Informational Bulletin

IRS Issues COVID-19 Related Relief for Section 125 Cafeteria Plans

May 2020

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SUMMARY:

On May 12, 2020, the Internal Revenue Service ("IRS") released Notices 2020-29 and 2020-33, collectively providing guidance related to cafeteria plan elections, health flexible spending accounts ("Health FSAs"), and dependent care assistance programs ("DCAPs"). This Informational Bulletin contains a summary of the following key points:

- Notice 2020-29 permits employers to adopt temporary plan provisions allowing for:
  - Mid-year election changes for health plans, health flexible spending accounts (Health FSAs), and dependent care assistance programs (DCAPs); and
  - Use of unused Health FSA and/or DCAP amounts remaining at the end of a grace period or plan year ending in 2020.
- Notice 2020-29 also clarifies that high deductible health plans providing coverage for testing and treatment for COVID-19, as well as telehealth, applies retroactively to January 1, 2020.
- Notice 2020-33 increases the Health FSA carryover limit from $500 to $550 for 2021.

Cafeteria Plan Elections

In general, benefit elections involving qualified benefits under a Section 125 cafeteria plan must be made prior to the first day of the plan year. Additionally, such benefit elections must be irrevocable in the absence of circumstances such as a qualified life event or change in cost of coverage. However, due to unexpected changes to medical and childcare expenses resulting from COVID-19, the IRS relaxed some of the standard requirements applicable to mid-year changes.

Pursuant to Notice 2020-29, an employer may, at its discretion, amend its plan to allow for any or all of the following changes during the 2020 calendar year:

1. An employee who did not enroll in health plan coverage may enroll themselves and any eligible dependents on a prospective basis.
2. An employee who enrolled in coverage under the health plan may elect to enroll in **a** different health plan option sponsored by the same employer on a prospective basis (this includes changing from self-only to family coverage).
3. An employee who enrolled in coverage may revoke the election on a prospective basis provided that the

employee attests* in writing that they are enrolled, or will immediately become enrolled, in other group health plan coverage not sponsored by the employer.

4. An employee may revoke a Health FSA election, make a new Health FSA election, or may increase or decrease an election for the remainder of the year on a prospective basis.
5. An employee may revoke a DCAP election, make a new DCAP election, or may increase or decrease an election for the remainder of the year on a prospective basis.

* The Notice includes an example of an acceptable attestation the employer may use. The employer may rely upon the employee's written attestation provided the employer does not have actual knowledge that the attestation is not truthful.

Health FSA and DCAP

Under standard Section 125 regulations, amounts remaining in a Health FSA or DCAP at the end of a plan year, including any grace period, are forfeited under the "Use-It-Or-Lose-It" rule. Again, due to the unforeseen nature of the current national health emergency, the IRS is temporarily relaxing this rule.

For Health FSA and DCAP plan years and plan year grace periods ending in 2020, the plan may permit any unused amounts remaining in a Health FSA or DCAP to be used to pay or reimburse qualifying expenses incurred no later than December 31, 2020. This guidance includes 2019 plan years ending or 2020, or plans whose grace period ends in 2020.

Though Health FSAs are not permitted to utilize both a grace period and a carryover provision (under which unused amounts up to the carryover limit rollover to the following plan year), plans containing a carryover provision are permitted to implement the extended claim filing limit provided for under this Notice.

Further, under separate guidance in Notice 2020-33, the IRS increased the Health FSA carryover limit from $500 to $550 for 2020. Employer**s** wishing to implement the carryover provision for the first time are permitted to change the plan prospectively provided an amendment is completed no later than December 31, 2021 (though eligible employees must be informed of the change).

Additional Considerations

The IRS acknowledged that permitting some of the mid-year changes made allowable under Notice 2020-29 creates a high likelihood of adverse selection. To manage this risk, the Notice allows an employer to take the following steps:

- Limit election changes to circumstances in which an employee's coverage will be increase or improved as a result of the election change (e.g., switching from self-only to family coverage or from a low plan option to a high plan option)
- Set a time limit on when employees may make changes pursuant to the Notice
- Limit employees' ability to revoke or reduce Health FSA and DCAP elections to amounts no less than the amount already reimbursed

Lastly, the IRS cautioned employers to remain aware of Section 125 nondiscrimination rules as well as other plan sponsor notice obligations under ERISA (i.e., summary plan description and summary of material modification requirements).

Plan Amendments

Though employers are normally required to execute cafeteria plan amendments before any change can take effect, the IRS provided additional time to complete necessary plan amendments due to the unusual circumstances. Employers who implement some or all of the permitted changes must adopt a plan amendment no later than December 31, 2021, but the changes may be retroactive to January 1, 2020. In the meantime, employers are required to inform all employees eligible to participate in the cafeteria plan of the changes.

Clarification of Prior Guidance on Telemedicine, COVID-19 Testing and Treatment, and HSA Eligibility

Pursuant to previously issued IRS Notice 2020-15 and the Coronavirus Aid, Relief, and Economic Security Act ("CARES Act"), individuals remain eligible to contribute to a health savings account (HSA) if the high deductible health plan under which they are covered provides coverage for testing and treatment for COVID-19 and/or telehealth services prior to satisfaction of the minimum high deductible health plan deductible. In Notice 2020-29, the IRS clarified that this relief applies retroactively to January 1, 2020.