



STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**EMPLOYEES' BENEFIT ASSOCIATION
PORTLAND, OREGON**

AS OF

DECEMBER 31, 2003

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January 7, 2005

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

Dear Director:

In accordance with your instructions and pursuant to ORS 731.300, we have examined the business affairs and financial condition of

EMPLOYEES' BENEFIT ASSOCIATION
2235 NW Savier Street
Portland, Oregon 97210

hereinafter referred to as "EBA" or the "Association." The following report of examination is respectfully submitted.

SCOPE OF EXAMINATION

This regular examination of the Association was conducted as of December 31, 2003, covering the five-year period then ended, and included a review of material transactions or events which occurred subsequent to the examination cut-off date and which 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 Association's financial condition and ability to fulfill its obligations, the 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 Association. The record testing included, but was not limited to, assets, liabilities, income and expense related items. A review was also made of the corrective actions taken by the Association with respect to comments and/or recommendations in the previous financial report of examination as of December 31, 1998.

In addition to the above, the examiner reviewed work papers prepared by Moss-Adams, the Association's independent auditors, during their audit of the Association's accounts for the year ended June 30, 2004. 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.

A management affirmation attesting to the Association's compliance with Oregon laws relating to location of accounts and records, conduct of the Association's affairs in a nonhazardous manner, and exercise of managerial control by a duly qualified and constituted Board of Directors was signed by and received from the Accounting/Property Manager, acting on authority assigned to her by the Board of Trustees.

HISTORY OF THE ASSOCIATION

The Association is an exempt insurer pursuant to the provisions of ORS 731.032 and 731.042, operating under a Certificate of Exemption issued by the Oregon Insurance Division on April 1, 1967. The Association was incorporated as a nonprofit corporation under the laws of the State of Oregon on December 24, 1942. The Association's purpose is to provide short-term disability, life insurance, and accidental death and dismemberment benefits to its members.

Membership is limited to employees of Freightliner (FC), CNF Transportation, Inc. (CNF), and their subsidiaries (including Menlo Worldwide and Conway), and Canadian Freightways, as well as other participating employers in the trucking industry. Membership also includes the Association's employees. The membership is voluntary and bears no relationship between the Association and the companies involved, other than to define those qualified to be members.

MANAGEMENT AND CONTROL

The Articles of Incorporation and Bylaws provide that the members elect four trustees as members of the Board of Trustees, with a fifth trustee appointed by a majority vote of the elected trustees. Trustees must be members of the Association for not less than five years prior to being nominated as trustees. Terms of service are for three years each. The four

trustees are divided into three classes of one or two trustees each, and at each annual meeting of the members, one class of trustees is elected for a three-year term so that the term of office of one class of trustees expires each year. The trustees are empowered to conduct the Association's affairs.

Members of the Board of Trustees as of December 31, 2003 are as follows:

<u>Name and Address</u>	<u>Occupation and Affiliation</u>
Jimmy Wohl 1510 SW 3 rd Drive Gresham, OR 97080	Freightliner Corporation Inspections
Dave Densmore 16409 NE 82nd Street Vancouver, WA 98682	Freightliner Corporation Mechanic Inspector
Robert Hahn 9803 SE 42 nd Avenue Milwaukie, OR 97222	Freightliner Corporation Production Mechanic
Linda Werbin 14003 NE 13 th Street Vancouver, WA 98684	CNF Transportation Service Customer Service
Becky Carstensen 6221 SW Wilbard Street Portland, OR 97219	CNF Transportation Service Print Shop

The trustees are elected at the December annual members meeting. The date of the meeting is determined by the Board of Trustees. The officers of the Association are appointed by the Board of Trustees at the first meeting of the Board following the annual members meeting.

Officers serving as of December 31, 2003 were:

<u>Name</u>	<u>Title</u>
Jimmy Wohl	President
Dave Densmore	Vice President
Linda Werbin	Secretary

In accordance with Section VI of the Bylaws, the president is authorized to be the principal executive officer of the Association and to supervise and control the day-to-day operations of the Association. The day-to-day operations of the Association are currently co-managed by Judy Sigler and Betty Brant based on authority assigned to them by the Board of Directors and subject to control by the Board of Directors.

CONFLICT OF INTEREST

The Association has a conflict of interest policy that requires officers and directors to report conflicts of interest to the Association. Based on the completed conflict of interest questionnaires, there were no conflicts of interest reported by the officers or directors.

CORPORATE RECORDS

Board of Director Minutes

The Board of Trustees' minutes were reviewed for the period examined. In addition, minutes subsequent to the period examined, up to October 19, 2004, were reviewed. Regular Board meetings are held quarterly. Special Board meetings may be called by the president or by any trustee. It was noted that the Board minutes were recorded in sufficient detail to determine the actions taken by the Board. Although the Association, as an exempt insurer, is not subject to ORS 733.730 and ORS 733.740, the Board of Trustees approved investment transactions. A quorum was achieved at all meetings held during the period under examination. Overall, the minutes supported the transactions of the Association.

Articles of Incorporation and Bylaws

The Association restated its entire Articles of Incorporation and Bylaws effective July 1, 2003, and further amended Section III Subsection 3 of the Bylaws (Disability Waiver of Dues) on November 19, 2003. The restated Articles of Incorporation and Bylaws were the result of the bankruptcy of Consolidated Freightways, Inc., in September 2002, which resulted in a drastic decline of membership, the elimination of the Association as a self-insured and claims paying entity, and the resulting purchase of all insurance coverages from Standard Insurance Company. Article III of the Restated Articles of Incorporation states that “the Association shall not issue any policies or certificates of insurance, but the Association may obtain and maintain from an insurance company, for the benefit of the members and their dependents, policies of life, disability and other insurance.”

Holding Company Registration Statement

The Association is not subject to the holding company registration statutes.

FIDELITY BONDS AND OTHER INSURANCE

The Association is insured up to \$500,000 per occurrence, with a \$1,000 deductible, against losses from acts of dishonesty and fraud by its employees. Fidelity bond coverage was found to exceed the minimum coverage recommended by the NAIC. The Association does not have any directors' and officers' liability coverage.

Other insurance coverages in force at December 31, 2003, included property and general liability insurance. All coverages were found to be adequate, with the exception of the replacement cost coverage on the home office property, which was increased from \$853,000 in 2004 to \$1,095,000 in January 2005.

TERRITORY AND PLAN OF OPERATION

The Association provides disability, loss of time benefits, accidental death and dismemberment, and life insurance benefits to its eligible members. Eligible members who are 62 or older with ten years of membership with the Association or at any age up to age 65 with 20 years of membership meet the requirements for the \$2,000 retiree term life policy . The Association holds a liability for all currently employed members who meet the eligibility requirements. The liability for the policies is held by EBA, and the death benefits are paid by Standard Life.

In prior years the Association's Bylaws required that minimum net assets of \$40 per member be maintained. The Association was also required to maintain a reserve sufficient to cover the contingent liability for group term life insurance in effect for all retired or terminated members covered under the \$2,000 group life insurance policy. The Board of Directors negotiated with Standard Insurance Company to purchase the \$2,000 group paid-up life insurance for all retired or terminated members meeting the Association's age and length of membership requirements. This purchase occurred on December 1, 2003, at a cost of \$4,354,005, which reduced the liability for member life insurance from this amount at June 30, 2003 to \$102,149 at December 31, 2003.

The Association's products are offered to CNF (including Menlo Worldwide and Conway), FC and Canadian Freightway employees by means of wall posters and printed materials mailed to the truck plants and locations throughout the United States and Canada. The Association has no agents and pays no commissions. With the exception of a small number of individuals who remit directly, most of the premium income is derived via payroll deduction from the members' employers. Additionally, the Association plans to have a

website to advertise their products beginning in February 2005. Also, consultants may be hired to present the products to prospective new employers during 2005.

REINSURANCE

The Association does not have any reinsurance contracts in force. As an exempt insurer, in accordance with ORS 731.042(4), the Association is not subject to ORS 731.504 to ORS 731.514, which specify limits of risk and approved reinsurance.

GROWTH OF THE ASSOCIATION

The following exhibit reflects the annual growth of the Association since the prior examination. The amounts were compiled from copies of the Association's filed annual statements and, where indicated, from the current and previous examination reports.

<u>Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Surplus as Regards Policyholders</u>	<u>Net Change in Plan Assets</u>
1998*	\$12,793,076	\$4,800,597	\$7,992,479	\$ 218,354
1999	14,420,881	4,614,480	9,806,401	1,667,075
2000	14,631,801	4,720,952	9,910,849	100,583
2001	14,201,382	4,631,398	9,569,984	(327,527)
2002	11,901,625	4,651,013	7,250,612	(2,466,464)
2003*	9,476,618	154,644	9,321,974	2,104,770

*Per examination

LOSS EXPERIENCE

The following exhibit reflects the annual underwriting results of the Association since 1998. The amounts were compiled from copies of the Association's filed annual statements and, where indicated, from examination reports.

<u>Year</u>	<u>(1) Premium Earned</u>	<u>(2) Benefits Paid</u>	<u>(2)/(1) Ratio</u>
1998*	\$1,566,294	\$1,701,834	109%
1999	1,448,478	1,826,973	126%
2000	1,389,518	1,906,965	137%
2001	1,347,713	1,678,822	125%
2002	840,397	1,248,010	148%
2003*	79,762	266,495	334%

*Per examination

A benefits paid to premium earned ratio of more than 100% typically indicates an underwriting loss. As indicated from the ratio column, an underwriting loss occurred in all six years presented above. The Association has been able to absorb these underwriting losses based on its current level of surplus. The bankruptcy of Consolidated Freightways in September 2002 drastically reduced the Association's membership base and the related premium earned amounts in 2002 and 2003. The Association has not been self insured since July 1, 2003. After that date, the Association began purchasing coverage for all of its policies from Standard Insurance Company. Standard also assumed claims paying responsibility for all claims incurred after that date. While this resulted in a large reduction of benefits paid by the Association during 2003, it also contributed to a significantly higher ratio of benefits paid to premium earned.

PENSION PLAN AND OTHER EMPLOYEE BENEFITS

Pension Plan

The Association offers a Simplified Employee Pension - Individual Retirement Account (plan). At December 31, 2003, the plan provided that employees who had completed at least one year of service were eligible to receive benefits. Under the terms of the plan, the Association contributed 15% of the employee's compensation up to \$200,000. Beginning

January 1, 2004, eligibility was changed to any employee over the age of 21 without any requirement for prior years of service. The contribution amount is now determined by the employer on an annual basis, in accordance with Article III of the plan. The employment agreements for the Association's co-managers states that 15% of the employee's salary and bonus compensation for the prior year, including any year in which the employee's employment is terminated, shall be contributed to a SEP account for the benefit of the employee in January of the following year.

Benefits

The Association provides its co-managers and their families health insurance. It provides its part-time employee health insurance, which does not include family coverage. The Association also provides its co-managers and their families a dental allowance of \$1,500 per calendar year. It provides its part-time employee a dental allowance of \$750 per calendar year, which does not include family coverage. Employees are given an option to purchase a \$25,000 term life insurance policy.

Post-retirement Benefits

The Association does not offer any post-retirement benefits.

Bonuses

The co-managers' employment agreements state that as additional compensation, the Association may pay a bonus. The times and amounts of the bonuses are at the sole discretion of the Board of Trustees. The employment agreement does not require the Board of Trustees to pay a bonus to any employee. As additional compensation, the Association's co-managers and part-time employee were each paid a \$2,000 bonus in 2003.

LIMITATIONS ON THE STATUTORY REGULATION

Under ORS 731.032 and 731.042, the Association is not subject to many Insurance Code requirements that apply to other insurers. By way of example, the Association is not subject to several of the provisions which limit insurer investments, such as the limitations imposed on investments in mortgage loans (ORS 733.600), real property (ORS 733.610), stocks of corporations (ORS 733.620), stocks or obligations of subsidiaries (ORS 733.630), data processing systems (ORS 733.660), noninvestment grade securities (733.695), and many other such items. The Association is exempt from the "prudent investor" (733.670) and prohibited investment statutes (733.780).

Additionally, the Association is not subject to the statutory minimum required capital or surplus requirements (ORS 731.554). In the event of an impairment or insolvency, the Association is not subject to the statutes related to supervision, rehabilitation or liquidation (ORS 734.043, 743.150). Ordinarily, the claims of an insolvent insurer are protected by the Oregon Insurance Guaranty Association (ORS 734.550). These provisions are not applicable to Association pursuant to ORS 731.032 and 731.042.

Certain rating practice statutes do not apply to the Association (ORS 737.230). Many trade practice statutes also do not apply to the Association. These include statutes related to inducements (ORS 746.035); rebates (ORS 746.045); illegal dealing in premiums (ORS 746.120; and practices injurious to free competition (ORS 746.160).

Because of these and many other non-applicable provisions of the Insurance Code, this report of examination is limited in its scope.

ACCOUNTS AND RECORDS

The Association's records are maintained on a fiscal year basis with the reporting period ending June 30 of each year. The Association uses this system in order to coincide with the CNF fiscal year end. Prior to the bankruptcy in 2002, the fiscal year end was maintained in order to coincide with Consolidated Freightways' year-end. Afterward, the Association's independent auditors recommended maintaining the fiscal year-end in order to allow them more time to review the accounts and records supporting the financial statements. The Association has fiscal year end financial statements that are prepared by its independent Certified Public Accountants (CPA). In addition, the CPA reviewed the Association's calendar year statutory financial statements filed pursuant to the provisions of ORS 731.574.

In general, the Association records supported the figures presented in the year end financial statements. However, the following issues were noted:

Investments

As of the date of this examination, all of the Association's securities were held by either Morgan Stanley or CIBC Wood Gundy (Canadian Account). The NAIC Examiners Handbook suggests that insurers have a custodial or safekeeping agreement with a bank, trust company, or securities depository which contains satisfactory safeguards and controls to protect an insurer's assets. The Association does not have such an agreement in place. I suggest the Association consider entering into a custodial agreement with a bank or trust company that is regulated by the Securities and Exchange Commission, the Federal Reserve System, and the banking authorities.

The NAIC Examiners Handbook requires performing procedures to ascertain that the insurer has properly complied with the SVO filing requirements as stated in the Purposes and Procedures Manual of the NAIC Securities Valuation Office, and that all securities not considered 'filing exempt' be filed with the NAIC SVO. The examiner could not verify that the Association complied with these filing requirements. **As a result, I recommend the Association submit its securities to the NAIC Securities Valuation Office or obtain evidence that the securities are listed by a Nationally Recognized Statistical Rating Organization (NRSRO). This recommendation is supported by the provisions of ORS 731.302(1).**

The Association's Statement of Plan Assets lists all of its investments at fair market value as one amount. This makes it very difficult to determine what type of investments are included in this amount. **As a result, I recommend the Association report its investments as separate line items, such as bonds, common stocks, and real estate, to clearly identify the nature of the investment. This recommendation is supported by the provisions of ORS 733.170.**

Bond and stock purchases and sales should be recorded as of their trade date, not the settlement date. The Association is recording purchase and sales of their securities on the settlement date. **As a result, I recommend the Association record all purchases and sales of securities on their trade date, and not the settlement date. This recommendation is supported by the provisions of ORS 731.302(1).**

Real Estate

The Statement of Plan Assets did not list investment real estate separately from other assets. The amount was included as a portion of investments at fair market value. Further, the Association combined the depreciation for investment real estate with bond amortization. The investment property was subsequently sold on May 26, 2004. **However, I recommend future investments in real estate be reported net of depreciation as a separate line item in its Statement of Plan Assets. This recommendation is supported by the provisions of ORS 733.170.**

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The Association has substantially complied with the recommendations made in the previous examination, except for the following:

1. “I recommend that the Association classify investment real estate and the related depreciation as land, building and equipment. This recommendation is supported by the provisions of ORS 733.170.”

The Statement of Plan Assets page combined investment real estate with other investments. Also, the Association combined the depreciation for investment real estate with the balance for amortization of bonds.

The Association sold its investment real estate on May 26, 2004. However, prior to its sale, the investment property was combined with other investments and listed as one amount under Investments at Fair Market Value. Please refer to the Accounts and Records section of this report for a discussion on this issue.

EMPLOYEES' BENEFIT ASSOCIATION
BALANCE SHEET
AS OF DECEMBER 31, 2003

<u>ASSETS</u>	<u>Per</u>	<u>Examination</u>	<u>Per</u>
	<u>Association</u>	<u>Adjustments</u>	<u>Examination</u>
Cash	\$ 5,835	\$	\$ 5,835
Money market funds	402,106		402,106
Members dues receivable	4,890		4,890
Interest and notes receivable	34,851		34,851
Investments at fair market value:			
Bonds (adjusted for amortization)	3,476,625		3,476,625
Stocks (including Canadian stocks)	5,082,581		5,082,581
Real estate (Note 1)	136,385	(136,385)	
Land, building, and equipment (Note 1)	<u>333,345</u>	<u>136,385</u>	<u>469,730</u>
TOTAL ASSETS	<u>\$9,476,618</u>	<u>\$ 0</u>	<u>\$9,476,618</u>
<u>LIABILITIES</u>			
Liability for member life insurance	\$ 102,149	\$	\$ 102,149
Liability for claims not filed	20,000		20,000
Other Liabilities (Note 1)	<u>32,495</u>	<u>0</u>	<u>32,495</u>
TOTAL LIABILITIES	<u>154,644</u>	<u>0</u>	<u>154,644</u>
SURPLUS	<u>9,321,974</u>	<u>0</u>	<u>9,321,974</u>
TOTAL LIABILITIES & SURPLUS	<u>\$9,476,618</u>	<u>\$ 0</u>	<u>\$9,476,618</u>

EMPLOYEES' BENEFIT ASSOCIATION
CHANGE IN PLAN ASSETS EXHIBIT
FOR THE YEAR ENDED DECEMBER 31, 2003

<u>ADDITIONS IN NET PLAN ASSETS</u>	<u>Per Association</u>	<u>Examination Adjustments</u>	<u>Per Examination</u>
Membership dues	\$ 79,762	\$	\$ 79,762
Net realized capital gains	17,934		17,934
Investment income	567,986		567,986
Change in FMV and other income	2,104,039		2,104,039
Miscellaneous income	<u>213</u>		<u>213</u>
 Total Additions	 <u>2,769,934</u>		 <u>2,769,934</u>
 <u>REDUCTION IN NET PLAN ASSETS</u>			
Group term policies (\$25,000)	50,915		50,915
Members' life policies (\$2,000)	224,932		224,932
Insurance premiums AD&D	7,898		7,898
Benefit - sickness and accident	(18,750)		(18,750)
Benefit - funeral	1,500		1,500
Administrative expenses	<u>398,669</u>		<u>398,669</u>
 Total Expenses	 <u>665,164</u>		 <u>665,164</u>
 Net Change in Plan Assets	 <u>\$2,104,770</u>	 \$	 <u>\$2,104,770</u>
 <u>SURPLUS ACCOUNT</u>			
Surplus December 31, 2002	<u>\$7,250,612</u>	\$	<u>\$7,250,612</u>
2003 net change in Plan assets	2,104,770		2,104,770
Change in adjustment to record real estate at cost less depreciation.	(4,785)		(4,785)
Change in nonadmitted assets	15,945		15,945
Change in adjustment to record bonds at amortized cost	<u>(44,568)</u>		<u>(44,568)</u>
 Surplus December 31, 2003	 <u>\$9,321,974</u>	 <u>\$0</u>	 <u>\$9,321,974</u>

NOTES TO FINANCIAL STATEMENTS

Note 1 - Investments and Real Estate

	<u>Investments at Fair Market Value</u>	<u>Land, Building & Equipment</u>
Per Association	\$8,695,593	\$333,345
Per Examination	<u>8,559,208</u>	<u>469,730</u>
Difference	<u>\$ 136,385</u>	<u>\$(136,385)</u>

The December 31, 2003, balance of investments at fair market value included investment real estate. For purposes of this examination investment real estate has been reclassified to land, building and equipment. There is no effect on surplus as a result of this reclassification.

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

- 15 I recommend the Association submit its securities to the NAIC Securities Valuation Office or obtain evidence that the securities are listed by a Nationally Recognized Statistical Rating Organization (NRSRO). This recommendation is supported by the provisions of ORS 731.302(1).
- 15 I recommend the Association report its investments as separate line items, such as bonds, common stocks, and real estate, to clearly identify the nature of the investment. This recommendation is supported by the provisions of ORS 733.170.
- 15 I recommend the Association record all purchases and sales of securities on their trade date, and not the settlement date. This recommendation is supported by the provisions of ORS 731.302(1).
- 16 I recommend future investments in real estate be reported net of depreciation as a separate line item in its Statement of Plan Assets. This recommendation is supported by the provisions of ORS 733.170.

CONCLUSION

No adjustments to the Association's December 31, 2003, surplus were made as a result of this examination. During the five year period covered by this financial examination, the surplus of the Association has increased from \$7,992,479 as presented in the December 31, 1998, financial report of examination, to \$9,321,974 as shown in this report of financial examination. The comparative assets and liabilities are shown below:

	<u>2003</u>	December 31, <u>1998</u>	<u>Change</u>
Assets	\$9,476,618	\$12,793,076	\$(3,316,458)
Liabilities	<u>154,644</u>	<u>4,800,597</u>	<u>(4,645,953)</u>
Surplus	<u>\$9,321,974</u>	<u>\$ 7,992,479</u>	<u>\$ 1,329,495</u>

ACKNOWLEDGMENT

The cooperation and assistance extended by the co-managers and employees of the Association during the examination process are gratefully acknowledged.

Respectfully submitted,

Mark A. Giffin, CFE
Insurance Examiner
Insurance Division
Department of Consumer and Business Services
State of Oregon

AFFIDAVIT

STATE OF OREGON)
) ss
County of Marion)

Mark A. Giffin, CFE, being duly sworn, deposes and says that the preceding report of financial examination as of December 31, 2003, of Employees' Benefit Association of Portland, Oregon, subscribed by him is true and correct to the best of his knowledge and belief.

Mark A. Giffin, CFE
Insurance Examiner
Insurance Division
Department of Consumer and Business Services
State of Oregon

Subscribed and sworn to before me this _____ day of _____, 2005.

Notary Public for the State of Oregon