

**Report of the
Market Conduct Examination
for
Massachusetts Division of Insurance**

of

**The HealthMarkets Companies
NAIC Group #0264**

**The MEGA Life and Health Insurance Company
NAIC #97055
9151 Boulevard 26
North Richland Hills, Texas 76180**

**Midwest National Life Insurance Company of Tennessee
NAIC #66087
9151 Boulevard 26
North Richland Hills, Texas 76180**

**The Chesapeake Life Insurance Company
NAIC #61832
9151 Boulevard 26
North Richland Hills, Texas 76180**

August 26, 2009

Honorable Nonnie S. Burnes
Commissioner of Insurance
Division of Insurance
Commonwealth of Massachusetts
One South Station
Boston, MA 02110-2208

Dear Commissioner Burnes:

Pursuant to your instructions and in accordance with Massachusetts General Laws, Chapter 175, Section 4, a targeted re-examination has been made of the market conduct affairs of

The MEGA Life and Health Insurance Company
Midwest National Life Insurance Company of Tennessee
The Chesapeake Life Insurance Company
(collectively, "The Company")

at its home office located at:

9151 Boulevard 26
North Richland Hills, TX 76180

The following report thereon is respectfully submitted.

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Foreword

This report on the market conduct examination of the Company is provided pursuant to the *NAIC Market Regulation Handbook* and is made by exception. Additional practices, procedures and files subject to review during the examination were omitted from the report if no improprieties were noted.

Profile of HealthMarkets

The HealthMarkets Group¹ is composed of three companies: The MEGA Life and Health Insurance Company (“MEGA”), Mid-West National Life Insurance Company of Tennessee (“Mid-West”) and The Chesapeake Life Insurance Company (“Chesapeake”). MEGA is an insurer domiciled in the State of Oklahoma that writes health insurance in all states except New York. Mid-West is an insurer domiciled in the State of Texas that writes health insurance in all states except Maine, New Hampshire, New York and Vermont. Chesapeake is an insurer domiciled in the State of Oklahoma that writes health insurance in all states except New Jersey, New York, and Vermont. Although all three of the companies wrote coverage in Massachusetts during the examination period of January 1, 2008 to December 31, 2008, due to the limited writings in Massachusetts, Chesapeake’s, business was excluded from this examination.

Background

Regulatory Settlement Agreement

In December 2006, the Company and the Massachusetts Division of Insurance (“Division”) entered into a Regulatory Settlement Agreement (“RSA”) following the conclusion of two examinations conducted by INS Regulatory Insurance Services, Inc. (“INS”). The RSA had several key objectives: to implement a meaningful claim reassessment process; to implement significant revisions to oversight of producer practices; to make changes to how

¹ HealthMarkets was formerly known as UICI. Effective April 5, 2006, HealthMarkets (formerly UICI) was purchased by The Blackstone Group, Goldman Sachs Capital Partners and DLJ Merchant Banking Partners, each of which is a private equity firm. Following the purchase, the stockholders of HealthMarkets include members of management, the Company’s dedicated insurance agents and the investment affiliates of the private equity firms.

complaints/grievances are handled; and to monitor and measure the results of these changes. Specifically, the RSA provided for the following actions:

1. Claim Reassessment Process: The Company agreed to offer persons who believed they were covered for benefits that were not listed in the policy and for whom certain claims were denied between 2004 and 2006 the opportunity to have their claims reassessed. Claims identified as eligible for reassessment were ones denied based on specific remark codes identified by the Division for those persons whose coverage was effective January 1, 2002 through December 31, 2004, including claims on policies issued on and after August 1, 2004 through July 31, 2005 to the date of their first renewal or lapse. As a result of this reassessment, the Company paid out a total of \$840,005 on 7,408 previously denied claims.
2. Oversight of Producer Practices
 - The Company was required to review producer disciplinary procedures and institute procedures to address producer-related complaints.
 - The Company was required to conduct a good faith investigation of all allegations of improper sales practices and implement appropriate discipline and producer training for substantiated infractions to prevent recurrence of improper practices.
 - The Company was specifically prohibited from allowing any reference to the Massachusetts Insurance Partnership Program (“IPP”), the Children’s Medical Security Plan (“CMSP”), MassHealth or any state or federal programs as selling points.
 - The Company was required to establish procedures designed to reasonably ensure that all advertising and marketing materials comply with both Massachusetts statutes and regulations and the Company’s written procedures.

3. Handling of Complaints/Grievances

- The Company was required to bring all significant or systematic issues identified in complaints/grievances or other credible sources to senior management so changes could be implemented to eliminate repeated complaints/grievances.
- The Company was required to identify and convert verbal complaints/grievances to writing and to ensure all verbal and written complaints/grievances were recorded and logged.
- The Company was required to comply with the terms of timely response in accordance with Massachusetts law.
- The Company was required to ensure that all issues raised in a complaint/grievance were acknowledged and completely addressed.

4. Regulatory monitoring: During the two-year period following the RSA, the Division continued oversight of the Company's activities and implementation of the RSA requirements. Such oversight included members of the examination team conducting periodic reviews of randomly selected files. Oversight also included meetings with Company senior management to discuss compliance with the RSA.

The RSA identified a corrective action plan that the Company would follow to address concerns raised in the examination reports. In the two-year period following the RSA, staff from the Company, the Division, and INS met or participated in regular conference calls to monitor the Company's actions toward meeting the requirements of the RSA. In addition to the conference calls, INS conducted three on-site reviews, at the Division's direction, to provide interim observations to the Company regarding its progress toward meeting the RSA. Following each of these reviews, INS communicated recurring problems that needed to be addressed by the Company, including ongoing concerns associated with the Company's oversight of its producers' activities and its handling of complaints and grievances. INS also pointed out concerns regarding the Company's marketing of prescription drug benefits, and catastrophic benefit plans, as well as the Company's processing of reassessment claims and benefit confirmation calls.

During the two-year period following the RSA, the Division raised additional concerns regarding the marketing of certain Company products. In December 2007, the Division contacted the Company about the marketing of the “Total and Permanent Disability Accelerated Living Benefit Rider” (form identifier of 25921-IR MA) when it was issued with a term life insurance product and marketed with a catastrophic hospital expense plan known as the “Signature Benefit Plan” (form identifier of 25876-C-MA (07/07)). The Division requested that the Company suspend sales of the rider until the Company developed procedures to ensure that consumers understood the features of the product. Further, the Division required the Company to write to each insured advising them of the features of the rider. The Company sent the requested letters and decided to cease marketing this product in Massachusetts.

In August 2008, the Company submitted a filing for the Division to review for its CareChoice Plus HSA II health products (with form identifier CH-26039-C (SSMB) MA (8/08) when issued by Chesapeake and 26039-C (SSMB) MA (8/08) when issued by MEGA). The products, as developed, would offer coverage that would meet Massachusetts’ required Minimum Creditable Coverage standards only during calendar year 2009, not for subsequent years. Based upon the features of this product and concerns regarding the Company’s marketing practices, the Division suspended the review of this product pending the conclusion of this component of the re-examination.

Scope of Examination

On January 9, 2009, the Division sent a call letter to the Company announcing a re-examination². The Division instructed INS to conduct a two-phase review of the Company’s compliance with certain key provisions of the RSA. The initial phase of the examination reviewed the Company’s oversight of producer practices and handling of complaints/grievances

² In addition, the RSA specifically provided for a re-examination of the Company to review compliance with the requirements of the RSA.

during the period between January 1, 2008 and December 31, 2008. As part of the first phase of the re-examination, the examiners conducted an on-site visit of the Company between January 19, 2009 and February 12, 2009. The purpose of this visit was to evaluate the Company's compliance with certain key provisions of the RSA. Specifically, the RSA provisions related to the oversight of producer³ practices and the handling of complaint/grievances were a focus during the January-February 2009 review⁴. The second phase of the review was not conducted prior to the issuance of this report.

Examination Results

Oversight of Producer Practices

The examiners reviewed producer oversight activities involving 16 producers selected from the interim reviews, based on records of complaints against the producer alleging forgery/fraud or records that the producer exceeded a minimum threshold of complaints determined by the Division. There were 11 adverse findings resulting from the review of the Company's oversight of producer practices:

Finding 1⁵: The Company failed to conduct good faith investigations for certain reported allegations of fraud/forgery and for some instances of improper sales practices by agents.

Finding 2⁶: The Company failed to take appropriate action regarding the fraud/forgery complaint with Agent 12.

Finding 3: The Company failed to take immediate and decisive action to discipline Agent 13 and immediately notify all persons sold accident only policies by Agent 13 about the

³ In the Commonwealth of Massachusetts, the term agent and producer are used interchangeably.

⁴ Other terms of the RSA were not tested during this re-examination.

⁵ The Company has reported that since this re-examination, it has changed its process and will conduct a full investigation of fraud and forgery cases upon receipt of any complaint. Related to Finding 1, the Company had not initiated the investigation because, under its old process, the Company required a complainant to submit a notarized affidavit regarding the fraudulent activity in order for an investigation to begin.

⁶ The Company reported that it does have a process to report such activity to state agencies, the Company acknowledged that after investigating the fraud/forgery complaint for Agent 12, it did not submit the information to the Division and instead submitted the fraud/forgery information to a non-state agency.

nature of the product they purchased. The complaint files include allegations that Agent 13 misrepresented that the Company's accident only plan meets Massachusetts Minimum Creditable Coverage standards.

Finding 4: The Company failed to ensure that producers were properly characterizing benefits in their accident only plans.

Finding 5: The Company failed to institute changes related to check handling that would be necessary to eliminate sources of repeated complaints/grievances.

Finding 6: The Company failed to properly use its High Complaint Report which identifies producers who have had five or more complaints in a rolling twelve-month period to identify significant or systematic issues.

Finding 7⁷: The Company failed to utilize measurable criteria to determine when a warning letter should be sent to a producer and to require producers to affirmatively state they would modify their behavior so that the letter resulted in positive action.

Finding 8⁸: The Company failed to consistently discipline producers and apply adequate levels of discipline in certain cases.

Finding 9: The Company failed to provide materials to producers advising whether plans meet Minimum Creditable Coverage standards in Massachusetts after January 1, 2009 and confirm that producers informed consumers of this information.

Finding 10: The Company failed to ensure that producers did not use reference to the IPP or CMSP as selling points for coverage.

⁷ The Company has reported that since this re-examination, it has changed its process and the warning letters used with producers. Related to this finding, the Company has reported that its disciplinary notifications, including the warning letter, now informs the producer of the specific issue in question; communicates the importance of corrective action to avoid future complaints; advises additional action that the Company may take if the issue is not resolved; and requires written confirmation from the producer as well as their Division Leader.

⁸ The Company has reported since this re-examination that it has revised its agent progressive discipline program.

Finding 11: The Company failed to ensure that producers properly described the Company's prescription benefits. Although the Company does not offer prescription drug coverage in Massachusetts, its affiliated association offers drug discount programs on the same application as the insurance coverage.

Handling of Complaints and Grievances

The examiners reviewed 201 MEGA and 108 Mid-West complaints/grievances. There were 3 adverse findings resulting from the complaints/grievance review:

Finding 1: The Company failed to resolve complaints within 30 days of receipt in 15% of all files reviewed.

Finding 2: The Company failed to include appropriate documentation in files.

Finding 3: The Company failed to request a producer's statement in 14% of all findings reviewed.

Report Submission

This report of examination is hereby respectfully submitted.

Examiners:

INS Regulatory Insurance Services, Inc.

A handwritten signature in black ink, reading "Roger L. Fournier". The signature is written in a cursive style with a large, stylized initial "R".

Roger L. Fournier, Examiner-in-Charge

A handwritten signature in black ink, reading "Shelly G. Schuman". The signature is written in a cursive style with a large, stylized initial "S".

Shelly G. Schuman, Supervising Insurance Examiner

APPENDIX A
Regulatory Settlement Agreement
(with amendments)