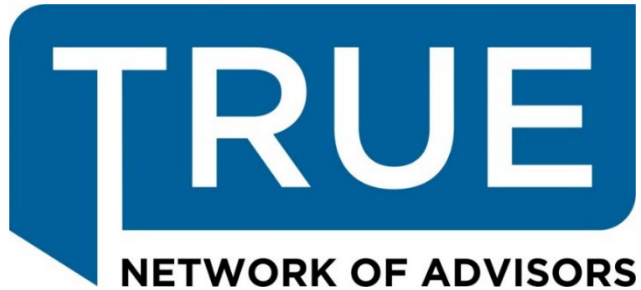


Cafeteria Plan, Open Enrollment, and Election Change Best Practices



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Code Section 125 – Basic Concepts

- ❖ A Cafeteria Plan gives employees a choice between non-taxable benefits (e.g., health coverage) and taxable benefits (e.g., cash)
 - Allows employees to pay premiums and contributions on a pre-tax basis
- ❖ Purpose
 - Avoiding the Constructive Receipt Doctrine
 - IRS: Cafeteria plan is the *exclusive* means by which an employer may offer a choice without the choice itself resulting in taxable income to the employee
- ❖ Tax Savings for the Employer and Employee

Code Section 125 – Basic Concepts

❖ Applicable Laws

➤ Internal Revenue Code

- §§ 105, 106, 125, 129, 213...

➤ ERISA?

- **No, but ERISA may apply to the underlying benefits, including the Health FSA**
- **Beware: Endorsement**

Code Section 125 – Basic Concepts

❖ 125 Cafeteria Plan Requirements

➤ Written Plan Document

- SPD?

➤ Only employees may participate

➤ Elections must be made in advance and can only be changed during the year in limited circumstances

Cafeteria Plan Eligibility Considerations

- ❖ Only employees (including any employees within a controlled group) may participate in the cafeteria plan
 - Former employees okay as long as plan is not maintained predominantly for them
 - Temporary employees?
- ❖ NOT Eligible:
 - Self-employed individuals
 - Partners in a partnership
 - More-than-2%-shareholders in a Subchapter S corporation
- ❖ *Special Issue: Independent Contractors*

What Benefits May Be Offered Under a Cafeteria Plan?

- ❖ **“Qualified Benefits,” including**
 - **Accident and Health Plans (including dental, vision, etc.)**
 - **Disability Benefit Plans**
 - **Dependent Care Assistance Programs**
 - **Health FSAs**
 - **Group Term Life Insurance**
 - **HSA Contributions**
 - **Adoption Assistance**
 - **401(k) Contributions**
- ❖ **Permitted Taxable Benefits, including Paid Time Off**

Substantiation Requirements & Guidance

- ❖ **IRS Chief Counsel Memorandum 202317020**
 - Re-enforces requirement that any and all reimbursements requested by a cafeteria plan participant must be fully substantiated.
- ❖ **The memo suggests that the following are NOT sufficient to fully substantiate claims:**
 - **Self-certification Method:** Cafeteria plans may not rely on a participant's own certification. Substantiations that lack independent certification are insufficient, even when such certifications provide details about the expense (including, e.g., the service or product, the date the expense was incurred, and the amount of the expense) or rely on debit card charge statements.
 - **Sampling Method:** All claims must be independently substantiated. It is not sufficient to require substantiation only of a random sampling of expense claims.

Substantiation Requirements & Guidance

- ❖ The memo suggests that the following are NOT sufficient to fully substantiate claims:
 - *De Minimis* – All claim amounts must be independently substantiated. Plans do not meet minimum requirements if they only require substantiation of claims above a certain threshold. In other words, there is no “de minimis” exception to the substantiation requirement.
 - Favored Providers – Claims from all sources must be independently substantiated. Plans may not exempt claims from certain providers from the substantiation requirement.
 - Anticipated DCAP Expenses – Only actual expenses may be reimbursed. It is not sufficient, therefore, for dependent care expenses, to rely only on an advance estimate of expenses without additional verification.

Substantiation Requirements & Guidance

❖ What *does* work?

- The plan only reimburses section 213(d) medical expenses that are substantiated by information from a third party that is independent of the employee and the employee's spouse and dependents.
- The information from the third party must describe the service or product, the date of service or sale, and the amount of the expense (employee's share)
 - For example, EOBs from an insurance company
- The plan also requires the employee to certify that any expense paid by the plan has not been reimbursed by insurance or otherwise and that the employee will not seek reimbursement from any other plan covering health benefits.

Open Enrollment

- ❖ **Employee Communication & Education**
- ❖ **Wellness Programs**
- ❖ **ACA Compliance**
 - **Timing for Measurement Period, Administrative Period, Stability Period**
 - **Keep record of declinations of coverage**
- ❖ **Documentation – Open Enrollment / EB Guide**
 - **“Plan Documents Control” Disclaimer**

Elections and Permitted Election Changes

- ❖ **Types of Elections**
 - **Affirmative**
 - **“Negative” – Automatic, Default, “Evergreen”**
- ❖ **Elections must generally be made before the beginning of coverage period**
 - **New hires may be allowed to make initial elections within 30 days retroactive to date of hire (all pre-tax amounts must still be taken from future pay)**
- ❖ **Must be irrevocable during the coverage period, unless a change is based on a permitted election change event**
- ❖ **Permitted election changes must be set forth in the plan document**

Mid-Year Election Changes

- ❖ Election change events for your plan must be provided for in 125 cafeteria plan document
 - Coordinate with ERISA plan document and underlying plan materials (e.g., health plan document)
- ❖ Only certain reasons/events allow for a change
- ❖ Two Part Test: (1) specified event must have occurred and (2) the requested change must be consistent with that event
- ❖ Required election change events:
 - FMLA Leaves of Absence
 - *Special Enrollment Rights*

Permitted Election Changes

Change in Status	COBRA Qualifying Event
Cost Changes <ul style="list-style-type: none">• Insignificant Cost Changes (Automatic)• Significant Cost Changes	Judgments, Decrees, or Orders
Significant Curtailment of Coverage	Entitlement to Medicare or Medicaid
Addition or Improvement of Benefit Package Option	FMLA Leave
Change in Coverage of Spouse or Dependent Under Another Employer Plan	Pre-tax HSA Contributions
Loss of Certain Other Health Coverage	Reduction of Hours
HIPAA Special Enrollment Rights	Exchange Enrollment

Mid-Year Election Changes

- ❖ **Change in Status Election Change Events:**
 - **Change in employee's legal marital status**
 - **Change in number of dependents**
 - **Change in employment status**
 - **Dependent satisfies (or ceases to satisfy) dependent eligibility requirements**
 - **Change in residence**
 - **Commencement or termination of adoption proceedings**

Mid-Year Election Changes

- ❖ **Change in (Coverage) Status Election Change Events:**
 - **Change in Coverage Under Other Employer Plan**
 - **Change in Coverage of Spouse or Dependent Under Another Employer Plan**
 - **Loss of Group Health Coverage Sponsored by Governmental or Educational Institution**

Mid-Year Election Changes

- ❖ **Change to Benefits, Cost**
 - **Automatic Increases/Decreases in Elective Contributions to Reflect Cost Changes**
 - **Significant Cost Changes (increase or decrease)**
 - **Significant Coverage Curtailment (With or Without Loss of Coverage)**
 - **Addition or Significant Improvement of Benefit Package Option**

Mid-Year Election Changes

- ❖ **HIPAA Special Enrollment Rights**
- ❖ **COBRA Qualifying Events**
- ❖ **Judgments, Decrees, or Orders**
- ❖ **Medicare or Medicaid Entitlement**
- ❖ **FMLA Leaves of Absence**
- ❖ **Pre-Tax HSA Contribution Changes**
- ❖ **ACA Election Change Events**
 - **Reduction of Hours**
 - **Exchange Enrollment**

