



## 2010 Health Care Reform

For owners of small businesses and their workers, the newly enacted 2010 Health Care Act and the 2010 Reconciliation Act has some key provisions regarding tax credits, excise taxes, and penalties. Whether a business will be affected by them depends on a variety of factors, such as the number of employees and the amount of compensation your employees earn.

**Tax credits to certain small employers that provide health insurance.** The new law provides small employers with a tax credit (i.e., a dollar-for-dollar reduction in tax) for nonelective contributions to purchase health insurance for their employees. The credit can offset an employer's regular tax and its alternative minimum tax (AMT) liability.

*Small business employers eligible for the credit.* To qualify, a business must offer health insurance to its employees as part of their compensation and contribute at least half the total premium cost. The business must have no more than 25 full-time equivalent employees ("FTEs"), and the employees must 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.

*Years the credit is available.* The credit is initially available for any tax year beginning in 2010, 2011, 2012, or 2013. For tax years beginning after 2013, the credit is only available to an eligible small employer that purchases health insurance coverage for its employees through a state exchange and is only available for two years.

*Calculating the amount of the credit.* For tax years beginning in 2010, 2011, 2012, or 2013, the credit is generally 35% (50% for tax years beginning after 2013) of the employer's nonelective contributions toward the employees' health insurance premiums. The credit phases out as firm-size and average wages increase.

*Special rules.* The employer is entitled to a business expense deduction equal to the amount of the employer contribution minus the dollar amount of the credit. For example, if an eligible small employer pays 100% of the cost of its employees' health insurance coverage and the amount of the tax credit is 35% of that cost, the employer can claim a deduction for the other 65% of the premium cost.

Self-employed individuals, including partners and sole proprietors, 2% shareholders of an S corporation, and 5% owners of the employer are not treated as employees for purposes of this credit. The credit is not available for a domestic employee of a sole proprietor. There is also a special rule to prevent sole proprietorships from receiving the credit for the owner and their family members.

**Most small businesses exempted from penalties for not offering coverage to their employees.** Although the new law imposes penalties on certain businesses for not providing coverage to their employees (so-called "pay or play"), most small businesses won't have to worry about this provision because employers with fewer than 50 employees aren't subject to the "pay or play" penalty. For businesses with at least 50 employees, the possible penalties vary depending on whether or not the employer offers health insurance to its employees. If it does not offer coverage and it has at least one full-time employee who receives a premium tax

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credit, the business will be assessed a fee of \$2,000 per full-time employee, excluding the first 30 employees from the assessment. So, for example, an employer with 51 employees who doesn't offer health insurance to his employees will be subject to a penalty of \$42,000 (\$2,000 multiplied by 21). Employers with at least 50 employees that offer coverage but have at least one full-time employee receiving a premium tax credit will pay \$3,000 for each employee receiving a premium credit (capped at the amount of the penalty that the employer would have been assessed for a failure to provide coverage, or \$2,000 multiplied by the number of its full-time employees in excess of 30). These provisions take effect Jan. 1, 2014.

**The "Cadillac tax" on high-cost health plans.** The new law places an excise tax on high-cost employer-sponsored health coverage (often referred to as "Cadillac" health plans). This is a 40% excise tax on insurance companies, based on premiums that exceed certain amounts.

**Medicare tax hike.** Beginning in 2013, the Act imposes an additional 0.9 percent Medicare Hospital Insurance tax (HI tax) on self-employed individuals and employees with respect to earnings and wages received during the year in excess of \$200,000. If an individual or employee files a joint return, then the tax applies to all earnings and wages in excess of \$250,000 on that return.

For wage earners, the Act requires the employer to withhold the employee's tax from wages paid to the employee in excess of \$200,000.

**Unearned income Medicare contribution.** Unearned income such as interest, dividends, capital gains, annuities, royalties, and rents are subject to Medicare tax at a rate of 3.8%. The tax is applied against the lesser of the taxpayer's net investment income or modified adjusted gross income in excess of \$200,000 for single filers and \$250,000 for joint filers.

### **Miscellaneous Updates**

#### **Employer's reporting of health insurance coverage on Forms W-2 is optional for 2011**

IRS has announced that employers won't have to report the aggregate cost of employer-sponsored group health plan coverage on Forms W-2 issued for 2011. Reporting for 2011 will be optional. IRS anticipates issuing guidance on this reporting requirement before the end of this year.

In addition, IRS announced that it has issued a draft Form W-2 for 2011. The draft Form W-2 includes the codes that employers may use to report the cost of coverage under an employer-sponsored group health plan. IRS will be publishing guidance on the new requirement later this year. IRS stresses that the amounts reportable are not taxable, and that the new reporting requirement is intended to be informational only and to provide employees with greater transparency into overall health care costs.

The intent of this writing is to give you an overview of the provisions in the new law with the biggest impact on small business. Nobody knows if parts of this law will be repealed or modified, but this overview is of the law as it stands today. Many aspects of this law do not take place for a few years.

Please call our offices to discuss how the new changes may affect your specific business.

Sincerely,

Leverone & Associates