

“Change in family status” rules revised by IRS

Changes become effective January 1, 2002

The IRS recently released regulations on when participants can change their employee benefits elections under a pre-tax deduction plan. These regulations replace the “change in family status” rules for health plans (medical and dental) and group-term life insurance. These regulations will now be referred to as “Changes in Status” and can be grouped into three categories:

1. Change in Status Events
2. Significant Cost or Coverage Changes
3. Other Events

Please examine the changes described below to determine how they might apply to your benefits options.

“Changes in Status” Events

The following five categories of events are listed in the regulations as being “changes in status:”

- Legal marital status changes, such as marriage, divorce, separation, or the death of a spouse.
- A change in the number of dependents such as birth, death or adoption.
- Changes in employment status of the employee, or of the employee’s spouse or dependents. This includes the beginning or ending of employment, new or different work hours, a change due to a strike, a change from full-time to part-time status or visa versa, the beginning or end of an unpaid leave of absence, or a change in work site. Also, if employment status affects eligibility under the plan, that is deemed to be an employment status change (e.g., salaried to hourly).
- A dependent becoming eligible or ceasing to be eligible for coverage due to age, student status, or any similar circumstance.
- A change in the residence of the participant, or the participant’s spouse or dependent.

Medical/dental coverage changes must satisfy a consistency rule. That is, a change in medical/dental coverage level or election change must be on account of and correspond with a change in status that affects eligibility for coverage under the medical/dental plan. This includes a change in status that results in an increase or decrease in the number of an employee’s family members or dependents who may benefit from coverage.

“Significant Cost or Coverage” Changes

These rules permit election changes to be made as a result of significant changes in cost or coverage. The new regulations do not say specifically what a “significant cost” change is. With respect to cost changes, Medical Flexible Spending accounts cannot be changed. However, changes can be made with regard to Dependent Care accounts.

Significant Cost Changes

If the cost of a benefits plan increases or decreases during the plan year and employees are required to make a corresponding change in their payment for the coverage, an employee may be permitted to make a corresponding election change due to the increase or decrease. These elections may be made regardless of whether the cost increase or decrease change results from an action taken by the employee or employer. However, for Dependent Care accounts, the dependent care provider cannot be a relative of the employee. In other words, if a relative is the caregiver and increases or decreases the rate for dependent care, the employee cannot make changes to his/her dependent care account.

Coverage Changes

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- An election change may be permitted where there is a significant curtailment of coverage that is not a total loss of coverage. For example, if there is a significant increase in the deductible, copay, or out-of-pocket limit for the health/dental plan by the employer, the employee participating in the plan and receiving coverage may revoke this election and elect another coverage option providing similar coverage.
- If an employee or the employee’s spouse or dependent has a significant curtailment which results in loss of coverage, the plan may permit that employee to end his or her election and elect either to receive coverage under another plan or to drop coverage if no similar benefit package option is available. A loss of coverage is defined as a complete loss of coverage under the benefit package. For example, if a spouse’s company no longer offers health/dental insurance, the employee may add or increase his/her coverage. If an HMO ceases to be available in the area where the individual resides or is losing all coverage by reason of lifetime or annual limitation, a change in election can be made. Also, if benefits are reduced for a specific type of medical condition or treatment which the employee or the employee’s spouse or dependent is currently in a course of treatment, or any other similar fundamental loss of coverage, it may be treated as a loss of coverage.
- If a plan adds a new benefit package or other coverage option, or an existing benefit is significantly improved during the plan year, employees may be permitted to revoke their election and make a new election of new and/or improved benefit package, even if they had refused coverage previously.
- The employee may make benefit package changes, including dropping coverage, if it is on account of open enrollment and coverage periods different from their own. For example, the SSU enrollment period is usually during November with an effective date of January 1 of the following year. If the employee’s spouse’s open enrollment period is in May, and takes effect in July of the same year, and the plan is better suited for their family needs, the SSU employee can drop his/her coverage effective with the month prior to the spouse’s coverage beginning.

Other events

A pre-tax benefit plan may permit an employee to make a mid-year election change for certain other events as described below:

- Plan election changes may be made consistent with an employee, spouse or dependent becoming, or ceasing to be, eligible for Medicare or Medicaid.
- A judgment, decree, or order that results from a divorce, legal separation, annulment, or change in legal custody may require a change in health/dental coverage for an employee’s child or dependent foster child.
- An employee taking leave under the Family and Medical Leave Act may revoke an existing election related to health coverage and make another election for the remaining portion of the period of coverage as provided under the FMLA rules.