~GSRA~ newsletter

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Pursuant to our goal of keeping you informed, this newsletter issue is dedicated to facts regarding the State Health Benefit Plan. In the article below, Claude Vickers, former state auditor and chairman of the GSRA steering committee, states the background, the recent developments and the current situation.

State Health Benefit Plan Info

Like many of you I have listened to several members of the General Assembly and the Governor when they explain the problems and express their concern with the State Health Benefit Plan (SHBP). After having read articles in the media about the SHBP, I have concluded that a number of writers do not fully understand the situation. This paper is my attempt to explain the facts to you - the members of the *Georgia State Retirees Association - so* that you will have an accurate understanding when changes to the SHBP are being discussed. Although several information sources were used, a report issued by the Department of Audits, Performance Audits Division in 2005 regarding the SHBP was used extensively. These sources along with my State Government experience form the basis of the opinions that I express in this document.

Background

Legislation creating a Health Insurance plan for state employees was enacted in 1961. The legislation placed the policy-making functions with the constitutional State Personnel Board and the administration of the plan with the State Merit System of Personnel Administration. The insurance plan for state employees began operation in 1962. The General Assembly enacted two additional laws in 1975 creating a health insurance plan for public school teachers and a health insurance plan for non-certificated public school employees. Both enactments provided for the same policy-making and administration bodies as was provided for state employees. The plan for teachers was funded and began operation in 1979 and the plan for non-certificated public school employees was funded and began operation in 1985. All of these health insurance plans were subsequently combined into the State Health Benefit Plan. Legislation was enacted in 1999, to transfer policy-making functions to the Board of Community Health and to transfer the administration of the Plan to the Department of Community Health (DCH).

The DCH now administers the SHBP which covers more than 600,000 state employees, certificated school system employees, non-certificated school employees, retirees and dependents. The SHBP is operated as a single fund, not four separate funds. The stated purpose of the SHBP is to provide a healthcare benefit that is competitive with other commercial benefit plans in quality of care, access to providers, and efficient management of provider fees and utilization. As of November 2003, there were 313,187 active and retired employees covered by the Plan of which active employees made up 76.68% of the total and retirees comprised the remaining 23.32%. In addition to employees, the Plan also covered 320,003 dependents for a total number of covered individuals of 633,190.

Funding

The SHBP is primarily funded by employee premiums and employer contributions. While employee premium rates are established for each of the coverage tiers (single and family) within each coverage option (PPO, Indemnity, etc.); **employer contributions are set to provide the employer share of the total funding needed for the entire plan** (i.e. they are not tied to the costs of individual plan options and/or tiers). The employee premium is typically deducted from the employee's paycheck once a month and submitted to SHBP by the employee's payroll location. Employer contributions are also typically submitted monthly to SHBP by each payroll location.

Employee's Contributions

A primary objective in setting employee premium rates is that employees contribute 25% of Plan costs and employers contribute the remaining 75%. This objective is driven by a 1982 Resolution of the General Assembly providing that the cost of the Plan "shall be established at approximately 75 percent to be borne by the state and approximately 25 percent to be borne by the employees of the state."

To set employee premiums, the SHBP has developed estimated total equivalent premiums for each option and tier. Employees pay varying proportions of the total equivalent premiums. While SHBP personnel seek to achieve a 25% employee contribution proportion in aggregate for the entire Plan, they also attempt to "manage" the Plan by setting premiums for different coverage options and tiers. For example, employees are required to pay a higher proportion of the total equivalent premium for the Indemnity Option in an effort to discourage use of this higher-cost coverage. Employees also pay a higher proportion of the total equivalent premiums of Consumer Choice versions of each option as allowed by law.

Employee premium rates are evaluated and revised annually. Based on actuarial projections of anticipated cost increases for the Plan, representatives of DCH, the Governor's Office, and the Office of Planning and Budget (OPB) develop proposed changes in employee rates while also considering benefit changes and employer funding available to address cost increases. For example, in fiscal year 2005 the changes included; 1.) A 10% increase in employee contributions for most coverage options, 2.) Several benefit changes and 3.) Use of a portion of the Fund Balance (reserves) *but no change to employer contributions.* The changes were reviewed and approved by the DCH Board <u>*and (for the first time) the changes were also included in DCH's Budget for approval by the General Assembly*</u>.

In addition to the regular employee premium rates, SHBP sets employee premium rates for special groups of members. Examples of special groups include:

· Members on certain types of leave (such as Disability and Emergency Military Leave) are required to pay an administrative fee ($5 monthly) in addition to the normal employee premium. Members on other types of leave (such as Educational and Convenience Leave) are required to pay the total cost of coverage (both employee and employer portions of the estimated option cost) and an administrative fee.

· Members that are allowed to continue coverage after terminating employment are required to pay the total cost of coverage (both employee and employer portions of the estimated option cost). Under state law, employees with eight or more years of service are eligible to continue coverage indefinitely. Under federal law, employees that meet certain requirements under the Consolidated Omnibus Budget Reconciliation Act (COBRA) are eligible to continue coverage for 18 to 36 months.

· Retirees and dependents that are covered by Medicare have lower premiums in recognition of the fact that that the SHBP becomes secondary coverage to Medicare. Members that are 65 years of age and older that do not have Medicare coverage have higher premiums.

Employer Contributions

DCH regulations provide that employer contribution rates are established by the DCH Board *subject to the Governor's approval* and that the rates may be a dollar amount, a dollar amount for each enrolled employee, or a percentage of salary. As stated above, the employer contribution rates are based on the objective of providing 75% of the total cost of the Plan.

The following is a description of the Plan's rates for employers:

· **State Employees** - Employer contributions made by state entities are based on a percentage of the total outlay for personal services. The current monthly employer contribution rate is 16.7% of the salaries of active employees. This employer contribution rate provides coverage for both active and retired state employees.

· **Public School Teachers** - Employer contributions made by local school systems are based on a percentage of the total "state-based" salaries for certificated positions (regardless of fund source). The current employer contribution rate is 16.7% of the state base salaries of active employees and provides coverage for both active and retired teachers; a separate employer contribution is made by the Department of Education (DOE) for teachers that retired prior to January 1, 1979. The additional amount of contributions made by DOE for teachers that retired prior to 1979 is approximately $10 million.

· **Public School (Non-certificated) Employees** - (school bus drivers, cafeteria workers, etc.) - SHBP funding policy provides that local school systems and the state should each contribute approximately one-half of the required employer contribution. The current employer rate paid by local school systems for public school employees is $162.72 per covered active employee per month; a separate employer contribution is made by the DOE for public school employees that retired prior to January 1, 1985.

In some years the SHBP has also received direct appropriations from the General Assembly.

The Board of DCH provides policy direction for the operation of the SHBP and is authorized by law to set rules and regulations for the SHBP. The Board is also responsible for plan design, establishing member premium rates for each coverage type and option, establishing employer contribution rates (*subject to the Governor's approval and, since 2005, also subject to the General Assembly's approval*), and approving contracts for insurance, health services, and administrative services.

In fiscal year 2004, the SHBP collected approximately $1.74 billion in earned premiums (employee premiums and employer contributions), $34 million in appropriated state funds, and $5.5 million in interest and other income. The Plan had expenditures of approximately $1.85 billion, of which $1.33 billion (72%) was claims expense for the PPO, Indemnity, and self-insured HMO options. Premium payments for the fully-insured HMOs totaled $424.2 million (23%). Administrative expenses included $93.0 million of management and consulting contract expenses and $5.3 million of other administrative expenses for a total of $98.4 million (5%). In other words, the SHBP's expenditures exceeded its revenues by approximately $76.5 million in fiscal year 2004. This shortfall was covered by the plan's reserves (or Fund Balance) which totaled $356.1 million at the end of fiscal year 2004.

The employer contribution rates were increased from 13.1% in 2006 to 14.2% and again in 2007 to the present rate of 16.713%. The fund balances have eroded from a high of $438 million in 2002 to $79 million in 2006. It is not presently known if the recent increases in the employer rates have changed this downward trend.

Governmental Accounting Standards Board

The Financial Accounting Foundation is an independent, private-sector, not-for-profit organization established to set financial reporting standards for any entity that produces accounting statements. *This is not a Federal Agency and receives no Federal funds and the standards it sets are not Federal rules or laws.* Two groups are under this Foundation; the Financial Accounting Standards Board, (FASB) which sets standards for non-government entities and the Governmental Accounting Standards Board (GASB) which sets financial reporting standards for all levels of government; municipal, county, state and the U.S. Government. Governments and the accounting industry recognize GASB as the official source of generally accepted accounting principles (GAAP) for state and local governments.

The reason for setting standards is so that the readers of financial statements will have some degree of consistency, comparability and reliability from government to government. This is particularly important to the individuals who invest in the bonds sold by the governments. GASB has recently issued their Statement 45. This statement recognizes that the individuals at the various levels of government who make decisions are quite prone to creating programs, regulations, laws, etc. which are politically expedient at the time but which may have significant financial impact in the future. GASB 45 requires that any program, policy, law regulation, etc. which has a financial impact in the future be clearly stated in the financial statements of that governmental unit and that the amount of the impact be shown. The future liability of the SBHP obviously is one that should be reported in the financial statements under this rule.

Georgia's current "AAA" bond rating is the highest rating offered by the rating agencies. The Governor and a number of Senators and Representatives have been pointing to GASB 45 as a factor in why "something will have to be done" to correct the "problems" with the SHBP to prevent Georgia's "AAA" bond rating from being lowered. It should be noted here that there are many factors that can affect the bond rating of a government. In addition to the future liability of the SHBP there are others in similar straits, such as the self-insurance programs operated by the Department of Administrative Services. The overall financial condition of the State is the driving force behind the bond rating, not just one program. If the Governor and General Assembly do not develop and implement plans to address the funding of these liabilities over the next several years then the bond rating could be affected.

Conclusions

The participants of the SHBP, DCH, the Governor and the General Assembly are faced with two problems: 1) The possibility of the fund expending all of it available reserves in the short run (within the two or three years) and 2) The formulation and implementation of a plan to meet the long-term liability surfaced by GASB 45.

By not appropriating funds to increase the employer rates for several years (from 2000 through 2005) the Governor's Office and the General Assembly consciously set up a situation that precipitated a financial crisis for the SBHP and all of its participants. All of the reserves were depleted because expenses exceeded income in those years. This places the Board of DCH in a position of recommending significant increases in premiums (both employee and employer) and/or increasing co-pays significantly and/or reducing benefits to keep the SHBP solvent. If the Governor and General Assembly chooses to ignore any or all of the recommendations the problem grows larger, quicker. When the Board of DCH makes the recommendation(s) that it must make to keep the SHBP solvent, the Governor and your Senators and Representatives will be able to say they didn't do this, they were only following the recommendations of the Board. Remember, as stated previously, that changes in premium rates, co-pays and benefits are developed by DCH in concert with the Governor's Office and OPB and are approved by the General Assembly in the annual Appropriations Act.

GASB 45 is a large problem but there is a significantly longer period of time to solve it. The pending actuarial report will shed light on the size of the unfunded liability and the Governor and the General Assembly will then know the magnitude of the liability they are facing. GASB 45 does not mandate funding of the liability, only that it be recognized in the financial statements. How the government chooses to fund the liability is a policy decision of the government. This policy decision is then evaluated by the bond rating agencies for any effect on the bond rating. In other words, there may or may not be an effect on the bond rating depending on how the government chooses to solve the liability.

Clearly, the Governor and the General Assembly are intimately knowledgeable of the problems and are the only ones who have the power to solve the "problem."

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