



Memorandum

TO: HONORABLE MAYOR
AND CITY COUNCIL

FROM: Caroline H. Krewson

SUBJECT: SEE BELOW

DATE: March 26, 2018

Approved

Date

4/6/18

**SUBJECT: AMENDMENT TO THE VENDOR AGREEMENT WITH KAISER
FOUNDATION HEALTH PLAN, INC. FOR MEDICAL INSURANCE FOR
CITY EMPLOYEES, RETIREES AND THEIR DEPENDENTS**

RECOMMENDATION

Adopt a resolution authorizing the City Manager to negotiate and execute an Amendment to the Vendor Agreement with Kaiser Foundation Health Plan, Inc., for medical insurance for City employees, retirees, and their dependents, increasing the not to exceed Agreement amount from \$255,343,698 to a revised not to exceed amount of \$466,446,407; and extending the term of the Agreement from December 31, 2018 to December 31, 2020.

OUTCOME

Council approval of the Amendment will result in a two-year extension of the Agreement with Kaiser Foundation Health Plan, Inc. (Kaiser), to provide medical insurance to City employees, retirees, and their dependents.

BACKGROUND

Human Resources staff conducted a Request for Proposal (RFP) process in February 2014 for the City's medical plan, resulting in Agreements with Kaiser and Blue Shield of California (Blue Shield) from January 1, 2015 through December 31, 2018.

In February 2016, HR staff initiated an out of cycle RFP for all medical plans to explore cost competitive medical plan options. Due to Kaiser's contractual obligation with CalPERS, which prohibited Kaiser from providing rates to other agencies prior to providing them to CalPERS, and the timing of the RFP in February 2016, Kaiser did not provide rates in their response to the City's RFP. Therefore, Kaiser's response to the RFP was deemed non-responsive. The RFP resulted in new Agreements with Blue Shield and Sutter Health Plus from January 1, 2017

through December 31, 2020. The City also maintained its existing Kaiser Agreement, which is set to expire December 31, 2018.

ANALYSIS

The current Kaiser Agreement, covering calendar years 2015 through 2018, includes a not to exceed amount of \$255,343,698. This amount was determined in 2014 based on projections for enrollment and premium increases for the 4-year term.

Since 2015, there has been significant migration from Blue Shield to Kaiser, mostly due to the affordability of the Kaiser plans against the Blue Shield plans. This movement has been promoted in large measure by the City's cost-sharing model which is: the City pays 85% of the lowest cost non-deductible plan for active employees and 100% of the lowest cost plan available to an active employee for the pre- and post-65 retirees. Kaiser has continually had the lowest cost non-deductible plan and the lowest cost plan. Additionally, the Blue Shield plans have seen significant premium increases, while those of Kaiser have remained low. The result is that the enrollments for Kaiser increased much more than originally projected in 2014. As such, the amount of the current Agreement will be exceeded in 2018.

Kaiser plans have historically been very popular with high enrollment. With the increased migration into the plans over the years, Kaiser now accounts for approximately 80% of the City's employees and retirees enrolled in a Kaiser medical plan. This situation is unfavorable in that the risk for the smaller population in the non-Kaiser plans contributes greatly to the significant premium increases, rendering the non-Kaiser plans less desirable from a cost perspective.

As part of an effort to explore cost competitive medical plans to Kaiser, Human Resources conducted an off-cycle RFP in 2016 with the intent of soliciting proposals from medical plan providers which would not only provide plan offerings for the non-Kaiser population; but, also offer competitive rates to those of Kaiser, with the hope that enrollments would become more balanced between medical plan providers.

As noted above, the RFP resulted in new Agreements with Blue Shield and Sutter Health Plus from January 1, 2017 through December 31, 2020. The City also maintained its existing Kaiser Agreement, which is set to expire December 31, 2018.

For the competitive process and for the City to be able to offer medical plan choices, having the term end dates of the medical plan providers aligned is crucial, advantageous and preferred for many reasons including economies of scale for one RFP for all medical plan offerings and attracting bidders. Kaiser has agreed to extend the current Agreement for two years, until December 31, 2020. The premium rates will continue to be based on enrollments and utilization. Aon Hewitt, the City's Benefit Consultant, advises that Kaiser rates are competitive and supported by claims experience.

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To ensure the continued efficient and uninterrupted delivery of medical services to employees, retirees and their dependents, staff recommends an Amendment to the Agreement with Kaiser extending the term through December 31, 2020 to align with the term end dates of the Blue Shield and Sutter Health Plus Agreements, and increasing the maximum compensation under the Agreement to \$466,446,407, which includes projections for premium and enrollment increases. This new not to exceed amount includes the original Agreement amount of \$255,343,698, plus \$27,302,709 for the projected 2018 deficit due to inflated enrollment increases, as well as projections for 2019 of \$89,700,000 and for 2020 of \$94,100,000; the new costs totaling \$211,102,709.

EVALUATION AND FOLLOW-UP

This project addresses the Human Resources' performance measure of the cost of benefits administration and operations per budgeted full-time employee. The Employee Benefits Division of Human Resources ensures that the City of San Jose employees and retirees receive high quality and cost effective benefits by subjecting benefit plan providers to regular competitive processes (usually every four years).

PUBLIC OUTREACH

This Memorandum will be posted on the City's website for the April 17, 2018 City Council Agenda.

COORDINATION

This memorandum has been coordinated with the Office of the City Attorney and City Manager's Budget Office

COMMISSION RECOMMENDATION/INPUT

No commission recommendation or input is associated with this action.

COST SUMMARY/IMPLICATIONS

Per the City's Memoranda of Agreement with its bargaining units, the City's share of the premium cost for active employees is tied to the lowest-cost non-deductible plan, regardless of coverage level elected (employee, employee plus spouse/domestic partner, employee plus child(ren) or family coverage.). Per the City's Municipal Code, for retirees, the City's share of the premium cost is tied to the lowest cost plan available to active employees. Employees and

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retirees pay the difference between the City's share of the medical plan premium and the total premium cost of the plan each employee/retiree chooses.

The increase in enrollments over the last several years in the Kaiser medical plans has resulted in an estimated \$27,302,709 shortfall to cover the cost of the premium payments through December 31, 2018. Medical premium payments for 2019 and 2020 will vary based on actual enrollment and plan utilization, with premiums determined annually. Premiums for 2019 assume a 10% rate increase and a 5% rate increase for 2020. The following costs are based on January 2018 enrollment and estimated enrollment and premium increases.

The plan year 2018 projected cost to cover the deficit is \$27,302,709

1. The plan year 2019 projected cost is \$89,700,000
2. The plan year 2020 projected cost is \$94,100,000

The total cost for the two-year Amendment to the Kaiser Agreement, including the estimated 2018 deficit, is projected to be \$211,102,709.

BUDGET REFERENCE

Fund #	Appn #	Appn. Name	Total Appn.*	2017-2018 Adopted Budget Page	Last Budget Action (Date, Ord. No)
160	0116	Health Plans	\$51,840,000	Page 955	6/20/2017, 29962

*Funding in 2017-2018 for Health Plans is sufficient to cover the deficit described in this memorandum. Future year costs are subject to appropriation and will be included as part of the annual budget process.

CEQA

Not a Project, File No. PP17-003, Agreements/Contracts (New or Amended) resulting in no physical changes to the environment.

/s/
CAROLINE H. KREWSON
Director of Human Resources

For questions please contact Emily Hendon, Benefits Manager, (408) 975-1448.