

On Sept. 18, 2014, the Internal Revenue Service (IRS) issued [Notice 2014-55](#), which expands the situations in which individuals can change their health coverage elections under an Internal Revenue Code (Code) Section 125 cafeteria plan.

Cafeteria Plan Elections

In most cases, a participant may not change his or her elections under a cafeteria plan during the period of coverage (usually the plan year). However, there are limited exceptions for certain changes in status, if permitted by the plan and if the election change is consistent with the change in status.

Notice 2014-55 addresses cafeteria plan elections in two specific situations related to the availability of coverage through a Health Insurance Exchange (or Marketplace). An employee may want to revoke an election under his or her employer's plan in order to purchase coverage through an Exchange if:

- > The employee's hours of service are reduced so that the employee is expected to average less than 30 hours of service per week, but the reduction does not affect eligibility for coverage under the employer's group health plan; or
- > The employee would like to cease coverage under the employer's group health plan and purchase coverage through an Exchange, without having a period of either duplicate coverage or no coverage.

In each of these situations, Notice 2014-55 permits a cafeteria plan to allow an employee to prospectively revoke his or her election for coverage under the employer's group health plan during a period of coverage, as long as the plan:

- > Is not a health FSA; and
- > Provides minimum essential coverage.

Certain conditions must be met for the change to be permitted. Also, an election to revoke coverage on a retroactive basis is not allowed.

Interaction with the Pay or Play Rules

Under the Affordable Care Act's employer shared responsibility (or "pay or play") rules, applicable large employers (ALEs) may have to pay penalties if they do not offer minimum essential coverage (MEC) to all full-time employees. Penalties are triggered if a full-time employee receives a premium tax credit for Exchange coverage.

ALEs may use the **look-back measurement method** to determine whether an employee is full-time or not full-time. Under the look-back measurement method, an employee who works, on average, at least 30 hours of service per week during a measurement period must be treated as full-time during a subsequent stability period, regardless of the employee's hours of service during the stability period.

Under this method, an employee could have a change in employment status (for example, a change from a full-time position to a part-time position) resulting in a reduction in hours that does not change the employee's status as a full-time employee, at least for some period of time.

Employers might offer coverage to employees for all periods that they qualify as full-time, to avoid any potential penalties under the pay or play rules. In these cases, the change in employment status would not result in a change in an employee's eligibility for the group health plan. Therefore, under the current regulations, the employee would not have been able to change his or her elections during the period of coverage.

Interaction with Exchange Enrollment

Under the current change in status regulations, a cafeteria plan may not allow an employee to revoke an election under the group health plan during a period of coverage solely to enroll in an Exchange plan.

This rule does not pose a problem for individuals enrolled in a group health plan with a calendar plan year. These employees may continue their coverage under the plan for the remainder of the employer's plan year, and then immediately begin coverage under a plan purchased through an Exchange.

However, the rule can cause issues for an individual in a non-calendar year plan, because the Exchange enrollment rules do not allow individuals to purchase coverage that would begin after the end of the non-calendar cafeteria plan year. Enrolling in a plan during the Exchange open enrollment would require these individuals to have either overlapping coverage or a period without any coverage.

Also, existing special enrollment rules for health plans do not permit employees to revoke a cafeteria plan election in order to enroll in Exchange coverage, even if they qualify for special enrollment in an Exchange. To expand access to Exchange coverage, Notice 2014-55 allows employees to revoke a cafeteria plan election to obtain coverage through an Exchange.

Conditions for Election Changes Due to Reduction in Hours of Service

A cafeteria plan may allow an employee to prospectively revoke an election of coverage under a group health plan if both of the following conditions are met:

- > An employee who was reasonably expected to average at least 30 hours of service per week has a change in employment 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
- > 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 MEC. The new coverage must be effective no later than the first day of the second month *after* the month in which the original coverage is revoked.

A cafeteria plan may rely on an employee's reasonable representation that he or she and related individuals have enrolled (or intend to enroll) in another plan that provides MEC within the required timeframe.

Conditions for Election Changes Due to Exchange Enrollment

A cafeteria plan may allow an employee to prospectively revoke an election of coverage under a group health plan if both of the following conditions are met:

- > The employee is eligible for special enrollment in an Exchange plan OR the employee wants to enroll in an Exchange plan during the Exchange's annual open enrollment period; and
- > 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 an Exchange plan. The Exchange coverage must be effective beginning no later than the day immediately following the last day of the original coverage that is revoked.

A cafeteria plan may rely on the reasonable representation of an employee who has an enrollment opportunity for an Exchange plan, that he or she and related individuals have enrolled (or intend to enroll) in an Exchange plan for new coverage that is effective within the required timeframe.

Plan Amendments Required

Allowing the changes permitted by Notice 2014-55 is optional. Employers do not have to permit these changes under their cafeteria plans. However, if the employer chooses to allow the new permitted election changes under Notice 2014-55, a cafeteria plan must be amended to provide for the election changes.

In general, the amendment must be adopted on or before the last day of the plan year in which the elections are allowed. It may be effective retroactively to the first day of that plan year, if:

- > The cafeteria plan operates in accordance with guidance under Notice 2014-55; and
- > The employer informs participants of the amendment.

However, a cafeteria plan may be amended to adopt the new permitted election changes for a plan year that begins in 2014 **at any time on or before the last day of the plan year that begins in 2015.**

Effective Date

The guidance contained in Notice 2014-55 is effective on Sept. 18, 2014. The IRS intends to amend the current cafeteria plan regulations to reflect the guidance in this notice. However, taxpayers may rely on the guidance in Notice 2014-55 until further guidance is issued.

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