

**STATE OF OREGON
DEPARTMENT OF CONSUMER AND BUSINESS SERVICES
INSURANCE DIVISION**

BEFORE THE DIRECTOR
OF THE DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

In the Matter of the Proposed Plan of Acquisition of)
Control of PacificSource Health Plans, Springfield,)
Oregon, by PacificSource, Springfield, Oregon)

Findings of Fact, Conclusions of
Law and Order
Case No. 13-10-001

INTRODUCTION

On July 2, 2013, PacificSource (“Holding”) filed a Statement Regarding the Acquisition and Control of or Merger with a Domestic Insurer to acquire control of PacificSource Health Plans (“PSHP”) as required by ORS 732.517 through 732.546. The restructuring described in the filing (the “Restructuring”) was approved by the Board of Directors of PSHP on April 16, 2013.

Supplemental information was periodically provided until the filing was complete on September 19, 2013. An amendment to the filing was also submitted on September 19, 2013.

FINDINGS OF FACT

- (1) Holding is a newly formed Oregon nonprofit public benefit corporation with no members formed with the approval of the board of directors and professional members of PSHP to facilitate the reorganization of the PacificSource group of companies as described below, and will become the sole member of PSHP.
- (2) PSHP is an Oregon nonprofit public benefit corporation with members, authorized under ORS Chapter 750 to operate as a health care service contractor.
- (3) PacificSource Community Health Plans, Inc. (“PCHP”) is an Oregon domestic insurance company authorized under ORS Chapter 731 to operate as an insurance company and is a wholly-owned subsidiary of PSHP.

(4) PSHP's electronic data processing equipment and software, other equipment, furniture, and employees are to be transferred to Holding where they will be available to provide services to PSHP and Holding's and PSHP's subsidiaries under administrative services agreements. Centralizing in Holding data and claims processing, other administrative functions, and human resources functions will allow for more efficient and effective use and allocation of resources among the various entities that are a part of the current PSHP insurance holding company system.

(5) The lines of business of PSHP and PCHP will not change as a result of the Restructuring.

(6) Holding will obtain control rights in PSHP upon the filing of the PSHP Restated Articles of Incorporation and adoption of the Restated Bylaws. This is not an acquisition transaction in the traditional sense and will not involve payment of consideration by Holding to PSHP.

(7) Each of the Holding's Executive Officers and members of the Board of Directors currently hold similar positions with PSHP.

(8) Once the control relationship is established, Holding will purchase certain assets of PSHP and its current subsidiaries to effect the next stages of the Restructuring (collectively, the "Asset Acquisitions"). The Asset Acquisitions will include acquisition of (i) PSHP's electronic data processing equipment and software, other equipment, and furniture ("the EDP/Equipment/Furniture Acquisition"; (ii) PSHP's Springfield, Oregon headquarters building (the "Springfield Building"); (iii) the office building in Bend, Oregon in which PCHP's headquarters offices are located (the "Bend Building"), and (iv) all of the stock of PSHP wholly-owned subsidiary PacificSource Administrators, Inc., an Oregon corporation ("PSA"). The Bend Building is presently owned by Clear Choice Properties, LLC, a wholly-owned subsidiary of PCHP.

(9) Holding's funding for the Asset Acquisitions is to come from a credit facility provided by a commercial lender (the "Credit Facility"). The Credit Facility will be secured by the revenues

generated under the administrative services agreements to be established between Holding, PSHP and other current subsidiaries of PSHP. In addition, Holding will obtain mortgage loans to fund a portion of the purchase price for the Springfield Building and a portion of the purchase price for the Bend Building, each mortgage loan to be secured by a customary first priority deed of trust or mortgage on the subject building. Upon the closing of the Credit Facility, PSHP will repay in full PSHP's current line of credit facility with Wells Fargo Bank, N.A. and close the associated account.

(10) Because Holding does not anticipate closing on the Credit Facility until after the expected closing date for the EDP/Equipment/Furniture Acquisition, Holding expects to pay the purchase price for the EDP/Equipment/Furniture Acquisition with a promissory note secured by the acquired property. This note receivable due to PSHP will be reported by PSHP in its statutory accounting financial statements as a nonadmitted asset. Upon the closing of the Credit Facility, the promissory note will be paid in full.

(11) It is expected that Holding will repay the amounts borrowed under the Credit Facility within seven years.

(12) Holding intends to close the EDP/Equipment/Furniture Acquisition on approximately December 1, 2013. The EDP/Equipment/Furniture Acquisition will include PSHP's electronic data processing equipment and software (including, but not limited to PSHP's Facets claims system), other equipment, and furniture. The price paid by Holding will be equal to the value of the assets on the books of PSHP. Upon completion of the EDP/Equipment/Furniture Acquisition, Holding will use the purchased assets to provide data processing, data management and storage, claims processing and other services to PSHP and other current PSHP subsidiaries under one or more administrative services agreements between Holding and PSHP or the applicable PSHP subsidiary.

(13) Holding intends immediately after the close of business on December 31, 2013, to have all of the employees of PSHP become employees of Holding, which employees will thereafter provide services to PSHP and other current PSHP subsidiaries under administrative services agreements between Holding and PSHP and other members of the insurance holding company system. The transfer of employees will include continuation of all employee benefit plans, carryover of individual lengths of service, assumption of payroll liability, etc.

(14) Holding intends no later than March 31, 2014, to purchase from PSHP the Springfield Building, and fixtures and equipment used in the operation of the Springfield Building, with the purchase price for the building to be fair market value, and the purchase price for the fixtures and equipment to be the value of the furniture and fixtures on the books of PSHP. A portion of the purchase price for the Springfield Building will be financed by a mortgage loan secured by a first priority deed of trust or mortgage on the building. The Springfield Building will be leased back by Holding to PSHP.

(15) Holding intends no later than March 31, 2014, to purchase from Clear Choice Properties, LLC the Bend Building, and fixtures and equipment used in the operation of the Bend Building, with the purchase price for the building to be fair market value, and the purchase price for the fixtures and equipment to be the value of the furniture and fixtures on the books of Clear Choice Properties, LLC. A portion of the purchase price for the Bend Building will be financed by a mortgage loan secured by a first priority deed of trust or mortgage on the building. The office space PCHP presently leases in the Bend Building will continue to be leased to PCHP under a lease between Holding and PCHP.

(16) Holding intends no later than March 31, 2014, to cause PSHP to sell all of the stock of PSA to Holding for a price equal to the value of the stock on the books of PSHP.

(17) Holding intends, at such time as is indicated by upcoming regulatory requirements, to purchase all of the stock of PacificSource Community Solutions, Inc., an Oregon corporation and wholly-owned subsidiary of PCHP.

(18) The day-to-day governance of PSHP is expected to remain substantially as it was before the Restructuring, with no change in the executive officers.

(19) The administrative services agreement between Holding and PSHP that is to be effective approximately December 1, 2013 (the "2013 ASA") is described in and attached to a Form D, Prior Notice of a Transaction, filed with the Insurance Division at the same time as this Form A.

(20) A new administrative services agreement Holding and PSHP will be put into effect January 1, 2014 (the "2014 ASA") and will replace the 2013 ASA. The 2014 ASA will be described in and attached to a Form D, Prior notice of a Transaction, to be filed with the Insurance Division in the near future.

(21) The form used for the 2014 ASA will also be used for new administrative services agreements between Holding and other members of the insurance company holding system, with the compensation to be paid to Holding by a given entity to be determined on a case by case basis. The new agreements will be described in and attached to Forms D timely filed with the Insurance Division.

(22) Holding eventually intends that PSHP distribute or sell the stock of PCHP to Holding so that PCHP will be a direct subsidiary of Holding. When Holding is ready for this transaction to occur, it will prepare and file with the Insurance Division a Form A exemption request as provided by Oregon Revised Statute 732.521(2).

(23) Holding has no plans or proposals to declare an extraordinary dividend out of PSHP or PCHP, to liquidate PSHP or PCHP, to sell PSHP's or PCHP's assets to or merge either of them with any person or

persons, or to make any other material change to PSHP's or PCHP's business operations or corporate structure or management that are not described above.

(24) On the basis of the Statement Regarding the Acquisition of Control of PacificSource Health Plans by PacificSource, and specifically on the basis of the findings of fact above, the Director enters the following:

CONCLUSIONS OF LAW

1. The Statement Regarding the Acquisition of Control of PacificSource Health Plans by PacificSource that was submitted to the Director is properly supported by the required documents, and meets the requirements of the Oregon Insurance Code for approval with respect to acquisitions and mergers pursuant to ORS 732.517 to 732.546.
2. The Director finds that there is no evidence that:
 - (a) The activity is contrary to law or would result in a prohibited combination of risks or classes of insurance.

The acquisition of control of PSHP by Holding is permitted by ORS 732.517 to 732.546.

- (b) The activity is inequitable or unfair to the policyholders or shareholders of any insurer involved or to any other person affected by the proposed activity.

PSHP has no shareholders. This is not an acquisition transaction in the traditional sense and will not involve payment of consideration by Holding to PSHP. However, once the control relationship is established, Holding will purchase certain assets of PSHP and its current subsidiaries to effect the next stages of the Restructuring (collectively, the "Asset Acquisitions"). The reorganization will increase PSHP's capital and surplus in the approximate amount of \$28 million. Based on projected financial statements, PSHP's capital and surplus will total \$163 million as of December 31, 2013. PSHP capital and surplus, as reported in its Quarterly Statement as of June 30, 2013, totals \$126 million.

- (c) The activity would substantially reduce the security of and service to be rendered to policyholders of any domestic insurer involved, or would otherwise prejudice the interests of such policyholders in this state or elsewhere.

With respect to continued operations, the financial security afforded by the sale of assets for cash received from Holdings and the continuity provided to PSHP and PCHP policyholders and employees are factors that enhance the benefits of the proposed transaction to PSHP and PCHP policyholders.

(d) The activity provides for a foreign or alien insurer to be an acquiring party, and the insurer cannot satisfy the requirements of this state for transacting an insurance business involving the classes of insurance affected by the activity.

The activity does not provide for a foreign or alien insurer to be an acquiring party. As such, this provision is not relevant to the Director's consideration.

(e) The activity or its consummation would substantially lessen competition in insurance in this state or tend to create a monopoly.

This transaction will not substantially lessen competition of insurance in this state or another state or tend to create a monopoly.

(f) After the change of control and ownership, the domestic insurer to which the activity applies would not be able to satisfy the requirements for the issuance of a certificate of authority to transact the line or lines of insurance for which the insurer is currently authorized.

PSHP and PCHP will be adequately capitalized to transact the lines of business for which they are authorized insurance in Oregon. *See* ORS 750.045 and 731.554.

(g) The financial condition of any acquiring party might jeopardize the financial stability of the insurer.

The transaction with Holdings will enhance – not jeopardize – the financial stability of PSHP and PCHP. The cash received from Holding will provide greater liquidity to PSHP by exchanging cash totaling approximately \$50 million for illiquid assets.

(h) The plans or proposals that the acquiring party has to liquidate the insurer, sell its assets or consolidate or merge it with any person, or to make any other material change in the insurer's business or corporate structure or management, are unfair and unreasonable to policyholders of the insurer and not in the public interest.

Following the proposed transaction, Holding has no plans to liquidate PSHP or PCHP, sell their assets or consolidate or merge them with any person, or to make any other material change in its business or corporate structure or management.

(i) The competence, experience and integrity of those persons who would control the operation of the insurer are such that it would not be in the interest of policyholders of the insurer and of the public to permit the activity or its consummation.

The current directors, officers, and employees of PSHP and PCHP will continue to manage the day-to-day operations of the companies' book of business following the transaction. There is nothing to suggest that these individuals lack the necessary competence, experience, or integrity to continue in the operations of PSHP and PCHP. The Director is not aware of any person who is an officer or director of Holdings or may

become an officer or director of Holding who lacks the necessary competence, experience, or integrity to manage PSHP.

(j) The activity or its consummation is likely to be hazardous or prejudicial to the insurance-buying public.

The transaction will not be hazardous or prejudicial to the insurance-buying public, but will be beneficial.

(k) The activity is subject to other material and reasonable objections.

There are no other material and reasonable objections.

ORDER

Based on the foregoing Findings of Fact and Conclusions of Law, it is hereby ordered that the acquisition of control of PacificSource Health Plans by PacificSource is hereby approved and is found to be fair, just, and equitable to the PacificSource Health Plan members.

DATED this 28th day of October, 2013.



LAURA N. CALI, FCAS, MAAA
Oregon Insurance Commissioner and Chief Actuary

NOTICE

Pursuant to ORS 732.528 (6), any insurer or other party to the proposed activity, including the insurer proposed to be acquired, within 60 days after receipt of a notice of approval or disapproval, may appeal the final order of the director as provided in ORS 183.310 to 183.550. For purposes of the judicial review the specifications required to be set forth in the written notice from the director will be deemed the findings of fact and conclusions of law of the department.

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