investment fund managers to treat 75% of the remaining carried interest as ordinary income (50% for taxable years beginning before January 1, 2013)

# American Jobs and Closing Tax Loophole Act of 2010 (Cont.)

- Ensuring Collection of employment taxes earned by certain service professionals
  - Social Security taxes are imposed on compensation and self-employment income up to the Social Security Wage Base (currently \$106,800) and the Medicare tax is imposed on all self-employment and compensation income
  - Some service professionals have been avoiding Medicare and Social Security taxes by routing their self-employment income through an S corporation.

# American Jobs and Closing Tax Loophole Act of 2010 (Cont.)

- Ensuring Collection of employment taxes earned by certain service professionals (cont)
  - Would address the aforementioned abuse in situations where
    - An S corporation is engaged in a professional service business that is principally based on the reputation and skill of 3 or fewer individuals
    - An S corporation is a partner in a professional service business
  - Would also clarify that individuals that are engaged in professional service businesses are unable to avoid employment taxes by routing their earnings through a limited liability corporation or a limited partnership
- Effective for tax years beginning after 12/31/10