

Gaining steam: Mid-market interest in self-funding and stop loss



For years, large employers have self-funded their health benefits. Today, as the health care market continues its transformation, many mid-sized and even smaller companies are considering joining their ranks.

Self-funding fundamentals

Self-funding (also known as self-insurance) is an alternative means of financing a group medical benefits program. It differs from a traditional fully insured program. A fully insured employer pays a premium to an insurance company, which assumes the financial risk for payment of eligible medical expenses incurred by the members. In a self-insured program, however, the employer assumes that risk.

A third-party administrator (TPA) operates the plan, so it looks the same as a fully insured plan to employees. The TPA handles all the traditional administrative services associated with a medical benefits plan, including maintaining eligibility, paying claims, billing, ID cards, communications and reporting.

Self-insured plans, which cover 60 percent of workers who have health coverage, are increasingly popular because they give employers greater control over plan design and may provide savings over a fully insured plan. There are other advantages too (see sidebar).

Advantages of self-funding

- Opportunity for improved cash flow
- Potential for lower administrative costs compared to fully insured plan
- Greater plan design flexibility
- Exemption from some state-mandated benefits laws
- Governed by federal law (ERISA)
- Ability to manage risks through stop loss coverage
- Choice of service providers

Where stop loss fits in

Because the liability associated with claims can be unpredictable and potentially very large, employers purchase stop loss insurance to protect them from claims above a certain dollar amount. This is called the “stop loss deductible” and claims over the deductible are reimbursed by the carrier to the employer.

Stop loss insurance can protect against unexpectedly high individual claims (called specific stop loss) or against aggregate claims of the entire group (called aggregate stop loss). In short, stop loss insurance allows employers to limit their financial exposure. The coverage can be designed in accordance with an employer’s financial strength and cash flow outlook — with premiums typically decreasing as the deductible increases.

Today, almost three in five covered workers in self-funded plans are in plans with stop loss protection.

High-dollar claims

Buying stop loss insurance can be critically important, particularly for mid-sized and smaller companies, because of the potential financial exposure. In fact, a catastrophic claim for a serious illness could significantly impact an employer’s financial viability.

The cost of cancer care, for example, has soared in recent years. The monthly price of the average brand-name cancer drug has doubled to \$10,000 in the past decade. Some drugs may cost as much as \$30,000 per month.

Transplants can also be hugely expensive. Consider the average costs for transplants and first-year expenses: liver (\$575,000), bone marrow — allogeneic (\$800,000) and heart (\$1 million).

Some stop loss carriers also provide carve-out options, such as separate, fully insured coverage for expenses related to transplants. Or, they may assist a health plan’s administrator with services to help them recover or contain costs, such as medical management for complex cases like premature births or cancer.

Increased interest in self-funding

Optum™ has recently seen a significant uptick among fully insured mid-sized and small companies interested in exploring a shift to self-funding with stop loss coverage. There are several drivers behind this trend:

- The Affordable Care Act includes several new taxes and fees on insurers and employers that provide health coverage to their employees, many of which took effect this year. Self-insured plans and stop loss coverage, however, are subject to fewer of these measures.
- Concerned about the rising cost of health care, employers view self-funding as a potential option for controlling those costs.
- With increased state and federal regulation over fully insured plans, employers see self-funding as a way to assume more control over the benefits they offer their employees.

Big financial hits



Monthly price of the average brand-name cancer drug
\$10,000



Average first-year liver transplant expenses
\$575,000

Improved reporting

Obtaining insights into valuable claims data is another reason that employers are eyeing self-funding. In fully insured programs, businesses generally don't have access to claims data since it resides with the carrier in its capacity as plan fiduciary.

Self-insured firms, on the other hand, as the plan sponsor, are able to view this information, which can be used to implement chronic disease management programs targeted at their specific employee population.

For example, if claims data reveals that a large number of employees suffer from diabetes, effective programs — blood sugar control, lipid management, foot and eye exams, monitoring for kidney disease — can be devised to help limit future claims.

Tie-in to wellness

Armed with claims data, employers can also provide population health management programs tailored to employees who are susceptible to chronic conditions. For example, claims data may reveal that a segment of an employer's population is pre-diabetic — having blood sugar levels that are higher than normal but not high enough to be classified as diabetes.

That employer may want to implement a wellness program for those employees to help them lose weight and pursue healthy lifestyles so that they don't become diabetic. Such programs can lead to a healthier workforce, fewer medically related absences and greater productivity, and can also help employers contain future diabetic care costs.

Controlling diabetes among the workforce is becoming a growing concern. According to a recent report by the Centers for Disease Control and Prevention, more than 29 million U.S. residents have diabetes, up from an estimated 26 million in 2010. Another 86 million adults — more than one in three — have pre-diabetes. Diabetes and its related complications accounted for \$245 billion in total medical costs and lost work and wages in 2012 — up from \$174 billion in 2007.

Long-term strategy

Self-funding should be thought of as a long-term strategy to manage workforce health and control costs. It is not a one-time, quick-fix solution to all the challenges employers face in providing health benefits.

Employers should recognize that having more control over their health benefits plan means being more involved in plan decisions, such as working with a broker to find a suitable stop loss carrier with a long track record. Selecting an experienced TPA who is able to manage claim costs through superior care management and utilizes a high quality provider network is also critical.

The cost of diabetes

29 million

Diabetic American adults.

84 million

Pre-diabetic American adults.

Accounting for

245 billion

In total medical costs.

Avoid these pitfalls

Exclusions/definitions

Due diligence is key when shopping for stop loss coverage. In a worst case scenario, an employer that submits a high-dollar claim to its stop loss carrier could have it rejected because that particular type of claim, while covered under the employer's plan, is excluded from coverage under the carrier's policy.

Brokers must carefully compare stop loss policies and understand definitions, exclusions, time frames for submitting claims and other key provisions. An employer does not want to be shocked with a rejected claim resulting from inconsistent definitions or exclusions between its own self-funded plan and the stop loss policy.

Increases upon renewal

Suppose late in the first year of coverage, an employee is identified as a liver transplant candidate. The treatment will not take place until the following year. At renewal time — the end of year one — some stop loss carriers would impose a higher deductible on that employee because the risk is known (stop loss insurance covers unknown risks). So, for example, in year two, while all other employees may continue to have the same \$40,000 deductible as in year one, the transplant candidate's deductible jumps to \$200,000. That means the employer is liable for the first \$200,000 of transplant expenses.

Brokers can advise their clients to consider adding a rate cap option, which gives the employer peace of mind by guaranteeing a maximum renewal premium increase while preventing the stop loss carrier from imposing a higher deductible on any covered individual identified as a high risk.

Coverage gaps

It's critically important to structure the stop loss contract to avoid any gaps in coverage. This could arise in the situation where a fully insured company converts to self-funding with a stop loss policy designed to cover claims incurred and paid during the 12 months of the policy period. After the first year, however, the company decides to return to a fully insured program. If, during that next year, a catastrophic claim is identified that occurred while the plan was self-funded, the firm may be liable for the entire claim since neither the stop loss nor the fully insured policy covers it.

To mitigate a potential gap in coverage, consider adding a Terminal Liability Option provision to a stop loss policy. This option provides an additional run-out period — typically three months — to cover claims that were incurred during the self-funded policy year, but paid after the termination date.

Health care reform is driving employers to think about ways to gain greater control over their health benefits. Self-funding, with stop loss insurance, provides that opportunity along with the potential to better manage costs. As uncertainty grows concerning the direction of the health care market, increasing numbers of mid-sized employers will be taking a hard look at this alternative.

For more information, visit <http://www.optum.com/landing/br/broker-hub>.

1 Employer Health Benefits 2013 Annual Survey, Kaiser Family Foundation and Health Research & Educational Trust

2 Employer Health Benefits 2013 Annual Survey, Kaiser Family Foundation and Health Research & Educational Trust

3 <http://capsules.kaiserhealthnews.org/index.php/2014/05/chemo-costs-in-u-s-driven-higher-by-shift-to-hospital-outpatient-facilities/>

4 National Foundation for Transplants, <http://www.transplants.org/faq#n313>

5 Optum Stop Loss products are underwritten by Unimerica Insurance Company, and in California, Unimerica Life Insurance Company

6 http://www.cdc.gov/features/diabetesfactsheet/index.html?s_cid=cdc_homepage_feature_001

