August 18, 1994

To: Jennifer Klein

From: Stephanie Cutter

Subject: SMALL BUSINESS CAPS IN GEPHARDT/MITCHELL

As requested, below are a few paragraphs regarding the small business caps in the Gephardt and Mitchell bills. Please let me know if you have any questions.

> In the Mitchell bill, subsidies for small businesses are based on the wage of the individual employee, not on the average wage of the firm. From 1997 to 2002, employers who expand coverage to all employees within a class -- i.e. part-time or full-time -- will be eligible for subsidies for currently uninsured employees. Firms paying 50 percent or more of the premium receive a subsidy for any amount above eight percent of the newly-insured employee's wages, up to 50 percent of the premium. The self-employed may deduct 50 percent of their health insurance costs. In 2002, a 50-50 employer-individual mandate will go into effect in states with less than 95% coverage. Firms with fewer than 24 employees will be exempted from any requirement to contribute.
>
> The Gephardt bill relies on firm-based rather than individual-based subsidies to relieve the burden on small businesses. In 1999, employers in firms with 100 or fewer employees would be required to contribute to the cost of private health insurance. Employers would be required to contribute 80% of the cost of their employees' premiums, with subsidies for small, low-wage employers. Employers with 50 or fewer workers and average payroll of less than $26,000 would be eligible for a tax credit which would reduce the amount they must contribute toward their workers' premiums. Firms with 25 or fewer employees would be eligible for a maximum subsidy of 50 percent of the employers' share, and firms with 26-50 employees would be eligible for a maximum subsidy of 37.5 percent of the employers' share. The self-employed may deduct 80 percent of their health insurance costs.

THE HOUSE BILL: POLICY ON SMALL BUSINESS

Today, small businesses have a hard time finding affordable insurance and offering their employees any choice of health plans. They are often discriminated against by insurance companies, charged higher prices than large companies, or denied coverage altogether. The House bill contains provisions to improve small business access to insurance, make sure that insurance is more affordable, and give employees of small businesses the same choices as all other Americans.

I. INCREASED ACCESS

The bill reforms the insurance market to eliminate the policies which have traditionally been used to discriminate against small business.

- *Guaranteed Issue:* Health plans cannot deny coverage to any eligible group.
- *Guaranteed Renewability:* Health plans must renew all eligible groups [i.e., can't drop a company.]
- *Elimination of Pre-Existing Condition Exclusions:* Health plans will not be able to deny coverage for pre-existing conditions.
- *Elimination of Experience Rating:* Health plans will no longer be able to charge small businesses more based on the health status of their employees.

II. SHARED RESPONSIBILITY

- **Shared Responsibility**: In 1999, employers in firms with 100 or fewer employees would be required to contribute to the cost of private health insurance. Employers would be required to contribute 80% of the cost of their employees' premiums, with subsidies for the smallest low-wage employers. [see below]

- **Tax Credits for Smallest Businesses:** Employers with 50 or fewer workers and average payroll of less than $26,000 would be eligible for a tax credit which would reduce the amount they must contribute toward their workers' premiums. Firms with 25 or fewer employees would be eligible for a maximum subsidy of 50 percent of the employers' share, and firms with 26-50 employees would be eligible for a maximum subsidy of 37.5 percent of the employers' share.

III. AFFORDABILITY

- **Purchasing Cooperatives:** Allows states to establishe voluntary or mandatory purchasing cooperatives to increase bargaining power of small businesses. Plans sold through the cooperative would be sold at a community rate.

- **<u>Community Rating</u>:** Pure community rating would apply to health plans sold to groups of 100 or less. That means that everyone pays the same price, and no small business can be charged more because it has old or sick employees. There can be no premium variations based on age in this market.

- **<u>Self Employed Tax Deduction:</u>** The self-employed tax deduction is increased from 25% to 80% of health insurance premiums. This is the amount of the employer contribution that will be required under the proposal.

IV. <u>EXPANDED CHOICES</u>

Small employers would have several choices of insurance for their employees. They could:

- Offer a minimum of two private insurance plans -- a fee-for-service and a managed care plan.
- Voluntarily enroll their employees in <u>Medicare Part C</u> -- which will offer at least a fee-for-service health care plan -- with unlimited doctor choice -- and a managed care plan.
- Join a voluntary purchasing alliance to consolidate their bargaining power with other businesses to get the most choices and the lowest prices.
- Offer a Medical Savings Account which would receive special tax treatment.
- Employees of small firms (fewer than 100 employees) that offer private coverage could choose coverage under a new <u>Universal Federal Employees Health Benefit Program</u> [FEHBP], which today offers over 300 choices nationwide.

V. <u>OTHER PROVISIONS RELEVANT TO SMALL BUSINESSES</u>

- **<u>Independent Contractor:</u>** Before January 1, 1996, the Treasury Department will submit a legislative proposal providing statutory standards for the classification of workers as independent contractors.

- **<u>Subchapter S Corporations:</u>** A 2% shareholder's pro-rata share of taxable income from a service-related business would be treated as net earnings from self-employment.

- **<u>Reform Health Care Part Of Workers' Compensation:</u>** To end unnecessary duplication and reduce costs for small businesses, injured workers will obtain treatment through their health plans for work-related injuries. Employers would continue to purchase experience-rated workers' compensation from insurers. A Commission will be established to study the issues involved in full integration and make detailed recommendations within 2 years which Congress would have to consider.

THE HOUSE BILL: GOOD FOR SMALL BUSINESS

SUMMARY: *The House bill makes important changes to increase protection for small business. The leadership listened to the owners of small businesses -- and the new legislation has taken many additional measures to address their concerns -- with more choices, extra incentives to buy insurance, and a longer phase in to make sure we do things right.*

PROHIBITS INSURANCE DISCRIMINATION AGAINST SMALL BUSINESSES:

- The House bill eliminates insurance company practices that make small businesses pay so much more for insurance than larger firms. Insurance companies will be prohibited from dropping firms, denying coverage, or raising a small company's premiums when even just one worker gets sick. All will pay the same "community" rate -- no small business may be charged more for having older or sick workers.

SMALL BUSINESSES GIVEN SPECIAL PROVISIONS -- EXTRA TIME TO ADJUST:

- Provisions for small businesses are phased in over a longer period of time, giving small businesses an extra two years to adjust.

OFFERS SMALL BUSINESSES BARGAINING POWER TO GET BEST RATES:

- It encourages small businesses to join voluntary purchasing alliances, to give them the same negotiating power that allows large firms to get the best rates and the most choices today. This will also reduce the administrative costs which burden small businesses today.

PROVIDES DISCOUNTS FOR THE SMALLEST LOW-WAGE FIRMS:

- The proposal offers generous provisions for the smallest firms -- those with fewer than 50 employees and an average wage of less than $26,000 -- to help them finally bring affordable insurance into reach

MORE CHOICES FOR SMALL FIRMS AND THEIR EMPLOYEES:

- Employees of small businesses will finally get the choices they've been denied in the current system. They may join the federal employees health care system -- a proven system with over 300 choices nationwide. Or small businesses may decide to enroll their employees in Medicare Part C -- a fee-for-service health care plan, allowing them to choose any doctor they want.

ELIMINATES "HIDDEN TAX" SMALL BUSINESS PAY TODAY:

- Today, small businesses that provide insurance pay extra for the dependents of their employees who work for companies who do not provide insurance. When all employers take responsibility, costs will be substantially reduced for businesses that currently provide insurance.

IN CONTRAST -- INCREMENTAL REFORM STILL BURDENS SMALL BUSINESS:

- A recent study in Health Affairs concluded that: *"For those who have suggested that the best policy may be to muddle through with only small, incremental changes, our analysis suggests that...* ***in the years ahead, 30 percent of small businesses currently providing insurance will drop their insurance coverage because of the high cost."*** [Health Affairs, Spring 1992]

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THE SENATE BILL: POLICY ON SMALL BUSINESS

Today, small businesses have a hard time finding affordable insurance and offering their employees any choice of health plans. They are often discriminated against by insurance companies, charged higher prices than large businesses, or denied coverage altogether. The Senate bill contains provisions to improve small business access to insurance, make sure that insurance is more affordable, and give employees of small businesses the same choices as all Americans.

I. *INCREASED ACCESS*

The bill reforms the insurance market to eliminate some of the policies which have been traditionally used to discriminate against small business.

- *Guaranteed Issue:* Health plans cannot deny coverage to any eligible group.
- *Guaranteed Renewability:* Health plans must renew all eligible groups [i.e., can't drop a company.]
- *Elimination of Pre-Existing Condition Exclusions:* Pre-existing conditions will be phased out and eventually eliminated.
- *Eliminates Experience Rating:* Health plans will no longer be able to charge small businesses more based on the health status of their employees.

II. *SHARED RESPONSIBILITY*

- **Shared Responsibility Only As A Back-Up:** A requirement for shared responsibility will only go into effect if 95% of the population is not covered by the year 2000. The CBO predicts that the Mitchell bill will *"meet its target of 95% coverage"* by 1997, using market forces and subsidies. Only if this goal has not been met will a 50-50 employer-individual mandate go into effect in 2002 in states with less than 95% coverage and then, only if Congress has not acted on the recommendations of a Coverage Commission.

- **Small Business Exemption:** Even if the back-up plan does go into effect, **firms with fewer than 25 employees will be exempted from any requirement to contribute.**

- **Subsidies for Expanding Coverage:** Employers who expand coverage to all employees within a class -- i.e., part-time or full-time -- will be eligible for subsidies for currently uninsured employees, beginning in 1997 and available for 5 years. Firms paying 50% or more of the premium receive a subsidy for any amount above 8% of the newly-insured employee's wages, up to 50% of the premium.

III. *AFFORDABILITY*

- **Purchasing Cooperatives:** Requires states to establishes voluntary purchasing cooperatives to increase bargaining power of small businesses. Plans sold through the cooperative would be sold at a community rate.

- **Community Rating:** Modified community rating would apply to health plans sold to groups of 500 or less. That means that all businesses pays the same price, adjusted only by a 2:1 age band (eliminated in 2002).

- **Self Employed Tax Deduction:** Beginning in 1996, the self-employed tax deduction is increased from 25% to 50% of health insurance premiums. This is the amount of the employer contribution that would be required if the back-up system of shared responsibility goes into effect.

IV. EXPANDED CHOICES

Small employers (with fewer than 500 employees) would have several choices of insurance to offer their employees (with no requirement to contribute, except as a potential back-up beginning in 2002):

- They must offer their employees the option of purchasing coverage through a voluntary purchasing alliance, consolidating their bargaining power with other businesses to get the most choices and the lowest prices. The purchasing cooperative will have to offer a minimum of three plans, including a fee-for-service plan.
- And, they may offer a minimum of three private insurance plans -- a fee-for-service plan, a managed care plan, and a point-of-service plan -- in addition to the choices offered under the purchasing cooperative.
- Employees of small firms (with fewer than 500 employees) may always choose coverage under the Federal Employees Health Benefits Program [FEHBP], which today offers over 300 choices nationwide.

V. OTHER PROVISIONS RELEVANT TO SMALL BUSINESSES

- **Independent Contractor:** Before January 1, 1996, the Treasury Department will submit a legislative proposal providing statutory standards for the classification of workers as independent contractors.

- **Subchapter S Corporations:** All 2% shareholders who provide significant services to S Corporations will include as net earnings from self-employment the lesser of: a) their net share of income from the trade or business, or b) 30% of the Social Security wage base ($18,200).

- **Reform Health Care Part Of Workers' Compensation:** A Commission will be established to study the issues related to the relationship between health plans and workers' compensation medical services. The Commission will report to the President, as well as the House Education & Senate Labor and Human Resources Committees, by 10/1/2000. The plan also authorizes a number of state demonstration projects with respect to work-related illnesses and injuries.

THE SENATE BILL: GOOD FOR SMALL BUSINESS

SUMMARY: *The Senate bill makes important changes to increase protection for small business. The leadership listened to small businesses owners -- and the new legislation goes to great lengths to address their concerns -- with greater flexibility, more choices, extra incentives to buy insurance, and a longer phase-in to make sure we do things right.*

SMALLEST BUSINESSES EXEMPTED FROM SHARED RESPONSIBILITY:

- Under the Senate bill, small businesses with 25 or fewer employees will be exempted from any requirement to contribute to their workers' insurance -- and they will have a more accessible, affordable system if they choose to provide insurance. If these firms choose not to provide coverage, their eligible employees will be given subsidies to help them purchase insurance on their own.

PROHIBITS INSURANCE DISCRIMINATION AGAINST SMALL BUSINESSES:

- The bill eliminates insurance company practices that make small businesses pay much more for insurance than larger firms. Insurance companies will be prohibited from dropping firms or denying them coverage. Pre-existing condition exclusions -- used to deny small businesses insurance today -- will be phased-out. The variations in rates that characterize the small business market today will be reformed; all businesses will pay the same "community" rate, adjusted only by a 2:1 age band.

OFFERS SMALL BUSINESSES BARGAINING POWER TO GET BEST RATES:

- The bill offers small businesses voluntary purchasing alliances, to give them the same negotiating power that allows large firms to get the best rates and the most choices today. This will also reduce the administrative burden on small businesses, who today pay eight times what large companies do for this.

INCREASED INCENTIVES FOR BUSINESSES TO EXPAND COVERAGE:

- Employers who expand coverage to a new class of employees -- i.e., part-time or full-time -- will be eligible for subsidies for currently uninsured employees, beginning in 1997 and available for 5 years. Firms paying 50% or more of the premium receive a subsidy for any amount above 8% of the newly-insured employee's wages, up to 50% of the premium.

MORE CHOICES FOR SMALL FIRMS AND THEIR EMPLOYEES:

- Employees of small businesses will finally get the choices they've been denied in the current system. They may join the federal employees health care system -- a proven system with over 300 choices nationwide -- or choose from the range of options offered by the purchasing cooperatives their employers must offer them. And their employers may also choose to offer them a choice of three plans -- one of which must be a fee-for service plan with unlimited choice of doctors.

IN CONTRAST – INCREMENTAL REFORM STILL BURDENS SMALL BUSINESS:

- A recent study in Health Affairs concluded that: *"For those who have suggested that the best policy may be to muddle through with only small, incremental changes, our analysis suggests that... **in the years ahead, 30 percent of small businesses currently providing insurance will drop their insurance coverage because of the high cost.**"* [Health Affairs, Spring 1992]

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