

The Impact of the Affordable Care Act on Self-Employment

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Subcommittee on Contracting and Workforce**

**At the hearing on
*Obamacare and the Self-Employed: What About Us?***

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Thank you, Chairman Hanna and Ranking Member Meng, for inviting me to address the Subcommittee on the impact of the Affordable Care Act (ACA) on self-employment. I will make three points in my testimony.

- 1) There is considerable research showing that the fear of losing health insurance coverage discourages workers from leaving a job that provides insurance to start their own business. By allowing workers to get affordable insurance through the individual market the ACA will substantially increase the rate of small business formation.
- 2) There is also evidence that workers leave jobs that do not provide insurance to get jobs that do provide insurance. Since many small businesses have found it difficult to provide insurance for their workers, their ability to get insurance through the individual market should make it easier for small businesses to retain workers.
- 3) The rate of health care cost growth has slowed sharply over the last six years. While the exact reasons for this slowdown are disputed, it is almost certain that the ACA played some role. This slowdown in health care cost growth has reduced the burden for many small businesses that provide insurance.

For these reasons, the ACA is likely to prove to be a strong net positive for small businesses, leading more to be started and making it easier for the existing businesses to prosper.

The Impact of Employer-Provided Insurance on Self-Employment

There is an extensive literature examining the impact of employer-provided health insurance (EPHI) on self-employment. The basic issue is whether workers fear the prospect of being

uninsured and therefore are less likely to leave a job that offers health insurance to start their own business than would be the case if they were not dependent on their job for insurance. While studies using data from the 1980s were inconclusive on this issue, several recent studies found strong evidence showing that EPHI discouraged workers from starting their own businesses.

For example, a recent study pooled eleven years of data from the Bureau of Labor Statistics' Current Population Survey (CPS) (1996-2006) to determine whether workers with EPHI were more likely to experiment with self-employment if they were able to get insurance through their spouse than if they had no alternative source of health insurance.¹ As a result of pooling so many years of data from the CPS, the study was able to get a very large sample, with 81,214 employed men and 75,317 employed women between the ages of 25-64. In statistical tests that controlled for a variety of personal characteristics (e.g. education, age, industry), the analysis found sharply lower rates of transitions to self-employment among workers with EPHI who could not get insurance through their spouse. This result held up across a number of different specifications, which indicates that it was not driven by a statistical fluke.

The study then examined the rate at which workers started new businesses as they turned age 65 and became eligible for Medicare coverage. The study found a sharp increase in the rate of self-employment as workers reached the age of Medicare eligibility. There was no comparable upturn in self-employment around other landmark birthdays, such as age 55 or 75, suggesting that hitting the age of Medicare eligibility was the key factor. Once workers were no longer dependent on their job for insurance, they were more willing to try their chances with starting a new business.

Another recent study examined whether the creation of Individual Health Coverage Plan in New Jersey in 1993 led to an increase in self-employment compared with neighboring states and the rest of the country.² This study used the Behavioral Risk Factor Surveillance System (BRFSS) for the years 1991 to 1996 to determine if there was a difference in the rate of self-employment in New Jersey in these years compared with those in surrounding states and the rest of the country. The study looked at individuals between the ages of 25-59. This gave a sample size of 18,409 for the Pennsylvania comparison, 40,880 for the Mid-Atlantic states, 66,893 for the Northeast region, and 382,670 for the comparison with the country as a whole.

¹ Fairlie, Robert W., Kanika Kapur, and Susan Gates. 2011. "Is Employer-Based Health Insurance a Barrier to Entrepreneurship?" *Journal of Health Economics*, vol 30, pp. 142-162.

² DeCicca, Phillip. 2010. "Health Insurance Availability and Entrepreneurship," Upjohn Institute Working Paper, no 10-167.

The analysis found solid support in each case for an increase in self-employment in New Jersey relative to the comparison group. The implied increase in self-employment from the insurance reform was between 16-20 percent.

Finally, a recent study examined whether the ACA's requirement that children up to the age of 26 could remain on their parents' insurance policy increased the rate of self-employment among workers between the ages of 19-25.³ The study used the Census Bureau's American Community Survey to compare the change in rates of self-employment among this age group in the period just after the provision just took effect, with changes in self-employment rates among workers a little younger or older (ages 17-19 and 27-33) who would not be affected by the provision. This gave them a sample of 2,637,376.

The study consistently found evidence of an increase in self-employment among the affected age group in a variety of specifications. The implied increase in self-employment was 13-24 percent. This result is especially striking since this is an age group in which we would not expect health care insurance to be an especially important consideration.

These three studies examined the impact of EPHI on self-employment using very different tests and completely different data sources. In all three cases the sample sizes were quite large. (By comparison, some of the earlier studies had samples with around 1000 workers.) Based on the findings of these and other studies, it is reasonable to conclude that the ACA will increase self-employment by between 15-25 percent when its effects are fully felt in the next few years.

The Impact of the ACA on Job Retention at Small Businesses

The overwhelming majority of large businesses provide insurance to their workers. Many small businesses find it difficult or impossible to provide insurance to their employees. This is partly due to the fact that a smaller pool of workers is likely to face higher costs and also simply a result of the fact that arranging insurance can involve a substantial commitment of a business owner's time. However, not providing insurance can leave small businesses at a serious disadvantage in hiring and retaining workers compared with larger competitors.

Several studies have examined a "job push" pattern, where workers leave jobs with which they were otherwise satisfied in order to find a job that provides health insurance. This pattern was

³ Baily, James. 2013. "Health Insurance and the Supply of Entrepreneurs: New Evidence from the Affordable Care Act's Dependent Coverage Mandate." Available at SSRN: <http://ssrn.com/abstract=2230099>

most closely examined in a 1997 study that used the National Longitudinal Youth Survey.⁴ This study examined job changes among men between the ages of 20-27 in 1989. The sample had 5,305 job spells.

This study found that married men working at jobs without EPHI were substantially more likely to quit their jobs when their spouse became pregnant. This would seem to imply that workers became more concerned about finding insurance through an employer when they suddenly faced a greater need for in insurance. While most of the research on this topic has focused on the extent to which EPHI discourages workers from leaving a job where they have insurance, this study and others provide evidence that the need to get insurance is also an important factor leading workers to leave jobs that do not offer insurance.

For this reason, the ACA should be an important factor in leveling the playing field for many small businesses. Since workers will now be able to buy affordable insurance in the individual market, they will not feel the need to leave jobs that don't provide insurance in order to make their families secure.

The Impact of the ACA on Health Care Costs

There has been a lot of attention given to the ways in which the ACA may lead to higher insurance costs. Specifically, by setting minimum standards for acceptable policies, there will be cases where individuals or employers have to pay more than they did when they held policies that did not meet these standards. While there are cases where the ACA has caused some policies to cost more, it is important to note that this is against a backdrop of sharp slowdown in health care costs. Health care costs have consistently risen as share of GDP for more than sixty years. Their share of GDP has been virtually flat in the last four years and actually fell slightly in 2013.

To get an idea of how important this slowdown in health care costs has been, in 2008 the Congressional Budget Office projected that the country would spend \$671 billion Medicare in 2014.⁵ The most recent projections show that the government will spend just \$603 billion in 2014, a savings of 10.1 percent.⁶ Most other areas of health care spending have seen a comparable slowing of costs. This means that most health insurance policies will cost less in 2014, even with the requirements imposed by the ACA, than if health care costs had continued

⁴ Anderson, Patricia M. 1997. "The Effect of Employer-Provided Health Insurance on Job Mobility: Job Lock or Job Push?" Unpublished Paper, Dartmouth College.

⁵ Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2008-2018*, Table 3-1.

⁶ Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2014-2024*, Table 3-1.

on their previous trajectory and the ACA had not been passed. If this slower growth persists then the savings will be even larger through time.

At this point the causes of the slowdown in health care cost growth are not clear. While the economic downturn in 2008 was undoubtedly a factor in the slowdown, the recession can't explain why cost growth has remained slow even as the economy has recovered in the last few years. It will take longer to determine the extent to which cost containment provisions in the ACA have been responsible for slowing the growth in health care costs, but they almost certainly played some role in this dramatic reduction in the pace of health care inflation.

This is certainly good news for employers who provide health insurance coverage. Most immediately this has lessened an important source of cost pressure on businesses. In principle, this slower pace of cost growth should allow workers to earn higher wages in the years ahead.

Conclusion

The main motivation for the ACA was to extend insurance coverage to people who did not have it; however the law will also have important implications for the labor market. A substantial body of research implies that workers who previously felt tied to their jobs because of the need to get insurance from their employers will now more readily change jobs. Many more workers will also be willing to experiment with starting their own businesses.

In addition, many workers had previously left jobs that did not offer insurance in order to find a job that did. Now that workers are able to get insurance in the individual market, more workers will remain employed at small businesses that are not able to offer insurance.

Finally, there has been a sharp slowdown in health care cost growth over the last six years. The ACA was one of the factors behind this slowing of health care inflation. This has substantially reduced the cost of most insurance policies compared with their prior path. This will lead to large savings for businesses that provide insurance.

For these three reasons, the ACA has been a substantial benefit for small businesses. This will become more apparent as the impact of the law is increasingly felt over the next few years.