Items 6 and 7 Files 11-0069 & 11-0076	Department(s): Health Service System (HSS)

EXECUTIVE SUMMARY

Legislative Objective

- The proposed ordinance (File 11-0069) would amend Section 16.703 of the City's Administrative Code, to (a) approve the FY 2011-2012 health plans offered by the Health Service System (HSS) to its members and (b) set the employer's and members' contributions for the monthly health plan premiums.

- The proposed resolution (File 11-0076) would establish the monthly employer contribution to the Health Service System Trust Fund for FY 2011-2012. The monthly employer contribution is based on the results of the ten-county survey conducted by the Health Service Board, as required by the Charter.

Fiscal Impact

- Based on the results of the ten-county survey conducted by the Health Service Board, the employer's FY 2011-2012 contribution to the Health Service System Trust Fund is $503.94 per member per month, which is an increase of $31.09 or 6.6 percent from the FY 2010-2011 employer's contribution of $472.85 per member per month.

Policy Issues

- Implementation of the Federal Patient Protection and Affordable Care Act (PPACA) of 2010, effective July 1, 2011, increases healthcare coverage and increases the monthly health plan premiums for all three health plans.

- The City and County will bear a substantial and increasing proportion of the costs for the two HMO providers, Kaiser and Blue Shield, with City employees bearing a significantly smaller percentage of the costs.

Recommendations

- Approve the proposed ordinance and resolution.

MANDATE STATEMENT/BACKGROUND

Under Section A8.423 of the City Charter, the Health Service Board is required to (a) conduct a survey of the ten most populous California counties each year, excluding San Francisco, and (b) determine and set the employer's contribution for member health plans' monthly premiums, which is equal to the average of the contributions made by each of the ten counties.

The Health Service Board oversees the Health Service System and adopts the annual health plans and employer and member[1] contributions to monthly premiums. The Health Service System (HSS) administers non-pension benefits, including health, dental, vision, and other benefits that may be available to City employees, such as life and disability insurance.

DETAILS OF PROPOSED LEGISLATION

File 11-0069: The proposed ordinance would amend Section 16.703 of the City's Administrative Code to (a) approve the FY 2011-2012 health plans offered by the Health Service System (HSS) to its members and (b) set the employer's and members' contributions for the monthly premiums of the City Health Plan, Kaiser, and Blue Shield plans.

The Health Service Board approved these plans and employer's and members' contributions to the plans' monthly premiums on January 13, 2011.

File 11-0076: The proposed resolution would approve the FY 2011-2012 employer's contribution to the Health Service System Trust Fund[2] of $503.94 per member per month, which is an increase of $31.09 or 6.6 percent from the FY 2010-2011 employer's contribution of $472.85 per member per month. The proposed FY 2011-2012 employer's monthly contribution is based on the results of the ten-county survey, as shown in Attachment I, provided by HSS.

THE FY 2011-2012 HEALTH, DENTAL AND VISION PLANS' MONTHLY PREMIUMS

Proposed Monthly Premiums and Benefits for the Health Plans and Vision Plans

In FY 2011-2012, HSS will offer three health plans, including one self-funded health plan, the City Health Plan, and two plans provided through third-party insurers, Kaiser and Blue Shield. The City Health Plan is a preferred provider organization, or PPO, which provides services through a network of providers. Both Kaiser and Blue Shield are health maintenance organizations, or HMOs, which provide services through a closed panel of providers. HSS will offer one vision plan provided through third-party insurer, VSP Vision.

[1] HSS employers include the City and County of San Francisco, the San Francisco Unified School District, the San Francisco Community College District, and the San Francisco Superior Court. HSS members are active and retired employees of these employers, their dependents, and members of eligible boards and commissions. Dependents include children, spouses, domestic partners, surviving spouses of deceased employees, and other legal dependents.

[2] Under the Charter, the Health Service System Trust Fund receives all contributions and pays all health plan expenses.

As of January 1, 2011, there are approximately 56,932 active and retired HSS members who currently receive health benefits through the City, as shown in Table 1 below.[3]

Table 1: Active and Retired HSS Members

	Active Employees	Retired Employees	Total	Percent
City Health Plan	1,228	5,495	6,723	11.81%
Kaiser	17,207	9,525	26,732	46.95%
Blue Shield	17,230	6,247	23,477	41.24%
Total	**35,665**	**21,267**	**56,932**	**100.00%**

Source: Health Service System, as of January 1, 2011

Monthly Premium Increases for the Employer and Employees: Both the employer and members contribute to the total monthly premium. The proposed FY 2011-2012 monthly premiums for the three health plans and the vision plan are shown in Table 2 below for single employees (without dependents). Additional premium information for active and retired employees are further detailed in Attachment II, provided by HSS. Members enrolled in one of the three HSS health plans also receive vision benefits. The monthly VSP Vision premium for employees is included in the total monthly premium for each of the three health plans, shown in Table 2 and in Attachment II.

Table 2: Comparison of FY 2010-2011 and FY 2011-2012 for the Medical and Vision Monthly Premiums for Single Employees

	Proposed FY 2011-2012	FY 2010-2011	Increase (Decrease)	Percent Change
City Health Plan	1,110.87	$926.66	$184.21	19.9%
Kaiser	505.22	481.69	23.53	4.9%
Blue Shield	589.40	593.73	4.33	-0.7%

Source: Health Service System

As shown in Table 2 above, the total City Health Plan monthly premium for single employees is increasing by $184.21 or 19.9 percent, from $926.66 in FY 2010-2011 to $1,110.87 in FY 2011-2012. As noted on page 1 of the January 25, 2011 letter to the Board of Supervisors from Mercer (Attachment III), the HSS consultant and actuary, the monthly premium for single employees under the City Health Plan "represents the best estimate of future expenditures based on the information available at the time they were developed".

Also shown in Table 2 above, (a) the total Blue Shield monthly premium for single employees is decreasing by $4.33 or 0.7 percent, from $593.73 in FY 2010-2011 to $589.40 in FY 2011-2012, and (b) the total Kaiser monthly premium for single employees is increasing by $23.53 or 4.9 percent, from $481.69 in FY 2010-2011 to $505.22 in FY 2011-2012. As noted on page 1 of Attachment III, the insured premiums and administrative fees agreed to with Kaiser and Blue Shield "represent a fair price given the services provided and the risks insured".

[3] HSS has a total of approximately 109,237 members of the City and County of San Francisco, San Francisco Unified School District, Superior Court, and the Community College District.

HSS is making several substantive changes in each of the three health plans to comply with provisions of the Federal Patient Protection and Affordable Care Act of 2010 (PPACA), which will be effective in FY 2011-2012. (See Patient Protection and Affordable Care Act of 2010 in the Policy Issues section below.) Consequently, as noted on page 2 of Attachment III, the health plans' monthly premiums were presented and adopted by the Health Services Board.

The Health Service Board recommends one additional change to the FY 2011-2012 City Health Plan, an increase in the non-formulary drug copayment from $35 to $45 for retail and from $70 to $90 for Mail Order to incentivize members to use generic drugs.

Monthly Premium Increases for the Employer: The increases and decreases to the monthly premiums for single employees (without dependents) of the three health plans, as shown in Table 2 above, are shared by both the employer and the members. As shown in Table 3 below and also further detailed in Attachment IV, provided by HSS, the monthly increase to the employer's contribution is $31.09 or 6.58 percent. As noted above, the increase in the employer's FY 2011-2012 contribution is based on the results of the ten-county survey. As shown in Table 3 below and also further detailed in Attachment IV, there would be significant reductions in employee contributions for both Kaiser and Blue Shield health plans in FY 2011-2012.

Table 3: Comparison of FY 2010-2011 and FY 2011-2012 Medical and Vision Monthly Premiums for Single Employees by Employer and Employee Contribution

	Total Contribution	Employee Contribution				Employer Contribution			
	Proposed FY 2011-2012	Proposed FY 2011-2012	FY 2010-2011	Increase (Decrease)	Percent Change	Proposed FY 2011-2012	FY 2010-11	Increase (Decrease)	Percent Change
City Health Plan	$1110.87	$606.93	$453.81	$153.12	33.74%	$503.94	$472.85	$31.09	6.58%
Kaiser	$505.22	$1.28	$8.84	-$7.56	-85.52%	$503.94	$472.85	$31.09	6.58%
Blue Shield	$589.40	85.46	120.88	-$35.42	-29.30%	$503.94	$472.85	$31.09	6.58%

Source: Health Service System

Proposed Monthly Premiums and Benefits for the Dental Plans

In FY 2011-2012, HSS will offer three dental plans including one PPO plan, the Delta Dental, and two HMO plans, DeltaCare USA and UHC Dental. The Delta Dental Plan is a dental PPO with a network of preferred providers. The Delta Dental plan is (a) self-insured through HSS for active members and (b) fully insured for retirees. The DeltaCare USA and UHC Dental Plans are dental HMOs with a closed panel of providers and are fully insured plans. Retirees pay for their individual dental coverage, such that there is no employer contribution for retiree dental plans.

Employers, including only the City and the Superior Court (not including the San Francisco Unified School District and the Community College District), pay the dental plan premiums for active members. The employer contributes the average cost of employees' monthly dental plan premiums. As shown in Table 4 and in Attachment V, the employer's contribution for dental benefits increased from $131.94 per member per month in FY 2010-2011 to $137.70 per member per month in FY 2011-2012, an increase of $5.76 per month, or approximately 4.4 percent.

Table 4: Comparison of FY 2010-2011 and FY 2011-2012 for the Dental Monthly Premiums for Single Employees

	Proposed FY 2011-2012	FY 2010-2011	Increase	Percent Change
Delta Premier, DeltaCare USA and UHC Dental.	$137.70	$131.94	$5.76	4.4%

Source: Health Service System

FY 2011-2012 CONTINGENCY AND STABILIZATION POLICIES AND AMOUNTS

In October 2007, the Health Service Board approved policies designating a portion of the Health Service System Trust Fund balance to: (a) provide contingencies for HSS's self-funded City Health Plan and self-funded employee dental plan and (b) stabilize City Health Plan and employees' dental plan premium increases by including prior years' premium revenue surpluses or shortfalls when calculating required premiums in the new plan year.

Contingency Fund: The Contingency Fund is intended to protect against shortfalls in the Health Service System Trust Fund's claims reserve for the self-funded City Health Plan and employee dental plan, resulting from higher than expected claims compared to premium payments. For the past three fiscal years, HSS has reviewed the contingency policy amount annually to assess the adequacy of the contingency to meet potential claims liability, and will increase the contingency amount as necessary.

As shown in Table 5 below, the Contingency Fund amount has increased every year since FY 2008-2009.

Table 5: Contingency Fund Increases

	City Health Plan	Dental Plan	Total	Increase	Percent Change
FY 2008-2009	$10,200,000	$3,000,000	$13,200,000	--	--
FY 2009-2010	$10,700,000	$3,100,000	$13,800,000	$600,000	4.54%
FY 2010-2011	$10,800,000	$3,300,000	$14,100,000	$300,000	2.17%
FY 2011-2012	$10,900,000	$3,600,000	$14,500,000	$400,000	2.84%

Source: Health Service System

According to Ms. Robin Courtney, Chief Financial Officer of HSS, and shown in Table 5 above, HSS will increase the total contingency amount by $400,000, or 2.84 percent, from $14,100,000 in FY 2010-2011 to $14,500,000 for FY 2011-2012. The increases to the contingency amounts has already been included in the FY 2011-2012 City Health Plan and dental monthly premiums as listed in Table 2 above and Table 4 above.

Stabilization Policy: In addition to the Contingency Fund, the Health Service Board has adopted a stabilization policy. Under this stabilization policy, HSS will incorporate the City Health Plan's

actual premium revenue[4] surpluses[5] or shortfalls[6] from a prior audited year, over a period of three years, when calculating required premiums in the new plan year.

In FY 2010-2011 the Health Service Board approved a $1,200,000 surplus stabilization amount for the City Health Plan. This stabilization amount of $1,200,000 was included when calculating the monthly premiums for FY 2010-2011. The Health Service System has calculated and the Health Service Board has approved a $1,000,000 shortfall stabilization amount for FY 2011-2012. This $1,000,000 stabilization amount has been incorporated into the calculations for determining FY 2011-2012 monthly premiums.

In FY 2010-2011 the Health Service Board approved a $1,300,000 shortfall stabilization amount for the Delta Dental Plan. This stabilization amount of $1,300,000 was included when calculating the monthly premiums for FY 2010-2011. The Health Service System has calculated and the Health Service Board has approved a $2,500,000 shortfall stabilization amount for the Delta Dental Plan for FY 2011-2012. This $2,500,000 stabilization amount has been incorporated into the calculations for determining FY 2011-2012 monthly premiums.

FISCAL ANALYSIS

Fiscal Impact of the FY 2010-2011 Health Plan Premium Contributions is Not Known

The Budget and Legislative Analyst notes that based on the City's FY 2010-2011 existing monthly premium rates, the total cost for FY 2010-2011 health and dental premium contributions to the Health Service System was $323,116,874, including City General Fund costs of $185,248,468, as approved in the FY 2010-2011 budget.

According to the Controller's Office, the City's total estimated cost for FY 2011-2012 health and dental premium contributions to the Health Service System Trust Fund was not available as of the writing of this report. The Controller's Office is waiting for additional information from Health Service Systems, which is needed to calculate these costs, including those to the City's General Fund.

[4] Premium revenue is the actual amount of monthly premium collected less the actual amount of health expenses and administrative costs claimed.

[5] Premium revenue surpluses are when more money is collected in monthly premiums than health expenses and administrative costs expended.

[6] Premium revenue shortfalls are when less money is collected in monthly premiums than health expenses and administrative costs expended.

Health Service System Trust Fund Balance

The FY 2009-2010 financial audit, conducted by a private auditing firm, KPMG LLP, found that the Health Service System Trust Fund in FY 2009-2010 had increased by $800,000, or 5.97 percent, from FY 2008-2009, as shown below.

Fund Balance as of June 30, 2010[7]	$14,200,000
Fund Balance as of June 30, 2009	$13,400,000
Increase	$800,000

According to the Ms. Courtney, this increase in the Trust Fund balance resulted from (a) an increase of $1,600,000 in revenues from performance guarantee penalties, (b) increase of $900,000 in interest income and (c) an increase in fair market value of assets offset by a shortfall in contributions of $1,700,000.

POLICY ISSUES

Implementation of the Federal Patient Protection and Affordable Care Act (PPACA) of 2010 Increases Healthcare Coverage and Increases the Monthly Health Plan Premiums

The Federal PPACA has established several requirements affecting medical, dental, and vision coverage which go into effect on July 1, 2011. The first requirement mandates dependent children be eligible for healthcare coverage until their 26th birthday and impacts health, dental, and vision coverage. The second requirement mandates that no lifetime dollar limits be placed on essential health benefits and primarily impacts the City Health Plan. The third requirement mandates that no annual dollar limits be placed on essential health benefits and impacts all health plans. The fourth requirement mandates that preventive services provided within the health network be fully covered with no deductibles or co-pays and impacts all health plans. The fifth requirement mandates that medicals plans update their claims and appeals process to comply with new standards established under the PPACA and impacts all health plans. As a result of these requirements, as shown in Table 6 below, premium rates for all three health plans have increased.

[7] Does not include the Contingency Fund amount.

Table 6: Summary of Impact of Federal Patient Protection and Affordable Care Act of 2010 on Premium Rates for Medical Plans		
Plan	**Percent Change for Active Employees/Non-Medicare Retirees**	**Percent Change for Medicare Retirees**
The City Health Plan	1.4%	1.0%
Kaiser	0.5%	2.8%
Blue Shield	0.2%	0.9%
Source: Health Service System		

City and County of San Francisco Bears a Substantial Portion of the Costs for Both HMO Providers

Based on Table 1 above, over 88.2 percent of active and retired City employees opt into one of the two HMOs, either Kaiser or Blue Shield, with the remaining 11.8 percent using the City Health Plan. As shown above in Table 2, in FY 2011-2012 the total cost of medical and vision monthly premiums for (a) Blue Shield would decrease by $4.33 or 0.73 percent, (b) Kaiser would increase by $23.53 or 4.89 percent, and (c) City Plan would increase by $184.21 or 19.88 percent.

Yet, as shown in Table 3 above, the City and County will bear an increased proportion of the costs for Blue Shield and Kaiser, while the City employees' contributions in these two HMOs decreases. For FY 2011-2012, employee contributions for Kaiser will decrease 85.52 percent to $1.28 per month per employee out of the total monthly cost of $505.22. Similarly, as shown in Table 3 above, employee contributions for Blue Shield will decrease 29.30 percent to $85.46 per month per employee out of the total monthly cost of $589.40. For FY 2011-2012, employee contributions for the City Health Plan will rise by 33.74 percent. Although, as shown in Table 3 above, the employer contributions for all three plans would rise by 6.58 percent, as shown in Table 7 below, the City will pay 99.75 percent of the costs for Kaiser employees, and 85.5 percent of the costs for Blue Shield employees.

Table 7: Comparison of Employer and Employee Contributions for FY 2011-2012 Medical and Vision Monthly Premiums for Single Employees

	Total Contribution	Employee Contribution	Employee Contribution Percentage of Total Contribution	Employer Contribution	Employer Contribution Percentage of Total Contribution
City Health Plan	$1,110.87	$606.93	54.64%	$503.94	45.36%
Kaiser	$505.22	$1.28	0.25%	$503.94	99.75%
Blue Shield	$589.40	$85.46	16.92%	$503.94	85.50%
Source: Health Service System					

The Budget and Legislative Analyst therefore notes that based on the current system for determining employer's (City's') contribution, determined by the results of a 10-county survey as explained above, the City continues to bear an unusually large and growing proportion of the costs of HMO care. Given the increasing concern regarding health and pension benefit costs, the Board of Supervisors may want to consider submitting a charter amendment to the electorate to revise the way the employer's (City's) costs are calculated to more equitably share the costs of health care between employees and their employer (City).

RECOMMENDATIONS

Approve the proposed ordinance and resolution.

10-County Survey

Exhibit 1
10-County Amount -- Change from 2010-11 to 2011-12

	2011-12	2010-11	Percent Change
1 Los Angeles	$478.56	$457.56	4.60%
2 San Diego	406.00	364.00	11.50%
3 Orange	434.41	383.75	13.20%
4 Riverside	513.02	488.44	5.00%
5 San Bernardino	399.70	397.51	0.60%
6 Santa Clara	655.97	608.44	7.80%
7 Alameda	541.06	521.89	3.70%
8 Sacramento	637.98	561.35	13.70%
9 Contra Costa	521.90	495.15	5.40%
10 Fresno	450.80	450.43	0.10%
10-County Average	**$503.94**	**$472.85**	**6.57%**

6 & 7 - 10

Attachment I

City Health Plan – Full Monthly Premium Equivalent

	2011-12					
	Before Claims Stabilization and Closedown Amount	Claims Stabilization[2]	Flex-Funded Closedown Amount	After Claims Stabilization and Closedown Amount	Dollar Change[3]	Percent Change[3]
Employee Only	$ 1,096.47	$ 14.40	$ -	$1,110.87	$184.21	19.9%
Employee + 1 Dependent	2,150.39	28.25	0.00	2,178.64	366.64	20.2%
Employee + 2 or more Dependents	3,016.11	39.62	0.00	3,055.73	512.97	20.2%
Retiree without Medicare	1,271.02	16.70	0.00	1,287.72	218.33	20.4%
Retiree and Spouse without Medicare	2,499.47	32.84	0.00	2,532.31	434.82	20.7%
Retiree with Medicare	376.92	4.97	0.00	381.89	14.01	3.8%
Retiree and Spouse with Medicare	720.18	9.48	0.00	729.66	27.97	4.0%

	2010-11			
	Before Claims Stabilization and Closedown Amount	Claims Stabilization[2]	Flex-Funded Closedown Amount	After Claims Stabilization and Closedown Amount
Employee Only	$939.01	($13.97)	$1.62	$926.66
Employee + 1 Dependent	1,836.16	(27.32)	3.16	1,812.00
Employee + 2 or more Dependents	2,576.67	(38.34)	4.43	2,542.76
Retiree without Medicare	1,083.66	(16.13)	1.86	1,069.39
Retiree and Spouse without Medicare	2,125.46	(31.63)	3.66	2,097.49
Retiree with Medicare	372.79	(5.55)	0.64	367.88
Retiree and Spouse with Medicare	711.05	(10.58)	1.22	701.69

[1] Rates shown include medical, pharmacy, vision, expense, claims stabilization, and the federal Medicare Part D subsidy. The 2010-2011 plan year was the final year for the PacifiCare Flex Funded closedown.

[2] Reflects claims stabilization amount pursuant to the Board's Self-Funded Plan Funding Policy

[3] Change after Claims Stabilization and Flex Funded Closedown Amount.

HMOs – Full Monthly Premium Equivalent

Exhibit 4

HMOs -- Change in Full Monthly Premium Equivalent[1]

	2011-12			2010-11		
	Before Flex-Funded Closedown	Flex-Funded Closedown Amount	After Flex-Funded Closedown	After Flex-Funded Closedown	Dollar Change[2]	Percent Change[2]
Blue Shield						
Employee Only	$ 589.40	$ -	$589.40	$593.73	($4.33)	-0.7%
Employee + 1 Dependent	1,177.81	0.00	1,177.81	1,186.46	(8.65)	-0.7%
Employee + 2 or more Dependents	1,666.17	0.00	1,666.17	1,678.40	(12.23)	-0.7%
Retiree without Medicare	1,308.44	0.00	1,308.44	1,318.34	(9.90)	-0.8%
Retiree and Spouse without Medicare	1,896.85	0.00	1,896.85	1,911.07	(14.22)	-0.7%
Retiree with Medicare	378.81	0.00	378.81	383.84	(5.03)	-1.3%
Retiree and Spouse with Medicare	756.60	0.00	756.60	766.65	(10.05)	-1.3%
Kaiser						
Employee Only	$ 505.22	$ -	$505.22	$481.69	$23.53	4.9%
Employee + 1 Dependent	1,009.42	0.00	1,009.42	962.34	47.08	4.9%
Employee + 2 or more Dependents	1,427.91	0.00	1,427.91	1,361.29	66.62	4.9%
Retiree without Medicare	1,014.87	0.00	1,014.87	967.56	47.31	4.9%
Retiree and Spouse without Medicare	1,519.07	0.00	1,519.07	1,448.22	70.85	4.9%
Retiree with Medicare	355.13	0.00	355.13	346.99	8.14	2.3%
Retiree and Spouse with Medicare	709.24	0.00	709.24	692.94	16.30	2.4%

[1] Rates shown include HMO premium, vision, and expense components. The 2010-2011 plan year was the final year for the PacifiCare Flex Funded closedown and included in the 2010-2011 rates.

[2] Change from the 2010-11 full monthly premium equivalent

6, & 7 - 12

Attachment II
Page 2 of 3

Vision Benefits

Exhibit 7
VSP Vision Plan -- Change in Full Monthly Cost

	Member Contributions				
	Core Plan				Buy-up Plan[2]
	2011-12[1]	2010-11[1]	Dollar Change	Percent Change	2011-12
Employee Only	$3.78	$3.57	0.21	5.9%	6.09
Employee + 1 Dependent	7.58	7.15	0.43	6.0%	12.19
Employee + 2 or more Dependents	10.73	10.12	0.61	6.0%	17.24
Retiree without Medicare	$3.78	$3.57	0.21	5.9%	6.09
Retiree and Spouse without Medicare	7.58	7.15	0.43	6.0%	12.19
Retiree with Medicare	$3.78	$3.57	0.21	5.9%	6.09
Retiree and Spouse with Medicare	7.58	7.15	0.43	6.0%	12.19

[1] Core plan rates are built into the Rates & Benefits process and included in medical total premium rates. Vision plan rates are under a 36 month rate guarantee for the period July 1, 2011 through June 30, 2014.

[2] Buy-up Plan introduced in 2011-12 plan year. Contributions are 100% paid by employees. Contributions represent the difference between the Core Plan and the total premium cost of the Buy-up plan.

6 & 7 - 13

Attachment II
Page 3 of 3

Rhys Evans, FIA, ASA, MAAA
Partner

MERCER

Four Embarcadero Center, Suite 400
San Francisco, CA 94111-4156
+1 415 743 8758
Rhys.Evans@mercer.com
www.mercer.com

Board of Supervisors
City and County of San Francisco
City Hall Room 244
1 Dr. Carlton B. Goodlett Place
San Francisco, CA 94102

January 25, 2011

Subject: 2011-12 Plan Benefits, Rates, and Contributions

Honorable Members of the Board of Supervisors:

This letter serves to document our position as the consultant and actuary to the Health Service System (HSS) in regards to the recently completed rate and contribution setting process. This process was conducted under the direction of the Rates and Benefits Committee (the "Committee") of the Health Service Board. The rates, benefits, and contributions presented herein were approved by the full Health Service Board (the "HS Board") during their meeting on January 13, 2011.

In our opinion, the process was completed in a complete and thorough manner. In particular, it is our opinion that:

- The insured premiums and administrative fees agreed to with HSS's vendors represent a fair price given the services provided and the risks insured.
- The premium equivalents set for the HSS self funded programs (City Health Plan and Active Dental benefits) represent our best estimate of future expenditures based on the information available at the time they were developed.
- Existing Trust Fund assets are expected to be sufficient to protect the HSS trust against adverse claims experience.

City Contributions Under the 10-County Survey

According to the City Charter, the City's contribution towards medical benefits is determined by the results of a survey of the amount of contributions provided by the ten most populous counties in California. This survey is conducted annually by HSS Staff. For the 2011-12 plan year, the survey determined that the average monthly contribution increased 6.57% from $472.85 to $503.94. Exhibit 1 of the attachment presents the individual responses from this survey.

MERCER

Patient Protection and Affordable Care Act of 2010

On March 23, 2010, President Barack Obama signed into law the Patient Protection and Affordable Care Act of 2010 (PPACA). The law establishes health reform that expands access to coverage over the next several years. For compliance with PPACA, a number of plan changes are required for the 2011-12 plan year. A summary of these changes follows:

- **Dependent children will be eligible for healthcare coverage until their 26th birthday.** This applies regardless of whether the child is married, qualifies as a tax dependent or is a full-time student. This applies to medical, dental, and vision coverage.
- **No lifetime dollar limits on essential health benefits.** Medical plan can no longer limit the dollar amount of benefits that it will reimburse over an enrolled person's lifetime for essential health benefits. This primarily impacts the City Plan.
- **Restrict annual dollar limits on essential health benefits.** There will no longer be dollar limits on essential health benefits. This impacts all medical plans.
- **Provide mandated preventive services in network with no cost-sharing.** Routine preventive care services that are received from in-network providers will be 100% covered by all medical plans, with no deductibles or copays.
- **Establish and provide notice of internal and external appeals procedure.** Medical plans are required to update their claims and appeals process to comply with new standards under PPACA.

Below is a summary of the impact on the premium rates from the changes highlighted above:

Plan	Actives / Non-Medicare Retires	Medicare Retirees
The City Plan	+1.4%	+1.0%
Kaiser	+0.5%	+2.8%
Blue Shield	+0.2%	+0.9%

MERCER

Rates, Contributions, and Benefits for the City Health Plan

The City Plan is a self-funded plan administered by United Health Care (UHC). The medical and pharmacy monthly premium equivalent costs were set based on recent experience, with costs developed separately for actives, retirees without Medicare and retirees with Medicare based on group-specific experience. Additionally, we provided a retrospective analysis of historical rates and experience to examine the actual cost trends evident in the City Health Plan's recent claims data. These analyses were considered in conjunction with overall industry and normative data when determining the premium levels for the 2011-12 plan year (all analyses are on the www.myhss.org website as public documents).

As part of the annual Rates and Benefits process, the Committee, HSS and Mercer review the continued appropriateness and competitiveness of the benefit design for the City Plan. The HS Board was presented with many options and, in addition to the changes required by PPACA, adopted the following benefit changes for the City Plan:

- Increase the non-formulary drug copayment from $35 to $45 for Retail and from $70 to $90 for Mail Order; to incentivize members to use generic drugs

This estimated impact on non-Medicare premium equivalent rates was (0.2%) and on Medicare premium equivalent rates was (0.7%).

The UHC administration fees were increased by 1.5% from the prior year. The HSS administration load remains unchanged.

Exhibit 2 of the attachment summarizes the change in full monthly premium equivalents for the City Health Plan. Included in the premium equivalent rate, pursuant to the HS Board's Self Funded Plans' Funding Policy, is the application of the claims stabilization amount (see below). The closedown amount for the PacifiCare Flex Funded plan is no longer applicable, beginning in the 2011-12 plan year.

Exhibit 3 of the attachment summarizes the change in employee and retiree contributions for the City Health Plan. These contributions were determined in accordance with the City Charter. The exhibit does not include any City contributions negotiated for specific groups in addition to the 10-County amount.

Rates, Contributions, and Benefits for HMOs

Similar to the 2010-11 plan year, two HMOs are offered to HSS members

MERCER

Kaiser

Kaiser requested a premium increase of 5.1% for actives and retirees without Medicare. For retirees with Medicare, the requested premium increase was 2.5%.

Non-Staff Model HMO

A comprehensive vendor search was performed on the non-staff model HMO plan offering. The process was initiated in August 2010 and proposals received from the following vendors on September 29:

- Blue Cross of California
- Blue Shield of California
- Chinese Community Health Plan
- Health Net of California

The vendor search process was constructed to follow a two phased approach. During the first phase, the Selection Panel convened to score the proposals would identify the finalist vendors that, with the HS Board's direction, Mercer would negotiate final terms. The Selection Panel would then score the results of these negotiations and identify the vendor to be recommended to the HS Board as the successful non-staff model HMO vendor for the 2011-12 plan year.

Mercer completed its analysis of the proposals received over October and presented its findings to the Selection Panel at a meeting convened in the HSS offices on November 10. Based on the compiled scoring of the proposals by the Selection Panel, Blue Shield and Health Net were identified as the two vendors with the highest scores that would proceed to the finalist negotiations phase of the vendor search process. The results of this initial phase of the process were presented to the HS Board at the November Board meeting.

Subsequent to the November Board meeting, the Centers for Medicare & Medicaid Services (CMS) issued a letter to Health Net, immediately suspending enrollment of new members in their Medicare Advantage plan. Reasons cited included:

- Failure to demonstrate that corrective actions were taken from an August 2010 CMS audit
- Corrective actions were primarily around the administration of the Medicare Pharmacy Part D plan and non-compliance with CMS policies

MERCER

Due to the CMS sanctions applied to Health Net, it was determined by the HSS Director, in consultation with Chair of the Rates & Benefits Committee, to include Blue Cross of California as a third vendor finalist

On December 10, the finalist vendors provided Mercer with a response to follow-up questions developed by HSS and Mercer, including those raised at the November 18 Board meeting. The Selection Panel convened on January 5 to score the second and final phase of the vendor selection process. Based on this second phase scoring, Blue Shield was identified as the successful vendor to be recommended to the HS Board. The HS Board voted to approve Blue Shield as the 2011-12 non-staff model HMO vendor at the January Board meeting.

Blue Shield's initial proposal requested a 0.0% increase across all plans (actives, retirees without Medicare, and retirees with Medicare). This proposal was subsequently reduced to a (0.25%) decrease following negotiations

HMO Plan Design Changes

As part of the annual Rates and Benefits process, the Committee, HSS and Mercer review the continued appropriateness and competitiveness of the benefit design for the HMOs. The benchmark information (available on www.myhss.org website) reviewed suggested that certain sections of the plan design were outdated and did not reflect the impact from the continued high healthcare trends. The HS Board was presented with many options and adopted the following benefit changes for the Blue Shield (as Kaiser already has the desired incentives in their plan design, there were no plan design changes adopted for Kaiser outside those required to meet the requirements of PPACA):

- Increase hospital per admit copayment from $100 to $150; to incentivize members to use outpatient surgery when possible
- Increase non-formulary drug copayment from $35 to $45 for Retail and from $70 to $90 for Mail Order; to incentivize members to use generic drugs
- Inclusion (at an additional cost in aggregate of less than +0.2% to the premium rates) of transitional residential recovery services and residential rehabilitation under Chemical Dependency; to equalize with benefits currently offered by the Kaiser plan

As a result of the changes, 2011-12 active and non-Medicare retiree premiums were reduced by (0.35%) and the Medicare retiree premiums were reduced by (0.96%).

MERCER

Exhibit 4 of the attachment summarizes the full monthly HMO cost for the 2011-12 plan year. The application of the PacifiCare Flex Funded plan's closedown amount is not longer applicable, beginning in the 2011-12 plan year.

Contributions for HMO members were determined in accordance with the City Charter. Exhibits 5 and 6 of the attachment summarize changes in contributions for actives and retirees respectively.

The above exhibits do not include any City contributions negotiated for specific groups in addition to the 10-County amount.

Close out of PacifiCare Flex Funded Plan

During the 2009-10 plan year, the HS Board approved the process that the close out amount on the PacifiCare Flex Funded plan be amortized over two plan years across all remaining medical plans (City Health Plan, Kaiser & Blue Shield). Each plan was allocated a proportion of the close out liability based on their anticipated aggregate premium cost over the year of amortization.

The close-out liability has now been fully settled and as such, no further adjustments to the remaining plans' required contributions are necessary beginning in the 2011-12 plan year.

Rates and Benefits for the Vision Plan

Members enrolled in any medical plan offered by HSS also receive vision benefits through VSP. The cost of the vision benefit is a component of the cost of the medical plan and has been included in the rate exhibits referenced above. In addition to the core vision plan, beginning in July 1, 2011 members will have the option to elect a buy-up vision plan with enhanced vision benefits. Members are responsible to contributing 100% of the cost difference between the core and buy-up vision plan.

The vision plans are fully insured plans. As a result of a competitive renewal process, the final VSP requested premium rate increase was 6.0% for the core vision plan, with a rate guarantee through the end of the 2013-14 plan year. During the rates and benefit process, VSP has offered two plan enhancements to the core and buy-up vision plans, with no impact on premium rates. Below is a summary of the plan enhancements that were adopted by the HS Board:

MERCER

- Implement a $60 cap for contact lens fitting and evaluation charges to the member, applies only if member goes to a preferred VSP provider (negligible impact on premiums)
- Upgrade reimbursement schedule for out-of-network claims from a non-VSP provider (negligible impact on premiums)
  - Increase exam from $40 to $50
  - Increase Frames from $55 to $70

Exhibit 7 in the attachment summarizes the VSP vision plan costs for the core and buy-up plans.

Rates, Contributions, and Benefits for Dental Plans

Three dental plans are offered to HSS members: Delta Dental PPO, Delta Care USA and UHC Dental (formerly known as Pacific Union). The Delta Dental PPO plan is a dental PPO with a network of preferred providers while the other two plans are dental HMOs with closed panels of providers. The City pays the cost of dental benefits for employees, while retirees pay the full cost of their dental benefits.

The Delta Dental PPO plan for active employees is self-insured and administered by Delta Dental Plan of California. Future plan costs are projected based on the City employees' claim experience. Delta Dental's fee for claim administration remains unchanged from the 2010-11 fee and is guaranteed until the end of the 2012-13 plan year.

The Delta Dental PPO plan for retirees, Delta Care USA dental plans for employees and retirees, and UHC dental plans for employees and retirees are all fully insured. The rates for the Delta Dental PPO plan for retirees remain unchanged from the 2010-11 rates. The rates for the DeltaCare dental plan and UHC dental plan for employees and retirees also remain unchanged from the 2010-11 plan year.

As part of the annual Rates and Benefits process, the Committee, HSS and Mercer review the continued appropriateness and competitiveness of the benefit design for the active dental PPO plans and also compared the plan designs of the active to the retirees. The information (available on www.myhss.org website) reviewed suggested that certain sections of the plan design were outdated and the active plan did not align with the retiree plan. The HS Board adopted the following benefit changes for the active Delta Dental PPO plan:

- Include a third cleaning for pregnant women (estimated +0.4% impact on premiums or $200K a year)

MERCER

- Add an Implant benefit subject to the $2,500 annual per person plan maximum (estimated +2.6% impact on premiums or $1.1M a year). This benefit will be provided at the same member cost sharing level as currently available for crowns.

The City's per-employee contribution for dental benefits is based on the average cost of coverage for all employees. The monthly contribution for 2011-12 will be $137.70 per employee per month, an increase of 4.4% over the $131.94 per employee per month contributed for the 2010-11 plan year. Included in this per employee rate, pursuant to the HS Board's Self Funded Plans' Funding Policy, is the application of the claims stabilization amount of approximately $2.5 million (equivalent to $7.25 per employee per month) of accrued deficit, which represents the shortfall of contributions received from employers compared to the costs incurred over the 2009-10 plan year.

Exhibit 8 in the attachment summarizes the changes in cost for active employee dental benefits.

City retirees who elect dental benefits have three plans to choose from. Benefits and rates differ from those for active employees. Exhibit 9 in the attachment summarizes the changes in cost for retirees' dental benefits.

Summary of Projected 2011-12 Plan Year Costs

Set out below is a summary of how projected 2011-12 aggregate HSS plan costs are distributed across the different plans available to employees and retirees. Costs are shown only for those plans where the employers subsidize the total premium cost. The premium costs associated with the Vision Plan are embedded in the medical plans' costs.

MERCER

		Distribution of Aggregate Plan Costs ($millions)		
	Aggregate Plan Cost	Employers' (incl. bargained conts.) Contributions	Members' Contributions	Member Contributions as a % of Aggregate Costs
The City Plan[1]	$78.8	$62.6	$16.2	20.5%
% Increase	13.5%	10.5%	26.7%	
Kaiser[1]	$273.3	$249.8	$23.5	8.6%
% Increase	4.5%	5.0%	(0.1%)	
Blue Shield[1]	$294.1	$255.1	$39.0	13.3%
% Increase	(0.8%)	1.9%	(15.4%)	
Employee Dental	$47.5	$47.5	$0.0	0.0%
% Increase	4.4%	4.4%	0.0%	
Total	$693.7	$615.0	$78.7	11.3%
% Increase	3.1%	4.2%	(4.5%)	

The overall estimated increase of 3.1% compares favorably with the corresponding 2010-11 plan year estimated increase of 9.3%. Similarly, this year's projected aggregate cost increase also compares favorably with available benchmark information. Based on the recently published 2010 National Survey of Employer Sponsored Health Plans[1], anticipated 2011 post-benefit change cost increases within the governmental employers category is 6.3%. Within the category focusing on Northern California employers only (both public and private combined), the corresponding anticipated 2011 increase is 9.1%.

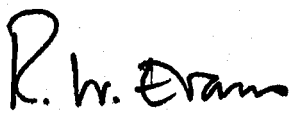
[1] Established in 1986, Mercer's *National Survey of Employer-Sponsored Health Plans* is the nation's largest, most authoritative annual survey on the topic of health benefits. The survey uses a national probability sample of U.S. employers with 10 or more employees (including local and state governments) stratified by employer size and region to ensure a representative mix of employers. Each year around 3,000 employers participate.

MERCER

Conclusion

Mercer would be pleased to answer any questions or provide clarification about the information included in this letter to any interested parties.

Sincerely,



Rhys Evans, FIA, ASA, MAAA

Copy:
Members of the Health Service Board
Catherine Dodd, Lisa Ghotbi, Robin Courtney, Health Service System
Gerry Murphy, Donna Kinsman, Mercer

Enclosure

c:\documents and settings\rhys-evans\my documents\bos letter 2011-12 py_final.doc

City Health Plan – Employee, Retiree, and Employer Contributions

Exhibit 3
City Health Plan – Change in Monthly Employee, Retiree, and Employer Contributions

	Member Contributions				Employer[1] Contributions			
	2011-12	2010-11	Dollar Change	Percent Change	2011-12	2010-11	Dollar Change	Percent Change
Employee Only	$ 606.93	$453.81	$153.12	33.7%	$ 503.94	$472.85	$31.09	6.6%
Employee + 1 Dependent	1,674.70	1,339.15	335.55	25.1%	503.94	472.85	31.09	6.6%
Employee + 2 or more Dependents	2,551.79	2,069.91	481.88	23.3%	503.94	472.85	31.09	6.6%
Retiree without Medicare	303.46	226.90	76.56	33.7%	984.26	842.49	141.77	16.8%
Retiree and Spouse without Medicare	925.75	740.95	184.80	24.9%	1,606.56	1,356.54	250.02	18.4%
Retiree with Medicare	-	-	-	N/A	381.89	367.88	14.01	3.8%
Retiree and Spouse with Medicare	173.88	166.90	6.98	4.2%	555.78	534.79	20.99	3.9%

[1] Excludes additional negotiated contributions which apply to certain collectively bargained employees

6 & 7 - 24

Attachment IV
Page 1 of 4

HMOs – Employee and Employer Contributions

Exhibit 5
HMOs -- Change in Monthly Employee and Employer Contributions

	Member Contributions				Employer[1] Contributions			
	2011-12	2010-11	Dollar Change	Percent Change	2011-12	2010-11	Dollar Change	Percent Change
Blue Shield								
Employee Only	$ 85.46	$120.88	($35.42)	-29.3%	$ 503.94	$472.85	$31.09	6.6%
Employee + 1 Dependent	673.87	713.61	(39.74)	-5.6%	503.94	472.85	31.09	6.6%
Employee + 2 or more Dependents	1,162.23	1,205.55	(43.32)	-3.6%	503.94	472.85	31.09	6.6%
Kaiser								
Employee Only	$ 1.28	$8.84	($7.56)	-85.5%	$ 503.94	$472.85	$31.09	6.6%
Employee + 1 Dependent	505.48	489.49	15.99	3.3%	503.94	472.85	31.09	6.6%
Employee + 2 or more Dependents	923.97	888.44	35.53	4.0%	503.94	472.85	31.09	6.6%

[1] Excludes additional negotiated contributions which apply to certain collectively bargained employees

6 & 7 - 25

Attachment IV
Page 2 of 4

HMOs – Retiree and Employer Contributions

Exhibit 6
HMOs -- Change in Monthly Retiree and Employer Contributions

	Member Contributions				Employer Contributions			
	2011-12	2010-11	Dollar Change	Percent Change	2011-12	2010-11	Dollar Change	Percent Change
Blue Shield								
Retiree without Medicare	$ 42.73	$60.44	($17.71)	-29.3%	$ 1,265.71	$1,257.90	$7.81	0.6%
Retiree and Spouse without Medicare	336.93	356.80	(19.87)	-5.6%	1,559.92	1,554.27	5.65	0.4%
Retiree with Medicare	-	-	-	N/A	378.81	383.84	(5.03)	-1.3%
Retiree and Spouse with Medicare	188.89	191.40	(2.51)	-1.3%	567.71	575.25	(7.54)	-1.3%
Kaiser								
Retiree without Medicare	$ 0.64	$4.42	($3.78)	-85.5%	$ 1,014.23	$963.14	$51.09	5.3%
Retiree and Spouse without Medicare	252.74	244.75	7.99	3.3%	1,266.33	1,203.47	62.86	5.2%
Retiree with Medicare	-	-	-	N/A	355.13	346.99	8.14	2.3%
Retiree and Spouse with Medicare	177.05	172.97	4.08	2.4%	532.19	519.97	12.22	2.4%

6 & 7 - 26

Attachment IV
Page 3 of 4

Dental Benefits – Active Employees

Exhibit 8
Dental Plans -- Change in Monthly Cost for Active Employees

	2011-12			2010-11				
	Before Claims Stabilization Amount	Claims Stabilization Amount[1]	After Claims Stabilization Amount	Before Claims Stabilization Amount	Claims Stabilization Amount[1]	After Claims Stabilization Amount	Dollar Change[2]	Percent Change[2]
Composite City Contribution[3]								
All Employees	$130.45	$7.25	$137.70	$128.30	$3.64	$131.94	$5.76	4.4%

[1] Total claims stabilization amount of approximately $0.1 million and $2.5 million applied to the 2010-11 and 2011-12 plan years respectively, pursuant to the Board's Self Funded Plans' Funding Policy

[2] Change from the 2010-11 composite rate, after the claims stabilization amount

[3] The composite rate reflects composites of the self-insured Delta Dental PPO and the two fully insured plans: Delta Care USA and UHC Dental (formally known as Pacific Union). The Delta Dental PPO Plan is self-insured by the City, with administrative fees unchanged from 2008-09 and guaranteed until the end of the 2012-13 plan year. The fully insured Delta Care USA plan premiums are guaranteed until the end of the 2012-13 plan year. The UHC Dental plan premiums remain unchanged from 2009-10 and are guaranteed until the end of the 2011-12 plan year.

6 & 7 - 27

Attachment IV
Page 4 of 4