

REPORT OF  
FINANCIAL EXAMINATION

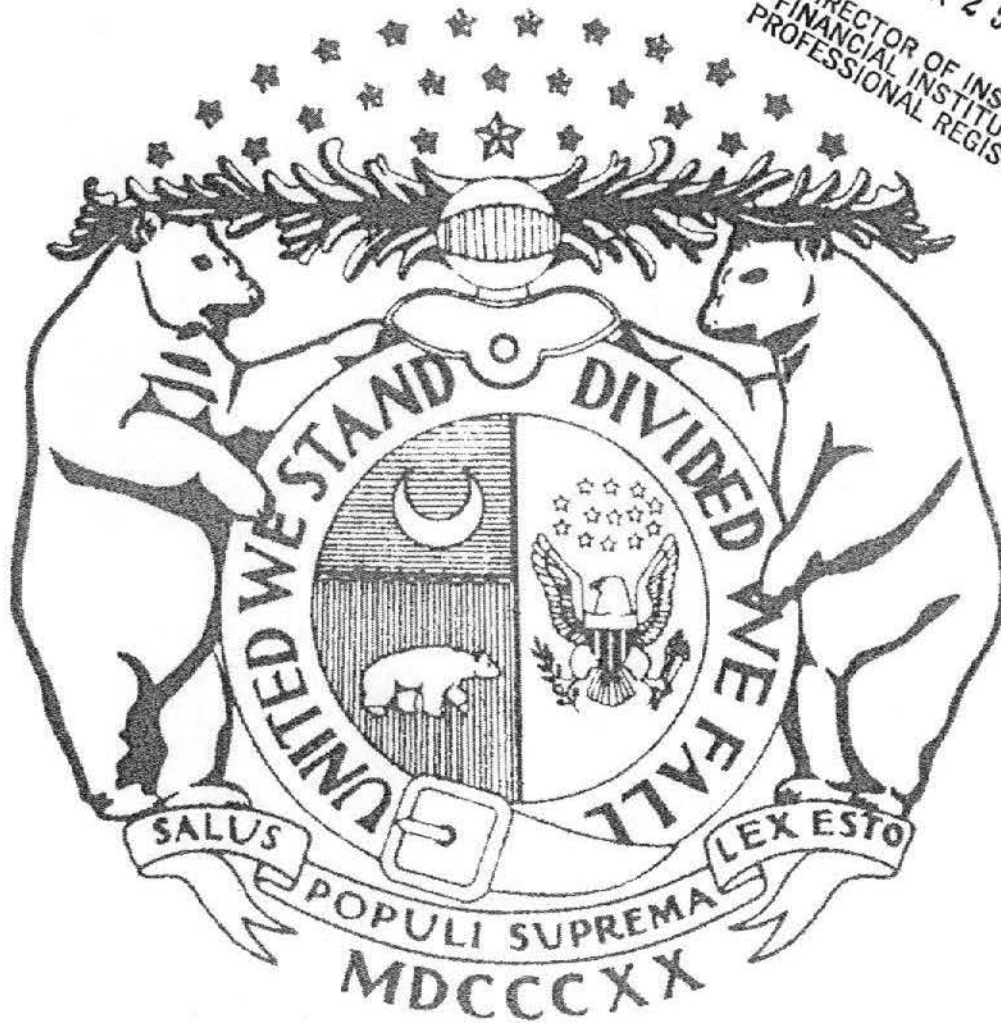
HEALTHCARE USA OF MISSOURI, LLC

As Of  
December 31, 2007

FILED

APR 25 2009

DIRECTOR OF INSURANCE,  
FINANCIAL INSTITUTIONS &  
PROFESSIONAL REGISTRATION



STATE OF MISSOURI

DEPARTMENT OF INSURANCE, FINANCIAL INSTITUTIONS  
AND PROFESSIONAL REGISTRATION

JEFFERSON CITY, MISSOURI

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March 5, 2009  
St. Louis, Missouri

Honorable Alfred W. Gross, Commissioner  
State Corporation Commission  
Bureau of Insurance  
Commonwealth of Virginia  
Chair of the NAIC Financial Condition (E) Committee

Honorable Merle Scheiber, Director  
South Dakota Division of Insurance  
Secretary of the Midwestern Zone, NAIC

Honorable John M. Huff, Director  
Missouri Department of Insurance, Financial Institutions  
and Professional Registration  
301 West High Street, Room 530  
Jefferson City, MO 65101

Dear Gentlemen:

In accordance with your financial examination warrant, a comprehensive financial examination has been made of the records, affairs and financial condition of

### **HEALTHCARE USA OF MISSOURI, LLC**

hereinafter referred to as such or as the "Company." The Company's statutory home office is located at 10 S. Broadway, Suite 1200, St. Louis, Missouri 63102, telephone number (314) 444-7264. This examination began on December 22, 2008 and concluded on the above date.

### **SCOPE OF EXAMINATION**

#### **Period Covered**

The last full scope association financial examination of the Company was made as of December 31, 2003 by examiners from the state of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC) with no other zones participating.

The current full scope association financial examination covers the period from January 1, 2004 through December 31, 2007 and was conducted by examiners from the state of Missouri representing the Midwestern Zone of the NAIC with no other zones participating.

This examination also included material transactions or events occurring subsequent to December 31, 2007.

## **PRIOR EXAMINATION COMMENTS**

Listed below is the comment taken from the prior examination report as of December 31, 2003. The Company's response and the item's current status are also indicated.

*Comment: Management-Office of Treasurer*

"The office of Treasurer has been vacant since early 2003. It is recommended that the Company comply with Section 5.10.5 of its Amended and Restated Operating Agreement by appointing someone to fill the office of Treasurer."

*Company response:*

"The health plan is currently recruiting for a Chief Financial Officer (CFO); upon hiring, the CFO will be appointed as Treasurer. In the meantime, the Assistant Treasurer is fulfilling all Treasurer responsibilities."

*Current status:*

John Stelben was elected Treasurer in January 2005 and continued to serve in that position at year-end 2007.

## **HISTORY**

### **General**

On January 31, 1995, HealthCare USA Midwest, Inc. and SLR Managed Care Corporation organized the Company under the Missouri Limited Liability Company Act. HealthCare USA Midwest, Inc. held a seventy percent (70%) equity interest in the Company; SLR Managed Care Corporation held the remaining thirty percent (30%). HealthCare USA Midwest, Inc. eventually purchased SLR Managed Care Corporation's interest in the Company for approximately \$1.5 million effective January 1, 1996.

On February 3, 2005, the Department approved the merger of HealthCare USA Midwest, Inc. (Delaware), the Company's direct parent, into Coventry Health Care, Inc. (Delaware). Coventry Health Care, Inc., which had been the Company's ultimate controlling person prior to the merger, became the Company's direct parent.

On July 17, 1995, the Company was licensed as a health maintenance organization (HMO) under Sections 354.400-354.550 RSMo. In September 1995, the Missouri Department of Social Services, Division of Medical Services awarded the Company a contract to provide services to Medicaid enrollees in the City of St. Louis and four surrounding counties. In 1996, the Company was awarded an additional contract to provide service in central Missouri. In 2002, the Company was awarded a third contract to service western Missouri.

### Capital Stock

The Company is not authorized to issue capital stock under the Missouri Limited Liability Company Act. As of December 31, 2007, Coventry Health Care, Inc. had contributed \$11,042,055 in capital to the Company.

### Dividends

The Company has paid dividends to Coventry Health Care, Inc. as follows:

<u>Year</u>	<u>Amount</u>
2000-2003	\$ 17,200,000
2004	8,000,000
2005	<u>12,000,000</u>
Total	<u>\$ 37,200,000</u>

### Management

The Board of Managers, consisting of at least three members, directs the Company's affairs. Managers serving at December 31, 2007 were as follows.

<u>Director</u>	<u>Affiliation</u>
Beverly A. Allen Rochester Hills, MI	President and Chief Executive Officer OmniCare Health Plan, Inc.
Claudia Bjerre Akron, OH	President and Chief Executive Officer HealthCare USA of Missouri
Jan Hodges Carlisle, PA	Vice President HealthCare USA of Missouri
Francis S. Soistman, Jr. Darnestown, MD	Executive Vice President HealthCare USA of Missouri
Allen H. Spath Caseyville, IL	Chief Operating Officer HealthCare USA of Missouri

Officers appointed and serving as of December 31, 2007 were as follows.

<u>Name</u>	<u>Office</u>
Claudia Bjerre	President and Chief Executive Officer
John J. Stelben	Treasurer
Shirley A. Smith	Secretary
Francis S. Soistman, Jr.	Executive Vice President
Allen H. Spath	Chief Operating Officer
John J. Ruhlmann	Controller
Jonathan D. Weinberg	Assistant Secretary
G. Kenneth Robinson, III	Assistant Treasurer
Jan Hodges	Vice President

### **Conflict of Interest**

Conflict of interest disclosure statements are executed annually by all officers and members of the board of managers. Disclosure statements for the years 2004 through 2007 were reviewed. No material conflicts were disclosed.

### **Corporate Records**

The Company's Articles of Organization and the Operating Agreement were reviewed. There were no changes to the Operating Agreement during the current examination period. The company restated its Articles of Organization on July 16, 2004. The restated Articles of Organization were submitted to the Missouri Secretary of State and approved on July 30, 2004. The restated Articles of Organization changed the Company's registered agent. There were no other changes in the restated Articles of Organization.

The minutes of the meetings of the Sole Member and of the Board of Managers were reviewed. The minutes appear to reflect proper approval of the transactions and corporate events for the period under examination.

### **Acquisitions, Mergers and Major Corporate Events**

In February 2007, the Company completed an asset purchase agreement with FirstGuard Health Plan, Inc. (FirstGuard), a wholly-owned subsidiary of Centene Corporation. Under this agreement, the Company acquired all FirstGuard members as of February 1, 2007 at a price of \$550 per member. The purchase price was based upon existing FirstGuard membership as of mid-January 2007 as reported by the state of Missouri. The agreement resulted in the acquisition of approximately 26,000 new members.

### **Surplus Debentures**

There are no surplus debentures issued or outstanding.

## **AFFILIATED COMPANIES**

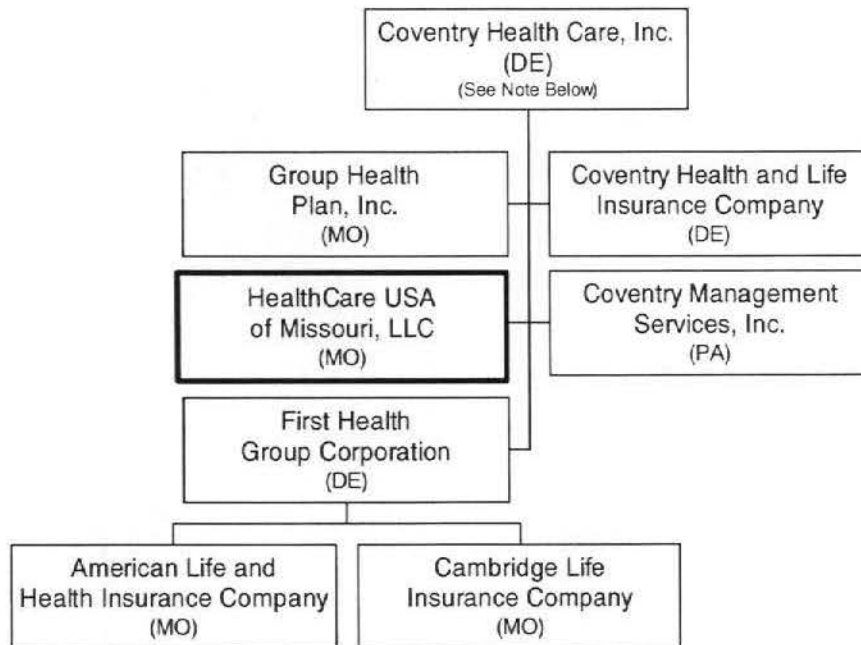
### **Holding Company, Subsidiaries and Affiliates**

The Company is a member of an insurance holding company system as defined by Section 382.010 RSMo (Definitions). The ultimate controlling entity in the insurance holding company system is Coventry Health Care, Inc. (Delaware). Coventry Health Care, Inc. is a publicly traded corporation headquartered in Bethesda, Maryland. The common stock of Coventry Health Care, Inc. trades on the New York stock exchange under the symbol CVH. At December 31, 2007, Janus Capital Management, LLC (Colorado) owned 10.81% of the outstanding shares of Coventry Health Care, Inc. No other entity owned 10% or more of the outstanding shares of Coventry Health Care, Inc. at year-end 2007. The Company filed Insurance Holding Company system Registration Statement Forms B and C with the Department for the years under examination.

### **Organizational Chart**

The following is a portion of the Coventry Health Care, Inc. organizational chart as of December 31, 2007. Only companies directly related to HealthCare USA or those domiciled in Missouri or those with which the Company has a contractual agreement are

included in the organizational chart. All companies are 100% owned by their immediate parent unless otherwise noted.



\*\*\* - At December 31, 2007, Janus Capital Management owned over 10% of Coventry Health Care, Inc., giving it a controlling interest in the company, Janus has filed a disclaimer of affiliation and control with the Missouri Department of Insurance, Financial Institutions and Professional Registration. Janus Capital Management owned 10.81% while other public investors owned 89.19%.

### Affiliated Transactions

#### *Management Services Agreements*

Effective January 1, 2003, the Company entered into an agreement with its parent, Coventry Health Care, Inc. Under the agreement the Company receives the following services: senior management; advertising, marketing and public relations; purchasing; pharmacy; corporate and legal; regulatory compliance and governmental affairs; accounting; tax compliance and consulting; facilities management; risk management; human resources consulting; and payroll. In return for the services provided, the Company pays a per-member-per-month fee. On January 1, 2007, the agreement was amended to increase the per-member-per-month fee from \$2.95 to \$3.15. The Department approved the original agreement on January 30, 2003. The amendment was approved on November 17, 2006.

The Company also entered into an agreement with an affiliate, Coventry Management Services, Inc., a Missouri-licensed Third Party Administrator, effective January 1, 2003. Under this agreement, the Company receives information systems support, including

equipment and services, desktop support, application development, data center support, telecommunications support and network support. The Company also receives service center services including claims processing, premium billing and collection, enrollment and eligibility services, fraud and recovery support, member services and benefit and contract administration. In return for the services provided, the Company pays a per-member-per-month fee. On January 1, 2007 the agreement was amended to change the per-member-per-month fee from \$3.40 to \$4.32 for information systems support and from \$3.50 to \$3.33 for service center services. The Department approved the original agreement on February 3, 2003. The amendment was approved on November 17, 2006.

#### *Guarantor Agreement*

On January 1, 2001, the Company entered into a Guarantor Agreement with its parent, Coventry Health Care, Inc. Under the agreement, Coventry Health Care, Inc. agrees to pay all expenses and claims incurred by the Company in the event of the Company's inability to pay, including any inability resulting from insolvency. Coventry Health Care, Inc. guarantees payments through the end of the Company's Medicaid contract with the state of Missouri.

#### *Tax Allocation Agreement*

The Company is party to a Tax Allocation Agreement among Coventry Health Care, Inc. and its subsidiaries originally effective December 31, 1998. Under the agreement, each affiliate computes its tax liability or refund as if filing a separate return. Intercompany balances are settled within ninety days of the filing of the consolidated return. The Department approved the original agreement on April 27, 1999. On November 30, 2004, the Department approved an amendment to the agreement that clarified the allocation of tax assets and liabilities.

#### *Reinsurance Agreement*

The Company is party to a reinsurance agreement with an affiliate, Coventry Health and Life Insurance Company. This agreement is detailed in the Reinsurance section of this report.

## **FIDELITY BOND AND OTHER INSURANCE**

The Company is a named insured on a \$10,000,000 financial institution bond issued to its ultimate parent, Coventry Health Care, Inc. The amount of coverage meets the suggested minimum amount recommended by the NAIC. The coverage also meets the requirement of Section 354.425 RSMo, Bonding of officers who disburse or invest funds, which stipulates a minimum bond amount of \$100,000.

Section 354.425 RSMo further requires that a bond with a discovery period of less than three years be non-cancellable without ninety days' prior notice to the Department Director. At December 31, 2007, the Company's financial institution bond did not meet this requirement. Effective November 4, 2008 the Company amended its financial institution bond to comply with the requirements of Section 354.425 RSMo, Bonding of officers who disburse or invest funds.



The Company is also a named insured on policies issued to Coventry Health Care, Inc. for the following types of coverage: general liability, automobile liability, professional liability, umbrella liability and workers' compensation. The Company's coverage appears to be adequate.

## **EMPLOYEE BENEFITS**

The Company provides a comprehensive benefit package to eligible employees including paid holidays, vacation, sick leave, bereavement leave, term life insurance, accidental death insurance, short-term disability insurance, long-term disability insurance and tuition assistance. These benefits are provided at no cost to participating employees. The Company also provides medical, dental and vision coverage. Employees pay a portion of the premium to secure coverage for these benefits.

The Company's employees are eligible to participate in the Coventry Health Care Retirement Savings 401(k) plan. Under the terms of this plan, employees can defer up to 75% of eligible compensation on a pre-tax basis. In addition, eligible employees receive matching contributions in Coventry Health Care, Inc. stock equal to 100% of pre-tax contributions (up to the first 3.0% of an employees' compensation). Coventry matches the next 3.0% of an employee's compensation at the rate of 50% on pre-tax contributions. The maximum matching contribution is 4.5% of eligible pay. Matching percentages are subject to change at Coventry's discretion. The Company contributed approximately \$226,000 to this plan during 2007.

Coventry Health Care, Inc. also sponsors a Stock Incentive Plan under which shares of its common stock are authorized for issuance to key employees, consultants and directors in the form of stock options, restricted stock and other stock-based awards. Under the Stock Incentive Plan, the terms and conditions of the awards are established on an individual basis. Awards are made solely at the discretion of the Compensation and Benefits Committee of Coventry Health Care, Inc.'s Board of Directors. The Company recognized no expense related to this plan during 2007.

## **STATUTORY DEPOSITS**

### **Deposits with the State of Missouri**

The funds on deposit with the Missouri Department of Insurance, Financial Institutions and Professional Registration as of December 31, 2007, reflected below, were sufficient in par and market value to meet the deposit requirement for the state of Missouri in accordance with Section 354.410 RSMo (Certificate issued, when—annual deposit required).

<u>Security</u>	<u>Par Value</u>	<u>Book Value</u>	<u>Market Value</u>
US Treasury Note	\$ 350,000	\$ 351,044	\$ 349,965
Kansas City, MO GO Bonds	250,000	250,325	250,390
Totals	<u>\$ 600,000</u>	<u>\$ 601,369</u>	<u>\$ 600,355</u>

## **INSURANCE PRODUCTS AND PRACTICES**

### **Territory and Plan of Operation**

The Company services three regions in the state of Missouri. The Eastern Region consists of the City of St. Louis and eleven surrounding counties. Twenty-eight counties in mid-Missouri, generally around Jefferson City and Columbia, comprise the Central Region. The Western Region consists of thirteen counties around Kansas City.

The Company operates as a Medicaid HMO (health maintenance organization) under Chapter 354 RSMo (Health service corporations, health maintenance organizations and prepaid dental plans). The Missouri Department of Social Services, MO Healthnet Division administers the Medicaid program in Missouri. In 1995 a managed care program was established that requires all Medicaid recipients to enroll in an HMO, if one is available, in order to receive benefits. The MO Healthnet Division provides membership information to the Company each month. The MO Healthnet Division also allocates a portion of new enrollees that did not select a plan to the Company.

### **Marketing**

Guidelines established by the MO Healthnet Division govern the Company's marketing efforts. All marketing materials must be submitted to the MO Healthnet Division for approval before being distributed to prospective enrollees.

### **Provider Contracts**

The Company contracts with various health care providers for the provision of medical services to its enrollees. Primary care physicians in the Eastern Region are compensated on a capitation basis with additional reimbursement for most services. Primary care physicians in the Central and Western Regions are compensated on a fee-for-service basis. Fees paid to physician may exceed, but cannot fall below, the Medicaid established rates.

Hospitals are compensated for inpatient hospitalization costs on a per diem basis using Medicaid per diem rates or rates established under separate contracts between the individual hospital and the Company. Hospital reimbursements may fall below the Medicaid established rates. The Missouri Health Improvement Act of 2007 requires the MO Healthnet Division to achieve parity with Medicare reimbursement rates over a four-year period, contingent upon funding by the Missouri Legislature.

### **Rates**

Rates are established annually through a bidding process. Health plans are invited to bid on Medicaid business and must meet specific minimum requirements mandated in the Medicaid Request for Proposal (RFP). The MO Healthnet Division sets maximum rates that can be charged. Those rates tend to be the benchmark bids. Rates vary depending on age, gender and location of the member.

**Grievance Procedures; Quality Assurance; Utilization Review: Provider Credentialing**

The MO Healthnet Division requires the Company to periodically submit reports related to these areas. The reports for the years under examination were reviewed. The Company appears to have an adequate system in place monitoring grievances.

**REINSURANCE**

Premiums reported during the period under examination were as follows:

	<u>2004</u>	<u>2005</u>	<u>2006</u>	<u>2007</u>
Direct Premiums	\$ 352,095,541	\$ 352,518,263	\$ 332,577,599	\$ 447,738,858
Reinsurance Ceded	<u>8,144,771</u>	<u>8,233,268</u>	<u>7,990,983</u>	<u>10,047,182</u>
Net Premiums Written	<u>\$ 343,950,770</u>	<u>\$ 344,284,995</u>	<u>\$ 324,586,616</u>	<u>\$ 437,691,676</u>

**Ceded**

Effective December 1, 2000, the Company entered into an HMO Excess Risk Reinsurance Agreement with affiliate Coventry Health and Life Insurance Company, a Delaware domestic insurer. This agreement, which was approved by the Missouri Department of Insurance on March 15, 2001, initially covered the Eastern Missouri non-waiver Medicaid members. However, the agreement also began covering the Central Missouri non-waiver members and all of the waiver members on March 1, 2001, and April 1, 2001, respectively.

Under the terms of the reinsurance agreement with Coventry Health and Life Insurance Company, the Company cedes 80% of the eligible charges in excess of \$250,000 per Medicaid Member. Eligible charges include inpatient, physician and outpatient claims. Pharmacy claims and capitation payments are excluded from eligible charges. The maximum reinsurance coverage payable is \$1,000,000. In exchange for this coverage, the Company pays a premium to the reinsurer based on the number of Medicaid members in force each month. On March 26, 2007, the Department approved the Sixth Amendment to the Excess Risk Reinsurance Agreement which increased the rate from \$4.52 per-member-per-month to \$4.93 per-member-per-month.

## ACCOUNTS AND RECORDS

### **General**

The Company maintains its general ledger on PeopleSoft accounting software. Membership data and claims data are maintained on the IDX system.

### **Independent Auditor**

The Company's financial statements are audited annually by Ernst & Young, LLP. The 2007 audit work papers were reviewed and included in the examination to the extent deemed appropriate.

### **Independent Actuary**

The 2007 loss reserves were reviewed and certified by Timothy J. Meyers, FSA, MAAA, Vice-President and Chief Actuary of Coventry Health Care, Inc. The Department retained Karen Elsom, FCAS, MAAA, of Lewis & Ellis, Inc. to opine on the adequacy of the loss reserves and related liabilities. According to the consulting actuary, the year-end 2007 loss reserves and related liabilities were adequately stated.

### **Information Systems**

In conjunction with this examination, Andrew Balas, Information Systems Financial Examiner with the Department, conducted a review of the Company's information systems. No material exceptions were noted.

## FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of the Company as of December 31, 2007 and the results of operations for the year then ended. Any examination adjustments to the amounts reported in the annual statement or comments regarding such are made in the "Notes to the Financial Statements," which follow the Financial Statements. The failure of any column to add to its respective total is due to rounding or truncation.

There may have been additional differences found in the course of this examination which are not shown in the "Notes to the Financial Statements." These differences were determined to be immaterial concerning their effect on the financial statements, and therefore were only communicated to the Company and noted in the workpapers for each individual annual statement item.

## ASSETS

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	\$ 54,059,043	\$ -	\$ 54,059,043
Cash and short-term investments	10,785,761	-	10,785,761
Investment income due and accrued	824,965	-	824,965
Uncollected premiums	42,313,336	-	42,313,336
Amounts recoverable from reinsurers	1,410,247	-	1,410,247
Current federal and foreign income tax recoverable	1,361,214	-	1,361,214
Net deferred tax asset	5,429,045	4,571,194	857,851
Electronic data processing equipment and software	2,095	2,095	-
Furniture and equipment	49,188	49,188	-
Intangible assets and amortization	13,949,253	13,949,253	-
Prepays	141,191	141,191	-
Vehicles and depreciation	38,427	38,427	-
Receivables	1,115	1,115	-
Totals	<u>\$ 130,364,880</u>	<u>\$ 18,752,463</u>	<u>\$ 111,612,417</u>

## LIABILITIES, CAPITAL AND SURPLUS

Claims unpaid	\$ 49,623,324
Unpaid claims adjustment expenses	1,084,732
General expenses due or accrued	3,716,606
Current federal and foreign income tax payable	76
Amounts withheld or retained for the account of others	7,377
Amounts due to parent, subsidiaries and affiliates	1,128,996
Payable for securities	1,072,460
Abandoned property liability	<u>128,479</u>
Total liabilities	\$ 56,762,050
Gross paid in and contributed surplus	\$ 11,042,055
Unassigned funds	<u>43,808,310</u>
Total capital and surplus	\$ 54,850,365
Total liabilities, capital and surplus	<u>\$ 111,612,415</u>

## STATEMENT OF REVENUE AND EXPENSES

Net premium income	\$ 437,691,676
Total revenues	\$ 437,691,676
Hospital and medical benefits	\$ 290,500,503
Emergency room and out-of-area	47,921,168
Prescription drugs	55,789,322
Net reinsurance recoveries	<u>(9,798,651)</u>
Sub-total hospital and medical benefits	\$ 384,412,342
Claims adjustment expenses	7,505,104
General administrative expenses	<u>28,355,918</u>
Total underwriting deductions	\$ 420,273,364
Net underwriting gain	\$ 17,418,312
Net investment income earned	\$ 3,032,675
Net realized capital gains	<u>216</u>
Net investment gains	\$ 3,032,891
Net income (pre-tax)	\$ 20,451,203
Federal income taxes incurred	<u>(4,952,780)</u>
Net income (loss)	<u>\$ 15,498,423</u>

## CAPITAL AND SURPLUS

Capital and surplus, December 31, 2006	\$ 52,262,152
Net income	15,498,423
Change in net deferred income tax	4,698,201
Change in nonadmitted assets	(17,608,411)
Examination changes	<u>-</u>
Net change in capital and surplus	\$ <u>2,588,213</u>
Capital and surplus, December 31, 2007	<u>\$ 54,850,365</u>

**EXAMINATION CHANGES**

None.

**NOTES TO FINANCIAL STATEMENTS**

None.

**GENERAL COMMENTS OR RECOMMENDATIONS**

None.

**SUBSEQUENT EVENTS**

None.



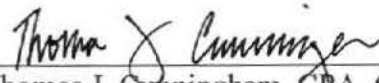
## ACKNOWLEDGEMENT

The assistance and cooperation extended by HealthCare USA of Missouri, LLC during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Arthur Palmer, CFE, Amy Snyder and Andrew T. Balas, CPA, CFE, AES, examiners for the Department of Insurance, Financial Institutions and Professional Registration participated in this examination.

## VERIFICATION

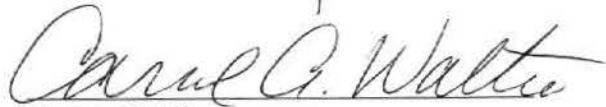
State of Missouri     )  
                                  ) ss  
County of St. Louis    )

I, Thomas J. Cunningham, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of the Company, its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

  
\_\_\_\_\_  
Thomas J. Cunningham, CPA, CFE  
Examiner-in-Charge  
DIFP/Insurance

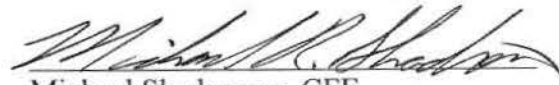
Sworn to and subscribed before me this 25 day of February 2009  
My commission expires:

\_\_\_\_\_

  
\_\_\_\_\_  
Notary Public

## SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting work papers have been reviewed and approved. Compliance with the National Association of Insurance Commissioners procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

  
\_\_\_\_\_  
Michael Shadowens, CFE  
Audit Manager  
DIFP/Insurance

**Carol A. Walter**  
**NOTARY PUBLIC - NOTARY SEAL**  
State of Missouri  
County of Jefferson  
Commission # 06436365  
My Commission Expires 3-26-2010