

State: Rhode Island **Filing Company:** Blue Cross & Blue Shield of Rhode Island
TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.003 Small Group Only
Product Name: Small Group Commercial Medical
Project Name/Number: Small Group Medical Rating Factors for 2013 Dec Filing/SGM-201212

Filing at a Glance

Company: Blue Cross & Blue Shield of Rhode Island
Product Name: Small Group Commercial Medical
State: Rhode Island
TOI: H15G Group Health - Hospital/Surgical/Medical Expense
Sub-TOI: H15G.003 Small Group Only
Filing Type: Rate
Date Submitted: 12/07/2012
SERFF Tr Num: BCBS-128801388
SERFF Status: Assigned
State Tr Num:
State Status: Open-Pending Actuary Review
Co Tr Num: SGM-201212
Implementation: On Approval
Date Requested:
Author(s): Jeffrey McLane, Catherine Mitchell, Sean Neylon
Reviewer(s): Herbert Olson (primary), Adrienne Evans, Sandra West, Charles DeWeese, Maria Casale
Disposition Date:
Disposition Status:
Implementation Date:

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General Information

Project Name: Small Group Medical Rating Factors for 2013 Dec Filing Status of Filing in Domicile:
 Project Number: SGM-201212 Date Approved in Domicile:
 Requested Filing Mode: Review & Approval Domicile Status Comments:
 Explanation for Combination/Other: Market Type: Group
 Submission Type: New Submission Group Market Size: Small
 Group Market Type: Employer, Association Overall Rate Impact: 5.1%
 Filing Status Changed: 12/10/2012 Deemer Date:
 State Status Changed: 12/10/2012 Submitted By: Sean Neylon
 Created By: Sean Neylon
 Corresponding Filing Tracking Number:
 PPACA: Not PPACA-Related
 PPACA Notes: null
 Include Exchange Intentions: No
 Filing Description:
 Small Group Commercial Medical Updated Rating Factors for new and renewal business effective January 1, 2013 through December 1, 2013 including Rhode Island Builders Association groups effective November 1, 2012 and HealthPact groups

Company and Contact

Filing Contact Information

Sean Neylon, Actuarial Project Analyst sean.neylon@bcbsri.org
 500 Exchange Street 401-459-1278 [Phone] 1278 [Ext]
 Providence, RI 02903

Filing Company Information

Blue Cross & Blue Shield of Rhode Island CoCode: 53473 State of Domicile: Rhode Island
 500 Exchange Street Group Code: Island
 Providence, RI 02903 Group Name: Company Type: Health Insurance
 (401) 459-1000 ext. [Phone] FEIN Number: 05-0158952 State ID Number:

Filing Fees

Fee Required? Yes
 Fee Amount: \$125.00
 Retaliatory? No
 Fee Explanation: Five products times \$25 per product
 Per Company: Yes

Company	Amount	Date Processed	Transaction #
Blue Cross & Blue Shield of Rhode Island	\$125.00	12/07/2012	65544442

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Rate Information

Rate data applies to filing.

Filing Method: Review and Approval
Rate Change Type: Increase
Overall Percentage of Last Rate Revision: 5.100%
Effective Date of Last Rate Revision: 01/01/2013
Filing Method of Last Filing: Review and Approval

Company Rate Information

Company Name:	Company Rate Change:	Overall % Indicated Change:	Overall % Rate Impact:	Written Premium Change for this Program:	# of Policy Holders Affected for this Program:	Written Premium for this Program:	Maximum % Change (where req'd):	Minimum % Change (where req'd):
Blue Cross & Blue Shield of Rhode Island	Increase	5.100%	5.100%	\$19,242,000	33,869	\$398,050,000	3.100%	7.100%

Product Type:	HMO	PPO	EPO	POS	HSA	HDHP	FFS	Other
Covered Lives:		59,890		1,743	5,389			
Policy Holders:		30,572		931	2,365			

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Rate Review Detail

COMPANY:

Company Name: Blue Cross & Blue Shield of Rhode Island
HHS Issuer Id: 53473
Product Names: HealthMate Coast to Coast
 HealthMate Coast to Coast HDHP
 HealthMate Coinsurance Option
 HealthMate for HSA
 HealthMate for HRA
 BlueSolutions for HSA
 BlueSolutions for HRA
 Classic
 VantageBlue Coinsurance
 BlueChip
Trend Factors: Baseline trend increase of 7.5%; net of new PBM contract @ 1/1/2013 and demographics, effective trend is 2.9%

FORMS:

New Policy Forms:
Affected Forms:
Other Affected Forms: FRONT GRP (09-10); SUMMARY GRP (09-10); INTRODUCTION GRP (09-10); ELIGIBILITY GRP (09-10); COVERED GRP (09-10); EXCLUSIONS GRP (09-10); HOW WE PAY GRP (09-10); COB GRP (09-10); APPEALS GRP (09-10); GLOSSARY GRP (09-10).

REQUESTED RATE CHANGE INFORMATION:

Change Period: Annual
Member Months: 804,264
Benefit Change: None
Percent Change Requested: Min: 3.1 Max: 7.1 Avg: 5.1

PRIOR RATE:

Total Earned Premium: 378,809,000.00
Total Incurred Claims: 322,015,000.00
Annual \$: Min: 462.00 Max: 471.00 Avg: 480.00

REQUESTED RATE:

Projected Earned Premium: 398,050,000.00
Projected Incurred Claims: 331,353,000.00
Annual \$: Min: 486.00 Max: 495.00 Avg: 504.00

SERFF Tracking #:

BCBS-128801388

State Tracking #:

Company Tracking #:

SGM-201212

State:

Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI:

H15G Group Health - Hospital/Surgical/Medical Expense/H15G.003 Small Group Only

Product Name:

Small Group Commercial Medical

Project Name/Number:

Small Group Medical Rating Factors for 2013 Dec Filing/SGM-201212

Rate/Rule Schedule

State: Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.003 Small Group Only

Product Name: Small Group Commercial Medical

Project Name/Number: Small Group Medical Rating Factors for 2013 Dec Filing/SGM-201212

Item No.	Schedule Item Status	Document Name	Affected Form Numbers (Separated with commas)	Rate Action	Rate Action Information		Attachments
1		2013 Small Group Cover Memorandum	FRONT GRP (09-10), SUMMARY GRP (09-10), INTRODUCTION GRP (09-10), ELIGIBILITY GRP (09-10), COVERED GRP (09-10), EXCLUSIONS GRP (09-10), HOW WE PAY GRP (09-10), COB GRP (09-10), APPEALS GRP (09-10), GLOSSARY GRP (09-10)	Revised	Previous State Filing Number:		OHIC 2013 Small Group Rate Factor Filing.pdf
					Percent Rate Change Request:	5.100	
2		2013 Small Group Actuarial Memorandum		Other	Previous State Filing Number:		2013 Actuarial Memo - Small Group.pdf
					Percent Rate Change Request:		
3		Exhibit 1 - Small Group		Other	Previous State Filing Number:		SG Exhibit 1 - Template.pdf
					Percent Rate Change Request:		
4		Exhibit 2 - Operating Expense		Other	Previous State Filing Number:		Exhibit 2 -2013 filing (both Large and Small).pdf
					Percent Rate Change Request:		
5		Exhibit 3 - Milliman, Inc. Actuarial Opinion		Other	Previous State Filing Number:		Exhibit 3 Milliman Opinion RIX01 Letter 20121204 doc.pdf
					Percent Rate Change Request:		

SERFF Tracking #:

BCBS-128801388

State Tracking #:**Company Tracking #:**

SGM-201212

State: Rhode Island**Filing Company:**

Blue Cross & Blue Shield of Rhode Island

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Item No.	Schedule Item Status	Document Name	Affected Form Numbers (Separated with commas)	Rate Action	Rate Action Information	Attachments				
6		Exhibit 4 - S & P Rating Report		Other	<table border="1"> <tr> <td>Previous State Filing Number:</td> <td></td> </tr> <tr> <td>Percent Rate Change Request:</td> <td></td> </tr> </table>	Previous State Filing Number:		Percent Rate Change Request:		Exhibit 4 - S and P BCBSRI_Full Analysis_2012.pdf
Previous State Filing Number:										
Percent Rate Change Request:										

December 7, 2012

Mr. Christopher F. Koller
Health Insurance Commissioner
Office of Health Insurance Commissioner
1511 Pontiac Avenue, Bldg. 69-1
Cranston, Rhode Island 02920

Subject: 1) Rating Factors Applicable to Small Group Subscription Rates for Business
Written or Renewed in 2013

Dear Commissioner Koller:

This letter and the attached documents comprise a rate factor filing by Blue Cross & Blue Shield of Rhode Island ("BCBSRI") of claims projection trends, reserve contribution factors, and related rating information to be used in commercial rating of small employer groups.

As you know, premium is driven primarily by medical expenses paid on behalf of our members. This equates to roughly 85% of each premium dollar. Medical expenses are driven by both utilization (frequency and volume) of services and the cost of those services. Since our filing in May of 2012, which relied on medical expenses incurred in calendar year 2011, we have experienced a significant increase in medical expense trend. Because the approved rate factors and rate cap do not reflect this unanticipated escalation in costs, absent this filing, rates for the calendar year 2013 will be inadequate to cover expenses. This filing is necessary to meet our fiduciary obligation to act in a financially prudent manner.

We recognize the burden of high healthcare costs on the businesses and people of Rhode Island and we do not take this filing lightly. Since your September decision on our previous filing, we have conducted various analyses to understand the actual and emerging costs and to test our projections for future medical trend. To ensure that our methods and assumptions in this filing are actuarially sound, we engaged Milliman, Inc to review our filing.

We have identified the following key factors driving our medical expenses:

- Increases in inpatient costs per admission have added about 1% to overall medical spend over the past year.
- Inpatient admissions are up 3.9% over 2011.
- Outpatient costs have increased steadily as more complex and expensive treatments are provided in an outpatient setting. This is particularly driven by a rapid increase in costs associated with specialty outpatient chemotherapy treatment.

These topics are discussed in more detail in the enclosed filing. As a result of these increased medical expenses, among other factors, this filing reflects an overall average rate increase of 5.1%, which is 3.4% higher than the rate cap previously approved by your office. Please note

that while this filing provides for an increase in our 2013 rates over the levels previously approved, the rate increases we are proposing are lower than the Small Group rate increases you have approved over the last four years.

The current 1.7% rate cap places BCBSRI's financial stability in serious jeopardy. After four years of underwriting losses, BCBSRI ranks last among Blue Cross and Blue Shield plans nationwide in financial strength as measured by the amount of Risk Based Capital ("RBC"). Without an increase to the rate cap now, or a much more significant increase to 2014 renewals, BCBSRI's reserve level will fall below 375% RBC by the end of 2014 resulting in sanctions from the Blue Cross and Blue Shield Association.

We recognize that providing affordable healthcare is critical to our customers, members, and the Rhode Island economy. For these reasons, we have undertaken a number of initiatives designed to aggressively transform our business, improve internal operations, and moderate both medical and administrative expense trends. We continue to work collaboratively with our healthcare delivery system partners to develop and implement new approaches that pay for quality, not quantity, of care. These ongoing and important efforts have proven to be successful and are expected to continue for the coming years. Some of the measurable outcomes include:

- We are on target to reduce operating expenses by roughly \$15 million, or 7% in 2013;
- Professional Services costs have decreased by 2.7% due to innovative provider contracting arrangements and the establishment of an enhanced radiology management program;
- A new pharmacy benefit management contract with Catamaran will mitigate pharmacy expenses in 2013. The projected savings resulting from this contract is about \$65 million over three years for group insured business, and reduces the average annual premium increase for employers by roughly 2.2% in this filing.

We respectfully ask for your timely consideration and approval of the proposed rating factors as submitted. We believe that the proposed rating factors are in the best interest of both the public and the corporation and consistent with the proper conduct of our business. As always, we are available and prepared to respond to any questions you, your staff, or your consulting actuary, Mr. DeWeese, may have.

Sincerely,



Michael Hudson, FSA, MBA
Executive Vice President & Chief Financial Officer

ACTUARIAL MEMORANDUM FOR SMALL GROUP COMMERCIAL RATING

Revised Group Rate Factor Filing

Blue Cross & Blue Shield of Rhode Island (“BCBSRI”) submits this filing as an amendment to the 2013 Small Group rating factors approved by the Office of Health Insurance Commissioner in September 2012. This filing results in a 5.1% average renewal increase for the 2013 rating period. This average increase replaces the 1.7% rate cap that was previously approved in September 2012.

Several factors contribute to the expected average increase, with the major factor being an updated claims experience base (2.4% impact)¹. Our expectation of future trend has increased modestly as well (0.2% impact). Finally, the operating expenses included in this filing are consistent with the expenses originally filed by BCBSRI in May 2012 (0.8% impact). This filing also addresses BCBSRI’s reserve position and rate cap compliance.

This filing will apply to all 2013 new and renewal business. Please note, however, that an account which has already received a new business or renewal rate prior to the approval of this filing will not receive an additional rate change.

Financial Results

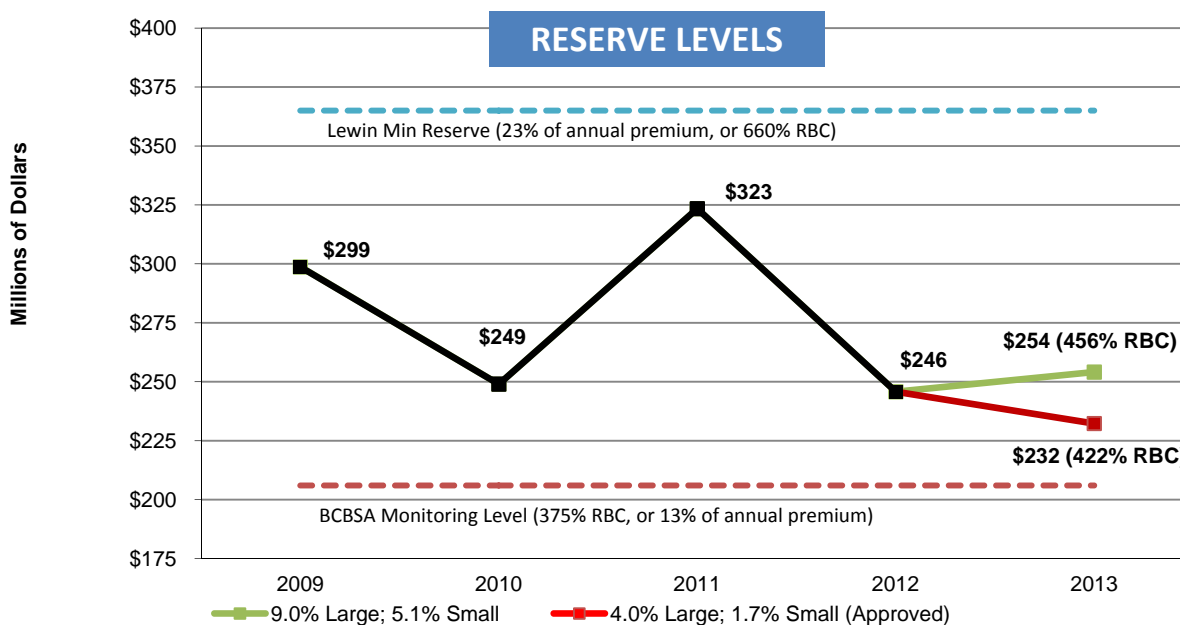
Through September 2012, BCBSRI has experienced a commercial group operating loss of \$33.6 million, which we project will be \$40.7 million by year end. The full year net loss for 2012 marks the fourth consecutive year BCBSRI has posted an Underwriting loss, despite being approved for a reserve contribution factor. These historical losses have resulted in a \$167 million reduction to our overall reserves, which we project to be \$245.8 million (454% RBC) by year end 2012.

BCBSRI strongly believes these reserve levels are below an acceptable range given the current regulatory environment and uncertainty of risk associated with the Patient Protection & Affordable Care Act (“ACA”). Our current reserve level would cover approximately one emergency room visit for each of our members.

The recommended minimum reserve level (23% of premium) cited in the Lewin Study for OHIC in August 2006 presently equates to \$358 million or 661% RBC. Our 2012 reserve projection falls \$113 million below that benchmark. In addition, the Blue Cross and Blue Shield Association (“BCBSA”) maintains a financial performance standard applicable to all licensees. This standard requires monitoring to begin if a licensee falls at or below 375% of risk-based capital, which equates to roughly \$203 million in reserves. Compared to all other independent Blue Cross Blue Shield plans nationwide, BCBSRI currently has the lowest reserve adequacy level measured in terms of risk-based capital. The charts on the next page illustrate our reserve

¹ The May filing utilized calendar year 2011 data; this filing has data incurred through July 2012.

levels and underwriting losses in the commercial group market for the past few years. We have also included a projection of our previously approved 2013 filing versus this filing.

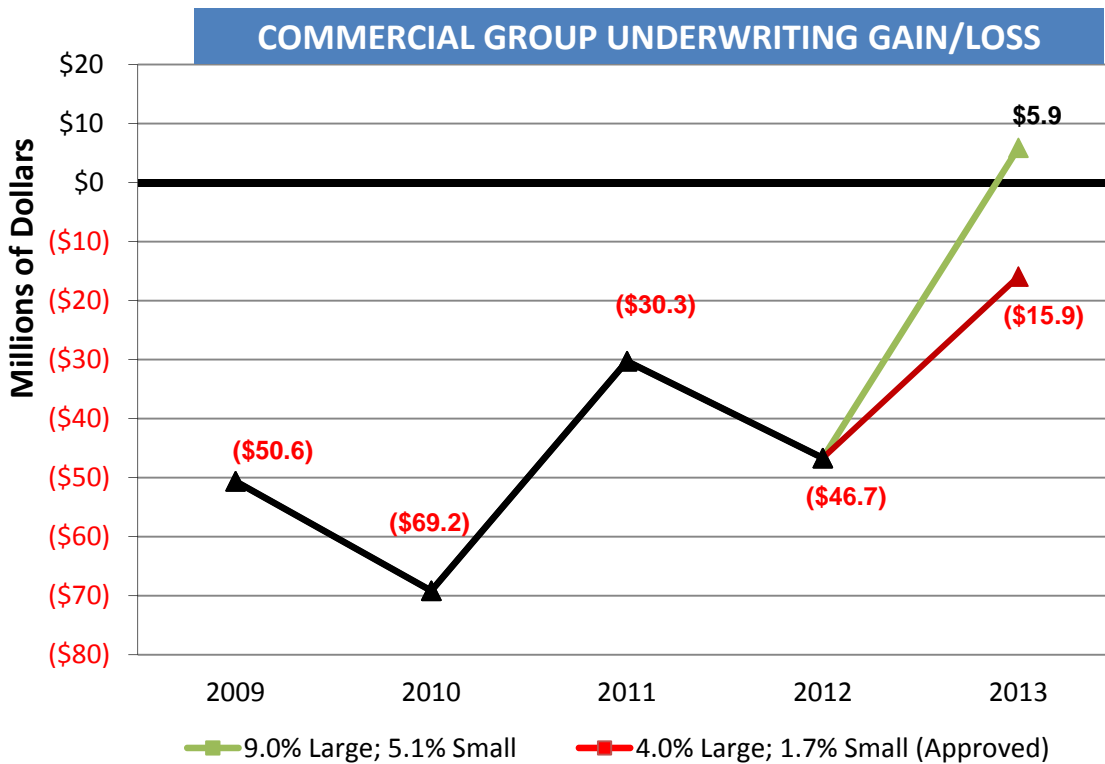


In May 2012, Standard & Poor’s issued their annual credit rating of BCBSRI (see Exhibit IV). It upheld a prior year downgrade to BBB, which is the lowest investment-grade credit rating. This latest report cites a “difficult regulatory environment as evidenced by inadequate premium rate approvals in the past” as a primary driver of the continued lower rating. Recognizing the need for strong risk-adjusted capitalization, we anticipate Standard & Poor’s future rating evaluations would be negatively impacted by continued deterioration of operating performance and the resulting drawdown on reserves. The Standard & Poor’s credit rating is an important risk indicator that many current and prospective clients review as they make decisions about purchasing services from us, and it also has a direct impact on our ability to maintain an affordable credit line.

New ACA fees will also deteriorate our reserve position beginning in 2014. In 2014 the estimated Health Insurer and Transitional Reinsurance fees on our Small and Large group business will amount to \$30 million. About 30% of our 2014 premium volume will arise from the 2013 renewal rates as determined by this filing. As a result, the ACA fees alone will represent a \$9 million reserve strain. The fees effectively lower the reserve contribution by 1.1% of group premium covered by this filing. This does not include any additional assessments the state may impose to cover the costs of discharging its ACA-related responsibilities (e.g., exchange-related funding).

Other carriers across the country are filing for these fees in their 2013 rate submissions and have received regulatory approval to recover their liability. Within New England, the Connecticut, Massachusetts, and New Hampshire insurance departments have approved the inclusion of ACA fees in 2013 rate year filings. It would be standard actuarial practice and good accounting for carriers to reflect ACA fees in the development of 2013 plan year rates in proportion to the

degree the policy years extend into calendar year 2014. However, in accordance with OHIC’s instructions this filing makes no provision for the collection of the new ACA fees.



This chart displays the commercial group portion of BCBSRI underwriting losses since 2009 and projected gain/loss scenarios for 2013.

BCBSRI understands the importance of providing predictable, affordable, and adequate rates to our customers. However, our deteriorating financial position and obligation to act in a prudent manner and in the best interest of the Company requires that we submit this filing. If this filing is not approved, BCBSRI projects that we will enter BCBSA monitoring in 2014 when our reserve level drops below 375% RBC. In the event our RBC ratio falls below 200%, we will lose our BCBSA license and Blue Cross/Blue Shield trademarks. This would dramatically impair our ability attract new enrollment. Additionally, as a member of the BCBSA, we and our customers benefit from the very favorable provider reimbursement arrangements our fellow Blue plans are able to negotiate. Approximately 25% of the medical payments we make are to providers outside of Rhode Island. These payments are for services rendered to Rhode Island residents who receive care out of state as well as non-residents who are covered by our Rhode Island group customers. If we were to lose our status as a licensee of the BCBSA, we would likely not be able to negotiate payment terms as favorable. Our inability to do so would inevitably lead to a loss of a significant volume of business and would threaten our continued survival.

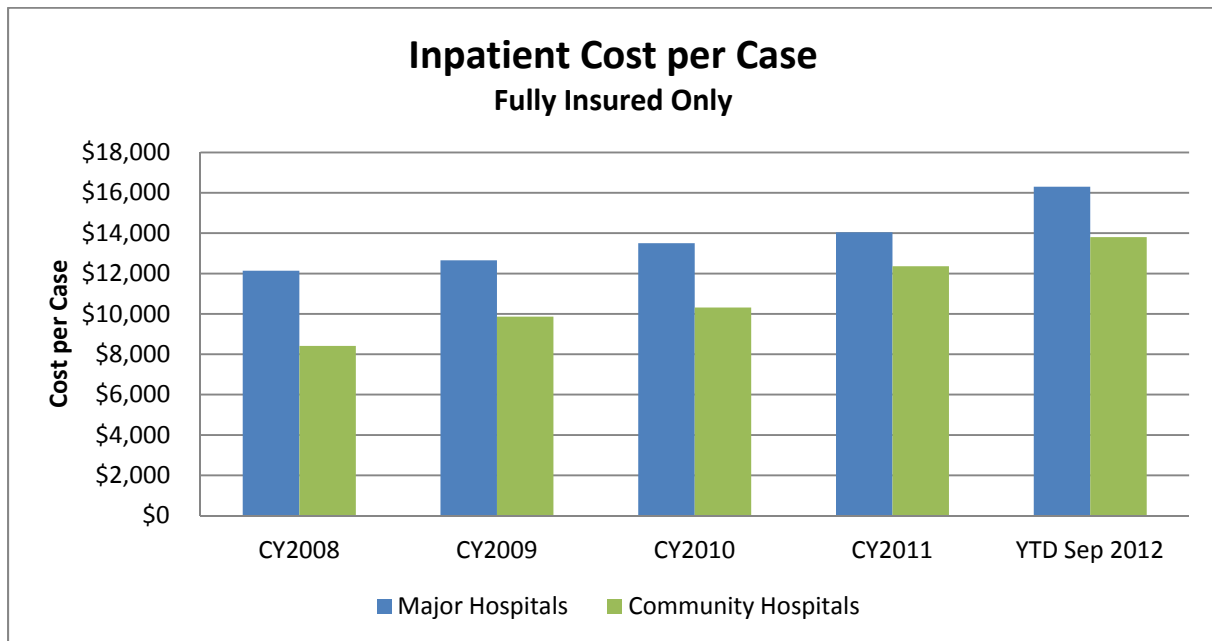
Medical Expenses

Exhibit I, *Small Group Rate Filing Template*, illustrates the variances by cost category between our previous filing and our current projection based on an additional seven months of experience. Our primary concern with the gap between projections is maintaining the soundness of our actuarial rating standards while also being compliant with OHIC's promulgated rate cap. It is not our intent to recoup losses we have experienced in 2012 or the preceding three years. However, we do need the ability to incorporate the updated claims experience when we rate Small Groups.

The trend factors being proposed in this filing were developed in accordance with the methodology we have used in all recent rate factor filings. The unit price trends are based on existing provider contracts and a best estimate of the price increases for those provider contracts that are still outstanding. Utilization trends were developed through an analysis of 36 months of historical experience through July 2012 incurred dates. The medical trend factors being proposed for our Small Group segment are in the aggregate equal to what was filed and approved in our May submission. The medical trend factors being proposed for our Large Group segment are in the aggregate 80 basis points higher than what was filed and approved in our May submission. This is due to the trend acceleration we have seen over the course of 2012.

Below is a description of several key drivers of medical trends in this filing:

Hospital Per Admission Costs –The average cost per admission increased over 2011 levels, with a net impact of 1% on overall medical trend. The chart below shows the average cost per admission for major versus community hospitals since 2008. We are currently working with our local hospitals to moderate cost per admission trends for 2013 and forward.



Maternity and Behavioral Health Costs – Overall, the per admission costs for maternity and behavioral health admissions in 2011 are higher than their respective Blue Health Intelligence (BHI) regional averages for 2011. This excess cost adds approximately 1% to Commercial premium rates. BHI is a data set made up from a large number of Blue Cross and Blue Shield plans from across the country. For the regional comparison cited here we utilized the aggregated data of five Blue Cross plans located in the northeast United States.

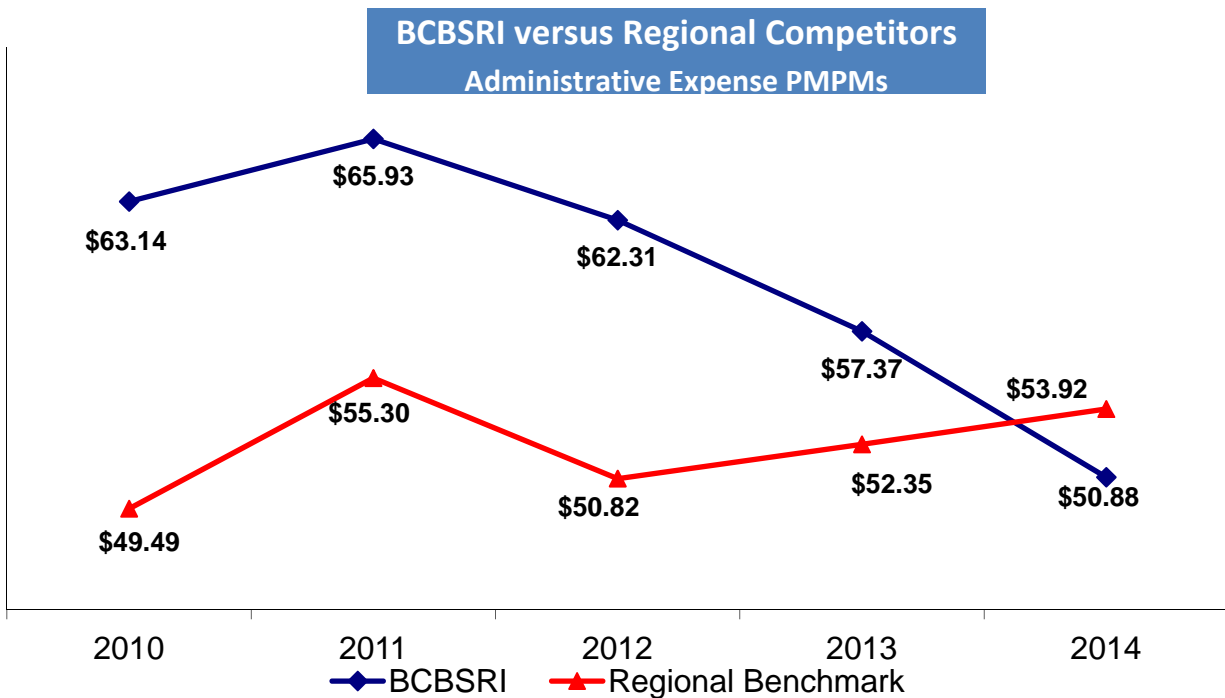
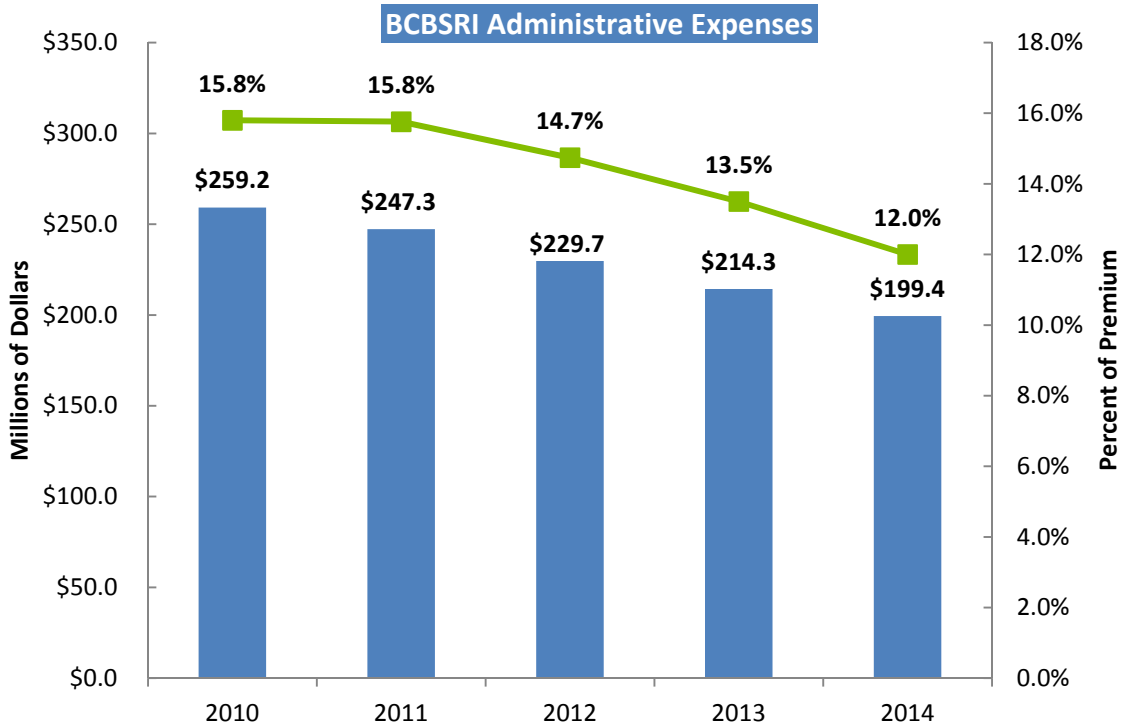
Hospital Rate of Admission – The hospital admission rate across our group business has increased 3.9% over 2011 levels. This reverses the declining inpatient admission rates we have seen over recent years. This increased admission rate has added about 1% to our overall medical trend.

Outpatient Chemotherapy/Injections – BCBSRI has also seen a significant increase in costs and utilization for drugs provided in outpatient facilities. This includes drugs used for chemotherapy as well as other drugs administered in a facility setting. Year-to-date trends for these drugs are running at about 24%. This trend is being driven equally by utilization (11%) and price (12%). This trend is not attributed to any particular drug or new therapy, but rather a general increase in use and some widespread pricing increases by drug manufacturers. This escalation has increased our overall insured cost by .6%.

Operating Expenses

Exhibit II, *Administrative Costs Request*, provides information on our actual 2011 and projected 2013 administrative costs as well as the administrative charge levels we are proposing to assess in this submission. The administrative charges being proposed in this filing are consistent with the operating expense levels we will reach by 2014, but do not cover the entirety of expected 2013 expenses. This shortfall is about \$9 million and lowers the reserve contribution by 1.1% of premium covered by this filing. In prior filings, we had laid out a multiyear glide path to reduce operating expenses to approximately 12% of premium, consistent with our regional benchmarks. Since 2010, we have reduced operating expense by \$45 million—a reduction from 15.8% of premium in 2010 to 13.5% in 2013. Our 2014 benchmark of 12% means an additional \$15 million of administrative expense reductions.

We are confident that we will achieve this goal in 2014 and for this reason are proposing to base our 2013 rates on this level of operating expenses. The first chart on the next page summarizes the progress that we have made. The second chart compares our actual and projected per member per month charges with those of other carriers operating in the region. The expense levels in the second chart reflect the expense levels reported in financial statements filed by each carrier through 2012. The 2012 data is based on the statements filed through June 30, 2012. For earlier years, we pulled the data from the annual statement blanks. The benchmarks for 2013 and 2014 were developed by applying an assumed 3% inflation rate to the historical data. Please note that the values reported in these tables reflect operating expenses levels across the entire organization and not just those associated with the Commercial Group business. Our regional benchmarking is consistent with the benchmarking study OHIC commissioned from Wakely last year. However, our comparison excludes state premium taxes since differences in state tax levels have nothing to do with a carrier's operating efficiency.



OHIC's September 2012 decision to reduce our administrative charges was based on a comparison of our proposed charges with those of the other carriers. However due to inconsistencies in the way carriers characterize expenses as "medical" or "administrative," we do not believe the comparison made by OHIC was appropriate. Specifically, in a footnote to Part 1 of its rate factor filing template United clearly indicates that certain capitation payments and "other costs associated with affiliated agreements, i.e. OPTUM SERVICES" have been included

with medical expenses. We also note that in its approved rating formula Tufts included certain of its cost-containment expenses in medical expenses for rating purposes. On the other hand, the administrative charges we propose to assess are our only provision to recover our operating expenses. Therefore, we submit that it is not appropriate to compare the administrative charge levels being proposed by the different carriers without first adjusting for these differences in characterization.

The 5.1% average rate increase estimate included in this filing was developed by applying our proposed rating factors to all 2013 renewals excepting only the advanced notice groups that were rated in accordance with the May 2011 filing. We are proposing that this average rate increase become the rate cap applicable to all 2013 new and renewing business and against which compliance will be monitored.

Projections of future medical costs are invariably wrong. They are either too high or too low due to changes in the morbidity and composition of the covered population, changes in medical practice and/or simple statistical fluctuation. In order to reduce these projection errors it is our practice (and standard industry practice) to utilize the most up to date experience period data available at the time we are actually setting rates. Additionally we point out that another source of divergence between the filed estimate and the actual formula driven average rate increase are unknowns about the current rates and the composition of the book of business that will actually be rated. Some of the cases that will be getting a renewal rate increase next year will not have been renewed or, in the case of new business, even written at the time of our rate filing. Furthermore a fair number of the cases included in the projection of the estimated average rate increase will not remain in force and hence will not be part of the actual average increase that will be monitored. For all of these reasons we suggest that OHIC permit carriers to apply their approved rating formulas to the developing experience and the actual business that winds up being issued a renewal even if the resulting average rate increase runs at least somewhat above the promulgated rate cap without the need to submit a new rate filing. Our consulting actuaries at Milliman, Inc share this view as discussed in their actuarial opinion letter (see Exhibit III). We would like the opportunity to discuss with OHIC the appropriate size of permitted deviations from the rate cap.

We note that the Medical Loss Ratio provisions of the ACA will prevent us (or any carrier) from making any windfall profit. Premium revenues in excess of the 80% of claims in the Small Group market and 85% in the Large Group market will have to be returned to customers in the form of rebates. Additionally, if our future medical experience unfolds more favorably than we are currently projecting, we will recognize it in accordance with the provisions of our approved rating formula that provides for us to utilize updated experience period data.

If both Small Group and Large Group filings are approved as filed, we anticipate that it will result in a CY 2013 underwriting gain across our combined Small and Large Group business of \$6 million. This amounts to less than 1% of annual premium. Our experience would have to get materially better than we are forecasting for our proposed rating factors to result in excessive gains.

Actuarial Certification

In accordance with the filing fee requirements contained in R.I. Gen. Laws § 42-14-18, an electronic funds transfer (EFT) transaction in the amount of \$125 is submitted via the SERFF system. Policy forms pertaining to this filing are listed in Attachment 1 to this Memorandum.

The actuarial assumptions underlying this filing have been developed by my staff and reviewed by myself. With one qualification, I certify that this rate factor filing was developed utilizing sound actuarial assumptions and methodologies. My sole reservation relates to excluding any provision for the new ACA fees that will be assessed in 2014 on business that will be rated under this filing.

In addition, we engaged Milliman to provide an independent third party review of the data and analysis used in the development of this rate filing (see Exhibit III). Their opinion letter is being submitted with this filing. It concludes that our methods and assumptions are actuarially sound and result in factors that are reasonable and appropriate.

This filing includes the following Exhibits:

- Exhibit I, *Small Group Rate Filing Template*
- Exhibit II, *Administrative Costs Request*
- Exhibit III, *Actuarial Opinion Letter from Milliman, Inc re: Actuarial Review of Rating Factors Applicable to Small and Large Group Subscription Renewals (“Group Rating Factor Filing”)*
- Exhibit IV, *Standard and Poor’s, Global Credit Portal[®] RatingsDirect[®], Blue Cross & Blue Shield, Inc*



John Lynch, F.S.A., M.A.A.A.
Chief Actuary
Blue Cross & Blue Shield of Rhode Island

Attachments

Attachment 1: Policy Forms

Policy forms pertaining to this filing are as follows:

FRONT GRP (09-10);

SUMMARY GRP (09-10);

INTRODUCTION GRP (09-10);

ELIGIBILITY GRP (09-10);

COVERED GRP (09-10);

EXCLUSIONS GRP (09-10);

HOW WE PAY GRP (09-10);

COB GRP (09-10);

APPEALS GRP (09-10); and

GLOSSARY GRP (09-10).

Blue Cross & Blue Shield of Rhode Island
Small Group Rate Filing Template: December 2012 Filing

Part 1. Historical Information

Experience Period for Developing Rates

From	To
10/1/2009	9/30/2012

Total Small Group and Rhode Island Builders Association

Quarter	End Date	IP Days	Member Months	Earned Premium	Incurred Claims Total	Incurred Claims IP	Incurred Claims OP	Incurred Claims		Incurred Claims Rx	Loss Ratio	Quality Improvement Expense*	Other Cost Containment Expense*	Other Claim Adjustment Expense*	Other Operating Expense*	Investment Income	State Premium		Contribution to Reserves
								Primary Care	M/S								Tax	Commissions	
1 (Oldest)	12/31/2009	4,863	220,642	\$85,468	\$72,437	\$13,743	\$17,031	\$3,752	\$23,043	\$13,707	84.8%	\$689	\$1,099	\$5,232	\$12,908	\$124	\$1,777	\$1,366	(\$9,918)
2	3/31/2010	2,872	214,763	\$83,767	\$72,903	\$17,929	\$17,711	\$3,135	\$20,764	\$13,363	87.0%	\$674	\$1,029	\$3,427	\$8,376	\$230	\$1,744	\$2,349	(\$6,505)
3	6/30/2010	4,543	214,394	\$85,759	\$73,424	\$14,085	\$14,643	\$3,039	\$26,400	\$15,258	85.6%	\$682	\$1,045	\$3,484	\$8,457	\$230	\$1,744	\$2,349	(\$5,196)
4	9/30/2010	4,543	212,340	\$85,961	\$75,022	\$15,920	\$17,302	\$3,090	\$23,520	\$15,190	87.3%	\$677	\$1,036	\$3,452	\$8,412	\$230	\$1,744	\$2,349	(\$6,502)
5	12/31/2010	4,318	208,951	\$88,639	\$76,857	\$13,580	\$14,810	\$3,199	\$29,237	\$16,031	86.7%	\$698	\$1,077	\$3,600	\$8,625	\$230	\$1,744	\$2,349	(\$6,081)
6	3/31/2011	6,164	205,736	\$84,447	\$72,438	\$18,099	\$17,121	\$3,148	\$18,989	\$13,715	85.8%	\$758	\$1,131	\$3,480	\$7,534	\$189	\$1,707	\$1,607	(\$4,018)
7	6/30/2011	5,237	203,734	\$83,825	\$71,615	\$15,384	\$17,660	\$3,164	\$19,665	\$14,376	85.4%	\$734	\$1,100	\$3,387	\$7,305	\$199	\$1,716	\$1,887	(\$3,720)
8	9/30/2011	5,533	201,333	\$85,912	\$70,063	\$15,331	\$17,208	\$3,093	\$18,641	\$14,254	81.6%	\$742	\$1,114	\$3,434	\$7,385	\$185	\$1,701	\$1,886	(\$228)
9	12/31/2011	4,707	199,769	\$81,796	\$70,258	\$14,603	\$17,501	\$3,360	\$18,643	\$14,615	85.9%	\$812	\$1,197	\$3,674	\$8,051	\$166	\$1,793	\$1,683	(\$5,507)
10	3/31/2012	4,173	195,780	\$83,544	\$68,596	\$14,960	\$17,262	\$3,025	\$17,349	\$14,228	82.1%	\$606	\$1,215	\$2,577	\$7,110	\$160	\$1,569	\$1,874	\$155
11	6/30/2012	3,567	193,090	\$83,201	\$70,263	\$15,465	\$17,726	\$2,924	\$17,795	\$14,459	84.4%	\$639	\$1,295	\$2,835	\$7,484	\$170	\$1,580	\$1,835	(\$2,560)
12	9/30/2012	3,851	191,606	\$83,081	\$68,869	\$16,076	\$17,091	\$3,007	\$17,052	\$14,415	82.9%	\$614	\$1,240	\$2,675	\$7,203	\$160	\$1,543	\$1,821	(\$724)

* These categories should conform generally to the reporting in the NAIC statement Underwriting & Investment Exhibit Part 3- Analysis of Expenses and/or to the Supplemental Health Care Exhibit, Lines 6.3 and 8.1
If any of the historical information reported is different from that period as reported in the prior rate filing, please provide a reconciliation and explanation showing the amount of each element of difference.

Part 2. Prospective Information (Small Groups and Rhode Island Builders Association only)

A. Trend Factors for Projection Purposes (Annualized)

	IP	OP	Primary Care	Other M/S	Rx	Weighted Total
Total	7.52%	8.88%	11.07%	5.65%	7.43%	7.48%
Price Only	4.86%	4.15%	6.76%	1.55%	2.76%	3.43%
Utilization	1.00%	4.00%	3.50%	3.50%	3.00%	2.95%
Mix	1.00%	0.00%	0.00%	0.00%	0.00%	0.23%
Leveraging	0.52%	0.52%	0.52%	0.52%	1.50%	0.72%

Weights	23%	24%	5%	28%	20%	100%
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Note: The above factors together with the new PBM impact and expected demographic changes produce an effective trend of 2.9%.

Blue Cross & Blue Shield of Rhode Island
Small Group Rate Filing Template: December 2012 Filing

B. The following items for the period to which the rate filing applies, by quarter:

Quarter	Beginning Date	Average	Pure	Expected	Quality	Other Cost	Other Claim	Other	Average	Investment	Premium Tax
		% Rate Increase	Medical Cost Ratio	Contribution to Reserves %	Improvement Expense %*	Containment Expense %*	Adjustment Expense %*	Operating Expense %*	Commissions %*	Income Credit %	
Weighted Average		5.1%	83.2%	3.3%	0.6%	0.9%	2.6%	6.0%	1.5%	-0.2%	2.0%

* These categories should conform generally to the reporting in the NAIC statement Underwriting & Investment Exhibit Part 3 - Analysis of Expenses and to the Supplemental Health Care Exhibit, Lines 6.3 and 8.1
The sum of the expenses, commissions, contributions to reserves, investment income credit, taxes and the medical loss ratio should be 100%.

C. Average Rate Increase Components

The following items should reconcile to the Weighted Average Percent Rate Increase for the year:

	Price	Utilization, Mix	Total
Inpatient	0.9%	0.5%	1.4%
Outpatient	0.7%	0.7%	1.4%
Physician	0.7%	1.1%	1.8%
Pharmacy	0.1%	0.1%	0.2%
NEW PBM Effect			-1.9%
Admin Expense (Aggregated)			1.5%
Contribution to Reserves			0.2%
Taxes and Assessments			0.5%
Total			5.1%

Part 3. Retrospective Reconciliation of Experience with Filed Factors (Small Groups and Rhode Island Builders Association only)

Year	Filed Data ¹					PMPM Increase ²		Standard Plan PMPM ³		Standard Plan Increase ⁴		Approved		Loss Ratio ⁵	
	Member Months	Earned Premium	Incurred			Premium	Claims	Premium	Claims	Premium	Claims	Trend Increase%	Contrib to Reserves%	Actual%	Filed%
			Claims Total	Premium PMPM	Claims PMPM										
2009	862,139	340,954	293,787	\$395.47	\$340.76			\$377.56	\$321.41			9.4%	1.3%	86.2%	84.3%
2010	819,754	342,824	290,973	\$418.20	\$354.95	5.7%	4.2%	\$402.33	\$348.65	6.6%	8.5%	8.8%	2.0%	84.9%	84.0%
2011	780,245	331,622	277,986	\$425.02	\$356.28	1.6%	0.4%	\$435.73	\$371.66	8.3%	6.6%	9.7%	2.3%	83.8%	85.0%

¹ Corresponds to historical information data in Part 1 above

² Percent increase compared to prior year

³ For most commonly held plan of benefits in 2010 and for the same plan of benefits in 2011

⁴ Percent increase compared to prior year

⁵ Represents claims loss ratio, claims divided by premium, which differs from the Federal MLR calculation for potential rebate determination

Blue Cross & Blue Shield of Rhode Island
Group Rate Factor Filing of December 2012
Administrative Costs Request

1. The expenses provided below are presented consistent with the categorization required in the Underwriting and Investment Exhibit - Part 3 Analysis of Expenses in accordance with NAIC instructions. The 2011 Actuarial values shown below are incorporated in the analogous values reported for our Commercial segment in both our NAIC blank and on page 2 of this exhibit. Our Commercial line of business as reported in the annual statement consists of the Small Group and Large Group segments that are the subject of this rate filing as well as our Direct Pay line. Note that there are approximately two years of inflationary increases between 2011 Actual and 2013 Projected values. Our proposed retention charges are below our projected costs in recognition of our ongoing efforts to improve administrative efficiency.

	2011 Actual		2013 Projected		2013 Proposed ⁽¹⁾		% Change	
	Small Group	Large Group	Small Group	Large Group	Small Group	Large Group	Small Group	Large Group
Total Estimated Member Months	816,413	1,472,976	743,081	1,484,325	743,081	1,484,325	-9.0%	0.8%
Total Estimated Premiums (\$mpm)	\$411.53	\$395.83	\$494.94	\$449.78	\$494.94	\$449.78	20.3%	13.6%
Total General Administrative Expense (\$mpm)	\$54.20	\$44.74	\$50.27	\$35.68	\$45.11	\$36.63	-16.8%	-18.1%
Total Cost Containment Expense (\$mpm)	\$9.29	\$8.39	\$9.31	\$7.81	\$6.64	\$6.08	-28.5%	-27.6%
Total Other Claim Adjustment Expense (\$mpm)	\$17.12	\$17.82	\$13.50	\$13.47	\$10.85	\$12.33	-36.6%	-30.8%
Total Admin Expense (\$mpm)	\$80.62	\$70.96	\$73.07	\$56.96	\$62.60	\$55.04	-22.4%	-22.4%
Breakdown of General Administrative Expense (\$ pmpm)								
a. Payroll and benefits	\$25.10	\$18.42	\$19.92	\$12.77	\$17.88	\$13.11	-20.6%	-30.7%
b. Outsourced Services (EDP, claims etc.)	\$8.65	\$8.64	\$8.80	\$8.70	\$7.89	\$8.93	1.7%	0.7%
c. Auditing and consulting	\$3.73	\$3.16	\$3.49	\$2.79	\$3.13	\$2.86	-6.4%	-11.7%
d. Commissions	\$8.65	\$6.72	\$12.90	\$5.81	\$11.57	\$5.96	49.1%	-13.6%
e. Marketing and Advertising	\$0.65	\$0.55	\$0.38	\$0.29	\$0.34	\$0.29	-41.8%	-48.4%
f. Legal Expenses	\$0.44	\$0.36	\$0.37	\$0.29	\$0.34	\$0.30	-14.2%	-18.8%
g. Taxes, Licenses and Fees	\$8.88	\$8.61	\$8.69	\$8.02	\$7.80	\$8.23	-2.1%	-6.9%
h. Reimbursements by Uninsured Plans	(\$11.30)	(\$9.39)	(\$12.82)	(\$9.63)	(\$11.50)	(\$9.88)	13.4%	2.5%
i. Other Admin Expenses	\$9.40	\$7.67	\$8.54	\$6.65	\$7.66	\$6.83	-9.2%	-13.3%

⁽¹⁾ For comparison purposes 2013 proposed charges represent 1st Quarter 2013 rates.

Blue Cross & Blue Shield of Rhode Island
Group Rate Factor Filing of December 2012
Administrative Costs Request

2. The following table details actual calendar year 2007-2011 fully insured Commercial administrative costs. This is consistent with the annual statement filings to OHIC for administrative costs using the categories defined by NAIC financial statement and as allocated to Commercially insured business only.

Fully Insured Commercial Administrative Cost History (Comprehensive Column)					
	2007	2008	2009	2010	2011
Total Premiums	1,108,466,606	1,079,151,863	1,025,508,205	994,470,562	984,903,252
Total General Administrative Expense	100,746,665	121,463,184	132,106,574	133,474,919	121,420,201
General Admin Exp. Ratio	9.09%	11.26%	12.88%	13.42%	12.33%
Total Fully Insured Member Months	3,326,346	3,049,827	2,775,423	2,603,304	2,468,947
General Administrative Expense (\$pmpm)	\$30.29	\$39.83	\$47.60	\$51.27	\$49.18
Breakdown of General Administrative Expenses (\$ pmpm)					
a. Payroll and benefits	\$17.53	\$17.40	\$21.04	\$18.84	\$19.82
b. Outsourced Services (EDP, claims etc.)	\$9.28	\$8.93	\$8.62	\$12.13	\$10.75
c. Auditing and consulting	\$2.20	\$5.75	\$6.38	\$6.18	\$4.55
d. Commissions	\$5.49	\$6.06	\$6.78	\$6.96	\$7.21
e. Marketing and Advertising	\$0.81	\$0.99	\$0.89	\$0.72	\$0.76
f. Legal Expenses	\$1.02	\$0.33	\$0.25	\$0.32	\$0.40
g. Taxes, Licenses and Fees	\$0.10	\$3.68	\$7.49	\$7.79	\$8.28
h. Reimbursements by Uninsured Plans ⁽¹⁾	(\$11.59)	(\$12.49)	(\$10.76)	(\$11.78)	(\$11.59)
i. Other Admin Expenses	\$5.44	\$9.18	\$6.90	\$10.11	\$8.98
Cost Containment Expense	\$4.10	\$4.30	\$5.73	\$7.58	\$7.82
Other Claim Adjustment Expense	\$10.06	\$13.38	\$18.19	\$17.42	\$20.04
Total Self Insured Member Months for all affiliated companies doing business in RI	2,409,639	2,474,355	2,677,918	2,448,365	2,625,181

⁽¹⁾ Includes total reimbursements from uninsured plans, not just the portion allocated to general administrative expenses, therefore the breakdown of general expenses does not match the total listed above. The differential is the portion of self funded fees that are treated as a contra expense for cost containment and other claim adjustment expenses.



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Robert H. Dobson, F.S.A., M.A.A.A.
Consulting Actuary

December 4, 2012

John J. Lynch, F.S.A., M.A.A.A.
Chief Actuary
Blue Cross Blue Shield of Rhode Island
500 Exchange Street
Providence, RI 02903

Via email to john.lynch@bcbsri.org

Re: Actuarial Review of Rating Factors Applicable to Small and Large Group Subscription
Rate Renewals ("Group Rating Factor Filing")

Dear Mr. Lynch:

Blue Cross & Blue Shield of Rhode Island (BCBSRI) has asked Milliman to review the development of rating factors applicable to Small Group and Large Group renewals effective in 2013. These rating factors are intended to be filed for approval with the State of Rhode Island Office of the Health Insurance Commissioner (OHIC). The filing procedure has been in place in similar form for many years, though the current filing is being prepared specifically in accordance with instructions issued by the OHIC in a letter dated April 19, 2012 and supplemented with letters dated May 16, 2012 and August 27, 2012. The April letter sets out, among other things, what standards will be used by OHIC for review, what documents should be included in the filing and how public input and accessibility will be handled. The supplemental letters deal with trends and rate caps, respectively. The particular filing that is the subject of this review is an amendment / additional filing as described in paragraph 10 of the April letter.

We, the undersigned, are members of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

This review was performed for the specific purpose of assessing the reasonableness of the methods and assumptions used in the development of the rating factors contained in BCBSRI's filing. This report should not be used for any other purpose. This work product was prepared for BCBSRI for the purpose described herein and may not be appropriate to use for other purposes. Milliman does not intend to benefit and assumes no duty of liability to other parties who receive this work product. Any third party recipient of this work product who desires professional guidance should not rely upon Milliman's work product, but should engage qualified professionals for advice appropriate to its own specific needs. Any release of this report to a third party shall be in its entirety.

We have reviewed BCBSRI's development of required rating factors in the filing, and we have done our own testing as we deemed appropriate. In our opinion, the actuarial methods and assumptions used in BCBSRI's calculation of required rating factors are sound and result in factors that are reasonable and appropriate for producing group rates. We observe that BCBSRI is proposing to limit the provision developed for recoupment of administrative costs in its group rates. Further, BCBSRI is not proposing to include any provision for taxes, fees and assessments which will be required under the federal Affordable Care Act (ACA). Finally, BCBSRI is not requesting any additional risk charge to cover the cost of the revenue loss it may incur as a result of the OHIC rate cap. As a result of these three issues, the resulting rates may not produce adequate revenue to cover all of the costs identified in the development.

As part of this filing, BCBSRI has addressed the issue of "rate caps" imposed by OHIC and clarified in its letter of August 27, 2012. As described in that letter, the rate cap is not intended to require modification to the premium rates for any particular group, but is designed to drive the health plan to take other actions (provider contracting and administrative management are mentioned in the letter) if the health plan sees that the cap will be exceeded for the year.

The problem with the rate cap from an actuarial standpoint is that the rating factors are developed based on prior experience and assumptions about the future, notably increases in health care utilization and cost. When the rating factors are actually applied during the rating period, the resulting premium rates are based on later experience that reflects actual emerging increases in health care utilization and cost. When these emerging costs are greater than assumed, as appears to be the case with BCBSRI in 2012, the rate caps will be exceeded.

BCBSRI has addressed this issue in the current filing in two ways:

1. Increasing the trend assumption and including an additional experience adjustment for months not yet complete based on a review of recent experience, and
2. Suggesting that relatively minor deviations from the rate cap be allowed without penalty.

In our opinion, these adjustments are necessary and appropriate. We recommend that minor deviations be defined as +/-2%. In addition, depending on the magnitude of any lost revenue that might result from the rate cap, it is our opinion that it may be appropriate to include an additional risk charge in the rates to reflect the expected cost of the rate caps. BCBSRI has decided not to request such an additional charge at this time.

We would characterize the trend factors developed by BCBSRI for use in projecting claim costs as falling within the range of most likely anticipated outcomes, based on information provided to us and our own independent research and actuarial judgment at this time. We also find the trend factors to be within the range of trends observed and expected elsewhere in the industry.

We reviewed BCBSRI's development of required administrative costs, which is defined for purposes of the Group Rating Factor Filing to include the net of operating and related administrative expenses, Federal income tax, premium tax, various state mandated assessments, and investment income (credit). We found BCBSRI's development to be sound. We note that BCBSRI proposes to actually charge in its group renewals a lower amount.

We were also asked to comment on comparisons with expense charges filed in Rhode Island by United Healthcare of New England (United). In particular, United mentions in its filings that

certain external vendor and internal affiliate expenses are treated differently under GAAP accounting than under statutory accounting. For 2013, they note that GAAP is used. Further, in a footnote it is noted that claims include certain capitation payments and “other costs associated with affiliated agreements”. While we have no personal knowledge of United’s practices in this regard, we note that it is common in the industry for the total cost of payments for outsourced services to be included as claims, including portions that would be used for administrative expenses by the external vendor or internal affiliate. Since BCBSRI has no such arrangements, it would be appropriate to make an adjustment when comparing filed administrative expense charges between the two companies.

As part of the review of administrative costs, we considered the impact of taxes, fees and assessments which will be required under ACA. While one small element of these fees is already in effect, the more significant ones begin January 1, 2014, and are effective based on calendar year, not plan year. Therefore, groups renewing after January 1, 2013, will have a portion of their premiums extending into 2014 and thus subject to the additional taxes, fees and assessments. In our opinion, it is actuarially appropriate to include a charge for these fees on an estimated basis. While it is not universal, many other health plans are including these charges in 2013 rates, often increasing by renewal month. If these fees are not imposed in 2013 premium rates, they will have to be paid out of contingency reserves and recouped from future premiums, leading to larger rate increases than would otherwise be necessary. We have reviewed the development of the specific charges proposed by BCBSRI and find them to be within a reasonable range of estimates for these items. However, as noted elsewhere, BCBSRI is not including provision for these charges in this filing.

We believe the stated required reserve contribution factor to be consistent with industry practices and, under normal circumstances, we would find it to be within a reasonable range. However, given the Plan’s current reserve situation (at the extreme bottom for all Blue Cross Blue Shield Plans), we view the required reserve contribution as only being at the very low end of a reasonable range. In addition, due to potential shortfalls in the proposed administrative cost factors, the lack of any provision for ACA taxes, fees and assessments, and potential penalties that could be incurred under the OHIC rate cap, we believe the actual contribution to corporate reserves based on this filing will likely be less than the stated level requested in it. There is a material possibility of no contribution to corporate reserves at all. In addition, even with fully adequate rates in all lines of business, reserve contribution factors will likely need to be increased in the future in order for BCBSRI to achieve an appropriate corporate reserve target within a reasonable period of time.

We have reviewed, at a high level (that is, not in detail) BCBSRI’s forecast and resulting risk based capital ratio. We find the forecast to be reasonable, based on our review. We note that it is possible that BCBSRI could approach the monitoring threshold established by the Blue Cross Blue Shield Association in the absence of the requested increase in rating factors.

The following elements of the filing were also part of our review:

- Experience adjustment – we find the experience adjustment noted above to be reasonable and appropriate;
- Incurral factor – we find the incurral factor used to add unpaid claims to the underlying experience to be reasonable and appropriate; and
- Mandated benefits – we considered mandated benefits both at the state and federal levels. BCBSRI has confirmed that there have been no changes at the state level. At the federal level, the Women’s Preventive Health mandate is not

yet in the experience. BCBSRI has elected not to reflect this in the premium rate development, however. While this represents less than one half of one percent of premium, it is another reason to expect that the desired reserve contribution in this filing is unlikely to be achieved.

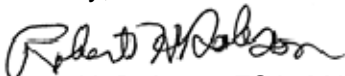
We also investigated the need for a conversion charge and understand that such a charge is no longer a part of the rate development.

Our review included the rating factors to be filed, but not the rating formula itself or its application. We assume the rating formula is appropriate and rating factors are appropriately applied.

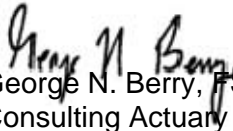
In performing this analysis, we relied on data and other information provided by BCBSRI. We have not audited or verified this data and other information. If the underlying data or information is inaccurate or incomplete, the results of our analysis may likewise be inaccurate or incomplete. We performed a limited review of the data used directly in our 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 our assignment.

It is certain that actual experience will not conform exactly to the assumptions and factors developed in the rate filing and reviewed by us. Since BCBSRI has elected to limit the rating factor for administrative costs, the likelihood of losses arising even with the rating factors requested in the filing is increased. Further, to the extent that emerging experience differs from the assumptions used in the filing, the actual required rates produced by them will also deviate from the projected required amounts produced using the rating factors in the filing. In accepting risks such as these, it is imperative that BCBSRI maintain adequate reserves for the protection of the Plan and its subscribers.

Sincerely,



Robert H. Dobson, FSA, MAAA
Consulting Actuary



George N. Berry, FSA, MAAA
Consulting Actuary



James A. Dunlap, FSA, MAAA
Actuary

Blue Cross & Blue Shield of Rhode Island Inc.

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Blue Cross & Blue Shield of Rhode Island Inc.

Major Rating Factors

Strengths:

- Strong brand and wide provider network supporting a dominant market position
- Strong risk-adjusted capitalization supported by strong growth in surplus in 2011
- Strong liquidity profile, sustained by a liquid, high-quality investment portfolio

Weaknesses:

- Geographic market concentration in a single state
- Difficult regulatory environment as evidenced by inadequate premium rate approvals in the past

Operating Company Covered By This Report

Financial Strength Rating

Local Currency

BBB-/Positive/--

Rationale

The insurer financial strength rating on Blue Cross & Blue Shield of Rhode Island Inc. (BCBSRI) reflects BCBSRI's dominant market position, its strong liquidity profile, and its good risk-adjusted capitalization. Offsetting these strengths is BCBSRI's geographic market concentration in a difficult regulatory region.

In Standard & Poor's Ratings Services' view, BCBSRI's dominant market position in Rhode Island remains a strength for the rating. The company has a dominant share of the commercial health insurance market in that state, supported by strong brand equity and an extensive provider network. BCBSRI achieved and has maintained its leadership position through its competitive pricing, diversified product platform, focus on local communities, and high-quality customer service, as well as an extensive provider network. As of Dec. 31, 2011, the company had about 505,600 medical members under its commercial (group and individual) and government-sponsored (Medicare Advantage) plans.

BCBSRI's risk-adjusted capitalization is strong. In 2011, its statutory surplus saw an increase for the first time in four years. The company's capital had declined sharply in 2010 and 2009 due to negative net earnings and additional nonadmitted assets. However, with improved net retained earnings, the company added to its surplus in 2011. The company's capitalization also improved on a risk-adjusted basis, with capital being redundant at the 'AAA' level as per our 2011 pro forma insurance risk-based capital model, as compared with 'A' level redundancy at year-end 2010. We view capitalization to be critical for the company to improve credit quality. The stronger capital level, in our view, offsets any short-term volatility brought about possible inadequate premium rate approvals in the future.

The company's liquidity profile is strong, based on Standard & Poor's liquidity ratio of more than 200%. The company's investment portfolio comprises high quality, fairly liquid assets, which support the liquidity profile.

We consider BCBSRI's operating performance to be improving and supportive of the rating. We had previously lowered our ratings on BCBSRI due to its deteriorating financial profile, which stemmed from two years of negative retained earnings. The company's operating performance diminished in 2010 and 2009 because of inadequate

premium rate increases and higher-than-expected utilization in its commercial book of business. However, in 2011, the company saw a significant improvement in operating performance, primarily driven by the release of the premium deficiency reserve (PDR) and better medical cost trends. For full-year 2011, BCBSRI had pretax income (excluding realized capital gains and losses) of \$77 million, compared with a pretax loss of \$35 million in 2010 and pretax loss of \$101 million in 2009.

The company has already received adequate rate approvals for 2012, which indicates a likely stabilization of earnings in the near term. We expect the BCBSRI to report pretax return on revenue (ROR) of about 1.0%-1.5% in 2012 and about 2% in 2013. Our expectation for improvement in earnings takes into account higher-than-2011 cost trends, which are offset by adequate rate approvals and a reduction of administrative cost expenses.

The rating remains constrained by BCBSRI's geographic concentration in a single state, which exposes the company to adverse legislative, regulatory, economic, and competitive challenges. We believe it faces tough regulatory conditions in Rhode Island which, in 2008, changed its policy regarding proposed premium rate increases from a "file and use" approach to a "file and review" approach, further supporting our view of a strict regulatory environment.

Outlook

The outlook is positive based on improvements in BCBSRI's financial profile. Both operating performance and capitalization have improved in 2011, and we expect them to stabilize over 2012 and 2013. We could consider raising the rating over the next 24 months if BCBSRI maintains strong capitalization (capital being redundant at least at the 'AA' level as per our capital model) and stabilizes pretax operating ROR (excluding realized capital gains and losses) at about 1%-2%.

On the other hand, we could lower the ratings if BCBSRI's capital declines significantly and becomes deficient at the 'A' level and operating performance deteriorates, with ROR dropping below 1%.

Competitive Position: Leading Health Insurer In Rhode Island

BCBSRI has a good competitive position as the largest provider of health insurance in Rhode Island. The company has more than a 60% share of the state's health insurance market. BCBSRI achieved and maintained this position through its competitive pricing, diversified product platform, focus on local communities, and high-quality customer service as well as an extensive provider network. Further, BCBSRI has relationships with the vast majority of the physician providers and all of the hospitals in the state.

BCBSRI has a strong membership base, with 505,600 medical members in its commercial and government-sponsored programs. The company has an additional 93,500 members through the Blue Card and Blue CHIP programs. The company also has about 121,600 ancillary (dental) members and 9,000 Medicare Prescription Drug Plan members. Overall medical membership was in line with our expectations for 2011, but below 2010 levels. The year-over-year decline was due to a loss of a large group account in 2011. We don't expect this to have a material impact on the company's operations.

BCBSRI does face some competition (albeit somewhat fragmented), in particular from UnitedHealth Group Inc. and Tufts Health Plan of New England Inc. However, BCBSRI has remained its market leadership position through wide

local presence and strong community branding.

BCBSRI competes in all segments of the health insurance market. Its medical membership spreads over a diverse product platform: large and small group risk (43%), group nonrisk (43%), individual (8%), and government (6%) segments. Its products are well represented in all major employer groups in the state. The company markets its products to municipalities, large and small local groups, individuals, students, and senior citizens. An expanded network of brokers distributes BCBSRI's products, and third-party vendors provide prescription and vision care under various negotiated contracts. BCBSRI has relationships with the vast majority of the physician providers and all of the hospitals in the state.

BCBSRI's complete line of health insurance offerings enhances its competitive position. The company provides a wide variety of medical and dental benefits, managed care (HMO), point-of-service, and traditional indemnity type plans. It also offers medical and dental benefits to large groups that choose to self-fund all or a part of their benefits.

Tough rate regulations in Rhode Island somewhat constrain BCBSRI's business profile. Past decisions by the Office of the Health Insurance Commissioner (Rhode Island)--OHIC--to deny adequate premium rate increases has had a significant negative impact on the company's financial profile. BCBSRI's hospital provider concentration--Lifespan and Care New England Health System--also somewhat limits its business profile. These two hospital providers control more than 75% of the hospital beds in the state. Although we haven't seen any major contracting issues between BCBSRI and those providers, we do view this level of concentration as a limiting factor to the business profile.

Prospective

We expect that BCBSRI will maintain its position as the dominant health insurer in Rhode Island, and that its membership will likely remain flat in 2012--in the 505,000 to 506,000 range.

Management And Corporate Strategy: Improving Infrastructure To Compete More Efficiently

BCBSRI's management has maintained its market-leading position as a provider of affordable health care services in Rhode Island. The company has a history of good operating performance, as evidenced by its three-year (2006-2008) average ROR of 3.9%. However, in 2009 and 2010, a tough regulatory environment and overall weak economic conditions led to a sharp decline in earnings. The company has been able to turn around its operations in 2011, and we expect that the management will be able to execute on its medical and administrative cost improvement measures in the future.

Strategic positioning

BCBSRI is a not-for-profit health insurance company. A key facet of management's strategy is to position the company as a premium provider of health care by building a superior interactive relationship with its subscribers while maintaining strong pricing discipline. In addition, BCBSRI is focused on improving its provider contracting methodologies. Favorable discounts from hospitals and other health care entities have enabled BCBSRI to maintain competitive premium rates. The company also has been successful in switching to global fee contract agreements with a few community hospitals.

Operational effectiveness

We believe the company's senior management team has the necessary experience and expertise for this line of business. And the company usually performs according to its financial plans. Although there were occasions when the company did veer from its financial plans, these instances were caused by regulatory conditions. Rate regulations add some unpredictability to the company's operations.

Further, in line with its focus on improving operational management, BCBSRI is undertaking a major investment in technology to replace its information technology (IT) systems. The company's primary strategic objectives are to achieve cost efficiency and to enhance the servicing capabilities it needs to compete effectively with larger national health care companies. The new system should enable BCBSRI to support advanced integrated health management, reduce administrative costs, and improve process efficiencies. The company has contracted with a third-party vendor that has implemented this system for other major health insurers and Blue Cross and Blue Shield plans.

BCBSRI also implemented a patient-centered medical home model in 2010. Even though the project is still in its nascent stage, we view this strategic initiative favorably because patient-centered medical homes could potentially strengthen BCBSRI's care delivery systems and have a longer-term affect on reducing cost trends.

Financial management

BCBSRI maintains a high-quality balance sheet. It has no intangibles or long-term debt except for a commercial mortgage on its corporate headquarters. Management focuses on pricing its business rationally, underwriting its business conservatively, and improving its overall operating efficiencies. Management is also pursuing an expense control strategy that emphasizes greater technological efficiencies in order to help the company improve operating performance, remain price competitive, and enhance services for its stakeholders.

Governance

BCBSRI has an independent board of directors. The board is involved in developing goals and strategies for the company. We didn't note any material deficiencies in the company's audit controls.

The company has seen a couple of major changes in its senior management. The former CEO, James Purcell, retired in 2011, and the board hired Peter Andruszkiewicz as the new CEO after a nationwide search. Mr. Andruszkiewicz has significant experience in health insurance, and mostly recently was president of Kaiser Health Plan of Georgia. BCBSRI's previous CFO resigned earlier this year, and the board hired Mr. Michael Hudson as the new CFO. Mr. Hudson was most recently CFO at Health Plan Holdings in Tampa, Fla. Before that, he held senior management positions at Aetna and Cigna.

We will pay close attention to management's ability, under new CEO and CFO leadership, to continue to improve the company's near-term operational performance amid the currently tough regulatory environment in Rhode Island.

Enterprise Risk Management: Adequate For The Level Of Risk

We consider BCBSRI's enterprise risk management (ERM) to be adequate. The company's portfolio of health insurance products is not particularly complex. BCBSRI has good processes in place for identifying and mitigating risks. Both senior management and the board support the initiative. The head of the ERM team reports directly to the board's audit committee.

We expect that BCBSRI will continue to dedicate the resources necessary to promote ongoing integration of risk identification, risk management assessment, and management practices into its business process. Over the next few years, we believe the company will be able to further strengthen its ERM practices.

Accounting

In our view, BCBSRI maintains no unusual accounting practices. The company presents its financial statements on both a statutory and a generally accepted accounting principles (GAAP) basis. We adjusted the company's pretax income and ROR by excluding any realized investment gains or losses and other-than-temporary-impairments in order to focus on its operating earnings.

On statutory accounting basis, BCBSRI reports real estate (properties occupied by the company) as net of the outstanding mortgage loan and depreciation. As of Dec. 31, 2011, the company had a reported \$32.1 million--the total cost of construction (\$122.9 million) less the outstanding mortgage and depreciation on the property (\$90.8 million)--on its balance sheet.

Operating Performance: Earnings Stability Expected In The Near Term

We view BCBSRI's operating performance as improving and supportive of the current rating. The company had reported negative earnings in 2009 and 2010 due to higher-than-expected utilization rates coupled with inadequate premium rate increases. Its pretax income remained negative for two consecutive years: pretax loss (excluding realized investment gains or losses) of \$35 million in 2010 and pretax loss of \$101 million in 2009. The 2009 pretax loss included a premium deficiency reserve (PDR) of \$101 million, which was related to the inadequate rate increase received from the OHIC regarding commercial group and individual books of business. In 2010, the company released about \$9 million of the PDR and released the remaining (\$92 million) in 2012.

Operating performance improved in 2011, with the company reporting a pretax income (excluding realized gains and losses) of \$73 million, which translated to an ROR of 4.9%. The improvement in 2011 was primarily driven by improved results in the company's commercial business and the release of its PDR.

Excluding the impact of the PDR in 2011, the commercial segment reported better-than-2010 underwriting results, although the figure was still a loss due to the impact of previously approved inadequate rate increases. The Medicare Advantage (MA) segment in 2011 had positive underwriting income, which somewhat offset the weakness in the commercial results. Going forward, we expect adequate rates and improved administrative cost trends to help improve underwriting performance in the commercial book of business, while MA underwriting income will likely remain close to current levels.

Prospective

In 2012, we expect that the company's pretax ROR will be in the 1%-2% range. Further improvements in medical management and reduction in administrative costs will help maintain this positive trend in operating performance.

Investment And Liquidity: High-Quality Investment Portfolio

BCBSRI's liquidity profile is strong, underpinned by a liquid investment portfolio of high-quality fixed-income securities and cash investments. BCBSRI has an investment portfolio designed to match the short-term needs of its

liabilities and generate an adequate return in the long term to maximize policyholders' reserves. BCBSRI's liquidity ratio, as measured by Standard & Poor's liquidity model, was strong at more than 200% as of year-end 2010.

Majority of the company's assets are in fixed income securities. Equities, which currently make up about 8% of total invested assets, are in domestic and international equities. One key change in the portfolio's composition during 2010 was related to its exposure to equities. Due to the decline in its health risk-based capital (RBC) level, the company reduced its exposure to equities to 5% of total invested assets from 15%. Since its RBC level has increased in 2011, we expect BCBSRI will likely increase its equity exposure to closer to the 10% level.

Prospective

We expect BCBSRI's liquidity will remain strong, with a liquidity ratio of more than 200%, because of its high-quality investment portfolio.

Capitalization: Returning To Historical Strength

We believe that BCBSRI's risk-adjusted capitalization is strong and a key strength to the rating. In 2011, the company was able to stem the declining trend in capitalization it faced in 2010 and 2009. BCBSRI's statutory surplus improved almost 30% at year-end 2011 compared with year-end 2010.

Negative net income and higher levels of nonadmitted assets were the main reasons for the surplus decline in 2010 and 2009. The company's nonadmitted assets increased due to development of its new IT system and the deferred tax assets. In 2011, strong retained earnings helped strengthen in capitalization and add to its capital cushion.

In terms of risk-based capital, the company's capital adequacy also saw significant improvement. Based on our pro forma 2011 insurance capital model, capital is redundant at the 'AAA' level compared with only a 'A' level at year-end 2010. Also, in terms of the National Association of Insurance Commissioners' (NAIC) RBC, the company reported RBC (action company level) of 605% as of year-end 2011 compared with 454% at year-end 2010.

Prospective

We expect that BCBSRI will maintain a surplus that's redundant at least at the 'AA' confidence level.

Financial Flexibility: Sufficient Internal Accruals Offset Limited Capital Market Access

We believe that BCBSRI's financial flexibility is sufficient, supported by its relatively limited need for capital. In recent years, it has undertaken some capital expenditures, such as updating its IT system. We believe the company will likely be able to fund its capital expenditures through internal accruals without putting a strain on capital.

The company's access to external financing is limited because of its not-for-profit status and restricted access to the capital markets. Nevertheless, we believe the company will be able to meet any reasonable funding needs in the near term with its own resources.

Related Criteria And Research

- Research Update: Blue Cross & Blue Shield of Rhode Island Outlook Revised to Positive; 'BBB-' Rating Affirmed, April 2, 2012
- Criteria And Research Methodology For Assessing U.S. Insurers' Capital Adequacy Beyond The Financial Crisis, May 31, 2011
- Evaluating Insurers' Competitive Positions, April 22, 2009

Table 1

Blue Cross & Blue Shield Of Rhode Island Inc. Selected Statistics*					
(Mil. \$)	--Year ended Dec. 31--				
	2011	2010	2009	2008	2007
Total medical membership (000s) (consolidated)	505.6	514.2	535.2	579.1	591.2
Premiums earned	1,568.9	1,631.1	1,703.4	1,755.8	1,768.9
Net underwriting gain/loss	75.3	(60.6)	(126.2)	47.4	69.3
Net income/loss	72.7	(14.1)	(99.9)	43.5	61.3
Pretax return on revenue (excluding realized capital gains/losses) (%)	4.9	(2.1)	(5.9)	3.9	4.2
Pretax return on revenue (including realized capital gains/losses) (%)	4.6	(1.3)	(6.1)	2.8	4.3
Total assets	605.5	606.8	678.8	710.3	728.7
Total adjusted capital	323.4	249.0	298.7	412.3	428.8

*Based on statutory accounting.

Table 2

Blue Cross & Blue Shield Of Rhode Island Inc. Business Statistics					
	--Year ended Dec. 31--				
	2011	2010	2009	2008	2007
Number of members (000s)					
Fully insured risk membership	285.80	292.51	329.46	349.61	382.80
Nonrisk ASO/ASC membership	219.80	221.70	205.73	229.50	208.40
Total medical membership (consolidated)	505.60	514.21	535.19	579.11	591.20
Medicare Part D membership	8.99	9.08	8.92	8.10	9.46
BlueCard and National Par membership	93.50	96.90	93.03	99.20	98.51
Year-over-year change (%)					
Fully insured risk membership	(2.29)	(11.22)	(5.76)	(8.71)	(1.91)
Nonrisk ASO/ASC membership	(0.86)	7.76	(10.36)	10.12	2.88
Total medical membership (consolidated)	(1.67)	(3.92)	(7.58)	(2.07)	(0.27)
Medicare Part D membership	(0.94)	1.78	10.06	(14.35)	14.08
BlueCard and National Par membership	(3.51)	4.16	(5.90)	0.35	2.31
Premiums earned (mil.\$)	1,568.92	1,631.07	1,703.43	1,755.80	1,768.94
Year-over-year change (%)	(3.81)	(4.25)	(2.98)	(0.74)	4.25

Table 3

Blue Cross & Blue Shield Of Rhode Island Inc. Operating Statistics*					
	--Year ended Dec. 31--				
(Mil. \$)	2011	2010	2009	2008	2007
Total revenue	1,570.60	1,656.50	1,728.40	1,778.20	1,774.50
Net underwriting gain or loss	75.30	(60.60)	(126.20)	47.40	69.30
Pretax income (excluding realized capital gains or losses)	77.00	(35.20)	(101.20)	69.80	74.90
Pretax income (including realized capital gains or losses)	72.70	(21.20)	(105.10)	50.20	75.60
Net income or loss	72.70	(14.10)	(99.90)	43.50	61.30
Pretax return on revenue (excluding realized capital gains or losses) (%)	4.90	(2.10)	(5.90)	3.90	4.20
Pretax return on revenue (including realized capital gains or losses) (%)	4.60	(1.30)	(6.10)	2.80	4.30
Medical loss ratio (%)	79.40	87.80	92.10	84.00	84.70
Expense ratio (%)	15.70	15.60	15.00	13.10	11.30

*Based on statutory accounting.

Table 4

Blue Cross & Blue Shield Of Rhode Island Inc. Investment Statistics*					
	--Year ended Dec. 31--				
(Mil. \$)	2011	2010	2009	2008	2007
Net investment income	15.00	15.70	20.60	24.70	25.10
Net realized capital gain	(4.30)	14.00	(3.90)	(19.60)	0.70
Net investment gain	10.70	29.70	16.70	5.10	25.80
Net investment yield excluding realized capital gains and losses (%)	3.40	3.30	3.90	4.30	4.40
Net investment yield including realized capital gains and losses (%)	2.40	6.30	3.10	0.90	4.50
Total invested assets excluding real estate	441.40	439.20	506.50	556.90	603.00
Total invested assets	473.50	470.50	537.40	589.50	622.70
Portfolio composition					
Cash and short-term investments (%)	3.20	1.70	2.70	3.40	4.10
Bonds (%)	71.90	86.40	76.30	80.10	81.30
Preferred stock (%)	0.10	0.10	0.00	0.10	0.10
Total common stock (%)	8.70	3.90	14.30	10.20	11.20
Unaffiliated common stock (%)	8.70	3.90	14.30	10.20	11.20
Mortgages (%)	0.00	0.00	0.00	0.00	0.00
Real estate (%)	6.80	6.70	5.70	5.50	3.20
Other (%)	9.30	1.30	1.00	0.70	0.10
Total invested assets (%)	100.00	100.00	100.00	100.00	100.00

*Based on statutory accounting.

Table 5

Blue Cross & Blue Shield Of Rhode Island Inc. Capitalization Statistics*					
	--Year ended Dec. 31--				
(Mil. \$)	2011	2010	2009	2008	2007
Total assets	605.5	606.8	678.8	710.3	728.7
Total liabilities	282.1	357.8	380.1	298	299.9
Total adjusted capital	323.4	249	298.7	412.3	428.8

Table 5

Blue Cross & Blue Shield Of Rhode Island Inc. Capitalization Statistics* (cont.)					
Total equity assets to capital§ (%)	22.8	20.1	36.1	22.6	21

*Based on statutory accounting. §Includes real estate holdings.

Table 6

Blue Cross & Blue Shield Of Rhode Island Inc. Liquidity Statistics*					
(Mil. \$)	--Year ended Dec. 31--				
	2011	2010	2009	2008	2007
Cash flow from operations	15.50	(37.00)	(12.40)	31.80	78.00
Cash and short-term investments	15.20	7.90	14.40	19.90	25.80
Total invested assets (excluding real estate/affiliated investments/other)	401.00	433.30	501.40	552.90	602.30
Unpaid claims liability	113.00	126.40	124.70	133.60	147.30
Quick liquidity ratio (%)	13.50	6.30	11.50	14.90	17.50

*Based on statutory accounting.

Ratings Detail (As Of May 2, 2012)

Operating Company Covered By This Report

Blue Cross & Blue Shield of Rhode Island Inc.

Financial Strength Rating

Local Currency

BBB-/Positive/--

Counterparty Credit Rating

Local Currency

BBB-/Positive/--

Domicile

Rhode Island

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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State: Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.003 Small Group Only

Product Name: Small Group Commercial Medical

Project Name/Number: Small Group Medical Rating Factors for 2013 Dec Filing/SGM-201212

Supporting Document Schedules

		Item Status:	Status Date:
Bypassed - Item:	A&H Experience		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Actuarial Certification - Life & A&H		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Actuarial Memorandum - A&H Rate Revision Filing		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Health Insurance Checklist		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Premium Rate Sheets - Life & A&H		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Rate Summary Worksheet		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Consumer Disclosure Form		
Bypass Reason:	See rate/rule schedule documentation.		

State: Rhode Island **Filing Company:** Blue Cross & Blue Shield of Rhode Island
TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only
Product Name: Large Group Commercial Medical
Project Name/Number: Large Group Medical Rating Factors for 2013 Dec Filing/LGM-201212

Filing at a Glance

Company: Blue Cross & Blue Shield of Rhode Island
Product Name: Large Group Commercial Medical
State: Rhode Island
TOI: H15G Group Health - Hospital/Surgical/Medical Expense
Sub-TOI: H15G.002 Large Group Only
Filing Type: Rate
Date Submitted: 12/07/2012
SERFF Tr Num: BCBS-128801694
SERFF Status: Assigned
State Tr Num:
State Status: Open-Pending Actuary Review
Co Tr Num: LGM-201212
Implementation: On Approval
Date Requested:
Author(s): Jeffrey McLane, Catherine Mitchell, Sean Neylon
Reviewer(s): Herbert Olson (primary), Adrienne Evans, Sandra West, Charles DeWeese, Maria Casale
Disposition Date:
Disposition Status:
Implementation Date:

State: Rhode Island **Filing Company:** Blue Cross & Blue Shield of Rhode Island
TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only
Product Name: Large Group Commercial Medical
Project Name/Number: Large Group Medical Rating Factors for 2013 Dec Filing/LGM-201212

General Information

Project Name: Large Group Medical Rating Factors for 2013 Dec Filing Status of Filing in Domicile:
 Project Number: LGM-201212 Date Approved in Domicile:
 Requested Filing Mode: Review & Approval Domicile Status Comments:
 Explanation for Combination/Other: Market Type: Group
 Submission Type: New Submission Group Market Size: Large
 Group Market Type: Employer, Association Overall Rate Impact: 9%
 Filing Status Changed: 12/10/2012
 State Status Changed: 12/10/2012 Deemer Date:
 Created By: Sean Neylon Submitted By: Sean Neylon
 Corresponding Filing Tracking Number:

PPACA: Not PPACA-Related

PPACA Notes: null

Include Exchange Intentions: No

Filing Description:

Large Group Commercial Medical Rating Factors for new and renewal business effective January 1, 2013 through December 1, 2013 excluding so-called required early notice accounts effective January 1, 2013.

Company and Contact

Filing Contact Information

Sean Neylon, Actuarial Project Analyst sean.neylon@bcbsri.org
 500 Exchange Street 401-459-1278 [Phone] 1278 [Ext]
 Providence, RI 02903

Filing Company Information

Blue Cross & Blue Shield of Rhode Island	CoCode: 53473	State of Domicile: Rhode Island
500 Exchange Street	Group Code:	Island
Providence, RI 02903	Group Name:	Company Type: Health Insurance
(401) 459-1000 ext. [Phone]	FEIN Number: 05-0158952	State ID Number:

Filing Fees

Fee Required? Yes
 Fee Amount: \$125.00
 Retaliatory? No
 Fee Explanation: Five products filed times \$25 per product
 Per Company: Yes

Company	Amount	Date Processed	Transaction #
Blue Cross & Blue Shield of Rhode Island	\$125.00	12/07/2012	65543783

State: Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only

Product Name: Large Group Commercial Medical

Project Name/Number: Large Group Medical Rating Factors for 2013 Dec Filing/LGM-201212

Rate Information

Rate data applies to filing.

Filing Method: Review and Approval

Rate Change Type: Increase

Overall Percentage of Last Rate Revision: 9.000%

Effective Date of Last Rate Revision: 01/01/2013

Filing Method of Last Filing: Review and Approval

Company Rate Information

Company Name:	Company Rate Change:	Overall % Indicated Change:	Overall % Rate Impact:	Written Premium Change for this Program:	# of Policy Holders Affected for this Program:	Written Premium for this Program:	Maximum % Change (where req'd):	Minimum % Change (where req'd):
Blue Cross & Blue Shield of Rhode Island	Increase	9.000%	9.000%	\$34,474,000	38,231	\$417,413,000	5.000%	13.000%

Product Type:	HMO	PPO	EPO	POS	HSA	HDHP	FFS	Other
Covered Lives:		69,275		1,849	4,208	1,191	255	
Policy Holders:		34,864		847	1,887	499	134	

State: Rhode Island Filing Company: Blue Cross & Blue Shield of Rhode Island
 TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only
 Product Name: Large Group Commercial Medical
 Project Name/Number: Large Group Medical Rating Factors for 2013 Dec Filing/LGM-201212

Rate Review Detail

COMPANY:

Company Name: Blue Cross & Blue Shield of Rhode Island
 HHS Issuer Id: 53473
 Product Names: HealthMate Coast to Coast
 HealthMate Coast to Coast HDHP
 HealthMate Coinsurance Option
 HealthMate for HSA
 HealthMate for HRA
 BlueSolutions for HSA
 BlueSolutions for HRA
 Classic
 VantageBlue Coinsurance
 BlueChip
 Trend Factors: Baseline trend increase of 7.3%; net of new PBM contract @ 1/1/2013 and demographics, effective trend is 3.6%

FORMS:

New Policy Forms:
 Affected Forms:
 Other Affected Forms: FRONT GRP (09-10); SUMMARY GRP (09-10); INTRODUCTION GRP (09-10); ELIGIBILITY GRP (09-10); COVERED GRP (09-10); EXCLUSIONS GRP (09-10); HOW WE PAY GRP(09-10); COB GRP (09-10); APPEALS GRP (09-10); GLOSSARY GRP (09-10).

REQUESTED RATE CHANGE INFORMATION:

Change Period: Annual
 Member Months: 921,336
 Benefit Change: None
 Percent Change Requested: Min: 5.0 Max: 13.0 Avg: 9.0

PRIOR RATE:

Total Earned Premium: 382,669,000.00
 Total Incurred Claims: 331,020,000.00
 Annual \$: Min: 398.00 Max: 415.00 Avg: 432.00

REQUESTED RATE:

Projected Earned Premium: 417,143,000.00
 Projected Incurred Claims: 342,937,000.00
 Annual \$: Min: 436.00 Max: 469.00 Avg: 453.00

SERFF Tracking #:

BCBS-128801694

State Tracking #:

Company Tracking #:

LGM-201212

State:

Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI:

H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only

Product Name:

Large Group Commercial Medical

Project Name/Number:

Large Group Medical Rating Factors for 2013 Dec Filing/LGM-201212

Rate/Rule Schedule

State: Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only

Product Name: Large Group Commercial Medical

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Item No.	Schedule Item Status	Document Name	Affected Form Numbers (Separated with commas)	Rate Action	Rate Action Information		Attachments
1		2013 Large Group Cover Memorandum	FRONT GRP (09-10), SUMMARY GRP (09-10), INTRODUCTION GRP (09-10), ELIGIBILITY GRP (09-10), COVERED GRP (09-10), EXCLUSIONS GRP (09-10), HOW WE PAY GRP (09-10), COB GRP (09-10), APPEALS GRP (09-10), GLOSSARY GRP (09-10)	Revised	Previous State Filing Number:		OHIC 2013 Large Group Rate Factor Filing.pdf
					Percent Rate Change Request:	9.000	
2		2013 Large Group Actuarial Memorandum		Other	Previous State Filing Number:		2013 Actuarial Memo - Large Group.pdf
					Percent Rate Change Request:		
3		Exhibit 1 - Large Group		Other	Previous State Filing Number:		LG Exhibit 1 - Template.pdf
					Percent Rate Change Request:		
4		Exhibit 2 - Operating Expense		Other	Previous State Filing Number:		Exhibit 2 -2013 filing (both Large and Small).pdf
					Percent Rate Change Request:		
5		Exhibit 3 - Milliman, Inc. Actuarial Opinion		Other	Previous State Filing Number:		Exhibit 3 Milliman Opinion RIX01 Letter 20121204 doc.pdf
					Percent Rate Change Request:		

SERFF Tracking #:

BCBS-128801694

State Tracking #:

Company Tracking #:

LGM-201212

State: Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

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Item No.	Schedule Item Status	Document Name	Affected Form Numbers (Separated with commas)	Rate Action	Rate Action Information	Attachments				
6		Exhibit 4 - S & P Rating Report		Other	<table border="1"> <tr> <td>Previous State Filing Number:</td> <td></td> </tr> <tr> <td>Percent Rate Change Request:</td> <td></td> </tr> </table>	Previous State Filing Number:		Percent Rate Change Request:		Exhibit 4 - S and P BCBSRI_Full Analysis_2012.pdf
Previous State Filing Number:										
Percent Rate Change Request:										

December 7, 2012

Mr. Christopher F. Koller
Health Insurance Commissioner
Office of Health Insurance Commissioner
1511 Pontiac Avenue, Bldg. 69-1
Cranston, Rhode Island 02920

Subject: 1) Rating Factors Applicable to Large Group Subscription Rates for Business
Written or Renewed in 2013

Dear Commissioner Koller:

This letter and the attached documents comprise a rate factor filing by Blue Cross & Blue Shield of Rhode Island ("BCBSRI") of claims projection trends, reserve contribution factors, and related rating information to be used in commercial rating of large employer groups.

As you know, premium is driven primarily by medical expenses paid on behalf of our members. This equates to roughly 85% of each premium dollar. Medical expenses are driven by both utilization (frequency and volume) of services and the cost of those services. Since our filing in May of 2012, which relied on medical expenses incurred in calendar year 2011, we have experienced a significant increase in medical expense trend. Because the approved rate factors and rate cap do not reflect this unanticipated escalation in costs, absent this filing, rates for the calendar year 2013 will be inadequate to cover expenses. This filing is necessary to meet our fiduciary obligation to act in a financially prudent manner.

We recognize the burden of high healthcare costs on the businesses and people of Rhode Island and we do not take this filing lightly. Since your September decision on our previous filing, we have conducted various analyses to understand the actual and emerging costs and to test our projections for future medical trend. To ensure that our methods and assumptions in this filing are actuarially sound, we engaged Milliman, Inc to review our filing.

We have identified the following key factors driving our medical expenses:

- Increases in inpatient costs per admission have added about 1% to overall medical spend over the past year.
- Inpatient admissions are up 3.9% over 2011.
- Outpatient costs have increased steadily as more complex and expensive treatments are provided in an outpatient setting. This is particularly driven by a rapid increase in costs associated with specialty outpatient chemotherapy treatment.

These topics are discussed in more detail in the enclosed filing. As a result of these increased medical expenses, among other factors, this filing reflects an overall average rate increase of 9.0%, which is 5.0% higher than the rate cap previously approved by your office. Please note

that while this filing provides for an increase in our 2013 rates over the levels previously approved, the rate increases we are proposing are lower than the Large Group rate increases you have approved over the last four years.

The current 4.0% rate cap places BCBSRI's financial stability in serious jeopardy. After four years of underwriting losses, BCBSRI ranks last among Blue Cross and Blue Shield plans nationwide in financial strength as measured by the amount of Risk Based Capital ("RBC"). Without an increase to the rate cap now, or a much more significant increase to 2014 renewals, BCBSRI's reserve level will fall below 375% RBC by the end of 2014 resulting in sanctions from the Blue Cross and Blue Shield Association.

We recognize that providing affordable healthcare is critical to our customers, members, and the Rhode Island economy. For these reasons, we have undertaken a number of initiatives designed to aggressively transform our business, improve internal operations, and moderate both medical and administrative expense trends. We continue to work collaboratively with our healthcare delivery system partners to develop and implement new approaches that pay for quality, not quantity, of care. These ongoing and important efforts have proven to be successful and are expected to continue for the coming years. Some of the measurable outcomes include:

- We are on target to reduce operating expenses by roughly \$15 million, or 7% in 2013;
- Professional Services costs have decreased by 2.7% due to innovative provider contracting arrangements and the establishment of an enhanced radiology management program;
- A new pharmacy benefit management contract with Catamaran will mitigate pharmacy expenses in 2013. The projected savings resulting from this contract is about \$65 million over three years for group insured business, and reduces the average annual premium increase for employers by roughly 2.2% in this filing.

We respectfully ask for your timely consideration and approval of the proposed rating factors as submitted. We believe that the proposed rating factors are in the best interest of both the public and the corporation and consistent with the proper conduct of our business. As always, we are available and prepared to respond to any questions you, your staff, or your consulting actuary, Mr. DeWeese, may have.

Sincerely,



Michael Hudson, FSA, MBA
Executive Vice President & Chief Financial Officer

ACTUARIAL MEMORANDUM FOR LARGE GROUP COMMERCIAL RATING

Revised Group Rate Factor Filing

Blue Cross & Blue Shield of Rhode Island (“BCBSRI”) submits this filing as an amendment to the 2013 Large Group rating factors approved by the Office of Health Insurance Commissioner in September 2012. This filing results in a 9.0% average renewal increase for the 2013 rating period. This average increase replaces the 4.0% rate cap that was previously approved in September 2012.

Several factors contribute to the expected average increase, with the major factor being an updated claims experience base (3.1% impact)¹. Our expectation of future trend has increased modestly as well (1.4% impact). Finally, the operating expenses included in this filing are consistent with the expenses originally filed by BCBSRI in May 2012 (0.5% impact). This filing also addresses BCBSRI’s reserve position and rate cap compliance.

This filing will apply to all 2013 new and renewal business except so-called early notice January 2013 accounts that were rated in accordance with the May 2011 filing (approved on July 19, 2011). Please note, however, that an account which has already received a new business or renewal rate prior to the approval of this filing will not receive an additional rate change.

Financial Results

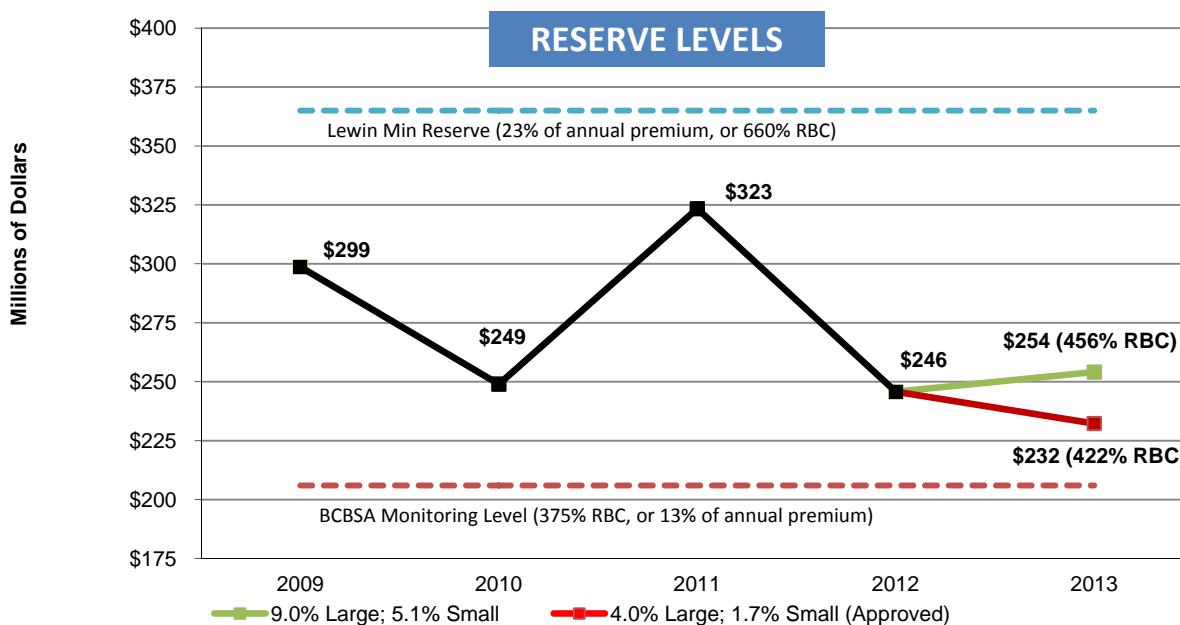
Through September 2012, BCBSRI has experienced a commercial group operating loss of \$33.6 million, which we project will be \$40.7 million by year end. The full year net loss for 2012 marks the fourth consecutive year BCBSRI has posted an Underwriting loss, despite being approved for a reserve contribution factor. These historical losses have resulted in a \$167 million reduction to our overall reserves, which we project to be \$245.8 million (454% RBC) by year end 2012.

BCBSRI strongly believes these reserve levels are below an acceptable range given the current regulatory environment and uncertainty of risk associated with the Patient Protection & Affordable Care Act (“ACA”). Our current reserve level would cover approximately one emergency room visit for each of our members.

The recommended minimum reserve level (23% of premium) cited in the Lewin Study for OHIC in August 2006 presently equates to \$358 million or 661% RBC. Our 2012 reserve projection falls \$119 million below that benchmark. In addition, the Blue Cross and Blue Shield Association (“BCBSA”) maintains a financial performance standard applicable to all licensees. This standard requires monitoring to begin if a licensee falls at or below 375% of risk-based capital, which equates to roughly \$203 million in reserves. Compared to all other independent Blue Cross Blue Shield plans nationwide, BCBSRI currently has the lowest reserve adequacy level measured in terms of risk-based capital. The charts on the next page illustrate our reserve

¹ The May filing utilized calendar year 2011 data; this filing has data incurred through July 2012.

levels and underwriting losses in the commercial group market for the past few years. We have also included a projection of our previously approved 2013 filing versus this filing.

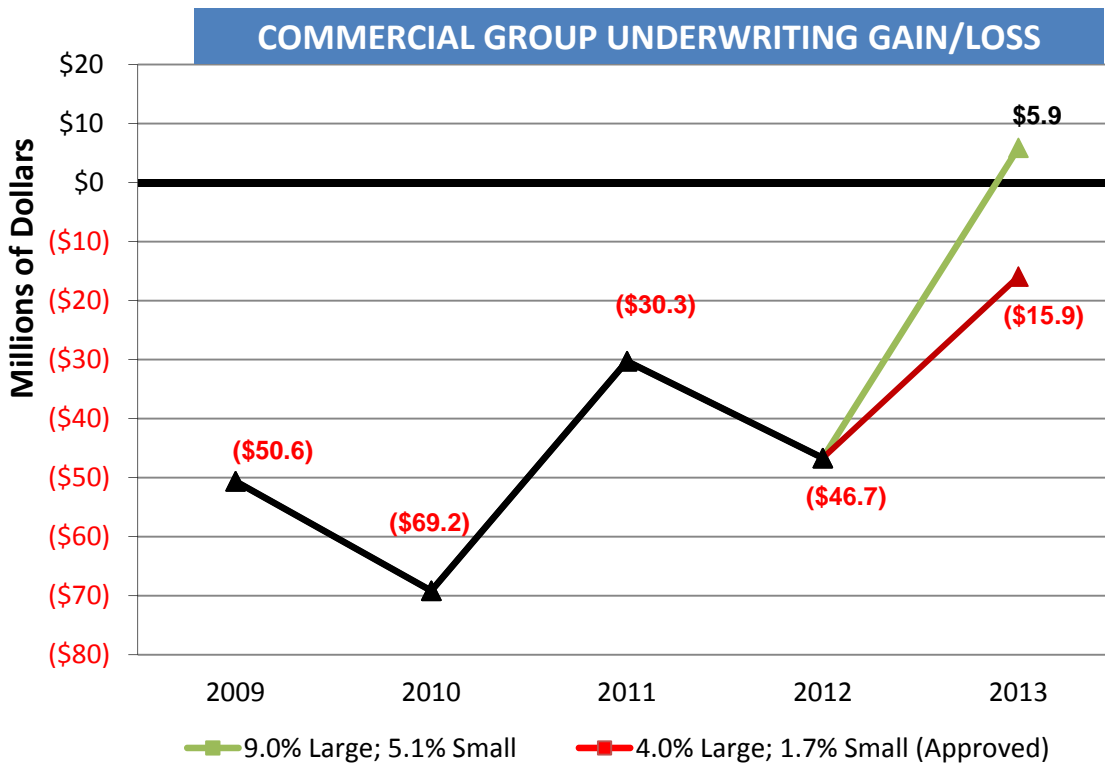


In May 2012, Standard & Poor’s issued their annual credit rating of BCBSRI (see Exhibit IV). It upheld a prior year downgrade to BBB, which is the lowest investment-grade credit rating. This latest report cites a “difficult regulatory environment as evidenced by inadequate premium rate approvals in the past” as a primary driver of the continued lower rating. Recognizing the need for strong risk-adjusted capitalization, we anticipate Standard & Poor’s future rating evaluations would be negatively impacted by continued deterioration of operating performance and the resulting drawdown on reserves. The Standard & Poor’s credit rating is an important risk indicator that many current and prospective clients review as they make decisions about purchasing services from us, and it also has a direct impact on our ability to maintain an affordable credit line.

New ACA fees will also deteriorate our reserve position beginning in 2014. In 2014 the estimated Health Insurer and Transitional Reinsurance fees on our Small and Large group business will amount to \$30 million. About 30% of our 2014 premium volume will arise from the 2013 renewal rates as determined by this filing. As a result, the ACA fees alone will represent a \$9 million reserve strain. The fees effectively lower the reserve contribution by 1.1% of group premium covered by this filing. This does not include any additional assessments the state may impose to cover the costs of discharging its ACA-related responsibilities (e.g., exchange-related funding).

Other carriers across the country are filing for these fees in their 2013 rate submissions and have received regulatory approval to recover their liability. Within New England, the Connecticut, Massachusetts, and New Hampshire insurance departments have approved the inclusion of ACA fees in 2013 rate year filings. It would be standard actuarial practice and good accounting for carriers to reflect ACA fees in the development of 2013 plan year rates in proportion to the

degree the policy years extend into calendar year 2014. However, in accordance with OHIC’s instructions this filing makes no provision for the collection of the new ACA fees.



This chart displays the commercial group portion of BCBSRI underwriting losses since 2009 and projected gain/loss scenarios for 2013.

BCBSRI understands the importance of providing predictable, affordable, and adequate rates to our customers. However, our deteriorating financial position and obligation to act in a prudent manner and in the best interest of the Company requires that we submit this filing. If this filing is not approved, BCBSRI projects that we will enter BCBSA monitoring in 2014 when our reserve level drops below 375% RBC. In the event our RBC ratio falls below 200%, we will lose our BCBSA license and Blue Cross/Blue Shield trademarks. This would dramatically impair our ability to attract new enrollment. Additionally, as a member of the BCBSA, we and our customers benefit from the very favorable provider reimbursement arrangements our fellow Blue plans are able to negotiate. Approximately 25% of the medical payments we make are to providers outside of Rhode Island. These payments are for services rendered to Rhode Island residents who receive care out of state as well as non-residents who are covered by our Rhode Island group customers. If we were to lose our status as a licensee of the BCBSA, we would likely not be able to negotiate payment terms as favorable. Our inability to do so would inevitably lead to a loss of a significant volume of business and would threaten our continued survival.

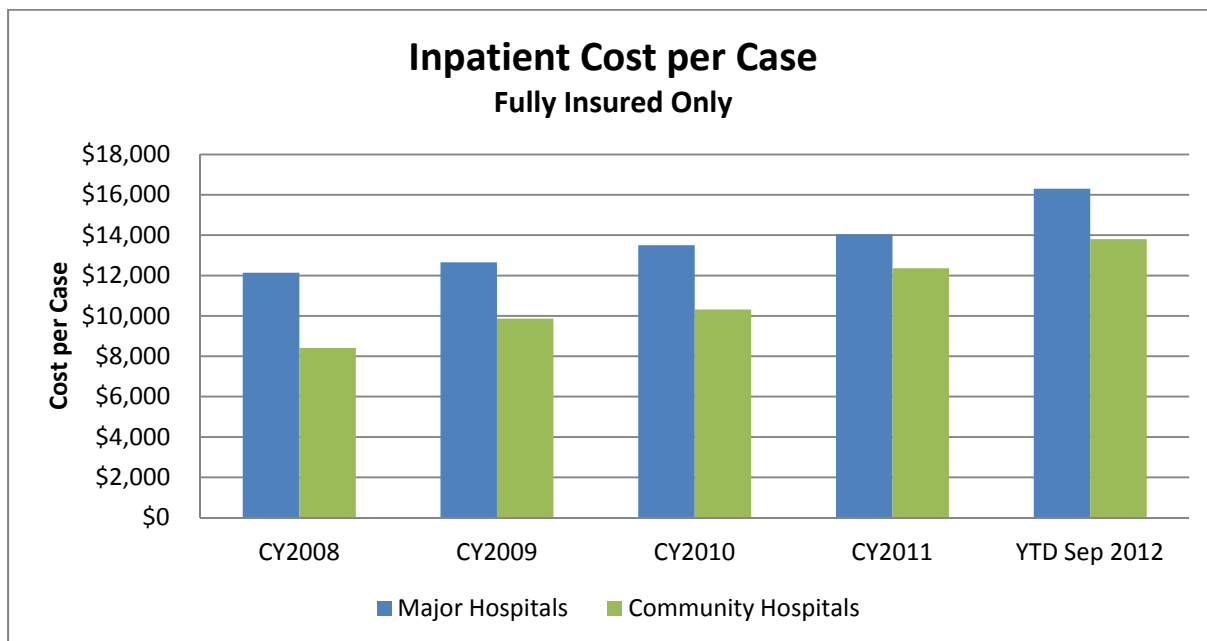
Medical Expenses

Exhibit I, *Large Group Rate Filing Template*, illustrates the variances by cost category between our previous filing and our current projection based on an additional seven months of experience. Our primary concern with the gap between projections is maintaining the soundness of our actuarial rating standards while also being compliant with OHIC's promulgated rate cap. It is not our intent to recoup losses we have experienced in 2012 or the preceding three years. However, we do need the ability to incorporate the updated claims experience when we rate Large Groups.

The trend factors being proposed in this filing were developed in accordance with the methodology we have used in all recent rate factor filings. The unit price trends are based on existing provider contracts and a best estimate of the price increases for those provider contracts that are still outstanding. Utilization trends were developed through an analysis of 36 months of historical experience through July 2012 incurred dates. The medical trend factors being proposed for our Small Group segment are in the aggregate equal to what was filed and approved in our May submission. The medical trend factors being proposed for our Large Group segment are in the aggregate 80 basis points higher than what was filed and approved in our May submission. This is due to the trend acceleration we have seen over the course of 2012.

Below is a description of several key drivers of medical trends in this filing:

Hospital Per Admission Costs –The average cost per admission increased over 2011 levels, with a net impact of 1% on overall medical trend. The chart below shows the average cost per admission for major versus community hospitals since 2008. We are currently working with our local hospitals to moderate cost per admission trends for 2013 and forward.



Maternity and Behavioral Health Costs – Overall, the per admission costs for maternity and behavioral health admissions in 2011 are higher than their respective Blue Health Intelligence (BHI) regional averages for 2011. This excess cost adds approximately 1% to Commercial premium rates. BHI is a data set made up from a large number of Blue Cross and Blue Shield plans from across the country. For the regional comparison cited here we utilized the aggregated data of five Blue Cross plans located in the northeast United States.

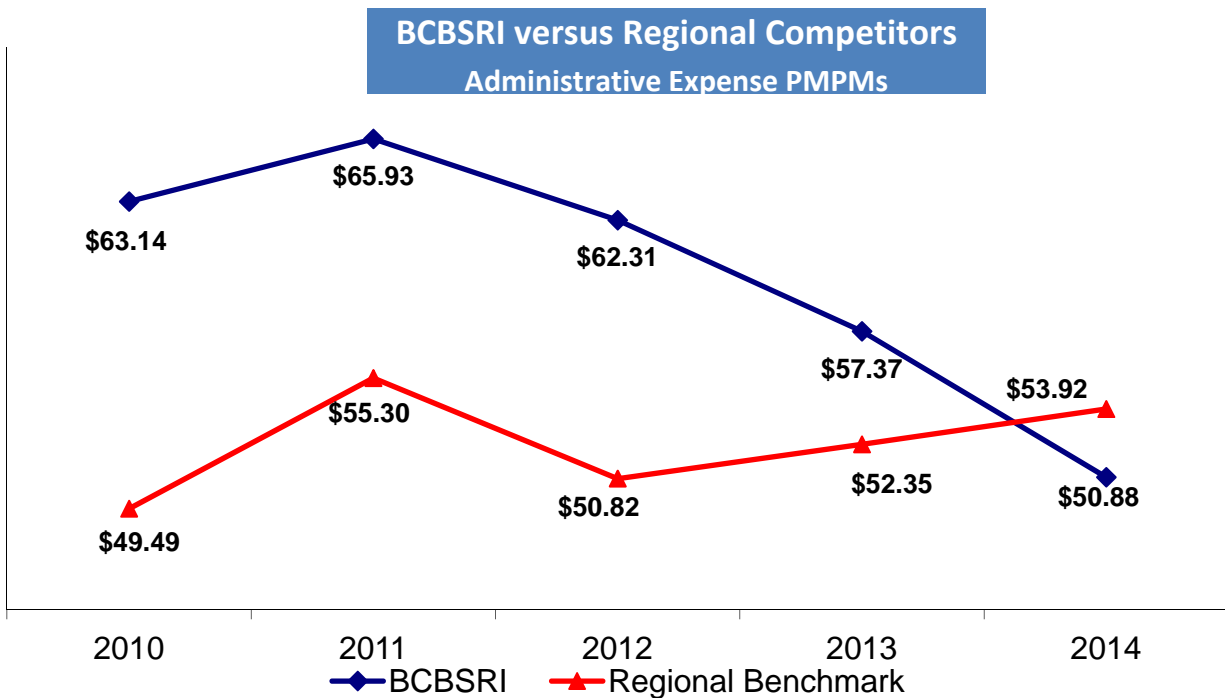
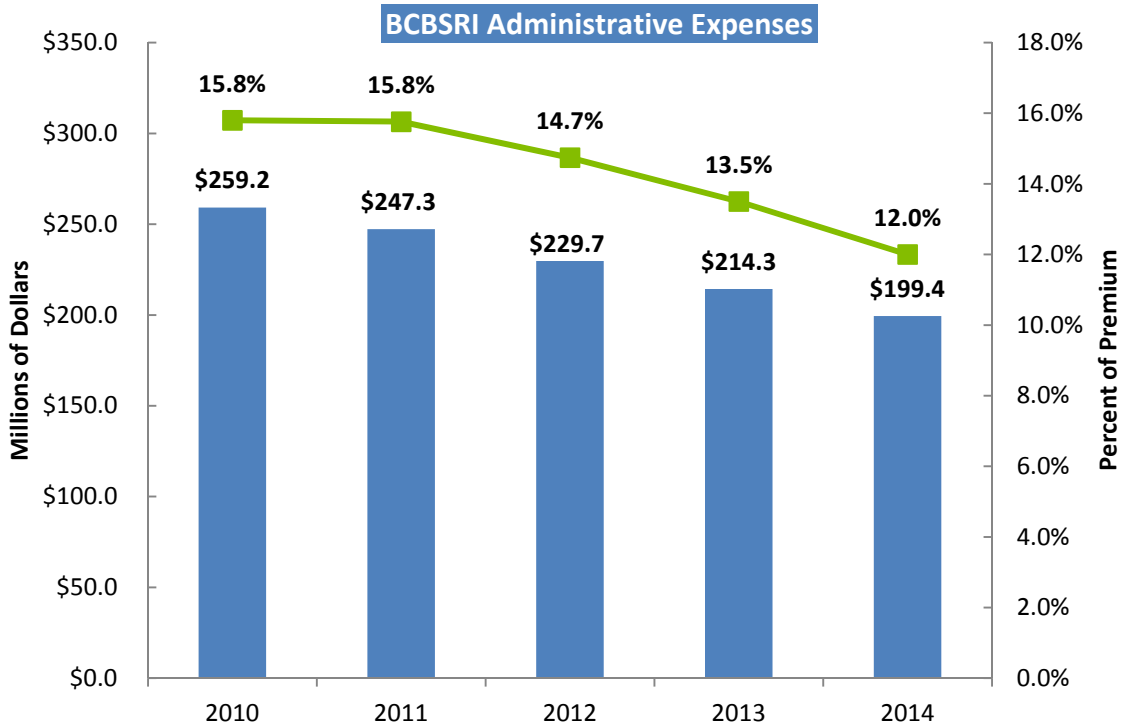
Hospital Rate of Admission – The hospital admission rate across our group business has increased 3.9% over 2011 levels. This reverses the declining inpatient admission rates we have seen over recent years. This increased admission rate has added about 1% to our overall medical trend.

Outpatient Chemotherapy/Injections – BCBSRI has also seen a significant increase in costs and utilization for drugs provided in outpatient facilities. This includes drugs used for chemotherapy as well as other drugs administered in a facility setting. Year-to-date trends for these drugs are running at about 24%. This trend is being driven equally by utilization (11%) and price (12%). This trend is not attributed to any particular drug or new therapy, but rather a general increase in use and some widespread pricing increases by drug manufacturers. This escalation has increased our overall insured cost by .6%.

Operating Expenses

Exhibit II, *Administrative Costs Request*, provides information on our actual 2011 and projected 2013 administrative costs as well as the administrative charge levels we are proposing to assess in this submission. The administrative charges being proposed in this filing are consistent with the operating expense levels we will reach by 2014, but do not cover the entirety of expected 2013 expenses. This shortfall is about \$9 million and lowers the reserve contribution by 1.1% of premium covered by this filing. In prior filings, we had laid out a multiyear glide path to reduce operating expenses to approximately 12% of premium, consistent with our regional benchmarks. Since 2010, we have reduced operating expense by \$45 million—a reduction from 15.8% of premium in 2010 to 13.5% in 2013. Our 2014 benchmark of 12% means an additional \$15 million of administrative expense reductions.

We are confident that we will achieve this goal in 2014 and for this reason are proposing to base our 2013 rates on this level of operating expenses. The first chart on the next page summarizes the progress that we have made. The second chart compares our actual and projected per member per month charges with those of other carriers operating in the region. The expense levels in the second chart reflect the expense levels reported in financial statements filed by each carrier through 2012. The 2012 data is based on the statements filed through June 30, 2012. For earlier years, we pulled the data from the annual statement blanks. The benchmarks for 2013 and 2014 were developed by applying an assumed 3% inflation rate to the historical data. Please note that the values reported in these tables reflect operating expenses levels across the entire organization and not just those associated with the Commercial Group business. Our regional benchmarking is consistent with the benchmarking study OHIC commissioned from Wakely last year. However, our comparison excludes state premium taxes since differences in state tax levels have nothing to do with a carrier's operating efficiency.



OHIC's September 2012 decision to reduce our administrative charges was based on a comparison of our proposed charges with those of the other carriers. However due to inconsistencies in the way carriers characterize expenses as "medical" or "administrative," we do not believe the comparison made by OHIC was appropriate. Specifically, in a footnote to Part 1 of its rate factor filing template United clearly indicates that certain capitation payments and "other costs associated with affiliated agreements, i.e. OPTUM SERVICES" have been included

with medical expenses. We also note that in its approved rating formula Tufts included certain of its cost-containment expenses in medical expenses for rating purposes. On the other hand, the administrative charges we propose to assess are our only provision to recover our operating expenses. Therefore, we submit that it is not appropriate to compare the administrative charge levels being proposed by the different carriers without first adjusting for these differences in characterization.

The 9.0% average rate increase estimate included in this filing was developed by applying our proposed rating factors to all 2013 renewals excepting only the advanced notice groups that were rated in accordance with the May 2011 filing. We are proposing that this average rate increase become the rate cap applicable to all 2013 new and renewing business and against which compliance will be monitored.

Projections of future medical costs are invariably wrong. They are either too high or too low due to changes in the morbidity and composition of the covered population, changes in medical practice and/or simple statistical fluctuation. In order to reduce these projection errors it is our practice (and standard industry practice) to utilize the most up to date experience period data available at the time we are actually setting rates. Additionally we point out that another source of divergence between the filed estimate and the actual formula driven average rate increase are unknowns about the current rates and the composition of the book of business that will actually be rated. Some of the cases that will be getting a renewal rate increase next year will not have been renewed or, in the case of new business, even written at the time of our rate filing. Furthermore a fair number of the cases included in the projection of the estimated average rate increase will not remain in force and hence will not be part of the actual average increase that will be monitored. For all of these reasons we suggest that OHIC permit carriers to apply their approved rating formulas to the developing experience and the actual business that winds up being issued a renewal even if the resulting average rate increase runs at least somewhat above the promulgated rate cap without the need to submit a new rate filing. Our consulting actuaries at Milliman, Inc share this view as discussed in their actuarial opinion letter (see Exhibit III). We would like the opportunity to discuss with OHIC the appropriate size of permitted deviations from the rate cap.

We note that the Medical Loss Ratio provisions of the ACA will prevent us (or any carrier) from making any windfall profit. Premium revenues in excess of the 80% of claims in the Small Group market and 85% in the Large Group market will have to be returned to customers in the form of rebates. Additionally, if our future medical experience unfolds more favorably than we are currently projecting, we will recognize it in accordance with the provisions of our approved rating formula that provides for us to utilize updated experience period data.

If both Small Group and Large Group filings are approved as filed, we anticipate that it will result in a CY 2013 underwriting gain across our combined Small and Large Group business of \$6 million. This amounts to less than 1% of annual premium. Our experience would have to get materially better than we are forecasting for our proposed rating factors to result in excessive gains.

Actuarial Certification

In accordance with the filing fee requirements contained in R.I. Gen. Laws § 42-14-18, an electronic funds transfer (EFT) transaction in the amount of \$125 is submitted via the SERFF system. Policy forms pertaining to this filing are listed in Attachment 1 to this Memorandum.

The actuarial assumptions underlying this filing have been developed by my staff and reviewed by myself. With one qualification, I certify that this rate factor filing was developed utilizing sound actuarial assumptions and methodologies. My sole reservation relates to excluding any provision for the new ACA fees that will be assessed in 2014 on business that will be rated under this filing.

In addition, we engaged Milliman to provide an independent third party review of the data and analysis used in the development of this rate filing (see Exhibit III). Their opinion letter is being submitted with this filing. It concludes that our methods and assumptions are actuarially sound and result in factors that are reasonable and appropriate.

This filing includes the following Exhibits:

- Exhibit I, *Large Group Rate Filing Template*
- Exhibit II, *Administrative Costs Request*
- Exhibit III, *Actuarial Opinion Letter from Milliman, Inc re: Actuarial Review of Rating Factors Applicable to Small and Large Group Subscription Renewals (“Group Rating Factor Filing”)*
- Exhibit IV, *Standard and Poor’s, Global Credit Portal[®] RatingsDirect[®], Blue Cross & Blue Shield, Inc*



John Lynch, F.S.A., M.A.A.A.
Chief Actuary
Blue Cross & Blue Shield of Rhode Island

Attachments

Attachment 1: Policy Forms

Policy forms pertaining to this filing are as follows:

FRONT GRP (09-10);

SUMMARY GRP (09-10);

INTRODUCTION GRP (09-10);

ELIGIBILITY GRP (09-10);

COVERED GRP (09-10);

EXCLUSIONS GRP (09-10);

HOW WE PAY GRP (09-10);

COB GRP (09-10);

APPEALS GRP (09-10); and

GLOSSARY GRP (09-10).

Blue Cross & Blue Shield of Rhode Island
Large Group Rate Filing Template: December 2012 Filing

Part 1. Historical Information

Experience Period for Developing Rates

From	To
10/1/2009	9/30/2012

Utilization/Experience Data by Quarter (Last 12 Available Quarters)

Quarter	End Date	IP Days	Member Months	Earned Premium	Incurred Claims Total	Incurred Claims IP	Incurred Claims OP	Incurred Claims		Incurred Claims Rx	Loss Ratio	Quality Improvement Expense*	Other Cost Containment Expense*	Other Claim Adjustment Expense*	Other Operating Expense*	Investment Income	Premium Tax	Commissions	Contribution to Reserves
								Primary Care	M/S										
1 (Oldest)	12/31/2009	10,808	424,918	\$155,426	\$133,890	\$28,102	\$32,207	\$5,710	\$42,588	\$23,046	86.1%	\$1,318	\$2,328	\$9,857	\$17,496	\$228	\$3,122	\$3,051	(\$15,407)
2	3/31/2010	6,889	405,840	\$154,278	\$134,067	\$33,441	\$34,099	\$4,815	\$39,315	\$22,398	86.9%	\$1,277	\$1,939	\$7,417	\$11,297	\$426	\$3,045	\$2,037	(\$6,374)
3	6/30/2010	9,978	405,459	\$151,992	\$134,327	\$26,587	\$28,765	\$4,583	\$49,558	\$24,834	88.4%	\$1,252	\$1,889	\$7,235	\$11,035	\$426	\$3,045	\$2,037	(\$8,401)
4	9/30/2010	9,803	395,911	\$149,395	\$132,518	\$28,028	\$31,712	\$4,523	\$44,556	\$23,700	88.7%	\$1,261	\$1,908	\$7,303	\$11,133	\$426	\$3,045	\$2,037	(\$9,385)
5	12/31/2010	10,194	388,546	\$146,897	\$132,179	\$24,322	\$27,898	\$4,588	\$50,748	\$24,622	90.0%	\$1,239	\$1,864	\$7,143	\$10,903	\$426	\$3,045	\$2,037	(\$11,087)
6	3/31/2011	11,279	368,670	\$146,381	\$121,082	\$30,421	\$29,877	\$4,553	\$33,939	\$19,642	82.7%	\$1,167	\$1,877	\$6,469	\$10,815	\$331	\$2,979	\$2,254	\$69
7	6/30/2011	10,250	365,863	\$149,128	\$124,908	\$29,555	\$31,604	\$4,513	\$36,202	\$20,384	83.8%	\$1,160	\$1,865	\$6,428	\$10,750	\$345	\$2,994	\$2,646	(\$1,279)
8	9/30/2011	10,256	367,421	\$141,139	\$122,812	\$29,433	\$30,993	\$4,473	\$34,857	\$20,074	87.0%	\$1,152	\$1,860	\$6,407	\$10,688	\$313	\$2,969	\$2,645	(\$7,080)
9	12/31/2011	9,219	368,315	\$146,395	\$123,494	\$27,215	\$31,599	\$4,780	\$35,902	\$21,016	84.4%	\$1,265	\$2,014	\$6,944	\$11,678	\$369	\$3,130	\$2,360	(\$4,121)
10	3/31/2012	10,160	361,651	\$143,517	\$125,094	\$33,196	\$30,954	\$4,149	\$33,402	\$20,498	87.2%	\$861	\$1,958	\$4,604	\$9,916	\$309	\$3,156	\$2,668	(\$4,431)
11	6/30/2012	9,886	358,135	\$141,660	\$127,041	\$33,850	\$31,485	\$3,959	\$33,991	\$20,649	89.7%	\$914	\$2,087	\$5,014	\$10,513	\$327	\$3,178	\$2,611	(\$9,371)
12	9/30/2012	9,067	359,984	\$142,935	\$123,833	\$31,925	\$31,005	\$4,118	\$33,149	\$20,527	86.6%	\$889	\$2,025	\$4,810	\$10,234	\$314	\$3,103	\$2,592	(\$4,238)

* These categories should conform generally to the reporting in the NAIC statement Underwriting & Investment Exhibit Part 3- Analysis of Expenses and/or to the Supplemental Health Care Exhibit, Lines 6.3 and 8.1
If any of the historical information reported is different from that period as reported in the prior rate filing, please provide a reconciliation and explanation showing the amount of each element of difference.

Part 2. Prospective Information

A. Trend Factors for Projection Purposes (Annualized)

	IP	OP	Primary Care	Other M/S	Rx	Weighted Total
Total	7.66%	9.02%	11.21%	5.79%	5.63%	7.25%
Price Only	4.86%	4.15%	6.76%	1.55%	1.33%	3.19%
Utilization	1.00%	4.00%	3.50%	3.50%	3.00%	2.92%
Mix	1.00%	0.00%	0.00%	0.00%	0.00%	0.24%
Leveraging	0.65%	0.65%	0.65%	0.65%	1.20%	0.75%
Weights	24%	25%	5%	28%	19%	100%

Note: The above factors together with the new PBM impact and expected demographic changes produce an effective 2013 over 2012 trend of 3.6%.

Blue Cross & Blue Shield of Rhode Island
Large Group Rate Filing Template: December 2012 Filing

B. The following items for the period to which the rate filing applies, by quarter:

Quarter	Beginning Date	Average %	Expected	Expected	Quality	Other Cost	Other Claim	Other	Average	Investment	Premium Tax
		Rate Increase	Pure Medical Cost Ratio	Contribution to Reserves %	Improvement Expense %*	Containment Expense %*	Adjustment Expense %*	Operating Expense %*	Commissions %*	Income Credit %	
Weighted Average		9.0%	82.2%	3.3%	0.6%	1.0%	3.6%	6.0%	1.4%	-0.2%	2.0%

* These categories should conform generally to the reporting in the NAIC statement Underwriting & Investment Exhibit Part 3 - Analysis of Expenses and to the Supplemental Health Care Exhibit, Lines 6.3 and 8.1. The sum of the expenses, commissions, contributions to reserves, investment income credit, taxes and the medical loss ratio should be 100%.

C. Average Rate Increase Components

The following items should reconcile to the Weighted Average Percent Rate Increase for the year:

	Price	Utilization, Mix	Total
Inpatient	1.6%	0.9%	2.5%
Outpatient	1.2%	1.4%	2.6%
Physician	1.2%	2.2%	3.4%
Pharmacy	0.3%	0.8%	1.1%
NEW PBM Effect			-2.0%
Administrative Expense (Aggregated)			0.4%
Contribution to Reserves			0.3%
Taxes and Assessments			0.7%
Total			9.0%

Part 3. Retrospective Reconciliation of Experience with Filed Factors

Year	Filed Data ¹					PMPM Increase ²		Standard Plan PMPM ³		Standard Plan Increase ⁴		Approved		Loss Ratio ⁵	
	Member Months	Earned Premium	Incurred Claims Total	Premium PMPM	Claims PMPM	Premium	Claims	Premium	Claims	Premium	Claims	Trend Increase%	Contrib to Reserves%	Actual%	Filed%
2009	1,236,217	461,697	402,284	\$373.48	\$325.42			\$369.22	\$324.47			9.2%	1.4%	87.1%	87.2%
2010	1,518,990	591,801	510,687	\$389.60	\$336.20	4.3%	3.3%	\$384.94	\$340.56	4.3%	5.0%	8.7%	2.0%	86.3%	86.0%
2011	1,455,522	572,712	498,441	\$393.48	\$342.45	1.0%	1.9%	\$425.36	\$363.04	10.5%	6.6%	9.6%	2.3%	87.0%	86.8%

¹ Corresponds to historical Information data in Part 1 above

² Percent increase compared to prior year

³ For most commonly held plan of benefits in 2010 and for the same plan of benefits in 2011

⁴ Percent increase compared to prior year

⁵ Represents claims loss ratio, claims divided by premium, which differs from the Federal MLR calculation for potential rebate determination

Blue Cross & Blue Shield of Rhode Island
Group Rate Factor Filing of December 2012
Administrative Costs Request

1. The expenses provided below are presented consistent with the categorization required in the Underwriting and Investment Exhibit - Part 3 Analysis of Expenses in accordance with NAIC instructions. The 2011 Actuarial values shown below are incorporated in the analogous values reported for our Commercial segment in both our NAIC blank and on page 2 of this exhibit. Our Commercial line of business as reported in the annual statement consists of the Small Group and Large Group segments that are the subject of this rate filing as well as our Direct Pay line. Note that there are approximately two years of inflationary increases between 2011 Actual and 2013 Projected values. Our proposed retention charges are below our projected costs in recognition of our ongoing efforts to improve administrative efficiency.

	2011 Actual		2013 Projected		2013 Proposed ⁽¹⁾		% Change	
	Small Group	Large Group	Small Group	Large Group	Small Group	Large Group	Small Group	Large Group
Total Estimated Member Months	816,413	1,472,976	743,081	1,484,325	743,081	1,484,325	-9.0%	0.8%
Total Estimated Premiums (\$mpm)	\$411.53	\$395.83	\$494.94	\$449.78	\$494.94	\$449.78	20.3%	13.6%
Total General Administrative Expense (\$mpm)	\$54.20	\$44.74	\$50.27	\$35.68	\$45.11	\$36.63	-16.8%	-18.1%
Total Cost Containment Expense (\$mpm)	\$9.29	\$8.39	\$9.31	\$7.81	\$6.64	\$6.08	-28.5%	-27.6%
Total Other Claim Adjustment Expense (\$mpm)	\$17.12	\$17.82	\$13.50	\$13.47	\$10.85	\$12.33	-36.6%	-30.8%
Total Admin Expense (\$mpm)	\$80.62	\$70.96	\$73.07	\$56.96	\$62.60	\$55.04	-22.4%	-22.4%
Breakdown of General Administrative Expense (\$ pmpm)								
a. Payroll and benefits	\$25.10	\$18.42	\$19.92	\$12.77	\$17.88	\$13.11	-20.6%	-30.7%
b. Outsourced Services (EDP, claims etc.)	\$8.65	\$8.64	\$8.80	\$8.70	\$7.89	\$8.93	1.7%	0.7%
c. Auditing and consulting	\$3.73	\$3.16	\$3.49	\$2.79	\$3.13	\$2.86	-6.4%	-11.7%
d. Commissions	\$8.65	\$6.72	\$12.90	\$5.81	\$11.57	\$5.96	49.1%	-13.6%
e. Marketing and Advertising	\$0.65	\$0.55	\$0.38	\$0.29	\$0.34	\$0.29	-41.8%	-48.4%
f. Legal Expenses	\$0.44	\$0.36	\$0.37	\$0.29	\$0.34	\$0.30	-14.2%	-18.8%
g. Taxes, Licenses and Fees	\$8.88	\$8.61	\$8.69	\$8.02	\$7.80	\$8.23	-2.1%	-6.9%
h. Reimbursements by Uninsured Plans	(\$11.30)	(\$9.39)	(\$12.82)	(\$9.63)	(\$11.50)	(\$9.88)	13.4%	2.5%
i. Other Admin Expenses	\$9.40	\$7.67	\$8.54	\$6.65	\$7.66	\$6.83	-9.2%	-13.3%

⁽¹⁾ For comparison purposes 2013 proposed charges represent 1st Quarter 2013 rates.

Blue Cross & Blue Shield of Rhode Island
Group Rate Factor Filing of December 2012
Administrative Costs Request

2. The following table details actual calendar year 2007-2011 fully insured Commercial administrative costs. This is consistent with the annual statement filings to OHIC for administrative costs using the categories defined by NAIC financial statement and as allocated to Commercially insured business only.

Fully Insured Commercial Administrative Cost History (Comprehensive Column)					
	2007	2008	2009	2010	2011
Total Premiums	1,108,466,606	1,079,151,863	1,025,508,205	994,470,562	984,903,252
Total General Administrative Expense	100,746,665	121,463,184	132,106,574	133,474,919	121,420,201
General Admin Exp. Ratio	9.09%	11.26%	12.88%	13.42%	12.33%
Total Fully Insured Member Months	3,326,346	3,049,827	2,775,423	2,603,304	2,468,947
General Administrative Expense (\$pmpm)	\$30.29	\$39.83	\$47.60	\$51.27	\$49.18
Breakdown of General Administrative Expenses (\$ pmpm)					
a. Payroll and benefits	\$17.53	\$17.40	\$21.04	\$18.84	\$19.82
b. Outsourced Services (EDP, claims etc.)	\$9.28	\$8.93	\$8.62	\$12.13	\$10.75
c. Auditing and consulting	\$2.20	\$5.75	\$6.38	\$6.18	\$4.55
d. Commissions	\$5.49	\$6.06	\$6.78	\$6.96	\$7.21
e. Marketing and Advertising	\$0.81	\$0.99	\$0.89	\$0.72	\$0.76
f. Legal Expenses	\$1.02	\$0.33	\$0.25	\$0.32	\$0.40
g. Taxes, Licenses and Fees	\$0.10	\$3.68	\$7.49	\$7.79	\$8.28
h. Reimbursements by Uninsured Plans ⁽¹⁾	(\$11.59)	(\$12.49)	(\$10.76)	(\$11.78)	(\$11.59)
i. Other Admin Expenses	\$5.44	\$9.18	\$6.90	\$10.11	\$8.98
Cost Containment Expense	\$4.10	\$4.30	\$5.73	\$7.58	\$7.82
Other Claim Adjustment Expense	\$10.06	\$13.38	\$18.19	\$17.42	\$20.04
Total Self Insured Member Months for all affiliated companies doing business in RI	2,409,639	2,474,355	2,677,918	2,448,365	2,625,181

⁽¹⁾ Includes total reimbursements from uninsured plans, not just the portion allocated to general administrative expenses, therefore the breakdown of general expenses does not match the total listed above. The differential is the portion of self funded fees that are treated as a contra expense for cost containment and other claim adjustment expenses.



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Consulting Actuary

December 4, 2012

John J. Lynch, F.S.A., M.A.A.A.
Chief Actuary
Blue Cross Blue Shield of Rhode Island
500 Exchange Street
Providence, RI 02903

Via email to john.lynch@bcbsri.org

Re: Actuarial Review of Rating Factors Applicable to Small and Large Group Subscription Rate Renewals ("Group Rating Factor Filing")

Dear Mr. Lynch:

Blue Cross & Blue Shield of Rhode Island (BCBSRI) has asked Milliman to review the development of rating factors applicable to Small Group and Large Group renewals effective in 2013. These rating factors are intended to be filed for approval with the State of Rhode Island Office of the Health Insurance Commissioner (OHIC). The filing procedure has been in place in similar form for many years, though the current filing is being prepared specifically in accordance with instructions issued by the OHIC in a letter dated April 19, 2012 and supplemented with letters dated May 16, 2012 and August 27, 2012. The April letter sets out, among other things, what standards will be used by OHIC for review, what documents should be included in the filing and how public input and accessibility will be handled. The supplemental letters deal with trends and rate caps, respectively. The particular filing that is the subject of this review is an amendment / additional filing as described in paragraph 10 of the April letter.

We, the undersigned, are members of the American Academy of Actuaries and meet the Qualification Standards of the American Academy of Actuaries to render the actuarial opinions contained herein.

This review was performed for the specific purpose of assessing the reasonableness of the methods and assumptions used in the development of the rating factors contained in BCBSRI's filing. This report should not be used for any other purpose. This work product was prepared for BCBSRI for the purpose described herein and may not be appropriate to use for other purposes. Milliman does not intend to benefit and assumes no duty of liability to other parties who receive this work product. Any third party recipient of this work product who desires professional guidance should not rely upon Milliman's work product, but should engage qualified professionals for advice appropriate to its own specific needs. Any release of this report to a third party shall be in its entirety.

We have reviewed BCBSRI's development of required rating factors in the filing, and we have done our own testing as we deemed appropriate. In our opinion, the actuarial methods and assumptions used in BCBSRI's calculation of required rating factors are sound and result in factors that are reasonable and appropriate for producing group rates. We observe that BCBSRI is proposing to limit the provision developed for recoupment of administrative costs in its group rates. Further, BCBSRI is not proposing to include any provision for taxes, fees and assessments which will be required under the federal Affordable Care Act (ACA). Finally, BCBSRI is not requesting any additional risk charge to cover the cost of the revenue loss it may incur as a result of the OHIC rate cap. As a result of these three issues, the resulting rates may not produce adequate revenue to cover all of the costs identified in the development.

As part of this filing, BCBSRI has addressed the issue of "rate caps" imposed by OHIC and clarified in its letter of August 27, 2012. As described in that letter, the rate cap is not intended to require modification to the premium rates for any particular group, but is designed to drive the health plan to take other actions (provider contracting and administrative management are mentioned in the letter) if the health plan sees that the cap will be exceeded for the year.

The problem with the rate cap from an actuarial standpoint is that the rating factors are developed based on prior experience and assumptions about the future, notably increases in health care utilization and cost. When the rating factors are actually applied during the rating period, the resulting premium rates are based on later experience that reflects actual emerging increases in health care utilization and cost. When these emerging costs are greater than assumed, as appears to be the case with BCBSRI in 2012, the rate caps will be exceeded.

BCBSRI has addressed this issue in the current filing in two ways:

1. Increasing the trend assumption and including an additional experience adjustment for months not yet complete based on a review of recent experience, and
2. Suggesting that relatively minor deviations from the rate cap be allowed without penalty.

In our opinion, these adjustments are necessary and appropriate. We recommend that minor deviations be defined as +/-2%. In addition, depending on the magnitude of any lost revenue that might result from the rate cap, it is our opinion that it may be appropriate to include an additional risk charge in the rates to reflect the expected cost of the rate caps. BCBSRI has decided not to request such an additional charge at this time.

We would characterize the trend factors developed by BCBSRI for use in projecting claim costs as falling within the range of most likely anticipated outcomes, based on information provided to us and our own independent research and actuarial judgment at this time. We also find the trend factors to be within the range of trends observed and expected elsewhere in the industry.

We reviewed BCBSRI's development of required administrative costs, which is defined for purposes of the Group Rating Factor Filing to include the net of operating and related administrative expenses, Federal income tax, premium tax, various state mandated assessments, and investment income (credit). We found BCBSRI's development to be sound. We note that BCBSRI proposes to actually charge in its group renewals a lower amount.

We were also asked to comment on comparisons with expense charges filed in Rhode Island by United Healthcare of New England (United). In particular, United mentions in its filings that

certain external vendor and internal affiliate expenses are treated differently under GAAP accounting than under statutory accounting. For 2013, they note that GAAP is used. Further, in a footnote it is noted that claims include certain capitation payments and “other costs associated with affiliated agreements”. While we have no personal knowledge of United’s practices in this regard, we note that it is common in the industry for the total cost of payments for outsourced services to be included as claims, including portions that would be used for administrative expenses by the external vendor or internal affiliate. Since BCBSRI has no such arrangements, it would be appropriate to make an adjustment when comparing filed administrative expense charges between the two companies.

As part of the review of administrative costs, we considered the impact of taxes, fees and assessments which will be required under ACA. While one small element of these fees is already in effect, the more significant ones begin January 1, 2014, and are effective based on calendar year, not plan year. Therefore, groups renewing after January 1, 2013, will have a portion of their premiums extending into 2014 and thus subject to the additional taxes, fees and assessments. In our opinion, it is actuarially appropriate to include a charge for these fees on an estimated basis. While it is not universal, many other health plans are including these charges in 2013 rates, often increasing by renewal month. If these fees are not imposed in 2013 premium rates, they will have to be paid out of contingency reserves and recouped from future premiums, leading to larger rate increases than would otherwise be necessary. We have reviewed the development of the specific charges proposed by BCBSRI and find them to be within a reasonable range of estimates for these items. However, as noted elsewhere, BCBSRI is not including provision for these charges in this filing.

We believe the stated required reserve contribution factor to be consistent with industry practices and, under normal circumstances, we would find it to be within a reasonable range. However, given the Plan’s current reserve situation (at the extreme bottom for all Blue Cross Blue Shield Plans), we view the required reserve contribution as only being at the very low end of a reasonable range. In addition, due to potential shortfalls in the proposed administrative cost factors, the lack of any provision for ACA taxes, fees and assessments, and potential penalties that could be incurred under the OHIC rate cap, we believe the actual contribution to corporate reserves based on this filing will likely be less than the stated level requested in it. There is a material possibility of no contribution to corporate reserves at all. In addition, even with fully adequate rates in all lines of business, reserve contribution factors will likely need to be increased in the future in order for BCBSRI to achieve an appropriate corporate reserve target within a reasonable period of time.

We have reviewed, at a high level (that is, not in detail) BCBSRI’s forecast and resulting risk based capital ratio. We find the forecast to be reasonable, based on our review. We note that it is possible that BCBSRI could approach the monitoring threshold established by the Blue Cross Blue Shield Association in the absence of the requested increase in rating factors.

The following elements of the filing were also part of our review:

- Experience adjustment – we find the experience adjustment noted above to be reasonable and appropriate;
- Incurral factor – we find the incurral factor used to add unpaid claims to the underlying experience to be reasonable and appropriate; and
- Mandated benefits – we considered mandated benefits both at the state and federal levels. BCBSRI has confirmed that there have been no changes at the state level. At the federal level, the Women’s Preventive Health mandate is not

yet in the experience. BCBSRI has elected not to reflect this in the premium rate development, however. While this represents less than one half of one percent of premium, it is another reason to expect that the desired reserve contribution in this filing is unlikely to be achieved.

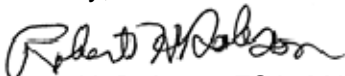
We also investigated the need for a conversion charge and understand that such a charge is no longer a part of the rate development.

Our review included the rating factors to be filed, but not the rating formula itself or its application. We assume the rating formula is appropriate and rating factors are appropriately applied.

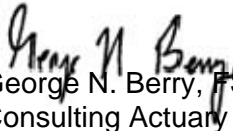
In performing this analysis, we relied on data and other information provided by BCBSRI. We have not audited or verified this data and other information. If the underlying data or information is inaccurate or incomplete, the results of our analysis may likewise be inaccurate or incomplete. We performed a limited review of the data used directly in our 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 our assignment.

It is certain that actual experience will not conform exactly to the assumptions and factors developed in the rate filing and reviewed by us. Since BCBSRI has elected to limit the rating factor for administrative costs, the likelihood of losses arising even with the rating factors requested in the filing is increased. Further, to the extent that emerging experience differs from the assumptions used in the filing, the actual required rates produced by them will also deviate from the projected required amounts produced using the rating factors in the filing. In accepting risks such as these, it is imperative that BCBSRI maintain adequate reserves for the protection of the Plan and its subscribers.

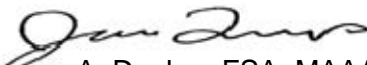
Sincerely,



Robert H. Dobson, FSA, MAAA
Consulting Actuary



George N. Berry, FSA, MAAA
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Blue Cross & Blue Shield of Rhode Island Inc.

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Blue Cross & Blue Shield of Rhode Island Inc.

Major Rating Factors

Strengths:

- Strong brand and wide provider network supporting a dominant market position
- Strong risk-adjusted capitalization supported by strong growth in surplus in 2011
- Strong liquidity profile, sustained by a liquid, high-quality investment portfolio

Weaknesses:

- Geographic market concentration in a single state
- Difficult regulatory environment as evidenced by inadequate premium rate approvals in the past

Operating Company Covered By This Report

Financial Strength Rating

Local Currency

BBB-/Positive/--

Rationale

The insurer financial strength rating on Blue Cross & Blue Shield of Rhode Island Inc. (BCBSRI) reflects BCBSRI's dominant market position, its strong liquidity profile, and its good risk-adjusted capitalization. Offsetting these strengths is BCBSRI's geographic market concentration in a difficult regulatory region.

In Standard & Poor's Ratings Services' view, BCBSRI's dominant market position in Rhode Island remains a strength for the rating. The company has a dominant share of the commercial health insurance market in that state, supported by strong brand equity and an extensive provider network. BCBSRI achieved and has maintained its leadership position through its competitive pricing, diversified product platform, focus on local communities, and high-quality customer service, as well as an extensive provider network. As of Dec. 31, 2011, the company had about 505,600 medical members under its commercial (group and individual) and government-sponsored (Medicare Advantage) plans.

BCBSRI's risk-adjusted capitalization is strong. In 2011, its statutory surplus saw an increase for the first time in four years. The company's capital had declined sharply in 2010 and 2009 due to negative net earnings and additional nonadmitted assets. However, with improved net retained earnings, the company added to its surplus in 2011. The company's capitalization also improved on a risk-adjusted basis, with capital being redundant at the 'AAA' level as per our 2011 pro forma insurance risk-based capital model, as compared with 'A' level redundancy at year-end 2010. We view capitalization to be critical for the company to improve credit quality. The stronger capital level, in our view, offsets any short-term volatility brought about possible inadequate premium rate approvals in the future.

The company's liquidity profile is strong, based on Standard & Poor's liquidity ratio of more than 200%. The company's investment portfolio comprises high quality, fairly liquid assets, which support the liquidity profile.

We consider BCBSRI's operating performance to be improving and supportive of the rating. We had previously lowered our ratings on BCBSRI due to its deteriorating financial profile, which stemmed from two years of negative retained earnings. The company's operating performance diminished in 2010 and 2009 because of inadequate

premium rate increases and higher-than-expected utilization in its commercial book of business. However, in 2011, the company saw a significant improvement in operating performance, primarily driven by the release of the premium deficiency reserve (PDR) and better medical cost trends. For full-year 2011, BCBSRI had pretax income (excluding realized capital gains and losses) of \$77 million, compared with a pretax loss of \$35 million in 2010 and pretax loss of \$101 million in 2009.

The company has already received adequate rate approvals for 2012, which indicates a likely stabilization of earnings in the near term. We expect the BCBSRI to report pretax return on revenue (ROR) of about 1.0%-1.5% in 2012 and about 2% in 2013. Our expectation for improvement in earnings takes into account higher-than-2011 cost trends, which are offset by adequate rate approvals and a reduction of administrative cost expenses.

The rating remains constrained by BCBSRI's geographic concentration in a single state, which exposes the company to adverse legislative, regulatory, economic, and competitive challenges. We believe it faces tough regulatory conditions in Rhode Island which, in 2008, changed its policy regarding proposed premium rate increases from a "file and use" approach to a "file and review" approach, further supporting our view of a strict regulatory environment.

Outlook

The outlook is positive based on improvements in BCBSRI's financial profile. Both operating performance and capitalization have improved in 2011, and we expect them to stabilize over 2012 and 2013. We could consider raising the rating over the next 24 months if BCBSRI maintains strong capitalization (capital being redundant at least at the 'AA' level as per our capital model) and stabilizes pretax operating ROR (excluding realized capital gains and losses) at about 1%-2%.

On the other hand, we could lower the ratings if BCBSRI's capital declines significantly and becomes deficient at the 'A' level and operating performance deteriorates, with ROR dropping below 1%.

Competitive Position: Leading Health Insurer In Rhode Island

BCBSRI has a good competitive position as the largest provider of health insurance in Rhode Island. The company has more than a 60% share of the state's health insurance market. BCBSRI achieved and maintained this position through its competitive pricing, diversified product platform, focus on local communities, and high-quality customer service as well as an extensive provider network. Further, BCBSRI has relationships with the vast majority of the physician providers and all of the hospitals in the state.

BCBSRI has a strong membership base, with 505,600 medical members in its commercial and government-sponsored programs. The company has an additional 93,500 members through the Blue Card and Blue CHIP programs. The company also has about 121,600 ancillary (dental) members and 9,000 Medicare Prescription Drug Plan members. Overall medical membership was in line with our expectations for 2011, but below 2010 levels. The year-over-year decline was due to a loss of a large group account in 2011. We don't expect this to have a material impact on the company's operations.

BCBSRI does face some competition (albeit somewhat fragmented), in particular from UnitedHealth Group Inc. and Tufts Health Plan of New England Inc. However, BCBSRI has remained its market leadership position through wide

local presence and strong community branding.

BCBSRI competes in all segments of the health insurance market. Its medical membership spreads over a diverse product platform: large and small group risk (43%), group nonrisk (43%), individual (8%), and government (6%) segments. Its products are well represented in all major employer groups in the state. The company markets its products to municipalities, large and small local groups, individuals, students, and senior citizens. An expanded network of brokers distributes BCBSRI's products, and third-party vendors provide prescription and vision care under various negotiated contracts. BCBSRI has relationships with the vast majority of the physician providers and all of the hospitals in the state.

BCBSRI's complete line of health insurance offerings enhances its competitive position. The company provides a wide variety of medical and dental benefits, managed care (HMO), point-of-service, and traditional indemnity type plans. It also offers medical and dental benefits to large groups that choose to self-fund all or a part of their benefits.

Tough rate regulations in Rhode Island somewhat constrain BCBSRI's business profile. Past decisions by the Office of the Health Insurance Commissioner (Rhode Island)--OHIC--to deny adequate premium rate increases has had a significant negative impact on the company's financial profile. BCBSRI's hospital provider concentration--Lifespan and Care New England Health System--also somewhat limits its business profile. These two hospital providers control more than 75% of the hospital beds in the state. Although we haven't seen any major contracting issues between BCBSRI and those providers, we do view this level of concentration as a limiting factor to the business profile.

Prospective

We expect that BCBSRI will maintain its position as the dominant health insurer in Rhode Island, and that its membership will likely remain flat in 2012--in the 505,000 to 506,000 range.

Management And Corporate Strategy: Improving Infrastructure To Compete More Efficiently

BCBSRI's management has maintained its market-leading position as a provider of affordable health care services in Rhode Island. The company has a history of good operating performance, as evidenced by its three-year (2006-2008) average ROR of 3.9%. However, in 2009 and 2010, a tough regulatory environment and overall weak economic conditions led to a sharp decline in earnings. The company has been able to turn around its operations in 2011, and we expect that the management will be able to execute on its medical and administrative cost improvement measures in the future.

Strategic positioning

BCBSRI is a not-for-profit health insurance company. A key facet of management's strategy is to position the company as a premium provider of health care by building a superior interactive relationship with its subscribers while maintaining strong pricing discipline. In addition, BCBSRI is focused on improving its provider contracting methodologies. Favorable discounts from hospitals and other health care entities have enabled BCBSRI to maintain competitive premium rates. The company also has been successful in switching to global fee contract agreements with a few community hospitals.

Operational effectiveness

We believe the company's senior management team has the necessary experience and expertise for this line of business. And the company usually performs according to its financial plans. Although there were occasions when the company did veer from its financial plans, these instances were caused by regulatory conditions. Rate regulations add some unpredictability to the company's operations.

Further, in line with its focus on improving operational management, BCBSRI is undertaking a major investment in technology to replace its information technology (IT) systems. The company's primary strategic objectives are to achieve cost efficiency and to enhance the servicing capabilities it needs to compete effectively with larger national health care companies. The new system should enable BCBSRI to support advanced integrated health management, reduce administrative costs, and improve process efficiencies. The company has contracted with a third-party vendor that has implemented this system for other major health insurers and Blue Cross and Blue Shield plans.

BCBSRI also implemented a patient-centered medical home model in 2010. Even though the project is still in its nascent stage, we view this strategic initiative favorably because patient-centered medical homes could potentially strengthen BCBSRI's care delivery systems and have a longer-term affect on reducing cost trends.

Financial management

BCBSRI maintains a high-quality balance sheet. It has no intangibles or long-term debt except for a commercial mortgage on its corporate headquarters. Management focuses on pricing its business rationally, underwriting its business conservatively, and improving its overall operating efficiencies. Management is also pursuing an expense control strategy that emphasizes greater technological efficiencies in order to help the company improve operating performance, remain price competitive, and enhance services for its stakeholders.

Governance

BCBSRI has an independent board of directors. The board is involved in developing goals and strategies for the company. We didn't note any material deficiencies in the company's audit controls.

The company has seen a couple of major changes in its senior management. The former CEO, James Purcell, retired in 2011, and the board hired Peter Andruszkiewicz as the new CEO after a nationwide search. Mr. Andruszkiewicz has significant experience in health insurance, and mostly recently was president of Kaiser Health Plan of Georgia. BCBSRI's previous CFO resigned earlier this year, and the board hired Mr. Michael Hudson as the new CFO. Mr. Hudson was most recently CFO at Health Plan Holdings in Tampa, Fla. Before that, he held senior management positions at Aetna and Cigna.

We will pay close attention to management's ability, under new CEO and CFO leadership, to continue to improve the company's near-term operational performance amid the currently tough regulatory environment in Rhode Island.

Enterprise Risk Management: Adequate For The Level Of Risk

We consider BCBSRI's enterprise risk management (ERM) to be adequate. The company's portfolio of health insurance products is not particularly complex. BCBSRI has good processes in place for identifying and mitigating risks. Both senior management and the board support the initiative. The head of the ERM team reports directly to the board's audit committee.

We expect that BCBSRI will continue to dedicate the resources necessary to promote ongoing integration of risk identification, risk management assessment, and management practices into its business process. Over the next few years, we believe the company will be able to further strengthen its ERM practices.

Accounting

In our view, BCBSRI maintains no unusual accounting practices. The company presents its financial statements on both a statutory and a generally accepted accounting principles (GAAP) basis. We adjusted the company's pretax income and ROR by excluding any realized investment gains or losses and other-than-temporary-impairments in order to focus on its operating earnings.

On statutory accounting basis, BCBSRI reports real estate (properties occupied by the company) as net of the outstanding mortgage loan and depreciation. As of Dec. 31, 2011, the company had a reported \$32.1 million--the total cost of construction (\$122.9 million) less the outstanding mortgage and depreciation on the property (\$90.8 million)--on its balance sheet.

Operating Performance: Earnings Stability Expected In The Near Term

We view BCBSRI's operating performance as improving and supportive of the current rating. The company had reported negative earnings in 2009 and 2010 due to higher-than-expected utilization rates coupled with inadequate premium rate increases. Its pretax income remained negative for two consecutive years: pretax loss (excluding realized investment gains or losses) of \$35 million in 2010 and pretax loss of \$101 million in 2009. The 2009 pretax loss included a premium deficiency reserve (PDR) of \$101 million, which was related to the inadequate rate increase received from the OHIC regarding commercial group and individual books of business. In 2010, the company released about \$9 million of the PDR and released the remaining (\$92 million) in 2012.

Operating performance improved in 2011, with the company reporting a pretax income (excluding realized gains and losses) of \$73 million, which translated to an ROR of 4.9%. The improvement in 2011 was primarily driven by improved results in the company's commercial business and the release of its PDR.

Excluding the impact of the PDR in 2011, the commercial segment reported better-than-2010 underwriting results, although the figure was still a loss due to the impact of previously approved inadequate rate increases. The Medicare Advantage (MA) segment in 2011 had positive underwriting income, which somewhat offset the weakness in the commercial results. Going forward, we expect adequate rates and improved administrative cost trends to help improve underwriting performance in the commercial book of business, while MA underwriting income will likely remain close to current levels.

Prospective

In 2012, we expect that the company's pretax ROR will be in the 1%-2% range. Further improvements in medical management and reduction in administrative costs will help maintain this positive trend in operating performance.

Investment And Liquidity: High-Quality Investment Portfolio

BCBSRI's liquidity profile is strong, underpinned by a liquid investment portfolio of high-quality fixed-income securities and cash investments. BCBSRI has an investment portfolio designed to match the short-term needs of its

liabilities and generate an adequate return in the long term to maximize policyholders' reserves. BCBSRI's liquidity ratio, as measured by Standard & Poor's liquidity model, was strong at more than 200% as of year-end 2010.

Majority of the company's assets are in fixed income securities. Equities, which currently make up about 8% of total invested assets, are in domestic and international equities. One key change in the portfolio's composition during 2010 was related to its exposure to equities. Due to the decline in its health risk-based capital (RBC) level, the company reduced its exposure to equities to 5% of total invested assets from 15%. Since its RBC level has increased in 2011, we expect BCBSRI will likely increase its equity exposure to closer to the 10% level.

Prospective

We expect BCBSRI's liquidity will remain strong, with a liquidity ratio of more than 200%, because of its high-quality investment portfolio.

Capitalization: Returning To Historical Strength

We believe that BCBSRI's risk-adjusted capitalization is strong and a key strength to the rating. In 2011, the company was able to stem the declining trend in capitalization it faced in 2010 and 2009. BCBSRI's statutory surplus improved almost 30% at year-end 2011 compared with year-end 2010.

Negative net income and higher levels of nonadmitted assets were the main reasons for the surplus decline in 2010 and 2009. The company's nonadmitted assets increased due to development of its new IT system and the deferred tax assets. In 2011, strong retained earnings helped strengthen in capitalization and add to its capital cushion.

In terms of risk-based capital, the company's capital adequacy also saw significant improvement. Based on our pro forma 2011 insurance capital model, capital is redundant at the 'AAA' level compared with only a 'A' level at year-end 2010. Also, in terms of the National Association of Insurance Commissioners' (NAIC) RBC, the company reported RBC (action company level) of 605% as of year-end 2011 compared with 454% at year-end 2010.

Prospective

We expect that BCBSRI will maintain a surplus that's redundant at least at the 'AA' confidence level.

Financial Flexibility: Sufficient Internal Accruals Offset Limited Capital Market Access

We believe that BCBSRI's financial flexibility is sufficient, supported by its relatively limited need for capital. In recent years, it has undertaken some capital expenditures, such as updating its IT system. We believe the company will likely be able to fund its capital expenditures through internal accruals without putting a strain on capital.

The company's access to external financing is limited because of its not-for-profit status and restricted access to the capital markets. Nevertheless, we believe the company will be able to meet any reasonable funding needs in the near term with its own resources.

Related Criteria And Research

- Research Update: Blue Cross & Blue Shield of Rhode Island Outlook Revised to Positive; 'BBB-' Rating Affirmed, April 2, 2012
- Criteria And Research Methodology For Assessing U.S. Insurers' Capital Adequacy Beyond The Financial Crisis, May 31, 2011
- Evaluating Insurers' Competitive Positions, April 22, 2009

Table 1

Blue Cross & Blue Shield Of Rhode Island Inc. Selected Statistics*					
(Mil. \$)	--Year ended Dec. 31--				
	2011	2010	2009	2008	2007
Total medical membership (000s) (consolidated)	505.6	514.2	535.2	579.1	591.2
Premiums earned	1,568.9	1,631.1	1,703.4	1,755.8	1,768.9
Net underwriting gain/loss	75.3	(60.6)	(126.2)	47.4	69.3
Net income/loss	72.7	(14.1)	(99.9)	43.5	61.3
Pretax return on revenue (excluding realized capital gains/losses) (%)	4.9	(2.1)	(5.9)	3.9	4.2
Pretax return on revenue (including realized capital gains/losses) (%)	4.6	(1.3)	(6.1)	2.8	4.3
Total assets	605.5	606.8	678.8	710.3	728.7
Total adjusted capital	323.4	249.0	298.7	412.3	428.8

*Based on statutory accounting.

Table 2

Blue Cross & Blue Shield Of Rhode Island Inc. Business Statistics					
	--Year ended Dec. 31--				
	2011	2010	2009	2008	2007
Number of members (000s)					
Fully insured risk membership	285.80	292.51	329.46	349.61	382.80
Nonrisk ASO/ASC membership	219.80	221.70	205.73	229.50	208.40
Total medical membership (consolidated)	505.60	514.21	535.19	579.11	591.20
Medicare Part D membership	8.99	9.08	8.92	8.10	9.46
BlueCard and National Par membership	93.50	96.90	93.03	99.20	98.51
Year-over-year change (%)					
Fully insured risk membership	(2.29)	(11.22)	(5.76)	(8.71)	(1.91)
Nonrisk ASO/ASC membership	(0.86)	7.76	(10.36)	10.12	2.88
Total medical membership (consolidated)	(1.67)	(3.92)	(7.58)	(2.07)	(0.27)
Medicare Part D membership	(0.94)	1.78	10.06	(14.35)	14.08
BlueCard and National Par membership	(3.51)	4.16	(5.90)	0.35	2.31
Premiums earned (mil.\$)	1,568.92	1,631.07	1,703.43	1,755.80	1,768.94
Year-over-year change (%)	(3.81)	(4.25)	(2.98)	(0.74)	4.25

Table 3

Blue Cross & Blue Shield Of Rhode Island Inc. Operating Statistics*					
	--Year ended Dec. 31--				
(Mil. \$)	2011	2010	2009	2008	2007
Total revenue	1,570.60	1,656.50	1,728.40	1,778.20	1,774.50
Net underwriting gain or loss	75.30	(60.60)	(126.20)	47.40	69.30
Pretax income (excluding realized capital gains or losses)	77.00	(35.20)	(101.20)	69.80	74.90
Pretax income (including realized capital gains or losses)	72.70	(21.20)	(105.10)	50.20	75.60
Net income or loss	72.70	(14.10)	(99.90)	43.50	61.30
Pretax return on revenue (excluding realized capital gains or losses) (%)	4.90	(2.10)	(5.90)	3.90	4.20
Pretax return on revenue (including realized capital gains or losses) (%)	4.60	(1.30)	(6.10)	2.80	4.30
Medical loss ratio (%)	79.40	87.80	92.10	84.00	84.70
Expense ratio (%)	15.70	15.60	15.00	13.10	11.30

*Based on statutory accounting.

Table 4

Blue Cross & Blue Shield Of Rhode Island Inc. Investment Statistics*					
	--Year ended Dec. 31--				
(Mil. \$)	2011	2010	2009	2008	2007
Net investment income	15.00	15.70	20.60	24.70	25.10
Net realized capital gain	(4.30)	14.00	(3.90)	(19.60)	0.70
Net investment gain	10.70	29.70	16.70	5.10	25.80
Net investment yield excluding realized capital gains and losses (%)	3.40	3.30	3.90	4.30	4.40
Net investment yield including realized capital gains and losses (%)	2.40	6.30	3.10	0.90	4.50
Total invested assets excluding real estate	441.40	439.20	506.50	556.90	603.00
Total invested assets	473.50	470.50	537.40	589.50	622.70
Portfolio composition					
Cash and short-term investments (%)	3.20	1.70	2.70	3.40	4.10
Bonds (%)	71.90	86.40	76.30	80.10	81.30
Preferred stock (%)	0.10	0.10	0.00	0.10	0.10
Total common stock (%)	8.70	3.90	14.30	10.20	11.20
Unaffiliated common stock (%)	8.70	3.90	14.30	10.20	11.20
Mortgages (%)	0.00	0.00	0.00	0.00	0.00
Real estate (%)	6.80	6.70	5.70	5.50	3.20
Other (%)	9.30	1.30	1.00	0.70	0.10
Total invested assets (%)	100.00	100.00	100.00	100.00	100.00

*Based on statutory accounting.

Table 5

Blue Cross & Blue Shield Of Rhode Island Inc. Capitalization Statistics*					
	--Year ended Dec. 31--				
(Mil. \$)	2011	2010	2009	2008	2007
Total assets	605.5	606.8	678.8	710.3	728.7
Total liabilities	282.1	357.8	380.1	298	299.9
Total adjusted capital	323.4	249	298.7	412.3	428.8

Table 5

Blue Cross & Blue Shield Of Rhode Island Inc. Capitalization Statistics* (cont.)					
Total equity assets to capital§ (%)	22.8	20.1	36.1	22.6	21

*Based on statutory accounting. §Includes real estate holdings.

Table 6

Blue Cross & Blue Shield Of Rhode Island Inc. Liquidity Statistics*					
(Mil. \$)	--Year ended Dec. 31--				
	2011	2010	2009	2008	2007
Cash flow from operations	15.50	(37.00)	(12.40)	31.80	78.00
Cash and short-term investments	15.20	7.90	14.40	19.90	25.80
Total invested assets (excluding real estate/affiliated investments/other)	401.00	433.30	501.40	552.90	602.30
Unpaid claims liability	113.00	126.40	124.70	133.60	147.30
Quick liquidity ratio (%)	13.50	6.30	11.50	14.90	17.50

*Based on statutory accounting.

Ratings Detail (As Of May 2, 2012)

Operating Company Covered By This Report

Blue Cross & Blue Shield of Rhode Island Inc.

Financial Strength Rating

Local Currency

BBB-/Positive/--

Counterparty Credit Rating

Local Currency

BBB-/Positive/--

Domicile

Rhode Island

*Unless otherwise noted, all ratings in this report are global scale ratings. Standard & Poor's credit ratings on the global scale are comparable across countries. Standard & Poor's credit ratings on a national scale are relative to obligors or obligations within that specific country.

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SERFF Tracking #:

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State Tracking #:

Company Tracking #:

LGM-201212

State: Rhode Island

Filing Company:

Blue Cross & Blue Shield of Rhode Island

TOI/Sub-TOI: H15G Group Health - Hospital/Surgical/Medical Expense/H15G.002 Large Group Only

Product Name: Large Group Commercial Medical

Project Name/Number: Large Group Medical Rating Factors for 2013 Dec Filing/LGM-201212

Supporting Document Schedules

		Item Status:	Status Date:
Bypassed - Item:	A&H Experience		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Actuarial Certification - Life & A&H		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Actuarial Memorandum - A&H Rate Revision Filing		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Health Insurance Checklist		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Premium Rate Sheets - Life & A&H		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Rate Summary Worksheet		
Bypass Reason:	See rate/rule schedule documentation.		
		Item Status:	Status Date:
Bypassed - Item:	Consumer Disclosure Form		
Bypass Reason:	See rate/rule schedule documentation.		