REPORT ON EXAMINATION

OF THE

PREFERRED ASSURANCE COMPANY, INC.

AS OF

DECEMBER 31, 2007

DATE OF REPORT	**FEBRUARY 26, 2010**
EXAMINER	**JEFFREY USHER**

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

David Paterson
Governor

James J. Wrynn
Superintendent

February 26, 2010

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

Sir:

Pursuant to the provisions of the New York Insurance Law and acting in compliance with the instructions contained in Appointment Number 22770, dated June 1, 2009, attached hereto, I have made an examination into the financial condition and affairs of Preferred Assurance Company, Inc. (PAC), a not-for-profit corporation licensed pursuant to Article 43 of the New York Insurance Law. The following report thereon is respectfully submitted.

The examination was conducted at the home office of Preferred Assurance Company, Inc. located at 625 State Street, Schenectady, New York 12305.

Wherever the designations "the Plan" or "PAC" appear herein, without qualification, they should be understood to indicate Preferred Assurance Company, Inc.

1. SCOPE OF EXAMINATION

The previous examination of the Plan was conducted as of December 31, 2004. This examination covered the three-year period from January 1, 2005 through December 31, 2007. Transactions occurring subsequent to December 31, 2007 were reviewed where deemed appropriate by the examiner.

The examination comprised a verification of assets and liabilities as of December 31, 2007, in accordance with statutory accounting principles (SAP), as adopted by the Department, a review of income and disbursements deemed necessary to accomplish such verification, and utilized, to the extent considered appropriate, work performed by the Plan'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):

History of the Plan
Management and controls
Corporate records
Fidelity bonds and other insurance
Reinsurance
Territory and plan of operation
Growth of the Plan
Accounts and records
Loss experience
Financial statements

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

A review was also made to ascertain what action, if any, was taken by the Plan with regard to comments and recommendations contained within the prior report on examination.

2. DESCRIPTION OF THE PLAN

Preferred Assurance Company, Inc. was incorporated on June 2, 1992, pursuant to Section 402 of the New York Not-For-Profit Corporation Law. The Plan was licensed on August 6, 1992, to do business within New York State as a non-profit Health Service Corporation pursuant to the provisions of Article 43 of the New York Insurance Law. The Plan commenced operations in New York State in 1993.

The Plan is a membership corporation as defined within the New York Not-For-Profit Corporation Law. Pursuant to Article I of its by-laws, the Plan has one member only, MVPRT Holdings, Inc. (MVPRT). MVPRT is a holding company for three New York State and two New Hampshire regulated entities within the MVP Health Care, Inc. holding company system. Further details relative to MVPRT may be found in the "Holding Company System" section (2D) of this Report on Examination.

A. Management and Controls

The by-laws of the Plan provide for management to be vested in a board of directors consisting of not less than four directors.

As of December 31, 2007, the Plan's board of directors was comprised of seven (7) members as set forth below:

Name and Residence	Principal Business Affiliation
Provider Representative	
Michael Schneider, MD Rochester, New York	Physician, Rheumatology Associates of Rochester
Community Representatives	
Gary Bonadona Webster, New York	Director, Rochester Regional Joint Board, UNITE HERE, AFL-CIO, CLC
William Reddy Rochester, New York	Treasurer & Chief Operating Officer, Veterans' Outreach Center, Inc.
Michael Copeland Rochester, New York	Manager, Human Resources, Alstom Signaling, Inc.
Public Representatives	
Anthony M. Constanza Webster, New York	Retired
Wilfred J. Schrouder Penn Yan, New York	Retired
Gerald E. Van Strydonck Fairport, New York	Retired

The minutes of all meetings of the board of directors and committees thereof, held during the examination period, were reviewed. During the examination period, board meetings were generally well attended. All directors attended at least one-half of the meetings they were eligible to attend.

The Plan's principal salaried officers as of December 31, 2007 were as follows:

Name	Title
Dave Oliker	President and Chief Executive Officer
Thomas Combs	Executive Vice President and Chief Financial Officer
Denise Gonick	Executive Vice President and Chief Legal Officer

B. Territory and Plan of Operation

The Plan is licensed to do business throughout the state of New York, as a non-profit health service corporation, pursuant to the provisions of Article 43 of the New York Insurance Law. The Plan provides hospital, medical and other health services through indemnity contracts or preferred provider arrangements. Indemnity contracts are issued to small groups and individuals on a community rated basis and to large groups on an experience rated basis. Contracts providing managed care coverage, based on a preferred provider organization (PPO) are also offered.

During the examination period, PAC provided coverage for hospital, medical and other health services for the out-of-network component of Rochester Area Health Maintenance Organization Inc.'s (an affiliated health maintenance organization, licensed pursuant to Article 44 of the New York Public Health Law) point-of-service product in the Rochester metropolitan area. In addition, the Plan offered administrative service contracts (ASC), which provided indemnity or preferred provider benefits to certain large self-insured groups, who reimbursed the Plan for the cost of claims plus administrative charges.

The Plan commenced business in 1993 in both the Rochester and Albany areas. Contracts issued in the Rochester area consist mainly of a point-of-service indemnity contract that complements the basic benefit package offered by its affiliate, Rochester Area Health Maintenance Organization (RAHMO). The contract covers health maintenance organization subscribers who elect to seek services outside RAHMO's provider network. Although enrollment in the Rochester area was quite minimal in 2004, there has been a substantial increase in this business as evidenced by the following chart:

	2005	2006	2007
Net Premiums Written	$3,332,541	$3,984,682	$4,357,901

The increase in net premiums written noted above was primarily attributable to increased premium writings applicable to PAC's preferred provider option (PPO) product. PAC does not use any agents or brokers.

Starting in January 2008, the Plan began to aggressively market a new exclusive provider option (EPO) product and its preferred provider option (PPO) product (first offered in January, 2004). These products were not adequately priced and contributed to the Plan's insolvency, as initially reported in its filed June 30, 2008 quarterly statement. Further details are included within the "Subsequent Events" section (5) of this report.

C. Reinsurance

As of December 31, 2007, PAC's lines of business were covered pursuant to a reinsurance agreement between HCC Life Insurance Company (HCC Life), an authorized reinsurer, and RAHMO. The agreement covered eligible health care services provided under PAC's point-of-service policies as follows:

Lines of Business Covered	**Type of Cession**	**Limits**
Commercial EPO and PPO		
Eligible healthcare services (authorized reinsurer)	Excess of Loss	90% excess of $300,000 of loss per member. Maximum benefit payable per covered member, per policy year, is $2,000,000.

As of January 1, 2008, PAC entered into a separate reinsurance contract with HCC Life relative to PAC's commercial PPO and EPO products. This excess of loss reinsurance contract provided the same coverage as noted in the above schedule.

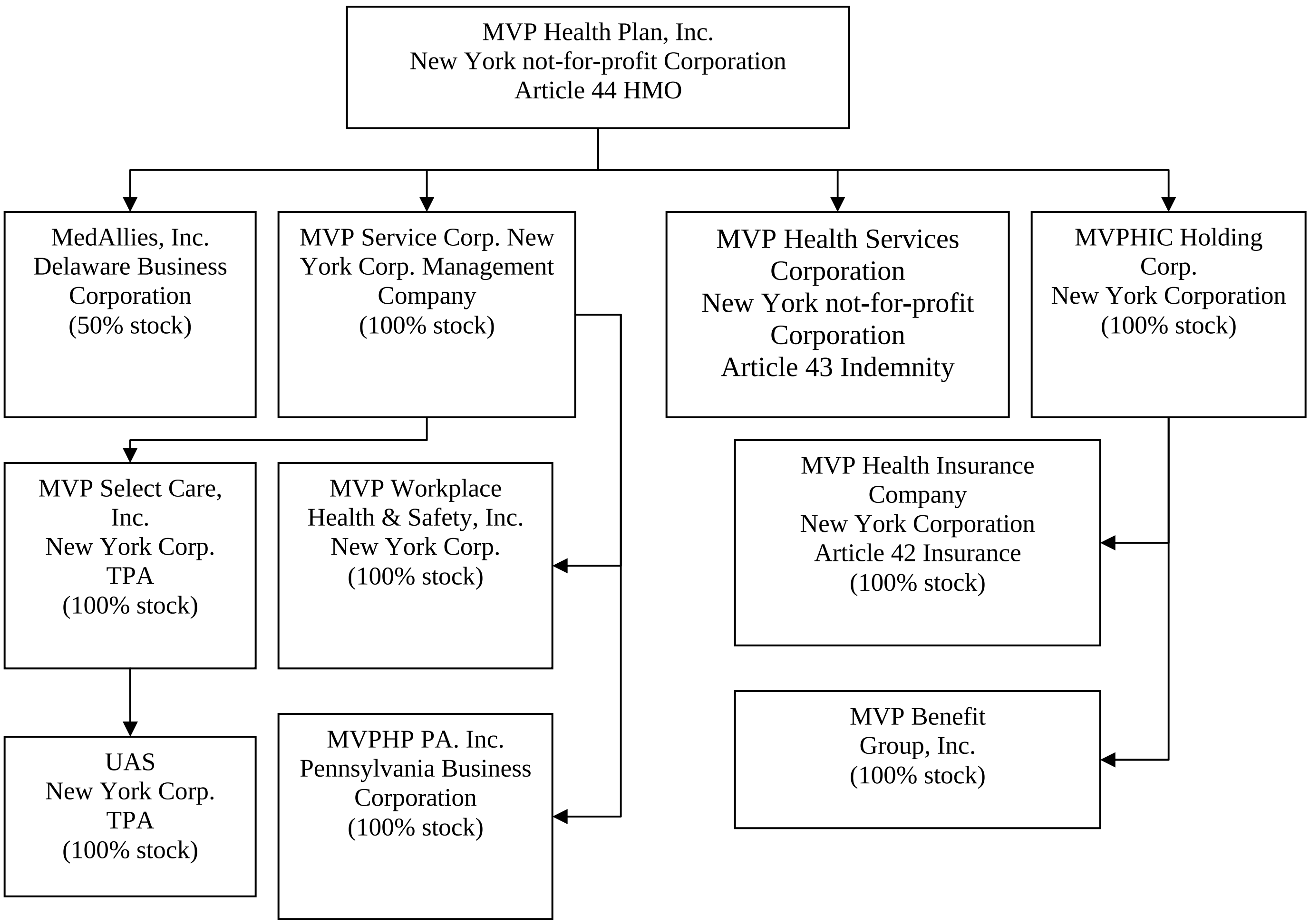
The above mentioned reinsurance agreement contained all of the required standard clauses, including the insolvency clause required by Section 1308 of the New York Insurance Law.

D. Holding Company System

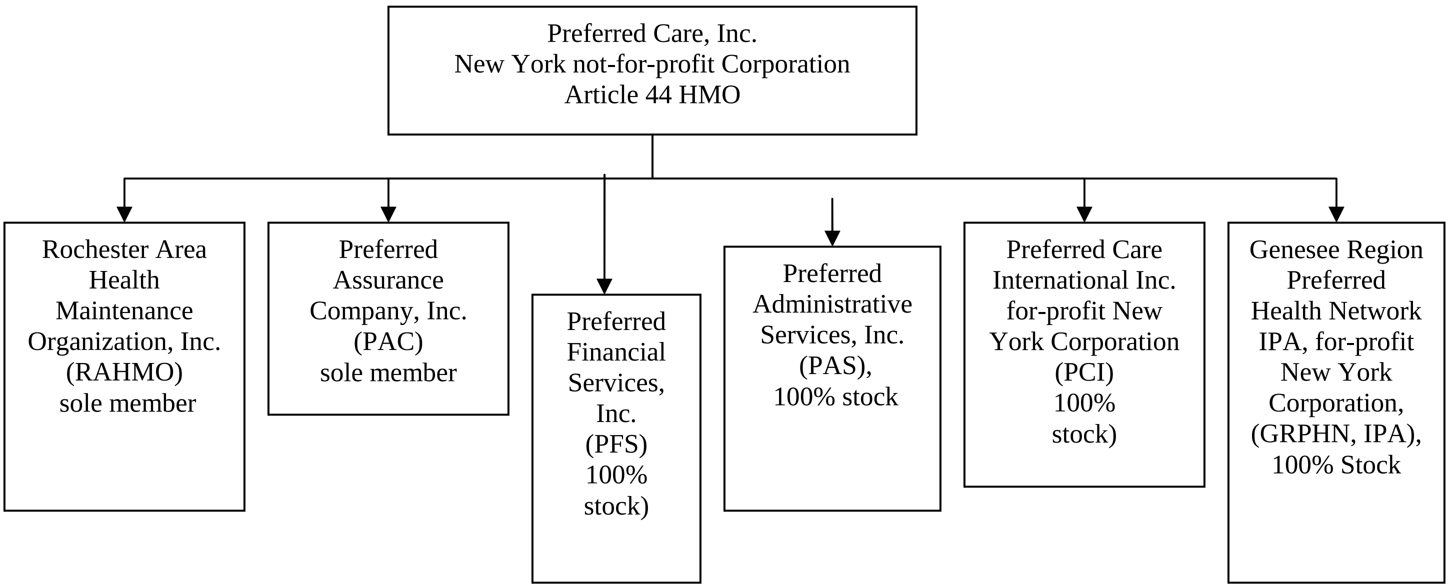
The Plan is a wholly-owned subsidiary of MVP Health Care, Inc. (Ultimate Parent). MVP Health Care, Inc. and its wholly-owned subsidiaries comprise an integrated health benefits insurance and health benefit management holding company system. On January 6, 2006, MVP Health Plan, Inc. (HMO), a tax-exempt New York State not-for-profit corporation licensed as a health maintenance organization to deliver healthcare services in New York and Vermont, combined with Preferred Care, Inc. (PC), a tax exempt New York State not-for-profit corporation.

Under the terms of the agreement and plan of reorganization by and between Preferred Care, Inc. and MVP Health Plan, Inc., the HMO and PC reorganized their respective enterprises under a holding company structure, with the ultimate holding company being MVP Health Care, Inc., which now serves as the direct or indirect parent company of all of the former PC, subsidiaries and of the HMO and all of its subsidiaries.

The following chart depicts the MVP Health Plan, Inc. holding company system prior to January 2006:



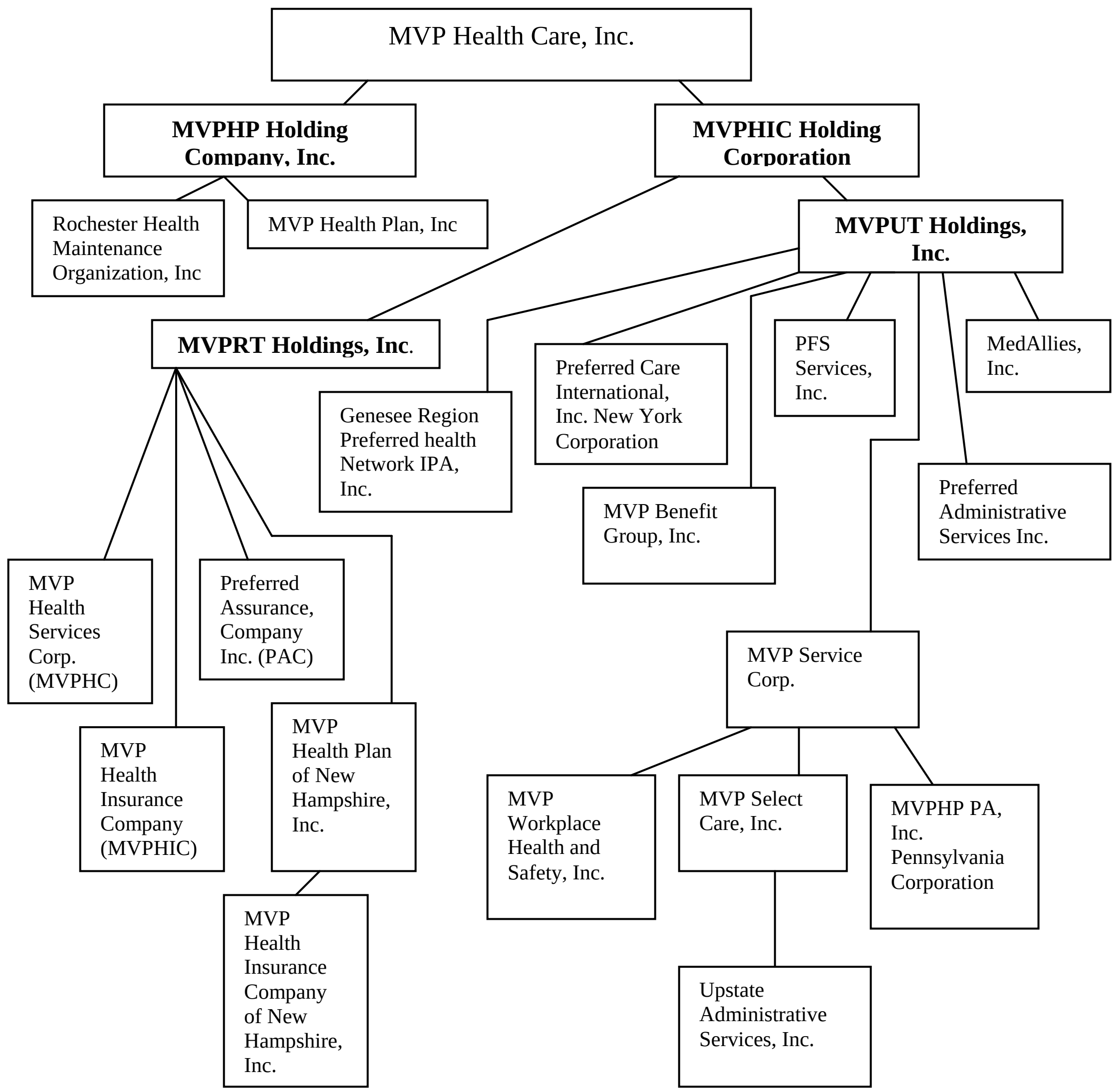
The following chart depicts the Preferred Care, Inc. holding company system prior to January 2006:



As a result of the reorganization of the corporate structure, Rochester Area Health Maintenance Organization, Inc. (RAHMO) and MVPHP became wholly-owned subsidiaries of MVPHP Holding Company, Inc., which in turn is a wholly-owned subsidiary of the ultimate parent, MVP Health Care, Inc.

MVP Health Service Corp., Preferred Assurance Co. Inc., and MVP Health Insurance Company are wholly-owned subsidiaries of MVPRT Holdings, Inc., which, in turn, is a wholly-owned subsidiary of MVPHIC Holding Corp. MVPHIC Holding Corp is a wholly owned subsidiary of the ultimate parent company, MVP Health Care, Inc.

The following is the organization chart of MVP Health Care, Inc. (Ultimate Parent) and its subsidiaries subsequent to January 2006 (and as of December 31, 2007):



Preferred Assurance Company, Inc.

Preferred Assurance Company, Inc. (PAC) is licensed to do business within New York State as a non-profit health service corporation pursuant to the provisions of Article 43 of the New York Insurance Law. During the examination period, PAC provided coverage for hospital, medical and other health services for the out-of-network component of RAHMO's point-of-service product in the Rochester metropolitan area and a PPO product. In 2008, PAC started marketing an EPO product. PAC is a subsidiary of MVPRT Holdings, Inc., which is a wholly-owned subsidiary of MVPHIC Holding Corp. MVPHIC Holding Corporation is a wholly-owned subsidiary of MVP Health Care, Inc.

PAC has entered into an administrative services agreement with its affiliate, MVP Service Corporation (MVPSC), wherein certain services are provided to PAC by MVPSC, including, but not limited to: financial, legal, internal operations, management information system, marketing, consulting, utilization review, claims administration, developing, revising and refining new health care products, systems, policies and overall administration.

MVPHP Holding Company, Inc.

MVPHP Holding Company, Inc. was formed on January 6, 2006, as a not-for-profit corporation; its ultimate parent is MVP Health Care, Inc. As a result of the restructuring that took place in 2006, MVPHP Holding Company, Inc. became the parent company of RAHMO and MVP Health Plan, Inc. As of December 31, 2007, the net worth of RAHMO and MVP Health Plan, Inc. was $183,334,542 and $138,719,155, respectively. MVPHP Holding Company, Inc., as of

December 31, 2007, had a consolidated net value of $322,053,697, which is the combined net worth of RAHMO and MVP Health Plan, Inc.

MVPHIC Holding Corporation

MVPHIC Holding Corporation was incorporated on November 22, 2000, pursuant to Section 402 of the New York Business Corporation Law. It was specifically formed to hold the stock of MVP Health Insurance Company (MVPHIC). MVPHIC is a for-profit accident and health insurance company licensed pursuant to Article 42 of the New York Insurance Law in the State of New York. MVPHIC Holding Corporation holds and controls 100% ownership of MVPRT Holdings, Inc. and MVPUT Holdings, Inc. MVP Health Care, Inc. in turn, owns and controls 100% of the stock of MVPHIC Holding Corp.

MVPHIC Holding Corporation controls five subsidiaries of MVPRT Holdings, Inc. Three of the five subsidiaries are regulated by the New York State Insurance Department as follows: MVP Health Services Corporation, Preferred Assurance Company, Inc., and MVP Health Insurance Company. As of December 31, 2007, MVPRT Holdings, Inc. and MVPUT Holdings, Inc. had a net value of $6,852,493 and $36,076,674, respectively. MVPHIC Holding Corporation valued its investments in MVPRT Holdings, Inc. and MVPUT Holdings, Inc. at $42,929,167 as of December 31, 2007, which is the combined value of MVPRT Holdings, Inc. and, MVPUT Holdings Inc.

The structure under reorganization included the addition of two holding company entities, MVPRT Holdings, Inc. (MVPRT) and MVPUT Holdings, Inc. (MVPUT). MVPRT consists of subsidiaries which are regulated by various Insurance and Health Departments (New York

Insurance and Health Departments, Vermont Department of Banking, Insurance, Securities & Health Care Administration and the New Hampshire Insurance Department). MVPRT Holdings, Inc. maintains 100% ownership of MVP Health Insurance Company (MVPHIC) and MVP Health Plan of New Hampshire and is the parent company of MVP Health Services Corporation (MVPHSC) and Preferred Assurance Corporation (PAC). MVPRT Holdings, Inc. is a wholly-owned subsidiary of MVPHIC Holding Corporation.

Rochester Area Health Maintenance Organization, Inc. (RAHMO)

RAHMO is a not-for-profit corporation operating as a federally qualified health maintenance organization under the provisions of Article 44 of the New York Public Health Law and Section 501(c)(4) of the Internal Revenue Code. RAHMO is exempt from federal income taxes on related income pursuant to Section 501(a) of the Internal Revenue Code. As of December 31, 2007, RAHMO is controlled by its sole member, MVPHP Holding Company, Inc., which is a wholly-owned subsidiary of MVP Health Care, Inc., the ultimate holding company. Preferred Care, Inc. was the sole member of RAHMO, prior to the merger with MVP Health Plan, Inc.

During the period July 1992 through July 1995, RAHMO provided funding to PAC by means of several New York Insurance Law Section 1307 loans. The total amount of the loans and accumulated accrued interest thereon were $7,998,461 and 7,096,000, respectively, as of December 31, 2007.

MVP Health Plan, Inc. (MVPHP)

MVPHP was incorporated on July 30, 1982, pursuant to Section 402 of the New York Not-For-Profit Corporation Law, for the purpose of operating as a health maintenance organization, as such term is defined in Article 44 of the New York Public Health Law. MVPHP which operates as an IPA model HMO, is also a federally qualified HMO.

MVP Health Services Corporation

MVP Health Services Corporation (MVPHSC) is a not-for-profit corporation, licensed pursuant to Article 43 of the New York Insurance Law. Currently, MVPHSC issues only indemnity dental insurance products. MVPHSC is a subsidiary of MVPRT Holdings, Inc., which is a wholly-owned subsidiary of MVPHIC Holding Corporation. MVPHIC Holding Corp. is a wholly-owned subsidiary of MVP Health Care, Inc.

MVP Health Insurance Company

MVP Health Insurance Company (MVPHIC) is a for-profit New York corporation, wholly-owned by MVPHIC Holding Corporation, which in turn is a wholly-owned subsidiary of MVP Health Care, Inc. MVPHIC was incorporated on April 24, 2000. MVPHIC received its license as an accident and health insurance company pursuant to Article 42 of the New York Insurance Law in June 2001. MVPHIC underwrites PPO, point-of-service (out-of-network) and indemnity only products for large and small groups.

MVP Service Corporation (MVPSC)

The HMO has a management services and consulting agreement with MVP Service Corporation, a company owned by MVPUT Holdings, Inc. MVP Service Corporation's employees perform all of the day to day operations of the HMO and MVPSC charges the HMO for its share of costs based on a contractual cost allocation methodology approved by this Department.

MVP Health Plan of New Hampshire, Inc.

MVP Health Plan of New Hampshire, Inc. (MVPHP NH) is a wholly-owned subsidiary of MVPRT Holdings, Inc., which in turn is a wholly-owned subsidiary of MVPHIC Holdings, Inc. MVPHP NH is the immediate parent of MVP Health Insurance Company of New Hampshire, Inc. These entities are domestic business corporations, incorporated under the New Hampshire revised statutes annotated (RSA) 293-A. MVPHP NH is licensed to operate as a health maintenance organization in the state of New Hampshire.

MVP Select Care, Inc.

MVP Select Care, Inc. (Select Care) is a for-profit New York corporation wholly-owned by MVP Service Corporation. Select Care was incorporated in 1987 to provide administrative services to companies that self-insure health care benefits.

MVP Select Care, Inc. owns 100% of Upstate Administrative Services (UAS), a New York corporation licensed as a third party administrator (TPA). UAS business was fully integrated into Select Care to achieve administrative service efficiencies.

On November 16, 1992, Select Care entered into an administrative services agreement with MVPSC, whereby MVPSC's employees provide for all the day-to-day operations of Select Care.

After the execution of the Agreement and Plan of Reorganization by and between Preferred Care, Inc. and MVP Health Plan, Inc., the ultimate parent funded the Greater Rochester Health Foundation (Foundation) pursuant to the New York Not-for-Profit Corporation Law for the purpose of promoting and improving the delivery, efficiency and quality of health services in the Rochester, New York region.

MVP Health Care, Inc. was funded from the proceeds of an $80,000,000 bank term loan (discussed below) and by cash transfers from the Rochester Area Health Maintenance Organization, Inc. in the amount of $107,000,000, from MVPHP in the amount of $30,000,000 and from Select Care in the amount of $13,500,000. MVP Health Care, Inc. subsequently funded the Foundation with a $200,000,000 cash payment. In addition, MVP Health Care, Inc. is required to contribute an additional amount to the Foundation in the amount of $26,639,000, which is payable on January 6, 2012 and bears interest at 3.5%. The additional contribution, plus interest, is expected to be funded by subsidiaries of MVP Health Care, Inc.

MVP Health Care, Inc. obtained a five-year $80,000,000 bank term loan for which some of the affiliated companies are guaranteeing repayment of the term loan. The term loan includes restrictive covenants, including: a fixed charge coverage ratio of 2.00 to 1.00 through December 31, 2007 and 2.25 to 1.00 thereafter; a leverage ratio not to exceed 1.75 to 1.00 for the combined company and a minimum total reserves ratio of not less than 1.50 to 1.00 for New York Public Health Law Article 44 subsidiaries (i.e., MVPHP and RAHMO). The subsidiaries of MVP Health Care, Inc. fund the debt service of the term loan. MVP Health Care, Inc. paid back the $80,000,000 term loan in full on November 2, 2007, without penalties.

E. Consolidated Tax Agreement

It was noted that after the reorganization MVP Health Care Inc., MVPHIC Holding Corporation and all of its subsidiaries, including the Plan, filed a 2007 consolidated federal corporate income tax filing. However, the Plan did not have a consolidated tax agreement in effect with MVPHIC Holding Corporation during the examination period.

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 thirty days prior thereto, or such shorter period as he may permit, and he has not disapproved it within such period:
>
> (4) any material transaction, specified by regulation, which the superintendent determines may adversely affect the interests of the insurer's policyholders or shareholders…"

New York Insurance Department Circular No. 33 (1979) states in part:

> "…every domestic insurer is directed to notify this Department within 60 days of this circular letter if it participates in a consolidated tax return and to submit a copy of its tax allocation agreement with such notification. Any domestic insurer which currently does not participate in a consolidated tax return shall file a copy of its tax allocation agreement with this Department within 30 days of electing to do so…"

Subsequent to the examination period, the Plan entered into a written consolidated tax agreement with MVPHIC Holding Corporation as required by Section 1505(d) of the New York Insurance Law. Such agreement was approved by this Department on January 8, 2010.

It is recommended that the Plan, in the future, comply with the requirements of Section 1505(d) of the New York Insurance Law and Department Circular Letter 33 (1979).

F. Significant Operating Ratios

The following ratio has been computed as of December 31, 2007, based upon the results of this examination:

Development of Unpaid Claims	(21)%

The above ratio is outside of the Department benchmark guideline of + / -10%. A review of PAC's reported one-year development of unpaid claims indicated a deficiency of $116,017 of PAC's 2006 unpaid claims reserves (21%).

The underwriting ratios presented below are on an earned-incurred basis and encompass the three-year (January 1, 2005 to December 31, 2007) period covered by this examination:

	Amount	Ratio
Claims incurred	$ 8,937,686	77%
Claims adjustment expenses incurred	167,203	1%
Other underwriting expenses incurred	1,331,335	11%
Net underwriting gain	1,238,901	11%
Premiums earned	$11,675,125	100.0%

G. Allocation of Expenses

As of December 31, 2007, the Plan entered into a cost sharing agreement with several affiliated companies. The Plan's portion of shared costs was determined using a cost allocation worksheet which uses various drivers to calculate the percentage of cost that is allocated to the participating companies. Examples of such drivers included the number of groups (statistical driver) and corporate projects (judgmental driver).

The examination review revealed that the Plan's costs are charged to various cost centers. A review of the definitions and functions of the cost centers revealed that some of the cost centers have more than one function and the costs should have been allocated to more than one expense grouping (e.g., loss adjustment, general administrative and/or investment expenses as shown on the Underwriting and Investment Exhibit, "Part 3 – Analysis of Expenses"). The Plan elected to choose what it considered to be the most appropriate expense group, but did not separate these costs among the expense groupings.

Statement of Statutory Accounting Principles (SSAP) No. 70 of the NAIC Accounting Practices and Procedures Manual establishes prescribes the presentation and allocation of certain expenses of reporting entities, into general categories, and the apportionment of shared expenses between members of a group of entities.

SSAP No. 70 of the NAIC Accounting Practices and Procedures Manual states in part:

> "…It is necessary to allocate those expenses which may contain characteristics of more than one classification, which this statement will refer to as allocable expenses…
>
> Allocable expenses for health insurers shall be classified as claim adjustment expenses; general administrative expenses; or investment expenses which are netted against investment income on the Statement of Revenue and Expenses."

Part 107.3 of Department Regulation 30 (11 NYCRR 107.3) states in part:

> “The composition of each expense group shall be as follows:
>
> (a) *Investment expenses.* Investment expenses shall comprise all expenses incurred wholly or partially in connection with the investing of funds and the obtaining of investment income…
> (b) *Loss adjustment expenses.* Loss adjustment expenses shall comprise all expenses incurred wholly or partially in connection with the adjustment and recording of policy claims, including the totals of the operating expense classification, claim adjustment services…
>
> (c) *Acquisition, field supervision and collection expenses.*
> (1) Acquisition, field supervision and collection expenses shall comprise all expenses incurred wholly or partially in the following activities...
>
> …keeping general and detail records; paying and receiving; general clerical, secretarial, office maintenance, supervisory and executive work; and handling personnel, supplies, mail, etc...”

It is recommended that the Plan apply the guidelines included in SSAP No. 70 of the NAIC Accounting Practices and Procedures Manual and Part 107 of Department Regulation 30 (11 NYCRR 107.3) by revising and updating its expense allocation methodology to reflect an appropriate allocation among the proper annual statement expense groupings within the Underwriting & Investment Exhibit of the Plan's annual statement.

H. Abandoned Property Law

The Plan filed its abandoned property reports for each year within the examination period with the State of New York Comptroller’s Office in accordance with the requirements of the New York Abandoned Property Law. However, the Plan failed to publish the names and addresses of persons appearing as owners of the unclaimed property within such abandoned property reports in major newspapers pursuant to the requirement of Section 1316(3) of the New York Abandoned Property Law.

Section 1316(3) of the New York Abandoned Property Law states the following:

> "Within thirty days following the filing of the report of abandoned property with the comptroller pursuant to subdivision two of this section, the insurer shall cause to be published a list of such abandoned property in the same manner as that prescribed for life insurance companies by section seven hundred two of this chapter."

It is recommended that the Plan comply with the (publishing of) notice requirements of Section 1316(3) of the New York Abandoned Property Law.

3. FINANCIAL STATEMENTS

A. Balance Sheet

The following shows the Plan's assets, liabilities and surplus as determined by this examination as of December 31, 2007. This statement is the same as the balance sheet filed by the Plan.

	Examination	Plan
Assets		
Cash, cash equivalents and short-term investments	$1,951,564	$1,951,564
Investment income due and accrued	7,894	7,894
Uncollected premiums	98,571	98,571
Receivables from parent, subsidiaries and affiliates	294,226	294,226
Healthcare and other amounts receivable	182,601	182,601
Total assets	$2,534,856	$2,534,856
Liabilities		
Claims unpaid	$607,021	$607,021
Unpaid claims adjustment expenses	11,000	11,000
Premiums received in advance	39,559	39,559
General expenses due and accrued	733	733
Amounts due to parent, subsidiaries and affiliates	440,336	440,336
Total liabilities	$1,098,649	$1,098,649
Surplus		
Surplus notes	$ 7,998,461	$ 7,998,461
Statutory reserve	544,738	544,738
Unassigned funds (surplus)	(7,120,140)	(7,120,140)
Total surplus	$1,423,059	$1,423,059
Total liabilities and surplus	$2,521,708	$2,521,708

Note 1: The Internal Revenue Service has not conducted any audits of the income tax returns filed during the period under examination. The examiner is unaware of any potential exposure of the Plan to any tax assessments and no liability has been established herein relative to such contingency.

Note 2: No liability appears herein for a loan in the amount of $7,998,461 and interest thereon in the amount of $7,096,000. The loan was granted pursuant to the provisions of Section 1307 of the New York Insurance Law. As provided in Section 1307, repayment of principal and interest shall only be made out of free and divisible surplus, subject to the prior approval of the Superintendent of Insurance of the State of New York.

B. Statement of Revenue and Expenses

Capital and surplus increased $1,063,744 during the period under examination, January 1, 2005 through December 31, 2007, detailed as follows:

Revenue		
Net premium income	$ 11,675,124	
Net investment income	132,530	
Net realized capital gain	6,633	
Total revenue		$ 11,814,286
Expenses		
Hospital and medical benefits	$ 7,448,758	
Prescription drugs	1,259,014	
Other hospital and medical benefits	229,914	
Claim adjustment expenses	167,203	
General administrative expenses	1,331,335	
Total expenses		10,436,224
Net income before federal income taxes		$ 1,378,063
Federal and foreign income taxes incurred		11,000
Net income		$ 1,367,063

Change in Capital and Surplus

	Gains in Surplus	Losses in Surplus	
Capital and surplus per report on examination as of December 31, 2004			$ 359,315
Net income	$1,367,063	$	
Change in non-admitted assets	896,681		
Aggregate write-ins for losses in surplus		1,200,000	
Net increase in surplus			1,063,744
Capital and surplus per report on examination as of December 31, 2007			$1,423,059

4. CLAIMS UNPAID

The examination liability of $607,021 for the above captioned account is the same as the amount reported by the Plan in its filed annual statement as of December 31, 2007.

The examination analysis of the claims unpaid reserve was conducted in accordance with generally accepted actuarial principles and practices and was based on statistical information contained in the Plan's internal records and its filed annual statements as verified during the examination. The examination reserve was based upon actual payments made through a point in time, plus an estimate for claims remaining unpaid at that date. Such estimate was calculated based on actuarial principles, which utilized the Plan's experience in projecting the ultimate cost of claims incurred on or prior to December 31, 2007.

5. SUBSEQUENT EVENTS

In its June 30, 2008 filed quarterly statement to the Superintendent of Insurance, it was revealed that PAC was insolvent in the amount of $(3,241,215). The insolvency grew to $(17,967,951) as of September 30, 2008. PAC's losses in 2008 were mainly due to erroneous pricing assumptions for its EPO and PPO products. The resulting low premium rates caused a growth in membership from approximately 1,000 members reported at December 31, 2007, to approximately 25,000 members reported at September 30, 2008.

Management indicated that in 2007, RAHMO experienced membership losses to its principal Rochester area competitor's EPO offering. RAHMO's management responded with competitive PPO and EPO products developed and offered to employer groups by its affiliate, PAC. Assumptions were made relative to medical utilization that proved to be lower than the actual medical trend for those groups which purchased the products and resulted in significant under-pricing and underwriting losses on the part of PAC for its PPO and EPO products in the amounts of approximately $17M and $5.7M, respectively, for 2008.

In order to remedy PAC's reported insolvency of $17,967,951 as of September 30, 2008, and to provide sufficient funds so that PAC's statutory surplus requirements were met, RAHMO proposed to transfer $30,000,000 to its parent, MVPHP Holding Company, Inc. The $30,000,000 would then be transferred to MVP Health Care Inc., the Ultimate Parent of both PAC and RAHMO. The Ultimate Parent would then transfer the $30,000,000 down to PAC.

On November 7, 2008, the New York Insurance Department, based on the review of RAHMO's financial condition as reported in the June 30, 2008 quarterly statement, approved

RAHMO's request to transfer $30,000,000 to MVPHP Holding Company, Inc. under the condition that the additional proposed transfers within the holding company system occur immediately, resulting in PAC's receipt of a $30,000,000 infusion of funds. Additionally, on November14, 2008, RAHMO received an approval from the New York Department of Health for the same $30,000,000 transfer.

On November 19, 2008, RAHMO transferred the $30,000,000 through the holding company as detailed above. PAC received the $30,000,000 on the same day which caused PAC to no longer be insolvent, or impaired.

Since the premium rates charged that gave rise to the substantial losses were inadequate, the New York Insurance Department directed PAC to submit an application for a premium rate increase, which became effective January 1, 2009.

As noted previously in this report, during the period July 1992 through July 1995, RAHMO provided funding to PAC by means of several New York Insurance Law Section 1307 loan agreements. The total amount of the loans and accumulated accrued interest were $7,998,461 and $7,096,000, respectively, as of December 31, 2007.

In a letter to this Department dated October 22, 2008, RAHMO requested approval to forgive all the principal and interest of the Section 1307 loans that it had with PAC. On November 8, 2008, this Department advised RAHMO that the Department had no objection to the forgiveness of these loans and their respective interest. On November 10, 2008, RAHMO's board of directors approved the forgiveness of the Section 1307 loans and interest it made to PAC.

6. COMPLIANCE WITH PRIOR REPORT ON EXAMINATION

The prior report on examination as of December 31, 2004, contained five (5) comments and recommendations. The comments and recommendations of the financial condition examination and the information systems review are detailed as follows (page numbers refer to the prior reports):

ITEM NO.		PAGE NO.
	Board of Directors	
1.	It is once again recommended that the Plan set up a system of staggered terms for its directors. The Plan has complied with this recommendation.	4
2.	It is recommended that the Plan restructure its board of directors so that its public and member representatives are composed in equal number in compliance with Section 4301(k)(1)(A) and (B) of the New York Insurance Law. The Plan has complied with this recommendation.	6
	Evergreen Clauses	
3.	It is recommended that the Plan refrain from entering into contracts with its officers that contain evergreen clauses that are in violation of Section 4312(b) of the New York Insurance Law. The Plan has complied with this recommendation.	11
	Reinsurance	
4.	It is recommended that PAC amend its reinsurance contract with Zurich American Insurance Company to include the wording prescribed by Section 1308(a)(2)(A)(i) of the New York Insurance Law. The Plan has complied with this recommendation.	14

ITEM NO.		PAGE NO.
	Administrative Services Agreement	
5.	It is recommended that PAC comply with the requirements of Section 1505(d) of the New York Insurance Law and act to obtain approval from the Superintendent of Insurance relative to its administrative services agreement with RAHMO. The Plan has complied with this recommendation.	18

7. SUMMARY OF COMMENTS AND RECOMMENDATIONS

ITEM		**PAGE NO.**
A.	Consolidated Tax Agreement	
	It is recommended that the Plan, in the future, comply with the requirements of Section 1505(d) of the New York Insurance Law and Department Circular Letter 33 (1979).	18
B.	Allocation of Expenses	
	It is recommended that the Plan apply the guidelines included in SSAP No. 70 of the NAIC Accounting Practices and Procedures Manual and Part 107 of Department Regulation 30 (11 NYCRR 107.3) by revising and updating its expense allocation methodology to reflect an appropriate allocation among the proper annual statement expense groupings within the Underwriting & Investment Exhibit of the Plan's annual statement.	21
C.	Abandoned Property Law	
	It is recommended that the Plan comply with the (publishing of) notice requirements of Section 1316(3) of the New York Abandoned Property Law.	22

Appointment No. <u>22770</u>

STATE OF NEW YORK
INSURANCE DEPARTMENT

I, **<u>ERIC R. DINALLO</u>**, Superintendent of Insurance of the State of New York, pursuant to the provisions of the Insurance Law, do hereby appoint:

Jeffrey Usher

as a proper person to examine into the affairs of the

Preferred Assurance Company, Inc.

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 this Department, at the City of New York.

this <u>1st</u> day of <u>June</u>, 2009

Eric R. Dinallo
Superintendent of Insurance