Several readers have asked me to comment on the new health care act and how it relates to small businesses. Specifically, are there any benefits to the small business in the recently enacted Affordable Care Act? We have seen several pieces in the press about this, but what really is there for the small business owner. To answer this, I asked Ann Makres, Senior Stakeholder Liaison in the Bloomington (Twin Cities office) of the Internal Revenue Service for help.

There are two major pieces that have implications for small businesses. First, health coverage provided for an employee's children that are under 27 years of age is now generally tax-free to the employee, effective March 30, 2010. This means that these changes immediately allow employers with cafeteria plans — plans that allow employees to choose from a menu of tax-free benefit options and cash or taxable benefits — to permit employees to begin making pre-tax contributions to pay for this expanded benefit. IRS Notice 2010-38 explains these changes and provides further guidance to employers, employees, health insurers and other interested taxpayers.

“These changes give employers a unique opportunity to offer a worthwhile benefit to their employees,” IRS Commissioner Doug Shulman said. “We want to make it as easy as possible for employers to quickly implement this change and extend health coverage on a tax-favored basis to older children of their employees.”

This expanded health care tax benefit applies to various workplace and retiree health plans. It also applies to self-employed individuals who qualify for the self-employed health insurance deduction on their federal income tax return. The notice says that employers with cafeteria plans may permit employees to immediately make pre-tax salary reduction contributions to provide coverage for children under age 27, even if the cafeteria plan has not yet been amended to cover these individuals. Plan sponsors then have until the end of 2010 to amend their cafeteria plan language to incorporate this change.

The second implication for small businesses is the new health reform law gives a tax credit to certain small employers that provide health care coverage to their employees, effective with tax years beginning in 2010. The eligibility rules for qualifying for this credit include:

- The employer must cover at least 50 percent of the cost of health care coverage for some of its workers based on the single rate.
- The employer must have less than the equivalent of 25 full-time workers (for example, an employer with fewer than 50 half-time workers may be eligible).
- The employer must pay average annual wages below $50,000.
Both taxable (for profit) and tax-exempt firms qualify.

The credit is worth up to 35 percent of a small business' premium costs in 2010. On Jan. 1, 2014, this rate increases to 50 percent (35 percent for tax-exempt employers). But note that this credit phases out gradually for firms with average wages between $25,000 and $50,000 and for firms with the equivalent of between 10 and 25 full-time workers.

The IRS gave the following examples:

Example 1: An Auto Repair Shop with 10 employees with wages of $250,000 total, or $25,000 per worker and employee Health Care Costs of $70,000 would receive a 2010 Tax Credit of $24,500 (35% credit) and a 2014 Tax Credit: of $35,000 (50% credit)

Example 2: A Restaurant with 40 Half-Time employees (the equivalent of 20 full-time workers) with wages of $500,000 total, or $25,000 per full-time equivalent worker and employee Health Care Costs of $240,000 would receive a 2010 Tax Credit of $28,000 (35% credit with phase-out) and a 2014 Tax Credit: $40,000 (50% credit with phase-out)

Details on these and other Affordability Care Act provisions can be found on www.IRS.gov.

To learn more about management of a small business, contact SCORE for free and confidential business mentoring and coaching. We are "Counselors to America’s Small Businesses."

Dean L. Swanson
South East Minnesota SCORE
c/o Rochester Area Chamber of Commerce
220 South Broadway, Suite 100
Rochester, MN 55904
*Dean is a volunteer SCORE Counselor.