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Cutting The Rising Cost Of Employee Health Benefits

It isn't getting any easier to provide health coverage for your workers. While premiums for employer-sponsored health insurance rose less in 2007 than in any other year since 1999, according to the annual Employer Health Benefits Survey by the Kaiser Family Foundation, the latest increase, at 6.1%, still outpaced a 3.7% rise in workers' wages and a 2.6% general inflation rate. And small businesses, increases often face much bigger premium hikes. Such significant increases in this important employee benefit can wreak serious havoc on your bottom line.

One response to runaway health premiums is simply not to offer coverage. According to the Kaiser survey, only 60% of companies that responded said they provide health insurance, down from 69% in 2000. Small businesses with three to nine workers fare the worst, with a 45% coverage rate. And more belt-tightening is likely. Twenty-one percent said they were "very likely" to require a bigger contribution from workers in 2008. Asking employees to pay more is one way to curb rising costs, but there are other options. Consider these:

Switch to a "consumer-driven" plan. Some health economists say that because people with health insurance are partly shielded from costs, they go to the doctor too often and ask for too many tests, ratcheting up expenses and premiums. Health savings accounts (HSAs) and other "consumer-driven health plans" (CDHPs) give account owners financial incentive to seek healthcare judiciously. With an HSA plan, an employer offers insurance with a high deductible (at least $1,100 for individuals, $2,200 for families) and a chance to save up to $2,850 or $5,650 (for individuals or families, respectively) in pre-tax dollars annually to pay for doctor visits and other medical care. Employees who save more than they spend can use the money in future years. A catch-up contribution of $800 applies to employees age 55 or over. Your cost for an HSA, even if you make optional contributions to employee accounts, is likely to be lower than for traditional coverage. A study by human resources consultant Aon Consulting found that companies implementing an effective CDHP save an average of 8% in the first year. Keep in mind, though, that HSAs tend to appeal most to employees at the higher end of the income scale, who can afford to contribute and benefit most from tax advantages. Also, HSAs may discourage preventive care—would you still get an annual physical if it cost you several hundred dollars out of pocket?—and that could lead to health problems and higher expenses down the road.

Become a health insurance expert. Whether you already provide health coverage or are considering adding this employee benefit, it's important to understand the products and how much they cost. Point-of-service plans and PPOs let workers choose their doctors, though they'll have to pay more if they go outside the plan's physician network. HMOs and EPOs (exclusive provider organizations) further limit patient choices but reduce out-of-pocket payments. According to a survey by consultant United Benefit

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Planning For Your Future

It's hard to believe that summer is quickly approaching This year we have continued to see uncertainty in the real estate market and in the overall economy. With these trends in mind, this newsletter includes articles to help increase your awareness about several tax issues and provides information about retirement and social security benefits. In addition, we focus on how growing costs for health care are of great concern to business owners.

With the current turmoil surrounding the economic wellness of our country this is an excellent time to assess your individual "financial wellness". You may want to review your own plan to ensure you have both your short and long-term goals in place to weather the ups and downs of the economy. Your review may include revising your overall financial plan, updating your investment plan or reallocating your portfolio so you can meet your long-term goals and objectives. If you have any questions about the strategies or information presented in this newsletter please feel free to call us.

Horace

Should You Delay Taking Social Security Benefits?

When should you start collecting your hard-earned Social Security? Conventional wisdom says the longer you delay, the better off you are. Yet maximizing your payment through waiting is just one way to get the most out of this key retirement income source.

In essence, the government pays you to wait for Social Security, and docks you for taking benefits early. You're allowed to begin collecting at age 62, but your monthly payment will be lower than your "full benefit," and it will stay that way (see "The Cost Of Starting Early"). To get more, you must wait until you reach the Social Security Administration's "full retirement age," which used to be 65—and still is, if you were born in 1937 or earlier—but is now inching upward, depending on your birth year. If you delay taking benefits beyond your specified retirement age, your payment will increase an extra 8% for each year you postpone benefits until age 70.

If you opt to start Social Security payments at 62, you'll lose up to 30% of the benefit you'd get by waiting until retirement age. Still, delaying payments may not always be possible or even desirable. You could need the money—if, say, you've been downsized at work, or your health has forced you to retire early. In such cases, starting Social Security at age 62 may be better than draining your savings while you wait several years.

If you have plenty of other income, starting benefits early could pay off if you invest the money. But there's no guarantee you'd come out ahead with this strategy. Your success depends not only on your return, but also on how long you live. Receiving several extra years of payments undeniably puts money in your pocket, and if you start benefits at age 70 rather than at 62, for example, you'll need to live a number of years before the higher monthly payments make up for the cash you gave up by waiting. On the other hand, investing your early benefits in anything but the most conservative assets could put some of your otherwise guaranteed retirement income at risk.

The lower your portfolio's returns, the better off you may be spending down your savings while you wait for benefits to kick in at age 70, suggests John Marotta of MoneyNews.com. If your savings only keep pace with inflation—and if you live past the age of 83.4—waiting for the age 70 payout will be a better deal. But if you earn 2.5% a year above inflation, the "break-even" age is 87.25 years, according to Marotta.

These days, of course, achieving those milestones isn't unusual. According to the American Society of Actuaries, a 65-year-old male now has a 50% chance of surviving until age 85, while the average 65-year-old woman has 50-50 odds of being alive at 88. For a couple in which both spouses are 65, there's a 50% chance one will make it to age 92.

Ultimately, your decision about when to begin Social Security benefits may hinge on how that income affects your financial plan. If you're nearing 62 and would like to discuss your options, please give us a call. ●

The Cost of Starting Early

Year of birth	Age When You Can Begin Full Benefit	Percent Of Full Benefit Lost By Retiring At 62
1937	65	20.00
1938	65 and 2 months	20.83
1939	65 and 4 months	21.67
1940	65 and 6 months	22.50
1941	65 and 8 months	23.33
1942	65 and 10 months	24.17
1943 - 1954	66	25.00
1955	66 and 2 months	25.84
1956	66 and 4 months	26.66
1957	66 and 6 months	27.50
1958	66 and 8 months	28.33
1959	66 and 10 months	29.17
1960 & later	67	30.00

Source: Social Security Administration

Be Very Careful, But You Can Make Penalty-Free Withdrawals

IRAs, obviously, are for retirement. And except in very special circumstances—say, if you've come into a major inheritance—the money in your retirement account ought to be off limits for any other purpose. But if your financial plan shows you really won't need your IRA for retirement, there's another way you could use it, even if you have not yet passed the age 59½ threshold to make penalty-free withdrawals. You could pull out cash to pay for your children's education.

The basic rule is pretty simple. Though you'd ordinarily incur a 10% early withdrawal penalty for taking a distribution from your IRA before age 59½, that doesn't apply if the money goes to pay qualified education expenses for you, your spouse, or any child or grandchild of you or your spouse. And for these purposes, "child" is defined rather broadly. A stepchild, a legally adopted son or daughter, or even a foster child (subject to some conditions) can qualify.

Almost any post-secondary educational expenses count for this preferential treatment. The money for tuition, fees, and books can come out of your IRA as long as it goes to an accredited college, junior college, or graduate or professional school. The school can be public or private, nonprofit or for profit. If the student is attending at least half time, room and board counts, too.

Though there's no preordained ceiling on the educational costs an IRA withdrawal can cover, you can't take out more than the total qualified expenses incurred during a particular tax year. You'll also have to subtract the amount of any other tax-advantaged distributions or aid applied to school costs. This may include tax-free Coverdell distributions, the non-taxable portion of scholarships or fellowships, Pell grants, or tax-free assistance from your employer, among other things. But

A Plot Twist In The 0% Capital Gains Rule

One of the biggest tax blockbusters ever is scheduled to debut in 2008: the 0% capital gains rate. Despite advance reviews suggesting it will only benefit individuals in the lowest tax brackets, this marquee tax break could play well with affluent families, too. But a last-second twist in the plot complicates matters for families with older children.

This intriguing tax saga began in 2003. The Jobs and Growth Tax Relief Reconciliation Act (JGTRRA) lowered the maximum tax rate on long-term capital gains from 20% to 15% for taxpayers in most brackets. But for those in the 10% and 15% brackets, the tax rate was pushed even lower, to 5%.

And that's only part of the story. Under JGTRRA, the 5% rate drops to 0% for qualified filers in 2008, and the Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA) extended the 0% rate through 2010. Thus, taxpayers in the lower brackets can benefit from this unprecedented tax break in 2008, 2009, and 2010.

What does it have to do with you? Based on the inflation-indexed figures just released for 2008, the cutoff for the 15% tax bracket is only $65,100 for joint-filers, and $32,550 for single taxpayers. Short of taking a year-long, unpaid vacation, you're probably unlikely to squeeze under the bar. You'll probably be stuck with the 15% maximum capital gains rate.

But that doesn't stop your family members from benefitting from the 0% rate. For instance, you could transfer stock or other appreciated assets to a child or grandchild fresh out of school. Then, the child can sell the shares in 2009, or 2010, when the zero percent tax rate applies. If you were thinking of giving your son or daughter a gift, for a house down payment or to pay off college loans, this approach has the added benefit of cutting capital gain taxes.

What assets should you transfer? Highly appreciated ones. A block of stock you've been holding for years and that is now worth several times what you paid, for instance, would be a good gift to a child. If you were reluctant to pay a 15% tax on your gain, this would be a good way to get out from under that tax burden.

The current market value of the assets you transfer will be considered a taxable gift. But an annual exclusion lets you give $12,000 to any individual every year without paying any gift tax. This exclusion is doubled to $24,000 if your spouse consents to making a gift. So if you're married and have, say, two low-bracket children, you could give each child securities worth $24,000, for a total of $48,000, all completely gift tax-free. And you could repeat the strategy in 2008, 2009 and 2010. (Larger annual gifts would count against your lifetime $1 million gift tax exclusion.)

There is one complication. The Small Business and Work Opportunity Tax Act of 2007 expanded the reach of the "kiddie tax." Kiddie tax rules say that if a child receives unearned income (usually in the form of capital gains or dividends) that exceeds an annual threshold—$1,800 for 2008—the excess amount is taxable at the top tax rate of the child's parents. Prior to 2007 law, the kiddie tax applied only to children under age 18. Beginning in 2008, though, it affects any child under age 19, as well as full-time students up to age 24, if they don't have earned income that accounts for at least half of their support.

So if you have a dependent child in college or high school in 2008, you should be aware that gifting appreciated assets for them to sell could backfire. Your child's unearned income in excess of $1,800 could be taxed at your higher rate and undermine the gifting strategy. The amount of your gift, your child's earned income, and other numbers need to be considered and analyzed beforehand.

If you have a sizable amount of securities with significant unrealized gains, you may want to consider transferring them to a Charitable Remainder Trust to avoid capital gains, receive a charitable contribution deduction and lifetime income, and to benefit one or more charities.

Also keep in mind that it almost never makes sense to sell securities based solely on potential tax savings. Remember, this tax break is scheduled to last through the 2010 tax year. But if everything falls into place, this new tax rule could help your family enjoy the best of all possible tax rates. ●

From An IRA For Education Expenses

the amount you can withdraw without penalty won't be reduced by payments from other sources, including your income, loans, gifts, or withdrawals from 529 college savings accounts.

The only real downside to using IRA money—again, assuming you won't need it for retirement—is that withdrawals for education from a traditional IRA will be taxed as income. If the withdrawal comes from a Roth IRA funded with after-tax dollars, only the portion deemed to come from account earnings will be taxed.

Moreover, any tax you pay on an IRA withdrawal poses another problem. Your penalty-free distribution is capped by the amount of qualified educational expenses less any adjustments for tax-free awards. You can't withdraw enough to generate that total amount after taxes; you can take only the amount itself. So, for example, if the expenses amount to $50,000 and you pay total federal and state taxes of 40%, that extra $20,000 will have to come from outside the IRA. If you take the entire $70,000 from your IRA, the 10% penalty applies to the $20,000, increasing your tax bill by $2,000.

Just be sure you don't need the money to fund your retirement and have that all figured out first in a detailed financial plan. ●

Treating Your Retirement As A Liability

You already pay your bills on time. So why not add one more really important obligation to your monthly budget. If you begin treating your retirement needs as a future liability that you must fund now, you'll likely put away more money than if you pretend retirement saving is optional.

It's easy to fund your retirement account last. You know you should save, but there are competing priorities. The kids want to go to college, and you would like a new boat. And often, retirement saving loses out. But if you treat your retirement saving as another bill you have to pay, it will stay at the front of your mind. You won't miss payments, because—just as when you're paying the mortgage or the electric bill—getting behind has consequences.

While this solution to retirement planning sounds pretty simple, it comes from the sophisticated world of institutional investing. Pension fund managers, for example, have to treat future obligations—payments to pensioneers—as liabilities, and that forces them to deal now with something that may be years or decades off. Using actuarial tables, they calculate the cost of future obligations to determine what return they require on their investments and whether the pension fund is adequate.

While you may not use actuarial tables, you can manage your retirement account like a pension fund. The first step is to determine the savings you need to support the lifestyle you want during retirement, keeping in mind that you probably want to fund retirement through age 90 or 95. Next, determine how many years you have to reach your savings goal. If you are 45 and plan to retire at 62, for example, you have 17 years to fund your retirement account. Finally, determine how much you must save each year and make projections about returns on your investments.

If you're already funding your retirement goal by contributing to a 401(k) or other plan at work, treating that money along with all of your other retirement savings as a liability, may provide you with a more realistic picture about how much you need to put away and the retirement you should expect. It may make you save more.

A simple way to establish a monthly liability for your retirement obligation is to divide your goal into equal installments. So if you have 17 years to save $500,000, you can divide that obligation into 204 monthly payments of just over $2,450 apiece. Given the expected growth of your investments, you're likely to "over-fund" your retirement obligation.

If you would like us to calculate your payments more precisely, we will estimate the impact of inflation, investment returns, and taxes. That may give you a realistic number for your monthly liability. By thinking of your retirement account as a liability, you're paying yourself along with your other debts. It's a great way of funding retirement. Of course, making calculations about how much you need to save today to fund a debt in the future, while also making judgments about inflation and taxes and selecting the right investments, requires the help of a professional. We're here to assist you with any aspect of this and help you create a disciplined system for planning your retirement. ●

Employee Health Benefits

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Advisors, the average covered employee now pays $3,110 per year for insurance, with employers chipping in $3,771. Choosing an HMO or CDHP might save you 10% compared with the average plan, while a point-of-service plan costs 11% more than the average plan.

Cover less, but provide what's most important to your employees. Health coverage for your employees is a crucial benefit for recruiting and keeping workers. If economic realities call for cutting back, though, consider explaining the trade-offs and soliciting opinions about different coverage options. A relatively young, healthy work force, for example, might embrace an HSA or care more about dental insurance, say, than prescription drug coverage. Though you'll still have to make the final call and while your decision may be influenced by regulation, your employees may be more understanding if you've made them part of the process.

R***eview your health insurance costs and coverage every year.*** Even before you get a notice that your premiums are rising 10%, look around to compare costs and benefits. Often, switching to a new plan may cause minimal disruption to employees—local doctors tend to participate in several insurance programs—but could mean significant savings.

Help your employees get healthy. The impact of employee claims on your health insurance premiums may vary according to the kind of health plan you provide. If your plan is not "community rated" but based instead on the health and claims record of your employees, helping your staff stay healthier could lower premiums over the long run. However, only when a company grows to over 200 employees does the "experience rating" of the group's members begin to make a difference—and your company plan may not be experience-rated. Subsidizing a quit-smoking program or bringing in a nurse for health screenings or flu shots could, however, help reduce employee sick days.

According to a recent survey of employers by human resources consultant Mercer, health insurance costs are expected to increase by almost 9% in 2008. Yet because many companies are taking steps to control their premiums, they project just a 6.7% increase in their outlays. Your cost-saving measures might generate similar dividends.

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