

FSRA Nondiscrimination

Testing guide

This guide is designed to provide an overview of nondiscrimination testing (NDT) requirements for Flexible Spending and Reimbursement Accounts (FSRA) program administrators. This guide also addresses services offered through Fidelity to support program administrator compliance with NDT requirements.

Overview

Various employer-sponsored health and welfare benefit programs receive favorable tax treatment under the Internal Revenue Code when these benefits are offered under a cafeteria plan on a pre-tax basis. In exchange for favorable tax treatment, the Internal Revenue Service (IRS) has developed certain nondiscrimination testing rules for these plans to ensure that rank-and-file employees, the group that Congress intended to benefit from favorable treatment, do in fact benefit in the way Congress intended. These tests—though complex—are fundamentally about fairness: ensuring that all employees, regardless of compensation level, have equitable access to tax-advantaged benefits.

Which FSRA plans must be tested?

IRS NDT rules apply to the following FSRA plan types:

Cafeteria plan

This is the vehicle that allows employees to use their salary to fund spending accounts, such as the HCFSAs, which covers out-of-pocket, qualified medical expenses for employees, their spouses, and their dependent children

Healthcare FSA (HCFSAs)

Covers qualified medical, dental, vision, and preventive care expenses for employees, their spouses, and their dependent children

Limited Purpose FSA (LPFSA)

Covers qualified dental, vision, and preventive care expenses for employees, their spouses, and their dependent children, subject to limitations based on design

Dependent Care FSA (DCFSA)

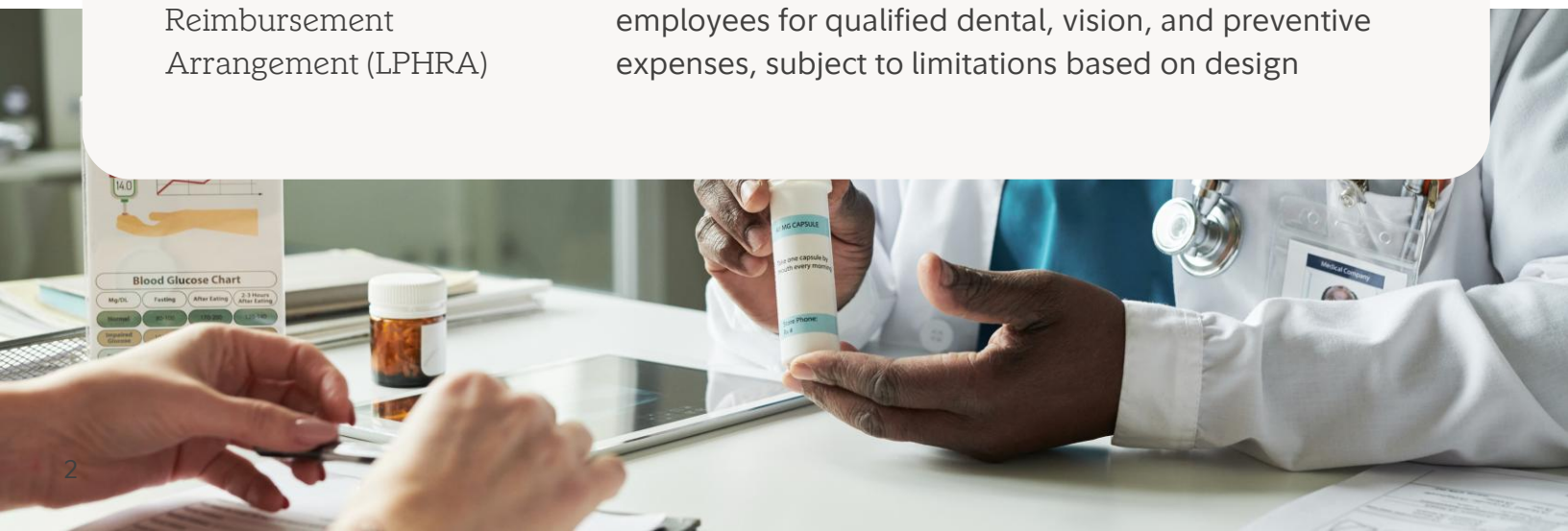
Covers qualified dependent care expenses for eligible dependents or eligible relatives

Health Reimbursement Arrangement (HRA)

An employer-funded plan that assists employees with paying for qualified medical, dental, and/or vision expenses

Limited purpose Health Reimbursement Arrangement (LPHRA)

An employer-funded plan that typically only reimburses employees for qualified dental, vision, and preventive expenses, subject to limitations based on design



What does testing entail?

The IRS has detailed and distinct requirements based on plan type. The different testing formulas are based in part on what each benefit is meant to confer on a participant, so testing must be designed to achieve that goal. See below for further details on testing.

Employee Designations

Highly Compensated Employee (HCE):

For 2026, defined as:

- An employee who earned \$160,000 or more in 2025, or
- A 5% owner in the current or prior year, or
- An employee in the top 20% of compensation (if elected)

Non-Highly Compensated Employee (NHCE):

An employee who does not meet the criteria to be classified as an HCE

Key Employee:

For 2026:

- An officer earning \$235,000+, or
- A 5% owner, or
- A 1% owner earning \$150,000+

IRC Section 105(h) – Self-Insured health plans (including HCFSA, LPFSA, HRA, and LPHRA)

Eligibility Test:

Three options are provided to pass this test based on eligibility, participation, and by demonstrating that the plan provides benefits to employees, under a qualified classification, that are found not to be discriminatory in favor of HCEs

Benefits Test:

Responses to subjective questions determine if all benefits provided for participants who are HCEs are also being provided for all other participants

Internal Revenue Code Section 129 – Dependent Care Assistance Programs (DCAPs, including DCFSA)

Eligibility Test:

Ensures the plan benefits a non-discriminatory class of employees

Contributions and Benefits Test:

Ensures that benefits or contributions provided under the DCAP do not discriminate in favor of HCEs

More-Than-5% Owner Test:

Utilization test that ensures that not more than 25% of the total benefits under the DCAP are provided to more-than-5% owners of the company

55% Average Benefits Test:

Utilization test that requires that the average benefits provided to non-HCEs must be at least 55% of the average benefits provided to HCEs. Plan sponsors should pay keen attention to this test since it has a high failure rate depending on participation levels of HCEs/key employees and benefit election amounts

Note: In August 2026, Treasury and IRS proposed new regulations clarifying, among other things, application of the 55% Average Benefits Test, indicating that employees who are eligible but do not contribute to a DCFSA are excluded from the average benefits calculation.

Internal Revenue Code Section 125 – Cafeteria plans

Eligibility Test:

Compares percentage of eligible NHCEs to percentage of eligible HCEs

Contributions and Benefits Test:

Evaluates whether the percentage of benefit dollars compared to compensation for HCEs is equal to or less than the same percentage for NHCEs

Key Employee Concentration Test:

Utilization test that typically limits the nontaxable benefits elected by key employees (i.e., certain officers and owners) to a maximum of 25% of the total nontaxable benefits provided to all employees under the cafeteria plan

Note: NDT should be performed annually and whenever there are significant plan changes.

How are NDT corrections made?

There could be several potential correction paths, depending on the plan type that failed. Each path carries different employee impact considerations. Plan sponsors should engage their benefits counsel and/or consultant to identify the best correction path.

How does Fidelity support plan sponsors?

Fidelity works with RTO Benefits to offer NDT services. Reimbursement Account Client Service Managers will submit an initial request to RTO Benefits to schedule a meeting with the client contact(s) to review the tests offered, the data and templates needed, and the project timeline. RTO Benefits will remain the primary point of contact for clients until all required tests have a passing result.

When working with RTO Benefits, clients are not charged for their initial NDT testing—including if retests are needed due to testing failure. When RTO Benefits is engaged for additional testing, clients are charged \$750 per request.

Additionally, Reimbursement Account Client Service Managers provide NDT education and best practices throughout the year to ensure clients will be able to meet the IRS NDT deadline—which is the last business day of the plan year.



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