



IRS Updates “Use-or-Lose” Rule for Health FSAs to Permit Limited Rollovers

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The IRS recently issued an important notice modifying “use-or-lose” rules for health flexible spending accounts (“FSAs”), effective immediately, which should alleviate the typical end-of-the-year scramble to spend unused amounts before they are forfeited. The notice permits plan sponsors to allow participants to carry over up to \$500 of the unused amounts left in their health FSAs into the next year. The policy change is a response to the difficulty many participants face in predicting future needs for medical expenditures and the desire to minimize incentives for unnecessary spending at the end of the year.

If you wish to take advantage of this carry-over option in 2013, you will *need to amend your cafeteria plan by the end of the 2013 plan year*. In addition, you will want to communicate the change to your participants as soon as possible. It’s important to note that a health FSA cannot have both a carry-over feature and a grace period. Therefore, if your plan currently provides for a grace period, this feature would need to be eliminated in order to take advantage of the rollover option.

For example, if a participant has a health FSA account with \$400 remaining in it as year-end 2013 approaches, currently he or she would have to spend all of that \$400 on qualifying expense incurred before January 1, 2014 (unless the cafeteria plan provides a grace period). Under the new notice, the plan sponsor could amend their cafeteria plan by the end of the plan year to allow for a carryover of up to \$500 of unused health FSA amounts that could then be applied to expenses incurred at any time during the subsequent plan year. The participant would then have the option to spend those \$400 on qualifying expenses incurred on or after January 1, 2014.

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