

COVID-19 Related Modifications to Cafeteria Plans and Flexible Spending Accounts

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In response to the COVID-19 pandemic, the IRS has issued two notices that allow employers to provide some relief to cafeteria plan participants. Together, Notice 2020-20 and Notice 2020-29 allow cafeteria plans to permit prospective midyear election changes for any reason during calendar year 2020 and to provide an extended period for employees to incur eligible expenses for reimbursement under flexible spending accounts.

Cafeteria Plan Election Changes

Usually, employees are required to make cafeteria plan benefit elections before the beginning of the plan year, and these elections may only be changed midyear in response to a permissible election change event. However, Notice 2020-29 allows an employer to amend its cafeteria plan to permit certain prospective election changes during calendar year 2020 regardless of whether a participant meets the usual election change requirements.

For employer group health plans, the following changes are permitted:

- Employees who initially declined coverage may enroll in health coverage;
- Employees who enrolled in one coverage option may enroll in different health coverage; and
- Employees who enrolled in health coverage may revoke their coverage election, if the employee certifies in writing that the employee is or will immediately be enrolled in other health coverage.

For health FSAs and dependent care FSAs, the following changes are permitted:

- Employees may revoke existing elections on a prospective basis;
- Employees may increase or decrease an existing election; or
- Employees may make a new election.

An employer implementing this relief can determine the extent to which additional elections will be permitted. For instance, an employer may consider only allowing employees to elect increased benefits or coverage or may allow some types of changes but not others.

The employer may want to consider the potential for adverse selection in implementing these changes and, if the change affects insurance coverage, the employer should confirm that its insurer will accept these midyear changes. In addition, any changes remain subject to the cafeteria plan non-discrimination rules and other applicable laws.

Extended Grace Period

Usually, for an eligible expense to be reimbursable by a health FSA or dependent care FSA, the expense must be incurred during the cafeteria plan's plan year (and, for plans that permit a grace period, during a period of up to 2½ months following the end of the plan year). However, under the new IRS guidance, an employer may also amend its cafeteria plan to permit employees to use amounts remaining in a health FSA or dependent care FSA at the end of a plan year or grace period ending in 2020 to pay or reimburse expenses incurred through December 31, 2020.

Employers implementing this extension should notify participants that if the claim period is extended for a health FSA that is not HSA-compatible, participants with unused amounts remaining at the end of a plan year or grace period ending in 2020 will not be eligible to make HSA contributions during the extended period. In addition, employers who offer flexible spending accounts administered by a third-party administrator should verify that they can implement these changes.

Plan Amendments

Employers who choose to allow increased flexibility for participant elections or an extended grace period, as described above, must adopt a plan amendment. The cafeteria plan relief may be implemented immediately, as long as an amendment is adopted on or before December 31, 2021 and may be effective retroactively as early as January 1, 2020. In addition, the employer must inform all eligible employees of the opportunity to participate in the changes.

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