Three Mistakes to Avoid this Open Enrollment Season

It's almost that season again! I'm not talking about the fall season, football season, or playoff baseball season. Rather, it is that time of year when you receive that dreaded e-mail that completely overwhelms: it's open enrollment season!

If you are like most, you tuck that e-mail away and stressfully wait until the last day of open enrollment to begrudgingly enroll into your company's employee benefits. On the last day, you open the email, click the link to enroll, and then suddenly get overwhelmed with the amount of options from which to choose.

Enter decision overload. If you click on too many options, your paycheck can potentially be reduced to an unrecognizable amount. But if you click on too few options, you could end up paying more later and missing out on valuable benefits. And if you are like many people, you decide to ignore the potential consequences while mindlessly clicking through in anticipation of pressing "submit" and being able to move on.

By selecting too many options, you can drastically decrease your income, but if you click on too few options during Open Enrollment, you could end up paying big bucks later and missing out on valuable benefits.

These decisions, like many financial decisions, tend to take a back seat to our everyday lives. They end up being made without enough time and education, and under stressful deadlines. My hope is that you take the time this year to educate yourself and make the right decisions.

The current approach many people take to open enrollment is unhealthy.

Therefore, my goal in this article is not only to make you aware of commonly made financial mistakes, but to also expose the common myths of open enrollment. My hope is that you see it as the financial decision it is and treat it as such by giving it the time, attention, and preparation that you would if you were investing in stocks, purchasing real estate, or choosing a financial advisor.

Disclosure: Your situation is unique, as is everyone's. Please seek advice from a licensed professional for specific recommendations.

Mistake #1

Not Optimizing the HSA Election

In most investment vehicles, we eventually pay taxes.

In a Roth IRA, we pay taxes on the contributions, and the money inside the Roth IRA grows tax deferred. We can then take out our money without paying additional taxes.

In a traditional 401k, we defer taxes on the income and growth and then pay it later when we take withdrawals. There's no way to get around paying taxes at some point … or is there?

Enter an HSA. An HSA not only allows us to deduct the contributions from our income, but that same money can be invested and grow tax deferred over time. Sounds like a 401k, but with an extra twist: as long as the money is used for qualified medical expenses, it can be taken out tax free.

An HSA not only allows us to deduct the contributions from our income, but that same money can be invested and grown tax deferred over time while giving us the ability to take out money tax free to pay for qualified medical expenses.

The contribution is tax deductible, the growth is tax deferred, and when you take it out for medical expenses it is *tax free*. That's a triple threat in the financial planning world, ***yet few people are taking advantage of this tax advantaged vehicle.***

For you to contribute to an HSA, your employer must first offer the program. Next, you must select a HDHP (High Deductible Health Plan), and finally, you must elect to contribute. An individual can contribute $3,450 per spouse for those covered under qualifying medical plans.

Warning: Sometimes a high deductible health plan is not the best option for a family, thus eliminating the possibility of an HSA. Make sure to review all your options to determine what is the most appropriate for your situation. If you have questions, consider speaking with a financial professional.

Mistake #2

Not Utilizing a Dependent Care FSA

If you don't have children yet, go ahead and skip to the next mistake. If you do have children or are thinking of having them in the near term, knowing what a Dependent Care FSA (Flexible Spending Account) is and what it provides can help save you even more money on taxes.

For starters, it is important that we do not get an FSA and Dependent Care FSA confused. An FSA provides similar benefits to an HSA and is available for those who choose a lower deductible health care plan. The biggest difference between an HSA and an FSA, is that you generally must use the money in an FSA within the plan year. But your employer may provide a "grace period" of up to 2 ½ extra months to use the money in your FSA, or it can allow you to carry over up to $500 per year to use in the following year

If you do elect a lower deductible health care plan, I do encourage you to consider option into an FSA for the amount that you think you will come out of pocket for medical expenses in that given year.

In addition to an HSA, you can opt into a Dependent Care FSA in the same year, and the tax benefits can be enormous. As long as you have what the IRS deems to be a qualified dependent, you can deduct up to $2,500 per spouse into a Dependent Care FSA.

If you have a qualified dependent, you can deduct up to $2,500 per spouse into a Dependent Care FSA.

With this Dependent Care FSA, you can pay for after school care, preschool, day care, and even summer camps (only day camps, not overnight). Although this is mostly used for children, be aware that an elderly or disabled person can qualify as a dependent person as well.

Mistake #3

Making Assumptions about Group Insurance Options

Manny people assume the group life and disability income insurance options through work are not only enough protection, but also cheaper than privately owned insurance. This is really two mistakes in one. In my opinion, the bigger of the two is assuming that your employee benefits provide all the insurance you need. Although this might be true for your individual situation, assuming that you need no extra coverage can be a costly mistake.

For example, a company may offer $50,000 of life insurance and 60% of your base salary in long term disability benefit for free. Free is great, don't get me wrong, but these benefits may leave a gap in coverage.

An example of a coverage gap would be that the $50,000 of life insurance covers you only when you an employee of the company. Since a death can be preceded by a lengthy disability due to illnesses, often, the employee-employer relationship my be long terminated prior to death, meaning that the life insurance may not be in force at the time of actual death.

In addition to group life insurance, group disability income insurance may also leave a gap in coverage. For instance, if a company can offers a 60% disability income insurance at no cost to the employee, some points to consider are…

- Will the benefit be a taxable benefit to me? If so, what percentage of my income is it replacing, and will that be enough?
- Does the benefit include any bonuses or commissions, or does it just cover my base salary?
- What definition of disability does my group coverage offer?

The second mistake is adding additional group coverage from your company's benefits without shopping outside for personal coverage first. Although it is easier to press the button for additional life and disability income insurance, it doesn't mean it is cheaper and it may also not be the best long-term option.

Before adding additional group coverage, consider shopping for personal coverage first.

Depending on the situation, these additional benefits can be vitally important for someone who has or has had health issues and may not be able to get a healthy rating in the private market. This "adverse selection" can drive the cost of these products up, meaning that if you are healthy and willing to go through underwriting, you might be able to secure lower cost coverage elsewhere.

Maybe more importantly than cost, **private insurance is portable and will be with you no matter what company you are working with**. Securing this private coverage while younger and healthier can potentially save you in the long term.

In Conclusion….

While going through your employee benefits this year, take a little more time learning about the coverage your employer offers and how the choices you elect might affect your overall financial wellbeing. Talk to your tax professional about what options will be most tax advantageous for you, ask yourself if the group insurance policies are enough or if it would make sense to look at private options, and if you have questions, schedule a phone call with me at the link below and we can work together on creating the best plan for you.

Click here to schedule your financial planning meeting!

Happy Benefits Season,

-Alan

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