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Potential Tax Implications of Healthcare Reform

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by Monica Coakley and Lori Robbins, Washington National Tax*

President Trump has said that healthcare reform and tax reform are two of his administration's highest priorities, and congressional Republicans have echoed this sentiment. The exact timing and contours of these reforms are far from certain—but what is clear is that the two are not mutually exclusive. It is a near-certainty that healthcare reform legislation (if enacted) would include significant tax law changes—changes that would affect individuals, the healthcare industry, and the business community at large.

In January 2017, Congress passed a budget resolution that sets the stage for a future budget reconciliation bill to be the vehicle for repealing certain (but not all) provisions of the Affordable Care Act ("ACA"), most notably the tax provisions. Since then, however, there has been significant debate over the mechanics to be used to effect healthcare reform, including whether "repeal and replace" should be done in multiple stages of legislation or presented simultaneously. More than a dozen legislative healthcare reform proposals have been introduced during the first two months of the 115th Congress. Most recently, sources leaked a discussion draft of legislative text for a budget reconciliation bill to repeal and replace key provisions of the ACA. There are many unanswered questions about this leaked draft, including whether it can garner sufficient support of congressional Republicans and the president, and whether some of its provisions exceed the limited scope permitted for a budget reconciliation bill. Debate is likely to continue for some time and, accordingly, no one knows today exactly what the tax law provisions of healthcare reform legislation ultimately will look like.

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* Monica Coakley is the principal-in-charge of the Healthcare group of Washington National Tax ("WNT"). Lori Robbins is a tax managing director in the WNT Healthcare group.

To illustrate some of the possibilities, this article includes an appendix with a table to summarize the tax provisions of some of the more visible healthcare reform proposals to date.

There are three principal ways that tax law could potentially intersect with healthcare reform:

- Repeal of the taxes and fees under the ACA
- Enactment of healthcare-related tax expenditures as part of a reform package
- Enactment of revenue-raising tax provisions as part of a reform package

Each of these can have different effects on the healthcare industry and on taxpayers generally.

Repeal of ACA Taxes and Fees

A complete repeal of the ACA at first blush might seem to not be politically feasible because Senate Republicans would not have the votes needed by themselves to block a filibuster. They could, however, have sufficient votes to pass legislation in the form of a budget reconciliation bill without any Democratic support. Budget reconciliation is a legislative tool that may only be used to enact (or repeal) legislation related to taxes and spending. Through this mechanism, the Republicans could enact legislation by a simple majority vote to dismantle key provisions of the ACA—specifically, the tax law provisions of the ACA. This limited repeal could be given immediate effect or could contain delayed effective dates.

In early February 2017, both chairs of the congressional tax-writing committees (Rep. Kevin Brady of the House Ways & Means Committee and Sen. Orrin Hatch of the Senate Finance Committee) separately stated that all ACA taxes and fees must be repealed. It is unclear whether they were referring to a complete repeal of all tax law provisions of the ACA (including ones that do not directly impose a tax such as the section 162(m)(6)[1] compensation deduction limitation on covered health insurance providers) or merely those provisions that affirmatively impose tax on a particular group of individuals or entities (such as the medical device excise tax).

Many of the tax provisions of the ACA are industry-specific levies, but not all. The ACA includes tax provisions that affect employers (such as the excise tax on high-cost employer-sponsored health plans commonly referred to as the “Cadillac” tax), individuals (such as the Medicare surtax), and taxpayers generally (such as the codification of the economic substance doctrine).

The tax provisions of the ACA, potentially subject to repeal, include:

- Health insurance premium assistance tax credits
- Small business health insurance tax credits

[1] Unless otherwise indicated, section references are to the Internal Revenue Code of 1986, as amended (the “Code”) or the applicable regulations promulgated pursuant to the Code (the “regulations”).

- Penalty tax to enforce the individual mandate
- Penalty tax to enforce the employer mandate
- Section 501(r) requirements and excise taxes on tax-exempt hospitals
- Annual fee on health insurance providers
- Section 162(m)(6) compensation deduction limitation
- Limitations on the tax benefits to Blue Cross Blue Shield organizations
- Medical device excise tax
- Branded prescription drug fee
- “Cadillac tax” on high-cost employer sponsored health plans
- Modified threshold for itemized medical expense deduction
- Tax on indoor tanning
- Net investment income tax
- Medicare surtax
- Codification of the economic substance doctrine
- Various information reporting requirements

Despite the rhetoric about repealing "all" ACA taxes and fees, most of the current healthcare reform proposals would repeal some—but not all—of these tax provisions.

Enactment of New Healthcare-Related Tax Expenditures

Healthcare policy is often implemented through tax law. Some of these tax law provisions are intended to penalize conduct that lawmakers deemed undesirable. For example, the ACA imposes penalty taxes on individuals who fail to purchase health insurance and large employers that fail to offer health insurance to their employees.

On the other hand, some tax law provisions are enacted to provide benefits to an activity or group of taxpayers that Congress, for policy reasons, wanted to favor. These tax breaks are sometimes referred to as “tax expenditures,” because they are, in effect, a form of government spending. An example of a tax expenditure is the home mortgage interest deduction, which advances the policy objective of encouraging home ownership.

There are a number of healthcare-related tax expenditures, many of which pre-date the ACA. The single-largest tax expenditure in the United States is the income and payroll tax exclusion for employer-provided health insurance. Other healthcare-related tax expenditures include the itemized deduction for medical expenses (to the extent these expenses exceed a certain percentage of income), favorable tax

treatment for amounts deposited into health savings accounts ("HSAs"), medical savings accounts, and flexible savings accounts. The ACA introduced additional tax expenditures, the largest one being the subsidies for health insurance purchased on the individual exchanges.

Most of the recent healthcare reform proposals have included new tax expenditures—most notably in the expanded use of HSAs and the introduction of new healthcare-related tax credits and deductions for individuals. Examples of these proposals are included in the summary table in the Appendix to this article. It remains to be seen what tax expenditures will be included in the final healthcare reform legislation.

Enactment of Revenue Raisers

When Congress embarks on new legislation, how that legislation will affect the deficit is generally considered. If legislation is projected to increase the federal deficit (due to either an increase in federal spending or a decrease in tax revenue, or both), Congress may include offsets in the form of spending cuts or new sources of revenue to minimize the negative impact on the deficit. Such "revenue raisers" frequently take the form of tax law changes that raise or impose new taxes, or decrease existing tax benefits.

The ACA, when enacted, had a slightly positive revenue effect, but dismantling all or part of it is likely to affect the budget deficit in some way. Accordingly, some recent healthcare reform proposals include revenue raisers. One notable revenue raiser that has appeared in several healthcare reform proposals is a repeal of (or limitation on) the exclusion from income and payroll tax for employer-provided health insurance. If enacted, this tax law change could have a significant impact on both individuals and employers.

ACA taxes and fees were significant revenue raisers that were used to pay for premium tax credits and other subsidies provided for under that law. A complete repeal of the ACA taxes and fees would make it difficult for Congress to pay for any new healthcare spending or tax expenditures (such as the health insurance tax credits or deductions that have been proposed in the legislation summarized in the Appendix), unless new taxes are imposed or certain income exclusions or deductions are eliminated. Modifying the exclusion for employer-provided health insurance may appear in the final healthcare reform legislation, but any number of tax law changes—potentially having nothing to do with healthcare—are also possible. This is one area where all taxpayers—including those having no connection to the healthcare industry—could be impacted by healthcare reform and should stay alert as the legislative efforts proceed.

Enactment of Comprehensive Tax Reform

Comprehensive tax reform is another priority for President Trump and the Republicans in Congress. Enactment of tax reform legislation is by no means certain—and a detailed discussion of current tax reform proposals is beyond the scope of this article—but it is important for members of the healthcare industry to be alert to the potential implications of tax reform, as these would be in addition to the tax implications of healthcare reform.

The tax reform proposal currently receiving the most attention is contained in the "Better Way" document published by the House Republican Tax Reform Task Force in June 2016 (generally referred to as the "Blueprint"). Business tax provisions contained in the Blueprint include (but are not limited to):

- lower corporate tax rates;
- immediate expensing of investments in tangible and intangible assets (other than land);
- elimination of the tax deduction for net interest expense; and
- movement to a destination-based tax system that taxes imports and exempts exports (generally referred to as border adjustability).

For taxable healthcare organizations, the net effect of these proposals may be positive or negative, depending on each company's particular facts and circumstances, including whether the company is highly leveraged, whether it is in a net operating loss position, whether it has foreign operations, the extent of its capital expenditures, and the structure of its supply chain. Lower tax rates and immediate expensing of capital expenditures are generally favorable changes, but they might not offset the detriment of lost interest deductions and the increased cost of imported equipment and supplies for some taxpayers, for example. Under the Blueprint proposal, some healthcare companies would be "winners" and some would be "losers."

The Blueprint's approach to comprehensive tax reform does not specifically affect tax-exempt organizations. However, even if the basic treatment of tax-exempt organizations remains unchanged, comprehensive tax reform will still affect many tax-exempt organizations. For example, changes to the corporate tax system will directly affect the treatment of taxable subsidiaries and activities subject to unrelated business income tax. Border adjustability may affect the supply chain and pricing for medical supplies, equipment, pharmaceuticals, and other purchases. Reduced income tax rates could impact the market for tax-exempt bonds, and limitations on the itemized deductions, which includes the charitable contribution deduction, could influence funding for certain organizations.

Conclusion

There is currently a great deal of uncertainty around the substance, timing, and potential effective dates for both healthcare reform and tax reform. However, it is not too soon for companies to consider the potential impact of current proposals under their particular facts and circumstances, identify possible areas of concern, and develop strategies for monitoring and reacting to ongoing legislative developments.

Healthcare Reform Proposals
A Tax Comparison

The table below compares key tax provisions of several recent healthcare reform proposals. This table does not address the non-tax provisions in these proposals, nor does it present all outstanding legislative proposals.

It is important to note that it is unclear which, if any, of these proposals Congress ultimately might adopt. There is currently a great deal of uncertainty around the substance, timing and effective date of legislative actions, including whether healthcare reform will occur in stages (e.g., a "repeal" bill followed later by a "replace" bill vs. a comprehensive legislative package).

	A Better Way: Our Vision for a Confident America, 2016	Empowering Patients First Act, 2015 (H.R. 2300)	American Health Care Reform Act, 2017 (H.R. 277)	Patient Freedom Act, 2017 (S. 191)	Obamacare Replacement Act, 2017 (S. 222)
Introduced by	House Speaker Paul Ryan	Dr. Tom Price (now HHS Secretary)	Rep. David Roe	Sen. Bill Cassidy	Sen. Rand Paul
Date introduced	Better Way: Jun. 22, 2016 Policy Brief: Feb. 16, 2017 Legislative text has not yet been introduced.	May 13, 2015	Jan. 4, 2017	Jan. 23, 2017	Jan. 24, 2017
Summary	This high-level House Republican plan would repeal the ACA, provide refundable tax credits to purchase health insurance, expand HSAs, and	This legislation was introduced by current HHS Secretary Dr. Tom Price when he was a member of Congress. It would repeal the ACA,	Championed by the Republican Study Committee, this bill was the first comprehensive "repeal and replace" legislation introduced during the 115th Congress. This	This legislation would repeal Title I of the ACA and allow each state to choose from three options: 1) maintain the ACA model using subsidies and insurance	This legislation, which has been endorsed by the House Freedom Caucus, would repeal portions of the ACA but would retain premium tax credits and cost sharing subsidies. It would also provide a tax

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	add certain measures to improve health insurance access and consumer choice. House Republicans recently presented a similar proposal in the "Obamacare Repeal and Replace Policy Brief." Legislative text has not yet been introduced.	replacing it with refundable tax credits to purchase health insurance, expanded HSAs and federal funds for state high-risk pools. This bill was introduced during the 114th Congress and would have to be reintroduced to be considered by the 115th Congress.	legislation would repeal the ACA, provide individuals with a standard "above the line" tax deduction for health insurance, expand HSAs, and add certain measures to improve health insurance access and consumer choice.	exchanges to provide insurance coverage; 2) enact a market-based option that would deposit subsidies in new Roth HSAs; or 3) design its own health system without federal funds.	deduction for health insurance premiums, expand HSAs, and add certain measures to improve health insurance access and consumer choice.
Tax Provisions for Employers					
Employer mandate	Repeal	Repeal	Repeal	Repeal, but states may choose to reimpose	Repeal
Information reporting (section 6056)	Not addressed	Repeal, but reporting would be required by modifications to section 6051	Repeal, but reporting would be required by modifications to section 6051	Not addressed	Not addressed
Cadillac Tax	Likely to be repealed	Repeal	Repeal	Unchanged	Unchanged

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Small business healthcare tax credit	Not addressed	Retained but modified	Repeal	Unchanged	Unchanged
Tax Provisions for Individuals					
Individual mandate	Repeal	Repeal	Repeal	Repeal, but states may choose to reimpose	Repeal
Premium tax credits for individuals	Yes, refundable and advanceable	Yes, refundable and advanceable	No	Yes, refundable and advanceable under market-based option	Only for payroll taxes attributable to health insurance premiums
Increased threshold for medical expense deductions	Repeal	Repeal	Repeal	Unchanged	Unchanged
Medicare surtax	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Net investment income tax	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Statutory limit on FSA contributions	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Tax exclusion for employer-provided health insurance	Capped	Capped at $8,000 ($20,000 for family coverage)	Repeal	Unchanged	Unchanged
Deduction for health insurance premiums	No	No	Yes	No	Yes
Expanded availability of HSAs	No	No	No	No	Yes

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beyond high deductible plans					
Expanded limits for HSAs	Yes ($6,550 for self-only and $13,100 for family coverage)	Yes (up to maximum allowable IRA contribution)	Yes (deductible plus out-of-pocket limit, capped at $5,000 for self-only and $10,000 for family coverage)	Yes ($5,000 per individual in new Roth HSAs; $6,000 if 55 or older)	Yes (unlimited, with a $5,000 tax credit for an individual's contributions up to that amount)
Healthcare Industry Tax Provisions					
Section 501(r)	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Branded prescription drug fee	Repeal	Repeal	Repeal	Unchanged	Unchanged
Medical device excise tax	Repeal	Repeal	Repeal	Unchanged	Unchanged
Health insurer fee	Repeal	Repeal	Repeal	Unchanged	Unchanged
Blue Cross Blue Shield medical loss ratio requirement	Not addressed	Repeal	Repeal	Unchanged	Repeal
Section 162(m)(6)	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Information reporting by insurers (section 6055)	Not addressed	Repeal, but reporting would be required under new section 6050X	Repeal, but reporting would be required under new section 6050X	Not addressed	Not addressed
Patient-Centered Outcomes Reinsurance Trust Fund Fee	Not addressed	Repeal	Repeal	Unchanged	Unchanged

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Section 501(c)(29) CO-OPs	Likely to be repealed	Repeal	Repeal	Unchanged	Unchanged
Modified tax treatment of retiree drug subsidies to plan sponsors	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Other Tax Provisions					
Indoor tanning tax	Not addressed	Repeal	Repeal	Unchanged	Unchanged
Codification of the economic substance doctrine	Not addressed	Repeal	Repeal	Unchanged	Unchanged