

CLIENT ALERT

STATE LAW CONFORMITY TAXATION OF EMPLOYER-PAID HEALTH COVERAGE OF EMPLOYEES' DEPENDENTS TO AGE 26 (As of April 20, 2011)

For plan years beginning on or after September 23, 2010, the Patient Protection and Affordable Care Act (“**PPACA**”) requires employer group health plans that provide dependent child coverage to make the coverage available to an employee's child until the child reaches age 26. Effective March 30, 2010 the Health Care and Education Reconciliation Act of 2010 (“**HCERA**”) was enacted to expand the favorable tax treatment provided for employer-provided medical coverage to include the PPACA-mandated adult-child coverage.¹ While most states follow the Internal Revenue Code when it comes to defining "wages" and other forms of taxable income, unless the state's revenue code is drafted to automatically conform to changes made in the Internal Revenue Code, state action is needed to maintain the conformity. The period between the enactment of a federal law and the enactment of conforming state legislation creates reporting and payroll concerns to employers. The following chart summarizes the current status of state tax law legislation conforming to the Internal Revenue Code definition of dependent for employer-provided health coverage.

STATE	AUTOMATIC CONFORMITY WITH FEDERAL STATUTES	CONFORMING LEGISLATION OR ANNOUNCEMENT	NO CONFORMING LEGISLATION OR ANNOUNCEMENT	NO STATE PERSONAL INCOME TAX
ALABAMA	X			
ALASKA				X
ARIZONA			X	
ARKANSAS			X	

¹ Specifically, (i) section 105(b) of the Internal Revenue Code, which excludes from the employee's gross income employer-provided reimbursements for the medical care of the employee, spouse or dependents, was expanded to also exclude reimbursements for the medical care of an employee's child who has not attained age 27 as of the end of the taxable year, (ii) section 162(l)(1) of the Internal Revenue Code, which allows a self-employed individual to deduct the cost of medical insurance for the individual, spouse, and dependents, was expanded to also include the cost of coverage for the individual's child who has not attained age 27 and (iii) section 501(c)(9) of the Code, which exempts voluntary employees' beneficiary associations (“VEBAs”) from tax, was expanded to permit VEBAs to provide sick and accident benefits to a member's child who has not attained age 27.

STATE	AUTOMATIC CONFORMITY WITH FEDERAL STATUTES	CONFORMING LEGISLATION OR ANNOUNCEMENT	NO CONFORMING LEGISLATION OR ANNOUNCEMENT	NO STATE PERSONAL INCOME TAX
CALIFORNIA		X ²		
COLORADO	X			
CONNECTICUT	X			
DELAWARE	X			
DISTRICT OF COLUMBIA	X			
FLORIDA				X
GEORGIA			X	
HAWAII			X	
IDAHO			X	
ILLINOIS	X			
INDIANA			X	
IOWA		X ³		
KANSAS	X			
KENTUCKY		X ⁴		
LOUISIANA	X			
MAINE			X	
MARYLAND	X			
MASSACHUSETTS			X	
MICHIGAN	X			
MINNESOTA		X ⁵	X ⁶	

² The California State Legislature approved A.B. 36 on March 24, 2011, which conforms California tax law to PPACA provision eliminating federal tax on employer-paid coverage for employee's adult children to age 26. Employer's who previously calculated a fair market value benefit and imputed such amount as income for California Personal Income Tax wages may correct the wages and withholding amount by following the appropriate provisions in the 2011 California Employer's Tax Guide.

³ The Iowa Department of Revenue has determined that Iowa Code §422.7 provides that the value of health care coverage provided for a nonqualified dependent ages 25 and 26 is not subject to Iowa income tax. Consequently, the value of such coverage is excluded from the employee's gross income through the end of the taxable year in which the child turns age 26. See Iowa Department of Revenue Notice, *Health Care Coverage for Nonqualified Dependents*, 12/23/10. It is not clear whether this guidance will provide for the retroactive recoupment of income taxes for the fair market value of any benefits previously reported as Iowa income. Accordingly, further monitoring of this issue is required.

⁴ The Kentucky General Assembly passed House Bill 255, which was signed into law on March 16, 2011, extending federal income tax treatment to the extended health care insurance for certain adult children. It is not clear whether this guidance will provide for the retroactive recoupment of income taxes for the fair market value of any benefits previously reported as Kentucky income so further monitoring of this issue is required.

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MISSISSIPPI			X	
MISSOURI	X			
MONTANA	X			
NEBRASKA	X			
NEVADA				X
NEW HAMPSHIRE				X
NEW JERSEY			X	
NEW MEXICO	X			
NEW YORK	X			
NORTH CAROLINA			X	
NORTH DAKOTA	X			
OHIO	X			
OKLAHOMA	X			
OREGON			X ⁷	
PENNSYLVANIA	X			
RHODE ISLAND	X			
SOUTH CAROLINA			X	

⁵ Minnesota amended state tax law to conform to federal tax law only for 2010. See Minn. Stat. §289A.02, subd. 7 (2011). Employers are not required to issue corrected W-2 forms or amend existing withholding tax returns. Employees who have not yet filed their Minnesota tax return should not add the value of the coverage for purposes of filing their 2010 Minnesota return on Form M1. Employees who have filed should not file an amended return, and the department will make any necessary adjustments. See Minnesota Revenue web site.

⁶ Minnesota has not adopted legislation for years after 2010. Since employees will be required to include those federally exempt benefits as income on their 2011 Minnesota income tax returns unless Minnesota law is changed, the Department of Revenue encourages employers to share this information with affected employees so the employees can decide whether to elect additional withholding if they are concerned about being sufficiently withheld. Employees can elect additional Minnesota withholding by completing Form W-4MN, Minnesota Employee Withholding Allowances/Exemption Certificate. See Minnesota Revenue web site.

⁷ The Oregon Department of Revenue has taken the position that that provision of health coverage to a child who is not a "dependent", i.e., not a qualifying child or dependent under the January 1, 2009 Internal Revenue Code), will result in taxable imputed income. The amount of imputed income is the fair market value of the coverage. *The department recommends that employers take the necessary steps to include these amounts on the affected employee's W-2 statement for tax year 2010.* The department further suggests one method for computing the imputed income is to use the plan's COBRA rate minus the administrative fee. *This interpretation may not apply following 2010 due to an amendment to ORS §316.013, which matches Oregon law to federal definition of taxable income to match federal law definition of same; however, we were unable to find any additional guidance confirming this point so further monitoring of this issue is required.*

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SOUTH DAKOTA				X
TENNESSEE				X
TEXAS				X
UTAH	X			
VERMONT	X			
VIRGINIA		X ⁸		
WASHINGTON			X	
WEST VIRGINIA			X	
WISCONSIN			X ⁹	
WYOMING			X	X

Please note that this information is provided as general guidance with respect to the current status of state conforming tax legislation. For specific guidance regarding any state's tax laws, you should seek local counsel in such state or locality.¹⁰

IRS Circular 230 Disclosure: To the extent this communication contains any statement regarding federal taxes, that statement was not written or intended to be used, and it cannot be used, by any person (i) as a basis for avoiding federal tax penalties that may be imposed on that person, or (ii) to promote, market or recommend to another party any transaction or matter addressed herein.

⁸ Virginia amended § 58.1-301e Code of Virginia to conform to federal tax laws effective on December 31, 2010. It is not clear whether this guidance will provide for the retroactive recoupment of income taxes for the fair market value of any benefits previously reported as Virginia income. Accordingly, further monitoring of this issue is required.

⁹ Wisconsin follows the Internal Revenue Code as in effect on December 31, 2008. The Wisconsin Department of Revenue has issued guidance that states that the requirement to include the fair market value of employer-provided health insurance benefits for nondependent adult children under the age of 27 applies for Wisconsin tax years beginning in 2010 and thereafter.

¹⁰ We are not authorized to give advice with respect to state or local laws outside of our jurisdiction (Texas). If you would like specific guidance regarding any other state's or locality's tax laws, we are happy to consult with local counsel in such state or locality or to assist in obtaining local counsel in such state or locality.