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November 19, 2007

Ms. Pam Parker
Manager, Special Needs Purchasing
Minnesota Department of Human Services
540 Cedar Street
St. Paul, MN 55101-2208

Re: Trend & Surplus Adjustments for 2008 Payment Rates – Seniors

Dear Pam:

This letter contains my analysis of trend and surplus rate adjustments for the payment rates for basic care services for the Minnesota Senior Health Options (MSHO) and Minnesota Senior Care / Minnesota Senior Care Plus (MSC) programs. I will refer to the enrollees in these programs and rate cells collectively as "seniors". The purpose of this analysis is to assist the Minnesota Department of Human Services (DHS) with setting payment rates for contracting health plans for these programs. The results may not be appropriate for other purposes.

The results contained in this letter are intended only for use by DHS and CMS, the federal agency that must approve these capitation rates. This analysis should be considered preliminary until the resulting capitation rates are approved by DHS and CMS. Milliman does not intend to benefit and assumes no duty or liability to other parties who receive this work. This letter should be reviewed only in its entirety. It assumes the reader is familiar with Minnesota's Medicaid programs and managed care rating principles.

The results in this letter are technical in nature and are dependent upon specific assumptions and methods. No party should rely upon specific assumptions and methods nor upon these results without a thorough understanding of those assumptions and methods. Such an understanding may require consultation with qualified professionals.

The trends and rate adjustments I have developed are based on the historical financial results for the public program business for the health plans that participate in the MSHO and MSC programs. The recommended trends and rate adjustments are intended to provide rate

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levels that result in a targeted contribution to surplus as a percentage of income before investment income for the health plans in aggregate, assuming prudent management. For this analysis, this target percentage is equal to 0.75%. I have reviewed the overall capital position of the MCOs and aggregated gains and losses on Minnesota Medicaid business over the past few years. I describe my findings in my letter regarding trend and surplus adjustments for the PMAP, PGAMC, and MNCare programs.

Differences between estimates and actual amounts depend on the extent to which future experience conforms to the assumptions made for this analysis. It is almost certain that actual experience will not conform exactly to the assumptions used in this analysis. Actual amounts will differ from projected amounts to the extent that actual experience is different than expected. Accordingly, DHS should continue to carefully monitor actual experience and make adjustments as necessary.

In performing this analysis, I have relied on data and other information provided to me by DHS and the plans with which it contracts. I have not audited or verified this data and other information. If the underlying data or information is inaccurate or incomplete, the results of my analysis may likewise be inaccurate or incomplete.

For this analysis, I relied on the following data and information:

- Various Enrollment and Capitation reports from DHS that provide detail by rate cell for each health plan for January 2006 through June 2007;
- Copies of the Minnesota State Supplement Report #1, Statement of Revenue, Expenses and Net Income for each health plan for 2006, as submitted to the State of Minnesota;
- Restated net hospital and medical expenses for Medicaid-covered services provided by the health plans, based on more recent experience, including information on reinsurance recoveries. I also requested from each health plan a certification by a qualified actuary that the restatement reflects a best estimate. I am following up with the plans from which I have not yet received certifications;
- Certifications, provided by the health plans, certifying the percentage of expenses that were for non-State Plan services; and
- Miscellaneous data and information provided by DHS and the health plans.

I also received and reviewed the health plans' 2008 CMS Medicare Advantage and Part D bid forms. I have performed a limited review of the data used directly in my analysis for reasonableness and consistency and have not found material defects in the data. If there are material defects in the data, it is possible that they would be uncovered by a detailed, systematic review and comparison of the data to search for data values that are questionable or for relationships that are materially inconsistent. Such a review was beyond the scope of this assignment.

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The following provides an overview of the rate development, a summary of the rate adjustments, and describes the analysis that was performed.

Overview of Rate Development

For this preliminary analysis, rate levels have been set to target a contribution to surplus equal to 0.75% for the health plans in aggregate. The structure, assumptions, and data used in the development of the rates are summarized below:

- I. The base utilization and cost data used to determine the rate levels is actual experience for Medicaid-covered services for calendar year 2006 for the MSHO and MSC populations enrolled in managed care programs in Minnesota. This analysis includes MSHO data from seven of the nine plans (91.7% of enrollment) and MSC data from six of the nine plans (72.3% of enrollment). Experience for the other plans was not available in the format I requested or involved unresolved data issues. This analysis reflects the experience of 87.6% of combined MSHO and MSC enrollment. I assumed that all nursing facility costs are covered by the add-on rate, not the basic care rate.
- II. Demographic rates vary by eligibility category, age and gender, and geographic location. Current eligibility categories include aged institutionalized and aged non-institutionalized.
- III. Rate relationships for dual eligible seniors, which recognize the impact of Part D on Medicaid program costs, were developed in 2005 based on actual claim experience from 2001 through 2004. Current rate relationships for non-duals by demographic rate cell were developed in 2002. They are based on actual claim experience from 2000-2001. New rate relationships for all seniors are being developed for 2008. The new relationships are based on actual claim experience from 2004-2006 for the aged populations enrolled in managed care programs in Minnesota.
- IV. Adjustments are made for trends in utilization and cost per service, on a combined basis. The trends are based on historical claim trends from 2004 to 2006 for public program populations enrolled in managed care programs in Minnesota and on benchmark utilization and provider payment rates for public programs including the Medicare fee-for-service program. Adjustments were considered to the historical trends to reflect factors that might have a different impact on future claim trends.
- V. Administrative expenses are assumed to be 8.89% of total expenses in 2006, based on actual adjusted health plan experience for 2006 for the PMAP, PGAMC, and MNCare programs, as discussed in my letter regarding Trend & Surplus for those programs.

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- VI. The load for the 2008 contribution to surplus in this analysis is 0.75%. I have made an additional adjustment of 0.25% to reflect that over the past two years the plans have, on average, received about 95% of withheld revenue (that is, the plans have on average received 99.75% of targeted revenue).

Development of Recommended Rate Increase

Exhibit A provides a summary of the development of the recommended rate increase (6.37%). Exhibits B and C describe the development of the claim cost trend figures. Exhibit D describes the impact of benefit changes in 2007. Exhibit E describes the calculation of 2007 revenue. The exhibits are discussed below.

Exhibit A

The 2006 Medicaid-covered MSHO and MSC claim cost of \$425.84 reflects average costs of \$388.90 for MSHO (also shown on Exhibit B) and \$596.11 for MSC. These figures in turn were developed from actual data received from the plans (as mentioned above), are before reinsurance, and do not include costs for non-state plan services. For MSC I relied on enrollment figures provided by DHS since the Minnesota State Supplement Reports #1 completed by the plans do not include this level of detail.

The annual claim cost trend rate of 9.38% shown in Exhibit A is a 50/50 blend of a Benchmark Trend Rate (Exhibit B) and an Experience Trend Rate (Exhibit C). The administrative trend of 3.0% and surplus margin of 0.75% were chosen in consultation with DHS. Based on an analysis of average withhold returned in 2005 and 2006, a withhold adjustment of 0.25% has been included, as described above.

After applying trend, benefit, and surplus adjustments to 2006 claim cost, the recommended rate increase (6.37%) is calculated by comparing this total to average 2007 revenue.

Exhibit B

The benchmark trend rate of 7.59% shown in Exhibit A is developed by applying benchmark trend rates for various service categories to plan data as shown in Exhibit B. The claim costs shown by benefit category were developed using the MSHO data provided by the plans. (The MSC data is not available to me at this level of detail.)

The prescription drug trend of 8.25% is the average of the 2007 and 2008 Target Trends shown in Exhibit H of my letter regarding Trend & Surplus for the PMAP, PGAMC, and MNCare programs.

The benchmark trend rates for Medicare cost sharing are based on Milliman research regarding trends in Medicare cost-sharing for 2007 and projected trends for 2008, including the effect of published increases in the Part A and Part B deductibles. The Part A cost-

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sharing trend of 3.75% reflects the recently-published increase in the Part A deductible for 2008. The Part B cost-sharing trend of 7.0% includes 2008 projected trend components of 6.0% for hospital outpatient and 7.7% for physician cost-sharing.

The trend rates for "Other Medicaid-Covered Costs" are based on the target trends in my Trend & Surplus letter as well as other Milliman research. The "HH/PCA" trend rate of 11% includes an extra 3% in recognition of fee schedule pressure due to COLA increases.

Exhibit C

The Experience-Based trend rate of 11.16% shown in Exhibit A is developed by calculating trend in claim cost for 2004-2006 and backing out trend due to changes in demographic and area mix, as shown in Exhibit C, and the impact of benefit changes. The impact of benefit changes is detailed in my letter regarding Seniors Costs by Demographic Rate Cell (the "rate cell study").

The average claim costs and demographic and area factors shown in Exhibit C were developed using the data provided for that study. This data includes both MSHO and non-MSHO data for certain plans, and non-MSHO data only for other plans. Due to a change in CMS policy related to Part D, there was a significant shift of enrollment from MSC to MSHO in 2006. This shift may explain the increase in the average demographic/area factor and incurred claim cost PMPM in 2006 (since not all plans submitted MSHO data for the rate cell study).

Exhibit D

The aggregate impact of 2007 benefit changes on claim cost is calculated as the revenue-weighted average of the adjustment factors for each group of rate cells (institutionalized and non-institutionalized). These adjustment factors were developed in my November 30, 2006 letter regarding benefit changes for 2007.

Exhibit E

The 2007 revenue figure of \$526.47 shown on Exhibit A is calculated as the weighted average capitation rate among enrollees whose data is reflected in the average 2006 claim costs of \$425.84 (Exhibit A). The calculation of 2007 revenue is shown on Exhibit E.

The 2007 capitation rates used for this calculation reflect the recently-developed rate relativities and have been adjusted to reflect that the MCOs receive the MERC amount for MSHO enrollees (except Non-MC MSHO enrollees). I understand that the MERC amount received by the plans for these dual-eligible MSHO enrollees is subject to ratable reductions, whereas MERC carve-outs are not subject to ratable reductions.

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Ms. Pam Parker

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November 19, 2007



Pam, I am available for questions by phone at [REDACTED] and by e-mail at [REDACTED]

Sincerely,

Leigh M. Wachenheim, FSA, MAAA
Principal & Consulting Actuary

LMW/ral

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Exhibit A: Recommended Rate Increase for 2008 Rates – Seniors

(a) 2006 Medicaid-Covered MSHO & MSC Claim Cost	\$ 425.84	
(b) Annual Trend Rate - Benchmark	7.59%	Exhibit B
(c) Annual Trend Rate - Experience	11.16%	Exhibit C
(d) Annual Trend Rate - 50/50 Blend	9.38%	= (b + c) / 2
(e) Projected 2008 Claim Cost	\$ 509.45	= (a) * (1 + d) ^ 2
(f) Administrative Margin	8.89%	
(g) 2006 Administrative Cost	\$ 41.55	= (a) * (f) / (1 - f)
(h) Administrative Trend Rate	3.00%	
(i) Projected 2008 Administrative Cost	\$ 44.08	= (g) * (1 + h) ^ 2
(j) Preliminary 2008 Claim and Administrative Cost	\$ 553.53	= (e) + (i)
(k) Impact of 2007 Benefit Changes	1.0016	Exhibit D
(l) Projected 2008 Claim and Administrative Cost	\$ 554.43	= (j) * (k)
(m) Surplus Margin (Including Withhold Adjustment)	1.00%	
(n) Projected 2008 Required Revenue	\$ 560.03	= (l) / (1 - m)
(o) 2007 Revenue	\$ 526.47	Exhibit E
(p) Recommended Rate Increase for 2008 Rates	6.37%	= (n) / (o) - 1

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Exhibit B: Benchmark Trend Rate

Item	Benchmark	
	2006 Claim Cost	Annual Trend Rate
<u>Drug Costs</u>		
Non-Medicare-covered drugs	12.61	8.25%
<u>Part C Cost Sharing</u>		
Medicare Part A cost sharing	62.79	3.75%
Medicare Part B cost sharing	117.39	7.00%
<u>Other Medicaid-Covered Costs</u>		
Dental	12.81	5.50%
HH, PCA	118.72	11.00%
All other Non-Medicare services	64.59	6.25%
<u>Total Medicaid-Covered Costs</u>		
Subtotal	388.90	450.20
Reinsurance recoveries	-	-
Grand Total	388.90	7.59%

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Exhibit C: Experience-Based Trend Rate

Average Demog/Area Factor *	<u>2004</u>	<u>2005</u>	<u>2006</u>
Trend in Demog/Area Factors	0.9703	0.9837	1.2127
		1.38%	23.28%
Incurred Claim Cost PMPM *	<u>2004</u>	<u>2005</u>	<u>2006</u>
Claim Cost Trend	378.76	418.92	584.73
Net of Trend in D/A Factors		10.60%	39.58%
		9.10%	13.22%
50/50 Weighted Average Trend			11.16%

* Avg Demog/Area Factors and Incurred Claim Costs are based on data used in the preliminary seniors rate cell analysis performed earlier this year.

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Exhibit D: Impact of Benefit Changes in 2007

Item	Rate Cells	
	Inst.	Non-Inst.
Adj Factor for Rate Increase for CA MH Providers	1.0004	1.0004
Adj Factor for Adult MH Rehab Services (ARMHS & Crisis)	1.0001	1.0015
Composite Adjustment Factor for 2007 Benefit Changes	1.0005	1.0019
Distribution of Revenue (Exhibit E)	18.79%	81.21%
Aggregate Impact of 2007 Benefit Changes on Claim Cost		1.0016

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Exhibit E: 2007 Revenue

Rate Cell	Hennepin	Ramsey	Greater Metro	Core Metro	North East	North Central	Carver	South West	Olmsted	South East	Total
65 - 74	3,370	1,303	375	814	566	2,329	140	841	227	1,731	11,896
75 - 84	6,886	3,586	886	2,704	2,368	7,603	279	2,949	609	6,043	33,918
85 +	11,621	6,445	2,479	5,983	5,100	19,867	699	9,288	1,543	14,473	77,498
All Ages - Non MC	213	31	19	33	40	52	-	8	8	63	467
65 - 74	2,376	913	182	617	563	1,859	68	852	234	1,289	8,953
75 - 84	2,810	1,190	387	1,122	916	3,587	83	1,678	232	2,667	14,672
85 +	1,787	1,048	335	1,006	1,106	4,527	128	1,873	209	3,530	15,549
All Ages - Non MC	171	40	10	6	10	42	-	11	8	25	323
65 - 74	19,989	11,851	1,567	10,221	4,130	14,234	477	5,504	2,047	8,916	78,336
75 +	22,516	13,326	3,539	11,857	5,698	27,206	887	10,964	3,403	19,616	119,011
All Ages - Non MC	6,171	1,855	97	1,174	117	361	51	292	439	369	10,926
65 - 74	11,754	6,192	731	4,221	2,424	8,287	146	3,084	1,238	5,143	43,220
75 +	8,438	4,399	681	3,285	1,162	7,819	258	3,400	1,212	5,769	36,423
All Ages - Non MC	4,241	1,560	58	635	74	240	27	359	395	177	7,766
Total	102,343	53,739	11,346	43,678	24,274	98,012	3,243	41,103	11,804	69,816	459,358
2007 Capitation Rates Recalculated using Average 2007 Capitation Rate and Recommended Adjustment Factors (Including MERC received by MCOs)											
65 - 74	\$ 549.79	\$ 661.85	\$ 470.47	\$ 472.62	\$ 281.92	\$ 359.46	\$ 352.82	\$ 348.84	\$ 336.53	\$ 336.87	\$ 451.04
75 - 84	\$ 384.62	\$ 460.78	\$ 327.36	\$ 328.84	\$ 196.05	\$ 250.31	\$ 245.28	\$ 242.81	\$ 234.43	\$ 234.71	\$ 300.56
85 +	\$ 269.94	\$ 323.16	\$ 229.89	\$ 230.69	\$ 137.54	\$ 175.61	\$ 172.03	\$ 170.34	\$ 164.48	\$ 164.57	\$ 202.56
All Ages - Non MC	\$ 2,318.47	\$ 2,887.92	\$ 2,058.70	\$ 2,058.70	\$ 1,236.90	\$ 1,571.11	\$ 1,532.91	\$ 1,532.91	\$ 1,472.67	\$ 1,472.67	\$ 2,009.44
65 - 74	\$ 538.31	\$ 650.23	\$ 461.42	\$ 463.90	\$ 277.03	\$ 353.29	\$ 345.48	\$ 343.24	\$ 331.04	\$ 331.14	\$ 432.91
75 - 84	\$ 426.38	\$ 512.65	\$ 364.06	\$ 365.75	\$ 218.04	\$ 278.38	\$ 273.33	\$ 270.02	\$ 260.78	\$ 260.97	\$ 326.47
85 +	\$ 351.78	\$ 423.22	\$ 301.19	\$ 302.19	\$ 180.22	\$ 229.99	\$ 225.40	\$ 222.95	\$ 215.02	\$ 215.59	\$ 255.32
All Ages - Non MC	\$ 2,318.47	\$ 2,887.92	\$ 2,058.70	\$ 2,058.70	\$ 1,236.90	\$ 1,571.11	\$ 1,532.91	\$ 1,532.91	\$ 1,472.67	\$ 1,472.67	\$ 2,132.29
65 - 74	\$ 656.36	\$ 795.37	\$ 565.56	\$ 567.64	\$ 338.94	\$ 432.42	\$ 422.67	\$ 420.02	\$ 405.17	\$ 405.72	\$ 554.74
75 +	\$ 787.94	\$ 951.39	\$ 676.61	\$ 678.93	\$ 404.73	\$ 517.43	\$ 506.20	\$ 502.11	\$ 484.62	\$ 485.05	\$ 624.79
All Ages - Non MC	\$ 1,765.67	\$ 2,199.34	\$ 1,567.83	\$ 1,567.83	\$ 941.98	\$ 1,196.50	\$ 1,167.41	\$ 1,167.41	\$ 1,121.53	\$ 1,121.53	\$ 1,722.24
65 - 74	\$ 602.59	\$ 727.81	\$ 517.11	\$ 519.52	\$ 310.35	\$ 395.74	\$ 387.25	\$ 384.69	\$ 370.71	\$ 371.25	\$ 504.47
75 +	\$ 843.86	\$ 1,022.01	\$ 727.56	\$ 728.80	\$ 434.91	\$ 555.56	\$ 544.25	\$ 539.69	\$ 520.39	\$ 521.05	\$ 685.48
All Ages - Non MC	\$ 1,663.31	\$ 2,071.84	\$ 1,476.95	\$ 1,476.95	\$ 887.37	\$ 1,127.14	\$ 1,099.74	\$ 1,099.74	\$ 1,056.51	\$ 1,056.51	\$ 1,632.08
Total	\$ 729.79	\$ 834.93	\$ 512.41	\$ 571.28	\$ 291.74	\$ 383.86	\$ 385.42	\$ 373.64	\$ 436.91	\$ 358.75	\$ 526.47

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