November 7, 2013

Transition Relief for Non-Calendar Year Cafeteria Plans

The IRS recently issued Notice 2013-71 which clarifies when non-calendar year cafeteria plans can permit employees to change their 2013 salary reduction elections to take into account the availability of coverage offered through the healthcare reform Marketplace (exchange) and their potential exposure to the individual mandate. This transition relief was initially set out in proposed regulations addressing the employer-shared responsibility (mandate) penalties.

Election change limitations. For participants in a non-calendar year cafeteria plan, health plan coverage through the Marketplace will first become available in the middle of the plan's 2013-2014 non-calendar plan year (that is, January 2014). When Marketplace coverage becomes available in 2014, plan participants may wish to enroll in that coverage and discontinue their employer-sponsored coverage. Or, alternatively, an employee who did not elect employer-sponsored coverage may wish to enroll in that coverage to avoid the individual mandate. For non-calendar year cafeteria plans, this may occur mid-plan year. Generally, cafeteria plan elections must be made before the start of the plan year and are irrevocable during the plan year, except for certain "changes in status" (such as termination of employment or marriage). Without the transition relief, the availability of health plan coverage through the Marketplace beginning in 2014 does not constitute such a change in status, which would mean that employees would not be able to change their salary reduction elections for health coverage during the non-calendar year plan year in order to cease their cafeteria plan coverage and elections and purchase coverage through the Marketplace.

Transition relief. In order to give employees greater flexibility to make changes in salary reduction elections for health coverage, a plan sponsor can (but is not required to) amend its non-calendar year cafeteria plan to permit one or both of the following changes in salary reduction elections during the plan year beginning in 2013:

- An employee who elected to salary reduce beginning in 2013 for health coverage through a non-calendar year cafeteria plan can prospectively revoke or change his/her election with respect to the health coverage once during that plan year without regard to whether the participant experienced a change in status event under the cafeteria plan rules; and
- An employee who did not make a salary reduction election beginning in 2013 for health coverage through a non-calendar year cafeteria plan (before the deadline for making elections) can make a prospective salary reduction election for health coverage on or after the first day of the plan year beginning in 2013 without regard to whether the participant experienced a change in status event under the cafeteria plan rules.

Amendment required. The notice makes clear that this relief may be adopted by all employers and not just those subject to the employer shared-responsibility mandate. The notice also provides that cafeteria plans can impose more, but not less, restrictive conditions on these options. For example, a non-calendar year cafeteria plan could limit the number of months during which employees who want to enroll in health coverage offered through a Marketplace may make cafeteria plan election changes (e.g., permit revocations only during January, or only during January, February and March, rather than at any time during the plan year). The transition relief may be applied beginning on or after December 28, 2012, the date the proposed regulations were issued. To allow this relief, a plan sponsor must amend the relevant cafeteria plan document accordingly. The plan sponsor can adopt this amendment retroactively but must do so by December 31, 2014, effective retroactively to the first day of the plan year beginning in 2013.

Next steps. With the introduction of Marketplace coverage, several considerations need to take place as individuals contemplate enrollment choices, changes and limitations. The coordination of Marketplace coverage, employer-sponsored health coverage, and compliance with other laws is important and if necessary, should be considered as election changes are made and administered. Employers that manage calendar year plans will have a plan year that aligns with the Marketplace enrollment year, so employees looking to change at their normal open enrollment from employer-sponsored coverage to Marketplace coverage, or vice-versa, will likely not experience any gaps in coverage.

Employers with non-calendar year section 125 plans need to decide if they will take advantage of the transition rule for their 2013 plan year. Non-calendar year plan sponsors also must determine whether to permit one or both of the allowable changes (i.e., allow a prospective revocation/change to an existing election, and/or a prospective new election for employer coverage), and decide whether to place any restrictions on the election (e.g., permit changes only during December 2013). Employers must then advise employees of the new election change opportunity and amend their section 125 plans to account for the additional mid-year change events.

Should you have questions about this or any aspect of federal health insurance reform, contact your Conner Strong & Buckelew account representative toll free at 1-877-861-3220. For a complete list of Legislative Updates issued by Conner Strong & Buckelew, visit our online Resource Center.