

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



**FINANCIAL EXAMINATION**

of

**Washington State Health Insurance Pool  
Bow, Washington**

**December 31, 2007**

Order No. 09-01  
Washington State Health Insurance Pool  
Exhibit A

**SALUTATION**

Seattle, Washington  
December 30, 2008

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, Washington 98504

Dear Commissioner Kreidler:

In accordance with your instructions, and in compliance with the statutory requirements of RCW 48.41.070 and RCW 48.03.010, an examination was made of the corporate affairs and financial records of

**Washington State Health Insurance Pool**

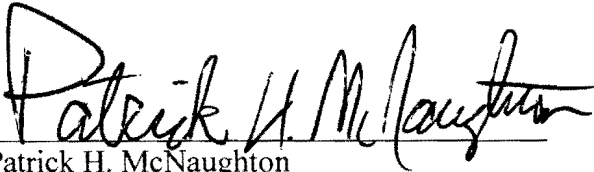
of

Bow, Washington

hereinafter referred to as “WSHIP” at the location of its third party administrator, 2015 16<sup>th</sup> Street, Great Bend, Kansas 67530. This report is respectfully submitted showing the condition of the WSHIP as of December 31, 2007.

**CHIEF EXAMINER'S AFFIDAVIT**

I hereby certify I have read the attached Report of the Financial Examination of the Washington State Health Insurance Pool of Bow, Washington. This report shows the financial condition and related business matters as of December 31, 2007.



Patrick H. McNaughton  
Chief Examiner

12-30-08

Date

## TABLE OF CONTENTS

<b>SCOPE OF THE EXAMINATION.....</b>	<b>1</b>
<b>COMMENTS AND RECOMMENDATIONS .....</b>	<b>1</b>
<b>WSHIP PROFILE.....</b>	<b>2</b>
WSHIP History .....	2
Organizational Funding and Structure.....	2
Acquisitions, Mergers, Disposals, Dissolutions, Purchases, and Sales .....	2
Growth of WSHIP .....	3
<b>AFFILIATED COMPANIES.....</b>	<b>3</b>
<b>MANAGEMENT AND CONTROL.....</b>	<b>3</b>
Ownership.....	3
Board of Directors .....	3
Officers .....	4
Conflict of Interest.....	4
Fidelity Bond and Other Insurance.....	4
Officers', Employees', and Agents' Welfare and Pension Plans .....	4
Agreements .....	4
<b>BUSINESS RECORDS.....</b>	<b>5</b>
<b>ACTUARIAL REVIEW .....</b>	<b>5</b>
<b>REINSURANCE .....</b>	<b>5</b>
<b>SPECIAL DEPOSITS.....</b>	<b>5</b>
<b>ACCOUNTING RECORDS AND INFORMATION SYSTEMS .....</b>	<b>5</b>
<b>SUBSEQUENT EVENTS.....</b>	<b>6</b>
<b>FOLLOW UP ON PREVIOUS EXAMINATION FINDINGS .....</b>	<b>6</b>
<b>FINANCIAL STATEMENTS.....</b>	<b>6</b>
Assets, Liabilities, Capital and Surplus .....	7
Statement of Revenue and Expenses .....	8
Surplus Reconciliation.....	9
<b>NOTES TO THE FINANCIAL STATEMENTS.....</b>	<b>10</b>
<b>ACKNOWLEDGMENT .....</b>	<b>11</b>
<b>AFFIDAVIT .....</b>	<b>12</b>

## SCOPE OF THE EXAMINATION

This examination covers the period beginning January 1, 2003 through December 31, 2007 and comprises a comprehensive review of the books and records of WSHIP. The examination followed the statutory requirements contained in the Washington Administration 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.

Business records, external reference materials, and various aspects of WSHIP'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, WSHIP's certified public accountant's (CPA) work papers were reviewed and utilized, where possible, to facilitate efficiency in the examination.

## COMMENTS AND RECOMMENDATIONS

The examiners reviewed WSHIP's 2003 through 2007 Annual Financial Reports as part of the statutory examination authorized under Chapters 48.41 and 48.03 RCW and Chapter 284-91 WAC. WSHIP files an Annual Financial Report with the OIC. RCW 48.41.070 requires that an annual financial report be submitted to the OIC in a form approved by the commissioner. WSHIP's audited financial reports state that they are audited in conformity with accounting practices prescribed or permitted by the OIC and accounting principals generally accepted in the United States of America.

### **1. Overstatement of Assets and Liabilities**

WSHIP has been incorrectly recording an asset and offsetting liability when billing for premiums before the due date. The recording of an asset and liability for billed premiums is an incorrect accounting procedure in that it overstates total assets and total liabilities, however, this accounting procedure had no effect on income.

For year 2003, WSHIP debited, "Uncollected premiums in the course of collection", and credited, "Aggregate health policy reserves", incorrectly. For years 2004 through 2006, WSHIP debited, "Uncollected premiums in the course of collection", and credited, "Premiums received in advance", incorrectly. To properly account for premiums, WSHIP should not record premiums until the due date.

**The above accounting treatment was discussed by the examination team with WSHIP and WSHIP's CPA firm. WSHIP agreed to make appropriate changes to future Annual Financial Reports.**

## **2. Access to Datacenter should be Limited to Information System (IS) personnel**

The president, general manager and the claims operations manager have access to the datacenter. Access to the datacenter should be limited to IS personnel who have specific job functions that need to be performed within the datacenter.

**It is recommended that, if access to the datacenter is required by individuals other than IS personnel, they should sign in, using an entry log, and be escorted by someone from the IS department.**

## **WSHIP PROFILE**

### **WSHIP History**

WSHIP was established in 1987 by the state of Washington, under Chapter 48.41 RCW, the Health Insurance Coverage Access Act as a nonprofit unincorporated entity, to make health care coverage available for eligible persons in the state of Washington who have been rejected for individual coverage by licensed insurance carriers. WSHIP has the authority to assess insurance companies writing health premiums in the state of Washington for all losses of WSHIP. Assessments are made periodically throughout the year as funds are needed to pay benefits to insured persons and to maintain a positive surplus position.

### **Organizational Funding and Structure**

Organizational funding and structure are obtained through assessments to insurer members. There are four classes of insurer members as defined in Article VI of the Articles of Organization. Assessments of the insurer members are determined and approved by the Board of Directors (BOD) and are recognized as a contribution to accumulated surplus. Assessment receivable represents outstanding balances assessed to insurance companies, but not yet collected.

In addition to member assessments, there are two other sources of funds that are applied directly to "Unassigned surplus". Excess loss receipts represent funds received from member carriers for loss experience beyond statutorily defined limits on certain lines of business, and are recognized as a contribution to "Unassigned surplus". Grant funds from the Federal Government are usually earmarked to be used in a specific way.

### **Acquisitions, Mergers, Disposals, Dissolutions, Purchases, and Sales**

There are no plans for acquisitions, mergers, disposals, dissolutions, purchases or sales.

## Growth of WSHIP

The following reflects the growth of WSHIP based on information filed in the Annual Financial reports for the five years ended December 31:

<u>Year</u>	<u>Premium Income</u>	<u>Member assessments</u>	<u>Net investment gain (loss)</u>	<u>Other income</u>	<u>Total underwriting deductions</u>	<u>Net change in capital and surplus</u>
2007	\$18,617,550	\$37,868,709	\$456,626	\$47,253	(\$60,923,667)	(\$3,933,529)
2006	18,250,241	31,737,155	404,148	3,149,873	(45,845,306)	7,696,111
2005	17,483,874	37,677,862	348,200	352,761	(53,662,639)	2,200,058
2004	14,249,945	27,667,167	35,862	46,904	(53,693,867)	(11,693,989)
2003	12,829,025	18,732,850	62,510	1,310,317	(37,232,494)	(4,297,792)

## AFFILIATED COMPANIES

WSHIP is not affiliated with any other companies.

## MANAGEMENT AND CONTROL

### Ownership

The ultimate controlling entity is the Board of Directors (BOD).

### Board of Directors (BOD)

The BOD is composed of ten (10) directors, of which six are appointed by the governor of the state of Washington pursuant to the procedures specified in RCW 48.41.040(2). One member is elected by a vote of the Class A members (members that provide disability insurance or stop loss insurance), one member is elected by a vote of the Class B members (health care service contractors (HCSC)), one member is elected by a vote of the Class C members (health maintenance organizations (HMO)), and one member is elected by a vote by all members of WSHIP. No more than one director may be employed by the same member or an affiliate of the same member. In addition to the ten voting directors, the insurance commissioner of the state of Washington, or his designee, is a non-voting, ex-officio director. Directors serve a term of three years which may be adjusted as necessary to stagger the terms of all directors.

The following were members of the Board of Directors serving as of December 31, 2007:

G. Robert Appel	Mason General Hospital - Governor appointed, providers
Patti L. Carter	Pony Mailing (former owner) - Governor appointed, small business
Dorothy Graham	The Graham Group - Governor appointed, large business
Matthew Damon	Former WSHIP enrollee, retired - Governor appointed, consumer
Robert D. Jaffe, MD	Seattle King County Dept. of Health - Governor appointed, consumer
William Perkins	Governor appointed, insurance agents
James Grazko	Premera Blue Cross - Elected by HCSC's
Robert Thomas Moore	Group Health Cooperative - Elected by HMO's

Norman Seabrooks      Aetna – Elected by Disability Carriers  
Robert Scott Kuecker      Regence Blue Shield – Elected by all member plans  
Pete Cutler      Office of Insurance Commissioner, Ex Officio, Non-voting

**Officers**

WSHIP officers are appointed annually by the Board of Directors to serve a one year term. Officers allowed by WSHIP Bylaws are: president, vice presidents, a secretary and a treasurer. The following were officers serving as of December 31, 2007:

Robert Thomas Moore      President  
Robert D. Jaffe, MD      Vice President  
Patti L. Carter      Secretary/Treasurer  
Karen Larson      Executive Director

**Conflict of Interest**

WSHIP’s Conflict of Interest Policy and Procedure is stated in Article VIII of the Bylaws. Each director, principal officer and member of a committee annually prepares a statement of compliance which is reviewed by the BOD.

**Fidelity Bond and other Insurance**

WSHIP does not have fidelity insurance covering its three employees. Only the executive director has authority over cash transactions, but has not utilized that authority during the period of this examination. The BOD has chosen not to purchase fidelity insurance. However, Benefit Management, Inc. (BMI), does handle all of WSHIP cash transactions as well as those of other clients and carries fidelity insurance for the exposure that exists.

WSHIP carries property insurance, commercial general liability and directors and officers’ liability coverage for the protection of corporate assets.

**Officers’, Employees’, and Agents’ Welfare and Pension Plans**

WSHIP uses a Simple IRA plan, managed by Schwab Independent Investing, as a retirement plan for its employees. WSHIP contributes matching funds up to a limit per employee. The plan is subject to Internal Revenue Service regulations pertaining to deposits and withdrawals. The BOD approves all salaries and benefit packages.

**Third Party Agreement**

WSHIP contracts with a third party administrator, BMI, located in Great Bend, Kansas, to handle all of its premium billing and collection, claims adjudication and payment, policy administration and accounting functions effective through March 31, 2010. Pursuant to the agreement, WSHIP is charged a per member per month fee based on the number of active members. Additionally, WSHIP contracts BMI for preferred provider organization services, pharmacy benefits management, and case management services. The agreements and terms are approved by the BOD.



## **BUSINESS RECORDS**

The Articles of Organization, Bylaws, Operating Rules and minutes of the BOD and committees were reviewed for the period under examination. No exceptions were noted and all BOD meetings were conducted with a quorum present.

## **ACTUARIAL REVIEW**

The OIC health actuary reviewed WSHIP's actuarial report, claims unpaid, and other claim liabilities as of December 31, 2007. The review included examining WSHIP's reserving philosophy and methods to determine the reasonableness of the claim liabilities; verifying that claim liabilities included provisions for all pertinent actuarial components; reviewing historical paid claims and loss ratios; and estimating claims unpaid as of December 31, 2007.

The claim data provided to the examiners and to the opining actuary by WSHIP was consistent with the claim data reported in the 2007 Annual Financial Report, Underwriting and Investment Exhibit, Part 2B.

Upon reviewing the opining actuary's assumptions, methodologies, and calculations for the actuarial liabilities, and re-performing the same functions using more current data, the OIC actuary determined that the opining actuary's method is more conservative. Based upon this review, the opining actuary's method and estimate for the claim liabilities are satisfactory.

## **REINSURANCE**

WSHIP has no reinsurance program.

## **SPECIAL DEPOSITS**

There are no special deposits required for WSHIP.

## **ACCOUNTING RECORDS AND INFORMATION SYSTEMS**

Accounting records are maintained by BMI pursuant to an administrative services agreement. Accounting records are maintained on a Generally Accepted Accounting Principles (GAAP) accrual basis of accounting. WSHIP is audited annually by a CPA firm. WSHIP received an unqualified opinion for all years under review. Accounting procedures, internal controls, and transaction cycles were reviewed during the planning and testing phase of the examination.

The information system (IS) operational functions for WSHIP are also performed by BMI. The IS staff are sufficiently knowledgeable of IS operational issues. Systems development,

acquisition, and maintenance controls were evaluated to gain assurance that appropriate internal 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 internal controls exercised to maintain data security. BMI has sufficient internal controls in place to monitor system activity and processes.

There is a disaster recovery plan that includes an alternate site, which is available in the event of a disruption of normal business activities.

The president, general manager and the claims manager have access to the datacenter. Access to the datacenter should be limited to IS personnel who have specific job functions that need to be performed within the datacenter, as recommended by best business practices. (See Comments and Recommendations No. 2.)

### **SUBSEQUENT EVENTS**

No material subsequent events were disclosed during the examination.

### **FOLLOW UP ON PREVIOUS EXAMINATION FINDINGS**

There were no prior examination report findings that required follow up.

### **FINANCIAL STATEMENTS**

The following examination financial statements show the financial condition of the Washington State Health Insurance Pool, as of December 31, 2007:

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

**WASHINGTON STATE HEALTH INSURANCE POOL  
ASSETS, LIABILITIES, CAPITAL AND SURPLUS  
December 31, 2007**

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
<b>Assets</b>			
Cash and short-term investments	\$10,880,876		\$10,880,876
Premiums and considerations:			
Uncollected premiums and agents' balances	109,016		109,016
Aggregate write-ins for other than invested assets:			0
Member assessments receivable	3,603,424		3,603,424
Accounts receivable	349,531		349,531
<b>Total Assets</b>	<u><u>\$14,942,847</u></u>	<u><u>\$0</u></u>	<u><u>\$14,942,847</u></u>
<b>Liabilities, Capital, and Surplus</b>			
Claims unpaid	\$11,018,000		\$11,018,000
Unpaid claims adjustment expenses	297,000		297,000
Premiums received in advance	233,193		233,193
General expenses due or accrued	1,491,847		1,491,847
Aggregate write-ins for other liabilities:			
Assessments payable	625,495		625,495
<b>Total Liabilities</b>	<u><u>13,665,535</u></u>	<u><u>0</u></u>	<u><u>13,665,535</u></u>
Unassigned funds (surplus)	1,277,312		1,277,312
<b>Total Capital and Surplus</b>	<u><u>1,277,312</u></u>	<u><u>0</u></u>	<u><u>1,277,312</u></u>
<b>Total Liabilities, Capital and Surplus</b>	<u><u>\$14,942,847</u></u>	<u><u>\$0</u></u>	<u><u>\$14,942,847</u></u>

**WASHINGTON STATE HEALTH INSURANCE POOL**  
**STATEMENT OF REVENUE AND EXPENSES**  
**December 31, 2007**

	<u>BALANCE PER COMPANY</u>	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE PER EXAMINATION</u>
Net premium income	<u>\$18,617,550</u>	<u>\$0</u>	<u>\$18,617,550</u>
Total revenues	<u>18,617,550</u>	<u>0</u>	<u>18,617,550</u>
<b>Less:</b>			
Hospital and medical	57,357,281	0	57,357,281
Claims adjustment expenses	1,040,141		1,040,141
General administrative expenses	<u>2,526,245</u>		<u>2,526,245</u>
Total underwriting deductions	<u>60,923,667</u>	<u>0</u>	<u>60,923,667</u>
Net underwriting gain or (loss)	<u>(42,306,117)</u>	<u>0</u>	<u>(42,306,117)</u>
Net investment income earned	<u>456,626</u>		<u>456,626</u>
Net investment gains or (losses)	<u>456,626</u>	<u>0</u>	<u>456,626</u>
Aggregate write-ins for other income or expenses			0
Excess loss ratio receipts	<u>47,253</u>		<u>47,253</u>
<b>Net Income (Loss)</b>	<u><b>(\$41,802,238)</b></u>	<u><b>\$0</b></u>	<u><b>(\$41,802,238)</b></u>
<b><u>CAPITAL AND SURPLUS ACCOUNT</u></b>			
Capital and surplus prior reporting period	<u>\$5,210,841</u>	<u>\$0</u>	<u>\$5,210,841</u>
Net Income (Loss) from above	<u>(41,802,238)</u>	<u>0</u>	<u>(41,802,238)</u>
Aggregate write-ins for gains or (losses) in surplus			
Assessments levied	<u>37,868,709</u>		<u>37,868,709</u>
Net change in capital and surplus	<u>(3,933,529)</u>	<u>0</u>	<u>(3,933,529)</u>
<b>Capital and surplus end of reporting period</b>	<u><b>\$1,277,312</b></u>	<u><b>\$0</b></u>	<u><b>\$1,277,312</b></u>

**SURPLUS RECONCILIATION  
FOR THE PERIODS ENDING**

	<u>12/31/2007</u>	<u>12/31/2006</u>	<u>12/31/2005</u>	<u>12/31/2004</u>	<u>12/31/2003</u>
<b>Capital and surplus, prior reporting year</b>	<u>\$5,210,841</u>	<u>(\$2,485,270)</u>	<u>(\$4,685,328)</u>	<u>\$6,808,661</u>	<u>\$11,106,453</u>
Net income or (loss)	(41,802,238)	(24,041,044)	(35,477,804)	(39,408,060)	(24,340,959)
Aggregate write-ins for gains or (losses) in surplus:					
Assessments levied	37,868,709	31,737,155	37,677,862	27,914,071	18,732,850
Correction of prior years error					1,310,317
Net change in capital and surplus	<u>(3,933,529)</u>	<u>7,696,111</u>	<u>2,200,058</u>	<u>(11,493,989)</u>	<u>(4,297,792)</u>
<b>Capital and surplus, end of reporting period</b>	<u><b>\$1,277,312</b></u>	<u><b>\$5,210,841</b></u>	<u><b>(\$2,485,270)</b></u>	<u><b>(\$4,685,328)</b></u>	<u><b>\$6,808,661</b></u>

**NOTES TO THE FINANCIAL STATEMENTS**

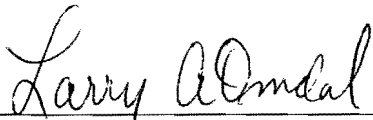
WSHIP has no special consents, permitted practices or orders from the state of Washington. There were no examination report adjustments.

## ACKNOWLEDGMENT

Acknowledgment is hereby made of the cooperation extended to the examiners by the officers of Washington State Health Insurance Pool during the course of this examination.

In addition to the undersigned, Michael V. Jordan, CPA, CFE, MHP, Assistant Chief Examiner; Carl M. Baker, CPA, CFE, CISA, Health Field Supervisor; John R. Jacobson, AFE, CISA, AES, Automated Examination Specialist; Shiraz Jetha, FSA, FCIA, MAAA, Health Actuary; Friday P. Enoye, Financial Examiner; all from the Washington State Office of the Insurance Commissioner participated in the examination and the preparation of this report.

Respectfully submitted,



---

Larry A. Omdal, Examiner in Charge  
State of Washington

**AFFIDAVIT**

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

Larry A. Omdal, 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 Washington State Health Insurance Pool 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).

*Larry A Omdal*  
Larry A. Omdal, Examiner in Charge  
State of Washington

Subscribed and sworn to before me this 30<sup>th</sup> day of December, 2008.

*Colleen Jansen*  
Notary Public in and for the  
State of Washington

