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IRS Clarifies Employer's Ability to Recover Mistaken HSA Contributions

INTRODUCTION

On December 28, 2018, the IRS issued Information Letter Number 2018-0033 (<https://www.irs.gov/pub/irs-wd/18-0033.pdf>), which provides clarification about the situations in which an employer may attempt to recoup a mistaken contribution to an employee's Health Savings Account (HSA). Specifically, the letter provides additional examples of HSA contributions, resulting from administrative or processing errors that an employer may try to recoup.

BACKGROUND

In general, employer contributions to an employee's HSA are nonforfeitable, except in limited circumstances:

1. When the employee was never actually eligible to establish an HSA; or
2. When the employer erroneously contributes too much to an employee's HSA because of an administrative error.

The nonforfeitable rule, along with the two exceptions above, was discussed in Q/A-23 and Q/A-24 in IRS Notice 2008-59 (located at <https://www.irs.gov/pub/irs-drop/n-08-59.pdf>). However, the IRS indicated in 2015¹ that the situations outlined in IRS Notice 2008-59 were not exhaustive, and that an employer may request a return of mistaken contributions if there is clear, documentary evidence of an administrative or process error. IRS Information Letter Number 2018-0033 confirms this stance.

ANALYSIS

The information letter provides several examples of situations that would be considered "administrative process errors":

- 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 unintended employer contribution that was transmitted because an incorrect spreadsheet was accessed or because employees with similar names were confused with each other;
- A contribution received by an employee because an incorrect entry by a payroll administrator (whether in-house or third-party) caused the incorrect amount to be withheld and contributed;
- A second HSA contribution received by an employee because duplicate payroll files were transmitted;
- A contribution received by an employee because a change in employee payroll elections was not processed in a timely manner, so amounts withheld and contributed are greater (or less) than the employee elected;
- An amount that an employee receives because the HSA contribution amount was calculated incorrectly, e.g., if an employee elects a total amount for the year that is allocated by the system over an incorrect number of pay periods; and
- An amount that an employee receives as an HSA contribution because the decimal position was set incorrectly, resulting in a greater than intended contribution.

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In issuing IRS Information Letter 2018-0033, the IRS is confirming its stance that an employer may attempt to recoup its contributions in an expanded set of circumstances. Provided that the employer can provide clear, documentary evidence that a contribution was made as the result of an administrative or processing error, it may attempt to recoup its contributions in order to put the employee and employer in the same position they would have been in if the error had not occurred. This is true even if there was neither a mistake about an individual's HSA-eligibility nor any contribution in excess of the individual's annual maximum.

SUMMARY

This IRS Information Letter provides helpful information describing the IRS's viewpoint on the nonforfeitability rule, confirming the view that it expressed previously. Note that an HSA trustee or custodian is not obligated to return an employer's contributions. If an employer is unable to recoup its erroneous contributions, it should make appropriate adjustments to the affected employee's W-2 to include the contributed amounts in the employee's gross wages and income.

As always, should you have any questions, please contact your Parker, Smith & Feek Benefits Team. While every effort has been taken in compiling this information to ensure that its contents are totally accurate, neither the publisher nor the author can accept liability for any inaccuracies or changed circumstances of any information herein or for the consequences of any reliance placed upon it.

REFERENCES AND RESOURCES

1. IRS Information Letter to Dennis Triplett and Kevin McKechnie (Sept. 9, 2015) from Harry Beker, Chief, Health and Welfare Branch, IRS Office of Associate Chief Counsel