FINANCES | MONEY | TAXES

Health Reform Changes Affecting Small Business

There are some great provisions in the new law... but the drawbacks could end up causing a loss of jobs.

by **Sandy Botkin**

1597 words | 5 pages

"Don't tax him. Don't tax me. Tax the guy behind the tree." ~attributed to Former Congressman Rostenkowski

Owners of small businesses and their workers could be severely impacted by the recently enacted health reform legislation. Some key provisions related to tax credits, new excise taxes, penalties, and some higher taxes, all of which depend on a number of factors such as number of full time employees in the business, average incomes of the employees, etc. This article will provide you an overview of its significance to self employed taxpayers who have less than ten full time employees.

Generally, the present Obama administration and Congress have noted that the new health reform proposals will provide better insurance for small businesses at a lower cost, which will create more jobs. However, there are also a lot of strongly negative feelings among the business community. Let me present some of the provisions so that you can judge for yourself and plan accordingly.

Benefits to small businesses: Despite the negative press about the law there really are some positive changes that will affect small businesses.

1. Small Business Exchanges: Small business will be able to pool their resources in state exchanges called "Shop Exchanges" in order to buy insurance. Normally these exchanges apply to companies who have less than 100 employees by 2014; however, states have the option to limit access to these exchanges for companies of fewer than 50 full time employees. Premium expectations are expected to reduce overall insurance costs by 1-

4% per year for each employee, which is a very good provision under this plan.

2. Tax Credits for certain small employers who provide insurance. Generally, if you have fewer than 50 full-time employees, you don't have to provide health insurance for your workers. However, if you do provide insurance, you might be eligible for a yummy tax credit, which is a dollar-for-dollar reduction in your taxes.

   To be eligible for this credit, you have to have less than 25 full-time employees whose annual average earnings (not counting the owner) of no more than $50,000. For companies of 10 or fewer employees, you would be eligible for a 35% tax credit (which goes up to 50% after 2013) in later years, if your average full time equivalent wages are less than $25,000 per year. This credit began in 2010 and goes until 2014. There is a second phase of the credit that small business would get up to 2016. Thus, qualifying small businesses can get this credit for up to six years.

   Sandy's elaboration: This credit sounds great, but having it apply to small businesses (of no more than 10 full-time workers) and who average under $25,000 of wages will substantially reduce its applicability to most businesses. Estimates are that this will benefit about 7% of self employed businesses.

3. No more lifetime caps: For most health insurance, there is a $2,000,000 lifetime cap for usage. Starting immediately, these caps are to be removed. This could allow coverage for a number of small business folks who might have exceeded the cap.

4. No pre-existing conditions: Starting in 2014, there will bot be any pre-existing conditions. Thus, even if you have a major medical problem, you will be guaranteed to get health insurance. This is a great provision that will allow coverage for those small business folks and their employees who might not have been able to get insurance coverage.

5. Dependent children can be kept on parent's insurance until turning age 26: Normally, kids who turn age 21 have to get their own insurance and can't be kept on their parent's insurance. This will be changed so that dependent children who are under age 26 can be kept on the parent's insurance. This became effective on March 30, 2010. I should note that although dependents under

age 26 can be added to the parent's insurance e policy, there is no requirement that an employer add them to the policy.

6. Small Businesses are exempt from penalties for failing to provide health insurance: Generally only companies that have 50 or more full-time employees need to provide health insurance coverage or face penalties. However, since small businesses of fewer than 50 full-time employees don't need to provide any coverage, they are exempt from the “Pay or Play” penalties.

   Sandy's elaboration: If you have a business with 50 or more full-time employees, you are indeed required to provide health insurance.

   As you can see, there are some good provisions for both the business owner and for the small businesses. Thus, why the strongly negative comments from the business community? The reason is that there are a lot of congressional “gotchas” that affect everyone.

Problems with the health reform legislation

1. *New taxes:* There are a number of new taxes and costs that will beef up the overall insurance costs for small businesses. For example, there is an income tax increase starting in 2010 of between 5-10% for those who make over $200,000 of adjusted gross income. In addition, Medicare has been increased for everyone by .9% for all employees and for the owners who make over $200,000 of adjusted gross income and is single. Married taxpayers filing joint returns have to make a $250,000 adjusted gross earnings in order for this .9% Medicare surcharge to kick in. This may not sound like a lot, but for someone earning $300,000 in salary, this could result in a $900 increase in Medicare taxes for each employee in that income bracket regardless of profitability of the business! In addition, if the adjusted gross income of the worker or the owner is over $200,000 (for single taxpayers) or over $250,000 (for married filing joint taxpayers), there will be a 3.8% Medicare surcharge on all of their interest, dividends, rents and royalties. This will also apply to dividends from S Corporations. So much for saving costs!

2. *New excise taxes:* In order to help pay for this new law, there are some additional excise taxes on many medical devices that

ordinarily aren't purchased by most people. Thus, there will be no excise taxes on glasses, hearing aids, and contact lenses. Most other devices, however, will probably have the excise taxes apply to them. In addition, there will be additional taxes on the health insurance companies, some insurance plans and pharmaceutical companies. You might wonder how these additional taxes apply to self employed taxpayers. The reason is that these additional costs will be passed through to everyone including the self employed.

3. *Additional 40% excise tax on "Cadillac" health insurance plans:* The new law places a whopping 40% excise tax on high-cost employer-sponsored health coverage, often referred to as "Cadillac" health plans. This tax applies to premiums that exceed $10,200 for single coverage and those that exceed $27,500 for family coverage. There are some increased thresholds for retired taxpayers who are age 55 and older and for those engaged in "high risk occupations." Thus, if you want top notch expensive insurance coverage, you will pay a lot more to get it. This even assumes that an insurance company will even offer it at all.

4. *Increased paperwork*: Generally those who do provide insurance through the exchange for their workers will need to fill out some potentially new paperwork showing the name of the employee, the amount of premium paid, the contribution by the employee, notification to the employee about the coverage, etc.

5. *Midsize to large companies must provide health insurance:* If you have a company consisting of 50 or more full-time employees (part time will be counted on a fractional basis depending on their hours), you are required to provide medical insurance or face big penalties. However, this is required regardless of profitability. Think about this. This could result in a number of unprofitable or marginally profitable companies going broke, which could actually substantially reduce jobs. In addition, this would spur either the hiring of more part time at the cost of reducing the number of full-time employees or increase the sucking sound of companies going to places like China or India. The result of all this would mean a lot less jobs.

Bottom Line: Although there are some great provisions in the new law such as waiving pre-existing conditions and lifetime benefit caps, the increased taxes and costs incurred for most small businesses will probably exceed the decrease in health premiums resulting in an overall

increase in total health costs and taxes to self employed businesses. Thus, I don't see any job creation resulting from this law. In fact, it may well cost a lot of jobs.

Sandy Botkin is a CPA, attorney and former trainer of IRS attorneys nationwide. Sandy's book, *Lower Your Taxes Big Time!,* is the best-selling tax book at Amazon.com. He lectures all over the nation on tax planning for self-employed and corporate taxpayers... he's been written up in Newsweek and many other magazines. He is also a syndicated writer and noted author of this famed tape series *"Tax Strategies for Business Professionals"* and *"Tax and Financial Strategies for Residential Real Estate."* To find out more about Sandy and his products, visit his website with our affiliate link here: www.TaxReductionInstitute.com or e-mail Sandy at: info@taxreductioninstitute.com. Or, call at (800) TRI-0-TAX (800-874-0829 or (301) 972-3600.