ADDITIONAL RELIEF FOR CORONAVIRUS DISEASE (COVID-19) UNDER § 125 CAFETERIA PLANS

Notice 2021-15

I. PURPOSE AND OVERVIEW

This notice clarifies the application of § 214 of the Taxpayer Certainty and Disaster Tax Relief Act of 2020 (the Act), recently enacted as Division EE of the Consolidated Appropriations Act, 2021, Pub. L. 116-260, 134 Stat. 1182 (Dec. 27, 2020), which provides temporary special rules for health flexible spending arrangements (health FSAs) and dependent care assistance programs[1] under § 125 cafeteria plans. As described more fully below, § 214 of the Act:

- Provides flexibility with respect to carryovers of unused amounts from the 2020 and 2021 plan years;
- Extends the permissible period for incurring claims for plan years ending in 2020 and 2021;
- Provides a special rule regarding post-termination reimbursements from health FSAs during plan years 2020 and 2021;
- Provides a special claims period and carryover rule for dependent care assistance programs when a dependent "ages out" during the COVID-19 public health emergency; and
- Allows certain mid-year election changes for health FSAs and dependent care assistance programs for plan years ending in 2021.

[1] Although § 214 of the Act refers to "dependent care flexible spending arrangements," this notice uses the term "dependent care assistance programs."

This notice also provides additional relief with respect to mid-year elections for plan years ending in 2021. Specifically, with respect to employer-sponsored health coverage, a § 125 cafeteria plan may permit employees who are eligible to make salary reduction contributions under the plan to take any of the following actions for plan years ending in 2021: (1) make a new election on a prospective basis, if the employee initially declined to elect employer-sponsored health coverage; (2) revoke an existing election and make a new election to enroll in different health coverage sponsored by the same employer on a prospective basis; and (3) revoke an existing election on a prospective basis, provided that the employee attests in writing that the employee is enrolled, or immediately will enroll, in other health coverage not sponsored by the employer.

The notice also provides relief with respect to the effective date of amendments to § 125 cafeteria plans and health reimbursement arrangements (HRAs) to implement the expansion of allowed expenses for health FSAs and HRAs by the Coronavirus Aid, Relief, and Economic Security Act (CARES Act), Pub. L. 116-136, 134 Stat. 281 (March 27, 2020) to include over-the-counter drugs without prescriptions and menstrual care products.

II. BACKGROUND

A. Elections Under a § 125 Cafeteria Plan

Section 125(d)(1) of the Internal Revenue Code (Code) defines a § 125 cafeteria plan as a written plan maintained by an employer under which all participants are employees, and all participants may choose among two or more benefits consisting of cash and qualified benefits. Subject to certain exceptions, § 125(f) defines a qualified

benefit as any benefit which, with the application of § 125(a), is not includable in the gross income of the employee by reason of an express provision of the Code. Qualified benefits that may be provided under a § 125 cafeteria plan include, but are not limited to, employer-provided accident and health plans excludable under §§ 105(b) and 106, health FSAs excludable under §§ 105(b) and 106, and dependent care assistance programs excludable under § 129.

Elections regarding qualified benefits under a § 125 cafeteria plan generally must be irrevocable and must be made prior to the first day of the plan year, except as provided under Treas. Reg. § 1.125-4. Treas. Reg. § 1.125-4 provides that a § 125 cafeteria plan may permit an employee to revoke an election during a period of coverage and to make a new election under certain circumstances, such as if the employee experiences a change in status or there are significant changes in the cost of coverage. Section 125 does not require a § 125 cafeteria plan to permit the mid-year election changes allowed under Treas. Reg. § 1.125-4.

B. Health FSAs and Dependent Care Assistance Programs – Carryovers and Grace Periods

A § 125 cafeteria plan may permit the carryover of unused amounts remaining in a health FSA as of the end of a plan year to pay or reimburse a participant for medical care expenses incurred during the following plan year, subject to the carryover limit (the carryover rule).[2] See Notice 2013-71, 2013-47 IRB 532, and Notice 2020-33, 2020-22 IRB 868. In the alternative, a § 125 cafeteria plan may permit a participant to apply

[2] The maximum unused amount remaining in a health FSA from a plan year beginning in 2020 allowed to be carried over to the plan year beginning in 2021 is $550 (20 percent of $2,750, the indexed 2020 limit under § 125(i)).

unused amounts (including amounts remaining in a health FSA or dependent care assistance program) at the end of the plan year to pay expenses incurred for those same qualified benefits during a period of up to two months and 15 days immediately following the end of the plan year (the grace period rule). See Notice 2005-42, 2005-1 C.B. 1204, and Prop. Treas. Reg. § 1.125-1(e). For a health FSA, a § 125 cafeteria plan may adopt a carryover or a grace period (or neither) but may not adopt both features. See Notice 2013-71. Under generally applicable rules, without regard to § 214 of the Act, a § 125 cafeteria plan may not adopt a carryover for a dependent care assistance program.

In Notice 2020-29, 2020-22 IRB 864, the Department of the Treasury (Treasury Department) and the Internal Revenue Service (IRS) explained that, due to the nature of the COVID-19 public health emergency and unanticipated changes in the availability of certain medical care and dependent care, employees may be more likely to have unused health FSA amounts or dependent care assistance program amounts at the end of plan years, or grace periods, ending in 2020. To provide related relief, Notice 2020-29 extended, to the end of calendar year 2020, the period during which employees could be permitted to apply unused health FSA amounts and dependent care assistance program amounts remaining as of the end of a grace period or plan year ending in 2020 to pay or reimburse medical care expenses or dependent care expenses.

C. Impact of Health FSA Reimbursements on Eligibility to Contribute to an HSA

Section 223 of the Code permits eligible individuals to establish and contribute to health savings accounts (HSAs). Pursuant to § 223(c)(1)(A), an eligible individual is, with respect to any month, any individual if (i) the individual is covered under a high deductible health plan (HDHP) as of the first day of the month, and (ii) the individual is not, while covered under an HDHP, covered under any health plan which is not an HDHP and which provides coverage for any benefit which is covered under the HDHP. An HDHP is a health plan that satisfies the minimum annual deductible requirement and maximum out-of-pocket expenses requirement under § 223(c)(2)(A). Coverage by a general purpose health FSA disqualifies an otherwise eligible individual from contributing to an HSA, although coverage by an HSA-compatible health FSA, such as a limited purpose health FSA or a post-deductible health FSA, would not do so.[3] See Rev. Rul. 2004-45, 2004-1 C.B. 971.

III. GUIDANCE RELATED TO SECTION 214 OF THE ACT

A. Section 214 Carryovers for Health FSAs and Dependent Care Assistance Programs

Section 214 of the Act temporarily increases flexibility for a § 125 cafeteria plan to provide a carryover of unused amounts remaining in a health FSA or dependent care assistance program to pay or reimburse medical care expenses or dependent care expenses in a subsequent plan year.[4] Specifically, § 214(a) of the Act provides that, for

[3] Notice 2005-86, 2005-49 IRB 1075, clarifies that coverage by a general purpose health FSA during a grace period is health coverage that disqualifies an otherwise eligible individual from contributing to an HSA during that period. However, Notice 2005-86 provides methods an employer can use to amend the health FSA for the grace period so it does not disqualify employees from contributing to an HSA during that period. For a more detailed discussion of these options, see section III.F. of this notice.

[4] Except as provided in § 214 of the Act, a § 125 cafeteria plan may not adopt a carryover for a dependent care assistance program.

plan years ending in 2020, a plan that includes a health FSA or dependent care assistance program shall not fail to be treated as a cafeteria plan merely because the plan or arrangement permits participants to carry over (under rules similar to current rules for health FSAs) any unused benefits or contributions from that plan year to the plan year ending in 2021. Section 214(b) of the Act provides a similar rule for plan years ending in 2021, permitting the carryover of any unused benefits or contributions from that plan year to the plan year ending in 2022. (Collectively, the relief provided in § 214(a) and (b) of the Act related to carryovers is referred to in this notice as the § 214 carryover.) Thus, an employer, in its discretion, may amend one or more of its § 125 cafeteria plans to provide a carryover of all or part of the unused amounts remaining in a health FSA or a dependent care assistance program as of the end of a plan year ending in 2020 or 2021[5] to the immediately subsequent plan year.[6]

[5] All amounts available on the last day of the 2020 or 2021 plan year are available to carry over, regardless of the source of the amounts. Thus, for example, a $500 amount carried over from a 2019 calendar plan year to the 2020 calendar plan year that remains unused is available to be carried over to the 2021 calendar plan year, and a $500 amount carried over from a 2019 non-calendar plan year to a 2020 non-calendar plan year that remains unused is available to be carried over to the 2021 non-calendar plan year. For employers with plan years or grace periods ending in 2020 that, pursuant to Notice 2020-29, adopted the extended claims period until December 31, 2020, amounts made available during that extended claims period that remain unused as of December 31, 2020, are available to be carried over pursuant to § 214 of the Act. However, if a plan did not provide for a carryover for its 2019 plan year, the extension of the runout period to submit 2019 claims for health FSAs until after the COVID-19 emergency period pursuant to the joint notice of relief, Extension of Certain Timeframes for Employee Benefit Plans, Participants, and Beneficiaries Affected by the COVID-19 Outbreak, issued by the Treasury Department and the Department of Labor, under § 7508A(b) of the Code (85 FR 26351) does not otherwise permit the carryover of unused 2019 amounts to the 2020 plan year.

[6] An employer adopting the § 214 carryover may, in its discretion, require employees to enroll in the health FSA or dependent care assistance program with a minimum election amount to have access to the unused amounts from the prior plan year. See Q&A 24 of Notice 2015-87, 2015-52 IRB 889. If an employer adopts both the § 214 carryover from the 2020 calendar year to the 2021 plan year and the flexibility for mid-year election changes, and an employee later elects to participate in the health FSA or dependent care assistance program mid-year on a prospective basis, the § 214 carryover amount may be made available to reimburse employee expenses retroactive to January 1, 2021, as discussed in more detail in section III.E. of this notice.

For example, if an employer sponsored a calendar year § 125 cafeteria plan in 2020 with a health FSA that provides for a $550 carryover, the employer may amend the plan to carry over the entire unused amount remaining in an employee's health FSA as of December 31, 2020, to the 2021 plan year (even if that amount exceeds $550). The employer also may amend the plan to carry over the entire unused amount remaining in an employee's health FSA as of December 31, 2021, to the 2022 plan year. This relief applies to all health FSAs, including HSA-compatible health FSAs, and also applies to all dependent care assistance programs. However, health FSA amounts may be used only for medical care expenses, and dependent care assistance program amounts may be used only for dependent care expenses. The § 214 carryover is available to § 125 cafeteria plans that currently have a grace period or provide for a carryover, as well as plans that currently do not have a grace period or provide for a carryover, notwithstanding Notice 2013-71, which otherwise continues in effect and provides that health FSAs can either adopt a grace period or provide for a carryover amount but cannot have both.[7] In addition, an employer may limit the carryover to an amount less than all unused amounts and may limit the carryover to apply only up to a specified date during the plan year.[8]

For purposes of determining whether an eligible individual qualifies to make contributions to an HSA, the carryover of unused amounts to the 2021 plan year or the

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[7] For example, if a § 125 cafeteria plan provides for a carryover from the 2022 plan year to the 2023 plan year, the plan may not provide a grace period for the 2022 plan year.

[8] Amounts carried over or available during an extended period in accordance with § 214(c) of the Act are not taken into account in determining whether a health FSA satisfies the maximum benefit payable limit condition under the excepted benefits regulations (Treas. Reg. § 54.9831-1(c)(3)(v)). See Q&A 6 in FAQs About Affordable Care Act Implementation (Part XIX) (May 2, 2014), available at https://www.dol.gov/sites/dolgov/files/EBSA/about-ebsa/our-activities/resource-center/faqs/aca-part-xix.pdf.

2022 plan year is an extension of the coverage by a health plan that is not an HDHP (except in the case of an HSA-compatible health FSA, such as a limited purpose health FSA). Therefore, an individual is not eligible to make contributions to an HSA during a month in which the individual participates in a general purpose health FSA to which unused amounts are carried over pursuant to § 214 of the Act.[9] See section III.F. of this notice for information regarding the conversion of a general purpose health FSA to an HSA-compatible health FSA to permit individuals with a health FSA carryover to qualify to make contributions to an HSA. Employers may also amend their plans to allow employees, on an employee-by-employee basis, to opt out of the carryover to preserve their HSA eligibility.[10]

B. Extended Claims Periods for Health FSAs and Dependent Care Assistance Programs, and Post-Termination Reimbursements from Health FSAs

Section 214 of the Act temporarily provides flexibility for a § 125 cafeteria plan to provide an extended period to apply unused amounts remaining in a health FSA or dependent care assistance program to pay or reimburse medical care expenses or dependent care expenses, respectively. Specifically, § 214(c)(1) of the Act provides that a plan that includes a health FSA or dependent care assistance program shall not fail to be treated as a cafeteria plan merely because the plan or arrangement extends the grace period for a plan year ending in 2020 or 2021 to 12 months after the end of

[9] An individual continues to participate in the general purpose health FSA for the entire coverage period of the health FSA, even if the health FSA's funds are exhausted before the end of the coverage period, subject to the special rule for health FSA grace periods under § 223(c)(1)(B)(iii)(I).
[10] See Chief Counsel Advice memorandum 201413005 (Feb. 12, 2014), available at https://www.irs.gov/pub/irs-wd/1413005.pdf.

that plan year, with respect to unused benefits or contributions remaining in a health FSA or a dependent care assistance program.

Thus, an employer, in its discretion, may amend one or more of its § 125 cafeteria plans to permit employees to apply any unused amounts remaining in a health FSA or a dependent care assistance program as of the end of a plan year ending in 2020 or 2021 to reimburse expenses incurred for the same qualified benefit (medical care or dependent care) up to 12 months after the end of the plan year. For example, if an employer sponsored a calendar year § 125 cafeteria plan in 2020 with a health FSA, the employer may amend the plan to permit employees to apply the entire unused amount remaining in their health FSAs as of December 31, 2020, to reimburse employees for medical care expenses incurred through December 31, 2021.

In addition, § 214(c)(2) of the Act provides that a plan that includes a health FSA shall not fail to be treated as a cafeteria plan merely because the plan or arrangement allows (under rules similar to the rules applicable to dependent care assistance programs)[11] an employee who ceases participation in the plan during calendar year 2020 or 2021 to continue to receive reimbursements from unused benefits or contributions through the end of the plan year in which participation ceased (including any grace period, taking into account any modification of a grace period permitted under § 214(c)(1) of the Act).

[11] See Prop. Treas. Reg. § 1.125-6(a)(4)(v), which provides that, at the employer's option, the written cafeteria plan may provide that dependent care expenses incurred after the date an employee ceases participation in the cafeteria plan (for example, after termination of employment) and through the last day of that plan year (or grace period immediately after that plan year) may be reimbursed from unused benefits, if all of the requirements of § 129 are satisfied.

The relief provided under § 214(c) of the Act applies to all health FSAs, including HSA-compatible health FSAs. An employer may choose to adopt an extended period for incurring claims that is less than 12 months, and an employer may choose to adopt a period that ends before the end of the plan year, during which employees who have ceased participation in a plan may continue to receive reimbursements. The extension of time for incurring claims pursuant to § 214(c)(1) of the Act is available to § 125 cafeteria plans that currently have a grace period or provide for a carryover, as well as plans that currently do not have a grace period or provide for a carryover, notwithstanding Notice 2013-71, which otherwise continues in effect and provides that health FSAs can either adopt a grace period or provide for a carryover amount but cannot have both. Finally, health FSA amounts may be used only for medical care expenses, and dependent care assistance program amounts may be used only for dependent care expenses.

The extension of the period for incurring claims that may be reimbursed by a health FSA is an extension of the coverage by a health plan that is not an HDHP in determining whether an individual is eligible to make contributions to an HSA (except in the case of an HSA-compatible health FSA). Therefore, an individual is not eligible to make contributions to an HSA if the individual participates in a general purpose health FSA, including during any extended period in which the participant can incur claims pursuant to § 214(c) of the Act. This restriction on making contributions to an HSA if amounts remain available in a general purpose health FSA applies not only to current participants in the health FSA but also to individuals who remain eligible to incur claims but have ceased participation in the health FSA as the result of termination of

employment, change in employment status, or a new election during calendar year 2020 or 2021. See section III.F. of this notice for information regarding the conversion of a general purpose health FSA to an HSA-compatible health FSA. Employers also are permitted to amend their plans to allow employees, on an employee-by-employee basis, to opt out of any extended period for incurring claims in plan years ending in 2021 and 2022, to preserve their HSA eligibility.

With respect to the extension of the period for incurring claims for an employee who ceases to be a participant, the employer, in its discretion, is permitted to limit the unused amounts in the health FSA to the amount of salary reduction contributions the employee had made from the beginning of the plan year in which the employee ceased to be a participant up to the date the employee ceased to be a participant. This option is available for an employee who ceases to be a participant as the result of termination of employment, change in employment status, or a new election during calendar year 2020 or 2021. Finally, the extension period is limited to the end of the plan year in which participation ceased (including any grace period, taking into account any modification of a grace period permitted under § 214(c)(1) of the Act).

C. Interaction of § 214 Carryovers and Extended Periods for Incurring Claims

As a practical matter, in most cases the flexibility provided by the § 214 carryover and the extension of grace periods under § 214(c)(1) of the Act provide the same relief, as both provisions allow all unused benefits remaining for plan years ending in 2020 and 2021 to be made available for the same benefit (medical care expenses or dependent care expenses) incurred in the immediately subsequent plan year ending in

2021 and 2022, respectively.[12] However, the relief available to employees may vary depending on whether an employer adopts either the extended grace period under § 214(c)(1) or the § 214 carryover, because the two types of relief interact differently with an extended period for incurring claims available under § 214(c)(2). An employer that adopts a grace period under § 214(c)(1) may also allow employees who have ceased participation in a plan in an earlier plan year to further extend a period for incurring claims until the end of the subsequent plan year under § 214(c)(2), but this additional extended period for incurring claims is not available for employees who ceased participation in the earlier plan year and whose employers have adopted the § 214 carryover instead. Therefore, consistent with current guidance,[13] an employer may not amend its plan to adopt both the § 214 carryover and the extended grace period under § 214(c)(1) for a particular plan year for a particular health FSA or dependent care assistance program, and an amendment must specify which option is adopted for the applicable plan years.[14] See section III.H. of this notice for information regarding plan amendments. Subject to the nondiscrimination rules under §§ 125 and 129, an employer is permitted to adopt this relief for some, but not all, health FSA or

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[12] Notice 2005-42 provides that unused amounts available during a grace period are forfeited at the end of the grace period; however, that is a function of the grace period being limited to 2½ months. Thus, under the rules providing for a 2½ month grace period, unused amounts from year 1 available during a grace period in year 2 are no longer available at the end of year 2 and cannot be made available for any subsequent grace period in year 3. In contrast, because § 214(c) of the Act provides for a 12-month grace period, it is possible that some or all of the unused amounts available in a grace period at the beginning of a plan year will remain available at the end of that plan year, in which case they may be made available in the next grace period. Specifically, amounts available on the last day of a plan year due to a 12-month grace period adopted pursuant to § 214(c) are not required to be forfeited, and the plan terms may allow the unused amounts to be made available for expenses incurred during a grace period in the following plan year.

[13] See Notice 2013-71.

[14] Note that, if an employer adopts a plan amendment pursuant to § 214 of the Act and this notice that provides that the amendment supersedes normal operations for the duration of the period for which the plan adopts the relief, an employer is not required to also delete an existing plan provision that provides for a $550 carryover or a 2½ month grace period.

dependent care assistance program participants.[15] Amounts carried over or available during an extended claims period will not be taken into account for purposes of the nondiscrimination rules applicable to § 125 cafeteria plans and to dependent care assistance programs under § 129.

The otherwise applicable rules regarding carryovers and grace periods will apply for plan years ending in or after 2022. For a plan that provides for a grace period for the plan year ending in 2022, the grace period would allow a participant to use all unused amounts remaining at the end of the plan year ending in 2022 for expenses incurred during the first two and one-half months of the plan year ending in 2023. For a plan that provides for a carry over for the plan year ending in 2022, the carryover would allow the participant to use up to $550 (or, if greater, 20 percent of the indexed contribution limit under § 125(i)) of unused amounts remaining at the end of the 2022 plan year for expenses incurred during any month of the plan year ending in 2023. In accordance with the otherwise applicable rules, for plan years ending in or after 2022, the carryover is available only for a health FSA and is not available for a dependent care assistance program. The following examples illustrate the application of these rules and assume that the applicable carryover limit continues to be $550 for all relevant periods:

Example 1. Employer provides a health FSA under a calendar year § 125 cafeteria plan that allows a $550 carryover from one plan year to the next. Pursuant to § 214 of the Act, Employer amends the plan to adopt a 12-month temporary extended period for incurring claims with respect to the 2020 plan year, allowing for claims incurred on or after January 1, 2021, but prior to January 1, 2022, to be paid with amounts remaining from the 2020 plan year.

[15] An employer also may choose to adopt one type of relief, or no relief, under § 214 of the Act for a health FSA and a different type of relief, or no relief, for a dependent care assistance program. An employer that offers multiple health FSAs or dependent care assistance programs may also adopt differing relief for each particular health FSA or dependent care assistance program.

As of December 31, 2020, Employee A has a remaining balance of $2,000 in a health FSA for the 2020 plan year. For the 2021 plan year, Employee A elects to contribute $2,000 to a health FSA. Between January 1, 2021 and December 31, 2021, Employee A incurs $3,300 in medical care expenses. The health FSA may reimburse Employee A $3,300, leaving $700 in the health FSA as of December 31, 2021.

Pursuant to § 214 of the Act, Employer amends the plan to adopt the temporary extended period for incurring claims with respect to the 2021 plan year, allowing for claims incurred on or after January 1, 2022, but prior to January 1, 2023, to be paid with amounts remaining at the end of the 2021 plan year. For the 2022 plan year, Employee A elects to contribute $1,500 to a health FSA. Between January 1, 2022, and December 31, 2022, Employee A incurs $1,200 in medical care expenses. The health FSA may reimburse Employee A $1,200, leaving $1,000 in the health FSA as of December 31, 2022. Under the plan terms that provide for a $550 carryover from the 2022 plan year to the 2023 plan year, Employee A is allowed to use $550 of the remaining $1,000 in the health FSA during the 2023 plan year to reimburse expenses incurred on or after January 1, 2023, and before January 1, 2024. The $450 remaining as of December 31, 2022, is forfeited. A 2½ month grace period is not available for the plan year ending December 31, 2023, because the plan provides for a carryover.

Example 2. Employer provides a health FSA under a non-calendar year (July 1 to June 30) § 125 cafeteria plan that allows a $550 carryover from one plan year to the next. Pursuant to § 214 of the Act, Employer amends the plan to adopt a 12-month temporary extended period for incurring claims with respect to the 2020 plan year, allowing claims incurred on or after July 1, 2021, but prior to July 1, 2022, to be paid with amounts from the 2020 plan year (which ends on June 30, 2021).

For the 2020 plan year, Employee B elects to contribute $1,800 to a health FSA. As of June 30, 2021, Employee B has a remaining balance in the health FSA for the 2020 plan year of $1,800. For the 2021 plan year, Employee B elects to contribute $1,000 to a health FSA. Between July 1, 2021, and June 30, 2022, Employee B incurs $2,000 in medical care expenses. The health FSA may reimburse Employee B $2,000, leaving $800 in the health FSA as of June 30, 2022. Under the plan terms that provide for a carryover, Employee B is allowed to use $550 of the remaining $800 in the health FSA during the 2022 plan year to reimburse expenses incurred on or after July 1, 2022, but prior to July 1, 2023. The $250 remaining as of June 30, 2022, is forfeited. A 2½ month grace period is not available for the plan year ending June 30, 2022, because the plan provides for a carryover.

Example 3. Employer provides a dependent care assistance program under a calendar year § 125 cafeteria plan. Pursuant to § 214 of the Act, Employer amends the plan to adopt a 12-month temporary extended period for incurring claims with respect to the 2020 plan year, allowing for claims incurred on or after January 1, 2021, but prior to January 1, 2022, to be paid with amounts remaining from the 2020 plan year.

As of December 31, 2020, Employee C has a remaining balance of $4,000 in a dependent care assistance program for the 2020 plan year. For the 2021 plan year, Employee C elects to contribute $3,000 to a dependent care assistance program. Between January 1, 2021, and December 31, 2021, Employee C incurs $6,000 in dependent care expenses. The dependent care assistance program may reimburse Employee C $6,000, leaving $1,000 in the dependent care assistance program as of December 31, 2021.

Pursuant to § 214 of the Act, Employer amends the plan to adopt a 12-month temporary extended period for incurring claims with respect to the 2021 plan year, allowing for claims incurred on or after January 1, 2022, but prior to January 1, 2023, to be paid with amounts remaining at the end of the 2021 plan year. For the 2022 plan year, Employee C elects to contribute $2,000 to a dependent care assistance program. Between January 1, 2022, and December 31, 2022, Employee C incurs $2,800 in dependent care expenses. The dependent care assistance program may reimburse Employee C $2,800, leaving $200 in the dependent care assistance program as of December 31, 2022. A carryover is not available for a dependent care assistance program from the 2022 plan year to the 2023 plan year. Employer adopts a 2½ month grace period for the 2022 plan year, during which the $200 remaining as of December 31, 2022, may be applied to reimburse dependent care expenses incurred during the grace period.

D. Special Age Limit Relief Applicable to Carryover Relief for Dependent Care Assistance Programs

Section 214(d)(1) of the Act provides that in the case of certain employees, § 21(b)(1)(A) of the Code shall be applied by substituting ''age 14'' for ''age 13'' for purposes of determining the dependent care assistance which may be paid or reimbursed during (A) the last plan year with respect to which the end of the regular enrollment period for such plan year was on or before January 31, 2020, and (B) in the case of an employee who has an unused balance in a dependent care assistance program for such plan year (determined as of the close of the last day on which, under the terms of the plan, claims for reimbursement may be made with respect to such plan year), the subsequent plan year.[16] Regarding the subsequent plan year, § 214(d)(2) of

the Act provides that § 214(d)(1) shall only apply to so much of the amounts paid for dependent care assistance with respect to the dependents referred to in § 214(d)(3)(B)(ii) as does not exceed the unused balance described in § 214(d)(3)(B)(ii).

Only certain employees are eligible for this relief. Section 214(d)(3) of the Act provides that, for purposes of this relief, the term ''eligible employee'' means any employee who (A) is enrolled in a dependent care assistance program for the last plan year with respect to which the end of the regular enrollment period for the plan year was on or before January 31, 2020, and (B) has one or more dependents (as defined in § 152(a)(1) of the Code) who attain the age of 13 either (i) during that plan year, or (ii) in the case of an employee who (after the application of § 214 of the Act) has unused dependent care amounts for that plan year (determined as of the close of the last day on which, under the terms of the plan, claims for reimbursement may be made with respect to that plan year), during the subsequent plan year. Thus, an employer, in its discretion, may amend one or more of its § 125 cafeteria plans[17] in accordance with § 214(d) of the Act.[18]

This special age limit relief for certain dependents is separate from the general carryover and extended claims periods relief available under § 214(a), (b) and (c) of the

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[16] Section 129(a) generally excludes from an employee's gross income amounts paid or incurred by the employer for "dependent care assistance" provided to the employee if the assistance is furnished pursuant to a dependent care assistance program. Section 129(e) provides that "dependent care assistance" means the payment of, or provision of, those services, which if paid for by the employee would be considered employment-related services under § 21(b)(2). Generally, and assuming the requirements of §§ 21 and 129 otherwise are satisfied, "dependent care assistance" includes expenses incurred for the care of a dependent child who is under age 13 that enable an employee to be gainfully employed.

[17] References in this notice to amendments to § 125 cafeteria plans include any necessary amendments to plans under § 129, as applicable.

[18] Without regard to § 214 of the Act, employers are permitted to limit reimbursable expenses to expenses incurred for the care of a dependent child who is under age 13 or who is under a specified age that is less than age 13.

Act. An employer that adopts the special age limit relief provided in § 214(d)(3)(B)(ii) of the Act is *not* required to adopt the carryover provided in § 214(a) of the Act or an extended period for incurring claims (for example, the relief provided in § 214(c)(1) of the Act) in order to adopt the special age limit relief. Thus, an employer, in its discretion, may amend one or more of its § 125 cafeteria plans to adopt any or all of the relief provided in § 214 of the Act, and an employer that adopts any or all of the relief provided in § 214(a), (b) and (c) of the Act is not required to adopt the special age limit relief provided in § 214(d) of the Act, and vice-versa.

If an employer sponsors a § 125 cafeteria plan with a dependent care assistance program and amends the plan to substitute "under age 14" for "under age 13" for purposes of determining the dependent care assistance expenses that may be paid or reimbursed, then all amounts from the most recent plan year with respect to which the end of the regular enrollment period was on or before January 31, 2020, may be applied to dependent care expenses for a dependent who attained age 13 during that plan year. In addition, employers may allow employees to carry over all unused amounts from that plan year (the first plan year) to reimburse dependent care expenses during the subsequent plan year for a dependent that attained age 13 during the first plan year (until that dependent attains age 14) and for a dependent who attains age 13 during the subsequent plan year. This special age limit relief for dependent care assistance programs does not apply to any unused amounts carried over from the subsequent plan year. This special age limit relief rule also does not permit an employer to reimburse expenses for a child who is age 14 years or older.

Example 1. Employer provides a dependent care assistance program under a § 125 cafeteria plan with a non-calendar plan year. The regular enrollment period for the 2020 plan year (March 1, 2020, through February 28, 2021) ended on January 31, 2020. Employee elected to enroll in the dependent care assistance program for the 2020 plan year, electing to contribute the maximum $5,000 allowed. Employee's Dependent turns age 13 on February 1, 2021. As of January 31, 2021, Employee has incurred no qualifying expenses for the 2020 plan year. However, Employee anticipates incurring dependent care expenses during February 2021, which is during the 2020 plan year.

Employer amends its § 125 cafeteria plan by substituting "under age 14" for "under age 13" for the 2020 and 2021 plan years, making that change applicable to all amounts permitted under § 214(d) of the Act, and does not adopt any other relief provided by § 214 of the Act. Employee incurs $5,000 in dependent care expenses in February 2021 for Dependent, who at that time is age 13. The $5,000 in dependent care expenses may be reimbursed by the dependent care assistance program for the 2020 plan year.

Example 2. Employer provides a dependent care assistance program under a § 125 cafeteria plan with a non-calendar plan year. The regular enrollment period for the 2020 plan year (March 1, 2020, through February 28, 2021) ended on January 31, 2020. Employee elected to enroll in the dependent care assistance program for the 2020 plan year, electing to contribute $4,000. Employee's Dependent turns age 13 on February 1, 2021. As of January 31, 2021, Employee has incurred no qualifying expenses for the 2020 plan year. However, Employee anticipates incurring dependent care expenses during the summer of 2021, which is during the 2021 plan year.

Employer amends its § 125 cafeteria plan to adopt the relief provided by § 214(d) of the Act by substituting "under age 14" for "under age 13" for the 2020 and 2021 plan years, making that change applicable to all amounts permitted under § 214(d) of the Act. Employer allows employees until the end of the next plan year to incur claims and does not adopt any other relief provided by § 214 of the Act. Employee elects to contribute $500 for the 2021 plan year. Employee incurs $4,200 in dependent care expenses from June through August 2021 for Dependent, who during that time is age 13. For the 2021 plan year (March 1, 2021, through February 28, 2022), $4,000 of the $4,200 in dependent care expenses may be reimbursed by the dependent care assistance program for Dependent. ($4,000 is the unused amount from the 2020 plan year that may be applied to reimburse dependent care expenses during the subsequent plan year for a dependent that attained age 13 during the preceding plan year, until that dependent attains age 14, so the remaining $200 in dependent care expenses for Dependent may not be reimbursed.) Employee does not incur any other dependent care expenses during the 2021 plan year. The $500 remaining in the dependent care assistance program as of February 28, 2022, is forfeited.

E. Elections Under a § 125 Cafeteria Plan

Section 214 of the Act provides that § 125 cafeteria plans may permit employees to make prospective mid-year election changes for health FSAs and dependent care assistance programs for plan years ending in 2021. Specifically, § 214(e) of the Act provides that for plan years ending in 2021, a plan that includes a health FSA or dependent care assistance program shall not fail to be treated as a cafeteria plan merely because the plan or arrangement allows an employee to make an election to modify prospectively the amount (but not in excess of any applicable dollar limitation) of the employee's contributions to the arrangement (without regard to any change in status). Thus, an employer, in its discretion, may amend one or more of its § 125 cafeteria plans to allow each employee who is eligible to make salary reduction contributions under the plan to make prospective election changes for plan years ending in 2021 regarding a health FSA or dependent care assistance program, regardless of whether the basis for the election change satisfies the criteria set forth in Treas. Reg. § 1.125-4. In particular, subject to the limitations discussed later in this section, an employer may amend one or more of its § 125 cafeteria plans to allow employees, on a prospective basis, to (1) revoke an election, make one or more elections, or increase or decrease an existing election, for plan years ending in 2021 regarding a health FSA, or (2) revoke an election, make one or more elections, or increase or decrease an existing election, for plan years ending in 2021 regarding a dependent care assistance program. Prospective election changes may include an initial election to enroll in a health FSA or dependent care assistance program for the year, for example, to gain use of the § 214 carryover or extended period for incurring claims pursuant to § 214 of the Act if the employee initially declined to enroll in the health FSA or dependent care assistance

program for the year. An employer adopting this relief may limit the period during which election changes may be made.

In addition, similar to relief provided by Notice 2020-29, an employer may amend one or more of its § 125 cafeteria plans to allow employees to: (1) make a new election for employer-sponsored health coverage[19] on a prospective basis, if the employee initially declined to elect employer-sponsored health coverage; (2) revoke an existing election for employer-sponsored health coverage and make a new election to enroll in different health coverage sponsored by the same employer on a prospective basis (including changing enrollment from self-only coverage to family coverage);[20] (3) revoke an existing election for employer-sponsored health coverage on a prospective basis, provided that the employee attests in writing that the employee is enrolled, or immediately will enroll, in other health coverage not sponsored by the employer.

To accept an employee's revocation of an existing election for employer-sponsored health coverage when the employee does not make a new election to enroll in different health coverage sponsored by the employer, the employer must receive from the employee an attestation in writing that the employee is enrolled, or immediately will enroll, in other comprehensive health coverage not sponsored by the employer.[21] The employer may rely on the written attestation provided by the employee, unless the

[19] The term "health coverage" in this notice refers to health, dental, or vision coverage.
[20] The ability to amend a plan to allow an employee to revoke an existing election for employer-sponsored health coverage and make a new election to enroll in different health coverage sponsored by the same employer may include allowing employees to change from one type of health plan (such as a health maintenance organization (HMO)) to another (such as a preferred provider organization (PPO)). An employer also may choose to limit the ability of employees to change from one type of health plan to another. For example, an employer may choose to restrict the election to allow employees to change only from a narrow network plan to a broader network plan or to allow only employees who previously elected a particular plan to elect to move to a different plan.
[21] An employee revoking an existing election for comprehensive health coverage may not revoke the election by attesting to enrollment in coverage solely for dental or vision benefits.

employer has actual knowledge that the employee is not, or will not be, enrolled in other comprehensive health coverage not sponsored by the employer. The following is 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: _____

An employer using the relief provided under § 214(e) of the Act and this notice is not required to provide unlimited election changes but may, in its discretion, determine the extent to which election changes are permitted, provided that any permitted election changes are applied on a prospective basis only (with the exception of elections related to previously contributed amounts as part of the relief provided under § 214(a), (b) and (c)(1) of the Act, as discussed elsewhere in this section III.E.). In addition, except for changes in election requirements that, pursuant to § 214(a), (b), (c) and (d) of the Act, allow employees to carry over amounts, have amounts available during an extended claims period, or have amounts available to reimburse dependent care expenses for certain dependents who attain age 13, as described in sections III.A. through D. of this notice, any change to the plan's election requirements may not result in the failure of the plan to comply with the nondiscrimination rules applicable to § 125 cafeteria plans. In

determining the extent to which election changes are permitted and applied, an employer may wish to consider the potential for adverse selection of health coverage by employees. To prevent this result, an employer may wish to limit elections to circumstances in which an employee's coverage will be increased or improved as a result of the election (for example, by electing to switch from self-only coverage to family coverage, or from a low option plan covering in-network expenses only to a high option plan covering expenses in or out of network).

With respect to mid-year election changes for employer-sponsored coverage, this relief applies both to employers sponsoring self-insured plans and to employers sponsoring insured plans. With respect to health FSAs, this relief applies to all health FSAs, including HSA-compatible health FSAs. In addition, with respect to health FSAs and dependent care assistance programs, employers are permitted to limit mid-year election changes to amounts no less than amounts already reimbursed and to certain types of mid-year election changes, such as decreases in elections only. Employers also are permitted to allow mid-year election changes without a status change[22] up to a certain date during the plan year but require a status change after that date (for example, no status change is required if an election is changed before March 31, 2021, but a status change is required if an election is changed after that date), and to limit the number of election changes during the plan year that are not associated with a status change (for example, allow only one election change in the 2021 plan year without a status change). Although salary reductions may be applied only prospectively under any revised election, employers may allow amounts contributed to the health FSA or

[22] See Treas. Reg. § 1.125-4.

dependent care assistance program after the revised election to be used for any medical care expense or dependent care expense, respectively, incurred during the first plan year that begins on or after January 1, 2021, through the end of the 2021 plan year. This relief extends to expenses incurred by employees who were not enrolled in the health FSA or dependent care assistance program on January 1, 2021. This relief does not allow unused amounts to be paid to an employee in cash or paid to an employee in the form of any taxable or nontaxable benefit without regard to whether the employee incurs medical care expenses or dependent care expenses during the period of coverage.

If an employer adopts the § 214 carryover or the extended period for incurring claims permitted by § 214(c)(1) of the Act, the annual limits under §§ 125(i) and 129(a) apply to amounts contributed to a health FSA or dependent care assistance program for a particular year, and not to amounts reimbursed or otherwise available for reimbursement from a health FSA or dependent care assistance program in a particular plan or calendar year. Thus, unused amounts carried over from prior years or available during an extended period for incurring claims are not taken into account in determining the annual limit applicable for the following year.

If a health FSA or dependent care assistance program election is revoked, the treatment of amounts previously contributed to a § 125 cafeteria plan on a pre-tax basis to fund a health FSA or dependent care assistance program are subject to the terms of the plan, which must apply uniformly to all participants in the plan. The plan may provide that amounts contributed before the election is revoked remain available to reimburse medical care expenses or dependent care expenses incurred for the rest of

the plan year. Alternatively, the plan may provide that if the election is revoked, amounts contributed before the revocation will be available only to reimburse eligible expenses incurred before the revocation takes effect (and not later incurred expenses), or that amounts contributed before the revocation will be forfeited. An employer, in its discretion, may allow employees to elect to revoke elections under a health FSA or dependent care assistance program as of a future specified date.

Regarding health FSAs, if the plan provides that revocation of the election terminates participation in the health FSA, and that no subsequent reimbursements will be available under the health FSA regardless of when the expense is incurred, following the revocation, the health FSA will no longer be treated as health coverage that disqualifies an otherwise eligible individual from contributing to an HSA. In that case, an otherwise eligible individual may begin contributing to an HSA as soon as the termination of participation (including the lack of continued availability of reimbursements in the health FSA) is effective. Similarly, if under the terms of the plan, the health FSA reimburses only expenses incurred before the date of the revocation, following the revocation, the health FSA will not be treated as health coverage that disqualifies an otherwise eligible individual from contributing to an HSA for months after the date of the revocation and an otherwise eligible individual may begin contributing to an HSA.

Example 1. During the regular enrollment period for the 2021 calendar plan year, employee elects to contribute $1,200 to a health FSA for the year. The plan allows the employee to revoke or change the election by March 1, 2021. The employee makes a prospective election to revoke the election effective March 1, at which time the employee has contributed $200 to the health FSA. Under the terms of the plan, amounts contributed before the revocation of the election remain available to reimburse medical care expenses incurred for the rest of the plan year and, therefore, the

employee may use the $200 previously contributed to the health FSA to reimburse medical care expenses incurred throughout 2021. Consequently, the employee has coverage by the health FSA for 2021 and will not be eligible to contribute to an HSA for calendar year 2021 even if otherwise eligible (that is, covered by an HDHP), unless the plan allows the employee to opt out of this extended period for incurring claims, and the employee opts out of this period.

Example 2. During the regular enrollment period for the 2021 calendar plan year, Employee elects to contribute $1,200 to a health FSA for the year. The plan allows the employee to revoke or change the election by March 1, 2021. The employee makes a prospective election to revoke the election effective March 1, at which time the employee has contributed $200 to the health FSA. Under the terms of the plan, revocation of the election means that the employee may use the $200 that was contributed to the health FSA prior to March 1 to reimburse only medical care expenses incurred prior to March 1. The coverage during January and February will not make the employee ineligible to contribute to an HSA during the rest of the plan year if otherwise eligible.

F. Changes Between HSA-compatible and General Purpose Health FSAs and HSA Contributions

Under the relief provided by this notice and § 214 of the Act, § 125 cafeteria plans may be amended to allow an employee to make a mid-year election to be covered by a general purpose health FSA for part of the year and an HSA-compatible health FSA for part of the year.[23] Eligibility to contribute to an HSA is determined on a month-by-month basis under § 223 of the Code. If an employee begins the year with an HSA-compatible health FSA and is otherwise an eligible individual under § 223(c)(1) and then elects coverage under a general purpose health FSA, the employee's permissible HSA contribution is based on the number of months that the employee was covered under the HSA-compatible health FSA and an HDHP and was otherwise an eligible individual.

[23] In addition, employers are permitted to amend their plans to offer employees a choice between an HSA-compatible health FSA or general purpose health FSA during the period to which the § 214 carryover or the extended period for incurring claims applies, on an employee-by-employee basis. Also, employers are permitted to implement a plan design in which employees who elect an HDHP are automatically enrolled in an HSA-compatible health FSA. To the extent changes result in an employee being ineligible for an HSA mid-year on a prospective basis, the employee would not be rendered HSA-ineligible for the earlier part of the plan year.

Only those expenses both allowed by the HSA-compatible health FSA and incurred during the months in which the employee was covered by the HSA-compatible health FSA may be reimbursed by that health FSA. Although unused amounts in the HSA-compatible health FSA may be added to the general purpose health FSA, the general purpose health FSA may reimburse only allowable medical care expenses incurred after the change in coverage.

If an employee begins the year with a general purpose health FSA and then elects coverage by an HDHP and an HSA-compatible health FSA, the employee's permissible HSA contribution is based on the number of months that the employee is an eligible individual.[24] Any allowable medical care expense incurred during the months before the change in coverage may be reimbursed by the general purpose health FSA. Although unused amounts in the general purpose health FSA may be added to the HSA-compatible health FSA, only expenses both allowed by the HSA-compatible health FSA and incurred during months after the change in coverage may be reimbursed by the HSA-compatible health FSA.

Finally, if an employee is covered under an HDHP at the beginning of the plan year without a health FSA and then elects coverage by a plan that is not an HDHP and coverage by a health FSA that can be used to reimburse medical expenses incurred while the employee was covered by the HDHP, the health FSA must be operated as an HSA-compatible health FSA for the months that the employee was otherwise an eligible individual under § 223(c)(1) in order for the employee to contribute to an HSA with

[24] Alternatively, pursuant to § 223(b)(8), an employee that is an eligible individual during the last month of the year will be treated for purposes of the HSA contribution limitation as having been an eligible individual for the entire year, even if the individual was not otherwise an eligible individual for the entire year, provided, generally, that the eligible individual remains an eligible individual (including through enrollment in an HDHP) for the entire next year.

respect to those months. Therefore, only the expenses both allowed by an HSA-compatible health FSA and incurred during those months before the change may be reimbursed. For months after the change in coverage, the health FSA may be operated as a general purpose health FSA and may reimburse any allowable medical care expense incurred during that later period.

In each of these cases, the maximum reimbursements for the combined health FSAs for the year are limited to the amount of salary reduction elected for the year (subject to the $2,750 limit under § 125(i) of the Code (as indexed)) plus any available unused amounts from prior years (including unused amounts carried over or available due to plan amendments under § 214 of the Act) and any nonelective employer contributions.

G. Interaction with COBRA

In certain circumstances, § 4980B permits qualified beneficiaries who lose coverage under a group health plan, including under a health FSA, to elect continuation health coverage under the Consolidated Omnibus Budget Reconciliation Act of 1985 (COBRA continuation coverage). See Treas. Reg. § 54.4980B-2, Q&A 8. For COBRA purposes, a qualified beneficiary generally includes the covered employee, the spouse of the covered employee, or the dependent child of the covered employee, if the employee had coverage under the plan on the day before the employee experiences a qualifying event and would have a loss of coverage but for the COBRA continuation coverage. See § 4980B(g) and Treas. Reg. § 54.4980B-3, Q&A 1. For COBRA purposes, a qualifying event includes certain events, such as the termination of the employee or a reduction of hours, that would result in a loss of coverage but for the

COBRA continuation coverage, and a loss of coverage means ceasing to be covered under the same terms and conditions as in effect immediately before a qualifying event. See § 4980B(f)(3) and Treas. Reg. § 54.4980B-4, Q&A 1. If an individual is otherwise a qualified beneficiary with respect to coverage by a health FSA, a limited extension of coverage to the individual pursuant to § 214(c)(2) of the Act will not prevent the individual from having a loss of coverage resulting in a qualifying event (for example, by termination of employment or reduction in hours of a covered employee), and the relevant employer will be required to provide a notice of the right to elect COBRA continuation coverage to the individual.[25]

For example, if an employer allows an employee who ceases to be a participant as the result of termination of employment or change in employment status to be reimbursed for expenses incurred after the termination or reduction in hours through access to the amount of salary reduction contributions that have been made as of the date the employee ceased being a participant, this event would constitute a COBRA qualifying event subject to notice requirements. As a further example, if an employee elected to contribute $2,400 to a health FSA, terminated employment on January 31 after making $200 in salary reduction contributions, and as a result of the termination was no longer permitted to contribute to the health FSA other than by electing COBRA continuation coverage, the employer may allow the employee to request reimbursement for up to $200, or the employee may elect COBRA continuation coverage to have

[25] An individual who ceases to be covered by a health FSA due to an election to revoke participation in a health FSA, while qualifying for the limited extension of coverage pursuant to § 214(c)(2) of the Act, would not have a qualifying event satisfying the requirement to be a qualified beneficiary. See Treas. Reg. § 54.4980B-4, Q&A 1.

access to $2,400 by paying the applicable COBRA premium of $200 per month on an after-tax basis.

Nonetheless, regardless of whether an individual is offered or elects COBRA continuation coverage, if an employer allows the individual the limited extension of coverage pursuant to § 214(c)(2) of the Act, the health FSA may reimburse expenses incurred after the termination of participation and through the end of the plan year. The health FSA also may reimburse expenses incurred during any period to which unused amounts are carried over or during any grace period provided under the plan.

Additionally, if an employer adopts a § 214 carryover or extended period for incurring claims pursuant to § 214(c)(1) of the Act, the maximum amount that a health FSA may require to be paid as the applicable COBRA premium does not include unused amounts carried over or available during the extended period for incurring claims. Thus, if a qualified beneficiary is allowed a § 214 carryover to a later plan year or an extended period for incurring claims, the applicable COBRA premium payable to provide access to the carryover amounts or the amounts attributable to the extended period for incurring claims for that later year or for the extended period for incurring claims is zero. See Q&A 23 of Notice 2015-87. In addition, amounts carried over or available during the extended period for incurring claims are included in the amount of the benefit that a qualified beneficiary is entitled to receive during the remainder of a plan year in which a qualifying event occurs. See Q&A 21 of Notice 2015-87.

Finally, notwithstanding the special rule of § 214(c)(2) of the Act, an employer is not required to allow individuals who cease participation in the plan to continue to receive reimbursements from unused benefits in a health FSA if the individual does not

qualify for and elect COBRA continuation coverage. An employer is not obligated to amend its plan to make the relief permitted under § 214(c)(2) of the Act available to all employees. Instead, employees for whom the extension of coverage under § 214(c)(2) of the Act is unavailable remain eligible to elect COBRA, as do employees for whom the extended coverage is available.

H. Plan Amendments

An employer that decides to implement the relief provided under § 214 of the Act for one or more of its § 125 cafeteria plans (including plans that do not currently have a grace period or permit a carryover) must adopt a plan amendment to do so. Section 214(g) of the Act provides that a plan that includes a health FSA or dependent care assistance program shall not fail to be treated as a cafeteria plan merely because the plan or arrangement is amended pursuant to a provision under § 214 of the Act and the amendment is retroactive, if (1) the amendment is adopted not later than the last day of the first calendar year beginning after the end of the plan year in which the amendment is effective, and (2) the plan or arrangement is operated consistent with the terms of the amendment during the period beginning on the effective date of the amendment and ending on the date the amendment is adopted. For example, if an employer sponsors a calendar year § 125 cafeteria plan with a health FSA that provides for a $550 carryover (from 2020 to 2021) and amends the plan to carry over the entire unused amount remaining in employees' health FSAs as of December 31, 2020, to the 2021 plan year, the amendment must be adopted by December 31, 2021. An amendment for the 2020 plan year of a non-calendar year plan, however, must be

adopted by December 31, 2022, because the last day of the first calendar year beginning after the end of the 2020 plan year that ends in 2021 is the last day of 2022.

An amendment pursuant to § 214 and this notice may be effective retroactively to the beginning of the applicable plan year, provided that the § 125 cafeteria plan operates in accordance with the terms of the amendment during the period beginning on the effective date of the amendment and ending on the date the amendment is adopted, and the employer informs all employees eligible to participate in the § 125 cafeteria plan of the changes to the plan. Changes to the plan may also implicate requirements under other applicable laws, such as notice requirements under Title I of the Employee Retirement Income Security Act of 1974. Except for amendments that, pursuant to § 214(a), (b), (c), and (d) of the Act, allow employees to carry over amounts, have amounts available during an extended claims period, or have amounts available to reimburse dependent care expenses for certain dependents who attain age 13, as described in sections III.A. through D. of this notice, all permissible amendments are subject to the nondiscrimination rules under §§ 125 and 129 of the Code.

I. Reporting Requirements for Dependent Care Assistance Programs

With respect to Form W-2, "Wage and Tax Statement," amounts contributed to a dependent care assistance program are required to be reported in Box 10 of Form W-2. Under current guidance (Notice 2005-61, 2005-39 IRB 607), employers may report in Box 10 for a year the salary reduction amount elected by the employee for the year for dependent care assistance (plus any employer matching contributions) and are not required to adjust the amount reported in Box 10 to take into account amounts that remain available in a grace period. This rule continues to apply with respect to

employers who amend their § 125 cafeteria plans to provide for the temporary flexibility provided by § 214 of the Act. For this purpose, any amount carried forward from 2019 and used in 2020, whether a § 214 carryover or an extended period for incurring claims, is treated as an amount that remains available in a grace period. With respect to Form 2441, "Child and Dependent Care Expenses," any amounts carried forward from 2019 are similarly treated as amounts carried over and used during the grace period when completing Part III of the form. The Treasury Department and the IRS anticipate that for the 2021 and 2022 Forms W-2 and 2441, instructions will provide for similar rules that dependent care amounts carried forward from prior years pursuant to § 214 of the Act will be treated as amounts remaining available during a grace period for reporting purposes and no change to the reporting requirements will be necessary.

IV. GUIDANCE RELATED TO SECTION 3702 OF THE CARES ACT

Section 3702 of the CARES Act amended the Code to allow expenses incurred for menstrual care products to be treated as incurred for medical care with respect to health FSAs and HRAs, as well as HSAs and Archer medical savings accounts (MSAs). In addition, the provision allows health FSAs and HRAs, as well as HSAs and Archer MSAs, to reimburse expenses incurred for over-the-counter drugs without regard to whether the drug has been prescribed. As enacted, the expansion applies to expenses incurred after December 31, 2019.[26]

[26] Section 3702 of the CARES Act amends §§ 220, 223 and 106 of the Code. In addition to removing statutory language at §§ 220(d), 223(d) and 106(f) of the Code which limited the excludable expenses under those provisions to prescribed drugs and insulin, § 3702(a) and (b) of the CARES Act amended §§ 220 and 223 of the Code to provide that for purposes of Archer MSAs and HSAs, amounts paid for menstrual care products shall be treated as paid for medical care. Similarly, § 3702(c) of the CARES Act adds a new subsection (f) to § 106 of the Code providing that, for purposes of §§ 106 and 105 of the Code, expenses incurred for menstrual care products are treated as incurred for medical care.

Generally, the exclusion under § 105(b) for reimbursements of medical expenses by an employer applies only if the plan covered the expense on the date the expense was incurred. See Treas. Reg. § 1.105-5. Furthermore, Proposed Treasury Regulation § 1.125-1(c)(5), implementing § 125 of the Code, provides that amendments adding new benefits to a cafeteria plan may allow payment or reimbursement of expenses for those benefits only to the extent those expenses are incurred after the later of the amendment's adoption date or effective date. Notwithstanding the general rule under § 105(b), and notwithstanding any inconsistency with the proposed regulations under § 125, upon which taxpayers may rely prior to the issuance of final regulations, health FSAs and HRAs may be amended pursuant to this notice to provide for reimbursements of expenses for menstrual care products and over-the-counter drugs without prescriptions incurred for any period beginning on or after January 1, 2020, and such an amendment will not result in a failure of the reimbursement to be excludable from income under § 105(b) or for the cafeteria plan to fail to meet the requirements of § 125. This relief includes amendments made prior to the issuance of this notice.

V. DRAFTING INFORMATION

The principal author of this notice is Jennifer Solomon of the Office of Associate Chief Counsel (Employee Benefits, Exempt Organizations, and Employment Taxes), though other Treasury Department and IRS officials participated in its development. For further information on the provisions of this notice, contact Jennifer Solomon at (202) 317-5500 (not a toll-free number).