V. Flexible Spending Accounts

Table of Contents

About This Section

This section describes the Flexible Spending Accounts (FSAs). Flexible spending accounts enable you to save on taxes while providing a convenient way to budget for certain health care and dependent care expenses. There are three types of FSAs:

- The Health Care FSA
- Combination (Combo) FSA
- The Dependent Day Care FSA

Each year, you may direct a portion of your pay into one, two or both, accounts on a pre-tax basis. You may use the money in your account(s) to reimburse yourself for qualified expenses throughout the year.

This section explains how these accounts work and what expenses are eligible for reimbursement.

Some of the terms and phrases used in this benefits document have a specific meaning. Please refer to the *Important Terms* section of this document for further information.

You should also refer to the *Benefits Highlights* and the *Additional Information About Your Benefits* sections of this document for more important information regarding eligibility, how contributions are made, how elections can be changed, how to file claims and your rights under ERISA.

An Overview of the Flexible Spending Accounts

You can choose to participate in one of the health flexible spending accounts, the Health Care FSA or the Combination (Combo) FSA and the Dependent Day Care FSA, or you can choose not to participate. You can deposit money on a pre-tax basis into the Health Care or Combo FSA to be reimbursed for certain health care expenses for you and your dependents. You can deposit money into the Dependent Day Care FSA on a pre-tax basis to be reimbursed for expenses related to the care of any dependent you claim on your federal income tax return.

How Flexible Spending Accounts Work

Ordinarily, you pay for unreimbursed health care and dependent care expenses with after-tax dollars. FSAs allow you to pay for certain expenses with pre-tax dollars. The money you deposit in the accounts is deducted from your pay before federal income taxes, social security and most state and local taxes are taken out, and you don't need to pay taxes on the reimbursements you receive from the accounts. That means you pay taxes on a smaller amount of money, and your disposable income is higher. However, certain states do not recognize these contributions for state income tax purposes. For example, if you are a resident of New Jersey, you will pay personal income taxes on your pre-tax contributions. If you are a resident of Pennsylvania, you will pay personal income taxes on your pre-tax contributions to the Dependent Day Care FSA.

Here's how FSAs work:

1. Each year you decide how much money you want to deposit in the accounts.
2. The money is deducted from your pay in equal amounts each pay period throughout the year and goes into your account before federal and, in most cases, state and local income taxes are deducted.
3. After you pay for an eligible health care, combo or dependent care expense, you submit a claim and are reimbursed with tax-free money from your account. You can submit claims for expenses incurred during the year until March 31 of the following year.
4. You can also use your Mercer Marketplace Visa® Debit card to pay for expenses

Remember, the health care, combo and dependent care accounts are all separate. You *cannot* use money in the Health Care FSA or Combo FSA for your dependents' day care expenses, and you *cannot* use money in the Dependent Day Care FSA for your or your dependents' health care expenses.

Your Deposits – Use It or Lose It

It is important that you plan carefully and contribute only as much money as you are sure to use. If you do not use all of the money you deposit in your FSA accounts during the year, you will forfeit the unused balance. Your unused balance will not be refunded to you or carried over to the next year – you either use it or lose it.*

To be reimbursed as an active employee, your eligible expenses must be incurred during the plan year (January 1 through December 31) and while you were making FSA contributions. You can submit claims for these expenses until March 31 of the following year. After March 31, you forfeit any unused amount in your accounts.

See Life Events Action Chart in the Benefits Highlights section for reimbursement rules following termination of employment.

* *The sole exception to this rule is if you are a qualified reservist who is called to active duty for more than 180 days, in which case unused funds from your health care FSA may be distributed to you in accordance with the terms of the HEART Act.*

How Other Benefits Are Affected

Even though participation in the flexible spending accounts reduces your taxable income, it will not affect other benefits related to your income, for example, life insurance.

However, if you earn less than the Social Security wage base your Social Security taxes will be lower, and your Social Security benefits could be reduced slightly. For many employees, however, the immediate tax benefits of participating in the accounts will outweigh the slightly reduced future Social Security benefit. Since each employee's financial situation is different, you should consult with your tax advisor to determine how this reduction in benefits will affect you.

Special Rules for Flexible Spending Accounts

Specific Treasury regulations govern benefit plans such as flexible spending accounts. These regulations and laws place stringent requirements on the Company to monitor and regulate the amounts that different groups of employees may contribute. To comply with these regulations, the Company may at times need to change contribution levels under the Plan. Therefore, while there are certain contribution limits shown in this section of the document, all flexible spending account participants may not be able to contribute up to the limit, or the amount they have elected to contribute may be reduced.

Health Care FSA

The Health Care FSA allows you to set aside money from your pay on a pre-tax basis to pay for eligible health care expenses not covered by any medical, dental or vision program. After you pay these expenses and submit a claim, you can be reimbursed with tax-free money.

How Much You Can Deposit

You can deposit between $120 and $2,700 (in 2019), as indexed, each calendar year in the Health Care FSA. Your deposit is subtracted from your pay in equal amounts each pay period before income taxes and social security taxes are taken out.

Eligible Dependents

Besides yourself, you can claim health care expenses for:

- Your spouse
- Your dependent children
- Any other person who can be claimed as your dependent for federal income tax purposes (without regard to their gross income).

You do not have to cover your Eligible Dependents under the medical, dental or vision plans to use the Health Care FSA for their eligible expenses. Similarly, you do not have to enroll in health care coverage to use this account.

Consult the definition of Eligible Dependent in the *Important Terms* section of this SPD for more information.

Eligible Expenses

Expenses eligible for reimbursement through the Health Care FSA are those health care expenses not covered or only partly covered by any health care plan you may have. They include:

- Medical, dental and vision deductibles
- Coinsurance amounts
- Copayments and fees
- Expenses not reimbursed because they are greater than reasonable and customary amounts
- Certain services or treatment not covered by your health care plans
- Amounts over scheduled payments.

In general, any health care expenses, excluding insurance premiums and certain long term care expenses, that the IRS considers to be deductible on your income tax return and not covered by any health care plan, are eligible for reimbursement from the Health Care FSA.

The following is a partial list of some specific expenses eligible for reimbursement through the Health Care FSA. Refer to IRS Publication 502, "Medical and Dental Expenses," (available on the IRS website at www.irs.gov) for more information regarding eligible and ineligible expenses.

- Adapters for telephone and TV for the deaf
- Alcoholism treatments
- Artificial limbs, eyes
- Braille books and magazines
- Child-birthing classes
- Contact lens solution
- Crutches, splints and braces
- Fees for smoking cessation (including classes, nicotine gum and patches)
- Fertility treatment
- Guide dogs for the blind or deaf (including the cost of buying, training and maintaining the dog)
- Hearing aids
- Medical supplies and equipment
- Nurse's board and wages, including employment-related taxes paid
- Orthopedic shoes
- Podiatrists
- Psychotherapy
- Remedial reading lessons for dyslexic child
- Repair of medically necessary equipment
- Telephone for the deaf

- Travel expenses related to medical treatment
- School costs for mentally or physically handicapped children
- Wheelchair
- Wigs purchased upon the advice of a physician for the mental health of a patient who has lost all of his or her hair from a disease.

Ineligible Expenses

According to the IRS, some expenses are not considered deductible health care expenses, and therefore are not eligible to be reimbursed through the Health Care FSA. Ineligible expenses include:

- Amounts reimbursed by any health plan
- COBRA premiums
- Cosmetic surgery, unless expenses are necessary to correct a deformity arising from, or directly related to, a congenital abnormality, a personal injury resulting from an accident or trauma, or a disfiguring disease.
- Covered expenses incurred before the effective date of your participation in the plan
- Covered expenses you also claim as a deduction on your federal income tax return
- Custodial care
- Fees for fitness or exercise classes, except when prescribed by a doctor as medically necessary
- Fees for weight loss programs, except when prescribed by a doctor as medically necessary
- Funeral and burial expenses
- Health and beauty supplies
- Health club memberships
- Marriage counseling
- Maternity clothing
- Over-the counter medications to treat illness or injury, unless ordered by a physician and accompanied by a prescription.

- Plan premiums or contributions for your coverage or that of your dependents under the Pearson medical, dental and vision plans

- Premiums for another health plan (such as your spouse's plan) or any other insurance policy

- Wigs (except when purchased upon the advice of a physician for the mental health of a patient who has lost all his or her hair from a disease).

Note: The eligibility of a deduction for these expenses is always subject to IRS review. Therefore, the Company cannot guarantee that the same expenses will always be eligible (or ineligible) for reimbursement from an account. Should the IRS change its ruling concerning the eligibility of a particular expense, the Plan will accept the ruling effective on the date the IRS publishes its rule. However, any such change by the IRS in the tax-deductible status of an expense does not allow you to stop or start contributions to an account.

Reimbursement

With the Health Care FSA, you can be reimbursed for eligible expenses up to the full amount you choose to deposit for the year – whether or not your current balance is sufficient to cover the amount to be reimbursed.

The IRS requires you to keep documentation associated with reimbursement from your FSA. Make sure you keep copies of all invoices, receipts and claim forms as you might be required to produce them in the event you are asked to verify a claim by Mercer or are audited by the IRS.

How To File A Claim

To receive reimbursement from your Health Care FSA, you can use your Mercer Marketplace Debit Card or log into the Pearson Benefits Marketplace.

Tax Considerations

The IRS allows you to deduct unreimbursed health care expenses on your federal income tax return if they exceed 10% of your adjusted gross income. Health care expenses, to the extent reimbursed through your Health Care FSA or through any other health plan, cannot be deducted on your federal income tax return.

You should consult with your personal tax advisor to determine whether the Health Care FSA makes sense for you.

Combination (Combo) FSA

The Combination (Combo) FSA allows you to set aside money from your pay on a pre-tax basis to pay for eligible health care expenses not covered by any medical, dental or vision care program.

Employees enrolled in a Health Savings Account (HSA) may also enroll in the Combination FSA for additional tax savings on dental and vision services. Once you meet the IRS-required deductible amounts of $1,350 for individual coverage or $2,700 if you cover dependents for medical services, you can then use your Combination FSA for medical and prescription expenses, too. Please keep in mind that just like the Health Care FSA, the Combo FSA has a “use it or lose it” rule. This means you will forfeit any money left in your FSA at the end of the year. Because of this, it’s smart to estimate your 2019 expenses before locking in your FSA contribution amount.

How To File A Claim

To receive reimbursement from your Combo FSA, you can use your Mercer Marketplace Debit Card or log into the Pearson Benefits Marketplace.

Health Spending Accounts Overview

When choosing your plan, it’s important to consider the tax-free accounts each plan might be paired with. The health accounts you are eligible for depends on the medical plan you choose. See the chart below to see how the health accounts work.

	Health Savings Account (HSA)	Combination FSA Pairs with the HSA	Health Care FSA
Who’s eligible?	Employees enrolled in the $1,850 medical option or the $2,850 medical option	Employees enrolled in an HSA looking for additional tax savings	Employees enrolled in the $400 medical option or the $900 medical option and others not enrolled in an HSA
Who contributes?	You and Pearson	You	You
What does it cover?	Eligible medical, dental, and vision expenses	Eligible dental and vision expenses only, until IRS deductible is met* then medical/Rx	Eligible medical, dental, and vision expenses
What is the 2020 annual limit?	$3,550 single/$7,100 family	$2,700	$2,700
Use it or lose it at year-end?	No	Yes	Yes
Can you use it to save for future health expenses?	Yes	No	No
Can you invest your money?	Yes, for additional tax-free earning potential once your account has reached a minimum balance	No	No
Is the money always yours to keep?	Yes, even if you leave Pearson or enroll in a non-CDHP option in the future	No	No

**Once you meet the 2020 IRS-required deductible amounts of $1,400 for individual coverage or $2,800 if you cover dependents, for medical/Rx services, you can then use your Combination FSA for medical and prescription expenses.*

Dependent Day Care FSA

The Dependent Day Care FSA allows you to set aside money from your pay before taxes are taken out to pay for eligible dependent care expenses. The expenses must be necessary to allow you – or if you are married, you and your spouse – to work or to enable your spouse to attend school full-time (unless your spouse is disabled). After you pay for these expenses, you can be reimbursed with tax-free money from your dependent day care account.

How Much You Can Deposit

You can deposit between $120 and $5,000 each calendar year in the Dependent Day Care FSA (but see the next section on the maximum tax-free reimbursement you can receive). Your deposit is deducted from your paycheck in equal amounts each pay period before income taxes and Social Security taxes are taken out.

Maximum Tax-Free Reimbursement

Generally, amounts reimbursed from your Dependent Day Care FSA are tax-free to you. However, federal law provides that the amount excluded from your gross income cannot exceed the lesser of:

- $5,000 ($2,500 if you are married and filing separate federal income tax returns);
- Your annual income; or
- Your spouse's annual income.

If your spouse is (1) a full-time student for at least five months during the year or (2) physically and/or mentally handicapped, there is a special rule to determine his or her annual income. To calculate the income, determine your spouse's actual taxable income (if any) earned each month that he or she is a full-time student or disabled. Then, for each month, compare this amount to either $250 (if you claim expenses for one dependent) or $500 (if you claim expenses for two or more dependents). The amount you use to determine your spouse's annual income is the greater of the actual earned income or these assumed monthly income amounts of either $250 or $500. By making an election under the Plan to contribute to a Dependent Day Care FSA, you are representing to the Company that your contributions to the Dependent Day Care FSA are not expected to exceed these limits.

If you are married and filing separate federal income tax returns, the $2,500 limit described above will not apply if you are (1) legally separated or (2) your spouse did not reside with you for the last six months of the calendar year, you maintained a household that was your dependent's primary residence for more than six months during the year and you paid more than half of the expenses of that household.

The $5,000 maximum limit is a household limit if you are married filing a joint federal income tax return. Therefore, if both you and your spouse participate in a dependent care assistance plan (through Pearson or through another employer), your combined maximum tax-free benefit is $5,000 in a calendar year.

To qualify for tax-free treatment, you are required to list on your federal income tax return the names and taxpayer identification numbers of any person who provided you with dependent care services during the calendar year for which you have claimed a tax-free reimbursement. The identification number of a care provider who is an individual and not a care center is that individual's social security number. Your care provider should be made aware of this reporting requirement.

The amount of your Dependent Day Care FSA deposit will automatically be reported on your W-2 form.

Eligible Dependents

You can claim dependent care expenses for:

- Any child under age 13 who can be claimed as your dependent for federal income tax purposes
- Your spouse who is physically or mentally unable to care for himself or herself and who lives with you for more than one-half of the year
- Any other person who is physically or mentally unable to care for himself or herself, who lives with you for more than one-half of the year and who can be claimed as your dependent for federal income tax purposes (without regard to gross income).

For expenses related to services outside your home to be eligible, a dependent (other than a child under age 13) must spend a minimum of eight hours a day in your home.

Eligible Expenses

You can use the money you deposit in this account to pay dependent day care expenses you incur in order to work. If you are married, your spouse must also work, be a full-time student or be disabled.

The following expenses for dependent care are eligible for reimbursement through the Dependent Day Care FSA:

- Childcare in your home or someone else's home
- Dependent care center that meets all state and local licensing requirements, if the center cares for more than six individuals

- Pre-school, up to but not including first grade; provided, that coverage for kindergarten requires documentation that the costs incurred are not educational expenses
- Summer day camp
- Certain expenses for a live-in, full-time housekeeper who provides dependent care in your home
- A relative who provides care, as long as the relative is not your dependent and is not your child under age 19
- After-school childcare
- Adult day care, either in your home or in an adult day care center.

To make sure your situation and the type of care being provided meet IRS requirements, refer to IRS Form 2441 and IRS Publication 503, “Child and Dependent Care Expenses.” In addition, you should know that if you use a dependent care provider inside your home you may be considered the employer of that individual and may be responsible for withholding and paying employment taxes. For more information, refer to IRS Publication 926, “Employment Taxes for Household Employees.” These forms and publications are available on the IRS’ website (www.irs.gov).

Ineligible Expenses

According to the IRS, some expenses are not eligible for reimbursement through a Dependent Day Care FSA. These include:

- Health care expenses for your dependents
- Education expenses for a child in the first grade or above, or the portion of the costs of kindergarten which relate to the education of the dependent
- Twenty-four-hour nursing home care
- Overnight camp
- Care provided by someone you claim (or could claim) as a dependent on your federal income tax return
- Care provided by your child who is under age 19
- Transportation to and from school or day care
- Baby-sitting expenses during non-working hours
- Expenses incurred while you are not working due to vacation or illness

- Food or clothing expenses
- Dependent care expenses you claim on your federal income tax return
- Expenses incurred when you were not contributing to the Dependent Day Care FSA
- Care in an unlicensed day care center, if the center cares for six or more individuals.

Reimbursement

With the Dependent Day Care FSA, you can be reimbursed only up to your current account balance. If your claim is for an amount greater than what is currently in your account, your claim will be held until there is enough money in your account to cover your claim.

After you have claimed reimbursements totaling your deposit for the plan year so that your account balance is zero, no remaining or additional claims for that plan year will be paid.

How To File A Claim

To receive reimbursement from your Dependent Day Care FSA, you can use your Mercer Marketplace Debit Card or log into the Pearson Benefits Marketplace.

Comparing the Dependent Day Care FSA and Tax Credit

A federal tax credit is available for the same dependent care expenses that can be reimbursed through the Dependent Day Care FSA. The tax credit is an alternative to reimbursement from the FSA. As a general rule, the higher your gross family income, the less valuable the tax credit becomes to you. Whether it is better for you to contribute to an FSA or take advantage of the tax credit depends on your individual circumstances. Here is a general approximation of how they compare:

- The tax credit allows you to subtract a part of your expenses directly from the federal income taxes you owe. With the FSA you reduce your taxable income by the amount of your contributions. This, in turn, reduces the total taxes you owe. The tax advantage of the FSA depends on you being able to exclude any reimbursement from your gross income for tax purposes (see above). In general, you can exclude up to $5,000, unless you are married filing a separate income tax return, in which case you can exclude only $2,500.
- The expenses you can apply toward the tax credit are limited to $3,000 if you have one dependent and $6,000 if you have more than one. With the FSA, your IRS filing status, rather than the number of dependents you have, determines the amount of reimbursement that you can exclude from your gross income.

Determining whether the Dependent Day Care FSA is more advantageous than the tax credit is a determination which depends on several factors. You should consult your personal tax advisor before making your election.

Another tax credit available under current tax law is the earned income credit. This credit also reduces dollar-for-dollar the federal tax you have to pay, but is calculated somewhat differently from the childcare credit. Again, you should consult your personal tax advisor to determine whether the Dependent Day Care FSA makes sense for you.