

Understanding FSA Benefits Post-PPACA

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Imagine you're walking the hallways of your office and you pass a poster on the wall that reads, "Stop by the benefits office and pick up a coupon that is good for a significant discount on daycare, contact lenses, orthodontia treatment and more." Would you pass the sign without a second thought, or would you run to the benefits office as fast as possible?

That particular hypothetical coupon is actually known as a flexible spending account (FSA). An FSA has quickly become a highly valued, voluntary employee benefit for many organizations. Payroll contributions made to an FSA are exempt from federal income tax, Social Security taxes and, in most cases, state income tax. As a result, those employees who use an FSA can essentially shield a portion of their income from taxes to pay for approved medical and dependent care expenses. Yet, despite this significant benefit, in most organizations FSAs are often one of the

most under-utilized company benefits.

A Misunderstood Benefit

When you consider the potential savings, it's a bit mystifying that FSA participation within most organizations is typically very low. There may be several factors contributing to this: (1) employees may not fully understand the true FSA savings; (2) it may be difficult for employees to get excited about the concept of a pre-tax benefit; (3) it's not tangible; (4) people may focus on the word "tax" and then shy away from wanting to learn more about a related benefit; and (5) the idea of reducing employees' paychecks may have a negative connotation. When employees learn that an FSA involves having their paychecks reduced – without really understanding the reason – they are understandably skeptical. Top executives may not even understand FSA benefits. But employers need to be made

aware that they also benefit when employees utilize an FSA because it reduces the company's taxable income as employers save on the Social Security and Medicare taxes that they would otherwise pay on these wages.


So, what's the secret to increased employee participation in an FSA? As with any benefit offering, employee communication and education are critical to driving enrollment. The benefit of an FSA becomes much clearer when the financial savings are connected to money employees spend every day, when they learn that their asthma prescription, braces for a 14-year-old or monthly daycare expense can be reimbursed from an FSA.

Health Care Reform and the Future of FSAs

The 2010 Patient Protection and Affordable Care Act will impact FSA accounts. However, participation in FSA programs may actually increase as more employers and employees see the tax saving benefits that can be realized through plan participation. Furthermore, other accounts, such as health savings accounts, will continue to offer out-of-pocket savings and are likely to gain popularity, at least in the short term.

Near-term changes to FSA accounts began on January 1, 2011, with over-the-counter medicine and drug purchases only being reimbursed from an FSA if the participant

has a valid prescription or a prescription number for the item purchased. In 2013, there will be a \$2,500 limit on the amount participants can contribute to their FSAs. The average contribution for FSA participants is approximately \$1,500, which is well within the limit established by the new legislation.

Ultimately, employers will still get the tax benefits from the payroll contributions to FSA programs, and participation in the programs still provides the financial savings for employees on medical and dependent care expenses they would normally incur. Explaining the benefits to employees in terms of using a coupon or getting a discount helps relate these programs to daily life and may increase participation in these voluntary benefits. As a CPA, you have a multi-dimensional opportunity to advise both business and individual clients on the financial benefits of utilizing FSAs, not to mention incorporating FSA benefits at your own firm. 



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