Insured vs. Self-Insured Plans

Commercial and Self-Insured Plans: What's the Difference?

There are several ways employers can provide health coverage to their workers. Some employers buy an "off the shelf" health benefit package from an insurance company. But others may choose to self-fund healthcare coverage on their own. But, what difference does it make? And, why does it matter?

Commercially Insured Plans

What is a commercially insured plan?

In a commercially insured plan, your employer pays a premium to an insurance company or HMO – usually monthly – for a certain package of health benefits. As an employee, you will usually pay a share of the premium, too. Then, the insurer takes care of all the administrative work. They pay for your doctors' visits, medications and other care, process your claims, and issue the ID cards you use at the doctor's office or pharmacy.

How do they set costs?

Premiums usually change each year. To decide how much to charge for premiums, insurance companies generally look at how much they expect to pay for their members' care over the year, and how much it will cost them to run the plan. They may also add on charges to generate profits or cover taxes.

The amount that you and your employer pay for your premiums is fixed for that year. It stays the same, no matter how much care you and the other members of your plan receive. If the cost of care ends up higher than the insurance company expected, the insurance company must cover the cost.

What rules do they need to follow?

Commercially insured plans are mostly regulated at the state level. Each state has its own rules that insurance companies need to follow, like limits on cost-sharing, your right to appeal if a claim is denied, and basic health services that plans must provide. Plans must also follow certain federal laws, like the recent Patient Protection and Affordable Care Act, also known as the health reform law.

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Self-Insured Plans

What is a self-insured plan?

If you are in a self-insured plan, your employer pays for all your care directly instead of paying an insurance company to handle it. If the cost of care ends up higher than your employer predicted, your employer must cover the cost.

Your employer may hire an outside company – sometimes called a "Third Party Administrator" or TPA – to handle the day to day work, like processing claims or sending out ID cards. The TPA may also run the provider network for your employer. For example, some commercial insurers serve as TPAs for self-insured plans, and rent their own provider networks to employers for a fee. The cost of hiring a TPA and renting a provider network will also figure into your employer's healthcare costs.

Some groups of employers – for instance, some plans that cover union workers – administer the benefits themselves and manage their own provider networks, instead of hiring an outside TPA.

How do they set costs?

Like commercial insurers, employers generally look at how much they expect to pay for their workers' care for the year. They will also factor in how much it will cost them to run the plan – for instance, hiring a Third Party Administrator and renting a provider network. If you are in a self-insured plan, your employer will use that information to determine how much your contribution will be. Your contribution will usually be deducted from your paycheck. The amount you contribute is generally fixed for the year, and will not change no matter how much care you and the other members of your plan use.

What rules do they need to follow?

Self-insured plans are mostly regulated at the federal level. The main law that guides these plans is the Employee Retirement Income Security Act, or ERISA. Most self-insured plans must follow ERISA's rules, like giving members the right to appeal if a claim is denied. The Patient Protection and Affordable Care Act also includes certain requirements for care applicable to self-insured plans.

Pros and Cons

Why Do Employers Self-Insure?

There are a lot of good reasons to self-insure, like:

- More control over plan design: Commercial insurance companies usually offer set packages of benefits. By self-insuring, employers can tailor a plan for their workers that they may not be able to buy "off the shelf."

- Cost savings: Self-insured plans are not commercial products, so they have different types of costs. They don't need to build in extra charges for profits, or taxes.
- Better cash flow: In a self-insured plan, the employer pays the actual cost of care instead of a fixed monthly premium. With a commercially insured plan, the employer pays the same premium even if members use less care one month than predicted. So, in that case, the insurance company would set aside the difference for future months when costs might be higher. But in a self-insured plan, the employer holds on to that extra money.

Why Do Employers Buy Commercial Plans?

There are also good reasons for employers to buy commercially-insured plans, like:

- Costs are fixed: In a commercially insured plan, your employer pays a set premium each month, no matter how many doctor's visits, hospital visits and prescriptions you and the other members of your plan use. In a self-insured plan, your employer's costs might be high one month, and low the next.

- Costs can be higher than anticipated: In a self-insured plan, there will likely be times that more employees need medical care than expected. Or, if an employee gets seriously ill, their treatment costs could run into the hundreds of thousands, or even millions, of dollars. Some employers may not be able to absorb these costs, and buy commercially-insured plans to protect themselves from the risk.

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