

1 **FAEGRE BAKER DANIELS LLP**  
1700 Lincoln Street, Suite 3200  
2 Denver, Colorado 80203

3 **Joel A. Glover** (State Bar No. 034018)  
Direct Dial: 303.607.3648  
4 Direct Fax: 303.607.3600  
5 Email: [Joel.Glover@FaegreBD.com](mailto:Joel.Glover@FaegreBD.com)

6 Attorneys for Receiver

7  
8 SUPERIOR COURT OF ARIZONA  
9 COUNTY OF MARICOPA

10 STATE OF ARIZONA, *ex rel.*  
11 KEITH SCHRAAD, Interim Director  
of Insurance,

12 Plaintiff,

13 vs.

14 COMPASS COOPERATIVE MUTUAL  
HEALTH NETWORK, INC., dba MERITUS  
15 MUTUAL HEALTH PARTNERS, an  
Arizona corporation; and  
16 COMPASS COOPERATIVE HEALTH  
PLAN, INC., dba MERITUS HEALTH  
PARTNERS, an Arizona corporation,

17 Defendants.  
18

No. CV2016-011872

**PETITION NO. 26**

**REQUEST FOR HEARING, CLAIM  
DETERMINATION AND SETOFF  
RELATED TO CLAIMS OF THE  
UNITED STATES**

(Assigned to The Honorable  
Daniel Martin)

19 Keith Schraad, Interim Director of Insurance, as Receiver (hereinafter “Receiver”)  
20 of Compass Cooperative Mutual Health Network, Inc. doing business as Meritus Mutual  
21 Health Partners (“Meritus Mutual”) and Compass Cooperative Health Plan, Inc. dba  
22 Meritus Health Partners (“MHP”) (collectively referred to as the “Meritus Companies”),  
23 appointed pursuant to A.R.S. § 20-611, *et seq.*, hereby submits this Request for Hearing,  
24 Claim Determination and Setoff Related to Claims of the United States (“Petition for  
25 Setoff”) for the reasons set forth herein.

26 1. **Introduction.** Subject to and in accordance with the procedures established  
27 by this Court in the Order Approving Liquidation Plan dated March 8, 2017, claims have  
28 been submitted against the Meritus Companies by and on behalf of the United States

1 Department of Health and Human Services, Centers for Medicare & Medicaid Services  
2 (“CMS”) and by the United States Department of Justice (“DOJ”) in three separate proofs  
3 of claim (“POC’s”). At the same time, the Meritus Companies have claims against CMS.  
4 With this Petition for Setoff, the Receiver seeks: (i) scheduling a hearing at a date and  
5 time determined by the Court in the form of the attached proposed order;<sup>1</sup> (ii) a declaration  
6 as to claim priority level with respect to certain claims asserted by CMS and DOJ; and (iii)  
7 an Order from this Court approving a setoff of certain specified claims involving the  
8 Meritus Companies and CMS/DOJ.

9       **2. Background – Affordable Care Act.** The mutual claims between the  
10 Meritus Companies and CMS/DOJ are based upon the Affordable Care Act.<sup>2</sup>

11       **a. The ACA and Co-Ops.** In March of 2010, Congress passed the Affordable  
12 Care Act (“ACA”) in a dramatic overhaul of the nation’s healthcare system, reshaping the  
13 health insurance market through a series of “interlocking reforms” and programs designed  
14 to expand coverage in the individual and small group health insurance market. *King v.*  
15 *Burwell*, 135 S. Ct 2480, 2485 (U.S. 2015). The ACA prohibits insurers from denying  
16 coverage or setting premiums based on a person’s health; generally requires individuals to  
17 maintain health insurance coverage or make a payment to the Internal Revenue Service;  
18 and provides subsidies to low-income insurance purchasers through refundable tax credits.  
19 *Id.* at 2486-87. In conjunction with these reforms, the ACA created a network of “Health  
20 Benefit Exchanges” (“Exchanges”) on which insurers would offer “Qualified Health  
21 Plans” (“QHP’s”) to eligible purchasers.<sup>3</sup> It also created the Consumer Operated and

---

22 <sup>1</sup> In order to provide a full opportunity for responses and/or objections, if any, the Receiver requests that the hearing be  
23 scheduled at least seventy-five (75) days after the date of this filing.

24 <sup>2</sup> The Affordable Care Act has been the subject of extensive litigation and numerous petitions and court orders from  
25 around the country. A brief discussion is included here. For more thorough discussions of the Affordable Care Act, and  
26 related disputes, see, among others, *Moda Health Plan, Inc. v. United States*, 130 Fed. Cl. 436 (2017); *Molina*  
*Healthcare of California, Inc. et al. v. United States*, (United States Court of Federal Claims, No. 17-97C, filed August  
27 4, 2017); and *Liquidator’s Brief in Support of Motion to Approve the First Accounting and Status Report of the*  
*Liquidation Proceeding and the Acts Reported Therein*, filed on March 3, 2017 in The Matter of HealthyCT, Inc., in  
Liquidation, (Superior Court, Judicial District of Hartford, Docket No. HHD-CV16-6072516-S) (seeking approval of  
28 proposed set off under the ACA).

<sup>3</sup> Qualified Health Plans refers to those plans that met the criteria to be sold on the exchange. Only enrollees who  
purchased on the exchange were entitled to ACA Cost Share Reduction assistance. 45 CFR 155.20, Part 156, 155.1000,  
Part 156, subpart C. Eligible purchasers refers to those purchasers that provided financial information in order to  
qualify for Cost Share Reduction.

1 Oriented Plans Program (the “Co-Op Program”), which issued loans to help establish non-  
2 profit insurers to bring new competition into the insurance market in the form of Co-Ops,  
3 the creators of which had little or no experience with starting or running a health insurance  
4 company. 42 U.S.C. §§ 18031, 18041, 18042. The Meritus Companies were Co-Ops that  
5 offered QHPs on the exchange. They also offered health plans off the exchange in certain  
6 circumstances, though in those cases the enrollee would not qualify for Cost Share  
7 Reduction. Most Co-Op states had one C-Op that sold both PPO and HMO plans.  
8 However, due to Arizona’s licensing requirements, the Meritus Companies were affiliates,  
9 but had distinct insurance licenses. Meritus Mutual operated as a Preferred Provider  
10 Organization (“PPO”) while MHP operated as a Health Care Services Organization  
11 (“HCSO”).<sup>4</sup> The distinction in licenses drives important differences in the liquidation of  
12 the two companies. For example, a PPO would be covered by the Arizona Guaranty Fund  
13 while an HMO would not.<sup>5</sup> Also, in-network (or contract) providers of an HCSO have a  
14 lower priority level for claims than do out of network HCSO provider or PPO providers.<sup>6</sup>

15           **b. Federal Regulators – HHS and CMS.** The United States Department of  
16 Health and Human Services (“HHS”) is responsible for overseeing implementation of  
17 major provisions of the ACA and for administering certain programs thereunder, including  
18 the Co-Op Program. *See, e.g.*, 42 U.S.C. §§ 18041(a)(1), 18042(a)(1). HHS delegated  
19 many of its responsibilities under the ACA to CMS.

20           **c. Surplus Notes.** Section 1322 of the ACA authorized CMS to extend loans  
21 to qualified applicants to foster the creation of new Co-Ops.<sup>7</sup> The program was intended  
22 to improve consumer choice and plan accountability, promote integrated models of care,  
23 and enhance competition in the insurance market place, including on the exchanges  
24 established by the Act and off the Exchanges. *See* 42 U.S.C. § 18042. The program  
25 established two types of Co-Op loans: start-up loans, which were loans to provide

---

26 <sup>4</sup> While it is referred to as an HCSO in Arizona statutes and regulations, the more common term for the license is an  
27 HMO.

<sup>5</sup> See A.R.S. § 20-681(9)(d).

<sup>6</sup> See A.R.S. § 20-629(A)(7).

28 <sup>7</sup> While CMS “qualified” the applicants, CMS knew that the applicants had no experience creating or running a health  
insurance company.

1 assistance to Co-Ops in meeting their start-up costs; and solvency loans, which were loans  
2 to assist Co-Ops in meeting any state solvency requirements. In some cases, including  
3 here, the start-up loan was subsequently converted to a surplus note. The surplus notes  
4 (also referred to as converted start-up notes) and the solvency loans contained significant  
5 restrictions and limitations on repayment.

6 i. With respect to the surplus note, the purpose of amending the start-up  
7 note and converting it to a surplus note was to ensure that it was treated as a “surplus note  
8 pursuant to National Association of Insurance Commissioners Statement of Statutory  
9 Accounting Principles No. 41.” Among other things, that requires that any debt under the  
10 loan be subordinated to policyholders, claimant and beneficiary claims, and to all other  
11 classes of creditors other than surplus note holders. Additionally, the repayment  
12 obligations were subject to the Co-Op’s “ability to meet State Reserve Requirements and  
13 other solvency regulations, or requisite surplus note arrangements.”<sup>8</sup>

14 ii. With respect to the solvency loan, it was originally structured as a  
15 surplus note and was “expressly subordinated to claims of creditors and members” of the  
16 Co-Op. The solvency loan acknowledged that, in the event of insolvency, the solvency  
17 loan would be of equal rank with other surplus note holders (unless those surplus note  
18 holders agreed otherwise). Moreover, the solvency loan was not subject to security, offset  
19 or any form of recoupment.

20 d. **The “3Rs” Generally.** The changes to the health insurance market brought  
21 by the ACA created significant uncertainty for health insurers, particularly with respect to  
22 setting premium rates. Health insurers could no longer engage in medical underwriting  
23 and lacked data regarding millions of new consumers, including those with pre-existing  
24 health conditions, that were entering the health insurance market. To mitigate pricing risk,  
25 the ACA established three premium stabilization programs, known informally as the

26 \_\_\_\_\_  
27 <sup>8</sup>In Arizona, those solvency requirements include, among other things, that the holder’s interest is “subordinate to the  
28 claims of policyholders, claimants and beneficiaries and to all other classes of creditors other than surplus note holders  
and that interest payments and principal payments require prior approval of the director.” A.R.S. § 20-725.  
Additionally, in an insurance delinquency proceeding, the distribution priority for surplus note holders is Class 10,  
above only shareholders. A.R.S. § 20-629.

1 “3Rs”: a temporary risk corridor program (“Risk Corridor”); a permanent risk adjustment  
2 program (“Risk Adjustment”); and a transitional reinsurance program (“Reinsurance”). 42  
3 U.S.C. §§ 18061-18063. In addition, the ACA established premium subsidy and cost-  
4 sharing programs and imposed various fees (collectively, the “Affordable Care Act Fees”)  
5 on QHPs. The result of these programs is that at any given time, QHPs (including those  
6 sold by the Meritus Companies) may owe money to the United States under some  
7 programs and be owed money from the United States under other programs.

8           i. **Risk Corridor Program.** Section 1343 of the ACA established a  
9 temporary Risk Corridor program that applied to insurers who offered QHPs on an  
10 exchange for years 2014, 2015 and 2016. The Risk Corridor program provided that QHP  
11 issuers would receive compensation from the United States if their losses exceeded a  
12 certain defined amount due to higher-than-expected utilization and medical costs for the  
13 issuer’s insureds. At the same time, the Risk Corridor program provided that QHP issuers  
14 would pay the government a percentage of any unexpectedly high profits they made over  
15 similarly-defined amounts.<sup>9</sup> In appropriations acts for 2015 and 2016, Congress prohibited  
16 CMS and HHS from making risk corridor payments from funds appropriated under those  
17 acts. HHS and CMS adopted a “budget neutral” approach to the program in which only  
18 risk corridor collections from QHP issuers would be used to make risk corridor payments  
19 out to other QHP issuers. HHS also stated that distributions under the Risk Corridor  
20 program would be reduced pro rata to the extent of any shortfall. As a result, QHP issuers  
21 received less than 15% of amounts owed them for 2014 and nothing for amounts owed  
22 them for 2015. In response, there have been numerous lawsuits filed seeking payments  
23 under the Risk Corridor program. With Court approval, the Receiver (on behalf of Meritus  
24 and MHP) opted into a class action related to the Risk Corridor program. *See Health*  
25 *Republic Ins. Co. v. United States*, Case No. 1:16-cv-00259-MMS, United States Court of  
26 Federal Claims (the “Risk Corridor Class Action”). The Risk Corridor Class Action is

27 \_\_\_\_\_  
28 <sup>9</sup> QHPs collectively incurred compensable losses under the Risk Corridor Program of almost \$2.9 billion in 2014 and  
\$5.8 billion in 2015. *See Class Action Notice from Health Republic Ins. Co. v. United States*, Case No. 1:16-cv-00259-  
MMS, United States Court of Federal Claims.

1 currently stayed pending appeals of two other matters that had been brought in the Federal  
2 Claims Court and are on appeal before the Federal Circuit Court of Appeals. *See Moda*  
3 *Health Plan, Inc. v. United States*, Case No. 17-1994; *Land of Lincoln Mutual Health Ins.*  
4 *Co.*, Case No. 16-1224, and *see also Blue Cross and Blue Shield of North Carolina v.*  
5 *United States*, Case No. 17-2154.

6           ii. **Risk Adjustment Program.** Section 1343 of the ACA established a  
7 permanent Risk Adjustment program designed to protect against adverse selection by  
8 spreading the risk of insuring comparatively less healthy populations among insurers in a  
9 given state and to stabilize premiums for issuers of ACA-compliant coverage in the  
10 individual and small group markets. *See* 42 U.S.C. § 18063. Under the Risk Adjustment  
11 program, insurers are charged more if their actuarial risk is less than the average actuarial  
12 risk of all plans in that state for that year (that is, with plans whose populations are  
13 comparatively healthier) while insurers whose average actuarial risk is greater than  
14 average (that is, with plans whose populations are comparatively less healthy) receive  
15 payments from the program. The program is administered by CMS because Arizona  
16 elected not to do so. *See* 42 U.S.C. § 18041(c). As a result, the Risk Adjustment program  
17 also includes a user fee based on qualifying business in states such as Arizona where CMS  
18 administers the program. *See* 45 C.F.R. § 153.610(f).

19           iii. **Reinsurance Program.** The Reinsurance program is addressed  
20 under section 1341 of the ACA (42 U.S.C. § 18061) and under 45 C.F.R. § 153.200 and  
21 provides for circumstances under which insurers with QHPs might be required to make  
22 payments (generally referred to as “required contributions”) to a designated reinsurance  
23 entity and also might be entitled to receive Reinsurance payments. With respect to  
24 required contributions, HHS established a methodology to collect a per enrollee amount  
25 based on plan enrollment. 45 C.F.R. § 153.400. With respect to receiving payments, 45  
26 C.F.R. § 153.200 provides that, under certain circumstances, health insurance issuers  
27 would be eligible to receive Reinsurance payments when claims costs for an individual  
28 enrollee’s covered benefits in a benefit year exceed an attachment point. Essentially, if an

1 enrollee’s total claims exceed a specified level (the “attachment point”), the insurer would  
2 be paid a proportion of claims costs (the “coinsurance rate”) beyond the attachment point  
3 until total claims costs reached a cap (the “reinsurance cap”). HHS has previously  
4 published attachment points, coinsurance rates, and reinsurance caps, the payment  
5 parameters of the Reinsurance program.

6 **iv. Cost-Sharing Reduction Reconciliation Program.** While not  
7 typically included in the “3-Rs,” a reconciliation associated with the Cost-Sharing  
8 Reductions (“CSR”) also contributes to debts owing between insurers that offered QHPs  
9 and the United States.<sup>10</sup> The CSR is a subsidy created by the ACA to reduce the cost-  
10 sharing expenses of low- and middle-income individuals who purchase health insurance  
11 through a health insurance Exchange. *See generally* 42 U.S.C. § 18071. Because the  
12 monthly advances of CSRs are based on estimates, they are subject to reconciliation after  
13 calculation of the actual amount of CSRs provided to eligible enrollees, with payment  
14 amounts payable to/from the United States and/or the QHP. *See* 45 C.F.R. § 156.430(c)-  
15 (e).

16 **3. United States Claims against the Meritus Companies.** Three Proofs of Claims  
17 (“POC”s) were submitted by or on behalf of the United States in the receivership  
18 proceedings, including: (i) a POC filed by HHS/CMS against MHP for a total amount of  
19 \$50,650,123.02 (the “CMS-MHP Claims”); (ii) a POC filed by HHS/CMS against Meritus  
20 Mutual for a total amount of \$94,581,998.78 (the “CMS-Meritus Mutual Claims”) and (iii)  
21 a POC filed by the DOJ against both MHP and Meritus Mutual for an undetermined  
22 amount essentially seeking recovery of all amounts owed to the United States (“DOJ  
23 Claims”).

24 . . .

25 . . .

26 . . .

27 . . .

---

28 <sup>10</sup> As noted in the CMS claims, there are other smaller programs under the ACA generating amounts due that are also included in the setoff analysis herein and addressed in Exhibits 5 and 6.

1 a. **Claims against MHP.** With respect to the CMS-MHP Claims, the asserted  
2 claim amounts attributable to the specific ACA Risk-Sharing Programs<sup>11</sup> referenced herein  
3 are as follows (see Exhibit 1):

4	CSR:	\$ 3,899,178.47
5	PPACA Reinsurance: <sup>12</sup>	\$ 510,975.30
6	Risk Adjustment:	\$ 46,195,827.78
7	PPACA Fee:	\$ 44,141.47
8	Total:	\$ 50,650,123.02

9 b. **Claims against Meritus Mutual.** With respect to the CMS-Meritus Mutual  
10 Claims, the asserted claim amounts were attributable to the loan and note claims and to the  
11 ACA Risk-Sharing Programs as follows (see Exhibit 2):

12 **Loan/Note Claims:**

13	Start-Up Loan:	\$ 20,890,333.00
14	Solvency Note:	\$ 72,935,928.25
15	Total:	\$ 93,826,261.25

16 **ACA Related Claims:**

17	CSR:	\$ 115,649.36
18	PPACA Reinsurance: <sup>13</sup>	\$ 46,091.54
19	Risk Adjustment:	\$ 594,168.87
20	Exchange User-Fee:	\$ 7.76
21	Total:	\$ 755,917.53

22 c. **DOJ Claims.** With respect to the DOJ Claims, no claim amount was  
23 specified. However, the claimant identified the nature of the claim and asserted rights  
24 associated with set-offs and security, with the following statements (see Exhibit 3):<sup>14</sup>

25 <sup>11</sup> For purposes of this Petition, ACA Risk-Sharing Programs that are the subject of the setoff include the Risk Corridor,  
26 Reinsurance, CSR, PPACA Reinsurance, Risk Adjustment, and Exchange User-Fee/PPACA Fee. The ACA Risk-  
Sharing Programs as defined herein do not include the surplus note claims which by their terms are not subject to setoff.

27 <sup>12</sup> As explained in Exhibits 1 and 2, the PPACA Reinsurance claim asserted by CMS differs from the transitional  
28 Reinsurance program. This distinction is noted, but not explained in footnote 4 of the CMS-MHP Claims and in  
footnote 5 of the CMS-Meritus Mutual Claims.

<sup>13</sup> Same as above reinsurance comment.

<sup>14</sup> Essentially identical statements were incorporated in the CMS-MHP Claims and the CMS-Meritus Mutual Claims.



1 i. With respect to the nature of the claim, the DOJ Claim states:

2 Recovery of amounts owed to the United States  
3 and/or any federal agency or entity. These  
4 claims are entitled to first priority treatment  
5 pursuant to 31 U.S.C. § 3713.

6 ii. With respect to set-offs, the DOJ Claim states:

7 The United States reserves the right to amend these claims to  
8 assert subsequently discovered liabilities. The United States  
9 may hold estimated debts owed to the estate that are subject to  
10 set-off and/or recoupment rights. The United States hereby  
11 expressly reserves its right to set-off or recoup any claim  
12 against debts owed to the estate by any federal agency or  
13 entity.

14 iii. With respect to security for the claim, the DOJ Claim states:

15 These claims are entitled to treatment as secured claims to the  
16 extent they are subject to set-off by a claim of the estate against  
17 any United States agency or entity. The United States is a  
18 unitary creditor for purposes of set-off and recoupment.

19 **4. Jurisdiction.**

20 a. This Court is vested with exclusive original jurisdiction of insurer  
21 receiverships and is authorized to make all necessary and proper orders to carry out the  
22 purposes of A.R.S. § 20-601, *et seq.* (the “Arizona Receivership Act”). A.R.S. § 20-  
23 612(A). Among other things, one of the purposes of the Arizona Receivership Act is to  
24 provide an exclusive forum to hear and determine claims against the Meritus Companies.  
25 *See* A.R.S. § 30-628.

26 b. CMS and DOJ have filed POCs against MHP and Meritus Mutual in these  
27 receivership proceedings asserting claims for amounts due under the ACA and in response  
28 to the POC process ordered by this Court. As a result, this Court has jurisdiction with  
respect to the determination and adjudication of those claims under the Arizona  
Receivership Act. Courts have concluded that insurance insolvency proceedings “are  
analogous to proceedings in bankruptcy” and thus those Courts have looked to “federal

1 bankruptcy law for guidance,” particularly regarding jurisdictional issues. *Garamendi v.*  
2 *Executive Life Ins. Co.*, 17 Cal. App. 4th 504, 516, 21 Cal. Rptr. 2d 578, 585 (1993). The  
3 jurisdictional rule consistently followed by courts applying bankruptcy law to questions of  
4 jurisdiction associated with a proof of claim filing is as follows:

5 [A] creditor who files a proof of claim against the estate of a bankrupt consents  
6 to the jurisdiction of the bankruptcy court for a full determination of the claims  
7 between the creditor and the estate. Indeed, the Supreme Court has held that  
8 filing a proof of claim waives such entitlements as a creditor’s Seventh  
9 Amendment right to a jury trial; the right of a state or commonwealth to invoke  
10 sovereign immunity under the Eleventh Amendment; and of relevance here, the  
11 right to have private claims heard by an Article III court as established in  
12 *Katchen.*” *In re Applied Thermal Systems, Inc. v. Zeeco, Inc.*, 294 B.R. 784, 788  
13 (Bankr. N.D. Okla. 2003) (citing *Wiswall v. Campbell*, 93 U.S. 347, 351, 23 L.  
14 Ed. 923 (1876); *Gardner v. New Jersey*, 239 U.S. 565, 573, 91 L. Ed. 504, 67 S.  
15 Ct. 467 (1947); *Katchen v. Landy*, 382 U.S. 323, 15 L. Ed. 2d 391, 86 S. Ct. 467  
16 (1966); and *Langenkamp v. Culp*, 498 U.S. 42, 44, 112 L. Ed. 2d 343, 111 S. Ct.  
17 330 (1990)).

18 5. **Surplus Notes – Class 10 Priority Level Determination.** The first item to  
19 be addressed in the claims asserted by CMS is the priority level of the claims for notes  
20 (start-up note and solvency note) against Meritus Mutual, which combined total  
21 \$93,826,261.25 (collectively, the “CMS Surplus Notes”). It is well-established under  
22 Arizona law that surplus notes must be assigned a Class 10 priority level and the CMS  
23 Surplus Notes are no different.<sup>15</sup> Section 20-629(A)(10), A.R.S., provides as follows:

24 In a delinquency proceeding against an insurer domiciled in  
25 this state, the priority of distribution of claims from the general  
26 assets of the insurer shall be determined pursuant to this  
27 section. Every claim in each class shall be paid in full or  
28 adequate funds shall be reserved for the payment before the  
members of the next class may receive any payment.  
Subclasses may not be established within any class. The order  
of distribution is as follows:

\*\*\*

---

<sup>15</sup> This low recovery priority level is consistent with Arizona law which requires that, with respect to surplus notes, the holder’s interests shall be “subordinate to the claims of policyholders, claimants and beneficiaries and to all other classes of creditors other than surplus note holders and that interest payments and principal payments require prior approval of the director.” A.R.S. § 20-725.

1                   10. Claims of surplus note or certificate of contribution  
2                   holders or other similar obligations and for premium refunds  
3                   on assessable policies

4                   a. **Converted Start-Up Note.** The first of the two notes that were the basis for  
5 the CMS claims is referred to as the start-up note and was asserted to have an amount due  
6 of \$20,890,333.00. A copy of the start-up note was included with the CMS-Meritus  
7 Mutual Claim. (See Exhibit 2.) As acknowledged by CMS in its claim, the start-up note  
8 was amended and converted to a surplus note. (See Exhibit 2.) As amended, the start-up  
9 note requires that it be treated as “surplus note pursuant to National Association of  
10 Insurance Commissioners Statement of Statutory Accounting Principles No. 41.” Among  
11 other things, that requires that any debt under the loan be subordinated to policyholders,  
12 claimant and beneficiary claims, and to all other classes of creditors other than surplus note  
13 holders. Additionally, the repayment obligations were subject to the Co-Op’s “ability to  
14 meet State Reserve Requirements and other solvency regulations, or requisite surplus note  
15 arrangements.” Thus, the plain language of the note, agreed to and signed by CMS,  
16 requires that the start-up note be determined to be a Class 10 priority level claim against  
17 Meritus Mutual.<sup>16</sup>

18                   b. **Solvency Note.** The second note that forms the basis of the CMS claim is  
19 referred to as the solvency note and was asserted to have an amount due of  
20 \$72,935,928.25. A copy of the solvency note was included with the CMS-Meritus Mutual  
21 Claim. (See Exhibit 2.) Similar to the converted start-up note, the solvency note  
22 acknowledged that, in the event of insolvency, any claims for payment under the solvency  
23 note would be of equal rank with claims of other surplus note holders (unless those surplus  
24 note holders agreed otherwise). Moreover, the solvency note was not subject to security,  
25 offset or any form of recoupment. Thus, just like the converted start-up note, the plain  
26 language of the solvency loan indisputably requires that any claims be categorized at the  
27 Class 10 priority level against Meritus Mutual.

28  

---

<sup>16</sup> Consistent with this Court’s Order dated September 25, 2017, if it ever appears that there could be a distribution to Class 10 level claimants, then it would be necessary to determine the amount of the Class 10 claim. Until that time, the amount of the Class 10 claim need not be determined.

1 c. **Notice to CMS.** In accordance with A.R.S. § 20-628, the Receiver has  
2 provided CMS with notice of its claim determination regarding the surplus notes as Class  
3 10 Claims against Meritus Mutual. See Exhibit 6. As part of that notice, the Receiver  
4 asked CMS to notify it if it had any objection and, in that event, to provide all available  
5 support for CMS's position. To date, there has been no substantive response. The  
6 Receiver shall also send notice to CMS of the hearing after it is scheduled.

7 d. **Requested Declaration – Class 10 Claims.** In light of the express language  
8 from the converted start-up note and the solvency note, the Receiver requests that the  
9 Court enter an Order that establishes CMS's claims under the converted start-up note and  
10 the solvency note as Class 10 priority level claims with the amount of such claims to be  
11 determined only if it appears likely that a distribution will be made to Class 10 priority  
12 level claimants.

13 6. **Claims of the Meritus Companies against CMS.** As noted above in the  
14 discussion of debts and obligations under the ACA, in addition to the Meritus Companies  
15 owing debts to CMS, CMS owes substantial debts to the Meritus Companies. Specifically,  
16 CMS owes MHP \$55,513,299 under the Risk Corridor program and \$7,171,320 under the  
17 Reinsurance program. Likewise, CMS owes Meritus Mutual 12,938,057 under the Risk  
18 Corridor program and \$3,283,275 under the Reinsurance program. (See Exhibit 4.) The  
19 Receiver has been vested by operation of law with title to all of the property of the Meritus  
20 Companies (including rights of action for unpaid claims due under the ACA) and has been  
21 ordered to liquidate and reduce the assets to possession. A.R.S. § 20-624(B).

22 a. **Risk Corridor.** Efforts by insurers to collect payments due under the Risk  
23 Corridor program has generated substantial litigation. Currently, the U.S. Court of Federal  
24 Claims is adjudicating at least 26 claims for payment under the Risk Corridor program.  
25 *See Molina Healthcare of California, Inc., et al. v. United States*, U.S. Court of Federal  
26 Claims, Case No. 17-97C, Order dated August 4, 2017, page 17. Among the 26 lawsuits is  
27 a class action against the United States for payments under the Risk Corridor program. *See*  
28 *Health Republic Ins. Co. v. United States*, U.S. Court of Federal Claims, Case No. 16-cv-

1 00259 MMS. In accordance with this Court’s May 4, 2017 Order Re Petition No. 10  
2 Approving Contingency Fee Arrangement for Risk Corridor Suit, Meritus Mutual and  
3 MHP are participating in the Risk Corridor Class Action, which is currently stayed  
4 pending appeals before the Federal Circuit involving other Risk Corridor lawsuits.<sup>17</sup>  
5 MHP’s Risk Corridor claims against CMS total \$55,513,299 while Meritus Mutual’s Risk  
6 Corridor claims against CMS total \$12,938,057. (Exhibit 4.) After the setoff  
7 contemplated herein is implemented, the Receiver currently anticipates that recovery  
8 efforts associated with the remaining balance due to the Meritus Companies would  
9 continue to be prosecuted in the Risk Corridor Class Action.

10           b. **Reinsurance.** In addition to amounts due under the Risk Corridor claims,  
11 CMS also owes MHP and Meritus Mutual significant amounts under the Reinsurance  
12 programs described above. Specifically, MHP has an unpaid claim against CMS under the  
13 Reinsurance program in the amount of \$7,171,320. (Exhibit 4.) Likewise, Meritus Mutual  
14 has an unpaid claim against CMS under the Reinsurance program in the amount of  
15 \$3,283,275. (Exhibit 4.) Other insurers and receivers of insolvent insurers have similar  
16 debts and have pursued different strategies in an attempt to recover those amounts.

17           i. For example, in two recent cases, liquidators have filed Complaints in  
18 the United States Court of Federal Claims including causes of actions for payments under  
19 the Reinsurance program. *See, e.g., Vullo (as Liquidator of Health Republic Ins. Of New*  
20 *York) v. United States*, U.S. Court of Federal Claims, Case No. 17-1185C, filed on  
21 September 1, 2017, Complaint, Second Cause of Action; and *Atkins (as Liquidator of*  
22 *Kentucky Health Cooperative) v. United States*, U.S. Court of Federal Claims, Case No.  
23 17-1108C, filed on August 16, 2017, Complaint Paragraphs 63-68.

---

24  
25 <sup>17</sup> The Risk Corridor Class Action has been stayed pending certain appeals to the United States Court of Appeals for the  
26 Federal Circuit (“Federal Circuit”). On June 14, 2018, the Federal Circuit entered an Order in *Moda Health Plan, Inc.*  
27 *v. United States*, 2017-1994. The Federal Circuit ruled that the United States is obligated to pay participants in the  
28 health benefit exchanges the full amount indicated by the statutory formula for payments out under the risk corridors  
program. *Id.*, Document 87-1. Page 19. However, the Federal Circuit also ruled that Congress temporarily suspended  
payments on the risk corridors program beyond the sum of payments in. *Id.*, Document 87-1. Pages 20-31. That  
decision remains subject to motions to reconsider.

1                   ii. Alternatively, in a recent petition, a liquidator sought to have the  
2 receivership court impose a set-off related to payments due under the Reinsurance  
3 Program. *See Motion to Approve the First Accounting and Status Report of the*  
4 *Liquidation Proceeding and the Acts Reported Therein, in In re HealthyCT, Inc., in*  
5 *Liquidation*, Superior Court, Judicial District of Hartford, Connecticut, Docket No.  
6 HHD0CV16-6072516-S, filed on February 17, 2017.

7                   iii. After the setoff contemplated herein is implemented, the Receiver  
8 anticipates seeking recovery of the amounts due under the Reinsurance Program, including  
9 but not limited to by means of commencing a judicial action, depending on the  
10 circumstances.

11           7.       **Liquidation Act Authority for Offsets.** Under the Arizona Liquidation  
12 Act, A.R.S. § 20-638, setoff of mutual debts or mutual credits as contemplated in this  
13 Petition is expressly authorized, as follows:

14                   A. In all cases of mutual debts or mutual credits between the  
15 insurer and another person in connection with any action or  
16 proceeding under this article, such credits and debts shall be set  
17 off and the balance only shall be allowed or paid, except as  
18 provided in subsection B of this section.

19                   B. No offset shall be allowed in favor of any such person  
20 where the obligation of the insurer to such person would not at  
21 the date of the entry of any liquidation order or otherwise as  
22 provided in section 20-635,<sup>18</sup> entitle him to share as a claimant  
23 in the assets of the insurer,

24                   \*\*\*

25           8.       **Setoff – ACA Risk-Sharing Programs.**

26                   a. **Setoff and Notice to CMS.** CMS asserts that each claim is entitled to  
27 treatment as a secured claim to the extent it is subject to set-off by claims of the Meritus  
28

---

<sup>18</sup> A.R.S. § 20-635 provides: “The rights and liabilities of the insurer and of its creditors, policyholders, stockholders, members, subscribers and all other persons interested in its estate shall, unless otherwise directed by the court, be fixed as of the date on which the order directing the liquidation of the insurer is filed in the office of the clerk of the court which made the order, subject to the provisions of this article with respect to the rights of claimants holding contingent claims.”

1 companies.<sup>19</sup> (See Exhibits 1 and 2). As set forth in the chart below, the Receiver has set  
2 off amounts due and owed under the ACA Risk-Sharing Programs, subject to this Court's  
3 approval, that would leave approximately \$17 million still due to the Meritus Companies  
4 under the Risks Corridor program and approximately \$10 million still due to the Meritus  
5 Companies under the Reinsurance program. (See Exhibit 4 for additional details and  
6 support regarding the following charts.) In accordance with A.R.S. § 20-628, the Receiver  
7 has provided CMS and DOJ with notice of its setoff of these amounts. See Exhibits 5, 6  
8 and 7. As part of that notice, the Receiver asked CMS and DOJ to notify it if it had any  
9 objection and, in that event, to provide all available support for their position. To date,  
10 there has been no substantive response. The Receiver shall provide a copy of this Petition  
11 and also provide notice to CMS and DOJ of the hearing after it is scheduled.

12           **b. MHP Setoff - Generally.** With respect to MHP, the setoff analysis  
13 associated with the ACA Risk-Sharing Programs is as follows (see Exhibit 5):

14           The following amounts are owed by CMS to MHP:

15           Risk Corridor Claims:	\$ 55,513,299.00
16           Reinsurance:	\$ 7,171,320.00
17           Total:	\$ 62,684,619.00

18           The following amounts were submitted as claims by the United States  
19 against MHP:

20           CSR:	\$ 3,899,178.47
21           PPACA Reinsurance:	\$ 510,975.30
22           Risk Adjustment:	\$ 46,195,827.78
23           PPACA Fee:	\$ 44,141.47
24           Total:	\$ 50,650,123.02

25           After application of a setoff, the remaining debt owed by CMS to MHP is  
26 \$12,034,495.98 with all related mutual debts and credits setoff and otherwise  
deemed satisfied.

27 \_\_\_\_\_  
28 <sup>19</sup> Under A.R.S. § 20-629(E), the “owner of a secured claim \*\*\* may surrender the owner’s security and file the  
owner’s claim as a general creditor, or the claim may be discharged by resort to the security, in which case the  
deficiency, if any, shall be treated as a claim against the general assets of the insurer on the same basis as claims of  
unsecured creditors.”

1 c. **MHP Setoff – Specific Programs.** With respect to the specific ACA Risk-  
2 Sharing Programs, the setoff allocation proposed by the Receiver is set forth below.

3 Risk Corridor Claims due from  
4 CMS to MHP: \$55,513,299.00

5 (MINUS)  
6 Total Due from MHP to CMS: \$50,650,123.00

7 (EQUALS)  
8 Net Risk Corridor Claims due from  
9 CMS to MHP: \$4,863,176.00

10 The total amount of the Risk Corridor Claims exceeds the amount due to CMS under the  
11 ACA Risk-Sharing Programs. As a result, there is no setoff applicable to reduce the  
12 amount of the Reinsurance Claims.

13 Reinsurance Claims due from  
14 CMS to MHP: \$ 7,171,320.00

15 (MINUS)  
16 Balance Due from MHP to CMS: \$ 0.00

17 (EQUALS)  
18 Net Reinsurance Claims due from  
19 CMS to MHP: \$ 7,171,320.00

20 d. **Meritus Mutual Setoff - Generally.** With respect to Meritus Mutual, the  
21 setoff analysis associated with the ACA Risk-Sharing Programs claims is as follows (see  
22 Exhibit 6):

23 The following amounts are owed by CMS to Meritus Mutual:

24 Risk Corridor Claims: \$ 12,938,057.00

25 Reinsurance: \$ 3,283,275.00

26 Total: \$ 16,221,332.00

27 The following amounts were submitted as claims by the United States  
28 against Meritus Mutual:

29 CSR: \$ 115,649.36

30 PPACA Reinsurance: \$ 46,091.54



Risk Adjustment:	\$594,168.87
Exchange User-Fee:	\$ 7.76
Total:	\$755,917.53

After application of a setoff, the remaining debt owed to Meritus Mutual is \$15,465,414.47 with all related mutual debts and credits setoff and otherwise deemed satisfied.

e. **Meritus Mutual Setff – Specific Programs.** With respect to the specific ACA Risk-Sharing Programs, the setoff allocation proposed by the Receiver is set forth below.

Risk Corridor Claims due from CMS to Meritus Mutual:	\$12,938,057.00
(MINUS)	
Total Due from Meritus Mutual to CMS:	\$ 755,917.00
(EQUALS)	
Net Risk Corridor Claims due from CMS to Meritus Mutual:	\$12,182,140.00

The total amount of the Risk Corridor Claims exceeds the amount due to CMS under the ACA Risk-Sharing Programs. As a result, there is no setoff applicable to reduce the amount of the Reinsurance Claims.

Reinsurance Claims due from CMS to Meritus Mutual:	\$ 3,283,275.00
(MINUS)	
Balance Due from Meritus Mutual to CMS:	\$ 0.00
(EQUALS)	
Net Reinsurance Claims due from CMS to Meritus Mutual:	\$ 3,283,275.00

9. **Continuing Participation in Risk Corridor Class Action.** After the setoff has been implemented, MHP and Meritus Mutual will have claims against CMS under the Risk Corridor program in the following amounts, respectively:

1 Net Risk Corridor Claims  
due to MHP: \$ 4,863,176.00

2 Net Risk Corridor Claims  
3 due to Meritus Mutual: \$ 12,182,140.00

4 The net amount due under the Risk Corridor program would continue to be prosecuted in  
5 the Risk Corridor Class Action currently stayed in the Federal Claims Court.

6 **10. Prosecution of Reinsurance Claims.** After the setoff has been implemented, MHP  
7 and Meritus Mutual will have claims against CMS under the Reinsurance program in the  
8 following amounts, respectively:

9 Net Reinsurance Claims  
10 due to MHP: \$ 7,171,320.00

11 Net Reinsurance Claims  
12 due to Meritus Mutual: \$ 3,283,275.00

13 The Receiver, in his discretion, may seek to prosecute the claims of MHP and of Meritus  
14 Mutual under the Reinsurance program against CMS in the Federal Claims Court or such  
15 other forum determined by the Receiver as reasonable and appropriate under the  
16 circumstances, and/or to negotiate the potential resolution of such claims, if possible.

17 **11. Limit to CMS Claims.** This Petition is limited to the claims related to the surplus  
18 notes and the ACA Risk-Sharing Programs as asserted by CMS under the two POCs,  
19 including the CMS-MHP Claim and the CMS-Meritus Mutual Claim. It is not intended to  
20 address or resolve issues unrelated to the ACA Risk-Sharing Programs and/or to the  
21 surplus notes that were raised in the DOJ Claim. The Receiver reserves the right to  
22 proceed with the existing DOJ program that allows for a Receiver to request a release from  
23 the United States (for matters other than tax) before closing an estate, subject to any setoff  
24 orders that may be entered by this Court.

25 WHEREFORE, the Receiver requests that the Court enter an Order:

26 (1) Approving the Receiver's Request for Claim Determination and Setoff  
27 Related to Claims of the United States and granting the relief requested therein;  
28

1 (2) Determining that CMS’s claims for payment from Meritus Mutual under the  
2 converted start-up note and the solvency note are Class 10 priority level claims under  
3 A.R.S. § 20-629;

4 (3) Deferring any determination as to the amount of CMS’s claims for payment  
5 from Meritus Mutual under the converted start-up note and the solvency note unless and  
6 until such time as the Receiver reasonably anticipates that there may be a distribution for  
7 Class 10 level claimants;

8 (4) Approving the setoff of all claims as between MHP and CMS under the  
9 ACA Risk-Sharing Programs, including but not limited to CSR, Reinsurance, Risk  
10 Adjustment, and Risk Corridor, so that the net effect is that the remaining amount that  
11 CMS owes MHP under the ACA Risk-Sharing Programs (with all related mutual debts and  
12 credits setoff and otherwise deemed satisfied) is as follows:

13 Net Risk Corridor Claims  
14 due to MHP: \$ 4,863,176.00

15 Net Reinsurance Claims  
16 due to MHP: \$ 7,171,320.00

17 (5) Approving the setoff of all claims as between Meritus Mutual and CMS  
18 under the ACA Risk-Sharing Programs, including but not limited to CSR, Reinsurance,  
19 Risk Adjustment, and Risk Corridor, so that the net effect is that the remaining amount that  
20 CMS owes Meritus Mutual under the ACA Risk-Sharing Programs (with all related mutual  
21 debts and credits setoff and otherwise deemed satisfied) is as follows:

22 Net Risk Corridor Claims  
23 due to Meritus Mutual: \$ 12,182,140.00

24 Net Reinsurance Claims  
25 due to Meritus Mutual: \$ 3,283,275.00

26 (6) Ordering that, pursuant to A.R.S. § 20-624 and paragraphs 8 and 10 of the  
27 August 10, 2016 Order for Appointment of Receiver and Injunction (the “Receivership  
28 Order”), the Receiver may institute, prosecute and/or compromise any suits, actions and/or

1 claims related to the Risk Corridor Claims, including the continued participation as a class  
2 member in the Risk Corridor Class Action;

3 (7) Ordering that, pursuant to A.R.S. § 20-624 and paragraphs 8 and 10 of the  
4 Receivership Order, the Receiver may institute, prosecute and/or compromise any suits,  
5 actions, and/or claims related to the Reinsurance Claims, including but not limited to  
6 prosecution of claims of MHP and Meritus Mutual against CMS in the Federal Court of  
7 Claims or such other forum determined by the Receiver as reasonable and appropriate  
8 under the circumstances, and/or to negotiate the resolution of such claims; and

9 (8) Granting such further relief as the Court deems reasonable and necessary  
10 under the circumstances.

11 Dated this 11th day of December, 2018.

12 FAEGRE BAKER DANIELS LLP

13 By: /s/ Joel Glover (#034018)  
14 Joel A. Glover

15 *Attorneys for Receiver*

16  
17  
18 COPY of the foregoing mailed this  
19 11th day of December, 2018 to the  
20 attached Master Service List

21 /s/ Brenda McHenry  
22 Brenda McHenry

1 SUPERIOR COURT OF ARIZONA

2 COUNTY OF MARICOPA

3  
4 No. CV2016-011872 (Assigned to The Honorable Daniel Martin)

5 **MASTER SERVICE LIST**

6 Keith Schraad, Receiver  
7 Interim Director  
8 Arizona Department of Insurance  
9 100 North 15th Avenue, #102  
Phoenix, Arizona 85007

10 Liane Kido, Deputy Receiver  
11 Arizona Department of Insurance  
12 100 North 15th Avenue, #102  
Phoenix, Arizona 85007

13 Lynette Evans, Assistant Attorney General  
14 Office of the Attorney General  
15 1275 West Washington Street  
16 Phoenix, Arizona 85007  
*Attorneys for Arizona Department of Insurance*

17 Richard G. Erickson  
18 Robert F. Kethcart  
19 Snell & Wilmer L.L.P.  
20 One Arizona Center  
21 400 East Van Buren  
Phoenix, Arizona 85004  
*Attorneys for Defendants*

22 Richard J. Voth, Sr.  
23 P.O. Box 3970  
Pinetop, Arizona 85935

24 Larry Aldrich, Executive Chairman  
25 Employers Health Alliance of Arizona  
26 7520 East McLellan Lane  
Scottsdale, Arizona 85250

1 Christophe Burusco  
2 Sidley Austin LLP  
3 555 West 5th Street, 40th Floor  
4 Los Angeles, California 90013  
5 *Attorneys for Care1st Health Plan Administrative Services, Inc.*

6 Matthew A. Clemente  
7 Sidley Austin LLP  
8 One South Dearborn  
9 Chicago, Illinois 60603  
10 *Attorneys for Care1st Health Plan Administrative Services, Inc.*

11 Michael Surguine, Executive Director  
12 Arizona Life & Disability  
13 Insurance Guaranty Fund  
14 2910 North 44th Street, Suite 201 (2nd Floor)  
15 Phoenix, Arizona 85018

16 Darren Ellingson  
17 Special Deputy Receiver  
18 Raintree Corporate Center I  
19 15333 North Pima Road, Suite 305  
20 Scottsdale, Arizona 85260

21 Banner Health  
22 Patient Financial Services  
23 Attn: Anna Rosalez, Manager  
24 525 West Brown Road, Third Floor  
25 Mesa, Arizona 85201

26 S. David Childers  
27 Kutak Rock LLP  
28 8601 North Scottsdale Road, Suite 300  
Scottsdale, Arizona 85253

Ortencia Solis  
Arrowhead Pediatrics  
Billing Department Insurance Rejections  
17215 North 72nd Drive  
Building D, Suite 140B  
Glendale, Arizona 85308

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

Debbie Bailey  
Cactus Children’s Clinic, PC  
5940 West Union Hills Drive  
Suite D100  
Glendale, Arizona 85308

Monica Gaspari  
Billing Office Supervisor  
Pima Heart Physicians  
3709 North Campbell Avenue  
Suite 201  
Tucson, Arizona 85719

United States Department of Justice  
40 North Central Avenue, #1800  
Phoenix, Arizona 85004

U.S. Department of Justice  
950 Pennsylvania Avenue, NW  
Washington, DC 20530

United States Attorney General  
U.S. Department of Justice  
950 Pennsylvania Avenue, NW  
Washington, DC 20530

U.S. Centers for Medicare & Medicaid Services  
7500 Security Boulevard  
Baltimore, Maryland 21244

Sinead Baldwin  
1200 Brickell Avenue  
PH 2000  
Miami, Florida 33131  
*Attorneys for HealthSouth Rehabilitation Hospital*

Jill Wright  
Parallon  
1100 Charlotte Avenue  
Suite 1600  
Nashville, Tennessee 37203

1  
2  
3  
4  
5  
6  
7  
8  
9  
10  
11  
12  
13  
14  
15  
16  
17  
18  
19  
20  
21  
22  
23  
24  
25  
26  
27  
28

D.B. Udall  
Udall Law Firm LLP  
4801 East Broadway Boulevard  
Suite 400  
Tucson, Arizona 85711  
*Attorneys for Sarah McMahon*

Susan Sweat  
Ambulance Billing Office Supervisor  
Bullhead City Fire Department  
1260 Hancock Road  
Bullhead City, Arizona 86442

Justin J. Henderson  
Lewis Roca Rothgerber Christie LLP  
201 East Washington Street, Suite 1200  
Phoenix, Arizona 85004-2595  
*Attorneys for Receiver*