

Rein in Rising Health Care Costs by Self-Funding



A Viable Funding Option for Large and Small Companies

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As a broker, you know only too well that rising health care costs weigh heavily on your customers' minds and that they are interested in ways to manage those costs. Like you, they've read the myriad troubling statistics published over the last year. For instance, the 2005 Towers Perrin Health Care Cost Survey found employers will see an eight-percent increase in health care costs in 2006, or about \$600 per employee. In that same study, employers learned that health care costs over the last five years have risen a staggering 78%, far outpacing other inflation gauges.

Virtually all of your clients are asking workers each year to assume a greater share of benefit costs. Urge clients to focus on two important aspects: a carefully calibrated benefits plan design and an appropriate funding option.

Offering plan options—such as consumer-driven designs—that engage members in health care decisions and purchases can potentially save employers money. The idea is that with “more skin in the game,” employees will be more judicious in ordering tests and making trips to the doctor, thus driving down claims costs.

For the funding options, many employers have explored only briefly, or dismissed out of hand completely, self-funding. This article offers a closer look at self-funding as

an attractive option for your employer customers, large and small.

The Basics

With self-funding, employers establish their own health benefits programs for employees and assume the financial risk of the benefits, unlike fully insured plans in which the employer pays a full premium regularly, whether there are many claims, few claims or none at all. That premium includes claims costs, administrative fees/profit and reserves. With a self-insured plan, the employer pays for actual claims, not expected claims and pays an administrative fee if it chooses to have a third party process claims for it. This means that if actual claims are more favorable than expected, the employer pockets the savings. However, if actual claims are higher than expected, the employer could pay more than it would with a fully insured policy.

This is where stop-loss insurance comes in. It protects the self-insured employer from those high-claim costs by capping liability. The benefit of stop-loss insurance is that if claims exceed the predetermined level, the insurer pays that cost, not the employer. Brokers should encourage clients to purchase stop-loss coverage. The most common

is individual coverage, or specific stop-loss, which guards against any one person whose claims exceed a certain dollar threshold. Claims exceeding this individual cap are paid by the insurer. Aggregate stop-loss insurance mitigates overall claims exposure, is typically set as a percentage of total expected annual claims, and limits the client's total risk.

The Two Cs – Client Characteristics

Self-funding is used by tens of thousands of employers across the country and is one way for companies to rein in costs while continuing to provide attractive benefits plans to workers. But self-funding is not for every employer. As a broker, there are certain characteristics your clients should have to determine if they are a good fit for self-funding.

Relatively health population and/or a history of good claims experience—When employees have good health, claims are usually lower. Clients can obtain this information from their current carrier, or submit underwriting information that would allow a carrier specializing in self-funding to determine whether the company would be a good candidate. If the results are positive, the employer should know that, under its fully insured plan, it likely does not benefit from its strong record of member health. The fully insured model pools costs of an entire segment to set an average price. Therefore, the majority of groups within the segment tend to subsidize the higher-cost companies. With self-funding, employers can back out of the pool and benefit directly from their own claims experience.

Trim state-mandated benefits and reduce state insurance premium taxes—A self-funded plan needs to comply with the Employee Retirement Income Security Act (ERISA), a federal law, and is exempt from state-mandated benefit insurance requirements. Because self-funded plans need not comply state by state with mandated benefits, a multi-state employer can offer a single, consistent plan to all employees nationwide. The total premium paid for a fully insured plan is subject to state insurance premium taxes, which can total two to three percent of the entire premium. Under a self-funded plan, only the stop-loss insurance premium is subject to the premium tax. Many employers may not realize this is a benefit, so as a broker you should position this as an advantage.

Save money and improve cash flow—Employers save money when the plan runs well because they pay only for actual claims. Self-funding also allows an employer to retain and invest that portion of a fully insured premium that is held by the insurer for claim reserves (money set aside for payment of claims incurred prior to plan termination but submitted for payment after plan termination). With self-funded plans, the insurance company does not collect reserves up front, and the employer holds the reserve money to pay for claims incurred before termination, but submitted after termination. Reserves are the primary area where the employer sees cash-flow benefits in self-funding.

Understand concepts of risk—Employers need to make sure they understand the risks involved in self-funded plans as well as the ways to mitigate those risks. Brokers

should impress upon clients that risk can be minimized by such strategies as specific stop-loss, aggregate stop-loss and programs that focus on managing the health care of those members with chronic or potentially catastrophic conditions.

You may have employer customers that aren't familiar with self-funding. Additionally, you may find it difficult to explain self-funding in terms your customers understand. Now there is a new aid available for brokers to use with clients: **Great-West Healthcare's Insider's Guide to Self-Funding**. It is a 15-minute interactive CD that takes users through the basics of self-funding. The tool is divided into three sections: a breakdown on how self-funding works, the advantages of this type of approach, and common misperceptions. At the conclusion, employers may complete a short survey to help determine if self-funded health plans are a good fit for their companies. Brokers may request a copy of the CD by sending an e-mail with their name, company name, address, e-mail and phone number to insidersguide@gwl.com.

A Viable Option for Companies of All Sizes

Large employers have been taking advantage of the self-funding mechanism for years, and the trend has been catching on with midsize and small employers as well. According to a 2004 survey conducted by the Kaiser Family Foundation and the Health Research and Educational Trust, half of the workers in the United States from companies with 200 to 1,000 employees have self-funded health plans. The study also showed that 10% of employees in companies with fewer than 200 workers are covered under a self-funded plan.

"Recently, we have suggested that companies with 50-150 employees seriously investigate self-funded systems," said Scott Schultz, CEBS, client relations manager for Burkwald & Associates, a Pewaukee, WI, employee benefits broker. "They are attracted to the possibility of saving money as well as improving cash flow. Why pay up front to subsidize other companies if your own claims experience is better than the (average) company?"

The key with small companies is to apply the same underwriting principles, medical management and stop-loss coverage to a group of 25 as one would to a group of 20,000. In the past, smaller employers were concerned that they would not have access to the same kinds of products and funding options that larger employers would, but health plans today are trying to level the playing field.

Huntington House, a 130-employee manufacturer and distributor of handcrafted furniture, began to self-fund its

health benefits a couple of years ago. The company saved an estimated eight percent to nine percent in its first year of experience. During the next year, 2004, Huntington House's costs did not rise at all, compared to an industry average increase of about 12 to 14%. Their plan design let them control costs and offer quality coverage, which in turn helped retain employees.

Employee Education

According to the Disease Management Association of America, approximately 10% of employees account for 80% of all claims, so urge clients to explore programs that focus on managing the health care of those members with chronic or potentially catastrophic illnesses. The benefits can lead to healthier employees and a healthier bottom line.

"Of the clients we work with, almost everyone is satisfied with the self-funded route, especially the reporting capability," noted Schultz. "We encourage our clients to go over these reports and look at the problematic areas. For instance, from the drug portion of the statement, one client noticed a high use of a drug to control diabetes, so they took the time to educate their employees about available disease-management programs that could help manage diabetes. After those meetings, the

disease-management program, which is intrinsic to the health insurance, experienced an increase in participation. This gives both the employer and employee a vested interest in reducing costs."

In addition, advise employers to implement an employee-education program that teaches health care costs and the role of members in helping control rising costs. Also, recommend they combine self-funding with a health plan that engages employees in the cost and use of discretionary medical services. Resources for employees include interactive online wellness systems, drug-cost and hospital-comparison tools, provider cost and quality information, and health risk assessments.

As the old adage goes, insanity is doing the same thing over and over again and expecting different results. So, next time an employer is looking for alternatives to managing costs, suggest self-funding. It's not for every employer, but when it is combined with medical management to reduce claims costs, employee education to teach employees how best to use their health plan, and reporting to see how its plan is running, then self-funding may be an attractive option to employers of all sizes. ■

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