

Southeastern Actuaries Conference
Spring Meeting June 23-25, 2004

Individual and Small Group Medical Products

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Current Amount Spent on Health Care (in billions)

	Hospital	Nursing Home	Home Health	Physician	Rx	OTC Drugs	Dental/ Vision	Misc.	Admin	Total Private Mkt.	Total All
Individual <age 65	\$15	\$1	\$1	\$19	\$7	\$1	\$5	\$5	\$15	\$61	\$69
Small Group <age 65	40	2	3	50	18	2	10	11	28	147	164
Large Group <age 65	113	8	7	148	60	7	34	21	57	399	455
Medicaid <age 65	77	0	4	16	21	0	8	4	7		138
Medicaid >age 65	24	0	1	6	7	0	2	6	2		47
Medicaid – LTC	0	83	0	0	0	0	0	0	6		89
Medicare – Program pd	131	24	16	79	4	0	0	10	6		269
Medicare OOP-cvsv	8	0	0	15	0	0	0	0	0		23
Non-Medicare >age 65	0	30	6	3	33	8	31	5	0		116
Uninsured	37	0	1	25	5	1	1	6	0		75
Other Public	67	0	0	25	8	0	3	110	3		215
Total	\$511	\$148	\$38	\$385	\$163	\$19	\$93	\$178	\$124	\$607	\$1,660

Average Health Care Cost of Basic Population

	Cost (Excluding Admin)	Popu- lation	Cost Per Person	OOP Exc.	Revised Cost PP	Total Relativity
Private Market	588	160	3,675	0	3,675	1.00
Medicaid	259	36	7,194	0	7,194	1.96
Medicare	263	40	6,575	139	10,050	2.73
Uninsured	75	43	1,744	35	2,558	0.70
Other Public	212	11	19,273	0	19,273	
Other (seniors)	139					
Total	1,536	290	5,266			

Note: Bad debt for uninsured estimated at \$35 billion in other studies

Who Pays for Health Care

Description	Estimated for 2000			Annual Trend 1975- 2000	Estimated Cost 2002
	Population (millions)	Total Cost (billions)	Cost/ Pop		
Medicare	39	\$225	\$5,769	1.092	\$255
Medicaid	36	188	5,222	1.081	510
Uninsured	42	32	762	1.067	586
Individual	16	36	2,250	1.102	625
Small Group	36	85	2,361	1.099	705
Large Group	111	250	2,252	1.095	1,035
Other		454		1.081	480
Total	280	\$1,270	\$4,536	1.083	1,500

Current System in 2003

Market	Population (millions)	Bill-all Services Cost Med	Cost Per Person	Admin %	1-OOP Benefit %	Admin Only	Benefit Cost w/Admin	Insurance Only		Cost Per Person Benefit Only	Exp Ratio to LG bnct
								Benefit Cost	Total Cost		
Ind	15	46.0	3066.7	0.3	0.8	16.4	54.5	38.2	62.4	2545.3	1.0
SG	32	114.0	3562.5	0.2	0.9	30.6	133.2	102.6	144.6	3206.3	1.2
LG	112	336.0	3000.0	0.1	0.9	45.1	361.0	315.8	381.1	2820.0	1.0
Medicare	40	335.0	8375.0	0.0	0.8	6.1	270.7	264.7	341.1	6616.3	2.8
Medicaid	38	270.0	7105.3	0.1	1.0	15.7	285.7	270.0	285.7	7105.3	2.4
Uhinsured	43	77.0	1790.7	0.0	1.0	0.0	77.0	77.0	77.0	1790.7	0.6
Msc	10	*									
Subtotal	290	1178.0				113.9			1291.9		
LTC-NM		35.0				1.0					
Home Health		30.0				1.0					
Dental		85.0				3.0					
Other gov		178.0				5.0					
OTC Rx		15.0									
Rx65+		above									
65+ oop		above									
Vision		15.0									
Subtotal		358.0				10.0			368.0		
Grand Total		1536.0				123.9			1659.9		

* included in other government
Med OOP coins and lack of rx

Factors Causing Problems

- Tax Code
- Medicare
- Medicaid
- Uncompensated Care (Uninsured)
- Mandated Benefits
- Rating Restrictions
- Other Regulations

Individual Market

Serious Issues Facing Market

- Cost and cost shifting
- Mandated benefits
- Underwriting restrictions
- Rating
- Compliance
- Other

Market Characteristics

- Transitional in Nature – 3 year average
- Lapse of 35-50% year 1, 20-30% renewal years
- Trend of 10-15% per year before aging
- Adverse selection against rate increase vs. normal lapse / durational experience
- Deductible increasing over time (often 1,000+ avg) and leveraging
- Market is competitive in some states, not in others

Estimated Impact (trend increase) in Market Costs - 1954 to Present

Description of Factor	Estimated Range of Impact
Cost Shift	15-50%
Mandated Benefits	5-45%
Underwriting/Rating Restrictions	0-100%+
Personal Responsibility/Product Mix	0-30%
Tax Equity	Affordability Effect Only
Uninsured/Uninsurable/Insurer of Last Resort	Minimal Effect
Small Group Market Reform	Minimal Effect
Administrative Costs	An Increase Relative to Group
Composite	20-225%

Profitability Illustration

Percentage of Income
Average – Not Target

Average Policy Year							
	0-6 Mo	6-12	2	3	4	5+	Lifetime
Premium	0.50	0.50	1.00				1.00
Investment Income	-	0.01	0.02	0.025	0.075		0.020
Incurred Claims	0.20	0.32	0.70	0.74	0.76	0.78	0.0690
Expenses	0.40	0.14	0.225	0.220	0.215	0.210	0.305
Gain/(Loss)	(0.10)	0.05	0.055	0.045	0.050	0.035	0.025

Benefit Design and Underwriting Issues

- Risk versus Lean Plan (Marketing Direction)
- Underwriting and Caliper of Risk
(Preferred, Standard, Substandard, Imp Riders)
- Experience characteristics by bucket
(benefits, underwriting)
- Other (age, area, industry, leverage, discretion)

Types of Rating Strategies

- A. Form Position
 - 1. Closed/Open Method
 - 2. Always Open
- B. Condition/Experience Recognition
 - 1. At Issue Only*
 - 2. At Issue and Renewal (more limited at renewal)
- C. Durational Recognition
 - 1. None
 - 2. Limited, Much Less Than Actual

* Includes condition-related discounts or rate-ups and/or impairment riders.

Types of Rating Strategies

(continued)

D. Age/Sex

1. For Each Age by Sex
2. By Groups of Age by Sex

E. Other

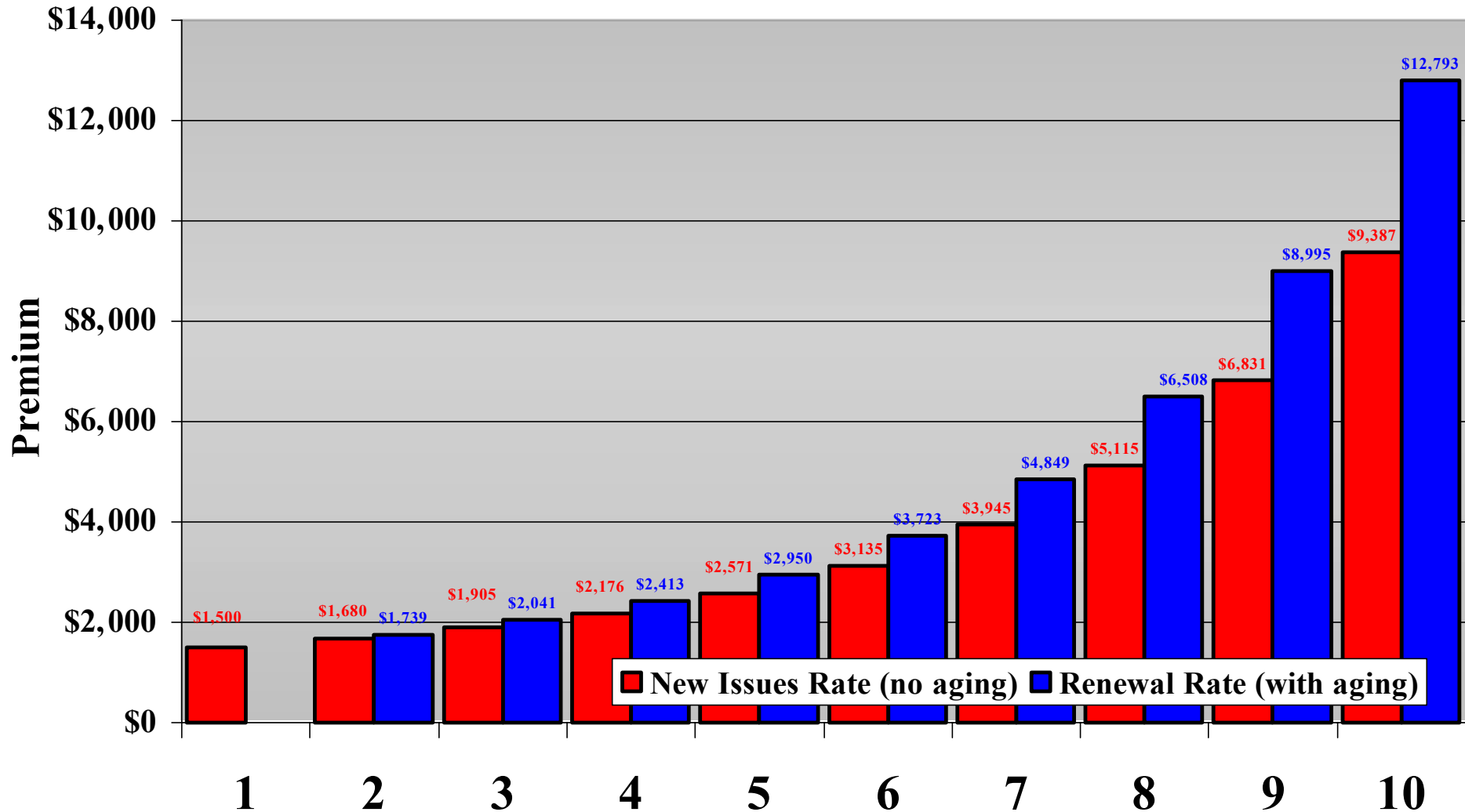
1. Benefit Driven (Mandates)
2. Risk Driven (Generally Included or Options)

Case Studies of Strategies A & B

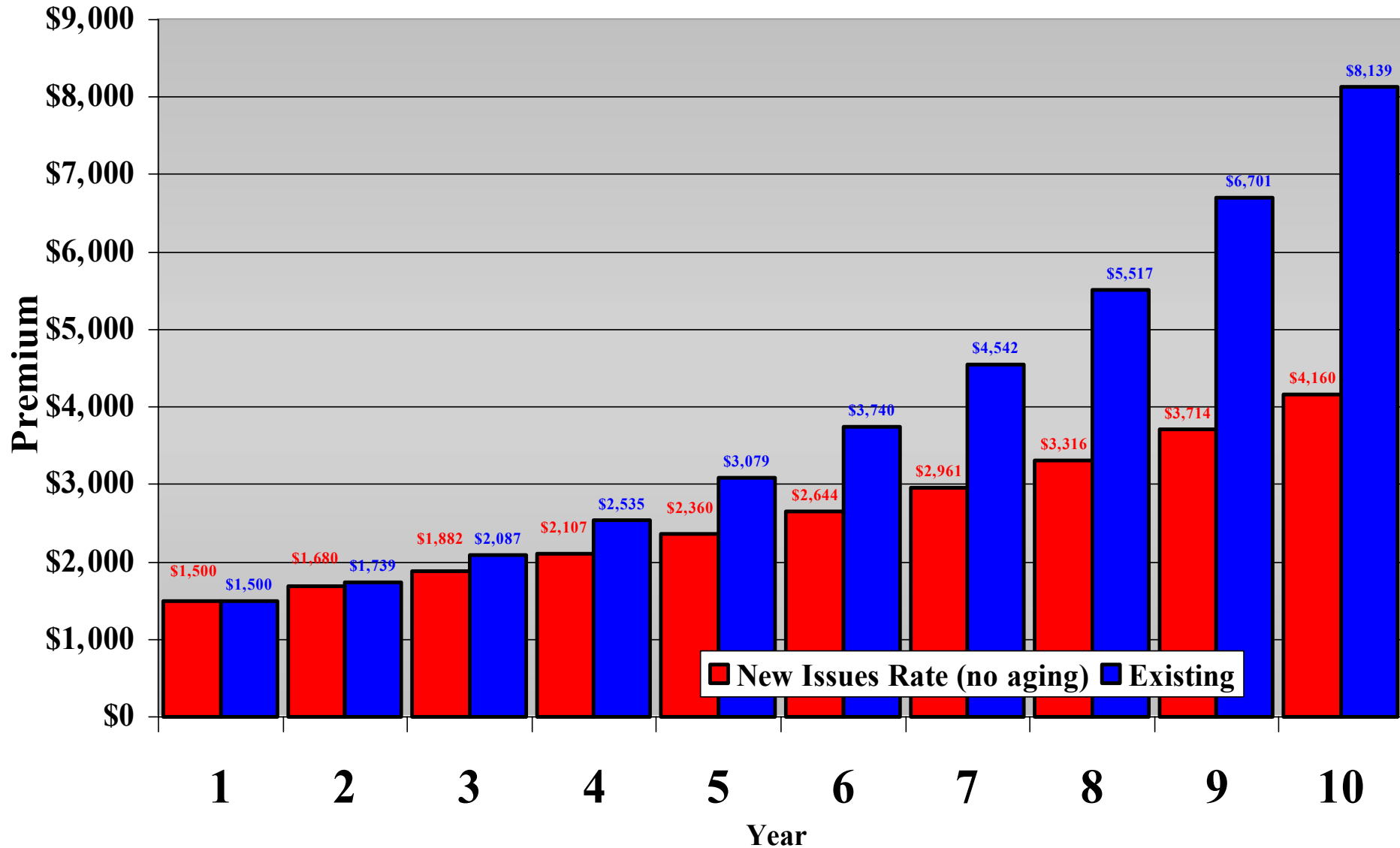
Underlying Assumptions

- Annual Trend 12%
- Annual Aging 3.5%
- New Business increases by 0.25% for every 1% decrease in rates and vice versa
- Lapse increases by 0.25% for every 1 point increase in renewals, premiums and vice versa
- Adverse Selection impact based on probability distributions under standard cost distribution relativities for all services from the 2001 Milliman *Health Cost Guidelines*
- Durational Rating Models based on similar relationships using constant durational increase (0.25% relative to rate) every year
- Rate increases equal to trend plus aging plus adverse selection due to rate increase

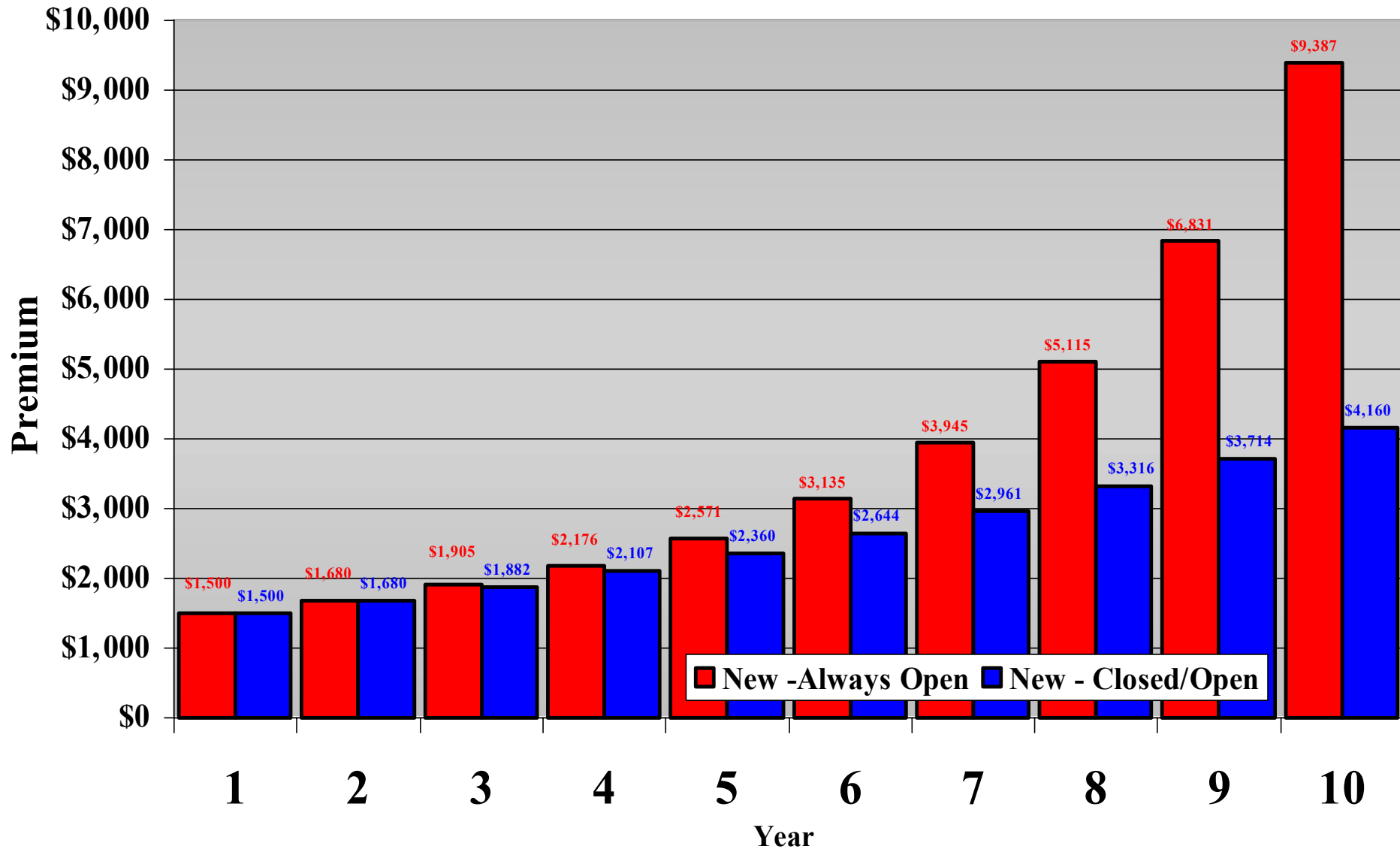
Illustrative Average Premiums Under Always Open Method over 10 Years with New Issues and Renewal Business at Same Annual Premium



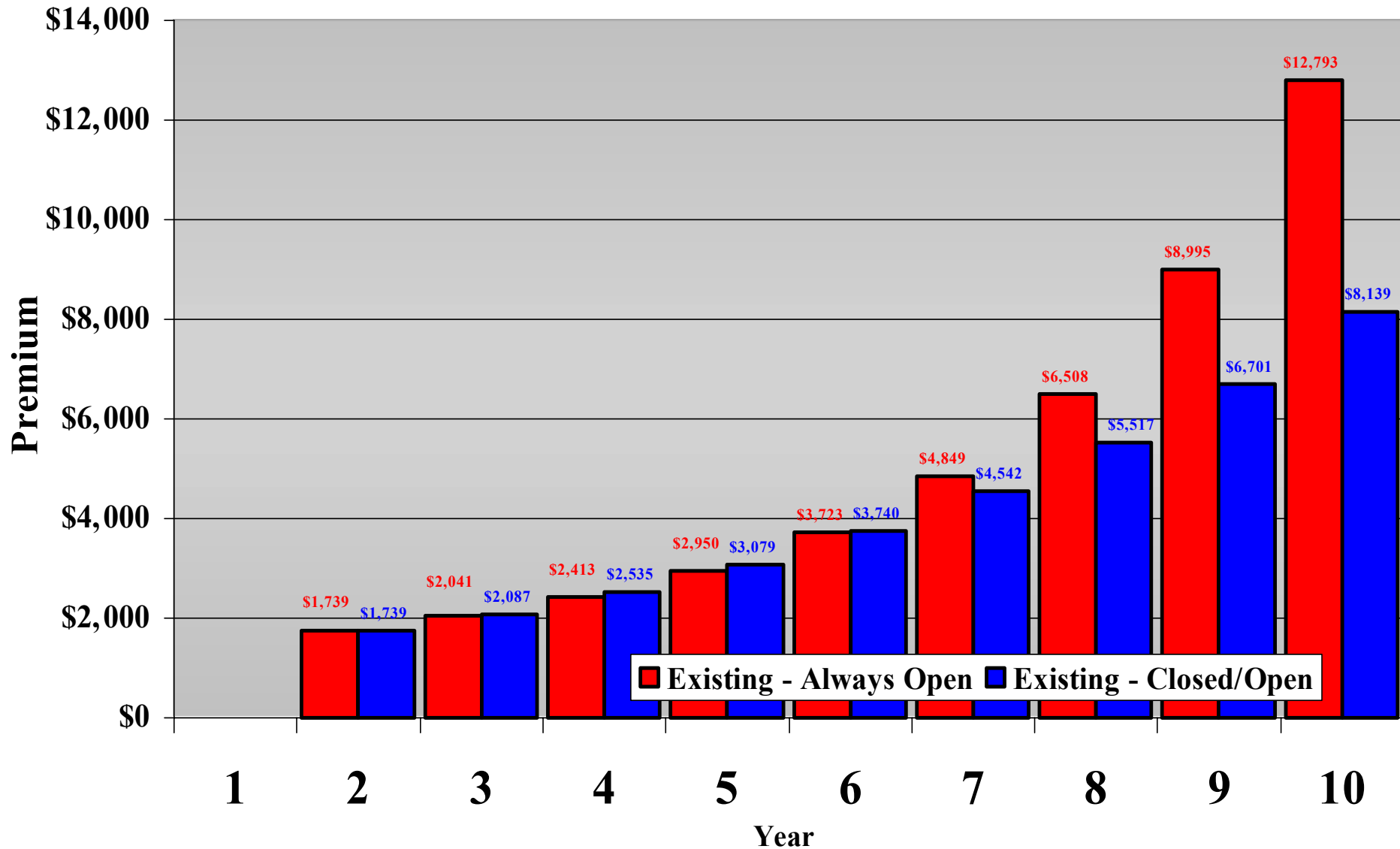
Illustrative Average Premiums Under Closed/Open Method over 10 Years with New Issues and Existing Business Rates



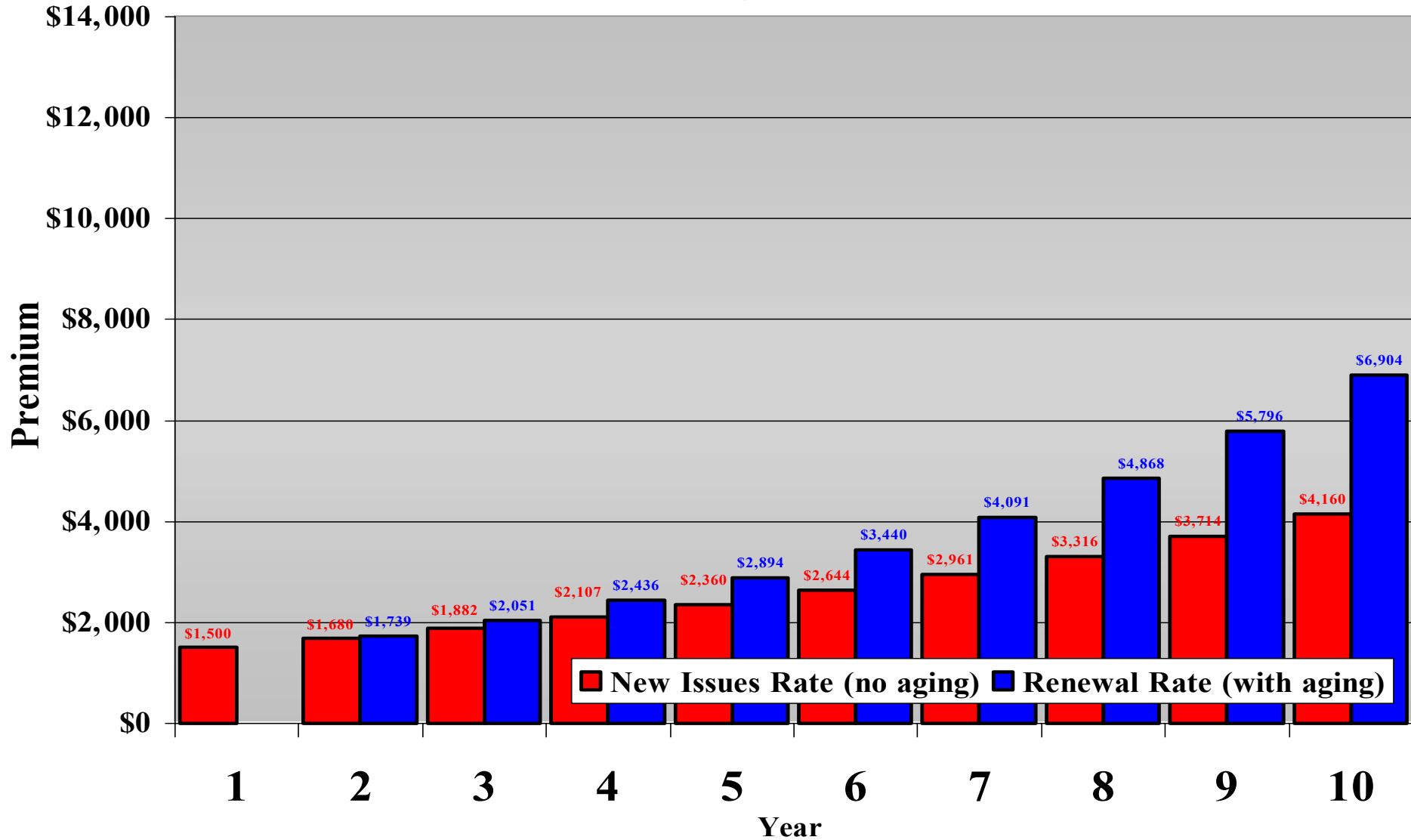
Comparison of New Business Rates Always Open vs. Closed/Open Approach



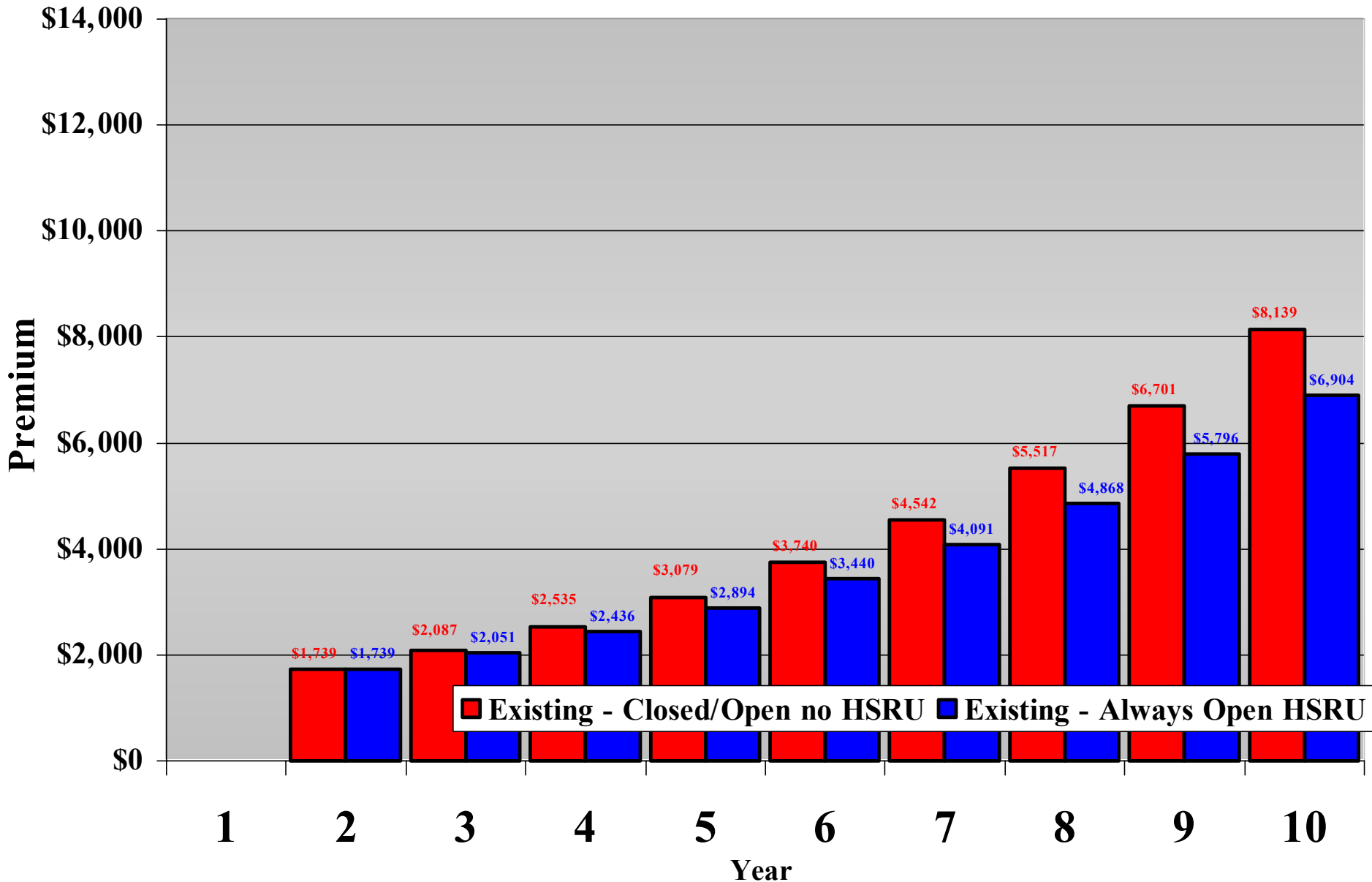
Comparison of Existing Business Rates Always Open vs. Closed/Open Approach



Illustrative Average Premiums Under Health Status Renewal Underwriting (HSRU) Method over 10 Years with New Issues and Renewal Business at Same Annual Premium



Comparison of Existing Business Premiums for Closed/Open no HSRU vs. Always Open HSRU (note: new business rates are the same)



Compliance Ranking

Ranking	Number of States	States
<p>Viable – Profit potential exists with prudent company management due to a combination of reasonable if not favorable regulatory environment in the state and external influences that do not appear to be causing rapidly rising trends due to cost shifting.</p>	14	AR, IL, IN, IO, MI, MT, NE, OH, OK, PA, TN, TX, VA, WI
<p>Between Viable & Questionable – This category indicates a state where some carriers maybe profitable, but often that may be the case only in local markets. Further market adjustments will be needed in the future so that this state can become viable in all cases.</p>	11	AR, CA, GA, ID, KA, MO, NC, ND, SC, SD, WY
<p>Questionable – The market has recently been deteriorating and indications are that future profitability is questionable for most companies.</p>	12	AK, CT, DE, FL, HI, KT, MN, NV, NH, UT, WV, DC
<p>Poor – Carriers could lose money due to the regulatory environment and/or substantial cost shifting – unlikely to improve without substantial modifications.</p>	14	AL, CO, LA, ME, MD, MA, MS, NJ, NM, NY, OR, RI, VT, WA

Market Summary

- Individual market is perhaps nearing a crossroads (driven by numerous trends)
- Biggest risk continues to be growing costs and restrictive regulation
- Biggest opportunity comes from group market and health care system perils
- Market will ultimately prosper only if flaws in current system are fixed

Small Group Market

Serious Issues Facing Market

- Cost and Cost Shifting
- Guarantee Issue / Risk Selection
- Rating Bands
- Discounts / Networks
- Regulations

Characteristics

- Averse selection varies by state, but very serious in general
- Lapse rate about 25%
- 2-5 life employee groups serious problems
- Trend at least 10-20%+ per year before aging
- Cost sharing escalating significantly
- Market in trouble in many states

Estimated Impacted in Market 1954 to Present

- Cost shift – 15-50%
- Mandated Benefits - Less than individual market – less than 5%
- Underwriting/Rating Restrictions – 3-50%
- Personal Responsibility – 0-50%
- Composite 20-160%

Profitability Illustration

Percentage of Income
Average – Not Target

	Policy Year		
	1	2+	Lifetime
Premium	1.000	1.000	1.000
Investment Income	0.010	0.025	0.020
Claims	0.650	0.800+	0.760+
Experience	0.320	0.200	0.230
Gain/Loss	0.040	0.025	0.030-

Benefit Design and Underwriting Issues

- Rich versus Lean Benefits (market direction)
- Underwriting Tiers
- Experience Characteristics by Bucket
- Other (size, discounts, etc.)

Rating Issues

- Durational Targets
- Networks
- Exemptions

Compliance Ranking

Ranking	Number of States	States
<p>Viable – Profit potential exists with prudent company management due to a combination of reasonable if not favorable regulatory environment in the state and external influences that do not appear to be causing rapidly rising trends due to cost shifting.</p>	7	IL, IN, IA, NB, OH, TN, WI
<p>Between Viable & Questionable – This category indicates a state where some carriers maybe profitable, but often that may be the case only in local markets. Further market adjustments will be needed in the future so that this state can become viable in all cases.</p>	10	AR, DE, GA, ID, MI, OK, PA, TX, VI, WV
<p>Questionable – The market has recently been deteriorating and indications are that future profitability is questionable for most companies.</p>	17	CO, CT, HI, KA, LA, MO, MT, NJ, NV, NC, ND, OR, SC, SD, UT, WY, DC
<p>Poor – Carriers could lose money due to the regulatory environment and/or substantial cost shifting – unlikely to improve without substantial modifications.</p>	17	AL, AK, AZ, CA, FL, KY, ME, MD, MA, MN, MS, NH, NM, NY, RI, VT, WA

Market Summary

- Market in Trouble (Washington debates)
- Biggest issues continue to be growing costs and regulations
- Biggest opportunities – consumer driven plans and changes in regulations
- Market will only prosper if flaws in current system are fixed