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March 14, 2014

The Honorable Chester A. McPherson, Commissioner
District of Columbia Department of Insurance, Securities and Banking
810 First Street NE
Suite 701
Washington, D.C. 20002

*Re: Surplus Review of Group Hospitalization and Medical Services,
Inc. (GHMSI)*

Dear Commissioner McPherson:

Thank you for your recent responses to DC Appleseed's data requests regarding the Rector and Milliman analyses of GHMSI's surplus. We appreciate your processing of these requests, which have been designed to illuminate important issues in this proceeding. As you know, this proceeding necessarily involves consideration of rather technical actuarial reports. Resolving questions surrounding these reports now will help ensure that the upcoming hearing can be conducted as efficiently as possible. It will also ensure that you will have a complete record on which you can reach a sound determination, which the D.C. Court of Appeals noted is especially important here, where "even a small variance can implicate millions of dollars." *D.C. Appleseed Ctr. for Law & Justice v. D.C. Dep't of Ins., Secs. & Banking*, 54 A.3d 1188, 1219 (D.C. 2012). And from our viewpoint, resolving these matters now will allow DC Appleseed to meaningfully participate in the hearing, consistent with the Court's decision. *Id.* at 1219 n.41.

Below we seek to clarify whether certain data we requested earlier will be available, and also seek to understand new information recently provided to us in the responses from Milliman and Rector. We are happy to work with you, your staff, Milliman, and Rector to resolve these requests.

We discuss each relevant data request below:

1) Please confirm that the column headings "RBC % Change" in the charts at pp. 2 and 3 of the March 6, 2014, Rector/FIT Response ("Rector/FIT Response") refer to changes in the number of percentage points in the RBC ratio.

2) The Rector/FIT Response, at p. 3, suggests that material changes to Rector's assumptions since 2009 included changes reflecting "Other Business Risks." The Chart below this statement includes fourteen enumerated factors that led to changes in the RBC percentage. Which of these fourteen factors correspond to changes in "Other Business Risks"?

- 3) Appleaseed asked that Rector explain why its target surplus ratio increased from 600% (2009 Report) to 958% RBC (2013 Report). *See* Data Request # 8.¹ In response, Rector provided two charts: the first chart shows the impact of changes Milliman made to its assumptions between 2008 and 2011; the second shows the impact of changes that Rector made between 2009 and 2013. *See* Rector/FIT Response, at 2–3. However, Rector’s target surplus increased 358 percentage points between 2009 and 2013, while the Rector chart suggests a difference of only 250 percentage points. *Id.* at 3. Moreover, the 2009 Rector surplus determination was for a 99% certainty threshold and the 2013 Rector surplus determination was for a 98% certainty threshold. We estimate based on normal distributions that a 98% certainty would lower the 600% calculated in the 2009 Report to 553%. We request:
- a) A detailed explanation of whether and how these charts reconcile this 405 percentage point difference in light of the change in confidence level, and of any other factors that reconcile the difference.
 - b) If Rector cannot explain the additional 155 percentage points – the difference between 250% and 405% – please so state.
 - c) If Rector estimates that a change from the 99% confidence level to the 98% confidence level would, based on normal distributions, lower the 600% to a number that is different from 553%, a detailed explanation of whether and how these charts reconcile the percentage-point difference between 600% and Rector’s different number, and of any other factors that reconcile the difference.
 - d) A statement whether Rector did or did not account for the difference in confidence levels between its 2009 and 2013 reports when it prepared the above-referenced chart identifying a difference of 250 percentage-points.
 - e) Whether or not Rector accounted for the difference in confidence levels between its 2009 and 2013 reports, a detailed explanation of the reasons for the additional 108 percentage-points – the difference between 358 percentage points and 250 percentage points.
- 4) The Rector charts showing the changes in Milliman and Rector assumptions between 2008 and 2013 also show changes in assumptions about equity portfolio asset values (including the impact of pensions). These changes led to an increase of 70 percentage points in the target surplus RBC ratio. Neither the Rector nor the Milliman reports previously discussed any details of the impact of GHMSI’s equity portfolio on the required surplus. We therefore request that Rector or Milliman provide detailed explanation regarding the reasons for this impact on the target surplus, including but not limited to:
- a) The assumed changes in the GHMSI equity portfolio asset values that generated a surplus increase of 70 percentage-points, including the magnitude and probability of each assumed change;
 - b) Any data relied on by Milliman in support these assumed changes;

¹ Appleaseed’s January 29 and February 19 letters each included an “Attachment A” describing, and clarifying, the relevant data requests. These requests were numbered one through nine and designated by the same number in each attachment. For purposes of this letter, references to a given numbered “Data Request” (i.e. “Data Request # 8”) refer to the requests and explanations described in those attachments.

- c) Any data provided by Milliman to Rector in support of these assumed changes; and
 - d) Any data relied on by Rector in determining whether to accept or adjust these assumed changes.
- 5) Appleseed has sought information regarding rank-ordered gain or loss outcomes from the stochastic modeling by Milliman that the Rector Report indicates exists. *See* Data Request # 2. Specifically, even if Rector was not provided with all of the gain or loss outcomes, we requested all those outcomes provided to Rector. We also requested, for all gain/loss outcomes that were put through the financial projection component of the model, the resulting projected impacts on GHMSI's surplus after the loss outcomes were applied to the pro forma financial projections. Because we have not yet received a response to this request, we again request:
- a) A spreadsheet in electronic format that ranks by percentile the gain/loss outcomes from the first stage of Milliman's stochastic modeling;
 - b) The gain/loss outcomes from the first stage of the stochastic modeling that Milliman put through the pro forma financial projections to determine the impact of those gain/loss outcomes on surplus;
 - c) The gain/loss outcomes from the first stage of the stochastic modeling that were provided by Milliman to Rector;
 - d) A statement as to whether Rector adjusted any of the pro forma financial projections;
 - e) The gain/loss outcomes that Rector requested Milliman to put through the pro forma financial projections; and
 - f) The pro forma financial results for all gain/loss outcomes that were put through the pro forma model by Milliman at Rector's request.
- 6) Milliman states that the values and probabilities of the expected gain/loss amount are "based on analysis of historical data." *See* March 5, 2014, Milliman Response, at 2 ("Milliman Response"). The Milliman 2008 and 2011 reports discuss historical GHMSI data extending back as far as the mid-1970s. We request:
- a) The time span identified by years of the historical data upon which Milliman relied to derive expected gain/loss values and probabilities, including but not limited to the gain/loss values and probabilities with respect to the rating adequacy and fluctuation factor;
 - b) The historical time spans identified by years that Rector relied upon or asked Milliman to rely upon for any of the gain/loss values and probabilities;
 - c) Any documents in which Rector discussed the appropriate historical time spans to rely upon for the derivation or validation of gain/loss values and probabilities;
 - d) A statement as to whether Rector was aware, before it submitted its Report, of the historical time spans relied upon by Milliman to derive gain/loss values and probabilities; and
 - e) A description of how Rector became aware of the historical time spans, including any documents provided by Milliman to Rector.

- 7) In our Data Request #4, we noted that the Rector Report, at pp. 28-29, offers some reasons for departing from historical experience concerning premium growth. We requested, but have not received, an explanation of how the cited reasons bear on future premium growth, and why those reasons support departures from historical experience in the magnitudes that Rector assumes. We renew this request.
- 8) Appleseed requested a description of the multiple extremely adverse events that the model assumes could occur. *See* Data Request # 9. To date, we have not received this information. We request:
 - a) A description of the extremely adverse events that were assumed to occur;
 - b) A description of the combinations of simultaneously occurring extremely adverse events that were assumed to occur; and
 - c) Identification of the probabilities and magnitudes of each assumed combination of simultaneously occurring extremely adverse events.
- 9) With respect to the impact of health care reform on the model, we have several follow-up questions:
 - a) First, the Milliman Response (pages 15-16) stated that the rating adequacy and fluctuation factor accounted for pre-2014 ACA changes and then added after all calculations were made an additional amount for the estimated impact of 2014 ACA changes (page 24). The Rector Report (page 23) indicates it incorporated in the rating adequacy and fluctuation factor “the anticipated impact of health care reforms, regardless of whether they were in effect at the time of Milliman’s analysis.” Please explain whether and how Rector ensured that it did not “double count” the impact of the pre-2014 ACA changes already accounted for by Milliman in the Rating Adequacy and Fluctuation factor?
 - b) The Rector Report and the Rector/FIT Response discuss modeling for effects of health care reform as one of the bases for modifying the rating adequacy and fluctuation factor and the premium growth rate. Please explain whether and how Rector quantified the impact of the ACA in revising the rating adequacy and fluctuation factor and the premium growth rate (as described on page 4 of the Rector/FIT Response).
 - c) In making upward adjustments to RBC due to the impact of the ACA, did Rector account for any ACA provisions, other than those identified on pages 22 through 23 of the Rector report, which might have decreased/increased the target RBC ratio? If so, please identify each such additional ACA provision, and explain how Rector quantified the negative or positive impact of each such provision on surplus.
- 10) In Chart 1 of Attachment A of the Milliman Response, Milliman provides probabilities of various surplus changes resulting from deviations from baseline trended rates when the deviations are unremediated over both a two- and three-year period. Footnotes to this table state that the “[m]easurement of impact of deviation on surplus” in this chart “is the cumulative amount over a 2-3 year period.” The chart states that Milliman estimates, for example, that there is a 3% probability that GHMSI’s surplus will increase by 26% of non-FEP premiums over the course of a 2-year period, and by 31.1% over the course of a 3-year period. Rector asked Milliman to incorporate revised modeling for this factor but did not provide the same level of detail regarding the time frame over which the changes would

apply or whether the impact on surplus was measured annually or as a cumulative amount across a given time frame. *See* Rector Report, at 22. We understand from the February 21st call that Rector's revised modeling applies to a 2.5 year period. We request:

- a) Confirmation by Rector and Milliman of the relevant time period corresponding to the revised Rating and Adequacy Fluctuation surplus impacts, and
 - b) A statement as to whether those impacts represent the impact on surplus during a single year or across multiple years.
- 11) Appleseed requested current enrollment data, split into Individual, Small Group, and Large Group. *See* Data Request # 4. We have been able to locate this enrollment data for calendar year 2012, but not for any later period. We request the most current enrollment data available.
- 12) In Data Request #4 we asked that Rector explain how it used the Society of Actuaries March 2013 research report to calculate impacts on the premium growth levels specific to GHMSI. We have not received a response, and we here renew that request.
- 13) The Rector Report (pages 22-23) lists seven specific reasons (4 non-ACA and 3 ACA) for modifying the rating adequacy and fluctuation factor. In Data Request # 1, we requested the probability distributions for each of those factors, and their separate impacts on Rector's modification of the rating adequacy and fluctuation factor. We again request that information.
- 14) Pages 28-29 of The Rector Report state that the following considerations were taken into account in determining GHMSI's future premium growth levels: Enrollment Changes Including Health Care Reform Effects, Rising Health Care Costs, and Policyholder Cost-Sharing Decisions.
- a) Please identify the specific impacts of each of these considerations in establishing GHMSI's future premium growth levels.
 - b) Please identify which lines of business (i.e., individual, small group, large group, Medicare Supplement, Dental, Vision, Other) to which each consideration was applied.
- 15) On page 17 of the May 31, 2011, Milliman Report it states, "...we used an automated process to simulate the tens of millions of possible combinations produced by our distribution, employing a simulation model that is commonly applied in financial modeling." On page 10 of the December 9, 2013, Rector Report it states, "First, Milliman uses a stochastic modeling process to generate hundreds of thousands of potential gain or loss outcomes...." We request:
- a) A detailed explanation of why the number of scenarios changed from "tens of millions" to "hundreds of thousands";
 - b) A statement as to whether some possible scenario combinations were not considered;
 - c) If some possible scenario combinations were not considered, an identification of the ones that were not considered; and
 - d) If some possible combinations were not considered, a detailed explanation of the reasons why each was not considered.

Thank you again for your attention to this matter. While we realize we are seeking significant information about a number of complex issues, for the reasons stated, we think it is in everyone's interest to provide this information and clarify these issues prior to the hearing.

Sincerely,



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