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Attorneys for Department of Insurance

BEFORE THE DIRECTOR OF THE DEPARTMENT OF INSURANCE

STATE OF IDAHO

In the Matter of:	
BLUE CROSS OF IDAHO HEALTH SERVICE, INC.	**ORDER ADOPTING REPORT OF EXAMINATION AS OF DECEMBER 31, 2008**
Idaho Certificate of Authority: 1900 NAIC Company Code: 60095	Docket No. 18-2630-10

The Report of Examination as of December 31, 2008 (Report) of *Blue Cross of Idaho Health Service, Inc.* (Company), was completed by examiners from the Idaho Department of Insurance (Department) and originally signed the 28th day of May 2010 by the Examiner-in-Charge, Lois Haley, CFE. The original verified (attested) copy of the Report was filed with the Department effective May 28, 2010. Previous to this, a draft copy of the Report was delivered to the Company on May 14, 2010, with the original verified Report being transmitted to the Company electronically (PDF file, via e-mail) on May 28, 2010, to

Mr. Raymond Ralph Flachbart, President & Chief Executive Officer, C/O Mr. Jack Alan Myers, Executive Vice President & CFO. Subsequently, during the 30-day statutory review period prescribed by Idaho Code (see § 41-227(5), I.C.), various modifications, clarifications and/or minor corrections were made to the original verified report. The modified verified Report was filed by the examiner with the Department on June 23, 2010, and delivered electronically on June 25, 2010, to Mr. Jack Alan Myers, Executive Vice President & CFO, C/O Ms. Carol Mulder, Senior Statutory Accountant, and is attached hereto and incorporated herein as Exhibit A.

WAIVER

Attached hereto and incorporated herein as Exhibit B is a Waiver signed by Mr. Myers on June 25, 2010 and hand-delivered to the Department on June 25, 2010. Based upon the Waiver/Exhibit B, this is a final order, and the Company has waived its rights to seek reconsideration and judicial review of this order.

WRITTEN SUBMISSION

The Company made a written submission from Mr. Myers, as provided for under § 41-227(5), Idaho Code, containing responses to the examination report, in the form of a letter dated and hand-delivered to the Department as of June 25, 2010. The Company requested that the written submission become a public record of the Department. This written submission is incorporated herein as Exhibit C.

ORDER

NOW THEREFORE, after carefully reviewing the above-described Report of Examination attached hereto as Exhibit A and the written submission incorporated herein as Exhibit C, and good cause appearing therefor, it is hereby ordered that the above described Report, which includes the findings, conclusions, comments and recommendations

supporting this order, is hereby ADOPTED as the final examination report and as an official record of the Department under Idaho Code § 41-227(5)(a).

DATED and EFFECTIVE at Boise, Idaho, this 29th day of June 2010.

William W. Deal, Director
IDAHO DEPARTMENT OF INSURANCE

CERTIFICATE OF SERVICE

I hereby certify that on this 29th day of June, 2010, I caused to be served the foregoing document on the following parties in the manner set forth below:

Mr. Raymond Ralph Flachbart, President & CEO Blue Cross of Idaho Health Service, Inc. 3000 E Pine Avenue Meridian, Idaho 83642	X 	certified mail first class mail hand delivery Facsimile e-mail
Mr. Jack Alan Myers, Executive VP & CFO Blue Cross of Idaho Health Service, Inc. 3000 E Pine Avenue Meridian, Idaho 83642 JMyers@bcidaho.com	 X X	certified mail first class mail hand delivery Facsimile e-mail
Georgia Siehl, CPA, CFE Bureau Chief / Chief Examiner Idaho Department of Insurance 700 W. State St., 3rd Floor Boise, Idaho 83720-0043 Georgia.Siehl@doi.idaho.gov	 X X	certified mail first class mail hand delivery facsimile e-mail

William R. Michels, MBA, CPA, CFE
Deputy Chief Examiner
IDAHO DEPARTMENT OF INSURANCE

EXHIBIT A

DEPARTMENT OF INSURANCE

STATE OF IDAHO

REPORT OF EXAMINATION

of

BLUE CROSS OF IDAHO HEALTH SERVICE, INC.
(a mutual insurance company)

as of

December 31, 2008

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State of Idaho
DEPARTMENT OF INSURANCE

C. L. "BUTCH" OTTER
Governor

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Phone (208)334-4250
FAX # (208)334-4398

WILLIAM W. DEAL
Director

Meridian, Idaho
June 23, 2010

The Honorable William W. Deal
Director of Insurance
State of Idaho
700 West State Street
P. O. Box 83720
Boise, Idaho 83720-0043

Dear Director:

Pursuant to your instructions, in compliance with Section 41-219(1), Idaho Code, 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, 2008, of the financial condition and corporate affairs of:

Blue Cross of Idaho Health Service, Inc.
3000 East Pine Avenue
Meridian, Idaho 83642

hereinafter referred to as the "Company," at its offices in Meridian, Idaho. The following Report of Examination is respectfully submitted.

SCOPE OF EXAMINATION

This examination covered the period January 1, 2005, through December 31, 2008. The examination was conducted at the Meridian, Idaho office of the Company by examiners from the State of Idaho. The examination was conducted in accordance with Section 41-219(1), Idaho Code, the National Association of Insurance Commissioners (NAIC) *Financial Condition Examiners Handbook*, the NAIC *Accounting Practices and Procedures Manual*, and the NAIC *Market Regulation Handbook*.

All accounts and activities of the Company were considered in accordance with the NAIC's risk-focused examination process. The *Financial Condition Examiners Handbook* requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. An examination also includes assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and NAIC Annual Statement instructions as governed and prescribed by Idaho law.

A Letter of Representation was signed by the Company attesting to its ownership of all assets and to the nonexistence of unrecorded liabilities or contingent liabilities.

The actuarial review of reserves, related liabilities, and other actuarial items was performed by Lewis & Ellis, Inc., consulting actuaries, for the Idaho Department of Insurance. A risk assessment review of the Company's information technology systems and controls was performed by Examination Resources, LLC. There was some reliance placed on the 2008 Certified Public Accountants' statutory audit report and workpapers during the examination of the Company.

In addition to the Report of Examination, a Management Letter was issued to the Company by the Department which covered items that were not included in the Report, due to the materiality threshold, items that were related to proprietary/operational issues, as well as minor accounting and/or annual statement reporting corrections.

PRIOR EXAMINATION

The prior financial examination was conducted by the Idaho Department of Insurance covering the period January 1, 2000 through December 31, 2004.

A review was made to ascertain what action was taken by the Company with regard to comments and recommendations made by the Department in the prior examination report. Unless otherwise mentioned in the *Comments and Recommendations* section of this report, the prior report exceptions were adequately addressed by the Company.

HISTORY AND DESCRIPTION

General

The Company was formed as a non-profit entity on December 31, 1977. Its incorporation and formation was the result of a consolidation of Blue Cross of Idaho, Inc. and South Idaho Medical Service Bureau, Inc., who had maintained separate operations in Idaho since 1945 and 1962, respectively. The Company was formed under Title 41, Chapter 34, Idaho Code, and operated as a hospital and professional service corporation. In 1995, the Company converted to a nonprofit mutual insurer under Title 41, Chapter 28, Idaho Code.

Beginning in 1987, the Company became subject to Federal income taxes. Prior thereto it had been exempt under Section 501(c)(4), Internal Revenue Code.

Prior to the Company's mutualization, it was exempt from Idaho State premium taxes, state corporation taxes, and participation in the Life and Health Guaranty Association. State taxation in lieu of Idaho premium taxes was provided under Section 41-3427, Idaho Code, which required assessment of four cents per subscriber contract per month.

A certificate of authority was issued to Idaho Preferred Healthcare, the Company's managed care line of business, on September 4, 1990.

As a result of mutulization in 1995, the Company's lines of business, with the exception of its administrative service contract business, are no longer exempt from Idaho premium taxes and participation in the Life and Health Guaranty Association. In addition, the Company's Annual Statement reporting form was changed from a hospital, medical, dental and indemnity form to a Life, Accident and Health blank.

Beginning in 1994, the Company's managed care line of business, Idaho Preferred Healthcare, was no longer required to file a separate annual statement. Idaho Preferred Healthcare's line of business was to be reported in the Company's annual statement separately as to premium income, claims, administrative expenses and enrollment in the same manner as required for the other lines of business. Idaho Preferred Healthcare was reported in the Company's 1994 and 1995 annual statements.

The Department notified the Company in a letter dated March 12, 1996 that, effective with the quarterly statement as of March 31, 1996, Idaho Preferred Healthcare was to begin filing separate statements. Although Idaho Preferred Healthcare did not operate as a separate legal entity, it was required to file a separate statement, since it operated under a separate certificate of authority and its business and operations were clearly distinguishable from the other types of insurance offered by the Company.

In August 1996, the name of Idaho Preferred Healthcare was changed to Blue Cross of Idaho Coordinated Care Services. As noted in the preceding paragraph, Blue Cross of

Idaho Coordinated Care Services was not a corporation or legal entity, but was operated concurrently with the operations of the Company and was considered a separate and distinct division within the Company, in accordance with Section 41-3406 (4), Idaho Code.

Effective February 11, 1999, Health Ventures Corporation received its certificate of authority to operate as a managed care organization under Title 41, Chapter 39, Idaho Code. Prior to this, Health Ventures Corporation was incorporated as a third party administrator for the Company's Medicare managed care line of business, which was written by Blue Cross of Idaho Coordinated Care Services. Health Ventures Corporation changed to an insurer on February 11, 1999 and effective that date became the 100 percent reinsurer of the Blue Cross of Idaho Coordinated Care Services' group managed care and Medicare Choice lines of business. Health Ventures Corporation was owned equally by the Company and St. Luke's Regional Medical Center. Health Ventures Corporation owned 50 percent of Triad Limited Liability Company while Eastern Idaho IPA, PLLC owned the remaining 50 percent.

On January 1, 2000, Blue Cross of Idaho Coordinated Care Services voluntarily surrendered its certificate of authority and ceased writing business. Consequently, Blue Cross of Idaho Coordinated Care Services' assets, liabilities, equity, and all managed care products were absorbed within the Company. The Company's Certificate of Authority was re-issued on January 3, 2000 to include managed care business.

Health Ventures Corporation executed surplus note agreements with the Company and St. Luke's Regional Medical Center on June 29, 2000. During 2000, surplus notes in the amount of $3,250,000 each were issued to the Company and to St. Luke's.

In December 2001, the Company acquired St. Luke's Regional Medical Center's interest in Health Ventures Corporation for $7,000,000 in cash in exchange for St. Luke's shares and surplus notes receivable of $3,250,000. The Board of Directors authorized the transaction on November 30, 2001. The Plan of Dissolution was submitted to the Idaho Department of Insurance and in a letter dated December 27, 2001, the Department indicated it had no objections to the acquisition. Pursuant to the Plan, Health Ventures Corporation was dissolved on February 26, 2002 and voluntarily surrendered its certificate of authority on February 28, 2002. Health Ventures Corporation's share of Triad Limited Liability Company was transferred to the Company. The surplus notes issued to St. Luke's were surrendered and the Company became the owner of Health Ventures' assets and liabilities.

Blue Cross of Idaho Foundation for Health, Inc. was incorporated as a non-profit entity on December 28, 2001. The Board of Directors approved the establishment of the Foundation on November 13, 2001. The purpose of the foundation was to promote health improvement initiatives to Idaho residents.

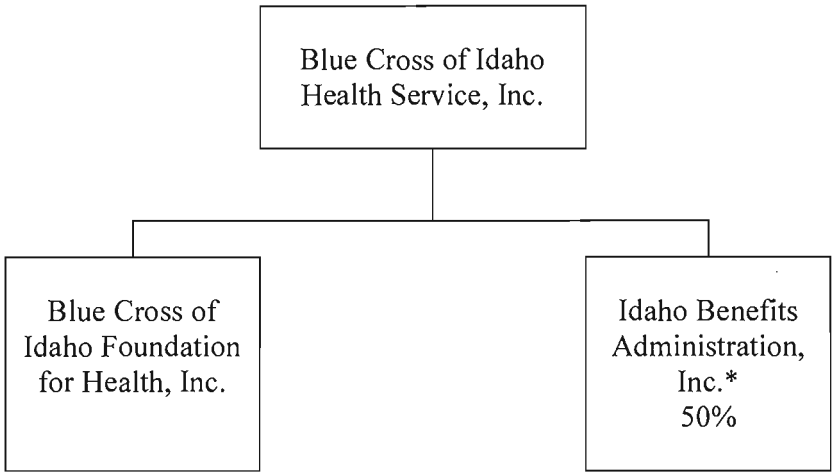
The Company changed its reporting format from the NAIC Life, Accident and Health blank to the Health blank effective January 1, 2004.

The Company is a member of the Blue Cross and Blue Shield Association. The Association serves as a national non-affiliated advisory organization for all Blue Cross and Blue Shield Plans in the United States.

MANAGEMENT AND CONTROL

Insurance Holding Company System

The Company is a member of an insurance holding company system and is the ultimate controlling person, as depicted in the following organizational chart:



*WellPoint Health Networks, Inc. owns 50 percent of Idaho Benefits Administration, Inc.

The Company received an exemption from the Department on filing a Holding Company Registration Statement, which would have included the Blue Cross of Idaho Foundation for Health, Inc. The exemption was granted under Section 41-3806(10), Idaho Code due to the immateriality of Idaho Benefits Administration and Blue Cross of Idaho Foundation for Health, Inc.

Idaho Benefits Administration, Inc. is a joint venture with WellPoint Health Networks, Inc., which owns the other 50 percent of Idaho Benefits. The Company contracts with Idaho Benefits Administration, Inc., a third party administrator, for administrative services for its dental and pharmaceutical products. Subsequent to the examination date, Express Scripts, Inc. acquired WellPoint's pharmacy benefits management business.

As previously reported, the Board of Directors established the Blue Cross of Idaho Foundation for Health, Inc. in 2001. The purpose of the foundation is to promote health improvement initiatives to Idaho residents. The Company donated $2,400,000 to the Foundation during the year ended December 31, 2008.

The Company acquired 6 percent of WPMI, LLC, a joint venture with three other Blue Cross Blue Shield plans for the purpose of providing third party administrative services and health insurance products in China. The Company invested approximately $1,285,000 and $1,200,000 during 2008 and 2007, respectively to the venture. The Company reports this investment in Schedule BA – Other Invested Assets and is non-admitted per instructions from the Idaho Department of Insurance.

During 2008, the Company purchased 2.56 percent of BlueCross BlueShield Ventures, a joint venture with several other Blue Cross Blue Shield Plans for the purpose of providing a structure to gain access to innovative companies and achieve significant strategic insights and returns in the healthcare insurance industry related to new ventures. The Company invested $30,000 in common stock that is reported on Schedule D and $172,414 in a private equity fund that is reported on Schedule BA. Both investments are non-admitted per instructions from the Department.

Directors

The Company is a mutual organization with each policyholder being a member of the corporation. The members annually elect Company directors to three-year terms. The directors' terms are arranged so that approximately one-third of the terms expire annually.

The Company is governed by its Board of Directors, which consists of a maximum of 17 and a minimum of 5 directors, including the President as an ex offico director. The number of directors is in compliance with Section 41-2835(5), Idaho Code, which requires not less than 5 nor more than 25 directors. Pursuant to the Company's amended By-laws effective May 1, 2008, the Company has three types of directors: at least one physician director, at least one hospital director, with the remaining majority being public directors.

The following persons are the duly elected or ex officio members of the Board of Directors at December 31, 2008:

Name	Principal Occupation
Physician Directors:	
Micheal John Adcox, M.D.	Nephrologist
Samuel Milton Summers, M.D.	Family Practice
Hospital Directors:	
Joseph Edward Morris III	Chief Executive Officer, Kootenai Medical Center
Public Directors:	
Raymond Ralph Flachbart	President & Chief Executive Officer, Blue Cross of Idaho Health Service, Inc.
Jack Wynn Gustavel	Chairman & Chief Executive Officer, Idaho Independent Bank
Norman Charles Hedemark	Retired, Executive Vice President, Chief Operating Officer, Intermountain Gas
Kenlon Porter Johnson	President, Forde Johnson Oil Company, Inc.
Ward Douglas Parkinson	Director, Ovonyx, Inc.
Michael James Shirley	President & General Manager, Bogus Basin Mountain Recreation Area
Jo Anne Stringfield	Consultant

Subsequent to the examination date, Steven Lee Goddard, President and Chief Executive Officer, WinCo Foods and Thomas Frederick Kealey, President, Silver Creek Holding Company, were elected to the Board of Directors as public directors. Sally E. Jeffcoat, President and Chief Executive Officer, Saint Alphonsus Regional Medical Center and David C. Pate, M.D., President and Chief Executive Officer, St. Luke's Health System, were elected to the Board of Directors as hospital directors.

Officers:

The following persons were serving as officers of the Board of Directors at December 31, 2008:

Jack Wynn Gustavel	Chair of the Board
Michael James Shirley	Vice Chair of the Board
Norman Charles Hedemark	Secretary-Treasurer

Subsequent to the examination date, the Board positions of Corporate Secretary and Corporate Treasurer became corporate officer positions held by and Steven John Tobiason and Jack Alan Myers, respectively.

The Company's daily operations are managed by the Executive Staff named below.

Executive Staff

Raymond Ralph Flachbart	President & Chief Executive Officer
Jack Alan Myers	Executive Vice President & Chief Financial Officer
Zelda Geyer-Sylvia	Executive Vice President & Chief Operating Officer
David James Hutchins	Vice President, Actuarial Services & Underwriting
Steven John Tobiason	Senior Vice President, Legal Services & Government Affairs
Lance Clifford Hatfield	Vice President, Information Services & Chief Information Officer
Douglas William Dammrose, M.D.	Senior Vice President, Medical Director
Drew Shelton Forney	Vice President, Benefits Management & Member Services
Debra Marie Henry	Vice President, Human Resource & Administrative Services
Jerome Anthony Dworak	Senior Vice President, Chief Marketing Officer

The executives named above are responsible for the operations of a division within the Company. Division directors were responsible for the various departmental operations and are members of the Company's Management Advisory Committee. This Committee meets on a regular basis to discuss operations, benefit and personnel policies and makes recommendations to the Executive Staff.

Committees:

The By-laws provide for an Executive Committee of the Board of Directors composed of the Chair of the Board, Vice Chair and the Secretary. One or more other members of the Board shall also be appointed. In addition, the President of the Company is an ex officio member of the Executive Committee.

The Company's By-laws also provide for a Nominating Committee (subsequently re-named Governance and Nominating Committee) and various Board committees. The committees operate under Statements of Purpose and Organization, which set forth the purpose of each committee, responsibilities, duties, eligibility, appointment, and meetings.

Directors appointed to the Board committees at year-end 2008, as well as staff advisors, are shown below.

Executive Committee

Jack Wynn Gustavel	Chair
Michael James Shirley	Vice Chair
Micheal John Adcox, M.D.	
Norman Charles Hedemark	
Raymond Ralph Flachbart	Ex Officio

Audit Committee

Norman Charles Hedemark	Chairman
Jack Wynn Gustavel	
Kenlon Porter Johnson	
Joseph Edward Morris III	
Jo Anne Stringfield	
Jack Alan Myers	Staff

Compensation and Benefits Committee

Norman Charles Hedemark	Chair
Jack Wynn Gustavel	
Ward Douglas Parkinson	
Michael James Shirley	
Jo Anne Stringfield	
Samuel Milton Summers, M.D.	
Raymond Ralph Flachbart	Staff

Finance Committee

Michael James Shirley	Chair
Kenlon Porter Johnson	
Jack Wynn Gustavel	Ex Officio
Raymond Ralph Flachbart	Ex Officio
Jack Alan Myers	Staff

Governance and Nominating Committee

Jo Anne Stringfield	Chair
Micheal John Adcox, M.D.	
Jack Wynn Gustavel	
Ward Douglas Parkinson	
Raymond Ralph Flachbart	Staff

Quality Committee

Joseph Edward Morris III	Co-Chair
Samuel Milton Summers, M.D.	Co-Chair
Micheal John Adcox, M.D.	
Kenlon Porter Johnson	
Raymond Ralph Flachbart	Ex Officio
Douglas William Dammrose, M.D.	Ex Officio
Zelda Geyer-Sylvia	Staff

In addition to the foregoing Board committees, the Company also maintains various internal committees, such as the IT Steering Committee.

Corporate Governance

A review of the Company's corporate governance structure and the "tone at the top" was performed in compliance with the NAIC's risk-focused examination standards. This review included an evaluation of the Company's organizational structure and assessments of the Board of Directors and Company management. Overall, the Company has a sound organizational structure in place, with an open and ethical culture. The review determined that the Board of Directors utilized independent judgment and evaluation in their decision making and oversight functions. The Board also met the duty of care and loyalty standards in fulfilling their corporate obligations. An assessment of Company management indicated a competent management team that was experienced, stable, and conservative in their business practices.

Conflict of Interest

The Company has a conflict of interest policy in place that requires the directors, corporate officers, managers, supervisors, administrative assistants and employees in designated sensitive areas to disclose annually, on a prescribed written form, any outside personal interests, activities or affiliations that conflicted or may potentially conflict with their official duties with the Company.

Conflict of interest statements that were completed for the period January 1, 2005, through December 31, 2008 appeared to appropriately disclose any actual or possible conflicts of interest. The Company has established processes for addressing and mitigating any conflicts of interest, which includes reviews by the Company's General Counsel and Corporate Compliance Officer or Manager. Furthermore, summaries of conflicts of interest reported by Company employees are submitted to the Board of Directors for their review.

Contracts and Agreements:

The Company had the following agreements in effect at December 31, 2008.

Vision Care Subscriber Agreement

The Company entered into a Vision Care Subscriber Agreement with Idaho Vision Services, dba as Vision Service Plan. Idaho Vision Services, Inc. is the former name of Vision Service Plan of Idaho, Inc. The agreement provided for Vision Service Plan to arrange and provide covered services as described therein and as described in the Company's group contracts and certificates. Vision Service Plan is a prepaid program and covered services are provided at no out-of-pocket cost, other than the insured's copayment. Vision Service Plan pays the member doctor directly for covered services. A member may elect to obtain covered services from any licensed optometrist, ophthalmologist, or optician. Vision Service Plan reimbursed the member for covered

services pursuant to the agreement. For this service the Company paid Vision Service Plan scheduled amounts also set forth in the agreement.

The agreement was effective February 1, 1993 for a two year period, continuing thereafter until terminated with 60 days written notice. The Vision Care Subscriber Agreement was amended effective June 24, 2003 to comply with the requirements of the Health Insurance Portability and Accountability Act of 1996 and its implementing regulations (45 C.F.R. Parts 160-64).

Subsequent to the examination date, a new vision care agreement was executed with Vision Service Plan of Idaho, Inc., effective January 1, 2009.

Vision Service Plan of Idaho, Inc. is licensed in Idaho as a hospital and professional services company; and therefore, meets the requirements of Section 41-901(3), Idaho Code.

Development and Management Agreement and Administrative Services Agreement

Effective March 31, 1997, the Company entered into a Development and Management Agreement with Idaho Benefits Administration, Inc., a related party, and WellPoint Health Networks Inc. The agreement provided that Idaho Benefits Administration, Inc. (i) develop a national accounts program for the benefit of WellPoint Health Networks Inc. and the Company, (ii) develop a dental program to be offered by the Company, (iii) provide comprehensive management services to the Company regarding the dental program, and (iv) carry out other benefit coverage, management and administrative services arrangements. Idaho Benefits Administration, Inc. was supported in the management of the dental program by WellPoint Health Networks Inc. pursuant to the terms of an Administrative Services Agreement between WellPoint Health Networks Inc. and Idaho Benefits Administration, Inc.

The management services provided by Idaho Benefits Administration, Inc. included the following:

- assistance in development of premium rates and underwriting standards for the dental program.
- provision of support to the sales and marketing staff of the Company, who are responsible for the dental products.
- assistance in the preparation of appropriate financial and regulatory reports.
- agreed-upon system support.

The Company was responsible for the billing and collection of premiums attributed to the dental program, except for national accounts serviced by WellPoint Health Networks Inc. The original agreement provided for Idaho Benefits Administration, Inc. to settle claims. Compensation was on a per member per month basis for the use of WellPoint's claims processing system, plus administration costs.

The Development and Management Agreement and the Administrative Services Agreement were amended effective January 1, 2003 whereby the following management services previously provided were deleted:

- assistance in enrollment of members into the BCI dental program.
- administration of claims and customer service function and grievance process applicable to the dental program.
- utilization management relating to the dental program, including assistance in development of policies and procedures.

The agreement with Idaho Benefits Administration and WellPoint Health Networks Inc. was amended effective October 8, 2003 to comply with the requirements of the Health Insurance Portability and Accountability Act of 1996 and its implementing regulations (45 C.F.R. Parts 160-64).

WellPoint Inc. is a licensed third party administrator in compliance with Section 41-913(1), Idaho Code.

Pharmacy Benefit Management Services Agreement

Effective January 1, 1999, the Company entered into a Pharmacy Benefit Management Services Agreement with WellPoint Pharmacy Management Inc.; whereby, WellPoint Pharmacy Management Inc. provided clinical pharmacy management, claims processing, and pharmacy network management services to the Company. For these services, the Company paid WellPoint Pharmacy Management Inc. the cost of the claim, an administration fee, plus the cost of using ReViewPoint® software. The administrative fee was based on a per claim processing fee, a clinical services fee based on per member per month, plus a retention and a flat monthly fee for usage of ReViewPoint® software.

The agreement between the Company and WellPoint Pharmacy Management Inc. was amended effective February 21, 2003 to comply with the requirements of the Health Insurance Portability and Accountability Act of 1996 and its implementing regulations (45 C.F.R. Parts 160-64). The term of the agreement was extended to November 1, 2007 by an amendment effective September 21, 2004.

The Company entered into a new Pharmacy Benefit Management Services Agreement with NextRx Services, Inc., formerly known as Professional Claim Services, Inc. dba WellPoint Pharmacy Management, Inc., for the purposes of providing certain pharmacy benefit management services to the Company. The initial term of the agreement was October 1, 2007 through September 30, 2012, with automatic annual renewals following the initial five year period unless terminated by either party with 180 days written notice. Pricing under the contract will remain in effect for four years and will be open to re-negotiation in the fourth year.

Under this agreement NextRx Services, Inc. provides prescription drug program services, which include clinical pharmacy management, claims processing, formulary

management, manufacturer discount management, and pharmacy network management services, among other things. In addition, NextRx Services, Inc. shall maintain a disaster recovery plan and business contingency plan. The Company pays a management fee for services provided under the contract. Additional services may be performed for additional fees. The agreement also includes pharmacy reimbursement rates and performance guarantees.

The agreement may be terminated by either party for any reason or for no reason with 90 days written notice to the other party after the end of the initial term. Provisions for early termination, breach of contract or for other reasons are contained within the agreement. If the agreement is terminated during the initial term for reasons other than for cause, the parties shall pay an early termination fee. Notice of early termination shall be provided in writing 90 days in advance of the termination date. The agreement may also be terminated as otherwise specifically provided for therein.

The agreement was amended effective January 1, 2008 to reflect the acquisition of WellPoint Pharmacy Management, Inc. by NextRx Services, Inc. The agreement was amended June 29, 2008 to add RxHub e-Prescribing Services to the scope of services provided under the agreement.

NextRx Services, Inc. was also engaged by the Company to perform pharmacy benefit management services for its Medicare Part D benefit plans. In this connection, an addendum for Medicare Part D was added to the Pharmacy Benefit Management Services Agreement effective January 1, 2008.

The initial term of the addendum is January 1, 2008 through December 31, 2012, with automatic renewals annually thereafter unless terminated by either party. In addition to the termination rights in the Pharmacy Benefit Management Services Agreement discussed above, in the event the Centers for Medicare and Medicaid Services (CMS) contract with the Company is terminated or expires, the addendum will terminate concurrently with the termination and/or expiration of the CMS contract.

The addendum was amended June 1, 2009 to add a Special Needs Program to NextRx Service, Inc.'s scope of services provided to the Company.

As previously reported, Express Scripts, Inc. acquired WellPoint's pharmacy benefits management business subsequent to the examination date.

Indemnification Agreements

In 2004, the Company's Board of Directors entered into Indemnification Agreements with the Company. Under the agreements, the Company agreed to hold harmless and indemnify the Directors to the full extent authorized or permitted by law, the Company's articles of incorporation, or its bylaws and against all liability incurred in connection with any claim of the Company.

The agreements are continuous during the period the Director is a director of the Company and shall continue thereafter so long as the Director is subject to any possible threatened, pending, or completed action, suit or proceeding, arising out of or related to the fact that the Director is or was director, officer, fiduciary, employee or agent of the Company. On April 25, 2003, the Board of Directors approved the Corporate Resolution authorizing the President and Chief Executive Officer of the Company to enter into the Indemnification Agreements with Directors and senior executives.

At their meeting of October 20, 2003, the Board authorized management to modify the Board Indemnification Agreement to be suitable for physicians who serve on committees at the Company's request.

Service Agreement

During the examination period, the Company executed a service agreement with Blue Cross Blue Shield of South Carolina. Under the agreement, Blue Cross Blue Shield of South Carolina provides the Company with electronic transaction processing services conducted through the Inter-Plan Teleprocessing System (ITS). The ITS was established by the Blue Cross and Blue Shield Association in support of inter-plan health care transactions of Blue Plans' members (process health insurance claims between Home Plans and Host Plans). The agreement covered the initial implementation service as well as ongoing production services. The agreement also contains a compensation schedule and a Service Level Agreement which sets forth service and performance standards.

The service agreement was effective July 1, 2005 for a three year period, to continue on a year-to-year basis thereafter. After the initial term, either party may terminate the agreement upon 180 days notice prior to the anniversary date. Either party may terminate the agreement upon 30 days written notice for the other's uncured material breach.

State of Idaho Department of Health and Welfare

During the examination period, the Company entered into a contract with the State of Idaho Department of Health and Welfare to administer the State's dental insurance plan for Medicaid enrollees, otherwise known as "Idaho Smiles".

Under the contract, the Company provides insurance coverage by maintaining a statewide network of qualified and licensed dental care providers to eligible Idaho Medicaid participants. In addition, the Company is responsible for processing and paying claims for all covered dental benefits provided to eligible participants for whom the Company is paid a premium (fixed fee).

The Company is paid a fixed fee per eligible participant per month. The per participant per month fees paid to the Company must be inclusive of all services in the contract. From this fixed fee, specific dollar amounts are allocated to administrative costs and to provider costs. The administrative cost portion is fixed for the first five years of the agreement, and then negotiated annually thereafter. The portion allocated to provider

costs is adjusted annually by a percentage determined by Health and Welfare. The Company must increase the dental provider's reimbursements by at least this percentage adjustment.

The contract dates are from April 19, 2007 through April 18, 2012. The parties may cancel the contract at any time with or without cause upon 180 days written notice specifying the date of termination. The contract may also be terminated immediately due to causes specified therein. After the fifth year of the contract, upon mutual agreement, the parties may renew the contract at one year intervals under the same terms and conditions.

Administrative Services Agreement

In connection to the contract with the Department of Health and Welfare, the Company entered into an administrative services agreement with Dentaquest LLC (formerly Doral Dental USA, LLC), Mequon, Wisconsin. Under this agreement, the Company transmits 100 percent of the fixed fee per eligible participant per month it receives from Health and Welfare, less a per contract administrative fee and amounts for premium taxes. Under the risk share arrangement contained within the administrative services agreement, Dentaquest will pay the Company a certain percentage of any positive variance in claims. Dentaquest's primary duty under the contract is to process claims for covered services subject to the Company's oversight, auditing, and monitoring. Dentaquest shall also arrange for participating providers to submit claims to itself for covered services. Claims are paid in accordance with the terms and conditions of the provider agreements and the agreement between the Company and Dentaquest LLC.

This agreement went into effect on the effective date of the Company's contract with Health and Welfare and continues through the term of that contract and subsequent renewals unless terminated or unless the Health and Welfare contract is either terminated or put out to bid. In such case, the Company shall provide Dentaquest with written notice.

The Company treated the accounting transactions under the administrative service agreement with Dentaquest as if it were reinsurance. Based on a review of the administrative service agreement and related transactions, it is the Department's opinion that this agreement is an administrative services agreement only, not a reinsurance contract. Pursuant to Section 41-510, Idaho Code, reinsurance is a contract under which an originating insurer (the Company) procures insurance for itself in another insurer with respect to part or all of an insurance risk of the originating insurer. Dentaquest LLC is not licensed as an insurer or reinsurer. Therefore, the contract and related accounting should not have been treated as reinsurance.

The Company has indicated that it will record all revenues received and claims incurred for the dental insurance coverage with the State of Idaho's Department of Health and Welfare in 2010. Any transactions that the Company has with Dentaquest LLC would be separately recorded based on the nature of the transaction, since the

administrative services agreement would not be considered a reinsurance agreement. See Note 2 to the Financial Statements for additional comments.

CORPORATE RECORDS

Articles of Incorporation and By-laws

The Company's Articles of Incorporation were not amended during the examination period. However, subsequent to the examination date, the Board of Directors approved the Company's amended and restated Articles of Incorporation on February 12, 2010. Policyholders of the Company approved the amended and restated Articles of Incorporation at the Annual Policyholders' Meeting held on April 30, 2010.

The Company's By-laws were amended once during the examination period. The Board of Directors adopted such changes at their meeting held on February 8, 2008. These amended and restated By-laws, effective May 1, 2008, were submitted to the Idaho Department of Insurance pursuant to Section 41-2830(3), Idaho Code. In a letter to the Company dated April 23, 2008, the Department indicated the amended and restated By-laws were accepted as filed.

Subsequent to the examination date, the Company's By-laws were re-written to separate Board leadership positions from corporate officer positions. Specifically, the amendments eliminated the Secretary/Treasurer of the Board position and set forth the corporate officer positions of Secretary and Treasurer. Additionally, the By-laws were amended to conform to the Company's policies on director independence, to reinforce the Board's oversight and leadership role versus corporate management, and to simplify the By-laws. The proposed By-law amendments were initially adopted by the Board of Directors on February 6, 2009, subject to approval by the Idaho Department of Insurance. Based on additional changes, the By-laws were again adopted on November 6, 2009, also subject to the Department's approval. The Department made suggested changes which were incorporated into the By-laws subsequently approved by the Board of Directors on February 12, 2010.

Minutes of Meetings

A review of the minutes of the meetings of the Policyholders, the Board of Directors, and the various committees for the period January 1, 2005 through December 31, 2008 and subsequent thereto, indicated compliance with the Company's Articles of Incorporation and By-laws with respect to the election of the Board of Directors and Officers, and the election or appointment of Committee members.

This review of the minutes also indicated that a quorum was present at all Board of Directors' meetings held during the examination period and that significant Company transactions and events were properly authorized.

Investment transactions were approved by the Finance Committee, which is charged by the Board of Directors with the duty of making investment transactions, in compliance with Section 41-704, Idaho Code. Furthermore, the Company maintained records of its investments in conformity with Section 41-705, Idaho Code.

The external auditors presented the audited financial statements and required communications to the Company's Audit Committee as required by IDAPA 18.01.62.021.06.

The minutes of the Board of Directors' meeting held on July 29, 2006 indicated that all Board members present signed affidavits confirming they had received a copy of the Examination Report as of December 31, 2004, conducted by the Idaho Department of Insurance.

FIDELITY BOND AND OTHER INSURANCE

Insurance coverage in force as of December 31, 2008 included a financial institutional bond, which covered losses resulting from dishonest or fraudulent acts committed by employees up to $1.5 million per single loss. The deductible was $50,000 per single loss. This coverage was increased to $1.75 million effective August 5, 2009. The financial institutional bond insurance coverage met the suggested minimum limits recommended by the NAIC *Financial Condition Examiners Handbook.*

Other insurance maintained by the Company included director and officers liability; errors and omissions liability; employment practice liability; commercial property; general liability; business automobile; umbrella excess liability; workers compensation and employers liability coverages.

The insurance carriers providing coverages to the Company were licensed or otherwise authorized in the State of Idaho.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

Defined Benefit Plan

The Company participated in a noncontributory defined benefit retirement program administered by the Blue Cross and Blue Shield Association National Employee Benefit Administration covering substantially all of its employees hired before January 1, 2007. Employees hired on or after January 1, 2007 are not eligible to participate in the defined benefit retirement program, but may receive an enhanced benefit of an additional 2.5 percent annual Company contribution to their 401(k) Plan. Benefits were based on years of service and employees' final coverage compensation. The Company's contribution to the 401(k) Plan for the enhanced benefit was approximately $173,500 for the year ended December 31, 2008. The Company accrued benefits in

accordance with actuarially determined amounts. The Company contributed $9.5 million to the defined benefit retirement program in 2008.

Deferred Compensation 401(k) Plan

The Company had a 401(k) salary deferral plan that covered all employees who have attained age 18. The Company made matching contributions equal to 100 percent of the employee's deferral up to 3 percent of the employee's annual salary and 50 percent of the employee's additional deferrals up to 5 percent of the employee's annual salary. The Company's matching contributions were approximately $1,454,000 in 2008.

Postretirement Benefit Plans

The Company also provided health and life insurance benefits for retired employees and health insurance to their eligible dependents. These benefits were provided once the employee became eligible by satisfying plan provisions including certain age and/or service and participation requirements. Employees hired on or after March 1, 2003 were not eligible to participate in the Company's retiree health and life plans. Participants in the plans were required to contribute 10 percent to 100 percent of the premiums. The Company's postretirement benefit plans, other than pension plans, were not funded.

Employee Insurance Plans

The Company provides a non-contributory long term disability program for regular full-time and eligible part-time employees. The Company also provides a group health care, dental and vision plan for which the employee contributes part of the premium. Group life and accidental death and dismemberment coverages were provided for which the employee contributed part of the premium. Additional voluntary group accidental death coverage and group universal life plans were also made available to the employees at their own expense.

A flexible spending account was also made available to Company employees to pay eligible health related, dependent care expenses, or group health care expenses as qualified by Section 125 (d) of the Internal Revenue Code.

Executive Plans

The Company had three corporate whole life par policies in effect for current and retired highly compensated key personnel. The policies were established in trust as a deferred compensation and supplemental retirement plan for employed corporate officers. The Rabbi trust was originally established in 1993 and the Company was the beneficiary and owner of the policies. The policies remain in place as of December 31, 2008.

In December 1994 the Company established the non-contributory retirement program for certain company employees. The program was adopted for those employees whose retirement benefits would be reduced as a result of the benefit limitations of Sections 401(a)(17) and 415 of the Internal Revenue Code. The Board of Directors approved amending the definition of earnings for the Company's qualified and non-qualified retirement and long-term disability programs to be effective January 1, 2003.

On June 11, 2002, the Company established the Blue Cross of Idaho Health Service, Inc. Executive Non-Qualified Deferred Compensation Plan. In this connection, a Rabbi trust was established between the Company and Fidelity Management Trust Company, as well as a recordkeeping agreement between the Company and Fidelity Investments Institutional Operations Company, Inc. The purpose of the plan was to attract, motivate and retain valuable key executives. The participants have the right to direct the investment of their plan account into the registered investment companies advised by Fidelity Management & Research Company.

Incentive Plans

The Company had corporate incentive and division director incentive plans. The objective of the plans was to improve performance and productivity, and reward the individuals that helped to accomplish the agreed upon goals. The incentive plans were based upon annual performance with the exception of the Claims and Customer Service incentive plans which were based on quarterly results. The incentives were based on a range to determine percentage, which is multiplied by the participant's salary, with the exception of the Federal Employees Program. The Federal Employees Program incentive consisted of a dollar amount that was determined by the national program, which was then divided between eligible participants.

TERRITORY AND PLAN OF OPERATION

The Company is licensed only in the State of Idaho as a mutual insurer authorized to write disability insurance, including managed care. In addition to the home office located in Meridian, Idaho, the Company maintains five district offices located throughout the State of Idaho in the cites of Coeur d'Alene, Idaho Falls, Lewiston, Pocatello, and Twin Falls. The primary functions of the district offices include marketing, policyholder service, and writing new business. Claims processing is performed in the home office located in Meridian, Idaho.

The Company provided health care services to group and individual subscribers utilizing participating/contracting providers as a means of fulfilling their contractual obligations. In addition, the Company provided administrative services to companies which have self-funded a portion of their employees' health care claims, and the Federal Employee Health Benefit Plan to federal government employees.

During the examination period, the Company provided traditional individual major medical and Medicare supplement plans, Medicare Advantage plans, small and large group plans, Preferred Provider Organization plans, Managed Care plans and also administered Administrative Service Contracts (ASC) for self-funded plans. As previously reported under the caption, *MANAGEMENT AND CONTROL: Contracts and Agreements*, the Company began administering and paying the claims to participants of the State of Idaho Medicaid dental program, "Idaho Smiles".

The Company marketed its insurance products through commissioned producers and agencies and utilized a field force of approximately 2,900 appointed producers.

Agencies produce business pursuant to Independent Production Agreements – Agency. There is a separate Independent Production Agreement for individual agents. An Addendum to Agreement with Business Associate, which is included as part of the Independent Production Agreement, specifically pertains to privacy issues and responsibilities. The Production Agreements contain standard language, such as Agency responsibilities, confidentiality, indemnification, hold harmless, and compensation information. The contracts may be terminated by either party by written certified notice or personal delivery. The termination date will be effective 30 days after the date a written notice is mailed by either party.

STATUTORY AND SPECIAL DEPOSITS

As of December 31, 2008, the Company provided the following deposits for the protection of its policyholders and/or creditors:

Description	Par Value	Statement Value	Market Value
US Treasury Notes, 3.875%, Due 2/15/2013	$1,200,000	$1,193,506	$1,336,872
Totals:	$1,200,000	$1,193,506	$1,336,872

Securities on deposit through the Idaho Director of Insurance were held in compliance with Section 41-316A, Idaho Code.

GROWTH OF THE COMPANY

The Company's growth for the years indicated, as taken from the prior examination report and its Annual Statements, is shown in the following schedule:

Year	Admitted Assets	Liabilities	Capital & Surplus	Net Income(Loss)
2003*	$207,185,369	$102,990,791	$104,194,578	$12,451,484
2004	287,456,463	144,382,497	143,073,966	32,491,252
2005	334,277,660	137,814,406	196,463,254	49,138,531
2006	386,577,458	162,375,443	224,202,015	31,749,196
2007	424,390,898	163,501,052	260,889,846	33,794,180
2008*	443,803,958	180,673,313	263,130,645	13,927,868

Overall, the Company performed very well during the period under examination. Surplus increased from $143 million at year-end 2004 to $263 million at year-end 2008 and to $334 million as of September 30, 2009. Total revenues increased from $690.9 million at year-end 2004 to $999.8 million at year-end 2008. Due to a combination of effective medical management of claims costs (including process improvements) and pricing, the Company had strong underwriting gains during the period under examination. Net income declined in 2008 due to an other than temporary impairment (OTTI) investment(s) write-down of approximately $27 million. The Company allocated fewer invested assets to equities in 2008 because of the downturn in the investment market that year. The Company's investments recovered well in 2009 with a reported $19.5 million in unrealized gains at year-end 2009 compared to an unrealized loss of $13 million in 2008.

*As determined by Examination.

MORTALITY/LOSS EXPERIENCE

The ratios of benefits and expenses to premium shown in the following schedule were derived from amounts reported in the Company's Annual Statements.

Year	Premiums Earned	Claims and Claims Adjustment Expenses Incurred	Other Expenses Incurred	Total Claims, Claims Adjustment Expenses and Other Expenses Incurred	Ratio of Claims, Claims Adjustment Expenses and Other Expenses Incurred to Premiums Earned
2004*	$690,948,397	$589,543,727	$68,874,255	$658,417,982	95.29
2005	807,026,656	678,000,760	78,782,013	756,782,773	93.77
2006	888,037,147	785,857,851	77,877,537	863,735,388	97.26
2007	969,018,397	876,799,390	79,697,867	956,497,257	98.71
2008*	999,804,286	914,051,087	78,586,585	992,637,672	99.28

*As determined by Examination.

REINSURANCE

The Company did not assume or cede reinsurance business with any third party insurance or reinsurance companies during the period under examination. However, the Company did participate in the Idaho Individual High Risk Reinsurance Pool.

Idaho Individual High Risk Reinsurance Pool

The Company ceded business to the Idaho Individual High Risk Reinsurance Pool during the examination period. Under the Pool, the Company could submit high risk applications to the Pool if said applications were denied a preferred program, based on a health statement application, or if the premium for the preferred program was higher than the High Risk Program counterpart.

The Board of Directors of the Idaho Individual High Risk Reinsurance Pool were responsible for the design of the individual Basic, Standard, Catastrophic A and Catastrophic B high risk plans and also established the premium rates for the plans.

The Company had to meet a $5,000 deductible per person per calendar year and was also responsible for 20 percent coinsurance for the next $25,000 of benefit payments during a calendar year. The Pool reinsured the remainder. Lifetime policy maximums were determined by the plan selected.

In 2005, Health Savings Account compatible health plans were also added to Pool eligibility.

INSURANCE PRODUCTS AND RELATED PRACTICES

Policy Forms and Underwriting

The Market Conduct Examiners reviewed policy form and rate filings for part of 2008. It was noted that the Company did not file several policy forms or rates (the files did not contain the filed policy forms marked "filed certified") with the Idaho Department of Insurance. It is therefore recommended that in the future, the Company submit all rate and policy form filings with the Idaho Department of Insurance. Specifically, this recommendation pertains to a dental product, Form #3-204 (see Section 41-2136, Idaho Code) and to a small group rate (see IDAPA Rule 18.01.69.036) that were not filed with the Department. Management indicated that the rate for this small group was subsequently filed with the Department of Insurance.

The Company filed only the template for the generic large group product with the Idaho Department of Insurance. Large group contracts that deviated from the template in any manner were not filed with the Department pursuant to Section 41-1812, Idaho Code, which requires such contracts be filed. Therefore, it is recommended that large group contracts be filed with the Department in compliance with Section 41-1812, Idaho Code.

New Business Review

Statistical samples, with a 90 percent confidence level, of group and non-group business written in 2008 were reviewed. This review indicated that writing producers were properly licensed and/or agents properly appointed. Premiums were re-calculated by the examination with only minor rounding differences noted. The review of non-group business indicated compliance with Section 41-5203(13), Idaho Code with respect to use of appropriate index rates. Furthermore, premiums did not vary more than 50 percent of the index rate pursuant to Section 41-5206(a), Idaho Code. This review also verified, as previously reported, that certain policy forms and rates were not filed with the Idaho Department of Insurance.

Renewal Business Review

Statistical samples, with a 90 percent confidence level, of group and non-group business renewed in 2008 were reviewed. This review indicated that writing producers were properly licensed and/or agents properly appointed. Premiums for the non-group business were re-calculated by the examination with only minor rounding differences noted.

For the small group renewals, the premium calculation for one of the individual group members in each group was reviewed. Eight or approximately 17 percent of the rates reviewed were found to be non-complaint with Section 41-4706(1)(c), Idaho Code, and IDAPA 18.01.69.036.16 whereby the renewal rate increase as a result of claim expense and/or health status exceeded 15 percent as set forth by Idaho law.

Therefore, it is recommended that the Company come into compliance with Section 41-4706(1)(c), Idaho Code, and IDAPA 18.01.69.036.16.

Cancelled/Non-Renewed Business Review

A statistical sample with a 90 percent confidence level of cancelled/non-renewed business was reviewed for appropriate cancellation or non-renewal. Nothing exceptional regarding Idaho Code violations was noted in this review.

Treatment of Policyholders

Claims

A statistical sample, with a 95 percent confidence level, of claims incurred and paid during 2008 was reviewed. This review indicated that claims, in general, were settled promptly and in accordance with policy terms. No exceptions were noted as to the requirements of Section 41-1329, Idaho Code, Unfair Claim Settlement Practices nor Section 41-5602, Prompt Payment of Claims.

Complaints

The Company maintained complaint handling procedures and a complaint register as required by Section 41-1330, Idaho Code. A review of complaint files found no exceptions.

The Company verified that it did not have any advisory panels for commercial managed care contracts. Therefore, it is recommended the Company establish an advisory panel as set forth by Section 41-3916, Idaho Code.

Advertising and Sales Material

Subsequent to a review of various advertising materials by the Market Conduct Examiners, the Company could not produce any records that such materials were filed with the Department. Additionally, the Department of Insurance did not have any records that several advertising materials reviewed by the Market Conduct Examiners were filed with the Department pursuant to IDAPA 18.01.24.025. Further, the Company did not maintain a file containing every printed, published or prepared advertisement of individual policies and typical printed, published or prepared advertisements of its blanket, franchise and group policies for the longer of a period of 4 years or the filing of the next examination report (12/31/08) as required by IDAPA 18.01.24.024.

It is recommended that the Company file its advertising materials in compliance with IDAPA 18.01.24, Advertisement of Disability (Accident and Sickness) Insurance. It is further recommended the Company maintain an advertising file in compliance with IDAPA 18.01.24.

Information about the Company and its products is available to the general public on its website at www.bcidaho.com.

None of the Company's advertising materials or information available on the Internet appeared to be deceptive or misleading.

ACCOUNTS AND RECORDS

General Accounting

The Company's claims payment, processing, group administration, membership/billing administration, provider administration, customer service, medical/management, commissions, and benefits administration applications were performed on the Facets system. The Facets system runs on a series of IBM Windows Servers with a Sybase database on an IBM AIX host. Lawson software was utilized for financial and human resource applications. Lawson runs on a series of IBM Windows Servers with a Microsoft SQL database.

The general ledger and supporting accounting records were maintained on a GAAP basis and then adjusted to a Statutory basis of accounting through adjusting journal entries. The Annual Statements were compiled utilizing the Sunguard software package, the NAIC *Annual Statement Instructions* and the NAIC *Accounting Practices and Procedures Manual*.

During the previous and current examination periods, the Idaho Department of Insurance approved the use of non-NAIC fair market values for the Company's investments. It was determined that the differences in fair market values were immaterial to the financial statements.

In 2009, the Company began reporting the "Idaho Smiles" contract activity as "Dental Only" activity on the schedules reporting line-of-business activity. In previous years, this activity had been reported as "Title XIX Medicaid" activity. The Company received permission from the Idaho Department of Insurance for this reclassification.

The Company also has two current practices prescribed by the Idaho Department of Insurance that differ from NAIC Statutory Accounting Principles. The prescribed practices relate to amortization periods for cost of electronic and mechanical machines set forth under Section 41-601(11), Idaho Code and Section 41-601(12), Idaho Code which permits office equipment, office furniture, and private passenger automobiles as admitted assets.

Independent Accountants

The annual independent audits of the Company for 2005 and 2006 were performed by Deloitte & Touche LLP, Boise, Idaho. For 2007 and 2008 KPMG LLP, Boise, Idaho was retained to perform the independent audits. The Company properly notified the Department of the change in auditors pursuant to IDAPA 18.01.62.

The financial statements in each report were on a statutory basis. There was some reliance on the 2008 audit report and workpapers in this examination of the Company.

Actuarial Opinion

The unpaid claims reserves and unpaid claims adjustment expenses and related actuarial items were calculated by the Company and reviewed by Will Fox, FSA, MAAA, consulting actuary with Milliman, Inc. The December 31, 2008 statement of actuarial opinion stated that the amounts carried in the balance sheet:

(i) are computed in accordance with accepted actuarial standards consistently applied and are fairly stated in accordance with sound actuarial principles, based upon the relevant Standards of Practice and Compliance guidelines as promulgated by the Actuarial Standards Board;

(ii) are based on actuarial assumptions relevant to contract provisions and appropriate to the purpose for which the statement was prepared;

(iii) meet the requirements of the insurance laws of the State of Idaho;

(iv) make good and sufficient provision of all unpaid claims and other actuarial liabilities of the Company guaranteed under the terms of its contracts and agreements;

(v) are computed on the basis of assumptions consistent with those in computing the corresponding items in the annual statements of the Company for the preceding year-end; and

(vi) include provision of all related actuarial items which ought to be established.

The identified actuarial items in the 2008 Annual Statement were as follows:

Claims unpaid, page 3, line 1	$96,900,000
Accrued medical incentive pool and bonus amounts, page 3 line 2	10,088,756
Unpaid claims adjustment expenses, page 3, line 3	3,158,000
Aggregate health policy reserves, page 3, line 4	3,684,945
Aggregate health claim reserves, page 3, line 7	0

The actuarial review of reserves, related liabilities, and other actuarial items was performed by Lewis & Ellis, Inc., consulting actuary, for the Idaho Department of Insurance.

See the *NOTES TO THE FINANCIAL STATEMENTS* section, later in this report, for further discussion regarding the Department's consulting actuary's analysis.

INFORMATION SYSTEMS REVIEW

The Company's information systems were reviewed by Information System Specialist, Jenny L. Jeffers, CISA, AES, on behalf of Examination Resources, LLC. The procedures were performed in accordance with the guidelines and procedures set forth in the NAIC's *Exhibit C Evaluation of Controls in Information Systems Questionnaire (ISQ)* contained in the NAIC *Financial Condition Examiners Handbook*. In summary, the functional areas reviewed by the Information System Specialist included the following:

- Section A – Management and Organizational Controls
- Section B – Logical and Physical Security
- Section C – Changes to Applications
- Section D – System and Program Development
- Section E – Contingency Planning
- Section F – Service Provider Controls
- Section G – Operations
- Section H – Processing Controls
- Section I – E-Commerce Controls
- Section J – Network and Internet Controls

The Information System Specialist's findings were presented to the Company in the Management Letter.

FINANCIAL STATEMENTS

The financial section of this report contains the following statements:

Balance Sheet as of December 31, 2008

Statement of Revenue and Expenses, Year 2008

Reconciliation of Examination Changes to the Statement of Revenue and Expenses

Capital and Surplus Account, Year 2008

Reconciliation of Capital and Surplus Account, December 31, 2004, through December 31, 2008.

Balance Sheet
As of December 31, 2008

ASSETS

	Assets	Nonadmitted Assets	Net Admitted
Bonds	$211,037,597	$ 0	$211,037,597
Stocks			
Preferred stocks	1,208,634	0	1,208,634
Common stocks	102,284,553	5,440,731	96,843,822
Real estate, properties occupied by the company	21,103,314	0	21,103,314
Cash, cash equivalents and short-term investments	60,527,799	0	60,527,799
Other invested assets	1,210,232	1,210,232	0
Investment income due and accrued	1,716,962	0	1,716,962
Uncollected premiums and agents' balances in the course of collection	3,912,488	109,757	3,802,731
Amounts receivable relating to uninsured plans	8,244,407	0	8,244,407
Net deferred tax asset	53,295,622	39,876,777	13,418,845
Electronic data processing equipment & software	15,736,232	11,592,377	4,143,855
Furniture and equipment, including health care delivery assets	3,756,694	158,065	3,598,629
Health care and other amounts receivable	16,812,314	659,166	16,153,148
Aggregate write-ins for other than invested assets:			
Non-qualified Executive Deferred Compensation	666,177	666,177	0
Prepaid Expenses and Miscellaneous Receivables	13,353,323	13,353,323	0
Cash Value Life Insurance	2,004,216	0	2,004,216
Rounding	(1)	0	(1)
Totals	$516,870,563	$73,066,605	$443,803,958

LIABILITIES, CAPITAL AND SURPLUS

	Covered	Uncovered	Total
Claims unpaid (less $1,437,000 reinsurance ceded) (Note 1)	$ 96,900,000	$ 0	$ 96,900,000
Accrued medical incentive pool and bonus amounts (Note 1)	10,088,756		10,088,756
Unpaid claims adjustment expenses (Note 1)	3,158,000		3,158,000
Aggregate health policy reserves (Note 1)	3,684,945		3,684,945
Premiums received in advance	13,747,718		13,747,718
General expenses due or accrued	50,568,770		50,568,770
Current federal and foreign income tax payable and interest thereon	127,462		127,462
Amounts withheld or retained for the account of others	1,576,829		1,576,829
Mortgage Interest Rate Swap	820,833		820,833
Total liabilities	$180,673,313	$ 0	$180,673,313
Unassigned funds (surplus)			$263,130,645
Total capital and surplus			$263,130,645
Total Liabilities, capital and surplus			$443,803,958

STATEMENT OF REVENUE AND EXPENSES

For the Year Ending December 31, 2008

	Per Company	Reclassification	Per Exam
Net premium income (Note 2)	$998,672,339	$26,497,993	$1,025,170,332
Change in unearned premium reserves and reserve for rate credits	(387,564)		(387,564)
Host Access Fees	1,400,611		1,400,611
Fixed Asset Disposal & Other Income	118,900		118,900
Total revenues	$999,804,286	$26,497,993	$1,026,302,279
Hospital and Medical:			
Hospital/medical benefits	$593,606,726		$593,606,726
Other professional services	79,926,569		79,926,569
Outside referrals	48,661,801		48,661,801
Emergency room and out-of-area	37,315,785		37,315,785
Prescription drugs	107,324,900		107,324,900
Incentive pool, withhold adjustments and bonus amounts	6,015,533		6,015,533
Subtotal	$872,851,314		$872,851,314
Less:			
Net reinsurance recoveries (Note 2)	$ 26,497,993	($26,497,993)	$ 0
Total Hospital & Medical	$846,353,321	($26,497,993)	$872,851,314
Claims adjustment expenses, including $27,568,901 cost containment expenses	41,199,773		41,199,773
General administrative expenses	78,586,585		78,586,585
Total underwriting deductions	$966,139,679		$992,637,672
Net underwriting gain	$ 33,664,607		$ 33,664,607
Net investment income earned	$ 16,036,583		$ 16,036,583
Net realized capital losses, less capital gains tax of $0	(27,267,467)		(27,267,467)
Net investment losses	$(11,230,884)		$(11,230,884)
Net income before federal income taxes	$ 22,433,723		$ 22,433,723
Federal and foreign income taxes incurred	8,505,855		8,505,855
Net income	$ 13,927,868		$ 13,927,868

RECONCILIATION OF EXAMINATION CHANGES

TO THE STATEMENT OF REVENUE AND EXPENSES

As of December 31, 2008

Capital and surplus per Company				$263,130,645
Account	Per Company	Per Examination	Increase/ (Decrease) in Surplus	
Net premium income (Note 2)	$998,672,339	$1,025,170,332	$26,497,993	
Net reinsurance recoveries (Note 2)	26,497,993	0	(26,497,993)	
Net increase (decrease) in surplus			$ 0	
Capital and surplus per Examination				$263,130,645

CAPITAL AND SURPLUS ACCOUNT

For the Year Ending December 31, 2008

	Per Company	Examination Changes	Per Examination
Capital and surplus, December 31, 2007	$260,889,846	$ 0	$260,889,846
GAINS AND (LOSSES) IN SURPLUS			
Net income	$ 13,927,868	$ 0	$ 13,927,868
Change in net unrealized capital gains	(12,883,299)	0	(12,883,299)
Change in net deferred income tax	4,824,264	0	4,824,264
Change in nonadmitted assets	(3,233,786)	0	(3,233,786)
Difference GAAP-SAP on write-ins	(394,248)	0	(394,248)
Net change in capital and surplus	$ 2,240,799	$ 0	$ 2,240,799
Capital and surplus, December 31, 2008	$263,130,645	$ 0	$263,130,645

RECONCILIATION OF CAPITAL AND SURPLUS ACCOUNT

December 31, 2004 Through December 31, 2008

	2005	2006	2007	2008
Capital and surplus, December 31, previous year	$143,073,966	$196,463,254	$224,202,015	$260,889,846
Net income	49,138,531	31,749,196	33,794,180	13,927,868
Change in net unrealized capital gains or (losses)	1,709,541	6,188,477	(1,466,376)	(12,883,299)
Change in net deferred income tax	2,815,752	3,732,847	(161,667)	4,824,264
Change in nonadmitted assets	(1,741,427)	(15,153,539)	3,694,946	(3,233,786)
Difference GAAP-SAP on Write-ins	1,039,090	1,041,132	826,748	(394,248)
Other Comprehensive Income Adjustment	427,791	180,648	0	0
Rounding	10	0	0	0
Net change in capital and surplus	$ 53,389,288	$ 27,738,761	$ 36,687,831	$ 2,240,799
Capital and surplus, December 31, current year	$196,463,254	$224,202,015	$260,889,846	$263,130,645

NOTES TO THE FINANCIAL STATEMENTS

Note (1) Claims unpaid (less $1,437,000 reinsurance ceded)	$96,900,000
Accrued medical incentive pool and bonus amounts	10,088,756
Unpaid claims adjustment expenses	3,158,000
Aggregate health policy reserves	3,684,945

Michael A. Mayberry, F.S.A., M.A.A.A., Vice President and Principal of Lewis & Ellis, Inc., was retained by the Department to perform the actuarial portion of the examination. The scope of Lewis & Ellis' duties included issuing an opinion as to the adequacy of certain amounts reported by the Company as of December 31, 2008, which is noted above. In conjunction with Department examiners, Lewis & Ellis also reviewed inherent risks and mitigating internal controls in the Company's reserving system. Finally, Lewis & Ellis reviewed the administrative services agreement between the Company and Dentaquest LLC. See *MANAGEMENT AND CONTROL: Contracts and Agreements* for further discussion.

Based on their review and results of procedures performed, Lewis & Ellis concluded the year-end 2008 reserves reported by the Company were adequate. Furthermore, Lewis & Ellis did not recommend any adjustments to the reported reserves and other actuarial items related to their report.

Note (2) Net Premium Income	$1,025,170,332
Net Reinsurance Recoveries	$ 0

Subsequent to an analysis of the "Idaho Smiles" Medicaid dental contract between the Company and the Idaho Department of Health and Welfare, it was determined by the Idaho Department of Insurance that the Company bears insurance risk of loss. In other words, the Company is ultimately responsible for losses resulting from the insured risk with Health and Welfare and the contract should be properly classified as a "fully insured" contract.

In this connection, the Company has contracted with the provider network of Dentaquest LLC to facilitate claims administration and payment. However, again, the principle/primary insurance risk of loss is borne by the Company.

Based upon the above determinations, the Department has concluded the following:

1) The Company should account for this contract as a "fully insured" product line.
2) Reinsurance accounting is not appropriate in this case.

Therefore, reclassification adjustments on the 2008 Statement of Revenue and Expenses, within this examination report, have been made to effectuate the Department's understanding of the "Idaho Smiles" contract as identified in items 1 and 2 above. It should also be noted, however, that these reclassification entries taken as a whole, have no effect on the 2008 net income or policyholder surplus.

As a result, it is recommended that the Company implement the above accounting for the "Idaho Smiles" Medicaid contract in future statutory statements.

SUMMARY, COMMENTS AND RECOMMENDATIONS

Summary

The results of this examination disclosed that as of December 31, 2008, the Company had admitted assets of $443,803,958, liabilities of $180,673,313, and unassigned funds of $263,130,645. Therefore, the Company's total capital and surplus exceeded the $2,000,000 minimum prescribed by Section 41-313, Idaho Code.

Comments and Recommendations

Page

22 It is recommended that in the future, the Company submit all rate and policy form filings with the Idaho Department of Insurance.

22 It is recommended that large group contracts be filed with the Department in compliance with Section 41-1812, Idaho Code.

23 It is recommended that the Company come into compliance with Section 41-4706(1)(c), Idaho Code and IDAPA 18.01.69.036.16.

24 The Company verified that it did not have any advisory panels for commercial managed care contracts. Therefore, it is recommended the Company establish an advisory panel as set forth by Section 41-3916, Idaho Code.

24 It is recommended that the Company file its advertising materials in compliance with IDAPA 18.01.24. It is further recommended the Company maintain an advertising file in compliance with IDAPA 18.01.24.

34 It is recommended the Company implement the recommended accounting for the "Idaho Smiles" Medicaid contract in future statutory statements.

CONCLUSION

The undersigned acknowledges the assistance and cooperation of the Company's officers and employees in conducting the examination.

In addition to the undersigned, David W. Emery, CFE, FLMI; Kelvin Ko, CFE; Dale Freeman, MBA, CIE; and Arlene Barrie of the Idaho Department of Insurance, participated in the examination. Michael A. Mayberry, F.S.A., M.A.A.A, Lewis & Ellis, Inc. conducted the actuarial portion of the examination. The Company's information systems were reviewed by Information System Specialist, Jenny L. Jeffers, CISA, AES, on behalf of Examination Resources, LLC.

Respectfully submitted,

Lois Haley

Lois Haley, CFE
Senior Insurance Examiner
State of Idaho
Department of Insurance

AFFIDAVIT OF EXAMINER

State of Idaho
County of Ada

Lois Haley, being duly sworn, deposes and says that she is a duly appointed Examiner for the Department of Insurance of the State of Idaho, that she has made an examination of the affairs and financial condition of Blue Cross of Idaho Health Service, Inc. for the period from January 1, 2005, through December 31, 2008, that the information obtained in the report consisting of the foregoing pages is true and correct to the best of her knowledge and belief; and that any conclusions and recommendations contained in this report are based on the facts disclosed in the examination.

Lois Haley
Senior Insurance Examiner
Department of Insurance
State of Idaho

Subscribed and sworn to before me the 28th day of May, 2010 at Boise, Idaho.

JOHN C. KEENAN NOTARY PUBLIC STATE OF IDAHO

Notary Public

My Commission Expires: 30 OCTOBER 2013

EXHIBIT B

State of Idaho
DEPARTMENT OF INSURANCE

C. L. "BUTCH" OTTER
Governor

700 West State Street, 3rd Floor
P.O. Box 83720
Boise, Idaho 83720-0043
Phone (208)334-4250
FAX # (208)334-4398

WILLIAM W. DEAL
Director

WAIVER

In the matter of the Report of Examination as of December 31, 2008, of the:

Blue Cross of Idaho Health Service, Inc.
3000 East Pine Avenue
Meridian, Idaho 83642

By executing this Waiver, the Company hereby acknowledges receipt of the above-described examination report, originally verified as of the 28th day of May, 2010, and including revisions to pages 23 and 34 (and other minor clarifications and/or corrections) as of June 23, 2010, by this Waiver hereby consents to the immediate entry of a final order by the Director of the Department of Insurance adopting said report without any modifications.

By executing this Waiver, the Company also hereby waives:

1. its right to examine the report for up to thirty (30) days as provided in Idaho Code section 41-227(4),
2. its right to make a written submission or rebuttal to the report prior to entry of a final order as provided in Idaho Code section 41-227(4) and (5),
3. any right to request a hearing under Idaho Code sections 41-227(5) and (6), 41-232(2)(b), or elsewhere in the Idaho Code, and
4. any right to seek reconsideration and appeal from the Director's order adopting the report as provided by section 41-227(6), Idaho Code, or elsewhere in the Idaho Code.

Dated this 25 day of June, 2010

Jack Myers
Name (print)

Name (signature)

Exec V P of Finance & CFO
Title

EXHIBIT C

Blue Cross of Idaho

June 25, 2010

Lois Haley, CFE, CPA
Examiner-in-Charge
Idaho Department of Insurance
700 West State Street
Boise, Idaho 83720

Dear Ms. Haley,

Attached are the responses to the Report of Examination of Blue Cross of Idaho Health Service, Inc. as of 12-31-08. We understand these responses will be attached to the Report and become a public document; therefore, we did want to acknowledge the Comments and Recommendations, and make note to the Department of Insurance of our actions taken.

Comments and Recommendations

Page

22 *It is recommended that in the future, the Company submit all rate and policy form filings with the Idaho Department of Insurance.*

RESPONSE:
Blue Cross has initiated a checklist process to reduce the possibility that Small Group rates filed do not match the Small Group rates billed. The SERFF system adopted by the Department and Blue Cross eliminates the cause of the dental rates not being marked as filed.

22 *It is recommended that large group contracts be filed with the Department in compliance with Section 41-1812, Idaho Code.*

RESPONSE:
Blue Cross agrees with this recommendation. We have worked with the Department of Insurance to develop a plan and process to file the large group contracts in a manner that is efficient and agreeable to both parties. The variable filing, which encompasses the majority of the large group contracts, has already been filed. There are approximately 20 remaining contracts that deviate from the variable filing. These contracts will be individually filed under separate form numbers soon.

23 *It is recommended that the Company come into compliance with Section 41-4706(1)(c), Idaho Code and IDAPA 18.01.69.036.16.*

RESPONSE:
Blue Cross has changed its Small Group renewal formulas as recommended.

24 *The Company verified that it did not have any advisory panels for commercial managed care contracts. Therefore, it is recommended the Company establish an advisory panel as set forth by Section 41-3916, Idaho Code.*

RESPONSE:
Blue Cross agrees with this recommendation and will reinstate the advisory panels for our commercial managed care contracts.

24 *It is recommended that the Company file its advertising materials in compliance with IDAPA 18.01.24. It is further recommended the Company maintain an advertising file in compliance with IDAPA 18.01.24.*

RESPONSE:
Blue Cross agrees with this recommendation and will file all future advertising materials with the Department, as required. We will also establish an internal filing system to maintain a record of all advertising materials.

34 *It is recommended the Company implement the recommended accounting for the "Idaho Smiles" Medicaid contract in future statutory statements.*

RESPONSE:
Blue Cross agrees with the recommended accounting for the "Idaho Smiles" Medicaid contract for future statutory statements. We will make the appropriate changes to reporting beginning with the second quarter 2010 statutory report.

We respectfully submit our responses to you and welcome any comments you may have regarding them. If you have any questions, please contact David Slonaker at (208) 331-7456 or Carol Mulder at (208) 331-7464.

Sincerely,

Jack Myers
Exec VP of Finance & CFO