



# UNDERSTANDING SELF-FUNDED INSURANCE PLANS

**Health Insurance  
Cooperative Agency**

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## Is a self-funded insurance plan right for your organization?

The costs of fully insured health care plans represent a significant expense for employers. Many companies don't realize, however, that there is a way out of skyrocketing insurance premiums: Self-funded plans, in which the employer pays directly for employee health care expenses, are a competitive alternative to fully insured plans. Today, roughly 50% of workers in the United States are covered by a self-funded plan.

Ultimately, the benefits of self-funded health plans are numerous. Traditionally these kinds of self-funded plans have worked well for large companies with over 1,000 employees. In fact, a significant proportion of Fortune 500 companies utilize self-funded insurance plans. With the rising costs of health care, self-funded plans are increasingly becoming viable options for smaller companies as well. These kinds of plans can provide organizations with better cash flow, tax benefits, a greater degree of flexibility over the plan's design, and reduced administration costs.



## ObamaCare and the rising costs of health care

ObamaCare, officially known as the Patient Protection and Affordable Care Act (PPACA), is a United States federal statute signed into law by President Obama in 2010. It is often described as the most significant restructuring of the American health care system since the 1965 passage of Medicare and Medicaid. The ObamaCare Employer Mandate states that all businesses with over 50 full-time equivalent employees must provide health insurance for their full-time employees. If companies fail to provide health care, they will face an annual fee of \$2,000 per employee. It is important to note that this coverage must also be offered to employees at an affordable price. If the employer insurance fails to cover 60% of health care expenses for a typical population or costs employees more than 9.5% of their family income, the employer will also face a fee.

The bottom line is that with these new ObamaCare mandates, employers with over 50 full-time equivalent employees must provide their employees with affordable health care. However, providing employees with health care can be a very expensive prospect, seriously cutting into profit margins. Numerous studies have suggested that ObamaCare will actually increase employer costs per worker. This is in part because ObamaCare requires that insurance policies cover a broad range of services for each patient, including substance abuse treatment, psychiatric care, and maternity benefits, even though many patients may not need or use such services. Several think tanks, including the Manhattan Institute, have actually done research indicating that health insurance premiums will rise by over 90% as a result of ObamaCare.

# The difference between self-funded and fully insured health plans

Self-funded plans can be an excellent way for employers to escape the ever-rising insurance premiums and take control of their health care spending. First and foremost, it is important to note that self-funded and fully insured health plans differ in one fundamental way: in a fully funded plan, an employer contracts an insurance company to meet employees' health care needs, while in a self-funded plan, an employer meets the health care needs of an employee itself. In a fully funded insurance plan, an employer works with a health insurance company to provide its employees with health insurance. The cost of the premium the employer pays is based on its projected claims; employers pay insurance companies up front to cover projected claims, the insurer's overhead, and administrative costs. These premiums have been becoming increasingly more expensive as a result of the skyrocketing costs of the healthcare in the US. Luckily, self-funded plans are a way out.

Essentially, self-funded insurance plans are funded by individual companies, as the name suggests. In other words, employers set aside money themselves to pay employees' medical expenses themselves, varying the cost of the plan and the specific level of coverage according to the needs of the employees. The company never has to pay for services it isn't using, and there is an incredible amount of flexibility in plan design and administration. Companies are free to set premium rates based on claims history, taking into account fixed costs per employee and account claims, also known as variable expenses. The company then uses the premiums to pay claims out-of-pocket, as opposed to compensating an insurance provider.

# The costs of self-funded plans

Self-funded plan costs can be broken into two distinct categories: fixed costs for an employee and variable costs. Fixed costs are essentially claim costs for an employee. This amount cannot be perfectly predicted every month. It depends on how frequently employees seek medical services as well as the nature of the medical services they seek. This amount can, however, be predicted through a careful analysis of claims history. Variable costs are less predictable. All in all, this amount will depend on the number of employees covered by a company as well as the nature of coverage offered.

## Stop-loss coverage

In a fully funded insurance plan, premiums are based on projected claim amounts. However, should claim amounts exceed the projections, the premiums remain constant, protecting the company from losses. But in a self-funded plan, an employer simply doesn't have this kind of protection. In some cases, an employer may end up spending less than the projected claims amount. This is always ideal, as the employer is free to invest the money and decrease premium amounts appropriately. But in the case that an employer ends up spending more than the projected claim, this can be problematic.

Therefore, when it comes to self-funded plans it is essential to have protection against unpredictable or above average claims. This kind of protection is known as stop-loss protection. As the name suggests, it prevents the employer from losing any money on health insurance, or spending more money than it has collected as premiums from their employees. Stop-loss coverage is essentially a way of mitigating risk, insulating the company from a catastrophic event.



## Third-party administrators

While self-funded insurance plans do often help a company slash health costs, it is important to note that companies also incur a significant amount of administrative responsibilities. While some companies do perform these administrative services themselves, many rely on third-party administrators. This third party is responsible for all administrative services, also providing access to preferred provider networks, prescription drug card programs, and utilization review. Oftentimes, insurance companies provide these services to companies through what is known as administrative services only or “ASO” contracts.

# The advantages of self-funded health plans

An appropriately planned and organized self-funded health care plan with stop-loss protection can be tremendously advantageous for many employers. Health insurance costs are a very substantial expense for most organizations. Through self-funded insurance plans, employers are often able to save significant amounts of money. Instead of paying monthly fees, companies have to pay only for the medical expenses that their employees use.

Unlike fully insured health plans, with self-funded plans, companies don't have to pay upfront for claims; the money collected by an organization is paid out only when it is needed for a claim. Until then, the money can remain in an account, collecting interest. Furthermore, if a company spends less than is projected on health care claims, it is free to invest that money back into the organization. Aside from fiscal savings, self-funded plans also offer an unprecedented level of claims transparency. Employers receive a monthly report detailing both medical claims and pharmacy costs. They are able to see exactly what amount of money is being spent on what.

Last but not least, self-funded plans also allow for an incredible level of flexibility. This flexibility is incredibly advantageous should a company's health care needs evolve or change. Furthermore, employers are free to design plans to best meet the needs of their employees. They may also craft wellness incentives. Several studies have shown that wellness incentives function much better within the context of self-funded plans, helping employers to cut costs. This may eventually lead to lower premiums for employees, saving both employers and employees money in the long run.

# Conclusion: Is self-funding right for your company?

If you are wondering whether or not self-funding is right for your company, there are several factors to consider. First and foremost, most employers can benefit from self-funding, whether large or small. However, proper planning is absolutely crucial. Companies need to make an accurate assessment of the costs that they will incur by moving to such a plan and set rates accordingly. Companies also need a clear, effective plan to handle administrative responsibilities, whether they plan to hire a third-party administrator or handle administration themselves. All in all, however, self-funded insurance plans can help employers to provide high-quality, affordable healthcare to employees.

The HIC Agency has been providing consultative insurance services to employers since 1993. Whether you are interested in implementing your own self-funded plan or seeking a new fully funded plan for your organization, we can help you navigate the ever-changing world of health care law. The HIC Agency specializes in group benefits plans for service industries such as restaurants, hotels, nursing homes, and other health care facilities. Contact us today at 913-649-5500 to learn how we can help you offer the benefits your employees need while keeping health insurance costs stable.

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