The Heritage Foundation
LEADERSHIP FOR AMERICA

ISSUE BRIEF

No. 3637 | JUNE 13, 2012

Delaying Obamacare Tax Increases Key Part of Stopping Taxmageddon

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Taxmageddon, a one-year $494 billion tax increase, threatens to strike the economy on January 1, 2013, unless Congress and President Obama act to stop it soon.[1] Taxmageddon includes the implementation of five of the 18 separate tax increases in the Patient Protection and Affordable Care Act, better known as Obamacare[2]:

1. An increase in the Hospital Insurance (HI) portion of the payroll tax and the application of the tax to investment income;

2. A new excise tax on the sales of medical device manufacturers and importers;

3. A reduction of the income tax deduction for medical expenses;

4. An elimination of the corporate income tax deduction for expenses related to the Medicare Part D subsidy; and

5. A limitation of the corporate income tax deduction for compensation that health insurance companies pay to their executives.

All five of these tax increases will have painful impacts on the economy and job creation while expanding the government's role in the health care market. The HI tax and the medical devices tax are the most harmful.

HI Tax Increase. The HI portion of the payroll tax raises the current rate applied to workers' wages and salaries from 1.45 percent to 2.35 percent for incomes over $200,000 a year ($250,000 for married filers). This brings the total HI tax on wages and salaries to 3.8 percent for incomes over $200,000 when including the 1.45 percent portion of the tax paid by employers on their workers' behalf.

It also applies that 3.8 percent rate to investment income, including capital gains, dividends, rents, and royalties. This surtax will apply to incomes over $200,000, which in this case includes taxpayers' combined total of wages, salaries, and investment income. This tax increase applies the payroll tax to investment income for the first time ever, which breaks the long-held precedent that the payroll tax only applies to wage and salary income.

The HI tax is a dedicated tax to fund Medicare Part A. Obamacare, however, uses the new revenue raised from these increases to fund new spending created by the law. This breaks another long-held precedent that the revenue that payroll taxes raise goes only to programs that Congress created the taxes to fund.

The higher tax rate on wages and salaries will cause workers to cut back on their hours, which will slow economic growth. It will also deter job creation at small businesses. The income of certain small businesses (sole proprietorships) is wage and salary income to the owner. As both employee and employer, the owner therefore pays the entire newly increased 3.8 percent HI tax rate. With more of the owner's—and therefore the business's—income taken by higher taxes, the owner will have fewer resources to invest back into the business to create jobs.

The application of the 3.8 percent HI tax to investment income will have an even more deleterious impact on job creation because it will reduce investment that is essential

This paper, in its entirety, can be found at
http://report.heritage.org/ib3637

Produced by the Thomas A. Roe Institute for Economic Policy Studies

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for job creation. If Taxmageddon goes into effect, the capital gains rate rises from 15 percent this year to 20 percent in 2013. The Obamacare surtax would raise the rate to 23.8 percent, which means the capital gains rate will rise 59 percent in 2013.

This steep increase will raise the "hurdle rate" for *new* investment. Entrepreneurs seeking to launch new ventures and existing businesses seeking to expand need these investments to at minimum meet the after-tax rate of return demanded by investors whom they ask to finance their plans. Investors do not fund investments that fail to generate returns adequate to meet that threshold.

A higher capital gains rate raises the return that investments must earn in order to continue meeting the return that investors' require. The result is less investment, because investments that otherwise would have been made now fail to meet that higher return requirement. The jobs that forgone investment would have created are forgone as well.

The dividends tax rate will rise from 15 percent this year all the way back to 39.6 percent in 2013, because under current law, dividends return to being taxed as wage and salary income. Adding on the 3.8 percent HI surtax brings the dividends rate to 43.4 percent. The higher dividends rate will also cause businesses to cut back on the dividends they pay out. They will instead seek to return value to their shareholders through other means. This will hurt seniors that rely on dividends to supplement their Social Security benefits and other retirement income to meet their basic needs.

Medical Device Tax a Job Killer. Obamacare applies a new 2.3 percent excise tax on the sales of manufacturers and importers of medical devices. Medical devices include a broad range of instruments commonly used in medical offices—everything from MRI and X-ray machines to syringes and stethoscopes. It also includes products necessary to patients, such as prosthetics.

The tax could have differing impacts depending on how the manufacturers and importers are able to pass its cost along. If they are able to pass the entire cost of the tax to their customers, then it will essentially be a sales tax that raises prices for doctors, hospitals, medical centers, and patients. If the manufacturers and importers cannot pass the entire cost of the tax to their customers, then the tax will function as a corporate income tax without any deductions. And, like the corporate income tax, the burden will fall on the businesses' customers, shareholders, and workers in some proportion.

Anecdotal evidence points to the latter scenario, with workers of these businesses bearing the brunt of the tax. Layoffs of thousands of workers have already occurred at some manufacturers that have anticipated the tax's impact on their businesses.[3]

For instance, Stryker Corporation of Kalamazoo, Michigan, announced it will lay off about 1,000 workers—about 5 percent of its workforce—because of the tax. Many of those job losses will occur in the company's research and development department.[4] This will stifle the company's ability to innovate to create new products or improve existing products.

More job losses could follow as more medical device manufacturers and importers realize the impact that the tax will have on them. The jobs already lost will remain lost unless Congress repeals the tax.

Delay Obamacare Tax Increases When Stopping Taxmageddon. The three other Obamacare taxes that begin in 2013 each raises more revenue that Obamacare spends to further expand the government's role in the health care market. Proper health care reforms would not raise taxes to grow the government's control over American's health care.

Congress should permanently stop Taxmageddon, including a repeal of Obamacare and its harmful assortment of tax increases. If Congress cannot repeal it this year, it should delay Obamacare's tax increases for as long as possible, whether that is one year, two years, or longer.

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