

## HEALTH CARE REFORM UPDATE

### Changes to the Tax Code for Benefits Provided to Dependent Children

The Patient Protection and Affordable Care Act (the “Act”) requires all health care plans offering dependent coverage to provide coverage to adult children until age 26.<sup>1</sup> Although health plans in New Hampshire were already required to offer such coverage under certain circumstances, the requirement under the Act expands the definition of dependent and also includes corresponding changes to the Internal Revenue Code (the “IRC”) that could impact employers and employees in New Hampshire. These changes to the IRC exclude from the employee’s gross income amounts paid or reimbursed to employees for medical expenses associated with those children now required to be covered.

#### Affect on New Hampshire Dependant Coverage Law

Effective September 14, 2009, New Hampshire amended the Insurance Law by defining the term “dependent” for purposes of health insurance coverage as an unmarried individual who is:

- (1) Under age 19;
- (2) Under age 25 and a full-time student; or
- (3) Under age 26, a resident of New Hampshire and not provided coverage under any other group plan or Medicare.

New Hampshire Revised Statutes Annotated 415:5, I(3).

The Act impacts the New Hampshire law in two ways. First, New Hampshire insurers will now be required to provide dependent coverage up to age 26, regardless of New Hampshire residence or other criteria specific to the New Hampshire law. Second, as described below, some dependents covered under this provision of New Hampshire law would not have qualified as dependents or children under the IRC prior to the changes made by the Act.

#### Changes to the IRC

Before the enactment of the Act, an employee’s child generally had to be under age 20 (or under age 24 if a full-time student) to qualify as a dependent under federal tax law for purposes of the income exclusion associated with reimbursement of medical expenses with respect to such child. The Act and Notice 2010-38 published by the IRS provide that, effective March 30, 2010, coverage provided under an employer

<sup>1</sup> In the case of “grandfathered plans” (i.e., plans existing prior to enactment), coverage must only be offered to these dependents if they are not eligible for employer-sponsored coverage.

### HEALTHCARE Practice Group

Lucy C. Hodder  
Chair  
[lch@rathlaw.com](mailto:lch@rathlaw.com)  
Kenneth C. Bartholomew  
Vice Chair  
[kcb@rathlaw.com](mailto:kcb@rathlaw.com)

#### PROFESSIONALS

Lindsey F. Dalton  
[lfid@rathlaw.com](mailto:lfid@rathlaw.com)

Barbara J. Greenwood  
[bjg@rathlaw.com](mailto:bjg@rathlaw.com)

Rose Marie Joly  
[rmj@rathlaw.com](mailto:rmj@rathlaw.com)

Ann McLane Kuster  
[amk@rathlaw.com](mailto:amk@rathlaw.com)

Steven J. Lauwers  
[sjl@rathlaw.com](mailto:sjl@rathlaw.com)

Michael A. Pignatelli  
[map@rathlaw.com](mailto:map@rathlaw.com)

Antony K. Sayess  
[aks@rathlaw.com](mailto:aks@rathlaw.com)

Oliver W. Stalter  
[ows@rathlaw.com](mailto:ows@rathlaw.com)

Christopher J. Sullivan  
[cjs@rathlaw.com](mailto:cjs@rathlaw.com)

Adam C. Varley  
[acv@rathlaw.com](mailto:acv@rathlaw.com)

#### WWW. RATHLAW.COM

The Healthcare Practice Group provides a wide range of regulatory, corporate and litigation support to healthcare providers and suppliers throughout New England and nationally.

National Impact. Uniquely New Hampshire.

Rath, Young and Pignatelli, P.C.  
[www.rathlaw.com](http://www.rathlaw.com)

One Capital Plaza  
Concord, NH 03302-1500  
T (603) 226-2600  
F (603) 226-2700

20 Trafalgar Square  
Nashua, NH 03063  
T (603) 889-9952  
F (603) 595-7489

54 Canal Street  
Boston, MA 02114  
T (617) 523-8080  
F (617) 523-8855

health plan as well as amounts paid or reimbursed under such plan for medical expenses for an employee's child who has not reached age 27 as of the end of the employee's taxable year are excluded from the employee's income.<sup>2</sup>

Notice 2010-38 also confirms that these changes apply to Section 125 cafeteria plans. As such, coverage and reimbursement provided with respect to children under 27 are "qualified benefits" under the cafeteria plan and employers may permit employees to make pre-tax salary reductions to pay for the benefits. Mid-term elections by employees in cafeteria plans are only permitted due to specific change in status events, which do not contemplate the eligibility change here. To remedy this problem, the IRS indicated it will amend its regulations retroactive to March 30, 2010 to include situations where children become newly eligible under the Act. In addition, in recognition of the potential need of employers to amend cafeteria plans to accommodate these changes and the prohibition on retrospective amendments to such plans, the IRS will allow employers to permit employees to immediately make election changes if the plan is amended to cover the newly qualified children by December 31, 2010, and the amendment is made retroactive to the first date employees are permitted to make the new salary reductions (but not earlier than March 30, 2010).

### **Impact on New Hampshire Employers**

The changes discussed above impact New Hampshire employers directly and indirectly:

- (1) Employees will now be able to continue coverage for their children until age 26 regardless of the child's residence or student status;
- (2) Employees whose dependents receive coverage under an employer plan will no longer be taxed on the benefit of that coverage or any medical expenses paid or reimbursed under that coverage for any child under age 27 during the taxable year. Because coverage and reimbursements for these children are not considered wages, they are also exempt from income tax withholding; and
- (3) If employers wish to permit employees to pay for medical coverage for the newly qualifying children on a pre-tax basis under a cafeteria plan, an amendment to the plan must be made by December 31, 2010 (and must be retroactive to the first day such pre-tax reductions were permitted).

*For further questions, please contact Adam C. Varley at [acv@rathlaw.com](mailto:acv@rathlaw.com) or Steven J. Lauwers, Chair of the Insurance Law Practice Group at [sjl@rathlaw.com](mailto:sjl@rathlaw.com).*

*This information should not be construed as legal advice or relied upon to resolve legal problems.*

---

<sup>2</sup> There is a discrepancy in the Act between the age of dependency for coverage purposes (i.e., up to 26) and the age of children for income exclusion purposes (i.e., up to 27).