

REFORM *Update*

Issue Ninety-Three

October 2014

October 3, 2014

On September 18, 2014, the Internal Revenue Service (IRS) released guidance for Section 125 plans. The guidance adds two new permitted mid-year election changes. These election changes address issues that would potentially challenge employers as they comply with the Affordable Care Act (ACA):

- Employers have new ways to determine full-time status. In some situations, an employee may earn coverage for a stability period. During that stability period, the employee could experience a reduction of work hours and move to part-time status. Under the employer mandate rules, an employee's reduction in work hours may not affect his or her eligibility for the health plan. Currently, the Section 125 rules allow a mid-year change if the reduction in work hours results in a loss of eligibility for the plan. While many employees may want to drop coverage because of reduced work hours, such a change is not allowed mid-year under the current rules.
- Employees enrolled for group medical coverage could not consider plans in the Health Insurance Marketplace if their employers did not have a calendar-year plan. The current Section 125 rules do not permit a mid-year election change because of Open Enrollment in the Marketplace.

The two new status changes permitted by the Section 125 rules will resolve these issues.

Background

Because Section 125 allows employees to pay for qualified plans on a pre-tax basis, employers that sponsor these plans must manage them in compliance with the Section 125 rules. One requirement is that employees must make a binding election for pre-tax benefits for the entire plan year. Mid-year changes are only permitted following specific events. Currently, an employee's reduction in hours is only considered a status change if it results in the employee's ineligibility for coverage. In addition, the current rules allow an employee to make a mid-year change following enrollment in another employer's group plan, but not if the employee enrolls for individual coverage (such as that available through the Marketplace).

Neither of these two current permitted change events addressed the situations described above. These events came about as a result of the ACA and are thus relatively new.

Two Newly Permitted Mid-Year Changes

A Section 125 plan may now allow two additional status changes:

1. Revocation Due to a Reduction in Hours that Does Not Cause an Employee to be Ineligible for Benefits

Two conditions must be met for an employee to revoke a benefits election after a reduction in hours without a corresponding loss of eligibility for coverage:

- 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 that would reduce the expected hours of service to less than 30 per week (which may or may not cause the employee to be ineligible for coverage); and

- The revocation of coverage by the employee (and any related individual) is allowed only if he or she intends to enroll in another plan providing Minimum Essential Coverage (MEC), effective no later than the first day of the second month following the month the coverage was revoked. A plan offering MEC may include employer coverage, Marketplace coverage and government coverage.

Please note that this mid-year change is permitted if the employee intends to secure other coverage. An employee could not necessarily drop coverage without securing other coverage.

2. Revocation Due to Enrollment in a Qualified Health Plan (QHP)

Two conditions must be met for an employee to revoke a benefits election for enrollment in a QHP:

- The employee must be eligible for Special Enrollment or Open Enrollment for QHPs available through the Marketplace; and
- The revocation relates to the intended enrollment of the employee (and other covered dependents) into a QHP through the Marketplace (also known as the Exchange) for new coverage that is effective no later than the last day of the employer-sponsored coverage.

Please note that this will primarily affect employers with non-calendar year plans. Again, the employee is permitted to drop coverage as long as he or she intends to enroll in Marketplace coverage.

In both of these scenarios, employers may rely upon an individual's reasonable representation of his or her intention to secure other coverage.

Concluding Thoughts

Employers with Section 125 plans are required to have a plan document that outlines plan provisions. The plan document has to state all mid-year status changes permitted under the plan. Therefore, if an employer wants to allow one or both of these new status changes, the plan must be amended to include them in the document.

Copyright McGraw Wentworth, a Marsh & McLennan Agency LLC company

Our publications are written and produced by McGraw Wentworth staff and are intended to inform our clients and friends on general information relating to employee benefit plans and related topics. They are based on general information at the time they are prepared. They should not be relied upon to provide either legal or tax advice. Before making a decision on whether or not to implement or participate in implementing any welfare, pension benefit, or other program, employers and others must consult with their benefits, tax and/or legal advisor for advice that is appropriate to their specific circumstances. This information cannot be used by any taxpayer to avoid tax penalties.