

In connection with Congressional efforts to repeal and replace the Affordable Care Act (ACA), the House Ways and Means Committee marked up and adopted March 8 and 9 budget reconciliation legislative recommendations relating to repeal of the net investment income tax, the tanning tax and certain “consumer taxes,” and the repeal and replace of certain health-related tax policy provisions. The changes, if enacted, would affect individual taxes and business taxes relating to healthcare plans, and taxes and fees enacted to finance the ACA.

The legislation provides, beginning in 2020, an income-based refundable tax credit for insurance coverage for Americans who do not have employer-sponsored healthcare plans. The credit would replace the current system for helping Americans to purchase health insurance.

The most costly provisions in the tax-related legislation are likely to be the refundable credit, the repeal of the net investment income tax and the repeal of the annual fee on health insurance providers. Provisions eliminating tax benefits for healthcare plans that pay for abortions are likely to attract attention.

As expected, the proposed legislation met with strong opposition from Democrats. The Ways and Means Committee voted down or determined as non-germane a variety of amendments from Democrats. Some conservative Republicans had attacked the provisions and other ACA reform provisions that are being considered by the Energy and Commerce Committee as being “Obamacare-lite” and not going far enough. Nevertheless, Ways and Means Committee approved the recommendations.

Summary of Changes

The House Ways and Means Committee approved the following changes:

Repeal of Special Taxes

- Repeal the 3.8% tax on net investment income for taxable years beginning after 2017.
- Repeal the tanning tax on services performed after 2017.
- Repeal the annual fee on branded prescription pharmaceutical manufacturers and importers, effective for calendar years beginning 2017.
- Repeal the annual fee on health insurance providers effective for calendar years beginning after 2016.
- Make permanent the suspension of the medical device excise tax.
- Repeal the additional 0.9% Medicare tax imposed on wages and self-employment income above certain thresholds, effective with taxable years beginning after 2017.

Repeal and Deferral of Penalty Taxes

- Set at zero (i.e., effectively repeal) the maximum amount of assessable penalties for failure to comply with the employer mandate for large employers, effective for months beginning after 2015.
- Defer the so-called “Cadillac tax” on high cost employer-sponsored health insurance plans so that the tax would first be effective for taxable periods beginning after 2024 rather than taxable periods beginning after 2019.
- Repeal the penalty tax for failure to maintain minimum essential coverage, effective for months beginning after 2015.

Changes to Tax Credits

- Repeal the small business tax credit under Internal Revenue Code section 45R for an eligible small employer for up to 50% of the employer’s nonelective contributions to purchase health insurance for its employees. The repeal generally would be effective for taxable years beginning after 2019. However, the repeal would apply for taxable years beginning after 2017 to credits with respect to plans that provide coverage with respect to abortion.
- Substantially restructure the refundable tax credit for health insurance (as described below), effective for months beginning after 2019.
- Modify and repeal the premium tax credit (as described below), effective in stages beginning in taxable years beginning after 2017.

Rule Changes for HSAs, MSAs, HRAs and FSAs

- Change the definition of qualified medical care for purposes of the exclusions for reimbursements for medical care under employer-provided accident and health insurance plans and for distributions from Health Savings Accounts (HSAs) and Archer MSAs used for qualified medical expenses to include over-the-counter medication not prescribed by a physician. Thus, for example, amounts distributed to pay for over-the-counter allergy medicines will be excluded from income. The provision would be effective, in the case of HSAs and MSAs, for amounts paid with respect to taxable years beginning after 2017 and, in the case of health flexible spending arrangements (FSAs) and Health Reimbursement Arrangements (HRAs), expenses incurred with respect to taxable years beginning after 2017.
- Reduce the additional tax on HSA distributions not used for qualified medical expenses from 20% to 10% and the additional tax on Archer MSA distributions not used for qualified medical expenses from 20% to 10%, in both cases effective for distributions made after 2017.

- Repeal the limitation on salary reduction contributions to health FSAs, effective for taxable years beginning after 2017.
- Allow the annual contribution limit that can be divided between spouses to include catch-up contributions of both spouses to HSAs in certain cases, effective for taxable years beginning after 2017.
- Treat an HSA as having been established on the date that an individual's coverage under a high deductible health plan begins if the taxpayer establishes the HSA within the 60-day period beginning on the date that an individual's coverage under a high deductible health plan begins.

Rules Affecting Other Tax Deductions

- Not take into account the exclusion for qualified retiree prescription drug plan subsidy payments in determining whether a deduction is allowed with respect to retiree prescription drug costs taken into account in determining the subsidy payment from HHS, thereby allowing a taxpayer to claim a deduction for covered retiree prescription drug expenses even if the taxpayer excludes from income qualified retiree prescription drug plan subsidies received from HHS with respect to the expenses, effective for taxable years beginning after 2017.
- Extend through 2017 the reduced 7.5% (10% for alternative minimum tax) of adjusted gross income threshold for taxpayers who have attained the age of 65.
- Permanently lower the percentage of adjusted gross income threshold for regular and minimum tax purposes for all taxpayers to 7.5%, effective for taxable years beginning after 2017.
- Increase the basic limit on aggregate HSA contributions for a year to equal the maximum on the sum of the annual deductible and out-of-pocket expenses permitted under high deductible health plans (US\$6,550 for self-only coverage and US\$13,100 for family coverage in 2017), effective for taxable years beginning after 2017.
- Repeal the US\$500,000 cap on tax deductions for compensation of individuals performing services for covered insurance providers, effective for taxable years beginning after 2017.

Modification of the Premium Tax Credit

The legislation would repeal the present-law provision that limits the additional tax liability resulting from excess advance premiums in the case of individuals with household income below 400% of the FPL.

Under the legislation, the premium assistance credit would be available with respect to catastrophic-only qualified health plans and health plans that otherwise meet the requirements relating to qualified health plans, except that they are not offered through the Health Benefit Exchange if requirements for eligibility are otherwise met. The premium assistance credit would not be available for qualified health plans that include coverage for abortions, other than an abortion necessary to save a life of the mother or a pregnancy resulting from rape or incest.

The legislation revises the schedule under which an individual's or family's share of premiums is determined in applying the credit for 2019. The schedule varies with household income and with the age of the individual or family members. The legislation repeals the premium assistance credit with respect to coverage months beginning after 2019.

Refundable Tax Credit

The legislation establishes a refundable tax credit with respect to eligible health insurance for individuals and their qualifying family members for eligible coverage months. Qualifying family members are the individual's spouse, in the case of a joint return, a dependent and a child who has not attained age 27 as of the end of the taxable year and is covered for the month by the same health insurance plan as the individual or the individual's spouse.

Advance payments with respect to the credit may be made during the year directly to the insurer, as discussed below. Alternatively, individuals may choose to pay their total health insurance premiums without advance payments and claim the credit at the end of the taxable year.

An individual will be eligible for a credit if the individual is covered by eligible health insurance, is not eligible for other specified coverage, is a citizen or national of the US or a qualified alien, and is not incarcerated, other than incarceration pending the disposition of charges. Eligible health insurance is health insurance coverage that is offered in the individual market within a state or is unsubsidized COBRA continuation coverage, substantially all of such coverage is not of excepted benefits, and that does not include coverage relating to abortions, other than an abortion necessary to save the life of the mother or an abortion with respect to a pregnancy that is the result of an act of rape or incest.

Other specified coverage is (1) coverage under a group health plan, other than COBRA continuation coverage or coverage under a plan substantially all of the coverage of which is of excepted benefits; (2) Part A Medicare coverage; (3) Medicaid coverage; (4) coverage under the Children's Health Insurance Plan (CHIP); (5) military-related medical coverage, including coverage under the TRICARE program; (6) coverage under a veterans healthcare program, as determined by the Secretary of Veterans Affairs, in coordination with the Secretary of Health and Human Services and the Secretary of the Treasury; (7) coverage under a health plan for Peace Corps volunteers; or (8) coverage under the Nonappropriated Fund Health Benefits Program of the Department of Defense.

The monthly credit amount applicable with respect to an individual is 1/12 of an annual amount that varies with the age of the individual. Credits increase from US\$2,000 per year for individuals under age 30 to US\$4,000 per year for individuals who have attained the age of 60. In general, the monthly credit amount for a family is the sum of the monthly credit amounts applicable with respect to the five oldest family members with respect to whom monthly credit amounts are available, up to a cap of US\$14,000 per year. The credit amount otherwise determined for a taxable year under this rule is reduced by 10% of the excess of the individual's modified adjusted gross income for the taxable year in excess of US\$75,000 (or US\$150,000 in the case of a joint return).

The total credit for a year cannot exceed the amount paid for eligible health insurance for the individual and qualifying family members eligible for coverage in months beginning during the year. If the amount paid for the insurance is less than the maximum credit amount described above and the individual or a qualifying family member is eligible to contribute to an HSA for the year, the excess amount may be deposited into an HSA.

The legislation includes reporting requirements and a penalty of 25% of the amount of a refund or credit claimed in excess of the amount allowable.

Revenue Effect

The Joint Committee on Taxation estimated that some of the changes would result in a 10-year revenue loss of more than US\$593 billion. This estimate does not include revenue provisions relating to premium tax credits, the small business tax credit, the individual mandate, the employer mandate or the refundable healthcare credit for health insurance coverage. Those estimates will be included in a Congressional Budget Office estimate.

Contacts

George Schutzer

Partner, Washington

T +1 202 457 5273

E george.schutzer@squirepb.com

Matthew Cutts

Partner, Washington

T +1 202 457 6079

E matthew.cutts@squirepb.com

Brandon Roman

Associate, Washington

T +1 202 457 5330

E brandon.roman@squirepb.com

Beth Goldstein

Associate, Washington

T +1 202 475 5129

E beth.goldstein@squirepb.com

The contents of this update are not intended to serve as legal advice related to individual situations or as legal opinions concerning such situations, nor should they be considered a substitute for taking legal advice.

© Squire Patton Boggs.

All Rights Reserved 2017