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The Case for Expanding HSA and FSA Coverage to More Treatments and Health Products:

A Deregulation that Cuts Costs and Improves Care

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Introduction

Back in 2011 the federal government narrowed the range of "qualified medical expenses" that are eligible for reimbursement under Health Savings Accounts (HSAs) and Flexible Savings Accounts (FSAs). Over the counter drugs were removed from coverage although co-pays for doctor visits and prescription drugs could be used in HSAs and FSAs. While over-the-counter drugs are now eligible for HSA/FSA coverage, still many other health-related items, such as dietary supplements, weight loss programs, treatments for allergies, and alternative medicines are not reimbursed.

This White Paper finds that a move to expand the HSA and FSA coverage to add more qualified medical expenses to these coverage plans would improve health, and lower health care costs, while costing the Treasury much less in revenue than has been reported by the Congressional Budget Office. This recognition of additional health-related expenses would expand the usage of HSAs and thus reduce overall health care costs. The benefits of broadening the allowable and legitimate health-related expenditures covered by HSAs and FSAs would likely outweigh the costs.

Background

Health care costs are rising far faster than inflation and have been for the past four decades. Less expensive and more effective health remedies are available – but not always encouraged by our multi-trillion dollar medical industry.

One way to reduce costs of treatments and medications would be to give Americans more control over their health-care spending. That's difficult in today's health-care market, which is a mishmash of regulation that shortchanges consumers but benefits health insurance companies, which are seeing record profits. (UnitedHealth now has the highest per price share in the Dow, and it's **bigger than JPMorgan**, which is America's largest bank.)

The list of needed remedies is long, but one of them should be reforms that will promote greater access to the health products Americans need at an affordable cost – and this is NOT an endorsement of socialistic price controls. One of many ways to achieve health savings without sacrificing health quality is through health savings accounts and flexible spending accounts.

An HSA functions like an individual retirement account, with individuals making pre-tax contributions, which are used to fund qualified medical expenses. Today, individuals can contribute up to $3,850 for their own coverage or up to $7,750 for family coverage, with unused funds carrying over from one year to the next. With about 35.52 million Americans owning an HSA, **according to Devenir**, an HSA consulting firm, they can be a vehicle for shaking up a sizable chunk ($104 billion) of the health care market.

FSAs are also funded with pre-tax dollars, and individuals can choose how to spend on qualified expenses. But these accounts, which are held by close to two million people, are offered by employers, and the annual allocations are forfeited if they haven't been used within the calendar year. The maximum contribution is $3,050.

The biggest benefit of these accounts is that they empower individuals to take control of their health-care spending, and provide an incentive to shop around for products and services. That can help with cost containment, but also provide a pool of capital to help cover unexpected health expenses.

Despite the evident benefits of HSA and FSA accounts, they remain an underutilized resource. The Employment Benefit Research Institute (EBRI) **reports** that on average individuals contribute less than 75 percent of the maximum contribution limit to their HSA, and only 37 percent for account holders with family coverage. Even with the benefit of employer funds, FSAs are no different, with **only 2 percent** of employees contributing the maximum and almost half forfeiting part or even all of their annual contributions.

With Medicaid providing coverage for those with lower incomes, the customer base of those who have HSAs and FSAs is solidly middle class. Nearly half of those with these accounts earn less than $72,000 per year. And the highest percentage of users come from the $50,000 and $59,999 income bracket.

Because HSAs incentivize patients to seek lower cost treatments, these accounts have proven to be a money saver for families and help lower the overall cost of the medical care industry.

A landmark 2010 study comparing those with HSAs and those with traditional health insurance coverage published in Health Services Research found that "HSAs are associated with a statistically significant and economically meaningful relative decrease in spending when compared with individuals who remained in traditional plans. Overall, enrollees in HSAs spent roughly 5–7 percent less when compared with traditional health plan enrollees."

Given these savings to consumers and taxpayers, Congress should expand HSA coverage. Instead federal laws continue to impose needless restrictions on the types of health-related services, healthcare products, and preventive health measures that are covered by HSAs, even though these treatments can keep patients healthy and out of hospitals and lower overall healthcare costs.

For many years HSAs could only be used for prescription drugs, not "over the counter" (OTC) medications that millions of Americans purchase every day. During Covid, Congress passed, and President Trump signed into law the (CARES) Act which expanded coverage.

Yet many medical products remain ineligible for HSA/FSA coverage: nutritional supplements, vitamins, natural medicines, weight loss programs, , and some oral care products. This limitation only encourages patients to select expensive medications over less costly alternatives. Prescription drugs can often be five to 10 times more expensive than over-the-counter treatments.

The use of options outside of prescription drugs can have significant health benefits. A recent **meta-analysis** conducted by the US Preventive Services Task Force found that simply taking aspirin can lower the risk of cardiovascular disease and stroke, the leading cause of mortality in the U.S., accounting for more than 1 in 4 deaths. A economic study commissioned by the CRN Foundation identified billions of dollars in healthcare expenses that could be reduced by the appropriate use of nine specific dietary supplement **regimens**. For instance, well-documented clinical trials demonstrate that calcium and vitamin D can significantly reduce the risk of osteoporosis; widespread usage of these supplements (at a cost of 28 cents a day) could reduce emergency room visits from falls and fractures attributable to osteoporosis with healthcare savings of nearly $20 billion between 2022 and 2030.

A recent **study** from the Consumer Healthcare Products Association (CHPA) estimates that OTC medicines save the U.S. healthcare system $167.1 billion a year. So for every dollar that is spent on OTC drugs, the healthcare system saves $7.33. These savings are primarily derived from low cost of OTC drugs compared to pharmaceuticals and the avoided cost of unnecessary doctors visits for minor ailments. These savings don't even account for the estimated $45 billion in indirect value from workplace productivity due to fewer missed workdays.

What Is Blocking Reform and Deregulation?

Several efforts have been made to expand the allowable range of qualified medical expenses, but these attempts have run into roadblocks from exorbitant—and faulty—cost projections from the Congressional Budget Office and the Joint Committee on Taxation. In 2019, **CBO said** that expanding coverage to include dietary supplements in HSAs and FSAs would cost more than $3.6 billion over four years. In 2016, JCT put the cost at $4.1 billion in revenue losses.

These "losses" were based on a inaccurate forecast that assumes consumers would significantly boost their pre-tax contributions to the accounts as a result of the broader options, thus depriving the Treasury of revenue from income taxes and payroll taxes.

But these analyses don't reflect research over the past decade showing that when Congress alters the benefits available through HSA/FSA accounts, consumers often set aside roughly the same amount in their pre-tax accounts. When factoring in inflation, consumers' contribution levels have declined. While there could be some revenue loss to the Treasury, the taxpayer "cost" is likely to be much less than the "static analysis" by CBO and Joint Tax forecasts. Static analysis is the failure to take into account behavior changes when laws are revised or changed.

A study by Lindsey Associates – Larry Lindsey is a former Federal Reserve Board Governor and former chief economist at the White House – found flaws in the CBO/JTC scoring: "These revenue costs reflect the fact that certain taxpayers would increase their tax-deductible contributions to HSAs and/or their reimbursements from FSAs and HRAs. The costs reflect both reductions in personal income taxes (direct effect) and payroll taxes (indirect effects). In this paper, we examine the most recent data on the utilization of HSAs, FSAs and HRAs to arrive at an estimate that is significantly lower than JCT's: a revenue loss of approximately $1.3 billion in both direct and indirect effects."

In sum, this study finds a relatively small revenue loss to the treasury from expanding HSA and FSA coverage to OTC drugs and less than half the official government projections.

The defects of the JTC/CBO static analysis are all the more apparent in light of the previously mentioned underutilization of HSA/FSA accounts. Contrary to stashing away more pre-tax dollars in their FSA, expanding coverage would allow Americans to obtain, dietary supplements currently NOT covered by HSAs and FSAs.

Because patients with HSAs turn to less expensive treatments, expanding coverage should encourage more Americans to enroll in such accounts and this should save money to consumers AND through competitive pricing pressures, incentivize pharmaceutical companies to lower prices.

This could also put pressure on the FDA to speed up the process of approving life- saving and pain reduction medications – which will mean better health and lower prices over the long term.

There's another reason to support the change: Many OTC medications, dietary supplements, and treatments – covering everything from pain management, to allergies to smoking cessation – are cheaper than prescription medications. Nearly one in three consumers **have said** they don't take all of their prescribed medicines because of the expense of doing so. **A healthier population can translate to less health spending**. But there's no evidence that was factored into the CBO and Joint Tax calculations.

Further, a 2022 economic study entitled "Supplements to Savings: Health Care Cost Savings from the Targeted Use of Dietary Supplements" revealed that widespread use of dietary supplements can save hundreds of billions of dollars in costs for the U.S. health-care system by reducing risks associated with chronic diseases. Specifically, supplement use leads to direct cost savings via avoided adverse health events and indirect costs associated with avoided productivity losses. This is particularly important as 75% of health-care spending goes toward chronic diseases. Thus, in the long-run, expanding HSAs and FSAs to include products such as dietary supplements will be a value-add to the American health system.

The case for expansion also rests on just how much Americans spend on prescription medications. In 2019, it was $1,126. Price controls are is the worst option of all it reduces innovation and delay the introduction of new life-saving drugs. An **analysis** by University of Chicago economist Tomas Phillipson finds that drug price controls slow R&D drug innovation and can cost lives.

More free market competition and deregulation of the health care industry could lead to significant cost savings without stifling innovation. It's clear with a more deregulated regime and giving more power and flexibility to consumers to choose more freely products to keep themselves healthy, costs will fall both for individual patients and for the medical system overall.

Conclusion

HSAs and FSAs have proven to be sensible options to increase consumer choices and lower health costs. The Covid pandemic made clear the need for flexibility in how Americans can use their health dollars. The economic disruptions led millions of people to change how they access care — with the lightning-fast expansion of telehealth being the most obvious innovation.

Congress should be looking for additional ways to bring greater flexibility to the healthcare market. Including dietary supplements in HSA and FSA coverage would be one way to do that.

Retirees on Medicare could see the greatest benefit from having expanded HSA options. Most of them already supplement their government benefits with additional coverage and could use accumulated HSA savings to offset the out-of-pocket costs that come with increased usage of prescription drugs and routine care.

Fundamentally, consumers should have the right to decide how they spend their pre-tax dollars on health care. This, ultimately, is the point and the potential of wider coverage for HSAs and FSAs. When people have more freedom to choose how they will use their own tax-free health care dollars, they can shop for what works for them instead of being stuck inside the box of one-size-fits-all government-restricted options. That promotes better health and lower levels of health care spending.

The reported "cost" of this deregulation reform is greatly exaggerated. The many unaccounted health and economic benefits of allowing American consumers more flexibility in how they spend from their HSAs and FSAs will help HSA and FSA account holders with little cost to taxpayers.

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