

**Office of Chief Counsel
Internal Revenue Service
Memorandum**

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subject: Health Savings Accounts - Ability to Levy

This Chief Counsel Advice responds to your request for assistance dated March 12, 2009. This advice may not be used or cited as precedent.

ISSUES

Whether the Service's levy under section 6331 of the Internal Revenue Code attaches to a taxpayer's Health Savings Account (HSA) established pursuant to section 223 and, if so, whether levy on an HSA results in the additional 10 percent tax liability imposed by section 223(f)(4)(A).

CONCLUSIONS

A levy extends to a taxpayer's interest in an HSA. A taxpayer is liable for the additional 10 percent tax on the amount of levy unless, at the time of levy, the taxpayer had attained the age of 65 or was disabled (as defined in section 72(m)(7)).

LAW AND ANALYSIS

If a person neglects or refuses to pay a tax liability, section 6331 provides that the Service may levy "upon all property and rights to property" of the taxpayer except property that is exempted from levy under section 6334. An HSA is a "trust created or organized in the United States as a health savings account exclusively for the purpose

of paying the qualifying medical expenses of the account beneficiary.” I.R.C. § 223(d)(1). An account beneficiary is the individual who establishes an HSA. I.R.C. § 223(c)(3). The HSA trust or custodian account is tax-exempt and is established through a written governing instrument under state law. See Notice 2008-59, Q&A-38, 2008-29 I.R.B. 123. Banks, credit unions, insurance companies, and other financial institutions serve as trustees or custodians for HSAs. I.R.C. § 223(d)(1)(B). The account beneficiary (taxpayer) that establishes the HSA owns and controls the funds in his or her HSA. The account beneficiary may receive a distribution at any time. Notice 2004-2, Q&A-24, 2004-1 C.B. 269.

The account beneficiary makes decisions regarding which qualified medical expenses are paid from the account and how the money in the account is invested. The HSA trustee or account custodian is not required to determine whether the distributions are used for qualified expenses. The funds in the HSA roll over from year to year.

The account beneficiary is entitled to a distribution for any purpose and the HSA trust or custodial agreement may not contain a provision that restricts the HSA to distributions for the account beneficiary’s qualified medical expense. Notice 2004-50, Q&A 80, 2004-2 C.B. 196. Further, the account beneficiary’s interest in the HSA is nonforfeitable under section 223(d)(1)(E). State law determines whether the taxpayer has a right in the property at issue. Drye v. United States, 528 U.S. 49, 58 (1999). The trust or custodial account is established by a state law instrument. The question of whether the state created right qualifies as property or rights to property is determined by federal law. Id. The right to withdraw funds from an account is a property interest subject to levy. United States v. National Bank of Commerce, 472 U.S. 713 (1985). Therefore, we conclude that the account beneficiary’s interest in an HSA constitutes “property” or “rights to property” that is subject to levy under section 6331.

A distribution from an HSA to pay “qualified medical expenses” is excludible from the account beneficiary’s gross income under section 223(f)(1). Qualified medical expenses are medical expenses as defined in section 213(d) (with modifications not relevant in this case). I.R.C. § 223(d)(2). A distribution from an HSA for any purpose other than qualified medical expenses is includible in the account beneficiary’s gross income under section 223(f)(2) and subject to an additional 10 percent tax under section 223(f)(4). However, the 10 percent tax does not apply if, at the time of the distribution, the account beneficiary was dead, had attained age 65, or was disabled (as defined in section 72(m)(7)). I.R.C. § 223(f)(4)(A), (B), (C); Notice 2004-2, Q&A-25, 2004-1 C.B. 269.

We agree that the additional 10 percent tax imposed by section 223(f)(4)(A) is similar to the additional 10 percent tax imposed by section 72(t). However, Congress amended section 72(t) in 1998 to exclude distributions on account of levy from the 10 percent tax on premature distributions. CCDM Notice N(36)000-2 (January 21, 1999) notes that “the Service will continue to assess section 72(t) tax unless a statutory exception applies.” Section 223(f)(4)(A) contains three express exceptions to the imposition of the

10 percent tax. A levy is not one of the three exceptions. For this reason, we believe that the levy exception in section 72(t) is not relevant to section 223(f)(4).

A levy on an HSA pursuant to section 6331 is not a distribution to pay qualified medical expenses. Therefore, we conclude that the account beneficiary is liable for the additional 10 percent tax imposed by section 223(f)(4) on the amount of the levy, unless, at the time of the levy, the taxpayer had attained age 65 or was disabled (as defined in section 72(m)(7)).

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call (202) 622-3630 if you have any further questions.