

**STATE OF MICHIGAN
DEPARTMENT OF ENERGY, LABOR & ECONOMIC GROWTH
OFFICE OF FINANCIAL AND INSURANCE REGULATION**

Before the Commissioner of the Office of Financial and Insurance Regulation

In the matter of:

Order No. 09-041-BC

**BCBSM Request for Interim Rates for
Other Than Group Medicare Supplemental Subscribers**

**Issued and entered
this 12th day of August, 2009
by Ken Ross
Commissioner**

**ORDER GRANTING INTERIM RATES
IN THE MATTER OF
BCBSM OTHER THAN GROUP
MEDICARE SUPPLEMENTAL SUBSCRIBERS**

On June 3, 2009 a Notice of Hearing and Order for Hearing were issued in the matter of the request of Blue Cross and Blue Shield of Michigan (BCBSM) for rate increases for its Nongroup, Group Conversion and Other Than Group Medicare Supplemental (Medigap) lines of business. Both the Attorney General and the Office of Financial and Insurance Regulation (OFIR) Staff (Staff) have been admitted as additional parties.

On June 17, 2009 BCBSM filed a request for interim rates for those lines to be effective August 1, 2009 and to remain in effect until final rates are approved. Due to a more favorable trend experience based upon updated data, for Nongroup subscribers, BCBSM has requested an interim rate increase of 44.4% instead of the 56% increase sought in the original filing. For Group Conversion subscribers, BCBSM seeks an interim rate increase of 28.82% instead of the 39.2% originally sought. For Medigap subscribers, BCBSM seeks a 31.2% interim rate increase, an increase identical to its original request.

OFIR Staff argue that the Medigap interim rate increase granted to BCBSM should not exceed 1.6%. The Staff argues that updated data through the third quarter of 2008 results in a trend adjustment that reduces the Medigap rate increase, as calculated by BCBSM, from 31.2% to 27.7%. The Staff additionally argues that an application of the full 1% subsidy, authorized by statute and previously ordered by the Commissioner, will have the effect of reducing the rate increase needed to 1.6%. BCBSM disputes the staff trend calculations.

The Attorney General argues that the expedited rate hearing process previously ordered by this office for the main rate case now alleviates the need for an interim rate increase. The Attorney General also argues that interim rate relief is unwarranted where BCBSM's filing shows that it has not collected the full statutory subsidy which could substantially reduce the need for any rate

increase for Medigap subscribers and in light of questions concerning the appropriate trends and claims experience relied upon by BCBSM to justify its request.

A. Interim Rate Standard

MCL 550.1614(2) provides:

The commissioner shall grant an interim rate, in an amount as determined by the commissioner, if the commissioner makes a finding that the corporation has made a convincing showing that there is probable cause to believe that the failure to grant the interim rate will result in an underwriting loss for that line of business for the period for which rates are being requested. As used in this subsection, “underwriting loss” means the difference between income from current rates plus investment income, and projected claims plus projected administrative expenses.

B. Medigap Cost Transfer

MCL 550.1609(5) provides that “there may be cost transfers for the benefit of senior citizens and group conversion subscribers.” This section further provides that the cost transfers, or subsidies, for the benefit of senior citizens “in the aggregate, annually shall not exceed 1% of the earned subscription income of the health care corporation as reported in the most recent annual statement of the corporation.” The proper calculation of the Medigap cost transfer, together with the corresponding total subsidy amount, has a tremendous impact on the appropriate Medigap final rate increase. Prior OFIR Commissioners have set the amount of the Medigap cost transfer at the full 1% permitted by the statute in recognition of the statutory language and the “critical importance of both health care coverage and affordable rates” to Michigan’s senior citizens and the unique role BCBSM plays in providing both. [See December 21, 1992 Final Decision, Case No. 91-11806-BC, p 5; *Id.* July 7, 1998 Proposal for Decision, Docket No. 97-0514, Insurance Bureau Case No. 97-092- R (re: BCBSM’s April 7, 1997 Medigap rate filing), p 42 (“The Insurance Bureau points out that the cost transfer for the benefit of senior citizens is at a maximum level permitted by the Act.”).]

BCBSM argues that the subsidy should not be calculated on its total earned subscription income, but only on part of that income. In particular, BCBSM argues that the subsidy should not be calculated based upon income from administrative services contracts (ASC) because certain ASC contracts do not include a provision to contribute to the subsidy. BCBSM’s Medigap interim rate request applies a subsidy totaling only \$113.1 million, which it calculates by “carving out” various business revenues and by including only amounts that it expects to collect from ASC customers.

A series of prior Commissioner orders have expressly rejected BCBSM’s “uncollected subsidy” arguments and have held that BCBSM must calculate the subsidy based upon 1% of its total subscription income as reported in its most recent Annual Statement. [See December 21, 1992 Final Decision, Case No. 91-11806-BC, p 23 (“The cost transfer must be calculated as a percentage of earned subscription income reported in the most recent annual statement, not as a percentage of that portion of BCBSM’s subscription income that is received from customers who pay the cost transfer.”); *Id.* at p 24 (“The fact that BCBSM is experiencing difficulty collecting the cost transfer from ASC customers is not sufficient justification for a smaller cost transfer

percentage.”); *Id.* (“It is BCBSM’s obligation to pursue the collection of cost transfers from its ASC customers.”).]

According to BCBSM’s 2008 Annual Statement, its total subscription revenue was \$18,153,967,211. As BCBSM explains in its response to the Staff’s position, the term “earned subscription income” is not defined in the BCBSM enabling legislation, 1980 PA 350 and does not occur on the annual financial statement. When P.A. 350 was drafted, BCBSM’s self-funded business was virtually nonexistent and according to the accounting rules in place at that time, any ASC income BCBSM received was included with underwritten premiums in BCBSM’s financial statement. It was the line in the statement that included these amounts against which the 1% subsidy was calculated. Subsequent changes to accounting rules required BCBSM to separate its underwritten premium from ASC premium. Only underwritten premium is now reported on the line in the statement that previously included both sources of income. BCBSM continues to identify its self-funded income in a footnote to the financial statement even though it is no longer reported with net premium income. Despite this change, it is clear that both the statute and the subsequent Commissioner orders implementing the statute have intended that the subsidy be calculated on total subscription/premium income regardless of what it is called, from where it came or where it is reported.

As the Commissioner noted in 1992, “BCBSM’s tax exempt status benefits the ASC customers just as it benefits BCBSM’s other lines. It is not unreasonable to expect that in return for such benefits, the ASC customers contribute a cost transfer to foster the affordability of health care coverage of our State’s elderly.” [See December 21, 1992 Final Decision, Case No. 91-11806-BC, p 5.]

One-percent of BCBSM total subscription/premium income is \$181,539,672. Regardless of the mechanism that BCBSM has chosen to recoup this amount from its other customers, and regardless of whether BCBSM’s chosen mechanism has been effective, \$181,539,672 is the proper amount of the Medigap cost transfer that must be applied and used in determining the interim rate increase resulting from BCBSM’s January 30, 2009 Medigap rate filing and June 17, 2009 interim rate request. By applying the correct Medigap subsidy amount of \$181 million, the interim rate increase needed for BCBSM’s Medigap business line is reduced from the 31.2% requested to 5.1%.

C. Trend Adjustment

There is considerable disagreement between the parties concerning the appropriate trend projection. A review of the information presented by BCBSM provides convincing support, for the purpose of this interim rate request, that losses will continue. The staff has similarly made a plausible case that the BCBSM trend is inappropriately high and downward adjustment is appropriate.

D. Conclusion

Applying the correct Medigap subsidy amount results in a substantial reduction of the proposed interim rate increase. BCBSM has made, however, a convincing showing that there is probable cause to believe that the failure to grant a reasonable interim rate will result in a Medigap underwriting loss. Because rate making is an exercise in future projection, reasonable disputes may arise over anticipated trend development, as those projections are based upon both past

experience and future expectations. The accuracy of both have yet to be explored and presumably will be thoroughly scrutinized during the contested rate hearing.

The determinations made here are for purposes of deciding the interim rate request for Medigap subscribers only. (The parties reached a negotiated settlement regarding final rates for Nongroup and Group Conversion subscribers and a Final Order has been issued setting those rates.) Regarding BCBSM's request for final rates for Medigap subscribers, any and all factual and legal arguments may be made by the parties in the rate hearing. The Independent Hearing Officer is, of course, free to make her own analysis and conclusions on these issues in her Proposal for Decision. Moreover, the Commissioner will, himself, in addressing these issues in the Final Decision following the Proposal for Decision, ground his decision in the factual record and the arguments presented.

THEREFORE, IT IS ORDERED that

1. BCBSM is authorized to implement interim rates generating an overall 4.7% increase for its Other Than Group Medicare Supplemental (Medigap) line of business;
2. BCBSM shall implement cost transfers such that the overall increase in rates billed for this coverage shall not exceed a 4.7% increase;
3. BCBSM shall compile a schedule with respect to the rate increases for both High and Low Options and shall submit that schedule for Commissioner approval;
4. BCBSM shall not bill its underwritten business for more than its share of cost transfers based upon its percentage of earned subscription income reported in BCBSM's 2008 annual statement.

A handwritten signature in black ink, appearing to be 'KR' with a long horizontal stroke extending to the right.

Ken Ross
Commissioner