



Federal Health Care Reform Update

Extension of Tax-Free Employer-Provided Coverage



On April 27, 2010, the Internal Revenue Service issued Notice 2010-38. This Notice clarifies the tax treatment of health coverage for children up to the age of 27.

The federal health care reform laws require group health plans and health insurance carriers to make coverage available to adult children up to the age of 26. These laws also amend the Internal Revenue Code (the Code) to extend the current favorable tax treatment for dependent children to these newly eligible adult children.

Exclusion of Employer-Provided Medical Care Reimbursements

Section 105(b) of the Code excludes employer provided reimbursements made directly or indirectly to the employee, the employee's spouse and the employee's dependents from an employee's gross income.

The reform laws extend this exclusion to reimbursement for the medical care of the employee's child who has not attained the age of 27 as of the end of a taxable year. This exclusion includes children who are not dependents. Therefore, the age limit, residency, support and other "dependent" tests do not apply. In addition, an employer may rely on an employee's representation as to a child's date of birth.

Exclusion of Employer-Provided Accident or Health Coverage

Section 106 of the Code excludes the cost of coverage under an employer-provided accident or health plan from an employee's gross income. Prior to the reform law, the exclusion under Section 106 paralleled the exclusion under Section 105.

Therefore, the IRS and Treasury Department will amend the regulations under Section 106 to provide that the cost of coverage for an employee's child who has not attained the age of 27 as of the end of a tax year is excluded from the employee's gross income.

Flexible Spending Accounts and Health Reimbursement Arrangements

Claims incurred by an employee's dependent child who has not yet attained the age of 27 will now be eligible for reimbursement out of that employee's FSA.

Furthermore, regulations allow an employee to revoke an election during the plan year and make a new election in the event of a "change in status". The IRS and Treasury Department will amend those regulations to include as a "change in status event" a child (who has not attained the age of 27) becoming newly eligible for coverage *or* becoming eligible for coverage beyond the date on which that child would otherwise have lost coverage.

The same rules that apply under Sections 105 and 106 to an employee's child who has not attained the age of 27, as explained above, will apply to these children under an HRA.

Effective Date

All these changes are being made effective retroactive to March 30, 2010 for *all* health plans, regardless of anniversary date.

In sum, any changes that an employer makes to its plan to include children up to the age of 26 will be tax-free, regardless of whether the change is made because it is required under the federal health care reform law, or because an employer or a carrier decides to accelerate the process and offer an enhanced benefit before it is required by the reform law.

Cafeteria Plan Documents

As of March 30, 2010, employers may permit employees to make pre-tax contributions for accident and health benefits under a cafeteria plan (including FSA's) for children who have not attained the age of 27, even if the cafeteria plan has not been amended to include these individuals. However, a retroactive amendment to cover these individuals must be made no later than December 31, 2010 and must be retroactive to the first day such contributions were permitted, but not earlier than March 30, 2010.

Benemax will prepare Cafeteria Plan amendments on behalf of those clients for which Benemax prepared original Cafeteria Plan (Section 125) documents.

In the meantime, should you have any questions regarding compliance matters, please contact Benemax Compliance Officer Walter Hiltz at 800-528-1530 ext. 120 or walter@benemax.com.