

Department of Economic Security / Division of Developmental Disabilities (DES/DDD) Actuarial Memorandum

I. Purpose

The purpose of this actuarial memorandum is to demonstrate that the capitation rates were developed in compliance with 42 CFR 438.6(c). It is not intended for any other purpose.

Arizona Health Cost Containment System (AHCCCS) intends to review and possibly update the DDD Contractor capitation rates effective October 1, 2015 to include changes to the acute care and behavioral health categories of service. This capitation rate update for July 1, 2015 does not include adjustments for anticipated reimbursement changes or program changes with effective dates after July 1, 2015. If appropriate, AHCCCS will include these adjustments in the capitation rates updated effective October 1, 2015.

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. AHCCCS intends to make a revision once the impacts are known, if applicable to DDD's sub-contractors.

II. General Program Information

This certification covers the DD program. This program covers Medicaid eligible members with intellectual and developmental disabilities. The program offers long-term care services, acute physical health services, and behavioral health services.

Contract year ending 2016 (CYE 16) capitation rates were developed as a rate rebase from the previously approved contract year ending 2015 (CYE 15) capitation rates. The CYE 16 capitation rates represent the twelve month contract period from July 1, 2015 through June 30, 2016. DDD is a division of the state's Department of Economic Security and thus operates on the state fiscal year period.

The experience used in the development of these rates only includes DDD Medicaid eligible expenses for DD Medicaid eligible individuals.

Ideally, the experience data should be analyzed by different rate cells which are comprised of members with similar risk characteristics. However, segregating the DD population into different rate cells would lead to a statistical credibility problem due to the statewide disbursement of the relatively small membership base. Accordingly, DDD will have three separate capitation rates – a regular DDD capitation rate, a Behavioral Health capitation rate, and a targeted case management (TCM) capitation

rate. The regular DDD capitation rate covers the DD members' physical health and long-term care services. The Behavioral Health capitation rate covers the DD members' behavioral health services. The TCM capitation rate covers case management services for members who have a DD diagnosis and meet the financial eligibility for Title XIX and XXI programs, but do not meet the functional requirements of Arizona Long Term Care Services (ALTCs).

The Behavioral Health capitation rate and the Acute rate component (including the Acute reinsurance offset) of the regular DDD capitation rate will not be rebased or updated for this certification. These rates will be reviewed for an October 1, 2015 effective date and updated as appropriate.

III. Overview of Rate Setting Methodology

CYE 16 actuarially sound capitation rates were developed utilizing the steps outlined as follows:

1. Develop base period data (Section IV)
2. Develop trend factors (Section V)
3. Apply trend factors to bring base period data forward (Section VI)
4. Adjust CYE 16 claims costs for programmatic and provider fee schedule changes, if applicable (Section VII)
5. Add provision for share of cost (SOC) (Section VIII)
6. Add provision for non-benefit costs (Section IX)
7. Combine for final capitation rates (Section X)

IV. Base Period Data

The base period data consisted of historical Medicaid encounter and member month data for this population for the time period July 1, 2011 through June 30, 2014. In addition, AHCCCS used the Contractor's supplemental experience data for the same time frame due to zero payment data submitted on encounter data for a small portion (approximately three percent) of nursing facility (institutional) and home and community based services (HCBS) expenses.

The data was reviewed for accuracy, timeliness and completeness through encounter validation studies as well as studies comparing the encounter data to the Contractor's financial statements.

Adjustments were made to the base data for completion factors, historical programmatic changes and historical provider fee for service rate schedule changes.

Equal weights were then applied to the adjusted base data for the three periods of CYE 12 (July 1, 2011 through June 30, 2012), CYE 13 (July 1, 2012 through June 30, 2013) and CYE 14 (July 1, 2013 through June 30, 2014) to arrive at the base period claim costs per member per month (PMPM) rates. The base period claim costs PMPM by category of service (COS) are shown in Table I.

Table I: Base Period Claims Costs PMPM

| High Level COS | Data Source | Detail COS | Base Period PMPM |
|----------------|------------------------------|----------------------------|------------------|
| Institutional | Encounters | Inst | \$ 48.65 |
| Institutional | DDD Supplemental Information | ATPC, ICF/IID ¹ | \$ 72.67 |
| HCBS | Encounters | Attendant Care | \$ 197.57 |
| HCBS | Encounters | Respite | \$ 270.34 |
| HCBS | Encounters | Hab Res Per Diem | \$ 910.26 |
| HCBS | Encounters | Hab Rest Per 15 mins | \$ 274.54 |
| HCBS | Encounters | Day Treatment | \$ 306.61 |
| HCBS | Encounters | Self Care Home | \$ 9.83 |
| HCBS | Encounters | Therapy and Evals | \$ 112.84 |
| HCBS | Encounters | Transportation | \$ 38.29 |
| HCBS | Encounters | Nursing | \$ 110.07 |
| HCBS | Encounters | Employment | \$ 72.91 |
| HCBS | Encounters | Misc | \$ 1.06 |
| HCBS | DDD Supplemental Information | SOGH ² | \$ 15.76 |

1) Arizona Training Program Coolidge (ATPC), Institutional Care Facility/Individuals with Intellectual Disabilities (ICF/IID)

2) State Operated Group Home (SOGH)

V. Projected Trend Rates

A trend analysis was performed using the adjusted base period data. The historical trends were developed from the adjusted base period data and were examined using monthly, quarterly and annual regression analysis. The trends were developed at a category of service (COS) level, with a limit on the percentage change to smooth out unreasonable trends.

The annual historical PMPM trend rates by COS are identified in Table II.

Table II: Annual Historical Trend Rates

| High Level COS | Data Source | Detail COS | Annual Trend Rate |
|----------------|------------------------------|---------------|-------------------|
| Institutional | Encounters | Inst | 2.2% |
| Institutional | DDD Supplemental Information | ATPC, ICF/IID | -6.2% |

| | | | |
|------|------------------------------|----------------------|-------|
| HCBS | Encounters | Attendant Care | 5.5% |
| HCBS | Encounters | Respite | 0.6% |
| HCBS | Encounters | Hab Res Per Diem | 0.2% |
| HCBS | Encounters | Hab Rest Per 15 mins | 0.7% |
| HCBS | Encounters | Day Treatment | 4.1% |
| HCBS | Encounters | Self Care Home | -0.7% |
| HCBS | Encounters | Therapy and Evals | 3.4% |
| HCBS | Encounters | Transportation | 4.9% |
| HCBS | Encounters | Nursing | 5.5% |
| HCBS | Encounters | Employment | 7.1% |
| HCBS | Encounters | Misc | -3.1% |
| HCBS | DDD Supplemental Information | SOGH | 7.6% |

VI. Projected Claim Costs

Base period claim costs PMPM were trended 36 months using the trend rates shown in Table II from the midpoint of the base period claim costs to the midpoint of the projected claims period. The midpoint of the projected claims period is January 1, 2016. The midpoint of the base claims period is January 1, 2013.

The projected claims cost PMPM by COS are identified in Table III.

Table III: Projected Claims Costs PMPM

| High Level COS | Data Source | Detail COS | Proj Claim Cost PMPM |
|----------------|------------------------------|----------------------|----------------------|
| Institutional | Encounters | Inst | \$ 51.91 |
| Institutional | DDD Supplemental Information | ATPC, ICF/IID | \$ 59.91 |
| Institutional | Total | Total | \$ 111.83 |
| HCBS | Encounters | Attendant Care | \$ 231.86 |
| HCBS | Encounters | Respite | \$ 275.65 |
| HCBS | Encounters | Hab Res Per Diem | \$ 915.28 |
| HCBS | Encounters | Hab Rest Per 15 mins | \$ 280.74 |
| HCBS | Encounters | Day Treatment | \$ 345.44 |
| HCBS | Encounters | Self Care Home | \$ 9.61 |
| HCBS | Encounters | Therapy and Evals | \$ 124.79 |
| HCBS | Encounters | Transportation | \$ 44.18 |
| HCBS | Encounters | Nursing | \$ 129.43 |
| HCBS | Encounters | Employment | \$ 89.50 |
| HCBS | Encounters | Misc | \$ 0.96 |
| HCBS | DD Supplemental Information | SOGH | \$ 19.62 |
| HCBS | Total | Total | \$2,467.06 |

VII. Projected Programmatic Changes

Cost Effectiveness Study Rates

The Special Terms and Conditions of Arizona's 1115 Waiver permit DD member placement in an HCBS setting if the HCBS services will meet the individual member's needs and the HCBS costs for the specific member do not exceed 100 percent of the net cost of institutional care for that member. This determination is done through a Cost Effectiveness Study (CES). DDD is currently rebasing the institutional care costs used in the CES. While this is not expected to materially impact the capitation rates, AHCCCS and DES will monitor this situation and, if it is determined there was a material impact, the capitation rates will be adjusted.

VIII. Projected Share of Cost

The CYE 16 capitation rates include a provision for the recipients' share of cost (SOC). The share of cost was estimated based on the DD member SOC data, and was rebased for CYE 16. This is a similar method to previously approved rates. The CYE 16 SOC PMPM for the DD population is \$5.18.

IX. Non-Benefit Costs

Case Management

For DD members the CYE 16 case management PMPM was developed by reviewing supplemental case management cost reports provided by the Contractor, the AHCCCS case management model, and the Contractor financials. This is a similar methodology to previously approved rates. The CYE 16 case management PMPM for the DD population is \$154.13.

The targeted case management (TCM) PMPM was developed by reviewing supplemental TCM cost information for the TCM population provided by the Contractor and the AHCCCS TCM model. The supplemental TCM cost information showed large increases for CYE 14 and CYE 15. These increases were researched to identify cost drivers and to determine if costs were expected to increase, stabilize, or decrease. It was concluded that the main driver of this increase was the ramp-up of an initiative which required more case management services provided to a target population of 0-3 year olds. It was also determined this model has now been fully implemented and thus the TCM PMPM is not expected to continue increasing at the historical levels. The CYE 16 TCM PMPM with premium tax for the TCM population is \$145.92.

Administrative Costs, Risk Contingency and Premium Tax

The administrative cost component was developed by reviewing the Contractor's administrative expense report which includes historical and projected administrative costs, and financial statements. The increase for this component is due to a misalignment between the capitation rates and the actual administrative expense for the Contractor. After determining the appropriate administrative cost component, AHCCCS compared the administrative expense for DDD to the administrative expense

of the similar ALTCS Elderly and Physically Disabled (EPD) program to confirm that an increase in this component is valid. The CYE 16 administrative expense PMPM for the Contractor for the DD population is \$197.79. The risk contingency for the Contractor is 1.00% and the premium tax is 2.00%.

X. Proposed Capitation Rates and Their Impacts

The proposed capitation rates equal the sum of projected claim costs (Section VI), projected programmatic and provider fee schedule changes (Section VII), projected SOC (Section VIII) and provision for non-benefit costs (Section IX), divided by one minus the two percent premium tax. The premium tax for the behavioral health component is included in the DDD capitation rate.

Appendix I shows the current and proposed capitation rate build-up by rate component. As noted above the Acute component (including the Acute reinsurance offset) of the regular DDD capitation rate and the Behavioral Health capitation rate have not been rebased or updated thus those two rate components will show no impact over current capitation rate components. They will be reviewed for a possible October 1, 2015 capitation rate rebase/update.

Table IV shows the current and proposed capitation rates and the budget impact from CYE 15 (04/01/15 capitation rate) to CYE 16 using CYE 16 projected members.

Table IV: Proposed Capitation Rates and Budget Impact

| Rate Cell | Projected CYE 16 Member Months | CYE 15 (4/1/15) Rate | | CYE 16 Rate | | Costs Based on Projected CYE 16 Member Months | | Dollar Impact | Percentage Impact |
|--------------------------|--------------------------------|----------------------|-------------|--------------------------------------|-----------------------------|---|--------------|---------------|-------------------|
| | | CYE 15 (4/1/15) Rate | CYE 16 Rate | Estimated CYE 15 (4/1/15) Capitation | Estimated CYE 16 Capitation | | | | |
| DDD | 344,079 | \$ 3,358.43 | \$ 3,414.03 | \$ 1,155,562,524 | \$ 1,174,693,614 | \$ 19,131,090 | 1.66% | | |
| Behavioral Health | 344,079 | \$ 124.18 | \$ 124.18 | \$ 42,727,431 | \$ 42,727,431 | \$ - | 0.00% | | |
| Targeted Case Management | 51,964 | \$ 123.61 | \$ 145.92 | \$ 6,423,403 | \$ 7,582,502 | \$ 1,159,099 | 18.04% | | |
| Total | | | | \$ 1,204,713,357 | \$ 1,225,003,547 | \$ 20,290,189 | 1.68% | | |

BH does not reflect premium tax

XI. Coordination of Benefits

While this section does not directly impact the capitation rate development it is important to note the efforts made by the State and the Contractors when it comes to coordination of benefits. 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, the Contractors submit encounters for these amounts. From state fiscal year (SFY) 2008 through SFY 2014, encounter-reported Coordination of Benefits (COB) cost avoidance grew by greater than 187.5%, from \$16 million to \$46 million. Additionally, DDD cost-avoided

more than \$8 million in SFY ending 2014 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 therefore those services are excluded completely from capitation expenditure projections. AHCCCS continues to emphasize the importance of COB activities with the Contractor.

XII. CMS Rate Setting Checklist

1. Overview of rate setting methodology

AA.1.0: Overview of rate setting methodology

AHCCCS is performing a rebase from the previously approved capitation rates for contract year ending 2015 (CYE 15) under 42 CFR 438.6(c). Please refer to Section II.

AA.1.1: Actuarial certification

Please refer to Section XIII.

AA.1.2: Projection of expenditure

Please refer to Section X and Appendix I.

AA.1.3: Procurement, prior approval and rate setting

This is a sole source contracting method, between AHCCCS and DES/DDD.

AA.1.5: Risk contract

The contract is an at risk contract, however there are provisions for share of cost and reinsurance.

AA.1.6: Limit on payment to other providers

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

AA.1.7: Rate modification

Please refer to Sections II through IX.

2. Base Year Utilization and Cost Data

AA.2.0: Base year utilization and cost data

Please refer to Section IV.

AA.2.1: Medicaid eligibles under the contract

The data includes only those members eligible for managed care.

AA.2.2: Dual Eligibles (DE)

There are dual eligibles.

AA.2.3: Spenddown

Not applicable, not covered under this contract.

AA.2.4: State plan services only

The contract between AHCCCS and DDD specifies that DDD may cover additional services. Non-covered services were excluded from the base data and not included in the rates.

AA.2.5: Services that can be covered by a capitated entity out of contract savings.

Same as AA.2.4

3. Adjustments to the Base Year Data

AA.3.0 Adjustments to base year data

Please refer to Section IV.

AA.3.1 Benefit differences

There are no changes to the covered benefits. Therefore, no adjustment was made.

AA.3.2 Administrative cost allowance calculation

Please refer to Section IX.

AA.3.3 Special populations' adjustment

It is anticipated that the risk characteristics of this population will not change materially from the base period to the effective period of the capitation rates. Therefore, no adjustment was made.

AA.3.4 Eligibility Adjustments

No adjustment was made.

AA.3.5 DSH Payments

No DSH payment was included in the capitation development.

AA.3.6 Third party Liability (TPL)

This is a contractual arrangement between AHCCCS and its Contractors.

AA.3.7 Copayments, coinsurance and deductible in the capitated rates

Not applicable, member cost sharing is not required.

AA.3.8 Graduate Medical Education (GME)

The experience excludes any payment for GME.

AA.3.9 FQHC and RHC reimbursement

The experience excludes any additional payments that FQHCs may receive from the state.

AA.3.10 Medical cost/ trend inflation

Please refer to Section V.

AA.3.11 Utilization adjustment

Other than trend, no specific adjustment was made to utilization.

AA.3.12 Utilization and cost assumptions

Not applicable since actual experience was used.

AA.3.13 Post-eligibility treatment of income (PETI)

Not applicable, not required to consider PETI.

AA.3.14 Incomplete data adjustment

The encounter data was not fully complete. AHCCCS applied completion factors to the encounter data.

4. Establish Rate Category Groupings

AA.4.0: Establish rate category groupings

Please refer to Section II.

AA.4.1: Age

Please refer to Section II.

AA.4.2: Gender

Please refer to Section II.

AA.4.3: Locality/region

Please refer to Section II.

AA.4.4: Eligibility category

Please refer to Section II.

5. Data Smoothing, Special Populations and Catastrophic Claims

AA.5.0: Data smoothing

Please refer to Sections II, IV and V.

AA.5.1: Special populations and assessment of the data for distortions

Data was not adjusted for special populations.

AA.5.2: Cost-neutral data smoothing adjustments

Please refer to Section V.

AA.5.3: Risk-adjustment

There is no risk adjustment.

6. Stop Loss, Reinsurance, or Risk-Sharing arrangements

AA.6.1: Commercial reinsurance

There is no commercial reinsurance.

AA.6.2: Simple stop loss program

There is a reinsurance program with DDD. See contractor for additional information.

AA.6.3: Risk corridor program

There is no risk sharing between AHCCCS and DDD, except the stop loss program (i.e. Reinsurance). DDD assumes all other risks.

7. Incentive Arrangements

There is no incentive arrangement between AHCCCS and DDD.

XIII. Actuarial Certification of the Capitation Rates

I, Windy J. Marks, am an employee of Arizona Health Care Cost Containment System (AHCCCS). I am a Member of the American Academy 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 July 1, 2015.

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 DES/DDD and the AHCCCS internal databases. I have accepted the data without audit and have relied upon the DES/DDD 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 DD program, Medicaid eligibility rules and actuarial rating techniques. It is intended for AHCCCS, DES/DDD 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.

Signature on File

05/15/15

Windy J. Marks

Date

Fellow of the Society of Actuaries
Member, American Academy of Actuaries

APPENDIX I: Capitation Rates by Rate Component

| DES/DDD Capitation Rate | CYE 15 (4/1/15) Capitation Rate PMPM | CYE16 Capitation Rate PMPM | Effective Percentage Change from Current Rate | Certification Sections |
|---|---|----------------------------------|--|------------------------|
| Claim Costs | | | | |
| Institutional Services | \$ 119.82 | \$ 111.83 | -6.67% | Section IV-VI |
| Home and Community Based Services | \$ 2,423.06 | \$ 2,467.06 | 1.82% | Section IV-VII |
| Acute Services | \$ 415.01 | \$ 415.01 | 0.00% | Section II |
| Total Claim Costs | \$ 2,957.89 | \$ 2,993.89 | 1.22% | |
| Share of Cost | \$ (5.50) | \$ (5.18) | -5.82% | Section VIII |
| Acute Services Reinsurance | \$ (28.85) | \$ (28.85) | 0.00% | Section II |
| Total Net Claim Costs | \$ 2,923.54 | \$ 2,959.86 | 1.24% | |
| Non-Benefit Costs | | | | |
| Case Management | \$ 153.62 | \$ 154.13 | 0.33% | Section IX |
| Administration | \$ 180.50 | \$ 197.79 | 9.58% | Section IX |
| Risk Contingency | \$ 31.12 | \$ 31.48 | 1.17% | Section IX |
| Premium Tax | \$ 69.65 | \$ 70.76 | 1.60% | Section IX |
| Total Non-Benefit Costs | \$ 434.88 | \$ 454.16 | 4.43% | |
| DES/DDD Capitation Rate (includes Premium Tax) | \$ 3,358.43 | \$ 3,414.03 | 1.66% | |

| Behavioral Health Capitation Rate | CYE 15 (4/1/15) Capitation Rate PMPM | CYE16 Capitation Rate PMPM | Effective Percentage Change from Current Rate | Certification Sections |
|---|---|----------------------------------|--|------------------------|
| Claim Costs | | | | |
| Behavioral Health Services | \$ 111.33 | \$ 111.33 | 0.00% | Section II |
| Total Claim Costs | \$ 111.33 | \$ 111.33 | 0.00% | |
| Non-Benefit Costs | | | | |
| Administration and Risk Contingency | \$ 12.85 | \$ 12.85 | 0.00% | Section II |
| Total Non-Benefit Costs | \$ 12.85 | \$ 12.85 | 0.00% | |
| Behavioral Health Capitation Rate (no Premium Tax) | \$ 124.18 | \$ 124.18 | 0.00% | |

| Targeted Case Management (TCM) | CYE 15 (4/1/15) Capitation Rate PMPM | CYE16 Capitation Rate PMPM | Effective Percentage Change from Current Rate | Certification Sections |
|--------------------------------------|---|----------------------------------|--|------------------------|
| Non-Benefit Costs | | | | |
| Case Management | \$ 121.14 | \$ 143.00 | 18.04% | Section IX |
| Premium Tax | \$ 2.47 | \$ 2.92 | 18.04% | Section IX |
| Targeted Case Management Rate | \$ 123.61 | \$ 145.92 | 18.04% | |

Notes

DES/DDD Capitation Rate includes Premium Tax for the Behavioral Health Capitation Rate