



**Senate Small Business and Entrepreneurship Committee
Roundtable on Small Business and Health Care Reform
July 9, 2009
Comments of John Arensmeyer, founder and CEO
Small Business Majority**

Small Business Majority appreciates the opportunity to provide the small business perspective on the vital issue of healthcare reform. We extend our thanks to Sens. Landrieu and Snowe for organizing a roundtable discussion that allows us to take a moment to consider the needs of small business as the reform debate accelerates.

Small Business Majority is a nonprofit, nonpartisan organization founded and run by small business owners and focused on solving the biggest problem facing small businesses today: the skyrocketing cost of healthcare. We represent the 27 million Americans who are self-employed or own businesses of up to 100 employees. Our organization uses scientific research to understand and represent the interests of all small businesses.

I have been an entrepreneur for more than 20 years, including 12 years owning and managing an Internet communications company specializing in financial services. Together with two other senior managers in our organization, we have a total of 70 years running successful small businesses ranging from high-tech to food production to retail.

We are pleased to be invited to discuss small business and comprehensive healthcare reform. We welcome the current work toward reform that will reduce the costs of insurance and medical care, while making coverage affordable, fair and accessible. Our research shows that comprehensive health insurance reform is small business owners' number one need, and controlling costs is essential to ensuring our ability to obtain high-quality, affordable healthcare for ourselves, our families and our employees.

My comments will highlight a few of the issues of most interest to small businesses. I'll discuss what we have learned from our scientific research about both the opinions of small business owners and the projected economic impact of various reform options—and the impact of failing to act. The points I'll be making include:

- Our research shows that small business owners want and need reform now. The high cost of healthcare is killing us.
- A well-designed insurance exchange could erase some of the inequities that currently exist in the individual and small-group markets and simplify the process of obtaining insurance for small businesses.
- The self-employed have separate, specific problems with the healthcare system and need their own remedies, such as bringing the tax rules for purchase of health insurance by the self-employed in line with those of all other businesses.

- A properly designed shared responsibility reform model will significantly help small businesses, according to an economic study we commissioned from M.I.T. economist Jonathan Gruber.
- For small businesses to participate in a shared responsibility model, they will need assistance such as tax credits and exemptions for the smallest businesses.

Healthcare Costs are Killing Small Business and Sapping Our Economic Vitality

National surveys of small business owners consistently show that the cost of health insurance is our biggest overall problem. In fact, the crushing costs of healthcare outranked fuel and energy costs and the weak economy for 78% of small business people polled by the Robert Wood Johnson Foundation in 2008.¹

Small businesses are at a disadvantage in the marketplace largely because our small numbers make rates higher. According to research supported by the Commonwealth Fund, on average we pay 18% more than big businesses for coverage.² Small businesses, including the growing legions of the self-employed, need a level playing field to succeed and continue as the job generator for the U.S. economy.

Small business owners want to offer health coverage, and our surveys show that most of us feel we have a responsibility to do so. With staffs of 5, 10 or even 20 people, we run tight-knit organizations, know our employees well and depend on each employee for our businesses' success. We don't want to see our valuable employees wiped out financially by a health problem, or ignore illnesses because they can't afford to go to the doctor.

Many small businesses are forced to drop coverage altogether. According to the Kaiser Family Foundation, among firms with 3 to 9 workers, the percentage that offers insurance dropped from 57% in 2000 to 49% in 2008.³

This makes small business employees a significant portion of the uninsured population. Of the 45 million Americans without health insurance in 2007, nearly 23 million were small business owners, employees or their dependents, according to Employee Benefit Research Institute estimates.⁴

Finally, if we don't get control of the healthcare crisis facing small businesses, we will impede our overall economic growth. Small businesses under 100 employees employ 42% of American workers.⁵ Traditionally, small businesses lead the way out of recessions. Addressing this crisis is essential to our vitality as a nation.

¹ "Study shows small business owners support health reform," Robert Wood Johnson Foundation, 2008.

² J Gabel et al, Generosity and Adjusted Premiums in Job-Based Insurance: Hawaii is Up, Wyoming is Down, *Health Affairs*, May/June 2006.

³ Kaiser Family Foundation/HRET Employer Health Benefits Annual Survey, 2008

⁴ Employee Benefit Research Institute, Sources of Health Insurance and Characteristics of the Uninsured: Analysis of the March 2008 Current Population

⁵ U.S. Bureau of Census, 2006 County Business Patterns

Scientific Research Demonstrates the Urgency of Reform for Small Business

We have sponsored research that actually models what would happen to small business without comprehensive reform. The research underlying this report, made public last month, was conducted for Small Business Majority by Jonathan Gruber, noted economist at the Massachusetts Institute of Technology. Dr. Gruber's research found that without reform, over the next 10 years the continued rising cost of healthcare coverage will cost small businesses \$2.4 trillion, more than 178,000 jobs, \$52 million in profits and reduce small business wages by \$834 billion.⁶

Our scientific opinion research also reinforces what we hear anecdotally every day: High healthcare costs are putting enormous pressure on small business owners. We have just completed a series of telephone surveys of a scientific sample of small business owners in 16 states⁷. The staggering cost of health coverage is reflected in some of the key findings:

- Only 40% of those surveyed are able to offer health insurance to their employees.
- An average of 86% of those who don't offer coverage say that it is because they can't afford it.
- An average of 72% of those who do offer insurance say they are struggling to do so.
- An average of 69% say that healthcare reform is necessary to save the economy.
- When asked about the most important goals for healthcare reform, the top choice is most often "control costs."

In Louisiana, for example, only 36% of respondents in our survey are able to offer healthcare coverage; of those who don't offer it, 87% say that they can't afford to do so, and half said their access to affordable health insurance is fair or poor.

A Well-Designed Health Insurance Exchange is Crucial for Small Business

We need to slow the growth of overall healthcare costs to make coverage affordable and to improve the competitiveness of small businesses. The key to cost containment is to create a marketplace where there is healthy competition among insurers, which would create incentives to lower costs by increasing price competition.

The best way to control costs for small businesses is with a well-designed health insurance exchange as part of comprehensive healthcare reform legislation. An insurance exchange is intended to address many of the problems that individuals and small businesses face in the current health insurance market. This type of marketplace or exchange was supported by an average of 81% of small business owners in our recent state polling.⁸

⁶ The Economic Impact of Healthcare Reform on Small Business, Small Business Majority; available at www.smallbusinessmajority.org

⁷ <http://www.smallbusinessmajority.org/sbmresearch.php>

⁸ <http://www.smallbusinessmajority.org/sbmresearch.php>

A well-designed exchange will:

- Reduce the extra premium paid by small businesses, and reduce the volatility (year-to-year changes) in health premiums, by pooling small business buying power and gaining economies of scale;
- offer people choices of multiple insurers, providers and delivery systems, and—by allowing portability of health coverage—reduce employee recruitment barriers;
- help people shop for insurance and make it easy for them to compare options by providing individuals and employees with clear and comparable information regarding insurers, provider networks and benefit plan options available to them;
- greatly reduce the burden on small business owners of administering health benefits; and
- drive innovation and improvements in affordability, quality and customer service resulting from healthy competition among both insurers and providers.

For an exchange to be successful, it must also be financially sustainable over the long run. Many exchanges have been plagued in the past by adverse selection. If the exchange is not designed properly, there is a danger that the risk profile of the exchange participants is higher than that of the rest of the market, i.e., high-cost people are selectively enrolled in the exchange. As a result, the premiums charged in the exchange are higher than normal, which leads to a spiral of rising premiums as lower-cost people opt out of the exchange.

We believe that the exchange should be a large, national pool with strong administrative direction. A large exchange will be able to provide help to more of the people in small businesses who will benefit the most from it. It will also spread fixed administrative costs over a larger base, and spread the risk more broadly.

The health insurance exchange should have a strong role. This will enable the exchange to exert its market power to drive innovation and improvements in affordability, quality and customer service resulting from healthy competition among both insurers and providers. Its role should not be limited to information and decision support (an “insurance mart”); it should also provide enrollment and administrative functions that will benefit individuals and small businesses. In addition, it should be an “active purchaser”—similar to the role played by many large employers—with the authority to determine which health plans will be offered, based on their ability to meet affordability and quality standards.

The design of the exchange must also include elements that define the structure, governance, financing and state role in the administration of the exchange. So, for instance, the exchange could be modeled upon the Federal Employee Health Benefits Plan (FEHBP) and similar health benefit plans managed by large private employers. There would also need to be administrative oversight at the federal level, and options for states to establish their own state-level exchanges.

The transition to the new system and structure must be managed to minimize rate shocks and other disruptions. States currently have a wide variety of insurance regulations (rating, benefit design, medical screening, etc.), resulting in very different markets in different states. In addition, the insurance regulations for individuals and small groups within a state are

usually different. (For example, most states allow medical screening and age rating in the individual market but not in the group market.) In these states, applying the same insurance rules—in effect, merging the individual and small group markets in the exchange—would create major disruptions. Some kind of transitioning makes sense, but small businesses and individuals face serious problems now, and they need relief as soon as possible.

The Self-Employed Need a Level Playing Field

A significant majority of the small business sector consists of self-employed people—as of 2007 there were more than 21.7 million of them, a number that continues to grow as the information economy expands. Reform must address their specific concerns, which are slightly different from those of firms with employees. For instance, self-employed people usually purchase insurance from the individual market, which is often more expensive and restrictive than health plans offered in the small group market.

Healthcare reform needs to provide a fairer, more predictable alternative to the individual market. At the same time, if reform includes a requirement that every American obtain healthcare coverage, the new system will need to offer tax credits or premium assistance for the self-employed, depending on their financial status.

Another issue of great concern to us is the unfair tax treatment of the self-employed. Under the current tax code, self-employed individuals are unable to deduct premiums as a business expense and are required to pay an additional 15.3% self-employment tax on their healthcare costs. These business owners are at a significant tax disadvantage to larger businesses, which do not pay payroll taxes on the health insurance they provide employees. It is one of many barriers these Americans face in trying to access affordable health insurance for themselves and their families.

The self-employed should be allowed to fully deduct their health insurance premiums for the purposes of their income tax and self-employment tax.

Rural Small Businesses are Hit Particularly Hard

Small states and rural parts of America are particularly vulnerable to the health insurance cost spiral in part because they are dominated by small businesses and self-employed people, according to a 2006 comparison of the medical out-of-pocket expenses of urban and rural people.⁹ Privately insured rural residents were more likely to be self-employed or work for a small business and to have inadequate coverage. For instance, in Montana 55% of workers are self-employed or work for small businesses, compared with the 42% national average.

In addition, rural residents have less access to affordable coverage. Nearly one in five of the uninsured live in rural areas. Farmers and ranchers have a particularly hard time obtaining adequate coverage and are usually relegated to the individual insurance market, which is

⁹ Ziller, E. C., Coburn, A. F., & Yousefian, A. E. "Out-of-pocket health spending and the rural underinsured." *Health Affairs*, Nov/Dec 2006; 25(6), 1688-1699.

restrictive and expensive. A survey of Missouri farmers found that those buying their own insurance paid \$2,117 more than those who were able to buy through a group plan.¹⁰ Another survey of farmers and ranchers in several rural states found one in five carries medical debt.¹¹

These high and rising costs can be directly correlated to the increasing market dominance of just a few insurers in most parts of the country, particularly small and rural states. For example, the top two insurers have 95% of market share in Alaska, 95% in Rhode Island, 88% in Maine, 85% in Montana and Wyoming, and 74% in Louisiana.¹²

Rural residents also have a harder time obtaining medical care because there are fewer primary care physicians and specialists available. There are 55 primary care physicians per 100,000 residents in rural areas, compared with 72 per 100,000 in urban areas.¹³ The shortage is even worse in isolated rural places.

Rural Americans working for themselves or for small firms would benefit greatly from an insurance exchange that would provide a simpler, fairer, more efficient market for obtaining health insurance. Freed from the worries and cost of inadequate coverage, they could focus on running their businesses and being productive, thereby strengthening their local economies, which are particularly stressed by the economic downturn.

Making a System of Shared Responsibility Work for Small Business

Our scientific polling across the country shows clearly that small business owners are willing to collaborate with other stakeholders to develop a comprehensive plan that improves healthcare for everyone. Sixty-six percent of small business owners responding to our recent state surveys support the idea that the responsibility for financing a more affordable healthcare system should be shared among individuals, employers, insurance companies, providers and government. In Louisiana 63% agree with this concept. [It should be noted that respondents to our surveys included an average of 17% more Republicans (40%) than Democrats (23%), while 28% identified as independent.]¹⁴

A well-designed system of shared responsibility will achieve the following goals:

- Strengthen the employer-based system of health benefits.
- Minimize the need for publicly funded subsidies and additional taxes.

¹⁰ Dohogne, Aaron. (Sept. 2008). "Survey recommends remedies for farmers' high insurance rates." *The Missouriian*. <http://www.columbiamissourian.com/stories/2008/09/26/missouri-farmers-paying-more-individual-healthcare-insurance/>

¹¹ The Access Project. (Sept. 2007). "Issue Brief: 2007 Health Insurance Survey of Farm and Ranch Operators." http://www.accessproject.org/adobe/issue_brief_no_1.pdf

¹² "Competition in health insurance: A comprehensive study of U.S. Markets: 2007 Update," American Medical Association.

¹³ Fordyce MA, Chen FM, Doescher MP, Hart LG. (2007). *2005 physician supply and distribution in rural areas of the United States*. Final Report #116. Seattle, WA: WWAMI Rural Health Research Center, University of Washington.

¹⁴ <http://www.smallbusinessmajority.org/sbmresearch.php>

- Put all businesses on a level playing field by ensuring that everyone contributes equitably and eliminating the competitive disadvantage for businesses that do provide health insurance.
- Improve affordability and access to coverage for employees who currently can't afford the premiums.
- Align the cost of health coverage with the small business's ability to pay, which will enable small businesses to continue to be the engine of growth in the American economy.

Our economic modeling by Jonathan Gruber demonstrates that, for shared responsibility to work, it must be accompanied by an acknowledgement that small businesses cannot bear the full burden of healthcare costs. Dr. Gruber's research found that comprehensive reform including even modest cost containment measures coupled with a well-designed structure of tax credits, sliding scale obligations and exemptions for the smallest companies, will offer a vast improvement over the *status quo* and spiraling future costs for small businesses. This type of system will give small businesses the relief they need, potentially saving them as much as \$855 billion over the next 10 years, reducing lost wages by up to \$339 billion and minimizing job losses by 72%.¹⁵

Specifically, our modeling of the most successful reform scenarios presumes an exemption for the smallest businesses, a sliding scale of obligations based on the size of payroll or the number of employees up to 6.5% of payroll, and tax credits of 50% of health costs for employees earning under \$100,000 at businesses with fewer than 50 employees.

Conclusion

Healthcare reform is not an ideological issue—it's an economic one. Small business owners know this, which is why they overwhelmingly support a comprehensive solution to reforming the way we pay for healthcare. We are encouraged by the progress being made in Congress on healthcare reform, and we appreciate the Senate Small Business and Entrepreneurship Committee's efforts to shed further light on this complicated, but very important, topic.

¹⁵ The Economic Impact of Healthcare Reform on Small Business, Small Business Majority; available at www.smallbusinessmajority.org