

Self-Employment Tax on Health Care

The fight continues for health care parity

Self-employed individuals, unlike large corporations, cannot permanently deduct the cost of their health insurance as a business expense. Although NSBA won the first battle in 2003 allowing self-employed individuals to deduct the cost of health insurance for income tax purposes, they still are not on par with large businesses, meaning more must be done.

At issue is the 15.3 percent tax that self-employed individuals must pay on their employer-provided health insurance costs to which nobody else is subjected. This significant tariff comes in the form of FICA payroll taxes, commonly referred to as payroll or self-employment taxes. The self-employment tax rate on net earnings is the sum of 12.4 percent for Social Security (old age, survivors, and disability insurance), and 2.9 percent for Medicare (hospital insurance).

While the important change in 2003 enabled small-business owners to deduct the cost of health care from their income, that income already has been exposed to the payroll tax. Thus, the self-employed effectively pay the self-employment tax on income used to purchase health care.

The self-employed pay an average of \$12,680 per year for health insurance. Because they cannot deduct this as an ordinary business expense, the 15.3 percent payroll tax they alone pay on their premiums amounts to \$1,940.04 in extra taxes that only the self-employed pay. This is money that could be used to reinvest and grow the business, hire part-time help or cover the ever-increasing costs of health insurance. This additional 15.3 percent tax makes already disturbingly high-priced health care cost even more by adding thousands of dollars to the cost of an individual's health care.

In Sept. 2010, after many months of work to get legislation passed to help America's struggling small-business community, the NSBA-supported Small Business Jobs Act was finally signed into law. For one-year only (2010), the law will allow self-employed individuals to fully deduct the cost of their health insurance from their self-employment taxes. Though only applicable to 2010 tax returns, the passage of this provision is a critically important first step and signal that lawmakers understand the egregious nature of this tax penalty.

This one-year fix is expected to save self-employed business owners approximately \$456 to \$968 in taxes this year. Additionally, the temporary provision will provide a one-year level playing field for America's smallest businesses that have not benefited from the same tax treatment of health care costs that all other larger businesses have enjoyed.

The NSBA-led coalition will continue our efforts in the 112th Congress to permanently remove this significant inequity within the tax code that penalizes self-employed Americans and makes it increasingly difficult for them to afford quality health care coverage.

NSBA has been leading the charge on ending this unfair penalty on the self-employed for nearly 10 years, and was integral in its inclusion in the Jobs bill. NSBA believes legislators finally are realizing that placing additional taxes on small-business owners' health insurance is not a sound policy position.