

Chapter 1

Health Savings Accounts - A New Approach



This chapter provides an overview of how Health Savings Accounts (HSAs) combined with High Deductible Health Plans (HDHPs) are poised to change the health care coverage landscape.

- ✓ The HDHP
- ✓ The HSA
- ✓ Funding (the Basics)
- ✓ The Two-part Plan-How it Works
- ✓ Not All HSAs are the Same
- ✓ HSA Transition Rules and Grace Periods

The High Deductible Health Plan

The HDHP is the insurance component of the health plan and the foundation of the HSA. The HDHP is similar to other, traditional health plans. However, unlike other plans, the HDHP must satisfy certain requirements regarding deductibles and out-of-pocket limits to be combined with an HSA. The purpose of the HDHP is to cover higher cost health care expenses that would be difficult to pay for out-of-pocket—care which is unexpected and very expensive. Plans that satisfy these deductibles and out-of-pocket limits are referred to as qualified HDHPs. Here are the terms and concepts you need to be familiar with:

Deductibles

The deductible is the amount of covered expenses that an individual must pay in a given plan year before any charges are paid by the medical care plan. The plan year may be the calendar year (January 1 to December 31), or some other twelve-month period your employer or insurer chooses for managing your plan and keeping track of deductibles and other limits. For a single person with an HDHP, the deductible must be \$1,000 or higher; it's \$2,000 or more for a family. In future years, the deductible will be increased with increases in the Consumer Price Index (CPI) to keep up with medical care inflation.

Some HDHP plans provide multiple deductibles, sometimes called "embedded" deductibles. In such plans, the lowest deductible in the plan is the one that determines whether the plan is a qualified HDHP.

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Example: The plan in this example has an embedded deductible that keeps it from being an HDHP. The Jones family is covered under a plan that provides family coverage with a per-person deductible of \$1,000 per family member. The plan begins paying for care once an individual in the family exceeds \$1,000 in expenses even if the \$2,000 family deductible has not been met. Mr. Jones incurs covered medical expenses of \$1,500 during the year. The plan pays benefits of \$500 on his behalf, even though the \$2,000 family deductible has not been met. Since benefits are available before the family's covered medical expenses reach \$2,000, the plan is not an HDHP, and the family is therefore not eligible to contribute to an HSA. Without the \$1,000 per-person deductible, however, the plan would be an eligible HDHP.



The consumer is responsible for keeping records of expenses that qualify for reimbursement under the HSA, and for documenting these expenses if audited by the IRS. The HDHP insurance carrier will keep track of your expenses that are covered under the health plan as it processes your claims and will determine when you have met your plan's deductible.

Out-of-Pocket Limits

The deductible governs the first expenses you must pay in a plan year before the HDHP picks up the tab for the services it covers. The out-of-pocket limit signals the last expenses you must pay. Most health insurance plans limit the out-of-pocket expenses that you have to pay in a given plan year.

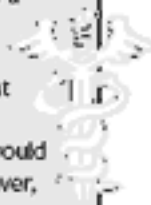
Amounts you pay as deductibles, co-payments, or

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coinsurance, are included in your out-of-pocket expenses, which are kept as a running total. Insurance premiums you pay are not counted toward out-of-pocket limits. Once you have reached your plan's limit for the year, remaining eligible expenses are covered at 100 percent regardless of the plan's usual co-payment or coinsurance arrangements. Some plans refer to this limit as the stop-loss limit.

For 2004, a qualified HDHP's out-of-pocket limits must be no higher than \$5,000 per year for self-only coverage and no higher than \$10,000 per year for family coverage, though they can be lower. Your HDHP must explicitly state the out-of-pocket maximum, unless the plan's design limits your out-of-pocket spending within the limits of the law.

Example: Dean and Laurie and their 2 children have a family plan. Their plan specifies that each out-of-pocket maximum is \$2,000, after which the plan pays 100 percent for each member of the family that reached that maximum. Since the out-of-pocket maximum per family by law is \$10,000, their plan would be a qualified HDHP ($4 \times \$2,000 = \$8,000$). However, if they had four children, their plan would not be a qualified HDHP, because the maximum out-of-pocket limit would be higher than legal maximum ($6 \times \$2,000 = \$12,000$).



Network Plans

If the HDHP is a network plan (such as a PPO), services can be re-priced to reflect the network discount, even if the deductible has not yet been met. A network plan is a health plan that generally provides more favorable pricing