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## Medical Costs for Adult Dependents

In our continuing efforts to cover the myriad of topics contained in recent healthcare legislation, this month's topic will focus on the new rules regarding medical costs for adult dependents. As part of the Patient Protection and Affordable Care Act and Health Care and Education Reconciliation Act of 2010 - collectively referred to as the Affordable Care Act (the Act), the parameters for a parent to provide for the medical costs of their children have been greatly broadened.

Prior to the Affordable Care Act, tax-free health coverage was only available for dependent children up to the age of 19, or age 24 if enrolled as a full-time student. Dependent status was based on a relationship test and a support test. The term "dependent" as used in the new Act can be misleading. It does not mean that the child is claimed as a dependent on your personal tax return. It means that the child is *treated like a dependent* of a taxpayer for health coverage-related purposes. The term dependent merely describes a parent/child relationship.

The new law has two key provisions:

- 1.) It **requires** group health plans and health insurance issuers that provide dependent coverage to children to continue to make such coverage available for an adult child until age 26 for plan years starting after September 23, 2010.
- 2.) It **allows for** children until age 27 to qualify for medical care reimbursements under a qualified plan effective as of March 30, 2010.

A child is defined as an individual who is the son, daughter, stepson, stepdaughter, legally adopted individual, or foster child of the employee.

The following points have been refined since the passage of the Act:

- The provision relating to medical care reimbursements applies to individuals who are not age 27 or older at **any time** during the calendar year. Therefore, if an adult child turns 27 during 2010, none of their medical costs qualify for exclusion under the new law.
- Expenses for adult children must be bifurcated for 2010. For the period of January 1, 2010 to March 29, 2010, the old rules above apply. From March 30, 2010 forward, the new rules apply. Thus, for example, the medical costs of an adult child who is 25 years old at the end of 2010 qualify for reimbursement for costs incurred on or after March 30, 2010.
- Employers may rely on an employee's representation as to the birthdate of an adult child.
- Although the new law applies to married and unmarried adult children, it does not apply to the spouse or children of those adult children.
- Employees who add adult dependents to their existing coverage during 2010 due to changes in the law are allowed to increase their current year health flexible savings account elections.

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- Employers may amend their cafeteria plans retroactively to comply with the new law, as long as they execute the amendment by December 31, 2010.
- The expansion also applies to:
  - Voluntary employee benefit associations (VEBAs)
  - Self-employed medical tax deduction
  - Retiree health care accounts in pension plans
- Nonprescription drugs will not qualify as a reimbursable medical cost after 2010.

**Examples**

**#1:** Employer X provides health care coverage for its employees, their spouses, dependents, and children under age 26. During 2010, X provides coverage to Employee A and to A's son, C. C will turn age 26 on November 15, 2010. During 2010, C is not a full-time student. C does not work for X.

C is not a dependent of A for tax purposes because C is over 19 and not a full-time student. However, C is a dependent child for purposes of the new healthcare provision. Therefore, since C will not attain age 27 during 2010, C is eligible for health care coverage and reimbursement of medical costs for the period on or after March 30, 2010 through November 15, 2010 (when C attains age 26).

*Comment:* If the plan specified that it allowed coverage for children up to age 27, C would be eligible for benefits up through December 31, 2010. Since it only specified "for children under age 26", coverage ends on the child's 26<sup>th</sup> birthday.

**#2:** Same facts as example 1, but with the added twist that C is employed by a company that offers health insurance. C has decided not to participate in his employer's plan.

The fact that C is offered coverage through his/her employer does not affect the outcome. C is still eligible to be covered under A's plan.

**#3:** Same facts as example 1, but C is married to D. Neither C nor D is a dependent of A for tax purposes. C and D both have access to health care coverage through their respective employers.

The fact that C is married does not alter the result. C is still eligible to be covered under A's plan. If X allows D to be covered under X's plan, the fair market value of the coverage for D is includible in A's gross income for the 2010 taxable year.

**Conclusion**

Although the new provisions make it easier to maintain health coverage for your adult children, you need to be aware of the potential pitfalls that exist. If you have a personal situation that is outside the scope of this article or just would like clarification on an issue, we encourage you to call us to discuss.

For our prior articles discussing the new healthcare act, please visit our website at [www.fwcpas.com](http://www.fwcpas.com) and click on the Client Resources link.