

REPORT ON EXAMINATION

OF

HIGHMARK BCBSD INC.

AS OF

DECEMBER 31, 2012

Karen Weldin Stewart, CIR-ML
Commissioner



Delaware Department of Insurance

I, Karen Weldin Stewart, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT OF EXAMINATION, made as of December 31, 2012 of the

HIGHMARK BCBSD INC.

is a true and correct copy of the document filed with this Department.

Attest By: Brandi Biddle

Date: March 24, 2014



In Witness Whereof, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover, this 24th day of March, 2014.

A handwritten signature in black ink, appearing to read "Karen Weldin Stewart".

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Karen Weldin Stewart, CIR-ML
Commissioner



Delaware Department of Insurance

REPORT OF EXAMINATION
OF THE
HIGHMARK BCBSD INC.
AS OF
DECEMBER 31, 2012

The above-captioned report was completed by examiners of the Delaware Department of Insurance.

Consideration has been duly given to the comments, conclusions and recommendations of the examiners regarding the status of the company as reflected in the report.

This report is hereby accepted, adopted and filed as an official record of this Department.

A handwritten signature in black ink, appearing to read "Karen Weldin Stewart".

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Dated this 24th day of March, 2014

TABLE OF CONTENTS

SALUTATION	1
SCOPE OF EXAMINATION.....	1
SUMMARY OF SIGNIFICANT FINDINGS	3
SUBSEQUENT EVENTS	3
COMPANY HISTORY	3
MANAGEMENT AND CONTROL	4
INSURANCE HOLDING COMPANY SYSTEM.....	6
INTERCOMPANY AGREEMENTS	7
TERRITORY AND PLAN OF OPERATION	9
LOSS EXPERIENCE	11
ACCOUNTS AND RECORDS.....	12
FINANCIAL STATEMENTS	13
Analysis of Assets.....	14
Statement of Liabilities, Surplus and Other Funds	15
Summary of Operations - Statement of Income.....	16
Reconciliation of Surplus from Prior Examination	17
SCHEDULE OF EXAMINATION ADJUSTMENTS.....	17
NOTES TO FINANCIAL STATEMENTS.....	17
Note 1 - Bonds	17
Note 2 – Common Stock.....	18
Note 3 – Claims Unpaid.....	19
Note 3 – Unpaid Claims Adjustment Expense	19
Note 3 – Aggregate Health Policy Reserves.....	19
COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS	20
SUMMARY OF RECOMMENDATIONS	21
CONCLUSION.....	21

SALUTATION

January 29, 2014

Honorable Karen Weldin Stewart, CIR-ML
Delaware Insurance Commissioner
Delaware Department of Insurance
Rodney Building
841 Silver Lake Blvd.
Dover, Delaware 19904

Dear Commissioner;

In compliance with instructions and pursuant to statutory provisions contained in Certificate of Authority No. 13.012, dated November 14, 2012, an examination has been made of the affairs, financial condition and management of

HIGHMARK BCBSD INC.

hereinafter referred to as the "Company" and incorporated under the laws of the State of Delaware as a non-stock corporation. The examination was conducted at the statutory home offices of the Company, located at 800 Delaware Avenue, Wilmington, Delaware, 19801. The report of examination thereon is respectfully submitted.

SCOPE OF EXAMINATION

The last examination was completed as of December 31, 2008. This examination covered the period of January 1, 2009, through December 31, 2012, and encompasses a general review of transactions during the period, the Company's business policies and practices, as well as management and relevant corporate matters, with a determination of the financial condition of the Company at December 31, 2012. Transactions subsequent to the examination date were reviewed where deemed necessary.

We conducted our examination in accordance with the *National Association of Insurance Commissioners (NAIC) Financial Condition Examiners Handbook* (Handbook) and generally accepted statutory insurance examination standards consistent with the Insurance Laws and Regulations of the State of Delaware. The NAIC Handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. The examination also included assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic State regulations.

All accounts and activities of the Company were considered in accordance with the risk focused examination process. The examination report addresses regulatory issues reviewed during the examination process.

During the course of this examination, consideration was given to work performed by the Company's external accounting firms, Ernst & Young (E&Y) for 2011 and prior, and PricewaterhouseCoopers (PwC) for 2012. Certain auditor work papers have been incorporated into the work papers of the examiners and have been utilized in determining the scope, areas of emphasis in conducting the examination and in the area of tests of controls, risk mitigation and substantive testing.

In addition to items noted in this report, the topics below were reviewed without material exception and are included in the work papers of this examination:

- Corporate Records
- Fidelity Bonds and Other Insurance
- Pensions, Stock Ownership and Insurance Plans
- Statutory Deposits
- Reinsurance

SUMMARY OF SIGNIFICANT FINDINGS

There were no significant findings or adjustments noted.

SUBSEQUENT EVENTS

On January 1, 2013, the Company adopted *Statements of Statutory Accounting Principles* (SSAP) No. 92 – “Accounting for Postretirement Benefits Other than Pensions” and SSAP No. 102 – “Accounting for Pensions”. Consistent with Generally Accepted Accounting Principles (GAAP), the new guidance requires non-vested employees be included in qualified benefit plan liabilities with the impact recorded as a prior service cost. The Company estimates the before-tax impact to be a reduction to surplus of approximately \$29,200,000 and has elected to record the full impact on January 1, 2013.

On May 17, 2013, pursuant to the affiliation plan, the migration of Company’s systems to Highmark Inc.’s (Highmark) systems was completed.

COMPANY HISTORY

The Company was originally incorporated by the filing of a Certificate of Incorporation with the Secretary of State on August 15, 1935 as a non-profit non-stock corporation and is operated as a health service corporation in the State of Delaware. The Company, as a licensee of the Blue Cross and Blue Shield Association (BCBSA), underwrites various indemnity and managed care health insurance products as well as Medicare supplemental, dental and vision products. The Company also provides Administrative Services Contracts (ASC) to self-funded plans.

On December 30, 2011, the Delaware Commissioner approved an affiliation between Highmark Inc. and the Company (Affiliation Approval) imposing 49 conditions on the affiliation that, among other things, were intended to preserve the Company's surplus and reserves and make it possible for the Company to disaffiliate if necessary. Effective January 1, 2012, Highmark became the sole member of the Company, which thereupon changed its name to Highmark BCBSD Inc. As the sole member of the Company, Highmark has the authority to elect the Company's Board of Directors. The Company is a separate legal entity and is not liable for Highmark's obligations. In accordance with its articles of incorporation, in the event of dissolution of the Company, the Directors shall cause any remaining assets of the Company to be distributed to a foundation created pursuant to Delaware law or to a federally tax-exempt organization.

MANAGEMENT AND CONTROL

Pursuant to the General Corporation Law of the State of Delaware, as implemented by the Company's Certificate of Incorporation and bylaws, all corporate powers and its business property and affairs are managed by, or under the direction of, its Board of Directors (Board). The Board shall consist of nine members, consisting of four Class A Directors, four Class B Directors and the President of the Company. The initial Class A Directors will serve, respectively, until the sole member's (Highmark's) third, fourth, fifth and sixth annual meetings following the affiliation. Subsequent Class A Directors shall hold office for a term of three years. Class B Directors shall hold office for a term of one year. The Board of the Company is elected by the sole member.

The management and control of the Company is vested in the Board. The persons elected and serving as Directors of the Company at December 31, 2012 were:

Directors	Primary Business Affiliation
Timothy J. Constantine Wilmington, DE	President, Highmark BCBSD Inc. Class A Director
Thomas E. Archie Wilmington, DE	Retired, Business Manager for Laborers International Union of North America, Local 199 Class B Director
Ben Corballis, M.D. Wilmington, DE	Chairman Emeritus of the Department of Emergency Medicine at Christiana Care Class A Director
Nanette P. DeTurk Pittsburgh, PA	EVP, Chief Administrative and Financial Officer Highmark Inc. Class B Director
Deborah L. Rice-Johnson Pittsburgh, PA	Division President of Health Service and Executive VP, Highmark Inc. Class B Director
David P. Roselle, Ph.D. Wilmington, DE	Director, Winterthur Museum, Garden and Library Class A Director
Frances M. West Wilmington, DE	Retired, State of Delaware Employee, Past President of the BBB of Delaware. Class A Director
William H. Willis, Jr. Wilmington, DE	President of Willis Chevrolet, Inc. , Willis Ford, Inc. and Willis Automotive Class A Director
William Winkenwerder, Jr., M.D., MBA Pittsburgh, PA	President & CEO, Highmark Inc. Class B Director

The Officers of the Company are elected by the Board. Those persons serving as of December 31, 2012 were:

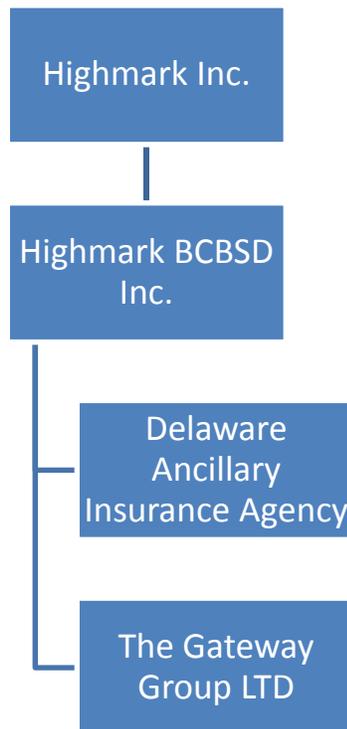
<u>Officers</u>	<u>Title</u>
Timothy J. Constantine	President
Todd P. Graham	Corporate Controller and Treasurer
William E. Kirk, III	Corporate Secretary

The minutes of the meetings of the Board and Committees, which were held during the period of examination, were read and noted. Attendance at meetings, election of directors and officers and approval of investment transactions were also noted.

INSURANCE HOLDING COMPANY SYSTEM

The Company is a member of an insurance holding company system as defined under 18 Del. C. §5001 (4) “Insurance Holding Company System”. Although there is no “ownership” of a non-stock corporation, the Company is a direct subsidiary of Highmark Inc. (the “Parent”).

The following is an abbreviated organization chart as of the examination date;



At December 31, 2012, Highmark Inc. reported the following:

Assets	\$ 7,286,271,681
Shareholders' Equity	\$ 4,138,085,333
Total Revenues for 2012	\$ 2,063,035,834
Net Income	\$ 163,167,106

The examiners have reviewed the Company's most recently filed Form B- Insurance Holding Company Registration Statement. Based on that review, it appears that the Company has disclosed all intercompany arrangements and in turn has filed the applicable information/agreements with the Delaware Insurance Department.

The Company's total premium and annuity considerations for the year ended December 31, 2012 were as follows:

<u>Direct</u>	
Accident and Health	\$420,047,145
Federal Employee Program	<u>116,553,748</u>
Total Direct Written Premium	<u>\$536,600,893</u>

Note: The Company does not engage in any reinsurance agreements.

INTERCOMPANY AGREEMENTS

Administrative Services Agreement

The Company entered into an Administrative Service Agreement with Highmark Inc. effective January 1, 2012 in connection with the Affiliation Approval. The agreement establishes a plan of systems conversion and integration priorities, performance standards, budgets and timelines. The scope of services and plan of systems integration includes, but is not limited to, services in the following areas:

- Executive management;
- Finance, financial administration, accounting and investment management;
- Payroll, employee benefits management and human resource/employee relations;
- Corporate training;
- Procurement;
- Corporate communications;
- Audit, compliance and integrity;
- Computer and data processing;
- Marketing and sales;
- Actuarial and underwriting;
- Pharmacy/prescription drugs;
- Customer service;

- Enrollment and membership;
- Claims adjudication and administration;
- Spending/reimbursement account administration;
- Broker and agent administration;
- Credentialing;
- Utilization management
- Quality assurance;
- Grievances and complaints;
- Member agreements and literature;
- Provider relations; and
- Such other services as the parties may agree from time to time.

The Company and Highmark are to implement the plan of systems conversion referred to in the Affiliation Agreement between the companies. Costs charged or allocated to the Company by Highmark for integration services are to be capped at \$42 million. Costs in excess of \$42 million are to be paid or absorbed by Highmark.

The Company is to compensate Highmark's provision of services in an amount equal to the Company's fair and reasonable allocable share of the total actual cost without provision for profit to Highmark. Such costs shall include, without limitation, employee salaries, employee benefits and other direct and indirect administrative costs, including reasonable charges for corporate overhead. The Company's allocable share of the cost of the Services shall be determined in accordance with Highmark's established cost accounting practices as in effect from time to time. The Company also shall reimburse Highmark for any and all direct third party costs incurred by Highmark for the benefit of the Company.

Highmark is to invoice the Company on a regular basis for amounts due, and the Company shall pay all amounts due to Highmark upon receipt of the invoice. The Company shall pay a service charge of 1% per month on the amount of any invoice remaining unpaid more than 30 days following the due date. The agreement was initially in effect for one year and

Highmark BCBSD Inc.

renewable automatically for successive terms of one year each subject to prior written notice of termination.

Line of Credit Agreement

A Line of Credit (LOC) Agreement was also filed in connection with the Affiliation Approval wherein Highmark provided a LOC in favor of the Company up to an outstanding principal amount of \$45 million. Use of LOC proceeds by the Company are solely for the payment of costs associated with the systems conversion and integration contemplated by the Administrative Services Agreement. This LOC has not been utilized during the Examination period.

Letter of Credit

In compliance with Condition 47 of the Affiliation Approval, Highmark obtained an Irrevocable Letter of Credit from PNC Bank in favor of the Company for an aggregate total sum of \$17.5 million which shall be made available if disaffiliation occurs as a result of a triggering event within the first 3 years after the closing of the affiliation. This Letter of Credit has not been utilized during the Examination period.

TERRITORY AND PLAN OF OPERATION

The Company is licensed to solicit business as a Health Service Corporation in the State of Delaware only. The Company writes primarily Comprehensive (medical and hospital) business. A significant portion of the Company's business (approximately two-thirds) is "non-underwritten", meaning there is no insurance risk to the Company. For large, self-insured accounts, the Company processes claim payments and receives reimbursement for claims and expenses from the account.

The Company offers a comprehensive portfolio of health insurance products and administrative services to individuals and accounts throughout the State of Delaware. The administrative services provided include management of benefits, adjudication and payment of claims, response to inquiries from covered individuals and health care providers, and providing Plan Sponsors with information enabling them to manage their health benefit programs. The Company's core health insurance products are categorized into five major segments:

- Indemnity
- Preferred Provider Organization
- Point of Service
- Health Maintenance Organization
- Exclusive Provider Organization

The total for underwritten business and Federal Employee Program (FEP) business is broken down by the following lines of business:

<u>Line of Business</u>	<u>Direct Premiums</u>	
	<u>Written</u>	<u>Percent</u>
Comprehensive (Medical and Hospital)	\$ 401,879,989	74.9%
Medicare Supplement	14,789,766	2.8%
Dental Only	2,512,432	0.5%
Vision Only	90,554	0.02%
FEP	116,553,748	21.7%
Other Health	774,404	0.1%
Total	<u>\$ 536,600,893</u>	<u>100.0%</u>

Note: The FEP Business is actually non-underwritten business; however, the NAIC Annual Statement has certain reporting requirements with regards to FEP business on certain schedules within the Annual Statement. As a result, the Company must include the FEP business on the Statutory Balance Sheet so that the Balance Sheet will tie to the supporting schedules of the Annual Statement.

GROWTH OF COMPANY

<u>Year</u>	<u>Admitted Assets</u>	<u>Capital & Surplus</u>	<u>Net Premium Income</u>	<u>Net Underwriting Gain/(Losses)</u>	<u>Net Income</u>
2008	\$ 245,310,403	\$ 120,807,157	\$ 477,182,765	\$ (20,074,350)	\$ (16,749,008)
2009	\$ 261,988,887	\$ 139,688,660	\$ 482,122,236	\$ (7,553,852)	\$ 827,007
2010	\$ 306,717,984	\$ 171,131,264	\$ 498,775,482	\$ 7,606,964	\$ 15,235,044
2011	\$ 305,844,943	\$ 158,584,262	\$ 516,520,209	\$ (6,240,130)	\$ 4,745,237
2012	\$ 312,540,261	\$ 168,660,304	\$ 536,600,893	\$ (6,618,787)	\$ (11,051,116)

For the period January 1, 2009 through December 31, 2012, the Company's financial results were as follows:

- 27.41 % increase in admitted assets
- 39.61 % increase in capital and surplus
- 12.45% increase in net premium income
- 67.03% improvement in underwriting
- 34.02% improvement in net income

Admitted Assets increase of \$67.2 M or 27.41%, was primarily due to the recovery of market values of stock portfolios, reinvested dividends, increases in receivables and favorable operating results. Capital and Surplus increase of \$47.9 M or 39.61% was primarily due to net unrealized gains and favorable operating results. The Net Premium Income increase of \$59.4M or 12.45% was primarily due to increases in FEP business. The improvements in Underwriting of \$13.5 M or 67.03% and Net Income of \$5.7 M or 34.02%, were primarily due to the increase in premium and a decrease in the actuarial estimate of claims incurred but not yet reported, offset by increased operating expenses and affiliation costs.

LOSS EXPERIENCE

Reserves for incurred claims and claims adjustment expenses attributed to insured events of prior years decreased \$2.6 million and \$84K respectively during 2012 and by \$3.3 million and \$97K respectively during 2011 as a result of re-estimation of unpaid claims and claim adjustment expense.

ACCOUNTS AND RECORDS

The statutory-basis financial statements of the Company have been audited annually by external accounting firms; Ernst & Young for 2011 and prior, and PricewaterhouseCoopers for 2012. The Company's external firms reviewed the internal control structure in order to establish the necessary audit procedures required to express an opinion on the financial statements as of each year end. No significant or qualifying deficiencies were found to exist in the design or operation of the internal control structure.

The accounts and records review included an assessment of the Company's risk management process in identifying and controlling risks in the key operational areas of the Company. In making the assessment in each key area, processes were reviewed, risks were identified, operational and organizational controls were identified and tested and the Company's methodology for assessing the effectiveness of the established mitigation factors were evaluated.

The consulting firm of INS Services, Inc. performed a review of the Company's global controls over its information technology (IT) environment. It was determined that global controls surrounding the IT environment were sufficient.

During the examination the following was observed:

The Company is carrying unclaimed checks (from 1999 to 2007) as reconciling items on several of its bank accounts. These items had not been remitted to the respective State(s). 12 Del. C. §1197 "Other Property Escheated" requires that all unclaimed Delaware property greater than 5 years old shall be remitted to the State. Therefore, all unclaimed property greater than 5 years old shall be remitted to the State of Delaware, unless the property is subject to being remitted to another State.

As noted in the previous examination management comments, it is recommended the Company utilize procedures which comply with 12 Del. C. §1197 “Other Property Escheated”.

FINANCIAL STATEMENTS

The following pages contain a statement of assets, liabilities, surplus and other funds as of December 31, 2012, as determined by this examination, along with supporting exhibits as detailed below:

- Analysis of Assets
- Statement of Liabilities, Surplus and Other Funds
- Underwriting and Investment Exhibit
- Statement of Income
- Reconciliation of Surplus Since last Examination
- Schedule of Examination Adjustments

Analysis of Assets
As of December 31, 2012

	<u>Assets</u>	Nonadmitted <u>Assets</u>	Net Admitted <u>Assets</u>	<u>Note</u>
Bonds	\$ 194,627,571		\$ 194,627,571	1
Common stocks	54,824,207		54,824,207	2
Mortgage loans on real estate	196,989		196,989	
Cash and short-term investments	5,041,441		5,041,441	
Receivables for securities	53,381		53,381	
Investment income due and accrued	1,540,367		1,540,367	
Uncollectible premiums and agents' balances in course of collection	16,601,412		16,601,412	
Amounts receivable relating to uninsured plans	20,851,190		20,851,190	
Current federal and foreign income tax recoverable and interest thereon	870,978		870,978	
Net deferred tax asset	13,149,188	\$ 4,463,985	8,685,203	
Electronic data processing equipment and software	12,677,967	8,415,701	4,262,266	
Furniture and equipment	7,536,694	7,536,694	-	
Receivables from parent, subsidiaries & affiliates	2,654		2,654	
Health care and other amounts receivable	7,527,827	2,545,225	4,982,602	
Aggregate write-ins:	28,590,558	28,590,558	-	
Total Assets	<u>\$ 364,092,424</u>	<u>\$51,552,163</u>	<u>\$ 312,540,261</u>	

Statement of Liabilities, Surplus and Other Funds
As of December 31, 2012

<u>Liabilities, Surplus and Other Funds</u>		<u>Note</u>
Claims unpaid	\$ 40,380,155	3
Unpaid claims adjustment expenses	2,541,000	3
Aggregate health policy reserves	5,080,606	3
Premiums received in advance	5,710,947	
General expenses due or accrued	69,380,831	
Amounts withheld or retained for the account of others	844,173	
Amounts due to parent, subsidiaries and affiliates	7,897,159	
Liability for amounts held under uninsured plans	9,028,840	
Aggregate write-ins for liabilities	3,016,246	
Total Liabilities	<u>\$ 143,879,957</u>	
Unassigned funds (surplus)	<u>\$ 168,660,304</u>	
Surplus as regards policyholders	<u>\$ 168,660,304</u>	
Total Liabilities, Capital and Surplus	<u><u>\$ 312,540,261</u></u>	

Summary of Operations - Statement of Income
As of December 31, 2012

Premiums and annuity considerations	\$ 536,600,893
Net investment income	6,054,615
Net investment gains or (losses)	5,488,448
Change in unearned premium reserves	(4,410,606)
Changes and fees for deposit type contracts	-
Totals	<u>543,733,350</u>
Hospital/medical benefits	325,188,635
Other professional services	37,345,062
Emergency room and out-of-area	10,734,894
Prescription drugs	84,283,529
Totals	<u>457,552,120</u>
Claims adjustment expenses	21,412,288
General administrative expenses	63,044,666
Increase in reserves for life and accident and health contracts	(3,200,000)
Totals	<u>538,809,074</u>
Net gains from operations before dividends to policyholders and Federal Income Taxes	4,924,276
Federal and foreign income taxes	<u>(852,184)</u>
Net gains from operations after dividends to policyholders and Federal Income Taxes	5,776,460
Aggregate write-ins for other income or expenses	<u>(16,827,576)</u>
Net Income	<u><u>\$ (11,051,116)</u></u>

Reconciliation of Surplus from Prior Examination

Surplus as regards to policyholders, December 31, 2008	\$ 120,807,157
Net Income	9,756,172
Change in net unrealized capital gains/(losses)	28,774,280
Change in unrealized foreign exchange capital gains	-
Change in net deferred income taxes	(1,769,134)
Change in non-admitted assets and related items	16,661,071
Change in liability for reinsurance in unauthorized companies	-
Change in reserve on account change in valuation basis	0
Change in asset valuation reserve	-
Cumulative effect of changes in accounting principles	3,412,316
Dividends to stockholders	0
Aggregate write-ins	(8,981,558)
Net change in surplus as regards to policyholders, December	\$ 47,853,147
Surplus as regards to policyholders, December 31, 2012	\$ 168,660,304

SCHEDULE OF EXAMINATION ADJUSTMENTS

There were no financial examination adjustments.

NOTES TO FINANCIAL STATEMENTS

Note 1 - Bonds

\$194,627,571

Investments in bonds are reported at values (amortized cost) adopted and approved by the Securities Valuation Office (SVO) of the NAIC. Bonds owned by the Company are as follows:

<u>Type</u>	<u>Statement Value</u>
U.S government	\$ 45,855,215
All other governments	1,238,212
States, territory and possessions	4,378,042
Obligations of states and political sub div of the U.S	563,259
Special revenue	60,071,508
Mortgage backed securities	
Residential	1,107,215
Commercial	3,649,577
Asset backed securities	12,652,498
Other loan backed and structural securities	2,726,816
Industrial miscellaneous securities	62,385,229
Total	<u>\$ 194,627,571</u>

Of the Company's bond holdings, which comprised 76.4% of the Company's total invested assets and 62.3% of total admitted assets at December 31, 2012, 100% were categorized as Class 1 or 2 with respect to NAIC credit quality standards and with maturity dates consistent with the Company's expected reserve payout.

The Company did not hold any loan backed securities for which the yield has become negative at December 31, 2012. The Company wrote down to market value \$87,064 of impaired securities during 2012.

Note 2 – Common Stock

\$54,824,207

As of December 31, 2012, the Company held securities as follows:

<u>Type</u>	<u>Statement Value</u>
Industrial and miscellaneous (unaffiliated)	\$ 1,587,505
Mutual Funds	53,236,702
Total	<u>\$ 54,824,207</u>

<u>Note 3 – Claims Unpaid</u>	<u>\$ 40,380,155</u>
<u>Note 3 – Unpaid Claims Adjustment Expense</u>	<u>2,541,000</u>
<u>Note 3 – Aggregate Health Policy Reserves</u>	<u>5,080,606</u>

The Delaware Department of Insurance retained the services of INS Consultants, Inc. (INS), to conduct an independent review of the Company's Unpaid claims, Unpaid Claims adjustment expense and Aggregate Health Policy Reserves as of December 31, 2012. The Consulting Actuary's analysis was performed using a risk-focused approach according to the guidelines contained in the NAIC Financial Condition Examiner's Handbook. The conclusions set forth in the Consulting Actuary's report are based on information provided by the Company, including the 2012 Annual Statement. Reserves as of December 31, 2012 were \$48,001,761. Reserves were held primarily for medical and hospital and FEP claims. The Five-year Historical Data Exhibit of the Annual Statement indicates that no new type of business was entered into and that there were insignificant changes in reserves during the examination period. There were no significant trends or unanticipated events noted in 2012.

The Company's reserves were reviewed through data validity and inclusion testing of reported claims. INS monitored the development of the Company's December 31, 2008 reserve through December 31, 2012. In summary, INS concluded the Company's reserves at December 31, 2012 were fairly stated.

<u>Claims Unpaid</u>	<u>\$40,380,155</u>
-----------------------------	----------------------------

The liability was calculated separately for each line of business using a combination of completion factors, claim trends, claim payment triangles and membership. INS reviewed the methodology and it appears reasonable and consistent with standard actuarial liability calculation methodologies. The Company also includes an 8.0% margin for adverse deviation of claims for

all lines of business, except for FEP. Based on prior experience and analysis, INS believes this a reasonable margin for adverse deviation.

The Company also provided unpaid claims data by line of business as of May 31, 2013. Using this data, INS recalculated the claim liability as of December 31, 2012. INS concluded that the Company's December 31, 2012 liability for claims unpaid appears sufficient.

Unpaid Claims Adjustment Expenses **\$2,541,000**

The amount is established to cover expenses associated with the claims unpaid liability for the Company's insured business. INS reviewed work papers and supporting documentation provided by the Company for the unpaid claims adjustment expenses. The unpaid claims adjustment expense of \$2,541,000 is 6.3% of the unpaid claims liability of \$40.38 million. The 6.3% factor falls within the accepted industry range of 2%-10%. INS also performed a trend analysis which indicated a reasonable trend over the examination period. Consequently, INS concluded that the unpaid claims adjustment expenses were fairly stated.

Aggregate Health Policy Reserves **\$5,080,606**

This reserve is primarily for unearned premiums relating to FEP. INS concluded that the aggregate health policy reserves were fairly stated.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The examination reviewed the December 31, 2008 Report on Examination along with the Company's compliance with the prior examination recommendations, comments and concerns. Based on that review, the Company has complied with all applicable prior Report on Examination recommendations, comments and concerns.

1. It was recommended that the Company provide information in a timely manner.
2. It was recommended that the Company conduct an annual on-site audit of its third party administrators in accordance with Regulation 1406 of the Delaware Insurance Code.

3. It was recommended that the Company comply with the NAIC Annual Statement instructions when categorizing bonds.

SUMMARY OF RECOMMENDATIONS

As noted in the previous examination management comments, it is recommended the Company utilize procedures which comply with 12 Del. C. §1197 “Other Escheated Property”.

CONCLUSION

The following schedule shows the results of this examination and the results of the prior examination with changes between the examination periods:

<u>Description</u>	<u>December 31, 2008</u>	<u>December 31, 2012</u>	<u>Increase (Decrease)</u>
Assets	\$ 245,310,403	\$ 312,540,261	\$ 67,229,858
Liabilities	\$ 124,503,246	\$ 143,879,957	\$ 19,376,711
Common Capital Stock	-	-	-
Gross Paid In and Contributed Surplus	-	-	-
Unassigned Funds (Surplus)	120,807,157	168,660,304	47,853,147
Total Surplus	<u>\$ 120,807,157</u>	<u>\$ 168,660,304</u>	<u>\$ 47,853,147</u>
Totals	<u>\$ 245,310,403</u>	<u>\$ 312,540,261</u>	<u>\$ 67,229,858</u>

Highmark BCBSD Inc.

In addition to the undersigned, Anthony Cardone CFE, CPA (Examination Supervisor) Barry Lupus, Staff Examiner, CPA, CFE, CFE (Fraud), Samuel Kohlmeyer, CFE, James Grimes, CFE, Andrew Bougie, CPA and Kyle Poplos, CPA participated in the examination. The assistance of Delaware's consulting actuarial firm, INS Consultants, Inc. and INS Services, Inc. are acknowledged.

Respectfully submitted,

A handwritten signature in cursive script that reads "Albert M. Piccoli, Sr." The signature is written in black ink and is positioned above a horizontal line.

Albert M. Piccoli, Sr., CFE
Examiner-In-Charge
State of Delaware