Health Insurance for the Self-Employed - Protecting Your Business's Greatest Asset

By Elena Fawkner

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"I've been considering quitting my full-time job and getting a part-time job that would pay the bills [so I can start a home business] ... The one biggie my full-time job provides me now is health insurance. If I was to get a part-time job, I'd probably have to pay for my own health insurance and I know that can be expensive."

Like Jason, who sent me the above email this week, many a dissatisfied employee would chuck in their full-time J.O.B. (just over broke) for their part-time home-based business in a heartbeat if not for one thing. Employer-provided health benefits. It's a biggie, no doubt about it.

Undeniably, employer-paid or -subsidized health benefits are one of the few real perks of working for someone else. In fact, surveys have shown that, for employees (especially those with families), paid benefits are hands down the most important element of their compensation packages.

And there's no shortage of people already running their own home businesses with no health or disability coverage at all. Scary. After all, if you're dependent upon your home business as your sole source of income and you lose your health, you lose your livelihood as well.

Bottom line? If you run a home-based business you can't afford not to have health coverage of one form or another. Here's how to make it happen, whatever your circumstances.

BASIC OPTIONS FOR THE EMPLOYER OF ONE (YOU)

You have three basic options when it comes to health and disability insurance.

= Spouse Coverage

If your spouse has health coverage from his or her employer, as a general rule, use that. It probably provides better and less expensive coverage than you could get on your own.

= Group Health Insurance

The main advantage of group health insurance plans is that they can't turn you away because of health problems. The good news for the solo entrepreneur is that an increasing number of companies are offering group health plans for "groups" of one. This varies by state though so you'll need to do your homework to find one.

= Individual Health Insurance

These plans are fine if you don't have any pre-existing medical conditions. (If you do, try your best to find a group plan that will cover a group of one.) They're subject to medical underwriting so your state of health will be a factor the insurance company takes into account in determining whether to accept your application.

Of course, the mere fact that you're able to get into a good plan is one thing. Doing so affordably is quite another.

REDUCING THE HIGH COST OF HEALTH INSURANCE

There are several ways of minimizing the cost of health insurance. Your tolerance for risk will determine which, if any, you are comfortable with.

= Reduce the Level of Coverage

Do you really need to have every doctor's visit and prescription covered? If you only go to the doctor once a year for an annual examination, have no health conditions, don't need regular expensive prescription medications and are generally healthy, consider cutting out coverage for office visits and prescriptions.

= Higher Deductible

Similarly, if you're reasonably healthy, don't visit the doctor very often and don't need to use expensive medications, consider switching to a higher deductible to save on premium costs. By increasing your deductible from $100 to $2,000, you can cut your premium payment in half.

= Annual Premium Payments

If you can afford to do so, pay your premiums annually rather than monthly or quarterly to avoid service fees and to take advantage of prepayment discounts where available.

= Join Associations

Just because you're going it alone in your business doesn't mean you can't take advantage of the group buying power that being a member of an association offers. Check out your local chamber of commerce, various trade and professional groups and small and home business associations for member benefits. Many offer access to discounted health insurance.

Here are a few small/home business association links to get you started (you'll need to cut and paste some of these links if they wrap to the next line):

National Association for the Self-Employed
http://www.nase.org/nase_benefits/health_benefits.asp
American Association of Home-Based Businesses
http://www.aahbb.org/benefits.htm
Home Office Association of America
http://www.hoaa.com/allbenefitsnew.htm
National Business Association
http://www.nationalbusiness.org/NBAWEB/Directory/Internal_Pages/Member_Benefits/Health.htm

Don't forget to check out local associations in your area or associations relevant to your particular profession.

= Shop Online

Being able to offer insurance products online means insurance companies save on broker and agent fees. Often, this translates into premium savings for policies purchased over the Internet. So, when your fingers do the walking, make sure they do so on a keyboard and not the Yellow Pages.

= Medical Savings Accounts

Under the Health Insurance Portability and Accountability Act (HIPAA), if you're self-employed you may be eligible to use a medical savings account, or MSA.

MSAs work in conjunction with higher deductible health insurance policies to reduce premiums and allow you to use pre-tax dollars to pay for your medical expenses up to the limit of the deductible on your insurance policy.

Basically, you reduce your premium by replacing a low-deductible policy with high-deductible policy and use the premium saving to make fully tax-deductible contributions to your MSA. You can contribute up to 65% of the deductible each year into your MSA (75% for families). The money goes into a tax-deferred account or trust and you pay your medical expenses (until you reach the deductible) by drawing from the account. Once you hit the deductible, of course, the insurance policy kicks in.

If you spend less than you contributed, the surplus stays in the account and earns interest. Not only that, the funds can be invested in high-return vehicles such as mutual funds and stocks.

As the balance can be carried forward, an MSA can be used to accumulate a pretty healthy nest egg for retirement. In fact, a Journal of Financial Planning analysis calculated that if you contribute $1,500 per year into an MSA for 25 years, assuming a 12% rate of return, you'll end up with almost $1.5 million. That's assuming you don't draw from it to pay for medical costs, of course.

There are some limitations though. First, the range of deductibles is limited to $1,500 - $2,250 for individuals and $3,000 - $4,500 for a family. Second, as we saw above, you can contribute only 65% of the deductible as an individual or 75% for a family.

So, if you're an individual and you choose a policy with a $2,000 deductible, you'll be able to contribute 1,300 pre-tax dollars into an MSA each year. In other words, Uncle Sam pays for part of your health insurance/retirement fund. How fitting.

The money in the MSA can be used to pay any medical expenses incurred before the deductible is reached, as well as other eligible costs such as contact lenses and dental work. If you use the money for anything else, you must not only pay tax on the amount withdrawn, but a 15% penalty on the top. (If you're over 65 when you make the withdrawal the penalty is not applied but you'll still have to pay the tax.)

(By the way, MSAs are also available to you if you work for a business with fewer than 50 employees.)

In short then, MSAs offer a very tax-effective and potentially lucrative way to self-fund part of your health care costs while dramatically reducing your premiums. If luck is on your side and you remain healthy, by the time you reach retirement age, your MSA could well fund your retirement.

Pretty neat.

= Self-Employed Health Insurance Deduction

Finally, the self-employed can write off 70% of their health insurance premiums in 2002. This increases to 100% in 2003. That's only so long as the total doesn't exceed the net profit from your Schedule C minus deductions for one half of the self-employment tax and Keogh, SEP and Simple contributions though.

Also, the deduction can only be claimed for months when you weren't eligible to participate in a subsidized health plan from another employer (including your spouse's employer).

Self-employed workers who qualify for both the self-employed health deduction and the itemized medical deduction can write off the other 30% this year on Schedule A. (Medical expenses are deductible on Schedule A only to the extent they exceed 7.5% of adjusted gross income.)

WHAT TO DO IF YOU'RE UNINSURABLE

The foregoing is all well and good if you're able to get health insurance in the first place. But what if you have a pre-existing condition that disqualifies you from an individual health plan and you can't get into a group plan? In other words, you can't get insurance at any price.

= HIPAA

Although beyond the scope of this article, the Health Insurance Portability and Accountability Act (HIPAA) may offer you some protections. For more information about how HIPAA may help you obtain health insurance even if you have a pre-existing condition, visit http://www.hcfa.gov/medicaid/hipaa/content/hipsteps.asp .

= Risk Pools

High-risk health insurance plans, also known as risk pools, are state-funded plans and are an important safety net for individuals who are denied health insurance because of a medical condition. They're available only in 29 states though.

To be eligible, you must be a resident of the state from which you seek coverage (unless there's reciprocity between that state and the state you reside in) and you must be able to prove at least one of the following:

1. that you've been rejected for similar health insurance coverage by at least one insurer; or

2. you're presently insured with a higher premium; or

3. you're presently insured with a rider or rated policy.

You will not be eligible for participation in a risk pool if:

1. you're not a resident of the state from which you seek coverage (again subject to reciprocity between states); or

2. you're eligible for Medicare or Medicaid; or

3. you've terminated previous coverage in the plan unless at least 132 months have since elapsed; or

4. you're an inmate of a public institution.

For more information on risk pools in your state, contact your state health insurance department, the national association "Communicating for Agriculture and the Self-Employed" (1-800-432-3276) or visit http://www.selfemployedcountry.org .

Coverage via the safety-net protections of the HIPAA may end up being "risk-pool" coverage.

= Healthcare Savings Programs

Healthcare savings programs are patient advocacy programs that minimize out-of-pocket healthcare expenses.

They're not insurance policies but rather programs that allow you to access networks of healthcare providers for the same negotiated rates that large insurance companies enjoy. Savings range from 20% to 50%.

Not ideal but better than nothing. Also, since they're not insurance policies, all pre-existing conditions are accepted.

A modest monthly fee is usually required to participate. See, for example, Care Entree at http://www.careentree.com for $20 per month.

Although health insurance may seem like a luxury you just can't afford if your finances are already stretched to breaking point thanks to your home-based business, you never know what's around the corner. Quite simply, you and your business can't afford not to have health (and disability) insurance.

You are your business's greatest asset. Protect it.

Elena Fawkner is editor of A Home-Based Business Online ... practical business ideas, opportunities and solutions for the work-from-home entrepreneur.
http://www.ahbbo.com
Also, visit Elena's newest site, Web Work From Home
http://www.web-work-from-home.com