Legislative Fiscal Bureau

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State Contributions to State Employee Health Care Coverage Plans (ETF -- Departmentwide)

[LFB 2003-05 Budget Summary: Page 153, #10]

CURRENT LAW

Under current law, the state contributes an amount equal to 90% of the monthly premium cost of the Standard Plan or 105% of the premium cost of the lowest cost alternative health care plan (but not more than the total amount of the remaining premium), whichever contribution amount is less. The basis for establishing the amount of the state's contribution for alternative plan coverage is determined by the county in which the employee receives medical care. The basis for establishing the amount of the state's contribution for Standard Plan coverage is determined by the employee's county of residence.

GOVERNOR

Require the Group Insurance Board to place each of the state's health care coverage plans into one of three tiers established in accordance with standards adopted by the Board. Require that the tiers be separated according to the employee's share of premium costs. Require the state to pay premium costs for eligible employees, regardless of the plan selected by the employee, not less than 80% of the average premium cost of plans offered in the tier with the lowest employee premium cost. Repeal the current 90%/105% contribution structure. This modified state payment requirement would not affect payments required under current collective bargaining agreements for represented state employees and under the current state compensation plan for nonrepresented state employees.

Provide that the current prohibition barring the Group Insurance Board from modifying or expanding group insurance coverage in a manner which conflicts with public employee trust fund law or ETF rules, or materially affects the premium level paid by the state or its employees,

or the level of benefits under any group insurance coverage, would not be deemed to prohibit the Board from modifying the Standard Plan to establish a more cost effective benefit plan design.

Stipulate that these provisions would first apply to premiums paid by state employees for health care coverage for the period that begins on January 1, 2004.

DISCUSSION POINTS

1. The Governor's recommendation reflects proposals developed by a study group of the Group Insurance Board to devise alternative state group health insurance premium contribution structures. The study group recommended converting the current premium contribution structure to one based on a tiered approach. On November 19, 2002, the Board approved the study group recommendations in concept and asked ETF to identify the steps necessary for implementation.

2. The study group recommendations included the following elements: (a) changing the basis of the current health insurance premium contribution structure to a three-tier scaled approach; (b) removing the prescription drug benefit from the uniform benefits package and contracting with a pharmacy benefit manager (PBM) for all drug benefits under the program; (c) conversion of the Standard Plan and Standard Plan II plans into one Preferred Provider Plan; (d) integration of certain quality and safety standards into the program requirements for all state health plans; and (e) exclusion of optional dental benefits from the participating plans and the creation of a stand-alone dental plan available to all state employees (when a reasonable employer contribution becomes available).

3. This paper addresses the Governor's recommendations relating to the tiered contribution provisions and the possible conversion of the Standard Plan and Standard Plan II plans into one Preferred Provider Plan.

4. The current employer premium contribution formula has been in effect since 1984. Under current law, state employees become eligible for state group health insurance coverage when they become eligible for participation under the Wisconsin Retirement System (WRS). While most new state employees are eligible for state group health insurance coverage immediately, they generally do not become eligible for state contributions towards health insurance premiums until after six months of service under the WRS. (Major exceptions to this rule are state elected officials and University faculty and academic staff, who become eligible for the state's contribution upon employment.)

5. When the state begins to make contributions towards the costs of an employee's health insurance premiums, it contributes an amount equal to 90% of the premium cost of the Standard Plan or 105% of the premium cost of the lowest cost alternative health care plan (but not more than the total amount of the premium), whichever contribution amount is less, based on the county where the employee receives the medical care.

6. This premium contribution formula provides an incentive to state employees to

select coverage from among the available lower cost alternative plans in order to minimize their out-of-pocket premium contributions. In counties where there is a qualified alternative health care plan, there will always be a no-cost group health insurance coverage option available to state employees, with the state paying the full amount of the premium contribution. Under current law, the state's share of premium payments in 2003 is projected to be 97.5% of total premium costs.

7. Because current law requires that group health insurance agreements continue from year-to-year with their basic benefits structures largely unchanged (except possibly to add additional new mandated benefits), the operation of the state premium contribution formula in an environment of escalating medical insurance costs has had a major impact on total state health insurance expenditures. The following table shows state and state employee estimated total health insurance premium contributions payments for the last five calendar years. The amounts are based on the premium payment levels, the source of the premium payment, and the total number of group health insurance coverage contracts in effect for each January of the calendar year indicated:

Estimated Annual State and State Employee Health Insurance Premium Payments (All Funds)

Calendar Year	Employee-Paid Contributions	State-Paid Contributions
1999	$13,248,500	$306,678,800
2000	13,352,500	349,905,200
2001	10,582,500	423,910,200
2002	11,978,300	500,851,100
2003	14,515,700	576,137,400

8. ETF officials indicate that, while the current contribution formula has been effective at fostering a competitive environment that is essential to the program, the formula has created some problems that would be better addressed with a new approach.

9. The current formula has created an opportunity for plans providers to “shadow price.” As the current formula operates, being the lowest cost plan does not provide a competitive advantage over any other plan that is within 5% of the lowest premium rate. This is because the state will still pay the full premium costs for the employee up to 5% above the premium costs for the lowest cost plan. Further, the lowest premium may be more a function of the plan having a better risk pool than of a more efficient system of health care delivery. The current formula also creates inequities between employees in different counties when the employer contribution amount is calculated on a county-by-county basis. Finally, agency staff indicate that the formula has likely led, at least in part, to making the Standard Plan unaffordable for many, as employee out-of-pocket premium costs have increased sharply due to adverse selection to the plan.

10. The rationale for the three-tier proposal is that it will address these issues and

provide a framework for encouraging health plans to become more cost-effective and encouraging state employees to choose the most efficient health plans.

11. Under the proposal, the current state health plan providers would be placed in one of three tiers. Tier one plans would include those evaluated by ETF and its consulting actuary to be the most cost-effective. Employees choosing these plans would be required to contribute a lower monthly premium contribution than employees who choose plans placed in the other two tiers. Tier two plans would be those evaluated to be less cost-effective than those in tier one but more cost-effective than those in the third tier. Tier three plans would those plans deemed the least cost effective plans based on staff and actuarial reviews. Required employee contributions would increase for tier two plans and would be at the highest level for tier three plans.

12. Plans would be placed in a tier on the basis the risk-adjusted per-member-per-month (PMPM) cost of each plan. The risk adjustment factor relates to the degree to which a plan has a high-risk makeup to its risk pool and the manner in which this is addressed by each plan. In this way, plans would not be penalized for having a higher risk population as long as they manage care for that risk appropriately. Conversely, a plan would not be unduly rewarded merely for having a better risk profile, especially if they fail to manage that risk profile appropriately.

13. According to ETF officials, the PMPM adjusted cost method measures the relative efficiency with which a plan is able to provide care and encourages plans to be more efficient, and not just less expensive. By establishing the lowest state employee contribution level for tier one plans and by placing the most efficient or cost effective plans in the first tier, the proposed modifications are intended to provide an incentive for state employees to choose those plans. Presumably plan administrators would want their plans to increase overall efficiency in order to avoid being placed in higher tiers (which would require higher employee contributions).

14. Under the bill, the state would be required to pay premium costs for eligible employees, regardless of the plan selected by the employee, equal to not less than 80% of the average premium cost of plans offered in the tier with the lowest employee premium cost. This proposed language effectively provides for the minimum state contribution, but does not specify any employee contribution levels for the three tiers.

15. While the bill is silent on the process for setting the employee contribution rates, the Department of Employment Relations (DER) made recommendations for these contributions as part of the proposed 2003-05 compensation plan for nonrepresented classified employees and certain unclassified employees.

16. On April 23, 2003, the Secretary of DER recommended that the Joint Committee on Employment Relations approve the following monthly employee contribution rates for group health insurance coverage, contingent of the enactment of the three-tier system:

Recommended Monthly Employee Contribution Rates

	Single Coverage	Family Coverage
Tier 1	$25.00	$62.50
Tier 2	50.00	125.00
Tier 3	100.00	250.00

17. Under this proposal, employees' monthly out-of-pocket premium contributions would not vary between plans in the same tier nor would they vary by county of residence of the employee.

18. The proposal submitted by the Secretary of DER states that no estimate has been developed by the administration with respect to the fiscal implications of implementing the three-tiered contribution structure. The Secretary advises that the fiscal estimate of the program cannot be effectively projected at this time because the new premium structure is also a subject of collective bargaining. The Secretary further states that "while we expect some amount of the anticipated increases in health insurance premiums charged to the State in the 2003-05 biennium will be offset by reduced charges from health plans seeking to move from a higher to lower tier, as well as through employee premium contributions, it is too early to benchmark these amounts with certainty."

19. No potential state group health insurance cost savings have been recognized in the bill. While state savings would certainly accrue (given that state employees would be required to make higher contributions to their health care premiums beginning in 2003-04), any cost savings associated with the provisions are largely unknown at this time.

20. ETF has done some modeling with respect to the potential range of the fiscal impact of the proposed three-tiered premium structure. The Department allocated current plan providers among the three tiers, based on these plans' current cost efficiencies, and then modeled cost projections under a three-tier approach, based on current year enrollment patterns. Based on state employee premium payments that were set at half the level actually recommended by the Secretary of DER, potential annual savings to the state on the order of $25 million (all funds) were indicated.

21. It is important to note, however, that the Department's projections were based on current year plan efficiencies, which the agency believes may well change as providers bid premium levels for the next plan year. It unknown at this time how the plans would be ranked in the three-tier system for the 2004 plan year. It is also unknown the extent to which a contribution rate tiering system will result in significant enrollment shifts between plan providers that could affect the level of cost savings. Further, to the extent that the increment in total health insurance costs for state employees in the next plan year might exceed any savings due to the premium structure change, there might not be any net savings to the state, compared to current base year funding for health insurance costs. Finally, any potential cost savings will depend on the extent to which current collective bargaining agreements are modified to reflect the proposed changes.

22. Nonetheless, the proposed changes should at least mitigate some of the impact of likely health insurance cost increases during the next biennium. Further, it is likely that the new premium structure will provide the Board with tools to encourage the more efficient and const-effective delivery of group health insurance coverage for state employees by plan providers. The proposal would also increase state employee participation in contributing towards health insurance costs. Some have argued that all state employees should contribute a share of health care costs in order to: (a) create greater equity between state workers and private sector employees and (b) require state employees to share in the cost increases for health insurance coverage. These considerations could be advanced as strong arguments to approve the Governor's recommendations.

23. These contribution requirements, if adopted, would affect only nonrepresented classified employees and certain unclassified employees. Represented employees would remain under the health premium contribution provisions specified in current collective bargaining agreements. Current represented state employee collective bargaining agreements generally reference state employer contributions under the current 90%/105% formula. Contract renegotiations would likely affect the degree to which the Governor's recommendations may be implemented and applied to such employees.

24. The provisions under the bill would result in a major change to the contribution formula for health insurance premiums for state workers. Under current law, state employees can generally choose among a variety plans with different employee contribution requirements, but always with the option of at least one plan that does not require an employee contribution towards the premium. This is of particular benefit to state employees who are lower-paid or part-time employees. Setting flat fees for each tier under the proposed system would require lower-paid employees to pay the same amount, and, therefore, a higher proportion of earnings for health insurance coverage that would be the case with more highly compensated state employees.

25. It could also be argued that the modest compensation increases that are likely in the 2003-05 biennium (the proposed compensation plan for nonrepresented employees recommends a 0% wage adjustment for 2003-04 and a 1% wage adjustment for 2004-05), in combination with new employee health coverage contribution requirements, could lead to a net reduction in take-home pay for many state employees. If the proposed compensation plan is approved, the resulting wage adjustment would not match the required health plan premium contribution requirement for most state workers, particularly those with family coverage.

26. The lack of a no-cost (to the employee) health plan alternative, the effect of a flat-fee health premium contribution requirement on lower-paid employees, and the overall effect of imposing an increased health plan contribution requirements on state employees at a time of modest wage adjustments could all be advanced as arguments for deleting the Governor's recommendations relating to the state's contributions to health care coverage.

27. A technical concern may be raised about the implementation schedule for the proposal. The bill would require the Group Insurance Board to place each of the state's health care coverage plans into one of three tiers established in accordance with standards adopted by the Board

in time for implementation in the 2004 plan year. However, at this writing, these standards have not been fully developed or approved by the Board. Further, health care plans are required to submit proposed 2004 rates by August 1, 2003. While ETF officials indicate that these standards will be available for health plans to consider in preparing these proposed rates, it is not clear, at this time, when the standards will be approved by the Board.

28. The bill also stipulates that these provisions would first apply to premiums paid by state employees for health care coverage for the period that begins on January 1, 2004. State agencies pay ETF the health premiums for its employees two months in advance of the month of coverage; therefore, the January, 2004 premiums would be paid by agencies on November 1, 2003. As a result, the new system would need to be fully implemented by October, 2003, in time for the normal annual "dual-choice" open enrollment period.

29. Finally, while collective bargaining negotiations are expected to begin soon, it is unclear when new agreements would be completed.

30. Thus, it could be argued that an initial applicability of January 1, 2004, could prove to be too ambitious for the Board to achieve, given the uncertainty over these various factors. While ETF officials indicate that they are confident they can implement the proposed changes in time for calendar year 2004 coverage, unanticipated problems associated with a significant programmatic change such as this could result in delays.

31. In order to provide additional flexibility to the Board in implementing the Governor's recommendations, the Committee could also provide a nonstatutory mechanism to allow for a one-time, one-year delay in the implementation of the changes to January 1, 2005. Under this alternative, the Group Insurance Board, with the approval of the Joint Committee on Finance, would be authorized to implement the new contribution system on January 1, 2005, instead of January 1, 2004, if the transition to the new contribution system cannot be accomplished by January 1, 2004, because of administrative difficulties. The Board would be required to report to Joint Finance on or before September 15, 2003, recommending any delay if, in the Board's view, the implementation of the changes cannot be made successfully by January 1, 2004. Joint Finance would be required to meet within 14 working days of the submission to approve or disapprove the Board's recommendation. A nonstatutory provision would authorize the temporary continuation of the current 90%/105% contribution formula for the 2004 plan year under such a contingency.

32. Finally, the bill would provide the Board with the authority to modify the Standard Plan to establish a more cost-effective benefit plan design. Under current law, the Group Insurance Board is not allowed to modify or expand group insurance coverage if it materially affects the level of premiums required to be paid by the state or its employees, or the level of benefits.

33. As noted above, the recommendations of the Board's study group included a recommendation relating to the conversion of the Standard Plan and Standard Plan II plans into one Preferred Provider Plan (PPP). Under a PPP, participants may see any provider, but if they see a provider within a recognized network, they receive a higher benefit level. According to ETF, the

change is being sought because adverse selection to the Standard Plans has made the plan too expensive and its operation under current law may not be sustainable. The proposal would appear to grant the Board the necessary tools to establish a workable Standard Plan option for employees who desire such coverage. The Committee may want to approve the proposed modification.

ALTERNATIVES

1. Approve the Governor's recommendation to: (a) require the Group Insurance Board to place each of the state's health care coverage plans into one of three tiers; (b) require that the tiers be separated according to the employee's share of premium costs; (c) require the state to pay premium costs for eligible employees, regardless of the plan selected by the employee, not less than 80% of the average premium cost of plans offered in the tier with the lowest employee premium cost; (d) repeal the current 90%/105% contribution formula structure; (e) authorize the Board to make modifications to the operation of the Standard Plan; and (f) apply the provisions to premiums paid by state employees for health care coverage for the period that begins on January 1, 2004.

2. *In addition to Alternative 1,* provide a nonstatutory provision authorizing the Group Insurance Board, with the approval of the Joint Committee on Finance, to implement the new contribution system on January 1, 2005, instead of January 1, 2004, if the transition to the new contribution system cannot be accomplished by January 1, 2004, because of administrative difficulties. Require the Board to report to the Joint Committee on Finance on or before September 15, 2003, recommending any delay if, in the Board's view, the implementation of the changes cannot be made successfully by January 1, 2004. Require the Joint Committee on Finance to meet within 14 working days of the Board's request to approve or disapprove the Board's recommendation. If a delay is approved, authorize the temporary continuation of the current 90%/105% contribution formula for the 2004 plan year only.

3. Delete the Governor's recommendations.

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