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Attorneys for Stillman Consulting Services, Special Deputy Liquidator for Arches Mutual Insurance Company in Liquidation

IN THE THIRD JUDICIAL DISTRICT COURT

IN AND FOR SALT LAKE COUNTY, STATE OF UTAH

In re: ARCHES MUTUAL INSURANCE COMPANY	**AMENDED REPORT OF THE SPECIAL DEPUTY LIQUIDATOR** Case No. 150907803 Judge Royal I. Hansen

Attached as Exhibit A is the Report of the Special Deputy Liquidator of Arches Mutual Insurance Company. Attached as Exhibit B is the Arches balance sheet as of May 31, 2016.

DATED this 14th day of July, 2016.

FABIAN VANCOTT

/s/ *Scott M. Lilja*
Scott M. Lilja

Attorneys for Stillman Consulting Services, Special Deputy Liquidator for Arches Mutual Insurance Company in Liquidation

CERTIFICATE OF SERVICE

I certify that on the 14th day of July, 2016, I caused a true and correct copy of the foregoing **AMENDED REPORT OF THE SPECIAL DEPUTY LIQUIDATOR**, to be electronically filed, which delivered immediate notice of the same to all counsel of record.

/s/ Scott M. Lilja
Scott M. Lilja

4817-9189-2276, v. 1

EXHIBIT A

**FIRST REPORT OF THE SPECIAL DEPUTY RECEIVER
ARCHES MUTUAL INSURANCE COMPANY
IN LIQUIDATION**

Aarches Community Health Care (AKA Arches Health Plan. The original documents filed to form the company contained the double "A" in its title) was established in 2012 pursuant to The Patient Protection and Affordable Care Act (PPACA), commonly called the Affordable Care Act (ACA) or Obamacare. The company name changed from Aarches Community Health Care to Arches Mutual Insurance Company but has been more commonly known as Arches Health Plan (hereinafter "Arches").

Pursuant to the terms of the ACA, Arches was established as a non-profit Health Maintenance Organization in accordance with Chapter 8 of Title 31A of the Utah Code.

Startup operations of an insurer in Utah and elsewhere require significant capital and, as policies are added require increasing cash reserves to maintain solvency. Arches did not have startup or reserve capital. Thus it entered into a loan agreement with the federal government. This loan arrangement was created by the ACA to assist in the formation of these sorts of companies, specifically designed to help insure people who had either not been previously insured or who could not afford insurance.

In June of 2012, Arches entered into a loan agreement with the United States Department of Health and Human Services (HHS) consisting of a startup loan ($10,106,003 paid in 2 installments) and a solvency loan ($79,544,300). The purpose of the solvency loan was to maintain capital and surplus requirements imposed by state law. Per the loan agreement: "The Loans are being provided by Lender to Borrower for the establishment of a CO-OP" (a consumer-owned and oriented plan). Arches was required to operate as a non-profit corporation. The solvency loan, by its terms, was a "surplus note"; that is, a claim to repay the note is expressly subordinated to all other creditors.

Arches began selling Insurance both on and off the state and federal insurance exchanges in 2013. Claims against Arches (and other co-ops) exceeded expert actuarial projections due to the built-up demand for insurance that co-ops were designed to alleviate.

To assist in paying expensive claims, HHS through the Center for Medicare and Medicaid Services (CMS) provided a level of reinsurance**.** That is, once claims reached a certain level, the federal reinsurance would reimburse a portion of the claim to Arches. Federal reinsurance funds must await claim development and presentment and lag behind payment of claims by Arches by a number of months. Arches hoped to receive a reinsurance payment in August, 2016 of about $9 million based on claims under 2015 policies. On May 23, 2016, however, Arches was notified by CMS that it would not receive further reinsurance or other payments from the federal government. CMS provided no response to an inquiry from the Special Deputy Liquidator (see Liquidation section below) as to the basis of its action, although, many news sources report that the defunding of the federal loan and support programs for the ACA resulted from the "cromnibus" budget bill passed by congress in December, 2014. Subsequent congressional action defunded proposed payments to companies resulting from ACA participation that might have rendered the program anything other than "revenue neutral".

In 2015, Arches was expecting approximately $11 million in risk corridor (federal support) payments. However, , Congress reduced or eliminated funding for the risk corridor program which resulted in a reduction of expected payments to Arches (and all qualified health plans) by 87.4 percent to approximately $1.4 million.

During 2014, the Utah Insurance Department (UID) was closely monitoring Arches' financial condition. Through that monitoring some issues arose that caused concern both at the UID and within the company, particularly relating to high levels of claims and expenses. On January 12, 2015, these concerns were presented to management and the Arches board of directors in the form of a report generated by the UID reflecting that Arches was in a "financially hazardous condition" under UID's Administrative Rules ("UID Report"). The UID Report informed Arches management that Arches assets were rapidly diminishing and that, absent additional capital, Arches would be unable to continue operations for more than 6 to 8 months. That prediction assumed a best case scenario where risk corridor funds were received, as promised, under the ACA. Without those risk corridor funds and other federal funding, however, the company had essentially no ability to continue operations. Although the UID Report was withdrawn due to Arches' management's strong objection and concern that when the UID Report was shared with Arches' Board members whose companies were insured by Arches those companies as well as other insureds would leave Arches, it proved to be an accurate assessment of Arches financial condition. Despite the serious issues raised in the UID Report, Arches' management made no substantial changes in Arches' operations during 2015, aside from bringing in a financial consultant and agreeing to make certain changes to its Board. Company management did undertake an effort to attract investors to supply enough capital to allow the company to continue operations. Those efforts were ultimately unsuccessful. Expenses went unrestricted and marketing, sponsorship and enrollment activity levels continued at high levels up until the day before the company was placed into receivership. The UID determined that without promised levels of funding from the federal government and with continued high levels of claims and corporate spending, Arches would fall below required financial levels and sought an order of rehabilitation. Arches consented to the petition to rehabilitate the company which was granted by the Third Judicial District Court, County of Salt Lake, State of Utah on November 2, 2015.

The insurance commissioner, acting as Rehabilitator under the Utah Act, appointed a Special Deputy Rehabilitator to take over company operations. After several weeks of evaluating company operations, the insurance commissioner acting as Rehabilitator through his Special Deputy determined that Arches was unable to fund its operations and was insolvent. Notably, only a few days after the receiver took over operation of the company, the company was served with an eviction notice from its landlord for having failed to pay rent on the Arches corporate offices. An unopposed order of liquidation under the Utah Act, with a finding of insolvency, was issued by the Third Judicial District Court on January 13, 2016. The claims bar date was set by the Court for July 14, 2016.

OPERATIONS

Due to its insolvency, Arches is unable to pay its doctors, pharmacies, other health care providers under its policies or other creditors. Arches is considering a partial distribution to claimants after the bar date passes.

Utah has no insurance guaranty association that covers the shortfall in Arches' ability to pay provider and member claims. There is, however, a statutory provision under which the Liquidator may require Utah's other Health Maintenance Organizations (HMOs) to pay amounts owing for Arches' covered claims as outlined in section 31A-27a-403, Utah Code. Any deficit in Arches' ability to pay covered claims will be funded by the other remaining HMOs in Utah. Any funds ultimately recovered from the federal government that are not required for operations will flow to the Arches creditors including the contributing HMOs to the extent they are required to pay pursuant to sections 403 and 701 of Title 31A-27a of the Utah Code.

Prior to the commencement of the receivership, Arches had very little or no ability in-house to maintain its operations. Most of the Arches operational activity was out-sourced to contractors and vendors including but not limited to primary functions such as claims administration, database management and maintenance, subrogation and recovery of overpayments, etc. Arches did maintain a medical support staff to assist claimants with claim-related issues. This internal function required the retention of a medical practitioner to oversee the operation. That individual was absent from the premises during much of the early part of the receivership and left without notice. Arches only other internal operations appeared to have been focused on marketing and dealing with CMS. Part of the latter responsibility was to assure compliance with CMS requirements in order to assure the flow of federal funds into the company under the ACA.

REHABILITATION

Upon entry of the rehabilitation order, the receiver and his staff began an evaluation of the company operations and conducted interviews with Arches' staff and officers. The statutory Rehabilitator (insurance commissioner) was kept informed of the progress of the rehabilitation and recommendations of the Special Deputy. By way of rehabilitation options:

- It was hoped that the company could allow the group policies in place to run their natural course. (Policies that covered individuals all would expire on December 31, 2015 and would not be renewed.) Unfortunately, due to negative publicity surrounding the commencement of the receivership, many policy holders began terminating their policies which left Arches with diminishing premium income but continued claim expenses. This option would have led to an increasing deficit in the company's financial position.

- The Special Deputy looked to sell the remaining business including the company as a whole to another HMO (as required by the terms of the federal loan agreement). No buyer was interested in acquiring all or part of the company or its policies or trademarks.

- In order to protect members from risk of non-coverage due to Arches' continuing financial decline, the remaining option was to seek assistance from Arches and other agents to find new insurers who would issue new policies to the members. This is the option that was ultimately utilized and all members continued their insurance in force with new companies.

During the pendency of the rehabilitation many staff left voluntarily and others were terminated as their services were no longer needed for the operations of the company, e.g. most marketing staff. All accrued wages were paid departing employees. The receiver sought and received resignations from the board of directors. On December 9, 2015, the Rehabilitator terminated the CEO after he declined the opportunity to resign from the company.

At the commencement of the receivership there was no complete inventory of assets owned by the company. Some computers were off-site and held by part time or work-at-home employees. There were two storage areas full of Arches-logoed marketing merchandise. The receivership continues to be unable to determine if all of the company equipment has been accounted for.

Arches' furniture and equipment was purchased on credit cards issued to officers and other C-suite employees and then billed to the company. Purchasers of the assets received the personal benefit of credit card points. There was little or no detail in reimbursement records to determine the validity of reimbursements paid by Arches to company employees purportedly for company expenses. According to an internal company audit, expenses lacked prior approval, internal controls, and proper documentation.

LIQUIDATION

Upon entry of the Liquidation Order on January 13, 2016, the statutory requirements of the liquidation were applied. The liquidation court entered an Amended Liquidation Order setting the claims bar date as July 14, 2016. Notices required by statute were sent out and published as required and an order approving the notice procedure was entered by the court. All relevant pleadings have been and will be posted at www.utinsreceivers.org and archeshealth.org . Proof of Claim forms are available on-line at the archeshealth.org website.

After the entry of the liquidation order CMS notified Arches that it would no longer receive federal funding from reinsurance, loan proceeds or risk corridor payments. The federal government offset federal reinsurance funds owed to Arches by approximately $634,000.

Due to reductions in staffing and requirements for operations, the receiver has begun the required process of liquidating assets not needed for operations. Some furniture and equipment was sold to then-employees, some donated to charities and some brought to the Special Deputy's Salt Lake City office. Arches receivership operations have been relocated to the Special Deputy's location effective June 30, 2016 and the former location in Murray, UT has been vacated.

Further reductions in staff, both voluntary and involuntary continued until reaching four, the present number of remaining Arches employees. An investigation of the company's books and records has begun. The findings of the investigation will appear in future reports to this court. This and future reports will be posted on archeshealth.org and www.utreceivers.org.

Len Stillman
Stillman Consulting Services, L.L.C.
Special Deputy Liquidator

EXHIBIT B

Arches Health Plan
Balance Sheet
As of May 31, 2016

	May 31, 16
ASSETS	
Operating Bank Accounts	17,235,363.37
Investment Bonds	4,592,866.09
Other Current Assets	52,692.47
TOTAL ASSETS	**21,880,921.93**
LIABILITIES & EQUITY	
Liabilities	
Accounts Payable	2,299.58
Current Liabilities	
A/P - Vendor/Broker claims	2,198,072.18
A/P - Medical/Pharmacy claims	32,015,141.57
Total Current Liabilities	34,213,213.75
Long Term Liabilities	
Federal Startup Loan	10,106,003.00
Federal Solvency Loan	79,544,300.00
Accrued Interest, Solvency Loan	335,067.88
Total Long Term Liabilities	89,985,370.88
Total Liabilities	124,200,884.21
Equity	-102,319,962.28
TOTAL LIABILITIES & EQUITY	**21,880,921.93**