

WebMemo



Published by The Heritage Foundation

No. 1239
October 20, 2006

Building on the Successes of Health Savings Accounts

Greg D'Angelo and Robert E. Moffit, Ph.D.

Health Savings Accounts (HSAs) allow individuals with a high-deductible health plan to save pre-tax dollars in a personal, portable account for qualified medical expenses. Due to their lower costs and flexibility, HSA arrangements are rapidly gaining market share. Congress should build on the success of HSAs by clearing away several problems with their management and administration: (1) authorize individuals to fund HSAs with a one-time transfer from other health accounts; (2) allow individuals opening an HSA mid-year to contribute up to the yearly limit; (3) give employers the leverage to make higher contributions for low-wage workers; and (4) simplify compliance with contribution limits by indexing and adjusting amounts annually. These changes are included in the Health Opportunity and Patient Empowerment Act of 2006 (H.R. 6134).¹ In addition, Congress must make crucial changes in the federal tax code that would level the playing field for *all* health care options, including HSA-eligible plans.

What HSAs Deliver

HSAs' quick rise to popularity proves their attractiveness to consumers. HSA arrangements make up a small, but rapidly increasing, share of the health insurance market. According to a January 2006 survey conducted by America's Health Insurance Plans, nearly 3.2 million individuals are enrolled in HSA-qualified high-deductible plans, up from 438,000 in 2004.² The Kaiser Family Foundation recently reported that these new plans constitute 6 percent of the employer-based market, with 2.4

million individual employees enrolled.³ Conservative estimates project that one-quarter or more of employers not offering HSA-style plans now may offer them next year.⁴

HSA-style plans offer individuals three clear advantages that most other kinds of health insurance arrangements do not:

- **HSAs build savings.** HSA-style health plans enable individuals and families to save today for tomorrow's health care expenses, including those in retirement. No other mechanism in the current system—either in private employer-provided insurance or public government programs—is designed to fund future expenses. Considering the enormous unfunded liabilities that large private employers and government-managed health programs face, HSAs can provide individuals with future protection should these other sources of health care be scaled back or unavailable.

Individuals are taking advantage of HSAs to build up savings. According to a recent Government Accountability Office study, approximately 55 percent of individuals reporting HSA contributions in 2004 did not withdraw any funds

This paper, in its entirety, can be found at:
www.heritage.org/research/healthcare/wm1239.cfm

Produced by the Center for Health Policy Studies

Published by The Heritage Foundation
214 Massachusetts Avenue, NE
Washington, DC 20002-4999
(202) 546-4400 • heritage.org

Nothing written here is to be construed as necessarily reflecting the views of The Heritage Foundation or as an attempt to aid or hinder the passage of any bill before Congress.

from their accounts in the entire year.⁵ Of those who did make withdrawals, 90 percent used those funds for qualified medical expenses.⁶ A more recent Aetna study showed that 52 percent of its HSA members did not withdraw any funds in 2005, 28 percent withdrew some funds, and only 20 percent exhausted their accounts.⁷ As demonstrated by the way that individuals are using their accounts, HSAs represent a vast improvement in health insurance product development and design.

- **HSAs provide affordable coverage.** Critics of HSAs have been quick to question the effectiveness of these new plans in providing low-cost coverage. The preliminary data, however, refute this criticism. The Kaiser Family Foundation recently reported that HSA-qualified plan premiums are 20 to 30 percent lower than premiums in the general employer-based market,⁸ a finding confirmed in the individual market by a similar survey by eHealthInsurance.com,⁹ a large Internet-based health insurance broker. Likewise, a 2005 Deloitte survey found that HSA premiums increased at approximately one-third the rate of

traditional plan premiums.¹⁰ Reflecting these savings, data from several sources indicate that 30 to 40 percent of HSA-style plan participants were previously uninsured.¹¹

- **HSAs empower consumers.** HSAs engage individuals in health care decision-making; as a result, individuals are making better choices. Based on the early evidence, individuals with HSA-style plans are more likely to seek preventative care and routine treatments for chronic illnesses than individuals in conventional plans.¹² HSA-style plans, by design, create incentives for better utilization of services and encourage price and quality comparisons.

All individuals can benefit from an HSA-style plan. For those with low health care expenses, HSAs provide a sufficient level of health insurance, with catastrophic and preventative care coverage, while freeing up dollars for future health care expenses. Individuals with moderate health care expenses, while also benefiting from lower premiums, have the flexibility to be prudent consumers by exercising informed consumption choices. High-cost health care

1. As amended by the Committee on Ways and Means on September 29, 2006.
2. America's Health Insurance Plans, "January 2006 Census Shows 3.2 Million People Covered by HSA Plans," March 3, 2006, at www.ahipresearch.org/pdfs/HSAHDHPReportJanuary2006.pdf.
3. Kaiser Family Foundation, "Employer Health Benefits Survey 2006," § 8, at www.kff.org/insurance/7527/sections/ehbs06_sec8_print.cfm.
4. *Ibid.*
5. Government Accountability Office, "Consumer-Directed Health Plans: Early Enrollee Experiences with Health Savings Accounts and Eligible Health Plans," Report to the Ranking Minority Member, Senate Committee on Finance, GAO-06-798, August 2006.
6. *Ibid.*
7. Aetna HealthFund, "Making a Difference," September 2006.
8. Kaiser Family Foundation, "Employer Health Benefits Survey 2006," § 8, at www.kff.org/insurance/7527/sections/ehbs06_sec8_print.cfm.
9. eHealthInsurance, "Health Savings Accounts: January 2005-December 2005," May 10, 2006, at image.ehealthinsurance.com/content/ReportNew/2005HSASFullYearReport-05-10-06F.pdf.
10. Deloitte Center for Health Solutions, "Consumer-Driven Health Plan Cost Growth Significantly Slower than Other Plans," January 24, 2006.
11. America's Health Insurance Plans, "January 2006 Census Shows 3.2 Million People Covered by HSA Plans," March 3, 2006, at www.ahipresearch.org/pdfs/HSAHDHPReportJanuary2006.pdf; eHealthInsurance, "Health Savings Accounts: January 2005-December 2005," May 10, 2006, at image.ehealthinsurance.com/content/ReportNew/2005HSASFullYearReport-05-10-06F.pdf.
12. Aetna HealthFund, "Making a Difference," September 2006.

consumers, although unable to save as much for future health care consumption, can control how their money is spent by redirecting dollars from costly premiums to direct payment for goods and services that best meet their needs, preferences, and values—a powerful instrument generally unavailable under conventional, restrictive health plans.

The Next Step: A Level Playing Field

The Health Opportunity Patient Empowerment Act of 2006, recently passed by the House Committee on Ways and Means, includes needed management and administrative changes to HSAs. As good as these changes are, however, they are insufficient. Alone, HSAs will not fix the health care system. They work within a distorted health insurance market where tax policy favors the purchase of some health plans over others and where government officials and employers still choose health plans for most individuals. While health accounts are portable, the high-deductible plans are often still tied to the place of work.¹³

The next target for reform, then, should be the arbitrary and inequitable federal tax code, which unduly favors employer-based health insurance. Congress should fix this inequity and level the playing field. Health insurance offered by employers or government, and constrained by their incentives, cannot meet the needs, preferences, or values of all health care consumers. Nor can any single health insurance product. Individuals and families

need the freedom to make personal health care decisions without government officials picking winners and losers for them.

Meanwhile, Congress should refrain from adding another layer of distortion by giving individuals a tax break or credit to purchase *only* HSA-qualified plans. This preference would run counter to tax neutrality, equitability, and simplification. Government involvement in the health insurance marketplace, though perhaps well intentioned, will ultimately stifle rather than enhance freedom of choice for health care consumers. A better policy would be a tax credit applicable to any kind of health coverage.¹⁴

Conclusion

HSAs promise substantial benefits for millions of Americans, but Congress must realize that for a market to be truly competitive and consumer-driven, it is necessary to have multiple, viable products whose merits can be tested on a level playing field by informed and empowered consumers. Congress should move forward in making HSAs better and more attractive to consumers, but the biggest gains will be had by fixing the tax treatment of health insurance in a way that gives individuals real choice.

Greg D'Angelo is Research Assistant in, and Robert E. Moffit, Ph.D., is Director of, the Center for Health Policy Studies at The Heritage Foundation.

13. Of the estimated 3.2 million enrolled in HSA-qualified plans, approximately 75 percent obtain coverage through an employer.

14. See Nina Owcharenko, "Health Care Tax Credits: Designing an Alternative to Employer-Based Coverage," Heritage Foundation *Backgrounder* No.1895, November 8, 2005, at www.heritage.org/Research/HealthCare/bg1895.cfm.