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February 23, 2006

Debra K. Davenport, CPA  
Auditor General  
2910 North 44<sup>th</sup> Street, Suite 410  
Phoenix, AZ 85018

Dear Ms. Davenport:

I would like to thank you and your audit team for the professional and thorough way that you managed the audit of the Healthcare Group of Arizona (HCG). The audit was invaluable to my office and the management of Healthcare Group as we had the opportunity to evaluate the processes, procedures and financial management of the health plan. We also appreciate the disciplined way your staff reviewed the financial reserving methodology used by HCG. Now that HCG is self funded it is critical that our financial reserving methodology assure there are adequate reserve funds to reimburse health plan contractors for extraordinary medical losses and to maintain financial long term financial stability. The audit provided an outside validation of HCG effective financial management and statutory compliance.

Although there were no specific recommendations to respond to, the audit findings will serve as a basis to improve processes and procedures going forward. There are areas we agreed to continue to strengthen and improve such as operational and financial performance metrics, bare period insurance validation beyond just an attestation, and financial oversight of contracted health plan operations and financial stability. HCG financial management will continue to closely monitor the adequacy of the health plan financial reserves. I also plan to have an outside actuary peer review our methodology as soon as our HCG administrative budget will permit. As a self funded health care coverage program, it is important to validate our reserving methodology and management of medical cost risk meets appropriate health insurance actuarial practice.

As your audit documents, Healthcare Group now offers more than 15 different health benefit options including Health Saving Account plans, contracts for dental, vision and four health plan networks, and has expanded to offer statewide health plan coverage. In a recent satisfaction survey, HCG received strong satisfaction results from members, especially regarding the new benefit options and expanded networks. Healthcare Group has grown more than 50% over the last 12 months. Managing the business and operational processes for the current level of membership growth has required HCG to update telecommunication equipment, reengineer systems and improve operational processes. Over the next 18 months HCG expects to grow to over 50,000 members, doubling the number of small businesses and public employers participating in the program.

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As membership has grown, the percent of premium dollars allocated for HCG administration and operations has been reduced. To properly manage this enterprise and provide the level of ongoing membership support small businesses need, HCG must be appropriated adequate funds from the premium revenues collected for its general administration and customer care operations. As the audit points out, there are high expectations placed on the effective financial management and statutory compliance of HCG and the continued self-sufficiency of the program. Your findings state the HCG administrative cost was 8.5% of total program cost between July 2003 and September 2005; however, by next fiscal year that percent will drop to 6.8%.

The key to financial sufficiency and keeping HCG premiums affordable is continued membership growth and attracting not only the “*forty-somethings*” but also the “*twenty-somethings*” to our health plan benefits. Marketing and sales expenditures for HCG are well below expenditures of commercial health plans. Interest in HCG by small businesses remains high. For HCG to be able to meet with businesses to explain all the benefits, premium rate, verify employer eligibility and process all the enrollments requires an increasing amount of resources and close oversight.

Finally, I would like to take this opportunity to remind those who have an interest in this audit and the success of Healthcare Group of Arizona, that a high percentage of small businesses in Arizona remain uninsured. The number one reason according to the Kaiser Foundation for small business failure or declared bankruptcy is because of a major illness suffered by the small business owner. Additionally, small businesses must now compete with large employers for the same pool of employees. Large employers often have the competitive advantage for Arizona’s labor market because they can offer health benefits. Nearly every state and local chamber of commerce action agenda includes advocacy for affordable healthcare coverage for small business. With the support and leadership of the Governor and the state legislature, HCG will be part of the solution for affordable health care for Arizona small businesses.

Thank you for this opportunity to comment on the Healthcare Group of Arizona audit findings.

Sincerely

Anthony D. Rodgers  
Director