

**NEWS ALERT: EXPLORING WHAT THE AFFORDABLE
HEALTH CARE FOR AMERICA ACT WILL MEAN
FOR CLOSELY-HELD BUSINESSES AND PORTFOLIO COMPANIES**

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Freeborn & Peters LLP represents a significant number of closely-held businesses and businesses that are owned, in whole or in part, by private equity funds. Over the past few months, there has been an extensive amount of discussion on health care reform. Late last week, after assessing a number of competing proposals, a Bill was introduced by the Democrats in the House of Representatives that appears to be the framework for these sweeping reforms.

The recently released Bill, captioned as the “Affordable Health Care for America Act,” sets forth significant changes to the way businesses will provide health care benefits to their employees. If this Bill is enacted into law, however, its impact on businesses will extend well beyond the imposition of certain requirements on employer-provided health care coverage. We believe that the Bill will significantly change the analysis for potential purchases and sales of existing businesses and the structure adopted for these transactions.

This news alert provides a brief summary of some of the provisions in the Bill that will likely result in significant changes in the operations of owners of closely-held businesses and portfolio companies.

An Overview of the Proposals on Employer-Provided Health-Care

In general, under the Bill an employer would be required to either: (i) offer qualified health care coverage to its employees; or (ii) pay an 8% payroll tax. Employers with an annual payroll that does not exceed \$500,000, however, would be exempt from the 8% payroll tax and employers with an annual payroll ranging from \$500,000 to \$750,000 would be subject to a reduced payroll tax ranging from 0% to 8%.

To qualify under the Bill, employer-provided health care coverage would have to satisfy several requirements:

- employers would have to offer their employees the option of selecting individual health care coverage or family health care coverage;
- employers would have to provide for the automatic enrollment of their employees into their health plans; and
- employers would have to make a minimum contribution of 72% of the costs for individual coverage and 65% of the costs for family coverage.

Further, to qualify under the Bill, employer-provided health care coverage may not:

- impose any annual or lifetime limits on coverage;
- provide for cost-sharing for preventative items and services; or

- provide for annual cost-sharing for an individual that exceeds \$5,000 or for a family that exceeds \$10,000.

An Overview of the Minimum Coverage That Will Be Required

The Bill provides that employer-provided health care coverage must include certain essential benefits which would be determined by the newly-created “Benefits Advisory Committee.”

Details about the Benefits Advisory Committee continue to emerge. What is currently known is that the types of essential benefits would also be subject to the approval of the Secretary of Health and Human Services.

At this point, essential benefits would include the following covered services: (i) hospitalization; (ii) prescription drugs; (iii) mental health services; (iv) maternity care; and (v) children's oral health, vision and hearing services.

Observations

A detailed analysis of all of the provisions of the Bill is beyond the scope of this news alert. However, there are several issues raised in the Bill that will effect how stock purchases, mergers and other business transactions are structured.

As discussed above, employers who do not offer health care coverage to their employees would be subject to an 8% payroll tax. The Bill also provides that small employers would be eligible for a credit equal to 50% of the amount paid by the employer for employee health care coverage. This credit would be phased out for employers with 10 to 25 employees and employers with average wages of \$20,000 to \$40,000. At this point, it is unclear how these rules will apply to affiliated companies or to businesses that are operated through limited liability companies. What is clear is that these proposed law changes will have an impact on the structure implemented for various transactions and the due diligence that will need to be performed for such transactions.

In addition, the Bill contains several other revenue provisions, such as the codification of the substantial economic effect doctrine and a 5.4% additional tax on individuals with gross income in excess of \$500,000 (\$1,000,000 for married couples filing joint returns). We expect that both of these proposed law changes will have a significant effect on how various transactions will be structured in the future.

The details of health care reform are still being debated and it is unclear when or whether any sweeping changes to health care reform will occur. The members of Freeborn & Peters' Tax and Employee Benefits Practice Groups will continue to monitor the proposed legislation so that the attorneys at Freeborn & Peters can keep our clients apprised of how this proposed legislation could affect future acquisitions or sales.



We anticipate that we will issue periodic updates as the proposed legislation evolves. If you would like to discuss any of these issues in more detail, please feel free to contact Ed Hannon, lead Partner in the Tax Group at Freeborn & Peters or Mike Tomasek, lead Partner in the Employee Benefits Group at Freeborn & Peters. Mr. Hannon can be reached at (312) 360-6754 or <mailto:ehannon@freebornpeters.com> and Mr. Tomasek can be reached at (312) 360-6538 or <mailto:mtomasek@freebornpeters.com>.