

A Tale of Two IRS Notices

IRS Provides Relief for Mid-Year Election Changes and Flexible Spending Accounts

On May 12, 2020, the IRS issued two notices (collectively referred to as the “Notices”):

- [IRS Notice 2020-29](#) gives employers additional flexibility to allow mid-year benefit election changes, permits employers to provide flexible spending account (FSA) participants an extended grace period to use their 2019 FSA plan year funds, and addresses some previous loose ends.
- [IRS Notice 2020-33](#) increases the carryover limit for unused health care FSA (HCFSA) funds and indexes it for inflation.

When, Exactly?

The relief and other guidance provided in the Notices were effective May 12, 2020, with certain provisions available retroactive to January 1, 2020. Employers wanting to implement any of the permitted relief will need to amend their plans by **December 31, 2021**. Employers must inform eligible employees of any changes. Although [some plan notification requirements have been relaxed](#) during the COVID-19 pandemic, employers should communicate any changes as soon as it is practical to do so.

IRS Relaxes 2020 Mid-Year Election Change Rules

In general, Internal Revenue Code Section 125 cafeteria plans may only allow pre-tax mid-year election changes if an employee experiences a qualifying life event (QLE) permitted under the cafeteria plan rules. IRS Notice 2020-29 allows what we will refer to as a new “amnesty QLE” in response to the COVID-19 pandemic. During the 2020 calendar year, a cafeteria plan may permit employees to make changes to pre-tax elections for health coverage, HCFsAs, and dependent care FSAs (DCFsAs) as an amnesty QLE when no traditional QLE exists.¹

A Flexible Blank Slate

Employers have enormous flexibility to adopt and tailor amnesty QLEs to meet their needs, including:

- **Yes or no** – An employer can implement an amnesty QLE, but it is not required to do so.
- **Which benefits are affected** – An employer has the freedom to choose which benefits are subject to the amnesty QLE. For example, an employer may limit the amnesty QLE to just medical coverage, medical coverage and FSAs, just FSAs, etc.

¹ The amnesty QLE does not apply to other pre-tax benefits offered through the cafeteria plan. Remember that no QLE is required to change an HSA election

- **Permitted election changes** – An employer has the freedom to choose which types of benefit election changes to permit. For example, an employer may:
 - Permit any election change;
 - Permit any enrollment or drop in coverage but not changes between plan options;
 - Only permit enrollment in the lowest cost medical plan; or
 - Only permit a drop of FSA coverage.

An employer should have the flexibility to limit which employee groups are eligible for the amnesty QLE provided any applicable nondiscrimination rules are satisfied.

Note: Employers should confirm permitted election changes with any applicable insurance carriers (including stop-loss carriers) *before* implementation. An insurance carrier may not agree to administer certain election changes because of adverse selection concerns.

- **When to allow amnesty QLEs** – An employer can choose when to permit an amnesty QLE. We believe most employers will choose to administer amnesty QLEs during a limited enrollment window rather than on an ongoing basis.

Dropping Health Coverage

An employee may only drop health coverage if the employee has other health coverage or will shortly enroll in other health coverage. An employer may rely on an employee's written attestation as evidence of current or pending enrollment in another health plan, unless the employer has actual knowledge that the employee is not or will not enroll in other health coverage. IRS Notice 2020-29 provides the following sample attestation:

Name: _____ (and other identifying information requested by the employer for administrative purposes).

I attest that I am enrolled in, or immediately will enroll in, one of the following types of coverage: (1) employer-sponsored health coverage through the employer of my spouse or parent; (2) individual health insurance coverage enrolled in through the Health Insurance Marketplace (also known as the Health Insurance Exchange); (3) Medicaid; (4) Medicare; (5) TRICARE; (6) Civilian Health and Medical Program of the Department of Veterans Affairs (CHAMPVA); or (7) other coverage that provides comprehensive health benefits (for example, health insurance purchased directly from an insurance company or health insurance provided through a student health plan).

Signature: _____

Note: The guidance does not address whether an attestation is required if the employee will remain enrolled but wants to drop coverage for a spouse or dependent. This may be an oversight, and an employer might consider using an attestation in these instances as a precaution.

Dropping FSA Coverage

Under the amnesty QLE rules, an employer permitting changes or drops to FSA coverage does not have to permit a change or drop in FSA coverage below the amount already reimbursed during the plan year.

Prospective Changes, Retroactive Blessing

In general, election changes for amnesty QLEs must be prospective.² As a reprieve for employers who made impermissible exceptions to the normal QLE rules during 2020 prior to May 12th, the Notice permits plans to retroactively treat impermissible exceptions as amnesty QLEs.

Note: This retroactive effect only applies to exceptions that occurred before May 12, 2020. An amnesty QLE permitted today cannot be retroactively effective.

Grace Periods and FSA Carryovers

An employer can amend FSAs (both HCFSA and DCFSA) to allow unused funds from a plan whose grace period or plan year ends in 2020³ to reimburse expenses incurred through December 31, 2020 in an extended grace period.⁴ This may be impractical for calendar year FSAs, because forfeitures have already occurred and it may be administratively difficult to “undo” them.

Under the cafeteria plan rules, a HCFSA cannot use a grace period and carryover feature during the same plan year. IRS Notice 2020-29 temporarily excuses this and permits the same HCFSA to use both an extended grace period and a carryover feature for the 2020 plan year.

² We assume most plans will administer these changes according to their customary rules for determining the effective date of coverage. This might be: (i) the first of the following month; (ii) the next payroll period; or (iii) the date of the election.

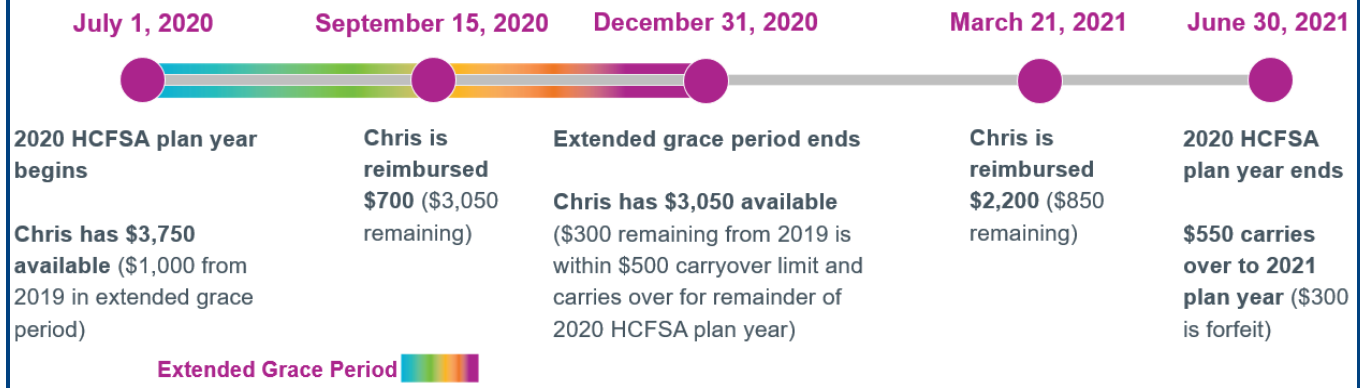
³ This would include a 2019 calendar year FSA with a grace period ending March 15, 2020, but it does not include a 2019 calendar year FSA with no grace period.

⁴ The extended grace period is available for any HCFSA, including a limited purpose HCFSA.

Example

The Situation:

- Chris works for Employer A with a July 1st – June 30th HCFSA plan year
- The HCFSA includes a carryover feature (up to \$500 for 2020; \$550 for 2021)
- The HCFSA is amended to include the extended grace period
- Chris has \$1,000 in 2019 HCFSA funds remaining on June 30, 2020 because of a delay in a planned medical procedure
- Chris elects to contribute \$2,750 for the 2020 HCFSA plan year



The IRS did not grant relief for any health savings account (HSA) eligibility issues an extended grace period might cause. The HCFSA rules permit a carryover from a general purpose HCFSA to an HSA-compatible HCFSA for individuals that elect high deductible health plan (HDHP) coverage in a subsequent year. This is not the case for extended grace period funds, which remain in their original HCFSA.

An individual with any amount in a general purpose HCFSA when the extended grace period begins will be ineligible to make or receive HSA contributions until January 1, 2021. This may be especially frustrating for individuals who elected HDHP coverage for the 2020 plan year and who have only small HCFSA balances remaining from 2019. An employer could alleviate this by permitting employees to forfeit remaining HCFSA balances before the extended grace period begins.

Other Noteworthy Items

Carryover Amount Increased and Indexed

- IRS Notice 2020-33 finally increases the maximum HCFSA carryover amount for inflation. Beginning with the 2020 plan year, the carryover maximum will be 20% of the overall HCFSA salary reduction limit. That limit is \$2,750 for 2020 plan years, making the HCFSA carryover amount \$550.

Health Savings Accounts (HSAs)

- Earlier relief granted HDHP/HSA relief to allow first dollar coverage for COVID-19 testing. The testing relief now also includes diagnostic testing for influenza A & B, norovirus and other coronaviruses, and respiratory syncytial virus (RSV).
- HSA eligibility for HDHPs providing \$0 telehealth services will apply retroactively to January 1, 2020.

Individual Coverage Health Reimbursement Accounts (ICHRA)

- IRS Notice 2020-33 provides that individual coverage health reimbursement arrangements may reimburse individual insurance policy premium expenses paid prior to the beginning of the plan year as long as that premium applied to a period of coverage that began during the plan year.

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