



## Employee Benefits News

May 15, 2020

# Now on the COVID-19 Menu: Temporary Flexibility for Cafeteria Plans

With the 2019 novel coronavirus (“COVID-19”) national health emergency continuing, employers are continuing to try to find ways to help their employees. In response to requests from employers, the Internal Revenue Service (“IRS”) has issued guidance, in the form of Notices,<sup>1</sup> to temporarily allow greater flexibility in midyear coverage and election changes under group health plans and flexible spending accounts (“FSA”). This guidance also provides some clarification with respect to (i) high deductible health plans (“HDHPs”) and COVID-19-related expenses and (ii) telehealth benefits.

### Midyear Elections under Cafeteria Plans and Flexible Spending Accounts in 2020

Cafeteria plans and FSAs can be amended to permit eligible employees to make the following midyear changes during calendar year 2020, and no particular reason for making any such change is required:

- **Election Changes Related to Group Health Coverage:**
  - Eligible employees can be allowed to make a new election for coverage under the employer’s group health plan on a prospective basis, if the employee initially declined that coverage.
  - If the employer group health plan offers different health coverage options, eligible employees can be allowed to revoke an existing election and make a new election to enroll in a different health coverage option sponsored by the same employer on a prospective basis.
  - Eligible employees can be allowed to revoke existing coverage under the employer’s group health plan on a prospective basis, provided the employee attests in writing that the employee is enrolled, or immediately will enroll, in other comprehensive health coverage not sponsored by the employer.
    - ✓ Reliance on Employee’s Attestation. The employer may rely on this attestation unless the employer has actual knowledge that the employee is not or will not be enrolling in other coverage. Helpfully, in [Notice 2020-29](#), the IRS provides an example of an acceptable written attestation. *Brownstein Comment:* It would be helpful if the IRS were to provide some examples of situations where an employer would be considered to have actual knowledge (other than the example of an employee saying aloud they aren’t going to buy other coverage).
- **Election Changes Related to Health and Dependent Care FSA Participation:** Eligible employees can revoke an election, make a new election, or decrease or increase an existing election applicable to a health FSA and/or dependent care FSA on a prospective basis. The ability to make this change applies to all health FSAs, including limited purpose health FSAs. The IRS notes in [Notice 2020-33](#) that, although only future salary may be reduced under the revised election, amounts contributed to the health FSA after the revised election may be used for any medical care expense incurred during the first plan year that begins on or after Jan. 1, 2020.

<sup>1</sup> See, IRS [Notice 2020-29](#), COVID-19 Guidance Under § 125 Cafeteria Plans and Related to High Deductible Health Plans, and IRS [Notice 2020-33](#), Section 125 Cafeteria Plans - Modification of Permissive Carryover Rule for Health Flexible Spending Arrangements and Clarification Regarding Reimbursements of Premiums by Individual Coverage Health Reimbursement Arrangements.

- **Other Considerations:**
  - Employer Discretion. Subject to the applicable nondiscrimination rules, an employer may exercise its discretion in determining which midyear election changes will be made available during 2020, whether there will be any limitations on the frequency with which employees may make these prospective midyear changes during 2020, and the extent of those elections. For example:
    - ✓ An employer may offer a one-time election to be effective July 1, or allow elections to be made once each calendar quarter or after some stated number of days.
    - ✓ An employer may limit group health coverage elections only to provide for broader coverage, for example, amend the plan to only allow for election changes from single to family coverage, or from the plan's low option to its high option.
    - ✓ The IRS specifically noted that an employer may consider adverse selection when deciding whether and to what extent to make this midyear election available.
  - Limitations to Recover FSA Reimbursements Already Made. With respect to FSA election changes, the employer can limit midyear election changes to amounts no less than amounts already reimbursed.
  - Guidance Applies Retroactively. Helpfully, the IRS extends reliance on this guidance retroactively to Jan. 1, 2020, in an acknowledgment that some employers already have permitted these types of midyear elections prior to the issuance of IRS guidance allowing for these kinds of midyear elections. **Brownstein Comment:** Employers that have done so should review their plan amendments and procedures to make sure they are consistent with this guidance. If the prior amendment and procedures are not consistent, the employer should consider changes to confirm to this guidance.
  - Amendment Required. Cafeteria and FSA plans wishing to implement any of the midyear election changes discussed above must be properly amended. In accordance with Notice 2020-29, any such amendment for the 2020 plan year must be adopted on or before Dec. 31, 2021, and, as indicated above, can be retroactive to Jan. 1, 2020, provided that the plan previously was administered consistent with the amendment and all eligible employees were informed of the plan changes.

## Additional Guidance

- **Extension of Period to Use FSA Grace Period and Carryover Amounts.** Health FSAs and dependent care FSAs can be amended to allow employees to apply unused amounts remaining in a health FSA or a dependent care FSA as of the end of a grace period or carryover period ending in 2020 or a plan year ending in 2020 to pay or reimburse expenses incurred for the same qualified benefit through Dec. 31, 2020. This extension applies whether the FSA utilizes a grace period or a carryover provision—but the rule that a health FSA cannot have a grace period *and* a carryover provision remains in effect.<sup>2</sup>
  - Impact on HSA Eligibility. It is important to note that an employer's decision to implement this discretionary extension to year-end 2020 is viewed by the IRS as an extension of coverage by a health plan that is not an HDHP for purposes of determining whether an eligible individual qualifies to make contributions to an HSA (except in the case of an HSA-compatible health FSA, such as a limited purpose health FSA). Therefore, an employee who is eligible for reimbursements from a health FSA during this extended period of time would *not* be eligible to make contributions to an HSA (except in the case of an HSA-compatible health FSA, such as a limited purpose health FSA). **Brownstein Comment:** It is unclear whether an employee is ineligible to make HSA contributions where the employer amends the health FSA plan to add the carryover extension but the employee who is covered under an HDHP option in 2020

<sup>2</sup> IRS Notice 2020-29 citing IRS [Notice 2013-71](#), Modification of "Use-or-Lose" Rule For Health Flexible Spending Arrangements (FSAs) and Clarification Regarding 2013-2014 Non-Calendar Year Salary Reduction Elections Under § 125 Cafeteria Plans.

did not participate in the health FSA in 2020 or does not have a carryover balance from 2019. Employers need to make certain they understand the complexities that may arise if they implement this extension.

- **Increase in Health FSA Carryover Amount.** In [Notice 2020-33](#), the IRS has increased the maximum carryover amount under a health FSA to be an amount equal to 20% of the maximum salary reduction contribution allowed for that year, subject to some rounding rules. As a result, the maximum unused amount from a plan year starting in 2020 allowed to be carried over to the immediately following plan year beginning in 2021 is \$550.
- **Amendment Required.** Health FSAs wishing to extend the carryover access period and/or implement the larger carryover amount must be amended. With respect to the larger carryover amount, the amendment can provide for the specific dollar amount or reflect the formulaic increase, so that future amendments are not needed as the maximum carryover amount is increased in later years. A plan that will utilize the increased carryover amount for the 2020 plan year must be amended no later than Dec. 31, 2021, and the amendment may be retroactive to Jan. 1, 2020, provided all employees eligible to participate in the plan are notified of the changes to the health FSA. A plan that will utilize the increased carryover amount for a plan year that begins in 2021 must be amended by the last day of that plan's 2021 plan year.
- **Timing of Reimbursements from Health Plans.** In an effort to address practical difficulties related to the general rule that only payment or reimbursement for medical care expenses incurred by an employee during the plan year may be excluded from that year's income and wages under Code Secs. 105 and 106 and provide a rule of administrative convenience, Notice 2020-33 provides that, notwithstanding the normally applicable rules under Code Secs. 105, 106 and 125 as to when expenses are incurred, a health plan is permitted to treat an expense for a premium for health insurance coverage as incurred on (1) the first day of each month of coverage on a pro rata basis, (2) the first day of the period of coverage, or (3) the date the premium is paid. Thus, for example, an individual coverage HRA with a calendar-year plan year may immediately reimburse a substantiated premium for health insurance coverage that begins on Jan. 1 of that plan year, even if the covered individual paid the premium for the coverage prior to the first day of the plan year. *Brownstein Comment:* For this purpose, a health plan includes including a premium-reimbursement plan in a cafeteria plan or an individual coverage HRA.

### Clarification of Prior Guidance Regarding HDHPs and COVID-19-Related Treatment

Our [March 12, 2020, alert](#) ("Health Plan Coverage of Coronavirus Testing and Treatment") discussed IRS Notice 2020-15, which confirms that (i) an HDHP can fully pay for all testing and medical treatment related to COVID-19 before the otherwise applicable annual minimum deductible has been met and (ii) individuals participating in such HDHPs continue to be eligible to make HSA contributions. Now, in [Notice 2020-29](#), the IRS clarifies that:

- The relief provided in Notice 2020-15 regarding HDHPs and expenses related to testing for and treatment of COVID-19 applies with respect to reimbursements of expenses incurred on or after Jan. 1, 2020.
- The panel of diagnostic testing for influenza A & B, norovirus and other coronaviruses, and respiratory syncytial virus (RSV) and any items or services required to be covered with zero cost sharing under section 6001 of the Families First Coronavirus Response Act (P.L. 116-127, 134 Stat. 178 (March 18, 2020)), as amended by the CARES Act, are part of testing and treatment for COVID-19 for purposes of Notice 2020-15.
- An otherwise eligible individual with HDHP coverage may receive coverage for telehealth and other remote care services outside the HDHP, before satisfying the deductible of the HDHP, and still contribute to an HSA. This exception applies with respect to these services if provided on or after Jan. 1, 2020, with respect to plan years beginning on or before Dec. 31, 2021.
  - The IRS provides the following example to illustrate this clarification: An otherwise eligible individual with coverage under an HDHP who, beginning Feb. 15, 2020, also received coverage for telehealth and other remote care services under an arrangement that is not an HDHP and before satisfying the deductible for the HDHP will not be disqualified from contributing to an HSA during 2020.

## Required and Recommended Actions

If you are an employer that wants to make the midyear cafeteria plan election flexibility available to employees or the additional FSA changes, you should take the following actions (in addition to the actions described above):

- **Determine the Plan Changes Appropriate to Your Workforce.** An employer should consider what are the appropriate changes permitted under the Notices to implement for its workforce, and when they should become effective: midyear election flexibility, extension of the availability of the carryover amount, increase in the maximum carryover amount, and HDHP coverage of COVID-19-related treatment and telehealth. Also consider what administrative processes will be necessary or desirable to implement any of these changes.
  - **If Fully Insured, Check With Insurer.** If your group health plan is fully insured, we recommend that you communicate with your insurer the desire to make the midyear election changes available to employees to make sure the insurer will process and pay claims incurred as a result of these election changes. Failure to do so could result in the employer being responsible for paying for claims incurred as a result of allowing these midyear election changes.
  - **Work With Vendors.** If your cafeteria plan is administered by a third-party administrator (“TPA”), you can expect to hear from the TPA about the ability to make these changes. We expect the TPA also will ask you to complete an election form to indicate which of the flexible options you want to implement. While this election would serve to establish intent and document administrative practice, an official plan amendment still is required to be properly adopted.
- **Timely Adopt Plan Amendments.** Employers have until Dec. 31, 2021, to adopt amendments to their cafeteria plans to reflect the decisions to implement the midyear election provisions in 2020 and/or the FSA claim extension in 2020 and/or implement the increased carryover limit in 2020. This amendment can be effective retroactively to Jan. 1, 2020. Make sure that any plan amendments that are adopted retroactively are consistent with prior plan administration.
- **Notify Employees.** If you amend your plan(s) for any of these permitted changes, be certain to notify employees of the changes, as well as any rules and procedures that they must follow.
- **Keep Alert.** Since it is unclear when the COVID-19 national health emergency may end, it is important to keep alert for any other benefits-related guidance that the IRS (or other agencies) may issue.

## How We Can Help

Please contact one of us or your regular Brownstein attorney for answers to your questions about how this new guidance affects cafeteria plan administration and for assistance in plan amendments and developing related communications to your employees.

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