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What are employees supposed to do with their excess pretax deductions?

Not a frivolous question, considering that telecommuting employees spend less on things like monthly train tickets and childcare.

The IRS issued guidance earlier this year allowing employees to cancel their pretax contributions into health and dependent care FSAs.

Which is great as far as it goes.

But what can employees do with the money they salted away into their accounts before they made the election to cancel?

There are no refunds

The cafeteria plan rules are pretty strict and operate on the principle of constructive receipt—if you can exercise control over the receipt funds, they are taxable to you, regardless of whether you actually ever get the cash in hand.

Roughly speaking, constructive receipt is why employees can't get cash refunds of their pretax contributions.

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Dependent care

Dependent care FSAs can have grace periods, but rollovers of unused amounts into the next plan year aren't permitted. So in the case of excess dependent care contributions, employees will either have to spend the money by the end of the grace period or forfeit it.

What to spend it on? The IRS' guidance didn't change the rules regarding what counts as a tax-free dependent care expense—an expense incurred that enables employees to work. That means we have to get creative. Some ways employees can spend their FSA dollars:

- Computer tutorials or an in-house helper for employees whose kids are remote learning
- After-school care for employees whose kids aren't remote learning
- Homework help, regardless of how employees' kids are learning.

Transportation fringes

Tax relief for pretax contributions for transportation fringes—mass transit passes or employer-provided parking—wasn't included in the IRS' earlier guidance.

Transportation fringes are treated a bit differently from other benefits employees can purchase with pretax deductions. Employees can revoke their elections for pretax contributions prospectively and/or rollover amounts leftover into the next month or even the next year. But there are still no cash refunds.

Lots of people are leery of taking public transportation right now. In fact, we've read about used car sales going through the roof, because even in cities, employees now prefer to drive to work.

Employees can continue to rollover their contributions for mass transit benefits or they can opt for another qualified transportation fringe, like employer-provided parking, to the extent you offer parking as a benefit and the benefit doesn't exceed the maximum monthly amount—$270 a month for this year and next year.

Employees must present receipts for their parking expenses before you can reimburse them.

But there is a huge glitch: You can no longer deduct the cost of providing transportation fringes to employees on your Form 1120.

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