

**Blue Cross and Blue Shield of North Carolina**

Durham, North Carolina

**Report on Medical Loss Ratio Examination**

As of December 31, 2011

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Raleigh, North Carolina  
September 16, 2014

Honorable Wayne Goodwin  
Insurance Commissioner  
North Carolina Department of Insurance  
Raleigh, North Carolina 27603

Dear Commissioner:

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

Blue Cross and Blue Shield of North Carolina

(hereinafter also referred to as the Company) at its home office located at 5901 Chapel Hill Road, Durham, North Carolina 27707.

### **SCOPE OF EXAMINATION**

We have performed a Medical Loss Ratio (MLR) limited scope examination of Blue Cross and Blue Shield of North Carolina for compliance as described under Section 2718 of the federal Public Health Service Act (PHSA). Section 2718 of the federal PHSA authorizes the U.S. Code of Federal Regulation (CFR) Title 45 – Public Welfare Part 158 to be implemented. This limited scope examination covers the twelve months ending December 31, 2011, plus the period through March 31, 2012, for runoff activity. As an additional resource, we relied on the guidance of National Association of Insurance Commissioners’ (NAIC) and U.S. Department of Health and Human Services’ (HHS) collaboration efforts which produced the MLR Examination Procedures Spreadsheet, MLR Examinations and MLR Supplement Report Language.

We examined the MLR Annual Reporting Form as completed by the Company and submitted to HHS for the 2011 MLR reporting year, to ensure the validity of the underlying data, accuracy of the rebate 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) permits HHS to accept the State's examination 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 examination 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 non-stock, nonprofit hospital and medical service corporation domiciled in the State of North Carolina and licensed under NCGS § 58-65. It was incorporated in 1968 and commenced business in the same year. The Company has four wholly owned subsidiaries, Saegis Benefits, LLC (Saegis) (renamed Mosaic Group Services, LLC (Mosaic) as of 8/31/2012), Corium, LLC (Corium), ACS Benefit Services, Inc. (ACS), and NobleHealth, Inc. (Noble). Saegis functions as an insurance agency selling third-party life and disability, death and dismemberment, and property and casualty products and is licensed as a third-party administrator. Corium owns, operates, and manages certain office buildings of the Company.

ACS provides self-funded plans with complete third-party administration services for group medical, dental and disability benefits. Noble participates in various other ventures.

### **TERRITORY AND PLAN OF OPERATION**

The Company is licensed and operates exclusively in the State of North Carolina. It holds the exclusive licenses to use the Blue Cross® and Blue Shield® names and service marks in North Carolina. It provides a comprehensive spectrum of health benefits products to customers primarily located in North Carolina and is authorized to write life and disability insurance. Direct premiums written in 2011 totaled \$4,986,633,034 of which over 77% is written in accident & health policies with the remainder consisting of Government Business, Other Business and Other Health as defined for 2011 MLR reporting.

### **MEDICAL LOSS RATIO REPORTING FORM**

Title 45 CFR §158.110(b) requires that a report for each MLR reporting year be submitted to the Secretary of HHS by June 1<sup>st</sup> 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, the Company filed an acceptable MLR Reporting Form by June 1, 2012 for the 2011 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) also require that an issuer must provide a rebate to enrollees if the issuer has an MLR of less than

80% for the small group and individual markets. Title 45 CFR §158.301 provides that a state may request a waiver from the standard 80% MLR requirement for the individual group market. North Carolina requested a waiver for 2011, 2012 and 2013 and was approved to use 75% for 2011 only. The Company's MLR and Rebate Calculations from the 2011 MLR Reporting Form, Part 5, are as follows:

<b>MLR Components</b>	<b>Individual</b>	<b>Small Group</b>	<b>Large Group</b>	<b>Notes</b>
Adjusted Incurred Claims	821,537,880	814,866,927	1,590,320,476	
Plus: Quality Improvement Expenses	7,788,515	6,169,724	11,554,318	
MLR Numerator	829,326,395	821,036,651	1,601,874,794	(1)
Premium Earned	1,009,717,321	998,157,795	1,832,145,915	
Less: Federal & State Taxes and Licensing or Regulatory Fees	(34,228,916)	(38,045,378)	(41,513,064)	
MLR Denominator	975,488,405	960,112,417	1,790,632,851	(2)
Preliminary MLR Before Credibility Adjustment	85.0%	85.5%	89.5%	
Credibility Adjustment	N/A	N/A	N/A	(3)
Credibility Adjusted MLR	85.0%	85.5%	89.5%	(4)
2011 Standard/Waived MLR	75.0%	80.0%	85.0%	
Rebate Amount	-	-	-	(5)

## **COMMENTS ON MEDICAL LOSS RATIO CALCULATION**

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

According to Title 45 CFR §158.221(b), the numerator of the 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. From the claims data requested, we were able to reconcile the totals reported by lines of business to the Company's claims system. We were able to verify the lines of business on a sample basis without exception.

We also examined the reasonableness of the health care quality improvement expenses and confirmed that the methodology used complied with the narrative provided within the MLR Part 4 – Allocation Methodology Report and it does conform to the definition of Healthcare Quality Expenses as defined in Title 45 CFR §158.150 and Title 45 CFR §158.151. Based on our examination, the Company's allocation methodology and health care quality improvement expenses reported in the MLR numerator were reasonable and conform to the regulations.

### **(2) Medical Loss Ratio Denominator**

According to Title 45 CFR §158.221(c), the denominator of MLR 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 Title 45 CFR §158.162(a)(1) and (b)(1). From the premium data requested, we were able to verify the data used to calculate the

premium revenue on a sample basis without exception. Based on our examination, the Company included appropriate premiums earned in the MLR denominator. We examined the reasonableness of the federal and state taxes, and the licensing and regulatory fees, including the appropriateness of allocations. The Company's allocation methodology, federal and state taxes, and licensing 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, if required. For individual, small group and large group business, the Company's experience is fully credible under the definition specified in Title 45 CFR §158.232, therefore no credibility adjustment was required for this year. The calculation of member months and life-years were examined without exception.

(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. As noted above, the Company has no credibility adjustment for the MLR segments. Additionally, based on a February 16, 2012 letter to HHS from the North Carolina Department of Insurance, HHS agreed to reduce the minimum loss ratio for the individual health insurance market from 80% to 75% for the 2011 year only. This had no impact for rebate determination because the MLR was in excess of the minimum. Based on examination, the Company appropriately calculated the MLR for each market segment.

#### (5) Rebate Amount Calculation and Distribution

According to Title 45 CFR §158.240, a rebate is required if an issuer's MLR is less than the minimum percentage. Based on examination, the Company's MLR exceeded the minimum percentage for the individual, small and large markets and, as such, no rebates were required to be paid by the Company.

#### **MEDICAL LOSS RATIO INFORMATION NOTICE**

According to Title 45 CFR §158.251(a), a one-time notice of the MLR process is required when the MLR exceeds the minimum standard. As noted, the Company's MLR exceeded the minimum percentage for the individual, small and large group markets. Based on our examination, the Company appropriately issued these MLR information notices. In future years, notifications are required only when rebates are paid to eligible insureds.

#### **SUMMARY OF FINDINGS AND RECOMMENDATIONS**

1. As part of our examination regarding the classification activities that improve health care quality, the NCDOI MLR review team was required to test that health care quality improvement expenses reported on the MLR form conform to the definition of health care quality improvement expenses in Title 45 CFR §158.150-151. In addition, health care quality improvement (QI) activities reported on the MLR form must be consistent with the activities described in Part 4 of the MLR form. Our examination did not identify any specific exception to these tests, however, we did note that policies and procedures had not been developed to provide guidance, define ownership, or convey documentation requirements for QI activities and expenses. This would include providing certainty regarding roles and responsibilities for identifying eligible QI programs, the level of documentation required and the appropriate

retention policy for MLR records. Effective formal policies and procedures are required to manage risk in an organization.

We recommend that the necessary departments meet and create MLR policies and procedures related to QI expenses included in the MLR calculation. It should be noted that this issue was identified by the NCDOI MLR review team during our testing, and it also was identified in an internal audit by BCBSNC Audit & Risk Management in 2013. Substantial progress has been made in complying with this recommendation for 2013 MLR reporting.

2. A substantial number of QI program managers and cost center contacts required additional training in understanding the rationale used to determine cost center QI versus non-QI Full Time Employee (FTE) time allocations in 2011. In addition, although program checklists are maintained by the Cost Accounting Department to support MLR compliance, these checklists did not include evidence of cost center manager review and approval and, in certain instances, were not satisfactorily completed.

We recommend that QI programs specified for MLR reporting include the rationale as to how and why the activity meets the QI definitions in the regulations in addition to how and when the program results will be measured and verified. The Cost Accounting Department should verify that checklists are fully completed by cost center personnel and contain evidence of the QI program owner and cost center approver. It again should be noted that this issue was identified by the NCDOI MLR review team during our testing, and it also was identified in an internal audit by BCBSNC Audit & Risk Management in 2013. Substantial progress has been made in complying with this recommendation for 2013 MLR reporting.

**ACKNOWLEDGEMENT**

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

Respectfully submitted,

Hasije P. Harris, CPA, CGMA  
MLR Section Manager  
Examiner-In-Charge  
Department of Insurance  
State of North Carolina

STATE OF NORTH CAROLINA  
COUNTY OF WAKE

Hasije Harris, MLR Section Manager, North Carolina Department of Insurance, states that this report on examination, subscribed by her, is true and correct to the best of her knowledge and belief.

Signature: \_\_\_\_\_ Date: \_\_\_\_\_

Sworn and subscribed before me this \_\_\_\_ day of \_\_\_\_\_, 2014.

Notary Public Signature: \_\_\_\_\_ Notary Public Seal:

**Blue Cross and Blue Shield of North Carolina**

Appendix A – Report Distribution

December 31, 2011

Mitchell W. Perry, Vice President, Financial Services & Treasurer  
5901 Chapel Hill Blvd  
Durham, NC 27707

Thomas R. Krebs, Director of Financial Reporting  
5901 Chapel Hill Blvd  
Durham, NC 27707

Frances Doyle, Manager, Financial Reporting  
5901 Chapel Hill Blvd  
Durham, NC 27707