

Strengthening the Safety Net: Strategies for Improving the Stop-Loss Coverage that Provides Protection from Large Claims Costs

Public sector employers that self-fund their health plans avoid some of the charges associated with commercial insurance (e.g., risk charges and profit margin). In addition, they retain plan design flexibility (that would otherwise be affected by state insurance coverage mandates) and their role as claims fiduciary, giving themselves the final right of appeal for disputed claims. Perhaps the most attractive advantage of self-funding health benefits is that it enables the employer to improve cash flow when claims experience is better than insurance company premiums. Recognizing the advantages, many public sector employers self-fund their health coverage. (For relevant data from a Segal Company survey, see Table 1.)

The downside of self-funding is the assumption of two types of risk:

➤ **Ordinary Risk** This risk consists of managing fluctuating claim levels.

➤ **Catastrophic Risk** As the name suggests, this risk entails absorbing large catastrophic claims. These are sometimes referred to as “shock” claims due to their association with a one-time or unexpected event. In recent years, catastrophic risk is being amplified by advances in technology and the high and rising incident rates of obesity, diabetes and other chronic conditions.

As the data in Table 2 shows, a very small percentage of claimants generate a disproportionately large percentage of high-claim dollars. Although this implies that there is very little risk associated with catastrophic claims, all self-funded plan sponsors know that this risk is very real.

Self-funded plan sponsors can mitigate these risks by purchasing stop-loss or “medical excess” insurance, which provides protection against large claims as well as fluctuations in claims. This *Public Sector Letter* provides an overview of available stop-loss coverage options, discusses strategies for avoiding potential coverage gaps and other common pitfalls, and illustrates what plan sponsors can expect from today’s dynamic stop-loss market.

Table 1: Percentage of Self-Funded State Employee Health Benefits Plans* by Plan Type

Indemnity	71%
POS	69%
PPO	64%
HMO	32%

* Includes plans with or without stop-loss insurance.

Source: 2003 *Segal State Health Benefits Survey: Medical Benefits for Employees and Retirees*: http://www.segalco.com/publications/surveysandstudies/2003statesurvey_medicalbenefits.pdf

Table 2: Breakdown of Large Claims by Percent of Claimants and Percent of Total Claim Dollars

Paid Claim Amounts	Percent of Claimants	Percent of Total Claim Dollars
\$70,000+	0.19%	17%
\$100,000+	0.10%	12%
\$150,000+	0.05%	8%
\$250,000+	0.02%	4%

Source: Ingenix, 2004. Cited with permission.

IN THIS ISSUE:

- Stop-Loss Insurance Coverage Options
- Policy Considerations
- Coverage Gaps and Other Potential Pitfalls
- Market Conditions
- New Business Underwriting
- Renewals
- Strategies for Managing the Cost of Stop-Loss Coverage – and Other Sources of Savings
- Conclusion

The Segal Company is pleased to announce that George N. Korean has joined Segal’s Los Angeles office as a vice president and health consultant to public sector employers and plans. Most recently, he was managing director and consulting actuary at Paragon Consultants. Mr. Korean is an Associate of the Society of Actuaries, a Fellow of the Conference of Consulting Actuaries and a graduate of Brown University.

STOP-LOSS INSURANCE COVERAGE OPTIONS

For health plans, stop-loss insurance generally has two component pieces that can exist independently but usually come in tandem:

➤ **Specific Stop-Loss Insurance**
Specific stop-loss insurance provides protection for large, catastrophic claims associated with one individual for a set period (e.g., a 12-month policy period). For example, a \$100,000 specific deductible would require the plan sponsor to pay up to

\$100,000 in claims for each individual. The stop-loss insurance carrier would reimburse the plan sponsor for covered claim dollars exceeding \$100,000 for any individual.

➤ **Aggregate Stop-Loss Insurance**

Aggregate stop-loss insurance provides protection for the overall claim levels of the plan. The stop-loss carrier establishes an aggregate attachment point. This is a projection of the plan’s expected claim levels, with additional margin, called the “claims corridor.” This margin commonly is set at 125 percent of expected claims, but it can be lower (e.g., 120 percent or 110 percent). Lower margins require higher premiums due to the increased carrier risk and are more difficult to obtain from the insurance companies. When there is individual as well as aggregate coverage, reimbursements from an individual stop-loss policy are not eligible for reimbursement under the aggregate stop-loss policy.

At 125 percent of expected claims, the chances are small that a large employer (i.e., one with at least 1,000 employees) would ever receive a reimbursement under an aggregate stop-loss policy. Larger employers’ overall claim levels do not fluctuate as much as those of smaller plan sponsors. Consequently, some large plan sponsors have chosen not to purchase aggregate stop-loss protection. However, before deciding to forego aggregate stop-loss protection, Segal recommends that plan sponsors have at least 12 months of current claim levels available in reserve assets. Without this protection, there is no limit to the plan’s liability except as defined by the limits within the plan policies and provisions.

POLICY CONSIDERATIONS

There are a number of policy considerations to take into account when initially purchasing or renewing

stop-loss insurance. This section focuses on the most important ones.

Prescription Drugs

Although specific stop-loss insurance is designed to provide protection against large medical claims, policies may include or exclude prescription drug benefits. Because prescription drug benefits often are administered by a separate pharmacy benefit manager (PBM), the stop-loss carrier and/or the medical claims administrator will need to have the means necessary to “marry” the claims data from two different sources (i.e., a PBM and a medical claims payer). To avoid that, some stop-loss carriers may exclude prescription drug coverage when a PBM is the administrator.

Specialty Drugs

Increasingly, specialty drugs¹ have become a contributing factor in overall medical cost inflation. Traditionally, these drugs have been covered under medical plans. Increasingly, however, specialty drug providers are administering these programs. With the high cost and increasing use of specialty biotechnology drugs, a growing number of plan sponsors are beginning to include specialty drugs in their stop-loss policies.

Match Between Policy Provisions and the Underlying Plan

Often, the provisions contained in a stop-loss policy do not match the plan document from which the medical plan is administered. For example, procedures deemed “experimental”² may be excluded from stop-loss policies. Because stop-loss policies provide protection to the plan sponsor, and

not benefits to a participant in a group plan, in most states stop-loss carriers are not subject to certain requirements of the Health Insurance Portability and Accountability Act (HIPAA). For example, many stop-loss policies contain “actively-at-work” language requiring employees to be “actively at work” before protection would begin. In most cases, we have found that stop loss carriers are willing to waive these requirements, sometimes in exchange for full disclosure of potential large claims information.

These provisions can be negotiated with the stop-loss carrier. It is beneficial for plan sponsors to have the stop-loss policy provisions match the provisions of the underlying plan as closely as possible in order to obtain meaningful protection.

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Care Management

Many stop-loss carriers will closely assess and negotiate provider claims submitted once the stop-loss threshold is hit. Effective care management programs can and do drive the value. In addition, care management is in the best interest of the insurer because it is now financially responsible for the balance of the claim.

COVERAGE GAPS AND OTHER POTENTIAL PITFALLS

There can be coverage gaps associated with stop-loss insurance. Because these liabilities often involve hundreds of thousands of dollars, it is essential that plan sponsors address any potential gaps in coverage. This section addresses how to close those gaps — and avoid other potential pitfalls.

¹ Specialty drugs are genetically engineered compounds designed to treat and target certain diseases, such as hemophilia, Crohn’s disease and cancer. These are expensive drugs developed by biotechnology companies and the per-patient costs can exceed \$250,000. Often injectable and/or refrigerated, they also require special handling.

² Experimental care involves any device, treatment, supply or procedure that is unproven or for which the efficacy has not been established. Examples include non-FDA approved drugs/compounds used to treat certain procedures and *in utero* fetal surgery.

Period Covered

Stop-loss policies cover claims for a specific period. Typically, a stop-loss policy will cover a 12-month period during which a claim is processed or “paid.” Lags from the time when a claim is first incurred to when it is paid can be problematic if a claim paid during the policy’s time frame began (at least partially) prior to the policy’s effective date. With the advent of electronic claims submissions and automated processing and in response to various regulations requiring that providers be reimbursed within 30 days of a claim submission, lag times tend to be 30 days or less. Under policies that cover a 12-month period, some claim dollars could “fall through the cracks” and not be covered. In addition, there could be issues in settling large, complex claims from the time the claim is incurred to the time the claim is paid.

Speed of Reimbursement

If the claims administrator is also the provider of stop-loss insurance, as is the case with most large health care insurers, reimbursements on settled claims are often immediate and generated electronically. Otherwise, stop-loss carriers typically reimburse claims within 10 to 30 business days from the time they receive complete information. However, this timing usually only applies to “clean” or problem-free claims. If the proper documentation is not supplied, if notification procedures have not been followed,³ or if policy amendments

have not been updated and communicated to the stop-loss carrier, reimbursement can take longer. Although most often handled by the claims administrator, ultimately it is the plan sponsor’s responsibility to resolve these issues, especially if they lead to disputes.

For aggregate stop-loss claims, reimbursement times are longer — usually 90 or more days. Most stop-loss carriers require a claims and eligibility audit to occur before making such reimbursements.

MARKET CONDITIONS

The competitiveness of the medical stop-loss market tends to be cyclical. When stop-loss carriers tighten their underwriting controls (e.g., refusing to negotiate a proposed renewal rate, not renewing policies and increasing “lasering” activity⁴) to improve their profits, insurance companies tend to direct more capacity to the market and competition usually increases. Eventually, margins are reduced and underwriting controls are relaxed. Plan sponsors should require their consultant or broker to keep an eye on changes in market conditions to take advantage of favorable markets.

NEW BUSINESS UNDERWRITING

In a new business, or RFP situation, stop-loss carriers require certain information from the plan sponsor and/or third party administrator. The summary of benefits, claims, information on vendors and disclosure statements, including diagnosis and prognosis

information on all claimants above a certain level (i.e., 50 percent of the stop-loss deductible) will typically be required for quotes.

If the RFP process occurs 60 to 90 days ahead of the effective date of the policy, the stop-loss carrier often will require an updated disclosure statement 30 days or sooner from the effective date.

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“Lasering”

“Lasering” is a common method stop-loss insurance carriers use to reduce their risk by transferring some of it back to the plan sponsor. Under the practice, after identifying individuals with known conditions, the carrier will apply a higher deductible than that stated in the policy for these potential high-cost claimants. Lasering is commonly used when underwriting new specific stop-loss coverage. It may be presented as an option, in return for a lower premium, at renewal.

Carrier’s “Approval” of the Claims Administrator

Most carriers will write stop-loss insurance only through pre-approved claims administrators. If a claims administrator is not pre-approved, the carrier may decline to quote, or provide a conditional proposal requiring that the claims administrator be approved. The approval process usually requires that claims administrators complete a questionnaire and accommodate the carrier on a site visit or audit of its procedures.

RENEWALS

Stop-loss policies renew annually. Stop-loss trend increases likely will be higher than overall medical inflation due to

³ Stop-loss carriers typically require advance notice when a claim exceeds 50 percent of the individual stop-loss deductible, if an individual is a candidate for an organ transplant or large case management.

⁴ “Lasering” is defined in the next column.

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leveraging.⁵ The renewal increases will also depend on several factors, including the amount of the individual stop-loss deductible, whether the benefit plans include managed care networks and/or transplant networks, as well as the overall demographics of the group. Generally, only the very largest groups (*i.e.*, 20,000 employees or more) will have actuarially “credible experience” (*i.e.*, stop-loss claims taken into consideration when premium rates are developed), but stop-loss carriers have been known to increase the rates substantially for groups with high losses. Consequently, it is not unusual for plan sponsors to see renewal increases ranging from 15 percent to 30 percent. Similarly high rates of increase are expected to continue throughout 2007.

Stop-loss carriers will often continue existing lasers, as well as add new ones at renewal. Some carriers require new disclosure statements for participants identified during the renewal disclosure process that have the potential for future large claims.

STRATEGIES FOR MANAGING THE COST OF STOP-LOSS COVERAGE – AND OTHER SOURCES OF SAVINGS

There are various strategies for managing the cost of stop-loss coverage. In addition, stop-loss coverage presents opportunities for savings that can help offset the cost of coverage.

Request Rates Related to Experience

Plans that have better-than-average experience including lower overall trend, should ask carriers to consider those factors in their premiums for renewals and bids. If the market cycle is “soft,” carriers may be amenable to reducing their quotes.

⁵ Leveraging is explained in the following example: If overall medical inflation is 10 percent per year, a \$125,000 claim in the first year of the policy would become \$137,500 in the second year. If the stop-loss deductible is set at \$100,000, the insurance carrier’s stop-loss liability will increase by 50 percent (from \$25,000 to \$37,500).

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Negotiate Discounts for Networks

Traditionally, stop-loss carriers have discounted their premiums if there is a strong provider network in place. Stop-loss carriers will focus on how networks reimburse the “outlier” claims within their contracts. For example, a network may have a certain fixed fee in place for a certain procedure up to \$50,000, and a less favorable “discount off charges” for claims in excess of \$50,000. (Charges in excess of \$50,000 are considered the “outlier” portion of the claim.)

In general, the higher this outlier, the more favorable the contract. Many carriers may provide premium discounts, if they believe solid reimbursement arrangements for large claims exist.

Many stop-loss carriers have also contracted with “centers-of-excellence” networks that provide discount and utilization monitoring for organ transplants. Discounts of up to 5 percent can be offered for these types of arrangements, but sometimes there will be a small fee to implement the program. Most carriers will provide similar discounts if the plan sponsor already has a transplant network in place.

It should be noted that stop-loss carriers predominantly believe that consumer-driven health plans will have no, or very little, impact on the large catastrophic claims. They have also been slow to provide discounts associated with disease management and wellness programs.

CONCLUSION

Stop-loss coverage can provide valuable protection against catastrophic claims

for plan sponsors that self-insure, but still need some budgeting protection. Maximizing that protection entails knowing what policy provisions to request and what potential pitfalls to avoid. Minimizing the cost of coverage requires similar savvy.

Segal can help by facilitating the RFP process, negotiating renewals, helping to settle claim disputes, and reviewing stop-loss policies to assure that plan sponsors are protected to the fullest extent possible.



For more information about or assistance with stop-loss insurance, contact your Segal Company benefits consultant or Peter Kavanaugh at 312.984.8650 or pkavanaugh@segalco.com.

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