Committee on Ways and Means
Democrats

Representative Charles B. Rangel - Ranking Member

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"CONSUMER-DIRECTED" HEALTH CARE: A Primer On Health Savings Accounts (HSAs) and High-Deductible Health Plans (HDHPs)

What is "Consumer-Directed Health Care?"

Consumer-directed health care is the term Republicans use to describe the combination of health savings accounts (HSAs) and high deductible health plans (HDHPs). In theory, proponents believe that shifting costs to consumers will make them more prudent purchasers. At a minimum, such arrangements require comprehensive information systems to allow individuals to "shop" for medical services by comparing providers based on price and quality. Such systems do not exist in the U.S. health system today and would take years to develop. Even if these systems were available, it is impractical to shop in emergency situations. Plus, patients would still need to rely on the expertise of physicians and other trained medical professionals to determine the appropriate course of treatment.

What is an HSA?

An HSA (health savings account)[1] is a tax-exempt account that is used to pay or reimburse certain medical expenses for individuals with high deductible health plans (HDHPs). Both individuals and employers may contribute to an HSA, and contributions are made with pre-tax dollars. Account balances roll over from year to year, earnings on funds in these accounts accrue tax-free, and withdrawals are not taxed if they are used to pay for qualified medical expenses.[2]

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[1] Health savings accounts were created in the Medicare Modernization Act of 2003; HSAs have largely replaced Archer medical savings accounts (MSAs) which were created in 1996 (HIPAA).

[2] Qualified medical expenses are determined by the IRS. The HSA rules do not permit tax-free withdrawals from the accounts to pay HDHP premiums.

Who is Eligible for an HSA?
To be eligible for an HSA, individuals must be enrolled in a high-deductible health plan (see explanation below). Eligible individuals may not have any other health insurance coverage (including Medicare or coverage through their spouse), and they may not be claimed as a dependent on someone else's tax return. Employees covered by a health FSA (flexible spending arrangement) or an HRA (health reimbursement arrangement) that pays for medical expenses generally cannot make contributions to an HSA.[3]

What is a High Deductible Health Plan (HDHP)?
Minimum HDHP deductibles are defined in statute. Currently, they are more than three times the deductibles of typical health plans.[4] HDHPs have a maximum limit on annual out-of-pocket spending (also called a catastrophic limit) for medical expenses covered by the plan. The insurer has absolute authority to determine what medical expenses count toward the deductible and out-of-pocket limits, which means that patients can spend much more than these limits suggest. Expenses for out-of-network services do not apply toward the deductible or out-of-pocket limit if the plan uses a network. Coverage after the deductible varies significantly, according to the individual policy. The following table shows the minimum and maximum annual deductible and out-of-pocket expenses for HDHPs for 2006. It also shows the maximum contribution to an HSA under current law.

Type of Coverage	Minimum Annual Deductible	Maximum Annual Deductible and Other Out-of-Pocket Expenses[5]	Maximum Contribution to an HSA
Self-only	$1,050	$5,250	The lesser of annual deductible or $2,700
Family	$2,100	$10,500	The lesser of annual deductible or $5,450

Individuals over age 55 may contribute an additional $700 in 2006. Contributions above the specified limits are not tax deductible. As with other employer-sponsored insurance, contributions made by an employer are not taxed.

[3] Individuals covered by a limited-purpose health FSA or an HRA, a suspended HRA, a post-deductible health FSA or HRA, or a retirement HRA may contribute to an HSA. For additional information on FSAs or HRAs, see the Ways and Means Issue Brief on Tax Preferred Accounts for Medical Expenses.
[4] Kaiser Family Foundation/HRET 2005 Survey of Employer Health Benefits.
[5] Premiums do not count toward deductible or out-of-pocket limits.