



## **MEMORANDUM**

**To:** Kurt Triplett, City Manager

**From:** Tracey Dunlap, Deputy City Manager  
George Dugdale, Sr. Financial Analyst

**Date:** September 27, 2018

**Subject:** HEALTHCARE PROGRAM UPDATE

## **BACKGROUND**

In April 2015, the City of Kirkland implemented an innovative employee healthcare program, the Healthy Kirkland Initiative. The objectives of the program were to improve employee health while mitigating the rising cost of health care and to avoid liability under the Affordable Care Act "Cadillac Tax", now delayed until 2022. In December 2015, the City Council received a comprehensive briefing on the evolution of the City's program and this memorandum will summarize some of the highlights of that report and provide an update on the program's impact on the budget since that point in time. The full 2015 briefing (170 pages including attachments) is available on the City's website at:  
[https://www.kirklandwa.gov/Assets/City+Council/Council+Packets/120815+SpecMtg/3a\\_StudySession.pdf](https://www.kirklandwa.gov/Assets/City+Council/Council+Packets/120815+SpecMtg/3a_StudySession.pdf)

The background that follows is a description of the initiative and the plan design excerpted from the 2015 briefing:

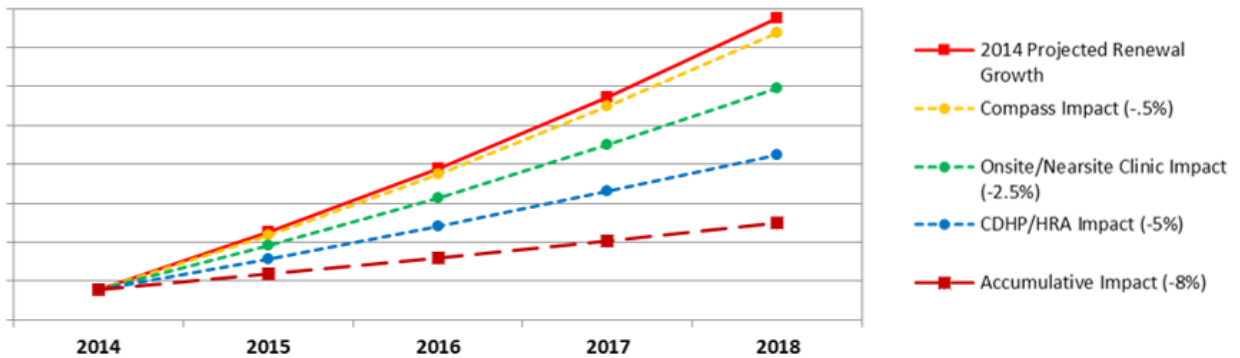
### **The Healthy Kirkland Initiative**

"The City opted for a "full systems approach" dubbed the Healthy Kirkland Initiative that included:

- 1) individual economic incentives to better empower individuals to make more informed medical decisions and improve the likelihood of health savings;
- 2) increased market transparency so employees could be more informed in those decisions;
- 3) unlimited primary care services, free to employees and qualified dependents, to promote proactive healthy behavior, and ensure participants had ample opportunity to get the critical on-demand primary care necessary to help ensure healthier lives.

Each element of the Initiative has been done successfully somewhere in the United States. What differentiated the City's new approach was not so much the implementation of any of these ideas separately as isolated efforts to improve care. Rather what was unique to the City's strategy was implementing each of these elements together, at the same time, as ***interdependent*** parts of a full health care delivery system.

Below is a graphical depiction of the projected savings associated with each of each element in the system working together to bend the trend of future growth previously presented by the City Manager at the 2014 Washington City Managers Association Summer Conference. The combined cost reductions for all the elements were estimated to place the City within reasonable striking distance of the 2.5% growth rate necessary to avoid the Cadillac Tax.



## How Does the Healthy Kirkland Initiative Work?

### *High Deductible Health Plan*

First, the City moved to a high deductible health plan. Establishing a high deductible framework created the necessary structure to incorporate real economic decision making to everyone participating in the new plan. With a high deductible plan, participants are required to pay a much larger portion of their initial health costs, emphasizing the need to make informed decisions on nearly every element of their care.

### *HRA VEBA*

To offset the new financial exposure to employees, the City created an expansive Health Reimbursement Voluntary Employee Benefits Association (HRA VEBA) benefit contribution, essentially matching annually the cost of the entire deductible for both individuals and families. HRA VEBA's, unlike traditional HRA's, are savings accounts that stay with employees and eligible dependents and accumulated account balances roll over from year to year. With this new approach, employees are given both a new economic exposure (the higher deductible) combined with a new financial incentive to save (the HRA VEBA contribution). In order to fully match the annual cost of the high deductible as part of their HRA VEBA contribution, however, most employees and their spouses/domestic partners have to complete a wellness incentive program. These activities include a biometric screening, health risk assessment, visiting with a health provider and meeting with a health coach, and registering with the health concierge service.

| <b>Financial Exposure</b>      |                              |               |
|--------------------------------|------------------------------|---------------|
|                                | <b>Healthy Kirkland Plan</b> |               |
|                                | <b>Employee Only</b>         | <b>Family</b> |
| Deductible                     | 1500                         | 3000          |
| <b>Out-Of Pocket Max</b>       | <b>2500</b>                  | <b>5000</b>   |
| VEBA Contribution              | 1200                         | 2400          |
| Wellness Contribution          | 600                          | 600           |
| <b>Total VEBA Contribution</b> | <b>1800</b>                  | <b>3000</b>   |
| <b>Maximum Exposure</b>        | <b>700</b>                   | <b>2000</b>   |

Thus, the new framework provides an incentive to engage in healthy behavior and make more judicious decisions regarding the utilization of care, supporting the notion put forth by economist Milton Friedman when he stated "nobody spends somebody else's money as carefully as he spends his own."

#### *Compass Health Service Concierge*

Recognizing that putting employees into the health care marketplace without guidance or better information was not enough, the City implemented the next critical element to the new approach by adding, at no cost to the employee, the availability of a health concierge service. This service helps guide employees in making better decisions in the market place by providing much needed data on provider cost, quality of care and convenience. The company selected to provide the service, Compass, even helps individuals better understand any questions on appropriate coverage and billing statements. By contracting with the Compass health service, City employees are more empowered consumers in an otherwise opaque marketplace.

#### *Vera Whole Health Near Site Primary Care Clinic*

The final element of the full systems approach was the creation of a near site primary care health center, free to employees and qualified dependents. The City chose Vera Whole Health Services as the operator of the health center. The Kirkland Vera clinic is located in the Totem Lake area, just a short drive from the Evergreen Hospital Emergency Room. Parking at the facility is free, and it is open to employees and their family members who are enrolled in the City's health plans. The health center provides preventative and same day acute care (immunizations, check-ups, limited prescriptions, etc.) along with behavioral and lifestyle health coaching, all at no cost to the employee. The health professionals at the clinic provide care that includes both coaching and education, so employees can schedule appointments for a variety of preventative and acute services, as well as wellness and nutritional consultations. Finally, Vera was chosen as the clinic provider because it provides reciprocity among its clinics. Kirkland employees and qualified dependents can visit any Vera clinic for free. Currently there are several clinics in Seattle in addition to the Kirkland location and as more clinics are added, access for Kirkland employees and their families to high quality, free health care will only increase.

The health center is a critical component of the entire system. The reasons for this are several. First, because primary care is free to employees and convenient, employees and

qualified dependents have a powerful financial incentive to use the clinic to save their HRA VEBA balances and be more active in maintaining their health. Second, because the operation of the clinic is informed by a council made up of employees, the quality and availability of care is part of a participatory process that encourages employee engagement and oversight. Finally, because the Vera model involves unlimited free access to a health coach, the clinic could become a catalyst for cultural change at the City that promotes more healthy proactive living as part of the employment experience.

Each element of the Healthy Kirkland Initiative taken alone would likely be an important improvement to an existing health care plan. Taken together and implemented as part of a comprehensive system however, each element is enhanced to realize much more of its full potential providing entirely new opportunities for participants to improve health, increase savings and enjoy a better quality of life.”

## **PROGRAM UPDATE SINCE 2015**

Initially, the City’s AFSCME, PSEU, and Teamster bargaining units and Management and Confidential staff joined the program in 2015 and subsequently the remaining Police bargaining units joined as well. Effective in 2017, the firefighter’s union (IAFF) opted to participate in a plan outside the City’s system sponsored by the LEOFF Trust PFP for which the City pays the premiums.

Initial results from the Healthy Kirkland Initiative are positive. The 2016 recommended contribution to the self-insurance fund for the program decreased 4.5% at a time that the national average for health care costs was a 6% increase and the Association of Washington Cities increase for its high deductible plan similar to the City’s increased 9.1%.

The 2015-2016 Budget assumed zero percent growth in the health benefits fund as a result of higher than expected health cash reserves from the early results of the program and in anticipation of continued success of the Healthy Kirkland Plan.

The 2017-18 Budget assumed no increase to the contribution to the health care fund in 2017 and a 2% increase in 2018, still well below the national average and AWC plan increases (AWC’s HDHP premium increased 13.2% from 2017 to 2018). The premiums paid to LEOFF Trust in 2018 increased 13%.

The 2017-2018 assumptions recognized that the reserve maintained in the health care fund was substantially above the required minimum of 16-weeks of claims data. This balance was the result of several dynamics:

- By diverting claims to the clinic, the 16-week rolling average of claims was substantially lowered.
- The amount set aside for claims is based on an actuarial analysis. In the early years of the program, claims performed better than the calculated actuarial result.
- A \$1 million contingency had been added to the reserve in the beginning of the City’s self-insurance program as a hedge against higher than expected claims growth, which has proven to be unnecessary after the first year of self-insurance in 2011. This amount has been reallocated to help fund the replacement of the City’s core financial and human resources system.

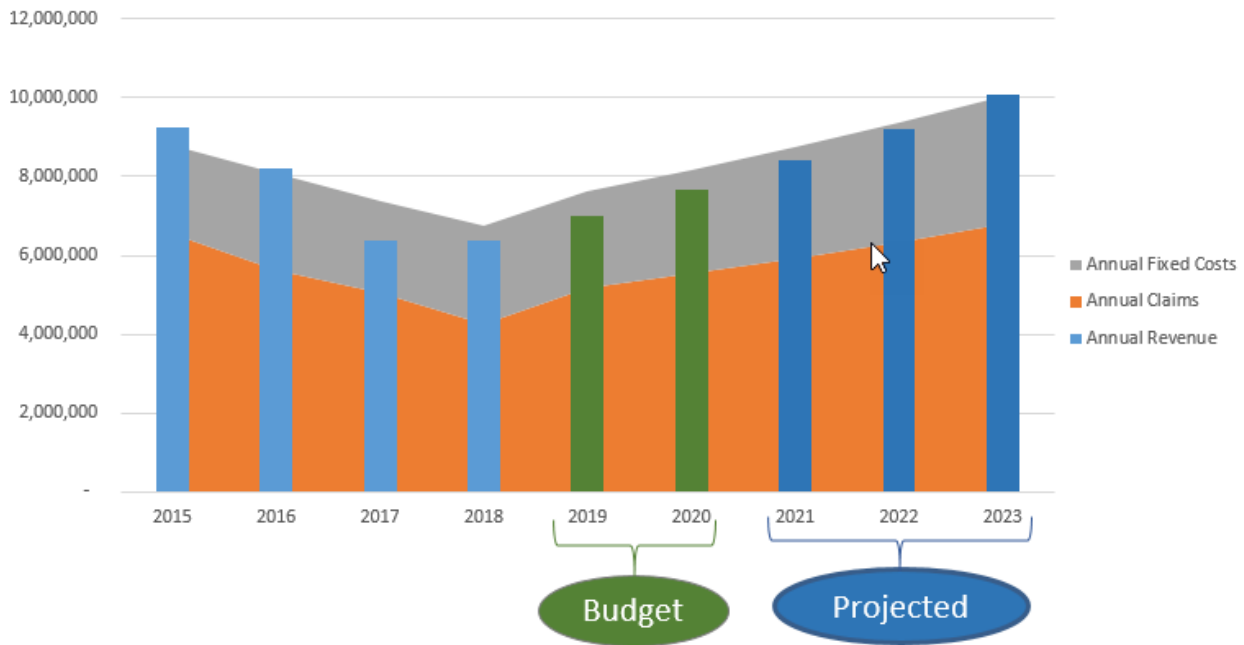
To begin to draw down the reserve balances, the 2017-2018 rates were set below the actuarial recommendation which in fact did draw down the balance in 2017 and is expected to draw it down in 2018 as well, as illustrated in the table below. Note that a portion of the reserve draw down in 2017 reflects the “run off” of claims for IAFF members, which is the amount of claims incurred in 2016, but paid out in 2017 when they were no longer part of the City’s plan. A portion of the reserve is a mandated 16 week minimum claims balance. This amount is estimated as part of the budgeting process, and has been declining through recent budget cycles. Future reserve requirements have been estimated at the 2019-2020 budgeted levels.

| Category                        | Actuals   |           |             | Projected |           |           |           |           |           |
|---------------------------------|-----------|-----------|-------------|-----------|-----------|-----------|-----------|-----------|-----------|
|                                 | 2015      | 2016      | 2017        | 2018      | 2019      | 2020      | 2021      | 2022      | 2023      |
| Starting Reserve Balance        | 6,639,981 | 7,214,986 | 7,130,429   | 5,172,161 | 4,834,232 | 4,211,511 | 3,721,724 | 3,384,798 | 3,222,792 |
| Use/Addition to Reserves        | 575,005   | (84,557)  | (958,268)   | (337,929) | (622,721) | (489,787) | (336,926) | (162,006) | 37,296    |
| Contingency Reserve*            |           |           | (1,000,000) |           |           |           |           |           |           |
| Ending Reserve Balance          | 7,214,986 | 7,130,429 | 5,172,161   | 4,834,232 | 4,211,511 | 3,721,724 | 3,384,798 | 3,222,792 | 3,260,088 |
| Approximate 16-Week Requirement | 2,058,000 | 2,058,000 | 2,023,000   | 2,023,000 | 1,650,000 | 1,650,000 | 1,650,000 | 1,650,000 | 1,650,000 |

\*Contingency was transferred to the Finance System Replacement CIP project

Looking forward to the 2019-2020 budget and beyond, the most recent actuarial analysis indicates that an increase of approximately 35% in the claims-related premium contribution might be necessary to bring the premiums in line with costs. Given that the current reserve is still well in excess of the required minimum, staff has laid out a four year plan to raise those premiums in line with costs covered by those premiums. The preliminary budget reflects a 9.5% premium increase that would close the current gap between claims and fixed costs and medical premiums by 2023, as illustrated in the table above and the graphic on the following page.

2015-2023 Premium Revenues vs Expenses Paid from Premiums



To put these figures into context, the 9.5% increase does not apply to all healthcare expenses, just those tied to claims-related costs. It excludes costs such as the clinic and HRA/VEBA

related to the Healthy Kirkland Plan that represent relatively fixed costs. The cost growth in the overall Healthy Kirkland plan is summarized in the table below.

### Healthy Kirkland Plan Components

#### Assumptions for 2019-2020

| Category                                      | % Increase  |             |
|---|-------------|-------------|
|   | 2019        | 2020        |
| Fully Insured Equivalent (includes Stop Loss) | 9.5%        | 9.5%        |
| Vera Clinic                                   | 1.5%        | 1.5%        |
| HRA/VEBA                                      | 0.0%        | 0.0%        |
| Third Party Administration                    | 1.0%        | 1.0%        |
| Compass/EAP                                   | 0.0%        | 0.0%        |
| <b>Overall Increase</b>                       | <b>6.7%</b> | <b>6.7%</b> |

Further, the City's overall healthcare expenditures includes premiums associated with the Kaiser managed care plan offered by the City, the LEOFF PFP plan costs, dental benefits, and internal staff costs associated with administering the program. The table below summarizes the increase in overall healthcare expenditures reflected in the preliminary budget (note that the LEOFF PFP increase is an estimate as the plan has not yet published its 2019 rates). The overall benefit rate increases approximately 5.8% in 2019 and 6.0% in 2020, excluding pension costs which are discussed in a separate issue paper. The one-time decrease in dental and vision premiums reflects moving to updated programs with similar benefits. Note that the 2020 factors are the best estimates available at this point in time and will be refined as part of the mid-biennial budget update in the Fall of 2019.

| Overall Healthcare Expenditure Changes |             |             |
|--|-------------|-------------|
|  | 2019        | 2020        |
| <b>Premiums and Premium Equivalent</b> |             |             |
| HDP                                    | 9.5%        | 9.5%        |
| Kaiser                                 | 3.1%        | 3.1%        |
| IAFF PFP                               | 12.0%       | 12.0%       |
| Willamette                             | 1.5%        | 1.5%        |
| Delta Dental                           | -2.5%       | 0.0%        |
| Vision                                 | -7.4%       | 0.0%        |
| <b>Other Fees</b>                      |             |             |
| HRA/VEBA                               | 0.0%        | 0.0%        |
| Clinic Fee                             | 1.5%        | 1.5%        |
| Other Costs                            | 1.0%        | 1.0%        |
| Compass                                | 0.0%        | 0.0%        |
| EAP                                    | 0.0%        | 0.0%        |
| Workers Compensation                   | 6.1%        | 6.1%        |
| <b>Overall Increase</b>                | <b>5.8%</b> | <b>6.0%</b> |

### CONCLUSION

The Healthy Kirkland Initiative has been successful in working toward all three objectives – economic incentives to promote informed health care choices, market transparency and promotion of health behaviors. While it is difficult to judge the overall health of the employee population, participation in the clinic and wellness incentive programs is the highest that the

providers have experienced. We have “bent the trend” in healthcare cost growth and we are expecting that our costs will be below the Cadillac Tax threshold should it take effect in 2022. Another illustration of the success of the strategy is that the employee balances in their HRA/VEBA accounts are in excess of \$3.7 million as of September 2018.

Phasing in the claims-related premium increase should still maintain a healthy reserve and allows the decisions in future budget cycles to recognize actual claims trends. The four-year strategy would result in a planned reserve drawdown illustrated below. The projected reserve above the minimum also acts as a hedge against worse than expected performance or the need to increase the reserve in the event that the IAFF returns to the City’s plan.

