



# COMPLIANCE SNAPSHOT

## Section 125 Election Rules

Under a Section 125 plan, or cafeteria plan, benefits can be funded in a variety of ways. The most common way is for employees to reduce their salaries on a pre-tax basis to pay for benefits via “salary reduction agreements” with their employers. Only participants can make elections under a cafeteria plan, even though the underlying benefits (e.g., health insurance) may cover other individuals (e.g., dependents). The following rules apply to these elections.

### Prospective Only

Participant elections under a Section 125 cafeteria plan must be made **before the first day of the plan year or the date taxable benefits would currently be available**, whichever comes first. Typically, employees make their elections each year during an annual open enrollment period. There are only two exceptions to the general rule that Section 125 elections must be made on a prospective (not retroactive) basis:

- **Limited exception for new hires**—Elections that new employees make within 30 days after their hire date can be effective on a retroactive basis. Elections made during this enrollment window can be effective as of the employee’s date of hire.
- **HIPAA special enrollment**—Elections under a Section 125 plan may be retroactive to correspond with HIPAA special enrollment rights when an employee acquires a new dependent through birth, adoption or placement for adoption.

### Irrevocable

Participant elections generally must be **irrevocable until the beginning of the next plan year**. This means participants ordinarily cannot make changes to their cafeteria plan elections during a plan year. Employers do not have to permit any exceptions to the election irrevocability rule for cafeteria plans. However, IRS regulations permit employers to design their cafeteria plans to allow employees to change their elections during the plan year if certain conditions are met.

## Types of Elections

- ☑ **Affirmative elections (most common):** Employees complete a written agreement authorizing their cafeteria plan elections.
- ☑ **Automatic elections:** Employees who do not want to participate must complete a waiver. Employers must provide adequate notice to employees and confirm the default elections do not violate state tax withholding laws.
- ☑ **Rolling elections:** Current participants’ elections continue to the next plan year unless the employee files an election not to participate.

## Plan Document Procedures

- ☑ A cafeteria plan must specify the procedures that govern participants’ elections under the plan, including when elections may be made and the periods for which they are effective.

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