

Medical Stop Loss Carriers Evaluation & Selection

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Introduction

The basic premise of any alternative risk transfer (ART) program is to decrease an employer's ultimate cost of retaining risk. This is done by increasing the efficiency in which retained risk is structured and financed by the employer in order to promote long-term stability.

Whether using pure self-insurance or a captive, and depending on the complexity of the program, the employer will need to engage a series of independent service providers to structure, manage, and secure the program.

A basic principle for achieving structural efficiency is attaining the control to unbundle the rigid structure associated with traditional insurance programs. This is achieved by having the ability to select the best-in-class independent service providers for each segment of the program. For a self-funded healthcare program, this list would include third party administrators (TPAs), PPO networks, and large case management (LCM) providers. Medical stop loss captives would add a captive manager, asset manager, auditor and attorney to the list. Of course, both structures will rely on a highly rated medical stop loss (re)insurance carrier to properly secure the program, which is the focus of this discussion.

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D. Market Expansion and Carrier Contraction

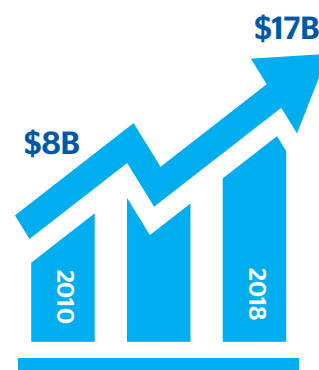
The current healthcare environment is highly unpredictable and the medical stop loss (MSL) market extremely competitive; the stakes for writing profitable business have gotten much higher since the implementation of the Affordable Care Act (ACA) in 2010. The cost of claims, especially large claims, has increased dramatically with the ACA's mandate to abolish lifetime benefit limits within health plans. Many claims that used to be \$100,000 or \$200,000 are now regularly eclipsing \$500,000 or more, and the frequency of \$1 M+ claims has risen to unsettling levels for both plan sponsors and underwriters.

Attaining stability for a self-funded program is predicated on the plan sponsor's ability to efficiently retain and manage predictable layers of risk while transferring the more unpredictable layers to a (re)insurer via medical stop loss coverage. These larger claims would obviously penetrate the specific stop loss deductibles of most self-funded programs and captive layers. The increased frequency of large claims has forced significant change in the medical stop loss market.

In 2010, the MSL market was estimated to be an \$8b - \$10b industry with 70% of that market being controlled by the top 25 writers of the coverage. The MSL industry is now estimated to be \$14b - \$17b, with 70% of the market being consolidated among the top 10 largest writers. The growth in MSL market volume parallels the growth in self-funding; however, the consolidation in volume among a smaller group of carriers is especially intriguing but not surprising from a macroeconomic perspective.

Given the increased volatility in healthcare market, there has been a definitive migration away from smaller carriers and Managing General Underwriters (MGUs) by larger brokers. Even though there have been some new MGU market entrants over the past few years, more have either been absorbed by or sold to carriers, effectively becoming blocks of assumed direct-written premium for the carrier. A few prominent carriers have also recently entered the medical stop loss market, either from scratch or through the purchase of MGUs, but they have yet to stabilize significant positioning in this segment. There has also been an increased trend of brokers forming preferred stop loss carrier "panels" which has further consolidated the amount of MSL business among larger carriers. Again, the larger writers will continue to accumulate market share, and the smaller writers and especially MGUs will face increasing headwinds in remaining competitive.

Unrelenting regulatory and healthcare economic uncertainty, along with the increasing frequency of highly unpredictable large (catastrophic) claims, will continue to drive employers toward self-funding. Consequently, the selection of which medical stop loss carrier to partner with has become one of the most important decisions a self-insurer or MSL captive will make.



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II. Considerations for Carrier Selection

As an excess coverage, it can be easy for many program sponsors or consultants to mistakenly commoditize medical stop loss by focusing solely on which carrier has the lowest rates as the primary selection criteria.

The following items should be evaluated when choosing a stop loss carrier:

• Institutional Strength

In this increasingly volatile market environment, medical stop loss, even as a short-tail coverage, needs to be written primarily by carriers having underwriting expertise, market experience, and the financial strength and stop loss portfolio large enough to absorb the growing frequency of losses, especially the increased instances of large, multi-million dollar claims. It's natural to consider the long-term operating stability of smaller carriers, MGUs or other program managers that will invariably incur a series of multi-million dollar claims.

• Direct Writing Carrier

The market continuously pushes for aggressive pricing and expanded contract terms, while rising costs in a volatile healthcare environment push in the opposite direction. Smaller carriers and MGUs with heavily leveraged reinsurance structures will not have the underwriting discretion and claims settlement authority of larger carriers that retains most, if not all MSL risk on a net basis. Performance standards for underwriting, claims and policy issuance are important considerations.

• Direct Access to SMEs

Most stop loss carriers use an account or business development representative as the primary liaison between the client/broker and the underwriting, claims, medical, actuarial, and other operative teams. Inaccurate or delayed transmission of information can lead to inaccurate pricing or administrative processing issues. Working with a carrier that provides direct access to departmental SMEs will streamline processes and also serve as a valuable knowledge resource for clients/brokers when additional support is needed.

• Quality of Contract and Scope of Product Options

None of the aforementioned issues will matter if the carrier cannot deliver a competitive product. For traditional self-funded plans, the carrier must be able to deliver a market-responsive excess contract which includes: the ability to mirror the employer's plan document, a full range of specific deductibles and contract claims basis (from 12/12 through PAID), aggregating specific deductibles, experience refund options, no new laser options, renewal rate caps, specific and aggregate advance accommodations and the like. Does the carrier impose provisions that differ from the industry standard for such things as actively-at-work or disclosure?

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• **Support Services**

As with “product scope,” the array of support services can be a long and significant list. In this era of increasing large claim frequency, having a professionally credentialed medical team to evaluate ongoing conditions during the underwriting (accurate pricing), treatment (outcome excellence and cost options) and claims (accuracy) process is an essential risk management support service. Actuarial and underwriting resources to assist in appropriate network identification and selection are helpful. MSL carriers providing these services on a value-added basis can significantly reduce loss costs for a self-funded plan through improved program structure and performance.

III). Special Considerations for Medical Stop Loss Captives

Although growth in the self-funded employee benefit healthcare market has stabilized over the past year or so, the use of captives for MSL continues to be one of the most active growth segments within the alternative risk industry. Large single-parent captives continue to add MSL, and group captive growth among mid-sized employers continues to be quite robust. With both structures, the basic carrier considerations are generally the same as they would be for a single (traditional) self-insurer selecting an MSL carrier, but with a few additional considerations:

A). Single-Parent Stop Loss Captives

As a recognized insurance company, many single-parent captives are able to issue a stop loss policy directly to its owner (aka: parent). If the captive is able to issue the policy, and purchase medical stop loss in the form of reinsurance, as opposed to an excess insurance policy, some of the related policy expenses, such as fronting fees, collateralization, and taxes, can be reduced or even eliminated. Having the ability to assume risk from the captive as a reinsurer is an important consideration when selecting a carrier for a single-parent captive.

B). Group Stop Loss Captives

There are two general types of group MSL captives. The first is a tightly-controlled, “closed” group of employers that form their own group captive. The second is an “open-market” (typically heterogeneous industry composition) captive that is open to outside membership. The tightly controlled “closed” groups typically have fewer member-employers (with a higher average member size) and are more likely to access a direct-writing (re)insurer to develop a customized ceded risk-sharing arrangement for specifically designated layers of risk. They usually require less in terms of program service components and can have a more efficient expense structure. With fewer participants, collaboration and active engagement among members is higher and each member has more influence in the direction of the captive.



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The more prevalent “open-market” groups tend to be prepackaged and operated by third-party Program Administrators (PAs) or MGUs. It is important for a self-insured employer to understand that a PA or MGU has less control than a direct-writing carrier. These entities will only have the level of authority that has been delegated from the issuing carrier. Decisions above the PA’s designated authority level, in terms of underwriting, administrative and claims decisions, fall to the carrier and/or the carrier’s reinsurer. This reduces the level of control to the captive and its participating employers in terms of overall program direction and management. This program structure also adds additional expenses that ultimately reduce the programs profitability on a net basis.

Expense transparency is a major consideration when evaluating PA managed group programs. Any program that does not provide a detailed and unbundled disclosure of the gross-to-net expense structure with complete transparency should be avoided. Typical fees include fronting fees, reinsurance, taxes, brokerage commissions, and PA management fees. As more fixed expenses are charged to the program, the less capital remains to pay claims, retain as surplus, and eventually return to participants as profitability dividends. A discerning approach needs to be taken when evaluating programs, especially when expenses exceed 35%, which is pretty common.

Other evaluation considerations for group captives should include:

- Length of tenure with the current (and any prior) carriers as evidence of the stability of the program
- Underwriting guidelines for new members: admittance standards, minimum acceptable loss history, etc.
- Program history in terms of dividend returns or collateral calls
- Member requirements for participation in risk reduction programs, wellness initiatives etc.
- Exit parameters: Are there handcuff provisions such as surplus forfeitures? What is the timeline for return of collateral?
- What is the voting voice of members? Do they have input on the direction, structure, surplus allocation, membership standards, service providers, etc.?

For both single-parent and group captives, the engaged carrier should be able to provide essential insurance company program management functions on behalf of the captive. This includes services such as retained layer pricing, policy development and issuance, reserve management, claims adjudication, advice to pay, explanation of reimbursement, and monthly bordereaux preparation. Since the captive itself is an insurance company, it will need to provide these functions internally or outsource them. Having them delivered by the captive’s reinsurer, and coupled with the previously mentioned value-added support services, provides seamless management and performance advantages as opposed to outsourcing to an otherwise unaffiliated service vendor or MGU.



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IV). Unbundling the BUCAs

Many self-insurers conventionally purchase a “bundled” program from a single insurer such as Blue Cross, United Healthcare, Cigna, or Aetna; which are known collectively as the BUCA providers. The bundled programs from these carriers can provide all needs - administration, network, LCM, and stop loss coverage - in one simple package to the self-insurer. This bundled approach simplified self-funding and remains a practical option for many employers. A bundled approach does have simplicity advantages; however, significant disadvantages also exist and are leading to an increasing trend, especially among larger employers of unbundling the stop loss coverage from the rest of the package:

- There are inherent conflicts-in-interest associated with having the same organization that provides medical stop loss, also adjudicating and paying claims. Opaque pricing practices and administrative and claims transparency challenges associated with some bundled programs can frustrate plan sponsors.
- Most BUCA carriers also do not like to share data. A major advantage of self-insured plans is attaining the ability to capture, analyze and use plan data to manage the program to higher levels of effectiveness. Many BUCA carriers, particularly with bundled arrangements, are reluctant to appropriately provide plan data needed to effectively evaluate and manage the plan by any other entity - including the plan sponsor in some cases. By unbundling the medical stop loss to an independent carrier, an additional layer of protection is provided to enhance administrative accuracy and ensure appropriate transparency.
- Most BUCA carriers are unable to offer many competitive contract enhancements, e.g., experience refund options, aggregating specific deductible, rate cap, terminal liability rider, or even mid-policy reserve reporting. Most are also unable to provide stop loss (assume risk or cede risk) to captives.
- Overall program control is also sacrificed with a bundled program. Effectiveness and control of a self-funded program is optimized by unbundling the various components. It's much easier to replace underperforming program components rather than an entire structure.



Unbundling the medical stop loss to an independent carrier, empowers the plan sponsor with control to select the most appropriate stop loss carrier to accommodate specific needs. An unbundled approach also provides separation from any latent interest conflicts to enhance administrative accuracy and ensure appropriate transparency.

Conclusion

As mentioned earlier, among the basic advantages of an alternative risk program is attaining greater control over individual program components. This is especially true of self-funded programs which are uniquely empowered with increased plan design agility. The ability to preempt state insurance and benefit mandates provides a self-insuring employer with an enormous amount of flexibility to tailor a benefit plan design that best fits the needs of its specific employee population. Self-insured employers can also adopt more advanced cost containment initiatives that are not typically pursued or otherwise available within more conventionally regulated insurance arrangements.



As the desire for increased predictability of healthcare expenses continues to drive expansion of self-insured structures, each program component should be evaluated on its ability to contribute to the qualitative depth of the overall program. In terms of medical stop loss, the consideration needs to be based on much more than the lowest rates. The importance of selecting the most appropriate

carrier by evaluating contract quality, underwriting agility, claims settlement autonomy, service depth, and financial strength is magnified in this current environment of escalating catastrophic medical claims.

About the Author

Phillip C. Giles, CEBS is Vice President of Sales and Marketing for QBE North America's Accident and Health division, overseeing business development and strategic marketing initiatives, including medical stop loss captive production. He has 30 years of experience in Accident & Health and Property & Casualty alternative risk. He was named to Captive Review's 2016 *Power 50* list of most influential individuals in the Global Captive Insurance Industry and was recognized as the *Captive Professional of the Year* at the 2017 U.S. Captive Awards.

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