



EXHIBIT 7  
DATE 4-1-05  
SB 154

March 9, 2005

Mr. Tom Bilodeau  
Director of Research, Bargaining & Member Benefits  
MEA-MFT  
1232 E 6th Ave, Helena, MT 59601

**Re: Administrative Cost Study for HB124 / K12-SHIP**

Dear Tom,

In response to the MEA-MFT request, this letter contains the results of our administrative cost analysis for the HB124 / K12-SHIP program. Following is a summary of the project scope, as well as a description of the data gathering process, definition of administrative cost and other assumptions, and results of the analysis.

Project Scope

MEA-MFT requested that eBenX / SHPS help determine the proportion of health care premiums allocated to administrative costs for school district plans in Montana. Based on our understanding, the purpose of the analysis is to respond to statements that the 7% administrative cost assumed in the K12-SHIP premium development and budget estimates was high.

Data Gathering Process

Since gathering data for all districts was not feasible within the given timeframe, the analysis attempted to study a cross-section of districts. This cross-section included a pool of primarily small school districts (MUST), two large school districts (Bozeman and Missoula), as well as the State Health plan. Data collected included total premiums paid, claims paid, expenses for various administrative categories, and contributions to (or withdrawals from) general reserve funds.

Though attempts were made to identify specific areas of administrative costs, the data received did not provide enough detail to confidently report on specific areas. Therefore, results were presented in broader administrative cost categories, as detailed below.

Results

The following table illustrates the percentage of premium charged to each component.

Period	Bozeman 9/03 - 8/04	Missoula 7/03 - 6/04	MUST 7/03 - 6/04	State Plan 1/04 - 12-04
Claims	90.7%	77.2%	83.4%	83.1%
Contribution to Reserves	-6.7%	15.3%	7.9%	12.9%
Stop Loss Premiums	7.7%	5.2%	0.8%	0.0%
General Administration	8.3%	2.3%	7.9%	4.0%
Total Administration	16.0%	7.5%	8.7%	4.0%

The percentages vary significantly, but all are well above the 3.5% to 4.0% quoted by those concerned with the 7% assumption. The State Plan at 4.0% is the exception, but there is a high likelihood that some portion of the 12.9% allocated to reserve contributions should be allocated to administrative costs.

Since it is unlikely that stop loss insurance will be purchased for the K12-SHIP program, the general administration estimates provide a good comparison for the required administration percentage. Also keep in mind that there are implicit costs that would not be required under the K12-SHIP program; for example, the MSSF sponsorship fees currently paid by MUST.

To conclude, there is no evidence to support the claim that administrative costs are less than 4% of premiums.

Please feel free to call with any questions or concerns.

Sincerely,

Kelly Grebinsky, FSA, MAAA

kwg/kwg  
Admin Cost Analysis - 03-09-05.doc

### Definition of Administrative Cost / Other Assumptions

With any study involving administrative cost, it is imperative to establish a consistent definition across entities. While many definitions exist in the healthcare marketplace, the K12-SHIP analysis incorporated the following approach.

To begin, premium payments were separated into three major components: payments required to cover claims costs, payments required to cover the cost of administering the program, and payments used to build or draw down from general reserve funds.

For the purpose of this study, we have defined administrative cost as including, but not limited to, expenses related to the following items:

- Eligibility processing and maintenance fees
- Claims processing fees
- Wellness program fees
- Stop loss insurance premiums
- Member education expenses
- Staff expenses (only if included in financial statements or provided separately)
- Consulting / auditing / actuarial fees
- Other miscellaneous expenses

It is important to note that, although other district staff time is spent on projects related to their health program, we would expect many of these activities to continue in the same way under the K12-SHIP program.

All of these expenses, with the exception of stop loss insurance premiums, are expected to occur under the K12-SHIP program. Because the administrative cost details we received were not consistent across entities, it was impossible to identify specific cost areas. The only identifiable expense across all entities was stop loss insurance premiums. Therefore, administrative expenses were separated into two categories: stop loss insurance premiums and general administration. Total premiums were then allocated to these two categories, along with claim payments and contributions to reserves.

While applying the above definition of administrative costs, the following general assumptions were observed:

- Assume the percentage of total costs identified in the studied population provides a good representation of Montana school districts.
- Assume the administrative cost percentage for the period studied provides a reasonable estimate for future periods. However, it is understood that administrative costs become a smaller percentage of total premiums during periods where medical claim trends exceed administrative cost trends.