Health Care Reform Advisory: Agencies Issue Guidance on Health Care Reform's New Child Coverage Rules

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By Patricia A. Moran

The Patient Protection and Affordable Care Act of 2010, together with the Health Care and Education Reconciliation Act of 2010 (collectively, the "Affordable Care Act"), provide that, effective for plan years beginning on or after September 23, 2010, a plan or issuer that makes available dependent coverage of children must make such coverage available to children until the attainment of 26 years of age (the "Coverage Requirement"). In a sister provision effective upon enactment of the Affordable Care Act (March 31, 2010), the Affordable Care Act amends Section 105(b) of the Internal Revenue Code (the "Code") to provide that medical reimbursements made to an employee with respect to any child of the taxpayer are not taxable through the end of the taxable year in which the child turns 26 (the "Tax Provision").[1]

As a threshold matter, it is important to understand the differences between, and the interaction of, the Coverage Requirement and the Tax Provision. The Coverage Requirement is a new coverage mandate; when the provision takes effect, all plans offering medical coverage to dependent children in the United States, whether insured or self-funded, and whether or not subject to any of the Affordable Care Act's "grandfathering" provisions, will need to be amended to include coverage for children under the age of 26. The Tax Provision, on the other hand, does not require plans to provide any specific coverage to children or anyone else. However, if a medical plan does cover a child of a plan participant, the coverage will not be taxable to the participant through the end of the taxable year in which the child turns 26 even if the child is not a tax dependent of the participant.[2]

Since the enactment of the Affordable Care Act, federal government agencies have published two key items of guidance with respect to these provisions. On April 27, 2010, the Internal Revenue Service issued Notice 2010-38 (the "Notice"), which provides guidance on the Tax Provision. On May 13, 2010, the Internal Revenue Service, Department of Labor and Department of Health and Human Services issued interim final rules (the "Regulation") with respect to the Coverage Requirement. The purpose of this Advisory is to highlight the key provisions of this guidance.

Notice 2010-38

Effective March 30, 2010, the Tax Provision provides that medical reimbursements made to an employee with respect to any child of the taxpayer are not taxable through the end of the taxable year in which the child turns 26, whether or not that child is a "dependent" under Section 152 of

the tax code. "Child" is defined broadly to include a son, daughter, stepson, stepdaughter, legally adopted child, or foster child placed with the parent by judgment or decree.

Notice 2010-38 provides the following guidance and clarifications with respect to the Tax Provision.

Technical Changes

The Notice confirms that the Tax Provision applies to Code Section 106 retroactively to March 30, 2010. Code Section 106 excludes from an employee's gross income coverage under an employer-provided accident or health plan.

Cafeteria Plan Changes

- Coverage provided to children who are under 27 as of the end of the taxable year and excludible under Code Section 105(b) and 106 is a "qualified benefit" under the cafeteria plan rules (and may be funded using pre-tax salary reduction).
- Effective March 30, 2010, a cafeteria plan "change in status" may include a nondependent child under age 27 becoming newly eligible for coverage or eligible for coverage beyond the date on which the child otherwise would have lost coverage. In such a case, a cafeteria plan may, if it so chooses, permit a mid-year election change.
- Ordinarily, cafeteria plans may not be amended retroactively. However, the Notice specifies that, as of March 30, 2010, employers may permit employees to immediately make pre-tax salary reduction contributions for accident or health benefits under a cafeteria plan (including a health flexible spending account) for children who have not turned 27 by the end of a taxable year, even if the cafeteria plan has not yet been amended to cover these individuals. A retroactive amendment to a cafeteria plan to cover children under age 27 must be made no later than December 31, 2010, and must be effective retroactively to the first date in 2010 when employees are permitted to make pre-tax salary reduction contributions to cover children under age 27.

Tax Treatment Spans Entire Year

The Notice makes clear that benefits may be excluded from tax for the entire year in which a child turns 26.

Other Technical and Administrative Guidance under Notice 2010-38

- Coverage and reimbursements under a plan for an employee's child under age 27 are not wages for FICA or FUTA purposes.
- The Tax Provision applies only for reimbursements for medical care of individuals who are not age 27 or older at any time during the taxable year (employers may assume that an employee's taxable year is the calendar year).
- A child attains age 27 on the 27th anniversary of the date the child was born.
- Employers may rely on the employee's representation as to the child's date of birth.
- The Tax Provision applies to health reimbursement arrangements (HRAs).

The Regulation

Effective for plan years beginning on or after September 23, 2010, a plan or issuer that makes available dependent coverage of children must make such coverage available to children until the attainment of 26 years of age pursuant to the Coverage Requirement.

The Regulation provides the following guidance and clarifications with respect to this new Coverage Requirement.

The Parent-Child Relationship Controls

A plan may not condition "child" coverage on any factors other than (1) the parent-child relationship between the child and a plan participant, and (2) the requirement that the child be under the age of 26. In other words, a plan will not satisfy the Coverage Requirement if it:

- Charges different premiums or cost sharing on, or makes different coverage options available to, different age groups of age 26-and-under children;
- Requires that the age 26-and-under children show residency, financial dependency, student status, or unemployment status in order to obtain coverage;
- Denies a 26-and-under child coverage because he or she is eligible for another employer's coverage (although "grandfathered" plans have the right to do this for plan years beginning before January 1, 2014); or
- Denies a 26-and-under child coverage because he or she is married (however, spouses of the covered child, or children of the covered child, need not be covered).

Two-Parent Coverage

The Regulation notes that, in the case of an age 26-and-under child who is eligible for coverage under the plans of the employers of both parents, neither plan may exclude the child from coverage based on the fact that the child is eligible to enroll in the plan of the other parent's employer.

New Special Enrollment Rights for Child and Parent

If a child was denied coverage (or was never eligible for coverage) under a parent's plan, or "aged out" of the plan because he or she exceeded a plan's age limits, but is still under 26 at the time the Coverage Requirement takes effect, he or she will be able to enroll in the plan.

The child's enrollment right is contingent upon his or her parent's eligibility for, and participation in, a plan. Accordingly, the special enrollment right also applies to a parent who is eligible to participate in a health plan; in this case, the parent may himself join the plan (or change coverage options), and enroll the child accordingly. Upon enrollment, the child (and parent) may not be required to pay more than, and must be offered the same benefits (including cost-sharing options) as, similarly situated participants.

Coverage must begin by the first day of the first plan year beginning on or after September 23, 2010.

Open Enrollment Notice Requirements

Plans must provide a notice of the enrollment opportunity to individuals whose coverage ended, or who were denied coverage (or were not eligible for coverage) under a group health plan or health insurance coverage, because, under the terms of the plan or coverage, the availability of dependent coverage of children ended before the attainment of age 26.

An enrollment notice must be provided not later than the first day of the first plan year (in the individual market, policy year) beginning on or after September 23, 2010. The enrollment opportunity must continue for at least 30 days, regardless of whether the plan or coverage offers an open enrollment period and regardless of when any open enrollment period might otherwise occur.

The written notice must include a statement that children whose coverage ended, or who were denied coverage (or were not eligible for coverage), because the availability of dependent coverage of children ended before attainment of age 26 are eligible to enroll in the plan or coverage.

The notice may be provided to an employee on behalf of the employee's child. In addition, the notice may be included with other enrollment materials that a plan distributes to employees, provided the statement is prominent.

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Endnotes

[1] In our previous alert issued on April 20, we describe the of the immediate effects of this provision on taxation of health coverage provided to children of employees on "imputed income" charged to employees.

[2] Under Federal Tax Code § 152, a "dependent" is either a "qualifying child" dependent or a "qualifying relative" dependent. A "qualifying child" is a child who lives with an employee for

more than half a year, who is either under age 19 or is a full-time student under age 24, and who does not provide over half of his or her own support for the calendar year. A "qualifying relative" is an individual who bears a relationship to the taxpayer (including any child of the taxpayer who is not a "qualifying child," regardless of the child's age), whose gross income is less than the exemption amount ($3,650 in 2010), and who receives over one half of his or her support from the taxpayer. But for purposes of the exclusion for employer-provided health coverage, the $3,650 gross income limit does not apply to a qualifying relative.

For further information regarding this or any issue related to Health Care Reform, please contact one of the professionals listed below or the Mintz Levin attorney who ordinarily handles your legal affairs.

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