

Report on Examination
of
Freedom Health, Inc.
Tampa, Florida
as of
December 31, 2007

By The
State of Florida
Office of Insurance Regulation

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Tallahassee, Florida

April 6, 2009

Kevin M. McCarty, Commissioner
Florida Office of Insurance Regulation
200 E. Gaines Street, Room 101
Tallahassee, Florida 32399-0301

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, 2007, of the financial condition and corporate affairs of:

Freedom Health, Inc.
5403 Church Avenue North
Tampa, Florida 33614

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

SCOPE OF EXAMINATION

This examination covered the period of February 14, 2005 through December 31, 2007. This was the first financial condition examination of the Company by the Florida Office of Insurance Regulation (the "Office").

Planning for the current examination began on March 27, 2008. The fieldwork commenced on March 31, 2008 and concluded on January 30, 2009. 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 2007 annual statement. Transactions subsequent to December 31, 2007 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:

- Uncollected premiums and agents' balances
- General expenses due or accrued
- Amounts due to parent, subsidiaries and affiliates
- Commitments and contingent liabilities

HISTORY

GENERAL

The Company was incorporated in Florida on February 27, 2004 and commenced business on September 1, 2005.

As of the date of this examination, the Company was authorized to transact business as a health maintenance organization (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, 2007, the Company's capitalization was as follows:

	<u>Common Stock</u>
Shares authorized	25,000,000
Shares issued and outstanding	14,347,826
Total capital stock	\$1,435
Par value per share	\$0.0001

At December 31, 2007, the Company was owned by Health Management Services of USA, LLC (HMS) and Liberty Acquisition Group, LLC, and was affiliated with Pagidipati Enterprises, Inc. and Global TPA, LLC. In its 2007 annual statement, the Company incorrectly reported that HMS was the Company's sole shareholder when in fact HMS owned 10 million of its common shares and Liberty Acquisition Group, LLC owned 4,347,826 of its common shares. An abbreviated organizational chart appears on page 7.

PROFITABILITY

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

	<u>2007</u>	<u>2006</u>	<u>2005</u>
Year-end enrollment	12,554	4,033	1,328
In millions:			
Net premiums	\$98.4	\$26.2	\$1.8
Total revenues	\$98.4	\$26.2	\$1.8
Net loss	\$10.7	\$1.3	\$0.9
Total capital and surplus (deficit)	(\$3.8)	(\$0.4)	\$1.5

DIVIDENDS

The Company did not pay 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, 2007 were:

Directors	
<u>Name and Location</u>	<u>Principal Occupation</u>
Devaiah Pagidipati, M.D. Ocala, Florida	Physician
Rahuldev R. Pagidipati Jacksonville, Florida	Student
Siddhartha Pagidipati Ocala, Florida	Chief Operating Officer of Freedom Health, Inc.
Srujani D. Pagidipati Ocala, Florida	Legal Consultant
Krishna Rao, M.D. Ocala, Florida	Physician

The Company's senior officers at December 31, 2007 were:

Senior Officers	
Name	Title
Devaiah Pagidipati, M.D.	President and Chief Executive Officer
Siddhartha Pagidipati	Secretary, Treasurer and Chief Operating Officer

According to the Company's bylaws, the Company's officers were to have been elected for a term of one year by the Company's board of directors at the board's annual meeting. However, there was no indication of such an election in the minutes of the Board of Directors meetings.

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. Except as noted above, 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.). Its latest holding company registration statement was filed with the State of Florida, as required by Section 628.801, F.S., and Rule 69O-143.046, F.A.C., on April 1, 2008; however, the registration statement failed to include the names of all affiliates of the Company, as required.

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

Management Agreement

Global TPA, LLC (Global) provided administrative and operational services to the Company pursuant to an October 1, 2004 management agreement, as amended on October 1, 2005 and October 1, 2006, in return for fees which amounted to \$1.9 million, \$4.6 million, and \$13.9 million in 2005, 2006, and 2007, respectively. The services provided by Global included claims management, marketing, enrollment, member, provider relations and network development, provider credentialing, utilization management, grievance and appeals, administrative, contracts management, and information systems management and reporting services.

Management and Administrative Services Agreement

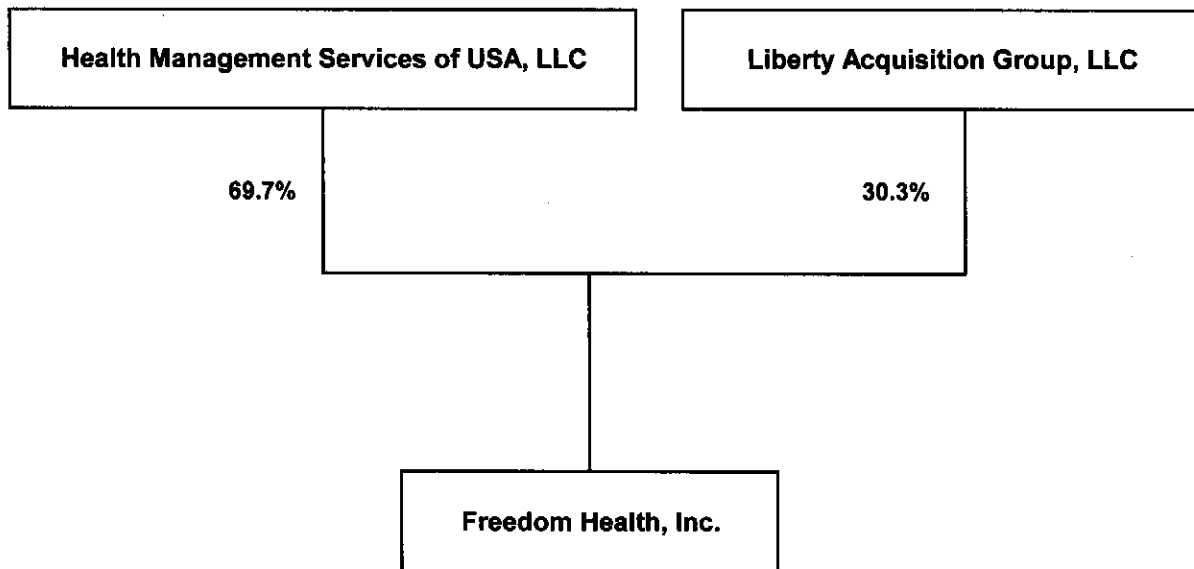
Global outsourced certain of the above services to U. S. Healthcare Holdings, LLC (USHH) pursuant to an April 1, 2005 agreement between Global, USHH and the Company.

Ancillary Services Agreement

Pagidipati Enterprises, Inc. provided clinical laboratory services to the Company pursuant to a February 1, 2005 agreement in return for fees which amounted to \$30,288, \$497,017, and \$1,113,819 in 2005, 2006, and 2007, respectively.

An abbreviated organizational chart as of December 31, 2007 reflecting the holding company system is shown below. Schedule Y of the Company's 2007 annual statement did not provide the names of all related companies in the holding company group.

**Freedom Health, Inc.
Organizational Chart
December 31, 2007**



FIDELITY BOND AND OTHER INSURANCE

The Company maintained acceptable levels of general liability insurance in compliance with Rule 69O-191.069, F.A.C., and was insured by a blanket fidelity bond in the amount of \$1 million as required by Section 641.22, F.S.

As an individual practice association (IPA) model HMO, the Company maintained adequate professional liability insurance. It required in its provider contracts that its providers certify and maintain appropriate levels of medical malpractice insurance or its equivalent in compliance with Rule 69O-191.069, F.A.C.

PENSION, STOCK OWNERSHIP, AND INSURANCE PLANS

The Company had no direct employees and, as a result, did not provide pension or other employee benefits.

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, 2007, 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., valid until January 22, 2009.

The Company used a network of general agents and brokers and operated as an IPA model as defined by Rule 69O-191.024, F.A.C. It provided health care services to Medicare and Medicaid members. Its total membership at December 31, 2007 was 12,554, of which 99% was Medicare.

The Company operated in the Florida counties of Broward, Hernando, Lake, Marion, Miami-Dade, Orange, Palm Beach, Pasco, Pinellas, Sarasota and Sumter.

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 stop-loss reinsurance coverage of up to \$1 million per member per year with OneBeacon Insurance Company with an annual retention limit of \$200,000. The premium rate was \$4.95 per member per month subject to a minimum annual premium of \$400,000. The agreement was found to comply with NAIC standards with respect to the standard insolvency and arbitration clauses, transfer of risk, and reporting and settlement information deadlines. The reinsurance contract was reviewed by the Company's appointed actuary and utilized in determining the ultimate loss opinion.

ACCOUNTS AND RECORDS

Independent CPA's audited the Company's statutory-basis financial statements annually for years 2005, 2006 and 2007, 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 was located in Tampa, Florida, where this examination was conducted.

Internal Control Weakness

A single individual performed accounting services for the Company and made its bank deposits, received its signed checks for mailing, reconciled its bank statements, and made entries to the Company's general ledger. This lack of segregation of duties constituted a weakness in the Company's internal controls over cash.

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

Independent Auditor Agreements

The Company contracted with Aidman, Piser & Company to audit the Company's 2005 statutory-basis financial statements, and with Gregory, Sharer & Stuart, P.A. to audit the Company's 2006 and 2007 statutory-basis financial statements.

CMS Agreement

On July 7, 2005, the Company contracted with the Centers for Medicare & Medicaid Services (CMS) to operate as a Medicare Advantage Organization. The agreement was subsequently augmented and renewed and was effective through December 31, 2008.

Pharmacy Benefits Services Agreement

Pharmaceutical Care Network provided pharmacy services to the Company pursuant to a November 1, 2004 agreement which was amended on January 1, 2005 and March 2, 2007.

Management Services Agreement

Preferred Physicians Healthcare Alliance, LLC provided utilization management, case management and care management services to the Company pursuant to an October 1, 2006 agreement.

Consulting Agreement

IkaSystems Corporation provided claims processing, accounting processing and consulting services to the Company pursuant to an October 18, 2004 agreement.

FINANCIAL STATEMENTS PER EXAMINATION

The following four pages contain statements of the Company's financial position at December 31, 2007 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 20.

Freedom Health, Inc.
Assets
December 31, 2007

	Per Company	Examination Adjustments	Per Examination
Bonds	\$5,808,795	\$0	\$5,808,795
Common stocks	0	1,686,266	1,686,266
Cash, cash equivalents and short-term investments	6,104,046	(3,619,202)	2,484,844
	<u>11,912,841</u>	<u>(1,932,936)</u>	<u>9,979,905</u>
Investment income due and accrued	91,831	0	91,831
Uncollected premiums and agents' balances	12,352	0	12,352
Accrued retrospective premiums	6,592,072	0	6,592,072
Health care and other amounts receivable	186,500	0	186,500
Total assets	<u><u>\$18,795,596</u></u>	<u><u>(\$1,932,936)</u></u>	<u><u>\$16,862,660</u></u>

Freedom Health, Inc.
Liabilities, Capital and Surplus
December 31, 2007

Liabilities	Per Company	Examination Adjustments	Per Examination
Claims unpaid	\$21,952,000	\$0	\$21,952,000
Unpaid claims adjustment expenses	400,285	0	400,285
Aggregate health policy reserves	115,554	0	115,554
General expenses due or accrued	110,203	0	110,203
Total liabilities	<u>22,578,042</u>	<u>0</u>	<u>22,578,042</u>
Capital and Surplus			
Common capital stock	0	1,435	1,435
Gross paid in and contributed surplus	11,203,512	(1,435)	11,202,077
Unassigned funds (deficit)	<u>(14,985,958)</u>	<u>(1,932,936)</u>	<u>(16,918,894)</u>
Total capital and surplus (deficit)	<u>(3,782,446)</u>	<u>(1,932,936)</u>	<u>(5,715,382)</u>
Total liabilities, capital and surplus	<u>\$18,795,596</u>	<u>(\$1,932,936)</u>	<u>\$16,862,660</u>

Freedom Health, Inc.
Statement of Revenue and Expenses
For The Year Ended December 31, 2007

Net premium income		\$98,367,113
Hospital and medical benefits	\$73,155,590	
Other professional services	2,072,179	
Emergency room and out-of-area	599,989	
Prescription drugs	15,917,142	
Total hospital and medical	<u>91,744,900</u>	
Claims adjustment expenses	321,575	
General administrative expenses	<u>17,676,907</u>	
Total underwriting deductions		<u>109,743,382</u>
Net underwriting gain (loss)		(11,376,269)
Net investment income earned	697,464	
Net realized capital gains	<u>15,565</u>	
Net investment gains		<u>713,029</u>
Net income (loss)		<u><u>(\$10,663,240)</u></u>

Freedom Health, Inc.
Capital and Surplus Account
For The Year Ended December 31, 2007

Capital and surplus (deficit) - December 31, 2006		(\$362,145)
Net income (loss)	(\$10,663,240)	
Change in net unrealized capital gains (losses)	(146,934)	
Change in net deferred income tax	3,771,824	
Change in nonadmitted assets	(3,663,951)	
Paid in surplus	7,282,000	
Examination adjustments	<u>(1,932,936)</u>	
		<u>(5,353,237)</u>
Capital and surplus (deficit) - December 31, 2007		<u><u>(\$5,715,382)</u></u>

COMMENTS ON FINANCIAL STATEMENTS

Common Stocks	\$1,686,266
Cash, Cash Equivalents and Short-Term Investments	\$2,484,844

In its 2007 annual statement, the Company reported 'cash, cash equivalents and short-term investments' in the amount of \$6,104,046 which incorrectly included \$3,619,202 in mutual fund investments. In accordance with *Statement of Statutory Accounting Principles (SSAP) No. 30*, the investments should have been reported as investments in common stocks. The admitted portion of the Company's investments in common stocks is limited by Section 641.35(14)(a)4, F.S., to 10% of its total admitted assets. Accordingly, the mutual fund investments have been reclassified from 'cash, cash equivalents and short-term investments' to 'common stocks', and the admitted portion of the investments has been limited to \$1,686,266.

Losses and Loss Adjustment Expenses	\$22,467,839
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The Company's appointed actuary rendered an opinion that the amounts carried in the Company's balance sheet as of December 31, 2007 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.

Common Capital Stock	\$1,435
Gross Paid In and Contributed Surplus	\$11,202,077

In its 2007 annual statement, the Company reported 'gross paid in and contributed surplus' of \$11,203,512 which incorrectly included \$1,435 of issued common stock. As a result, \$1,435 has been reclassified from 'gross paid in and contributed surplus' to 'common capital stock'.

Deficit**\$5,715,382**

The deficit of \$3,782,446 reported by the Company at December 31, 2007 has been increased by \$1,932,936 to \$5,715,382 as a result of the examination adjustments described above. Because the Company's actual capital and surplus after examination adjustments was a deficit of \$5,715,382, which is \$7,973,186 less than its minimum required amount of capital and surplus of \$2,257,804, the Company was insolvent and in violation of Section 641.225, F.S. On April 1, 2008, the Company received \$6.1 million from America's 1st Choice Holdings of Florida, LLC in exchange for a surplus note.

Freedom Health, Inc.
Comparative Analysis of Changes in Capital and Surplus
December 31, 2007

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

Capital and surplus (deficit), December 31, 2007 - per annual statement				(\$3,782,446)
	<u>Per</u> <u>Company</u>	<u>Per</u> <u>Examination</u>	<u>Increase</u> <u>(Decrease)</u> <u>In Capital</u> <u>& Surplus</u>	
Assets:				
Common stocks	\$0	\$1,686,266	\$1,686,266	
Cash, cash equivalents and short-term investments	\$6,104,046	\$2,484,844	(\$3,619,202)	
Capital and Surplus:				
Common capital stock	\$0	\$1,435	\$1,435	
Gross paid in and contributed surplus	\$11,203,512	\$11,202,077	(\$1,435)	
Net change in capital and surplus				<u>(1,932,936)</u>
Capital and surplus (deficit), December 31, 2007 - per examination				<u><u>(\$5,715,382)</u></u>

SUBSEQUENT EVENTS

In April of 2008, the Company was acquired by America's 1st Choice Holdings of Florida, LLC, following approval by the Office on March 6, 2008.

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, 2007.

Shareholders

As reported on page 3, the Company incorrectly reported in its 2007 annual statement that HMS was the Company's sole shareholder when in fact HMS owned 10 million of its common shares and Liberty Acquisition Group, LLC owned 4,347,826 of its common shares. **We recommend that, in future statements filed with the Office, the Company accurately report the names of its affiliates in accordance with the *Annual Statement Instructions*.**

Compliance With Bylaws

As reported on page 5, there was no indication in the minutes of the Board of Directors meetings that the Company's officers were elected in accordance with the bylaws. **We recommend that the Company comply with its bylaws and that the Board of Directors document the election of officers in the minutes of its meetings.**

Holding Company Registration Statement

As reported on page 6, the Company's holding company registration statement filed on April 1, 2008 failed to include the names of all affiliates of the Company, as required. **We recommend that the Company include the names of all of its affiliates in its future holding company registration statements.**

Internal Control Weaknesses

As discussed on page 11, the Company's internal controls of its cash were inadequate. **We recommend that the Company establish adequate internal controls over its cash including segregation of duties in its accounting department.**

Mutual Fund Investments

As discussed on page 18, in its 2007 annual statement the Company improperly classified and overstated the amount of its mutual fund investments. **We recommend that, in future statements filed with the Office, the Company report its mutual fund investments in accordance with the provisions of SSAP No. 30 and Section 641.35(14)(a)4, F.S.**

Common Capital Stock

As reported on page 18, the Company incorrectly reported the amount of its common stock in its 2007 annual statement. **We recommend that, in future statements filed with the Office, the Company correctly report the amount of its common stock in accordance with the *Annual Statement Instructions*.**

Deficit

As reported on page 19, the Company was insolvent and in violation of Section 641.225, F.S., as of December 31, 2007. Its total capital and surplus was a deficit of \$5,715,382, and was \$7,973,186 less than its minimum required amount of capital and surplus of \$2,257,804. On April 1, 2008, the Company received \$6.1 million from America's 1st Choice Holdings of Florida, LLC in exchange for a surplus note. **We recommend that the Company maintain at least the minimum amount of capital and surplus required by Section 641.225, F.S., at all times.**

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of **Freedom Health, Inc.** as of December 31, 2007, consistent with the insurance laws of the State of Florida.

Per examination findings, the Company's total capital and surplus was a deficit of \$5,715,382, which was not in compliance with Section 641.225, F.S. Its required minimum capital and surplus at December 31, 2007 was \$2,257,804. On April 1, 2008, the Company received \$6.1 million from America's 1st Choice Holdings of Florida, LLC in exchange for a surplus note.

In addition to the undersigned, the following participated in this examination: Thomas I. Cook, CISA, Financial Examiner/Analyst; Stephen Feliu, CFE (Fraud), Financial Examiner/Analyst; Cathy S. Jones, CPA, Financial Examiner/Analyst Supervisor; and Richard Tan, Actuary.

Respectfully submitted,

Robert Y. Meszaros, Financial Specialist
Florida Office of Insurance Regulation