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## Health Savings Accounts -- an option to consider

### IT'S YOUR BUSINESS

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**Q: My company recently began offering a Health Savings Account available to all the employees. Why are employers throughout New Jersey rolling out these plans? What are the pros and cons of a HSA?**

- The problem: healthcare costs.

If you think rising healthcare costs are only the insurance company's problem or your employer's problem, think again. Most employees pay 10 to 90 percent of their healthcare costs, when all costs are included. All it takes is a quick review of your pay stub over the last few years to see that the insurance companies are passing on increasing healthcare costs to employers and employees are passing on these costs to employees.

Healthcare costs have risen 8 to 10 percent each year over the last three years and are likely to grow two to three times the rate of inflation for the foreseeable future. Compounding the problem are New Jersey insurance laws.

Almost every state in the U.S. can deny individuals coverage through the underwriting process. New Jersey is one of only five states in the U.S. that provides for "guaranteed issue" — which guarantees health coverage, regardless of health status, age, claims history, or any other risk factor. Although this may be considered a blessing, it is an expensive blessing. Almost by definition, this increases the cost of insurance coverage for everyone in the state to account for those who use the benefits most.

- The solution: a Health Savings Account.

Just a quick background on a Health Savings Account and how it works. Established as part of the Medicare Prescription Drug, Improvement, and Modernization Act of 2003, the HSA is a hybrid between health insurance and a retirement plan. The HSA was established so savings used for qualified medical expenses for yourself, or anyone you claim as a spouse or dependent would be free from taxes.

Qualified medical expenses include: medical doctors, dental and optical care, chiropractic care, long-term care, and Medicare Part A or Part B and Medicare HMO insurance premiums. Unqualified medical expenses include: cosmetic surgery, health club dues, nonprescription drugs and medicines, and funeral expenses.

A contribution to a HSA is only permitted if the health insurance accompanying it has a deductible (your out of pocket expense) of at least \$1,100 for individual coverage or \$2,200 for family coverage. The current contribution limit per year is \$2,850 for individual coverage or \$5,650 for family coverage. Those 55 and older can contribute an additional \$800 in 2007. Contributions are all pre-tax, a tremendous benefit for those seeking tax breaks. If the savings are used for qualified medical expenses, the entire amount can be withdrawn free of taxes.

Yes — that is right, free of taxes. If the savings are used for other purposes, the withdrawal is taxed as income and accessed a 10 percent penalty (if under the age of 65). At age 65, when Medicare begins, withdrawals are only taxed as income at your then tax rate. All interest, gains and dividends in a HSA are sheltered from taxation — allowing all earnings to compound on a tax-advantaged basis. Unused balances can be rolled over from year to year.

Many employees view the HSA as a retirement plan — providing them a tax-advantaged way to save for retirement above and beyond their 401(k) and their Individual Retirement Account.

- A win for employees, employers and insurers.

Because the HSA is based on a high deductible insurance plan the employee takes on a higher level of responsibility and risk for medical expenses than a traditional insurance policy. Employees who run their family to the doctor's office every time someone has the sniffles — because the visit only costs them \$10, while the insurance company pays the remaining \$65 under a traditional plan — will think twice when they pay the full \$75 out of their own pocket under a HSA. That said, those out of pocket costs are all with pre-tax dollars that were contributed to the HSA. By utilizing a HSA employers can reduce their premium costs by as much as 50 percent, passing most or all of those savings directly to the employees.

Many employers, particularly in "guaranteed issue" states like New Jersey, are implementing a HSA based on these benefits.

- Action steps: Implement a Health Savings Account.

Implement a HSA for your company or ask your employer to implement one. With health care costs increasing faster than wage increases, employees are bearing more and more of the cost burden. A HSA provides a pre-tax means to contribute towards an account that will grow over time, with the option to use the money for medical expenses on a tax-free basis or for any purpose in retirement on a penalty free basis.

Implementing a HSA saves money for all those involved and forces employees to be more responsible with their own savings. While the healthcare problem is not going away anytime soon, the HSA provides one powerful tool to combat the problem. When it comes to important employee benefits, speak with a licensed financial professional before making irreversible decisions that may haunt you for years to come.

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