

Report on the Review of Anthem, Inc.'s Acquisition of Cigna and Affiliates

March 31, 2016



FLORIDA OFFICE OF
INSURANCE REGULATION

Kevin M. McCarty, Insurance Commissioner

Table of Contents

Executive Summary	3
Introduction	4
Methodology.....	5
Current Market Presence in Florida.....	5
Additional Considerations	7
Summary of Findings.....	10
Appendix 1: OIR Data Call.....	11

Executive Summary

The Office of Insurance Regulation (Office) is required by statute to consider the impacts on market structure and competition resulting from proposed mergers between insurance companies operating in the state. This report analyzes the potential market impact in Florida of the proposed acquisition of Cigna Corporation (Cigna) by Anthem, Inc.

The analysis is based on well-recognized methodologies that rely on current and historical data and is used largely to consider the impact of horizontal mergers, where the entities involved in the proposed merger offer the same, or highly substitutable, products. Particular care is taken to ensure that the analysis provides an accurate and appropriate representation of Florida product and geographic markets.

The report finds:

- On the whole, there is no meaningful adverse impacts resulting from the acquisition;
- The companies, individually, or in combination, are an important part, but not a dominant factor in the Florida market, and their combination does not noticeably increase the market concentration across the broadly measured market on a statewide basis;
- The only product market for which Anthem and Cigna currently compete in Florida is the Medicare Advantage market. Analysis in this report suggests that the acquisition will not have a meaningful adverse impact on this market; and,
- The Blue Cross Blue Shield Association (BCBSA) licensing agreement threshold on premium compensation impacts the acquisition on a national level. For the Florida market, it does not appear to be a prohibitively significant adverse factor, even under the assumption that no change to the agreement is reached between Anthem and the BCBSA within two years following the acquisition.

Introduction

The Office is required by statute to consider the impacts on market structure and competition resulting from proposed mergers between insurance companies operating in the state.¹ This report analyzes the potential market impact in Florida of the proposed acquisition of Cigna by Anthem, Inc.²

The analysis and conclusions presented here apply to the potential impact of this proposed acquisition on the Florida health insurance marketplace. While this is a national level merger, the Office has the regulatory responsibility and authority to analyze the effects of the proposed merger on activity within the state. While other states are conducting their own analysis, likely using similar measures and methodologies, the results are likely to be different, in some cases dramatically so, across the states based on the current business models and activity of the two insurance groups. As such, the results and conclusions provided in this report are not, and should not be, directly comparable to the results and findings from other states.

The core of the analysis provided here is based on well-recognized methodologies that rely on current and historical data and is used largely to consider the impact of horizontal mergers, where the entities involved in the proposed merger offer the same, or highly substitutable, products. The veracity of the analysis depends on the accurate representation of product and geographic markets.

This report recognizes that health insurance products are not generally considered close substitutes for one another, but vary considerably in terms of providers, policyholders, and geographic markets. To that end, this report provides results based on careful definitions of product markets, and considers several different definitions of geographic regions.

The focus on the competitive impact resulting from business combinations through acquisition or merger is based on concerns that these combinations can have on output pricing and quantity (e.g., monopoly power) and on input pricing and quantity (e.g., monopsony power). In the health insurance markets, the concerns over the exercise of monopoly power are expressed in terms of the cost and availability of health insurance products to current and potential policyholders. Concerns regarding the exercise of monopsony power are expressed in terms of fee schedules and accessibility for physicians, hospitals, and other medical service providers.

¹ For this merger application, this requirement would be subject to Sections 628.461, F.S.; 628.4615, F.S.; 636.065, F.S.; and 641.255(3), F.S.

² The proposed acquisition will have a direct impact on three Florida based companies: HealthSpring of Florida, Cigna Dental Health of Florida and Cigna Healthcare of Florida.

While these are valid concerns, the current regulatory and legal framework in the health insurance market is designed to address the issues, at least on some level. For major medical policyholders, the Minimum Loss Ratio (MLR) requirement would, all else equal, tend to dampen price (premium) increases. For example, in the individual market if the MLR were to fall below 80% for an insurer, some portion of premium income is rebated back to policyholders. Providers also receive some protection, as the laws require health maintenance organizations and exclusive provider organizations to have an adequate network to ensure access to care for its policyholders.

The focus of the current analysis is on the competitive impact of the proposed merger on the output portion of the market. This is consistent with the Office’s regulatory responsibility regarding market stability, availability, and cost.

Methodology

Current Market Presence in Florida

To assess the economic impact of the proposed acquisition on the Florida marketplace, this analysis begins with measuring the current market footprint of the two entities. Using data collected by the Office in its Major Medical and Medicare (MMMA) data call, the current presence of Anthem and Cigna are first measured on a statewide aggregate basis across these lines of health care insurance business.³ Table 1 summarizes the findings.

Table 1: Florida Enrollment and Premium with Market Shares

	Enrollment	Market Share	Premium	Market Share
Anthem	476,087	5.82%	\$1.64 B	4.40%
Cigna	228,908	2.80%	\$1.52 B	4.10%
Combined Entity	704,995	8.62%	\$3.16 B	8.50%

**Data underlying this table were obtained through the MMMA data call; see footnote 3 below.*

As Table 1 shows, Anthem and Cigna separately are important but not dominant market participants on a broad aggregate basis. When presence is measured by enrollment, Anthem is a larger part of the broad aggregate market (5.82%, compared to Cigna’s 2.8%). Alternatively, when measured by premium, the two are roughly equals (Anthem has 4.4% of the broad aggregate premium, Cigna 4.1%). If

³ The data underlying this report, including product line definitions, were obtained through the Major Medical and Medicare Advantage (MMMA) data call performed by the Office in the fall of 2015. Data were requested at the county level from a constrained list of companies that make up roughly 95% of Florida GAP reported premiums as collected in the *Accident & Health Markets Gross Annual Premium and Enrollment Summary CY 2014 (GAP) Report*.

combined, the new single entity would have 8.62% of the market as measured by enrollment, or 8.5% of the market if measured by premium. Given these market share numbers, there is not *a priori* reason to assume the proposed combination of the two entities would have an adverse effect on the Florida market on a broad, aggregate basis.⁴

The data were next used to calculate the amount of overlap between Anthem and Cigna in specific health insurance product markets within Florida in order to address the more reasonable concern that the acquisition could adversely impact specific markets.⁵ The data are shown in Table 2.

Table 2: Market Impacts of Acquisition in Florida

	Small/Medium Group		Large Group		Individual	
	Enrollment	Premium	Enrollment	Premium	Enrollment	Premium
Anthem	0	0	0	0	0	0
Market Share	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Cigna	33	166,528	137,261	\$571.57 M	42,298	\$173.87 M
Market Share	0.01%	0.01%	10.96%	10.32%	3.32%	3.89%
Combined Entity						
Market Share	0.01%	0.01%	10.96%	10.32%	3.32%	3.89%
	Medicare Adv.		Medicaid		Healthy Kids	
	Enrollment	Premium	Enrollment	Premium	Enrollment	Premium
Anthem	29,975	\$480.28 M	403,717	\$1.08 B	42,395	\$73.41 M
Market Share	2.11%	3.04%	12.82%	16.13%	22.94%	22.72%
Cigna	49,316	\$779.03 M	0	0	0	0
Market Share	3.48%	4.93%	0.00%	0.00%	0.00%	0.00%
Combined Entity						
Market Share	5.59%	7.97%	12.82%	16.13%	22.94%	22.72%

For purposes of this analysis, Table 2 provides a key finding. Whether measured by enrollment or premium, there is only one product market, Medicare Advantage, in which the two entities both have a presence. For all of the other lines of business reported, based on the data available, the proposed acquisition by definition cannot have any impact on the market. In the case of the Medicare Advantage market, the combined entity would have a nonmaterial impact on competition (the combined market share is 5.6% as measured by enrollment and 7.97% as measured by premium).⁶

⁴ The finding is supported by an analysis of the aggregate market using the widely recognized Herfindahl-Hirschman Index (HHI) methodology; the results show no material change in market concentration as a result of the acquisition. Details of the calculation and use of the HHI are widely published; see particularly *Horizontal Merger Guidelines*, U.S. Department of Justice and Federal Trade Commission, Issued August 19, 2010

⁵ See footnote 3 for data definition source.

⁶ An HHI analysis was performed on the Medicare Advantage market, and the results showed no significant increase in market concentration.

Additional Considerations

A thorough evaluation of the competitive impact of the proposed Anthem/Cigna acquisition on the Florida market has to take into consideration activity occurring beyond Florida. Anthem operates in 14 states (but not Florida) as a licensee of the BCBSA. The agreements governing a license from the BCBSA could adversely impact the ability of the combined Anthem/Cigna entity to grow in the Florida marketplace.

Under BCBSA rules, nationally 66 2/3% of the premium generated by a member company must be in their “Blue” business. Using statutory financial statement data for year-end 2014, the Office has estimated the impact of these requirements with results provided in Table 3. In part A of this Table, 79.39% of Anthem premium revenue prior to the acquisition comes from “Blue” branded business. After combining the reported premium revenue of the Anthem and Cigna groups, the Blue percentage drops to 56.08%, below the agreement threshold. One possible course of action proposed in the application is for the combined entity to rebrand its Cigna business as Blue business in those states where Anthem is the BCBSA licensee. Table 3, part B, shows that if this rebranding were completed, the Blue percentage would be 65.06%, still below, but nearing the threshold agreement percentage.

Table 3: Anthem Revenue Shares¹ Before and After Acquisition - Broad A&H

Group	Total Premium	Post-Acquisition Share	Total Premium for BCBS Affiliates	Pre-Acquisition Share of BCBS Affiliates	Total Share Post-Acquisition of BCBS Affiliates
A. Initial Positions					
Anthem	\$56.35 B	70.64%	\$44.74 B	79.39%	56.08%
Cigna	\$23.42 B	29%	-	-	-
Initial Total	\$79.77 B	100%	\$44.74 B	-	56.08%
B. Adjusting for Branding*					
Cigna in Anthem Blue States	\$7.16 B	8.97%	-	-	-
Adjusted Anthem	\$63.51 B	79.61%	\$51.9 B	-	65.06%
Adjusted Cigna	\$16.26 B	20.39%	-	-	-
Adjusted Total	\$79.77 B	100%	\$51.9 B	-	65.06%

1. Data are from Statutory Financial Statements filed with the NAIC, Schedule T and the Supplemental Health Care Exhibit 2014. *Adjustments assume Cigna rebranding in states where Anthem is the designated BCBSA affiliate.

The potential impact of the national BCBSA thresholds on Cigna business in Florida, were considered within the context of the overall combined Anthem/Cigna entity on a national basis. Based on year-end 2014 annual statement data, Cigna’s premium revenue in Florida was 2.9% of the overall combined Anthem/Cigna premium

revenue. Given that this is such a small portion of the combined entity's premium revenue, it is unlikely the BCBSA agreement threshold would have a substantial impact on the Florida Cigna business, or its ability to grow. As evidence, Table 4 estimates the impact on the combined entity's threshold ratio under varying assumed growth rates in Florida Cigna business.

Table 4: Impact of Cigna Growth in Florida on National Anthem as Blue Ratio*

Rate of Increase	FL Premium ¹	% of Anthem Nationally	Anthem-Blue Ratio	% Change Anthem-Blue Ratio
Current	\$2.33 B	2.9%	65.1%	-
10%	\$2.56 B	3.2%	64.9%	-0.29%
20%	\$2.79 B	3.5%	64.7%	-0.58%
30%	\$3.02 B	3.8%	64.5%	-0.87%
40%	\$3.26 B	4.1%	64.3%	-1.15%
50%	\$3.49 B	4.4%	64.1%	-1.44%
100%	\$4.65 B	5.8%	63.2%	-2.83%

**Assuming re-branding of Cigna business in states where Anthem is the BCBSA affiliate.*

If Cigna's Florida business were to double, the impact on the combined entity's BCBSA threshold would be lowered from 65.1% to 63.2%, less than a 3% drop. Cigna's Florida business has grown by about 26% over the last five years. Using this as an estimate, the combined entity's threshold ratio would drop by less than 1%, as shown in Table 4, from 65.1% to somewhere between 64.5 and 65.7%. It is also important to note that the calculations in Table 4 assume Anthem's Blue branded premium, on a national level, does not increase at all.

A slightly different view of the competitive impact of the BCBSA threshold on Cigna business in Florida was estimated under the assumption that that the existing combined entity's distribution of business would not allow Cigna to grow in Florida. The impact on the Florida market is shown in Table 5 (next page) where the existing Cigna business is measured in each of the relevant geographic markets (the Metropolitan Statistical Area (MSA)) it currently serves.

As Table 5 shows, the Cigna business is not the dominant part of the market in any of Florida's MSAs (to also include the nonurban counties not included in the MSA definitions but grouped here as Northwest, North, and South). Not only are the market share percentages modest, there is no MSA where Cigna would be one of the four largest market providers. As such, there does not appear to be a meaningful adverse competitive effect as a result of the proposed acquisition, even under the most conservative estimation.

Table 5: Cigna* Market Share by MSA**

MSA Name	Market Share
Pensacola-Ferry Pass-Brent, FL	2.92%
Crestview-Ft Walton Beach-Destin	1.06%
Panama City-Lynn Haven-Panama City Beach	1.66%
Tallahassee	0.54%
Jacksonville	1.21%
Gainesville	0.99%
Palm Coast	2.20%
Ocala	0.45%
Deltona-Daytona Beach-Ormond Beach	2.26%
Orlando-Kissimmee-Sanford	4.50%
Palm Bay-Melbourne-Titusville	3.96%
Sebastian-Vero Beach	3.41%
Tampa-St. Petersburg-Clearwater	1.71%
Lakeland-Winter Haven	1.20%
Punta Gorda	1.43%
Port St. Lucie	2.86%
Cape Coral-Ft. Myers	2.72%
Naples-Marco Island	1.47%
Miami-Ft Lauderdale-Pompano Beach	3.47%
North Port-Bradenton-Sarasota	2.02%
Northwest	2.41%
North	0.76%
South	6.55%
Statewide	4.10%

**In reference to Cigna, this dataset represent roughly \$1.6B of their total statewide premium for 2014.*

***The data underlying these market shares are from the MMA data call conducted by the OIR in the fall of 2015. It is of a constrained sample of companies and in no way represents the broad definition of A&H used elsewhere in this workbook. Instead it covers only comprehensive lines of business listed in the table below.*

The existence of the BCBSA threshold premium ratio complicates the analysis for any particular state. Anthem and the BCBSA have over two years to work out this issue and there are any number of ways, impacting any or some combination of the applicable states, to achieve a satisfactory agreement consistent with Anthem's overall business model and strategic plan. Anecdotal evidence suggests that Anthem's BCBSA business is 25% or more of the overall Blue business, so there is some significant level of market power available to Anthem in this discussion.

Summary of Findings

This report has analyzed the competitive impact of the proposed Anthem acquisition of Cigna on the Florida health insurance market. The companies, individually, or in combination, are an important part, but not a dominant factor in the Florida market, and their combination does not noticeably increase the market concentration across the broadly-measured market on a statewide basis. Moreover, the only product market for which Anthem and Cigna currently compete in Florida is the Medicare Advantage market. On the whole, this report finds no meaningful adverse impacts resulting from the acquisition.

The BCBSA threshold on premium compensation impacts the acquisition on a national level. For the Florida market, it does not appear to be a prohibitively significant adverse factor, even under the assumption that no change to the agreement is reached between Anthem and BCBSA over the next two years.

Appendix 1: OIR Data Call

The data underlying this report were obtained through the Major Medical and Medicare Advantage (MMMA) data call performed by the Office of Insurance Regulation in the fall of 2015. Data were requested at the county level from a constrained list of companies that make up roughly 95% of Florida GAP reported premiums as collected in the *Accident & Health Markets Gross Annual Premium and Enrollment Summary Report CY 2014* (GAP). While constrained by design, the scope and breadth of business represented in the data call is sufficient to draw meaningful insights as to the competitive effects on the Florida market resulting from the proposed merger of Cigna and its affiliates by Anthem, Inc.

A copy of the data call template appears on the next page.



FLORIDA OFFICE OF INSURANCE REGULATION

Kevin M. McCarty, Insurance Commissioner

200 E. Gaines Street – Tallahassee, Florida 32399

Phone: (850) 413-3140

www.floir.com