



OFFICE OF
INSURANCE COMMISSIONER

In the Matter of)	No. G07-202
)	
The Financial Examination of)	FINDINGS, CONCLUSIONS,
REGENCE BLUESHIELD)	AND ORDER ADOPTING REPORT
)	OF EXAMINATION

A Registered Health Care Service Contractor.

BACKGROUND

An examination of the financial condition of **REGENCE BLUESHIELD** (the Company) as of December 31, 2005, 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 May 22, 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 19 of the report.

CONCLUSIONS

It is appropriate and in accordance with law to adopt the attached examination report as the final report of the financial examination of **REGENCE BLUESHIELD** 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 1-6.

1. The Company is ordered to file an accurate statement of its financial condition, transactions, and affairs in compliance with RCW 48.43.097, which requires the filing of its financial statements in accordance with the NAIC AP&P Manual; and with WAC 284-07-050(2) which requires adherence to the NAIC Annual Statement Instructions. Instruction 1, Examination Report, page 3.
2. The Company is ordered to file its SAO pursuant to RCW 48.43.097 and WAC 284-07-060(2)(a), which require health care service contractors to file an SAO and financial statement in accordance with the AP&P Manual and the NAIC Annual Statement Instructions. Instruction 2, Examination Report, page 4.
3. The Company is ordered to file amendments to its Plan and Agreement of Affiliation or file a new agreement, which addresses specific methodology or basis used on how inter-company expenditures, fiduciary responsibilities, and type of service allocated across Plans and between Plans, TRG and other affiliates with the OIC pursuant to RCW 48.31C.050 in compliance with SSAP No. 70, Paragraph 8. The agreement should include additional documentation, which explicitly states the services, responsibilities, and considerations under the performance of the contract. Instruction 3, Examination Report, page 5.
4. The Company is ordered to calculate all future premium taxes based on written premiums in accordance with RCW 48.14.0201(2) and the premium tax return instructions. Instruction 4, Examination Report, page 5.

5. The Company is ordered to allocate internal investment expenses into the proper categories in Column 4 pursuant to RCW 48.43.097 which requires the filing of its financial statement in accordance with the AP&P Manual; and WAC 284-07-050(2) which requires adherence to the NAIC Annual Statement Instructions and the AP&P Manual. Instruction 5, Examination Report, page 5.
6. Pursuant to RCW 48.31C.040(2)(c)(i), the Company is ordered to include current information on any loans with affiliates on its Form B - Annual Registration Statement. Instruction 6, Examination Report, page 6.
7. It is ordered that the Company consider establishing procedures to ensure that claims for the self-funded groups are not recorded, or reported, as claim expense in the Company's loss triangles. Comments and Recommendations 1, Examination Report, page 6.
8. It is ordered that the Company consider implementing additional controls over private placement securities, which are kept on-site, to prevent stock certificates from being lost or misplaced. Comments and Recommendations 2, Examination Report, page 6.
9. It is ordered that the Company consider establishing procedures and implementing controls to ensure that all future information transmitted to the 401K Plan trustee is accurate and complete. Comments and Recommendations 3, Examination Report, page 6.

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 11th day of July, 2007.


MIKE KREIDLER
Insurance Commissioner



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June 14, 2007

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INSURANCE
COMMISSIONER
DIVISION

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

Re: Regence BlueShield– Report of Examination as of December 31, 2005

Dear Mr. Odiome,

Enclosed please find for your consideration, our responses to be included in the final Report of Examination for Regence BlueShield. We appreciate the opportunity to respond and comment on the Report.

Instructions

1. NAIC Annual Statement Errors and Misclassifications

a) Investment in Subsidiaries

The Company's investments in two wholly owned subsidiaries, CSN Acquisition Company and Healthcare Management Administrators, were incorrectly reported on Schedule D, Part 2, of the Company's 2005 Annual Statement. The investment values were based on the underlying statutory equity as of December 31, 2004, instead of 2005, resulting in an understatement of \$122,629 and \$782,523 for the investments in CSN Acquisition Company and Healthcare Management Administrators, respectively. However the errors had no impact on the Company's surplus since the subsidiary valuation amounts were based on unaudited financial statements and thus were non-admitted in 2005 NAIC Annual Statement in accordance with SSAP No.88.

The Company's investment in Commencement Bay Life Insurance Company is incorrect on Schedule D – Part 2 – Section 2, in columns 6 and 8. The Company only included Commencement Bay's reported surplus as of December 31, 2005 in the amount of \$19,270,977. The value that should have been reported was total capital and surplus of \$21,670,977 under the equity method required by SSAP 46, paragraph 7 b.

Company Response:

The Company agrees with these findings. The Company has taken corrective action and began reporting these correctly in its 2006 Annual Statement.

The Company's investment in Ninth and Howell Real Estate Joint Venture was incorrectly valued at \$1,166,574 on Schedule BA – Part 1. In accordance with SSAP No. 48, paragraph 7 and SSAP No. 88, the investment in a non-insurance joint venture is valued based on the underlying audited statement based on GAAP equity method of the investee, or \$4,186,668, resulting in an understatement of assets by \$3,020,095.

Company Response:

The Company agrees with this finding. Beginning in 2007, the Company will correctly report this investment.

b) Reclassification of Unearned Premium Reserves to Premiums Received in Advance

The Company misclassified "Premiums received in advance" in the amount of \$11,368,750 as "Unearned premium reserves" on Part 21, Line 1 of the Underwriting and Investment Exhibit. In accordance with SSAP No. 54, unearned premiums are policy reserves and shall be required for all accident and health contracts for which premiums have been reported for a period beyond the date of valuation other than premiums that have been received prior to the valuation date but are due on or after the valuation date. (See examination reclassification No.1, debiting "Aggregate health policy reserves", and crediting "Premiums received in advance" in the amount of \$11,368,750.)

Company Response:

The Company agrees with this finding. Beginning in 2007, the Company will reflect the premiums in the proper classification, per SSAP No.54.

c) Retrospectively Rated Contract Disclosure

SSAP No.66, Paragraph 12 requires Annual Statement disclosure of premium amounts subject to retrospective rating. The financial statements were correct except for the amounts disclosed in Note 24.B. of the Notes to the Financial Statements. The retrospective premiums should have been \$291,466,202 and \$280,999,981 for 2005 and 2004 respectively, instead of the reported amounts of \$360,378,907 and \$309,210,972.

Company Response:

The Company agrees with this finding. The Company has taken corrective action and began reporting these correctly in its 2006 Annual Statement.

d) Retirement Plan Disclosure

SSAP No.14, Paragraph 15, requires Annual Statement disclosure of employees that participated in a defined contribution plan sponsored by the holding company. In Note 12, Notes to the Financial Statements, the Company failed to disclose its 401(k) Plan, a defined contribution plan sponsored by its parent, The Regence Group (TRG). The fact that the Company has no legal obligation for the parent sponsored plan, the amount of the benefit expense incurred and the allocation methodology utilized by TRG should also be disclosed.

Under Note 12D, Notes to the Financial Statements, the Company disclosed the benefit expenses incurred for the Past Retirement Health and Life Insurance Benefit Plans but failed to disclose, as required by SSAP No. 89, Paragraph 15, the allocation methodology utilized by TRG and the fact that it has no legal obligation for the TRG sponsored pension plans.

Company Response:

The Company agrees with this finding. The disclosure for the Company's participation in the The Regence Group (TRG) 401k plan was mistakenly excluded from the Annual Statement footnotes. However, the disclosure of the plan and the Company's expenses were included in the Annual Audited Statutory Statements. Beginning in 2007, the Company will revise its filings to include the appropriate disclosures in all documents.

The disclosure for the Company's participation in the Postretirement Health Care and Life Insurance benefit plans did not include the expense allocation methodology or a statement regarding legal obligations. Legal obligations were disclosed in the Annual Audited Statutory Statement. Beginning in 2007, the Company will revise its filings to include the appropriate disclosures in all documents.

e) Security Lending Disclosure

Throughout the five year period under examination, the Company did not disclose its security lending program policy under Note 17.B.(2), Notes to the Financial Statement.

The Company has maintained a security-lending program during the examination period. The program is structured so that the Company calls back all loaned securities prior to the end of the year. To provide a complete disclosure, the Company is instructed to disclose its security lending policy the future NAIC Annual Statement filings in accordance with SSAP No. 91, Paragraph 88.h.

Company Response:

The Company agrees with this finding. It was our interpretation of SSAP #91, that since no securities were on loan as of the end of the year, there was nothing to report under the Notes to Financial Statements No. 17.b(2). The Company agrees that in an effort to provide a more complete disclosure, beginning in 2007, we will note our participation in a Securities Lending Program and further note that there were no securities on loan as of the end of the year.

f) Reclassification of Premium Received in Advance

Advance premium deposits as required by administrative service contracts (ASC) for uninsured plans in the amount of \$2,525,510 are incorrectly classified in the 2005 NAIC Annual Statement as "Amounts withheld or retained for the account of others". The 2005 NAIC Instructions excludes liabilities related to uninsured plans from the account as "Amounts withheld or retained for the account of others". The correct classification for the advance premium deposits are "Premiums received in advance".

Company Response:

The Company agrees with this finding. The Company has reported advance deposits on line 8, Premiums Received in Advance, beginning with the 2006 Annual Statement.

g) Commission Expenses Not Accrued

The Company did not accrue commission expenses associated with uncollected premiums and agents' balances in the course of collection. SSAP No. 54, Paragraph 12, requires that the amount of unpaid commissions, and the cost of collection associated with due and unpaid premiums, be carried as offsetting liabilities of uncollected premium. It was determined the amount was not material.

Company Response:

The Company agrees with this finding. Currently, the company does not have a systems process that will allow it to report commissions payable related to premiums receivable. However, the company will review the recommendation and will work to formulate a process to more accurately report these liabilities beginning in 2007, in accordance with SSAP No. 54, paragraph 12.

h) Number of Shares Owned of Regence Life and Health Insurance Company (RLHIC)

On Schedule D -- Part 2 -- Section 2 (Common Stock), the Company incorrectly reported the number of shares of stock owned in RLHIC, a subsidiary. The Company has an 18% ownership interest in RLHIC which equates to 5,439 shares, not 4,139 shares.

Company Response:

The Company agrees with this finding. The Company began reporting these correctly in its 2006 Annual Statement.

2. Statement of Actuarial Opinion

The 2005 Statement of Actuarial Opinion (SAO), prepared by its consulting actuary, failed to report the experience rated refund liability. The Company reported an experience rated refund liability in the Underwriting and Investment Exhibit, Part 1, Column 1, Line 4 of the 2005 NAIC Annual Statement in the amount of \$26,736,208.

The Company is instructed to file its SAO pursuant to RCW 48.43.097 and WAC 284-07-060(2)(a), which require health care service contractors to file an SAO and financial statement in accordance with the AP&P Manual and the NAIC Annual Statement Instructions.

Company Response:

The Company agrees with this finding. An amended filing of the SAO was filed on December 20, 2006.

3. Intercompany Transactions and Agreements

The following areas were identified as deficient in the course of our examination and require amendments to the PAA agreement pursuant to RCW 48.31C.050: Specific methodology or basis used on how intercompany expenditures, fiduciary responsibilities, and type of service are allocated across Plans and between Plans, TRG and other affiliates.

An amended or new agreement should address and correct the deficiencies noted above to maintain compliance with RCW 48.31C.050(1)(d) which states,

“The books, accounts and records of each party to all transactions must be so maintained as to clearly and accurately disclose the nature and details of the transactions, including such accounting information as is necessary to support the reasonableness of the charges or fees to the respective parties...”

Company Response:

The Company disagrees with this finding, but it will execute a formal cost-sharing agreement as recommended.

The cost sharing arrangement between The Regence Group and the Company has been handled consistently with the cost sharing criteria in the Management and Administrative Services Agreement between The Regence Group and Regence BlueShield of Idaho, Inc. Such cost sharing was permitted under Item B.6. in the Plan and Agreement of Affiliation between The Regence Group and the Company. Nonetheless, Regence will execute an agreement in 2007 between The Regence Group and the Company reiterating and formalizing existing cost sharing criteria.

4. Premium Tax Base

In computing its premium tax payment, the Company has been using earned premiums instead of written premiums, as its premium tax base during the five-year examination period. In due course, written and earned premiums will be the same. As a result, no examination adjustment is recommended given the fact that the premium tax differences identified over the five-year examination period were immaterial.

The Company is instructed to calculate all future premium taxes based on written premiums in accordance with RCS 48.14.0201(2) and the premium tax return instructions.

Company Response:

The Company agrees with this finding. Beginning with the 1st quarter 2006 filing, premium taxes were based on written premiums.

5. Investment Expense Allocation – Underwriting and Investment Exhibit

In Column 4 –Investment Expenses of the Underwriting and Investment Exhibit, Part 3-Analysis of Expenses, of the 2005 NAIC Annual Statement, the Company did not allocate investment expenses incurred internally. Only external investment expenses billed by outside parties were reported in Column 4. The internal investment expenses were misclassified as General Administration Expenses in Column 3.

SSAP No. 70, Paragraph 9, states, "Any basis adopted to apportion expenses shall be the one which would yield the most accurate results and may result from special studies of employee activities, salary ratios, premium ratios or similar analyses." In addition, SSAP No. 70 Paragraph 5 states that the allocation of expenses for health insurers should be based on a method that yields the most accurate results.

The Company is instructed to allocate internal investment expenses into the proper categories in Column 4 pursuant to RCS 48.43.097 which requires the filing of its financial statement in accordance with the AP&P Manual; and WAC 284-07-050(2) which requires adherence to the NAIC Annual Statement Instructions and the AP&P Manual.

Company Response:

The Company agrees with this finding. Beginning in 2007, the Company will review and take the steps necessary to collect and report internal costs associated with investment activity in accordance with SSAP No. 70.

6. Form B – Annual Registration Statement Disclosure

The Company loaned \$1,820,000 to The Regence Group (TRG) for the term of 20 years with interest compounded annually at the prime rate for standard commercial loans. However, the Company's 2005 Form B – Annual Registration Statement incorrectly states that the Company has no loans with affiliates. The aforementioned loan should have been fully disclosed in the registration statement.

In accordance with RCW 48.31C.040(2)(c)(i), the Company is instructed to include current information on any loans with affiliates in its Form B – Annual Registration Statement.

Company Response:

The Company agrees with the finding. Beginning in 2007, the Company will ensure that all information reported on the holding company annual registration statement is complete, accurate and in compliance with RCW 48.31C.040, of the Washington Code.

Comments and Recommendations

1. Incurred-Paid Triangle Error

The paid claim amounts for one self-funded group was erroneously included in the incurred-paid loss triangle data submitted to the examination team.

It is recommended that the Company establish procedures to ensure that claims for the self-funded groups are not recorded, or reported, as claim expense in the Company's loss triangles.

Company Response:

The Company agrees with this finding. The Company will continue to monitor data quality and is taking steps to mitigate the effects that clerical errors may have on our statutory reporting and filings. Examples of current activities in progress include periodic group reporting analysis by funding type as well as calibration of membership to the Company corporate census report. These actions help increase the level of accuracy and ensure groups and members are correctly assigned by line of business.

2. Safekeeping of Private Placements

The Company needs to improve its procedures or controls for the safekeeping of private placement securities. The following security certificate was lost, or misplaced, and had to be replaced: Plans Liability, Ins.Co - Stock certificate representing 12.15 shares originally issued on December 1, 1998; replaced on August 2, 2005.

It is recommended that the Company implement additional controls over private placement securities, which are kept on-site, to prevent stock certificates from being lost or misplaced.

Company Response:

The Company agrees with the finding. However, it should be noted that these certificates are non-negotiable and that the corporate assets they represent were never at risk from loss or theft. Subsequent to this finding, measures were taken to comply with the recommendation and all private placement stock certificates have been placed in a safety deposit box at a Bank of America branch in Seattle.

3. 401 (k) Plan

Payroll data transmitted to the Company's 401(k) Plan trustee was incomplete, thus the non-discrimination test (NDT) performed by the Plan trustee was invalid. The NDT is an important test that a qualified retirement plan must pass in order to qualify for favorable tax accounting treatment. Without a valid NDT, the 401(k) Plan is potentially at risk of losing its qualified status since plan non-compliance issues may not be detected, and rectified, in a timely manner. The Company later was able to identify the errors and the Plan's status was not adversely affected.

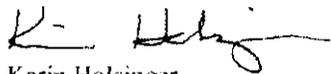
It is recommended that the Company establish procedures and implement controls to ensure that all future information transmitted to the Plan trustee is accurate and complete.

Company Response:

The Company agrees with this finding. While the amounts were de minimis and the deferrals and contributions were transmitted and posted on a timely basis, corrective measures have been implemented to ensure that year-end contributions and deferrals are identified and designated to the appropriate plan year.

Please feel free to contact me at (503) 226-5922 with any further questions or concerns that you have regarding our responses.

Sincerely,



Karin Holsinger
Director, Financial Accounting Services