

Benefit Brief



SUBJECT: New Definition of Dependent under IRC § 152

DATE: November 15, 2005

This Benefit Brief summarizes the effect of the new Internal Revenue Code definitions of qualifying child and qualify relative under §152 on employee welfare benefit plans.

Sections 105 and 106 of the Internal Revenue Code (the "Code") provide that employees will not be taxed either on the value of the health benefits that they receive from a health plan or on the premium (or other) amounts paid by the employer for the health coverage. Employees are only allowed to exclude this income if they cover "dependents" as defined under the Code.

New Code Section 152 now defines a dependent as a "qualifying child" or a "qualifying relative." To satisfy the definition of a "qualifying child," a child must meet the following requirements:

- have a specified relationship to the employee (child, stepchild, foster child, sibling, step-sibling or dependent of one of these);
- have the same principal residence as the employee for more than one-half of the taxable year;
- satisfy age requirements (i.e., must not have attained age 19 (age 24 for a student) before the close of the calendar year, or must be totally and permanently disabled); and
- not provide more than one-half of his or her own support.

Previously, the definition of dependent did not include a residence or age requirement for qualifying children.

If an individual does not satisfy the definition of a "qualifying child," the individual may still be treated as a "qualifying relative." To satisfy the definition of a "qualifying relative," the individual must meet the following requirement:

- have a specified relationship to the employee (child, stepchild, foster child, sibling, step-sibling or dependent of one of these) or be an individual (other than a spouse) who has the same principal residence as the employee and is a member of the employee's household; and
- receive over one-half of his or her support from the employee.

If there is a joint custody situation, there are special rules that permit divorced or separate parents to agree that the child will be treated as the qualifying child of the non-custodial parent.

What you need to look for in your Group Health Plans

1. Does the definition of dependent require that the child live with the parent?

If it does not include this requirement, it should be added.

2. Does the definition of dependent require either that the employee provide more than half of the child's support or that the child is "primarily dependent on the employee"?

If it does not include this requirement, it should be added.

3. Does the provision for coverage of college students require that the student receive more than half of his or her support from the employee or that the student is "primarily dependent upon the employee"?

If not, this requirement should be added.

Definitions of Dependent that refer to § 152 of the Code

If your group health plan or flexible spending account has a definition that refers back to section § 152 of the Code, you will not need to make any changes.

Adopted Children and Children Placed for Adoption

ERISA and the Code both require and allow adopted children to be treated as if they are "children" from the point that they are "placed for adoption" with the employee. Therefore, your plan can cover adopted children and those placed for adoption and provide tax free benefits to employees for these individuals.

Additional Requirements for Dependent Care Assistance Programs

In addition to the requirements for qualifying child and qualifying relative that are discussed above, a qualifying relative for purposes of a Dependent Care Assistant must not earn more than \$3,200 per year. Coverage is permitted for children under age 13 and for any other qualifying relative or spouse who is physically or mentally incapable of caring for himself or herself subject to the income limitation.

Why this matters

If your health plan is covering dependents who do are not either qualifying children or qualifying relatives under Section 152, then you are required to impute income to the employee who is receiving benefits for these individuals. An easier approach would be to change any dependent eligibility requirements that do not conform to these changes in the Code, though this may result in the loss of eligibility of some dependents.

If you have any questions about how the new definition of dependent applies to your health plans, or if you have any questions about complying with these rules, please contact Judy Griffith at The Benecon Group at jgriffith@benecon.com, or the number shown below.