



Health Care Reform News

April 16, 2010

Small Business Tax Credits

Under the Patient Protection and Affordable Care Act (PPACA; P.L. 11-148) small businesses that choose to provide health insurance could be eligible for a credit toward their cost of health insurance. Though certain businesses may be exempt from any employer responsibility to provide health insurance or any penalties for non-compliance, the new law would offer an incentive to small businesses by helping pay for their employees' coverage through a tax credit toward the purchase of health insurance.



Eligibility

The new small business tax credit is effective for amounts paid or incurred after December 31, 2009, and applies for the determination of AMT credits after that date and their carryback. It is not restricted to those with a tax liability. Small businesses that currently provide health care for their workers could receive immediate help with their premium costs, and additional firms that initiate coverage this year could receive the tax assistance.

To be eligible, small employers would have to contribute at least 50% of the cost of premiums towards a qualified health plan (or 50% of a benchmark premium). Small businesses with 10 or fewer full-time employees and with average taxable wages of \$25,000 or less could claim the full credit amount. *§1421(a): IRC §45R(a) and (d) as amended by §10105*

- In addition to business size (full credit for 10 or fewer employees/tiered credit for 11-15 employees), the credit is also linked to the average wage of employees. A small business must pay their workers \$25,000 or less in order to qualify for the full credit. The amount of the credit is tiered for those with workers making up to \$50,000. An employer paying average taxable wages above \$50,000 is not eligible for the tax credit.

Employers will not be eligible to use the credit for certain employees, including defined "seasonal workers," self-employed individuals, 2% shareholders of an S corporation (as defined by section 1372(b), 5% percent owners of a small business (as defined by section 416(i)(1)(B)(i)), and dependents or other household members. However, leased employees are eligible employees for the credit. *§1421(a): IRC §45R(e)*. The self-employed are eligible for the individual premium assistance available in 2014 if they meet the income requirements (individual making below \$43,320 or family of four with income below \$88,200.)

Non-profit organizations would be eligible. The credit amount would be the lesser of (1) a 25% credit (2010-2013) and a 35% credit (beginning in 2014), or (2) the amount of employer-paid payroll taxes (including the Medicare contribution) for the relevant calendar year. *§1421(a): IRC §45R(f) and (g) as amended by §10105*

Employers receiving credits will be denied any deduction for health insurance costs equal to the credit amount.

Small Business Tax Credits Cont.

Credit Amount & Duration

A 35% credit (in years 2010-2013) and 50% credit (beginning in 2014 for no more than two consecutive taxable years) is offered for employer costs for the lesser of (1) the employer premium contribution toward plans offered by the employer through an exchange, or (2) the contribution the employer would have made if each of those same employees had enrolled in a qualified health plan with a premium equal to the average (determined by the HHS Secretary) for the small group market in the rating area I which the employee enrolls for coverage. To avoid an incentive to choose a high-cost plan, an employer's eligible contribution is limited to the average cost of health insurance in that state. (For 2010-2013, "average" would be determined by the Secretary based on the average premium for the small group market in the state, or area in the state, in which the employer offers health insurance). *§1421(a): IRC §45R(b) and (g) as amended by §10105*

The tax credit phases out as average employee compensation increases from \$25,000 to \$50,000 and as the number of full-time employees increases from 10-25. Full-time employees would be calculated by dividing the total hours worked by all employees during the tax year by 2,080 (with a maximum of 2,080 hours for any one employee). Seasonal workers would be exempt from this calculation. Average annual wages would be determined by dividing the aggregate amount of wages paid by the employer by the number of full-time equivalent employees, for the taxable year. *§1421(a): IRC §45R(c) and (d) as amended by §10105* The average wage threshold for determining the phase-out of credits will be adjusted for inflation after 2013.

Firms can claim the credit for 2010 through 2013 and for any two years after that.

To continue receiving a tax credit in 2014, a small employer must drop their existing coverage and purchase group coverage in the newly created Exchanges.

Small Business Health Care Tax Credit Scenarios

Examples of Employers Receiving the Credit

Example 1: Auto Repair Shop with 10 Employees

Main Street Mechanics:

- *Employees:* 10
- *Wages:* \$250,000 total, or \$25,000 per worker
- *Employee Health Care Costs:* \$70,000

*2010 Tax Credit: \$24,500
(35% credit)*

*2014 Tax Credit: \$35,000
(50% credit)*

Example 2: Restaurant with 40 Part-time Employees

Downtown Diner:

- *Employees:* 40 half-time (equivalent to 20 full-time)
- *Wages:* \$500,000 total, or \$25,000 per full-time equivalent worker
- *Employee Health Care Costs:* \$240,000

*2010 Tax Credit: \$28,000
(35% credit with phase-out)*

*2014 Tax Credit: \$40,000
(50% credit with phase out)*

3 SIMPLE STEPS

If you are a small employer (business or tax-exempt) that provides health insurance coverage to your employees, determine if you may qualify for the **Small Business Health Care Tax Credit** by following these three simple steps:

1

Determine the total number of your employees (not counting owners or family members):

Full-time employees: _____
(enter the number of employees who work at least 40 hours per week)

+

Full-time equivalent of part-time employees: _____
(Calculate the number of full-time equivalents by dividing the total annual hours of part-time employees by 2080.)

= total employees

If the total number of employees is fewer than 25 **GO TO STEP 2**

2

Calculate the average annual wages of employees (not counting owners or family members):

Take the total annual wages paid to employees: _____

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Divide it by the number of employees from STEP 1: _____
(total wages ÷ number of employees)

= average wages

If the result is less than \$50,000, **AND**

3

You pay at least half of the insurance premiums for your employees at the single (employee-only) coverage rate, then



you may be able to claim the **Small Business Health Care Tax Credit**.
Find out more information at IRS.gov

