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TO: Representative John Nygren, Assembly Chair
Senator Alberta Darling, Senate Chair
Joint Committee on Finance

FROM: Bob Lang, Director

SUBJECT: State Employee Health Program Reserves, Premium Increases, and Estimated Savings

At the request of a number of members of the Joint Committee on Finance, this memorandum provides information relating to issues recently raised by the administration and the Group Insurance Board (GIB) relating to the state employee health program, including program reserves. Specifically, the following information is provided: (a) the amounts of reserves associated with state health plans for the past five calendar years; (b) estimated program reserves in those years that would correspond to the GIB reserve policy; (c) the amount of reserves available to reduce health plan costs in the 2017-19 biennium; (d) a history of health insurance premium increases; and (e) state employer savings estimated by Segal and the GIB associated with self-insuring for group health plans.

Health Program Reserves. The Group Insurance Board approved a program reserves policy in August, 2011, recommended by the state's health program actuary at the time, Deloitte Consulting, to maintain a fund balance that equals 15% to 25% of the sum of: (a) 100% of annual self-funded medical claims; and (b) 20% of annual fully-insured medical claims. The policy has not been modified since its adoption in 2011. Table 1 provides the actual amounts of year-end reserves (2016 figures are unaudited) for the past five calendar years and the estimated amount of year-end reserves that would correspond to the Board's reserve policy based on actual or estimated medical claims expenses for the same years. As shown in the table, as of the end of calendar year 2016, program reserves were $18.4 million greater than the maximum 25% medical claims benchmark and $68.8 million more than the minimum 15% medical claims benchmark.

TABLE 1

Health Program Reserves for State Employees and State Retirees, Calendar Years 2012 to 2016 ($ in Millions)

	Calendar Year				
	2012	2013	2014	2015	2016
Claims Benchmark*	$430.8	$449.0	$481.6	$502.2	$504.0
Year-End Reserves	140.8	129.8	100.1	81.5	144.4
Reserves as % of Claims	32.7%	28.9%	20.8%	16.2%	28.6%

	Amount	Difference
2016 Reserves	$144.4	N/A
25% of Claims	126.0	$18.4
15% of Claims	75.6	68.8

*Benchmark established in August, 2011, was 100% of actual self-insured claims and 20% of estimated fully insured claims.

Planned Reserves for Self-Insurance. The state's consulting actuary for health programs, Segal, recommended that the GIB not utilize program reserves to reduce state health program costs in calendar year 2016 and calendar year 2017. In developing 2016 state rates, Segal projected that program reserves at the end of calendar year 2015 would be approximately 18%, which would be closer to the minimum reserve policy of 15%. Table 1 shows that actual year-end program reserves for the state in 2015 were approximately 16%. On August 16, 2016, Segal again recommended to the GIB that program reserves not be used to reduce state health program costs for calendar year 2017. However, in contrast to the prior year, Segal projected that year-end state health program reserves in 2016 would be "approximately 29% of claims and outside of the 15-25% corridor." In its August, 2016, presentation Segal further noted that:

> Given this is a year of good experience for the overall program, particularly with the low renewals on the medical side, we recommend not implementing a buy-down this year and maintaining the cash for future years. With the potential move to self-insurance in 2018, this will also provide a solid starting reserve.

Reserves in Budgetary Terms. Table 2 below shows the share of premium contributions paid in calendar year 2016 relative to the program as a whole by state employers, state employees, state retirees, and local participants (local employers, employees, and retirees). State employer contributions constitute approximately 81.8% of total program costs and approximately 83.2% of state program costs.

TABLE 2

Share of Premium Contributions by Program Group for Pre-Medicare Participants, Calendar Year 2016

	Premiums Paid ($ in Millions)	Contribution Percentage	Share of State Program Only
State Employer	$956.9	81.8%	83.2%
State Employee	126.0	10.8	11.0
State Retiree	67.4	5.8	5.9
Local Programs	19.3	1.6	
Total	$1,169.5	100.0%	100.0%

Table 3 below shows the proportions budgeted in the bill for state employer compensation costs, including health insurance, that are funded from GPR and from other fund sources (FED, PR, and SEG). As shown in the table, 45.1% of state employer compensation expenses are allocated to GPR funding. As a result, 37.5% of program reserves for the state (45.1% of 83.2%) would correspond to budgeted GPR expenses for compensation reserves for most state employees as well as compensation expenses of the University of Wisconsin (UW) System. The amounts shown in Table 1 in excess of 25% and 15% would correspond to approximately $6.9 million GPR (25% policy) and $25.8 million GPR (15% policy). If used over a two-year period, reductions of $2.3 million GPR in 2017-18 and $4.6 million GPR in 2018-19 could be applied if reserves were drawn down to 25%, while $8.6 million GPR in 2017-18 and $17.2 million GPR in 2018-19 could be applied if reserves were drawn down to 15%.

TABLE 3

2017-19 Budget Allocation of State Employer Compensation Expenses by Fund Source

Fund Source	Allocation
GPR	45.1%
Other Funds	54.9
All Funds	100.0%

Health Insurance Premium History. In a November, 2016, memorandum from Employee Trust Funds (ETF) staff to the GIB, a summary of nine years of health insurance premium increases was presented. Over the nine-year period, health insurance premiums increased by 3.7% annually on average. The information presented by ETF is provided in Table 4 below. The memorandum additionally noted that "reductions in 2012 and 2016 were greatly influenced by state budget-required benefit changes that shifted additional costs to program members." If

calendar years 2012 and 2016 are excluded from the nine-year average, the remaining seven years on average experienced a 5.3% annual premium increase.

TABLE 4

Preliminary Premium Bids and Final Increases, 2009 to 2017

Calendar Year	Final Premium Increase	Preliminary Bid	Negotiation "Savings" (in Millions)
2009	8.1%	10.0%	$13.50
2010	7.7	10.0	18.80
2011	6.3	9.5	28.00
2012	-1.5	2.1	30.10
2013	5.1	8.7	33.10
2014	3.5	8.2	45.50
2015	5.0	6.9	19.30
2016	-2.5	7.7	56.40
2017	1.6	5.4	37.90
Average	3.7	7.6	--

Segal Projection for 2018. On May 24, 2017, Segal made a presentation to the GIB relating to addendum information submitted by the health plans that currently participate in the program. Segal indicated that the insurers are required to submit reports on "a wide array of information -- membership, claims, admin, trends, high dollar claimants, premiums, revenues, rate build-up, etc." Based on the information that was submitted on May 15, 2017, Segal made assumptions relating to medical cost increases and administrative expenses to produce estimated premium increases for 2018, with a projected preliminary bid of 14.0% and an overall target for the state to negotiate increases to 10.4%. In projecting an estimate, Segal indicated that: (a) actual medical claims decreased in 2016 relative to previous estimates; and (b) health plans participating in the program are currently operating at a very efficient level of only 4% administrative expenses including profit (96% medical loss ratio estimated in 2017 associated with medical expenses). Segal reasons that a decrease in medical expenses and efficient administration by insurers will result in higher costs when the health plans submit preliminary bids. However, Segal's projections are well outside the range of preliminary and final bids for the past nine years, shown in Table 4 above.

It should be noted that the information submitted by health plans on May 15, 2017, did not include preliminary bids, which are not yet due. The annual negotiation process requires that health plans submit a preliminary bid, which is used to compare between plans in establishing an initial pricing tier. The initial tier and premium bid may then be modified based on an insurer's willingness to lower the bid through the negotiation process. Preliminary bids are expected to be submitted in June, 2017.

Self-Insurance Savings Estimates. In a press conference held May 26, 2017, the Secretary of the Department of Administration (DOA), Director of the State Budget Office, and a member of the GIB representing the Office of the Commissioner of Insurance presented several figures

estimating state employer savings over the 2017-19 biennium associated with self-insuring for group health plans: (a) $60 million associated with self-insurance savings from reduced administrative and claims expenses; (b) $22 million associated with the federal Affordable Care Act health insurer fee; and (c) $21 million associated with the cost to budget for a 10.4% health insurance premium increase in 2018, which would be above the 7% annual increase the administration included in the Governor's recommended budget. In total, the three figures estimated by DOA and the GIB sum to $103 million GPR. Based on amounts budgeted in the bill, the administration indicated that $60 million GPR associated with lower administrative and claims expenses would correspond to state employer savings of $134.4 million on an all-funds basis. [The total differs from $133 million due to rounding and the allocation of compensation funding between the UW System and other state agencies.] Further, it was indicated that the savings are a minimum guarantee of savings that would be realized, based on bids by the vendors the state would contract with to administer a self-insured program.

Segal estimated self-insurance savings based on a range of assumptions relating to: (a) annual medical trend; (b) medical loss ratio indicating administrative expenses including profit; and (c) medical CPI (consumer price index, a measure of inflation in costs). As indicated in their presentation to the GIB on May 24, 2017, the numbers upon which the biennial budget were based "were focused on the midpoint scenario and deemed 'most likely.'" The actual medical trend, medical loss ratio, and medical CPI cannot be predicted with certainty and are, therefore, still not known at this time. The midpoint savings estimate Segal produced was $85.2 million per calendar year, while its lower bound estimate of savings was $53.8 million per calendar year. [As a point of reference, the upper bound savings estimate was $116.1 million per calendar year.] It is important to note that these savings estimates, and an estimate of the Affordable Care Act health insurer fee totaling $32.5 million per calendar year, are associated with the total cost for the pre-Medicare population of all groups that participate in a group health insurance program offered by the GIB. In other words, the savings estimates include not only state employer contributions, but also premiums paid by local governments and local employees, local retirees, state retirees, and state employee contributions.

Segal also noted in its May 24, 2017, presentation that estimates of GPR savings that were used in developing the biennial budget were based on an assumption that 50% of midpoint savings of $85.2 million per calendar year, or $127.8 over the biennium, would be GPR savings ($42.6 million per calendar year, rounded down to $40 million for an estimated $60 million GPR over the biennium). A similar calculation method was utilized in determining GPR savings associated with the Affordable Care Act health insurer fee (utilizing 45.1% rather than 50%). This assumption was applied to estimated savings for not only state employer contributions, but also local active and retiree contributions, state retiree contributions, and state employee contributions. However, as shown in Table 2 above, state employer contributions constitute approximately 81.8% of total premiums paid by all groups, including employees. In addition, as shown in Table 3, the percentage used by the administration to budget for state employer compensation and health insurance costs is 45.1%. As a result, the proportion of GPR savings that would correspond to the group health program as a whole would be 36.9% rather than 50% or 45.1%.

A reestimate of state employer savings based on low and midpoint projections by Segal would correspond to: (a) $29.7 million GPR over the biennium ($19.8 million GPR on a calendar year basis); and (b) $47.1 million GPR over the biennium ($31.4 million GPR on a calendar year basis). As a result, "minimum" savings estimated by Segal would equal $29.7 million GPR over the biennium rather than $60 million GPR. This figure would not, however, be an absolute minimum given that the assumptions upon which Segal based its estimates could differ from actual market prices, administrative expenses, and use of medical care by covered members. Exhibit B of each self-insurance contract, which relates to discount guarantees, sets a 2018 "discount target" that is calculated by vendors based upon enrollment and regional assumptions. The contracts indicate that "Upon open enrollment, these will be re-based accordingly." The contracts also indicate that actual performance relative to discount targets would be calculated six months after the end of the calendar year. The consequence to a vendor of not meeting its discount target would be to reduce up to 10% of the vendor's total administrative fees. Discount targets and administrative fees for each vendor are not known at this time, as they were redacted from the contracts that have been submitted for review by the Joint Committee on Finance.

Finally, because the Affordable Care Act (ACA) fee was calculated in a similar manner using an allocation of 45.1% rather than 36.9%, a reestimate of GPR savings associated with the fee would be equal to $12 million GPR per calendar year (36.9% of $32.5 million per calendar year), or $18 million GPR over the biennium, rather than $22 million GPR over the biennium as estimated in the bill. Table 5 summarizes reestimated self-insurance and ACA fee savings using Segal projections and the administration's method for allocating compensation expenses to GPR and other fund sources.

TABLE 5

Reestimated 2017-19 Self-Insurance and ACA Savings Using Segal Estimates and DOA Budgeting Practices ($ in Millions)

		State Employer GPR							
	Total		Bill Estimate				Reestimate		
Type of Expense	Program per Calendar Year	Percentage Applied	2017-18 (Six Mos.)	2018-19 (12 Mos.)	Biennium (18 Mos.)	Percentage Applied	2017-18 (Six Mos.)	2018-19 (12 Mos.)	Biennium (18 Mos.)
Claims and Administration									
High	$116.1		N/A	N/A	N/A	36.9%	$21.4	$42.8	$64.2
Midpoint*	85.2	50.0%*	$20.0	$40.0	$60.0	36.9	15.7	31.4	47.1
Low	53.8		N/A	N/A	N/A	36.9	9.9	19.8	29.7
Affordable Care Act Fee	$32.5	45.1%	$7.3	$14.7	$22.0	36.9%	$6.0	$12.0	$18.0

*Under AB 64/SB 30, 50% of $85.2 million ($42.6 million) was rounded down to $40 million per calendar year, or $60 million for the 2017-19 biennium.

cc: Members, Joint Committee on Finance