Self-Insured Trusts: Buyer Beware

By Adam Friedlander

When it comes to self-insured trusts, the policy should be buyer beware. Forty-one percent of New York group self-insured trusts are "under-funded," according to a recent report by the New York Workers' Compensation Board. This alarming number should be carefully considered by the insurance buying public, their agents and brokers.

Group self-insurers whose liabilities exceed assets are deemed to be under funded, according to the rules and regulations that govern group self-insured trusts. Of the 64 New York trusts listed in the report, 26 are deemed under-funded. Of the 26 that are under-funded, 58 percent have "no new members" restrictions imposed by the Workers' Compensation Board, and 10 have "membership restrictions."

For existing and prospective members, the fact that 41 percent of group self-insured trusts are under-funded has significant financial ramifications. Members of group self-insured trusts are co-owners. In exchange for what appears to be relatively competitive "contributions," members can be assessed if the trust runs short of funds. Members agree to cover any shortfall when they assume, at time of application, joint and several liability. Agreeing to joint and several liability provides the trust with signed "blank checks" to be cashed as necessary, for years to come, to cover any shortfalls in funds to pay claims and other obligations arising during the period of the member's participation.

Members can also be assessed for the insolvency of any other trust in New York, according to New York workers' compensation law. In light of this additional, broad based exposure, buyers should evaluate the suitability of trust membership.

Also of concern to insurance agents and brokers is the insolvency exclusion for self-insured plans in the errors & omissions policy offered by Westport Insurance Company, the carrier for the Insurance Association of Agents and Brokers in New York. Why are small business owners willing to expose their assets to the self-insured trusts' risk of insolvency when an experienced insurance company refuses at any price? Agents and brokers using trusts should review their own exposure.

Self-insured trusts purchase reinsurance in an attempt to protect against high frequency or severity of claims and to avoid triggering joint and several liability. However, the fact that 41 percent of self-insured trusts are under funded is evidence that reinsurance does not provide adequate protection for all of a trust's obligations.

Liabilities can exceed assets without triggering reinsurance for several reasons. Those reasons include underpricing to attract and retain members, high operating costs, a high frequency of claims that fall below the large reinsurance deductibles, premature payment of dividends, and the ever growing New York State assessment liability. The New York State assessment, charged as a percentage of paid indemnity claims, is not covered by reinsurance.

Significant problems have occurred in other states with group self-insured trusts. The most recent example is the Associated Industries of Kentucky (AIK) which insures 70,000 employees. According to the Kentucky office of Insurance, AIK requested the state to approve a plan that allows it to assess its members $59 million to cover shortfalls incurred from January 1, 1999 to December 31, 2003. All employers who were members during those years will be assessed. A total of 3,729 current and prior members will be affected. AIK's self-insured trust went from a small surplus to a $59 million deficit in one year.

In Florida, the number of self-insurance trusts dropped from 60 to four throughout the 1990's as several were declared insolvent. In Illinois, the Environmental Services Workers' Compensation Trust was liquidated in 2001 and found to be insolvent by $3 million. There have been a total of four group self-insured trust insolvencies in Illinois. These are examples where the actual costs of self-insurance far exceeded projected costs.

Workers' compensation has historically proven to be unprofitable for most insurance companies. Workers' compensation is exactly the kind of risk that business owners should transfer to insurance companies, rather than retain. Low upfront pricing is appealing but when employers are forced to assume joint and several liability, which is like signing blank checks, it has proven to be very costly. ▲

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New Yorkers Urged To Act Quickly To Get $1200 Credit Towards Prescription Drugs

NEW YORK, N.Y., November 15 — Older and disabled New Yorkers with low incomes can still get $1,200 credit toward their prescription drugs, if they apply for a Medicare-approved drug discount card by December 31, advised the Medicare Rights Center (MRC).

New Yorkers who are age 65+ with incomes below $12,569 ($16,862 for a couple) can enroll in New York State's Elderly Pharmaceutical Insurance Coverage (EPIC) program to automatically get a $600 Medicare subsidy this year and another $600 in 2005, MRC said. Once the credit, known as "transitional assistance" (TA), is exhausted, "significant savings on prescription drugs will be available through the state's EPIC program," according to MRC. Any portion of the $600 Medicare credit that is not used by year's end can be used in 2005. Anyone who is approved for the $600 benefit this year will automatically get another $600 credit in 2005. People who receive TA are responsible for paying five or 10 percent of the cost of covered drugs, depending on their income.

Anyone who has drug coverage from a current or former employer, Medicaid, the Federal Employee Health Benefits Program, or Tricare is not eligible for the credit. For more information, visit www.medicare.gov. ▲