



Small Businesses and the Affordable Care Act

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The Patient Protection and Affordable Care Act, referred to as the Affordable Care Act (ACA), is the national health care reform adopted by Congress and signed into law by President Obama on March 23, 2010. The ACA provides small businesses — *both for-profit and nonprofit organizations* — immediate assistance to help purchase or maintain health insurance for their employees. Over time the ACA will make purchasing health insurance simpler and will reduce administrative costs.

Currently, small businesses pay almost 20 percent more than large businesses for the same health insurance policy.¹ An insurance company’s administrative costs for selling policies to large employers are much lower than the costs for policies for small employers – 15 percent of the premium for businesses with 50 to 100 employees, compared to 35 percent for businesses with two to four employees.²

Consequently, small businesses are less likely to offer health insurance to their employees. Only 59 percent of employers with 3 to 9 employees offer health insurance benefits to their employees, compared to 96 percent of employers with more than 50 employees that offer this benefit.³

Clearly, small businesses, including nonprofits, struggle to provide health insurance to their employees. The ACA targets relief to these employers in a number of ways.

First, beginning in 2010 small employers qualify for tax credits of up to 35 percent of the employer share of premium costs, which makes their premiums more affordable. Employers with 10 or fewer employees and average wages of \$25,000 or less qualify for the maximum tax credit of 35 percent of the

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employer's contribution to premiums. This tax credit is phased out on a sliding scale to larger employers that pay higher salaries—those with fewer than 25 employees and average wages of less than \$50,000. Employers who pay at least 50 percent of the total premium are eligible for the tax credit. Sole proprietors are not eligible for these tax credits.

See Chart 1 on page 4 for small business tax credit rates based on the number of employees and average salaries. Non-profit organizations qualify under the same criteria as for-profits, except their tax credit is capped at 25 percent of the employer's contribution. Since non-profit organizations do not pay income tax, their payroll taxes are reduced in order to receive the tax credit.

During Phase II of health reform (2014 and beyond), small businesses that purchase health insurance through a health exchange will be eligible for tax credits. Most of the same criteria for the tax credits in Phase I apply to the tax credits in Phase II, although the maximum percentage of tax credits increases from 35 percent to 50 percent of the employer's premium contribution. Again, this applies to employers that pay at least 50 percent of the total premium. *Tax credits in Phase II can only be taken for two years.* The maximum tax credit that non-profit organizations can receive under Phase II is 35 percent.

Second, small businesses with fewer than 50 employees will not pay a penalty for not offering health insurance to their employees. Beginning in 2014, businesses with more than 50 employees face a penalty if they do not offer health insurance benefits *and* one or more of their employees receive a tax credit for purchasing health insurance. Businesses with 50 or fewer employees are exempt from this employer responsibility. Ninety-six percent of businesses with more than 50 employees already provide insurance to their employees. This employer responsibility provision will not impact the vast majority of these larger businesses.

Third, in 2012 insurance companies with administrative costs that exceed 20 percent will have to provide a rebate to their small business customers. A "medical loss ratio" of 80 percent means that the insurance company is spending 80 percent of the premium they collect on medical claims and quality improvements and 20 percent on administrative costs and profit. Beginning in 2011, insurance companies will have to report their medical loss ratio to the US Department of Health and Human Services (HHS). HHS will publish these medical loss ratios so businesses and consumers will have information on what insurance companies are spending on paying claims and improving quality and what is spent on administrative costs. Beginning in 2012, insurance companies must have at least an 80 percent medical loss ratio or provide a rebate to their small business customers. This requirement will provide a strong incentive to insurance companies to be more efficient in the policies they sell to small businesses.

Fourth, beginning in 2014 small businesses will qualify to purchase health insurance in the health exchange. A health insurance exchange is a marketplace where individuals and small businesses can shop for health insurance, compare plans and choose the ones best suited to their needs. This is the most important provision in health care reform, because it will simplify the process of purchasing health insurance, promote competition and consumer choice, and lower costs.

Small businesses will be able to use the tax credits listed above to purchase four different levels of

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plans, where the employee's share of the cost will range from 10 to 40 percent. If a small business does not offer health insurance, its employees may be eligible for help with health insurance in one of two ways:

Low-wage employees under age 65 will be eligible for Medicaid if their family income is below 133 percent of the federal poverty level, or FPL (currently \$14,400 for a single person and \$24,400 for a family of three).

Employees who purchase health insurance in the exchange as individuals will receive tax credits on a sliding scale if their income is between 100 percent of FPL up to 400 percent of the FPL (currently about \$43,300 for a single person and \$73,000 for a family of three).

Fifth, beginning in 2014 insurance policies may no longer be limited or denied based on pre-existing conditions. Insurance companies that sell policies after January 1, 2014 will be prohibited from: charging higher premiums if their employees have a pre-existing condition; selling a policy that covers everything but the pre-existing condition; or refusing to sell a policy to a small employer because one or more of their employees has a pre-existing condition. Many small businesses have been charged significantly higher premiums after one of their employees has a serious illness. This practice ends in 2014.

Additional Paperwork: Not all of the provisions of the ACA are positive for small businesses. Starting in 2012 both small and large businesses will be required to file 1099-MISC forms with the IRS for any vendor who is paid more than \$600 a year. This is a significant change in the number of 1099-MISC forms that businesses will be required to report. Previous IRS rules exempted payments made to corporations. And even when payments were made to unincorporated organizations, payments made for goods and property (as opposed to services) were also exempt.

Both Democrats and Republicans in Congress agree that, at a minimum, businesses with fewer than 25 employees should be exempt from this expanded reporting requirement. However, Congress has not been able to agree on how to replace the revenues that are projected to be generated as a result of this increased reporting requirement. WVAHC fully expects that small businesses will be exempt from it prior to this provision going into effect. However, at the time of printing this report (October 2010) this issue has not been resolved.

In conclusion, the ACA recognizes the fragile nature of small businesses' ability to provide their employees with health insurance benefits. The Act exempts small businesses from the employer responsibility that is applied to employers with more than 50 employees. The ACA also provides very small employers — principally those with 2 to 10 employees, who traditionally have the hardest time affording insurance — with tax credits to make health insurance more affordable; provides small businesses with protection against high administrative insurance costs; allows, beginning in 2014, small businesses to participate in the health exchange to make purchasing health insurance more transparent and with lower costs; and small businesses will be protected from increased premiums because one or more of their employees becomes sick and uses their health insurance. In short, the ACA protects and assists small businesses in their efforts to provide their employees with health insurance benefits.

**Table 1:
Percentage of the Employer’s Premium that Will
Be paid by the Tax Credits in 2010 through 2013.⁴**

These tax credits apply to for-profit organizations between 2010 through 2013 and to nonprofit organizations beginning in 2014. The rate for nonprofit organizations from 2010 through 2013 (when the maximum rate is 25 percent) is projected to be 28.6 percent lower than the percentages listed below. In 2014 and beyond, for-profit organizations’ rates are projected to be 42 percent higher than the percentages listed below (when the maximum rate increases to 50 percent).

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

(Endnotes)

1 Jon Gabel, et. al., *Generosity and Adjusted Premiums in Job-Based Insurance*, Health Affairs, May/June 2006 25(3):832-843.

2 Sara Collins, et. al., *Realizing Health Reform’s Potential: Small Businesses and the Affordable Care Act*, Commonwealth Fund, September 2010. Accessed at <http://www.commonwealthfund.org/Content/Publications/Issue-Briefs/2010/Sep/Small-Businesses.aspx> on September 6, 2010.

3 Kaiser Family Foundation and Health Research and Education Trust, *Employer Health Benefits, 2010 Annual Survey*, September 2010. Accessed at <http://ehbs.kff.org/> on September 6, 2010.

4 Chris Peterson and Hinda Chaikind, *Summary of Small Business Health Insurance Tax Credit Under the Patient Protection and Affordable Care Act (PPACA)*, Congressional Research Service, April 20, 2010.