

No Small Matter

How Small Businesses Make Decisions About Employee Benefits

Kimberly Landry
Insurance Research — Product
(860) 285-7889
klandry@limra.com

This publication is a benefit of LIMRA membership. No part may be shared with other organizations or reproduced in any form without L.L. Global's written permission.



Table of Contents



	Page
▶ Introduction	3
▶ Key Findings and Implications	4
▶ Section I. Issues and Challenges Facing Small Businesses	6
▶ Section II. The Decision-Making and Purchasing Process	9
▶ Section III. Employers Not Offering Benefits	13
▶ Section IV. Key Trend: Voluntary Products	18
▶ Section V. Key Trend: Health Reform	22
▶ Methodology	26



- ▶ There are over 5.6 million businesses in the United States with fewer than 100 employees, representing approximately 98 percent of all employers and 35 percent of the labor market.¹ With such immense scale, the small business market represents a wealth of opportunity for the employee benefits industry. Only 47 percent of these small firms currently offer insurance benefits to their employees, and those that do tend to offer fewer products than do their larger peers.² Despite these shortcomings, small business employees place a high value on having access to benefits at work.³ To better meet the needs of this diverse market, it is critical to understand the decision-making process that small businesses use when navigating their benefits options.

¹ U.S. Census Bureau, 2009 data. Estimates exclude non-employer firms.

² *Small World: Trends in the U.S. Small Business Market*, LIMRA, 2013.

³ *What Is \$1 Billion an Hour Worth? Employee Perspectives on Benefits*, LIMRA, 2010.

Key Findings and Implications



- ▶ **Small businesses are worried about the cost of benefits.**

With health insurance premiums rising much faster than overall inflation, small firms are preoccupied with controlling the escalating cost of these plans. However, the cost of nonmedical benefits is also a major concern for these employers.

- ▶ **Benefit communication is not a high priority.**

Although it is well-known that many employees have a limited understanding of their own benefits, most employers do not see benefit education to be a critical issue and are unlikely to take the initiative to improve their communication efforts. Benefit carriers that want to improve communications to their enrollees will have to be proactive about offering solutions that make it easy for employers to convey information.

- ▶ **Owners are heavily involved in benefits decisions.**

Sales reps and producers marketing benefits to small firms should be prepared to deal directly with the business leader rather than a human resource or benefits administrator. Communications should be tailored to account for the lack of expertise and limited time that these individuals may have to devote to benefit decisions.

- ▶ **Many have not been contacted about benefits.**

Two thirds of small businesses without benefits have not been approached about offering them in the past year, but many will agree to meet with a producer when contacted. The benefits industry needs to do a better job of reaching out to these firms.

Key Findings and Implications



- ▶ **Small firms give a variety of reasons for not offering benefits.**

Most claim that the business cannot afford them, while some believe they do not have enough employees to offer benefits or that their employees prefer higher take home pay.

- ▶ **Many firms without benefits are unfamiliar with voluntary products.**

While cost is the major reason these firms give for not offering benefits, many are unaware that they have the option of making these products available on an employee-pay-all basis. This points to a clear need for the industry to raise awareness about voluntary benefits among small employers.

- ▶ **Most small businesses do not want to drop medical coverage.**

In the face of continued inflation of medical costs, small businesses are much more likely to consider dropping *nonmedical* products or switching these benefits to voluntary-funding arrangements rather than eliminating medical plans. To avoid these losses, the benefits industry will need to focus its attention on increasing awareness among small businesses of the value of nonmedical products.

Section I.

Issues and Challenges Facing Small Businesses



No decision is ever made in a vacuum, and this is particularly true for small businesses evaluating their benefit offerings. Small employers face a multitude of competing challenges and priorities that must be weighed when deciding whether or not to offer benefits to their employees. Understanding which issues matter the most to these firms is the key to anticipating their future actions.



Key Findings

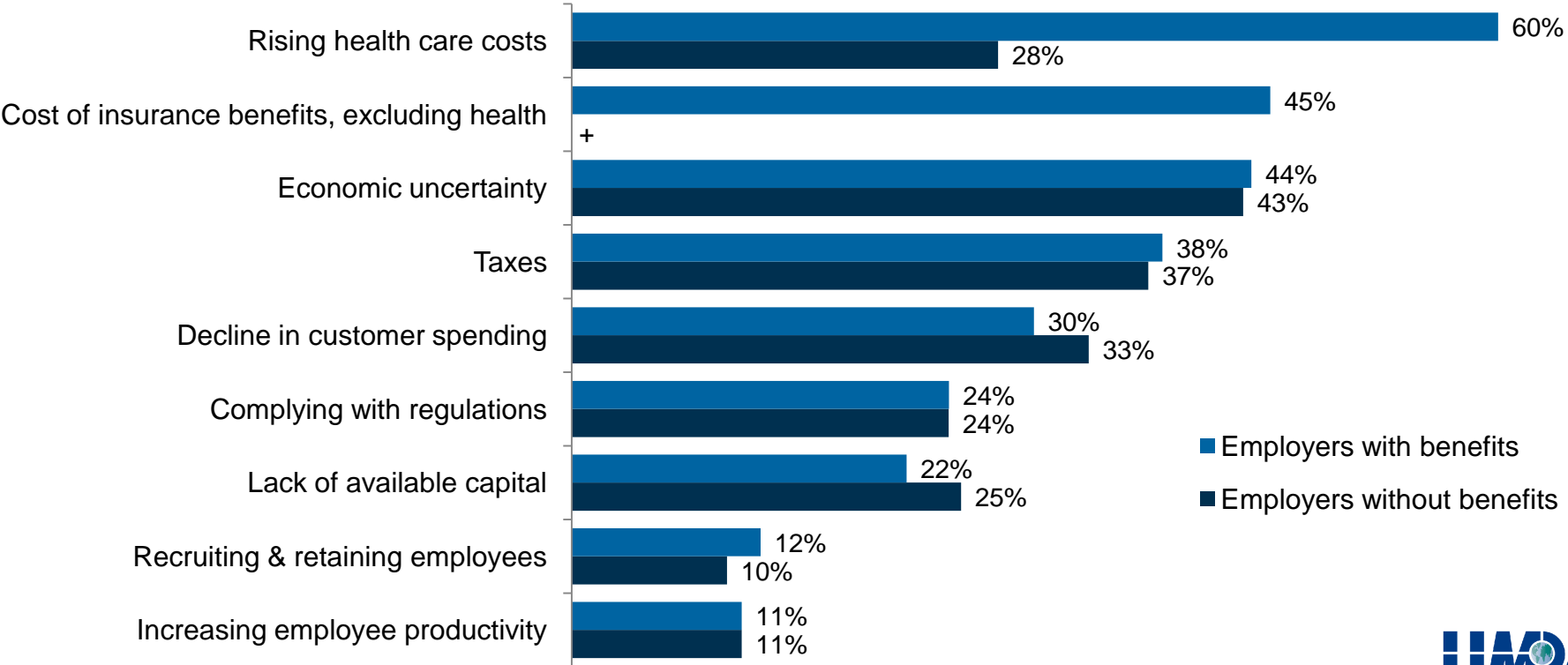
- ▶ **The cost of benefits is a dominant concern for small businesses.** With health insurance premiums rising much faster than overall inflation, small firms are preoccupied with controlling the escalating cost of these plans. However, the cost of nonmedical benefits is also a critical issue for these employers.
- ▶ **They are not worried about attracting and retaining employees.** Despite recent economic improvements, the still-elevated unemployment rate means that small businesses do not feel that recruitment and retention are challenges at the moment, eliminating a key source of motivation for offering competitive benefit plans. It is unlikely that these firms will show significant interest in expanding their benefit packages until the economy improves.
- ▶ **Benefit communication is not on the radar.** With so many other pressing concerns, most employers will not make it high-priority to improve benefit communication and education to employees in the near future. Benefit carriers that wish to improve communication to enrollees will have to be proactive about offering these solutions to employers.



Critical Issues Facing Small Employers

- ▶ Among those firms that currently offer insurance benefits, cost is a matter of significant concern. These businesses rate rising health care costs and the cost of other insurance benefits as the top two critical issues facing their companies, surpassing many other topics.
- ▶ Firms that do not offer benefits show significantly less concern over rising health care costs, since in these cases it is likely that the business owner is only responsible for his or her own coverage. Among these firms, economic uncertainty is the most critical issue, followed by taxes.
- ▶ Employee recruitment, retention, and productivity are all fairly low priorities for small businesses at this time. These issues tend to be viewed as more important as company size increases.

Figure 1: Critical Issues Facing Small Employers

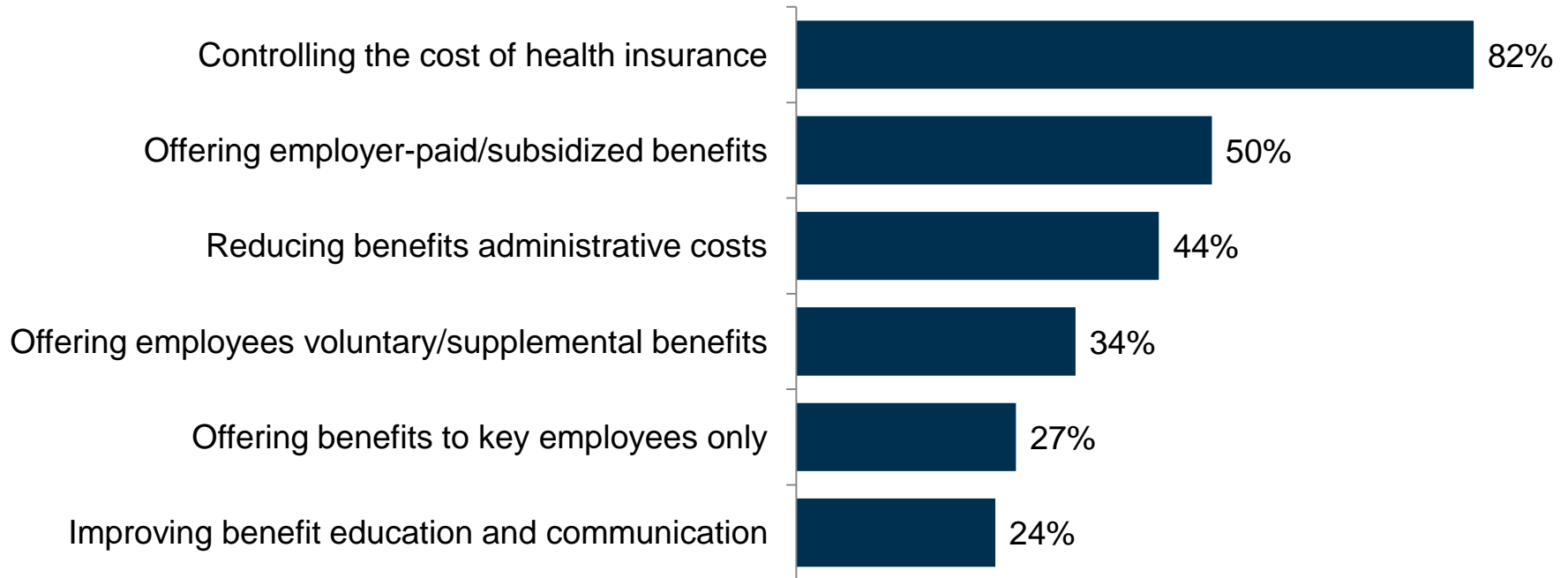


Challenges to Offering Insurance Benefits



- ▶ Small businesses that currently offer insurance benefits also report a number of challenges specifically related to these offerings.
- ▶ Cost issues rise to the top once again: 4 out of 5 small businesses find it difficult to control the cost of health insurance while half struggle with offering employer-funded benefits. Conversely, only a minority of small firms find it challenging to offer voluntary benefits or benefits to key employees only. This is most likely because voluntary and executive benefits impose significantly less financial burden on the company.
- ▶ It is also notable that most small businesses do not consider improving benefit education and communication to be a challenge, even though it is widely known that many employees have only a limited understanding of their own benefit options. Younger business owners are more likely to see this as a challenging issue.

Figure 2: Challenges to Offering Employee Benefits*



*Percent rating the issue "challenging" (4 or 5 on a 5-pt scale)

Section II.

The Decision-Making and Purchasing Process

Small businesses that choose to offer benefits face a variety of options for evaluating and completing the purchasing process. The person within the firm that makes the decision, their sources of information and advice, and the ultimate purchasing channel may all influence how benefits are offered.



Key Findings

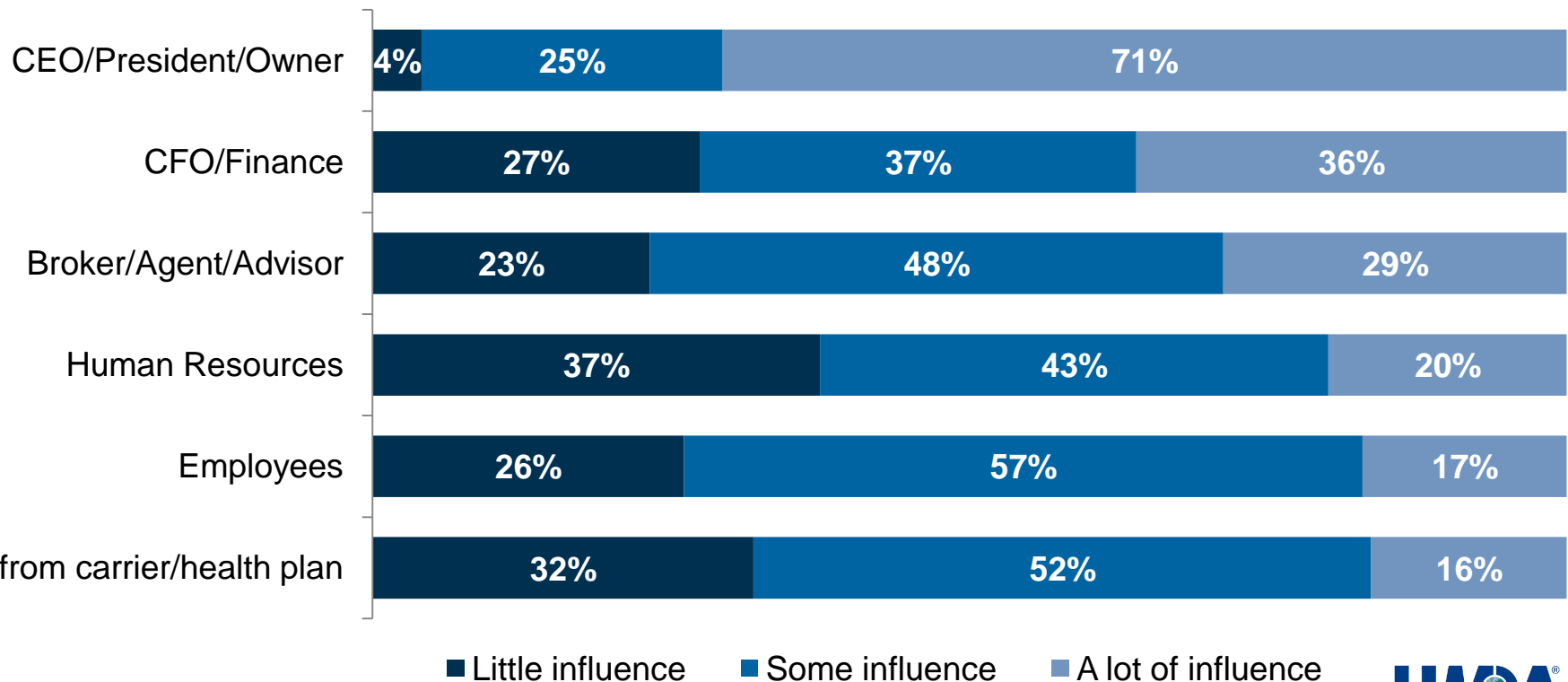
- ▶ **Small business owners are heavily involved in benefit selection.** Sales reps and producers marketing benefits to small firms should be prepared to deal directly with the business leader rather than a human resource or benefits administrator. Communications should be tailored to account for the lack of expertise and limited time that these individuals may have to devote to benefit decisions.
- ▶ **Agents and brokers are a key resource.** These financial professionals are the top source of information and advice about benefits, as well as the most common channel through which purchases are made. However, there are still a significant number of small businesses that are not utilizing these advisors.

Who Has the Most Influence Over Benefit Decisions?



- ▶ When it comes to selecting a benefits carrier, health plan, or administrator, the small business owner or CEO has dramatically more influence over the decision than any other party. The CFO or finance area is also very influential, pointing to the fact that cost is a major factor in benefit decisions.
- ▶ While human resource personnel appear to have little influence over carrier selection overall, this is mostly due to the fact that many businesses are too small to have HR departments. As company size increases, HR teams become significantly more influential in the decision-making process.
- ▶ Conversely, employees tend to have a lot more influence at very small firms, where benefit decisions are more likely to be discussed with staff.

Figure 3: Influence Over Benefits Decisions

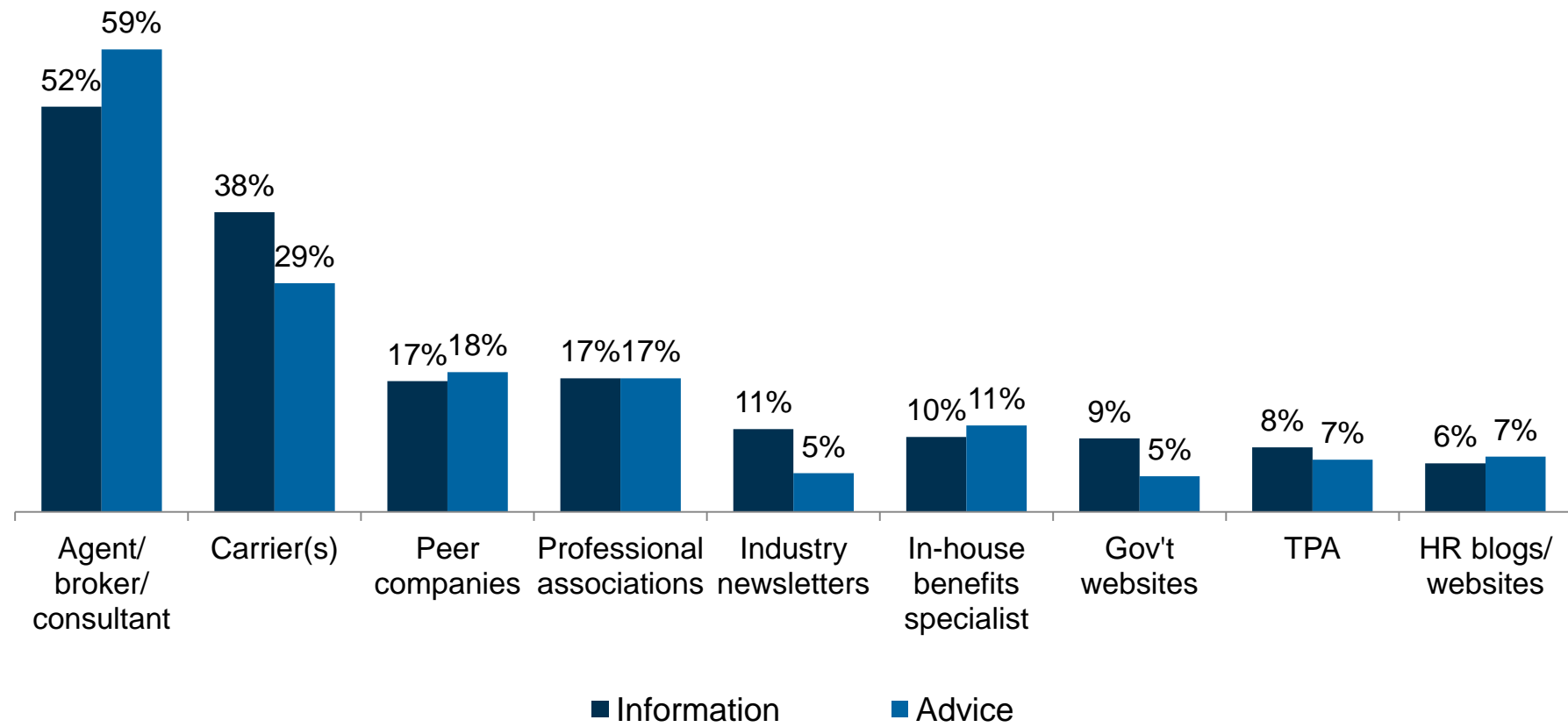




Top Sources of Information and Advice About Benefits

- ▶ When making decisions about employee benefits, small businesses consult a wide variety of sources for information and advice. However, insurance producers such as agents, brokers, and consultants stand out by a wide margin as the top resource for small employers.
- ▶ Insurance carriers are also considered a key resource. However, they are more likely to be utilized for information than advice, most likely due to concerns about their objectivity. Firms that are still establishing themselves are more likely to turn to their carrier for advice.

Figure 4: Sources of Information and Advice About Benefits*

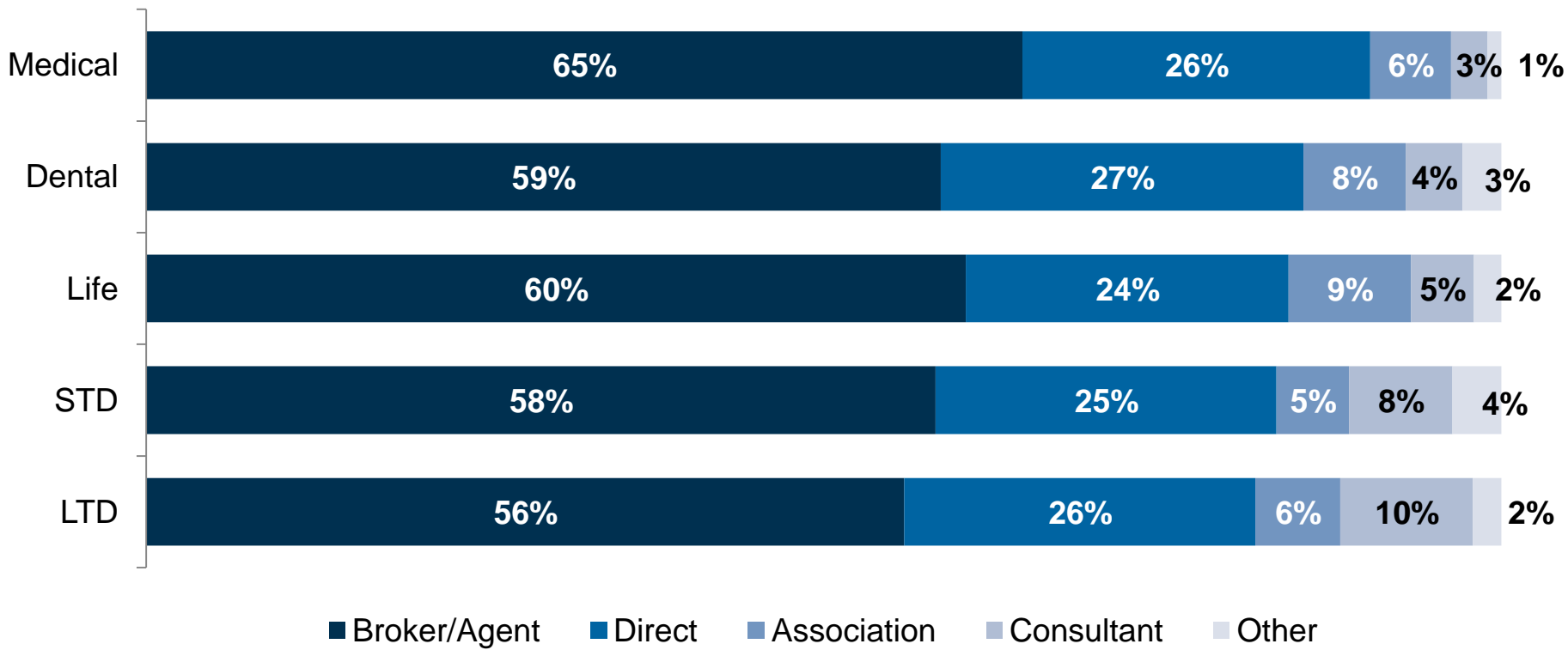


* Respondents selected their top two resources for information and advice about employee benefits.

Purchasing Channel

- ▶ Approximately 60 percent of small businesses purchase benefits through an agent or broker, a trend that is consistent across both medical and nonmedical products. Firms in the wholesale or retail trade industry are the most likely to utilize an agent or broker.
- ▶ Another quarter of small businesses choose to purchase benefits directly from the carrier, health plan, or third-party vendor. The preference for direct purchasing has been growing since 2005, when approximately 17 percent of small businesses bought at least one benefit directly from a carrier.

Figure 5: Channel Used to Purchase Benefits



Note: Some rows may not add to 100 percent due to rounding.

Section III.

Employers not Offering Benefits

When examining the decision-making process around employee benefits, it is also important to look at those small businesses that choose *not* to offer these products. Their reasons for opting out of the benefits market can provide insights into how the industry could better meet their needs in the future.



Key Findings

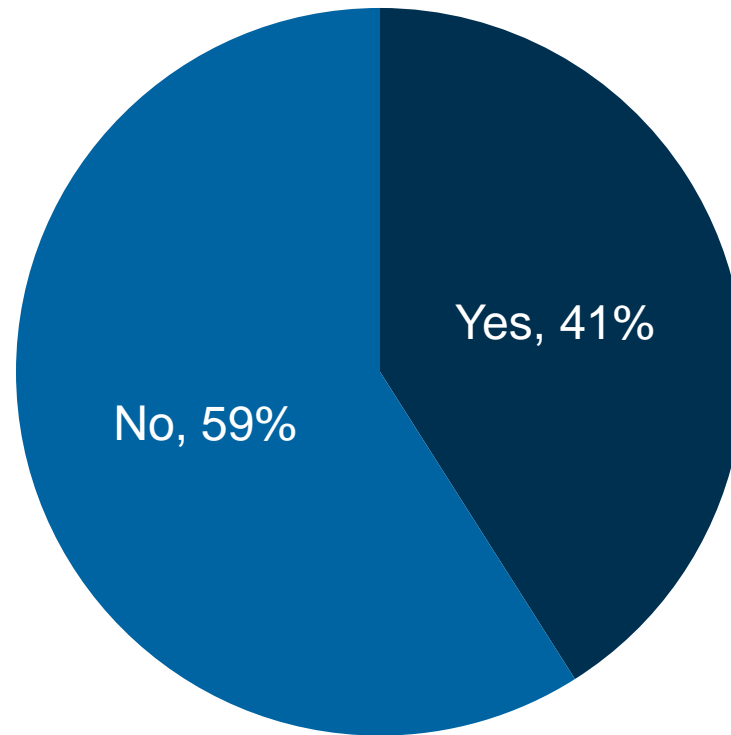
- ▶ **Misperceptions abound.** Most firms that do not offer benefits claim that the business cannot afford them, demonstrating a lack of knowledge about their options regarding voluntary products. Some also believe they do not have enough employees to offer benefits or that their employees prefer higher take home pay.
- ▶ **Many have not been contacted.** Two thirds of these small businesses were not approached about offering benefits in 2012, suggesting a significant missed opportunity for the industry.
- ▶ **There is a lot of interest.** Over 40 percent of small firms have already considered introducing employee benefits. Nearly half will agree to meet with a producer when contacted.

Have They Considered Offering Benefits?



- ▶ Among small businesses that do not currently offer insurance benefits to their employees, 41 percent have considered introducing benefits in the past. Firms that are based outside the home and are not family-owned are more likely than others to have considered adding benefits. Similarly, interest was higher among businesses in the Midwest region and those that are actively expanding.

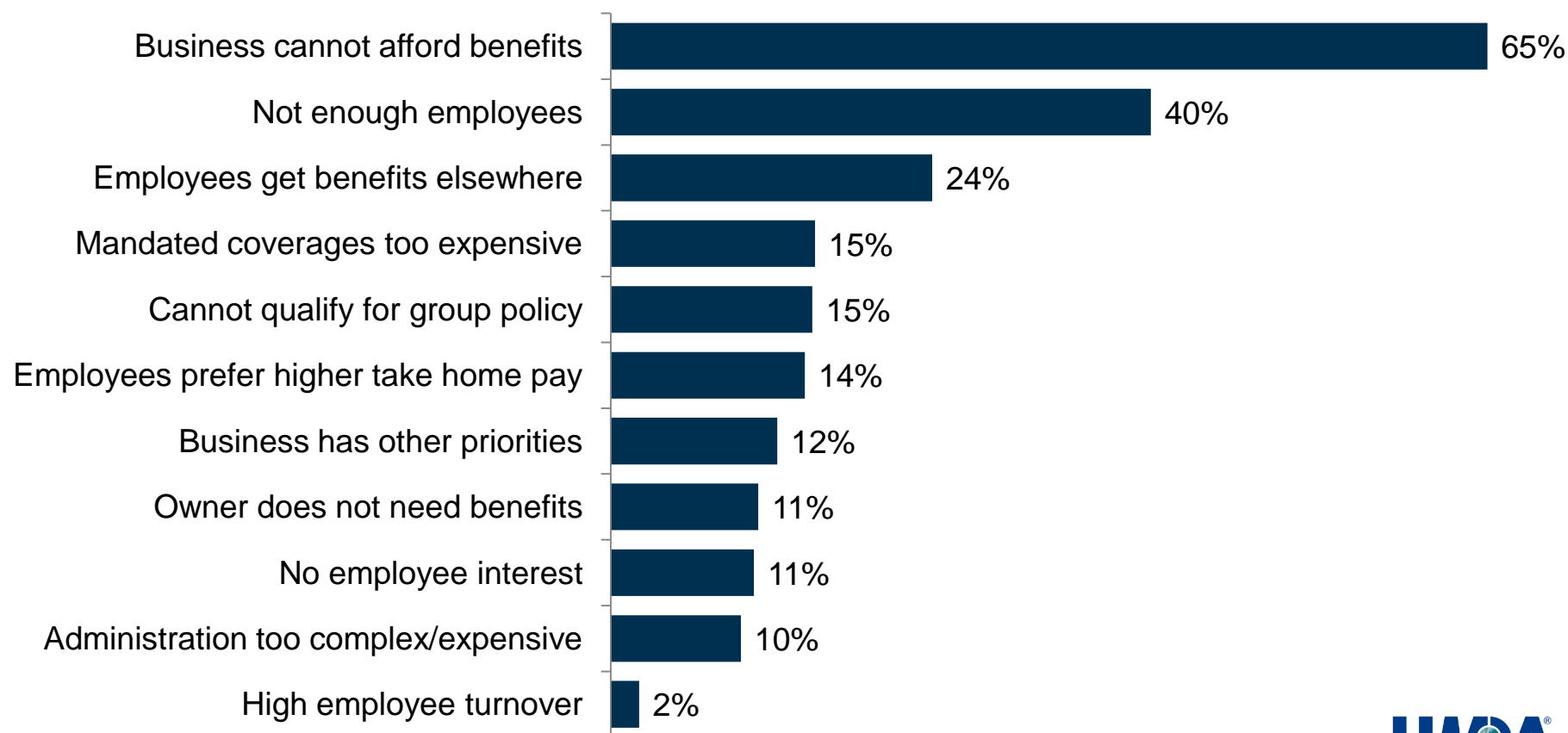
Figure 6: Considered Introducing Benefits



Reasons for not Offering Benefits

- ▶ Small businesses cite a variety of reasons for not offering insurance benefits. Cost is a major factor, with more than 6 in 10 stating that the business cannot afford benefits at this time.
- ▶ The reasons that small firms give for not offering benefits have evolved somewhat over time. While affordability has always been a top concern, firms are more likely to say they do not have enough employees to offer benefits now compared with prior years. This objection may become less prominent in the future, when the exchanges created by health care reform make it easier for small businesses to purchase medical benefits.

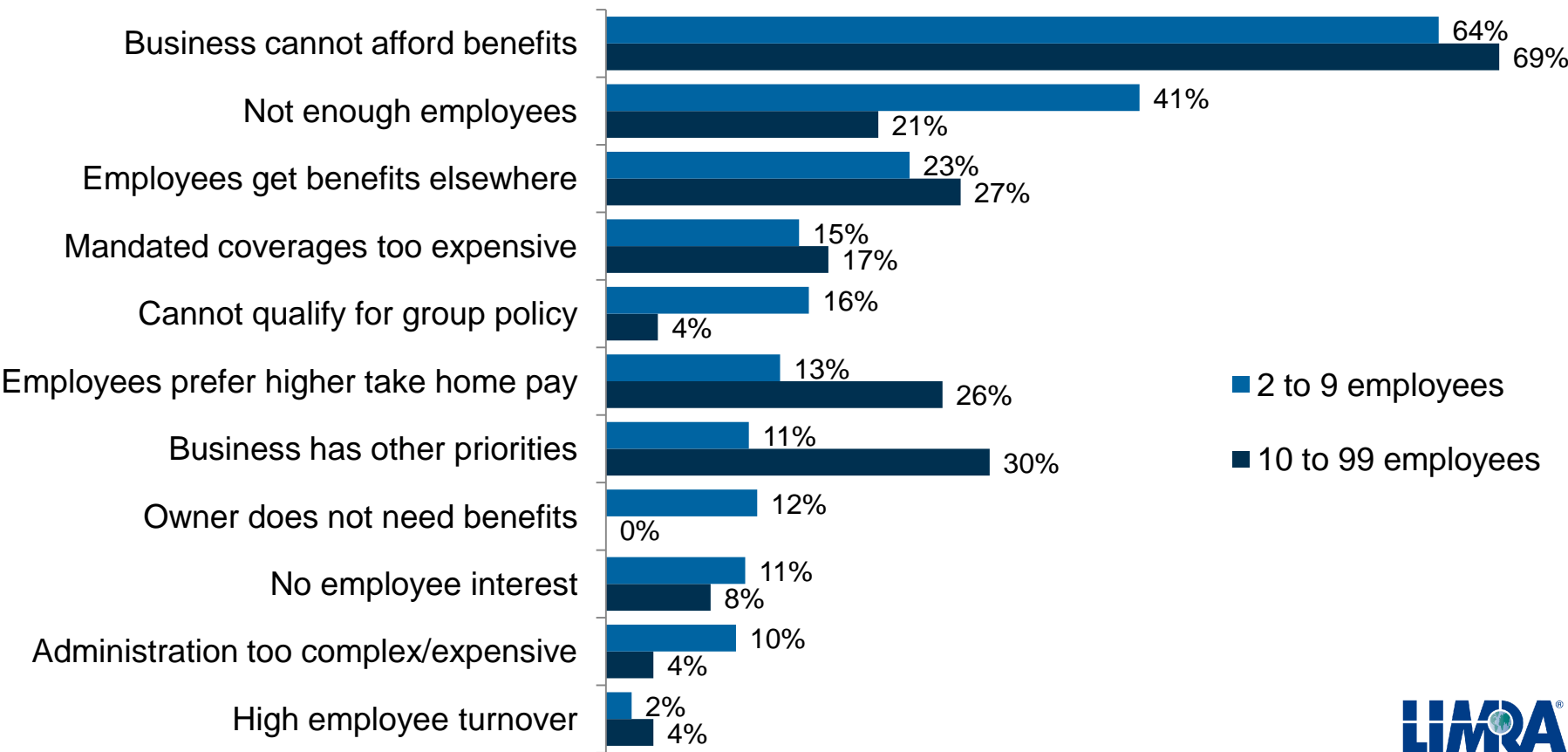
Figure 7: Reasons for not Offering Benefits



Reasons for not Offering Benefits

- ▶ The size of a business has a significant impact on its reasons for not offering benefits.
- ▶ Firms with fewer than 10 workers are much more likely than slightly larger firms to cite having too few employees, being unable to qualify for a group policy, and the owner not needing benefits.
- ▶ Among firms with 10 to 99 employees, the top reasons for not offering benefits are cost, employees getting benefits elsewhere, focusing on other business priorities, and believing that employees prefer higher take home pay. They are much more likely than smaller firms to mention the latter two issues.

Figure 8: Reasons for not Offering Benefits by Size of Firm

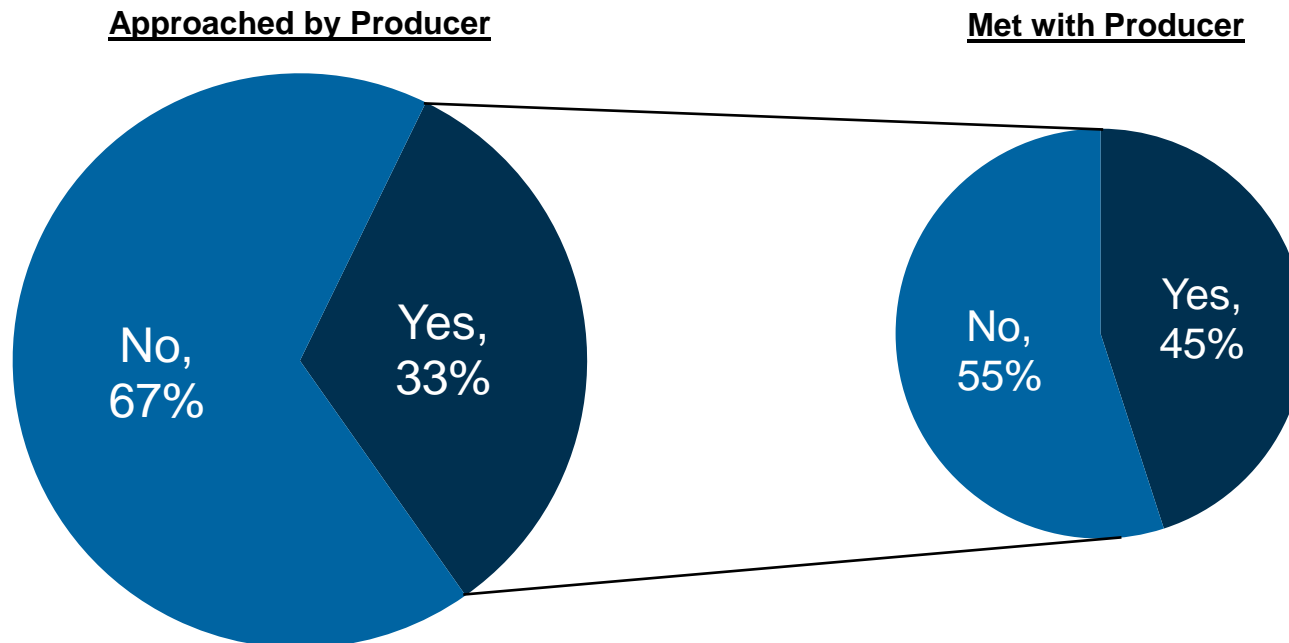


Producer Contact



- ▶ The significant portion of small businesses that do not offer benefits appear to be a missed opportunity for the group insurance industry. Only 33 percent of firms without benefits were approached by an agent, broker, carrier rep, or anyone else about purchasing benefits within the past 12 months. The smallest firms (those with fewer than 10 employees) were the least likely to be approached about benefits.
- ▶ Among those firms that were approached about benefits, 54 percent were contacted by someone who had previously assisted them with other business or personal coverages, while the rest were contacted by an unknown financial professional.
- ▶ The percent of small businesses being approached about benefits has declined since 2005, when approximately 41 percent were contacted. However, the percent of all approaches that are cold calls has declined as well.
- ▶ Of those that were approached, nearly half agreed to meet with the producer to discuss offering benefits, indicating that many firms without benefits are open to the idea of adding them.

Figure 9: Firms That Were Approached by and Met With a Benefits Producer



Section IV.

Key Trend: Voluntary Products

Given the growing concern over rising benefit costs, voluntary products are a vital tool that small employers can use to round out their benefit packages at no cost to the business. However, small firms' knowledge of and attention to these products still has much room for improvement.



Key Findings

- ▶ **Many firms without benefits are unfamiliar with voluntary products.** While cost is the major reason these firms give for not offering benefits, many are unaware that they have the option of making these products available on an employee-paid basis. This points to a clear need for the industry to raise awareness about voluntary benefits among small employers.
- ▶ **Voluntary benefits are not right for everyone.** Among small businesses that do offer insurance benefits, a majority of products are still offered on an employer-paid or contributory basis. In fact, many benefits are less likely to be offered on a purely voluntary basis now compared with prior years. This shift may be due to a variety of factors, including the recovering economy, turnover in the small business market, and attempts to improve participation rates by contributing employer funds.

Benefit Funding Methods



- ▶ Ancillary products such as long-term disability, critical illness, life insurance, and accident insurance are more likely than other benefits to be offered on a voluntary (employee-pay-all) basis.
- ▶ Firms with fewer than 10 employees are less likely to offer benefits on a voluntary or contributory basis and more likely to cover the full cost of benefits for employees. This is particularly true for medical, dental, vision, and accident coverage.
- ▶ Compared with prior years, small businesses are now somewhat less likely to offer benefits on a purely voluntary basis, shifting more toward employer-paid or contributory funding methods. In particular, critical illness and accident insurance are much more likely to be partially employer-funded than in the past.

Table 1: Benefits Offered by Funding Method

	Employer-Paid	Contributory	Voluntary
Medical	43%	52%	5%
Dental	39%	41%	19%
Vision	44%	41%	15%
Life*	48%	18%	34%
AD&D	53%	25%	22%
Short-Term Disability	51%	25%	24%
Long-Term Disability**	38%	20%	42%
Accident	42%	25%	33%
Critical illness	29%	30%	41%

* Voluntary data includes pure voluntary plans and supplemental life plans.

**Voluntary data includes pure voluntary plans and buy-up options.

Note: Some rows may not add to 100 percent due to rounding.

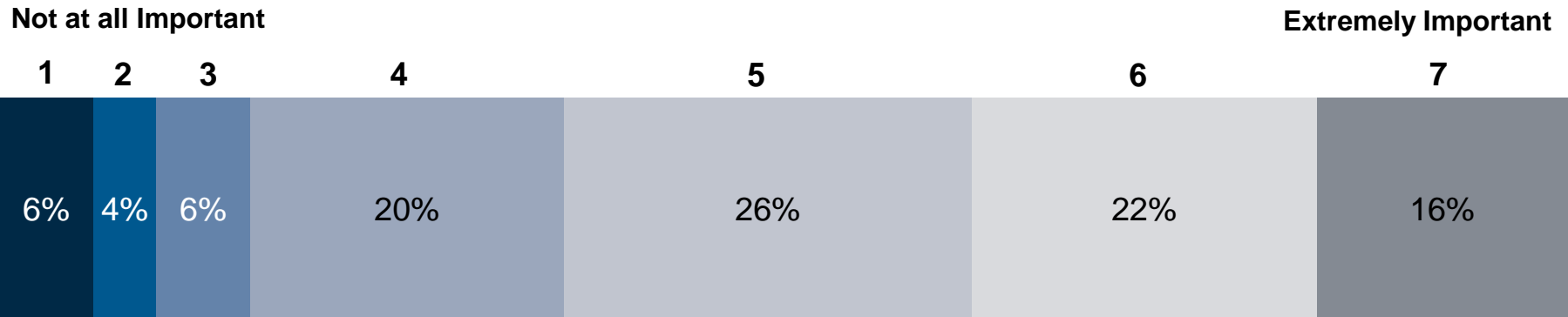


Importance of Voluntary Benefits

- ▶ Altogether, 64 percent of small employers think it is at least somewhat important to offer voluntary benefits to their employees, while only 16 percent consider it unimportant.
- ▶ Younger firms and those that are actively expanding are the most likely to place a high value on voluntary benefits. As might be expected, firms that offer a wider array of insurance benefits are also more likely to see the value of voluntary products.
- ▶ Firms that do not value voluntary products are also more likely to say that the cost of insurance benefits is *not* an important issue for them.

Figure 10: Importance of Offering Voluntary Benefits

“On a scale of 1 to 7, how important is it to your company to offer voluntary benefits?”

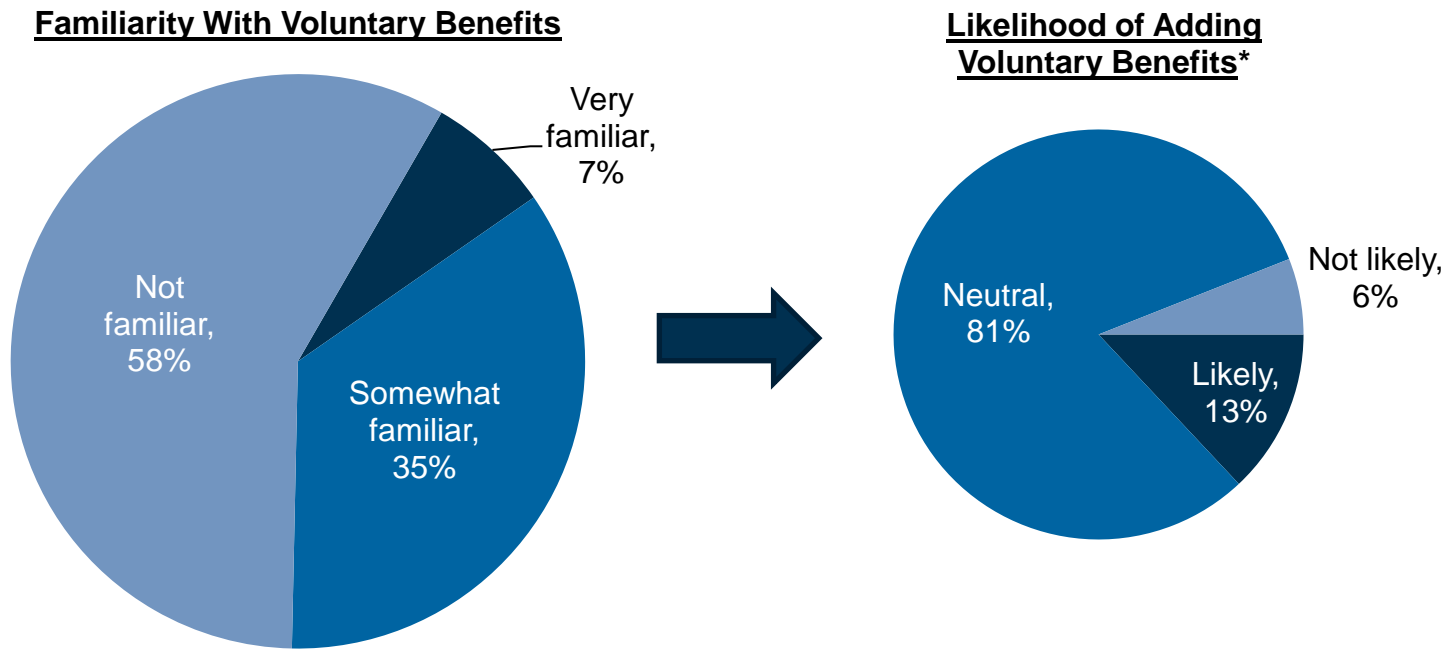




Interest in Voluntary Among Firms Without Benefits

- ▶ Among small employers that do not currently offer insurance benefits, more than half are not familiar with voluntary benefits. This knowledge gap is particularly concerning since lack of affordability is the number-one reason small firms cite for not offering benefits. Many of these businesses may not be aware that they could introduce voluntary products at little or no cost to their company.
- ▶ Firms with fewer than 10 employees are the most likely to be unfamiliar with voluntary products. Younger firms and those in the Midwest and West regions also display the least familiarity.
- ▶ Of those small businesses that are planning to introduce insurance benefits within the next 3 years, the majority are undecided about whether it will be a voluntary or employer-paid benefit.

Figure 11: Interest in Voluntary Products Among Firms Without Benefits



* Based on small employers without insurance benefits that are considering introducing benefits in the next 3 years and are at least somewhat familiar with voluntary benefits.

Section V.

Key Trend: Health Reform



Finally, the continued implementation of PPACA is certain to have an impact on the benefit strategies of small businesses, although the nature of that effect is far from clear. While businesses with more than 50 employees could face penalties for not offering health insurance to their employees, those with fewer than 25 employees may be eligible for temporary tax credits to encourage them to offer coverage.⁴ Many small businesses will also be eligible to purchase group medical plans from SHOP (Small Business Health Options Program) exchanges, although the company size cutoffs may vary by state. As the new regulations go into effect, the only sure outcome for the small business market is a lot of uncertainty over the next few years.



Key Findings

- ▶ **Most firms do not want to drop medical coverage.** In the face of continued inflation of medical costs, small businesses are much more likely to consider dropping *nonmedical* products or switching these benefits to voluntary-funding arrangements rather than eliminating medical plans. To avoid these losses, the benefits industry will need to focus its attention on increasing awareness among small businesses of the value of nonmedical products.
- ▶ **Small employers are not optimistic about health reform.** Less than one third of small firms expect health reform to have a positive impact on their business, while many expect a negative outcome. However, these attitudes are strongly colored by personal political views on the issue and may not be predictive of the actual results.

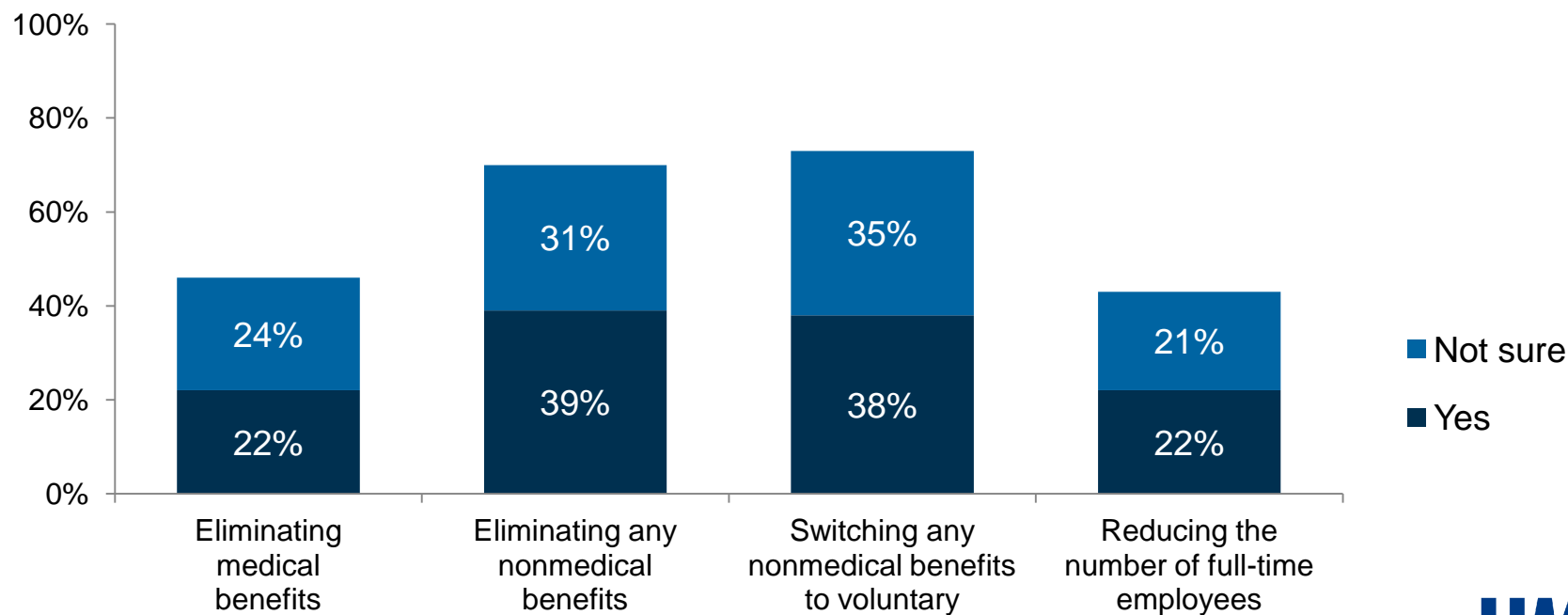
⁴ Explaining Health Care Reform: How will the Affordable Care Act affect small businesses and their employees?, Kaiser Family Foundation, 2012.

Responses to Rising Health Care Costs

- ▶ Small businesses are concerned about the escalating cost of offering health benefits, and suggest several courses of action they may consider if costs continue to rise. While medical plans are by far the most expensive insurance benefits offered, only 22 percent of small employers would consider eliminating these benefits due to rising costs. In contrast, nearly twice as many small businesses would choose to eliminate nonmedical benefits to control costs.
- ▶ Nearly 4 in 10 small employers would consider switching a presently offered nonmedical benefit from employer-subsidized to voluntary in response to rising health care costs.
- ▶ Small employers' reactions are strongly influenced by their patterns of growth. Those that have experienced recent negative growth are most likely to consider all of these potential changes.

Figure 12: Possible Responses to Rising Health Benefit Costs*

If the cost of your health benefits increased 8 percent annually over the next 3 years, would your company consider:



* Based on small employers that offer benefits.

Attitudes About Health Care Reform

- ▶ Small employers tend to be pessimistic about the impact that the health care reform law will have on their overall business, employees, and ability to nonmedical benefits. Firms with fewer than 10 employees have a somewhat more positive view of the legislation than do larger firms. In addition, home-based, female-owned, and minority-owned businesses are more likely to take a positive stance.

Figure 13: Expected Impact of Health Reform in the Next 3 to 5 Years*

Expected impact on your overall business:



Expected impact on your employees:



Expected impact on your ability to offer nonmedical benefits:



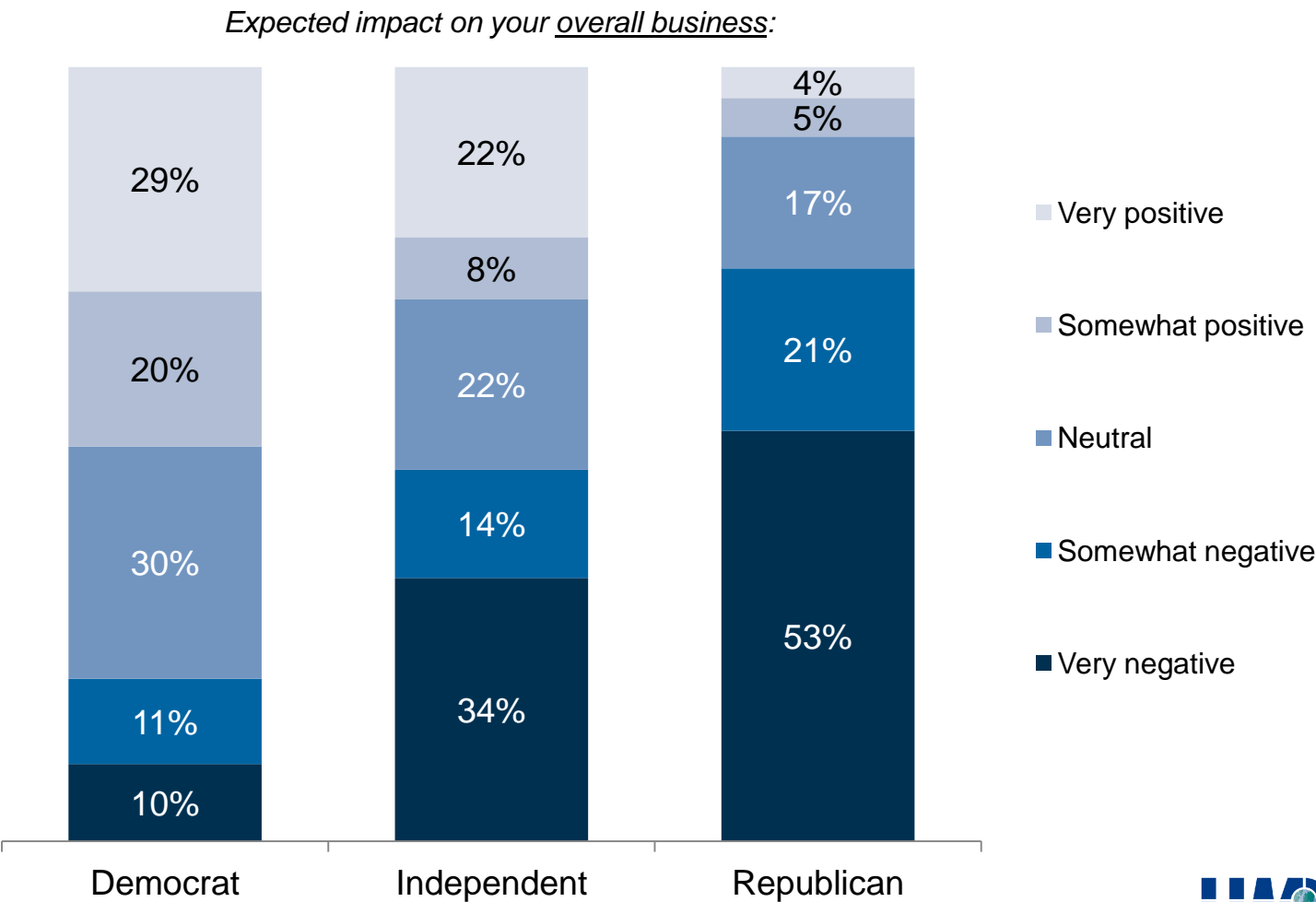
■ Very negative ■ Somewhat negative ■ Neutral ■ Somewhat positive ■ Very positive

* Based on small employers that offer benefits.

Attitudes About Health Care Reform

- ▶ The heavily partisan nature of the health care reform debate also appears to have had a strong impact on small business opinions. Attitudes about health reform are significantly impacted by the political beliefs of the benefits decision-maker.

Figure 14: Expected Impact of Health Care Reform by Political Affiliation*



* Based on small employers that offer benefits.



- ▶ In January 2013, LIMRA conducted an online survey of U.S. small businesses to explore a variety of topics pertaining to employee benefits. The survey included 1,184 private small businesses with 2 to 99 employees (including the owner) that had been in business for at least one year. Respondents were the individuals that made or shared in the firms' decisions concerning employee benefits.
- ▶ The sample was weighted by company size and industry to be representative of the total population of U.S. small businesses, based on data from the U.S. Census Bureau.
- ▶ The data presented in this report is from the second phase of a two-phased series of research on small business.

Call...
LIMRA*first*

Research • Assessment & Development • Consulting • Compliance



HARTFORD • ATLANTA • TORONTO • LONDON • KUALA LUMPUR • SHANGHAI • TAIPEI • HONG KONG • MEXICO CITY

© 2013, LL Global, Inc.SM

300 Day Hill Road, Windsor, CT 06095-4761, U.S.A.

Phone: 860-688-3358 • Fax: 860-298-9555 • Web: www.limra.com