

HJR

18

Alaska State Legislature House of Representatives

COMMITTEE ASSIGNMENTS:

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TO: Senator Lyda Green, Chair
Health, Education & Social Services Committee

FROM: Representative Pete Kott

DATE: February 23, 1995

RE: HJR 18

HJR 18, Relating to medical savings account legislation has been referred to the Senate Health, Education and Social Services Committee.

This resolution calls on Congress to enact legislation to allow individuals to establish medical savings accounts. These accounts would be funded through savings and efficiencies of use by private citizens. The concept requires no new federal bureaucracy and would not bear an additional cost for employers.

Medical savings accounts are an important element in allowing the private sector to control health care costs without government interference.

Enclosed is a copy of HJR 18, a copy of the adopted fiscal note, and a sponsor statement.

Please schedule this resolution for a hearing at your earliest convenience. Thank you in advance for your consideration.



Representative Pete Kott

FEB 23 1995

A handwritten signature in black ink, appearing to read "Pete Kott".

FISCAL NOTE

STATE OF ALASKA
1995 LEGISLATIVE SESSION

NO. _____
BILL VERSION: HJR 18
PUBLISH DATE: _____

Revision Date: _____
Title: Relating to medical savings account
legislation.
Sponsor: Representative Kott
Requestor: Hon. HESS

Department Affected: Legislative Affairs Agency
BRU: All
Component: All

COMPONENT SERIAL NO:

Expenditures/Revenues: (Thousands of Dollars)

OPERATING	FY 96	FY 97	FY 98	FY 99	FY 00	FY 01
PERSONAL SERVICES	0	0	0	0	0	0
TRAVEL	0	0	0	0	0	0
CONTRACTUAL	0	0	0	0	0	0
SUPPLIES	0	0	0	0	0	0
EQUIPMENT	0	0	0	0	0	0
LAND & STRUCTURES						
GRANTS, CLAIMS						
MISCELLANEOUS						
TOTAL OPERATING	0	0	0	0	0	0

CAPITAL	0	0	0	0	0	0
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REVENUE FUND SOURCE	0	0	0	0	0	0
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FUNDING: (Thousands of Dollars)

GENERAL FUND	0	0	0	0	0	0
FEDERAL FUNDS						
OTHER FUND SOURCE						
TOTAL	0	0	0	0	0	0

POSITIONS:

FULL-TIME	0	0	0	0	0	0
PART-TIME	0	0	0	0	0	0
TEMPORARY	0	0	0	0	0	0

Estimate of current year impact: _____

ANALYSIS: (Attach a separate page if necessary)

Zero fiscal impact.

Prepared By: Karla Schofield, Deputy Director
Division: Administrative Services

Phone: 465-3852
Date: 2/13/95

Approved By: Pamela A. Vami, Executive Director
Agency: Legislative Affairs Agency

Date: 2/13/95

Distribution (by preparer): Leg. Finance, Legislative Sponsor, Requestor, OMB, Gov., & Impacted Agency(ies).

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HJR 18 SPONSOR STATEMENT

As medical costs nationally and in Alaska continue to rise, the need for innovative approaches to health care cost containment becomes more acute. The concept behind Medical Savings Accounts is to encourage employees to shop more carefully for medical services. It recommends the purchase of high deductible coverage by employers. The savings realized by this effort results in reduced health insurance premiums. These savings are then placed by the employers in individual employee Medical Savings Accounts.

Employee Medical Savings Accounts then may be used by employees to purchase additional, more specific insurance coverage and to pay deductibles incurred under employer provided or employee purchased medical coverage plans.

Medical Savings Accounts belong to the individual employee and move with the individual to purchase health insurance when between jobs or for coverage when re-employed, even when with a different employer.

The additional benefit to Medical Savings Accounts is that they allow the individual to select and purchase coverage at reduced cost without a new federal bureaucracy and would be revenue neutral to employers. It is compatible with the free market in that it protects individual freedom and rewards prudent decision making.

HJR 18 urges Congress to enact legislation that will make Medical Savings Accounts a viable option in the national effort to reduce and contain health care costs.

I urge your support for this legislation.



Representative Pete Kott



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I urge your support for this legislation.



Representative Pete Kott



A L A S K A



NFIB

National Federation of
Independent Business

February 23, 1995

Representative Pete Kott
State Capitol
Juneau, AK 99801-1182

Subject: NFIB Support for HJR 18

Dear Representative Kott,

With nearly 4,590 Alaska members, the National Federation of Independent Business/Alaska is the state's largest small-business advocacy organization. On behalf of the Alaska membership I would like to thank you for introducing House Joint Resolution 18 in support of Congress establishing Medical Savings Accounts.

Each year, NFIB/Alaska polls its diverse membership on a variety of issues. The federation uses the poll results to form its legislative agenda. The August 1994 Federal ballot results showed a clear majority of respondents favored Congressional action to create tax-free medical savings accounts.

Enclosed you will find an article on Medical Savings Accounts prepared by the National Center for Policy Analysis. I hope you find this to be helpful background information on this issue.

Sincerely,

Thyas Shaub



Based On Brief Analysis No. 105
Released on Wednesday, April 20, 1994

Medical Savings Accounts The Private Sector Already Has Them

All across the country, private employers are discovering a new way of controlling health care costs. It works so well that at some companies health care costs are actually going down. The secret: giving employees incentives

Take the United Mine Workers, for example. Last year they had a health plan with first-dollar coverage for most medical services. This year they accepted a plan with a \$1,000 deductible. In return, each employee receives a \$1,000 bonus at the beginning of the year, and employees get to keep whatever they don't spend. As a result, the mine workers still have first-dollar coverage, but now, the first \$1,000 they spend will be their own money rather than their employers' money.

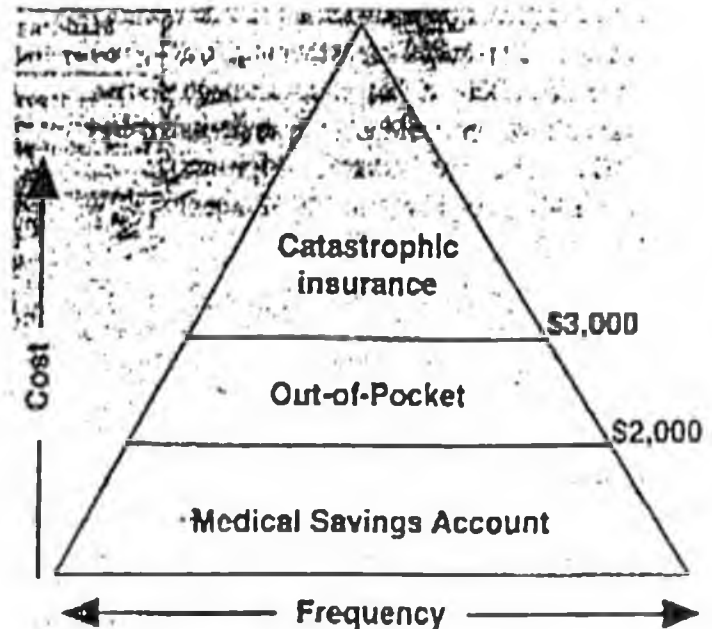
If the mine workers are like other employees, they and their families will respond to the new incentives by finding numerous ways to cut out waste and reduce their health care spending.

Saving Money by Empowering Employees. Most health economists agree that the primary reason why health care costs are rising is that the money we are spending in the medical marketplace is usually someone else's.

More than a decade ago, the Rand Corporation discovered that when people are spending their own money on health care they spend 30 percent less with no adverse effects on their health. Some employers are putting this principle to work:

- Until the IRS forced a change in the plan, Quaker Oats had a high-deductible policy and paid \$300 annually into the personal health accounts of employees, who got to keep any unspent balance; the result: over the past decade the company's health care costs grew at an average of 6.3 percent per year, while premiums for the rest of the nation grew at double digit rates.

- *Forbes* magazine pays each employee \$2 for every \$1 of medical claims they do not incur up to a maximum of \$1,000; the result: *Forbes'* health costs fell 17 percent in 1992 and 12 percent in 1993.



- Dominion Resources, a utility holding company, deposits \$1,620 a year into a bank account for the 80 percent of employees who choose a \$3,000 deductible rather than a lower deductible; the result: the company has experienced no premium increase since 1989, while other employers faced annual increases of 13 percent

- Golden Rule Insurance Company deposits \$2,000 a year into a medical savings account (MSA) for employees who choose a \$3,000 family deductible (see the figure); the result: in 1993, the first year of the plan, health costs were 40 percent lower than they otherwise would have been.

Why Employees Like Medical Savings Accounts. These plans are popular with employees because: (1) they can save money in an amount directly related to their own efforts; (2) they are not deterred from seeking medical care by the traditional out-of-pocket deductibles; (3) they can usually use their medical savings to buy

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services not covered by the employer's plan; and (4) they are usually not restricted to certain doctors as they would be under managed care plans.

Take Golden Rule's experience, for example. As the table shows, employees can choose a traditional policy with a \$500 deductible and a 20 percent copayment up to a maximum of \$1,000. If they choose a high deductible, however, Golden Rule deposits \$1,000 (individual) or \$2,000 (family) into their medical savings account in 12 equal installments.

Last year, 80 percent chose the medical savings account option, and in 1994 the number is up to 90 percent. It's not hard to understand why. At year-end 1993, employees withdrew the surplus remaining in their MSAs — an average of \$602 per employee. These funds were a direct reward for being a prudent shopper in the medical marketplace.

Why Employers Like Medical Savings Accounts. When employees save money for themselves, they save for their employers as well. For example, at Golden Rule last year, medical costs above the catastrophic limits were about 60 percent of what had been projected.

What About Preventive Medical Care? Some critics claim that MSAs will encourage people to avoid preventive care. Yet experience shows the reverse is true.

With MSAs, people get preventive care that they might have otherwise postponed.

MSAs make money available immediately when the medical need for it exists. This allows people to make purchases they might not make if they had a traditional deductible requiring an immediate out-of-pocket payment. A survey of Golden Rule employees who opted for MSAs found that one out of every five used their MSA for a medical service they would not have purchased under

Options For Golden Rule Employees

	INDIVIDUAL		FAMILY	
	Conventional Policy	Medical Savings Account Policy	Conventional Policy ¹	Medical Savings Account Policy
Maximum deductible	\$500	\$2,000	\$500	\$3,000
Maximum copayment	\$1,000 ²	- 0 -	\$1,000 ²	- 0 -
MSA deposit	- 0 -	\$1,000	- 0 -	\$2,000
Total out-of-pocket exposure	\$1,500	\$1,000	\$1,500	\$1,000

¹ The figures in this column are per family member up to a maximum of three people.

² 20 percent of the first \$5,000 of expenses above the deductible.

What About Adverse Selection? MSAs benefit the sick as well as the healthy. For example, those Golden Rule employees who are certain to have more than \$3,000 of expenses are better off choosing MSAs. That's because their overall out-of-pocket costs will be lower. Moreover, Golden Rule allows employees to borrow against future MSA deposits in cases of catastrophic illness that occur early in the year.

What About Taxes? Under current law, unspent medical savings account balances are taxable, but health insurance premiums paid by an employer are not. Thus the tax law subsidizes third-party insurance and penalizes individual self-insurance. In this way, the tax law subsidizes the problem and penalizes the solution. Wise tax policy would give just as much encouragement to self-insurance through medical savings accounts as it gives to third party insurance

Recommended Reading: John Merline, "Employers as Health Reformers," *Investor's Business Daily*, March 18, 1994 and Rachel Wildavsky, "Here's Health-Care Reform That Works," *Reader's Digest*, October 1993; "Personal Medical Savings Accounts: Medical IRAs: An Idea Whose Time Has Come," *NCPA Policy Solutions*, No. 22, July 22, 1994.



Based on a forthcoming Brief Analysis

Answering the Critics of Medical Savings Accounts: Part I

Medical Savings Accounts (MSAs) are probably the single most popular idea on Capitol Hill. In this session of Congress they have been included in 24 different proposals with 243 cosponsors. They have been endorsed by Democrats and Republicans, liberals and conservatives — by people as divergent in views as Senator Harris Wofford (D-PA) and Senator Phil Gramm (R-TX).

At the same time, Medical Savings Accounts are being attacked on the left, on the right and by special interests. They have been criticized by the liberal *New York Times* and the conservative American Enterprise Institute. The most vocal criticism comes from large insurance companies who fear a huge loss of premium income if MSA deposits are tax free. Most of the criticisms are bogus. Let's see why.

Bogus Argument: Medical Savings Accounts Won't Control Costs Because...

Response: The strongest argument in favor of MSAs is that their use will control health care costs. By choosing a high deductible rather than a low one and putting the premium savings in an MSA, employees gain control over a large portion of their own health care dollars. Since MSAs are their private property, when they spend a dollar from an MSA they know that they are spending their own money rather than an employer's or an insurance company's. With this incentive, most employees find ways to cut spending without harming their health.

The critics present a number of ingenious arguments about why MSAs won't control costs. What they ignore are the facts. Even without the advantage of tax free deposits, many companies have already adopted MSAs and their experiences prove that MSAs work.

■ Until the IRS forced a change in the plan, Quaker Oats had a high-deductible policy and paid \$300 annually into the personal health account of each employee, who got to keep any unspent balance; the result, over the past decade the company's health care costs grew an average of 6.3 percent per year, while premiums for the rest of the nation grew at double digit rates

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■ Golden Rule Insurance Company deposits \$2,000 a year into an MSA for each employee who chooses a \$3,000 family deductible; the result: in 1993, the first year of the plan, health costs were 40 percent lower than they otherwise would have been.

In virtually every instance in which companies have empowered consumers rather than bureaucracies, the companies — and their employees — have saved money.

Bogus Argument: ... Individuals cannot bargain with providers as well as managed care plans can.

Response: Individuals frequently outperform third-party bureaucracies in deciding whether to obtain a service and in negotiating a price if they do obtain it. The tradition in medicine has been to undercharge individuals and overcharge bureaucracies, not the other way around. Furthermore, among different medical services, costs have been contained largely in proportion to the percentage of payments made out-of-pocket by patients. Over the past 30 years, for example, drug costs (mainly paid by individuals) have increased modestly, while hospital costs (mainly paid by third parties) have soared.

Most patients already know that many physicians will give them a better deal if they pay their own bills — especially at the time of treatment — rather than ask the physician to collect from a third-party payer. Increasingly, the same is true of hospitals. Although they rarely discuss it, many hospitals have special package prices and discount rates for uninsured patients who pay their own bills — usually lower than the fee charged by insurance companies and large employers.

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Will individuals *always* outperform bureaucracies in the medical marketplace? That's not clear, but the burden of proof is on anyone who argues in favor of bureaucracies. There also may be a third option. Most employers already have negotiated special discounts with doctors and hospitals. If employees find they cannot get a better deal on their own, they can take advantage of their employer's discount, even if they are paying the bill from their MSA.

Bogus Argument: ... people would spend MSA funds on services not covered by an employer's policy.

Response: Many employer policies do not cover such providers as chiropractors and marriage counselors and such services as acupuncture or in vitro fertilization. Given access to MSA funds, would employees spend more on these types of services? Some might. But many employees can spend pretax dollars on these services today through Flexible Spending Accounts.

More importantly, this argument is irrelevant. Health care spending is a social problem only because most of the time we are spending someone else's money. If we were spending our own money, it would not be a social problem. For example, most of us do not know or care how much the nation spends on shoes, or what shoe spending is as a fraction of GDP. Similarly, we have no social reason to care how much people spend on chiropractors — as long as it is their own money.

Bogus Argument: ... Medical Savings Accounts would undermine the ability of managed care to control costs.

Response: Some evidence suggests that managed care has improved quality and reduced costs for such very expensive procedures as heart surgery. Because these procedures are so costly, it pays to spend money managing them. However, there is very little evidence that managed care saves more than it costs for smaller expenditures such as CAT scans and blood tests. The view that managed care works better than Medical Savings Accounts should be tested in the market, not imposed by fiat.

If the purpose of managed care is to save money by rationing health care, it probably does work best when the managers control all of the money. But if the purpose is to meet medical needs in an efficient way, it probably works best if the patients have a financial interest in seeing their needs met efficiently.

Bogus Argument: ... MSAs would affect a very small percentage of total health care spending.

Response: In a typical insurance pool, 4 percent of the people spend about half the health care dollars. However, one-third to one-half of *all* health spending is on bills below \$3,000 to \$5,000. That's why MSAs would result in such a huge transfer of money from third-party payers to individuals.

Moreover, when individuals eliminate war for themselves, in many cases they frequently also reduce costs for their employers as well. For example, if a male employee with a \$3,000 deductible finds a way to avoid a \$6,000 operation (say, because a second opinion establishes that the surgery is unnecessary), he saves \$3,000 for his employer as well as \$3,000 for himself.

Bogus Argument: ... people would use MSAs as a device to get a tax subsidy for out-of-pocket spending.

Response: Suppose that people did not increase their deductible, and that every time they had a medical expense they deposited their share of the costs in an MSA to pay the bills in order to get a tax deduction. In this case, there would be no reduction in health spending. In fact, there might be an increase because the tax deductibility of MSA deposits would amount to a subsidy for out-of-pocket health care spending.

To discourage such behavior, most serious MSA proposals restrict MSA deposits to the difference in premiums between high- and low-deductible plans. Well-designed MSA plans also prohibit making deposits in anticipation of paying medical bills. Instead, they require people to make annual decisions about their insurance coverage and MSA deposits — before, not after, medical episodes occur.



Based on a forthcoming Brief Analysis

Answering the Critics of Medical Savings Accounts: Part II

Medical Savings Accounts (MSAs) are probably the single most popular idea on Capitol Hill. In this session of Congress they have been included in 24 different proposals with 243 cosponsors. They have been endorsed by Democrats and Republicans, liberals and conservatives — by people as divergent in views as Senator Harris Wofford (D-PA) and Senator Phil Gramm (R-TX).

At the same time, Medical Savings Accounts are being attacked on the left, on the right and by special interests. They have been criticized by the liberal *New York Times* and the conservative American Enterprise Institute. The most vocal criticism comes from large insurance companies who fear a huge loss of premium income if MSA deposits are tax free. Most of the criticisms are bogus. Let's see why.

Bogus Argument: Individuals do not have sufficient information to be intelligent consumers of health care.

• **Response:** If they do not, they can solicit advice and assistance. For example, most large employers and practically all insurance companies have teams of cost management experts who judge whether, when and where medical procedures should be performed. These experienced professionals might help patients decide about complicated and expensive procedures. But their advisory roles should not include decision-making power. We should let the experts advise and the patients decide.

In addition, markets naturally generate information for those with purchasing power. One of the primary tasks of purveyors of goods and services is to provide information to potential customers. If patients had greater control over their health care dollars, health care providers would supply more information that would enable informed decisions.

Quaker Oats, International Paper and other companies have provided their empowered employees with access to sophisticated databases containing information about quality and price. But even if employers do nothing, employees can get numerous medical questions

answered at little or no cost. According to the *Harvard Health Letter*.

- Ask-A-Nurse is a 24-hour-a-day free service under which registered nurses with an average of 10 years of emergency room experience answer patient inquires.
- Doctors By Phone charges \$3.00 per minute over a 900 number and callers' questions are answered by physicians who are usually board certified.
- Pharmacy Questions? Ask the Pharmacist is another 900 number service; at \$1.95 per minute, licensed pharmacists answer questions about drugs 24 hours a day.

There are many other public and private sources from which laypersons can learn about treatment options. For example, the National Institutes of Health makes available to the general public recommendations on a range of treatments and technologies, as does the Public Health Services Agency for Health Care Policy and Research. People without access to a major medical library can access the latest journal articles via computer and modem; Medline, the National Library of Medicine's database, contains as many as 3,700 different journals. And several private organizations will search out data for a modest fee. These include the Planetree Health Resource Center in San Francisco and the nonprofit World Research Foundation in Sherman Oaks, California.

Bogus Argument: MSAs benefit only the rich.

Response: The tax treatment of all employee fringe benefits helps higher-income employees more than lower income employees. Whenever a tax is avoided, the higher the employee's tax bracket, the greater the gain. That could be changed through a system of refundable tax credits — weighted to benefit lower-income families. However, MSAs can fit into any tax structure.

MSAs for employees are not a new tax-favored fringe benefit. They are simply a new way of paying for health care that can partially substitute for traditional health insurance. Wise tax policy would treat MSA deposits the same way it treats health insurance premiums. That would level the playing field on which individuals choose between self-insurance and third-party insurance.

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Even under the current tax system, however, the allowable MSA deposits are likely to be viewed as insignificant to a rich person but important to a poor one. A single mother, living from paycheck to paycheck, may be deterred from taking her child to the doctor by the \$200 deductible in the Clinton health care plan. With an MSA, she would have the money at hand.

When MSAs empower people in the medical marketplace, those who gain the most power are not rich. They're poor.

Bogus Argument: MSAs benefit only the healthy.

Response: MSAs confer their greatest benefit on people who are sick — especially the chronically ill. Under the current system, people are being priced out of the market for fee-for-service insurance, under which they can choose their own doctor. The alternative for most people is a health maintenance organization (HMO) or other managed care plan under which the choice of doctors is limited, the doctor-patient relationship is disrupted and the bureaucracy dictates to its doctors how they will practice medicine. In this environment, it is all too easy for the bureaucracy to pursue its financial self-interest by skimping on care for the chronically ill.

That's why MSAs are a lot more valuable to sick people than to people who are well. MSAs allow people to freely enter the medical marketplace, choose any doctor and select any therapy.

When MSAs empower people, those who gain the most are sick, not healthy.

Bogus Argument: MSAs encourage people to avoid preventive care.

Response: MSAs encourage people to make sure they get a dollar's worth of value when they spend a dollar. They do not encourage people to defer needed health care. In fact, people with MSAs are more likely to get the preventive care they need. Under conventional health insurance, people receive no reimbursement until they have met the deductible, which can be a major out-of-pocket expense for low-income individuals. MSAs, by contrast, provide first-dollar coverage so that people with limited funds can pay medical expenses. A survey of Golden Rule employees who opted

for MSAs found that *one out of every five used their MSA for a medical service they would not have purchased under the traditional insurance plan.*

Bogus Argument: MSAs would attract the healthy, making the cost of a standard plan much higher than otherwise for sick people who are likely to choose it.

Response: "Adverse selection" occurs when plans attract a disproportionate number of healthy or sick people. The plans tend to adjust their premiums to reflect these choices. But the premiums then become a reflection of the people who joined the plan rather than the actuarial value of the benefits. This problem is much more serious for systems of managed competition, since adverse selection is greatest when premiums are artificially distorted by government regulations. However, some adverse selection could occur with Medical Savings Accounts.

Even so, 90 percent of the people with private health insurance obtain it through an employer, any problems are confined to the workplace and employers can easily deal with the problems. For example, if employers offer a choice of health plans, they can "tax" one plan and "subsidize" another so that the revealed price to the employees reflects actuarial value rather than the results of adverse selection.

For the remaining 10 percent who purchase individual and family policies, the marketplace premiums are already higher for people who are older and sicker. Yet these are the very people for whom the financial gain from selecting a higher deductible is greatest.

Bogus Argument: If some (healthy) employees have positive MSA balances at the end of the year, there would not be enough money to pay the medical expenses of the other (sick) employees.

Response: Even if employees did not change their behavior, the savings from lower administrative costs would be significant. As existing MSA plans prove, employees' behavior changes substantially and leads to less overall spending on medical care. As an example, *Ferber* discovered that when it paid employees bonuses for not making claims against the company insurance plan, the bonuses paid for themselves in reduced overall health costs.