



COMPLIANCE BULLETIN

HIGHLIGHTS

- As a general rule, amounts in an employee's HSA are not forfeitable and cannot be returned to the employer.
- However, the IRS allows for the return of HSA contributions in limited situations.
- The IRS recently recognized an employer's ability to recover HSA contributions that were made by mistake.

RESOURCES

- [IRS Information Letter 2018-0033](#)
- [IRS Notice 2008-59](#)
- [Code Section 223](#)

Provided By:
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IRS Allows Employers to Recover Mistaken HSA Contributions

OVERVIEW

The IRS recently released an [information letter](#) describing circumstances that would allow an employer to recover contributions mistakenly made to its employees' HSAs.

Previously, IRS guidance allowed employers to recover HSA contributions in very limited situations, such as when the contribution exceeded the applicable annual limit. The new guidance also allows employers to recover HSA contributions when there is clear documentary evidence showing there was an administrative or process error.

In addition, the new IRS information letter provides specific examples of common administrative or process mistakes that occur when administering HSA contributions.

ACTION STEPS

This is helpful guidance for employers that administer HSA contributions. Employers that recover mistaken HSA contributions should maintain documentation showing that a mistake occurred. Also, any correction should put the employer and employees in the same position they would have been had the mistake not occurred.

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HSAs – In General

An HSA is a tax-exempt trust or custodial account that an eligible individual sets up with a qualified financial institution. Amounts in an HSA can be accumulated over years or distributed on a tax-free basis to pay for (or reimburse) qualified medical expenses.

Anyone can make contributions to an individual's HSA, including the individual's employer. However, there is a cap on the amount of HSA contributions for each year that varies depending on whether the HSA owner has individual or family HDHP coverage.

Internal Revenue Code (Code) [Section 223](#) contains the basic tax rules governing HSAs. One of these rules is that an individual's balance in his or her HSA is nonforfeitable. This means that, generally, contributions an employer makes to an employee's HSA belong to that employee and cannot be forfeited or returned to the employer.

IRS Notice 2008-59

In Notice 2008-59, the IRS clarified **limited circumstances** under which an employer may recoup contributions that it makes to an employee's HSA. These limited circumstances are:

- ✓ If an employee was **never eligible** for HSA contributions (that is, the employee never met the eligibility criteria for an HSA); or
- ✓ If an employer contributes amounts to an employee's HSA that **exceed the maximum annual contribution amount** due to an error.

In these circumstances, Notice 2008-59 says, the employer may request that the financial institution return to the employer the mistaken or excess amounts contributed to the employee's HSA.

However, Notice 2008-59 also states that the employer may not recover amounts contributed that are less than or equal to the maximum annual contribution limit, even if made in error. Also, Notice 2008-59 says that if an employer contributes to the HSA of an employee who ceases to be an eligible individual during a year, the employer may not recover contributions made after the employee stopped being eligible.

New IRS Information Letter

The IRS' Office of Chief Counsel recently released an [information letter](#) (Letter 2018-0033) that clarifies the ability of employers to recover contributions to employees' HSAs that **were made by mistake**. This information letter expands on the guidance in IRS Notice 2008-59 by allowing employers to recover HSA contributions in more situations.

The IRS information letter clarifies that employers may ask financial institutions to return HSA contributions made due to an administrative error or process mistake. Employers should maintain records showing the error or mistake.

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According to this letter, IRS Notice 2008-59 does not provide an exhaustive list of when HSA contributions may be returned to an employer. Rather, if the employer has **clear documentary evidence showing an administrative or process error**, an employer may request that the financial institution return the amounts to the employer, as long as the parties are put in the same position that they would have been had the error not occurred.

Some examples of correctible errors include:

- ✓ An amount withheld and deposited in an employee's HSA for a pay period that is greater than the amount shown on the employee's HSA salary reduction election.
- ✓ An amount an employee receives as an employer contribution that the employer did not intend to contribute but was transmitted because an incorrect spreadsheet is accessed or because employees with similar names are confused with each other.
- ✓ An amount an employee receives as an HSA contribution because it is incorrectly entered by a payroll administrator (whether in-house or third-party) causing the incorrect amount to be withheld and contributed.
- ✓ An amount an employee receives as a second HSA contribution because duplicate payroll files are transmitted.
- ✓ An amount an employee receives as an HSA contribution because a change in employee payroll elections is not processed timely, so that amounts withheld and contributed are greater than (or less than) the employee elected.
- ✓ An amount an employee receives because an HSA contribution amount is calculated incorrectly, such as a case in which an employee elects a total amount for the year that is allocated by the system over an incorrect number of pay periods.
- ✓ An amount an employee receives as an HSA contribution because the decimal position is set incorrectly, resulting in a contribution greater than intended.

Employers that recover HSA contributions made by mistake should maintain documentation to support their position that an administrative or process error occurred.