HSAs: Four Years Later and Growing Strong

by Cora M. Tellez

The law creating Health Savings Accounts (HSAs) was enacted four years ago amidst growing concerns about rising healthcare costs and a burgeoning interest in what consumers can do to reduce costs and utilization, and the financial incentives to help them do so. In the intervening years, much has been written about HSAs, from glowing reports about adoption rates to raging criticisms about their impact on consumers who have inadequate tools to make good healthcare purchasing decisions.

Like most new trends, consumer directed health care plans (CDHP) and the accounts that accompany them (like HSAs), need time to mature and become fully absorbed in the mind-set of average citizens. The HMO did not become a household word until at least 10 years after its enactment as a required offering to employers. Similarly, IRAs introduced over 20 years ago were slow to be adopted, but now represent a crucial element in retirement planning.

We now have evidence of a growing adoption of HSAs. We have emerging evidence about their utility in abating challenging medical trends. This article will discuss the factors that are driving higher adoption and will review emerging trends about consumer demographics and behavior.

Adoption of HSAs

There is growing evidence that HSAs are entering the American mainstream in terms of serious consideration, especially by big companies and they are steadily growing in adoption by small and mid-size companies.

A recent survey by the American Association of PPO Plans (March 4, 2008) notes that enrollment in CDHPs grew by 25% in 2007, from 10 million in 2006 to 12.5 million in 2007. Once begun, enrollment grows steadily. Average enrollment grew significantly each year among companies that offered an HSA for three years, reaching 29% in year three. The same survey notes that 41% of large companies (those with over 20,000 employees) offered an HSA or HRA in 2007 versus 37% in 2006.

Another survey by Watson Wyatt and the National Business Group on Health (March 13, 2008) notes that more companies are offering CDHPs and enrollment has nearly doubled over the past two years.

Kaiser Permanente, the most ardent proponent of organized group practice HMOs in our time, has been introducing HSA-compatible products in recent years. This is a profound statement about the emerging role of CDHP and HSAs in the thinking of industry leaders. George Halvorson, CEO of Kaiser Health Plans, was quoted in the *San Francisco Business Times* (March 28, 2008) noting that Kaiser's membership growth in 2007 came from its CDHP plans, not its core products.

In terms of financial assets, HSAs are a multi billion-dollar business. This asset growth is coming at a time when financial institutions are pinched for cash deposits. It may explain, in part, the growth in the number of financial custodians for these assets.

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Four Drivers of HSA Growth

There are four main drivers explaining the significant growth in HSAs:

1. **The Economics of Switching To an HSA Compatible Plan**
   Wages are rising at about 3% per year while healthcare costs are increasing at three times that rate. CDHP/HSAs are experiencing more moderate trend increases. The premium rate increase for companies with high CDHP enrollment is roughly half those facing only traditional health coverage (3.5% versus 7%), according to the Watson Wyatt report.
   Watson Wyatt also compared best and worst performing employers in terms of healthcare costs. Best performing employers had two-year cost increases of 1% while worst performing employers had a 10% increase. Among the features of best performing employers was having a CDHP.
   A recent Milliman study reveals that CDHP claims were about 41% lower than in non-CDHP plans before adjusting for risk and benefit factors.
   Employers will move to CDHP/HSA plans when there are compelling financial reasons to do so. The premium savings must be significant enough to offset natural concerns about switching and employee unease about higher deductibles.
2. **Improved Benefit Designs Limit Out-Of-Pocket Cost Exposure**
   We've noticed that with top selling CDHP products, the deductible is equal to the out-of-pocket maximum. For employees, that means reduced risk of high out-of-pocket costs, and greater certainty about cost exposure. These plans also cover many preventive care services outside of the deductible, such as well-baby care and cancer screenings.
3. **Recent Regulatory Changes Have Made It Easier To Open HSA Accounts**
   The US Treasury Dept.'s ruling in 2007 has vastly reduced the complicated formulas around contribution (no more pro-rating of contributions, for example.) Moreover, the government has considered the issue of low-wage earners and their ability to save funds in an HSA. Employers can now contribute more to low wage workers and their families. Finally, anticipating concerns about catastrophic events befalling HSA accountholders, the Treasury Dept. has allowed IRA, HRA, and FSA rollovers as well as accelerated employer contributions to help employees faced with such events. While catastrophic claims occur rarely, they still represent a key concern for employees.

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4. **Benefit Consultants and Insurance Agents Are Increasingly Suggesting CDHP/HSA Plans To Their Clients**
   While initially reluctant to recommend these plans because of their newness and potential impact on incomes, they have become more comfortable with these plans. We've noticed that a few brokers are converting their entire book of business to HSA plans. In so doing, they have saved enough money for the employers so that they have an easier sale with other lines of business previously considered unaffordable.

HSA Demographics

Because there is little published material about individuals choosing and using HSA accounts, we've relied on data from Sterling HSA to make the following observations:

- The average age of HSA accountholders is getting younger. It was 52 in 2004 and 43 in 2007.
- In 2004, the majority of Sterling's clients were self-employed individuals. Today, 85% of our clients enroll via their employers.
- The employer base has changed from small professional affiliations to a wide diversity of public and private employers of varying size.
- Clients value convenience and ease of use. More than 52% of our clients have registered online to view account activity and transact business.
- Education and communication about HSAs continue to be an important driver of client satisfaction.
- As expected, balances in HSA accounts are growing. Sterling accountholders ended 2007 with an average balance of $2,552 compared with an average ending balance of $1,984 in 2006.
- Employers are contributing an average of $900 to each employee's HSA account.
- As balances build, accountholders are increasingly interested in self-directed investments.

While health savings accounts are still new to the general public, they are becoming more familiar among insurance agents and their clients. As knowledge and experience grow about these accounts, we should expect to see even faster adoption. The financial impact of switching to HSA plans and seeding of HSA accounts must be reflected in the employer's bottom line. If our hypothesis is correct that consumers will behave in their best self-interest given financial incentives to do so, we should expect more moderate medical trends for employers enrolled in such plans. In turn, that should translate into increased adoption of HSAs. ❑

Cora Tellez founded Sterling HSA in 2004 and serves as its president and CEO. She has 25 years of management experience in healthcare finance and delivery. Prior to founding Sterling HSA, Cora was president of the health plans division of Health Net. She has also served as president and chair of Prudential's western healthcare operations, CEO of Blue Shield of California, Bay Region and regional manager for Kaiser Permanente of Hawaii. Cora received her master's degree in public administration from California State University and is a Phi Beta Kappa graduate of Mills College. She serves on the boards of First Consulting Group (NYSE:FCGI) and Crescent Healthcare and serves on the boards of several nonprofit organizations.