CBO TESTIMONY

Statement of
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before the
Committee on Small Business
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Mr. Chairman and Members of the Committee, I am pleased to be here today to discuss the provision of employer-sponsored health insurance by small firms. The Congressional Budget Office (CBO) recently completed a paper on that topic entitled *Increasing Small-Firm Health Insurance Coverage Through Association Health Plans and HealthMarts*. I ask that it be included in the record.

My comments today will focus on three aspects of CBO's report: the circumstances that contribute to the relatively low rates of health insurance coverage through small firms, a summary of the rules that would apply to the proposed association health plans (AHPs) and HealthMarts, and CBO's estimate of how the introduction of AHPs and HealthMarts would affect the number of people insured through small firms and the premiums they face.

Factors Contributing to Lower Rates of Coverage Through Small Firms

Employees of small firms are less likely to have health insurance than are employees of large firms. For 1996, data from the Medical Expenditure Panel Survey indicate that about 40 percent of employees in small firms—those with fewer than 50 workers—obtained health insurance through their employer. In contrast, almost 70 percent of workers in firms of 100 or more employees obtained coverage through their job.

Several factors appear to play a role in the lower rate of insurance coverage through small employers:

- Workers in small firms, on average, have lower wages and lower family incomes than workers in large firms. As a result, small-firm employees are less able to afford comprehensive health insurance, and less of a tax incentive exists for providing health insurance through their employer.

- Small firms typically face higher costs for providing a given benefit package than do larger firms because of higher administrative expenses per enrollee and less purchasing power.

- Small firms generally purchase insurance that is subject to state benefit mandates and other regulations, which tend to increase average premiums. Firms that self-insure—mostly large firms—are exempted from those state insurance rules by the Employee Retirement Income Security Act (ERISA).

Association Health Plans and HealthMarts

Recent proposals would establish federally certified AHPs and HealthMarts, entities that would offer health plans to participating employers. Those plans would be exempt from most state benefit mandates. Trade, industry, or professional associations that had been in existence for at least three years could sponsor an AHP, which would have to offer its insurance products to all member firms. HealthMarts, in contrast, would have to be available to all small firms in a specific geographic area rather than be offered in conjunction with an association.

Effects of AHPs and HealthMarts on Coverage and Premiums

To explore the effects of AHPs and HealthMarts, CBO constructed an analytical model using assumptions based on the relevant economics literature. We estimate that about

4.6 million small-firm employees and their dependents would receive coverage through the new insurance vehicles, but most of those individuals would have obtained insurance even if current law remained unchanged. On balance, about 330,000 more people would be covered through small-firm employment than would otherwise have been the case. That represents a 1.3 percent increase in coverage through small firms.

Because of lower premiums, some small firms would begin to offer their employees coverage through AHPs and HealthMarts, and others would shift from coverage obtained in the traditionally regulated market to the new entities. Firms that moved to the new plans would, on average, pay premiums that were about 13 percent lower than they would have faced in the traditional market under current regulations. They would be paying less money for less insurance, however, since some of those premium savings would be the result of a less generous benefit package.

Introducing AHPs and HealthMarts would be likely to lead to some selection. For plans that were fully state regulated, the proportion of firms with higher expected health costs would rise after the new AHPs and HealthMarts became established. Consequently, firms remaining in the traditional insurance market would see an average increase in premiums of about 2 percent.

The impact of AHPs and HealthMarts would vary from state to state, depending on the extent of state insurance regulation. In general, states that were more highly regulated would be riper markets for the new entities, as would areas with greater concentrations of small firms. The actual outcome of the proposed legislation would also depend on the activities of the regulatory authorities responsible for AHPs and HealthMarts.