



Health Care Reform

LEGISLATIVE BRIEF

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States Conform Tax Laws for Dependent Coverage Rules

The Affordable Care Act (ACA) requires health plans and issuers that offer dependent coverage to make the coverage available until the adult child reaches the age of 26. When the ACA was passed, the federal tax code was also revised to take this new dependent coverage requirement into account. Under the revised federal tax code, effective March 30, 2010, the value of employer-provided coverage for an adult child is excluded from the employee's gross income through the end of the year in which the child attains age 26.

While many states' tax laws automatically conform to the federal tax code, other states need to take legislative action to make their tax laws consistent with the federal tax code. Some states did not immediately amend their tax laws for the ACA's dependent coverage requirement, and this created state tax issues. However, all state tax laws regarding dependent coverage currently conform to the federal tax code.

Also, some states have dependent coverage requirements for insured plans that exceed the federal minimum created by the ACA. In states where coverage is required past age 26, employees may have to recognize additional income and pay tax on the value of coverage.

This Legislative Brief describes the ACA's dependent coverage requirement and the related federal and state tax issues.

FEDERAL TAX TREATMENT

Before the ACA was enacted, Internal Revenue Code (Code) Section 105(b) provided that an employee's child had to qualify as a tax dependent in order for the value of the child's employer-provided health coverage to be excluded from income, and therefore be tax-free, at the federal level. Generally, a child had to be under age 19, or under age 24 if a full-time student, and had to rely on the employee for more than half of his or her financial support to be considered a tax dependent.

Under the tax changes related to the ACA, Code Section 105(b) was revised to accommodate the extended coverage requirement. The revised section states that coverage provided by an employer to an employee's child will be excluded from income through the end of the taxable year in which the child turns 26. This tax provision allows adult children to receive tax-free coverage for a time beyond their 26th birthday, even though the ACA coverage requirement ends once the child has turned 26.

STATE TAX ISSUES

Employer-provided health plan coverage for an adult child can be excluded from income for federal tax and state tax purposes through the end of the tax year in which the child attains age 26. Some state insurance laws require dependent coverage beyond age 26. Employer-provided health coverage for an adult child after the year in which the child turns age 26 will be subject to federal and state tax, unless the child qualifies as a tax dependent.

State Tax Laws

State tax laws are generally related to the federal tax code in some way. Some states have laws that are designed to automatically conform to changes in the Code. This ensures that state and federal tax laws remain consistent.

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Several states do not have state income tax, so dependent coverage of adult children will be tax-free at the state level. These states include Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington and Wyoming.

However, other states have to amend their laws to bring them into line with the federal rules. These states have taken legislative action to make their state tax law **consistent with the federal exclusions** for employer-provided coverage:

- Arizona
- Hawaii
- Maine
- South Carolina
- Wisconsin
- California
- Indiana
- Minnesota
- Vermont
- Georgia
- Kentucky
- Oregon
- Virginia

Extended State Dependent Coverage

A number of states have passed laws that require insured group health plans to cover dependents beyond age 26. Such state mandates, to the extent they require coverage past age 26, will continue to apply. In the event state laws mandate coverage past age 26, employers will generally have to impute the fair market value of the coverage as income to employees for tax years after the child turns 26, unless employees pay for it on an after-tax basis or the child qualifies as a tax dependent.

The following states have requirements for dependent coverage that exceed the federal minimum standard. In addition, many state insurance laws extend dependent coverage beyond the limiting age for disabled dependents.

STATE	DEPENDENT COVERAGE REQUIREMENT
Florida	Up to age 30 for unmarried children without dependents who are state residents or students and do not have their own coverage. (F.S.A. § 627.6562) No state income tax.
Illinois	Up to age 30 for unmarried dependents who are veterans and state residents. (215 ILCS 5/356z.12)
Nebraska	Up to age 30 for unmarried children who are state residents or full-time students and do not have their own coverage. (Neb. Rev. St. § 44-7,103)
New Jersey	Up to age 31 for unmarried children without dependents who are state residents or full-time students and do not have their own coverage. (N.J.S.A. 17B:27-30.5)
New York	Up to age 30 for unmarried children that are state residents. (NY Stat 3216(a)(4)(C))
Ohio	Up to age 28 for unmarried children that are state residents or full-time students. (Ohio Rev. Code § 1751.14)
Pennsylvania	Up to age 30 for unmarried children without dependents who are state residents or full-time students. (40 P.S. § 752.1)
Wisconsin	Under prior law, up to age 27 for unmarried children who did not have their own coverage. (W.S.A. 632.885). This provision was amended to mirror the ACA's dependent coverage standard, effective Jan 1, 2012. Thus, effective Jan. 1, 2012, the age limit for dependent eligibility was lowered from 27 to 26.

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ACTIONS FOR EMPLOYERS

If you are located in a state that requires dependent coverage beyond the federal minimum age you may need to take some additional steps in administering the coverage. Note that these steps may vary due to subtleties in a state's laws.

- Request that employees provide information on covered adult children to determine whether they meet state dependent requirements.
- Provide information to applicable employees on tax requirements and notify them that the value of the coverage for their adult children may need to be included on their W-2 forms as imputed income.
- Determine the fair market value of the employer-provided coverage. Methods used to determine this value include using the plan's COBRA premium or having an actuary calculate the fair market value.
- Impute income to employees for tax purposes for the fair market value of coverage provided to adult children under state laws that are more generous than the federal minimum requirements.
- Report any imputed income on the employee's W-2 form (unless coverage was paid for on an after-tax basis).

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