OFFICE OF GROUP BENEFITS - PROPOSED PRIVATIZATION STATE OF LOUISIANA

INFORMATIONAL REPORT
ISSUED AUGUST 24, 2011

LOUISIANA LEGISLATIVE AUDITOR
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LOUISIANA LEGISLATIVE AUDITOR
DARYL G. PURPERA, CPA, CFE

August 24, 2011

The Honorable Joel T. Chaisson, II,
President of the Senate
The Honorable Jim Tucker,
Speaker of the House of Representatives

Dear Senator Chaisson and Representative Tucker:

This report provides the results of our informational report on the proposed privatization of the Office of Group Benefits. I hope this report will benefit you in your legislative decision-making process.

We would like to express our appreciation to the management and staff of the Division of Administration and the Office of Group Benefits for their assistance.

Sincerely,

Daryl G. Purpera, CPA, CFE
Legislative Auditor

BDC:EFS:THC:dl

OGB PROPRIV 2011

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Louisiana Legislative Auditor

Daryl G. Purpera, CPA, CFE, Legislative Auditor

Office of Group Benefits - Proposed Privatization

August 24, 2011

Executive Summary

During fiscal year 2011, the State of Louisiana began to explore alternative methods of carrying out the statutory responsibilities of the Office of Group Benefits (OGB), including the sale, lease, or other transfer of tangible and/or intangible assets. OGB, as of June 26, 2011, had nearly 226,000 total covered lives, of which nearly 133,000 are covered employees and retirees.

This report was developed in an effort to provide information about:

(1) the timeline of events in relation to privatizing OGB's health plan(s);

(2) OGB's administrative costs;

(3) the Chaffe & Associates, Inc., report;

(4) privatization of health insurance agencies that may have occurred in other states;

(5) the role of the Legislature in relation to privatizing OGB's health plan(s);

(6) various factors that should be considered before the sale/lease of OGB;

(7) requests for proposals for a financial advisor; and

(8) an overview of OGB's operations.

Key issues include the following:

- The scope of the assessment in the May 6, 2011, request for proposal includes **any and all** health benefits programs offered by the State of Louisiana including, but not limited to, the OGB Preferred Provider Organization (PPO) plan, the self-insured Health Maintenance Organization (HMO) plan, and the self-insured consumer-directed health plan with a health savings account. The negotiations, as well as any resulting contract, may include any or all of these plans. Any proposal for plan alternatives and/or combination of services may be acceptable if the Governor and the Legislature conclude that the proposed plan alternatives and/or combinations of services are advantageous to the state.

Among the numerous possibilities that could be proposed by the selected financial advisor, the two most publicly discussed options are the privatization of the PPO and HMO plans and the sale/lease of OGB. The privatization of the PPO plan relates to a private company managing the PPO plan instead of the state, while the privatization of OGB relates to the sale/lease of all OGB's health benefit programs to a private company. The HMO is currently managed by a third-party administrator, Blue Cross and Blue Shield of Louisiana. In Senate Retirement Committee testimony, Commissioner Rainwater, in one instance, described the PPO and HMO being offered as a package.

- In regard to the privatization of the PPO plan, the Legislature has expressly charged OGB with the power and duty to negotiate contracts with various health providers [Louisiana Revised Statute (R.S.) 42:802(B)(8)(a)]. Furthermore, the Legislature has determined that these contracts shall be subject to review and final approval by the House Appropriations and Senate Finance committees [R.S. 42:802(B)(S)(d) and R.S. 49:968(B)(21)(c)].

- Legislative approval is necessary for the sale of the assets of OGB, including its monetary reserve fund. R.S. 42:854(C) states, "Notwithstanding any other provision of law to the contrary, any money received by or under the control of the Office of Group Benefits shall not be used, loaned, or borrowed by the state for cash flow purposes or any other purpose inconsistent with the purposes of or the proper administration of the Office of Group Benefits." Any proceeds from a sale of OGB assets, including its monetary reserve fund, would have to be placed into the State Treasury and be appropriated prior to their expenditure. It is unclear whether the purpose of R.S. 42:854(C) would restrict the use of any sale/lease proceeds.

- Any substantial changes to the function and role of OGB in regard to the administration and management of group insurance policies would require legislative action to amend applicable substantive laws addressing the resulting reorganization of the Executive Branch. This reorganization is, by Constitution, within the exclusive authority of the Legislature.

- On February 16, 2011, the State of Louisiana contracted with Chaffe & Associates, Inc., (Chaffe) to establish the fair market value of OGB's book of business as of January 31, 2011. The resulting report, dated June 3, 2011, concluded that the market value at January 31, 2011, was between $133 million and $217 million, assuming a five-year privatization term.

- Louisiana Legislative Auditor (LLA) staff contacted ten different states to determine if any of these states considered privatizing their state's health insurance agency. Of the ten states contacted, two states considered privatizing their state health insurance agency at some point in the past. Alabama considered privatizing its administrative risk pool; however, it was cost prohibitive to do so. Missouri also considered privatizing in the past, but no action was taken. Utah was the only state where the health insurance agency provided all the services.

Louisiana's OGB provided services for its PPO plan, but shared responsibilities with third-party administrators for other health plans.

- The sale/lease of OGB may result in higher insurance premiums to state employees under a private insurer because of an increase in marketing costs, premium taxes, necessary profit margin, and reinsurance costs. These would be points for negotiation with the buyer/lessor.

- The sale of OGB may diminish the legislative and/or state administrative control over costs, benefits, or changes to the plans. These issues would need to be addressed in the contract.

- According to the 2012 OGB Executive Budget initially submitted, OGB estimated a savings of $10,155,906 resulting from personnel reductions of 149 positions. It was explained to us that the reduction would be the result of the PPO being privatized. Those positions were restored in the budget process.

Timeline of Events

The scope of the assessment in the current request for proposal (RFP) includes any and all health benefits programs offered by the State of Louisiana. The two most discussed options are the privatization of the PPO and HMO plans and the sale/lease of OGB. The privatization of the PPO plan relates to a private company managing the plans instead of the state, while the privatization of OGB relates to the sale/lease of all OGB's health benefit programs to a private company.

A timeline of events from February 1, 2011, through July 15, 2011, relating to the proposed privatization of OGB functions, is as follows:

- February 4, 2011 - OGB issued a RFP for the services of a financial advisor to explore alternative methods of carrying out OGB's statutory responsibilities through contract(s) for the provision of basic health care services and other health care services to the OGB program's covered persons and/or for any other health care plan or systems.

- February 16, 2011 - Unrelated to the RFP on February 4, OGB contracted with Chaffe to establish the fair market value of the operations of OGB as of January 31, 2011.

- March 7, 2011 - The formal bid opening occurred for the state's RFP on the financial advisor, resulting in Goldman Sachs being the only bidder. However, a contract was never finalized from that first bid process.

- March 24, 2011 - LLA staff met with Mr. Tommy Teague, OGB chief executive officer (CEO), and requested all information submitted by OGB to Chaffe, a copy of the Chaffe report, data used in the analysis to sell or retain OGB's book of business, and data submitted to the Division of Administration (DOA) and/or Goldman Sachs.

- March 25, 2011 - Mr. Teague informed LLA staff that he was instructed by DOA to not provide this information to LLA because it was part of the DOA "deliberative process privilege."

- March 30, 2011 - The Legislative Auditor wrote a letter to the Commissioner of Administration stating that his auditors must have unfettered access to OGB files.

- April 1, 2011 - The Commissioner of Administration wrote a letter to the Legislative Auditor. The letter included the following statement, "In response to this inquiry, and the others by phone from your office, we advised that we believe this matter is still within the scope and protections of the deliberative process privilege."

- April 15, 2011 - Mr. Teague was terminated by the DOA. Mr. Teague was replaced as CEO by Mr. Scott Kipper.

- April 18, 2011 - The LLA requested the same information from Mr. Kipper that was originally requested from Mr. Teague on March 24, 2011. Mr. Kipper also cited that the deliberative process privilege protected the information from disclosure.

- May 6, 2011 - OGB issued a second RFP for the services of a financial advisor to assess the market value of the book of business and services provided by OGB and to negotiate for and on behalf of the OGB alternative methods by which OGB may perform its statutory responsibilities.

- May 26, 2011 - Proposers conference was held on the second RFP with a representative from Goldman Sachs present, and with Morgan Keegan & Co. Inc., and UBS Investment Bank representatives on a conference call.

- June 6, 2011 - Proposals submitted to OGB were collected by DOA representatives. Goldman Sachs, Morgan Keegan & Co. Inc., and Barclays Capital submitted proposals.

- June 8, 2011 - Commissioner Rainwater provided a copy of the Chaffe report to the LLA and certain select legislators. The report that was released was dated June 3, 2011, and concluded that the market value of the operations of OGB was between $133 million and $217 million at January 31, 2011, assuming a five-year privatization term. This analysis did not consider the value of the existing fund balance, which was approximately $499 million at January 31, 2011.

- June 24, 2011 - Mr. Kipper resigned as CEO of OGB, two months after being hired.

- July 15, 2011 - Commissioner Rainwater announced that Morgan Keegan & Co. Inc., will advise the Jindal administration on a possible privatization of OGB.

OGB Administrative Cost

In recent legislative committee meetings regarding OGB's operations, possible sale, and administrative costs, OGB personnel described an administrative rate of 3.23% of total expenditures for fiscal year 2010, while DOA personnel noted an administrative cost rate of approximately 6% of total expenditures. The difference relates to what is considered to be administrative cost. OGB considers the Humana, United, and Catalyst administrative expenses as part of the medical benefits expense since it is not an expense of OGB operations.

The following table shows the breakdown for the 3.23% (OGB-calculated administrative cost of operation including the PPO) and 5.73% (DOA-calculated administrative cost of operation including PPO + Humana admin + United admin + FARA admin + Catalyst admin).

OGB-Calculated	FY 2010		DOA-Calculated	FY 2010		Difference
Medical Benefits	$885,257,465	71.96%	Medical Benefits	$859,032,581	69.83%	$26,224,884
Prescription Drugs	264,995,620	21.54%	Prescription Drugs	260,385,941	21.17%	4,609,679
Administrative	39,796,193	3.23%	Administrative	39,796,193	3.23%	
Mental Health	11,526,329	0.94%	Mental Health	11,526,329	0.94%	
Life Insurance	28,350,559	2.30%	Life Insurance	28,350,559	2.30%	
Cafeteria	349,413	0.03%	Cafateria	349,413	0.03%	
Total Expenses	**1,230,275,579**	**100.00%**	Humana Admin	19,929,133	1.62%	
			United Admin	6,290,561	0.51%	
			FARA MCO Fees	5,190	0.00%	
			Catalyst Admin	4,609,679	0.37%	
			Total Expenses	**1,230,275,579**	**100.00%**	
		3.23%			5.73%	

According to OGB data, OGB covers 225,912 people and OGB has 309 positions. The administrative costs to run OGB operations, including the PPO, are $39,796,193 based on OGB calculations and $70,630,756 based on DOA calculations (see table above).

In the May 2, 2011, Senate Committee on Retirement meeting, a Legislative Fiscal Office representative provided, based upon fiscal year 2010 data, the administrative cost and the third-party administrative fees were approximately 5% of total revenue. In addition, based on fiscal year 2011 data through March 2011, the percentage of the administrative cost and third-party administrative fees were 5.9%.

According to an official with Alabama's State Employees Insurance Board (SEIB), Alabama has:

- Covered lives as of 6/1/11: 100,918
- Employees, all SEIB programs: approximately 62

- Total state administrative cost, all SEIB programs: approximately $6 million

According to an official with Tennessee's State Group Insurance Program (SGIP), Tennessee has:

- Covered lives as of 12/31/10: approximately 300,000
- Employees: approximately 75
- Total FY 2010 state administrative cost (health and pharmacy benefits, state plan): approximately $5.1 million

Based on the results of our limited review, ten states besides Louisiana* are liable for the claims of at least one of their state employee health plans. Each of these states contracted with one or more third-party administrators.

* *Alabama, Arkansas, Florida, Georgia, Missouri, Oklahoma, Mississippi, Kansas, North Carolina, Tennessee*

Both Alabama's and Tennessee's state employee health plans are self-insured, and these states contract with third-party administrators. These states are liable for the claims.

According to the 2012 OGB Executive Budget initially submitted, OGB estimated a savings of $10,155,906 resulting from personnel reductions of 149 positions. It was explained to us that the reduction would be the result of the PPO being privatized. Those positions were restored.

Chaffe Report

On February 16, 2011, the State of Louisiana contracted with Chaffe for an amount not to exceed $49,999.99 to establish the fair market value of the operations of OGB as of January 31, 2011. If the contract were $50,000, the professional service contract would have been subjected to statutory review. The resulting report, dated June 3, 2011, concluded that the market value was between $133 million and $217 million at January 31, 2011, assuming a five-year privatization term.

The valuation range (1) does not assume any increased costs as a result of the Patient Protection and Affordable Care Act; (2) does not consider the impact, if any, of increased premium costs incurred by the state as a result of the privatization; and (3) does not consider the value of the existing fund balance, which was $499,184,108, as of the valuation date of January 31, 2011.

For each privatization scenario, Chaffe assumes the increase in equity plus the existing Incurred But Not Reported (IBNR) claim reserve of $73.7 million at January 31, 2011, and earns the median comparable public company investment yield of 2.52% beginning January 1, 2012.

The report notes that OGB is a government-run division and therefore does not attempt to generate surpluses. Therefore, valuation methods such as precedent transactions analysis and comparable public company analysis that apply relevant multiples to historical earnings and current equity values are not appropriate valuation methodologies for OGB.

The evaluation was made by an analysis of various factors as of the valuation date including, but not limited to, those listed below:

- The nature of OGB's operations and the history of OGB
- The general economic outlook and the economic outlook for the health insurance industry
- The attractiveness of OGB's operations to a potential buyer
- The projected cash flows of OGB's operations under various scenarios
- The performance characteristics of publicly traded companies with similar characteristics and actively traded in a free and open market, either on an exchange or over-the-counter

The report lists many values based on various assumptions including discount rates, health care inflation rates, projected premium increases, and presumed operating margins. Chaffe also calculated medical loss ratios for 2009, 2010, and 2011-projected. When projecting necessary premium increases, Chaffe considered that OGB currently manages to breakeven status; in a privatization scenario a pre-tax margin must be achieved. In projecting necessary premium increases for the privatization scenario, Chaffe analyzed the pre-tax operating margins for the most comparable division of a group of comparable publicly traded companies.

Chaffe assumes a privatization occurs on December 31, 2011. Chaffe also assumes that the purchaser enters into a five-year contract with OGB and administers the plans on a full risk basis and IBNR funds are transferred back to the state at the end of the contract.

Health Services and Privatization in Other States

LLA staff contacted ten different states to determine if any of these states considered privatizing their state health insurance agencies (moving to all fully insured plans rather than self-insured). The states contacted were Alabama, Arkansas, Florida, Georgia, Kansas, Mississippi, Missouri, North Carolina, Oklahoma, and Utah. Of the ten states contacted, two states considered privatizing at some point in the past. Alabama considered privatizing its administrative risk pool; however, it was cost prohibitive to do so. Missouri also considered privatizing in the past, but no action was taken. Utah was the only state where the health insurance agency provided all the services. Louisiana's OGB provided services for its PPO plan, but shared responsibilities with third-party administrators for other health plans.

OGB's plans are either fully insured (MH-HMO and Medicare Advantage plans) or self-insured (PPO, HMO, and CD-HSA).

- Fully Insured Plan - A fully insured plan is a plan where OGB contracts with another organization (e.g., Vantage Health MH-HMO Plan) to assume financial responsibility for the members' medical claims and all incurred administrative costs. In a fully insured plan, the contractor assumes all risk and any excess funds that remain after claims payments are kept by the contractor as profit or for administrative overhead.

- Self-Insured Plan - A self-insured plan is a plan where OGB assumes the major costs of health insurance for its members, reimburses the third-party administrator (e.g., Blue Cross and Blue Shield of Louisiana) for claims cost, and pays the third-party administrator an administrative fee. As a self-insured entity, OGB assumes all risk; excess funds that remain after claims reimbursement and administrative fees (paid to the third-party administrator or administrative costs of OGB) remain with OGB. OGB is able to use the surplus to suppress annual premium rate increases. Currently, the PPO, HMO, and CD-HSA plans are self-insured.

The chart below provides a summation of the services provided by the states contacted in comparison to Louisiana.

State	Determines Eligibility	Billing and Collection of Premiums	Network Administrator	Processes/Pays Medical Claims	Provides Customer Service	Liable for Claims	Number of Employees
Alabama	S	S	TPA	TPA	B	S	64
Arkansas	S	S	TPA	TPA	B	S	50
Florida	S	S1	TPA	TPA	TPA	B	23
Georgia	S	S	TPA	TPA	B	S	65
Kansas	S	S1	TPA	TPA	TPA	B	25
Louisiana	S	S	B	B	B	B	309
Mississippi	S	B	TPA	TPA	B	S	20
Missouri	S	S1	TPA	TPA	B	S	75
North Carolina	B1	B	TPA	TPA	B	S	40
Oklahoma	S	S1	TPA	TPA	B	S	170
Utah	S	S	S	S	S	S	225

S - State's Health Insurance Agency provides service.
TPA - Third-Party Administrator provides service.
B - Both state and outside administrator provide service and assume risk depending on plan.
S1 - A state agency/vendor (other than their Health Insurance Agency) provides the service.
B1 - The eligibility rules are in statute and the TPA follows those guidelines.

In addition to these ten states, LLA staff conducted a general Internet search and researched other states' websites individually to determine whether any state had privatized its state health insurance agency. We were unable to readily identify any states that had fully privatized their state health insurance agencies as a result of this research.

Role of the Legislature

In regard to the privatization of the PPO plan, the Legislature through R.S. 42:802 has expressly charged OGB with the power and duty to negotiate contracts with various health providers. (R.S. 42:802(B)(8)(a). Furthermore, the Legislature has determined that these contracts shall be subject to review and final approval by the House Appropriations and Senate Finance committees [R.S. 42:802(B)(S)(d) and R.S. 49:968(B)(21)(c)].

However, full legislative approval would appear to be necessary for the sale of OGB's assets, including its monetary reserve fund, as no applicable delegation of the Legislature's constitutional authority seems to exist in the current statutes. R.S. 42:854(C) prohibits the use of the monetary reserve fund of OGB.

> Notwithstanding any other provision of law to the contrary, any money received by or under the control of the Office of Group Benefits shall not be used, loaned, or borrowed by the state for cash flow purposes or any other purpose inconsistent with the purposes of or the proper administration of the Office of Group Benefits.

It appears this statute must be repealed or amended for a sale of OGB to occur. Any proceeds from a sale of OGB assets, including its monetary reserve fund, must be placed into the State Treasury and be appropriated before their expenditure. Finally, any substantial changes to the function and role of OGB in regard to the administration and management of group insurance policies would require legislative action to amend applicable substantive laws, addressing the resulting reorganization of the Executive Branch. This reorganization is, by Constitution, within the exclusive authority of the Legislature.

In so far as the proposed sale of OGB's assets, including its monetary reserve fund, would not appear to be allowed under the surplus property provisions,[1] any such sale of OGB assets, including its monetary reserve funds, would require prior approval of the Legislature to prevent any infringement upon its sovereign constitutional authority over the finances of the state. Furthermore, the wholesale privatization of an entire state agency would appear to constitute a reorganization of the Executive Branch, which may only occur through legislative action in accordance with the provisions of Article IV, §1(C) of the Louisiana Constitution. The Attorney General (AG) in Opinion No. 78-35 stated that the Governor did not have the authority to merge the School of Nursing at LSU with the School of Nursing at Charity Hospital School of Nursing through executive order without legislative act, as Sections 1 and 6 of Article IV of the Louisiana Constitution places the authority for the organization of the Executive Branch within the powers

[1] The Legislature, through statute, has delegated some of its fiscal authority to the Governor and the Executive Branch, specifically the DOA, to allow the sale of surplus immovable and movable property of the state. The Legislature has provided for the sale of movable property through two primary statutory authorizations, R.S. 49:125 and R.S. 39:330.1.

of the Legislature, and further R.S. 36:251 (c) expressly required legislative approval prior to any reorganization of the Department of Health and Human Resources.

The Legislature has previously mandated that OGB shall exist within the DOA in the Office of Governor. OGB shall administer group insurance for state employees and other employees allowed to join by legislative authorization. Therefore, legislative action would similarly appear to be required to eliminate OGB and to reallocate, amend, or repeal its statutory powers and duties. If the Legislature concurs with the Governor in the privatization of OGB and the sale of its assets, including its monetary reserve fund, it must do this through new legislation and repeal old provisions.

Article VII, §9(A) of the Louisiana Constitution provides that all money received by the state or by any state board, agency, or commission shall be deposited immediately upon receipt in the state treasury, except that received:

(1) as a result of grants or donations or other forms of assistance when the terms and conditions thereof or of agreements pertaining thereto require otherwise;

(2) by trade or professional associations;

(3) by the employment security administration fund or its successor;

(4) by retirement system funds;

(5) by state agencies operating under authority of this Constitution preponderantly from fees and charges for the shipment of goods in international maritime trade and commerce; and

(6) by a state board, agency, or commission, but pledged by it in connection with the issuance of revenue bonds as provided in Paragraph (C) of Section 6 of this Article, other than any surplus as may be defined in the law authorizing such revenue bonds.

Any funds obtained from the sale of OGB's assets must be immediately placed within the State Treasury as none of the exceptions provided for above under Article VII, §9(A) would appear to apply. Furthermore, Article VII, §10(D) of the Louisiana Constitution requires that no money shall be drawn from the State Treasury absent an appropriation made in accordance with law. As such, any monies obtained from the sale of OGB's assets must first be appropriated by the Legislature before they may be used. It is unclear whether the purpose of R.S. 42:854(C) would restrict the use of the proceeds from a sale or lease of the OGB plans.

Other Considerations

Various considerations should be deliberated before the decision to sell/lease OGB is made.

1. Marketing costs - A private company may incur marketing costs that are higher than OGB.
2. Premium taxes - As a state agency, OGB is exempt from paying premium taxes while other health insurance companies are required to pay premium taxes according to R.S. 22:838(B).
3. Profit margin - OGB does not have a profit motivation because it is a state agency whose goals are to provide a service and pay claims. A private company will most likely build a profit margin into the premium structure.
4. Reinsurance - If the contractor assumes all risk (fully insured), the contractor will most likely purchase reinsurance. Currently, OGB does not have reinsurance. The cost of reinsurance varies based on the plan purchased. These cost considerations are dependent on the premium and/or benefit structure restrictions that are placed in the contract.
5. Revenue stream - If the state sells the business, the incurred liabilities, up to the date of the sale, must be paid by either the state or the new owner. If the state remains responsible for the incurred liabilities, there should be a provision in the contract to address payment of these liabilities. If not, there would be no revenue stream after the sale to pay the outstanding claims.
6. Administrative Control - The sale of the business would diminish the legislative and/or state administrative control over cost, benefits, or changes to the plans.
7. Cost savings - Cost savings may result from the efficiencies gained by using an established health care provider with well-structured administrative processes. The contract would be the vehicle for establishing cost parameters.

February Request for Proposals

At the January 19, 2011, OGB Policy and Planning board meeting, Mr. Tommy Teague, CEO, reported that the Governor announced the administration is exploring the sale and privatization of the PPO as one possible solution to the budget challenges facing the state. He explained that a preliminary analysis showed that OGB’s PPO operations are a marketable asset with value to the private sector.

On February 4, 2011, OGB issued a RFP for the services of a financial advisor to explore alternative methods of carrying out OGB’s statutory responsibilities through contract(s) for the provision of basic health care services and other health care services to the OGB program’s covered persons and/or for any other health care plan or systems. These included, but were not limited to, any health care service, delivery system, benefits programs, insurance, or any other plan or programs that may be authorized by law. The RFP terms also included the possible sale, lease, or other transfer of tangible and/or intangible assets of OGB. In furtherance of this effort, OGB sought the services of a qualified financial adviser to assess the market value of the tangible and/or intangible assets of OGB and to negotiate for and on behalf of the OGB, in accordance with OGB's authority pursuant to R.S. 42:802.

Proposals under the RFP were due March 7, 2011. Goldman Sachs was the only company to submit a proposal, but OGB and Goldman Sachs were unable to finalize a contract.

May Request for Proposals

On May 6, 2011, OGB issued another RFP, similar to the February RFP, seeking the services of a qualified financial adviser to assess the market value of the book of business and services provided by OGB and to negotiate for and on behalf of the OGB alternative methods by which OGB may perform its statutory responsibilities in accordance with Louisiana Revised Statute.

Specifically, the RFP defines the scope of services and deliverables as follows:

- Assess the market value of the book of business and/or services provided by OGB
- Assist OGB in the formulation of alternative methods of benefit delivery while retaining the same or improved level of services and benefits for plan members
- Identify potential contractors based on the alternative methods developed and assist OGB with negotiation of contracts
- Provide recommendations to OGB for contracting in light of the assessment and negotiations
- Assist in the drafting and final execution of any contract resulting from the assessment and negotiations
- Provide testimony before any committee of the Louisiana legislature or other tribunal that may conduct hearings regarding any contract resulting from the assessment and negotiations

The scope of the assessment includes any and all health benefits programs offered by the State of Louisiana, including but not limited to the OGB PPO plan, the self-insured HMO plan, and the self-insured consumer directed health plan with a health savings account. The negotiations, as well as any resulting contract, may include any or all of these plans. Any proposal for plan alternatives and/or combination of services may be acceptable if OGB finds that the proposed plan alternatives and/or combinations of services are advantageous to the state.

Proposals were due to OGB by June 6, 2011, and were collected by representatives from DOA. Goldman Sachs, Morgan Keegan & Co. Inc., and Barclays Capital submitted proposals.

On July 15, 2011, Commissioner Rainwater announced that Morgan Keegan & Co. Inc., will advise the Jindal administration on a possible privatization of OGB.

Supplemental Information - OGB Operations

Products Offered and Administered by OGB

During fiscal year 2011, OGB offered four standard health plans for both active and retired employees: the Preferred Provider Organization (PPO) plan, the Health Maintenance Organization (HMO) plan, the Consumer Driven Plan with a Health Savings Account option (CD-HSA), and the Medical Home HMO (MH-HMO) plan. The PPO is self-administered by OGB. The HMO is administered by Blue Cross and Blue Shield of Louisiana. The CD-HSA Plan is administered by United Healthcare. The MH-HMO is self-insured by Vantage Health Plan, making it a fully insured product of OGB. Retired employees who have Medicare Part A and Part B coverage also have access to Medicare Advantage plans that are offered on a calendar year basis. For calendar year 2011, there are three HMO plans and two PPO plans offered by four companies. The MH-HMO and the Medicare Advantage plans are fully insured, and OGB acts only as a pass-through for premiums collected. Amongst the plans mentioned above, OGB, as of June 26, 2011, has nearly 226,000 total covered lives, of which nearly 133,000 are covered employees and retirees as follows:

Plan	Provider	Active and Retired Employees	Covered Lives Enrollees and Dependents
HMO	Blue Cross Blue Shield of LA	85,358	155,007
MH-HMO	Vantage Health Plan	2,823	5,540
PPO	OGB	41,546	61,186
CD-HSA	United Healthcare	180	282
		129,907	**222,015**
Medicare Advantage Plans			
HMO	Humana	925	1,239
PPO	Humana	59	82
HMO	People's Health	248	312
PPO	United Healthcare	91	130
HMO	Vantage Health Plan	1,655	2,134
		2,978	**3,897**
	Total Covered Lives	**132,885**	**225,912**

OGB's plans are either fully insured (MH-HMO and Medicare Advantage plans) or self-insured (PPO, HMO, and CD-HSA).

- Fully Insured Plan - A fully insured plan is a plan where OGB contracts with another organization (e.g., Vantage Health MH-HMO Plan) to assume financial responsibility for the members' medical claims and all incurred administrative costs. In a fully insured plan, the contractor assumes all risk and any excess funds that remain after claims payments are kept by the contractor as profit or for administrative overhead.

- Self-Insured Plan - A self-insured plan is a plan where OGB assumes the major costs of health insurance for its members, reimburses the third-party administrator (e.g., Blue Cross and Blue Shield of Louisiana) for claims cost, and pays the third-party administrator an administrative fee. As a self-insured entity, OGB assumes all risk; excess funds that remain after claims reimbursement and administrative fees (paid to the third-party administrator or administrative costs of OGB) remain with OGB. OGB is able to use the surplus to suppress annual premium rate increases. Currently, the PPO, HMO, and CD-HSA plans are self-insured.

In addition to the health coverage, OGB also offered Group Term Life Insurance through Prudential to active and retired employees. The maximum for the Basic plan is $5,000 and for the Basic Plus Supplemental plan is $50,000 (based on salary). Active employees and retirees are eligible for coverage; however, this policy is nontransferable for active employees who resign from employment with the state.

OGB also has agreements with the Department of Health and Hospitals (DHH) and Louisiana State University (LSU) to provide health insurance assistance. DHH and OGB entered into an agreement during fiscal year 2008 to coordinate available resources to provide more effective coverage for those individuals that are enrolled in the LaChip Affordable Plan, the Family Opportunity Act, and the Medicaid Purchase Plan. This agreement provides for OGB to use its existing premium billing system to invoice individuals enrolled in all three programs as well as establishing a plan of benefits for the LaChip Affordable Plan that takes advantage of OGB's existing PPO provider network and services. OGB has a memorandum of understanding (MOU) with LSU. The MOU allows LSU to create its own health insurance plan (known as the LSU First plan) to serve employees of LSU and the Legislature of Louisiana. Under this MOU, OGB provides LSU any information necessary or useful to the administration and implementation of the requirements of the Health Insurance Portability and Accountability Act of 1996 (HIPAA) and the Consolidated Omnibus Budget Reconciliation Act of 1986 (COBRA) at no cost to LSU. Also, OGB provides LSU any information necessary or useful to LSU in determining member, spouse, or dependent eligibility at no cost to LSU. LSU transmits eligibility reports to OGB, and OGB maintains all eligibility documentation for the LSU First plan at no cost to LSU.

Functions of OGB

OGB performs five main functions: eligibility determination, premium collections, network administration, medical claims' payments, and customer service. OGB performs eligibility determination for all of the insurance plans offered to state employees. The insurance plans include the PPO, HMO, MH-HMO, CD-HSA, LSU First, and the five Medicare Advantage plans. OGB collects premiums for the PPO, HMO, MH-HMO, CD-HSA, the five Medicare Advantage plans, and the DHH plans (LaChip Affordable Plan, the Family Opportunity Act, and the Medicaid Purchase Plan). Collecting premiums involves interfacing with over 200 different payroll systems. The network administration function includes maintaining a provider network by negotiating contracts with various doctors, hospitals, etc., and developing fee schedules. OGB maintains a provider network for the PPO plan. The LaChip Affordable Plan uses the PPO provider network and services. OGB processes claims for the PPO. OGB also reimburses the HMO and CD-HSA administrators for their health claims. OGB provides customer service for participants with the PPO plan. Although each provider has its own customer service to answer questions, OGB's customer service also answers questions dealing with eligibility and other generic issues about the third-party provider plans. Below is a summary of the functions performed by OGB indicated by "X."

Plan	Determines Eligibility	Collects Premimums	Passes Premiums to 3rd-Party Administrator	Network Administrator/ Maintains Provider Network	Processes/ Pays Medical Claims	Reimburses 3rd-Party Administrator for Medical Claims	Pays Administrative Fee to 3rd-Party Administrator	OGB Assumes Risk/Retains Access	Provides Customer Service
PPO	X	X		X	X			X	X
HMO	X	X				X	X	X	(B)
MH-HMO	X	X	X						(B)
CD-HSA	X	X				X	X	X	(B)
Medicare Advantage Plan	X	X	X						(B)
LSU First	X								
DHH Plan - LaChip		X	X	(A)	(C)				
DHH Plan - Family Opportunity Act		X	X						
DHH Plan - Medicaid Purchase Plan		X	X						

(A) - The DHH LaChip plan uses the OGB PPO provider network and services.

(B) - Although each provider has its own customer service to answers questions, OGB's customer service also answers questions dealing with eligibility and other generic issues about the third-party provider plans.

(C) - OGB functions as a third-party administrator for the LaChip plan. OGB processes/pays claims for the LaChip plan and is reimbursed for the claims' payments. OGB also receives an administration fee.

As of June 30, 2011, OGB has 309 positions as shown in this chart.

Division	Number
Fiscal	40
Customer Service	59
Provider Service	11
Legal	7
Claims	58
Eligibility	22
Internal Audit	4
Info Systems	49
HIPAA	4
Quality Assurance	10
Administration	21
Executive	8
Flexible Benefits	16
Agency Total	**309**

Background

OGB is an agency of the State of Louisiana within the Office of the Governor, Division of Administration. OGB is charged with providing health care services to state employees, retirees, and their dependents. OGB is created and authorized by Chapter 12 of Title 42 of the Louisiana Revised Statutes of 1950, Sections 801, et seq., as amended and reenacted by Act 1178 of 2001 to provide health insurance, accidental benefits, life insurance, and a flexible benefits plan to eligible state employees, retirees, and their dependents. Eligible plan participants include employees of state agencies, institutions of higher education, local school boards that elect to participate in the program, and certain political subdivisions. Local government entities or municipalities are not eligible. OGB determines eligibility for plan participants and reconciles all premium payments from approximately 370 different agencies and communicates with approximately 200 different payroll systems statewide.

The philosophy of OGB is to use informed decision making, proactive services, and innovative actions for plan members and providers, while offering a competitive system of benefits to assist the state of Louisiana's goal to attract and retain competent and productive employees. The mission of OGB is to offer an employee benefits system that meets or exceeds industry standards and/or benchmarks. The agency's goals to accomplish its mission are to:

(1) measure and improve operational efficiency and effectiveness at OGB;

(2) continuously increase customer satisfaction for OGB customer; and

(3) improve the health of plan members.

Scope and Methodology

This informational report provides data regarding OGB operations and the Division of Administration's plans for privatization of part or all of those functions. Because this is an informational report, we did not conduct this project in accordance with all governmental auditing standards. This report was developed in an effort to provide information about:

(1) the timeline of events in relation to privatizing OGB's health plan(s);

(2) OGB's administrative costs;

(3) the Chaffe & Associates, Inc., report;

(4) privatization of health insurance agencies that may have occurred in other states;

(5) the role of the Legislature in relation to privatizing OGB's health plan(s);

(6) various factors that should be considered before the sale/lease of OGB;

(7) requests for proposals for a financial advisor; and

(8) an overview of OGB's operations.

To complete this project, we gathered data from OGB, the Division of Administration, the Chaffe report, state laws, legislative testimony, and news articles. Because of the nature of this project and time limitations, we did not assess the reliability of the data or all information sources used to generate this report.

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Management’s Response

BOBBY JINDAL
GOVERNOR

PAUL W. RAINWATER
COMMISSIONER OF ADMINISTRATION

State of Louisiana
Division of Administration
Office of the Commissioner

August 15, 2011

Mr. Daryl G. Purpera, CPA, CFE
Legislative Auditor
Post Office Box 94397
Baton Rouge, Lousiana 70804-9397

Dear Mr. Purpera:

Thank you for the opportunity to submit an official response to your report on the Office of Group Benefits. While the report does not appear intended to break new ground nor to delve into a detailed audit, it does provide a broad overview of background information that may prove helpful in our exploration of potential service delivery alternatives that are in the best interest of both plan members and taxpayers. As such, we will limit our response to just a few topics.

First, the report notes that as a result of research conducted by LLA staff, they were unable to identify any states that had "fully" privatized their state employee health insurance agencies. Given that this administration itself has never proposed the complete privatization of OGB, the relevance of this research point is not exactly clear.

Similarly, when the report asserts that the "wholesale privatization" of OGB would appear to require approval by the full Legislature, I wonder, again, about the practical usefulness of the point since it is based on a premise – the "full" or "wholesale" privatization of OGB – that is not even under consideration.

On the other hand, we do find noteworthy certain information contained in the report's section comparing Louisiana to other states, particularly the number of employees in their respective state employee health insurance agencies:

Louisiana: 309
Utah: 225
Oklahoma: 170
Missouri: 75
Georgia: 65
Alabama: 64
Arkansas: 50
North Carolina: 40
Kansas: 25
Florida: 23

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Mississippi: 20

The stark contrast in these numbers does beg the questions as to how these other states appear to be able to deliver service to their plan members so much more efficiently, and whether it has anything to do with the fact that they already rely on private delivery of service to a far greater degree than does Louisiana. The report makes reference to one possible explanation, namely that Louisiana and Utah stand alone among the states in the extent to which they self-administer health insurance plans, essentially making state government function as a health insurance business, in competition with the private sector.

The possibility of providing quality service in a manner that's also more efficient is precisely why we have begun this evaluation of OGB, and we owe it to the taxpayers to evaluate it fully.

Lacking such a full evaluation, the report speculatively asserts that the further privatization of OGB "may" result in higher insurance premiums to plan members due to various "other considerations" – a speculation which, even as tentatively as it is stated, cannot be supported based on the research in your report. On the one hand, it omits the fact that premium costs are regularly increasing under the current structure anyway, while on the other hand it does not factor in any of the relative cost savings that your report also says "may result from the efficiencies gained by using an established health provider with well-structure administrative processes."

Of course, given that we are at a very early stage in our evaluation, presumably these and other questions will be more readily understood the further along we get in the process, particularly when there is an actual contract to evaluate, as your report notes on several occasions.

As you are aware, we are currently engaging the services of a financial advisor who will, over the coming months, conduct a comprehensive and in-depth analysis of OGB and the health care market, and provide recommendations to the administration as to the proper administrative structure of OGB. If the financial advisor recommends structural changes to OGB, such changes are not anticipated to be implemented until the start of the plan year beginning January 1, 2013.

As we have stated previously, any changes implemented would have to comply with the following parameters:

- Plan members will continue to receive quality service and coverage;
- Benefits for all plan members, including retirees, will not change, and current eligibility rules for coverage will not change for any plan members as a result of possible further privatization of OGB;
- Premiums rates, likewise, would be unaffected by such a transition and increases, when they occur, will continue to be reflective of medical market rates, as they are now; and
- OGB's administrative oversight will continue, securing the continued success of all the plans.

In conclusion, we are in the very early stages of what will be a lengthy, careful, and thorough evaluation process to arrive at the best possible policy for plan members and taxpayers alike.

We appreciate the insights on the matter contained in your report, and look forward to working with you in the future.

Sincerely,

Paul W. Rainwater