

REPORT ON EXAMINATION

OF THE

HIP INSURANCE COMPANY OF NEW YORK

AS OF

DECEMBER 31, 2001

DATE OF REPORT

NOVEMBER 5, 2004

EXAMINER

LISA M. FERNÉZ

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STATE OF NEW YORK
INSURANCE DEPARTMENT
25 BEAVER STREET
NEW YORK, NEW YORK 10004

George E. Pataki
Governor

Gregory V. Serio
Superintendent

November 5, 2004

Honorable Gregory V. Serio
Superintendent of Insurance
Albany, New York 12257

Sir:

Pursuant to the requirements of the New York Insurance Law, and acting in compliance with the instructions contained in Appointment Number 21855, dated March 11, 2002, attached hereto, I have made an examination into the financial condition and affairs of the HIP Insurance Company of New York, a domestic for-profit health insurance company licensed under the provisions of Article 42 of the New York Insurance Law, as of December 31, 2001, and respectfully submit the following report thereon.

A concurrent examination was made of the Health Insurance Plan of Greater New York ("HIP-NY"), an affiliated not-for-profit health service corporation licensed under the provisions of Article 43 of the New York Insurance Law. A separate report thereon has been submitted.

The examination was conducted at the Company's home office located at 7 West 34th Street, New York, New York 10001.

Wherever the terms "HIPIC" or the "Company" appear in this report, without qualification, they shall be understood to refer to the HIP Insurance Company of New York.

1. SCOPE OF EXAMINATION

This examination covers the period from March 4, 1995 through December 31, 2001. A previous examination on organization was conducted as of March 3, 1995. Where deemed appropriate, transactions occurring subsequent to December 31, 2001 were also reviewed.

The examination comprised a verification of assets and liabilities as of December 31, 2001 in accordance with Statutory Accounting Principles, as adopted by the Department; a review of income and disbursements to the extent deemed necessary to accomplish such verification; and utilized, to the extent considered appropriate, work performed by the Company's independent certified public accountants. A review or audit was also made of the following items as called for in the Examiners Handbook of the National Association of Insurance Commissioners ("NAIC"):

- Company history
- Management and control
- Corporate records
- Fidelity bond and other insurance
- Territory and plan of operation
- Growth of Company
- Reinsurance
- Accounts and records

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

2. DESCRIPTION OF COMPANY

HIPIC was incorporated under the laws of the State of New York as a for-profit health insurance company on September 7, 1994. On January 12, 1995 HIPIC issued 30,000 shares of \$10 par value per share common stock to its immediate parent, HIP Holdings, Inc., for a consideration of \$5,000,000, bringing its authorized capital to \$300,000 and contributed capital to \$4,700,000. On June 5, 1995, the Department granted HIPIC a license to operate as an accident and health insurance company as defined in paragraphs 3(i) and (ii) of Section 1113(a) of the New York Insurance Law. HIPIC commenced operations in September 1995.

A. Management and Controls

The Company's by-laws provide that the board of directors shall be comprised of not less than thirteen (13) nor more than eighteen (18) members. Directors are elected for a period of one year at the annual meeting of the shareholders held in May of each year. As of December 31, 2001 the board of directors consisted of fourteen members.

The fourteen board members and their principal business affiliations as of December 31, 2001, were as follows:

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Roslyn Berrin* Far Rockaway, NY	Recreational Consultant	1995
Fred Blickman Scarsdale, NY	Senior Vice President, Human Resources, Health Insurance Plan of Greater New York	2001
Jeannette DiLorenzo* New York, NY	Retired Schoolteacher	1995

<u>Name and Residence</u>	<u>Principal Business Affiliation</u>	<u>Year First Elected</u>
Michael Fullwood, Esq. New York, NY	Executive Vice President, Chief Financial Officer, Corporate Secretary and General Counsel, Health Insurance Plan of Greater New York Treasurer, HIP Insurance Company of New York	1999
Paul Gibson* Uniondale, NY	Manager Capital Funding, Conti Group Companies, Inc.	1995
Edward Lucy Ottsville, PA	Senior Vice President, Delivery Systems Management and Strategy, Health Insurance Plan of Greater New York	2001
Daniel McGowan Centerport, NY	President and Chief Operating Officer, Health Insurance Plan of Greater New York	2000
Ronald I. Platt, M.D. Parkland, FL	Senior Vice President, Medical Affairs and Chief Medical Officer, Health Insurance Plan of Greater New York	2001
Leslie Strassberg Scarsdale, NY	Senior Vice President, Actuarial Services and Underwriting, Health Insurance Plan of Greater New York President, HIP Insurance Company of New York	1996
John Steber West Windsor, NY	Executive Vice President, Operations and Chief Information Officer, Health Insurance Plan of Greater New York	2000
Anthony Watson West Orange, NJ	Chairperson and Chief Executive Officer, Health Insurance Plan of Greater New York	1994
Robert Wick* Scarsdale, NY	President, Wick Publications	1999
Sadie Winslow* New York, NY	Retired Schoolteacher	1995
Marc Wolfert Long Island City, NY	Senior Vice President/COO, Centralized Laboratory Services	1999

* Not affiliated with the Company or any other company in the holding company system

It should be noted that the following board changes transpired subsequent to December 31, 2001:

- Jeannette DiLorenzo passed away on May 14, 2002.
- Peter Meringolo was elected to the board on June 19, 2002.
- Robert Wick resigned from the board on June 19, 2002.

A review was performed of the attendance of HIPIC's directors at the twenty-three board meetings held during the examination period. The following directors were found to have attended less than 50% of the scheduled board meetings that they were eligible to attend during this period:

<u>Name</u>	<u># of Meetings Attended</u>	<u># of Meetings Eligible to Attend</u>	<u>Percentage</u>
Amarilys Cortijo	5	13	38%
Jeanette Dilorenzo	10	23	43%
Sadie Winslow	10	22	45%
Robert Wick	4	10	40%

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 Company. 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 Company take corrective action by developing a policy to evaluate whether board members who are unable or unwilling to attend meetings consistently should resign or be replaced. Furthermore, in selecting prospective 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 Company.

It is noted that, of the four directors listed, only Ms. Sadie Winslow remains on HIPIC's board.

A review of the Company's corporate charter and by-laws revealed the following:

- The Company amended its by-laws three times during the examination period. With each amendment, however, the Company failed to carry forth provisions from previous amendments.
- The Company had not held any annual shareholder meetings since its incorporation. In lieu of the annual meeting the Company exercised its power to act by written consent, pursuant to Section 3.8 of its by-laws.
- Section 4.3 of the Company's by-laws states, "In addition to the meeting of the Board of Directors following the annual meeting of the shareholders, the Board of Directors shall hold at least three regular scheduled quarterly meetings each year, none of which may take place during the quarter in which the annual meeting is held." The examination review revealed that the board held only two regular meetings in 1998 and 1999.
- Although the Company's by-laws allow for its board of directors to create special committees ad hoc, HIPIC's board did not have any committees during the period under examination. However, it should be noted that, at its December 20, 2001 board meeting, the board resolved to amend the Company's by-laws regarding the composition of the board of directors and its committees. Specifically, Article 4, Section 4.11 was amended to contain language requiring the board to establish an audit committee. However, as of the date of this report, HIPIC's board had not established an audit committee.

Based on the above, it is recommended that HIPIC abide by its by-laws by convening the prescribed number of meetings.

It is also recommended that HIPIC establish an audit committee comprised solely of directors who are not officers or employees of the Company or any of its affiliated entities.

It is further recommended that the Company take greater care in carrying forward any revisions made to its by-laws.

The following is a listing of the principal officers of the Company as of December 31, 2001:

<u>Name</u>	<u>Title</u>
Leslie Strassberg	President
Williams Lewis	Secretary
Michael Fullwood	Treasurer
Michael Vincent	Assistant Treasurer
Stephen Giasi*	Controller

* Ceased employment effective December 8, 2003.

The examiners reviewed HIPIC's Conflict of Interest ("COI") Policy which calls for annual distribution, completion and review of COI forms. The examination review revealed that HIPIC had not distributed COI forms prior to 2001. However, as HIPIC has no employees and its officers are shared with HIP-NY, HIPIC's failure to distribute these forms was limited to those members of its board of directors that serve on HIPIC's board exclusively. It is noted that HIPIC did abide by its COI policy by distributing the COI forms for the year 2001.

It is recommended that HIPIC continue to comply with its Conflict of Interest policy and have its COI forms distributed, completed and reviewed on an annual basis.

The examination review of HIPIC's 2001 COI forms revealed that the questions contained therein failed to adequately elicit its employees, officers, and directors' outside business affiliations and, where applicable, current employment position and work status.

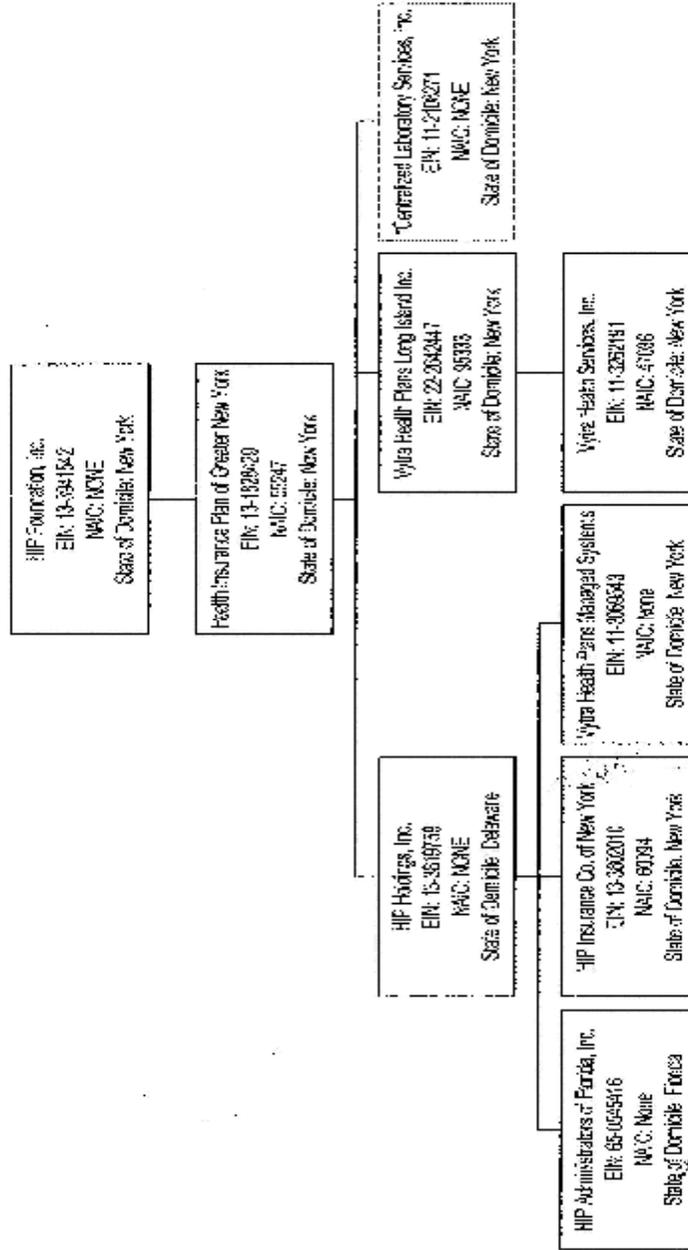
It is recommended that, in order for the Company to make a truly informed decision regarding whether a conflict of interest may exist, the Company obtain full disclosure from its employees, officers, and directors with respect to their outside business affiliations.

B. Holding Company

The Company is a wholly-owned subsidiary of HIP Holdings, Inc. ("HIP Holdings"), a Delaware holding corporation. HIP Holdings, in turn, is a wholly-owned subsidiary of the Health Insurance Plan of Greater New York ("HIP-NY"), a not-for-profit health insurer incorporated in the state of New York, operating under the provisions of Article 43 of the Insurance Law. The ultimate parent of these companies is HIP Foundation, Inc., a New York not-for-profit charitable organization.

An organization chart reflecting the relationship between the Company and significant entities in its holding company system as of December 31, 2001 follows:

Organizational Chart



* Determined to be a member of HIP's holding company system during the examination period pursuant to Section 1501(a)(6) of the New York Insurance Law

Since 1995, HIPIC has underwritten the out-of-network portion of the Point of Service (“POS”) product offered jointly with HIP-NY. This out-of-network benefit is provided on an indemnity basis. As HIPIC has no dedicated employees or facilities, all services are provided to HIPIC by HIP-NY pursuant to the terms of a service agreement. Such agreement provides for HIP-NY to charge HIPIC for services rendered based on the allocation of various departments’ fully loaded expenses.

Section 1505(d) of the New York Insurance Law states in part:

“The following transactions between a domestic controlled insurer and any person in its holding company system may not be entered into unless the insurer has notified the superintendent in writing of its intention to enter into any such transaction at least 30 days prior thereto, or such shorter period as he may permit, and he has not disapproved it within such period...(3) rendering of services on a regular or systematic basis;...”

The examination review of HIPIC’s holding company transactions revealed that prior to June 2001, inter-company transactions between HIP-NY and HIPIC were entered into without making the requisite filings and obtaining the superintendent’s non-disapproval. On June 25, 2001, HIP filed an Administrative Service Agreement (“Agreement”) with the Department that was non-disapproved on August 22, 2001. The effective date of the Agreement is August 31, 2001.

The Company violated Section 1505(d)(3) of the New York Insurance Law when it failed to notify the superintendent of its intention to enter into an agreement with an affiliate for the purpose of receiving services on a regular or systematic basis.

It is recommended that, prior to entering into transactions with any member of its holding company system involving either the rendering or receiving of services on a regular or systematic basis, HIPIC notify the Department of its intention in writing, pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.

Pursuant to the terms of the Agreement, HIP-NY and HIPIC are required to settle any outstanding balances on a monthly basis. However, the examination review of inter-company transactions revealed that, while HIPIC recorded all amounts due HIP-NY on

its books each month, settlement on these outstanding balances was not made monthly. In fact, during the period from September through December 2001, HIPIC made only one remittance, in the month of October.

It is recommended that HIPIC abide by the terms of its Agreement with HIP-NY and settle any outstanding balances on a monthly basis.

Department Circular Letter No. 33 (1979) sets forth guidelines to be used by domestic insurers that enter into tax allocation agreements with members of their holding company system. During the examination, HIPIC advised that it files a consolidated federal income tax return with HIP Holdings and its subsidiaries. According to the Company's filed annual statement, the consolidated tax liability is allocated among members of the group according to a Tax Sharing Agreement. However, the examination review revealed that a formal agreement between the parties was never executed. Further, it was also determined that the Tax Sharing Agreement referenced was not filed with the Department during the examination period as required pursuant to the provisions of Section 1505(d)(3) of the Insurance Law.

In response to the examination finding, HIPIC filed a draft copy of a Tax Sharing Agreement with the Department on October 30, 2003. However, in response to the Department's determination that the draft Agreement was unacceptable, HIPIC withdrew the October filing. In February 2004, HIPIC submitted a second draft copy of a Tax Sharing Agreement. As the second draft failed to contain provisions deemed necessary for compliance with Circular Letter No. 33 (1979), it was also determined to be unacceptable. Although the Company advised the Department that it intended to produce a document that did comply with the Circular Letter, a revised Agreement was never submitted. Accordingly, a Tax Sharing Agreement meeting the standards set forth in the Circular Letter was never formally filed with the Department.

During the examination period, HIPIC violated Section 1505(d)(3) of the New York Insurance Law by entering into a Tax Sharing Agreement with members of its holding company system without giving prior notice to the superintendent.

It is recommended that HIPIC immediately file the Tax Sharing Agreement with the Department and that such Agreement complies with the guidelines set forth in Department Circular Letter No. 33 (1979).

It is again recommended that, prior to entering into transactions with any member of its holding company system involving either the rendering or receiving of services on a regular or systematic basis, HIPIC notify the Department of its intention in writing, pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.

It is further recommended that, prior to engaging in any holding company transactions, HIPIC ensure that the agreements under which it intends to operate have been properly executed.

C. Territory and Plan of Operation

HIPIC is authorized to write accident and health insurance as defined in paragraphs 3(i) and (ii) of Section 1113(a) of the New York Insurance Law. The Company is licensed to do business in New York State only. As of December 31, 2001, HIPIC served approximately 22,000 members in the following New York counties: Bronx, Kings, Nassau, New York, Orange, Queens, Richmond, Rockland, Suffolk, and Westchester.

As noted previously, HIPIC underwrites the out-of-network portion of the POS products offered jointly with HIP-NY. As HIPIC was formed to market insurance products primarily to members of HIP-NY, it is economically dependent on HIP-NY.

D. Reinsurance

At December 31, 2001 the Company had one ceded reinsurance agreement in effect, with an unauthorized reinsurer. Pursuant to the terms of this agreement, the reinsurer is obligated to reimburse HIPIC for eligible medical and hospital services, excluding out-of-area emergency claims, incurred by members enrolled in HIPIC's POS Plan, either originally written or renewed, during the period of January 1, 2001 through January 1, 2002. The agreement contains three layers of liability, detailed as follows:

Layer 1

Reinsurer is liable to HIPIC for 80% of the ultimate net loss incurred by HIPIC for any one individual member (direct pay) in excess of an initial ultimate net loss of \$150,000 per member, subject to a limit of liability of \$250,000 per individual member.

Layer 2

Reinsurer is liable to HIPIC for 80% of claim amounts in excess of \$250,000, subject to a limit of liability of \$500,000 for any individual member and \$1,000,000 for group members.

Layer 3

Reinsurer is liable to HIPIC for 100% of claim amounts in excess of \$1,000,000, subject to a limit of liability of \$5,000,000 for group members only.

All reinsurance contracts effected during the examination period were reviewed and were found to contain the necessary clauses required by statute, including the insolvency clause required by Section 1308 of the New York Insurance Law.

E. Significant Operating Results

The following ratios have been computed as of December 31, 2001, based upon the results of this examination:

Net premiums written in 2001 to Surplus as regards policyholders	1.69 to 1
Liabilities to Liquid Assets	73.40%
Premiums in course of collection to Surplus as regards policyholders	34.20%

The underwriting ratios presented below are on an earned-incurred basis and encompass the March 4, 1995 to December 31, 2001 period covered by this examination:

	<u>Amounts</u>	<u>Ratios</u>
Claims incurred	\$36,963,996	61%
Claims adjustment expenses incurred	1,364,797	2%
Other underwriting expenses incurred	13,822,079	23%
Net underwriting gain	<u>8,417,604</u>	<u>14%</u>
Premiums earned	<u>\$60,568,476</u>	<u>100%</u>

F. Investment Activities

The Company has a cash management program which provides for the investment of excess cash balances in financial instruments that are readily convertible into cash. The Company primarily invests its operating funds in obligations of the U.S. Government and its agencies. Investments that have maturities of one year or less from the date of purchase are considered short-term investments.

HIPIC utilizes the services of investment managers to effect its day to day investment activities. The investment managers are given broad authority to take any action deemed necessary or desirable in the management of HIPIC's portfolio, subject to the Company's Investment Policy and Guidelines.

Pursuant to the terms of the Investment Manager Agreements entered into by HIP-NY, HIPIC's upstream affiliate, and the various investment managers, the securities held in HIPIC's portfolio were confirmed to be held by Deutsche Bank Trust Company Americas, the designated custodian. However, the examination review of these transactions revealed that HIPIC is neither a named party to these agreements, nor has it entered into separate agreements with the investment managers. Further, although the securities were confirmed in HIPIC's name, the name on the account was HIP-NY.

Accordingly, it is recommended that HIPIC either enter into separate agreements with its investment managers or take immediate action to become a named party, with the same powers as other named parties, to the existing agreements. Further, it is recommended that HIPIC be the named entity reflected on the custodial account.

Prior to the adoption of NAIC Codification ("Codification") in January 2001, statutory accounting principles historically called for bonds to be reported at amortized cost using various amortization methodologies that the Department deemed acceptable. Codification, however, limits the calculation of amortization of bond premium or discount to the scientific interest (constant yield) method. Note that at no time prior to Codification was reporting bonds at fair market value ("FMV") an acceptable valuation method.

During the examination review of HIPIC's investment portfolio it was revealed that the Company reported all bond investments held during the years 1995 through 2000 at FMV. As noted above, this method of valuing bonds is inconsistent with statutory accounting principles and accepted Department practices.

During the year 2001, pursuant to statutory accounting principles, HIPIC began reporting its bond investments at amortized cost. However, the Company derived its amortized cost using the straight-line method of amortization, rather than the scientific interest method prescribed under Codification.

However, as HIPIC's 2001 portfolio reflected that, on average, its investments were held for a short duration, it was determined that, for reporting purposes, using either the straight-line or scientific interest amortization methodologies would yield immaterial differences. Accordingly, no examination change was made to the amount reported by HIPIC for its bond investments in its December 31, 2001 annual statement.

It is recommended that, in its future filings with the Department, HIPIC report its bond investments using the prescribed amortization methodology.

G. Accounts and Records

During the course of this examination it was noted that the Company's reporting of certain items was not in accordance with prescribed statutory accounting principles and/or annual statement instructions, detailed as follows:

1. Allocation of Expenses

Department Regulation No. 33 sets forth classification and allocation methods to be used by Article 42 companies such as HIPIC for its expense reporting.

Pursuant to its Administrative Service Agreement with HIP-NY (*see Item 2B of this report, Holding Company*), HIPIC's share of expenses is based on the allocation of various departments' fully loaded expenses. However, the examination review revealed that HIP-NY did not employ uniform allocation methods when determining the various departments' share of corporate expenses. Further, the documentation provided by HIP-

NY to support the data reported by HIPIC in its December 31, 2001 annual statement, *Underwriting and Investment Exhibit, Part 3 – Analysis of Expenses*, was inconsistent with the data contained in the filing. The Company was unable to substantiate the differences. Accordingly, the examination concluded that HIPIC's expense allocations were not consistent with the provisions of Department Regulation No. 33.

It is recommended that HIPIC comply with the requirements of Department Regulation No. 33 in the determination of its expense allocations included in the financial statements filed with the Department.

2. Annual Statement Reporting

HIPIC's annual statements, as filed with the Department during the examination period, were found to contain various reporting errors and misclassifications of accounts. In some instances, such erroneous reporting resulted in the Company having to make revisions to previously filed schedules and exhibits. In other instances, errors were first identified by the examination.

For example, the following reporting errors were among those identified during the examination review of the Company's 2001 annual statement:

- The Underwriting and Investment Exhibit reported inaccurate expense allocations as the information reported therein was not consistent with the information used by the Company to prepare the exhibit (*see Item 2G-1 of this report, Allocation of Expenses*).
- Schedule S, Part 2 reflected inaccurate data that the Company revised after the annual statement was bound (*see Item 5 of this report, Amounts Recoverable from Reinsurers*).
- Schedule Y, Part 2 failed to reflect the entire year's transactions as called for in the NAIC Annual Statement Instructions.

It is recommended that the Company exercise greater care in the compilation of data for reporting purposes and comply with the annual statement instructions when preparing its Health Blank.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the assets, liabilities, surplus and unassigned funds as determined by this examination and as reported by the Company as of December 31, 2001:

	<u>Examination</u>	<u>Company</u>	<u>Surplus Inc/(Dec)</u>
<u>Admitted Assets</u>			
Bonds	\$15,443,366	\$15,443,366	
Cash	1,123	1,123	
Short term investments	6,356,596	6,356,596	
Accident and health premiums due and unpaid	4,658,381	4,658,381	
Amounts recoverable from reinsurers	0	105,969	(105,969)
Investment income due and accrued	<u>142,985</u>	<u>142,985</u>	
Total admitted assets	<u>\$26,602,451</u>	<u>\$26,708,420</u>	<u>\$(105,969)</u>
<u>Liabilities, Capital and Surplus</u>			
Claims unpaid	\$ 8,345,053	\$ 7,741,335	(603,718)
Aggregate claim reserves	0	603,718	603,718
Premiums received in advance	60,632	60,632	
General expenses due or accrued	160,913	160,913	
Federal income tax payable	440,082	440,082	
Amounts due to parent, subsidiaries and affiliates	3,636,212	3,636,212	
Payable for securities	<u>446,977</u>	<u>446,977</u>	
Total liabilities	<u>\$13,089,869</u>	<u>\$13,089,869</u>	<u>\$ 0</u>
Common capital stock	\$ 300,000	\$ 300,000	\$ 0
Gross paid in and contributed surplus	4,700,000	4,700,000	
Unassigned funds (surplus)	<u>8,512,582</u>	<u>8,618,551</u>	<u>(105,969)</u>
Total capital and surplus	<u>\$13,512,582</u>	<u>\$13,618,551</u>	<u>\$(105,969)</u>
Total liabilities, capital and surplus	<u>\$26,602,451</u>	<u>\$26,708,420</u>	<u>\$(105,969)</u>

NOTE 1: The Internal Revenue Service has not conducted any audits of the income tax returns filed on behalf of the Company. The examiner is unaware of any potential exposure of the Company to any tax assessment and no liability has been established herein relative to such contingency.

B. Underwriting and Investment Exhibit

Reserves and unassigned funds increased by \$8,438,123 from March 4, 1995 through December 31, 2001, detailed as follows:

Underwriting Income

Premiums earned		\$60,568,476
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Deductions:

Claims incurred	\$ 36,963,996	
Claims adjustment expenses	1,364,797	
Administrative expenses incurred	12,033,374	
Insurance taxes, licenses & fees	848,957	
Commission expenses incurred	<u>939,748</u>	
Total underwriting deductions		<u>52,150,872</u>
Net underwriting gain		\$ 8,417,604

Investment Income

Net investment income earned	2,370,222	
Net realized capital gains	<u>262,559</u>	
Net investment gain		<u>2,632,781</u>
Net income/(loss) before federal income tax		11,050,385
Federal and foreign income taxes		<u>2,384,447</u>
Net income		\$ <u>8,665,938</u>

Reserves and Unassigned Funds

Reserves and unassigned funds as of March 3, 1995		\$ 5,074,459
Net income	\$ 8,665,938	
Net unrealized capital gains	0	
Change in non-admitted assets	(227,815)	
Capital changes: Paid in	0	
Surplus adjustment: Paid in	<u>0</u>	
Net increase in reserves and unassigned funds		<u>8,438,123</u>

Reserves and Unassigned Funds as of December 31, 2001 per report on examination		<u>\$13,512,582</u>
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4. CLAIMS RESERVES

In its December 31, 2001 annual statement HIPIC reported total claims reserves in the amount of \$8,345,053, comprised of the following components:

Annual Statement <u>Line Item</u>	<u>Description</u>	<u>Amount</u>
1	Claims Unpaid	\$7,741,335
5	<u>Aggregate Claim Reserves</u>	<u>603,718</u>
	Claims Reserves	<u>\$8,345,053</u>

¶ Claims Unpaid

The examination amount of \$8,345,053 is \$603,718 more than the \$7,741,335 reported by the Company in its December 31, 2001 filed annual statement. The examination liability is greater due to the reclassification of the Aggregate Claim Reserves to this annual statement line item. (see *Aggregate Claim Reserves, below*)

¶ Aggregate Claim Reserves

The captioned liability of \$603,718, as reported by the Company at December 31, 2001, has been eliminated and the reserve was reclassified to the claims unpaid liability.

The liability amount reported by HIPIC as Aggregate Claim Reserves on line 5 of the annual statement represents the value of some future benefits which are to be provided after December 31, 2001, for claims which have already occurred at December 31, 2001 (i.e. Incurred but not Reported or “IBNR” losses). Per the NAIC Annual Statement Instructions for Health Companies, IBNR losses are to be reported as a component of claims unpaid.

Accordingly, this examination has determined that the amount reported by the Company as Aggregate Claim Reserves on page 3, line 5 of the annual statement should have instead been reported as Claims Unpaid on page 3, line 1.

SSAP #54, which was effective as of January 1, 2001, provides statutory guidance for income recognition and policy reserves for individual and group accident and health contracts. It is noted that, based on its interpretation of SSAP #54, HIPIC acted reasonably in its reporting of Aggregate Claims Reserves for 2001.

In its 2002 annual statement filing HIPIC properly reported this liability on page 3, line 1 as a component of claims unpaid.

5. AMOUNTS RECOVERABLE FROM REINSURERS

The Company reported an admitted asset in the amount of \$105,969 as of the examination date. Pursuant to this examination, the captioned asset has been eliminated.

During the examination review it was revealed that HIPIC erroneously reported a reinsurance recoverable asset that did not exist. It was further revealed that this error was due to an oversight by the Company — HIPIC had submitted revised supporting schedules indicating that there was no asset after the statement was bound, but failed in its revisions to remove the amount from its balance sheet.

6. SUMMARY OF COMMENTS AND RECOMMENDATIONS

<u>ITEM</u>		<u>PAGE NO.</u>
A.	<u>Management and Controls</u>	
i.	It is recommended that the Company take corrective action by developing a policy to evaluate whether board members who are unable or unwilling to attend meetings consistently should resign or be replaced.	5
ii.	It is recommended that HIPIC abide by its by-laws by convening the prescribed number of meetings.	6
iii.	It is recommended that HIPIC establish an audit committee comprised solely of directors who are not officers or employees of the Company or any of its affiliated entities.	7
iv.	It is recommended that the Company take greater care in carrying forward any revisions made to its by-laws	7
v.	It is recommended that HIPIC continue to comply with its Conflict of Interest policy and have its Conflict of Interest forms distributed, completed and reviewed on an annual basis.	7
vi.	It is recommended that, in order for the Company to make a truly informed decision regarding whether a conflict of interest may exist, the Company obtain full disclosure from its employees, officers, and directors with respect to their outside business affiliations.	8
B.	<u>Holding Company</u>	
i.	The Company violated Section 1505(d)(3) of the New York Insurance Law when it failed to notify the superintendent of its intention to enter into an Administrative Service Agreement with an affiliate for the purpose of receiving services on a regular or systematic basis.	10
ii.	It is recommended that, prior to entering into transactions with any member of its holding company system involving either the rendering or receiving of services on a regular or systematic basis, HIPIC notify the Department of its intention in writing, pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.	10

<u>ITEM</u>	<u>PAGE NO.</u>
B. <u> Holding Company</u>	
iii. It is recommended that HIPIC abide by the terms of its Administrative Service Agreement with HIP-NY and settle any outstanding balances on a monthly basis.	11
iv. HIPIC violated Section 1505(d)(3) of the New York Insurance Law by entering into a Tax Sharing Agreement with members of its holding company system without giving prior notice to the superintendent.	12
v. It is recommended that HIPIC immediately file the Tax Sharing Agreement with the Department and that such Agreement complies with the guidelines set forth in Department Circular Letter No. 33 (1979).	12
vi. It is again recommended that, prior to entering into transactions with any member of its holding company system involving either the rendering or receiving of services on a regular or systematic basis, HIPIC notify the Department of its intention in writing, pursuant to the provisions of Section 1505(d)(3) of the New York Insurance Law.	12
vii. It is recommended that, prior to engaging in any holding company transactions, HIPIC ensure that the agreements under which it intends to operate have been properly executed.	12
C. <u> Investment Activities</u>	
i. It is recommended that HIPIC either enter into separate agreements with its investment managers or take immediate action to become a named party, with the same powers as other named parties, to the existing agreements.	15
ii. It is recommended that HIPIC be the named entity reflected on the custodial account.	15
iii. The Company reported all bond investments held during the years 1995 through 2000 at fair market value, which was inconsistent with statutory accounting principles and accepted Department practices.	15

<u>ITEM</u>	<u>PAGE NO.</u>
C. <u>Investment Activities</u>	
iv. In 2001, pursuant to statutory accounting principles, HIPIC began reporting its bond investments at amortized cost. However, the Company derived its amortized cost using the straight-line method of accounting, rather than the scientific interest method prescribed under Codification.	16
v. It is recommended that, in its future filings with the Department, HIPIC report its bond investments using the prescribed amortization methodology.	16
D. <u>Accounts and Records</u>	
i. It is recommended that HIPIC comply with the requirements of Department Regulation No. 33 in the determination of its expense allocations included in the financial statements filed with the Department.	17
ii. It is recommended that the Company exercise greater care in the compilation of data for reporting purposes and comply with the annual statement instructions when preparing its Health Blank.	18
E. <u>Claims Reserves</u>	
The amount reported by the Company as Aggregate Claim Reserves on page 3, line 5 of the annual statement should have instead been reported as Claims Unpaid on page 3, line 1.	21
F. <u>Amounts Recoverable from Reinsurers</u>	
In its 2001 annual statement, HIPIC erroneously reported a reinsurance recoverable asset that did not exist.	22

Appointment No. 21855

**STATE OF NEW YORK
INSURANCE DEPARTMENT**

I, **GREGORY V. SERIO**, Superintendent of Insurance of the State of New York,
pursuant to the provisions of the Insurance Law, do hereby appoint:

Lisa Fernez

as a proper person to examine into the affairs of the

HIP Insurance Company of New York

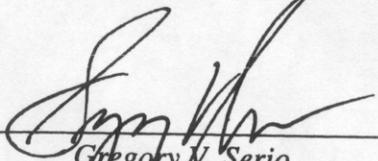
and to make a report to me in writing of the said

Company

with such information as she shall deem requisite.

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

this 11th day of March 2002



Gregory V. Serio
Superintendent of Insurance

