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### Health Care Reform: Coverage for Adult Children to Age 26

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As part of Health Care Reform, adult children under the age of 26 must be offered health coverage beginning with plan years on or after September 23, 2010. For example, this new requirement will be effective for a calendar year plan on January 1, 2011, while an employer-sponsored plan with a plan year of October 1<sup>st</sup> will be required to begin offering adult child coverage on October 1, 2010. Some employers (and their insurers and/or stop-loss carriers) have already begun implementing this change even before the required starting date.

The IRS has provided guidance on implementing this rule, including coverage options and the tax status of payments for that coverage. Virtually all employers sponsoring health plans will need to pay close attention.

#### *Coverage Requirements*

For all health plans that provide dependent coverage availability, adult children must now be offered coverage at least up to their 26<sup>th</sup> birthday, even if that adult-child is no longer a tax dependent. However, there is a small exception that pushes back the effective date of this new requirement for some specific adult-children. If the parent's employer-sponsored plan was in effect on March 23, 2010, the enactment date of the health care reform law (the "Patient Protection and Affordable Care Act of 2010", or PPACA) *and* if the adult-child is eligible for the child's own employer-sponsored health plan coverage, then the effective date to offer coverage to that specific adult-child under the parent's health plan is for plan years beginning on or after January 1, 2014.

For purposes of coverage under this new provision, a "child" is a son, daughter, stepson or stepdaughter of the employee, including a legally adopted child and a child lawfully placed with the employee for legal adoption. The definition also includes a foster child—that is, a child who is placed with the employee by an authorized placement agency or by judgment, decree or other court order.

Many health plans previously had provisions extending coverage to adult-children but often only if the child was a full-time student or if the child resided with the employee-parent, or if the child was a tax dependent. Under this new provision of the PPACA, none of those provisions will be allowable any longer.

Thus, virtually all health plan documents will need to be amended for the new coverage eligibility for adult-children.

It is important to note that the PPACA did *not* extend the health coverage requirement to spouses of adult-children, nor to children-of-children. While a health plan could permissively allow such coverage, none is required.

### *Tax Ramifications*

The PPACA also extended both tax exclusions for coverage and benefit receipt for covering adult-children, and actually extended the exclusions for a period of time likely to be longer than the coverage itself. This will greatly simplify providing tax-free coverage for adult-children in all health plans, including health care flexible spending accounts and health reimbursement arrangements (HRAs). ([Treasury Notice 2010-38](#))

While health plan coverage for adult children must extend to at least the adult-child's 26<sup>th</sup> birthday, the tax exclusion continues to the end of the employee's tax year, typically December 31<sup>st</sup>, as long as the adult-child has not yet attained the age of 27. For example, an adult-child turns 26 on July 1, 2011 and is covered by Mom's employer's plan that operates on a calendar year. Coverage for the adult-child could terminate on July 1, 2011, but the tax exclusion would extend until December 31, 2011 since the adult-child had not yet attained age 27 and the employee's tax year would typically end on that date.

So why would it matter if health plan coverage ended in July that the exclusion could continue through the end of the calendar year? Because a health care FSA or an HRA, might also cover that adult-child through the end of the year, and the employee could be allowed by plan design to submit eligible claims incurred by the adult-child to any of those plans.

Further, the IRS has said that it will provide a new rule to allow employers to permissively allow employees to change their health care FSA elections under the employer's Section 125 plan (including both adding children and changing the amount of the employee's contribution to a FSA). Although a change in elections would not be permitted under existing change-in-status rules (which apply only to changes in the number of tax-qualified dependents), the IRS will amend those rules retroactively in order to explicitly permit this optional change should the employer so desire.

The new tax exclusion is retroactively effective to March 30, 2010. This retroactive date is even allowed for qualified cafeteria plans under IRC Section 125 as long as the cafeteria plan documents are amended on or before December 31, 2010. Thus, most employers will want to review their options and make sure that their plan documents are properly amended before the end of the year.

Employers will also want to review their policies and procedures regarding current practices of covering adult-children. Many states have required coverage

for adult-children, and if those individuals were not tax dependents then the employer was required to impute taxable income to the employee who chose coverage for their adult-child. Therefore, some income may have already been imputed for coverage from March 30, 2010 forward. This will no longer be required, and favorable adjustments to employee and employer payroll taxes may be in order.

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