

# BenAlert

BENEFIT TRENDS AND LEGISLATIVE UPDATES

DECEMBER 2010



HOWITT  
Benefit Services

Howitt Benefit Services is pleased to provide you with periodic updates on benefit trends and legislative updates. As part of our valuable services, we want to ensure that you are in compliance and well-informed of the ongoing changes in our industry.

## In this BenAlert:

- **Health Care Reform: California Taxation and Related Issues**

In the last few days, we have received a number of questions surrounding the failure of the California Legislature to adopt the federal income tax rules governing the tax treatment of health care coverage provided to adult children (age 24-26). Additionally, there has been some confusion over the availability of dental and vision benefits to adult children under California law ([SB 1088](#)). The purpose of this BenAlert is to address these two specific issues.

### Taxation

Under the Health Care Reform Law and pursuant to an IRS Notice ([2010-38](#)), group health coverage provided to adult children (up to age 27) will no longer result in imputed income to the employee effective March 30, 2010. So for federal income tax purposes, employers will no longer add the value of the coverage to an employee's wages.

Unfortunately, the California Legislature failed to pass AB 1178 which would have provided the same break under California tax law. As a result, employers must impute income for the value of coverage provided to adult dependents for state tax purposes and may not allow pre-tax contributions for state tax purposes. We know this is a bit confusing.

### **Imputed Income Tax**

Historically, the customary method of calculating the value of group health care coverage for income tax purposes has been somewhat vague. The shorthand rule would be to look at the COBRA rate (minus 2%) charged to provide individual COBRA coverage. This will vary based on the plan's overall rate structure (employee only, employee plus spouse, employee plus family), the premium rate with a family of four is the same for a family of five or even eight. So, if the employee has elected full family coverage and then enrolls an adult dependent pursuant to Health Care Reform, the employee still pays the same full family contribution as before. However, since the value of the coverage is the single rate (minus any after-tax employee contributions) the employee will receive additional compensation, for California income tax purposes, based on the single rate. You will need to alert your payroll provider so the necessary deductions can be made for the 2011 tax year for those employees who choose to add an overage dependent to their coverage. Remember this only applies to overage dependents ages 24-26!

### **Dental and Vision Coverage**

Recently, Vision Service Plan provided a notice to its contract holders that adult children must be eligible for vision benefits. It's now clear that the California law adopting the federal Health Care Reform rule for making coverage available to adult dependents is to be identical in all respects (other than taxation) to the federal rule. This means medical only unless the dental and/or vision plan is an integral part of the medical package.

### **The Meaning of Integral**

Dental and vision are integral parts of the medical plan unless:

- The dental or vision plan is under a separate contract; and,
- Employees can elect dental or vision separately; and,
- Employees pay an additional contribution amount for the coverage.

If not, Plan Sponsors must offer dental and vision to adult dependent children as a part of their medical package offering.

### **Action Plan**

1. It is even more important now for California employers to conduct a survey of all dependents covered under their respective group health plans.
2. If employers who enroll in the medical plan automatically get coverage under a dental or vision plan with no additional contribution requirement, then the adult children get dental and vision as well. If the dental and vision plans require separate elections, then adult children will have access to medical only.
3. Initiate discussions with your payroll service immediately.

Copyright © 2010 Alfred B. Fowler, Attorney at Law. All Rights Reserved. This legislative update is published as an information source for our clients and colleagues. It is general in its nature and is no substitute for legal advice or opinion in any particular case.

\*\*\*\*\*

Howitt Benefit Services (HBS) is not an attorney firm and HBS is not giving legal advice or interpreting the law. This update is published as an information source for our clients and colleagues. It is general in nature and not a substitute for legal advice or an opinion on a particular case. For more information, contact us at [benefits@howittins.com](mailto:benefits@howittins.com) or at 1-866-445-1550.