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Date: June 25, 2013

To: Consumer Watchdog

From: Allan I. Schwartz, FCAS, ASA, MAAA

Re: Review of Health Net Life Insurance Company
H16I.005A Individual - Preferred Provider (PPO) Rate Filing Dated May 23, 2013
SERFF Tracking #: HNLI-129044832 State Tracking #: HAO-2013-0108

We have reviewed the above captioned filing submitted by Health Net Life Insurance Company ("Health Net), as well as some additional information that was supplied.[1,2,3] Since this is a new product, technically there is not a rate change being requested. However, the Unified Rate Review Template ("URRT") does indicate an increase over the two year period from 2012 to 2014 in the projected average gross premium PMPM over the average gross premium PMPM in the experience period of 127%.[4] That is an average annual increase of 50.7%.

There are a number of assumptions / factors driving that increase, the largest by far being the use 2012 small group experience (as adjusted in numerous calculations) as a surrogate for the projected 2014 individual market experience. The Health Net calculations effectively include an increase in the "population risk morbidity" for the individual insurance market of 71.4%.[5] The remainder of this memo deals with this particular issue from three different perspectives: (i) Health Net's individual market experience compared to small group experience, (ii) Health Net's

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[1] This analysis was provided to assist Consumer Watchdog (CWD) in its evaluation of the Health Net filing, including submitting this document to the California Department of Insurance (CDI). It should not be relied upon for any other purpose or by any other entities. If this analysis is provided to any other entity the following conditions apply: (i) it should only be done after obtaining the written consent of AIS, (ii) the entire analysis should be supplied and (iii) that entity should be informed that AIS is available under appropriate circumstances to discuss the analysis.

[2] My analysis is based upon the information currently available. My analysis and conclusions may change if additional relevant information becomes available. Furthermore, my lack of comment on particular aspects of the filing should not be taken to mean that I agree with those procedures.

[3] The initial filing as well as additional information is available at the CDI website at:
https://interactive.web.insurance.ca.gov/apex/f?p=102:9:0::NO::P9_RATE_FILINGS_ID,P9_COMPANY_NAME,P9_REFERRING_PAGE_NUM:7607,Health%20Net%20Life%20Insurance%20Company,4&cs=16FDA54247E591EFDF83F502B7028D59A
CDI also provided some EXCEL spreadsheets that were not available on the website

[4] Health Net filing, URRT, Cell V45; 127% = [$337.10 (Cell V43) / $148.53 (Cell G14) – 1] X 100%

[5] Health Net filing, URRT, Cells J24-J29

small group PPO experience compared to small group HMO experience and (iii) Health Net's proposed rates versus other companies.

All three of these measures indicate that the Health Net proposed PPO rates may be unreasonably high.

1. Individual Market Experience Compared To Small Group Experience

Health Net makes the assumption that it cannot rely on its historical individual market experience to calculate individual health insurance premiums for California and instead relies upon small group historical data, stating "We do not consider calendar year 2012 experience of underwritten members in the Individual market to have any credibility in predicting 2014 claims costs for the state of California in light of the new market rules, including guarantee issue. Instead, we relied on Health Net claims experience in the Small Group market which is guarantee issue today."[6]

The conclusion by Health Net that the historical individual market experience is not credible cannot be based upon the volume of experience, since Health Net's $68 million in allowed claims for 2012 in the individual insurance market is more than sufficient for full credibility based upon standard actuarial procedures. Health Net's decision is instead based upon the various adjustments that would need to be made to reflect the changes in the environment from 2012 to 2014. However, in its rate calculation Health Net also makes numerous adjustments to the 2012 small group experience to convert that to a 2014 individual market basis.[7] So the distinction between those two underlying databases (i.e., 2012 individual versus 2012 small group) in that regard is not clear.

In any case, Health Net does make projections of the 2014 individual market index rate based upon both 2012 individual market experience and 2012 small group market experience. The results from the two projections are remarkably similar, $424.95 based on individual market experience[8] compared to $425.33 based on small group market experience[9], a difference of only 0.1%. That small difference is not a

[6] Health Net filing, Actuarial Memorandum and Certification, Experience Period Premium and Claims

[7] Health Net filing, Table 18: Index Rate Calculation (based on Small Group Experience)

[8] Health Net filing, Table 17: Index Rate Calculation (based on Individual Experience)

[9] Health Net filing, Table 18: Index Rate Calculation (based on Small Group Experience)

coincidence, but is a result of the interaction between the adjustments made by Health Net to the historical individual and small group market experience.

As previously discussed, the 2014 index rate projection by Health Net includes an increase in the individual market morbidity of 71.4%.[10] The biggest component of that is an increase for an "Adjustment to reflect ave experience for the market" of 61.5%.[11] That is an extremely large increase in the average morbidity. By way of comparison, Milliman prepared a report for Covered California which included a best estimate for the "Impact Due to Change Health Status Factor" of 26.5%.[12,13]

This large disparity between the Health Net factor of 61.5% compared to the Milliman factor of 26.5% is an indication that the Health Net Index Rate, along with the resulting premium rates could be unreasonably high.

2. Small Group PPO Experience Compared To Small Group HMO Experience

Health Net made a rate filing for its PPO business with the California Department of Insurance (CDI) and for its HMO business with the Department of Managed Health Care (DMHC).

In both instances, Health Net derived a projected index rate based upon an analysis of the historical small group experience. A comparison of those index rates, as shown in the following table, shows the index rate submitted by Health Net to CDI for its PPO product is much higher than the index rate submitted by Health Net to DMHC for its HMO product.

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[10] Health Net filing, Table 3: Individual Morbidity Adjustments

[11] *Ibid.*

[12] "Factors Affecting Individual Premium Rates in 2014 for California" (March 28, 2013), Figure 11: Estimated Premium Impact Due to Change Health Status Factor. A range was given from a low of 15% to a high of 40%.

[13] Health Net relied on that Milliman report for a number of other factors, such as a "Benefit Coverage Anti-Selection" increase of 1.9% and a "Pent Up Demand" increase of 2.1%. (Health Net filing, Table 3: Individual Morbidity Adjustments)

Comparison of Health Net 2014 HMO and PPO Index Rates

	2014 Index Rate
Health Net of California, Inc. - IEX HMO Plans *	$339.12
Health Net Life Insurance Company - IFP PPO P30601 **	$425.33
Percent Difference	25.4%

* SERFF Tracking #: HNLH-129042377, Table 21: Index Rate Calculation

** SERFF Tracking #: HNLI-129044832, Table 18: Index Rate Calculation

The index rate represents the average allowed claims PMPM for essential health benefits. Hence, any difference in the index rate between the HMO and PPO products cannot be attributed to a variation in the level of benefits. One possible reason for the dissimilarity between the HMO and PPO index rates could be differences in the provider networks.[14] However, a variance of more than 25% based upon this seems rather large and could be an indication that the Health Net's PPO Index Rate, along with the resulting premium rates could be unreasonably high.

With regard to provider networks, the Milliman report had a best estimate for a cost savings resulting from "provider contracting changes" of -6%.[15] In regard to this issue, the Milliman report states in part "Our best estimate also includes some savings from narrow network plan designs. According to the 'Managed Care and Providers Wrap-Up' from the January 2013 J.P. Morgan Health Conference, carriers are expecting to offer narrow network plans with hospital contracts that are 10-15% lower than current commercial rates."

[14] Another issue could relate to differences in population morbidity between the two products. We are not commenting on whether or not the ACA allows for differences in rates based upon differences in morbidity in this type of situation. However, both the Health Net PPO and HMO filings include a factor for an "Adjustment to reflect ave experience for the market". Furthermore, both the Health Net PPO and HMO filings state "We estimate the market to have a risk score of 1.168." Hence, in this particular situation, after the adjustments made by Health Net, it appears that the differences in the index rates would not be expected to reflect a difference in the projected morbidity for the 2014 period. It was not possible to verify the numerical value of the adjustments made by Health Net in this regard because sufficient information was not supplied.

[15] "Factors Affecting Individual Premium Rates in 2014 for California" (March 28, 2013), Figure 12: Estimated Premium Impact Due to Provider Contracting Changes. A range was given from a low of -9% to a high of 1%.

It is also probable that there can be a reduction in provider charges due to a decrease in the uncompensated care resulting from uninsureds being unable to pay for medical care. As the uninsured population in California decreases as a result of the Affordable Care Act, the amount of uncompensated care will decrease, and that should result in a reduction in provider charges for commercial insurance coverage. Historically there has been a large amount of uncompensated medical care in California, which has been estimated at $2.4 billion for 2010.[16] Hence, as the uninsured population decreases in California, the amount of uncompensated care that is built into provider charges for commercial insurance coverage should decease, resulting in a lowering of those charges.

The Milliman Report also discusses this issue, stating in part "The Affordable Care Act has the potential to reduce the costs for commercially funded health services by reducing the impact of 'cost shifting.' Providers currently argue that they are underpaid for Medicare and Medi-Cal patients, and not paid for uninsured patients. In order to cover their costs and achieve target total revenue, the only reimbursement rates that the providers can negotiate are for commercial members. If providers believe that their revenue for services provided to Medi-Cal and for currently uninsured patients will increase in 2014, they may be willing to accept lower reimbursement for commercial patients, or possibly just for Exchange patients."

CDI inquired with Health Net about this subject asking for the following "**Networks** – describe any differences in provider contracting between the network serving small-group plans in 2012 and the networks serving individual and small-group plans in 2014. Specify any effects these differences have on 2014 rate development for individual and small-group plans."[17] The response from Health Net indicated they did not reflect any savings from provider networks / contracting stating "The only network difference contemplated at this time is the addition of Essential Community Providers to network per the requirements of Covered California. There is no expected pricing impact of this relatively minor change."

Health Net's inability to implement any savings from changes to provider networks / contracting could also result in unreasonably high rates.

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[16] California Health Care Almanac, published by the California Health Care Foundation, January 2013

[17] CDI Website, file "HAO20130108SubsequentSubmissionJune172013", Item 7

3. **Health Net Proposed Rates Versus Other Companies**

We reviewed the Covered California publication "Health Plans & Rates for 2014" (March 23, 2013). An evaluation of those rates by region / plan / company indicated that the Health Net PPO rates were generally higher than the average rates for all companies combined as contained in that Covered California publication. This is consistent with the prior two items that the Health Net's proposed PPO rates as filed with CDI could be unreasonably high.

I am a member of the American Academy of Actuaries and meet the requirements to provide this opinion, which is based upon generally accepted actuarial procedures.

Please feel free to contact me if there is anything you would care to discuss.