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November 14, 2006

AGENDA ITEM 7

TO: MEMBERS OF THE HEALTH BENEFITS COMMITTEE

I. SUBJECT: Medicare Part D Options for 2008

II. PROGRAM: Health Benefits

III. RECOMMENDATION:

1. Staff recommends CalPERS participate in Medicare Part D for 2008 by:
   a. applying for the Retiree Drug Subsidy for Medicare-eligible members not enrolled in the Kaiser Medicare Senior Advantage program; and
   b. providing the Kaiser MA-PD plan for Kaiser Senior Advantage enrollees.
2. Staff recommends CalPERS notify the Legislature and Department of Finance by December 1, 2006, that the Part D participation of association plans for 2008 may differ from participation for 2007.

IV. ANALYSIS:

Background

The Medicare Prescription Drug, Improvement, and Modernization Act established a voluntary prescription drug benefit program (Part D) effective January 1, 2006.

Below is a summary of CalPERS participation in Part D:

For 2006:

- CalPERS applied for the Retiree Drug Subsidy (RDS) for Medicare-eligible members not enrolled in the Kaiser Medicare Senior Advantage program in September 2005; staff expects approximately $51 million in federal RDS payments for calendar year 2006.
- Kaiser enrolled its CalPERS Medicare Senior Advantage members in the Medicare Advantage Prescription Drug (MA-PD) plan.

- CalPERS requested an Attorney General opinion regarding various Part D issues at the direction of the Health Benefits Committee. By opinion dated November 2, 2006, (Attachment I) the Attorney General states that RDS payments by the Centers for Medicare and Medicaid Services (CMS) should be deposited into the Contingency Reserve Fund (CRF) and that the use of these funds should be pursuant to the statute governing the CRF with respect to those plans that generate RDS funds. A copy of the Attorney General's opinion is attached.

For 2007:

- 2006 budget control language provides, "The Public Employees' Retirement System shall continue to apply directly for the maximum possible amount of Medicare Part D drug subsidies in 2006 and 2007." It also provides that, "No Medicare Part D drug subsidy funds remaining in the Special Deposit Fund after payment of the uses listed in Provision 1 may be spent or transferred to other funds except upon appropriation by the Legislature."
- On June 21, 2006, the Board voted to apply for the RDS consistent with its application regarding Medicare Part D for calendar year 2006 (i.e., apply for the RDS for all Medicare-eligible members except Kaiser Senior Advantage members).
- The November 2, 2006 Attorney General's opinion states in footnote 6 that "[W]e find this budget act language to be contrary to both state and federal law."

For 2008:

- 2006 state budget control language provides, "If the Board of Administration of the Public Employees' Retirement System wishes to propose an amended approach concerning applications for Medicare Part D drug subsidy funds in 2008 or a use for Medicare Part D drug subsidy funds expected to be accumulated in the Special Deposit Fund, the Board of Administration shall submit a proposal for these purposes to the Chair of the Joint Legislative Budget Committee, the chairs of the appropriate fiscal and policy committees of the Legislature, and the Director of Finance on or before December 1, 2006."
- The Peace Officers Research Association of California notified CalPERS that it will independently pursue a health plan based PDP for 2008. According to the Department of Personnel Administration, the California Correctional Peace Officers Association and California Association of Highway Patrolmen have not yet determined their intent regarding Part D participation for 2008.

<u>Review of RDS and Health Plan Based PDP Comparison</u>

Below is a comparison of the RDS and the health plan based PDP using four criteria: disbursement flexibility, ease of administration, member impact, and federal financial participation.

Disbursement flexibility:

RDS – CalPERS will work with the Department of Personnel Administration, Department of Finance, and the State Controller's Office for distribution of the RDS funds consistent with the Attorney General's November 2, 2006 opinion.

Health plan based PDP – If not otherwise directed by 2007 state budget control language, CalPERS could negotiate with its health plans to use PDP funds to:

- reduce premiums only,
- reduce prescription drug co-payments only, or
- reduce premiums and prescription drug co-payments.

Ease of administration:

RDS – CalPERS has already established the necessary RDS administrative systems.

Health plan based PDP – PDP administration is relatively complex with numerous Centers for Medicare and Medicaid Services (CMS) requirements for:

- member support
- appeals systems
- member communications
- marketing, and
- reporting.

Blue Shield and Medco (Pharmacy Benefits Manager for our self-funded plans) would participate as health plan based PDPs and Kaiser would participate as a Medicare Advantage Prescription Drug (MA-PD) plan for its CalPERS Senior Advantage members. CalPERS would continue to administer an RDS system for CalPERS Kaiser members who are not Senior Advantage members and for all Medicare Western Health Advantage members.

Member impact:

RDS – Enrollees would continue receiving their prescription drugs without formulary disruption or network changes.

Health plan based PDP - There would be minor formulary adjustments affecting the tier assignment of drugs for our self-funded and Blue Shield plans. For the self-funded plans, CalPERS could choose to place these drugs in their current tier, so there would be no disruption to enrollees. To meet CMS requirements, Blue Shield would add some drugs to its formulary that are now non-formulary. This would reduce co-payments for these drugs because formulary drugs have lower co-payments than non-formulary drugs.

Medco informed CalPERS staff of other Medicare member impacts as follows:

- Current pharmacy networks may change.
- Members would no longer have a single identification card for health and pharmacy benefits. They would have two cards--one for health and one for pharmacy.
- The administrative appeals process would change.

If CalPERS had implemented the health plan based PDP in 2007 and reduced premiums and co-payments (eliminated generic and reduced brand formulary co-payments from $15 to $10):

- Kaiser would not have reduced its Medicare premium since Kaiser already accounted for its expected Part D payments when it proposed premiums; its single party monthly Medicare rate would have increased by $24 to account for reduced pharmacy co-payments.
- Western Health Advantage (WHA) would not have participated as a PDP; its single party monthly Medicare rate would have increased by $26 to account for reduced pharmacy co-payments.

Kaiser and WHA Medicare members whose employers make low premium contributions would have experienced increased out-of-pocket expenses to pay premiums.

Federal financial participation:

RDS – CMS bases RDS payments on 28 percent of drug costs between specified dollar thresholds per calendar year using claims experience for RDS-eligible members. The estimated RDS total gross revenue for 2007 is $58 million. After deducting administrative costs, the estimated net revenue is $57 million. (See chart below.) Since prescription drug claims increase year to year, we expect the RDS revenue to increase for 2008.

Health plan based PDP – CMS calculates payments to PDPs using an annually published national average of PDP bids for retiree prescription drug coverage, which CMS risk-adjusts based on the demographics of each health plan. CMS publishes the average PDP bid after CalPERS sets rates for a given year. The estimated total PDP gross revenue for 2007 is $65 million. This amount is not necessarily indicative of the revenue that would be available in 2008 since it depends on the national average bid CMS will publish by September 2007. After deducting administrative costs, the estimated net revenue is $53 million. (See chart below.)

The following chart shows estimated RDS and health plan based PDP revenue, administrative costs, and total net revenue for 2007, by health plan. Staff based RDS revenue estimates on projections of 2007 enrollments and health plan based PDP revenue on health plan estimates.

2007 MEDICARE PART REVENUE AND ADMINISTRATIVE COST

PLAN	Retiree Drug Subsidy			Health Plan Based PDP		
	REVENUE	ADMIN COST	NET REVENUE	REVENUE	ADMIN COST	NET REVENUE
Blue Shield (1)	$9,835,731	N/A	$9,835,731	$12,878,208	N/A	$12,878,208
PERS Choice (2)	$15,806,240	$191,440	$15,614,800	$18,475,662	$4,149,018	$14,326,644
PERSCare (2)	$31,629,430	$347,114	$31,282,316	$33,499,637	$7,522,903	$25,976,734
WHA (3)	$194,005	$0	$194,005	N/A		
CCPOA(4)	$110,420	N/A	$110,420	$144,576	N/A	$144,576
CalPERS Admin		$439,000	-$439,000		$439,000	-$439,000
TOTAL	$57,575,826	$977,554	$56,598,272	$64,998,083	$12,110,921	$52,887,162

Following are explanations of footnote references in the chart:

(1) Blue Shield will absorb RDS administrative costs. Blue Shield estimates CMS reimbursement of $48 per member per month under the health plan based PDP and will account for PDP administrative costs in its existing overall administrative fee.

(2) Medco will charge an RDS administrative fee of $0.55 per member per month. Medco estimates CMS reimbursement of $53.08 per member per month under the health plan based PDP and will charge a PDP administrative fee of $11.92 per member per month. See below for detail on Medco's PDP administrative costs.

(3) Western Health Advantage will have no RDS administrative costs and does not intend to offer a health plan based PDP for 2008.

(4) CalPERS applied for the RDS on behalf of CCPOA for 2007.

Medco PDP Administrative Costs Detail

Medco provided the following explanation of the costs associated with administering the health plan based PDP option for PERS Choice and PERSCare.

Medco's administrative fee of $11.92 per member per month includes a mark-up of $1.54, or 12.9 percent. Of the $11.92 (for non-pharmacy expenses), $10.38 is Medco's 2007 CMS bid submission for health plan based PDPs. This represents Medco's cost of providing PDP services.

CMS-required services fall into two categories:

1. Member support - communications and services ($5.86), which includes:
   - CMS-required marketing materials
   - Customer service calling costs

- Medication Therapy Management Program
- Reviews and appeals, including transition programs

2. Medco staff, operational support and account maintenance and systems support and setup ($4.52), which includes:
   - Operational support (CMS reporting, financial management, account team support, and other operational activities)
   - Third party vendor fees (enrollment, premium reconciliation, certification, Low Income Subsidy management)
   - Medicare required fees to support CMS systems development and to track the co-payments paid by each member to determine when a member enters the CMS mandated catastrophic coverage benefit stage.

Medco informed CalPERS staff that if CalPERS implements the health plan based PDP for 2008:

- Medco would waive its contracted program administration fee of $3.49 per subscriber for Medicare eligibles participating in the health plan based PDP.
- Medco expects overall drug costs will increase due to loss of some rebates and less deeply discounted mail and retail rates.

V. STAFF RECOMMENDATION:

Staff recommends CalPERS participate in Medicare Part D for 2008 by:

a. applying for the Retiree Drug Subsidy for Medicare-eligible members not enrolled in the Kaiser Medicare Senior Advantage program; and

b. providing the Kaiser MA-PD plan for Kaiser Senior Advantage enrollees.

This option has the following advantages:

a. results in maximum federal financial participation,

b. allows another year of experience to evaluate the administrative feasibility of the health plan based PDP, and

c. has less opportunity for member confusion and formulary disruption.

Due to 2006 state budget control language, staff also recommends CalPERS notify the Legislature and Department of Finance by December 1, 2006, that the Part D participation of association plans for 2008 may differ from participation for 2007.

VI. STRATEGIC PLAN:

This issue relates to the CalPERS Strategic Plan, Goal X to “Develop and administer quality, sustainable health benefit programs that are responsive to and valued by enrollees and employers.”

VII. RESULTS/COSTS:

The estimated RDS total net revenue for 2007 is $57 million. Since RDS payments are based on claims experience, we expect the revenue to increase for 2008.

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