



# COMMONWEALTH of VIRGINIA

## *Department of Human Resource Management*

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October 15, 2015

The Honorable Terry McAuliffe, Governor, Commonwealth of Virginia  
The Honorable J. Chris Jones, Chairman, House Appropriations Committee  
The Honorable Walter A. Stosch, Co-Chairman, Senate Finance Committee  
The Honorable Charles J. Colgan, Co-Chairman, Senate Finance Committee

Subject: Report on the Impact of Renewal Cost on Employee and Employer Premiums

The attached report is pursuant to Chapter 665, Item 81.G. of the 2015 Virginia Acts of the General Assembly.

Please contact me if there are any questions.

Sincerely,

A handwritten signature in cursive script that reads "Gene Raney".

Gene Raney  
Director, Office of Health Benefits

cc: The Honorable Paul J. Reagan, Chief of Staff, Office of the Governor  
The Honorable Nancy Rodrigues, Secretary of Administration  
Sara R. Wilson, Director, Department of Human Resource Management

**REPORT ON THE IMPACT OF RENEWAL COST ON  
EMPLOYEE AND EMPLOYER PREMIUMS**

This report is submitted as required by Chapter 665, Item 81.G. of the 2015 Virginia Acts of the General Assembly, which states:

*The Department of Human Resource Management shall report to the Governor and Chairmen of the House Appropriations and Senate Finance Committees, by October 15 of each year, on the renewal cost of the state employee health insurance program premiums that will go into effect on July 1 of the following year. This report shall include the impact of the renewal cost on employee and employer premiums and a valuation of liabilities as required by Other Post-Employment Benefits reporting standards.*

**Other Post-Employment Benefits**

Regarding a valuation of liabilities as required by Other Post-Employment Benefits reporting standards, Other Post-Employment Benefits (OPEB) valuation reports are due every other year unless there have been material changes in underlying assumptions. Our last report was provided October 17, 2014 and the next will be prepared mid-2016.

**Summaries of Rating Projections**

**Overview**

The following information summarizes the renewal cost of the state employee premiums for fiscal year 2017 that will go into effect on July 1, 2016, and the key drivers of FY 2017 projections compared to the FY 2016 rates. The information package complies with all of prior actuarial methods / procedures endorsed and approved by the APA audit report of October 2011.

The three charts shown in this report provide summaries of rate projections for FY 2016 through FY 2018 and these include:

- Recast FY 2016 Projection
- FY 2017 Projection
- FY 2018 Projection

Each chart includes three scenarios (A, B, and C). Scenario A represents the most aggressive projection, Scenario B the most likely projection, and Scenario C the most conservative projection.

It is important to note that each scenario represents a reasonable actuarial outcome. Historically this range has been utilized in final budget setting based on the Commonwealth's fiscal priorities and internal assessment of the risk to be assumed for the applicable budget cycle.

Each chart shows the baseline rates under the three scenarios. Separate tables at the end of the document provide the underlying claim trend assumptions based on the IBNR valuation completed mid-September and Aon's current outlook for future trends.

- Projected Cost per Contract Unit is synonymous with *actuarial rate or per contract unit per month (PCUPM* for these projections, represent a per-employee equivalent unit cost and serve as the actuarial baseline for cost projections in the requested three FY iterations). The assumptions inherent in the contract unit measure take into account the relative cost of each dependent class (spouse or child) relative to an employee. The per-employee or contract unit equivalent is the "base" level of exposure for rating purposes. This method was approved by the APA actuarial methods audit report of October 2011.
- The COVA Care Basic plan is shown because it is the basis for employer contributions. This chart shows rate projections and percentage increases or decreases from each fiscal year's premium rates per contract unit.
- Claim trend analysis inherent in Aon's future trend outlook includes detailed claim patterns to forecast future inflationary impact. The latter includes: price inflation; utilization rates of health care providers; government (Medicare/ACA) cost shifting; plan changes; and, other current factors influencing health provider cost. Historical claim experience for the Commonwealth is also considered when establishing the estimated trends.
  - The updated trend analysis is based on review of the most recent 36\_months of claims and Aon forward looking trends.
  - The trend tables for Fiscal Years 2017 and 2018 are shown in the last section of this document. Overall Scenario B health plan trend is 7.5% and 8.0% respectively for these years.

## Recast FY 2016 Projection

The recast is the first step in the three fiscal year projection process required by the Commonwealth. It provides an early estimate of how actual current FY costs compare to previously projected costs/rates. The recast is based on claim data through June 2015, consistent with the IBNR valuation completed in mid-September. This analysis also provides an updated important baseline for projecting rates for FY 2017.

- The chart compares the recast actuarial rate for FY 2016 with the previous year's FY 2016 rate projection (and the claim data used to establish the FY 2016 rates).
  - This recast projection utilized an additional year of claim experience and the updated trend outlook.
  - The chart shows the recast comparison for each plan component and rolls it up to the total. For Scenario B, Medical is -0.2%, Dental -0.9%, Rx +3.2%, MISA/Behavioral Health +28.4%. The overall total, based on the weighted value of each component's relativity to premium is +1.0%, or very close to the previous year's projection.
- The recast vs. FY 2016 rate comparison is shown for each component of the COVA Care Basic rate. However, the Total percentage increase is the critical cost impact factor in the table.

### Commonwealth of VA Summary of FY2016 Rating Projections Actives, COBRAs, and Retirees without Medicare

|   | Enrollees(@July15) | Medical      | Dental       | Rx Drugs    | Subtotal     | MISA         | Total        |
|---|--------------------|--------------|--------------|-------------|--------------|--------------|--------------|
| FY2016 COVA Rates                       | 83,159             | \$447.28     | \$19.90      | \$131.23    | \$598.42     | \$11.02      | \$609.44     |
| FY2016 Projected Cost per Contract Unit |                    |              |              |             |              |              |              |
| Scenario A                              |                    |              |              |             |              |              |              |
| COVA Care                               | 83,159             | \$442.20     | \$19.55      | \$133.34    | \$595.09     | \$14.03      | \$609.12     |
| <b>% Increase</b>                       |                    | <b>-1.1%</b> | <b>-1.8%</b> | <b>1.6%</b> | <b>-0.6%</b> | <b>27.4%</b> | <b>-0.1%</b> |
| Scenario B                              |                    |              |              |             |              |              |              |
| COVA Care                               | 83,159             | \$446.19     | \$19.72      | \$135.48    | \$601.39     | \$14.15      | \$615.55     |
| <b>% Increase</b>                       |                    | <b>-0.2%</b> | <b>-0.9%</b> | <b>3.2%</b> | <b>0.5%</b>  | <b>28.4%</b> | <b>1.0%</b>  |
| Scenario C                              |                    |              |              |             |              |              |              |
| COVA Care                               | 83,159             | \$450.17     | \$19.90      | \$137.61    | \$607.68     | \$14.26      | \$621.95     |
| <b>% Increase</b>                       |                    | <b>0.6%</b>  | <b>0.0%</b>  | <b>4.9%</b> | <b>1.5%</b>  | <b>29.4%</b> | <b>2.1%</b>  |

## FY 2017 Projection

Developing an estimated cost for the upcoming fiscal year (FY 2017) is the second step in the Commonwealth's requested three year projection cycle. The Exhibit shown below contains the rate projections and expected cost increase for FY 2017, which will be effective on July 1, 2016, for COVA Care under its current plan design. This chart builds on the outcome of the recast step above and blends current experience and trends compared to current rates.

- The FY 2017 rate increase is shown for each component of the COVA Care Basic rate. For budget planning purposes, the total percentage increase is the critical cost impact factor in the table.
- The chart shows the rate change comparison for each plan component and rolls it up to the total. For Scenario B, Medical is +5.1%, Dental +3.0%, Rx +16.9%, MISA/Behavioral Health 45.6%. The overall projected total increase, based on the weighted value of each component's relativity to premium, is 8.3%.

### Commonwealth of VA Summary of FY2017 Rating Projections Actives, COBRAs, and Retirees without Medicare

|   | Enrollees(@July15) | Medical  | Dental      | Rx Drugs    | Subtotal     | MISA        | Total        |              |
|---|--------------------|----------|-------------|-------------|--------------|-------------|--------------|--------------|
| FY2016 COVA Rates                       | 83,159             | \$447.28 | \$19.90     | \$131.23    | \$598.42     | \$11.02     | \$609.44     |              |
| FY2017 Projected Cost per Contract Unit |                    |          |             |             |              |             |              |              |
| Scenario A                              |                    |          |             |             |              |             |              |              |
|   | COVA Care          | 83,159   | \$461.86    | \$20.13     | \$149.72     | \$631.70    | \$15.78      | \$647.49     |
|   | <b>% Increase</b>  |          | <b>3.3%</b> | <b>1.1%</b> | <b>14.1%</b> | <b>5.6%</b> | <b>43.2%</b> | <b>6.2%</b>  |
| Scenario B                              |                    |          |             |             |              |             |              |              |
|   | COVA Care          | 83,159   | \$470.22    | \$20.50     | \$153.47     | \$644.18    | \$16.04      | \$660.23     |
|   | <b>% Increase</b>  |          | <b>5.1%</b> | <b>3.0%</b> | <b>16.9%</b> | <b>7.6%</b> | <b>45.6%</b> | <b>8.3%</b>  |
| Scenario C                              |                    |          |             |             |              |             |              |              |
|   | COVA Care          | 83,159   | \$478.58    | \$20.87     | \$157.36     | \$656.81    | \$16.30      | \$673.11     |
|   | <b>% Increase</b>  |          | <b>7.0%</b> | <b>4.9%</b> | <b>19.9%</b> | <b>9.8%</b> | <b>47.9%</b> | <b>10.4%</b> |

## FY 2018 Projection

Development of the FY 2018 rate increase is the third and final step in the Commonwealth's requested three year projection cycle. Similar to the FY 2017 projection, the increase is shown for each component of the COVA Care Basic rate. The total percentage increase is the critical cost impact factor in the table.

The chart shows the rate change comparison for each plan component and rolls it up to the total. For Scenario B, Medical is +6.9%, Dental +3.9%, Rx +14.3%, MISA/Behavioral Health +14.5%. The overall projected total increase, based on the weighted value of each component's relativity to premium, is 8.7%.

### Commonwealth of VA Summary of FY2018 Rating Projections Actives, COBRAs, and Retirees without Medicare

|  | Enrollees(@July15) | Medical     | Dental      | Rx Drugs     | Subtotal    | MISA         | Total       |
|--|--------------------|-------------|-------------|--------------|-------------|--------------|-------------|
| Estimated FY2017 COVA Rates (A Scenario) | 83,159             | \$461.86    | \$20.13     | \$149.72     | \$631.70    | \$15.78      | \$647.49    |
| Estimated FY2017 COVA Rates (B Scenario) | 83,159             | \$470.22    | \$20.50     | \$153.47     | \$644.18    | \$16.04      | \$660.23    |
| Estimated FY2017 COVA Rates (C Scenario) | 83,159             | \$478.58    | \$20.87     | \$157.36     | \$656.81    | \$16.30      | \$673.11    |
| FY2018 Projected Cost per Contract Unit  |                    |             |             |              |             |              |             |
| Scenario A                               |                    |             |             |              |             |              |             |
| COVA Care                                | 83,159             | \$489.29    | \$20.73     | \$169.62     | \$679.63    | \$17.93      | \$697.56    |
|  |                    | <b>5.9%</b> | <b>3.0%</b> | <b>13.3%</b> | <b>7.6%</b> | <b>13.6%</b> | <b>7.7%</b> |
| Scenario B                               |                    |             |             |              |             |              |             |
| COVA Care                                | 83,159             | \$502.83    | \$21.30     | \$175.41     | \$699.54    | \$18.37      | \$717.91    |
|  |                    | <b>6.9%</b> | <b>3.9%</b> | <b>14.3%</b> | <b>8.6%</b> | <b>14.5%</b> | <b>8.7%</b> |
| Scenario C                               |                    |             |             |              |             |              |             |
| COVA Care                                | 83,159             | \$516.37    | \$21.89     | \$181.33     | \$719.59    | \$18.83      | \$738.42    |
|  |                    | <b>7.9%</b> | <b>4.9%</b> | <b>15.2%</b> | <b>9.6%</b> | <b>15.5%</b> | <b>9.7%</b> |

## **Roll Forward Chart**

The following Roll Forward chart is a supplement to the aforementioned projection summary charts. It shows the key component drivers of the FY 2017 projections on a per contract unit, percentage, and total dollar basis, and ties to the recast and projection detail previously noted.

The roll-forward contains both recast FY 2016 cost and projected FY 2017 cost on a COVA Care Basic cost basis (the baseline rate for the plan) using Scenario B (most likely) assumptions from the projection. It shows, as detailed below, an 8.3 % increase versus the FY 16 actuarial rate if no IBNR re-build rate component in FY 2016 and FY 2017. In addition, it shows a 10.9% increase versus the final FY 2016 rate (including the HIF supplement provision) if an IBNR re-build component is included in FY 2017.

### **Chart Detail**

The recast FY 2016 and projected FY 2017 cost are shown on two bases for comparison to the final FY 2016 rates:

- The top portion of the chart shows key contract rates for the overall analysis:

|  |          |
|--|----------|
| FY2016 COVA Actuarial Rates (w/o IBNR Funding/HIF Supplement \$) | \$609.44 |
| FY2016 COVA Total Rates (w/IBNR Funding/HIF Supplement \$)       | \$602.29 |
| Scenario B FY 2016 Actuarial Rates - Update                      | \$615.55 |
| Scenario B FY 2017 Actuarial Rates                               | \$660.23 |
| Scenario B FY 2017 Total Rates (w/IBNR Funding \$)               | \$667.80 |

- Section A: projected rates for claims and administrative expense year over year (excludes IBNR funding). However, the FY 2016 total rate baseline (\$602.29) includes the net effect of the \$12.7M HIF Funding Supplement.
- Section B: IBNR re-build funding. IBNR reserves were exhausted at the end of FY 2011. Based on the APA audit recommendation that this reserve should be rebuilt, a rebuild strategy of 20% per year FY 14-18 was implemented per agreement with DPB given the budget process circumstances at the time. This section of the chart shows the increase over FY 16 rates including the re-build component. Going forward, as well as included when applicable in the past, additional impact statement line items in this exhibit may include significant cost drivers based on current health care cost developments (ACA driven plan changes most typical in recent years).
- Section A + B: sum of the FY 17 over FY 16 operational cost (Section A) plus fiscal additions such as an IBNR re-build contribution (Section B). The chart format is built to be flexible. In

previous years it has included varied combinations of increase drivers (IBNR rebuild; ACA cost) and decrease drivers (ACA ERRP reimbursement; HIF surplus subsidy).

Using the projected FY 2017 rate change scenario, this Roll Forward provides information on key anticipated drivers of final rates including claim experience and trend, plus other state plan dynamic factors, to yield a recommended baseline rate change.

For example, this year's exhibit notes:

- FY 2017 and 2018 rates exclude the ACA Comparative Effectiveness (PCORI) fees estimated to be approximately \$410K and \$430K respectively. Based on most recent guidance, PCORI fees may not be passed on to participants / paid from plan assets.
- 80% of IBNR (as of 6/30/15) is estimated to be \$79.8 million. FY16 rates were intended to include funding 60% of IBNR (cumulative) which was estimated to be \$65.7 million as of 6/30/14. However, due to the HIF balance the IBNR load was not needed. Since the HIF balance was sufficient to cover the IBNR, the 60% IBNR is viewed as "funded" in this analysis. Therefore, if the intent is to build to 80% of IBNR through FY17, the FY17 rates need to include a provision for the incremental \$14.0 million.

In reviewing the chart, the bottom two items (A) and (A+B) show the important FY change detail in the two right hand columns. As stated, the rates/costs are represented on a COVA Care Basic basis. Therefore, the aggregate dollars do not represent the total plan cost - they exclude cost associated with benefit buy-ups, which are employee contribution funded. However, the estimated percentage change is representative of the expected percentage change in total costs in the absence of plan changes:

- The actuarial rate change (A) of 8.3% over FY 2016 shows impact without an IBNR component or the FY 2016 HIF supplement. With catch up for the FY 2016 \$12.7 M supplement, the total change is 9.6%.
- The total rate change (A+B) of 10.9 % over FY 2016 shows the impact to achieve an 80% IBNR rebuild over the FY 2016 60% funded level. The need for additional rebuild will be based on current HIF status.



Commonwealth of VA  
Drivers of FY2017 Rating Projections  
Actives, COBRAs, and Retirees without Medicare

|  |   |  |             | Estimated % Increase |  | Financial Impact (Basic Benefit)   |                        |                                      |                                  |
|--|---|--|-------------|----------------------|--|------------------------------------|------------------------|--------------------------------------|----------------------------------|
|  |   |  |             | Total Cost per CU    | % Increase vs. Budget - Actuarial Rate | % Increase vs. Budget - Total Rate | Aggregate Cost         | Increase vs. Budget - Actuarial Rate | Increase vs. Budget - Total Rate |
| FY2016 COVA Actuarial Rates (w/o IBNR Funding/HIF Supplement \$)       |   |  |             | \$609.44             |  |                                    | \$1,133,244,465        |                                      |                                  |
| FY2016 COVA Total Rates (w/IBNR Funding/HIF Supplement \$)             |   |  |             | \$602.29             |  |                                    | \$1,119,946,766        |                                      |                                  |
| Scenario B FY 2016 Actuarial Rates - Update                            |   |  |             | \$615.55             | 1.0%                                   |                                    | \$1,144,596,249        | \$11,351,785                         |                                  |
| Scenario B FY 2017 Actuarial Rates                                     |   |  |             | \$660.23             | 8.3%                                   |                                    | \$1,227,680,756        | \$94,436,292                         |                                  |
| Scenario B FY 2017 Total Rates (w/IBNR Funding \$)                     |   |  |             | \$667.80             |  | 10.9%                              | \$1,241,760,441        |                                      | \$121,813,675                    |
| A  | FY 2016 vs. FY 2016 Budget  |  |             |                      |  |                                    |                        |                                      |                                  |
|  | FY 2016 Base Claims Experience (Actual vs. Expected)  |  |             | 2.1%                 |  |                                    |                        |                                      |                                  |
|  | Admin Fees (Actual vs FY16 Budget Estimate)   |  |             | 0.2%                 |  |                                    |                        |                                      |                                  |
|  | HCR Fees (Reinsurance) <sup>2</sup>   |  |             | 0.0%                 |  |                                    |                        |                                      |                                  |
|  | Pharmacy Rebates (Actual vs Procurement Estimate)   |  |             | -1.3%                |  |                                    |                        |                                      |                                  |
|  | <b>Total % Increase vs. 2016 Budget - Actuarial Rate</b>  |  |             | <b>1.0%</b>          | \$615.55                               |                                    | <b>\$1,144,596,249</b> | <b>\$11,351,785</b>                  |                                  |
|  | FY 2017 vs. FY 2016   |  |             |                      |  |                                    |                        |                                      |                                  |
| HCR Fees (Reinsurance)   |   |  | -0.4%       |                      |  |                                    |                        |                                      |                                  |
| Trend  |   |  | 7.7%        |                      |  |                                    |                        |                                      |                                  |
| <b>Total % Increase (Incremental) vs. 2016 Budget - Actuarial Rate</b> |   |  | <b>7.3%</b> | \$660.23             | 8.3%                                   | 9.6%                               | <b>\$1,227,680,756</b> | <b>\$94,436,292</b>                  |                                  |
| B  | Additional / Catch-Up Liability Funding Impacts <sup>3</sup>  |  |             |                      |  |                                    |                        |                                      |                                  |
|  | 80% Cumulative Active IBNR Funding (Ind. Margin and Claim Settlement Expenses) as of 6/30/15  |  |             | 1.2%                 |  |                                    |                        |                                      |                                  |
|  | Active Contingency Reserve Funding (not built into rates; letter of credit used for this reserve)                                     |  |             | 0.0%                 |  |                                    |                        |                                      |                                  |
| <b>Total % Increase (Incremental) vs. 2016 Budget - Actuarial Rate</b> |   |  | <b>1.2%</b> | \$667.80             | 9.6%                                   | 10.9%                              | <b>\$14,079,684</b>    | <b>\$14,079,684</b>                  | <b>(\$9,634,727)</b>             |
| = A  | FY 2017 Plan Cost <b>excluding</b> Liability Funding Change Impacts   |  |             |                      |  |                                    | \$1,227,680,756        |                                      |                                  |
|  | Total \$ Increase vs. 2016 Budget - Actuarial Rate  |  |             |                      |  |                                    |                        | \$94,436,292                         |                                  |
|  | Total % Increase vs. 2016 Budget - Actuarial Rate   |  |             |                      |  |                                    |                        | 8.3%                                 |                                  |
| = A + B  | FY 2017 Plan Cost <b>including</b> Liability Funding Change Impacts (80% IBNR Cumulative; nothing additional for Contingency Reserve) |  |             |                      |  |                                    | \$1,241,760,441        |                                      |                                  |
|  | Total \$ Increase vs. 2016 Total Rate   |  |             |                      |  |                                    |                        |                                      | \$121,813,675                    |
|  | Total % Increase vs. 2016 Total Rate  |  |             |                      |  |                                    |                        |                                      | 10.9%                            |

Notes:

1. FY 2016 Total Rate reflects a HIF Funding supplement in the amount of \$12.7 million, or approximately \$6.71 PCUPM. This funding supplement was an offset/decrease to the actuarial rate. The supplement was shared between the state and the employee.
2. FY 2016 and 2017 rates exclude the Comparative Effectiveness (PCORI) fees estimated to be approximately \$410K/\$430K. Based on most recent guidance, PCORI fees may not be passed on to participants / paid from plan assets.
3. 80% of IBNR (as of 6/30/15) is estimated to be \$79.8 million. FY16 rates were intended to include funding 60% of IBNR (cumulative) which was estimated to be \$65.7 million as of 6/30/14. However, due to the HIF balance the IBNR load was not needed. Because the HIF balance was sufficient to cover the IBNR, the IBNR is viewed as "funded" in this analysis. Therefore, if the intent is to build to 80% of IBNR through FY17, the FY17 rates need to include a provision for the incremental \$14.0 million.

## Trend Tables

These tables show the trend for each plan component and roll it up to the total. For Scenario B, FY 2017 Medical is 6.0 %, Dental +4.0 %, Rx 11.5%, MISA/Behavioral Health 14.0 %. The overall projected total trend (Scenario B), based on the weighted value of each component's relativity to premium is 7.5%.

FY 2017 Trend Assumptions

|            |           | Medical | Dental | Rx Drugs | Subtotal | MISA  | Total |
|------------|-----------|---------|--------|----------|----------|-------|-------|
| Scenario A | COVA Care | 5.0%    | 3.0%   | 10.5%    | 6.3%     | 13.0% | 6.5%  |
| Scenario B | COVA Care | 6.0%    | 4.0%   | 11.5%    | 7.3%     | 14.0% | 7.5%  |
| Scenario C | COVA Care | 7.0%    | 5.0%   | 12.5%    | 8.3%     | 15.0% | 8.5%  |

FY 2018 Trend Assumptions

|            |           | Medical | Dental | Rx Drugs | Subtotal | MISA  | Total |
|------------|-----------|---------|--------|----------|----------|-------|-------|
| Scenario A | COVA Care | 5.5%    | 3.0%   | 11.0%    | 6.8%     | 13.5% | 7.0%  |
| Scenario B | COVA Care | 6.5%    | 4.0%   | 12.0%    | 7.8%     | 14.5% | 8.0%  |
| Scenario C | COVA Care | 7.5%    | 5.0%   | 13.0%    | 8.8%     | 15.5% | 9.0%  |