

35TH ANNUAL ISCEBS
Symposium

Employee Benefit Group Captives: A Gateway to Self-Funding

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PARTNERS IN EDUCATIONAL EXCELLENCE



International Society
of Certified Employee Benefit Specialists

International Foundation
OF EMPLOYEE BENEFIT PLANS



Today's Agenda

1. Group Captives—What, Why, How, Who
2. The Market Climate
3. Stop Loss Group Captives
4. Financial Scenarios
5. Other Considerations
6. Next Steps

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What is a Captive?

A Captive is a medium for taking risk.



It can be formed by
a **single** company



Single Parent Captive

Or **multiple** companies



Group Captive

What is a Group Captive?

A Group Captive can be made up of companies in the same industry or different:

Same industry



Closed membership
(Homogeneous)

Different industries, sizes,
or regions



Open membership
(Heterogeneous)

Why do Group Captives exist?

Group Captives exist to give employers:

- ☑ Control
- ☑ Lower overhead/inefficiency from insurance carriers
- ☑ Long-term stability
- ☑ Capacity
- ☑ Data transparency
- ☑ Collaboration/best practices

Who are Good Candidates?

Good candidates are typically companies with:

- ☑ 50-500 eligible employees
- ☑ Forward-thinking management team
- ☑ Good communication with employees on health care costs
- ☑ Willing to implement robust health/wellness programs
- ☑ Financially stable and willing to take on a portion of the health plan risk

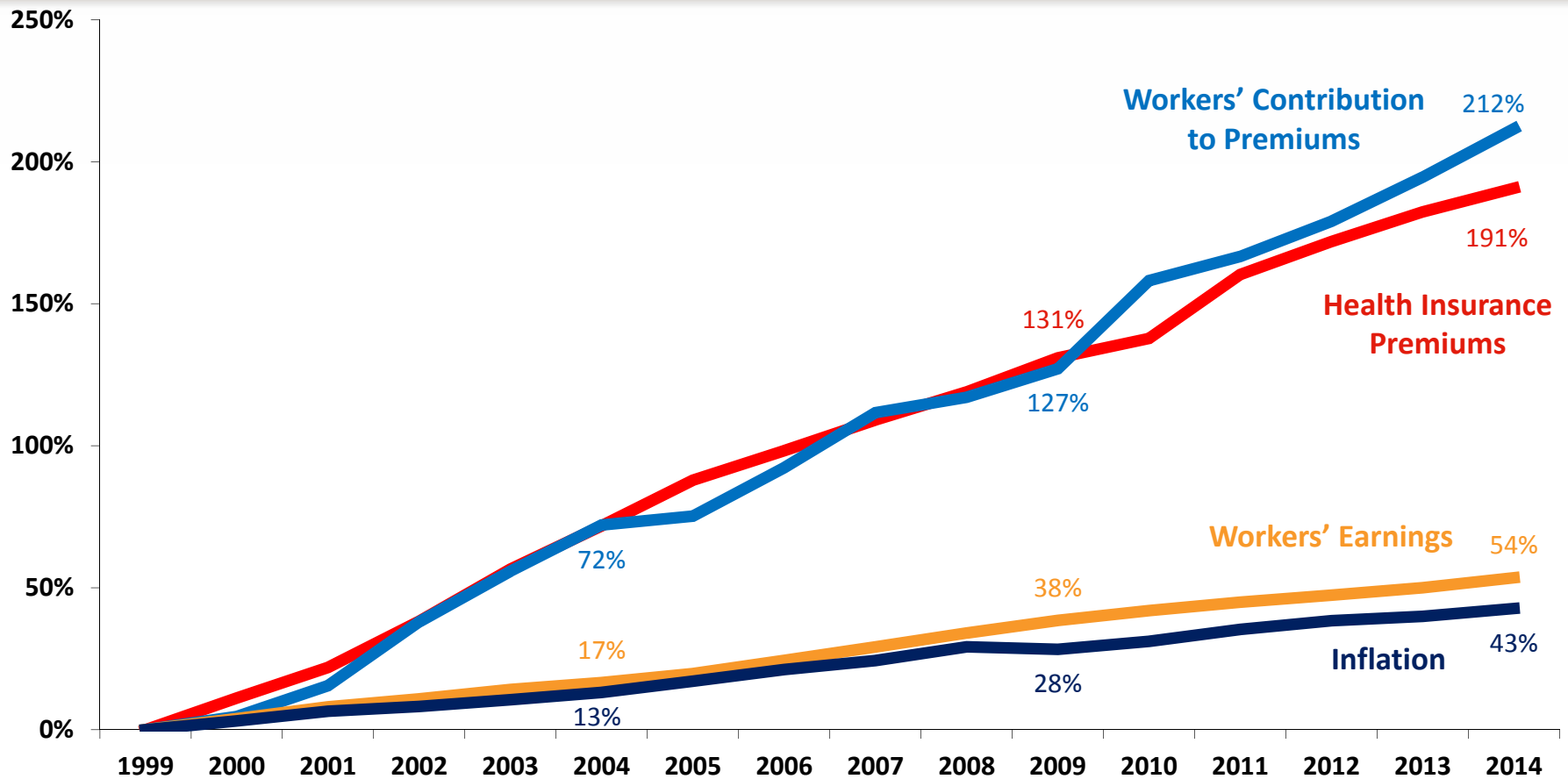
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An Unsustainable Path: 1999-2014



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2014. Bureau of Labor Statistics, Consumer Price Index, U.S. City Average of Annual Inflation (April to April), 1999-2014; Bureau of Labor Statistics, Seasonally Adjusted Data from the Current Employment Statistics Survey, 1999-2014 (April to April).

An Unsustainable Path

		2013	2014	2015	2016	2017
Revenue	↑ 3%	\$5,000,000	\$5,150,000	\$5,304,500	\$5,463,635	\$5,627,544
Expenses						
Employee Benefits	↑ 10%	500,000	550,000	605,000	665,500	732,050
All Other Expenses	↑ 3%	4,000,000	4,120,000	4,243,600	4,370,908	4,502,035
Total Expenses		\$4,500,000	\$4,670,000	\$4,848,600	\$5,036,408	\$5,234,085
Pre-Tax Margin		\$500,000	\$480,000	\$455,900	\$427,227	\$393,459
After-Tax Margin	(in \$)	\$325,000	\$312,000	\$296,335	\$277,698	\$255,748
	(in %)	6.5%	6.1%	5.6%	5.1%	4.5%
Margin Erosion			-6.8%	-14.1%	-21.8%	-30.1%

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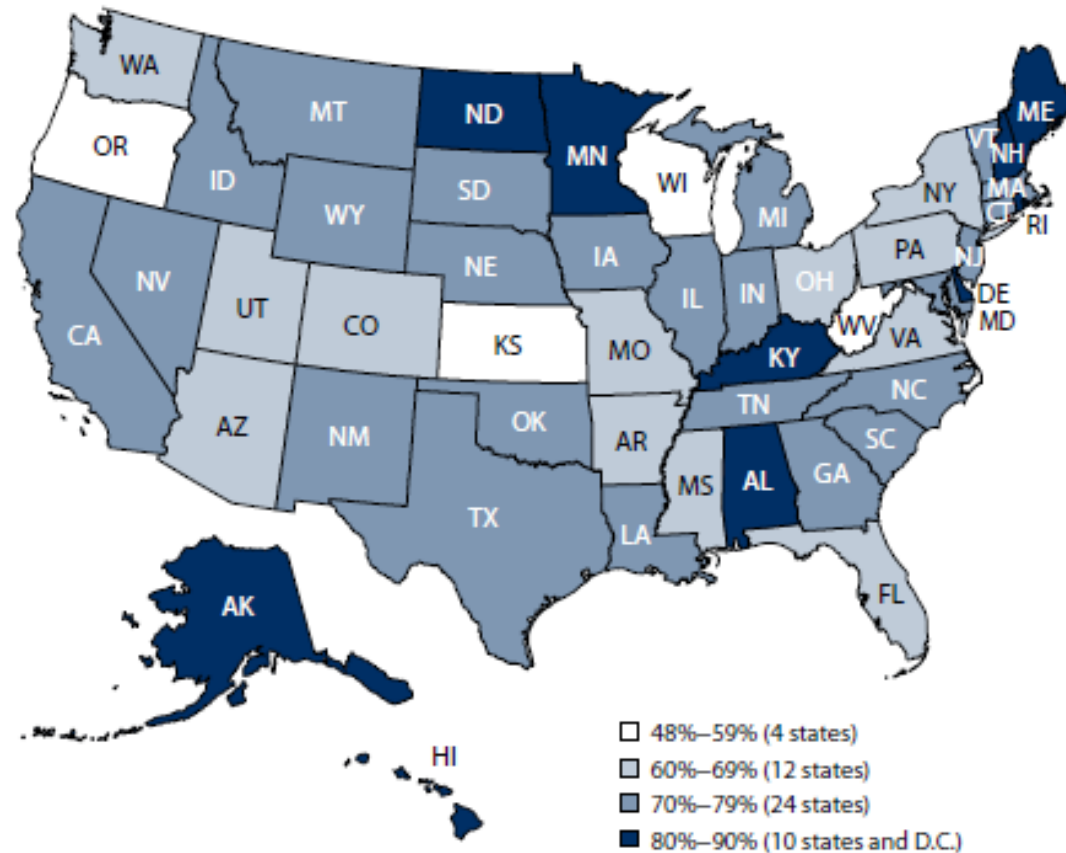
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Who wants to be CFO of this company?

Options for Financing Health Plans

- A. Fully Insured Plan
- B. Self-Funded Plan
- C. Emerging: Group Captive

Option A—Fully Insured



Market Share of
Three Largest
Health Plans

by State, 2010

Source: Analysis of Managed Market Surveyor, HealthLeaders-Interstudy (Jan. 2010), HealthLeaders-Interstudy.

Option A—Fully Insured

- Significant rate increases every year, with little or no meaningful data
 - Are you supporting the market, or being supported by it?
 - Where do the premium dollars go?
- Buying cycle isn't linked to true cost
- Your available options:
 1. Change carriers
 2. Shift costs—By changing benefits or contributions

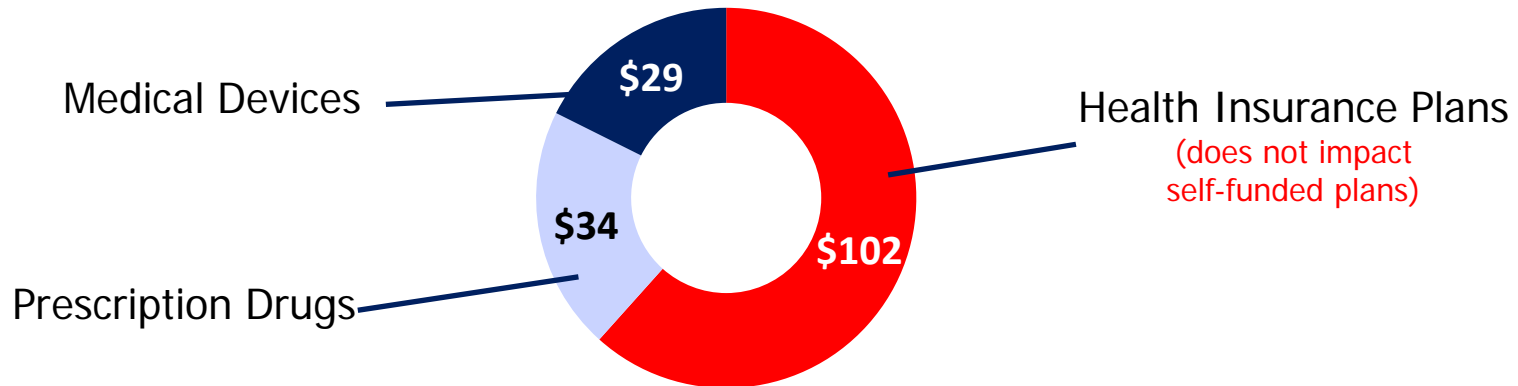
Option A—Fully Insured

Affordable Care Act (ACA) hits fully insured plans the hardest

ACA's Ten-Year Total Tax Impact = \$164 billion

Small Employers	+\$2,760 single	+\$6,830 family
Large Employers	+\$2,610 single	+\$7,130 family

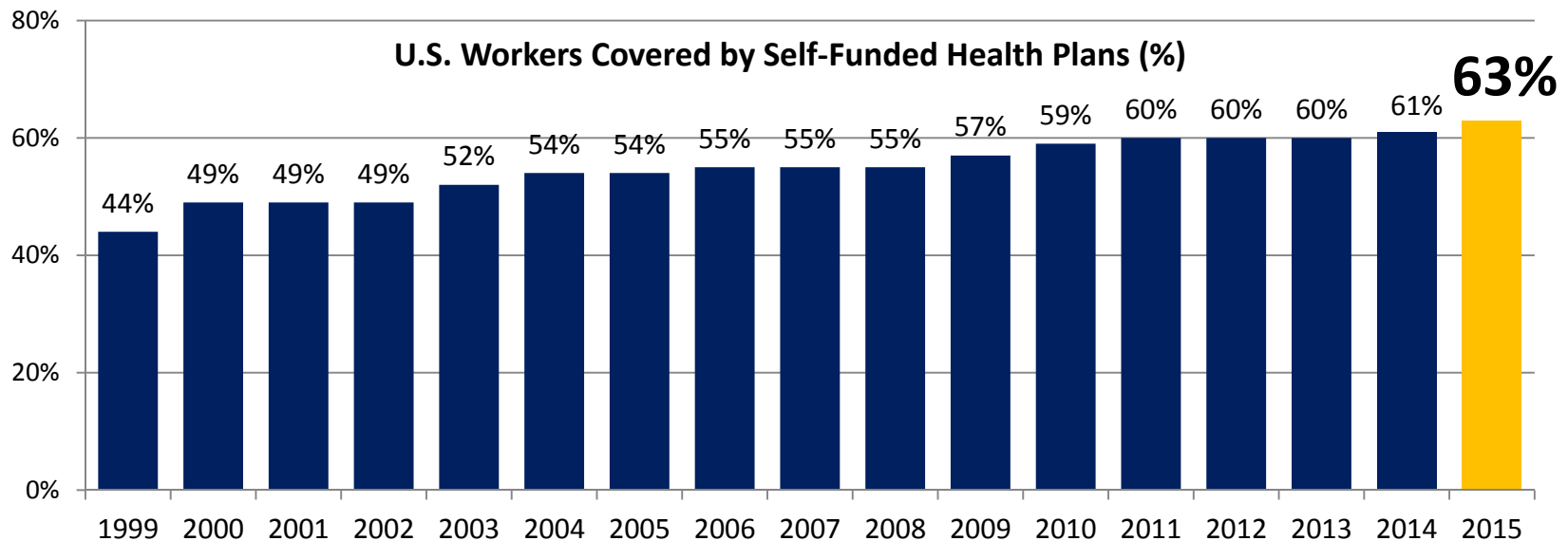
ACA's Tax Sources (in billions)



Source: Effects of the PPACA Premium Tax on Small Businesses and Their Employees: An Update, <http://www.nfib.com>; Estimated Premium Impacts of Annual Fees Assessed on Health Insurance Plans, <http://www.ahip.org>; based on the ten-year period from 2014-2023; AHIP 2013.

Option B—Self-Funded

Today, the majority of workers are in self-fund health plans



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 1999-2015

Option B—Self-Funded

Advantages of self-funding

1. Traditional Advantages

- Cash flow advantages; no pre-funding of claims
- Data transparency
- Multi-state plan design; flexibility; ease of administration
- Lower fixed costs
- Exempt from premium tax
- Retain carrier profit

2. Under ACA

- Not required to provide coverage with minimum essential benefits
- Not required to participate in a risk-adjustment system
- Not subject to provisions, such as Medical Loss Ratio requirements and premium increases

Option B—Self-Funded

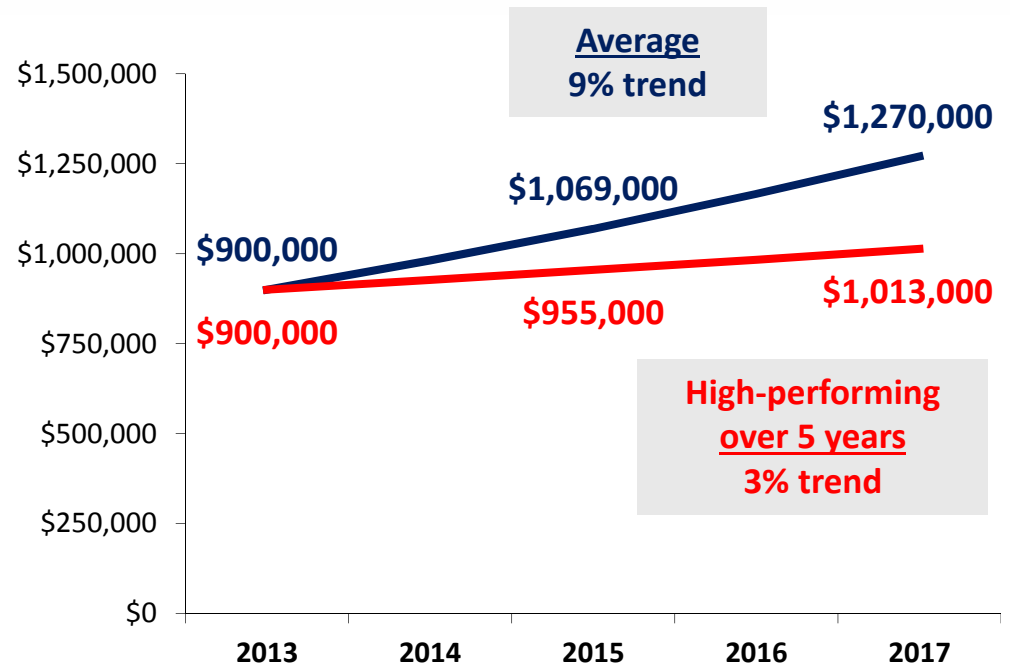
Why do large employers self-fund?

- Significant advantages to self-funding
- They have the financial leverage to assume risk
- They have the size to provide predictability (lower risk premium)
- They purchase medical stop loss at a higher retention level (mitigation/stability) = Less insurance
- They can implement best-practice health risk management strategies (high-performing companies)

Option B—Self-Funded

Proactively manage your health risk

- Impact is huge
- Employer health premiums have increased at a compounded rate of 9% for the last 10 years¹
- “High-performing” risk companies have trend at or below 3%²

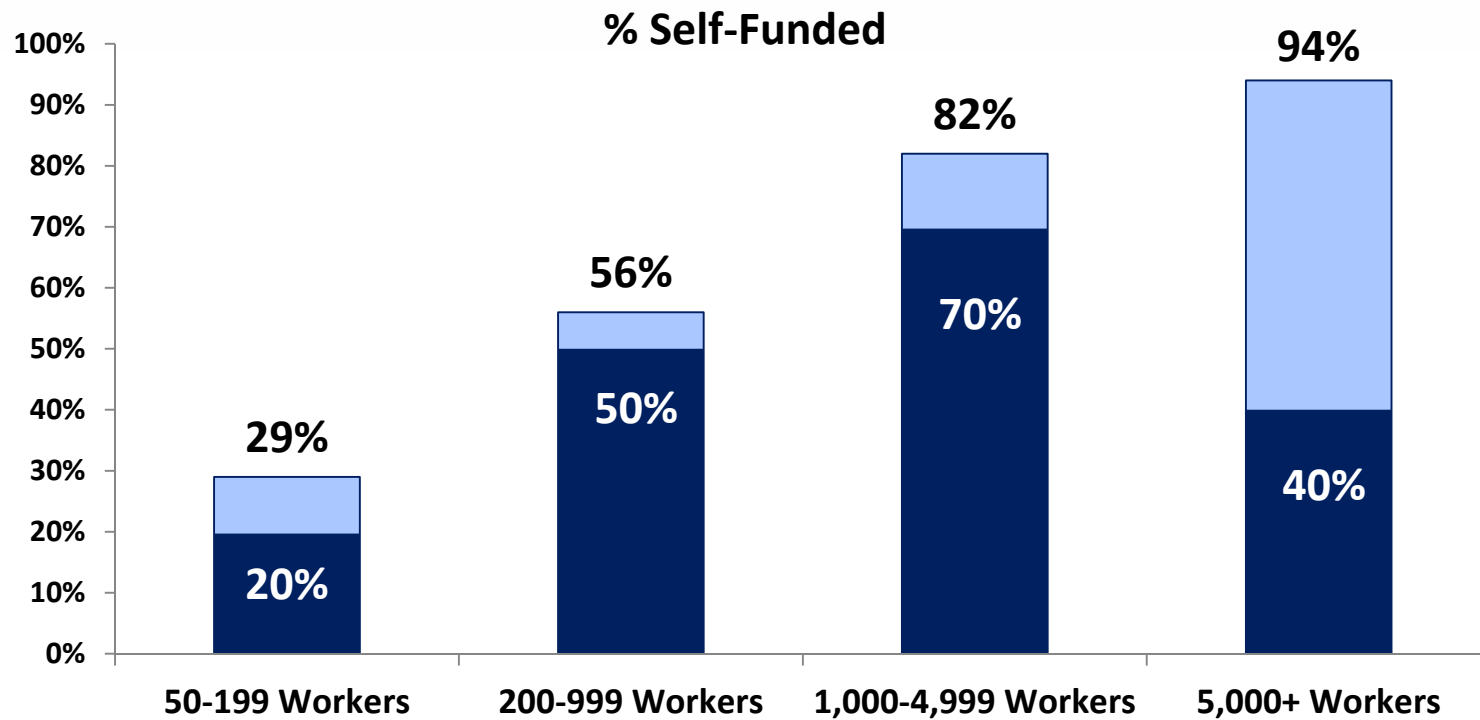


¹Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 2013, www.kff.org.

²Towers Perrin, annual study of health insurance costs

Option B—Self-Funded

Employers that self-fund with and without stop loss



Source: Kaiser/HRET Survey of Employer-Sponsored Health Benefits, 2015, www.kff.org.

Option B—Self-Funded

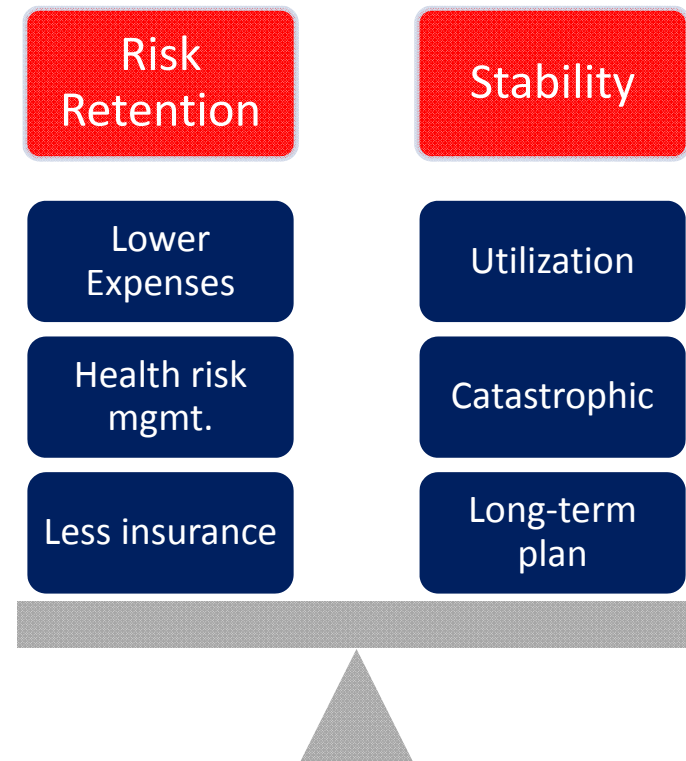
How does Medical Stop Loss insurance work?

- Covers catastrophic or unpredictable losses
- Protects the self-funded employer's assets
- Individual/Specific Stop Loss
 - Protects against high claims from any one individual
 - Protects against the severity of a single catastrophic claim
- Aggregate Stop Loss
 - Provides a ceiling for overall claims liability
 - Protects against higher-than-expected usage or frequency of claims from the entire group

Option B—Self-Funded

Challenges of self-funding for midsize companies

- Retaining risk
- Long-term focus
- Data overload
- Volatility and lasering
- Resources to manage health risk programs

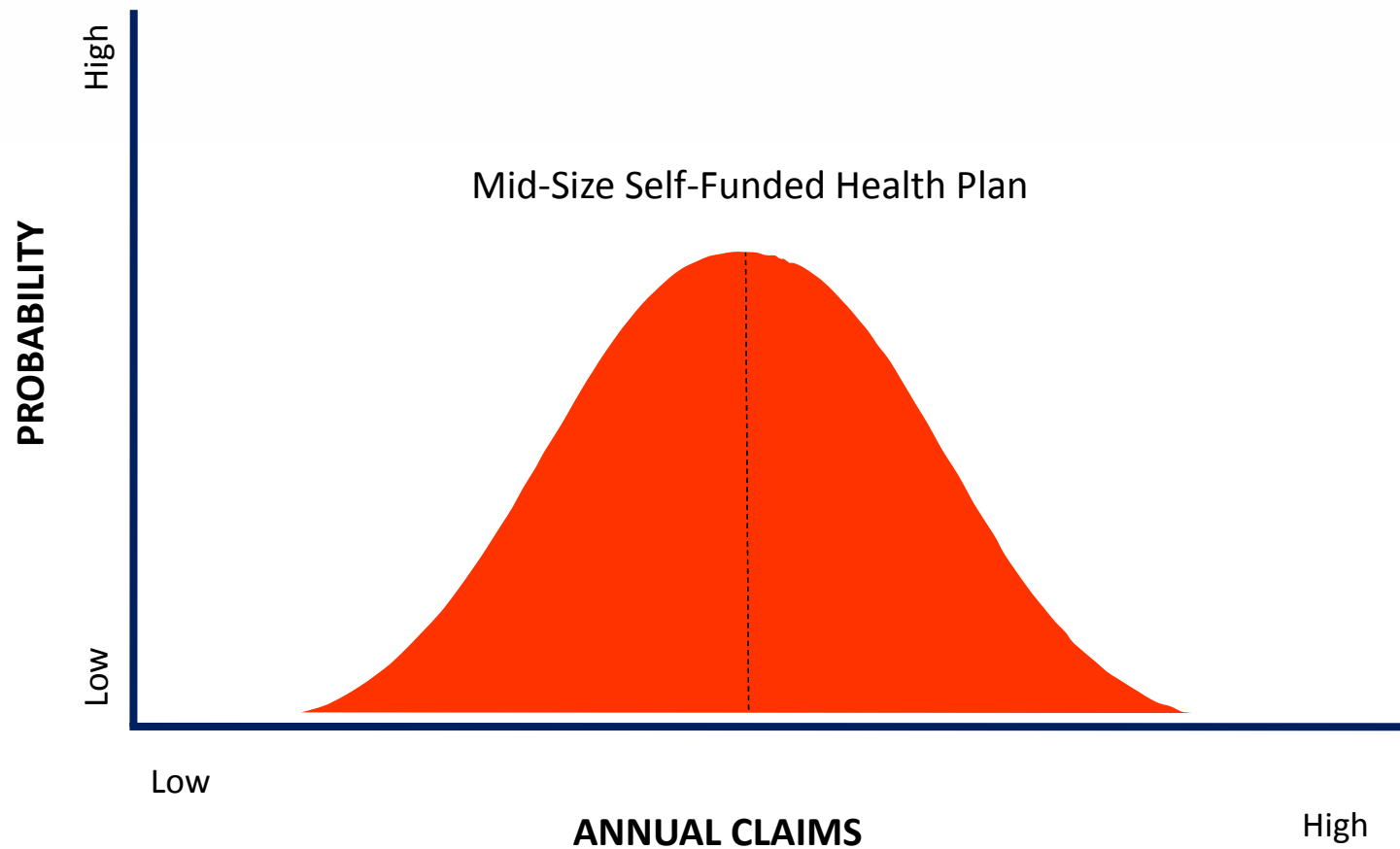


Why Don't More Employers Self-Fund?

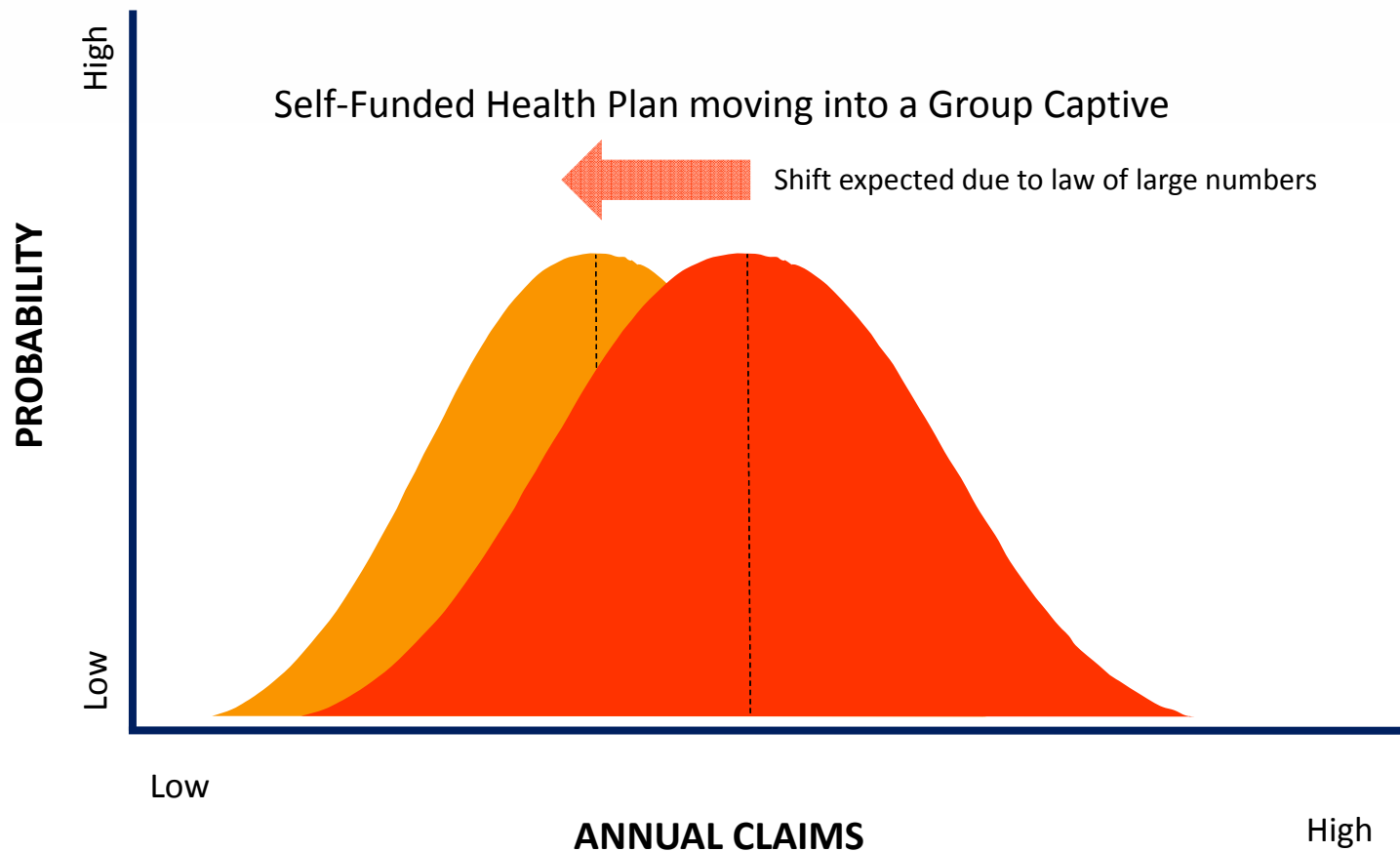
Challenge: How do you create the *large* employer advantage for *small and midsize* companies?

1. Self-funding provides benefits typically enjoyed only by large companies:
 - **Control**
 - **Transparency**
2. Group Captives can provide **stability** by spreading risk across its members
3. Health risk management can lower short- and long-term cost trends:
 - **Opportunity to control costs**

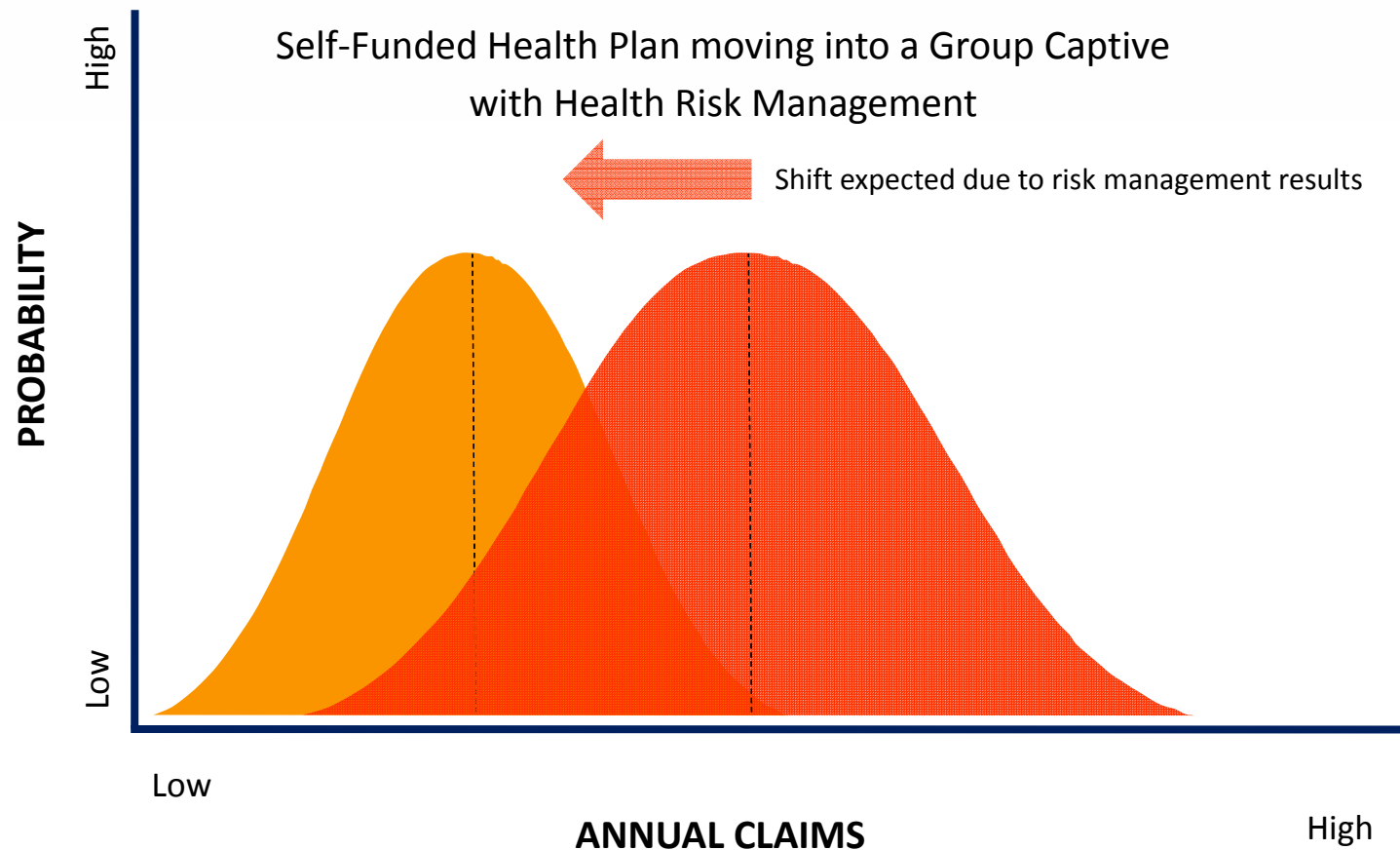
Why Don't More Employers Self-Fund?



Group Captives Mitigate Volatility



Group Captives + Health Risk Management



Option C—Group Captive

Group Captives bring it all together by allowing small employers to act like large employers:

1. Traditional advantages of self-funding
2. Additional advantages with ACA
3. Best practices for health risk management
4. Collaborative financial strength
5. Greater scale for predictability
6. Buy less Stop Loss insurance (higher deductible)

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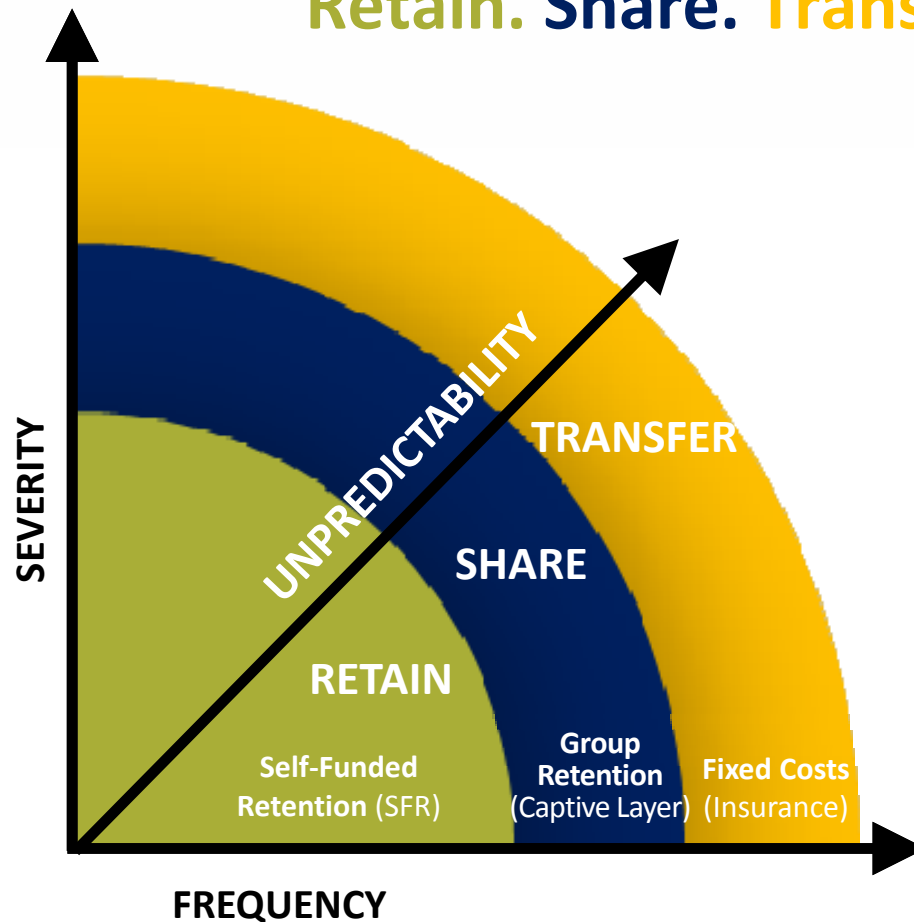
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Predictability and Probability

Retain. Share. Transfer.



Group Captives = a funding strategy, NOT a benefit plan design strategy.

Risk Layers: Claims Exposure/Costs

Retain. Share. Transfer.

Stop Loss Retained Layer

Retained Excess + Captive Aggregate Coverage + Fixed Costs

Risk assumed by
Stop Loss insurer
>\$250k individual
and captive max

Group Captive Layer

Premium + Non-Premium Funding (collateral)

Risk shared among
members in captive

Employer Layer

Employer	Employer	Employer	Employer	Employer
1	2	3	4	5
(SFR)	(SFR)	(SFR)	(SFR)	(SFR)

No risk sharing
Employers pay for
claims up to
Stop Loss
(Individual or
Aggregate claims)

Step 1–Self-Fund

Retain risk

Each employer:

- Chooses to self-fund its employee health benefits
- Creates and manages its own self-funded health plan
- Commits to a focused and consistent strategy of health risk management
- Pays for claims on behalf of its plan

Step 2–Buy Stop Loss Policy

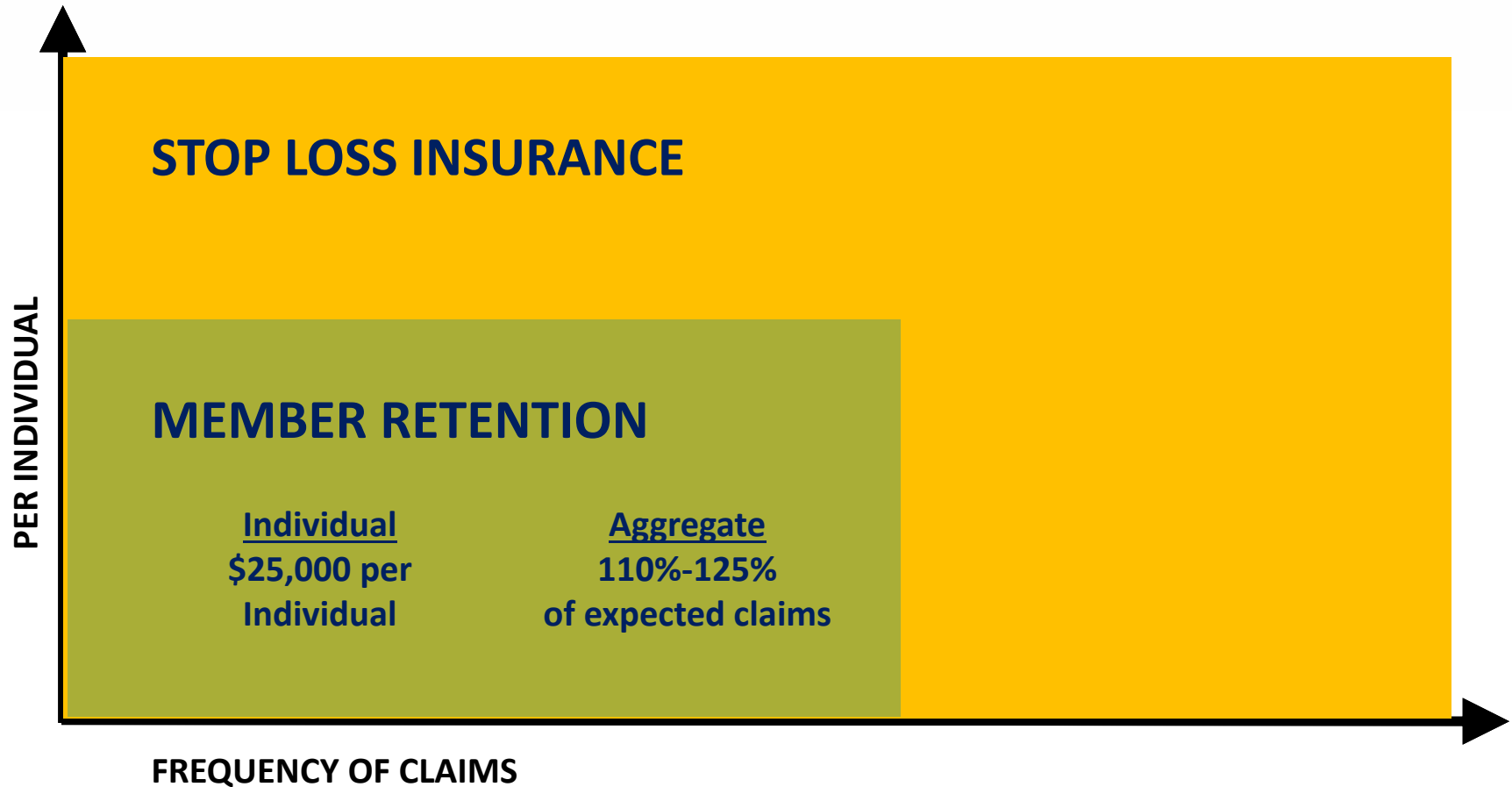
Transfer risk

Each employer:

- Buys a Stop Loss policy with Specific and Aggregate protection (individually rated; no group rates)
- Determines own retention levels (\$25k used for example purposes)
- Pays premiums to insurer for Stop Loss policy
- Gets reimbursed by Stop Loss policy for covered claims above Specific or Aggregate level

Stop Loss Policy Structure

Retain. Share. Transfer.



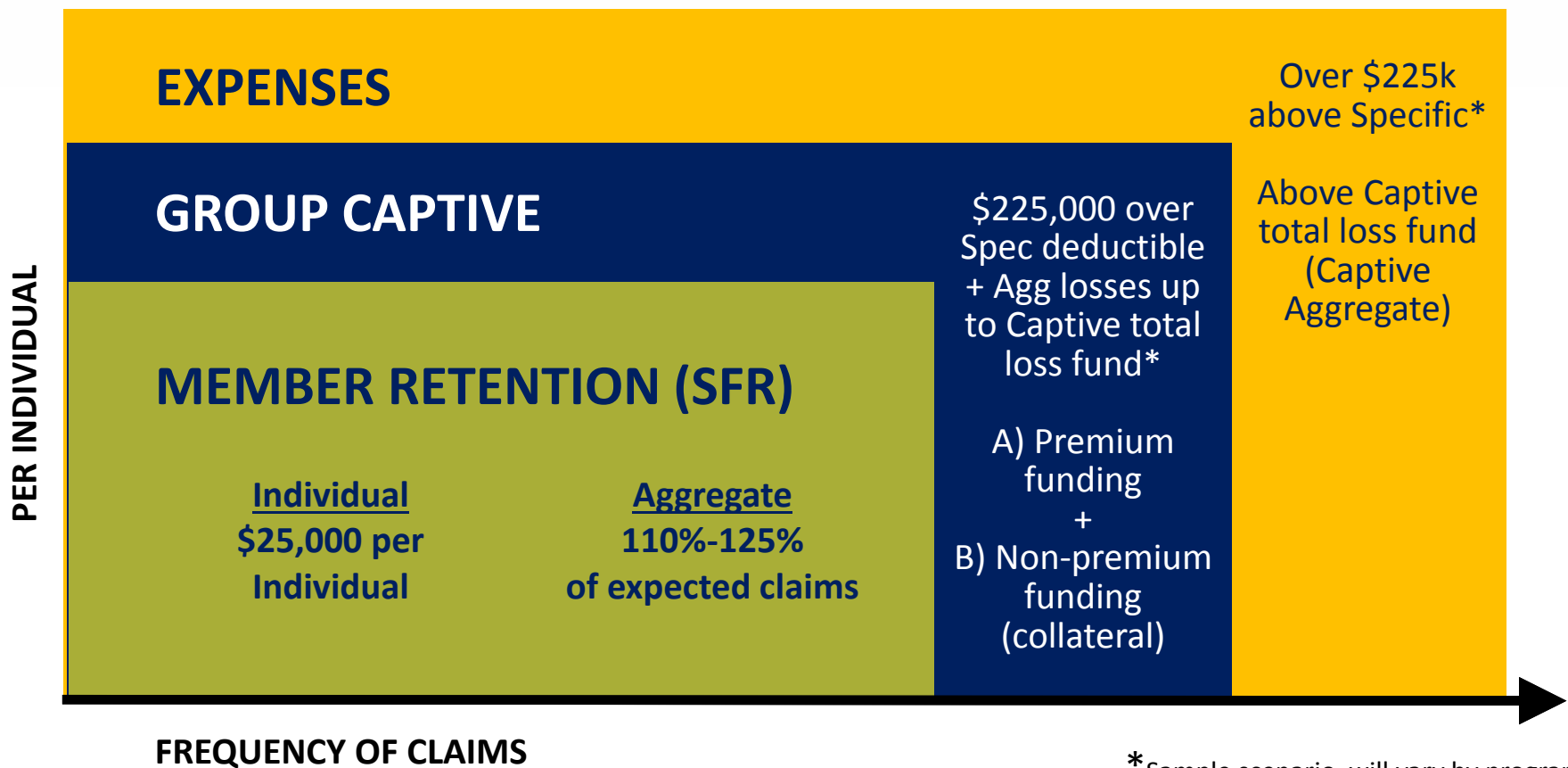
Step 3—Join the Group Captive

Share risk

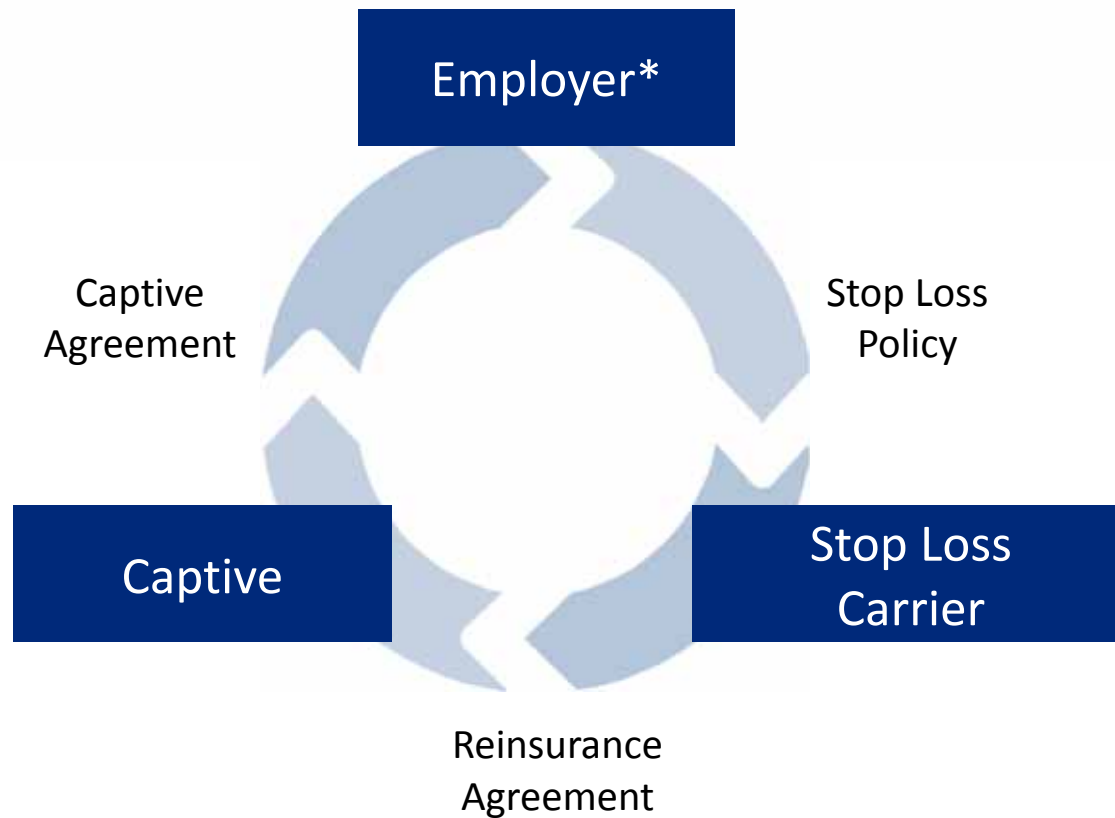
- Stop Loss carrier reinsures the layer between \$25,000-\$250,000 per individual to a captive
- The captive is a reinsurer of the Stop Loss carrier and does not issue policies
- The captive receive premium for the layer from Stop Loss carrier
- Each employer provides collateral to the captive, in case premiums are insufficient, and pays a fee to cover the captive's expenses
- Stop Loss carrier limits the captive's exposure with a program Aggregate

Risk Layer Funding

Retain. Share. Transfer.



Relationship of Parties



*Includes plan, broker, TPA, and risk management strategies

Large Claim Example

Employer has a \$600,000 claim from a premature birth:

STOP LOSS CARRIER

**Stop Loss policy reimburses
\$575,000 to the employer**

**GROUP CAPTIVE reimburses
Stop Loss carrier for \$225,000**

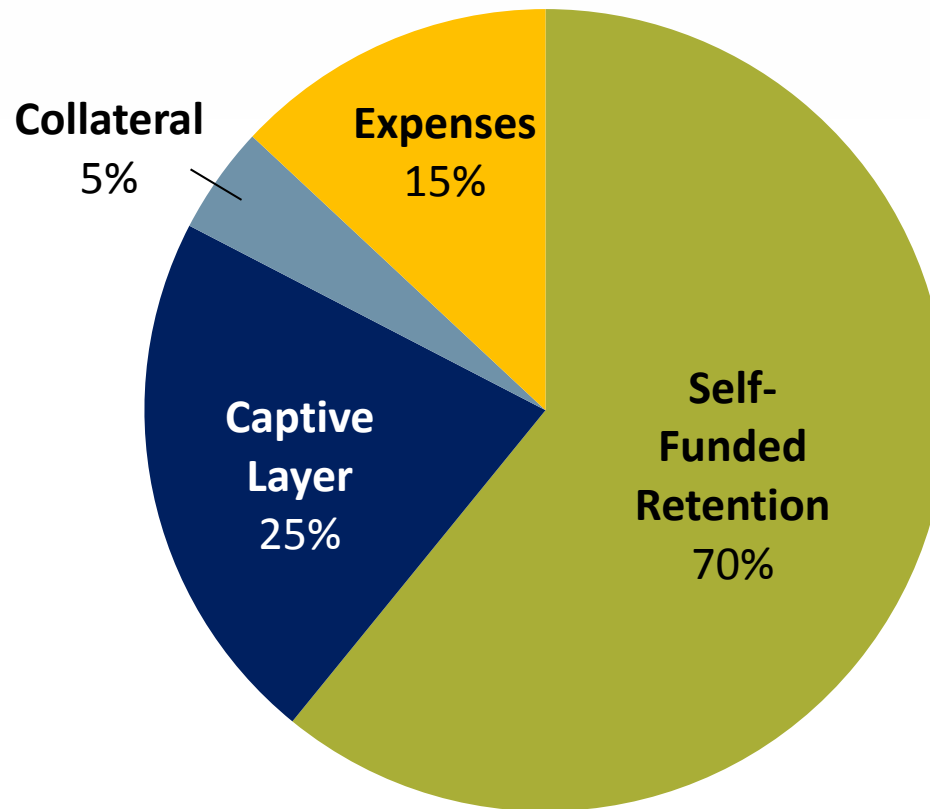
**EMPLOYER funds first \$25,000
through its self-funded retention**

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Costs, Results, and Financial Scenarios

Sample Captive Layers vs. Scenarios



Captive Proposal: Risk and Reward

Retain. Share. Transfer.

Sample Account	Captive Proposal	% of Fully Insured Premium Pie	
Currently Fully Insured Premium	\$2,500,000	100%	
Captive Expenses	\$375,000	15%	FIXED
Captive Self-Funded Retention	\$1,750,000	70%	VARIABLE
Captive Premium	\$625,000	25%	VARIABLE
Captive Collateral	\$125,000	5%	VARIABLE
Variable Costs	\$2,500,000	100%	
Projected Captive Minimum	\$375,000	15%	
Projected Captive Maximum	\$2,875,000	115%	

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← Current guaranteed cost

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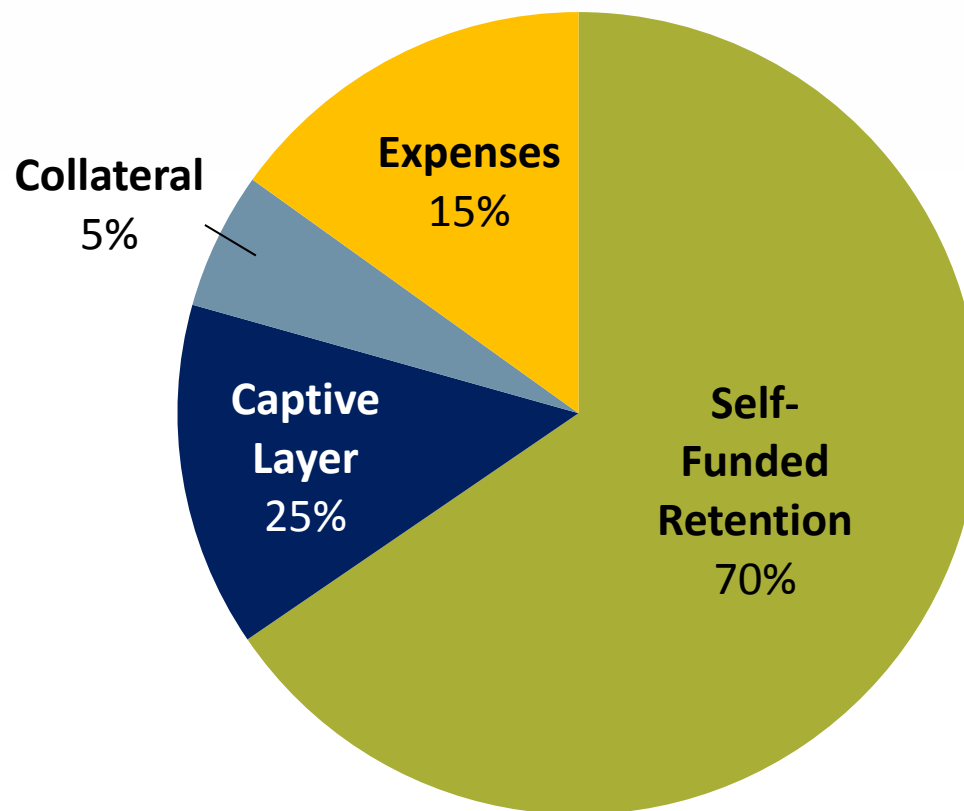
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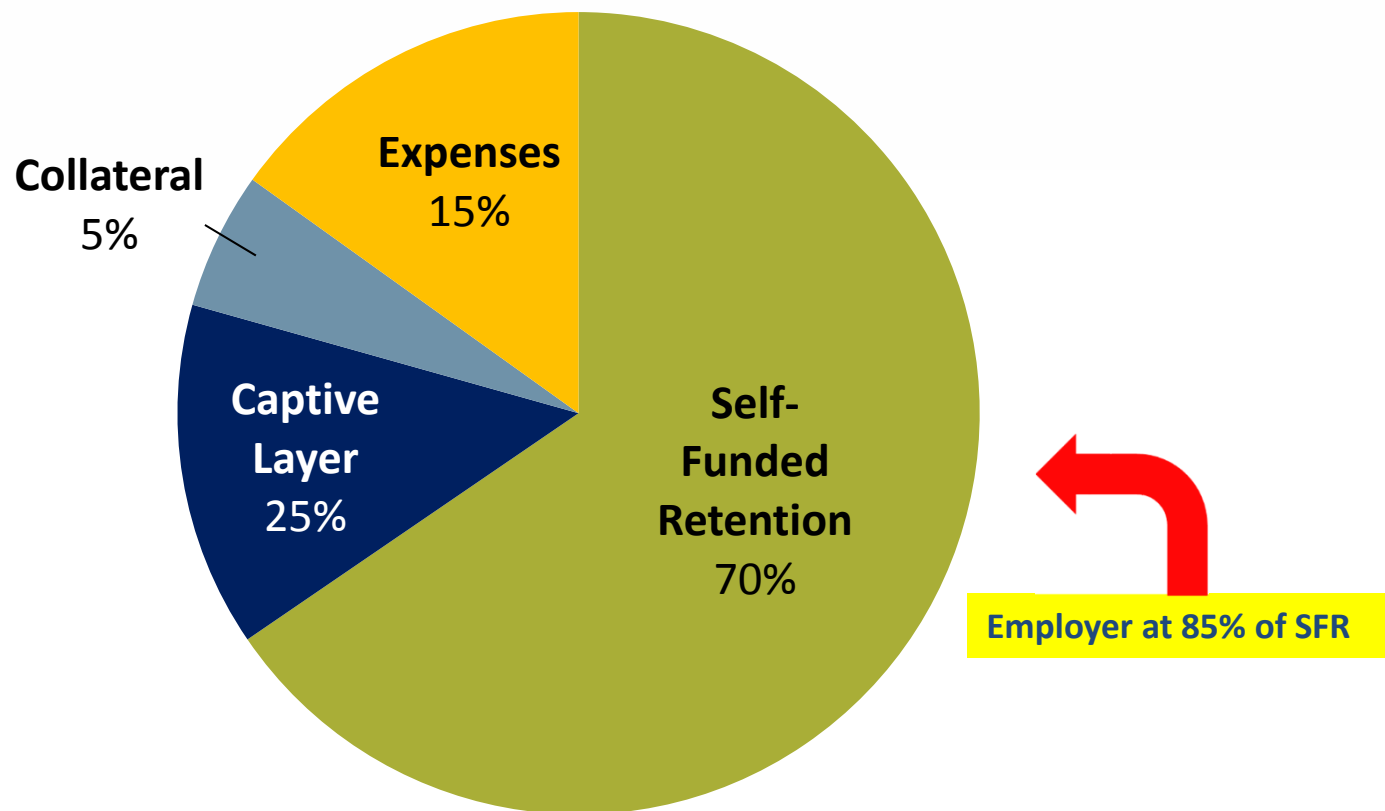
Potential risk or maximum cost

Captive Layers: Surplus Scenario



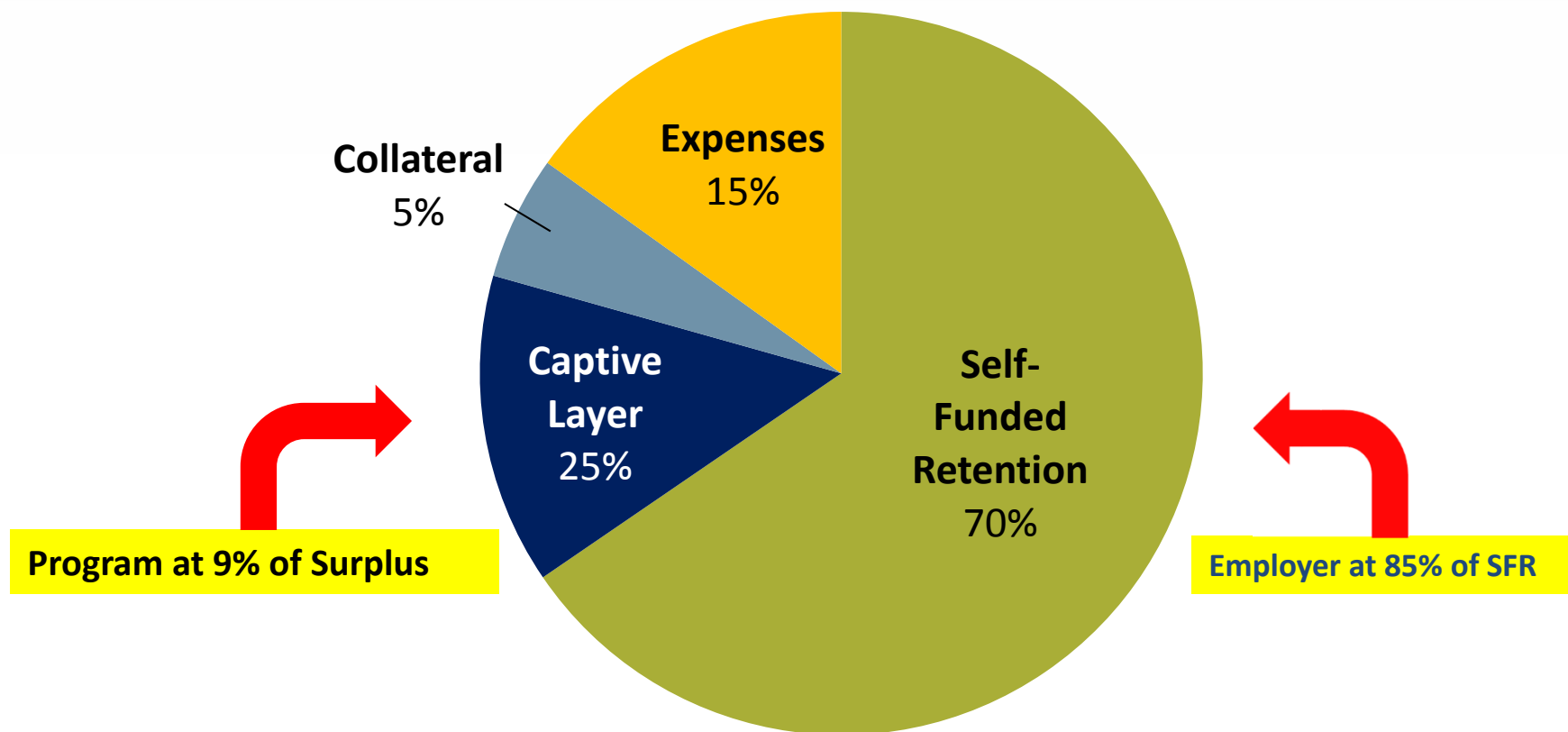
Past captive results are not a predictor of future results. Past performance does not guarantee future results. Actual performance may be lower or higher than the performance data shown.

Captive Layers: Surplus Scenario



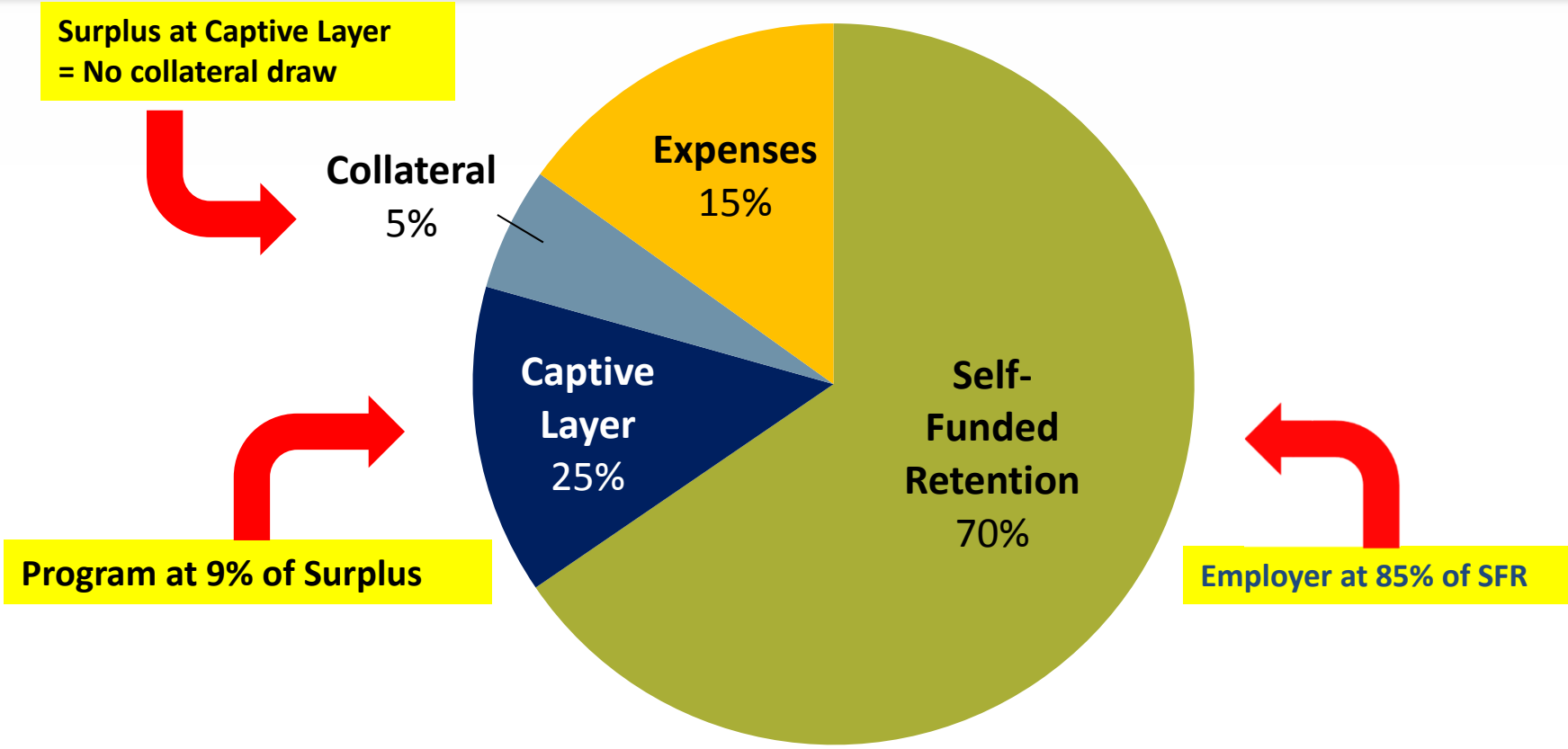
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Captive Layers: Surplus Scenario



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Sample Surplus

200 Lives, Fully Insured, \$25K Specific Proposal

Sample Account	Captive Proposal	Sample Results*	
Expenses	\$375,000	FIXED	\$375,000
Self-Funded Retention	\$1,750,000	85%	\$1,487,500
Captive Retention**	\$625,000	91%	\$568,750
Collateral	\$125,000	0%	\$0
Total Cost			\$2,431,250
vs. Insured Premium			\$2,500,000
Captive Total Savings			\$68,750

► **Potential savings opportunity, plus data, stability, and transparency**

* Past Captive results are not a predictor of future results. Past performance does not guarantee future results. Actual performance may be lower or higher than the performance data shown.

**All unused funds are returned to the member.

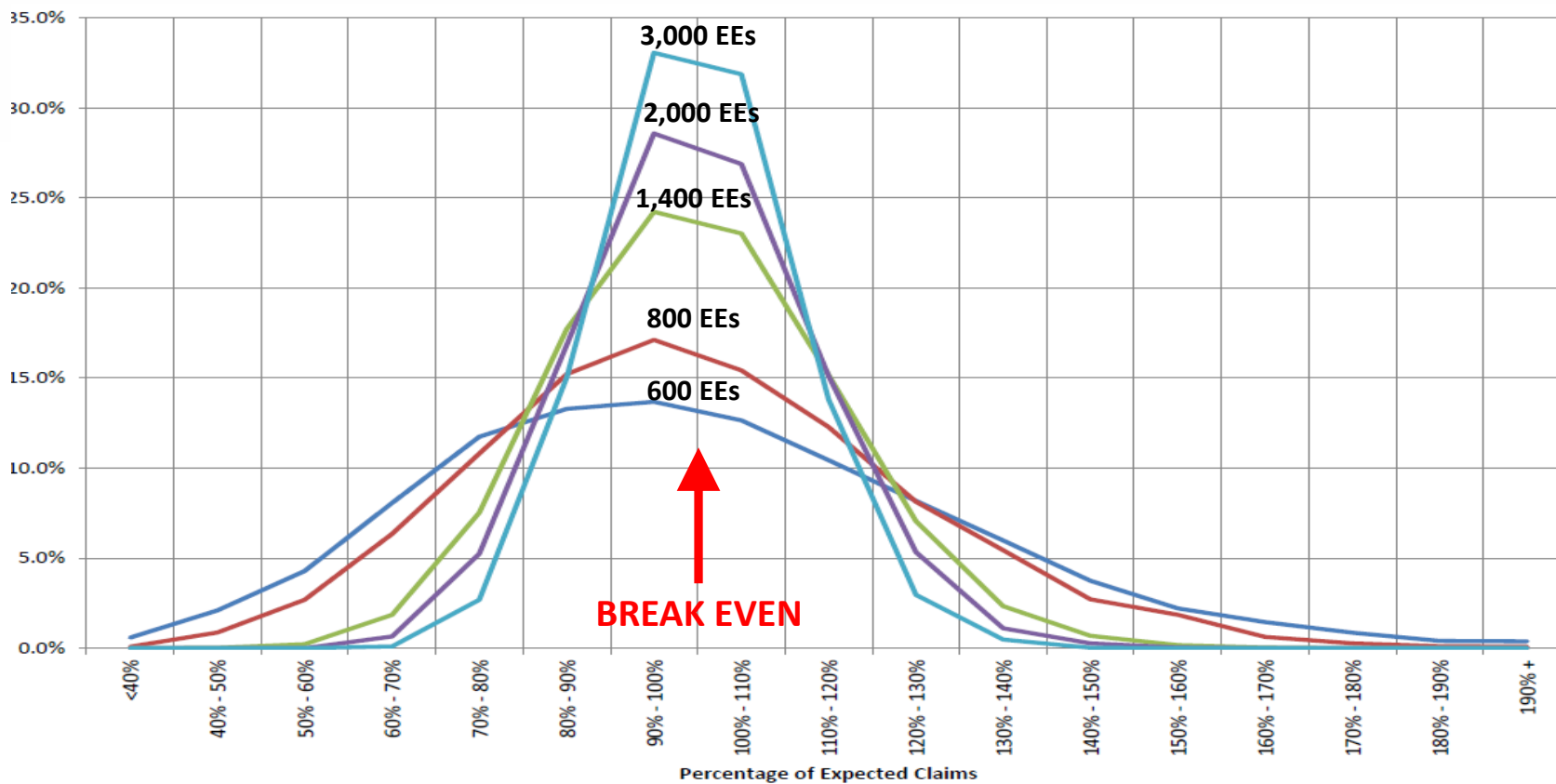
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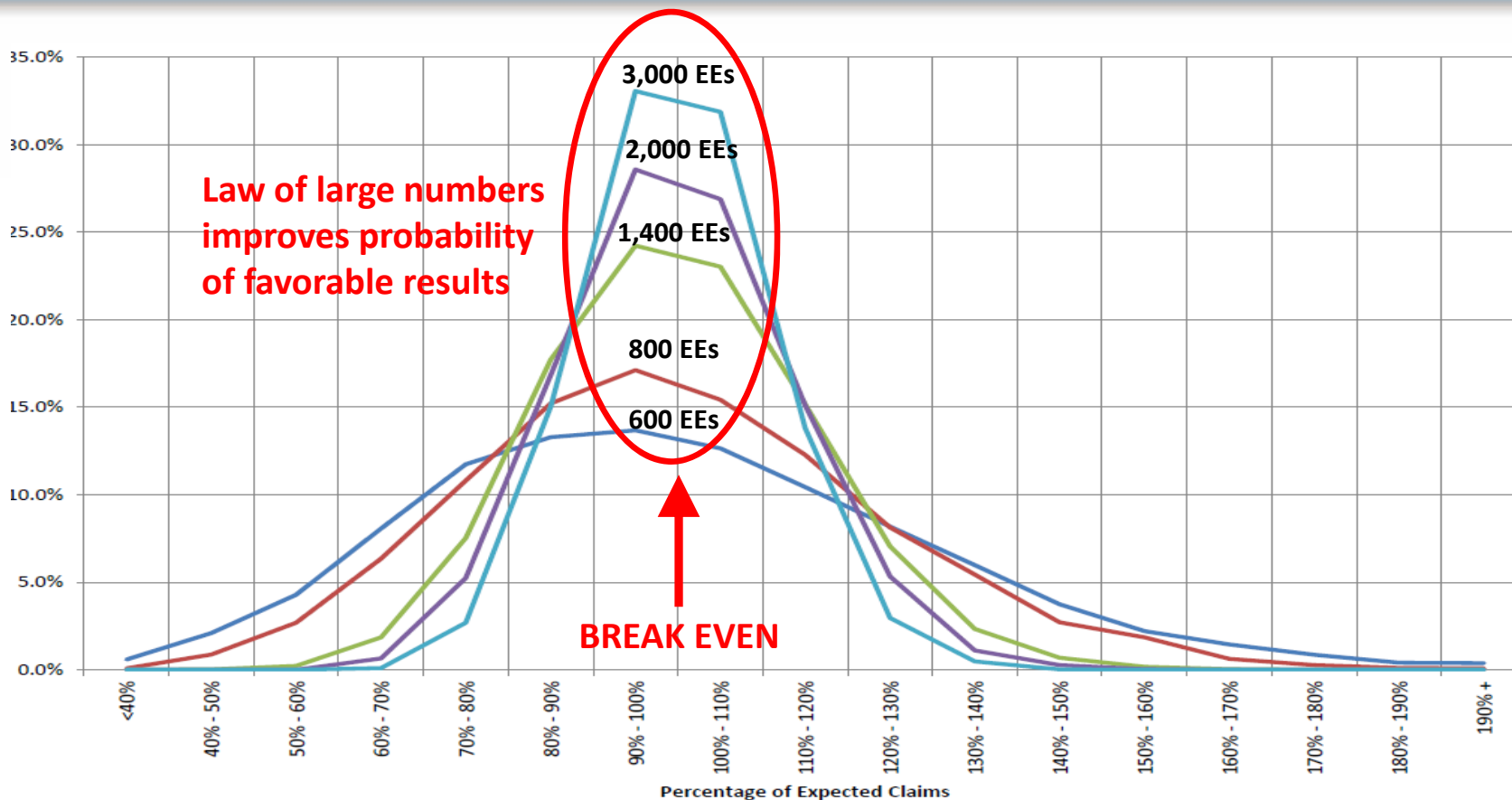
Considerations and Potentials

- Economies of scale = Improves probability of results
- Decrease variability + Increase predictability
- Positive results help offset future years
- Captive layer and risk tolerance

Captive Results: Simulated Probability



Captive Results: Simulated Probability



Considerations and Potentials

- Cumulative effect of retention = Long Term Plan
 - Retain positive variability
 - Spread negative variability
- Increased risk tolerance with experience/data
- Surplus potential also = Collateral carryover
- “Pay yourself” leveraged trend

Considerations and Potentials

- Leveraged pricing:
 - Health risk management services
 - TPA fees
- Plan design flexibility
- Vacuum-sealed ROI
- Collaboration: Best practices and pilot programs

Group Captive: What the Industry is Saying



“a captive can typically help to save between 5% and 30%...”



“exponential growth in the next several years...”



“a viable way for employers to financial their employee health benefits...”



“the fast-growing captive insurance market niche...”



“such arrangements typically are cheaper than traditional insurance and reinsurance...”

Our Experience: What Members are Saying

*" . . . **most significant advancement** regarding true cost containment we've seen in years."*

- President, current Captive Member

*" . . . **far more control** of our health insurance costs than can be done in the fully insured market."*

- President, current Captive member

*" . . . access to a **larger risk pool** while retaining the chance to benefit from good loss experience."*

- Risk Manager, current Captive member

*" . . . able to **control pricing volatility** that we would have faced in a traditional stop loss environment."*

- CFO, current Captive member

*" . . . **support from...other members of the captive to lean on.**"*

- CFO, current Captive member

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Next Steps?

- Set up a consultation with your broker to discuss:
 1. Pros and cons
 2. Which captive program is right for you
 3. Determine effective date and implementation
 4. Get a group captive proposal
- **Is Captive right for your company?**



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Questions?