

Report on Examination
of
Leon Medical Centers
Health Plans, Inc.

Miami, Florida

as of

December 31, 2005

By The
State of Florida
Office of Insurance Regulation

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Tallahassee, Florida

June 25, 2007

Kevin M. McCarty, Commissioner
Florida Office of Insurance Regulation
200 East Gaines Street
Tallahassee, Florida 32399-0326

Dear Sir:

Pursuant to your instructions, in compliance with Section 641.27, Florida Statutes (F.S.), and in accordance with the practices and procedures promulgated by the National Association of Insurance Commissioners (NAIC), we have conducted an examination as of December 31, 2005, of the financial condition and corporate affairs of:

Leon Medical Centers Health Plans, Inc.
11501 SW 40th Street
Miami, Florida 33165

hereinafter referred to as the "Company." Such report of examination is herewith respectfully submitted.

SCOPE OF EXAMINATION

This examination covered the period of October 17, 2002 through December 31, 2005. This was the first financial condition examination of the Company conducted by the Florida Office of Insurance Regulation (the "Office").

Planning for the current examination began on February 5, 2007. The fieldwork commenced on February 12, 2007 and concluded on April 10, 2007. The examination included any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

This was a statutory financial condition examination conducted in accordance with the NAIC *Financial Examiners Handbook, Accounting Practices and Procedures Manual, and Annual Statement Instructions*, with due regard to the requirements of the insurance laws and rules of the State of Florida.

In this examination, emphasis was directed to the quality, value, and integrity of the statement assets and the determination of liabilities, as they affect the Company's solvency.

The examination included a review of corporate and other selected records deemed pertinent to the Company's operations and practices. In addition, various ratio results, the Company's independent audit reports, and certain work papers prepared by the Company's independent certified public accountant (CPA) were reviewed and utilized where applicable within the scope of this examination.

We valued and/or verified the Company's assets and liabilities as reported by the Company in its 2005 annual statement. Transactions subsequent to December 31, 2005 were reviewed where relevant and deemed significant to the Company's financial condition.

This report of examination is confined to financial statements and comments on matters that involve departures from laws, regulations or rules, or which require special explanation or description.

After considering the Company's control environment and the materiality level set for this examination, we relied on work performed by the Company's CPA for the following accounts:

- Investment income due and accrued
- Uncollected premiums
- Commitments and contingent liabilities
- General expenses due or accrued

HISTORY

GENERAL

The Company was incorporated in Florida on June 12, 2001 and licensed by the Office as a health maintenance organization (HMO) on October 17, 2002. It commenced business on May 1, 2005.

As of the date of this examination, the Company was authorized to transact business as an HMO in accordance with Part I of Chapter 641, F.S.

Neither the Company's articles of incorporation nor its bylaws were amended during the period covered by this examination.

CAPITAL STOCK

As of December 31, 2005, the Company's capitalization was as follows:

| | |
|--|--------|
| Number of authorized common capital shares | 1,000 |
| Number of shares issued and outstanding | 250 |
| Total common capital stock | \$2.50 |
| Par value per share | \$0.01 |

At December 31, 2005, the Company was wholly-owned and controlled by Benjamin Leon, Jr. An abbreviated organizational chart appears on page 7.

PROFITABILITY

For the period of this examination, the Company reported the following:

| | <u>2005</u> | <u>2004</u> | <u>2003</u> |
|-------------------------|-------------|-------------|-------------|
| Year-end enrollment | 19,465 | 0 | 0 |
| In millions: | | | |
| Net premium income | \$97.6 | \$0.0 | \$0.0 |
| Total revenues | \$97.6 | \$0.0 | \$0.0 |
| Net loss | \$4.5 | \$0.4 | \$0.0 |
| Total capital & surplus | \$1.7 | \$1.9 | \$1.9 |

DIVIDENDS

The Company did not pay any shareholder dividends during the period of this examination.

MANAGEMENT

The annual shareholder meeting for the election of directors was held in accordance with Section 607.0701, F.S. Directors serving as of December 31, 2005 were:

Directors

| Name and Location | Principal Occupation |
|--------------------------------------|--|
| Stuart Eiseman Miami, Florida | Chief Operating Officer of the Company |
| Benjamin Leon, Jr. Miami, Florida | Chief Executive Officer of the Company |
| Benjamin Leon, III Miami, Florida | Vice President of Marketing of the Company |
| Lourdes Leon Miami, Florida | Treasurer of the Company |
| Albert R. Maury Miami, Florida | Chief Financial Officer of the Company |

At December 31, 2005, members of the Board of Directors Executive Committee were:

Executive Committee

Stuart Eiseman
Benjamin Leon, Jr.
Benjamin Leon, III
Lourdes Leon
Albert R. Maury

The following were the Company's senior officers as of December 31, 2005, as appointed by its board of directors in accordance with the Company's bylaws:

| Senior Officers | |
|------------------------|---------------------------------------|
| Name | Title |
| Benjamin Leon, Jr. | President and Chief Executive Officer |
| Stuart Eiseman | Chief Operating Officer |
| Albert R. Maury | Chief Financial Officer |
| Benjamin Leon, III | Vice President of Marketing |
| Lourdes Leon | Treasurer |

CONFLICT OF INTEREST PROCEDURE

The Company adopted a policy statement requiring annual disclosure of conflicts of interest in accordance with Section 607.0832, F.S. No exceptions were noted during this examination.

CORPORATE RECORDS

The recorded minutes of the shareholder, Board of Directors, Executive Committee, and Quality Improvement Committee meetings were reviewed for the period examined. The recorded minutes of the Board adequately documented its meetings and approval of Company transactions in accordance with Section 607.1601, F.S., including the authorization of investments as required by Section 641.35(7), F.S.

AFFILIATED COMPANIES

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), Florida Administrative Code (F.A.C.). However, the Company had not filed a holding company registration statement with the State of Florida as required by Section 628.801, F.S., and Rule 69O-143.046, F.A.C.

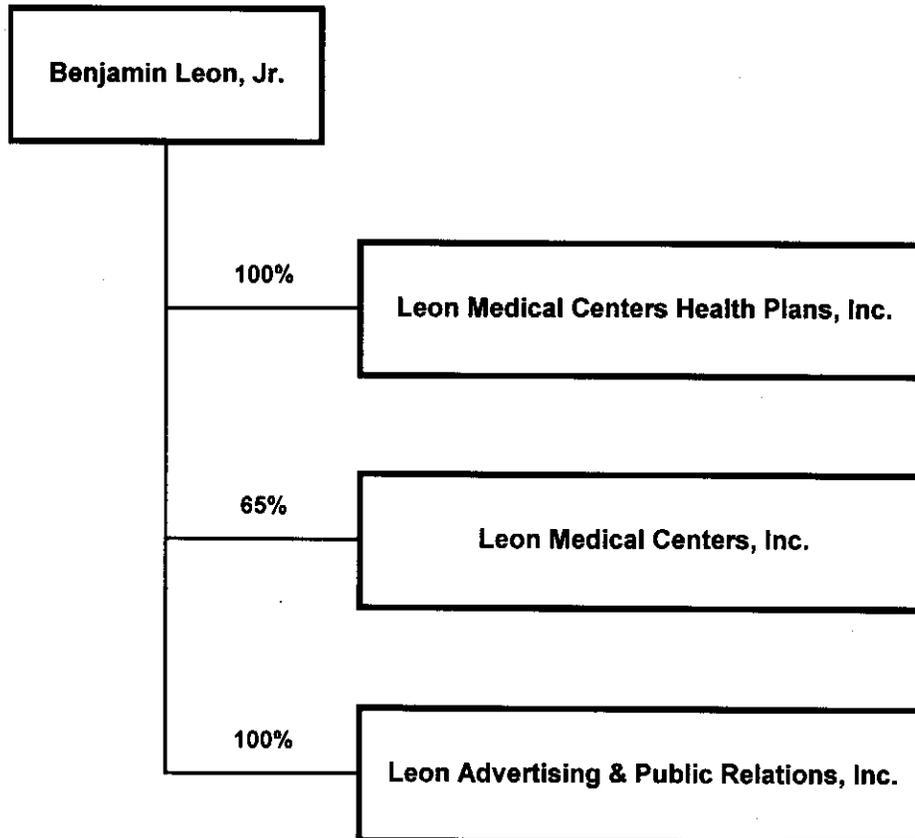
The following agreement was in force between the Company and an affiliate:

PROVIDER AGREEMENT

Leon Medical Centers, Inc. provided health care services to the Company's members pursuant to a September 15, 2004 provider agreement on a per member per month capitation basis in return for fees which amounted to \$39.0 million in 2005.

An abbreviated organizational chart as of December 31, 2005 reflecting the holding company system is shown below.

**Leon Medical Centers Health Plans, Inc.
Organizational Chart
December 31, 2005**



FIDELITY BOND AND OTHER INSURANCE

The Company maintained acceptable levels of general liability insurance as required by Rule 69O-191.069, F.A.C., and maintained a blanket fidelity bond in the amount of \$100,000, as required by Section 641.22, F.S. As a staff model HMO, the Company maintained adequate medical malpractice insurance for the Company as well as the physicians it employed, as required by Rule 69O-191.069, F.A.C.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

The Company offered to eligible employees participation in a 401(k) retirement plan.

STATUTORY DEPOSITS

The Company maintained on deposit with the Office an insolvency protection deposit of \$300,000 in accordance with Section 641.285, F.S., and a Rehabilitation Administrative Expense Fund deposit of \$10,000 in accordance with Section 641.227, F.S.

INSURANCE PRODUCTS AND RELATED PRACTICES

TERRITORY AND PLAN OF OPERATION

At December 31, 2005, the Company was authorized to transact business in Florida as an HMO in accordance with Part I of Chapter 641, F.S. It held a current health care provider certificate issued by the Florida Agency for Health Care Administration pursuant to Part III of Chapter 641, F.S., which was valid until September 22, 2006.

The Company employed internal agents and operated as a staff model HMO. It provided health care services solely to Medicare members. Its total membership at December 31, 2005 was 19,465.

The Company operated solely in Miami-Dade County, Florida.

TREATMENT OF MEMBERS

The Company established procedures for handling written complaints in accordance with Section 641.511, F.S., and maintained a claims procedure manual that included detailed procedures for handling each type of claim.

REINSURANCE

The Company maintained an excess loss reinsurance policy with Zurich American Insurance Company. The policy covered 90% of the Company's eligible expenses in excess of an annual deductible of \$150,000 per member per agreement year, up to a maximum of \$1 million per individual, except for certain organ and tissue transplants which were reimbursable at 50% with the same deductible and maximum. The maximum limit of liability was \$10 million per agreement year. The premium rate was \$10 per member per agreement month, subject to a minimum annual premium of \$250,000. The company was eligible for an experience refund if the agreement year premium exceeded \$500,000.

The reinsurance agreement reviewed was found to comply with NAIC standards with respect to the transfer of risk, and reporting and settlement information deadlines.

Rule 69O-144.010(3)(c)3, F.A.C., provides that reinsurance agreements shall contain provisions which provide that the reinsurance is payable by the reinsurer on the basis of the liability of the ceding insurer under the contract or contracts reinsured without diminution because of insolvency of the ceding insurer, and that payments by the reinsurer will be made directly to the ceding insurer or its receiver. The Company's reinsurance agreement did not contain these provisions, in violation of Rule 69O-144.010(3)(c)3, F.A.C.

The reinsurance contract was reviewed by the Company's appointed actuary and was utilized in determining the ultimate loss opinion.

ACCOUNTS AND RECORDS

An independent CPA audited the Company's statutory-basis financial statements annually for years 2003, 2004, and 2005, pursuant to Section 641.26(1)(c), F.S.

The Company's accounting records were maintained on a computerized system. Its balance sheet accounts were verified with the line items of its annual statement submitted to the Office.

The Company's main administrative office is located in Miami, Florida, where this examination was conducted.

The following agreements were in effect between the Company and non-affiliates:

SERVICE AGREEMENTS

Psychcare, LLC provided mental health and substance abuse benefits to the Company's members on a per member per month capitation basis pursuant to an agreement with the Company dated January 1, 2005, in return for total fees in 2005 of \$276,251.

RESTAT, LLC provided Medicare prescription drug benefit administration services to the Company's members pursuant to an agreement with the Company dated May 1, 2005, in return for total fees in 2005 of \$419,853.

PREFERRED CARE PARTNERS, INC. AGREEMENT

The Company paid to Preferred Care Partners, Inc. (PCP) a monthly fee of 8% of cash received from the Centers for Medicare & Medicaid Services (CMS) pursuant to an agreement with PCP dated April 21, 2005. The agreement provided for the Company to enroll Medicare members during the term of PCP's agreement with Leon Medical Centers, Inc. Fees related to this agreement amounted to \$10.2 million in 2005.

FINANCIAL STATEMENTS PER EXAMINATION

The following three pages contain statements of the Company's financial position at December 31, 2005, as determined by this examination, and the results of its operations for the year then ended as reported by the Company.

Leon Medical Centers Health Plans, Inc.
Assets
December 31, 2005

| Classification | Per Company | Examination Adjustments | Per Examination |
|--|----------------------------|----------------------------|----------------------------|
| Cash, cash equivalents, and short-term investments | \$34,667,206 | \$0 | \$34,667,206 |
| Investment income due and accrued | 37,798 | 0 | 37,798 |
| Uncollected premiums and agents' balances | 1,294,645 | 0 | 1,294,645 |
| Amounts recoverable from reinsurers | <u>101,303</u> | <u>0</u> | <u>101,303</u> |
| Totals | <u>\$36,100,952</u> | <u>\$0</u> | <u>\$36,100,952</u> |

Leon Medical Centers Health Plans, Inc.
Liabilities, Capital and Surplus
December 31, 2005

| Liabilities | Per Company | Examination Adjustments | Per Examination |
|--|------------------------|------------------------------------|----------------------------|
| Claims unpaid | \$28,859,249 | \$0 | \$28,859,249 |
| Unpaid claims adjustment expenses | 770,213 | 0 | 770,213 |
| General expenses due or accrued | 634,130 | 0 | 634,130 |
| Amounts due to parent, subsidiaries and affiliates | <u>4,096,185</u> | <u>0</u> | <u>4,096,185</u> |
| Total liabilities | <u>34,359,777</u> | <u>0</u> | <u>34,359,777</u> |
| Capital and Surplus | | | |
| Common capital stock | 3 | 0 | 3 |
| Gross paid in and contributed surplus | 6,933,756 | 0 | 6,933,756 |
| Unassigned funds | <u>(5,192,584)</u> | <u>0</u> | <u>(5,192,584)</u> |
| Total capital and surplus | <u>1,741,175</u> | <u>0</u> | <u>1,741,175</u> |
| Total liabilities, capital and surplus | <u>\$36,100,952</u> | <u>\$0</u> | <u>\$36,100,952</u> |

Leon Medical Centers Health Plans, Inc.

**Statement of Revenue and Expenses
For Year Ended December 31, 2005**

| | | |
|---------------------------------|------------------|-----------------------------|
| Net premium income | | \$97,571,679 |
| Hospital/medical benefits | \$66,406,182 | |
| Other professional services | 11,187,667 | |
| Outside referrals | 1,136,795 | |
| Emergency room and out-of-area | 544,783 | |
| Prescription drugs | 12,867,232 | |
| Net reinsurance recoveries | <u>(101,303)</u> | |
| | 92,041,356 | |
| Claims adjustment expenses | 4,092,986 | |
| General administrative expenses | <u>6,338,917</u> | |
| Total underwriting deductions | | <u>102,473,259</u> |
| Net underwriting gain or (loss) | | (4,901,580) |
| Net investment income earned | | <u>368,747</u> |
| Net income or (loss) | | <u><u>(\$4,532,833)</u></u> |

**Capital and Surplus Account
For Year Ended December 31, 2005**

| | |
|--|---------------------------|
| Capital and surplus, December 31, 2004 | \$1,903,438 |
| Net income or (loss) | (4,532,833) |
| Change in nonadmitted assets | (1,439,585) |
| Paid in surplus | <u>5,810,155</u> |
| | 1,741,175 |
| Examination adjustments | <u>0</u> |
| Capital and surplus, December 31, 2005 | <u><u>\$1,741,175</u></u> |

COMMENTS ON FINANCIAL STATEMENTS

Losses and Loss Adjustment Expenses **\$29,629,462**

The Company's appointed actuary rendered an opinion that the amounts carried in the Company's balance sheet as of December 31, 2005 reasonably provided for all unpaid loss and loss expense obligations of the Company under the terms of its policies and agreements. The Office actuary reviewed work papers provided by the Company and concurred with this opinion.

Based on the results of the Office actuary's review and analysis of work papers and data provided by the Company, we concluded that the aggregate liability was not materially misstated.

Surplus **\$1,741,175**

The \$1,741,175 reported by the Company as its total capital and surplus at December 31, 2005 was \$1,694,803 less than the Company's required minimum capital and surplus of \$3,435,978.

Consequently, the Company was in violation of Section 641.225, F.S.

Leon Medical Centers Health Plans, Inc.
Comparative Analysis of Changes in Capital & Surplus
December 31, 2005

The following is a reconciliation of capital and surplus between that reported by the Company and as determined by the examination.

| Capital & surplus, December 31, 2005 - per annual statement | | \$1,741,175 | | | | | | | | | | | | | | | | | | | | |
|--|--|---------------------|---|---------------------|---|--------|--------------|--------------|-----|-------------|--------------|--------------|------------|-----------------------------------|--|--|----------|--|--|--|----------------------------------|--|
| | <table style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 35%;"></th> <th style="width: 35%; text-align: center;"><u>Per Company</u></th> <th style="width: 35%; text-align: center;"><u>Per Exam</u></th> <th style="width: 35%; text-align: center;"><u>Increase (Decrease) In Capital & Surplus</u></th> </tr> </thead> <tbody> <tr> <td>Assets</td> <td style="text-align: right;">\$36,100,952</td> <td style="text-align: right;">\$36,100,952</td> <td style="text-align: right;">\$0</td> </tr> <tr> <td>Liabilities</td> <td style="text-align: right;">\$34,359,777</td> <td style="text-align: right;">\$34,359,777</td> <td style="text-align: right;"><u>\$0</u></td> </tr> <tr> <td>Net change in capital and surplus</td> <td></td> <td></td> <td style="text-align: right;"><u>0</u></td> </tr> <tr> <td>Capital & surplus, December 31, 2005 - per annual statement</td> <td></td> <td></td> <td style="text-align: right;"><u><u>\$1,741,175</u></u></td> </tr> </tbody> </table> | | <u>Per Company</u> | <u>Per Exam</u> | <u>Increase (Decrease) In Capital & Surplus</u> | Assets | \$36,100,952 | \$36,100,952 | \$0 | Liabilities | \$34,359,777 | \$34,359,777 | <u>\$0</u> | Net change in capital and surplus | | | <u>0</u> | Capital & surplus, December 31, 2005 - per annual statement | | | <u><u>\$1,741,175</u></u> | |
| | <u>Per Company</u> | <u>Per Exam</u> | <u>Increase (Decrease) In Capital & Surplus</u> | | | | | | | | | | | | | | | | | | | |
| Assets | \$36,100,952 | \$36,100,952 | \$0 | | | | | | | | | | | | | | | | | | | |
| Liabilities | \$34,359,777 | \$34,359,777 | <u>\$0</u> | | | | | | | | | | | | | | | | | | | |
| Net change in capital and surplus | | | <u>0</u> | | | | | | | | | | | | | | | | | | | |
| Capital & surplus, December 31, 2005 - per annual statement | | | <u><u>\$1,741,175</u></u> | | | | | | | | | | | | | | | | | | | |

SUBSEQUENT EVENTS

As reported on page 12, the Company paid to PCP a monthly fee of 8% of cash received from CMS pursuant to an agreement dated April 21, 2005. The agreement provided for the Company to enroll Medicare members during the term of PCP's agreement with Leon Medical Centers, Inc., and was scheduled to expire on December 31, 2006. On February 15, 2006, the Company entered into a Settlement and Termination Agreement with PCP and paid \$10 million for early termination of the agreement.

As reported on page 17, the amount reported by the Company as its total capital and surplus at December 31, 2005 was less than its required minimum capital and surplus, and the Company was in violation of Section 641.225, F.S. On March 31, 2006 the Company submitted to the Office a corrective action plan, and on April 5, 2006 the Company received \$2 million in return for a surplus note for that amount.

SUMMARY OF FINDINGS

The following is a brief summary of items of interest and corrective action to be taken by the Company regarding findings in the examination as of December 31, 2005.

HOLDING COMPANY REGISTRATION STATEMENT

As reported on page 6, the Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), F.A.C. However, the Company had not filed a holding company registration statement with the State of Florida as required by Section 628.801, F.S., and Rule 69O-143.046, F.A.C. **We recommend that the Company file the required holding company registration statement.**

REINSURANCE AGREEMENTS

As reported on page 10, Rule 69O-144.010(3)(c)3, F.A.C., provides that reinsurance agreements shall contain provisions which provide that the reinsurance is payable by the reinsurer on the basis of the liability of the ceding insurer under the contract or contracts reinsured without diminution because of insolvency of the ceding insurer, and that payments by the reinsurer will be made directly to the ceding insurer or its receiver. The Company's reinsurance agreement did not contain these provisions, in violation of Rule 69O-144.010(3)(c)3, F.A.C. **We recommend that the Company amend its reinsurance agreement to comply with Rule 69O-144.010(3)(c)3, F.A.C.**

SURPLUS

As reported on page 17, the \$1,741,175 reported by the Company as its total capital and surplus at December 31, 2005 was \$1,694,803 less than the Company's required minimum capital and surplus of \$3,435,978. Consequently, the Company was in violation of Section 641.225, F.S. On April 5, 2006 the Company received \$2 million in return for a surplus note for that amount. **We recommend that the Company maintain at all times the minimum amount of capital and surplus as required by Section 641.225, F.S.**

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Leon Medical Centers Health Plans, Inc.** as of December 31, 2005, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's total capital and surplus was \$1,741,175, which was not in compliance with Section 641.225, F.S. Its required minimum capital and surplus at December 31, 2005 was \$3,435,978. On April 5, 2006 the Company received \$2 million in return for a surplus note for that amount.

In addition to the undersigned, the following participated in this examination: Tom Cook, Financial Examiner/Analyst; Russell K. Judge, Financial Examiner/Analyst; David C. Schleit, CPA, CFE, Financial Examiner/Analyst Supervisor; and Richard Tan, Actuary.

Respectfully submitted,

Cathy S. Jones, CPA, Financial Examiner/Analyst
Florida Office of Insurance Regulation