



JOINT COMMITTEE ON TAXATION

September 26, 2006

JCX-46-06

**DESCRIPTION OF CHAIRMAN'S AMENDMENT IN THE NATURE OF  
A SUBSTITUTE TO H.R. 6134, THE "HEALTH OPPORTUNITY PATIENT  
EMPOWERMENT ACT OF 2006"**

The Chairman's amendment in the nature of a substitute makes the following modifications to H.R. 6134.

**A. Modification of Cost-of-Living Adjustment**

The Chairman's amendment provides that the provision of H.R. 6134 relating to cost-of-living adjustments is effective for adjustments made for taxable years beginning after 2007.

**B. Certain FSA Coverage Treated as Disregarded Coverage**

The provision provides that, for taxable years beginning after December 31, 2006, in certain cases, coverage under a health flexible spending arrangement ("FSA") during the period immediately following the end of a plan year during which unused benefits or contributions remaining at the end of such plan year may be paid or reimbursed to plan participants for qualified expenses is disregarded coverage.<sup>1</sup> Such coverage is disregarded if (1) the balance in the health FSA at the end of the plan year is zero, or (2) in accordance with rules prescribed by

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<sup>1</sup> Under present law, individuals who are covered by a high deductible health plan and no other health plan that is not a high deductible health plan (other than certain permitted coverage) are eligible to make tax deductible HSA contributions. Health FSAs constitute other coverage not permitted under the HSA rules. Health FSAs are subject to the general requirements relating to cafeteria plans, including a requirement that a cafeteria plan generally may not provide deferred compensation, which is referred to as the "use-it-or-lose-it-rule." In general, amounts remaining in a health FSA as of the end of a plan year must be forfeited by the employee. However, the Treasury Department allows a grace period not to exceed two and one-half months immediately following the end of the plan year during which unused amounts may be used (Notice 2005-42). An individual participating in a health FSA that allows reimbursements during a grace period is generally not eligible to make contributions to the HSA until the first month following the end of the grace period even if the individual's health FSA has no unused benefits as of the end of the prior plan year. (Notice 2005-86).

the Secretary of Treasury, the entire remaining balance in the health FSA at the end of the plan year is contributed to an HSA as provided under another provision of the proposal.<sup>2</sup>

Thus, for example, if as of December 31, 2006, a participant's health FSA balance is zero, coverage under the health FSA during the period from January 1, 2007, until March 15, 2007 (i.e., the "grace period") is disregarded in determining if tax deductible contributions can be made to an HSA for that period. Similarly, if the entire balance in an individual's health FSA as of December 31, 2006, is distributed and contributed to an HSA (as under another provision of the proposal) coverage during the health FSA grace period is disregarded.

It is intended that the Secretary will provide guidance under the proposal with respect to the timing of health FSA distributions contributed to an HSA in order to facilitate such rollovers and the establishment of HSAs in connection with high deductible plans. For example, it is intended that the Secretary would provide rules under which coverage is disregarded if, before the end of a year, an individual elects high deductible plan coverage and to contribute any remaining FSA balance to an HSA in accordance with the proposal even if the trustee-to-trustee transfer cannot be completed until the following plan year. Similar rules apply for the general proposal allowing amounts from a health FSA to be contributed to an HSA.

The proposal does not modify the permitted health FSA grace period allowed under existing Treasury guidance.

Effective date.-- The proposal is effective after the date of enactment with respect to coverage for taxable years beginning after December 31, 2006.

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<sup>2</sup> The amount that can be contributed is limited to the balance in the health FSA as of September 21, 2006.