

Commonwealth of Puerto Rico
OFFICE OF THE COMMISSIONER OF INSURANCE

HUMANA HEALTH PLANS OF PUERTO RICO
As of December 31, 2011

NAIC Code: 95721
Amended

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COMMONWEALTH OF PUERTO RICO
OFFICE OF THE COMMISSIONER OF INSURANCE

October 25, 2013

Ángela Weyne Roig
Commissioner of Insurance
Office of the Commissioner of Insurance
Guaynabo, Puerto Rico

Dear Commissioner:

Pursuant to the Amended Order Number EX-2012-05A, dated October 1, 2012, and in accordance with the provisions of Section 2.140 of the Insurance Code of Puerto Rico, 26 L.P.R.A, section 214, as amended, a comprehensive risk focused examination and financial affairs examination was conducted of the books, records and financial condition of

Humana Health Plans of Puerto Rico,

hereinafter referred to as "the Organization."

SCOPE OF EXAMINATION

The examination covered financial transactions and operations between January 1, 2006, and December 31, 2011, and subsequent transactions, which in the judgment of the examiner were relevant. The examination was conducted at the home office of the Organization located at 383 FD Roosevelt Avenue, San Juan, Puerto Rico.

We conducted our examination in accordance with the National Association of Insurance Commissioners *Financial Condition Examiners Handbook* (Handbook). The

Handbook requires that the examination be planned and performed to evaluate the financial condition and identify prospective risks of the Organization by obtaining information about the Organization, including corporate governance, identifying and assessing inherent risks within the Organization, and evaluating system controls and procedures used to mitigate those risks. The examination also includes 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, as applicable to the Insurance Code of Puerto Rico, "the Code", and Regulations.

HISTORY

The Organization is a federally-qualified HMO under Title XIII of the Public Health Services Act and is subject to the provisions of Chapter 19 of the Insurance Code of the Commonwealth of Puerto Rico. The Organization is ultimately wholly-owned by Humana, Inc.

The Organization was incorporated on December 8, 1983, in accordance with the provisions of the Insurance Code of Puerto Rico with the name of Health Plus, Inc., commencing business on May 1, 1986. The Organization was authorized by this Office to act in Puerto Rico as a Health Maintenance Organization (HMO). The Articles of Incorporation showed the total authorized capital of one million dollars (\$1,000,000), comprising two hundred thousand (200,000) common shares with a par value of \$5 per share.

On December 14, 1994, the Organization amended its Articles of Incorporation for the first time in order to reduce the quantity of common shares in the authorized

capital from 200,000 to 8, and to increase the par value per share to \$142,500, authorized capital for a total of \$1,140,000. Subsequently, the Articles of Incorporation were amended once again to increase the quantity of common shares from 8 to one millions (1,000,000), and to decrease change the par value to \$5 per share, for a total of \$5,000,000 authorized capital.

The Organization changed its name to PCA Health Plans of Puerto Rico on March 31, 1995 and then to Humana Health Plans of Puerto Rico on January 12, 1998.

BY-LAWS

Section 1 of Article II of the By-laws of the Organization establishes that the annual meeting of the stockholders shall be held on the third Wednesday of April each year. For the examination period, the annual meetings of stockholders were held on the following dates:

<u>Date Held</u>	<u>Third Wednesday</u>
April 21, 2006	April 19, 2006
April 18, 2007	April 18, 2007
April 17, 2008	April 16, 2008
May 14, 2009	April 15, 2009
May 18, 2010	April 21, 2010
April 5, 2011	April 20, 2011

For the years 2006, 2008, 2009, 2010 and 2011, the Organization did not comply with Section 1 of Article II of the By-laws of the Organization and the established dates for stockholder's annual meetings.

BOARD OF DIRECTORS

Section 2 of Article III of the By-laws of the Organization establishes that the Board of Directors will consist of not less than five (5) and no more than thirteen (13) directors. Each director will be elected for a term of one (1) year.

As of December 31, 2011, the members of the Board of Directors of the Organization were the following:

James E. Murray	Chairman
David M. Krebs	Director
Luis M. Montaner, M.D.	Director
P. Anthony Hammond	Director

As of December 31, 2011, the Organization did not comply with Section 2 of Article III of the By-laws of the Organization by having a Board of Directors composed only of four (4) directors.

Furthermore, Section 3 of Article III of the By-laws of the Organization establishes that the first meeting of each newly elected Board of Directors shall be held immediately after the stockholders meeting and in the same place.

For the years 2006, 2008, 2009, 2010 and 2011, the Organization failed to comply with Section 3 of Article III since it did not hold the directors meeting on the third Wednesday of every year. Please refer to previous section "By-Laws" for annual meetings of stockholders.

OFFICERS

As of December 31, 2011, the Officers of the Organization were the following:

David M. Krebs	President and Chief Operating Officer
Thomas J. Liston	Senior Vice President Senior Products

James H. Bloem Treasurer
 María del Carmen Rosario Secretary
 Joan O. Lenahan Assistant Secretary

On July 2, 2012, the Organization notified this Office that Mr. Earl M. Harper was appointed as President of the Organization.

CAPITAL STOCK

As of December 31, 2011, the paid-in capital of the Organization was \$142,525 distributed as follows:

Name	Outstanding Shares	Value	Paid-in Capital
Humana, Inc.	28,500	\$5	\$142,500
James E. Murray	1		5
David M. Krebs	1		5
Luis M. Montaner, M.D.	1		5
P. Anthony Hammond	1		5
Vacant	1		5
Total	<u>28,505</u>		<u>\$142,525</u>

RETIREMENT SAVINGS PLAN

The Humana Puerto Rico Retirement Savings Plan (the Plan) offers the opportunity to defer a portion of the employee’s compensation that would be subject to current income taxes and contribute that amount to the Plan on a “before-tax” basis and, in doing so, defer taxation until the contribution is distributed to the employee.

In addition, the Organization will make a matching contribution of a portion of the amount that the employee contributes up to certain limits. The Plan is generally open to employees of Humana, Inc., or affiliates who live and work in Puerto Rico and adopted the Plan.

The employee will automatically be enrolled in the Plan for a 4% Pre-tax Contribution as of the first day of the payroll period that begins 45 days following the date of hire, unless the employee elects not to participate or participate at a different amount. If the employee remains enrolled, the contribution will increase to 5% after the second Plan Year following the end of the enrollment and to 6% after the third Plan Year following the end of the enrollment, percentage that will remain the same until the employee elects to change it.

The Organization will match 125% of the amount of the employee Pre-tax Contributions up to 6% of the employee's compensation.

HEALTH INSURANCE FOR EMPLOYEES

The Organization offers its employees several alternative health coverages for medical services. The Organization pays part of the cost of the health plan.

GRIEVANCE PROCEDURE

Article 19.120(b) of the Insurance Code of Puerto Rico requires that the complaints procedure shall include the designation of a Grievance Committee which shall not exceed five (5) members and on which the subscribers of individual contracts, the subscribers of the different group plans and the providers shall be represented. The members of the Committee shall not be employees, officials, directors or shareholders of the health maintenance organization, and shall be members of the Committee for a period of not less than one (1), year and no more than three (3) years, as follow:

Name	Period
Mr. Rodney Estrella Morell	4 years
Mr. Víctor Rivera	4 years

Dr. Segio López del Pozo 2 years
Mrs. Ali Martel 3 years

The Organization did not comply with the referred Article 19.120(b), since two of the members, Mr. Rodney Estrella and Mr. Víctor Rivera, had been members of the Grievance Committee for more than three (3) years.

FIDELITY BONDS

As of December 31, 2011, the Organization maintained a Managed Care Organization Directors & Officers liability policy issued by an insurer authorized by this Office. Following is the summary of this insurance coverage:

Coverage	Aggregate/ Limit per Coverage	Retention
Directors & Officers	\$1,750,000	\$250,000

The coverage complied with the minimum amount for the level of exposure suggested by the National Association of Insurance Commissioners.

RELATION OF STOCKHOLDERS

Ruling Letter No. 2009-104-AF of September 22, 2009, requires that all health maintenance organizations submit, no later than March 31 of each year, a list of all stockholders as of December 31 of the preceding year along with the number of stocks held by each one and the percentage representing the total number of stocks issued and outstanding.

The relationship of stockholders for the year 2009, was submitted to this Office on February 17, 2010, and included an error in the number of stock owned by Humana, Inc. The amount of stock owned by Humana, Inc., is 28,500 instead of 28,505, as presented in the list of relationship. The Organization noticed the error and filed an amended list of

stockholders on May 4, 2010. The Organization must be diligent in reviewing prior to submitting to this Office information required.

PROTECTION AGAINST INSOLVENCY

Article 19.140 of the Insurance Code of Puerto Rico requires that as a guarantee of compliance with the obligations towards subscribers, providers and creditors, each health services organization shall deposit the amount of \$600,000 in eligible assets with the Commissioner, as provided by sect. 802. of this Code.

The Organization maintained, as of December 31, 2011, a statutory deposit of \$600,455 at amortized value, thus complying with Section 19.140 of the Insurance Code of Puerto Rico.

TERRITORY AND PLAN OF OPERATIONS

The Organization is authorized to operate in the territory of the Commonwealth of Puerto Rico.

GROWTH OF THE COMPANY

The following data was obtained from the annual statements filed with this Office:

Year	Admitted Assets	Liabilities	Capital	Gross Paid Contributed Surplus ¹	Unassigned Surplus
2011	\$234,806,753	\$150,718,866	\$142,525	\$27,107,930	\$56,837,432
2010	\$228,275,952	\$160,402,254	\$142,525	\$26,625,570	\$41,374,304
2009	\$192,651,036	\$131,644,628	\$142,525	\$26,169,379	\$34,694,504

¹ There is a monthly entry related to the monthly expensing of restricted stock awards that are granted to certain associates. The entry is to record expense and debit CIEPV. Awards are granted at various times throughout the year to certain associates. The expense for each award will take place over the vesting period, typically three years. The expense follows the associate. So wherever the associate that receives the awards is coded in the payroll system, this is the company that will receive the expense. This is a non-cash transaction as the associates receive stock, not cash at the end of the vesting period- -therefore the offset to the expense account is CIEPV. The expense is recorded on a monthly basis for all of Humana.

Year	Admitted Assets	Liabilities	Capital	Gross Paid Contributed Surplus ¹	Unassigned Surplus
2008	\$205,177,168	\$155,348,453	\$142,525	\$25,723,732	\$23,962,458
2007	\$167,692,983	\$148,628,229	\$142,525	\$24,632,546	(\$5,710,317) ²

ANNUAL STATEMENT

Article 19.090(1) of the Insurance Code of Puerto Rico requires that each health maintenance organization shall render to the Commissioner, with a copy to the Secretary of Health, on or before March 31, a true statement certified by an authorized public accountant under oath of two of its principal officers, covering the period ending December 31st of the preceding year and shall be made in the form prescribed by the Commissioner.

The Annual Statement for the year ended on December 31, 2007, was submitted on April 1, 2008, thus not complying with Article 19.090(1) of the Insurance Code of Puerto Rico.

There are other instances in which the Organization did not comply with the Annual Statements Instructions such as:

1. The Organization did not submit the Management Discussions and Analysis (MD&A). The MD&A is a comprehensive part of the Annual Statement.
2. Schedule E of the Annual Statement was not completed properly, and did not include a breakdown of all cash accounts held by the Organization for the year ended on December 31, 2011.
3. The Organization did not include the Notes to Financial Statements in the Annual Statement for the years 2006, 2008, 2009, 2010 and 2011.

² The negative unassigned surplus for the year end 2007 was due to the income loss in operations during 2006 of \$11,354,610, and operational net losses of \$7,628,531 for the year 2007.

During the examination, the Organization made reclassifications and adjustments to many accounts of the Annual Statement as of December 31, 2011, after presenting the annual statement to this Office. The Organization did not present the amended annual statement, as required by Ruling Letters NE-3-74-94 of April 12, 1994. We will present later in this examination report those accounts presented as accounting adjustments or reclassification between them for which the Organization did not file the Amended Annual Statement.

ACTUARIAL OPINION

The Annual Statement Instructions for the year 2011, requires that the actuary must have been appointed by the Board of Directors, or its equivalent, or by a committee of the board as of December 31st of each calendar year for which the opinion is rendered. During the review of the minutes of the Board of Directors of the Organization, we noted the Board did not appoint Mr. P. Anthony Hammon as Actuary for the year 2011, as required in the Annual Statements Instructions.

Later, on April 5, 2011, P. Anthony Hammond, MAAA, ASA, was elected to serve as Director of the Organization and remained in that position until July 23, 2012. Mr. Hammond is also Vice President Risk & UM, Chief Actuary for Humana, Inc.

According with Precept 7 of the Code of Professional Conduct for Actuaries, an Actuary shall not knowingly perform Actuarial Services involving an actual or potential conflict of interest unless:

- The Actuary's ability to act fairly is unimpaired;
- There has been disclosure of the conflict to all present and known prospective Principals (Clients) whose interests would be affected by the conflict; and

- All such Principals (Clients) have expressly agreed to the performance of the Actuarial Services by the Actuary.

In order to avoid any possibility of conflict of interest, in the future the Organization shall indicate that as a Principal, he has agreed to Precept 7 of the Code of Professional Conduct for Actuaries.

RULE 14 A OF THE PUERTO RICO INSURANCE CODE

Article 5(G) of Rule 14-A requires that the audited financial statements shall be prepared in a form and substantially similar sections as the annual statement of the insurer filed in this Office.

During the examination, it was noted that the Organization amended the annual statement to comply with Article 5(G) of Rule 14-A of the Regulations of the Insurance Code of Puerto Rico, because there were differences between the audited financial statements of the Organization and the annual statements filed

However, it was noted that the amendment was filed June 27, 2013, one (1) year after. We recommend that subsequent annual statements amendments be filled within reasonable period of time after the submittal of the audited financial financial statements in June.

Article 11(A) of Rule 14-A of the Regulations of the Insurance Code of Puerto Rico requires that each insurer shall file with the Commissioner a written communication describing material deficiencies that arose during an audit related to internal controls. The communication shall be prepared by the accountant within sixty (60) days after

filing the audited financial reports. If there are no material weaknesses, the written communication shall so state it.

The Organization did not submit the communication of the internal control related matters in the audit as of December 31, 2010 and December 31, 2011, prepared by the external auditors.

RULE 83 OF THE PUERTO RICO INSURANCE CODE

Rule 83 of the Regulations of the Insurance Code of Puerto Rico became effective on January 26, 2011 with the purpose of regulating the activities of the Insurance Holding Companies, and to establish the criteria to approve or disapprove any transaction that threatens the economic stability of an affiliated insurer or a health maintenance organization. At the examination date, the Organization is a controlled HMO under the definitions set forth Rule No. 83. The structure of the Holding Company, as of the examination date, is presented in Schedule III of this examination report.

It is noted that the ultimate parent of the Organization, Humana, Inc., maintained direct relationships with four investment managers, among which is Black Rock.

Black Rock, Inc. is an investment advisor who, acting on behalf of the Organization, has access to the investment account, handles securities and has authority to make investment decisions.

Section 13 of the Rule 83 of the Regulations of the Insurance Code of Puerto Rico requires annual registration filing of Form B to all insurers or health maintenance organizations authorized to transact insurance business in Puerto Rico who are part of a holding company system.

During the examination, it was noted that the Organization failed to comply with Section 13 of Rule 83, since the Organization did not submit to this Office the Annual Registration - Form B for the year 2011.

Besides, Section 14 of Rule 83 of the Regulations of the Insurance Code of Puerto Rico requires the summary of registration filing Form C from all insurers or health maintenance organizations authorized to transact insurance business in Puerto Rico and who are part of a holding company system. Insurers or health maintenance organizations shall file a copy of Form C in every state where they are authorized to transact insurance business, if so required by the commissioner of that state.

During the examination, it was noted that the Organization failed to comply with the Section 13 and Section 14 of Rule 83, since the Organization did not submit to this Office the Annual Registration - Form B and Summary of Registration - Form C for the year 2011.

UNCLAIMED FUNDS

Article 26.040(1) of the Insurance Code of Puerto Rico requires that every insurer and every general agent, manager or authorized representative shall, on or before May 1st of each year, submit a written report to the Commissioner on all unclaimed funds, withheld and indebted to the former as defined in Section 2603(b) of the Insurance Code of Puerto Rico, as of the immediately preceding December 31.

The Organization submitted the unclaimed funds report as of December 31, 2007, on May 14, 2008, in violation of the Article 26.040(1) of the Insurance Code of Puerto Rico.

CONTRACT WITH HEALTH INSURANCE ADMINISTRATION OF PUERTO RICO

Effective October 1, 2010, the Organization and the Health Insurance Administration of Puerto Rico (ASES by its acronym in Spanish) signed an agreement to provide health coverage to the beneficiaries of the Government Health Reform, known in Spanish as "Mi Salud". Under "Mi Salud" Program, the Organization provides healthcare to approximately 519,000 persons that are covered in the geographical areas of the East, Southeast and Southwest of the Island of Puerto Rico. The contract will be effective from October 10, 2010 to June 30, 2013, subject to annual renegotiation of premiums. The Article 21.1.1 of the agreement provides the monthly premium to be paid to the Organization to be in the amount of \$ 131.99 per subscriber at the East area, \$115.71 in the Southeast and \$91.00 for the Southwest.

The agreement states that the profit of the Organization for each Fiscal Year shall not exceed two and one half percent (2.5%) on a per member per month basis. In the event that the profit exceeds this amount, the parties shall share the Excess of Profit in twenty-five percent (25%) for the Organization and seventy-five percent (75%) for ASES. For the period covered for the years 2010 and 2011 such earnings did not exceed the agreed payment per member per month.

The Organization also has an agreement with ASES to provide health insurance coverage to medically indigent persons in the Medicare Platino Program. The agreement has been extended to December 31, 2012.

AFFILIATED AND RELATED COMPANIES

The Organization maintains a service agreement effective on January 1, 2011 with Humana Insurance of Puerto Rico (Humana) in order to provide certain administrative and operational services. The services to be rendered to Humana under this agreement are listed on Schedule I of this examination report.

According to the agreement, the Organization shall allocate or make a distribution on a pro rata sharing cost based upon appropriate cost drivers such as resources distribution, segments or lines of business and/or membership, which will vary depending on each cost. Such cost drivers are also evaluated from time to time by the parties to ascertain that the analysis process is in-line with the current operational structure. Some of the conditions of the sharing costs agreements are:

1. The settlement of the current month's costs under the agreement shall occur during the same month based on an estimate or based on the methodology developed by the Organization to determine the cost attributable to the operations of Humana. These estimated amounts will be paid throughout the month following the process followed by the Organization and Humana to settle due to/due from.
2. All settlements required to be made under the Agreement shall be made through internal reconciliations in the relevant intercompany accounts of Humana and the Organization.

During the examination, we requested from the Organization a detail of administrative expenses allocated to Humana. An explanation of the way to determine the allocation of cost was also requested. The responses for these requests are presented in Schedule II of this examination report.

During the examination, according to the books of the Organization, it was not possible to determine the expense allocations of the Organization. The books, accounts and records of each party to all such transactions shall be so maintained as to clearly and accurately disclose the nature and details of the transactions, including such necessary accounting information to support the reasonableness of the charges or fees to the respective parties.

Article 19.180(3) of the Insurance Code of Puerto Rico requires that each health maintenance organization or provider shall submit its books and records relating to the health care plan for examination, and shall facilitate such examination. For purpose of the examination, the Commissioner and the Secretary of Health may administer oaths and examine the officers and agents of the organization and the officers of the providers related to its business.

In connection with the above, Rule 9 of the Insurance Code of Puerto Rico requires that books of accounts and contracts, vouchers, records and all other documentation relating to such business transactions will be handled and disposed in such a way that the economic conditions of the insurer can be easily determined, and the financial statements and reports submitted to this Office should be tested at any time.

The Organization did not comply with Article 19.180(3) and Rule 9 of the Regulations of the Insurance Code of Puerto Rico failing to maintain accounting records of the intercompany account.

SSAP No. 25 of the Accounting Practice and Procedures Manual of NAIC, establishes statutory accounting principles and disclosure requirements for related party

transactions. Also, in SSAP No. 70, the statutory accounting principles for 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 are established.

The Organization did not clearly demonstrate the process of recording the transactions between itself and its affiliates. Therefore, it was not possible to validate during the examination if the distribution of expenses were fair and reasonable in accordance with SSAP No. 25 of the Accounting Practice and Procedures Manual of the NAIC.

DIVIDENDS

On April 27, 2006, the Board of Directors of the Organization approved a dividend payment in the amount of \$736.69 per share (aggregate amount of \$21 million) on 28,506³ outstanding shares of the Organization. On May 22, 2006 dividend was paid from available surplus funds of the Organization.⁴

The Organization was in compliance with provision of Article 29.340 of the Insurance Code of Puerto Rico.

ACCOUNTING RECORDS

The accounting records of the Organization are prepared on a combined cash and accrual basis for the purpose of preparing the Financial Statements and the Annual Statement. Some of the reports observed were the general ledger, uncollected premiums subsidiaries, income and disbursement registers as well as automated journals.

³ On October 23, 2007 by Unanimous Consent of the Board of Directors was amended the Consent dated April 27, 2006, to clarify that the contingent approval was not required.

⁴ Any prior approval was not required.

During the examination period, the Organization was audited by the external firm PriceWaterhouseCoopers.

FINANCIAL STATEMENTS

The following financial statements are included below:

- Comparative Balance Sheet as of December 31, 2011 and December 31, 2010.
- Balance Sheets showing examination adjustments and reclassifications as of December 31, 2011.
- Summary of Operations, as included in the Annual Statement as of December 31, 2011.
- Reconciliation Statement for Unassigned Surplus as of December 31, 2011.

HUMAN HEALTH PLANS OF PUERTO RICO
COMPARATIVE BALANCE SHEET
AS OF DECEMBER 31, 2011 AND 2010

	2011	2010
ASSETS		
Bonds	\$96,558,406	\$92,664,291
Cash and Cash Equivalents	52,305,249	9,051,139
Investment Income Due and Accrued	775,656	780,101
Uncollected Premiums	72,498,146	113,714,437
Accrued Retrospective Premiums	417,919	705,881
Amounts Receivable Relating Uninsured	717,080	
Current Federal and Foreign Income Tax Recoverable	5,313,931	10,529,639
Electronic Data Processing Equipment	1,659,445	321,110
Receivable from Parents, Subsidiaries and Affiliate	1,764,451	
Health Care and Other Amounts Receivables	<u>2,796,471</u>	<u>509,354</u>
Total Assets	<u>\$234,806,754</u>	<u>\$228,275,952</u>
LIABILITIES		
Claims Unpaid	\$116,896,781	\$104,741,973
Accrued Medical and Other Incentive Pool	7,308,807	4,388,193
Unpaid Claims Adjustment Expenses	805,975	1,251,975
Aggregate Health Policy Reserves	6,546,446	5,677,162
Aggregate Health Claims Reserves	2,019,186	1,731,818
Premium Received in Advance	152,921	54,628
General Expenses Due and Accrued	10,629,701	1,821,796
Amounts Withheld or Retained	1,478,351	7,645,825
Remittances and Items Not Allocated	48,979	(7,753)
Amounts Due to Parent, Subsidiaries and Affiliates		27,728,285
Payable for Securities		99,550
Liability for Amounts Held Under Uninsured	(188,015)	
Aggregate Write-in for Others Liabilities	<u>5,019,735</u>	<u>5,268,802</u>
Total Liabilities	<u>\$150,718,867</u>	<u>\$160,402,254</u>
CAPITAL AND SURPLUS		
Common Capital Stock	\$142,525	\$142,525
Gross Paid-in and Contributed Surplus	27,107,930	26,625,570
Unassigned Surplus	<u>56,837,432</u>	<u>41,105,603</u>
Total Capital and Surplus	<u>\$84,087,887</u>	<u>\$67,873,698</u>
TOTAL LIABILITIES, CAPITAL AND SURPLUS	<u>\$234,806,754</u>	<u>\$228,275,952</u>

HUMANA HEALTH PLANS OF PUERTO RICO
ADJUSTED BALANCE SHEETS
AS OF DECEMBER 31, 2011

	Annual Report Balance	Adjustments and/or Reclassifications		Examination Balance
		DR	CR	
ASSETS				
Bonds ⁵	\$96,558,406			\$96,558,406
Cash and Cash Equivalents	52,305,249	658,820(R) 467,343(A)	3,790,753(R)	49,640,659
Investment Income Due and Accrued	775,656			775,656
Uncollected Premiums	72,498,146		809,629(A) 389,717(R)	71,298,800
Accrued Retrospective Premiums	417,919			417,919
Amounts Receivable Relating Uninsured	717,080			717,080
Current Federal and Foreign Income Tax Recoverable	5,313,931		1,674,939(A)	3,638,992
Electronic Data Processing Equipment	1,659,445			1,659,445
Receivable from Parent, Subsidiaries and Affiliates	1,764,451			1,764,451
Health Care and Other Amounts Receivable	2,796,471	389,717(R) 188,015(R)	2,901,927(R)	472,276
Total Assets	<u>\$234,806,754</u>	<u>\$1,703,895</u>	<u>\$9,566,965</u>	<u>\$226,943,684</u>
LIABILITIES				
Claim Unpaid	\$116,896,781	\$2,901,927(R)	\$1,947,327(A)	\$115,942,181
Accrued Medical and Other Incentive Pool	7,308,807			7,308,807
Unpaid Claims Adjustment Expenses	805,975			805,975
Aggregate Health Policy Reserves	6,546,446			6,546,446
Aggregate Health Claims Reserves	2,019,186			2,019,186
Premium Receivable in Advance	152,921			152,921
General Expenses Due and Accrued	10,629,701			10,629,701
Amounts withheld or Retained	1,478,351			1,478,351
Remittances and Items Not Allocated	48,979			48,979
Liability for Amounts Held under Uninsured	(188,015)		188,015(R)	0
Aggregate Write-in for Others Liabilities	5,019,735	3,790,753(R)	658,820(R) 600,000(A)	2,487,802
Total Liabilities	<u>\$150,718,867</u>	<u>6,692,680</u>	<u>3,394,162</u>	<u>\$147,420,349</u>
CAPITAL AND SURPLUS				
Gross Paid in and Contributed Surplus	27,107,930			27,107,930
Unassigned Surplus	56,837,432	4,564,552		52,272,880
Total Capital and Surplus	<u>\$84,087,887</u>	<u>4,564,552</u>		<u>\$79,523,335</u>
TOTAL LIABILITIES, CAPITAL AND SURPLUS	<u>\$234,806,754</u>	<u>\$11,257,232</u>	<u>\$3,394,162</u>	<u>\$226,943,684</u>

⁵ This account includes the amount of \$3,093,139 with a maturity date of one year or less. The Organization shall classify these Bonds as short-term investments.

HUMANA HEALTH PLANS OF PUERTO RICO
STATEMENT OF REVENUES AND EXPENSES
FOR THE YEAR ENDED DECEMBER 31, 2011

Net Premium Earned	\$917,724,977
Aggregate Write-in for Other Health Care Related	<u>2,072</u>
Total Income	\$917,727,049
Hospital/Medical Benefits	\$644,217,629
Other Professional Services	2,304,355
Outside Referrals	36,532,594
Prescription Drugs	143,905,872
Incentive Pool, Withhold Adjustments and Bonus	<u>4,687,929</u>
Subtotal	\$831,648,379
Claims Adjustment Expenses	20,155,456
General Administrative Expenses	<u>47,876,429</u>
Total Underwriting Deductions	<u>\$899,680,263</u>
Net Underwriting Gain	\$18,046,785
Net Investment Income Earned	3,286,858
Net Unrealized Capital Loss	<u>(20,505)</u>
Net Investment Gains	\$ 3,266,354
Net Income After Capital Gains Before Taxes	\$ 21,313,139
Less: Federal and Foreign Income Taxes	<u>(5,634,361)</u>
Net Income	<u>\$15,678,778</u>

HUMANA HEALTH PLANS OF PUERTO RICO
RECONCILIATION OF UNASSIGNED SURPLUS
AS OF DECEMBER 31, 2011

	<u>EXAMINATION ADJUSTMENTS</u>	<u>BALANCE</u>
Annual Report Unassigned Surplus		\$56,837,432
Cash and Cash Equivalents	467,343	
Uncollected Premiums	(809,629)	
Current Federal Income Tax Recoverable	(1,674,939)	
Claims Unpaid	(1,947,327)	
Aggregate Write-in for Others Liabilities	<u>(600,000)</u>	
Adjustments According to Examination		<u>(\$4,564,552)</u>
Examination Unassigned Surplus		<u>\$52,272,880</u>

COMMENTS AND FINDINGS OF EXAMINATION

The following are comments and findings related to some of the items shown in the Organization's Annual Statement as of December 31, 2011.

BONDS **\$96,558,406**

In the Organization's Annual Statement as of December 31, 2011, the balance for this account was \$96,558,406. The balance of these assets represent the amortized value of investments acquired by the Organization.

The Organization complied with the provisions of Section 6.060 (1) of the Insurance Code of Puerto Rico and the SSAP No. 26 of the Accounting Practice and Procedure Manual of NAIC, and registered its bonds at amortized cost. The investment balances were confirmed without exceptions.

The investments as of December 31, 2011, were held by Citibank, N.A. and UBS Financial Services Incorporate of Puerto Rico. The Organization investments are distributed as follows:

US Treasury Securities	\$3,101,632
US Government Agencies	24,494,976
State Territories	1,343,318
FNMA	29,589,177
Others	2,298,267
Corporations	35,731,036
Total	<u>\$96,558,406</u>

CASH AND CASH EQUIVALENTS **\$49,640,659**

As of December 31, 2011, the Organization maintained ten (10) banks accounts, which were validated by bank confirmation with different financial institutions:

ACCOUNT NUMBER	DESCRIPTION	BALANCE	BANK
10101	Premium #1	\$54,478	BPPR
10116	Claims Disbursement	(3,790,753)	Citibank
10139	Operating #1	49,401,894	BBVA
10141	Concentration #1	240,357	Citibank
10142	Concentration #2	9,947	Citibank
10158	BlackRock#1	1,569,605	Citibank
10159	BlackRock#2	215,926	Citibank
10175	Petty Cash	1,500	
10234-10236	Cash Equivalents	<u>1,278,884</u>	Citibank
	Total	<u>\$48,981,838</u>	

The bank reconciliations prepared by the Organization were verified and no exceptions were noticed. The cash balance accounts were confirmed by the banks and the investment manager BlackRock, Inc.

In this examination we reclassified the amount of \$658,821 from cash account number 10139 to the reserve for unclaimed funds since the amount corresponded to outstanding checks with more than (1) one year.

We observed that the Organization prepared adjusted entries to the cash accounts, after filing of the 2011 Annual Statement, to correct the balance of the account by \$467,363. We are including this adjustment in this examination.

The Organization presented a negative balance of cash account 10116, Claims Disbursements, as a liability in the Aggregate Write-in for Other Liabilities. In this examination we are reclassifying the amount of (\$3,790,753) to Cash and Cash Equivalents account as required in the SSAP No. 2 of the Accounting Practices and Procedures Manual for a total examination balance of \$49,640,659.

UNCOLLECTED PREMIUMS

\$71,298,800

The balance shown by the Organization in the 2011 Annual Statemet was \$72,498,146. The balance presented in the Annual Statement included amounts that were not uncollected premiums. The Organization made some reclassifications from this account to the Health Care and Other Amounts Receivables account in the amount of \$389,717, and other accounting adjustments for the amount of \$809,629, after submission of the 2011 Annual Statement. In this examination, we are including the reclassifications and adjustments made by the Organization to set up the correct balance of the account which is \$71,298,800.

Furthermore, during the examination, we reviewed the Uncollected Premiums Aging Report against the billing premiums in order to ascertain accurate and correctiveness and no exeptions were noticed.

CURRENT FEDERAL AND FOREING INCOME TAX RECOVERABLE

\$3,638,992

As of December 31, 2011, the Organization presented a balance of \$5,313,931, in the Annual Statement. This balance was adjusted by external auditors by \$1,674,939 to present the corrected balance of the account of \$3,638,992. In this exam we are including this adjustment to correct the Current Federal and Foreing Income Tax Recoverable.

HEALTH CARE AND OTHER AMOUNTS RECEIVABLES

\$472,276

As of December 31, 2011, the Organization presented a balance of \$2,796,471, in the Annual Statement. After the Annual Statement was sumitted, the Organization made the followings reclasifications:

Annual Statement Balance	\$2,796,471
Reclass	\$188,015
	389,717
	(2,901,927)
	<u>(\$2,324,195)</u>
Adjusted Balance	<u>\$472,276</u>

The Organization made some reclassifications from the Uncollected Premiums to this account, in the amount of \$389,717. This amount represents an accounts receivable from CMS and Medicare Retroactivity. The amount of \$ 188,015 was reclassified to the Health Care and Other Amounts Receivable. In this examination report we are including these reclassifications of accounts.

Another reclassifications were \$2,900,000 for Providers Receivable balance and \$1,927, was adjusted by the external auditors.

CLAIMS UNPAID **\$115,942,181**

The Organization established a reserve for reported losses and incurred but not reported cases (IBNR) in the amount of \$116,896,781. To determine the reasonability of the unpaid claims in compliance with the provisions of Section 5.020 and 5.050(2) of the Insurance Code of Puerto Rico, we performed an analysis considering the payments made by the Organization from January 1, 2012 until December 31, 2012, with dates of services on or before December 31, 2011, and claims outstanding to be paid, in which the dates of claims services were reported on December 31, 2011 or prior. We also reviewed the development of the reserve in the quarterly and annual reports prepared

by the Organization for the year 2012. The analysis showed that the estimate should be increased in the amount of \$1,947,327. Below is the result of the analysis:

Description	Amount
Annual Statement Reserve at December 31, 2011	\$116,896,781
Reclassification -Payment	2,901,927
Adjusted Reserve at December 31, 2011	\$113,994,854
Claims Paid from January 1, 2012 to December 31, 2012 of year 2011	\$106,941,947
Claims Unpaid of year 2011 at December 31, 2012	9,000,234
Total losses Developed as of December 31, 2012	115,942,181
Claims Reserve Deficiency	(\$1,947,327)

In this examination, we included the payment for the amount of \$2,900,000 at December 27, 2011, and the amount of \$1,927 as previously commented under the Health Care and Other Receivable.

AGGREGATE WRITE-INS FOR OTHER LIABILITIES **\$2,487,802**

Pursuant to Article 19.142 of the Insurance Code of Puerto Rico, to determine the financial situation of the Health Maintenance Organization, the statutory deposit shall be considered as a liability. The Organization did not present in the Annual Statement of 2011 the statutory deposit as a liability, as required by Article 19.142. We are adjusting by \$600,000 the unassigned surplus of the Organization.

Also, we are reclassifying the amount of (\$3,790,753) from Aggregate Write-ins for Others Liabilities to Cash account as required by the SSAP No. 2 of the Accounting Practices and Procedures Manual of NAIC as previously mentioned in this examination report.

We reclassified the amount of \$658,821 from Cash and Cash Equivalents to this account since these were checks that had been issued over one year.

UNASSIGNED SURPLUS

\$52,272,880

The unassigned surplus was affected by \$4,562,552 for accounting adjustments to its assets and liabilities accounts: Uncollected Premiums, Current Federal and Foreign Income Tax Recoverable, Claims Unpaid and Aggregate Write-in for Others Liabilities as discussed in this examination.

CONCLUSION

The financial situation of the Organization as of December 31, 2011, considering the examination adjustments is:

Assets	<u>\$226,943,684</u>
Liabilities	\$147,420,349
Common Capital Stock	142,525
Gross Paid in and Contributed	27,107,930
Unassigned Funds	<u>52,272,880</u>
Total Liabilities, Capital and Surplus	<u>\$226,943,684</u>

Respectfully submitted,

Maribel Figueroa Diaz
Examiner

SUMMARY OF EXAMINATION AND RECOMMENDATIONS

1. For the years 2006, 2008, 2009, 2010 and 2011, the Organization did not comply with Section 1, Article II of its By-laws, since it did not hold the annual shareholders meetings on the third Wednesday of April. Page 3 of the Examination Report.
2. For the years 2006, 2008, 2009, 2010 and 2011, the Organization failed to comply with Section 3, Article III of its By-Laws, since it did not hold the annual directors meeting on the third Wednesday of April. Page 3 of the Examination Report.
3. Section 2 of Article III of the Organization's By-laws establishes that the Board of Directors will consist of not less than five (5) and no more than thirteen (13) directors. The Organization did not comply with Section 2 of Article III of its By-laws, since the Board of Directors consisted of only four (4) directors. Page 4 of the Examination Report.
4. Article 19.120(b) of the Insurance Code of Puerto Rico requires that the complaints procedure shall include the designation of a Grievance Committee in which its members shall hold office for not less than one (1) nor more than three (3) years. The Organization did not comply with Article 19.120(b) of the Insurance Code of Puerto Rico, since two of its Grievance Committee members held office for more than three (3) years. Pages 6-7 of the Examination Report.
5. The list of the relation of stockholders for the year 2009, which was submitted to the OCI on February 17, 2010, included an error in the number of stock owned by Humana, Inc. The Organization noticed the error and filed an amended list of

stockholders on May 4, 2010. Prior to submitting to the OCI any and all information required by disposition of law, the Organization should be more diligent in reviewing said information in order to rule out any errors. Page 7 of the Examination Report.

6. The Organization submitted the Annual Statement for the year ended on December 31, 2007 on April 1, 2008, 2011, thus failing to comply with Article 19.090(1) of the Insurance Code of Puerto Rico. Pages 9-10 of the Examination Report.
7. The Organization did not submit the Management Discussions and Analysis (MD&A), thus not complying with the Annual Statement Instructions published for health services organizations. Pages 9-10 of the Examination Report.
8. Schedule E of the Annual Statement for the year ended on December 31, 2011, was not completed properly and did not include a breakdown of all cash accounts held by the Organization, as required in the Annual Statements Instructions. Pages 9-10 of the Examination Report.
9. For the years 2006, 2008, 2009, 2010 and 2011, the Organization did not include the Notes to Financial Statements in the Annual Statement, not complying with the Annual Statement Instructions published for health services organizations. Pages 9-10 of the Examination Report.
10. The Organization made some reclassifications and adjustments on its Annual Statement as of December 31, 2011, after the release and presentation of said Statement to the OCI. However, the Organization did not present the Amended

Annual Statement as required by Ruling Letter NE-3-74-94, dated April 12, 1994.
Page 10 of the Examination Report.

11. Mr. P. Anthony Hammond, MAAA, ASA was elected as Director of the Organization on April 5, 2011 and remained in this position until July 23, 2012. Mr. Hammond is also Vice President Risk & UM, Chief Actuary for Humana, Inc. and is the appointed actuary to certify and present the actuarial opinion for the Organization. In order to avoid any conflict of interest, in the future the Organization shall comply with Precept 7 of the Code of Professional Conduct for Actuaries. Pages 10-11 of the Examination Report.
12. The Organization did not submit the communication of internal controls related matters, noted in the audit of December 31, 2010 and December 31, 2011 prepared by the external auditors, thus failing to comply with Section 11(A) of Rule 14-A of the Regulations of the Insurance Code of Puerto Rico. Pages 11-12 of the Examination Report.
13. The Organization failed to comply with Sections 13 and 14 of Rule 83 of the Regulations of the Insurance Code of Puerto Rico, since it did not submit to the OCI the Annual Registration - Form B and the Summary of Registration - Form C for the year 2011. Pages 12-14 of the Examination Report.
14. Article 26.040(1) of the Insurance Code of Puerto Rico requires that every insurer, on or before May 1st of each year, submit a written report to the Commissioner on all unclaimed funds withheld. The Organization submitted the unclaimed

funds report as of December 31, 2007 on May 14, 2008, thus not complying with the aforesaid regulatory disposition. Page 13 of the Examination Report.

15. The Organization did not clearly demonstrate the process of the transactions between itself and its affiliates, therefore the OCI could not validate if the distribution of expenses were fair and reasonable in accordance with SSAP No. 25 of the Accounting Practice and Procedures Manual of the NAIC. The Organization did not comply with Article 19.180(3) of the Insurance Code of Puerto Rico and Rule 9 of the Regulations of said Code, as it did not maintain accounting records of the intercompany account. Pages 15-17 of the Examination Report.
16. After filing its 2011 Annual Statement, the Organization made adjusted entries to the cash account, in order to rectify the balance of the account by \$467,363. The OCI included this adjustment in its examination. Pages 23-24 of the Examination Report.
17. The OCI reclassified the amount of \$658,821 corresponding to outstanding checks of more than one year in Cash and Cash Equivalent account to the Aggregate Write-in for Other Liabilities. The OCI also reclassified \$3,790,753 from Aggregate Write-in for Others Liabilities to Cash and Cash Equivalents account, as required by SSAP No. 2 of the Accounting Practices and Procedures Manual. Pages 23-24 of the Examination Report.
18. The Organization made a reclassification from Uncollected Premiums to Health Care and Other Amounts Receivable in the amount of \$389,717 and another

- accounting adjustment in the amount of \$809,629, after it submitted its 2011 Annual Statement. Page 25 of the Examination Report.
19. In its Annual Statement, the Organization presented a balance of \$5,313,931 as Current Federal and Foreign Income Tax Recoverable. This balance was adjusted by external auditors by \$1,674,939 to present the corrected balance. Page 25 of the Examination Report.
 20. The amount of \$188,015 was reclassified to the Health Care and Other Amounts Receivable. Other reclassifications were \$2,900,000 for Providers Receivable balance and \$1,927 was adjusted by the external auditors. In this examination report the OCI included these reclassifications of accounts. Pages 25 and 26 of the Examination Report.
 21. In compliance with the provisions of Articles 5.020 and 5.050(2) of the Insurance Code of Puerto Rico, the OCI adjusted the unpaid claims reserve in the amount of \$1,947,327. Pages 26 and 27 of the Examination Report.
 22. The Organization did not present in its Annual Statement for the year 2011 the statutory deposit as a liability, as required by Article 19.142 of the Insurance Code of Puerto Rico. The OCI adjusted the amount of \$600,000 against the unassigned surplus of the Organization. Page 27 of the Examination Report.
 23. The Organization's Unassigned Surplus was reduced in the amount of \$4,562,552 due to accounting adjustments to certain assets and liabilities accounts. Page 28 of the Examination Report.

SCHEDULE I

SERVICES AGREEMENT

The followings are the services to be rendered under the service agreement to Humana

Insurance:

1. Claims Processing
2. Customer and Provider Services
3. Front End Operations
4. Enrollment
5. Billing and Collections
6. Utilization Review and Actuarial
7. Case and Disease Management and clinical affairs functions.
8. Pharmacy
9. Legal, Grievances and Appeals functions.
10. Other Support including senior leadership, education and development, financial management, human resources, systems administration and information technology, and other administrative functions.
11. Costs directly related to the above such benefits, payroll taxes, and occupancy.

SCHEDULE II

1. The allocation of expenses is mainly driven by the workload of each area/unit. The Financial Planning team will review the allocation of each area on an annual basis to ensure updated data is used for the allocation process.
2. Key drivers are identified in selected areas to provide accurate distribution to each line of business. Areas without an identifiable driver are based on the overall normal operation, as provided by the each corresponding leader.
3. After determining a ratio or percentage for each line of business, the distribution is allocated to each product based on membership and from there it flows to each legal entity.
4. In the distribution process the nature of the expenses is also taken in consideration, as some expenses are not allowed for some lines of business.
5. The whole allocation process is made by Admin Allocation Tool that manages the dollar distribution.
6. The costs allocation process were prepared in electronic process and during our examination it was not possible to analyze the allocation of costs since the organization did not provide the analysis made by the Administration to establish the parameters of the allocations of costs. The internal reconciliations in the relevant intercompany accounts of the Humana and the Organization were not available during the examination.

