

# Bridging the Gap Between Small Business Owners and the Health Care Tax Credit

by Chris Patton

Small business owners are interested in health care and ways to pay for it. They are making inquiries to insurance agents, tax preparers, and the state exchange program, [Covered California for Small Business](#).

The number of small businesses that are capitalizing on the small business health care tax credit is rising with the exchange program now in its third year and expansive outreach efforts underway. For many, the tax-credit topic had been a non-starter with various barriers for agents and their clients. But now, small business owners seem willing to discuss health care benefits—many for the first time. The tax credit has been the catalyst for this conversation for many agents. With tax filing deadlines looming, there is no better time for agents to use this opportunity to increase their client base.

## **The Small Business Health Care Tax Credit In ACA's Early Years**

The Affordable Care Act provides a tax credit for small businesses [enrolled](#) in a public exchange. It offsets the premium paid by the employer dollar-for-dollar. The tax credit offsets health insurance premiums by 50% to for-profit companies and 35% for non-profit organizations.

According to the IRS, non-profit companies that don't incur a tax liability get the credit as a refund as long as the refund amount does not exceed their income tax and Medicare withholdings.

The small business [health care tax credit](#) was one of the first benefits of the ACA, becoming effective to small business owners on January 1, 2010. The tax credit was an incentive to encourage small businesses (25 or fewer full-time employees) to provide health insurance to their workers. In return for helping to increase the availability of affordable health care, the IRS offered small business owners premium relief in the form a tax credit, reducing their tax liability.

At the time that it was offered, the Council of Economic Advisors estimated that up to 4 million small businesses in the country were eligible. The Congressional Budget Office estimated that the tax credit would save small businesses nearly \$40 billion by 2019.

Federal regulators have worked hard to bring attention to the tax credit program. The [IRS](#) initiated several programs to educate small business owners and their advisors. Beginning in 2010, IRS representatives hosted small business forums and tax workshops; sent e-mails to more than 175,000 tax professionals; and mailed millions of postcards to urging small business owners to consider the health care tax credit.

Despite the outreach, only 170,300 small businesses claimed the tax credit for the first year of the program, according to the Government Accountability Office (GAO). The total amount claimed for tax year 2010 was \$468 million, with small businesses receiving an average of \$2,748 to offset their overall tax liability. The small business tax credit was not adopted as widely as anticipated because the calculation was too complicated or cumbersome. At the start of the tax credit program, the IRS and some of the larger tax software providers did not yet provide tools for employers and consultants to calculate the tax credit (e.g. counting full-time equivalent employees, average wages, or qualifying health insurance premiums).

Additionally, many businesses that were eligible for the tax credit were not aware of the opportunity. They may have been overwhelmed with the responsibility of filing taxes on their own and left with little resources to incorporate the services or knowledge of a certified tax preparer.

For many small businesses, access to the tax credit was also hindered by narrowly defined eligibility requirements. Beginning January 1, 2014, the program mandated that small businesses enroll in a public health care exchange in order to qualify for the tax credit, whether state-run or federally facilitated.

Throughout the nation, the ACA's small business public health care exchanges were launched as the Small Business Health Options Program (SHOP). In California, SHOP was renamed as "Covered California for Small Business" to capitalize on Covered California's brand recognition and bring greater awareness of the small business program to the public. However, a less-than-ideal launch of the federal and many state exchange programs slowed the tax credit adoption rate.

As reported by the GAO, SHOP programs were operational nationwide, but many features were not initially available, and enrollment had been lower than anticipated. Many small businesses did not enroll because they were apprehensive about joining an unestablished program.

In addition, there were misconceptions that the tax credit was only available for two particular years: 2014 and 2015. The tax credit is available for any two consecutive tax years for eligible small businesses that are enrolled in a public health exchange. However, tax year 2016 is the last year that a group that has not taken advantage of the program can benefit from three years of tax credits.

To achieve this, a small business owner would need to have been enrolled in a qualified health insurance program and enrolled in a public exchange program in the two subsequent years beginning in 2014. In this example, the small business owner could file an amended return this year for the 2013, 2014, and 2015 tax years. They would get the health care tax credit all three years if they met the participation requirements.

With respect to claiming a past year's tax credit, an article from CPA Advisor says, "Businesses that have already filed and later find that they qualified in 2013 or an earlier year can still claim the credit by filing an amended return for the affected years." The IRS says that the small business owner must make a refund claim within three years from when they filed their taxes or within two years of paying associated taxes, whichever period is longer.

### **So how does the small business health care tax credit work?**

The following are conditions for a small business to be eligible for the tax credit:

- Employ fewer than 25 full-time equivalent employees.
- Contribute at least 50% of the employees' premium cost.
- Pay an average salary of less than \$52,000 per year in 2015 (excluding owners and family members). This amount is adjusted annually for inflation. Small business owners should consult with a tax advisor for a definition of those excluded.

The tax credit is available on a sliding scale, providing a lesser benefit to groups that increase in employee count or average annual salary. The sweet spot for the tax credit is with companies with 10 employees or fewer with an average of \$25,000 in annual salary or less. The table below illustrates how a small business can reduce their premium by 50% through

the tax credit when they offer health insurance through a public exchange program:

<b>Example of Small Business Receiving Maximum Tax Credit for Health Insurance</b>	
<b>Employees</b>	<b>10</b> full-time-equivalent employees
<b>Wages</b>	<b>\$250,000</b> total, or an average of \$25,000 per employee
<b>Employee Health Insurance Cost</b>	<b>\$70,000</b>
<b>Tax Credit (Year 1)</b>	<b>\$35,000</b> (50%)
<b>Tax Credit (Year 2)</b>	<b>\$35,000</b> (50%)
<b>Tax Credit (Year 3)</b>	<b>Not eligible for tax credit</b>

The other good news is that it has gotten easier to claim the tax credit. Now calculations for estimating the tax credit are supported by tax software vendors as well as the IRS and many of the exchanges, including Covered California for Small Business. A simple one-page tax form (8941) is all that is required to file.

In many markets, including California, the fastest growing public and private exchanges are those with multiple carriers and plan offerings in different metallic tiers. Now that the public exchange is operating on par with private exchanges, in many cases, there is no reason to not look to exchanges for coverage. When considering the advantage of a tax credit, public exchanges offer small employers a way to reduce premium costs while providing competitive health insurance options that attract and retain quality talent.

As a quick note, you must be very careful not to offer tax advice, especially if you are not certified as a tax preparer. There is a fine line between tax advice and a health insurance consultation. Just as with HSA plans and MSA plans before them, health insurance and tax law is woven together. As insurance professionals, we have to bridge the gap among many business advisory disciplines. The small business tax credit offers a chance for agents to expand their practice and help small businesses, many of which might be first-time insurance buyers.



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Chris Patton has more than 15 years of industry experience in the California market with knowledge of the retail and wholesale distribution of group health insurance products. As the vice president of Sales for

[Covered California for Small Business](#), Chris and his team are staffed statewide to support the role of Covered California's [certified insurance agent community](#) and to ensure the successful and ongoing distribution of California's small business public exchange program.