REPORT OF MEDICAL LOSS RATIO
EXAMINATION
OF THE
HEALTH NET LIFE INSURANCE COMPANY
FOR THE
2017 MLR REPORTING YEAR

Filed on March 17, 2020

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Los Angeles, California
February 15, 2020

Honorable Ricardo Lara
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, a Medical Loss Ratio examination was made of the

Health Net Life Insurance Company

(hereinafter also referred to as the Company). The Company's statutory home office is located at 21281 Burbank Boulevard, Woodland Hills, California 91367. The primary location of the Company's books and records is at 7700 Forsyth Boulevard, Saint Luis, Missouri 63105.

SCOPE OF EXAMINATION

We have performed a Medical Loss Ratio (MLR) examination of the Company to determine compliance with California Insurance Code (CIC) Section 10112.25 related to minimum medical loss ratio requirements. CIC Section 10112.25 grants the Insurance Commissioner authority to adopt regulations to implement the medical loss ratio, as described under Section 2718 of the federal Public Health Service Act. Section 2718 of the Public Health Service Act authorizes the U.S. Code of Federal Regulations (CFR) Title 45 – Public Welfare Part 158 to be implemented. This examination covered the reporting period of January 1, 2015 through December 31, 2017, including 2015 and 2016 experience and claims run-out through March 31, 2018.

We performed procedures established by the U.S. Department of Health & Human Services (HHS) to examine the MLR Annual Reporting Form as completed by the

Company and submitted to HHS for the 2017 MLR reporting year, to ensure the validity of the underlying data, accuracy of the calculation, and accuracy and timeliness of the rebate payments made and reported in compliance with Title 45 CFR Part 158. Title 45 CFR §158.403(a)(2) permits HHS to accept the state's audit provided it, amongst other things, reports on the validity of the data regarding expenses and premiums that the issuer reported to the Secretary of HHS, including the appropriateness of the allocations of expenses used in such reporting and whether the activities associated with the issuer's reported expenditures for quality improving activities meet the definition of such activities. Title 45 CFR §158.403(a)(3) further permits HHS to accept the state's audit provided it also, amongst other things, reports on the accuracy of rebate calculations, and the timeliness and accuracy of rebate payments.

OWNERSHIP

The Company is a wholly-owned subsidiary of Health Net of California, Inc., which is owned by Health Net, LLC. The ultimate parent is Centene Corporation.

TERRITORY AND PLAN OF OPERATION

As of December 31, 2017, the Company was licensed to sell life and accident and health products in the District of Columbia and all states except Michigan and New York. The main line of business written is health insurance. The Company concentrates on the small group and individual market.

The Company offers preferred provider organization, point of service, exclusive provider organization, indemnity, dental, vision, Medicare supplement, Medicare Advantage preferred provider organization (PPO), behavioral health, and life insurance products including group and individual term life, accidental death and dismemberment, supplemental term life, and dependent term life. These products are marketed through sales employees and independent sales agents, with the exception of the dental and vision products, which are marketed via strategic relationships with

Dental Benefit Providers, Inc., a United Healthcare Company, and EyeMed Vision Care LLC.

In 2017, the Company wrote $1.37 billion of direct premiums. Of the direct premiums written, $889 million (65.0%) was written in California, $324 million (23.7%) in Oregon, $109 million (8.0%) in Arizona, and $46 million (3.3%) in the remaining states.

MEDICAL LOSS RATIO REPORTING FORM

Title 45 of the U.S. Code of Federal Regulations (CFR) §158.110(b) requires that a report for each Medical Loss Ratio (MLR) reporting year be submitted to the Secretary of the U.S. Department of Health and Human Services (HHS) by July 31st of the year following the end of a MLR reporting year, on a form and in the manner prescribed by the Secretary. Based on our review of the filing, the Company filed an acceptable form by July 31, 2018 for the 2017 reporting year, and complies with Title 45 CFR §158.110(b).

Title 45 CFR §158.210(a) requires that an issuer must provide a rebate to enrollees if the issuer has an MLR of less than 85% for the large group market segment. Title 45 CFR §158.210(b) and (c) require that an issuer must provide a rebate to enrollees if the issuer has an MLR of less than 80% for the small group, the individual, and the student health market segments.

The three-year adjusted, aggregated numerator and denominator, along with the resulting credibility-adjusted MLRs for 2017, are shown in the following tables. The tables show the difference between the amounts in the “As Recalculated” and “As Filed” rows, which reflect the net impact of the adjustments made due to the identified findings as a result of this examination. The recalculated MLRs did not result in the Company owing rebates.

Arizona - Individual

	Numerator	**Denominator**	**MLR**
As Filed	$254,961,348	$191,310,365	134.6%
As Recalculated	$254,961,348	$188,823,262	136.4%
Difference	$0	($2,487,103)	1.8%

Arizona – Small Group

	Numerator	Denominator	MLR
As Filed	$260,385,239	$294,212,407	89.1%
As Recalculated	$259,114,823	$298,247,035	87.5%
Difference	$(1,270,147)	($4,034,628)	(1.6%)

Arizona – Large Group

	Numerator	Denominator	MLR
As Filed	$91,158,253	$95,826,793	96.4%
As Recalculated	$90,603,050	$93,118,317	98.6%
Difference	($555,203)	($2,708,476)	2.2%

California - Individual

	Numerator	Denominator	MLR
As Filed	$729,372,278	$546,656,733	133.4%
As Recalculated	$726,515,137	$542,325,529	134.0%
Difference	($2,857,141)	($4,331,204)	0.5%

California – Small Group

	Numerator	Denominator	MLR
As Filed	$1,223,879,710	$1,400,921,254	87.4%
As Recalculated	$1,219,013,837	$1,387,811,559	87.8%
Difference	$(4,865,873)	($13,109,695)	0.5%

California – Large Group

	Numerator	Denominator	MLR
As Filed	$426,016,694	$474,629,991	89.8%
As Recalculated	$451,560,501	$477,982,944	94.5%
Difference	$25,543,808	$3,352,953	4.7%

California – Student Health

	Numerator	Denominator	MLR
As Filed	$90,372,394	$109,098,368	84.4%
As Recalculated	$89,963,950	$108,327,800	84.6%
Difference	($408,443)	($770,568)	0.2%

COMMENTS ON MEDICAL LOSS RATIO

Medical Loss Ratio Numerator

According to Title 45 of the U.S. Code of Federal Regulations (CFR) §158.221(b), the numerator of the Medical Loss Ratio (MLR) calculation is comprised of incurred claims, as defined in Title 45 CFR §158.140, plus expenditures for activities that improve health care quality, as defined in Title 45 CFR §158.150, and §158.151. We verified the data used to calculate the numerator.

Incurred claims:

During the examination, it was observed that the Company did not properly aggregate its 2017 California large group market incurred claims in Part 2, Line 2.1b, 3/31 Column. In 2017, the student health market incurred claim experience was removed from the California large group market twice in error. The error resulted in an understatement of the California large group market incurred claims by $27,673,943. Due to this reporting error, the Company was found noncompliant with Title 45 CFR §158.120(a) which requires, in part, that the experience of all policies be aggregated separately for each market. It is recommended that the Company implement procedures to properly identify and aggregate the experience of all policies issued during the reporting year to the appropriate market as required by Title 45 CFR §158.120(a).

It was also observed that the Company inadvertently included expenses classified as Quality Improvement Activities (QIA) in the incurred claims reported in the 2017 MLR Annual Reporting Forms, Part 2, Line 2.1b, 3/31 Column. Per the MLR Annual Reporting Form Filing Instructions, Line 2.1b should not include expenditures for QIA. QIA expenses should be reported in Lines 4.1 through 4.5 of Part 1 of the Medical Loss Ratio Annual Reporting Form (MLR Reporting Form). The error resulted in an overstatement of the Arizona small group and large group markets incurred claims by $187,423, and $50,266, respectively. Additionally, the California individual, small group, and large group markets incurred claims were overstated by $707,460, $1,575,739, and $1,120,430, respectively. It is recommended that the Company implement procedures to properly report incurred claims as prescribed by the MLR Annual Reporting Form Filing Instructions, Part 2, Line 2.1b, 3/31 Column.

It was also observed that the Company inadvertently overstated incurred claims reported in the MLR Reporting Forms, Part 2, Line 2.1b by the amount of pharmacy rebates received. The error resulted in an overstatement of the incurred claims reported for the Arizona small group and large group markets by $973,844 and $457,499, respectively. Additionally, the California individual, small group, large group, and student health markets incurred claims were overstated by $2,149,681, $3,290,134, $1,009,705, and $408,443, respectively. Additionally, it was observed that the Company inadvertently underreported the Arizona small group and large group markets healthcare receivables by the provider receivable amounts of $105,856 and $47,478, respectively. Due to these reporting error, the Company was found noncompliant with Title 45 CFR §158.140(b)(1)(i), which requires, in part, that prescription drug rebates received by the issuer be treated as an adjustment that must be deducted from incurred claims. It is recommended that the Company implement procedures to ensure future compliance with Title 45 CFR §158.140(b)(1)(i).

It was observed that the Company improperly included prior years (2015 and 2016) pharmacy claims adjustments in the California individual and small group, and the Arizona large group incurred claims reported in Part 2, Line 2.1b, 3/31 Column of the MLR Reporting Form. A similar reporting error was observed with the Arizona small group incurred claims, where the Company included prior years (2013, 2014, 2015 and 2016) pharmacy claims adjustments. Reporting prior year incurred claim adjustments in the MLR reporting year is not in compliance with the MLR Annual Reporting Form Filing Instructions, Part 2, Line 2.1b, 3/31 Column, which provides, in part, that Line 2.1b, 3/31 Column only includes claims incurred during the MLR reporting year. This reporting error had a zero-net effect on the California individual and small group, and the Arizona large group three-year aggregate denominator. However, the reporting error resulted in an overstatement of the Arizona small group pharmacy claims reported in Line 2.1b, 3/31 Column by $15,571. Of this amount $12,277 was due to 2015 and 2016 adjustments and the remaining $3,294 was due to 2013 and 2014 adjustments. 2015 and 2016 incurred claims adjustments should be made to the PY2 and PY1 columns, respectively of Part 3 of the MLR Reporting Form. 2013 and 2014 adjustments should not be included in the 2017 MLR Reporting Form. It is recommended that the Company implement procedures to properly report incurred claims in accordance with the MLR Annual Reporting Form Filing Instructions, Part 2, Line 2.1b, 3/31 Column.

Activities that improve health care quality:

In the U.S. Department of Health and Human Services (HHS) Notice of Benefit and Payment for the 2019 Final Rule, the Center for Medicare and Medicaid Services (CMS) amended Title 45 CFR §158.221 by adding paragraph (b)(8), which provides issuer with the option to report Healthcare Quality Improvement Activities (QIA) as a flat rate of 0.8 percent of earned premiums beginning with the 2017 MLR reporting year, rather than reporting their actual expenses. Issuers that choose this method of reporting QIA must use this method for three consecutive MLR reporting years and for all of their individual, small group and large group markets; and all affiliated issuers must choose the same reporting method. For the 2017 MLR Annual Reporting, the Company elected to utilize the standard QIA reporting option offered by CMS. Compliance with the requirements under Title 45 CFR §158.221(b)(8) were reviewed. Based on the review, the Company appropriately reported QIA, and no adjustments to the MLR numerators were recommended.

Based on the review of the various components of the MLR numerator, as noted above, the California individual, small group, and large group markets were adjusted by ($2,857,141), $(4,865,873), and $25,543,808, respectively. The Arizona small group and large group markets were adjusted by ($1,270,417), and ($555,203), respectively. The student health market was adjusted by ($408,443).

Medical Loss Ratio Denominator

According to Title 45 CFR §158.221(c), the denominator of the MLR calculation is comprised of premium revenue, as defined in Title 45 CFR §158.130, minus federal and state taxes, and licensing and regulatory fees, as described in Title 45 CFR §158.161(a), and §158.162(a)(1) and (b)(1). We verified the data used to calculate the denominator.

Earned premiums:

During the examination, the Company discovered an error in the reporting of the large group and student health markets earned premium. In the Medical Loss Ratio Annual Reporting Form (MLR Form), the Company reported student health market earned premium of $43,051,185 for the 2017 reporting year. When the actual earned premium data was pulled for the student health market, the total amount was $40,329,843, meaning that the reported earned premium was overstated by $2,721,342. Since the student health market allocation came from the large group market earned premium, this error also resulted in an understatement of the large group market earned premium by the same amount. Due to this reporting error, the Company was noncompliant with Title 45 CFR §158.120(a), which requires, in part, that the experience of all policies be aggregated separately for each market segment. It is recommended that the Company implement procedures to properly identify and aggregate the experience of all policies issued during the reporting year to the appropriate market, as required by Title 45 CFR §158.120(a).

It was also observed that the Company reported Experience Rating Refund (ERR) balances for the individual market segment in Lines 1.4a and 1.5 of the Premium section in Part 2 of the California and Arizona 2017 MLR Forms, 12/31 Column. However, the Company failed to report identical balances in Lines 2.8a and 2.9a of the Claim section in Part 2 of the MLR Forms as required by the MLR Annual Reporting Form Filing Instructions. It is recommended that the Company comply with Title 45 CFR §158.140(a)(5) and the MLR Annual Reporting Form Filing Instructions by implementing procedures to properly report ERR in both the Premium and the Claim sections in Part 2 of the MLR Annual Reporting Form, but to exclude ERR from written premiums.

Federal and state taxes, and licensing or regulatory fees:

During the 2017 Medical Loss Ratio (MLR) reporting year, the Company did not incur state premium taxes for the Arizona small group market segment. However, the Company incorrectly reported state premium taxes for the Arizona small group market in its 2017 Arizona Medical Loss Ratio Annual Reporting Form (MLR Form). This error resulted in the overstatement of the Arizona small group markets state premium taxes by $1,444,819. Due to this error, the Company was noncompliant with Title 45 CFR §158.120(a), which requires, in part, that the experience of all policies be aggregated separately for each market. It is recommended that the Company implement procedures to properly identify and aggregate the experience of all policies issued during the reporting year to the appropriate market as required by Title 45 CFR §158.120(a).

It was also observed that the Company inadvertently did not exclude federal income taxes on investment income and capital losses from the federal income tax amounts reported in the 2017 MLR Forms, Part 1, Line 3.1a, 3/31 Column. This is not in compliance with Title 45 CFR §158.162(a)(2), which prescribes, in part, that federal income taxes on investment income and capital losses are not taxes based on premium revenue, and thus should not be used to adjust premium revenue. This error resulted in an overstatement of the reported federal income taxes for the California small group, large group, and student health markets in the amounts of $424,469, $309,680, and $103,227, respectively. Conversely, the California individual and the Arizona small group and large group markets federal income tax benefits were understated by $178,854, $72,998, and $335,877, respectively. It is recommended that the Company implement procedures to properly report federal income taxes by excluding the federal income taxes on investment income and capital gains as prescribed by Title 45 CFR §158.162(a)(2).

The Company calculated and reported federal income taxes in the MLR Forms, Part 1, Line 3.1a, 3/31 Column by applying a marginal tax rate instead of using the effective tax rate. This method of calculating and reporting federal income taxes does not comply with the Medical Loss Ratio (MLR) Annual Reporting Form Filing Instructions, which indicate that issuers should report federal taxes and assessments incurred by the reporting issuer during the MLR reporting year. This reporting error resulted in the following adjustments to the federal income taxes for the 2015-2017 MLR reporting years:

Arizona – FIT Adjustments

MLR Reporting Year	Individual	Small Group	Large Group
2015	$762,974	$1,897,392	$1,707,726
2016	$2,636,942	($7,467,659)	$391,800
2017	($125,442)	$3,437,949	$472,815

California – FIT Adjustments

MLR Reporting Year	Individual	Small Group	Large Group	Student Health
2015	($300,935)	($1,711,085)	$131,385	($98,549)
2016	($2,139,981)	$8,859,143	($852,645)	($1,187,126)
2017	$3,750,339	($1,226,239)	($1,697,168)	($1,002,423)

It is recommended that the Company implement procedures to properly report federal income taxes in accordance with the MLR Annual Reporting Form Filing Instructions, Part 1, Line 3.1a, 3/31 Column.

It was also observed that the Company calculated and reported state premium taxes in the MLR Forms, Part 1, Line 3.2a, 3/31 Column by multiplying the 3/31 premiums by the corresponding state premium tax rate. Calculating state premium taxes based on the 3/31 premiums does not properly reflect the actual premium tax expense for the year and is not consistent with the MLR Annual Reporting Form Filing Instructions. The Instructions prescribed issuers to report state insurance, premium, and other taxes incurred by the reporting issuer during the MLR reporting year. This reporting error resulted in the following adjustments to the state premium taxes for the 2015-2017 MLR reporting years:

Arizona – Premium Tax Adjustments

MLR Reporting Year	Individual	Small Group	Large Group
2015	($1,163,070)	($1,374,703)	($315,572)
2016	254,226	$2,289,034	($38,877)
2017	121,443	($1,444,820)	$154,697

California – Premium Tax Adjustments

MLR Reporting Year	Individual	Small Group	Large Group	Student Health
2015	$256,036	$226,593	($233,576)	($16,693)
2016	$2,586,891	$7,385,752	$2,330,073	$477,244
2017	0	0	0	0

It is recommended that the Company implement procedures to properly calculate and report state premium taxes in accordance with the MLR Annual Reporting Form Filing Instructions, Part 1, Line 3.2a, 3/31 Column.

Based on the review of the various components of the MLR denominator, as noted above, the California individual, small group, and large group markets were adjusted by ($4,331,204), ($13,109,695), and $3,352,953, respectively. The Arizona individual, small group and large group markets were adjusted by ($2,487,103), $4,034.628, and ($2,708,476), respectively. The student health market was adjusted by ($770,568).

Credibility Adjustment

According to Title 45 CFR §158.232, the credibility adjustment is the product of the base credibility factor multiplied by the deductible factor. The experience for the California individual, small group, and large group market segments were fully credible; therefore, no base credibility factors were calculated for these segments. The experience for the student health and the Arizona individual, small group, and large group market segments was partially-credible, and a credibility factor of 1.6%, 1.4%, 0.6%, and 1.3%, respectively, were calculated in accordance with Title 45 CFR §158.232.

All market segments for both California and Arizona did not report an average deductible factor; therefore, a deductible factor of 1 was assigned in accordance with Title 45 CFR §158.232(c). Based on the review, the Company appropriately calculated the credibility adjustments.

Credibility Adjusted Medical Loss Ratio

According to Title 45 CFR §158.221(a), the calculation of MLR is the ratio of the numerator to the denominator, subject to the applicable credibility adjustment, if any. Based on our review, it appears that the Company appropriately calculated the MLRs for each market segment.

REBATE NOTICE

According to Title 45 of the U.S. Code of Federal Regulations (CFR) §158.250(a) and (b), a notice of rebate is required when the Medial Loss Ratios do not exceed the minimum percentage. Based on the review, the Company's medical loss ratios exceeded the minimum percentage for all market segments, and no rebates were issued.

REBATE PAYMENTS ON SOLVENCY

According to Title 45 of the U.S. Code of Federal Regulations (CFR) §158.270(a), rebate payments having any adverse impact to the Company's Risk-Based Capital (RBC) level requires notification by the California Department of Insurance to the Secretary of the U.S. Department of Health & Human Services (HHS). Based on the review, the Company's MLRs exceeded the minimum percentage for all market segments, and no rebates were issued; therefore, there was no impact on the RBC level that would warrant notification to the Secretary of HHS.

ACCOUNTS AND RECORDS

The examination team experienced difficulties in obtaining supporting documentation for the information reported by the Company in its filed 2017 Medical Loss Ratio Annual Reporting Forms (MLR Form). This included routine requests for conformation on information, account reconciliations, and detailed supporting reports. It is recommended that the Company maintain adequate documentation to support all MLR Form balances. The documentation should be prepared in sufficient detail to allow for a full and complete audit trail from the MLR Forms to the individual records.

SUMMARY OF RECOMMENDATIONS

Current Report of Examination

Incurred claims (Page 5); Earned premiums (Page 8); and Federal and state taxes, and licensing or regulatory fees (Page 8) – It is recommended that the Company implement procedures to properly identify and aggregate the experience of all policies issued during the reporting year to the appropriate market as required by the Title 45 U.S. of the Code of Federal Regulations (CFR) §158.120(a).

Incurred claims (Page 5) – It is recommended that the Company implement procedures to properly report incurred claims by excluding any Quality Improvement Activities (QIA) in Part 2, Line 2.1b, 3/31 Column as prescribed by the Medical Loss Ratio (MLR) Annual Reporting Form Filing Instructions.

Incurred claims (Page 6) – It is recommended that the Company implement procedures to properly exclude prescription rebates received from incurred claims as required by Title 45 CFR §158.140(b)(1)(i).

Incurred claims (Page 6) – It is recommended that the Company implement procedures to properly report only claims incurred during the MLR reporting year in Part 2, Line 2.1b, 3/31 Column of the MLR Reporting Form as prescribed by the MLR Annual Reporting Form Filing Instructions.

Earned premiums (Page 8) – It is recommended that the Company comply with Title 45 CFR §158.140(a)(5) and the MLR Annual Reporting Form Filing Instructions by implementing procedures to properly report Experience Rating Refunds (ERR) in both the Premium and the Claim sections in Part 2 of the MLR Reporting Form, but to exclude experience rating refunds from written premiums.

Federal and state taxes, and licensing or regulatory fees (Page 8) – It is recommended that the Company implement procedures to properly report federal income taxes by excluding the federal income taxes on investment income and capital gains as prescribe by Title 45 CFR §158.162(a)(2).

Federal and state taxes, and licensing or regulatory fees (Page 9) – It is recommended that the Company implement procedures to properly report federal income taxes in accordance with the MLR Annual Reporting Form Filing Instructions, Part 1, Line 3.1a, 3/31 Column.

Federal and state taxes, and licensing or regulatory fees (Page 10) – It is recommended that the Company implement procedures to properly calculate and report state premium taxes in accordance with the MLR Annual Reporting Form Filing Instructions, Part 1, Line 3.2a, 3/31 Column.

Accounts and Records (Page 12) – It is recommended that the Company maintain adequate documentation to support all Medical Loss Ratio (MLR) Annual Reporting Form accounts. The documentation should be prepared in sufficient detail as to allow for a full and complete audit trail from the MLR Forms to the individual records.

Previous Report of Examination

Medical Loss Ratio Reporting Form (Page 6) – It was recommended that the Company adopt and implement procedures to ensure that all market classification determinations are in compliance with Title 45 CFR §158.220 and comply with the definitions contained within section 2791 of the PHS Act and the applicable requirements of Title 45 CFR §158 and associated technical guidance. It was also recommended that the Company implement procedures for determining group size. Proper determination of the group size and market classification was confirmed during the current examination of the Company, therefore the Company complied with Title 45 CFR §158.220.

ACKNOWLEDGMENT

The courtesy and cooperation extended by the Company's officers and parent company's employees during the course of this examination are hereby acknowledged.

Respectfully submitted,

/S/

Cuauhtémoc Beltran, CFE
Examiner-In-Charge
Department of Insurance
State of California

/S/

Sayaka Dillon, CFE
Senior Insurance Examiner, Supervisor
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