

REPORT OF MEDICAL LOSS RATIO EXAMINATION  
OF  
BLUE SHIELD LIFE AND HEALTH INSURANCE COMPANY  
AS OF  
DECEMBER 31, 2015

Filed June 30, 2017

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San Francisco, California  
May 25, 2017

Honorable Dave Jones  
Insurance Commissioner  
California Department of Insurance  
Sacramento, California

Dear Commissioner:

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

**BLUE SHIELD LIFE AND HEALTH INSURANCE COMPANY**

(hereinafter also referred to as the Company) at its home office located at 50 Beale Street, San Francisco, California 94105.

**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 granted 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 (PHSA). Section 2718 of the federal PHSA authorized the U.S. Code of Federal Regulation (CFR) Title 45 – Public Welfare Part 158 to be implemented. This examination covered the reporting period from January 1, 2012 through December 31, 2015.

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 2012, 2013, 2014, and 2015 MLR reporting years, 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) permitted HHS to accept the State's audit provided it, among 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 permitted HHS to accept the State's audit provided it, among other things, reported on the accuracy of rebate calculations and the timeliness and accuracy of rebate payments.

### OWNERSHIP

The Company is a wholly-owned subsidiary of California Physicians' Service (d.b.a. Blue Shield of California), an independent organization licensed by Blue Cross Blue Shield Association to offer certain products and services under the Blue Shield brand.

### TERRITORY AND PLAN OF OPERATION

The Company is licensed and operates exclusively in California. It writes ordinary life, group life; and group and other accident and health insurance. Direct premiums written in 2015 by line were as follows: Ordinary and group life combined were \$8,963,808 (0.7%); group accident and health was \$1,055,102,737 (83.2%); and other accident and health was \$204,088,727(16.1%).

The Company has no direct employees. Employees of Blue Shield of California (BSC), the Company's parent, manage the affairs of the Company. The Company markets through independent agents and brokers, and directly through the distribution system of BSC. Accident and health products offered by the Company included Preferred Provider Organization (PPO) health plans for individuals, and for small, midsize and large employer groups; as well as vision, dental, and stop-loss coverage during the examination period.

Effective January 1, 2014, the Company opted out of its participation in the Covered California Health Exchange, which was created to assist citizens and legal residents with applying for marketplace coverage in order to comply with the federal Patient Protection and Affordable Care Act and Health Care and Education Reconciliation Act of 2010, (collectively, "Health Care Reform"). As a result, the Company's non-grandfathered individual and small group medical plans were replaced by Health Care Reform compliant plans offered by its parent, BSC, or other health insurers. Effective December 1, 2015, the Company ceased to offer small group PPO health plans, which used to be the Company's largest membership base.

#### 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). For reporting years 2011, 2012, and 2013, the reports must be submitted to the HHS by June 1st of the year following the end of an MLR reporting year, on a form and in the manner prescribed by the HHS. Beginning with the 2014 MLR reporting year, the report for each MLR reporting year must be submitted to HHS by July 31st of the year following the end of an MLR reporting year, on a form and in the manner prescribed by HHS.

Based on our review of the filing, the Company filed an acceptable form by July 26, 2016 for the 2015 reporting year and is in compliance 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 a MLR of less than 85% for the large group market. 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 individual market and small group market. The Company's MLR and rebate calculations from the 2015 MLR Annual Reporting

Form, Part 4, for California are as follows:

MLR Components	Individual	Small Group	Large Group	Notes
Adjusted Incurred Claims	\$879,265,646	\$2,648,575,899	\$543,854,563	
Plus: Quality Improvement Expenses	\$11,509,493	\$25,310,252	\$5,217,826	
Less: Federal Risk Adjustment program charges payable to HHS	\$0	\$0	\$0	
MLR Numerator	\$890,775,139	\$2,673,866,151	\$549,072,389	(1)
Premium Earned	\$1,081,455,151	\$3,495,555,020	\$680,481,230	
Less: Federal & State Taxes and Licensing or Regulatory	\$20,275,937	\$211,638,893	\$40,570,394	
MLR Denominator	\$1,061,179,214	\$3,283,916,127	\$639,910,836	(2)
Preliminary MLR Before Credibility Adjustment	83.9%	81.4%	85.8%	
Credibility Adjustment	0.0%	0.0%	0.0%	(3)
Credibility-Adjusted MLR	83.9%	81.4%	85.8%	(4)
MLR Standard	80.0%	80.0%	85.0%	
Rebate Amount	\$0	\$0	\$0	(5)

Based on our examination, the Company did not owe any rebates for the MLR Reporting Year 2015 in any of the markets. However, the Company owed rebates for MLR Reporting Year 2012 for the individual and large group markets.

#### COMMENTS ON MEDICAL LOSS RATIO CALCULATION

##### (1) Medical Loss Ratio Numerator

According to the U.S. Code of Federal Regulations (CFR), Title 45, §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 Title 45 CFR §158.151. We reviewed and verified the data used to calculate the adjusted incurred claims. Based on our review, the Company included appropriate adjusted incurred claims and health care quality improvement expenses in the MLR numerator.

## (2) Medical Loss Ratio Denominator

According to Title 45 CFR §158.221(c), the denominator of the MLR calculation is comprised of issuer's premium revenue, as defined in Title 45 CFR §158.130, excluding federal and state taxes, and licensing and regulatory fees, described in Title 45 CFR §158.161(a), and Title 45 CFR §158.162(a)(1) and (b)(1) and after accounting for payments or receipts related to risk adjustment, risk corridors, and reinsurance, described in Title 45 CFR §158.130(b)(5). We reviewed and verified the data used to calculate the premium revenue. Based on our review, the Company included appropriate premiums earned in the MLR denominator.

We reviewed the reasonableness and appropriateness of the federal and state taxes, and regulatory fees including the appropriateness of allocations and the definition of such activities. Based on our review, the Company's allocation methodology and federal and state taxes, and regulatory fees reported in the MLR denominator are reasonable and conform to the regulations.

## (3) 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. For MLR Reporting year 2015, the Company's life years for each of its individual, small, and large group markets were over 75,000. Therefore, the Company was considered "fully credible" and is held to the normal MLR standards. Based on our review, it is appropriate that the Company did not apply any credibility adjustments.

#### (4) 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 MLR for each market segment.

#### (5) Rebate Amount

According to Title 45 CFR §158.240, an issuer must provide a rebate if the issuer's MLR does not meet or exceed the minimum percentage required for the applicable market segment. Based on our review, the Company's MLR for the reporting years 2013, 2014, and 2015 exceeded the minimum percentage for individual, small, and large market segments. However, the Company's 2012 MLR ratio for the individual market segment was 78%, which was lower than the minimum required percentage of 80%. For this market segment the Company rebated \$13,327,883 to 226,034 policyholders/subscribers. The Company's 2012 MLR for the large group market segment was 84.8%, which was lower than the minimum required percentage of 85%. For this market segment, the Company rebated \$399,933 to 43,889 policyholders/subscribers for the 2012 MLR year.

#### NOTICE OF REBATE

According to Title 45 of the U.S. Code of Federal Regulations §158.250(a) and (b), a notice of rebate is required when the medical loss ratios do not exceed the minimum percentage. Based on our review, the Company's medical loss ratios for MLR reporting year 2015 exceeded the minimum percentage for the individual, small, and large market segments and no rebates were issued.

As discussed above, the Company issued rebates for MLR reporting year 2012 for the individual and large group market segment. Based on our review, the Company issued rebate notices appropriately and timely.

#### REBATE PAYMENTS ON SOLVENCY

According to Title 45 of the U.S. Code of Federal Regulations §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 our review, the Company's MLRs exceeded the minimum percentage for the individual, small, and large group market segments for MLR reporting year 2015, and no rebates were issued. Therefore, there was no adverse impact on the RBC level that would warrant notification to the Secretary of HHS. The rebates issued by the Company for the individual and large group market segment for MLR reporting year 2012 did not have an adverse impact on the RBC level that would warrant notification to the Secretary of HHS.

#### SUMMARY OF COMMENTS AND RECOMMENDATIONS

##### Current Report of Examination

None.

##### Previous Report of Examination

Medical Loss Ratio Numerator (Page 3): It was recommended that the Company make appropriate changes to its claims system so that it is able to produce claim reports by lines of business. The Company has complied with this recommendation.

ACKNOWLEDGMENT

Acknowledgment is made of the cooperation and assistance extended by the Company's officers and employees during the course of this examination.

Respectfully submitted,

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