



# IRS offers relief to cafeteria plans, HDHPs, individual-coverage HRAs

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IRS [Notice 2020-29](#) expands temporary COVID-19 relief so cafeteria plans can allow certain midyear election changes and extend special grace periods for claims under health flexible spending arrangements (FSAs) and dependent care assistance programs (DCAPs). Notice 2020-29 also clarifies earlier guidance for health savings accounts (HSAs) and high-deductible health plans (HDHPs) on coverage of COVID-19 testing and treatment costs and telehealth services. Permanent guidance in [Notice 2020-33](#) provides an annual cost-of-living increase to the \$500 health FSA carryover limit, starting in 2020. Notice 2020-33 also allows individual-coverage health reimbursement arrangements (HRAs) to cover current plan-year premiums paid before the plan year began. This GRIST details both notices and steps for employers to consider. The most important step is for employers to coordinate with an insured plan's carrier or a self-funded plan's stop-loss carrier before adopting certain midyear election changes.

## Midyear changes to health coverage, health FSAs and DCAPs eased for 2020

Cafeteria plan participants must make elections before the first day of the plan year (or on initial eligibility, if later) and generally must maintain those elections without any change for the rest of the plan year. Under certain circumstances, however, IRS rules (26 CFR [§ 1.125-4](#)) allow — but do not require — cafeteria plans to let an employee revoke an election midyear and make a new election. Examples include when the employee experiences certain life events or changes in employment status, or when the plan has significant cost or coverage changes.

Due to the COVID-19 public health emergency, some employers would like to let employees change their elections to meet unanticipated medical and child care needs. However, unless the impetus for the change is a reason permitted under current IRS rules, cafeteria plans usually can't allow employees to modify their elections midyear, for example, to:

- Enroll in or drop health coverage
- Switch to a different health coverage option or tier offered by the employer
- Increase or decrease health FSAs or DCAP elections

### **Midyear election change relief**

Notice 2020-29 gives cafeteria plan sponsors the flexibility to allow certain midyear election changes to health coverage, health FSAs and DCAPs *during calendar-year 2020 only*, without adhering to the current IRS rules. Under the temporary relief, an employer may amend its cafeteria plan to allow the following midyear election changes, regardless of the reasons permitted under current cafeteria plan rules:

- Make a new election for employer-sponsored health coverage, if the employee initially declined to elect the employer's health coverage
- Revoke an existing election for the employer's health coverage and make a new election to enroll in different health coverage (including a change in coverage tier) sponsored by the same employer
- Revoke an existing election for the employer's health coverage, provided the employer receives written attestation that the employee is enrolled or immediately will enroll in other comprehensive health coverage
- Revoke an election, make a new election, or decrease or increase an existing election regarding a health FSA and/or a DCAP

**Benefits covered by and excluded from the relief.** The relief for midyear election changes applies to health FSAs, DCAPs and "health coverage," including insured or self-funded medical, dental, and vision benefits. The relief does not apply to the following qualified benefits in cafeteria plans (although pre-existing guidance generally allows midyear election changes to some of these benefits):

- Group term life insurance
- Paid time-off purchases and sales
- Adoption assistance

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- Long- or short-term disability plans
- HSA contributions
- 401(k) contributions

Although the notice is unclear, the relief doesn't seem to permit midyear changes to pretax elections for certain voluntary benefits like accidental death and dismemberment (AD&D) insurance or specified disease/illness or fixed-indemnity policies (e.g., a cancer insurance policy or a hospital indemnity plan). IRS confirmation would be helpful.

In any event, if contributions for benefits are made with after-tax dollars, then this pandemic relief is not needed. That's because employers already have flexibility to allow after-tax midyear election changes, without a change in status or other IRS-recognized event.

**Prospective election changes only.** The relief allows midyear election changes to apply on a prospective basis only. This means election changes will only affect employee contributions and coverages going forward after the election change and cannot apply retroactively.

**Attestation required to revoke health coverage.** To revoke the employer's health coverage midyear, employees must provide the employer a written attestation stating they are enrolled or will immediately enroll in other comprehensive health coverage. Absent actual knowledge to the contrary, the employer may rely on this written attestation. Notice 2020-29 provides an example of an acceptable written 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: \_\_\_\_\_

Revoking employer-provided health coverage is the only election change under the pandemic relief that requires an employer to obtain supporting documentation. No other changes permitted under the relief require any sort of justification or documentation.

**Application to dental and vision coverage unclear.** Dental and vision elections can be changed (e.g., to switch coverage options or tiers), but whether those coverages can be revoked is unclear. If dental or vision can be revoked, whether an employee must provide written attestation of enrollment in other comprehensive health coverage — and if so, what qualifies as “other comprehensive health coverage” for these benefits — is uncertain. Formal IRS guidance on these issues would be welcome.

**COBRA considerations.** To comply with COBRA rules (26 CFR [§ 54.4980B-5](#), Q&A-4(c)), an employer that allows midyear election changes under this relief will likely need to offer COBRA qualified beneficiaries the same opportunities to change elections.

**Notice to eligible employees and plan beneficiaries.** An employer adopting changes permitted by the pandemic relief must notify all employees eligible to participate in the cafeteria plan (and probably COBRA qualified beneficiaries as well). Notice 2020-29 does not provide any specifics on how or when employers should provide this notice, although ERISA’s notice requirements to provide a summary of material modifications (SMM) may apply. However, separate pandemic relief ([Disaster Relief Notice 2020-01](#)) from the Department of Labor (DOL) has eased the timing requirements for SMMs and other ERISA Title I notices and disclosures. (As discussed [later](#), employers taking advantage of the IRS temporary relief must also amend the plan document to allow the new elections.)

**Relief effective retroactively.** Some employers may have allowed election changes similar to those provided in Notice 2020-29 before IRS issued the guidance. For example, employers that reduced hours or instituted furloughs or wanted to extend coverage to additional employees may have allowed election changes not normally permitted under the cafeteria plan rules. Mindful of this fact, IRS has made the pandemic relief effective from Jan. 1 through Dec. 31, 2020. This means an employer that allowed election changes consistent with the relief prior to publication of the IRS notice has not violated the cafeteria plan rules, as long as the employer timely adopts a conforming plan amendment (as discussed [later](#)).

The relief does not, however, allow employees’ election changes to apply retroactively (for example, to their health FSA or DCAP) and trigger a cash reimbursement of previous contributions. In fact, the pandemic relief does not allow any cashouts or refunds for any benefit elections.

## Implementation considerations

**Design flexibility.** Employers do not have to adopt the temporary relief for midyear election changes and can choose to offer all, some, or none of the new election-change options. If an employer chooses to provide some of the flexibility permitted under the relief, the employer can limit the period (e.g., to one month) for making election changes. On the other hand, nothing in the relief prohibits an employer from allowing election changes consistent with the relief more than once during 2020.

**Nondiscrimination.** Employers adopting any of the pandemic relief's options should be mindful of the nondiscrimination rules for cafeteria plans and watch for unintended compliance failures that could result.

**Adverse selection.** Adverse selection can occur in group health plans when higher-risk employees enroll, but lower-risk people don't. Adverse selection can also happen when multiple coverage options are offered and the higher-risk employees enroll in the more robust options, while lower-risk employees enroll in the less expensive, less comprehensive options. To reduce the possibility of adverse selection, employers may decide to limit the election changes allowed or not to offer any of new options under the relief. Any limitations, however, need to comply with the Health Insurance Portability and Accountability Act (HIPAA) rules that prohibit discriminating on the basis of health status.

*Example.* To prevent adverse selection, an employer could limit midyear health coverage changes to permit only new elections reducing an employee's coverage, such as a switch from family to self-only coverage or from a high-option to a low-option plan.

**Health FSA issues.** Under the uniform coverage rule (proposed 26 CFR [§ 1.125-5\(d\)](#)), the full amount of a participant's health FSA election must be available from the start of the plan year, rather than accrued based on the participant's actual contributions. This means that employees may receive distributions greater than their contributions to date and have a so-called overspent account. For example, an employee could — if the plan allows — reduce a prospective health FSA election below the amounts already reimbursed, leaving the employer on the hook for the overspent account. To avoid this result, the pandemic relief permits employers to limit allowable changes so the new election amount is no less than the amount the health FSA has already reimbursed the employee. (This rule already applies to DCAPs.)

*Example.* During open enrollment, Jim elected to contribute \$1,200 to his health FSA. To date, Jim has contributed \$600 and received \$1,000 in reimbursements for medical expenses. Jim's employer can limit election change options under pandemic relief so he can't reduce his FSA election below \$1,000 for the year. That means Jim will still have to contribute \$400 to his health FSA. Alternatively, if Jim had spent \$600 or less, he could reduce his election to eliminate any more contributions for the year.

## **Temporary special grace period for health FSAs and DCAPs**

Notice 2020-29 allows cafeteria plans to provide a special grace period during which unused amounts from the prior plan year remaining in a health FSA (general- or limited-purpose) or a DCAP may be used to pay or reimburse qualifying expenses incurred through Dec. 31, 2020. Ordinarily, a health FSA can either adopt the standard 2-1/2-month grace period or provide for a carryover amount, but cannot have both. Under this limited relief, health FSAs can allow both carryovers and the special grace period. DCAPs can have a grace period but cannot have a carryover provision.

The pandemic relief specifically allows a special grace period in two scenarios:

- **A cafeteria plan with an existing grace period ending in 2020.** For example, an employer with a calendar-year cafeteria plan with an existing grace period ending March 15 can extend that grace period until Dec. 31, 2020. This relief is likewise available to noncalendar-year plans with (or newly adopting) a grace period ending in 2020. The relief is not available to calendar-year plans that ended on Dec. 31, 2019, and didn't already provide a grace period.
- **A cafeteria plan year ending in 2020.** For example, an employer with a noncalendar-year cafeteria plan that ends on June 30 but currently lacks any grace period can amend the plan to add a special grace period that lasts until Dec. 31, 2020. This relief also applies to noncalendar year plans ending in 2020 that currently have a shorter grace period or a carryover provision for the health FSA, or offer neither option.

Similar to the relief for midyear election changes, this relief is not mandatory for employers to offer. Instead, an employer can choose to take advantage of all, some or none of the relief. In any event, the special grace period cannot extend beyond Dec. 31, 2020. Notably, the guidance doesn't provide any extensions or relief for health FSAs or DCAPs that end after 2020. As noted earlier, the relief does not allow any cashouts or refunds of unused amounts.

### Special grace period can create complications for HSA eligibility

An individual who can apply unused amounts in a general-purpose health FSA when a plan year or a standard grace period ends in 2020 toward expenses incurred during a special grace period is ineligible to make or receive HSA contributions during that extended grace period. This is the case even if the health FSA is spent down before the end of the special grace period. In contrast, a participant in a limited-purpose or other HSA-compatible health FSA would continue to be eligible for HSA contributions during the special grace period, as under current rules.

**Earlier IRS/DOL pandemic relief for claim deadlines not affected.** Under [earlier pandemic relief](#) from IRS and DOL, any ERISA-covered plan — such as a health FSA — with a claim run-out period ending on or after March 1 must suspend the run-out period until after the outbreak period ends. The run-out period is typically a 90-day period after the end of a health FSA plan year (or, if applicable, a standard grace period). During that period, a participant can submit claims for expenses incurred during the prior plan year against funds remaining in the account at the end of that plan year. This relief is not affected by the new IRS relief allowing midyear changes to cafeteria plan elections or a special grace period. In addition, prior IRS guidance ([Notice 2020-23](#)) allowing employees hired on or after April 1 through July 14 to make initial elections until July 15 that apply retroactively is not affected.

## Permanent improvement to health FSA carryovers

Under [Notice 2013-71](#), cafeteria plans can let participants carry over up to \$500 of any unused health FSA amounts at plan year-end and use those funds to reimburse medical expenses incurred in the next plan year. An executive order ([EO 13877](#)) published June 27, 2019, gave the Treasury secretary 180 days to issue guidance increasing the amount of health FSA funds that can carry over without penalty at plan year-end. Notice 2020-33 comes in response to the executive order.

### Indexing of carryover limit

Notice 2020-33 provides an annual cost-of-living adjustment (COLA) to the maximum \$500 carryover amount. The maximum carryover amount now equals 20% of the limit on employee pretax contributions to a health FSA for a plan year. The COLA calculation for the pretax contribution limit is rounded down to the nearest multiple of \$50, so the indexed increase to the maximum carryover amount will be a multiple of \$10 (20% of any \$50 increase to the pretax contribution limit). As a result, the maximum unused health FSA amount that a participant can carry over from a plan year starting in 2020 into the 2021 plan year is \$550 (20% of the \$2,750 pretax contribution limit for 2020).

### Midyear election changes permitted

The pandemic relief in Notice 2020-29 means employers can allow participants to increase or begin health FSA contributions to take advantage of the higher carryover limit. Under Notice 2020-33, health FSA participants apparently may use contributions made after the revised election for any medical expenses incurred during the first plan year that begins on or after Jan. 1, 2020. Employers adopting the higher carryover limit must provide notice to eligible employees and adopt a plan amendment on or before Dec. 31, 2021 (see discussion below). But like the relief provided for midyear election changes, Notice 2020-33 does not require an employer to increase the permissible health FSA carryover limit.

## Cafeteria plan amendments required

An employer that wants to offer the 2020 temporary relief permitting midyear changes to health coverage, health FSA or DCAP elections or a special grace period for health FSA or DCAP claims must adopt a plan amendment. An employer that decides to adopt the COLA increase to the maximum health FSA carryover for 2020 and future plan years likewise must adopt a plan amendment. Although sponsors typically must amend cafeteria plans by the end of the plan year in which the amendment takes effect, the pandemic relief provides additional flexibility on timing.

### 2020 plan year amendments

Amendments adopting the IRS relief for midyear election changes during 2020 must be adopted on or before Dec. 31, 2021, but can apply retroactively to any date in 2020, as long as plan operations conform

to the guidance and the employer provides adequate notice to all employees eligible to participate in the cafeteria plan. In addition, a noncalendar-year plan apparently can make amendments to either the plan year that begins or ends in the 2020 calendar year or both, as long as the plan amendments are adopted on or before Dec. 31, 2021.

## 2021 plan year amendments

To adopt the increased carryover amount for a plan year that begins in 2021, a plan amendment is due by the last day of the plan year that begins in 2021.

## Additional relief for HDHPs

Notice 2020-29 clarifies earlier guidance ([Notice 2020-15](#)) allowing predeductible HDHP coverage of COVID-19 testing and treatment costs and telehealth services without affecting HSA eligibility.

## Testing and treatment for COVID-19

The Families First Coronavirus Response Act (FFCRA) ([Pub. L. No. 116-127](#)), as amended by the Coronavirus Aid, Relief and Economic Security (CARES) Act ([Pub. L. No. 116-136](#)), requires group health plans to cover COVID-19 tests and related items and services without cost sharing. Even before those acts took effect, IRS guidance ([Notice 2020-15](#)) allowed HDHPs to cover services and items related to COVID-19 testing and treatment before participant have met their deductible. However, that guidance, published March 11, did not indicate an effective date.

Notice 2020-29 clarifies that the earlier IRS relief applies to HDHP reimbursements of expenses related to COVID-19 tests and treatment incurred on or after Jan. 1, 2020. The new pandemic relief also clarifies that diagnostic testing for influenza A and B, norovirus, other coronaviruses, respiratory syncytial virus (RSV), and any items or services that the FFCRA and CARES Act require health plans to cover without cost sharing are part of the HDHP relief for COVID-19 testing and treatment coverage under Notice 2020-15.

## Telehealth

The CARES Act allows HSA-eligible HDHPs to cover telehealth and other remote care services with no deductible or a lower deductible than the minimum otherwise required by law. The act also allows an otherwise HSA-eligible individual to receive coverage for telehealth and other remote care services from a vendor outside of the HDHP — even before satisfying the HDHP deductible — without affecting eligibility for HSA contributions. This CARES Act safe harbor took effect March 27 and applies to plan years beginning on or before Dec. 31, 2021. Notice 2020-29 extends the safe harbor retroactively to telehealth services provided on or after Jan. 1, 2020 (but still limits the relief to plan years beginning on or before Dec. 31, 2021).



## **Fix for individual-coverage HRAs**

Group health plans, including individual-coverage HRAs, may not reimburse medical expenses incurred before the start of the plan year. Medical expenses are treated as incurred when the covered individual receives the related medical care — not when the amount is billed or paid. Because health insurance premiums are often due in advance, these rules create problems for individuals seeking HRA reimbursement of premiums for individual health or Medicare coverage paid before the first day of a plan year.

Notice 2020-33 allows a plan to treat health insurance premiums as incurred on (i) the first day of each month of coverage, on a prorated basis; (ii) the first day of the coverage period; or (iii) the date the premium was paid. For example, a calendar-year individual-coverage HRA may immediately reimburse a substantiated premium for health insurance coverage that begins on Jan. 1, even if the participant paid the premium before the start of the HRA plan year (for example, in December).

## **Next steps for employers**

- Employers should review the changes allowed under the recent guidance and determine if they want to adopt some, all or none of those changes. Employers may want to weigh providing maximum flexibility to their employees against the possibility of adverse selection, vendor limitations or administrative complexity. Employers could choose to limit midyear election changes to address those concerns.
- Employers with insured plans should confirm whether their carriers permit the midyear election changes under the pandemic relief, while employers with self-funded plans should check with their stop-loss carriers. Some stop-loss carriers reportedly are refusing to pay claims related to health coverage extended to any newly covered individuals as a result of these midyear election changes.
- Employers with HDHPs should consider how providing a special grace period for a general-purpose health FSA will impact eligibility for 2020 employer and employee HSA contributions.
- Benefit administrators should be consulted to confirm they are prepared to help inform eligible employees about the election-change opportunities and to administer the changes.
- Employers should confirm that their carrier or third-party administrator is ready to cover retroactively to Jan. 1, 2020, all of the required COVID-19 and related tests (e.g., influenza, etc.), including associated items and services, without cost sharing.
- Employers should provide notice of any changes to all eligible employees. In the absence of specific guidance from regulators, employers should consult counsel about the timing and method of notice delivery, factoring in the recent relief for any notices and disclosures required by ERISA Title I.

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- Sponsors should prepare any necessary plan amendments related to the pandemic relief and plan for timely adoption.
- Employers may also want to review whether their plans need amendments to reflect the retroactive HDHP relief to Jan. 1, 2020, or the change in premium reimbursements for individual-coverage HRAs.

## Related resources

### Non-Mercer resources

- [Notice 2020-29](#), COVID-19 relief for cafeteria plans and HDHPs (IRS, May 12, 2020)
- [Notice 2020-33](#), Modification of carryover rule for health FSAs and clarification of premium reimbursements by individual-coverage HRAs (IRS, May 12, 2020)
- [Joint DOL and IRS notice](#), Extension of certain timeframes for employee benefit plans, participants and beneficiaries affected by the COVID-19 outbreak (Federal Register, May 4, 2020)
- [Disaster Relief Notice 2020-01](#), Guidance and relief for employee benefit plans due to the COVID-19 (novel coronavirus) outbreak (DOL, April 28, 2020)
- [Description of tax provisions in the CARES Act](#) (Joint Committee on Taxation, April 23, 2020)
- [Pub. L. No. 116-136](#), the CARES Act (Congress, March 27, 2020)
- [Section-by-section summary of the CARES Act](#) (Senate Health, Education, Labor & Pensions Committee, March 25, 2020)
- [Pub. L. No. 116-127](#), the FFCRA (Congress, March 18, 2020)
- [Notice 2020-15](#) (IRS, March 11, 2020)
- [EO 13877](#), Improving price and quality transparency in American health care to put patients first (Federal Register, June 27, 2019)

### Mercer Law & Policy resources

- [IRS, DOL ease deadlines for health, other benefit plans and participants](#) (May 27, 2020)
- [Keeping track of COVID-19 laws affecting employee benefits, jobs](#) (May 4, 2020)
- [Employer health plans have to meet new COVID-19 coverage mandate](#) (April 21, 2020)

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- [CARES Act boosts telehealth, makes other health, paid leave changes](#) (March 27, 2020)
- [Virus aid legislation includes cost-sharing curbs, new leave rights](#) (March 18, 2020)
- [COVID-19 spurs IRS relief for HDHPs, state insurance guidance](#) (March 18, 2020)

### Other Mercer resources

- [Stay informed on the coronavirus](#) (regularly updated)
- [IRS allows more election changes, modifies FSA rules](#) (May 14, 2020)
- [HSAs: Saving for and during an emergency](#) (May 14, 2020)
- [Extended timeframes for plan disclosures and elections, including COBRA and HIPAA](#) (May 7, 2020)

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