

Taking credit

How to take advantage of the new health insurance credit for small businesses

The recently passed Patient Protection and Affordable Care Act contains more than \$400 billion in revenue raisers and new taxes on employers and individuals. However, there are some significant tax breaks for small businesses contained in the bill, as well.

If a business has fewer than 25 full-time employees with average wages less than \$50,000 per year and contributes more than 50 percent of the cost of its employees' health insurance, the business may be eligible for a new tax credit that was enacted as part of the Health-care Reform package President Obama recently signed.

Smart Business recently talked with Tasca Russo of Habif, Arogeti & Wynne about credits that businesses can take advantage of now.



Tasca Russo
Senior tax manager
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What are the criteria for eligibility?

Any business is eligible for the credit as long as it meets the following eligibility requirements:

- The business cannot have more than 25 full-time employees (defined below).
- It must have employees earning average annual wages equal to or less than \$50,000 (for years 2010 through 2013).
- It must contribute more than 50 percent of the employees' health insurance premiums.

Businesses employing more than the 25 people could qualify if some of the total number of employees are part-time. The total number of full-time employees is calculated by taking the total number of hours worked by all employees, both full and part time, and dividing by 2,080.

For example: ABC Company had 12 employees who each had 2,080 hours of service (i.e., 40 hours a week for 52 weeks) and four employees who each had 1,560 hours of service. The total hours of service is:

$[(2,080 \times 12) + (1,560 \times 4)]$ or (24,960 + 6,240) or 31,200 hours.

This amount (31,200) divided by 2,080 is 15.

ABC Company has 15 full-time employees.

If an employee works more than the annual 2,080 hours during the year, the

excess is not taken into account for this calculation. However, any overtime pay for an employee paid hourly is taken into consideration for the average wages paid.

Leased employees are included but seasonal workers are only included if they work more than 120 days during the tax year.

Certain employees such as more than 2 percent shareholders, 5 percent owners, self-employed individuals, partners, sole proprietors and persons related to them are not eligible for the credit and thus not taken into account in determining the total number of full-time employees.

How large is the credit?

Only the amount of insurance premiums paid by the employer, and not paid by the employee, are used in calculating the credit. For tax years beginning in 2010 through 2013, the credit is 35 percent of the employer's contributions toward the employee health insurance premiums. For years beginning after 2013, the credit increases to 50 percent.

For example: In 2010, an auto repair shop has 10 employees. The total

amount of wages paid to the employees is \$250,000. The average annual wages are \$25,000. If the auto repair shop pays employee health care costs of \$70,000, its 2010 tax credit is \$24,500 (35 percent \times \$70,000).

The credit begins to phase out as the number of full-time employees and average wages increase and is completely phased out once there are either more than 25 employees or average annual wages exceed \$50,000.

An adjustment to health insurance premiums deducted as an ordinary business expense must be made for those premiums taken with regard to this credit.

For example: In year 2014, employer XYZ Company is entitled to a \$4,000 small employer health insurance credit as a result of making \$8,000 of nonelective contributions for premiums for qualified health plans on behalf of its two FTE employees. XYZ Company has to reduce its otherwise allowable deduction for employee health insurance expenses by the amount of the small employer health insurance credit to \$4,000 (\$8,000 minus \$4,000).

How do eligible companies claim the credit?

The small employer health insurance credit is claimed as part of the general business credit and is not a refundable credit. The credit can only be used to offset a regular tax liability, not alternative minimum tax. The credit can be carried back one year and any unused carried forward 20 years.

For a tax-exempt entity, instead of being a general business credit, the small business health insurance credit is a refundable credit and can be used to obtain a refund of payroll withholding taxes. <<

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