

BRIEF ANALYSIS

No. 295

For immediate release:

Friday, June 11, 1999

Making Medical Savings Accounts Better

In 1996 Congress created a demonstration project permitting small employers and the self-employed to establish tax-free Medical Savings Accounts (MSAs). However, congressional lawmakers imposed strict limits on who can purchase MSAs and undermined their ability to work properly.

Although about 54,000 qualified MSA policies had been sold by December of 1998, the restrictions have diminished the popularity of MSAs among employers, consumers and insurers. They also have discouraged insurers from offering MSAs. In response, 43 senators are supporting five needed MSA reforms intended to correct problems in the original legislation and to make Medical Savings Accounts available to every working American.

Current MSA Law. Tax-advantaged MSAs are personal savings accounts that must be combined with high-deductible health insurance. Account holders typically use their MSA funds to pay small and routine health care bills, while relying on health insurance to pay more costly ones. Money not spent during the year may be left in the account to grow tax free. In addition to medical expenses, MSA funds may be used to pay health insurance premiums when people are between jobs.

Under the demonstration project created by Congress, certain individuals or their employers may make annual tax-deductible MSA contributions of up to 65

percent of the policy's deductible in the case of individual coverage and 75 percent of the deductible for family coverage. Qualified deductibles range from a minimum of \$1,500 to a maximum of \$2,250 for an individual and from \$3,000 to \$4,500 for a family.

MSAs Help the Uninsured. The U.S. General Accounting Office (GAO) released an analysis of the demonstration project for qualified Medical Savings Accounts and found that almost four in every ten people who set up MSAs were previously uninsured. [See the figure.] That means MSAs may be one of our most powerful weapons for reducing the number of uninsured.

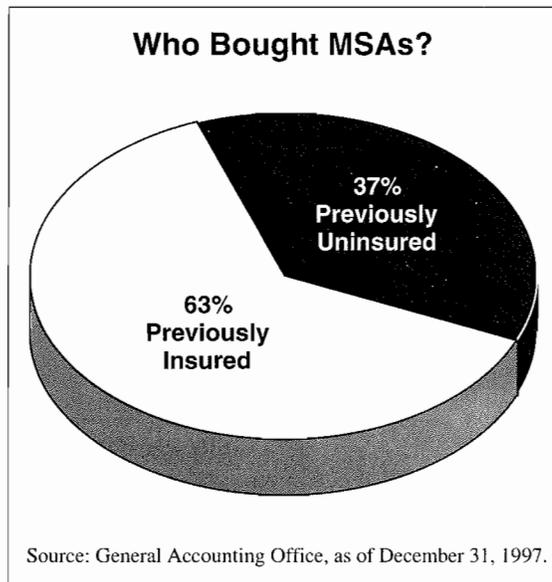
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Needed Reform: Allow All Americans to Have an MSA. The current pilot program permits the sale of only 750,000 MSA policies over a four-year period and only to the self-employed and to small businesses with 50 or fewer employees. Major insurers are reluctant to enter such a market, since its small size does not warrant creating and marketing a new product. Congress should lift the 750,000 cap, allow an unlimited number of people to have an MSA and allow all employers to offer high-deductible health insurance coupled with an MSA.

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Needed Reform: Make the Program Permanent. Another restriction that discourages insurers from offering and aggressively promoting MSA products is the four-year time limit, with an end date of December 31,



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2000. Congress should eliminate the sunset provision so MSA buyers will be able to use their accounts for years to come and MSA sellers will be assured of a long-term market for their new product.

Needed Reform: Lower the Minimum Deductible.

Under current law, MSA plan deductibles cannot be lower than \$1,500 for individual policies and \$3,000 for families. While these deductibles are not unusual among standard high-deductible plans, they are intimidating to many middle-income Americans, especially those used to low deductibles. In addition, the restricted deductible makes it difficult for insurers to create a plan that meets consumer needs. Congress should lower the minimum deductibles at least to \$1,000 and \$2,000, respectively.

Needed Reform: Reduce Out-of-Pocket Exposure.

Another problem is that MSA tax-free deposits are limited to 65 percent of the individual deductible and 75 percent of the family deductible. The remaining gap could leave individuals and families exposed to significant out-of-pocket expenditures. Congress should allow people to deposit the entire amount of the deductible in their MSA accounts.

Needed Reform: Let Employers and Employees Contribute to MSAs. Under current MSA law, employers or employees can contribute to an MSA, but not both. This provision discourages employers from contributing anything unless they can contribute the entire allowable deposit. As a result, employers may not contribute anything and employees may have to bear the entire cost. Congress should remove this restriction so both employers and employees can make contributions.

How MSAs Meet People's Health Care Needs.

People can spend their MSA money for health care not covered by their health insurance, though the expenses may not apply toward the deductible. Because MSAs make money available when health care expenses arise, they encourage preventive care. They allow people to

save for the long-term (i.e., nursing home care and retirement), even to pay long-term care insurance premiums. MSA funds can also be used to pay health insurance premiums during job transition. MSAs usually impose lower out-of-pocket expenditures and thus are better for the chronically sick. In addition, MSAs address current tax inequities by giving people who self-insure for small and routine medical expenditures the same tax break they get for giving the money to insurers.

How MSAs Can Help Meet the Challenge of Managed Care. Most Americans are currently in some form of managed care. While managed care appears to have reduced the growth of health care spending, it also has interfered with the doctor-patient relationship, often turning doctors into agents of a managed care bureaucracy rather than agents of their patients. Some critics also believe that managed care has lowered the overall quality of health care. MSAs can solve many managed care problems by restoring money — and control — to patients and encouraging the reestablishment of trusting doctor-patient relationships.

Conclusion. While the MSA demonstration project was a step in the right direction, it needs some adjustments. Lifting the restrictions on MSAs would encourage the health insurance industry to promote the concept more aggressively. Increasing the number of MSA plans would slow the growth in health care costs as Americans become more prudent shoppers for health care.

It is also clear that many uninsured people are voting with their dollars by choosing MSAs. At a time when the number of uninsured is at an all-time high, it makes sense to remove the restrictions so every American — not just those favored by Congress — can have an MSA.

This Brief Analysis was prepared by NCPA Vice President of Domestic Policy Merrill Matthews Jr. and Vice President of External Affairs Jack Strayer.