

**Report 08-12  
October 2008**

An Audit

# **Health Insurance Risk-Sharing Plan Authority**

*For Calendar Year 2007*

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State Auditor – Janice Mueller

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**STATE OF WISCONSIN**  
Legislative Audit Bureau

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Janice Mueller  
State Auditor

October 29, 2008

Senator Jim Sullivan and  
Representative Suzanne Jeskewitz, Co-chairpersons  
Joint Legislative Audit Committee  
State Capitol  
Madison, Wisconsin 53702

Dear Senator Sullivan and Representative Jeskewitz:

As required under s. 13.94(1)(dh), Wis. Stats., we have completed a financial and compliance audit of the Wisconsin Health Insurance Risk-Sharing Plan (HIRSP) Authority for calendar year 2007. The audit also satisfies the HIRSP Authority's audit requirements under the federal Single Audit Act of 1984, as amended, and U.S. Office of Management and Budget Circular A-133. We have also issued a separate audit report (08-11) on our audit of the HIRSP Authority for the six-month period ended December 31, 2006, which was a transition period as the financial reporting period changed from a fiscal year basis to a calendar year basis.

The HIRSP Authority provides medical and prescription drug insurance for individuals who are unable to obtain coverage in the private market or who have lost employer-sponsored group health insurance. 2005 Wisconsin Act 74 made significant changes to the operations of HIRSP. Among the most significant was the creation of the HIRSP Authority, which assumed oversight responsibility from the Wisconsin Department of Health and Family Services (currently the Department of Health Services) on July 1, 2006.

We have provided an unqualified audit opinion on the HIRSP Authority's 2007 financial statements. Our report also contains the auditor's reports on internal control over financial reporting and on compliance with program requirements, and our unqualified audit opinion on the HIRSP Authority's Schedule of Expenditures of Federal Awards. Overall, we did not identify any significant concerns, although we include a recommendation for the HIRSP Authority to work with the federal government to resolve a federal cash management issue.

The HIRSP Authority has maintained a sound financial position, with a net increase in assets of \$6.8 million during 2007. Following years of significant increases during the early 2000s, policyholder enrollment has decreased in recent years. As of December 31, 2007, 17,126 policyholders were enrolled in one of the HIRSP Authority's plans.

We appreciate the courtesy and cooperation extended to us by the HIRSP Authority and the plan administrator.

Respectfully submitted,

A handwritten signature in cursive script that reads "Janice Mueller".

Janice Mueller  
State Auditor

JM/DA/ss



## Introduction ■

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The Wisconsin Health Insurance Risk-Sharing Plan (HIRSP) Authority provides medical and prescription drug insurance for individuals who cannot obtain coverage in the commercial health insurance market because of the severity of their health conditions. In the late 1990s, HIRSP was also designated as Wisconsin's plan to meet federal Health Insurance Portability and Accountability Act (HIPAA) regulations and to provide health insurance to people who lose employer-sponsored group health insurance and meet other specified criteria.

The HIRSP Authority, which was created under 2005 Wisconsin Act 74 as a public body corporate and politic, assumed responsibility for HIRSP on July 1, 2006. HIRSP was originally administered by the Office of the Commissioner of Insurance when it was established in 1980, and subsequently administered by the Department of Health and Family Services (currently the Department of Health Services) from 1998 through June 30, 2006. The HIRSP Authority is governed by its Board of Directors, consisting of 13 voting members that include representatives of insurers, health care providers, and small businesses; HIRSP policyholders; and a professional consumer advocate. The Commissioner of Insurance or a designee also serves as a nonvoting board member. The HIRSP Authority, which employs four staff members, contracts with Wisconsin Physicians Service Insurance Corporation (WPS) to function as the plan administrator.

At the request of the HIRSP Authority and as required under s. 13.94 (1)(dh), Wis. Stats., we have completed a financial and

compliance audit for calendar year 2007. We reviewed the HIRSP Authority's control procedures, assessed the fair presentation of the 2007 financial statements, and reviewed compliance with statutory provisions. The HIRSP Authority changed its financial reporting period from a fiscal year to a calendar year basis beginning with 2007. We have issued a separate report on our audit of the interim period of July 1, 2006, through December 31, 2006.

## Plan Provisions

Various eligibility requirements must be met to participate in HIRSP. All applicants must be Wisconsin residents who are not eligible for employer-sponsored group health insurance, Medicaid, or BadgerCare. Applicants then must meet specified criteria based on their medical condition or loss of employer-sponsored group health insurance.

Effective January 1, 2007, the HIRSP Authority is allowed to establish the plan design, which previously had been defined largely in Wisconsin Statutes. Certain services specified by statutes must still be covered, but the HIRSP Authority may change benefit levels, deductibles, copayment and coinsurance requirements, exclusions, and limitations that it determines generally reflect and are commensurate with comprehensive health insurance coverage offered in the private individual market in Wisconsin.

***HIRSP currently offers eligible applicants five plans.***

The HIRSP Authority currently offers eligible applicants five plans. One of the plans is a Medicare supplement plan for participants under the age of 65 who participate in the Medicare program because of a disability. The other four plans are for policyholders who are not eligible for Medicare. The four plans offer identical coverage and differ primarily in the amounts of premiums and deductibles.

- HIRSP 1,000 offers the lowest deductible with the highest premium levels.
- HIRSP 2,500 offers a moderate deductible with moderate premium levels.
- HIRSP 5,000 offers the highest deductible with the lowest premium levels.
- HIRSP HSA qualifies policyholders to open a health savings account to pay for health-related expenses and to save for future medical expenses on a tax-free basis.

The HIRSP 1,000, HIRSP 2,500, and HIRSP Medicare supplement plan were referred to as Plans 1A, 1B, and 2, respectively, until 2008. HIRSP 5,000 and HIRSP HSA are newly created plans first offered at the beginning of 2008.

Policyholders who have annual household incomes below \$25,000 may be eligible for premium, medical deductible, and drug coinsurance subsidies. In 2007, 16.0 percent of HIRSP policyholders received subsidies from the program at a cost of \$5.8 million.

## Funding

***Program costs are shared by policyholders, health insurance companies, and health care providers.***

Program costs are funded primarily through policyholder premiums, financial assessments on health insurance companies that do business in Wisconsin, and reduced reimbursements to health care providers. None of the funding is from general purpose revenue tax dollars. The HIRSP Authority also earns interest income and periodically receives federal grants from the federal Centers for Medicare and Medicaid Services, which are available to qualified high-risk state health insurance pools that meet certain criteria. Statutes require that these federal grants be used to help fund subsidy costs.

Statutes require that policyholder premiums fund 60 percent of estimated operating and administrative costs. The remaining 40 percent of program costs are to be funded equally by the insurers and health care providers, who also are equally responsible for the premium, deductible, and drug coinsurance subsidies not funded by federal grants. Insurers fund their share of annual operating and administrative costs through annual assessments that are proportionately based on their annual revenue from health insurance premiums. Health care providers contribute through reduced reimbursements for billed services.

## Enrollment

***HIRSP enrollment totaled 17,126 policyholders on December 31, 2007.***

Enrollment in HIRSP plans increased significantly during the early 2000s but moderated and then decreased in recent years. As shown in Table 1, 17,126 policyholders were enrolled as of December 31, 2007. Enrollment declined 4.6 percent during 2006 and 5.2 percent during 2007. The decrease in enrollment is continuing in 2008, and total enrollment was 16,344 as of August 31, 2008.

Table 1

**HIRSP Enrollment**

Date	Total Policyholders	Percentage Change
December 31, 1998	7,248	–
December 31, 1999	7,904	9.0%
December 31, 2000	10,042	27.0
December 31, 2001	12,606	25.5
December 31, 2002	15,882	26.0
December 31, 2003	17,447	9.9
December 31, 2004	18,341	5.1
December 31, 2005	18,947	3.3
December 31, 2006	18,073	(4.6)
December 31, 2007	17,126	(5.2)

At least part of the decrease in enrollment is associated with a decrease of 635 policyholders in the Medicare supplement plan (Plan 2) during 2006 and 2007. The 40.4 percent decrease in this plan over the two-year period was largely attributed to the availability of the federal Medicare Part D program in January 2006, and the requirement that Medicare supplement plan policyholders, many of whom enrolled primarily for prescription drug coverage, must also enroll in the Medicare Part D program beginning May 15, 2006. The highest-premium plan, HIRSP 1,000 (Plan 1A), also experienced a decrease of 934 during 2007, which the HIRSP Authority suggests was attributable to premium levels for that plan.

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# Audit Opinion ■

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## *Independent Auditor's Report on the Financial Statements of the Wisconsin Health Insurance Risk-Sharing Plan Authority*

We have audited the accompanying financial statements of the Wisconsin Health Insurance Risk-Sharing Plan (HIRSP) Authority as of and for the year ended December 31, 2007, as listed in the table of contents. These financial statements are the responsibility of HIRSP Authority management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the HIRSP Authority as of December 31, 2007, and the changes in its financial position and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The required supplementary information included as Management's Discussion and Analysis on pages 9 through 14 is not a required part of the financial statements of the HIRSP Authority, but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

The accompanying Schedule of Expenditures of Federal Awards on page 39 is presented for purposes of additional analysis as required by Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the financial statements. The information in the schedule has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 14, 2008, on our consideration of the HIRSP Authority's internal control over financial reporting; our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements; and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

October 14, 2008

LEGISLATIVE AUDIT BUREAU  
by   
Diann Allsen  
Audit Director

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# Management's Discussion and Analysis ■

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## *Prepared by the Health Insurance Risk-Sharing Plan Authority*

The Health Insurance Risk-Sharing Plan (HIRSP) Authority is a Wisconsin state government public body corporate and politic. The HIRSP Authority was established effective July 1, 2006, by Chapter 149, Wis. Stats., to administer the insurance risk-sharing pool known as HIRSP, which provides individual health insurance policies to Wisconsin residents who are unable to obtain coverage from commercial insurers due to high costs or adverse health circumstances, and to persons who are entitled to continuation of coverage under federal law, including the Health Insurance Portability and Accountability Act (HIPAA) under Title XXII, P.L. 104-191.

This section provides management's discussion and analysis (MD&A) of HIRSP Authority financial statements for the calendar year ended December 31, 2007, and for comparative purposes the calendar year ended December 31, 2006. The financial statements are prepared in conformity with generally accepted accounting principles for governments as prescribed by the Governmental Accounting Standards Board. The financial statements report upon the financial position, changes in financial position, and cash flows of the HIRSP Authority and include accompanying notes. The financial statements, notes to the financial statements, and MD&A are the responsibility of management.

The time period reported upon by the MD&A includes calendar years 2007 and 2006. The two-year period was one of transition and significant change in the plan. Responsibility for plan administration was transferred from the Wisconsin Department of Health and Family Services (currently the Department of Health Services) to the HIRSP Authority effective July 1, 2006. Through June 30, 2007,

HIRSP Authority operations, budgeting, and assessments were conducted on a state fiscal year basis. The first half of 2006 was the final six months of fiscal year (FY) 2005-06, and the period from July 1, 2006, through June 30, 2007, was FY 2006-07. A calendar year convention was used for financial reporting for calendar year 2007. Effective January 1, 2008, a calendar year convention was implemented for budgeting and assessments, premium rates, and eligibility for low-income subsidies.

During the last half of calendar year 2007, a six-month interim operating budget was established through December 31, 2007, to transition from the state fiscal year ended June 30, 2007, to the 2008 calendar year. Assessments were levied and collected in the second half of 2007 to cover budgeted projections of program funding required for the six-month period. During the interim budget period, policyholder premium rates were unchanged from the rates that were applicable in FY 2006-07. Management planning for the interim budget included the objective to sustain operating losses and thereby use a portion of accumulated net assets to partially fund plan costs during the interim period. As a result, the HIRSP Authority incurred net losses during each month in the second half of 2007.

## Financial Position

While the HIRSP Authority incurred losses during the last six months of 2007, the overall financial position of the HIRSP Authority improved during both 2007 and 2006. As shown in Table A, total assets declined in 2007, but total liabilities declined even more. As a result, total net assets increased \$6.8 million, or 23.9 percent, in 2007 and equaled \$35.1 million as of December 31, 2007. In 2006, total net assets increased \$15.3 million, or 118.1 percent, from \$13.0 million as of December 31, 2005, to \$28.3 million as of December 31, 2006.

Table A

### Condensed Financial Information as of December 31, 2007 and 2006

	December 31, 2007	December 31, 2006	Percentage Change
Total Assets	\$68,133,050	\$79,429,816	(14.2)%
Total Liabilities	33,033,856	51,098,808	(35.4)
<b>Total Net Assets</b>	<b>\$35,099,194</b>	<b>\$28,331,008</b>	23.9

## Assets

Total assets decreased by \$11.3 million, or 14.2 percent, in 2007 to \$68.1 million as of December 31, 2007. Cash assets increased by \$8.5 million, or 14.9 percent, in 2007 and equaled \$65.4 million as of December 31, 2007. The increase in cash was offset by a \$17.7 million decrease in assessment receivable assets in 2007. Year-end 2007 assessment receivable assets equaled \$0 because the HIRSP Authority operated under a six-month interim budget for the second half of 2007, and all assessments for the second half of 2007 had been received as of December 31, 2007. In contrast, assessment receivables as of December 31, 2006, were \$17.7 million, as one-half of FY 2006-07 assessment revenues had been uncollected as of December 31, 2006, and were due during the first half of 2007.

As of December 31, 2007, the Balance Sheet reflected a federal grant receivable asset of \$0, compared to a federal grant receivable asset of \$2.3 million as of year-end 2006. In September 2006, the Centers for Medicare and Medicaid Services awarded federal grants to the HIRSP Authority totaling \$4.4 million. The federal grant funds were recognized as revenue as they were used to offset policyholder premium subsidies from July 1, 2006, through June 30, 2007. As of December 31, 2006, \$2.3 million of the grant had been earned but was recorded as a receivable because the funds were not received until January 2007. The remaining \$2.1 million was recognized as revenue during 2007. All grant funds had been received as of December 31, 2007.

## Liabilities

Total liabilities decreased \$18.1 million, or 35.4 percent, in 2007 to \$33.0 million as of December 31, 2007, compared to total liabilities of \$51.1 million as of December 31, 2006. Unpaid medical loss liabilities increased 6.1 percent, to \$15.6 million, in 2007 and unpaid pharmacy loss liabilities increased 5.9 percent, to \$841,000 as of December 31, 2007. The primary source for the overall decrease in liabilities in 2007 was the decrease to \$0 in the liability for unearned assessments. Assessments levied for the operating budget for the second half of 2007 were fully earned at the end of 2007, and there was no unearned assessment liability. As of December 31, 2006, the unearned assessment liability was \$19.2 million because one-half of FY 2006-07 assessment revenue was unearned as of December 31, 2006.

## Change in Financial Position

As shown in Table B, the \$6.8 million increase in net assets in 2007 comprised total operating income of \$1.5 million, plus nonoperating income of \$5.3 million. The 2007 increase in net assets was 55.9 percent less than the \$15.3 million increase in net assets in 2006. Decreased net income in 2007 resulted from decreased operating revenues and increased net incurred losses during the second half of the year. As noted, decreased net income was an objective of management's six-month interim operating budget from July 1, 2007, through December 31, 2007.

Table B

**Condensed Financial Information**  
for 2007 and 2006

	2007	2006	Percentage Change
Total Operating Revenues	\$134,405,542	\$145,229,753	(7.5)%
Total Operating Expenses	132,955,160	134,813,302	(1.4)
Operating Income	1,450,382	10,416,451	(86.1)
Total Nonoperating Income	5,317,804	4,926,693	7.9
<b>Change in Net Assets</b>	<b>\$ 6,768,186</b>	<b>\$ 15,343,144</b>	<b>(55.9)</b>

### Operating Revenues

Total operating revenues in 2007 were \$134.4 million, a decrease of \$10.8 million, or 7.5 percent, compared to 2006 operating revenues. During the last half of calendar year 2007, a six-month operating budget was established to transition from the state fiscal year ended June 30, 2007, to the 2008 calendar year. Assessments were levied in the second half of 2007 to cover budgeted projections of program funding required during the six-month period. During the interim period, policyholder premium rates were unchanged from the rates applicable in FY 2006-07.

The budget for the second half of 2007 had the objective of realizing decreased operating revenues relative to plan costs, so as to incur operating losses and thereby apply a portion of accumulated net assets to fund HIRSP Authority operations. The budget maintained the overall HIRSP statutory funding formula. However, by not increasing policyholder premium rates from the prior fiscal year budget, premium income was maintained as relatively budget neutral, whereas medical claims increased due to rising costs for medical services. During the first half of 2007, total operating revenues were \$70.4 million, total operating expenses were \$60.4 million, and the net increase in assets was \$13.7 million. During the second half of 2007, total operating revenues were \$64.0 million, total operating expenses were \$72.5 million, and the net decrease in assets was \$6.9 million, resulting in a net increase in assets of \$6.8 million for calendar year 2007.

## Operating Expenses

The total incurred medical loss expense in 2007 was \$89.2 million, an increase of \$2.4 million, or 2.8 percent, from the 2006 total incurred medical loss expense of \$86.8 million. The gross medical loss expense decreased by \$864,000 in 2007. Provider contributions, which offset the gross medical loss expense, increased in 2007 by \$5.5 million.

The total pharmacy loss expense in 2007 was \$37.3 million, a decrease of \$3.9 million, or 9.5 percent, from the 2006 pharmacy loss expense of \$41.2 million. The 2007 decrease was primarily due to decreased enrollment in Plan 2 (currently known as the Medicare supplement plan) and enrollment of HIRSP members in the federal Medicare Part D drug benefit program, which shifted former HIRSP drug claim costs to Medicare. The decreased pharmacy expense in 2007 was also due to increased use of generic drugs and decreased use of branded drugs, as the proportion of generic drugs to total dispensed drugs increased from 57.3 percent in 2006 to 62.0 percent in 2007. Drug rebates obtained in 2007 were \$4.8 million, compared to \$3.5 million in 2006.

## Nonoperating Income

Nonoperating income in 2007 was \$5.3 million, an increase of \$391,000 from 2006. Federal grant revenues decreased \$244,000 in 2007, and investment income increased \$635,000 in 2007 due to increased cash assets and increased market interest yield on cash deposits in 2007.

## Plan Enrollment

Plan enrollment as of December 31, 2007, was 17,126, a decrease of 947 policyholders, or 5.2 percent, compared to enrollment of 18,073 in December 2006. In 2006, enrollment decreased by 874 policyholders, or 4.6 percent, from December 2005, when it was 18,947 policyholders. HIRSP enrollment peaked in June 2005 with 19,256 policyholders. As of December 31, 2007, enrollment had declined 11.1 percent from the June 2005 peak, or by 2,130 policyholders.

## Per Member per Month Plan Costs

Per member per month (PMPM) gross claim costs in 2007 were \$800, an increase of 8.0 percent from PMPM gross claim costs in 2006. The PMPM data shown in Table C reflect the decreased membership trend that continued in calendar year 2007, combined with price inflation in the health care market and increased utilization of HIRSP health care services during 2007. Claim costs incurred during 2007 equaled 96.3 percent of total plan costs in 2007. Claim costs incurred in 2006 equaled 96.1 percent of the total plan costs in 2006.

Table C

**Plan Cost Summary on a per Member per Month (PMPM) Basis  
2007 and 2006**

Description	2007	2006	2007 PMPM	2006 PMPM
Member Months (Sum of Total Members Enrolled in Each Month)	210,985	222,541		
Gross Claims (Costs before Provider Contributions are Deducted)	\$168,788,865	\$164,805,399	\$800.00	\$740.56
Administrative Expenses	\$6,407,505	\$6,615,812	\$30.37	\$29.73

Administrative expenses incurred in 2007 equaled 3.7 percent of total plan costs during the 12-month period. Administrative expenses incurred in 2006 equaled 3.9 percent of total plan costs during 2006.

### **HIRSP Authority Contact Information**

General information regarding the risk-sharing plan may be obtained from the HIRSP Authority's Web site at <http://www.hirsp.org>.

Questions concerning any of the information provided in the HIRSP Authority's financial reports, or requests for additional information, should be directed to the HIRSP Authority at the following address:

HIRSP Authority  
33 East Main Street, Suite 230  
Madison, WI 53703  
Phone: (608) 441-5777  
Fax: (608) 441-5776

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## **Financial Statements ■**

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**Balance Sheet**  
**December 31, 2007**

	<u>December 31, 2007</u>
<b>ASSETS</b>	
Cash and Cash Equivalents (Note 2)	\$ 65,405,499
Drug Rebates Receivable (Note 3)	2,012,513
Premiums Receivable (Note 3)	257,062
Claims Recoverable (Note 3)	169,814
Assessments Receivable	0
Prepaid Items	18,092
Federal Grants Receivable	0
Other Assets	<u>270,070</u>
<b>TOTAL ASSETS</b>	<b><u>\$ 68,133,050</u></b>
<b>LIABILITIES AND NET ASSETS</b>	
Liabilities:	
Unpaid medical loss liabilities (Note 6)	\$ 15,627,420
Unpaid pharmacy loss liabilities (Note 6)	841,155
Unpaid loss adjustment expenses (Note 6)	770,000
Unearned premiums (Note 1E)	13,673,031
Unearned assessments	0
Payments to providers (Note 3)	1,492,659
Accrued administrative expenses	<u>629,591</u>
<b>Total Liabilities</b>	<b>33,033,856</b>
<b>Total Net Assets</b>	<b><u>35,099,194</u></b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b><u>\$ 68,133,050</u></b>

The accompanying notes are an integral part of this statement.

## Statement of Revenues, Expenses, and Changes in Net Assets for the Year Ended December 31, 2007

	For the Year Ended December 31, 2007
<b>OPERATING REVENUES</b>	
Premiums (Note 1E)	\$ 100,822,871
Insurers' Assessments (Note 1E)	33,582,671
<b>Total Operating Revenues</b>	<b>134,405,542</b>
<b>OPERATING EXPENSES</b>	
Losses:	
Gross medical losses	130,017,451
Provider contributions (Note 9)	(42,296,580)
Increase (Decrease) in unpaid medical losses (Note 6)	1,481,144
Total medical losses	89,202,015
Gross pharmacy losses	37,243,581
Increase (Decrease) in unpaid pharmacy losses (Note 6)	46,689
Total pharmacy losses	37,290,270
<b>Total Losses</b>	<b>126,492,285</b>
General and Administrative Expenses (Note 4)	6,407,505
Referral Fees (Note 1E)	55,370
<b>Total Operating Expenses</b>	<b>132,955,160</b>
<b>OPERATING INCOME</b>	<b>1,450,382</b>
<b>NONOPERATING REVENUES AND EXPENSES</b>	
Federal Grant Revenue (Note 10)	2,089,225
Investment Income	3,228,579
<b>Total Nonoperating Income</b>	<b>5,317,804</b>
<b>CHANGE IN NET ASSETS</b>	<b>6,768,186</b>
<b>NET ASSETS</b>	
Total Net Assets—Beginning of the Year	28,331,008
<b>Total Net Assets—End of the Year</b>	<b>\$ 35,099,194</b>

The accompanying notes are an integral part of this statement.

**Statement of Cash Flows  
for the Year Ended December 31, 2007**

For the Year Ended  
December 31, 2007

**CASH FLOWS FROM OPERATING ACTIVITIES**

Cash Received for Premiums	\$ 101,152,825
Cash Received for Assessments	32,068,001
Cash Received for Federal Grant	4,422,935
Cash Payments for Medical Losses	(88,164,531)
Cash Payments for Pharmacy Losses	(37,748,140)
Cash Payments for Other Expenses	(6,489,265)
<b>Net Cash Provided by Operating Activities</b>	<b>5,241,825</b>

**CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES**

Purchases of Capital Assets	(19,304)
<b>Net Cash Used for Capital and Related Financing Activities</b>	<b>(19,304)</b>

**CASH FLOWS FROM INVESTING ACTIVITIES**

Investment Income	3,238,798
<b>Net Cash Provided by Investing Activities</b>	<b>3,238,798</b>
<b>NET INCREASE IN CASH AND CASH EQUIVALENTS</b>	<b>8,461,319</b>
Cash and Cash Equivalents, Beginning of Year	56,944,180
Cash and Cash Equivalents, End of Year	<u>\$ 65,405,499</u>

**RECONCILIATION OF NET OPERATING INCOME  
TO NET CASH PROVIDED BY OPERATING ACTIVITIES**

Net Operating Income	\$ 1,450,382
Adjustments to Reconcile Net Operating Income to Net Cash Provided by Operating Activities:	
Depreciation expense	5,310
Federal grant revenue reported as nonoperating revenue	2,089,225
Changes in assets and liabilities:	
Decrease (Increase) in receivables	19,757,100
Decrease (Increase) in prepaids	4,759
Increase (Decrease) in accounts payable	(19,209,263)
Increase (Decrease) in unearned premiums	231,617
Increase (Decrease) in medical loss liabilities	909,744
Increase (Decrease) in pharmacy loss liabilities	2,951
Total Adjustments	3,791,443
<b>Net Cash Provided by Operating Activities</b>	<b>\$ 5,241,825</b>

The accompanying notes are an integral part of this statement.

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# Notes to the Financial Statements ■

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## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### A. Description of the HIRSP Authority

The Health Insurance Risk-Sharing Plan (HIRSP) Authority is a Wisconsin state government public body corporate and politic. The HIRSP Authority was established by Chapter 149, Wis. Stats., for the purpose of maintaining and administering the insurance risk-sharing pool that provides individual health care insurance policies to Wisconsin residents who are high risk for adverse health care costs and who cannot obtain health insurance in the commercial individual health insurance market. HIRSP also provides health care policies to persons who are entitled to continuation of coverages under federal law, including the Health Insurance Portability and Accountability Act (HIPAA) under Title XXII, P.L. 104-191.

HIRSP was originally established in 1980 as a Wisconsin state government fund, administered by the Wisconsin Office of the Commissioner of Insurance. From 1998 through June 30, 2006, it was administered by the Wisconsin Department of Health and Family Services (DHFS), which is currently the Department of Health Services. The HIRSP Authority was created by 2005 Wisconsin Act 74 and assumed responsibility for administration of HIRSP effective July 1, 2006.

The HIRSP Authority qualifies as exempt from federal income taxation pursuant to Internal Revenue Code Section 501(c)(26). An application for recognition of the HIRSP Authority's status as a tax-exempt public corporation is currently pending before the Internal Revenue Service.

The HIRSP Authority derives all funding for its plan costs and policyholder subsidy costs through a funding formula prescribed by s. 149.143, Wis. Stats. Insurance policy premiums paid by policyholders fund 60.0 percent of plan costs. Assessments levied on insurance companies that write health insurance coverages in Wisconsin and discounts on payments to health care providers for health care services rendered to HIRSP policyholders each fund 20.0 percent of plan costs.

HIRSP policyholders who have annual incomes of \$25,000 or less are eligible for subsidized assistance for premium payments, health care deductible payments, and drug copayments. Premium subsidies are first funded by any available federal grant funds. The remaining premium subsidy costs, plus the deductible and drug copayment subsidy costs, are paid on an equal-share basis by the assessed insurance companies and the participating health care providers.

**B. Accounting Practices**

The financial statements of the HIRSP Authority have been prepared in conformity with generally accepted accounting principles (GAAP) for governments as prescribed by the Governmental Accounting Standards Board (GASB) for determining and reporting the financial position, changes in financial position, and cash flows of a governmental enterprise. The HIRSP Authority has not applied Financial Accounting Standards Board pronouncements issued after November 30, 1989. The financial statements are presented using the economic resources measurement focus and the accrual basis of accounting. Under accrual accounting, revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows.

**C. Financial Statement Reporting Periods**

The financial statements report on the financial condition and activities of the HIRSP Authority for the calendar year ended December 31, 2007.

The HIRSP Authority's Board of Directors adopted a calendar year convention for the HIRSP Authority's annual operating budget commencing with calendar year 2008. HIRSP Authority budgeting and financial reporting were previously conducted on a state fiscal year basis. The most recent audited financial statements reported on FY 2005-06, which ended June 30, 2006, and FY 2004-05, which ended June 30, 2005. To establish comparable audited financial statements on a calendar year basis going forward, financial statements have been issued that report on the calendar year ended December 31, 2007, and separate financial statements have been issued concurrently that report on the six-month period ended December 31, 2006.

**D. Use of Estimates in Preparation of the Financial Statements**

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires disclosure of contingent assets and liabilities as of the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from management's estimates. Estimates that are particularly susceptible to significant change are the unpaid loss liabilities as described in Note 1E and Note 6, and the health care provider contributions as described in Note 9.

**E. Accounting Policy****a) Operating Revenues and Operating Expenses**

HIRSP Authority operating revenues and operating expenses arise from transactions that are directly related to ongoing indemnity health care insurance and services activities. Nonoperating revenues, including investment income and federal grant funds, are not directly related to ongoing indemnity health care insurance and services. On the financial statements, both policyholder premiums, net of allowed policyholder premium subsidies, and insurer assessments are reported as elements of total operating revenues. Provider funding contributions, which are derived from discounted payments for provider services, are reported as a deduction from gross medical losses and therefore as a reduction of total operating expenses.

**b) Cash and Cash Equivalents**

Effective July 2006, cash and cash equivalents consist solely of demand deposits maintained by the HIRSP Authority at a commercial bank. Refer to Note 2 for further information regarding cash deposits.

**c) Premium Income Recognition**

Premiums are recognized as earned in the period in which policyholders are entitled to receive services and are reported in the financial statements net of allowed premium subsidies. Premium rates required for a calendar year period are determined during the annual budget planning process. A liability for unearned premiums is established to properly recognize the liability for premiums that have been written but will be earned in subsequent accounting periods.

**d) Assessment Revenue Recognition**

An assessment to provide a funding contribution for HIRSP Authority program costs is levied on commercial insurance companies that issue health insurance coverages in Wisconsin. The commercial insurers have a statutory requirement to fund

20.0 percent of HIRSP Authority plan costs, plus one-half of the premium, deductible, and copayment subsidies granted to eligible low-income policyholders and not otherwise funded by federal grants.

Insurers that have written health insurance premiums in one calendar year are legally obligated to participate in the HIRSP Authority assessment that will be issued in the subsequent calendar year. The total assessment required for a calendar year period is determined during the annual budget planning process. As provided by s. 149.13, Wis. Stats., each insurer that participates in the assessment pays a proportionate share of the total assessment corresponding to that insurer's proportionate share of the aggregate premiums charged for health insurance coverages issued in Wisconsin in the prior calendar year.

Assessment receipts are recognized as earned revenue during the budget period for which the assessments are levied as a funding contribution. A liability for unearned assessments is established to properly recognize the liability for assessment assets that will be earned subsequent to the close of the current accounting period.

e) Policyholder, Insurer, and Health Care Provider Contribution

The HIRSP Authority uses fund accounting methodology to provide for equitable accounting of contributed funds and to ensure that HIRSP program funding operates in conformity with the funding model mandated by s. 149.143, Wis. Stats. An annual operating budget based on actuarial analysis of projected revenues and program costs determines contribution amounts required from policyholders, assessed insurers, and participating health care providers. Inception-to-date funding contributions, plan cost participation, and surplus or deficit net asset positions of each of the three funding constituencies are maintained in three separate, closed fund accounts.

Contributions and surplus net assets provided by any one constituency group are restricted to that constituency's account and are not available to offset the program cost obligations or deficit net asset position of the other two funding constituencies. The surplus or deficit net asset interest of each funding constituency is carried forward from one accounting period to the next and is applied solely to the ongoing contribution requirements of the respective funding constituency.

## f) Liabilities for Unpaid Losses

Liabilities for unpaid losses consist of health care claims incurred and reported but not paid prior to the close of the accounting period, plus estimates of claims incurred during the accounting period but not reported as of the financial statement date. Unpaid loss liabilities are reported net of estimated health care provider discounts. Liabilities for unpaid losses are estimated using actuarial methods and assumptions based on claim payment patterns, medical cost inflation, historical developments such as claim inventory levels and claim reporting patterns, and other relevant factors. Corresponding administrative costs to process outstanding claims are estimated and accrued as unpaid loss adjustment expense liabilities. Estimates of future payments related to claims incurred in the current and in prior accounting periods are continually reviewed by management and adjusted as necessary, with resulting adjustments to the liabilities reflected in current operations.

## g) Policy Acquisition Costs

The HIRSP Authority does not engage in marketing activities and does not incur sales commissions. Insurance agents who assist individuals with the HIRSP application process are paid a one-time referral fee in the amount of \$35 for each policy issued. The referral fees, which represent the sole policy acquisition cost of the HIRSP Authority, are miscellaneous expenses, are minimal, and are recorded as incurred.

**2. CASH DEPOSITS**

The HIRSP Authority maintains three bank accounts under a bank services contract at a commercial bank. These accounts include one depository account and two zero-balance bank accounts. The zero-balance accounts are used to remit policy-related disbursements and administrative expense disbursements. Disbursements issued on the zero-balance bank accounts are funded as necessary from the depository account, which serves as a concentration account for cash receipts and cash assets.

Under the bank services contract, the HIRSP Authority's average collected deposits balance is paid interest at an agreed-upon HIRSP interest rate. The collected balance in the HIRSP cash management account pool at the bank is collateralized with federal agency securities having market value in excess of the HIRSP Authority's cash deposit balance. The securities are pledged as collateral for the benefit of the HIRSP Authority and are held in a restricted securities account under the control of a federal reserve bank. The HIRSP Authority holds a perfected security interest in the pledged securities.

### 3. RECEIVABLES AND PAYABLES

Unless otherwise noted, receivable balances are expected to be collected within the following 12-month period. Management expects that all reported drug rebates will be received; however, it can sometimes take more than one year for final settlement of drug rebate balances to occur.

The financial statements report a liability balance labeled "Payments to providers." The reported liability is for pharmacy claims that were adjudicated and paid by the third-party pharmacy benefit manager in the final two weeks of the reporting period. As of the close of the reporting period, the pharmacy benefit manager was in the process of billing the HIRSP Authority for reimbursement of the paid claims, and HIRSP Authority payment had not yet been remitted.

### 4. GENERAL AND ADMINISTRATIVE EXPENSES

HIRSP Authority indemnity insurance operations are performed by a third-party plan administrator under an administrative services agreement with Wisconsin Physicians Service Insurance Corporation (WPS). WPS administration of HIRSP operations commenced April 1, 2005. The administrative services agreement provided for an initial termination date of April 1, 2008, with three one-year renewals possible. Effective December 17, 2007, the agreement was extended through March 31, 2009.

Services currently provided under the administrative services agreement include policyholder and provider services, claims and systems administration, medical management, data collection and reporting, subrogation, coordination of benefits, disaster recovery, pharmacy benefit management, and actuarial services. WPS maintains service contracts with third-party contractors, whereby HIRSP Authority pharmacy benefit management services are currently performed by Navitus Health Solutions, and HIRSP Authority actuarial services are currently performed by Milliman Consultants and Actuaries.

General and administrative expenses for the 12-month period ended December 31, 2007, include the following:

Plan Administrator Fees	\$5,736,081
State Administrative Costs (DHFS)	21,959
Authority Administrative Costs	570,368
Transition Costs	29,219
Other Expense	<u>49,878</u>
Total	\$6,407,505

**5. LEASES**

**A. Operating Leases**

The HIRSP Authority has entered into a lease for administrative office space for a lease term of five years and ten months. The lease was executed in July 2006, but the leased premises were not completed and available for occupancy until February 2007. The lease term commenced on March 1, 2007, and will terminate December 31, 2012. Office lease rental payments charged to expenses for the 12-month period ended December 31, 2007, were \$44,041.

The HIRSP Authority has entered into an equipment operating lease for office copier equipment. The lease has a term of 60 months and commenced November 15, 2006. Equipment lease rental payments charged to expenses for the 12-month period ended December 31, 2007, were \$2,916.

**B. Noncancelable Lease Terms**

As of January 1, 2008, the minimum aggregate rental commitments are as follows:

<u>Year</u>	<u>Commitment</u>
2008	\$50,834
2009	53,159
2010	55,168
2011	56,773
2012	56,516

The HIRSP Authority is not party to any sales-leaseback transactions.

**6. LIABILITY FOR UNPAID LOSSES AND LOSS ADJUSTMENT EXPENSES**

The following is a reconciliation of changes in the combined medical and pharmacy unpaid loss liabilities and unpaid loss adjustment expense liabilities for the 12-month period ended December 31, 2007:

Balance—Beginning of the Year	<u>\$16,289,654</u>
Incurred Claims:	
Provision for insured events of the current fiscal year	133,041,670
Changes in provision for insured events of prior fiscal years	<u>(1,722,105)</u>
Total Incurred	<u>131,319,565</u>
Payments:	
Claims attributable to insured events of the fiscal year	116,433,316
Claims attributable to insured events of prior fiscal years	<u>13,937,328</u>
Total Paid	<u>130,370,644</u>
Balance—End of the Year	<u>\$17,238,575</u>

## 7. DRUG COINSURANCE ANNUAL OUT-OF-POCKET MAXIMUMS

During the 12-month period ended December 31, 2007, the HIRSP pharmacy benefit design was structured to apply coinsurance and annual out-of-pocket maximum limitations on policyholder payments for prescription drugs. The annual out-of-pocket maximum amount varied for each HIRSP benefit plan. When a policyholder reached the coinsurance out-of-pocket maximum, HIRSP subsequently paid 100.0 percent of the allowed amount of drug benefits for the remainder of the calendar year.

Plan 1A policyholders who qualified for deductible reduction subsidies also qualified for reductions in drug coinsurance out-of-pocket maximums. The following table provides a schedule of the medical deductible and corresponding drug coinsurance out-of-pocket maximums that were applicable during the 12-month period ended December 31, 2007. Refer to Note 8 for further discussion of the drug coinsurance subsidies provided during the reporting period.

HIRSP Benefit Plan	Annual Household Income		Medical Deductible	Drug Coinsurance Out-of-Pocket Maximum
	At least	but less than		
Plan 1A	\$20,000	–	\$1,000	\$ 750
	17,000	\$20,000	800	600
	14,000	17,000	700	525
	10,000	14,000	600	450
	0	10,000	500	375
Plan 1B	All Income Levels		2,500	1,000
Plan 2	All Income Levels		500	125

Effective January 1, 2008, the HIRSP prescription drug benefit design was changed to a tiered copayment plan with a new out-of-pocket benefit design, and the predecessor benefit design model of drug coinsurance with maximum out-of-pocket limitations for drug spending was terminated.

## 8. PREMIUM, DEDUCTIBLE, AND DRUG COINSURANCE SUBSIDIES

The HIRSP Authority provides subsidies to eligible low-income policyholders, which reduce the amounts policyholders are required to pay for premiums, health care deductibles, and prescription drug costs. Effective January 1, 2008, significant changes were made in HIRSP benefit plan designs and the subsidy program. The following discussion pertains to the subsidy program and subsidy benefits applicable during the 12-month period ended December 31, 2007.

During the 12-month period ended December 31, 2007, HIRSP policyholders who were enrolled in Plan 1A or Plan 2 and who had annual household incomes below \$25,000 were eligible for a premium subsidy. No premium

subsidy was available for policyholders enrolled in Plan 1B. Policyholders enrolled in Plan 1A with incomes below \$20,000 were also eligible for a deductible subsidy and for drug copayment maximums. No deductible subsidy was available for policyholders enrolled in Plan 1B or Plan 2.

The full premium rates for HIRSP policyholders who are not eligible for a premium subsidy are established through actuarial modeling of projected annual revenues and plan costs. Chapter 149, Wis. Stats., established HIRSP's subsidized premium rates as a percentage of the standard-risk rate; that is, the rate that a commercial insurer would charge for an individual insurance policy that provides substantially the same coverage and deductibles as provided under a HIRSP policy.

Premium rates for unsubsidized HIRSP policyholders in Plan 1A equaled 148.8 percent of the standard-risk rate for the period July 1, 2006, through June 30, 2007, and equaled 153.9 percent of the standard-risk rate for the period July 1, 2007, through December 31, 2007. During the 12-month period ended December 31, 2007, the subsidized premiums paid by Plan 1A or Plan 2 policyholders who were eligible for the subsidy program were indexed to the standard-risk rate as indicated in the following table:

<u>Annual Household Income</u>		<u>Amount of Premium as Percentage of Standard-Risk Rates</u>	<u>Reduction in Deductible for Plan 1A Participants</u>
<u>at Least</u>	<u>but Less Than</u>		
\$ 0	\$10,000	100.0%	\$500
10,000	14,000	106.5	400
14,000	17,000	115.5	300
17,000	20,000	124.5	200
20,000	25,000	130.0	N/A

In the 12-month period ended December 31, 2007, 16.0 percent of HIRSP policyholders received premium, deductible, and/or drug coinsurance subsidies totaling \$5,781,505. The following table summarizes the subsidies provided for each subsidy type during that period.

<u>Subsidy Type</u>	
Premium	\$4,844,378
Deductible	620,445
Drug Coinsurance	<u>316,682</u>
Total	\$5,781,505

For the 12-month period ended December 31, 2007, federal grant funds totaling \$2,089,225 were applied to premium subsidies. The remaining premium, deductible, and drug coinsurance subsidy costs were shared equally by health insurers and health care providers, with each contributing \$1,846,140.

## 9. HEALTH CARE PROVIDER CONTRIBUTIONS

Statutes require that 20.0 percent of HIRSP plan costs be funded by health care providers. In addition, 50.0 percent of the plan subsidies not covered by federal funding are funded by health care providers. Under current HIRSP practice, only nonpharmacy providers supply the funding for provider contributions. Provider contributions are not a source of revenue; rather they represent a decrease in expenditure and are therefore reflected in the financial statements as a reduction to gross medical losses and a decrease to total operating expenses. Provider contributions are obtained by reducing the amount paid to participating providers for billed services.

The basis for calculating HIRSP's program costs is usual and customary charges, which are reported as gross medical losses in the financial statements. The usual and customary charges are determined by applying a 28.5 percent discount to billed services. Provider contributions represent the difference between HIRSP-defined usual and customary charges and reimbursed or allowed amounts, which are primarily based on Medicaid reimbursement rates plus an add-on percentage.

Although management believes the results of the estimates for provider contributions are materially correct, uncertainties inherent in estimates may potentially result in actual provider contributions that exceed or are less than the amounts estimated.

Effective January 1, 2008, the HIRSP Authority adopted a fee schedule to serve as the usual and customary rates. This schedule is based on an actuarial analysis of HIRSP claim experience and on analysis of generalized medical payment billing and payment practices in the health care industry. For most health care services, the current discount factor applied to the HIRSP Authority's fee schedule rates to derive the HIRSP-allowed or reimbursed amount is 29.0 percent.

## 10. FEDERAL GRANT REVENUE

In certain years, the federal government has appropriated monies for federal grants that are awarded for the purpose of providing funds to state risk-sharing insurance plans. The grants are awarded by the Centers for Medicare and Medicaid Services (CMS). HIRSP was awarded \$4,422,935 in CMS federal grant funds in September 2006.

Pursuant to s. 149.143, Wis. Stats., the Authority "shall pay for premium, deductible, and copayment subsidies in a policy year first from federal funds, if any." Any grant fund receipts in excess of policyholder subsidy costs are applied to offset operations losses, per the grant agreement. Consequently, the federal grant funds of \$4,422,935 were applied to partially offset premium subsidy funding required for the period from July 1, 2006, through June 30, 2007, and equaled 86.4 percent of the premium subsidies that were

allowed in that period. The HIRSP Authority applied \$2,333,710 of the federal grant funds to offset policyholder subsidy costs in the six-month period ended December 31, 2006, and \$2,089,225 in the six-month period ended June 30, 2007.

## 11. PENSION BENEFITS

During the 12-month period ended December 31, 2007, HIRSP Authority employees participated in a Section 457 deferred compensation plan. The employer contributions to the plan were up to 3.0 percent of the employee's gross salary. In addition, the HIRSP Authority contributed up to 2.0 percent of the employee's gross salary to an Individual Retirement Account (IRA) for each of the HIRSP Authority employees.

2007 Wisconsin Act 20, which was enacted in October 2007, allowed HIRSP Authority employees to participate in the Wisconsin Retirement System (WRS), a cost-sharing, multiple-employer, defined benefit plan governed by ch. 40, Wis. Stats. State and local government public employees are entitled to an annual formula retirement benefit based on: 1) the employee's final average earnings, 2) years of creditable service, and 3) a formula factor. If an employee's contributions, matching employer's contributions, and interest credited to the employee's account exceed the value of the formula benefit, the retirement benefit may instead be calculated as a money purchase benefit. Copies of the separately issued financial report that includes financial statements and required supplementary information of the WRS may be obtained by writing to:

Department of Employee Trust Funds.  
P.O. Box 7931  
Madison, WI 53707-7931

The most current financial report is also available on the Department of Employee Trust Funds' Web site, <http://etf.wi.gov>.

The WRS requires employee contributions equal to specified percentages of qualified earnings based on the employee's classification, plus employer contributions at a rate determined annually.

**12. CAPITAL ASSETS**

The HIRSP Authority purchased office equipment and furniture during the 12-month period ended December 31, 2007. These items are included in other assets on the Balance Sheet; depreciation expense is included in general and administrative expenses.

	<u>Beginning Balance</u>	<u>Increases</u>	<u>Decreases</u>	<u>Ending Balance</u>
Capital Assets Being Depreciated:				
Equipment, at Historical Cost	\$15,539	\$19,304	\$ 0	\$34,843
Less Accumulated Depreciation for:				
Equipment	<u>(243)</u>	<u>(5,310)</u>	<u>0</u>	<u>(5,553)</u>
Total Capital Assets Being Depreciated, Net	<u>\$15,296</u>	<u>\$13,994</u>	<u>0</u>	<u>\$29,290</u>

**13. SUBSEQUENT EVENTS**

Effective January 1, 2008, the HIRSP Authority instituted numerous changes to the risk-sharing plan. Changes in the benefit plan design included the addition of two new indemnity benefit plans: a \$3,500 deductible health savings account qualified plan, and a \$5,000 deductible health care benefit plan. Modifications to the plan design include applicability of low-income subsidies to all of the indemnity insurance benefit plans, modification of the drug benefit plan design to a tiered copayment plan, and an increase in the maximum out-of-pocket limitation for prescription drug benefits. Significant changes were made in the provider contribution methodology, including the adoption of a HIRSP Authority fee schedule for health care services.



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# Auditor's Report ■

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***Independent Auditor's Report on Internal Control over  
Financial Reporting and on Compliance and Other Matters  
Based on an Audit of Financial Statements Performed in  
Accordance with Government Auditing Standards***

We have audited the financial statements of the Wisconsin Health Insurance Risk-Sharing Plan (HIRSP) Authority as of and for the year ended December 31, 2007, and have issued our report thereon dated October 14, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

## **INTERNAL CONTROL OVER FINANCIAL REPORTING**

In planning and performing our audit, we considered the HIRSP Authority's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the HIRSP Authority's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the HIRSP Authority's internal control over financial reporting.

*A control deficiency* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that

adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control.

*A material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Our consideration of internal control was for the limited purpose of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control that we consider to be material weaknesses, as defined in the preceding paragraph.

#### COMPLIANCE AND OTHER MATTERS

As part of obtaining reasonable assurance about whether the HIRSP Authority's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This independent auditor's report is intended for the information and use of the HIRSP Authority's management and Board of Directors, the Wisconsin Legislature, federal awarding agencies, and pass-through entities. This report, upon submission to the Joint Legislative Audit Committee, is a matter of public record and its distribution is not limited. However, because we do not express an opinion on the effectiveness of the HIRSP Authority's internal control over financial reporting or on compliance, this report is not intended to be used by anyone other than these specified parties.

October 14, 2008

LEGISLATIVE AUDIT BUREAU  
by   
Diann Allsen  
Audit Director

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# Auditor's Report ■

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## ***Independent Auditor's Report on the Wisconsin Health Insurance Risk-Sharing Plan Authority's Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133***

### **COMPLIANCE**

We have audited the Wisconsin Health Insurance Risk-Sharing Plan (HIRSP) Authority's compliance with the types of compliance requirements described in the federal Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to the HIRSP Authority's major federal program for the year ended December 31, 2007. The major federal program is identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to the HIRSP Authority's major federal programs is the responsibility of HIRSP Authority management. Our responsibility is to express an opinion on the HIRSP Authority's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above, and which could have a direct and material effect on a major federal program, occurred. An audit includes examining, on a test basis,

evidence about the HIRSP Authority's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the HIRSP Authority's compliance with those requirements.

In our opinion, the HIRSP Authority complied, in all material respects, with the requirements referred to in the preceding paragraphs that are applicable to its major federal program for the year ended December 31, 2007. However, the results of our auditing procedures disclosed an instance of noncompliance with those requirements that is required to be reported in accordance with OMB Circular A-133 and which is described in the accompanying Schedule of Findings and Questioned Costs as finding WI HIRSP 07-1.

### INTERNAL CONTROL OVER COMPLIANCE

Management of the HIRSP Authority is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the HIRSP Authority's internal control over compliance with the requirements that could have a direct and material effect on its major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the HIRSP Authority's internal control over compliance.

*A control deficiency* in an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

*A material weakness* is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control.

Our consideration of the internal control over compliance was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined in the preceding paragraph.

This independent auditor's report is intended for the information and use of the HIRSP Authority's management and Board of Directors, the Wisconsin Legislature, federal awarding agencies, and pass-through entities. This report, upon submission to the Joint Legislative Audit Committee, is a matter of public record and its distribution is not limited. However, this report is not intended to be used by anyone other than these specified parties.

LEGISLATIVE AUDIT BUREAU

October 14, 2008

by   
Diann Allsen  
Audit Director



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## **Schedule of Expenditures of Federal Awards ■**

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**Schedule of Expenditures for Federal Awards  
for the Year Ended December 31, 2007**

FEDERAL GRANTOR/Pass-Through Grantor/Program Title	<u>CFDA Number</u>	<u>Federal Expenditures</u>
U.S. DEPARTMENT OF HEALTH AND HUMAN SERVICES— Centers for Medicare and Medicaid Services		
Pass-through from the Wisconsin Office of the Commissioner of Insurance		
<i>Grants to States for Operation of Qualified High Risk Pools</i>	93.780	<u>\$2,089,225</u>
<b>TOTAL EXPENDITURES OF FEDERAL AWARDS</b>		<u><u>\$2,089,225</u></u>

*The accompanying notes are an integral part of this schedule.*



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# Notes to the Schedule of Expenditures for Federal Awards ■

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## 1. PURPOSE

The Schedule of Expenditures for Federal Awards includes the federal grant activity of the Wisconsin Health Insurance Risk-Sharing Plan (HIRSP) Authority for the year ended December 31, 2007. The Grants to States for Operation of Qualified High Risk Pools is a major federal program that was tested for compliance with federal requirements for 2007.

Because the schedule presents only a selected portion of the activities of the HIRSP Authority, it is not intended to and does not present the financial positions or results of operations of the HIRSP Authority.

## 2. BASIS OF ACCOUNTING

The information in the schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. The amounts in the schedule are presented on the same basis as used in the financial statements—the accrual basis of accounting.

The information included in the schedule may not fully agree with other federal award reports that the HIRSP Authority submits directly to the federal granting agency because the award reports may be prepared for different fiscal periods and may include cumulative data from a prior period rather than data for the current period only.

**3. CHANGE IN FISCAL PERIOD**

HIRSP financial information was previously reported on a state fiscal year basis through the fiscal year ended June 30, 2006. The HIRSP Authority used a calendar year basis for financial reporting beginning with calendar year 2007. A separate single audit report for the interim six-month period ended December 31, 2006, has been issued concurrently.

**4. AMOUNT PROVIDED TO SUBRECIPIENTS**

OMB Circular A-133 requires the Schedule of Expenditures of Federal Awards, to the extent practical, to include the amount provided to subrecipients under each federal program. The HIRSP Authority did not provide any federal awards to subrecipients during 2007.

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# Schedule of Findings and Questioned Costs ■

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OMB Circular A-133 requires the auditor to prepare a schedule of findings and questioned costs that includes the following three sections:

- 1) a summary of the auditor's results;
- 2) findings related to the financial statements, which are required to be reported in accordance with *Government Auditing Standards*; and
- 3) findings and questioned costs for federal awards.

## Section I

### Summary of Auditor's Results

As required by OMB Circular A-133, the Wisconsin Legislative Audit Bureau is providing the following summary information related to the Wisconsin HIRSP Authority's single audit for 2007:

#### Financial Statements

Type of auditor's report issued	Unqualified
Internal control over financial reporting:	
Material weaknesses identified?	No
Significant deficiencies identified that are not considered to be material weaknesses?	No
Noncompliance material to financial statements noted?	No

**Federal Awards**

Internal control over major program:	
Material weaknesses identified?	No
Significant deficiencies identified that are not considered to be material weaknesses?	No
Type of auditor’s report issued on compliance for major programs:	Unqualified
Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133?	Yes
Dollar threshold used to distinguish between type A and type B programs:	\$300,000
Auditee qualified as a low-risk auditee?	No

The HIRSP Authority’s major federal program is the Grants to States for Operation of Qualified High Risk Pools, CFDA 93.780, which was awarded by the U.S. Department of Health and Human Services—Centers for Medicare and Medicaid Services.

**Section II**

**Financial Statement Findings**

This section of the schedule includes all significant deficiencies related to internal control over financial reporting and compliance and other matters that are required to be reported by auditing standards generally accepted in the United States of America and by *Government Auditing Standards*, including those that do not affect federal awards. No financial statement findings are reported for the 12-month period ended December 31, 2007.

**Section III**

**Federal Award Findings and Questioned Costs for 2007**

**Finding WI HIRSP 07-1: Cash Management**

*Criteria:*

45 CFR 92.21 requires that a grantee and subgrantee maintain procedures to minimize the time elapsing between the transfer of federal funds and their disbursement by the grantee or subgrantee. At least quarterly, the grantee or

subgrantee should remit to the federal government interest earned on advances of federal funds. The grantee or subgrantee may keep interest amounts up to \$100 per year for administrative expenses.

***Condition:***

The entire amount of the \$4,422,935 grant awarded to Wisconsin for HIRSP in September 2006 by the Centers for Medicare and Medicaid Services (CMS) in the U.S. Department of Health and Human Services under the Grants to States for Operation of Qualified High Risk Pools Program, CFDA 93.780, was drawn from the federal government by the Wisconsin Department of Administration (DOA) in November 2006. The funds were transferred through Wisconsin Office of the Commissioner of Insurance (OCI) to the HIRSP Authority in the first week of January 2007. The HIRSP Authority had spent only \$2,333,710 of the federal grant when it received the funds in January 2007. The remaining \$2,089,225 was spent from January through June 2007. The HIRSP Authority did not remit to CMS any interest earned on the federal funds it received.

***Questioned Costs:***

None

***Context:***

Responsibility for administering HIRSP was transferred from the Wisconsin Department of Health and Family Services to the HIRSP Authority effective July 1, 2006. At that time, state statutes designated OCI as the state agency to receive federal high-risk pool grants to be paid to the HIRSP Authority. Subsequently, statutes were changed, and currently the federal grant funds are remitted directly to the HIRSP Authority, which indicates it is drawing federal funds as related expenditures are incurred.

***Effect:***

The HIRSP Authority may owe interest to CMS on the advance of \$2,089,225 it received in January 2007. Potential interest earnings on those funds are estimated to not exceed \$33,000 for the period January through June 2007.

***Cause:***

The HIRSP Authority's staff were not aware of and were not informed about the cash management requirements. The change in administration of HIRSP and the various state agencies involved during the transition period may have caused some confusion regarding the administration of the federal grant and related cash management requirements.

***Recommendation:***

We recommend the HIRSP Authority work with CMS, DOA, and OCI to resolve the federal cash management issue and take steps to ensure it is meeting federal cash requirements in the future.

*Management's Response and Corrective Action Plan:*

The HIRSP Authority agrees to comply with the recommendation and expects to be in compliance within 60 days of the issuance of the audit report. It is currently working with CMS to determine what liabilities the State of Wisconsin and the HIRSP Authority may have for unpaid interest on the federal funds. The HIRSP Authority will promptly remit full payment of any amount of interest that may be due to the federal government for the period in which the HIRSP Authority was in custody of the unexpended grant funds. It will also work with DOA and OCI to identify any interest liability of the State for the period November 2006 through December 2006.

In the future, the HIRSP Authority's federal grant cash management practices will comply in all respects with federal laws and rules that govern grant recipient treatment of federal grant cash. Management of federal grants awarded to the HIRSP Authority is now entirely the responsibility of the HIRSP Authority executive staff and no longer requires that actions be performed on behalf of the HIRSP Authority by multiple third-party entities.

**Federal Award Findings and  
Questioned Costs for Prior Periods**

No federal award findings or questioned costs were reported for prior periods.

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