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IRS Releases Information on Claiming Small Employer Health Care Tax Credit

The Patient Protection and Affordable Care Act (PPACA) was enacted on March 23, 2010. PPACA includes a tax credit for small businesses that provide health care coverage to their employees. The tax credit is effective for tax years beginning in 2010. The credit is designed to encourage small employers to offer health insurance coverage for the first time or maintain coverage they already have.

On December 2, 2010, the Internal Revenue Service (IRS) released a final Form 8941 that small businesses and tax-exempt organizations will use to calculate the small business health care tax credit when they file income tax returns. The IRS also added guidance on additional issues relating to the small employer tax credit in Notice 2010-82 to enhance the previously provided Notice 2010-44.

The Small Business Tax Credit

In 2010, the credit is generally available to small employers that contribute an amount equivalent to at least half the cost of single coverage toward buying health insurance for their employees. The credit is specifically targeted to help small businesses and tax-exempt organizations that primarily employ moderate- and lower-income workers.

For tax years 2010 to 2013, the maximum credit is 35 percent of premiums paid by eligible small business employers and 25 percent of premiums paid by eligible employers that are tax-exempt organizations. Beginning in 2014, the maximum tax credit will go up to 50 percent of premiums paid by eligible small business employers and 35 percent of premiums paid by eligible, tax-exempt organizations for two years. The maximum credit goes to smaller employers – those with 10 or fewer full-time equivalent (FTE) employees – paying annual average wages of \$25,000 or less.

The credit is completely phased out for employers that have 25 FTEs or more or that pay average wages of \$50,000 per year or more. Because the eligibility rules are based in part on the number of FTEs, and not simply the number of employees, businesses that use part-time help may qualify even if they employ more than 25 individuals.

IRS Notice 2010-82

IRS Notice 2010-82 contains information designed to help small employers correctly figure and claim the credit. This Notice clarifies that certain employers, including farmers cooperatives, employers whose employees do not perform services in a trade or business, and employers located outside of the United States, can qualify for the credit as long as they meet applicable requirements.

The notice also makes clear that the “family members” of owners and partners that are not taken into account as employees includes spouses of these individuals, for purposes of determining the number of FTEs. It states that leased employees are counted in calculating FTEs, but their insurance premiums are not counted by the employer if they are paid by the leasing organization.

The IRS has also provided information about how to calculate average annual wages. It states that all wages paid are taken into account, including overtime pay. Employers must also calculate hours of service, using one of three methods. Notice 2010-82 clarifies that employers can use different methods for different classifications of employees as long as the classifications are reasonable and consistently applied. Employers can also change the method from year to year.

Notice 2010-82 gives additional information about which types of plans qualify as health insurance coverage for an employer to claim the credit. Self-insured plans, health reimbursement arrangements (HRAs), health flexible spending

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accounts (health FSAs) and health savings accounts (HSAs) are not considered eligible health insurance coverage. However, contributions to multiemployer plans and church plans can be considered qualifying arrangements if applicable requirements are met.

To claim the credit, employers must meet uniformity requirements for contributions to their employees' coverage. Notice 2010-82 contains rules regarding these requirements for the 2010-2013 tax years. The requirements will depend on the number of plans or benefit packages the employer offers and whether premiums are charged on a list or composite basis.

Form 8941 - Credit for Small Employer Health Insurance Premiums

The IRS has posted final version Form 8941 on www.irs.gov. Both small businesses and tax-exempt organizations will use the form to calculate the credit. A small business will then include the amount of the credit as part of the general business credit on its income tax return.

Tax-exempt organizations will instead claim the small business health care tax credit on a revised Form 990-T. The Form 990-T is currently used by tax-exempt organizations to report and pay the tax on unrelated business income. Form 990-T will be revised for the 2011 filing season to enable eligible tax-exempt organizations – even those that owe no tax on unrelated business income – to claim the small business health care tax credit.

More Information

The resources listed below contain additional information about the tax credit:

- Final Form 8941: www.irs.gov/pub/irs-pdf/f8941.pdf
- General IRS information about PPACA: www.irs.gov/newsroom/article/0,,id=220809,00.html.
- Steps for determining eligibility for the credit: www.irs.gov/pub/irs-utl/3_simple_steps.pdf.
- Answers to frequently asked questions about the credit: www.irs.gov/newsroom/article/0,,id=220839,00.html

Source: Internal Revenue Service

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