EDUCATION

PODCAST: Health Savings Accounts: How They Work and Are They Right for You

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Many individuals may not realize how health savings accounts (HSAs) work, and how they can be powerful savings tools, even into retirement. Our Kevin Murphy, Head of Strategic Accounts, Defined Contribution Investment Only Division – US, sits down with Jamie Greenleaf, lead advisor and principal with Cafaro Greenleaf, to discuss the ins and outs of HSAs.

Key Takeaways:

- Health Savings Accounts often get confused with Flexible Spending Accounts (FSAs). The money allocated to an FSA needs to be spent each year, but an HSA allows you to roll your dollars into the future and accumulate savings.
- The earnings in an HSA can grow tax free, and it can be invested. When it comes out for medical expenses, whether it's today or sometime in the future or even into retirement, it comes out tax-free.
- An HSA account follows you to different jobs. If you're working for an employer today and contribute to an HSA then switch jobs tomorrow, that HSA account comes with you.

Host/Richard Banks: *Hello and welcome to Talking Markets with Franklin Templeton.*

I'm your host, Richard Banks.

Coming up on this episode, are you over-insuring your health? Should you consider a Health Savings Account? We'll look at the key aspects to consider with HSAs. Plus, learn how they could help build your retirement savings and some ways employers might be able to better promote HSAs with their employees.

Kevin Murphy, Head of Strategic Accounts, Franklin Templeton Defined Contribution, sits down with recognized expert in the retirement plan industry, Jamie Greenleaf, lead advisor and principal with Cafaro Greenleaf. We hope you enjoy their conversation.

Kevin Murphy: So Jamie, let's start with the basics. What exactly is an HSA?

Jamie Greenleaf: An HSA is a Health Savings Account. So, if you're in a high-deductible health care plan, you may be eligible for a Health Savings Account, or HSA.

Kevin Murphy: And I'd like to think that most people actually know that in an HSA, the "S" stands for savings. But do you think that's necessarily true?

Jamie Greenleaf: No. I think, unfortunately, HSAs and FSAs get confused. FSAs are a Flexible Spending Account, which means that you need to spend it, the same year that you accumulate it, whereas an HSA is actually a Health Savings Account, which allows you to save your dollars. So, if you don't spend it all by the end of the year, that's okay. It rolls into the next year.

Kevin Murphy: I think the biggest misconceptions out there is that it is sort of a "use it or lose it" type of account. How do you get that message across when you're engaging with individuals?

Jamie Greenleaf: As we're moving from kind of the defined benefit space where the employer took care of our health care costs to now more of a defined contribution side where the employee now is becoming a consumer. There's a lot of education that needs to be done in order to kind of change the way that we consume health care and the behaviors around what we think of when we think of health savings accounts and high-deductible health care plans. And there's a lot of misconceptions. Once you understand, you definitely can see the light bulbs go off and, and most employees will say, "How come nobody ever told me I was over-insuring myself and this is money that I could have kept in my pocket?"

Kevin Murphy: Well, that's it. I think we over insure a lot of things, right?

Jamie Greenleaf: Well, I think it's similar to car insurance. If I'm driving a motorcycle that's worth $10,000, I'm not going to go insure it as if I'm driving a Porsche, which might be worth close to $100,000 and I think that's what we do with insurance. We have a tendency to not understand that we're insuring our health and, ultimately, if we're healthy and we don't have a lot of medical expenses, why do we want to over-insure ourselves and pay that additional premium? And, that's money that can be put into our pocket.

And by the way, going into an HSA, it's triple tax free, which means that the money that comes out of my pocket in savings of premiums goes into my HSA as a tax-free contribution. The earnings then can grow tax free as well, and you can also invest it. And then when it comes out for medical expenses, whether it's today, tomorrow, or sometime in the future or into retirement, it comes out tax-free.

Kevin Murphy: Could you hit on portability and how that works? I think there's some misunderstandings there, as well.

Jamie Greenleaf: HSAs are actually individually owned. So, you as an employee or a consumer who has an HSA, that HSA account follows you to different jobs. If you're working for an employer today and contribute to an HSA and tomorrow you switched jobs, that HSA account comes with you. And if you continue to contribute to an HSA or be eligible for a high-deductible health care plan with your new employer, you can continue to contribute. If, however, you move to an employer that doesn't offer a high-deductible health care plan, that HSA stays in your name and continues to grow until you can contribute to it again. And, you can still use it for medical expenses even if you're not in a high-deductible care plan at that time.

Kevin Murphy: Let's take a little bit of a deeper dive. I think starting with the employees and the individuals, because I think that's where probably, as an industry, we have the most work to do. When we set out and you, you mentioned changing behavior, what exactly do you mean by that? Could you take a little bit of a more detail on that and let us know what sort of behaviors we're looking to change and how do we go about doing that?

Jamie Greenleaf: Sure. Inertia is extremely strong, right? We tend to do the same things that we did last year. So if we walk into an open enrollment meeting and they hand us a large book and they say, select the plan that you'd like to use this year, we have a tendency to do the same thing, which is check the box, the same box that we checked last year. So, we have to change that behavior. We have to actually get employees engaged in the process.

By engaging them, we actually are going to make them better consumers of health care and ultimately there should be a cost savings to them, as well as their employer. Health care today is a financial decision. Financial decisions come with emotions. Emotions tend to be not rational at times. So, it's important that employees start to ask questions and actually get a better understanding of the direct impact that it will have on them from a financial aspect, both today and into the future before they check that box that they did last time.

Kevin Murphy: Yeah, I think that's a great point. Just speaking from my own personal experience, as I've been enrolled in an HSA, with four young children, you know, we're pretty frequent customers at the local urgent care or the pediatrician, the ER, you name it. And it forces us to be better consumers of health care. Do we really need the third or fourth opinion when it's maybe just a case of the sniffles?

What about health care costs in retirement? You mentioned it's a financial decision and I wholeheartedly agree. Are folks generally aware of this looming liability in retirement? And there's, there's multiple numbers out there. There's one that kind of consistently appears is, you know, the average healthy 65-year-old couple retiring today should expect to have about $300,000-ish out-of-pocket medical expenses, which would include premiums, as well as out of pocket expenses. You know, is that, you feel, that's an accurate number? It's certainly a scary number.

Jamie Greenleaf: So as far as accuracy, I guess it depends on how healthy you remain in retirement. But I guess that the thing that I find is that health care is going to be the number one threat to our retirement accounts. If we've been fortunate enough to work for an employer that has a 401(k) plan and we've been able to save within the 401(k) plan, when we retire, we're going to have benefits that come out after taxes and those benefits that we kind of, those savings that we put aside in those 401(k) plans are benefits so that we can turn on the lights and we could go on trips and we could visit our grandchildren. But we don't really think about planning for health care. Yet, it's potentially the number one expense that we're going to have in retirement.

And where should we save for health care expenses? Well, if we save in the 401(k) plan, that $300,000 is going to be more like $345,000 because it comes out, and we owe taxes on it, in an HSA because it comes out tax free we save.

The other thing that people don't understand is that Medicare kicks in when we retire and it covers about 51% of our health care expenses. So again, that gap that we're solving for is we have another almost 50% of out of pocket expenses that we're going to end up paying for in retirement. But then, we have things like long-term care. But, Medicare is also means tested, which means that as an employee when you retire, depending on what your modified adjusted gross income is, will determine the premiums that you pay on Medicare. HSAs do not apply to your modified adjusted gross income, which means that by, again, contributing and withdrawing from an HSA, you may get significant benefits of the taxes from a tax savings. But then also when Medicare means testing comes into play, you can potentially get some savings there, as well.

Kevin Murphy: And I think it just goes to show you that it's very complex. These are very important questions when it comes to planning for retirement and that, you know, that it truly is a financial decision. And it takes really thorough planning and I think individuals should really seek out professional help and guidance that can help navigate through all of these different scenarios. Not that this is a social security podcast, but I think social security, adding in social security decisions, which are very complex with Medicare decisions. You know, having this sort of third bucket of assets for retirement, specifically earmarked for health care costs I think is an extremely efficient way to plan for your retirement.

You mentioned earlier this sort of shift in health care from somewhat of a defined benefit traditional system to more of a defined contribution system. Could you just expand on that a little bit and what are employers faced with in making these decisions? And what are some of the challenges that the employers out there are seeing?

Jamie Greenleaf: So, employers today are looking for ways to impact their PNL [Profit and Loss] health care costs are extremely expensive, both for the employee, as well as the employer. They know that if they can have a higher adoption rate into the high-deductible health care plans from their employees, that there's a direct savings to the organization, which can be used to offset additional expenses, salaries or additional benefits that they might want to offer. Unfortunately, when we talk to most employers who have rolled out a high-deductible health care plan in conjunction with some of their other plans, they see a very low adoption rate anywhere from 10% to 15%.

I was speaking to an employer the other day and they said they had a 36% adoption rate into their high-deductible health care plan. But when they did a study on their employees, they actually found that 99% of their employees should be in the high-deductible health care plan and would potentially be better off with that option. So employers, once they understand the value of offering the high-deductible health care plan, both a cost savings to them, but also for a value add to their employees.

Kevin Murphy: Is it true or false in that really HSAs and high-deductible health plans are really only for large employers?

Jamie Greenleaf: Absolutely not. HSAs, or high-deductible health care plans are for any size employer group. We're actually seeing the small- to mid-size moving from the HRA [Health Reimbursement Arrangement] because the cost is becoming prohibitive into a high-deductible health care plan on offering the HSA.

There are benefits to an employer offering an HSA in that their premiums should go down, which ultimately is going to impact their PNL. But the other thing is the employer can make a contribution into the HSA account on behalf of their employee and there's a benefit to the employer making a contribution into the HSA. So, when they contribute into a 401(k) plan in the form of a match or a company contribution, they still pay FICA [Federal Insurance Contributions Act] taxes on that. When they make a contribution into the HSA, the employer does not pay FICA taxes. So, if an employer and employee make a contribution into an HSA, there's a 15.3% savings just from FICA taxes. So I would say that all employers, regardless of their size, should take the time to understand the financial impact of offering a high-deductible health care plan, but more importantly, they need to, once they understand it, be able to communicate it properly to their employees, so that they take advantage of it.

Kevin Murphy: Yeah, I think it's all, it's all very connected, right? I think as we talked about the employee behavior and changing their behavior and you know, really education being the primary component who are making that work, then of course the employer. But it really takes both working together in a coordinated effort to really make it successful

Jamie Greenleaf: I think that's the, the beauty of open enrollment. It's an opportunity for the employer to give meaningful and relevant information at the proper time, which is when they're enrolling into the health care plan. So, if you engage the right team to communicate the benefits of the high-deductible health care plan, again, you as an employer may see a significant impact to your bottom line. And you as an employee may be better off in the high-deductible health care plan.

Jamie Greenleaf: One of the things that we've done at HSAgateway is we've provided modeling tools that allow employees to determine—based upon the programs that are available to them or the options that are available to them—what the financial impact is for choosing the health care plan that's being offered by their employer, between the different offerings. And it shows not only the impact today, but it also models the impact out short-term, intermediate and into retirement. And they can plug in things like, "Well, what if my child falls out of the tree and breaks their leg?" Or, "what if next year I have a heart attack? How does that impact me?" So, giving them the tools to kind of model it out is the first step that we've seen to change behavior. With just the tool alone, we get an uptick in adoption, but we really find the one-on-one, the coaching, the ability for us to take them through the tool and then talk to them about the financial decision—because again, it is emotional.

On top of that, unfortunately, what we've found is that if we can get them to change behavior and view the high-deductible health care plan as a benefit, unfortunately about 64% of the population then don't open the HSA. So now they've put their money into or they've decided to move to a high-deductible health care plan and instead of saving that premium, they're spending it. And ultimately if they do have the health care expense come up, they have no savings set aside. So, by making sure that we can follow that employee through the decision of moving to a high-deductible health care plan and then making sure that they open the HSA and actually save those premiums, we're setting them up for success. Once they're in that high-deductible health care plan, they've made the commitment to put those premiums aside, then we want to give them the tools, the ability for them to understand, "How do we become a better consumer?"

If you think about it, we Google everything in life. If we want a new car, we go out and see where can we buy that car and ultimately what is the price? We have a tool inside of our HSA that allows the employee to do the same thing. I have to get an MRI. Where can I get that MRI and what is the price of that MRI? Are they in-network, out-of-network? So, we've made them better consumers. And last but not least, the big innovation today is that you can invest your HSA.

Kevin Murphy: We certainly appreciate your time today, Jamie. And, just to recap, the "S" is for savings, right? It's not a "use it or lose it" and the accounts are portable, meaning you own it. Any other sort of things on the basic front that you would like the audience to hear?

Jamie Greenleaf: Yeah, I would tell both employers and employees don't think of high-deductible health care plans as a negative. Actually, think of them as a positive. You're potentially putting money back into your pocket and once you understand that, you truly appreciate them as a benefit and that's really what they are. So, I think the more that we can get people to understand the value of them, the better off we'll be as consumers moving forward with health care. So, I would tell you to view them a little differently than perhaps you might have in the past.

Kevin Murphy: That's great. Well, Jamie Greenleaf, thank you for joining us.

Host/Richard Banks: *And thank you for joining us with this episode of Franklin Templeton Talking Markets. We hope you enjoyed the conversation. If you'd like to hear more, visit our archive of previous episodes and subscribe on iTunes, Google Play, or just about any other major podcast provider. So, until next time when we uncover more insights from our on the ground investment professionals, goodbye!*

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