

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



**FINANCIAL EXAMINATION**

of

**Group Health Cooperative  
Seattle, Washington**

NAIC CODE 95672  
DECEMBER 31, 2008

Order No. 10-113  
Group Health Cooperative  
Exhibit A

**SALUTATION**

Seattle, Washington  
June 18, 2010

The Honorable Mike Kreidler, Commissioner  
Washington State Office of the Insurance Commissioner (OIC)  
Insurance Building – Capitol Campus  
302 Sid Snyder Avenue SW, Suite 200  
Olympia, WA 98504

Dear Commissioner Kreidler:

In accordance with your instructions, and in compliance with the statutory requirements of RCW 48.46.120 and RCW 48.03.010, an examination was made of the corporate affairs and financial records of

**Group Health Cooperative**

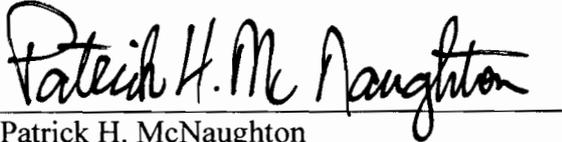
of

Seattle, Washington

hereinafter referred to as "GHC" or the "Company," at the location of its home office, 320 Westlake Avenue North, Suite 100, Seattle, Washington 98109. This report is respectfully submitted showing the condition of the Company as of December 31, 2008.

**CHIEF EXAMINER'S AFFIDAVIT**

I hereby certify I have read the attached Report of the Financial Examination of Group Health Cooperative of Seattle, Washington. This report shows the financial condition and related corporate matters as of December 31, 2008.



Patrick H. McNaughton  
Chief Examiner

6-18-10

Date

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## **SCOPE OF THE EXAMINATION**

This examination covers the period January 1, 2004 through December 31, 2008 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 (FCEH). The examination included identification and disposition of material transactions and events occurring subsequent to the date of examination through the end of field work on June 3, 2010.

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 accountants' (CPA's) work papers were reviewed and utilized, where possible, to facilitate efficiency in the examination.

## **INSTRUCTIONS**

The examiners reviewed the Company's filed 2008 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).

### **1. NAIC Annual Statement Errors and Misclassifications**

The results of the examination disclosed instances in which the Company's filing of the 2008 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 deficiencies, none of the following items were material to the financial statements and no examination adjustments were necessary.

a. **Real Estate Investments**

In the Notes to Financial Statements, No. 5.F, the Company only included information on real estate held for the production of income. Note No. 5. F. requires other disclosure information such as real estate held for sale which GHC holds but did not disclose.

b. **Material Related Party Transactions**

In the Notes to Financial Statements, No. 10.B, the Company states that it did not have material related party transactions in the reporting period. The Company had material transactions with Group Health Options, Inc. (GHO) and KPS Health Plans (KPS). Per the 2008 NAIC Annual Statement Instructions for Notes to Financial Statements, Note 10, the financial statements should include disclosures of all material related party transactions. The disclosures should include descriptions of the transactions for each of the periods for

which financial statements are presented, and such other information considered necessary to obtain an understanding of the effects of the transactions on the financial statements.

c. Settlement of Inter-Company Transactions

In the Notes to Financial Statements, No. 10.D, GHC reported amounts due from affiliates of \$37,623,128 as amounts due from Group Health Cooperative. The 2008 NAIC Annual Statement Instructions for Note 10 require the reporting of amounts due from related parties. The amounts due were from GHO, KPS, and Group Health Foundation (GHF); not from GHC.

In addition, inter-company transactions were not settled on a monthly basis as disclosed in Note 10.D. Inter-company transactions between GHC and KPS were settled once every three to five months. Inter-company transactions between GHC and GHF were settled twice a year.

d. Repayment of Loan

In the Notes to Financial Statements, No. 14.A, the Company did not disclose the nature and amount of the guarantees relating to the loan for the construction and long-term financing of the Westlake Terry Building, the principal offices for GHC. The Company and City Investors V LLC have joint and severable liability for repayment of the loan in full under certain circumstances for the Westlake Terry Building. The circumstances in which the Company becomes liable and the amount of the loan or contingent commitment that remains at December 31, 2008 should be disclosed. The 2008 NAIC Annual Statement Instructions require that the nature and amount of guarantees should be disclosed. The value of any possible recovery should also be included.

e. Medicare Risk Corridor

The experience rating refunds for the Company's Medicare Part D obligation in the amount of \$1,324,251 was misclassified in the Company's 2008 NAIC Annual Statement as "Premiums received in advance" instead of "Aggregate health policy reserves". In addition, the Company did not record the liability as a separate line item in the Statement of Actuarial Opinion as required in the 2008 NAIC Annual Statement Instructions, page 10, paragraph 5.F. SSAP No. 66, paragraph 8.b.ii, requires experience rating returns to be recorded in the NAIC Annual Statement, Underwriting and Investment Exhibit, Part 2D, in column 1, line 4, and on the Balance Sheet as "Aggregate health policy reserves".

f. Potential Risk Exposure

The Company incorrectly calculated the risk exposure on an interest rate swap agreement at \$3,729,890. Based on the formula required in the 2008 NAIC Annual Statement Instructions for Schedule DB, Part C, Section 1, column 15, the correct risk exposure should have been calculated as \$1,984,313.

g. Misclassification of Prescription Drugs

In the 2008 NAIC Annual Statement, the Company included in error prescription drug administrative fees as part of the expense for "Prescription drugs" on page 4, line 13. Administrative fees for prescription drugs should be recorded under the "Claims

adjustment expenses” on page 4, line 20 and on the Underwriting and Investment Exhibit, Part 3 - Analysis of Expenses, on page 14, line 14.

h. Medicare Cost Sharing and Medicare Reinsurance

The Company incorrectly recorded Medicare Low-Income Cost Sharing (LICS) and Medicare Reinsurance in its 2008 Annual Statement as “Premiums received in advance”. The amount of \$620,675 (LICS) and \$207,635 (Reinsurance) should have been recorded as “Amounts receivable relating to uninsured plans” in accordance with SSAP 47.

i. Derivative – Cap on Early Termination Clause

In the Notes to Financial Statements, No. 8, for an interest rate swap agreement the disclosure note does not reflect the terms of the contract to include potential losses and incorrectly cites the market value. The Company states, “The terms include a provision to cap the market value of the swap at \$22,500,000.” However, according to the swap agreement, the \$22,500,000 is the maximum potential loss to GHC in an early termination clause, not a cap on the market value as stated. In addition, there are other potential losses that should have been disclosed such as interest rate losses and market value losses.

j. Reserves for Long-Term Health Care

In the Underwriting and Investment Exhibit, Part 2D, the reserve for the long-term health care line of business of \$4,537,908 was recorded on line 5, “Aggregate write-ins for other policy reserves”. In accordance with SSAP No. 54, paragraphs 13 and 19, the current claim obligation should be reclassified to line 11, “Aggregate write-ins for other claim reserves”. Each of these components should carry forward to the Liabilities, Capital, and Surplus, page 3, line 4, “Aggregate health policy reserves” and line 7, “Aggregate health claim reserves”, respectively.

**The Company is instructed 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 AP&P, and WAC 284-07-050(2) which requires adherence to the NAIC Annual Statement Instructions.**

**2. Settlement of Inter-Company Balances**

In 2008, GHC did not settle its inter-company transactions with KPS on a timely basis, and did not charge KPS an annual administrative fee as required by the inter-company administrative services agreement (ASA). Section 7.1 of the ASA requires that inter-company transactions be settled on a monthly basis. The First Amendment to the ASA Schedule B, Section 2, requires an annual administrative fee with annual adjustments.

**In accordance with RCW 48.31C.050(5), GHC is instructed to follow the existing inter-company ASA or file a new Form D with the OIC that correctly reflects the terms.**

### **3. Custodial Agreement Deficiencies**

The Company did not have a custodial agreement for securities on deposit with Bank of America. The Company erred in stating this is a money market account which is similar to a bank account. The investment is in a mutual fund and therefore classified as a security. In addition, the custodial agreement with Bank of New York did not include several provisions of RCW 48.13.480 such as the requirement that all custodian securities that are registered shall be registered in the name of the company.

**The Company is instructed to execute a custodial agreement with Bank of America and to amend a custodial agreement with Bank of New York that contains the required terms under RCW 48.13.480.**

### **4. Approval of Investment Transactions**

The Board of Trustees' (BOT) meeting minutes did not document approval of investment transactions. RCW 48.13.340 requires all investments, loans, sales or exchanges to be approved or authorized by the BOT or by a committee charged by the BOT with the duty of making said investment, loan, sale or exchange. The minutes of any said committee shall be recorded and reports submitted to the BOT for approval or disapproval.

**Pursuant to RCW 48.13.340, the Company is instructed to obtain and document approval by the BOT for all investments purchased. Pursuant to RCW 48.13.350(1), a permanent written record of investment transactions must be kept and authorized by an officer or by the chairman of the committee authorizing the investment.**

### **5. Security Deposit Non-Admitted**

GHC had a Washington State Labor and Industries Department (L&I) security deposit of \$5,769,367. This amount represented the required deposit imposed by L&I since GHC was self-insured with respect to its workers' compensation, safety, and labor protection. The fund was held at Bank of New York Mellon, was designated for a specific purpose, and thus was neither accessible nor available to the general public. As such, the entire amount should have been non-admitted. No adjustment is required because the amount is below the examination materiality level.

**The Company is instructed to non-admit the Labor and Industries security deposit of \$5,769,367 that was held at Bank of New York Mellon, pursuant to SSAP No. 4, paragraph 2, and SSAP No. 87, paragraph 3, and comply with RCW 48.43.097 by filing a true annual statement in compliance with the NAIC Annual Statement Instructions and the AP&P as required by WAC 284-07-050(2).**

## **COMMENTS AND RECOMMENDATIONS**

None

## COMPANY PROFILE

### **Company History**

Group Health Cooperative was organized in 1945 in the state of Washington and received its original certificate of registration on April 7, 1976 as a health maintenance organization (HMO) pursuant to Chapter 48.46 RCW. The Company changed its name effective December 31, 2002, from Group Health Cooperative of Puget Sound by dropping the words “of Puget Sound”.

### **Capitalization**

Pursuant to RCW 48.46.235, GHC met minimum capital requirements with approximately \$550 million net worth (capital and surplus) as of December 31, 2008.

### **Territory and Plan of Operation**

GHC owns and operates its own medical facilities throughout the state of Washington and hires medical support personnel to staff them. GHC also contracts with Group Health Permanente, P.C. (GHP), an independent contractor, for the provision of medical services and also contracts with outside medical providers on a fee-for-service or capitated basis for services unavailable through its own facilities. Based in Seattle, Washington, GHC and its subsidiary health carriers, Group Health Options, Inc, and KPS Health Plans, serve more than half a million residents in Washington and Idaho. In Washington, the Company offers coordinated-care plans for both groups and individuals; residents who qualify for Medicaid Title XIX (Healthy Options), Medicare Title XVIII, Basic Health Plan, the State Children’s Health Insurance Plan (SCHIP), and the Federal Employees Health Benefit Plan.

### **Growth of Company**

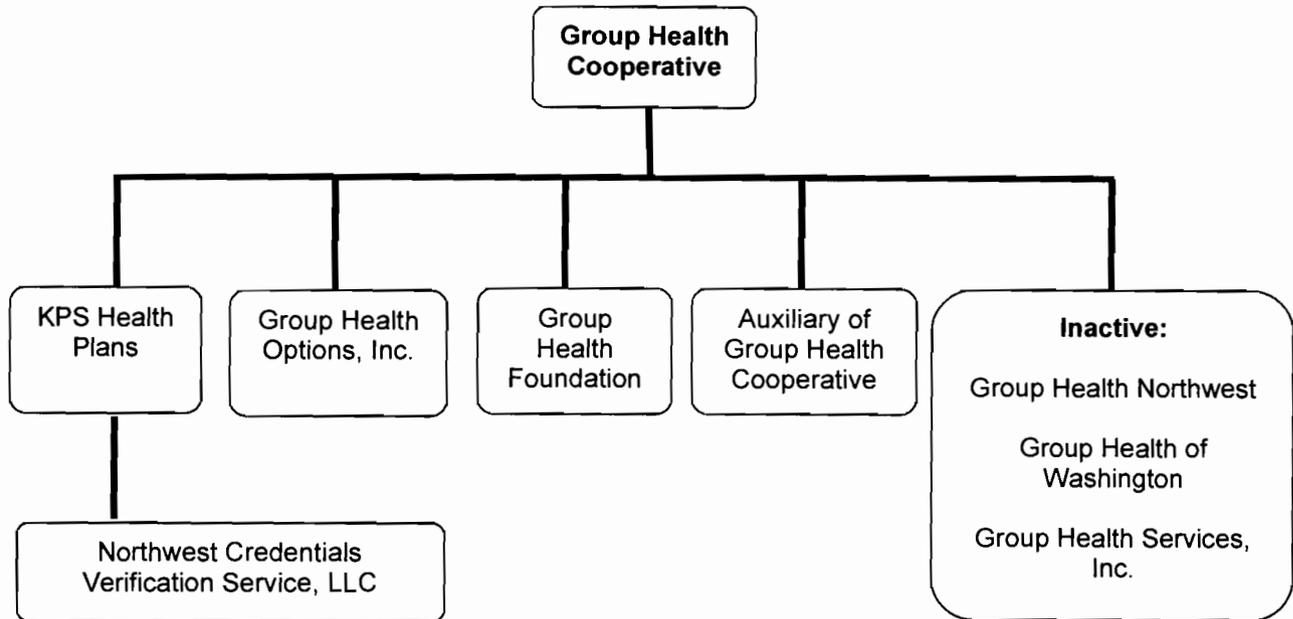
The following reflects the growth of the Company as reported in its filed NAIC Annual Statements for the five year period under examination:

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>
<b>Assets, Liabilities,</b>					
<b>Capital and Surplus:</b>					
Admitted Assets	\$899,307,217	\$1,001,047,180	\$1,382,832,495	\$1,444,272,520	\$1,380,675,192
Liabilities	521,322,385	562,477,535	747,691,839	706,518,789	830,440,298
Capital and Surplus	<u>377,984,832</u>	<u>438,569,645</u>	<u>635,140,656</u>	<u>737,753,731</u>	<u>550,234,894</u>
<b>Revenue and Expenses:</b>					
Premiums Earned	1,997,805,726	2,143,686,808	2,301,743,059	2,242,125,443	1,939,291,775
Net Underwriting Deductions	<u>1,923,327,660</u>	<u>2,067,083,796</u>	<u>2,125,164,874</u>	<u>2,235,278,682</u>	<u>1,909,421,901</u>
Underwriting Gain or Loss	74,478,066	76,603,012	176,578,185	6,846,761	29,869,874
Investment and Other Income	<u>16,679,717</u>	<u>24,269,756</u>	<u>45,845,689</u>	<u>57,347,393</u>	<u>(54,220,286)</u>
Pre-Tax Income	91,157,783	100,872,768	222,423,874	64,194,154	(24,350,412)
Taxes Incurred			91,500	19,352	
<b>Net Income</b>	<u>\$91,157,783</u>	<u>\$100,872,768</u>	<u>\$222,332,374</u>	<u>\$64,174,802</u>	<u>(\$24,350,412)</u>

## AFFILIATED COMPANIES

### Organization Chart

The following is an organization chart as of December 31, 2008:



#### **Group Health Options, Inc.**

GHO was incorporated in 1990 as a wholly owned subsidiary of GHC. GHO was issued a certificate of registration as a health care service contractor (HCSC) in the state of Washington on October 23, 1990. It offers a variety of health plans in Washington and Idaho. These plans range from a defined physician-network plan to point-of-service plans in which members can get care from outside the network for higher out-of-pocket costs. An administrative services agreement (ASA) was prepared between GHC and GHO wherein GHC contracted to provide a wide range of administrative support services to GHO. GHC and GHO also entered into a medical services agreement (MSA) through which GHC agreed to provide or arrange medical services to enrollees of GHO on a capitated basis.

#### **KPS Health Plans**

KPS is a Washington taxable nonprofit corporation registered and operating as a health care service contractor (HCSC) and is headquartered in Bremerton, Washington. KPS provides health care services through contracts with participating physicians and hospitals.

#### **Northwest Credentials Verification Service, LLC (NCVS)**

NCVS, a Washington limited liability company, performs primary source credentials verification of health care providers requesting new or continued participation with KPS and contracts nationally with health plans, hospitals and other organizations to provide credentials verification services. NCVS is a wholly owned subsidiary of KPS.

**Group Health Foundation**

GHF (formerly the Group Health/Kaiser Permanente Community Foundation) is a Washington nonprofit corporation organized September 28, 1983, and a supporting organization to GHC under section 501(c)(3) of the Internal Revenue Code. The name was changed in December 2008 to GHF. GHF is registered in the state of Washington as a charitable gift annuity organization and is organized exclusively to benefit, to perform the functions of, and to carry out the purposes of GHC by securing, investing, and allocating charitable gifts in order to support research, health career training, health education, and other charitable programs that support the purpose of GHC. GHF is a membership corporation and has no capital stock. The membership of GHF consists of those persons elected as trustees of GHC.

**Auxiliary of Group Health Cooperative (Auxiliary)**

The Auxiliary is an unincorporated association. It is organized for the purpose of promoting and advancing the welfare of GHC through fund raising in order to provide services and gifts to the hospitals, medical centers, specialty centers and health related programs of GHC and its patients.

**Inactive Affiliates**

Group Health Northwest, Group Health of Washington and Group Health Services, Inc., are inactive affiliates of GHC. These affiliates have been inactive during the examination period of 2004-2008.

**INTERCOMPANY AGREEMENTS**

The Company had several in-force agreements with affiliates. As a member of a health carrier holding company system, these agreements and any amendments with effective dates May 7, 2001 and later must be filed with the OIC pursuant to RCW 48.31C.050(2). As of December 31, 2008, the Company had the following intercompany agreements in force:

### **Administrative Services Agreement (ASA) between GHC and GHO**

The January 01, 2008 ASA superseded and replaced all amendments dating back to January 01, 2001. It is indefinite in term, subject to termination with or without cause pursuant to the terms of the contract. GHO engages GHC to provide to or on behalf of GHO the administrative services described in Schedule A of the agreement. Through Schedule B of the agreement, GHO compensates GHC based on a cost-allocation methodology using a per member per month basis. The ASA has been submitted to the OIC in a Form D filing.

### **Medical Services Agreement (MSA) between GHC and GHO**

The current MSA was amended on January 1, 2002. It is indefinite in term, subject to termination with or without cause pursuant to the terms of the contract. Generally, GHC performs as an independent contractor and provides covered medical care services to GHO enrollees who elect to receive care from GHC as described within this agreement. GHO compensates GHC according to Appendix A of the agreement. The compensation arrangement was on a capitated percentage of GHO premiums.

### **Administrative Services Agreement (ASA) between GHC and KPS**

An administrative services agreement was entered into between KPS and GHC, effective January 1, 2007. GHC is to provide administrative services to KPS in the area of legal services, risk management and insurance services, internal audit services, governance services, and financial services. Schedule A, B, C and D of the ASA provide the compensation calculation from KPS to GHC. The agreement remains in effect until written notice of termination. The ASA has been filed via Form D with the OIC.

### **Agreement between GHC and GHF**

An agreement was entered on April 3, 2001 between GHC and GHF for an indefinite period unless terminated by written notice of either party given ninety days prior notice to the date of termination. GHC agrees to contribute to GHF, as consistent with GHC's own operational needs, certain of its personnel and services to assist GHF in its development and community service efforts. At its sole discretion, GHC may make a contribution of funds necessary to support certain work of GHF, but no other payments are called for by the agreement. This agreement has been filed with the OIC.

## **MANAGEMENT AND CONTROL**

### **Ownership**

The Company is organized as a nonprofit membership corporation under Chapter 24.03 RCW. Its restated Articles of Incorporation effective January 8, 2003, state that the corporation shall have no capital stock and that no one shall receive any pecuniary gain or benefit by reason of their membership in the corporation. Membership in GHC is open to those consumers who believe in its purposes and in democratic cooperative principles. Consumers apply for membership and are admitted to membership upon compliance with the requirements and procedures established by the Board of Trustees pursuant to the corporate bylaws. If the corporation is dissolved, any monies or assets remaining after payment of creditors and the return to members of the capital (membership fees) invested by each, shall be donated by the

Board of Trustees to some public, nonprofit or charitable health organization having purposes similar to those of GHC.

### **Board of Trustees (BOT)**

Board of Trustees (BOT) as of December 31, 2008:

Jerry F. Campbell, Chair  
Bobbie A. Berkowitz, Vice Chair  
Ruth A. Ballweg  
Phyllis C. Best  
Ann E. Daley  
Rosemary Daszkiewicz  
Porsche Everson  
Ira M. Fielding  
Jennifer Joly  
Robert J. Margulis  
ChangMook Sohn

### **Officers**

Officers as of December 31, 2008:

Jerry F. Campbell	Chair, Board of Trustees
Bobbie A. Berkowitz	Vice Chair, Board of Trustees
Scott E. Armstrong	President and CEO
Pamela A. MacEwan	Assistant Secretary
Richard E. Magnuson	Treasurer
Breton C. Myers	Assistant Treasurer
Rick D. Woods	Vice President, Secretary

### **Conflict of Interest**

The Company's policy requires that members of the BOT and officers file a conflict of interest statement each year. Any conflict is referred to the chief compliance officer or executive vice president or general counsel for final resolution. The purpose of the statement is to detect any activities or participation on the part of the trustees/officers that could possibly be interpreted as a conflict of interest. No exceptions were noted.

### **Fidelity Bond and Other Insurance**

The Company is a named insured on a Financial Institution Fidelity Bond. An aggregate loss limit of coverage in the amount of \$10,000,000 is provided for all of the affiliated companies insured and the single loss deductible is \$100,000. The minimum amount recommended by the NAIC for the insured companies is \$2,000,000 to \$2,250,000. The aggregate amount of coverage meets the NAIC recommended level for the Company.

The Company is also provided protection against certain property and liability losses as a named insured on several other purchased insurance policies. Policies in effect at December 31, 2008 provided the following coverage:

- Directors' and officers' liability insurance including employment practices liability coverage
- Fiduciary liability
- Professional, general, automobile and employers liability
- Kidnap/ransom and extortion
- Property
- Excess workers' compensation
- Errors and omission

The Company also maintains a self insurance fund for professional liability risk, industrial insurance, and unemployment insurance. The Company reported a cash reserve in the amount of \$76,023,479 for that fund as of December 31, 2008. The professional liability risk includes an amount to indemnify employees of the independent contractor GHP as agents of GHC.

#### **Officers', Employees', and Agents' Welfare and Pension Plans**

Group Health Cooperative maintains the following qualified retirement plans for the benefit of eligible employees: (1) Group Health Cooperative Employee Defined Contribution Plan, and (2) Group Health Cooperative 403(b)(7) Restated Group Custodial Account Agreement (deferred compensation).

Prepaid pension assets in the amount of \$44,398,365 were non-admitted pursuant to SSAP No. 8, paragraph 7. The Company also reported a liability for retiree medical benefits in the amount of \$52,663,000. The OIC actuary reviewed the documentation provided by Milliman USA that supports the reserve.

The Company also has procedures in place to determine and monitor various accrued liabilities for salaries, severance pay, vacation pay, and retirement benefits. No under accruals were noted and reasonable amounts were included as general expenses due and accrued.

#### **CORPORATE RECORDS**

The Articles of Incorporation, Bylaws, Certificate of Registration, and minutes of the BOT and committees were reviewed for the period under examination. All BOT meetings were conducted with a quorum present. No exceptions were noted.

## **ACTUARIAL REVIEW**

The OIC health actuary reviewed the Company's actuarial report, claims unpaid, and other claim liabilities as of December 31, 2008. This review included: examining the Company's reserving philosophy and methods to determine the reasonableness of the claim liabilities; verifying that claim liabilities included provisions for all components noted in SSAP No. 54 Paragraphs 12, 13, 18 and 19 and SSAP No. 55, Paragraphs 7 and 8; reviewing historical paid claims and loss ratios; checking the consistency of the incurred-paid data from the Company system to the amounts reported in the 2008 NAIC Annual Statement; and estimating claims unpaid as of December 31, 2008.

GHC claim data provided to the opining actuary is used to estimate the Company's "Claims unpaid" obligations. To check for consistency of the data to the figures reported in the 2008 NAIC Annual Statement, the actuary's claim triangle data was compared to the corresponding claim information from the Underwriting and Investment Exhibit Part 2B for the 2008 NAIC Annual Statement. Additionally, the claims paid during 2008 from the actuary's data was compared to the corresponding data from the updated (through April 2009) claims triangle provided by the Company. Lastly, the data from sample cells of the actuary's incurred paid triangles were submitted for testing against data from the Company's GL. The reconciliation and data testing outcomes were within acceptable ranges.

## **REINSURANCE**

The Company did not utilize reinsurance as of December 31, 2008.

## **STATUTORY DEPOSITS**

The Company has two required statutory deposits with the state of Washington as of December 31, 2008.

The State of Washington Department of Labor and Industries requires a statutory deposit pursuant to RCW 51.14.020(2) and RCW 51.14.060 to qualify as a self insurer. The Bank of New York Mellon is holding funds in the amount of \$5,769,367.

The OIC requires the filing of the Underwriting of Indemnity Calculation or Funded Reserve form. The security held was identified as a Dreyfus Institutional Reserves Money Market Fund in the amount of \$166,957. The funds are being held by the custodian, Bank of New York Mellon. This special deposit satisfies the funded reserve valuation requirements of RCW 48.46.240. The Company is in compliance with the filing requirements of WAC 284-07-050(8).

## **ACCOUNTING RECORDS AND INFORMATION SYSTEMS**

The Company maintains its accounting records on a Generally Accepted Accounting Principles (GAAP) accrual basis of accounting and adjusts to Statutory Accounting Practices (SAP) basis for NAIC Annual Statement reporting. The Company was audited annually by the certified public accounting firm of Deloitte & Touche, LLP for 2004 to 2007 and by KPMG for 2008. The Company 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. Control weaknesses described in a management letter from KPMG were acknowledged by the Company and slated for correction in the future.

The management of Group Health Cooperative (GHC) is sufficiently knowledgeable of information systems (IS) operational issues and provides direction and oversight through its information technology (IT) Strategy Council and IS Operations Council. Systems development, acquisition and maintenance controls were evaluated to gain assurance that appropriate internal controls are in place. The Company maintains operations procedures and an information security policy that defines the responsibilities of users, management and IS personnel.

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 internal controls exercised to maintain data security. The Company has sufficient internal controls in place to monitor system activity and processes.

During the prior examination period, GHC did not have a formal written business contingency or disaster recovery plan. It did not have an agreement or contract for the use of an alternative data center in the event the data facility necessitates relocation. GHC is in the process of putting together a detailed, written business contingency plan and disaster recovery plan. It includes appropriate escalation procedures to resolve operational failures in a timely manner and 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. GHC has built a systems recovery site at its facility located in Liberty Lake, Washington. The portion of the plan that has been completed has been tested, and the plan has been updated according to test results.

## **FINANCIAL STATEMENTS**

The following examination financial statements show the financial conditions of Group Health Cooperative as of December 31, 2008:

Assets, Liabilities, Capital and Surplus  
Statement of Revenue and Expenses  
Five Year Reconciliation of Surplus

**GROUP HEALTH COOPERATIVE  
ASSETS, LIABILITIES, CAPITAL AND SURPLUS  
AS OF DECEMBER 31, 2008**

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
<b>Assets</b>			
Bonds	\$547,235,939	\$0	\$547,235,939
Preferred stocks	100,000		100,000
Common stocks	169,517,159		169,517,159
Real estate:			
Properties occupied by the company	270,275,333		270,275,333
Properties held for sale	20,248,035		20,248,035
Cash and short-term investments	211,204,038		211,204,038
Other invested assets	17,843,173		17,843,173
Receivable for securities	93,562		93,562
Aggregate write-ins for invested assets:			
Funds held by trustee	9,434,314		9,434,314
Interest Rate Swap	5,485,487		5,485,487
Investment income due and accrued	5,576,860		5,576,860
Uncollected premiums and agents' balances	28,434,550		28,434,550
Amounts receivable relating to uninsured plans	781,284		781,284
Electronic data processing equipment and software	7,773,559		7,773,559
Furniture and equip., incl. health care delivery assets	55,692,252		55,692,252
Receivable from parent, subsidiaries and affiliates	626,773		626,773
Health care and other amounts receivable	27,972,916		27,972,916
Aggregate write-ins for other than invested assets:			
Other deposits/assets	2,379,958		2,379,958
<b>Total Assets</b>	<b><u>\$1,380,675,192</u></b>	<b><u>\$0</u></b>	<b><u>\$1,380,675,192</u></b>
<b>Liabilities, Capital, and Surplus</b>			
Claims unpaid	\$123,944,780	\$0	\$123,944,780
Unpaid claims adjustment expenses	5,285,083		5,285,083
Aggregate health policy reserves	29,270,945		29,270,945
Premium received in advance	6,654,492		6,654,492
General expenses due or accrued	116,382,091		116,382,091
Current federal and foreign income tax payable and interest thereon	94,800		94,800
Amounts withheld or retained for the account of others	972,576		972,576
Borrowed money and interest thereon	200,617,629		200,617,629
Amounts due to parent, subsidiaries and affiliates	27,040,228		27,040,228
Aggregate write-ins for other liabilities:			
Additional pension minimum liability	140,493,688		140,493,688
Self insurance fund	76,023,479		76,023,479
Retiree medical benefits	55,014,000		55,014,000
Capitation claim liability	24,385,350		24,385,350
Deferred gain on sale of real estate	22,121,953		22,121,953
Center for Health Studies grants	1,460,262		1,460,262
Miscellaneous unearned deposits	237,263		237,263
Unclaimed properties	441,679		441,679
<b>Total Liabilities</b>	<b><u>830,440,298</u></b>	<b><u>0</u></b>	<b><u>830,440,298</u></b>
Common capital stock			0
Gross paid in and contributed surplus	15,468,500		15,468,500
Unassigned funds (surplus)	534,766,394		534,766,394
<b>Total Capital and Surplus</b>	<b><u>550,234,894</u></b>	<b><u>0</u></b>	<b><u>550,234,894</u></b>
<b>Total Liabilities, Capital and Surplus</b>	<b><u>\$1,380,675,192</u></b>	<b><u>\$0</u></b>	<b><u>\$1,380,675,192</u></b>

**GROUP HEALTH COOPERATIVE  
STATEMENT OF REVENUE AND EXPENSES  
FOR YEAR ENDING DECEMBER 31, 2008**

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
Member months	4,735,998		4,735,998
Net premium income	\$1,942,950,406		\$1,942,950,406
Change in unearned premium reserves	(1,621,445)		(1,621,445)
Fee-for-service	(13,184,159)		(13,184,159)
Risk revenue	9,827,458		9,827,458
Aggregate write-ins for other health care related revenues	1,319,515		1,319,515
<b>Total revenues</b>	<b>1,939,291,775</b>	<b>\$0</b>	<b>1,939,291,775</b>
<b><u>Hospital and Medical:</u></b>			
Hospital/medical benefits	1,440,793,380		1,440,793,380
Emergency room and out-of-area	70,455,151		70,455,151
Prescription drugs	202,323,572		202,323,572
Aggregate write-ins for other hospital and medical	1,107,290		1,107,290
<b>Subtotal</b>	<b>1,714,679,393</b>	<b>0</b>	<b>1,714,679,393</b>
<b><u>Less:</u></b>			
Total hospital and medical	1,714,679,393		1,714,679,393
Claims adjustment expenses	25,849,436		25,849,436
General administrative expenses	145,781,480		145,781,480
Increase in reserves for A&H contracts	23,111,592		23,111,592
<b>Total underwriting deductions</b>	<b>1,909,421,901</b>	<b>0</b>	<b>1,909,421,901</b>
Net underwriting gain or (loss)	29,869,874	0	29,869,874
Net investment income earned	35,498,381		35,498,381
Net realized capital gains or (losses)	(89,718,667)		(89,718,667)
Net investment gains or (losses)	(54,220,286)	0	(54,220,286)
Aggregate write-ins for other income or expenses	0		0
Net income or (loss) before FIT	(24,350,412)	0	(24,350,412)
Federal and foreign income taxes incurred	0		0
<b>Net Income (Loss)</b>	<b>(\$24,350,412)</b>	<b>\$0</b>	<b>(\$24,350,412)</b>
<b><u>CAPITAL AND SURPLUS ACCOUNT</u></b>			
<b>Capital and surplus prior reporting period</b>	<b>\$737,753,731</b>	<b>\$0</b>	<b>\$737,753,731</b>
Net Income (Loss) from above	(24,350,412)		(24,350,412)
Net unrealized capital gains and losses	1,330,940		1,330,940
Change in nonadmitted assets	(6,263,491)		(6,263,491)
Surplus adjustments:			
Paid in	(152,425)		(152,425)
Aggregate write-ins for gains or (losses) in surplus:			
Audit Adjustment	(17,589,760)		(17,589,760)
Additional minimum pension liability	(140,493,689)		(140,493,689)
Net change in capital and surplus	(187,518,837)		(187,518,837)
<b>Capital and surplus end of reporting period</b>	<b>\$550,234,894</b>	<b>\$0</b>	<b>\$550,234,894</b>

**GROUP HEALTH COOPERATIVE  
FIVE YEAR RECONCILIATION OF SURPLUS  
FOR THE YEARS ENDING DECEMBER 31,**

	<u>2008</u>	<u>2007</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
<b>Capital and Surplus, December 31, prior year</b>	<u>\$737,753,731</u>	<u>\$635,140,656</u>	<u>\$438,569,645</u>	<u>\$377,984,832</u>	<u>\$300,412,703</u>
Net income or (loss)	(24,350,412)	64,174,802	222,332,374	100,872,768	91,157,783
Change in valuation basis of aggregate policy and claim reserves					
Net unrealized capital gains and losses	1,330,940	(28,428,229)	23,151,580	117,943	1,888,152
Change in nonadmitted assets	(6,263,491)	20,990,930	(36,252,034)	(53,559,181)	(6,736,821)
Cumulative effect of changes in accounting principles	0	0	0	11,402,761	0
Surplus adjustments:					
Paid in	(152,425)	(155,400)	(155,925)	(135,100)	(140,575)
Aggregate write-ins for gains or (losses) in surplus:					
Audit adjustment	(17,589,760)	1,013,972	(12,504,984)	1,885,622	(8,596,410)
Actuarial adjustment to Medical Retiree Liability		45,017,000	0	0	0
Additional minimum pension liability	(140,493,689)	0	0	0	0
Net change in capital and surplus	<u>(187,518,837)</u>	<u>102,613,075</u>	<u>196,571,011</u>	<u>60,584,813</u>	<u>77,572,129</u>
<b>Capital and Surplus, December 31, current year</b>	<u><u>\$550,234,894</u></u>	<u><u>\$737,753,731</u></u>	<u><u>\$635,140,656</u></u>	<u><u>\$438,569,645</u></u>	<u><u>\$377,984,832</u></u>

**NOTES TO THE FINANCIAL STATEMENTS**

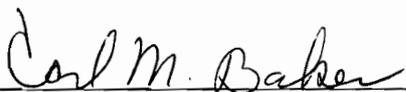
None

## ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers of Group Health Cooperative during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner; Jeanette Liao, CPA, Examiner-in-Charge; Kathy Hicks, CPA, Financial Examiner; Timothy F. Hays, CPA, JD, Investment Specialist; John R. Jacobson, AFE, CISA, AES, Automated Examination Specialist; Shiraz Jetha, FSA, FCIA, MAAA, Health Actuary; Cynthia Clark, CPA, Financial Examiner; Friday P. Enoye, Financial Examiner; Ann Kauffman, CPA, Financial Examiner; and Tony Quach, Financial Examiner; all from the Washington State Office of the Insurance Commissioner, participated in the examination and the preparation of this report.

Respectfully submitted,



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Carl M. Baker, CPA, CFE  
Supervising Examiner  
State of Washington

**AFFIDAVIT**

**STATE OF WASHINGTON**        }  
  }  
**COUNTY OF KING**                } **ss**  
  }

Carl M. Baker, being duly sworn, deposes and says that the foregoing report subscribed is true to the best of his knowledge and belief.

He attests that the examination of Group Health Cooperative was performed in a manner consistent with the standards and procedures required or prescribed by the Washington State Office of the Insurance Commissioner and the National Association of Insurance Commissioners (NAIC).

Carl M. Baker  
Carl M. Baker, CPA, CFE  
Supervising Examiner  
State of Washington

Subscribed and sworn to before me this 18<sup>th</sup> day of June, 2010.

Colleen Jansen  
Notary Public in and for the  
State of Washington

