Benefits Audit 101: How to Conduct an Internal Audit for Dependent Eligibility

Andrew Weegar – Employee Benefits Specialist
August 11, 2017

Nothing in this presentation is intended to constitute financial or investment advice. Please consult with your legal, tax, or financial advisor for more information about your personal situation.
Established 39 years ago, IPS Advisors is an independent benefits consulting firm. Our governmental division services over 45 municipalities, counties and State agencies across Texas with their health and welfare benefits planning needs.

We provide specialized services through our core practice areas:

- **Corporate Benefits Consulting**
  - Long Term Strategic Planning
  - Fully Insured and Self Insured Benefits Programs
  - Health Risk Management Programs
  - Compliance Assistance
  - Benefits Administration
  - Retiree Consulting – GASB / OPEB Services

- **Corporate Retirement Consulting**
  - Qualified and Non-qualified Plans
  - Governmental (457/401a, etc.)

- **Life Insurance Portfolio Management**
Overview

- What is a Dependent Eligibility Audit?
- Why is it important to audit dependent eligibility?
- How to implement and manage an internal Dependent Eligibility Audit?
- Determining if your organization can internally manage dependent eligibility.
- Questions?
What is a Dependent Eligibility Audit?

- A dependent eligibility audit verifies that individuals listed by employees as eligible for coverage under the plan—primarily spouses and dependent children—indeed meet the plan requirements for eligibility. Many times a simple employee certification or affidavit of dependent eligibility does not provide proof of continued eligibility after the initial date of hire, and therefore an audit requires employees to submit documents that substantiate eligibility.

- The purpose of a dependent eligibility audit is to ensure only those entitled to health coverage are receiving health coverage.
Define "Dependents" Clearly

- Spouse
  - If state law does not apply, does the employer want to include domestic partners, common-law spouses, same-sex spouses?
    - Never use "spouse" without a definition

- Child
  - Health care reform requires coverage to age 26
  - Who is a "child"?
    - Federal law: Some gray areas, but Safe Harbor is defined as biological, adopted or placed for adoption, step-child, or foster child (placed by state agency or court order)
    - Never use "child" without a definition
Define "Dependents" Clearly

- Others
  - Can be as broad as employer wishes
  - But be aware of tax issues
  - Never use "dependent" without a definition
  - Be very cautious if using "tax dependent"—be sure you understand the breadth of the definition in the tax code and that you really want to cover all who meet the definition
    - Definition of "dependent" for federal income tax purposes at 26 USC § 152
Most Common Potential Ineligible Dependents

- Divorced spouses
- Step-children following divorce of natural parent
- Over-age dependents
- Grandchildren or other extended family dependents under no legal guardianship
- Unmarried partners with no recognized relationship under the plan
- Children of live-in partners with no legal relationship
Why is it important to audit dependent eligibility?
Dependent Audits – Did you know?

- On average, 8-10% of dependents are found to be ineligible.

- Cost savings on average of $3,500 per ineligible dependent removed from plan. Can be much higher.

- Given the opportunity, 46% will try to reenroll an ineligible dependent.

### Sample Audits - Texas Municipalities in 2016

<table>
<thead>
<tr>
<th></th>
<th>Dependents Reviewed</th>
<th>Member Response Rate</th>
<th>Ineligible Dependents</th>
<th>Found Ineligible</th>
<th>First Year Savings</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>659</td>
<td>99.7%</td>
<td>11.5%</td>
<td>76</td>
<td>$228,000</td>
</tr>
<tr>
<td></td>
<td>756</td>
<td>95.3%</td>
<td>6.1%</td>
<td>46</td>
<td>$138,000</td>
</tr>
<tr>
<td></td>
<td>3,367</td>
<td>94.0%</td>
<td>10.9%</td>
<td>368</td>
<td>$1,101,000</td>
</tr>
<tr>
<td></td>
<td>759</td>
<td>98.8%</td>
<td>3.4%</td>
<td>26</td>
<td>$78,000</td>
</tr>
<tr>
<td></td>
<td>1,896</td>
<td>94.6%</td>
<td>10.8%</td>
<td>205</td>
<td>$615,000</td>
</tr>
<tr>
<td></td>
<td>1,301</td>
<td>99.2%</td>
<td>1.5%</td>
<td>19</td>
<td>$62,924</td>
</tr>
<tr>
<td></td>
<td>3,882</td>
<td>98.3%</td>
<td>5.1%</td>
<td>197</td>
<td>$591,000</td>
</tr>
<tr>
<td></td>
<td>1,174</td>
<td>99.8%</td>
<td>1%</td>
<td>12</td>
<td>$60,000</td>
</tr>
</tbody>
</table>

-Towers Watson
Market Trends

- Although not a new practice, Dependent Audits are becoming increasingly popular in the public entity space due to increasing costs of spousal / dependent coverage and ACA coverage requirements.
- Total dependent costs (Spouse and Children) typically range from 50% to 70% of the overall cost of health care.
- On average spousal claims cost is 1.2 x greater than employee claims cost.
- The average public sector contribution towards dependent coverage is 63% and can significantly exceed other private entities dependent subsidies.
- Approximately 30% of employers conduct Dependent Audits of their Health Plan.
How to implement and manage an internal Dependent Eligibility Audit?
Process: High Level

- Planning: 30 days
- Verification: 30-45 Days
- Grace: 15-20 Days
- Optional Amnesty Period
- Completion Removal of Ineligible Dependents
- Ongoing Programs
Planning Phase – 30 Days

During the planning phase, it is recommended to create and establish a well defined documented project workbook.

- Assign a dedicated team / project manager.
- Notify insurer, TPA, or claims administrator that audit is taking place.
- Confirm the project timeline and plan.
- Analyze SPD rules and guidelines to define the required verification process.
- Review and complete design of the employee communications.
- Define and test enrollment files.
- Train your team.
- It is recommended to complete this process in 30 days, but this is flexible!

*Optional – some employers may establish an amnesty period.*
During the planning phase, it is important to notify employees in advance that HR will be requesting dependent documentation. Here are a few ways you can provide this announcement:

- Employee Newsletter
- Website Notice – Benefit Administration Website
- Broadcast e-mail or voicemail
- Worksite posters
- Bulletin boards
- Social Media
- Group Meetings
- Mail
Verification Phase – 30 to 60 days

Initial Letter

☑️ A letter that lists the dependents on the plan, the rules for eligibility, and required documents to be submitted by the plan member. Includes a detailed FAQ.

*For Consideration*

☑️ A reminder letter is recommended to be sent out if employees have not submitted documents by a certain date.

Final Notice

☑️ A few days into the Grace Period, a FINAL notice will be sent which explains the consequences of a partial or non-response and provides a final opportunity to comply (Grace Period deadline announced).
Required Documents (continued)

- Documentation for spouse, domestic partner, same-sex spouse
  - Marriage certificate plus statement under penalty of perjury that the marriage is still intact.
  - Domestic partner registration if state recognizes the relationship; statement under penalty of perjury if the state does not; statement under penalty of perjury that the relationship is intact.

- Documentation for child
  - Birth certificate naming employee as parent.
  - Birth certificate naming employee's spouse as parent (for step-child).
  - Adoption decree or evidence of placement for adoption.
  - Court order placing child with employee or evidence of placement by state agency (for foster child).
Required Documents (continued)

- Documentation for others
  - Will depend on how other eligible dependents are defined by the plan; for example:
    - Evidence of shared residence?
    - Evidence of financial support?
    - Evidence of full-time student status?
    - Evidence of disability?
  - If plan allows coverage of "tax dependents," copy of tax return
    - But note: Tax returns are for previous years; plan wants proof of current status; tax return plus statement under penalty of perjury might be better.
Follow-Up Communications

During the Verification Phase, it’s important to provide strong outbound communication:

**Customer Response Letter**
- For incomplete submissions, it is recommended to complete customized response letters that will highlight the areas of non-compliance and request that the plan member provide specific additional information.

**Voluntary Termination Confirmation Letter**
- For plan members that elect to remove one or more dependents, a termination confirmation letter is recommended to be sent to ensure the intentions of the plan member are properly captured.
Grace Period – 15 to 20 Days

The response rate is typically around 85% by the start of the Grace Period. Some members will have procrastinated, or simply chosen not to respond.

Some groups will extend this Grace period of 15-20 days to give a little extra time to partial or non-responders.

- Final Notice Letter
- E-mail Blast
- Personal HR Interaction (internal outreach)
Completion of Audit – Ineligible Dependents

- If an employee is unable to establish a dependent relationship, the employer may impose penalties, terminate coverage or seek reimbursement for claims paid for ineligible dependents. It is not typical for employers to seek out disciplinary action as a result of the initial audit. Some employers also offer an appeals process to give those deemed to have ineligible dependents (or non-respondents) a chance to reinstate their children or spouses.

- The Affordable Care Act (ACA) limits an employer’s ability to retroactively remove ineligible dependents from coverage. Under the law, a rescission (or retroactive cancellation of coverage) is permissible only if the individual obtained coverage through fraud or an intentional misrepresentation of material facts and the individual is given at least 30 days advance notice of the rescission. An employer can avoid the law’s restrictions on rescissions by canceling coverage on a prospective basis.
Completion of Audit – Ineligible Dependents

- Disenrollment may not be a COBRA qualifying event, but an employer may choose to offer COBRA to all, not just those that are truly COBRA eligible as a result of the audit. Self-insured plans should get permission from their stop-loss carriers and fully insured plans should get permission from their insurers before offering COBRA coverage to all ineligible dependents removed from coverage.

- Also, an employer may need to retroactively adjust employee W-2s for those employees who made pretax contributions for an ineligible dependent. For this reason, some employers choose not to seek reimbursements for past claims, but simply to deny coverage to ineligible dependents going forward.

- It is recommended that enrollment forms and plan documents be amended to reflect the process that will be followed in determining dependent eligibility going forward, such as frequency of audits, verification process at the point of new employee enrollment and penalties.
On-Going Recommendations

- Make sure eligibility is communicated effectively to employees if not so today.
- Continue to validate the eligibility of new dependents and spousal relationships for new hires or new benefit eligible employees.
- Determine when to complete the next Dependent Eligibility Audit. (Do you consider outsourcing?)
- If eligibility requirements change, it is recommended to complete a new eligibility audit.
- Enhance internal privacy and security. Ensure data is backed up and employees handling materials are fully HIPAA compliant. (Ask your consultant for training details)
- Document all communication materials!
Determining if your organization can internally manage Dependent Eligibility
Can my organization Manage an Internal Audit?

- Typically smaller fully insured public entities (under 250) elect to conduct dependent audits internally due to costs of outsourcing.

- Many larger self insured public entities hire independent audit firms due to resources and technology required for larger employee populations. A larger employer may choose to use the independent third party auditor for ongoing audit of new dependent enrollment.

- Outside Audits can be done on Flat Fee or % of Savings basis. A flat fee ranges from $15,000 to $25,000 for a third party dependent audit of 500 Employees. A percent of savings contract can range from 20% to 30% of savings obtained.

- For larger public entity populations, Independent Audit firms will put a Return on Investment guarantee in place from 1:1 to 3:1.

- Using an outside audit firm may help with employee perception of the independence and objectivity of the Audit.
Recap – 5 Benefits of a Dependent Audit!

1. Produce significant savings
2. Strengthen benefit plan compliance
3. Improve employee understanding of company benefits
4. Create a culture of compliance
5. Dependent data is validated