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Know the specifics of your health and welfare stop-loss policy

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Many health and welfare trusts elect to provide medical and prescription drug coverage on a self-insured basis. In other words, the trust retains the risk of unfavorable claims experience.

However, many trusts that do provide medical and prescription drug benefits on a self-insured basis do not have sufficient assets to absorb the impact of unexpected large claims. As a result, self-insured trusts often protect themselves against the impact of large claims by contracting with a stop-loss carrier.

As fiduciaries to health and welfare trusts, trustees must understand the details regarding their stop-loss carrier contracts in order to ensure the trust is receiving the most competitive price while also receiving sufficient protection against large claims in order to maintain sufficient trust assets.

Types of coverage

There are two primary types of stop-loss coverage available: specific coverage and aggregate coverage. Specific stop-loss coverage protects a plan sponsor from large claims for individual participants during a policy period, while aggregate stop-loss coverage protects a plan sponsor from overall total plan claims during a policy period.

This article focuses primarily on specific stop-loss policies, as that is the most common type of policy used by multiemployer plan sponsors. However, some states require a plan sponsor that has a specific stop-loss policy to also have an aggregate stop-loss policy.

Who is covered?

Generally, a stop-loss policy covers claims for a plan sponsor that provides self-insured medical and prescription drug benefits to its participants.

A plan will typically provide a stop-loss policy for all of its active and pre-Medicare members and their dependents.

Many plan sponsors elect to exclude coverage for Medicare-eligible participants under a stop-loss policy, as the plan sponsor pays benefits secondary to Medicare, and therefore retains less risk (i.e., it is unlikely for a plan sponsor to see a large claim for a participant for whom Medicare pays first).

Occasionally, a stop-loss policy will either exclude or require a higher specific deductible for certain participants for whom it is known large claims will occur, which is referred to as "lasering." We discuss lasering later in this article.

What benefits are covered?

Dependent upon the contractual terms between a stop-loss carrier and a plan sponsor, covered benefits may include medical claims, prescription drug claims, or both. Given the rise of specialty drugs in recent years, it is generally a prudent decision to combine medical and prescription drug coverage in a stop-loss policy.

Specific stop-loss contract basis

While stop-loss policies are typically underwritten for a 12-month period, the incurred and paid date criteria in the stop-loss contract determines whether claims are eligible for reimbursement and for which policy year a claim is reimbursed.

There are several different stop-loss contract basis options available. The general format of the contract basis is (incurred claim months / paid claim months). Below are some examples.

- **(12/12):** Covers claims that are both incurred and paid in the 12-month policy period.
- **(12/15):** Covers claims that are both incurred and paid in the 12-month policy period, as well as claims that are *incurred* in the 12-month policy period and paid within the three months following the end of the policy period (e.g., incurred January 2019 to December 2019, paid by March 2020). This is often referred to as a "run-out" policy.

- **(15/12):** Covers claims that are both incurred and paid in the 12-month policy period, as well as claims that are *paid* in the 12-month policy period and incurred within the three months preceding the beginning of the policy period (e.g., incurred October 2018 to December 2019, paid January 2019 to December 2019). This is often referred to as a "run-in" policy.
- **Paid:** Covers claims that are paid during the 12-month policy period, regardless of when claims are incurred. This is the most comprehensive contract basis available, and is therefore the most expensive.

Specific stop-loss deductible

Specific stop-loss policies reimburse the plan sponsor when eligible claims for an individual exceed a deductible amount defined in the contract, also often referred to as the individual attachment point. The contractually defined deductible applies separately to each individual covered under the policy and resets upon entering a new policy period.

For example, if a specific stop-loss policy has a deductible of $300,000 and a covered individual has $500,000 of eligible claims during the policy period, the stop-loss carrier would reimburse the plan sponsor $200,000, or the amount of eligible claims in excess of the deductible. If a second individual has $400,000 of eligible claims during the policy period, the stop-loss carrier would reimburse the plan sponsor an additional $100,000. There is no limit to the number of individuals for whom a plan sponsor can receive reimbursement in a given policy period.

Stop-loss carriers are able to offer a large range of deductible options from which to choose. The lower the deductibles, the higher the premiums will be, and vice versa. Generally, a plan with a larger population or a more predictable claims pattern should choose a higher deductible with lower premiums, because it can afford to retain more risk. Conversely, a plan with a smaller population or a less predictable claims pattern should opt for paying higher monthly premiums in exchange for the security of a lower deductible.

Aggregating specific stop-loss deductible

In addition to a specific deductible, a stop-loss carrier may also offer the option of an aggregating specific deductible to plan sponsors. An aggregating specific deductible is an additional (aggregate) deductible that the plan sponsor must satisfy prior to receiving claims reimbursements from the carrier.

The chart in Figure 1 contains two different examples of a stop-loss policy that combines a specific deductible of $300,000 with an aggregating specific deductible of $200,000.

The purpose of an aggregating specific deductible is to lower premiums paid to the stop-loss carrier in exchange for the plan sponsor potentially paying a bit more in claims throughout the policy period. Additionally, an aggregating specific deductible paired with a slightly lower specific deductible can help to mitigate the risk of an unusually large number of claims that are just below the original higher specific deductible. While including an aggregating specific deductible can be favorable for plan sponsors, stop-loss carriers will not always offer this as an option.

Lasers and conditional lasers

The purpose of a stop-loss policy is to protect a plan sponsor from unpredictable catastrophic claims that exceed predetermined amounts. However, stop-loss carriers require disclosure of information for review prior to entering a contract period (policies are generally rated based on a historical period of three to five years), in addition to

FIGURE 1: EXAMPLES OF AGGREGATING SPECIFIC STOP-LOSS DEDUCTIBLES

		STOP-LOSS POLICY A	STOP-LOSS POLICY B
(1)	Specific Deductible	$300,000	$300,000
(2)	Aggregating Specific Deductible	$200,000	$200,000
(3)	Claims for Individual X	$500,000	$400,000
(4) = (3) – (1)	Claims for Individual X After Specific Deductible	$200,000	$100,000
(5) = MAX[(4) – (2) , 0]	Claims for Individual X After Specific Deductible **AND** Aggregating Specific Deductible	$0	$0
(6) = MAX[(2) – [(3) – (1)] , 0]	Remaining Aggregating Specific Deductible (after Individual X's claims)	$0	$100,000
(7)	Claims for Individual Y	$450,000	$450,000
(8) = (7) – (1)	Claims for Individual Y After Specific Deductible	$150,000	$150,000
(9)* = MAX[(8) – (6) , 0]	Claims for Individual Y After Specific Deductible **AND** Remaining Aggregating Specific Deductible	$150,000	$50,000

* This is the amount that the plan sponsor would be reimbursed for Individual Y's claims. In addition, any subsequent claims by Individual X, Individual Y, or any other covered individual with claims greater than the specific deductible ($300,000 in both examples) would also be reimbursed if they occurred during the policy period.

any information regarding known future large claims. For participants with an existing condition that will result in a high likelihood of large claims in an upcoming policy period, the stop-loss carrier will impose a higher deductible, or laser, for those participants.

Using the same example from Figure 1, suppose that a specific stop-loss policy has a deductible of $300,000 during the 2019 policy period. Upon review of required disclosure information, the stop-loss carrier determined that Individual X will need a kidney transplant in 2019. As a result, the stop-loss carrier imposes a laser on the participant with a deductible of $500,000, meaning that claims will only be reimbursed for this individual if they exceed $500,000, rather than $300,000, during the policy period.

Furthermore, the stop-loss carrier determined that Individual Y might need spinal surgery. As a result, the stop-loss carrier imposes a conditional laser on the participant, with a deductible of $600,000, conditional on the participant receiving spinal surgery during the contract period. If the participant does not receive spinal surgery, they would be subject to the lower ($300,000) deductible.

Stop-loss carriers are also often willing to enter a contract period without imposing any lasers or offering a "no laser on renewal" policy, which is a contractual agreement that prohibits the stop-loss carrier from adding a new laser at renewal; however, doing so comes at an increased premium rate, because the "known" reimbursements will just be included in the premiums.

Leveraged trend

Leveraged trend occurs when specific stop-loss policies renew, but the deductible either does not change or increases at a percentage that is less than the corresponding assumed medical and/or prescription drug trend. Generally, a higher specific deductible results in a higher leveraged trend.

Using the same example as in Figure 1, suppose that a specific stop-loss policy has a deductible of $300,000 during the 2019 policy period. If a covered individual has $500,000 of eligible claims during the policy period, the stop-loss carrier would reimburse the plan sponsor $200,000.

Fast forward to the 2020 policy period. Under an assumed trend rate of 7.0%, the $500,000 in claims from 2019 now becomes $535,000 in 2020. Under the same $300,000 deductible, the stop-loss reimbursement to the plan sponsor would increase from $200,000 to $235,000, or 17.5%, rather than the claims trend of 7.0%.

Due to this leveraged trend, stop-loss policy renewal rate increases tend to be larger than medical and/or prescription drug trend increases, unless the specific deductible increases annually by the same percentage as the claims trend.

Changing stop-loss providers

Plan sponsors should "shop" their stop-loss policies every few years to ensure they are receiving the most competitive premiums and contract terms. In the event that trustees make the decision to change carriers, it is important to ensure there is no lapse in coverage during the change, so the plan is not on the hook for large claims that would have normally been reimbursed by the incumbent stop-loss carrier.

Summary

Stop-loss policies can be a useful tool for plan sponsors to transfer the risk of large claims. Trustees should speak with their consultants and other plan professionals to assess whether stop-loss coverage is appropriate, and if so, the optimal contractual terms.

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