

HEALTH CARE REFORM:  
TAX-RELATED PROVISIONS FOR CORPORATIONS GENERALLY

MAY 2010

The Health Care & Corporate Groups at Murtha Cullina are pleased to provide clients and friends with information about topics of interest.

If you have questions about the issues addressed in this newsletter, or any other matters, please feel free to contact any of our attorneys listed in this newsletter.

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*This Bulletin discusses tax related provisions of the Health Care Reform Laws affecting corporations generally. A second installment discusses tax related issues pertaining to hospitals and other health care entities. Both of these publications, as well as others on the Health Care Reform Laws, are available on our website, [www.murthlaw.com](http://www.murthlaw.com).*

Big changes are coming to the health care system, courtesy of the new Health Care Reform Laws\*. These big changes need to be funded, and that means new taxes.

This Bulletin summarizes the principal new taxes and fees and the principal new tax mandates under the Health Care Reform Law. It does not address all aspects of the tax-related provisions of the Health Care Reform Law, including certain employee benefit-related provisions of the Health Care Reform Law, which are the subject of another Bulletin.

**Excise Tax on Employers Who Fail To Offer Health Insurance.** For tax years beginning in 2014, if an employer (i) had more than 50 full-time employees ("FTEs") in the preceding tax year, and (ii) employs at least one person who receives a premium assistance tax credit or cost-sharing reduction for health insurance purchased from a state exchange, and (iii) fails to offer "minimum essential coverage," it will be required to pay a monthly assessable penalty of \$166.67 (\$2,000 per year) multiplied by the number of FTEs in excess of 30. If the employer does offer "minimum essential coverage," but still has at least one employee who receives a premium tax credit or cost-sharing reduction from the government, the monthly fee is the lesser of (i) \$250 (\$3,000 per

year) per employee receiving the credit/reduction, or (ii) \$166.67 (\$2,000 per year) multiplied by the number of FTEs in excess of 30.

**Excise Tax on Uninsured Individuals.** For tax years beginning in 2014, individuals who do not maintain certain minimal health insurance coverage for themselves and their dependents will be subject to a penalty. The penalty will be included with the taxpayer's income tax return for the tax year that includes the month for which the penalty is imposed. Generally, the penalty will be fully phased in by 2016 and then will be the greater of (i) \$695 per failure, adjusted in subsequent years for inflation (the "applicable dollar amount"), but half the applicable dollar amount for individuals under the age of 18, up to 300 percent of the applicable dollar amount, or (ii) 2.5 percent of household income in excess of the threshold amount of income required for income tax filing, provided that the greater of the amount determined under (i) or (ii) must not exceed the national average premium for the newly-created "bronze level" health plans. New information returns will be required to be filed by providers of health care in order to properly determine who is subject to this new tax. Exemptions will be allowed for (i) individuals below the income tax filing threshold, (ii) individuals whose lowest cost option is still greater than eight percent of their adjusted gross income

("AGI"), (iii) members of recognized religious sects, (iv) de minimis lapses in coverage, (v) members of Indian tribes, and (vi) other hardship situations.

**Premium Assistance Tax Credits.** For tax years beginning in 2014, there is a sliding scale refundable tax credit for individuals and families with household income between 100 percent to 400 percent of the federal poverty level who purchase certain health insurance through a state exchange because either they were (i) not offered "minimum essential coverage," (ii) offered only "unaffordable" coverage by their employer, or (iii) offered coverage by their employer where the plan's share of the cost of the benefits provided is less than 60 percent of the total. Generally the refundable tax credit will be based on the percentage of income that the cost of the premium of the newly-created "silver plan" represents to the taxpayer.

**Small Business Tax Credits.** Generally for tax years beginning in 2010, employers with (i) average annual wages of \$25,000 or less, and (ii) 10 or less FTEs will commonly be eligible for a tax credit up to 35 percent of their contributions to their employees' health care premiums for the years 2010 to 2013. For years after 2013, the employer generally will be eligible for a tax credit of up to 50 percent of its contributions, but only for the first two years in which it purchases its health insurance coverage through its state exchange. The credits will be available at a reduced rate for (i) employers with average annual wages between \$25,000 and \$50,000, and (ii) employers with between 10 and 25 FTEs. The credit will be part of the general business tax credit. Organizations that are exempt from tax under Section 501(c) of the Internal Revenue Code also will be eligible for the credits (at reduced rates) which can be offset against payroll taxes.

**Therapeutic Project Tax Credit.** Companies with fewer than 250 employees are eligible for a tax credit for qualified investments made in acute and chronic disease research during 2009 or 2010. The credit equals 50 percent of the qualified investment. The Department of the Treasury, in consultation with the Department of Health and Human Services, will award certifications of eligibility for this credit.

**Excise Tax on High Cost Insurance.** For tax years beginning in 2018, a 40 percent excise tax will be imposed on the cost of each employee's "employer-sponsored health coverage" that exceeds a threshold amount (generally \$10,200 for individuals and \$27,500 for families). Such tax will be imposed on the issuers of the health insurance. The foregoing thresholds, which do not include certain coverages such as long term care and separate dental and vision care, are tentatively set for 2018. The thresholds may be increased under specified circumstances and after 2018 the thresholds will be subject to an annual cost-of-

living adjustment. The employer or the plan sponsor of a multi-employer plan will be required to make the excess benefit calculations for each employee and then notify the coverage provider and the Secretary of the Treasury. Penalties will apply for reporting failures.

**Annual Fees on Manufacturers and Importers of Branded Drugs and Health Insurance Providers.** Beginning in 2011, manufacturers and importers of branded drugs must pay an annual fee, allocated by market share, in the amount of \$2.5 billion to \$4.1 billion (depending on the year). Beginning in 2014, health insurance providers must pay an annual fee, allocated by market share, in the amount of \$8 billion to \$14.3 billion (depending on the year).

**Fees on Health Plans.** A fee is imposed on each specified health insurance policy. The fee is equal to \$2 (\$1 in policy years ending during fiscal year 2013) multiplied by the average number of lives covered under the policy. The issuer of the policy is liable for payment of the fee. A similar fee is imposed on self-insured health plans, equal to \$2 (\$1 in policy years ending during fiscal year 2013) multiplied by the average number of lives covered under the plan. For any policy year beginning after Sept. 30, 2014, the dollar amount is equal to the sum of the dollar amount for policy years ending in the preceding fiscal year plus an amount equal to the product of (1) the dollar amount for policy years ending in the preceding fiscal year, multiplied by (2) the percentage increase in the most recent projected per capita amount of national health expenditures. The fee is effective with respect to policies and plans for portions of policy or plan years beginning on or after October 1, 2012.

**Additional Medicare Tax on Wages and Self-Employment Income.** For tax years beginning after December 31, 2012, an additional 0.9 percent Medicare tax is imposed on the wages and self-employment income of taxpayers with wages or self-employment income in excess of \$200,000 for individuals, 250,000 for joint filers, and \$125,000 for a married taxpayer filing separately. The additional Medicare tax is excluded from self-employment taxes for purposes of calculating the deduction from AGI of one-half of self-employment taxes.

**New Medicare Tax on Unearned Income.** For tax years beginning in 2013, individuals will be subject to a new 3.8 percent Medicare tax on the lesser of (i) net investment income, or (ii) modified adjusted gross income ("MAGI") in excess of a threshold amount. The threshold amount is \$200,000 for single taxpayers, \$250,000 for joint filers, and \$125,000 for a married taxpayer filing separately. Net investment income generally consists of: (i) gross income from interest, dividends, annuities, royalties, and rents, other than such income which is derived in the ordinary course of a trade or business that is not described in (ii),

(ii) other gross income derived from a passive trade or business or the business of trading in financing instruments or commodities, and (iii) net gain (to the extent taken into account in computing taxable income) attributable to the disposition of property other than property held in a trade or business not described in (ii), net of allowable deductions which are properly allocable to such gross income or net gain. MAGI means adjusted gross income increased by the taxpayer's otherwise excludable foreign earned income. Estates and trusts (with certain exceptions) also will be subject to the tax using a slightly different formula.

**Excise Tax on Sales of Medical Devices.** Beginning in 2013, a 2.3 percent excise tax will be assessed on the sales price of any taxable medical device sold by a manufacturer, producer or importer. Exclusions will apply for devices, such as eye glasses, contact lenses and hearing aids, generally sold to the public at retail for individual use.

**Excise Tax on Indoor Tanning.** Effective for services performed on or after July 1, 2010, a tax equal to 10 percent of the amount paid for tanning services will be assessed on customers.

**Limitation on Itemized Deduction for Medical Expenses.** For taxable years beginning in 2013, the threshold for deducting unreimbursed medical expenses on Schedule A is increased to 10 percent of a taxpayer's adjusted gross income from 7.5 percent. However, through 2016, taxpayers over the age of 65 and their spouses are excepted from this change.

**Elimination of Deduction for Federal Prescription Drug Subsidies.** For taxable years beginning in 2013, sponsors of qualified retiree prescription drug plans that receive tax-free Medicare Part D subsidy payment will be prohibited from deducting the costs reimbursed by such subsidy for federal income tax purposes.

**Exclusion From Gross Income of Forgiveness of Certain Student Loans.** In addition to repayments under the National Health Service Corps Loan Program and State repayment programs under the Public Health Service Act, repayments under other State loan repayment or forgiveness programs that are intended to provide for the increased availability of health care services in underserved or health professional shortage areas (as determined by the State) are also excluded from gross income for tax years beginning after 2008.

**Modification of Tax Treatment of Blue Cross, Blue Shield and Other Qualifying Health Insurance Organizations.** The special deduction that Blue Cross and Blue Shield organizations and other qualifying health insurance organizations are allowed under Section 833 of the Internal Revenue Code is modified to provide that these

organizations will only be entitled to the special tax treatment if 85 percent or more of their insurance premium revenues are spent on clinical services.

**W-2 Reporting.** Effective for tax years beginning after December 31, 2010, employers are required to report on Form W-2 the aggregated cost of health coverage (determined on a basis similar to that under COBRA) received by an employee under the employer's health plan, excluding FSAs, HRAs and Archer medical savings accounts from the cost analysis.

**Reporting Requirements Relating to Health Insurance Coverage Information.** Insurers (including employers who self-insure) that provide minimum essential coverage to any individual during a calendar year are required to report certain health insurance coverage information to both the covered individual and to the IRS. The information required to be reported includes: (1) the name, address and taxpayer identification number of the primary insured, and the name and taxpayer identification number 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 the Secretary of the Treasury may require. This requirement is effective for calendar years beginning after 2013.

**Increased Information Reporting for Payments to Corporations.** Effective for payments made in taxable years beginning after December 31, 2011, any person engaged in a trade or business who makes a payment to a corporation (other than a corporation that is tax-exempt under Section 501(a) of the Internal Revenue Code) of \$600 per year or more in exchange for either property or services is required to file an information return with the IRS and the corporation.

**Liberalized Adoption Credit and Assistance Rules.** For tax years beginning in 2010, the adoption tax credit is increased by \$1,000 to \$13,170, made refundable, and extended through 2011. The exclusion for employer provided adoption assistance is also increased to \$13,170.

**Certain Estimated Tax Payments of Large Corporations Increased.** The estimated tax payment required to be made in July, August, or September of 2014 by a corporation with assets of \$1 billion or more (determined as of the end of the preceding tax year) has been increased by an additional 15.75 percent from the amount otherwise due. The next required installment of estimated tax is reduced accordingly to reflect the increase.

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**Cellulosic Biofuel Producer Credit.** For fuels sold after December 31, 2009, a cellulosic biofuel eligible for the cellulosic biofuel producer credit is defined to exclude any fuel if: (1) more than four percent of it, by weight, is any combination of water and sediment, or (2) its ash content is more than one percent by weight. This will exclude “black liquor” from qualifying for the credit.

### **Codification of Economic Substance Doctrine and New Penalties.**

Effective for transactions entered into after March 23, 2010, to be protected from a re-characterization in which tax benefits are not recognized for federal tax purposes, a transaction entered into by an individual in connection with a trade or business or an activity engaged in for the production of income must: (i) change the taxpayer’s economic position in a meaningful way (apart from federal, state and local tax effects), and (ii) have a substantial purpose (apart from federal, state and local tax effects). Transactions lacking economic substance are added to the list of situations to which the 20 percent accuracy-related underpayment penalty applies and such penalty is increased to 40 percent if the relevant facts affecting the tax treatment are not adequately disclosed. Reasonable cause defenses to the imposition of the penalty are not permitted.

\*The President signed the Patient Protection and Affordable Care Act into law on March 23, 2010 and the Health Care and Education Reconciliation Act into law on March 30, 2010 (collectively, the “Health Care Reform Law”).

*IRS Circular 230 Notice: To ensure compliance with requirements imposed by the Internal Revenue Service, you are hereby advised that nothing contained in this communication is intended to be used, nor can it be used, for either the purpose of avoiding penalties under the Internal Revenue Code or the purpose of promoting, marketing or recommending to another party any transaction or matter addressed herein.*