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2005-06

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**Committee on
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(AC-In)**

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**CENTER ON BUDGET
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September 13, 2004

**INITIAL DATA ON INDIVIDUAL MARKET ENROLLMENT FAIL TO DISPEL
CONCERNS ABOUT HEALTH SAVINGS ACCOUNTS**

by Edwin Park and Robert Greenstein

Debate continues over Health Savings Accounts. Many leading health care analysts and economists have warned that HSAs pose a high risk of causing "adverse selection," under which healthy people and less-healthy people separate into different insurance arrangements and the cost of insurance for the less-healthy consequently rises, which can place them at risk of becoming uninsured or underinsured. Past studies by the Urban Institute, the American Academy of Actuaries, and RAND concluded that accounts like HSAs would have these effects if use of the accounts

became widespread.^[1] Analyses by health and tax policy analysts also have concluded that HSAs are likely to be used extensively as tax shelters by high-income individuals.

HSA proponents have long dismissed these warnings and criticisms, and they recently have begun citing what they say are new data that refute these critiques.^[2] This analysis considers the new data. As it demonstrates, careful examination of the new data shows that they do not support the claims of HSA proponents and shed little light on the issues being debated. The use of these data to claim that concerns and criticisms about HSAs are unfounded does not withstand scrutiny.

Background on Health Savings Accounts

Health Savings Accounts were established as part of last year's Medicare drug legislation and made available as of January 1, 2004. Any individual who enrolls in a high-deductible health insurance plan with a deductible of at least \$1,000 for individual coverage and \$2,000 for family coverage may establish a tax-favored savings account known as a Health Savings Account.^[3] An individual with a HSA may take a tax deduction for contributions he or she makes to the account (up to the amount of the deductible contained in his or her high-deductible insurance policy), as long as the contributions do not exceed an annual limit, set at \$2,600 for individuals and \$5,150 for family coverage in 2004.^[4] Both employers and employees may make deductible contributions to an employee's HSA in the same year; the combined contributions made on behalf of an individual may not exceed the plan deductible or the contribution limits, whichever is lower.

Funds held in these accounts may be placed in various investment vehicles such as stocks and bonds, with the earnings accruing on a tax-free basis. Withdrawals from

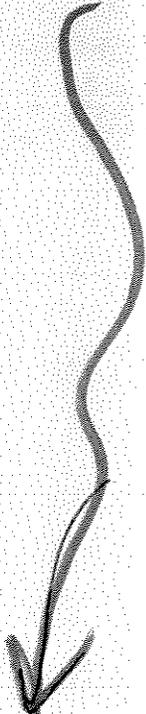
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the account also are exempt from tax as long as they are used to pay for out-of-pocket medical costs such as deductibles, co-payments, and other uncovered medical expenses. Withdrawals for non-medical purposes are subject to income tax and a financial penalty, but no penalty applies to withdrawals for non-medical purposes made after an individual reaches age 65.^[5]

Due to the structure of HSAs, they hold particular attractions for healthier and more affluent people. For healthy individuals who do not expect to incur significant health care costs, HSAs provide a way to build up a new stream of tax-favored savings. To the extent that funds in HSAs are not needed for health care costs, account-holders can build up account balances that accumulate over time and enjoy tax advantages that regular savings accounts do not have. These tax advantages are worth the most to people at higher-income levels; the higher your tax bracket, the greater the benefit that the HSA tax breaks provide you.

HSAs do not provide the same benefits for less healthy individuals. For such people, who tend to consume more health care, the high-deductible insurance policies that must be used in conjunction with HSAs can mean significantly greater out-of-pocket costs, as compared to the out-of-pocket costs typically borne under comprehensive insurance, which usually carries significantly lower deductibles. These added out-of-pocket costs are of greatest concern for those less-healthy individuals who are not in the higher tax brackets, since they have fewer resources to draw upon and also would derive much less benefit from the HSA tax breaks.

Health Savings Accounts Raise Substantial Concerns

HSAs are a controversial element of last year's Medicare prescription drug legislation. They raise two principal concerns: that they are likely to weaken the comprehensive employer-based health insurance system through which the vast majority of Americans now obtain their health insurance; and that they will be used primarily as tax shelters by healthy, affluent individuals.

- **Effects on employer-based coverage.** Under employer-based coverage, healthier and sicker employees are combined into a single insurance pool. This enables less healthy individuals to obtain insurance at an affordable price. If each individual had to purchase insurance individually based on his or her own health status, older, sicker workers would in many cases be priced out of the market.

A major concern about HSAs is that if employers begin offering HSAs and high-deductible insurance as an option alongside traditional comprehensive insurance, then healthy and less-healthy workers may separate into different insurance arrangements, with the healthier workers shifting to HSAs and high-deductible policies and workers in poorer health seeking to remain in comprehensive coverage. Numerous health policy experts believe this development is likely under HSAs. Such a development would be highly problematic. The cost of insuring any group of workers — and hence the price of insurance coverage for those workers — depends on the health status of the people in the group. If the healthier, less-costly-to-insure employees opt out of comprehensive coverage to take advantage of the HSA tax breaks, then the average cost of insuring the people remaining in comprehensive coverage

must go up, since those left in comprehensive coverage will be a less-healthy group that tends to use more health care services.^[6]

The withdrawal of healthier workers from comprehensive employer-based coverage to take advantage of HSAs also could occur even if an employer does *not* offer HSAs and high-deductible insurance as an option. Some affluent, healthier workers may conclude they would do better purchasing a high-deductible policy in the individual insurance market and setting up a HSA than remaining in employer-based coverage (especially if the employer-based coverage requires employees to bear a significant share of the premiums).

If HSAs lead significant numbers of healthier workers to opt out of comprehensive employer-based coverage, making those who remain in such coverage more expensive, on average, to insure, then the comprehensive coverage that employers typically offer will become less affordable over time — and a growing number of employers may ultimately cease to provide it. That would pose a particular problem for vulnerable workers in poorer health who need such coverage and seek to remain in it.

- **Creation of a lucrative new tax shelter.** The second concern stems from the fact that under HSAs, not only are contributions to the accounts tax-deductible, but withdrawals from the accounts to pay for out-of-pocket medical costs are tax-free. This tax treatment — under which *both* contributions to a savings account *and* withdrawals from that account are tax advantaged — is without precedent in the tax code. Retirement accounts such as traditional Individual Retirement Accounts (IRAs) and 401(k) plans permit deductible contributions, but withdrawals upon retirement are treated as taxable income. Other plans, such as Roth IRAs, permit tax-free withdrawals but the contributions are not tax-deductible.

Furthermore, unlike under traditional IRAs, there are no income limits on participation in HSAs. As a result, affluent healthy individuals who have reached the maximum annual contribution limits on their IRA or 401(k) plans — or who are ineligible to make tax-deductible contributions to IRAs because their incomes exceed the IRA income limits — could use HSAs to shelter a greater share of their income for retirement. HSAs consequently are likely to become a major tax shelter for affluent individuals, causing substantial revenue losses to the Treasury and adding to budget deficits.

Of added concern, the exceptionally generous tax treatment that HSAs enjoy creates a dangerous precedent. If this type of tax treatment, under which contributions to an account are deductible *and* withdrawals are tax free, is extended in whole or in part to other savings accounts — such as retirement accounts, as some Congressional leaders already are proposing — the adverse long-term fiscal consequences for the nation may be severe.^[7] For example, a proposal to convert a portion of 401(k) and IRA accounts into HSA-like accounts, which has been designed by Fidelity Investments and endorsed by Senate Majority Leader Bill Frist, would be likely to cost the Treasury hundreds of billions of dollars over coming decades (and, depending on how large a portion of retirement accounts were allowed to be converted to HSA-like accounts, could cost \$1 trillion or more).

Analysis of the Data Cited by HSA Proponents

HSA proponents have claimed these concerns and criticisms are incorrect or overblown. Recently, they have begun to cite data released earlier this year by eHealthInsurance and Assurant Health as evidence that concerns about HSAs are unfounded.^[8] eHealthInsurance is an online individual market health insurance broker that sells HSAs. Assurant Health is an insurer specializing in offering HSAs to both employers and individuals. Since both firms stand to make profits from expansion of HSAs, evidence from such sources should be subject to careful scrutiny. As it happens, examination of these data shows they do not support these claims.

What HSA Proponents Say

HSA proponents contend these data demonstrate that concerns about adverse selection are unfounded. They say the data refute concerns that HSAs will be used primarily by healthier or more affluent individuals. They cite data from Assurant Health indicating that the company made an offer of coverage to 93 percent of those who applied for a high-deductible policy in conjunction with a HSA. They say this shows that this coverage is available to nearly all who seek it, not just to those who are healthier. They also cite Assurant data that 29 percent of those purchasing HSA-related coverage from Assurant had income below \$50,000 as evidence there is not a tilt in favor of higher-income people. And they cite data that 43 percent of HSA applicants lacked health insurance coverage in the months before purchasing a high-deductible policy in conjunction with a HSA as proof that HSAs can play a large role in reducing the ranks of the uninsured.

Weaknesses in These Data

The eHealthInsurance and Assurant Health data cited in support of these claims relate *only* to use of HSAs in the individual health insurance market; they include *no* data regarding HSA use in conjunction with employer-based health insurance. Yet it is in their potential effects on employer-based coverage that the greatest dangers of HSAs, and the greatest risks of adverse selection, lie. As a result, these data are not especially relevant to such concerns about HSAs.

Moreover, the data are highly preliminary. The eHealthInsurance data cover only the first two months of 2004. The Assurant data were collected only for the first four months of 2004.

Furthermore, eHealthInsurance is an online provider; its data may be affected by the characteristics of individuals who are using the Internet to apply for and purchase HSAs in the individual market. In addition, it is unclear how many HSAs were purchased through eHealthInsurance and Assurant and served as the data set for these findings. No information as to the number of HSAs has been provided by eHealthInsurance. Assurant notes there were 56,396 *applicants* to Assurant for individual market HSA coverage during the four-month period the data cover, but the number of individuals who actually obtained coverage from Assurant is not provided.

In short, the limited data from these two sources, which apply only to the individual health insurance market, do not provide a rational basis for dismissing concerns about HSAs that stem from years of analysis conducted by leading institutions with no financial interest in these matters, such as the Urban Institute, the American

Academy of Actuaries, and RAND. We now proceed to examine the specific claims that HSA proponents have made with these data.

Unsupported Conclusions Drawn by HSA Advocates

HSA proponents have drawn three questionable conclusions from these data.

1. HSA supporters have claimed that the data show HSAs are *not* primarily attracting healthy individuals and thus do not risk adverse selection.^[9]

Nothing in the data supports this conclusion. The eHealthInsurance data on HSA purchasers include *no* information about the health status of the purchasers. The data include information only about the age, family size, premiums, and plan benefits of an unknown number of online HSA purchasers.

The Assurant Health data similarly lack information about the health status of HSA purchasers. HSA proponents have noted that Assurant Health provided an offer of coverage to 93 percent of the individuals who applied for HSA coverage,^[10] but this factoid sheds little light on the health status of HSA users. Given that HSA accounts and high-deductible insurance policies are considerably more attractive to healthier individuals than to less healthy people and pose risks for those in poorer health, it is likely that those who applied for HSA coverage were a healthier-than-average group.

Furthermore, insurers in the individual market can and do deny coverage to applicants, based on an applicant's health or medical history. They also can offer coverage to a less-healthy applicant that carries higher premiums charges and/or excludes coverage for certain important medical conditions or health benefits. The eHealthInsurance data and Assurant data include no information about premium or benefit variation among the offers of coverage that were made. This further invalidates the drawing of inferences about the health status of those using HSAs from the limited data that have been provided.

Moreover, some applicants who were in poorer health may have received an offer of coverage but found the premium they were quoted to be unaffordable and decided not to purchase health insurance. The data made available lack information on this matter, as well.

Nor do the eHealthInsurance or the Assurant Health data offer any comparison between the average health status of HSA purchasers in the individual market and the average worker in employer-based health insurance. The individual market is accessible primarily to healthier individuals, due to the widespread use in that market of medical underwriting, under which insurers can decline to offer coverage, offer more limited coverage, or charge much higher premiums to less healthy people. As a consequence, it is likely that most people who have actually purchased a high-deductible policy in the individual market in conjunction with a HSA are people who are in better health, on average, than people who have employer-based coverage. To help assess the degree to which HSAs may result in adverse selection, it would be useful to have data on the health status of workers with employer-based coverage who have chosen a HSA and how their health status compares to that of workers in the same firm who have chosen comprehensive coverage. No such data have been provided by eHealthInsurance or Assurant Health.

2. HSA supporters have claimed these enrollment data show that HSA

participants are not primarily higher-income individuals taking advantage of the tax shelter benefits of HSAs. Here, as well, the data do not back up the claim. The Assurant Health data indicate that 29 percent of individuals who purchased individual market coverage from Assurant in conjunction with a HSA had incomes below \$50,000 per year.^[11] This means that 71 percent of HSA purchasers had incomes of more than \$50,000. The Assurant data do not provide a more detailed income breakdown of the purchasers with incomes above \$50,000 to determine the extent to which high-income individuals purchased high-deductible plans and HSAs through Assurant.

Moreover, the Assurant Health data indicate that nearly 57 percent of purchasers were from professional or managerial occupations.^[12] People in those occupations tend to have higher salaries. As a result, the Assurant data themselves seem to suggest that higher-income individuals may be more likely to purchase HSAs than those with low- or moderate-incomes.^[13]

The eHealthInsurance data that have been made publicly available do not include any data on income. One HSA proponent has cited eHealthInsurance as finding that 46 percent of HSA participants had family incomes of less than \$50,000.^[14] Even if these data (which are not publicly available) are accurate, they provide little basis for drawing conclusions about HSAs. It is important to recognize that data about HSAs that come solely from the individual health insurance market are likely to skew the income of the purchasers downward. Lower-income workers tend to use the individual market in great proportions than higher-income workers due to their greater lack of access to employer-based coverage. Lower-income workers often work for smaller businesses; such firms, particularly those with large numbers of low-wage employees, are among the least likely to offer health insurance coverage to their workers. As a result, in 2003 — *before* HSAs came into existence — insured households with incomes below \$25,000 were nearly 80 percent more likely to obtain their coverage through the individual market than households with incomes of \$75,000 or more.^[15] Since it makes sense for people who already were purchasing high-deductible coverage in the individual market to set up HSAs, a sample of HSA purchasers in the individual market would likely be biased downward in terms of income. Such data cannot be used to make inferences about the income of HSA participants generally.

A much more useful examination would look at individuals participating in HSAs in the *employer-based* health insurance system and compare their incomes to the incomes of individuals enrolled in comprehensive health insurance plans offered by the same employers. Data on the income of employees who choose a HSA plan as compared to workers within the same firm who opt for a comprehensive plan would be particularly relevant. Such data are not currently available since the large majority of employers do not yet offer HSAs. Without such idea, conclusions on the matter are premature.

3. HSA proponents also have claimed that the data show a large share of HSA users are people who previously were uninsured and thus that HSAs can be an important tool for expanding coverage. According to the Assurant data, 43 percent of HSA applicants did not have health coverage in the months before purchasing a high-deductible policy in conjunction with a HSA. This statistic is cited to show that HSAs can play an important role in making coverage more affordable for

the uninsured.

These Assurant data, however, require considerable qualification. The individual market is often a market of last resort, particularly for adults who have lost their jobs and health insurance, cannot afford COBRA coverage, and do not qualify for Medicaid. Even before the advent of HSAs, many individuals purchasing insurance in the individual market are likely to have been uninsured for a period immediately preceding the purchase. The fact that a certain percentage of people who purchased individual-market coverage in conjunction with a HSA were uninsured for the months before the purchase is not especially meaningful in assessing the contribution of HSAs. Moreover, no data have been provided on the percentage of actual HSA *purchasers* — as distinguished from HSA *applicants* — who previously were uninsured. Some uninsured applicants may have declined to purchase coverage once they were provided an offer of coverage if the offer carried a premium cost they considered unaffordable. (It is curious that data on the extent to which *purchasers* previously were uninsured have not been made available along with data on applicants.)

Most important, these data are *for the individual market only*. HSA use will become widespread only if HSAs are adopted by large numbers of employers, which many analysts now expect to occur. Since the vast majority of employers who adopt HSAs are likely to be employers that already offer coverage to their workers, most employer-based HSA enrollment will involve workers who already are insured and are shifting their health insurance arrangements (or having the arrangements shifted by their employers) from comprehensive coverage to high-deductible plans attached to HSAs. Over time, the vast majority of HSA participants thus is likely to consist of people who previously were insured.^[16]

Conclusion

Some HSA proponents have claimed that recent data on HSA use in the individual market refute concerns that HSAs may weaken employer-based coverage through adverse selection and that HSAs may be used extensively as tax shelters by higher-income individuals. These proponents also argue that the data show HSAs are effective in covering the uninsured. In reality, the data do not support any of these conclusions.

HSAs are likely to become increasingly common in the employer-based health insurance system. The Kaiser Family Foundation and the Health Research and Educational Trust determined 27 percent of employers were somewhat likely or very likely to offer a high-deductible health insurance plan attached to a HSA or other personal savings account in the next two years. Among very large firms with 5,000 or more workers, 50 percent were somewhat likely or very likely to offer such plans.^[17] Similarly, a survey of 991 primarily large employers recently conducted by Mercer Human Resource Consulting found that nearly three-quarters of employers (73 percent) are somewhat likely or likely to offer Health Savings Accounts by 2006.^[18] A smaller employer survey conducted by Hewitt Associates found that 61 percent of large employers are likely to offer HSAs in the near future.^[19] As more employers adopt HSAs over time, more data will become available to evaluate the risks that HSAs pose. These data will provide much better evidence than the preliminary, fragmentary, conflicting, and incomplete data from eHealthInsurance and

Assurant Health.

It is likely that when better data become available, they will confirm the risks that health and tax policy experts believe HSAs pose. Indeed, the recent Mercer survey of employers heightens these concerns. The survey found that employers believe HSAs will be most attractive to healthy, higher-income workers. A plurality of employers surveyed (44 percent) reported they believed their healthiest employees would be most likely to participate in HSAs. A substantial majority of employers (61 percent) said they believed their higher-paid employees would be most likely to use HSAs.^[20]

The Center on Budget and Policy Priorities is grateful to the Nathan Cummings Foundation for its support of this report.

End Notes:

[1] See Emmett B. Keeler, et. al., "Can Medical Savings Accounts for the Nonelderly Reduce Health Care Costs?" *Journal of the American Medical Association*, June 5, 1996, p. 1666-71; Len M. Nichols, et. al., "Tax-Preferred Medical Savings Accounts and Catastrophic Health Insurance Plans: A Numerical Analysis of Winners and Losers," Urban Institute, April 1996; and American Academy of Actuaries, "Medical Savings Accounts: Cost Implications and Design Issues," May 1995.

[2] See, for example, Laura Trueman, "Health Savings Accounts: Myth vs. Fact," National Center for Policy Analysis, July 19, 2004; Grace Marie Turner, "Health Savings Accounts Gain Popularity," *Galen Institute*, July 26, 2004; Richard Nadler and Dan Perrin, "The Center on Budget and Policy Priorities' Study on HSA Premium Tax Deduction Misses the Point," *The HSA Coalition*, May 25, 2004; and Derek Hunter, "New Data on Health Insurance, the Working Poor, and the Benefits of Health Care Tax Changes," *Heritage Foundation*, April 28, 2004.

[3] The high-deductible health insurance plan must have an out-of-pocket limit of no more than \$5,000 for individuals and \$10,000 for family coverage. The out-of-pocket limit may be higher for out-of-network services. Certain preventive services such as annual physicals and routine screenings may be exempted from the deductible.

[4] Individuals age 55 or older may make additional contributions (in excess of the limit) of another \$500 in tax year 2004, rising to \$1,000 by tax year 2009. Individuals age 65 or older who are eligible and participating in Medicare are not eligible to make deductible contributions to HSAs.

[5] The financial penalty for a non-medical withdrawal prior to retirement age of 65 is equal to 10 percent. Unlike other retirement accounts, there are no mandatory withdrawals upon retirement.

[6] See Emmett B. Keeler, et. al., "Can Medical Savings Accounts for the Nonelderly Reduce Health Care Costs?" *Journal of the American Medical Association*, June 5, 1996, p. 1666-71; Len M. Nichols, et. al., "Tax-Preferred Medical Savings Accounts and Catastrophic Health Insurance Plans: A Numerical Analysis of Winners and Losers," Urban Institute, April 1996; American Academy of Actuaries, "Medical Savings Accounts: Cost Implications and Design Issues," May 1995; Daniel Zabinski et. al., "Medical Savings Accounts: Microsimulation Results from a Model with Adverse Selection," *Journal of Health Economics*, April 1999, p.195-218; Gail Shearer, "The Health Care Divide: Unfair Financial Burdens," *Consumers Union*, August 10, 2000 (relying on Lewin Group estimates).

[7] See, for example, Edwin Park and Robert Greenstein, "New Retirement Medical Account

Proposal Would Create Lucrative Tax Shelter and Swell Deficits but Do Little to Help Low- and Moderate-Income Seniors," Center on Budget and Policy Priorities, revised July 22, 2004.

[8] eHealthInsurance, "More than 70 Percent of Consumers Obtaining Health Savings Accounts Paid \$100 or Less for their HSA-Eligible Health Plans," April 21, 2004; Assurant Health, "U.S. House Speaker Hastert Joins Business Leaders to Review Latest Data on Success of Health Savings Accounts," June 21, 2004. Some of the data attributed to both eHealthInsurance and Assurant Health by HSA proponents are not included in the publicly available eHealthInsurance report or in the Assurant Health press release. That makes such data difficult to evaluate. It is assumed here that data that have been attributed to eHealthInsurance and Assurant Health but are not publicly available have been cited accurately.

[9] Trueman, p.3; Nadler and Perrin, p.15; Turner.

[10] Trueman, p.2; Coalition for Affordable Health Coverage, "Myth vs. Fact about HSAs," available at www.cahc.net/pages/hsa_facts.htm.

[11] Assurant Health.

[12] Assurant Health.

[13] One HSA proponent also cites Assurant Health data as showing that 38 percent of HSA purchasers had homes with a market value of less than \$125,000 and that 27 percent had a net worth of less than \$25,000. Trueman, p.1. This implies that 62 percent of HSA purchasers had home with market values in excess of \$125,000 and 73 percent had a net worth in excess of \$25,000. Without a further breakdown of these data, which have not been made publicly available, one cannot infer the extent to which higher-income people are purchasing HSAs.

[14] Trueman, p.1. This statistic was not included in the publicly available eHealthInsurance report.

[15] CBPP analysis of 2003 CPS data.

[16] The publicly available data from eHealthInsurance include no information about previous insurance status. Two HSA proponents claim that eHealthInsurance found 32.8 percent of applicants did not have health insurance coverage in the prior six months (Nadler and Perrin, p.2; Trueman, p.1). Assuming these data attributed to eHealthInsurance are accurate, qualifications similar to those just cited for the Assurant data are needed. First, this statistic implies that 67.2 percent of applicants already had coverage. Most important, these data apply only to a limited number of individuals who secured coverage in the individual market; the data do not involve the employer-based market, in which most HSA participants will, as just noted, consist of already-insured individuals who shift insurance arrangements. In addition, these data apply to applicants for insurance, not to those who actually purchased coverage.

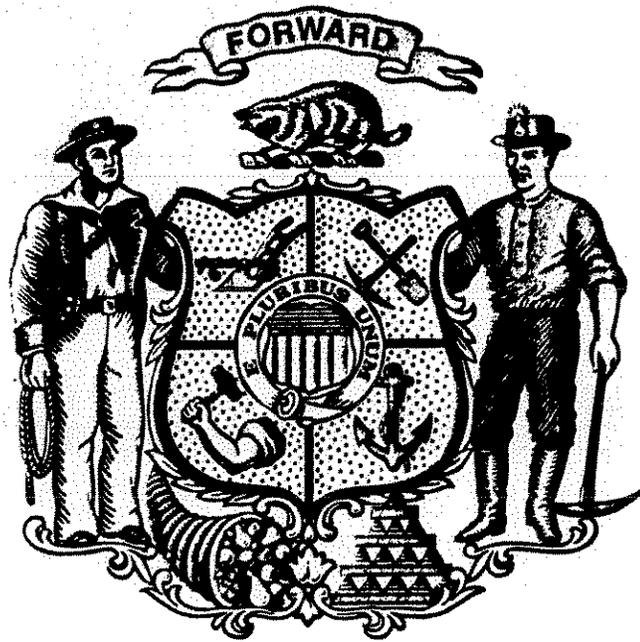
[17] Kaiser Family Foundation and Health Research and Educational Trust, "Employer Health Benefits: 2004 Annual Survey," September 2004.

[18] Mercer Human Resource Consulting, "US Employers See a Role for New Health Savings Accounts in their Benefit Programs," April 26, 2004.

[19] Hewitt Associates, "Addition of HSAs Will Require Substantial Health Plan Design Changes," March 31, 2004.

[20] Mercer Human Resource Consulting, *op cit*.







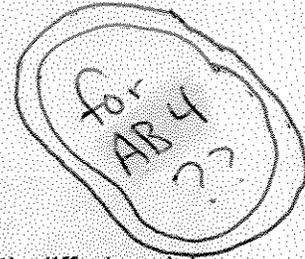
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December 2004

**The Potential Impact of Adding New Groups
to the State of Wisconsin Group Health Insurance Plan**

ADVERSE SELECTION



WHAT IS GROUP HEALTH INSURANCE?

Group health insurance is a system of pooling many members with differing risk characteristics and potential health care costs into a group that provides coverage for health care costs in return for a premium that is shared equally among the members and reflects the average costs of the group. For example, if a group of 1000 members had \$1,000,000 in health care costs, each member would need to contribute \$1,000 in premium.

HOW DOES ADVERSE SELECTION AFFECT GROUP HEALTH INSURANCE?

- ◆ In any reasonably sized group plan, 20% of the members will incur no costs, 60% of the members will incur costs that represent 20% of the total costs, and 20% will incur 80% of the total costs.
- ◆ **Adverse selection** occurs when members of the group have the freedom or an incentive to choose to participate, or not, based on their anticipated health expenditures.

EXAMPLE If the 20% of the members who incur no health care costs decide not to participate because they anticipate spending less than \$1,000, the costs of the original group remain at \$1,000,000, but there are 200 fewer people to cover those costs. Under this scenario, the premium for the remaining members increases to \$1,250.

With the premium increase of \$250, more members may decide that the added cost does not justify their continued participation. So, they too, decide to drop coverage. The members that decide to drop coverage are always the ones who have incurred the least amount of health care costs. Then, as they drop coverage, the average premium costs to those that remain increase substantially. **This is known as a *premium death spiral*.**

HOW DOES ADVERSE SELECTION AFFECT A COMMUNITY- RATED PLAN?

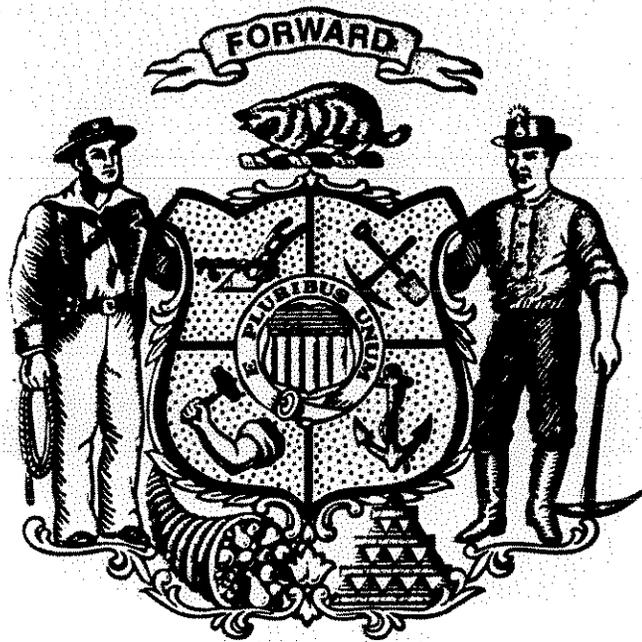
- ◆ The Wisconsin Public Employer (WPE) Group Health Plan is similarly affected by **adverse selection**. The WPE plan is “community-rated,” which means that all employers that join pay the same premiums as all others, regardless of their true costs.

EXAMPLE If there were 10 employers participating, each with 1,000 employees, and their total health expenditures equaled \$10,000,000, the premium for each employer would be \$1,000,000. The actual experience for each employer varies, as shown:

<u>Employer</u>	<u>Actual incurred costs</u>
A	\$ 750,000
B	\$ 800,000
C	\$ 850,000
D	\$ 900,000
E	\$ 950,000
F	\$1,050,000
G	\$1,100,000
H	\$1,150,000
I	\$1,200,000
J	\$1,250,000

Knowing that their actual experience is less than the \$1,000,000 premium, Employers A through E find coverage elsewhere. The total cost for the remaining employers is \$5,750,000, and can no longer be supported by an equal \$1,000,000 in premium, so the premium is raised to \$1,150,000. At that premium level, Employers F and G can find less expensive coverage elsewhere, and they decide to leave the group. This **premium death spiral** continues.

- ◆ **Adverse selection** also occurs with employers that may want to join the WPE plan. If they are currently paying less than our average rate, they will not join. But, if they are currently paying more, they will have an incentive to join. The employers who have employees with the most expensive health care costs *stay* in the plan, while employers who have employees with the least costs *leave*. Consequently, the WPE plan's average premiums rise, and the cycle continues.





Wisconsin Manufacturers' Association • 1911

Wisconsin Council of Safety • 1923

Wisconsin State Chamber of Commerce • 1929

James S. Haney
President

James A. Buchen
Vice President
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James R. Morgan
Vice President
Education and Programs

Michael R. Shoys
Vice President
WMC Service Corp.

To: Chairperson Ann Nischke
Members of the Assembly Committee on Insurance
From: James Buchen, Vice President of Government Relations
Date: January 20, 2005
Subject: **Support Assembly Bill 4**, relating to health savings accounts.

Wisconsin Manufacturers & Commerce **supports Assembly Bill 4 (AB 4)**, as amended by Assembly Substitute Amendment 1 (ASA 1). We recognize that rising health insurance costs are a major concern for businesses, big and small, as they strive to stay competitive, whether doing business regionally, nationally or globally. One way to reduce the costs of health insurance over the long run is to re-establish a level of consumer driven competition in the purchase of health care services. Health savings accounts are an important component of an effective consumer driven health care plan.

AB 4 as amended by ASA 1 would create a state tax exemption for health savings accounts, mirroring federal law, thereby allowing a Wisconsin employee a state income tax deduction for any contribution to a health savings account.

Health savings accounts are federally tax-exempt accounts used to pay for certain medical expenses for employees who are covered under certain health plans¹. To qualify, health plans must have a "high deductible," that is, with a minimum deductible of \$1,000/single coverage or \$2,000/family coverage (indexed annually for inflation) and, for 2005, an out-of-pocket maximum of \$5,100/single coverage or \$10,200/family coverage. Qualifying high deductible health plans can have first-dollar coverage (no-deductible) for preventive care².

Each year, the individual, his or her employer, and/or others (e.g., family members) can contribute an amount up to the deductible of the high deductible health plan, but not more than \$2,600 annually for individuals and \$5,150 annually for families (adjusted annually for inflation). Both the contributions and the account earnings are not subject to federal taxation. Employer contributions to an HSA on an employee's behalf are not counted as taxable income.

¹ IRS Publication 502 (2004) discusses medical expenses which may be paid for from health savings account dollars, such as doctors' office visits, hospital care, dental care, vision care, prescription care and over-the-counter medications. Other expenses are specifically excluded, such as cosmetic surgery, hair transplants, nutritional supplements and teeth whitening.

² IRS Notice 2004-23 provides a safe harbor list of preventive care that high deductible health plans can provide as first-dollar coverage: periodic health evaluations (e.g., annual physicals), screening services (e.g., mammograms), routine pre-natal and well-child care, child and adult immunizations, tobacco cessation programs, and obesity weight loss programs.

In addition:

- Health savings accounts may be carried over (year to year AND employer to employer).
- Health savings accounts can grow with tax-free earnings.
- Withdrawals from health savings accounts are not subject to taxation if used to pay for medical care.
- For those under age 65, withdrawals from health savings accounts for non-medical expenses are included in gross income and subject to an additional 10 percent tax.
- For those over age 65, withdrawals from health savings accounts for non-medical expenses are included in gross income.

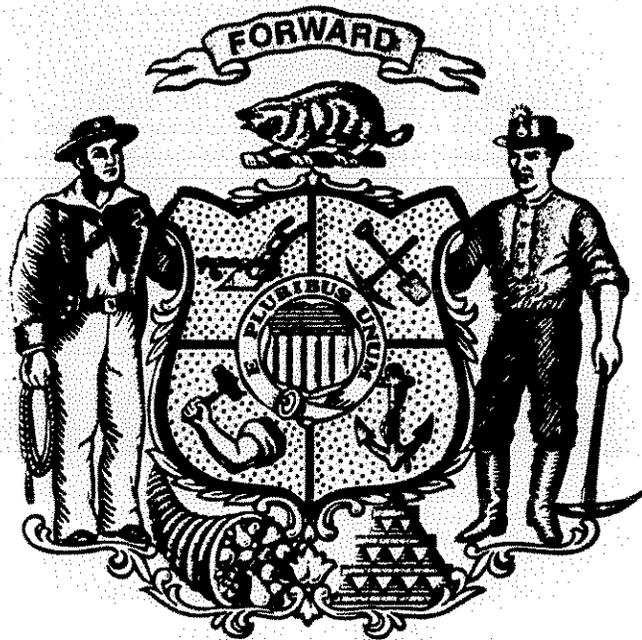
Even though HSAs have only been on the market since January 1, 2004, retrospective data is already available regarding purchasers. Based on actual market experience with HSAs:

- Assurant Health, a national health insurance carrier, has reported that 29 percent of HSA purchasers have family incomes of less than \$50,000, 43 percent of the applicants were previously uninsured, 70 percent of its HSA applicants were over age 40, and 77 percent of its HSA purchasers are families with children.
- eHealthInsurance, an online insurance company, has reported that nearly half of HSA purchasers make less than \$50,000 a year. Also, eHealthInsurance has reported that 56 percent of HSA purchasers who had annual incomes under \$15,000 were previously uninsured, and 46 percent of those making \$15,001 to \$35,000 were previously uninsured.

Health savings accounts can give workers a strong financial stake in their health care purchasing decisions, giving them incentives to aggressively manage their health care costs by becoming more active, engaged consumers.

Wisconsin businesses are national leaders in providing health care benefits to Wisconsin workers. Nearly 70 percent of the Wisconsin population is covered by employment-based health insurance, putting Wisconsin eighth-best among the fifty states in terms of the percent of the population covered by employment-based health insurance. As such, Wisconsin businesses are keenly interested in ensuring health insurance is affordable.

Wisconsin Manufacturers & Commerce respectfully requests you support AB 4, as amended by ASA 1.





State of Wisconsin / OFFICE OF THE COMMISSIONER OF INSURANCE

Jim Doyle, Governor
Jorge Gomez, Commissioner

Wisconsin.gov

125 South Webster Street • P.O. Box 7873
Madison, Wisconsin 53707-7873
Phone: (608) 266-3585 • Fax: (608) 266-9935
E-Mail: information@oci.state.wi.us
Web Address: oci.wi.gov

TESTIMONY TO ASSEMBLY INSURANCE COMMITTEE
AB 4 – HEALTH SAVINGS ACCOUNTS
January 20, 2005

By
Eileen Mallow, Assistant Deputy Commissioner

Thank you, Representative Nischke and members of the Insurance Committee for the opportunity to testify on AB 4, that would create a state income tax deduction for Health Savings Accounts (HSAs). Insurance Commissioner Jorge Gomez has asked me to appear on behalf of the Office of the Commissioner of Insurance. I am Eileen Mallow, Assistant Deputy Commissioner of Insurance and I will be testifying for information on the bill.

What is an HSA? In a nutshell, an HSA is much more of a tax policy question than an insurance question. It is a tax deferral vehicle that can be used to meet the allowable deductibles for a high deductible health insurance policy. It differs from some of the other funding mechanisms for health insurance deductibles in that the account belongs to the individual, and any balance can be rolled over from one calendar year to the next. The Internal Revenue Service decides which expenses can be claimed against an HSA, but the information contained on their website suggests that any health care expense that would otherwise deductible for income tax purposes is an allowable expense for an HSA. Federal income tax deductibility is available to Wisconsin residents and we understand we are one of 10 states that have not adopted the federal tax deduction.

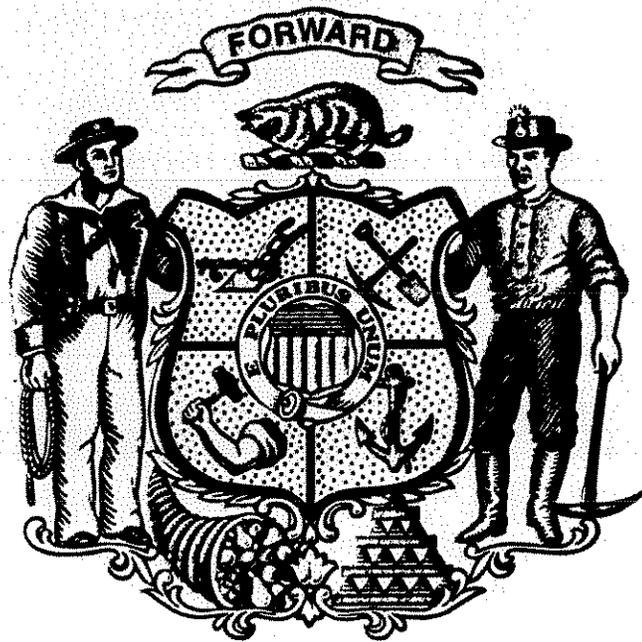
The Office of the Commissioner of Insurance has approved high deductible insurance products for marketing in the state. Our understanding is that most of the larger health insurers in Wisconsin have an approved policy to market. However, policy form approval is merely the first step in getting this product into the hands of consumers. Ultimately employers or individual

purchasers must make the decision as to whether or not this product is right for them taking into consideration the total out-of-pocket expenses for the insureds, benefits offered under the policy, and tax consequences.

We have no information as to the willingness of consumers to purchase high deductible health policies in Wisconsin. A story in the January 11, 2005 *New York Times* suggested that consumers are generally not yet aware of these products, but would likely be resistant to paying for the higher deductibles that accompany these types of health plans. The article went on to say that a very small number of employers (3%) had offered the plans for calendar year 2005. Only time will tell if the product is adopted by employers and individuals needing to purchase a health insurance policy.

Finally, I would like to make a plea for a program our office believes will offer assistance to individuals who need assistance with their health insurance. The federal Health Care Tax Credit (HCTC) program offers up to a 70% income tax credit to individuals who have been displaced from their jobs because their job has been transferred overseas. The credit is only available for a qualifying health insurance plan, as defined by the Trade Adjustment Act. Wisconsin does not have a qualifying plan at this time except for state continuation, which offers very few individuals opportunity to claim the credit. OCI has approached the larger health insurers in the state about voluntarily developing a qualifying plan and all have declined. The only remaining option for the state is to modify the eligibility requirements for the Health Insurance Risk Sharing Plan (HIRSP) to make it qualifying coverage. We understand that there is bi-partisan support for this change and I encourage you to take up the issue as soon as you can.

Thank you for your time and I would be happy to answer any questions you may have.



Testimony on AB 4 (Health Savings Accounts),
Assembly Committee on Insurance, January 20, 2005

by

Robert Kraig, Ph.D.

Political Director, SEIU Wisconsin State Council

SEIU is the largest union of health care workers in North America, and the largest union of nurses and health professionals, nursing home workers, and home care workers in Wisconsin. We also represents many other service workers who have great difficulty obtaining affordable health insurance coverage. On behalf of SEIU members across the state of Wisconsin who are struggling to provide health care, and to hold onto basic coverage for their families, we strongly oppose this legislation.

At a time when health care hyper-inflation is placing a huge burden on individuals, businesses who provide health insurance benefits, and on all levels of government, it is certainly timely that the Legislature consider comprehensive solutions to the crisis.

But rather than doing that, this misguided approach will actually make the crisis worse. Advocates of AB 4 are selling snake oil to the sick. Not only does it not cure the disease, it has its own toxic effects which will make the patient even sicker.

First, HSAs will primarily help wealthier individuals who already can afford health insurance, and will not help the uninsured. Because this bill provides a non-refundable tax credit, the vast bulk of the benefit will go to people in the upper tax brackets. Yet, according to an analysis by Jonathan Gruber, a Professor of Economics at MIT, 90% of the uninsured either are too poor to owe taxes, or are in the 10% to 15% tax brackets. As a result, Professor Gruber estimates that 87% of the people who would take advantage of HSAs already have health insurance.¹

Second, if HSAs become commonplace, they will undermine traditional employer based comprehensive health insurance, which is still the bedrock of our health care system. Once employers offer the high deductible and less comprehensive policies required to receive the credit, there would be an incentive for healthier and wealthier individuals to participate, because they could take advantage of significant tax shelter advantages, with substantially less risk to their assets from out-of-pocket health insurance expenses. This process of "adverse selection" would substantially dilute the risk pool for traditional comprehensive insurance. The basic premise of health insurance is that healthy people pay into the system in order to spread the cost of sicker individuals who utilize more health care services. Research by RAND, the Urban Institute, and the American Academy of Actuaries concludes that if HSA use became widespread, premiums for traditional comprehensive insurance could more than double.² This would put tremendous pressure on employers to eliminate comprehensive health insurance or pass substantially more cost onto employees, and would make it almost impossible for many modest and middle income individuals to retain comprehensive coverage.

Third, HSAs shift health care costs to working families. According to the Center for Policy and Budget Priorities, by creating incentives for employers to contribute less, HSAs “shift a greater proportion of the costs of health insurance from firms to employees.” As a result, “many low-and moderate income-families would likely be unable to afford to maintain their existing coverage.”³³ According to one insurance industry estimate, if they had to rely on high deductible HSA policies, “a typical family might have to earmark \$8,000 a year to get good coverage.”⁴

Fourth, the promise that HSAs will put downward pressure on health care costs is also erroneous. It is well established that preventive medicine greatly reduces health care costs by preventing conditions from becoming more serious. But high-deductible HSA policies actually discourage preventive medicine for people who cannot afford out-of-pocket expenses. As a result, according to Henry Aaron of the Brookings Institution, “high deductible insurance policies required under HSAs could result in increases in health care costs over time for such individuals.”⁵ A Commonwealth Fund study found that older individuals with high deductible policies are twice as likely to skip seeing a doctor than those with traditional comprehensive coverage.⁶

In summary, the only demonstrated benefit of HSAs is the creation of yet another tax shelter for wealthier and healthier individuals. Such individuals can make contributions and disbursements tax free, and role the assets tax free into the retirement savings after the age of 65.

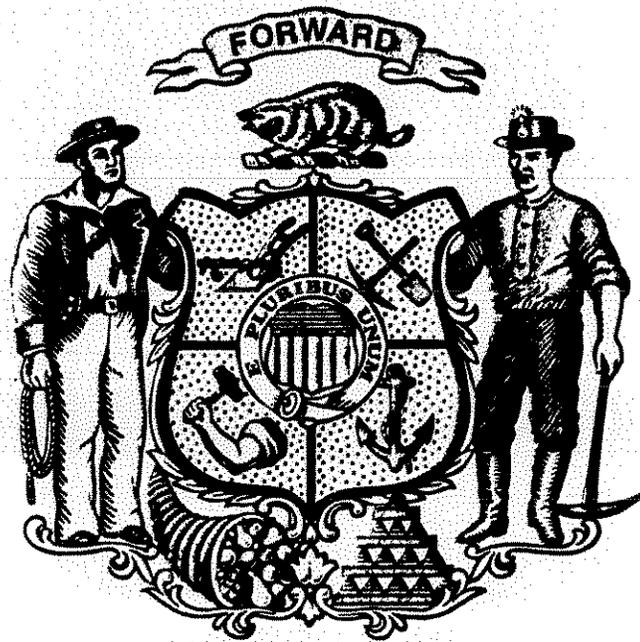
As health care policy, HSAs are a radical departure from the system of social insurance that has been built up since Word War 2, and could irreparably damage our employer-based health insurance system. This system, despite its faults, still provides coverage to the vast majority of Wisconsin working families.

It is entirely understandable why some businesses and consumers, desperate for relief from health care hyper-inflation, would be attracted to any proposal that promised to remedy the situation. But rather than falling for false promises, we need to work together for real health care reform.

There needs to be a much more careful public discussion of real reform during this Legislative session, as there is certainly no public consensus favoring the dismantling of the current health insurance system. Despite the clear desire of many to ram this bill through the Legislature, its implications are almost entirely unknown to the general public. According to a recent national poll by the Kaiser Family Foundation and the Harvard School of Public Health, 70% of Americans either had not heard of HSAs, or did not know what the term meant.⁷

Endnotes

1. Edwin Park and Robert Greenstein, "Proposal for New HSA Tax Deduction Found Likely to Increase the Ranks of the Uninsured," Center on Budget and Policy Priorities, May 10, 2004, p. 2
2. Robert Greenstein and Edwin Park, "Health Savings Accounts in Final Medicare Conference Agreement Pose Threats Both to Long-Term Fiscal Policy and to the Employer-Based Health Insurance System," Center on Budget and Policy Priorities, December 1, 2003, p. 2-3. Also see Dina El Boghdady, "A Health Care Cost Shift," *Washington Post*, January 16, 2005, p. F1.
3. Edwin Park, Joel Friedman and Andrew Lee, "Health Savings Security Accounts: A Costly Tax Cut That Could Weaken Employer-Based Health Insurance," Center for Budget and Policy Priorities, July 8, 2003, p. 3, p. 6.
4. *Eau Claire Leader-Telegram*, Sept. 19, 2004.
5. Henry Aaron, "HSAs –The Sleeper in the Drug Bill," *Tax Notes*, February 23, 2004.
6. Greenstein and Park, "Health Savings Accounts in the Final Medicare Conference Agreement," p. 7.
7. Kaiser Family Foundation/Harvard School of Public Health, "Health Care Agenda for the New Congress," January 2005.





Wisconsin State AFL-CIO *...the voice for working families.*

David Newby, President • Sara J. Rogers, Exec. Vice President • Phillip L. Neuenfeldt, Secretary-Treasurer

TO: Assembly Insurance Committee

FROM: Phil Neuenfeldt, Secretary-Treasurer
Joanne Ricca, Legislative Staff

DATE: January 20, 2005

RE: **Opposition to Assembly Bill 4: Health Savings Accounts**

This bill to allow special tax treatment for Health Savings Accounts (HSA) that are tied to high-deductible insurance plans is being offered as a harmless incentive to encourage their use and as an option to help address our health care crisis. The effects of HSAs will not be harmless and they are a totally inadequate response at this point in time to the magnitude of the health care crisis.

Under current federal law HSAs are authorized and receive federal tax breaks, so the option to use them already exists. The question is whether Wisconsin should *further* encourage their use with extremely favorable tax treatment at the state level. The Wisconsin State AFL-CIO is strongly opposed to expanding favored tax treatment for HSAs because the state will be encouraging a health care policy that—over time—is projected to substantially increase the cost for quality, comprehensive health insurance and seriously erode employment-based coverage for working families.

Background: New federal tax provisions to encourage Health Savings Accounts were slipped into law through the Medicare prescription drug legislation of 2003. HSAs are linked to high-deductible insurance plans (at least \$1,000 deductible for an individual and \$2,000 for a family with an out-of-pocket maximum for the year 2005 at \$5,100 for an individual and \$10,200 for a family). Money deposited into an HSA, either through payroll deduction or directly, is from pre-tax income and the contribution allowed is increased each year. Interest earned on the account is tax-free, as well as withdrawals for medical expenses.

Major Concerns:

- **Will Drive Up the Costs of Comprehensive Employment-Based Insurance.** The concept of HSAs undermines the basic premise on which group insurance operates—a broad and mixed risk pool. Younger, healthier and/or higher income employees will be attracted to the HSAs and opt to “take their chances” with the high-deductible plans, but older workers and those with families are more likely to need the comprehensive coverage. Certainly those employees with chronic health problems will need better coverage. The pool of people who remain in the traditional comprehensive plans will be sicker, the cost of those plans will soar and that option

will become even more unaffordable for employees who need it. **Research by the RAND Corporation, the Urban Institute and the American Academy of Actuaries found that premiums for traditional insurance could more than double if Health Savings Account use becomes widespread.** (“What’s in a Name? House Bill Would Change Name But Not the Substance of a Proposed Expansion of Medical Savings Accounts”, Center on Budget and Policy Priorities, July 8, 2003)

- **Long-Term Threat to Employment-Based Coverage.** Charles Boorady, a securities analyst at Smith Barney commented at the time HSAs were created: “This provision gives employers a door to discontinue health care as an employee entitlement.” (New York Times 12/9/03) Access to health care in our country currently relies on an employment-based system, so any federal or state policy that will encourage employers to abandon comprehensive health care coverage or drive up the costs of such coverage is reckless.

- **Increases Health Risks for Individual.** HSAs provide a perverse incentive for individuals to gamble with their health rather than use the money in the savings account for routine and preventive care. Employees will try to avoid tapping into the account for fear they will not have sufficient funds to cover some future major medical expenses. This will drive up health care costs in the long run because illness and disease that goes untreated will require more expensive care. Dr. James Marks of the U.S. Center for Disease Control stated at a health care conference in Madison that “**catastrophic coverage is absolutely the wrong direction to go if we are concerned with prevention.**” (“Health and Health Care in Wisconsin Conference”, October 3, 2003)

Additional Concerns:

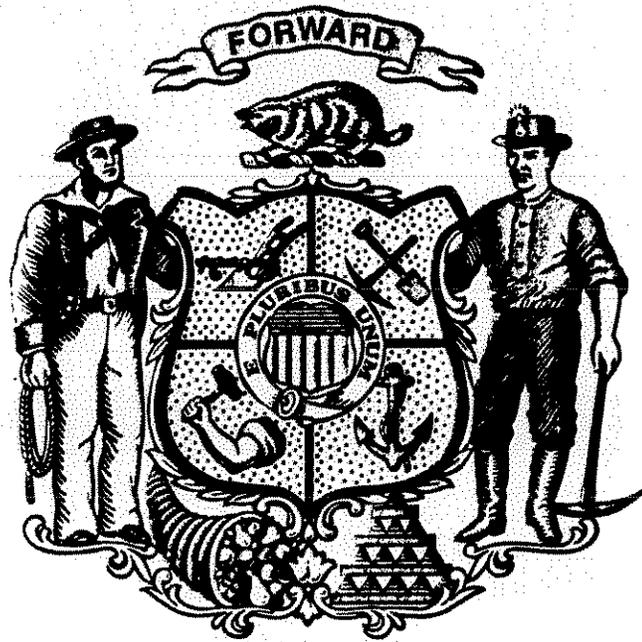
- **Avoids real cost control measures.** HSAs do little to control the overall increases in health care costs that are making health care unaffordable for growing numbers of employers and employees. What HSAs really do is *shift* medical costs to employees. Promoters of HSAs admit as much. They believe that health care costs are high because too many people abuse the system. They promote “consumer driven” plans which really are code words for shifting even more health care costs to employees who are already paying substantially toward their health care. Since 2000, employees’ share of medical costs has risen from 26% to 32%. (*Business Week*, “Your New Health Plan”, November 8, 2004) And we strongly disagree with the cynical idea that people are rushing to doctors for the fun of it. **It is an accepted fact that a small percentage of any insured group is responsible for approximately 80 percent of the medical costs due to chronic illness or serious medical problems.** HSAs do not address this major factor. They do not provide any systemic way of controlling health care costs, improving the quality of health care or providing chronic disease management.

- **A windfall for the wealthy.** Low-income and middle-class families who work paycheck to paycheck do not have the extra income to make substantial pre-tax contributions to an HSA account. Many do not benefit from the tax break because they incur little, if any, tax liability. Those who will benefit the most from this legislation are wealthier individuals who can use the HSA as still another tax shelter—and the insurers who will profit from selling high-deductible policies.

Proponents of AB 4 and HSAs cite some statistics that claim HSAs are being used by lower-income individuals and the uninsured. The attached report from the Center on Budget and Policy Priorities shows how their data is faulty—mainly that it is based on some early, limited information related to the *individual* market for high-deductible policies, and is not relevant to the major concern about adverse selection.

The fiscal note of \$38.7 million over the first eight years is substantial. **It is wrong to use state revenue to encourage a health care policy that will erode quality, affordable employment-based health coverage.**

AB 4 and the promotion of Health Savings Accounts deflects attention from the urgent need to fundamentally reform our health care system, something that our policymakers must address. Every other advanced country has some form of universal health care. How we provide affordable, comprehensive coverage for everyone is what we should be talking about—instead of legislation that simply shifts costs to individuals and threatens the comprehensive health coverage under our employment-based system.



WISCONSIN CITIZEN ACTION



The State's Largest Public Interest Organization

Wisconsin Citizen Action Testimony before the Assembly Committee on Insurance

In Opposition to AB4

January 20, 2005

My name is Darcy Haber and I am the Health Care Campaign Director for Wisconsin Citizen Action. Thank you for the opportunity to testify today in opposition to AB4. As you all know, we are in the midst of a terrible health insurance crisis. What you may not know is that the Institute of Medicine estimates that, every year, about 18,000 Americans die prematurely and unnecessarily solely because they do not have health coverage. That is about two deaths per hour.

So I understand the impetus to act quickly to try to assuage our health care crisis –but following the false hope of Health Savings Accounts is like clicking on a pop-up advertisement on the internet that promises to get rid of pop-up ads. It seems so easy to do, but in the end it makes the problem worse. I urge this committee not to follow the fallacy that Health Savings Accounts will do anything to help our health insurance crisis. They will only exacerbate the problem.

Since you serve on the insurance committee you understand that insurance is about spreading risk as broadly as possible. Historically, five percent of the public has always used about 50 percent of the health care dollar. None of us can predict with certainty who will end up in that five percent. The only way to make insurance affordable for everyone, especially for those who are part of the five percent with significant medical needs, is to spread the risk as broadly as possible.

Health Savings Accounts run counter to this basic concept – instead of trying to spread risk, HSAs help one small group – the healthy *and* wealthy –save money at the cost of those who actually need health insurance. Penalizing people unfortunate enough to get sick is not only unfair, it is also immoral.

We believe that the HSAs will be harmful to Wisconsin's employer-provided insurance system. Employers will likely use HSAs to justify offering high-deductible, high co-payment health insurance plans. These plans will be likely to siphon off healthier people who anticipate few medical treatment costs and hope to shelter more income from taxes in the account. The people who can't afford to put cash into HSAs will stay in insurance plans with a smaller deductible and lower co-payments. So will people who have health problems and who expect to have health care expenses. As the traditional plans lose their healthier

MILWAUKEE

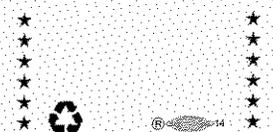
★ 912 N. Hawley Rd. - 2nd Floor South
★ Milwaukee, WI 53213
★ (414) 476-4501
★ Fax: (414) 302-4619
★ E-Mail: info@wi-citizenaction.org
★ www.wi-citizenaction.org

MADISON

★ 1202 Williamson St., #B
★ Madison, WI 53703
★ (608) 256-1250
★ Fax: (608) 256-1177
★ E-Mail: madison@wi-citizenaction.org
★ www.wi-citizenaction.org

NORTHEAST

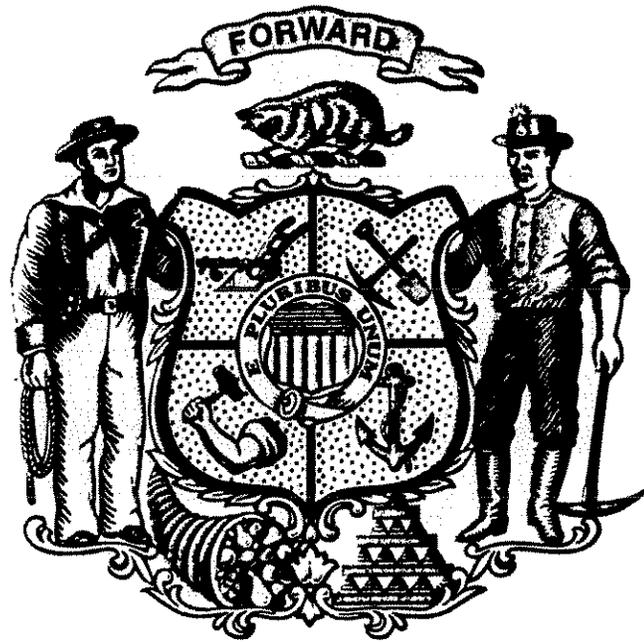
★ 1642B Western Ave.
★ Green Bay, WI 54303
★ (920) 496-1188
★ Fax: (920) 496-1008
★ E-Mail: greenbay@wi-citizenaction.org
★ www.wi-citizenaction.org



enrollees, they will be left with a higher proportion of unhealthy people. More unhealthy people will mean higher per capita costs, so premiums will have to be raised. The faster the premiums rise, the more healthy people with financial wherewithal will decide to opt into HSAs. This continuing cycle of "adverse selection" also known as "cherry picking" healthy people will make the insurance we are used to—plans with smaller deductibles and low co-payments—extremely expensive, leading more and more employers to drop this kind of coverage.

Wisconsin is the laboratory for the nation. A state that has always taken the lead in ensuring its residents were treated with fairness and given equal opportunity. Passing legislation that helps those who are healthy and hurts those who are sick does not follow in our great tradition.

Thank you for your attention today.





Assembly Committee on Insurance

Assembly Bill 4

January 20, 2005

The members of the Wisconsin Association of Health Underwriters (WAHU) and National Association of Health Underwriters (NAHU) are comprised of insurance professionals involved in the sale and service of health benefits, long-term care benefits, and other related products, serving the insurance needs of over 100 million Americans. We have almost 18,000 members around the country and nearly 600 members here in Wisconsin. Our membership is primarily made up of insurance agents that work directly for and with the consumers of health care. Since our number one concern is our customers, we consider ourselves to be consumer advocates and look at how any legislation or issue will affect these customers.

Long before the advent of Health Savings Accounts, WAHU has long supported the concept of consumer driven health care. The dramatic rise of health care costs will continue until normal consumer behavior is applied to the purchase of health care. Such behavior has been prevented through current benefit design and structure, with the use of first dollar coverages and the continued removal of the patient from the financial responsibility of their own health care. Consumer driven plans, like HSA's, provide the opportunity to bring back normal consumer behavior to the health care marketplace. Unlike any other, financial responsibility is the driving force that will provide the right kind of incentive for consumers to competitively shop price and quality in the health care they purchase.

Health Savings Accounts are tax-exempt accounts used to pay for certain medical expenses for employees who are covered under qualified high deductible major medical policies. In essence, an individual or employee would purchase a health plan that has a large deductible. The individual or employee would then set up a savings account to put aside money in order to help pay for medical care under the deductible. If the individual seeks medical care, the money in the account would be used to pay for such care until the deductible is met, at which time, the insurance plan would pay for medical care. Any money left over in the savings account becomes the property of the individual to carry over from year to year. The money to put in the savings account can come from two sources.

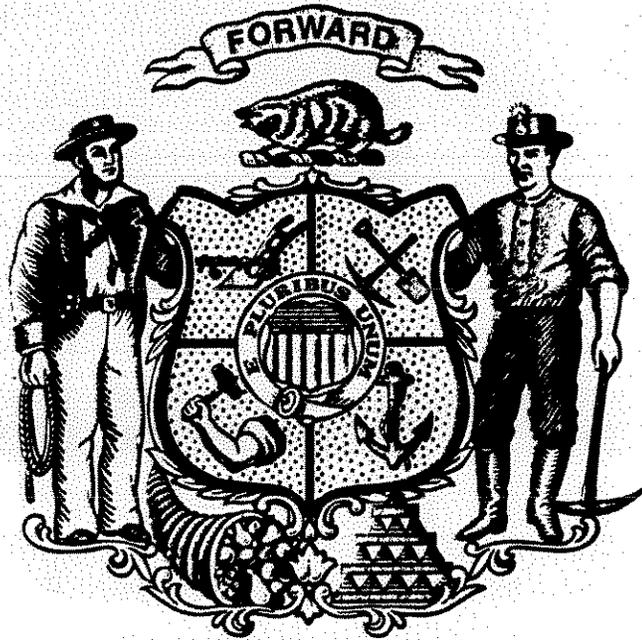
1. An employer, if the HSA is set up under a group plan.
2. The savings in premium that is generated by purchasing a large deductible plan in comparison with a small deductible plan.

Everyone can benefit from an HSA, regardless of your health status or financial condition. The concept of this plan is to fund the account through the savings realized by purchasing a large deductible major medical policy. Statistically, only a small percentage of consumers actually have large catastrophic claims. For the small minority of people who will end up using those savings for medical expenses, they are no worse off than if they purchased an expensive health insurance policy that had little or no deductible. However, for the majority of people who incur very little medical expenses during the course of a year, the savings remains their money rather than the insurance companies. This type of consumer driven health care benefits all consumers.

Ironically, Wisconsin consumers continue to purchase health plans with higher deductibles each year. For many, they have already purchased a qualified high deductible plan. All this legislation does is provide tax incentives that allow individuals to put aside money to help pay for medical expenses, with the potential of large savings over traditional plans. Objecting to this legislation is simply hurting the thousands of cost minded Wisconsin citizens who have, and who will purchase these types of plans in an effort to save money. Wisconsin must provide its citizens with the same tax savings provided by the federal government, and by nearly every other state, for the purchase of these plans.

We urge you to support AB 4.

Thank you for the opportunity to provide our comments.





WISCONSIN ASSOCIATION
OF PROVIDER NETWORKS

4600 American Parkway • EastPark One • Ste. 208 • Madison, WI 53718

(608) 243-1007 • Fax (608) 241-7790

Written Comments on Assembly Bill 4

Assembly Committee on Insurance

January 20, 2005

The Wisconsin Association of Provider Networks (WAPN) is an association whose members represent nearly **1.8 million Wisconsin health care consumers**. In 2004, our members contracted for over **\$4.5 billion dollars in health care expenditures**. Our members are made up of non-HMO entities that produce Preferred Provider Organization (PPO) type products, including provider networks and insurance carriers.

WAPN supports AB4, as it provides real solutions to Wisconsin's health care cost crisis, and provides the ability for consumers to purchase affordable and comprehensive health care coverage. Health Savings Accounts are a new option for health insurance and they have two parts. The first part is a health insurance policy that covers large hospital bills. The second part of the Health Savings Account is an investment account from which you can withdraw money tax-free for medical care. Otherwise, the money accumulates with tax-free interest until retirement, when you can withdraw for any purpose and pay normal income taxes.

The health care cost crisis we find ourselves in will continue until normal consumer behavior is applied to the purchase of health care. Such behavior has been prevented through current benefit design and structure, with the use of first dollar coverages and the continued removal of the patient from the financial responsibility of their own health care. Consumer driven plans, like HSA's, provide the opportunity to bring back normal consumer behavior to the health care marketplace.

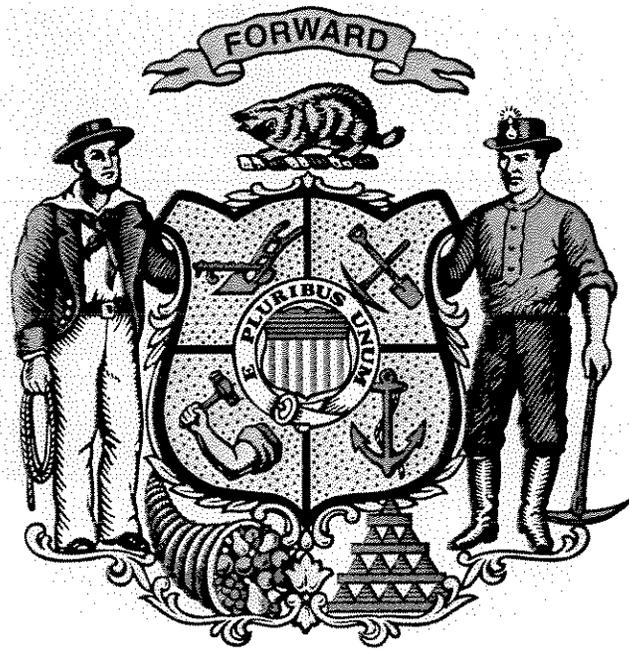
The objections to Health Savings Accounts have consisted of the claim that these plans are only for the wealthy and healthy. This is simply not supported by the facts. The statistics with the insurers selling these plans show that 46% of the HSA consumers have family incomes of less than \$50,000 per year. One insurer with nearly 70,000 covered HSA lives finds that average self-reported income during the HSA application process was approximately \$32,000. 36% have only high school or technical school training. 38% live in homes with a market value of less than \$125,000 and 27% have a net worth of less than \$25,000. As for the age group buying these plans, some of the statistics by these same insurers found that over 70% of purchasers were over 40 years of age. Furthermore, these same statistics show that HSA's are helping with the uninsured. Over 40% of the HSA applicants did not list any prior coverage and nearly 33% had not had coverage for at least 6 months prior to enrollment. One HSA Administrator I talked with said that nearly 90% of all groups

that are purchasing HSA plans are groups under 5 lives in size. These size groups are typically not wealthy individuals. These size groups are typically made up of low wage earners.

Wisconsin is only one of 11 states that have not provided their residents with the same tax incentive that the federal government has provided. One HSA Administrator I talked with gets nearly 100 calls a month from Wisconsin residents confused as to why they aren't getting the state tax credit. The only answer they are able to give is that the legislation was vetoed. This doesn't sit well with Wisconsin residents. By not conforming to the Internal Revenue Code, Wisconsin taxpayers are also exposed to higher administration costs from their income tax preparers, as well as through flexible compensation administrators.

WAPN urges you to support AB4 and we also urge you to contact the Governor asking him to finally sign this legislation into law.

Thank you for the opportunity to provide our comments.





WISCONSIN

**Statement Before the
Assembly Committee on Insurance**

By

**Bill G. Smith
State Director
National Federation of Independent Business
Wisconsin Chapter**

**Thursday, January 20, 2005
Assembly Bill 4**

Madam Chair and members of the Assembly Committee on Insurance, thank you for the opportunity to make some brief comments on behalf of the 13,000 member firms of NFIB/Wisconsin.

This important legislation, which would adopt federal law as it relates to the establishment of health savings accounts, has the strong support of our state's small business community.

We believe HSAs have the potential to do for health care what IRAs have done for retirement savings. While obviously adopting the federal law will not have as great an impact as the federal tax advantages, extending state tax advantages will further enhance the appeal of HSAs in Wisconsin.

The benefits of Health Savings Accounts have already made these accounts very popular. Last week the America's Health Insurance Plan, a major trade association representing health insurers, reported 438,000 people have signed up for health savings accounts through September, 2004 – almost half of these individuals were over the age of 40, and 30% of the individual HSA purchasers were previously uninsured.

Assurant Health reports that 43% of its applicants were previously uninsured, while eHealthInsurance reports that approximately 33% of its HSA purchasers were previously uninsured. Assurant Health also reports 77% of HSA purchasers are families with children; 45% are from households of four or more people; 70% of HSA purchasers are over the age of 40; and to those who criticize HSAs as only for the wealthy, Assurant Health data indicates 29% of purchasers have family incomes of less than \$50,000 and 19% have family incomes of less than \$40,000 per year.

Statement Before the Assembly Committee on Insurance
January 20, 2005
Assembly Bill 4

Attached to my testimony today is a list of small business owners who are saving money on their health insurance premiums as a result of purchasing their Health Savings Account plans. You will see an Ohio self-employed engineering consultant who saves \$8,400 (66%) the first year with an HSA plan. You will also see a Minnesota small business with 15 employees that saved \$12,000 with an HSA.

There is also the Iowa small business counseling service with 8 employees who reported saving \$14,740 (32%) on health insurance premiums with an HSA. There is an Iowa OB/GYN Clinic with 13 employees that reports saving \$40,608 (38%) on health insurance premiums the first year of an HSA plan. And, finally, there is a Wisconsin small business owner, a chiropractor, who reduced health insurance costs by 70% saving \$8,400 in the first year with an HSA plan. As a result of these dramatic savings, these employers are able to make significant contributions to the HSAs of their employees.

Also attached to my testimony is a copy of an article that appeared in NFIB's member magazine *MY Business*. This article shows an example of how contributions to an HSA can even result in substantial savings for retirement. The article also quotes a Nashville NFIB member who will save 30-40% each year with an HSA account.

Since 1998, NFIB Member Benefits Corporation reports over \$12 million in premiums between MSAs and HSAs. There are thousands of NFIB member employers and employees currently covered through an HSA insurance plan.

Finally, Madam Chair:

- HSAs provide the employee with power and control over their own money and encourage physicians to act autonomously without interference from HMOs and insurance companies;
- Offer additional financial security for today's mobile workforce;
- HSA contributions are 100 percent tax-deductible;
- Funds in HSAs grow tax-deferred, medical costs are tax and penalty free, and left over funds from one year are rolled over to the next. In short, you get the triple crown of tax planning with an HSA. The money goes in tax free, it grows tax free, and it comes out tax free. And, hopefully, soon the money will also be free of state taxes.

Thank you, and I urge the Committee to act promptly and favorably on Assembly Bill 4.