



# THE VALUE OF **SELF-FUNDING**

# THE CHALLENGE OF AFFORDABLE HEALTH COVERAGE

Rising costs and increased instability in the healthcare marketplace has prompted more employers of all types and sizes to consider self-funding (also known as self-insurance) as a solution to provide quality health benefits to their workers and dependents.

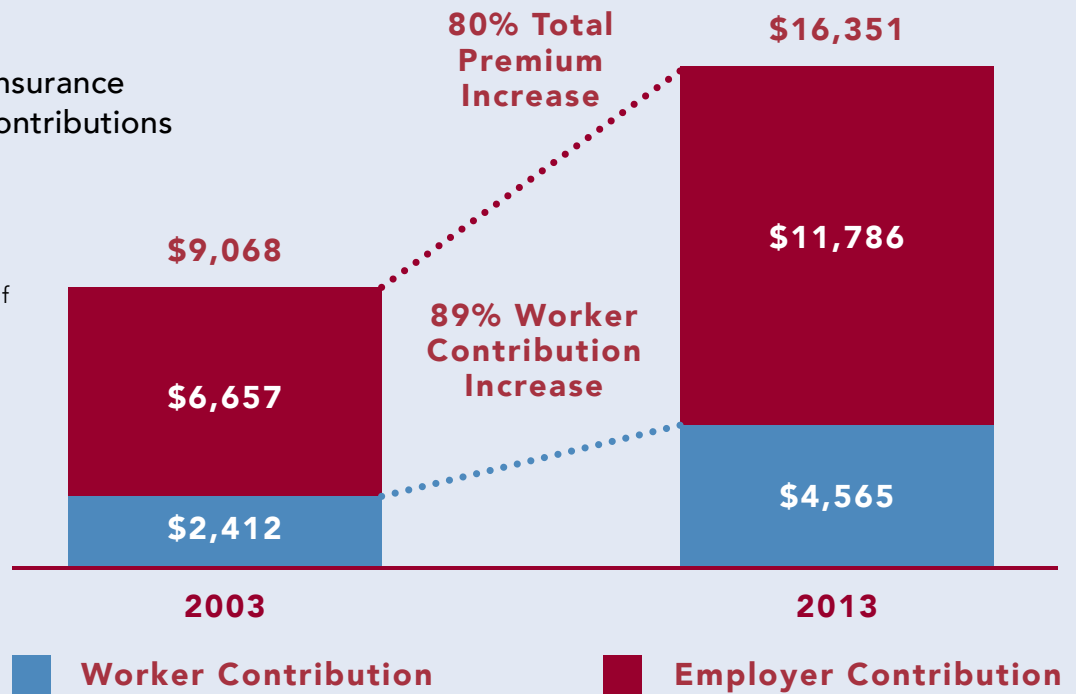
This solution can offer many advantages, but like any significant business decision it should be given due consideration, including appropriate consultations with knowledgeable business advisors, as self-insurance may or may not be the best fit for an organization. This publication is intended to assist employers and brokers to familiarize themselves with what is needed to effectively evaluate the self-insurance option for one's business.

As shown in the 2013 Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 2003-2013, (Exhibit A), the premium for workers and employers has increased more than 80% in the past ten years. These figures include self-funded, fully insured and other coverage options combined. These increases are not sustainable for either the worker or the employer and therefore must change. The solution for many employers today is self-funding.

## EXHIBIT A

Average annual health insurance premiums and worker contributions for family coverage

Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 2003-2013.



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# THE FACTS OF SELF-FUNDING

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**SELF-FUNDING ALLOWS FOR GREATER COST CONTAINMENT OPPORTUNITIES. THIS GIVES ORGANIZATIONS CUSTOMIZED PLAN COVERAGE FEATURING THE BEST OPTIONS TO MEET THE SPECIFIC NEEDS OF THEIR WORKFORCE.**

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Self-funding is an important contributor to the financial and physical health of America's wellness future. Self-funding is more than processing claims and receiving premiums, it provides quality coverage and proactive healthcare management for employers of all sizes and industries.

- Organizations of all types and sizes consider self-insurance as a solution for quality health benefits to their workers and dependents due to the rising cost of healthcare and increased instability.
- Self-insured group health plans now provide coverage to the majority of U.S. employees and dependents (KFF Survey, 2013).<sup>\*</sup> This has created increased interest and involvement from brokers and consultants in the self-funding option.
- Self-insured health plans are sponsored by thousands of companies, as well as many labor unions and public sector entities. Some of these companies include:
  - Whole Foods<sup>®</sup>
  - Microsoft<sup>®</sup>
  - Starbucks<sup>®</sup>
  - Wells Fargo<sup>®</sup>
  - The Home Depot<sup>®</sup>
  - Southwest Airlines<sup>®</sup>
- Companies today can benefit by being self-funded through:
  - Greater cost containment opportunities
  - Ability to customize benefit offerings
  - Increase in employer cash flow
  - Ownership of claims data
- Self-funding allows for greater cost containment opportunities. This gives organizations customized plan coverage featuring the best options to meet the needs of their specific workforce.
- Due to aggregated claims data availability, companies identify and promote healthier employee cultures. This is traditionally through innovative wellness and disease management experts, who actively engage at the group and member level.
- Through stop-loss insurance, normally obtained by the plan sponsors, self-funded companies have the security of a financial backstop should they incur large healthcare claims.

<sup>\*</sup>[kff.org/private-insurance/report/2013-employer-health-benefits/](http://kff.org/private-insurance/report/2013-employer-health-benefits/)

# SELF-FUNDING-THE SOLUTION

## **Risk Management - Charges, Commissions and Retention**

One advantage of self-funding is the flexibility in controlling risk. Business objectives of self-insuring employers revolve around the best use of their money devoted to benefits: controlling claims, managing and benefiting from investments. Compared to fully insured plans, a self-insured health plan can allocate more of each dollar toward the payment of medical claims, eliminating insurance commissions, risk charges and other costs of a commercial insurer, such as marketing and overhead. Costs also decrease thanks to the sponsor's ability to exert greater control over administrative expenses and utilization.

## **Improved Cash Flow**

Self-funding allows claims to be paid as they are incurred while fully insured premiums constitute a form of prepayment. With self-insurance, a plan can delay payment of recurring health plan costs until the services have been rendered. Commercial insurers, by contrast, set health insurance premiums at levels that anticipate projected increases in healthcare costs—usually well in excess of the actual rise in costs.



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**OVER 100,000,000 AMERICANS  
RECEIVE THEIR HEALTH  
INSURANCE TODAY THROUGH  
SELF-FUNDED BENEFITS.**

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## **Innovative Plan Document Design and Control**

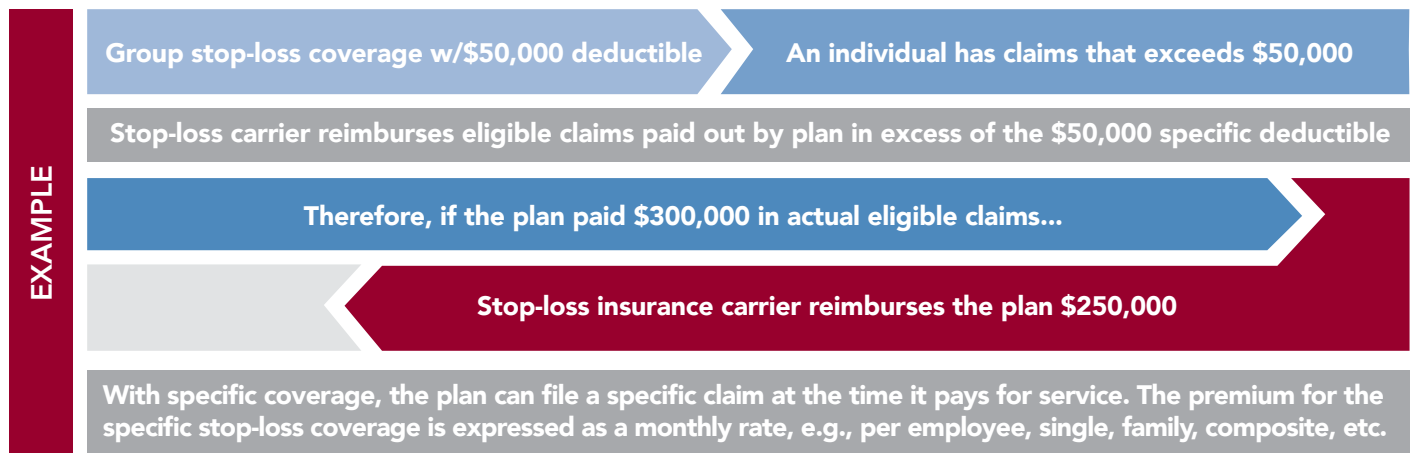
Decisions about plan design belong to the employer and not an insurance company. The employer can design his or her plan without the restrictions, delays and costs involved in obtaining the approval of an insurer or regulatory agency; thus, employers make the overall compensation package more attractive, and plan design options can be tailored to the working population and company preferences. Language can be modified to fit individual plan needs, and accurately reflect the true intentions of the plan.

## **Value-Based Benefits and Wellness Programs**

As medical costs have continued to skyrocket, sponsors have been taking steps to reduce medical costs by emphasizing prevention and care for chronic diagnoses. Employers have the flexibility to design and integrate such elements as health risk assessments, disease prevention and wellness programs tailored to the specific employee demographics and needs.

## Stop-Loss Coverage

Specific stop-loss coverage is purchased to limit the plan's financial exposure on any one individual and/or aggregated claims experience. The exposure (i.e., specific deductible) should be a function of the company's size, risk tolerance, financial resources, location, benefits plan, PPO network and claims experience.



## Stop-Loss Contract Types

When an employee is covered by a fully insured plan and incurs a claim during the effective period of the contract, the employee simply submits the claim to the insurance carrier, and either the employee or the provider is paid the benefits due. This is known as an "incurred" contract.

A stop-loss contract operates differently because it is actually insuring the employer and not the individual employee. When a plan is self-insured, the stop-loss contract insures the employer against catastrophic losses under the plan. The medical plan established by the employer accepts the responsibility for paying providers' claims for individuals but limits its risk with stop-loss coverage. Individual employees are not personally insured by the stop-loss carrier.

The stop-loss contract used most often in the first year of a self-insured plan is known as "incurred and paid" or a "12/12" contract. In order for an employer's plan to be reimbursed for a claim covered by a 12/12 contract, the claim must be incurred during the 12 months of the policy period and paid during that same 12-month period.

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**SPECIFIC STOP-LOSS COVERAGE  
IS PURCHASED TO LIMIT THE  
PLAN'S FINANCIAL EXPOSURE  
ON ANY ONE INDIVIDUAL.**

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# THE STEP-BY-STEP PROCESS FOR SELF-FUNDING

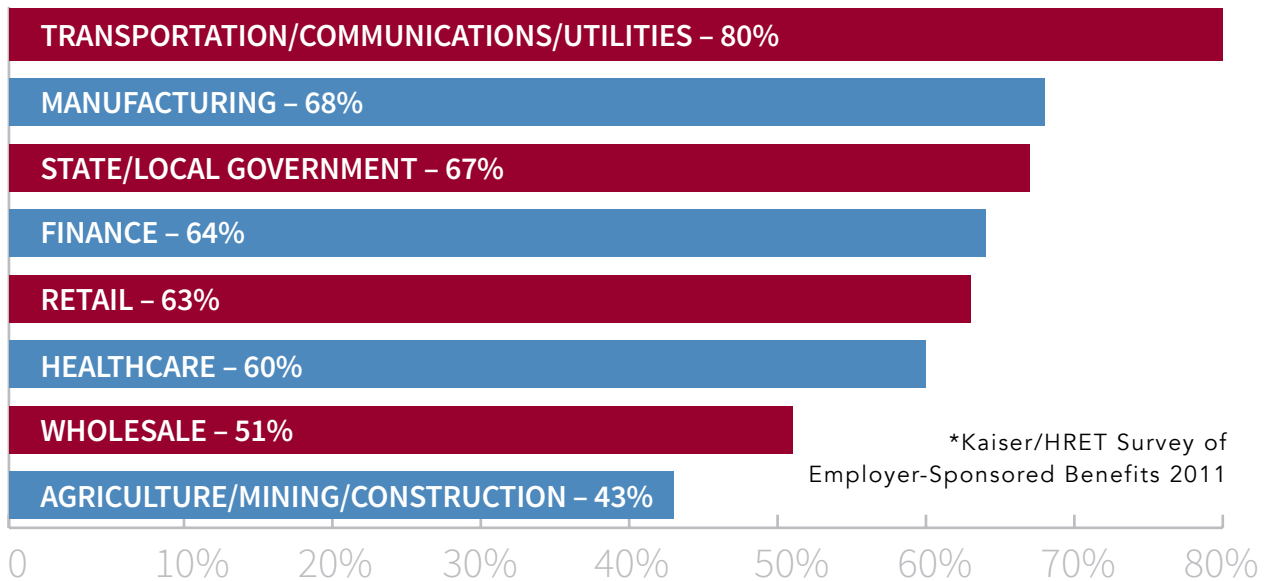
In many cases, self-funding is a viable means for companies with strong balance sheets, stable work forces and executive leadership teams that want to take a proactive approach to managing their insurance costs.

The first step to self-funding is traditionally an internal feasibility study that is guided by an insurance broker or third party administrator (TPA). This study includes a risk and cash flow analysis to determine if the level of risk is acceptable and if the company has monetary resources to set aside for potential future loss and management resources. A listing of TPAs and other self-insurance providers can be accessed on-line at [www.siefonline.org](http://www.siefonline.org). Click on the **"Getting Started"** link (at the bottom) included as part of the **"Employer Section."**

**ADEQUATE RESERVES MUST BE AVAILABLE TO HANDLE THE EXPECTED CLAIMS PAYMENT LOAD, AS WELL AS MONTHLY PAYMENT REQUIREMENTS, WHICH ARE UNPREDICTABLE AND CAN VARY WIDELY MONTH TO MONTH.**



Self-Funding By Industry Type\*





LEGAL ADVICE

ACCOUNTING ADVICE

CONSULTANTS

ADMINISTRATIVE COSTS

FINANCIAL RESOURCES

EMPLOYEE DEMOGRAPHICS

**Additionally, companies considering self-funding should examine:**

- **Workplace Demographics**  
Age, gender and other demographic factors, such as smoking and obesity, should be considered.
- **Funding Considerations/Cash Flow**  
Adequate reserves must be available to handle the expected claims payment load, as well as monthly payment requirements, which are unpredictable and can vary widely month to month. Additionally, financial resources should be available to take advantage of discounts that can be negotiated with providers for timely payment.
- **Employee Value/Cost Control**  
The plan must be of real and perceived value to the employee while simultaneously controlling employer costs.
- **Administrative Time Requirements**  
The employer will have to allocate time for management to oversee administration of the plan, even if a TPA or ASO is engaged.
- **Administrative Costs**  
There will be up-front costs for consultants, legal and accounting advice and plan development. There will be ongoing administrative costs whether the employer self-administers or contracts with a third party administrator (TPA) or administrative services offered by an insurance company (ASO) to administer the plan.
- **Medical Management Services Costs**  
These are costs for utilization review, case management, disease management, wellness programs etc., which theoretically will reduce claims expenditures over time.
- **Stop-Loss Insurance Options**  
The cost of singular and aggregate coverage to limit the employer's liability will depend in part on the number of employees, employee demographics and claims history.
- **Plan Benefit Coverage Options**  
Costs will vary depending on what the plan covers and how much of the responsibility will be placed on the employee through co-payments and deductibles. A plan must be created in order to project costs and cash flow requirements.



The Self-Insurance Educational Foundation, Inc. (SIEF) is a 501(c)(3) non-profit organization affiliated with the Self-Insurance Institute of America, Inc. (SIIA). The foundation's mission is to raise the awareness and understanding of self-insurance among the business community, policy-makers, consumers, the media and other interested parties.



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