* 1. **What happens when account owners mistakenly use an HSA for a non-qualified expense?**

HSA account owners that mistakenly take distributions from their HSAs have an opportunity to fix the mistake through special rules for the return of mistaken distributions.[[1]](#endnote-1) The HSA account owner had to have made the mistake due to a reasonable cause and be able to support that with clear and convincing evidence. The HSA account owner should save the evidence along with other tax documents in the case of an IRS audit in the case. The HSA custodian will generally not request any evidence as the custodian can rely on the representation of the HSA account owner that the distribution was a reasonable mistake supported by evidence.

The HSA account owner must repay the mistaken distribution amount to the HSA prior to the tax filing due date for the year the HSA account owner knew or should have known of the mistake. Custodians generally provide a form for this purpose. Failure to notify the HSA custodian that the reason for the contribution is the return of mistaken distribution will result in incorrect IRS reporting. HSA custodians are not required to accept the return. In that case, the HSA account owner would have to pay taxes plus a 20% penalty on the amount of the mistaken distribution.

#### HSA account owners generally do not report the mistaken distribution on their income tax return and the HSA account owner correspondingly also does not report the return of the amount to the HSA. If the mistaken distribution is corrected in the same year as it’s made, then no reporting is necessary. The HSA custodian will not include the original mistaken distribution as a distribution on the 1099-SA or the return of the money as a contribution on the IRS form 5498-SA. If the custodian already filed the 1099-SA, it will need to do a corrected 1099-SA.[[2]](#endnote-2)

1. IRS Notice 2004-50, A37. [↑](#endnote-ref-1)
2. IRS Instructions for Form 1099-SA and 5498-SA. [↑](#endnote-ref-2)