Healthcare Insurance Options for the Self-Employed

One of the most challenging tasks for any self-employed individual is securing adequate and affordable health insurance. Whether the coverage is only for the owner and his or her family, or for a small group of employees, the myriad of options can be complex and quite different from a cost perspective.

For those self-employed entrepreneurs who have a working spouse, coverage through their spouse's employer's group plan may be one alternative. COBRA (Consolidated Omnibus Budget Reconciliation Act) coverage may be available for others who have recently left the corporate world. But what about the options for those who do not easily have ready access to a group plan?

Assuming insurability is not an issue, one increasingly popular choice is a high deductible individual or family health plan. The advantage of this coverage is the inverse relationship between premium dollars and the selected deductible level. In exchange for paying for smaller expenses directly out-of-pocket, the policy holder is rewarded with more palatable monthly outlays for premiums.

Pairing a high deductible health plan with a Health Savings Account (HSA) makes the high deductible route even more attractive since it offers a tax advantaged way to pay the deductible dollars. In order for a health plan to qualify to be used in tandem with an HSA, the deductible must be at least $1,050 for single coverage and $2,100 for family coverage. Additionally, total out-of-pocket amounts (including the deductible) cannot be greater than $5,250 and $10,500, respectively, for single and family coverage.

Funds are deposited into the HSA on either a pretax basis, or an above-the-line deduction is taken on one's 1040. The amount that can be deposited into an HSA in any given year is limited to the deductible on the related health insurance policy. Once in the account, the funds can be invested in many different vehicles, including stocks, bonds, mutual funds and cash type investments. Considering that any dollars in an HSA that are not used to pay qualifying medical expenses remain in the account for future years, there is potential for these accounts to earn rates of return unavailable to Flexible Spending Accounts or Health Reimbursement Arrangements (HRAs). There is no limit on the size to which these accounts may grow.

If the self-employed person has employees, and offers them a high deductible policy paired with an HSA, the employer has the option of funding dollars into the HSA, but is not required to do so. As employees become savvier, the offering of an HSA can help attract and retain employees. The downside of an HSA from the employer's perspective is that the accounts belong to the employees, and if an employee chooses to leave the company, he or she can take their HSA with them.

For the self-employed person who has employees but is not necessarily interested in helping the employees accumulate a portable pool of dollars, but is nonetheless interested in the lower premiums of a high deductible health plan and would like to lessen the sting of a high deductible for workers, a Health Reimbursement Arrangement (HRA) is an option to consider. Similar to an HSA, the HRA is used in combination with a high deductible health care plan. It represents a pool of dollars to help the covered person defray the out-of-pocket costs of the high deductible. Unlike the HSA, however, the HRA can be funded as expenses are incurred, and there is no limit on how much can be contributed in any given year. If no one in the health plan submits eligible claims in a given month, then the employer is not obligated to fund any monies into the HRA. This feature helps limit the outlays for healthcare expenses to those actually incurred.

Another difference is that the HRA is not portable. Should an employee decide to leave his employer, that employee has no claim on unused dollars in his or her HRA account. For example, if an employer commits to funding an HRA for an employee to the tune of $1,000 each year, and the employee works for eleven months and then resigns after submitting no expenses for reimbursement, then the employer is spared from any HRA outlays for that particular employee.

Another notable difference is that, unlike an HSA, employees are not able to contribute to their own HRA account. Additionally, a self-employed person without employees is not eligible to establish and HRA for their own benefit.

What about the opportunities to link these vehicles together to try to provide the biggest benefit to employees? HRAs and HSAs generally cannot be used in tandem due to the ways the rules are currently written, nor can an HSA be used with a Flexible Spending Arrangement (FSA). An HRA, however, can usually be paired with an FSA.

We see there are attractive lower cost options for the self-employed person who is able to secure health coverage, whether or not employees are in the picture. But what about those who are unable to secure a health insurance policy due to a condition that makes that person uninsurable?

Some states, although Arizona is not one of them, offer an insurance pool for individuals who are otherwise privately uninsurable. Although these premiums can be significantly more expensive than an individual policy, they do at least offer coverage that would otherwise be unavailable. Considering today's health care costs, premiums of more than $1,000 per month are still preferable to paying for health care out-of-pocket. Similar to other health care plans, many of these state health insurance pools offer options to those willing to accept higher deductibles in exchange for lower premiums. Depending upon the deductible and a person's age, some of these premiums are in the range of $300 to $500 per month, which may be acceptable for those who cannot secure coverage otherwise.

By doing your homework, internet searches, and querying your professional colleagues, you may find a few other options for self-employed individuals who are labeled as privately uninsurable. For example, in Arizona there is a state sponsored plan that covers self-employed individuals and 50 or fewer employees that uses community rating (meaning it does not consider the particular individual or individuals in any one application group and any specific conditions they might have), so self-employed individuals who are otherwise uninsurable may qualify for coverage under this plan. There are conditions that must be met to qualify, dealing with areas such as the percentage of employees covered, the length of time doing business in Arizona, and the length of time previously without insurance, but this plan is an example that there are options for some who are otherwise having a difficult time finding coverage.