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ON

THE IMPACT OF THE AFFORDABLE CARE ACT ON SMALL BUSINESSES

BEFORE THE

**UNITED STATES HOUSE COMMITTEE ON SMALL BUSINESS,
SUBCOMMITTEE ON HEALTHCARE AND TECHNOLOGY**

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House Committee on Small Business, Subcommittee on Healthcare and Technology
Hearing on the Impact of the Affordable Care Act on Small Businesses
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Chairwoman Ellmers, Ranking Member Richmond, and Members of the Subcommittee, thank you for the opportunity to discuss how the Affordable Care Act is improving the affordability, accessibility, and quality of health insurance available to small businesses and their employees. The provision of health insurance to employees can present a very real challenge to small businesses. On average, small businesses pay about 18 percent more than large firms for the same health insurance policy.¹ Small businesses lack the purchasing power that larger employers have and are often the targets of insurance industry coverage restrictions and significant annual rate increases. Given the difficulties small businesses face in finding and keeping affordable, high-quality health insurance, it is not surprising that they are less likely to offer insurance to their employees. According to the 2010 Kaiser/HRET Employer Health Benefits Survey, 59 percent of businesses with 3 to 9 employees offered health insurance, compared with 99 percent of businesses with more than 200 employees. The Kaiser/HRET Survey also found that the most important reason that small businesses cited for not offering health benefits is that the cost of insurance is too high.² Small businesses in today's market are disadvantaged not only by their lack of purchasing power compared to large businesses, but also by the challenges they face in comparing various insurance products and selecting the best option.

The Affordable Care Act contains a number of provisions that will help close the gap between small and large businesses' ability to offer health insurance to their employees. For example, the law establishes tax credits for small businesses that provide health insurance to employees beginning with the 2010 tax year. Additionally, starting in 2014, it prohibits most insurers from charging small businesses higher rates based on the health status or gender of employees. Finally, it creates, as part of the Affordable Insurance Exchanges, the Small Business Health Options Program (SHOP), which will help small business owners compare insurance options in their State and purchase coverage for themselves and their employees. SHOP, which will

¹Gabel J, McDevitt R, Gandolfo L, et al. Generosity and Adjusted Premiums in Job-Based Insurance: Hawaii is Up, Wyoming is Down. *Health Affairs*, 2006, 25(3): 832-843.

²<http://ehbs.kff.org/pdf/2010/8085.pdf>, pages 37 and 43

become operational by January 1, 2014, will help enhance competition in the health insurance market, improve choice of affordable health insurance, and give small businesses the same purchasing clout as large businesses.

Tax Credits for Small Businesses that Insure their Employees

The Affordable Care Act establishes a Small Business Tax Credit that is making health coverage more affordable for small businesses. The tax credit is designed to encourage both small businesses and small tax-exempt organizations to offer health insurance coverage to their employees for the first time, or to maintain the coverage they already offer. It is targeted at small businesses and tax-exempt organizations that primarily employ moderate- and lower-income workers. Small businesses can claim the credit for 2010 through 2013 and for two years after that. For each year from 2010 through 2013, the maximum credit is 35 percent of the employer contribution to premiums paid by an eligible small business, and 25 percent of the contribution paid by an eligible tax-exempt organization. After 2013, the maximum matching rate increases to 50 percent for small businesses and 35 percent for tax-exempt organizations, and the credit will be available only to small businesses that offer coverage to their employees through the SHOP.³ The tax credits provide a vitally needed bridge to 2014, when small firms will be able to shop for coverage in the state-run Affordable Insurance Exchanges.

We are already seeing the benefits of these provisions of the Act. In a survey released by Small Business Majority in January 2011, one-third of small business owners surveyed who do not offer insurance said they would be more likely to do so because of the tax credit and the Exchanges. Nearly a third of respondents who were offering insurance said they would be more likely to continue offering it because of the tax credit and the Exchanges.⁴ There are signs that insurance sales to small businesses are increasing. Blue Cross/Blue Shield of Kansas City, which reached out to local employers to make sure they were aware of the credit, is reporting a 58 percent increase in the number of small businesses buying insurance since April 2010. This

³ <http://www.irs.gov/pub/newsroom/taxcreditflyer.pdf>

⁴ http://www.smallbusinessmajority.org/reports/SBM-Healthcare_Survey_010411.pdf

translates into 400 new small businesses buying coverage for 9,000 employees in the area.⁵ UnitedHealth Group enrolled 75,000 new customers in firms with fewer than 50 employees.⁶

Ending Price Discrimination Based On Illness and Other Factors

Small businesses are heavily disadvantaged in today's insurance markets. Without a large group of enrollees to pool risk, a single sick employee can cause a drastic premium spike for small employers. The premium spike can be particularly large if the employee or dependent has a costly condition such as cancer or heart disease or a complicated birth. While most States limit the extent to which premiums can vary due to employee health status and other factors, many do not. In the current market, health status and experience rating have a disproportionate impact on small businesses, and even with limits on variation, premiums can be significantly higher for small businesses.

The Affordable Care Act takes significant steps to eliminate this disparity. Beginning in 2014, the law prohibits new health plans from rating on the basis of health status or claims history. By eliminating these discriminatory rating practices, small businesses will no longer see their premiums skyrocket because one or two employees fall ill. In addition, the law prevents insurers from varying rates based on the gender of a small business's employees and limits how much issuers can increase rates based on employees' ages. These new rating rules will help make small businesses' health insurance rates fairer, more predictable, and easier to understand. CBO estimates that premiums in the small group market could be up to 1 to 4 percent lower than they would have been without the Affordable Care Act in 2016. Savings will come primarily from insurance reforms, the competitive nature of the Exchanges, and lower administrative costs. The small business tax credits that will help reduce costs for eligible small employers in SHOP will save those businesses even more.

Starting this year, limits on health plans' medical loss ratio (MLR) will also save small businesses money as insurers that fail to meet the standard (80 percent in the small group market) must provide refunds to the businesses to which they sold coverage. Finally, the Affordable Care

⁵ Cauthin P., "Tax Credits Spur Health Coverage," Kansas Health Institute News Service, January 10, 2011.

⁶ Levey NN, "More Small Businesses are Offering Health Benefits to Workers," The Los Angeles Times, December 27, 2010.

Act provides \$250 million to States to help improve the oversight of proposed health insurance premium increases, take action against insurers seeking unreasonable rate hikes, and ensure consumers receive value for their premium dollars.

Affordable Insurance Exchanges: Choices, Competition, and Clout for Small Businesses

The Affordable Care Act created the Affordable Insurance Exchanges (Exchanges), which are new State-based competitive marketplaces for buying private health insurance. Both individuals and small businesses will be able to buy health insurance through Exchanges beginning in 2014.

On July 11, 2011, the Centers for Medicare & Medicaid Services (CMS) released a Notice of Proposed Rulemaking (NPRM) outlining a framework that will enable States to build Exchanges. On the same date, CMS released a second NPRM that provides a framework for ensuring premium stability for plans and enrollees in the Exchanges. These NPRMs reflect more than a year's worth of work with States, small businesses, consumers and health insurance plans, and offer substantial flexibility to States in designing their Exchanges. We are engaged in a continuous dialog with States, small businesses, consumer advocates, and others on the best way to shape the Exchanges to meet their needs. In addition, on July 18, 2011, CMS released an NPRM that proposes standards for Consumer Operated and Oriented Plans (CO-OPs), new private non-profit, consumer-governed health insurance plans that will help increase competition in the Exchanges and give small businesses additional affordable health insurance choices.

These proposed rules are the latest in an ongoing series of steps that CMS has taken to help States develop Exchanges. Already, 49 States, the District of Columbia, and 4 Territories have received Exchange Planning grants authorized under the Act, and to date, over half of the States have taken additional action to establish Exchanges. CMS is accepting public comment on the proposed rules for 75 days to learn from States, consumers, and other stakeholders how the rules can be improved. CMS will modify these proposals based on feedback that we receive.

Small Business Health Options Program (SHOP)

Small businesses will be able to buy health insurance through a part of the Exchange called the SHOP. States can choose to operate separate Exchanges for individuals and small businesses, or

have a single Exchange offering individual and small group insurance. Additionally, States can choose to keep participants in the individual Exchange and those in the SHOP in separate risk pools, or they may merge the two risk pools, giving individuals in the Exchange and workers in small businesses the same plan options.

SHOPs are designed to make buying health coverage easier and more affordable. SHOPs will give small businesses and their employees many of the advantages large employers have today – such as more choice, more competition, and more clout in the marketplace. Small businesses and their employees will be able to easily compare health plans, get answers to questions, and enroll in a high-quality health plan that meets their needs.

Under the Affordable Care Act, businesses with up to 100 employees will be eligible to purchase health insurance through the SHOP. States can choose to limit participation to businesses with up to 50 employees until 2016. Starting in 2017, States may let businesses with more than 100 employees buy large group coverage through the SHOP.

Increasing choice and competition: SHOPs will enable small businesses to offer their employees a much greater choice of health plans from insurers, options that large employers enjoy in the current marketplace. In general, small businesses participating in the SHOPs will choose a level of coverage and a level of employer contribution to determine which qualified health plans they will make available to their employees. In this context, levels of coverage include four benefit categories that will be available through the Exchanges (bronze, silver, gold, and platinum) which indicate the cost-sharing level for consumers. Employees will choose among the available qualified health plans within the level offered by their employer, applying the applicable employer contribution to a plan within that level. This employee choice model provides side-by-side comparisons of health plans, benefits, premiums, cost-sharing, and quality. Exchanges may also choose to provide additional options to employers through SHOP.

Plans that participate in the Exchanges will need to compete for business by proving to employers and consumers that they can offer the best product at the best price. This type of market competition has the power to drive improvement in plan quality and affordability.

Exchanges will use a streamlined, simple enrollment system geared toward consumers.

Exchanges will enable consumers to learn about coverage options provided in the market so they can make informed choices about the coverage available through the Exchange. State Exchanges have flexibility regarding how they design their website and whether they use the application that will be made available by CMS or design one on their own that is comparable. State Exchanges will design a process for ensuring that participants' information is safe and secure.

Exchanges will also build partnerships with and award grants to entities known as "Navigators," who will reach out to employers and employees, consumers, and self-employed individuals to:

- Conduct public education activities to raise awareness about qualified health plans;
- Distribute fair and impartial information about enrollment in qualified health plans, premium tax credits, and cost-sharing reductions;
- Assist consumers in selecting qualified health plans;
- Provide referrals to an applicable consumer assistance program or ombudsman in the case of grievances, complaints, or questions regarding health plans or coverage; and
- Provide information in a manner that is culturally and linguistically appropriate.

States are given substantial flexibility in determining what role brokers and agents, who are a vital part of the small group market, will play in the SHOP. For example, States may allow agents and brokers to serve as Navigators in the SHOP.

Preserving employer control and State flexibility: While there are many new options available for small businesses as a result of the Affordable Care Act, small business owners will decide whether to participate in the SHOP. While the SHOP and Exchanges will dramatically expand coverage options for many, small businesses will still have the choice of purchasing private health insurance outside of the SHOP and the Exchanges.

If small businesses do participate in the SHOP, the NPRM proposes that they will be able to choose their own level of contribution toward their employees' coverage, and, if they choose, make a single monthly payment via SHOP rather than making individual payments to multiple

plans on behalf of their employees. Employers will write one check to the SHOP, and the SHOP will take care of paying each insurance company the correct amount. This single payment is designed to increase the convenience of participating in the SHOP for small employers and reduce their administrative burden, making it easier for them to offer a choice of plans to their employees.

Under the NPRM, States will have flexibility in deciding how the SHOP functions. During the current public comment period, we hope to hear from all stakeholders, including small businesses, on the best way to structure the SHOP to maximize choice, competition, and value for the employer's premium dollar. For example, in addition to employee choice among plans in a particular benefit level, the NPRM provides Exchanges the option to allow an employer to select one or more plans for its employees. This is how many small employers offer coverage in the current small group market. This additional flexibility could allow employers to choose an option where employees choose plans at multiple levels, with the employee paying the cost difference for more generous plans.

Increased clout: In the current market, small businesses pay disproportionately higher administrative costs compared to large businesses. SHOPS can save small businesses money by creating a competitive marketplace of qualified health plans and a simplified enrollment system. CBO estimates that lower administrative costs in the small group market, through economies of scale and standardization of benefits, will reduce average premiums by 1 to 4 percent.⁷ In addition, insurance companies within the SHOPS will compete for business on a level and transparent playing field, driving down costs. As previously mentioned, small business may also be eligible for the small business tax credit when they offer health coverage to their employees through a SHOP after 2013.

Conclusion

Small businesses are already benefiting from the Affordable Care Act and those benefits will expand dramatically as the Act continues to take effect. The small business tax credit is lowering costs and providing a bridge to 2014, when small businesses will enjoy many of the

⁷ <http://www.cbo.gov/ftpdocs/107xx/doc10781/11-30-Premiums.pdf> (2009)

advantages from which large businesses already benefit: larger risk pools, greater purchasing power, and a choice of plans. In addition, limits on discriminatory rating practices, risk adjustment, reinsurance, risk corridors, and greater pooled purchasing of coverage will go into effect in 2014 – ensuring that small businesses do not face a premium shock when their employees get sick and need health coverage most, thus keeping coverage affordable into the future.

Small businesses will continue to benefit from the Affordable Care Act. The Rand Corporation estimates that without passage of the Affordable Care Act, only 53 percent of small businesses with fewer than 10 employees and 71 percent of small businesses with 11 to 25 employees would have offered coverage in 2016.⁸ However, because of the Affordable Care Act, an estimated 77 percent of small businesses with fewer than 10 employees will offer coverage in 2016 – resulting in over 1 million additional employers and 6 million additional workers with health insurance coverage – and almost 90 percent of small businesses with 11 to 25 employees will offer coverage in 2016 – that’s 3 million additional workers with coverage.⁹

Thank you for the opportunity to appear before you to discuss the Affordable Care Act’s critical provisions to support small businesses’ ability offer health insurance to their employees.

⁸ http://www.rand.org/content/dam/rand/pubs/technical_reports/2010/RAND_TR825.pdf (2010)

⁹ *ibid.*