Milliman

1550 Liberty Ridge Drive, Suite 200
Wayne, PA 19087-5572
Tel + 610 687.5644
Fax + 610 687.4236
www.milliman.com

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Jeanne Kennedy
Vice President and Treasurer
CareFirst BlueCross BlueShield
10455 Mill Run Circle
Mail Stop 01-700
Owings Mills, MD 21117-5559

Re: Response to DISB October 3, 2014 Order with Supplemental Information Requests

Dear Jeanne:

This material is provided in response to Items 1.a, 1.b, and 1.c of the *Order with Supplemental Information Requests (Order No. 14-MIE-008)* issued by Acting Commissioner Chester A. McPherson of the District of Columbia Department of Insurance, Securities and Banking (DISB), dated October 3, 2014. This request relates to the modeling approach that Milliman utilized in carrying out our target surplus analysis for GHMSI in 2011 and, specifically, the modified modeling approach ("Modified Milliman Model") that was carried out at the request of Rector & Associates in connection with their December 9, 2013 report titled *"Report to the DC Department of Insurance, Securities and Banking; Group Hospitalization and Medical Services, Inc."*

The referenced DISB order requests that Milliman provide to Rector & Associates (with a copy to DISB) the calculated surplus targets generated by a series of specified assumptions as to confidence levels and assumed growth rates, based on the Modified Milliman Model. This letter presents the results of those calculations.

Modified Milliman Model

As stated in the Order, the "Modified Milliman Model" means *"the Milliman model with the adjustments described in the December 9, 2013 Rector Report and:*

- *the probability distributions used in the stochastic modeling process set forth in the 2013 Rector Report with respect to the rating adequacy and fluctuation factor, the unidentified growth and development factor, the catastrophic event factor, and the premium growth level factor;*

- *the probability distributions used in the stochastic modeling process set forth in Milliman's February 27, 2014 correspondence describing the probability distribution assumptions used in Milliman's analysis for the remaining 9 factors; and*

- *the baseline assumptions used in the pro forma projections set forth in Rector's August 27, 2014 response to Question 5.a., available at http://disb.dc.gov/node/888512."*

Requested Surplus Target Calculations

Using Milliman's modelling approach as described in our May 31, 2011 report titled "*Group Hospitalization and Medical Services, Inc.; Development of Optimal Surplus Target Range"*, modified as previously requested by Rector & Associates (i.e., the Modified Milliman Model), we were asked to derive the GHMSI surplus targets reflecting the following:

a. **Alternative Confidence Levels for 200% RBC-ACL Threshold –** We were asked to provide the surplus targets generated if, instead of a 98% confidence level, the following confidence levels are used for the 200% RBC-ACL threshold:

    i. 90% confidence level;
    ii. 93% confidence level; and
    iii. 95% confidence level.

b. **Alternative Confidence Level for 375% RBC-ACL Threshold –** We were asked to provide the surplus targets generated if, instead of an 85% confidence level, **a 75% confidence level** is used for the 375% RBC-ACL threshold.

c. **Alternative Annual Premium Growth Rates –** We were asked to provide the surplus targets generated at the previous (as assumed in December 9, 2013 Rector Report) confidence levels of 98% for the 200% RBC-ACL threshold and 85% for the 375% RBC-ACL threshold, plus the additional thresholds specified in a. and b. above, if instead of the non-FEP Annual Premium Growth rates set forth in the 2013 Rector Report the alternative growth rates shown below are used:

Non-FEP Business			FEP Business[1]	
Previous Growth Rate	**Alternative Growth Rate**	**Probability**	**Growth Rate**	**Probability**
9.1%	4.5%	25%	6.5%	25%
12.4%	8.0%	50%	7.5%	50%
16.1%	12.2%	25%	8.4%	25%
[1] No changes in FEP growth rates were requested.				

Surplus Target Results

The following table presents the surplus targets generated based on the approach and assumptions outlined above. For comparison purposes, we have also included the surplus targets based on the previous 85% and 98% confidence levels with the previous premium growth rates, as reflected in the modeling process set forth in the December 9, 2013 Rector Report (and as presented on page 30 of that report).

Summary of GHMSI
Surplus Target Calculations
Based on Modified Milliman Model

Confidence Level	Based on December 9, 2013 Premium Growth Rate Assumptions		Based on Alternative Premium Growth Rate Assumptions[1]	
	375% of RBC-ACL	200% of RBC-ACL	375% of RBC-ACL	200% of RBC-ACL
75%	604%		541%	
85%	746%		672%	
90%		631%		575%
93%		714%		653%
95%		788%		721%
98%		958%		880%

[1] As outlined in Item c. above.

Limitations and Caveats

The information presented here is being provided for informational purposes, in response to a request by DISB. The alternative assumptions and resulting surplus target values provided do not reflect the opinion of Milliman, nor are they consistent with the opinion of Milliman regarding an appropriate surplus target range for GHMSI. The intent of this letter is to present the alternative calculation results as requested, and not to address their suitability or reasonableness, either individually or collectively.

This letter refers to, and relates to, Milliman's 2011 GHMSI report on the Development of an Optimal Surplus Target Range. It should be considered only in connection with that report; applicable terms and concepts are not repeated here. The limitations and caveats presented in that report also apply to this letter; key provisions are highlighted below.

This material was developed for the exclusive use of GHMSI management, for its internal consideration in connection with surplus targets. We understand that GHMSI may wish to share

this material with regulators and their professional advisors in the District of Columbia, Maryland and Virginia, or other appropriate regulators. We hereby grant permission, so long as this letter and the entire 2011 have been provided. We recommend that any party receiving this material have its own actuary or other qualified professional review this material to ensure that the party understands the assumptions and uncertainties inherent in our estimates. Milliman does not intend to benefit any third party either through this analysis or by granting permission for this material to be shared with other parties.

In order to provide the requested information, we have incorporated the specified "Modified Milliman Model" assumptions (as outlined on pages 1 and 2 above), along with the specified changes in confidence levels and growth rate assumptions (outlined in Items a., b., and c. above) into the projection models that we had previously developed. Differences between the resulting projection values (or any such projection results) and actual amounts depend on the extent to which future experience conforms to the assumptions made in the projections. It is certain that actual experience will not conform exactly to the assumptions used in any particular projection. Actual amounts will differ from projected amounts to the extent that actual experience deviates from the assumptions as to future experience (in this case, those specified by Rector and DISB).

In developing this material we relied on data and other information provided by CareFirst. We have not audited or verified this data or information. The expectations for CareFirst in the future and the subsequent actual experience of CareFirst may vary materially from the assumptions used in this analysis.

The authors of this material are Consulting Actuaries for Milliman, are members of the American Academy of Actuaries, and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

Please let us know if you have any questions regarding this information, or if you wish to discuss it.

Sincerely,

Phyllis Doran

Phyllis A. Doran, FSA, MAAA
Principal and Consulting Actuary

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