



COMPLIANCE ALERT

IRS OFFERS INCREASED FLEXIBILITY FOR CAFETERIA PLANS AND FSAS IN RESPONSE TO COVID-19

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The Internal Revenue Service (IRS) has issued guidance to make temporary changes to Section 125 cafeteria plans, with the goal of providing increased flexibility in the midst of the coronavirus pandemic. IRS has added to the situations in which a cafeteria plan may allow employees to make mid-year election changes (including an initial election) and allowed more flexibility with respect to health FSAs and dependent care assistance programs.

Specifically, the IRS is offering extra flexibility to participants by:

- Extending the ability of participants to make mid-year elections for health coverage, health FSAs and dependent care assistance programs, allowing them to respond to changes in needs as a result of the COVID-19 pandemic; and
- Extending the claims period for participants to apply unused amounts remaining in a health FSA or dependent care assistance program for expenses incurred for those same qualified benefits through December 31, 2020.

The IRS also increased the limit for unused health FSA carryover amounts from \$500 to \$550.

The increased flexibility provisions and carryover amounts are both available through December 31, 2020.

Increased flexibility for mid-year election changes

The Notice provides temporary flexibility for cafeteria plans to permit employees to make certain prospective mid-year election changes for employer-sponsored health coverage, health FSAs and dependent care assistance programs during calendar year 2020.

Specifically, an employer, in its discretion, may amend its cafeteria plan to allow employees to:

1. Make a new election for employer-sponsored health coverage on a prospective basis, if the employee initially declined to elect coverage;

2. Revoke an existing election for employer-sponsored health coverage and make a new election to enroll in different health care coverage sponsored by the same employer on a prospective basis (including changing enrollment from self-only coverage to family coverage);
3. Revoke an existing election for employer-sponsored health coverage on a prospective basis, provided that the employee attests in writing that the employee is enrolled, or immediately will enroll, in other health coverage not sponsored by the employer;
4. Revoke an election, make a new election, or decrease or increase an existing election regarding a health FSA on a prospective basis; and
5. Revoke an election, make a new election, or decrease or increase an existing election regarding a dependent care FSA on a prospective basis.

An employer utilizing this relief is not required to allow unlimited election changes but may, in its discretion, determine the extent to which such election changes are permitted and applied, provided that any permitted election changes are applied on a prospective basis only, and the changes to the plan's election requirements do not result in failure to comply with nondiscrimination rules.

With respect to mid-year election changes for employer-sponsored coverage, the relief applies to both self-insured and fully-insured plans. With respect to health FSAs, the relief applies to all health FSAs, including limited purpose FSAs designed for compatibility with HSAs.

Extended claims period for FSAs and dependent care assistance programs

The Notice also provides flexibility for a cafeteria plan to provide an extended period to apply unused amounts remaining in a



health FSA or dependent care assistance program to pay or reimburse medical care expenses or dependent care expenses.

Specifically, an employer may, in its discretion, amend its cafeteria plan to permit employees to apply unused amounts remaining in a health FSA or dependent care FSA until the end of a grace period ending in 2020 or a plan year ending in 2020 to pay or reimburse expenses incurred through December 31, 2020.

The extension of time for incurring claims is available to FSAs with a grace period and those with a carryover, but does not change the existing rule that an FSA cannot have both features.

Example

Assume an employer provides a health FSA with a July 1st plan year that allows a \$500 carryover for the 2019 plan year (July 1, 2019 – June 30, 2020). The employer amends the plan to adopt a \$550 carryover beginning with the 2020 plan year, and also amends the plan to adopt the temporary extended period for incurring claims, allowing for claims incurred prior to January 1, 2021 to be paid with respect to amounts from the 2019 plan year.

Jane has a remaining balance in her health FSA for the 2019 plan year of \$2,000 on June 30, 2020 because a scheduled non-emergency procedure was postponed. For the 2020 plan year beginning July 1, 2020, she elects to contribute \$2,000 to her FSA. She is able to reschedule the procedure before December 31, 2020 and incurs \$1,900 in medical expenses between July 1, 2020 and December 31, 2020. Jane can be reimbursed from her FSA \$1,900 of the \$2,000 she had left at the end of the 2019 plan year. Under the plan terms that provide for a carryover, she is allowed to use the remaining \$100 until June 30, 2021 to reimburse claims incurred during the 2020 plan year. She can be reimbursed up to \$2,100 (\$2,000 contributed for the 2020 plan year, plus \$100 carried over from the 2019 plan year) for medical care expenses incurred between January 1, 2021 and June 31, 2021. In addition, she can carry over to the plan year beginning July 1, 2021 up to \$550 of any remaining portion of that \$2,100. Because the plan has a carryover provision, a grace period is not available for the plan year ending June 30, 2021.

The extension of the period for incurring claims that may be reimbursed by the health FSA is an extension of coverage by a health plan that is not an HDHP for purposes of determining whether an individual qualifies to make contributions to an HSA. Therefore, an individual who had unused amounts remaining at the end of a plan year or grace period ending in 2020 and who is allowed an extended period to incur expenses will not be eligible to contribute to an HSA during the extended period (except in the case of an HSA-compatible FSA).

Plan amendments required

An employer that wishes to amend its cafeteria plan to provide for mid-year election changes for employer-sponsored health coverage, health FSAs, or dependent care assistance programs in a manner consistent with the new increased flexibility rules must adopt a plan amendment. In addition, an employer that decides to amend its health FSA to provide for an increase in the carryover amount must adopt a plan amendment.

Amendments for the 2020 plan year must be adopted by December 31, 2021 and may be effective retroactively to January 1, 2020, provided that the employer informs all eligible employees of the changes to the plan.

As always, please contact your Hilb Group Benefits Advisor with any questions.