



November 3, 2014

Honorable Mayor and Members of the Audit Committee:

An audit of eligible dependents on the City’s health benefit plans was conducted in accordance with the fiscal year 2014 audit plan. The audit was completed by HMS Employer Solutions. The scope of review included employee dependents enrolled in the City’s Blue Cross Blue Shield (BCBS) health care plans as of August 12, 2014. At the time of the audit, there were 415 employees with 935 dependents within the scope.<sup>1</sup>

**Background:** Dependent eligibility audits usually consist of a third-party vendor asking employees to provide documentation that proves their relationship to the dependents enrolled on their employer’s health benefit plan. Once documentation has been received, the vendor verifies that the relationship meets the definitions of eligible dependents under plan guidelines. Nationally reported average health care costs for each dependent range from \$2,000 to 3,500 each year. The typical ineligible rate for dependents audited ranges between 3% and 12%. Therefore, these audits can yield significant savings.

The City has two self-funded health care plans for employees and their dependents, a high deductible health care plan (HDHP) and a preferred provider organization (PPO) plan, both managed by BCBS. Because these plans are self-funded, the City can choose to be more generous than what is required by federal statutes in determining who to cover. Currently, covered dependents under both plans are as follows: (1) an employee’s spouse, (2) a child<sup>2</sup> of an employee who is under the age of 26, or (3) a grandchild who is an employee’s dependent for federal income tax purposes at the time application for coverage of the child is made.

**Audit Results:** Employees voluntarily removed 10 dependents from the City’s health care plans. Employees did not submit documentation for 19 dependents and submitted insufficient documentation for 15 dependents. Table 1, below summarizes these results.

**Table 1: HMS Dependent Eligibility Audit Results**

<b>Result Category</b>	<b>Dependents</b>	<b>Percentage</b>
<i>Verified</i>	879	94.0%
<i>Voluntary Removal</i>	10	1.1%
<i>No Documentation</i>	19	2.0%
<i>Insufficient Documentation</i>	15	1.6%
<i>Removed from Scope<sup>3</sup></i>	12	1.3%
<b>Total Dependents</b>	<b>935</b>	<b>100%</b>

<sup>1</sup> Not included in the scope were dependents only enrolled in the City’s vision plan.

<sup>2</sup> A child means the employee’s (a) natural child; or (b) legally adopted child; or (c) stepchild; or (d) an eligible foster child; or (e) grandchild that is a dependent for federal tax purposes; or (f) dependent child by legal guardianship based on IRS tax rules.

<sup>3</sup> During the audit several employees were terminated, resulting in 12 dependents being removed from the scope.

**Audit Impact:** There were 44 dependents identified for removal from the City’s health care plans by HMS, and they reported that the City would realize an annual savings of \$154,000 per year due to the audit. However, these savings make the following two assumptions: (1) these dependents would remain on the plan in perpetuity if the audit was not conducted and (2) an average annual cost per dependent of \$3,500 a year. However, it is difficult to determine how many of these dependents would have been removed voluntarily during open enrollment if employees were not asked to provide supporting documentation. In addition, as noted earlier, reported average health care costs per dependent range from \$2,000 to 3,500 each year.

Some employees’ family situations were complex; therefore, providing adequate documentation demonstrating dependent eligibility in a timely manner proved difficult. I fully expect that some of these employees will be able to submit the required documentation for their dependents during open enrollment in November. In addition, there were some dependents that will age out of the plan by January 2015. As a result, a more conservative estimate of the number of dependents that will be removed from the plan as a result of the audit is 31 rather than 44.

I also decided to use a more conservative estimate of \$2,750 annual cost per dependent in calculating potential savings rather than the \$3,500 figure HMS used—resulting in 2015 potential savings of \$85,250. If we reduce this amount by HMS’s fee of \$18,000, the estimated savings for 2015 would be \$67,250.

Table 2 below compares the adjustments I made to the savings calculations put forth by HMS.

**Table 2: 2015 Potential Saving Resulting from the Audit**

Result Category	Savings Identified by HMS Dependents		More Likely Dependents	
	Removed	Savings	Removed	Savings
Voluntary Removal	10	\$ 35,000	9	\$ 24,750
No Documentation	19	\$ 66,500	17	\$ 46,750
Insufficient Documentation	15	\$ 52,500	5	\$ 13,750
<b>Total Dependents</b>	<b>44</b>	<b>\$ 154,000</b>	<b>31</b>	<b>\$ 85,250</b>

**Audit Recommendations:** Based on (1) the results of the audit conducted by HMS and (2) a review of current city policies, procedures, and processes; Human Resources (HR) should consider the following recommendations:

1. A comprehensive plan to effectively communicate to city employees dependent eligibility requirements on an ongoing basis should be implemented. During the open enrollment process, the following should occur: (1) clear guidelines identifying who is and who is not eligible should be communicated to employees, (2) employees should be required to annually acknowledge eligibility of each dependent, and (3) employees should be informed that they will be subject to disciplinary action, which may include termination, if they are found to knowingly enroll an ineligible dependent.

**Management Response:** Management is in agreement with this recommendation. Human Resources has already modified the communications for new employees and for any employees adding dependents, to include the requirement for certifying dependent eligibility before being added to the City's Health Plan.

2. For the 2016 plan year, the City should consider changing its dependent criteria to "children for whom the employee is the legal guardian".

The greatest population of employees that would be affected by this change would be grandparents who would be required to seek legal guardianship in order to continue to cover their grandkids. Other dependents such as step children may also be affected by this change. For example, step children of an employee that live in another state and do not rely upon the employee for primary support can be covered under current plan rules.

**Management Response:** Management will take this into consideration. Current Health Plan policy, and other organizational practices, both locally and nationally include alternative legal documents for consideration. There is agreement that documentation should be required.

3. For the 2015 plan year, a process for verifying the dependents of employees not included in the scope of the audit should be implemented. This would include dependents of new hires and those who are solely on the City's vision plan.

The process utilized by HMS should be considered in guiding HR in the creation of this process. However, HR may not need to retain verification documents in order for the process to be adequate. For example, employees could be required to present acceptable documents evidencing dependent eligibility to HR. HR would then examine the documents to determine whether the documents reasonably appear to be genuine and record the document information on an eligibility form to be retained in the employee's file.

**Management Response:** Management is in agreement with this recommendation, and this practice is already in place.

The HMS report and management's responses to the audit recommendations are attached. I look forward to discussing this work during our audit committee meeting scheduled for November 17, 2014. If you have any questions prior to then, don't hesitate to contact me.

Sincerely,



Ty Elliott  
City Internal Auditor