Report of 2000 Loss Ratio Experience in the Individual and Small Employer Health Plan Markets for Insurance Companies and Nonprofit Health Service Plan Corporations

June, 2001

Minnesota Department of Commerce

Table of Contents

Legislative Request for Report

The 1997 Minnesota Legislature passed a law requiring the Commissioners of Commerce and Health to issue a report listing loss ratios for the individual and small group health plan markets. The text of the law appears below:

> **S.F 1208 Article 2, Section 2(g)** The commissioners of commerce and health shall each annually issue a public report listing, by health plan company, the actual loss ratios experienced in the individual and small employer markets in this state by the health plan companies that the commissioners respectively regulate. The commissioners shall coordinate release of these reports so as to release them as a joint report or as separate reports issued the same day. The report or reports shall be released no later than June 1 for loss ratios experienced for the preceding calendar year. Health plan companies shall provide to the commissioners any information requested by the commissioners for purposes of this paragraph.

Background on the Markets

Roughly 10 percent of the population receives coverage through a small group, while 4.8 percent of the population purchases individual coverage. Of the remainder, 58 percent of the population receives coverage through a large group, 23 percent receives coverage through public programs, and 5 percent is uninsured. Recently claim cost levels have increased significantly for most health plan companies, leading to higher rate increases for small employer and individual health plans. Many large employers have moved from fully-insured health plans into self-insured plans, which allow them to reduce cost while having more control over their employee benefits. Self-insured plans are not subject to state benefit mandates or state premium taxes and assessments. This option is not generally available to small employers, because they do not usually have the financial resources to accept the risk of large claims.

How to Use the Data

In order to use the loss ratio data for a specific purpose, it is important to find out additional information relevant to that purpose. As discussed below, loss ratios may not be a good way to compare health plan companies, unless other information is taken into account.

For example, when the Commerce Department reviews health plan rates for compliance with statutory requirements, we ask for additional information to evaluate the rates, including (1) how the loss ratio has been calculated, (2) the benefits that will be offered, (3) any recent changes in rates or benefits, (4) national experience when Minnesota experience is not very credible, (5) an analysis of the relative newness of the experience, and (6) any other information that will help evaluate whether rates will meet the statutory requirements.

Definition of Loss Ratio

Background

The first report appeared in June, 1998 for 1997 experience. Due to the short lead time for preparing the first report, the Department did not provide detailed guidance for the calculation of the earned premiums and incurred claims. The Department has developed detailed guidance and a technical list of what is included in the loss ratio calculation required by law. This list appears below.

Data Requested

Companies were asked to provide the total earned premium, incurred claims, and loss ratio for the year ending December 31, 2000, separately for the individual and small employer health plan markets. The small employer market includes non-compliant small employer plans that have been treated as part of the small employer block of business. The small employer market does not include employers with 51 or more employees, even if fewer than 51 employees from a group have enrolled for health plan coverage.

The individual market includes individual policies issued as conversions from group health plan coverage. If a company has conversion policies in force, but no other individual health plan business, it need not report data for the individual market.

Earned Premium

Premium earned during 2000, without adjusting for any payments to the Minnesota Health Care Reinsurance Association (MHCRA) or private reinsurance arrangements. Earned premiums are equal to paid premium for the year plus uncollected premiums minus premiums paid in advance. The number should be based on the most recent available estimates of the premium-related accrual amounts. The number includes any fees from policyholders such as enrollment fees, monthly fees, or processing fees. The number should be calculated without subtracting any commissions or marketing expenses from the premiums. Premiums do not include any payments for Administrative Services Only (ASO) contracts or any fee-for-service income that was given on a non-insured basis to medical care providers.

Incurred Claims

Incurred claims include the paid-on-incurred claims for the year, plus a reserve for claims incurred but not yet paid, plus the change in any other claim reserves held (such as active life reserves or rate stabilization reserves), plus the expenses incurred during the year for the following items, where expenses for a functional area should include allocated costs such as EDP equipment, office space, management, overhead, and so on.

- Any accrued expected value of withholds, bonuses, or other amounts to be paid to providers for services provided in 2000.
- Any accrued prescription drug rebates or refunds from pharmaceutical companies (a reduction to the claims).
- Case management activities.
- Capitations paid or accrued to providers for claims incurred during 2000.
- Clinical quality assurance and other types of medical care quality improvement efforts.
- Concurrent or prospective utilization review as defined in Minnesota Statutes, section 62M.02, subdivision 20.

- Consumer education solely for health improvement.
- Detection and prevention of payment for fraudulent requests for reimbursement.
- Net reinsurance cost (premiums less claims) for the MHCRA and private reinsurance, and assessments by MHCRA.
- Network access fees to Preferred Provider Organizations and other network-based health plans.
- Provider contracting and credentialing costs.
- Provider tax required by Minnesota Rules, part 295.52.

Loss Ratio

The ratio of incurred claims to earned premiums.

Unintentional Errors

The earned premiums, incurred claims, and loss ratios that are listed in this report have been provided by the health plan companies. We have not independently verified the loss ratios, and even the most careful process will sometimes include unintentional errors.

Calculation Methods

There are different ways of calculating a loss ratio, depending on the accounting method used for calculating earned premiums and incurred claims. One method is used for the annual statement, and includes estimates of premiums and claims that have not yet been recorded, and also includes changes in the estimates for the previous year. Another method is commonly used for setting and filing rates. This method restates the earned premium and incurred claims using the most recent information, and does not incorporate adjustments from previous periods. For this report, we have asked the health plan companies to provide loss ratios using the second method.

Loss Ratio is not the Same as Value

The Minnesota Legislature has passed laws requiring health plans to set their rates so as to meet minimum loss ratio standards because the loss ratio is a way to measure value. The loss ratio is a good measure of relative value if two health plan companies are very similar in the benefits they provide and other factors. In that case, the plan with the higher loss ratio would be a better value.

However, health plan companies differ in a variety of ways, and therefore the relative loss ratio is not always indicative of relative value. For example, one health plan company may not spend much effort preventing payment of fraudulent claims, while another may spend much more time and money, resulting in non-payment of many fraudulent claims. The first company would have a higher loss ratio due to the fraudulent claims it paid, but that would not be a value to the honest policyholders. Similarly, one health plan company may pay doctors and hospitals at a higher charge level than another, due to different contractual arrangements. Those higher payments do not represent greater value to the policyholder.

Also, every prospective policyholder is different, with different needs for health care. In order to compare health plan companies, it is necessary to review other aspects of the company affecting value, such as availability of particular medical care providers, quality of patient service, and quality of care management.

Statistical Fluctuation

Loss ratios also are subject to statistical fluctuation. Each individual's health care costs are more or less unpredictable, and the total incurred claims of a health plan company are also more or less unpredictable. Having a high or low loss ratio may have been due to such fluctuations, and may not be repeated in a future time period.

Recent Changes

Any change that has been made in a health plan company's business since the beginning of the reporting period also affects the loss ratio. For example, the rate levels or benefits offered may have changed significantly, due to legislative requirements or improvements offered by the health plan company.

Newness of Coverage

The newness of the health plans also has an effect on the loss ratio. Policies that have been recently sold typically have lower levels of claims than policies that have been in force for a year or more. Thus a health plan company may have a relatively low loss ratio, due to a large proportion of relatively new policies, but their expected future loss ratio may not be low.

How Rates are Regulated

Minnesota Statutes, section 62A.02, requires all health plan rates to be approved by the Commissioner of Commerce (for HMOs, the Commissioner of Health) before being used. The health plan company must supply actuarial reasons and data demonstrating that the benefits are reasonable in relation to the premiums. The Commerce Department reviews all rates to verify reasonableness and compliance with other statutory limitations such as rate bands. Rate restrictions for small employer plans are specified in Minnesota Statutes, section 62L.08, and for individual plans are specified in Minnesota Statutes, section 62A.65.

Loss Ratio Standards After 1997 Changes

In addition to being reasonable and meeting rate restrictions, individual and small employer health plan rates must be calculated to meet specific minimum loss ratio standards in Minnesota Statutes, section 62A.021.

A health plan company that has at least 3% of the total health plan market (individual, small employer, and large employer) in Minnesota must meet a loss ratio standard that increased each July 1, from 1994 to 2000. The minimum loss ratio for individual health plans for rates to be used on and after July 1, 2000 is 72%. For small employer plans it is 82%.

A health plan company that has less than 3% of the market must meet fixed minimum loss ratios (specified in a law that was passed in 1997). Those minimums are 68% for individual health plans, 71% for small employer plans with 10 or fewer employees, and 75% for small employer plans with 11 or more employees.

Individual Health Plan Loss Ratios

The following page lists the loss ratios experienced in the individual health plan market in 2000 by companies that cover policyholders in that market. Not all companies with individual health plans in force are included, as some did not respond to our request for information, and some had premium volume lower than $100,000, which we considered too low to include. Page 8 contains a list in order by decreasing premium volume of the companies that responded, and Page 9 contains an alphabetical list.

The loss ratios for 2000 ranged from 29% to 263%. The total loss ratio for 2000 is 95%, higher than the 88% total loss ratio from last year.

The lowest loss ratios are usually on small, non-credible blocks of business. The highest loss ratios are usually on blocks of business that are primarily polices used as the mandated portability option required by Minnesota Statutes, section 62A.65, subdivision 5(b), for insured persons formerly covered in group health plans who have exhausted the mandated continuation coverage.

Questions about this information may be addressed to Melane Milbert at the Minnesota Department of Commerce, 85 Seventh Place East, Suite 500, St Paul, MN 55101. Phone number: (651) 282-5605

Premium Order List for Individual

Company	Premiums	Claims	Loss Ratio
BCBSM, Inc.	$ 142,687,685	$ 130,037,682	91%
Fortis Insurance Company	$ 30,078,582	$ 28,335,464	94%
State Farm Mutual Automobile Insurance Company	$ 13,380,803	$ 14,991,587	112%
World Insurance Company	$ 11,450,694	$ 9,958,113	87%
American Family Mutual Insurance Company	$ 6,178,918	$ 5,596,818	91%
Golden Rule Insurance Company	$ 4,690,439	$ 3,935,745	84%
Mutual of Omaha Insurance Company	$ 3,509,895	$ 2,775,195	79%
Pioneer Life Insurance Company	$ 2,831,200	$ 2,631,700	93%
Medica Insurance Company	$ 2,273,351	$ 3,230,077	142%
Aid Association for Lutherans	$ 2,002,138	$ 4,303,598	215%
Principal Life Insurance Company	$ 1,367,986	$ 2,742,270	200%
American Fidelity Assurance Company	$ 1,228,325	$ 360,928	29%
Trustmark Insurance Company	$ 1,145,001	$ 1,615,658	141%
United Teacher Associates Insurance Company	$ 1,076,334	$ 1,053,771	98%
General American Life Insurance Company	$ 348,516	$ 156,976	45%
Prudential Insurance Company of America (The)	$ 269,860	$ 709,808	263%
Alta Health and Life Insurance Company	$ 182,149	$ 137,326	75%
National Travelers Life Company	$ 181,501	$ 281,539	155%
Lutheran Brotherhood	$ 131,360	$ 145,288	111%
John Alden Life Insurance Company	$ 129,943	$ 65,779	51%
The Guardian Life Insurance Company	$ 61,205	$ 113,553	186%
Total	$ 225,205,885	$ 213,178,875	95%

Alphabetic List for Individual

Company	Premiums	Claims	Loss Ratio
Aid Association for Lutherans	$ 2,002,138	$ 4,303,598	215%
Alta Health and Life Insurance Company	$ 182,149	$ 137,326	75%
American Family Mutual Insurance Company	$ 6,178,918	$ 5,596,818	91%
American Fidelity Assurance Company	$ 1,228,325	$ 360,928	29%
BCBSM, Inc.	$ 142,687,685	$ 130,037,682	91%
Fortis Insurance Company	$ 30,078,582	$ 28,335,464	94%
General American Life Insurance Company	$ 348,516	$ 156,976	45%
Golden Rule Insurance Company	$ 4,690,439	$ 3,935,745	84%
The Guardian Life Insurance Company	$ 61,205	$ 113,553	186%
John Alden Life Insurance Company	$ 129,943	$ 65,779	51%
Lutheran Brotherhood	$ 131,360	$ 145,288	111%
Medica Insurance Company	$ 2,273,351	$ 3,230,077	142%
Mutual of Omaha Insurance Company	$ 3,509,895	$ 2,775,195	79%
National Travelers Life Company	$ 181,501	$ 281,539	155%
Pioneer Life Insurance Company	$ 2,831,200	$ 2,631,700	93%
Principal Life Insurance Company	$ 1,367,986	$ 2,742,270	200%
Prudential Insurance Company of America (The)	$ 269,860	$ 709,808	263%
State Farm Mutual Automobile Insurance Company	$ 13,380,803	$ 14,991,587	112%
Trustmark Insurance Company	$ 1,145,001	$ 1,615,658	141%
United Teacher Associates Insurance Company	$ 1,076,334	$ 1,053,771	98%
World Insurance Company	$ 11,450,694	$ 9,958,113	87%
Total	$ 225,205,885	$ 213,178,875	95%

Small Employer Health Plan Loss Ratios

The following pages list the loss ratios experienced in the small employer health plan market in 2000 by companies that cover policyholders in that market. Not all companies with small employer health plans in force are included, as some did not respond to our request for information. Page 11 contains a list in order by decreasing premium volume of the companies that responded, and Page 12 contains an alphabetical list.

The loss ratios for 2000 ranged from 65% to 111%. The total loss ratio for the market as reported is 90%, which represents a loss to the health plan companies to the extent that their expenses exceed 10% of premium. Typical health plan company expenses for small employer health plans range from 20% to 35% of premium, so the 2000 experience represents a year in which the small employer market was generally unprofitable for health plan companies.

Questions about this information may be addressed to Melane Milbert at the Minnesota Department of Commerce, 85 Seventh Place East, Suite 500, St Paul, MN 55101. Phone number: (651) 282-5605

Premium Order List for Small Employer

Company	Premiums	Claims	Loss Ratio
BCBSM, Inc.	$ 400,527,407	$ 361,414,664	90%
Medica Insurance Company	$ 71,346,315	$ 58,738,856	82%
Federated Mutual Insurance Company	$ 30,158,362	$ 25,461,126	84%
Principal Life Insurance Company	$ 29,698,768	$ 27,178,800	92%
Fortis Insurance Company	$ 10,696,347	$ 10,698,836	100%
John Alden Life Insurance Company	$ 9,843,759	$ 9,343,181	95%
General American Life Insurance Company	$ 8,098,312	$ 8,523,558	105%
Fortis Benefits Insurance Company	$ 3,960,884	$ 4,398,313	111%
United Wisconsin Insurance Company	$ 2,132,183	$ 1,598,878	75%
EPIC Life Insurance Company (The)	$ 1,352,360	$ 1,393,456	103%
Sentry Insurance Company	$ 1,285,301	$ 1,253,012	97%
Guardian Life Insurance Company of America (The)	$ 989,651	$ 927,006	94%
Trustmark Insurance Company	$ 536,127	$ 347,644	65%
Total	$ 570,625,776	$ 511,277,330	90%

Alphabetic List for Small Employer

Company	Premiums	Claims	Loss Ratio
BCBSM, Inc.	$ 400,527,407	$ 361,414,664	90%
EPIC Life Insurance Company (The)	$ 1,352,360	$ 1,393,456	103%
Federated Mutual Insurance Company	$ 30,158,362	$ 25,461,126	84%
Fortis Benefits Insurance Company	$ 3,960,884	$ 4,398,313	111%
Fortis Insurance Company	$ 10,696,347	$ 10,698,836	100%
General American Life Insurance Company	$ 8,098,312	$ 8,523,558	105%
Guardian Life Insurance Company of America (The)	$ 989,651	$ 927,006	94%
John Alden Life Insurance Company	$ 9,843,759	$ 9,343,181	95%
Medica Insurance Company	$ 71,346,315	$ 58,738,856	82%
Principal Life Insurance Company	$ 29,698,768	$ 27,178,800	92%
Sentry Insurance Company	$ 1,285,301	$ 1,253,012	97%
Trustmark Insurance Company	$ 536,127	$ 347,644	65%
United Wisconsin Insurance Company	$ 2,132,183	$ 1,598,878	75%
Total	$ 570,625,776	$ 511,277,330	90%