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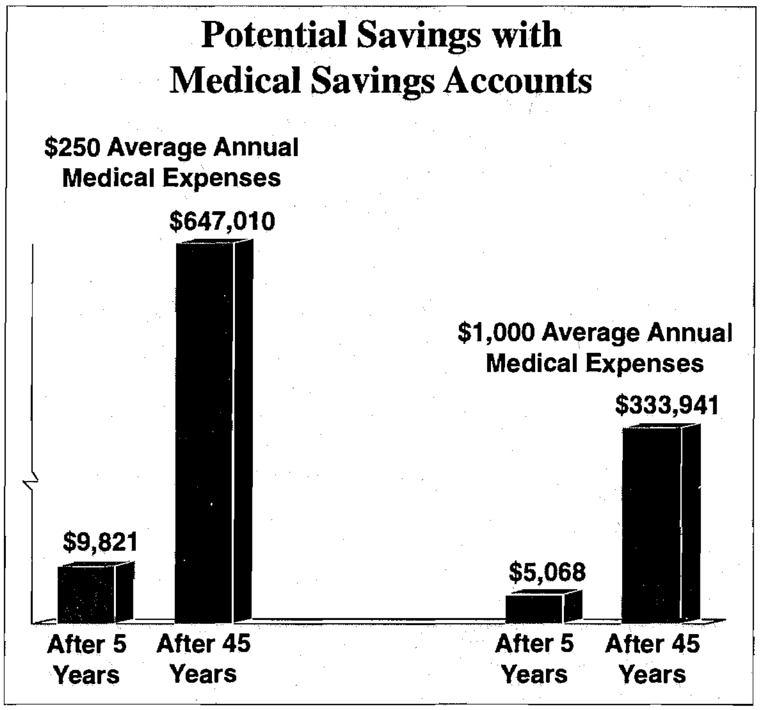
Misplaced Criticism of MSAs

Medical Savings Accounts (MSAs) have become the most controversial element of the health insurance reform proposal before Congress.

They *should* be the least controversial.

MSAs give people the opportunity to move from a traditional low-deductible health insurance plan to one with a high deductible (say $2,000 to $3,000) and to deposit the premium savings in a personal savings account. They use the account to pay for routine and preventive medical care, and the high-deductible policy pays for major expenses. If they have money left over in the MSA at the end of the year, they can withdraw it or roll it over to grow with interest.



Under a typical plan available now in the health insurance marketplace, a family with employer-provided health insurance can get a $1,500 contribution to its MSA and a $2,000 deductible policy. The employee pays for health care expenses with the $1,500, easily enough to cover most families during a year. If the family exhausts the $1,500, the employee pays the next $500 out of pocket, and insurance pays everything over $2,000.

Opponents of current MSA legislative proposals offer several criticisms of them. Yet anyone who understands the MSA and the private health insurance marketplace recognizes that the criticisms are unfounded.

Bogus Criticism No. 1: *MSAs would attract only healthy people, leaving the sick in a separate pool.* During the health care debate a few years ago, critics of the Clinton plan argued that his proposal would limit people's choices. President Clinton responded that people's choices already were limited. Most people, he said, had only one employer health plan to choose from.

Precisely. Employers determine what type of health insurance their employees have. Most companies — 83 percent by one estimate — offer their employees only one policy. "Adverse selection" — in which the healthy move into one plan while the sick remain in another — is impossible because only one policy is available.

Many larger employers offer their employees a choice, usually between traditional health insurance and a health maintenance organization (HMO). However, they often price the options to encourage employees to choose one health insurance plan over the other. For example, an employer may make participation in an HMO free, but require employees who want traditional health insurance to pay a contribution, deductible and/or copayment.

No employer is required to offer an MSA option. Those who do are free to structure and price their plan as they choose and to drop the plan if they find it unworkable.

Bogus Criticism No. 2: *MSAs would attract only wealthy people looking for a tax break.* The MSA legislation before Congress caps the annual tax-free deposit at $2,000 for an individual and $4,000 for a family. The MSA legislation also permits either the employer or the employee to make the deposit, but not both. Thus an individual with extra money cannot "top up" the account above the employer's contribution just to get some tax-free savings.

Furthermore, while the MSA legislation before Congress would permit people to make deposits with pretax dollars, hundreds of companies have already switched to

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MSA plans in which the deposit is made with aftertax dollars. The MSA legislation would simply make those deposits tax free, giving individuals more money to cover routine care. This would primarily help lower-income workers, since high-income workers could more easily pay the $500 out-of-pocket difference between the $1,500 aftertax contribution and their $2,000 health insurance deductible (as in the scenario above).

Bogus Criticism No. 3: *MSAs are being promoted by special interests.* MSAs let people keep some of the money they or their employer are currently giving to insurance or managed care companies. Not surprisingly, many managed care companies and insurers oppose MSAs. Yet MSA opponents are accusing supporters — who are working to let people keep more of their health care dollars, rather than giving them to insurers — of being controlled by special interests, while those who want insurers and managed care companies to keep all the money portray themselves as patients' advocates.

Bogus Criticism No. 4: *MSAs will never provide enough money for people to pay their health care bills.* The vast majority of people spend little money on medical expenses in any given year, so most would have a significant balance in their MSAs at year's end. Since the proposal before Congress imposes penalties for withdrawing those funds for nonhealth expenses, most people would roll over the balance. This makes MSAs a powerful mechanism for encouraging higher savings.

Consider the findings reported by health economists Gail A. Jensen and Robert J. Morlock in the *Journal of American Health Policy* (May-June 1994). Their 1989 survey of about one million individuals in large self-insured plans, many with generous benefits, found that:

- One-third filed no claims at all.
- 73 percent filed claims for less than $500.
- 89 percent filed claims for less than $2,000.

Thus, as in the example given above, about three-fourths of the employees would have between $1,000 and $1,500 available for savings at the end of the year.

Jensen and Morlock then calculated the growth of the MSAs under several scenarios to estimate the savings impact of MSA compounding.

Suppose a 20-year-old or his employer placed $1,800 a year in an MSA. (That is the actual MSA deposit amount for employees of Jersey City, N.J.) Jensen and Morlock estimated the savings that would result if individuals spent, on average, $250 and $1,000 a year over their working lives and earned 8 percent interest on the remaining deposit. [See the figure.]

- The person whose expenses averaged $250 a year would have $9,821 after five years and $647,010 at retirement, after 45 years of deposits.
- The person with an average of $1,000 in medical expenses would have $5,068 after five years and $333,941 at retirement.

Bogus Criticism No. 5: *Medical Savings Accounts will cost employers more money.* A new study shows that MSAs save employers about as much as managed care and could save them much more.

The study by Michael T. Bond, Brian P. Heshizer and Mary W. Hrivnak of Cleveland State University looked at 27 Ohio firms, all with fewer than 200 employees and each with an MSA plan. The professors compared the cost of the plans to the cost of traditional insurance.

On average, employees had lower out-of-pocket costs under an MSA plan than under a traditional health insurance plan — about $317 less for individuals and $1,355 less for families.

Employers saved, too. The MSA plan for individuals cost more than a traditional plan, but taking the individual and family MSA plans together, the employers saved about 12 percent per year.

Criticism of MSAs for the under-65 population represents a concerted effort to kill MSA legislation. But none of the criticisms are valid. Once people understand MSAs, they realize that tax-free Medical Savings Accounts would reduce health care costs and expand choices in the health care marketplace.

This Brief Analysis was prepared by NCPA Vice President of Domestic Policy Merrill Matthews Jr., Ph.D.