Market *Alert*

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STANDARD & POOR'S

Ready or Not, Here Comes Health Care Reform

"It's complicated, but it does establish a very key policy that you're going to have options, regardless of your health situation or your employment situation." - DeAnn Friedholm, Consumers Union, publisher of Consumer Reports.

Congressional Democrats passed the $940 billion health care reform bill in late March. Now the real work of implementing the mammoth piece of legislation begins. Who is affected, how, and when? Here's a broad outline of the bill's key provisions with some thoughts on what it may mean to investors and consumers.

The Patient Protection and Affordable Care Act of 2010 represents the most sweeping legislative action since Medicare became law in 1965. At a minimum, it promises to provide health care coverage for some 32 million uninsured Americans, to prohibit insurance companies from cancelling or denying coverage to individuals with pre-existing medical conditions, and to require all individuals to maintain some form of coverage or face a tax penalty.

Some important changes take effect this year

- **For small businesses.** A tax credit for employers with 25 or fewer employees and average annual wages of $50,000. This year and through 2013, qualifying employers may receive a credit of up to 35% of their contributions to employee health insurance premiums.[1]
- **For minor children.** Insurance companies will be prohibited from denying coverage to children with pre-existing medical conditions.
- **For adult children.** Dependent coverage will be extended for young adults (through age 26) via their parents' insurance plan.
- **For Medicare recipients.** A $250 rebate for those who are affected by the Medicare Part D prescription drug "donut hole" - a big expensive gap in coverage that affects millions. Starting in 2011, those affected will receive a 50% discount on prescription drugs. By 2020, the donut hole is expected to be eliminated.[2]
- **For the insured.** A ban on lifetime limits on coverage imposed by insurance companies and on denying coverage or cancelling policies if the policyholder becomes ill.
- **For the uninsured.** The establishment of high-risk pools for individuals who have been uninsurable due to pre-existing medical conditions.

Other changes phase in between now and 2014

- **Mandatory insurance coverage.** Most Americans not already eligible for Medicaid or Medicare will be required to maintain "minimal essential coverage." Those who fail to do so will be liable for a penalty.
- **Expanded Medicaid and federal subsidies.** Additional federal

subsidies will help to make coverage more affordable for lower- to middle-income families (individuals earning less than $43,000 annually or $88,000 for a family of four). Subsidies will also increase to help more small businesses afford coverage for their employees.[3]

- **State-run insurance exchanges.** These marketplaces are intended to provide a more competitive, consumer-friendly way for individuals without employer coverage as well as small businesses to shop for health care coverage.

Takeaways for Consumers and Investors

Health care reform is the most hotly debated initiative in decades. Even the recent passage of legislation has not quelled some disputes. What is more, as DeAnn Friedholm of Consumers Union, the nonprofit publisher of *Consumer Reports* said, "It's complicated, but it does establish a very key policy that you're going to have options, regardless of your health situation or your employment situation." With the continued controversy in mind, here are some potential next steps to consider.

- **Plan for new tax rules -** One way Uncle Sam plans to pay the $940 billion tab for health care is to raise payroll taxes on households earning more than $250,000. Look for this new tax starting in 2013. Another will be a 3.8% tax on unearned income on investment interest and dividends. A third will be a 40% excise tax on high-cost insurance plans - those valued at more than $10,000 for individual coverage and $27,500 for family coverage.[1]

- The new law will also limit the amount individuals can contribute each year to flexible spending accounts for medical uses and modify the definition of "qualified medical expenses" as it pertains to FSAs, HSAs, and HRAs. In addition the law raises the threshold for the itemized medical expense deduction to 10% of adjusted gross income (AGI) from 7.5%.

- Aside from new taxes assessed to individuals and families, the law will also glean revenue from businesses by imposing "play or pay" fines, and from the health care sector itself via annual fees.

- **Be open to new investment opportunities -** With the uncertainty surrounding health care reform lifted, investors can focus on the potential impact it may have on various industries within the Health Care sector. Toward that end, S&P Equity Research sees health care reform as positive for the managed care industry, generic drug manufacturers, biotechnology, hospitals, and clinics.

- Elsewhere, investors are viewing municipal bonds with fresh eyes. Due to their typically tax-exempt status, interest payments from munis could avoid the new 3.8% tax on investment income slated to go into effect in 2013.

- **Do your homework -** Legislation this complex and comprehensive will no doubt evolve over time. Try to stay on top of the provisions that pertain directly to you. Luckily there is a wealth of information available from numerous sources. Some are listed below. If a face-to-face discussion is what you prefer, a trusted tax or financial planning professional should be able to help.

Resources

The Kaiser Family Foundation, www.kff.org

U.S. Department of Health and Human Services, www.hhs.gov

HealthReform.Gov, www.healthreform.gov

Medicare, www.medicare.gov

[1]Source: *CCH Tax Briefing*, "Special Report: Health Care Reform Act," March 30, 2010.

[2]Source: *The New York Times*, "For Consumers, Clarity on Health Care Changes," March 21, 2010.

[3]Source: *The Wall Street Journal*,"Steps You Can Take Ahead of Changes in Coverage, Taxes," March 22, 2010.