BDO KNOWS:
COMPENSATION AND BENEFITS

SUBJECT

IRS PROVIDES RELIEF FOR 2018 FAMILY HEALTH SAVINGS ACCOUNTS

SUMMARY

For 2018, taxpayers who qualify for a family Health Savings Account can treat $6,900 as the maximum deductible contribution, notwithstanding changes made to the inflation adjustment calculations by the Tax Cuts and Jobs Acts that reduced the 2018 limit to $6,850. Any taxpayer who had funds withdrawn from their HSA to comply with the $6,580 limitation can treat the distribution as a mistake and return the contribution to the HSA by April 15, 2019.

DETAILS

Background

Contributions to an HSA made by or on behalf of an individual are deductible up to the maximum annual contribution limit, which is adjusted for inflation annually. The maximum HSA contribution limit for individuals with family coverage under a high deductible healthcare plan (HDHP) for calendar year 2018 was originally set at $6,900 (per Rev. Proc. 2017-37 issued on May 4, 2017). The Tax Cuts and Jobs Act (TCJA), enacted in December 2017, subsequently changed the method for measuring annual inflation[1]. The IRS adjusted the 2018 maximum family HSA contribution limit to $6,850 to reflect the statutory amendment (per Rev. Proc. 2018-18 issued on March 2, 2018). No change was made to the self-only HSA contribution limit.

Upon receiving comments from employers and other stakeholders regarding the administrative and financial burdens of implementing this mid-year change, the IRS issued Rev. Proc. 2018-27 to allow taxpayers to treat the $6,900 annual limitation originally published in Rev. Proc. 2017-37 as the 2018 inflation adjusted limitation on HSA contributions for individuals with family coverage under an HDHP.

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1 PL 115-97, § 11002.

Procedures for Returned Excess Contributions

An individual who receives a distribution from an HSA of an excess contribution (with earnings) based on the $6,850 deduction limit (as published in Rev. Proc. 2018-18) may repay the distribution to the HSA and treat the distribution as the result of a mistake (under the reasonable cause provision of Q&A-37 of Notice 2004-50). Accordingly, the portion of a distribution (including earnings) that is repaid to an HSA by April 15, 2019, is not included in the individual's gross income or subject to the 20 percent additional tax under section 223(f)(4), and repayment is not subject to the six percent excise tax on excess contributions under section 4973(a)(5). However, an HSA trustee or custodian is not required to allow individuals to repay mistaken distributions.

Alternatively, an individual who receives a distribution from an HSA of an excess contribution (with earnings) based on the $6,850 deduction limit and does not repay the distribution to the HSA, may treat the distribution as an excess contribution returned before the due date of the individual's tax return. Thus, the excess contribution generally would not be included in gross income or subject to the 20 percent additional tax, provided the distribution is received on or before the due date (including extensions) for filing the individual's 2018 income tax return. This treatment does not apply to distributions from an HSA that are attributable to employer contributions (including cafeteria plan elections) if the employer does not include any portion of the contribution in the employee's wages because the employer treats $6,900 as the annual limitation on the deductions. In this situation, the distribution from the HSA must be used to pay qualified medical expenses to avoid including the amount in the employee's income and subjecting it to the 20 percent additional tax.

BDO INSIGHTS

For plan sponsors and administrators who have not yet taken any action to implement the reduced limit of $6,850, Rev. Proc. 2018-27 allows plan operations to continue as usual without any adjustments to the originally announced limit of $6,900.

For plan sponsors and administrators who have already adjusted HSA contributions for the remainder of the year so as not to exceed the $6,850 contribution limit, the employer may either maintain the reduced limit or reinstate the original limit and readjust the contributions for the remainder of the year so as not to exceed $6,900.

These changes are confined to a narrow population of an employer's HSA accounts – those employees with family coverage under a HDHP who *maximize* their employer contributions to an HSA (including cafeteria plan elections). Other employees with family coverage whose salary reductions and other employer contributions to their HSA accounts that will not approach the limit are not impacted. Similarly, eligible employees with self-only coverage who contribute to HSAs are not affected since the TCJA did not result in any change to the HSA contribution limit of $3,450 for self-only coverage.