

Individual taxes: Health care reform's impact

By James P. Sacher, CPA, Skoda Minotti

Last month, *CPA Voice* examined the effects of health care reform on businesses. This month, we'll take a closer look at the tax effects on individuals due to passage of the Patient Protection and Affordable Care Act.

Unless otherwise noted, the provisions described below become active after 2013.

Health insurance required

The Act makes health insurance mandatory and assigns a penalty to individuals not in compliance. The penalty is the greater of \$95 (growing to \$695 in 2016) or 2.5% of household income over the income threshold for tax filing.

There are exceptions to the requirements, including:

- Financial hardship
- Those without coverage for less than three months
- Those for whom the lowest plan option is greater than 85% of household income
- Those below the tax filing threshold (\$9,350 single / \$18,700 couples in 2010)

To help low and middle income individuals and families meet this requirement, tax credits will be available to individuals and families with income up to 400% of the federal poverty level (\$43,320 for individual and \$88,200 for family) and who are not otherwise eligible for Medicaid or employer health insurance.

The amount of the credit awarded is based on a sliding scale of an individual's household income and the cost of the insurance. To receive the credit, the individual provides the information to their State Insurance Exchange, which in turn certifies the person. The IRS then pays the credit amount directly to the insurance plan in which the individual is enrolled. For employed individuals who purchase through an exchange, premium payments are made through payroll deductions

Higher Medicare taxes

Singles with an adjusted gross income (AGI) greater than \$200,000 and couples with an AGI greater than \$250,000 will be the hardest hit by the new bill.

Current law imposes a Medicare tax on earned income at 2.9% (1.45% paid each

by employee and employer) without a limit. Under the new law, higher income taxpayers will pay an additional 0.9% Medicare tax (2.35% total) on earned income in excess of the limits stated above. Employers will not be affected by the new tax, but must collect through withholdings.

As this tax is collected through withholdings, couples earning less than \$200,000 individually, but greater than \$250,000 collectively need to be aware of a possible extra burden at tax filing time. For example, if a couple were each earning \$170,000 per year, both would only have the traditional 1.45% withheld from their pay checks. At tax filing time, however, because their joint income totaled \$340,000, the couple would be responsible for paying the additional .9% Medicare tax on the income earned over \$250,000. In this case, that results in an additional \$810 ($\$90,000 \times .9\%$) tax liability.

Additionally, under the new law, the Medicare tax is now extended to net investment income for the high income taxpayers above the thresholds described above. The amount is 3.8% (1.45% + 1.45% + .9%). This is all paid by the employee.

The following is considered net investment income:

- Interest
- Dividends
- Royalties
- Rents
- Passive activity income and gain from disposition of property (capital gains)

This income may be reduced by any properly allocable deductions. It does not include income from tax deferred retirement accounts and it applies only to the \$200,000/\$250,000 thresholds described above. For example, if the couple described above (AGI of \$340,000) has \$50,000 in capital gains income, it would be taxable at the 3.8% rate for an additional tax liability of \$1,900. This is effective after 2012.

Other provisions to consider

Medical expense deductions

The floor on medical expense deductions is raised from 7.5% of AGI to 10% of AGI for years after 2012.

Over-the-counter medication

Over-the-counter medications from HSAs, HRAs, FSAs, and MSAs are no longer eligible for reimbursement for years after 2010.

Non-qualified distributions

There is an increase in penalties on non-qualified distributions from HSAs and MSAs to 20% of the disbursed amount for years after 2010.

Flexible spending accounts

The amount contributed to FSAs will be limited to \$2,500 for years beginning after 2012.

Employees' children

The exclusion from income of reimbursements for medical care under an employer sponsored health plan is extended to children of employees up to age 27. This also includes the exclusion for employer provided coverage and is effective March 31. ♥

James P. Sacher, CPA is a partner with Skoda Minotti and leads the firm's health care practice. He provides tax and business consulting services to a variety of businesses including physician practices, hospital based physician groups and hospitals.

New 1099 requirement means (a lot) more paperwork on the way

Who would have thought that just a few lines of a bill that is over 2,000 pages could be so important? Well, that indeed is the case with Section 9006 of the new health care bill.

Section 9006 now requires that, beginning in 2012, all companies will have to issue 1099 tax forms not just to contract workers, but also to any individual or corporation from which they buy more than \$600 in goods or services in a tax year.

So in other words, that \$800 laptop that you bought for your small business at Best Buy? You now have to send Best Buy a 1099 for the purchase.

This seemingly small change will result in literally millions of new required tax documents issued by both large and small companies each year. So why is the change being made? Basically, the thinking is that the use of the 1099 forms will generate more government revenue and help offset the cost of the health bill.

Before everyone gets too worked up, keep in mind that the final impact of the law won't be known until the IRS issues its regulations on the new law. The IRS has not yet commented on when it will release regulations or schedule public hearings, but these are not expected to arrive until sometime next year.



TAKEAWAYS

The Patient Protection and Affordable Care Act contained many changes impacting individuals, including:

- ▶ Health insurance is mandatory for individuals, though there are exceptions and credits to help people.
- ▶ Singles with an Adjusted Gross Income (AGI) greater than \$200,000 and couples with an AGI greater than \$250,000 will face higher Medicare taxes.

Other changes impact:

- ▶ Medical expense deductions
- ▶ Over the counter medication deductions
- ▶ Non-qualified distributions
- ▶ Flexible spending accounts
- ▶ Age of allowable dependents

1099 Requirement: Beginning in 2012, all companies will have to issue 1099 tax forms not just to contract workers, but to any individual or corporation from which they buy more than \$600 in goods or services in a tax year.

LEARN MORE

WEBINAR

Individual Tax Update

This webinar with Rex Decker, CPA, JD, MBA covers the latest developments in individual taxation along with related analysis and planning strategies. Expand your professional network and gain insight on a range of tax topics with these sessions designed specifically for our members with an interest in tax. Course 80312WB

TELECONFERENCE

Not-for-Profit Accounting, Auditing and Tax Update

Not-for-profit organizations of all sizes are finding that they are subject to more oversight and regulation than ever before.

Our panel of experts will provide you with what you need to know about the latest and most important developments affecting non-profit organizations. They will provide a thorough review of the latest developments affecting tax and GAAP issues for these specialized entities.

FOR MORE INFORMATION on this and other CPE programs, visit www.ohioscpa.com or call CPAnswers at 888.959.1212.