

# **Comments on “Employee Cost-Sharing and the Welfare Effects of Flexible Spending Accounts”**

Louise Sheiner  
Federal Reserve Board of Governors

# Overview

- First empirical paper to examine the effects of tax subsidies to out-of-pocket health expenditures.
- Theory: exclusion of employer-paid health insurance encourages the overconsumption of health insurance by increasing the share of health expenditures that are insured.
- Providing a tax subsidy to out-of-pocket payments has two effects: (1) it lowers the effective out-of-pocket payment holding the nominal coinsurance rate constant but (2) it provides an incentive to choose insurance policies with higher cost-sharing
- This paper attempts to measure which of these effects dominates.

# Empirical Framework

- Compares nominal coinsurance rate of firms with and without FSAs.
- Recognizes that firms with good benefits might choose to offer FSAs and chose to offer insurance with low coinsurance. To solve this problem, instruments for the decision to offer FSAs.
- Finds large effects of FSAs on coinsurance rate. After taking into account effects of tax subsidy, find FSAs have no effect on effective after-tax coinsurance, so no effect on health spending.

- Important paper. Shows how tax policy affects the form of the insurance contract.
- Now quibbles:
- Not clear why instruments work. Old firms more likely to offer FSAs? Why? Perhaps also less likely to offer HMO or PPO, and therefore have higher copay?
- Why restrict sample to firms that offer at least one conventional insurance product?
- Why control for BC/BS as if exogenous? This is a choice that firms make when offering plans.
- Theory is about share of health spending that is insured. This share depends on:
  - Deductible
  - Coinsurance rate or copayment
  - Out of pocket maximum
  - Types of services covered
- This paper focuses only on one of these. Authors should examine other margins as well (and looks like they may go the other way)

- Is the insurance plan the best unit of analysis, or the coinsurance actually chosen by employees?
  - One mechanism through which FSAs could raise coinsurance is by inducing employees to choose a plan with higher cost sharing, rather than changing the nature of the plan offers.
- It seems clear that firms with high out-of-pocket spending would be more likely to offer FSAs. Can we take these results as evidence that firms actually raised out-of-pocket spending when FSAs were adopted? Trends are actually strongly the other way:

1977	1987	1996	2002
68%	56%	44%	41%

It would be interesting to compare whether these trends were different for firms with and without FSAs over time.

# Tax Cost of FSAs

- Finally, evidence suggests that FSA are neutral with respect to after-tax marginal price of health services. This suggests that, as currently structured, they might not be worth the tax cost.
  - Authors should estimate real tax cost of FSAs (if they lower premiums, then the tax costs will be less than the tax expenditure calculated by JCT).
  - Would be nice to take into account likely effects of use-it-or-lose it provisions. Would straight tax subsidy be more or less effective at reducing marginal cost of health insurance?