ATTACHMENT B

Sally Symanski, CPA
State Auditor

STATE OF COLORADO

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Legislative Services Building
200 East 14th Avenue
Denver, Colorado 80203-2211

September 13, 2006

MEMORANDUM

To: Legislative Audit Committee

From: Sally Symanski, CPA, State Auditor

Re: Status of Group Benefit Plans Statewide Pilot Program

Statute (Section 24-50-617, C.R.S.) authorized the State Personnel Director to conduct a group benefit plans statewide pilot program for all employees. The purpose of the pilot program was to offer at least one low-cost catastrophic medical benefit plan to all state employees, as well as other medical benefit plans with differing costs that allow employees to make choices to meet their individual needs. Statute also required the State Auditor to conduct a performance review of the pilot program and present the review to the Legislative Audit Committee on or before February 1, 2007. According to statute, the pilot program terminates automatically on December 31, 2007, unless terminated on an earlier date by the State Personnel Director.

This legislation was enacted during the 2002 Legislative Session when the cost of the medical benefit plans offered to employees statewide increased significantly over the prior year, and many employees could no longer afford even minimal coverage. In response to the legislation, the Department of Personnel & Administration reported that it developed and released a Request for Proposal (RFP) requesting one carrier to offer both an HMO and a PPO statewide. However, the Department received only one response to the RFP, and the rates in the proposal were not competitive. As a result, the Department did not implement the statewide pilot program on January 1, 2003 as originally planned.

In Fiscal Year 2005 the Department implemented changes which resulted in the State self-funding its medical benefit plans, as recommended in our 2003 Employee Benefit Program audit report. This allowed the Department to offer four plans statewide that vary in price and include an option for low-cost catastrophic coverage. Fiscal Year 2007 employee costs for these plans range from $7.08 to $235.68 per month for individual coverage and from $160.28 to $824.76 per month for family coverage. With this change in the funding mechanism for medical benefit plans, the Department reports that it was able to accomplish the goal of the pilot program to provide employees with several options for medical coverage, including a low-cost alternative, without actually having to implement the pilot program.

Since the pilot program was not implemented, an audit will not be conducted at this time. The Office of the State Auditor will continue to review aspects of employee benefits as part of the Total Compensation performance audit, as required by Section 24-50-104, C.R.S., and through additional reviews as deemed appropriate. The next Total Compensation audit is scheduled for June 2009. We have asked the Department to provide a status report on the implementation of recommendations contained in our 2003 Employee Benefit Program audit report related to medical benefits. This status report is attached for your review.

State of Colorado

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September 11, 2006

Legislative Audit Committee
Office of the State Auditor
Legislative Services Building
200 East 14th Avenue, 2nd floor
Denver, CO 80203

Dear Committee Members:

The following are our responses to the request for a status update of several recommendations from the August 2003 Performance Audit of the Employee Benefit Program.

Recommendation No. 1: Use the results of survey of state employees who are not participating in the State's health plan to make appropriate plan adjustments aimed at increasing employee participation.

Implementation Status: *Implemented.*

The Department completed a survey of state employees who are not participating in the State's health plans. Based upon the results of this survey, the Department determined there is a direct correlation between employer (state) contribution and employee participation. Therefore, the Department worked with the General Assembly to increase the state contribution to 56 percent of prevailing market employer contribution levels in 2005, 66 percent in FY 2005-06, and 75 percent in FY 2006-07. DPA plans to pursue additional increases in the state contribution over the next two years to bring them up to prevailing levels. The Department is also aggressively working to keep premium increases as low as possible. A wider range of choices is already offered and the Department will continue to refine plan designs. Three medical plans are now offered: two fully insured HMOs in certain geographic areas and a statewide self-funded plan offering four options, including a low cost plan that qualifies for Health Savings Accounts and an affordable catastrophic plan for as little as $7.08 per employee for employee-only coverage. The progress made in the state contribution levels and plan adjustments resulted in increased enrollment of nearly 1 percent

(0.88%) in FY 2005-06 and 2 percent for FY 2006-07. Although these seem relatively small, they represent progress given the inertia factor and reverse several years of falling enrollment (1.75% decline in FY 2004-05).

Recommendation No. 2: Consider modifying the medical benefit plan by eliminating the current 3-tier premium rate structure in favor of a 4-tier rate structure with consistent tier ratios for all fully insured plans.

Implementation Status: *Implemented.*

The Department completed the conversion to a four-tier rate structure (i.e., employee only, employee plus spouse, employee plus child/children, employee plus spouse and child/children) beginning July 1, 2005.

Recommendation No. 3: Consider proposing legislation to eliminate specific statutory mandates on the numbers and types of medical plans offered and streamline carrier choices.

Implementation Status: *Implemented.*

Senate Bill 04-008 repealed Section 24-50-606, C.R.S. that required the availability of two Health Maintenance Organizations in counties with 500 or more state employees.

Recommendation No. 4: Re-evaluate the minimum employee work requirement: re-evaluate eligibility for foster children and grandchildren; analyze the costs and benefits of more restrictive open enrollment policies that minimize adverse selection; and limit employees' ability to change their elections, and that of their dependents, to the annual enrollment opportunity.

Implementation Status: *Implemented.*

The Department has comprehensively re-evaluated eligibility and a number changes have been made.

The General Assembly passed Senate Bill 04-008 granting authority to the Director to adopt procedures determining benefit eligibility requirements and the percentage of the state contribution to health benefits for all employees. The Department conducted a study of eligibility for permanent part-time employees and concluded that it is not cost effective to implement changes at this time. To do so would necessitate dual systems because of the grandfathering provision so it is expected to cost more to implement and administer than would be saved in the first few years. In addition, it has potential for significant impact on the attraction and retention of essential seasonal employees in the state workforce and the Department will shortly begin to work closely with state agencies in assessing the impact. To date, DPA prioritized its resources to focus on major cost containment initiatives of higher priority, including self-funding medical and dental plans, changing the plan year to a fiscal year, and disease management initiatives.

DPA researched eligibility for foster children and grandchildren (mandated by 24-50-603(5)(a), C.R.S.) and found current state policies were consistent with permitted changes by Section 125 of the Internal Revenue Code and reflect standard industry practice. House Bill 06-1256 tightened the eligibility of adult dependent children by adopting the consistent policy that such dependents are eligible through the end of the month in which their eligibility ends, rather than the end of the plan year (e.g., they turn age 19, are no longer a full-time student, or full-time students turn age 24). The Department has begun to require more robust documentation of eligibility and plans to conduct an eligibility audit this fiscal year to identify ineligible participants and remove them from the plans. In general, this area is continuously analyzed in consideration of the data now available and legislatively mandated changes on dependent coverage. For example, with the additional types of adult dependents now eligible for coverage, pursuant to HB05-1101, the Department is considering changes to the more restrictive special enrollment events required under the Health Insurance Portability and Accountability Act (HIPAA) in order to avoid adverse selection against the plans from mid-year elections.

Finally, effective July 1, 2005, post-tax elections for both health and dental are subject to the same restrictions as pre-tax elections; that is the election is irrevocable except as specifically permitted by the Plan Document.

Recommendation No. 5: Consider alternatives for partial employer contributions to the health benefits of eligible part-time employees.

Implementation Status: *Implemented.*

In conjunction with Recommendation No. 4, the Department evaluated policy options and the methodologies for determining partial employer contributions. For reasons stated above in response to Recommendation No. 4, the Department prioritized its limited resources to focus on major cost containment initiatives of higher priority, but is continuing to evaluate this issue.

Recommendation No. 6: Establish reporting requirements to capture appropriate pricing, claims, and utilization data in order to fully inform plan funding and design decisions regardless of whether the State remains fully-insured or elects to switch to self-insurance.

Implementation Status: *Implemented.*

Under self-funding the State now controls the data and DPA negotiated better reporting from the fully insured carriers so utilization data and metrics, such as average hospital days, are now available and will help with future data-driven decisions. A utilization and financial analyst was hired and in-depth data analysis has begun. With 18 months of self-funded data (July 1, 2005, through December 31, 2006) and better data from the fully insured carriers, the Department will have a much clearer picture for pricing FY 2007-08 plans and beyond. Having access to complete utilization data through self-funding is already being used as a baseline to measure the efficacy of disease management initiatives and leverage negotiations. For example, the diabetes initiative was instituted this year is to measure the degree to which removing obstacles to compliance with prescribed therapy (e.g., price of prescriptions and equipment) reduces overall claims costs for diabetics. The data will drive the future plan design decision on this initiative as well as other initiatives such as asthma.

Recommendation No. 7: Analyze the most recent and comprehensive demographic and financial information on the plan to evaluate financing options and benefit designs for a possible State self-insurance plan.

Implementation Status: *Implemented.*

Self-funded medical and dental was implemented on July 1, 2005, which saved employees approximately $4 million in premiums increases in the first year. In addition, by prioritizing the shift of the plan year to a fiscal year basis, employees realized the savings in increases six months earlier than they would have under the former calendar year cycle. This shift also aligned benefits with salaries so total compensation budgeting is easier and employees can make more informed decisions about their insurance needs at the same time pay increases are implemented.

Please contact me if you wish to discuss this status update further.

Sincerely,

David M. Kaye, Acting Director
Division of Human Resources

cc: Jeffrey M. Wells, Executive Director, Department of Personnel & Administration
Jennifer Okes, Chief Financial Officer, Department of Personnel & Administration
Karen Fassler, Total Compensation Manager, Division of Human Resources
Michelle Colin, Legislative Auditor