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Addressing COVID-19 Disruption in Health Flexible Spending Arrangements, Dependent Care Assistance Plans, and Health Reimbursement Arrangements

NEA members are increasingly concerned that they may lose money in their health flexible spending arrangement (health FSA), dependent care flexible spending arrangement (dependent care assistance plan, DCAP), or health reimbursement arrangement (HRA) when the HRA does not roll over from year to year. In some instances, that concern arises because the daycare center they use is closed due to COVID-19 or because they are now home and do not need the daycare center. In other cases, members remain enrolled in their employer's health coverage but the health care providers on which they planned to spend health FSA or HRA money is closed or only seeing patients on an emergency basis. In yet other cases, the ability to use account balances is questioned when a member is laid off or furloughed.

Broadly speaking, employees cannot change how much they elect, before the plan year, to set aside from their pay to fund their health FSA or DCAP. There are, however, certain circumstances in which mid-year changes are permitted. For HRAs, the issues are different, because HRAs cannot be funded with pre-tax dollars or through a cafeteria plan and because only employers are permitted to contribute funds to HRAs.

This document discusses the conditions under which employees can make mid-year election changes to their health FSA or DCAP. To simplify an already-complex topic, it doesn't address rules related to mid-year changes in employer health coverage. With respect to HRAs that do not include a rollover feature, there is no statutory or regulatory requirement that the plan year be 12 months long, like there is for health FSAs and DCAPs, so mid-year changes are not prohibited; as a result, the extent to which employer contributions to an HRA can be rolled over during COVID-19-related health care disruption is likely to come down to negotiations or other labor-management engagement.

Summary of mid-year FSA election changes

The regulatory requirements for mid-year election changes differ between health FSAs and DCAPs, although no mid-year election changes are mandatory for either. That is, a Section 125 cafeteria plan can allow some or all of the possible changes, but a health FSA or DCAP must expressly permit them if an employee is to be able to make any mid-year change. Most employers permit employees to change elections mid-year for any IRS-permitted reason. Some plans specifically list all the reasons, but others just refer to the IRS list. Very few employers pick and choose among IRS-permitted change events. In addition, plans that allow changes should have processes in place regarding how and when an employee must notify the plan about changes and the documentary requirements related to the need for the change.

National Education Association/Collective Bargaining and Member Advocacy Department

Ability to Make Mid-Year Election Changes in Health FSAs and Dependent Care Assistance Plans (DCAPs)

Change-in-Status Events

(Note: Any mid-year change is only permissible if allowed by the plan, and any status-related election change must be consistent with the event.)

	Health FSAs	Dependent Care Assistance Plans
No longer employed	Contributions cease so no mid-year election change needed	Contributions cease so no mid-year election change needed
Furloughed	Mid-year election change depends on plan language	Mid-year election change depends on plan language
Using leave to which the employee is otherwise entitled	If paid, mid-year election ability depends on plan language. If unpaid, can make a mid-year election change that is consistent with the reason for the leave	If paid, mid-year election ability depends on plan language. If unpaid, can make a mid-year election change that is consistent with the reason for the leave
Working from home	No mid-year election change	Can make a mid-year change if provider no longer needed or available
Change in residence	No mid-year election change	No mid-year election change
Taking a new job	Contributions cease so no mid-year election needed; could elect COBRA use of health FSA with continuation coverage	Contributions cease so no mid-year election needed
Using Family and Medical Leave Act benefits	Access to health FSA must be available but mid-year election change must also be available	Mid-year election change is permitted; contributions to DCAP can continue but reimbursements not permitted
Using emergency paid sick leave	No mid-year election change	No mid-year election change
Continuation coverage	Health FSA can continue at employee choice but no election change	DCAP cannot continue because there is no employee pay

Cost and Coverage Changes (if allowed by the plan)

	Health FSAs	Dependent Care Assistance Plans
Automatic changes for “insignificant” cost changes	No mid-year election change	Mid-year election change permitted
Significant cost changes	No mid-year election change	Mid-year election change permitted if conditions are satisfied
Loss of coverage	No mid-year election change	Mid-year election change permitted if no similar coverage is available

Health FSAs and DCAPs

The place to start the analysis of permissible mid-year health FSA and DCAP changes is not with rules regarding the circumstances that can lead to such changes. It is, rather, with whether the FSA allows any or all of the changes that regulations say could potentially be made.

1. Plan design issues related to mid-year changes

Cafeteria plan benefits must operate consistent with the terms of the plan (and, of course, consistent with applicable law and regulation). So, regardless of a member's changed circumstances due to COVID-19, those circumstances cannot lead to mid-year changes in a health FSA or DCAP if the plan does not allow such changes. Keep in mind that a particular plan can allow some but not all of the changes permitted in the regulations.¹

2. Change in status: Health FSAs and DCAPs

The regulations recognize six types of events that could lead to a permissible mid-year election change due to a change in status.² They apply to both health FSAs and DCAPs. For both health FSAs and DCAPs, the election change must be consistent with the event. Rather than explore each of the six, this document analyzes the one that is likely to be most relevant in the context of disruption caused by COVID-19: a change in the employment status of the employee, the employee's spouse, or the employee's dependent.

The regulations define permissible mid-year election changes related to employment status this way:

A termination or commencement of employment; a strike or lockout; a commencement of or return from an unpaid leave of absence; and a change in worksite. In addition, if the eligibility conditions of cafeteria plan or other employee benefit plan of the employer of the employee, spouse, or dependent depend on the employment status of that individual and there is a change in that individual's employment status with the consequence that the individual becomes (or ceases to be) eligible under the plan, then that change constitutes a change in employment under this paragraph (e.g., if a plan only applies to salaried employees and an employee switches from salaried to hourly-paid with the consequence that the employee ceases to be eligible for the plan then that change constitutes a change in employment status under this paragraph (c)(2)(iii)).³

¹ In laying out the types of changes that could potentially be made mid-year, the regulations indicate, "Section 125 does not require a cafeteria plan to permit any of these changes" (26 CFR section 1.125-4(a)). Consistent with that language, the Office of the Chief Counsel of the Internal Revenue Service noted in a 2019 letter related to a dependent care assistance plan: "A plan is not required to permit an employee to revoke or make a new election outside of the enrollment period if the employee experiences a significant change in coverage or a significant increase or decrease in the cost of coverage" (<https://www.irs.gov/pub/irs-wd/19-0028.pdf>).

² These six types of event are changes in status for purpose of mid-year election changes: legal marital status; number of dependents; employment status; dependent satisfies or ceases to satisfy eligibility requirements; residence; and adoption assistance (26 CFR section 1.125-4(c)(2)).

³ 26 CFR section 1.125-4(c)(2)(iii).

Whether a COVID-19-related change in employment status allows a member to change a health FSA or DCAP election mid-year depends on what the change is.

- **No longer employed.** If a member is laid off or otherwise no longer employed, there would be no more salary; as a result, no additional salary reduction could take place. Funds still available in a health FSA at the time of severance from work can be used with continuation coverage (subject to continuation coverage rules and if such coverage is available); DCAP funds revert to the employer, minus any outstanding claims. Upon being hired or rehired, the member would be eligible to make a new election.
- **Furloughed.** If a member is furloughed (required to take unpaid leave), the ability to make a mid-year election change to a health FSA depends on whether the health plan permits furloughed workers to participate in the health plan and on whether the health FSA permits continued participation in that situation. If access to the employee's employer plan is not possible, funds still available in a health FSA at the time of furlough could be used with continuation coverage (if available) or with a spouse's employer's plan. For a DCAP, the plan language will govern; if permitted by the plan, DCAP funds will remain available for use. Upon the end of the furlough, a member who made an election change because of the furlough would be eligible to make a new election.
- **Using medical leave or other leave benefits to which the member is otherwise entitled.** A commencement or return from an unpaid leave of absence is a change-in-status event allowing a member to change their election to a health FSA or DCAP as long as the change is consistent with the reason for the leave. A member using paid medical, vacation, or other leave could remain eligible for the employer's health FSA, as long as the health plan document and health FSA plan documented permitted enrollment for those types of leave; a member would remain eligible for the DCAP as long as the plan document permitted it.
- **Working from home.** Members who are working at home would not have a change-in-status event for FSAs, because the change in worksite does not affect eligibility under the FSA.⁴ However, working at home would be a change-in-status event for a DCAP program, because the childcare may no longer be needed. Similarly, a school being closed will also allow a change in status because the childcare provider is no longer available.
- **Change in residence.** Regulations also permit election changes for health plans for a change in residence, which could arise in the context of quarantine and self-isolation, but, while eligibility for an employer health plan might change due to a COVID-19-related residence change,⁵ eligibility for the employer's FSA would not similarly change. As a result, a change in residence due to COVID-19 disruption would not create the option for a change in the health FSA or DCAP election.

⁴ 26 CFR section 1.125-4(c)(4), example 4.

⁵ This could happen, for example, if a member moves outside the service area of a health maintenance organizations (HMO).

- **Taking a new job.** If a member takes a new job, health FSA and DCAP funds accumulated during the previous employment would revert to the previous employer, minus outstanding claims. A mid-year election change would, then, be irrelevant. However, the member would have the ability to elect continuation coverage for the health FSA (if available) if staying with the former employer’s plan through continuation coverage.
- **Using Family and Medical Leave Act (FMLA) leave.** For employees working for employers subject to FMLA, continued access to a health FSA is required. If using paid leave during FMLA, coverage would continue as it did before FMLA. If on unpaid FMLA leave, an employee must be allowed to revoke coverage or discontinue paying into the health FSA during the leave.⁶ Employees must also be allowed to prepay their FSA contributions for the time they will be on FMLA leave.⁷ DCAPs are different, as their purpose is “to enable the taxpayer to be gainfully employed,”⁸ so they can only be used for temporary absences from work, such as for a vacation or short illness.⁹ Although a DCAP reimbursement would not be available while the person is still working, the employee may still make contributions to their DCAP. In addition, during an FMLA leave, the employee may elect a change in their DCAP contributions because they have experienced a change in status because they are no longer working and do not need the childcare.
- **Using emergency paid sick leave benefits under the Families First Coronavirus Response Act (FFCRA).** FFCRA, the second coronavirus response bill, signed on March 18, 2020, created an emergency paid sick leave benefit. If an employee qualifies for this benefit, health FSA and DCAP contributions would continue and would not be subject to mid-year election changes simply because emergency paid sick leave is used. Emergency paid sick leave benefits can only be used for a specific COVID-19 qualifying event, not simply because an employee is laid off or furloughed.¹⁰
- **Using continuation continuation benefits (benefits similar to those under the Consolidated Omnibus Budget Reconciliation Act, COBRA).** Health FSAs must continue for employees on continuation coverage, but employees can only make after-tax contributions at the rate originally selected, plus a potential administrative fee, once they are no longer receiving a paycheck. Such after-tax payments would be optional. DCAP contributions cannot continue because the

⁶ 26 CFR § 1.125-3, Q6/A6.

⁷ 26 CFR § 1.125-3, Q3/A3.

⁸ 26 CFR § 1.21-1(a)(1).

⁹ 26 CFR § 1.21-1(c)(2)(ii).

¹⁰ Qualifying events are if an employee: is subject to a federal, state, or local quarantine or isolation order related to coronavirus; has been advised by a health care provider to self-quarantine due to concerns related to coronavirus; is experiencing coronavirus symptoms and seeking a medical diagnosis; is caring for an individual who is subject to a federal, state, or local quarantine or isolation order related to coronavirus (or who has been advised by a health care provider to self-quarantine due to concerns related to coronavirus; is caring for a son or daughter if a school or place of care has been closed due to coronavirus, or the childcare provider of the son or daughter is unavailable due to coronavirus; is experiencing any other substantially similar condition specified by the Secretary of Health and Human Services in consultation with the Secretary of Labor and Secretary of the Treasury.

employee is not receiving pay; unused funds revert to the employer, minus outstanding claims.

3. Change in cost or coverage: DCAPs but not health FSAs

Regulations allow for mid-year election changes as a result of changes in cost or coverage, but not for health FSAs.¹¹ For DCAPs, mid-year election changes can be made in the following circumstances.

- **Automatic changes.** A DCAP can be structured to automatically change when costs increase or decrease (or increase) insignificantly. If a member would be required to change the amount paid because of the change, and if the member pays for dependent care services from an entity that is now closed, employee contributions should automatically decrease.¹²
- **Significant cost changes.** A member may make a mid-year election change if there is a significant cost decrease if several conditions are satisfied. As with all FSA mid-year election changes, the plan must allow the change. In addition, the cost change must result from something the provider did (like closing), and the provider must not be related to the employee by blood or marriage. Finally, similar coverage must not be available. There is no clear definition of what constitutes a “significant” change, but, presumably, the elimination of any dependent care cost due to a COVID-19-related disruption would qualify. Plan sponsors have leeway to interpret what is or isn’t significant.
- **Loss of coverage.** Although regulations differ when coverage is curtailed, we focus here on mid-year changes when coverage is lost completely. If coverage is lost altogether, a member may revoke their DCAP election, as long as the plan allows such mid-year changes and no similar coverage is available.

4. Health reimbursement arrangements that do not roll over from year to year

Nothing in regulation requires an employer to make changes to the structure of a health reimbursement arrangement if circumstances change—for example, if employees are no longer able to expend the funds contributed by the employer. However, nothing prohibits an employer from agreeing to do so.

Where HRA funds do not automatically roll over from year to year, affiliates should seek changes from the employer to permit unused HRA funds to remain in the employee’s account through the end of the plan year following the year in which any relevant COVID-19-related emergency is lifted. This timing would allow members to use their funds even if the emergency were lifted at the end of a plan year or if providers are delayed in resuming regular operations. The language that follows is also designed to ensure that if members are subject to different emergency requirements because they live in different locations, all members have rolled-over funds as long as one member remains under a COVID-19 emergency.

¹¹ 26 CFR § 1.125-4(F)(1).

¹² 26 CFR § 1.125-4(F)(2)(i).

The following language could be part of a broader COVID-19-related memorandum of understanding or a stand-alone MOU. Where members do not bargain collectively, the following language can serve as a guideline for what to seek from employers.

The employer's health reimbursement arrangement contributions will continue as established in [cross-reference relevant CBA section]. Any funds that remain unexpended at the end of the plan year shall remain in the account through the end of the plan year following the calendar year in which the COVID-19 emergency affecting any members is lifted. The employer shall make the changes to the plan and pay any expenses that are necessary to put this change into effect before the end of the current plan year.