Arizona Long Term Care System (ALTCS), Elderly and Physically Disabled (EPD) Actuarial Memorandum

I. Purpose

The purpose of this actuarial memorandum is to demonstrate that the Arizona Long Term Care System (ALTCS) Elderly and Physically Disabled (EPD) capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

Arizona Health Care Cost Containment System (AHCCCS) intends to update these capitation rates quarterly on a retroactive basis to reflect enhanced payments to nursing facilities.

The Affordable Care Act (ACA) places an annual fee on the health insurance industry nationwide including most Medicaid health plans effective January 1, 2014. The fee will be allocated to health insurers based on their respective market share of premium revenue in the previous year. Due to the uncertainty of the actual fees and other unknowns, AHCCCS will not be adjusting the capitation rates for this fee at this time, but intends to make a revision once the impacts are known.

II. Overview of Rate Setting Methodology

The contract year ending 2014 (CYE 14) rates were developed as a rate update from the CYE 13 rates as adjusted January 1, 2013 and approved by CMS. These rates represent the twelve month contract period October 1, 2013, through September 30, 2014.

The assumed trend rates were developed from EPD encounter data for CYE 10, CYE 11 and CYE 12. This encounter data was made available to AHCCCS' actuaries via an extract that provides utilization and cost data, referred to as the "databook". Claims' costs observed for all categories of service were then adjusted to reflect program changes and reimbursement reductions that were effective subsequent to the experience periods used, and the May 2012 termination of the EPD contract with the Senior Care Action Network (SCAN) health plan in Maricopa County. Prospective capitation rates for CYE 14 are built up separately for members dually eligible for Medicare and Medicaid ("duals") and members not eligible for Medicare ("non-duals"). The databook contained the information necessary to distinguish duals from non-duals. The dual and non-dual prospective capitation rates are actuarially sound, as are the rates for the Prior Period Coverage (PPC) and Acute Care Only rate cohorts. Those cohorts are not split out into dual and non-dual rates.

Other data sources used in setting the actuarially sound rates and ranges include health plan financial statements, projected changes in the home and community based services (HCBS) placement, and cost of living adjustment (COLA) figures from the Social Security Administration for use in updating the share of cost (SOC) projection for members placed in nursing facilities.

Trend rates were calculated from the databook and other sources on a unit cost and/or utilization basis by category of service (COS). For more information on trends see Section IV Projected Trend Rates.

Ideally, the experience data should be analyzed by different rate cells which are comprised of members with similar risk characteristics. However, segregating the ALTCS population into different rate cells would lead to a statistical credibility problem due to the statewide dispersion of the relatively small membership base. The ALTCS program has four rate cells: a prospective dual rate, a prospective non-dual rate, a prior period coverage (PPC) rate and an Acute Care Only rate. Capitation rates for the ALTCS population do not differ by gender and/or age, but do differ by Geographical Service Area (GSA).

The experience data includes only ALTCS Medicaid eligible expenses for ALTCS Medicaid eligible individuals, as well as reinsurance amounts. The Prior Period Coverage (PPC) rates are reconciled to a maximum 5% profit or loss.

The general process in developing the prospective rates involves:

- trending the CYE 13 projected capitation gross costs PMPM for nursing facility (NF) and HCBS components to the midpoint of the effective period, which is April 1, 2014, and applying the projected mix percentage;
- projecting the CYE 14 gross costs PMPM for acute care;
- making adjustments for share of cost offsets, provider reimbursement changes and program changes;
- applying a deduction of the reinsurance offsets;
- adding the projected case management, administrative expenses, risk/contingency and premium tax to the projected claim PMPMs to obtain the capitation rates.

Each step is described in the sections below. There are also separate sections describing the PPC population and the Acute Care Only population.

III. Gross Costs PMPM by Category of Service

For NF and HCBS components AHCCCS used the gross costs PMPM from the CYE 13 capitation rates and trended those components forward one year to develop the CYE 14 projected gross costs. For the acute component AHCCCS used actual CYE 12 encounter data, with completion factors, and trended that component forward two years to develop the CYE 14 projected acute component gross cost. The encounter data was reviewed and audited for accuracy, timeliness and completeness through encounter validation studies as well as studies comparing the encounter data to the Contractors' financial statements.

IV. Projected Trend Rates

The trend calculation is based on the time period from October 1, 2009 through September 30, 2012. The claim PMPMs were computed on a yearly basis and a trend factor was calculated. Trend factors are built up separately for dual, non-dual, and

PPC. Trend factors also vary by COS. The trend rates developed were used to bring the base encounter data and gross cost projections from previous periods to the effective midpoint of the contract year.

The trend rates used in projecting the claim costs by rate cell and category of service are identified in Table I. The trend rates shown below in Table I do not include AHCCCS FFS provider rate changes.

Table I: Average Annual Trend Rate before Mix and SOC

	NF	HCBS	Acute
Prospective Dual	1.7%	0.6%	-1.4%
Prospective Non-Dual	2.9%	2.0%	-3.9%
PPC	-1.4%	-5.7%	39.0%

V. Projected Gross Claim PMPM

The contract period for CYE 14 rates is October 1, 2013, through September 30, 2014, so the midpoint is April 1, 2014. The claims' PMPMs from the base data were trended to the midpoint of the CYE 14 rate period.

VI. Mix Percentage

The CYE 14 dual and non-dual mix percentages are set using a combination of current placement percentages, program growth/saturation and the number of ALTCS members. These sources were reviewed by Contractor and by county. The HCBS mix percentages can be found in Table II.

Table II: HCBS Mix Percentages (Dual and Non-Dual)

			CYE13 HCBS Mix		CYE14 HCBS Mix	
GSA	County	Plan	Dual	Non-Dual	Dual	Non-Dual
40	Pinal/Gila	Bridgeway	74.10%	85.24%	74.23%	82.30%
42	LaPaz/Yuma	UHC LTC	61.63%	74.38%	61.79%	74.95%
44	Apache/Coconino/Mohave/Navajo	UHC LTC	68.31%	80.31%	67.77%	76.62%
46	Cochise/Graham/Greenlee	Bridgeway	60.54%	76.45%	59.28%	73.50%
48	Yavapai	UHC LTC	61.62%	78.17%	62.12%	79.11%
50	Pima/Santa Cruz	UHC LTC	72.42%	82.59%	74.72%	83.53%
50	Pima	Mercy Care	65.60%	71.64%	66.00%	71.16%
52	Maricopa	Bridgeway	78.82%	77.85%	77.49%	75.65%
52	Maricopa	UHC LTC	69.58%	79.16%	69.98%	78.48%
52	Maricopa	Mercy Care	74.17%	80.55%	74.12%	81.41%
Statewide Total			71.96%	79.44%	71.94%	79.11%

VII. State Mandates, Court Ordered Programs, Program Changes and Other Changes

Children's Rehabilitative Services (CRS) Costs Moving to EPD
Some EPD members with special health care needs receive services related to specific conditions through the Children's Rehabilitative Services (CRS) program at that same time they are enrolled with an EPD Contractor for unrelated physical health services, and long-term care and behavioral health services. Effective October 1, 2013, the CRS-specific services for those members will be delivered through the members' EPD Contractors in order to integrate total member service delivery through a single Contractor. This results in a shift of approximately $5.5 million to EPD Contractors for CYE 14. The anticipated impact varies by Contractor and GSA.

Provider Rate Changes
Effective October 1, 2013, AHCCCS is increasing FFS provider rates for certain providers based either on access to care needs, Medicare or ADHS fee schedule rates, legislative mandates, or cost of living adjustments. The unit cost (inflation) trends were adjusted appropriately for these changes. The estimated statewide impact is an increase of approximately $13.1 million.

Medical Management Changes
The State of Arizona's 2013 Health and Welfare Budget Reconciliation Bill (BRB) reinstated well visits, which were previously eliminated October 1, 2010, as a covered service for enrolled adults for federal fiscal year 2014. The estimated statewide impact is an increase of approximately $84,000.

Primary Care Provider (PCP) Payment Increase
Section 1902(a)(13)(C) of the Social Security Act, as amended by the Affordable Care Act, requires minimum levels of Medicaid payment for certain primary care services, provided by certain physicians. The AHCCCS managed care model, with strict requirements regarding actuarially-sound capitation rates, necessitates that Contractors be funded for expected cost increases due to primary care rate parity. AHCCCS proposes to provide Contractors the necessary funds to increase primary care payments by using Model 3: Non-risk Reconciled Payments for Enhanced Rates as referenced in the *Medicaid Managed Care Payment for PCP Services in 2013 and 2014, Technical Guidance and Rate Setting Practices* (Technical Guidance) document released by CMS.

In summary, under Model 3, prospective capitation rates would not be adjusted for the enhanced primary care payments. Rather, AHCCCS would query actual encounter data on a quarterly basis to calculate the total payments that eligible providers were paid for eligible services in order to reach the mandated enhanced payment rates. Once the data on this report is verified, AHCCCS would pay the Contractors the calculated additional payment amounts. A more detail explanation of the process and methodology can be found in the Actuarial Certification submitted to CMS for approval of AHCCCS methodology. There is no impact to the CYE 14 capitation rates.

In-Lieu of Services
Included in the base rates is funding for "in lieu of" services, substituting cost-effective alternative inpatient settings in place of more costly inpatient non-specialty hospital placements. State approved FFS rates at inpatient non-specialty hospitals are approximately 93.5% more expensive than those provided in alternative inpatient settings. The proposed capitation rates allow for the provision of services in alternative inpatient settings that are licensed by Arizona Department of Health Services/Arizona Licensing Services/Office of Behavioral Health License, in lieu of services in an inpatient non-specialty hospital, thus no increase to cap rates is included.

VIII. Projected Net Claim PMPM

The NF and HCBS projected gross claim PMPMs were adjusted for the mix percentages. The projected gross claims PMPMs were then discounted for the recipients' Share of Cost (SOC). The SOC component is fully reconciled with each Contractor. To develop the reinsurance offset PMPM AHCCCS used actual CYE 12 reinsurance payment data and trended forward two years using the trend assumption from the acute component of the capitation rates. The calculation of the reinsurance offset PMPM was performed separately for dual and non-dual members.

IX. Coordination of Benefits

Inherent in the encounter and financial data are unit cost trends which incorporate Contractors' Coordination of Benefits (COB) activities. AHCCCS provides Contractors with verified commercial and Medicare coverage information for their members which Contractors utilize to ensure payments are not made for medical services that are covered by the other carriers. When Contractors make a payment to cover members' coinsurance, deductibles, or Medicaid-covered services that are not covered by the other carriers, they submit encounters containing these reduced amounts. From state fiscal year (SFY) 2008 to SFY 2013, encounter-reported COB cost avoidance grew by greater than 128%, from $130 million to $297 million. Additionally, in CYE 2013 ALTCS EPD Contractors cost-avoided $61 million in the nine months ending March 31, 2013, in additional claims for which the Contractor had no financial obligation after the private insurance or Medicare payment was made. Consequently no encounters were submitted to AHCCCS and thus those services are excluded from capitation expenditure projections completely. AHCCCS continues to emphasize the importance of COB activities.

X. Case Management, Administrative Expenses and Risk Contingency

The Case Management rates represent those rates awarded as part of the CYE 12 RFP process, adjusted for expected growth in the HCBS mix, which would increase case management expenses. The administrative expenses also represent rates

awarded as part of the RFP process. The risk contingency percentage remains the same as CYE 13 at 1%.

XI. Proposed Capitation Rates and Their Impacts

The proposed capitation rates for the EPD population equal the sum of the projected net claim PMPM (in Section VIII) and the projected case management, administrative expenses and risk contingency PMPM (in section X) divided by one minus the two percent premium tax. Tables IIIa and IIIb show the proposed dual and non-dual capitation rates for the EPD population statewide.

Table IIIa: Statewide Projected Net Capitation PMPM EPD - Dual

Service Category	Gross CYE13 Rate	Mix	Net CYE13 Rate	Pct Gross Change	Pct Net Change	Gross CYE14 Rate	Mix	Net CYE14 Rate
Nursing Facility (NF)	$5,538.45	28.04%	$1,553.26	3.2%	3.3%	$5,717.71	28.06%	$1,604.59
Share of Cost			($268.16)		-6.3%			($251.31)
Net Nursing Facility			$1,285.09		5.3%			$1,353.28
Home/Community (HCBS)	$1,397.40	71.96%	$1,005.50	2.3%	2.2%	$1,428.87	71.94%	$1,027.88
Case Management			$113.55		0.2%			$113.74
Acute Care			$137.77		-5.2%			$130.61
Administration			$166.84		-0.4%			$166.24
Risk Contingency			$27.90		2.6%			$28.64
Premium Tax			$55.85		3.1%			$57.56
Net Capitation PMPM			$2,792.50		3.1%			$2,877.94

Table IIIb: Statewide Projected Net Capitation PMPM EPD - Non-Dual

Service Category	Gross CYE13 Rate	Mix	Net CYE13 Rate	Pct Gross Change	Pct Net Change	Gross CYE14 Rate	Mix	Net CYE14 Rate
Nursing Facility (NF)	$6,784.50	20.56%	$1,395.22	4.1%	5.7%	$7,060.54	20.89%	$1,474.94
Share of Cost			($32.19)		0.7%			($32.41)
Net Nursing Facility			$1,363.03		5.8%			$1,442.53
Home/Community (HCBS)	$1,719.72	79.44%	$1,366.06	3.6%	3.2%	$1,781.70	79.11%	$1,409.50
Case Management			$114.26		0.1%			$114.34
Acute Care			$1,311.29		6.7%			$1,398.82
Administration			$162.72		0.2%			$163.08
Risk Contingency			$50.01		0.0%			$50.01
Premium Tax			$89.13		4.8%			$93.43
Net Capitation PMPM			$4,456.50		4.8%			$4,671.72

Note: The product of the gross NF or HCBS rate and mix percentages as shown may not equal the net rate due to rounding.

XII. Acute Care Only Members

As in prior years, for members who are only eligible for acute care services in the ALTCS program, Contractors will be paid the combined acute care component plus

the case management and administrative components. Since the reinsurance policy is the same for these members as for the other ALTCS members, the same reinsurance offset is appropriate.

XIII. Prior Period Coverage (PPC) Rates

PPC rates cover the period of time from the effective date of eligibility to the day a member is enrolled with the Contractor. AHCCCS developed the CYE 14 PPC rates by applying a trend factor to the CYE 13 rates. The trend calculation is based on the time period from October 1, 2009 through September 30, 2012. Due to the relatively short PPC enrollment period and low member month counts, AHCCCS' actuaries combined geographic regions in order to enhance statistical credibility when needed. Since PPC costs are highly volatile and unable to be managed by the Contractors, AHCCCS limits the magnitude of the rate change for each geographic area. PPC rates are reconciled to a five percent profit/loss corridor.

XIV. Proposed Capitation Rates and Budget Impact

Table IV includes the net capitation rates on a statewide basis for all rate cells as well as the estimated budget impact based off of CYE 14 projected member months. The adjustments impact Contractors ranging from +3.0% to +5.0%. Appendix I shows EPD rates by geographical service area and Contractor.

Table IV: Proposed Capitation Rates and Budget Impact

Rate Cell	EPD Prospective - Dual	EPD Prospective - Non-Dual	PPC	Acute Only	Total
CYE 14 Projected MMs	258,191	48,965	11,186	4,744	
CYE 13 Rate (1/1/13)	$2,792.50	$4,456.50	$855.56	$497.57	
CYE 14 Rate	$2,877.94	$4,671.72	$899.76	$511.80	
Estimated CYE 13 Capitation	$720,998,611	$218,211,329	$9,570,627	$2,360,400	$951,140,967
Estimated CYE 14 Capitation	$743,058,157	$228,749,601	$10,065,065	$2,427,905	$984,300,728
Dollar Impact	$22,059,546	$10,538,272	$494,438	$67,505	$33,159,762
Percentage Impact	3.1%	4.8%	5.2%	2.9%	3.5%

XV. CMS Rate Setting Checklist

1. Overview of rate setting methodology

A.A.1.0: Overview of rate setting methodology

AHCCCS is performing a rate update from the previously approved contract year ending 2013 (CYE 13) rates under 42 CFR 438.6(c). Please refer to Section II.

AA.1.1: Actuarial certification

Please refer to Section XVI.

AA.1.2: Projection of expenditure

Please refer to Section XIV.

AA.1.3: Procurement, prior approval and rate setting

AHCCCS is operating under the Competitive Procurement contracting method.

AA.1.5: Risk contract

The contract is an at risk contract.

AA.1.6: Limit on payment to other providers

AHCCCS makes no additional payment to the providers, except for Disproportionate Share Hospital (DSH), Graduate Medical Education (GME) and Critical Access Hospitals. GME is paid in accordance with state plan. DSH and Critical Access Hospital payments are paid in accordance with Waiver Special Terms and Conditions. None of the additional payments to the providers were included in the capitation calculation.

AA.1.7: Rate modification

Please refer to Sections III, IV, VI, VII, VIII, XII, and XIII.

XVI. Actuarial Certification of the Capitation Rates

I, Matthew C. Varitek, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy of Actuaries and a Fellow of the Society of Actuaries. I meet the qualification standards established by the American Academy of Actuaries and have followed the practice standards established from time-to-time by the Actuarial Standards Board.

The rates were developed using generally accepted actuarial principles and practices and are considered to be actuarially sound. The rates were developed to demonstrate compliance with the CMS requirements under 42 CFR 438.6(c) and are in accordance with applicable laws and regulations. The rates are appropriate for the Medicaid populations covered and Medicaid services to be furnished under the contract. The rates may not be appropriate for any other purpose. The documentation has been included with this certification. The actuarially sound capitation rates that are associated with this certification are effective for the twelve-month period beginning October 1, 2013.

The actuarially sound capitation rates are a projection of future events. It may be expected that actual experience will vary from the values in the rates.

In developing the actuarially sound capitation rates, I have relied upon data and information provided by the Program Contractors and the AHCCCS internal databases. I have accepted the data without audit and have relied upon the Program Contractors auditors and other AHCCCS employees for the accuracy of the data.

This actuarial certification has been based on the actuarial methods, considerations, and analyses promulgated from time to time through the Actuarial Standards of Practice by the Actuarial Standards Board.

This certification letter assumes the reader is familiar with the EPD program, Medicare and Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS and CMS and should not be relied upon by third parties. Other readers should seek the advice of actuaries or other qualified professionals competent in the area of actuarial rate projections to understand the technical nature of these results.

Matthew C. Varitek — 08.28.2013

Matthew C. Varitek — Date

Fellow of the Society of Actuaries
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Appendix I

GSA	County	Contractor	EPD Dual	EPD Non-Dual	Acute Only	PPC
40	Pinal/Gila	Bridgeway	$3,031.61	$4,341.89	$475.58	$985.24
42	LaPaz/Yuma	UHC LTC	$2,954.83	$4,089.22	$464.85	$985.24
44	Apache/Coconino/Mohave/Navajo	UHC LTC	$2,486.88	$4,454.40	$442.81	$985.24
46	Cochise/Graham/Greenlee	Bridgeway	$2,936.61	$4,306.48	$441.19	$985.24
48	Yavapai	UHC LTC	$3,119.45	$4,386.19	$375.43	$985.24
50	Pima/Santa Cruz	UHC LTC	$2,821.21	$4,245.36	$378.66	$733.38
50	Pima	Mercy Care	$3,082.38	$4,980.13	$496.09	$733.38
52	Maricopa	Bridgeway	$2,616.67	$5,136.17	$496.08	$899.90
52	Maricopa	UHC LTC	$2,871.00	$4,816.84	$353.47	$899.90
52	Maricopa	Mercy Care	$2,962.57	$4,686.70	$576.01	$899.90