

VEHI Memo

CAFETERIA PLAN ACTION STEPS

Update from VEHI

July 1 Plan Years

May, 2014

IMPORTANT

The school must operate their benefit plans based on a single open enrollment period.

The school's open enrollment period should coincide with the July 1 plan year.

All employee elections must be irrevocable for the 12-month plan year unless there is a valid change in status event.

All requests by employees to make a change in their elections during the plan year must be permissible under the IRS rules and the governing plan document.

Failure to follow the Code Sec. 125 rules may result in the plan losing its tax-favored status and unfavorable tax consequences to both the school and its employees.

A cafeteria plan is a separate written plan that generally allows an employee the opportunity to pay for certain benefits with pre-tax dollars. A cafeteria plan gives employees the opportunity to choose among a menu of benefits consisting of cash (for example, regular pay) and certain nontaxable benefits (for example, health insurance). A cafeteria plan is not a typical employee benefit plan—instead of providing benefits directly to employees, it serves as a vehicle for employees to elect benefits under other plans and to finance their elections. Therefore, the advantage to the employee is generally twofold. First, the employee obtains a tax benefit. Second, the employee retains a choice in benefits.

In order to maintain tax-favored status, the IRS requires cafeteria plans to meet certain requirements (both in written form and in the operation of the plan). Significantly, under the Code Sec. 125 plan rules, a school that allows a pre-tax option may only allow one open enrollment period during the plan year. This enrollment period should correspond with a school's July 1 plan year.

In addition, schools may not allow an employee to change his or her elections unless the employee experiences **a valid change in status** recognized under the IRS rules. As such, a school may not allow a participant to change plans mid-year due to the plan's loss in grandfathered status because this is not permissible change under Code Sec. 125.

Information from this memo was taken from Code Sec. 125 and its governing regulations.

This memo is for general guidance purposes only—it is NOT legal advice.

If you have questions about the information in this document, please contact Laura Soares, Joseph Zimmerman and Mark Hage, your VEHI Trust Administrators: laura@vsbit.org, 223-5040 (ex. 208); joe@vsbit.org, 223-5040 (ex. 209) & mhage@vtnea.org, 223-6375 (ex. 2420).

Thank you.

Cafeteria Plan Action Steps

In order to comply with the Code Sec. 125 requirements, VEHI recommends the following action steps be taken immediately:

1. Confirm that your school allows the election of pre-tax benefits and has a written plan document that complies with IRS Code Section 125. The latter is not the only law governing benefits under a cafeteria plan; however, it is imperative to comply with Code Section 125 to preserve the plan's preferential tax treatment.
2. Confirm that your Cafeteria Plan operates on a fiscal year, July 1 to June 30.
3. Ensure the plan is operating using a single open enrollment period (with a July 1 effective date of change). Ensure that employee elections are irrevocable once the plan year begins. Each benefit must have a 12-month period of coverage following the open enrollment unless an event occurs that would allow a mid-year election change.
4. Only allow mid-year changes as defined by law.
5. Communicate the change to employees. If past practice has been different from this, employees should be notified about the change to a single 'open' enrollment opportunity as soon as reasonable. All plan documents and employee communications should also be changed to reflect the proper rules.
6. Consider utilizing the attached sample language on the last page to notify employees of this policy.
7. Do not rely upon BCBSVT for guidance on Code Sec. 125 rules. BCBSVT does not know if a school has a Code Section 125 plan, nor are they aware of the specific rules each plan has adopted. Schools must establish their own plan design in accordance with the IRS's rules.
8. Continue to work with VEHI. VEHI will modify its Benefit Guide to support schools in communicating about open enrollment.

Sample Employee Communication

Important: Revised **Open Enrollment Period** for Benefit Changes

For many years, employees with VEHI/BCBSVT health coverage have been permitted to voluntarily change benefit plans or levels of coverage without a change in the employee's family or employment status (status change) once every 12 months. The change became effective on either January 1 or July 1.

Recently, it came to VEHI's and the school's attention that in order to maintain the tax-advantaged status of our **Cafeteria Plan**, which allows you to elect benefits on a **pre-tax basis**, the school must limit the opportunity to change benefit plans without a legally sanctioned, status change to just once per year. This is a requirement of the IRS.

Because our district's Cafeteria Plan runs on a **fiscal year** cycle, July 1 to June 30, any change in benefits that is not the result of a change in life circumstances- see below- will take effect on the following **July 1**. January 1 will no longer be an option.

Therefore, effective immediately, the school's annual open enrollment period will take place **[fill in the dates]**, with coverage changes effective July 1, 2014. This means that changes in plan coverages, including changing plan options and/or adding or removing eligible dependents without a status change, may only occur during the open enrollment period.

Please Note: This new rule applies not only to VEHI health plans, but to all employee benefits offered by the district that are subject to our Cafeteria Plan, which includes **[list all]**.

Can an employee still change health or other benefit plans at any time during the year if there is a status change approved under law? Yes. The only exception to the new open enrollment rule above is if you have to make a plan or coverage change based on legally permitted changes in your life circumstances; for example, changes resulting from marriage, a birth or adoption, or a dependent's loss of coverage. In cases like these and certain others, under federal tax rules, you can make benefit changes consistent with the type of status change within **[fill in number of days from your Plan document]** days of the event and not pose a problem for the tax-advantaged status of your employer's Cafeteria Plan. For a complete listing of change-in-status events, please contact the business office.

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When does the one open enrollment period go into effect? As noted above, the change to one open enrollment period is effective immediately. Therefore, your next opportunity to enroll in or change your elections for any employee benefit offered by the district is this spring and will be effective July 1, 2014 unless you or an eligible dependent experience a recognized status change.

Please contact the business office if you have any questions or concerns about this change and its impact on you.