



STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**CENTRAL OREGON INDEPENDENT HEALTH SERVICES, INC.
DBA CLEAR CHOICE HEALTH PLANS
BEND, OREGON**

NAIC COMPANY CODE 47087

AS OF

DECEMBER 31, 2005

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February 1, 2007

Cory Streisinger, Director
Department of Consumer and Business Services
State of Oregon
350 Winter Street NE, Room 440
Salem, Oregon 97301-3883

Dear Director:

In accordance with your instructions and pursuant to the provisions of Oregon Revised Statute (ORS) 731.300, we have examined the business affairs and financial condition of

**CENTRAL OREGON INDEPENDENT HEALTH SERVICES, INC.
DBA CLEAR CHOICE HEALTH PLANS
2650 NE Courtney Drive
Bend, Oregon 97701**

NAIC Company Code 47087

hereinafter referred to as the "Plan." The following report of examination is respectfully submitted.

SCOPE OF EXAMINATION

The examination of the Plan was conducted as of December 31, 2005, covering the two year period then ended, and included a review of material transactions or events which occurred subsequent to the examination date and were noted during the examination.

The examination was conducted pursuant to the provisions of ORS 731.300 and in accordance with procedures and guidelines prescribed by the National Association of Insurance Commissioners (NAIC) for the purpose of determining the Plan's financial condition, ability to fulfill its obligations, nature of its operations, and compliance with the Insurance Code. Accounting methods, internal control procedures, records, and other supporting evidence were examined or tested by appropriate methods to the extent deemed necessary and appropriate for the type, volume, and complexity of the accounting system and operations utilized by the Plan. Record testing included, but was not limited to, assets, liabilities, income and expense related items.

In addition to the above, work papers were reviewed that were prepared by Symonds, Evans & Company PC, the Plan's independent auditors, in its audit of the Plan's accounts for the year ended December 31, 2005. A portion of the auditors' work papers has been incorporated into our work papers and has been utilized in determining the scope and areas of emphasis in conducting the examination.

David N. Ball, FSA, MAAA, actuary for the State of Oregon, Department of Consumer and Business Services, Insurance Division, evaluated the Plan's unpaid claims reserves, accrued medical incentive pool and bonus amounts, and unpaid claims adjustment expenses. The results of his analysis are found under the relevant section of this report.

COMPANY HISTORY

The Plan was incorporated under the laws of the State of Oregon on June 5, 1995, and commenced business on April 24, 1998, as a for-profit health care service contractor under ORS Chapter 750.

The Plan was formed by Central Oregon Independent Practice Association and Central Oregon Hospital Network to administer a fully capitated contract for the Oregon Health Plan through the Oregon Medical Assistance Programs (OMAP). In 1998 the Plan was qualified by the Health Care Financing Administration (now known as the Centers for Medicare and Medicaid Studies, or CMS) as the first Provider Sponsored Organization in the nation to write Medicare+Choice business. Beginning in 2001, the Plan began offering commercial health plans in the large-group employers market, expanding into small-group employers during 2004.

Effective January 1, 2004, all OMAP business was transferred to a newly formed subsidiary, Clear Choice Individual Health Solutions.

MANAGEMENT AND CONTROL

Board of Directors

Amended and Restated Bylaws vest management and control of the Plan in a Board of Directors. Section 3.2 of the Bylaws vests the Plan's management and control in a Board consisting of not less than nine (9) members, of which one-third (1/3) of the Board shall be representatives of the public who are not practicing doctors or an employee or trustee of a participant hospital. Following is the Board of Directors serving as of December 31, 2005:

<u>Name</u>	<u>Business Address</u>	<u>Representative</u>
Michael M. Kendrick, MD Chairman Director since 1996	Neurosurgeon Center for Neurosurgery 2275 NE Doctors Drive Bend, OR 97701	Medical
F. Peter Boehm, MD Vice Chairman Director since 1996	Pediatrician Central Oregon Pediatric Associates 2200 NE Professional Court Bend, OR 97701	Medical
Jeffrey Drutman, MD Corporate Secretary/ Treasurer Director since 1996	Radiologist Central Oregon Radiology Associates, PC 1460 NE Medical Center Drive Bend, OR 97701	Medical
Robert V. Pinnick, MD Director since 2001	Nephrologist Bend Memorial Clinic 1501 NE Medical Center Drive Bend, OR 97701	Medical
Michel A. Boileau, MD Director since 2003	Urologist Bend Urology Associates, LLC 2090 Wyatt Court, Suite 101 Bend, OR 97701	Medical
Stuart G. Garrett, MD Director since 2001	Family Medicine Bend Memorial Clinic 1501 NE Medical Center Drive Bend, OR 97701	Medical
Eric W. Alexander Director since 1998	CONet Executive Vice President St. Charles Medical Center 2500 NE Neff Road Bend, OR 97701	CONet Medical
James A. Diegel Director since 2005	President/CEO St Charles Medical Center – Redmond 1253 N Canal Blvd Redmond, OR 97756	CONet Medical
Duane W. Francis Director since 2001	President Mid Columbia Medical Center 1700 East 19 th Street The Dalles, OR 97058	CONet Medical
Craig W. Moore Director since 1997	President Pepsi Cola Bottling of Bend 2440 NE 4 th Street Bend, OR 97701	Public

<u>Name</u>	<u>Business Address</u>	<u>Representative</u>
Patricia L. Moss Director since 1997	President & CEO Bank of the Cascades 1100 NW Wall Street Bend, OR 97701	Public
Jerol E. Andres Director since 1997	CEO & President Eagle Crest, Inc. PO Box 1215 Redmond, OR 97756	Public
Gary D. Fish Director since 2003	President Deschutes Brewery 901 SW Simpson Bend, OR 97701	Public
Neil R. Bryant, JD Director since 1997	Senior Partner Bryant, Lovlien & Jarvis 40 Greenwood Avenue Bend, OR 97701	Public

Two additional individuals were listed as directors on the 2005 annual statement jurat page who were not actually directors of the Plan. David L. Harman resigned from the Board at the March 18, 2005 board meeting, but was still being listed as a member of the board at year-end. Michael A. Patmas, MD, was not elected nor appointed at any board meeting during 2005.

At least one-third of the members of the Board of Directors are representatives of the public pursuant to the provisions of ORS 750.015(1).

Officers

Operating management of the Plan as of December 31, 2005, was under the direction of the following principal officers:

Patricia J. Gibford	President and Chief Executive Officer
Jeffrey Drutman, MD	Corporate Secretary and Treasurer
P. Gunnar Hansen, CPA	Chief Financial Officer
Michael A. Patmas, MD	Vice President/Medical Affairs and Medical Director

Parent, Subsidiary and Affiliated Companies

The Plan is a member of an insurance company holding system, which includes a wholly owned subsidiary. The following is a list of entities either holding direct or indirect ownership of the Plan, or having agreements in place with the Plan during the period under review:

Central Oregon Independent Practice Association (COIPA) – contracts with the Plan to provide health care services to the Plan’s enrollees. Members of COIPA include primary and specialty care providers in the same service area that the Plan operates, and many own shares of stock of the Plan.

Central Oregon Hospital Network (CONet) – is a nonprofit entity that owns 19.54% of the outstanding shares of the Plan. CONet is comprised of eight hospitals covering the same service area as the Plan. CONet provides health care services to Plan members under the terms of a provider contract.

Central Oregon Individual Health Solutions (COIHS) – is a wholly owned subsidiary of the Plan formed to service Medicaid business. Effective January 1, 2004, the Plan transferred all of its OMAP business to COIHS.

Clear Choice Health Plans, Inc. (Clear Choice) – is a wholly owned subsidiary formed during 2005 to apply for a certificate of authority as a life and health insurer under ORS Chapter 732. See the Subsequent Events section later in this Report for more information.

INTERCOMPANY AGREEMENTS

Effective January 1, 2003, the Plan signed an administrative services agreement with COIPA, whereby the Plan furnishes administrative services and rents office space to COIPA. For

these services, COIPA pays the Plan a set monthly fee for the administration plus monthly rent for space used.

Effective January 1, 2004, the Plan entered into an administrative services agreement with COIHS, whereby the Plan furnishes administrative services, technical and support services, office space and equipment, and staff. For these services, COIHS reimburses the Plan a percentage of total administrative expenses incurred by the Plan. There is a provision in the agreement for the Plan to pay COIHS an allocated portion of its investment income, which shall be considered an interest payment on a promissory note owned by COIHS dated December 31, 2003. However, since the formation of the subsidiary, no settlement of the intercompany account has occurred. At December 31, 2005, the balance of the intercompany payable had grown to \$23,763,660. SSAP No. 25, paragraphs 15 and 16, notes that terms of an agreement between related parties must be arms-length, fair and reasonable.

I recommend the Plan settle the intercompany payable to its subsidiary, COIHS, and reconcile the general ledger account on a regular basis.

For the tax years 2004 and 2005, the Plan filed a consolidated tax return for itself and for its subsidiary. The Plan filed a Form 1120-PC return to the IRS and a Form 20 corporation excise tax return to the State of Oregon, Department of Revenue. However, there is no formal tax allocation agreement in place between the Plan and COIHS.

I recommend the Plan enter into a tax allocation agreement with its subsidiary, COIHS, and submit this agreement to the Oregon Insurance Division on a Form D for approval, pursuant to ORS 732.574.

CAPITALIZATION

The Plan's initial capitalization was completed in June of 1995 by offering COIPA members shares of Class A common stock. This initial subscription generated sales of 141 shares of Class A stock and \$670,000. As of the date of the last examination, December 31, 2003, the Plan reported 6,059 shares of Class A stock, 4,655 shares of Class C stock, and 783 shares of Class D stock outstanding, with a total capital value of \$3,249,392.

During 2004, the Plan restructured its existing capital stock classes and authorized two additional classes of stock: 5,000,000 shares of Class 1 Common Stock and 1,000,000 shares of preferred stock. During 2005, the Plan's shareholders approved an exchange of each share of existing Class A, Class C and Class D common stock for 150 shares of Class 1 Common stock.

In 2005, the Plan's largest shareholder, CONet, redeemed half of its holding of Class 1 common stock, reducing its stake to 19.54% of the outstanding shares of the Plan. To pay for the redemption, the Plan sold 250,000 shares, priced at \$30 per share, to individual investors through DA Davidson, a regional stock brokerage firm. This generated \$7,500,000, less issuance costs, which was used in part to repurchase 349,125 shares held by CONet.

At December 31, 2005, there were approximately 446 separate owners of 1,786,660 Class 1 common shares. With the exception of CONet, no individual shareholder owns or controls more than 5% of the outstanding Class 1 common shares of the Plan.

The Board has adopted an Equity Incentive Plan to issue Incentive Stock Options (ISOs) and Non-qualified Stock Options (NSOs) of the Plan's Class 1 common stock. ISOs are granted to key employees and officers at not less than fair market value as determined by the Board, and NSOs are granted to members of the Board at any amount as determined by the Board.

These options have vesting periods ranging between zero and three years, with expiration dates between five and ten years from date of grant. At December 31, 2005, a total of 348,150 shares were available under the Equity Incentive Plan for future grant. This information is not being reported in the Notes to Financial Statement of the filed Annual Statement blanks, as required by the NAIC Annual Statement Instructions for Health manual.

I recommend the Plan disclose the total amount of stock held for special purposes, such as stock options or stock purchase warrants, in the Notes to Financial Statement, Note No. 13, pursuant to SSAP No. 13, paragraph 15.

CONFLICT OF INTEREST

A resolution of the Board of Directors created a Standard of Conduct and Disclosure Statement, which requires any officer, director, or responsible employee to disclose to the Board of Directors any material interest or affiliation which conflicts with the duties of such person on behalf of the Plan. Completed conflict of interest statements for Board members and officers were reviewed for 2004 and 2005. No conflicts were noted.

CORPORATE RECORDS

The corporate records, including the Articles of Incorporation, Bylaws and minutes of the Board of Directors meetings and committee meetings, were reviewed for the period under examination.

Board Minutes

All of the Board meetings, including all committees, during the examination period were conducted with a quorum of directors present. The Board minutes were recorded in sufficient detail to have an understanding of the actions taken by the Board. The minutes of

the Audit Committee reflected the approval of investments as required by the provisions of ORS 733.730.

Articles of Incorporation

The Articles of Incorporation conformed with Oregon Statutes. Revised Articles of Incorporation were adopted on December 16, 2004. These revisions allowed for the reorganization of stock classes as described in the Capitalization section above.

Bylaws

The Bylaws conformed with Oregon Statutes. Bylaws were revised on December 19, 2004. During 2005, these Bylaws were further amended to: 1) combine the authority of the Executive, Governance and Nominating Committees, 2) change the name of the Finance/Audit/Compliance Committee to the Audit Committee, 3) allow the President and CEO of the Plan to be a voting member of the Board of Directors, 4) reduce the number of directors to not less than nine, and removed the representation requirements of the hospital and medical members, and 5) remove the three-year term of office requirement for board members.

FIDELITY BONDS AND OTHER INSURANCE COVERAGES

The examination of insurance coverages included a review of adequacy of limits and retentions. Two dishonesty policies insured the Plan against employee dishonesty. A blanket employee dishonesty policy insures the Plan against losses up to \$25,000 per employee after a deductible of \$1,000. A specific employee dishonesty policy covers losses up to \$750,000 with a \$2,500 deductible for the following corporate officers: CFO, CEO, controller, accounting worker and treasury director. This amount exceeds the minimum coverage recommended by the NAIC. No exceptions were noted in the examination of the Plan's coverages.

The examination of insurance coverages protecting the Plan at December 31, 2005, involved a review of the adequacy of policy limits and retentions, as well as the solvency of the insurers. Other insurance coverages in force were found to be adequate, and are as follows:

Workers' compensation
Commercial general policy

Premises liability
General liability

PENSION PLANS AND OTHER POST RETIREMENT BENEFITS

The Plan sponsors a 401k plan, which covers all full-time employees who have at least 90 days of service. Eligible employees may contribute up to 15% of their salaries to this plan, which the Plan matches up to 3% of the employee's gross salary.

In addition to the 401k plan, the Plan has a salary continuation plan for certain highly compensated employees, whereby a key employee is entitled to a percentage of their compensation for ten years after retirement, subject to certain vesting requirements. The salary continuation plan included a provision for death benefits related to the participants.

The Plan managed a deferred compensation plan for certain Board members to defer board fees into an interest bearing account.

TERRITORY AND PLAN OF OPERATION

The Plan provides health care services for Medicare, group commercial members, and administrative services contracts for self-insured and partially-insured groups. Coverage is written primarily in Central Oregon, Eastern Oregon and the Columbia Gorge regions. Medicare Advantage business is operated under a contract with the Center for Medicare and Medicaid Services (CMS) as a state-licensed provider sponsored organization. COIPA and CONet represent the majority of the contracted provider network for professional and

hospital services in the Plan's service region. During the period under examination, the Plan reported total enrolled members as follows:

<u>Line of Business</u>	<u>2005</u>	<u>2004</u>
Group hospital & medical	3,946	2,506
Medicare	<u>9,919</u>	<u>9,261</u>
Total enrollment	<u>13,865</u>	<u>11,767</u>

GROWTH OF THE COMPANY

Growth of the Plan is illustrated by the following schedule. Amounts shown are derived from filed annual statements, except for those years where a report of examination has been published by the Oregon Insurance Division.

<u>Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Capital and Surplus</u>	<u>Net Income</u>
2001	\$34,304,419	\$23,833,100	\$10,471,319	\$2,643,354
2002	38,101,237	26,204,186	11,897,051	2,460,476
2003*	47,270,028	29,614,474	17,655,554	6,097,601
2004	65,941,275	37,241,574	28,699,701	4,613,061
2005*	82,529,286	44,329,617	38,199,668	5,740,855

*Per examination

LOSS EXPERIENCE

Annual underwriting results for the Plan are shown below. Amounts shown were compiled from the Plan's filed annual statements and, where indicated, from the current and previous examination reports published by the Oregon Insurance Division.

<u>Year</u>	(1) <u>Total Hospital and Medical Expenses</u>	(2) <u>Premiums and Related Revenues</u>	(1/2) <u>Claims Ratio</u>
2001	\$79,540,182	\$ 89,780,873	88.6%
2002	95,974,000	108,025,421	88.8%
2003*	90,014,658	107,130,220	84.0%
2004	61,976,145	74,874,918	82.8%
2005*	75,289,946	89,379,355	84.2%

*Per examination

Premiums and claims both declined beginning in 2004 due to the Plan moving all its Medicaid business to a newly formed subsidiary, COIHS, as noted previously in this report.

STATUTORY DEPOSIT

As of December 31, 2005, the Plan maintained a \$506,000 security deposit with the State of Oregon, Department of Consumer and Business Services, Insurance Division, pursuant to the provisions of ORS 750.045. The deposit was verified from the records of the Insurance Division.

REINSURANCE

For 2005, the Plan's reinsurance program was comprised of an HMO Excess Risk Reinsurance Agreement with Reliastar Life Insurance Company (NAIC #67105) covering both Medicare Advantage and commercial business. Under terms of the agreement, the reinsurer reimburses the Plan for losses per member up to \$1,000,000 for each Medicare risk, and \$2,000,000 for each commercial risk, with a lifetime benefit per member of \$2,000,000. Retention was \$75,000 per Medicare Advantage member and \$125,000 per commercial risk, subject to an average per day maximum of \$5,000 for eligible inpatient and outpatient services. It was determined the Plan's reinsurance agreements clearly specified the risk taken by the reinsurer, with no unusual provisions reducing the reinsurer's risk.

Insolvency Clause

The reinsurance agreement contained an insolvency clause in accordance with ORS 731.508(3) as required to take reserve credits for reinsurance ceded.

Risk Retention

The Plan did not retain risk on any one subject in excess of 10% of its surplus to policyholders as required by the provisions of ORS 731.504.

ACCOUNTS AND RECORDS

In general, the Plan's records and source documentation supported the amounts presented in the Plan's December 31, 2005, annual statement and were maintained in a manner by which the financial condition was readily verifiable as required by the provisions of ORS 733.170.

However, the following comments or recommendations have been made as a result of this examination:

Reconciliations

A number of general ledger accounts did not appear to have been properly reconciled on a timely basis during the period under examination. As an example, the Accounts Receivable Aged Invoice Report reported incorrect data, including policies that should not have any balances and aged items. In a review of subsequent events the examiner was able to determine some entries had been cleared during 2006. These entries included policies terminated and never removed, miscellaneous invoices recorded in error and cancelled policies with remaining balances. The Company has put an emphasis on reconciling this report on a more frequent basis.

I recommend the Plan perform regular reconciliations of its accounts to determine if adjusting entries are required, and to identify logical errors in the general ledger accounts.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The Plan complied with all the recommendations made in the 2003 examination report.

CENTRAL OREGON INDEPENDENT HEALTH SERVICES, INC.
DBA CLEAR CHOICE HEALTH PLANS
BALANCE SHEET
AS OF DECEMBER 31, 2005

<u>ASSETS</u>	<u>Annual Statement</u>	<u>Examination Adjustments</u>	<u>Examination Balance</u>
Bonds (Note 1)	\$22,189,628	\$(8,180,055)	\$14,009,573
Common stocks (Note 1)	39,560,291		39,560,291
Real estate	836,225		836,225
Cash and short-term investments (Note 1)	17,069,770	8,180,055	25,249,825
Investment income due and accrued	326,927		326,927
Uncollected premiums (Note 2)	699,427	(16,520)	682,907
Amounts recoverable from reinsurers	678,335		678,335
Federal income tax recoverable	582,940		582,940
Net deferred tax asset	215,102		215,102
Electronic data processing equipment	390,473		390,473
Rec. from parent, subsidiary and affiliates	2,024		2,024
Health care and other amounts receivable (Note 4)	<u>1,052,663</u>	<u>(1,058,000)</u>	<u>(5,337)</u>
Total Assets	<u>\$83,603,805</u>	<u>\$(1,074,520)</u>	<u>\$82,529,285</u>
 <u>LIABILITIES</u>			
Claims unpaid (Note 3)	\$ 9,534,433	\$ 0	\$ 9,534,433
Accrued medical incentive pool & bonus (Note 3)	7,308,511		7,308,511
Unpaid claims adjustment expenses (Note 3)	673,000		673,000
Premiums received in advance (Note 4)	1,579,607	(1,058,000)	521,607
General expenses due or accrued (Note 5)	2,455,073	(592,689)	1,862,384
Amounts withheld or retained for others (Note 5)		664,901	664,901
Amounts due to parent, subsidiaries and affiliates	23,763,660		23,763,660
Aggregate write-ins for other liabilities (Note 5)	<u>0</u>	<u>1,121</u>	<u>1,121</u>
Total Liabilities	<u>45,314,284</u>	<u>(984,667)</u>	<u>44,329,617</u>
 <u>CAPITAL AND SURPLUS</u>			
Common capital stock	10,350,232		10,350,232
Unassigned funds (surplus)	<u>27,939,289</u>	<u>(89,853)</u>	<u>27,849,436</u>
Total Capital & Surplus	<u>38,289,521</u>	<u>(89,853)</u>	<u>38,199,668</u>
Total Liabilities, Capital & Surplus	<u>\$83,603,805</u>	<u>\$(1,074,520)</u>	<u>\$82,529,285</u>

**CENTRAL OREGON INDEPENDENT HEALTH SERVICES INC.
DBA CLEAR CHOICE HEALTH PLANS
INCOME STATEMENT
FOR THE YEAR ENDING DECEMBER 31, 2005**

Net premium income	<u>\$89,379,355</u>
Hospital and medical deductions:	
Hospital/medical benefits	62,172,066
Other professional services	111,170
Outside referrals	2,648,409
Emergency room and out-of-area	2,034,893
Prescription drugs	1,636,411
Aggregate write-ins for other hospital and medical	83,904
Incentive pool, withhold adjustments and bonus amounts	<u>7,313,391</u>
Subtotal	76,000,244
Less:	
Net reinsurance recoveries	<u>710,298</u>
Total Hospital and Medical Deductions	75,289,946
Claims adjustment expenses	3,606,958
General administrative expenses	<u>3,435,511</u>
Total Underwriting Deductions	<u>82,332,415</u>
Net underwriting gain or (loss)	<u>7,046,940</u>
Net investment income earned	1,565,382
Net realized capital gains or (losses)	<u>0</u>
Net investment gains or (losses)	<u>1,565,382</u>
Net income or (loss) before federal income taxes	8,612,322
Federal income tax incurred	<u>2,871,467</u>
Net Income	<u>\$ 5,740,855</u>

CAPITAL & SURPLUS

Capital and surplus December 31, 2004	<u>\$28,699,701</u>
Gains and Losses to Capital and Surplus	
Net income	5,740,855
Net unrealized capital gains	8,351,583
Change in net deferred income tax	2,181
Change in nonadmitted assets	(2,690,443)
Capital Changes	
Paid in	(9,007,425)
Transferred to surplus	6,925,107
Prior year audit adjustment	267,963
Examination adjustment	<u>(89,853)</u>
Net change in capital and surplus	<u>9,499,967</u>
Capital and surplus December 31, 2005	<u>\$38,199,668</u>

NOTES TO FINANCIAL STATEMENTS

Note 1 – Investments

The Plan's bond investments were in high quality US Treasury obligations and industrial and miscellaneous bonds. Common stocks consisted of industrial and miscellaneous issues, an investment in a subsidiary, and various mutual funds. A comparison of the major invested assets over the past five years is as follows:

<u>Year</u>	<u>A</u> <u>Bonds</u>	<u>B</u> <u>Common</u> <u>Stocks</u>	<u>C</u> <u>Cash and</u> <u>Short-term</u>	<u>Ratio</u> <u>A/</u> <u>Total Assets</u>	<u>Ratio</u> <u>B/</u> <u>Total Assets</u>	<u>Ratio</u> <u>C/</u> <u>Total Assets</u>
2001	15,466,622	4,722,994	11,711,799	45%	14%	34%
2002	16,195,197	3,639,623	15,284,730	42%	9%	40%
2003*	18,304,669	4,275,800	20,160,971	39%	9%	43%
2004	19,806,980	7,238,232	30,982,667	32%	12%	50%
2005*	14,009,573	39,560,292	25,249,825	17%	48%	30%

*Per examination

As of December 31, 2005, invested assets with a book value of \$15,166,917, representing 19% of the total invested assets, were invested in amply secured obligations of the United States or FDIC insured cash deposits, which exceeded the required capitalization amount required by ORS 733.580.

The Plan did not report any bonds rated below investment grade as of December 31, 2005.

The examiners noted that ten of the bonds listed in Schedule D – Part 1 were purchased within one year of their maturity, and should have been recorded as short-term investments, pursuant to SSAP No. 26, paragraph 2. A reclassification of \$8,180,055 was made from long-term bonds to short-term investments in this Report. **I recommend the Plan report all investments purchased within one year or less to maturity or call date as a Short-term Investment on Schedule DA.**

Note 2 – Uncollected Premiums

The account for uncollected premiums was reduced by \$16,210, representing incorrectly posted amounts due from employees of the Plan, and a further \$310, which was identified as premium receivables more than 90 days past due.

Note 3 - Claims Unpaid, Accrued Medical Incentive Pool and Bonus and Unpaid Claims Adjustment Expenses

David N. Ball, FSA, MAAA, actuary for the State of Oregon, Department of Consumer and Business Services, Insurance Division, performed independent calculations of the IBNR claims liability which stem from claims on the commercial business and on Medicare. He also reviewed the Plan's calculations of the accrued medical incentive pool and recalculated the unpaid claims adjustment expenses. His estimates for the Plan's 2005 liabilities are as follows:

	<u>Examination Balance</u>	<u>Company Balance</u>
Claims unpaid	\$ 9,534,433	\$ 9,534,433
Accrued medical incentive pool & bonus	7,308,511	7,308,511
Unpaid claims adjustment expenses	<u>673,000</u>	<u>673,000</u>
Total	<u>\$ 17,515,944</u>	<u>\$ 17,515,944</u>

Note 4 – Premiums Received in Advance and Health Care Receivables

At year-end 2005, the Plan booked a receivable from CMS for Medicare premiums in the amount of \$1,058,000, which it offset with a liability for deferred premiums. It was subsequently discovered that the entry should not have been made, and the entries were reversed. However, the amounts were shown on the 2005 annual statement. **I recommend the Plan reconcile the general ledger accounts for premiums received in advance and for health care receivables on a more timely basis.**

Note 5 – General Expenses Due or Accrued, Amounts Withheld for Account of Others, and Aggregate Write-ins for Other Liabilities

During the examination of general expenses, it was determined that the following items should be reclassified from general expenses to amounts withheld or retained for account of others. This exception was also noted in the prior report of examination.

The accounts were reclassified are as follows:

Misc/Other payroll deductions	\$ 91
WCC payable	1,670
SAIF accrued liability	12,611
401-K loan payable	263
SUTA payable	11,170
401-K payable	13,738
Medical employee W/H	1,637
Cobra/Insr payable	(32)
FUTA payable	374
EE fun fund	627
Deferred board compensation	369,940
Deferred exec comp	<u>252,812</u>
Total	<u>\$664,901</u>

In addition, the Plan continues to report amounts identified for escheatment in general expenses. The Annual Statement Instructions for Health manual specifically requires these amounts to be reported as an aggregate write-in for other liabilities. The examiners reclassified \$1,121 from general expenses due to aggregate write-ins.

Additionally, a review of the January and February 2006 check registers revealed a number of expenses that were paid in 2006 for expenses that occurred during 2005. An adjustment in the amount of \$73,333 was made to increase the liability for general expenses due or accrued.

I recommend the Plan follow the directions in the NAIC Annual Statement Instructions for Health manual and record amounts withheld or retained for others separately from general expenses, pursuant to ORS 733.302. Additionally, items identified as available for escheatment shall be recorded as an aggregate write-in for other liabilities.

CONCLUSION

During the period from the last examination as of December 31, 2003, through December 31, 2005, the Plan's capital and surplus increased from \$17,655,554 as of December 31, 2003, to \$38,199,668, as shown in this report of examination.

The comparative assets and liabilities are shown below:

	<u>2005</u>	December 31, <u>2003</u>	<u>Change</u>
Assets	\$82,529,285	\$47,270,028	\$35,259,258
Liabilities	<u>44,329,617</u>	<u>29,614,474</u>	<u>14,715,143</u>
Capital & surplus	<u>\$38,199,668</u>	<u>\$17,655,554</u>	<u>\$20,544,114</u>

SUMMARY OF COMMENTS AND RECOMMENDATIONS

The following are issues and concerns the examiner believes should be brought to management's attention as a result of this examination.

Page

- 9 I recommend the Plan settle the intercompany payable to its subsidiary, COIHS, and reconcile the general ledger account on a regular basis.
- 9 I recommend the Plan enter into a tax allocation agreement with its subsidiary, COIHS, and submit this agreement to the Oregon Insurance Division on a Form D for approval, pursuant to ORS 732.574.
- 11 I recommend the Plan disclose the total amount of stock held for special purposes, such as stock options or stock purchase warrants, in the Notes to Financial Statement, Note No. 13, pursuant to SSAP No. 13, paragraph 15.
- 16 I recommend the Plan perform regular reconciliations of its accounts to determine if adjusting entries are required, and to identify logical errors in the general ledger accounts.
- 19 I recommend the Plan report all investments purchased within one year or less to maturity or call date as a Short-term Investment on Schedule DA.
- 20 I recommend the Plan reconcile the general ledger accounts for premiums received in advance and for health care receivables on a more timely basis.
- 21 I recommend the Plan follow the directions in the NAIC Annual Statement Instructions for Health manual and record amounts withheld or retained for others separately from general expenses, pursuant to ORS 733.302. Additionally, items identified as available for escheatment shall be recorded as an aggregate write-in for other liabilities.

SUBSEQUENT EVENTS

On December 12, 2005, the Plan formed Clear Choice Health Plans, Inc., (NAIC #12595) as a for-profit life & health insurance company under ORS Chapter 732. On June 23, 2006, the company was issued a Certificate of Authority (#3293) to transact health insurance in Oregon. It was formed to facilitate the conversion of the Plan from a health care service contractor authorized to transact health insurance pursuant to ORS Chapter 750 to an insurer authorized to transact health insurance under ORS Chapter 732. The conversion was

accomplished through the merger of the Plan with and into the company, with the company being the surviving company (“the Merger”). The company submitted a Form A filing and Merger Agreement (“Merger Documents”) with the Oregon Insurance Division.

A public hearing was held on November 8, 2006, at the St. Charles Medical Center in Bend, Oregon, to present the transaction to the public and interested parties, and to take testimony. On November 16, 2006, the director of the Department of Consumer and Business Services issued an order approving the plan of merger.

A majority of the shareholders of the Plan approved the merger at a shareholders' meeting held on January 8, 2007. All shareholders of Clear Choice Health Plan, Inc., approved the merger on March 12, 2007. The merger was effective March 15, 2007. The Plan surrendered its Certificate of Authority as a health care service contractor upon consumation of the merger.

The Plan's December 31, 2006, annual statement was required to be filed with the Oregon Insurance Division and postmarked by March 1, 2007. It was, however, not received until April 3, 2007, and postmarked on April 2, 2007.

ACKNOWLEDGMENT

The cooperation and assistance extended by the officers and employees of the Plan during the examination process are gratefully acknowledged.

In addition to the undersigned, Timothy R. Hurley, CFE, insurance examiner, for the State of Oregon, Department of Consumer and Business Services, Insurance Division, and David N. Ball, FSA, MAAA, actuary for the State of Oregon, Department of Consumer and Business Services, Insurance Division, participated in this examination.

Respectfully submitted,

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Insurance Division
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