RICK SNYDER
GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF LICENSING AND REGULATORY AFFAIRS
OFFICE OF FINANCIAL AND INSURANCE REGULATION
R. KEVIN CLINTON
COMMISSIONER

STEVEN H. HILFINGER
DIRECTOR

TRANSMITTED VIA EMAIL

July 28, 2011

The Honorable Kathleen Sebelius
Secretary
U.S. Department of Health and Human Services
200 Independence Avenue, S.W.
Washington, DC 20201

Re: Request for Adjustment of Individual Market Medical Loss Ratio for Michigan

Dear Secretary Sebelius:

Pursuant to Section 2718 of the Public Health Service Act, the State of Michigan hereby submits this request for an adjustment of the 80% minimum medical loss ratio (MLR) requirement for individual health insurance policies issued in Michigan until 2014. The current minimum MLR requirements in Michigan for individual policies are 65% for rated by age and optionally/collectively renewable policies, and 55% for all other policy types. To allow for a smooth transition to the new federal requirements, we propose gradually increasing the MLR over a three year period whereby the MLR for 2011 is 65%, followed by 70% for 2012, and 75% for 2013.

Absent the adjustment, we anticipate significant disruption in the individual health insurance marketplace. The market is dominated by one issuer, Blue Cross Blue Shield of Michigan that already operates at an MLR exceeding the federally mandated 80%. However other commercial carriers have been operating with business models assuming lower minimum MLR requirements and need time to adjust to higher federal standard or be faced with significant rebates that could undermine profitability. Applying the 80% minimum MLR to the 2010 results, fourteen (14) companies would be scheduled to issue rebates totaling $30.6 million, with eight (8) paying rebates in excess of their after-tax profit for 2010.

We appreciate your consideration of our state's request and look forward to receiving your approval.

Best Regards,

R. Kevin Clinton
Commissioner

Enclosures:
Appendices (2)
Exhibits (2)

APPENDIX 1:
Discussion of Michigan Market and Relevant Criteria for Adjustment

Characteristics of the Michigan Individual Health Insurance Market

In Michigan, over 340,000 residents purchase coverage on an individual basis through approximately 70 issuers. Like many other states, most enrollees are covered by a limited number of issuers with the remaining issuers covering niche or regional markets. Blue Cross Blue Shield of Michigan (BCBSM) is the largest writer covering 55% of the individual health population. Including BCBSM, the largest seven writers account for nearly 90% of the state's individual market. The following table shows the number of enrollees and market share for the top seven issuers:

Table 1 – Largest Individual Health Insurance Issuers

Rank	Issuer	Enrollees	Market Share
1	Blue Cross Blue Shield of Michigan	189,503	55.1%
2	Golden Rule Insurance Co. (United Health)	40,104	11.7%
3	Time Insurance Co (Assurant)	21,919	6.4%
4	BCS Life Insurance Co	19,081	5.6%
5	Aetna Life Insurance Co	15,409	4.5%
6	Humana Insurance Co	12,631	3.7%
7	World Insurance Co (American Enterprise)	6,356	1.8%
Total – Largest Issuers (7)		**305,003**	**88.7%**
Other Issuers with > 1,000 Enrollees (13)		32,384	9.4%
Total – Issuers with > 1,000 Enrollees (20)		**337,387**	**98.1%**

Source: Exhibit 2 (from 2010 Supplemental Health Care Exhibits, Individual Comprehensive Health Coverage)

Regulatory Criteria for Adjustment

Title 45 CFR §158.330 lists six criteria that the Secretary may consider "in assessing whether application of an 80 percent MLR...may destabilize the individual market in a State." In an effort to better organize the issues facing the state of Michigan with regard to the new federal MLR regulations, we have described below the characteristics of the market leading to OFIR's decision to request an adjustment for Michigan, with respect to the six criteria under consideration.

(a) Number of Issuers Reasonably Likely to Exit the State

Currently no companies have expressed intent to exit the state or cease offering coverage in the individual health insurance market absent an adjustment to the 80% MLR. However given the magnitude and number of potential rebates, relative to individual and company market profitability, OFIR is concerned about the impact that the potential rebates payable in the next several years will have on the Michigan

market, particularly because the existence of a vibrant insurance market is critical to the success of the proposed Exchange effective in 2014.

While not specific to the MLR regulations, the state has lost two issuers from the individual health market in last couple years. American Community was placed into rehabilitation and subsequently withdrew from the individual and small group markets in March, 2010. MEGA Life and Health decided to discontinue marketing of all of its health plans in Michigan and many other states in September, 2010. According to the Management Discussion and Analysis filed with their 2010 Annual Statement, MEGA's action was driven by and coincided with the implementation of many of the provisions of the Patient Protection and Affordable Care Act of 2010, including but not limited to the minimum MLR requirements. Both American Community and MEGA continue to have policies in force as of December 31, 2010 totaling 1.6% of the individual enrollees.

Two other issuers have recently made decisions to exit or significantly scale back their presence in the small group market. Aetna has exited the small group (2-50 enrollees) market effective February 1, 2011 and Humana has decided to "focus more on selling voluntary workplace specialty benefit programs to employers and Medicare Advantage policies and to de-emphasize commercial products."[1] While the decisions made by these two issuers may alone not destabilize the individual markets, they signal potential concerns on their behalf with the health insurance market in Michigan.

(1) and (2): Impact of Federal MLR Standard on Profitability and Solvency

As mentioned earlier, the greater concern is the magnitude of the indicated rebates for 2011-2013 under the federal 80% MLR standard. Currently, commercial issuers (excluding BCBS and HMOs) are subject to minimum MLRs of 55% or 65% depending upon the renewal type (Mich. Admin. Rule 500.803). Therefore, a change to an 80% MLR would be significant for these issuers. The following table shows the current MLRs for the seven largest issuers, including credibility adjustments as allowed by §§158.230-158.232.

Table 2 – Indicated Individual Medical Loss Ratios based on 2010 Results

Rank	Issuer	MLR Before Credibility Adjustment	Credibility Adjustment	MLR After Credibility Adjustment
1	Blue Cross Blue Shield of Michigan	93.0%	0.0%	93.0%
2	Golden Rule Insurance Co. (United Health)	60.0%	1.4%	61.4%
3	Time Insurance Co (Assurant)	65.0%	1.8%	66.8%
4	BCS Life Insurance Co	84.0%	2.0%	88.0%
5	Aetna Life Insurance Co	70.0%	2.2%	72.2%
6	Humana Insurance Co	70.0%	2.4%	72.4%
7	World Insurance Co (American Enterprise)	52.0%	3.4%	55.4%

Source: Exhibit 2 (from 2010 Supplemental Health Care Exhibits, Individual Comprehensive Health Coverage)

As highlighted above, five of the seven largest issuers would be facing rebates based on their 2010 results. In total, fourteen of the twenty issuers with greater than 1,000 enrollees have indicated rebates.

[1] Crain's Detroit Business, July 30, 2010.

Absent an adjustment to the federal MLR standard, these companies may be forced to lower premiums, increase claims costs, increase expenditures on quality improvement activities, or reduce non-claim related expenses in order to reduce their potential for rebates. Many of these companies will be challenged to lower premium or increase claims and claims related payments without sacrificing profitability below an acceptable level. Many may even cause otherwise profitable business in Michigan to become unprofitable. As a significant component of these non-claim expenses are production related (e.g. agency commissions), many companies will find it difficult to reduce these costs in the short term due to the common practice of multi-year commission agreements. The table below shows the impact of rebates for the top seven issuers:

Table 3 – Estimated Rebates and Impact on After Tax Gains/ (Losses)

Rank	Issuer	Estimated Rebates	Estimated After-Tax Net Gain/ (Loss) Before Rebates - Individual	Estimate After-Tax Net Gain/ (Loss) After Rebates - Individual
1	Blue Cross Blue Shield of Michigan	$0.0	$(56.0)	$(36.8)
2	Golden Rule Insurance Co. (United Health)	9.8	10.0	3.6
3	Time Insurance Co (Assurant)	5.2	1.2	(2.1)
4	BCS Life Insurance Co	0.0	4.5	4.5
5	Aetna Life Insurance Co	1.8	3.2	2.0
6	Humana Insurance Co	1.4	0.0	(0.8)
7	World Insurance Co (American Enterprise)	2.9	0.7	(1.2)
Total – Largest Issuers (7)		**$21.0**	**$(17.2)**	**$(30.9)**
Other Issuers with > 1,000 Enrollees (13)		9.6	4.8	(1.4)
Total – Issuers with > 1,000 Enrollees (20)		30.6	(12.4)	(32.3)
Total - Companies with Indicated Rebates (14)		**$30.6**	**$20.3**	**$0.4**

Source: Exhibit 2 (from 2010 Supplemental Health Care Exhibits, Individual Comprehensive Health Coverage)

Notes:
(1) After-tax gain before rebates are estimated as the sum of underwriting profit plus an allocation of federal income taxes and investment income based the percentage written in the individual market.
(2) Assuming a 35% tax rate, the After-tax gain after rebates = After-tax gain before rebates – 65% x Estimated rebate
(3) Estimated rebates assume the 2010 MLR, number of enrollees, and adjusted premium are applicable to the 2011 year. Any changes to the non-claim expense structure, claims experience, size of insured population, and premium adequacy, among other factors, may cause the estimated rebates to be higher or lower than shown.

The table above illustrates the significance of the indicated rebates under the 80% federal MLR. The profitability of the issuers estimated to issue rebates will be significantly impaired if the 80% federal MLR were applicable. Using 2010 results as a proxy for estimating rebates, fourteen issuers would indicate rebates totaling **$30.6 million**. These same fourteen companies generated an after-tax gain on their individual business of $20.3 million. After adjusting the indicated rebates for taxes, the after-tax gain after payment of rebates would be $0.4 million, effectively eliminating all the profits in the

individual market. Of course capacity in the individual marketplace is determined at the individual company level. Of the fourteen companies with indicated rebates, nine would face rebates in excess of their after-tax gain. If companies are unable to adjust their business practices to meet the higher MLR requirement, they may be faced with the decision to significantly reduce their writings or exit altogether the individual health market in Michigan. Depending on the size of the companies choosing to exit, this may have a significant destabilizing effect on the market unless the remaining issuers are willing to absorb the non-renewed business.

Finally, with respect to the solvency, it is difficult to determine the impact on surplus of these rebates. However all issuers currently have RBC ratios in excess of 2.5:1 with most having ratios in excess of 5:1. One would need to calculate the indicated rebates for all states to measure the impact that an adjustment in Michigan would have on the solvency ratios.

(3) Withdrawal Requirements and Limitations

Michigan has no specific withdrawal requirements if an issuer chooses to leave the state.

(b) Enrollee Impact of Exiting (Exited) Companies

Although no companies have indicated plans to exit the individual health market, two companies have recently chosen to exit the market for other reasons (MEGA, American Community). Together these companies insure 5,357 residents as of December 31, 2010. Absent a change to the MLR requirements, however, OFIR believes there is a reasonably high likelihood that some or all of the eight companies facing an after-tax loss after the payment of rebates will consider leaving or significantly reducing their writings in the state.

(c) Access to Agents and Brokers

OFIR believes that it is inevitable that agents' commissions will be reduced by issuers looking to lower non-claim related expenses to comply with the new MLR requirements. This may lead to fewer qualified agents being available to consumers needing to purchase individual and small group health insurance. In addition to reasons cited above with respect to issuers, we believe an adjustment will allow agents time to adjust their own business practices in recognition of the lower commission environment.

(d) Alternate Coverage Options

Michigan has several options available to consumers in the event an insurer withdraws from the market. BCBSM, HMOs, and the Health Insurance Program for Michigan all have guarantee issue requirements assuming you meet certain requirements. Additional details can be found in Appendix 2 under the response to §158.321(c).

(d) Impact on Premiums, Benefits and Cost-Sharing of Remaining Issuers

As it is difficult to identify which companies, if any, would choose to leave the market, evaluating the impact on premium costs and benefit features available on the remaining plans would be equally challenging. Certainly, if one of the larger issuers chooses to leave the market the number of coverage options available to individuals will decrease dramatically.

(e) Other Relevant Information Submitted by State

Michigan's request for an adjustment of the federal MLR requirements applicable to individual health insurance constitutes a phase-in approach whereby the MLR for 2011 would be 65%, followed by 70% for 2012, and 75% for 2013.

This approach does not simply postpone the payment of rebates until 2014. Rather, it allows companies to issue more manageable rebates over the next several years to minimize the likelihood that companies will realize significant losses in the short term, and to allow time for them to adjust their business practices to reflect the higher MLR requirements.

Per §158.323(c) and (d), we have provided the amount of rebates to be paid under both the current 80% MLR requirement and the proposed phase-in approach. Detail for the individual companies is shown below:

Table 4 – Impact of Proposed Phase-In MLR for Michigan ($Millions)

Rank	Issuer	2011		2012		2013	
		80% MLR	65% MLR	80% MLR	70% MLR	80% MLR	75% MLR
1	BCBS of MI	$0.0	$0.0	$0.0	$0.0	$0.0	$0.0
2	Golden Rule	9.8	1.9	10.5	5.3	10.5	7.9
3	Time	5.2	0.0	5.4	1.4	5.7	3.7
4	BCS Life	0.0	0.0	0.0	0.0	0.0	0.0
5	Aetna Life	1.8	0.0	1.9	0.0	2.0	0.9
6	Humana	1.4	0.0	1.5	0.0	1.5	0.6
7	World Life	2.9	1.1	3.0	1.8	3.1	2.5
Largest Issuers (7)		**$21.0**	**$3.0**	**$22.3**	**$8.5**	**$22.8**	**$15.6**
Other Issuers (13)		**9.6**	**2.6**	**10.6**	**5.4**	**10.9**	**8.2**
Total Issuers (20)		**$30.6**	**$5.6**	**$32.9**	**$13.9**	**$33.7**	**$23.8**

Note:
(1) Estimated rebates assume the 2010 MLR, number of enrollees, and adjusted premium are applicable to the 2011-2013 years. Any changes to the non-claim expense structure, claims experience, size of insured population, and premium adequacy, among other factors, may cause the estimated rebates to be higher or lower than shown.

APPENDIX 2:
Requested Information per §§158.321-158.323 on Michigan's Individual Health Insurance Market

§158.321 Information regarding the State's individual health insurance market

(a) State MLR standard. The State must describe its current MLR standard for the individual market, if any, and the formula used to assess compliance with such standard.

Commercial insurers offering individual health insurance policies in Michigan have been subject to the following minimum anticipated loss ratios in their prospective rates since 1979 (Mich. Admin. Rule 500.803):

(a) 65% percent for rated by age insurance.
(b) 65% for collectively renewable insurance or optionally renewable insurance.
(c) 55% for guaranteed renewable insurance or nonrenewable for stated reasons only insurance.
(d) 55% for non-cancellable insurance, non-cancellable, and guaranteed renewable insurance or individual accident insurance.
(e) 55% percent for all other insurance.

The minimum anticipated loss ratio is calculated as the ratio of the present value of all expected future benefits, excluding dividends, to the present value of all future premiums, less dividends, based on a credible premium volume over a reasonable period of time with proper weight given to trends and other relevant factors.

The above regulations regarding MLRs are not applicable to non-profit health care corporations (e.g. Blue Cross Blue Shield) and HMOs.

(b) State market withdrawal requirements. The State must describe any requirements it has with respect to withdrawals from the State's individual health insurance market. Such requirements include, but are not limited to, any notice that must be provided and any authority the State regulator may have to approve a withdrawal plan or ensure that enrollees of the exiting issuer have continuing coverage, as well as any penalties or sanctions that may be levied upon exit or limitations on re-entry.

Michigan has no statutes or rules governing insurer withdrawal from the state.

(c) Mechanisms to provide options to consumers. The State must describe the mechanisms available to the State to provide consumers with options in the event an issuer withdraws from the individual market. Such mechanisms include, but are not limited to, a guaranteed issue requirement, limits on health status rating, an issuer of last resort, or a State operated high risk pool. A description of each mechanism should include detail on the issuers participating in and products available under such mechanism, as well as any limitations with respect to eligibility, enrollment period, total enrollment, and coverage for pre-existing conditions.

Michigan has several options available to consumers in the event an insurer withdraws from the market. By statute, Blue Cross Blue Shield of Michigan (BCBSM) must provide health insurance coverage to any applicant who is a Michigan resident (MCL 550.1401(1)). HMOs have a similar requirement after 24 months of operation. All HMOs must have a 30 day enrollment period every 12 months during which time it offers individual policies on a guaranteed issue basis up to its capacity (as approved by the

Commissioner). Both BCBSM and HMOs are allowed to impose pre-existing condition exclusions for individuals (non-group) for the first 6 months of coverage.

The state has also created a temporary high-risk pool called Health Insurance Program for Michigan (HIP, http://www.hipmichigan.com) administered by Physicians Health Plan of Michigan. Individuals must have been without insurance for 6 months or more and been denied or offered restricted coverage due to pre-existing conditions in order to be covered by HIP.

(d) Issuers in the State's individual market. Subject to §158.320 of this subpart, the State must provide:

(1) For each issuer who offers coverage in the individual market in the State its number of individual enrollees by product, available individual premium data by product, and individual health insurance market share within the State;

(2) For each issuer who offers coverage in the individual market in the State to more than 1,000 enrollees, the following additional information:

- **(i) Total earned premium on individual market health insurance products in the State;**
- **(ii) Reported MLR pursuant to State law for the individual market business in the State;**
- **(iii) Estimated MLR for the individual market business in the State, as determined in accordance with §158.221 of this part;**
- **(iv) Total agents' and brokers' commission expenses on individual health insurance products;**
- **(v) Estimated rebate for the individual market business in the State, as determined in accordance with §158.221 and §158.240 of this part;**
- **(vi) Net underwriting profit for the individual market business and consolidated business in the State;**
- **(vii) After-tax profit and profit margin for the individual market business and consolidated business in the State;**
- **(viii) Risk-based capital level; and**
- **(ix) Whether the issuer has provided notice of exit to the State's insurance commissioner, superintendent, or comparable State authority.**

The attached Exhibits 1 and 2 provide the requested data with the exception of item 2(ii). Companies comply with the state MLR requirements by submitting rates that meet the minimum MLR threshold as certified by an actuary. Retrospective tests are neither requested nor performed by the insurance department. Also, as the state of Michigan does not collect information by product type, our response to item (1) the requested information at the company level as provided in the 2010 Supplemental Health Care Exhibit.

§158.322 Proposal for adjusted medical loss ratio. A State must provide its own proposal as to the adjustment it seeks to the MLR standard.

Michigan proposes a phased-in approach to the 80% MLR standard whereby the MLR would start at the current level for age rated and optionally/collectively renewable (65%) then transition to 70% for 2012 and 75% for 2013.

This proposal must include:
(a) An explanation and justification of how the proposed adjustment to the MLR was determined;

The proposed MLR adjustment represents a bridge between the current state MLR requirements of 55-65% to the new federal MLR of 80%. We believe that three years represents a reasonable timeframe to allow companies to adjust their business practices to meet the 80% MLR level by 2014 as the magnitude of the rebates relative to the company's profits is significant.

(b) An explanation of how an adjustment to the MLR standard for the State's individual market will permit issuers to adjust current business models and practices in order to meet an 80 percent MLR as soon as is practicable;

Most commercial health insurers in Michigan support an MLR adjustment for the transition period. Companies have been operating under the current statutory MLR requirement of 55% or 65% and the immediate imposition of the 80% MLR will cause many markets to refund profits that were never generated. Further, many of these companies enter into multi year agency agreements making it difficult to quickly adjust a significant component of their cost structure. Agents represent a valuable resource for insureds to assist them in evaluating the numerous and complex health care options. Consumers would find themselves challenged to identify the appropriate health care insurance for their family without adequate representation.

In addition, the imposition of the new MLR statute could present additional challenges for smaller companies who, because of their scale, cannot operate efficiently enough to meet the 80% minimum MLR and still generate a reasonable profit. We want to encourage health insurers to continue offering individual policies in Michigan to ensure a broad selection of products and features available to consumers as part of the state health insurance exchange effective in 2014.

(c) An estimate of the rebates that would be paid if the issuers offering coverage in the individual market in the State must meet an 80 percent MLR for the applicable MLR reporting years;

2011	80%	$30.6 million
2012	80%	$32.9 million
2013	80%	$33.7 million

These estimates assume no change in earned premium, benefit payments, and cost structure during the three year period.

(d) An estimate of the rebates that would be paid if the issuers offering coverage in the individual market in the State must meet the adjusted MLR proposed by the State for the applicable MLR reporting years.

2011	65%	$5.6 million
2012	70%	$13.9 million
2013	75%	$23.8 million

The estimates assume no change in earned premium, benefit payments, and cost structure during the three year period.

§158.323 State contact information.
A State must provide the name, telephone number, e-mail address, and mailing address of the person the Secretary may contact regarding the request for an adjustment to the MLR standard.

Kevin M. Dyke
Office of Financial and Insurance Regulation

State of Michigan
611 West Ottawa, 3rd Floor
Lansing, MI 48933
phone: (517) 335-1144
email: dykek1@michigan.gov