STATE OF WEST VIRGINIA

PRELIMINARY PERFORMANCE REVIEW OF THE

PUBLIC EMPLOYEES INSURANCE AGENCY
FINANCE BOARD

The Cost of Insurance Plans
are not Equitably Apportioned
Among Participants

The PEIA Finance Board Actively
Participates
in Meetings

OFFICE OF LEGISLATIVE AUDITOR
Performance Evaluation and Research Division
Building 1, Room W-314
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January 2001

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January 2001

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John Sylvia
Director

January 7, 2001

The Honorable Edwin J. Bowman
State Senate
129 West Circle Drive
Weirton, West Virginia 26062

The Honorable Vicki V. Douglas
House of Delegates
Building 1, Room E-213
1900 Kanawha Boulevard, East
Charleston, West Virginia 25305-0470

Dear Chairs:

Pursuant to the West Virginia Sunset Law, we are transmitting a *Preliminary Performance Review of the Public Employees Insurance Agency Finance Board*, which will be presented to the Joint Committee on Government Operations on Sunday, January 7, 2001. The issues covered herein are *"The Cost of Insurance Plans are not Equitably Apportioned Among Participants; and The PEIA Finance Board Actively Participates in Meetings."*

We conducted an exit conference on January 2, 2001, with the Public Employees Insurance Agency Finance Board. We received the agency response on January 4, 2001.

Let me know if you have any questions.

Sincerely,

John Sylvia

John Sylvia

JS/wsc

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Issue Area 1: The Cost of Insurance Plans are not Equitably Apportioned Among Participants.

By law (§5-16-5), the PEIA Finance Board is required to apportion necessary insurance costs equitably among participating employers, employees, retired employees, and providers of health care services. However, **the PEIA Finance Board has primarily relied upon employers and providers to pay an inequitable amount of rising plan costs.** In addition to employers paying 88% to 93% of the premiums for its active employees which is high compared to the national average, State and local employers also contribute funds for the costs of State and local retirees by paying premiums in excess of the amount necessary for their active employees. Employers' contribution for retirees is between 60% and 70% of the retirees' insurance costs. This employer contribution for retirees is growing three times faster than the growth of employers' total contributions for both retirees and employees, while retirees have gone several years without any changes in their premium payment. However, these costs do not include the cost incurred by providers in the form of contractual allowances that pay providers less than their actual costs. Providers have been used to consume the inflationary medical costs by reducing reimbursement rates. Rather than a proportional increase in retiree and employee premiums in relation to each groups' costs, the Board has depended on providers and employers to absorb medical cost increases.

Issue Area 2: The PEIA Finance Board actively participates in meetings.

The Finance Board meets quarterly and with a quorum as required by law (§5-16-5). The Board has almost perfect attendance for every meeting and have always met with a quorum. The board members take their responsibility seriously and actively represent their interest groups in the development, implementation and approval of financial plans.

Objective, Scope and Methodology

The preliminary performance review of the PEIA Finance Board is required and authorized by the West Virginia Sunset Law, Chapter 4, Article 10, Section 5 of the West Virginia *Code*, as amended. The Finance Board is mandated to bring fiscal stability to PEIA through the development of annual financial plans and long-range plans and apportion costs equitably among participating employers, employees, retired employees, and providers of health care services.

Objective

The objective of this review is to determine the extent of the PEIA Finance Board's involvement in developing financial plans. This was to test whether the Director of PEIA as the Chair of the Board was actually developing financial plans or if Board members were involved in developing the plans. Another objective of the review is to determine the Board's effectiveness in achieving the important statutory requirement of providing an equitable apportionment of insurance costs among the plan participants.

Scope

The scope of this report examined the Finance Board's activities since 1990. Of primary interest is the extent of the Board's participation in developing financial plans, and its efforts in achieving the statutory requirement to apportion insurance costs equitably among employers, employees, retired employees, and providers of health care services.

Methodology

The report includes a review of the PEIA Finance Board minutes, financial plans, PEIA financial reports, the Segal report, West Virginia Health Care Authority reports, and a survey of Finance Board members.

active employees to compensate for the insufficient retiree premium. The State has paid an average of 65% of total claim expenses and administrative costs for retirees over the past 8 years. As exhibited in Table 1, you can see the difference and the amount contributed by employer funds for retirees.

Table 1
Employers' Contribution Rates and Amounts for Retirees

Fiscal Year	Employers' Contribution Rates	Employers' Contribution Amount
1993	60%	$34,040,000
1994	64%	$39,457,000
1995	67%	$46,176,000
1996	67%	$44,920,000
1997	70%	$53,744,000
1998	65%	$51,106,000
1999	65%	$57,962,000
2000	64%	$55,821,766

--Employer Contribution Amount is calculated by taking the retiree's share of the plan costs and subtracting their premiums. For FY 1993, the retirees plan costs were 56,659,000 and their premiums were 22,619,000.
22,619,000 (premium revenue) - 56,659,000 (plan costs) = -34,040,000 (costs picked up by employers)
--Employer Contribution Rates are calculated by taking the retiree fund negative balance and dividing it by the plan costs (-34,040,000(negative fund balance)/56,659,000(retiree plan costs) = 60%).

A concern with the retiree fund is the rate of growth of the needed employer contributions compared to the rate of growth in the amount of employers' contributions for both employees and retirees (see Table 2). Since 1993 to 2000, the needed retiree contribution from employers has increased by 64%, while the total employer contribution for both employees and retirees has increase by only 20% over the same period. While retirees' total expenses have been rising 64%, retiree premiums have in many years not changed at all because the Board has relied on Employers to pay the difference. The disparity in growth rates creates the situation that: 1) employers will be under pressure to pay a larger proportion of its premiums for retirees; 2) If employers cannot pay the larger proportion, then the growth in the needed retiree contribution absorbs the Board's ability to accumulate surpluses or reserves for unexpected events or forecasting errors.

Table 2 Growth Rate of Employers' Contribution to Retirees & the State Employer's Contributions for <u>both</u> Active Employees and Retirees				
Fiscal Year	Employers' Contribution to Retiree Costs	Percentage Increase	State Contributions for Active Employees & Retirees	Percentage Increase
1993	$34 million		$232.5 million	
2000	$55.8 million	64%	$279.7 million	20%

Providers

Providers make up all health care facilities that provide services to policyholders. Although they do not literally contribute premium revenues to PEIA, they do, however, pay in an indirect manner. This is accomplished by PEIA setting reimbursement rates for particular procedures performed by the provider. For example, when a patient receives a physical, the provider is paid what PEIA's reimbursement rate is for a physical regardless what the provider bills. Also, due to the fact that health care providers cannot "balance bill" patients in West Virginia; providers must accept, to a certain extent, the reimbursement rates set by PEIA. It should also be noted that PEIA's policyholders make up approximately 11% of the State's population which adds to PEIA's market power within the State and bordering State counties.

Over the past 10 years multiple cost saving measures have been enforced by the PEIA on providers. This has been accomplished by reducing physician fee schedule reimbursement, hospital fee schedule reimbursement and implementing resource-based relative value scale. PEIA has provided dollar estimates showing a $47,188,000 reduction in revenues to providers based on changes to the plan over the past 10 years.

These data are supported by the West Virginia Health Care Authority annual reports to the Legislature. The reports show that contractual allowances for government insurance programs are a contributing factor for lower hospital profit margins. Medicare, which represents 50% of inpatients in the State, paid 92 cents for each $1 of operating expenses (net bad debt, charity care and contractual allowances) during fiscal year 1999. While Medicaid, which represented 16% of inpatients in the state, only paid 90 cents for each $1 of costs (net bad debt, charity care and contractual allowances). The contractual allowance for Medicare reduced gross revenues by $938,280,685 and Medicaid's allowances reduced gross revenues by $270,673,610. PEIA's contractual allowances reduced providers' gross revenues by $73,226,507 and paid 98 cents to each dollar of expenses (net bad debt, charity care and contractual allowances) during fiscal year 1999. Table 3 below displays the contractual allowances of each government insurance provider.

Table 3 Government Insurance Contractual Allowances for All Hospitals FY 1999			
	Gross Patient Revenue	Contractual Allowances	Net Patient Revenue
PEIA	$173,792,404	$73,226,507	$100,565,897
Medicare	$2,087,956,713	$938,280,685	$1,149,676,028
Medicaid	$620,307,115	$270,673,610	$349,633,505
Source: West Virginia Health Care Authority Annual Report, 2000, P. 30.			

As can be seen by these numbers, PEIA pays more per dollar and shows a lower contractual allowance than Medicare or Medicaid. But with the three governmental programs combined, providers may not be able to assume further reductions, and an accessibility problem could arise. The possibility of provider accessibility limitations could occur with continued reimbursement rate decreases.

Conclusion

The PEIA Finance Board has relied upon the employer and providers to pay an inequitable amount of rising plan costs. This is largely due to shortfalls of retiree and employee premiums in relation to each groups' costs. The Finance Board has not set rates representative of the inflationary costs for employees and retirees. A quote from the "Segal Report - Legislative Study" is as follows:

> The State appears to have gone out of its way to absorb the majority of inflationary cost increases in the PEIA program without passing along to employees and retirees their fair share of those increases. As a result, the premiums charged to employees and retirees are among the lowest of all states.

The providers have also been used to absorb the inflationary medical costs by reducing reimbursement rates. This is done rather than increasing employee, employer and retiree premiums. But, there is concern of reaching the limit in reducing provider cost reimbursement further without an adverse effect on the provider industry and accessibility of health care.

Recommendation 1:

The PEIA Finance Board should implement tools provided in the Code which allow them to set premiums based on individual participant group costs and ability to pay for all participants. The Finance Board should implement an ability to pay premium schedule for retirees in addition to years of service. Information is obtained by the Agency for premium assistance programs and could be used at the other end of the spectrum for increased premiums due to income.

Recommendation 2:

The PEIA Finance Board should implement premium establishment methods which offset medical cost inflation. A formula should be developed which considers each participant groups' costs to the plan, medical cost inflation rates, and other necessary factors to determine premiums for each participant group. In addition, the Finance Board needs to determine and set the percentages expected from each participant so less ambiguity surrounds the budget process. Once this is determined, all participants' costs should then be adjusted representative of medical cost increases on a percentage basis.

Recommendation 3:

The PEIA Finance Board should continue their method of controlling provider costs with reimbursement rates but maintain close scrutiny of these methods to avoid harming providers.

Issue Area 2: The PEIA Finance Board Actively Participates in Meetings.

The intent of the Public Employees Insurance Agency (PEIA) Finance Board is to develop financial plans that provide financial stability to PEIA' s insurance programs. In developing these plans, it is also the intention to have citizen input representing a variety of interest groups, including a representative of education employees, a representative of public employees, a representative of organized labor and three members from the public at large. The citizen members take their responsibility seriously through providing adequate input in financial plan development and maintaining close to perfect attendance.

Board Members Provide Adequate Input in Developing Financial Plans

A Board that consists of citizen members and the Director of the administrative agency runs the risk of having most of the decision making done by the Director and plans being implemented without Board approval. Therefore, part of this review included an assessment of the citizen members' involvement in developing the financial plans. A review of the Board minutes indicates that Board members take their responsibilities seriously as indicated by the high number of meetings and near-perfect attendance since 1990 (see Table 4).

Table 4
Meetings and Attendance

Year	Number of Meetings	Quorum	Attendance Rate
1990	17	17	100%
1991	17	17	91%
1992	9	9	98%
1993	5	5	92%
1994	7	7	97%
1995	12	12	97%
1996	11	11	85%
1997	13	13	94%
1998	13	13	92%
1999	8	8	82%
March, 2000	1	1	100%

West Virginia Code §5-16-5 states that the Finance Board shall meet on at least a quarterly basis. The Finance Board has met well in excess of the required quarterly meetings for the past 10 years. From 1990 through March 2000, the Finance Board has held 113 meetings, for an average of 11 meetings per year. The Board attendance rate was 93% for this duration. Consequently, a quorum has always been reached.

Board minutes also reveal that members actively participate in meetings. The members submit a variety of requests to PEIA staff and the Actuary to be introduced for the development of financial plans including:

- Premium increases tiered for salary ranges.
- Subsidy programs for lower income employees.
- Co-pay and deductible increases.
- Discount rates on generic drugs for prescription program.
- Utilization management.
- Public Hearing concerns and input.
- Error rate issues between projected and actual financial plans.
- Wellness program initiatives.
- Trend Analysis.

In addition, according to meeting minutes and Board member testimony, the financial plans and revisions are approved by a majority vote.

Conclusion

PEIA Finance Board members are actively involved in developing and carrying out financial plans. The members are in compliance with the statute by maintaining close to perfect attendance, meeting quarterly and with a quorum present. Additionally, the Board members actively take part in developing, approving and implementing plans.

Recommendation 4:

The Board members should continue to attend meetings and actively participate in the development, approval and implementation of financial plans in order to attempt to keep financial stability within PEIA.

APPENDIX A

Transmittal Letter to Agency

WEST VIRGINIA LEGISLATURE

Performance Evaluation and Research Division

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John Sylvia
Director

December 21, 2000

Robert L. Ayers, Executive Director
Public Employees Insurance Agency
Building 5, Room 1001
1900 Kanawha Blvd., East
Charleston, WV 25305

Dear Mr. Ayers:

Enclosed are two issues regarding the PEIA Finance Board which will be presented at the January Legislative Interims on January 7, 2001 between 4 P.M. and 6 P.M. The meeting is scheduled to be held in the Senate Judiciary committee room. Please review the enclosed issues and contact us to schedule an exit conference for next week. I also need to inform you that there will be two more issues reported on the PEIA Finance Board at the February Interims. These issues were originally planned to be included in this current January report but were removed to complete further work. The issues will discuss the Finance Board's performance with respect to providing financial stability to PEIA, and the cost of sick leave conversion to the State.

A written response from the Board must be submitted by January 3, 2001 in order for it to be included in the January report. If you have any questions give me a call. Thank you and your staff for the cooperation we received during this audit.

Sincerely,

John Sylvia

John Sylvia

Joint Committee on Government and Finance

APPENDIX B

Premiums

Premium Rate Increases

	07/89	7/90	11/90	1/91	7/91	7/96	1/97	7/97	1/98	1/99	7/99	11/99	7/00
1	9.60	10.60	10.60	0.00	0.00	0.00	10.00	10.00	10.00	10.00	10.00	15.00	15.00
2	22.00	24.20	24.20	40.00	40.00	40.00	50.00	50.00	48.00	48.00	48.00	58.00	58.00
3	198.00	217.80	317.70	404.00	381.00	388.34	388.34	404.64	392.62	441.10	452.10	452.00	476.00
4	64.00	64.00	64.00	117.00	117.00	117.00	132.10	132.10*	132.60*	132.60*	132.60*	132.60*	132.60*

Premium Rate Percentage Increases

	7/89-7/90 % +/-	7/90-11/90 % +/-	11/90-1/91 % +/-	1/91-7/91 % +/-	7/91-7/96 % +/-	7/96-1/97 % +/-	1/97-7/97 % +/-	7/97-1/98 % +/-	1/98-1/99 % +/-	1/99-7/99 % +/-	7/99-11/99 % +/-	11/99-7/00 % +/-	Total
1	10%	0%	-100%	0%	0%	100%	0%	0%	0%	0%	50%	0%	60%
2	10%	0%	65%	0%	0%	25%	0%	-4%	0%	0%	21%	0%	117%
3	10%	46%	27%	-6%	2%	0%	4%	-3%	12%	3%	0%	5%	100%
4	0%	0%	83%	0%	0%	13%	0%	0%	0%	0%	0%	0%	96%

Legend:
1. Single employee coverage
2. Employee with family coverage
3. Employer family
4. Single Retiree

- Effective January 1, 1990 Employee Premiums became salary based. The salary range of 15,000 to 30,000 was used for 1991 to 1996 while 18,000 to 30,000 was used for 1997 to January 1999 and 22,000 to 30,000 for 6 months of 1999 and 18,000 to 30,000 for 1999, 2000 and 2001 in this review.

* PEIA enacted a years of service premium for all retirees subsequent to June 30, 1997. This rate format creates lower premiums for retirees with more years of service to the state. The premiums ranges from $45.50 to $1,401.26. All retirees prior to 1997 premiums ranged from $45.50 to $267.06 depending on tier and medicare eligibility.

APPENDIX C

Agency Response

Cecil H. Underwood
Governor

Robert L. Ayers, ARM
Executive Director

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January 3, 2001

Mr. John Sylvia
West Virginia Legislature
Performance Evaluation and Research Division
Building 1, Room W-314
1900 Kanawha Boulevard, East
Charleston, West Virginia 25305-0610

Dear Mr. Sylvia:

On behalf of the PEIA Finance Board, I respectfully submit the following responses to work completed by the Performance Evaluation Division of the West Virginia Legislature.

First, please allow me to say that PEIA clearly views this process as meaningful and informative. Having an outside, objective eye reviewing the work of public agencies is beneficial to the taxpayers as well as the individual responsible for the program. We sincerely believe we benefit from the review process.

Below is a brief response to the items covered in the report dated December 21, 2000.

Issue Area 1 The Cost of Insurance Plans are not Equitably Apportioned Among Participants.

While this continues to be a heavily debated issue, the facts as presented by the auditors speak for themselves. PEIA's costs are largely borne by the state taxpayers (the Employer). As costs continue to rise, and State revenues slow, this issue will forcibly correct itself.

The retiree funding mechanism is a totally different issue. The "subsidy" as defined in the report, is the biggest "time bomb" surrounding the program. Because its growth rate remains in double digits, it will soon consume most, if not all the growth in state revenues. This area is an immediate action item for long term change.

The providers in the state clearly are the most unrepresented and statutorily obligated participants in the program. They unwittingly have to accept, in most part, what action is taken without recourse. Clearly, PEIA enjoys a program benefit like no other. We set rates and they are non-negotiable.

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Mr. John Sylvia
January 3, 2001
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Issue Area 2 The PEIA Finance Board actively participates in meetings.

The PEIA Finance Board meets regularly and when necessary to conduct the business for which it is charged. Our members are well educated in all aspects of our program and actively participate in the development and implementation of our financial plans while still seeking to represent the interest groups for which they were appointed.

Mr. Sylvia, thank you for the opportunity to respond to the issues raised in this report. Should you require any additional information, please do not hesitate to contact me at 558-6244 extension 225.

Sincerely,

Robert L. Ayers

Robert L. Ayers, ARM
Executive Director

RLA:ksc

C: PEIA Finance Board