

Small and Micro Businesses: America's Growth Engine

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Small and Micro Businesses: America's Growth Engine

» Introduction

Since 1982, the number of small and micro businesses in the U.S. has **increased by 49%**, to between **27.9 million** [PDF] and **42 million** entities. Several factors have impacted this growth, including shifts in large businesses toward hiring independent contractors (rather than fulltime employees) and evolving generational values, with younger professionals often prioritizing flexibility over stability. Analysts predict that these trends will accelerate in coming years, cementing the transition toward a "freelance economy."

But with their increased presence in the U.S. economy comes an increased exposure to litigation for micro businesses. The U.S. Chamber of Commerce's Institute for Legal Reform reports that **more than half of all tort cases in the U.S. (57%) target businesses with less than \$1 million in revenue** – and fully one in three small U.S. businesses has been either threatened or actually charged with a lawsuit. Those lawsuits cost micro businesses billions of dollars in legal fees – costs which are then passed on to customers. This means that commercial liability insurers, by helping micro businesses

minimize lawsuit expenses with appropriate insurance products, have a tremendous opportunity to reduce costs to both business owners and the customers they serve.

Promisingly, the process of connecting with and educating micro businesses in need of liability protection may be easier now than ever before. Research shows that, as of 2013, the majority of business owners are comfortable purchasing commercial insurance products online.

This finding is reinforced by search engine analytics, which show precipitous increases in search terms related to business insurance.

This report examines growth trends for small and micro businesses in recent years, the sector's need for liability protection to increase revenue and retain customers, and the role insurance advisors can play in facilitating micro business growth.



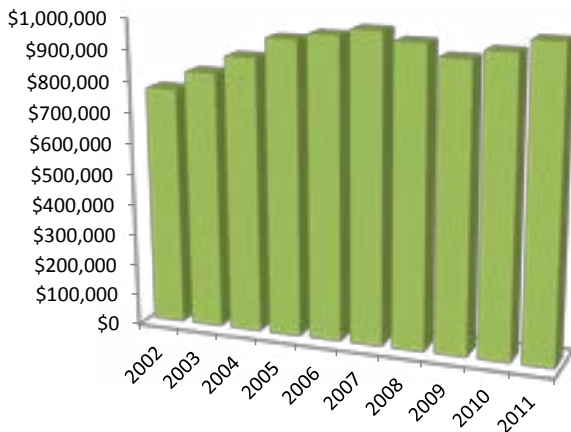
Source: <http://www.sba.gov/content/small-business-trends>

» Part I: Small and Micro Business Growth

A number of factors have influenced the growth of small and micro businesses in recent years, not least of which was the Great Recession of 2008. But the shift away from big-company employment extends beyond the impact of the country's recent economic turmoil. According to the Small Business Administration, the trend away from employment by large companies and toward self-employment or employment by smaller firms has been gaining momentum since 1990: in the last 23 years, large companies have eliminated 4 million jobs while **smaller firms have added 8 million**.

The 2010 Census showed that the nation's 27.9 million small businesses include 21.9 million non-employers (those that have no employees – often sole proprietors or partnerships), which means micro businesses account for at least 78.5 percent of all small businesses. In comparison, there are only 18,500 businesses with 500 or more employees currently operating in the U.S.

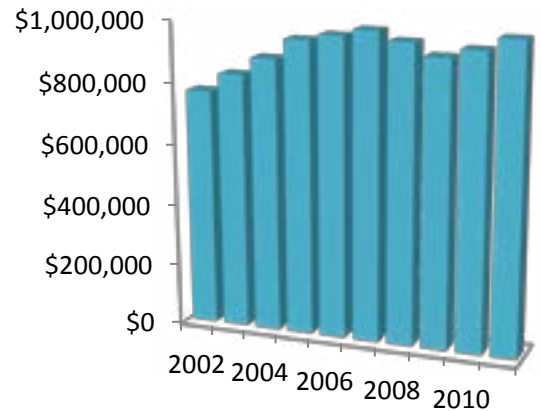
Increase in Non-Employer Businesses, 2002 - 2011



Source: US Small Business Administration

It is difficult to overstate the importance of smaller businesses on the overall economic health of the U.S. economy, especially in the post-recession economic landscape. The Atlantic claimed in a [2011 article](#) that the shift in the U.S. toward a "freelance economy" is no less significant for the nation's economic infrastructure than the changes brought on by the Industrial Revolution, when the U.S. transformed from a nation of farmers to a nation of factory workers. This bold claim is supported by data: since the recent recession, small businesses have been responsible for two-thirds of new jobs, and the National Federation of Independent Business (NFIB) recently reported that, despite woes related to the federal government shutdown in October, NFIB members **increased employment slightly** (by an average of .11 workers). As of 2011, non-employers alone accounted for \$989.0 billion in revenue, with the average revenue per non-employer business clocking in at \$44,000.

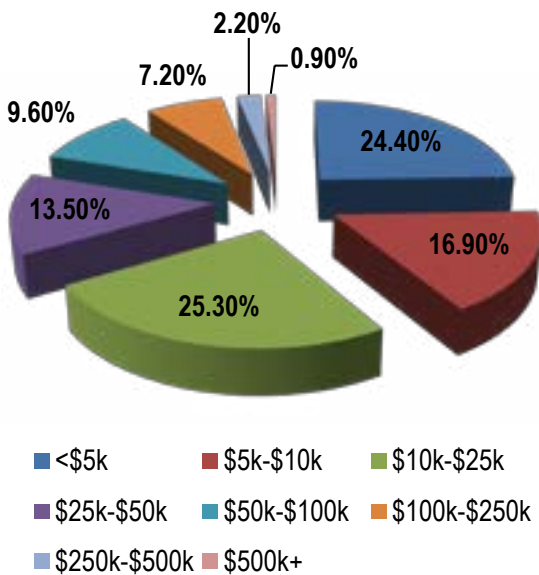
Increase in Non-Employer Business Revenue, 2002 - 2011



Source: US Small Business Administration

These numbers are only expected to grow in the coming years. The Freelancers Union estimates that 42 million people currently work as freelancers or independent contractors at least part-time (we discuss below the significance of the gap between the 42 million figure and the SBA's 27.9 million number). **That accounts for one in three working Americans.** In 2005, only 10.5 million Americans worked on a freelance basis. If current trends – both in [large company layoffs](#) and in a preference for flexibility among younger professionals – continue, freelancers will [outnumber full-time workers by 2020](#) – less than seven years from now. This [shift toward freelance work](#) was made possible in no small part by the dawn of the Internet, which eliminated the need for proximity of qualified workers to the physical location where their expertise was needed.

Non-Employer Business Revenue, 2011



Source: US Small Business Administration

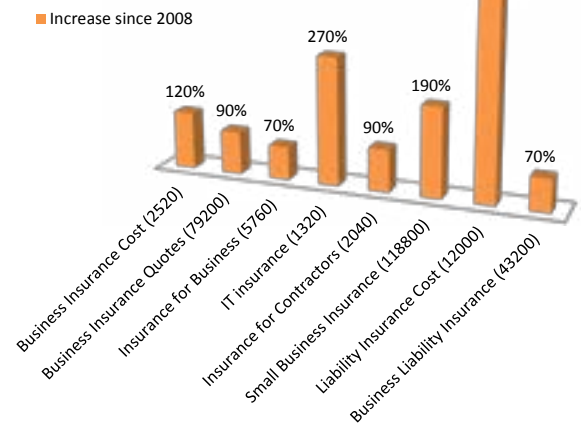
» Part II: The Rising Demand for Online Business Insurance

Given the increasing reliance of today's small businesses on the Internet to secure clients and complete projects, it comes as no surprise that small businesses are also turning to the Internet for insurance-related research. Search volume

data from the past five years show a marked increase in terms related to small commercial insurance (see chart). Between 2008 and 2013, monthly search volume for key phrases related to commercial insurance skyrocketed, showing that consumers are turning to Internet searches to find information about business coverage in increasing numbers. Of particular note are the following terms:

- ▶ **Business Insurance Cost:** 120% increase in search terms since 2008.
- ▶ **IT Insurance:** 270% increase since 2008.
- ▶ **Small Business Insurance:** 190% increase since 2008.
- ▶ **Liability Insurance Cost:** 500% increase since 2008.

Commercial Insurance: Online Search Trends, 2008 - 2013



Source: Google Analytics

The Internet has long been referred to as the "Information Superhighway," and the marked increase in "information-seeking" search terms reinforces the notion that business owners are flocking to search engines in growing numbers to educate themselves about the insurance products necessary to protect their businesses.

Equally significant is a [2013 survey conducted by Deloitte \[PDF\]](#), which shows that the majority of small-business owners are, for the first time, comfortable buying commercial insurance over the Internet. While individuals in the U.S. have long found the Internet suitable for buying personal insurance products (think Geico and Esurance), businesses have been more reluctant to hop aboard. The Deloitte study shows that the majority of small-business

owners (52%) are now willing to purchase commercial insurance over the Internet. Other research has shown that [trust is a key element](#) [PDF] in customer willingness to make purchases online, which suggests that business owners have, in 2013, decided that online insurance advisors are trustworthy enough to provide financial protection for their firms.

» Part III: Growing Legal Risks for Micro-Business Owners

It will not come as a surprise to insurance industry insiders that the rapid growth of small and micro businesses in the U.S. has corresponded with growth in liability exposure and costs. As of 2008, small businesses in the U.S. accounted for only 22 percent of total revenue, but bore a whopping 81 percent of tort liability costs. Even more troubling?

Data suggest that much of this expense could be avoided with proper liability insurance: of the \$105.4 billion small businesses paid in tort liability costs in 2008, \$35.6 billion came directly from their revenue rather than from insurance benefits. Business owners seem aware of the risk lawsuits present them: in a 2007 poll, 62 percent of small business leaders who were worried about litigation reported making decisions specifically to avoid lawsuits and 61 percent noted that those decisions increased the cost of their goods or services. And this decision making is not paranoid behavior: in recent years, fully [a third of small businesses report having been sued or threatened with a lawsuit](#).

The fallout from lawsuits against small and micro businesses is significant: nearly three-quarters of small companies that have faced a lawsuit have had to increase their prices, and 71 percent have reported decreasing hiring because of funds diverted to legal costs.

Mind the Gap

Thanks to a lack of clarity about what counts as a small business, as many as 16 million Americans may not realize they're legally considered business entities and are therefore exposed to business-related liabilities. This knowledge gap costs small businesses, independent contractors, and freelance \$35.6 billion in uninsured liability costs per year.

2010 Census Report 27.9 Million

According to the 2010 Census Report, there were 27.9 million registered small businesses in the United States.



52% Home-based business owners.



73.2% Sole Proprietors.



78.5% Non-Employers.

Freelancers Union 42 Million Strong

According to the Freelancers Union, there are 42 million independent workers in the U.S. – 1 in 3 working adults.



These numbers suggest two needs among the nation's small and micro businesses: first, a need for greater financial protection in the form of liability insurance; and second, a need for educational materials targeted at informing micro-business owners about the many and real liability risks they face. A simple comparison of the numbers of U.S. small businesses as estimated by SBA.gov and the Freelancers Union reveals one potential source of misunderstanding and thus unnecessary risk exposure for the nation's micro businesses: while the SBA estimates the number of small businesses at 27.9 million, the Freelancers Union puts the number at 42 million. The difference comes from varying definitions of what constitutes a "small business:" while the SBA counts only those small businesses actually registered with state or local governments, the Freelancers Union includes all part-time and full-time freelance and contract workers, many of whom operate without formally incorporating or forming LLCs.



Significantly, the IRS's definition of a small business (which includes contract workers and the self-employed) aligns with the Freelancers Union's, putting the most legally accurate estimate of small and micro businesses and self-employed workers in the U.S. closer to the 42 million mark. But considering that the SBA fails to count many freelancers in its statistics – and thus presumably does not target this group in its outreach – many professionals who

are legally considered small businesses may be uninsured or underinsured simply because they are not aware that their freelance work exposes them to liability risks.

Insurance professionals who serve the small and micro business sector, then, must focus on not only securing markets able and willing to write lines for freelance business owners but also on educating these businesses about their very real (and potentially very costly) liability exposures



» Conclusion

Growth in the micro business sector is the way of the future. Insurance providers that serve small commercial clients can both facilitate and benefit from that growth by investing in online infrastructure to both educate prospective clients and make products available for purchase where these clients want to buy. By doing so, insurance providers can help reduce the out-of-pocket liability costs currently weighing down small and micro businesses, thus helping them grow more steadily and sustainably.