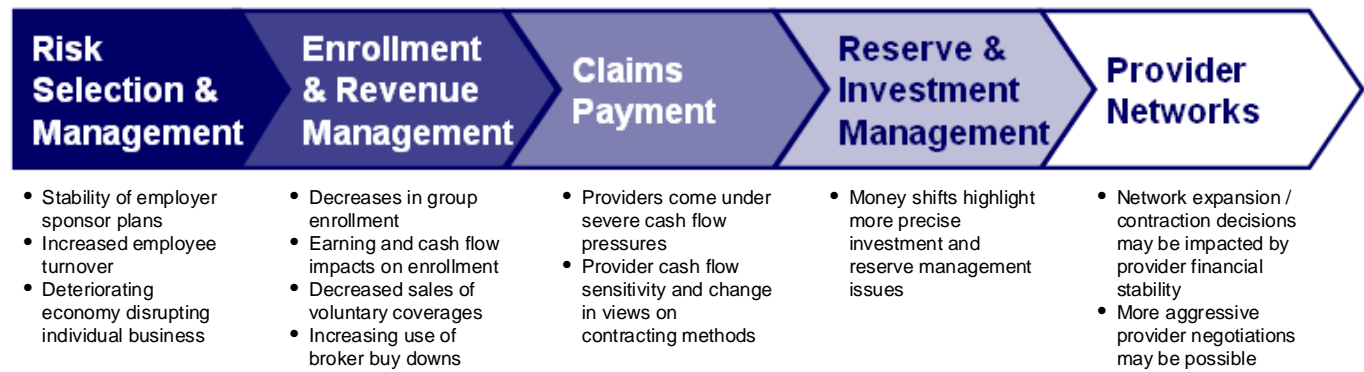


ROBERT E. NOLAN COMPANY

**Responding to the Financial Crisis
Today's High Priority Health Care Issues**

Strategy	<ul style="list-style-type: none"> • Liquidity and credit crisis reactions • Competitor impacts • Product and segment impacts 	<ul style="list-style-type: none"> • Regulatory response • Customer concerns and confusion
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ASO Products	<ul style="list-style-type: none"> • Declining business and cash flows reduce ASO client financial strength • Declining ability to make funding calls 	<ul style="list-style-type: none"> • Increased interest in alternative funding arrangements to maintain benefits
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Operations and Financial Management	<ul style="list-style-type: none"> • Operational effectiveness becomes more important in uncertain times • Expense issues addressing internal liquidity issues • Vendors potentially become unstable 	<ul style="list-style-type: none"> • Unknown international currency risk in operations or investment portfolio
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View an electronic version at: www.renolan.com/healthcare/financial_crisis.pdf

STRATEGY		
IMPACT	IMPLICATIONS	INITIATIVES
The liquidity and credit crisis, and reactions to them, have changed our environment.	If environment changes, is current strategy appropriate?	Rescan environment to determine if strategy remains sound and appropriate.
		Place priority to elements of strategy that require capital or where rapid growth was expected.
The impacts of liquidity and credit crises has different impacts on different players in our markets.	Among our competitors, who is now stronger? Who is now weaker?	Assign cross-functional teams to develop competitor-specific modification of strategies. Key effect to achieve is to flex our activities to reflect them as they are now rather than as they were when the strategy was developed.
	If we are strong, who can we buy now?	Increase staff allocation to corporate development and strategy efforts. Establish / modify due diligence capability to support quick response efforts. Renew / revise contacts and relationships with professional service firms used in M&A activities such as investment bankers, accountants, consultants, and law firms. Signal interest in acquiring distressed firms.
	If we are weak, who may be interested in us? What can we do to obtain the best outcome if there is a move on us?	Determine what are critical actions that would increase sale price. Assemble team to prepare pre-work for offer package. Anticipate due diligence process needs. Create specific actions to increase / conserve cash flow and improve RBC reserve needs.
The impacts of liquidity and credit crises has different impacts on different products and segments.	What products and markets are more attractive? Which ones are less?	Assign cross-functional teams to develop product-specific modification of strategies. Key effect to achieve is to flex our activities to target product opportunities as they exist now rather than as they were when the strategy was developed.
Regulatory response.	Expect increased reporting requirements.	No immediate actions required.
	Expect intense pressure if claims are delayed.	Review claims payment processes and alternative funding administration.
	Expect changes in reserving and reserve investment policy.	No actions required currently.
	Localities are facing lower revenue receipts and may try to attack reserves by demanding more money be directed to the locality (i.e. DC versus CareFirst - DC says reserves are too high and want a bigger share).	Review legal options and reserve requirements. Prepare a defense contingency.

STRATEGY		
IMPACT	IMPLICATIONS	INITIATIVES
Customers (benefit program sponsors and members) are confused and concerned.	Understandable, specific, and continuous communication may be required to reduce fear.	Review issue with cross functional team including customer service, sales team, and select brokers. Determine concerns, craft product specific messages to address issues. Anticipate need to send same content via different communications channels multiple times before messages are received and understood.

RISK SELECTION AND RISK MANAGEMENT		
IMPACT	IMPLICATIONS	INITIATIVES
Liquidity and credit issues impact employer sponsors in different ways. Clients that may have been stable or attractive may not be good risks in future.	Risk selection now needs to reflect financial stability and credit worthiness.	Underwrite groups for credit worthiness; include payment history as an element of underwriting. Assess industry groups, too, for changes in stability and employee turnover. Be prepared to modify industry loads.
Industries and firms that have increased risk of employee turnover may be less attractive.	Shift in age-sex mix within groups may lead to higher medical loss ratios.	Assess risk of excess turnover and lay offs for new group. Reflect risk in rate factors.
Deteriorating economy may disrupt individual business.	Individual members' ability and willingness to pay premium may become a problem.	Modify individual product reinstatement offer to reflect payment history of insured.
	Health care cost trends are rising in a down economy, which will result in increased premiums and pressure on a business.	Intensify review of medical policy, costs, and establish remediation strategies now.

ENROLLMENT AND REVENUE PROCESSING

IMPACT	IMPLICATIONS	INITIATIVES
Reduced economic activity decreases enrollment within groups.	Membership and revenue budgets may not be met.	Establish monitoring system to anticipate / track economic and employment trends and their impact on budgets.
	Increased enrollment and revenue processing and reconciliation.	Review and validate processes and controls for revenue processing. Assess staffing levels to allow timely processing and collection of funds due.
	Dis-enrolled members may change age-sex factors and medical loss ratio.	Monitor block of business for shifts in age-sex and unanticipated MLR shifts. Communicate impact and implication to sales staff and brokers. If justified, initiate early rating actions on select groups.
Deteriorated earnings and cash flow decreases enrollment within groups.	Delayed premium payment.	Proactively communicate receivables policy to sales team and brokers. Retrain staff on application of policy.
	Carrier may become lender to groups without compensation or security.	Assess credit status and payment history of block and determine which groups will not be extended pay extensions. Selectively offer ASO products to groups with financial difficulties. Propose benefit buy down or reduced program to maintain benefit offering within the group. Reduce employer contribution.
Decreased revenue and sales of voluntary or discretionary coverages.	Ancillary product sales budget many not be met.	Revise ancillary sales targets and activities. Consider revising benefits to maintain ancillary coverage in place.
Increasing use of benefit buy downs by brokers or employees within groups.	Although groups are maintained, revenue yield PMPM may be low pricing assumptions.	Monitor extent of buy downs on total block revenue.
		If necessary, recast revenue and expense budget to reflect impact of buy downs.
		Train sales staff on issue and counter tactics.

RESERVE AND INVESTMENT INCOME

IMPACT	IMPLICATIONS	INITIATIVES
As money moves differently in the economy, reserve issues become more important.	Are our current reserves adequate in this environment?	Review reserve methods.
		Review assumptions used in reserve methods.
		Review sensitivity of reserving to changes in member and provider behaviors such as increased submission of discretionary claims by members anticipating lay off. Review reserve methods with appropriate Board of Directors governance group.
	Are reserves invested appropriately?	Review investment policy with appropriate Board of Directors governance group. Assure investment managers are investing in accordance with policy.
		Consider diversification among group of investment managers. Critically review portfolio duration. Critically review use of non-US investments in portfolios.

CLAIMS PAYMENT

IMPACT	IMPLICATIONS	INITIATIVES
Provider organizations' economics come under severe cash flow pressure.	Balancing cash flow with claims service becomes more challenging.	Monitor claims "pipeline" and link to three-day cash flow model. Consider daily check runs to relieve provider cash flow issues.
	Increasing demand and pressure for prompt payment and increased reimbursement.	Anticipate intense pressure concerning payment cycle from providers with liquidity or credit problems. Anticipate "firmer" negotiating positions during provider contract negotiations. Expect greater regulatory monitoring of quick payment rules.
Provider cash flow sensitivity may change their attitude towards contracting methods.	Capitation and case rates may become more attractive.	Selectively include capitation in provider negotiations. Offer more than one reimbursement method, when possible.

ASO PRODUCTS		
IMPACT	IMPLICATIONS	INITIATIVES
Declining business activity and cash flows reduce ASO clients' financial strength and ability to self fund claims.	What may have been an appropriate product for a specific client may no longer be appropriate.	Retrain sales and service staff to understand alternative funding products and employer responsibility to directly fund claims.
		Review credit status (D&B, etc.) of current ASO clients.
		For ASO clients with poor credit and poor funding history, develop client-specific approach to assure their ability to fund benefits.
		Offer lower reinsurance attachment points.
		Review current claims and disbursement processes to assure that claims are properly funded and plan is not funding employer liabilities.
Declining ability to respond to funding calls.	Member claims are not paid; providers are not paid.	Retrain sales and service staff to understand alternative funding products and employer sponsor to directly fund claims.
		Review and revise claims and customer service procedures used in event of non-funding.
		Prepare brokers and benefit consultants for what will happen if claims are not funded.
Many firms may become more interested in alternative funding arrangements as a means of maintaining benefit programs even while they struggle with intense credit and liquidity problems in their businesses.	A number of firms newly interested in alternative funding do not have financial strengths or discipline sufficient for the successful operation of these programs.	Establish strong leadership over ASO sales and administration. Review and revise materials used with potential clients to correctly explain the employer funding responsibilities. Retain sales and service staff to assure that concepts are correctly sold and administered.
		Prepare sales methods to move selected clients from fully funded to alternative funding. Make these products available to clients with liquidity but not credit problems.
		Review and revise underwriting methods to include credit underwriting of prospects.
		Make selective use of Letters of Credits for marginal risks.
		Prepare specific benefit designs that can help minimize employer funding needs: higher dollars, individual accounts, etc.
		Use lower reinsurance limits to reduce employer funding requirements.

PROVIDER NETWORKS		
IMPACT	IMPLICATIONS	INITIATIVES
Many providers have weak liquidity and credit positions.	Negotiations may be more difficult than normal.	Better preparation of negotiation team may be required. Anticipate service and cycle time issues to become enmeshed in the financial negotiation.
	Payer negotiation positions may be stronger than normal.	Negotiators should push for more favorable rates, concessions, and terms. However, pushing too hard may contribute to provider instability or deteriorate long-term relationships.
		Opportunity to expand or prune networks may have changed, which creates a stronger negotiating position.
	Some providers, especially facilities, may experience severe credit / liquidity problems.	Monitoring provider finances and operations can help anticipate these problem situations.

GENERAL OPERATIONAL - FINANCIAL MANAGEMENT

IMPACT	IMPLICATIONS	INITIATIVES
Operational effectiveness becomes more important in uncertain times.	Better balancing of expenses against volumes can improve financial results.	Review current operations and budgets to find areas of mismatch between volumes and operating expenses.
		Review mismatch areas with accountable executives.
		Assist accountable executives with preparing improvements in mismatches.
		Monitor improvement.
		Prepare a limited number of scenarios and contingencies. Discuss these with accountable executives and their financial staffs. Having discussed how we might reduce Department X's expenses by 8% if required by external events helps prepare Department X for successful implementation.
Labor mix for operations will change as service mix and financial results change.		Review current transaction and inquiry volumes against budgets.
		Review staffing (permanent, temp, overtime) against operational needs.
		Establish / maintain control over labor costs via increased controls to hire.
		Be prepared to shift labor to areas experiencing increased transaction and inquiry volumes.
		Make selective use of new technologies, process improvements, or specialty vendors, where there is a high probability of net economic effects within current financial period.
Availability of capital may require rethinking of current capital programs.		Conduct systematic capital review against newly established criteria. Use triage categories of Mandated, Needed, Can Be Deferred, No Longer Appropriate.
		For each project that survives capital review, review project to determine if capital or expense budget for project can be reduced or rescheduled to minimize financial requirements.
		Review current projects and vendor contracts to obtain cost or schedule concessions.
More aggressive management of fixed expenses can be critically important in uncertain times.		Create and maintain schedule of all fixed expenses. Scheduling these expenses supports better management and allows time to rebid or revise them.
		Establish within finance area ownership of fixed cost issue.
		Review and revise procedures and methods for managing fixed expenses.
Carriers may have their own liquidity issues.	Treasury operations become more important.	Review department including staffing, skills, budget, and control environment.
		Improve three-day forecasting of cash position.

GENERAL OPERATIONAL - FINANCIAL MANAGEMENT

IMPACT	IMPLICATIONS	INITIATIVES
		<p>Review revenue processing processes and controls to improve operations-treasury linkage. Critical issue is unintended extension of credit to slow or no pay clients.</p> <p>Review claims payment cycle with emphasis on metrics and controls that are required to improve operations-treasury linkage.</p> <p>Review capitation cycle with emphasis on metrics and controls to improve operations-treasury linkage. Critical issues are payment of cap without corresponding premium and reconciliation and correction of capitation errors.</p> <p>Review non-product receivables processing and controls.</p> <p>Review trade payables processing and controls.</p>
<p>Vendors may become unstable.</p>	<p>Non-viable vendors may be embedded in key service processes and enterprise infrastructure</p>	<p>Assess key service processes and enterprise infrastructure to inventory critical vendors.</p> <p>Conduct credit review of critical vendors to assess vendor viability if their cash flow is disrupted.</p> <p>Assess vendor client base to assure adequate cash flow to maintain vendor viability.</p> <p>If substantial risk of viability is present in a key service process or enterprise infrastructure, selectively rebid relationship to remove incumbent or diversify risk across more than one vendor. Also consider insourcing of vended functions as a risk reduction technique.</p>
<p>Carriers may have unknown international currency risk in operational environment or investment portfolio.</p>	<p>Unknown risks cannot be managed.</p>	<p>Review key vendor relationships to determine if currency risk exists. If so, reduce risk by restating to US currency or consider hedge.</p> <p>Review key customer relationships to determine if currency risk exists. If so, explore methods of reducing or hedging.</p> <p>Review international investment exposure with investment managers. Assure that investments are consistent with board approved policy and investment strategy of investment firm.</p>