

WHAT YOU NEED TO KNOW



Cafeteria Plans: Qualifying Events and Changing Employee Elections

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Cafeteria plans, or plans governed by IRS Code Section 125, allow employers to help employees pay for expenses such as health insurance with pre-tax dollars. Employees are given a choice between a taxable benefit (cash) and two or more specified pre-tax qualified benefits, for example, health insurance. Employees are given the opportunity to select the benefits they want, just like an individual standing in the cafeteria line at lunch.

Only certain benefits can be offered through a cafeteria plan:

- Coverage under an accident or health plan (which can include traditional health insurance, health maintenance organizations (HMOs), self-insured medical reimbursement plans, dental, vision, and more);
- Dependent care assistance benefits or DCAPs
- Group term life insurance
- Paid time off, which allows employees the opportunity to buy or sell paid time off days
- 401(k) contributions
- Adoption assistance benefits
- Health savings accounts or HSAs under IRS Code Section 223

Some employers want to offer other benefits through a cafeteria plan, but this is prohibited. Benefits that you cannot offer through a cafeteria plan include scholarships, group term life insurance for non-employees, transportation and other fringe benefits, long-term care, and health reimbursement arrangements (unless very specific rules are met by providing one in conjunction with a high deductible health plan). Benefits that defer compensation are also prohibited under cafeteria plan rules.

Cafeteria plans as a whole are not subject to ERISA, but all or some of the underlying benefits or components under the plan can be. The Patient Protection and Affordable Care Act (ACA) has also affected aspects of cafeteria plan administration.

Making Election Changes

Employees are allowed to choose the benefits they want by making elections. Only the employee can make elections, but they can make choices that cover other individuals such as spouses or dependents. Employees must be considered eligible by the plan to make elections. Elections, with an exception for new hires, must be prospective. Cafeteria plan selections are considered irrevocable and cannot be changed during the plan year, unless a permitted change in status occurs. There is an exception for mandatory two-year elections relating to dental or vision plans that meet certain requirements.

Plans may allow participants to change elections based on the following changes in status:

- Change in marital status
- Change in the number of dependents
- Change in employment status
- A dependent satisfying or ceasing to satisfy dependent eligibility requirements
- Change in residence
- Commencement or termination of adoption proceedings

Plans may also allow participants to change elections based on the following changes that are not a change in status but nonetheless can trigger an election change:

- Significant cost changes
- Significant curtailment (or reduction) of coverage
- Addition or improvement of benefit package option
- Change in coverage of spouse or dependent under another employer plan
- Loss of certain other health coverage (such as government provided coverage, such as Medicaid)
- Changes in 401(k) contributions (employees are free to change their 401(k) contributions whenever they wish, in accordance with the administrator's change process)
- HIPAA special enrollment rights (contains requirements for HIPAA subject plans)
- COBRA qualifying event
- Judgment, decrees, or orders
- Entitlement to Medicare or Medicaid
- Family Medical Leave Act (FMLA) leave
- Pre-tax health savings account (HSA) contributions (employees are free to change their HSA contributions whenever they wish, in accordance with their payroll/accounting department process)
- Reduction of hours (new under the ACA)
- Exchange/Marketplace enrollment (new under the ACA)

Together, the change in status events and other recognized changes are considered "permitted election change events."

Common changes that do not constitute a permitted election change event are: a provider leaving a network (unless, based on very narrow circumstances, it resulted in a significant reduction of coverage), a legal separation (unless the separation leads to a loss of eligibility under the plan), commencement of a domestic partner relationship, or a change in financial condition.

There are some events not in the regulations that could allow an individual to make a mid-year election change, such as a mistake by the employer or employee, or needing to change elections in order to pass nondiscrimination tests. To make a change due to a mistake, there must be clear and convincing evidence that the mistake has been made. For instance, an individual might accidentally sign up for family coverage when they are single with no children, or an employer might withhold \$100 dollars per pay period for a flexible spending arrangement (FSA) when the individual elected to withhold \$50.

Plans are permitted to make automatic payroll election increases or decreases for insignificant amounts in the middle of the plan year, so long as automatic election language is in the plan documents. An "insignificant" amount is considered one percent or less.

Plans should consider which change in status events to allow, how to track change in status requests, and the time limit to impose on employees who wish to make an election.

Cafeteria plans are not required to allow employees to change their elections, but plans that do allow changes must follow IRS requirements. These requirements include consistency, plan document allowance, documentation, and timing of the election change.

Consistency. In order to make the change an employee must have experienced the specified change or event, and the requested change must be consistent with the change or event.

Example: Susan is a full-time benefits eligible employee of The Oyster House. Susan becomes Medicare eligible and wishes to make changes to her cafeteria plan elections. If the plan allows, she would be permitted to make changes to any benefit that provides accident or health coverage, including a health FSA. She would not be permitted to make changes to other elections such as dependent care, paid time off, or group life insurance. There is no consistency between Medicare eligibility and paid time off needs.

The consistency rules require that an election change is due to and corresponds with the change in status that effects eligibility for coverage under the plan. There are relaxed consistency rules for group term life insurance, dismemberment and disability coverage. There are also special consistency rules for election changes when DCAP or adoption assistance plan expenses are affected, a limitation on changes due to divorce, death of a spouse or dependent, or a dependent's loss of eligibility, and a limitation on election changes decreasing or ending coverage because a new family member has become eligible.

DCAP elections cannot be changed because an unemployed individual enrolls in educational courses. If a medical plan automatically terminates dependents when they reach age 26, there would be no qualifying event because no changes would need to be made by the employee.

Overview of Consistent Changes

Type of Event	Permitted Change
Change in status event (marital status, number of dependents, employment status, dependent eligibility change, change in residence, commencement or termination of adoption proceedings)	May make election changes for all qualified benefits
Significant cost change	May make changes to all qualified benefits other than health FSAs
Significant coverage curtailment or reduction	May make changes to all qualified benefits other than health FSAs
Addition or significant improvement of benefit	May make changes to all qualified benefits other than health FSAs
Change in coverage under another employer plan	May make changes to all qualified benefits other than health FSAs
Involuntary loss of health coverage (such as coverage sponsored by the government or educational institution)	May make election changes for any group health plans
HIPAA special enrollment	Must allow employee to make changes for any group health plans that are not an excepted benefit under HIPAA

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Type of Event	Permitted Change
COBRA qualifying event	May make election changes for any group health plans subject to COBRA (this includes FSAs)
Judgments, decrees, or orders	May make election changes for accident or health coverage (this includes FSAs)
Medicare/Medicaid entitlement	May make election changes for any accident or health coverage
FMLA leave of absence	May make election changes to accident or health plan coverage, including health FSAs
Reduction of hours	May make changes for group health plans (not FSAs) that provide minimum essential coverage under the ACA
Exchange enrollment	May make changes for group health plans (not FSAs) that provide minimum essential coverage under the ACA (other rules apply)

Plan Documents. If an individual has a permitted election change event and the desired change is consistent with the event, then it must be determined if the cafeteria plan document recognizes the permitted election change event. If it does not (or the plan does not allow individuals not already on the plan to elect benefits mid-year), the election change is not allowed. If the plan recognizes the change event, not only does the cafeteria plan document have to allow the change, but the plan documents of the component benefit must allow it as well (such as the underlying plan documents for the group health plan).

Documentation and Timing. If the individual has a permitted election change event, the desired change is consistent with the event, and the plan documents allow the change, documentation that all of those requirements have been met should be made. A signed certification by the employee is sufficient. Under ERISA, these records should be kept for at least eight years. Employees are permitted to make changes electronically by self-certifying. The employer should keep electronic records of this change.

Plan administrators should administer election changes involving same-sex spouses in the same manner that they handle election change requests for individuals with opposite-sex spouses.

Change in Status Events

As mentioned above, plans may allow participants to change elections based on an IRS-specified list of change in status events.

Change in Marital Status

Both same-sex and opposite-sex marital status changes are qualifying events. Legal separations (unless the legal separation leads to loss of eligibility under the plan) and the commencement and termination of a domestic partnership are not. There is a narrow exception if a domestic partnership changes an

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individual's tax status. If a domestic partner qualified as a tax dependent for health coverage purposes, this could trigger a qualifying event.

Example	Permitted election change event?
Jessica gets married to Timothy.	Yes
Timothy gets married to Christopher.	Yes
Jennifer enters into a domestic partnership (with either a same or opposite sex individual).	No, unless the domestic partnership changes an individual's tax status. If the domestic partner becomes a tax dependent, it could trigger a qualifying event.

Change in the Number of Dependents

The change in a number of dependents can trigger a qualifying change in status event. Birth, adoption, or placement for adoption will likely trigger a HIPAA special enrollment right, which creates a responsibility for plans subject to HIPAA (discussed later). "Dependent" refers to tax dependent under IRS Code Section 152, with an exception for accident and health coverage, under which a child to whom IRS Code section 152(e) applies is treated as a dependent of both parents. IRS Code Section 152(e) involves rules for divorced parents.

Change in Employment Status

A change in employment status that affects an individual's eligibility for a benefit is a permissible change in status event. The following events are a change in status of an employee (or their spouse, or dependent):

- Termination or beginning of employment
- Strike or lockout
- Return from or beginning of an unpaid leave of absence
- Change in worksite

If benefits eligibility is dependent upon employment status, and that status changes (such as a move from full time to part-time), this can be a qualifying event. However, unless a plan-allowed "reduction in hours or cost change event" (discussed below) occurs when an individual becomes part-time but is still benefits eligible, it is not a qualifying event.

A Dependent Satisfying or Ceasing to Satisfy Dependent Eligibility Requirements

If a tax dependent satisfies or ceases to satisfy the requirement for coverage due to aging out, changing student status, marriage, etc., this is a qualifying event. Practically speaking, due to the ACA's requirement to provide health coverage to children under the age of 26, marriage and student status changes are unlikely to trigger a qualifying event for health coverage. This might not be the case for other benefits such as vision or dental coverage.

Change in Residence

A change in residence that affects eligibility for coverage would be a qualifying event. The move must result in a loss of eligibility for coverage. FSAs cannot be changed due to a residence change. If, for example, an individual was covered by an HMO and moved out of the network of providers, the employee could be

permitted to drop coverage (if no other coverage was offered by the employer) or elect different coverage. Keep in mind that a carrier's network may have providers at the employee's residence or work location.

Example	Permitted election change event?
Joshua is enrolled in Underwater Diving's group health plan with single plus spouse coverage. His son Clyde, age 21, is released from prison and moves back in with his parents. Joshua asks Human Resources if he can add Clyde to the group health plan following his change in residence.	No. Although the group health plan would not have been utilized by Clyde when he was in prison, he was still technically eligible for coverage under the plan, despite his incarceration.

Commencement or Termination of Adoption Proceedings

For purposes of adoption assistance provided through a cafeteria plan, the commencement or termination of an adoption proceeding is a qualifying event.

Other Events that Allow a Change in Elections

Outside of the change in status events, the IRS recognizes other events that would allow a plan to permit an individual to make an election change.

Significant Cost Changes

A plan may permit individuals to make election changes due to significant cost changes. For this rule to apply the following must be met:

- A benefit plan must be an eligible qualified benefit other than a health FSA.
- The cafeteria plan document must include language regarding significant cost changes.
- The cost-change being passed on in the form of changed participant contributions must be significant.
- A determination must be made whether any alternative coverage is similar.

Employees would only be permitted to revoke or drop coverage due to a cost change if no similar coverage option is available, which is defined as "coverage of the same category of benefits for the same individuals." If an employer offers two medical plans, one that is expensive and one that is inexpensive, regardless of the cost change, an employee would only be permitted to switch to the other plan, not revoke coverage entirely. This rule would apply even if the two medical plans were very different, such as an HMO versus a high deductible health plan (HDHP). There is no definition of what constitutes a "significant" cost change, but the change can be employer or employee initiated.

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Example	Permitted election change event?
Susan works for ABC Widget Co., and her husband John works for XYZ Chicken Farm. They have coverage under John's group health plan offered by XYZ. It is announced that beginning next month, XYZ's plan cost will increase by \$40 a month. Susan asks Human Resources if she can enroll in ABC's group health plan as a result (it is not ABC's open enrollment period).	No. This is not a qualifying event for Susan because the significant cost increase was not related to ABC's group health plan. However, if John chooses to drop XYZ's plan as a result of the cost change, and ABC recognizes "Change in Coverage Under Another Employer Plan" (see below), Susan might be able to enroll under that qualifying event criteria.

Significant Coverage Curtailment or Reduction

Plans may allow employees to make mid-year election changes due to a significant coverage curtailment, with or without a loss of coverage. The definition of coverage curtailment is not entirely clear, and the regulations state that there is a significant curtailment of coverage "only if there is an overall reduction in coverage provided under the plan so as to constitute reduced coverage generally."

In the event of coverage curtailment without a loss of coverage, a participant is only permitted to revoke his or her election and elect similar coverage. If there is a loss of coverage, participants may only revoke elections if "no similar benefits package" is available. Again, if an employer offered two medical plans, the employee would only be permitted to elect the second plan.

Addition or Significant Improvement of Benefit Package Option

In the event an employer adds a new benefit package option or other coverage option, or if an existing option is significantly improved, eligible employees (including those who had not previously made an election) may revoke their election and make new elections on a prospective basis for coverage under the new plan or option. The term "significant improvement of coverage" is not defined but generally an increase in medical providers available in network is an improvement. If only one component of the cafeteria plan has an addition, changes can only be made to the election of that component.

Change in Coverage under Another Employer Plan

A cafeteria plan may permit a participant to make election changes due to a change in coverage under another employer plan. This would be triggered by one of two situations:

- The other employer plan allows a permissible election change.
- The other employer plan has a different period of coverage.

Example: Susan and John each have medical coverage from their individual employers. Susan's employer has a fiscal year plan; John's employer has a calendar year plan. Susan and John are married and make no changes to their elections at that time. Six months after getting married they determine that they would like to be on the same plan. Shortly thereafter, Susan's plan has open enrollment. She drops her employer coverage during open enrollment, thus triggering a permissible change that would allow John to enroll her in his employer's plan.

Loss of Group Health Coverage Sponsored by Governmental or Educational Institutions

A plan may allow participants to make changes due to the loss of coverage under other group health coverage, such as a state children's health insurance program (CHIP), a medical program of an Indian

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Tribal government, a state health benefits risk pool, or a foreign government group health plan. This change applies only to the loss of coverage, not to a gain. Loss of coverage from an educational institution would also qualify.

Example	Permitted election change event?
James works for Coastal Airlines and is enrolled in its group health plan. His spouse acquires TRICARE coverage for their family. James wishes to drop Coastal Airlines' group health plan as a result.	No.
James works for Coastal Airlines and is not enrolled in its group health plan, although he is eligible. His spouse loses TRICARE coverage for their family. James wishes to enroll in Coastal Airlines' group health plan as a result.	Unclear, but likely. Employers should seek guidance from their attorney and clearly outline in their plan documents, based on their attorney's advice, whether loss of TRICARE coverage would be allowed. (Loss of TRICARE coverage is not specifically discussed in the regulations.)

HIPAA Special Enrollment Rights

Group health plans subject to HIPAA must provide special enrollment for certain individuals. Plans are not required to allow pre-tax election changes for HIPAA special enrollment events; however the administrative overhead of handling these changes on an after-tax basis is often unduly burdensome.

HIPAA special enrollment rights overlap with other change in status events. The other events are permissive, but HIPAA enrollment events require the ability to make health coverage changes. HIPAA special enrollment rights also allow a limited ability to elect retroactive coverage on a pre-tax basis. HIPAA special enrollment events also obligate the employer to offer a special enrollment period of a minimum specific duration, typically 30 or 60 days depending on the event.

HIPAA special enrollment events include the loss of health coverage (including loss of eligibility for short-term, limited-duration insurance), acquisition of a new dependent (by marriage, birth, adoption, or placement for adoption) and loss of Medicaid or CHIP coverage.

Enrollment due to loss of coverage under a group health plan means loss of eligibility for non-COBRA coverage, termination of employer contributions toward non-COBRA coverage, or exhaustion of COBRA coverage. It could also apply to the loss of student or private insurance. HIPAA special enrollment events permit employees to add coverage for other dependents at the same time.

Although retroactive elections are typically prohibited, under HIPAA if a newborn or child who is adopted or placed for adoption is enrolled during the special enrollment period, the child can have retroactive coverage to the date of birth, adoption, or placement for adoption.

COBRA Qualifying Events

A plan may permit an individual to make changes due to COBRA qualifying events. This would allow an individual who went part-time, lost benefit eligibility and thus elected COBRA, to increase his or her salary reductions to pay the increased COBRA cost. This would only be permissible if the individual lost health

plan eligibility but not cafeteria plan eligibility. An individual whose child elected COBRA after reaching age 26 could also make a mid-year election change to increase pre-tax deductions to pay for the coverage for the rest of the taxable year.

Judgments, Decrees, and Orders

A plan may allow election changes due to a judgment, decree, or court order, including qualified medical child support orders (QMCSOs). Plan sponsors are not required to allow this change, but not doing so would create a legal conflict if the plan documents and court order are at odds. This exception allows employees to enroll a child in coverage or drop a child from coverage, as ordered by the court. This exception does not include voluntary changes in health coverage between a child's parents.

Medicare or Medicaid Entitlement

A plan may allow employees to drop or reduce coverage for themselves, their spouse, or dependents, when any of those covered individuals gain Medicare or Medicaid entitlement. If an employee drops coverage under the cafeteria plan for himself or herself, he or she should consider the impact on their covered spouse's or dependents' eligibility under their group plan.

FMLA Leave of Absence

A plan may allow election changes due to leaves of absence under FMLA. FMLA requires covered employers to permit eligible employees to take a certain amount of unpaid job-protected leave. An employer must maintain coverage under any group plan during FMLA leave at the level and under the conditions that would have been met if the individual had not gone on leave. However, a plan may allow an employee to revoke or continue coverage, or discontinue employee contributions. Upon return from leave, the employee has the right to have coverage reinstated if their coverage was terminated during the leave (for example, for failure to pay premiums). To pay for the continued coverage the employee may prepay, make ongoing payments, or make catch-up contributions.

Pre-Tax HSA Contributions

Employees may make changes to HSA contributions through pre-tax salary reductions at any time during the year, as long as the change is effective before the salary to which the change applies becomes available to the employee.

Reduction of Hours

One of the newest allowed events (beginning September 18, 2014), a plan may allow a participant whose hours are reduced below 30 hours a week as a result of a change in employment status to drop his or her employer-sponsored health coverage mid-year, regardless of whether the hour reduction caused a change in the employee's eligibility status. The IRS gave two conditions that must be met:

1. The employee has been in an employment status under which the employee was reasonably expected to average at least 30 hours of service per week and there is a change in that employee's status so that the employee will reasonably be expected to average less than 30 hours of service per week after the change, even if that reduction does not result in the employee ceasing to be eligible under the group health plan; and
2. The revocation of the election of coverage under the group health plan corresponds to the intended enrollment of the employee, and any related individuals who cease coverage due to the revocation, in another plan that provides minimum essential coverage with the new coverage

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effective no later than the first day of the second month following the month that includes the date the original coverage is revoked.

This would allow an employee, otherwise locked into coverage due to his or her employer's use of the ACA's measurement and stability period, to drop coverage during a stability period. Because this is a new optional event, employers that wish to provide the opportunity to employees should amend their plans.

Exchange or Marketplace Enrollment

Another change under the ACA, the Exchange/Marketplace enrollment event permits plans to allow participants who are eligible to enroll in Exchange/Marketplace coverage during a special enrollment period to drop employer-sponsored health coverage mid-year, so long as the employee intends to enroll in Exchange/Marketplace coverage. The employer only has to obtain a reasonable representation from the employee that he or she intended to enroll on the Exchange. The following conditions must be met for this change:

1. The employee is eligible for a special enrollment period to enroll in a qualified health plan through an Exchange/Marketplace pursuant to guidance issued by the Department of Health and Human Services and any other applicable guidance, or the employee seeks to enroll in a qualified health plan through an Exchange/Marketplace during the Marketplace's annual open enrollment period; and
2. The revocation of the election of coverage under the group health plan corresponds to the intended enrollment of the employee and any related individuals who cease coverage due to the revocation in a qualified health plan through an Exchange/Marketplace for new coverage that is effective beginning no later than the day immediately following the last day of the original coverage that is revoked.

Because this is a new optional event, employers that wish to provide the opportunity to employees should amend their plans.

Example	Permitted election change event?
Emily declines coverage offered by The Coffee Shop's group health plan because she is enrolled in Marketplace coverage. Emily chooses not to renew the Marketplace coverage. It is not currently open enrollment for The Coffee Shop, but Emily asks Human Resources if she can now enroll in the group health plan.	No. Emily's voluntary decision to decline re-enrolling in a Marketplace plan is not a qualifying event.
Emily declines coverage offered by The Coffee Shop's group health plan because she is enrolled in Marketplace coverage. Emily is notified that her Marketplace plan is being terminated at the end of the year when the insurer will stop participating in the Marketplace Exchange. It is not currently open enrollment for The Coffee Shop, but Emily asks Human Resources if she can enroll in the group	No, Marketplace termination of a plan is not a Section 125 permitted election change event. However, under HIPAA's special enrollment rights, Emily is entitled to enroll in The Coffee Shop's group health plan. Because Emily was otherwise eligible for The Coffee Shop's group health plan, when Emily loses Marketplace

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Example	Permitted election change event?
health plan, either now or when the Marketplace plan terminates.	coverage due to the insurer's exit from the Marketplace Exchange, Emily is entitled to special enrollment in The Coffee Shop's group health plan, whether or not Emily may enroll in other individual market coverage, through or outside of an Exchange. This special enrollment right does not apply if Emily lost Marketplace coverage due to failure to pay premiums or if Emily's coverage was terminated for cause.
Emily declines coverage offered by The Coffee Shop's group health plan because she is enrolled in Marketplace coverage. Emily fails to pay the premium for her Marketplace coverage and the policy is cancelled. It is not currently open enrollment for The Coffee Shop, but Emily asks Human Resources if she can now enroll in the group health plan.	No. Emily's failure to pay the Marketplace premium is not a qualifying event.

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