Date: April 29, 2010

To: Paul Nerland, Rhonda Sjostrom

From: Gallagher Benefit Services

Re: Shared-Risk Renewal Rating

Background

The San Joaquin Valley Insurance Authority (SJVIA) currently develops medical rates by analyzing the claims experience of each member entity on a stand-alone basis. Claims are then projected and medical inflationary trend factors are applied to determine an overall cost projection for the following Plan Year. While the fixed costs of the SJVIA program (administrative costs, reinsurance, etc) are pooled, the primary driver of the overall plan costs, the member claims, are not pooled. Both the initial rating for the County of Fresno and the County of Tulare (Plan Year 2010) as well as the first renewal cycle (Plan Year 2011) was developed and finalized using this method.

Gallagher Benefit Services has reviewed several methodologies for pooling all entities costs when determining appropriate renewal projections. Among those reviewed were:

Pure Pooling
Pooling of Fixed Costs Components Only
Shared-Risk

Gallagher Benefit Services believes that the Shared-Risk approach will, over time, produce the rate stabilization and smoothing of potential spikes due to excessive utilization that is desirable to the Authority. Further, GBS believes that a Shard-Risk methodology guarantees fairness in rate development and encourages long-term participation in the Program.

Shared-Risk Renewal Rating Methodology

In the shared-risk model, each member entity is evaluated in order to determine their claims experience and plan performance in relation to the overall claims experience of the SJVIA. Once this evaluation of the SJVIA as a whole and the individual entities, adjustments will be made to further decrease (or increase) the premium rate from what the program renewal requires. Public entities that entered the program without any credible claim experience will undergo this assessment after their second year in the SJVIA.

Each year, SJVIA will establish the overall program renewal for the upcoming plan year by aggregating the total plan claims, projecting trended claims, applying fixed costs, adjusting projected reserves and

setting final rates as described above. During the member entities first two renewals, the member entity will receive the overall base pool increase.

When a member entity has been in the program for 2 years (1 year for those entities without claims information) several factors will be evaluated to apply a group-specific adjustment to the overall plan renewal. Initially, the individual entities variance must be identified. After the ***variance*** is calculated, an **adjustment** to the program renewal can be made.

Variance

The individual entity's variance will be the difference between the loss ratio of the individual entity and the loss ratio of the entire program. This variance can be reflected either as a positive number (individual entity has a loss ratio ***greater*** than the entire program) or a negative number (individual entity has a loss ratio ***lower*** than the entire program).

The overall program's loss ratio is established by dividing the incurred claims (less any stop-loss reimbursements) by the total program premiums collected. If the total incurred claims are $70,000,000 and the total program premiums are $100,000,000 than the overall program's loss ratio is 70%.

Next, the individual entities loss ratio is established. Incurred claims for each entity will include an adjustment for large claims using pooling points that are graduated based on group size. This ensures that smaller groups are not overly penalized due to large "shock" claims. This graduated scale suggests recommended pooling points from $100,000 (for groups less than 500 employees) to $450,000 (for groups 3,500 employees and above). Additionally, the three years claims experience is weighted 28% for the first year, 33% for the second year and 39% for the most recent year. This insures that all years in the experience period will have a significant impact on results while providing additional weight to the most recent years. This may positively reflect the impact of any cost management efforts implemented early in the experience period.

Each group's experience will be considered 100% credible for loss ratio determination. This is because the multiple-year experience period increases credibility (i.e., 200 life employer's experience over three years equals 600 Life years) and the pooling mechanism is customized by group size.

Once the loss ratio and variance have been determined, group-specific adjustments will be determined.

Adjustments

At the third renewal (second for manually rated groups), each group may qualify for an adjustment based on their variance. This adjustment will be weighted based on several key underwriting considerations, subject to a minimum and a maximum. The adjustments have been determined based on statistical testing for groups with weights currently existing in the SJVIA program. As membership grows, these weights may change and a re-evaluation of the adjustments, as well as minimum and maximum limits may be changed.

If an entity is determined to warrant an adjustment, that adjustment will be based on the Variance (entity loss ration minus program loss ratio) and the additional group specific weighting factors.