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POLICY & ACTION FROM CONSUMER REPORTS

May 31, 2012

Via email: epaniewski@dmhc.ca

Elaine Paniewski
Staff Services Manager
Department of Managed Health Care
980 9th Street, Suite 500
Sacramento, CA 95814-2725

Re: Kaiser Foundation Health Plan, Inc. (Kaiser) Individual HMO California Rate Filing

Dear Ms. Paniewski:

Consumers Union, the policy and advocacy division of Consumer Reports, writes to provide you with comments on the rate filing of Kaiser Foundation Health Plan, Inc. (Kaiser) Individual HMO California Rate filing. Consumers Union is concerned that Kaiser has not provided sufficient information to justify its proposed rate increase. Kaiser is proposing an overall average rate increase of 9% since July 2011, ranging from a minimum increase of 4% to a maximum increase of 14%. 17,653 enrollees are affected by this rate change.

As detailed in the attached memo by our consulting actuary, Allan I. Schwartz, DMHC should request more information to support the requested rate increase. Highlighted below are our areas of concern:

1. Kaiser should provide an explanation for the why the ratio of the "Written Premium Change for this Program" divided by the "Written Premium for this Program" is different than the stated valued for the rate change.
2. DMHC should request information from Kaiser regarding the accounting system used to make sure that expenditures are accurately and appropriately recorded for medical care as opposed to administrative and overhead expenses.
3. There is some reason to question whether the 7.8% annual medical trend may be too high for the business covered by this rate filing. Kaiser should provide a complete detailed explanation of how that 7.8% annual medical trend value was selected. Kaiser should also explain why the proposed annual rate increase exceeds the medical, as well as the combined medical and expense cost trend factor.
4. Kaiser should provide support for it cost provision for SB 946 of 0.7%.
5. Kaiser should provide all the underlying relevant documentation and analyses regarding the bases for KFHP Actuarial Services' estimates, projections and calculations.
6. Kaiser should provide the detailed documentation and analyses that represents and explains their actual rate setting process.

Consumers Union urges DMHC to request the additional information from Kaiser and thoroughly review the underlying assumptions in this rate filing. We also request that you post the additional documents you receive from Kaiser on your website.

Sincerely,

Laurie Sobel
Senior Attorney

Headquarters Office
101 Truman Avenue
Yonkers, New York 10703-1057
(914) 378-2029
(914) 378-2992 (fax)

Washington Office
1101 17th Street, NW #500
Washington, DC 20036
(202) 462-6262
(202) 265-9548 (fax)

West Coast Office
1535 Mission Street
San Francisco, CA 94103-2512
(415) 461-6747
(415) 431-0906 (fax)

South West Office
506 West 14th Street, Suite A
Austin, TX 78701
(512) 477-4431
(512) 477-8934 (fax)

AIS RISK CONSULTANTS, INC.

Consulting Actuaries • Insurance Advisors

4400 Route 9 South • Suite 1200 • Freehold, NJ 07728 • (732) 780-0330 • Fax (732) 780-2706

Date: May 31, 2012

To: Consumers Union

From: Allan I. Schwartz

Re: Comments on Kaiser Foundation Health Plan, Inc.
Individual HMO California Rate Filing Proposed Effective July 1, 2012
SERFF Tr Num: KHPI-128191279

Our comments on the above captioned filing follow. The issues addressed are those specified by the Department of Managed Health Care (DMHC).

- **Issue**:
  Looking at the historical context of the health plan's rate filing, does it appear the requested rate maintains rate stability and operates in a way to prevent excessive rate increases in the future?

  Response:
  The Kaiser Foundation Health Plan, Inc. ("Kaiser") individual HMO Population 3 proposed rate increase effective July 2012 is 4.5% over January 2012 rates and 9.0% over July 2011 rates.[1,2] Rate increases of this magnitude would generally be considered to be moderate for health insurance thereby maintaining rate stability, but also serve to offset health insurance medical cost inflation thereby lessening the possibility of excessive rate increases in the future. The Population 3 rate change is based upon combined experience for Populations 1, 2 and 3. Kaiser claims that "Population 3 has not accumulated credible experience yet."[3] However, it would be useful for Kaiser to provide the experience for Population 3 alone so that it could be evaluated.

  The range of rate changes around the 4.5% overall value is from a minimum of +0.0% to a maximum of 9.9%.[4] The range of rate changes around the 9.0% overall value is from a

[1] The experience that formed the basis for this rate filing is for Populations 1, 2 and 3 combined. Population 3 rates change on both January 1 and July 1. Population 1 and 2 rates change only in January of each year. This rate filing impacts the rates only for Population 3. For Populations 1 and 2 the January 2012 rate increase is 9.0% over January 2011 rates. (Rate filing, general information section) A description of Populations 1, 2 and 3 is contained in the rate filing in Exhibit E-1, pages 2 to 3.

[2] Rate filing, General Information Section

[3] Rate filing, General Information section

[4] Rate filing, Rate Review Details Section

minimum of +4.0% to a maximum of 14.0%.[5] Hence, the variation in rate changes between policyholders is about +/- 5% around the average value.

There were some statistical values regarding the rate change that did not appear to reconcile. Kaiser indicated that the "Written Premium for this Program" is $79,316,185 and that the "Written Premium Change for this Program" is $2,835,734.[6] The ratio of these two amounts is 3.6%, which is different than the stated value for the rate change. Kaiser should provide an explanation for this apparent discrepancy.

- **Issue**:
  Does the contractor believe the proposed profit or contribution to surplus is reasonable?

  Response:
  The filing did not include an explicit value for the proposed profit or contribution to surplus. The only numerical value for profit provided was the "July 12 to June 13 Estimated Margin (KFHP and KFH combined)".[7] The estimated margin values shown were 5.5% for copayment plans, -0.2% for deductible plans, -6.3% for deductible plans with HSA Option and -18.8% for continuation of coverage plans; for an overall value of -0.8%. The source for these values was given as "Implicit from KFHP management rate decision and other rating factors".

  A -0.8% underwriting profit margin as a percent of revenue, when considered along with investment income, is sufficient to allow Kaiser to operate at a positive combined profit. The proposed profit value is not excessive.

- **Issue**:
  The loss ratio is the relationship between the claims paid by the insurer and the premiums received. Does the loss ratio seem reasonable?

  Response:

[5] Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Table 4

[6] Rate filing, Rate Information Section

[7] Milliman document, Appendix C-4 "Development of Annual Rate Increase Percentage" and Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing Spreadsheet Table 5

The "Rate Development Worksheet" shows a "CY 2011 MLR (Unadjusted)" of 90.7% and a "Jul-12 - Jun-13 Projected MLR (Unadjusted)" of 95.1%.[8] Loss ratios of that magnitude are generally considered reasonable for individual business.[9] A possible issue regarding the loss ratio is that in an integrated system like that used by Kaiser, there could be difficulties in accurately separating expenditures between those made for health care as opposed to those for administrative and overhead expenses. DMHC may want to request information from Kaiser regarding the accounting system used to make sure that expenditures are accurately and appropriately recorded for medical care as opposed to administrative and overhead expenses.

- **Issue**:
  Trend is the rate of increase in the claims portion of an insurer's loss ratio, and consists of two components: medical inflation and use. Are the projected trends supported by the data?

  Response:
  The filing used an Overall Medical Trend Factor of 7.8% a year, consisting of 8.0% for Hospital Inpatient (and all other medical services other than prescription drugs) and 5.6% for prescription drugs.[10] This is the only breakdown of trend by component shown in the filing. The filing stated, "Due to the Kaiser Permanente (KP) integrated delivery model, KP does not develop forward looking trend expectations at the medical benefit category level (other than Prescription Drugs). 8.0% is the average medical cost trend for each of the individual plans" and "The projected trends shown above are largely attributable to implied increases in unit costs. Due to the Kaiser Permanente integrated delivery model, future trend projections are not easily separated into unit cost and utilization components".

  Despite these statements, data was provided regarding utilization trends from calendar year 2009 to 2011.[11] During this period Inpatient Hospital Days per 1000 Members were

[8] Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Table 5, Lines (17) and (18)

[9] Lower loss ratios in the 80%+ range could also be considered reasonable for individual business.

[10] Exhibit E-1 Att 1, Item 18

[11] Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Table 7 "Historical Individual HMO Utilization Data"

up by +3.2% or an average increase of +1.6% a year, Clinic Visits per Member were up by +3.0% or an average increase of +1.5% a year and Pharmacy Scripts per Member were up by +2.6% or an average increase of +1.3% a year. This overall increase in utilization would imply that the average cost is going up slower than the overall 7.8% medical trend.

A 7.8% annual medical cost trend would be considered to be within the range of reasonable trend values for health insurance. However, given the integrated nature of the Kaiser system where medical costs consist in large part of salaries and other internal expenditures, there is some reason to question whether the 7.8% annual medical trend may be too high for the business covered by this rate filing.

Kaiser provided two documents showing historical medical loss trends. Those were entitled "Comparison of Claims Cost and Rate of Changes over Time" and "KFHP Historical Individual Plan Trends".[12] With respect to the "Comparison of Claims Cost and Rate of Changes over Time" data, the combined PMPM trend from 2009 to 2010 was +5.4% and from 2010 to 2011 was +8.5%. With respect to the "KFHP Historical Individual Plan Trends", the combined PMPM trend from 2009 to 2010 was +5.1% and from 2010 to 2011 was +8.6%.[13] The average historical medical cost trends shown in those documents are somewhat lower than the overall 7.8% medical cost trend used in the rate calculation. However, the 7.8% annual trend used by Kaiser does fall within the range of historically observed trends. The only explanation given in the filing for the particular numerical trend value used was "Estimated by KFHP Actuarial Services". It would be useful for Kaiser to provide a complete detailed explanation of how that 7.8% annual medical trend value was selected.

The filing includes a cost provision for SB 946 of 0.7%. The filing states, "The Plan estimates that treatment protocols provided in compliance with SB 946 will result in a total medical cost increase of 0.7%. In the proposed rates, one half of the additional cost is spread among all members, while the rest is allocated to child subscribers of age 18

[12] Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Table 1 "Comparison of Claims Cost and Rate of Changes over Time" and Table 6 "KFHP Historical Individual Plan Trends"

[13] Kaiser stated that these data are based upon "Dollar amounts are prior to member cost sharing".

and younger (in order to maintain a reasonable rate structure, minor adjustments to the rates for young adults are made as well.)."[14] While not exactly a trend issue, this increased cost provision acts in the same manner as trend, by increasing future costs relative to historical costs. The filing did not include numerical support or data for the specific value of 0.7% used for this cost increase.

- **Issue**:
  Because every rate change tells its own story, health plans are required to file a plain language description on the website listing key factors underlying each rate filing decision. Are there key factors the contractor believes should be highlighted in the rate filing to give consumers a better understanding of the rate filing or the eventual DMHC decision?

  Response:

  The rate indication is driven in large part by the medical cost trend. We have previously raised some concerns regarding the 7.8% annual trend value. A more detailed explanation of the basis for this value should be provided by Kaiser.

  Furthermore, since administrative expense costs can be expected to increase at a slower rate than medical costs, the overall combined medical and administrative expense cost trend factor, which is an expectation for the rate change, should be lower than the medical cost trend.[15] However, for the current filing, the proposed annual increase of 9.0% is 1.2% higher than the annual medical cost trend, and would be even more in excess of the combined medical and administrative cost trend factor. Kaiser should explain why the proposed annual rate increase exceeds the medical, as well as the combined medical and administrative expense, cost trend factor.

[14] Kaiser filing, Exhibit E-1, Summary Description Of Plan Organization And Operation (Page 6 to 7 of 11), IV Explanation of Rate Information, A. Supporting Data and Assumptions

[15] As an illustrative example, if the medical costs in period 1 are $200 with a 6% annual trend and the administrative expense costs in period 1 are $25 with a 4% annual trend, the combined medical plus administrative cost trend is ($200 X 1.06 + $25 X 1.04) / ($200 + $25) = $238 / $225 = 1.058 = 5.8% annual trend. Therefore, the combined trend is between the medical trend and the administrative expense cost trend, which should be lower than the medical trend.

It would also be helpful to explain why the combined experience of Populations 1, 2 and 3 were used in the rate analysis, and how the result would have differed if the experience of Population 3 alone was used.

- **Issue**:
  Are there areas in the rate filing where DMHC should seek additional information from the health plan?

  Response:
  The only specific numerical calculation provided regarding the rate analysis was contained in the Milliman document, Appendix C-4 "Development of Annual Rate Increase Percentage".[16] The source for various items used in that calculation was given as estimated, projected or calculated by KFHP Actuarial Services. Those items included:

  Line 5: Average Annual Medical Trend

  Line 8: Adjustment for leverage and membership mix

  Line 10: July 12 to June 13 Projected Administrative PMPM

  Line 14: Cumulative Impact of Increases Implemented Prior to July 12

  Additional information, including all underlying relevant documentation and analyses, should be sought regarding the bases for these estimates, projections or calculations by KFHP Actuarial Services.

  We have also discussed elsewhere in relation to other items additional information and documentation that should be requested from Kaiser.

- **Issue**:
  Are there any unique facts about the rate filing that DMHC should be aware of that apply only to this filing or to this insurer?

  Response:

[16] This document is also contained in Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Table 5

Kaiser operates an integrated health care system. This has implications for an appropriate provision for the medical cost trends. Comments were provided on this item in other parts of this analysis.

An additional unique aspect of this filing is represented by Kaiser's statement that, "Exhibit E-1 Attachment 3, Table 5 shows an after-the-fact rate development view in a traditional presentation format. Note that this does *not* reflect the actual rate setting process described above in Section III. Instead, this simulated view is provided in response to a request from the Department to see the rate development in a format that allows the Department to more accurately compare the Plan with its non-integrated competitors. The experience period is calendar year 2011."[17] The only document provided by Kaiser that shows a numerical calculation of the rate change is Exhibit E-1 Attachment 3, Table 5. By Kaiser's own admission, that does not reflect the actual rate setting process. Kaiser should provide the detailed documentation and analyses that does represent and explain the actual rate setting process.[18]

- **Issue**:
  Health Plans must report and justify changes in administrative expenses by line of business and must provide more detail about what they spend on salaries, commissions, marketing, advertising and other administrative expenses. Do the administrative expenses seem reasonable? If not, please identify the particular unreasonable expense and explain why it is not reasonable.

  Response:

  The filing did not provide a breakdown of administrative expenses by category so we are not able to comment on individual expense items. The "July-12 - June-13 Projected Administrative PMPM" of $20.65 is about 6% of Kaiser's "Jul-12 - Jun-13 Required Revenue PMPM" of $367.53.[19] That ratio seems reasonable and does not seem excessive. The filing uses a slightly downward administrative expense trend factor,

[17] Kaiser filing, Exhibit E-1, Summary Description Of Plan Organization And Operation (Page 6 of 11), IV Explanation of Rate Information, A. Supporting Data and Assumptions

[18] The "explanation" of the actual rate setting process described above in Section III is vague and general. Much more detail, specifics and documentation should be required.

[19] Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Tables 2 and 5

which also is not excessive. The projected administrative expense PMPM for July 2012 to June 2013 is $20.65 compared to an historical value for 2011 of $20.83.[20] That is a total decrease of -0.6%, which is -0.4% on an annual basis.[21]

[20] Exhibit E-1 Att 3 Tables for Jul-12 IFP HMO Rate Filing, Spreadsheet Table 2 "Changes in Administrative Costs"

[21] The time period from January 2011 / December 2011 to July 2012 / June 2013 is 1.5 years. (0.994) ^ (1 / 1.5) = 0.996 = -0.4% annual trend