



UBA  
Compliance Advisor

## What every HR leader should know about compliance



### Internal Revenue Service Notice 2020-33

The Internal Revenue Service (IRS) issued [IRS Notice 2020-33](#) (Notice) that increases the limit for unused health flexible spending account (health FSA) carryover amounts from \$500 to a maximum of \$550 (carried over from a 2020 plan year to a 2021 plan year), as adjusted annually for inflation. Notice 2020-33 also clarifies the ability of a health plan to reimburse individual insurance policy premium expenses incurred prior to the beginning of the plan year for coverage provided during the plan year. According to Notice 2020-33, the Department of the Treasury (Treasury) and the IRS intend to revise the proposed cafeteria plan regulations to reflect the guidance in this notice, but taxpayers may rely upon Notice 2020-33 in the meantime.

#### Increased Carryover Amount

Under the grace period rule, a Section 125 cafeteria plan may permit a participant to apply unused amounts (including amounts remaining in a health FSA) to pay expenses incurred for certain qualified benefits during the period of up to two months and 15 days immediately following the end of the plan year. Notice 2013-71 provided a further liberalization, permitting a Section 125 cafeteria plan to allow up to \$500 of any unused amount in a participant's health FSA as of the end of a plan year to be paid or reimbursed to the participant for medical care expenses incurred in the immediately following plan year (the "permissive carryover" rule). A health FSA cannot have both a grace period and a carryover. The permissive carryover does not count against, or otherwise effect, the employee's salary reduction election during the carryover year. Although the maximum unused amount allowed to be carried over in any plan year has historically been \$500, the plan may specify a lower amount as the permissible maximum carryover (and the plan sponsor has the option of not permitting any carryover at all).

Because, by statute, the increase to the health FSA limit is rounded to the next lowest multiple of \$50, increases to the maximum carryover amount, as the result of that indexing, will be in multiples of \$10 (20 percent of any \$50 increase to the health FSA limit). Thus, the maximum unused amount from a plan year starting in 2020 allowed to be carried over to the immediately following plan year beginning in 2021 is \$550 (20 percent of \$2,750, the indexed 2020 limit under Section 125(i)). An employer increasing the carryover amount for the 2020 plan year must adopt an amendment on or before December 31, 2021, which may be retroactively effective to January 1, 2020. Further, the employer must notify all individuals eligible to participate in the plan.



## Timing for Health Plan Reimbursements

In addition to the increase in the permissive carryover, the Notice clarifies that a health plan, including a premium reimbursement plan in a Section 125 cafeteria plan or an individual coverage health reimbursement arrangement (HRA), may not reimburse medical care expenses incurred before the beginning of the plan year and qualify for exclusion from income and wages under Sections 105 and 106 of the Internal Revenue Code. Medical care expenses are treated as incurred when the covered individual is provided the medical care that gives rise to the expense, and not when the amount is billed or paid. The Notice, however, provides that a plan is permitted to treat an expense for a premium for health insurance coverage as incurred on (1) the first day of each month of coverage on a pro rata basis, (2) the first day of the period of coverage, or (3) the date the premium is paid. Thus, for example, an individual coverage HRA with a calendar year plan year may immediately reimburse a substantiated premium for health insurance coverage that begins on January 1 of that plan year, even if the covered individual paid the premium for the coverage prior to the first day of the plan year.

## Section 125 Plan Elections

The Treasury and the IRS simultaneously issued [Notice 2020-29](#), that, among other things, for the remainder of 2020, allows employers to permit mid-year elections to a health FSA under a Section 125 plan, including the ability to make an initial election to fund a health FSA, provided the changes are applied only prospectively. See our [Advisor on Notice 2020-29](#), which addresses the temporary flexibility in response to the 2019 Novel Coronavirus.

5/13/2020

---

This information is general and is provided for educational purposes only. It is not intended to provide legal advice. You should not act on this information without consulting legal counsel or other knowledgeable advisors.