Health Savings Accounts Scrutinized, Praised

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As President Bush pushes health savings accounts higher on his agenda, experts continue to debate whether they are a good idea for solving the problems of the uninsured.

“Different things are true about these proposals, the more troubling I find them to be,” Leonard Burman, codirector of the Urban-Brookings Tax Policy Center, said in a teleconference sponsored by the Center on Budget and Policy Priorities (CBPP). “I don’t think the idea (that people will be more cost conscious) is really true in practice. HSAs are accounts to which employees contribute to pay for the first several thousand dollars of their health care costs. They are also almost always linked to a high-deductible health insurance plan. Contributions to the HSA are tax free, as is money withdrawn for covered medical expenses. If the money is not used in a particular year, it can accumulate in the account.

The Galen Institute, a group that supports consumer-driven health care, has been more than a little skeptical of HSAs. “The idea is to give consumers even more control over their health spending decisions—and provide them an incentive to spend wisely and save on future health care needs,” according to a statement from Galen. Critics argue that sick people are not always in a position to shop around for care; that making consumers more cost conscious won’t help lower health care costs, because most health care spending is for expenses higher than the amount of the deductible, which is out of consumer control and that HSAs tend to attract mostly healthy people, driving up premiums for sicker individuals who remain in more traditional plans.

In a more detailed statement, White House officials said that the president ‘proposes making premiums for HSA-compatible insurance policies deductible from income taxes when [these policies] are purchased by individuals outside of work. In addition, the tax credit for these HSAs would offset payroll taxes paid on premiums paid for their HSA policies.”

The president is also proposing to allow any spending account. The president’s plan would allow the tax deduction for HSAs even more tempting to some people, said Jason Furman, senior fellow at the CBPP. “HSAs are already an unprecedentedly favored tax vehicle. This proposal will make HSAs already tilted and adds a new tax credit.”

If enacted, these proposals could make HSAs so attractive financially that they would be able to rival 401(k) plans as retirement savings vehicles, Mr. Furman said. For example, suppose a family in a 25% tax bracket could pay $11,500 to an HSA that is invested in a 3% interest rate. Under the Bush proposal, they would owe a payroll tax of $1,607, but would also get a tax credit for that amount, so the entire $11,500 would stay in the account. If they put the same amount into a 401(k), they would still owe the payroll tax, but would not get a tax credit, so only $8,893 would be deposited into the 401(k) account. Thus the HSA would have $25,486 in it by 2036, versus $21,587 for the 401(k), Mr. Furman said.

With such results, “a lot of employers who offer 401(k) plans would have a less of an incentive to be added. They could go on their own and get a much better deal than from an HSA than from a 401(k), and avoid nondiscriminations. The payroll tax for HSAs has already tilted and adds a new tax credit.”

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