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Small Businesses' Premiums Soar After One Illness

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To understand the challenges of insuring the health of the nation's work force, consider Varney's Book Store.

After a long bout with emphysema an employee at Varney's, a family-owned business in Manhattan, Kan., died several years ago. But for Varney's health insurer, her legacy lived on.

The next year, 2002, the insurer raised Varney's premiums by 28 percent — even though most of the other three dozen employees were significantly younger and healthier than their departed colleague, who had been in her mid-70's. And Varney's premiums continued to climb.

"It was as if her medical history stayed on the books for an additional three years," said Jeff Levin, 46, who runs Varney's with his younger brother. "How can you justify projecting those costs forward?"

Such are the challenges for smaller businesses in Kansas and the many other states where laws permit insurers to raise health premiums substantially for small employers when one worker incurs significant medical bills.

And it is why, as state legislatures, Congress and presidential candidates of all stripes debate the growing problem of Americans without health insurance, the struggles of small businesses — which employ about 40 percent of the nation's work force — are likely to become a central issue. Small-business employees are one of the fastest-growing segments of the nation's 44 million uninsured; they now represent at least 20 percent of the total, according to federal census data. And even modest-size employers like Varney's that say they remain committed to providing benefits find themselves wondering how long they can continue.

The challenges make small business a particularly tricky piece of the nation's health care puzzle, a problem compounded by the state-by-state jigsaw nature of insurance regulation.

"There are 50 sets of state rules," said David Fear, an insurance agent in Sacramento, who is president of the National Association of Health Underwriters, an agents' trade group.

With the rising cost of insurance, even the nation's biggest employers are struggling to cover their workers. But large companies at least wield some influence with insurance underwriters and providers of care, and are usually solvent enough to insure themselves as an alternative to the insurance market. Either way, they can spread their health costs over a pool of employees large enough that any one worker's medical bills do not make big financial waves.

But small employers cannot exercise those economies of scale. And because they typically are not rich enough to insure themselves, they are almost wholly dependent on insurance companies to provide health benefits. In the many states that do not closely regulate health coverage, small businesses have little bargaining power with the insurers.

In a small workplace, as a result, if an employee or a covered dependent becomes seriously ill, or if someone has even a routine medical need like maternity care, the entire group may pay the price through steeply higher insurance rates.

"Almost any kind of situation where one employee has a serious health condition almost makes the group uninsurable, because of cost," said the governor of Kansas, Kathleen Sebelius, a member of a group studying health care issues for the National Governors Association. "Affordable coverage for small-business owners and self-employed individuals is probably the biggest challenge that we have in Kansas and most states."

Ms. Sebelius, a Democrat, is currently at work on a bipartisan proposal with the state's Republican insurance commissioner that would insulate small groups by having the state provide backup insurance for the most expensive medical cases.

"If the insurer was guaranteed never to have to pay out over $100,000, for example, it could be a much more stable situation," she said.

But that only applies a patch to a bigger wound. In Massachusetts, which has embarked on a widely watched effort to make health insurance mandatory, the state plans to address the small-business issue by combining 800,000 small employers and 50,000 individuals into a single pool as a way to even out costs and increase their bargaining power.

Over the years, small employers around the country, often led by chambers of commerce, have occasionally sought to band into regional groupings. But the efforts often led nowhere — especially because insurers tend to assume that many young, healthy workers will opt out, leaving them saddled with older, sicker enrollees.

That is a big reason Massachusetts will require the young and healthy to join the pool, or pay into a state insurance fund if they choose not to buy coverage for themselves.

The insurance rules already in place in some states do provide various buffers for small businesses.

Nine states, for example, prohibit insurers from considering the health status of workers when setting rates for small groups. Those include Connecticut, New York, New Jersey and Maryland.

A number of states also limit the size of yearly rate increases. Rates in California, for example, typically can rise no more than 10 percent.

But in many other states it is essentially every mom-and-pop for itself. Kansas allows rate increases of up to 25 percent a year. Ohio permits 40 percent. In Arizona the annual jump can be 60 percent or more. And for Pennsylvania, Virginia, Hawaii and the District of Columbia, there are no ceilings at all.

When the rates can leap with each new employee illness, the only recourse may be shopping for another insurer. That is what Varney's did in 2005.

The bookstore, popular with students at Kansas State University, switched its coverage to Blue Cross and Blue Shield of Kansas after the previous insurer said it would raise Varney's premium by 17 percent. The reason was that another employee, a 59-year-old woman who was a longtime Varney's bookkeeper, died of stomach cancer the previous year.

Varney's former carrier, Trustmark Insurance, based in Lake Forest, Ill., declined to discuss the case's specifics. A Trustmark spokesman would say only that the bookstore had fared no worse over the years than the typical small employer.

"Over time, it appears that their aggregate rate increase was less than the national trend," said the spokesman, Patton Hollow.

Blue Cross currently charges Varney's about $16,500 a month. The Levins pay 80 percent of that, asking their employees to pick up the rest. A typical share, for an employee and spouse, requires a monthly paycheck deduction of about $115.

Even in states that impose government caps on rate increases, those protections may not cover all contingencies.

Despite the 40 percent ceiling in Ohio, for instance, United Healthcare early this year levied an increase of more than 100 percent on the premiums of CBG Biotech, a 26-employee hospital supplies maker in Macedonia, near Akron. The insurer argued that the high increase was justified because CBG had violated its contract.

Ohio permits insurers to solicit advance medical information from employees. One CBG worker had failed to disclose his wife's multiple illnesses — including cirrhosis, gout and an ulcer — when he signed up for coverage, according to a letter from United that became part of a court record.

When United learned of the omission after the woman was admitted to a hospital, where she died, "they decided to punish the entire company," said CBG's chairman, Gerald W. Camiener.

United raised CBG's total premium for the duration of the contract to $18,000 a month, from $8,800, he said, and demanded $118,000 in back payments.

CBG sought a federal injunction against the increase. In February, Judge Ann Aldrich of the United States District Court in Cleveland denied the CBG request, saying that United Healthcare's actions were permissible under its contract and "very likely legal, but also very far from laudable."

Mr. Camiener, in an e-mail message, lamented that ruling. "In the past, the policy of health insurers was to disqualify the employee when wrong information was furnished to them," he wrote.

"Now," he continued, "the insurers will be coming to the employer and demanding exorbitant sums of money with the threat that the entire group will be cut off forthwith, even in the middle of a policy year." Mr. Camiener changed his company's health coverage to Aetna, paying about $15,400 a month in premiums, and he complained to senior executives at United.

Kenneth A. Burdick, United Healthcare's president, said in an interview that his company had now decided to drop its demand for back payments from CBG and would no longer seek retroactive rate increases in such cases. He also said that because misrepresentation by employees was rare, with only a dozen or so cases a year among thousands of business groups, senior United Healthcare officials would now review the facts in each case.

Back in Kansas, meanwhile, Varney's owners say they are doing what they can to keep their health premiums in check.

Mr. Levin, 46, says he has been a fitness enthusiast since he had a heart attack in 2002. He says he has stopped smoking ("except for one cigar a year") and has improved his diet, supplementing it with fish oil pills.

And Varney's has made gym memberships a free perk for all employees. "Our managers can even use a trainer two to three times a week at our expense," he said.

All that may help the Varney's work force stay healthy. But so far, he said, Blue Cross has declined to reward the effort with any additional break on insurance premiums.

Graham Bailey, a Blue Cross spokesman, said that if the fitness efforts actually resulted in lower medical expenses, that could eventually reduce Varney's premiums.

For now, though, there is little the company can do.

"Since we're family-owned, we have the latitude and commitment to make sure our employees and their families are provided access to health coverage," Mr. Levin said. "My brother and I worry, though, that over time it will keep getting more and more expensive and be out of reach."