

## **Right Balance for Small Business in Health Reform** *In Iowa, Targeted Credits Offer Business Benefits, Employees Access*

**By Andrew Cannon**

A largely silent but very active movement within state and federal agencies is preparing for the full implementation of the Patient Protection and Affordable Care Act (PPACA). Though the new health reform law does not fully go into effect until 2014, dozens of agencies within the federal government are complying with the law's provisions to ensure that the law's implementation has the maximum impact of making insurance affordable to all.

One provision that takes immediate effect helps small businesses provide health insurance to their employees. The PPACA provides small businesses that pay at least half of their employees' health insurance premium with tax credits of up to 35 percent of the premium cost.

### **Background**

Small businesses and their employees have been disproportionately hurt by the rapid increase in health insurance premiums. Larger firms are able to spread the risk of insuring their employees across a larger pool. In addition, their size affords them bargaining power that smaller businesses lack.

A 2006 study found that the smallest firms pay considerably higher health insurance premiums than large firms. Premiums for firms with nine or fewer employees are 18 percent higher than those of large firms (those with 1,000 or more employees), and firms with 10 to 24 employees pay 10 percent more in premiums than large firms.<sup>1</sup>

In addition, premiums have risen significantly for all firms over the past 10 years. In 2000, Iowa companies reported an average premium of \$6,487 for a family health insurance plan. By 2008, the average family health insurance plan in Iowa had risen by more than \$4,400.<sup>2</sup>

Rising premiums have made health insurance a benefit that many smaller employers can simply no longer afford to offer employees. While larger firms have continued to offer health insurance to employees at an unchanged rate since 2000, the percentage of smaller firms offering health insurance benefits has declined. From 2000 to 2008, there was a drop of three to four percentage points in firms with 100 or fewer employees that offered health insurance.<sup>3</sup>

As a result, employees of small firms are less likely to get their health insurance through an employer. In 2008, about two-thirds of Iowa firms with between 10 and 24 employees offered health insurance to employees and only a third of Iowa firms with 10 or fewer employees offered health insurance.<sup>4</sup> By comparison, more than 91 percent of Iowa firms with 25 or more employees offered health insurance to their employees.<sup>5</sup>

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## Health Insurance, Small Businesses and the PPACA

The PPACA aims to reduce this disparity between 2010 and 2013 by offering highly targeted tax credits to small businesses that pay for at least half of their employees' health insurance premiums.

Eligibility for the full credit of 35 percent of an employer's contribution to employee health insurance is limited by both the number of full-time equivalent employees and the average taxable wages the employer pays.\* Firms with 10 or fewer full-time equivalent employees with an average wage per employee of \$25,000 or less are eligible for the full credit. Firms with more than 10 employees or average wages higher than \$25,000 are eligible for tax credits on a declining scale. At 25 employees, or an average wage of \$50,000, credit eligibility disappears. Table 1 shows the eligibility scale for the small business tax credits.

For example, if a small business that qualifies for the maximum credit offers its employees an individual health insurance plan with an average premium of \$4,500, and pays \$2,500 of the cost, the employer would receive a tax credit of \$875 per full-time employee.

A firm with eight full-time employees and eight part-time employees who work 20 hours a week, for

instance, would not be eligible for the full 35 percent credit, even if the average wage was \$25,000 or less. Under the PPACA tax credit guidelines, the example firm has the equivalent of 12 full-time employees. Such a firm would be eligible for a 30 percent credit.<sup>6</sup>

In 2014, when full implementation begins with the creation of state-based health insurance exchanges, or marketplaces for individuals and small businesses to purchase insurance, small businesses will be eligible for a maximum credit of 50 percent of the employer's contribution to the premium.<sup>†</sup>

**Table 1. Small Business Tax Credit Eligibility as a Percent of Employee Contribution**

# of Employees	Average Wage						
	Up to \$25,000	\$30,000	\$35,000	\$40,000	\$45,000	\$50,000	
Up to 10	35%	28%	21%	14%	7%	0%	
11	33%	26%	19%	12%	5%	0%	
12	30%	23%	16%	9%	2%	0%	
13	28%	21%	14%	7%	0%	0%	
14	26%	19%	12%	5%	0%	0%	
15	23%	16%	9%	2%	0%	0%	
16	21%	14%	7%	0%	0%	0%	
17	19%	12%	5%	0%	0%	0%	
18	16%	9%	2%	0%	0%	0%	
19	14%	7%	0%	0%	0%	0%	
20	12%	5%	0%	0%	0%	0%	
21	9%	2%	0%	0%	0%	0%	
22	7%	0%	0%	0%	0%	0%	
23	5%	0%	0%	0%	0%	0%	
24	2%	0%	0%	0%	0%	0%	
25	0%	0%	0%	0%	0%	0%	

Source: Congressional Research Service

\* Nonprofit organizations that meet the payroll and employee requirements will receive a 25 percent non-refundable credit, which can be used to reduce the organizations' income and Medicare tax withholdings.  
<sup>†</sup> Beginning in 2014, nonprofit organizations meeting the payroll and employee requirements will receive a 35 percent nonrefundable tax credit, again reducing the organizations' income and Medicare tax withholdings.

## **Iowa Small Businesses**

Firms with 20 or fewer employees account for over 85 percent of Iowa's private establishments.<sup>7</sup> Over 56,400 small businesses in Iowa have 20 or fewer employees. Depending on the average wage within the firm, these businesses may be eligible for the PPACA health insurance tax credit.

These targeted tax credits will provide a significant benefit to Iowa's qualifying small businesses that already pay the majority of costs for health coverage for their workers. There also may be some impact upon firms that have not been able to provide employees with health insurance because of its cost and now decide to do so. Even with the federal incentive, however, health insurance costs are likely to weigh against many small employers picking up coverage they do not now provide. The experience with state small business insurance incentive programs is that they generally serve a very small share of the businesses that are potentially eligible, with particular challenges to reaching those predominantly employing lower-wage employees.

Still, employers that do offer health coverage may benefit not only from the federal funding, but also from having a more stable workforce. Nearly three-quarters of workers in a national survey stated that employer-sponsored health insurance was a major factor in their decision to take a job.<sup>8</sup> Similarly, about 80 percent business executives in one national survey described the provision of health insurance benefits as "extremely" or "very important" in job retention.<sup>9</sup>

Overall, the provision of this credit will make health insurance provision by employers less costly. Some additional small business employees, as a result of the tax credit, may have health insurance offered by their employers, and small businesses currently offering coverage will be less likely to drop that coverage. Nearly 60 percent of Iowa's uninsured population is employed,<sup>10</sup> so the credit will have some impact on the number of uninsured workers within Iowa.

Iowa's small businesses and their employees stand to gain in obtaining affordable health insurance through this and other provisions in PPACA. Though the major provisions of health reform do not take effect until 2014, premium tax credits already have taken effect.

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<sup>1</sup> Jon Gable, Roland McDevitt, Laura Gandolfo, et. al. "Generosity and Adjusted Premiums in Job-Based Insurance: Hawaii is Up, Wyoming is Down," *Health Affairs*. May/June 2006.

<sup>2</sup> Agency for Healthcare Research and Quality. *Average total family premium in dollars per enrolled employee at private-sector establishments that offer health insurance by firm size and state* (Table II.D.1), years 1996-2008. Medical Expenditure Panel Survey Insurance Component Tables. Generated using MEPSnet/IC. Accessed June 15, 2010. <[http://www.meps.ahrq.gov/mepsweb/data\\_stats/MEPSnetIC.jsp](http://www.meps.ahrq.gov/mepsweb/data_stats/MEPSnetIC.jsp)>.

<sup>3</sup> AHRQ. *Percent of private-sector establishments that offer health insurance by firm size and selected characteristics* (Table I.A.2), years 1996-2008.

<sup>4</sup> AHRQ. *Percent of private-sector establishments that offer health insurance by firm size and state* (Table II.A.2), years 1996-2008.

<sup>5</sup> AHRQ MEPS, Table II.A.2.

<sup>6</sup> Chris L. Peterson and Hinda Chaikind, "Summary of Small Business Health Insurance Tax Credit Under PPACA (P.L. 111-148). *Congressional Research Service*. April 5, 2010.

<sup>7</sup> Small Business Administration, Office of Advocacy. *Employer Firms, Establishments, Employment, Annual Payroll and Estimated Receipts by Firm Size, and State, 2007*. <[http://www.sba.gov/advo/research/st\\_07.pdf](http://www.sba.gov/advo/research/st_07.pdf)>..

<sup>8</sup> Ellen O'Brien, "Employers' Benefits from Workers' Health Insurance," *the Milbank Quarterly*, Vol. 81, No. 1 (2003).

<sup>9</sup> Rachel Christensen, Paul Fronstin, Karl Polzer, and Ray Werntz, "Employer Attitudes Affecting and Practices Affecting Health Benefits and the Uninsured: Issue Brief No. 250." *Employee Benefits Research Institute*. October 2002. <<http://www.ebri.org/pdf/briefspdf/1002ib.pdf>>.

<sup>10</sup> Steven Ruggles, J. Trent Alexander, Katie Genadek, Ronald Goeken, Matthew B. Schroeder, and Matthew Sobek. *Integrated Public Use Microdata Series: Version 5.0* [Machine-readable database]. Minneapolis: University of Minnesota, 2010.

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