STATE OF CALIFORNIA Dave Jones, *Insurance Commissioner*

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Aetna Life Insurance Company Rate Filing
Small Group Major Medical Policies
State Tracking Number: HAO-2012-0010
Effective date: April 1, 2012
Determination by the Department of Insurance: Unreasonable

The California Department of Insurance finds the rate increases submitted by Aetna Life Insurance Company in its filing HAO-2012-0010 to be unreasonable.

Filed Rate Increase

The effective date for these increases is April 1, 2012 and they apply to the totality of the company's small group PPO policies in California. As of December 31, 2011 there were approximately 73,000 members in these policies.

The two year cumulative rate increase for these Aetna small group policies is on average 30.3% excluding benefit changes.

Aetna files rate increases each quarter for these small group policies. The average quarterly rate increase effective April 1, 2012 is 1.8% excluding benefit changes, which in conjunction with earlier increases is a cumulative average increase of 8% over 12 months. The maximum 12-month increase for any rating cell is 21.4%.

The rate filing was submitted to the Department on January 23, 2012. The filing is posted on the California Department of Insurance website for the public to view.
http://www.insurance.ca.gov/0250-insurers/HlthRateFilings/upload/AetnaHAO0010.pdf

Summary of Department's Findings

Pursuant to Guidance 1163:2, the Department considered a number of factors in making the determination that the rate increase is unreasonable. http://www.insurance.ca.gov/0250-insurers/0500-legal-info/0200-regulations/HealthGuidance/Guidance11632.cfm

Aetna assumes in its rate filing a 12.2 per cent core medical trend increase, which the Department finds unreasonable. Aetna's core medical trend increase assumption is significantly higher than what recent experience demonstrates and there is insufficient evidence to support this projected cost increase assumption. This finding alone is sufficient for the Department to determine that the rate increase is unreasonable. In addition, Aetna's substantial return on equity, level of payments of dividends to its parent company, comparison of Aetna's assumed medical cost trend to national medical inflation rates, and the cumulative impact of this rate hike when coupled with additional rate hikes over the last two years, all further substantiate the unreasonableness of this rate increase.

The Department's findings are discussed in more detail in the following:

<u>The assumptions on which the rate increase is based are not supported by substantial evidence</u>

Aetna's filed rates were based upon a projected pricing trend of 12.2% (leveraged). In its evaluation of the rate increases, the Department objected to the trend assumptions used by the company. The medical trend assumption of 12.2% is significantly higher than what Aetna's recent experience demonstrates and the utilization component of the trend (2.4%) has not been adjusted to reflect the significant reductions in plan benefit that will be implemented as of April 1, 2012.

The Department developed its own projection of pricing trend, based upon actual patterns of cost increases and known factors that are expected to increase costs more than indicated by recent experience. The Department's projected trend assumption is 7.7% (leveraged).

Using the 7.7% pricing trend in the rate development model provided by Aetna, the Department calculated an average rate increase of 0.0% excluding design changes. We estimate that the Department's calculated rate increases would, if implemented, result in an underwriting gain over the period April 1, 2012 through March 31, 2013, albeit less than that estimated if the filed rates were implemented.

Based on this information, Aetna's trend assumption and proposed rate increase are both unreasonable.

<u>Aetna's rate of return, evaluated on a return-on-equity basis, for the prior three years and anticipated rate of return for the following year, provide further support for finding this rate increase unreasonable</u>

Aetna Life Insurance Company's rate of return on equity for the prior three years climbed from 20.5 per cent to 27.7 per cent and is projected to be over 30 per cent for 2012. This is particularly noteworthy as compared to the overall economy whose growth has been sluggish at best. Aetna's substantial return on equity is further evidence of the unreasonableness of this filed rate increase.

Company-wide *($ in millions)*	**2009** **Actual**	**2010** **Actual**	**2011** **Actual**	**2012** **Forecast**
Statutory Net Income (post-tax)	882.6	1,193.1	1,001.2	1,163.0
Statutory Capital & Surplus	4,858.2	4,182.4	3,047.1	3,726.0
Avg. Statutory Capital & Surplus	4,300.9	4,520.3	3,614.2	3,386.6
Return on Equity (Statutory Capital)	20.5%	26.4%	27.7%	30.8%

Comparison with Medical CPI

From February 2011 to February 2102 (the most recent period available), the rate of medical cost inflation as reported by the U.S. Bureau of Labor Statistics Consumer Price Index (CPI) for All Urban Consumers Medical Care Services Cost Inflation Index was 3.4%. From February 2010 to February 2012, the rate of medical cost inflation per the same source was 6.5%

Aetna's filed 12-month rate changes average 8.0% (excluding benefit changes) for rates effective April 1, 2012, and the average 24-month rate changes average 30.3%, both of which are substantially in excess of the CPI Medical Services Cost Inflation Indices.

Dividend History

The company filing this rate increase, Aetna Life Insurance Company, paid significant dividends to its parent company, Aetna Inc. This dividend history is further evidence of the profitability of the company and the unreasonableness of the filed rate increase:

Year	Dividend
2008	$675.4 million
2009	$147.7 million
2010	$1,891.5 million
2011	$1,775.0 million ($425.0 million declared but unpaid as of December 31, 2011)

Dividends paid to the parent were modest in 2009 when ALIC was accumulating most of its earnings. Examination of the balance sheet shows that ALIC's statutory capital and surplus rose during that period. ALIC's capital and surplus dropped in 2010 when the Company paid generous dividends to the parent as it drew from current- and prior-year accumulated net income.

The cumulative impact of the filed rate, combined with previous increases, also causes the rate to be unreasonable

The average 12-month increase resulting from the filed rates is 8.0% and the average 24-month increase is 30.3%. The rate increase for some policies is substantially higher. The cumulative impact of the filed rate is further evidence of its unreasonableness.

Conclusion

The Department requested that the rate filing be withdrawn in order to prevent a finding that the rate increase is unreasonable. Aetna has decided to go forward in implementing the rate increase deemed unreasonable by the Department of Insurance. The Insurance Commissioner does not have the authority to reject excessive or unreasonable rate increases.