Paying for the Ineligible: Costs and Consequences

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Cities, towns and counties, as all employers, face increasing costs in their health insurance premiums.
Employer subsidies of healthcare vary depending on the company, but most employers finance some or most of dependent eligibility coverage for eligible employees. However, there is a growing trend within organizations for employees to share (co-pays) some part of the increasing costs in healthcare premiums. This creates an additional burden on the employees as healthcare costs continue to rise.

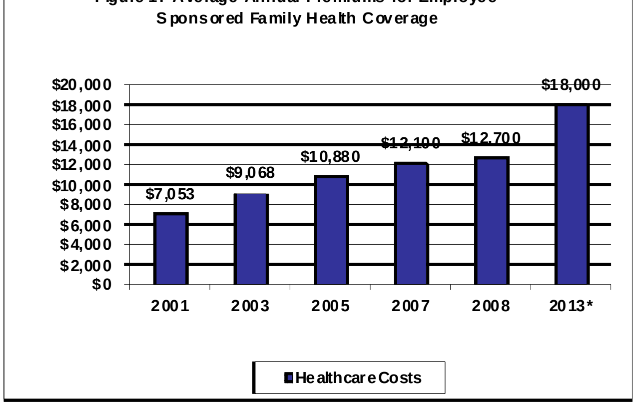
Reducing costs for both employer and employee is a priority for human resource managers in city and county governments. What, therefore, are the remaining available options for managing healthcare resources? Premiums continue to rise despite the implementation of carrier and health plan negotiations, high deductible plans, health reimbursement accounts (HRAs), health saving accounts (HSAs), and flexible spending accounts (FSAs). This rise in premiums is not expected to change in the near term.

The introduction of dependent eligibility audits is growing in popularity because of several factors. One is increasing premium costs; another is the legal challenges of carrying ineligible dependents on a plan. A *Wall Street Journal* article reported that between 10% to 15% of employees had one ineligible dependent on their insurance plans.[1] Eligibility restrictions typically range from change in marital status, unreported death of a dependent, and age of children, to an unauthorized dependent (nephew, grandchild, ex-spouse, etc.) This article will discuss these areas, the challenges associated with this subject, and steps for implementing changes.

Increasing Healthcare Premium Costs: Impact on the Employer and the Employee

The impact of rising healthcare premiums affects both employer and employee alike. The annual premium that a health insurer charged an employer for a health plan covering a family of four-averaged $12,700 in 2008. Contributions by employees averaged $3,400, or 12 percent more than they did in 2007. The annual premiums for family coverage significantly eclipsed the gross earnings for a full-time, minimum-wage worker ($10,712). In addition, workers now contribute roughly

Figure 1: Average Annual Premiums for Employee-Sponsored Family Health Coverage



$1,600 more in family coverage than they did in 1999.[2] Figure 1 illustrates the increase in premiums and the projection for premium increases through the year 2013.[3] The average cost for dependent coverage ranges from $3,000 to $5,000; between 2%-8% of this amount is ineligible for coverage.[4]

These costs affect employers' ability to provide pay increases, hire new employees, fill vacant positions~~,~~ and, in some organizations, allocate resources for research and new product development.

Legal Challenges Connected with Funding Ineligible Dependents

Employers who unknowingly allow coverage of ineligible dependents face several legal challenges.

- Sarbanes-Oxley Act (SOX) non-compliance
- Possible violation of the ERISA/Exclusive Benefit Rule
- Possible exposure under IRS Section 125

Sarbanes Oxley Act Non-Compliance

The Sarbanes-Oxley Act of 2002 (SOX) requires that a company's management to assess and report the effectiveness of its internal controls over its financial reporting. An independent external auditor must confirm the accuracy of the financial reporting. The auditor must also attest to the accuracy of the organization's~~'~~ internal assessment, including any shortcomings, such as the coverage of ineligible dependents.[5] It is necessary for the Chief Financial Officer (CFO) to coordinate with the Health Resource Department, in order to avoid possible exposure under SOX.

Exclusive Benefit Rule of ERISA

The Exclusive Benefit rule of ERISA requires that the plan sponsor(s) attest there are no claims paid to non-eligible dependents.[6] The fiduciary must discharge duties with respect to the Plan for the *exclusive* benefit of participants and their respective beneficiaries. [7] Personal liability may accrue to a benefits supervisor or plan sponsor who knowingly pays claims for ineligible dependents.

IRS Section 125

The IRS allows pre-tax employee contributions for qualified cafeteria plans and beneficiaries *only*. If an employer allows pre-tax contributions for unqualified dependents, there may be liability consequences. Traditional enrollment processes generally require employee attestations to evidence dependent relationships. These are inadequate to meet the required financial and fiduciary responsibility of plan sponsors and benefit administrators today. Depending on the plan design and employee demographics, removing these ineligible dependents can save an estimated two to five thousand dollars annually per dependent, and comply with IRS rules and regulations.

Best Practices Regarding Dependent Eligibility Audits

The methodology, communications, and follow up associated with implementing a successful dependent eligibility audit are of great importance. Generally, the steps to follow are:

Step 1: Amnesty Phase

Communication is sent to all covered employees notifying them that an audit will occur to verify eligibility of all covered employees. The communication should define the plan's eligibility requirements and the legal reasons surrounding the necessity for such an audit, as well as stressing the possible benefits to employees in terms of controlling their out-of-pocket expenses such as premiums co-pays and deductibles. Each employee receives a list of covered dependents and is instructed to make any necessary changes to the coverage status for each dependent listed. This is done with the understanding that there will be no negative action or penalty imposed by the employer with respect to any ineligible dependents dropped during the amnesty phase of the process.

Communication during amnesty phase

All employee communication should include:

- Explanation of the audit and reasons for conducting the audit (both financial and fiduciary)
- Terms and length of amnesty period (generally this is 30 days)
- Instructions for dis-enrolling ineligible dependents
- Consequences for continuing enrollment of ineligible dependents (cite legal and financial)
- 800 number call center for questions and hours available
- Notice that documentation verifying dependent status maybe requested at the conclusion of the amnesty phase
- Assurance that no penalties will be enacted during this phase
- Where to send the information confidentially

At the conclusion of the amnesty period, an evaluation of the post-amnesty enrollment relative to the pre-amnesty enrollment pattern is done. Any patterns of reduction and categories of potential concern are noted.

Step Two: Documentation of Eligibility Phase (Compliance Period)

This phase deals with the collection of the employee material necessary to provide formal documentation and verification of dependent status. Depending on the number of employees, all or part of an employee population is selected. Though conducting the audit on a sampling of the employee population may cost less in up-front administrative fees, collecting documentation on the entire population can generate the highest savings. In addition, it eliminates the perception that a group of employees have been "singled out" for an audit. Subset populations may be selected at random to provide a statistically valid sample for analysis or the population may be a focused sample, driven by changes in covered expenses combined with higher than average dependent medical expenses.

Employees are informed that, unlike the amnesty phase that releases the employee from any financial obligation, penalties imposed on ineligible dependents during this phase may be more severe and include reimbursement of plan paid expenses.

Information Packet
The employees receiving the audit information include a packet with the following information:

- Specific information on eligibility criteria
- Current list of the individuals enrolled as dependents under the employee's plan coverage
- List of valid documentation employees need to verify for covered dependents. This includes:
    - Tax documents (communication to include instructions about redacting confidential financial information)
    - Copy of spouse/domestic partner's pay stub showing address matching employee's residence
    - Declaration and registration of informal marriage certificates
    - Birth certificates/adoption papers for dependent children
    - Court orders for guardianship or financial responsibility of dependents
- Authorization allowing employer or external vendor to verify documentation provided, e.g. verification of spouse/domestic partner's address through ChoicePoint or other background check service
- Deadline for submitting information
- Where to submit information

Communication can be sent to employees via the U.S. Postal Service, other mail service, or email. Employees may respond via mail, facsimile, or through a secure web portal. During this compliance period, employees may contact the call center, email a designated address, or access a secure web portal to ask questions. All communication and information received from employees must be tracked and maintained on a secure system.

Tracking
The compliance period should include up to two letters or unlimited emails, and a reminder phone call to non-responders. Documents should be reviewed and logged as they are received. Copies of all written communication and a log of all phone calls should be tracked in the system. Employees are notified of any deficiencies or discrepancies as soon as possible. This assures that there are no delays in communication.

Step Three: Wrap Up and Final Analysis

At the conclusion of the documentation phase, results are collected and a final report is compiled to review results. Depending on the outcome of the audit, improvements in plan design are implemented to increase documentation efficiency, prevent future ineligible dependents from remaining on the plan, and expand communication to employees and new enrollees in the plan. These improvements can include some of the following:

- Web portal for notifying employees of plan changes, and updating information
- Notification to employees that audits will continue at random periods in the future
- Explanation for the reasons and importance of maintaining current information dependents enrolled in the plan

Summary

Dependent eligibility audits are a valuable tool that can be used to:

- reduce employer healthcare costs,
- reduce employee healthcare premiums, deductibles and co-pays,
- improve communication between employee and employer,
- increase communication between the human resource division and the finance department, and
- maintain an employer's compliance with fiduciary obligations imposed by federal statute.

If they are conducted with proper communication and confidentiality, both parties (employee and employer) view them as a valuable asset for the organization to maintain cost controls and legislation compliance.

Faith Glover, CEO for Sagebrush Solutions, LLC, has over 30 years of experience in the healthcare field. Ms. Glover has experience in all aspects of health care—from direct delivery of services to product development and management consulting. Her specific expertise encompasses data analysis and management, as well as new product development of data analysis software. Faith has an RN from Massachusetts General Hospital and a MBA from New York University. Additionally Faith is a Certified Fraud Examiner, certified by ACFE.

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[1] Wall Street Journal, March 2004
[2] The Henry J. Kaiser Family Foundation. Employee Health Benefits: 2008 Annual Survey. September 2008
[3] National Coalition on Healthcare Estimate
[4] HR Management, June 4, 2009
[5] Sarbanes-Oxley Compliance Guidelines
[6] Department of Labor Compliance Guidelines
[7] 29 U.S.C. §1104 (a) (1) (A)