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State of New Hampshire

DEPARTMENT OF ADMINISTRATIVE SERVICES
OFFICE OF THE COMMISSIONER
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Concord, New Hampshire 03301

FIS 16 123

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July 14, 2016

The Honorable Neal M. Kurk, Chairman
Fiscal Committee of the General Court
State House
Concord, New Hampshire 03301

Approved by Fiscal Committee 8/5/16 **Date**

Her Excellency, Governor Margaret Wood Hassan
and the Honorable Council
State House
Concord, New Hampshire 03301

Retroactive

REQUESTED ACTION

(1) Pursuant to RSA 14:30-a, VI and RSA 21-I:30-c, authorization is requested by the Department of Administrative Services (DAS) for the release of Active Health Benefit Reserve Funds in the amount of $379,000, retroactive to April 1, 2016, to support Active Dental ($341,000) and Active Trooper ($38,000) plan expenditures, effective upon Fiscal Committee and Governor and Executive Council approval.

(2) Pursuant to RSA 14:30-a, VI and RSA 21-I:30-c, authorization is further requested by the Department of Administrative Services (DAS) to reduce the Active Trooper Health Benefit reserve from 100% of estimated annual claims and administrative expenses to 90% of estimated annual claims and administrative expenses thereby releasing $384,400 (including the $38,000 noted in Requested Item #1) to be made available for fluctuations in plan costs that occur on a monthly basis, effective upon Fiscal Committee and Governor and Executive Council approval.

EXPLANATION

Background: Employee and Retiree Benefit Risk Management Fund and Reserves

RSA 21-I:30-e establishes the Employee and Retiree Benefit Risk Management Fund and this fund is nonlapsing and continually appropriated. RSA 21-I:30-e further requires the active and retiree health benefits to be accounted for separately such that the funds accumulated for Active employee health benefits are accounted for in the fund and used solely to pay for Active health care expenses and administrative costs. Similarly, DAS is required to account for accumulated Retiree health benefit funds separately and to use those funds solely for the purposes of paying Retiree health care expenses and administrative costs.

RSA 21-I:30-b requires the State's self-insured Health Benefit Plan to maintain a reserve equal to a minimum of 3% of estimated annual claims and administrative costs of the health plan for the active employee and retiree benefit risk management fund. While the statutory construct requires the reserve to be maintained at a retiree and active level, DAS further breaks out the accounting in the Active account into three major categories: Actives, Troopers and Dental. This separate accounting within the Active account is driven in part by the different working rates, or premium equivalents, that are deposited into the account for Active employees, Troopers and Dental health benefits. In addition, the breakout of the Active accounting also allows DAS to manage and maintain the different fund mix for the Actives, Troopers and Dental accounts. Finally, the separate accounting for Actives, Troopers and Dental benefits, also means that DAS maintains separate accounting for the reserve funds for each of these groups.

In general, DAS establishes the reserve amounts for a Fiscal Year in September after finalizing the financials for the prior Fiscal Year. In September 2016, the reserve amounts were maintained at 5% for Retirees, Actives and Dental and 100% for Troopers. After the budget passed in late September 2016, the minimum reserve amount required was reduced from 5% to 3% (Chapter 276:164, Laws of 2016).

In March 2016, DAS reduced the total Active Reserve, containing the Active, Trooper and Dental reserves, by $5.1 million total funds to comply with the Surplus Statement associated with the FY 16/17 budget and deposited $1.8 million into the General Fund, $652,000 into the Highway Fund and $53,900 into the Fish and Game Fund. See FIS 16-085, Informational Item. DAS did not reduce the Retiree reserve at that time because it was fiscally prudent to maintain those reserves at the 5% level based on recent experience with the volatility of prescription drug costs and the known deficit in the Retiree Health Benefits account for the biennium FY16/17.

After complying with the Surplus Statement, DAS used available surplus funds in the Active and Trooper accounts to return reserve levels to 5% and 100% respectively of projected annual claims and administrative expenses for those two groups. See FIS 16-033, Informational Item. DAS determined at that time that a 3% reserve was sufficient for the Dental account since the dental benefit provided to Active and Trooper plan participants is capped on an annual basis.

In the aggregate, the Active reserves consisting of the Active, Trooper, and Dental reserves, equals $13,355,000, or approximately 7% of the total Active (Active, Trooper and Dental) projected FY16 claims and administrative expenses. Thus, the 7% total Active reserve exceeds the minimum reserve amount of 3% that DAS is required to maintain pursuant to RSA 21-I:30-b, I(a).

Administering a Health Benefit Plan

In any given month, the Health Benefit Plan brings in revenue from the working rates paid by agencies and others authorized to participate in the plan and pays medical, prescription drug and dental claims expenses. Revenues can vary from month to month based on headcount and the number of pay periods in given a month. Claims expenses also vary from month to month depending on the health and dental care needs of plan participants. Therefore, on a monthly basis, revenues and claims expenses can increase or decrease the surplus on hand and the separate accounts may dip into a reserve to pay for regular monthly program expenses should those expenses prove to be high and if there are insufficient surplus funds, or operating capital, on hand.

The third party administrators for the medical, prescription drug and dental benefits pay the health benefit expenses up front and then invoice DAS for claims and administrative expenses. In general, the contracts with these vendors require DAS to pay the invoices within five or seven days. Under these circumstances, the Risk Management Unit places a priority on processing and paying vendor invoices.

The Trooper and Dental Accounts

In FY 16, the DAS dipped into the Trooper reserve account in the approximate amount of $38,000 and into the Dental reserve account in the amount of approximate amount of $341,000 in order to pay normal claims and administrative expenses. This was because in the past two years, the Health Benefit Program account surpluses have been exhausted to satisfy a Dental surplus rate holiday, a Collective Bargaining surplus payout, and the statutory reserve reduction as required by the FY16 Surplus Statement requirements. A summary of these reductions is found in the following chart.

Active Health Benefit Funds Returned to Agencies and Employees FY15 & FY16					
	Actives	**Troopers**	**Dental**	**Total**	**Total General Funds**
FY15 CBA Payout	$7,300,000	$300,000	$0	$7,600,000	$0
FY15 Dental Holiday	$0	$0	$1,400,000	$1,400,000	$423,000
FY16 Statutory Reserve Reduction	$4,800,000	$100,000	$200,000	$5,100,000	$1,800,000
Totals	**$12,100,000**	**$400,000**	**$1,600,000**	**$14,100,000**	**$2,223,000**

In retrospect, the health benefit plan has never been run on as thin margins as it has in the last year. In FY 15, the Collective Bargaining Agreements required the payout of $7.3 million in surplus funds to Active employees and the payout of $300,000 in surplus funds to Trooper employees. In FY 15, in compliance with FY 2014 audit of the Internal Service Fund (Fund 60), DAS conducted a Dental working rate holiday to reduce the surplus funds in the Dental account in the total amount of $1.4 million, returning $423,000 to the General Fund. In FY 16, as discussed above, DAS reduced the statutory reserves in the Active, Trooper and Dental accounts in the total amount of $5.1 million and then used available surplus funds to restore reserve levels for Actives and Troopers to 5% and 100% respectively. These three actions in combination reduced operating surpluses, particularly in the Trooper and Dental accounts, to extremely low levels. Typically, DAS administers the health benefit plan with some level of surplus in the various accounts and these surpluses afford DAS the flexibility to administer the plan and pay TPA invoices without having to consider using reserve funds. The detail for the Trooper and Dental accounts follows.

<u>A. The Trooper Account</u>

In FY 15, the Trooper account surplus was paid out to NHTA union members as part of the FY14/15 NHTA Collective Bargaining Agreement. Thereafter, the Trooper account status hovered around a zero surplus balance from month to month. In the fall of 2015, the FY16 budget passed and DAS planned to implement an employee and employer health and dental holiday to satisfy the statutory reserve reduction and to comply with the surplus statement amounts. The reserve reduction was applied to Actives, Troopers, and Dental accounts.

During the winter of 2016, the Trooper account had a surplus of approximately $115,000. After the reserve holiday and restoring the Trooper reserve to 100% of projected annual claims and administrative expenses, the surplus in April 2016 was approximately $28,000. In May and June 2016, the Trooper account experienced higher than average claims expenses. In May 2016, the prescription drug claims expense was $32,000 more than on average; in June 2016, the medical claims expense was approximately $45,000 more than on average. As of June 30, 2016, without a sizeable surplus or operating cash on hand to pay these higher than average claims expenses, the trooper account has used approximately $38,000 of its reserve fund.

<u>B. The Dental Account</u>

The Dental surplus had grown slowly since Calendar Year 2012 and was approximately $1.5 million as of April 30, 2015. In May 2015, in an effort to minimize surplus on hand and satisfy the recent FY14 LBA Audit finding about surplus management, DAS implemented a Dental Working Rate Holiday for employees and employers. The holiday spent down approximately $1.4 million of the $1.5 million Dental surplus and returned approximately $1.2 million in FY15 to state agencies, of which about $423,000 were general funds. Thereafter, similar to the Trooper account, the FY 16 reserve reduction was applied to the Dental reserve. When DAS applied the FY 16 reserve reduction to the Dental account, there was a surplus of approximately $140,000 in the account. Following this reserve reduction, DAS maintained the Dental reserve at 3% of annual projected claims and administrative expenses.

In general, Dental benefits trends are less volatile compared to health and prescription drug cost trends and the risk associated with the Dental account is minimal because there is a cap on the annual employee dental benefit. However, while DAS was planning and implementing the reserve reduction, a concurrent change in the dental plan annual benefit limits began affecting the rate of spending in the dental account.

Pursuant to the Collective Bargaining Agreements, effective January 1, 2016, the annual cap on dental benefits increased from $1,500 to $2,000. This increase was funded by increases in employee premium contributions. However, with a capped annual benefit, it is not uncommon for plan members to access services and to exhaust the plan year limit on benefits early in the year. In terms of plan year expenses, this often has the effect of front-loading plan year costs that taper as the plan year progresses. With the convergence of the Dental holiday, reserve reduction and increased annual Dental benefit amount, the front loading of claims expenses has been drawn out into the light. DAS expects monthly dental revenues to exceed expenses as we continue through the calendar year, allowing the replenishment of the Dental reserve.

Retroactive Request

It is only since DAS requested and received the Department of Justice opinion on use of the reserves to pay for the retiree health long term study and to pay for any projected deficit in the retiree health account (See companion item, Requested Action on Retiree Health) that DAS realized that while it is a proper use of reserve funds to pay for unexpected shortfalls or losses, it should seek Fiscal Committee and Governor and Executive Council approval to spend funds from the reserves.

This request is retroactive for two reasons. As stated above, DAS only recently learned about the nuance between the proper use of reserve funds and the required Fiscal Committee approval mechanism to use reserve funds to pay the bills. Moreover, in the course of running a health care business, DAS placed appropriate importance and priority on complying with the payment terms of its contracts with the health benefit plan's third party administrators. For this reason, DAS is requesting the release of $379,000 from the Active reserves account, $38,000 from the Trooper reserves and $341,000 from the Dental reserves, retroactive to April 1, 2016, the point in time prior to reserves falling below the established levels for these active sub-groups.

DAS further requests the Fiscal Committee and Governor and Executive Council approve the reduction in the Trooper reserve from 100% of estimated annual claims and administrative expenses to 90% of estimated annual claims and administrative expenses, or in the amount of $384,400. This $384,400 reduction in the reserve will leave the Trooper account with a surplus in the amount of $346,400. As stated above, the maintenance of a reasonable surplus allows DAS the flexibility to pay its TPA invoices given the unpredictability of monthly revenues and claims expenses.

In addition, DAS will be using $541,000 of the $4.695 million surplus in Active account to address the cash flow issues in the Dental account. DAS will use $341,000 of the $541,000 to restore the Active Dental reserve to 3% of estimated annual claims and administrative expenses. This will leave a $200,000 surplus in the Dental account for payment of monthly dental invoices. As we progress through the plan year, monthly Dental revenues will begin to exceed monthly Dental claims expenses and DAS will be able to fully restore the $541,000 to the Active account. DAS will account for this $541,000 separately until such time as the $541,000 is fully restored by the Dental account to the Active account, and DAS will report to the Fiscal Committee in its regular bi-monthly Informational Item about this accounting.

The below chart demonstrates updated reserve and surplus amounts based on the reduction of the Trooper reserve to 90% of estimated annual claims and administrative expenses and the use of the $541,00 in Active surplus to support the Dental account.

Current Reserve Detail				
	Actives	**Trooper**	**Dental**	**Total**
Total FY16 Projected Expenditures	$183,170,000	$3,844,000	$11,100,000	$198,114,000
Current Statutory Reserve Level	$9,159,000	$3,844,000	$352,000	$13,355,000
Percentage	*5%*	*100%*	*3%*	*7%*
Amount of Reserve Spent as of 6/30/2016	$0	($38,000)	($341,000)	($379,000)
Reserve Balances as of 6/30/16	$9,159,000	$3,806,000	$11,000	$12,976,000
Surplus Balances as of 6/30/16	$4,695,000	$0	$0	$4,695,000
Available Surplus Funds to Pay Claims as Necessary	($541,000)	$0	$0	($541,000)
Decrease Trooper Reserve by 10%	$0	$384,400	$0	$384,400
Replenishment of Dental Reserve and Operating Capital	$0	$0	$200,000	$200,000
Restore the Dental Reserve at 3%	$0	$0	$341,000	$341,000
Updated Surplus Balances as of 6/30/16	$4,154,000	$346,400	$200,000	$4,700,400
Updated Reserves Balances as of 6/30/16	$9,159,000	$3,459,600	$352,000	$12,970,600
Percentage	*5%*	*90%*	*3%*	*6%*

I am available to address any questions you may have.

Respectfully Submitted,

Vicki V. Quiram

Vicki V. Quiram
Commissioner

Attachment: Letter from Department of Justice Dated July 18, 2016.

ATTORNEY GENERAL
DEPARTMENT OF JUSTICE

33 CAPITOL STREET
CONCORD, NEW HAMPSHIRE 03301-6397

JOSEPH A. FOSTER
ATTORNEY GENERAL

ANN M. RICE
DEPUTY ATTORNEY GENERAL

July 18, 2016

Vicki Quiram, Commissioner
Department of Administrative Services
25 Capitol Street
Concord, NH 03301

Dear Commissioner Quiram:

This letter addresses the use of the two funds related to the health benefit program – the "Reserve Fund" established by RSA 21-I:30-b and c, and the "Management Fund" established by RSA 21-I:30-e.

There are two issues: 1) the appropriate use of reserve funds; and 2) the mechanism by which those funds can be spent.

Appropriate Use of Reserve Funds

RSA 21-I:30-b requires a reserve of three percent of claims and administrative costs as well as "the unpaid portion of ultimate expected losses, including incurred but not reported claims, and related expenses incurred in the provision of benefits for eligible participants..." (RSA 21-I:30-b, I(b)). The Reserve Fund is established in RSA 21-I:30-c which states, in pertinent part, "a reserve fund shall be established to protect the state from unexpected losses and self-insured losses and related expenses incurred in the provision of such a plan."

RSA 21-I:30-b, I(b) also states that "if the state self-insures for more than one employee group plan, a reserve meeting the requirements of this paragraph must be maintained for each plan." You have indicated that a reserve is accounted for separately for each of the following groups – active employees, troopers, retirees and dental benefits. The trooper and dental accounts are for "active" benefits.

The primary function of a self-insured health benefit plan is the payment of medical claims. As discussed below, these claims are typically paid from the Management Fund. However, if the Management Fund could not cover claims it would be appropriate to use the Reserve Fund, as this would be an unexpected or self-insured loss and an expense incurred in the provision of a self-insured plan.

You have also specifically inquired about the funding of a study focused on the long term status (financial and otherwise) of the retiree health plan. As this study would be done with the

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objective of identifying options to maintain a financially viable plan for the benefit of retirees, it is our opinion that it would constitute a related expense incurred in the provision of the plan.

Mechanism to Spend Funds

While RSA 21-I:30-b discusses the establishment and use of the fund, RSA 21-I:30-c establishes the fund itself and states:

"In the event that the medical and surgical benefits under RSA 21-I:30 are provided using a self-funded alternative, a reserve fund shall be established to protect the state from unexpected losses and self-insured losses and related expenses incurred in the provision of such a plan. Such reserve fund shall be administered by the commissioner of administrative services and shall be nonlapsing."

RSA 21-I:30-e establishes the Management Fund to pay for active and retiree health care expenses and any administrative costs related thereto. That fund is nonlapsing and continually appropriated (RSA 21-I:30-e(I)).

As you know, a fund that is nonlapsing does not have its contents revert back to the general fund at the end of the fiscal year or biennium. Both funds are nonlapsing. However, only the Management Fund is "continually appropriated." This language has been consistently interpreted by Administrative Services and the Legislative Budget Assistant to mean that the funds have been authorized by appropriation of the legislature to be spent even if in excess of estimated levels. The Reserve Fund is not continually appropriated and, thus, a request of the Fiscal Committee, and to the extent necessary the Governor and Executive Council, to transfer or expend the funds would be necessary.

As we have discussed, in 2015, the Legislature authorized a reduction in the Reserve Fund from five percent to three percent in House Bill 2. This was, in effect, legislative authorization to transfer the two percent excess out of the Reserve. I understand that a decision was made to keep the Active and Retiree Reserve Funds at five percent. The Dental and Trooper reserves are kept at three percent and 100 percent respectively. However, as House Bill 2 is so recent and we are in the biennium which it covers, if the Department now wishes to reduce those amounts below five percent and release the funds for use pursuant to RSA 21-I:30-b and c, you could reasonably do so without further permission, based on the House Bill 2 authorization. However, absent legislative approval such as House Bill 2, or for use of funds from a reserve account that is already maintained at three percent, it is our opinion that releasing those funds for use would require Fiscal Committee approval.

I hope this analysis is helpful in your administration of the health benefit plan. Please do not hesitate to contact me with further questions.

Sincerely,

Christen Lavers
Assistant Attorney General