

**IMMEDIATE
ATTENTION**

EB/CAP/01/3

November 1, 2001

To: Members of the Committee on Administrative Policies
From: The Committee Secretary
Subject: **Medical Benefits Plan Financial Position**

Attached for consideration by the Committee is a paper on the financial position of the Medical Benefits Plan.

Questions may be referred to Mr. Nicoson (ext. 38223) and Mrs. Shannon (ext. 37258).

In the absence of a request to the Committee Secretary by noon on Thursday, November 8, 2001 that this matter be taken up by the Committee, the proposed recommendation that appears on page 5 will be deemed approved by the Committee for transmittal to the Executive Board.

Att. (1)

Other Distribution:
Members of the Executive Board

INTERNATIONAL MONETARY FUND

Refund of Contributions to Medical Benefits Plan

Prepared by the Human Resources Department

Approved by Ulrich Baumgartner

October 31, 2001

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I. INTRODUCTION

1. The purpose of this paper is to propose that the Committee on Administrative Policies (CAP) recommend to the Executive Board the approval of a refund to the Fund and Medical Benefits Plan (MBP) participants of a portion of the MBP reserve. These reserves are currently well in excess of the target level.

II. BACKGROUND

2. By the end of CY2000, the MBP reserve had risen to 44 percent of expenses, well above the target level of 20 percent of projected annual expenses.¹

3. The following table shows: the MBP's actual income, expenses, and reserve levels for the period CY1998-2000; the projections for CY2000 prepared in early 2000; and the current projections for CY2001.

MBP Finances for CY 1998–2001									
(In thousands of U.S. dollars)									
	1998 (actual)	1999 (actual)	Percent change	2000 ¹ (proj.)	Percent change	2000 (actual)	Percent change	2001 ² (proj.)	Percent change
Total Income	23,149	26,490	14.4	27,930	5.4	31,282	18.1	35,275	12.8
Total Expenses	21,590	28,102	30.2	29,280	4.2	24,251	-13.7	30,874	27.3
Surplus (deficit)	1,558	-1,612		-1,350		7,030		4,401	
End of year reserve	4,497	2,886		1,536		9,916		14,317	
Reserve as a percentage of total expenses	21%	10%		5%		44%		46%	
¹ Projections made prior to contribution rate increase with effect from May 1, 2000.									
² The projections of income and expenditures in CY2001 are based on experience through September 2001.									

4. Against the background of a large increase in expenditures and a sizable MBP deficit in 1999, MBP reserves were projected to fall to 5 percent of projected expenses by the end of 2000, substantially below the target level of 20 percent. Consequently, a 15 percent increase in contribution rates with effect from May 1, 2000 was approved by the Executive Board in April 2000. With this increase in contribution rates, total income was expected to rise to about \$30.4 million in CY2000. However, the reserve level was projected at less than 20 percent of expenses at the end of CY2000, rising to 20 percent in the course of CY2001.

5. In the event, developments in MBP finances in CY2000 were substantially more favorable than projected. Three factors contributed to this better-than-expected outcome:

¹The target level of the reserve was raised from 12 percent to 20 percent of projected annual expenses in 1998 (EB/CAP/98/2).

- MBP expenses declined by 14 percent rather than increasing by 4 percent as envisaged in the projections. This sharp decrease was partly attributable to a drop in large claims.² In CY2000, these claims amounted to \$3.9 million, equivalent to 16.1 percent of total expenses. By comparison, in CY1999, large claims amounted to \$6.1 million, equivalent to 21.8 percent of total expenses. Other expenses also rose less rapidly than anticipated.
- In addition, the Preferred Provider Organization (PPO) discount arrangements implemented in 2000 produced savings to the Plan of \$3.6 million. The earlier projection estimated these savings at \$2.3 million.
- Income grew at a somewhat faster pace than projected owing to a more rapid increase in the number of enrollees and a slightly higher salary increase than anticipated in the original estimates. With the increase in contribution rates, income was projected at \$30.4 million, but actually amounted to \$31.3 million, or about 3 percent higher than anticipated.

III. PROJECTIONS FOR CY2001

6. HRD's projections for CY2001 are based on the following assumptions:
 - MBP expenses are projected to increase by 27 percent. There has been a significant upward trend in expenses for the past three months. In addition, it is expected that staff and families may seek increased medical attention for stress and anxiety caused by recent events which would also contribute to higher than normal costs.
 - Based on the latest claims information, large claims were projected at \$2.4 million or 8 percent of total expenses, which is unusually low given the historic large claims experience. However, the MBP's administrator has identified four potential organ transplant cases which have not yet reached the large claim level. It is prudent to use a projection based on the annual average of large claims since 1997 of \$4.4 million.
 - PPO savings are projected to be about 10 percent of expenses (close to \$3 million).
 - Income is projected to grow by about 13 percent over CY2000, based on the current contributions rates and participation levels.

²Large claims are those in excess of \$50,000. In a typical year, 20 to 30 individuals account for the large claims experience out of an entire enrolled population of almost 10,000. The small size of the group incurring large claims makes predicting large claims experience, on a year-to-year basis, very difficult.

7. Projected income in CY2001 is \$35.3 million while expenses are forecast at \$30.9 million. These projections imply a surplus of \$4.4 million and a reserve level of \$14.3 million, or 46 percent of expenses, at the end of CY2001.

Sensitivity analysis

8. Given the volatility of large claims, a sensitivity analysis is provided below to demonstrate the effect of changes in large claims on expenses and the MBP reserve. All scenarios assume the same level of income, \$35.3 million, and that the PPO will continue to generate the current level of savings, though these savings cannot be guaranteed as providers are becoming more aggressive in dealing with PPOs and other managed care organizations. Scenario 'A' shows projected expenses based on the current level of large claims, making no allowance for large claims which are likely to arise from possible organ transplants mentioned earlier. Scenario 'B' is the central scenario and corrects for the additional large claims expected. Scenario C shows that even if large claims as a percentage of total expenses increase to the 1999 level, the projected reserve will grow to more than one and one-half times the required level.

Large Claims Scenarios (In thousands of U.S. dollars)						
	Large Claims	Large Claims as Percent of Expenses	Projected Expenses CY2001	Percent Change Over CY2000	Total Reserve	Reserve as Percent of Projected Expenses
A	2,430	8.4	28,941	19.3	16,250	56.2
B	4,370	14.2	30,874	27.3	14,317	46.4
C	7,389	21.8	33,893	39.8	11,298	33.3

IV. CONCLUSION AND RECOMMENDATION

9. In the event that reserves exceed the target level, the Executive Board may be asked to approve a reduction in contribution rates, normally in conjunction with the Administrative Budget. A refund of contributions or a contribution holiday may also be considered by the Board in lieu of, or in addition to, a reduction in the contribution schedule. (See EB/CAP/00/1, 4/13/00).

10. With projected expenses of \$30.9 million in CY2001, the target level of the reserve should be \$6.2 million. The current level of the reserve is \$14.1 million and is expected to rise slightly to about \$14.3 million by the end of the year. Consequently, approximately \$8 million of it could be returned to the participants and the Fund. Contributions and refunds are shared between the Plan participants and the Fund, with the participants contributing 25 percent of the cost and the Fund contributing 75 percent. Consequently, the Fund would receive \$6 million and the participants would receive \$2 million, or about \$500 per participant on average.

If present financial trends continue, it is likely that excess reserves will continue to accumulate. The reserve levels will be examined again in early 2002 to determine if there is a case for a reduction in contribution rates with effect from May 1, 2002 (in addition to any further refund).

PROPOSED RECOMMENDATION

It is proposed that the Committee on Administrative Policies recommend the following draft decision for adoption by the Executive Board on a lapse-of-time basis.

The Managing Director is authorized to implement the return of \$8 million of the Medical Benefits Plan (MBP) reserves to MBP participants and the Fund in proportion to their respective contributions to the MBP.