CENTER FOR FINANCIAL PLANNING, INC.
Independent Registered Investment Advisor

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Health Care Reform - Planning Tips

“Health care costs and coverage are an important concern for all Americans. Center clients are no exception to this concern,” states Center partner Marilyn Gunther, CFP®. “We know only the basics of the new legislation which will probably unfold over the next months and years.”

In addition to services received and the cost of coverage, Center planners recognize the many financial planning issues that are raised by this new legislation.

The basic provisions of the new health care reform: in 2014, the bill will expand health coverage to 32 million U.S. residents who currently don't have it, mainly by allowing low-income uninsured persons into Medicaid and paying part of the premiums for people with incomes near the federal poverty line.

Financial planners have been trying to digest all the provisions of this legislation, so that we can give reasonable advice to our clients. We don't recommend that you read this bill unless you have a serious case of insomnia!

A recent article in *Financial Planning*, one of our leading trade magazines, offers a first hint at how planning for health care reform might look in the next few years.

The new law includes several tax increases. Starting in 2013, the Medicare payroll tax will go up from 1.45% to 2.35% of income for single taxpayers earning more than $200,000 a year (and couples earning more than $250,000). At the same time, people in these income levels will be hit by a new 3.8% Medicare tax on all dividends, capital gains and income from rental property.

These new taxes will be applied in a mostly unfamiliar way: if you earn one dollar over the threshold, the higher Medicare tax counts against your <u>entire</u> income, not just the income earned over the threshold amount. And the extra Medicare tax on dividends, capital gains and rent is only applied to people with income above these threshold amounts; if your adjusted gross income is one dollar lower than the threshold, the tax does <u>not</u> apply to you.

Next year, high-earning taxpayers will see dividend taxes rise from 15% to ordinary income rates (maximum: 39.6%), and capital gains taxes could rise from 15% to 20% in addition to the Medicare surtaxes.

How can we plan for this? Anybody who has accumulated earnings in a C corporation might be advised to take as much of the money out in dividends this year as possible, paying a 15% tax and avoiding the higher taxes in 2011 and later. People who own an S corporation might consider taking more of their income in salary and less in dividends, paying less Medicare tax in the process. But this can be tricky, since any salary increase might be subject to additional FICA taxes of 12.4%.

Another way to avoid some of the tax bite is to move money out of investments which generate high dividends or interest (corporate bonds and utilities) to muni bonds, which provide tax-exempt or tax-deferred income. Some might also defer more income through employer sponsored retirement plans or annuities.

Meanwhile, high deductible health insurance policies will face restriction; $2,000 will be the highest deductible for small group health plans for individuals; $4,000 for families. But existing policies will be grandfathered so long as they eliminate exclusions for pre-existing conditions, and eliminate yearly and lifetime limits on coverage.

The best way to plan for this provision is to buy a high-deductible policy now before they disappear. People with a health savings account should consider contributing the maximum this year, and employers might switch to a high-deductible group policy now in order to contain future costs.

Marilyn Gunther notes, “Keeping clients informed on how best to incorporate these changes in their financial and health care lives will continue to be a focus of our planners as the legislation evolves.”

Please note, changes in tax laws or regulations may occur at any time and could substantially impact your situation. While we are familiar with the tax provisions of the issues presented herein, as Financial Advisors of RJFS we are not qualified to render advice on tax or legal matters.