# San Francisco Health Service System

# Health Service Board

## Rates & Benefits

Review and Approve Proposed Modifications to
June 30, 2023, Self-Funded and Flex-Funded
Health Plan Contingency Reserve Amounts

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# Proposed Modifications to June 30, 2023, Self-Funded and Flex-Funded Health Plan Contingency Reserve Amounts —Agenda

- **Introduction—**basis for today's proposed June 30, 2023, contingency reserve amount modifications (from amounts approved by the Health Service Board [HSB] in January 2024)

- **Background—**HSB Contingency Reserve Policy 210

- **Medical Self-Funded/Flex-Funded Plans—**proposed modified June 30, 2023, contingency reserve amounts using 95$^{th}$ percentile confidence interval (relative to prior use of 99$^{th}$ percentile confidence interval amounts)

- **Dental Self-Funded Active PPO Plan—**proposal to approve one-time suspension of Contingency Reserve Policy 210 for this plan, and set the June 30, 2023, contingency reserve amount for this plan to $0

- **Recommendations for HSB action**

# 1

# Introduction — Basis for Today's Recommendations

# Introduction—Basis for June 30, 2023, Contingency Reserve Modifications

## Brainstorming Reasonable Approaches to Go-Forward Cost Increase Relief

- As presented to the HSB on February 8, 2024, by representatives of the City and County of San Francisco, San Francisco Unified School District, and Community College of San Francisco, these employers operating health benefits via the San Francisco Health Service System (SFHSS) are experiencing unprecedented adverse financial outlooks.

- Knowing these difficult financial positions for the employers, SFHSS and Aon have recently brainstormed possible approaches into the 2025 health plans budgeting cycle to create savings for employers and members going forward in a way that does not compromise the financial integrity of SFHSS health plans.

- From this brainstorming, SFHSS and Aon have focused in recent weeks on re-evaluating the levels of health plan contingency reserves for SFHSS self-funded and flex-funded health plans—leading to today's recommendations for HSB action.

# Introduction—Basis for June 30, 2023, Contingency Reserve Modifications

## Summary of Today's Recommendations

- **Self-funded and flex-funded medical plans:** reduce the June 30, 2023, contingency reserve amounts within the framework of methodologies outlined in HSB Contingency Reserve Policy 210 ($8.5 million reduction)—which will reduce total plan cost rates via lower Rate Stabilization actions in 2025 and after.

- **Self-funded active employee dental PPO plan:** reduce the June 30, 2023, contingency reserve amount to $0 given criteria for holding a contingency reserve do not apply for a dental plan—which will reduce the total cost rates in 2025 and after for the self-funded active dental PPO plan (this recommendation requires a one-time suspension for this specific plan of the HSB Contingency Reserve Policy 210). This dental item results in a $2.1 million contingency reserve reduction.

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# Background — HSB Contingency Reserve Policy 210

# Background—HSB Contingency Reserve Policy 210

The HSB Reserve Policies are captured in the sfhss.org website within the Governance Policies and Terms of Reference document (revised January 2023) available at this link:

https://sfhss.org/sites/default/files/2023-01/HSB%20Governance%20Policies%20and%20Terms%20of%20Reference%20Revised%201-2023%20Full%20Packet_1.pdf

The Reserve Policy numbers and descriptions are (with emphasis on the Contingency Reserve Policy for this action item):

- **210 — SFHSS Contingency Reserve Policy**
- 211 — SFHSS Self-Funded Plans' Rate Stabilization Policy
- 212 — SFHSS IBNR Reserve Policy and Methodology

# Background—HSB Contingency Reserve Policy 210

## What is a Contingency Reserve?

- First implemented by SFHSS in 2007, a Contingency Reserve protects the Trust from highly unusual, adversely high health plan claim experience that could occur in a self-funded or flex-funded health plan. These events, as outlined in Policy 210, could include:
  - Random variation from expected claims;
  - Credibility of the experience;
  - Fluctuations in large claims experience;
  - Vendor processing stability;
  - Changes in COBRA enrollment; and
  - Catastrophic events and whether to make and allowance or not.

# Background—HSB Contingency Reserve Policy 210

## Contingency Policy Objectives—Protecting Unusually High Claim Experience

- It is prudent for self-funded and flex-funded health plans to have a Contingency Reserve, otherwise known as excess loss reserve, to absorb financial strain brought about by adverse claims experience.
- A contingency reserve covers the risk of claims in excess of the expected claims target used in the underwriting rate setting process.
- Contingency reserves allow SFHSS to establish a budget based on a predetermined funding level and maintain that structure regardless of claims experience level.
- Having a contingency reserve serves the same purpose as external stop loss insurance, and therefore external stop loss insurance will not be purchased except where required by the health plan.

# Background—HSB Contingency Reserve Policy 210

## Contingency Policy—Health Plans Covered

- The HSB Contingency Reserve Policy 210 establishes contingency reserves for SFHSS flex-funded and self-funded health care plans:
  - Flex-Funded HMO Plans (non-capitated costs);
  - Self-Funded PPO Plan; and
  - Self-Funded Active Dental PPO Plan.

# Background—HSB Contingency Reserve Policy 210

**Contingency Policy—Reserve Calculation Methodology**

- The HSB Contingency Reserve Policy 210 outlines the calculation methodology that Aon uses annually to produce three levels of statistical confidence intervals for reporting to the SFHSS Chief Financial Officer (CFO).
- Per Policy 210, Aon's calculations are performed at the $95^{th}$, $97^{th}$, and $99^{th}$ percentile confidence intervals (where the $95^{th}$ is statistically significant on its own, with the two other methods producing higher, more conservative amounts).
- Historically, HSB-approved contingency reserves have been set at the $99^{th}$ percentile confidence interval—or the highest of the three calculated amounts per methodology outlined in HSB Contingency Reserve Policy 210.

***WHAT IS A "CONFIDENCE INTERVAL"?*** **Think of it as a "percentage of being right" (e.g., $95^{th}$ percentile is "contingency reserve is not needed 5 times out of 100")**

# Reserves in SFHSS Financial Accounting

**Required Liabilities Per Accounting Rules**

- Liabilities are required to be booked in financial statements per Accounting Rules for certain items—in this category, SFHSS needs sufficient assets to cover the following liabilities to avoid a deficit net position (e.g., insolvent):
  - Incurred But Not Reported (IBNR) reserves (for costs of health plan services delivered to members but not yet known as of June 30 each year, guided by HSB Policy 212);
  - Any advance payments received;
  - Any premiums due for services already received; and
  - Other one-time required liabilities (example: litigation claims).

# Reserves in SFHSS Financial Accounting

## How Contingency Reserves Are Reflected

- Beyond Accounting Rules requirements described on the prior page, HSB reserve policies require SFHSS to hold a certain of amount of funds for any reason as determined by the HSB—to carry out this goal, SFHSS should have sufficient assets on its books.
- HSB policies guide the Contingency and Rate Stabilization reserves held by SFHSS—these reserves are footnoted items on SFHSS financial statement.
- As SFHSS current net assets exceed the total amount of these items, SFHSS is fully funded for these items.
    - Contingency: HSB Policy 210 language indicates that this should be fully funded.
    - Rate Stabilization: Policy 211 states the purpose as stabilizing the annual premiums but does not state these should be fully funded.

# Reserves in SFHSS Financial Accounting

**How Contingency Reserves Are Reflected (continued)**

- Contingency reserve changes from the prior fiscal year-end to the most recent fiscal year-end are incorporated into the annual Rate Stabilization calculations to determine the annual recommended Rate Stabilization actions for next year's self-funded and flex-funded health plan rate cards each year.

- Hence, today's proposed modifications to June 30, 2023, self-funded and flex-funded plan contingency reserves would reduce the total cost rates in 2025 plan year health plan rate cards by approximately **$4.2 million**—leading to reduced member and employer costs for the 2025 plan year.

- The additional $6.4 million impact would flow to Rate Stabilization calculations in 2026 and after (to be reviewed with the HSB during the Rate Stabilization recommendations action item at the April HSB meeting).

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# Medical Self-Funded/Flex-Funded Plans

# Medical Self-Funded/Flex-Funded Health Plans

- Today's recommendation for the medical self-funded and flex-funded health plans falls within the framework of HSB Contingency Reserve Policy 210.

- The Aon actuary communicated during the January 11, 2024, HSB meeting for the Contingency Reserves approval item the potential impact of changing the confidence interval approach from the historically-utilized 99th percentile level to the other levels outlined in the HSB Contingency Reserve Policy 210 (95th and 97th percentile levels).

- The recommended modifications in today's recommendation for SFHSS self-funded and flex-funded medical plans result in a reduction of $8.5 million for June 30, 2023, contingency reserves in total as outlined on the next page. These modifications, if approved, will cascade into the 2025 Plan Year Rate Stabilization calculations for these plans that will be presented to the HSB at the April 11, 2024, meeting.

# Medical Self-Funded/Flex-Funded Health Plans

## Proposed Modified June 30, 2023, Contingency Reserves at 95th Percentile Confidence Interval (for Active Employee/Early Retiree Self-Funded and Flex-Funded Medical Plans—to $17,992,721 total)

| Medical Self-Funded/Flex-Funded Health Plan | Contingency Reserves | | | |
|---|---|---|---|---|
| | Original 6/30/23 (99th %ile) | Modified 6/30/23 (95th %ile) | Modified 6/30/23 vs Original 6/30/23 $ Increase/ (Decrease) | Modified 6/30/23 vs Original 6/30/23 % Increase/ (Decrease) |
| Flex-Funded Non-Medicare HMO Plans Administered by BSC (Access+ and Trio) / Self-Funded Non-Medicare EPO Plans Administered by UHC (Select and Doctors) | $17,377,132 | $12,116,214 | ($5,260,918) | -30.3% |
| Flex-Funded Non-Medicare HMO Plan Administered by Health Net (CanopyCare) | $402,249 | $280,761 | ($121,488) | -30.2% |
| Self-Funded Non-Medicare PPO Plan Administered by BSC/UHC | $8,710,826 | $5,595,746 | ($3,115,080) | -35.8% |
| Total Self-Funded/Flex-Funded Plans | $26,490,207 | $17,992,721 | ($8,497,486) | -32.1% |

# Medical Self-Funded/Flex-Funded Health Plans

## Example of Medical Contingency Reserve Amount Modification on Rate Stabilization Rate Card Portion for 2025—BSC HMO and UHC EPO Plans[1]

How Difference in Contingency Reserve Amount Impacts Rate Stabilization Fund (Currently in Deficit for BSC HMO and UHC EPO Plans)

| | **Expected 2023** | **Actual 2023 with Contingency at 99th Percentile** | **Actual 2023 with Contingency at 95th Percentile** |
|---|---|---|---|
| Revenue Shortfall/(Surplus) | $6,592,000 | $18,771,000 | $18,771,000 |
| Increase/(Decrease) in Contingency Reserve | | $2,782,000 | ($2,479,000) |
| Total Shortfall/(Surplus) | | $21,553,000 | $16,292,000 |
| Net to be Applied when Determining the Stabilization Carry Forward (Actual Less Expected)--Rating Buy-Up Since in Deficit Position | | $14,961,000 | $9,700,000 |
| Reduction in Rate Stabilization Deficit for BSC HMO and UHC EPO Plans | | | ($5,261,000) |

[1] To be reviewed with the HSB at the April 11 meeting

# Medical Self-Funded/Flex-Funded Health Plans

**Example of Medical Contingency Reserve Amount Modification on Rate Stabilization Rate Card Portion for 2025—BSC HMO and UHC EPO Plans[1]**

How The Reduction in Rate Stabilization Deficit for the BSC HMO and UHC EPO Plans Lowers the Proposed 2025 Rate Stabilization Rate Card Buy-Up Portions

- One-third of the overall amount applies in 2025 rating—**reduces these plans' stabilization buy-up by $1,753,000** (of the overall $4.2 million for all plans)

- Two-thirds of the overall amount applies after 2025 in rating

| | **Using 99th Percentile** | **Using 95th Percentile** | **Difference** |
|---|---|---|---|
| Prior carry-forward stabilization deficit balance | $6,718,000 | $6,718,000 | $0 |
| Recommended increase to the deficit based on 2023 experience | $14,961,000 | $9,700,000 | ($5,261,000) |
| Stabilization deficit balance as of December 31, 2023 | $21,679,000 | $16,418,000 | ($5,261,000) |
| Calculated amount per amortization policy to apply to 2025 rate buy-up per policy (1/3 of stabilization deficit balance) | $7,226,000 | $5,473,000 | ($1,753,000) |
| Updated carry-forward stabilization deficit for use after 2025 | $14,453,000 | $10,945,000 | ($3,508,000) |

[1] To be reviewed with the HSB at the April 11 meeting

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# Dental Self-Funded Active PPO Plan

# Dental Self-Funded Active PPO Plan

- The contingency reserve concept is highly prudent for medical plans, as outlined in language contained earlier in this presentation from the HSB Contingency Reserve Policy 210.
  - A key element guiding this is for **medical** plans, the member financial responsibility on high-cost claims is capped through plan out-of-pocket maximums, whereas plan financial responsibility for a member is not capped.
- However, for **dental**, the plan's financial responsibility per member is capped through plan annual maximums and lifetime orthodontic benefit maximums.
- Thus, the criteria outlined earlier in this presentation for prudency of a dental plan contingency reserve, as also stated in HSB Contingency Reserve Policy 210, do not apply to a self-funded dental plan as a practical matter—though historically the Contingency Reserve Policy 210 has included provision for the active employee self-funded dental PPO plan.

# Dental Self-Funded Active PPO Plan

- As a result, as part of the SFHSS and Aon review of contingency reserve modifications in this presentation, it is recommended that the active dental PPO plan contingency reserve be eliminated (e.g., set to $0) as of June 30, 2023.

- This results in a recommended change of June 30, 2023, contingency reserve for this plan from $2,060,327 (as approved by the HSB at the January 11, 2024, meeting) to $0.

- This change will lower the recommended 2025 active dental PPO plan total rate increase when presented to the HSB at the May 9, 2024, meeting (based on the impact to the Rate Stabilization proposed action for 2025 plan year to be presented to the HSB at the April 11, 2024, meeting).

- Approval of this recommended action today will require a one-time suspension of the Contingency Reserve Policy 210 for the self-funded active employee dental PPO plan. The Governance Committee of the HSB could consider Policy 210 modification for the dental self-funded active PPO plan at a later date.

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# Recommendations for HSB Action

# Today's Recommendation

## Proposed Modifications to June 30, 2023, Self-Funded and Flex-Funded Health Plan Contingency Reserve Amounts

It is recommended that the Health Service Board approve the modifications of the June 30, 2023, self-funded and flex-funded health plan contingency reserve amounts as outlined below:

(1) Approve the modification of the June 30, 2023, medical self-funded and flex-funded health plan contingency reserve amounts from those originally approved on January 11, 2024, to the 95th percentile confidence interval amounts captured on page 17 of this presentation document totaling $17,992,721.

(2) Make an exception to the HSB Contingency Reserve Policy 210 on a one-time basis for the dental self-funded active PPO plan.

(3) Approve the setting of the June 30, 2023, contingency reserve amount for the dental self-funded active PPO plan to $0.