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DON'T OVERLOOK BENEFITS OF FLEXIBLE SPENDING ACCOUNTS

One of the best fringe benefits offered by many employers is also one of the most overlooked by employees-flexible spending accounts, or reimbursement accounts. These accounts allow you to save tax dollars on money you spend for dependent-care or health care expenses. Here's how they work and why they can be a good deal.

Say your employer offers a flexible spending account (FSA) for health care. You direct your employer to set aside from your paycheck a certain amount of money for the year to be credited to the account. The amount isn't taken out all at once-it's usually spread out over the year. If the total amount is \$1,200, the employer would take out \$100 a month (some employers require larger upfront payments). As you incur unreimbursed medical expenses, such as co-pays, the account pays you back, up to the total amount set aside.

What's the big deal about this? The money the employer deducts from each paycheck is before taxes-not unlike money taken out for a retirement plan, only better. Say you have \$3,000 set aside in an FSA. If you're in the 28 percent federal income tax bracket, you will save \$840 on your tax bill. Looked at another way, without the FSA you'd have to earn \$1.39 to buy \$1 worth of health care. In essence, Uncle Sam subsidizes a portion of your health care costs. Obviously, the tax savings are more the higher your tax bracket. With the exception of a couple of states, you also can save state and local taxes.

Furthermore, unlike money deducted for retirement plans, the money set aside for an FSA is not subject to Social Security and Medicare taxes, though this could reduce the amount of Social Security benefits you're entitled to when you retire.

The federal government doesn't limit how much you can set aside in an FSA for health care as long as it doesn't exceed your income. However, most employers cap it at \$2,500 to \$5,000. Federal law limits the dependent-care FSA deductions to \$5,000, or \$2,500 for married filing separately. If your employer offers FSAs for both health care and dependent care, you can use both of them up to their limits.

Another benefit is that the entire amount you want set aside for the year is available to cover expenses at the start of the benefit year, even though the money is deducted from your paycheck over the course of the year. Should you leave before all FSA deductions are taken, the employer makes up the difference.

Surprisingly, although 56 percent of employers offered health-care spending accounts in 1998, according to a survey by the benefits consulting firm of William M. Mercer, only 19 percent of the employees took advantage of them. More employees don't take advantage of FSAs for two reasons: they don't fully realize the tax benefits, and they worry about the use-it-or-lose-it provision. That's the big catch to FSAs. Employees forfeit to the company any money they don't use from the account by the end of the benefit year. You can't roll it over or take out the remaining amount in cash.

To avoid wasting money, project your expenses carefully for the coming benefits year. This is easiest to do with dependent-care accounts, because expenses often are fairly predictable. This account isn't restricted to child care, by the way. Care expenses can be claimed for anyone whom you claim as a dependent on your income taxes, such as a parent or a disabled spouse.

One caution about using flexible spending accounts for child care: lower-income families may be better off claiming the child-care credit than using an FSA (you can't do both). That's because the percentage of child care credit you can claim is reduced the higher your income.

It's best to be more conservative estimating medical expenses. Average routine costs from the past two or three years, and factor in known major upcoming expenses, such as the deductible for a surgery. You can claim a wide range of reimbursements: co-pays, deductibles, dental care, eyeglasses, prescription drugs, acupuncture and psychiatric care, and in some situations even health insurance, to name a few.



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