CAPTIVE REVIEW

EMPLOYEE BENEFITS REPORT 2013

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GROWTH

As parent companies grow, so do the risks involved in their employee benefits

REINSURANCE

How this kind of arrangement can pay dividends for large employers

HEALTHCARE

Group structures gain recognition within the US, as healthcare reform becomes a key driver

FEATURING

Allianz Group / Berkley Accident & Health / Granite

The rise of the EB group captive

As employee benefits becomes a more expansive risk area to insure, **Jim Hoitt** of **Berkley Accident and Health** examines the advantages a stop-loss group captive can deliver to a US employer

In the US, group captives are gaining recognition as a viable way for employers to finance their private employee health benefits. Captives are cost-effective and long-term solutions that are becoming increasingly popular among small and midsize employers.

Unlike the fast, short-term time horizon of commercial health insurance, captives provide a stable, long-term environment that allows employers to focus on employee health and wellness strategies. Captives serve as an incubator to enable tailored, innovative risk management strategies to take root.

Employers first saw the benefits of group captives in the historically limited market for small and midsize employers providing self-funded health benefits for their employees. Berkley Accident and Health, a part of the US-based W.R. Berkley family of companies, introduced an approach (called EmCap) that marries the economies of scale of group captives with the control and transparency of self-funded health plans. While Berkley's approach is entirely flexible and captive-neutral, its segregated account captive model provides a cost-effective, turnkey solution for employers who don't have the time and resources to build a wholly owned captive.

US market of the past

History has shown that true innovation is born out of market-based needs. Innovators succeed by adapting existing products or strategies in new and unique ways. Traditionally, the alternative risk marketplace has been the setting for forward-thinking corporations to find solutions to their problems.

In the US, however, the alterative risk market was not meeting the major challenges facing employers:

1. Healthcare costs outpacing inflation in the rest of the economy

Cumulative increases in US healthcare costs have grown faster than all other broad financial growth metrics. From 1999 to 2010, health insurance premiums grew by 138%, while overall US inflation increased by only 31% during the same period.

2. Increasing government regulations

Starting in the 1990s, employers became burdened by a growing layer of healthcare regulations and consumer protections, all of which added to the cost and complexity of offering employee health benefits. Most recently, the federal Patient Protection and Affordable Care Act, along with various proposed state regulations, have left many employers feeling so overwhelmed by compliance that they have little time to explore alternatives.

3. Few options left for employers to control costs

US employers recognise that their healthcare costs are ultimately tied to the health and claims experience of their employees. However, in more than half of the states in the US, 70% of the market share is controlled by the three largest commercial health insurers in that state. This concentration of power leaves employers with few competitive alternatives. In addition, commercial insurers provide small to medium size employers with limited or no useful claims data. Therefore, it is virtually impossible for employers to plan and implement strategies to improve the health of their employees and therefore, control escalating costs.

As a result, small employers, with their limited resources and staffing, were more inclined to simply negotiate rates with the dominant commercial insurers than investigate new solutions. Only large employers had the resources needed to self-fund their employee benefits.

US market of the present

Today, large employers still look to self-funding as a method of choice to combat the overhead and inflexibility of the commercial marketplace. An estimated 96% of employers with over 5,000 workers self-fund their employee health benefits. When a US employer self-funds, it 'owns' its claim data, which is incredibly useful in plotting risk management strategies and setting measurable milestones. Large employers are empowered to take control of their costs, retain the cost savings, and invest in strategies that improve their long-term outlook.

The hard part is translating this outlook to small and midsize employers. To self-fund, small and midsize employers face two challenges:

- First, even well-capitalised employers cannot bear the risk exposure and volatility of a self-funded health benefit plan.

• Second, the lack of credible claims data makes it difficult to assess and project the financial risk.

To solve this problem, enter medical stop-loss insurance. Medical stop-loss insurance gives self-funded employers with two levels of protection:

• Individual coverage for any single health claim that exceeds a pre-determined deductible;

• Aggregate coverage for an unexpected increase in overall utilisation by the entire group .

Stop-loss insurance gives self-funded employers a financial backstop by limiting their exposure to unanticipated health claims. By retaining a tolerable, predictable amount of risk and transferring the higher level of risk to an insurer, the employer gains control over a significant portion of their healthcare costs.

Within this strategy, however, there is one final problem for small and midsize employers to solve. If employers set their retention level too low, then their stop-loss premiums become very expensive and are subject to big increases every year due to medical cost inflation. At renewal, employers may increase their retention level to offset the stop-loss premium increases – but this may lead to employers assuming bigger risks at renewal that are hard to swallow.

On the other hand, if employers set their retention level too high, then their stop-loss premiums may become more affordable and stable, but their balance sheet may be put at risk because of the uncertainty of future claim costs, due to lack of solid claims data at the beginning.

To solve this no-win situation is the EmCap Group Captive programme. Berkley Accident and Health designed EmCap to allow small and midsize employers to enjoy the spread of risk only available historically to larger employers. Employers with self-funded health benefits can purchase stop-loss insurance from an insurer and then the insurer reinsures a layer of the stop-loss risk to a group captive in which the employer participates.

US market of the future

The EmCap solution gives self-funded employers a chance to benefit from the upside, or times of positive claims variability. Employers manage their risk at a tolerable level for their company. Employers join the group captive, which becomes more stable and predictable as more employers join. The group captive, in turn, buys stop-loss insurance above the group captive layer to protect its members from the downside, or times of negative claims variability.

Perhaps most importantly, the group captive creates a collaborative environment for employers to implement creative and intelligent health risk management strategies. It is a community where employers in the captive can share success stories, evaluate and leverage service partners, and invest aggressively and confidently in strategies, knowing that they – and not an insurance company – will benefit most by any efforts to contain costs.

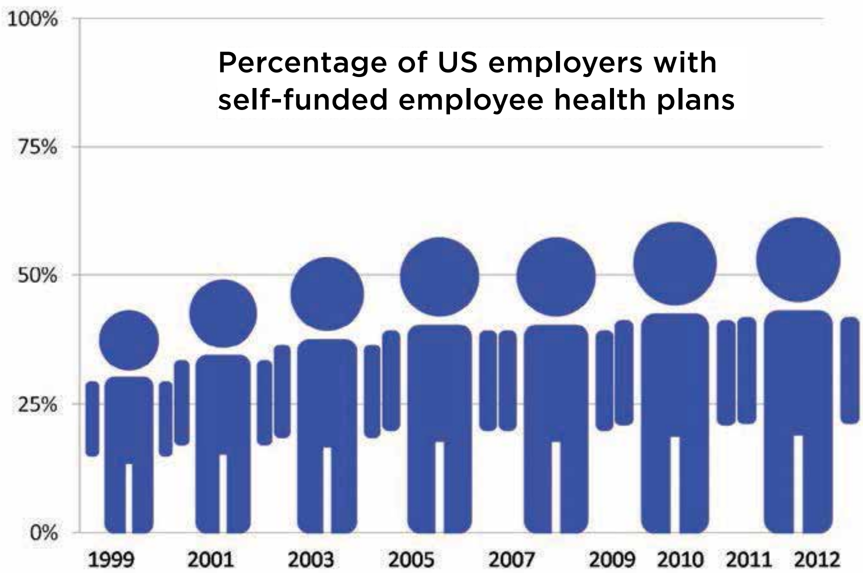
JIM HOITT
is the vice-president of sales at Berkley Accident and Health. With over 18 years' experience in self-funding and stop loss arrangements in the US, Mr. Hoitt is responsible for the distribution of Berkley's stop loss and group captive programmes.

Berkley's EmCap solution, and its philosophy in general, is focused on giving employers the tools to better manage their health and accident risk. As one of the largest providers of medical stop-loss insurance in the US, Berkley has long recognised that the main risk-taker in a self-funded plan is not in the employer.

In a country dominated by employer-sponsored healthcare plans, US employers are the market drivers. Change will come from the buyers of healthcare, not the providers. Realistic and intelligent employers want to control their enterprise risk, and skyrocketing healthcare costs are the most glaring opportunity *(see graph below)*.

The EmCap solution, which is a stop-loss group captive, emphasises several proven strategies designed to give employers more control over their risk and meshes them together. At its simplest, this approach is a funding mechanism that reduces volatility and insurer overhead. At its most complex, it creates a vacuum-sealed laboratory for like-minded employers to collaboratively invest in the health and wellness of their employees.

At our company, the continual growth in EmCap programmes is the best testament to gauge market response. As with all captives, the challenge remains containing programme costs, and long-term success will be measured by the actions of the members themselves. Considering the alternatives, most US employers would welcome that challenge.



Kaiser/HRETEmployer Health Benefits Annual 2012 Survey, Percentage of Covered Workers in Partially or Completely Self-Funded Plans, by Firm Size, 1999-2012, ehbs.kff.org