

Examination Warrant Number 16-1324-15451-R1

Report of Examination of

**UPMC Health Coverage, Inc.
Pittsburgh, Pennsylvania**

As of December 31, 2016

For Informational Purposes Only

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Harrisburg, Pennsylvania
April 19, 2018

Honorable Joseph DiMemmo, CPA
Deputy Insurance Commissioner
Commonwealth of Pennsylvania
Insurance Department
Harrisburg, Pennsylvania

Dear Sir:

In accordance with instructions contained in Examination Warrant Number 16-1324-15451-R1, dated August 4, 2016, an examination was made of

UPMC Health Coverage, Inc., NAIC Code: 15451

a Pennsylvania domiciled, single-state Health Maintenance Organization (“HMO”), hereinafter referred to as the “Company.” The examination was conducted at the Company’s home office, located at 600 Grant Street, Pittsburgh, Pennsylvania 15219.

A report of this examination is hereby respectfully submitted.

SCOPE OF EXAMINATION

The Pennsylvania Insurance Department (“Department”) has performed an examination of the Company, which was last examined as of February 28, 2014. The prior examination was an organizational examination to determine compliance with 40 P.S. § 1555.1(b). As a result of the examination, a Certificate of Authority was granted by the Department. This examination covered the period from March 1, 2014 through December 31, 2016.

Work programs employed in the performance of this examination were designed to comply with the standards promulgated by the Department and the National Association of Insurance Commissioners (“NAIC”) *Financial Condition Examiners Handbook* (“Handbook”).

The Handbook requires that the Department plan and perform the examination to evaluate the financial condition, assess corporate governance, identify current and prospective risks of the Company, evaluate system controls and procedures used to mitigate those risks, and review subsequent events. An examination also includes identifying and evaluating significant risks that could cause an insurer’s surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made by management and evaluating management’s compliance with statutory accounting principles.

The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination an adjustment is identified, the impact of such adjustment will be documented separately following the Company’s financial statements.

This examination report includes significant findings of fact, in accordance with 40 P.S. § 323.5(a), and general information about the Company and its financial condition. There may be

other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), are not included within the examination report but separately communicated to other regulators and/or the Company.

For each year during the period under examination, the certified public accounting firm of Ernst & Young, LLP (“CPA”) has provided an unmodified audit opinion on the Company’s year-end financial statements based on statutory accounting principles. Relevant work performed by the CPA, during its annual audit of the Company, was reviewed during the examination and incorporated into the examination workpapers.

The following Pennsylvania domestic affiliated insurance companies from the University of Pittsburgh Medical Center (“UPMC”) Group were examined at the same time with this examination:

<u>Company</u>	<u>NAIC Code</u>
UPMC Health Network, Inc.	11994
UPMC For You, Inc.	11995
UPMC Health Options, Inc.	15345
Community Care Behavioral Health Organization	47024
UPMC Health Plan, Inc.	95216
UPMC Health Benefits, Inc.	11018
UPMC Work Alliance, Inc.	14485
Tri-Century Insurance Company	17990

HISTORY

The Company was incorporated on May 15, 2013, licensed by the Department on April 28, 2014, and commenced business on August 1, 2014.

UPMC Coverage Products, Inc., a Pennsylvania business corporation, is the sole Member and incorporator of the Company.

The Company is currently authorized to transact those classes of insurance described in 40 P.S. § 1554 as an HMO.

MANAGEMENT AND CONTROL

CAPITALIZATION

As of the examination date, December 31, 2016, the Company’s total capital and surplus was \$10,854,300, consisting of \$1,500,000 gross paid in and contributed surplus and \$9,354,300 unassigned funds (surplus).

The Company’s minimum net worth requirement for the type of business for which it is licensed pursuant to 31 Pa. Code § 301.121(b)(2) is equal to the greater of \$1,000,000 or three months of uncovered health care expenditures for Pennsylvania enrollees. Accordingly, the

Company's required minimum net worth as of December 31, 2016 is \$1,000,000. The Company meets this requirement.

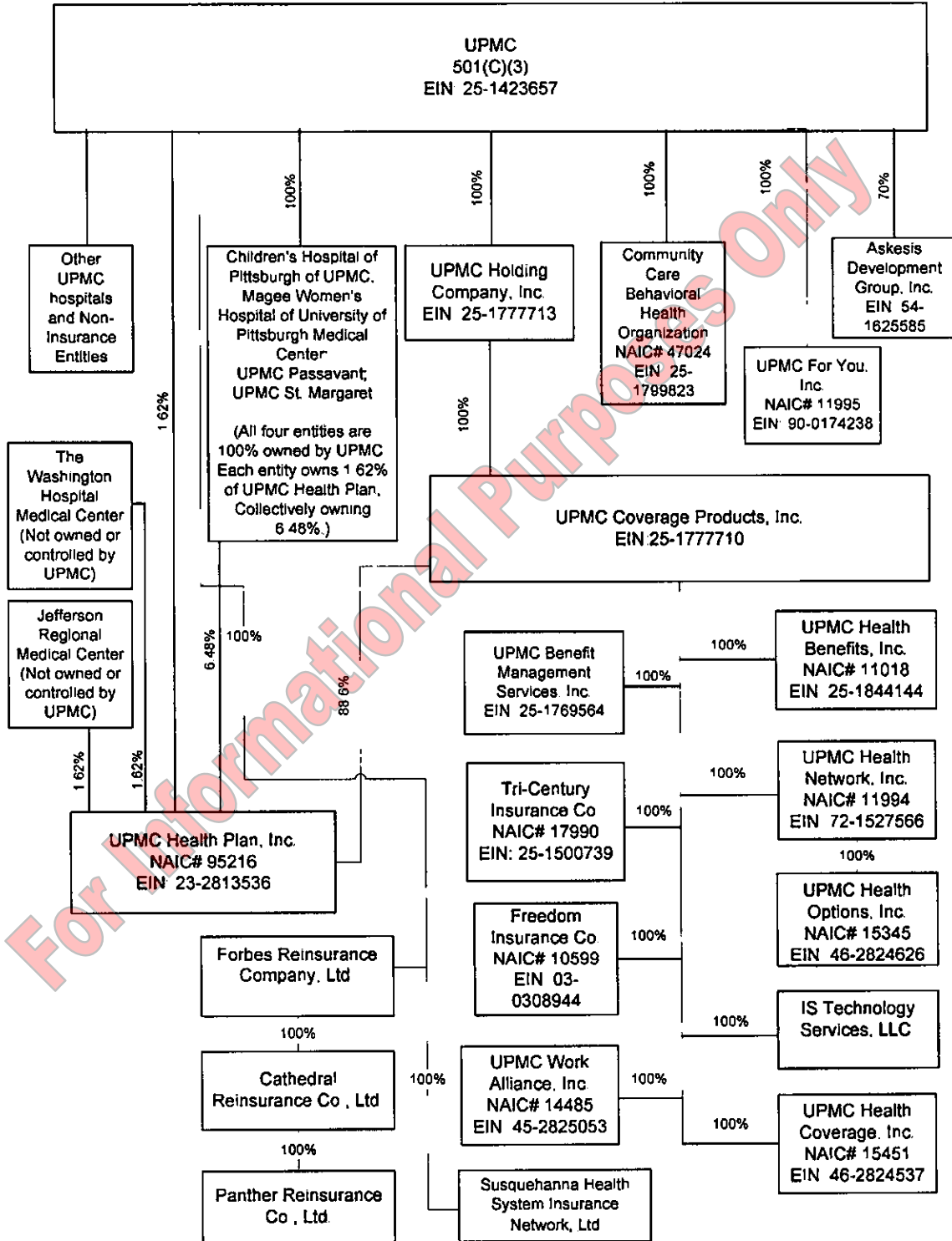
INSURANCE HOLDING COMPANY SYSTEM

The Company meets the requirements for filing an insurance holding company system annual registration statement ("Annual Registration Statement"), in compliance with 40 P.S. § 991.1404. The Company has filed the Annual Registration Statement and various amendments for all years of the examination period.

UPMC, a 501(c)(3) non-profit corporation is named as the ultimate controlling person in the system. The following abridged organizational chart depicts the Company's relationship within the UPMC holding company system at December 31, 2016:

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UPMC & Subsidiaries Organizational Structure



BOARD OF DIRECTORS

Management of the Company is vested in its Board of Directors (“Board”), which was comprised of the following members as of the examination date, December 31, 2016:

Name and Address	Principal Occupation
Diane Patricia Holder Pittsburgh, Pennsylvania	Chief Executive Officer UPMC Health Plan
Mark Laskow Stahlstown, Pennsylvania	Managing Director Greycourt & Company, Inc.
Robin Onder Newham Pittsburgh, Pennsylvania	Teacher and Head of School The Ellis School

The Company’s By-Laws provides that the number of voting directors of the Company shall consist of no less than three (3) nor more than twenty-one (21) members. At least one-third of the Board of Directors shall be Subscriber Directors. At least one-third of the Board of Directors shall be Outside Directors. Subscriber Directors may also serve as Outside Directors. The Directors shall be appointed annually by the Member and shall serve until their successors have been duly appointed and qualified or until a Director's earlier death, resignation, or removal.

The Company has a conflict of interest policy and requires all employees and directors to complete a conflict of interest questionnaire on an annual basis.

COMMITTEES

As of the examination date, December 31, 2016, the following committees were appointed by the Board and serving in accordance with the Company’s By-Laws:

Finance, Audit & Compliance Committee

Mark Laskow, Chairman
Peter Eisenbrandt
Diane Holder
Scott Lammie
Gary Weinstein
George Nicholas Beckwith III
Richard Hamilton
George Huber
Robin Newham
Susan Shipley

Outside Director Committee

George Huber, Chairman
Jack Babich
Peter Eisenbrandt
Richard Hamilton
Lisa Pupo Lenihan
Robert Lovett, Esq.
Norman Mity
Robin Newham
Greg Scott
Susan Shipley
Gary Weinstein

OFFICERS

As of the examination date, December 31, 2016, the following officers were appointed and serving in accordance with the Company's By-Laws:

Name	Title
Diane Patricia Holder	Chief Executive Officer
Mark Laskow	Chairman of the Board
Gordon Gebbens	Chief Financial Officer
Sheryl Kashuba, Esq.	Secretary
Scott Miller Lammie	Treasurer

CORPORATE RECORDS

MINUTES

A compliance review of the corporate minutes revealed the following:

- All Board meetings held during the period under examination were held in compliance with the Company's By-Laws, and quorums were established at all such meetings.
- The Company's officers and members of the Board were appointed by the Member in compliance with the By-Laws.
- The Company's investment transactions and policy are approved by the Board or a committee thereof.

ARTICLES OF INCORPORATION

There were no changes or amendments made to the Company's Articles of Incorporation during the examination period.

BY-LAWS

The Company amended its By-Laws effective March 26, 2014. The Company amended Article VII, Committees, Section 7.1(b), to reduce the minimum number of directors from five (5) to three (3) of the Finance, Audit & Compliance Committee.

The Company did not notify the Department of By-Laws changes nor report the changes in the 2014 Annual Statement General Interrogatory.

It is recommended that all changes to By-Laws are provided to the Department and appropriately reported in the General Interrogatory, pursuant to NAIC Annual Statement Instructions.

SERVICE AND OPERATING AGREEMENTS

The Company is party to various service and operating agreements, including several external and intercompany agreements. The following significant agreements were in place during the examination period:

Administrative Services Agreement

The Company has an Administrative Services Agreement with UPMC Health Plan, Inc. (“Health Plan”), under which Health Plan provides services for the administration and management of the Company. Specifically, Health Plan, has agreed to provide the following services: sales and marketing; enrollment and eligibility; member services; accounting; finance; claims adjudication and payment; information systems; network development and administration; provider credentialing and re-credentialing; quality improvement; utilization management services; development services; and executive management and administration services. Health Plan is reimbursed for the actual costs of expenses that are directly attributable to the Company. For those costs that are attributable to all health plans for which Health Plan provides administration and management services, Health Plan receives reimbursement based upon the respective revenues of the companies.

Tax Allocation Agreement

The Company participates in a consolidated federal income tax allocation agreement (“Agreement”) with some of its affiliated companies, originally dated November 1, 2000 and effective as of July 1, 1999. The Agreement was amended on July 1, 2011 and July 1, 2013. The Agreement calls for the Company to file its federal income tax return as part of a consolidated return filed by UPMC Holding Company, Inc. and its subsidiaries. The Agreement between the companies provides for the allocation of income tax or income tax benefits based upon each company’s share of consolidated net income or loss.

REINSURANCE

CEDED

The Company did not have any significant ceded business during the period covered under this examination.

ASSUMED

On August 1, 2014, the Company entered into an Assumption Agreement with an affiliate, Health Plan, whereby the Company assumed all of Health Plan’s obligations and liabilities under certain Commercial HMO Products, whether such obligations arose prior to, on or after the effective date. All liabilities and obligations of Health Plan related to these products are now those of the Company.

The Company’s reinsurance contract meets the transfer of risk test. The contract contains the appropriate insolvency clause.

TERRITORY AND PLAN OF OPERATIONS

The Company is a non-profit organization that operates an HMO for Small Health Options Program and Exchange (both on and off Marketplace plans) and that provides HMO products to employer groups.

The following chart summarizes the Company's direct and assumed, ceded and net written premiums for the year 2016:

Line of Business	Direct and Assumed Premium	Ceded Premium	Net Premium	Percentage of Total
Comprehensive (hospital and medical)	\$ 26,884,848	\$ 49,687	\$ 26,835,161	100.0 %
Health subtotal	26,884,848	49,687	26,835,161	100.0 %
Totals	\$ 26,884,848	\$ 49,687	\$ 26,835,161	100.0 %

SIGNIFICANT OPERATING TRENDS

The following table indicates the growth of the Company during the period covered by this examination:

	2016	2015	2014
Admitted Assets	\$ 15,650,300	\$ 14,742,500	\$ 7,080,821
Liabilities	\$ 4,796,000	\$ 4,940,843	\$ 4,984,574
Capital and Surplus Funds	\$ 10,854,300	\$ 9,801,657	\$ 2,096,247
Net Premium Income	\$ 26,835,161	\$ 27,538,506	\$ 5,150,309
Benefits to Members	\$ 22,759,997	\$ 15,277,106	\$ 4,214,702
Net Investment Income	\$ 10,345	\$ (18,029)	\$ (4,323)
Net Income	\$ 1,039,627	\$ 7,730,735	\$ 596,247

PENDING LITIGATION

The Company and certain of the UPMC insurance companies are subject to litigation and arbitration arising in the normal course of business. A review of the legal representation letters from the Company's legal counsel, and outside attorneys, explaining all current litigation to which the Company is a party indicated that the Company is not a party to any material litigation or arbitration, and none of which will, in the opinion of management that the ultimate liability, if any, associated with the outcome of these matters have a material adverse effect on the Company's financial condition.

FINANCIAL STATEMENTS

The financial condition of the Company, as of December 31, 2016, and the results of its operations for the period under examination, are reflected in the following statements*:

Comparative Statement of Assets, Liabilities, Surplus and Other Funds;
Comparative Statement of Income;
Comparative Statement of Capital and Surplus;
Comparative Statement of Cash Flow

*Note: Some financials shown in this report may contain immaterial differences to those reported in the Company's filed Annual Statements due to rounding errors.

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Comparative Statement of Assets, Liabilities, Surplus and Other Funds As of December 31,

	2016	2015	2014
Bonds	\$ 100,125	\$ 100,228	\$ 0
Cash, cash equivalents and short-term investments	13,879,503	13,439,519	4,794,946
Subtotal, cash and invested assets	<u>13,979,628</u>	<u>13,539,748</u>	<u>4,794,946</u>
Investment income due and accrued	294	501	0
Premiums and considerations	1,171,402	837,691	480,515
Amounts recoverable from reinsurers	0	23,481	1,805,360
Other amounts receivable under reinsurance contracts	8,372	2,092	0
Net deferred tax asset	4,940	6,258	0
Health care and other amounts receivable	485,665	332,729	0
Total	<u>\$ 15,650,300</u>	<u>\$ 14,742,500</u>	<u>\$ 7,080,821</u>
Claims unpaid	\$ 1,706,103	\$ 1,933,557	\$ 2,970,725
Unpaid claims adjustment expenses	20,085	14,828	164,906
Aggregate health policy reserves	0	0	818,547
Premiums received in advance	1,143,430	655,565	312,809
General expenses due or accrued	170,496	214,410	197,780
Remittances and items not allocated	0	65,162	3,547
Amounts due to parent, subsidiaries and affiliates	1,755,886	2,057,321	516,260
Total liabilities	<u>4,796,000</u>	<u>4,940,843</u>	<u>4,984,574</u>
Gross paid in and contributed surplus	1,500,000	1,500,000	1,500,000
Unassigned funds (surplus)	9,354,300	8,301,657	596,247
Total capital and surplus	<u>10,854,300</u>	<u>9,801,657</u>	<u>2,096,247</u>
Totals	<u>\$ 15,650,300</u>	<u>\$ 14,742,500</u>	<u>\$ 7,080,821</u>

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Comparative Statement of Income For the Year Ended December 31,

	2016	2015	2014
Net premium income	\$ 26,835,161	\$ 27,538,506	\$ 5,150,309
Risk revenue	863,822	0	0
Aggregate write-ins for other non-health revenues	(2)	(53)	0
Total revenues	<u>27,698,981</u>	<u>27,538,452</u>	<u>5,150,309</u>
Hospital/medical benefits	13,447,446	8,967,364	2,372,592
Other professional services	3,055,231	2,237,423	594,251
Emergency room and out-of-area	1,015,424	668,347	66,028
Prescription drugs	5,241,896	3,403,972	1,181,831
Subtotal (hospital and medical)	<u>22,759,997</u>	<u>15,277,106</u>	<u>4,214,702</u>
Net reinsurance recoveries	(23,481)	544,356	1,805,360
Total hospital and medical	<u>22,783,478</u>	<u>14,732,750</u>	<u>2,409,342</u>
Claims adjustment expenses, including cost containment expenses	380,066	392,981	118,848
General administrative expenses	2,929,585	1,927,943	458,426
Increase in reserves for life accident and health contracts	0	(818,547)	818,547
Total underwriting deductions	<u>26,093,129</u>	<u>16,235,127</u>	<u>3,805,163</u>
Net underwriting gain or (loss)	<u>1,605,853</u>	<u>11,303,325</u>	<u>1,345,146</u>
Net investment income earned	10,345	(18,029)	(4,323)
Net investment gains or (losses)	10,345	(18,029)	(4,323)
Net income or (loss) before federal income taxes	<u>1,616,198</u>	<u>11,285,296</u>	<u>1,340,823</u>
Federal income taxes incurred	576,571	3,554,561	744,576
Net income (loss)	<u>\$ 1,039,627</u>	<u>\$ 7,730,735</u>	<u>\$ 596,247</u>

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**Comparative Statement of Capital and Surplus
For the Year Ended December 31,**

	2016	2015	2014
Capital and surplus, December 31, previous year	\$ 9,801,657	\$ 2,096,247	\$ 0
Net income or (loss)	1,039,627	7,730,735	596,247
Change in net unrealized capital gains and (losses)	0	576	0
Change in net deferred income tax	(1,425)	6,258	293,801
Change in nonadmitted assets	14,441	(32,160)	(293,801)
Surplus adjustments:			
Paid in	0	0	1,500,000
Net change in capital and surplus	1,052,643	7,705,410	2,096,247
Capital and surplus, December 31 current year	<u>\$ 10,854,300</u>	<u>\$ 9,801,657</u>	<u>\$ 2,096,247</u>

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Comparative Statement of Cash Flow For the Year Ended December 31,

	2016	2015	2014
Cash from Operations			
Premiums collected net of reinsurance	\$ 26,989,316	\$ 26,705,538	\$ 5,801,150
Net investment income	(33,260)	(1,832)	(4,323)
Miscellaneous income	857,540	(2,145)	0
Total	<u>27,813,596</u>	<u>26,701,560</u>	<u>5,796,827</u>
Benefit and loss related payments	23,125,945	13,534,381	2,062,524
Commissions, expenses paid and aggregate write-ins for deductions	3,304,393	2,471,002	214,567
Federal and foreign income taxes paid (recovered)	576,677	3,554,562	744,576
Total deductions	<u>27,007,015</u>	<u>19,559,945</u>	<u>3,021,687</u>
Net cash from operations	<u>806,581</u>	<u>7,141,615</u>	<u>2,775,140</u>
Cash from Investments			
Proceeds from investments sold, matured or repaid:			
Miscellaneous proceeds	0	577	0
Total investment proceeds	<u>0</u>	<u>577</u>	<u>0</u>
Cost of investments acquired (long-term only):			
Bonds	0	100,297	0
Total investments acquired	<u>0</u>	<u>100,297</u>	<u>0</u>
Net cash from investments	<u>0</u>	<u>(99,720)</u>	<u>0</u>
Cash from Financing and Miscellaneous Sources			
Cash provided (applied):			
Capital and paid in surplus, less treasury stock	0	0	1,500,000
Other cash provided or (applied)	(366,597)	1,602,677	519,807
Net cash from financing and miscellaneous sources	<u>(366,597)</u>	<u>1,602,677</u>	<u>2,019,807</u>
Reconciliation of cash and short-term investments:			
Net change in cash and short-term investments	439,984	8,644,573	4,794,946
Cash and short-term investments			
Beginning of the year	13,439,519	4,794,946	0
End of the year	<u>\$ 13,879,503</u>	<u>\$ 13,439,519</u>	<u>\$ 4,794,946</u>

SUMMARY OF EXAMINATION CHANGES

There were no changes made to the Company's financial statements as a result of this examination.

NOTES TO FINANCIAL STATEMENTS

ASSETS

INVESTMENTS

As of December 31, 2016, the Company's invested assets were distributed as follows:

	Amount	Percentage
Bonds	\$ 100,125	0.7 %
Cash	8,969,421	64.2 %
Short-term investments	4,910,081	35.1 %
Totals	<u>\$ 13,979,627</u>	<u>100.0 %</u>

The Company's bond and short-term investment portfolio had the following quality and maturity profiles:

NAIC Designation	Amount	Percentage
1 - highest quality	\$ 5,010,206	100.0 %
Totals	<u>\$ 5,010,206</u>	<u>100.0 %</u>

Years to Maturity	Amount	Percentage
1 year or less	\$ 4,910,081	98.0 %
2 to 5 years	100,125	2.0 %
Totals	<u>\$ 5,010,206</u>	<u>100.0 %</u>

The Company's investment portfolio is primarily comprised of cash and short-term investments, which represent 99.3% of the invested assets.

The quality of the Company's bond and short-term investments portfolio is 100.0% investment grade, with 100.0% having an NAIC designation of "1" highest quality.

The Company has a written investment policy as required by 40 P.S. § 504.1(c). The investment policy is reviewed and approved on at least an annual basis by the Board. The Company was following its investment policy at December 31, 2016.

The Company holds its investment portfolio under a non-discretionary custodial agreement with The Bank of New York Mellon, N.A. The examiners reviewed the Custodial Agreement and found it to be compliant with 31 Pa. Code § 148a.3.

LIABILITIES

POLICYHOLDER AND CLAIM RESERVES

The Company reported reserves for Claims Unpaid of \$1,706,103 and Unpaid Claims Adjustment Expenses of \$20,085 in its December 31, 2016 Annual Statement.

Timothy J. Feeser, FSA, MAAA, Vice President, Actuarial Consulting, of the firm of Optum, has served as the Company's appointed actuary for all years in the examination period. Mr. Feeser concluded the December 31, 2016 reserves make an adequate provision for the anticipated cash flows required by the contractual obligations and related expenses of the Company; the appointed actuary also opined that the December 31, 2016 reserves and related actuarial values:

- (a) Are computed in accordance with presently accepted actuarial standards consistently applied and are fairly stated in accordance with sound actuarial principles,
- (b) Are based on actuarial assumptions relevant to contract provisions and appropriate to the purpose for which the statement was prepared,
- (c) Meet the requirements of the Insurance Laws and regulations of the Commonwealth of Pennsylvania and are at least as great as the minimum aggregate amounts required by the state in which this statement is filed,
- (d) Make good and sufficient provision for all unpaid claims and other actuarial liabilities of the organization under the terms of its contracts and agreements,
- (e) Are computed on the basis of assumptions and methods consistent with those used in computing the corresponding items in the annual statement of the preceding year-end,
- (f) Include appropriate provision for all actuarial items that ought to be established.

Ernst & Young, LLP, the Company's independent auditor, performed separate, independent actuarial analyses of reserves as of December 31, 2016. Their analyses concluded that reserves were within acceptable ranges, and therefore, were fairly stated.

In conjunction with the examination, the Department utilized the actuarial services of Lewis & Ellis, Inc., who subcontracted through Cerebres, LLC, to assist in the review of the Company's actuarial reserving process, assumptions, methodologies, calculations and reserve adequacy as of the examination date. Based upon procedures performed and results obtained, no material deficiencies were identified in the reported actuarial reserves and related actuarial values.

The examination staff obtained sufficient evidence to support the conclusion that the Company's policyholder and claim reserves are reasonably stated as of December 31, 2016.

SUBSEQUENT EVENTS

On December 14, 2017, Michael L. Rasmussen, FSA, MAAA, Senior Director, Actuarial Consulting, of the firm of Optum, was appointed by the Board to serve as the appointed actuary, replacing Mr. Feeser, for several UPMC companies, including UPMC Health Coverage, Inc.

On July 13, 2017, the Company notified the Department that it has submitted a license application in the state of Maryland to operate as an HMO Organization, to comply with the Uniform Certificate of Authority Application requirements. As of the date of this examination report, the Department believes the expansion application is still pending.

RECOMMENDATIONS

PRIOR EXAMINATION

There were no recommendations made as a result of prior examination.

CURRENT EXAMINATION

As a result of the current examination, the following recommendation is being made:

1. It is recommended that all changes to By-Laws are provided to the Department and appropriately reported in the General Interrogatory, pursuant to NAIC Annual Statement Instructions. (See "Corporate Records – By-Laws" at page 6.)

CONCLUSION


As a result of this examination, the financial condition of UPMC Health Coverage, Inc., as of December 31, 2016, was determined to be as follows:

	Amount	Percentage
Admitted assets	\$ 15,650,300	100.0 %
Liabilities	\$ 4,796,000	30.6 %
Capital and Surplus	10,854,300	69.4 %
Total liabilities, capital and surplus	\$ 15,650,300	100.0 %

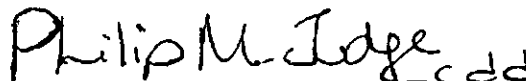
Since the previous examination, made as of February 28, 2014, the Company's assets increased by \$14,150,300, its liabilities increased by \$4,796,000, and its surplus increased by \$9,354,300.

This examination was conducted by examination staff from Cerebros, LLC, actuaries from Lewis & Ellis, Inc., Cornelius McConville, Ellamarie Durant, George Horey, CFE, Robert Smith, CFE, and David Jia, CFE, with the latter in charge.

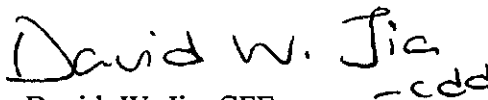
Respectfully,



Melissa L. Greiner
Director
Bureau of Financial Examinations



Philip M. Judge, CFE
Examination Manager



David W. Jia, CFE
Examiner-in-Charge