Minimum Solvency Criteria Discussion

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DEPARTMENT OF Managed Health Care

Financial Reserves

- Reserve Requirements
- Tangible Net Equity (TNE)
- Working Capital
- Cash-to-Claims
- Claims Timeliness
- Approvable methodology for estimation of Incurred But Not Reported (IBNR)

What is TNE?

- “Net Equity” means the excess of total assets over total liabilities.

- “TNE” is net equity reduced by the value of intangible assets (i.e. goodwill, organizational or start-up costs, etc.)

TNE Requirement

Maintain a positive TNE at all times, for the reporting period.

TNE Calculation

Net Equity
+ Subordinated Debt
- Unsecured Receivables from officers, directors and affiliates
- Intangibles

= TNE

Health Plan Minimum TNE

Required TNE is calculated using one of the following three methods. The method that results in the highest dollar amount equals the plan's required TNE.

	Full Service Plans	Specialized Plans
1	Minimum TNE Requirement: $1,000,000	Minimum TNE Requirement: $50,000
2	Based on a percentage of revenue	Based on a percentage of revenue
3	Based on a percentage of healthcare expenditures	Based on a percentage of healthcare expenditures
	Required TNE – Greater of 1, 2 or 3	**Required TNE – Greater of 1, 2 or 3**

Risk-Based Capital

- What is it?
  - It is a capital adequacy standard related to risk that provides a safety net and provides regulatory authority for timely action
- How does it compare to TNE?
  - It uses a hypothetical minimum capital level based upon which is compared to the actual Net Equity of the company
  - It establishes automatic authority for regulatory action

Regulatory Triggers Comparison

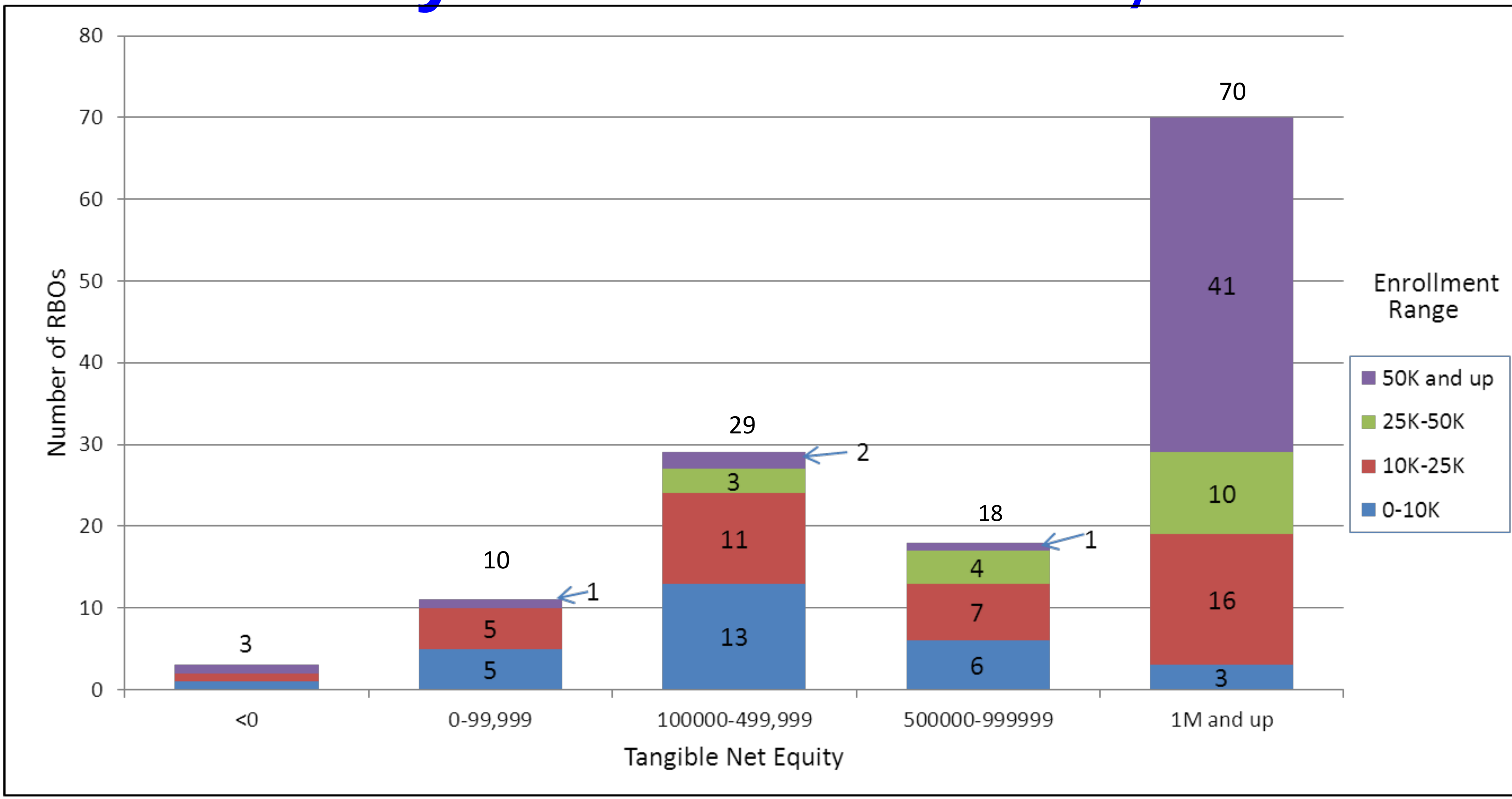
- For year end 2011, estimated RBC averaged slightly higher than required TNE (~10%)
- 23 of 55 plans measured minimum TNE higher than RBC
- The largest 11 plans by revenue had higher RBC vs TNE

Regulator Action Levels
RBC vs TNE

	RBC	TNE
• > 200% of Net Equity	No Action	
• 150 – 200% of Net Equity	Company Action	
• 100 – 150% of Net Equity	Regulatory Action	
• 130% of TNE		Monthly Reporting
• 70 – 100% of Net Equity	Authorized Control	Mandatory Action
• 0 – 70% of Net Equity	Mandatory Control	

* Excludes 1 outlier plan in each category

TNE of the RBOs that filed Financial Surveys at December 31, 2012



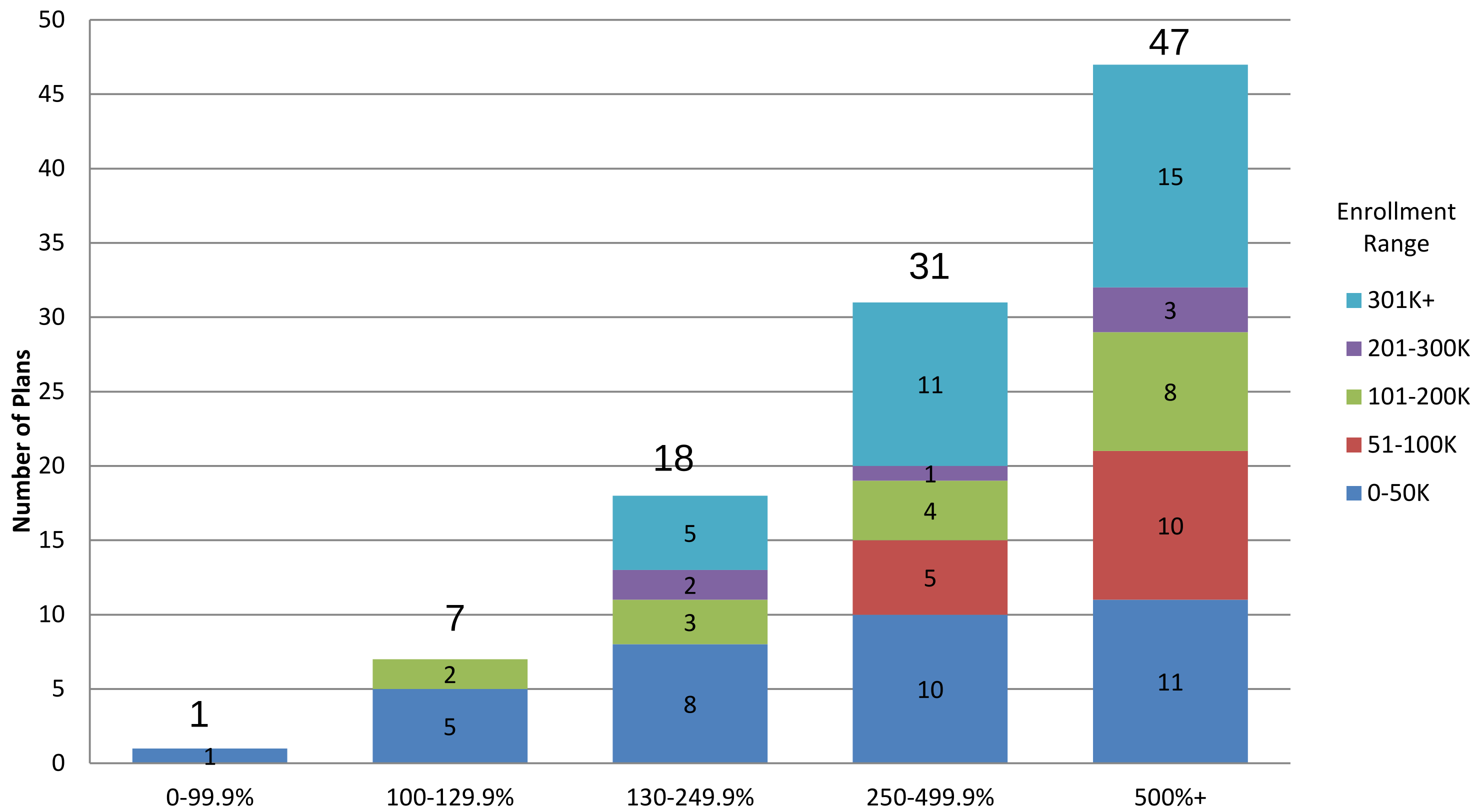
Solvency Background RBOs

- RBOs have had 118 Correction Action Plans (CAPs)
  - 27 CAPs were claims timeliness (23%)
  - 91 CAPs were solvency (78%)

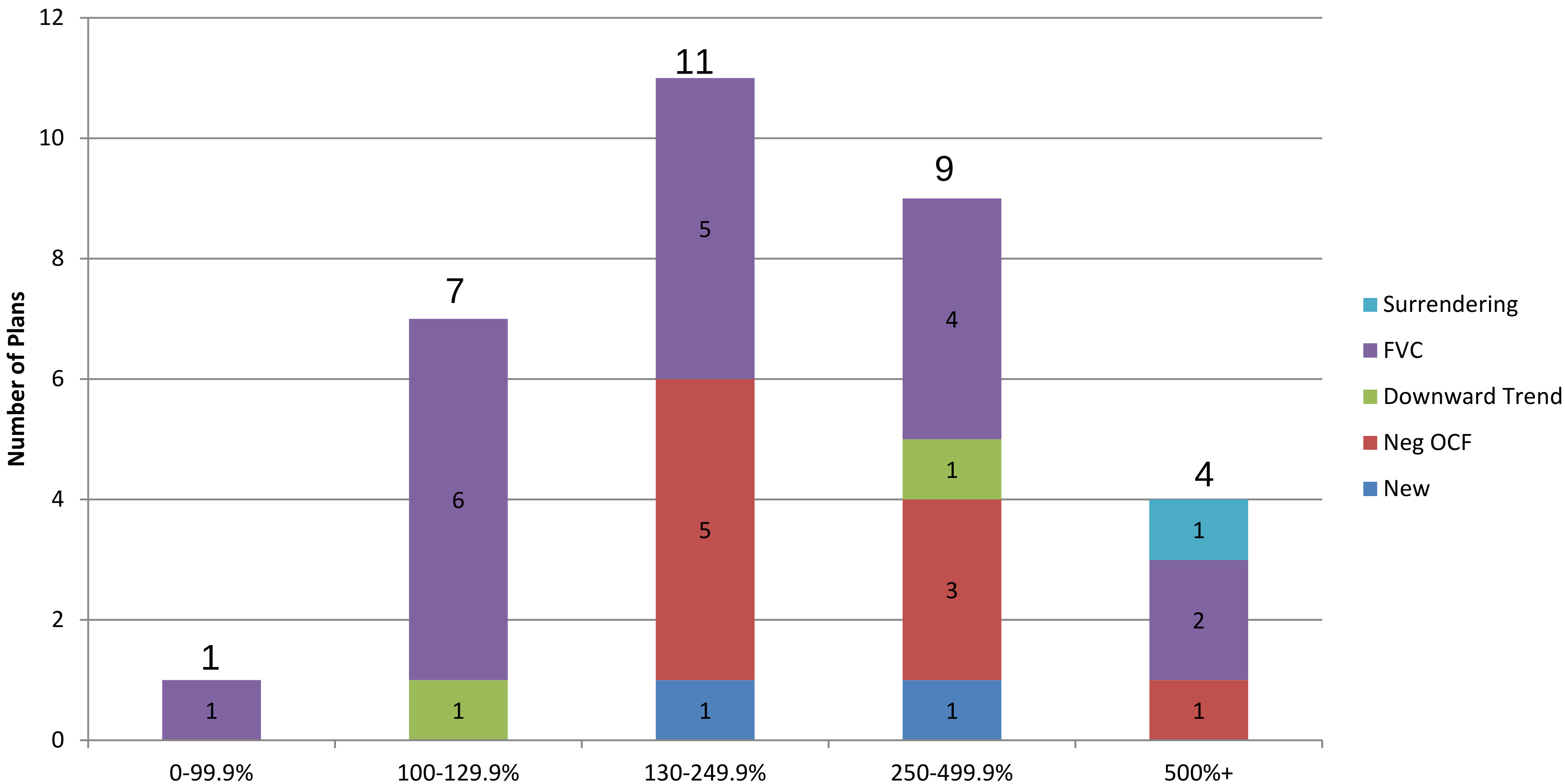
- Of the 91 Solvency CAPs
  - 72 successfully completed CAPs (80%)
    - 19 received cash infusions, subordinated debt or sponsoring organization (27%)
    - 53 became compliant through operations (74%)
  - 15 CAPs were unsuccessful (17%)

- Of the 15 unsuccessful CAPs
  - 7 loaned money to affiliates (47%)
  - 6 had heavy reliance on receivables (40%)

TNE of Plans as of December 31, 2012



TNE of Closely Monitored Plans as of December 31, 2012



Typical Reasons for TNE Deficiencies

- Unfavorable provider contracts or provider inefficiencies that lead to financial viability problems due to high medical expense
- Unsecured affiliate receivables that should be deducted from TNE (those not within the normal course of business, i.e., loans to officers)
- Under accrued liabilities established for medical expenses (claims payable and IBNR-Incurred But Not Reported claims liabilities)

Working Capital Calculation

Working Capital =

Current Assets – Current Liabilities

An RBO must maintain a positive working capital at all times, for the reporting period

Key Issues with Working Capital

- Not all current assets are liquid assets
  - Deferred Tax Asset
  - Prepaid Assets
  - Stop Loss Receivables
  - Risk Pool Receivables
  - Not all receivables are collectable (affiliate receivables, risk pools, stop-loss,)

What is the Cash-to-Claims Ratio

The organization's cash, readily available marketable securities, receivables, excluding all risk pool, risk-sharing, incentive payments and pay-for-performance receivables, and reasonably anticipated to be collected within 60 days

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Organization's unpaid claims (Claims Payable and Incurred But Not Reported Claims (IBNR) liability

Cash-to-Claims Requirement

- RBOs are required to maintain the required Cash-to-Claims Ratio at all times.
- Cash-to-Claims Ratio >.75
  (After 1/1/2007)

Key Issues with Cash-to-Claims

- "…receivables, excluding all risk pool, risk-sharing, incentive payments and pay-for-performance receivables, reasonably anticipated to be collected within 60 days."
- If this ratio is used to determine how much cash is readily available to pay claims, should all the receivables be included (within 60 days)
- Cash, marketable securities, HMO receivables that can be verified within 30/60 days.

Questions?