AmWINS Group Benefits

CLIENT ADVISORY

Barriers to Self-Funding Eliminated with Cooperative Strategy

Self-funding employee health care has long been the standard for large employers; 80 percent of those with more than 1,000 employees self-insured in 2010. But for small and even medium-sized employers, taking on full responsibility for health care costs can be a frightening prospect. Despite spiraling benefit costs, many of them stick with the solution they are most familiar with – buying full insurance at a price that pays not only for their employees' health care services but also for the carrier's overhead and profits.

A 2011 Rand report[1] does not envision that changing, despite the challenges employers face with increasing health insurance premiums and the uncertainty caused by the impending implementation of the Patient Protection and Affordable Care Act. The report identified three significant barriers that prevent smaller employers from making the leap to self-funding; however, the benefits of self-funding can work for smaller employers when they adopt a three-part strategy to address the barriers. That strategy includes: 1) joining with others to lower the initial costs of switching to self-funding; 2) relying on a cooperative to spread the risk of catastrophic expenses; and 3) finding the right partner to shoulder the administrative burden and manage health care costs.

The Case for Self-Insurance

The advantages to employers of self-funding health care benefits were recognized in a U.S. Department of Health Services report issued earlier in 2011[2]. These include:

- Greater flexibility and control over plan design
- Lower administrative services costs
- Access to data on claims to help shape coverage decisions
- Ease of change without disrupting patient care
- Improved cash flow by keeping funds in-house until needed for claims payment
- Avoidance of state insurance premium taxes and regulatory requirements.

Rand-Identified Barriers

The advantages to self-funding come with a cost. In its study of factors that may influence employer decisions about self-funding, Rand identified three barriers:

1) The cost of switching to self-funding for employers with low cash flow can be almost as expensive as full insurance coverage.

2) The relative risk of a single company experiencing a large claim is too high for most companies on limited budgets to tolerate.

3) The complexity of moving to a self-funding system is too much for a small company with few resources to manage the administrative and compliance duties associated with health care benefits.

Nonetheless, Rand noted that 20 percent of employers with 50 to 199 employees and 8 percent of employers with fewer than 50 employees were self-funded in 2010. Clearly, many small and medium-sized employers have found a way to make self-funding work to their advantage.

The Three-Part Strategy

Each of the three barriers can be addressed by understanding the underlying issues and then implementing a carefully constructed self-funding strategy.

Initial Cost of Self-Funding

The typical cost for self-insuring may actually be higher during the first year than purchasing full coverage. That is because small employers do not have unlimited cash flow to tap into for pay-as-you-go health care expenses. As a result, they may have to buy not only stop-loss insurance to protect against catastrophic events, but also coverage that in essence finances health care for their employees while the employer builds up reserves.

This can be expensive. Because insurers build in a margin for costs to be higher than anticipated plus an amount to cover their overhead and profit, the cost can be greater when added to stop-loss insurance than if the employer buys a full insurance package.

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AmWINS Group, Inc.

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By participating in a cooperative set up with other small employers, the dollars that would normally go to an insurer for the day-to-day health care costs instead go to a combined trust fund. At the end of the year, the funds that remain belong to the cooperative members rather than being retained by an insurance carrier.

The trust fund can be used to decrease the amount that must be deposited to pay for the next year's costs. While the first-year cost may be high, the cooperative strategy creates a "virtuous cycle" with future years becoming increasingly less costly than full insurance coverage.

Risk of Catastrophic Event
If an employer has thousands of employees and a few develop diseases that are costly to treat and manage, the cost on a per capita basis is spread widely. But small employers recognize that in any given year the impact of a single individual's health care can be devastating for their bottom line.

Buying stop-loss insurance addresses catastrophic illness, but it can be expensive. By purchasing stop-loss insurance through a cooperative, the risk is spread over a much larger pool of employees and the cost on a per capita basis is much lower.

Complexity of Changeover
When employers buy full health insurance coverage from a carrier, they are purchasing far more than just payment of medical bills. The bundled service includes a variety of administrative functions, from claims processing, negotiating with health care providers and managing costs to handling employee enrollment and fielding employee problems. When employers turn to self-funding, they must replace this infrastructure with something.

A third-party administrator with proven expertise, like AmWINS, can take the headaches out of self-funded plans without adding back in the high costs of traditional full insurance. In addition to administrative functions, AmWINS specializes in case management, wellness initiative support and bill auditing to ensure that employers get the most out of their self-funding arrangement.

Self-Funding: An Option Worth Examining
As employers continue to search for ways to provide health care benefits to their employees at lower costs, there is no need to be afraid of the self-funding option. While barriers exist that make the decision to abandon fully insured coverage more difficult for small employers, a cooperative purchasing strategy addresses those barriers and holds out the promise of greater control and lower costs. It's an option that can make a difference for small employers in today's challenging business environment.

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[1] Rand: "Employer Self-Insurance Decisions and the Implications of the Patient Protection and Affordable Care Act as Modified by the Health Care and Education Reconciliation Act of 2010" at http://www.rand.org/content/dam/rand/pubs/technical_reports/2011/RAND_TR971.pdf

[2] U.S. Department of Health and Human Services: "Report to Congress on a Study of the Large Group Market" at http://aspe.hhs.gov/health/reports/2011/LGHPstudy/index.pdf