

## WHAT YOU NEED TO KNOW



## Highlights of the Small Employer Tax Credit

Updated December 2018

Very small employers with a high percentage of employees who earn low wages are eligible for a tax credit for employer contributions made to purchase health insurance. Non-profit organizations also are eligible – they will receive the credit as an offset to their payroll taxes. Governmental entities are not eligible unless they qualify as 501(c) organizations.

### Eligibility

The tax credit is only available to employers if they satisfy these requirements:

- Have 25 or fewer full-time equivalent employees.
- The average annual wage per employee is \$50,000 or less (indexed annually for inflation; \$51,000 in 2014, \$52,000 in 2015, \$52,000 in 2016, \$53,000 in 2017, and \$54,000 in 2018).
- The employer makes a uniform contribution for covered employees of at least 50 percent of the cost of single coverage. (The employer does not need to contribute toward the cost of dependent coverage or offer dependent coverage.)
- Since 2014, employers must have purchased coverage through the SHOP Marketplace. In many states, SHOP coverage must be provided directly from a carrier, rather than through the Marketplace, but SHOP coverage still must be purchased to be eligible for the tax credit. Certain counties have no SHOP option—the SHOP requirement is waived for employers located in those counties. Employers in Hawaii cannot participate in the SHOP Marketplace or claim the tax credit for health plan years beginning after 2016.

Eligible health insurance includes medical, dental, vision, long term care, specified disease, hospital indemnity, and Medicare supplement policies. Because only health insurance is eligible for the credit, contributions toward self-funded plans, health reimbursement arrangements, health savings accounts, flexible spending accounts, or flex credits are not included. Employer contributions for meeting wellness incentives may be included.

Controlled group rules apply so all employees employed by employers in a controlled group or an affiliated service group must be considered when determining the number of full-time equivalent employees and the average wage.

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## Effect of Sequestration

Due to the Balanced Budget and Emergency Deficit Control Act of 1985, refund payments issued to some small tax-exempt employers claiming the refundable portion of the Small Business Health Care Tax Credit are subject to [sequestration](#). Thus, refund payments processed on or after October 1, 2015, and on or before September 30, 2016, will be reduced to 6.8 percent (the 2016 sequestration rate).

## Credit Amount

Since 2014, the maximum credit for businesses is 50 percent of the employer's contribution for health insurance. For tax-exempt organizations, the maximum credit is 35 percent. However, the employer premium on which the credit is determined may not exceed the average cost of coverage in the small group market of the employee's rating area.

## 2018 State Average Premiums for Small Group Markets

The [2018 Instructions for Form 8941](#) lists the average premiums for the small group market by county for each state. Please reference these tables for further details.

State	Single coverage (employee only)	Family coverage	State	Single coverage (employee only)	Family coverage
Alabama	\$6,564	\$17,213	Montana	\$7,253	\$16,413
Alaska	10,250	27,554	Nebraska	6,750	18,264
Arizona	6,329	17,630	Nevada	7,024	16,694
Arkansas	5,735	15,440	New Hampshire	7,363	20,071
California	6,623	16,754	New Jersey	7,633	19,942
Colorado	7,374	17,448	New Mexico	6,947	20,711
Connecticut	7,439	20,594	New York	7,246	18,657
Delaware	7,718	19,563	North Carolina	7,070	18,681
District of Columbia	6,547	20,896	North Dakota	6,966	17,708
Florida	6,690	18,822	Ohio	7,343	18,865
Georgia	6,570	17,837	Oklahoma	6,643	17,297
Hawaii	6,207	16,824	Oregon	6,779	16,213
Idaho	5,444	14,808	Pennsylvania	6,927	18,249
Illinois	6,522	18,855	Rhode Island	7,217	20,932
Indiana	6,950	19,469	South Carolina	6,418	18,120
Iowa	6,593	17,174	South Dakota	7,062	17,657
Kansas	5,934	17,279	Tennessee	5,933	14,812
Kentucky	6,255	17,514	Texas	7,175	17,000
Louisiana	6,723	17,438	Utah	6,627	18,441
Maine	6,253	16,586	Vermont	6,408	18,237
Maryland	6,223	16,765	Virginia	6,319	16,726
Massachusetts	7,901	20,271	Washington	6,245	17,558
Michigan	6,439	18,814	West Virginia	7,099	18,595
Minnesota	6,246	18,503	Wisconsin	6,811	19,299
Mississippi	6,404	14,982	Wyoming	7,959	20,776
Missouri	6,726	15,489			

Source: IRS Form 8941

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The credit is only available for two consecutive years since 2014. A partial year counts as a full year toward the two-year limit. Under a special rule, a non-calendar year plan may use the increased credit percentage for all of 2014.

The credit phases out for employers with more than 10 full-time equivalent employees and whose employees have average wages of \$25,000 or more (indexed to \$25,400 for 2014, \$25,800 for 2015, \$25,900 for 2016, \$26,200 for 2017, and \$26,600 for 2018) and is fully phased out when average wages exceed \$50,000 (indexed to \$50,800 for 2014, \$51,600 for 2015, \$51,800 for 2016, \$52,400 for 2017, and \$53,200 for 2018).

## Small Business Tax Credit as a percent (maximum of 50%) of employer contribution to premiums – For-profit firms in 2014 and after

Firm size	Average Wage					
	Up to \$25,000	\$30,000	\$35,000	\$40,000	\$45,000	\$50,000
Up to 10	50%	40%	30%	20%	10%	0%
11	47%	37%	27%	17%	7%	0%
12	43%	33%	23%	13%	3%	0%
13	40%	30%	20%	10%	0%	0%
14	37%	27%	17%	7%	0%	0%
15	33%	23%	13%	3%	0%	0%
16	30%	20%	10%	0%	0%	0%
17	27%	17%	7%	0%	0%	0%
18	23%	13%	3%	0%	0%	0%
19	20%	10%	0%	0%	0%	0%
20	17%	7%	0%	0%	0%	0%
21	13%	3%	0%	0%	0%	0%
22	10%	0%	0%	0%	0%	0%
23	7%	0%	0%	0%	0%	0%
24	3%	0%	0%	0%	0%	0%
25	0%	0%	0%	0%	0%	0%

**Source:** CRS analysis of PPACA (P.L. 111-148)

The credit also discounts any state-provided tax credit or subsidy.

## Counting Employees

Common law employees employed during the year must be counted, including part-time employees, former employees terminated during the year, and employees who do not enroll in the health insurance plan (whether they are covered under another plan). Seasonal workers are not taken into account unless they work more than 120 days during the tax year. Leased employees are counted only if they worked for the employer for at least one year. Sole proprietors, partners, more-than-two-percent shareholders of an S-corporation, more-than-five-percent shareholders of an organization that is not an S-corporation, and their family members and tax dependents are not considered employees.

An employer may count hours of includable employees using any of three methods – actual hours worked (including overtime, but not more than 2,080 hours per year), crediting an employee with a full day (eight hours) for each day the employee works one hour, or crediting an employee with a full workweek (40 hours) for each week in which the employee works one hour. Employees must be credited both with hours actually

worked and hours for which the employee was paid (such as for vacation, holidays and sick days). An employer may use different methods of calculating hours for different classifications of employees.

The number of full-time equivalent employees (FTEs) is generally calculated by dividing the total hours worked by all includable employees during the year by 2,080 and rounding down to the nearest whole number (but not less than 1).

**Example:** For the 2018 taxable year, Acme Co. pays five employees wages for 2,080 hours each, three employees wages for 1,040 hours each, and one employee wages for 2,300 hours. Acme uses a method that counts hours actually worked. The employer's FTEs would be calculated as follows:

10,400 hours for the five employees paid for 2,080 hours (5 x 2,080)  
3,120 hours for the three employees paid for 1,040 hours (3 x 1,040)  
2,080 hours for the one employee paid for 2,300 hours (lesser of 2,300 and 2,080)

The total hours counted is 15,600 hours. Acme has seven FTEs (15,600 divided by 2,080 = 7.5, rounded to the next lowest whole number).

## Calculating Wages

When calculating the average annual wages, the employer must use wages subject to Social Security payroll taxes (FICA), but without the Social Security wage base limitation. To calculate the average wages paid, the total annual wages paid to employees taken into account in the FTE calculation is divided by the number of FTEs, and rounded down to the nearest \$1,000.

**Example:** For the 2018 taxable year, Case Bros. pays a total of \$224,000 in wages to employees and has 10 FTEs. Case Bros.' average annual wages are \$22,000 ( $\$224,000 / 10 = \$22,400$ , rounded down to the nearest \$1,000).

## Contribution Levels

The employer must make a "uniform" contribution on behalf of each employee who is enrolled in health insurance. Employers with only one plan option and a composite rate must contribute at least 50 percent of the cost of single coverage. If the plan has a tobacco surcharge or a wellness incentive, the employer contribution rate must be based on the cost a smoker or a person who does not participate in the wellness program would pay. Employers that list bill may either contribute the same percentage (not less than 50 percent) of each employee's premium, or determine a composite premium and contribute at least 50 percent of the composite premium for each participating employee. Employers that offer family coverage do not need to contribute the same amount or any amount for dependents which do not live in the home. They may receive a credit for those contributions. The rules provide several ways to meet the uniform contribution requirement if the employer offers more than one plan or multiple tiers.

If state or local laws require an added contribution for certain types of employees, that employer contribution will not violate the uniformity requirement.

Although a seasonal employee who works fewer than 120 days is disregarded when calculating the number of full-time equivalent employees and the average wage, if the employer provides coverage to a seasonal employee, it is entitled to a credit on that contribution.

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## Claiming the Credit

For-profit employers must file IRS [Form 8941](#) with their tax return to claim the credit. The credit may be used toward their regular or the alternative minimum tax. Tax-exempt organizations must file [Form 990-T](#) and attach Form 8941. Their credit will be applied against their payroll taxes.

## Additional Resources

The IRS has created an online [tax credit estimator](#) and a comprehensive [FAQ](#) which may be helpful. [Instructions](#) for Form 8941 also are available.

See also the IRS [Small Business Health Care Tax Credit Questions and Answers: Calculating the Credit](#).

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