SJVIA
San Joaquin Valley Insurance Authority

Meeting Location:
Fresno County Employees' Retirement Association Board Chambers
1111 H Street
Fresno, CA 93721
July 14, 2016 9:00 AM

AGENDA DATE: July 14, 2016

ITEM NUMBER: Item 14

SUBJECT: Receive Staff and Gallagher Recommendations Responding to SJVIA Cash Flow and Provide Direction for Action to be Taken

REQUEST(S): That the Board Receive and Provide Direction for Action to be Taken on the Staff and Gallagher Recommendations Responding to the SJVIA Cash Flow

DESCRIPTION:

At the SJVIA Board Meeting on April 29, 2016, your Board received separate recommendations from staff and Gallagher Benefit Services. Additionally, on March 18, 2016 staff and your Board received an Actuarial Review from Aon and Strategic Observations. At the April 29th Board Meeting, your Board directed staff and Gallagher to return with joint recommendations to the SJVIA Board. Staff met with Gallagher to discuss actionable recommendations for your Board's consideration before coming back with the renewal rates at the August Board meeting. The following recommendations are separated into staff operational recommendations and joint (staff/Gallagher) recommendations

Staff/Operation Recommendations

1. **Plan Year 2016 Cash Flow**: The County of Fresno executed a loan agreement with the SJVIA for up to $2 million on December 15, 2015. The County of Tulare had not yet executed the loan agreement, however, there was concern expressed about the County of Fresno payment cycle (paying in arrears). On July 12, 2015, the County of Fresno approved modifying the payment cycle so that the County of Fresno will be on the same payment cycle of all other entities. The County of Tulare is scheduled to consider the loan agreement on July 19th.

2. **SJVIA Rate Stability/Volatility 2017** - Although the SJVIA may secure and use the loans already referenced, the loan from the County of Fresno, requires repayment by the end of plan year 2017. Based on these terms, the next renewal must include the current years experience, re-building a reserve, and repaying the loan in full. This will certainly result in a large rate increase in plan year 2017. Staff recommends consideration of alternatives that would allow for a smoothing of these impacts over time but also work towards rebuilding the reserve, repaying any outstanding loans and ensuring the long-term financial stability of the SJVIA. Alternatives could include negotiation of a longer-term loan, or partnership with another health insurance pool. Item 16 on today's agenda requests direction from your Board to negotiate a longer repayment term to both entities.

3. **SJVIA Growth** - Based on the continuing cash flow mitigation efforts, it is recommended that the Board maintain a moratorium on new growth only until the current issues have been addressed. It is expected that the SJVIA will revisit the underwriting guidelines in collaboration with the SJVIA consultant and recommend revisions that will restore stability, rebuild a healthy reserve and require building a contingent reserve that will handle extraordinary claim years as experienced in 2015 and 2016 to date.

4. **Consultant Compensation** - The SJVIA compensates the current consultant on a "per employee per month" (PEPM) fee. This creates, at minimum, the appearance of an incentive for new business joining the SJVIA. Staff maintains the recommendation of moving from a PEPM fee schedule to a flat fee arrangement with the SJVIA consultant. As this is a completely new model, and the SJVIA is in uncharted territory, it is recommended that the SJVIA conduct an RFP for these services on a flat fee schedule. As consultant compensation is built into the SJVIA rates, staff will need to conservatively estimate what should be collected in the rates with a potential effective date of January 2017.

5. **SJVIA Excess Reserves Policy** - It is recommended that the SJVIA Board consider adopting a formal policy for reserves in excess of the IBNR. The policy may describe the amount considered conservative or healthy enough based on Actuarial studies and may allow for the contribution towards a "stabilization reserve" that would be the only reserve used for the stabilization of health premiums. The recommended policy would be created in partnership with the SJVIA consultant and adopted by your Board.

6. **<u>Develop & Maintain Risk Sharing Underwriting Guidelines</u>** – The SJVIA has enjoyed relative rate stability from 2010 to 2015. Although both the HMO and PPO contributed to stabilization and impacted the other plan at different times, it is recommended that underwriting guidelines be adjusted to take the experience of the plan or group into account. Philosophically, this will avoid making decisions based on short-term rate impact and focus on long-term rate stability. Item 15 on today's agenda reflects Gallagher's report on the preliminary 2017 renewal and includes potential direction as to the blending or unblending of each plan. Aon's report found that the Underwriting Guidelines were technically sound and strict observance to these policies should produce viable long-term rates. The primary issue Aon's report raised in this context was creation of an excess reserve policy as we have also recommended.

SJVIA staff and Gallagher have met and considered options and challenges in responding to the SJVIA cash flow situation. The following recommendations are being made to the SJVIA Board for consideration:

1. **<u>Underwriting Trend Level:</u>** - The trend for both medical and prescription cost has been an important assumption when rates are approved by your Board. Although not an exact science, trend is set based on industry projections and should be relatively consistent. To add additional review, it is recommended that the trend be presented as compared to Anthem Blue Cross and the County of Fresno/Tulare's independent consultant's recommended trend. In future years, it is recommended that trend be set before the renewal comes to your Board to remove concerns about a trend that is either too aggressive or conservative.

2. **<u>Underwriting Experience History</u>** – The SJVIA has typically used 12 months of historical claims data in underwriting the rates but using 18 months of history for the 2016. Although intended to smooth out poor experience that seemed unprecedented, it could be a less conservative approach if claims continue to trend upward. It is recommended that the SJVIA adopt and maintain either a 12 or 18 month period and maintain the method going-forward.

3. **<u>Underwriting Based on Actual Cash Flow</u>** – Although Gallagher has used premiums collected minus claims paid since inception to determine cash on hand and reserve, prospectively there will be a reconciliation with actual cash on hand. Typically, when timing issues are removed, the differences should be immaterial but it is

recommended that a "true-up" be performed every year as part of the underwriting process.

4. **Independent Actuarial Review of Rating Variables** - An independent actuarial review of all rating variables, trend assumptions and methodologies to be used during the "upcoming" renewal process is recommended. The approximate cost of this review would be $20,000. It is recommended for the Board to authorize Staff to contract for this independent review. The alternative could be using the County of Fresno and County of Tulare's independent consultants for an independent review.

5. **Stop Loss Insurance** – Stop Loss insurance should be bid at different attachment levels with a recommendation to your Board based on historical claims data and stop loss premium cost. Additionally, Gallagher will study and determine the impact of including prescription claims in stop loss coverage for the HMO. It is not currently included for the HMO but is covered for the PPO. The final determination would consider both cost and risk.

6. **High Loss Participating Entities** – Consider whether there should be special renewal action for a high-loss group rather than the blended renewal depending on the impact. Additionally, development of a validation process on new groups once the group is enrolled is recommended. Each new entity would have their risk scores re-calculated after initial enrollment to validate the assumptions made during the new business process. If demographics change dramatically, more than 10%, rates could be adjusted.

7. **Adverse Selection Considerations** – It is recommended that the SJVIA consider the impact of both contribution strategies and Kaiser penetration on potential migration. This may significantly impact underwriting assumptions. Staff and Gallagher will work with Kaiser on potential options that consider responsible assumptions and underwriting for all parties.

There are additional considerations specifically related to the 2017 renewal as recommended by Gallagher in Item 15.

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FISCAL IMPACT/FINANCING:

None

ADMINISTRATIVE SIGN-OFF:

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