

REPORT OF EXAMINATION
OF THE
BLUE SHIELD OF CALIFORNIA LIFE & HEALTH
INSURANCE COMPANY
AS OF
DECEMBER 31, 2015

Filed on April 3, 2017

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San Francisco, California
February 10, 2017

Honorable Dave Jones
Insurance Commissioner
California Department of Insurance
Sacramento, California

Dear Commissioner:

Pursuant to your instructions, an examination was made of the

BLUE SHIELD OF CALIFORNIA LIFE & HEALTH INSURANCE COMPANY

(hereinafter also referred to as the Company) at its home office located at 50 Beale Street, San Francisco, California 94105.

SCOPE OF EXAMINATION

We have performed our single-state examination of the Company. The previous examination of the Company was as of December 31, 2011. This examination covered the period from January 1, 2012 through December 31, 2015.

The examination was conducted in accordance with the National Association of Insurance Commissioners *Financial Condition Examiners Handbook (Handbook)*. The Handbook requires the planning and performance of the examination to evaluate the Company's financial condition, assess corporate governance, identify current and prospective risks, and evaluate system controls and procedures used to mitigate those risks. An examination also includes identifying and evaluating significant risks that could cause an insurer's surplus to be materially misstated both currently and prospectively.

All accounts and activities of the Company were considered in accordance with the risk-focused examination process. This may include assessing significant estimates made

by management and evaluating management's compliance with Statutory Accounting Principles. The examination does not attest to the fair presentation of the financial statements included herein. If, during the course of the examination, an adjustment is identified, the impact of such adjustment will be documented separately following the Company's financial statements.

This examination report includes findings of fact and general information about the Company and its financial condition. There might be other items identified during the examination that, due to their nature (e.g., subjective conclusions, proprietary information, etc.), were not included within the examination report but separately communicated to other regulators and/or the Company.

The examination was conducted concurrently with the examination of the Company's affiliate, CareAmerica Life Insurance Company.

COMPANY HISTORY

In 2012 and 2013, the Company received capital contributions of \$80,000,000 and \$59,689,775 respectively, from its parent, California Physicians' Service (d.b.a. Blue Shield of California).

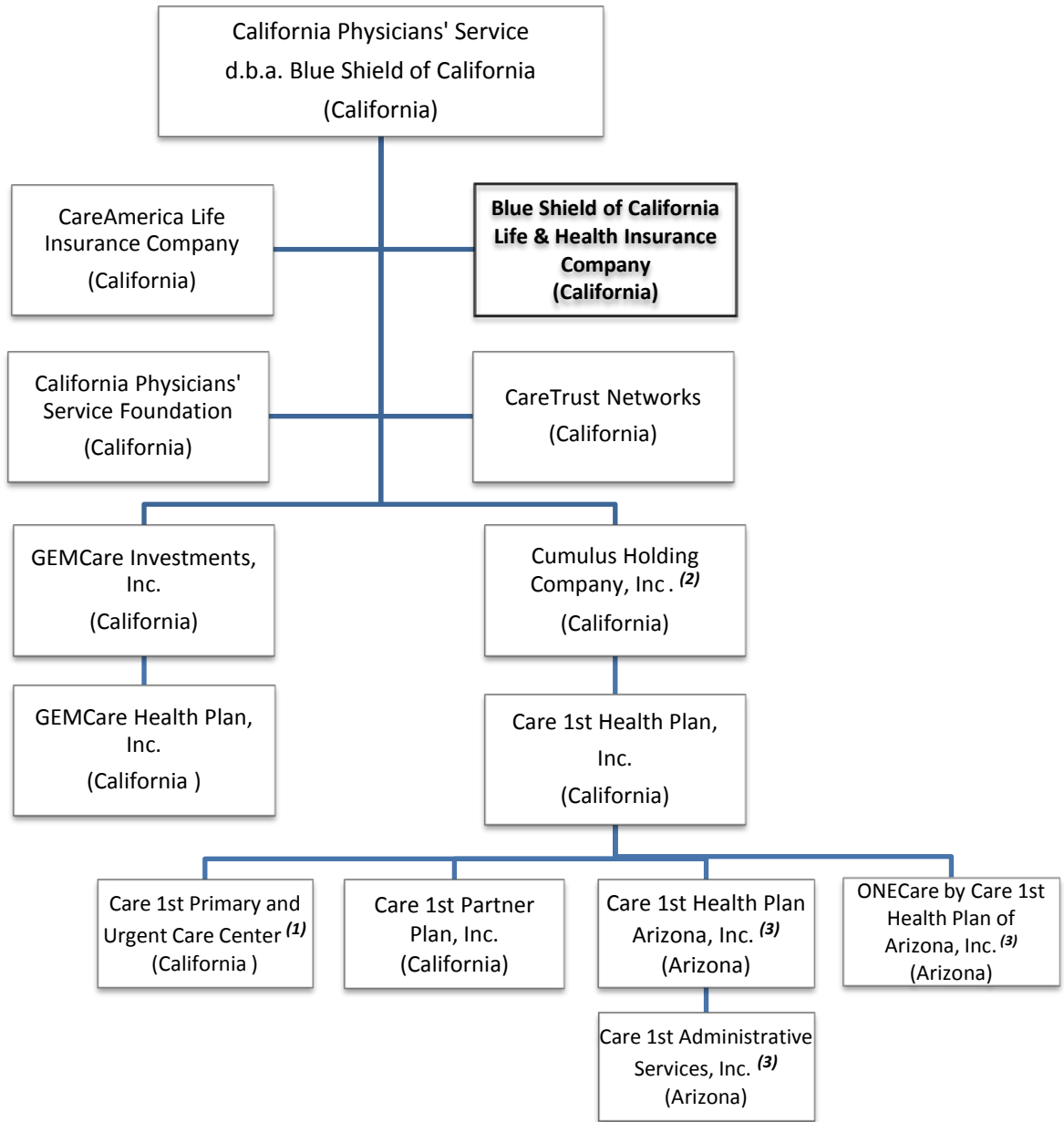
Capitalization

The Company is authorized to issue 6,000 shares of common stock with a par value of \$1,000 per share. As of December 31, 2015, there were 2,500 shares issued and outstanding.

MANAGEMENT AND CONTROL

The Company is a member of an insurance holding company system of which California Physicians' Service (d.b.a. Blue Shield of California) is the ultimate controlling

entity. The following organizational chart depicts the relationships of the companies within the holding company system as of December 31, 2015 (all ownership is 100%):



⁽¹⁾ Effective June 28, 2016, Care 1st Primary and Urgent Care Center was dissolved.

⁽²⁾ Effective August 19, 2016, Cumulus Holding Company, Inc. changed its name to FullSpan Holding Company, Inc.

⁽³⁾ ONECare by Care 1st Health Plan of Arizona, Inc., Care 1st Health Plan Arizona, Inc., and Care 1st Administrative Services, Inc. were sold on December 31, 2016.

The ten members of the Board of Directors, who are elected annually, oversee the business and affairs of the Company. Following are members of the Board and principal officers of the Company serving at December 31, 2015:

Directors

<u>Name and Location</u>	<u>Principal Business Affiliation</u>
Douglas F. Busch Penryn, California	Retired
Evelyn S. Dilsaver San Leandro, California	Retired
Helen M. DuPlessis, M.D. Lakewood, California	Chief Medical Officer St. John's Well Child and Family Center
Hector Flores, M.D. Los Angeles, California	Medical Director Family Care Specialists Medical Group, Inc.
Alan J. Fohrer Arcadia, California	Retired
Robert C. Lee* Moraga, California	Retired
Kristina M. Leslie Los Angeles, California	Retired
Paul S. Markovich San Francisco, California	President and Chief Executive Officer California Physicians' Service
Leon E. Panetta Monterey, California	Retired
Mohammad H. Qayoumi, Ph.D. San Jose, California	Retired

Note: The number of the Board members increased to twelve effective August 19, 2016. Sharon K. Belshé, Mari J. Baker and William Glaser were added to the Board.

** Effective October 31, 2016, Robert C. Lee retired as a Board member.*

Principal Officers

<u>Name</u>	<u>Title</u>
Kenneth Wood ⁽¹⁾	President and Chief Executive Officer
Seth A. Jacobs, Esq.	Secretary
Emily R. Glidden	Treasurer
Michelle Simpson ⁽²⁾	Vice President
Andrea DeBerry	Assistant Secretary
Michael Stuart	Controller

⁽¹⁾ Effective May 3, 2016, Kenneth Wood resigned as the President and Chief Executive Officer, and was replaced by Jeffrey Smith on the same date.

⁽²⁾ Effective March 31, 2016, Michelle Simpson resigned as Vice President, and was replaced by Daniel Prettyman effective May 3, 2016.

Note: Effective February 23, 2016, Devin Gensch was elected as an additional Assistant Secretary.

Management Agreements

Administrative Services Agreements: Effective October 1, 2003, the Company entered into an Administrative Services Agreement with its parent, Blue Shield of California (BSC). Under the terms of the Agreement, BSC provides the Company with personnel services, facilities, information systems, administrative and operational support on an actual cost basis. The Agreement was approved by the California Department of Insurance (CDI) on September 13, 2004. This Agreement had been revised three times, with each revision submitted to and approved by the CDI on August 17, 2004; December 27, 2005; and May 25, 2010. The total fees incurred by the Company for services under this Agreement were: \$379,284,352; \$436,486,428; \$102,124,805; and \$60,320,591 for 2012, 2013, 2014, and 2015, respectively.

Tax Allocation Agreement: Effective July 21, 2011, the Company entered into a Tax Allocation Agreement with BSC and its affiliates, CareAmerica Life Insurance Company and CareTrust Networks, for the purpose of filing a consolidated federal income tax return. The Agreement provides for separate income tax return calculations with credit

for net losses that can be used on a consolidated basis. The Agreement was filed with the CDI on May 11, 2011, and approved on August 14, 2012.

Effective July 31, 2014, GEMCare Investments, Inc. and GEMCare Health Plan, Inc. were added to the Tax Allocation Agreement. Effective January 1, 2016, as a result of additional acquisition, the following entities were also added as parties to the Agreement: (i) Cumulus Holding Company, Inc.; (ii) Care 1st Health Plan, Inc.; (iii) Care 1st Health Plan Arizona, Inc.; (iv) ONECare by Care 1st Health Plan of Arizona, Inc.; (v) Care 1st Administrative Services, Inc.; and (vi) Care 1st Primary and Urgent Care Center.

TERRITORY AND PLAN OF OPERATION

The Company is licensed and operates exclusively in California. It writes ordinary life, group life; and group and other accident and health insurance. Direct premiums written in 2015 by line were as follows: Ordinary and group life combined were \$8,963,808 (0.7%); group accident and health was \$1,055,102,737 (83.2%); and other accident and health was \$204,088,727(16.1%).

The Company has no direct employees. Employees of Blue Shield of California (BSC), the Company's parent, manage the affairs of the Company. The Company markets through independent agents and brokers, and directly through the distribution system of BSC. Accident and health products offered by the Company included Preferred Provider Organization (PPO) health plans for individuals, and for small, midsize and large employer groups; as well as vision, dental, and stop-loss coverage during the examination period.

Effective January 1, 2014, the Company opted out of its participation in the Covered California Health Exchange, which was created to assist citizens and legal residents with applying for marketplace coverage in order to comply with the federal Patient Protection and Affordable Care Act and Health Care and Education Reconciliation Act

of 2010, (collectively, "Health Care Reform"). As a result, the Company's non-grandfathered individual and small group medical plans were replaced by Health Care Reform compliant plans offered by its parent, BSC, or other health insurers. Effective December 1, 2015, the Company ceased to offer small group PPO health plans, which used to be the Company's largest membership base.

REINSURANCE

Assumed

The Company has no assumed reinsurance.

Ceded

The following table is an outline of the Company's ceded reinsurance programs as of December 31, 2015. All reinsurers are authorized.

Line of Business and Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Limit
<u>Life:</u>			
Excess Group Life and Accidental Death and Dismemberment (AD&D)	Swiss Re Life & Health America Inc.	For Group Life: \$200,000 per person For Group AD&D: \$200,000 per person	\$1 million per person excess of \$200,000
<u>Accident and Health:</u>			
Specific Excess of Loss – Medical Stop Loss for Self-Funded Groups	Swiss Re Life & Health America, Inc.	\$3 million ultimate net loss for each covered person, per policy period	Unlimited excess of \$3 million ultimate net loss for each covered person, per policy period

Line of Business and Type of Contract	Reinsurer's Name	Company's Retention	Reinsurer's Limit
Mental Health and Substance Abuse Quota Share	Magellan Life Insurance Company	None	All charges for covered services after the application of network discounts and net of Members' copayments, coinsurance, and deductibles.

CORPORATE RECORDS

Insurance Holding Company System Annual Registration Statement

Effective January 1, 2013, statements that the Board of Directors is responsible for overseeing corporate governance and internal controls and that the insurer's officers or senior management have approved, implemented, and continue to maintain and monitor corporate governance and internal control procedures are required to be included in the Insurance Holding Company System Annual Registration Statement (Form B) filed with the California Department of Insurance (CDI) pursuant to California Insurance Code (CIC) Section 1215.4(b)(6). It was noted that the Form B filings on April 22, 2013; April 15, 2014; April 1, 2015; and April 12, 2016 did not include the required statements. It is recommended that the Company include the required statements in its future Form B filings in accordance with CIC Section 1215.4(b)(6).

Annual Statement Instructions

Pursuant to the National Association of Insurance Commissioners (NAIC) Annual Statement Instructions, the Appointed Actuary must report to the Company's Board of Directors or the Audit Committee each year on the items within the scope of the Actuarial Opinion and the minutes of the Board of Directors shall indicate as such. During the course of the examination, it was noted that the Appointed Actuary did not report to the Board of Directors or the Audit Committee those items within the scope of the Actuarial Opinion, nor was there indication in the Board minutes that such report by

the Appointed Actuary was made. It is recommended that the Company implement procedures to ensure future compliance with the NAIC Annual Statement Instructions.

Annual Information Statement

An Annual Information Statement is required to be filed by the Company annually in order to establish the Company's continuing qualification to hold a California Certification of Authority. The Company is responsible for providing updated information in the Annual Information Statement filed with the CDI. It was noted that the Company amended and restated its Bylaws, effective November 13, 2012. However, such information was not reflected in the Annual Information Statements filed with the CDI from 2013 to 2016. It is recommended that the Company provide updated and accurate information in the Annual Information Statement filings.

FINANCIAL STATEMENTS

The following financial statements are based on the statutory financial statements filed by the Company with the California Department of Insurance and present the financial condition of the Company for the period ending December 31, 2015. The accompanying comments to the amounts reported in the annual statements should be considered as an integral part of the financial statements. There were no examination adjustments made to surplus as a result of the examination.

Statement of Financial Condition as of December 31, 2015

Summary of Operations and Capital and Surplus Account for the Year Ended
December 31, 2015

Reconciliation of Capital and Surplus from December 31, 2011 through
December 31, 2015

Statement of Financial Condition
as of December 31, 2015

<u>Assets</u>	<u>Ledger and Nonledger Assets</u>	<u>Assets Not Admitted</u>	<u>Net Admitted Assets</u>	<u>Notes</u>
Bonds	\$ 574,022,218	\$	\$ 574,022,218	
Cash and short-term investments	20,297,883		20,297,883	
Contract loans	22,867		22,867	
Receivable for securities	19,059		19,059	
Investment income due and accrued	2,150,697		2,150,697	
Uncollected premiums and agents' balances In the course of collection	15,376,421	2,070,385	13,306,036	
Deferred premiums, agents' balances and installments Booked but deferred and not yet due	4,956		4,956	
Amount recoverable from reinsurers	1,515,992	1,515,992	0	
Other amounts receivable under reinsurance contracts	406,411	406,411	0	
Current federal and foreign income tax recoverable and interest thereon	8,935,827		8,935,827	
Net deferred tax asset	6,873,176	3,155,705	3,717,471	
Receivables from parent, subsidiaries and affiliates	30,267,885		30,267,885	
Aggregate write-ins for other than invested assets	<u>12,675,113</u>	<u>256,359</u>	<u>12,418,754</u>	
 Total assets	 <u>\$ 672,568,503</u>	 <u>\$ 7,404,851</u>	 <u>\$ 665,163,651</u>	
 <u>Liabilities, Surplus and Other Funds</u>				
Aggregate reserve for life contracts			\$ 2,377,091	(1)
Aggregate reserve for accident and health contracts			44,061,444	(1)
Liability for deposit-type contracts			58,339	
Contract claims: Life			7,909,323	(1)
Contract claims: Accident and health			89,531,501	(1)
Premiums and annuity considerations for life and accident and health received in advance			17,808,754	
Provision for experience rating refunds			15,051	
Other amounts payable on reinsurance			1,922,403	
Interest Maintenance Reserve			9,216,773	
Commissions to agents due or accrued-life and annuity contracts			3,298,737	
General expenses due or accrued			1,821,488	
Taxes, licenses and fees due or accrued			4,012,620	
Asset valuation reserve			1,719,136	
Payable to parent, subsidiaries and affiliates			18,184	
Aggregate write-ins for liabilities			<u>244,965</u>	
 Total liabilities			 184,015,812	
 Common capital stock		 \$ 2,500,000		
Gross paid-in and contributed surplus		449,882,144		
Aggregate write-ins for special surplus funds		4,253,109		
Unassigned funds (surplus)		<u>24,512,585</u>		
 Capital and Surplus			 <u>481,147,839</u>	
 Total liabilities, surplus and other funds			 <u>\$ 665,163,651</u>	

Summary of Operations and Capital and Surplus Account
for the Year Ended December 31, 2015

Summary of Operations

Premiums and annuity considerations	\$ 1,249,241,776
Net investment income	14,588,658
Amortization of interest maintenance reserve	3,665,601
Commission and expense allowances on reinsurance ceded	<u>1,122</u>
 Total	 <u>1,267,497,157</u>
 Death benefits	 8,124,716
Disability benefits and benefits under accident and health contracts	916,546,035
Surrender benefits and withdrawals for life contracts	7,491
Increase in aggregate reserves for life and accident and health contracts	(375,965)
Commissions on premiums, annuity considerations and deposit-type contract funds	88,532,096
General insurance expenses	122,899,140
Insurance taxes, licenses and fees, excluding federal income taxes	66,283,294
Increase in loading on deferred and uncollected premiums	<u>2,239</u>
 Total	 <u>1,202,019,047</u>
 Net gain from operations before federal income taxes	 65,478,110
Federal and foreign income taxes incurred	<u>25,598,105</u>
 Net gain from operations after federal income taxes	 39,880,005
Net realized capital loss	<u>(397,855)</u>
 Net income	 <u>\$ 39,482,150</u>

Capital and Surplus Account

Capital and surplus, December 31, 2014	\$ 444,347,188
Net income	\$ 39,482,150
Change in net unrealized capital losses	(1,234)
Change in net deferred income tax	(2,858,989)
Change in nonadmitted assets	(746,568)
Change in asset valuation reserve	<u>925,291</u>
 Net change in capital and surplus for the year	 <u>36,800,651</u>
 Capital and surplus, December 31, 2015	 <u>\$ 481,147,839</u>

Reconciliation of Capital and Surplus
from December 31, 2011 through December 31, 2015

Capital and surplus, December 31, 2011 per Examination			\$229,856,345
	<u>Gain in Surplus</u>	<u>Loss in Surplus</u>	
Net income	\$ 111,203,924	\$	
Change in net unrealized capital losses		1,234	
Change in net deferred income tax		17,715,472	
Change in nonadmitted assets	18,231,148		
Change in asset valuation reserve		473,994	
Cumulative effect of changes in accounting principles	357,347		
Surplus adjustments: Paid-in	<u>139,689,775</u>		
Total gains and losses	<u>\$ 269,482,194</u>	<u>\$ 18,190,700</u>	
Net increase in capital and surplus			<u>251,291,494</u>
Capital and surplus, December 31, 2015, per Examination			<u>\$481,147,839</u>

COMMENTS ON FINANCIAL STATEMENT ITEMS

- (1) Aggregate Reserve for Life Contracts
Aggregate Reserve for Accident and Health Contracts
Contract Claims: Life
Contract Claims: Accident and Health

Pursuant to California Insurance Code Section 733(g), California Department of Insurance (CDI) actuaries performed an actuarial review of the aggregate reserves for the above liability accounts. Based on the review, the Company's reserves as of December 31, 2015 were found to be reasonably stated and have been accepted for purposes of this examination.

SUBSEQUENT EVENTS

On May 3, 2016, the Company declared \$180,000,000 extraordinary dividends payable to its parent, Blue Shield of California, which comprised of a return of capital of \$146,870,000 and a dividend of \$33,130,000. The distribution was subsequently made on June 30, 2016. The California Department of Insurance approved this extraordinary dividend on June 24, 2016.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Current Report of Examination

Corporate Records - Insurance Holding Company System Annual Registration Statement (page 8): It is recommended that the Company include the required statements in its future Insurance Holding Company System Annual Registration Statement filings in accordance with California Insurance Code Section 1215.4(b)(6).

Corporate Records - Annual Statement Instructions (page 8): It is recommended that the Company implement procedures to ensure future compliance with the National

Association of Insurance Commissioners Annual Statement Instructions in regard to the presentation by the Appointed Actuary to the Board of Directors or the Audit Committee.

Corporate Records - Annual Information Statements (page 9): It is recommended that the Company provide updated and accurate information in the Annual Information Statement filings.

Previous Report of Examination

None.

ACKNOWLEDGMENT

Acknowledgment is made of the cooperation and assistance extended by the Company's officers and Blue Shield of California's employees during the course of this examination.

Respectfully submitted,

/S/ _____

Mei Gu, CFE
Examiner-In-Charge
Senior Insurance Examiner
Department of Insurance
State of California

/S/ _____

Kyo Chu, CFE
Senior Insurance Examiner, Supervisor
Department of Insurance
State of California