



AMERICAN ACADEMY of ACTUARIES

September 15, 2008

Katie Campbell
Chair, Medicare Supplement Refund Formula Subgroup
NAIC Accident and Health Working Group of the Life and Health Actuarial Task Force

Subject: Medicare Supplement Refund Formula - Request for Assistance

Dear Katie,

Thank you for your request for assistance in updating the Medicare Supplement Refund Formula. The American Academy of Actuaries'¹ Medicare Supplement Work Group is happy to assist in the effort. Per your request, the group has considered the data and analysis available to it against what has been requested. In most cases, the data and analysis on hand will be sufficient to address the questions raised; and in some cases, data may not be necessary.

As you noted in your request, the most recent available national (approximately) experience² is from 1996 to 2000. This data was described in detail in the work group's *Report on Medicare Supplement Experience, Years 1996-2000*, presented to the NAIC in February 2003, and it includes one expansive dataset (the control data) representing over 1.8 million covered lives per year and a smaller dataset (the select data) representing around 600,000 covered lives per year, which includes the variables of attained age and gender. This same data was used in developing the recommendations in the work group's March 10, 2004, *Report on Loss Ratio Curves for Redetermination of Refund Benchmarks*.

In our view, this data, and the analysis provided in the reports, will be sufficient (or at least as sufficient as any other dataset we could create) to address item 1 of your request and will be used as an important source for our comments with respect to items 2, 3, 4, 6 and 7 of your request. A number of factors led us to the conclusion that the data is sufficient. First, the dataset is substantial—by our estimation, the control data represents over 15 percent of total Medicare Supplement covered lives and the select data around 5 percent. This characteristic will allow the group to generate averages that are reliable. Second, the data is made up of experience from a good number of companies (the control data involved 11 companies, the select data eight), presumably representing a variety of pricing approaches. Third, the data is also split by a number of variables (duration, state, rating method, underwriting, etc). This diversity will allow our group to explore the range of potential results that the refund formula will need to accommodate.

The work group did note that the data available (and likely any other data that could be compiled) will not be sufficient to be the only basis for addressing many of the items where you request pros and cons. Items 5 and 9 will not be based on experience data.

With respect to item 8, the group can smooth the tolerance levels such that the tolerance margin is comparable to the current formula for each broad range of exposed lives. However, the probability of an inappropriate refund (computed at a

¹ The American Academy of Actuaries is a professional association with over 16,000 members, whose mission is to assist public policymakers by providing leadership, objective expertise, and actuarial advice on risk and financial security issues. The Academy also sets qualification, practice, and professionalism standards for actuaries in the United States.

² It should be noted that the data does not include MA, MN or WI which have different benefit arrangements as grandfathered states not subject to the NAIC's standardized benefit plans, nor does it include pre-standardized plans, Medicare Select plans or Plans H through L. As plans M and N are not yet available, data is not available for these plans.

state/plan/company level) is a function of both the margin in the benchmark components relative to each cell, and the tolerance level. To determine how this probability would vary based on different tolerance levels would require data we do not have, nor do we expect it could be collected. We hope that our expectation to merely smooth the tolerance approach is an acceptable answer to item 8.

Our focus, unless you give us different direction, is to establish a refund formula consistent with the current formula but with factors based on actual experience with standardized Medicare Supplement plans. The probability of paying any refunds will not be specifically addressed, but may result in a number of pros/cons or transitions issues elsewhere in our ultimate response to your request.

Absent any concerns from your group, we intend to move forward in addressing the items in your request. Please do not hesitate to contact me, if you have any questions, or if other issues regarding this effort arise.

Sincerely,



Michael V. Carstens
Chair, Medicare Supplement Work Group
American Academy of Actuaries

W:\sep08\lha\wg\AAA-MSWG.doc