REPORT ON EXAMINATION

OF

GROUP HEALTH INCORPORATED

AS OF

DECEMBER 31, 2013

DATE OF REPORT	**MARCH 9, 2018**
EXAMINER	**JO LO HSIA, ARM**

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NEW YORK STATE
DEPARTMENT of
FINANCIAL SERVICES

Andrew M. Cuomo
Governor

Maria T. Vullo
Superintendent

March 9, 2018

Honorable Maria T. Vullo
Superintendent of Financial Services
Albany, New York 12257

Madam:

Pursuant to the requirements of the New York Insurance Law, and acting in accordance with the instructions contained in Appointment No. 31208, dated November 6, 2014, and annexed hereto, an examination has been made into the financial condition and affairs of Group Health Incorporated ("GHI"), a not-for-profit health service corporation licensed pursuant to Article 43 of the New York Insurance Law, as of December 31, 2013, and the following report thereon is respectfully submitted.

The examination was conducted at the home office of Group Health Incorporated, located at 55 Water Street, New York, NY.

Wherever the designations the "Plan" or "GHI" appear herein, without qualification, they should be understood to indicate Group Health Incorporated.

Wherever the designation "HIPNY" appears herein, without qualification, it should be understood to indicate the Health Insurance Plan of Greater New York, the direct Parent of GHI.

Wherever the designation "EmblemHealth" appears herein, without qualification, it should be understood to indicate EmblemHealth, Inc., the ultimate Parent of GHI and HIPNY.

Wherever the designation the “Department” appears herein, without qualification, it should be understood to indicate the New York State Department of Financial Services.

A separate market conduct examination reviewing the manner in which GHI conducts its business practices and fulfills its contractual obligations to policyholders and claimants was conducted as of December 31, 2013. A separate report will be submitted thereon.

1. **SCOPE OF THE EXAMINATION**

The Plan was previously examined as of December 31, 2008. This examination of the Plan is a financial examination as defined in the National Association of Insurance Commissioners ("NAIC") *Financial Condition Examiners Handbook, 2014 Edition* (the "Handbook") and it covers the five-year period January 1, 2009 through December 31, 2013. The examination was conducted observing the guidelines and procedures in the Handbook and, where deemed appropriate by the examiner, transactions occurring subsequent to December 31, 2013, were also reviewed.

This examination was conducted on a risk-focused basis in accordance with the provisions of the Handbook, which provides guidance for the establishment of an examination plan based on the examiner's assessment of risk in the Plan's operations and utilizes that evaluation in formulating the nature and extent of the examination. The examiner planned and performed the examination to evaluate the Plan's current financial condition, as well as to identify prospective risks that may threaten the future solvency of GHI.

The examiner identified key processes, assessed the risks within those processes and assessed the internal control systems and procedures used to mitigate those risks. The examination also included an assessment of the principles used and significant estimates made by management, an evaluation of the overall financial statement presentation, and determined management's compliance with the Department's statutes and guidelines, Statutory Accounting Principles, as adopted by the Department, and NAIC annual statement instructions.

Information concerning the Plan's organizational structure, business approach and control environment were utilized to develop the examination approach. The examination evaluated the

Plan’s risks and management activities in accordance with the NAIC’s nine branded risk categories.

These categories are as follows:

- Pricing/Underwriting
- Reserving
- Operational
- Strategic
- Credit
- Market
- Liquidity
- Legal
- Reputational

The Plan was audited annually, for the years 2009 through 2013, by the accounting firm of Deloitte & Touche LLP (“D&T”). The Plan received an unqualified opinion in each of those years. Certain audit workpapers of D&T were reviewed and relied upon in conjunction with this examination. EmblemHealth, ultimate Parent of GHI, has an Internal Audit Department and a separate Internal Control Department, which have been given the task of assessing the internal control structure and compliance with the Sarbanes-Oxley Act of 2002 (“SOX”) for its subsidiaries, including GHI. As a non-public company, the Plan is not obligated to comply with SOX directives, and accordingly, is not required to submit an assessment of its internal control structure to the U.S. Securities and Exchange Commission. However, GHI nonetheless established a department to achieve this goal. Where applicable, workpapers and reports were reviewed and portions thereof were relied upon for this examination.

The examiner reviewed the corrective actions taken by the Plan with respect to the recommendations concerning financial issues contained in the prior report on examination. The results of the examiner’s review are contained in Item 9 of this Report.

This report on examination is confined to financial statements and comments on those matters which involve departure from laws, regulations or rules, or which require explanation or description.

2. EXECUTIVE SUMMARY

The examination revealed several operational deficiencies that occurred during the examination period. The following are the significant findings included within this report on examination:

- At the time of examination, EmblemHealth's enterprise risk management function was not yet fully developed, in accordance with the requirements of Insurance Circular Letter No. 14 (2011), Section 1503(b) of the New York Insurance Law ("NYIL"), and Part 82.2(a) of Insurance Regulation No. 203 - *Enterprise Risk Management and Own Risk and Solvency Assessment*.
- The Plan failed to comply with the requirements of Part 89.5(e)(2) of Insurance Regulation No. 118 when it did not attach a statement, that its external auditor does not function in the role of management, does not audit his or her own work, and does not serve in an advocacy role for the Plan, to its filed audited financial statements for reporting years 2010 through 2013.
- The Plan's Audit Committee failed to comply with the requirements of Part 89.5(h) of Insurance Regulation No. 118 when it did not pre-approve all of its non-audit services provided by its external auditor. Further it did not document such approval in its meeting minutes.
- The Plan failed to comply with the requirements of Part 89.12(e) of Insurance Regulation No. 118 when it did not provide written notification to the Department of the selection of its audit committee within 30 days of the effective date of the Regulation and when it failed to provide written notice to the Department within 30 days of changes in membership of its audit committee during the examination period.
- The Plan failed to maintain a sufficient statutory reserve as required by Section 4310(d)(2) of the New York Insurance Law during the examination period.
- For years ending 2014 and 2015, GHI's administrative expense ratio exceeded the limitation set forth in Section 4309 of the NYIL.

The above findings, as well as others, are described in greater detail in the remainder of this report on examination.

3. DESCRIPTION OF THE PLAN

GHI is a New York State not-for-profit corporation operating under the provisions of Article 43 of the New York Insurance Law.

On November 15, 2006, having received regulatory approval from the Department, GHI and HIPNY, a not-for-profit health service corporation licensed under the provisions of Article 43 of the New York Insurance Law, became affiliated companies. As a result of this transaction, EmblemHealth Inc., a New York not-for-profit organization, became the sole member and Parent of HIPNY, GHI and their respective subsidiaries. HIPNY and GHI named an equal number of directors to the EmblemHealth Board of Directors.

On March 6, 2007, EmblemHealth Services Company, LLC ("EHS") was formed by a joint venture of HIPNY and GHI, in order to integrate operations of these two entities. On January 1, 2008, items such as vendor agreements and employees were transferred to EHS. GHI and HIPNY receive management and other services from EHS. Also on that date, with the approval of the Department, GHI and HIPNY entered into a written guaranty assuming jointly and severally the employee related compensation liabilities of EHS.

In December 2010, with the approval of the Department, HIPNY replaced EmblemHealth as the sole corporate member of GHI. In 2013, subsequent to the examination period, EmblemHealth filed to restructure the ownership of EmblemHealth Services Company, LLC so that it is wholly-owned by HIPNY. The Department issued a "non-objection" letter on December 23, 2013 with regard to this transaction.

Pursuant to Section 4301(j) and Section 7317 of the New York Insurance Law (the "Conversion Legislation"), GHI and HIPNY filed a plan of conversion (the "Conversion Plan") on April 16, 2007 seeking the approval of the Department's (then Department of Insurance) Superintendent (the "Superintendent") to convert from their not-for-profit status to for-profit status. The Conversion Plan was amended and refiled on December 31, 2007. Pursuant to the plan of conversion, GHI and HIPNY, both not-for-profit entities, would have become for-profit entities. Presently, GHI and HIPNY are not pursing conversion.

A. Management and Controls

1. Corporate Governance

Corporate governance, internal audit department ("IAD") and Model Audit Rule ("MAR"), Insurance Regulation No. 118 (11 NYCRR 89), processes for the Plan are provided by EmblemHealth, Inc., the ultimate Parent of GHI.

Exhibit M of the Handbook (*Understanding the Corporate Governance Structure*) was utilized by the examiner as guidance for assessing the Plan's Corporate Governance.

Standard 1110 – *Organizational Independence* – of the International Standards for the Professional Practice of Internal Auditing, issued by the Institute of Internal Auditors ("IIA"), states in part:

> "*The chief audit executive must report to a level within the organization that allows the internal audit activity to fulfill its responsibilities. The chief audit executive must confirm to the board, at least annually, the organizational independence of the internal audit activity…*
>
> *Organizational independence is effectively achieved when the chief audit executive reports functionally to the board. Examples of functional reporting to the board involve the board:*

- *Approving the internal audit charter;*
- *Approving the risk based internal audit plan;*
- *Approving the internal audit budget and resource plan;*
- *Receiving communications from the chief audit executive on the internal audit activity's performance relative to its plan and other matters;*
- *Approving decisions regarding the appointment and removal of the chief audit executive;*
- <u>*Approving the remuneration of the chief audit executive*</u>*..."* ***(emphasis added)***

It should be noted that the Plan's Board of Directors delegated its oversight function of Internal Audit to its Audit Committee.

The Chief Audit Executive of the Internal Audit Department of the Plan and its ultimate Parent, EmblemHealth, Inc., is also EmblemHealth's Senior Vice President ("SVP") of Corporate Compliance and Internal Audit. The Chief Audit Executive reported functionally to the Audit Committee instead of the Board. Additionally, the Audit Committees of the Plan and EmblemHealth did not establish a formal evaluation process to measure the performance of the Chief Audit Executive. It was further noted that the Audit Committees did not determine nor approve the compensation package for this individual. Instead, the Compensation Committees of the Plan and EmblemHealth not only determined the salary of the Chief Audit Executive of the Internal Audit Department but also determined and approved the incentive compensation of said person based on the financial performance goals and certain other goals of the Plan and EmblemHealth.

The performance and compensation of the Chief Audit Executive should have been determined and measured by the Audit Committee to ensure independence.

It is recommended as a best practice that the Audit Committees of the Plan and EmblemHealth, Inc., adhere to the provisions of Standard 1110 of the IIA's *International*

Standards for the Professional Practice of Internal Auditing by formally evaluating the performance of their Chief Audit Executive, and also by approving the annual compensation and salary adjustment of the position.

A similar recommendation was made to GHI's direct Parent, HIPNY, as part of the Department's financial examination of HIPNY as of December 31, 2011. In response to the Department's recommendation, HIPNY agreed that its Audit Committee, on a yearly basis, would evaluate the performance, and review and approve the compensation of the Chief Audit Executive.

It is recommended that the Audit Committee of GHI evaluate the performance, and review and approve the compensation of said Chief Audit Executive jointly with the Audit Committees of EmblemHealth and HIPNY.

Standard 1100 - *Independence and Objectivity* - of the IIA's International Standards for the Professional Practice of Internal Auditing states in part:

> *"Objectivity is an unbiased mental attitude that allows internal auditors to perform engagements in such a manner that they believe in their work product and that no quality compromises are made. Objectivity requires that internal auditors do not subordinate their judgment on audit matters to others..."*

Standard 1110.A1 - *Organizational Independence* - of the IIA's International Standards for the Professional Practice of Internal Auditing states:

> *"The internal audit activity must be free from interference in determining the scope of internal auditing, performing work, and communicating results."*

It should be noted that the Senior Vice President of Compliance, Internal Audit & Internal Controls of the Plan and EmblemHealth, had oversight responsibility for both the compliance and the internal audit functions of GHI during the examination period, which created the appearance of a conflict of interest.

The Department recommended, as part of its examination of HIPNY as of December 31, 2011, that EmblemHealth/HIPNY have separate individuals head their Compliance Department and their Internal Audit Department to ensure the objectivity and independence of their internal audit department.

In response to the Department's aforementioned recommendation to HIPNY, EmblemHealth/HIPNY appointed a new Chief Audit Executive. This new Chief Audit Executive reports functionally to the Audit Committee of the Board and administratively to the Chief Risk, Ethics, and Compliance Officer. However, the examiner determined that by having the Chief Audit Executive administratively report to the Chief Risk, Ethics, and Compliance Officer, the appearance of conflicts still exists.

It is recommended that EmblemHealth/HIPNY/GHI ensure the objectivity and independence of their Internal Audit Department by not having its Chief Audit Executive report to the Compliance Officer directly, or indirectly, or vice versa.

It should be noted that in May 2016, EmblemHealth/HIPNY/GHI terminated their employment relationship with their then Chief Risk, Ethics, and Compliance Officer. In the interim, the new Chief Audit Executive reports administratively to the Chief Legal Officer, who was also the Acting Chief Compliance Officer.

2. <u>Board of Directors</u>

In accordance with its 2010 amended by-laws, approved by the Department on December 1, 2010, the Plan is to be managed by a Board of Directors consisting of not less than seven (7) nor more than twenty-one (21) directors. An additional requirement of the by-laws is that the composition of the Board shall be structured and maintained in accordance with the requirements of Article 43 of the New York Insurance Law. The following listing, set forth by the classifications of Section 4301(k) of the New York Insurance Law, represents GHI's seven directors and their principal business affiliations as of December 31, 2013:

Name and Residence	Principal Business Affiliation
	Subscriber Directors
Susan Mathews Ft. Pierce, FL	Graduate Student, Bioethics
Arthur Pepper New York, NY	Executive Director, UFT Welfare Fund Co-Chair, MLC Health Benefits Subcommittee
Dennis Sullivan Yorkers, NY	Labor Relations Consultant, Self-employed
	Officers-Directors
Frank J. Branchini New York, NY	Chairman and CEO, EmblemHealth
John D. Feerick New York, NY	Professor of Law, Fordham University
David Weiss Northport, NY	Professor Emeritus, Hofstra University and Long Island University
	Provider Director
Bernard Schayes New York, NY	Physician, Private Practice

Subsequently, in 2015, Dennis Sullivan and Frank J. Branchini left GHI's Board of Directors (the "Board") and were replaced by Oliver Gray and Karen M. Ignagni, respectively. In

2016, Susan Mathews and Arthur Pepper left the Board and four new members (Stuart Altman, Richard Berman, James Gill, and Jay Russ) joined. Finally, James Gill left the Board early 2017.

The minutes of all meetings of the Board of Directors held during the examination period were reviewed. The following Directors were found to have attended less than 50% of the scheduled Board of Directors' meetings that they were eligible to attend during the examination period:

Director's Name	No. of Meetings Attended	No. of Meetings Eligible to Attend	Attendance Percentage
Harry Nespoli	1	13	8%
Roger Toussaint	0	3	0%

Attendance of Directors at Board meetings is critical in exercising their duties in a management oversight function. Members of the Board have a fiduciary responsibility and must evince an ongoing interest in the affairs of the Plan. It is essential that Board members attend meetings consistently and set forth their views on relevant matters so that appropriate policy decisions may be reached. Members who fail to attend at least one-half of the regular meetings do not fulfill such criteria.

It is recommended that the Plan take corrective action by developing a policy to evaluate whether Board members who are unable or unwilling to attend Board meetings consistently should resign or be replaced. Furthermore, in selecting prospective Board members, a key criterion should be their willingness and commitment to attend meetings and participate in the Board's responsibility to oversee the operations of the Plan.

It should be noted that the above two Directors are no longer serving on GHI's Board. Roger Toussaint was replaced by Dr. Aran Ron in 2009. Harry Nespoli vacated his Board seat in

2011; he was not replaced. During the examination period, GHI decreased the size of its Board of Directors from thirteen (13) members to seven (7) members.

3. Committees of the Board of Directors

Standing committees of the Board of Directors include the Executive Committee, Audit and Compliance Committee, Executive Remuneration and Organization Committee, Quality Improvement Committee and Investment Committee. In addition to the requirements set forth in the by-laws of the Board of Directors, each of the Committees is also subject to its own charter.

Section 15 of GHI's by-laws states in part:

> *"The Executive Remuneration and Organization Committee shall make recommendations to the Board of Directors as to the salaries to be paid to Chief Executive Officer, Officer, and for all elected officers of the Corporation who are also Directors of the Corporation... The Chief Executive Officer shall meet at least once a year with the Organization and Executive Remuneration Committee to review the Executive Remuneration Program for the Corporation's Officers and the organization plan of the Corporation."*

GHI's Organization and Remuneration Committee did not meet with the CEO during the examination period, as required by Section 15 of the Plan's by-laws. In fact, GHI's Organization and Remuneration Committee did not hold any meetings during the examination period.

It should be further noted that for the 2013 - 2014 serving term, there were no GHI Board members elected to serve on its Organization and Remuneration Committee; rather, the Committee's responsibility has been fulfilled by the Compensation Committee of EmblemHealth since 2008. EmblemHealth's Compensation Committee reviewed senior management's compensation across EmblemHealth's enterprise. Actions and reports of EmblemHealth's Compensation Committee were confirmed, ratified and adopted by GHI's Board during the examination period.

It is recommended that GHI update its by-laws to reflect the change in its committee structure and governance.

GHI filed its amended by-laws with the Department on October 6, 2015.

4. Executive Officers

Executive Officers of the Plan are elected by the Board of Directors at its annual meeting for a term of one year and serve at the discretion of the Board of Directors. The Executive Officers of the Plan at December 31, 2013, were as follows:

Name	**Position**
Frank J. Branchini	Chairman and Chief Executive Officer
Daniel P. Finke	President and Chief Operating Officer
Arthur J. Byrd	Chief Financial Officer

In early 2014, Daniel P. Finke left the Plan. The Chief Operating Officer position was subsequently filled by William Lamoreaux. In early 2015, Michael Palmateer replaced Arthur J. Byrd as the Chief Financial Officer. Frank J. Branchini retired in 2015. Karen M. Ignagni, became the President as of August 3, 2015, and the Chief Executive Officer as of September 1, 2015. Additionally, John D. Feerick became the Chairman of GHI's Board in 2015.

B. Territory and Plan of Operation

GHI is a health service corporation licensed under Article 43 of the New York Insurance Law to do business in New York State only.

As of December 31, 2013, the Plan's internal business divisions were: Hospital Preferred Provider Organization ("PPO"), Surgical-Medical PPO, Comprehensive PPO, Comprehensive Exclusive Provider Organization ("EPO"), Dental, Medicare Advantage, Medicare Supplement, Medicare Part D, Federal Employees Health Benefit Plan, and Healthy New York.

As of December 31, 2013, the total number of members reported by the Plan was 1,568,151, which represented a decline of 138,404 (8.1%) of members during the examination period. The decline in membership was mainly due to the loss of one of their large group accounts in 2011. The following shows the number of members enrolled and corresponding total revenue at the end of each year of the five-year examination period:

Year	Enrollment	Total Revenue
2009	1,706,555	$ 3,156,330,142
2010	1,733,827	$ 3,594,070,501
2011	1,616,818	$ 3,496,134,744
2012	1,593,995	$ 3,571,258,239
2013	1,568,151	$ 3,614,615,367

The Plan utilizes an internal sales force as well as independent agents and brokers.

C. <u>Enterprise Risk Management</u>

Insurance Circular Letter No. 14 (2011) states in part:

> "Given the importance of risk management, the Department of Financial Services ("Department") expects every insurer to adopt a formal Enterprise Risk Management ("ERM") function. An effective ERM function should identify, measure, aggregate, and manage risk exposures within predetermined tolerance levels, across all activities of the enterprise of which the insurer is part, or at the company level when the insurer is a stand-alone entity…"

Section 1503(b) of the New York Insurance Law states in part:

> "A holding company that directly or indirectly controls an insurer shall adopt a formal enterprise risk management function and shall file an enterprise risk report with the superintendent by April thirtieth of each year…"

Part 82.2(a) of Insurance Regulation No. 203 (11 NYCRR 82), which became effective June 9, 2014, states in part:

> "Pursuant to Insurance Law sections 1503(b), 1604(b), and 1717(b), an entity shall adopt a formal enterprise risk management function that identifies, assesses, monitors, and manages enterprise risk. Except as provided in subdivision (c) of this section, a domestic insurer that is not a member of a holding company system, an article 16 system, or an article 17 system also shall adopt such a formal enterprise risk management function. The enterprise risk management function shall be appropriate for the nature, scale, and complexity of the risk…"

In 2013, EmblemHealth started to develop its enterprise risk management ("ERM") function with the assistance of the public accounting firm of Dixon Hughes Goodman, LLP. It should be noted that EmblemHealth's ERM function, at the time of the examination, was not yet fully developed.

It is recommended that EmblemHealth adopt and implement its ERM function in accordance with the provisions of Insurance Circular Letter No. 14 (2011), Section 1503(b) of the New York Insurance Law, and Part 82.2(a) of Insurance Regulation No. 203.

D. Holding Company System

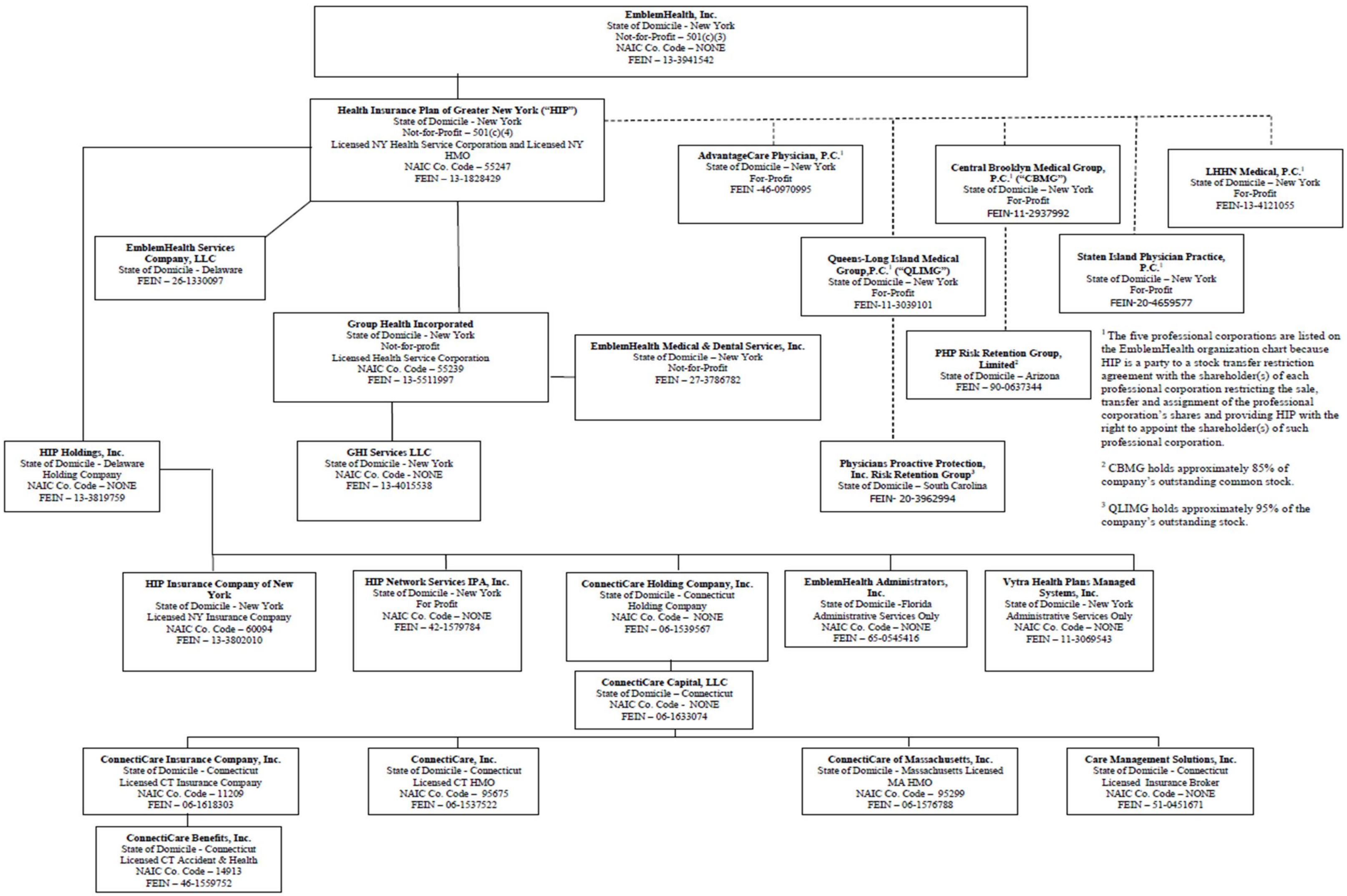
GHI is a not-for-profit health service corporation operating statewide in New York under the provisions of Article 43 of the New York Insurance Law. Its sole corporate member is Health Insurance Plan of Greater New York ("HIPNY").

HIPNY is a wholly-owned subsidiary of EmblemHealth, Inc., formerly known as *HIP Foundation, Inc.* EmblemHealth, Inc. is a New York not-for-profit charitable organization established to implement, expand and coordinate community outreach, medical research and other community based activities that support the well-being of the diverse population of the New York metropolitan area.

GHI is the Parent of GHI Services, LLC. GHI Services, LLC had been the sole shareholder of GHI HMO Select, Inc., doing business as GHI HMO. On June 26, 2013, with the approval of the New York Attorney General, the Department of Health, and this Department, GHI HMO merged into HIPNY.

On December 31, 2009, with approval of the Department, GHI merged with PerfectHealth, a for-profit stock accident and health company domiciled in New York and a direct subsidiary of HIP Holdings, Inc. GHI was the surviving entity after the merger. GHI funded this merger in a form of New York Insurance Law Section 1307 loan due to HIP Holdings, Inc. in an amount of $311,381 with zero interest.

The holding company chart depicting the relationship between the Plan and significant entities in its holding company system as of December 31, 2013, is as follows:



On September 18, 2008, GHI entered into the following administrative service agreements with members of its holding company system:

- Administrative Services Agreement with EmblemHealth Services Company, LLC (the "EHS Service Agreement")
- Administrative Services Agreement with ConnectiCare Capital, LLC (the "CCC LLC Service Agreement")
- Administrative Services Agreement with EmblemHealth Administrators, Inc. ("HIPA"), formerly known as HIP Administrators of Florida, Inc. (the "HIPA Service Agreement")

The aforementioned intercompany administrative service agreements were entered into for the purpose of the exchange of services and the use of certain personnel, facilities, equipment, personal property, licenses, and contracts owned or leased by each party named in the agreements.

Under the EHS Service Agreement, EHS provides management services and general administrative services such as accounting and financial services, investing, underwriting, rate and form development and filings, claims processing and other services to GHI. The administrative services provided by EHS are reimbursed by GHI on a pro-rata basis through intercompany accounts.

Under the CCC LLC Service Agreement, ConnectiCare Capital, LLC provides administrative services to EmblemHealth's ConnectiCare subsidiaries. Although GHI is a signing party of the CCC LLC Service Agreement, it should be noted that there were no direct services exchanged between GHI and ConnectiCare Capital, LLC during the examination period.

Under the HIPA Service Agreement, HIPA provides claims processing, customer services, enrollment processing, direct marketing, and grievance and appeals to entities served by EHS, including GHI and HIPNY. The services were charged based on rates set forth in the HIPA Service Agreement.

During the examination period, the Plan's federal income tax returns were consolidated with its 100% owned subsidiaries, GHI Services LLC, and GHI HMO Select, Inc. pursuant to their approved Intercompany Tax Allocation Agreement dated June 1, 1999.

E. Insurance Regulation No. 118 - Model Audit Rule

Part 89.5(e)(2) of Insurance Regulation No. 118 (11 NYCRR 89) states:

> "The company shall attach a statement to its audited annual financial statement, when filed, that the CPA does not function in the role of management, does not audit his or her own work, and does not serve in an advocacy role for the company."

Part 89.5(h) of Insurance Regulation No. 118 (11 NYCRR 89) states:

> "(h) The company's audit committee shall pre-approve all auditing services and non-audit services provided to the company by a CPA of the company except that a company need not preapprove non-audit services if:
>
> (1) the company is a SOX compliant company or a direct or indirect wholly-owned subsidiary of a SOX compliant company; or
>
> (2)(i) the aggregate amount of all such non-audit services provided to the company constitute five percent or less of the total amount of fees paid by the company to its CPA during the fiscal year in which the nonaudit services are provided;
>
> (ii) the services were not recognized by the company at the time of the engagement to be non-audit services; and
>
> (iii) the services are promptly brought to the attention of the audit committee and approved prior to the completion of the audit by the audit committee, or by one or more members of the audit committee who are the members of the board of directors to whom authority to grant such approvals has been delegated by the audit committee."

Part 89.12(e) of Insurance Regulation No. 118 (11 NYCRR 89) states:

> "(e) The company shall submit written notification to the superintendent of the selection of its audit committee within 30 days of the effective date of this Part and within 30 days of any change in membership of the audit committee. The notice shall include a description of the reason for the change."

GHI failed to attach the statement required by Part 89.5(e)(2) of Insurance Regulation No. 118 (11 NYCRR 89) when it filed its audited financial statements with the Department for reporting years 2010 through 2013.

GHI was audited annually, for the years 2009 through 2013, by the accounting firm of Deloitte & Touche LLP ("D&T"). It should be noted that in addition to the auditing services, D&T also provided non-audit services such as tax compliance, services in connection with the conversion and the filing of the S-1 Registration Statement, and services related to Medicare data validation. A review of the Audit Committee's minutes revealed the discussions of these non-audit services during the meetings. However, in some instances, the minutes failed to indicate whether these non-audit services were pre-approved by the Audit Committee.

GHI failed to provide written notification to the Department of the selection of its audit committee within 30 days of the effective date of Insurance Regulation No. 118. In addition, GHI failed to provide written notice to the Department within 30 days of any changes in membership of its audit committee during the examination period.

It is recommended that GHI comply with the requirements of Part 89.5(e)(2) of Insurance Regulation No. 118 by attaching the required statement to its filed audited financial statements.

It should be noted that GHI filed the statement required by Part 89.5(e)(2) of Insurance Regulation No. 118 for its 2015 and 2016 annual statements filings.

It is also recommended that GHI's Audit Committee comply with the requirements of Part 89.5(h) of Insurance Regulation No. 118 by pre-approving all non-audit services performed by its CPA and documenting such action in its meeting minutes.

In response to the aforementioned recommendation, GHI updated Section III, *Authority and Responsibilities*, of its Audit Committee charter to require its Audit Committee to pre-approve all services to be provided by its independent auditor to whom the internal auditing functions are outsourced.

It is recommended that GHI comply with the requirements of Part 89.12(e) of Insurance Regulation No. 118 by notifying the Department within 30 days of any change in membership of its Audit Committee. Such notice shall include a description of the reason for the change.

4. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities and surplus as contained in GHI's 2013 filed annual statement, a condensed summary of operations and a reconciliation of the surplus account for each of the years under review. The examiner's review of a sample of transactions did not reveal any differences which materially affected the Plan's financial condition as presented in its financial statements contained in the December 31, 2013 filed annual statement.

Independent Accountants

The accounting firm of Deloitte & Touche LLP ("D&T") was retained by the Plan to audit the Plan's combined statutory-basis statements of financial position as of December 31st of each year in the examination period, and the related statutory-basis statements of operations, surplus and cash flows for the year then ended. GHI received an unqualified opinion in each of those years.

D&T concluded that the statutory financial statements presented fairly, in all material respects, the financial position of the Plan at the respective audit dates. Balances reported in these audited financial statements were reconciled to the corresponding years' annual statements with no discrepancies noted.

Assets	
Bonds	$ 376,288,343
Common stocks	32,416,525
Properties occupied by the Plan	163,800,000
Cash, and short-term investment	(56,382,162)
Receivables for securities	221,751
Subtotal, cash and invested assets	516,344,457
Investment income due and accrued	2,773,598
Uncollected premiums and agents' balances in course of collection	223,420,865
Deferred premiums, agents' balances and installments booked but deferred and not yet due	2,943,494
Accrued retrospective premiums	2,310,389
Amounts receivable relating to uninsured plans	57,360,828
Federal and foreign income tax recoverable and interest thereon	4,056,052
Electronic data processing equipment, and software	51,542
Health care and other amounts receivable	26,852,096
Aggregate write-ins for other than invested assets	155,828,555
Total assets	$ 991,941,876
Liabilities	
Claims unpaid	$ 400,065,480
Unpaid claims adjustment expenses	14,380,815
Aggregate health policy reserves	174,274,344
Premiums received in advance	5,990,974
General expenses due or accrued	2,776,088
Amounts withheld or retained for the account of others	4,083,855
Remittances and items not allocated	348,057
Amounts due to parent, subsidiaries and affiliates	12,172,451
Liability for amounts held under uninsured plans	4,067,559
Aggregate write-ins for other liabilities	97,465,454
Total liabilities	$ 715,625,077
Surplus	
Aggregate write-ins for special surplus funds	49,326,697
Gross paid-in and contributed surplus	55,662,431
Surplus notes	165,311,381
Statutory reserves	434,229,044
Unassigned funds	(428,212,754)
Total surplus	$ 276,316,799
Total liabilities and surplus	$ 991,941,876

Note: The Internal Revenue Service has not completed its audit of the consolidated income tax returns filed on behalf of GHI and its subsidiaries through tax year 2011. The examiner is unaware of any potential exposure of the Company to any tax assessments and no liability has been established herein relative to such contingency.

B. Statement of Revenue and Expenses and Surplus

Surplus increased $ 36,861,287 during the five-year examination period, January 1, 2009 through December 31, 2013, detailed as follows:

Revenue		
Net premium income	$ 17,446,053,628	
Change in unearned premium reserve and reserve for rate credit	(22,874,875)	
Risk revenue	9,230,240	
Total revenue		$ 17,432,408,993
Expenses		
Hospital/ medical benefits	$ 5,427,679,301	
Other professional services	5,284,944,988	
Outside referrals	816,056	
Emergency room and out-of-area	2,237,481,672	
Prescription drugs	2,602,242,165	
Total hospital and medical expenses	$ 15,553,164,182	
Less net reinsurance recoveries	135,127	
Claims adjustment expenses	813,091,776	
General administrative expenses	1,258,283,991	
Increase in reserves for life and accident and health contracts	66,098,325	
Total underwriting deductions		$ 17,690,503,147
Net underwriting loss		$ (258,094,154)
Net investment income earned		54,889,780
Net realized capital gains less capital gains tax		7,510,585
Net loss from agents' or premium balances charged-off		(1,133,660)
Aggregate write-ins for other expenses		(7,069,283)
Net loss before federal income taxes		$ (203,896,732)
Federal and foreign income taxes incurred		(11,156,735)
Net loss		$ (192,739,997)

Changes in Surplus

Surplus, per report on examination, as of December 31, 2008			$ 235,813,956
PerfectHealth's capital and surplus as of December 31, 2008			3,641,556
*Restated surplus as of December 31, 2008			239,455,512
	Gains in Surplus	Losses in Surplus	
Net loss		192,739,997	
Change in net unrealized capital gains	93,739,241		
Change in net deferred income tax		1,093,478	
Change in nonadmitted assets	39,676,152		
Change in surplus notes	165,311,381		
Cumulative effect of changes in accounting principles		36,074	
Surplus adjustments	55,662,431		
Aggregate write-ins losses in surplus		123,658,369	
Net change in surplus			36,861,287
Surplus, per report on examination as of December 31, 2013			$ 276,316,799

*Pursuant to the requirements of SSAP No. 3, GHI restated its 2008 total capital and surplus to include Perfect Health's capital and surplus as a result of its merger with Perfect Health on December 31, 2009.

5. STATUTORY RESERVE

Section 4310(d)(2) of the New York Insurance Law ("NYIL") states in part:

> "Every such corporation shall maintain a reserve to be designated as the statutory reserve fund, which shall from time to time during each calendar year be increased in an amount equal to at least one per centum of the net premium income of such corporation during such whole calendar year, provided however, that…
>
> (2) the statutory reserve fund at the end of any calendar year shall not exceed twelve and one-half per centum of the net premium income of such calendar year…"

Pursuant to Section 4310(d)(2) of the New York Insurance Law, GHI is required to maintain a statutory reserve fund that meets the requirements set forth above. For the entire examination period, GHI's reported statutory reserve was below the minimum reserve requirement. As of December 31, 2013, GHI reported surplus of $276,316,799, which is $157,912,245 below the required statutory reserve of $434,229,044.

It is recommended that GHI maintain the minimum statutory reserve required by Section 4310(d)(2) of the NYIL.

On April 8, 2014, the Department directed GHI to submit a viable “Plan of Correction” detailing the actions GHI would take to fully restore its statutory reserve fund to the required level no later than December 31, 2016.

Subsequent to the examination period, GHI’s statutory reserve fund requirement decreased from $227.0 million to $113.6 million from 2014 to 2015 due to the drastic decrease in its written premiums which, as explained by GHI in its 2015 Management Discussion and Analysis, was related to a change in the funding arrangement of a significant group effective July 1, 2014. As of December 31, 2015, GHI reported surplus of $213,816,598 which is $100,244,194 above the required statutory reserve of $113,572,404.

6. CLAIMS UNPAID

The examination liability of $ 400,065,480 for the above captioned account is the same as the amount reported by GHI in its December 31, 2013 filed annual statement.

The examination analysis of the claims unpaid reserve was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Plan’s internal records and its filed annual statements as verified during the examination.

The examination reserve was based upon actual payments made through a point in time, plus an estimate for claims remaining unpaid at that date. Such estimate was calculated based on actuarial principles, which utilized the Plan's past experience in projecting the ultimate cost of claims incurred on or prior to December 31, 2013.

7. STATUTORY EXPENSE LIMITATION

Section 4309 of the NYIL states in part:

> "(a) No corporation subject to the provisions of this article shall, during any one year, disburse more than the percentages hereafter prescribed of the aggregate amount of the premiums received during such year as expenditures for expenses, which, for the purposes of this article, shall include all expenses paid or incurred by the corporation which do not constitute benefit payments made to or on behalf of persons covered under contracts issued by such corporations…
>
> (2) All other corporations: twenty per centum reduced by one per centum for each five million dollars or fraction thereof above one million dollars of premiums received to fifteen per centum except that for any corporation which derives more than fifty per centum of its premiums received from the sale of contracts which provide hospital service benefits: seventeen and one-half per centum reduced by one per centum for each five million dollars or fraction thereof above one million dollars of premiums received to twelve and one-half per centum…
>
> (b) If any such corporation shall in any calendar year make or incur expenses as hereinabove defined in excess of its expense limit the superintendent may, upon written application of such corporation and a showing that such corporation has taken steps in accordance with a plan submitted by the corporation and approved by the superintendent which will enable it to comply with the provisions of this section during the next calendar year, suspend the expense limit for such corporation for the calendar year in which the excess was incurred but the superintendent shall not suspend the expense limit for any such corporation for more than two calendar years in succession."

It is noted that for 2014 and 2015, GHI's administrative expense ratio was 16.7% and 31.8%, respectively, which exceeded the 12.5% limitation set forth in Section 4309 of the NYIL.

It is recommended that GHI adhere to the administrative expense limitation set forth in Section 4309 of the NYIL.

Pursuant to Section 4309(b), GHI filed an application on June 1, 2015 with this Department to suspend the expense limitation for this year. The Department granted GHI temporary forbearance from the NYIL Section 4309 expense limitation on September 21, 2016. The Department reserves its right to apply to the NYIL Section 4309 expense limitation at any time.

8. SURPLUS NOTES

On December 31, 2009, GHI funded its merger with PerfectHealth in the form of a $311,381 surplus note due to HIP Holdings, Inc., at zero interest, pursuant to Section 1307 of the New York Insurance Law.

GHI received from HIPNY Section 1307 statutory surplus loans of $40 million, $10 million, $80 million and $35 million on March 29, 2012, June 30, 2011, December 29, 2010 and March 31, 2010, respectively, with interest accruing at 2% per annum. As of December 31, 2013, the accrued interest payable to HIPNY on these Section 1307 loans was approximately $ 9.3 million, this amount was disclosed in the Notes to the Financial Statement of GHI's 2013 annual financial statement filing.

Section 1307(b) of the New York Insurance Law states in part:

> "Such borrowing …shall be repaid only out of free and divisible surplus of such insurer with the approval of the superintendent whenever, in his judgment, the financial condition of such insurer warrants…"

Section 1307(c) of the New York Insurance Laws states:

> "Any sum so advanced or borrowed shall not be part of the legal liabilities of such insurer and shall not be a basis of any set-off but until repaid all statements published by such insurer or filed with the superintendent shall show, as a footnote, the amount then remaining unpaid."

As of December 31, 2013, GHI reported $165,311,381 in Section 1307 statutory surplus notes.

9. COMPLIANCE WITH PRIOR REPORTS ON EXAMINATION

The prior financial report on examination as of December 31, 2008, contained the following eleven (11) comments and recommendations (page numbers refer to the prior report):

ITEM NO.		PAGE NO.
	Management and Controls	
1.	It is recommended that the audit committee continue to review and approve the salary of the head of internal audit. *The Plan has not complied with this recommendation. A similar recommendation is included in this report*	9
2.	Since EmblemHealth has initiated the process to become a for-profit, publicly held company, it is recommended that a formalized risk management function be established to oversee and address key enterprise risks, risk measurement approaches, remediation plans and their implementation consistent with such applicable standards. *The Plan has not fully complied with this recommendation. At the time of examination, EmblemHealth's ERM function was not fully developed.*	10
3.	It is further recommended that such function be established in a manner that clearly sets forth roles and responsibilities in accordance with industry frameworks and standards. *The Plan has not fully complied with this recommendation. At the time of examination, EmblemHealth's ERM function was not fully developed.*	10
	Board of Directors	
4.	It is recommended that GHI continue to take corrective action and evaluate whether board and committee members who are unable or unwilling to attend meetings consistently should resign or be replaced. Furthermore, in selecting prospective members, a key	13

10. SUMMARY OF COMMENTS AND RECOMMENDATIONS

ITEM			PAGE NO.
A.		Management and Controls	
	i.	It is recommended as a best practice that the Audit Committees of the Plan and EmblemHealth, Inc., adhere to the provisions of Standard 1110 of the IIA's *International Standards for the Professional Practice of Internal Auditing* by formally evaluating the performance of their Chief Audit Executive, and also by approving the annual compensation and salary adjustment of the position.	8
	ii.	It is recommended that the Audit Committee of GHI evaluate the performance, and review and approve the compensation of said Chief Audit Executive jointly with the Audit Committees of EmblemHealth and HIPNY.	9
	iii.	It is recommended that EmblemHealth/HIPNY/GHI ensure the objectivity and independence of their Internal Audit Department by not having its Chief Audit Executive report to the Compliance Officer directly, or indirectly, or vice versa.	10
	iv.	It is recommended that the Plan take corrective action by developing a policy to evaluate whether Board members who are unable or unwilling to attend Board meetings consistently should resign or be replaced. Furthermore, in selecting prospective Board members, a key criterion should be their willingness and commitment to attend meetings and participate in the Board's responsibility to oversee the operations of the Plan.	12
	v.	It is recommended that GHI update its by-laws to reflect the change in its committee structure and governance.	14
B.		Enterprise Risk Management	
		It is recommended that EmblemHealth adopt and implement its ERM function in accordance with the provisions of Insurance Circular Letter No. 14 (2011), Section 1503(b) of the New York Insurance Law, and Part 82.2(a) of Insurance Regulation No. 203.	16

ITEM			PAGE NO.
C.		Insurance Regulation No. 118 - Model Audit Rule	
	i.	It is recommended that GHI comply with the requirements of Part 89.5(e)(2) of Insurance Regulation No. 118 by attaching the required statement to its filed audited financial statements.	21
	ii.	It is also recommended that GHI's Audit Committee comply with the requirements of Part 89.5(h) of Insurance Regulation No. 118 by pre-approving all non-audit services performed by its CPA and documenting such action in its meeting minutes.	21
	iii.	It is recommended that GHI comply with the requirements of Part 89.12(e) of Insurance Regulation No. 118 by notifying the Department within 30 days of any change in membership of its Audit Committee. Such notice shall include a description of the reason for the change.	22
D.		Statutory Reserve	
		It is recommended that GHI maintain the minimum statutory reserve required by Section 4310(d)(2) of the NYIL.	27
E.		Statutory Expense Limitation	
		It is recommended that GHI adhere to the administrative expense limitation set forth in Section 4309 of the NYIL.	28

Respectfully submitted,

____

Jo Lo Hsia,
Principal Insurance Examiner

STATE OF NEW YORK)
)SS.
)
COUNTY OF NEW YORK)

Jo Lo Hsia, being duly sworn deposes and says that the foregoing report submitted by her is true to the best of her knowledge and belief.

____

Jo Lo Hsia

Subscribed and sworn to before me
this _____ of ______________, 2018

APPOINTMENT NO. **31208**

NEW YORK STATE

DEPARTMENT OF FINANCIAL SERVICES

I, ***<u>BENJAMIN M. LAWSKY</u>****, Superintendent of Financial Services of the State of New York, pursuant to the provisions of the Financial Services Law and the Insurance Law, do hereby appoint:*

JoLo Hsia

as a proper person to examine the affairs of

Group Health Incorporated

and to make a report to me in writing of the condition of said

Plan

with such other information as she shall deem requisite.

In Witness Whereof, I have hereunto subscribed my name
and affixed the official Seal of the Department
at the City of New York

this 6th day of November, 2014

BENJAMIN M. LAWSKY
Superintendent of Financial Services

By:

Lisette Johnson
Bureau Chief
Health Bureau