

Understanding the Small Employer Tax Credit for Health Care Coverage Questions and Answers for Those Considering the Credit

When is the new tax credit available? Now. The credit may be claimed on an employer's 2010 annual tax filing for any months the employer qualified for the credit and purchased health insurance for their employees.

How long will the credit last? Employers may be eligible for the credit through 2016.

Who qualifies for the credit? In general, employers must meet the following to qualify for the credit:

- employ 25 or fewer full-time equivalent employees (FTEs);
- pay average annual wages of less than \$50,000; and
- pay at least 50% of the premium costs for their employees

Do tax-exempt employers qualify? Yes, tax-exempt employers with 25 or fewer FTEs with average annual wages less than \$50,000 qualify for the credit, but the overall value of credit is lower for tax-exempt employers.

How much is the tax credit worth? The credit has a maximum value of 35% of eligible premiums paid. Employers with 10 or fewer FTEs with lower than \$25,000 in average annual salaries qualify for the maximum eligible premium credit. The value of the credit is reduced as the number of FTEs and/or average annual salaries increase until employer size exceeds 25 FTEs, or average annual salaries exceed \$50,000.

The maximum value of credit for tax-exempt employers is 25% of eligible premiums paid, and is subject to the same sliding scale as described above for all other eligible employers.

What are "eligible" premiums? The Secretary of the Department of Health and Human Services will annually identify the cost of the average small employer health insurance premium in each state. When determining the amount of the credit, only premiums paid up to the state average will be considered. For example, if the Secretary determines the average monthly small employer premium in Washington is \$275 per employee, and the health plan you purchase is \$350 per employee per month, the value of the credit you receive will be based on the state average of \$275, rather than the \$350 you actually paid.

How do I calculate how many "full-time equivalent (FTE)" employees I have? To determine whether you qualify for the tax credit based on your employer "size" divide the total number of hours you paid wages to employees during the year (but not more than 2,080 hours for any one employee) by 2,080. Do not include hours paid to seasonal employees in the calculation.

How do I calculate the average annual wages I pay? To determine the average annual wage paid, divide the total wages (as defined for FICA purposes) you paid to employees during the tax year by the number of FTEs calculated for the year (round down to the nearest \$1,000) (excluding wages paid to seasonal employees).

Should I include all employees I pay in the calculation of FTEs and salaries? No. Do not include in either the FTE or salary calculations: any employees that meet the federal definition of a seasonal employee; partners in a partnership; shareholders owning more than 2% of an S corporation; any owner owning more than 5% of a business; or family members of any of the owners or partners in the business.

Can I still receive the tax credit if I provided health insurance prior to passage of the new law? Yes. The credit may be claimed for premiums paid during the 2010 tax year.

Must I provide health insurance for all of my employees to receive the credit? The law is currently silent on this issue and states only that the credit is based on premiums paid by the eligible employer.

I have more than 25 employees but some of them are part-time and do not qualify for coverage. Am I still eligible to receive the credit? Possibly. Eligibility is not determined by the number of employees with insurance – it is determined by how many FTEs you employ. Employers with 25 or fewer FTEs are eligible for the credit, regardless of how many are offered insurance.

The current federal tax deduction I receive for providing health insurance saves me thousands in taxes each year. Will I lose this deduction if I take the tax credit? You may still be eligible for the tax deduction as well. However, when determining the deduction amount for premiums paid, the amount must be reduced by the value of the tax credit you receive. Employers will want to carefully evaluate the actuarial benefit of the tax credit versus receiving the full amount of the tax deduction to determine whether they receive more benefit from the credit or the deduction before applying for the credit. A miscalculation could result in the payment of much higher federal taxes.

The IRS says to be eligible for the tax credit I only have to pay 50% of the premium costs. Why are insurers telling me I have to pay 75% of the premium costs? Insurers in Washington have set a standard that requires employers to pay 75% of the premium costs. This is neither a state nor federal law but an industry standard. Thus, until either the feds or the state tells insurers they may no longer impose such a standard, employers in Washington must pay a higher portion of the premiums for their employees than what eligibility for the credit requires.

Please contact Donna Steward (1-800-521-9325 or donnas@awb.org) if you have further questions.