

Report on Examination
of
AMERIGROUP Florida, Inc.
(Formerly, Physicians Healthcare Plans, Inc.)
Tampa, Florida
as of
December 31, 2003

By The
Office of Insurance Regulation
Florida Department of Financial Services

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Tallahassee, Florida

March 28, 2005

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, 2003, of the financial condition and corporate affairs of:

AMERIGROUP Florida, Inc.
4200 West Cypress Street
Tampa, Florida 33607

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

SCOPE OF EXAMINATION

This examination covered the period of January 1, 2001 through December 31, 2003. The Company, formerly known as "Physicians Healthcare Plans, Inc.," was last examined by the Florida Office of Insurance Regulation (formerly, the Florida Department of Insurance) (the "Office") as of December 31, 2000.

Planning for the current examination began on March 15, 2004. The fieldwork commenced on April 12, 2004, and concluded on August 24, 2004. 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 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 those balances affect the Company's financial 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 A.M. Best Report, the Company's independent audit reports, and certain work papers prepared by the Company's independent certified public accountant's ("CPA") were reviewed and utilized where applicable within the scope of this examination.

We valued and/or verified the amounts of the Company's assets and liabilities as reported by the Company in its 2003 annual statement. Transactions subsequent to December 31, 2003 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 areas:

- Amounts due to parent, subsidiaries and affiliates
- Reinsurance

STATUS OF ADVERSE FINDINGS FROM PRIOR EXAMINATION

The following is a summary of significant adverse findings contained in the Office's prior examination report as of December 31, 2000, along with resulting action taken by the Company in connection therewith.

LOANS TO OFFICERS

In its 2000 annual statement, the Company incorrectly reported loans to corporate officers as admitted assets in the aggregate amount of \$1,090,000. Such loans are not allowed as assets pursuant to Section 641.35(2)(b), F.S. Resolution: The loans were repaid in February of 2001. The Company did not report loans to corporate officers as admitted assets in its 2003 annual statement.

HISTORY

GENERAL

The Company was incorporated in Florida on February 1, 1992, and commenced business on October 1, 1993. On December 31, 2002, the Company's name was changed from "Physicians Healthcare Plans, Inc." to "AMERIGROUP Florida, Inc." following the acquisition and merger of its parent corporation, as more fully discussed on page 6.

In accordance with Part I of Chapter 641, F.S., the Company was authorized to transact business as a health maintenance organization ("HMO") at December 31, 2003.

As a result of the change in control of the Company and its name change, the Company's articles of incorporation and bylaws were amended and restated on December 31, 2002.

CAPITAL STOCK

As of December 31, 2003, the Company's capitalization was:

Number of authorized common capital shares	1,000
Par value per share	\$1.00

On December 31, 2002, the Company issued 100 shares of its common capital stock to its sole shareholder PHP Holdings, Inc. Each of these shares had a \$1.00 par value, and all were outstanding at December 31, 2003. However, in its 2003 annual statement, the Company reported the total amount of its issued common capital stock at \$1.00.

At December 31, 2003, the Company was wholly-owned by PHP Holdings, Inc., which in turn was owned by AMERIGROUP Corporation. A simplified organizational chart appears on page 8.

PROFITABILITY

The Company reported net premium income of \$316.9 million, \$567.6 million, and \$256.5 million in years 2003, 2002, and 2001, respectively. It incurred a net loss of \$20.2 million in 2003, and reported net income of \$7.8 million and \$10.5 million in years 2002 and 2001, respectively.

DIVIDENDS

During 2003, the Company did not pay any shareholder dividends. During 2002 and 2001, it paid shareholder dividends in the amounts of \$18.3 million and \$6.8 million, respectively. During 2003, the Company received a capital contribution of \$21.5 million from PHP Holdings, Inc.

MANAGEMENT

The annual shareholder meeting for the election of directors was held in accordance with Sections 607.0701 and 607.0803, F.S. Directors serving as of December 31, 2003 were:

Directors

Name and Location	Principal Occupation
Stanley F. Baldwin Virginia Beach, Virginia	Vice President/Secretary of the Company
James G. Carlson Virginia Beach, Virginia	President/Assistant Secretary of the Company
Lorenzo Childress, Jr., MD Virginia Beach, Virginia	Director

The following senior officers were appointed by the Board of Directors in accordance with the Company's bylaws:

Senior Officers

Name	Title
Karen Bornhauser	Vice President & Acting CEO/COO
James G. Carlson	President/Assistant Secretary
Stanley F. Baldwin	Vice President/Secretary
Sherri E. Lee	Vice President/Treasurer
Kathleen K. Toth	Vice President/Assistant Secretary
Scott W. Anglin	Vice President/Assistant Treasurer
Catherine S. Callahan	Vice President

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 and Board of Directors meetings were reviewed for the period examined. The minutes adequately documented the 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.

ACQUISITIONS & MERGERS

On December 31, 2002, PHP Holdings, Inc. merged with a Florida corporation named "AMERIGROUP Florida, Inc.," which was a wholly-owned subsidiary of AMERIGROUP Corporation. PHP Holdings, Inc. was the surviving corporation. In conjunction with the merger, all shares of stock of PHP Holdings, Inc. were either cancelled or converted into one share of common stock owned by AMERIGROUP Corporation, and the name of Physicians Healthcare Plans, Inc., its wholly-owned subsidiary, was changed to AMERIGROUP Florida, Inc. The acquisition and merger were approved by the Office on November 21, 2002, subject to the terms and conditions of Consent Order 64108-02-CO.

On July 1, 2003, the Company acquired the Medicaid line of business from AvMed, Inc. in exchange for \$8,581,060. The Company acquired the rights to provide managed care services to approximately 26,000 Medicaid members who receive health care benefits under Florida's Medicaid program in nine counties in the Miami, Fort Lauderdale, Orlando and Tampa, Florida market areas.

SURPLUS NOTES

At December 31, 2003, the Company was obligated for surplus notes in the total amount of \$23 million. The notes were approved by the Company's board of directors and the Office, and comply with the provisions of Rule 69O-191.088, Florida Administrative Code ("F.A.C.").

AFFILIATED COMPANIES

The Company was a member of an insurance holding company system as defined by Rule 69O-143.045(3), F.A.C. Its latest holding company registration statement was filed with the State of Florida on April 1, 2004, as required by Section 628.801, F.S., and Rule 69O-143.046, F.A.C.

The following agreements were in force between the Company and its affiliates:

MANAGEMENT AGREEMENT

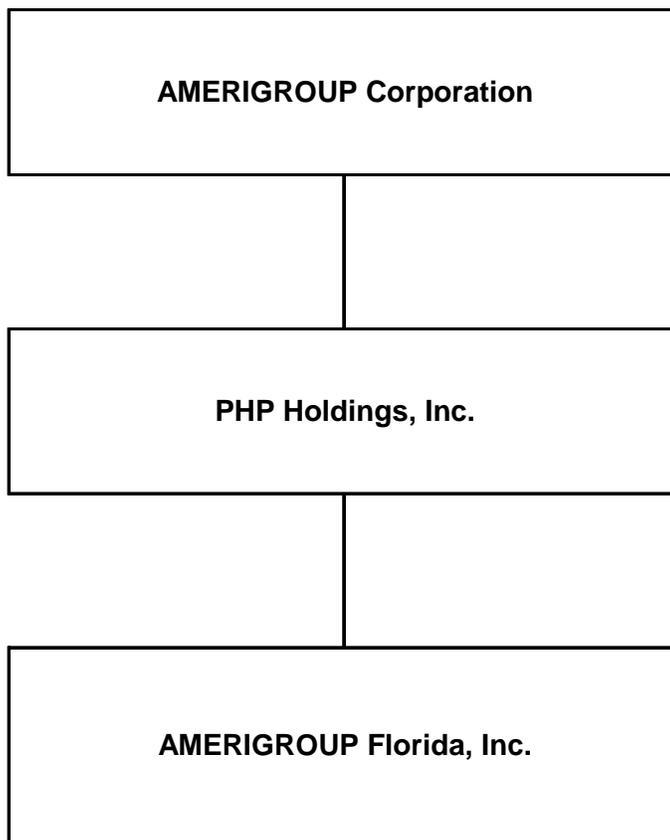
During 2003, AMERIGROUP Corporation provided the Company with administrative, claims processing, and financial support services, pursuant to a management agreement. Services were provided in exchange for a monthly fee based on the amounts of premiums and administrative costs, which fee amounted to approximately \$31,650,000 in 2003.

TAX ALLOCATION AGREEMENT

As of January 1, 2003, the Company's operations are included in the AMERIGROUP Corporation consolidated federal income tax return pursuant to a tax allocation agreement. Consolidated federal income tax is allocated among the members of the group based on the separate return method. The Company incurred no federal income taxes during 2003, and reported no federal income tax liability or recoverable for that year.

A simplified organizational chart as of December 31, 2003, reflecting the holding company system is shown below. Schedule Y of the Company's 2003 annual statement provided the names of all related companies in the holding company group.

**AMERIGROUP Florida, Inc.
Organizational Chart
December 31, 2003**



FIDELITY BOND AND OTHER INSURANCE

The Company maintains general liability and errors and omissions insurance policies which adequately cover its professional liability risk, as required by Rule 69O-191.069, F.A.C.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

Company employees are eligible to participate in a deferred compensation, insurance, and other employee benefit plans offered by AMERIGROUP Corporation.

STATUTORY DEPOSITS

The Company maintains \$300,000 cash on deposit with the Office in accordance with Section 641.285, F.S.

INSURANCE PRODUCTS AND RELATED PRACTICES

TERRITORY AND PLAN OF OPERATION

At December 31, 2003, the Company was authorized to transact business in Florida as an HMO in accordance with Part I of Chapter 641, F.S. It holds 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 is valid until July 30, 2006. The Company provides health care services to 221,651 Medicaid and Florida Healthy Kids members in the State of Florida. Prior to January 1, 2003, health care services were also provided to Medicare and commercial members. As a Medicaid-only provider, the Company has no general agents and brokers, but utilizes approximately 40 sales representatives to market its Medicaid products. As of December 31, 2003, the Company operates in the Florida counties of Broward, Hillsborough, Lee, Manatee, Miami-Dade, Orange, Osceola, Palm Beach, Pasco, Pinellas, Polk, Sarasota, and Seminole.

TREATMENT OF MEMBERS

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

REINSURANCE

ASSUMED

The Company does not assume any reinsurance business.

CEDED

The Company cedes risk to Allianz Life Insurance Company of North America under a reinsurance agreement. During 2003, premiums ceded amounted to \$389,110. The Company reported no reinsurance liabilities or recoverables at December 31, 2003.

ACCOUNTS AND RECORDS

An independent CPA audited the Company's statutory basis financial statements annually for years 2001, 2002, and 2003, 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 statutory home office is located in Tampa, Florida. A significant portion of the Company's books and records are located in Virginia Beach, Virginia, where this examination was conducted.

FINANCIAL STATEMENTS PER EXAMINATION

The following pages contain statements of the Company's financial position at December 31, 2003, as determined by this examination, and the results of its operations for the year then ended as reported by the Company. Adjustments resulting from this examination are summarized on page 18.

AMERIGROUP Florida, Inc.
Assets
December 31, 2003

Classification	Per Company	Examination Adjustments	Per Examination
Bonds	\$13,207,994	\$20,900,000	\$34,107,994
Preferred stocks	0	6,553,995	6,553,995
Cash	63,677,576	(39,400,000)	24,277,576
Investment income due & accrued	75,817	0	75,817
Uncollected premiums & agents' balances	304,818	0	304,818
Electronic data processing equipment & software	<u>219,748</u>	<u>0</u>	<u>219,748</u>
Totals	<u>\$77,485,953</u>	<u>(\$11,946,005)</u>	<u>\$65,539,948</u>

AMERIGROUP Florida, Inc.
Liabilities, Capital and Surplus
December 31, 2003

Liabilities	Per Company	Examination Adjustments	Per Examination
Claims unpaid	\$37,183,210	(\$5,486,820)	\$31,696,390
Accrued medical incentive pool and bonus payments	688,148	0	688,148
Unpaid claims adjustment expenses	923,232	0	923,232
Aggregate health policy reserves	0	5,486,820	5,486,820
Premiums received in advance	23,453,026	0	23,453,026
Amounts due to parent, subsidiaries and affiliates	5,451,222	0	5,451,222
Aggregate write-ins for other liabilities	<u>373,478</u>	<u>0</u>	<u>373,478</u>
Total liabilities	68,072,316	0	68,072,316
Capital and Surplus			
Common capital stock	1	0	1
Gross paid in and contributed surplus	23,718,429	0	23,718,429
Surplus notes	23,000,000	0	23,000,000
Unassigned funds (surplus)	<u>(37,304,793)</u>	<u>(11,946,005)</u>	<u>(49,250,798)</u>
Total capital and surplus	<u>9,413,637</u>	<u>(11,946,005)</u>	<u>(2,532,368)</u>
Total liabilities, capital and surplus	<u><u>\$77,485,953</u></u>	<u><u>(\$11,946,005)</u></u>	<u><u>\$65,539,948</u></u>

AMERIGROUP Florida, Inc.
Statement of Income
For Year Ended December 31, 2003

Net premium income		\$316,917,491
Hospital/medical benefits	\$163,124,985	
Other professional services	3,615,224	
Emergency room & out-of-area	35,639,056	
Prescription drugs	62,371,434	
Aggregate write-ins for other hospital & medical	3,831,764	
Incentive pool & withhold adjustments	1,190,353	
Total medical & hospital	<u>269,772,816</u>	
Claims adjustment expenses	8,093,184	
General administrative expenses	<u>59,911,844</u>	
Total underwriting deductions		<u>337,777,844</u>
Net underwriting gain or (loss)		(20,860,353)
Net investment income earned		<u>673,802</u>
Net income (loss)		<u><u>(\$20,186,551)</u></u>

Capital and Surplus Account

Capital and surplus, December 31, 2002		\$5,209,315
Net income or (loss)		(20,186,551)
Change in net deferred income tax		(90,813)
Change in nonadmitted assets		(12,677,176)
Change in surplus notes		15,700,000
Paid in surplus adjustments		<u>21,458,862</u>
		9,413,637
Examination adjustments		<u>(11,946,005)</u>
Capital and surplus, December 31, 2003		<u><u>(\$2,532,368)</u></u>

COMMENTS ON FINANCIAL STATEMENTS

ASSETS

Bonds **\$34,107,994**

The \$13,207,994 reported by the Company was increased by \$20,900,000 as a result of a reclassification of investments in bonds incorrectly classified by the Company as cash equivalents in its annual statement. The investments in bonds did not qualify as cash equivalents as defined by Section 641.35(1)(a), F.S.

Preferred Stocks **\$6,553,995**

The Company incorrectly reported \$18,500,000 in preferred stock investments as cash equivalents in its annual statement, of which \$6,553,995 has been reclassified as preferred stocks. The investments in preferred stocks did not qualify as cash equivalents as defined by Section 641.35(1)(a), F.S. The total amount of an HMO's corporate stock investments is limited by Section 641.35(14)(a)4., F.S., to 10% of its admitted assets. As a result, the remainder of the Company's preferred stock investments, or \$11,946,005, has been nonadmitted on the basis that it exceeds the aforementioned investment limitation.

Cash **\$24,277,576**

The \$63,677,576 reported by the Company was decreased by \$39,400,000 as a result of the exam adjustments to bonds and preferred stocks discussed above.

LIABILITIES

Reserves, claims liabilities, and related obligations **\$38,794,590**

The Company reported claims unpaid in the amount of \$37,183,210, accrued medical incentive pool and bonus payments in the amount of \$688,148, unpaid claims adjustment expenses in the amount of \$923,232, and no liability for aggregate health policy reserves. An outside actuarial firm appointed by the Board of Directors rendered an opinion that the amounts carried in the Company's balance sheet as of December 31, 2003 reasonably provided for all of the Company's unpaid claims under the terms of its subscriber agreements. The Office actuary reviewed work papers provided by the Company and concurred that the total of these reported liabilities, or \$38,794,590, reasonably provided for all such claims. However, because the Company did not specifically reserve for obligations resulting from insufficient premiums received from the Florida Agency for Health Care Administration, a premium deficiency reserve has been reclassified from claims unpaid to aggregate health policy reserves in the amount of \$5,486,820.

CAPITAL AND SURPLUS **(\$2,532,368)**

The Company is required by Section 641.225(1), F.S., to maintain a minimum surplus in an amount that is the greater of \$1.5 million, 10% of its total liabilities, or 2% of its total annualized premium. As of December 31, 2003, the Company's required minimum surplus, per Section 641.225(1), F.S., was \$6,807,232. In addition, the Company was required by Consent Order 64108-02-CO, filed on November 21, 2002, to attain \$3 million in excess surplus over the required minimum statutory surplus. At December 31, 2003, the Company's total minimum surplus requirement, therefore, was \$9,807,232. However, its actual total surplus after examination adjustments was (\$2,532,368), which is \$12,339,600 less than the total minimum surplus required at December 31, 2003 of \$9,807,232. As a result of examination adjustments, the Company was insolvent as of December 31, 2003 due to investments in preferred stocks in excess of limits set forth in Section 641.35(14)(a)4., F.S. Subsequent to the date of this examination, in April of 2004, the Company received a capital contribution of \$400,000.

AMERIGROUP Florida, Inc.
Comparative Analysis of Changes in Capital & Surplus
December 31, 2003

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, 2003 - per annual statement			\$9,413,637
	<u>Per Company</u>	<u>Per Exam</u>	<u>Increase (Decrease) In Capital & Surplus</u>
Assets	\$77,485,953	\$65,539,948	(\$11,946,005)
Liabilities	\$68,072,316	\$68,072,316	<u>\$0</u>
Net change in capital and surplus			<u>(11,946,005)</u>
Capital & surplus, December 31, 2003 - per examination			<u><u>(\$2,532,368)</u></u>

SUMMARY OF FINDINGS

COMPLIANCE WITH PREVIOUS DIRECTIVES

The Company has taken the necessary actions to comply with the comments contained in the prior examination report issued by the Office as of December 31, 2000.

CURRENT EXAMINATION COMMENTS AND CORRECTIVE ACTION

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, 2003.

CAPITAL STOCK

On December 31, 2002, the Company issued 100 shares of its common capital stock to its sole shareholder PHP Holdings, Inc., as discussed on page 3. Each of these shares had a \$1.00 par value, and all were outstanding at December 31, 2003. However, in its 2003 annual statement, the Company reported the total amount of its issued common capital stock at \$1.00. **We recommend that the Company accurately report its issued capital stock on future statements filed with the Office.**

PREFERRED STOCKS

In its 2003 annual statement, the Company incorrectly reported \$18,500,000 in preferred stock investments as cash equivalents. As discussed on page 16, this amount exceeded the investment limitation contained in Section 641.35(14)(a)4., F.S., by \$11,946,005. **We recommend that the Company comply with the Section 641.35(14)(a)4., F.S., investment limitation on all future statements filed with the Office.**

CLASSIFICATION OF INVESTMENTS

In its 2003 annual statement, the Company incorrectly reported the value of bonds and preferred stocks as cash equivalents in the total amount of \$39,400,000, as discussed on page 16. **We recommend that the Company correctly classify its investments in cash equivalents, bonds, and preferred stocks in accordance with the annual statement instructions and Section 641.35, F.S., on all future statements filed with the Office.**

RESERVES, CLAIMS LIABILITIES, AND RELATED EXPENSES

While the Company reported its obligations for unpaid claims at an adequate level in total, it did not properly classify premium deficiency reserves in the amount of \$5,486,820 as aggregate health policy reserves in its 2003 annual statement, as more fully discussed on page 17. **We recommend that the Company correctly classify its liabilities in accordance with the annual statement instructions on all future statements filed with the Office.**

CAPITAL AND SURPLUS

As discussed on page 17, the Company's required minimum surplus, per Section 641.225(1), F.S., was \$6,807,232 at December 31, 2003. In addition, the Company was required by Consent Order 64108-02-CO, filed on November 21, 2002, to attain \$3 million in excess surplus over the required minimum statutory surplus. At December 31, 2003, the Company's total minimum surplus requirement, therefore, was \$9,807,232. However, its actual total surplus after examination adjustments was (\$2,532,368), which is \$12,339,600 less than the required amount of \$9,807,232. As a result of examination adjustments, the Company was insolvent as of December 31, 2003 due to investments in preferred stocks in excess of limits set forth in Section 641.35(14)(a)4, F.S. **We recommend that the Company maintain at all times the minimum surplus required by Section 641.225(1), F.S.**

Subsequent event: On March 18, 2005, the Company represented to the Office that, subsequent to the date of the examination, its insolvent condition was corrected; that as of December 31, 2004, its investments in preferred stocks no longer exceeded the investment limitations of Section 641.35(14)(a)4., F.S., and that the Company currently complies with the surplus requirements of 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 **AMERIGROUP Florida, Inc.** as of December 31, 2003, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's total capital and surplus was (\$2,532,368), which did not comply with Section 641.225, F.S., or the surplus requirement of Consent Order 64108-02-CO, and the Company was insolvent as a result of examination adjustments. Subsequent event: On March 18, 2005, the Company represented to the Office that, subsequent to the date of the examination, its insolvent condition was corrected; that as of December 31, 2004, its investments in preferred stocks no longer exceeded the investment limitations of Section 641.35(14)(a)4., F.S., and that the Company currently complies with the surplus requirements of Section 641.225, F.S.

In addition to the undersigned, Robert Y. Meszaros, Financial Specialist, and Richard Tan, Actuary, participated in this examination.

Respectfully submitted,

Carolyn M. Maynard, CFE
Financial Specialist
Florida Office of Insurance Regulation