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REFORM Update

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The IRS recently released a Notice of Proposed Rule Making clarifying employers' shared health care reform responsibilities. The notice covers many of the questions employers have had on the "play or pay" requirements. Topics covered in depth include:

- Employers subject to "play or pay"
- Full-time employee status determination (30 or more hours a week)
- Employer penalties calculations
- Coverage affordability safe harbors
- Transitional relief for non-calendar year plans
- Section 125 plan years beginning in 2013

The IRS has requested stakeholder comments by March 18, 2013 on a number of issues in this proposed rule. The IRS has a public hearing scheduled for April 23, 2013, to address any further stakeholder concerns.

Employers Subject to "Play or Pay"

The "play or pay" rules apply to large employers. A large employer is one that has 50 or more full-time and full-time equivalent employees (FTEs). This proposed rule answers several questions regarding large employers:

- The employer must take into account both full-time employees and full-time equivalents.
- The measurement is based on the average number of employees on business days during the previous calendar year.
- IRS control group rules will determine who the employer is for meeting the 50-life threshold.
- Employees working outside the United States will not be counted toward the 50-life threshold.
- These rules do not cover predecessor or successor employer situations. The IRS has asked for comments on whether the established rules on taxable wages should be used to determine the large employer threshold in these situations.
- New employers can't use the previous calendar year for measurement. They are subject to "play or pay" if they are reasonably expected to employ an average of at least 50 full-time employees (including equivalents) on business days during the current calendar year. The government has requested comments on whether new employers need additional guidance.

The notice discusses seasonal employees in detail. If an employer with seasonal employees averages over 50 lives for fewer than 120 days, or four calendar months, then the "play or pay" provisions will not apply. This 120-day limit is used **only** to confirm whether the "play or pay" provisions apply. Different standards are used to determine whether to count seasonal employees as full-time employees when calculating the penalty.

Most employers will clearly fall above the 50-employee threshold and will have to "play or pay." Other employers may need to add full-time employees to full-time equivalents to determine whether they reach the threshold. To calculate full-time equivalents, employers should:

1. Calculate the total number of hours of service (no more than 120 hours for any one employee) for all part-time employees per month.
2. Next, divide the total hours of service by 120 hours.

The result is the number of FTEs for the month. Take fractions into account. Add full-time employees and the number of FTEs for each month, and divide the grand total by 12. This is your full-time employee/equivalent counts. If the total number of full-time employees and FTEs is 49.8, round the fraction down. Thus, this employer has 49 employees and is, therefore, not subject to "play or pay."

Transitional relief is provided to determine large employer status in 2014. Instead of using all 12 months of 2013 to measure the number of full-time employees, an employer may measure using any consecutive six-month period in 2013. For example, an employer could use the period from January 1, 2013, through June 30, 2013. This six-month measurement period will allow the employer time to analyze the results, determine whether to offer a plan and establish that plan.

To determine whether an employee and employer relationship exists, use the common law standard. Does the person for whom the services are performed have the right to control and direct the individual's work? The employee must be subject to the will and control of the employer. The employer determines what the employee will do and how to do it. Independent contractors, therefore, would not be considered employees.

For the "play or pay" rules, a sole proprietor, a partner in a partnership or a 2 percent or more Subchapter S shareholder is not an employee. An employee who provides services as both an employee and a non-employee (such as an employee who is also a director) is an employee for the hours of service spent working as an employee.

The new rules confirm that employers **must** cover full-time employees and their dependents (children up to age 26). The term "children" would include an employee's child, step-child, adopted child, a foster child or a child placed for adoption. Spouses **are not** included in this definition of dependents. Thus employers could choose not to cover spouses and still meet the "play or pay" requirements.

Employers who do not currently cover dependents will pay no penalty for the plan year beginning in 2014 if they take steps during that time to offer dependent coverage. For plan years beginning in 2015 and later, employers must cover full-time employees and their dependents to avoid penalties.

Full-Time Employee Status Determination (30 or more hours a week)

Initial guidance on determining full-time employment was issued last year and explained in our Reform Update at http://www.mcgrawwentworth.com/Reform_Update/2012/Reform_Update_51.pdf. The proposed rules offer more detail to help employers determine whether employees work 30 or more hours a week.

The regulations clarify when employers must begin the measurement periods to determine whether employees whose work hours vary are full-time employees. Employers using look-back periods must start their first measurement period in 2013. The corresponding stability period must start in 2014. While it is not completely clear, it appears that the IRS expects employers to align stability periods with their plan year. To illustrate, assume an employer has an October 1 to September 30 plan year. For ongoing employees, the employer may decide to set a measurement period from August 1 to July 31. The employer would have an administrative period from August 1 to September 30. The stability period would be from October 1 to September 30. If this is the case, the employer could start the first measurement period on August 1, 2013. An employer choosing a stability period that does not align with the plan year should probably consult a lawyer if upcoming guidance does not further clarify this issue.

The Departments recognize that some employers may face time constraints if they intend to use 12-month measurement periods and stability periods. For measurement periods in 2013, employers can use a transitional option:

- The measurement period beginning in 2013 can be shorter than 12 months, but must be at least six months.
- The measurement period must begin no later than July 1, 2013.
- The measurement period must end no earlier than 90 days before the first day of the first plan year beginning on or after January 1, 2014.

The goal for the transitional guidance is to allow employers to align stability periods with plan renewals. For example, let's say an employer has a plan year that runs from April 1 through March 31 and wants to include a 90-day administrative period. This employer could use a measurement period for 2013 only that begins on July 1, 2013, and runs through December 31, 2013. The administrative period would end on March 31, 2014. The stability period would begin on April 1, 2014. The stability period can be 12 months.

In another example, the employer's plan year runs from July 1 through June 30. In this case, the 2013 measurement period would have to exceed six months to comply with the requirement that it begin no later than July 1, 2013. This employer could start the 2013 measurement period on June 15, 2013. It would end on April 14, 2014. The employer could include an administrative period that runs from April 15 through June 30. The stability period would begin on July 1, 2014.

As a part of this transitional relief, in the first year only, an employer can have a shortened measurement period. In the example above, if the employer wanted a 12 month period for 2014, they could adopt a measurement period of April 15, 2014 to April 14, 2015.

Employers using a full 12-month measurement period need not begin that period by July 1, 2013. For example, an employer with a plan year beginning on November 1, 2014, could have a 12-month measurement period. The measurement period could run from September 1, 2013, until August 31, 2014. The administrative period could be from September 1, 2014, through October 31, 2014. The stability period would begin on November 1, 2014.

New details will answer many questions on determining full-time status. Full-time employees are those who average 30 or more hours of service a week, or 130 hours a month. Hours of service include the following:

1. Each hour for which an employee is paid, or entitled to payment for the performance of duties for the employer.
2. Each hour for which an employee is paid, or entitled to payment, even if no work is done. This would include vacation, holiday, illness, incapacity, layoff, jury duty, military duty or leave of absence.

For employees not paid by the hour, employers can calculate the hours of service using one of the three following methods:

1. Count the actual hours worked and any hours for which the employee is entitled to compensation.
2. Use a days-worked equivalency method. In this method employees are automatically credited for eight hours of service for each day that they would be credited with at least one hour of service.
3. Use a weeks-worked equivalency method. In this method employees are automatically credited for 40 hours of service for each week that they are credited with at least one hour of service.

Employers need not use the same method for all non-hourly employees. Employers may apply different methods for different classes of employees. The class, however, must be determined reasonably and the method applied consistently. Employers can change the method they use every calendar year.

Employers cannot use the days-worked or weeks-worked equivalency methods if using them would substantially understate an employee's hours of service. For example, assume an employer chooses the days-worked equivalency method. An employee works 3 days a week, 11 hours a day. Using actual hours worked, this employee is considered full-time at 33 hours a week. Using the days-worked equivalency, the employee would not be considered full-time at 24 hours a week. In this situation, the days-worked equivalency could not be used. The equivalency methods must reflect the paid hours generally worked

To determine whether an employee is full-time, count all hours worked for employers in the same control group.

Hours worked for services performed outside the United States do not count. Employees working overseas generally will not have hours of service, and are not counted as full-time employees for penalty calculation purposes. However, all hours of service for which an individual received U.S.-sourced income count as hours of service.

An employer must cover full-time employees or pay a penalty as discussed in the next section. Some employees are hired specifically for full-time positions. If these positions have predictable full-time hours, these employees are considered full-time as of their hire dates. These new regulations make it clear that employees expected to work 30 or more hours a week must be treated as full-time, and not variable-hour employees. The regulations make this distinction especially for positions with high turnover. An employer can't treat a full-time employee hired into a high turnover position as a variable-hour employee to avoid the requirement to offer coverage or pay the penalty.

For some employees, hours of service are much less predictable. Guidance from 2012 provided options for determining full-time status. The latest regulations do not materially change the approach proposed last year. The details are explained in our Reform Update at http://www.mcgrawwentworth.com/Reform_Update/2012/Reform_Update_51.pdf.

The new regulations more clearly define variable-hour and seasonal employees:

- An employee is treated as a variable-hour employee if, based on facts and circumstances, an employer cannot determine whether the employee will work 30 or more hours a week. Let's say an employer hires a variable-hour employee for more than 30 hours a week, but cannot determine whether the employee will work 30 hours a week for the whole measurement period. In this situation, the employer can treat these employees as variable-hour employees.
- Employers can change their standard measurement and stability periods, but they cannot change periods that have already begun.
- The stability period for new variable-hour employees has to be the same length as the stability period for ongoing employees.
- The new regulations allow employers to begin and end measurement periods on regular payroll periods. This only applies if payroll periods are one week, two weeks or semi-monthly. For example, an employer may have a calendar-year measurement period. The employer may decide to start counting as of the ***first full*** pay period in January. To align with the calendar year, the employer would have to include the December 31st pay period in the measurement period.

The latest guidance allows employers to use a reasonable, good faith interpretation of "seasonal employees" for 2014. The IRS is contemplating how to define seasonal employees and may use a time limit. For example, the IRS is considering that seasonal work should not exceed six months. It will continue to allow a good faith interpretation to be used until it formally defines "seasonal." However, several examples in the regulations suggest that employers should treat seasonal employees as variable hour employees. If the employees are truly seasonal and the employer has a long enough measurement period, the average hours worked will likely be less than 30/week.

Educational institutions cannot treat employees that work only during the academic year as seasonal employees. That would not be a good faith interpretation of the term.

The new rules also explain how to handle a change in employment for variable-hour and seasonal employees during the ***initial*** measurement period. This is defined as a material change in position or employment status when the employee has begun employment in a new position or is expected to work 30 or more hours a week. In this situation, the employee will be treated as a full-time employee on the earlier of:

- The first day of the fourth month following the change in employment status.
- The first day of the first month following the end of the initial measurement period and any associated administrative period, if the employee averaged 30 hours of service or more a week.

A change in status for an ongoing employee does not change the employee's status as a full-time or part-time employee during a stability period. The regulations also do not explain how to handle changes in employment status for regular full-time employees. It seems, however, that if you cover a new regular full-time employee within 90 days of the change in employment status, you will not run afoul of the rules.

Rehire situations

The new rules also deal with rehiring variable-hour employees. Employers can treat employees with no hours of service credited for at least 26 consecutive weeks as new employees when they return to work. Employers can treat employees working fewer than 26 weeks as newly hired when:

- The period of "no service" is at least four weeks long ***and***
- The period of "no service" is longer than the time the employee spent working.

For example, assume an employee works three weeks for an employer, leaves the company, and is then rehired 10 weeks later. The employee is considered newly hired because more than four weeks have elapsed without service. In addition, the 10-week period of "no service" is longer than the three weeks of active employment.

These rules apply only to employers that use the look-back measurement period to determine full-time status.

If an employer cannot treat a rehired employee as a new employee, then the employee is referred to as a "continuing" employee. The measurement and stability periods used for that employee before the period of no service hours apply again when the employee returns. If the employer needs to reinstate the employee's coverage, the reinstatement must be effective as of the return to work date, or as soon as administratively practicable.

Specific rules are proposed for special unpaid leaves, such as FMLA leave, USERRA leave and unpaid jury duty. The rules explain how to average the weekly hours of service in these situations. The employer can handle them in two ways:

1. Determine the average hours of work per week based on the time the employee spent in active service. This average disregards any time spent on a special leave.

2. Credit the hours of service during the special leave at the same rate in which hours were credited during the time spent actively employed during the measurement period.

Non-standard work situations

The government knows that some employers base their compensation on something other than hours worked. It will issue more guidance to help these employers. The proposed guidance considers a few situations directly.

Educational Institutions

Educational institutions are unique because they operate on an academic year. Traditional winter and spring breaks are often paid leave. Institutions must consider these hours when they calculate hours of service. The rules propose an averaging method that will allow an employee who works full-time during the academic year to be treated as a full-time employee.

Special employment break rules will apply for educational institutions to help them determine hours of service. An employment break is a period of least four consecutive weeks with no hours of credited service. An educational institution must either:

1. Determine average hours of service during the measurement period, excluding the employment break. The employer should use those average hours for the entire measurement period.
2. Credit hours of service during the employment break at a rate equal to the average weekly rate during the measurement period, not taking into account the employment break.

The educational institution does not need to credit more than 501 hours of service for any employment break. The 501 hours of service does not take into account any time off for special unpaid leave (FMLA, USERRA and jury duty).

The IRS has asked for comments on whether the above rules should apply to all employers. If it does expand the rules, they will not become effective until 2015.

Commission-Based Employees/Transportation Employees/Adjunct Faculty

The regulations request comments on how best to determine the hours of service for such employees. Until employers receive more information, they must use a reasonable method for calculating hours worked. A method **would not be** reasonable if it took into account only some of the employees' hours of service. For example, for an adjunct faculty member, an employer could not just measure instruction time because that would under-represent hours of service. A faculty member also spends time preparing lessons and grading student work. The employer must make a reasonable estimate of all the time an adjunct faculty member spends on a course in order to determine hours worked. Similarly, traveling salespeople could not have their service hours based solely on time spent on sales calls. At a minimum, employers would need to include travel time. In addition, employers must include an estimate of time spent preparing materials for a sales call.

<u>Temporary Staffing Agencies</u>

The IRS also wants comments on temporary staffing agencies, because the IRS recognizes that these agencies have unique challenges when they try to determine full-time employment. A temporary staffing agency is a common law employer that provides employees to a client. IRS Revenue Ruling 70-630 illustrates the facts and circumstances that occur when the staffing agency is considered the common law employer.

Staffing agency employees inherently have breaks in service, and expect periods with no work. In some cases, the work is sporadic. The IRS wants comments on whether to develop a safe harbor for these employees.

The new rules include provisions to prevent abuse of the "play or pay" rules. One of these possible abuses involves an employer splitting the hours of service for full-time employees. The employer would directly hire employees for 20 hours a week and then hire the same people through a temporary staffing agency to work an additional 20 hours a week. This arrangement would allow both the employer and the temporary staffing agency to treat these employees as part-time. However, under the new rules, in this situation all hours of service will be attributed to the employer.

<u>Employers Participating in Multiemployer Plans</u>

It may be a challenge to determine whether employees that qualify for multiemployer plans reach the full-time hourly threshold. Some multiemployer plans establish eligibility on criteria other than hours worked. In these situations, employees may work for multiple employers that participate with the plan. Because the IRS recognizes that hours worked may not be a practical measure for multiemployer plans, it has asked for comments on how the "play or pay" mandate should apply to multiemployer plans.

The IRS has established a transitional rule for 2014. An applicable large employer will not be treated as failing to offer employer-sponsored coverage if:

1. The employer contributes to a multiemployer plan for full-time employees under a collective bargaining agreement.
2. The multiemployer plan covers full-time employees and their dependents (dependent children).
3. The coverage passes the benefits and affordability tests. For affordability, the single contribution can exceed 9.5 percent of the wages reported to the multiemployer plan. Wages can be based on actual wages or an hourly rate under the collective bargaining agreement.

<u>**Employer Penalties Calculations**</u>

IRS controlled group rules determine whether an employer is a large employer for "play or pay" rules. However, it calculates penalties based on individual employers. If three related employers are grouped together to determine whether the employer is subject to "play or pay," then the penalty will be calculated separately for each of the three employers.

The new regulations detail how the IRS will determine the penalty. An employer may be assessed a penalty if:

1. In any month, a full-time employee has received an applicable premium tax credit or a cost-sharing reduction **and** the large employer did not offer substantially all employees (and their dependents) minimum essential coverage under an employer-sponsored health plan. This penalty is $2,000 annually, assessed monthly. The $2,000 penalty applies to **all** full-time employees, less the first 30.
2. In any month, if employer-sponsored coverage for full-time employees (and their dependents) fails either the benefits or affordability test for an employee **and** that employee receives subsidized coverage through the Exchange. This penalty is $3,000 annually, assessed monthly. It is assessed for each full-time employee receiving subsidized individual coverage in the Exchange. The penalty amount cannot be greater than the penalty assessed in the preceding bullet. If this penalty is greater, then the penalty is capped at the previous bullet's liability.

Following are more details on applying the penalties:

- Employers must cover full-time employees and their dependents. Remember, spouses are not included.
- Some employers are contemplating offering coverage to some full-time employees and excluding others. The rules specify that employers will meet the requirement to offer coverage to "substantially all" full-time employees if they offer coverage to 95% of their full-time employees and their dependents. If the employer fails to offer coverage to at least 95% of full-time employees, the penalty assessed would be $2,000 times **all** full-time employees less the first 30. This penalty will not apply for any month in which an employer offers coverage to all but 5% of its full-time employees (or five full-time employees, if greater). However, if any of the 5% of full-time employees not offered coverage secures subsidized coverage through the Exchange, the $3,000 penalty would apply for that individual.
- When calculating the penalty, the exclusion for the first 30 full-time employees applies to the IRS control group. However, penalties are assessed at the employer level. The 30-employee exclusion must be pro-rated across all members of the control group. The pro-rated number would depend on each employer's headcount compared to the control group as a whole. Employers offering full-time coverage will still be allotted their pro-rated employees. For example, if two of three related employers offer coverage, the entire 30-employee exclusion could not be applied to the one employer who does not offer coverage. In addition, if an IRS control group has more than 30 applicable large employer members, then each member employer would receive one employee exclusion. In this situation, the total employer exclusion may exceed 30 for the controlled group.

Following are more details on what it means to offer coverage:

- For new full-time employees, it means that coverage is effective for the full calendar month. If the coverage is offered mid-month, then it means that the employee is not offered coverage for that particular month. When determining penalties, the time spent during a new hire waiting period that meets the requirements of health care reform is not counted.

- If a terminated employee's coverage ends before the end of a month, then the employee is treated as having coverage for the full month.
- The employer must allow the employee to accept or elect coverage. Once the automatic enrollment rules take effect (no date yet), the employer must allow an employee to decline coverage that does not pass the affordability or benefits test.
- The employer does not need to cover the employee if the employee does not pay premiums on time. The employer can also terminate coverage if the employee does not pay the premium. The employee can re-elect coverage only at the next annual enrollment period. COBRA rules for grace periods and underpayments will apply to premium payments for coverage. For the purposes of penalty calculations, the employer will be treated as offering coverage for the entire plan year.

An employer can be assessed only one of the above penalties in any calendar month. In addition, the regulations do not define minimum essential coverage. Could an employer offer a low-value medical plan and still meet the requirement of offering minimum essential coverage? This point still needs to be clarified.

Penalties will be calculated monthly. The IRS is developing a process for communicating with employers about employees that enroll for subsidized coverage in the Exchange. These regulations refer to it as an IRS certification. These penalties are not deductible and will be payable upon "notice and demand." They will be collected in the same way as taxes. Large employers will be required to report specific information on employer-sponsored health plan coverage. Reporting for the 2014 calendar year will be due in January 2015. The IRS will publish additional regulations on this reporting requirement.

Coverage Affordability Safe Harbors

Employers can be penalized if the coverage they offer does not pass the affordability or benefits tests. The affordability test looks at the employee cost for single coverage. So long as the cost for single coverage does not exceed 9.5 percent of the employee's household income, the coverage is affordable for the employee and any eligible dependents. The Exchange will use household income to measure whether an employee is eligible for premium assistance. Employees considered eligible (even if coverage is not elected) for employer-sponsored coverage that passes the affordability and benefits tests will not receive premium assistance or cost-sharing reductions. The tests are based only on single coverage. If the employee can afford single coverage, the employee's entire family becomes ineligible for government assistance in the Exchange

Employers do not have access to an employee's household income. The IRS includes three safe harbors in these proposed regulations that employers can use to determine affordability.

Form W-2 safe harbor

Employers can determine affordability using the employee wages reported in Box 1 of the W-2. To use the W-2 safe harbor, employers must meet the following requirements:

- The employer must allow full-time employees and their dependents to enroll in minimum essential coverage under an employer-sponsored health plan.
- The required employee contribution for the self-only premium of the lowest-cost option providing at least a 60 percent benefit level cannot exceed 9.5 percent of the employee's W-2 wages (box 1).

An employer who meets these requirements will not be penalized if an employee can purchase subsidized coverage in the Exchange because his or her household income is less than the W-2 earnings.

Whether the safe harbor applies depends on the year-end 2014 employee W-2 wages as they compare to the required 2014 single coverage contributions. An employer could set contributions as a percentage of W-2 wages. In this case, so long as the percentage does not exceed 9.5 percent, the plan would pass the affordability test.

In some situations, W-2 earnings may not represent a full year of employment. Also, the contributions at year-end may not represent a full year of coverage if an employee joined the plan mid-year. In these situations, employers can determine affordability by adjusting wages and premiums. Multiply wages on the W-2 by a fraction. The numerator is the number of months the employee was covered and the denominator is the number of months of employment. The adjusted wage amount is compared to the premium the employee paid for months of coverage.

For example, an employee works eight months of a calendar year and was covered for five months of that time. The employee had W-2 wages of $24,000. Multiply this amount by 5/8 to arrive at the adjusted income of $15,000. This is the income used to determine whether the contributions for the five months of the year exceed 9.5 percent of income.

Rate of pay safe harbor

This safe harbor allows employers to determine in advance whether the health coverage is affordable. The employer would:

1. Take hourly pay for each hourly employee eligible to participate in the health plan at the beginning of the plan year.
2. Multiply that amount by 130 (the benchmark for full-time status).
3. Calculate affordability based on the monthly wages calculated in step 2. The employer would compare the monthly cost for single coverage in the lowest-cost plan offering at least a 60 percent benefit level.
4. For salaried employees, use the monthly salary.

Employers can use this safe harbor **only** if they do not reduce the employees' hourly or salaried wages during the year.

Federal Poverty Line (FPL) safe harbor

For this safe harbor, employer-sponsored health plan coverage is considered affordable if the employee's cost for single coverage does not exceed 9.5 percent of the FPL for a single person. For administrative convenience, employers can use the most recently published poverty guidelines as of the first day of the plan year.

These safe harbors are optional. Employers can use one or more of these safe harbors to determine affordability. However, they must use a single safe harbor consistently for any reasonable classification of employees.

Transitional Relief for Non-Calendar Year Plans

Although the law states that the "employer mandate" applies beginning January 1, 2014, the guidance allows a delayed effective date for some employers whose plan year does not begin on January 1.

In order to comply on the later plan year date, employers must meet *one* of the following two tests:

1. Was coverage *offered* to at least 33 percent of employees at the most recent open enrollment period before December 27, 2012? The regulations do not delineate a full-time employee measure. It appears this 33 percent requirement includes all employees, not just those working at or over 30 hours.

OR

2. Did the plan *cover* at least 25 percent of all employees? For this test, employers can use enrollment as of any date between October 31, 2012, and December 27, 2012.

The employer will not pay a penalty for the initial part of 2014 if all full-time employees are offered minimum essential coverage on the first day of the 2014 plan year. A penalty may apply after the first day of the 2014 plan year, if the employer plan fails the benefits or affordability tests and the employee purchases subsidized coverage in the Exchange.

Employers cannot change their plan years now in order to take advantage of this transitional relief for non-calendar year plans. The plan year must have been in place on December 27, 2012, for this delay to apply.

It appears that this transitional relief **will not apply** if an employer does not intend to cover full-time employees in 2014. If an employer will not offer coverage in 2014, penalties will apply as of January 1, 2014.

Employers with non-calendar year plans will still be responsible for the IRS reporting as part of the penalty process for the 2014 calendar year.

Section 125 Plan Years Beginning In 2013

Section 125 plans allow mid-year changes only for specific events and under specific circumstances. Not all employers have Section 125 plan years based on the calendar year. Employees that make annual elections under non-calendar year cafeteria plans will not have a mid-year event that would allow them to enroll for coverage in the Exchange. In addition, as of January 1, 2014, everyone must have health plan coverage or pay a tax penalty. Employees eligible for an employer-sponsored health plan may wish to enroll in that plan as of January 1, 2014 to avoid the penalty.

The IRS includes transitional relief from the Section 125 election rules. This transitional relief applies **only** to elections under a non-calendar year cafeteria plan and applies **only** to plan years that begin in 2013. Employers in this situation can amend their cafeteria plans to allow either or both of the following election changes:

1. An employee who elected a salary reduction for an accident or health plan for a plan year beginning in 2013 is allowed to prospectively revoke or change the election once during the year. This is allowed without regard to whether the employee had a qualified change in status.
2. An employee who failed to make a salary reduction election for an employer's cafeteria plan year beginning in 2013 is allowed to prospectively make an election once during the year. This is allowed without regard to whether the employee had a qualified change in status.

The employer must amend the plan document to allow these mid-year changes. The plan may be retroactively amended for these transitional rules. The amendment must be made by December 31, 2014, with an effective date retroactive to the first day of the 2013 plan year.

These rules apply only to employees' pre-tax deductions to pay for health coverage. If an employer intends to allow an employee to elect health plan coverage, or to modify health plan coverage mid-year, then the health plan (insurance carrier or stop loss vendor) must permit the change as well.

Concluding Thoughts

These regulations provide substantial detail on the "play or pay" provisions of health care reform in 2014. They also request a significant amount of stakeholder feedback on the proposed provisions.

The stakeholder comments will shape the final regulations. The IRS has been very accommodating on providing prospective effective dates as the regulations become final. Employers can rely on these rules when they plan for 2014.