



# MAKING HEALTH CARE WORK

## FOR VIRGINIA'S SMALL BUSINESSES

*Findings of the 2011 Virginia Small Business Health Insurance Survey*

January 2012

**Acknowledgements**

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## INTRODUCTION

As the new health care law goes into effect at the state level, small businesses are key stakeholders whose views should inform the implementation process. Small businesses are the engine of the Virginia economy, creating jobs and delivering essential services; implementing the health law to maximize benefits for small businesses will help ignite that engine and drive the economic recovery forward.

As real-life experts on the problems in the current health care and health insurance systems, small business owners have important perspectives on how to make health care work for businesses and the economy. This report focuses on the experiences and views of Virginia small business owners as documented in a survey conducted in 2011.

Compared to large employers, small employers and self-employed entrepreneurs are at a particular disadvantage in the small group and individual health insurance markets. Small businesses have limited means for purchasing insurance and also have limited bargaining power. As a result, small businesses frequently go without coverage for their employees (and owners, too) or receive less coverage in the plans they are able to afford, placing their health and financial security at risk.

The results presented in this report were gathered through a survey of 430 small business owners in 28 cities and towns across Virginia. Surveys were collected primarily through face-to-face and one-on-one interactions with business owners between February and December 2011.

## KEY FINDINGS

Key findings of the survey include that responding small business owners:

- Are struggling to keep up with the rising costs of health care, and many do not have or offer health coverage because they can't afford to;
- Support giving small businesses the opportunity to band together in a health benefits exchange to shop for coverage with other businesses in the state;
- Support strengthening the state's ability to review and modify or deny health insurance companies' proposed rate increases;
- Support implementing the 80 percent value for premiums (MLR) requirement as enacted in the Affordable Care Act;
- Support vesting Virginia's health benefits exchange with "active purchaser" bargaining powers to negotiate with insurers on benefits and costs;
- Lack information about opportunities like the new health premium tax credits designed to help small businesses afford health coverage.

## BACKGROUND

Small businesses are the engine of the U.S. economy. Small businesses create jobs and deliver essential goods and services to communities across America. In 2008, more than 5.8 million businesses in the U.S. (98 percent of all firms) had fewer than 100 workers. These businesses employed a total of 42.1 million people. In Virginia, 148,000 firms with fewer than 100 workers employed 1.1 million people. More than 86 percent of all firms in the state had fewer than 20 workers, and 75 percent had fewer than 10 workers.<sup>1</sup>

### Small Businesses Struggle to Find Quality Health Coverage They Can Afford

Despite the integral role small businesses play in the economy, recent research indicates that the health care system is not working for America's small businesses. Only 41 percent of businesses with fewer than 50 workers nationwide offered health coverage to their employees in 2009, compared to 96 percent of businesses with 50 or more employees. In Virginia, only 37 percent of businesses with fewer than 50 workers offered coverage, compared to 98 percent of businesses with 50 or more employees.<sup>2</sup> Compared to larger businesses, small businesses that do purchase insurance obtain lower quality coverage – often without dental benefits and with higher deductibles – despite the fact that their premiums have increased at a faster rate.<sup>3</sup>

Small businesses are seeing health insurance costs escalate rapidly in relation to payroll costs.<sup>4</sup> Rising costs are forcing small business owners across the country to make difficult choices about cutting back on benefits or dropping coverage entirely. This problem became particularly acute during the 2008 economic crisis and the subsequent slow recovery: *The Wall Street Journal* reported in 2009 that a growing percentage of small businesses were dropping health coverage in the face of accelerating costs and declining revenues due to the recession.<sup>5</sup>

Health care costs have long been a struggle for small businesses, but the portion of small businesses considering cutting benefits is growing. One 2009 study found that one in 10 small businesses was looking at dropping health coverage entirely.<sup>6</sup> Additional research conducted prior to the passage of health reform found that one third of small businesses were then faced with having to reduce coverage, whether dropping it entirely or cutting back in other ways.<sup>7</sup> Those small businesses able to retain coverage may find that the combination of higher out-of-pocket costs and more limited coverage affects the affordability and accessibility of health care.

### Small Businesses at a Disadvantage in Health Insurance Markets

Small businesses face a number of serious challenges in the small group health insurance market. Without bargaining power to negotiate with insurers, small business owners are vulnerable to steep year-to-year rate hikes. They pay more in administrative costs (often 20 to 25 percent of each premium dollar) than do larger groups (often around 10 percent).<sup>8</sup> And they face unpredictable rate increases because they can't spread risk effectively due to their small size.<sup>9</sup>

The version of competition that prevails in state small group health insurance markets places small businesses at a disadvantage. Rather than promote competition based on quality and affordability, the current market structure leads insurers to compete for “good risk” (young, healthy people) and avoid so-called “bad risk” (people they expect to cost more) in order to maximize profits. Depending on the market, carriers do this through a variety of mechanisms, ranging from preexisting condition waiting periods and rating practices based on expected health needs to the strategic design of benefit plans and rejection of applicants with health conditions.<sup>10</sup>

Furthermore, the high level of concentration in insurance markets leaves small businesses without meaningful choices or the leverage that comes

from having a credible threat of taking their business elsewhere. According to the American Medical Association, 94 percent of metropolitan insurance markets across the U.S. are “highly concentrated” based on the index used by federal regulators.<sup>11</sup> This type of market concentration leaves small businesses, especially those in rural areas, without real, affordable health care choices.

Unable to afford coverage as a group, many small business owners and employees are forced to turn to the individual health insurance market. States’ individual markets, however, are beset with even greater problems than the small group market. In many states insurers have greater latitude to raise rates in the individual market and spend a smaller portion of each premium dollar on health care.<sup>12</sup> Applicants also face rejection based on preexisting conditions and wind up with higher out-of-pocket costs than if they were covered through group insurance.<sup>13</sup>

### **Addressing the Health Care Challenges Small Businesses Face**

Small business owners have rated fixing health care as a top policy priority for many years. According to a 2008 survey by the Robert Wood Johnson Foundation, 42 percent of small business owners thought making health care more affordable should be the first or second priority for the next President and Congress. This put affordable health care ahead of all other issues, including energy independence (39 percent), tax breaks for small businesses (31 percent), and avoiding tax increases (24 percent).<sup>14</sup>

The challenges small businesses face rose to the forefront of the national dialogue over health reform in 2009-2010, with elected officials and a wide range of stakeholders agreeing that reform was necessary to promote the future prosperity of small businesses. The small business imperative for reforming the health insurance system was a key contributing factor to the passage of the Patient Protection and Affordable Care Act (hereinafter Affordable Care Act) in March 2010.

Now, states have the opportunity to make decisions about how to move forward with implementing health care changes, including the creation of a new competitive marketplace for health coverage called a health benefits exchange. However, critical questions remain to be answered:

- How are small business owners faring currently, and what are the biggest barriers they face to accessing quality health coverage?
- What steps should the State of Virginia take to maximize on opportunities to make health care work better for small businesses?
- As Virginia moves forward in the process of establishing a health benefits exchange for small businesses, what do small business owners think about some of the key decisions to be made about the structure and functions of an exchange?

The survey upon which this report is based posed these questions.

## **METHODOLOGY**

This report is based on a survey of 430 small businesses, including small employers with up to 100 employees and self-employed business owners, in 28 cities and towns across Virginia. Surveys were collected primarily through face-to-face interviews with business owners in their places of business. A small number of surveys

(three percent of the total) were collected by email.

Survey results reported here are rounded to the nearest percentage point. (In some cases, the combined tallies for a particular question may not sum to 100 percent due to rounding.)

## FINDINGS

### Respondent Information

Small business owners from the following cities and towns participated in this survey: Alexandria, Ashland, Bedford, Blacksburg, Charlottesville, Chesapeake, Chester, Chesterfield, Colonial Heights, Danville, Dumfries, Fairfax, Fredericksburg, Goochland, Hampton, Henrico, Hopewell, Lorton, Manassas, Newport News, Norfolk, Petersburg, Portsmouth, Richmond,

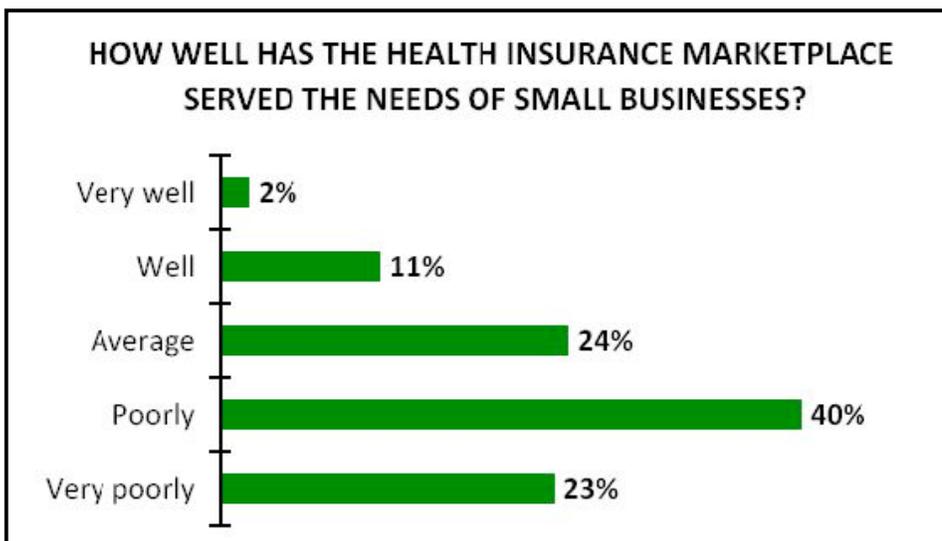
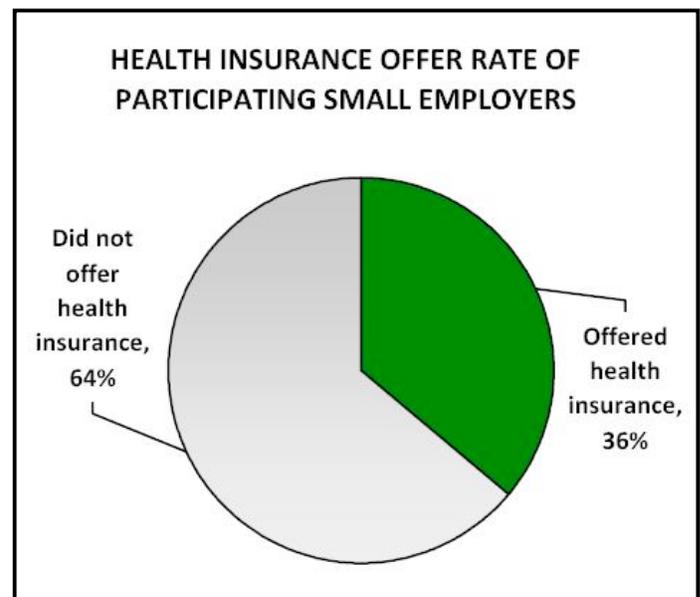
Virginia Beach, Waynesboro, Williamsburg and Woodbridge.

Seventy-four percent of responding business owners were small employers. Twenty-six percent were self-employed. Among the small employers, 58 percent had one to five employees, 21 percent had six to 10 employees, 14 percent had 11-25 employees and eight percent had more than 25 employees.

### Health Insurance Coverage and Offer Rates

Among responding small employers, 36 percent offered health insurance to all or some of their employees; 64 percent did not offer coverage at all.

Among self-employed respondents, 69 percent reported that they had health insurance coverage for themselves; 31 percent reported that they did not. Among those with dependents, 66 percent reported having coverage for all dependents and six percent for some dependents; 28 percent reported not having coverage for their dependents.



### General Views on Health Insurance in Virginia

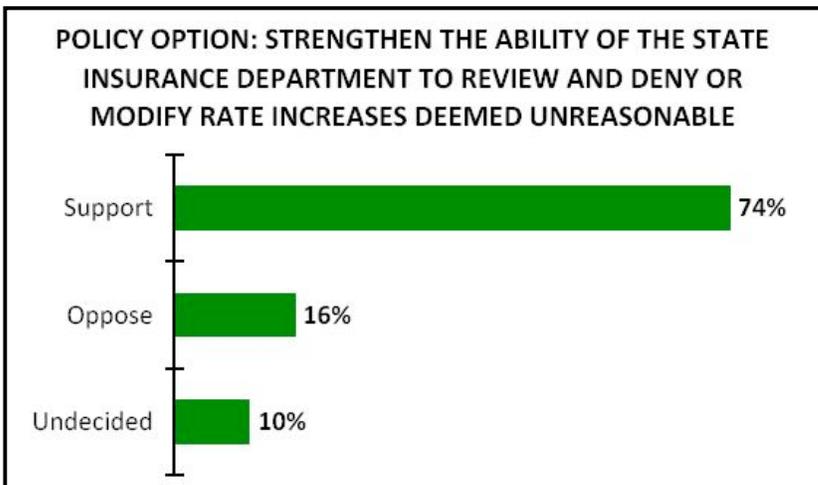
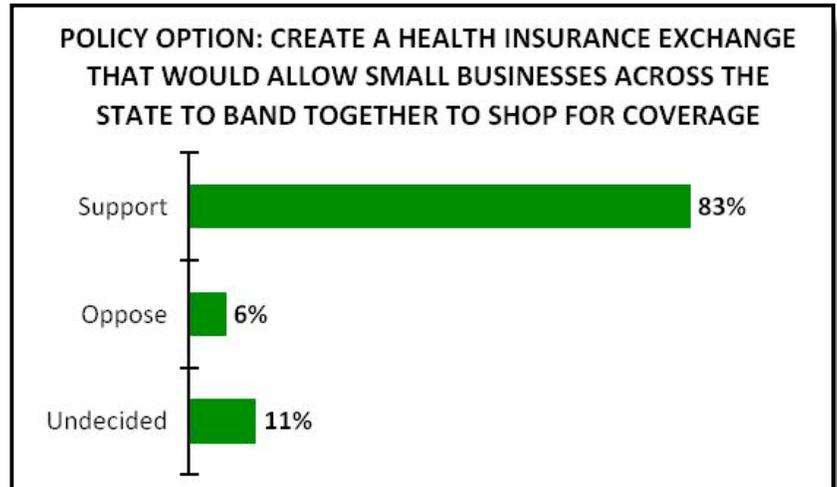
When asked how well the health insurance marketplace has served the needs of small businesses, 63 percent of responding business owners said “poorly” or “very poorly”; 13 percent of respondents said “well” or “very well”; 24 percent said “average.”

## State Options for Changes to Insurance System

The survey presented three separate policy options the state of Virginia could undertake in making changes to its health care system. It then asked respondents whether they support or oppose each option.

The first policy option tested was: “Create a health insurance exchange that would allow small businesses across the state to band together to shop for coverage.”

Eighty-three percent of respondents supported creating a health insurance exchange for Virginia’s small businesses. Six percent opposed this idea. Eleven percent were undecided.

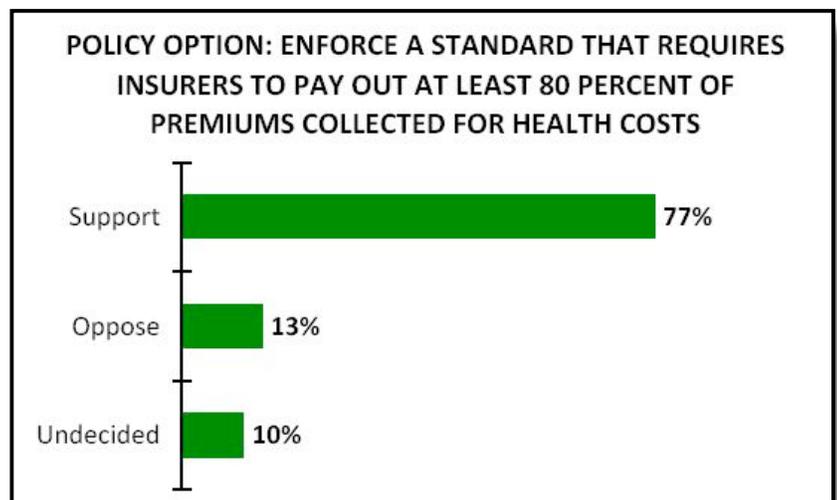


The second policy option tested was: “Strengthen the ability of the state insurance department to review rate increases and deny or modify increases that are deemed unreasonable.”

Seventy-four percent of respondents supported strengthening the insurance department’s authority to review and deny or modify rate increases. Sixteen percent opposed this policy option. Ten percent were undecided.

The third policy option tested was: “Enforce a standard that requires insurers to pay out at least 80 percent of premiums collected from small group and individual customers for health costs (as opposed to administration, compensation, advertising, and so on).”

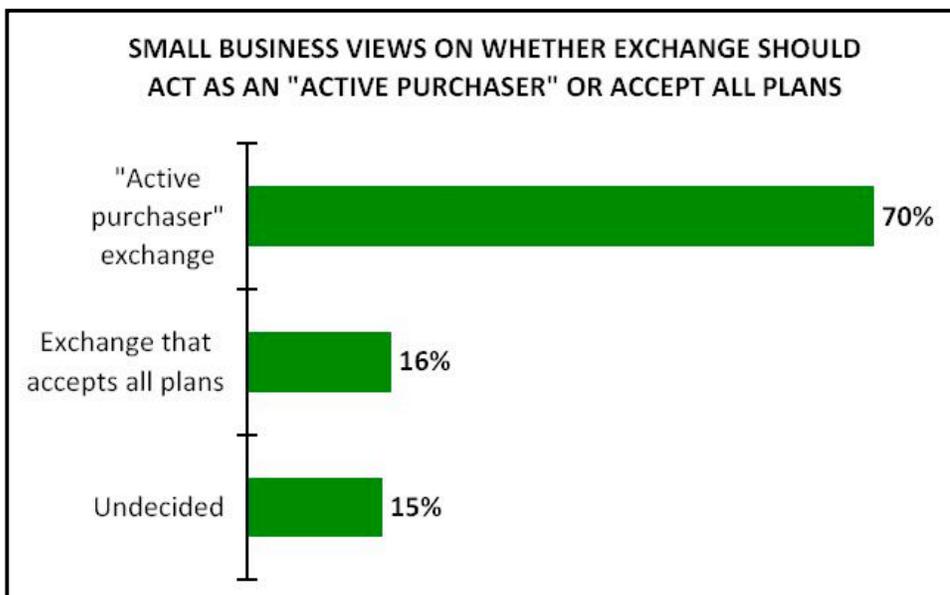
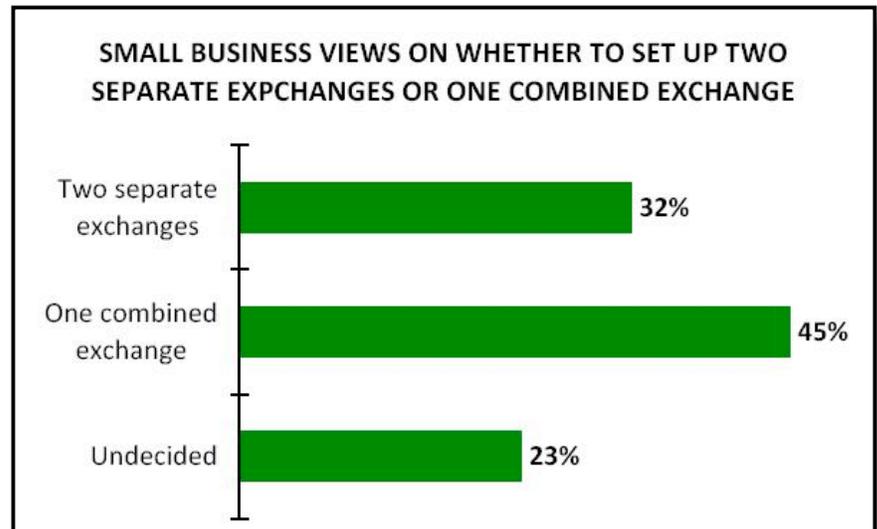
Seventy-seven percent of respondents supported a requirement that insurers meet this 80 percent threshold, while 13 percent opposed this policy option and 10 percent were undecided.



## Views on a State Health Insurance Exchange

The State of Virginia is in the process of evaluating options and making decisions about the design and structure of a health benefits exchange, a new competitive marketplace for health insurance. The survey asked a series of questions relating to key decisions about the structure and function of such an exchange.

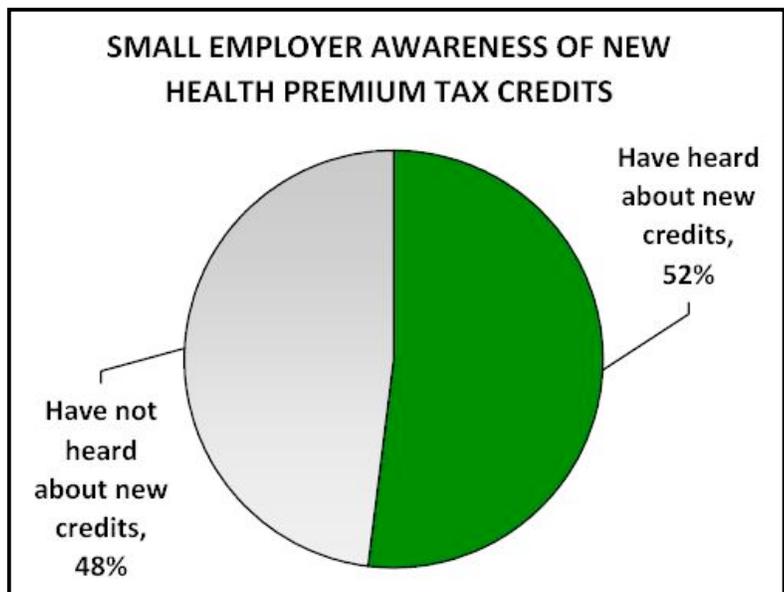
The survey queried respondents on whether they would support creation of two separate health benefits exchanges (one for small employers and one for people purchasing individual or family coverage) or one combined exchange. Forty-five percent of business owners who answered this question said they support the creation of one combined exchange. Thirty-two percent said they support the creation of two separate exchanges. Twenty-three percent were undecided.



The survey asked business owners if they support an “active purchaser” exchange (one that negotiates with insurers on benefits and costs) or an exchange that accepts all plans as designed by insurers. Seventy percent of business owners who answered this question said they support an active purchaser exchange, 16 percent said they support an exchange that accepts all plans, and 15 percent were undecided.

## Awareness of New Health Premium Tax Credits

When asked if they had heard about the new health premium tax credits that are available to many small employers who contribute toward employees' health coverage, 52 percent of responding small employers said they have heard about the credits, while 48 percent said they have not.



## CONCLUSION

Small businesses have found themselves at the center of the country's health insurance troubles for decades. Lacking bargaining power to negotiate with insurers, small business owners have been vulnerable to steep rate hikes come renewal time each year. Because of these rising costs, small businesses are routinely forced to reduce benefits by increasing deductibles and employees' share of premiums, or drop coverage altogether.

Small businesses pay more in administrative costs than do larger groups, and they are penalized because they can't spread risk effectively due to their small size. Small businesses also must contend with the great complexity and lack of transparency in the health insurance market, which make it difficult for busy business owners to make informed decisions and determine whether their health care dollars are being spent well.

Without concerted attention to address these issues at the policy level, small employers, their employees, and the self-employed will continue to be caught in a bind between paying unaffordable premiums and out-of-pocket costs, forgoing needed health care, and facing mounting medical debt.

The Virginia small business owners who participated in this survey have important perspectives on steps the state can take to ensure that the health insurance marketplace works better for small businesses. Business owners who participated in this survey:

- Are struggling to keep up with the rising costs of health care, and many do not have or offer health coverage because they can't afford to;
- Support giving small businesses the opportunity to band together in a health benefits exchange to shop for coverage with other businesses in the state;
- Support strengthening the state's ability to review and modify or deny health

insurance companies' proposed rate increases;

- Support implementing the 80 percent value for premiums (MLR) requirement as enacted in the Affordable Care Act;
- Support vesting Virginia's health benefits exchange with "active purchaser" bargaining powers to negotiate with insurers on benefits and costs;
- Lack, in many cases, information about opportunities like the new health premium tax credits designed to help small businesses afford health coverage.

The implementation of health reforms creates opportunities for the state of Virginia to address these issues and level the playing field for small businesses when it comes to health insurance. The Virginia Main Street Alliance's recommendations include:

- Create a single, unified Virginia health benefits exchange where small employers and self-employed business owners can band together to maximize risk pooling, bargaining power, and administrative efficiencies in shopping for and managing health insurance coverage;
- Give the exchange "active purchaser" powers so it can negotiate on behalf of small businesses to maximize value and control costs;
- Include a strong conflict of interest policy in the governance of the exchange to prevent financial conflicts of interest from undermining the potential of the exchange to reform the insurance marketplace and benefit small businesses;
- Develop and enforce new rate review standards to protect small businesses from unreasonable health insurance rate increases, including giving the state insurance department the authority to deny or modify unreasonable rate increases;
- Enforce the new minimum standards for insurance company medical loss ratios (MLRs), including requiring rebates from

insurers that fail to meet the new minimum standards;

- Conduct broad education in the small business community to ensure that all

small employers who are eligible for the new health premium tax credits are informed of the credits and can use them to continue or begin offering health coverage.

## ENDNOTES

- <sup>1</sup> U.S. Census Bureau, “Number of Firms, Number of Establishments, Employment, and Annual Payroll by Enterprise Employment Size for the United States and States, Totals: 2008,” 2008 County Business Patterns, [http://www2.census.gov/econ/susb/data/2008/us\\_state\\_totals\\_2008.xls](http://www2.census.gov/econ/susb/data/2008/us_state_totals_2008.xls).
- <sup>2</sup> Agency for Healthcare Research and Quality, Center for Financing, Access and Cost Trends, Medical Expenditure Panel Survey – Insurance Component, Table II.A.2(2009), Percent of private-sector establishments that offer health insurance by firm size and State: United States, 2009, [http://meps.ahrq.gov/mepsweb/data\\_stats/summ\\_tables/insr/state/series\\_2/2009/tia2.htm](http://meps.ahrq.gov/mepsweb/data_stats/summ_tables/insr/state/series_2/2009/tia2.htm).
- <sup>3</sup> Jon R. Gabel & Jeremy D. Pickreign, Issue Brief, “Risky Business: When Mom and Pop Buy Health Insurance for Their Employees,” Commonwealth Fund, April 2004, p.2.
- <sup>4</sup> Christine Eibner, “The Economic Burden of Providing Health Insurance: How Much Worse Off are Small Firms?,” Kauffman-Rand Institute for Entrepreneurship Public Policy, 2008, pp.37-38.
- <sup>5</sup> Dana Mattioli, “More Small Firms Drop Health Care,” *The Wall Street Journal*, May 26, 2009, [Hereinafter Mattioli].
- <sup>6</sup> Mattioli; Maureen Mersch & Mary Ann Armatys, “Challenges for Health Care in Uncertain Times, 2009: Hewitt’s 10<sup>th</sup> Annual Health Care Report,” Hewitt Associates, p.3, [http://www.hewittassociates.com/ MetaBasicCMAAssetCache /Assets/Articles/2009/ Hewitt\\_2009\\_Emerging\\_Health\\_Trends\\_Survey\\_Report.pdf](http://www.hewittassociates.com/ MetaBasicCMAAssetCache /Assets/Articles/2009/ Hewitt_2009_Emerging_Health_Trends_Survey_Report.pdf).
- <sup>7</sup> “Study Shows Small Business Owners Support Health Reform: Many Can’t Keep Up with Rising Health Care Costs,” Robert Wood Johnson Foundation Briefing Paper, December 2008, <http://www.rwjf.org/files/research/coveragesmallbizsummary2008.pdf> [Hereinafter RWJF Briefing Paper].
- <sup>8</sup> Lester Feder & Ellen-Marie Whelan, “Small Businesses, Large Problems: Health Care Costs Hit Small Employers,” Center for American Progress, October 30, 2008, [http://www.americanprogress.org/issues/2008/10/small\\_business\\_brief.html](http://www.americanprogress.org/issues/2008/10/small_business_brief.html) [Hereinafter Feder & Whelan].
- <sup>9</sup> Feder & Whelan.
- <sup>10</sup> Linda J. Blumberg, “Addressing Adverse Selection in Private Health Insurance Markets,” Statement before the Congress of the United States Joint Economic Committee, September 22, 2004, p.5; Yujing Shen & Randall P. Ellis, “How Profitable Is Risk Selection? A Comparison of Four Risk Adjustment Models,” *Health Economics*, vol. 11, 2002 (published online January 29, 2002 in Wiley InterScience, [www.interscience.wiley.com](http://www.interscience.wiley.com)), pp.165, 173.
- <sup>11</sup> “Competition in Health Insurance: A Comprehensive Study of U.S. Markets, 2008 Update,” American Medical Association, January 2009.
- <sup>12</sup> Sara R. Collins, et al, “Squeezed: Why Rising Exposure to Health Care Costs Threatens the Health and Financial Well-Being of American Families,” The Commonwealth Fund, September 2006, p.21 [Hereinafter Collins]; Ella Hushagen & Cheryl Fish-Parcham, “Failing Grades: State Consumer Protections in the Individual Health Insurance Market,” *Families USA*, June 2008. Data on out-of-pocket costs refers to adults.
- <sup>13</sup> Collins, p.10.
- <sup>14</sup> RWJF Briefing Paper.

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## About the Organizations Releasing this Report

### Virginia Main Street Alliance

*The Virginia Main Street Alliance, an initiative of Virginia Organizing, is a coalition of Virginia small business owners working to build a new voice on issues that matter to our businesses and our communities. Our members include both small employers and self-employed business owners, with a diverse representation of business types, race, gender and geography. We bring small business values into the public dialogue to advance policies that are good for small businesses, our employees and the communities that sustain us.*

### The Main Street Alliance

*The Main Street Alliance is a national network of small business coalitions in states across the country. The Alliance and its state partners create opportunities for small business owners to speak for themselves, advancing policies that work for small businesses and local economies.*

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