



IRS Helps Employers Recover Mistaken HSA Contributions

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The Internal Revenue Service (IRS) has released Information Letter 2018-0033 which lists seven new examples of situations where an employer can obtain a return of contributions made to an employee's health savings account (HSA).

Employers should review the examples of mistaken HSA contributions in the Information Letter (as discussed below), and implement procedures to prevent any of the mistakes from taking place. If the employer does in fact make a mistaken HSA contribution, it should contact the HSA trustee or administrator to request a return of the money, using one or more of the IRS examples as justification.

■ Background

Individuals have a "nonforfeitable" interest in the balance of their HSA. Under this general rule, an employer (or other third party, such as creditor) may not access an employee's HSA to obtain funds, including a return of employer contributions.

The IRS previously released Notice 2008-59, which contains three examples illustrating how the general rule operates in different situations. Two of the three examples in Notice 2008-59 relax the general rule, at least in part.

Examples in Notice 2008-59	IRS Conclusion
An employer contributes amounts to an employee's HSA that exceed the maximum annual contribution allowed by law due to an error	The employer may correct the error by contacting the HSA financial institution to obtain a return of the contribution to the employer; if the employer does not recover the money by the end of the taxable year, the contribution is treated as taxable income to the employee on Form W-2
An employer contributes to the HSA of an employee who was never eligible for HSA contributions	Same as above
An employer contributes to the HSA of an employee who was eligible for HSA contributions at the start of the year, but who ceases to be eligible for HSA contributions during the year	The employer cannot recoup any contribution from the employee's HSA

■ IRS Information Letter 2018-0033

The latest Information Letter contains seven new examples of situations where an employer may recover contributions made to an employee's HSA.

The IRS states, in the Information Letter, that if there is “clear documentary evidence” demonstrating that an administrative or process error occurred, then the financial institution holding the employee's HSA contributions can return them to the employer, provided that the correction puts the employer and employee in the same position that they would have been in had the error not occurred.

The Information Letter lists the following examples of “errors which may be corrected” by allowing the employer to recover contributions made to an employee's HSA.

The examples set forth below are listed in the Information Letter, while the recovery amounts are based on our analysis of what the employer's and employee's position would have been without the administrative or process error:

Examples in Information Letter 2018-0033	Recovery Amount
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	The employer may obtain a return of the amount contributed to the HSA that exceeds the employee's HSA salary reduction election
An amount that 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	The employer may obtain a return of the entire amount of the employer contribution
An amount that 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	The employer may obtain a return of the amount contributed to the HSA that exceeds the employee's HSA salary reduction election
An amount that an employee receives as a second HSA contribution because duplicate payroll files are transmitted	The employer may obtain a return of the second or duplicate HSA contribution
An amount that 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 what the employee elected	The employer may obtain a return of the amount contributed to the HSA that exceeds the employee's payroll election (in accordance with the change in the employee's payroll election)
An amount that an employee receives because an HSA contribution 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	The employer may obtain a return of the amount contributed to the HSA that exceeds the employee's HSA salary reduction election (as correctly calculated)
An amount that an employee receives as an HSA contribution because the decimal position is set incorrectly, resulting in a contribution greater than intended	The employer may obtain a return of the amount contributed to the HSA that exceeds the employee's HSA salary reduction election, with the decimal point set correctly

■ Timing

The changes outlined in Notice 2008-59 permit the employer to recover funds so long as the recovery occurs while the applicable tax year is open. For example, if an employer contributed to the HSA of an employee who was never HSA eligible in 2018, the employer may seek to recoup its incorrect HSA contribution in 2018. If the amount is not recovered in 2018, then the employer is to treat the impermissible employer contribution as taxable income reflected on the 2018 Form W-2.

Unfortunately, Information Letter 2018-0033 did not include guidance as to the proper timing to recover mistaken or incorrect employer HSA contributions. While it may be reasonable to follow the guidance in Notice 2008-59 (which is generally to correct in the open tax year or treat as additional taxable on the Form W-2 if not recovered), further clarification on this point would be helpful.

■ Employer Action

Employers should review the examples of mistaken HSA contributions discussed above, and implement procedures to prevent any of the mistakes from taking place.

When a mistaken contribution is made to an employee's HSA that fits one of the examples listed in the Information Letter or in Notice 2008-59, the employer should contact the HSA trustee or administrator (usually the bank) to recover the contribution. The employer should maintain documentation to support its assertion that a mistaken contribution occurred, in case of any future IRS inquiry.

The following FAQs address some other questions that may arise.

Frequently Asked Questions

Q1. Is the HSA trustee or administrator obligated to allow the employer's recovery of mistaken HSA contributions in accordance with the Information Letter and Notice 2008-59?

A1. This issue is not addressed in the IRS guidance. Employers should review their contract with the HSA trustee or administrator in advance, to determine whether the contract permits recoupment in certain circumstances.

Q2. What if the mistaken contribution does not fit into one of the IRS examples?

A2. IRS acknowledges in the Information Letter that the examples in the Information Letter and in Notice 2008-59 are not intended to provide an exclusive set of circumstances in which contributions made to an HSA may be returned to an employer. However, the HSA trustee or administrator may refuse the employer's request to recover contributions made to an employee's HSA unless the facts of the situation fit into one of the IRS examples.