SAN FRANCISCO
HEALTH SERVICE SYSTEM
Affordable, Quality Benefits & Well-Being

210: SFHSS CONTINGENCY RESERVE POLICY

Policy Objectives

1) It is prudent for an administrator of a self-funded and flex-funded benefit programs to establish a Contingency Reserve, otherwise known as excess loss reserve, to absorb financial strain brought about by adverse claims experience. A Contingency Reserve is funding reserved to cover the risk of claims in excess of the expected claims target used in the underwriting rate setting process.

2) Independent of the ability of a self-funded benefit plan to access external dollars to fund adverse experiences, it is prudent and sound to consider implementing a Contingency Reserve. It allows the Plan Sponsor to establish a budget based on a predetermined funding level and maintain that structure regardless of claims experience level.

3) Establishment of the 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.

Contingency Reserve Policy

1) This policy standardizes the SFHSS ***Contingency Reserve*** setting methodology for self-funded health plans. The purpose of the Contingency Reserve is to establish reserve funds that are available in the event claims are in excess of target costs. The Contingency Reserve policy is specific to SFHSS' flex and self-funded health care plans:
    a. Flex-Funded HMO Plans (non-capitated costs)Self-Funded PPO
    b. Self-Funded Dental PPO Plan (for Actives only)

The methods specified in this document will be applied for Contingency Reserve estimation as of the end of each fiscal year.

Definitions

2) *Contingency Reserve*: Any actuarial estimate is based upon the information available at a point in time and is subject to unforeseen and random events. At any point in time, estimated reserves may be higher or lower than required. Future funding projections will generate revenue that may be higher or lower than actual experience. Multiple factors impact the eventual experience of the self-funded and flex funded health plans. The range of plausible results around the best estimate rates would consider:

    a) Random variation from expected claims;

    b) Credibility of the experience;

    c) Fluctuations in large claims experience;

    d) Vendor processing stability;

    e) Changes in COBRA enrollment; and

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f) Catastrophic events and whether to make allowance or not.

The Contingency Reserve is intended to immunize against such adverse experience. *Large Claims Reserve*: a subset of the Contingency Reserve. The Contingency Reserve accounts for all claims over the projected claims target level. The Large Claims Reserve accounts for all large claims over a certain threshold. Since all large claims over the threshold are also over the projected claims target level, they are already being accounted for in the Contingency Reserve.

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Contingency Reserve Methodology

3) To establish the Contingency Reserve(s), linear regression is used, specifically:

a) The City and County of San Francisco's third-party administrator(s) provide either 36 or48 months of claim data which the actuarial consultant firm summarizes by incurred and paid period. This data is separate for each line of coverage (medical, pharmacy, and dental) and each plan.

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b) These amounts are converted to a per employee per month ("PEPM") basis and linear regression is performed on the monthly PEPM values.

c) The regression data are used to determine the predicted monthly values and the corresponding monthly variances, as well as the predicted annual claims per employee per year ("PEPY") and corresponding variance PEPY.

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d) Using the predicted claims PEPY and variance PEPY, the expected value is calculated at a particular level of confidence. This is done by using the normal distribution. For our analysis, we use three levels of potential excess cost; confidence levels of 95%, 97%, and99%.

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e) The gross Contingency Reserve is the difference between the cost at a particular confidence level and the projected PEPY costs times the anticipated enrollment, plus a margin between 0% and 10%.

f) The actuarial consultant firm presents the analysis at the three levels of confidence (95%, 97%, and 99%) to the HS Board for final determination of the approved contingency reserve amount for each plan

Review

4) The Board shall review this policy at least every three years.

Policy History

5) The Board adopted this policy on March 12, 2008, and amended it on March 14, 2013, February 13, 2014, February 10, 2022 and January 12, 2023.

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