

**STATE OF WASHINGTON
OFFICE OF THE INSURANCE
COMMISSIONER**



FINANCIAL EXAMINATION

of

**PACIFIC VISIONCARE WASHINGTON, INC.
CHEHALIS, WASHINGTON**

NAIC CODE 47100
DECEMBER 31, 2004

Pacific VisionCare Washington, Inc.
Order No. G06-50
Exhibit A

SALUTATION

Seattle, Washington
September 18, 2006

The Honorable Mike Kreidler, Commissioner
Washington State Office of Insurance Commissioner (OIC)
Insurance Building—Capital Campus
302–14th Avenue SW
Olympia, WA 98504

Dear Commissioner Kreidler:

In accordance with your instructions, and in compliance with the statutory requirements of RCW 48.44.145 and RCW 48.03.010, an examination was made of the corporate affairs and financial records of

Pacific Visioncare Washington, Inc.

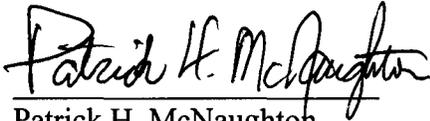
of

Chehalis, Washington

hereinafter referred to as "PVC" or the "Company," at the location of its administrative office at 2517 NE Kresky Avenue, Chehalis, Washington. This report is respectfully submitted showing the condition of the Company as of December 31, 2004.

CHIEF EXAMINER'S AFFIDAVIT

I hereby certify I have read the attached Report of the Financial Examination of Pacific Visioncare Washington, Inc., of Chehalis, Washington. This report shows the financial condition and related corporate matters as of December 31, 2004.



Patrick H. McNaughton
Chief Examiner

9-18-06

Date

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SCOPE OF THE EXAMINATION

This examination covers the period January 1, 2000 through December 31, 2004 and comprises a comprehensive review of the books and records of the Company. The examination followed the statutory requirements contained in the Washington Administrative Code (WAC), the Revised Code of Washington (RCW), and the guidelines recommended by the National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook. The examination included identification and disposition of material transactions and events occurring subsequent to the date of examination that were noted during the examination.

Corporate records, external reference materials, and various aspects of the Company's operating procedures and financial records were reviewed and tested during the course of this examination and are commented upon in the following sections of this report. In addition, the Company's certified public accountant's (CPA's) work papers were reviewed and utilized, where possible, to facilitate efficiency in the examination.

INSTRUCTIONS

The examiners reviewed the Company's filed 2004 NAIC Annual Statement as part of the statutory examination. This review was performed to determine if the Company completed the NAIC Annual Statement in accordance with the NAIC Annual Statement Instructions and to determine if the Company's accounts and records were prepared and maintained in accordance with Title 48 RCW, Title 284 WAC, and the NAIC Statements of Statutory Accounting Principles (SSAP) as contained in the NAIC Accounting Practices and Procedures Manual (AP&P).

The following summarizes the exceptions noted while performing this review.

1. Intercompany Agreements

The Company has two significant agreements in place with affiliates that are subject to the Health Carrier Holding Company Act: (1) A Provider Network Access Agreement with Pacific Eyecare Network (PEN), effective April 1, 2000, for two years, then automatically renewable for one year terms unless non-renewed by either party; and (2) a Management Support Services Agreement with Pacific Cataract & Laser Institute, effective April 1, 2002, for two years, then automatically renewable for one year terms unless non-renewed by either party.

The Company has not filed the annual registration statement (Form B) with the Commissioner for either of these agreements as required by RCW 48.31C.040(2)(c)(v). In addition, the Company did not notify the Commissioner as required by RCW 48.31C.050(2), (Form D), prior to renewing these agreements, which renew annually. The inception of Provider Network Access Agreement pre dates this code section and was therefore exempt from filing Form D until it renewed in April 1, 2002.

RCW 48.31C.050(1) states that intercompany agreements must be fair and reasonable and expenses must be allocated in conformity with statutory accounting practices consistently applied. Neither of the agreements includes terms or a description of how expenses are to be allocated.

The Company is instructed to comply with:

RCW 48.31C.040(2)(c)(v) by including these agreements in Form B;

RCW 48.31C.050(1) by disclosing the terms of the agreements in Form D; and,

RCW 48.31C.050(2)(d) by properly notifying the commissioner prior to entering into management agreements, service contracts and cost-sharing arrangements.

2. Officer Compensation Filings

The Company pays a management fee to an affiliate. The fee includes an allocation of officers' salaries, but the salary portion is not broken out in the billing or reported on the NAIC Supplemental Compensation Exhibit (SCE) or the compensation schedule required by RCW 48.43.045(2).

The Company did not respond to the second part of Question 1, Part 1 of the Interrogatories on the SCE, which state:

Do the amounts below represent 1) total gross compensation paid to each individual by or on behalf of all companies which are part of the group: Yes []; or 2) allocation to each insurer: Yes [].

The Company is instructed to follow the NAIC Annual Statement Instructions, RCW 48.43.045(2) and Technical Assistance Advisory, (TAA), T 04-06, by properly completing the required compensation schedules, the RCW 48.43.045(2) compensation report and by responding to all interrogatories in the SCE, pursuant to RCW 48.44.095.

3. NAIC Annual Statement Errors and Misclassifications

The results of the examination disclosed several instances in which the Company's filing of the 2004 NAIC Annual Statement did not conform to the NAIC Accounting Practices and Procedures Manual and the NAIC Annual Statement Instructions. While the Company needs to correct these practices, none of the following items in the instruction were material to the financial statements and no examination adjustments were made.

The Company is instructed to comply with RCW 48.43.097, RCW 48.44.095, and WAC 284-07-050(2) in filing its NAIC Annual Statements in accordance with the NAIC Accounting Practices and Procedures Manual, and the NAIC Annual Statement Instructions. The following exceptions were noted in our examination:

a. Claim Adjustment Expense

Expenses of \$47,085 paid to a third party administrator (TPA) that performs premium billing and collections and claims processing as well as maintaining the premium master file were all reported on the Underwriting and Investment Exhibit, Part 3, as claims

adjustment expense. These expenses should be split between claims adjustment expense and general and administrative expense.

b. Commission Expense

Commission expenses incurred in 2004 in the amount of \$1,538 were not reported until May 2005. As a result, Unassigned Funds were overstated by this amount in 2004.

c. Underwriting and Investment Exhibit

A regulatory fee of \$1,000 was improperly reported on the Underwriting and Investment Exhibit, Part 3, line 23.2 Premium Taxes. It should have been reported on line 23.3 Regulator Authority Licenses and Fees.

The Underwriting and Investment Exhibit, Part 2C - Development of Incurred Health Claims- Vision Only was not properly completed. Amounts reported were not cumulative and outstanding reserves for years prior to 2004 were not included in Section B or C as required by the NAIC Annual Statement Instructions

d. Schedule Y- Part I

Schedule Y - Part 1 does not comply with the NAIC Annual Statement Instructions, in that it does not include the ultimate controlling person, nor the relationships of the holding company group to the ultimate controlling person.

e. General Interrogatories

The Company's response to General interrogatory 10 did not include the name of the individual providing the statement of actuarial opinion and is therefore incomplete.

f. Notes to Financial Statements

Note 13.(9)b. fails to recognize the impact of nonadmitting the net deferred tax asset on unassigned funds. The response should have indicated the non-admitting of a portion of the deferred tax asset decreased unassigned funds by \$25,000.

Responses to Notes to Financial Statements, page 25.2, note 9.C.4, Income tax benefit 3,000 and 9.D. Amount booked- income tax benefit (\$3,000), are not consistent with amount reported in the Statement of Revenue and Expenses, page 4, line 31 of \$0 and are therefore incorrect.

COMMENTS AND RECOMMENDATIONS

1. Business Contingency Plan

The Company does not have a formal, written business contingency plan based on a business impact analysis; that has been tested, and addresses all significant business activities, including financial functions, telecommunication services, and data processing and network services.

It is recommended that the Company prepare a formal, written business contingency 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 NAIC.

2. Disaster Recovery Plan

The Company does not have a formal, written, disaster recovery plan for the resumption of information systems (IS) operations in the event of a disruption of normal operations.

It is recommended that PVC write, test and implement a disaster recovery plan that includes appropriate escalation procedures to resolve operational failures in a timely manner, as recommended by NAIC Guidelines.

COMPANY PROFILE

History

Pacific Visioncare Washington, Inc. (PVC) has operated as a limited health care service contractor in the state of Washington since November 10, 1999. PVC began marketing its voluntary primary vision care services product in 2000, with the first active members effective August 1, 2000. In August 2001, PVC began selling its group vision product.

Since that time, PVC has grown to annual revenues of \$273,472 with 5,053 members as of December 31, 2004. PVC's voluntary product accounted for 1,453 covered lives and the group product accounted for 3,600 covered lives. The voluntary product has 148 employer groups and the group product consists of 95 employer groups.

Territory and Plan of Operation

As a limited health care service contractor, Pacific Visioncare Washington, Inc., markets its vision products throughout the state of Washington. PVC issues group vision care policies with vision care services delivered on a discount fee-for-service basis by contracted optometrists. PVC sells its product through appointed insurance agents.

Although the benefits for the voluntary primary vision care services product and the group vision product are identical, unlike the voluntary product which has a minimum participation of one, the group product requires inclusion of all full time employees on the plan that are enrolled in the

companies medical insurance coverage plan, with a minimum enrollment of five employees. Future plans are to add the states of Idaho, Alaska, Oregon and Montana. The plan is to phase in these states beginning in 2006, starting with Idaho.

PVC outsources all phases of operations, as indicated below:

Management services have been outsourced to Pacific Cataract and Laser Institute, Inc. (PCLI) since inception.

The network provider panel services have been outsourced to Pacific Eyecare Network, Inc. since inception.

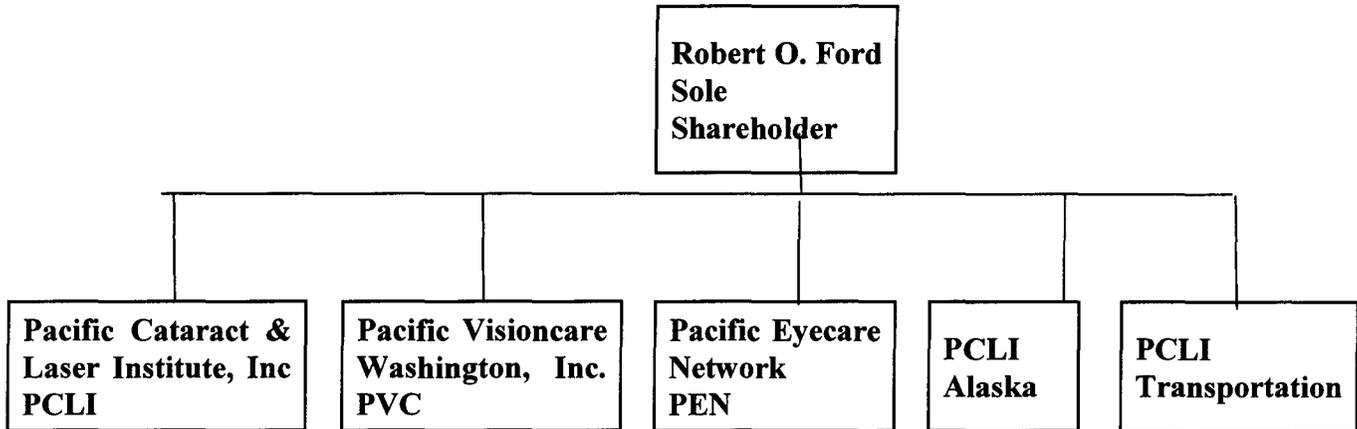
PVC has outsourced premiums and claims processing to a TPA since its inception. Trusteed Service Plans Corporation, located in Tacoma, Washington, has been the TPA since June 1, 2002. The TPA maintains enrollment records, provides customer service, and bills premiums to employers and collects and deposits premiums directly to a PVC bank account. In addition, the TPA processes and pays claims from the PVC bank account. (See Subsequent Event No. 2)

Growth of Company

The following schedule reflects the growth of the Company for the five year period ending December 31;

	<u>2004</u>	<u>2003</u>	<u>2002</u>	<u>2001</u>	<u>2000</u>
Assets, Liabilities, Capital and Surplus:					
Admitted Assets	\$ 364,170	\$368,857	\$377,851	\$372,049	\$363,842
Liabilities	44,933	33,440	30,701	14,536	15,509
Capital and Surplus	319,237	335,417	347,150	357,513	348,333
Revenue and Expenses:					
Premiums Earned	273,472	214,618	158,824	124,166	17,678
Net Underwriting Deductions	294,562	230,645	174,797	121,629	85,947
Underwriting Gain or Loss	(21,090)	(16,027)	(15,973)	2,537	(68,269)
Investment and Other Income	2,536	2,295	4,110	11,643	19,143
Pre-Tax Income	(18,554)	(13,732)	(11,863)	14,180	(49,126)
Taxes Incurred	-	(2,000)	(1,500)	5,000	(26,000)
Net Income (Loss)	<u>\$ (18,554)</u>	<u>(\$11,732)</u>	<u>(\$10,363)</u>	<u>\$9,180</u>	<u>(\$23,126)</u>

AFFILIATED COMPANIES



Pacific Visioncare Washington, Inc., is a member of a holding company, which consists of 5 corporations, all 100% owned by Robert O. Ford. The companies are:

Pacific Visioncare Washington, Inc. (PVC)

Pacific Visioncare Washington, Inc. was formed in 1999 and is licensed as a limited health care service contractor with the state of Washington, Office of the Insurance Commissioner. Certificate of Registration No. 172 was issued November 10, 1999.

Pacific Cataract and Laser Institute, Inc. (PCLI)

PCLI consists of twelve ambulatory surgery centers, providing low stress outpatient eye care. The Company owns two aircraft. Management services are provided to PVC by PCLI. Management services include marketing and accounting.

Pacific Eyecare Network, Inc. (PEN)

PVC's provider network is rented from PEN. As of December 31, 2004, the provider network consisted of 272 optometrists, located throughout Washington State.

PCLI of Alaska, Inc.

The Company has an ambulatory surgery center. There are no transactions with PVC.

PCLI Transportation, Inc.

Provides transportation services for providers and patients for PCLI and PCLI Alaska, there are no transactions with PVC. The Company owns two aircraft, and several buses and vans.

INTERCOMPANY AGREEMENTS

The Company has two significant agreements in place with affiliates:

- (1) A Provider Network Access Agreement with Pacific Eyecare Network.
 - (2) A Management Support Services Agreement with Pacific Cataract & Laser Institute.
- (See Instruction No. 1).

MANAGEMENT AND CONTROL

Board of Directors

Robert O. Ford, M.D. is the sole owner and appointed Director.

Principal Officers

Debbie J. Eldredge, President, Secretary, and Treasurer
Marlin Gimbel, MBA, Vice President & Director of Professional Relations
Kathy McWilliams, Director of Finance

Conflict of Interest

The Company does not have a conflict of interest policy. We have recommended the Company institute a conflict of interest policy that requires annual documentation of any potential conflicts of interest from officers and key employees.

Fidelity Bond and Other Insurance

The examination of insurance coverages included a review of coverages, adequacy of limits and retentions. The Company is a named insured for insurance coverages provided through its affiliates' insurance policies.

At December 31, 2004, the other companies of the group were insured up to \$50,000 per occurrence against losses from dishonest acts and fraud committed by its employees. The NAIC suggested minimum level of fidelity bond coverage for the size and volume of PVC's operations is \$25,000.

Officer's, Employees', and Agents' Welfare and Pension Plans

PVC does not have any direct employees. Officers and employees are employed by PCLI and all salaries, pension plans, and bonuses are paid by PCLI. Compensation costs for key officers are allocated to PVC under the Management Support Services Agreement.

CORPORATE RECORDS

In general, the review of minutes of the Board of Directors indicated that the minutes support the transactions of the Company and the actions taken by its officers. The minutes of meetings were adequately approved and supported Company transactions and events. All board meetings were conducted with a quorum present. There were no amendments to the Articles of Incorporation or corporate Bylaws during the period under review.

LOSS EXPERIENCE

The following exhibit reflects the Company's loss experience from 2000 through 2004.

Year	1 Total Revenues	2 Total Medical Expenses	(2/1) Ratio
2000	\$17,678	\$24,038	136.0%
2001	124,166	64,448	51.9%
2002	158,824	92,965	58.5%
2003	214,618	122,980	57.3%
2004	273,472	174,927	64.0%

REINSURANCE

The Company does not have reinsurance due to limited liability exposure. In view of the fact that the Company only writes vision care coverage, reinsurance is not necessary.

ACCOUNTING RECORDS

The Company maintains its accounting records on a Generally Accepted Accounting Principles (GAAP) accrual basis of accounting and adjusts to Statutory Accounting Principles (SAP) basis for NAIC Annual Statement reporting. The Company was audited annually by the certified public accounting firm of RSM McGladrey, Inc or its predecessor Knight Vale & Gregory, PLLC since inception and received an unqualified opinion for all years under review. The Company's accounting procedures, internal controls, and transaction cycles were reviewed during the planning and testing phase of the examination and no exceptions or significant weaknesses were noted.

INFORMATION SYSTEMS (IS)

The management of Pacific Visioncare Washington, Inc., is sufficiently knowledgeable of the IS process. Systems Development, Acquisition and Maintenance Controls were evaluated to gain assurance that appropriate controls are in place.

Operations and application controls were reviewed to determine the type of hardware installed; operating systems and proprietary software in use; back up and recovery facilities employed and the controls exercised to maintain data security. The Company has sufficient internal controls in place to monitor system activity and processes.

PVC does not have a formal, written disaster recovery plan for the restoration of the information system and, also, does not have a formal, written business contingency 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 NAIC Guidelines. (See Comments and Recommendations Nos.1 and 2.)

SUBSEQUENT EVENTS

1. During the first quarter of 2005, the Company terminated its relationship with Brown and Brown of Washington, the managing general agent (MGA) and has indicated it intends to deal directly with the subagents of the MGA.
2. The Company indicated it has verbally given notice to Trusteed Service Plans Corporation, the TPA, with the intent of taking over the processing of billing and cash receipts for premiums, and claim administration and payments effective in 2006.

The changes outlined above are designed to reduce commissions and administrative costs which are currently excessive and have resulted in operating losses for four of the five years being examined.

FINANCIAL STATEMENTS

The following examination financial statements show the financial condition of Pacific Visioncare Washington, Inc. as of December 31, 2004.

Statement of Assets, Liabilities Capital and Surplus
Statement of Operations
Reconciliation of Surplus for the Period Since the Last Examination

**PACIFIC VISIONCARE WASHINGTON, INC.
ASSETS, LIABILITIES, CAPITAL AND SURPLUS
DECEMBER 31, 2004**

	<u>BALANCE PER COMPANY</u>	<u>REF.</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
Assets				
Cash and short-term investments	\$361,550		\$0	\$361,550
Uncollected premiums and agent's balances in the course of collection	120			120
Net deferred tax asset	2,500			2,500
Total assets	<u>\$364,170</u>		<u>\$0</u>	<u>\$364,170</u>
Liabilities, Capital and Surplus				
Claims unpaid	\$28,829		\$0	\$28,829
Unpaid claims adjustment expense	300			300
Premiums received in advance	7,794			7,794
General expenses due or accrued	5,224			5,224
Amounts due to parent, subsidiaries, and affiliates	2,786			2,786
Total Liabilities	<u>44,933</u>		<u>0</u>	<u>44,933</u>
Common capital stock	499,375			499,375
Unassigned funds (surplus)	(180,138)			(180,138)
Total capital and surplus	<u>319,237</u>		<u>0</u>	<u>319,237</u>
Total liabilities, capital and surplus	<u>\$364,170</u>		<u>\$0</u>	<u>\$364,170</u>

**PACIFIC VISIONCARE WASHINGTON, INC.
STATEMENT OF REVENUE AND EXPENSES
DECEMBER 31, 2004**

	<u>BALANCE PER COMPANY</u>	<u>REF.</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
Member months	44,809			44,809
Net premium income	\$273,472		\$0	\$273,472
Hospital and Medical:				
Other professional services	174,927			174,927
Subtotal	174,927		0	174,927
Less:				
Net reinsurance recoveries	0		0	0
Total medical and hospital	174,927			174,927
Claim adjustment expenses	53,081			53,081
General administrative expenses	66,554			66,554
Total Underwriting deductions	294,562		0	294,562
Net underwriting gain or loss	(21,090)		0	(21,090)
Net investment income earned	2,536			2,536
Net income or (loss) before federal income taxes	(18,554)		0	(18,554)
Federal and foreign income taxes incurred	0		0	0
Net income (loss)	<u><u>(\$18,554)</u></u>		<u><u>\$0</u></u>	<u><u>(\$18,554)</u></u>

**PACIFIC VISIONCARE WASHINGTON, INC.
RECONCILIATION OF SURPLUS SINCE THE LAST EXAMINATION
FOR THE YEARS ENDED DECEMBER 31**

	2004	2003	2002	2001	2000
Capital and surplus, December 31, previous year	\$335,417	\$347,150	\$357,513	\$348,333	\$271,459
Net income	(18,554)	(11,733)	(10,363)	9,180	(23,126)
Change in net deferred income tax	3,000	-	-	-	-
Change in nonadmitted assets	(25,000)	-	-	-	-
Capital and surplus, December 31, current year	<u>\$319,237</u>	<u>\$335,417</u>	<u>\$347,150</u>	<u>\$357,513</u>	<u>\$348,333</u>

NOTES TO THE FINANCIAL STATEMENTS

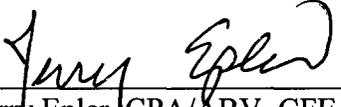
The Company has no special consents, permitted practices or orders from the state of Washington and there were no examination adjustments.

ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers of - Pacific Visioncare Washington, Inc. during the course of this examination.

In addition to the undersigned; Michael Jordan, CPA, CFE, MHP, Assistant Chief Examiner; John Jacobson, CISA, AFE, Information Systems Specialist; and Tim Navaja, CFE, CIE, Property and Casualty Field Supervising Examiner; all from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.

Respectfully submitted,



Jerry Epler, CPA/ABV, CFE
Examiner-in-Charge
State of Washington

