

Summary of key provisions in ground-breaking health reform law

The President's signature on H.R. 4872, the Health Care and Education Reconciliation Act of 2010 (Reconciliation Act, 03/30/2010) completes a massive overhaul of the U.S. health care system affecting nearly all taxpayers, many employers, and many elements of the health care industry will be complete.

The Reconciliation Act modifies legislation signed into law on March 23 that contains the bulk of the health reform law, H.R. 3590, the Patient Protection and Affordable Care Act (Health Care Act, [P.L. 111-148](#)). However, the Reconciliation Act also includes new provisions that weren't part of the earlier legislation, such as codification of economic substance, elimination of a tax credit for "black liquor" and expanded dependent coverage in employer health plans.

This article carries a summary of the key provisions in the new health reform legislation, along with Code Sections and amending Act Sections. Note some changes may be affected by more than one Health Care Act Section, or by both the Health Care Act and the Reconciliation Act. For a Special Study on health-related revenue raisers in the new health reform law, see [¶ 2](#). For a Special Study on tax changes relating to the new law's universal health coverage mandate, see [¶ 1](#).

Tax Changes Relating to Universal Health Coverage Mandate

Penalty for remaining uninsured. For tax years beginning after Dec. 31, 2013, non-exempt U.S. citizens and legal residents will have to maintain minimum essential coverage or pay a penalty.

Those failing to maintain minimum essential coverage in 2016 will be subject to a penalty equal to the greater of: (1) 2.5% of household income over the threshold amount of income required for income tax return filing, or (2) \$695 per uninsured adult in the household. The fee for an uninsured individual under age 18 will be one-half of the fee for an adult. The total household penalty won't exceed 300% of the per adult penalty (\$2,085), nor exceed the national average annual premium for the "bronze level" health plan offered through the Insurance Exchange that year for the household size.

The per adult annual penalty will be phased in as follows: \$95 for 2014; \$325 for 2015; and \$695 in 2016. For years after 2016, the \$695 amount will be indexed to CPI-U, rounded to the next lowest \$50. The percentage of income will be phased in as follows: 1% for 2014; 2% in 2015; and 2.5% beginning after 2015. If a taxpayer files a joint return, the individual and spouse will be jointly liable for any penalty payment. The penalty, which will apply to any period the individual does not maintain minimum essential coverage (determined monthly), will be assessed through the Code.

Among those individuals who will be exempted from the penalty: Individuals who cannot afford coverage because their required contribution for employer sponsored coverage or the lowest cost "bronze plan" in the local Insurance Exchange exceeds 8% of household income; those who are exempted for religious reasons; and those residing outside of the U.S. ([Code Sec. 5000A](#), as added by Health Care Act Sec. 1501, as amended by Health Care Act Sec. 10106, and as further amended by Reconciliation Act Sec. 1002)

Low-income tax credits for participating in health exchanges. For tax years ending after 2013, tax credits will be available for individuals and families with incomes up to 400% of

the federal poverty level (\$43,320 for an individual or \$88,200 for a family of four) that are not eligible for Medicaid, employer sponsored insurance, or other acceptable coverage. These individuals and families will have to obtain health care coverage in newly established Insurance Exchanges in order to obtain credits. (New [Code Sec. 36B](#), Health Care Act Sec. 1401, 1411 and 1412, as amended by Health Care Act Secs. 10104, 10105, and 1017, and as further amended by Reconciliation Act Sec. 1001) A "cost-sharing subsidy" will be provided to low income individuals to help with health insurance costs. (Health Care Act Secs. 1402, 1411, and 1412, as amended by Health Care Act Sec. 10104, and further amended by Reconciliation Act Sec. 1001)

Employer responsibilities. For months beginning after Dec. 31, 2013, an "applicable large employer" (generally, one that employed an average of at least 50 full-time employees during the preceding calendar year) not offering coverage for all its full-time employees, offering minimum essential coverage that is unaffordable, or offering minimum essential coverage that consists of a plan under which the plan's share of the total allowed cost of benefits is less than 60%, will have to pay a penalty if any full-time employee is certified to the employer as having purchased health insurance through a state exchange with respect to which a tax credit or cost-sharing reduction is allowed or paid to the employee. The penalty for any month will be an excise tax equal to the number of full-time employees over a 30-employee threshold during the applicable month (regardless of how many employees are receiving a premium tax credit or cost-sharing reduction) multiplied by one-twelfth of \$2,000.

Also, an applicable large employer that offers, for any month, its full-time employees and their dependents the opportunity to enroll in minimum essential coverage under an employer sponsored plan will be subject to a penalty if any full-time employee is certified to the employer as having enrolled in health insurance coverage purchased through a State exchange with respect to which a premium tax credit or cost-sharing reduction is allowed or paid to such employee or employees. ([Code Sec. 4980H](#), as added by Health Care Act Sec. 1513, as amended by Health Care Act Sec. 10106, and as further amended by Reconciliation Act Sec. 1003)

"Free choice vouchers." After Dec. 31, 2013, employers offering minimum essential coverage through an eligible employer-sponsored plan and paying a portion of that coverage will have to provide qualified employees with a voucher whose value can be applied to purchase of a health plan through the Insurance Exchange. Qualified employees are those employees:

- ... who do not participate in the employer's health plan;
- ... whose required contribution for employer-sponsored minimum essential coverage (if they did participate in the plan) exceeds 8%, but does not exceed 9.5% of household income; and
- ... whose total household income does not exceed 400% of the poverty line for the family.

After 2014, the 8% and 9.5% will be indexed to the excess of premium growth for the preceding calendar year. The value of the voucher is equal to the dollar value of the employer contribution to the employer-offered health plan and is not includable in income to the extent it is used for the purchase of health plan coverage. If the value of the voucher exceeds the premium of the health plan chosen by the employee, the employee is paid the excess value of the voucher. The excess amount received by the employee is includable in gross income. If an individual receives a voucher, he is disqualified from receiving any tax credit or cost sharing credit for the purchase of a plan in the Insurance Exchange. Similarly, if any employee receives a free choice voucher, the employer is not

assessed a shared responsibility payment on behalf of that employee. ([Code Sec. 139D](#), as added by Health Care Act Sec. 10108)

Tax credits for small employers offering health coverage. For tax years beginning after Dec. 31, 2009, an eligible small employer will be given a tax credit for nonelective contributions to purchase health insurance for its employees. An eligible small employer generally is an employer with no more than 25 full-time equivalent employees (FTEs) employed during the employer's tax year, and whose employees have annual full-time equivalent wages that average no more than \$50,000. However, the full amount of the credit is available only to an employer with 10 or fewer FTEs and whose employees have average annual full-time equivalent wages from the employer of less than \$25,000. These wage limits will be indexed to the Consumer Price Index for Urban Consumers ("CPI-U") for years beginning in 2014.

For tax years beginning in 2010 through 2013, the credit will be 35% for small employers with fewer than 25 employees and average annual wages of less than \$50,000 who offer health insurance coverage to their employees. In 2014 and later, eligible small employers who purchase coverage through the Insurance Exchange will be eligible for a tax credit for two years of up to 50% of their contribution. ([Code Sec. 45R](#), as added by Health Care Act Sec. 1421, as amended by Health Care Act Sec. 10105)

Dependent coverage in employer health plans. Effective on Mar. 30, 2010 (the enactment date of the Reconciliation Act), the general exclusion for reimbursements for medical care expenses under an employer-provided accident or health plan is extended to any child of an employee who has not attained age 27 as of the end of the tax year. The Committee Report says this change is also intended to apply to the exclusion for employer-provided coverage under an accident or health plan for injuries or sickness for such a child. Also, self-employed individuals may take a deduction for any child of the taxpayer who has not attained age 27 as of the end of the tax year. ([Code Sec. 105](#), [Code Sec. 162](#), [Code Sec. 401](#), and [Code Sec. 501](#), as amended by Reconciliation Act Sec. 1004(b))

Health-Related Revenue Raisers

Excise tax on high-cost employer-sponsored health coverage. For tax years beginning after Dec. 31, 2017, a 40% nondeductible excise tax will be levied on insurance companies and plan administrators for any health coverage plan to the extent that the annual premium exceeds \$10,200 for single coverage and \$27,500 for family coverage. An additional threshold amount of \$1,650 for single coverage and \$3,450 for family coverage will apply for retired individuals age 55 and older and for plans that cover employees engaged in high risk professions.

The tax will apply to self-insured plans and plans sold in the group market, but not to plans sold in the individual market (except for coverage eligible for the deduction for self-employed individuals). Stand-alone dental and vision plans will be disregarded in applying the tax. The dollar amount thresholds will be automatically increased if the inflation rate for group medical premiums between 2010 and 2018 is higher than the Congressional Budget Office (CBO) estimates in 2010.

Employers with age and gender demographics that result in higher premiums could value the coverage provided to employees using the rates that will apply using a national risk pool.

The excise tax will be levied at the insurer level. Employers will be required to aggregate the coverage subject to the limit and issue information returns for insurers indicating the

amount subject to the excise tax. ([Code Sec. 4980I](#), as added by Health Care Act Sec. 9001, as amended by Health Care Act Sec. 10901, and as further amended by Reconciliation Act Sec. 1401)

Cost of employer sponsored health coverage included on Form W-2. For tax years beginning after Dec. 31, 2010, employers must disclose the value of the benefit provided by them for each employee's health insurance coverage on the employee's annual Form W-2. ([Code Sec. 6051\(a\)\(14\)](#), as amended by Health Care Act Sec. 9002)

Other new employer reporting responsibilities for health coverage. For calendar years beginning after 2013, insurers (including employers who self-insure) that provide minimum essential coverage to any individual during a calendar year must report the following to both the covered individual and to IRS: (1) name, address, and taxpayer identification number (TIN) of the primary insured, and name and TIN of each other individual obtaining coverage under the policy; (2) the dates during which the individual was covered under the policy during the calendar year; (3) whether the coverage is a qualified health plan offered through an exchange; (4) the amount of any premium tax credit or cost-sharing reduction received by the individual with respect to such coverage; and (5) such other information as IRS may require. To the extent coverage is through an employer-provided group health plan, the insurer also must report the name, address and employer identification number of the employer, the portion of the premium, if any, required to be paid by the employer, and any other information IRS may require to administer the new tax credit for eligible small employers (see discussion above). ([Code Sec. 6056](#), as added by, and [Code Sec. 6724](#), as amended by, Health Care Act Sec. 1514)

Additional Hospital Insurance Tax (HI) for high wage workers. For tax years beginning after Dec. 31, 2012, the HI tax rate is increased by 0.9 percentage points on an individual taxpayer earning over \$200,000 (\$250,000 for married couples filing jointly); these figures are not indexed. ([Code Sec. 1401](#) and [Code Sec. 3101](#), as amended by Health Care Act Sec. 9015, as amended by Health Care Act Sec. 10906)

Surtax on unearned income. For remuneration received, and tax years beginning after, Dec. 31, 2012, a 3.8% surtax (called the Unearned Income Medicare Contribution) will apply to net investment income of higher income taxpayers. The surtax for individuals is 3.8% of the lesser of (1) net investment income or (2) the excess of modified adjusted gross income (AGI) over the threshold amount. The threshold amount is \$250,000 for a joint return or surviving spouse, \$125,000 for a married individual filing a separate return, and \$200,000 in any other case. Modified AGI is AGI increased by the amount excluded from income as foreign earned income under [Code Sec. 911\(a\)\(1\)](#) (net of the deductions and exclusions disallowed with respect to the foreign earned income).

For an estate or trust, the surtax is 3.8% of the lesser of: (1) undistributed net investment income or (2) the excess of AGI (as defined in [Code Sec. 67\(e\)](#)) over the dollar amount at which the highest income tax bracket applicable to an estate or trust begins.

The tax does not apply to a nonresident alien or to a trust all the unexpired interests in which are devoted to charitable purposes, a trust that is exempt from tax under [Code Sec. 501](#), or a charitable remainder trust exempt from tax under [Code Sec. 664](#).

The surtax is subject to the individual estimated tax provisions and is not deductible in computing any tax imposed by subtitle A of the Code (relating to income taxes).

Net investment income for surtax purposes is interest, dividends, royalties, rents, gross income from a trade or business involving passive activities, and net gain from disposition of property (other than property held in a trade or business). Investment income is reduced by properly allocable deductions to such income to arrive at net investment income. ([Code Sec. 1411](#), as added by Reconciliation Act Sec. 1402)

New limit on health FSA contributions. For tax years beginning after Dec. 31, 2012, the amount of contributions to health flexible spending accounts (FSAs) under cafeteria plans will be limited to \$2,500 per year. The dollar amount will be inflation indexed after 2013. ([Code Sec. 125](#), as amended by Health Care Act Sec. 9005, as amended by Health Care Act Sec. 10902, and as further amended by Reconciliation Act Sec. 1403)

Restricted definition of medical expenses for employer provided coverage. For purposes of employer provided health coverage (including health reimbursement accounts (HRAs) and health flexible savings accounts (FSAs), health savings accounts (HSAs), and Archer medical savings accounts (MSAs)), the definition of medicine expenses deductible as a medical expense is generally conformed to the definition for purposes of the itemized deduction for medical expenses. But this change does not apply to doctor prescribed over-the-counter medicine. Thus, the cost of over-the-counter medicine (other than insulin or doctor prescribed medicine) cannot be reimbursed through a health FSA or HRA. In addition, the cost of over-the-counter medicines (other than insulin or doctor prescribed medicine) cannot be reimbursed on a tax-free basis through an HSA or Archer MSA. These changes for HSAs and Archer MSAs apply for amounts paid with respect to tax years beginning after Dec. 31, 2010. The changes for health FSAs and HRAs apply for expenses incurred with respect to tax years beginning after Dec. 31, 2010. ([Code Sec. 106\(f\)](#), [Code Sec. 220\(d\)\(2\)](#), and [Code Sec. 223\(d\)\(3\)](#), as amended by Health Care Act Sec. 9003)

Increased tax on nonqualifying HSA or Archer MSA distributions. For distributions made after Dec. 31, 2010, the additional tax for HSA withdrawals before age 65 that are used for purposes other than qualified medical expenses is increased from 10% to 20%, and the additional tax for Archer MSA withdrawals that are used for purposes other than qualified medical expenses is increased from 15% to 20%. ([Code Sec. 220\(f\)\(4\)\(A\)](#) and [Code Sec. 223\(f\)\(4\)\(A\)](#), as amended by Health Care Act Sec. 9004)

Modified threshold for claiming medical expense deductions. For tax years beginning after Dec. 31, 2012, the adjusted gross income (AGI) threshold for claiming the itemized deduction for medical expenses will be increased from 7.5% to 10%. However, the 7.5%-of-AGI threshold will continue to apply through 2016 to individuals age 65 and older (and their spouses). ([Code Sec. 56\(b\)\(1\)\(B\)](#), [Code Sec. 213\(a\)](#), and [Code Sec. 213\(f\)](#), as amended by Health Care Act Sec. 9004)

Deduction for employer Part D is eliminated. For tax years beginning after Dec. 31, 2012, the deduction for the subsidy for employers who maintain prescription drug plans for their Medicare Part D eligible retirees will be eliminated. (Health Care Act Sec. 9012, as amended by Reconciliation Act 1407)

Industry-specific revenue raisers. The following revenue raising changes will be imposed on health related industries:

... A new deduction limit on executive compensation applies to insurance providers. If at least 25% of the insurance provider's gross premium income is derived from health insurance plans that meet the minimum essential coverage requirements in the new health reform law ("covered health insurance provider"),

an annual \$500,000 per tax year compensation deduction limit will apply for all officers, employees, directors, and other workers or service providers performing services for or on behalf of a covered health insurance provider. The limit applies to tax years beginning after Dec. 1, 2009, with respect to services performed after that date. ([Code Sec. 162\(m\)\(6\)](#)), as amended by Health Care Act Sec. 9014)

... Pharmaceutical manufacturers and importers will have to pay an annual flat fee beginning in 2011 allocated across the industry according to market share. The annual flat fee beginning in 2011 is allocated across the industry according to market share. The schedule for the flat fee is: 2011, \$2.5 billion; 2012 to 2013, \$2.8 billion; 2014 to 2016, \$3 billion; 2017, \$4 billion; 2018, \$4.1 billion; 2019 and later, \$2.8 billion. The fee will not apply to companies with sales of branded pharmaceuticals of \$5 million or less. (Health Care Act Sec. 9008, as amended by Reconciliation Act Sec. 1404)

... For sales after Dec. 31, 2012, manufacturers or importers of medical devices will have to pay a 2.3% of the sale price is imposed on the sale of any taxable medical device by the manufacturer, producer, or importer of the device. A taxable medical device is any device, defined in section 201(h) of the Federal Food, Drug, and Cosmetic Act, intended for humans. The excise tax will not apply to eyeglasses, contact lenses, hearing aids, and any other medical device determined by IRS to be of a type that is generally purchased by the general public at retail for individual use. ([Code Sec. 4191](#)), as added by Reconciliation Act Sec. 1405)

... Health insurance providers will face an annual flat fee on the health insurance sector effective for calendar years beginning after Dec. 31, 2013. The fee will be allocated based on market share of net premiums written for a U.S. health risk for calendar years beginning after Dec. 31, 2012. The aggregate annual flat fee for the industry will be: \$8 billion for 2014; \$11.3 billion for 2015 and 2016; \$13.9 billion for 2017; and \$14.3 billion for 2018. The fee will be indexed to the rate of premium growth for later years. The fee will not apply to companies whose net premiums written are \$25 million or less. (Health Care Act Sec. 9010, as amended by Health Care Act Sec. 10905, as further amended by Reconciliation Act Sec. 1406)

... For services provided on or after July 1, 2010, a 10% excise tax applies to indoor tanning services. ([Code Sec. 5000B](#)), as added by Health Care Act Sec. 9017, as amended by Health Care Act Sec. 10907)

... For tax years beginning after Dec. 31, 2009, nonprofit Blue Cross Blue Shield organizations must maintain a medical loss ratio of 85% or higher in order to take advantage of the special tax benefits provided to them, including the deduction for 25% of claims and expenses and the 100% deduction for unearned premium reserves. ([Code Sec. 833\(c\)\(5\)](#)), as amended by Health Care Act Sec. 9016)

... Effective generally for tax years beginning after Mar. 23, 2010, new qualification requirements apply to any [Code Sec. 501\(c\)\(3\)](#) organization that operates at least one hospital facility. ([Code Sec. 501\(r\)](#) and [Code Sec. 6033\(b\)](#)), as amended by Health Care Act Secs. 9007 and 10903) Additionally, for failures occurring after Mar. 23, 2010, an excise tax of \$50,000 applies if a tax-exempt charitable hospital organization fails to meet certain new community health needs assessments requirements for any tax year. [Code Sec. 4959](#), as added Health Care Act Sec. 9007)

Non-Health Related Revenue Raisers

Corporate information reporting. For payments made after Dec. 31, 2011, businesses that pay any amount greater than \$600 during the year to corporate providers of

property and services will have to file an information report with each provider and with IRS. ([Code Sec. 6041\(h\)](#), as amended by Health Care Act Sec. 9006)

Codification of economic substance doctrine and imposition of penalties. The economic substance doctrine is a judicial doctrine that has been used by the courts to deny tax benefits when the transaction generating these tax benefits lacks economic substance. The courts have not applied the economic substance doctrine uniformly. For transactions entered into after Mar. 30, 2010 (the enactment date of the Reconciliation Act), and to underpayments, understatements, and refunds and credits attributable to transactions entered into after Mar. 30, 2010, the manner in which the economic substance doctrine should be applied by the courts is clarified and a penalty is imposed on understatements attributable to a transaction lacking economic substance. ([Code Sec. 6662](#), [Code Sec. 6662A](#), [Code Sec. 6664](#), [Code Sec. 6676](#), and [Code Sec. 7701](#), as amended by Reconciliation Act Sec. 1409)

Elimination of credit for "black liquor." A \$1.01 per gallon tax credit applies for the production of biofuel from cellulosic feedstocks in order to encourage the development of new production capacity for biofuels that are not derived from food source materials. Congress is aware that some taxpayers are seeking to claim the cellulosic biofuel tax credit for unprocessed fuels, such as "black liquor." For fuel sold or used after Dec. 31, 2009, eligibility for the tax credit under the Reconciliation Act will be limited to processed fuels (i.e., fuels that could be used in a car engine or in a home heating application). ([Code Sec. 40](#), as amended by Reconciliation Act Sec. 1408)

Estimated taxes for large corporations. The required corporate estimated tax payments factor for corporations with assets of at least \$1 billion will be increased by 15.75 percentage points for payments due in July, August, and September of 2014. ([Code Sec. 6655](#), as amended by Reconciliation Act Sec. 1410)

Other Tax Changes

Simple cafeteria plans for small businesses. For tax years beginning after 2010, a new employee benefit cafeteria plan known as a Simple Cafeteria Plan will be available. This plan will be subject to eased participation restrictions so that small businesses could provide tax-free benefits to their employees; it will include self-employed individuals as qualified employees. ([Code Sec. 125\(j\)](#), as amended by Health Care Act Sec. 9022)

Liberalized adoption credit and adoption assistance rules. For tax years beginning after Dec. 31, 2009, the adoption tax credit will be increased by \$1,000, and made refundable. The adoption assistance exclusion also will be increased by \$1,000. Both credit and exclusion are extended through 2011. (Code Sec. 23 and [Code Sec. 137](#), as amended by Health Care Act Sec. 10909)

New credit for new therapies. For expenses paid or incurred after Dec. 31, 2008, in tax years beginning after that date, a two-year temporary credit applies, subject to an overall cap of \$1 billion, to encourage investments in new therapies to prevent, diagnose, and treat acute and chronic diseases. ([Code Sec. 48D](#), as added by Health Care Act Sec. 9023)

New exclusion for certain health professionals. Payments made under any State loan repayment or loan forgiveness program that is intended to provide for the increased availability of health care services in underserved or health professional shortage areas are excluded from gross income, effective for amounts received by an individual in tax years beginning after Dec. 31, 2008. ([Code Sec. 108\(f\)](#), as amended by Health Care Act

Sec. 10908) (A separate provision excludes from gross income the value of specified Indian tribal health benefits, effective for benefits and coverage provided after Mar. 23, 2010 (the enactment date of the Health Care Act.) ([Code Sec. 139D](#), as added by Health Care Act Sec. 9021)

© 2010 Thomson Reuters/RIA. All rights reserved.