



Small Business: Big Growth Opportunity

FOR GROUP/VOLUNTARY
BENEFITS INSURERS

White Paper

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Introduction

Small businesses (with less than 100 employees) offer a potentially tremendous growth opportunity area for group/voluntary benefits insurance companies, but present unique challenges. Small groups bring difficult access, cost, enrollment, and underwriting challenges that require creative solutions. First, small businesses and their employees find it difficult to afford health insurance and other types of employee benefits (including group/voluntary benefits insurance products). Second, small business employees often lack the in-person education and advice to know when it makes sense to enroll in group/voluntary benefits products. Third, time starved and budget constrained small business owners require the easiest, lowest cost possible way for their employees to enroll in benefits products, including group/voluntary benefits products. Fourth, group/voluntary benefits insurance companies often find it too expensive to underwrite and price small group coverages accurately using traditional approaches.

Health insurance costs have become so high, approximately \$20,000 per year for the average four-person family, that many small businesses simply cannot afford to offer health insurance to their employees.ⁱ Less than half of the 30 million U.S. small businesses offer health insurance to their employees and less than 25% of small business employees access health insurance through their employers, with the numbers continuing to decline each year.ⁱⁱ If these businesses cannot afford to offer core health insurance to their employees, then they also cannot offer voluntary benefits insurance products in general, and especially not in the correct context of supplementing, not replacing, core health insurance benefits.

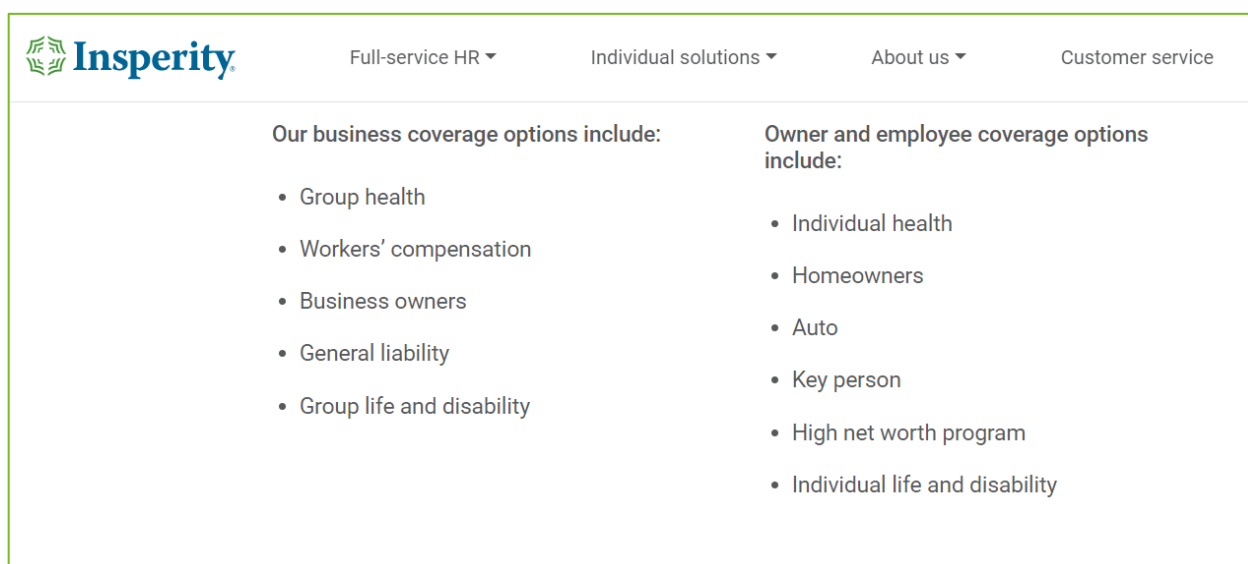
1. PEOs Provide the Best Option for Small Businesses to Access Lower Cost Health Insurance

Professional employer organizations (PEOs) offer a range of services to small businesses, including payroll processing, benefits administration, HR training and support, and workplace insurance coverage. PEOs combine the employees of multiple small businesses to create one larger pool of employees, which enables the PEO to provide access to employee benefits similar to what would be offered at a larger corporation.

Insurance Option	Advantages	Disadvantages
Small group health insurance plan	<ul style="list-style-type: none"> • Claims risk assumed by health insurance company • No medical underwriting for employees 	<ul style="list-style-type: none"> • Often very expensive because of the small number of employees and the underwriting and pricing risk for health insurer
Self-insure for health insurance	<ul style="list-style-type: none"> • Don't pay the profit margin to the health insurance company 	<ul style="list-style-type: none"> • Claims risk assumed by the small business • Small business has the administrative burden of managing the claims
QSEHRA – Qualified small employer health reimbursement arrangement	<ul style="list-style-type: none"> • Allows small businesses, other groups with fewer than 50 employees to reimburse workers tax-free for health care expenses. 	<ul style="list-style-type: none"> • Reimbursement limits to employees of only \$10,500 is not enough • Business owners aren't included – only employees • Administrative burden to the small business for tracking the claims
Health Savings Accounts (HSAs)	<ul style="list-style-type: none"> • Employees fund accounts with pre-tax dollars and then accumulate money tax-free to pay for health insurance costs. • Employees pay lower premiums for group health insurance because of high deductibles. 	<ul style="list-style-type: none"> • High deductibles. \$7,200 for a family, so HSAs work best for healthy people and families and those employees who are not risk averse about future health costs.
Professional Employer Organization (PEO)	<ul style="list-style-type: none"> • Leverage the buying power of multiple small businesses to access group health insurance at a better price. • Outsource overall HR and benefits function (including managing health insurance claims) to focus resources on business growth. 	<ul style="list-style-type: none"> • Somewhat expensive – typically 3-15% of overall payroll outlays but average HR administrative costs per year per employee are \$450 lower, on average. • Limited choice. Have to use the health insurance company or company chosen by the PEO. • Cost effective only if small number of employees.

PEOs provide services to 175,000 small and mid-sized businesses (a small fraction of the overall 30 million small businesses), employing 3.7 million people, with the number of covered employees growing nearly 10% per year.ⁱⁱⁱ This growth should accelerate, given the relative advantages of using PEOs for overall benefits management and access to more affordable health insurance. 2 out of 3 of the current 175,000 small businesses served by PEOs are white collar (information technology, financial services, professional services), with the attractive mortality/morbidity characteristics associated with higher income, more health-conscious types of employees, making this an attractive risk pool.

There are 907 PEOs in the U.S., but three companies currently dominate this market – ADP with 23% market share, Trinet with 19% market share, and Insperity with 10% market share.^{iv} A big opportunity exists for group/voluntary benefits insurance companies to fit their product offerings into the overall employee benefits offerings of PEOs. See the below screen shot for Insperity – they do not currently include core voluntary benefits like critical illness or hospital indemnity as part of their insurance offering. Vitech's research estimates that at least half of PEOs lack voluntary benefits insurance offerings, creating a major opportunity for voluntary benefits insurance companies and their distributors to fill these gaps.



The screenshot shows the Insperity website header with navigation links: Full-service HR, Individual solutions, About us, and Customer service. Below the header, there are two columns of coverage options.

Our business coverage options include:	Owner and employee coverage options include:
<ul style="list-style-type: none"> • Group health • Workers' compensation • Business owners • General liability • Group life and disability 	<ul style="list-style-type: none"> • Individual health • Homeowners • Auto • Key person • High net worth program • Individual life and disability

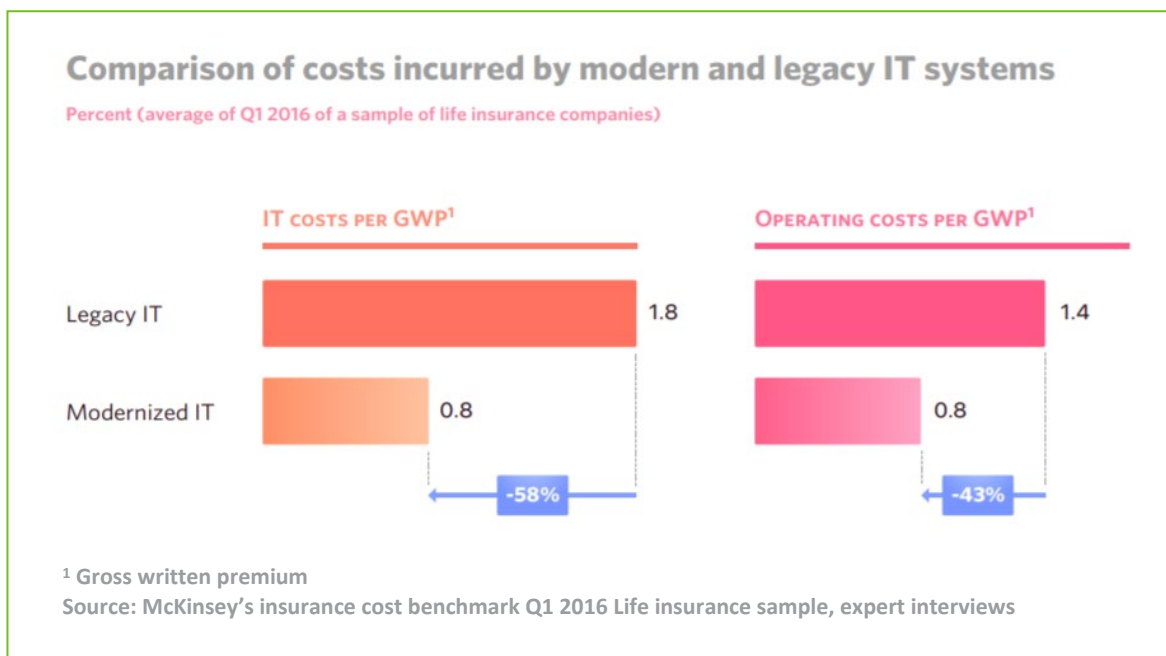
2. Find Benefit Administration Partners That Will Explain Group/Voluntary Benefits Products to Employees

Just providing access to group/voluntary benefits products to small businesses, via PEOs or otherwise, isn't enough. 67% of employees find shopping for or enrolling in benefits either too complicated, too time consuming, or too stressful.^v Employees want a simplified, Amazon-like comparison shopping experience. Group/voluntary insurance companies should work with human resource information system (HRIS) and employee benefit enrollment vendors to place their products in the right context for enrollees – not just as an afterthought at the end of the process. For example, for younger employees with children involved in sports with a concern about high deductibles or co-pays for sprained ankles or other sports injuries, recommend accident coverages. For older employees concerned about future hospital stays that may exceed their core health insurance maximums, recommend hospital indemnity coverages. Work with your core administration vendor to build standard interfaces to the HRIS and enrollment vendors that provide the most common and the best enrollment experiences for employees.

For overall employees with access to group/voluntary insurance products, Eastbridge Consulting has found that less than 1 out of 3 employees choose these products despite high satisfaction rates for those that do.^{vi} Aflac has found insufficient education and advice as the leading reason for non-enrollment.^{vii} Future social distancing requirements will make in-person education and ongoing advice difficult, so Zoom and other video conferencing applications will become increasingly important to provide ongoing employee benefits education and advice to employees. Use wholesalers to educate PEOs or other benefit administration partners that can provide a dedicated person or team responsible for clearly explaining employee benefits products, including group/voluntary benefits insurance products, within the individual contexts of small business employees. Make sure that this education and advice can be ongoing, in person and/or virtual, and not just once a year during open enrollment, to maximize enrollment rates.

3. Drive Down the Costs of Group/Voluntary Benefits Products With Core System Modernization

Employers of all sizes indicate cost as the most important reason why employees do not enroll in voluntary benefits products, and this is most pronounced for budget and resource-constrained small businesses. Across all lines of businesses at life insurance companies, McKinsey has found an opportunity to reduce unit operating costs, on average, by over 40% via process standardization and simplification, increased rates of straight through processing, customer self-service, and other digital operations types of savings derived from replacing legacy core systems with modern core systems.^{viii} To increase efficiency further, standard application programming interfaces (APIs) from modern core administration services to preferred HRIS and enrollment vendors will streamline the onboarding of new small business clients or benefit administration partners, maximize straight through processing rates for enrollment and ongoing servicing, and fit seamlessly into the preferred enrollment and servicing portal offerings used by small business employees.



4. In the Future, Use New Approaches to Predictive Analytics to Make Underwriting More Accurate and Cost-Effective

Driving down unit costs will not be enough to drive growth of group/voluntary benefits businesses. The small number of employees at small businesses makes it cost prohibitive not only to service these clients but also to underwrite and price them. Traditional, large group approaches of reviewing claims histories and census files that include basic employee demographics data generate too much expense and fail to provide good enough predictive information about the likely future frequency and severity of future claims, leading to suboptimal risk selection and pricing. A number of group/voluntary benefits insurance companies have reviewed third party data access and risk scoring approaches for small groups (using motor vehicle records, prescription drug histories, medical information bureau information, and electronic health record data) but found the data access to be too expensive when done on a case by case basis. In the future, innovative insurance companies and their predictive analytics scoring providers should pre-negotiate promised data access volumes over long periods of time to access the necessary third-party data cost effectively for initial and ongoing risk scoring for small groups. Automated, cost effective underwriting and risk scoring for small groups will enable and accelerate profitable growth for group/voluntary benefits insurance companies. This has already happened in other areas of insurance like small group workers compensation and small group health insurance.

Conclusion

Group/voluntary benefits insurance companies need strong technology partners to help them realize the many opportunities available in this market, including the small business growth opportunity enablement areas described above. Whether it be simplifying the administration needs of small businesses via increased rates of straight through processing, making it easier to integrate with the widening array of enrollment, HRIS, PEO, and other vendors to streamline the enrollment process, or, in the future, having access to next generation types of predictive analytics capabilities for underwriting, claims, and other high impact domain areas, Vitech looks forward to helping our clients position themselves for powerful, long term growth in the group/voluntary benefits insurance market.

ABOUT VITECH

Vitech is a global provider of cloud-based benefit and investment administration software. We help our clients expand their offerings and capabilities, streamline their operations, gain analytical insights, and transform their engagement models. Vitech employs over 1,200 professionals serving over 100 of the world's most successful insurance, retirement and investment organizations. An innovator and visionary, Vitech has been recognized by Gartner as a Magic Quadrant "Leader" for three years running and by Celent as a three time XCelent award winner. For more information, please contact us at info@vitechinc.com or visit our website at www.vitechinc.com.

ⁱ Kaiser Family Foundation. 2019 Employer Health Benefits Survey. <https://www.kff.org/report-section/ehbs-2019-section-1-cost-of-health-insurance/>

ⁱⁱ The Commonwealth Fund – The Health of the Small Group Insurance Market. <https://www.commonwealthfund.org/publications/issue-briefs/2018/oct/health-small-group-insurance-market>

ⁱⁱⁱ National Association of Professional Employer Organizations – Industry Statistics. <https://www.napeo.org/what-is-a-peo/about-the-peo-industry/industry-statistics>

^{iv} National Association of Professional Employer Organizations – Industry Statistics 2017 <http://netprofitgrowth.com/peo-industry-statistics-2017/#:~:text=The%20industry%20report%20states%20that,figure%204%20and%20figure%205>.

^v AFLAC Workforces Report - <https://www.paycom.com/resources/blog/74-of-employees-confused-about-health-care-benefits/>

^{vi} Eastbridge Consulting Group. <https://www.benefitnews.com/news/voluntary-enrollment-rates-rise-higher-than-predicted>

^{vii} AFLAC Workforces Report. <https://www.aflac.com/docs/awr/pdf/2018-overview/2018-aflac-workforces-report-employee-overview.pdf>

^{viii} McKinsey – Digital Disruption in Insurance – Cutting Through the Noise <https://www.mckinsey.com/~media/mckinsey/industries/financial%20services/our%20insights/time%20for%20insurance%20companies%20to%20face%20digital%20reality/digital-disruption-in-insurance.ashx#:~:text=This%20compendium%E2%80%94Digital%20disruption%20in,30%20executives%20whom%20we%20interviewed.&text=All%20shared%20their%20insights%20on,why%2C%20and%20where%20success%20lies>.