ART Gallery column for September

Scared of Obamacare? Here's one Cure

By Dick Goff

Obamacare's apparent threat of providing unlimited lifetime health benefits to members of employee health plans has become the monster in the closet – you're afraid to open the door and you're afraid *not* to open the door. Stop-loss insurance costs are expected to zoom to the stratosphere, or else employers will chuck the whole thing and just write a check for the new tax.

The monster wins in either of those scenarios. But Roosevelt was right (maybe about this one thing): *There is nothing to fear but fear itself.*

Here's another scenario: Transfer the risks of very large health claims into a captive where catastrophic losses may be expected, and dealt with as they come, from a pool large enough to return some underwriting profit. You can be afraid of the monster or you can tame it to dance a jig at circus sideshows and keep all the quarters it collects as your profit rewarding your intelligence and verve.

Would that be ART coming to the rescue of employers?

It will take a few words of explanation to wrap your mind around this concept. Heck, it's taken me a couple of years just to try writing it down.

Let's start at the beginning with first principles of self-insurance for an ERISA employee health plans. Traditionally the plan sponsor self-insures losses up to a self-elected retention level, and buys traditional stop-loss insurance to cover specific and aggregate losses in excess of the retention. Self-insurance 101, right?

Now, moving into less familiar territory, let's say several self-insured benefit plans (or 1,000) become members of a pool for the purposes of their stop-loss coverage. If a captive insurance company were to be formed for that purpose, it could insure each plan's excess losses over their retention levels.

All it takes is for someone like an insurance company, a big MGU or TPA to start the captive. A few of these excess coverage captives already exist on a modest level and you can learn more about them at SIIA's national conference in October. Check sessions in the ART track.

The strength of this kind of ART structure is that it's got the law of large numbers working for it. That law has nothing to do with tickets for three-digit speeds in a western state where enforcement was supposed to be lax but that's another kind of large number story. For today's purpose, the law simply and irrefutably states that the more risk-takers there are in a pool, the less any given risk will cost its members.

Or the captive could be structured in individual incorporated cells to keep everyone's risks in separate silos up to an actuarially predetermined assumption level prior to buying stop-loss coverage for all but specific named risks that potentially could become catastrophic losses. This would benefit plan sponsors that could actuarially forecast their most expensive risks. And the captive can be counted on for underwriting profit, investment profit and possibly tax advantages for the owner-insureds.

A point to be considered is that by using a captive to insure excess losses, and then buying reinsurance through the captive on a pooled basis to cover catastrophic losses, insureds are pushing traditional commercial involvement in their risk management farther out – or farther up the financial ladder, whichever image you prefer.

This could be called stair-stepping risk attachment levels for specified risks. I predict stair-stepping will replace cherry-picking in the benefits lexicon. Of course the metaphors are already related as some harvesters climb ladders to pick cherries.

In this kind of risk attachment level stair-stepping, a health plan could determine various attachment points, moving higher as the risks become increasingly expensive. Conditions such as certain cancer treatments, premature babies or organ transplantation come to mind.

While each cell within the large group captive could attach its excess loss coverage at varied levels to cover specific and aggregate health risks, all cells would participate in a pool to cover those few truly catastrophic claims. As an aside, the million dollar claims that everyone fears are not that common in reality. I asked an executive of a leading stop-loss carrier how many he had seen in his career and he estimated that number would be five.

An ART structure like this would certainly surmount Obamacare's scary requirement of unlimited lifetime benefits for members of employer benefits plans. The question is: Why doesn't everyone do it?

One response resides within that law of thermodynamics stating that an object in motion tends to continue in motion. My corollaries are: A buyer of stop-loss insurance tends to continue to buy the same product, and a seller of stop-loss insurance tends to continue to sell the same product.

But the joker in that deck is the difficulty of pricing unlimited stop-loss insurance without creating a captive-reinsurance structure that can deal with the catastrophic anomalies.

As I noted earlier, it will take a visionary service provider with access to a large number of self-insured benefit plans to make this work. Do we have any volunteers?

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