Coventry Health Care of the Carolinas, Inc.

Morrisville, NC

Report on Medical Loss Ratio Examination

As of December 31, 2011, 2012 and 2013

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Honorable Wayne Goodwin
Commissioner of Insurance
State of North Carolina
Raleigh, North Carolina

Sir:

Pursuant to your instructions, the North Carolina Department of Insurance ("Department") conducted a medical loss ratio ("MLR") examination of Coventry Health Care of the Carolinas, Inc. ("Company") as of December 31, 2011, 2012 and 2013, including the period through March 31, 2014, for runoff activity. This is the Department's first MLR examination of the Company.

This examination was performed in accordance with examination standards established by the Department. The purpose of this examination was to examine the components of the MLR Annual Report Form as completed by the Company and submitted to the U.S. Department of Health and Human Services ("HHS") for the 2011, 2012 and 2013 MLR reporting years. The Department examined the components of the MLR Annual Report Form by utilizing the MLR Examination Procedures Spreadsheet developed by HHS in consultation with the National Association of Insurance Commissioners ("NAIC") which was in effect for the specified examination period. The findings and recommendations of our examination are based solely on the work performed and are provided in the Summary of Objectives, Findings and Recommendations beginning on page six (6).

Respectfully submitted,

Hasije P. Harris, CPA

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

August 5, 2016

STATE OF NORTH CAROLINA
COUNTY OF WAKE

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

Signature: Hasije P. Harris, CPA Date: 8-5-2016
Hasije Harris

Sworn and subscribed before me this 5th day of August, 2016.

Notary Public Signature: [illegible] Notary Public Seal:

Djidade B. Muhovi
NOTARY
My Comm. Exp.
9/5/2017
PUBLIC
WAKE COUNTY, N.C.

1. Company Background

The ("Company") was incorporated on September 1, 1995, under the laws of the State of North Carolina as a health maintenance organization ("HMO"). The Company commenced business on January 1, 1996 and was incorporated under the name of WellPath Community Health Plans, Inc., and experienced name changes, mergers and acquisitions since its incorporation. On May 7, 2013, Aetna completed its acquisition of the Company. The parent of the Company prior to May 2013 was Coventry Health Care, Inc. and the parent as of January 1, 2014 was Aetna Health Holding, LCC. Effective January 1, 2016, Coventry Health Care of the Carolinas has merged with Aetna Health Inc. (a Pennsylvania corporation) and is no longer a North Carolina domiciled entity.

The Company provides or arranges managed care for health insurance, self-funded health care benefit plans, individuals, and other entities as a liaison with health care providers (hospitals, doctors, etc.). The Company is licensed in North and South Carolina. The Company writes health insurance products, which include traditional gate-keeper HMO's, POS and Open Access plans. Services are typically provided under one-year contacts with employers and individuals, under which the Company insures the health benefits plans of employees who select Company coverage. The majority of the Company's business is written in North Carolina, with approximately 25% in South Carolina. The Company does participate in the federally facilitated Health Insurance Market Place Exchange ("Federal Exchange"). Open enrollment began October 1, 2013.

2. Scope of the Examination

The Department performed a limited scope examination on the components of the MLR Annual Report Form as completed by the Company and submitted to HHS for the 2011, 2012 and 2013 MLR reporting years, at the Company's main administrative offices located at 9881 Maryland Drive, Richmond, Virginia 23233. The Company's statutory home office is located at 2801 Slater Road, Suite 200, Morrisville, North Carolina 27560. The Department reviewed and tested, as deemed appropriate, the following items in accordance with 45 CFR Part 158: validity of the data regarding premiums, claims and expenses that the Company reported to HHS, including the propriety of the allocations of expenses used in such reporting, whether the activities associated with the Company's reported expenditures for quality improving activities meet the definition of such activities, the accuracy of rebate calculations, and the timeliness and accuracy of rebate payments as applicable. As the lead state, this examination covers the filings in the states of North Carolina and South Carolina. The Company's last statutory examination was as of December 31, 2013.

3. Summary of Examination Objectives, Findings and Recommendations

2011 MLR Components (NC)	Individual	Small Group	Large Group
Adjusted Incurred Claims	$ 25,941,120	$ 74,925,424	$ 47,624,038
Plus: Quality Improvement Expenses	$ 245,043	$ 281,408	$ 150,153
MLR Rebates Paid on 2011 or 2012 experience			
MLR Numerator	$ 26,186,163	$ 75,206,832	$ 47,774,191
Premium Earned	$ 38,121,463	$ 103,755,273	$ 67,923,741
Less: Federal & State Taxes and Licensing or Regulatory Fees	$ (1,963,074)	$ (7,829,006)	$ (6,512,523)
MLR Denominator	$ 36,158,389	$ 95,926,267	$ 61,411,218
Preliminary MLR	72.5%	78.4%	77.8%
Credibility Adjustment	2.5%	1.6%	2.5%
Credibility Adjusted MLR	75.0%	80.0%	80.3%
2011 Standard/Waived MLR	75%	80%	85%
Rebate Amount	-	-	$ 2,886,327

2012 MLR Components (NC)	Individual	Small Group	Large Group
Adjusted Incurred Claims	$ 57,884,429	$ 163,225,652	$ 106,458,297
Plus: Quality Improvement Expenses	$ 374,031	$ 533,319	$ 320,199
MLR Rebates Paid on 2011 or 2012 experience	$ -		$ 2,886,327
MLR Numerator	$ 58,258,460	$ 163,758,971	$ 109,664,823
Premium Earned	$ 77,326,818	$ 218,288,434	$ 144,159,008
Less: Federal & State Taxes and Licensing or Regulatory Fees	$ (1,881,984)	$ (14,204,654)	$ (11,410,852)
MLR Denominator	$ 75,444,834	$ 204,083,780	$ 132,748,156
Preliminary MLR	77.2%	80.2%	82.6%
Credibility Adjustment	1.7%	1.0%	1.4%
Credibility Adjusted MLR	78.9%	81.2%	84.0%
2012 Standard/Waived MLR	80%	80%	85%
Rebate Amount	$ 392,864	$ -	$ 713,369

2013 MLR Components (NC)	Individual	Small Group	Large Group
Adjusted Incurred Claims	$ 91,766,496	$ 247,488,205	$ 174,961,505
Plus: Quality Improvement Expenses	$ 383,946	$ 861,393	$ 574,097
MLR Rebates Paid on 2011 or 2012 experience	$ 392,864		$ 3,599,696
MLR Numerator	$ 92,543,306	$ 248,349,598	$ 179,135,298
Premium Earned	$ 121,974,231	$ 327,766,110	$ 226,745,162
Less: Federal & State Taxes and Licensing or Regulatory Fees	$ (3,357,948)	$ (18,156,238)	$ (13,509,829)
MLR Denominator	$ 118,616,283	$ 309,609,872	$ 213,235,333
Preliminary MLR	78.0%	80.2%	84.0%
Credibility Adjustment	0.9%	0.0%	1.1%
Credibility Adjusted MLR	78.9%	80.2%	85.1%
2013 Standard/Waived MLR	80%	80%	85%
Rebate Amount	$ 431,714	-	$ -

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2011 MLR Components (SC)	Individual	Small Group	Large Group
Adjusted Incurred Claims	$ 1,727,482	$ 25,675,730	$ 10,194,927
Plus: Quality Improvement Expenses	$ 12,451	$ 109,193	$ 31,975
MLR Rebates Paid on 2011 or 2012 experience			
MLR Numerator	$ 1,739,933	$ 25,784,923	$ 10,226,902
Premium Earned	$ 3,136,961	$ 36,092,917	$ 13,059,124
Less: Federal & State Taxes and Licensing or Regulatory Fees	$ (223,346)	$ (2,252,312)	$ (591,947)
MLR Denominator	$ 2,913,615	$ 33,840,605	$ 12,467,177
Preliminary MLR	59.7%	76.2%	82.0%
Credibility Adjustment	9.0%	2.6%	5.5%
Credibility Adjusted MLR	68.7%	78.8%	87.5%
2011 Standard/Waived MLR	80%	80%	85%
Rebate Amount	$ 329,238	$ 406,087	$ -

2012 MLR Components (SC)	Individual	Small Group	Large Group
Adjusted Incurred Claims	$ 6,454,769	$ 56,763,368	$ 34,643,673
Plus: Quality Improvement Expenses	$ 34,828	$ 202,901	$ 90,997
MLR Rebates Paid on 2011 or 2012 experience	$ 329,238	$ 406,087	
MLR Numerator	$ 6,818,835	$ 57,372,356	$ 34,734,670
Premium Earned	$ 8,917,925	$ 77,340,672	$ 40,761,818
Less: Federal & State Taxes and Licensing or Regulatory Fees	$ (13,598)	$ (4,553,672)	$ (1,014,612)
MLR Denominator	$ 8,904,327	$ 72,787,000	$ 39,747,206
Preliminary MLR	76.6%	78.8%	87.4%
Credibility Adjustment	4.8%	1.9%	2.6%
Credibility Adjusted MLR	81.4%	80.7%	90.0%
2012 Standard/Waived MLR	80%	80%	85%
Rebate Amount	$ -	$ -	$ -

2013 MLR Components (SC)	Individual	Small Group	Large Group
Adjusted Incurred Claims	$ 13,712,629	$ 86,132,759	$ 61,900,055
Plus: Quality Improvement Expenses	$ 37,491	$ 328,494	$ 168,947
MLR Rebates Paid on 2011 or 2012 experience	$ 329,238	$ 406,087	
MLR Numerator	$ 14,079,358	$ 86,867,340	$ 62,069,002
Premium Earned	$ 19,681,245	$ 119,450,162	$ 70,063,686
Less: Federal & State Taxes and Licensing or Regulatory Fees	$ (480,673)	$ (5,724,963)	$ (1,099,315)
MLR Denominator	$ 19,200,572	$ 113,725,199	$ 68,964,371
Preliminary MLR	73.3%	76.4%	90.0%
Credibility Adjustment	0.0%	0.0%	2.2%
Credibility Adjusted MLR	73.3%	76.4%	92.2%
2013 Standard/Waived MLR	80%	80%	85%
Rebate Amount	$ 689,848	$ 1,473,775	$ -

a) **Reporting**

Test the accuracy of MLR annual reporting and reconcile with the Supplemental Health Care Exhibit.

Findings:

The Company filed an MLR Annual Report Form by June 1, 2012 for the 2011 reporting year, June 1, 2013 for the 2012 reporting year and July 31, 2014 for the 2013 reporting year in compliance with Title 45 CFR §158.110(b). The due date for the MLR Annual Report Form was permanently extended for all reporting organizations as of the 2013 reporting year. We reviewed and reconciled the NAIC's SCHE to the CMS' MLR Rebate Form for each year respectfully; no exceptions were noted. Center for Consumer Information and Insurance Oversight (CCIIO) Technical Guidance (CCIIO 2015-0001) was issued on May 27, 2015, and focused on the impact of broker fees and commissions on the reporting of earned premium in the MLR Annual Report Form. Within this technical guidance, CCIIO established seven specific conditions which must be met in order for an issuer to exclude broker fees and commissions from premiums for MLR reporting purposes. CCIIO 2015-0001 was meant to clarify MLR regulations; hence we informed the Company and reviewed their process. Based upon our review of the Company's procedures and accounting related to these conditions and additional documentation provided to us by the Company, we did not identify any exceptions to the conditions specified in CCIIO 2015-0001.

On January 1, 2014, the Company became subject to an annual fee under section 9010 of the Affordable Care Act (ACA). This annual fee is allocated to individual health insurers based on the ratio of the amount of an entity's net premiums written during the preceding calendar year. A health insurance entity's portion of the annual fee becomes payable once the entity provides health insurance for a United States health risk for each calendar year beginning on or after January 1, 2014. As of December 31, 2013, the Company had written health insurance subject to the ACA assessment and transferred $4,625,000 to its parent in 2014 for its portion of the 2013 annual assessment. The Company continued to write health insurance business subject to the ACA assessment in 2014. (Notes to Statutory Financial Statements, item (15) - Subsequent Events).

Recommendation:

None

b) **Validation of the Consistency of Included/Excluded Data**

Test the accuracy of state and market classifications, the accuracy of reporting under the dual contracts option, and the reasonableness and accuracy of expense allocations.

Findings:

The Company complied with all state and market classification requirements for the 2011, 2012 and 2013 reporting years and is in compliance with Title 45 CFR §158.110, §158.120 and §158.220. The Company elected to report dual option contracts written as an in-network issuer, therefore, no activity was required to be reported as defined under Title 45 CFR §158.120(c)(2).

The Company was a dual state writer (North Carolina and South Carolina) during the examination years. There is no business in government programs or plans and the Company does not write Mini-Med or Expatriate plans. There are no material amounts in other health business lines.

For expense purposes, Title 45 CFR §158.170 uses language such as "Allocation to each category should be based on a generally accepted accounting method that is expected to yield the most accurate results" and "Any basis adopted to apportion expenses must be that which is expected to yield the most accurate results and may result from special studies of employee activities, salary ratios, premium ratios or similar analyses." Coventry's QIA allocation model was developed to allocate costs to legal entities and market segments. These expenses are allocated based upon adjusted member months. While the QI activities are tracked and recorded across all market segments, the level of intensity of the services vary by member segment. For example, a Medicare member utilizes more services than an individual member due to the age of the population. In order to recognize this, weights were applied to member months to properly model different intensity levels by market segment. These allocations are performed after Coventry has calculated the total value of QI expenses. Once the model is complete, allocated QI expenses are distributed to Data Reporting to prepare the SCHE and HHS MLR reporting form. The examiners noted that the by-line reconciliation for non-claims costs for Lines 5.1 and 5.2 reflected differences between SHCE and MLR reporting. Although these non-claims costs do not impact the MLR ratio and would not impact the payments of refunds, there exists the need for statistical accuracy of reporting for comparison purposes among health insurers.

Recommendation:

We recommend that the Company revise their MLR policy to complete a by-line reconciliation for all statistical reporting, regardless of whether the data is included in the Company's MLR calculation. This will ensure accurate data for the comprehensive database developed by HHS to enable the agency to arrive at informed decisions regarding ACA policy. Also, a by-line reconciliation will support the verification that expenses reported for MLR purposes have been accurate for 2011-2013.

c) **Validation of Data Utilized in Calculating MLR**

Test the accuracy of reporting for new business, the accuracy of reporting of reinsurance and the accuracy of life-years. Findings:

The Company accurately reported new business in 2011, 2012 and 2013 in compliance with Title 45 CFR §158.121. The "block of business" test for reinsurance was not applicable for this Company in 2011, 2012 and 2013. Life-years were reported accurately as required in compliance with Title 45 CFR §158.230(b).

Recommendation:

None

d) **Calculation of the Medical Loss Ratio Numerator**

Test the accuracy of reporting of claims, the classification of activities that improve health care quality, and the aggregation of data in the MLR numerator.

Findings:

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 reviewed third-party vendor payments as specified in Title 45 CFR §158.160 and verified that no non-claim payments were recorded in direct losses.

We were 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. Health care quality improvement (QI) activities reported on the MLR Form must be consistent with the activities described in the MLR Annual Reporting Form. The Company's policy "Minimum Medical Loss Ratio Description of the Quality Improvement (QI) Expenses Process" indicates a robust system with necessary internal control and our testing concluded that there was no selection of expenses not qualified for QI. The Company's process flow for QI expenses documents how these expenses, once identified, are calculated, tracked and then finally allocated. This is done by year by each legal entity and each market.

2012 and 2013 were the only year that the aggregation of data in the MLR numerator was required to be verified based upon the demands of the formula. No errors were identified.

Recommendation:

None.

e) **Calculation of the Medical Loss Ratio Denominator**

Test the accuracy of reporting of earned premiums, taxes and regulatory fees and the aggregation of data in the MLR denominator.

Findings:

According to Title 45 CFR §158.221(c), the denominator of an issuer's MLR must equal the issuer's premium revenue, as defined in Title 45 CFR §158.130, minus the issuer's 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 Company's 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 federal and state taxes and licensing and regulatory fees, including the propriety 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.

2012 and 2013 were the only year that the aggregation of data in the MLR denominator was required to be verified based upon the demands of the formula. No errors were identified.

Recommendation:

None

f) **Validation of the MLR Calculation**

Test the accuracy of the MLR standard, the MLR calculation, the aggregation of member-months and life-years, the accuracy of the base credibility factor, the accuracy of the deductible factor and the accuracy of the credibility adjustment.

Findings:

The Company used the appropriate 2011, 2012, 2013 MLR standards for individual, small and large group markets as defined in Title 45 CFR §158.210 and Title 45 CFR §158.211. The preliminary MLR calculations and the credibility-adjusted MLR calculations were done in accordance with Title 45 CFR §158.221. Verification of the aggregation of life years was completed for reporting years 2012 and 2013. No exceptions were noted. No aggregation is applicable to the 2011 year.

The base credibility factors are correct and the deductibility factors are acceptable as specified by Title 45 CFR §158.230, Title 45 CFR §158.231, and Title 45 CFR §158.232(a) and (c). This resulted in an accurate base credibility factor calculation and an accurate final credibility adjustment for each market.

Recommendation:

None

g) **Rebate Notice and Payment**

Test the accuracy of rebate payments, accuracy of the distribution of the de minimis rebates, and compliance with rebates disbursement requirements.

Findings:

In accordance with Title 45 CFR §158.240, §158.241, §158.242, we verified that the Company paid rebates in North Carolina and South Carolina markets when required. Rebate payments were paid by check in all three MLR years for both North Carolina and South Carolina, although the Company did issue premium credits in lieu of checks in 2011 and 2012, if requested. The premium credit option was discontinued in 2013. Premium credits for 2011 and 2012 were tested to ensure that the credits were applied before new cash payment of premium was collected for renewal policies for the policyholder. The handling of de minimis rebates revealed no issues as per Title 45 CFR §158.243. Rebate payments were calculated by multiplying the difference between the Minimum Loss Ratio and the Actual Loss Ratio by the MLR earned premiums in each of the states and market groups. Rebate payments were made in the form of premium credits or checks issued on or before the due date for each of the years (2011, 2012 and 2013) respectfully. We selected rebate checks to verify that rebate mailings were done timely.

In accordance with Title 45 CFR §158.244, §158.250 and §158.251, we verified that rebate notices were issued in the prescribed form and contained all required disclosures to the subscribers in the large group market. Notification of the rebate was sent to the employees of each group by the Company.

A Notice of MLR Information when the MLR standard is met or exceeded was provided to policyholders or subscribers in groups for the 2011 reporting year as required by Title 45 CFR §158.251. The Company was required to provide this one-time notice, including the language required by Title 45 CFR §158.251(a)(4), with the first health plan document that the Company sent to enrollees on or after July 1, 2012 if an enrollee did not receive a rebate for the 2011 year. There were no outstanding checks applicable to rebates paid in 2011, 2012 and 2013.

Recommendation:

None

Appendix A – Report Distribution

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