THE WAGNER LAW GROUP

LAW ALERT
March 2, 2021

IRS Guidance on Flexible Spending Account Relief Under CAA

The IRS has issued Notice 2021-15 ("Notice") to provide clarification on the flexible spending account ("FSA") relief contained in the Consolidated Appropriations Act, 2021 ("CAA"). The Notice also extends cafeteria plan election relief, and provides guidance on adopting plan amendments to implement these optional changes.

Background

In response to the COVID-19 pandemic, Congress enacted temporary special rules to provide broader flexibility to plan sponsors in operating both health and dependent care FSAs. The new rules are part of the CAA, which was enacted in December 2020.

IRS Notice 2021-15

The Notice confirms that a plan's adoption of these provisions is optional, and that implementing this relief will not, by itself, cause a health FSA to lose "excepted benefit" status (and thereby become required to comply with the ACA's mandates). The Notice also explains that this relief only applies through the end of the 2022 plan year, and that the previous rules will resume, in most instances, for plan years ending in or after 2022.

Under the Notice, plans may be amended to provide that:

- **Mid-Year FSA Election Change Relief.** Employees may make (on a prospective basis) one or more elections, revoke an election, or decrease or increase an existing election for a health or dependent care FSA for the plan year ending 2021, irrespective of whether the employee has actually experienced a change in status event.
- **Unlimited Carryover.** Employees may carry over all or some of their unused health and/or dependent care FSA funds from a plan year ending in 2020 or 2021 and apply them to the next plan year.
- NOTE: While the new rules are similar to the existing rules for health FSAs, they can now be applied to dependent care FSAs, the dollar limits applicable under the previous rules do not apply.
- **Extended Grace Period.** The grace period for health and/or dependent care FSA for a plan year ending in 2020 or 2021 may be extended up to 12 months after the end of the plan year.
- **Health FSA Spend Down.** Employees who terminate participation in a health FSA during calendar year 2020 or 2021 may continue to spend down unused account balances through the end of the plan year in which their participation terminated (plus any applicable grace period). This change is a significant departure from the previously applicable rule that limited the reimbursement period during which expenses may be incurred to the employee's termination date (unless the participant elects COBRA) and is similar to the current rule for dependent care FSAs.

- NOTE: For health FSAs, the plan may limit reimbursement to the amount of contributions made up until the point of termination, less any previously incurred expenses.
- **Special Age Limit Relief for Dependent Care FSAs.** The Notice increases the maximum age for qualified dependents from 12 to 13, for purposes of determining the benefits that may be paid or reimbursed during: (i) the last plan year with regard to which the regular enrollment period ended on or before January 31, 2020; and (ii) where an employee has an unused balance in their dependent care FSA for such plan year, the immediately following plan year (until the child attains age 14).
- **New HSA Flexibility.** Employers may allow employees to terminate coverage under a health FSA to achieve HSA eligibility. However, the health FSA must limit reimbursements to expenses incurred before the employee dropped coverage. Employers may also allow employees to elect to convert their health FSAs to HSA-compatible limited purpose health FSAs for the carryover or grace period. Plan sponsors may implement this change so that that enrollees in high deductible health plans automatically have their health FSAs converted to limited purpose FSAs.

Plan Amendments

Plan sponsors that choose to provide these new options must amend their plans to implement the temporary relief. The Notice confirms that plan sponsors have until the end of the first calendar year following the plan year in which the change is effective to amend retroactively.

The Notice also discusses amendments that may be made to health FSAs and health reimbursement to allow them to reimburse for the cost of over-the-counter medicines and menstrual products. The Notice authorizes amending a plan to add this extra feature retroactively to January 1, 2020.

IRS Notice 2021-15 is available at https://www.irs.gov/pub/irs-drop/n-21-15.pdf

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