

## Making Sense of the New Health Care Law

By Ryan Craner

ON MARCH 23, 2010, H.R. 3590—The Patient Protection and Affordable Care Act was signed into law. Regardless of which “side of the aisle” you’re on, you have to admit that this has been a wild ride through white-hot debate and unprecedented political maneuvering. As the smoke clears, we find ourselves with 2,700+ pages of legislation that very few fully understand, leaving the majority of Americans confused and overwhelmed.

Many of my clients have expressed deep concerns about the Health Care Bill—*“How will it affect us? What will happen to our tax rates? What about our existing health insurance, Medicare and future health care? What exactly will happen this year, next year and going forward? What should we be doing to prepare for all of this?”*

While I certainly understand your concerns, confusion and fears, let me help put your minds at ease. First of all, I don’t want this article to be about “politics.” I have my own personal views on the health care bill and so do you. What I want to focus on is the amazing resilience,

ingenuity, and capacity of the American people to work through these challenges. We’ve been through major changes like this before—the introduction of Social Security, Medicare and other programs. Many said these programs would be the financial ruin of America. But somehow, we made it through and continued to prosper. Regardless of how this finally turns out, I believe we will all find a way to get through it and continue progressing.

Now, let’s talk about what this Health Care Bill is and how it might affect us going forward. First, at 2,700+ pages, we simply don’t know all the details—it will take quite some time to make sense of it all. Second, no one knows if the bill as it stands today will remain in force. Already there are numerous State Attorneys General challenging the constitutionality of this legislation. I fully expect this challenge to go all the way to the Supreme Court. No one knows how this will turn out. At a minimum, there will likely be court-mandated revisions. And third, there is serious talk about rescinding the bill. Much of this



Ryan Craner  
President

will depend on the November elections and future political contests. The bottom line is, all of this is very uncertain and unstable. So let’s not form all sorts of ironclad opinions or get ourselves in a panic over something that has yet to be firmed and settled.

For the time being, (and this could easily change), here are some of the basics we have received from the government, the mainstream media and the analysts—

### PROJECTED “SHORT-TERM” BENEFITS

One aspect of the Health Care Bill that is cause for some confusion is that there are benefits, mechanisms and stipulations that don’t kick in for many years—in some cases, 2020 and beyond. Here are some of the “short-term” benefits we could see in the next few years:

- 1. Small Business Tax Credits**—Offers tax credits to small businesses to make employee coverage more affordable. Tax credits of up to 35 percent of premiums will be immediately available to firms that choose to offer coverage. Effective beginning for calendar year 2010. (Beginning in 2014, the small business tax credits will cover 50 percent of premiums.)
- 2. Begins to Close the Medicare Part D “Donut Hole”**—Provides a \$250 rebate to Medicare beneficiaries who hit the “donut hole” in 2010. Under Medicare Part D, once someone reaches \$2,830 in total drug costs, they drop into the “donut hole” and have to pay the full cost of prescription drugs until the total out-of-pocket cost reaches \$4,550. Then drug plans pick up the cost again. Beginning in 2011, the Health Care Bill institutes a 50% discount on brand-name drugs in the donut hole; also completely closes the donut hole by 2020.
- 3. Free Preventative Care Under Medicare**—Eliminates co-payments for preventive services and exempts preventive services from deductibles under the Medicare program. Effective beginning January 1, 2011.

4. **Help for Early Retirees**—Creates a temporary re-insurance program (until the Exchanges are available) to help offset the costs of expensive health claims for employers that provide health benefits for retirees age 55–64. Effective 90 days after enactment.
5. **Ends Rescissions**—Bans health plans from dropping people from coverage when they get sick. Effective 6 months after enactment.
6. **No Discrimination Against Children with Pre-Existing Conditions**— Prohibits health plans from denying coverage to children with pre-existing conditions. Effective 6 months after enactment. (Beginning in 2014, this prohibition would apply to all persons.)
7. **Bans Lifetime Limits on Coverage**—Prohibits health plans from placing lifetime caps on coverage. Effective 6 months after enactment.
8. **Bans Restrictive Annual Limits on Coverage**—Tightly restricts new plans’ use of annual limits to ensure access to needed care. These tight restrictions will be defined by HHS. Effective 6 months after enactment. (Beginning in 2014, the use of any annual limits would be prohibited for all plans.)
9. **Extended Coverage for Young Adults**—The cut-off age for young adults to continue to be covered by their parents’ health insurance rises to age 27.
10. **New High-Risk Pool**—If you are refused coverage because of your health, you can get insurance from a new high-risk pool. The pool will be established within six months and will operate until 2014, when insurance companies can no longer refuse applicants with pre-existing health problems. Annual out-of-pocket medical costs will be capped at \$5,950 for individuals and \$11,900 for families.

## INCREASED TAXES

Of course, one of the biggest concerns my clients have is “*Who is going to pay for this new health care plan?*” and “*How will it affect my taxes?*” While there are a host of taxes that will be levied against corporations and organizations, I am only listing a summary of some of the mandated tax increases that will affect individuals and families.

1. **Medicare Tax on Investment Income**—For the first time, beginning in 2013, the Medicare payroll tax will be applied to investment income. A new 3.8 percent tax will be imposed on interest, dividends, capital gains and other investment income for individuals making more than \$200,000 a year and couples making more than \$250,000.
2. **Medicare Tax Increase on Wages**—The bill also increases the Medicare payroll tax by 0.9 percentage point to 2.35 percent on wages above \$200,000 for individuals and \$250,000 for married couples filing jointly.
3. **Increased Tax on Health Savings Accounts**—The law increases the tax from 10 percent to 20 percent for non-medical early withdrawals from a health savings account for those under the age of 65. This measure takes effect in 2011.
4. **Cap on Medical Expense Deductions**—Now, medical expenses that exceed 7.5 percent of a person’s adjusted gross income can be deducted for tax purposes. But the new law raises that deduction threshold to 10 percent of adjusted gross income, meaning fewer tax deductions for someone with high medical costs. This provision starts in 2013.
5. **Penalty Tax**—All legal U.S. residents must purchase a government-approved health insurance plan beginning in 2014. Generally, a single person making \$30,000 or more will have to pay a 2.5 percent penalty if they do not carry health insurance. A person making less than \$30,000 will have to pay \$695.
6. **Cadillac Tax**—Effective in 2013, a 40 percent excise tax will be imposed on the excess benefit provided under high value health insurance plans (known as “Cadillac plans”). These are plans that have annual premium payments of more than \$8,500 for individuals and \$23,000 for families. The excise tax will be charged to insurance companies or to employers in the case of self-insured plans. However, the costs are expected to be passed on to consumers.

Implementation of the excise tax is delayed until 2018 under the Reconciliation Act, and the thresholds increase to \$10,200 for individuals and \$27,500 for families.

**6. Tanning Excise Tax**—A 10-percent excise tax on anyone using indoor tanning salons.



## POTENTIAL TAX-REDUCTION STRATEGIES

If, and I emphasize the word “if,” the new health care law remains exactly as it is today, and the increased taxes take effect, what kinds of strategies can you implement to protect yourself?

**Medicare Tax on “Investment Income” starting 2013**—If you report more than \$200,000 (single); \$250,000 (married) annual investment income, then you should consider a “deferral strategy”—deferring as much capital gains and dividend income as possible. Deferring helps you take control and decide when you take the income and pay the tax. You may also want to consider restructuring your non-IRA investments to be owned by a Family Partnership or similar legal structure where the income generated may not be recognized as “investment income” to you.

**Medicare Tax Increase on Wages**—If you earn above \$200,000 (single); \$250,000 (married) in annual wages, you should consider an “AGI reduction strategy”—reducing your Adjusted Gross Income to a lower level in order

to legally avoid the higher tax. You can reduce AGI by increasing contributions to various types of retirement plans such as a 401k or Deferred Comp.

**Health Savings Plans**—Starting in 2011, if you have an HSA, in order to avoid the new tax, you should seriously consider other alternatives in place of the HSA.

**Reinsurance Program**—If you plan to retire, or are already retired, and under age 64, we should analyze the new temporary “re-insurance program” available to employers that have retirees between the ages of 55 and 64. We want to see what possible additional benefits your employer may be willing to pay under this new program.

**Medical Expense Deductions**—Starting in 2013, carefully review your medical expense deductions. If you are close to the new 10% threshold, you should carefully document all medical expenses and look for legitimate ways to reduce your reportable Adjusted Gross Income in order to clear the new higher 10% threshold for deduction. You may also consider having costly “planned” medical procedures performed prior to 2013.

**New Tax Credits for Small Business Owners**—If you are a small business owner, we should explore your options on employee health plans to see if the tax credits starting in 2010 will be applicable and beneficial to you.

**Cadillac Tax**—The strategy for this tax increase is very much “wait-and-see.” We fully expect insurance companies and employers to cut benefits to comply. The bill was originally slated to begin in 2013, but then a sketchy amendment moved that date to 2018, and expanded the thresholds. The final language did not contain exemptions for unions, which many believe will be adjusted. Also, a big part of the taxes to be raised to make the new law viable, were expected to come from the Cadillac Tax, so the 2018 date will likely not hold. So, be ready for either big cuts in health care benefits, or a very expensive excise tax of 40%.

**Excise Tax on Tanning Salons**—and finally, to add a little humor to a serious subject—stock up on bottles of “spray-on tan” or set up a tanning area in your backyard. That way you can stay out of the tanning salons and avoid the government’s “tanning tax”!

**Important Note:** Please keep in mind that the details of the new health care law are “in flux”—many aspects could change. Also remember that the tax-reduction strategies I have listed are “potential strategies.” As the new law becomes more defined, we need to analyze your specific situation and select strategies suited to your personal circumstances. Then, with the help of your qualified tax advisor, we can arrive at a sensible and accurate plan of action.

In the coming months and years, as the new health care law defines itself politically and legally, I will strive to keep you informed. ■

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