Dependent Care FSA Issues During the Pandemic

Changing Pre-Tax Elections

As a result of the on-going COVID-19 pandemic, many employees are working from home. Some employees have young children at home due to the closure of day care facilities and other COVID-19 related reasons. Other employees may be working fewer hours and, therefore, have lower than expected dependent care expenses. Employees in these circumstances often ask about changing the amount of their pre-tax contributions to their dependent care flexible spending accounts.

Fortunately, the applicable change of election rules are applied in a more liberal manner to dependent care flexible spending accounts than in the case of health flexible spending accounts. When applied to dependent care flexible spending accounts, the rules allow changes in pre-tax contributions under circumstances where the need for dependent care changes mid-year. Therefore, an employee who is working from home or working less and does not need, or have access to, dependent care, can be allowed to change (stop or reduce) his or her pre-tax contribution election. If the employee subsequently returns to working on-site or returns to a "normal" work schedule, another election change can be allowed to increase contributions, assuming that the need for dependent care increases.

Access to Unused Balances

Employees who have been furloughed, laid-off or terminated obviously stop making pre-tax contributions when they are no longer being paid. These individuals often ask about having access to their unused dependent care flexible spending account balances.

For employees who have been furloughed, laid-off or terminated, dependent care flexible spending accounts can include an optional "spend down" feature. Such a feature allows an otherwise ineligible employee or former employee to seek reimbursement for qualifying expenses incurred through the end of the current year, even though employment with the sponsoring employer has been interrupted or has ended.

Because a "spend down" feature is optional, not all plans/accounts have such a feature. In fact, some plans immediately terminate access to dependent care flexible spending accounts when active employment ends for any reason.

If desired, a "spend down" feature can be added at any time by a written amendment to the plan that includes the dependent care flexible spending account. Qualifying expenses incurred after the date the amendment is adopted (or after the amendment's effective date, if later) can then be reimbursed from the unused balance in the dependent care flexible spending account. As noted above, access to the unused balance is limited to qualifying expense incurred through the end of the current year.

Check the Plan Document

Before allowing employees to change pre-tax contribution elections, the governing plan documents should be reviewed to ensure changes are allowed by those governing documents. Plan amendments may be required. Similarly, before adding a “spend down” feature, the governing plan documents should be reviewed to ensure that the applicable amendment procedures are followed. Third-party administrators (if applicable) should be consulted in advance to ensure consistent administration of any desired plan design changes.

If you have any questions about this Information Memo, please contact Stephen Daley, any attorney in our Employee Benefits and Executive Compensation Practice Group, or the attorney at the firm with whom you are regularly in contact.