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The New Rules for Coverage of Adult Children

The recently enacted Affordable Care Act (ACA) (combining the Senate passed Patient Protection and Affordable Care Act and the House passed Health Care and Education Reconciliation Act) has two separate, but connected rules regarding coverage of adult children. Regulations issued May 13, 2010 by the Departments of Treasury; Labor; and Health and Human Services provides guidance as to one of them, and an IRS Notice issued on April 27, 2010 provides guidance as to the second. What might seem to have been a simple requirement has twists and turns of which employers must be aware.

The New Eligibility and Coverage Rules for Adult Children

- The first rule simply requires that effective for plan years beginning on or after September 23, 2010, employer-sponsored group health plans and health insurers must cover adult children of employees up to age 26, thereby allowing plans to terminate coverage effective as of the adult child's 26th birthday.
- An adult child means the son, daughter, stepson, stepdaughter, adopted son or daughter or eligible foster child of the participant. An eligible foster child is one placed with the participant by an authorized placement agency or by judgment, decree or other order of a court.
- Adult children cannot be defined for purposes of dependent eligibility other than in terms of a relationship between the adult child and the participant. Adult children cannot be excluded from coverage based on (i) financial dependency, (ii) student status, (iii) residency with the participant or any other person, (iv) employment status, (v) marital status, (vi) eligibility for other coverage (except as noted above for grandfathered plans), (vii) status as a federal tax dependent, or (viii) any combination of these. Plans do not, however, have to cover the spouses or children of adult children.
- Grandfathered plans (*i.e.*, those in existence on March 23, 2010) must also cover adult children until age 26, but can exclude them from coverage if they are eligible to enroll in another employer-sponsored group health plan which,

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as the regulations clarify, is not a group health plan of either parent. After January 1, 2014, this special rule for grandfathered plans expires, and the same rule applies to all group health plans and health insurers. Revising the terms of a grandfathered plan to comply with these rules will not cause the plan to lose its grandfathered status.

- Any adult child who is currently aged out of his or her parents' plan(s) may elect to re-enroll, and may do so any time, without having to wait for the next open enrolment period.
- Plans cannot require either the adult child or the employee to pay more for coverage than similarly situated persons. Thus, if the participant has family coverage and that coverage is the same no matter how many dependents, then no additional charge for covering the re-enrolled adult child can be imposed. If the plan has single and single plus one coverage, and the employee had single coverage when the adult child had aged out of the plan, the plan can charge the employee for single plus one coverage should the adult child re-enroll. If the plan charges a different premium rate for each dependent, the plan can charge whatever rate would apply for one additional dependent.
- Plans must notify all adult children who either aged out of the plan prior to March 23, 2010, never enrolled in the plan because they were over age when the parent enrolled, or who are or were covered as students, and provide them with an opportunity to enroll in the plan. The notice of the opportunity to enroll must be sent out no later than the first day of the first plan year beginning on or after September 23, 2010, and the opportunity to enroll must remain open for at least 30 days.
- If the parent of an adult child is not enrolled in the plan, the decision of an adult child to re-enroll will give the parent another opportunity to enroll.

The New Tax Rules for Coverage of Adult Children

- The second rule tracks, but is not the same as, the eligibility and coverage rules. Under the new tax rules, the cost of benefits provided to adult children will be deductible by the employer and excludable from the income of either the adult child or the parent until the end of the calendar year in which the child turns 26.

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- Plan sponsors, then, can either adopt an eligibility rule that cuts off coverage on the adult child's 26th birthday, or extend coverage to the end of that calendar year without any negative tax consequences.
- Effective retroactively to March 30, 2010, a cafeteria plan can include in the permissible change in status events a nondependent adult child under age 27 becoming newly eligible for coverage under these ACA provisions, so long as the cafeteria plan is amended by December 31, 2010.
- Adult children can be covered under a health care flexible spending account, a health reimbursement arrangement or a VEBA until the end of the calendar year in which they turn 26, so long as the applicable plan is so amended by December 31, 2010.
- There is no imputed income, nor any Federal Insurance Contributions Act, Federal Unemployment Tax Act, Railroad Retirement Tax Act, or income tax withholding on any amounts provided for health care coverage or reimbursements for an employee's adult children under age 27.

Action Steps

Employers' group health and cafeteria plans will have to be amended to comply with these new rules. Employers providing insured benefits should consult with their insurers to determine how and when the insurers will be implementing these changes. Many insurers have indicated they will be complying with these rules before the applicable deadlines. To see the list, go to the following Department of Labor website:

<http://www.dol.gov/ebsa/newsroom/fsdependentcoverage.html>

If you have any questions about these new requirements for covering adult children or any of the other changes imposed by the ACA, please contact any of the Honigman attorneys listed on this alert.