Deloitte.

State of Wisconsin Employee Trust Funds

High-Deductible Health Plan and Health Savings Account Actuarial Analysis

May 20, 2014

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Summary

Effective January 1, 2015, the State of Wisconsin will be offering a high-deductible health plan (HDHP) medical/pharmacy option to the employees of the State. This HDHP option is intended to be compatible with a health savings account (HSA).

Per the 2013 Wisconsin Act 20 (Section 9112. Nonstatutory provisions; Employee Trust Funds.)

(4L) Design of state employee high-deductible health plan and health savings accounts.

(a) Before the group insurance board offers state employees the option of receiving health care coverage through a program that consists of a high-deductible health plan and the establishment of a health savings account under section 40.515 of the statutes, as created by this act, the group insurance board and the director of the office of state employment relations shall design a proposed program that specifies key actuarial parameters of the program, including proposed required deductible amounts, out-of-pocket maximum limits, premium rates, employer contributions to health savings accounts, and any other relevant factors.

(b) The group insurance board shall submit the proposed program for an actuarial analysis under section 40.03 (5) (a) of the statutes to determine the fiscal effect of the proposed program on state employee health care costs. If the actuary determines that short-term or long-term state employee health care costs will increase under the proposed program, the actuary shall make recommendations to make the program more cost-effective.

(c) The group insurance board and the director of the office of state employment relations shall consider the actuary's recommendations, if any, in designing a program that consists of a high-deductible health plan and the establishment of a health savings account under section 40.515 of the statutes, as created by this act.

This report addresses the requirements under (4L)(b) above with respect to providing an actuarial review of the short-term and long-term cost impact of the HDHP+HSA plan option to validate that this plan option is not expected to have an adverse financial impact on the state health care costs compared to the absence of such a plan option.

Statement of Actuarial Opinion

Based on the financial and qualitative objectives presented in this report, the HDHP+HSA plan design to be implemented for plan year 2015, and the reasonableness of the assumptions used, Deloitte Consulting believes actuarially that the short-term and long-term state employee health care costs will not increase under the proposed HDHP+HSA plan design, HSA accrual levels, and employee contributions any more quickly than had such a plan not been implemented for plan year 2015.

The developments of this report have been made in accordance with generally accepted actuarial methods, as well as the tenets set forth by the Actuarial Standards Board and the Actuarial Standards of Practice.

Guidelines issued by the American Academy of Actuaries require actuaries to include their professional qualifications in all actuarial communications.

> *I, Daniel Plante, am a qualified actuary employed by Deloitte Consulting, am a Member of the American Academy of Actuaries, and am an Associate of the Society of Actuaries, and meet their Qualification Standards to perform the analyses included in this report.*

This document was prepared for the purpose of supporting the State in its financial analyses and understanding of HDHPs and HSAs. The conclusions, results, values, and calculations contained herein are for use solely in support of this purpose.

I have relied upon relevant information provided to us by ETF and its vendors, and as noted above have used this information on an "as is" basis. While the scope of this project did not call for the Deloitte actuaries to perform an audit or independent verification of this information, we have reviewed this information for reasonableness. The accuracy of the results presented in this document is dependent upon the accuracy and completeness of the underlying information.

The results contained in this document constitute the materials to which this statement pertains. To the best of my knowledge, the individuals involved in this analysis have no relationship that may impair or appear to impair the objectivity of our work. It should be recognized that because future events frequently do not occur exactly as expected, there are usually differences between projected and actual results. For example, actual experience may differ from assumptions, including but not limited to those for claim costs, trends and non-benefit expenses. Accordingly, there can be no assurance that the client's actual experience will match the projections.

HDHP+HSA Plan Design Objectives

The development of a HDHP+HSA plan design has been made to be consistent with several key financial and qualitative tenets set forth by the State's Group Insurance Board:

- The net cost (premium less employee contributions) of the Uniform Standard HMO plan design will be cost neutral to the net cost (premium plus HSA accrual less employee contributions) of the HDHP+HSA plan design.
- Cost neutrality will be based separately on single coverage versus family coverage rather than in aggregate.
- Employee contributions for the HDHP+HSA plan option will be set, on average across the single and family coverage tiers, at approximately 35% of the level for the HMO option (i.e., the ratio can vary from 35% for single coverage versus family coverage, but on average should be at 35%).[1]
- The HDHP component of the HDHP+HSA plan option will reflect deductibles and maximum out-of-pocket amounts that are consistent with the averages seen in the marketplace for such plans, and will maintain a 2:1 ratio family to single.

HDHP+HSA Plan Design Summary

A summary of the key plan design provisions that have been discussed for the HDHP+HSA plan design are presented below.

Key Plan Design Provision	In-Network
Deductible (Single / Family)	$1,500 / $3,000
HSA (Employer Funded)	$195 / $390
Out-of-Pocket Limit (Single / Family) (Includes Deductible)	$2,500 / $5,000
Preventive Care	100% (No Deductible)
Office Visits	90%
Emergency Room	90%
Prescription Drugs (Copays Apply After Deductible Met): • Level 1 Formulary Generic • Level 2 Formulary Brand • Level 3 Non-Formulary • Level 4 Specialty Drugs	 $5 $15 $35 $50
Hearing Aid (Adults)	80% Up to $1,000 Benefit
Hearing Aid (Children)	90% Up to OOPL
Cochlear Implants (Adults / Children)	80% / 90%
Diabetic Supplies	80%
Durable Medical Equipment	80%

[1] Note that the 35% level means that an average HMO employee contribution of $100 per month would translate to an average HDHP+HSA employee contribution of $35 per month.

The HDHP+HSA plan design provisions provided above reflect a summary only. In general, for services not listed, if the service is covered, the coinsurance rate is the same as is the case for the Uniform Standard HMO.

Key Actuarial Assumptions

In performing the actuarial review of the HDHP+HSA plan design with respect to assessing the short-term and long-term cost impacts to the State, a number of key actuarial assumptions have been made:

- **Health care inflation 2014 to 2015:** The underlying health care inflation trend assumption from 2014 to 2015 is 7.5%.
- **Health care inflation after 2015:** After 2015, HMO paid claims are assumed to increase by 5.0% per year, consistent with the actual average increase over three of the last four years (2010 to 2011, 2012 to 2013, and 2013 to 2014). There was a 1.5% decrease from 2011 to 2012, but this reflected a plan design change (and was, thus, excluded from the average).

  The 5.0% trend assumption on the HMO premium rates translated to an average 5.35% trend assumption for the HDHP premiums given the fixed nature of the HDHP deductible.
- **Adverse selection:** Adverse selection is defined as the ability for an employee to somewhat predict his/her prospective claims, and have the choice between two or more health plan options allowing the employee to financially benefit from that prediction.

  For example, an employee who is relatively certain he/she will have no claims next year will be more likely to select the health plan option with the lowest required employee contribution.

  For purposes of this actuarial analysis, no adverse selection has been assumed. Given that the expectation is that most members will remain with their current carrier, each carrier's claims risk exposure remains relatively unchanged, rendering the impact of any adverse selection at the plan level by an employee to be somewhat moot when all employees are considered.
- **HDHP utilization change:** There is expectation that, by simple virtue of enrolling in the HDHP+HSA option with its different cost-sharing structure, participants in that plan will alter their health utilization patterns.

  One HDHP utilization study demonstrated such a change[2]. Nonetheless, we

[2] "Consumer-Directed Health Plans Reduce The Long-Term Use Of Outpatient Physician Visits And Prescription Drugs", Health Affairs, 32, no.6 (2013):pp. 1,126-1,134.

have assumed no reductions in utilization among HDHP+HSA participants for purposes of being conservative in our financial analyses.

- **HSA accruals:** Employer accruals to the HSAs are assumed to occur regularly during the course of the year with each paycheck, rather than be end-loaded each quarter, semi-annually, or year-end. This funding accrual approach is expected to promote enrollment in the HDHP+HSA option.
- **Migration to the HDHP+HSA plan option:** Given the objective of cost-neutrality in this analysis, and the exclusion of a financial impact for adverse selection and HDHP utilization change, any assumed underlying migration assumption does not have an impact on the ultimate actuarial financial projection for 2015.
- **Opt Outs:** It has been assumed that employees who are currently opted out of coverage would not now enrol in the HDHP+HSA option merely to get the HSA accrual. Because employee contributions for the HDHP+HSA plan option are greater than the HSA accrual being provided, this seems a reasonable assumption.

Actuarial standards of practice dictate that each assumption in and of itself selected should be reasonable and supportable, and that all assumptions taken together are equally reasonable and supportable as a set. We believe the assumptions presented here do adhere to these standards.

Cost Neutrality to State for 2015

The basis for validating the cost neutrality of the HDHP+HSA plan option has been made per the following steps:

1. Project the 2014 Uniform Standard HMO plan design premium rate (weighted average across all carriers) to 2015.
2. Estimate the relative value[3] of the 2015 Uniform Standard HMO.
3. Offset the 2015 Uniform Standard HMO relative value by the employee contributions to derive the actuarial estimate of the net relative value of the plan option to the State.
4. Estimate the relative value of the 2015 HDHP plan design.
5. Include in the HDHP relative value the value of the entire employer-provided

[3] "Relative Value" and "actuarial value" are terms typically used synonymously. With the advent of health care reform, "actuarial value" has been identified as a specific valuation metric associated with the plan design value for small group and individual health plan options. Therefore, in order to avoid any confusion, this report will use the term "relative value" to describe the valuation metric associated with a plan design value that considers historic claims experience and enrollment (two things that the health reform actuarial value do not consider).

HSA accrual.

6. Offset the 2015 HDHP+HSA relative value by the employee contributions to derive the actuarial estimate of the net relative value of the HDHP+HSA plan option to the State.
7. In order to be cost neutral, the net relative values of the HMO and HDHP+HSA should be equivalent (or, if not equivalent, closely comparable).

The table below compares the relative value estimates for 2015 for the HMO and the HDHP+HSA plan options for the same covered Wisconsin populations.

Plan Component (Average of Single and Family Coverage Tiers)	Uniform Standard HMO Plan	HDHP+HSA Plan
Relative Value	0.950	0.852
Employer-Funded HSA Accrual		0.015
Gross Relative Value	0.950	0.867
Employee Contributions	(0.123)	(0.040)
Net Relative Value	0.847	0.847

For the 2015 plan year, the Uniform Standard HMO and the HDHP+HSA plan options have equivalent net relative values and are cost neutral to the State for 2015.

To the extent that some adverse selection occurs (whereby higher cost risks remain with the HMO and lower cost risks migrate to the HDHP+HSA option), the cost exposure rests with the carriers as the prospectively-set fully-insured premium rates assign that risk to the carriers. The risk to the State is, therefore, two-fold:

- The prospectively-set rates for 2015 include additional contingency margin in anticipation of potential adverse selection; and
- Rates for 2016 include some retrospective deficit recoveries for actual adverse selection impacts.

In each case, these can be controlled by the State in its annual prospective rate negotiation process. And, to the extent that there are utilization reductions by virtue of participation in the HDHP+HSA plan option, those savings would potentially offset any adverse selection exposure.

Long-Term Cost Neutrality to the State

The above section discusses the cost-neutrality of the HDHP+HSA plan option to the State for 2015. However, Section 9112 of the 2013 Wisconsin Act 20 also notes the need to consider the long-term state employee health plan cost impact.

Several assumptions are used in this consideration:

- Health care inflation will be consistent between the HMO and HDHP+HSA plan options (assumed to be 5% per year in this analysis consistent with actual average increases over the recent plan years);
- State funding of the HSAs will not increase;
- Employee contributions for the HMO and HDHP+HSA plan options will also increase at the rate of health care inflation (5% in this analysis); and
- Any plan design changes made to one plan option will be met with an actuarially equivalent plan design change made to the other option (no changes have been assumed in this analysis, however).

Under these assumptions the table below presents the projected per employee per month (PEPM) Uniform Standard HMO average premium rates, employee contributions, and net costs to the State over the period 2015 through 2030. The blended average rates for single and family coverages are based on the weighted averages (by enrollment) of the single versus family coverage.

Year	HMO Premium	Employee Contribution	Net State HMO Cost
2015	$1,440	($187)	$1,253
2016	$1,512	($197)	$1,316
2017	$1,588	($206)	$1,382
2018	$1,667	($216)	$1,451
2019	$1,751	($227)	$1,523
2020	$1,838	($239)	$1,599
2021	$1,930	($251)	$1,679
2022	$2,026	($263)	$1,763
2023	$2,128	($276)	$1,851
2024	$2,234	($290)	$1,944
2025	$2,345	($305)	$2,041
2026	$2,463	($320)	$2,143
2027	$2,586	($336)	$2,250
2028	$2,715	($352)	$2,362
2029	$2,850	($370)	$2,480
2030	$2,993	($388)	$2,604

Similarly, the table below presents the projected PEPM HDHP+HSA average premium rates, HSA employer accruals, employee contributions, and net costs to the State over the period 2015 through 2030.

Year	HDHP Premium	HSA Accrual	Employee Contribution	Net State HDHP+HSA Cost
2015	$1,295	$23	($65)	$1,253
2016	$1,361	$23	($69)	$1,315
2017	$1,430	$23	($73)	$1,380
2018	$1,502	$23	($76)	$1,449
2019	$1,578	$23	($80)	$1,522
2020	$1,658	$23	($84)	$1,598
2021	$1,742	$23	($88)	$1,677
2022	$1,830	$23	($93)	$1,761
2023	$1,923	$23	($97)	$1,849
2024	$2,020	$23	($102)	$1,942
2025	$2,123	$23	($107)	$2,039
2026	$2,230	$23	($112)	$2,141
2027	$2,343	$23	($118)	$2,248
2028	$2,462	$23	($124)	$2,362
2029	$2,586	$23	($130)	$2,480
2030	$2,717	$23	($137)	$2,604

While not exactly cost neutral for all years, the difference is with a couple of dollars each year (and in favor of the HDHP+HSA plan option), so for all intents and purposes over the course of the 2015 – 2030 period, under the assumptions presented above, the addition of the HDHP+HSA option does not present a cost increase to the State over and above what would be the expected costs increases each year if only the Uniform Standard HMO continued to be offered.

And, in the event that there is some factor that emerges that causes the above cost neutrality to erode, the State has the ability to adjust one or both of the HDHP+HSA employee contribution rates and/or the employer-funded HSA accrual to maintain cost neutrality.

Administrative Costs

The implementation of a HDHP+HSA plan option will produce additional administrative costs to the State, some hard costs, some soft costs. Hard costs consist of possible new administrative fees to accommodate the HSA plan. The State has undertaken a vendor search to find an HSA administrator. Typically the cost of administration of HSAs is charged in the form of a monthly fee per account, which is usually handled in one of two ways:

- A monthly fee deducted from the HSA itself (i.e., employee pays), or
- A monthly fee charged to the plan sponsor (i.e., employer pays).

It is not uncommon for HSA account administrative fees to be somewhat comparable with FSA administrative fees. Typical HSA plan participants do not also maintain FSAs, so to the extent to which some HDHP+HSA plan participants currently have FSAs, it is expected that there would be minimal additional administrative fee costs given this substitution. However, for those HDHP+HSA plan participants who do not currently have FSAs, then the HSA will represent a source of additional administrative fees, which can average about $5 (for example) per participant per month.

In addition, there will be soft administrative costs to be considered, expected to be internal costs to the State, examples of which include:

- Payroll System(s): Additional deduction fields in the payroll system(s) to accommodate employee contributions for the HDHP option;
- Payroll System(s): Additional deduction fields in the payroll system(s) to accommodate elective employee deductions for HSA contributions;
- Open Enrollment: Additional content in the annual “It’s Your Choice” enrollment guide;
- Open Enrollment: Additional communication effort to explain the new HDHP+HSA plan option; and
- Tax Forms: An annual IRS Form 1099-SA will need to be issued to each participant in the HDHP+HSA plan option.

This actuarial analysis does not consider any of the internal, soft administrative costs associated with the addition of the HDHP+HSA plan option.

Health Care Reform: 2018 Excise Tax

Health reform imposes an excise tax on so-called "Cadillac plans" if the aggregate value of employer-sponsored health insurance coverage for an employee (including retirees and their dependents) exceeds a threshold amount. The tax applies to all plans, whether self- or fully-insured, and includes Medicare Advantage plans. The tax is equal to 40% of the excess value over defined dollar thresholds, and is payable by the insurer for fully-insured plans, or the plan administrator for self-insured plans.

The value of health insurance coverage also includes reimbursements under a health reimbursement arrangement (HRA) and contributions to a health flexible spending arrangement (FSA), an HSA, or an Archer MSA. (The value of separate dental or vision insurance, employer-sponsored long-term care coverage, coverage only for accident or disability income insurance, liability insurance, workers compensation insurance and other similar insurance coverage will generally be excluded.)

The predominant view is that the "plan administrator" who pays the excise tax for self-insured plans is generally the Third Party Administrator (TPA). Under this view (and for fully-insured plans), it is reasonable to assume the TPA (insurer) will gross up the amount it charges employers to cover its costs of paying the excise tax, since the excise tax is not tax deductible to the TPA. The grossed-up percentage would then be 40% / (1- assumed tax rate of TPA).

The 2018 threshold amounts are $10,200 for single coverage, and $27,500 for family coverage, indexed from 2018 to 2019 by CPI+1%, and at CPI thereafter (rounded to the nearest $50 in each case).

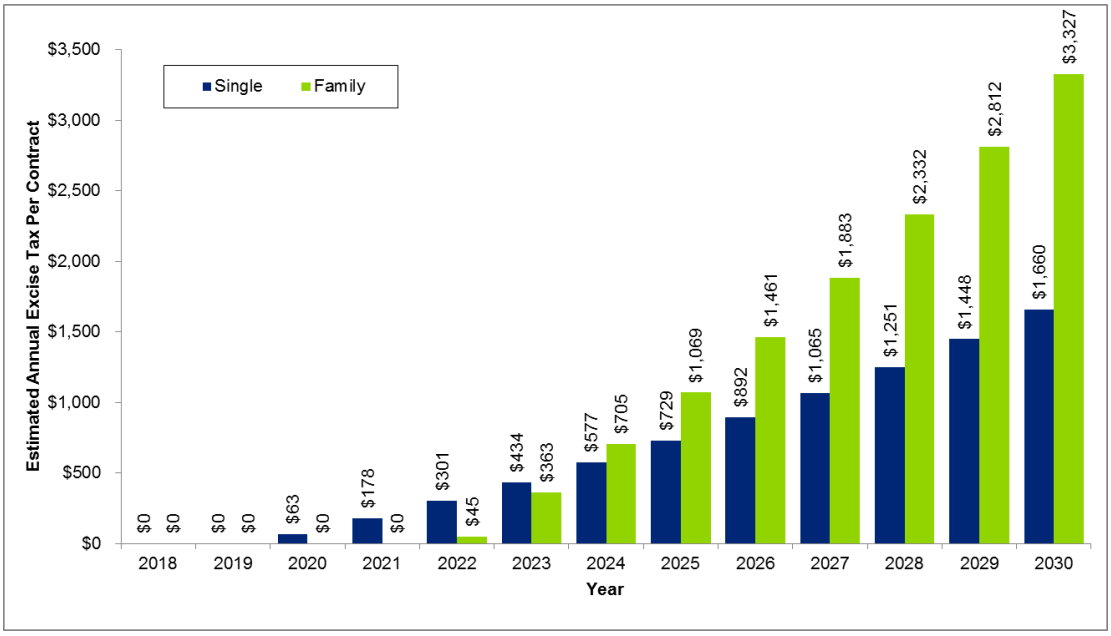
Based on the key assumptions outlined in this report, the expected implications of the excise tax on each of the Uniform Standard HMO and the HDHP+HSA plan options are as following (split between single and family):

Year	HMO		HDHP+HSA	
	Single	Family	Single	Family
2018	No Tax	No Tax	No Tax	No Tax
2019	No Tax	No Tax	No Tax	No Tax
2020	**40% Excise**	No Tax	No Tax	No Tax
2021	**40% Excise**	No Tax	No Tax	No Tax
2022	**40% Excise**	**40% Excise**	**40% Excise**	No Tax
2023	**40% Excise**	**40% Excise**	**40% Excise**	No Tax
2024	**40% Excise**	**40% Excise**	**40% Excise**	No Tax
2025	**40% Excise**	**40% Excise**	**40% Excise**	**40% Excise**
2026	**40% Excise**	**40% Excise**	**40% Excise**	**40% Excise**
2027	**40% Excise**	**40% Excise**	**40% Excise**	**40% Excise**
2028	**40% Excise**	**40% Excise**	**40% Excise**	**40% Excise**
2029	**40% Excise**	**40% Excise**	**40% Excise**	**40% Excise**
2030	**40% Excise**	**40% Excise**	**40% Excise**	**40% Excise**

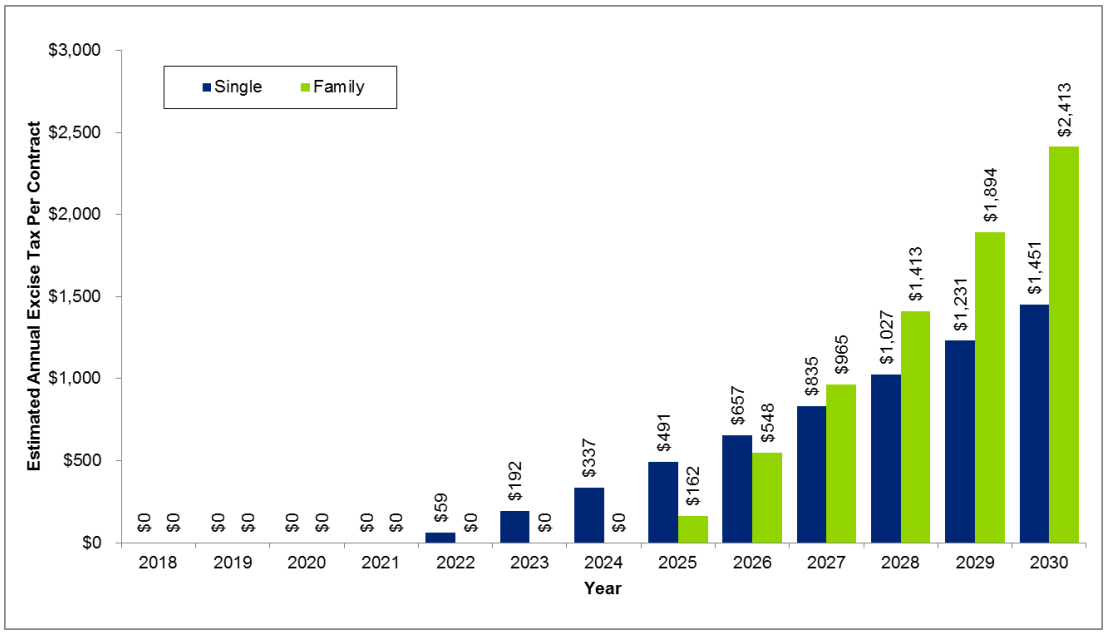
Under the assumptions noted in this report, the 40% Excise Tax is projected to apply to the Uniform Standard HMO single coverage starting in 2020, and in 2022 for the family coverage. For the HDHP+HSA, the application is not expected to begin until 2022 for single coverage, and 2025 for family coverage. Thus, there is expectation that once the Excise Tax is applicable, any cost neutrality of the two plans will shift in favor of the HDHP+HSA option.

The projected annual magnitude of the Excise Tax for the above years is illustrated below.

Uniform Standard HMO



HDHP+HSA



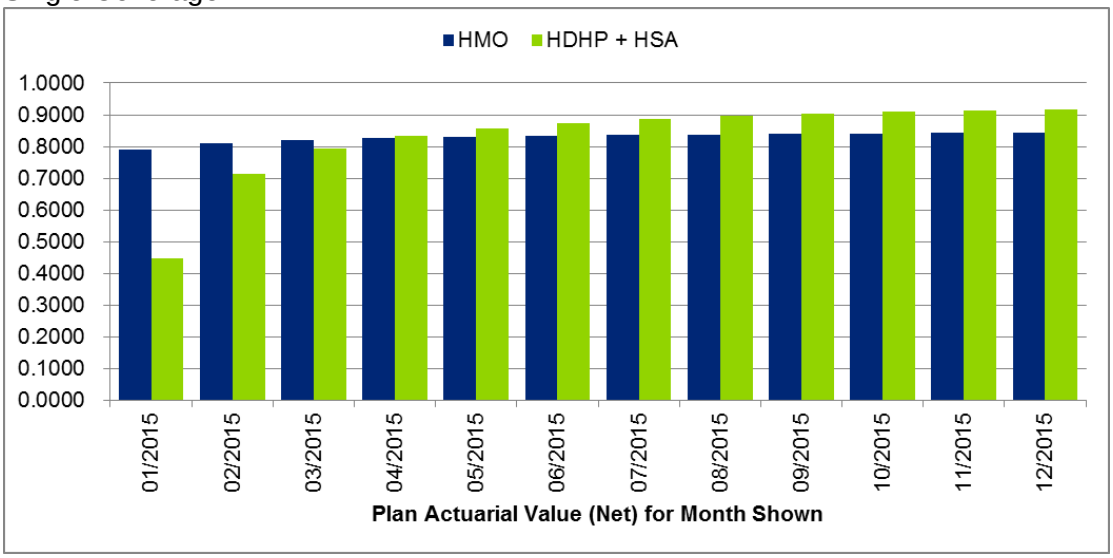
Cost Impact on Employees

Thus far this report has focused on the cost impact on the State. It is important also to provide an analysis of the cost impact on employees (out-of-pocket costs). While analyses of financial impacts from the employer's perspective focus on average costs over the course of the plan year, employee cost impacts can be viewed as more personal and variable month-to-month.

When looking at cost-neutrality, over the course of the year the HDHP+HSA plan option is cost neutral to the employee as well. However, when comparing the Uniform Standard HMO to the HDHP+HSA financial impact for each month during the year, there are differences.

The charts below compare the relative values for the two plans for each month. In the earlier months in the year, the HDHP+HSA plan option exhibits a much lower relative value than the Uniform Standard HMO due to the differences in the deductibles (i.e., more costs are borne by the employee). In the month of April, however, the two plans are roughly cost neutral, and each month thereafter the HDHP+HSA exhibits a higher relative value than the HMO for each month.

Single Coverage

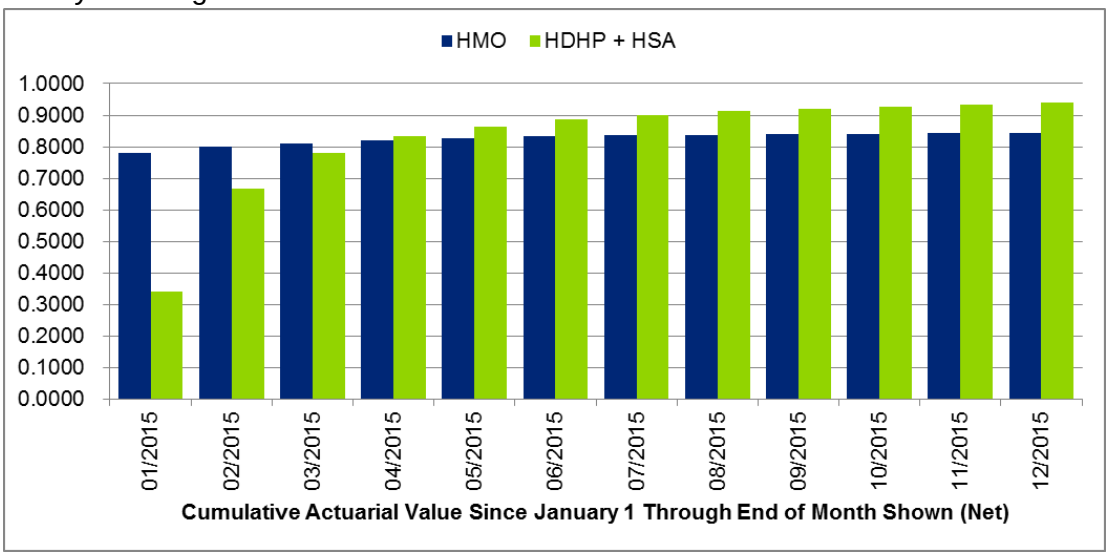


Such differences in the early months of the year may pose a barrier to attracting enrollment from those employees who are more concerned about the monthly

budget-ability of the HDHP+HSA health plan costs. There may also be some post-enrollment reaction from employees once they start incurring plan costs about their respective levels of understanding of the financial impacts of the new plan option.

For family coverage, the results are similar, as is shown in the chart below.

Family Coverage

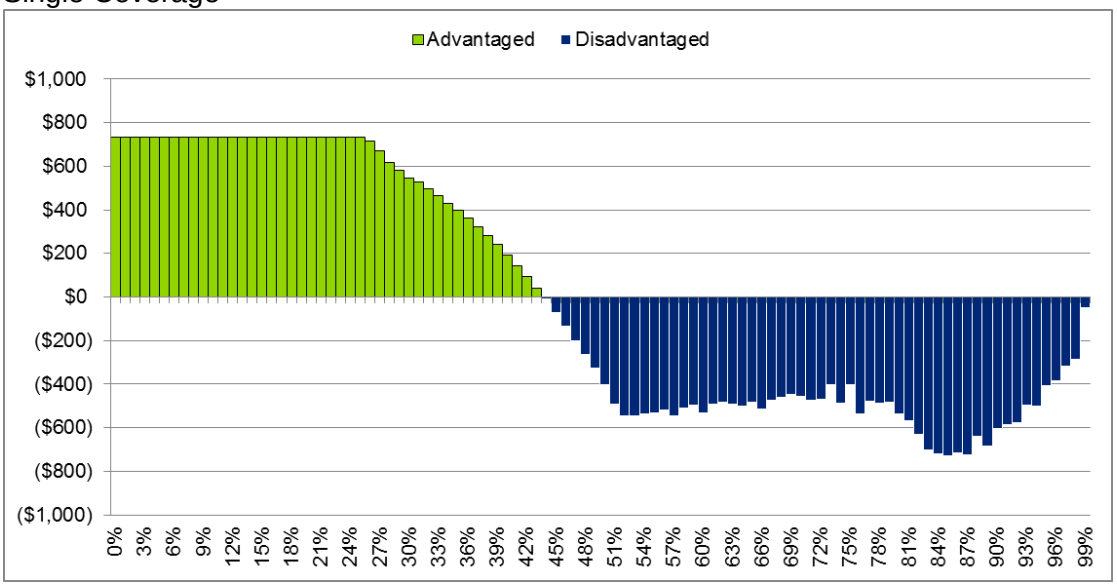


As discussed above with the single coverage, many of the same financial impacts to employees are seen for the family coverage.

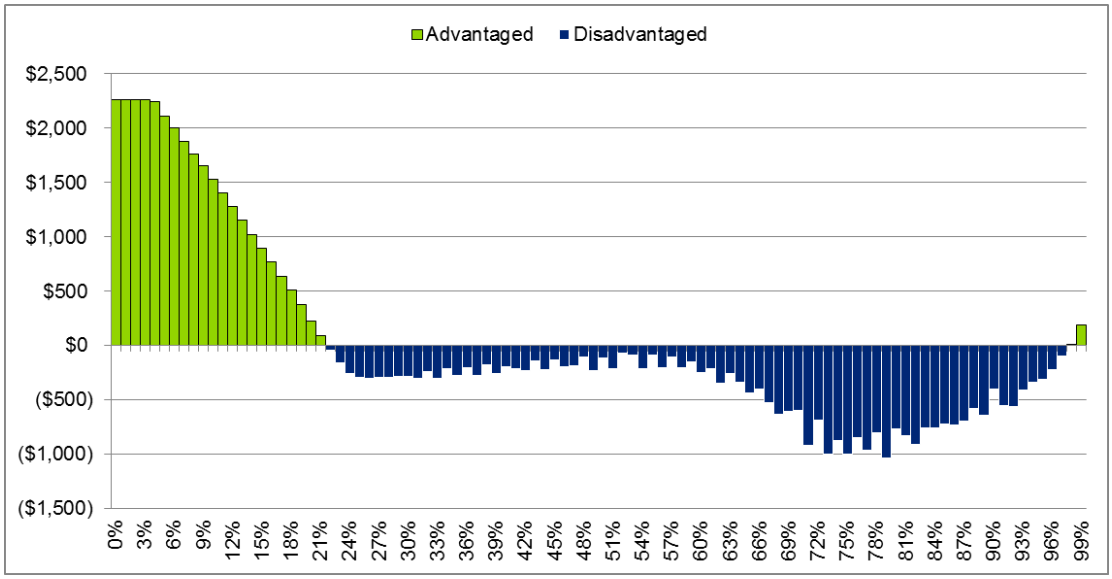
There are variations in employee financial impact when looking at different levels of claims incurred during the year. Employees who utilize fewer health plan services will generally be financially advantaged by the HDHP+HSA plan option. Employees with moderate to high utilization of health plan services will generally be financially disadvantaged by the HDHP+HSA plan option. And those employees with the very highest utilization of health plan services will, in general, by neither advantaged nor disadvantaged by the HDHP+HSA plan option.

The charts below illustrate the level of advantage or disadvantage expected for employees with single versus family coverage on a percentile basis. Those employees with the lowest claims utilization will be seen on the left side of each chart (low percentiles), those with moderate claims utilization levels will fall toward the 50th percentile, and those with the highest claims utilization will fall to the right side of the charts (high percentiles).

Single Coverage



Family Coverage



Employees who have a better prospective understanding of their health care AND who understand the financial workings of the two options will be more likely to exhibit adverse selection in their election of a 2015 health option.

Finally, with respect to the cost impact to annuitants, because the HDHP and Uniform Standard HMO have been actuarially priced without any adjustments for adverse selection, the intent is that the Uniform Standard HMO rates will not be any higher than would have been the case had a HDHP+HSA option not been offered. In this way, HMO annuitants are not expected to be adversely impacted financially just by virtue of a HDHP+HSA plan option being offered. The annual vendor negotiation process should include this objective as well in its discussions to continue to insulate the annuitants from any adverse financial impact.

Summary

For 2015 and after, from an actuarial perspective, Deloitte does not believe that the HDHP+HSA plan option as presented here represents an additional cost to the State over and above what would otherwise be experienced by offering just the Uniform Standard HMO plan option.

While actual experience will likely differ from the projections provided here, the level of employer funding of the HSA and the HDHP+HSA plan option employee contributions do present the mechanisms to avoid any additional costs.

And once the health reform excise tax starting in 2018 is effective, the HDHP+HSA plan option will experience lower potential exposure to this tax.

We would be happy to discuss the analyses and/or conclusions presented in this report further.

Daniel R. Plante

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