July 26, 1996; 12:00 pm

DRAFT

Medical Savings Account Agreement

Availability of MSAs

- Beginning in 1997, MSAs are available to employees covered under a qualified employer-sponsored high deductible health plan if the employer employed, on average, no more than 50 employees during the preceding or the second preceding year. Also beginning in 1997, MSAs are available to self-employed individuals who are covered under a high deductible plan.

- In order to have an MSA, an otherwise eligible individual must be covered under a qualified high deductible health plan and not covered under any other health plan (other than plans providing certain incidental health coverage).

- Contributions can be made both by the employer and the employee, but an individual is not eligible to make contributions for a year if the employer makes contributions for that year.

- If a small employer ceases to be a small employer, it remains an eligible employer until it has more than 200 employees. After that, only employees of the employer who already have an MSA can continue to make contributions to the MSA.

Cap on taxpayers utilizing MSAs

- The number of taxpayers benefiting annually from an MSA contribution is generally limited to 750,000. In determining whether the cap has been exceeded, MSAs of individuals who were not previously insured are not taken into account. For 1997, individuals are permitted to establish MSAs if they are in the qualifying group of self-employed individuals or employees working for employers with 50 or fewer employees.

- If the cap is exceeded in a year, then contributions may be made only for individuals who previously had MSA accounts.

- After December 31, 2000, generally no new contributions may be made to MSAs except by or on behalf of self-employed individuals who previously had MSA contributions and employees (including new employees or employees who did not previously have an MSA) employed by an employer that made contributions to an MSA on behalf of any employees during 1997-2000. In addition, if the employer did not make MSA contributions, employees of an otherwise eligible employer could establish new MSAs and make new contributions if participation standards were met for employees covered under a high deductible plan in the year 2000. Self-employed individuals who made contributions to an MSA during the period 1997-2000 also may continue to make

contributions after 2000.

Tax treatment of and limits on contributions

- Employer contributions are excludable and individual contributions are deductible.

- The maximum annual contribution is 65 percent of the deductible under the high deductible plan in the case of individual coverage and 75 percent of the deductible in the case of family coverage.

Comparability rule for employer contributions

- If an employer provides high deductible health plan coverage coupled with an MSA and makes employer contributions, the employer must make available the same contribution of behalf of all employees with comparable coverage during the same period. No special restrictions are imposed on the ability of the employer to offer different plans to different groups of employees, and no special requirements are imposed with respect to self-employed individuals who own a company.

Definition of high deductible plan

- A high deductible plan is a health plan with an annual deductible of at least $1,500 and no more than $2,250 in the case of individual coverage and at least $3,000 and no more than $4,500 in the case of family coverage.

- The maximum out-of-pocket expenses with respect to allowed costs (including the deductible) must be no more than $3,000 in the case of individual coverage and no more than $5,500 in the case of family coverage. (All dollar amounts are indexed for increases in the CPI beginning after 1998.)

- High deductible plans must disclose cost-sharing and related information as required by the Secretary of the Treasury. The NAIC would be encouraged to develop standards for high deductible plans that States could adopt.

Tax treatment of MSAs

- Earnings on amounts in an MSA are not currently includible in income.

- Distributions from an MSA for medical expenses are generally excludable from income. In any year in which an MSA contribution is made, withdrawals are excludable from income only if used for the medical expenses of someone covered by a high deductible plan.

- Distributions not used for medical expenses are includible in income. Such distributions

are also subject to an additional 15-percent tax unless made after age 65, death, or disability.

- Upon death, any remaining MSA balance would be includible in the decedent's gross estate, under rules similar to those applicable to individual retirement arrangements.

Measuring the effects of MSAs

- Treasury will regularly evaluate whether high deductible plans purchased in conjunction with MSAs are providing meaningful health coverage and will make reports to the Congress.

- Treasury will monitor MSA participation and the cost of the Federal Government of such participation during the 1997-2000 period and report on such participation to the Congress.

- An independent organization with expertise in health care matters will be requested to prepare a study regarding the effects of MSAs in the small group market on adverse selection, health costs, use of preventive care, consumer choice, and other relevant issues.

E X E C U T I V E O F F I C E O F T H E P R E S I D E N T

25-Jul-1996 09:14pm

TO: (See Below)

FROM: Christopher C. Jennings
Domestic Policy Council

SUBJECT: msa deal update

Senator Kennedy and Congressman Archer struck a deal on an MSA experiment late this afternoon that appears to be consistent with the President's previously stated criteria for an acceptable study. I have no paper as of this writing, but should have something tomorrow morning. The following is based on a very short oral phone call briefing. The study is:

1. Time limited (4-years).

2. Capped -- constrained to 750,000 active policies.

3. Designed to Expire at end of study period with transition rules for those who have purchased the policies during the study:

* Firms who have offered can continue to do so. (This is to address administrative complexity of offering more than one health plan for a small firm. Kennedy does not mind so much b/c there is so much turnover in these small businesses (i.e. they shut down) and he does not believe there will be much of an increase in purchasers.

4. Structured to avoid adverse selection by limiting out-of-pocket exposure to consumers to a maximum $2,250 deductible for individuals with a total out-of-pocket limit of $3,000.

5. Structured to assure relative tax equity between MSAs and traditional plans by limiting employer contribution to accounts to 65% of the set deductible. (There was a concern that allowing much more than the savings of the purchase of MSAs to be contributed to the account would provide incentives for employers/employees to shelter income tax free in these accounts -- acutally providing an additional financial incentive to opt for MSAs.)

6. Designed to not be able to be expanded UNLESS the Congress votes affirmatives, under normal voting procedures (i.e., someone could fillibuster the bill), to expand the study permanently.

This is all I can remember for now. Needless to say, the fact that Archer and Kennedy could come to an agreement significantly enhances the likelihood that an acceptable bill will be passed by the Congress. The long-awaited conference could begin as soon as tomorrow. Since there is great pressure on both sides to complete this bill before the August recess, OMB (Nancy Ann), HHS, Labor, and Jen and I will be quickly reviewing the bill for any major problems and trying to adress them as rapidly and as non-controversially as possible. (There are a number of MSA administrative issues that we and, in particular, Nancy Ann must work out with Treasury and Joint Tax.)

The two biggest outstanding non-MSA issues: An acceptable deal on group to individual portability and an acceptable compromise on mental health parity. We will keep you apprised of developments...

cj

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