



# No Good Deed...: Allowing Part-Time Employees to Make Health FSA Contributions May Trigger ACA Penalties

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When it comes to health coverage, many employers draw a distinction between full-time and part-time employees. To be eligible to enroll in the employer's health plan, an employee must work a minimum number of hours per pay period. But many of those *same* employers then allow even *part-time* employees to contribute to a health flexible spending account ("health FSA"). After all, doing so costs the employer nothing (and even saves a modest amount in employment taxes), and why not at least give those employees an opportunity to pay some of their medical expenses on a pre-tax basis? Unfortunately, this paternalistic approach may now subject an employer to substantial daily penalties under the Affordable Care Act ("ACA").

In September of 2013, the agencies charged with enforcing the ACA issued coordinated guidance sharply restricting the use of individual-account plans such as health reimbursement arrangements ("HRAs"), health savings accounts ("HSAs"), and health FSAs. We summarized that guidance in our [October 2013 article](#).

The thrust of that guidance was directed toward HRAs. The health FSA aspects were relegated to a virtual footnote. In the FSA context, the agencies seemed to be saying that an employer could not offer a *stand-alone* health FSA. Instead, it would also have to offer a more comprehensive health plan. During the course of the recent annual enrollment season, however, it became clear that this guidance has even broader implications.

The September 2013 guidance (including [IRS Notice 2013-54](#) and [DOL Technical Release 2013-03](#)) focused on the following two ACA mandates:

- The prohibition on applying any annual or lifetime dollar limit on coverage for essential health benefits, and
- The requirement that all non-grandfathered health plans cover a specified list of preventive-care services on a first-dollar, unlimited basis.

The guidance made clear that health FSAs offered through a *cafeteria plan* (as most are) need not comply with the prohibition on annual or lifetime limits. This is because those FSAs are separately subject to the ACA's annual *cap* on salary deferral contributions (\$2,550 in 2015).

Unless an exemption applies, however, *all* health FSAs must provide unlimited, first-dollar coverage for preventive-care services. Two such exemptions might conceivably apply.

First, some FSAs may be "grandfathered" under the ACA rules. If so, they would be exempt from this preventive-care mandate on that basis. As explained in our [June 2010 article](#), however, such grandfathering requires regular notice to plan participants of the plan's grandfathered status. In our experience, such notice is rarely provided in the FSA context.

The other exemption from the preventive-care mandate is far more common in the health FSA context. This is an exemption for "excepted benefits." As explained in our October 2013 article, a health FSA is an excepted benefit if *both* of the following conditions are met:

- Any employer contribution to an employee's FSA is limited to the greater of \$500 or the amount of the employee's salary-deferral contributions (i.e., as a dollar-for-dollar match), and
- Employees who are eligible to contribute to the FSA are also offered health coverage that is *not* an excepted

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benefit.

The first of these two conditions is easily satisfied. In fact, most employers make no contribution whatsoever to their employees' health FSAs.

Under the second condition, an employer may not offer *only* a health FSA, with no comprehensive medical plan. But what some employers may have overlooked is that this condition applies on an *employee-by-employee* basis. Therefore, even if an employer offers medical coverage to substantially all of its employees (such as those meeting a "full-time" definition), it would fail to satisfy this condition with respect to any employees who are *not* eligible for medical coverage (but who are nonetheless allowed to make health FSA contributions). The penalty for such an ACA violation would be \$100 per day for each employee in this group.

An employer that finds itself in this situation – and that cannot establish "grandfathered" status for its health FSA – will want to take immediate action to avoid this ACA violation. If part-time employees (or *any* employees who are not offered medical coverage) have been allowed to make health FSA elections for 2015, those elections should now be canceled. Either that, or those employees should be offered medical coverage.