# REPORT ON EXAMINATION

# OF THE

# INDEPENDENCE AMERICAN INSURANCE COMPANY

# AS OF

# DECEMBER 31, 2012

Karen Weldin Stewart, CIR-ML
Commissioner

Delaware Department of Insurance

I, Karen Weldin Stewart, Insurance Commissioner of the State of Delaware, do hereby certify that the attached REPORT OF EXAMINATION, made as of December 31, 2012 of the

**INDEPENDENCE AMERICAN INSURANCE COMPANY**

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

Attest By: ______________________

Date: May 21, 2014

*In Witness Whereof*, I have hereunto set my hand and affixed the official seal of this Department at the City of Dover, this 21st day of May, 2014.

______________________

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

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Karen Weldin Stewart, CIR-ML
Commissioner

Delaware Department of Insurance

REPORT OF EXAMINATION

OF THE

INDEPENDENCE AMERICAN INSURANCE COMPANY

AS OF

DECEMBER 31, 2012

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

Consideration has been duly given to the comments, conclusions and recommendations of the examiners regarding the status of the company as reflected in the report.

This report is hereby accepted, adopted and filed as an official record of this Department.

Karen Weldin Stewart, CIR-ML
Insurance Commissioner

Dated this 21st day of May, 2014

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## SALUTATION

April 15, 2014

Honorable Karen Weldin Stewart, CIR-ML
Delaware Insurance Commissioner
Delaware Department of Insurance
Rodney Building
841 Silver Lake Blvd.
Dover, Delaware 19904

Dear Commissioner,

In compliance with instructions and pursuant to statutory provisions contained in Certificate of Authority No. 13.021, dated June 12, 2013, an examination has been made of the affairs, financial condition and management of the

**INDEPENDENCE AMERICAN INSURANCE COMPANY**

hereinafter referred to as “the Company” or “IAIC” and incorporated under the laws of the State of Delaware as a stock company. The Company’s registered office in the State of Delaware is located at 1013 Centre Road, New Castle, Delaware 19805-1297. The examination was conducted at the Company’s administrative offices located at 485 Madison Avenue, $14^{th}$ Floor, New York, New York 10022-5872.

The report of examination report thereon is respectfully submitted.

## SCOPE OF EXAMINATION

The last examination was completed as of December 31, 2008, by the Delaware Insurance Department. This examination covered the period of January 1, 2009 through December 31, 2012, and encompasses a general review of transactions during the period, the Company’s business policies and practices, as well as management and relevant corporate matters, with a determination of the financial condition of the Company at December 31, 2012. Transactions subsequent to the examination date were reviewed where deemed necessary.

We conducted our examination in accordance with the National Association of Insurance Commissioners (NAIC) *Financial Condition Examiners Handbook* (Handbook) and generally accepted statutory insurance examination standards consistent with the Insurance Laws and Regulations of the State of Delaware. The NAIC Handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the Company by obtaining information about the Company including corporate governance, identifying and assessing inherent risks within the Company and evaluating system controls and procedures used to mitigate those risks. The examination also included assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk focused examination process. The examination report addresses regulatory issues reviewed during the examination process.

During the course of this examination, consideration was given to work performed by the Company's external accounting firm, KPMG LLC. Certain auditor work papers of their 2012 audit have been incorporated into the work papers of the examiners and have been utilized in determining the scope, areas of emphasis in conducting the examination, and in the area of risk mitigation and substantive testing.

In addition to items noted in this report, the topics below were reviewed without material exception and are included in the work papers of this examination:

Fidelity Bonds and Other Insurance
Pensions, Stock Ownership and Insurance Plans
Statutory Deposits

## SUMMARY OF SIGNIFICANT FINDINGS

There were no material adverse findings, adjustments to the financial statements, or specific recommendations as a result of this examination.

## SUBSEQUENT EVENTS

IHC purchased 762,640 common shares of AMIC from unaffiliated tendering AMIC stockholders, pursuant to a tender offer commenced in September 2013. After the tender offer ended in October 2013, IHC owned 2,800,795 shares of AMIC, increasing its ownership percentage of AMIC from 24.64% (2,038,155 of 8,272,332 AMIC outstanding shares at December 31, 2012) to 34.70% (2,800,795 of 8,072,548 AMIC outstanding shares at October 8, 2013). When combined with MIC's ownership of 4,464,501 shares of AMIC, the combined ownership of AMIC by affiliates IHC and MIC aggregated 7,265,296 shares, or 90.00%, of the 8,072,548 outstanding AMIC shares at October 8, 2013.

## COMPANY HISTORY

The Company was incorporated in Delaware on February 26, 1973, as Pinnacle Insurance Company and commenced business on March 15, 1973. By agreement dated October 16, 1975, the Company was acquired by Geneve Holdings, Inc. (GHI) and has since remained within this holding company structure. On November 14, 2002, the Company's name was changed to Independence American Insurance Company.

## CORPORATE RECORDS

The minutes of the meetings of the Stockholders and Board of Directors, which were held during the period of examination, were read and noted. Attendance at meetings, election of directors and officers and approval of investment transactions were also noted.

Inspection of Company files indicated that an ethics statement/conflict of interest statement was completed by all employees for the examination period. A review of the Company's bylaws revealed that no changes were made during the examination period.

## MANAGEMENT AND CONTROL

### Directors

Pursuant to the General Corporation Laws of the State of Delaware, as implemented by the Company's Certificate of Incorporation and bylaws, all corporate powers and its business property and affairs are managed by, or under the direction of, its Board of Directors (Board). The Board shall consist of at least two members with a maximum of ten members.

The Board, at December 31, 2012, was comprised of four members, each elected or appointed in accordance with Company bylaws. Each Director shall hold office until his successor is elected and qualified, or until earlier resignation or removal.

The Board of Directors, duly elected in accordance with the Company's bylaws and serving at December 31, 2012, is as follows:

| Individual | Principal Business Affiliation |
|---|---|
| David Thomas Kettig | Standard Security Life Insurance Co. of New York |
| Gary John Balzofiore | Standard Security Life Insurance Co. of New York |
| Jeffrey C. Smedsrud | Standard Security Life Insurance Co. of New York |
| Adam Christian Vandervoort | Standard Security Life Insurance Co. of New York |

Officers

The bylaws of the Company state the principal officers shall be a President, one or more Vice-Presidents, a Secretary and a Treasurer. The Board may elect a Controller, one or more Assistant Secretaries, one or more Assistant Treasurers, one or more Assistant Controllers and such other officers as the Board from time to time may determine.

The officers shown on the annual statement jurat page, duly appointed in accordance with the bylaws and serving at December 31, 2012, were as follows:

| Individual | Office |
|---|---|
| David Thomas Kettig | President |
| Gary John Balzofiore | Senior Vice President, CFO & Treasurer |
| Adam Christian Vandervoort | Senior Vice President, General Counsel and Secretary |
| David Brian Getz | Vice President and Controller |
| Thomas Anthony Gibbons | Vice President and Chief Compliance Officer |

During our review for compliance with 18 Del. C. §4919, it was noted that the Company properly reported changes in directors and principal officers.

Committee Members

There were no standing committees of the Board of Directors for the period under examination.

Insurance Holding Company System

The Company is a member of an insurance holding company system as defined under Title 18, Chapter 50, “Insurance Holding Companies” of the Delaware Insurance Code. Based upon a review of information provided, the Company’s ownership structure at December 31, 2012, is as follows:

The Netter Family {1}, 100% owner
- Geneve Holdings, Inc., (DE), 100% owner of
  - Geneve Corporation (DE), 100% owner of
    - GHC Corp. (DE), 100% owner of Argent, SIC and SMH
      - Argent Investors Management Corporation (NY), 11.04% owner of IHC

SMH Associates Corp. (DE), 19.82% owner of IHC
SIC Securities Corp. (DE), 20.14% owner of IHC
Independence Holding Co. (DE) (IHC) {2}, 100% owner of
Independence Capital Corp. (DE), 100% owner of
Standard Security Life Ins. Co. of New York (NY) (SSLICNY)
Madison National Life Insurance Co., Inc. (WI) (MNLIC), 100% owner of
Madison Investors Corporation (DE) (MIC), 53.97% owner of
American Independence Corp. (DE) (AMIC) {3}, 100% owner of
Independence American Holdings Corp. (DE) (IAHC), 100% owner of
**Independence American Insurance Company (DE)**

{1} The Company disclosed on the 2012 annual statement, Schedule Y – Part 1, that the Netter family owns 100% of GHI. As in the prior exam, management did not provide the ownership breakdown of GHI among the individual Netter family members.

{2} Publicly traded under the ticker "IHC". According to publicly available documents filed with the SEC and with information provided by management, there were 17,932,954 outstanding voting common shares of IHC stock at December 31, 2012. Of these shares, Argent Investors Management Corporation owned 1,980,000 shares (11.04%), SIC Securities Corp. owned 3,610,859 shares (20.14%) and SMH Associates Corp. owned 3,554,367 shares (19.82%). Together, these three affiliates owned 9,145,226 shares (51.00%) of the IHC outstanding shares. No other individual entity or group owned or controlled greater than 10% of IHC at December 31, 2012.

{3} Publicly traded under the ticker "AMIC". According to publicly available documents filed with the SEC, there were 8,272,332 outstanding voting common shares of AMIC stock at December 31, 2012. Of these shares, Madison Investors Corporation owned 4,464,501 shares (53.97%) and Independence Holding Company owned 2,038,155 shares (24.64%). Together, these two affiliates owned 6,502,656 shares (78.61%) of the AMIC outstanding shares. No other individual entity or group owned or controlled greater than 10% of AMIC at December 31, 2012.

Based on the above calculations, the Netter family members "acting in concert" directly or indirectly own or control 40.09% of IAIC through their 100% ownership of GHI (100% times 51.00% {2} times 78.61% {3}), which is greater than the 10% threshold under 18 Del. C. §5001(c). However, in its Holding Company Registration Statements (Form B) for the years under examination, the Company maintains that GHI is the ultimate controlling entity.

A review of the Annual Form B and Form C filings made by the Company for all years under examination revealed that the Company had complied with the requirements of Regulation 13 of the Delaware Insurance Code.

## Affiliated Agreements

*Service Agreement*

The Company is a party to an amended and restated service agreement with affiliate, SSLICNY, effective July 1, 2007. Under the terms of the agreement, SSLICNY provides legal, tax, financial statement preparation, accounting, policy issuance and premium services to the Company and other participating affiliates. The agreement also requires the Company to provide audit and marketing services to SSLICNY. All services are provided at cost and the settlement of all expenses occurs quarterly. For the years under examination, the Company paid the following amounts to SSLICNY pursuant to this agreement:

| | |
|---|---|
| 2009 | $518,078 |
| 2010 | $577,333 |
| 2011 | $483,952 |
| 2012 | $435,300 |

*Investment Agreements*

The Company is a party to an investment services agreement with IHC, effective December 15, 2006. IHC provides investment staffing services for the trading, sales and maintenance of the Company's investment portfolio.

The Company is a party to an investment counsel agreement with IHC, effective January 1, 2011. IHC provides investment counsel advice for the Company's investment portfolio. This agreement was approved by the Delaware Department of Insurance on March 15, 2011.

*Tax Allocation Agreement*

The Company is a party to a tax allocation agreement with affiliate, AMIC, effective May 1, 2008. The agreement allows the Company and AMIC to file federal income tax returns on a consolidated basis under Section 1504(c)(2) of the Internal Revenue Code of 1986. Amounts either payable or receivable under the agreement are calculated as if each participant filed a separate return with settlement amounts due within thirty days after the date the consolidated federal income tax return is filed.

*Reinsurance Agreements*

The Company is a party to an assumed quota share reinsurance agreement with affiliate, SSLICNY, effective November 10, 2012, and expiring on December 31, 2014. This new master reinsurance agreement, which allows the Company to assume a minimum of 15% and up to a maximum of 50% of SSLICNY's individual or group, fully insured or excess, medical, health, disability, vision or dental insurance business, replaced a similar assumed quota share reinsurance agreement with SSLICNY originally effective January 1, 2002. This new reinsurance agreement was approved by the Delaware Department of Insurance on November 9, 2012.

The Company is a party to an assumed 50% quota share reinsurance agreement with affiliate, Madison National Life Insurance Company (MNLIC), effective December 6, 2012, and expiring on December 31, 2014. This new master reinsurance agreement, which allows the Company to assume a minimum of 15% and up to a maximum of 50% of MNLIC's individual or group, fully insured or excess, medical, health, disability, vision or dental insurance business, replaced a similar assumed quota share reinsurance agreement with MNLIC originally effective April 1, 2002. This new reinsurance agreement was approved by the Delaware Department of Insurance on November 14, 2012.

The Company is a party to a ceded quota share reinsurance agreement with affiliate, MNLIC effective January 1, 2004. This agreement allows the Company to cede up to 55% of certain program business to MNLIC.

The Company is a party to a ceded quota share reinsurance agreement with affiliate, SSLICNY, effective January 1, 2012. This agreement, which allows the Company to cede up to 30% of certain program business to SSLICNY, was terminated effective December 31, 2012. The premiums ceded did not exceed the threshold for filing with the Delaware Department of Insurance.

*Management, Administrative, Marketing and Agency Agreements*

The Company is a party to an administrative agreement with affiliate, Health Plan Administrators, Inc. (HPA), effective January 3, 2005. On behalf of the Company, relating to short-term health insurance business, HPA performs underwriting services, premium billing and collection services, claims review, processing and payment services, and in-force administration services.

The Company is a party to a national marketing organization agency agreement with affiliate, IPA Family, LLC (IPA), effective May 18, 2007. On an exclusive basis, IPA markets, sells and distributes the Company's accident and health plans covering individuals and their families. IPA has the authority to collect premiums and must submit premiums to the Company immediately. IAHC owns 89.6% of IPA.

The Company is a party to an administrative and marketing services agreement with affiliate, IHC Health Solutions, Inc. (IHCHS), effective January 1, 2011. On behalf of the Company, relating to individual and group health insurance and voluntary dental plan business, IHCHS performs marketing, sales support services, underwriting services, premium billing and collection services, claims review, processing and payment services, and in-force administration services. This agreement was approved by the Delaware Department of Insurance on May 25, 2011.

The Company is a party to a management agreement with affiliate, IHC Risk Solutions (IHCRS), effective January 1, 2012. On behalf of the Company, relating to aggregate and specific medical stop loss coverage business, IHCRS performs underwriting services, premium billing and collection services, reimbursement of claims and in-force administration services. This agreement was approved by the Delaware Department of Insurance on July 24, 2012.

Unaffiliated Agreements

*Custodian Agreement*

The Company is a party to an amended and restated domestic custodian agreement with JP Morgan Chase Bank N.A. (JP Morgan Chase), effective April 16, 2007. JP Morgan Chase acts as custodian over the Company's invested assets in exchange for a fee as structured in the agreement. Review of the terms of the custodian agreement indicates that the agreement contains the minimum standards required under the NAIC Handbook.

*Management, Administrative, Marketing, Claims and Agency Agreements*

The Company was a party to a management agreement with Tactical Loss, LLC d/b/a Independence Insurance Group, Ltd. (Tactical Loss), effective September 1, 2008, and terminated on December 31, 2011. Tactical Loss managed and supervised the writing of the Company's aggregate and specific medical stop-loss insurance policies. Policies were marketed to employer or other approved groups in connection with self-funded medical benefit programs. Policies were not allowed to be marketed to multiple employer groups (MEGs) and aggregate-only stop-loss insurance policies were not allowed to be issued unless approved in writing by the Company. Tactical Loss received applications from prospective insureds, and underwrote, quoted and issued the policies or rejected applications on the Company's behalf. Tactical Loss also reimbursed claims, collected and received premiums for remittance to the Company or the Company's reinsurer.

The Company is a party to an administrative services agreement with IHC Administrative Services, Inc. (IHCAS), the successor-in-interest to Insurers Administration Corporation, and Employers Direct Health, Inc. (EDH), effective September 22, 2006. IHCAS performs program management services for the employer medical stop loss coverage business of the Company while EDH performs administrative and marketing services related to the employer medical stop loss coverage business of the Company. EDH underwrites the policies, collects premiums and manages claims activity. As compensation for services provided, the Company pays 14% of premiums to EDH and 1% of premiums written to IHCAS. Since EDH has the ability to bind policies and pay claims, it is considered to be an MGA under 18 Del. C. §1802(3). Related to this business, the Company is a party to an amended and restated indemnity and security agreement with EDH, effective May 21, 2010.

The Company is a party to an administrative services agreement with Ben-E-Lect (Benelect), effective January 1, 2011. Benelect performs management services related to group major medical plans and supplemental coverage of the Company. Benelect performs underwriting services, billing and collection services, reimbursement of claims and in-force administration services.

The Company is a party to a management agreement with ACEC Health MGU, Inc. (ACEC), effective August 1, 2011. On behalf of the Company, relating to aggregate medical stop loss coverage business, ACEC performs underwriting services, premium billing and collection services, reimbursement of claims in-force administration services.

The Company was a party to a management agreement with AJU Underwriters LLC (AJUU), effective September 1, 2011, and terminated on December 31, 2012. On behalf of the Company, relating to aggregate and specific medical stop loss coverage business, AJUU performed underwriting services, premium billing and collection services, reimbursement of claims and in-force administration services.

The Company is a party to a general agency agreement with Pets Best Insurance Services, LLC (PBIS), effective October 15, 2011. On behalf of the Company, relating to pet A&H coverage business, PBIS performs underwriting services, premium billing and collection services and in-force administration services.

The Company is a party to a claims services agreement with Pets Best Insurance, Inc. (PBII), effective October 15, 2011. On behalf of the Company, relating to pet A&H coverage business written by PBIS, PBII pays claims. PBIS and PBII are affiliates of each other.

## TERRITORY AND PLAN OF OPERATION

### Territory

At December 31, 2012, the Company is licensed to write property and/or casualty insurance in the District of Columbia and all fifty U.S. states except New Hampshire. The Company obtained a license in New Hampshire in January 2013.

### Plan of Operation

The majority of the Company’s business is assumed from affiliates. On a direct basis, the Company provides specialized health coverage to commercial customers and individuals, focusing on niche health products primarily written by managing general underwriters (MGUs) in the United States.

The Company writes medical stop-loss (direct and assumed), small group major medical (direct and assumed), short-term medical (direct and assumed), mini-medical/dental/ hospital indemnity/vision (direct and assumed), pet insurance (direct, beginning in 2012), expatriate medical and disability (assumed), and short-term statutory disability benefit product in New York State (DBL) insurance.

2012 direct written premiums by product segment are as follows:

| Product Segment | Premiums | Percent of Total |
|---|---:|---:|
| Group Major Medical (fully insured) | $17.94 million | 41.1% |
| Medical Stop-Loss | $17.06 million | 39.1% |
| Pet | 3.78 million | 8.7% |
| All Other Lines | 4.83 million | 11.1% |
| Total | $43.61 million | 100.0% |

2012 direct written premiums by state (top 5) are as follows:

| State | Premiums | Percent of Total |
|---|---:|---:|
| Texas | $11.39 million | 26.1% |
| North Carolina | 7.60 million | 17.4% |
| California | 4.49 million | 10.3% |
| Arizona | 3.34 million | 7.7% |
| Florida | 2.21 million | 5.1% |
| All Others (44 states and D.C.) | 14.58 million | 33.4% |
| Total | $43.61 million | 100.0% |

2012 direct written premiums by MGU (top 6) are as follows:

| Producer | Premiums | Percent of Total |
|---|---:|---:|
| Employers Direct Health (non-affiliate) | $14.06 million | 32.2% |
| Insurance Producers of America (affiliate) | 9.38 million | 21.5% |
| IHC Administrative (in-house) | 5.95 million | 13.6% |
| AJU Underwriters (non-affiliate) | 4.83 million | 11.1% |
| Pets Best Insurance (non-affiliate) | 3.27 million | 7.5% |
| IHC Risk Solutions (affiliate) | 2.06 million | 4.7% |
| All Other Sources | 4.06 million | 9.4% |
| Total | $43.61 million | 100.0% |

2012 assumed written premiums by product segment are as follows:

| Product Segment | Premiums | Percent of Total |
|---|---:|---:|
| Medical Stop-Loss | $31.39 million | 62.1% |
| Group Major Medical (fully insured) | 7.82 million | 15.5% |
| Disability | 3.16 million | 6.2% |
| All Other Lines | 8.21 million | 16.2% |
| Total | $50.58 million | 100.0% |

2012 gross written premiums (direct and assumed) by product segment are as follows:

| Product Segment | Premiums | Percent of Total |
|---|---|---|
| Medical Stop-Loss | $48.45 million | 51.4% |
| Group Major Medical (fully insured) | 25.76 million | 27.3% |
| Pet | 3.78 million | 4.0% |
| Disability | 3.16 million | 3.4% |
| All Other Lines | 13.04 million | 13.9% |
| Total | $94.19 million | 100.0% |

2012 gross written premiums (direct and assumed) by source are as follows:

| Source | Premiums | Percent of Total |
|---|---|---|
| Assumed from affiliate SSLICNY | $41.93 million | 44.5% |
| Direct from non-affiliate EDH | 14.06 million | 14.9% |
| Direct from affiliate IPA | 9.38 million | 10.0% |
| Assumed from affiliate MNLIC | 8.65 million | 9.2% |
| All Other Net | 20.17 million | 21.4% |
| Total | $94.19 million | 100.0% |

2012 gross written premiums (direct and assumed) by line of business are as follows:

| Annual Statement Line | Premiums | Percent of Total |
|---|---|---|
| Inland Marine (line 9) | $1.16 million | 1.2% |
| Group A&H – direct (line 13) | 39.52 million | 42.0% |
| Group A&H – assumed (line 13) | 50.58 million | 53.7% |
| Other (line 3401) | 2.93 million | 3.1% |
| Total | $94.19 million | 100.0% |

A.M. Best Rating

Based on A.M. Best's current opinion of the consolidated financial condition and operating performance of the Company, AAIC was assigned an A.M. Best rating of A- (Excellent) as of November 16, 2012. A.M. Best notes that the rating reflects the Company's consistent returns and excellent risk adjusted capitalization.

## GROWTH OF THE COMPANY

The following information was extracted from the Company's filed Annual Statements and covers the period from the last examination (2008), and the intervening period to this examination (2012):

| Year | Net Admitted Assets | Liabilities | Surplus as Regards Policyholders | Net Written Premiums | Net Income/ (Loss) |
|---|---|---|---|---|---|
| 2008 | $70,839,501 | $30,474,164 | $40,365,337 | $96,946,500 | $2,323,334 |
| 2009 | 72,463,070 | 28,248,330 | 44,214,740 | 85,464,099 | 2,759,909 |
| 2010 | 72,503,156 | 25,111,077 | 47,392,079 | 73,840,639 | 2,697,239 |
| 2011 | 74,439,855 | 23,033,315 | 51,406,540 | 72,742,585 | 4,541,506 |
| 2012 | 84,696,916 | 30,269,475 | 54,427,441 | 85,787,407 | 3,271,338 |

The Company's assets increased from 2008 through 2012, primarily through profitable operations. Written premiums decreased during the exam period up until 2011, primarily because of assumed quota share business from affiliates. In 2012, the premium written increased primarily because direct and assumed medical stop-loss business and the new pet insurance segment.

In a similar path, the Company's liabilities declined from 2008 to 2011 as the premium base declined, but then increased in 2012 due to increased written premiums and the additional losses related to that additional business.

Policyholders' surplus increased during the examination period by $14.1 million primarily due to the positive net income earned in each of the years under examination.

## LOSS EXPERIENCE

Reserves as of December 31, 2011 were $18,735,801. During 2012, $17,203,433 was paid for incurred losses attributable to insured events of prior years. Reserves remaining for incurred losses attributable to insured events of prior years as of December 31, 2012 were $1,339,741 and were $192,628 lower than what was provided for at December 31, 2011. This favorable variance was the result of a re-estimation of claims and ongoing analysis of recent loss development trends.

## REINSURANCE

The Company reported the following distribution of written premiums in 2012:

| | |
|---|---|
| Direct | $43,613,554 |
| Assumed from affiliates | 50,575,593 |
| Gross Premiums Written | $94,189,147 |
| | |
| Ceded to affiliates | $1,835,473 |
| Ceded to non-affiliates | 6,566,267 |
| Total Ceded Premium | $8,401,740 |
| | |
| Net Premiums Written | $85,787,407 |

The Company retained 91.08% of its gross business in 2012.

Assumed

The Company assumes business from affiliates SSLICNY and MNLIC, pursuant to reinsurance agreements originally effective January 1, 2002, (signed November 7, 2007), and April 1, 2002 (signed March 3, 2008), respectively. These agreements were amended effective November 10, 2012 (SSLICNY), and December 6, 2012 (MNLIC). Under the terms of these agreements, through December 31, 2014, the Company assumes on a quota share basis a minimum of 15% and up to a maximum of 50% of individual or group, fully insured or excess, medical, health, disability, vision or dental insurance business. During the period under review, the Company assumed the following premium amounts from these two affiliates:

| | |
|---|---|
| 2012 | $50,575,593 |
| 2011 | $42,183,988 |
| 2010 | $45,296,901 |
| 2009 | $56,598,526 |

All outside assumption reinsurance agreements were terminated in 2004. Consequently, the premiums received during the examination period under those reinsurance agreements in run-off are negligible.

Ceded

*Affiliated*

Under the terms of a reinsurance agreement with affiliate, MNLIC, effective January 1, 2004, the Company cedes up to 55% of aggregate and specific stop loss insurance, provider excess insurance and any other such insurance risks issued to managed care organizations. During the period under review, the Company ceded the following premium amounts to MNLIC:

| | |
|---|---|
| 2012 | $408,473 |
| 2011 | $1,249,896 |
| 2010 | $1,718,260 |
| 2009 | $1,049,964 |

Under the terms of a reinsurance agreement with affiliate, SSLICNY, effective January 1, 2012, and terminated effective December 31, 2012, the Company cedes up to 30% of aggregate and specific stop loss insurance, provider excess insurance and any other such insurance risks issued to managed care organizations. During 2012, the Company ceded $1,428,000 to SSLICNY.

*Unaffiliated*

The Company cedes IPA-produced individual and group association major medical business under a quota share reinsurance agreement with 50% participation from Munich Reinsurance America, Inc., effective June 1, 2007. The counterparty signed the participation interests and liabilities portion of the reinsurance agreement on October 5, 2007.

The Company also cedes fully insured medical business under a variable quota share reinsurance agreement with Munich Reinsurance America, Inc., effective July 1, 2007.

Premiums under these two reinsurance agreement for the years under examination were as follows:

| | |
|---|---|
| 2012 | $5,062,000 |
| 2011 | $8,117,000 |
| 2010 | $10,847,000 |
| 2009 | $7,409,000 |

The Company has been a party to other various ceded reinsurance agreements with non-affiliates during the examination period. The aggregate premiums under these reinsurance agreements for the years under examination were as follows:

| | |
|---|---|
| 2012 | $1,504,000 |
| 2011 | $334,000 |
| 2010 | $155,000 |
| 2009 | $85,000 |

## ACCOUNTS AND RECORDS

### Accounting System

During the examination period, all necessary accounting records of the Company were maintained on electronic data processing equipment. The general ledger is maintained on a statutory basis with additional accounts used to convert to the accrual basis suitable for Generally Accepted Accounting Principles. Investment transactions are administered through IHC's investment department, which is located in Stamford, Connecticut, and processed using PAM software.

### Information Systems

INS Services, Inc. reviewed the Company's responses to the Evaluation of Controls in Information Systems Questionnaire (Exhibit C) but did not perform any tests of the systems because the Company utilizes minimal levels of technology for processing financial transactions. INS Services analysis concluded the following:

- The Company's responses to Exhibit C present fairly, in all material respects, the aspects of the Company's policies and procedures that may be relevant to their internal control structure.

- The control structure policies and procedures were suitably designed to achieve the control objectives implicit in the questionnaire, if those policies and procedures were complied with, and that such policies and procedures have been in place and in operation as of December 31, 2012.

Independent Accountants

The Company's financial statements are audited each year by KPMG of New York, New York, which issues a statutory audit opinion. For all of the years under review, KPMG issued an unqualified opinion.

Actuarial Opinion

The Company's loss and loss adjustment expense (LAE) reserves and related actuarial items were reviewed by Russel L. Sutter, FCAS, MAAA, of Towers Watson, who issued a statement of actuarial opinion for each of the years under examination, based on the financial information presented by the Company. The opinions stated that the reserves and related actuarial values carried on the balance sheets were fairly stated and met the requirements of the insurance laws of the State of Delaware.

## FINANCIAL STATEMENTS

The following pages contain the Company's Financial Statements for the year ending December 31, 2012, as determined by this examination, with supporting exhibits as detailed below:

Analysis of Assets
Statement of Liabilities, Surplus and Other Funds
Underwriting and Investment Exhibit - Statement of Income
Capital and Surplus Account
Reconciliation of Surplus since last Examination
Dividends
Capitalization

It should be noted that the various schedules and exhibits may not add to the totals shown due to rounding. Narratives on certain individual accounts were included to provide the reader with additional supporting information.

## Analysis of Assets

### As of December 31, 2012

| | Ledger Assets | Non-admitted Assets | Admitted Assets | Note |
|---|---|---|---|---|
| Bonds | $ 56,496,134 | | $ 56,496,134 | 1 |
| Preferred stocks | 2,879,832 | | 2,879,832 | |
| Common stocks | 1,056,089 | | 1,056,089 | |
| Cash, cash equivalents and short-term investments | 5,897,864 | | 5,897,864 | |
| Receivable for securities | 60,876 | | 60,876 | |
| Investment income due and accrued | 704,795 | | 704,795 | |
| Uncollected premiums and agents' balances in the course of collection | 8,713,138 | $ 901,985 | 7,811,153 | |
| Funds held by reinsured companies | 4,760,645 | | 4,760,645 | |
| Other amounts receivable under reinsurance contracts | 25,325 | | 25,325 | |
| Current federal and foreign income tax recoverable and interest thereon | 46,898 | | 46,898 | |
| Net deferred tax asset | 848,748 | 311,556 | 537,192 | |
| Aggregate write-ins for other than invested assets | 4,420,113 | | 4,420,113 | 2 |
| Total Assets | $ 85,910,457 | $ 1,213,541 | $ 84,696,916 | |

## Statement of Liabilities, Surplus and Other Funds

### As of December 31, 2012

| | | Note |
|---|---|---|
| Losses | $ 23,999,400 | 3 |
| Loss adjustment expenses | - | 3 |
| Commissions payable, contingent commissions & other similar charges | 1,416,097 | |
| Other expenses | 114,731 | |
| Taxes, licenses and fees (excluding federal and foreign income taxes) | 538,603 | |
| Unearned premiums | 2,436,639 | |
| Ceded reinsurance premiums payable | (6,656) | |
| Funds held by company under reinsurance treaties | 1,398,514 | |
| Remittances and items not allocated | 237,595 | |
| Payable to parent,subsidiaries and affiliates | 108,809 | |
| Payable for securities | 21,970 | |
| Aggregate write-ins for liabilities | 3,773 | |
| Total Liabilities | $ 30,269,475 | |
| | | |
| Common capital stock | $ 3,000,000 | |
| Gross paid in and contributed surplus | 26,902,015 | |
| Unassigned funds (surplus) | 24,525,426 | |
| Surplus as regards policyholders | $ 54,427,441 | |
| | | |
| Total Liabilities, Capital and Surplus | $ 84,696,916 | |

## Underwriting and Investment Exhibit - Statement of Income

As of December 31, 2012

| | | |
|---|---|---|
| **UNDERWRITING INCOME** | | |
| Premiums earned | $ | 83,777,604 |
| | | |
| **DEDUCTIONS** | | |
| Losses incurred | $ | 56,436,634 |
| Loss adjustment expenses incurred | | 482,869 |
| Other underwriting expenses incurred | | 24,174,115 |
| Total underwriting deductions | $ | 81,093,618 |
| Net underwriting gain or (loss) | $ | 2,683,986 |
| | | |
| **INVESTMENT INCOME** | | |
| Net investment income earned | $ | 1,999,720 |
| Net realized capital gains or (losses) | | 346,835 |
| Net investment gain or (loss) | $ | 2,346,555 |
| | | |
| **OTHER INCOME** | | |
| Net gain (loss) from agents' balances charged off | $ | - |
| Aggregate write-ins for miscellaneous income | | - |
| Total other income | $ | - |
| | | |
| Net income before dividends to policyholders and before federal income taxes | $ | 5,030,541 |
| Federal and foreign income taxes incurred | | 1,759,203 |
| Net income | $ | 3,271,338 |

# Capital and Surplus Account

## As of December 31, 2012

**CAPITAL AND SURPLUS ACCOUNT**

| | | |
|---|---|---|
| Surplus as regards policyholders, December 31, 2011 | $ | 51,406,540 |
| | | |
| **GAINS AND (LOSSES) IN SURPLUS** | | |
| Net income | $ | 3,271,338 |
| Change in net unrealized capital gains or (losses) less capital gains tax | | 90,957 |
| Change in net deferred income tax | | 918,345 |
| Change in non-admitted assets | | 740,261 |
| Dividends to stockholder | | (2,000,000) |
| Change in surplus as regards policyholders for the year | $ | 3,020,901 |
| | | |
| Surplus as regards policyholders, December 31, 2012 | $ | 54,427,441 |

## Reconciliation of Surplus since last Examination

| | Common Capital Stock | Gross Paid -in & Contributed Surplus | Unassigned Funds (Surplus) | Total |
|---|---|---|---|---|
| December 31, 2008 | $ 3,000,000 | $ 26,902,015 | $ 10,463,322 | $ 40,365,337 |
| Operations 2009 (1) | | | 3,849,403 | 3,849,403 |
| Dividends 2009 (2) | | | - | - |
| Operations 2010 (1) | | | 4,677,339 | 4,677,339 |
| Dividends 2010 (2) | | | (1,500,000) | (1,500,000) |
| Operations 2011 (1) | | | 5,014,461 | 5,014,461 |
| Dividends 2011 (2) | | | (1,000,000) | (1,000,000) |
| Operations 2012 (1) | | | 5,020,901 | 5,020,901 |
| Dividends 2012 (2) | | | (2,000,000) | (2,000,000) |
| December 31, 2012 | $ 3,000,000 | $ 26,902,015 | $ 24,525,426 | $ 54,427,441 |

(1) Operations is defined as: net income, change in net unrealized capital gains or (losses), change in net deferred income tax, change in non-admitted assets, change in provision for reinsurance, and aggregate write-ins for gains and losses to surplus.

(2) See dividend section

## Dividends

The Company paid the following dividends to the sole shareholder of the Company upon approval of the Board of Directors during the period under examination:

| Amount | Dividend Type | Approved Date | Paid Date |
|---|---|---|---|
| $1,500,000 | Ordinary | December 30, 2010 | December 30, 2010 |
| $1,000,000 | Ordinary | October 10, 2011 | October 11, 2011 |
| $1,000,000 | Ordinary | October 1, 2012 | October 2, 2012 |
| $1,000,000 | Ordinary | December 27, 2012 | December 28, 2012 |

Capitalization

The Company is authorized to issue 10,000 shares of common capital stock capital with a par value of $600 per share. Currently, only 5,000 shares have been issued, all owned by Independence American Holding Corp. (IAHC). The capital stock and gross paid in have remained unchanged over the examination period.

**NOTES TO FINANCIAL STATEMENTS**

(1) Bonds $56,496,134

The above-captioned amount, which is the same as that reported by the Company in its Annual Statement, has been accepted for purposes of this report. 100% of the Company's bonds have a NAIC SVO rating of either 1 or 2. With the exception of bonds held for statutory purposes, investments are primarily held by JP Morgan Chase Bank under a custodial agreement. A review of corporate records indicates that the Board of Directors has approved the Company's investment transactions made during the examination period in accordance with 18 Del. C. §1304.

(2) Aggregate Write-ins for Other Than Invested Assets $4,420,113

This balance consists of the following components: $2,962,602 in admitted claims funds and $1,457,511 as "Due from MGU Settlement".

(3) Losses $23,999,400
Loss Adjustment Expenses $0

The above-captioned amounts, which are the same as those reported by the Company in its Annual Statement, have been accepted for purposes of this report.

Losses

| | |
|---|---|
| Reported Losses (Case) | |
| Direct | $10,271,400 |
| Reinsurance Assumed | 15,262,500 |

| | |
|---|---|
| Reinsurance Ceded | 0 |
| Net Reported Losses | $25,533,900 |
| | |
| Incurred but not reported (IBNR) | |
| Direct | $0 |
| Reinsurance Assumed | 0 |
| Reinsurance Ceded | 1,534,500 |
| Net IBNR | $1,534,500 |
| | |
| Net Losses Unpaid | $23,999,400 |
| Loss Adjustment Expenses (LAE) | $0 |

The Delaware Insurance Department retained the firm of INS Consultants, Inc. (INS or consulting actuary), to review the Company's stated reserves. The consulting actuary was provided with the Company's statement of actuarial opinion and an actuarial report as supporting documentation of the actuarial opinion with loss and loss adjustment expense reserves evaluated as of December 31, 2012. In addition, INS was provided with other reports, schedules, exhibits and relevant information as requested.

The Consulting actuary's review of loss and allocated loss adjustment expenses (ALAE) reserves consisted of separately analyzing the Company's property and casualty books of business on a gross and net basis. In addition, for unallocated loss adjustment expenses (ULAE), the consulting actuary reviewed the methodology employed by the Company's actuaries. INS accepted the methodology and factor selections utilized by the Company's actuaries and ultimately found the Company's reserves to be reasonable.

## SCHEDULE OF EXAMINATION ADJUSTMENTS

No examination changes were made as a result of this examination.

## COMPLIANCE WITH PRIOR EXAM REPORT RECOMMENDATIONS

It was determined that EDH, through its ability to bind policies and pay claims, is considered to be an MGA under 18 Del. C. §1802(3) and was in violation of 18 Del. C. §1803(b).

**Therefore, it was recommended that the Company comply with the licensure requirements of 18 Del. C. §1803(b).** The Company now recognizes EDH as an MGA and has complied with the Delaware licensure requirements.

## CONCLUSION

The following schedule shows the results of this examination and the results of the prior examination with changes between the examination periods:

| Description | December 31, 2008 | December 31, 2012 | Increase (Decrease) |
|---|---|---|---|
| Assets | $ 70,839,501 | $ 84,696,916 | $ 13,857,415 |
| Liabilities | $ 30,474,164 | $ 30,269,475 | $ (204,689) |
| Common Capital Stock | 3,000,000 | 3,000,000 | - |
| Gross Paid In and Contributed Surplus | 26,902,015 | 26,902,015 | - |
| Unassigned Funds (Surplus) | 10,463,322 | 24,525,426 | 14,062,104 |
| Total Surplus as Regards Policyholders | $ 40,365,337 | $ 54,427,441 | $ 14,062,104 |
| Totals | $ 70,839,501 | $ 84,696,916 | $ 13,857,415 |

The assistance of Delaware's consulting actuarial firm, INS Consultants, Inc. and INS Services, Inc. is acknowledged.

Respectfully submitted,

Andrew Chiodini, CFE
Examiner-In-Charge
State of Delaware