



Losing the FSA 'Use-it-or-Lose-it' Rule?

Lawmakers are considering a bill that would give employees with health care Flexible Spending Accounts (FSA) the option to cash out unused balances at the end of the year and report those amounts as taxable income.

The Medical Flexible Spending Account Improvement Act of 2011, introduced recently by Reps. Charles Boustany (R-LA), John Larson (D-CT), Erik Paulsen (R-MN) and others, aims to encourage more people to use health care FSAs by eliminating the so-called "use-it-or-lose-it" rule.

Currently, FSA account holders are required to forfeit any funds in their account at the end of each coverage year.

Critics who prefer a "carry-over" option to this proposed "cash-out" solution say the bill doesn't go far enough, and some feel the measure could leave employers open to risk. Current regulations allow employers to use forfeited contributions to pay plan administrative expenses and offset costs incurred by employees who spend FSA funds early in the year and then leave the company.

We asked Ernie Harris, Ceridian's Senior Product Manager for Consumer Directed Health Care (CDHC), and Mary Jo Davis, Vice President of Ceridian Product Management, to weigh in on the topic of health care FSAs and the "use-it-or-lose-it" rule.

How does this proposed FSA rule change fit into the greater health care reform dialogue that's occurring right now in our country?

Mary Jo Davis: One of the goals employers have always had when offering FSAs is to help employees and their families make medical care more affordable. This is the same goal our lawmakers have as they continue to refine the overhaul of the country's health care system. So, eliminating the "use-it-or-lose-it" rule definitely falls in line with the spirit of health care reform — giving consumers more freedom to manage their own health care and related expenses, with fewer penalties.

Ernie Harris: I agree. A key component of successful health care reform is empowering individuals to share responsibility for their health care and its costs with employers and the government. FSAs, as part of the greater CDHC suite, do exactly that. Especially now, with out-of-pocket medical expenses like deductibles and co-pays continuing to rise, consumer-directed health care is more important than ever because it helps families save for medical costs on a pre-tax basis.

Giving consumers relief from "use-it-or-lose-it" would drive FSA participation, which would in turn help more people spend less on health care, no matter how the health care reform debate ultimately plays out.

What would this mean to employers?

Ernie Harris: More than 85% of large companies in the U.S. offer FSAs, but actual participation rates among employees have only been around 20%¹, which is lower than was expected when Flexible Spending Accounts were introduced in the 1970s. The consensus we're hearing from our clients is that the "use-it-or-lose-it" rule discourages FSA participation because, let's face it, who wants to give up their hard-earned money at the end of the year?

Getting rid of "use-it-or-lose-it" would put health care FSAs more on par with other CDHC savings vehicles like Health Savings Accounts (HSA), which are rapidly gaining popularity due to the fact that they give employees greater control by allowing them to carry over balances from year to year.

Does Ceridian have a position on the bill?

Mary Jo Davis: Traditionally, Ceridian has expressed great support for tax-advantaged medical reimbursement accounts. And for many years we've advocated modification of the health care FSA "use-it-or-lose-it" rule, urging Congress to enact either an annual "carry-forward" option or a "cash-out" alternative. So we feel that this bill is a step in the right direction.

What else should people know about this bill?

Ernie Harris: The outlook for the bill is uncertain. Much will depend on the budget impact "score" estimated by the Congressional Budget Office and the Joint Committee on Taxation. It's hoped that the legislation could actually raise revenue for the Treasury since unspent FSA funds would become taxable income.

¹ Letter from Reps. Boustany and Larson to Congress, March 2011