A Helping Hand For New York's Small Businesses

Health Insurance Tax Credits

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A Report from Families USA and Small Business Majority

Families USA is the national organization for health care consumers. It is nonprofit and nonpartisan, and its mission is the achievement of high-quality, affordable health care for all Americans. Since 1982, Families USA has engaged in research and public education to promote the expansion of health coverage for uninsured people, especially low-income working families; to rein in health care costs; and to make other improvements in the health care system.

www.familiesusa.org

Small Business Majority is a national nonprofit, nonpartisan organization, founded and run by small business owners, that brings the voices of America's 28 million small businesses to the public policy table. It is focused on solving the single biggest problem facing small businesses: the skyrocketing cost of health care. Small Business Majority uses nonpartisan scientific research to understand and represent the interests and needs of all small businesses, from sole proprietors to 100-person companies.

www.smallbusinessmajority.org

Cover Design: Nancy Magill, Families USA

Introduction

Small businesses are the backbone of New York's economy. Across the state, there are nearly 350,000 businesses that employ 25 or fewer workers. They're your local diner, the hardware store down the street, and the mechanic in your neighborhood.

While small businesses have been serving us, however, our health care system has been failing them, making it difficult—if not impossible—to provide their workers with quality, affordable health coverage. Particularly for the smallest businesses, the cost of providing health insurance can be prohibitively expensive, especially in these tough economic times. Health care costs are daunting for everyone, but they are even more out of reach for small businesses: In 2008, employers with fewer than 10 workers paid $350 more for each employee's health insurance, on average, than firms with 50 or more workers. And the coverage they got for that extra $350 may not have been as comprehensive as what a larger employer got for a lower price.[1]

The result is that, the smaller the business, the less likely it is to be able to insure its workers. In 2009, less than half (46 percent) of businesses that employed three to nine workers offered coverage to their employees. Among small businesses with 10 to 24 workers, the offer rate increased to 72 percent, while almost all businesses with 50 or more workers (more than 95 percent) offered coverage to their employees.[2]

In the Patient Protection and Affordable Care Act, Congress and the President recognized that small businesses, particularly those with 10 or fewer workers, struggle to provide health insurance for their workers, and that some cannot afford to provide it at all. Legislators therefore included many provisions in the law to help small employers and their workers obtain high-quality, affordable coverage. One of these important provisions is a program to provide tax credits that small employers can use toward the purchase of health insurance for their workers.

Starting this year, businesses with fewer than 25 workers and average wages of less than $50,000 will be eligible to receive a tax credit for the health insurance that they provide for their employees. The value of the credit this year (and until 2014) is up to 35 percent of the employer's costs for employee coverage (and up to 25 percent of the costs for nonprofit employers). The smallest firms with the lowest wages—those that employ 10 or fewer workers who earn an average wage of less than $25,000—are eligible for the full 35 percent tax credit (or 25 percent for nonprofits). From there, the size of the credit will phase out on a sliding scale. Congress designed this system with the intent of providing the greatest help to those businesses most in need—the smallest employers who face the highest premiums and are the least able to offer coverage to their workers.

For this study, Families USA and Small Business Majority commissioned The Lewin Group to analyze data on business sizes and wages from the U.S. Agency for Health Care Research and Quality and the U.S. Census Bureau in order to quantify the number of employers who will be eligible to receive help from this provision. Lewin was then asked to use its Health Benefits Simulation Model to quantify the number of employers who will be eligible for the *maximum* tax credit.

Key Findings

- Approximately 285,000 New York small businesses will be eligible to receive a tax credit for the purchase of employee health insurance in 2010 (see Table 1).
- More than eight out of 10 small businesses[3] in New York (81.6 percent) will be eligible for a tax credit in 2010 (see Table 1).

Table 1.
Small Businesses in New York That Are Eligible for Premium Tax Credits in 2010

State	Number of Small Businesses*	Small Businesses Eligible for a Premium Credit	
		Number	Percent
New York	349,500	285,000	81.6%

Source: Estimates developed by The Lewin Group for Families USA and Small Business Majority. For more detail, see the Methodology on page 6.

* Small businesses are defined as those firms with 25 or fewer employees.

- Approximately 78,300 New York small businesses will be eligible to receive the *maximum* tax credit in 2010 (see Table 2).

Table 2.
Small Businesses in New York That Are Eligible for The *Maximum* Premium Tax Credits in 2010

State	Number of Businesses
New York	78,300

Source: Estimates developed by The Lewin Group for Families USA and Small Business Majority. For more detail, see the Methodology on page 6.

Discussion

How the Tax Credit Works

Small employers (those with up to 25 workers) who offer coverage can receive a tax credit for up to 35 percent (or 25 percent for nonprofits) of the average cost of a small group plan in the state, starting in the 2010 tax year. To qualify for the tax credits, businesses must cover at least 50 percent of each employee's health insurance premiums. In 2014, once the state health insurance exchanges for small businesses and individuals are up and running, small employers will be eligible for tax credits of up to 50 percent (or 35 percent for nonprofits) of the costs of covering their workers through the exchanges.

The eligibility limits for employers with up to 25 workers include the hours of part-time employees, who will be counted as "full-time equivalents." For example, two half-time workers count as one full-time worker for the purpose of calculating tax credit eligibility. This means that part-time workers, who are more likely to be uninsured than their full-time counterparts,[4] may finally be able to obtain job-based health insurance with the help of the small business tax credits.

A Summary of Other Health Reform Provisions That Help Small Businesses and Their Workers

The tax credits for purchasing coverage are just one of many important provisions in the Patient Protection and Affordable Care Act that will help make high-quality health coverage more affordable and accessible for New York's small businesses. Some of the other provisions that will improve our health care system for small businesses include the following:

- **Health Insurance Exchanges for Purchasing Coverage**

  Starting in 2014, the state health insurance exchanges will be up and running, creating a new marketplace where employers will be able to purchase high-quality, affordable health plans for their workers. In the exchanges, small employers will be able to view comparable and clear information on benefits and costs for each insurance plan so that they can find the policy that best meets the needs of their workers. This simplified system of shopping for and enrolling in health coverage will ease administrative burdens on small employers who may have limited staff and time for searching for health coverage.

In addition, health plans that sell coverage through the exchanges will have to meet a number of consumer protection and quality standards, and plans that impose unreasonable rate hikes in the years before 2014 may not be permitted to sell coverage through the exchanges. These features will make the exchanges a valuable new resource for small employers that are looking for high-quality, affordable coverage for their workers.

- **An Internet Web Portal for Health Insurance Information**

  Starting in July 2010, small business owners will be able to view all of the existing options for small group coverage in their state on a user-friendly website. The website will link to materials on all available health plans, and, starting in October 2010, it will include standardized information on plan benefits and costs so that small employers can make apples-to-apples comparisons while shopping for coverage for their workers. The site will include information on the small business tax credits as well.

- **Medical Loss Ratio Requirements**

  Under health reform, a medical loss ratio is defined as the percentage of premium dollars that an insurance company spends on medical care and quality improvement efforts, as opposed to administrative costs or profits. Health plans for small businesses will be required to spend at least 80 percent of the premium dollars that they receive on providing medical care and improving health care quality for enrollees, instead of on administration, marketing, and profits. Since health plans for small employers generally spend more on non-medical costs than those for larger employers,[5] medical loss ratio requirements are especially important in the small group market. They will ensure that employers and their workers receive good value for their money and that rates are not unreasonably increased to pad insurers' bottom lines.

- **An Exemption from Employer Responsibility Requirements**

  There are no employer mandates in the law, and no employer responsibility requirements at all for businesses with fewer than 50 workers. Starting in 2014, businesses with at least 50 workers that do not offer coverage (less than 5 percent of firms of this size)[6] or that offer only unaffordable coverage to their workers will be assessed a penalty if one or more of their workers receives a federal tax credit to purchase coverage in the exchange.

Conclusion

Targeting those businesses that are most in need, the small business tax credits and other critical provisions of the Patient Protection and Affordable Care Act will help make health coverage affordable and accessible for New York's small businesses. Employers who have postponed wage increases and sacrificed business growth in order to keep their workers covered, and those who have been forced to drop coverage altogether due to cost, will finally be able to provide their workers with the peace of mind that comes with health insurance. Not only will the credits ease the health insurance burdens experienced by existing small businesses, but they may spur the growth of new small businesses by allaying the concerns about health coverage that have discouraged some from starting a business until now.

The small business tax credits and the many other provisions of the Patient Protection and Affordable Care Act that will improve the health care system will help small businesses and their workers to be healthy and productive, both now and in the future.

[1] Agency for Healthcare Research and Quality, *Medical Expenditure Panel Survey-Insurance Component, 2008, Table II.C.1: Average Total Single Premium (in Dollars) Per Enrolled Employee at Private-Sector Establishments that Offer Health Insurance by Firm Size and State: United States, 2008* (Washington: AHRQ, 2008); Michelle M. Doty, Sara R. Collins, Sheila D. Rustgi, and Jennifer L. Nicholson, *Out of Options: Why So Many Workers in Small Businesses Lack Affordable Health Insurance, and How Health Care Reform Can Help* (New York: The Commonwealth Fund, September 2009).

[2] Kaiser Family Foundation and Health Research Educational Trust, *Employer Health Benefits: 2009 Annual Survey* (Washington: Kaiser Family Foundation, 2009).

[3] For the purposes of this study, small businesses are defined as those with 25 or fewer workers. For more information, please see the Methodology on page 6.

[4] U.S. Census Bureau, *Income, Poverty, and Health Insurance Coverage in the United States: 2008* (Washington: U.S. Census Bureau, September 2009), available online at http://www.census.gov/prod/2009pubs/p60-236.pdf.

[5] The Lewin Group, *A Path to a High Performance U.S. Health Care System: Technical Documentation* (Washington: The Lewin Group, February 19, 2009), available online at http://www.lewin.com/content/publications/4010.pdf.

[6] Kaiser Family Foundation and Health Research Educational Trust, op. cit.

Methodology

For this study, Families USA and Small Business Majority commissioned The Lewin Group to analyze data on business sizes and wages from the U.S. Agency for Health Care Research and Quality and the U.S. Census Bureau in order to quantify the number of employers who will be eligible to receive help from this provision. Lewin was then asked to use its Health Benefits Simulation Model to quantify the number of employers who will be eligible for the *maximum* tax credit.

An estimate of the number of small businesses (those with 25 workers and fewer) with average payrolls of less than $50,000 forms the foundation of this analysis. These data were compiled for each state by staff at the U.S. Agency for Healthcare Research and Quality (AHRQ) using the Medical Expenditure Panel Survey (MEPS) Insurance Component (IC) database for 2008. The MEPS-IC is a sample of about 39,000 businesses that is drawn from the U.S. Census Bureau's Business Register. The Census Bureau conducts a health insurance survey of the sampled businesses, and it reports about an 80 percent response rate to the survey. The Business Register includes sole proprietors, but such businesses are excluded from the sample for the MEPS-IC.

The MEPS-IC reports the number of paid employees, regardless of their work status (e.g. full-time, part-time, temporary, seasonal, etc.), toward the count of employees in the firm. There is no standard definition of part-time and full-time employees, so this determination is left up to each business. Also, the owner of the firm is counted as an employee.

The MEPS-IC survey does not collect payroll or average wage data. Therefore, the average wage information in the MEPS-IC database was populated using total payroll and the number of employees that was reported in the Business Register. As described above, counts of employees include full-time, part-time, temporary, and seasonal workers, as well as the business owners.

The small employer tax credit in the health reform law bases the size of the firm on the number of full-time equivalents (FTEs). Therefore, the definitions used in this analysis likely result in a conservative estimate of the number of firms that meet the size criteria. In addition, this methodology makes the denominator in the calculation of average wages larger, and it therefore might inflate the estimate of the number of eligible firms by capturing more firms that meet the average wage criteria. It is also important to note that the law limits eligibility for the credit to firms with fewer than 25 FTEs, while these estimates are for firms with 25 or fewer employees. Also, in the infrequent instances where a firm with 25 or fewer employees has more than one location, this analysis counted such firms as two separate establishments.

Using the data provided by AHRQ, The Lewin Group estimated the number of these firms that had 10 or fewer workers. Lewin based this split on the proportion of all small firms, regardless of payroll, with 10 or fewer workers and those with 11 to 25 workers. This calculation was done separately for each state.

For both firm size groups, Lewin estimated the number of firms with average annual payrolls below $25,000 using Lewin's Health Benefits Simulation Model (HBSM). The HBSM creates "synthetic firms" where workers from the MEPS household survey are matched to employers from a Robert Wood Johnson employer survey based on the characteristics of the workers that are reported for each employer, such as age, sex, wage level, full-time/part-time status, etc. Using the annual wages that are reported in the MEPS household survey for workers matched to the firm, Lewin calculated an average annual payroll for each "synthetic firm." Lewin used these data to estimate the number of firms with 10 or fewer workers and average annual payrolls of less than $25,000 and less than $50,000. Lewin then calculated the percentage of small firms with average payrolls under $50,000 that also had average payrolls of less than $25,000. Lewin applied this percentage to the number of employers from the MEPS data with average payrolls of less than $50,000 in order to estimate the number of firms with average payrolls of less than $25,000. Lewin then did the same calculations for firms with 11 to 25 workers.

Finally, Lewin trended the estimated number of small, low-wage firms from 2008 to 2010 based on the historical growth rate from 2003 to 2008 for all small firms. Lewin did this separately for each state for firms with 10 or fewer workers and then for firms with 11-25 workers.

Acknowledgments

This report was written by:

Claire McAndrew
Health Policy Analyst
Families USA

and

Kathleen Stoll
Deputy Executive Director, Director of Health Policy
Families USA

The following Families USA staff assisted in the preparation of this report:

Ron Pollack, Executive Director

Kim Bailey, Senior Health Policy Analyst

Peggy Denker, Director of Publications

Ingrid VanTuinen, Senior Editor

Nancy Magill, Senior Graphic Designer

The following Small Business Majority staff assisted in the preparation of this report:

John Arensmeyer, Founder and CEO

Terry Gardiner, National Policy Director

Rachel Radway, Communications Director

Data analysis provided by:

The Lewin Group

Families USA
www.familiesusa.org

Small Business Majority
www.smallbusinessmajority.org

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