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Locke Lord QuickStudy: Consolidated Appropriations Act of 2021: Relief for Flexible Spending Accounts ?

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The Consolidated Appropriations Act of 2021 (the "Act"), signed into law on December 27, 2020, includes relief for employers offering Health and/or Dependent Care Flexible Spending Arrangements ("FSAs").

Expanding the guidance issued in May 2020, the Act allows employers to amend Health FSAs and Dependent Care FSAs to give employees more flexibility to use unused account balances, at least through 2022, that may have arisen due to the COVID-19 pandemic. Employers may, but are not required to, adopt any of these provisions.

The Act's provisions include:

- ***Carryovers***. For plan years ending in 2020, an employer may amend its FSAs to allow participants to carry over all unused amounts remaining in the FSA at the end of the plan year to the plan year ending in 2021. Similarly, unused amounts from a plan year ending in 2021 may be carried over to the plan year ending in 2022. The carryovers must be administered under the same rules that apply to carryovers for Health FSAs under existing Treasury Regulations (except for the minimum carryover amount). This relief extends to both Health FSAs and Dependent Care FSAs, and is not limited to $550 (the 2021 carryover limit under existing Treasury Regulations). For reference Dependent Care FSAs have not been able to use carryovers and this provision represents a temporary period for Dependent Care FSAs to use carryovers.
  - Employers with Health FSAs that did not have a carryover provision in 2020 should consider whether to add a carryover for 2021 to allow amounts that would otherwise be treated as forfeitures to again become available for reimbursement during 2021. Note that an FSA cannot provide for both a carryover provision and a grace period (see below).
  - Employers who offer a high deductible health plan (HDHP) must consider the impact the addition of a carryover provision will have on an employee's ability to contribute to a health savings account (HSA). A carryover to a general purpose Health FSA will make a participant ineligible to contribute to an HSA for the entire plan year (even after the carryover is exhausted). If a carryover provision is added to a plan, or expanded, the employer should consider addressing this issue from a drafting perspective.

- ***Extension of Grace Periods***. Employers may extend the grace period from 2-½ months to up to 12 months after the end of the plan year. This relief applies to plan years ending in 2020 or 2021, and extends to both Health FSAs and Dependent Care FSAs.
    - These provisions do not alter the general rules for adding a new grace period. Therefore, for the 2020 plan year, if the FSA did not have a grace period feature, it cannot be amended to adopt this feature. The FSA may be amended to add the grace period feature for the 2021 plan year.
    - As mentioned above, employers who offer a high deductible health plan (HDHP) must consider the impact an extension of the grace period will have on an employee's ability to contribute to a health savings account (HSA). Employees cannot contribute to an HSA while general purpose Health FSAs funds are available during a grace period.
- ***Post-Termination Reimbursements***. For employees who cease to participate in a FSA in 2020 and 2021, employers may allow the participants to continue to receive reimbursements from unused contributions through the end of the plan year in which such participation ceased, including any grace period (including grace periods extended as permitted by the Act). Many Dependent Care FSAs may permit reimbursement for dependent care expenses incurred through the end of the year in which the participant ceased participation, but this provision is new for Health FSAs.
- ***Mid-Year Election Changes***. For plan years ending in 2021, employers may permit participants to modify their FSA contributions on a prospective basis, even if the participant did not experience a change in status. Participants may not elect to decrease their contributions below the amount which they have already been reimbursed for the plan year. Also, participants may not receive a refund of unused amounts. Employers who wish to adopt this change may consider limiting the election change period to a specified time frame (similar to an open enrollment) to ease the administrative burden.
- ***Dependent Care FSA Carry-Forward for Aged-Out Dependent***. Generally, a Dependent Care FSA can only reimburse dependent care expenses of a dependent child who is under 13 years old. For a plan year in which the enrollment period ended on or before January 30, 2020, however, Dependent Care FSAs may permit reimbursement for expenses incurred for children up to age 14. For calendar year plans, this applies to a participant with a dependent who turned 13 years old during calendar year 2020. In addition, if the participant had unused contributions at the end of the 2020 plan year (and the FSA provides for a grace period or a carryover), expenses incurred for dependents who are under the age of 14 may be reimbursed in the next plan year, but only to the extent of the unused balance.
- ***Plan Amendments***. Employers who wish to adopt any of these changes must amend the FSA plan documents to reflect the operational changes. The amendments may be adopted retroactively if adopted by the last day of

the first calendar year beginning after the end of the plan year in which the amendment is retroactively effective. For example, for a FSA with a calendar year plan year, changes that are effective for 2020 must be reflected in a plan amendment adopted by December 31, 2021. In addition, the FSA must be operated consistent with the terms of the amendment from the date the amendment is effective to the date the amendment is adopted.

Employers wishing to adopt any of these changes should consult with their third-party FSA administrator to confirm their ability to implement the changes. Also, employers should communicate any changes to employees as soon as possible to enable employees to take advantage of these changes.

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