

HEALTH SAVINGS ACCOUNTS

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Health Savings Accounts - Outline

- Health Savings Account- HSA
 - What are they?
 - Nifty features
 - Account requirements
 - Contributions
 - Distributions
- The High Deductible Health Plan- HDHP
- Comparison with the MSA and HRA
- Why I think the HSA Will Help Reduce High Trend
- Conclusion

Health Savings Accounts- What are they?

- Tax Exempt Trust Used to Pay Medical Expenses
- Combined with a High Deductible Health Plan (HDHP)
 - HDHP covers large expenses after minimum \$1000/\$2000 individual/family deductible
 - HSA used to accumulate funds to cover current and future routine medical care not covered under the HDHP
- Available 1/1/2004
 - Part of the Medicare Prescription drug act signed into law 12/8/2003

Health Savings Accounts- Nifty Features

- HSA- 100% Vested and Fully Portable
 - You always own the account- a lifetime healthcare savings vehicle
 - No use it or lose it provision
- Triple Tax Advantaged- IRA on steroids
 - Contributions are pretax; don't have to itemize to deduct; no income limit as there is with IRAs
 - Investment income is not currently taxed; no limit on fund balance
 - Disbursements for qualified medical expenses are never taxed
- Broad Eligibility- everyone w/ HDHP is eligible unless:
 - Medicare eligible
 - Claimed as a dependent on someone else's tax return
- Sponsorship Flexibility
 - Individual
 - Employer

The Health Savings Account

- Assets Must be Held in Trust- Like an IRA or 401(k)
- Eligible Trustees
 - Banks
 - Life insurance companies
 - Anyone w/IRS approval (current IRA & MSA trustees)
- Allowable Investments
 - Most financial instruments but not life insurance
 - Collectibles such as rare coins
- Reporting of Contributions and Expenditures
 - Trustee reports contributions and distributions to the IRS
 - Individual acct holder responsible for determining which expenditures are qualified – save your receipts

Contributions to the HSA

- Who Can Make Contributions?
 - Anyone
- When Can Contributions Begin?
 - Once the HSA and HDHP are in place
 - Timing: same as IRA 1/1 to 4/15
- When Must Contributions Stop?
 - When entitled to Medicare (eligible and enrolled)
 - No longer covered by an HDHP
- What is the Annual Contribution Limit?
 - Lesser of deductible and \$2600 for individual and \$5150 for a family
 - Deductibles and contribution max indexed to medical CPI
 - Catch up contributions for 55+
- Form of Contributions
 - Cash or rollover from an MSA or another HSA
- Discrimination Issues
 - Employer contributions must be comparable- constant \$ or %
 - 35% penalty

Distributions from the HSA

- Qualified Distributions- Not taxed
 - I.R.S. sec 213(d) expenses but not insurance premiums except
 - » insurance premiums while on COBRA or unemployed
 - » Long term care insurance premiums
- Other expenditures
 - Taxed as ordinary income
 - Additional 10% tax if <65 and not disabled
- Qualified Beneficiary- Self, spouse, dependents
 - Spouse and dependents even if covered under non-HDHP
 - Expenses must not be reimbursed by insurance
- When Can Funds be Spent?
 - Anytime after H.S.A. established
 - Don't need to be covered by HDHP

The High Deductible Health Plan (HDHP)

- Policyholder
 - Employer or individual
 - Insurance or self-funded
- HDHP Requirements
 - Two basic requirements
 - » Minimum deductible of \$1000/\$2000 for individual/family
 - » Maximum OOP \$5000/\$10000 for individual/family
 - Flexibility- example for an individual
 - » \$1000 deductible 80/20 coinsurance to \$20,000
 - » \$5000 deductible with 100% coinsurance
- Preventive Care Allowed on a first dollar basis
 - Physicals and well child care
 - Screens such as Mammography and Prostate
 - Tobacco cessation weight loss programs
- Out of PPO Network Penalties- don't apply to OOP Max

Comparison with MSAs and HRAs

| | HSA | MSA | HRA |
|--------------------------------|---|--|------------------------|
| Availability | Anyone w/ HDHP | Self-employed and small employer (<50 ees) | Employer Groups |
| Who can contribute | Anyone | Employer or Individual but not both | Employer Only |
| Contribution maximum | Lesser of Deductible and fixed amount set by law | 65% of deductible for individuals (75% family) | Determined by employer |
| Deductible and OOP flexibility | \$1,000 min ded; \$5,000 max OOP for an indiv (\$2,000 and \$10,000 for family) | \$1,700 min ded; \$3,450 max OOP for an indiv (\$3,450 and \$6,300 for family) | Determined by employer |
| Nonqualified withdrawals | Yes but taxed as ordinary income +10% penalty if <65 | Yes but taxed as ordinary income +15% penalty if <65 | Not allowed |
| Portability of account | Yes | Yes | No |

Why I think the HSA will help reduce medical trend

- Currently Little Incentive for Consumers to Efficiently Utilize Health Care Services
 - Other consumer goods/services- cost is related to usage
 - Why price shop or efficiently utilize when someone else is paying
 - Without an incentive to judiciously utilize, it is Human Nature to over utilize
- With an HSA Consumers Get to Keep the Money They Don't Use
 - Reintroduce consumer into health insurance equation
 - Reward consumers for efficient health care management
- Consumers Will Have Incentive to Manage Their Health Care Spending
 - Price shop- check charges; probably shocked when learn true cost
 - Judiciously utilize services
 - Maybe even check medical bills for accuracy
 - Maybe adopt healthy lifestyle- Center for Disease Control & Prevention: behavior is responsible for 50% of health status and associated cost
- Market Acceptance

Conclusion – It's the Money

- I think most agree that health care trend is currently too high
- Remote third party payers, copays, and low deductibles shield consumers from the true cost of healthcare which encourages over utilization
- Consumers' share of the total health care bill has fallen 20 points over the last 30 years
 - Now less than 20%
 - Diminishing stake in controlling cost
- Managed care
 - Initial success reducing trend but faded
 - Unhappy consumers and providers
- HSA
 - Not much motivates like money
 - HSA financially rewards cost effective consumption
 - Maybe a better gatekeeper than a PCP