



IMPORTANT NOTICE REGARDING DEBIT CARD TRANSACTIONS

As your administrator, we want to be sure you understand IRS requirements that may require action on your part as an employer. We also want you to be aware of steps PacificSource Administrators is taking to ensure that your plan remains in compliance with regulations. Earlier this year, the IRS released a Chief Counsel Advice (CCA) memorandum that provided further guidance on how to correct health FSA payments for expenses that are:

- not properly substantiated or
- later determined to be ineligible for reimbursement (improper payments).

We have provided an overview of the memorandum below. To review the original document, visit: <http://www.irs.gov/pub/irs-wd/1413006.pdf>.

- *Debit Card Correction Procedures.* The debit card correction procedures require five steps for improper debit card payments:
 - (1) deactivate the card,
 - (2) request repayment,
 - (3) withhold the payment from compensation (to the extent allowed by law),
 - (4) apply a claims substitution or offset, and
 - (5) treat the payment as any other business indebtedness (i.e., the same steps an employer would take to collect an equivalent business debt).
- *Order of Correction Steps.* Steps 2–4 of the correction procedures can be taken in any order, so long as the order is consistently applied for all participants. In contrast, **step 5 may only be applied after the employer has pursued all correction methods in the other steps.**
- *Reporting Improper Payments.* When step 5 is applied, the employer must first request payment consistent with its collection procedures for other business debts. If the payment is not recovered, the employer may forgive the indebtedness, in which case the payment should be reported as wages on Form W-2 for the year in which the indebtedness is forgiven. The reported amount is subject to withholding for income tax, FICA, and FUTA.

We take care of steps 1, 2, or 4. In order to keep your plan(s) in compliance with IRS guidance, we will be implementing some additional measures to help correct any improper payments or debit card transactions. The steps we currently take on your behalf are to deactivate the debit card (step 1), request repayment of the ineligible amount (step 2), or apply a claim substitution or offset for the ineligible amount (step 4).

We will provide reports. Once steps 1, 2 or 4 have been taken, we will provide reports detailing the transactions that have been designated as unrecoverable. These reports will provide the information you need to complete steps 3 and 5.

If withholding the payment amount (step 3) isn't an option, and you can't recover the funds otherwise, you must report the payments as wages on the employee's Form W-2 (step 5).

In early 2015, we will contact clients who offer the debit card to their employees and provide additional details about how to handle any unrecoverable transactions.

Questions? We're happy to help. Please contact us at (800) 422-7038 or psacustomerservice@pacificsource.com.