SEYFARTH SHAW

One Minute Memo®

IRS Retroactively Reduces HSA Contribution Limit; Transition Relief May Follow

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Last year, the IRS published the calendar year 2018 health savings account (HSA) contribution limits for individual and family coverage. *Rev. Proc. 2017-37, I.R.B. 2017-21 (5/4/2017)*. Ten months later and well into the start of the 2018 year, in response to changes under the 2017 Tax Cuts and Jobs Act, the IRS reduced by $50 the 2018 limit on HSA contributions for family coverage. *Rev. Proc. 2018-18, I.R.B. 2018-10 (3/5/2018)*. Although the HSA contribution limit for individual coverage remains at $3,450, the maximum contribution for family coverage dropped from $6,900 to $6,850. The reduction took effect immediately.

The amount of the reduction is small, but employees with family coverage in an HSA may feel the effects in their tax bills for 2018. To the extent contributions to an HSA exceed the annual limit, the amount of those excess contributions is included in the employee's taxable income and subject to an additional 6% excise tax. Absent transition relief from the IRS, to avoid the negative tax ramifications of the lowered contribution limit, the employee will need to receive a distribution from the HSA during 2018 in the amount contributions exceed $6,850, plus any earnings on that amount. The excise tax is cumulative, so for every future year the excess contribution remains in the HSA, the employee will be subject again to the excise tax.

Transition relief could be on the horizon. In mid-March, two members of the House Ways and Means Committee, Representatives Mike Kelly (R-PA) and Erik Paulsen (R-MN), wrote to Treasury Secretary Steven Mnuchin, identifying burdens the mid-year limit change inflicts on employees and employers and requesting a delay until 2019 of enforcement of the new contribution limit. Joining Reps. Kelly and Paulsen, the American Benefits Council, a prominent organization representing hundreds of plan sponsors and service providers (and of which Seyfarth Shaw is a member), likewise sought an enforcement delay or similar transition relief from Treasury and the IRS. Treasury and the IRS have acknowledged the concerns voiced by the Representatives and the American Benefits Council and expedited their consideration of potential transition relief.

In light of the high-profile feedback regulators are receiving and the regulators' concomitant discussions of transition relief, we do not believe employers and service providers need to take immediate action on the HSA limit reduction. Unless they have already implemented modifications to accommodate the new limit, for the present, sponsors and administrators may prefer to hold off on HSA program changes to see whether relief is forthcoming.

If, however, a sponsor or administrator prefers to take action now on the HSA limit change, we suggest a few steps to help minimize the effects of contribution limit reduction:

- Notify employees electing family HDHP coverage of the reduced HSA contribution limit;

- Evaluate whether payroll and plan administration systems require modifications to accommodate the reduced limit for the balance of 2018; and

    - **For employers forwarding contributions monthly:** For employees who have already contributed more than $571 (1/12 of $6,850) per month during 2018, advise employees to modify their monthly elections for the remainder of the year so they do not exceed $6,850 for the year; or

    - **For employers funding HSAs in full at the beginning of the plan year:** Contact the HSA custodian and request a return of excess contributions. If the custodian is unwilling to return excess contributions at the employer's request, advise affected employees to contact the custodian and request a return of excess contributions.

We anticipate decisions on transition relief to occur shortly. We will continue following the developments out of Washington and will publicize promptly any significant germane announcements from Treasury or the IRS.

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