



# MAKING HEALTH CARE WORK

## FOR SMALL BUSINESSES IN NORTH CAROLINA

*Findings of a Fall 2010 Small Business  
Health Insurance Survey*

February 2011



**North Carolina Fair Share**



**The Main Street Alliance**

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## INTRODUCTION

As implementation of the new health care law unfolds at the state level, small business is a key stakeholder whose views should inform the ongoing implementation process. Small businesses are the engine of the U.S. economy, creating jobs and delivering essential services; implementing the health care law to serve small businesses well will help fire that engine and drive economic recovery.

As real-life experts on the problems in the health care system, small business owners have important perspectives on how to solve these problems and make health care work for businesses and the economy. This report focuses on the experiences and views of North Carolina small business owners as related in a survey conducted in October and November 2010.

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 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 buy, placing their health and financial security at risk.

The results presented in this report were gathered through a survey of 123 small business owners in Raleigh and the surrounding areas. Surveys were collected through face-to-face and one-on-one interactions with business owners, small group meetings, and phone interviews between October 4 and November 14, 2010.

## KEY FINDINGS

Key findings of the survey include that the majority of 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 to shop for coverage with other businesses in the state to increase their bargaining power and make coverage more affordable;
- Support strengthening the state's ability to review and act on health insurance companies' proposed rate increases;
- Believe employers who can afford to should pay a portion of employees' health insurance costs, but nearly two thirds were not aware of the new health premium tax credits that could assist them in doing so.

## 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 2007, over 5.9 million businesses in the U.S. (98 percent of all firms) had fewer than 100 workers. These businesses employed a total of 42.7 million people. In North Carolina, 87 percent of all firms had fewer than 20 workers, and 76 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 North Carolina, only 34 percent of businesses with fewer than 50 workers offered coverage, compared to 97 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 more 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 has found that one in 10 small businesses is looking at dropping health coverage entirely.<sup>6</sup> Additional research has found that one third of small businesses may be forced to reduce coverage, including dropping it entirely or cutting back in other ways.<sup>7</sup> The 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 with health care 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 one key contributing factor to the passage of the Patient Protection and Affordable Care Act (hereinafter Affordable Care Act) in March 2010. However, now that states are responsible for making decisions about how to structure the implementation of the Affordable Care Act at the state level, 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 can the state of North Carolina take as it implements the Affordable Care Act to make health care work better for small businesses?
- Do business owners support the principle of shared responsibility in paying for health coverage, and are they aware of new avenues (such as the new health premium tax credits) to support employers to offer coverage through the Affordable Care Act?

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

## **METHODOLOGY**

This report is based on a survey of 123 small businesses, including small employers with up to 100 employees and self-employed business owners, in Raleigh and the surrounding areas. Surveys were collected primarily through face-to-face interviews with business owners in their places of business and meetings of groups of business owners between October 4 and

November 14, 2010. A small number of surveys were also collected by phone.

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

## FINDINGS

### Respondent Information

About two thirds of the 123 surveys came from business owners based in Raleigh. The balance included business owners in Apex, Cary, Clayton, Durham, Fuquay Varina, Garner, Henderson, Knightdale, Lumberton, Rocky Mount, Smithfield, Wake Forest, Wendell, Whiteville, Willow Springs, and Zebulon.

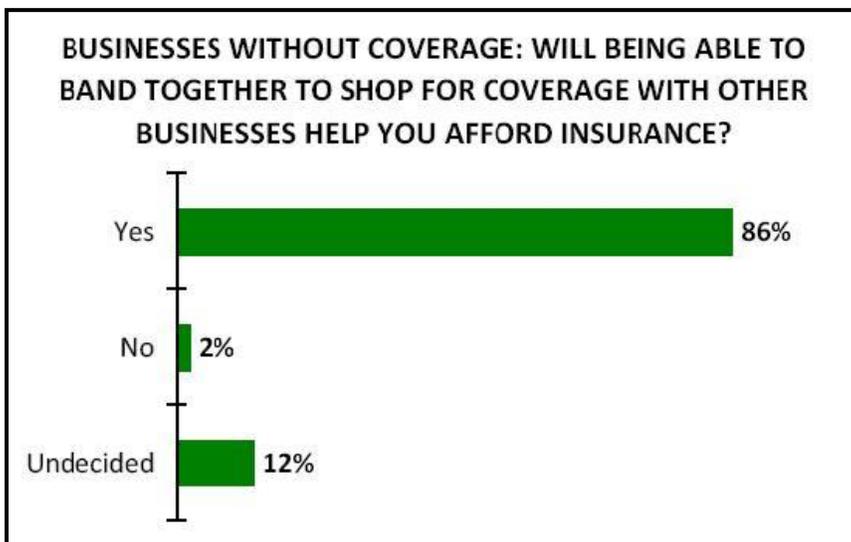
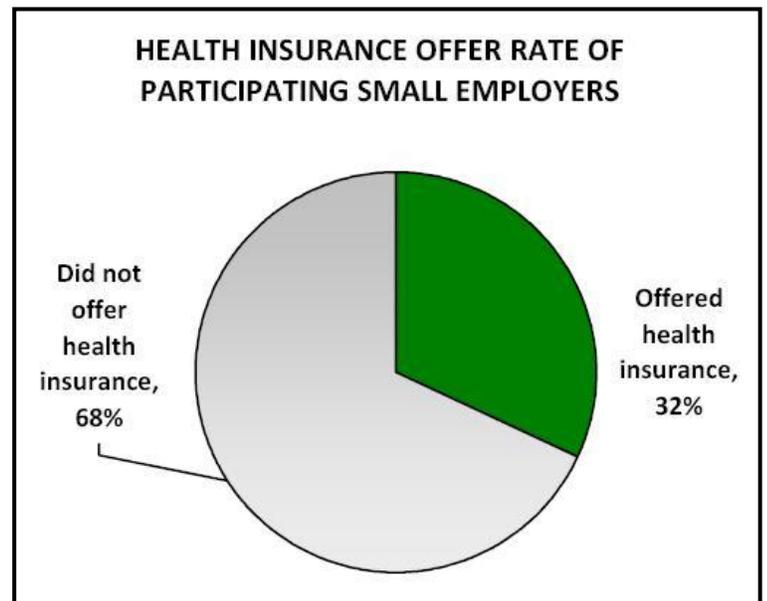
Thirty-four percent of responding business owners were small employers. Sixty-six percent were self-employed. Among the small employers, 59 percent had one to five employees, 21 percent had six to 10 employees, 13 percent had 11-25 employees and eight percent had more than 25 employees.

### Health Insurance Coverage and Offer Rates

Among self-employed respondents, 33 percent reported that they did not have health insurance coverage for themselves. Among those with dependents, 59 percent reported that they did not have coverage for their dependents.

Among responding small employers, 32 percent offered health insurance to all or some of their employees; 68 percent did not offer coverage at all.

When asked to identify contributing reasons why they do not have or offer health coverage, 75 percent of respondents indicated that health insurance is too expensive; among other response options (such as “it’s not a good value,” “don’t have time to investigate all the fine print,” and “don’t need it”), no other option received more than 16 percent.



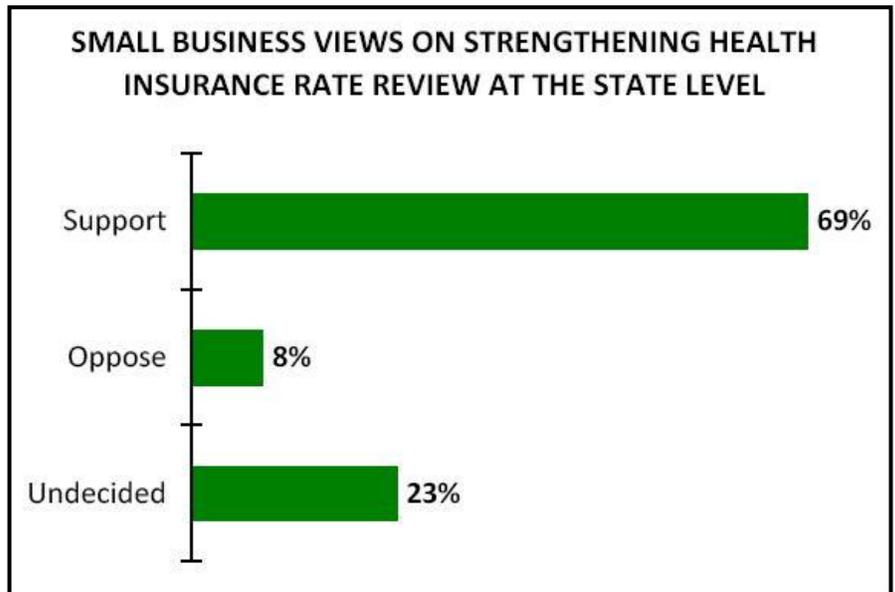
### Views on Banding Together to Shop for Health Coverage

The survey asked business owners who did not have or offer health coverage if they thought being able to band together to shop for coverage with other businesses and have more bargaining power would help them afford insurance.

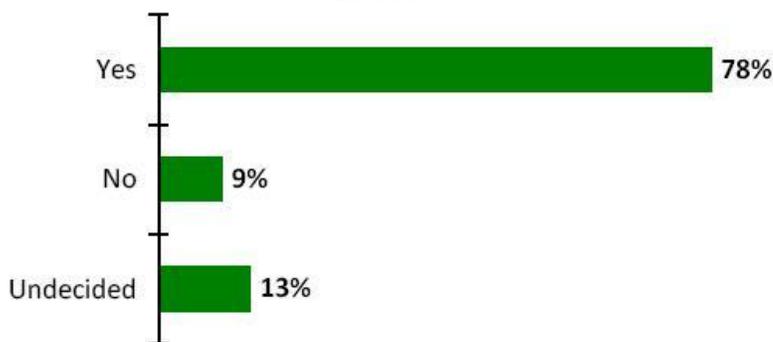
More than four out of five respondents (86 percent) said yes. Meanwhile, two percent said no and 12 percent were undecided.

### Views on Health Insurance Rate Review

When asked about a proposal to strengthen the state's ability to review and act on health insurance companies' proposed rate increases, 69 percent of respondents indicated they would support stronger rate review, while eight percent indicated they would oppose it and 23 percent were undecided.



### SHOULD EMPLOYERS WHO CAN AFFORD TO PAY A PORTION OF EMPLOYEES' HEALTH INSURANCE COSTS?

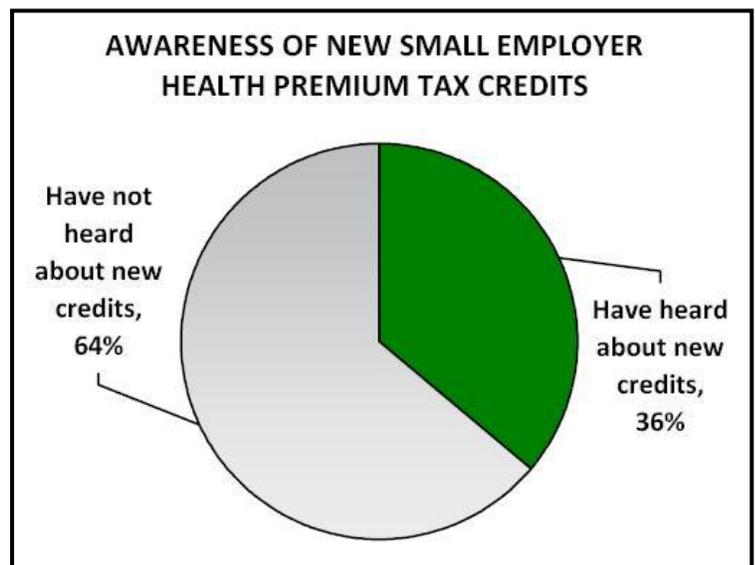


### Views on Employer Responsibility in Health Coverage

The survey asked business owners if they believe employers who can afford to should pay a portion of employees' health insurance costs. About three quarters of respondents (78 percent) said employers should contribute. About nine percent said they should not and 13 percent were undecided.

### Awareness of New Health Premium Tax Credits

When asked if they had heard about the Affordable Care Act's health premium tax credits that are available to many small employers who contribute toward employees' health coverage starting for the 2010 tax year, 36 percent of responding small employers said they had heard about the credits, while 64 percent said they had not.



## CONCLUSION

Small businesses have found themselves at the center of the country's health insurance troubles for decades. Without 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 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 North Carolina 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. Majorities of 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 to shop for coverage with other businesses in the state to increase their bargaining power and make coverage more affordable;

- Support strengthening the state's ability to review and act on health insurance companies' proposed rate increases;
- Believe employers who can afford to should pay a portion of employees' health insurance costs, but nearly two thirds were not aware of the new health premium tax credits that could assist them in doing so.

Implementation of the provisions of the Affordable Care Act creates opportunities for the state of North Carolina to address these issues and level the playing field for small businesses when it comes to health insurance. Some of these opportunities include:

- Development of a single, unified state health insurance 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.
- Development and enforcement of more stringent rate review standards that protect small businesses (as well as other insurance customers) from unjustified health insurance rate increases.
- Enforcement of the new minimum standards for insurance companies' medical loss ratios (a basic measure of insurance value based on the percentage of premium dollars spent on actual health costs versus administrative costs, advertising, executive compensation and lobbying expenditures), including requiring rebates from insurers who fail to meet the new minimum standards.
- 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 able to use them to begin or continue offering health coverage to their employees.

## ENDNOTES

- <sup>1</sup> U.S. Census Bureau, “Number of Firms, Number of Establishments, Employment, Annual Payroll, and Estimated Receipts by Enterprise Employment Size for the United States and States, Totals: 2007,” 2007 County Business Patterns and 2007 Economic Census, [http://www2.census.gov/econ/subs/data/2007/us\\_state\\_totals\\_2007.xls](http://www2.census.gov/econ/subs/data/2007/us_state_totals_2007.xls).
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- <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.
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### About the Authors of this Report

#### North Carolina Fair Share

*North Carolina Fair Share (NCFS) is a statewide membership organization established in 1987 to bring together people within communities impacted by issues of injustice on health care, the environment, economic justice and voting rights to work on their own behalf for solutions to these issues toward a fairer NC.*

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#### 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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