

COMMONWEALTH OF MASSACHUSETTS
OFFICE OF CONSUMER AFFAIRS AND BUSINESS
REGULATION

Division of Insurance

Report on the Statutory Examination of
HPHC Insurance Company, Inc.

Wellesley, Massachusetts

As of December 31, 2004

NAIC COMPANY CODE: 18975

EMPLOYERS ID NUMBER: 04-3149694

Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.

Table of Contents

SALUTATION	3
SCOPE OF EXAMINATION	4
DESCRIPTION OF COMPANY	4
History	4
Organization	4
Plan of Rehabilitation	5
Capital and Surplus	5
MANAGEMENT AND CORPORATE RECORDS	5
Articles of Organization and By-Laws	5
BOARD OF DIRECTORS	5
OFFICERS	7
CONFLICT OF INTEREST PROCEDURES	8
CORPORATE RECORDS	8
ACQUISITIONS, MERGERS, DISPOSALS, DISSOLUTIONS & PURCHASES OR SALES	8
MANAGEMENT CONTINUITY AND NATIONAL EMERGENCY	8
AFFILIATED COMPANIES	9
Subsidiaries and Affiliated Companies	9
RELATED PARTY TRANSACTIONS	9
FIDELITY BOND AND OTHER INSURANCE	10
PENSION AND INSURANCE PLANS	10
SPECIAL DEPOSITS	10
PRODUCTS	10
PROVIDER CONTRACTS	11
RESERVES	11
REINSURANCE	11
ACCOUNTS AND RECORDS	12
SUBSEQUENT EVENTS	12
COMMITMENTS AND CONTINGENCIES	12
FINANCIAL STATEMENTS	13
Statement of Assets, Liabilities, and Capital & Surplus As of December 31, 2004	14
Analysis of Assets Exhibit As of December 31, 2004	15
Statement of Revenue and Expenses For the Year Ended December 31, 2004	16
Capital and Surplus As of December 31, 2004	17
ACKNOWLEDGEMENT – Report of Certified Financial Examiner	18



COMMONWEALTH OF MASSACHUSETTS
Office of Consumer Affairs and Business Regulation
DIVISION OF INSURANCE

One South Station • Boston, MA 02110-2208
(617) 521-7794 • FAX (617) 521-7771
TTY/TDD (617) 521-7490
<http://www.state.ma.us/doi>

MITT ROMNEY
GOVERNOR

KERRY HEALEY
LIEUTENANT GOVERNOR

BETH LINDSTROM
DIRECTOR, CONSUMER AFFAIRS
AND BUSINESS REGULATION

JULIANNE M. BOWLER
COMMISSIONER OF INSURANCE

December 30, 2005

Honorable Julianne M. Bowler
Secretary, Northeastern Zone, NAIC
Commissioner of Insurance
Commonwealth of Massachusetts
One South Station
Boston, Massachusetts 02110

Honorable Alfred W. Gross
Chair, Financial Condition (E) Committee, NAIC
Commissioner, Bureau of Insurance
Commonwealth of Virginia
P. O. Box 1157
Richmond, VA 23218

Honorable Commissioners:

Pursuant to your instructions and in accordance with Massachusetts General Laws, Chapter 175, Section 4, an examination has been made of the financial condition and affairs of the

HPHC INSURANCE COMPANY, INC.

at its home office located at:

93 Worcester Street
Wellesley, MA 02481

The following report thereon is respectfully submitted.

SCOPE OF EXAMINATION

This statutory examination of HPHC Insurance Company, Inc., hereinafter referred to as "the Company" or "The Insurance Company" is as of December 31, 2004, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this statutory examination. KPMG LLP (KPMG) has applied certain agreed upon procedures to selected records and transactions of the Company. Such procedures were reviewed and approved by the Commonwealth of Massachusetts Division of Insurance ("the Division" or "the DOI").

The current examination was conducted at the direction of, and under the overall management and control of the examination staff of the Division. The statutory examination was performed at the Company's home office in Wellesley, Massachusetts. KPMG was engaged to perform certain agreed-upon procedures which are in compliance with the *NAIC Financial Condition Examiners' Handbook*. KPMG's actuaries were involved in the performance of those procedures to the extent that such procedures related to the Company's reserves for unpaid claims and claim adjustment expenses and provider risk sharing settlements as of December 31, 2004. KPMG's Information Risk Management (IRM) personnel were engaged to perform an Evaluation of Controls in Information Systems Questionnaire in a form substantially similar to the one established in the *NAIC Financial Condition Examiners' Handbook*. The IRM Specialists performed examination procedures pertaining to the examination of the EDP System as outlined in the *NAIC Financial Condition Examiners' Handbook*. All procedures were performed under the management and control and general supervision of the examination staff of the Division.

The examination was conducted in accordance with standards and procedures established by the National Association of Insurance Commissioners ("NAIC") Financial Condition (E) Committee and prescribed by the current *NAIC Financial Condition Examiners Handbook*.

In addition to a review of the financial condition of the Company, the examination included a review of the Company's business policies and practices, corporate records, provider contracts, reinsurance treaties, conflict of interest disclosure statements, fidelity bonds and other insurance, employees' pension and benefits plans, disaster recovery plan, and other pertinent matters to provide reasonable assurance that the Company was in compliance with applicable laws, rules and regulations. In planning and conducting the examination, consideration was given to the concepts of materiality and risk and examination efforts were directed accordingly.

In determining the scope of the statutory examination, after review and evaluation, the Division placed reliance on certain workpapers provided by the Company's external auditors, Deloitte & Touche, LLP. Wherever possible and wherever deemed appropriate and effective, their independent work product was used to define, support, document and expedite the overall examination process.

DESCRIPTION OF COMPANY

History

The Insurance Company was incorporated on September 27, 1991 and commenced underwriting accident and health risks on January 1, 1992. The Insurance Company is a wholly-owned subsidiary of Harvard Pilgrim Health Care, Inc. ("HPHC" or Harvard Pilgrim).

Organization

The Insurance Company operates as an indemnity insurance company and underwrites health insurance for group products, including a PPO indemnity product, a Medicare indemnity product and the out-of-network component of HPHC's POS plan.

Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.

Plan of Rehabilitation

HPHC, Inc, together with Harvard Pilgrim Health Care of New England, Inc., was placed in temporary receivership for purposes of rehabilitation in January of 2000. On May 24, 2000, a Plan of Rehabilitation (the "Plan") was approved by The Supreme Judicial Court for Suffolk County and on June 21, 2000, the temporary receivership was dismissed. As part of the court order, Harvard Pilgrim will remain subject to administrative supervision of the Commissioner for so long as the Condition imposed under the Plan remains in effect. The Insurance Company was not party to the receivership.

Capital and Surplus

The Insurance Company is a wholly-owned for-profit subsidiary of Harvard Pilgrim Health Care, Inc. The total admitted assets, total liabilities and Capital and Surplus of the Company from 2002 to 2004 is shown in the following schedule.

<u>Year</u>	<u>Total Admitted Assets</u>	<u>Total Liabilities</u>	<u>Capital & Surplus</u>
2002	\$ 9,488,138	\$ 859,978	\$ 8,628,160
2003	11,555,161	3,222,989	8,332,172
2004	11,698,914	2,103,800	9,595,114

MANAGEMENT AND CORPORATE RECORDS

Articles of Organization and By-Laws

The Company's By-Laws may be altered, amended or repealed at any annual or special meeting of the stockholders called for the purpose, of which the notice shall specify the subject matter of the proposed alteration, amendment or repeal or the sections to be affected, by vote of the stockholders. The By-Laws may also be altered, amended or repealed by vote of a majority of the directors then in office.

BOARD OF DIRECTORS

The Company's By-Laws indicate the following regarding its board of directors (the "Board"):

- **Number.** At the annual meeting of stockholders such stockholders as have the right to vote for the election of directors shall fix the number of directors at not less than five (5) and shall elect the number of directors so fixed. The number of directors may be increased at any time or from time to time either by the stockholders or by the directors by vote of a majority of the directors then in office. The number of directors may be decreased to any number permitted by law at any time or from time to time either by the stockholders or by the directors by a vote of a majority of the directors then in office, but only to eliminate vacancies existing by reason of the death, resignation, removal or disqualification of one or more directors. No director need be a stockholder.
- **Tenure.** Each director shall hold office until the next annual meeting of the stockholders and until his successor is duly elected and qualified, or until he sooner dies, resigns, is removed or becomes disqualified.
- **Powers.** Except as reserved to the stockholders by law, by the Articles of Organization or by the Bylaws, the business of the corporation shall be managed by the directors who shall have and may exercise all the powers of the corporation. In particular, and without limiting the generality of the foregoing, the directors may at any time issue all or from time to time any part of the unissued capital stock of the corporation from time to time authorized under the Articles of Organization and may determine, subject to any requirements of law, the consideration for which stock is to be issued and the manner of allocating such consideration between capital and surplus.

- Committees. The directors may, by vote of a majority of the directors then in office, elect from their number an executive committee and other committees and delegate to any such committee or committees some or all of the powers of the directors except those which by law, by the Articles of Organization or the Bylaws they are prohibited from delegating. Except as the directors may otherwise determine, any such committee may make rules for the conduct of its business, but unless otherwise provided by the directors or such rules, its business shall be conducted as nearly as may be in the same manner as is provided by these Bylaws for the conduct of business by the directors.
- Regular Meetings. Regular meetings of the directors may be held without call or notice at such places and at such times as the directors may from time to time determine, provided that reasonable notice of the first regular meeting following any such determination shall be given to absent directors. A regular meeting of the directors may be held without call or notice immediately after and at the same place as the annual meeting of the stockholders.
- Special Meetings. Special meetings of the directors may be held at any time and at any place designated in the call of the meeting, when called by the chairman, if any, the chief executive officer or the treasurer or by two or more directors, reasonable notice thereof being given to each director by the secretary or an assistant secretary, or, if there be none, by the clerk or an assistant clerk, or by the officer or one of the directors calling the meeting.
- Notice. It shall be sufficient notice to a director to send notice by mail at least forty-eight hours or by telegram at least twenty-four hours before the meeting addressed to him at his usual or last known business or residence address or to give notice to him in person or by telephone at least twenty-four hours before the meeting. Notice of a meeting need not be given to any director if a written waiver of notice, executed by him before or after the meeting, is filed with records of the meeting, or to any director who attends the meeting without protesting prior thereto or at its commencement the lack of notice to him. Neither such notice of a meeting nor waiver of notice need specify the purposes of the meeting.
- Quorum. At any meeting of the directors a majority of the directors then in office, but not less than four, shall constitute a quorum. Any meeting may be adjourned from time to time by a majority of the votes cast upon the question, whether or not a quorum is present, and the meeting may be held as adjourned without further notice.
- Action by Vote. When a quorum is present at any meeting, a majority of the directors present may take any action, except when a larger vote is required by law, by the Articles of Organization or by the Bylaws.
- Action by Writing. Any action required or permitted to be taken at any meeting of the directors may be taken without a meeting if all the directors consent to the action in writing and the written consents are filed with the records of the meetings of the directors. Such consents shall be treated for all purposes as a vote taken at a meeting.
- Presence Through Communications Equipment. Members of the board of directors may participate in a meeting of such Board by means of a conference telephone or similar communications equipment by means of which all persons participating in the meeting can hear each other at the same time, and participation by such means shall constitute presence in person at a meeting.

Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.

At December 31, 2004 the Board was comprised of five (5) directors which is in compliance with the Company By-Laws. Directors duly elected and serving at December 31, 2004, with addresses and business affiliations, follow:

<u>Director</u>	<u>Class of Director</u>	<u>Principal Occupation</u>
Charles D. Baker Swampscott, MA	Management Director	President and Chief Executive Officer HPHC, Inc.
Joseph C. Capezza Natick, MA	Management Director	Chief Financial Officer HPHC, Inc.
Bruce M. Bullen Weston, MA	Management Director	Chief Operating Officer HPHC, Inc.
David Cochran M.D. Norwell, MA	Management Director	Senior Vice President, Strategic Development, HPHC, Inc.
Laura Peabody Boston, MA	Management Director	Senior Vice President and General Counsel, HPHC, Inc.

Committees of the Board

The Board may, by vote of a majority of the directors then in office, elect from their number an executive committee and other committees and delegate to any such committee or committees some or all of the powers of the directors except those which by law, by the Articles of Organization or by the Bylaws they are prohibited from delegating. There are currently no committees of the Board of the Company.

OFFICERS

The Company's officers consist of a President, Treasurer, Clerk, and such other officers, if any, as the directors or the President may determine. The Clerk shall be a resident of the Commonwealth of Massachusetts unless the Corporation has appointed a resident agent to receive service of process. A person may hold more than one office at the same time.

The officers of the Corporation shall be elected by the directors at their first meeting following the annual meeting of the stockholders. Other officers, if any, may be elected or appointed by the board of directors at said meeting or at any other time.

The elected officers and their respective titles at December 31, 2004 were as follows:

<u>Officer</u>	<u>Officer</u>
Charles D. Baker	President
Joseph C. Capezza	Treasurer
Laura S. Peabody	Secretary

Subsequent to December 31, 2004 and pursuant to votes adopted September 6, 2005, the following officers were appointed to the positions indicated:

Charles D. Baker	President
Joseph C. Capezza	Treasurer
Laura S. Peabody	Clerk

CONFLICT OF INTEREST PROCEDURES

Harvard Pilgrim, the parent of the Company, has adopted a conflict of interest policy statement which is applied to the officers and directors of the Company. Harvard Pilgrim has an established procedure for the disclosure to the president or chairperson of any financial interest on the part of any officer or director which is in or is likely to be in conflict with his/her official duties. The financial interest shall be made a matter of record through such annual or other reporting and certification procedure as the board of directors shall require from time to time. After disclosure of the financial interest and all material facts, and any discussion with the fiduciary, the Board shall determine whether any conflict of interest exists. The fiduciary shall leave the board meeting while the determination of a conflict of interest is discussed and voted upon. The minutes of the board meeting shall include the names of the fiduciaries who disclosed financial interests, the nature of the financial interests, and whether the Board determined there was a financial interest.

Review of the 2004 Harvard Pilgrim board of directors records identified potential conflicts, noting that none was of any financial significance.

CORPORATE RECORDS

Articles of Incorporation and Bylaws

Our review of the By-Laws and Articles of Incorporation indicated that there were no changes since the prior examination.

Board of Directors Minutes

The minutes of the Board meetings for the period under statutory examination were read and indicated that all meetings were held in accordance with the Company By-Laws and the laws of the Commonwealth of Massachusetts. Activities of the committees were reported upon at various meetings of the Board.

ACQUISITIONS, MERGERS, DISPOSALS, DISSOLUTIONS AND PURCHASES OR SALES

See 'Organization' and 'Plan of Rehabilitation' on page 4.

MANAGEMENT CONTINUITY AND NATIONAL EMERGENCY

The Company provides for the continuity of management and operations in the event of a catastrophe or national emergency in accordance with Massachusetts General Laws, Chapter 175 § 180M-180Q.

AFFILIATED COMPANIES

Harvard Pilgrim Health Care, Inc. (Harvard Pilgrim or HPHC, Inc.)

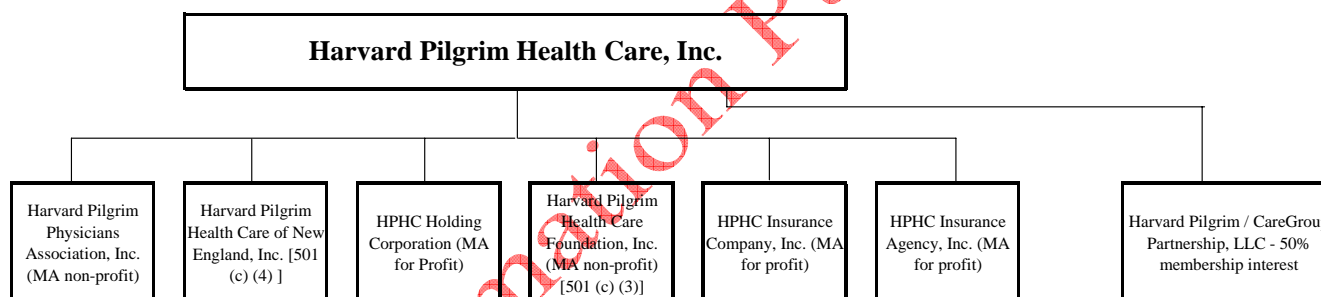
HPHC, Inc., a not-for-profit Massachusetts corporation, operates as a not-for-profit health insurance plan, providing comprehensive health insurance, access to health care and other related services in Massachusetts and Maine to group, individual, and Medicare members through contracts with physicians, established primary care and multi-specialty physician groups, hospitals and other health care providers.

Harvard Pilgrim Health Care of New England, Inc. (New England)

New England, a not-for-profit Massachusetts corporation, operates as a not-for-profit health insurance plan, providing comprehensive health insurance, access to health care and other related services in Massachusetts and New Hampshire to group and Medicare members through contracts with physicians, established primary care and multi-specialty physician groups, hospitals and other health care providers. New England was incorporated on November 18, 1978 and commenced operations as a health insurance plan on October 1, 1980. New England is an affiliate of HPHC, Inc. New England is a tax-exempt organization under Section 501(c) (4) of the Internal Revenue Code.

Subsidiaries and Affiliated Companies

A summary of ownership and relationship of the Company and its parent and affiliated companies as of December 31, 2004 is illustrated below:



RELATED PARTY TRANSACTIONS

The Insurance Company has no employees, and accordingly, HPHC, Inc. provides all administrative services to The Insurance Company, including premium collection, claims payments, and operational management. Administrative and claim adjustment expenses are charged to The Insurance Company based on Harvard Pilgrim's departmental cost allocation methodology. For the years ended December 31, 2004 and 2003, total administrative and claims adjustment expenses charged to The Insurance Company by Harvard Pilgrim were \$3.6 million and \$2.3 million, respectively. At December 31, 2004, The Insurance Company had a net payable to HPHC, Inc. of \$155,549 and at December 31, 2003, The Insurance Company had a net receivable from HPHC, Inc. of \$1,548,831 related to administrative services provided.

Due to the significance of the transactions between The Insurance Company and HPHC, Inc., the results of operations of The Insurance Company may not be indicative of the results which would have been attained had The Insurance Company not been a wholly owned subsidiary of HPHC, Inc.

FIDELITY BOND AND OTHER INSURANCE

The Company maintains fidelity bond coverage with an authorized Massachusetts insurer, consistent with Massachusetts General Laws, Chapter 175 § 60. The aggregate limit of liability exceeds the NAIC suggested minimum.

The Company has further protected its interest and property by acquiring policies of insurance covering other insurable risks. All coverage, including its Directors and Officers Liability policy, is provided by insurers licensed in the Commonwealth of Massachusetts and was in force as of December 31, 2004.

PENSION AND INSURANCE PLANS

Employees' Retirement Plan

The Insurance Company has no employees. See Related Party Transactions, above.

SPECIAL DEPOSITS

The special deposits of the Company at December 31, 2004 are as follows:

Description of Deposit	Where Deposited	Par or Book Value	Statement Value	Market Value
FNMA 4 3/8% 3/15/2013	Fleet National Bank, Boston, MA – State of New Hampshire	\$ 300,000	\$ 297,259	\$ 299,157
U.S. Treasury Bond 6 ¼ % 8/15/2023	Fleet National Bank, Boston, MA – State of New Hampshire	150,000	174,854	175,611
U.S. Treasury Bond 6 3/8% 8/15/2027	Fleet National Bank, Boston, MA – State of New Hampshire	500,000	598,097	600,390
Galaxy Institutional MMF	Fleet National Bank, Boston, MA – State of New Hampshire	53,897	53,897	53,897
		<u>\$ 1,003,897</u>	<u>\$ 1,124,107</u>	<u>\$ 1,129,055</u>

PRODUCTS

PPO – the PPO plan is available through employers in Massachusetts, Maine and New Hampshire. The PPO features comprehensive coverage for a wide range of preventive and medical services, including routine office visits, well-baby care, immunizations, hospitalization and worldwide emergency care. In some benefits packages, prescription drug coverage may also be included. PPO members can choose to receive care for covered services from providers and hospitals that belong to The Insurance Company's participating provider network or from those who don't. Outside of Massachusetts, Maine, New Hampshire and Rhode Island, participating providers also include the Private Healthcare Systems network of more than 360,000 providers and 3,500 hospitals across the United States. When provided or arranged by participating providers, services are typically covered in full with copayments. Services received outside of The Insurance Company's participating provider network are generally subject to deductibles and coinsurance.

Best Buy PPO – The Insurance Company offers a Best Buy PPO plan in New Hampshire. The Best Buy PPO plan has many of the same features as traditional PPO, but offer lower premiums. It has additional cost sharing responsibilities like deductibles, coinsurance and/or higher copayments.

**Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.**

Best Buy HSA PPO – The Insurance Company offers a Health Savings Account ('HSA') qualified high deductible PPO health plan in Massachusetts and New Hampshire. The Best Buy HSA may help members save money on their annual premium if they put money aside in a Health Savings Account to help offset medical costs.

POS – The Insurance Company underwrites the out-of-network coverage in HPHC's POS plan in Massachusetts.

Medicare Enhance – The Insurance Company offers a Medicare plan to retirees of Massachusetts employers that complements a subscriber's Medicare coverage.

PROVIDER CONTRACTS

The Insurance Company reimburses its participating hospitals and physicians on a fee for service basis. The Insurance Company has no risk sharing contracts with its network providers.

RESERVES

In conjunction with KPMG's examination of the statutory financial statements of the Company, KPMG was engaged by the Division to review the adequacy of the Unpaid Claim Liability (UCL) of the Company as of December 31, 2004.

KPMG actuaries prepared independent estimates of the unpaid claim liabilities for several periods prior to July 2005 based on paid claim triangles and membership information. Monthly claim payments were provided by month of service for the period from January 2002 to July 2005. For December 31, 2004, completion factors for the projection of ultimate incurred claims were developed using historical payment patterns and actuarial judgment. The "last 6" methodology was used in developing completion factors for the "Mid" estimate. The methodology considers the prior six months of claims payment patterns in calculating completion factors. This is among accepted methodologies that are widely used for calculating completion factors. "Low" and "High" estimates were developed by adjusting completion factors to reflect slightly faster and slower payment speeds. As the Company pays quickly, the range of estimates for the December 31, 2004 UCL is narrow and KPMG's estimates are similar to the Company's estimates with hindsight through July 31, 2005.

Based upon KPMG's review, the Unpaid Claims Liability at December 31, 2004 appears to be fairly stated in all material respects. The Company made a separate provision for Claim Adjustment Expenses (LAE/CAE) in 2004 in accordance with standard actuarial practice. The method used is reasonable, and results have been consistent from year to year. The resulting expense percentage levels used are within industry norms.

REINSURANCE

The Insurance Company carries reinsurance against excessive utilization on a per-member basis. Under policies, The Insurance Company is reimbursed 90% of certain hospital inpatient, hospital outpatient and pharmacy claims over the policy deductibles, which range from \$150,000 to \$500,000. Inpatient hospital claims are subject to Maximum Daily Allowance. Outpatient hospital and Pharmacy claims are subject to additional policy sub-limits. The maximum recoverable under the reinsurance agreement is \$2,000,000 for each member per year.

ACCOUNTS AND RECORDS

The books and records of the Company are audited annually by the independent certified public accounting firm of Deloitte & Touche LLP, in accordance with 211 CMR 43.14. The CPA Firm issued an unqualified opinion on the December 31, 2004 audited financial statements. The Company is also subject to review by an internal audit department.

The internal controls structure was discussed with management through questionnaires and through a review of the work performed by the Company's independent certified public accountants. No material deficiencies were noted. No material internal control weaknesses were noted in connection with the examination, nor were any such matters reported in the CPA Firm's filings with the Division.

The NAIC provides a questionnaire covering the evaluation of the controls in the EDP systems environment. The questionnaire was completed by the Company and reviewed by KPMG's Information Risk Management (IRM) team that evaluated the adequacy of the EDP controls. No material deficiencies were noted.

The Company uses an automated general ledger system. Trial balances were traced from the general ledger and supporting documents to the 2004 Annual Statement. No material exceptions were noted.

The Company has an internal audit department, including staff experienced in financial and information systems audits, who perform periodic audits of the Company's systems, controls and operational processes. KPMG reviewed the Internal Audit reports issued during the period under examination, and considered the results of the audits and, where appropriate, relied on the results during the application of the agreed-upon procedures.

SUBSEQUENT EVENTS

- **February 14, 2005** – The board of directors of HPHC Insurance Company, Inc. authorized the issuance of a stock dividend to Harvard Pilgrim Health Care, Inc., the sole stockholder of The Insurance Company, of 12,000 shares of common stock at a par value of \$50 per share. This transaction had no impact on total capital and surplus.

COMMITMENTS AND CONTINGENCIES

Legal Proceedings

None.

FINANCIAL STATEMENTS

The Financial Statement section includes the following:

	<u>Page</u>
Statutory Statement of Assets, Liabilities, and Capital & Surplus as of December 31, 2004	14
Analysis of Assets Exhibit as of December 31, 2004	15
Statement of Revenue and Expenses for the Year Ended December 31, 2004	16
Capital and Surplus as of December 31, 2004	17

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Commonwealth of Massachusetts Division of Insurance and by the National Association of Insurance Commissioners as of December 31, 2004.

For Information Purposes Only

Commonwealth of Massachusetts Division of Insurance
**REPORT ON THE STATUTORY EXAMINATION OF
 HPHC INSURANCE COMPANY, INC.**

HPHC Insurance Company, Inc.
Statutory Statement of Assets, Liabilities, and Capital & Surplus
As of December 31, 2004

	<u>Annual Statement</u>	<u>Statutory Examination Adjustment</u>	<u>Per Statutory Examination</u>
<u>ASSETS</u>			
Bonds	\$ 7,263,339	\$ -	\$ 7,263,339
Cash, cash equivalents and short-term investments	2,579,394	-	2,579,394
Subtotals, cash and invested assets	9,842,733	-	9,842,733
Investment Income due and accrued	76,161	-	76,161
Premiums and Considerations:			
Uncollected premiums and agents' balances in course of collection	64,737	-	64,737
Amounts receivable relating to uninsured plans	1,367,363	-	1,367,363
Net deferred tax asset	340,000	-	340,000
Cash surrender value - life insurance	7,920	-	7,920
Total Assets	\$ 11,698,914	\$ -	\$ 11,698,914
<u>LIABILITIES</u>			
Claims unpaid	1,367,927	-	1,367,927
Unpaid claims adjustment expenses	19,901	-	19,901
Premiums received in advance	194,864	-	194,864
General expenses due or accrued	8,860	-	8,860
Current federal and foreign income tax payable and interest thereon	3,470	-	3,470
Amounts due to parent, subsidiaries and affiliates	155,549	-	155,549
Liability for amounts held under uninsured accident and health plans	353,229	-	353,229
Total Liabilities	2,103,800	-	2,103,800
<u>CAPITAL & SURPLUS</u>			
Common capital stock	467,000	-	467,000
Gross paid in and contributed surplus	7,934,000	-	7,934,000
Unassigned funds (surplus)	1,194,114	-	1,194,114
Total Capital and Surplus	9,595,114	-	9,595,114
Total Liabilities, Capital and Surplus	\$ 11,698,914	\$ -	\$ 11,698,914

Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.

HPHC Insurance Company, Inc.
Analysis of Assets Exhibit
As of December 31, 2004

	Assets	Nonadmitted Assets	Net Admitted Assets	Statutory Examination Adjustment	Per Statutory Examination
<u>ASSETS</u>					
Bonds	\$ 7,263,339		\$ 7,263,339	\$ -	\$ 7,263,339
Cash, cash equivalents and short-term investments	2,579,394		2,579,394	-	2,579,394
Other invested assets	75,000	75,000	-	-	-
Subtotals, cash and invested assets	9,917,733	75,000	9,842,733	-	9,842,733
Investment Income due and accrued	76,161		76,161		76,161
Premiums and Considerations:					
Uncollected premiums and agents' balances in the course of collection	67,524	2,787	64,737	-	64,737
Amounts receivable relating to uninsured plans	1,367,363		1,367,363	-	1,367,363
Net deferred tax asset	916,809	576,809	340,000		340,000
Cash surrender value - life insurance	7,920		7,920	-	7,920
Total Assets	12,353,510	654,596	11,698,914	-	11,698,914

For Information Purposes Only

Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.

HPHC Insurance Company, Inc.
Statement of Revenue and Expenses
For the Year Ended December 31, 2004

	Annual Statement	Statutory Examination Adjustment	Per Statutory Examination
<i>Member Months</i>	41,056		41,056
Net premium income	\$ 13,452,977	\$ -	\$ 13,452,977
Total Revenues	13,452,977	-	13,452,977
Hospital and Medical:			
Hospital/medical benefits	6,696,516	-	6,696,516
Other professional services	363,662	-	363,662
Outside referrals	393,342	-	393,342
Emergency room and out-of-area	152,431	-	152,431
Prescription drugs	2,663,223	-	2,663,223
Subtotal	10,269,174	-	10,269,174
Less:			
Net reinsurance recoveries	279,116	-	279,116
Total and hospital and medical	9,990,058	-	9,990,058
Claims adjustment expenses	1,229,205	-	1,229,205
General administrative expenses	1,424,322	-	1,424,322
Total underwriting deductions	12,643,585	-	12,643,585
Total underwriting gain	809,392	-	809,392
Net investment income earned	337,918	-	337,918
Net realized capital gains or (losses)	(12,723)	-	(12,723)
Net investment gains	325,195	-	325,195
Net Income	\$ 1,160,729	\$ -	\$ 1,160,729

Commonwealth of Massachusetts Division of Insurance
REPORT ON THE STATUTORY EXAMINATION OF
HPHC INSURANCE COMPANY, INC.

HPHC Insurance Company, Inc.
Capital and Surplus
As Of December 31, 2004

	<u>Annual Statement</u>	<u>Statutory Examination Adjustment</u>	<u>Per Statutory Examination</u>
Capital and Surplus, December 31, 2003	\$ 8,332,172	\$ -	\$ 8,332,172
Net income	1,160,729	-	1,160,729
Change in net deferred income tax	(385,760)	-	(385,760)
Change in nonadmitted assets	487,973		487,973
Net change in capital and surplus	1,262,942		1,262,942
Capital and Surplus, December 31, 2004	<u>\$ 9,595,114</u>	<u>\$ -</u>	<u>\$ 9,595,114</u>

For Information Purposes Only

ACKNOWLEDGMENT

This is to certify that the undersigned is a duly qualified Certified Financial Examiner (CFE) and that, in conjunction with KPMG LLP, applied certain agreed upon procedures to the accounting and corporate records of the HPHC Insurance Company, Inc. in order for the Division of Insurance of the Commonwealth of Massachusetts to fulfill the Commonwealth's requirements regarding periodic Statutory Examinations of Massachusetts domiciled insurers.

The undersigned's participation in this Statutory Examination as the Examiner-in-Charge encompassed responsibility for the coordination and direction of the statutory examination performed which was in accordance with, and substantially complied with, those standards established by the Financial Condition (E) Committee of the National Association of Insurance Commissioners (NAIC) and the *NAIC Financial Condition Examiners' Handbook*. This participation consisted of involvement in the planning (development, supervision and review of agreed upon procedures), administration, review of work papers and preparation of the statutory examination report.

The cooperation and assistance of the officers and employees of Harvard Pilgrim Health Care, Inc. extended to all examiners during the course of the examination is hereby acknowledged.

John Smallwood, CFE
Chief Examiner & Examiner in Charge (EIC)
Commonwealth of Massachusetts
Division of Insurance
Boston, MA

For Information Purposes Only