



Report to Board of Administration

Agenda of: **JANUARY 26, 2010**

From:  Alex Rabrenovich, Chief Benefits Analyst

ITEM: **VIII-A**

SUBJECT: LACERS' PREMIUM STABILIZATION RESERVE FUNDING POLICY

Recommendation:

That the Board adopts the proposed resolution as LACERS' Premium Stabilization Reserve (PSR) funding policy.

Discussion:

On January 12, 2010, the Board approved staff's recommendation to adopt a policy of funding the LACERS' Anthem Blue Cross (ABC) PSR each year at a minimum rate of three times 5% of ABC's projected annual premium cost for the following year.

Staff has prepared a proposed resolution to formalize the PSR funding policy and make it applicable to any health insurance carrier with which LACERS may enter into an experience-rated refunding contract.

Attachment: Proposed Resolution for Premium Stabilization Reserve Funding Policy
Premium Stabilization Reserve Board Report of January 12, 2010

LACERS' PREMIUM STABILIZATION RESERVE FUNDING POLICY

PROPOSED RESOLUTION

WHEREAS, the Los Angeles City Employees' Retirement System (LACERS) administers a health and welfare program, which includes health insurance for retired employees and their eligible dependents;

WHEREAS, LACERS may enter into an experience-rated refunding contract with its health insurance carriers which requires year-end accounting after the close of a plan year to reconcile any differences between the amount of premiums paid to the carrier and the amount of claims and expenses associated with providing health coverage;

WHEREAS, these types of contracts contain an interest-earning Claims Stabilization Fund (CSF), which is required to maintain a certain balance, as directed by the carrier, to fund any deficits that may be found in the year-end accounting;

WHEREAS, these types of contracts may also include an interest-earning Premium Stabilization Reserve (PSR), into which year-end accounting surpluses beyond the CSF funding requirement are transferred and funds may be used to fund the CSF when year-end accounting deficits are greater than the CSF balance;

WHEREAS, LACERS may withdraw funds from the PSR for alternative uses;

WHEREAS, a minimum PSR balance should always be maintained and recalculated annually to offset possible year-end deficits;

WHEREAS, actuarially, there is a 90% probability that a deficit will be less than 5% of projected premiums for the following plan year;

NOW, THEREFORE, BE IT RESOLVED that the Board of Administration hereby adopts a Premium Stabilization Reserve (PSR) funding policy where the PSR is maintained at a minimum of three times 5% of the health plan's projected annual premium cost for the following plan year and that the Board review alternatives for the disposition of excess PSR funds annually.

January 26, 2010



Report to Board of Administration

Agenda of: **JANUARY 12, 2010**

From: Alex Rabrenovich, Chief Benefits Analyst

ITEM: **VIII-B**

SUBJECT: ANTHEM BLUE CROSS PREMIUM STABILIZATION RESERVE POLICY AND DISPOSITION OF EXCESS FUNDS

Recommendation:

That the Board adopt a Premium Stabilization Reserve (PSR) funding policy and approve use of excess PSR funds.

Discussion:

LACERS has an experience-rated refunding contract with Anthem Blue Cross (Anthem), which requires a year-end accounting after each calendar year. Anthem plan premiums are based on projected costs for the coming year. At the end of each plan year, a year-end accounting is conducted which compares Anthem's actual annual costs with the annual premium amount paid by LACERS and its members.

As part of the contract, LACERS has a Claims Stabilization Fund (CSF), which is required to maintain a certain balance, as determined by Anthem at the beginning of each plan year. The purpose of the CSF is to fund any deficits that may be found in the year-end accounting. In addition, LACERS has a Premium Stabilization Reserve (PSR) into which LACERS may transfer year-end surpluses after the CSF funding requirement is met. The PSR, which is not required by Anthem, also may be used to fund any deficits beyond the CSF, but only with LACERS' permission. Both the CSF and PSR are held in interest-earning accounts (CSF: 3% PSR: 3% in 2009; same rate projected for 2010).

Towers Watson (formerly Watson Wyatt), our health and welfare consultant, reviewed our Anthem year-end accounting. Highlights of their findings include:

- There was a surplus of \$2,205,280 for policy year 2008, approximately 6% of total premium paid, suggesting the premiums were set slightly higher than necessary
- \$2,186,725 of the surplus was transferred to the Premium Stabilization Reserve (PSR) – and the balance, \$18,555, was transferred to the Claims Stabilization Fund (CSF)
- The cumulative balance in the PSR as of 1/1/09 is \$11,499,968 after the transfer of funds
- The cumulative balance in the Claim Stabilization Fund as of 1/1/09 is \$910,920

Currently, LACERS does not have a policy regarding the disposition of excess PSR funds. In the past, once the year-end accounting was completed, our health and welfare consultant would evaluate the PSR account and recommend a course of action. There are several ways in which the excess PSR funds may be used. Some examples include:

- Premium defrayal for LACERS and its Anthem subscribers
- Return a portion of the surplus to LACERS for alternative investment/use
- Retain the excess PSR in the account in anticipation of increased claims
- Use to offset future premium increases

After review of our past practices and the surplus funds in our PSR, Towers Watson recommends the following actions be taken:

- Adopt a policy of funding the PSR each year at a minimum rate of three times 5% of Anthem's projected annual premium cost for the following year. For 2009, this amount would be \$5.1 million.
- Reduce funds in the PSR through a premium defrayal for our Anthem plans during the months of March and November of 2010

Staff concurs with Towers Watson's recommendations. Towers Watson will present its recommendations.

Note: Due to the transition to our current health and welfare consultant earlier this year, the presentation of this report has been delayed. Going forward, this report will be presented annually in June or July.

Attachment: Anthem 2008 Year-End Accounting, prepared by Watson Wyatt and Company