



The Case for Health Savings Accounts

By Jonathan J. Miltimore

In 2003, Health Savings Accounts (HSAs) were created as part of that year's Medicare legislation. HSAs allow individuals to save dollars tax free to be used for future medical expenses. HSAs are not a substitute for insurance; rather they are used in conjunction with high deductible health plans.¹

HSAs are one part of a plan devised by conservatives and libertarians to bring market principles back into the health insurance market. Health "insurance" in the United States today is not insurance in the traditional sense. Insurance originally meant protecting individuals or organizations from substantial and unforeseeable costs or circumstances. Minor costs incurred were not covered, expenses above a determined deductible were.

Most insurance markets still operate this way. The minimum deductible for homeowners insurance is, almost without exception, \$500. Your typical auto insurance plan protects individuals from collision damages or other costly expenses, not expenditures such as oil changes, new brakes, or flat tires. So why is healthcare different?

Many people may answer that they have a "right" to adequate healthcare. The United States Constitution declares many rights of the people. The Bill of Rights is peppered with phrases such as "Congress shall make no law," "shall not abridge," "will not infringe." The Constitution also guarantees people the right to fair criminal proceedings. But one thing is certain about the rights enumerated in the Constitution: they are rights of the people from government. There is not a syllable or phrase in the U.S. Constitution suggesting that the people have "a right" to free or affordable healthcare services or other material assets.

But, of course, we all want access to healthcare. Unless you have a single-payer government run system (where costs will be indirect), access to healthcare will largely be determined by affordability. Affordability can best be achieved by allowing prices to operate. This is where HSAs come in.

HSAs would allow individuals and their employers to contribute pre-tax dollars into a personal account to cover routine healthcare expenditures and deductibles. Ownership and control of these dollars belongs to the individual, and all expenses beyond the deductible are covered or partially covered by insurance. In 2007, the maximum annual contribution to an HSA was \$2,850 for an individual, \$5,650 for a family.

By allowing individuals to use some of their dollars tax free to save for future healthcare expenses, HSAs are a first step toward removing the distortions in the U.S. tax code that created much of the mess in the first place. Employer involvement in healthcare politics was an unintended consequence of government-enforced wage controls in the 1950s; employers, prohibited from raising wages to recruit workers, began to offer healthcare plans to employees as a substitute. This created a healthcare system with bad incentives.

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Because health plans are tax free and the costs indirect, it makes sense for employees to pursue costly comprehensive plans that they would have been less likely to demand without the tax incentive provided to businesses. And because comprehensive coverage paid for by a third-party insulates consumers from costs, people naturally consume more healthcare resources and services than they would if they bore all or some of the costs below a normal deductible level.

Americans are essentially removed from direct healthcare costs and the decision making process. For many working adult Americans, the only crucial medical insurance decision they make is determining which comprehensive plan to purchase.

HSAs provide workers with the same tax break as employers and allow more consumer control over their healthcare. A purchaser of an HSA would still be covered for major medical expenses by insurance, but would now be allowed to save and spend pre-tax dollars on other medical expenses as they see fit.

HSAs should not be regarded as a “silver bullet” that will fix our healthcare system overnight; rather, they offer the opportunity to take the first and most crucial step toward healthcare restoration: making people cost conscious of their healthcare expenditures again. As healthcare expert Michael Cannon of Cato Institute has observed, studies have shown that “people with HSAs or similar coverage were 50 percent more likely to ask providers about costs, 33 percent more likely to seek out treatment alternatives, and three times more likely to choose a less-expensive treatment alternative.”²

By insulating citizens from direct standard medical costs and virtually removing them from healthcare decisions, the federal government has indirectly prompted a healthcare system severed from prices that encourages over-consumption of healthcare. The result is that the United States spent 16 percent of its Gross Domestic Product on healthcare in 2006, compared to 5.2 percent in 1962.³

The economist Thomas Sowell points out that prices perform a simple but profound function: “rationing scarce resources.”⁴ By 2015 healthcare costs will gobble up one-fifth of the U.S. economy. This rate of increase cannot continue; some sort of rationing will take place. The only question is will it be consumers doing the rationing in a system governed by prices or politicians and government bureaucrats?

Endnotes

- 1) U.S. Department of Treasury, “All About HSAs,” May 18, 2007, Washington D.C., <http://www.treas.gov/offices/public-affairs/hsa/pdf/all-about-HSAs_051807.pdf> (October 15, 2007).
- 2) Michael F. Cannon, “Health Savings Accounts: Do the Critics Have a Point?” Cato Institute, Policy Analysis No. 569, May 30, 2006, p. 3, <<http://www.cato.org/pubs/pas/pa569.pdf>> November 7, 2007.
- 3) “Facts on Healthcare Costs,” National Coalition on Healthcare, <<http://www.nchc.org/facts/cost.shtml>> (November 7, 2007).
- 4) Thomas Sowell, Basic Economics: A Citizens Guide to Economics, Basic Books, NY, 2000, pp. 18-19.

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