



Courtesy of Parelius Insurance Services

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What is a health flexible spending account (FSA)?

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A health FSA is an employer-sponsored account that employees can use to pay for (or reimburse themselves for) qualifying medical expenses on a tax-free basis. Unlike a health savings account (HSA), employees do not need to be covered by a high-deductible health plan (HDHP) in order to participate in a health FSA. Health FSAs can be offered with any other type of health plan.

Both employers and employees can make health FSA contributions, in contrast to a health reimbursement arrangement (HRA) where only the employer is allowed to make contributions. Employees may contribute pre-tax dollars to their health FSAs through a Section 125 plan (or cafeteria plan). Employers do not pay FICA or unemployment taxes on employees' health FSA contributions.

Often, employers will set a maximum annual amount that employees may contribute to their health FSAs. Effective for plan years beginning on or after Jan. 1, 2013, the federal health care reform law limits employees' pre-tax health FSA contributions to \$2,500 each year. For **taxable years beginning in 2015**, the dollar limitation on employee salary reduction contributions to a health FSA **will increase from \$2,500 to \$2,550**.

Employees may use their health FSAs to pay for (or reimburse themselves for) their own qualifying medical expenses, as well as their spouses' and dependents' qualifying medical expenses. Qualifying medical expenses are unreimbursed medical care expenses, as defined under Section 213(d) of the Internal Revenue Code. An employer may more narrowly define the expenses that can be reimbursed from an employee's health FSA. Unlike HSAs, health FSAs cannot be used to pay for non-medical expenses.

Also, effective in 2011 as part of the health care reform law, over-the-counter medicine expenses (except insulin) cannot be reimbursed from a health FSA unless prescribed.

There are two unique rules that apply to health FSAs.

- Under the **uniform coverage rule**, an employee's annual health FSA election amount (minus any reimbursements already made) must be available to him or her at any time during the plan year, regardless of how

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- much the employee has contributed up to that point. For example, if an employee elects to contribute \$750 to their FSA, the entire \$750 must be available to the employee for reimbursement immediately, even though their contributions will be divided throughout the year.
- FSAs employ a use-it-or-lose-it model. If there are unused funds in the FSA at the end of the year (or after the grace period), the employee forfeits those funds. However, employers also have the option of allowing employees to roll over up to \$500 of unused funds from one year to the next. Employers may allow less than a \$500 to be rolled over or none at all. In addition, any amount that is carried over does not count toward the maximum contribution limit.