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Health-Care Reform: Tax Changes for Individuals

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The health-care reform legislation signed into law in 2010 contained a number of tax changes. Some of these changes took effect immediately; others have only recently become effective. Here are some of the changes worth noting:

Changes that went into effect prior to 2013

If you frequent tanning salons, you're probably well aware that the health-care reform legislation brought with it a 10 percent tax assessed on amounts paid for indoor tanning services.

The legislation also extended the tax benefits associated with employer health plans (i.e., the ability to exclude the value of the benefits from income) to any children who have not reached age 27 by the end of the year.

In addition, the legislation made changes to flexible spending arrangements (FSAs), health reimbursement arrangements (HRAs), health savings accounts (HSAs), and Archer MSAs: over-the-counter medications (except for insulin and medications that are prescribed by a physician) are no longer considered qualified medical expenses for purposes of reimbursement and tax-free distributions. And, the additional tax that applies to HSA and Archer MSA distributions not made for qualifying expenses increased to 20 percent.

Changes that went into effect in 2013

Do you typically itemize your deductions on Schedule A? Starting in 2013, unreimbursed medical expenses were deductible on Schedule A only to the extent that they exceeded 10 percent of adjusted gross income (AGI), instead of the 7.5 percent threshold that applied in prior years. Until 2017, however, if you or your spouse turns age 65 before the end of the taxable year, the 7.5 percent AGI threshold will continue to apply. Beginning in 2017, the 10 percent AGI threshold will apply to individuals who have reached age 65 as well.

Also starting in 2013, high-income individuals were subject to two new Medicare-related taxes. Those with wages over $200,000 (married couples filing jointly with wages over $250,000) are subject to an additional 0.9 percent hospital insurance (Medicare) payroll tax. A 3.8 percent Medicare contribution tax is also imposed on the unearned income of individuals with modified adjusted gross income (MAGI) over $200,000, or married couples filing jointly with MAGI over $250,000.

Finally, for 2013 and 2014, health FSAs that are part of a cafeteria plan are capped at a $2,500 reimbursement limit.

Changes effective in 2014

This is the year of the carrot and the stick. A premium assistance tax credit is available to help eligible individuals purchase health-care insurance through the Exchange Marketplace. Who qualifies? Individuals with household income between 100 percent and 400 percent of the federal poverty level will qualify, with the exact amount of the credit based on income level (for a family of four for 2014, that means income from $23,550 to $94,200). Generally, individuals who are offered coverage through an employer health plan don't qualify for the credit unless the employer health plan doesn't cover an adequate share of benefits (60 percent), or it's considered "unaffordable" (the employee portion of the premium is 9.5 percent or more of the employee's household income).

And then there's the stick. Beginning in 2014, if you're a U.S. citizen or legal resident, you'll generally be required to have adequate health-care coverage. If you don't, you'll face a penalty tax unless you qualify for an exemption. For 2014, the tax will equal the greater of 1 percent of the amount of your household income that exceeds a specific amount (generally, the standard deduction plus personal exemption amounts you're entitled to for the year) or $95 per uninsured adult (half that for uninsured family members under age 18), with a maximum household penalty of $285. By 2016, the percentage rate increases to 2.5 percent, the dollar amount per uninsured adult increases to $695, and the maximum household penalty increases to $2,085.

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