

October 19, 2015

Justification of Rate Increase – Small Group Market

Scope and Range of the Rate Increase

The overall requested rate increase for Small Groups in the Affordable Care Act (“ACA”) Single-Risk Pool is 6.2%. This is before any impacts due to member aging.

The actual rate changes realized by groups may vary significantly from the figure listed above. This may be for a variety of reasons including the age composition of the group, its geographic location, its unique benefit plan design, or product. Age is an allowable rating variable for small group, so groups that have added or dropped employees could see large changes in premium rates if the group has become older or younger compared to the previous year. The rates submitted by Blue Cross Blue Shield are prior to any government provided tax credits to purchase coverage on the Small Group Marketplace (“SHOP”); therefore the 6.2% only reflects the requested change for total premium cost and does not take into account any subsidies the group may be eligible for.

This filing impacts 36,758 members currently enrolled in our Small Group ACA market as of March 31, 2015.

Summary of Drivers

Higher baseline experience than was assumed when setting our 2015 rates contributes approximately 2.4% to our increase. A larger percentage of our Small Group segment than originally anticipated has retained their medical coverage as a Grandfathered plan or under the Federal Transitional program. Higher risk groups have migrated to the ACA market, which has led to worse experience than expected. Part of this increase is offset by risk transfer payments we expect to receive from other issuers for covering individuals with high cost or chronic conditions, such as major depressive disorders, metastatic cancers, and diabetes.

As demonstrated in our filed 2014 Supplemental Health Care Exhibit, BCBSNC received \$906.0 million in premium revenue, incurred \$739.9 million in medical expenses, and reported a \$3.4 million



underwriting gain on the Small Group segment (combined single risk pool, transitional, and grandfathered experience) in 2014 including operating expenses, fees, and State and Federal taxes. The rate increase requested here for approval is expected to return the segment to our target contribution to surplus after fees and taxes.

Changes in medical service costs and utilization: higher provider reimbursement levels due to increases in our fee schedules to cover medical services for hospital providers and physicians are contributing toward our rate increase. Expected medical service utilization increases are also contributing toward our rate increase with new drugs—particularly high-cost specialty drugs to treat breast cancer, high cholesterol, and cystic fibrosis—being one of the key drivers of this increase. BCBSNC efforts to contract with providers for our Blue Select, Blue Value, and Blue Local products will help offset some of these increases for the block overall versus 2015 levels. Furthermore, we expect the risk of our single risk pool to improve relative to 2014 and 2015 as more Small Groups move off of their Grandfathered/Transitional plans. Overall, changes to medical service costs from 2015 to 2016 contribute to 3.6% of our requested rate increase.

New benefits covered, notably Hepatitis-B screenings for at-risk individuals, low-dose aspirin for mothers at risk for preeclampsia, and preventive coverage for certain oral chemotherapy drugs add approximately 0.1%.

Changes in administrative expenses, taxes, and fees are relatively flat as a percent of premium.

We are not requesting any increase in our risk margin or contribution to surplus as a percent of premium in this rate filing, nor do we project to pay Medical Loss Ratio (“MLR”) rebates as a result of the premium rates requested. In other words, we expect to continue to spend over 80% of premium after taxes on qualified medical expenses in 2016 just as we priced in 2015.