

Small Employer Health Insurance Tax Credit

The health insurance reform package included an immediate tax break for small businesses: the small business health insurance tax credit. Qualified small employers, including nonprofit employers, may reduce the cost of providing health insurance to their employees this year. However, the credit is complex and there are important limitations, especially when calculating the number of employees and other provisions. Don't let the complexity of the credit discourage you from exploring its benefits. Please contact our office so we can explain in detail how the credit may help cut your health insurance costs.

Small employers. To be eligible, you must meet *all three* of the following requirements:

1. You must have fewer than 25 full-time equivalent employees (FTEs). (*see how to determine the number below*)
2. Your average employee wages must be less than \$50,000. (*see how to determine below*)
3. You must pay a uniform percentage for all employees receiving coverage, and this percentage must be at least 50% of the total premium cost of single (employee-only) coverage.

How long it's available. The Tax Credit became available beginning in 2010, and is only available for a limited time.

- From 2010 to 2013: The Tax Credit can equal up to 35% of allowed employer healthcare costs by eligible small businesses and 25% for qualifying tax-exempt organizations.
- From 2014 to 2016: The maximum tax credit will increase to 35% of premiums paid by eligible small and tax-exempt organizations – although many additional requirements will apply in those years.

Employees. To determine eligibility for the credit, employers have to calculate their number of FTEs. The number of an employer's FTEs is determined by dividing the total hours for which the employer pays wages to employees during the year (but not more than 2,080 hours for any employee) by 2,080. The result, if not a whole number, is rounded to the next lowest whole number. Lawmakers selected 2,080 hours because 2,080 hours comprise the number of hours in a 52-week assuming a 40-hour work week. Any hours beyond 2,080, such as overtime hours, are not taken into account when calculating FTEs. (*see attached example for calculation*)

Average annual wages. Employers also need to calculate average annual wages. The amount of average annual wages is determined by first dividing the total wages paid by the employer to employees during the employer's tax year by the number of the employer's FTEs for the year. The result is then rounded down to the nearest \$1,000 (if not otherwise a multiple of \$1,000).

Claiming the Credit. Eligible small businesses will use **Form 8941** to figure the credit and then include the amount of the credit as part of the general business credit on their income tax return. Tax-exempt organizations will use **Form 8941** to calculate their refundable tax credit, and then will claim the tax credit on Line 44f of **Form 990-T**. A tax-exempt organization can claim the Tax Credit, regardless of whether the organization is subject to the tax on unrelated business income. Generally Form 990-T is due by the 15th day of the 5th month after the organizations year-end.



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Please contact our office if you have any questions about the new small employer health insurance tax credit at 865-769-0660.

An Example

A local not-for-profit (NFP) has 2 full-time employees and 2 part-time employees. Employee 1 is paid \$35,000, employee 2 is paid \$25,000, and employee 3 and 4 are each paid \$12,500. The NFP has enrolled the 2 full-time employees in its health plan. The NFP pays 75% of the single employee-only premium, which is \$8,000 per employee, on behalf of each employee. The NFP pays \$18,000 for the coverage (\$6,000 per employee). The organization is located in Tennessee.

Calculate the FTEEs

Hours Worked: Employee 1 (2,080); Employee 2 (2,080), Employee 3, (1,040), Employee 4 (1,040).
Total hours: 6,240.

FTEEs: 3 (6,240 hours ÷ 2,080 hours)

Calculate average wages

Wages: \$35,000 + \$25,000 + \$12,500 + \$12,500 = \$85,000 aggregate wages.

Average Wages: \$85,000 ÷ 3 = \$28,333 per FTEE, rounded down to \$28,000. According to the table in the Appendix, the NFP is eligible for a credit of 20%.

Calculate premiums paid and Tax Credit

Employer Health Care Costs: \$12,000 (\$6,000 x 2).

Average Tennessee Premium: \$4,611, single coverage (family coverage is \$10,369). This limits the amount of premiums paid that can be counted toward the Tax Credit. The NFP can only claim 75% of \$4,611 (what it would have paid if the coverage were average Tennessee coverage) per employee. \$4,611 x 75% = \$3,458.25 x 2 = \$6,916.50 maximum premium limit.

2010 Tax Credit: **\$1,384** (20% x \$6,916.50). This amount is refundable as a credit as long as the NFP has withheld at least that much from employee wages combined with what the NFP has paid in employer Medicare taxes.



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