



North Carolina Law Life

Health Care Reform: Changing Employer Plans and Taxes

By: Donna Ray Chmura. *This was posted Wednesday, September 8th, 2010*

[John Vandenhoff](#) continues his exploration of the tax implications of the new health care law. There's also more in a series of [informational podcasts](#) on the Web site of the Law Firm Alliance, of which we are a member.

In our [previous posts](#), we briefly talked about the new [Healthcare legislation](#) which was signed into law (H.R. 4872 the Healthcare and Education Reconciliation Act of 2010 (Reconciliation Act, P.L. 101-152)) (the "Healthcare Act") and described a number of the major individual mandates contained within that Act.

We continue to present a brief overview of some of the key tax changes affecting individuals and businesses in the Healthcare Act. Please call our offices for details of how the new changes may affect your specific situation.

New for Employer-Provided Plans

The Healthcare Act requires certain changes so that in any [employer-provided health insurance plan](#), the child of any covered employee may be included in coverage until such child reaches age 27, even if the child cannot be claimed as a dependent of the employee on the employee's federal tax return. The same change is also effective for health insurance plans of self employed individuals (effective March 30, 2010, a self-employed individual may take a "for adjusted gross income" deduction of health insurance premiums where the insurance covers the self-employed individual, the individual's spouse, the individual's dependants, and the individual's children who have not attained age 27).

The Healthcare Act further requires that group health plans that cover dependant children must continue to make dependant coverage available for an adult child until the child reaches age 26. Although there is no requirement for a plan or issuer to provide health insurance coverage for anyone, including dependants, if coverage is provided for dependant children then, under the Healthcare Act, the coverage must continue until the child turns 26. (Note that it is unclear why this provision applies to children under age 26 and other provisions described above apply to children under age 27.)

Health Savings Plans Affected

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The Healthcare Act makes several significant changes to certain health savings plans, including [health savings accounts](#) (“HSA”), health flexible spending arrangements (“FSA”), health reimbursement arrangements (“HRA”), Archer or medical savings account (“MSA”) and other qualified employer health plans. Current law generally allows participants of these plans to set aside funds, pretax, which will be used to reimburse them for certain healthcare expenses. Presently, reimbursement for over-the-counter medicines and drugs have been very liberal (even over-the-counter aspirins and cough medicine would qualify). The Healthcare Act provides that for amounts paid in tax years beginning December 3, 2010, the allowable medicines for reimbursement will be more restricted. Unless a prescription from a doctor is acquired for over-the-counter medicines, only payments for prescribed drugs and insulin will be eligible for reimbursement.

Another significant change regarding health FSAs is that the amount a participant may set aside per year will be restricted. Currently, there is no statutory restriction as to how much an participant may set aside in a health FSA and such amount is usually limited only by the employer. Effective for tax years beginning after 2012, an employee may only set aside \$2,500.00 per year in an FSA. For taxpayers who have been setting aside amounts greater than \$2,500.00, this will effectively result in a lost deduction and an increase in tax (regardless as to the taxpayer’s current taxable income).

Due to the Healthcare Act there also will be additional reporting required of most businesses. For all payments made after 2011 by any person engaged in a trade or business (a “Payor”) an information return must be filed for all payments made totaling \$600.00 or more in a calendar year to a single payee (other than a payee that is tax exempt). Also, payments to corporations, except those made for medical or healthcare services, are not required to be reported on an information return.

Paying for the Healthcare Act

In another effort to raise money to assist in paying for the expense of increasing federal payments under Healthcare Act, individuals will find it harder to deduct medical expenses. Under current law, a taxpayer may only deduct medical expenses to the extent all such expenses incurred during a single year exceed 7.5% of the taxpayer’s adjusted gross income. Starting in 2013, the Healthcare Act generally increases the threshold for claiming an itemized deduction for unreimbursed medical expenses from 7.5% of adjusted gross income to 10% of adjusted gross income.

Beginning in tax years after 2013, a penalty will be assessed against most individuals who did not have minimum essential health coverage for a month. The penalty will be paid with an individual’s income tax return and be based upon a percentage of household income in excess of a threshold amount. The penalty will be lower in 2014 and gradually increase until 2016, when the penalty will generally be 1/12 of the greater of (i) \$695.00 per uninsured adult; or (ii) 2.5% of the household income in excess of the threshold amount of income required for filing a return.

Our [Virginia and North Carolina tax lawyers](#) are helping clients wrestle with these and other changes that proceed from the Healthcare Act. If you have questions or comments, please post them below and we will try to respond.

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