MIKE KREIDLER
STATE INSURANCE COMMISSIONER

STATE OF WASHINGTON

Phone (360) 725-7000
www.insurance.wa.gov

OFFICE OF
INSURANCE COMMISSIONER

In the Matter of	)	No. G07-347
	)	
The Financial Examination of	)	FINDINGS, CONCLUSIONS,
ARCADIAN HEALTH PLAN, INC.	)	AND ORDER ADOPTING REPORT
	)	OF EXAMINATION

A Registered Health Care Service Contractor.

BACKGROUND

An examination of the financial condition of **ARCADIAN HEALTH PLAN, INC.** (the Company) as of June 30, 2006, was conducted by examiners of the Washington State Office of the Insurance Commissioner (OIC). The Company holds a Washington certificate of registration as a health care service contractor. This examination was conducted in compliance with the laws and regulations of the state of Washington and in accordance with the procedures promulgated by the National Association of Insurance Commissioners and the OIC.

The examination report with the findings, instructions, and recommendations was transmitted to the Company for its comments on November 1, 2007. The Company's response to the report is attached to this order only for the purpose of a more convenient review of the response.

The Commissioner or a designee has considered the report, the relevant portions of the examiners' work papers, and the submissions by the Company.

Subject to the right of the Company to demand a hearing pursuant to Chapters 48.04 and 34.05 RCW, the Commissioner adopts the following findings, conclusions, and order.

FINDINGS

Findings in Examination Report. The Commissioner adopts as findings the findings of the examiners as contained in pages 1 through 13 of the report.

Mailing Address: P. O. Box 40255 • Olympia, WA 98504-0255
Street Address: 5000 Capitol Blvd. • Tumwater, WA 98501

CONCLUSIONS

It is appropriate and in accordance with law to adopt the attached examination report as the final report of the financial examination of **ARCADIAN HEALTH PLAN, INC.** and to order the Company to take the actions described in the Instructions and Comments and Recommendations sections of the report. The Commissioner acknowledges that the Company may have implemented some of the Instructions and Comments and Recommendations prior to the date of this order. The Instructions and Comments and Recommendations in the report are appropriate responses to the matters found in the examination.

ORDER

The examination report as filed, attached hereto as Exhibit A, and incorporated by reference, is hereby ADOPTED as the final examination report.

The Company is ordered as follows, these being the Instructions and Comments and Recommendations contained in the examination report on pages 1-3.

1. The Company is ordered to comply with RCW 48.44.100 and file an accurate statement of its financial condition, transactions, and affairs; with RCW 48.43.097 which requires the filing of its financial statements in accordance with the AP&P Manual; and with WAC 284-07-050(2) which requires adherence to the NAIC Annual Statement Instructions and the AP&P Manual. Instruction 1, Examination Report, page 2.

2. It is ordered that the Company consider preparing a formal, written business continuity plan that addresses the continuation of all significant business activities, including financial functions, telecommunication services and data processing services, in the event of a disruption of normal business activities, as recommended by the NAIC. Comments and Recommendations 1, Examination Report, page 3.

3. It is ordered that the Company consider writing, testing, and implementing a disaster recovery plan that includes appropriate escalation procedures to resolve operational failures in a timely manner, as recommended by NAIC Guidelines. Comments and Recommendations 2, Examination Report, page 3.

4. It is ordered that the Company consider closely monitoring its fidelity bond coverage to keep pace with its rapid growth and increase coverage as needed to an appropriate level for its exposure in line with the recommendations of the NAIC at a minimum. Comments and recommendation 3, Examination Report, page 3.

IT IS FURTHER ORDERED THAT, the Company file with the Chief Examiner, within 90 days of the date of this order, a detailed report specifying how the Company has addressed each of the requirements of this order.

ENTERED at Olympia, Washington, this 14th day of December, 2007.

MIKE KREIDLER
Insurance Commissioner

ARCADIAN

November 30, 2007

James T. Odiorne, CPA, JD
Deputy Insurance Commissioner
Company Supervision Division
P.O. Box 40255
Olympia, WA 98504-0255

RE: Financial Examination Report of Arcadian Health Plan, Inc. as of June 30, 2006

Dear Deputy Commissioner Odiorne:

Thank you for allowing us to collect our data and organize our thoughts in this format. We appreciate the thoroughness of the examination and the opportunity to provide input and responses that will make the final report the most meaningful and accurate it can be.

Please see Arcadian Health Plan's responses to the examination Instructions and Comments and Recommendations from the Office of Insurance Commissioner's ("OIC") Financial Examination Report in the letter dated November 1, 2007. Also, we noted some areas that we suggest can benefit from clarification in other sections of the Report and have suggested alternative text for your consideration.

INSTRUCTIONS

1. Unrecorded Liabilities for Medicare Part D Prescription Drug Program

The Company does not contest this finding. The Company self-identified and reported this issue to the OIC and immediately began regularly recording LICS and Part D Risk Sharing liabilities monthly beginning in November 2006. Additional resources have been added to address this new and complex area of Part D Risk Corridor on a go-forward basis. Final settlement was reached with CMS in October of 2007 and these liabilities were calculated using the current methodologies to well over 99% accuracy.

COMMENTS AND RECOMMENDATIONS

1. Business Continuity Plan

The Company takes Business Continuity Planning very seriously so that it can maintain high levels of service even in the event of some external factors. The Company has now had a Business Continuity Plan in place since August 2007. (Attachments 1 and 2) This plan includes call trees, system specific work-flows and action plans, as well as disaster recovery capabilities as noted below. Additionally, the Company has dedicated resources and contracted with a reputable outside vendor, Tamp Systems, to continue its on-going efforts in planning, documenting and maintaining an expanding comprehensive Business Continuity Plan. This more comprehensive plan is expected to be finalized during the first quarter of 2008. Based on the foregoing, the Company respectfully requests that this recommendation be removed or revised to reflect the updated conditions.

2. **Disaster Recovery Plan**

The Company considers addressing continuity of service a high priority – even in a situation involving a disaster scenario. As such, the Company has implemented a disaster recovery plan with multiple components, including a collocation facility in Washington hosted by AT&T.

In the event of critical server failures, the backup system will take over the master role after the primary servers in San Dimas have five minutes of inaccessibility. There are also several redundant servers that handle the Company's critical service roles. These servers are located in San Dimas and are configured to be on standby in case of an emergency. These replications have been successfully tested. In support of these activities, the Company has contracted with Tamp Systems to continue its on-going efforts in planning, documenting and maintaining a disaster recovery program. Additionally, the Company is negotiating with a vendor for an offsite workplace to temporarily relocate its operations in the event of a disaster. Based on the foregoing, the Company respectfully requests that this recommendation be removed or revised to reflect the updated condition.

3. **Fidelity Bond**

The Company takes risk management and its obligations to all its constituents, including enrollees and the regulators very seriously and accordingly maintains fidelity bonding to \$1,000,000. The initial bonding of \$1,000,000 with a \$10,000 deductible was effective December 1, 2003. On October 27, 2006, a fidelity bond for \$100,000 with no deductible and excess limits for named employees was implemented at the request of the State of Arizona. Bonding remains in place for claims in excess of the \$100,000 with a limit of \$1,000,000. (Attachment 3) Based on the foregoing, the Company respectfully requests that this recommendation be removed or revised to reflect the existence of the level of bonding coverage.

ACTUARIAL REVIEW

In our reading of the examination report, we believe we may have found an inadvertent inconsistency within the document. On page 7 the last sentence of paragraph 5 reads "A corresponding examination financial statement adjustment was required to reflect this increase to

"Claims unpaid"." Based on our understanding of the balance of the commentary and the situation, the Company believes that "increase" should be replaced with "decrease".

ACCOUNTING RECORDS AND INFORMATION SYSTEMS

On page 8 the last paragraph of this section notes that the Company does not have formal, written disaster recovery and business continuity plans as recommended by NAIC Guidelines. As described above, the Company does in fact have a disaster recovery solution in place with a collocation facility in Washington hosted by AT&T. In the event of critical server failures, the backup system will take over the master role after the primary servers in San Dimas have five minutes of inaccessibility. There are also several redundant servers that handle the Company's critical service roles. These servers are located in San Dimas and are configured to be on standby in case of an emergency. These replications have been successfully tested. In support of these activities, the Company has contracted with Tamp Systems to continue its on-going efforts in planning, documenting and maintaining a disaster recovery program. Additionally, the Company is negotiating with a vendor for an offsite workplace to temporarily relocate its operations in the event of a disaster. Based on the foregoing, the Company respectfully requests that this recommendation be removed or revised to reflect the current status.

SUBSEQUENT EVENTS

1. On page 8, the OIC notes in part "Adverse operating results, incorrect financial projections and a failure to timely record liabilities have resulted in operating ratios that our outside normal, expected ranges for year-end 2006 and 2007. This resulted in a requirement for the Company to obtain additional capital in order to comply with risk-based capital (RBC) requirements." The Company watches its ratios and capital requirements very carefully and is on track with its overall business plan to combine rapid growth with adequate financial strength. The Company feels it continues to meet its financial obligations and has shown steady improvement since it self-identified and corrected the accounting error with respect to Medicare Part D financial responsibility. The Company did obtain additional capital and feels that it will continue to be in a position to be able to do so if necessary to meet its requirements and achieve long-term stability. While a heavy burden of front end marketing related expenses have resulted in losses during the first four months of the year, the Company has maintained its profitability since then with a year to date net loss of approximately $335,000 which is consistent with current expectations. The Company willingly took on these up front costs of expansion in order to create profitable relationships with enrollees that it intends to preserve. The Company has provided long term financial forecasts that demonstrate the Company's ability to meet its financial obligations and create surpluses once the balance of growth versus existing business levels is closer to equalization. Based on the foregoing, the Company requests that the referenced paragraph be modified specifically excluding "financially hazardous", as the Company's financial position is greatly improved and on-track with expectations.

2. On page 9, the OIC noted "The Company's November 2006 financial statement added two additional liabilities which had a material effect on its operating results for 2006." The Company would also like it noted that these liabilities were significantly offset by the reduction of its claims unpaid liability.

3. On page 9 bullet two, the OIC notes in part "seven of the NAIC Financial Analysis Solvency Tools (FAST) ratios fell outside designated thresholds..." The Company takes its financial solvency, standing and capital situation seriously and regularly tracks its performance against ratios and believes it is meeting all known ratios for which it has an obligation. In order to track and improve its performance against them, the Company requests that the OIC provide the seven ratios so that the Company can determine how to satisfy those standards in a reasonable period of time.

4. On page 9 bullet three, the OIC notes the Company's high operating loss ratio. The Company would like it noted that expense ratios are improving with an October year to date underwriting loss ratio of 77.9% and an expense ratio of 23.9%. These are on track with its target underwriting loss ratio of 80% as presented in the Company's financial projections provided to the OIC, and its objective to continue leveraging its fixed costs to gain economies of scale and a manageable administrative cost ratio.

5. On page 9, the OIC noted "The Company's operating loss for the last twelve month or shorter period is greater than fifty percent of its remaining surplus." The Company believes that with its improved performance over the last several months, this is no longer true and respectfully requests that this comment either be removed or updated to reflect the current situation.

6. On page 9 bullet five, the OIC notes a premium to surplus ratio of approximately 13 to 1. With subsequent infusion of capital and improved current year performance, the Company's October 2007 ratio of premiums to capital and surplus is 7.6. Based on this, the Company respectfully requests that this bullet be removed or modified to reflect the current position.

7. On page 10 after the first full paragraph, the OIC notes that the Company was not following its documented procedures for broker commissions. In addition to the observations of E&Y, the Company conducted its own internal audit of the process resulting in the successful implementation of new policies and procedures to improve the internal controls related to broker commissions. The Company also invested in additional resources in terms of personnel and software/process enhancements, and moved the calculation and payment of commissions from marketing to finance to provide better oversight. The Company has addressed this observed weakness and the compliance with policies is now very strong. Hence the Company respectfully requests that this also be reflected in the OIC's narrative.

8. On page ten after the second full paragraph, the OIC noted E&Y's recommendation for formal policies for the reconciliation of balance sheet accounts. In the Company's letter to the OIC dated September 25, 2007, the Company outlined its Work Plan to reconcile all

balance sheet accounts, adopt standard uniform reconciliation formats and increase staffing with both internal and external resources. The Company has engaged a reputable consultant to assist in the development of processes around the regular reconciliation of balance sheet accounts. The Plan is being executed on currently. These actions, combined with the related policies and procedures continue to improve the accuracy and timeliness of the financial statements. Based on the foregoing, the Company respectfully requests that this be reflected in the OIC's narrative.

Thank you again for the opportunity to provide responses to or clarify portions of the report. Please feel free to call me with any questions you may have. I can be reached at (909) 971-6800.

Sincerely,

Les Granow

Les Granow
Chief Financial Officer
Arcadian Management Services, Inc.