

Report on Examination
of
Blue Cross and Blue Shield of Florida, Inc.
Jacksonville, Florida
as of
December 31, 2011



**FLORIDA OFFICE OF
INSURANCE REGULATION**

Kevin M. McCarty, Commissioner
Florida Office of Insurance Regulation
Tallahassee, Florida

Dear Sir:

In accordance with Section 624.316, Florida Statutes, and the *Financial Condition Examiners Handbook* of the National Association of Insurance Commissioners, we have completed a financial condition examination of Blue Cross and Blue Shield of Florida, Inc. as of December 31, 2011. Our report on the examination follows.

Florida Office of Insurance Regulation
February 12, 2013

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SCOPE OF EXAMINATION

We have completed a financial condition examination as of December 31, 2011 of Blue Cross and Blue Shield of Florida, Inc. (the "Company"), a single-state insurer domiciled in Florida. The last financial condition examination of the Company by the Florida Office of Insurance Regulation (the "Office") was as of December 31, 2006. The current examination covered the period of January 1, 2007 through December 31, 2011 and took place primarily in the Company's Jacksonville, Florida office.

We conducted our examination in accordance with the National Association of Insurance Commissioners (NAIC) *Financial Condition Examiners Handbook*. The Handbook required that we plan and perform our examination to evaluate the financial condition and identify prospective risks of the Company. It required that we do so 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. Our examination included assessing the principles used and significant estimates made by management. It also included evaluating overall financial statement presentation and 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.

COMPANY HISTORY

On July 1, 1980, the Company was incorporated in Florida and licensed by the Office as an insurer. It was authorized to operate as an accident and health insurer in accordance with Section 624.401, Florida Statutes (F.S.).

CORPORATE RECORDS

We reviewed the minutes of meetings held by the Company's members and board of directors, and by its audit and compliance, board governance and nominating, finance, and personnel and compensation committees. The Board's approval of Company transactions, including the authorization of its investments as required by Section 625.304, F.S., was recorded in the minutes of its meetings.

MANAGEMENT AND CONTROL

The Company was governed by a board of directors elected by the Company's members. Each holder of an in force insurance policy issued by the Company was a member of the Company. Its senior officers, directors, and members of principal board committees were:

Senior Officers

Name	Title
Patrick J. Geraghty	Chief Executive Officer and President
R. Chris Doerr	Executive Vice President, Chief Administrative Officer and Chief Financial Officer
Charles S. Joseph	Senior Vice President, General Counsel and Corporate Secretary
William A. Coats	Vice President, Chief Investment Officer and Treasurer
Cyrus M. Jollivette	Senior Vice President, Public Affairs
James C. Modaff	Vice President and Chief Actuary
Robert E. Wall	Senior Vice President, Human Services

Board of Directors

Name	Location
Robert M. Beall, II	Bradenton, Florida
Catherine P. Bessant	Charlotte, North Carolina
Patrick J. Geraghty	Ponte Vedra Beach, Florida
Steven T. Halverson	Jacksonville, Florida
Leerie T. Jenkins, Jr.	Jacksonville, Florida
Tracy A. Leinbach	Pinehurst, North Carolina
John B. Ramil	Tampa, Florida
Frank P. Scruggs, Jr.	Fort Lauderdale, Florida
Barbara S. Thomas	Belleair, Florida
Gonzalo F. Valdes-Fauli	Key Biscayne, Florida

Committees of the Board of Directors

Audit & Compliance

Leerie T. Jenkins, Jr.
John B. Ramil
Barbara S. Thomas
Gonzalo F. Valdes-Fauli

Board Governance & Nominating

Robert M. Beall, II
Catherine P. Bessant
Steven T. Halverson
Frank P. Scruggs, Jr.

Finance

Leerie T. Jenkins, Jr.
John B. Ramil
Barbara S. Thomas
Gonzalo F. Valdes-Fauli

Personnel & Compensation

Robert M. Beall, II
Catherine P. Bessant
Steven T. Halverson
Frank P. Scruggs, Jr.

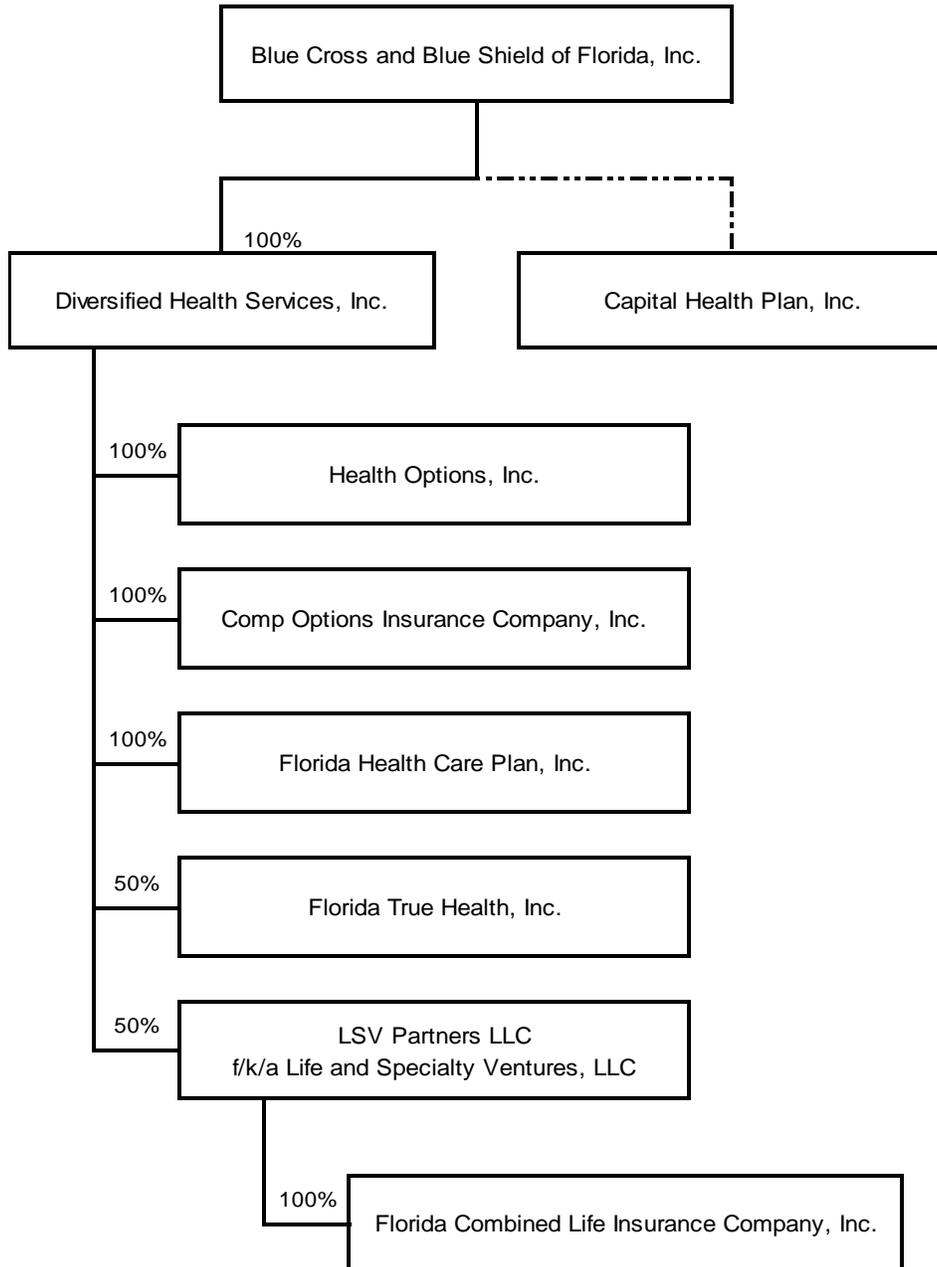
Executive

Catherine P. Bessant
Patrick J. Geraghty
Tracy A. Leinbach
John B. Ramil
Frank P. Scruggs, Jr.
Barbara S. Thomas

The Company was a member of an insurance holding company system. Its latest holding company registration statement was filed with the State of Florida as required by Section 628.801, F.S., and Rule 69O-143.046, Florida Administrative Code (F.A.C.), on May 31, 2012.

An abbreviated organizational chart reflecting a holding company system is shown below.

**Blue Cross and Blue Shield of Florida, Inc.
Abbreviated Organizational Chart
December 31, 2011**



Tax Sharing Agreement

The Company filed a consolidated federal income tax return which included the operations of certain of its affiliates pursuant to a tax sharing agreement effective January 1, 2001 and later amended. The agreement provided for the allocation of income tax liability based upon the separate taxable incomes of included companies. It also provided that an included company with a net operating loss would be reimbursed for the tax benefit associated with the loss in the year used in the group's consolidated return. Intercompany tax balances were settled annually after the filing of the consolidated return.

Administrative Services Agreement

The Company and various of its affiliates entered into an administrative services agreement effective December 31, 2007 and later amended. The agreement provided that the Company and the affiliates were entitled to provide services to and receive services from each other. The services included accounting, tax, auditing, underwriting, claims, investment, and functional support services. The agreement provided for reimbursement to affiliates providing services based on actual incurred costs or an otherwise reasonable basis.

Parental Guarantee Agreement

On March 16, 1989, the Company guaranteed that it would provide sufficient funds to assure payment of all liabilities including covered subscriber claims of Health Options, Inc. (HOI), a subsidiary health maintenance organization (HMO). In addition, it guaranteed the continuation of benefits to enrollees for the duration of any contract period for which payment has been made and to enrollees confined in an inpatient facility on the date of any HOI insolvency until their discharge, and payment to unaffiliated providers for services to covered enrollees.

Affiliation and Administration Agreement

The Company and Capital Health Plan, Inc. (CHP), a Florida not-for-profit HMO, entered into an agreement on December 4, 1981 giving the Company majority control of CHP's corporate membership. The agreement provided that the Company may supply certain administrative services and products to CHP and committed it to lend operating funds to CHP.

Accounting Agreement

The Company and CHP entered into an agreement, effective July 1, 1992, in order to manage any rating, finance, accounting, reporting, and regulatory issues arising from the administration of joint venture-type programs provided by them to group purchasers.

Anti-Fraud Investigative Services Agreement

The Company provided anti-fraud investigative services to CHP in return for monthly fees pursuant to an agreement entered into on May 1, 2000 and later amended.

FIDELITY BONDS AND OTHER INSURANCE

The Company maintained fidelity bond coverage of \$20,000,000 with a deductible of \$500,000 which adequately provided for the suggested minimum amount of coverage for the Company as recommended by the NAIC of \$4,000,000.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

The Company provided fringe benefits to eligible employees. Benefits included compensated time off and group medical and life, long-term and short-term disability, dental, and vision insurance. It also maintained a noncontributory defined benefit pension plan which provided retirement benefits to substantially all of its employees hired prior to January 1, 2007. As of January 1, 2007, the plan was closed to new entrants. Employees hired after January 1, 2007 were offered an enhanced defined contribution plan. In addition, the Company maintained for certain employees a non-qualified, unfunded supplemental pension plan, the benefits of which were frozen as of December 31, 2010. The Company provided in its December 31, 2011 financial statements for benefit obligations.

TERRITORY AND PLAN OF OPERATION

The Company was a not-for-profit mutual insurance company and independent licensee of the Blue Cross and Blue Shield Association. It was authorized as an accident and health insurer solely in the State of Florida. The Company offered a wide range of insurance products including traditional and preferred provider health insurance. Through its wholly owned subsidiary Diversified Health Services, Inc. (DHSI), the Company offered various other products. DHSI owned the HMOs Florida Health Care Plan, Inc. and HOI, and workers' compensation insurer Comp Options Insurance Company, Inc. The Company indirectly owned 50% of Florida Combined Life Insurance Company, Inc., a Florida life and accident and health insurer. In addition, the Company had a significant relationship with CHP which it controlled through its involvement with CHP's board of directors.

COMPANY GROWTH

The Company reported the following for years 2007 through 2011:

(In millions)

	2007	2008	2009	2010	2011
Member months	21.5	21.5	20.5	19.6	19.4
Year-end enrollment	1.8	1.7	1.7	1.6	1.6
Premiums	\$ 5,982.4	\$ 6,438.6	\$ 6,248.0	\$ 6,204.2	\$ 6,246.5
Total revenue	\$ 5,991.2	\$ 6,404.8	\$ 6,178.8	\$ 6,074.2	\$ 6,129.2
Underwriting deductions	\$ 6,068.8	\$ 6,358.6	\$ 6,251.2	\$ 5,805.8	\$ 6,078.6
Net income	\$ 132.6	\$ 64.2	\$ 16.8	\$ 395.0	\$ 204.2
Admitted assets	\$ 4,346.5	\$ 4,278.9	\$ 4,743.5	\$ 5,402.6	\$ 5,548.5
Liabilities	\$ 2,302.5	\$ 2,488.8	\$ 2,651.7	\$ 2,757.9	\$ 2,939.4
Capital and surplus	\$ 2,044.0	\$ 1,790.1	\$ 2,091.9	\$ 2,644.7	\$ 2,609.0

REINSURANCE

The Company ceded a portion of the risks under its long-term care insurance policies to Florida Combined Life Insurance Company, Inc. under a proportional share reinsurance agreement effective November 1, 1992. The agreement was reassigned to LifeSecure Insurance Company, a wholly owned subsidiary of Blue Cross Blue Shield of Michigan, effective October 1, 2008.

The Company ceded specific and aggregate medical excess loss risk to HM Life Insurance Company on a quota share basis under a reinsurance agreement which was effective August 1, 2008.

Under a workers' compensation reinsurance arrangement, the Company assumed risks from Comp Options Insurance Company, Inc. on excess of loss and quota share bases. Under the excess of loss provision, the Company assumed net medical losses greater than \$200,000 and less than \$5,000,000 per occurrence. Effective January 1, 2010, the Company shared proportionally in both medical and nonmedical losses.

ACCOUNTS AND RECORDS

On May 1, 1990, the Company entered into a custodial agreement with The Bank of New York providing for the holding and safekeeping of the Company's securities. We found that the agreement did not contain terms required by Rules 69O-143.042(2)(j), F.A.C., and 69O-143.042(2)(o), F.A.C., relating to maintenance of adequate insurance protection and notification to the Office of any termination or complete withdrawal of the account. However, the Company amended the agreement to include the required provisions on November 2, 2012 and its board of directors authorized the amendment on January 25, 2013.

STATUTORY DEPOSITS

The Company maintained a cash deposit of \$100,000 with the State of Florida as required by Section 624.411, F.S.

Blue Cross and Blue Shield of Florida, Inc.
Admitted Assets
December 31, 2011

Admitted Assets	Per Company	Examination Adjustments	Per Examination
Bonds	\$ 2,418,780,623	\$ -	\$ 2,418,780,623
Preferred stocks	137,207,441	-	137,207,441
Common stocks	989,514,623	-	989,514,623
Properties occupied by the company	222,615,615	-	222,615,615
Cash, cash equivalents and short-term investments	(17,038,687)	-	(17,038,687)
Other invested assets	43,229,613	-	43,229,613
Receivables for securities	779,588	-	779,588
Securities lending reinvested collateral assets	66,960,766	-	66,960,766
	3,862,049,582	-	3,862,049,582
Investment income due and accrued	24,603,430	-	24,603,430
Uncollected premiums and agents' balances	807,813,983	-	807,813,983
Deferred premiums and agents' balances	34,017,475	-	34,017,475
Accrued retrospective premiums	1,398,766	-	1,398,766
Funds held by or deposited with reinsured companies	4,652,708	-	4,652,708
Amounts receivable relating to uninsured plans	228,367,515	-	228,367,515
Current federal and foreign income tax recoverable	12,791,754	-	12,791,754
Net deferred tax asset	220,166,169	-	220,166,169
Electronic data processing equipment and software	3,154,438	-	3,154,438
Receivables from parent, subsidiaries and affiliates	12,284,005	-	12,284,005
Health care and other amounts receivable	44,802,250	-	44,802,250
Aggregate write-ins for other than invested assets	292,349,209	-	292,349,209
Total admitted assets	\$ 5,548,451,284	\$ -	\$ 5,548,451,284

Blue Cross and Blue Shield of Florida, Inc.
Liabilities, Capital and Surplus
December 31, 2011

Liabilities	Per Company	Examination Adjustments	Per Examination
Claims unpaid	\$ 507,818,626	\$ -	\$ 507,818,626
Unpaid claims adjustment expenses	21,591,487	-	21,591,487
Aggregate health policy reserves	1,272,823,381	-	1,272,823,381
Property and casualty unearned premium reserves	5,872,101	-	5,872,101
Premiums received in advance	135,966,633	-	135,966,633
General expenses due or accrued	572,217,405	-	572,217,405
Current federal and foreign income tax payable	2,873,038	-	2,873,038
Amounts withheld or retained for others	16,022,278	-	16,022,278
Remittances and items not allocated	21,061,298	-	21,061,298
Borrowed money	90,154,561	-	90,154,561
Amounts due to parent, subsidiaries and affiliates	10,550,692	-	10,550,692
Payable for securities	27,358,517	-	27,358,517
Payable for securities lending	66,960,766	-	66,960,766
Reinsurance in unauthorized companies	21,019,036	-	21,019,036
Liability for amounts held under uninsured plans	87,386,740	-	87,386,740
Aggregate write-ins for other liabilities	79,734,046	-	79,734,046
Total liabilities	2,939,410,605	-	2,939,410,605
Capital and Surplus			
Unassigned funds	2,609,040,679	-	2,609,040,679
Total capital and surplus	2,609,040,679	-	2,609,040,679
Total liabilities, capital and surplus	\$ 5,548,451,284	\$ -	\$ 5,548,451,284

Blue Cross and Blue Shield of Florida, Inc.
Statement of Revenue and Expenses
(As reported by the Company)
Year Ended December 31, 2011

Net premium income	\$ 6,246,541,146
Change in unearned premium reserves and reserve for rate credits	(124,637,090)
Aggregate write-ins for other health care related revenues	7,287,589
Total revenue	6,129,191,645
Hospital and medical benefits	3,221,540,708
Outside referrals	60,579,248
Emergency room and out-of-area	228,691,768
Prescription drugs	935,212,055
Aggregate write-ins for other hospital and medical	579,042,582
	5,025,066,361
Net reinsurance recoveries	5,232,462
Total hospital and medical	5,019,833,899
Non-health claims	9,716,632
Claims adjustment expenses	263,784,235
General administrative expenses	748,417,767
Increase in reserves for life and accident and health contracts	36,828,092
Total underwriting deductions	6,078,580,625
Net underwriting gain	50,611,020
Net investment gains	194,949,536
Aggregate write-ins for other income or expenses	7,500,554
Income before federal income tax	253,061,110
Federal income tax	48,906,175
Net income	\$ 204,154,935

Blue Cross and Blue Shield of Florida, Inc.
Statement of Changes in Capital and Surplus
Five Years Ended December 31, 2011

Capital and surplus - December 31, 2006	\$ 1,993,735,258
Net income	132,590,915
Change in net unrealized capital gains and losses	(68,946,954)
Change in net deferred income tax	71,039,321
Change in nonadmitted assets	(69,753,160)
Change in unauthorized reinsurance	(17,163,879)
Change in surplus notes	127,028
Aggregate write-ins for gains or losses in surplus	2,369,059
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Capital and surplus - December 31, 2007	2,043,997,588
Net income	64,205,513
Change in net unrealized capital gains and losses	(240,544,506)
Change in net deferred income tax	18,409,200
Change in nonadmitted assets	5,322,568
Change in unauthorized reinsurance	(640,924)
Change in surplus notes	137,984
Aggregate write-ins for gains or losses in surplus	(100,784,136)
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Capital and surplus - December 31, 2008	1,790,103,287
Net income	16,832,816
Change in net unrealized capital gains and losses	148,936,212
Change in net deferred income tax	8,313,183
Change in nonadmitted assets	53,215,185
Change in unauthorized reinsurance	(1,438,039)
Change in surplus notes	149,890
Aggregate write-ins for gains or losses in surplus	75,773,831
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Capital and surplus - December 31, 2009	2,091,886,365
Net income	395,009,258
Change in valuation basis of aggregate policy and claim reserves	168,367,269
Change in net unrealized capital gains and losses	(40,289,238)
Change in net deferred income tax	(62,478,462)
Change in nonadmitted assets	121,526,405
Change in unauthorized reinsurance	(2,804,347)
Change in surplus notes	162,823
Aggregate write-ins for gains or losses in surplus	(26,686,602)
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Capital and surplus - December 31, 2010	2,644,693,471

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Blue Cross and Blue Shield of Florida, Inc.
Statement of Changes in Capital and Surplus (continued)
Five Years Ended December 31, 2011

Net income	204,154,935
Change in valuation basis of aggregate policy and claim reserves	83,285,980
Change in net unrealized capital gains and losses	(67,810,505)
Change in net deferred income tax	3,091,797
Change in nonadmitted assets	(22,189,426)
Change in unauthorized reinsurance	1,028,152
Change in surplus notes	(149,827,871)
Aggregate write-ins for gains or losses in surplus	(87,385,854)
	<hr/> 2,609,040,679
Examination adjustments	-
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Capital and surplus - December 31, 2011	<u>\$ 2,609,040,679</u>

Blue Cross and Blue Shield of Florida, Inc.
Comparative Analysis of Changes in Capital and Surplus
December 31, 2011

The following is a reconciliation of capital and surplus between that reported by the Company and as determined by the examination.

Capital and surplus, December 31, 2011 - per annual statement			\$ 2,609,040,679
	Per Company	Per Examination	Increase (Decrease) In Capital & Surplus
Total assets	\$ 5,548,451,284	\$ 5,548,451,284	\$ -
Total liabilities	\$ 2,939,410,605	\$ 2,939,410,605	\$ -
Net change in capital and surplus			-
Capital and surplus, December 31, 2011 - per examination			\$ 2,609,040,679

COMMENTS ON FINANCIAL STATEMENTS

Aggregate Health Policy Reserves

During 2011, the Company filed with and received approval from the Office's Life & Health Product Review unit, as part of a rate filing, certain morbidity and persistency assumption changes that were also used to calculate its aggregate health policy reserves based on the Company's experience. We found that the change in assumptions, which resulted in an increase in the Company's capital and surplus of \$83 million, was made prior to obtaining approval from the Office as required by Section 625.121(10), F.S. However, the change in assumptions was reviewed during the examination and approved by the Office's Life & Health Financial Oversight unit on November 15, 2012.

SUBSEQUENT EVENTS

In 2012, the Company began using the trade name Florida Blue. No changes were made to the Company's corporate name.

Florida True Health, Inc. was licensed by the Office as an HMO on July 9, 2012. It was formed in December of 2011 by DHSI and AmeriHealth Mercy Health Plan, an unrelated partnership, to offer managed care services to Florida Medicaid members.

In December of 2012, DHSI acquired Diagnostic Clinic Medical Group, Inc., a multi-specialty physician practice based in Largo, Florida.

CONCLUSION

The customary insurance examination practices and procedures as promulgated by the NAIC have been followed in ascertaining the financial condition of Blue Cross and Blue Shield of Florida, Inc. consistent with the insurance laws of the State of Florida.

At December 31, 2011, the Company's capital and surplus was \$2,609,040,679 and the Company was in compliance with the minimum capital and surplus requirement of Section 624.408, F.S.

In addition to the undersigned, the following individuals participated in the examination: Walter F. Banas, CIE, Financial Specialist; Faisal Harianawalla, Financial Examiner/Analyst; Cathy S. Jones, CPA, CFE, Financial Examiner/Analyst Supervisor; Kerry A. Krantz, Actuary; and Michael D. Young, CFE, Financial Examiner/Analyst. The NAIC Capital Markets Bureau assisted with our analysis of the Company's investment portfolio. Highland Clark, LLC assisted with our review and evaluation of the design and effectiveness of the Company's information technology systems controls.

Respectfully submitted,

Christine N. Afolabi, CPA
Financial Specialist
Florida Office of Insurance Regulation