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Mr. Lee Voghel
State of Connecticut
Department of Social Services
25 Sigourney Street
Hartford, CT 06106-5033

Final & Confidential

Subject: Managed care rate ranges for State Fiscal Year 2009 HUSKY A Program – CMS rate certification letter

Dear Mr. Voghel:

In partnership with the State of Connecticut's (State) Department of Social Services (DSS), Mercer Government Human Services Consulting (Mercer), as a part of Mercer Health & Benefits, LLC, has developed capitation rate ranges for the Medicaid managed care program, HUSKY A. Mercer relied on encounter and financial information provided by the State and the managed care organizations (MCOs) to develop rates for the contract period July 1, 2008 through June 30, 2009, or state fiscal year 2009 (SFY09). This letter presents an overview of the analyses and methodology used in Mercer's capitation rate range development.

Base data development

Mercer developed managed care rate ranges from base data consisting of two sources. These sources are MCO encounter data and MCO audited financial data. The base data was adjusted for changes in covered benefits, trends and other programmatic changes to project managed care rate ranges for the SFY09 contract period. The following sections provide more detail around the specific adjustments made to each data source.

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Encounter data

In order to develop the encounter data portion of the base, Mercer used encounter data with dates of service from July 2005, through June 2007, with paid run out through December 2007. Encounters were included from each of the four MCOs that participated in the HUSKY A managed care program during the base data time period. These MCO's are Anthem, Community Health Network (CHN), WellCare and Health Net.

For purposes of developing managed care capitation rates, Mercer applied a set of adjustments to the base period encounter data as described below.

Changes in covered benefits

The encounter base data was adjusted to exclude services that were previously covered and captured during the base data time period but are no longer covered benefits in the HUSKY A capitated managed care program for SFY09.

Beginning January 1, 2006, behavioral health services covered under the HUSKY A program were transitioned to the Connecticut Behavioral Health Partnership (CTBHP) and no longer included as part of the HUSKY A benefit package.

The base encounter data was also adjusted to reflect the carve-out of dental and pharmacy services. Most dental and pharmacy services will no longer be a covered benefit in the HUSKY A managed care program for SFY09. The removal of pharmacy services from the HUSKY A managed care program to a fee-for-service (FFS) setting was effective beginning February 1, 2008. The removal of dental services from the HUSKY A managed care program is anticipated to be effective beginning July 1, 2008.

Pricing

Mercer applied a pricing algorithm for FFS and capitation subcontract type encounters with a zero-paid amount as reported by the MCO. The pricing algorithm used MCO-specific average unit costs based on FFS type encounters with paid amounts reported by the MCO. Three average unit cost schedules were built for the three full and partial calendar year time periods utilized in the encounter base: incurred dates July 2005 through December 2005, January 2006 through December 2006 and January 2007 through June 2007. Other MCO fee schedules were used where an MCO's data was inadequate to build its unit cost

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schedule for certain services. The net impact of Mercer's pricing algorithm was to raise the total reported paid amounts in the encounter data to more credible levels.

Incurred but not reported (IBNR) and shared risk

Mercer reviewed and adjusted the base encounter data to account for encounters processing lag and shared risk arrangements. These adjustments were based on encounter IBNR information and shared risk information obtained in the MCO financial surveys.

Third party liability (TPL) recoveries

Managed care contractors may keep any TPL recovery amounts. These recovery amounts are not reported in the base encounter data. Therefore, Mercer applied an adjustment to the base encounter data to reflect the estimated impact attributable to TPL recoveries.

Relational modeling

Relational modeling adjusted the base encounter data to more accurately reflect the category of service (COS) groupings that were reported in the MCO financials. These adjustments were made at the composite level for each time period and MCO and allocated to each rate cell based on their relativities. Note that the overall impact was budget-neutral for the base period since it was a reallocation of the reported total amounts in the encounter data.

Encounter omissions

Mercer also develops an estimate for an encounter omissions adjustment, also referred to as the encounters underreporting completion factor. For each major COS, the MCO's priced encounters per-member-per-month (PMPM) costs were compared to the reported amounts in the financial surveys. If the encounter data costs were below 95 percent of the financial data amounts, they were adjusted upward to 95 percent of the financial amount. If the encounter costs were above the financial amount, they were adjusted downward to the financial amount. In other words, the adjusted encounter data would be within 95 to 100 percent of the financial data. This is consistent with the policy that MCOs need to submit good encounter data as required contractually in order to provide encounter data that is complete and appropriate for rate development purposes.

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Reinsurance

An adjustment was made to reflect the total recoveries related to incurred health care services eligible for reinsurance. The adjustment was developed based on MCO-submitted financial data.

Financial data

In order to develop the financial data portion of the base, Mercer requested financial data surveys to be completed by the four MCOs that participated in the HUSKY A program during the base data time period.

The four MCOs that contracted with the State during the base data time period reported revenue and expenditure data by rate cell for service dates occurring in a thirty-month period from January 2005 through June 2007. To keep the financial reporting period consistent with the two-year incurred period of encounter data, two SFY-incurred periods were created from the thirty-month financial base.

Reported financials from January 2005 through December 2005, were adjusted to reflect only the last six incurred months of calendar year 2005. These last six incurred months of calendar year 2005, and the first six incurred months of calendar year 2006 were combined to create a SFY06 financial reporting period.

Similarly, the last six incurred months of calendar year 2006, and the first six incurred months of calendar year 2007, were combined to create a SFY07 financial reporting period. Both SFY reporting periods were completed using MCO IBNR estimates, with the benefit of additional paid run-out through September 2007.

Revenue data included capitation income, investment income and other income. Expenditure data included medical payments by COS split by type of subcontract (capitated or FFS) and separate liability components attributable to IBNR and shared risk. Expenditure data also included salaries and other administrative costs. For purposes of developing the financial component of the medical cost base, the items used from the financial surveys were the medical expenditures, including the IBNR and shared risk liabilities.

For purposes of developing managed care capitation rates, Mercer applied a set of adjustments to the base period encounter data as described below.

Changes in covered benefits

Similar to the adjustment made to the base encounter data, Mercer adjusted the financial base data to exclude services that were previously covered and captured during the base data time period but are no longer covered benefits in the HUSKY A capitated managed care program for SFY09. The services that were excluded from the base financial data are behavioral health, dental and pharmacy services.

IBNR and shared risk

Mercer reviewed and adjusted the base financial data to account for outstanding unpaid claims liability and for shared risk arrangements. This was based on reviewing the MCO's reported financial claims lag triangles and their reported IBNR estimates as part of the financial survey. Shared risk information was also reported in the financial surveys.

Third party liability recoveries

Managed care contractors may keep any TPL recovery amounts. These recovery amounts are reported net of the base financial data. Therefore, Mercer did not make any further adjustments to the base financial data for TPL recoveries.

Relational modeling

Relational modeling adjusted the base financial data to more accurately reflect the rate cell groupings captured in the MCO reported encounter data. This was necessary due to the low credibility in the allocation of expenditures by rate cell as reported in the financial surveys. The financial allocation was revised by using the relativities measured in the encounter data. Note the overall impact was budget neutral for the base period since it was a reallocation of the reported total amounts from the financial surveys.

Reinsurance

An adjustment was made to reflect the total recoveries related to incurred health care services eligible for reinsurance. The adjustment was based on MCO-submitted financial data.

Blending of base data

The adjusted MCO encounter and financial data described above were blended in three stages to produce the final blended base period used in the SFY09 rate development process. The three stages are described below.

Blending: Stage 1

The adjusted MCO-specific financial and encounter data as described above were each summarized to reflect SFY06 and SFY07 annual time periods. The SFY06 data was trended forward one year to be on a comparable time period as the SFY07 data. Next, each annual SFY time period was assigned a 50 percent credibility weight that blended the two time periods together.

The result of this blending produced one encounter base component and one financial base component for each MCO, with each component appropriately adjusted and centered at January 1, 2007.

Blending: Stage 2

The next stage of blending combines the financial base of all four MCOs and similarly combines the encounter base of all four MCOs. Weighting was based on MCO membership. The result of this blending produced one overall financial base component and one overall encounter base component reflecting the HUSKY A experience of the four MCO's.

Blending: Stage 3

The last stage of blending combines the two base components — financial and encounter — to form one integrated base. Mercer assigned 50 percent credibility weighting to encounter data and 50 percent credibility weighting to financial data to develop the integrated base experience centered at January 1, 2007.

Annual trend

Mercer trended the base data from January 1, 2007, the midpoint of the base period, to January 1, 2009, the midpoint of the SFY09 rate development time period. This trending was done by COS using annualized trends that were developed based on the methodology described below.

Annual trend factors for medical inflation were derived using information from various data sources while using both quantitative data and qualitative estimates. General regression techniques were applied to MCO financial cost data that included monthly cost information captured in the financial lag data file. Forty-eight months of incurred financial data through June 2007, were completed, adjusted and analyzed for Anthem, CHN, Health Net and

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WellCare. Historical encounter data covering incurred dates of service from July 2005 through June 2007, were also analyzed.

These encounter and financial trend estimates were reviewed and compared to trends from several other sources, including other states' Medicaid programs, Consumer Price Index (CPI) medical trends, Data Resources Incorporated (DRI) trends and general health care industry trends.

Mercer also reviewed the impact of various programmatic changes that could influence the ultimate annualized trends used for rate development purposes. These programmatic changes could impact either the base data that was analyzed for trend purposes or the projected prospective annualized trends developed for rating purposes. Program changes, such as changes to the Medicaid fee schedules and changes to benefits or eligibility requirements, were reviewed when determining the final annual COS specific trends. The final midpoint estimate for the annualized aggregate medical trend used in the rate development process is 6.8 percent.

Program changes

In addition to the carve-out of behavioral health, dental and pharmacy services as described in previous sections, Mercer incorporated adjustments for other program changes that impact the SFY09 HUSKY A rate development process. These additional program changes account for other mandated changes to the Medicaid program during the time period between the base data and the contract year. These mandated changes include the following:

- Coverage for the human papilloma virus (HPV) vaccine for females ages nine to twenty-six years old, effective July 1, 2006
- Expansion of eligibility for pregnant women up to 250 percent of FPL, effective January 1, 2008
- Expansion of eligibility for HUSKY A parents and caregivers up to 185 percent of FPL, effective July 1, 2007
- Inclusion of routine dental examinations by primary care physicians, effective January 1, 2008

- Inclusion of the full encounter rate for Federally Qualified Health Centers (FQHC) in the MCO's at-risk capitation rates. This payment includes the FQHC wrap-settlement payment that was previously paid by the State. This adjustment was based on correspondence between the State and Associate Regional Administrator, Richard McGreal, from CMS. Currently, an effective date of July 1, 2008, is anticipated

- Changes to the Medicaid fee schedules to incorporate a mandated floor level of reimbursement for HUSKY A providers effective at various dates throughout SFY08

Mercer worked with the State to identify and quantify the impact on the HUSKY A program for the various program changes listed above. These program changes have varied effective dates and therefore, the impacts for these changes are applied at various points in the rate development process.

Mercer received and reviewed the impact of these program changes based on information and estimates provided by the State. The resulting adjustments were applied to the data and varied by rate cell and category of service since not all of the programmatic changes impact each rate cell and service in the same magnitude.

Please note that the program changes are current to the best of our knowledge. However, the legislature continues to debate various program features that may have an impact on the rates. To the extent that the legislature approves other program changes that are expected to have a material impact on the HUSKY A program, the rate ranges presented in this letter may need to be revised.

Managed care rate development

The blended base data consists entirely of managed care data. By using the blended base data, the annualized trends and the program changes outlined above, Mercer projected the medical component for the managed care rate ranges for the HUSKY A program. For the administration, risk and profit loading, Mercer reviewed the financial surveys and built in a midpoint load of approximately 10.9 percent calculated as a percentage of gross capitation rates.

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Rate range development

To assist the State during its rate discussions with the MCO's, Mercer develops and provides rate ranges for each rate cell. The rate cell ranges were developed using a range of factors around specific assumptions used in the development of the SFY09 rates. These ranges are meant to account for the variability observed in the claims experience, population acuity, administrative efficiencies and trend projections.

The final rate ranges represent a "best estimate" of the range of anticipated costs to provide services during the contract period for the benefits and populations to be covered under the HUSKY A capitated managed care program. The final rate ranges vary by rate cell. In aggregate, the composite HUSKY A rate range varies from the midpoint estimate by -5.4 percent for the lower bound and 5.4 percent for the upper bound.

Please refer to Exhibit 1 for the SFY09 rate ranges for each individual rate cell.

Certification of final rate ranges

Mercer certifies that the HUSKY A rate ranges are developed in accordance with generally accepted actuarial practices and principles by actuaries meeting the qualification standards of the American Academy of Actuaries for the populations and services covered under the managed care contract. Rates developed by Mercer are actuarial projections of future contingent events. Actual MCO costs will differ from these projections. Mercer has developed these rate ranges on behalf of the State to demonstrate compliance with the Centers for Medicare and Medicaid Services (CMS) requirements under 42 CFR 438.6(c) and is in accordance with applicable laws and regulations. MCOs are advised that use of these rate ranges may not be appropriate for their particular circumstance and Mercer disclaims any responsibility for the use of these rate ranges by MCOs for any purpose. Mercer recommends that any MCO considering contracting with the State should analyze its own projected medical expense, administrative expense and any other premium needs for comparison to these rate ranges before deciding whether to contract with the State. Use of these rate ranges for any purpose beyond that stated may not be appropriate.

If you have any questions related to this certification, please call me at +1 602 522 6564.

Sincerely,

Kevin Lurito

Kevin Lurito, FSA, MAAA

KL/AJ/ad

Copy:
Rose Ciarcia, State
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Maria Dominiak, Mercer
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Attachments

EXHIBIT 1

SFY09 HUSKY A physical health Statewide rate ranges

Rate cell	Lower bound PMPM	Midpoint PMPM	Upper bound PMPM
TANF < 1 male and female	$629.60	$676.98	$724.37
TANF age 1–14 male and female	$ 84.06	$ 88.02	$ 91.98
TANF age 15 – 39 male	$ 99.85	$105.67	$111.48
TANF age 15 – 39 female	$287.36	$302.48	$317.61
TANF age 40+ male	$195.85	$207.25	$218.64
TANF age 40+ female	$287.40	$302.53	$317.65
SSI age 0 – 20 male and female	$424.68	$456.65	$488.61
DCF	$108.35	$118.42	$128.48