

# **Health FSA Dollar Limit for 2013 Impacts Some Fiscal Year Plans Now**

## **January 10, 2012**

The Affordable Care Act limits salary deferrals that may be made under a health flexible spending account (FSA) to \$2,500 in “taxable years” beginning on or after January 1, 2013. However Section 125 cafeteria plans that include health FSAs subject to the dollar limit, and that follow a fiscal rather than calendar plan year, need to take steps now to apply the dollar limit over their 2012 – 2013 plan year.

That is because, for purposes of the 2013 dollar limit, the term “taxable year” refers not to the plan year but to the taxable year of the *employee* participating in the health FSA. Almost universally, this will be the calendar year. The first fiscal plan year that will overlap with 2013 begins February 1, 2012 (ending January 31, 2013). Fiscal year plans that currently permit salary deferrals in excess of \$2,500 must ensure that deferrals occurring over the 2013 calendar year do not exceed the \$2,500 cap.

For instance, a plan that follows an April 1 – March 31 fiscal year and currently permits a maximum health FSA reimbursement of \$6,000 would ordinarily allow participants to defer \$500 per month under the plan. For the plan year beginning April 1, 2012 and ending March 31, 2013, this would permit salary deferrals of up to \$1,500 to occur between January 1, 2013 and March 31, 2013. A participant deferring the maximum amount in the current plan year would be limited to deferring \$1,000 over the balance of the 2013 calendar year (April through December), or only \$111.11 per month.

We do not yet have any specific guidance from the IRS on applying the new dollar limit to a fiscal year plan, and the pro-rata method described above is only one option.

Other options might include (a) allowing the current rate of deferrals to continue into 2013, but cutting them off as soon as they reach the \$2,500 dollar limit, and (b) imposing the \$2,500 dollar limit as of the beginning of the 2012-2013 fiscal plan year. One trusted research source, EBIA’s Cafeteria Plans (©2011 Thompson-Reuters) mentions “front-loading” the deferrals during 2012, so that the “old” budget is met even while deferrals made during the 2013 year stay within the new dollar limit. Even were the IRS expressly to sanction the front-loading approach, it might not be financially workable for employees, particularly under fiscal year plans that begin late in the calendar year. Although guidance from the IRS is needed on this and a number of other transition compliance points, employers with early fiscal year starts do not have the luxury of waiting much longer.

Whichever transition method is chosen, employers promptly should communicate their choice to plan participants and work closely with their payroll departments, or their third party payroll providers, to ensure that they transition smoothly into the new dollar limit applicable January 1, 2013 and beyond.