Business

Curb Insurance Costs With A Health Savings Account

by Judy Villella

If you're the owner of a small business, you know what it feels like to get hit with big increases in health insurance premiums. As one of the owners of a remodeling company, I am interested in any insurance option that promises to curb this ever-growing expense.

When our current insurance policy expires, we plan to switch to a health savings account (HSA) because it promises to reduce what we're spending on medical care. It also offers some attractive tax advantages.


Form 5305-C

Health Savings Custodial Account

What Is an HSA?

Health savings accounts were part of the Medicare bill that was signed into law in late 2003 and took effect on January 1, 2004. HSAs combine a high-deductible health insurance policy with a savings account that is used to pay medical expenses. Certain rules apply — for example, participants cannot also be covered by another health insurance policy while they have an HSA. And by law, the deductible on the policy must be at least $1,000 for an individual and $2,000 for a family.

Insurance policy. The high-deductible policy protects against a major illness or prolonged hospitalization. It's not designed to cover all medical expenses, which is why there is a savings component to the plan. Unreimbursed medical expenses, including the deductible, can be paid for out of the savings account. If the participant has enough medical expenses to reach the deductible, the health policy kicks in and begins paying for services.

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Cost Comparison: Traditional Plan vs. HSA

	Managed-care family plan	HSA family plan (anticipated outcome)	HSA family plan (break even)	HSA family plan (worst-case)
Yearly deductible	$0	$7,000	$7,000	$7,000
Yearly premium	$8,880	$5,268	$5,268	$5,268
HSA deposit (assume maximum allowable)	$0	$5,250	$5,250	$5,250
Assumed yearly cost for deductible and noncovered items	$300	$3,000*	$5,225**	$7,000***
Total outlay	$9,180	$10,518	$10,518	$12,268
Less HSA account balance at end of year	$0	$2,250	$25	$0
Less tax savings for HSA deposit (assume 25% tax rate x $5,250)	$0	$1,313	$1,313	$1,313
Net cost	$9,180	$6,955	$9,180	$10,955

* this amount is paid from the HSA and is the one big "if" in the calculation
** paid from HSA
*** $5,250 from HSA, $1,750 out-of-pocket

This table compares the cost of the author's current plan with the cost of an HSA. In the example, there is some risk to the participants because the HSA policy deductible is very high. However, the risk is offset by lower premiums, tax savings, and the possibility that the participants won't spend the entire deductible or deplete the savings portion of the account every year.

Savings account. Participants and their employers are allowed to contribute pre-tax dollars to the savings account. Since the premiums for high-deductible policies are lower than those for traditional policies, the idea is to take what you save on premiums and put it into the savings account. The participant can withdraw money from the account and spend it, tax-free, on qualified medical expenses. The list of qualified expenses contains many items that traditional health care plans will not pay for.

Contributions are not limited to what the employer and employee save on premiums — either one can put away more. Participants and their employers are allowed to contribute up to 100 percent of the annual deductible, within certain limits. For 2005, the maximum allowable contribution is $2,650 for someone with single coverage and $5,250 for someone with family coverage.

Tax Benefit

The money in the account is typically invested in mutual funds and allowed to grow, tax-free. Funds left over at the end of the year carry over to the following year. The participant owns this money and can take it with him if he leaves or changes jobs, much like an IRA or 401(k).

Excess funds. If the deductible is high enough and the participant is healthy enough not to need many medical services, a substantial balance could build up over time. Funds can be withdrawn for nonmedical expenses, but the participant has to pay income taxes on them plus a tax penalty. At age 65 or upon disability, however, funds can be spent on nonmedical expenses without a tax penalty; normal income taxes will still apply.

Because the participant owns what's in his HSA and can use the excess for future medical expenses or retirement, there is an incentive not to spend these funds unnecessarily — an incentive that does not exist when something is completely covered by insurance or when money goes into a flexible spending account that expires at the end of the year.

Advantages

HSAs give control over health care dollars to the consumer. Medical expenses not normally covered under most policies, like acupuncture and eyeglasses, may be paid for through the savings account. Participants may withdraw money at any time to cover medical expenses or health insurance premiums simply by writing a check from their savings-fund checkbook.

Availability. Because HSAs are relatively new, some insurance companies do not yet offer them or may offer them only in some states. Another disadvantage of HSAs is that medical questionnaires must be completed and many insurance companies do not want to cover people who are older or who have pre-existing medical conditions. This means some people will have a hard time getting the necessary high-deductible insurance policy, or will have to pay a lot for it.

Cost Comparison

Our company currently has a comprehensive managed-care plan that covers the owners under a family plan and one employee as a single. (Our other employee is covered by his spouse's policy.) With our current plan, there is no deductible for in-network services, but the premiums are high and getting higher every year.

If we switch to an HSA plan with high-deductible policies, the premiums will drop significantly. Right now our family plan costs $8,880 per year and the single plan for our employee costs $3,516 per year. If we're willing to switch to high-deductible plans, we could get family coverage for $5,268 per year and single coverage for $2,224.

Of course, the reduction in premiums is not pure savings, because the coverage we're looking at has a $7,000 deductible on the family plan and a $3,500 deductible on the single plan. We could opt for lower deductibles, but that would mean paying higher premiums. The table on page 57 shows what the one-year costs would be for our family coverage based on certain assumptions regarding how much we put into the savings account, how far we spend into the deductible, and what our marginal tax rate would be.

The HSA plan looks good for us as owners because we're already footing the entire bill for our coverage. If we can keep from using all of the money we contribute to the savings account, a balance will build up over time, which could come in handy in future years if we start spending all the way up to the deductible. If we're lucky enough not to have many medical bills, the balance will be a nest egg for our retirement.

The situation will be different for our employee. We're currently picking up 75 percent of the cost of his policy and will continue to do so when he has a high-deductible policy. However, someone has to fund his savings account and we're not sure we can do that in a significant way. The employee will be free to fund it, but past a certain point that will mean spending more for his own medical care. Ideally, there would be a way to avoid this, but the fact is we have to compete with companies that offer employees no medical coverage at all.

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Handyman's Choice: Generalization or Specialization?

by Leland Stone

Since many contractors won't even consider doing handyman work, offering this service means you're already setting yourself apart from the herd. But even though there's likely to be less competition for the smaller projects, you're still going to have to stand out to keep that phone ringing. To illustrate what I mean, let's start with lunch.

Here in Southern California, we've got a couple of burger chains — one is the same multinational brand that's in your neighborhood, and the other's a regional brand with only 40 or so stores. The big chain has a large menu and lots of choices, while the local guys sell just burgers, fries, and shakes. While these burger joints obviously aren't selling construction services, they do demonstrate the two business models from which you'll choose: generalization and specialization.

> "When you narrow the focus, everything — from bidding to tool maintenance — becomes simpler, making business more efficient and earning you more money."

Starting Out With Generalization

If you've got broad construction experience, a large assortment of tools, and a lot of patience, taking the general approach will allow you to field more leads — which makes sense when you're starting out and hungry for work. Some prospects like the convenience of "one-stop shopping," while others appreciate the security of having one contractor handle all phases of a project. Promoting yourself as an all-around handyman gives you a sales edge with both types of prospects.

The downside of offering a large menu of services is that it ramps up the logistical difficulties involved in your new business. Each trade requires its own tools and materials, all of which have to be acquired and transported to the job. Your rig has to be big enough to serve as a mobile warehouse, or you'll find yourself making multiple trips from your shop or supplier to the job; either way, your overhead increases. So does the cost of maintaining those tools and restocking your inventory. In addition, the variables added by each extra service you offer increase your chances of making a costly bidding error.

Play to Your Strengths

If you decide to take this "big menu" approach, you'll want to reduce the chances of making those errors to a minimum. Start by analyzing your strengths and creating a written list of marketable skills. At the top, write down the things you're good at and enjoy doing, followed by the things you can do but don't enjoy. It's all right to list marginal skills that you enjoy working at and are willing to improve, but leave off anything you can't enjoy on some level. You should be able to commit to doing everything on your list in a good and workmanlike manner.

You will use the resulting list to coordinate your shop, your rig, and your marketing and sales. For example, if your menu contains a variety of services like carpentry and wallcovering, what are the most common tasks you're likely to encounter in those trades? Do you have the tools and materials needed to perform daily what you've listed, or should you add to your inventory? Are your skills up to par, or do they need brushing up in some areas?

After completing the first list, you'll need a similar one analyzing your target client. Is this "ideal" client going to be commercial or residential? High-end or mid-range?

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Will you deal directly with the end user of your services, or will you be soliciting work from third parties — insurance adjusters, property managers, real estate agents, and so on? Bear in mind that third parties may require 30-day billing, so be prepared to float their invoices. Also, decide how far you'll travel to serve this ideal client, and what hours you'll be available (weekends or on-call repair service could be a big plus to your target market).

Moving Toward Specialization

Even though the second list isn't as complicated as the first, it gives some insight into why I favor specializing a handyman business. When you narrow the focus, everything — from bidding to tool maintenance — becomes simpler, making business more efficient and earning you more money. Eventually, you'll trim your workload anyway, picking the jobs you like best. You might as well start planning for that outcome.

At the same time that you, as a startup business, are grabbing all the handyman work that comes your way, you should be letting clients know that you "specialize" in the work you prefer. List that trade at the top of your cards, truck sign, and other advertising. The idea is to attract clients who need your preferred skill without discouraging others from calling for your secondary skills. By gradually moving toward specialization, you'll be able to establish yourself in a profitable niche market while weeding out the unwanted work from your schedule.

And what about those calls for work you don't like? You'll be farming those jobs out, to other contractors who do like that kind of work. No, not because you're such a nice guy, but because you've previously made deals with noncompeting contractors to swap unwanted leads.

***Leland Stone** operates a handyman business in La Mirada, Calif.*