STATE OF NEW YORK INSURANCE DEPARTMENT

REPORT ON FINANCIAL CONDITION EXAMINATION

OF

THE FIRST REHABILITATION LIFE INSURANCE COMPANY

OF AMERICA

CONDITION:	December 31, 2009
DATE OF REPORT:	May 5, 2011

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OF AMERICA

AS OF

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EXAMINER:	MARK MCLEOD

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

Andrew M. Cuomo
Governor

James J. Wrynn
Superintendent

May 13, 2011

Honorable James J. Wrynn
Superintendent of Insurance
Albany, New York 12257

Sir:

In accordance with instructions contained in Appointment No. 30466, dated January 7, 2010 and annexed hereto, an examination has been made into the financial condition and affairs of The First Rehabilitation Life Insurance Company of America, hereinafter referred to as "the Company," at its home office located at 600 Northern Boulevard, Great Neck, New York, 11021.

Wherever "Department" appears in this report, it refers to the State of New York Insurance Department.

1. SCOPE OF EXAMINATION

The examination of the Company was a full scope financial examination as defined in the NAIC Financial Condition Examiners Handbook, 2010 Edition (the "Handbook"). The examination covers the three-year period from January 1, 2007 through December 31, 2009. 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, 2009 but prior to the date of this report (i.e., the completion date of the examination) were also reviewed.

The examination was conducted on a risk focused basis in accordance with the provisions of the Handbook published by the National Association of Insurance Commissioners ("NAIC"). The Handbook guidance provides for the establishment of an examination plan based on the examiner's assessment of risk in the insurer's operations and utilizing that evaluation in formulating the nature and extent of the examination. The examiner planned and performed the examination to evaluate the current financial condition as well as identify prospective risks that may threaten the future solvency of the insurer. The examiner identified key processes, assessed the risks within those processes and evaluated the internal control systems and procedures used to mitigate those risks. The examination also included assessing the principles used and significant estimates made by management, evaluating the overall financial statement presentation, and determining management's compliance with Department statutes and guidelines, Statutory Accounting Principles as adopted by the Department, and annual statement instructions.

Information about the Company's organizational structure, business approach and control environment were utilized to develop the examination approach. The Company's risks and management activities were evaluated incorporating the NAIC's nine branded risk categories. These categories are as follows:

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

- Legal
- Reputational

The Company was audited annually, for the years 2007 through 2009, by the accounting firm of Ernst & Young. The Company received an unqualified opinion in all years. Certain audit workpapers of the accounting firm were reviewed and relied upon in conjunction with this examination. The Company has an internal audit department which was given the task of assessing the internal control structure. Where applicable, internal audit workpapers and internal audit reports were reviewed and portions were relied upon for this examination.

The examiner reviewed the corrective actions taken by the Company with respect to the financial recommendations contained in the prior report on examination. The results of the examiner's review are contained in item 8 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. DESCRIPTION OF COMPANY

A. History

The Company was incorporated in New York as a stock insurance company under the name of The First Rehabilitation Insurance Company of America on August 12, 1971. The Company was licensed on August 8, 1972 to write accident and health insurance as specified in paragraph 3 of Section 1113(a) of the New York Insurance Law and commenced business on November 1, 1972. In January 1997, the Company amended its charter to include the writing of life insurance and annuities as specified in paragraphs 1 and 2 of Section 1113(a) of the New York Insurance Law. The name of the Company was changed to The First Rehabilitation Life Insurance Company of America effective January 1, 1997. As of December 31, 2009, the Company had 20,000 shares of common stock outstanding and capital and paid in and contributed surplus of $2,000,000 and $6,006,228, respectively.

B. Holding Company

The Company is a wholly owned subsidiary of Rehab Services Corporation ("Rehab Services"), a New York domiciled insurance holding company. The major stockholders of Rehab Services are Seth Goldberg (26%), the estate of Bruce Goldberg (26%), and the estate of Glenn Goldberg (26%).

The Company and Rehab Services file a consolidated tax return. The Company has a consolidated tax allocation agreement on file with the Department in accordance with Department Circular Letter No. 33 (1979).

C. Management

The Company's by-laws provide that the board of directors shall be comprised of not less than nine and not more than 21 directors. Directors are elected for a period of one year at the annual meeting of the stockholders held in December of each year. As of December 31, 2009, the board of directors consisted of 10 members. Meetings of the board are held quarterly.

The 10 board members and their principal business affiliation, as of December 31, 2009, were as follows:

Name and Residence	Principal Business Affiliation	Year First Elected
John Baldwin Pleasantville, NY	President and Vice Chairman of the Board The First Rehabilitation Life Insurance Company of America	1981
Anthony Barbiero* East Islip, NY	Attorney Anthony Barbiero, P.C.	1972
Mehmet Cetin* Sarasota, FL	Retired	1972
Gerald Dolman* Brooklyn, NY	President Administrators of the Professions, Inc.	1998
Michelle Goldberg - Berezin New York, NY	Homemaker	2004
Seth Goldberg Roslyn, NY	Chairman of the Board	1972
Alvin Lefkowitz Rockville Centre, NY	Secretary The First Rehabilitation Life Insurance Company of America	1972
Norman Mandel* Brooklyn, NY	Retired	1995
Morton Povman* Forest Hills, NY	Attorney Morton Povman, P.C.	1972
Richard White Woodbury, NY	Chief Executive Officer The First Rehabilitation Life Insurance Company of America	2009

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

In June 2010, Debbie Goldberg joined the board of directors.

The examiner's review of the minutes of the meetings of the board of directors and its committees indicated that meetings were well attended and that each director attended a majority of meetings.

The following is a listing of the principal officers of the Company as of December 31, 2009:

Name	Title
Seth Goldberg	Chairman of the Board
John Baldwin	President and Vice Chairman of the Board
Richard White	Chief Executive Officer
Bruce Wallach	Executive Vice President, Chief Financial Officer and Treasurer
Constantine Lappas	Executive Vice President and Chief Operating Officer
Robert Slack	Senior Vice President and Controller
Alvin Lefkowitz	Secretary
Patricia McHugh	Senior Vice President and Chief Administrative Officer
Fern Summer*	Legal Counsel and Assistant Corporate Secretary

* Designated consumer services officer per Section 216.4(c) of Department Regulation No. 64

In December 2010, John Baldwin resigned as President and as of the date of this report had not yet been replaced.

In September 2010, Patricia McHugh left the Company and in November 2010, Robert Slack's title was changed from Senior Vice President and Controller to Senior Vice President, Finance and Treasury.

Section 4211(a) of the New York Insurance Law states, in part:

> "No election of directors of a domestic stock life insurance company shall be valid unless a copy of the notice of election shall have been filed in the office of the superintendent at least ten days before the day of such election in addition to the service thereof . . ."

Steven Ostrer was elected as a director of the Company on September 6, 2007 and Rich White was elected as a director on September 10, 2009. The Company did not file a copy of the notice of election in the office of the superintendent at least ten days before the days of such elections.

The Company violated Section 4211(a) of the New York Insurance Law by failing to file a copy of the notice of election in the office of the superintendent at least ten days before the elections of certain directors.

3. TERRITORY AND PLAN OF OPERATIONS

The Company is authorized to write life insurance, annuities and accident and health insurance as defined in paragraphs 1, 2 and 3 of Section 1113(a) of the New York Insurance Law.

The Company is licensed to transact business in 15 states and the District of Columbia. In 2009, 94% of accident and health premiums and 93% of life premiums were received from New York. Policies are written on a non-participating basis.

The Company's primary product is the New York State Statutory Disability Benefit ("DBL"). The Company also offers group term life and group accident and health coverage including: long term disability, two excess major medical policies (an excess group major medical policy (XGMM) and an excess group medical reimbursement policy (GMRP)), stop loss, dental and vision plans. All policies are written on a group basis. The Company does not issue policies on an individual basis. The Company does not write annuities.

The Company stopped accepting applications for its GMRP business in March 2010 and plans to exit the GMRP business in 2011.

A. Statutory and Special Deposits

As of December 31, 2009, the Company had $1,750,000 (par value) of United States Treasury Notes on deposit with the State of New York, its domiciliary state, for the benefit of all policyholders, claimants and creditors of the Company. As per confirmations received from the following states which were reported in Schedule E of the 2009 filed annual statement, an additional $954,004 was being held by the states of Massachusetts and North Carolina.

B. Direct Operations

The Company's agency operations are conducted on both a general agency and broker basis. Group accident and health insurance plans are sold by brokers and agents, and group term life insurance is sold exclusively through agents.

C. Reinsurance

The Company's life and accident and health business is reinsured on a coinsurance, modified-coinsurance, and/or yearly renewable term basis. Reinsurance is provided on an automatic basis.

As of December 31, 2009, the Company had three reinsurance treaties in effect with three companies, all of which were authorized or accredited. Long term disability policies are ceded to Union Security Life Insurance Company of New York on an automatic quota share basis with the Company retaining 20% of each risk and to GE Insurance Solutions on an automatic quota share basis with the Company retaining 10% of each risk.

Group term life insurance policies, which have a maximum face amount of $300,000, are ceded to Swiss Re Life & Health America Inc. on an automatic quota share basis. The maximum retention limit for the Company is 50% of the first $100,000 per person.

Stop loss policies are ceded on an automatic quota share basis with the Company retaining 20% of the risk up to $1,000,000. Policies with a lifetime maximum greater than $1,000,000 but less than or equal to $5,000,000, are reinsured 100% up to $4,000,000 in excess of $1,000,000, for a specific medical expense. However, no stop loss policies were issued during the examination period.

4. SIGNIFICANT OPERATING RESULTS

Indicated below is significant information concerning the operations of the Company during the period under examination as extracted from its filed annual statements. Failure of items to add to the totals shown in any table in this report is due to rounding.

The following table indicates the Company's financial growth (decline) during the period under review:

	December 31, 2006	December 31, 2009	Increase (Decrease)
Admitted assets	$93,977,575	$93,461,248	$ (516,327)
Liabilities	$61,467,585	$51,450,558	$(10,017,027)
Common capital stock	$ 2,000,000	$ 2,000,000	$ 0
Gross paid in and contributed surplus	5,400,000	6,006,228	606,228
Aggregate write-ins for special surplus funds	0	1,000,000	1,000,000
Aggregate write-ins for other than special surplus funds	(238,395)	(498,493)	(260,098)
Unassigned funds (surplus)	25,348,387	33,502,955	8,154,568
Total capital and surplus	$32,509,992	$42,010,690	$ 9,500,698
Total liabilities, capital and surplus	$93,977,577	$93,461,248	$ (516,327)

The Company's invested assets as of December 31, 2009 were mainly comprised of bonds (95.7%).

The majority (97.7%) of the Company's bond portfolio, as of December 31, 2009, was comprised of investment grade obligations.

The following is the net gain from operations by line of business after federal income taxes but before realized capital gains reported for each of the years under examination in the Company's filed annual statements:

	2007	2008	2009
Ordinary:			
Life insurance	$ 114,504	$ 276,618	$ 75,532
Total ordinary	$ 114,504	$ 276,618	$ 75,532
Accident and health:			
Group	$4,740,312	$7,868,740	$2,432,627
Total accident and health	$4,740,312	$7,868,740	$2,432,627
Total	$4,854,816	$8,145,358	$2,508,159

The increase in the group accident and health gain between 2007 and 2008 was due to the $4,226,985 increase in net premium written from 2007 to 2008 and the increase in federal income tax benefit recognized. The decrease in the group accident and health gain between 2008 and 2009 was due to the increase in expenses which was caused by the addition of a new executive management team, the creation of new staff positions to support an internal restructuring and professional fees necessary to evaluate controls, systems and risk management. The increase in expenses was also due to the New York franchise tax liability.

The following ratios, applicable to the accident and health business of the Company, have been extracted from Schedule H of the Company's filed annual statements for each of the indicated years:

	2007	2008	2009
Premiums earned	100.0%	100.0%	100.0%
Incurred losses	65.69%	65.23%	61.93%
Commissions	12.22%	14.21%	14.79%
Expenses	18.55%	17.94%	20.69%
	96.46%	97.38%	97.41%
Underwriting results	3.54%	2.62%	2.59%

5. FINANCIAL STATEMENTS

The following statements show the assets, liabilities, capital and surplus as of December 31, 2009, as contained in the Company's 2009 filed annual statement, a condensed summary of operations and a reconciliation of the capital and 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 Company's financial condition as presented in its financial statements contained in the December 31, 2009 filed annual statement.

A. Independent Accountants

The firm of Ernst & Young was retained by the Company to audit the Company's combined statutory basis statements of financial position of the Company as of December 31st of each year in the examination period, and the related statutory-basis statements of operations, capital and surplus, and cash flows for the year then ended.

Ernst & Young concluded that the statutory financial statements presented fairly, in all material respects, the financial position of the Company at the respective audit dates. Balances reported in these audited financial statements were reconciled to the corresponding years' annual statements with no discrepancies noted.

B. Net Admitted Assets

Bonds	$77,124,907
Cash, cash equivalents and short term investments	3,429,034
Investment income due and accrued	712,137
Premiums and considerations:	
Uncollected premiums and agents' balances in the course of collection	9,514,189
Reinsurance:	
Amounts recoverable from reinsurers	30,243
Net deferred tax asset	1,249,875
Electronic data processing equipment and software	162,409
Receivables from parent, subsidiaries and affiliates	890,000
Exchange	348,454
Total admitted assets	$93,461,248

C. Liabilities, Capital and Surplus

Aggregate reserve for accident and health contracts	$23,611,617
Contract claims:	
Life	65,000
Accident and health	10,003,332
Premiums and annuity considerations for life and accident and health contracts received in advance	2,783,914
Contract liabilities not included elsewhere:	
Provision for experience rating refunds	1,567,236
Other amounts payable on reinsurance	24,382
Interest maintenance reserve	172,149
Commissions to agents due or accrued	4,071,658
General expenses due or accrued	2,268,876
Taxes, licenses and fees due or accrued, excluding federal income taxes	(488,861)
Current federal and foreign income taxes	809,595
Amounts withheld or retained by company as agent or trustee	170,211
Dividends to stockholders declared and unpaid	2,800,000
Accrual for return premiums	3,591,449
Total liabilities	$51,450,558
Common capital stock	$ 2,000,000
Deferred compensation	(498,493)
Gross paid in and contributed surplus	6,006,228
Special assigned surplus	1,000,000
Unassigned funds (surplus)	33,502,955
Surplus	$40,010,690
Total capital and surplus	$42,010,690
Total liabilities, capital and surplus	$93,461,248

D. Condensed Summary of Operations

	2007	2008	2009
Premiums and considerations	$79,493,651	$83,716,816	$95,329,524
Investment income	3,762,570	3,348,824	3,471,760
Miscellaneous income	167,237	393,591	342,801
Total income	$83,423,458	$87,459,231	$99,144,085
Benefit payments	$52,047,289	$55,173,509	$57,977,166
Increase in reserves	1,983,001	(732,685)	1,755,551
Commissions	10,128,081	11,925,925	13,804,407
General expenses and taxes	15,223,164	14,961,829	19,230,584
Total deductions	$79,381,535	$81,328,578	$92,767,708
Net gain (loss)	$ 4,041,923	$ 6,130,653	$ 6,376,377
Federal and foreign income taxes incurred	(812,892)	(2,014,705)	3,868,218
Net gain (loss) from operations before net realized capital gains	$ 4,854,815	$ 8,145,358	$ 2,508,159
Net realized capital gains (losses)	4,100	(407,200)	(149,603)
Net income	$ 4,858,915	$ 7,738,158	$ 2,358,556

E. Capital and Surplus Account

	2007	2008	2009
Capital and surplus, December 31, prior year	$32,509,992	$35,512,195	$42,849,555
Net income	$ 4,858,915	$ 7,738,158	$ 2,358,556
Change in net unrealized capital gains (losses)	50,714	(62,029)	(243,539)
Change in net deferred income tax	(2,195,717)	(1,066,708)	2,188,260
Change in non-admitted assets and related items	(627,229)	2,339,352	(4,913,169)
Change in asset valuation reserve	(9,718)	205,438	0
Cumulative effect of changes in accounting principles	0	0	2,257,065
Surplus adjustments:			
Paid in	320,916	90,832	194,480
Dividends to stockholders	0	(1,400,000)	(2,800,000)
Aggregate write ins for gains and losses in surplus	604,322	(507,683)	119,482
Net change in capital and surplus for the year	$ 3,002,203	$ 7,337,360	$ (838,865)
Capital and surplus, December 31, current year	$35,512,195	$42,849,555	$42,010,690

The changes in the net deferred income tax during the exam period are primarily due to temporary differences related to the deductibility of premiums refunded and the reserve for the unemployed sick.

6. DISASTER RECOVERY AND BUSINESS CONTINUITY PLANS

The Company's disaster recovery plan indicated that the Company moved its disaster recovery facilities from 75 Greenery Avenue in Chappaqua, New York to 1 Penn Plaza, New York, New York in 2005, then subsequently relocated the site to 7 Penn Plaza in January 2007. The Company indicated that tests of the disaster recovery plan were conducted during the examination period but the Company did not maintain documentation of all tests performed so that the examiner could verify the results and sufficiency of the testing. In addition, the examiner’s review of the Company’s business continuity plan for all locations revealed that the Company last tested this plan in May 2008 and did not maintain any documentation of the tests performed.

The examiner recommends that the Company record and maintain all documentation related to the testing of their disaster recovery and business continuity plans. This recommendation appeared in the prior report on examination.

7. FRAUD REPORTS, FRAUD PREVENTION PLAN AND SPECIAL INVESTIGATION UNIT

Section 405(a) of the New York Insurance Law states, in part:

> “Any person licensed or registered pursuant to the provisions of this chapter, and any person engaged in the business of insurance . . . who has reason to believe that an insurance transaction . . . may be fraudulent, or has knowledge that a fraudulent insurance transaction . . .is about to take place, or has taken place shall, within thirty days after determination by such person that the transaction appears to be fraudulent, send to the insurance frauds bureau on a form prescribed by the superintendent, the information requested by the form and such additional information relative to the factual circumstances of the transaction and the parties involved as the superintendent may require. . . .”

Section 409 of the New York Insurance Law states, in part:

> “(a) Every insurer writing . . . individual, group or blanket accident and health insurance policies issued or issued for delivery in this state . . . shall . . . file with the superintendent a plan for the detection, investigation and prevention of fraudulent insurance activities in this state and those fraudulent insurance activities affecting policies issued or issued for delivery in this state. . . .
>
> (b)(1) The plan shall provide the time and manner in which such plan shall be implemented, including provisions for a full-time special investigations unit and staffing levels within such unit. Such unit shall be separate from the

> underwriting or claims functions of an insurer, and shall be responsible for investigating information on or cases of suspected fraudulent activity and for effectively implementing fraud prevention and reduction activities pursuant to the plan filed with the superintendent. An insurer shall include in such plan staffing levels and allocations of resources in such full-time special investigations unit as may be necessary and appropriate for the proper implementation of the plan and approval of such plan pursuant to subsection (d) of this section."

The Company detected four suspicious transactions during the examination period and failed to report these transactions to the superintendent in accordance with Section 405(a) of the New York Insurance Law. In addition, the Company did not have an adequate Special Investigations Unit ("SIU") in place during the examination period. It is noted that subsequent to the examination the Company contracted with a vendor to establish an adequate SIU and has submitted a new Fraud Prevention Plan to the superintendent reflecting the changes to the SIU.

The examiner recommends that the Company report suspicious transactions to the superintendent in accordance with Section 405(a) of the New York Insurance Law and maintain an adequately staffed Special Investigations Unit in accordance with Section 409(b) of the New York Insurance Law.

8. PRIOR REPORT SUMMARY AND CONCLUSIONS

Following are the recommendations contained in the prior report on examination and the subsequent actions taken by the Company in response to each citation:

Item	Description
A	The examiner recommends that the Company record and maintain minutes for the Audit and Review Committee meetings, contemporaneously with the occurrence of the meetings, in the future.
	The Company now records and maintains minutes for the Audit and Review Committee meetings, contemporaneously with the occurrence of the meetings.
B	The examiner recommends that the Company record and maintain all documentation related to the testing of their disaster recovery plan.
	The Company failed to take corrective action in response to this recommendation. (See item 6 of this report)
C	The examiner recommends the Company test its business continuity plan for all locations periodically.
	The Company failed to take corrective action in response to this recommendation. (See item 6 of this report)

9. SUMMARY AND CONCLUSIONS

Following is the violations and recommendations contained in this report:

Item	Description	Page No(s).
A	The Company violated Section 4211(a) of the New York Insurance Law by failing to file a copy of the notice of election in the office of the superintendent at least ten days before the elections of certain directors.	7
B	The examiner recommends that the Company record and maintain all documentation related to the testing of their disaster recovery and business continuity plans. This recommendation appeared in the prior report on examination.	16
C	The examiner recommends that the Company report suspicious transactions to the superintendent in accordance with Section 405(a) of the New York Insurance Law and maintain an adequately staffed Special Investigations Unit in accordance with Section 409(b) of the New York Insurance Law.	17

Respectfully submitted,

/s/
Mark McLeod
Associate Insurance Examiner

STATE OF NEW YORK)
)SS:
COUNTY OF NEW YORK)

Mark McLeod, being duly sworn, deposes and says that the foregoing report, subscribed by him, is true to the best of his knowledge and belief.

/s/
Mark McLeod

Subscribed and sworn to before me

this__________ day of ____________________

APPOINTMENT NO. 30466

STATE OF NEW YORK

INSURANCE DEPARTMENT

I, JAMES J. WRYNN, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

MARK MCLEOD

as a proper person to examine into the affairs of the

FIRST REHABILITATION LIFE INSURANCE COMPANY OF AMERICA

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

COMPANY

with such other information as he shall deem requisite.

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

this 7th day of January, 2010

JAMES J. WRYNN
Superintendent of Insurance

Superintendent