

Preliminary Performance Review

**Public Employee Insurance Agency
Finance Board**

**The PEIA Finance Board now has a Proactive
Outlook Rather than a Reactive Outlook as
in the Past**



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John Sylvia
Director

August 4, 2003

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

The Honorable J.D. Beane
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 Employee Insurance Agency Finance Board*, which will be presented to the Joint Committee on Government Operations on Monday, August 4, 2003. The issue covered herein is "The PEIA Finance Board Now Has A Proactive Outlook Rather Than A Reactive Outlook As In The Past."

We transmitted a draft copy of the report to the Public Employee Insurance Agency Finance Board on July 16, 2003. We held an exit conference with the Finance Board on July 23, 2003. We received the agency response on July 23, 2003.

Let me know if you have any questions.

Sincerely,

Handwritten signature of John Sylvia in cursive script.
John Sylvia

JS/wsc

Joint Committee on Government and Finance

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Executive Summary

Issue 1: The PEIA Finance Board now has a Proactive Outlook Rather than a Reactive Outlook as in the Past.

The purpose of the PEIA Finance Board is **to bring financial stability to the Public Employees Insurance Agency (PEIA)**. In 2001, the Legislative Auditor's Office issued a report that indicated that the Board was not accomplishing its purpose. To summarize, the 2001 report found the following:

- i For each fiscal year between 1994 and 1999, the Board approved financial plans that expected large deficits.
- i The Board relied on reserves accumulated in previous years to balance each year's financial plan. By 1997, the PEIA exhausted plan reserves and relied on additional legislative appropriations.
- i Other reasons for the Board's inability to provide financial stability were a reluctance to increase premiums on employees and retirees, and a lack of plan objectives.

This current performance review finds that legislative reform and internal changes by the Finance Board are advancing the Board in accomplishing financial stability for the PEIA. The Legislature has mandated increases in premiums to reach a cost sharing of 80% for the employer and 20% for employees. The Legislature also required the Board to develop a five year financial plan for distribution to the Governor and the Legislature. The Board's most recent financial plan predicts sufficient premiums to satisfy claims. Despite these positive signs, continuing increases in health care costs, and the possibility of other unforeseen circumstances, could pose a risk to the reserve fund. Consequently, both the PEIA Finance Board and the Legislature need to monitor the Board's financial plans.

Review Objective, Scope and Methodology

This preliminary performance review of the West Virginia Public Employees Insurance Agency Finance Board (Board) is required and authorized by the West Virginia Sunset Law, Chapter 4, Article 10 of the West Virginia *Code*, as amended.

Objective

The objective of this review was to determine if the Board was operating in an effective and efficient manner.

Scope

The scope of this evaluation covers the period from June 2000 to present.

Methodology

The methodology included but was not limited to interviews, conversations and correspondence with the Board. Every aspect of this review complied with Generally Accepted Government Auditing Standards (GAGAS).

Issue 1

Issue 1: The PEIA Finance Board now has a Proactive Outlook Rather than a Reactive Outlook as in the Past.

Issue Summary

According to WV Code §5-16-5, the purpose of the PEIA Finance Board is **to bring financial stability to the Public Employees Insurance Agency (PEIA)**. However, in 2001, the Legislative Auditor's Office issued a report that indicated that the Board was not accomplishing its purpose. For each fiscal year between 1994 and 1999, the Board approved financial plans that expected large deficits. The Board relied on reserves accumulated in previous years to balance each year's financial plan. By 1997, the PEIA exhausted plan reserves and relied on additional legislative appropriations. Other reasons for the Board's inability to provide financial stability were a reluctance to increase premiums on employees and retirees, and a lack of plan objectives.

This current performance review finds that legislative reform as well as internal changes by the Finance Board are advancing the Board in accomplishing financial stability for the PEIA. The Legislature has mandated increases in premiums to reach a cost sharing of 80% for the employer and 20% for employees. The Legislature also required the Board to develop a five year financial plan for distribution to the Governor and the Legislature. The Board's most recent financial plan predicts sufficient premiums to satisfy claims. Despite these positive signs, continuing increases in health care costs, and the possibility of other unforeseen circumstances, could pose a risk to the reserve fund. Consequently, both the PEIA Finance Board and the Legislature need to monitor the Board's financial plans.

Reliance on Plan Reserves and Deficit Spending

The primary finding of the two PERD reports indicated that the Board was relying on plan reserves and not participant premiums to meet current year costs.

*Plans for 1994, 1995, 1996 and 1998 **expected** claim expenses to exceed **expected** premium revenues. When other expenses are included,... the result has been forecasted deficits for current operations in six of the last seven years. **These imbalanced financial plans for current operations were approved and implemented by the Board.** In order to bal-*

ance the expected deficits for current operations, the Board relied on existing surpluses accumulated in previous years.

The result of this reliance on plan reserves to fund current operations was a reduction of reserves until 1997, when all reserves accumulated from previous years were exhausted. In 1997, the PEIA had a deficit of over \$8 million and another deficit of \$15 million in 1998. Each time the reserves were exhausted and the PEIA was faced with a deficit, the Board relied on the Legislature to provide supplemental appropriations instead of raising participant premiums.

Legislature Imposes Changes on PEIA Finance Board

In December 1999, the Legislative Joint Select Committee Studying the PEIA received the Segal Report. The Segal Report indicated the current condition of the PEIA in comparison to other states and private sector plans. According to the Segal Report,

The Legislature has been called upon for additional resources late in each of the past few fiscal years when the Administration has notified the Legislature that the plan is in danger of running out of money in future years at its current funding level. In each case, the Legislature has responded to the Administration's request by reallocating funds to the program or by approving the expenditure of additional funds....As a result, the State now finds itself faced with tough decisions on how to continue to fund the PEIA program at its present level without either directly affecting its support of other critical state programs or raising taxes to pay for this program.

House Bill 4800

House Bill 4800 passed March 11, 2000 and dramatically changed the purpose and structure of the PEIA reserve fund. Prior to HB 4800, the reserve fund was to receive monies on a monthly basis if premiums exceeded costs. The reserve fund was a reactionary measure to offset future costs. HB 4800 made the reserve fund proactive. According to HB 4800, beginning with fiscal year 2002 and for each succeeding fiscal year, the PEIA Finance Board is to transfer ten percent of projected total plan costs for that fiscal year into the reserve fund. Also, the PEIA Finance Board must submit approved financial plans to the Governor and the Legislature. HB 4800 also communicated to the

PEIA that the responsibility for maintaining the reserve fund was shared by the PEIA and not just the Legislature.

Senate Bill 1003

Senate Bill 1003 passed April 23, 2001. According to SB 1003, beginning with the financial plan for fiscal year 2002, the PEIA shall raise premiums for employees. According to the Chief Financial Officer of the PEIA,

*The Board underwent changes that are not only reflected in their finance plans but by new statutory requirements and current plan stability. On April 20, 2001 the West Virginia Legislature passed SB 1003 requiring financial plans commencing on FY 2003 to include incremental adjustments on contributions that will result in aggregate cost sharing percentages of 80% for state employers and 20% for state employees as of FY 2007. This is a significant step in documenting what is expected each year from the state employer and employees as recommended by PERD....**By approving plans with premium increases, the Board is not relying on existing reserves to offset plan costs.** (emphasis added)*

An additional change brought about by SB 1003 was a long term reporting requirement. According to SB 1003 the PEIA Finance Board must develop projected financial plans for a period not to exceed five years and submit those plans to the Governor and the Legislature. These plans provide the Legislature with information on how proposed premium increases will affect the long term financial stability of the PEIA.

Current PEIA Financial Plans

As a result of the Legislative reform, the PEIA Finance Board is no longer approving deficit spending or relying solely on plan reserves to balance financial plans. The most current approved financial plan indicates sufficient premium revenues to cover current claims for fiscal years 2003 - 2007. Table 1 shows the projected premium revenues, expenses, and the projected reserve fund surplus/(deficit) after all other expenses have been deducted.

Fiscal Year	Premium Revenues	Claims Expenses	Fiscal Year Surplus/(Deficit)*
2003	\$491 million	\$412 million	\$8 million†
2004	\$562 million	\$476 million	\$10 million
2005	\$646 million	\$554 million	\$10 million
2006	\$749 million	\$660 million	\$10 million
2007	\$870 million	\$778 million	\$10 million

†Source: PEIA Financial Plan for FY 2003-2007

*Indicates Surplus/(Deficit) of Premium Revenues plus all other transfers and other revenues, less Claims Expenses and all other expenses.

†The PEIA's May actuarial report now projects the FY 2003 surplus to be approximately \$30 million.

PEIA Finance Board Efforts for Financial Stability

In addition to Legislative reform, the PEIA Finance Board has undertaken a myriad of reforms internally to assure financial stability to the PEIA. The internal changes include but are not limited to the following:

- ii **Change in Pharmacy Benefits Provider** - The PEIA changed pharmacy benefits managers on July 1, 2002 to obtain a more favorable drug rebate program;
- ii **Education Targeting Unnecessary Utilization** - Educational materials were sent to selected plan members with an increased utilization of emergency room services as well as out of state care providers to explain the cost savings which could incur if these individuals would see their primary care physician, in state provider, or out of state network provider;
- ii **Kidney Disease Management Program** - The plan is preparing to enter contractual agreement with a new kidney disease management program. This contractual agreement is expected to save the plan money for those members that are candidates for dialysis, or are already receiving dialysis;
- ii **AIMS** - Accessible Intelligent Medication Strategies. AIMS is a program of academic detailing, or educational outreach. The purpose is to keep doctors informed of the benefits of prescribing one prescription

versus another. According to the Director of the PEIA Finance Board, *“We want to do this without restricting public access to effective medications or imposing an undue burden on physicians. Academic detailing is a proven method...that will enable cost-effective prescribing.”* (emphasis added)

- ii **Medicaid Transfer** - According to the PEIA Finance Board, *“Additionally, a major cost saving maneuver was implemented for FY 2003 by the agency to transfer the Department of Administration’s PEIA Reserve Balance to Medicaid to receive federal matching. This has resulted in estimated savings to PEIA of \$10.5 million to \$11.5 million without negatively impacting the providers;”* and,
- ii **Tobacco Cessation Incentive** - In FY 2002 the PEIA Finance Board implemented a tobacco user discount to encourage tobacco cessation. Table 2 shows the estimated numbers for those utilizing the tobacco free discount for FY 2002, FY 2003, and FY 2004.

Plan Type	Tobacco Free Count 2002	Discount FY 2002	Tobacco Free Count 2003	Discount FY 2003	Tobacco Free Count 2004	Discount FY 2004
Single	341,580	\$1,707,900	312,576	\$3,125,760	321,396	\$4,820,940
Family	406,368	\$4,063,680	380,844	\$7,616,880	391,380	\$11,741,400
Total		\$5,771,580		\$10,742,640		\$16,562,340

* Source: PEIA Financial Department

PEIA Finance Board Members Become Proactive

In addition to the plan initiatives that the PEIA Finance Board has instituted to make the plan more proactive, it appears that the members of the Board itself have adopted a new proactive approach. According to the Chief Financial Officer of the PEIA,

The Board now meets monthly instead of quarterly. The Board now receives a significant amount of information each month to monitor the plan and its performance. This information includes the weekly claims inventory reports of Acordia and

*the PBM management reports. This has helped increase awareness of the volatility of the healthcare industry and the necessity of staying ahead of any possible detrimental trends. **The Board and the agency are evolving into more proactive entities. This is crucial in maintaining fiduciary stability in a plan this size.** The Agency developed a strategic plan that was released April 15, 2002. Although not inclusive, these were some of the actions as a result of the PERD review. (emphasis added)*

Board and Legislature Need to Continue to Monitor Financial Plans Closely

Despite the increased efforts of the Finance Board to bring financial stability to the PEIA, and the predicted surplus in the current financial plans, the Finance Board and the Legislature need to continue to monitor the Board's financial plans closely for any unexpected changes. For example, a December 1999 financial plan predicted modest reserve growth for plan year 2002. However, in reality, the PEIA netted a \$15 million loss in 2002. According to the Chief Financial Officer of the PEIA, this loss was a result of the following:

Higher than anticipated claim costs were the main reason. The premium increases passed in December 2000 were not enough to offset actual claims increases. This was known and estimated to be about \$7 million as of June 30, 2001 per the premium deficiency reserve booked for FY 2001. However, the financial plan was already developed for FY 02 at this point and the anticipated loss was not enough to warrant an emergency increase in premiums. It was actually higher at \$15 million.

The current financial plan once again predicts a modest growth for the PEIA reserve fund and sufficient premiums to meet plan costs. However, health care costs are continually rising and could pose a risk to the PEIA's predicted financial stability. According to the Segal Report, 1996 national health care costs were approximately \$1.035 trillion. In 2007, it is predicted to double to over \$2 trillion. Furthermore, the Segal Report indicates that as the population ages, utilization of health care will also increase. West Virginia ranked third among all states in 2000 in percentage of population age 65 and older. Both the Segal Report and the PEIA Finance Board predict that sometime in the future the PEIA will cover more retirees than active employees. Given these factors, it is imperative for the PEIA Finance Board not to take the current

predicted growth of the reserve fund for granted.

Conclusion

The PEIA Finance Board was clearly not bringing financial stability to the PEIA when the Legislative Auditor's Office reported its findings in 2001. The Board was reluctant to raise premiums and the Board was approving deficit spending plans, and relying on the Legislature to offset plan costs with additional appropriations when reserves were exhausted. Clearly, the PEIA Finance Board has shown significant improvement. Many of the necessary changes were accomplished through the passage of significant legislation. In addition, the PEIA Finance Board has made numerous changes internally to contain costs.

It is difficult to tell whether or not the changes made through legislative reform and internal reform will indeed make the PEIA financially stable. The most recent financial forecast predicts a modest growth for the PEIA reserve fund and sufficient premiums to meet plan costs. However, this prediction was also made in 1999 when the Board released the 2001 to 2004 financial plan. The 1999 prediction of reserve growth for plan year 2002 never materialized and by 2001, the PEIA was expecting a plan loss of \$8 million for 2002. Plan Year 2002 resulted in a plan loss of over \$15 million. Only over time can it be determined whether or not the Finance Board is adding stability. What is clear is that **both the PEIA Finance Board and the Legislature will need to monitor the Board's financial plans.**

Appendix A: Transmittal

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John Sylvia
Director

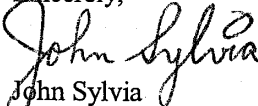
July 16, 2003

Mr. Tom Susman, Chairman
PEIA Finance Board
Building 5
Room 1001
1900 Kanawha Blvd. East
Charleston, WV 25305-0710

Dear Mr. Susman:

This is to transmit a draft copy of the Preliminary Performance Review of the West Virginia Public Employees Insurance Agency Finance Board. This report is scheduled to be presented at the August 3-5, 2003 interim meeting of the Joint Committee on Government Operations. It is expected that a representative from your agency be present at the meeting to orally respond to the report and answer any questions the committee may have. If you would like to schedule an exit conference to discuss any concerns you may have with the report between Thursday, July 17, 2003 and Tuesday, July 22, 2003, please notify us. We need your written response by noon on July 23, 2003 in order for it to be included in the final report. If your agency intends to distribute additional material to committee members at the meeting, please contact the House Government Organization staff at 340-3192 by Thursday, July 31, 2003 to make arrangements.

We request that your personnel treat the draft report as confidential and that it not be disclosed to anyone not affiliated with your agency. Thank you for your cooperation.

Sincerely,

John Sylvia

Joint Committee on Government and Finance

Appendix B: Agency Response

Bob Wise
Governor



Tom Susman
Director

WV Toll-free: 1-888-680-PEIA • Phone: 1-304-558-7850 • Fax: 1-304-558-2516 • Internet: www.wvpeia.com

July 23, 2003

John Sylvia, Director
West Virginia Legislature
Performance Evaluation and Research Division
Building 1, Room W-314
1900 Kanawha Blvd, E.
Charleston, WV 25305

Dear Mr. Sylvia:

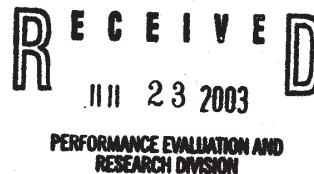
As Chairman of the PEIA Finance Board (Board), I have reviewed the report and will provide copies to the members for their review. Regardless of various policies and procedures implemented to mitigate the effects of unfavorable health and prescription drug claim trends, diligent oversight by all stakeholders must always be performed. The Board will continue to provide vital financial information to the Legislature at monthly legislative interim meetings for this purpose.

The Board will continue to develop financial plans that maintain the financial stability of the plan. Further, all potential mechanisms that may provide the plan cost savings, yet maintain the level of benefits PEIA policyholders expect, will continue to be explored. Thank you for the opportunity to respond to this report.

Sincerely,

A handwritten signature in black ink, appearing to read "Tom Susman".

Tom Susman, Chairman
PEIA Finance Board



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