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STATE OF HAWAII
DEPARTMENT OF BUDGET AND FINANCE

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MANAGEMENT DIVISION
FINANCIAL ADMINISTRATION DIVISION

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OFFICE OF THE AUDITOR
STATE OF HAWAII

Ms. Marion M. Higa
State Auditor
Office of the Auditor
465 S. King Street, Room 500
Honolulu, Hawaii 96813-2917

Dear Ms. Higa:

The Department of Budget and Finance (DB&F) has reviewed the draft Actuarial Study and Operational Audit of the Public Employees Health Fund. We are in general agreement with the recommendations contained in the draft report. Specific comments are provided as follows:

1. Reduce Potential for Adverse Selection

The Legislature authorized the porting of employer contributions as a means of expanding employee/retiree choices in health care. However, porting reduces the pool of participants and possibly results in adverse selection. Cautious of the financial consequences, we have opposed measures that increase the potential for adverse selection. For example, we recently opposed House Bill No. 762 which authorizes payment of Medicare Part B reimbursements to employee-beneficiaries and their spouses who are enrolled in an employee organization supplemental Medicare plan. A major exodus of retirees could result in higher premium rates and higher total costs should Health Fund enrollee levels be reduced, low risk enrollees leave and high risk enrollees remain.

The Employer-Union Trust is an alternative means of providing employee health benefits. We have supported studying this concept to the extent: 1) potential cost savings are generated; 2) the Board of Trustees is comprised of the Director of Finance and equal representatives from the unions and the public sector; 3) a single trust is established to minimize administrative costs; and 4) inclusion of retirees is satisfactorily addressed.

2. Composition of the Board of Trustees

The Department believes that in addition to the Director of Finance, the Board of Trustees should be comprised of equal representatives from the unions and the public sector.

The report further finds that knowledge of employee health benefit programs and their financing should be required for at least some of the members of the Board. During the 1998 session, the Administration submitted legislation to address concerns on the composition of the Health Fund Board. Senate Bill No. 2816 proposed the replacement of the clergy member of the Board with a private citizen for the purpose of providing greater flexibility in response to the evolving dynamics and complexities of the health care industry. Senate Bill No. 2816 failed to pass.

3. Increase Carrier Participation

The Department agrees with the recommendation that more carriers should be encouraged to participate in the program. The recent enactment of House Bill No. 1042, House Draft 2 (Act 25/99), an Administration measure, addresses the Legislative Auditor's recommendation to encourage carrier program participation by removing the requirement for statewide service capability.

4. Restructure Program Design for Cost Containment

The Department is deeply concerned with the rising costs of health benefits. It would, however, be extremely difficult to achieve substantial cost savings under the current statutes. Several variables affect the cost of providing health benefits for State and County employees and retirees including: benefit levels, negotiated premium rates, the number of enrolled actives and retirees opting for self or family plan, and the contribution rates negotiated through the collective bargaining process. In order to achieve any real cost savings, changes to one or more of these variables are required.

In an attempt to control costs, the Administration submitted House Bill No. 1060 during the 1999 legislative session but it was held by the Senate Committee on Commerce and Consumer Protection. This Bill provides a viable option to reduce cost by eliminating employer health benefit contributions for dependents of employees hired after June 30, 1999. In addition, when these employees retire, it limits the employer contributions to a percentage based on the employee's years of service as applied to a self-only plan. Savings would initially be

limited, approximately \$1.6 million over the fiscal biennium 2000-2001. Over the long run, however, this plan would result in substantial savings, especially when employees hired after June 30, 1999 begin to retire.

The Administration also submitted a measure (House Bill No. 1048/Senate Bill No. 1294) to mandate participation by eligible employee-beneficiaries and their spouses in the federal medicare plan for voluntary medical insurance coverage. This measure would reduce employer premium contribution costs. As of April 30, 1999, House Bill No. 1048 was in Conference Committee. Senate Bill No. 1294 was reported as Conference Draft 1 and contains language from the Administration's initial proposal.

5. Disposition of Excess Reserves Created by Employee Contributions

The Department agrees with the recommendation that the Board should work closely with the Legislature, the Department of Budget and Finance, and the Department of the Attorney General to resolve disposition of excess reserves created by employee contributions. Section 87-22.3, Hawaii Revised Statutes (HRS), permits carrier rate credits or reimbursement derived from employee-beneficiary contributions to be utilized only to improve health benefit plans or to reduce employee-beneficiary monthly contributions.

To resolve the issue of excess reserves, we submitted House Bill No. 1041/Senate Bill No. 1287 in the 1999 legislative session to permit return of the employee's share of insurance carrier refunds and rate credits to employee-beneficiaries based on their years of benefit plan participation. House Bill No. 1041 became a vehicle bill for the Employer Union Trust Fund pilot project and Senate Bill No. 1287 failed first lateral.

6. Audit Employee Organization Health Benefit Plans

The Department believes employee organizations which receive "ported" funds should be accountable and subject to the same provisions imposed on the Health Fund regarding return of carrier rate credits and reimbursements. The Administration submitted House Bill No. 1049/Senate Bill No. 1295 to: 1) clearly authorize the examination and audit of employee organization plan enrollment and financial transactions; and 2) require employee organizations providing health and life insurance programs to return to the Health Fund the employer's share of any rate credits or reimbursements from any carrier or self insurance plan and interests derived thereon. House Bill No. 1049 was held by the Senate Committee on Commerce and Consumer Protection and Senate Bill No. 1295 was never heard by the Senate.

7. Long-Term Care Plan

As noted in our comments provided on the Legislative Auditor's Financial Report of the Hawaii Public Employees Health Fund of the State of Hawaii, trust funds are included in the Fiscal Biennium 2000-2001 Budget request to implement the Long-Term Care program.

Thank you for the opportunity to comment on the report.

Aloha,



E. I. ANZAI
Director of Finance