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Business Tax Provisions of the Health Care Reform Act

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The Health Care and Education Reconciliation Act of 2010, amending the Patient Protection and Affordable Care Act (collectively the Health Care Reform Act), was signed into law on March 30, 2010. The Health Care Reform Act contains a number of significant tax provisions affecting business entities and individuals. This client alert summarizes the key business tax provisions of the Health Care Reform Act. The tax provisions affecting individuals are summarized in our companion client alert “Individual Tax Provisions of the Health Care Reform Act,” which is available by clicking [here](#).

General Tax Increases

Penalty Tax on Certain Large Employers that Fail to Offer Qualifying Health Insurance Coverage

Employers with an average of 50 or more full-time employees during the taxable year may be subject to a penalty tax if any employee is enrolled in health insurance coverage purchased through a State exchange with respect to which a premium tax credit or cost-sharing reduction is allowed or paid to the employee.

The penalty tax is assessed on a monthly basis and is not deductible for U.S. federal income tax purposes. The amount of the tax is \$2,000 per full-time employee if the employer does not offer qualifying coverage. If the employer offers coverage but has employees who receive a premium tax credit or cost-sharing reduction, the penalty is the lower of \$3,000 annually per full-time employee receiving a federal subsidy (\$250 per month) or \$2,000 annually per full-time employee. In each case, the \$2,000 per-employee penalty is determined only with respect to the number of full-time employees in excess of 30. The tax will be indexed for inflation.

This provision is effective for months beginning after December 31, 2013.



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Excise Tax on High-Value Health Plans

Health insurance issuers with “high-value” health plans will be subject to a nondeductible excise tax. Plans are deemed to be high value if annual premiums exceed a minimum threshold, generally \$10,200 for individual coverage and \$27,500 for family coverage. The thresholds are slightly higher for plans in which the majority of employees covered by the plan are engaged in certain high-risk professions, such as construction, mining, or law enforcement. The threshold is also adjusted for age, gender, and demographics of the employer’s workforce.

The excise tax is equal to 40 percent of the excess of (i) the aggregate premiums for health insurance coverage (whether paid by the employer or the employee) plus employee contributions to Health Flexible Spending Accounts (FSAs) for the taxable year plus employer contributions to Health Savings Accounts (HSAs) and Health Reimbursement Arrangements (HRAs) or Archer Medical Savings Accounts (Archer MSAs) over (ii) the dollar amount of the applicable threshold. Stand-alone dental and vision plans, long-term care benefits, and accident and disability insurance are excluded from the tax.

The tax will be imposed on the issuer of the high value plan. In the case of an employer that self-insures, however, the tax will be imposed on the plan administrator, which could be the employer itself or an insurance company administering the plan.

This provision is effective for taxable years beginning after December 31, 2017.

Repeal of Deduction for Medicare Part D Subsidies

Amounts attributable to the Medicare Part D subsidy received from the Federal government by sponsors of qualifying retiree prescription drug plans will no longer be deductible. In general, the subsidy is calculated as 28 percent of the qualifying retiree costs paid by the plan sponsor within certain ranges. This subsidy, which is not includible in the plan sponsor’s gross income, was made tax deductible under prior law to provide an additional incentive to employers to provide retiree drug coverage. Under the Health Care Reform Act, the amount otherwise allowable as a deduction for retiree prescription drug expenses must be reduced by the amount of the subsidy payments received.

This provision is effective for taxable years beginning after December 31, 2012.

Increased Estimated Tax Payments for Large Corporations

Calendar-year corporate taxpayers with assets of at least \$1 billion during 2014 are required to increase the amount of their estimated tax payments due in July, August and September 2014 by 15.75 percentage points.

This provision is effective as of March 30, 2010.



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Additional Reporting Obligations

Additional Form 1099 Reporting

Businesses generally will be required to file information returns for all payments aggregating \$600 or more during the calendar year to a single payee, including corporations (other than a payee that is a tax-exempt organization). The payments to be reported include amounts paid in consideration for property or services. However, this provision does not change the reporting rules applicable to payments of interest or dividends or the reporting rules that generally apply with respect to securities or broker transactions.

This provision is effective for payments made after December 31, 2011.

Additional Form W-2 Reporting

Employers will be required to report on each employee's annual Form W-2 the value of the employee's health insurance coverage provided by the employer. Employers must include the value of all employer-sponsored plans in which the employee enrolls, including medical insurance, dental, and vision coverage. The value of the employer-sponsored plan is calculated using the rules for COBRA coverage.

This provision is effective for taxable years beginning after December 31, 2010.

Minimum Essential Coverage Reporting Requirement

Insurers (including employers that self-insure) that provide minimum essential coverage to any individual during a calendar year will be required to report (by January 31 of the following year) certain health insurance coverage information to both the covered individual and to the Internal Revenue Service (the Service). Insurers failing to comply with these new reporting requirements will be subject to the penalties for failure to file an information return and failure to furnish payee statements.

This provision is effective for calendar years beginning after 2013.

Tax Credits and Other Subsidies

Small Business Credits

A tax credit is provided to offset the cost of employer-provided coverage to employers with 25 or fewer employees with average annual wages of less than \$50,000. The credit is a non-refundable general business credit. The employer is also entitled to a deduction equal to the amount of the employer contribution less the dollar amount of the credit.

For 2010 through 2013, the credit is equal to up to 35 percent of the aggregate amount of nonelective contributions made by the employer on behalf of its employees during the taxable year for premiums for qualified health insurance. For this purpose, qualified health insurance is health insurance coverage purchased from an insurance company licensed under State law. For taxable years after December 31, 2013, the maximum credit increases to 50 percent but is only available to a qualified small employer that



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purchases health insurance coverage for its employees through a State exchange and is only available for a maximum coverage period of two consecutive taxable years (not including taxable years beginning in years before 2014). The 35-percent and 50-percent credits are reduced for employers with between 10 and 25 employees and for employers with average annual wages per employee between \$25,000 and \$50,000.

This provision is effective for amounts paid or incurred in taxable years beginning after December 31, 2009.

Reinsurance of Early Retiree Plans

Under a reinsurance program that will be developed by the Department of Health and Human Services, an employer may receive a payment (subject to a limit of \$90,000) equal to 80 percent of its costs incurred in excess of \$15,000 for providing health insurance coverage to early retirees who are at least 55 but not yet eligible for Medicare. Payments received by an eligible employer under this reinsurance program are not includible in the employer's gross income.

This provision is effective for the period beginning on the date the program is established and ending on January 1, 2014.

Health Care Industry Tax Provisions

Health Insurance Provider User Tax

Health insurers providing coverage for a United States health risk will be required to pay an annual fee based on their relative share of the value of net premiums written with respect to health insurance for any United States health risk and third-party administration fees. A United States health risk means the health risk of an individual who is a United States citizen, a United States resident under § 7701(b)(1)(A), or located in the United States.

Each insurer must report net premiums written and third-party administration agreement fees for each calendar year to the Secretary of the Treasury. The Treasury Department (Treasury) will then calculate the insurer's share of the total fee based on its share of the market. The fee must be paid by September 30 of each year. The fee calculation is subject to certain minimum thresholds both in relation to net premiums and administration fees.

The fee will be treated as an excise tax with respect to which only civil actions for refunds under the Internal Revenue Code of 1986, as amended (the Code) will apply. The fee is not deductible. Exemptions are provided for, among others, governmental entities, some non-profit enterprises and certain self-insured employers.

This provision is effective for calendar years beginning after December 31, 2013. The fee is determined with respect to net premiums written after December 31, 2012, with respect to health insurance for any United States health risk.



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Pharmaceutical Company Tax

Brand name prescription drug manufacturers and importers will be required to pay an annual fee based on their relative market share of sales to federal government programs. This fee will be treated as an excise tax with respect to which only civil actions for refunds under the Code will apply. The fee is not deductible. The Treasury will calculate the amount of the annual fee owed by each covered entity, and each covered entity must pay the fee by September 30 of each year.

In general, a covered entity's relative market share is equal to a percentage derived by dividing its covered sales taken into account for a calendar year by the aggregate covered sales of all covered entities taken into account for the calendar year. Covered sales include sales to the following government programs: Medicare Parts B and D, Medicaid, programs of the Department of Veterans' Affairs, the Department of Defense, and TRICARE. Sales will be adjusted to reflect any rebates, discounts, or price concessions provided to the government. The percentage of an entity's covered sales taken into account is based on a graduated rate structure with annual sales of \$5 million or less excluded and annual sales in excess of \$400 million fully included in the calculation.

This provision is effective for calendar years beginning after December 31, 2010.

Medical Device Excise Tax

Manufacturers, producers and importers will be required to pay a 2.3 percent deductible excise tax on the sales price of taxable medical devices sold in the United States. A taxable medical device is any device, as defined in § 201(h) of the Federal Food, Drug, and Cosmetic Act, that is intended for human use. The excise tax does not apply to eyeglasses, contact lenses, hearing aids and any other devices that are determined by the Secretary of Health and Human Services to be of a type purchased by the general public at retail for individual use. It is anticipated that the Secretary of Health and Human Services will publish a list of exempt medical devices.

This provision is effective for sales after December 31, 2012.

Tax-Exempt Hospitals

To qualify for tax-exempt status under section 501(c)(3) of the Code, hospitals will be required to satisfy four additional requirements. These requirements apply to an organization that operates a facility that is required by a State to be licensed, registered, or similarly recognized as a hospital and any other organization that Treasury determines has the provision of hospital care as its principal function or purpose. If an organization operates more than one hospital, each hospital facility must separately meet these requirements. Facilities failing to meet these requirements could lose their tax-exempt status. This provision requires a hospital to: 1) conduct, adopt, and disclose a community health needs assessment at least once every three years; 2) adopt, implement, and "widely publicize" a written financial assistance policy containing information regarding eligibility criteria, payment information and other similar information; 3) limit its bill for emergency or other medically necessary care provided to individuals qualifying for



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assistance under the hospital's financial assistance policy to not more than the amount generally billed to individuals who have insurance covering such care; and 4) follow certain debt collection practices.

This provision is generally effective for taxable years beginning after March 23, 2010.

Executive Compensation Deduction Limitation for Health Insurers

A covered health insurance provider's deduction for compensation under section 162(m) of the Code will be capped at \$500,000 per tax year per applicable individual. An insurance provider is a covered health insurance provider if at least 25 percent of its gross premium income from its health business is derived from health insurance plans that meet certain coverage requirements. Employers with self-insured plans are not covered health insurance providers.

Applicable individuals include all officers, employees, directors and other workers or service providers performing services for or on behalf of a covered health insurance provider. If an individual is an applicable individual with respect to a covered health insurance provider for any taxable year, the individual is treated as an applicable individual for all subsequent taxable years.

This provision is effective for compensation paid in taxable years beginning after December 31, 2012 with respect to services performed after December 31, 2009.

Therapeutic Discovery Project Credit

Investors in "qualifying therapeutic discovery projects" may be eligible for a credit (or a grant in lieu of the credit) equal to 50 percent of the amount of qualifying expenditures incurred with respect to such projects. Qualifying therapeutic discovery projects include projects designed to develop a product, process or therapy to diagnose, treat or prevent diseases. The credit is available only to taxpayers with 250 or fewer employees that have projects certified by the Secretary of the Treasury as eligible for the credit.

In certifying projects as qualifying therapeutic discovery projects, the Treasury will consider only those projects that show reasonable potential to: (1) result in new therapies to treat areas of unmet medical need or to prevent, detect, or treat chronic or acute disease and conditions; (2) reduce long-term health care costs in the United States; or (3) significantly advance the goal of curing cancer within a 30-year period.

In calculating the credit, certain costs are excluded, including certain executive compensation, interest expenses, facility maintenance expenses, certain service-related costs, and any other costs identified by the Treasury. Expenditures taken into account in computing the credit do not qualify for other research-related credits under the Code or for "bonus" depreciation. The total amount of the credits authorized under the program is limited to \$1 billion.

This provision is effective for investments made after December 31, 2008 and on or before December 31, 2010.



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For more information on this provision refer to our client alert “New Tax Credit/Grant Available to Small Biotech Companies (While Supplies Last)” which is available by clicking [here](#).

Other Tax Provisions

Codification of Economic Substance

The court-developed economic substance doctrine is codified. New section 7701(o) of the Code provides that in the case of a transaction to which the economic substance doctrine is relevant, the transaction will be treated as having economic substance only if (1) the transaction changes the taxpayer’s economic position in a meaningful way (apart from the Federal income tax effects) and (2) the taxpayer has a substantial business purpose (apart from the Federal income tax effects) for entering into the transaction. The codification of this doctrine is not intended to change the standards used by courts to determine when to utilize an economic substance analysis.

The codification is purportedly not intended to alter the tax treatment of certain basic business transactions that, under longstanding judicial and administrative practice, are respected. The legislative history mentions the following examples:

- The choice between capitalizing a business enterprise with debt or equity;
- A U.S. person’s choice between utilizing a foreign corporation or a domestic corporation to make a foreign investment;
- The choice to enter a transaction or series of transactions that constitute a corporate organization or reorganization under Subchapter C of the Code; and
- The choice to utilize a related-party entity in a transaction, provided that the arm’s length standard of section 482 of the Code and other applicable concepts are satisfied.

Increased penalties apply in circumstances where the Service successfully challenges a transaction on economic substance grounds. A new 20 percent “strict liability” penalty is imposed for underpayments and understatements attributable to any disallowance of claimed tax benefits by reason of a transaction lacking economic substance. The penalty is increased to 40 percent if the relevant facts affecting the tax treatment of the transaction are not adequately disclosed. An amended return or supplement to a return will not be taken into account if filed after the taxpayer has been contacted for audit or such other date as may be specified by the Secretary of the Treasury. Because this penalty is based on strict liability, taxpayers cannot avoid the penalty by demonstrating reasonable cause.

This provision is effective for transactions entered into after March 30, 2010 and to underpayments, understatements, and refunds and credits attributable to transactions entered into after March 30, 2010.



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Black Liquor Ineligible for Cellulosic Biofuel Producer Tax Credit

The cellulosic biofuel producer credit is a nonrefundable income tax credit for each gallon of qualified cellulosic fuel production of a producer during a taxable year. The amount of the credit is generally \$1.01 per gallon. The credit is not available for fuels with significant water, sediment or ash content, such as “black liquor” (a by-product of the “kraft” pulping process employed by paper manufacturers).

This provision is effective for fuels sold or used on or after January 1, 2010.

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