



allowed per claim that the State of Alaska and their members will pay for prescription drugs in various settings (retail/mail, brand or generic).

Aetna Rx Claim Cost (Exhibit 4, Page 2 of 3)

Aetna Rx Claim Costs are derived from the base data from Exhibit 4, Page 1 of 3 and the reported discounts and dispensing fees in Aetna's BAFO, dated 2/28/2006. Although Aetna only reported discounts and dispensing fees for the first contract period (7/06 to 6/07), I assumed that those discounts and dispensing fees would hold for the two remaining contract periods – 7/07 to 6/08 and 7/08 to 6/09. The same assumption was also used in the Premera Rx Claim Cost projection.

Additionally, as with the medical claim cost projection, I assumed that the members would be responsible for 10% of the allowed amount (AWP amount less the discount). The 10% is an estimate of what members would be pay in copays, coinsurance, and deductibles, if any. The same 10% member responsibility assumption is also used in the Premera Rx Claim Cost projection.

Premera Rx Claim Cost (Exhibit 4, Page 3 of 3)

Premera Rx Claim Costs are derived from the base data from Exhibit 4, Page 1 of 3. The reported discounts and dispensing fees come from the Premera Medco (PBM vendor) contract. As with the Aetna Rx Claim Cost projection, I assumed that the Premera discounts would hold constant over the three-year contract period.

Additionally, as with the medical claim cost projection, I assumed that the members would be responsible for 10% of the allowed amount (AWP amount less the discount). The 10% is an estimate of what members would be pay in copays, coinsurance, and deductibles, if any. The same 10% member responsibility assumption is also used in the Aetna Rx Claim Cost projection.

The aggregate Rx claims impact comparing the Premera and Aetna discounts, dispensing fees, and charges for paper claim submissions (if any) is an estimated savings to the State of Alaska of 1.5M by choosing Premera. The direct Rx cost comparison is made possible by using the same Base Rx Claim Cost Data as described above.

Aetna Rx Rebates (Exhibit 4, Page 2 of 3)

Aetna Rx Rebates are guaranteed (as reported in Aetna's BAFO, dated 2/28/2006) at the greater of 13.3% of manufacturer rebates or 750,000 per year. Because the Rx claim count estimates in the 7/07 to 6/08 and 7/08 to 6/09 contract years produce rebate amounts of less than 750,000 per year, the rebate amount was set equal to 750,000.

Note: Rx claim counts used to calculate rebate amounts are obtained from the Mike Wiggins's March 10th Affidavit – Exhibit 1.

Premera Rx Rebates (Exhibit 4, Page 2 of 3)

Premera Rx Rebates are guaranteed (as reported in Premera's BAFO, dated 2/28/2006). The guarantee is a minimum of 3.0M dollars a year, contingent upon generating an average paid claims volume of at least 80,000 claims per month over any of the three contract years.

Based on Rx claim counts, the total Rx rebate credit is expected to be 10.1M versus the Aetna guarantee of 2.3M for a net savings to the State of Alaska of 7.8M over the course of the contract.

Note: Rx claim counts used to calculate rebate amounts are obtained from the Mike Wiggins's March 10th Affidavit – Exhibit 1.

Claims Runout Processing Fee (Exhibit 5, Page 1 of 1)

Aetna contends that its proposed fee for administration of claims following termination of the contract ("Runout Fee") is more than 2.0M less than the comparable fee for Premera. In reality, Premera's Runout Fee is significantly less than that of Aetna.

Aetna estimates its Runout Fee to be 2.6M and states that "the Premera fee will be almost 5.0M". (McGuinness Affidavit, paragraph 26.). Matt McGuinness provides no explanation for how he arrived at the 5.0M calculation. In fact, it is likely that the Premera Runout Fee will be close to 2.05M.

The State's contract with Premera provides that the State will pay Premera an administrative fee of 4.0% of eligible claims paid after the date of the contract termination. (Contract between the State and Premera, page 5.) Runout Claims are claims for medical and pharmacy services which were provided before a contract was terminated, but which were not received and/or processed by the administrator prior to the termination of the contract. To project the claims runout processing fee for the State of Alaska, I analyzed our claims payment history for Premera's group commercial business in the state of Alaska. For each of the last 33 months, I ran a computer-generated history that showed what volume of claims was paid following the end the month, thereby approximating a claims runout process. On average for those 33 months, Premera paid medical claims equivalent to 1.96 months worth of claims. For pharmacy claims, the claims equivalent is 0.58 months worth of claims.

Additionally, to better approximate the claims runout process for what the State of Alaska may experience (The State has a substantial number of retirees, which requires claims coordination with Medicare), I also analyzed Premera's claims processing for Medicare Supplement business. Coordination of benefits with Medicare adds additional time to the process, thus Medicare Supplement claims take longer to process. For the Medicare Supplement business, Premera pays claims runout over 2.05 months on average (slightly higher than the 1.96 months in the Premera group commercial Alaska business).

Finally, to estimate the 2.05M Premera claims runout processing fee shown on Exhibit 5, I used the longer (Medicare Supplement) period rather than the shorter Commercial period, recognizing that this produces a more conservative estimate for the fee. The projected runout processing fee was then calculated by multiplying the foregoing number of months for each of the medical and pharmacy claims by the average monthly claims volume for the third year of the contract (23.4M and 5.9M respectively), and totaling those. That number was then multiplied by the 4% Runout Fee to product the projected cost to the State of 2.05M, which is significantly less than Aetna's own projection of its termination fees - 2.6M.

**State of Alaska
Total Cost Comparison
Premera vs. Aetna**

	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09	Total	Difference
Employees					
Active	5,464	5,519	5,574		
Retiree	29,128	29,394	29,982		
Total	33,592	34,913	35,556		
Aetna					
Administration Fee ⁽¹⁾	7,203,823	12,011,706	12,839,123	32,054,652	
Medical Claim Cost ^{(9), (10), (11), (12), (13), (14)}	233,599,109	258,604,608	280,686,001	772,889,718	
Medical Shared Savings Fee ⁽²⁾	1,133,709	1,133,709	1,133,709	3,401,128	
Rx Claim Cost ^{(3), (12)}	66,832,747	66,199,894	71,374,530	204,407,171	
Rx Rebates ⁽⁴⁾	(762,107)	(750,000)	(750,000)	(2,262,107)	
Total	308,007,281	337,199,917	365,283,364	1,010,490,562	
Premera					
Administration Fee ⁽⁵⁾	8,190,903	10,990,649	11,769,483	30,951,035	1,103,617
Medical Claim Cost ^{(9), (10), (11), (12), (13), (14)}	233,614,981	258,600,267	280,674,470	772,889,718	0
Medical Shared Savings Fee ⁽⁶⁾	170,799	1,015,328	1,946,015	3,132,143	268,985
Rx Claim Cost ^{(7), (12)}	66,318,454	65,714,881	70,877,783	202,911,119	1,496,053
Rx Rebates ⁽⁸⁾	(3,303,187)	(3,339,405)	(3,438,189)	(10,080,780)	7,818,675
Total	304,991,950	332,981,721	361,829,563	999,803,234	10,687,328
Difference	3,015,330	4,218,196	3,453,801	10,687,328	

Notes and Assumptions

- 1) Aetna Administration Fee - From Section 7.23 - Cost Proposal (All Services) - BAFO, Dated 2/28/2006.
- 2) Aetna Shared Savings Fee - From Matt McGuinness Affidavit, Page 7 of 8, Dated 3/28/2006.
- 3) Aetna Rx Claim Cost - Estimated based on information from Aetna 12/28/2005 Bid and From Section 7.23 Cost Proposal (All Services) - BAFO, Dated 2/28/2006.
- 4) Aetna Rx Rebates - From Section 7.23 - Cost Proposal (All Services) - BAFO, Dated 2/28/2006. Rx script count estimates from Mike Wiggins' March 10th Affidavit - Exhibit 1.
- 5) Premera Administration Fee - From Section 7.23 - Cost Proposal (All Services) - BAFO, Dated 2/28/2006.
- 6) Premera Shared Savings Fee - Calculated from Premera BAFO, Dated 2/28/2006. To the extent that the PEPM Savings are less than 100.0 PEPM, Premera will reimburse the State of Alaska 30% of the difference between the actual savings and 100.0 PEPM.
- 7) Premera Rx Claim Cost - Estimated based on information from Premera's Medco (PBM vendor) contract.
- 8) Premera Rx Rebates - From Premera BAFO, Dated 2/28/2006. Rx script count estimates From Mike Wiggins' March 10th Affidavit - Exhibit 1.

**State of Alaska
Total Cost Comparison
Premera vs. Aetna**

Medical Claim Cost - Notes

- 9) Medical claims are assumed to be the same between Aetna and Premera. Also, assumes that for Dental, LTC, and FSA costs beyond administration fees are the same between Aetna and Premera.
- 10) Medical Future Savings - Assumes that provider discounts will stay at the Aetna 2005 levels - 13.6%. The future PEPM savings are 101.46, 108.07, and 115.17 over the the future policy periods of 7/03 to 6/07, 7/07 to 6/08, and 7/08 to 7/09, respectively.
- 11) Medical Past Savings - The past savings are 71.41, 73.90, and 91.91 PEPM for calendar years 2003, 2004, and 2005 respectively. Savings are assumed to be as reported in Aetna's 12/28/2005 Bid, Page 2 of 7.
- 12) Assumes that for both Medical and Rx, the member will pay 10% of the provider allowed amount.
- 13) Claims Trend - Trend in billed claims assumed to be 6.6% per annum or the difference in billed amounts from 2003 to 2004.
- 14) Provider Discount - The network discount is assumed to grow 0.0% per annum. The discount is assumed to be the same as the 2005 discount of 13.6%.

State of Alaska
Administration Fee
Section 7.23 - Cost Proposal
All Services - BAFO, Dated 2/28/2006

	# of Lives	Aetna		Premera	
		Year 1	Annual Dollars	Year 1	Annual Dollars
Per employee per month medical	5,464	24.16	1,583,892	24.79	1,625,431
Per retiree per month medical	28,128	14.62	4,933,586	16.95	5,721,235
Per retiree per month DVA	20,725	2.21	549,627	2.78	691,386
Per retiree per month LTC	19,011	0.39	88,971	0.42	95,815
Per participant per month Health FSA	1,358	2.93	47,747	3.50	57,036
			7,203,823		8,190,903
	# of Lives	Year 2	Annual Dollars	Year 2	Annual Dollars
Per employee per month medical	5,519	37.44	2,479,315	32.16	2,129,892
Per retiree per month medical	29,394	24.18	8,527,573	22.00	7,760,016
Per retiree per month DVA	21,658	3.09	803,079	3.61	938,225
Per retiree per month LTC	19,866	0.57	135,883	0.44	104,892
Per participant per month Health FSA	1,372	4.00	65,856	3.50	57,624
			12,011,706		10,990,649
	# of Lives	Year 3	Annual Dollars	Year 3	Annual Dollars
Per employee per month medical	5,574	38.68	2,587,131	33.77	2,258,808
Per retiree per month medical	29,982	25.42	9,146,052	23.10	8,311,010
Per retiree per month DVA	22,633	3.24	879,971	3.79	1,029,349
Per retiree per month LTC	20,760	0.63	156,946	0.45	112,104
Per participant per month Health FSA	1,386	4.15	69,023	3.50	58,212
			12,839,123		11,769,483
Grand Total (Years 1-3)			32,054,652		30,951,035

**State of Alaska
Aetna Medical Claim Costs and Savings**

Aetna Estimates

Active

	2003	2004	YTD2005 (6)	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	5,874	5,535	5,558	5,464	5,519	5,574
Members	14,884	14,811	14,049	14,097	14,239	14,381
Medical Claim Dollars	36,452,662	37,153,083	29,533,843	43,489,007	46,825,929	50,413,888

PMPM

Paid	204.09	211.90	233.58	257.08	274.05	292.13
Allowed (1), (5)	226.77	235.45	259.53	285.64	304.50	324.59
Billed (2), (4)	257.33	268.71	300.42	330.65	352.48	375.74
Savings (3)	30.56	33.27	40.89	45.01	47.98	51.15
Savings Dollars	5,458,978	5,832,526	6,894,184	7,613,838	8,198,050	8,826,212
Discount (5)	11.9%	12.4%	13.6%	13.6%	13.6%	13.6%

Retiree

	2003	2004	YTD2005 (6)	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	25,350	26,880	27,800	28,128	29,394	29,982
Members	48,838	51,343	52,573	53,162	55,555	56,666
Medical Claim Dollars	140,502,716	157,131,257	128,112,868	190,110,102	211,778,679	230,272,115

PMPM

Paid	240.72	255.04	270.76	298.00	317.67	338.64
Allowed (1), (5)	267.47	283.37	300.85	331.12	352.97	376.27
Billed (2), (4)	303.52	323.41	348.25	383.29	408.59	435.55
Savings (3)	36.05	40.04	47.40	52.17	55.62	59.29
Savings Dollars	21,041,022	24,667,474	29,905,816	33,283,529	37,077,155	40,314,894
Discount (5)	11.9%	12.4%	13.6%	13.6%	13.6%	13.6%

Total

Medical Claim Dollars	176,955,378	194,284,320	157,646,711	233,599,109	258,604,608	280,686,001
Savings Dollars	26,500,000	30,500,000	36,800,000	40,897,367	45,275,205	49,141,105
Savings PMPM	71.41	78.90	91.91	101.46	108.07	115.17

Notes

Shaded Numbers - Shaded areas represent numbers obtained during the bid process and Aetna's bid, dated 12/28/2005.

- 1) Allowed PMPM - Assumed to be 10% higher than Paid PMPM. The member would be responsible for amounts between the Allowed and Paid PMPM.
- 2) Billed PMPM - Estimated based on reported savings from the Aetna 12/28/2005 Bid, Page 2 of 7.
- 3) Savings = Difference between the Billed and Allowed amounts
- 4) Claims Trend - Trend in billed claims assumed to be 6.6% per annum or the difference in billed amounts from 2003 to 2004.
- 5) Discount - The network discount is assumed to grow 0.0% per annum. The discount is assumed to be the same as the 2005 discount of 13.6%.
- 6) YTD2005 - Information shown above has been extrapolated to produce estimated 2005 results

State of Alaska
Premera Medical Claim Costs and Savings

Premera Estimates

Active

	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	5,464	5,519	5,574
Members	14,097	14,239	14,381
Medical Claim Dollars	44,080,204	47,462,488	51,099,221

PMPM

Paid	260.57	277.77	296.11
Allowed ^{(1), (4)}	289.53	308.64	329.01
Billed ⁽²⁾	330.65	352.48	375.74
Savings ⁽³⁾	41.13	43.84	46.73
Savings Dollars	6,956,953	7,490,762	8,064,728
Discount ⁽⁴⁾	12.4%	12.4%	12.4%

Retiree

	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	28,128	29,394	29,982
Members	53,162	55,555	56,666
Medical Claim Dollars	189,534,777	211,137,779	229,575,249

PMPM

Paid	297.10	316.71	337.61
Allowed ^{(1), (4)}	330.11	351.90	375.13
Billed ⁽²⁾	383.29	408.59	435.55
Savings ⁽³⁾	53.18	56.68	60.43
Savings Dollars	33,922,779	37,789,266	41,089,190
Discount ⁽⁴⁾	13.9%	13.9%	13.9%

Total

Medical Claim Dollars	233,614,981	258,600,267	280,674,470
Savings Dollars	40,879,732	45,280,028	49,153,918
Discount	13.6%	13.6%	13.6%

Network Savings Split PMPM

State of Alaska Share	100.99	105.65	110.64
Premera Share	0.42	2.42	4.56
Total	101.41	108.08	115.20

Network Savings Split Dollars

State of Alaska Share	40,708,932	44,264,700	47,207,903
Premera Share	170,799	1,015,328	1,946,015
Total	40,879,732	45,280,028	49,153,918

Notes

- 1) Allowed PMPM - Assumed to be 10% higher than Paid PMPM. The member would be responsible for amounts between the Allowed and Paid PMPM.
- 2) Billed PMPM - Assumed to be the same as Aetna billed amounts.
- 3) Savings = Difference between the Billed and Allowed amounts.
- 4) Discount - The network discount is assumed to grow 0.0% per annum. The discount is assumed to be the same as the Aetna 2005 discount of 13.6% in total. We anticipate having slightly different discounts between Active and Retiree populations as the two populations live in different regions of the country.

**State of Alaska
Rx - Base Data**

Script Distribution	Scripts			
	7/06 - 6/07	7/07 - 6/08	7/08 - 6/09	
Subscribers (Est.)	Active	5,464	5,519	5,574
	Retiree	28,128	29,394	29,982
	Total	33,592	34,913	35,556
Members (Est.)	Active	14,097	14,239	14,381
	Retiree	53,162	55,555	56,666
	Total	67,259	69,794	71,047
Retail				
Brand (2)	52.0%	400,617	368,093	368,093
Generic (2)	48.0%	369,801	339,778	339,778
Total (1)	100.0%	770,418	707,871	707,871
Mail				
Brand (2)	52.0%	49,514	45,495	45,495
Generic (2)	48.0%	45,706	41,995	41,995
Total (1)	100.0%	95,220	87,490	87,490
Paper Claims		8,000	8,000	8,000

Estimated 2009 AWP Per Script	AWP Cost Per Script			
	7/06 - 6/07	7/07 - 6/08	7/08 - 6/09	
Retail				
Brand (3)	135.98	141.42	152.73	164.95
Generic (3)	50.73	52.75	56.97	61.53
Mail				
Brand (3)	336.68	350.15	378.16	408.41
Generic (3)	156.03	162.27	175.25	189.27

Notes

- 1) Retail and Mail Script Count - From Mike Wiggins' March 10th Affidavit - Exhibit 1.
- 2) Split between Brand and Generic - Based on Premera Experience. Experience in the bid was not available at this level of specificity.
- 3) AWP Per Script - Based on Premera Experience. Assumed an average trend of 8.0% per annum in AWP per script. As with the split between Brand and Generic, experience in the bid was not available at this level of specificity.

State of Alaska
Total Cost Comparison
Premera - Claims Runout Processing Fee

Range	Months ⁽¹⁾	Runout Claims ⁽²⁾	Fee - 4% of Runout ⁽³⁾
Medical Average	2.05	47,948,555	1,917,942
Rx Average	0.58	3,425,760	137,630
		Total	2,054,573

Notes

- 1) Months - Represents an average of the number of months of claims that are ultimately paid after contract termination. The average is derived from 33 months of historical Premera Medicare Supplement Business. We used the Medicare Supplement business as a benchmark because of the significant number of Retirees that the State of Alaska has. Premera's Commercial business averages 1.96 months of claims, slightly less than the Medicare Supplement business. The Rx Average is taken from our Commercial business and is expected to be a good approximation for the State of Alaska, regardless of the mix of individuals (Active versus Retiree).
- 2) Runout Claims - Runout claims are based on the estimated claims in the 7/08 to 6/09 contract period. An average month of claims is expected to be 23.4M for medical and 5.9M for Rx.
- 3) Premera Claims Runout Processing Fee is 4% of runout claims.

Attachment 2

Affidavit of Matt McGuinness

AFFIDAVIT OF MATT MCGUINNESS

STATE OF CALIFORNIA)
) SS:
COUNTY OF CONTRA COSTA)

I, Matt McGuinness, being first duly sworn, do depose and say that:

1. I am 40 years old. My home address is 114 Russell Drive, Walnut Creek, CA 94598.

2. My current position for Aetna is Underwriting Manager, National Accounts West. I have worked for Aetna for 14 years.

3. The RFP that is the subject of this protest is to provide medical and/or pharmacy benefit management claim services for the State of Alaska. Aetna and its affiliates have held this contract for these services for 24 years.

4. My own job experience in this field involves 10+ years directly related to the pricing of health insurance related matters.

5. In terms of my involvement with health management related RFPs, I have had, in addition to the current RFP in question, involvement in the (1) prior State of Alaska renewal, as well as numerous other RFPs and renewals for large self-insured customers.

6. My previous/past job titles have included Plan Coordination Consultant - Aetna, Underwriter - Aetna, Senior Underwriter- Aetna, Underwriting Manager - Aetna.

7. My current job function includes management of underwriting staff and pricing responsibility for governmental customers, including the State of Alaska, King County (WA) and County of San Mateo (CA) as well as corporate customers such as Costco, Alaska Airlines, Charles Schwab, Hewlett Packard and REI.

8. Specifically for the State of Alaska proposal at issue in this protest, I oversaw the development of the various financial components, and have been

involved in the decision making process for all the major financial issues in the original proposal as well as the best and final offer.

9. By virtue of this experience, I have personal knowledge and am competent to testify regarding the subject matter of this affidavit.

Attached Bar Chart

10. The purpose of this affidavit is to clarify the numbers discussed in the attached bar chart (attached as Exhibit 2) submitted by Aetna.

11. The bar chart highlights three things:

- o The relative amount of administrative fees paid toward the total cost of the plan over three years;
- o To point out that when Premera stated that they "eliminated" the \$6.88 million "Network Access Fee", they had actually just moved it to a less obvious place; and
- o That when looking at total plan costs, the Aetna proposal actually saves the State of Alaska almost \$2.5 million.

A. Premera, 2/13/06

12. In Premera's original bid on this project, it proposed to assess the State of Alaska a \$5.51/per employee/per month "Network Access Fee." *Attachment 4b, pg 2 & 4.*

13. All medical claims service providers (both Aetna and Premera) enter into Preferred Provider Organization agreements. The agreements provide that health providers (doctors, etc.) will write off a portion of the charge for their service when the service is provided to a covered insured.

14. Aetna does business as one corporate entity throughout the country therefore Aetna's PPO agreements have nationwide coverage. Premera does business through many state and regional affiliates therefore Premera Alaska's PPO agreements have only state wide coverage. This difference in Premera's operations is the source of the "Network Access Fee."

15. If a Premiera Alaska insured incurs a claim (for example) with an Arizona doctor, that Arizona doctor's PPO agreement will be with (again, just as an example) "Blue Cross of Arizona." Premiera Alaska will ask "Blue Cross of Arizona" to make use of the latter's PPO agreement, and for that, in its original bid on this project, Premiera proposed to assess the State a \$5.51/per employee/per month charge. This so-called "Network Access Fee" increases Premiera's Net Administrative Fees by \$6.88 million over the course of the contract.

16. In the bar chart *Premiera 2/13/06 Net Administrative Fees* of \$31,957,787 has been calculated as follows: \$34,077,774, as described in section 7.23 of Premiera's Cost Proposal dated February 13, 2006, plus \$6,880,513 in "Network Access Fees" minus \$9.0 million in "guaranteed" pharmacy rebates (\$3.0 million per year) ($\$34,077,774 + \$6,880,513 - \$9.0 = \$31,957,787$).

17. In the bar chart *Pramera 2/13/06 Carrier Retained Discounts* of \$5,496,780 is calculated as follows:

- o The \$5,49 million consists of 12% of the projected Network Discount Savings over \$100 per employee per month. The first year estimated network savings is \$117.32 per employee per month. The amount over \$100 would therefore be \$17.32 and Premiera would retain 12% of that number, which works out to \$2.08 per employee per month. We calculated this \$117.32 by following standard industry underwriting methodology.
- o We took Aetna's actual Network Discount Savings from our standard "level A" reporting package for the period 10/1/04 - 10/1/05 of \$92.42 and trended it forward to the 7/1/06 - 7/1/07 contract period at an annual rate of 15.4%, which works out to an adjusted rate of 27.0%. This adjusted rate is developed by measuring the number of months between the midpoint of the reporting period (4/1/05) and the midpoint of the upcoming contract period (1/1/07). There are 21 months between these two points in time. Therefore the annual trend rate of 15.4% is multiplied by 21/12, which gives the 27.0%. We

¹ Please note that this "guarantee" by Premiera is contingent upon a minimum average volume of \$0,000 "paid claims" per month. Premiera's guarantee specifies that if the number of paid claims does not meet this threshold, the "guarantee" will be prorated accordingly, meaning it can be less than \$3.0 million per year. Aetna's first year expectation of the number of paid claims (what Aetna calls "valid scripts") is 72,137 per month.

then increased \$92.42 by 27.0% to arrive at the first year estimated network savings of \$117.32 per employee (or retiree) per month.

- o Premera stated, in its "Clarification Questions" dated February 14, 2006, that 12% of any savings over \$100.00 per employee per month would be retained by Premera. *Attachment 4b, pg 4*. Therefore, 12% of \$17.32 would be retained by Premera. This works out to \$2.08 per employee per month x 33,592 employees (or retirees) x 12 months in the first contract period, for a total of \$837,954 estimated to be retained by Premera.
- o This same methodology was followed for the second and third contract years, trending each years estimated network discount savings forward at an annual rate of 15.4%, and assuming 12% of the amount over \$100.00 per employee per month would be retained by Premera. Second year estimated retained discounts are \$1,779,257. Third year estimated retained discounts are \$2,879,568. The three year total is: $\$837,954 + \$1,779,257 + \$2,879,568 = \$5,496,780$.

B. Premera, 2/28/06

18. The State, asked Premera, in "Clarification Questions" dated February 24, 2006, if it could bill the "Network Access Fee" in a different manner. *Attachment 4b, pg 2*.

19. Premera advised the Procurement Officer, in its February 28, 2006 Best and Final Response, that the fee was "eliminated." *Id. at 57*. Premera did remove the fees it titled "Network Access Fees" however Premera correspondingly increased others fees to its bid particularly Carrier Retained Discounts that would be more than enough to recover the \$6.88 million "Network Access Fee."

20. In the bar chart *Premera 2/28/06 Carrier Retained Discounts* of \$13,741,949 was calculated the same way *Premera 2/13/06 Carrier Retained Discounts* were in paragraph 16 above, but Premera changed their retained amount of rebates from 12% of anything over \$100.00 per employee per month to 30% of anything over \$100.00 per employee per month in its Cost Proposal dated February 28, 2006. This change in percentage is very significant.

- o The \$13.74 million consists of 30% of the projected Network Discount Savings over \$100 per employee per month. The first year estimated network savings is a \$117.32 per employee per month. The amount over \$100 would therefore be \$17.32 and Premiera would retain 30% of that number, which works out to \$5.196 per employee per month. We calculated this \$117.32 by following standard industry underwriting methodology.
- o We took Aetna's actual Network Discount Savings from our standard "level A" reporting package for the period 10/1/04 - 10/1/05 of \$92.42 and trended it forward to the 7/1/06 - 7/1/07 contract period at an annual rate of 15.4%, which works out to an adjusted rate of 27.0%. The adjusted rate is developed by measuring the number of months between the midpoint of the reporting period (4/1/05) and the midpoint of the upcoming contract period (1/1/07). There are 21 months between these two points in time. Therefore the annual trend rate of 15.4% is multiplied by 21/12, which gives the 27.0%. We then increased \$92.42 by 27.0% to arrive at the first year estimated network savings of \$117.32 per employee (or retiree) per month.
- o Premiera stated, in its "Performance Standards Summary" dated February 28, 2006, that 30% of any savings over \$100.00 per employee per month would be retained by Premiera. Therefore, 30% of \$17.32 would be retained by Premiera. This works out to \$5.196 per employee per month x 33,592 employees (or retirees) x 12 months in the first contract period, for a total of \$2,094,886 estimated to be retained by Premiera.
- o This same methodology was followed for the second and third contract years, trending each year's estimated network discount savings forward at an annual rate of 15.4%, and assuming 30% of the amount over \$100.00 per employee per month would be retained by Premiera. Second year estimated retained discounts are \$4,448,143. Third year estimated retained discounts are \$7,198,920. The three year total is: \$2,094,886 + \$4,448,143 + \$7,198,920 = \$13,741,949.²

² It is important to note that the amounts retained go up dramatically each year because the per employee per month savings are compounded each year (working out to \$117.32 in year 1, \$135.59 in year 2 and \$156.24 in year 3), but Premiera retains 30% of all amounts over a fixed amount of \$100.00 for the three year contract period.

21. In the bar chart *Premiera 2/27/06 Net Administrative Fee* of \$21,951,035 is the \$30,951,035 described in section 7.23 of Premiera's Cost Proposal dated February 28, 2006 less the \$9.0 million in guaranteed pharmacy rebates (\$3.0 million per year).

22. *Premiera 2/27/06 Net Administrative Fee* reflects the "removal" of the \$6.88 million "Network Access Fee." In conjunction with removing this \$6.88 million "Network Access Fee", Premiera's Cost Proposal dated February 28, 2006 increased the amount of Carrier Retained Discounts from 12% to 30%. As described in paragraph 20 above, 30% results in an estimated additional \$8.2 million in discount savings to be retained by Premiera.

23. The increase in Premiera's Carrier Retained Discounts effectively shifts the \$6.88 million from Net Administrative Fees to Carrier Retained Discounts. Therefore Premiera did not in fact eliminate the \$6.88 million "Network Access Fee." It hid the fee by increasing Carrier Retained Discounts.

C. Aetna

24. It is common practice, and in fact, common sense, that when judging one proposal against another, one cannot focus on just one category of costs, while excluding another.

25. To determine the total cost to the State of Alaska, in addition to the administrative fees specified in the Cost Proposal, one must also include:

- o The impact of pharmacy rebates (whether retained by the carrier or given to the State);
- o Fees collected through another mechanism besides the monthly billing;
- o Network discounts retained by the carrier in lieu of higher fees; and
- o Runoff processing charges.

The State of Alaska should have taken these factors into consideration when judging the proposals. If the state did take these factors into consideration the

proposal submitted by Aetna on February 28, 2006 would have been judged to save the state approximately \$2.5 million.

26. This \$2.5 million does not include the impact of the cost of runoff claim processing. Premiera charges 4% of claims processed after termination of the plan for this service. Aetna charges three months of service fees. Based on our projections, at the end of the 3 year contact period, the Aetna runoff processing fee would be \$2.6 million, while the Premiera fee will be almost \$5 million. This alone would result in a savings to the State of \$2.4 million at the time the plan terminates. Should the State of Alaska terminate the Aetna contract in 2006, the runoff processing fee payable at that time will be approximately \$2.8 million.

27. Including the impact of runoff claim processing, we feel the Aetna proposal would save the State a total of \$4.9 million.

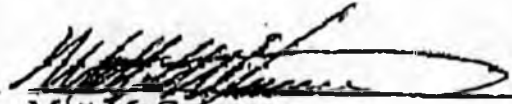
28. The following describes in some detail, how Aetna came up with each of the numbers in the graph, and their significance to Aetna's assertions

29. Aetna Carrier Retained Discounts of \$3,401,128 is made up of two components. The first is a potential "bonus" of up to 5% of medical fees that Aetna can earn for exceeding the Aetna network savings guarantee. For purposes of this comparison, we have assumed that Aetna will exceed that guaranteed network savings and thus earn the additional fee, and further that the "bonus" will be the same for each year of the three year contract period, totaling \$977,622 over 3 years. Please note that the threshold set for this guarantee was only set for year 1 of the contract period, with the intent that it will be reviewed towards the end of each year, and set at a level agreeable to the State for the subsequent year, based on the latest claim information available. The second component is the fee for Aetna's "National Advantage Program." The NAP program gains the State of Alaska special negotiated discounts on certain PPO out of network and indemnity claims that would normally be paid at a non-discounted rate. The fee for the NAP program is 30% of the actual savings attained. We have estimated the total three year fee at \$2,423,506 which is based off of actual 2005 NAP savings & fees.

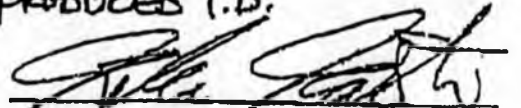
30. Actua Explicit Administrative Fee of \$29,804,652 is comprised of \$32,054,652, which is the total 3 year Actua fee in section 7.23 of the Cost Proposal dated February 28, 2006, less the \$2,250,000 guaranteed minimum pharmacy rebate to the State.

Further your affiant sayeth naught.

Dated this 24th day of March, 2006, at Walnut Creek, California.


Matt McGuinness

SUBSCRIBED AND SWORN before me this 24th day of March, 2006,
by Matt McGuinness who produced I.D.


Notary Public in and for California
My commission expires 1/13/09

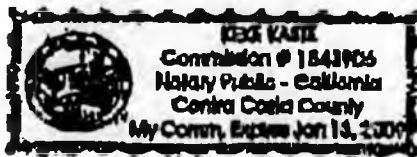
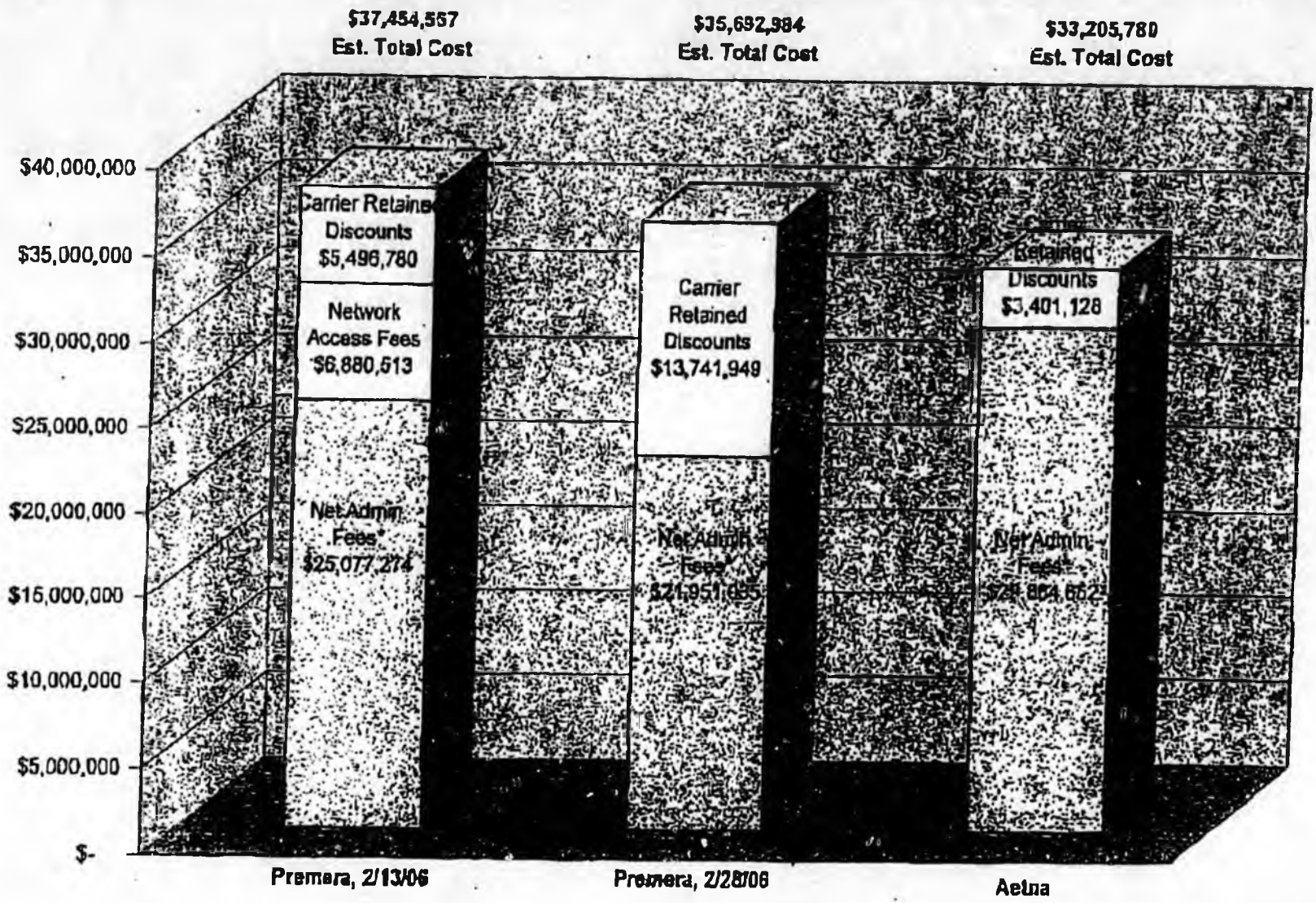


Exhibit 2: State of Alaska, Carrier Compensation Breakdown, 3 year view



*Net Administrative Fees is actual fees minus guaranteed pharmacy rebates

Robert K. Stewart, Jr.
Davis Wright Tremaine LLP
701 W. Eighth Avenue, Suite 800
Anchorage, Alaska 99501
(907) 257-5300
(907) 257-5399 (Facsimile)

Attorneys for Premera Blue Cross Blue Shield of Alaska

BEFORE THE ALASKA DEPARTMENT OF ADMINISTRATION

In the Matter of:)
)
Aetna Life Insurance Company and)
Aetna, Inc.,)
)
Appellants.) DGS Solicitation No. 2007-0200-5946
) OAH No. 06-0230-PRO

AFFIDAVIT OF DAVID BRAZA

STATE OF WASHINGTON)
) ss.
COUNTY OF SNOHOMISH)

David Braza, being first duly sworn on oath, deposes and says as follows:

1. I am Vice President of Actuarial Services for Premera Blue Cross ("Premera").

I am competent to make this affidavit, and do so on the basis of personal knowledge.

2. I have been Vice President of Actuarial Services with Premera since April, 2004. In total I have 14 years of work experience in actuarial science. I have a Bachelor of Science in Business Administration from Georgia State University, where I majored in Actuarial Science. I am a Fellow of the Society of Actuaries, an Associate of the Casualty Actuarial Society, and a Member of the American Academy of Actuaries.

3. I performed an analysis of the bids submitted by Premera and Aetna for the administration of the State of Alaska's health benefit plan. The conclusions of my analysis are included in my narrative description of my methodology, attached to this Affidavit as Exhibit 1, and my spreadsheet analysis, attached to this Affidavit as Exhibit 2.

Dated this 27th day of April, 2006.

David Braza

David Braza

SUBSCRIBED AND SWORN TO before me this 27th day of April, 2006.



Joyce A. Evers

Notary Public in and for the State of Washington

My commission expires: April 9, 2009

Printed Name: Joyce A. Evers

EXHIBIT 1

State of Alaska Total Cost Comparison Premera vs. Aetna

Purpose

To compare the *total costs* of the Premera and Aetna 2/28/2006 BAFO ("Best and Final Offer") for the State of Alaska. Total costs include costs that are both fixed and variable. Administration Fees and Pharmacy (Rx) Rebate credits are examples of fixed costs. Medical Claim Costs, Medical Shared Savings Fees, and Rx Claim Costs are examples of variable costs.

Data Sources

In performing a *total cost* comparison, I projected both the fixed and variable costs that the State of Alaska will likely see over the course of the future contract period. To do so, I used information that was made available to Premera during the bidding process, supplemental information made public from Aetna, and internal information relating to Premera that was not included in the Rx portion of the bid. The information used in the *total cost* projection includes:

- 1) Medical Claim Dollars by year for 2003, 2004, and YTD2005 (data through September). The Medical Claim Dollars were split between the active and retiree populations.
- 2) Employee/Member counts for 2003, 2004, and YTD2005.
- 3) Estimated Future Employee/Member counts from Aetna's 12/28/2005 bid.
- 4) Aetna Medical Network Savings (History) - As reported in Aetna's 12/28/2005 bid, page 2 of 7. Aetna also included an estimated calendar year 2005 savings using actual savings data through September of 2005.
- 5) Retail and Mail Prescription Claims - From Mike Wiggins' March 10th Affidavit - Exhibit 1.
- 6) Rx Rebate Guarantees - These guarantees were included in both Premera and Aetna's 2/28/2006 BAFO.
- 7) Aetna Rx Retail/Mail Discounts and Dispensing Fees - From Aetna's 2/28/2006 BAFO.
- 8) Premera Rx Retail/Mail Discounts and Dispensing Fees - Premera offered a straight pass-through of discounts and dispensing fees from our Rx vendor (presently Medco).

Note: The total cost comparison looks at all costs that the State of Alaska may incur - both fixed and variable (with the exception of dental claims). In contrast, the cost comparison produced by Matt McGuinness in his Affidavit, dated 3/28/2006, focused primarily on the fixed costs only with one variable cost component considered, namely, Medical Shared Savings Fees.

Total Cost Comparison – Explanation and Supporting Exhibits

Total Cost Comparison (Exhibit 1) – This exhibit summarizes the total expected dollar difference in costs for Administration Fees (fixed cost), Medical Claim Cost (variable), Medical Shared Savings Fee (variable), Rx Claim Cost (variable), and Rx Rebates (fixed). The total cost savings expected from the Premera bid is estimated to be 10.7 million dollars over the course of the three-year contract term. The savings are broken down as follows:

Administration Fee – 1.1M.
Medical Claim Costs – 0.0M.
Medical Shared Savings Fee – 0.3M.
Rx Claim Costs – 1.5M.
Rx Rebates – 7.8M.
Total – 10.7M.

Administration Fee (Exhibit 2) – The fees for both Actna and Premera are as reported from Section 7.23 – Cost Proposal (All Services) – BAFO, dated 2/28/2006.

Aetna Medical Claim Cost Projection (Exhibit 3, Page 1 of 2)

Historical Periods – 2003, 2004, and YTD2005 (annualized)

The basis for the Aetna medical claim cost projection is the historical Aetna paid medical claim dollars and members over the period 2003, 2004, and YTD2005 (annualized). The medical claim dollars and members are used to derive Paid PMPM (Per Member Per Month) costs. The Paid PMPM costs were then converted to an Allowed FMPM costs. To do this, I assumed the member would be responsible for 10% of the provider allowed charges. Members are liable and pay providers for certain items, such as deductibles, coinsurance, and copays, if any.

Note: The 10% member responsibility assumption is used throughout the historical and projection period and is also used in the Premera projection.

Aetna Discounts and Savings PEPM – 2003, 2004, and YTD2005 (annualized)

The Allowed PMPM is converted to a Billed PMPM using the reported historical savings from Aetna's 12/28/2005 bid, page 2 of 7. Converting the Paid PMPM to Allowed PMPM and then to a Billed PMPM enabled me to impute an average historical discount and Savings PEPM (Per Employee Per Month) for Aetna. The average discounts using this imputation technique for 2003, 2004, and YTD2005 (annualized) are 11.9%, 12.4%, and 13.6%, respectively. The Savings PEPM are 71.41, 78.90, and 91.91 for 2003, 2004, and YTD2005 (annualized), respectively.

Future Periods – 7/06 to 6/07, 7/07 to 6/08, and 7/08 to 6/09

The historical information is then used as the basis to project Aetna's medical claim costs into future periods. Using the historical data, I was able to derive a per annum claims trend of 6.6% as the difference in Billed PMPM figures from 2003 to 2004.

The 6.6% per annum trend is applied to the YTD2005 (annualized) Billed PMPM to project Billed PMPM figures into the future contract periods. Because the 2005 data (data available through September 2005) was annualized, the center of the YTD2005 claims is 7/1/2005. To project the Billed PMPM to the first contract period of 7/06 to 6/07, 18 months of trend was used. From there, only 12 months of trend was needed to move from the first to the second and from the second to the third contract periods.

Once the Billed PMPM figures for the future contract periods are established, I was able to derive an Allowed PMPM by assuming the provider discounts remain at 2005 levels - 13.6%. This produces PEPM Savings of 101.46, 108.07, and 115.17 for contract years 7/06 to 6/07, 7/07 to 6/08, and 7/08 to 6/09, respectively. The basis for this assumption is that as providers change their billing practices (pressure from self-pay lawsuits) discounts are anticipated to flatten in the future. Although, the discounts are anticipated to remain flat at 13.6%, the Savings PEPM will continue to grow as medical inflation continues to push costs higher.

Also, to test the sensitivity of the projection to higher than anticipated trends, I chose a 12.0% trend, which is nearly double the actual trend observed in the State's own experience from 2003 to 2004. The 12.0% per annum trend produces PEPM Savings of 109.26, 122.28, and 136.92 for contract years 7/06 to 6/07, 7/07 to 6/08, and 7/08 to 6/09, respectively. The total costs savings produced from the Premera offer (using the 12.0% trend) is still substantially more than Aetna, at 5.2M versus 10.7M over the course of the three-year contract period.

Finally, to calculate the projected Aetna Medical Claim Costs, the future Paid PMPM figures are multiplied by the anticipated members. As noted above, the member responsibility is assumed to remain at 10% of the provider allowed charges.

Premera Medical Claim Cost Projection (Exhibit 3, Page 2 of 2)

The starting point for the Premera Medical Claim Cost projection is the Billed PMPM figures from the Aetna Medical Claim Cost projection. The goal of the Premera Medical Claim Cost projection is to mirror the Aetna projection. Each projection uses the same assumptions. Although, we anticipate having significant claim savings versus the Aetna bid as referenced in Gubby Barlow's letter to the State of Alaska on 2/28/2006 (favorable provider discount differences that we have in the regions in which State employees live versus Aetna), the difference in claims over the course of the contract is reported to be the same as Aetna; meaning, network discounts achievable by Aetna and Premera are equal for purposes of this analysis.

Aetna Medical Shared Savings Fee

The Aetna Shared Savings Fee of 3.4M over the course of the contract term is obtained from the Matt McGuinness Affidavit, Page 7 of 8, dated 3/28/2006. It should be noted that Mr. McGuinness states that \$2,423,506 of that fee is for Aetna's "National Advantage Program". That program is described as a program based on Aetna's "special negotiated discounts on certain PPO out of network and indemnity claims". This fee is similar to the network discount fee that Premera eliminated from its final BAFO. Lastly, due to Aetna confidentiality designations, I was not able to independently validate the accuracy of the McGuinness Shared Savings Fee calculation.

Premera Medical Shared Savings Fee (Exhibit 3, Page 2 of 2)

The Premera Medical Shared Savings Fee is calculated based on the guarantee reported in the Premera BAFO, dated 2/28/2006. The guarantee is that Premera would obtain at least 100.0 PEPM savings from the provider discount arrangements. To the extent that the PEPM savings are less than 100.0 PEPM, Premera will reimburse the State of Alaska 30% of the difference between the actual savings PEPM and 100.0 PEPM. In this projection, I anticipate that over the course of the contract the shared savings fee charges to the State of Alaska would be 3.1M dollars.

As stated above in the "Premera Medical Claim Cost Projection", we anticipate having significant claim savings versus the Aetna bid. Our estimate is based on favorable provider discount differences that we have in the regions in which State employees and retirees live versus Aetna.

Base Rx Claim Cost Data (Exhibit 4, Page 1 of 3) – Both for Aetna and Premera

To project future Rx Claim Costs for both Aetna and Premera, base data from Exhibit 4, Page 1 of 3 was used. The base Rx claim counts for Retail and Mail were obtained from Mike Wiggins' March 10th Affidavit – Exhibit 1. The base Rx claim counts were further split between brand and generic drugs, assuming that 52% are brand drugs and 48% are generic drugs (the 52%/48% split is based on averages obtained from Premera internal experience). This split was necessary to project future Rx claim costs. Rx provider discounts are separately reported and split between the retail/mail setting and within the retail/mail setting by brand/generic. Paper claims were taken from the Aetna 12/28/2005 bid and assumed to remain at the 8,000 per year level for future contract periods.

In addition to the Rx claim counts, the Average Wholesale Price (AWP) per claim is needed to project future Rx claim costs. The AWP prices for retail/mail are estimates based on Premera's block-of-business. Future AWP prices are assumed to increase at the rate of 8.0% per annum (the 8.0% is based on historical and future experience that is anticipated by Premera over the course of the contract period). The average discounts as shown in Exhibit 4, Page 2 and 3 of 3 are applied to the AWP per claim to derive the net

allowed per claim that the State of Alaska and their members will pay for prescription drugs in various settings (retail/mail, brand or generic).

Aetna Rx Claim Cost (Exhibit 4, Page 2 of 3)

Aetna Rx Claim Costs are derived from the base data from Exhibit 4, Page 1 of 3 and the reported discounts and dispensing fees in Aetna's BAFO, dated 2/28/2006. Although Aetna only reported discounts and dispensing fees for the first contract period (7/06 to 6/07), I assumed that those discounts and dispensing fees would hold for the two remaining contract periods – 7/07 to 6/08 and 7/08 to 6/09. The same assumption was also used in the Premera Rx Claim Cost projection.

Additionally, as with the medical claim cost projection, I assumed that the members would be responsible for 10% of the allowed amount (AWP amount less the discount). The 10% is an estimate of what members would be pay in copays, coinsurance, and deductibles, if any. The same 10% member responsibility assumption is also used in the Premera Rx Claim Cost projection.

Premera Rx Claim Cost (Exhibit 4, Page 3 of 3)

Premera Rx Claim Costs are derived from the base data from Exhibit 4, Page 1 of 3. The reported discounts and dispensing fees come from the Premera Medco (PBM vendor) contract. As with the Aetna Rx Claim Cost projection, I assumed that the Premera discounts would hold constant over the three-year contract period.

Additionally, as with the medical claim cost projection, I assumed that the members would be responsible for 10% of the allowed amount (AWP amount less the discount). The 10% is an estimate of what members would be pay in copays, coinsurance, and deductibles, if any. The same 10% member responsibility assumption is also used in the Aetna Rx Claim Cost projection.

The aggregate Rx claims impact comparing the Premera and Aetna discounts, dispensing fees, and charges for paper claim submissions (if any) is an estimated savings to the State of Alaska of 1.5M by choosing Premera. The direct Rx cost comparison is made possible by using the same Base Rx Claim Cost Data as described above.

Aetna Rx Rebates (Exhibit 4, Page 2 of 3)

Aetna Rx Rebates are guaranteed (as reported in Aetna's BAFO, dated 2/28/2006) at the greater of 13.3% of manufacturer rebates or 750,000 per year. Because the Rx claim count estimates in the 7/07 to 6/08 and 7/08 to 6/09 contract years produce rebate amounts of less than 750,000 per year, the rebate amount was set equal to 750,000.

Note: Rx claim counts used to calculate rebate amounts are obtained from the Mike Wiggins's March 10th Affidavit – Exhibit 1.

Premera Rx Rebates (Exhibit 4, Page 2 of 3)

Premera Rx Rebates are guaranteed (as reported in Premera's BAFO, dated 2/28/2006). The guarantee is a minimum of 3.0M dollars a year, contingent upon generating an average paid claims volume of at least 80,000 claims per month over any of the three contract years.

Based on Rx claim counts, the total Rx rebate credit is expected to be 10.1M versus the Aetna guarantee of 2.3M for a net savings to the State of Alaska of 7.8M over the course of the contract.

Note: Rx claim counts used to calculate rebate amounts are obtained from the Mike Wiggins's March 10th Affidavit - Exhibit 1.

Claims Runout Processing Fee (Exhibit 5, Page 1 of 1)

Aetna contends that its proposed fee for administration of claims following termination of the contract ("Runout Fee") is more than 2.0M less than the comparable fee for Premera. In reality, Premera's Runout Fee is significantly less than that of Aetna.

Aetna estimates its Runout Fee to be 2.6M and states that "the Premera fee will be almost 5.0M". (McGuinness Affidavit, paragraph 26.). Matt McGuinness provides no explanation for how he arrived at the 5.0M calculation. In fact, it is likely that the Premera Runout Fee will be close to **2.05M**.

The State's contract with Premera provides that the State will pay Premera an administrative fee of 4.0% of eligible claims paid after the date of the contract termination. (Contract between the State and Premera, page 5.) Runout Claims are claims for medical and pharmacy services which were provided before a contract was terminated, but which were not received and/or processed by the administrator prior to the termination of the contract. To project the claims runout processing fee for the State of Alaska, I analyzed our claims payment history for Premera's group commercial business in the state of Alaska. For each of the last 33 months, I ran a computer-generated history that showed what volume of claims was paid following the end the month, thereby approximating a claims runout process. On average for those 33 months, Premera paid medical claims equivalent to 1.96 months worth of claims. For pharmacy claims, the claims equivalent is 0.58 months worth of claims.

Additionally, to better approximate the claims runout process for what the State of Alaska may experience (The State has a substantial number of retirees, which requires claims coordination with Medicare), I also analyzed Premera's claims processing for Medicare Supplement business. Coordination of benefits with Medicare adds additional time to the process, thus Medicare Supplement claims take longer to process. For the Medicare Supplement business, Premera pays claims runout over 2.05 months on average (slightly higher than the 1.96 months in the Premera group commercial Alaska business).

Finally, to estimate the 2.05M Premera claims runout processing fee shown on Exhibit 5, I used the longer (Medicare Supplement) period rather than the shorter Commercial period, recognizing that this produces a more conservative estimate for the fee. The projected runout processing fee was then calculated by multiplying the foregoing number of months for each of the medical and pharmacy claims by the average monthly claims volume for the third year of the contract (23.4M and 5.9M respectively), and totaling those. That number was then multiplied by the 4% Runout Fee to product the projected cost to the State of 2.05M, which is significantly less than Aetna's own projection of its termination fees – 2.6M.

EXHIBIT 2
Total Cost Comparison
Premera vs. Aetna

	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09	Total	Difference
Employees					
Active	5,464	5,519	5,574		
Retiree	28,128	29,394	29,982		
Total	33,592	34,913	35,556		
Aetna					
Administration Fee ⁽¹⁾	7,205,823	12,011,706	12,839,123	32,054,652	
Medical Claim Cost ^{(9), (10), (11), (12), (13), (14)}	233,599,109	258,604,608	280,686,001	772,889,718	
Medical Shared Savings Fee ⁽²⁾	1,133,709	1,133,709	1,133,709	3,401,128	
Rx Claim Cost ^{(3), (12)}	66,832,747	66,199,894	71,374,530	204,407,171	
Rx Rebates ⁽⁴⁾	(762,107)	(750,000)	(750,000)	(2,262,107)	
Total	308,007,281	337,199,917	365,283,364	1,010,490,562	
Premera					
Administration Fee ⁽⁵⁾	8,190,903	10,990,649	11,769,483	30,951,035	1,103,617
Medical Claim Cost ^{(9), (10), (11), (12), (13), (14)}	233,614,981	258,600,267	280,674,470	772,889,718	0
Medical Shared Savings Fee ⁽⁶⁾	170,799	1,015,328	1,946,015	3,132,143	268,985
Rx Claim Cost ^{(7), (12)}	66,318,454	65,714,881	70,877,783	202,911,119	1,496,053
Rx Rebates ⁽⁸⁾	(3,303,187)	(3,339,405)	(3,438,189)	(10,080,780)	7,818,673
Total	304,991,950	332,981,721	361,829,563	999,803,234	10,687,328
Difference	3,015,330	4,218,196	3,453,801	10,687,328	

Notes and Assumptions

- 1) Aetna Administration Fee - From Section 7.23 - Cost Proposal (All Services) - BAFO, Dated 2/28/2006.
- 2) Aetna Shared Savings Fee - From Matt McGuinness Affidavit, Page 7 of 8, Dated 3/28/2006.
- 3) Aetna Rx Claim Cost - Estimated based on information from Aetna 12/28/2005 Bid and From Section 7.23 Cost Proposal (All Services) - BAFO, Dated 2/28/2006.
- 4) Aetna Rx Rebates - From Section 7.23 - Cost Proposal (All Services) - BAFO, Dated 2/28/2006. Rx script count estimates from Mike Wiggins' March 10th Affidavit - Exhibit 1.
- 5) Premera Administration Fee - From Section 7.23 - Cost Proposal (All Services) - BAFO, Dated 2/28/2006.
- 6) Premera Shared Savings Fee - Calculated from Premera BAFO, Dated 2/28/2006. To the extent that the PEPM Savings are less than 100.0 PEPM, Premera will reimburse the State of Alaska 30% of the difference between the actual savings and 100.0 PEPM.
- 7) Premera Rx Claim Cost - Estimated based on information from Premera's Medco (PBM vendor) contract.
- 8) Premera Rx Rebates - From Premera BAFO, Dated 2/28/2006. Rx script count estimates From Mike Wiggins' March 10th Affidavit - Exhibit 1.

Medical Claim Cost - Notes

EXHIBIT 2
Total Cost Comparison
Premera vs. Aetna

- 9) Medical claims are assumed to be the same between Aetna and Premera. Also, assumes that for Dental, LTC, and FSA costs beyond administration fees are the same between Aetna and Premera.
- 10) Medical Future Savings - Assumes that provider discounts will stay at the Aetna 2005 levels - 13.6%. The future PEPM savings are 101.46, 108.07, and 115.17 over the the future policy periods of 7/06 to 6/07, 7/07 to 6/08, and 7/08 to 7/09, respectively.
- 11) Medical Past Savings - The past savings are 71.41, 78.90, and 91.91 PEPM for calendar years 2003, 2004, and 2005 respectively. Savings are assumed to be as reported in Aetna's 12/28/2005 Bid, Page 2 of 7.
- 12) Assumes that for both Medical and Rx, the member will pay 10% of the provider allowed amount.
- 13) Claims Trend - Trend in billed claims assumed to be 6.6% per annum or the difference in billed amounts from 2003 to 2004.
- 14) Provider Discount - The network discount is assumed to grow 0.0% per annum. The discount is assumed to be the same as the 2005 discount of 13.6%.

**State of Alaska
Administration Fee
Section 7.23 - Cost Proposal
All Services - BAFO, Dated 2/28/2006**

	# of Lives	Aetna		Premera	
		Year 1	Annual Dollars	Year 1	Annual Dollars
Per employee per month medical	5,464	24.16	1,583,892	24.79	1,625,431
Per retiree per month medical	28,128	14.62	4,933,586	16.95	5,721,235
Per retiree per month DVA	20,725	2.21	549,627	2.78	691,386
Per retiree per month LTC	19,011	0.39	88,971	0.42	95,315
Per participant per month Health FSA	1,358	2.93	47,747	3.50	57,036
			7,203,823		8,190,903

	# of Lives	Aetna		Premera	
		Year 2	Annual Dollars	Year 2	Annual Dollars
Per employee per month medical	5,519	37.44	2,479,315	32.16	2,129,892
Per retiree per month medical	29,394	24.18	8,527,573	22.00	7,760,016
Per retiree per month DVA	21,658	3.09	803,079	3.61	938,225
Per retiree per month LTC	19,866	0.57	135,883	0.44	104,892
Per participant per month Health FSA	1,372	4.00	65,856	3.50	57,624
			12,011,706		10,990,649

	# of Lives	Aetna		Premera	
		Year 3	Annual Dollars	Year 3	Annual Dollars
Per employee per month medical	5,574	38.68	2,587,131	33.77	2,258,808
Per retiree per month medical	29,982	25.42	9,146,052	23.10	8,311,010
Per retiree per month DVA	22,633	3.24	879,971	3.79	1,029,349
Per retiree per month LTC	20,760	0.63	156,946	0.45	112,104
Per participant per month Health FSA	1,388	4.15	69,023	3.50	58,212
			12,839,123		11,769,483
Grand Total (Years 1-3)			32,054,652		30,951,035

State of Alaska
Aetna Medical Claim Costs and Savings

Aetna Estimates

Active

	2003	2004	YTD2005 (6)	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	5,574	5,536	5,558	5,464	5,519	5,574
Members	14,884	14,611	14,649	14,097	14,239	14,381
Medical Claim Dollars	36,452,682	37,153,083	29,533,843	43,489,007	46,825,929	50,413,886

PMPM

Paid	204.09	211.90	233.58	257.08	274.05	292.13
Allowed (1), (5)	226.77	235.45	259.53	285.64	304.50	324.59
Billed (2), (4)	257.33	268.71	300.42	330.55	352.48	375.74
Savings (3)	30.56	33.27	40.89	45.01	47.98	51.15
Savings Dollars	5,458,978	5,832,526	6,894,184	7,613,838	8,198,050	8,826,212
Discount (5)	11.9%	12.4%	13.6%	13.6%	13.6%	13.6%

Retiree

	2003	2004	YTD2005 (6)	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	25,350	25,680	27,803	28,128	29,394	29,982
Members	18,639	18,343	18,673	53,162	55,555	56,666
Medical Claim Dollars	110,502,716	137,341,257	128,112,888	190,110,102	211,778,679	230,272,115

PMPM

Paid	240.72	255.04	270.76	298.00	317.67	338.64
Allowed (1), (5)	267.47	283.37	300.85	331.12	352.97	376.27
Billed (2), (4)	303.52	323.41	348.25	383.29	408.59	435.55
Savings (3)	36.05	40.04	47.40	52.17	55.62	59.29
Savings Dollars	21,041,022	24,667,474	29,905,816	33,283,529	37,077,155	40,314,894
Discount (5)	11.9%	12.4%	13.6%	13.6%	13.6%	13.6%

Total

Medical Claim Dollars	176,955,378	194,284,320	157,646,711	233,599,109	258,604,608	230,686,001
Savings Dollars	26,500,000	30,600,000	36,800,000	40,897,367	45,275,205	49,141,105
Savings PMPM	71.41	78.90	91.91	101.46	108.67	115.17

Notes

Shaded Numbers - Shaded areas represent numbers obtained during the bid process and Aetna's bid, dated 12/28/2005.

- 1) Allowed PMPM - Assumed to be 10% higher than Paid PMPM. The member would be responsible for amounts between the Allowed and Paid PMPM.
- 2) Billed PMPM - Estimated based on reported savings from the Aetna 12/23/2005 Bid, Page 2 of 7.
- 3) Savings = Difference between the Billed and Allowed amounts.
- 4) Claims Trend - Trend in billed claims assumed to be 6.6% per annum or the difference in billed amounts from 2003 to 2004.
- 5) Discount - The network discount is assumed to grow 0.0% per annum. The discount is assumed to be the same as the 2005 discount of 13.6%.
- 6) YTD2005 - Information shown above has been extrapolated to produce estimated 2005 results.

State of Alaska
Premera Medical Claim Costs and Savings

Premera Estimates

Active

	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	5,464	5,519	5,574
Members	14,097	14,239	14,381
Medical Claim Dollars	44,062,204	47,462,488	51,099,221

PMPM

Paid	260.57	277.77	296.11
Allowed ^{(1), (4)}	289.53	308.64	329.01
Billed ⁽²⁾	330.65	352.48	375.74
Savings ⁽³⁾	41.13	43.84	46.73
Savings Dollars	6,956,953	7,490,762	8,064,728
Discount ⁽⁴⁾	12.4%	12.4%	12.4%

Retiree

	7/06 to 6/07	7/07 to 6/08	7/08 to 6/09
Employees	28,128	29,394	29,982
Members	53,162	55,555	56,666
Medical Claim Dollars	189,534,777	211,137,779	229,575,249

PMPM

Paid	297.10	316.71	337.61
Allowed ^{(1), (4)}	330.11	351.90	375.13
Billed ⁽²⁾	383.29	408.59	435.55
Savings ⁽³⁾	53.18	56.68	60.43
Savings Dollars	33,922,779	37,789,266	41,089,190
Discount ⁽⁴⁾	13.9%	13.9%	13.9%

Total

Medical Claim Dollars	233,614,981	258,600,267	280,674,470
Savings Dollars	40,879,732	45,280,028	49,153,918
Discount	13.6%	13.6%	13.6%

Network Savings Split PMPM

State of Alaska Share	100.99	105.65	110.64
Premera Share	0.42	2.42	4.56
Total	101.41	108.08	115.20

Network Savings Split Dollars

State of Alaska Share	40,708,932	44,264,700	47,207,903
Premera Share	170,799	1,015,328	1,946,015
Total	40,879,732	45,280,028	49,153,918

Notes

- 1) Allowed PMPM - Assumed to be 10% higher than Paid PMPM. The member would be responsible for amounts between the Allowed and Paid PMPM.
- 2) Billed PMPM - Assumed to be the same as Aetna billed amounts.
- 3) Savings = Difference between the Billed and Allowed amounts.
- 4) Discount - The network discount is assumed to grow 0.0% per annum. The discount is assumed to be the same as the Aetna 2005 discount of 13.6% in total. We anticipate having slightly different discounts between Active and Retiree populations as the two populations live in different regions of the country.

**State of Alaska
Rx - Base Data**

Script Distribution	Scripts			
	7/06 - 6/07	7/07 - 6/08	7/08 - 6/09	
Subscribers (Est.)	Active	5,464	5,519	5,574
	Retiree	28,128	29,394	29,982
	Total	33,592	34,913	35,556
Members (Est.)	Active	14,097	14,239	14,381
	Retiree	53,162	55,555	56,666
	Total	67,259	69,794	71,047
Retail				
Brand (2)	52.0%	400,617	368,093	368,093
Generic (2)	48.0%	369,801	339,778	339,778
Total (1)	100.0%	770,418	707,871	707,871
Mail				
Brand (2)	52.0%	49,514	45,495	45,495
Generic (2)	48.0%	45,706	41,995	41,995
Total (1)	100.0%	95,220	87,490	87,490
Paper Claims		8,000	8,000	8,000

Estimated 2006 AWP Per Script	AWP Cost Per Script		
	7/06 - 6/07	7/07 - 6/08	7/08 - 6/09

Retail				
Brand (3)	135.98	141.42	152.73	164.95
Generic (3)	50.73	52.75	56.97	61.53
Mail				
Brand (3)	336.68	350.15	378.16	408.41
Generic (3)	156.03	162.27	175.25	189.27

Notes

- 1) Retail and Mail Script Count - From Mike Wiggins' March 10th Affidavit - Exhibit 1.
- 2) Split between Brand and Generic - Based on Premera Experience. Experience in the bid was not available at this level of specificity.
- 3) AWP Per Script - Based on Premera Experience. Assumed an average trend of 8.0% per annum in AWP per script. As with the split between Brand and Generic, experience in the bid was not available at this level of specificity.

State of Alaska
Total Cost Comparison
Premera - Claims Runout Processing Fee

Range	Months ⁽¹⁾	Runout Claims ⁽²⁾	Fee - 4% of Runout ⁽³⁾
Medical Average	2.05	47,948,555	1,917,942
Rx Average	0.58	3,425,760	137,030
		Total	2,054,973

Notes

- 1) Months - Represents an average of the number of months of claims that are ultimately paid after contract termination. The average is derived from 33 months of historical Premera Medicare Supplement Business. We used the Medicare Supplement business as a benchmark because of the significant number of Retirees that the State of Alaska has. Premera's Commercial business averages 1.96 months of claims, slightly less than the Medicare Supplement Business. The Rx Average is taken from our Commercial business and is expected to be a good approximation for the State of Alaska, regardless of the mix of individuals (Active versus Retiree).
- 2) Runout Claims - Runout claims are based on the estimated claims in the 7/08 to 6/09 contract period. An average month of claims is expected to be 23.4M for medical and 5.9M for Rx.
- 3) Premera Claims Runout Processing Fee is 4% of runout claims.

Robert K. Stewart, Jr.
Davis Wright Tremaine LLP
701 W. Eighth Avenue, Suite 800
Anchorage, Alaska 99501
(907) 257-5300
(907) 257-5399 (Facsimile)

Attorneys for Premera Blue Cross Blue Shield of Alaska

BEFORE THE ALASKA DEPARTMENT OF ADMINISTRATION

In the Matter of:)
)
Aetna Life Insurance Company and)
Aetna, Inc.,)
)
Appellants.) DGS Solicitation No. 2007-0200-5946
) OAH No. 06-0230-PRO

AFFIDAVIT OF JEFF DAVIS

STATE OF WASHINGTON)
) ss.
COUNTY OF SNOHOMISH)

Jeff Davis, being first duly sworn on oath deposes and says as follows:

1. I am the General Manager and Vice President of Premera Blue Cross, doing business in the state of Alaska as Premera Blue Cross Blue Shield of Alaska ("Premera"). I reside in Anchorage, Alaska. I have the primary responsibility for Premera's contract with the State of Alaska ("State") for administration of its self-funded health plan. I was involved in the procurement process, including the discussions and agreement among Premera, the State, and Aetna. Prior to my current role I was Vice President of Health Care Delivery Systems for Premera for 2 years. I have a Masters in Health Services

Administration. I am competent to make this affidavit, and do so on the basis of personal knowledge except as may be otherwise stated below.

2. On December 28, 2005, Premera submitted a proposal in response to Request for Proposals No. 2007-0200-5946 ("RFP"), issued by the Department of Administration, Division of General Services ("Division") to solicit administrative services for the State's self-funded health care benefit program. Premera's cost proposal at that time was in the amount of \$34,390,750.

3. On February 7, 2006, the Division sent Premera an e-mail with questions on twenty-one areas of Premera's technical proposal. Later the same day, the Division asked Premera a few additional questions and requested assurance that all components of its program would be administered for the stated fees.

4. On February 13, 2006, Premera responded in writing to Division's questions and submitted a best and final cost proposal of \$34,077,274 over 3 years.

5. The Division e-mailed two pages of additional clarification requests to Premera on February 14, 2006. Premera responded to those requests the same day.

6. I participated in the series of telephone conversations among the Division, Premera and Aetna on February 22 and 23, 2006. During those calls we learned from the Division that after issuance of the Notice of Intent and during conversations between the Division and Aetna to which Premera was not a party, the Division discovered it had overlooked part of Aetna's proposal. The Division also stated that it had disclosed the total amount of Premera's best and final cost proposal to Aetna.

7. During the first telephone conference, the Division outlined what had happened

and how it planned to remedy the situation. It stated it intended to proceed with the procurement process in the following manner: 1) evaluate Aetna's proposal and, assuming the Aetna proposal was determined to be responsive and reasonably susceptible for award; 2) share Aetna's original cost proposal with Premera in an attempt to put the parties in as comparable a position as possible (given the Division's earlier disclosure of Premera's best and final cost proposal); 3) solicit new best and final offers from both Premera and Aetna; 4) conduct discussions with offerors; and 5) after reviewing the final offers, issue a new notice of intent to award a contract.

8. The parties recognized there was an inherent inequity created by the disclosure of Premera's best and final cost proposal. The Division explicitly recognized that it "could not level the playing field" to remove this competitive disadvantage to Premera.

9. The Division, Aetna and Premera discussed the nature of the disclosure that had been made of Premera's cost proposal and agreed to confirm what had been disclosed and provide for mutual disclosures of some type of Premera's and Aetna's cost proposals. In a discussion of options to the process outlined by the Division, Premera proposed a process whereby Aetna would submit a preliminary best and final offer, to be disclosed to Premera, followed by final best and final offers from both parties. That proposal was not accepted by the Division and Aetna.

10. The parties also discussed at length the makeup of the proposal evaluation committee that would evaluate Aetna's proposal. The Division varied the names of the individuals who would be responsible for the evaluation--Freda Miller, Pat Shier, and Judy Carter--and described their job titles and responsibilities.

11. Because no agreement was reached on February 22, 2006, the parties reconvened by conference call the next morning, February 23, 2006. Mike Robinson stated on behalf of Aetna that it recognized this was a challenging situation and that, while it did not view the proposed process as ideal, it was willing to agree to the Division's original proposal.

12. Premera suggested a modification to the Division's proposal similar to the alternative that it had proposed the previous day. It proposed that Aetna submit an initial best and final proposal, and only if that cost proposal was less than Premera's existing cost proposal, would the parties go to final best and final offers. Premera based this approach on a desire not to be required to bid against itself should Aetna not submit a superior cost proposal.

13. Following a caucus, the Division declined Premera's proposal. After additional discussions, the parties reached an agreement which was memorialized in a document drafted by the Division and signed by the parties ("Agreement").

14. At several points during the calls on February 22 and 23, the Division solicited questions from Premera and Aetna and provided responses. In my opinion, there was more than ample time and opportunity for the parties to raise questions, offer suggestions, discuss issues, and explore alternate solutions.

15. During those calls, Aetna did not raise any questions as to the areas where they now challenge the Division's actions. For example, at no time during the several conference calls and extensive questioning and discussions which took place on February 22 and 23, 2006, was there any proposal by Aetna for discussion, much less agreement,

that the Division would start all over with a new technical evaluation of both proposals after the submission of the final best and final offers. Nor was there any statement by the Division that the technical evaluation of Aetna's proposal would be conducted by an evaluation team constituted exactly the same as that which had evaluated Premera's technical proposal.

16. Premera was informed on February 24, 2006, that the Division had completed its initial evaluation of Aetna's proposal as provided for in Paragraph 1 of the Agreement, and found the proposal to be responsive and reasonably susceptible for award. The Division then confirmed the cost proposal contained in Premera's initial best and final offer, \$34,077,274, and informed Premera of those contained in Aetna's proposal, \$49,163,735/\$45,237,171.

17. On February 24, 2006, the Division sent 3 new questions to Premera and conducted a telephone conference to allow us to provide clarification in response to the questions.

18. On February 28, 2006, Premera submitted a new best and final offer to the State. Premera reduced its administrative cost proposal to \$30,951,035. It also provided a guaranteed pharmacy rebate of \$3 million per year, based on a minimum number of pharmacy claims; doubled the amount of dollars Premera put at risk on the performance guarantees; and eliminated the network access fee. The revised financial proposal increased from 12% to 30% the percentage Premera would pay to the State in case it did not meet the guaranteed network savings amount of \$100 per member per month and similarly increased from 12% to 30% the amount Premera would be paid by the State for

amounts saved above the guaranteed savings. Premera reaffirmed its promise to save the State \$15 million per year compared to its current claims costs. (See letter from Gubby Barlow to Walt Harvey dated February 27, 2006, attached hereto as Exhibit 1.)

19. Based on Premera's superior proposal, the Division issued a new Notice of Intent to Award to Premera on February 28, 2006. The Notice of Intent specified that the Division determined that Premera's proposal was superior to Aetna's on both the cost and technical components. Premera scored 4,618.5 points to Aetna's 4,482.5. On March 13, 2006, the Division and Premera entered into a contract (the "Contract") for performance of this work.

20. Premera has been working diligently to implement the Contract, so as to ensure a smooth transition of the administrative responsibilities from Aetna to Premera. In particular, Premera wants to make certain that the State's employees and retirees do not have a disruption in service and that Premera meets its contractual commitments. Due to the short time between contract award and the date services begin, Premera has mobilized a dedicated team including representatives from all areas of its business to meet the implementation timeline.

21. As of April 28, 2006, the date of filing of this statement of position, Premera will have spent or irrevocably committed to the expenditure of over \$1.2 million for implementation of the State's business. By May 15th, the date by which a final decision in this case is expected, the amount incurred by Premera will be approximately \$2.3 million. Examples of Premera's implementation work as of April 28 includes: 1) completed implementation project planning; 2) various personnel hired, including

operations manager, care facilitation specialists, customer service representatives; 3) identification card designed; 4) membership and billing procedures developed; 5) purchased Ingenix PHCS System for provider reimbursement; 6) established banking arrangements, including appropriate accounts; 7) worked on finalizing contracts with vendors; 8) established toll-free numbers for 24-hour per day healthline and employee assistance program (EAP) provider; 9) held frequent meetings with the State to reach agreement on implementation details; 10) initiated system changes necessary to support the State's program; 11) developed required reports; and 12) entered into a letter of intent to lease office space in Juneau and started to build out that space.

22. Premera will be prepared to administer the contract by the July 1 date for the commencement of services because it has diligently executed its duties under the contract with the State.

23. In my opinion, Premera's nationwide network discounts are significantly better than those available through Aetna. As a result, Premera provides performance guarantees to certain groups based on savings from its network discounts. Premera has proven that it is able to deliver on those guarantees. For example, Premera won another major national account from Aetna as the third party administrator for its health benefits plan in 2003. For that customer, Premera guaranteed network savings of 36%, which were greater than the prior carrier's discounts, and has met that commitment.

Dated this 28 day of April, 2006.


Jeff Davis

SUBSCRIBED AND SWORN TO before me this 28th day of April, 2006.

Heather Ellen Marshall aka Scott

Notary Public in and for the State of WA

My commission expires: 10-8-06

Printed Name: Heather Ellen Marshall
aka Scott





February 27, 2006

Mr. Walt Harvey
Contracting Manager
Department of Administration
Division of General Services
333 Willoughby Avenue, 7th Floor State Office Building
Juneau, AK 99811-0203

Dear Mr. Harvey:

Thank you again for the opportunity to provide additional clarification and our "Best and Final" offer. I am personally pleased to reaffirm our commitment to the State of Alaska. I believe Premera Blue Cross Blue Shield of Alaska is uniquely qualified to deliver the lowest net cost while providing outstanding service to the State of Alaska and its members.

The highlights of Premera Blue Cross Blue Shield of Alaska's proposal to the State include:

▪ **Significant Claims Savings:**

The State of Alaska will achieve at least **\$45 million in net additional claims savings in the next three years (before health cost inflation)** through the use of the Blue Cross Blue Shield networks. These savings are over and above the savings now achieved using your current administrator's network, and after sharing any upside performance with Premera. To support this claim, we have reduced our administrative fees by 10%, eliminated our pharmacy fees and network access fees, plus placed additional amounts at risk for claims discount performance. In other words, the State will not pay unless Premera Blue Cross Blue Shield of Alaska delivers the network claims savings. Meeting our savings commitments was a big element to our success with Microsoft and Weyerhaeuser; both clients will be happy to validate this achievement.

▪ **No Surprises:**

The State of Alaska will have the security of an all-inclusive fee arrangement, other than for clearly identified optional services. This includes removal of the pharmacy administration fee proposed when the State requested receipt of full pharmacy rebates, as well as removal of the separately billed charge for use of the national BlueCard network. Additionally, we have now included 65 hours of training provided by Compsych, the EAP vendor partner.

▪ **Guaranteed Results:**

In addition to waiving our pharmacy administration fee, we are now guaranteeing a minimum of **\$3 million in annual pharmacy rebates**. Moreover, the State can also share our confidence in our ability to meet our commitments as we are **doubling the dollars at risk** in our other Performance Guarantees in each category.

- **Superior Service:**

The State will experience **Premera's outstanding service to members.** Both Microsoft and Weyerhaeuser named Premera their Benefits "Vendor of the Year." Extensive planning is **already well underway** on the implementation of this account –and you have my personal commitment that the State of Alaska can expect a similar experience.

- **Local Presence:**

The State will collaborate with Premera's **Alaska-based leaders** who understand the unique challenges of the Alaska health-care environment and will partner with an organization which has been providing service to Alaskans for the last 50 years.

Again, thank you for the opportunity to reaffirm the unique advantages of Premera Blue Cross Blue Shield of Alaska. You have my assurance that we will provide health benefits, service and savings with the highest level of integrity and quality. We are ready to be your partner.

Sincerely,



H. R. Brereton (Gubby) Bartow
President and CEO

Copy:

Heyward Donigan, EVP and Chief Marketing Executive
Jeffrey Davis, VP and General Manager, Alaska Market
Barbara Russell, Director of Sales, Alaska Market

Enclosure

Appeal

LAW OFFICES OF
SIMPSON, TILLINGHAST & SORENSEN, P.C.

ONE SEALASKA PLAZA, SUITE 300
TELEPHONE 907-586-1400

JUNEAU, ALASKA 99801
FAX 907-586-3065

HAND DELIVERED

March 28, 2006

The Honorable Scott Norstrand
Commissioner of Administration
Alaska Department of Administration
10th Floor, State Office Building
Juneau, Alaska 99811-0200

Re: Appeal of Denial of Protest of Intent to Award in
RFP No. 2007-0200-5946

OUR FILE NO.: 14671

Dear Commissioner Norstrand:

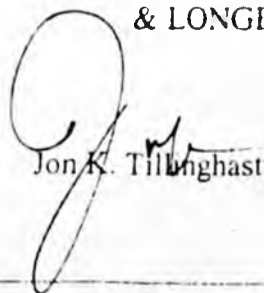
Enclosed, pursuant to AS 36 30.590, is the Appeal of Aetna Life Insurance Company and Aetna ("Aetna") of the procurement officer's denial of Aetna's protest in the above-captioned matter. The appeal and supporting documentation include all of the material required by that statute.

Aetna would respectfully request that your office immediately transfer this appeal to the Office of Administrative Hearings under AS 44 64.060. Given that you have already announced your recusal from this matter, Aetna does not believe there is any purpose served by retaining the file at the Department of Administration, and the parties to this proceeding will have need of current access to a hearing officer to establish procedures for resolution of the merits of this case.

The purpose of this letter is also to advise you that, pursuant to my telephone conversation with Asst. Attorney General Margie Vandor, the procurement office is being simultaneously served with this appeal by service on Ms. Vandor.

Sincerely,

SIMPSON, TILLINGHAST, SORENSEN
& LONGENBAUGH



Jon K. Tillinghast

1 ¶13. A subsequent phone call to Mr. Walt Harvey, the employee who had replaced Mr.
2 Leamer as procurement officer, disclosed that the Division had lost the meat of Aetna's
3 proposal, consisting of some four boxes of binders in which were contained a critical
4 portion of Aetna's overall proposal. *Id.* Over those two intervening months, the
5 Division had never simply contacted Aetna (who, through itself and its affiliates, had
6 been providing these services to the State for the past 24 years), and asked why there
7 was such a gaping omission in its bid. Rather, the Division simply declared Aetna
8 "nonresponsive" for failure to submit a complete bid. *Id.*^{1/}

9 The initial award to Premera was therefore, and in essence, predicated on the
10 erroneous conclusion that Premera was the sole responsive bidder.

11 The Division initially scored Premera's proposal under the RFP's point system
12 around January 20, awarding it 1489.5 points for the more subjective, technical elements
13 of the RFP (called here the "Non-Cost Factors"), which counted the most (50%) in
14 proposal evaluation. *See Section VI post. See also Chart I (attached directly to this*
15 *memorandum). See Attachment 5(c).*

16 Shortly thereafter, the Division began extensive private communications with
17 Premera aimed at improving its offer. These included 21 pages of questions on
18 Premera's proposals for various Non-Cost Factors in the RFP, each question being
19 designed to solicit a more beneficial answer. *Attachment 4(a)*. Premera answered those
20 questions in a 49-page reply on February 13, 2006. *Attachment 4(b) at 7-56. See,*
21 *generally, Section VIII, post.*

22
23
24 ^{1/} In rejecting Aetna's protest, the procurement officer claimed that it would have been improper
25 to contact Aetna, as the receipt of late bids is prohibited. *Attachment 10 at 3*. The purpose of such
26 a query, however, would not have been to solicit a late bid. Rather, it would have been to enquire

Aetna, of course, knew nothing of any of this

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As a result of Premera's answers (and even though Premera ostensibly had no competition at this point, Aetna's proposal still being lost), the Division rescored Premera's proposal on February 16-17, 2006, *Attachment 5(d)*, *Attachment 11 (email response from Walt Harvey)*. The Division's extensive work with Premera had succeeded in increasing Premera's point total for the Non-Cost factors by 629 points—to 2119 points. *Attachment 5(d) at 1-2, Chart 1*

One day after this re-scoring, the Division issued its initial Notice of Intent to Award, and Aetna placed its phone call to the Division. After considerable pleading by Aetna that it had timely delivered a comprehensive and complete proposal, the Division looked again, and found all of the missing boxes in a store room after a mere hour's search. *Id.* at ¶14.

The State promptly rescinded the Notice of Intent, and commenced another evaluation process that is the subject of this protest. *Id.* at ¶17. This process is explained in (i) ¶17 of the *Mike Wiggins Affidavit*, (ii) a confirming memorandum found at *Attachment 2*, (iii) the *Fifth Affidavit of Mike Wiggins*, and (iv) the *Affidavits of Mike Robinson and Reed Stoops*, all of whom were participants in a phone conference that resulted in the agreement contained at *Attachment 2*. The essence of that agreement is as follows:

Because of vacation plans, the same full evaluation team that had scored Premera could not be reformed to evaluate Aetna's newly-found bid. To accommodate a quick resolution of the matter, Aetna agreed that the Division could "reconstitute" the original

into the inarguably odd fact that the huge middle of the incumbent contractor's bid was nowhere to be found.

1 evaluation team so that it "consist[ed] of three members, two of whom were on the
2 original [evaluation committee] that scored Premera's proposal." *Attachment 2* at ¶1
3 This "reconstituted" team would first perform a threshold evaluation of Aetna's newly-
4 discovered bid to determine whether that bid was "reasonably susceptible for award." *Id.*
5 ^{2/} By "reconstituting" the team in this manner, Aetna was assured that the scores of the
6 "reconstituted" committee would be as comparable as possible to the scores of the
7 original committee, since 2/3 of the scores of the "reconstituted" committee would come
8 from individuals who had actually also scored Premera. *Robinson Aff.*, ¶7; *Stoops Aff.*,
9 ¶6. *Fifth Wiggins Aff.*, ¶7. ^{3/}

10 Unfortunately, the Division breached the agreement, and appointed only one
11 person who had actually scored Premera to the "reconstituted" committee. Neither of
12 the other two members of the "reconstituted" committee had scored Premera on either of
13 the two Premera scorings. *Section VII, post, see also Chart I and pp 1-2 of Attachments*
14 *5(a)-(d)*. ^{4/}

15 There was then a second undisclosed breach of the agreement. After the
16 "reconstituted" committee completed its initial scoring of Aetna, and if Aetna's proposal
17 passed its threshold evaluation (which it did [*Wiggins Aff.*, ¶18]), the agreement
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20 ^{2/} Under Alaska's procurement code, the Procurement Officer is allowed to discuss first
21 proposals, on an even-handed basis, with all bidders who are "reasonably susceptible of being
22 selected for award," and this for the purpose of ultimately soliciting a "best and final offer" from
23 this final pool of bidders. AS 36.30.240. This initial process does not constitute a scoring of one
24 proposer against another, but rather a look at the intrinsic strengths and weaknesses of a proposal,
25 so as to see whether, if improved, it might plausibly become the "best and final offer."

26 ^{3/} It is worth noting that Aetna would have been well within its rights to demand that the
Division comply with 2 AAC 12.260(a), and have its "found" proposal evaluated by exactly the
same "committee" that had evaluated Premera's bid. Aetna was being collegial here. But as we
shall shortly see, no good deed goes unpunished.

^{4/} Aetna had no knowledge of the Division's breach at the time, and thus no opportunity to
correct it.

1 provided that each party would have the opportunity to submit a best and final offer. In
2 conjunction with that best and final offer, the Division would contact both parties to
3 obtain new responses on Non-Cost Factor issues that were of concern to the Division.
4 *Attachment 2, ¶3* Once those offers, and the parties' answers' to the Division's
5 questions, were submitted, the agreement provided that "both proposals will be scored,"
6 and a winner would be selected. *Id.* at ¶4.

7 It was Aetna's understanding that this paragraph meant that the entire "proposal"
8 (both cost and Non-Cost Factor components) would be evaluated. *Robinson Aff.* ¶10.
9 This was very important to Aetna, since this last scoring would be the only opportunity
10 when both proposals would be re-scored by single, identical review committee--the so-
11 called "reconstituted" committee. *Id.*

12 Indeed, until the Division responded to Aetna's protest on March 21, 2006 (*see*
13 *Section V, post*), Aetna had assumed that a Premiera scoring tally entitled "2nd Score
14 *After Best and Final, Premiera*" and found at *Attachment 5(d)* was the promised scoring
15 of Premiera's last proposal by the "reconstituted" committee. It was not until service of
16 the Division's response to Aetna's protest that Aetna learned that, contrary to ¶4 of the
17 agreement, there had been no rescoring of Premiera's Non-Cost Factors by the
18 "reconstituted" committee. Rather, the rescoring found at *Attachment 5(d)* was actually
19 the rescoring of Premiera's proposal that had been done on February 17—before Aetna's
20 "lost" proposal had been found. *Attachment 10 at 8-10, Attachment 11*

21 Apparently, the only things done with the parties' final proposals under the
22 agreement were a comparison of the new cost bids, and a brief revisiting of three Non-
23 Cost topics in Aetna's final proposal. *Attachment 10 at 9*. It was on that basis that the
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1 Procurement Officer issued his February 28 Notice of Intent to award the contract to
2 Premera.

3 And so, at the time the final Notice of Intent Award had been issued, Aetna's and
4 Premera's final proposals have never been scored by either an identical review
5 committee, nor even by separate committees that had more than one common member
6 between them.

7 And yet despite all the disadvantages thrown Aetna's way in this unfortunate
8 process, when all was said and done, out of a 5000-point evaluation process, Premera
9 was able to top Aetna by only 141 points

10 III. Aetna's Protest

11 Aetna's protest is appended as *Attachment 9* to this Appeal. In a nutshell, Aetna
12 claimed that the procurement

- 13 o violated state statute (AS 36 30 240) and regulation (2 AAC 12 290(a)), and
14 created an appearance of impropriety that undermined the integrity of the
15 competitive bidding process, because, while the Department held prolonged and
16 extensive discussions with Premera to produce its "best and final offer," the
17 counterpart discussions with Aetna were only perfunctory. Because state law
18 requires that all proposors be accorded fair and equal treatment with respect to
19 any opportunity for discussion and revision of proposals" (AS 36 30.240(a)), and
20 "[t]he opportunity for confidential discussions, if held, must be extended to all
21 offerors submitting proposals deemed reasonably susceptible for award" (2 AAC
22 12 290(a)), Aetna contended that the procurement was illegal and subverted the
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competitive process. It also contended that this process actually affected the outcome of the evaluation, and

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- ▷ For the "best and final offer" evaluation, the Division used separate evaluation teams to evaluate the two bidders, with only one member of these three-member teams being in common. Because many of the factors on which the evaluation was based were subjective, and hinged on personal idiosyncrasy, the absence of common evaluators rendered the evaluation useless for determining which proposal was "most advantageous to the state" as required by AS 36 30.250(a), and impaired, if not destroyed altogether, the integrity of the competitive bidding process.⁵⁷ Aetna also asserted that this procedure clearly affected outcome of the procurement. Nor did the process comply with 2 AAC 12 260(a), which only authorizes the Division to score RFP's through a single "evaluation committee."

13 **IV. Aetna's Request for a Stay of Award**

14 Contemporaneous with its protest, Aetna filed a request with the Procurement
15 Officer, pursuant to AS 36 30 575, to stay award of the contract pending disposition of
16 Aetna's protest and any subsequent administrative appeal. *Attachment 9 at Cover Letter.*
17 The Department never ruled on that request before simply going ahead, and signing the
18 contract. Without notice of any kind to Aetna, the Department executed the contract on
19 March 13, 2006.
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⁵⁷ A third issue raised in the protest—*i.e.*, that the Division failed to separately score an Aetna proposal to provide pharmaceutical claim services only (an alternative specifically called for the RFP), is not being appealed, and does not receive further discussion in this Appeal.

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V. The Procurement Officer's Response to Aetna's Protest; Identification of Erroneous Factual Findings and Resultantly Erroneous Legal Conclusions

On March 21, 2006, the procurement officer rejected Aetna's protest. *Attachment*

10 The procurement officer's principal findings and conclusions were as follows:

- o The Division had complied with the parties' agreement, and had evaluated Aetna's proposal using a three-person review team comprised of two persons who had actually scored Premera's first proposal,
- o The communications between the Division and Aetna, on the one hand, and Premera, on the other, were essentially equal,
- o Any difference in communications between the Division and Aetna, on the one hand, and Premera, on the other hand, did not create an appearance of impropriety,^{6/}
- o Neither the use of different evaluation teams nor the disparity in treatment between proposors affected the outcome of the procurement; and
- o The Division acted in good faith.

From these factual findings, the procurement officer drew the ultimate legal conclusion that Aetna's protest was without merit. As required by AS 36.30.590(b)(2), Aetna respectfully submits that each of the above-described factual findings was erroneous, and that if any of those findings is reversed, Aetna will be entitled to appropriate relief as a matter of law.

^{6/} "Whether an appearance of impropriety exists is a factual question." *In the Matter of J&S Services, Inc.*, Alaska Dept. of Administration Case No. 02-01 (Sept. 16, 2002) ("*J&S Services*") at 5.

VI. The Nature of the Contract Being Awarded⁷

To evaluate Aetna's claims, a brief background on the contract at issue here is warranted

The services for which the RFP solicited proposals were to provide a wide range of medical and pharmacy insurance claim management services to the State. *Request for Proposals*, §1.03. ^{7/} Those services have been provided economically and efficiently by Aetna itself, or through its affiliates, for some 24 years. *Wiggins Aff.*, ¶4. The State of Alaska self-insures both its medical and pharmaceutical claims; however, it still needs an agent to evaluate and process those claims. *Third Wiggins Aff.*, ¶5; *RFP*, §6.06. The agent charges a per-employee and per-retiree fee for providing those administrative services, and its proposal consists, in part, on the proposed amount of those fees. *Id.*, *RFP at Section 7.23*.

However, because many factors other than cost bore on the State's choice of suppliers (factors such as expertise, system compatibility, ability to serve clientele, and the like), a "Request for Proposal" format was utilized, rather than a Request for Sealed Bids. Under the RFP, cost accounted for only 40% of the total bid evaluation, all the other relevant factors (loosely called "Non-Cost Factors") were in the technical portion of the RFP, and were collectively allocated 50% of the total scoring. *RFP*, §10. ^{8/} As to those Non-Cost Factors, each individual evaluator awarded points based upon that evaluator's personal judgment as to how the proposer dealt with each Non-Cost Factor.

^{7/} The lengthy RFP for this contract has not been appended as an exhibit to this Appeal because of its bulk. It is on file with the Procurement Officer, and Aetna would respectfully request that it be made part of this Appeal record by reference.

^{8/} The remaining 10% was allocated for preference points.

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When the so-called "best and final" proposals were opened, the cost of the two responsive proposals appeared virtually identical. On the cost side, Premera was awarded 2000 points for having the lowest cost bid, while Aetna was awarded 1930 points for having a cost bid that was only marginally higher than Premera's. *Attachment 10* at 7. However, Premera's cost bid was understated (and in fact materially higher than Aetna's) because some large costs that should have been included as part of Premera's administrative fees were in fact disclosed only in other, more subjective portions of Premera's proposal that are not added into the cost component of the proposal. See, generally, *Affidavit of Matt McGuinness*.

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VII. The Department Violated AS 36.30.250(a) and 2 AAC 12.260(a) by Using Different Evaluation Teams to Score the Two Applicants, Making it Impossible to Determine Which Proposal was "Most Advantageous to the State." The Division Erred in Finding that: (a); Aetna Had Agreed to this Process; and (b) any Error did not Affect the Outcome of the Procurement.

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A *In the absence of any agreement, the use of different evaluation teams to score different proposals is unlawful, and in this case affected the outcome of the procurement.* In its decision on Aetna's protest (*Attachment 10*), the Division does not contend that, absent some special agreement, it is permissible to use two different evaluation committees to score two different proposals under an RFP. After all, 2 AAC 12.260(a) only authorizes the Division to review RFPs through an "evaluation committee," *singular*, and for good reason.

1 The ultimate goal of the competitive bidding process—the one on which its
 2 “integrity” turns—is to provide “the opportunity to compare multiple responsible bids.”
 3 *Laidlaw Transit Inc v Anchorage School District*, 118 P 3rd 1018, 1033 (Alaska 2005),
 4 *emphasis added*. Any error that undermines the State’s ability to meaningfully compare
 5 competing proposals deprives the public and the courts of any basis to assess the legality
 6 of the agency’s choice.

7 In this case, the points for Non-Cost Factors were awarded based on an evaluation
 8 of largely qualitative (as opposed to quantitative) factors, ranging from the suitability of
 9 appeals procedures to transition and training concerns. *Wiggins Aff.*, 143. Points were
 10 awarded based on how individual evaluators reacted to the proposer’s approach to a long
 11 list of subjective issues—responses that would translate into very different point totals
 12 among different evaluators, depending on each evaluator’s individual background,
 13 grading policies and priorities.

14 The evaluators’ separate final scores for the subjective, 50% Non-Cost Evaluation
 15 illustrate how idiosyncratic this scoring process really was:

Evaluator	Evaluated	Score
Miller	Aetna	2440
	Premera	2160
Gray	Premera Only	2207
Porter	Aetna Only	2120
Williams	Premera Only	1990
Shier	Aetna Only	1585

SIMPSON, TULLINGHAST & SORESEN
 One Sealaska Plaza, Suite 300
 Juneau, Alaska 99801
 (907) 586-1400 FAX (907) 586-3065

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Attachment 5(b) and (d) at 1-2 The Division then took the average of each evaluator's scores (i.e., Aetna's score was based on the average of Miller's, Porter's and Shier's evaluation, while, Premera's was based on the average of Miller's, Gray's and J Williams' evaluation), and (because of the near-identity of the cost score), the proposer with the highest average evaluation won.⁹

It is also apparent that compromising the rating process by using non-comparable, idiosyncratic scoring affected the outcome. For example: (i) the only evaluator who evaluated both applications, Ms. Miller, rated Aetna significantly higher than Premera, while (ii) one of the evaluators who scored only Aetna (Shier) gave Aetna aberrationally low scores (535 points lower than Porter), and 855 points lower than Miller. Given that Premera ultimately received only 141 more points than Aetna, it is apparent that point swings of up to 855 points that were due entirely to the use of different evaluators plainly affected the procurement's outcome.

B. *Aetna did not agree to this procedure.* The Division's only defense to its unusual procedure here is that Aetna agreed to it. *Attachment 10 at 5-9* Aetna agreed to a process, but it did not agree to this process.

As discussed in *Section II, ante*, the parties' February 24, 2006 agreement provided that both Aetna's and Premera's final proposals would be reviewed by a so-called "reconstituted" Procurement Evaluation Committee (or "PEC") that would

consist[] of three members, two of whom were on the original PEC that scored Premera's proposal in the initial evaluation process

⁹ *Attachment 5(b) at 2 (Aetna "best and final" summary sheet), Attachment 5(d) at 2 (Premera "best and final" summary sheet)*

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Attachment 2, ¶1, emphasis added The members "who scored Premera's" proposal," on the one hand, and the members of the "reconstituted" committee who scored Aetna's proposal, can be found in summary fashion on *Chart 1* to this memorandum, and more directly on the scoring tally sheets for both Aetna and Premera at pp. 1-2 of *Attachments 5(a)-5(d)*

From those documents, one can see that there was, in fact, only one member of the "reconstituted" team, and not two as the agreement requires, who had also "scored Premera's proposal." That lone individual was Freda Miller.

The Division's answer is that Mr. Pat Shier was also a member of the evaluation team that "scored Premera's proposal" *Attachment 10* at 5-6. That is not true. The evaluation team score sheets for Premera's first and second proposals are found, respectively, at pages 1-2 of *Attachments 5(c) and 5(d)*. The reader will see that Mr. Shier's name has been crossed off the list of evaluators on both score sheets, and not a single Premera scoring sheet contains any score from Mr. Shier.

The Division's explanation is that Mr. Shier did begin to score Premera's first proposal. But Shier abruptly ceased his partial scoring just over half-way through the scoring factors, left his half-done worksheet incomplete, was resultantly scratched off the Premera evaluation team, and was never heard from again on any Premera proposal, first or second.^{10/}

The reason that Aetna insisted that a majority of the reconstituted team be comprised of employees who had "scored Premera's proposal" was to ensure

^{10/} Shier's partial scoring of Premera's first proposal is found at *Attachment: 5(c), pp. 114-136*. The remaining items that Shier did not score can be found (in the evaluation sheets of a different reviewer) at *Attachment 5(c), pp. 159-170*.

1 comparability of Aetna's and Premera's scores *Robinson Aff.*, ¶7, *Fifth Wiggins Aff.*, ¶
2 7, *Stoops Aff.*, ¶6. Premera's first and second scores were not affected in the slightest by
3 Shier, and so an Aetna score that include scoring by Shier would be less comparable, not
4 more. As Mr. Robinson, who attended the negotiations and signed the agreement for
5 Aetna, explains:

6 *It never occurred to us, and it was never mentioned, that one of*
7 *the two "original" PEC members would be a member that did not*
8 *score Premera. Such an individual would have been of no value in*
9 *reconstituting a comparable-as-possible review team, and we would*
10 *never have accepted such a major change in the agreement.*

11 *Robinson Aff.*, ¶7.

12 It is frivolous for the Division to maintain that Mr. Shier was a member of the
13 evaluation committee "that scored Premera's proposal." The allegation, in fact, is the
14 best illustration of the Division's bad faith in this entire procurement process.

15 Finally, the Division breached its promise that "both [final] proposals will be
16 scored" by the "reconstituted evaluation committee." *Attachment 2*, ¶4. Instead, the
17 Division simply looked at the new cost component of the proposals and three minor items
18 in Aetna's new proposal. *Attachment 10* at 8-9.

19 Mr. Harvey explained that it is a "longstanding practice" to review only the cost
20 component of final proposals, unless changes to other components of the proposal had
21 been made. But the parties' agreement here had little to do with "longstanding
22 practice"—it was, in many respects, a very unique arrangement. The obvious rationale
23 for not rescoring unchanged portions of a final proposal is that the same evaluation
24 committee had already scored the unchanged portions. But here, there was a new,
25 "reconstituted" evaluation committee, and a comprehensive review of both parties' final
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1 proposals gave the Division its only chance to have both parties' proposals scored, from
2 top to bottom, by the same people

3 The importance of this level playing field was why Aetna took the agreement at
4 its word, and properly assumed that "proposal" meant the entire proposal, and not just a
5 portion of the "proposal" that represented only 40% of the scoring weight (*i.e.* the cost
6 component). *Robinson Aff.*, ¶10.¹¹ The Division's failure to follow the plain wording
7 of the agreement here makes it doubly difficult for the Division to justify its conduct on
8 the basis of that agreement

9 **VIII. The Division Violated AS 36.30.240 and 2 AAC 12.290, and Created**
10 **an Appearance of Impropriety that Actually Affected the Outcome of**
11 **the Procurement. By Engaging in Prolonged and Complex**
12 **Negotiations With Premera, But Only Perfunctory Correspondence**
13 **With Aetna, Before Soliciting "Best and Final Offers." The Division**
14 **Erred in Finding that: (a) the Communications with Aetna and**
15 **Premera Were Equivalent; (b) any Difference did not Raise an**
16 **Appearance of Impropriety or Influence the Outcome of the**
17 **Procurement**

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19 "The appearance of impropriety and impropriety in fact are sufficient to void
20 procurement contracts" *Paul Wholesale v State*, 908 P.2nd 994, 1000 (Alaska 1995).
21 *Dick Fisher Development No. 2 v Department of Administration*, 838 P.2nd 263, 269

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25 ¹¹ / Aetna's interpretation of ¶4 of the agreement is consistent with Section 7.26 of the
26 Agreement, which makes it clear the the "proposal" includes the offeror's responses to all of the
sections of the RFP, including, but not limited to, the cost section.

(Alaska 1992); *In the Matter of J&S Services, Inc.*, Alaska Dept of Administration Case No. 02.01 (Sept. 16, 2002) ("*J&S Services*") at 5.

The appearance-of-impropriety rule was applied in *Paul Wholesale*, 753 P.2nd 1132. In that case, DOT&PF cancelled all parties' rights in a procurement that had already resulted in a contract award to two different bidders because of certain alleged *ex parte* communications between one party and DOT&PF. In upholding DOT&PF's cancellation, the Supreme Court reaffirmed its holding in *Dick Fisher* that the appearance of impropriety was enough to void a procurement. Further, it held that "subjective bad faith," or actual "bias" on the part of the agency, is not required. Bad faith was only one relevant factor; equally important was "the amount of agency discretion and whether the agency violated the relevant law." *Id.* at 1002.

Similarly, in *J&S Services*, the hearing officer ruled that extensive *ex parte* communications between a member of the evaluation committee and one proposer created a "substantial and material appearance of impropriety." *Id.* at 7.

In assessing whether apparent impropriety warrants relief, one relevant consideration is whether the impropriety violated specific statutes and regulations written to avoid that impropriety. *Paul Wholesale*, 908 P.2nd at 1002; *J&S Services*, *ante* at 7; *Keco Industries v. United States*, 492 F.2nd 1200, 1203 (Cl. Ct. 566 (1974)). Here, there exist specific statutory and regulatory prohibitions on precisely the kind of one-sided, *ex parte* communications in which Premera and the Division engaged.

Under AS 36.30.240 and 2 AAC 12.290, the Division may discuss proposals with proposers who are "reasonably susceptible of being selected for award" in order to flush

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out proposal details, and, those discussions can lead to changes in the proposer's so-called "best and final offer" ^{12/}

This authority, however, is subject to a caveat—that all such proposers "shall be accorded fair and equal treatment with respect to any opportunity for discussion and revision of proposals" (AS 36 30 240(a)), and that "[t]he opportunity for confidential discussions, if held, must be extended to all offerors submitting proposals deemed reasonably susceptible for award" 2 AAC 12 290(a)

Ostensibly under these laws, the Division held extensive discussions with Premera which had the effect of giving Premera detailed advice on how to

- retract portions of their proposal which, absent a retraction, would leave Premera's proposal unresponsive to the RFP.

^{12/} In addition, 2 AAC 12 285 permits the Division to communicate with an offeror and ask clarifying questions to eliminate confusion concerning the contents of a proposal, but the questions may not result in a substantive change in the proposal. 2 AAC 12 285 does not avail the Division here. Section 12 285 says

In order to determine if a proposal is reasonably susceptible for award, communications by the procurement officer or the procurement evaluation committee are permitted with an offeror to clarify uncertainties or eliminate confusion concerning the contents of a proposal which does not result in a material or substantive change to the proposal.

Emphasis added. The extensive discussions between the Division and Premera from 2/12/06 to 2/14/06, concerning Non-Cost Factors, resulted in a near 50% increase in Premera's point total from 1489.5 to 2119. *Chart 1, Attachment 5(c) at 1-2, Attachment 5(d) at 1-2.* The additional points were the product of Premera's significantly changing its answers to many RFP questions. *See Attachment 4(b) at 7 et seq.* And, further discussions between the Division and Premera, on 2/24/06, enabled Premera to lower its Best and Final proposal by more than \$6.88 million in costs. *Wiggins Aff ¶¶ 2-11, McGuinness Aff ¶¶ 10-23.* All of these changes to Premera's proposal were obviously material and substantive, and therefore beyond the scope of 2 AAC 12 285. Moreover, that regulation authorizes only "clarifying" questions. The questions asked by the Division here were not "clarifications," but rather suggestions by the Division to Premera to change its proposal. *See text, post.*

- insert items required to be included in the RFP, but originally omitted by Premera, and
- suggest available contract administration measures that could result in lower cost, or increased evaluator attractiveness, and hence higher point scores.

Wiggins Aff ¶¶ 21-29, Attachments 4(a) and 4(b) Premera accepted virtually every suggestion given by the Division, and as a direct result (1) Premera's gross point total from its Non-Cost factor evaluation rose by 629 points from its original proposal, and (2) Premera was able to move \$6.88 million in real, direct costs to the State into a category that was not counted as a proposed "cost," resulting, in turn, in a \$6.88 million understatement of its Best and Final cost bid. *Compare Attachments 5(c) and 5(d), Wiggins 3rd Aff ¶¶ 2-11, McGuinness Aff ¶¶ 10-23, Attachment 4(b) at 58, Attachment 4(c) at 1*

On February 7, 2006, the Division began extensive private communications with Premera aimed at improving its offer.¹³ On February 12-14, the Division and Premera exchanged 62 pages of "clarification" questions and answers on Premera's proposals for various Non-Cost Factors in the RFP, each question being aimed at soliciting a more beneficial answer. *Attachment 4(a) at 2-19, 4(b) at 7-56*. At the conclusion of these communications, the Division rescored Premera's heavily-revised proposal and, as a direct result of the Division's efforts to make Premera's proposal more attractive, Premera's proposal gained 629 points in the Non Cost Factor category—a near 50%

¹³ / Email messages document at least three private conversations between the procurement officer and Premera officials (on February 7, 9 and 15). *See Attachments 4(a) at 1 & 20-21 and 4(b) at 6*

increase in Premera's point total. See Chart 1. Compare Attachments 5(c) and 5(d). pp 12

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2 Aetna was never offered any similar opportunity, leaving Aetna so far behind the
3 competitive curve that even Department of Administration Commissioner Nordstrand
4 was forced to admit to the Alaska Legislature that the playing field was "[n]ot entirely
5 level" because the answers Premera resubmitted to the Division on February 14, 2006
6 were the equivalent of a "second offer." Attachment 12 at 24

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8 The second round of questions occurred on February 24, 2006, during the
9 evaluation process called for by the parties' agreement, when the Division asked
10 questions of both Aetna and Premera pursuant to paragraph 3 of that agreement
11 Attachment 2. Here, the different treatment that the Division gave Aetna and Premera
12 was substantive. Aetna, on the one hand, was given only three pages of minor, technical
13 suggestions that ultimately resulted in awarding a mere 21 extra points to Aetna (*Wiggins*
14 *Aff.*, ¶ 19, Attachment 3). Conversely, the Division's communications to Premera gave
15 Premera a clear road map as to how to reclassify \$6.88 million of its proposed costs to a
16 category that would not appear in the "cost" section of the bid, and thereby artificially
17 lower Premera's cost bid by that same \$6.88 million. *Third Wiggins Aff.*, ¶¶ 2-11, see
18 also *McGuinness Aff.* ¶¶ 10-23, see also text, post

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20 And so, while Premera benefited from the Division's extensive communications
21 by an 629 additional points and was also able to decrease its cost proposal by more than
22 \$6.88 million in its final bid, Aetna's perfunctory dialogue with the Division yielded it
23 only 21 additional points. Compare Attachments 5(a) and 5(b) with Attachment 5(c) and
24 5(d)

The relative impact of those questions on the scoring process was as follows:

COMPANY	EXTENT OF BIDDER QUESTIONING	ADDITIONAL POINTS FROM ANSWERS COST BID IMPACT
Premera	62 pages of questions and answers, several private conversations	629 points \$6.88 million cost bid reduction
Aetna	3 pages of questions	21 points No cost bid impact

The extra points granted to Premera were doubly significant:

- First, in the initial grading of the two proposers (the grading of the initial proposals, before the Division's extensive assistance to Premera), Aetna won the Non-Cost Scoring portion (i.e. the 50% of the bid that reflects proposal quality) by 541 points. Compare Attachments 5(a) and 5(c), while
- Second, even after its extensive assistance from the Division, Premera was able to beat Aetna's Non-Cost score by only 71 points. Compare Attachments 5(b) and 5(d). It is apparent, then, that without these extensive suggestions from the Division, Premera would not have won the Non-Cost Scoring on the final "best and final" round. The summary of all of these scores is contained in Chart 1, which is appended to this appeal.

As a result, the impropriety plainly affected the outcome of the solicitation — another factor counseling for relief. *Keko*, 492 F.2d at 1203; *J&S Services*, ante at 6.

Because of the potential for abuse in private bidder/agency conversations, courts are insistent on all qualified proposers in an RFP being given the "same opportunity" in curing proposal shortcomings. *Gunderson v University of Alaska, Fairbanks*, 922 P.2d

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229, 235 (Alaska 1996) "Fair" contract solicitation, and demanding that no proposer "receive[] an unfair competitive advantage," are critical to ensuring that the best possible offer emerges from the bidding process. *McBirney & Associates v. State*, 753 P.2nd 1132, 1135 (Alaska 1988)

Hence, Aetna was entitled to equal treatment in post-opening discussions with the Division. Indeed, because of the obvious potential for abuse in statutes giving bidding agencies the authority to engage in private conversations with qualified RFP proposers, courts have been especially alert in demanding equality in the substance of those communications, and not just in form.

Here, the danger of apparent inequality emerges from the Division's own wording in its questions to Premera. Time-and-time again, the Division asks Premera to "clarify" a point that needed no clarification. In one class of cases, for example, Premera's original offer unequivocally rejected a condition of the RFP. The Division, instead of simply asking Premera to reverse its position, asked it to "clarify" that it would accept the condition, despite the fact that its original proposal made it clear that it would not. Capable of taking a hint, Premera routinely agreed to "clarify" that it would, after all, abide by the RFP, which resulted in material and substantive changes to Premera's proposal.

Mr. Mike Wiggins offers several examples of this in his affidavit (*id.* at ¶¶ 21-29, *Wiggins 3rd Aff.* ¶¶ 2-11), including the following:

The RFP asks the offeror to agree that it will answer 85% of all telephone calls within 30 seconds in any given month, or face penalties. RFP, §10 11(a)(1). In its original proposal, Premera "disagreed" with this element of the RFP. ... This caused Premera to lose points on this issue in its first proposal, receiving only 2 points from one evaluator (Gray) and 0 from another (Williams) out of a possible 5 points. ... To raise Premera's

1 point total, the Department asked Premera to "clarify" that it would answer
2 85% of all calls on a monthly basis, despite what it said in its proposal ... In
3 response to the State's suggestion that Premera change its position, Premera
4 agreed to the State's demand. ... As a result, Premera received 3.5 added
5 points from one evaluator (Gray) and additional points from another
6 (Miller) in its "best and final" proposal.

7 *Id.* at ¶21. In a similar vein: (1) Premera clearly declined to offer direct deposit in its
8 original offer, but was convinced by the Division to change its mind (*id.* at ¶22), and (2)
9 the Division asked Premera to "agree" to a service that it had unequivocally not agreed to
10 provide in its proposal. *Id.* at ¶23. Additional "clarifications" that in fact resulted in
11 significant point increases and cost decreases are given as examples at ¶¶23-29 of Mr.
12 Wiggins' affidavit, and *Attachments 4(a) and 4(b)* are rife with them.

13 Wiggins and Mr. Matt McGuinness also discuss in their affidavits how the
14 Division suggested the re-packaging of nearly \$6.88 million of "Network Access Fees,"
15 which effectively helped lower Premera's Best and Final cost proposal by at least that
16 amount. *Third Wiggins Aff.*, ¶¶ 2-11, see also *McGuinness Aff.*, ¶¶ 10-23. Premera's
17 initial bid was understated by a significant amount, since its \$34 million bid did not
18 include \$6.88 million in "Network Access Fees." *Wiggins Aff.*, ¶ 10. Premera
19 accomplished this by calling these fees "claim charges," which are not included in the
20 cost portion of the bid. *Id.* ¹⁴ The Division advised Premera, in "clarification"
21 questions dated February 24, 2006, that these "Network Access Fees" were not "claim
22 charges" and needed to be billed in a different manner. *Attachment 4(b) at 2 & 57*.
23 Premera informed the procurement officer, in its February 28, 2006 Best and Final

24 ¹⁴ / The "cost" of the proposal to the State (which, again, is worth 40% of the total proposal) is
25 supposed to be disclosed in response to Section 7.23 of the RFP. In all fairness, all costs being
26 charged to the State as a result of the proposal should be included in the response to Section 7.23.
The point of this narrative is that, in Premera's case, they were not

1 Response, that these fees were "eliminated." *Attachment 4(b) at 57*. Those fees,
2 however, were not "eliminated." Rather, Premera merely removed "Network Access
3 Fees" from the category of claim charges, but recouped the amount of those formerly-
4 called "Network Access Fees" (\$6.88 million) by increasing the cost associated with a
5 Non-Cost Factor. *McGuinness Aff ¶ 19*. The net result was to bury \$6.88 million in real,
6 direct costs to the state in a Non-Cost Factor portion of the proposal, artificially reducing
7 the cost proposal itself by that same amount. *Id.* And, none of this would have been
8 possible without the guidance that had been supplied by the Division over the month of
9 February.

10 *In Dynacs Engineering Company v. United States*, 48 Fed Cl 124 (2000), the
11 government made a disproportionate effort to enhance one RFP proposer's bid, offering it
12 multiple opportunities to cure deficiencies and working with the favored bidder to cure
13 nine shortcomings while pointing out only two deficiencies in the other bidder's
14 proposal. The government tried to justify this substantive inequality by claiming that it
15 had made some effort to work with both bidders. The court disagreed, holding that, in
16 RFP discussions, the equality of treatment among proposers must be "meaningful," and
17 both sides must be given the "same opportunity" to address weaknesses. A bidding
18 agency cannot get by with "not telling [one bidder] about its continuing weaknesses,
19 [while continuing to inform the other bidder] about each of [its] weaknesses until [that
20 other bidder] got it right." 48 Fed.Cl. at 130. The disparity in both the frequency and
21 substance of the communications among the two bidders in our case, and the vastly
22 different results that the two sets of "discussions" achieved, proved that precisely the
23 same inequity occurred here.
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1 To the same effect is *Dubinsky v United States*, 43 Fed. Cl. 243 (1999), *appeal*
2 *dismissed* 215 F.3rd 1350 (Fed. Cir. 1999), where the government also used the device of
3 common discussions with potentially successful proposers to improve one bidder's
4 proposal, while giving *pro forma* attention to the other. Without substantive equality in
5 the discussions between proposers, the court held, "discussions with offerors readily
6 would be subject to abuse, merely becoming a cover for an agency's discussions with the
7 offeror it has selected to receive the contract prior to the formal selection decision." *Id.* at
8 263-4, *see also Paramax Systems Corp v CAE-Link Corp*, 1993 WL 485205 (*Com*
9 *Gen.*) (October 27, 1993), (where bidders "were not treated equally since they were not
10 given the same opportunity to participate in discussions and to amend their cost price
11 proposals after BAFO [Best and Final Offer]," Comptroller General recommended a new
12 round of BAFO's and, if necessary, cancellation of the originally-successful contract).

13 By selling Aetna short in the negotiation process, the big loser could well have
14 been the Alaska public. Could the Division have gotten the best deal for Alaskans by
15 engaging in the same discussions with Aetna that it had undertaken with Premera? As
16 the court in *McBirney* stressed, we've no idea, because equality of treatment never
17 occurred, and we thus do not know what kind of alternative proposal might have
18 emerged from a similarly intensive effort with Aetna. 753 P.2nd at 1138.

19 Arguably, the genesis of the unequal treatment may have arisen from the
20 Division's misplacement of Aetna's bid. From that point, and until the mistake was
21 discovered, the Division considered Premera the only qualified bidder, and one might
22 expect a government agency to communicate exclusively with the only bidder who (as
23 the Division thought at the time) was qualified for the contract. That spin gives the
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Division every benefit of the doubt. But even if that were the case, the Division's ultimate failure came in its refusal to give Aetna's proposal the same individual assistance once the Division learned that Aetna was a qualified bidder whose bid was "susceptible for award." As Commission Norstrand acknowledged, by that time the playing field was "not entirely level," but the Division did nothing to level it. *Attachment 12 at 24*. It was incumbent on the Division to level that playing field, by helping Aetna improve its proposal to the same extent as it already had with Premera. The Division, in a word, cannot excuse such clear inequality of treatment by its own mistake, particularly when the Division later had every opportunity to rectify that mistake. The plain fact remains that the contract was awarded based on a process that treated the two proposers with patent inequality—a fact that proves not only a material statutory and regulatory violation, but as well a "serious[] impair[ment] of the purpose of the competitive bidding statutes" that warrants voiding the contract. *Earthmovers of Fairbanks, Inc. v. State*, 765 P.2d 1360, 1369 (Alaska 1989).

IX. The Appropriate Remedy Here is to: (a) Re-Score the Parties' Previously-Submitted Final Proposals in their Entirety, Using a Three-Person Team Comprised of Uninvolved, Qualified and Unbiased Personnel Assisted by a Mutually-Agreeable Consultant With Expertise in Evaluating Health Claim Management Service Proposals; (b) Have the Evaluation Team Include Total Costs (as Defined in this Section) in the Cost Proposal Required by Section 7.23 of the RFP; and (c) Cancel Premera's Existing Contract, and Award

the Contract to Aetna, if the new Evaluation Committee Finds
Aetna's Final Proposal to be Most Advantageous to the State

The deciding officer's discretion to grant relief in this case is defined by AS 36.30.585, which broadly authorizes the grant of "an appropriate remedy." §585(a). Subsection (b) of that section guides the deciding officer in determining what remedy is appropriate.

In determining an appropriate remedy, the procurement officer shall consider the circumstances surrounding the solicitation or procurement including the seriousness of the procurement deficiencies, the degree of prejudice to other interested parties or to the integrity of the procurement system, the good faith of the parties, the extent to which the procurement has been accomplished, costs to the agency and other impacts on the agency of a proposed remedy, and the urgency of the procurement to the welfare of the state.

These remedies can include "award of bid or proposal preparation costs, termination of an existing contract, re-evaluation [and other appropriate relief]" *In the Matter of Bachner Company Inc and Bowers Investment Company*, Ak. Dept. of Administration Case No. 03-10 (Feb. 10, 2004) at 7 ("*Bachner*"), *J&S Services*, ante at 5. To the extent that the basis for the remedy is impropriety in the procurement, the deciding officer should also consider the factors set out in *Keko*, 492 F.2nd at 1203. *J&S Services*, ante at 6.

Aetna's proposed remedy requests the deciding officer to direct the Division to appoint a three-person uninterested,¹⁵ qualified and unbiased review team that includes a mutually-agreeable consultant (as the State has used in the past) to re-score the parties'

¹⁵ / As used in these Sections LX and X, "uninterested" means team members who have had no involvement in any evaluation process related to this procurement, nor any other substantive involvement in the procurement. None of the new team members should be made aware of any prior evaluation scores.

1 last proposals ^{16/} in their entirety, and, if the evaluation team determines that Aetna's
2 proposal is the most advantageous to the state (using the RFP's point system), (i) cancel
3 the contract awarded March 13, 2006 to Premera, and (ii) award the contract to Aetna. ^{17/}

4 Before re-evaluation, the evaluation team should modify the parties' proposals in one
5 respect only: the price offer made under Section 7.23 of the RFP should include total
6 costs to the state. ^{18/} As explained in *Section VIII, ante*, and in the *Third Affidavit of Mike*
7 *Wiggins* and the *Affidavit of Matt McGuinness*, by including "total costs," the cost portion
8 of the bid would capture (among other cost items) network savings sharing arrangements.
9 These sharing arrangements represent a true, direct cost to the state, because they deny
10 the State a portion of these otherwise important savings (in a nutshell, putting money in
11 the contractor's pocket that would otherwise go into the state's pocket—here to the tune
12 of \$6.88 million). *Id.* ^{19/} By not including those savings sharing arrangements as a

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16 ^{16/} The parties' last proposals are comprised of their RFP responses, all of their answers to the
17 various questions propounded by the Division that have heretofore been disclosed to the parties
18 and included in the *Attachments* to this Appeal, and the so-called Best and Final Offer submitted
19 on February 28, 2006.

20 ^{17/} This proposed remedy is premised on the assumption that this Appeal can be resolved on an
21 expedited basis. If the appeal is not expedited, or it is not expedited sufficiently, then Aetna
22 reserves the right to request alternative relief, and to seek such stays and interim relief as
23 circumstances may warrant.

24 ^{18/} As used in these Sections IX and X, "total costs" include program administration fees,
25 pharmacy rebate sharing arrangements, network savings sharing arrangements, run out fees in the
26 event of termination, banking arrangements, and other terms that affect cost. Pharmacy rebates
are being included because it is common practice to offset administration fees with rebate sharing
guarantees. This approach is referenced as a preferred approach in the RFP under 3.08 "Proposed
Payment Arrangements".

^{19/} In fact, Premera was able not only to effectively obscure the \$6.88 million in "Network
Access Fees" discussed throughout this memorandum, but also to add additional costs to the State
that were not disclosed in the cost section of Premera's proposal, such that the total amount of
undisclosed costs ultimately totaled \$13.74 million (using reasonable underwriting assumptions).
Id.

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"cost," the proposer's bid understates the cost to the state of the proposal by the corresponding amount.²⁰

Aetna submits that, taken as a whole and fairly balanced, the factors set out in §585 support such a remedy. For example:

- The initial factor listed in §585—the "seriousness of the procurement deficiencies," and the "degree of prejudice to the integrity of the procurement system" plainly argue for re-evaluation and (if necessary) cancellation of the existing contract

The extent to which the Division's statutory and regulatory violations have undermined the purpose of Alaska's competitive bidding laws has been extensively discussed *ante*. The extensive, one-sided contacts held with one bidder have undermined the purpose of AS 36.30.240 and 2 AAC 12.290, which is to guard against the potential for abuse inherent in pre-award conversations with proposers by placing strict limits of equality in dealings with all qualified proposers. And, as the court stressed in *McBirney v. State*, 753 P.2d 1132, the failure of the Division to work just as intensely with Aetna as it did with Premera to improve its proposal frustrated the central purpose of our competitive bidding system—to obtain the deal "most advantageous to the state" (AS 36.30.250(a))—

²⁰ It should be noted that the relief requested here is considerably less favorable to Aetna than the relief originally requested in the Protest. *Attachment 9* at 16-17. That is because one of the material factors for shaping relief under AS 36.30.585 has changed since the protest was submitted—*i.e.*, the status of the procurement. The ultimate standard for relief under §585 is "appropriateness," which is plainly a function of current realities. But if the Division can erect some arbitrary barrier to this Appeal's request, then the relief sought in the Protest is incorporated herein by reference. Of course, the deciding officer is not limited, in fashioning relief, to that set out in the parties' papers.