New Dependent Care FSA Nondiscrimination Rules Are Easier to Pass

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New proposed regulations make it easier for dependent care flexible spending accounts (“***DCFSAs***”) to pass applicable nondiscrimination rules under the Internal Revenue Code and, in particular, the “average benefits test.” Many employers have been unable to offer DCFSAs, or have limited participation in a DCFSA, because the literal application of statutory nondiscrimination requirements may cause the DCFSA to fail when highly compensated employees (“***HCEs***”) disproportionately elect to participate in the DCFSA. Generally, the average benefits test requires the average benefits provided to non-HCEs to be at least 55 percent of the average benefits provided to HCEs. A common interpretation of this test required looking at all non-HCEs and HCEs, regardless of whether they elected to participate in the DCFSA. The proposed regulations clarify that, for purposes of the average benefits test, an employee is taken into account only if they elect to participate in the DCFSA.

Employers may rely on these proposed regulations now, before the date that final regulations are published.

The proposed regulations can be found here.