

ORGANIZATIONAL EXAMINATION

OF

NMHC GROUP SOLUTIONS INSURANCE, INC.

AS OF

JUNE 30, 2006

I, Matthew Denn, Insurance Commissioner of the State of Delaware, do hereby certify that the attached ORGANIZATIONAL REPORT ON EXAMINATION, made as of JUNE 30, 2006 of the

NMHC GROUP SOLUTIONS INSURANCE, INC.

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

ATTEST BY:

Annette Handy

DATE: 30 AUGUST 2006



In witness Whereof, I HAVE HEREUNTO SET MY HAND AND AFFIXED THE OFFICIAL SEAL OF THIS DEPARTMENT AT THE CITY OF DOVER, THIS 30TH DAY OF AUGUST.

Matthew Denn

Insurance Commissioner

REPORT ON ORGANIZATIONAL EXAMINATION
OF THE
NMHC GROUP SOLUTIONS INSURANCE, INC.
AS OF
JUNE 30, 2006

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

Consideration has duly been 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 "Matthew Denn", with a horizontal line extending to the right from the end of the signature.

MATTHEW DENN
INSURANCE COMMISSIONER

DATED this 30TH day of AUGUST, 2006.

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SALUTATION

July 10, 2006

Honorable Mathew Denn
Insurance Commissioner
State of Delaware
Rodney Building
841 Silver Lake Boulevard
Dover, Delaware 19901

Dear Commissioner:

In accordance with instructions contained in Certificate of Authority No. 06.026, an Organizational Examination has been conducted of the

NMHC GROUP SOLUTIONS INSURANCE, INC.

hereinafter referred to as “the Company”, incorporated under the laws of the State of Delaware.

The examination was conducted at the Company’s administrative office, located at 26 Harbor Park Drive, Port Washington, New York 11050.

The report of such examination is respectfully submitted herewith.

SCOPE OF EXAMINATION

This organizational examination is conducted in conjunction with the Company's application for a domestic Certificate of Authority in the State of Delaware. A review was made of the Company's corporate records and financial data as of June 30, 2006.

HISTORY

The Company's certificate of incorporation was filed with the office of Secretary of the State of Delaware on March 2, 2006 by its sole incorporator, Carrie L. Tillman. Pursuant to Section 242 of the Delaware General Corporation Law and as authorized by the Board of Directors, the certificate of incorporation was amended on June 13, 2006 for the purpose of changing the number of authorized common shares of the Corporation.

The registered office of the Company is located at 103 Foulk Road, Suite 200, Wilmington, County of New Castle, Delaware 19803. The name of the Company's registered agent at such address is CSC Entity Services, LLC.

CAPITALIZATION

Initially, the Company was authorized to issue 1,000 shares of common stock with a par value of \$ 1.00 per share of which on March 7, 2006, the immediate parent company, National Medical Health Card Systems, Inc. (NMHC) purchased 1,000 shares. On June 13, 2006, the authorized number of shares of common stock was increased to 7,000,000 shares and 2,000,000 shares with a par value of \$ 1 were issued to NMHC.

In addition, NMHC contributed a net amount of \$ 4,611,333 of paid-in surplus during the period prior to June 30, 2006.

MANAGEMENT AND CONTROL

The Company's bylaws, adopted March 13, 2006, state that the business and affairs of the Company shall be managed by a Board of Directors consisting of not less than one (1) nor more than nine (9) Directors, of whom need not be residents of Delaware, citizens of the United States or stockholders of the Corporation. The Directors shall be elected at the annual meeting of stockholders of this Corporation and shall be held at such date and time as shall be designated from time to time by the Board of Directors. The following individuals were the elected and qualified members of the Board of Directors as of June 30, 2006.

Directors

James F. Smith
Stuart Diamond
Jonathan Friedman

Committees

Pursuant to Article IV of the bylaws, the Board of Directors may designate an Executive or other committees. Such committees are subject to limitations of authority as may be determined from time to time by the Board of Directors. As of the Examination date, the Board of Directors has not designated any committees.

Officers

In accordance with Article VI of the Company's bylaws, the Directors of the Company shall elect officers of the Corporation as deemed necessary to carrying on the business of the Corporation. Primarily, the Officers of the Company are to be elected annually by the Board of Directors and the following persons were initially chosen as the Officers of the Company on March 7, 2006:

<u>Officer</u>	<u>Position</u>
James F. Smith	President & Chief Executive Officer
Stuart Diamond	Chief Financial Officer & Treasurer
Jonathan Friedman	Secretary

The NAIC Biographical Affidavits of the Officers and Directors of the Company have been reviewed during this examination.

HOLDING COMPANY SYSTEM

The Company is a member of an Insurance Holding Company System. A Holding Company Registration Statement will be filed, when required, with the Delaware Insurance Department.

The Company is a wholly owned subsidiary of National Medical Health Card Systems Inc. (NMHC), a public-traded corporation that was incorporated in the State of New York on July 23, 1981 as a Pharmacy Benefits Manager and subsequently was re-incorporated in the State of Delaware on December 21, 2001. NMHC's clients include managed care organizations, Taft-Hartley and multi-employer union groups, third-party administrators, self-insured employer groups, workers' compensation plans, school districts and municipalities. The immediate parent company's headquarters are located at 26 Harbor Park Drive, Port Washington, New York and in addition, service centers are maintained in other states.

The entity with the majority controlling interest of NMHC is New Mountain Partners, LP, incorporated as a Delaware Limited Partnership on December 22, 1999 and located in New York, New York and serves as an investment management firm for private and public equity accounts.

New Mountain Partners, LP owns 56.8% of the series A preferred stock of NMHC. In addition, New Mountain Affiliated Investors, L.P. owns 3.2% of the series A preferred stock of NMHC. The remaining shares are held by various stockholders.

MANAGEMENT AND SERVICE AGREEMENTS

Pharmacy Benefits Management Agreement

The Company entered into a management agreement, effective March 9, 2006 with its parent, NMHC, of whom will manage the Company's prescription drug benefit plan with services that include; access to member pharmacies to dispense medication to members, claim processing and adjudication, customer service, account reporting, formulary management and other product administration.

Sublease and Administrative Services Agreement

The Company entered into a Sublease and Administrative Services Agreement on March 2, 2006 with an unaffiliated company, Blue Diamond Realty, LLC, a Delaware limited liability company for the purpose of leasing space and attaining access to office equipment and obtaining clerical support services.

Escrow and Depository Bank Agreements

The Company entered into three (3) separate bank agreements described as follows:

- 1) An Escrow Agreement with JPMorgan Chase Bank, N.A., effective June 22, 2006, was established for the purpose of maintaining financial requirements under the Medicare Modernization Act of 2003, whereby a segregated reserve fund was established for the Company to fulfill its obligations as an eligible non-state licensed prescription drug plan entity in the event of its insolvency. The initial cash deposit amounted to \$100,000.
- 2) A Depository Agreement with JPMorgan Chase Bank, N.A., effective June 19, 2006, was established for the purpose of maintaining sufficient funds to operate as a Prescription Drug Plan provider.

3) An Escrow Agreement with U.S. Bank Trust National Association, effective June 30, 2006, was established for the purpose of maintaining a deposit in the State of Delaware for the protection of all its policyholders pursuant to Section 513 of the Delaware Insurance Code. The initial deposit amounted to \$200,000.

The terms of all three (3) bank agreements appear reasonable and include an indemnification clause that is similar to the provisions stated in the NAIC Examiners Financial Condition Handbook.

PLAN OF OPERATION

The Company was created for the sole purpose of being a Prescription Drug Plan (PDP) Sponsor providing benefit services under Medicare's Part D coverage and will be the underwriter for such policies.

The Company will use the sales staff of its parent to introduce the Part D line of business to employer and union groups. Since this line of business will be sold directly to self-insured employer groups, there will be no sales staff employed to market and sell directly to individual Medicare beneficiaries. The Company will use a combination of internal sales representatives of its parent and outside sales consultants to sell to prospective organizations.

The Medicare Modernization Act legislation, enacted in December of 2003, provides seniors and people with disabilities with the first comprehensive prescription drug benefit ever offered under the Medicare program. The Company plans to enter this market area as a Prescription Drug Plan Sponsor (an entity contracted with the Centers for Medicare and Medicaid Services (CMS) to provide prescription coverage to Medicare enrollees) effective January 1, 2007. The product lines that will be offered are in accordance with the Centers for

NMHC Group Solutions Insurance, Inc.

Medicare and Medicaid Services defined standard benefit and the enhanced prescription drug benefits.

The Company plans to market its PDP products and services nationally to insured Medicare eligible members of employer group and union organizations that reside anywhere in the United States, District of Columbia and Puerto Rico.

All advertising will be developed, purchased, controlled and supervised by the parent company. Since the products and services will be directly marketed to businesses, the Company has no plans to use print, television, radio or internet media to promote or advertise its products and services.

CAPITAL AND SURPLUS REQUIREMENTS

Section 511 (a) of the Delaware Insurance Code requires the following minimum capital and surplus amounts for a stock life and health insurance company:

Common Capital Stock	\$350,000
Free Surplus	<u>200,000</u>
Total Capital and Surplus	<u>\$550,000</u>

FINANCIAL STATEMENT

The Company's financial position as of June 30, 2006, as determined by this examination was as follows:

	<u>Assets</u>	<u>Note</u>
Cash/Cash Equivalents	\$ <u>6,852,979</u>	1
Total Assets	\$ <u>6,852,979</u>	
<u>Liabilities, Surplus and Other Funds</u>		
Accounts payable	\$ 30,000	
Payable to parent company	<u>256,580</u>	2
Total Liabilities	\$ <u>286,580</u>	
Common Capital Stock	2,000,000	
Gross paid in and contributed surplus	4,611,333	
Unassigned funds	<u>(44,934)</u>	
Surplus as regards policyholders	<u>\$6,566,399</u>	
Total Liabilities and Surplus as Regards Policyholders	\$ <u>6,852,979</u>	

NOTES TO THE FINANCIAL STATEMENT

Note 1

The Company has three (3) separate agreements as discussed in the section of this report captioned, "Management and Service Agreements". All amounts as shown in the accounts as described below were as of June 30, 2006:

(1) The escrow agreement with JPMorgan Chase Bank, N.A. serves as a restricted reserve fund whereby the Company shall deposit additional amounts annually or on another periodic basis as determined appropriate by the Secretary of Health and Human Services that is sufficient to meet applicable regulations. An amount of \$100,079 was held by the bank.

(2) The escrow agreement with U.S. Bank Trust National Association was established as a statutory deposit with the State of Delaware and the amount of the funds held by the bank was \$203,000.

(3) The depository agreement with JPMorgan Chase Bank, N.A. was established to comply with certain minimum net worth requirements amounting to \$1.5 million and projected losses requirements of The Centers for Medicare and Medicaid Services (CMS). The projected losses calculation requires the Company to have allowable sources of funding sufficient to cover the greater of; (i) 7.5% of the aggregated projected target amount for a given year or (ii) resources to cover 100% of any projected losses, if the business plan projected losses is greater than 7.5% of the aggregated projected target amount. The projected loss calculation amounted to \$6,311,333. The Company's projections may change upwards or downwards and consequently the amount in the depository account may fluctuate upwards or downwards. The amount of \$6,347,525 was held by the bank.

The other funds held by two banks were a money market deposit account with Wachovia Bank N.A., amounting to \$201,702 and a regular account held by JPMorgan Chase Bank, N.A. amounting to \$673.

All the assets were verified by direct confirmation from the banks.

Note 2

The liabilities for accounts payable represents an accrual for consulting fees for actuarial services of \$30,000 and the amounts due to the parent company (NMHC) relates to fund deposit requirements for Medicare license applications and state filing fees amounting to \$256,580.

CONCLUSION

Based on the organizational examination conducted as of June 30, 2006, the financial condition of NMHC Group Solutions Insurance, Inc. was as follows:

Assets	\$ 6,852,979
Liabilities	\$ 286,580
Surplus As Regards Policyholders	\$ 6,566,399

This examination was conducted in conjunction with the Company's application to the Delaware Insurance Department to conduct an insurance business as a Prescription Drug Plan Sponsor under Medicare's Part D coverage.

Upon completion of the organizational examination, the Company has complied with the capitalization requirements for a stock life and health insurer for the State of Delaware.

The examination was conducted by the undersigned.

Respectfully submitted,



Ronald Fox CFE, CIE
Examiner-In-Charge
Department of Insurance
State of Delaware