

# BENEFITS ALERT

Rose & Kiernan, Inc.

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## Age 26 Tax Exclusion

The IRS has just issued Notice 2010-38 to give guidance on the tax treatment for the extended coverage given to children through the recently passed health care reform bill, PPACA, and the reconciliation act, HCERA. The effective date of the change in the IRS Code is retroactive to March 30, 2010.

You need to be aware of a discrepancy between the PPACA and the HCERA with regard to the dependent to age 26 changes.

The PPACA, in Section 2714 states "A group health plan...shall continue to make coverage available for an adult child (who is not married) until the child turns 26 years of age." This defines the period of time that the dependent is covered.

The intent of the HCERA change was to make the child's insurance eligible for the same tax exemption as the employee's insurance since normally a child over the age of 19 (or 24 if a full time student) is not a dependent under the Internal Revenue Code. In amending Sec 105(b) of the Internal Revenue Code, HCERA uses the phrase "...any child of the taxpayer who as of the end of the taxable year has not attained age 27." In other words the income tax exclusion continues until the end of the calendar year in which the child turns 26. Therein lies the discrepancy. **(Note: HCERA also struck the phrase "...who is not married" from the law allowing married dependent children to enroll only themselves, not the spouse)**

The reason for this discrepancy is to allow the tax exclusion to carry through the entire year for those plans that cover dependents until the end of the calendar year in which they reach a limiting age.

Therefore a child is covered until age 26 under the Federal bill. When that dependent turns age 26, **if** he or she can continue on the parent's policy because (1) the employer's policy wording covers them to the end of the year they turn 26 or (2) as allowed under NYS law, for example, until age 30, the period from their 26<sup>th</sup> birthday until the end of the calendar year in which they turn 26, the fair market value of the dependent's health insurance will not be taxed. However, beginning January 1 of the following year, the employee's W-2 will have to include as imputed income the fair market value of the dependent's insurance.

Coverage for dependents to their 26th birthday is effective on the first plan year following 9/23/2010. For most employers, that will be 1/1/2011 or 7/1/2011.

We're issuing this alert since the provision is retroactive to March 30th, 2010 so you may be getting questions. Also, many health plans have decided to allow graduating seniors to stay on their parent's plan even before the change becomes effective for the employer so many young people will be on your plan sooner than expected. The IRS' decision will help your payroll vendor or payroll department to handle the tax issues related to this change.

The IRS notice is attached and also includes examples.

*This Summary is provided to you for general information purposes only and does not include references to other legal resources (e.g., supporting regulations, or formal or informal opinions) unless specifically noted. Please seek qualified and appropriate counsel for further information and/or advice regarding the application of the topics discussed herein to your employee benefits plan.*

*Updated: May 6, 2010*

