

Executive Summary

Overview:

The *University of California Health Insurance Company* (UC) has considered entering the *Small Business Health Options* (SHOP) Exchange for Small Group Insurance, *Covered California Individual Market* (Covered CA) Exchange for Individual Insurance, and/or extending renewal offers to the rest of the small-large groups in 2016. Thus, the following scenarios must be considered:

- 1) Early renewals to a part of the small-large groups, no SHOP, and Covered CA
- 2) Early renewals to all the small-large groups, no SHOP, and Covered CA
- 3) Early renewals to a part of the small-large groups, SHOP, and Covered CA
- 4) Early renewals to all the small-large groups, SHOP, and Covered CA

Furthermore, we have the following assumption:

- 1) UC is not the only health insurance provider in the market, and if they do not provide competitive rates, clients will look for alternatives.
- 2) Early Renewal offers are at small-group in-force premium rates with 1% increase
- 3) Once early renewal has been completed, groups cannot back out of the rate for 2016
- 4) Other companies will offer SHOP and Individual Coverage through the market exchange as an option for 2016.
- 5) Claims from current small-large groups will be used to determine risk for 2016 and 2017.

The goal is to provide basic analysis and information to allow decision makers to understand the underlying dynamics and potential actions that could be taken to address any concerns that exist across different parts of the data.

Method:

We first calculated the baseline for our average membership for 2015 to 2017 with the provided lapse rates. We used the assumptions and analysis provided by *West Coast Limited Liability* in order to create rate, expense, and profit projections for 2016 and 2017 to calculate profit margin and evaluate the best scenario for UC to implement. For Individual Insurance, we looked at Covered CA and UC projections, calculating rates for the latter using the age curve per age group. Our final analysis consisted of merging the group and individual projections to give us better understanding of the overall effect of incorporating the two new lines of business. We were able to observe the impact of each scenario, and consider expansion by increasing the number of new members on the tables.

Observation:

When considering the potential financial effects of entering the Covered CA Exchange for Individual Insurance, we must take into account that while there is a high projected profit margin (12.49%, 13.51% for Covered California and 15.01% and 16.37% for UC Rates for 2016 and

2017 respectively), the lapse rate is significantly higher than that of the Large Group. Furthermore, because Individual and Small Group Insurance are much more regulated than Large Group Insurance, expenses and premiums are more subject to changes. Based on current projections, it does not readily appear that the Individual Insurance lines match the capital requirements of 15-20% that come with expanding UC's business lines.

When examining the membership sensitivity to premium change, we observed that most large group members are not as price elastic to that of small and individual groups. When comparing two individual rates, Covered California and UC, we found the UC rate to be more profitable due to higher average membership, higher premiums, and lower expenses.

Conclusion/Recommendations:

We concluded that Scenario 4, renewals to 55% of small-large groups, expansion into the SHOP and Covered CA Exchange using UC rates, is the most favorable scenario. Based on UC's 2015 projections pre-small group expansion, UC had projected a 6.6% and 7.5% profit margin for 2016 and 2017 respectively. Scenario 4 is projected to yield a profit margin of 7.81% and 9.34%, respectively and is also projected to have a higher average membership than the pre-small group expansion for 2017, meeting Management's goals of returning to a 10% profit margin, growing membership, and gaining experience in new markets, with their foray into the SHOP and Covered CA Exchange. Scenario 4 comes close to Management's goal of meeting or exceeding a 10% profit margin, with a profit margin of 9.33%. Our projected profit trend is promising, and appears to be slated to meet Management's goals beyond 2017.

We recommend the expansion of the large business group because it is more profitable, stable, and has a lower lapse rate compared to that of the new market. The projections for Small Group and Individual Insurance show promising profit margins. However, these markets are volatile and more subject to Government Regulation, causing freezes to rates and fluctuations in expenses. Because UC has never offered plans in the SHOP and Covered CA exchange, it is important that a foray into those exchanges is handled carefully, requiring at least a 5% increase in membership and looking at the results. Some factors to consider in any decisions include adverse selection, cost variability and frequency, additional capital requirement, government regulation.