

Running Head: CAN SMALL BUSINESSES PROVIDE AFFORDABLE HEALTH CARE

Can Small Businesses Provide Affordable Health Care to Employees

And Still Maintain Profits And Margins?

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## Can Small Businesses Provide Affordable Health Care to Employees And Still Maintain Profits And Margins?

Small businesses are extremely important for the prosperity of America's economy in today's competitive labor market. According to the United States Small Business Administration, "they represent about half of its output, employ about half of the private sector work force, fill niche markets, innovate, increase competition, and give individuals in all life circumstances a chance to succeed" (The Small Business Economy: A Report To The President, 2004, p. 5). To succeed is significant because the chance offers many individuals the opportunity to capitalize on business possibilities that large corporations may not be able to provide. However, small businesses have many challenges to overcome to ensure this success.

Offering health care plans to employees is an issue that has been magnified as a result of the rising cost of health care for large businesses as well as small businesses. The benefit for small businesses to provide reasonable health care presents an incentive to help attract and retain highly qualified individuals in the increasingly tight labor environment. However, over the last decade, health care cost has been on the rise nationally. Large firms have even reduced health care benefits and/or increased employee contributions to keep up with the rising tide. How are small businesses dealing with this issue? This paper will focus on one aspect of the many problems facing small business today. Can small businesses provide affordable health care to employees and still maintain profits and margins?

Because of the challenge to provide affordable health care for employees without decreasing profits, small businesses suffer and are unable to sustain experienced individuals. The employees who choose to be employed by businesses that do not offer health care suffer as well. This produces families who are not given the support of medical care when needed.

*Cover the Uninsured Week* states, “Nationally, 56% of adults without health insurance say they do not have a personal doctor or health care provider, compared with just 16% of people with health insurance.” (Wyle, 2004, para.7) If small businesses continue to not provide health care for their employees, a large number of employees and their families will not receive medical attention and their health will suffer.

For the purposes of this paper, our approach will be to investigate and discover the range of answers to our research questions and present our findings and conclusion to our readers. A small business is defined as any private or public for profit institution with 199 or fewer employees.

Historically, small businesses have always been an important part of the American economy. “During the last decade, small businesses led the way in the nation’s economic expansion, the longest economic expansion in American History”, said Gregg Steinberg, President and CEO of the international profit associates (IPA SBRB Study Indicates health care as fastest growing small business cost, 2004, para 4). The small business industry has also played a significant role in the health care of the American citizen, but has not always been able to fulfill the need of American workers. The Pepper Commission reported in 1989 that 31 million people did not have health insurance (Reynolds, 1989). Although all the uninsured are not employed in small business, from 1980 to 1990 the small business sector has consistently accounted for a disproportionate share of the uninsured (Marian, 2001). Throughout history, the government has intervened on the behalf of the uninsured and many laws and programs have been enacted to address health care concerns. Programs like Medicaid for the indigent, Medicare for the elderly and Health Maintenance

Organizations (HMOs) and Preferred Provider Organizations (PPOs) for everyone else have all been created to solve health care issues.

Managed care programs were not created by the health care industry. In fact, the federal government in the 1970s initiated managed care programs, such as HMOs. The HMO Act of 1973 was the foundation of HMO development and required employers to offer federally qualified HMOs to their employees. In 1998, 85% of all employees were enrolled in some form of managed care. In the mid-1990s, the typical employee with family coverage paid about 30% of his or her health insurance premiums; single employees paid 22% (Viet, 1998).

Managed care has not been the answer for small business owners' health care crisis. The constant rising of health care cost has been evident for decades. In 2002, small businesses saw a 12.5% cost increase from 2001 to 2002, while the smallest firms, those with three to nine workers, saw the largest increase at 16.5% (McCrea, 2002). By 2003, health insurance premiums had increased by 14% over the previous year and marked the seventh straight year of health insurance premium increases and the third consecutive year of double-digit increases. (Sinnott, 2004) Essentially, the rate of increase had exceeded the rate of inflation by over 10%.

Four consecutive years of double-digit hikes in 2001 through 2004 forced many small businesses to drop health care benefits or postpone hiring staff in lieu of dropping coverage for current employees. According to the Kaiser Foundation, just 63% of small firms offered health benefits in 2004, down from 68% in 2001 (Henry, 2004). On a national level, this translates into five million fewer jobs providing health care benefits. According to the U.S. House of Representative Small Business Committee, the loss of health care coverage will be difficult to recoup in the short-term (Frabotta, 2004). Thus, after years and years of skyrocketing health care cost, there is little optimism that cost will decrease. Most people believe that they pay too much

for health care and are looking for the government or industry to make a significant change that will provide a long-term solution.

One of the many challenges that the Government and the Industry have to surmount is provide the public with accurate data on the past and present state of health care in the United States. Looking back in the 1960s, individuals paid 55% of medical cost, which is more than 2.5 times greater than the 20% share they paid in the 1990s (Workforce, 2005). Still, this is considerably higher than what most people pay today. If cost continues to rise unabated, we may again be facing the premiums of the sixties. Statistically, the percentage of premiums paid by workers has not changed over the last 16 years resulting at 16% for single coverage and 28% for family coverage. (Employer Health Benefits: 2004 Annual Survey, 2004). Though the percentages have remained constant, rising cost exceeding inflation has made health care cost painful for both small business owners and their employees.

The rising cost of health care outpacing inflation, has been a hindrance to industry and government efforts to provide affordable health care to all. Small businesses have always seen the value in providing health care benefits to employees but have not consistently been able to do so. The National Association for the Self-Employed (NASE) has reported that 7 out of 10 owners of the smallest businesses do not provide any type of health care coverage to eligible employees. Costs are cited as the chief reason for this trend. For example, a small business owner in Arlington, VA, who could not afford coverage for her 10 employees, eventually signed up with a HMO, paying \$3,300 per worker (Epstein, 2002).

The negative impact of staggering health care costs produces the challenge for small firms to maintain profits and margins. Unfortunately, for many owners, the options are to reduce or cut-off benefits or shift cost to employees. When employees rank benefits by value,

health coverage is No. 1 (Tobacco, 2005). Health care benefits may become as important as salary when choosing careers and job opportunities. The drain that cost places on profits and margins is a major factor that determines if a health plan is offered or not.

Business owners believe that the state of the economy is a crucial factor in determining if they can provide benefits to workers. If the economy is bad, profits will suffer and owners will do whatever is necessary to survive. Reductions in salaries and benefits are often the first casualties of a bad economy. In today's recovering economy, health care cost were cited by small businesses as the single most important issue that owners felt would affect them this year. Out of the owners surveyed by IPA SBRB, 185 said this would have the greatest impact in 2005 (IPA SBRB Study: Health care Coverage an Important Assets to Small Businesses: Two-Thirds Support Employees by Providing Health Insurance, 2005). With many small businesses wanting to provide health care plans but unable to afford the benefits, they look for other alternatives.

The most common method to reduce the cost of health care would be requiring employees to pay a percentage of the premium. Employees have become accustomed to contributing a portion of their salary to a health care plan and are very familiar with having to make co-payments on certain medical supplies or procedures. Among small business offering health insurance, 34% pay the entire premium, 36% pay more than half and 29% pay up to half of the premium. (IPA SBRB Study: Health care Coverage Important Assets to Small Businesses: Two-Thirds Support Employees by Providing Health Insurance, 2005). Other options include plans with high deductibles that incorporate co-insurance as well as higher co-pays. Today on average, employees now pay 27% of family health plans (Tobacco, 2005).

Consumer Driven Health Plans (CDHPs), Health Savings Accounts (HSA), Health Reimbursement Accounts (HRA), and Association Health Plans (AHPs) are other methods available to help small business owners control health care cost. CDHPs cut premium cost by matching a high-deductible managed care plan with an employer-funded health care reimbursement account.

The Medicare Prescription Drug Improvement and Modernization Act of 2003 established HSA. This legislation allows employers and employees to make pre-tax contributions into a savings account that is designed specifically for medical costs. Monies not used can be transferred from year to year, and employees who switch jobs can take a HSA with them. Money from the account can even be used tax-free after retirement as long as it is being applied toward eligible medical costs. HSAs must be combined with high-deductible health insurance (with a deductible of at least \$1,000 for an individual and \$2,000 for families) to be used. Jamie L. Amaral, national director of health research and development at the National Federation of Independent Business (NFIB), says that small business owners can use HSAs to keep their overall health plan spending down, and they can get a tax benefit as well since the money that is contributed to HSAs is not taxed (Sinnott, 2004).

Health Reimbursement Accounts (HRA) features employer-paid health reimbursement accounts and incentives for employees to be better consumers of health care. The employer pays for a HRA account and can draw on this account for reimbursement of their health care costs. Once the account is exhausted, other health care costs can be covered by insurance. Unused balances in these accounts can be carried over for use in the next year (Sinnott, 2004).

The Association Health Plans (AHPs) are still awaiting approval by the U.S. Senate. This plan will allow small businesses to pool their employees through associations in an effort to

negotiate lower premiums as a group. AHPs could save small business about 25 to 30% due to possible purchasing, according to a preliminary assessment by the Congressional Budget Office (Frabotta, 2004). AHPs can also reduce health insurance costs by 15 to 30% by allowing small businesses to join to obtain the same economies of scale, purchasing clout, and administrative efficiencies now available to employees in large employer and union health plans (Washington, 2005).

In 2003, union workers at General Electric went on strike to protest that companies plan to shift more cost liability of its health care to workers. Benefit experts believe that unions at other companies may follow suit, as workers are asked to shoulder a greater percentage of medical benefit costs. (Taup, 2003) Large corporations have the ability to negotiate health plans because of the large dollar amount they pay on an annual basis however, small business owners have yet been able to form a consolidate effort to represent large groups of small businesses across state lines.

Robin Silverman, a business owner with 14 employees and \$1.1 million in sales, was able to reduce her small business health care cost by changing to a zero-deductible option that pays 70% of medical costs. The company cut its health care cost by about one-third, from \$2,500 per month to \$1700 a month (McCrea, 2002).

As the cost of health insurance increases by double digits for the past few years, the small business employer is faced with the hard choice of cutting coverage, increasing personal contributions or covering the cost from the revenue. According to a study by the Policy Journal of the Health Sphere released in February 2005, 46% of the 1.5 million filers for personal bankruptcy were due to uncovered medical expenses. In the survey, 59% missed needed doctor visits, 43% of the families reported services were shut off, and 21% of families went without

food due to the overwhelming medical expenses. The average out-of-pocket expenses for medical bankruptcies were \$11,854 (Himmelstein, 2005).

In summary, providing affordable health care to employees is the supreme challenge for small businesses to conquer. Small firms recognize the importance of offering health benefits to compete with larger organizations to remain successful. The perspective taken from this research was to examine and determine answers to health care questions and provide findings and results about the health care cost industry relative to small businesses.

Our findings conclude that over the history of the health care industry, small businesses have been unable to provide health care and have consistently produced employees who are uninsured. Fortunately, the federal government interceded on their behalf and made a decision to develop programs and regulations to assist the uninsured to acquire health care opportunities. Medicaid, HMOs and PPOs are examples of government-regulated programs that give small businesses health care options to their employees. Small businesses can also allow employees to pay a percentage of the insurance premium or offer CDHPs, HSAs, HRAs, and AHPs plans to control health care cost.

Small businesses recognize the importance of offering health care but are forced to cut back on benefit plans or discontinue offering them at all. For most small firms, the economic state of the country is an important factor in determining if businesses can provide benefits to workers. When the economy declines, a reduction in earnings and benefits normally pursues. This decrease in benefits and wages create a stumbling block for business owners to work through. The fact remains that the continual cost of health care has driven most small businesses to withdraw health care benefits for their employees to maintain profits. By offering other alternatives to employees small businesses have been able to sustain through the health

care crisis. The benefit of providing health care is imperative to small businesses and is a contributing factor to the prosperity of America's economy.

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