



**THE COMMONWEALTH OF MASSACHUSETTS**  
**OFFICE OF CONSUMER AFFAIRS AND BUSINESS**  
**REGULATION**  
**DIVISION OF INSURANCE**

***REPORT OF EXAMINATION OF THE***  
**NEIGHBORHOOD HEALTH PLAN, INC.**

**Boston, Massachusetts**

**As of December 31, 2005**

**NAIC COMPANY CODE 11109**

**EMPLOYER ID NO. 04-2932021**

## NEIGHBORHOOD HEALTH PLAN, INC.

### TABLE OF CONTENTS

|  | <u>Page</u> |
|--|-------------|
| Salutation   | 1           |
| Scope of Examination   | 2           |
| History  | 3           |
| General  | 3           |
| Growth of Plan   | 3           |
| Management   | 4           |
| Annual Meeting   | 4           |
| Board of Directors   | 4           |
| Patient Care Assessment Committee                            | 6           |
| Executive Committee  | 6           |
| Finance Committee  | 7           |
| Audit Committee  | 7           |
| Conflict Review Committee                                    | 7           |
| Contract Review Committee                                    | 8           |
| Officers   | 8           |
| Conflict of Interest Procedures                              | 8           |
| Corporate Records  | 9           |
| Articles of Incorporation and Bylaws                         | 9           |
| Board of Directors Minutes                                   | 9           |
| Surplus Notes  | 9           |
| Affiliated Companies   | 10          |
| Organization Chart   | 10          |
| Transactions and Agreements with Subsidiaries and Affiliates | 10          |
| Fidelity Bonds and Other Insurance                           | 10          |
| Pension, Stock Ownership and Insurance Plans                 | 11          |
| Statutory Deposits   | 11          |
| Insurance Products and Related Practices                     | 11          |
| Territory and Plan of Operation                              | 11          |
| Treatment of Subscribers                                     | 12          |
| Reinsurance  | 12          |
| Ceded Reinsurance  | 12          |
| Subsequent Events  | 13          |
| Accounts and Records   | 13          |
| Financial Statements   | 14          |
| Statement of Assets, Liabilities and Capital & Surplus       | 15          |
| Statement of Revenue and Expense                             | 17          |
| Reconciliation of Capital and Surplus                        | 18          |
| Notes to Financial Statements                                | 19          |
| Conclusion   | 20          |



**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) 521-7475  
TTY/TDD (617) 521-7490  
<http://www.state.ma.us/doi>

DEVAL L. PATRICK  
GOVERNOR

TIMOTHY P. MURRAY  
LIEUTENANT GOVERNOR

DANIEL O'CONNELL  
SECRETARY OF HOUSING AND  
ECONOMIC DEVELOPMENT

DANIEL C. CRANE  
DIRECTOR

JOSEPH G. MURPHY  
ACTING COMMISSIONER

January 19, 2007

Honorable Alfred W. Gross, Chair  
Financial Condition (E) Committee, NAIC  
Commissioner  
Virginia Bureau of Insurance  
State Corporation Commission  
1300 East Main Street  
Richmond, Virginia 23219

Honorable Joseph Torti, III  
Secretary, Northeastern Zone NAIC  
Superintendent  
Rhode Island Insurance Division  
Department of Business Regulation  
233 Richmond Street, Suite 233  
Providence, Rhode Island 02903-4233

Honorable Joseph G. Murphy  
Acting Commissioner of Insurance  
Commonwealth of Massachusetts  
Office of Consumer Affairs and Business Regulation  
Division of Insurance  
One South Station  
Boston, MA 02110-2208

Honorable Commissioners and Superintendent:

Pursuant to your instructions and in accordance with Massachusetts General Laws, Chapter 176G Section 10 and 211 CMR 43, an examination has been made of the financial condition and affairs of the

**NEIGHBORHOOD HEALTH PLAN, INC.**  
**Boston, MA**

at its home office located at 253 Summer Street, Boston, Massachusetts, 02210-1120. The following report thereon is respectfully submitted.

## **SCOPE OF EXAMINATION**

The Neighborhood Health Plan, Inc. (hereinafter referred to as the "Plan" or "NHP") was last examined as of December 31, 2002 under the association plan of the National Association of Insurance Commissioners (the "NAIC") by the Massachusetts Division of Insurance (the "Division"). The current association plan examination was also conducted by the Massachusetts Division of Insurance, and covers the period from January 1, 2003 through December 31, 2005, including any material transactions and/or events occurring subsequent to the examination date as noted during the course of this examination.

The examination was conducted in accordance with standards established by the Financial Condition (E) Committee of the NAIC as well as with the requirements of the NAIC Financial Condition Examiner's Handbook, the examination standards of the Division and with Massachusetts General Laws. The principal focus of the examination was 2005 activity; however, transactions both prior and subsequent thereto were reviewed as deemed appropriate.

In addition to a review of the financial condition of the Plan, the examination included a review of the Plan's business policies and practices, corporate records, reinsurance treaties, conflict of interest disclosure statements, fidelity bonds and other insurance, employees' pension and benefits plans, disaster recovery plan, treatment of Subscribers and other pertinent matters to provide reasonable assurance that the Plan 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.

Since 2004, the Plan has been audited annually by Deloitte & Touche LLP, an independent certified public accounting firm. For the year 2003, the Plan was audited by PricewaterhouseCoopers LLP, also an independent certified public accounting firm. The firms expressed unqualified opinions on the Plan's financial statements for the calendar years 2003 through 2005. A review and use of the certified public accountants' work papers was made to the extent deemed appropriate and effective. An independent certified public accounting firm, KPMG LLP, was retained by the Massachusetts Division of Insurance to evaluate the adequacy of the Plan's premium and claims unpaid reserves as of December 31, 2005. An evaluation of the adequacy and effectiveness of the IT Systems controls was done to determine the level of reliance to be placed on summary information generated by the data processing systems.

### **Status of Prior Examination Findings**

The examination included a review to verify the current status of any exception conditions commented upon in the previous Report of Examination as of December 31, 2002. It was determined that the Plan satisfactorily addressed all outstanding items.

## HISTORY

### General

The Plan was founded by the Massachusetts League of Community Health Centers (the “League”) and the Greater Boston Forum for Health Action (the “Forum”), and incorporated on May 22, 1986 under the provisions of M.G.L. c. 180 for the purpose of arranging for the delivery of comprehensive health services on a prepaid basis. On November 9, 1987, the Commonwealth of Massachusetts Division of Insurance licensed the Plan to operate as a Health Maintenance Organization (“HMO”) under the provisions of M.G.L. c. 176G. The Plan is a non-profit HMO, which contracts with businesses and the Commonwealth of Massachusetts to provide health care to their employees and to Medicaid beneficiaries. Initially allowed to conduct business in greater Boston only, the Plan now operates throughout Massachusetts.

During 1997, the Plan entered into negotiations with Harvard Pilgrim Health Care, Inc. (“HPHC”) for an affiliation. The deal was finalized in January 1998. Under the agreement, HPHC became the sole member of the Plan and agreed to provide up to \$9,000,000 to the Plan over a three-year period starting from the closing date. In addition, HPHC agreed to provide \$15,000,000 in funding to the Community Health Centers as grants over a three-year period. In January 1998, the Plan’s Board was reduced from 25 directors to 12 directors; five determined by the League and seven determined by HPHC.

In September 1999, Community Medical Alliance Clinical Group became a wholly owned affiliate of NHP. In January 2000, Community Medical Alliance Clinical Group changed its name to Community Medical Alliance, Inc., (“CMA”). CMA provides direct care and care management services to certain Plan members and is reimbursed by the Plan on a capitated basis. The Plan is the sole source of revenue for CMA.

### Growth of the Plan

The growth of the Plan for the years 2003 through 2005 is shown in the following schedule, which was prepared from the Plan’s Annual Statements, including any changes as a result of the examination.

| Year | <u>Admitted Assets</u> | <u>Net Premiums Income</u> | <u>Capital &amp; Surplus</u> |
|------|------------------------|----------------------------|------------------------------|
| 2003 | \$ 88,217,312          | \$ 366,024,136             | \$ 37,518,390                |
| 2004 | 121,419,193            | 387,606,250                | 58,516,750                   |
| 2005 | 147,852,304            | 443,700,986 *              | 73,653,750 *                 |

\* Examination Change

## Neighborhood Health Plan, Inc.

### Management

#### *Annual Meeting*

The bylaws indicate that the annual meeting of the Plan shall be held each year at such time, date and place as determined by the Directors upon twenty-four hours notice by telephone or facsimile, or upon written notice sent via the mail at least five days prior to the meeting. The annual meeting for 2005 was held on June 30, 2005.

#### *Board of Directors*

The bylaws provide that the Board of Directors shall manage the business and affairs of the Plan. Directors shall be elected at any meeting of the Members. The Members of the Plan are composed of the president of the Massachusetts League of Community Health Centers, Inc., a Massachusetts non-profit corporation (the "League"), the president of the Plan, and the chair of the Plan's Board of Directors. The Board of Directors shall consist of fifteen directors, subject to reduction to thirteen. Thirteen of the directors shall be elected by the Members and shall be (i) the president of the corporation and the president of the League and elected by the Members (the "Ex-Officio Directors" with the power to vote), (ii) seven directors nominated by the League and elected by the Members (the "League Directors"), and (iv) four directors that the Members shall elect (the "At Large Directors"). So long as any amounts remain unpaid under the Surplus Note issued by the Plan to Blue Cross Blue Shield of Massachusetts ("BCBSMA"), two of the directors shall be elected by BCBSMA (the "BCBSMA Directors"). Upon payment in full of the Surplus Note, the number of directors may be reduced to thirteen. Each Director, other than the Ex-Officio Directors, shall serve for a term of three years.

At December 31, 2005 the Board was comprised of fifteen members.

Directors duly elected and serving at December 31, 2005, with address and business affiliation below:

#### **Name of Director**

Lori Berry

#### **Business Affiliation**

Executive Director  
Lynn Community Health Center  
Lynn, MA

**Neighborhood Health Plan, Inc.**

|                      |  |
|----------------------|--|
| Tristram Blake       | Chief Executive Officer<br>South End Community Health Center<br>Boston, MA                       |
| Jay Breines          | Executive Director<br>Holyoke Health Center, Inc.<br>Holyoke, MA                                 |
| Bruce Bullen         | Chief Operating Officer<br>Harvard Pilgrim Health Care<br>Wellesley, MA                          |
| Deborah Enos         | Incoming CEO & President at Dec 2005<br>Neighborhood Health Plan<br>Boston, Ma                   |
| John A. Fallon, M.D. | Chief Physician Executive<br>Senior Vice President<br>Blue Cross Blue Shield of MA<br>Boston, MA |
| Joseph D. Feaster    | Of Counsel, Attorney<br>McKenzie & Associates, P.C.<br>Roxbury, MA                               |
| Zoila Torres Feldman | Executive Director<br>Great Brook Valley Health Center<br>Worcester, MA                          |
| Charles T. Grigsby   | Senior Vice President<br>The Life Initiative<br>Boston, MA                                       |
| James Hooley         | Retired CEO & President at Dec 2005<br>Neighborhood Health Plan<br>Boston, MA                    |
| James W. Hunt, Jr.   | President and Chief Executive Officer<br>MA League of Community Health Centers<br>Boston, MA     |
| Robert J. Ingala     | Chief Executive Officer<br>Greater Lawrence Family Health Center<br>Lawrence, MA                 |

## Neighborhood Health Plan, Inc.

|                       |   |
|-----------------------|---|
| Allen Maltz           | Chief Financial Officer<br>Blue Cross Blue Shield of MA<br>Boston, MA                           |
| Tom Manning           | Deputy Chancellor for Operations and<br>Commonwealth Medicine<br>UMass Medical<br>Worcester, MA |
| Paulette Shaw Querner | Executive Director<br>Neponset Health Center<br>Dorchester, MA                                  |
| Tobias Yarmonlinsky   | Managing Director, Fixed Income Banking<br>RBC Dain Rauscher<br>Boston, MA                      |

The bylaws do not specify the number of meetings to be held during a year. The minutes of the Board of Directors meetings indicated that meetings were held eleven times in 2003, ten times in 2004, and nine times in 2005. At any meeting of the Board of Directors, a majority of directors constitutes a quorum.

The Board of Directors appoints several committees in accordance with the By-laws. The purpose and membership of each committee at December 31, 2005 follows:

### *Patient Care Assessment Committee*

The Patient Care Assessment Committee ("PCA") reviews and recommends changes and improvements to the Plan's PCA Program. The committee also investigates and reports on quality of care issues.

### *Executive Committee*

The Executive Committee is comprised of not less than three Directors who are Independent Directors, in addition to the Chairman of the Board and the President. The Executive Committee is empowered to act on behalf of the Board between meetings and is charged with the duty of general supervision between regular meetings of the Board over the business operations, financial affairs, and corporate governance of the Plan. It reports to each meeting of the Board all deliberations and decisions it made since the last meeting of the Board. The Board of Directors shall annually appoint an Independent Director as Chairman of the Executive Committee, who shall be deemed for all purposes to be the Lead Director of the Plan. Directors serving on this Committee at December 31, 2005, are as follows:

|                  |            |
|------------------|------------|
| Robert Ingala    | Chair      |
| Joseph Feaster   | Vice Chair |
| Toby Yarmolinsky | Treasurer  |



## Neighborhood Health Plan, Inc.

### *Finance Committee*

The Finance Committee is comprised of not less than three Directors in addition to the President and the Treasurer. It is empowered to act on behalf of the Board on matters involving the general supervision over the investment or loaning of funds of the Plan. In addition to the powers specifically set forth in the Bylaws, the Finance Committee shall have such further powers and perform such other duties as the Board may from time to time prescribe. The Finance Committee shall report to each regular meeting of the Board all transactions carried out by the Committee since the last regular Board meeting. Directors serving on this Committee at December 31, 2005, are as follows:

|                  |       |
|------------------|-------|
| Tristam Blake    |       |
| James Hooley     |       |
| Toby Yarmolinsky | Chair |

### *Audit Committee*

The Audit Committee is comprised of not less than three Directors, a majority of whom qualify as Independent Directors. The Chairman of the Audit Committee, who shall be an Independent Director, shall be elected annually by members of this Committee. The Audit Committee is empowered to act on behalf of the Board on matters concerning general supervision and oversight of corporate accounting, the financial reporting processes and internal control systems of the Plan, and the quality and integrity of the Plan's financial statements. It shall engage the Plan's outside auditor, monitor its independence and performance, and meet privately as appropriate with the outside auditor; it is authorized to directly engage on the Plan's behalf such accountants, counsel, or other professionals as it believes necessary and appropriate. In addition, it shall have such further powers and perform such other duties as the Board may from time to time prescribe. Directors serving on this Committee at December 31, 2005, are as follows:

|                 |       |
|-----------------|-------|
| Charles Grigsby | Chair |
| Robert Ingala   |       |
| Allen Maltz     |       |

### *Conflict Review Committee*

The Conflict Review Committee is a special committee of the board of directors that is elected each year to review all disclosures made under Section I.A.I. of the Conflict of Interest Policy. The Committee is delegated the power and authority to approve for and on behalf of the board of directors interested transactions involving goods or services provided to NHP having a gross cost or value not exceeding \$50,000 in any one year and other interested transactions referred to it for review by the board of directors provided all of such committee's members are disinterested directors with respect to the transaction being reviewed. The Audit Committee may serve as the Conflict Review Committee if the board of directors so approves. The Conflict Review Committee shall report its decisions to the board of directors at the next meeting of the board of directors

## Neighborhood Health Plan, Inc.

following the meeting of the Conflict Review committee. A majority of the Conflict Review committee shall constitute a quorum thereof.

### *Contract Review Committee*

A special committee of the board of directors elected each year by the board of directors and shall be composed exclusively of directors of NHP who have no relationship with any Related Providers. The Conflict Review Committee may serve as the Contract Review Committee if its membership so qualifies and the board of directors approve. A majority of the Contract Review Committee constitutes a quorum thereof.

### *Officers*

The bylaws of the Plan provide that the officers of the Plan shall be a president, a chair, a vice chair, a treasurer, a clerk and such other officers as deemed necessary. The bylaws state that the chair, treasurer, and clerk shall be elected annually by the directors

Vacancies among the officers may be filled and new offices created and filled by an affirmative vote of the majority of directors then in office.

As noted in the annual statement, officers and their respective titles at December 31, 2005 follow:

| <u>Name</u>       | <u>Title</u>                        |
|-------------------|-------------------------------------|
| Deborah Enos      | President & Chief Executive Officer |
| Robert Ingala     | Chair                               |
| Joseph Feaster    | Vice Chair                          |
| Toby Yarmolinsky  | Treasurer                           |
| Frederick J. Marx | Clerk                               |

### Conflict of Interest Procedures

The Plan has adopted a policy statement pertaining to conflict-of-interest in accordance with Question 15 of the General Interrogatories of the Annual Statement. The Plan has an established procedure for the disclosure to the Board of Directors of any material interest or affiliation on the part of any officer or director, which is in or is likely to conflict with his/her official duties.

Annually, each officer, director and responsible employee completes a questionnaire disclosing any material conflicts of interest. The completed questionnaires were reviewed, and no discrepancies noted in the responses to the General Interrogatories regarding conflicts of interest as reflected in the Plan's 2005 Annual Statement.

## Neighborhood Health Plan, Inc.

### Corporate Records

#### *Articles of Incorporation and Bylaws*

The bylaws and Articles of Incorporation and amendments thereto were read. Based upon the reading of the bylaws and Articles and amendments thereto, the Plan is operating in compliance with its bylaws and in accordance with the purpose, functions and policies as set forth in its Articles of Incorporation.

#### *Board of Directors Minutes*

The minutes of meetings of the Board of Directors for the period under statutory examination were read and indicated that all meetings were held in accordance with the Plan bylaws and the laws of the Commonwealth of Massachusetts. The Board minutes contained the necessary votes and authorizations.

### Surplus Notes

On May 3, 2002 the Plan and HPHC entered into an agreement to deaffiliate and HPHC ceased to be the sole corporate member of NHP. On May 30, 2002 the Board of Directors was reduced to eleven directors. Under the deaffiliation agreement, HPHC continued to perform all of its responsibilities relative to the credentialing and recredentialing of a subset of the Plan's practitioner network for a period of three years following May 3, 2002; provide pharmaceutical contract management services for a period of three years following May 3, 2002, subject to permissions of contracting parties and payment of a quarterly fee to HPHC; and continued to sponsor the Plan and CMA under existing HPHC insurance policies until the expiration date of each policy, which extended through May 31, 2004.

On November 13, 2003, NHP issued a \$10,000,000 surplus note to BCBSMA in exchange for cash to be classified as surplus for statutory purposes. The note is unsecured and is subordinate to all present and future indebtedness of NHP, policy claims, and prior claims against the NHP, as provided by Massachusetts General Laws. This was voted by NHP's Board of Directors and appropriate filings were made with the Division. Issuance was approved by the Commissioner of Insurance of the Commonwealth of Massachusetts ("Massachusetts Commissioner").

The interest rate on the note is 5.3% annually for the first five years and two hundred basis points above the one-year US Treasury Bill rate, thereafter. Interest payments are paid semiannually for the first ten years and due April 1 and October 1. Principal payments commence on April 1, 2014 and will be paid at \$1,000,000 semiannually until October 1, 2018. All payments of principal and interest are subject to the approval of the commissioner of the DOI. The agreement requires NHP to notify BCBSMA in the event the total net assets of NHP decrease below \$20,000,000. NHP was in compliance with the debt covenant at December 31, 2005.

## Neighborhood Health Plan, Inc.

### AFFILIATED COMPANIES

The Plan is a member of a holding company system with Community Medical Alliance, Inc.

#### Organization Chart



#### Transactions and Agreements with Subsidiaries and Affiliates

Effective September 1, 1999, the Plan entered into a ten-year agreement with their affiliate, Community Medical Alliance, Inc. to provide certain accounting, management, and other services. CMA pays the Plan an amount equal to their Administrative Services budget in twelve equal monthly installments. The Plan is CMA's only source of revenue, other than occasional minor grant amounts.

### FIDELITY BOND AND OTHER INSURANCE

The Plan maintains fidelity coverage with an authorized Massachusetts insurer. The aggregate limit of liability exceeds the NAIC's suggested minimum.

The Plan has further protected its interests and properties by policies of insurance covering other insurable risks. Coverage is provided by insurers licensed in the Commonwealth of Massachusetts and was in force as of December 31, 2005.

### **PENSION, STOCK OWNERSHIP AND INSURANCE PLANS**

NHP offers various insurance plans, including group and family life, dental and health coverage, short-term and long-term disability, and personal accident insurance to all employees working a minimum of 20 hours per week.

NHP offers a retirement plan, which includes profit sharing, to all eligible employees of NHP. The plan, which is a defined contribution plan, permits all participating employees of NHP to make voluntary before-tax contributions on the first day of the calendar quarter following her or his date of hire. NHP offers matching and profit sharing contributions to eligible employees after satisfying certain waiting periods.

### **STATUTORY DEPOSITS**

The statutory deposits of the Plan as of December 31, 2005, are as follows:

| <u>Location</u> | <u>Description of Deposit</u>     | <u>Par Value</u> | <u>Statement Value</u> | <u>Fair Value</u> |
|-----------------|-----------------------------------|------------------|------------------------|-------------------|
| Massachusetts   | US Treasury Note<br>6.5% due 2006 | \$ 1,000,000     | \$ 1,034,072           | \$ 1,015,200      |
| Total           |                                   | \$ 1,000,000     | \$ 1,034,072           | \$ 1,015,200      |

### **INSURANCE PRODUCTS AND RELATED PRACTICES**

#### **Territory and Plan of Operations**

The Plan is licensed to transact business in Massachusetts and is not licensed in any other state.

The Plan is a Network-Model HMO, which arranges for the delivery of comprehensive health care services on a prepaid basis to covered members. Physicians providing services to Plan members are not employees of the HMO, but are affiliated through contractual relationships.

Approximately 81% percent of the Plan's business is derived from providing health care coverage to Medicaid beneficiaries through a Managed Care Organization contract with the Commonwealth of Massachusetts Division of Medical Assistance. The Plan also offers a commercial product.

#### **Advertising and Sales Materials**

The Plan uses brochures and trade journals to advertise its insurance products. Advertising and sales material used during the examination period were reviewed. No misleading advertising was noted.

Treatment of Subscribers

*Claims Settlement Practices*

Procedures performed in conjunction with the claims test work indicated that the Plan investigates and settles claims on a timely and equitable basis.

*Claimant Complaints*

During the course of the examination, a general review was made of the manner in which the Plan conducts its business practices and fulfills its contractual obligations to claimants. This review was limited in nature and was substantially narrower than a full scope market conduct examination.

**REINSURANCE**

Ceded Reinsurance

**Reliastar Life Insurance Company:**

Since January 1, 2001, the Plan has participated in an excess of loss reinsurance agreement with Reliastar Life Insurance Company (the "Reinsurer"), an authorized Massachusetts insurance company. The reinsurance services provided by the Reinsurer are facilitated through an intermediary, Evergreen Re. The excess of loss agreement provides for 90% reimbursement to the Plan for an insured member's eligible inpatient and outpatient services exceeding \$225,000 through the 2004 policy year and \$400,000 through the 2005 policy year. There are internal limitations in both percentage and dollar amount reimbursement, such as \$1,000/day for outpatient services and \$4,000/day for inpatient services. There is a limit of \$1,500,000 per member per year and a maximum of \$2,000,000 per member for all agreement years.

The reinsurance agreement also includes an endorsement that provides the Plan with \$10,000,000 coverage in the event of the Plan's insolvency. Please see the Subsequent Events section on page 13 of this Report of Examination for changes made to the reinsurance agreement.

Conversion coverage was available to all members. The agreement contained an insolvency clause.

The Plan did not assume any reinsurance risk during the years under examination.

### **SUBSEQUENT EVENTS**

- Effective January 1, 2006, the Plan changed reinsurance companies replacing Reliastar Life Insurance Company with Allianz Life Insurance Company of North America, a licensed or approved Massachusetts insurance company.
- In April 2006, the Massachusetts legislature passed a new law that will expand access to health insurance to all Massachusetts residents. A component of the law is The Commonwealth Care Health Insurance Program (“Commonwealth Care”), a program run by the Commonwealth Health Insurance Connector Authority (the “Connector”) that was established as part of the new law. There are two components of Commonwealth Care:
  - (1) Products for those earning 100% or less of the Federal Poverty Level (“FPL”) and paid for in full by the State. This product went live on October 1, 2006 with members effective beginning November 1, 2006.
  - (2) Products for those earning above 100% and up to 300% of FPL and subsidized by the State on a sliding scale based on income. This product went live on January 1, 2007 and members will be effective beginning on February 1, 2007.

NHP is one of four plans participating in offering Commonwealth Care to Massachusetts residents. As of January 12, 2007, NHP has 7,428 members in its 100% or less of FPL Commonwealth Care product.

An additional component of the new health care legislation is designed to offer non-subsidized, affordable health plans for those earning more than 300% of the FPL. These products will go live on April 1, 2007.

### **ACCOUNTS AND RECORDS**

The internal controls structure was discussed with management through questionnaires and through a review of the work performed by the Plan’s Independent Certified Public Accountants. No material differences were noted.

The NAIC provides a questionnaire covering the evaluation of the controls in the Information Systems (IS) environment. The questionnaire was completed by the Plan and reviewed by the Division, which evaluated the adequacy of the information systems controls. No material deficiencies were noted.

The Plan uses an automated general ledger system. Trial balances were traced from the general ledger and supporting documents to the 2005 Annual Statement.

The books and records of the Plan are audited annually by independent Certified Public Accountants in accordance with 211 CMR 23.00.

**Neighborhood Health Plan, Inc.**

**FINANCIAL STATEMENTS**

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Division of Insurance of the Commonwealth of Massachusetts and by the *National Association of Insurance Commissioners* as of December 31, 2005.

Statement of Assets, Liabilities, and Capital and Surplus as of December 31, 2005

Statement of Revenue and Expenses for the Year Ended December 31, 2005

Reconciliation of Capital and Surplus, for Each Year in the Three-Year Period Ended December 31, 2005

For Information Purposes Only



**Neighborhood Health Plan, Inc.**

**Statement of Assets, Liabilities, Surplus and Other Funds  
As of December 31, 2005**

| <b>Assets</b>                                      | <b>As Reported by<br/>the Plan</b> | <b>Examination<br/>Changes</b> | <b>Per Statutory<br/>Examination</b> | <b>Notes</b> |
|--|------------------------------------|--------------------------------|--------------------------------------|--------------|
| Bonds  | \$ 101,667,142                     | \$ 0                           | \$ 101,667,142                       |              |
| Cash and short-term investments                    | 41,578,707                         |                                | 41,578,707                           |              |
| Subtotals, cash and invested assets                | 143,245,849                        | -                              | 143,245,849                          |              |
| Investment income due and accrued                  | 746,242                            |                                | 746,242                              |              |
| Premiums and considerations:                       |                                    |                                |                                      |              |
| Uncollected premiums and agents' balances          |                                    |                                |                                      |              |
| in course of collection                            | 784,272                            |                                | 784,272                              |              |
| Reinsurance: Amounts recoverable from reinsurers   | 301,334                            |                                | 301,334                              |              |
| Electronic data processing equipment and software  | 1,608,653                          |                                | 1,608,653                            |              |
| Health care and other amounts receivable           | 1,007,051                          |                                | 1,007,051                            |              |
| Aggregate write-ins for other than invested assets | 158,903                            |                                | 158,903                              |              |
| Total Assets                                       | <u>\$ 147,852,304</u>              | <u>\$ 0</u>                    | <u>\$ 147,852,304</u>                |              |

**Neighborhood Health Plan, Inc.**

**Statement of Assets, Liabilities, Surplus and Other Funds  
As of December 31, 2005**

|   | As Reported by<br>the Plan | Examination<br>Changes | Per Statutory<br>Examination | Notes |
|---|----------------------------|------------------------|------------------------------|-------|
| <b>Liabilities</b>  |                            |                        |                              |       |
| Claim unpaid  | \$ 67,230,463              | \$ 0                   | \$ 67,230,463                | (1)   |
| Premiums received in advance                              | 978,606                    |                        | 978,606                      |       |
| General expenses due or accrued                           | 5,606,058                  |                        | 5,606,058                    |       |
| Amounts withheld or retained for the<br>account of others | 102,440                    |                        | 102,440                      |       |
| Borrowed money and interest thereon                       | 132,500                    |                        | 132,500                      |       |
| Amounts due to parent, subsidiaries and affiliates        | 17,355                     |                        | 17,355                       |       |
| Aggregate write-in for liabilities:                       |                            |                        |                              |       |
| Campaign for Excellence                                   | 131,132                    |                        | 131,132                      |       |
| Deferred Revenue  | 3,830,019                  | \$ (3,830,019)         |                              | (2)   |
| Total Liabilities   | <u>78,028,573</u>          |                        | <u>74,198,554</u>            |       |
| Surplus notes   | 10,000,000                 |                        | 10,000,000                   |       |
| Unassigned funds (surplus)                                | <u>59,823,731</u>          | 3,830,019              | <u>63,653,750</u>            | (2)   |
| Surplus as regards policyholders                          | <u>69,823,731</u>          | 3,830,019              | <u>73,653,750</u>            |       |
| Total Liabilities, Capital, and Surplus                   | <u>\$ 147,852,304</u>      | <u>\$ 0</u>            | <u>\$ 147,852,304</u>        |       |

**Neighborhood Health Plan, Inc.**

**Statement of Revenue and Expenses  
For The Year Ended December 31, 2005**

|  | As Reported by<br>the Plan | Examination<br>Changes | Per Statutory<br>Examination | Notes |
|--|----------------------------|------------------------|------------------------------|-------|
| Net premium income                                 | \$ 439,870,967             | \$3,830,019            | \$ 443,700,986               | (2)   |
| Total revenue                                      | 439,870,967                | \$3,830,019            | 443,700,986                  |       |
| <b>Hospital and Medical:</b>                       |                            |                        |                              |       |
| Hospital/medical benefits                          | 310,085,780                |                        | 310,085,780                  |       |
| Other professional services                        | 26,125,506                 |                        | 26,125,506                   |       |
| Emergency Room and out-of-area                     | 22,905,958                 |                        | 22,905,958                   |       |
| Prescription drugs                                 | 34,888,770                 |                        | 34,888,770                   |       |
| Aggregate write-ins for other hospital and medical | (130,807)                  |                        | (130,807)                    |       |
| Subtotal   | 393,875,207                | -                      | 393,875,207                  |       |
| <b>Less:</b>                                       |                            |                        |                              |       |
| Net reinsurance recoveries                         | 793,143                    |                        | 793,143                      |       |
| Total medical and hospital                         | 393,082,064                | -                      | 393,082,064                  |       |
| Claims adjustment expenses                         | 20,254,503                 |                        | 20,254,503                   |       |
| General administrative expenses                    | 17,593,987                 |                        | 17,593,987                   |       |
| Total underwriting deductions                      | 430,930,554                | -                      | 430,930,554                  |       |
| Net underwriting gain                              | 8,940,413                  |                        | 12,770,432                   |       |
| Net investment income earned                       | 3,373,665                  |                        | 3,373,665                    |       |
| Net realized capital losses                        | (345,840)                  |                        | (345,840)                    |       |
| Net investment gains                               | 3,027,825                  | -                      | 3,027,825                    |       |
| Aggregate write-ins for other income               | 253,467                    |                        | 253,467                      |       |
| Net income   | \$ 12,221,705              | \$ 3,830,019           | \$ 16,051,724                |       |

Neighborhood Health Plan, Inc.

**Reconciliation of Capital and Surplus  
For Each Year in the Three Year Period Ended December 31, 2005**

|  | 2005 *        | 2004          | 2003          |
|--|---------------|---------------|---------------|
| Capital and surplus prior reporting period           | \$ 58,516,750 | \$ 37,794,310 | \$ 15,854,089 |
| <b>Gains and Losses to Capital and Surplus:</b>      |               |               |               |
| Net income   | 16,051,724    | 22,099,042    | 11,711,431    |
| Post-filing audit adjustments                        |               |               | 275,920       |
| Net unrealized capital gains and losses              |               |               | (502,105)     |
| Change in non-admitted assets                        | (914,724)     | 107,650       | 454,975       |
| Change in surplus notes                              |               |               | 10,000,000    |
| Aggregate write-ins for gains or (losses) in surplus |               | (1,484,252)   |               |
| Net change in capital & surplus                      | 15,137,000    | 20,722,440    | 21,940,221    |
| Capital and surplus end of reporting period          | \$ 73,653,750 | \$ 58,516,750 | \$ 37,794,310 |

\* Per Examination

**NOTES TO FINANCIAL STATEMENTS**

**Note 1: Claims Unpaid**

In conjunction with the Division's regulatory examination of the Plan's financial statements, an independent certified public accounting firm, KPMG LLP, was retained by the Division to review the methodology and adequacy of the Unpaid Claim Liability of the Plan as of December 31, 2005, and to perform a review of the Plan's premium rating processes including the Plan's premium deficiency and rate adequacy analysis. A summary of findings is noted below:

- The Unpaid Claim Liability at December 31, 2005 is fairly stated in aggregate in all material respects.
- The reserve is calculated in accordance with Massachusetts' laws and regulations and NAIC requirements.
- The Plan's booked reserves include a provision for Loss Adjustment Expenses in 2005, and the resulting expense percentages are within industry norms.
- The Plan's premium deficiency reserve calculation was found to be reasonable, with no premium deficiency reserves required at December 31, 2005.
- There are no rate adequacy issues as of December 31, 2005.

**Note 2: Deferred Revenue**

Based upon a recommendation by the Plan's independent auditors, the Plan made a subsequent adjustment to its 2005 statutory annual statement filing to realize revenue as "Net Premium Earned" that it had reported as deferred revenue in its 2005 Statement of Liabilities, Capital and Surplus. This amount represented transitional payments made to the Plan through its Managed Care Organization Contract ("MCO") with the Commonwealth of Massachusetts, Executive Office of Health and Human Services Department. The recommendation was made following a review of the MCO and accompanying documents, and referencing guidance relative to revenue recognition.

**ACKNOWLEDGMENT**

Acknowledgment is made of the cooperation and courtesies extended by the officers and employees of the Plan.

The assistance rendered by the following Massachusetts Division of Insurance examiners who participated in this examination is hereby acknowledged:

Ravinder S. Chana, Examiner III  
Linh Ngu, Examiner II

---

John A. Turchi, CFE, CPCU  
Supervising Examiner  
Commonwealth of Massachusetts  
Division of Insurance