

**BY E-MAIL, FACSIMILE, AND FIRST CLASS MAIL**

June 24, 2011

The Honorable Jerry Brown  
Governor, State of California  
State Capitol  
Sacramento, California 95814

Re: Kaiser Foundation Health Plan Small Group HMO Plan Rate Hikes

Dear Governor Brown,

On July 1, 2011, more than 300,000 Californians enrolled in Kaiser Foundation Health Plan (Kaiser) small group HMO plans and the small businesses that sponsor their coverage are facing rate hikes averaging 10.9%,<sup>1</sup> with increases for some subscribers as high as 17.3%.<sup>2</sup> Kaiser's proposed rate increases affect far more California consumers than any other pending rate hikes under the regulation of the Department of Managed Health Care (DMHC), totaling almost half of all those affected.

We ask that you direct DMHC to exercise all of its statutory authority to investigate the planned rate increases to determine if they are justified and not unreasonable, to make its findings known widely to the general public, and to seek appropriate relief for Kaiser plan participants if it ultimately determines, as we think it should, that these rate hikes are excessive and unnecessary.

Kaiser's filings with DMHC demonstrate significant data deficiencies, and the evidence they do contain makes it hard for anyone to conclude that the rate hikes are justified. These deficiencies include, but are not limited to, the following:

**1. Profitability.** Kaiser's filings are conspicuously silent on issues of the company's overall profitability. It is hard to believe this silence is not intended to divert attention from the nominally non-profit Kaiser's enormous recent profits of more than \$5 billion from January 2009 through March 2011.

**Kaiser's Profitability**

<b>Period</b>	<b>Profits (in millions)</b>
2009	\$2,109
2010	\$1,991
1 <sup>st</sup> Qtr. 2011	\$921
<b>TOTAL</b>	<b>\$5,021</b>

Source: Kaiser Permanente<sup>3</sup>

During the first quarter of 2011, Kaiser recorded the highest profit margin among the ten largest DMHC-regulated health plans in California.<sup>4</sup> Kaiser's profit margin (despite its non-profit status) sharply exceeded those of California's largest for-profit, full-service DMHC-regulated health plans, including Blue Cross, Aetna, United HealthCare, Cigna and Health Net. Kaiser's \$920.5 million in first-quarter profits translates into more than \$10 million in profits per day.

### Profitability of California's 10 Largest HMOs: 1<sup>st</sup> Quarter of 2011<sup>4</sup>

HEALTH PLAN NAME	STATUS	PROFIT MARGIN IN 1 <sup>ST</sup> QTR. 2011	NET INCOME IN 1 <sup>ST</sup> QTR. 2011	NET INCOME IN 2010
Kaiser Foundation Health Plan, Inc	Nonprofit	7.5%	\$920.5 M	\$1,991.3 M
Blue Cross of California	For-Profit	5.3%	\$146.2 M	\$413.6 M
Aetna Health of California, Inc.	For-Profit	5.3%	\$23.5 M	\$55.5 M
United HealthCare of California	For-Profit	5.0%	\$82.2 M	\$310.2 M
Blue Shield of California	Nonprofit	3.6%	\$75.1 M	\$314.8 M
Molina Healthcare of California	For-Profit	2.4%	\$3.2 M	\$14.9 M
Care1st Health Plan	For-Profit	1.3%	\$2.3 M	\$14.8 M
Cigna HealthCare of California, Inc.	For-Profit	1.1%	\$2.4 M	(\$1.4 M)
Health Net of California, Inc.	For-Profit	0.8%	\$19.4 M	\$146.9 M
Heritage Provider Network, Inc.	For-Profit	0.1%	\$0.4 M	\$1.5 M

Source: DMHC

**2. Kaiser's Surplus Condition.** In addition to its surging profits, Kaiser reports extraordinary growth of its excess tangible net equity, which on March 30, 2011 exceeded statutorily required TNE levels by 1,159%, giving Kaiser more than eleven-and-a-half times the legally necessary reserves.

- On December 31, 2010, Kaiser's tangible net equity (TNE) "exceeded the aggregate regulatory minimum requirements by approximately \$12 billion," according to Kaiser's audited financial statement. This figure represents a substantial increase from the year-earlier period, when Kaiser's TNE exceeded the same requirements by \$11 billion.<sup>5</sup>
- Three months later (that is, on March 30, 2011), Kaiser's excess TNE had grown to \$12.675 billion. Kaiser's TNE exceeded its statutorily required level by 1,159%, according to data published by DMHC.<sup>6</sup>
- Additionally, as of December 31, 2010, Kaiser reported that its balance sheet contained \$42.8 billion in total assets and only \$3.8 billion in long-term debt, according to its audited financial statement.<sup>7</sup>

**3. Executive Compensation.** Kaiser fails to address its executive compensation practices, and these practices are arguably more egregious than its profits. According to its tax returns, Kaiser has used its extraordinary profitability to provide record compensation to its top executives.<sup>8</sup>

- In 2009, 14 Kaiser executives received more than \$1 million in compensation.<sup>9</sup>
- As part of their 2009 compensation packages, the top 14 executives received performance bonuses totaling more than \$11 million. What's more, these bonuses are partially tied to Kaiser's profitability, placing them potentially at odds with Kaiser's not-for-profit status.
- In 2009, Kaiser's CEO received \$7.9 million in compensation, including multiple bonuses totaling \$4,054,050.<sup>10</sup>
- Kaiser's top executives currently receive at least eight separate pension, retirement and deferred compensation plans, as well as at least four bonus plans.

- During 2009, Kaiser paid each member of its Board of Directors as much as \$200,000 per year for serving on the board.<sup>11</sup>

**4. Medical Cost Inflation.** Kaiser makes no effort to explain the degree to which its planned increases exceed the rate of medical cost inflation, as reported by the U.S. Bureau of Labor Statistics Consumer Price Index for All Urban Consumers Medical Care Cost Inflation Index. Rather, Kaiser's actuaries boldly assert that measures of past increases in actual costs are not relevant to projecting the future cost increases faced by its plans. In fact, the "CPI-U for U.S. Medical Care" and the "CPI-U for U.S. Medical Care Services" from May 2008 to May 2011 both showed average yearly increases of only 3.2%, less than a third of Kaiser's planned weighted average rate increase of 10.9%.

Additionally, during 2010, Kaiser's self-reported actual costs for providing healthcare services to individuals covered by these plans increased by only 2.0% per member per month, while Kaiser's administrative costs increased by 8.2% per member per month.<sup>12</sup> Furthermore, it appears that Kaiser failed to provide one of the years of historical data on these trends requested by DMHC.

**5. Past Rate Hikes.** Kaiser notes that it has recently increased the premiums of its Small Group HMO subscribers, but fails to provide any historical data regarding the prior increases.

In consideration of all the issues raised above, it is clear that Kaiser's planned rate hikes demand DMHC's full scrutiny. California consumers need DMHC's full protection and advocacy in this matter.

We ask you to see that DMHC act with all deliberate speed to investigate these issues and intervene with Kaiser to protect consumers' interests before the planned July 1 rate hikes, with a level of focus similar to that shown by the Department of Insurance around many of the rate hikes over which it exercises jurisdiction. At minimum, DMHC should ask Kaiser to place a temporary hold on the rate hikes otherwise scheduled for July 1 to prevent consumers from paying excessive premiums before DMHC has had a chance to fully review the proposed increases.

We and California's consumers thank you in advance for your prompt attention to this matter.

Respectfully,



Sal Rosselli  
President, National Union of Healthcare Workers

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<sup>1</sup> Kaiser Foundation Rate Plan, DMHC Rate Filing entitled "SBU HMO Rates July 2011," Exhibit E-1 Attachment 1, Question 13, page 4 of 7.

<sup>2</sup> Kaiser Foundation Rate Plan, DMHC Rate Filing entitled "SBU HMO Rates July 2011," Exhibit E-1 Attachment 4, page 2 of 3. The 17.3% rate hike applies to the July 2011-over-July 2010 increase for the Kaiser insurance product entitled "DHMO 30/1500" in Orange County.

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<sup>3</sup> Annual figures are taken from the audited financial statements of Kaiser Foundation Health Plan & Hospitals. The quarterly figure is reported in at least two separate sites: (a) Kaiser's press release ("Kaiser Foundation Hospitals and Health Plan Report 2011 First Quarter Financial Results") dated 5-6-11 and published on Kaiser's website and (b) data for Kaiser Foundation Health Plan reported on DMHC's website in its "Health Plan Financial Summary Report" for the quarter ended March 31, 2011 (captured at <http://wpso.dmhc.ca.gov/flash/> )

<sup>4</sup> DMHC, "Health Plan Financial Summary Report" for "Full-Service Health Plans" for the Reporting Period January 1 through March 31, 2011. The 10 "largest" full-service plans were selected according to "Total Enrollees." The plans' profit margins were calculated by using figures provided by DMHC and according to the following formula: Profit Margin = ("Net Income-Loss") ÷ ("Total Revenue"). Similarly, the figures for "Net Income in 2010" are taken from "Health Plan Financial Summary Report" for the annual reporting period of 2010. The term "Net Income in 2010" presents DMHC figures reported in the data field labeled "Net Income-Loss." Data were captured in June of 2011 from <http://wpso.dmhc.ca.gov/flash/>

<sup>5</sup> Kaiser Foundation Health Plan & Hospitals, "Combined Financial Statement and Additional Information: December 31, 2010 and 2009," p. 43.

<sup>6</sup> DMHC, "Health Plan Financial Summary Report" for Kaiser Foundation Health Plan, Reporting Period January 1 through March 31, 2011. The figures cited above are reported in the DMHC data fields labeled "Excess TNE" and "% TNE to Required." Data were captured on 6-23-11 from <http://wpso.dmhc.ca.gov/flash/>

<sup>7</sup> Kaiser Foundation Health Plan & Hospitals, "Combined Financial Statement and Additional Information: December 31, 2010 and 2009," p. 2.

<sup>8</sup> Kaiser Foundation Health Plan, IRS Form 990 for 2009, including Schedule J.

<sup>9</sup> Kaiser Foundation Health Plan, IRS Form 990 for 2009, Schedule J Part II ("Officers, Directors, Trustees, Key Employees, and Highest Compensated Employees").

<sup>10</sup> Kaiser Foundation Health Plan, IRS Form 990 for 2009, Schedule J Part II and Part III. Part II indicates that, in 2009, CEO George Halvorson received \$6,667,671 in various forms of compensation, including \$4,054,050 in "Bonus & Incentive Compensation." Part III (Schedule J, Part I, Line 4-B) indicates that Halvorson received an additional \$1,237,500 in "supplemental nonqualified retirement plan payments" in 2009.

<sup>11</sup> Kaiser Foundation Health Plan, IRS Form 990 for 2009, Part VII ("Compensation of Officers, Directors, Trustees...").

<sup>12</sup> Kaiser Foundation Rate Plan, DMHC Rate Filing entitled "SBU HMO Rates July 2011," Exhibit E-1 Attachment 1, Questions 20 and 24, pages 6 of 7 and 7 of 7 of Exhibit E-1.