

Claiming the Health Coverage Tax Credit for 2014 and 2015

Notice 2016-02

SECTION 1. PURPOSE

This notice provides guidance regarding the health coverage tax credit (HCTC) under § 35 of the Internal Revenue Code, as modified by the Trade Preferences Extension Act of 2015, Pub. L. 114-27 (June 29, 2015) (Extension Act). This notice provides information on who may claim the HCTC, the amount of the HCTC, and the procedures to claim the HCTC for tax years 2014 and 2015. This notice also provides guidance for taxpayers eligible to claim the HCTC who enrolled in a qualified health plan (QHP) offered through a Health Insurance Marketplace (Marketplace, also known as an Exchange) in tax years 2014 or 2015, and who claimed or are eligible to claim the premium tax credit (PTC) under § 36B (including taxpayers who received the benefit of advance payments of the PTC (APTC)).

SECTION 2. BACKGROUND

In General

Section 35 was originally enacted by the Trade Act of 2002, Pub. L. 107-210 (August 6, 2002), was amended multiple times, and expired at the end of 2013. However, § 35 was reinstated, modified, and extended through 2019 by the Extension Act.

Section 35(a) provides that the HCTC is 72.5 percent of the amount paid by an eligible individual for qualified health coverage of the individual and qualifying family

members for eligible coverage months.

Notice 2005-50, 2005-2 C.B. 14, provides guidance on various issues relating to the HCTC, including information about eligibility for the HCTC, qualifying health coverage for purposes of the HCTC, and computation of the HCTC. Taxpayers may continue to rely on Notice 2005-50, except as provided below.

Eligibility for the HCTC

Section 35(b) provides that an individual has an eligible coverage month if, as of the first day of the month, the taxpayer: (1) is an eligible individual, (2) is covered by qualified health coverage, the premium for which is paid by the taxpayer, (3) does not have other specified coverage, and (4) is not imprisoned under Federal, State, or local authority. These rules are described more fully below.

Eligible Individuals and Qualifying Family Members. There are three categories of eligible individuals. Eligible individuals are: (1) eligible trade adjustment assistance (TAA) recipients (individuals eligible for trade adjustment assistance under a program administered by the Employment and Training Administration of the U.S. Department of Labor), (2) eligible alternative TAA (ATAA) recipients and reemployment TAA (RTAA) recipients (individuals eligible for alternative or reemployment trade adjustment assistance under a program administered by the Employment and Training Administration of the U.S. Department of Labor), and (3) eligible Pension Benefit Guaranty Corporation (PBGC) pension recipients (individuals who are at least age 55 and who are receiving a benefit any portion of which is paid by the PBGC). Whether someone is an eligible individual is determined on a month-by-month basis.

An eligible individual may claim the HCTC for his or her qualifying family

members. Qualifying family members are the eligible individual's spouse and any person the eligible individual can claim as a dependent on the eligible individual's federal income tax return. Qualifying family members do not include an individual with other specified coverage (described below), or, in the case of divorced parents, a child of a noncustodial parent.

In general, an individual is an eligible individual for a month if the relevant benefit is received, or the individual is entitled to the relevant benefit, in any day in that month or in the prior month.

Qualified Health Coverage. Section 35(e) describes eleven categories of qualified health coverage. Seven categories are qualified coverage only if a state government elects for them to be qualified and the coverage meets certain requirements. The other four categories of qualified health coverage are Consolidated Omnibus Budget Reconciliation Act (COBRA) continuation coverage, coverage under a group health plan that is available through the eligible individual's spouse, coverage in the individual market, and coverage under certain employee benefit plans funded by a voluntary employees' beneficiary association. Qualified health coverage does not include flexible spending or similar arrangements, nor does it include insurance if substantially all of its coverage is of excepted benefits described in § 9832(c).

The Extension Act did not eliminate any coverage from the list of qualified health coverage – all prior qualified health coverage remains qualified. The Extension Act added individual health insurance through the Marketplace as qualified health coverage for coverage months in 2014 and 2015 taxable years. However, coverage through the Marketplace is not qualified health coverage for months in taxable years beginning after

2015. In addition, the Extension Act removed the requirement that applied for taxable years before 2014 that individual market coverage must start at least 30 days before the taxpayer becomes separated from employment to be qualified health coverage.

To learn more about qualifying coverage for the HCTC, go to www.irs.gov/HCTC.

Other Specified Coverage. In general, individuals otherwise eligible for the HCTC cannot receive the HCTC if they were enrolled in or had access to certain government-provided health insurance coverage, or were enrolled in or had access to health insurance coverage maintained by any employer (or former employer) of the taxpayer or the taxpayer's spouse and the employer subsidized 50 percent or more of the cost of coverage.

Eligibility for the HCTC is described more fully in Notice 2005-50 and the instructions for Form 8885, *Health Coverage Tax Credit*. The IRS has updated Form 8885 and its instructions for tax year 2015. The rules described in the updated instructions for tax year 2015 apply for tax years 2014 and 2015.

Electing the HCTC

Under § 35(g)(11), for coverage months in taxable years beginning after December 31, 2013, an eligible individual must make an election to claim the HCTC. The election must be made annually, applies to all subsequent coverage months in the taxable year for which the taxpayer is eligible to take the HCTC, and is irrevocable for all such coverage months. In general, the election must be made by the due date of the tax return (including extensions) for the applicable taxable year. However, an HCTC election may be made within the 3-year period of limitation prescribed in § 6511(a) (generally 3 years from the date a return is filed) for a taxable year beginning after

December 31, 2013 and before June 29, 2015. Thus, for example, a calendar year taxpayer who filed his 2014 return on April 15, 2015, must claim the HCTC for 2014 by filing an amended 2014 return by April 17, 2018 (an extended date because April 15, 2018, will fall on a weekend).

Advance Payment of the HCTC

The Extension Act reauthorized monthly advance payments of the HCTC as provided under § 7527. Section 7527(a) provides that the Secretary shall establish the HCTC advance payment system not later than 1 year from the date of enactment of the Extension Act (which was June 29, 2015).

SECTION 3. ELIGIBLE INDIVIDUALS ENROLLED IN A QHP THROUGH THE MARKETPLACE

The Premium Tax Credit (PTC)

Section 36B allows a PTC to applicable taxpayers to help individuals and families afford the cost of premiums for QHPs purchased through the Marketplace. In general, an individual is an applicable taxpayer if the individual's household income is at least 100% but not more than 400% of the Federal poverty line for the individual's family size, no one can claim the individual as a dependent, and if married, the individual files a joint return.

Individuals who receive the benefit of APTC, and individuals who do not receive the benefit of APTC but who wish to claim the PTC, are required to file Form 8962, *Premium Tax Credit (PTC)*, and attach it to their tax return (Form 1040, 1040A, or 1040NR).

Interaction of the HCTC and the PTC

A QHP offered through the Marketplace is qualified health coverage for the HCTC for months in taxable years beginning in 2014 or 2015. Therefore, an individual enrolled in a QHP who is both an eligible individual for purposes of the HCTC and eligible for the PTC in a month may claim either the HCTC or the PTC for the month.

Once the HCTC election is made for an eligible coverage month, the individual is ineligible to claim the PTC for the same coverage in that coverage month and for all subsequent months in the taxable year for which the individual is eligible for the HCTC. Thus, for example, if for every month of 2014 a taxpayer was enrolled in coverage through the Marketplace and was HCTC-eligible, the taxpayer could elect the HCTC beginning in July. The election would apply to coverage for July through December, and the taxpayer could claim the PTC for coverage for January through June. If the taxpayer's HCTC eligibility instead ended in August, the election would apply for coverage for July and August only, and the taxpayer could claim the PTC for coverage for September through December.

The HCTC election prevents a taxpayer from claiming both the PTC and the HCTC for the same month for the same coverage. However, a taxpayer may claim the PTC and the HCTC in the same month for different coverage. For example, if a taxpayer elects the HCTC for self-only coverage for a month, the taxpayer may claim the PTC for Marketplace coverage of the taxpayer's family members for that same month, if otherwise eligible to claim the PTC.

A unique situation arises if qualifying health coverage covers individuals eligible for the HCTC in addition to other individuals for whom the HCTC is not elected. Q&A3 of Notice 2005-50 provides that if qualifying health coverage covers eligible individuals,

qualifying family members, and individuals who are neither eligible individuals nor qualifying family members (nonqualifying beneficiaries), then qualifying health coverage premiums are allocated on an incremental basis, attributing amounts first to the eligible individuals and qualifying family members before allocating amounts to nonqualifying beneficiaries. Section 36B and its accompanying regulations, issued after Notice 2005-50, include special rules for allocating premium amounts when a QHP covers individuals in more than one tax family. See § 1.36B-3(h). For simplicity, to determine the allowable HCTC, taxpayers should apply the rules under § 36B to allocate premium amounts and APTC among tax families instead of the rule described in Q&A3 of Notice 2005-50. Accordingly, if the individuals enrolled in a QHP belong to different tax families, one family may claim the HCTC for the HCTC-eligible individuals in the plan, and the other family may claim the PTC for the other individuals enrolled in the plan, and each family determines their portion of the enrollment premiums and APTC using the allocation rules provided under § 36B. Notice 2005-50 is modified to the extent its rules are inconsistent with this paragraph. See Q&A9, below.

In general, a taxpayer with APTC in excess of allowable PTC must repay the difference as additional tax. Although the amount of additional tax that must be repaid may be limited by § 36B(f)(2), the repayment limitations in § 36B(f)(2) do not apply to coverage for 2014 or 2015 if the taxpayer elects the HCTC for any month in that year for that coverage. Therefore, a taxpayer who elects the HCTC for coverage in 2014 or 2015 and who received the benefit of APTC for that coverage must repay all APTC in excess of allowable PTC.

SECTION 4. FREQUENTLY ASKED QUESTIONS

Q1. I already filed my tax year 2014 return. I was eligible for and wish to claim the HCTC for coverage in 2014. May I amend my return and retroactively claim the HCTC for coverage for 2014?

Yes. File Form 1040X, *Amended U.S. Individual Income Tax Return*, to make the election and claim the HCTC. You generally have 3 years after you timely file your original return to make the election on an amended return. See “Health coverage tax credit (HCTC) for 2014” in the instructions for Form 1040X for information on how to claim the HCTC on Form 1040X, including special instructions for completing Form 8885.

Q2. I have not yet filed my tax year 2014 return. I was eligible for and wish to claim the HCTC for coverage in 2014. May I claim the HCTC on an original tax year 2014 return?

No. File your original tax year 2014 return first without claiming the HCTC and then file an amended 2014 return to claim the HCTC. See “Health coverage tax credit (HCTC) for 2014” in the instructions for Form 1040X for information on how to claim the HCTC on Form 1040X, including special instructions for completing Form 8885.

Q3. I was eligible for and wish to claim the HCTC for coverage in 2015. How will I claim the HCTC for tax year 2015?

You will be able to claim the HCTC on your original 2015 return by filing the 2015 Form 8885 with your return.

Make the HCTC election on line 1 of Form 8885 for the first coverage month you are electing to take the HCTC. Once you elect to take the HCTC for a month in a taxable year, the election to take the HCTC applies to all subsequent coverage months

in that taxable year for which you are eligible to take the HCTC, and you should check the box for each such month. For example, the election would not apply to your September coverage if your last month of being a qualified individual is August (because, for example, your trade adjustment allowance ended on July 13). Thus, even if you had elected the HCTC for your January coverage, although your election applies to January through August, your election would not apply to your coverage for September and any later months in which you are not eligible for the HCTC.

The IRS has updated Form 8885 and its instructions for tax year 2015. The rules described in the updated instructions for tax year 2015 apply for tax years 2014 and 2015.

Q4. I am enrolled in a QHP through the Marketplace and am eligible for both the HCTC and the PTC. May I claim both the PTC and the HCTC in one taxable year? What about for the same coverage month?

A QHP offered through the Marketplace is qualified health coverage for both the PTC and the HCTC for coverage months in taxable years beginning in 2014 or 2015. For coverage in those months for which you are eligible for both the HCTC and the PTC, you may choose to claim either the PTC or the HCTC for your Marketplace coverage. Therefore, you may be able to claim both the PTC and the HCTC in the same year. However, an election to claim the HCTC for coverage in a month applies to all subsequent coverage months in your taxable year that you are eligible for the HCTC.

In addition, you cannot claim both the PTC and the HCTC for the same coverage for the same month. For example, if you elected to claim the HCTC for your coverage for June to December, you cannot claim the PTC for the same coverage for June

through December.

If you claim the HCTC for some months of a taxable year and the PTC for other months of the taxable year, you will need to file both a Form 8962 and a Form 8885 with your return.

For coverage months in taxable years beginning after 2015, individual health insurance coverage through the Marketplace is not qualified health coverage for purposes of the HCTC.

Q5. My spouse enrolled in a QHP through the Marketplace for the entire year, and I enrolled in COBRA for the entire year. I am eligible for the HCTC for every month of the year and wish to claim the HCTC for each month of the year. My spouse wishes to claim the PTC for each month of the year. May we claim the HCTC for the COBRA coverage and the PTC for the Marketplace coverage in the same month on a joint tax return?

Yes. On the same joint return, you can make an HCTC election that applies only to your coverage, and your spouse also may claim the PTC for your spouse's coverage. You must complete and file both Form 8885 and Form 8962 when you file your tax return. Although for 2014 and 2015 the APTC repayment limitation does not apply to coverage for which you elect the HCTC, your spouse may apply the repayment limitation in § 36B(f)(2), if applicable, for your spouse's coverage for which the HCTC is not elected by following the instructions for Form 8962, line 28.

Q6. I was enrolled in a QHP through the Marketplace for all of 2014 and claimed the PTC when I filed my tax return. I meet the requirements to claim the HCTC in every month of 2014. How should I compare the PTC and the HCTC to determine

whether to amend my tax year 2014 return to claim the HCTC instead of the PTC?

If I decide to claim the HCTC for 2014, how do I do that?

In general, if you and your family were enrolled in a QHP through the Marketplace for the entire year, the HCTC will provide you with a larger subsidy than the PTC if the amount of the HCTC is greater than the sum of: (1) your PTC without reduction for any APTC paid (this is the amount on line 24 of the Form 8962) and (2) any APTC that you were not required to repay due to the repayment limitation because your household income was below 400 percent of the Federal poverty line (this is the amount, if any, by which line 27 exceeds line 28 of Form 8962).

As explained in the Background, the amount of the HCTC is 72.5 percent of the amount paid by eligible individuals for qualified health coverage of the individual and qualifying family members for eligible coverage months.

If you wish to amend your 2014 return to claim the HCTC for the entire year, you must file Form 1040X and attach both Form 8885 to claim the HCTC and Form 8962 to correct your net PTC to \$0 (line 26) and report the repayment of any excess APTC. If you are electing the HCTC for all coverage months of the year and you had received the benefit of APTC, all of the APTC (line 25) will be excess APTC (line 27).

Q7. I was enrolled in a QHP through the Marketplace in 2014 and some payments were made by the APTC. I was not eligible for the HCTC for the first six months of the year (January through June); I was eligible for and am electing the HCTC for the last six months of the year (July through December). How do I treat the APTC?

The APTC repayment limitation that applies to a taxpayer with household income

below 400% of the Federal poverty line does not apply to coverage for 2014 or 2015 if the taxpayer elects the HCTC for any month in that year for that coverage. Because you are claiming the HCTC but you received the benefit of the APTC, you will need to file with your amended return a Form 8885 to claim the HCTC and a Form 8962 to reconcile and, to the extent applicable, repay the APTC for the months for which you are electing HCTC. On Form 8962, enter the amount of APTC in column (f) of line 11 or lines 12 through 23, as applicable, for all months APTC was paid, even those coverage months checked on Form 8885. If you are instructed, in the Form 8962 instructions, to complete Form 8962, Part III, enter the amount from line 27 (excess APTC) on line 29 (excess APTC repayment). Leave line 28 (repayment limitation) blank.

Taxpayers who receive the benefit of monthly advance payments of the HCTC may be eligible to apply a repayment limitation in certain circumstances in 2016 and thereafter. The IRS anticipates additional guidance to address the application of the repayment limitation for taxable years beginning after 2015.

Q8. I was enrolled in a QHP through the Marketplace in 2014 or 2015, and APTC was provided for some or all of the payments. I understand that the amount of the HCTC is 72.5 percent of the amount paid by an eligible individual for qualified health coverage. How do I determine the amount paid for coverage for purposes of the HCTC, considering that some or all of the coverage was paid for by the APTC?

APTC payments are treated as amounts paid by you for purposes of the HCTC. Thus, you can determine the amount paid for coverage for purposes of the HCTC as the sum of (1) the amount you paid to your insurance provider for all coverage months for

which you are claiming the HCTC (that is, for all coverage months checked on Form 8885) and (2) the amount of the monthly APTC shown on Form 1095-A, lines 21–32, column C, for all coverage months for which you are claiming the HCTC (that is, for all coverage months checked on Form 8885).

Q9. I was enrolled in a QHP through the Marketplace in 2015, and APTC was provided for some of the payments. The QHP covered me, my son, and my daughter. Both children lived with me in 2015, and, when we all enrolled, I expected to claim both of my children as my dependents. However, I claimed only my son as a dependent for 2015. My ex-spouse claimed my daughter as a dependent. I am eligible for and am electing the HCTC for the entire year. I understand that my son and daughter are both treated as my qualifying children for the HCTC, but that I cannot claim the PTC for my daughter’s coverage because she was not my tax dependent. Can I claim the HCTC on the entire amount of my 2015 QHP premiums?

No. You may only claim the HCTC for the portion of the premiums that are allocated to you under § 36B. Check “Yes” on line 9 of Form 8962 and follow the instructions for Part IV to allocate the shared policy amounts for your daughter to your ex-spouse. Report the APTC allocated to you on Form 8962 line 11, column (f), and on lines 25, 27, and 29. Then, to compute your HCTC, report on Form 8885, line 2, the enrollment premiums allocated to you.

SECTION 5. EFFECT ON OTHER DOCUMENTS

Notice 2005-50 is modified.

SECTION 6. DRAFTING INFORMATION

The principal author of this notice is Shareen Pflanz of the Office of the Associate Chief Counsel (Income Tax and Accounting). For further information regarding this notice, contact Ms. Pflanz at (202) 317-4718 (not a toll-free call). For further information about the HCTC, go to www.irs.gov/HCTC.