



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

OFFICE OF THE CHIEF COUNSEL

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The Honorable James B. Renacci  
Member, U.S. House of Representatives  
1 Park Center Drive, Suite 302  
Wadsworth, Ohio 44281

Dear Representative Renacci:

I am responding to your letter dated September 6, 2016, on behalf of your constituent, . requested your assistance in determining whether unused funds in a flexible benefit plan default to the U.S. Treasury when a business ceases operations. You have asked whether this is true and if so, how he can claim those funds.

Flexible benefit plans like the plan sponsored by former employer (the "Flex Plan") are subject to requirements under section 125 of the Internal Revenue Code (the "Code"). Section 125 of the Code does not require that unused funds revert to the U.S. Treasury when the employer ceases operations and the plan terminates. In addition, how unused funds are disposed of when the plan terminates would depend on what the plan document provides about plan termination and the facts and circumstances at that time. Proposed Treasury Regulations under section 125 of the Code, however, do set forth rules on the use of unused amounts forfeited by a plan participant with respect to an ongoing plan. Proposed Treasury Regulation § 1.125-5(o)(1) (enclosed) provides that forfeitures may be:

- Retained by the employer maintaining the plan, or if not retained by the employer
- Used to defray plan expenses
- Returned to employees (that is, current participants) and allocated on a reasonable and uniform basis, based on, for example, contributions and not on claims experience

From the information that you provided to us, during the months he was employed in \_\_\_\_\_, \_\_\_\_\_ deposited money into the Flex Plan sponsored by his former employer. According to the Flex Plan's summary plan description, health care expenses incurred on or before termination of employment could be reimbursed.

\_\_\_\_\_ had unused funds in his Flex Plan account when his employment terminated but he did not have unreimbursed health care expenses as of that date. Your letter states that the Flex Plan document provided that any unused funds reverted to the plan to pay plan administrative expenses. \_\_\_\_\_ wrote that he was told that because his former employer went out of business, unused funds defaulted to the U.S. Treasury.

It appears from the information you provided to us that unused funds in the Flex Plan are forfeited upon an employee's termination of employment unless the employee had reimbursable health care expenses on or before the termination and submitted a claim within 60 days. This is consistent with Proposed Treasury Regulation §§ 1.125-6(a)(2)(i) and (iii) (enclosed), which together provide that a plan is prohibited from reimbursing health care expenses incurred after an employee terminates employment and no longer participates in the plan. As noted above, how unused funds are disposed of when the plan terminates would depend on what the plan document provides about plan termination and the facts and circumstances at that time.

I hope this information is helpful. If you need additional information, please contact \_\_\_\_\_ at \_\_\_\_\_, or me at \_\_\_\_\_.

Sincerely,

Victoria A. Judson  
Associate Chief Counsel  
(Tax Exempt and Government Entities)

Enclosure