



STATE OF MINNESOTA
DEPARTMENT OF COMMERCE
SAINT PAUL, MINNESOTA

REPORT OF EXAMINATION
OF
PRIMEWEST HEALTH SYSTEM
ALEXANDRIA, MINNESOTA
AS OF
DECEMBER 31, 2006



Protecting, maintaining and improving the health of all Minnesotans

The attached report of examination made of the condition and affairs as of December 31, 2006 of:

PRIMEWEST HEALTH SYSTEM
Alexandria, Minnesota

was recently completed by duly qualified examiners of the State of Minnesota.

Due consideration has been given to the comments of the examiners regarding the operations of Primewest Health System and its financial condition, as reflected in this report. This report is hereby, as of this date, approved, adopted, filed and made an official record of this Department.

A handwritten signature in cursive script, appearing to read "Sanne Magnan", is written over a horizontal line.

Sanne Magnan, M.D., Ph.D.
Commissioner of Health

Dated: 3/11/08

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Protecting, maintaining and improving the health of all Minnesotans

January 31, 2008

The Honorable Dr. Sanne Magnan
Commissioner of Health
State of Minnesota
Department of Health
85 7th Place East
St. Paul, Minnesota 55101

Honorable Glenn Wilson
Commissioner of Commerce
State of Minnesota
85 7th Place East, Suite 500
St. Paul, Minnesota 55101-2198

Dear Honorable Commissioners:

Pursuant to your instructions and the statutory requirements of the State of Minnesota, a comprehensive examination has been made of the books, records, business affairs and financial condition of

**PRIMEWEST HEALTH SYSTEM
2209 Jefferson Street, Suite 101
Alexandria, Minnesota 56308**

The following examination report is respectfully submitted.

SCOPE OF EXAMINATION

The examination was a comprehensive examination, conducted by the Minnesota Department of Commerce, observing the applicable guidelines and procedures in the *NAIC Financial Condition Examiners' Handbook*. The Department of Commerce Examination Order #07-006 directed that the examination include a determination of the financial condition of PrimeWest Health System (hereinafter referred to as the Company) and a general review of its corporate affairs and insurance operations to determine compliance with statutes.

The examination covered the three-year period from January 1, 2004 through December 31, 2006. In accordance with the *NAIC Financial Condition Examiners' Handbook*, the examination included significant transactions and/or events occurring subsequent to December 31, 2006 that were noted during the course of this examination.

The prior examination, conducted by the Minnesota Department of Commerce as of December 31, 2003, had no report findings.

FINDINGS, RECOMMENDATIONS AND INSTRUCTIONS

<u>Finding #</u>	<u>Page #</u>	
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1	6	<u>Finding:</u>
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The Company's fidelity coverage limits are less than the NAIC's suggested guidelines for minimum coverage.

The Company uses certain administrators who have access to the cash accounts of the Company but do not provide the Company with annual evidence of fiduciary coverage.

Recommendation:

It is recommended that the Company increase its fidelity coverage to a level that at least meets the NAIC's minimum suggested guidelines.

It is recommended that the Company obtain, from its administrators, annual evidence of adequate fidelity coverage which names the Company as the insured beneficiary.

Management Response:

For claims incurred in 2008 and going forward, Midwest Dental Benefits (MDB) is the only third-party administrator (TPA) that draws checks against PrimeWest accounts. Metropolitan Health Plan's (MHP) role as a TPA is phasing out in connection with the transition of medical claims in-house, and applies only to run-out claims with dates of service before 2008. Prime Therapeutics does not draw checks on PrimeWest accounts, and instead used their own accounts funded through weekly wire transfers from PrimeWest

based on documented aggregate claim volumes.

PrimeWest will obtain from MDB evidence of fidelity coverage which names PrimeWest as the insured beneficiary. Based on the volume of annual dental claims, we estimate that fidelity bond coverage consistent with NAIC guidelines will be in the \$75,000 to \$100,000 range. It should be noted that dental providers are contracted with directly by PrimeWest, rather than MDB. In addition to fidelity bond coverage, all claims paid by MDB, MHP, and PrimeWest directly are subject to a variety of controls to ensure the integrity of payments, including “positive pay” banking files, vendor set-up controls, claims delegation oversight activities, and annual audit reviews.

PrimeWest also contracts with Cirdan Health Systems, Inc. (Cirdan) to administer accounting, banking, and other financial management functions. Under this contract, Cirdan functions as PrimeWest’s Financial and Data Management Department, including the Chief Financial Officer role. PrimeWest will review whether its own fidelity bond coverage includes Cirdan in its activities on behalf of PrimeWest. If not, PrimeWest will obtain from Cirdan evidence of fidelity coverage which names PrimeWest as the insured beneficiary.

2 8 Finding: Reinsurance

The Company and the reinsurer employ reinsurance intermediaries to perform certain services related to the terms of the treaty including but not limited to the handling of reinsurance payments on behalf of the Company. The intermediaries are not named in the reinsurance treaty to perform these duties, as the agent for the Company. The Company is not secured against loss of funds flowing through the intermediary.

Also, the reinsurance treaty is executed by the reinsurer’s intermediary on behalf of the reinsurer.

Instruction:

The Company is instructed to have the treaty amended to include reference to the activities of any reinsurance intermediaries, as they pertain to the execution of the terms of the agreement. Additionally, the Company is instructed to obtain either from the reinsurer contractual guarantees or from the reinsurance intermediaries insured/secured guarantees to cover the Company’s funds that flow through the intermediaries.

Also, the Company is instructed to obtain from an authorized officer of the reinsurer written verification that its intermediary has authority to execute this reinsurance agreement on behalf of the reinsurer.

Management Response:

PrimeWest contracts with Standard Security Life Insurance Company of New York (SSLIC) for reinsurance coverage. Under the terms of the reinsurance treaty, SSLIC names IndependenceCare Underwriting Services –

Minneapolis, LLC (IndependenceCare) in their underwriting capacity. The treaty also states that premiums shall be payable to SSLIC at "the office of its choice." SSLIC has communicated to PrimeWest that IndependenceCare is SSLIC's office of choice for premium payment purposes, and provided a premium payment form to PrimeWest designating IndependenceCare for this purpose.

PrimeWest will seek an amendment to the reinsurance treaty that specifically designates IndependenceCare as SSLIC's designated agent for premium collection purposes, and any other roles under the treaty delegated to IndependenceCare by SSLIC. The amendment will also provide a contractual guarantee to cover the PrimeWest's funds that flow through IndependenceCare. PrimeWest will also seek from an authorized officer of SSLIC written verification that IndependenceCare has authority to execute this reinsurance agreement on behalf of SSLIC.

HISTORY

The County Boards of Commissioners of Big Stone, Douglas, Grant, McLeod, Meeker, Pipestone, Pope, Renville, Stevens and Traverse Counties (hereinafter referred to as Member Counties) executed a Joint Powers Agreement, during December 1998, whereby, under authority granted by Minnesota Statute Section 471.59, they agreed to establish a Joint Powers board of directors to organize, govern, plan and administer a multi-county county based purchasing program for Medical Assistance and General Assistance Medical Care services as authorized by Minnesota Statute Section 256B.692. Effective during 2007, the Counties of Beltrami, Clearwater and Hubbard were added as new members of the Company. Services in these Counties commenced in 2008.

The legal name of the Joint Powers program was determined to be "Prime West Central County Based Purchasing Initiative". A board consisting of one County Commissioner from each member county governs the program.

The Minnesota Department of Health, by letter dated October 7, 2002, found that the Company met the requirements for a county-based purchasing arrangement. Effective July 1, 2003, the Company began coverage for enrollees under Medicaid and General Assistance Medical Care in the Member Counties. Effective during 2005, the Company began issuing coverage to enrollees in MinnesotaCare and certain additional Medicare and Medicaid programs provided through the Centers for Medicare and Medicaid Services.

SUBSEQUENT EVENTS

The Company began conversion of all medical claims processing functions from its third-party administrator to in-house operations. In-house processing began during the first quarter of 2008.

The Company purchased and moved into new home office facilities in April 2007. The net cost to the Company, after exchange credit for the old home office building, was approximately \$1,800,000. This amount was fully paid during 2007.

The Company added three new counties, Beltrami, Hubbard and Clearwater, to the Joint Powers Agreement servicing area effective October 2007.

A branch service office was opened in Pipestone in 2007 and the Company is reviewing the possibility of purchasing office facilities for another branch service office in the Bemidji area during the first quarter 2008.

MANAGEMENT

Joint Powers Board of Directors

The Company is governed by the Joint Powers Board of Directors which is made up of one County Commissioner from each of the Member Counties. Terms of the Board members are one year with eligibility for re-appointment. The Board also includes the Company's Chief Executive Officer and Medical Director as non-voting members. Board meetings are held monthly.

The Joint Powers Board of Directors consisted of the following ten individuals at December 31, 2006:*

<u>Commissioner</u>	<u>County</u>
Brent C. Olson	Big Stone
David R. Naatz	Traverse
Larry J. Sayre	Stevens
Gale A. Dahlager	Renville
Larry D. Kittelson	Pope
Marvin J. Tinklenberg	Pipestone
Amy P. Wilde	Meeker
Beverly J. Wangerin	McLeod
Paul C. Anderson	Douglas
Ronald F. Woltjer	Grant

*Effective during 2007, the Joint Powers Board of Directors was expanded to thirteen members with the addition of three new Counties into the Company.

Program Officers

The following individuals served as principal officers of the Company at December 31, 2006:

<u>Name</u>	<u>Position</u>
Robert E. McCrory	Chairperson - Joint Powers Board
Marvin J. Tinklenberg	Vice Chairperson – Joint Powers Board
Richard S. Kastner	Treasurer
Paul C. Anderson	Secretary
James A. Przybilla	Chief Executive Officer
John D. Klein	Chief Financial Officer

Conflict of Interest

The Company Board of Commissioners and staff complete conflict of interest statements annually. The executed statements for the years under examination were reviewed with no material conflicts noted.

Corporate Records

The Company amended its Joint Powers Agreement in May 2005 to allow the Company to buy, own and sell property.

The Company's Bylaws were amended effective October 4, 2007 to allow for Company officers to execute contracts with Federal and State agencies when Director signatures are necessary.

The Company's Board minutes were reviewed and found to be in order.

AFFILIATED ENTITIES AND TRANSACTIONS

The initial ten member counties executed agreements that guarantee the required statutory surplus of the Company. Effective with the entrance of the three new member counties into the Joint Powers administration, the new member counties also executed agreements to guarantee the surplus of the Company.

The Joint Powers Agreement entered into during December 1998 required all member counties to make a start up loan to the Company no later than January 31, 1999. The size of each member's loan was based on each member county's total eligible insured member months for calendar year 1997.

The total loan principal of \$500,000 plus accrued interest compounded annually at a rate of 5% was payable on or before June 30, 2006. The Company repaid the loan principal of \$500,000 plus accrued interest of \$171,875 during 2006.

FIDELITY BOND AND OTHER COMPANY INSURANCE

The Company's fidelity coverage limits are less than the NAIC's suggested guidelines for minimum coverage. It is recommended that the Company increase its fidelity coverage to a level that at least meets the NAIC's minimum suggested guidelines.

The Company uses certain administrators who have access to the cash accounts of the Company but do not provide the Company with annual evidence of fiduciary coverage. It is recommended that the Company obtain, from its administrators, annual evidence of adequate fidelity coverage which names the Company as the insured beneficiary.

The Company maintains corporate insurance coverages at levels, which management believes are sufficient to cover risks in the normal course of business.

EMPLOYEE WELFARE

Company employees are provided a traditional employee benefit package including pension coverage through the Public Employees Retirement Association. The Company is in process of developing a performance based bonus program for all eligible employees.

The Company has executed an employment contract with the Chief Executive Officer, effective January 1, 2007. Provisions of the contract include guaranteed minimum salary level, company payment of specified health, life and disability benefits and severance benefit provisions.

STATUTORY DEPOSITS

The Company, as a county based purchasing program, must meet the financial solvency requirements of either Minnesota Statute Section 62D.041 or 62N.28. In lieu of the net worth and deposit requirements of these Statutes, the Department of Health has allowed guaranteeing entities to fund this deposit. The Member Counties have agreed by resolution to serve as the guaranteeing organizations for the Company's required deposit.

TERRITORY AND PLAN OF OPERATIONS

The Company contracts with the Minnesota Department of Human Services (DHS) and the Center for Medicare and Medicaid Services (CMS) to provide health care services to qualified enrollees in certain DHS and CMS programs. These coverages are provided to qualified residents of the member counties.

Coverage plans available through the Company include:

- Prepaid Medical Assistance Program (PMAP) – this program provides certain family and child health care coverage to those eligible enrollees under the age of 65. (Effective July 2003)

- General Assistance Medical Care (GAMC) – this program provides certain health care coverage to adults under the age of 65. (Effective July 2003)
- MinnesotaCare (MNCare) – this program provides certain health care coverage to any eligible Minnesota resident under the age of 65. (Effective January 2005)
- Minnesota Senior Care Plus (MSC+) - this program provides PMAP type coverage to eligible enrollees age 65 and over. (Effective June 2005)
- Minnesota Senior Health Option (MSHO) – this is a dual Medicare/Medicaid eligible program, on a voluntary basis, which includes Medicare Part D coverage. (Effective August 2005)
- Special Needs BasicCare – this program is designed to meet the health care needs of eligible enrollees who are disabled and qualify for Medicare. The program is voluntary and includes Medicare Part D coverage. (Effective January 2008)

The Company receives monthly capitation payments from DHS and CMS for all enrollees.

The Company staff administers the program and contracts with third-party administrators to process and pay claims. (The Company began processing medical claims in its offices effective January 2008).

The Company does not market its products through traditional insurance sales channels. Coverage is available to enrollees only through that person's eligibility for one of the aforementioned public programs, within the stated geographical regions. The Company has no appointed agents, except as required by law, or agency contracts and has no liability for commissions.

REINSURANCE

The Company cedes eligible hospital and physician services, on an excess basis to a reinsurer authorized in the State of Minnesota. Reinsurance coverage is on a co-insurance basis after application of a per-member per year deductible of \$100,000. The maximum reinsurance coverage payable per member per year is \$1,000,000 and per lifetime is \$2,000,000. The reinsurance contract effectively passes risk.

The Company and the reinsurer employ reinsurance intermediaries to perform certain services related to the terms of the treaty including but not limited to the handling of reinsurance payments on behalf of the Company. The intermediaries are not named in the reinsurance treaty to perform these duties, as the agent for the Company. The Company is not secured against loss of funds flowing through the intermediary.

Also, the reinsurance treaty is executed by the reinsurer's intermediary on behalf of the reinsurer.

The Company is instructed to have the treaty amended to include reference to the activities of any reinsurance intermediaries, as they pertain to the execution of the terms of the agreement. Additionally, the Company is instructed to obtain either from the reinsurer contractual

guarantees or from the reinsurance intermediaries insured/secured guarantees to cover the Company's funds that flow through the intermediaries.

Also, the Company is instructed to obtain from an authorized officer of the reinsurer written verification that its intermediary has authority to execute this reinsurance agreement on behalf of the reinsurer.

ACCOUNTS AND RECORDS

Financial Reporting

The Company contracted with an independent consulting firm to produce its quarterly and annual regulatory financial reporting statements and it used an independent actuarial services firm to attest to its reported loss and LAE reserves.

Third-Party Administrators

The Company employed third-party administrators, during the years 2004-2006, for medical, dental and pharmacy claims processing and related functions. An outside service was also used to administer the accounting and reporting systems. Delegation agreements were executed where required by Minnesota Rules Part 4685.1110, Subpart 6.

Independent Certified Public Accountant

The Company was audited annually, for the years 2004 through 2006, by the accounting firm of Larson, Allen, Weishair & Co., LLP. The Company received an unqualified opinion in all three years. Certain audit work papers of the accounting firm were reviewed and relied upon in conjunction with this examination.

FINANCIAL STATEMENTS

Following are the Company's statutory statements of admitted assets, liabilities and capital and surplus for the calendar years ending 2004 through 2006. Comparative statements of operations, reconciliation of surplus and cash flow for those years follow the statements. No adjustments have been made to the reported financial statements of the Company as a result of this examination.

PRIMEWEST HEALTH SYSTEM
STATEMENT OF ASSETS, LIABILITIES AND SURPLUS
AS OF DECEMBER 31,

<u>ASSETS</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Real estate – occupied	\$ 1,385,332	\$ 814,974	\$ 0
Cash and short-term investments	34,691,503	21,114,764	13,276,064
Subtotals, Cash and Invested Assets	36,076,835	21,929,738	13,276,064
Uncollected premiums	3,081,940	3,535,414	1,012,348
Recoverable from reinsurers	223,129	486,729	0
Furniture and equipment	59,485	49,860	64,765
Health care receivable	224,948	379,687	421,916
Total Assets	<u>\$ 39,666,337</u>	<u>\$ 26,381,428</u>	<u>\$ 14,775,092</u>
<u>LIABILITIES</u>			
Claims unpaid	\$ 18,339,432	\$ 11,753,703	\$ 6,569,619
Unpaid claims adjustment expenses	50,000	50,000	50,000
Advance premiums	4,424,267	3,769,626	3,421,641
General expenses due or accrued	1,433,695	862,134	334,092
Amounts withheld for others	153,001	0	0
Borrowed money	0	671,875	646,875
Aggregate liability write-ins	1,264,211	0	0
Total Liabilities	25,664,606	17,107,338	11,022,227
Unassigned funds (surplus)	14,001,731	9,274,090	3,752,865
Total Surplus	14,001,731	9,274,090	3,752,865
Total Liabilities and Surplus	<u>\$ 39,666,337</u>	<u>\$ 26,381,428</u>	<u>\$ 14,775,092</u>

**PRIMEWEST HEALTH SYSTEM
STATEMENT OF REVENUE AND EXPENSES
FOR PERIOD ENDING DECEMBER 31,**

	<u>2006</u>	<u>2005</u>	<u>2004</u>
Net premium income	\$ 82,530,075	\$ 54,484,104	\$ 36,943,409
Aggregate write-ins for other revenues	15,158	140,205	340,262
Total Revenues	<u>82,545,233</u>	<u>54,624,309</u>	<u>37,283,671</u>
Hospital/medical benefits	50,481,694	28,578,201	16,327,596
Other professional services	10,717,810	3,652,517	2,356,991
Emergency room and out-of-area	1,150,441	612,254	565,664
Prescription drugs	8,129,607	10,910,432	9,935,195
Aggregate write-ins medical & hospital	1,837,818	1,310,190	970,786
Less: Net reinsurance recoveries	459,689	486,729	0
Total Medical and Hospital	<u>71,857,681</u>	<u>44,576,865</u>	<u>30,156,232</u>
General administrative expenses	7,226,588	4,961,106	3,650,027
Total Underwriting Deductions	<u>79,084,269</u>	<u>49,537,971</u>	<u>33,806,259</u>
Net underwriting gain or (loss)	3,460,964	5,086,338	3,477,412
Net investment income earned	1,399,787	496,142	141,972
Aggregate write-ins for other expenses	(46,053)	(25,000)	(25,000)
Net Income	<u><u>\$ 4,814,698</u></u>	<u><u>\$ 5,557,480</u></u>	<u><u>\$ 3,594,384</u></u>
 <u>SURPLUS ACCOUNT</u>			
Surplus, prior reporting year	\$ 9,274,090	\$ 3,752,865	\$ 155,551
Net income	4,814,698	5,557,480	3,594,384
Change in non-admitted assets	(87,057)	(36,255)	2,929
Net change in surplus	<u>4,727,641</u>	<u>5,521,225</u>	<u>3,597,313</u>
Surplus End of Reporting Year	<u><u>\$ 14,001,731</u></u>	<u><u>\$ 9,274,090</u></u>	<u><u>\$ 3,752,864</u></u>

**PRIMEWEST HEALTH SYSTEM
STATEMENT OF CASH FLOWS
FOR PERIOD ENDED DECEMBER 31,**

<u>Cash from Operations</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>
Premiums collected	\$ 83,638,190	\$ 52,309,023	\$ 36,805,057
Net investment income	1,399,787	496,142	141,972
Miscellaneous income	15,158	140,205	350,546
Total income from operations	85,053,135	52,945,370	37,297,575
Benefit and loss payments	65,008,352	39,879,510	28,497,944
General administrative expenses	7,272,641	4,986,106	3,801,428
Total expenses from operations	72,280,993	44,865,616	32,299,372
Net cash from operations	\$ 12,772,142	\$ 8,079,754	\$ 4,998,203
<u>Cash from Investments</u>			
Miscellaneous proceeds	\$ 45,056	\$ 0	\$ 0
Real estate acquired	615,414	814,974	0
Net cash from investments	(\$ 570,358)	(\$ 814,974)	\$ 0
<u>Cash from Financing</u>			
Borrowed funds provided (applied)	(\$ 671,875)	\$ 25,000	\$25,000
Other cash provided (applied)	2,046,830	548,920	52,582
Net cash from financing	\$ 1,374,955	\$ 573,920	\$ 77,582
<u>Reconciliation of Cash & ST Investments</u>			
Net change in cash and ST investments	\$ 13,576,739	\$ 7,838,700	\$ 5,075,785
Cash and short-term investments			
Beginning of year	21,114,764	13,276,064	8,200,279
End of period	\$ 34,691,503	\$ 21,114,764	\$ 13,276,064

EXAMINATION NOTES TO FINANCIAL STATEMENTS

Reserves for Losses and Loss Adjustment Expenses

Reserve projections developed by the Company as of December 31, 2006 were accepted based on the examiners' review of underlying data and reserving methods. No exceptions were noted.

During the review of the underlying data used in the projections, the examiners performed procedures prescribed in the NAIC Financial Condition Examiners Handbook and other procedures as determined necessary by the Department actuary, to provide adequate validation of reserves. As a result, the Loss and Loss Adjustment Expense reserves appear to be reasonably stated and have been accepted for the purposes of this report.

Information provided to the examiners was further reviewed for consistency with the Annual Statement and compliance with related laws and regulations of the State of Minnesota.

Taxation

The Company, as a government program, is subject neither to federal or state income taxation nor to state premium taxation.

Expansion of Operations

The addition of new coverage plans, beginning in 2005, was the principal cause of materially increased financial operating results, surplus and certain balance sheet assets and liabilities during the period under examination.

Net Worth

The Company met the net worth requirements of Minnesota Statute 62N.28 at December 31, 2006.

CONCLUSION

Acknowledgement is hereby made of the courtesy and cooperation extended by the personnel of PrimeWest Health System during the course of this examination.

Participating in the examination were M. James Carr, Daniel Vogelgesang and John Mutyaba of the Minnesota Department of Commerce.