

WHAT IS IT?

Self-insurance is a benefit funding method in which an employer assumes some or all of the financial risk for providing health care benefits to employees. Instead of paying conventional premiums to an insurance company, the employer assumes the risk for eligible employees' healthcare claims and contracts with a third party administrator(s) (TPA) to provide claim adjudication, provider network access, prescription drug management and utilization review.

While self-insurance offers the possibility of lower costs as compared to fully-insured premiums, employers who self-insure greatly increase their exposure to liability and risk. The employer can limit this additional risk exposure by purchasing stop-loss insurance. Stop loss insurance is a product designed to protect employers and self-insured health plans from catastrophic losses. There are two types of stop loss coverage:

- **Specific Stop Loss** - employer protection against high claim cost exposure for one specific person
- **Aggregate Stop Loss** - employer protection against excessive claim expenditures for the entire covered population

WHY OFFER IT?

- Greater control and flexibility of plan design
- Improved cash flow
- Potential cost savings
- Tailor plan to fit specific needs
- Improved access to utilization data

WHAT SIZE EMPLOYERS OFFER IT?

Employee populations must be large enough to provide financial predictability. More predictable benefit plans, such as Dental and Vision, can be reliably self-insured down to 100 employees. Self-insuring medical benefits involves larger claim dollars and volume and is generally not recommended for populations of less than 500 employees.

HOW MUCH DOES IT COST?

Long term overall costs should be similar to purchasing insurance from an insurance carrier. Potential savings are realized when claims experience is more favorable than expected, and through elimination of the insurer's premium taxes, profits and margin. However, costs can be significantly higher than insurance alternatives if claim experience is less favorable than expected.

OTHER CONSIDERATIONS

CONTROL AND FLEXIBILITY OF PLAN DESIGN

PROS

- ERISA exemption from state mandates allows the employer greater control over benefit plan designs, resulting in more consistent benefit offerings across multiple states.

- Plan designs can be customized to meet the needs of an employer's specific population.
- The employer is not required to implement many of the carrier's mandatory plan design changes; however self-insured plans are still subject to provisions related to [healthcare reform](#).

CONS

- More sophisticated benefit management is required to design and maintain effective benefit plans.
- Self-insuring exposes the employer to greater risk of lawsuits otherwise defended by the insurer of a fully-insured plan. This risk can be minimized by paying the carrier or TPA an additional fee to assume claim fiduciary responsibilities.

CASH FLOW

PROS

- The employer does not pre-pay premiums, which results in improved cash flow.
- The employer holds the reserves for claims incurred but not recorded which can result in a cash flow advantage in the first plan year. In the first 12 months of a self-insured plan the employer generally pays only about 9-10 months' worth of medical plan costs.
- The employer pays fixed costs for administrative fees and stop loss premium. Claims are paid on a variable basis as they are submitted, approved and paid, creating a cash flow advantage in a low claims month.

CONS

- Financial management of reserves is required to ensure proper accrual of future liabilities.
- Monthly funding requirement could vary significantly as claims are paid.
- The employer generally can only take a tax deduction for reserve accumulation when a claim payment is made (i.e., the liability is not tax deductible).
- If the employer decides to move from self-insured to fully-insured, they will be required to utilize any reserves built-up to pay run-out claims from the self-funded plan. In addition, they would pay the full premium costs for the new fully-insured contract. This tends to equate to paying 14-15 months of medical plan costs in only 12 months, counteracting the cash flow advantage the employer received in the first year of self-funding.

COST SAVINGS

PROS

- The employer holds the reserve liability and can invest the funds at a higher rate of return than they would receive from the fully-insured carrier.
- Margin and profit paid to the insurance carrier is eliminated.
- Fully-insured premium tax is eliminated.
- The cost may be lower than a fully-insured plan for a given plan year. The employer benefits in years where actual claim costs are less than expected. This could be a result of lower than expected trend, a reduction in large claims and/or lower overall plan utilization than prior year patterns may have suggested.

CONS

- The cost may be higher than a fully-insured plan for a given plan year. Poor claims experience due to unfavorable demographics or higher than expected utilization can cause a significant financial loss for the employer. Specific Stop loss insurance protects against catastrophic claims to some extent, but claims can span two contract periods or otherwise slip through stop loss arrangements.
- Some states require self-insured plans to pay specific taxes based on claims, which can be complicated.
- Poor claims experience and/or high COBRA participation could cause the employer to be “locked out” of the fully- insured market place and be at the pricing discretion of the stop-loss provider.

TAILOR PLAN TO FIT SPECIFIC NEEDS**PROS**

- Employers can contract with niche best-of-breed providers for specialized functions such as provider networks, utilization management, pharmacy benefits management and population health management.
- Vendors can be unbundled, facilitating changing one function without having to change all others (e.g., changing administrators or stop loss insurers without changing the underlying health care network).

CONS

- The claims adjudicators are not at risk for the claims and could be less critical in the review process.
- Requires greater management oversight of increased number of vendors.

ACCESS TO DATA**PROS**

- Improved access to utilization experience provides valuable data for tailoring benefits to employee population and/or cost control.

CONS

- [HIPAA](#) compliance burden increases significantly.

INFORMATIONAL LINKS

- [Self Insurance Institute of America](#) (SIIA)
- [Stop Loss 101](#) (Meritain Health)



This Fact Sheet is designed to provide a general overview of the benefit program, service, or regulatory act it describes. The information included in this document is not a substitute for legal or professional opinion relative to a plan sponsor's particular fact pattern. Your ArlenGroup consultant can answer more specific questions relative to its application for your organization.