Government of the District of Columbia

Department of Insurance, Securities and Banking

PUBLIC ROUNDTABLE

On

REVIEW OF GROUP HOSPITALIZATION AND MEDICAL SERVICES, INC. ("GHMSI") 2011 SURPLUS

Before the

COMMITTEE ON BUSINESS, CONSUMER AND REGULATORY AFFAIRS

COUNCILMEMBER VINCENT B. ORANGE, SR.

COMMITTEE CHAIRPERSON

Testimony of

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ACTING COMMISSIONER

DEPARTMENT OF INSURANCE, SECURITIES AND BANKING

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Room 500
John A. Wilson Building
1350 Pennsylvania Avenue, NW
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Good Morning Chairman Orange, Members of the Committee on Business, Consumer, and Regulatory Affairs, and Committee staff. I am Stephen Taylor, the Acting Commissioner of the Department of Insurance, Securities and Banking ("Department"). The Department regulates insurance, securities, banking and other financial services in the District of Columbia. I appreciate the opportunity to testify today on the Review of Group Hospitalization and Medical Services, Inc. (the "Corporation") 2011 Surplus.

In light of the pending proceedings before the Department and the probable appeals by the Corporation and other parties, I am limited in what I can discuss during this Public Roundtable. I can talk about the status of the surplus review as well as issues in the public record. However, I am unable to discuss the Department's ongoing deliberations or analysis of the Corporation's 2011 surplus generally or of the Plan submitted by the Corporation specifically.

Please let me start by providing a little background on the review of the Corporation's surplus as of December 31, 2011. After a hearing on June 25, 2014 ("Hearing"), and a review of submissions, the former Acting Commissioner of the Department concluded that the Corporation 2011 surplus attributable to the District was "excessive" as defined by the Hospital and Medical Services Corporation Regulatory Act of 1996, as amended by the Medical Insurance Empowerment Amendment Act of 2008 ("Act"). The Act requires the Department to review the Corporation's surplus at least once every three years to determine whether the portion of the surplus attributable to the District is excessive. If the Corporation's surplus is found excessive

after a hearing, the Act requires the Commissioner to order the Corporation to submit a plan for dedication of the excess to community health reinvestment in a fair and equitable manner.

The former Commissioner issued a Decision and Order on December 30, 2014 ("Decision"), concluding that the Corporation's 2011 surplus was excessive, of which approximately $56 million was attributable to the District. To reach that conclusion, the former Commissioner examined the surplus in terms of its Risk-Based Capital Authorized Control Level ("RBC-ACL"). "Risk Based Capital" ("RBC") is a method developed by the National Association of Insurance Commissioners to determine the minimum amount of capital an insurer should hold to support its business operations in consideration of its size and risk profile. District law identifies various RBC action levels at which company or regulatory action is required to address an insurer's financial deficiencies. Each action level is a multiple of a reference level of RBC known as the insurer's RBC-ACL. In his review, the former Commissioner concluded that: (1) the Corporation's surplus as of December 31, 2011 was 998% RBC-ACL (approximately $963.5 million); (2) the appropriate level for the Corporation's 2011 surplus was 721% RBC-ACL (approximately $695.9 million); and (3) that 21% of the Corporation's 2011 surplus was attributable to the District. Additionally, the Decision ordered the Corporation to file a plan to dedicate the $56 million excess surplus to community health reinvestment in a fair and equitable manner.

The Corporation and the D.C. Appleseed Center for Law and Justice, Inc. ("Appleseed"), which participated in the Hearing, filed motions requesting the Department to reconsider the

Decision. The Corporation's motion for reconsideration included the following criticisms of the Decision:

1. The Commissioner failed to coordinate with Maryland and Virginia as required by the Act, and the Decision conflicts with a Maryland Insurance Administration order and therefore is arbitrary and capricious and violates the Corporation's constitutional rights.
2. The Decision should have first determined the surplus attributable to the District and only then evaluated whether it was excessive.
3. The Decision's method of attributing surplus to the District is arbitrary and does not comply with the Act.
4. The Decision's use of a 95% confidence level for the risk of dropping to 200% RBC-ACL is arbitrary and capricious.
5. The Decision erred by using a single surplus target point, rather than a range.

Appleseed's motion for reconsideration included the following criticisms of the Decision:

1. The Commissioner erred in adopting the Department's expert's probability distribution for the equity portfolio factor.
2. The Commissioner erred in allocating the Corporation's surplus to the District, and that he should have allocated 63.5% of the surplus to the District, not 21%.

The former Commissioner denied both motions for reconsideration.

The Corporation and Appleseed filed appeals of the Decision, and the Corporation also appealed the denial of its motion for reconsideration. The District of Columbia Court of Appeals dismissed the appeals on the grounds that the Decision was non-final, and therefore non-appealable. The Court indicated that the administrative process would be complete and appealable once the Department rules on the Plan.

On March 16, 2015, the Corporation submitted its plan required by the Decision ("Plan"). In the Plan, the Corporation argues, among other things, that it has already reduced the surplus attributable to the District by more than is required under the Decision. The Corporation also asserts that the Act requires the District to coordinate with the two other jurisdictions in which the Corporation operates (Maryland and Virginia) on any actions relating to the Corporation's surplus, and advocates for a "regional view" that would require a coordinated process and a joint agreement for any determination of, or distribution, of excess surplus. The Corporation also argues that, in the meantime, it cannot comply with the Decision because it is contradictory to an order issued by Maryland's insurance regulator.

After the Decision, Maryland and Virginia passed laws that, among other things, permit their insurance regulators to issue orders prohibiting the distribution of the Corporation's surplus. Both Maryland and Virginia have indicated that the Corporation may not reduce its surplus without their permission, which they have not given.

The Virginia State Corporation Commission Bureau of Insurance ("Bureau") conducted an examination of DISB's surplus review of the Corporation's 2011 surplus. In a report issued

on April 15, 2015, the Bureau noted that its consultant determined that the appropriate target surplus range for the Corporation was 798-963% RBC-ACL. The Bureau also concluded, among other things, that a distribution of surplus could cause some potential for future harm; however it recommended against an order prohibiting the Corporation from distributing the excess surplus identified in the Order and recommended in favor of taking a more active role in coordinating with the Department as well as the Maryland Insurance Administration on future actions relating to the Corporation's surplus.

On October 26, 2015, the Maryland Insurance Administration sent me a copy of its consultant's report regarding its review of the Corporation's surplus and the Corporation board's proposed targeted surplus range. The consulting firm issued a report recommending that the 2011 surplus range for the Corporation of 1,000% to 1,300% RBC-ACL be retained for 2014. The Maryland Insurance Administration Commissioner adopted the recommendation on October 26, 2015.

Under the Act, if the Commissioner determines that the Corporation failed to submit a plan as ordered within a reasonable period or failed to execute within a reasonable period a plan already submitted, then the Commissioner shall deny, for 12 months, all premium rate increases for subscriber policies written in the District sought by the Corporation and may issue such orders as are necessary to enforce the purposes of the Act. The Department is currently reviewing the Plan along with the 2011 surplus review process.

As the Committee may know, the surplus review process is not a simple exercise. Rather, the Act requires the Department to conduct a complex and thoughtful analysis of factual,

legal, actuarial and regulatory issues. So it is critical that we get this process correct. The last thing I want to do is make a mistake which could disrupt our health insurance market. Such a result would not be good for the Corporation; and it certainly would not be good for our consumers or businesses. Accordingly, the Department expects to complete its review and make a determination on how to complete the 2011 surplus review process as soon as possible so it can begin working in earnest on the current 2014 surplus review process, which began this past June.

Thank you again for the opportunity to testify today. I am happy to answer any questions you may have, subject to the limitations I referenced earlier.