Memorandum 13-137 Amendments to Employee Health Insurance Plan

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TO: Mayor Wythe and Homer City Council
FROM: Walt Wrede
DATE: October 5, 2013
SUBJECT: Amendments to Employee Health Insurance Plan
Introduction
In June of this year, the City Council held a workshop to hear a presentation from the City's insurance broker / consultant on the state of the employee health insurance plan. The picture presented was bleak despite recent amendments to the benefit package, the implementation of employee premiums, an increase in the City contribution, and the implementation of a new wellness program. Health care costs are rising so rapidly that it affects every decision we make about the budget. Health Insurance is now driving the bus. There are many factors contributing to this including escalating medical costs, an aging workforce, and very high utilization of a rich plan. Following is a quick recap of the workshop information. In calendar year 2012, the City budgeted $1,300 per employee per month for health insurance. Actual expenses for that year were $1,912.82 per employee per month. The City experienced cost overruns for that year of $641,115. In 2013 (this year), the City contribution was raised to $1,500 per employee, per month. The average cost was $1,871.20 per employee per month at the end of May and based upon that trend, it was projected that the City would lose another $371,290 in 2013. The Council transferred $800,000 from reserves to the self-insurance fund as part of the mid-year budget amendment. This transfer covered real and projected losses for these two years but it did little to replenish the insurance reserve fund.
To make matters worse, the broker projected that if no changes were made to the plan, the cost in 2014 would be $2,050.81 per employee, per month or $2,486,588 a year. This would require another $600,000 and would likely result in significant budget cuts. It was clear to everyone that this trend is not sustainable.

Response
The consensus of the Council was that we needed to again address rapidly rising health care costs. Several ideas were floated about how to approach it. The Council was informed that the Administration was already working on amendments to the plan for consideration. It was generally agreed that the best and most appropriate course of action would be for the administration to amend the plan and for the Council to approve it as part of the normal budget process. The City Manager reported that the administration's goal was to keep the City contribution at the same level as 2013; $1,500 per employee, per month. The extra funds needed would be made up through changes in the plan and a larger employee contribution.
Since the June workshop, HR Director Andrea Petersen and Insurance broker Jeff Paxton have been working almost non-stop to come up with plan amendments that satisfy our goals. Finance Director John Li and I were brought into the conversation at crucial decision making points. The broker also called upon other experts and an actuarial as needed. Our goals going into this process were:
• Maintain the current (FY 13) City contribution of $1,500 per employee, per month in order to slow the rapid growth in City expenses for health insurance and protect other programs from budget cuts.
• Protect existing jobs and programs
• Produce health insurance plan options for employees that are still very good plans compared to industry standards and comparable cities and organizations.
• Minimize to the extent possible the financial impacts to employees.
• Compensate employees for the loss in benefits with a COLA (if possible).
• Mitigate the potential impacts of the excise tax.
• Have the amendments approved as part of the normal budget process.
Andrea and Jeff worked very hard to come up with a plan that was sustainable and at the same time minimized to the extent possible the impacts on employees. This was a very difficult task given the magnitude of the problem. I believe they reviewed and adjusted at least 80 different plans using different assumptions, utilization trends, and interpretations of the data. We started out thinking that we would do as much as we could with plan amendments

and try to minimize premiums (money deducted from paychecks). The two plans forwarded to employees ended up containing both plan amendments and increases in premiums. Significant increases in premiums was necessary because if we relied totally on plan amendments, we would have had deductibles and out of pocket max levels so high that the end result was a plan that essentially covered only catastrophic events.

We met with employees the weeks of September 23 and 30 to explain the need for changes and go over the new, proposed insurance plans. The reaction was what you might expect. Employees in general were not very happy. Many employees knew this was coming sooner or later and were not surprised. Others appreciated the fact that they have a choice between two different plans. Employees who are recent arrivals let us know that these are still good plans compared with what is available in most other places.

But, there is no way to sugar coat this. If implemented, this would be a significant reduction in employee benefits and real hit to their wallets. I don’t like reducing employee benefits and would increase them if I had the resources to do so. They deserve it. The biggest impact will be disproportionately to employees in middle income brackets who have families. From my conversations with employees, it seems like the premiums are a bigger concern than increases in deductibles and other plan amendments. This is a lot to absorb all at once and will really impact family budgets. The Council could reduce premiums or delay their full implementation but that would likely require budget cuts elsewhere, new revenues, or acceptance of the risk that there might be additional cost overruns and no replenishment of the reserve fund.

Based upon the feedback we received from employees, we reduced the new premiums 20% across the board with the exception of the premium for employee only. The plans were calculated to cover the Plan costs and replenish the reserve fund. After a lot of additional number crunching, I concluded that this reduction in premiums was an acceptable risk. If this decision turns out to be a bad move, the risk is that the reserve fund will not be replenished and further adjustments may be necessary.

It is projected that the two plan options that have been rolled out would save the City approximately $600,000 in 2014 assuming we did nothing and maintained the status quo. It is important to be clear about this though. We have not cut the City budget for health insurance. We have simply stopped the escalation in cost. The City contribution to insurance is maintained at last year’s level. The employees are making up the additional cost through plan amendments and premiums. It is hoped that these plans will result in employees thinking more like consumers and making typical consumer choices when it comes to purchasing health care services. The result could be less utilization and lower costs.

Characteristics of the New Plans

Copies of the proposed health insurance plans that have been provided to the employees are attached for your information. A copy of the current plan is also attached for comparison purposes. In short, the primary amendments contained in the new plans are:

• Two plans for employees to choose from; a “Core Plan” and a “Buy-Up Plan.”
• Unbundling of medical, dental, and vision plans.
• Higher co-pays, higher deductibles, and higher out of pocket limits.
• The preferred Provider Organization (PPO) Network will no longer be silent to the participant
• Higher premiums (payroll deductions)
• A new co-pay for office visits.
• New fees for spouses who have insurance at their own employer but choose to seek coverage by the City Plan.
• Payments / incentives to employees who “opt-out” and take coverage with their spouse’s plan.

The Process Going Forward

It is my understanding that the Council’s expectation is that the Administration will amend the health insurance plan to reduce the City’s costs, hold the City contribution to the same level as the FY 2013 Budget, and submit the package to Council as part of the normal budget approval process. We have completed our work. I believe that we have produced the best product we could given the circumstances and the limited financial resources available to us. This has been a very painful process as you might imagine. But I believe that if implemented, the new plan will slow the rapid escalation in health care costs and still provide a very good benefit to employees. I very much want to provide a COLA this year but chances are that I may not be in a position to do so in the draft budget. I would welcome any Council discussion about COLAs or providing assistance with the premiums however, you should be aware going in that this will likely mean cuts somewhere else or new revenue.

The Budget schedule calls for the City Manager to deliver the draft budget to the Council by October 14. This is the date of a regular Council meeting and the Committee of the Whole will be used for an introduction to the draft FY 2014 Budget. As part of the budget discussion, we can also review the proposed health insurance plan.

I would strongly recommend that the Council let us know early on whether it is in favor of this plan or not. Council will have two opportunities to do this, at the meeting on the 14th, when the budget is delivered to you and on October 28th, when the budget is formally introduced by ordinance. The reason for requesting that you act quickly on this is that in order to implement the new plan beginning January 1, 2014, we must start an open enrollment

period on November 1. The open enrollment period will last for two months until the end of December.
Future Recommendations
As we worked our way through this process, it became clear to me that a self- insured plan may no longer be the most cost effective approach for the City. The self-insured plan has served us very well for many years. For a long time, the City had the best coverage at the lowest cost per employee of any City. But things have changed, and changed rapidly. We now have some of the highest costs per employee. There are many possible reasons for this. The reasons include rising medical costs overall, an aging workforce, a rich plan that results in high utilization and costs, and a very small pool over which to spread the risk.
I would recommend that the City stick with the self-insured plan for at least one more year until we have more information about some of the variables and uncertainties that currently exist. As things shake out, we might recommend a variety of changes next year that could reduce costs further. For example:
• The exchanges: As you know, the Affordable Health Care Act includes insurance exchanges which are currently being established. These exchanges may provide options that are not available now.
• Private Insurance: As we amend the benefit package to get closer to industry standards, the bids we receive from the private sector insurance companies become more and more attractive. We are rapidly moving toward the time when private insurance will be cheaper than the self- insurance plan.
• Plan Utilization: The proposed plan is projected to change utilization as employees make choices about where and how to spend their money. In short, there is a possibility that utilization may decrease, thus reducing costs.
Council will also need to consider how it will respond if costs continue to escalate in future years. Will the City increase its contribution? Will the City and employees split the additional costs based upon some formula? Employees are very worried about this because they know health care costs will only continue to go up. These are discussion items we will need to have as we move forward.
Thanks for your time and consideration. As always, do not hesitate to contact me if you have any questions or comments.