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The Baucus Plan: Implications for Small- and Medium-Sized Firms

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The health care reform legislation known as the "Baucus plan" will demand that firms with 50 or more employees offer health insurance coverage or pay an assessment fee to subsidize the cost of individual employee coverage through a State Health Insurance Exchange. This proposal essentially imposes a mandate on firms with 50 or more employees, which will dramatically affect companies' per-employee costs and their allocation of labor.

The Baucus Plan. The Baucus plan outlines a small-firm refundable tax credit, which would apply to all firms with 25 or fewer employees—although the full amount of this credit would apply only to firms with 10 or fewer employees. The small firm tax credit in this particular proposal is phased out for firms larger than 10 employees (and not exceeding 25 employees) with either a 6 percent reduction in the tax credit for every additional employee above the 10-employee threshold or a 5 percent reduction in the tax credit for each $1,000 increase of average wages for those employers with average wages between $20,000 and $40,000.[1]

Additionally, the Baucus plan includes an assessment penalty on firms with more than 50 employees that do not currently offer health coverage.[2] The Baucus plan defines this penalty as a flat amount equal to the national average subsidy multiplied by the number of employees receiving an "affordability waiver," or a capped amount of $400 multiplied by the total number of employees at the firm. The flat amount is abstractly documented in the proposed Baucus legislation, but it will be "set by the Secretary of HHS and published in a schedule each year."[3] This amount will likely to be set at thousands of dollars.

Burden on Medium-Sized Firms. Any potential health care reform legislation that punitively adds costs to employers will dramatically affect the way these firms treat their labor force. A company's decision not to offer health care will not be driven by a desire to deny its employees' coverage. Rather, it will be the result of the fact that, for many companies, it is too costly to offer health benefits in addition to current wage and other compensation. For example, if a firm with 49 employees decides to expand by one employee, then the potential marginal cost of the 50th employee could be $20,000—a capped amount of $400 multiplied by 50, the new number of employees at the firm—plus other costs of hiring this employee.

Moreover, the estimated share of average annual change in cost per employee as a share of per-employee compensation will rise by 5 percent on average for firms currently not offering health insurance coverage and 2.5 percent for those firms that currently do offer coverage. For all medium-sized firms, the estimated annual change in cost per

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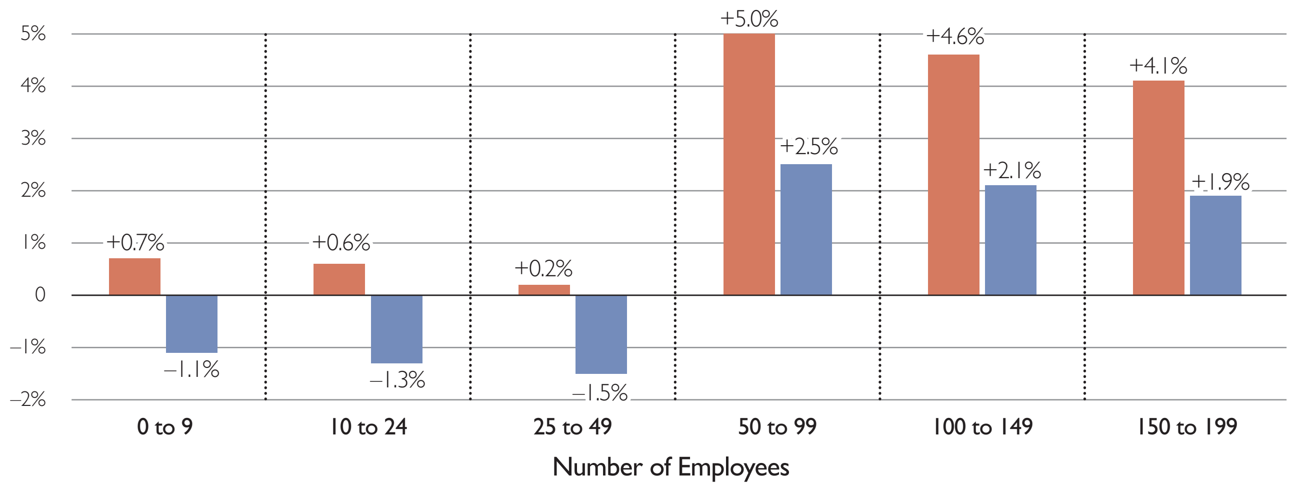
How the Baucus Bill Would Affect Small- and Medium-Sized Businesses

The Baucus health care bill mandates firms with 50 or more employees must either offer health insurance to their employees or pay an assessment fee. As a result, firms with 50 or more employees would face significantly higher per-employee costs, even those firms that currently offer insurance for their employees.

Firms currently not offering health insurance to employees

Firms currently offering health insurance to employees

Annual Change in Average Employer Costs per Employee as a Percentage of Average Employee Compensation



Note: See methodology section for assumptions used in calculating these cost estimates.

Source: Heritage Foundation calculations using data from the 2006 Small Business Administration, the 1997 Robert Woods Johnson Foundation Employer Health Insurance Survey, and the 2006 Kaiser Foundation Family and Health Education and Research Trust Employer Benefits Survey.

Chart 1 • WM 2656 heritage.org

employee as a share of per-employee compensation will be 4.6 percent for those currently not providing health insurance coverage and 2.2 percent for those that do currently offer health insurance.[4]

These firms will likely not be able to absorb this increase in cost of providing health insurance coverage (or paying the assessment penalty); thus, this cost increase will be passed on to employees in the form of reduced wages, increased insurance cost-sharing, discontinued hiring, or loss of employment.[5] Some firms, instead of hiring an additional employee, will simply increase hours for current employees. These increased costs could also result in a large number of employers contracting low-skilled and low-income labor or hiring a greater share of non-permanent (part-time or full-time) employees.

Implications for Small Firms. The Baucus plan's implications for small firms are not as dramatic as those illustrated for medium-sized firms—aside from reducing the incentive to expand. For instance, there is not a mechanism in the Baucus

1. Committee on Finance, U.S. Senate, "Chairman's Mark," September 22, 2009, p. 26–28, at *http://finance.senate.gov/sitepages/leg/LEG%202009/091609%20Americas_Healthy_Future_Act.pdf* (September 22, 2009).
2. Staff of the Center for Health Policy Studies, "The Baucus Health Bill: A First Look," Heritage Foundation *WebMemo* No. 2619. September 17, 2009, at *http://www.heritage.org/Research/Healthcare/wm2619.cfm*. Small-, medium-, and large-sized firms refer to firms with 0–49, 50–199, and 200 or more employees, respectively, unless noted otherwise.
3. Committee on Finance, U.S. Senate, "Chairman's Mark," p. 26–28.
4. According to Small Business Administration 2006 data on the total number of firms and employees by firm size, medium-sized firms accounted for only 8.8 percent of total firms but 21.9 percent of total employees in the U.S.

plan that requires small firms to offer health insurance coverage to their employees. As a result, under the Baucus plan, many small firms—perhaps most—either will decide to not offer coverage or drop coverage if they currently offer it. Subsequently, employees will have to procure coverage through the proposed State Health Insurance Exchanges.

Medium-Sized Firms under Fire. Overall, the estimated effects of the Baucus plan on medium-sized firms are quite substantial and, in addition to the added cost burden on medium-sized firms, could create a strong disincentive for small firms to expand to 50 or more employees. Firms ranging in size from 50 to 75 employees will be the hardest hit, and all medium-sized firms will likely see an increase in average costs per employees as a result of the Baucus plan.

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Methodology

The Heritage Foundation's calculation of the average annual costs per employee uses data from the U.S. Small Business Administration 2006 Statistics of U.S. Businesses and Non-Employer Statistics data set, the Robert Woods Johnson Foundation 1997 Employer Health Insurance Survey, and the 2006 Kaiser Family Foundation/Health Education and Research Trust Employer Health Benefits Survey. An estimation of average annual costs per employee change was constructed using aggregated data on firm/industry-level employment and payroll data weighting the distribution (based on firm size) by a premium per employee weight and a cost per employee weight (accounting for additional benefit compensation to employees).

The following assumptions are made in the cost calculations used to estimate the average annual change in costs per employee:

First, the proposed Baucus plan reforms on small-firm refundable tax credits and the employer penalty for firms with 50 or more employees will be fully implemented between 2013 and 2014.

Second, the estimated coverage distribution (i.e., number of workers offered as well as those who take up insurance) is the same from the baseline scenario to the policy implementation scenario and that the employer tax penalty is $400 for firms with 50–199 employees and slides for the remainder of the distribution (firms with 200 or more employees).

Third, there will be a potential tax incentive for some firms to offer coverage that had not previously offered it. Thus, the assumption is that some firms will change their coverage decisions.

Fourth, the share of firms that decide to offer coverage (as well as subsequent take-up rates) will decline as firm size increases, particularly for firms with 25–49 employees.

Last, these calculations assume that for firms with 49 or fewer employees that currently do offer health insurance coverage, a share will decide to drop coverage, and the greatest share of firms dropping coverage will be those with 25–49 employees.

5. Rea S. Hederman, Jr., and Paul L. Winfree. "Baucus Plan Increases Out-of-Pocket Costs for Many Families," Heritage Foundation *WebMemo* No. 2628, September 25, 2009, at *http://www.heritage.org/research/healthcare/wm2628.cfm*. See also Congressional Budget Office, "An Analysis of Premiums under the Chairman's Mark of America's Healthy Future Act," September 22, 2009, at *http://cbo.gov/ftpdocs/106xx/doc10618/09-22-Analysis_of_Premiums.pdf* (October 8, 2009); Robert A. Book, Guinevere Nell, and Paul L. Winfree, "The Baucus Individual Health Insurance Mandate: Taxing Low-Income and Moderate-Income Workers," Heritage Foundation *Backgrounder* No. 2325, September 25, 2009, at *http://www.heritage.org/Research/HealthCare/bg2325.cfm.*