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Updated June 22, 2023

Expanding Health Savings Accounts Would Boost Tax Shelters, Not Access to Care

By Gideon Lukens

Proposals to expand Health Savings Accounts (HSAs) often purport to help more people afford health coverage and health care, and proposed legislation in Congress would loosen restrictions on HSA contributions, withdrawals, and eligibility.[1] In reality, HSAs overwhelmingly benefit high-income people and exacerbate racial and ethnic inequities. The accounts often serve as lucrative tax shelters for people with high incomes while doing little to expand coverage and affordability. Meanwhile, HSAs already come at a steep cost to the federal government — estimated at $13 billion in 2022 and nearly $180 billion over the next ten years.[2]

Instead of expanding HSAs, which primarily benefit high-income people who already have health coverage, policymakers should target federal resources toward people who are uninsured, particularly those who have low incomes — for example, by closing the Medicaid "coverage gap" in states that have refused to expand Medicaid under the Affordable Care Act (ACA). Policymakers should also pursue policies to increase affordability, including permanently extending enhanced premium tax credits that help people afford ACA marketplace plans. Closing the coverage gap and making enhanced premium tax credits permanent would increase coverage and affordability for people with low and moderate incomes while also improving health equity.

Roughly 1 in 6 Privately Insured Adults Have HSAs

Under current law, people can set up an HSA if they enroll in a high-deductible health plan (HDHP) that meets certain standards. For 2023, this includes having an annual deductible of at least $1,500 for individuals and $3,000 for families, with a limit on out-of-pocket costs of no more than $7,500 for an individual and $15,000 for a family.[3] In 2021, 37 percent of all privately insured adults

[1] For example, H.R. 107 would no longer require an HSA to be paired with a high-deductible health plan and would increase the annual contribution limits: https://www.congress.gov/bill/118th-congress/house-bill/107. Another bill would allow gym memberships and fitness equipment to qualify as HSA expenses: https://www.congress.gov/bill/118th-congress/senate-bill/786.

[2] U.S. Treasury Department, fiscal year 2024 tax expenditures estimates, https://home.treasury.gov/policy-issues/tax-policy/tax-expenditures.

[3] IRS, https://www.irs.gov/pub/irs-drop/rp-22-24.pdf. Deductibles are an amount the enrollee must pay on their own before the plan begins covering most services.

aged 18 through 64 were enrolled in HDHPs, and slightly under half of those in HDHPs had HSAs. Nearly all of the private plans that are HDHPs with HSAs are employment-based plans, with a very small fraction being directly purchased on the individual market.[4] Both individual account holders and employers are permitted to contribute to accounts for employment-based plans, but not everyone who holds an HSA makes contributions or receives employer contributions on their behalf.

HSAs Provide a Lucrative Tax Shelter for High-Income People

Unsurprisingly, data show that HSAs overwhelmingly benefit and are more prevalent among high-income people. A Congressional Research Service analysis of 2017 IRS data found that tax returns exceeding $500,000 in adjusted gross income were the most likely to report individual HSA contributions, and returns between $200,000 and $1 million were the most likely to report employer HSA contributions.[5] (See Figure 1.) The prevalence of HSA contributions declined as income declined, and only a small percentage of low-income tax returns showed contributions.

HSAs offer substantial tax advantages for people with high incomes. Contributions are not taxed: individual contributions are tax deductible, while employer contributions are excluded from taxable income. Additionally, contributions can be invested in stocks and bonds, accruing earnings that are tax-free, and withdrawals are also not taxable if they are used for medical expenses deemed "qualified" under federal tax rules. Because of this unique "triple tax advantage" and the fact that HSA assets can be rolled over from year to year, financial advisors widely promote HSAs as investment vehicles.[6] After years of rapid growth, total HSA assets surpassed $100 billion in January 2022, with HSA investment assets (e.g., stocks, bonds) a large and fast-growing share, according to a survey of the industry.[7]

[4] CBPP analysis of 2021 National Health Interview Survey.

[5] Individual contributions to HSAs could include HSA-qualified plans that are employment-based or plans directly purchased on the individual market. Ryan Rosso, "Health Savings Accounts (HSAs)," Congressional Research Service, August 8, 2022, https://crsreports.congress.gov/product/pdf/R/R45277.

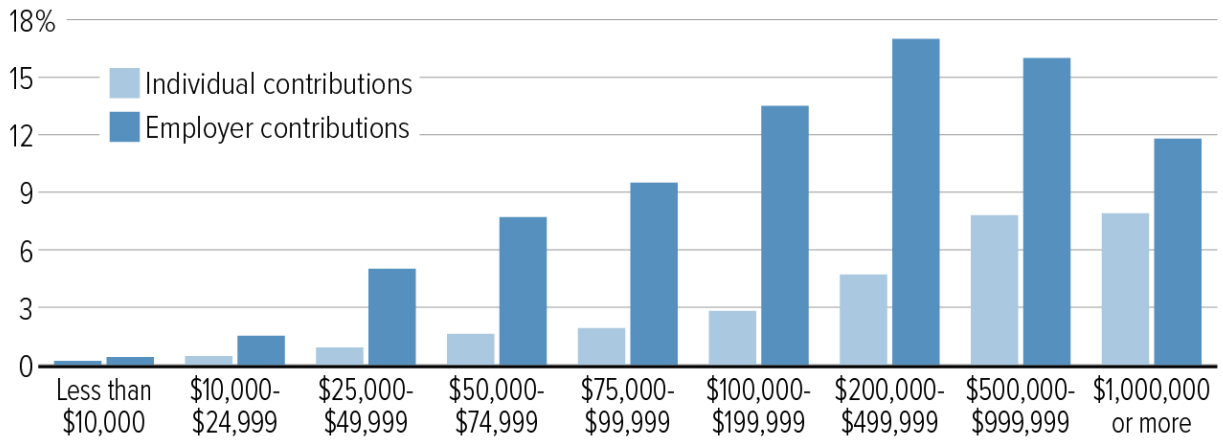
[6] Ramsey Solutions, "How to Make the Most of Your HSA Investment," December 15, 2022, https://www.ramseysolutions.com/insurance/hsa-investment.

[7] Devenir, "HSA Assets Hit $100 Billion Milestone," March 23, 2022, https://www.devenir.com/hsa-assets-hit-100-billion-milestone.

FIGURE 1

HSA Contributions Far More Prevalent Among People With High Incomes

Percentage of tax returns reporting Health Savings Account (HSA) contributions



Note: Income is measured as adjusted gross income.

Source: Congressional Research Service analysis of Internal Revenue Service data for tax year 2017

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For investors with high incomes, HSAs provide an attractive tax shelter for retirement, especially for people who have reached the contribution limit for their 401(k)[8] and other investments.[9] In 2023, the maximum annual contribution limits for HSAs are $3,850 and $7,750 for individuals and families, respectively, with an additional $1,000 available for people aged 55 and older.[10] With no income limits on who can hold HSAs, individuals with enough money can max out and roll over their HSA contributions year after year, then withdraw them tax-free in retirement to pay for their own or their family's health care expenses — and even reimburse themselves for medical expenses incurred years in the past.[11] After a person reaches age 65, HSA funds can also be used for non-medical expenses with no penalty, though withdrawals for non-medical expenses are subject to income taxes, similar to 401(k) and individual retirement account (IRA) withdrawals.

The fact that HSA contributions can be invested, accumulating tax-free earnings that compound over time, differentiates them from employer-based insurance premiums or flexible savings accounts, which are excluded from taxable income but cannot carry over from year to year. HSAs also are advantageous relative to 401(k) plans and other retirement vehicles in that both contributions and earnings are *never* taxed as long as they are used for qualified medical expenses.

[8] The contribution limit for 401(k) plans in 2023 is $22,500, and people aged 50 and older can contribute an additional $7,500 in catch-up contributions. Over 5.1 million people (roughly 3 percent of the workforce) maximized their elective retirement contributions in 2018. See https://www.irs.gov/newsroom/401k-limit-increases-to-22500-for-2023-ira-limit-rises-to-6500 and IRS W-2 Tabulations Table 2.G: https://www.irs.gov/statistics/soi-tax-stats-individual-information-return-form-w2-statistics.

[9] Ryan Ermey, "This savings account offers a 'triple tax benefit' — but 88% of users are missing out," CNBC, February 9, 2023, https://www.cnbc.com/2023/02/09/health-savings-accounts-how-to-save-for-retirement.html.

[10] IRS, https://www.irs.gov/pub/irs-drop/rp-22-24.pdf.

[11] HSAs cannot be used to pay for expenses incurred before the HSA was established.

Savings in retirement accounts are already heavily skewed toward people with higher earnings, and ownership rates for retirement accounts are far lower for Black and Latino people than for white people.[12] HSAs only widen these disparities, as discussed below.

HSAs Offer Little Benefit to People With Low and Moderate Incomes, Contribute to Inequities

HSAs are not a viable option for people who are uninsured and can't afford coverage, and people with low and moderate incomes benefit little from HSAs compared to high-income people. Those with low and moderate incomes are less likely to be able to afford to contribute, and these accounts are not helpful for people who can't afford to save, must use any available income for upfront medical costs, or are struggling with medical debt.

In 2022, roughly 68 percent of adults aged 19 through 64 with incomes under 200 percent of the federal poverty level (about $55,000 for a family of four) would not have been able to pay a $1,000 medical bill within 30 days.[13] In 2018, the majority of households had less than $3,000 in their checking and savings accounts and reported they had less than they needed for emergencies. The median household with an income of $20,000 or less had under $100 in their checking and savings accounts.[14] Almost half of uninsured adults aged 19 through 64 had difficulty paying or were unable to pay medical bills in the past year, and 80 percent reported financial problems resulting from medical debt in the past two years, such as an inability to pay for basic necessities.[15]

Additionally, people with low and moderate incomes receive a far smaller benefit than high-income people for each dollar contributed to HSAs because they are in lower marginal income tax brackets, and this lowers the value of the deduction and the tax-free earnings. For example, a large majority of uninsured people fall in the 12 percent or lower income tax bracket.[16] Were they to enroll in HSA-qualified plans, their ability to deduct HSA contributions would provide them with an income tax deduction of between 0 and 12 cents on the dollar. Likewise, a married couple filing jointly and earning $80,000 — slightly more than the median household income — would fall in the 12 percent tax bracket and deduct 12 cents on the dollar for their HSA contributions.[17] In

[12] Maria Hoffman, Mark Klee, and Briana Sullivan, "New Data Reveal Inequality in Retirement Account Ownership," U.S. Census Bureau, August 31, 2022, https://www.census.gov/library/stories/2022/08/who-has-retirement-accounts.html; U.S. Government Accountability Office, "Income and Wealth Disparities Continue through Old Age," August 2019, https://www.gao.gov/assets/gao-19-587.pdf.

[13] Sara Collins, Lauren Haynes, and Relebohile Masitha, "The State of U.S. Health Insurance in 2022: Findings from the Commonwealth Fund Biennial Health Insurance Survey," Commonwealth Fund, September 29, 2022, https://www.commonwealthfund.org/publications/issue-briefs/2022/sep/state-us-health-insurance-2022-biennial-survey.

[14] Caroline Ratcliffe *et al.*, "Perceived Financial Preparedness, Saving Habits, and Financial Security," Consumer Financial Protection Bureau, September 2020, https://files.consumerfinance.gov/f/documents/cfpb_perceived-financial-preparedness-saving-habits-and-financial-security_2020-09.pdf.

[15] Collins, Haynes, and Masitha, *op cit.*

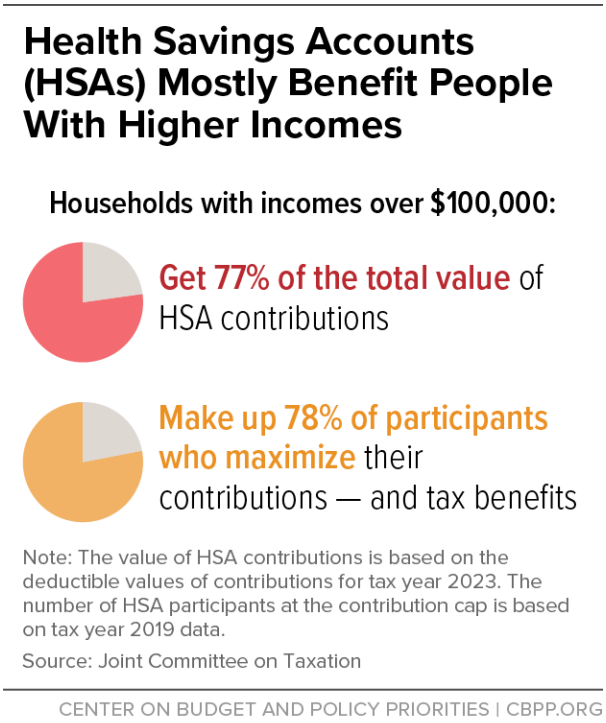
[16] CBPP analysis of 2021 American Community Survey.

[17] Median household income was about $71,000 in 2021. Jessica Semega and Melissa Kollar, "Income in the United States: 2021," U.S. Census Bureau, September 13, 2022, https://www.census.gov/library/publications/2022/demo/p60-276.html.

comparison, a married couple filing jointly and earning $700,000 per year would fall in the 37 percent bracket, saving 37 cents for each dollar put into an HSA.[18]

The benefits of HSAs are even more skewed toward high-income people when one considers not only the prevalence of HSA contributions, but also the dollar value of contributions. Many workers enroll in HSA-qualified HDHPs not because they plan to accumulate savings, but because there are no other health plans available through their employers. Likewise, many employers who offer HSA-qualified HDHPs contribute little or nothing to their employees' HSAs.[19] A study of 2012 IRS data found that tax filers in the highest income quintile were far more likely to report contributions than lower income quintiles; they also reported higher levels of contributions and were much more likely to maximize contributions and take full advantage of the tax benefits.[20] More recent data tell a similar story: 77 percent of the total value of HSA contributions in tax year 2023 went to those with incomes over $100,000, and 78 percent of HSA participants in tax year 2019 who maximized contributions had incomes over $100,000. (See Figure 2.)

FIGURE 2



Moreover, survey data show that HSAs are distributed highly unequally across race and ethnicity. Among people with private health coverage, Latino and Black people are about half as likely to have HSAs than are white and Asian people (the data do not indicate whether or how much HSA holders are contributing). (See Figure 3.) Against a backdrop of long-standing racial disparities in wealth — a typical white family in 2019 had eight times the wealth of a typical Black family and five times the wealth of a typical Latino family — HSAs provide preferential tax treatment that is disproportionately out of reach for people of color.[21]

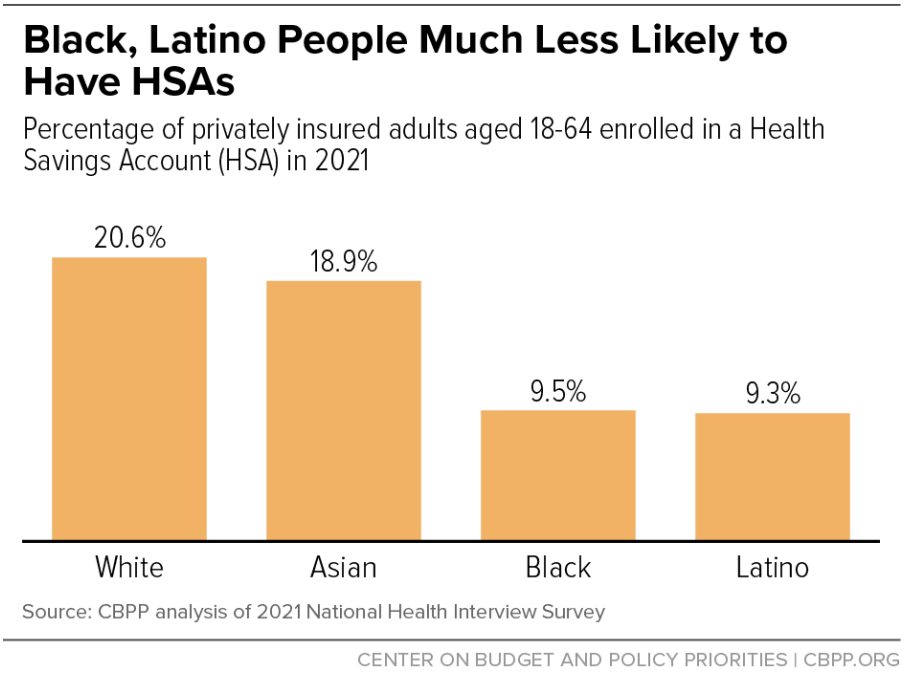
[18] IRS, "IRS provides tax inflation adjustments for tax year 2023," October 18, 2022, https://www.irs.gov/newsroom/irs-provides-tax-inflation-adjustments-for-tax-year-2023.

[19] KFF, "2022 Employer Health Benefits Survey," October 27, 2022, https://www.kff.org/health-costs/report/2022-employer-health-benefits-survey/.

[20] Lorens Helmchen *et al.*, "Health Savings Accounts: Growth Concentrated Among High-Income Households and Large Employers," *Health Affairs*, September 2015, https://www.healthaffairs.org/doi/epdf/10.1377/hlthaff.2015.0480.

[21] Neil Bhutta *et al.*, "Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances," Board of Governors of the Federal Reserve System, September 28, 2020, https://www.federalreserve.gov/econres/notes/feds-notes/disparities-in-wealth-by-race-and-ethnicity-in-the-2019-survey-of-consumer-finances-20200928.html.

FIGURE 3



Billions Spent on HSAs Could Be Used to Increase Coverage and Affordability

HSAs are not only highly inequitable, but also come at a steep cost. As noted above, HSAs are already projected to cost the federal government nearly $180 billion from 2023 to 2032. That amount is close to the ten-year cost in the President's fiscal year 2024 budget for permanently closing the Medicaid coverage gap ($200 billion) or permanently extending enhanced premium tax credits for ACA marketplace coverage ($183 billion), two policies that would each provide coverage to millions of uninsured people.[22]

Proposals to expand HSAs would only add to their costs. For example, the House Ways and Means Committee recently approved a bill that would allow HDHPs to cover telehealth services pre-deductible, while still qualifying for HSA tax benefits.[23] It is estimated to cost $5 billion from 2025 through 2033.[24] Instead of pursuing tax policies that primarily benefit high-income people while doing little to help the uninsured and people with low and moderate incomes, policymakers should focus on expanding health coverage, improving affordability, and increasing access to care.

[22] See https://www.whitehouse.gov/omb/budget/. Similarly, in an earlier estimate, the Congressional Budget Office projected that permanently closing the Medicaid coverage gap by extending ACA marketplace subsidies would cost $180 billion from 2022 to 2031: https://www.cbo.gov/system/files/2021-12/57673-BBBA-GrahamSmith-Letter.pdf.

[23] Sarah Lueck, "Health Bills Headed for a Vote in the House Undermine Consumer Protections and Market Rules," CBPP, June 20, 2023, https://www.cbpp.org/blog/health-bills-headed-for-a-vote-in-the-house-undermine-consumer-protections-and-market-rules.

[24] Description of H.R. 1843, The "Telehealth Expansion Act of 2023," Joint Committee on Taxation, June 5, 2023, https://www.jct.gov/publications/2023/jcx-12-23/.