



STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**REGENCE HMO OREGON  
PORTLAND, OREGON**

**NAIC COMPANY CODE 95699**

AS OF

DECEMBER 31, 2008

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## SALUTATION

January 29, 2010

Alfred W. Gross, Commissioner  
Chairman, NAIC Financial Condition (E) Committee  
State Corporation Commission  
Bureau of Insurance  
Commonwealth of Virginia  
PO Box 1157  
Richmond, Virginia 23218

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

Dear Director:

In accordance with your instructions and guidelines in the National Association of Insurance Commissioners (NAIC) Examiners Handbook, pursuant to ORS 731.300 and 731.302, respectively, we have examined the business affairs and financial condition of

**REGENCE HMO OREGON  
100 SW Market Street  
Portland, Oregon 97201**

**NAIC Company Code 95699**

hereinafter referred to as the “Company” or “RHO.” The following report of examination is respectfully submitted.

## **SCOPE OF EXAMINATION**

The full scope examination of the Company was conducted as of December 31, 2008, covering the three year period then ended, and included a review of material transactions or events which occurred subsequent to the examination cut-off date and were noted during the examination.

The examination was conducted pursuant to ORS 731.300 and in accordance with the NAIC *Financial Condition Examiner Handbook*. The handbook requires that we plan and perform the examination to evaluate the financial condition and identify prospective risks of the company 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. The examination also included assessing the principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation, management's compliance with Statutory Accounting Principles and annual statement instructions in accordance with the Oregon Insurance Code.

In addition to the above, work papers were reviewed that were prepared by Deloitte & Touche LLP, the Company's independent auditors, during its audit of the Company's accounts for the year ended December 31, 2008. Portions of the auditors' work papers have been incorporated into our work papers and have been utilized in determining the scope and areas of emphasis in conducting the examination.

Scott Fitzpatrick, FSA, MAAA, actuary for the State of Oregon, Department of Consumer and Business Services, Insurance Division, participated in this examination by evaluating

losses and loss adjustment expenses unpaid. The results of his analysis are found under the relevant section of this report.

Concurrent with this examination, other affiliated insurers domiciled in Oregon and Utah were examined. These companies included Regence Life and Health Insurance Company (OR), Regence Health Maintenance of Oregon, Inc. (OR), Regence BlueCross BlueShield of Oregon (OR), Regence BlueCross BlueShield of Utah (UT) and HealthWise (UT). This was part of a coordinated examination effort, whereby the states coordinate their efforts to examine all the companies within The Regence Group as of December 31, 2008. A separate report will be issued for each company.

### **COMPANY HISTORY**

The Company was incorporated as a non-profit corporation in Oregon on November 24, 1976, under the name Capitol Health Care, Inc., and received its Certificate of Authority as a domestic health care service contractor from the Oregon Insurance Division on March 1, 1977, under Oregon Revised Statutes Chapter 750. Prior to its incorporation, on September 23, 1976, the Company entered into an agreement with the United States Secretary of Health, Education and Welfare as a health maintenance organization to provide benefits and services under the Federal Medicare program. In March 1978, the Company became a federally qualified health maintenance organization under the provisions of Title XIII of the Public Health Service Act.

From its inception until 1988, the Company operated independently. Effective November 15, 1988, the Company entered into a "Plan and Agreement of Acquisition" with BlueCross BlueShield of Oregon (BCBSO). The agreement named BCBSO as the Company's sole corporate member and gave BCBSO the authority to appoint the chairman of the Board of Directors, approve all directors, budgets, changes in product lines and amendments to

Bylaws and Articles of Incorporation. Under the terms of the agreement, BCBSO transferred to the Company 100% the issued and outstanding shares of stock of its wholly owned subsidiary — Health Maintenance of Oregon, Inc. The agreement also provided the Company with a \$4,000,000 loan from BCBSO in exchange for a \$5,000,000 subordinated promissory note. Also, BCBSO authorized a \$5,000,000 line of credit for the Company. Capitol Health Care was re-named HMO Oregon on October 22, 1993.

On June 1, 1995, BCBSO became part of The Benchmark Group, a non-profit holding company located in Portland, Oregon. On April 1, 1997, The Benchmark Group changed its name to The Regence Group (TRG), and concurrently, the Company's name changed to Regence HMO Oregon.

**Dividends to Stockholders and Other Distributions**

The Company is a non-profit corporation, and may not make distributions to members pursuant to ORS 750.025. However, due to the winding-down of operations beginning in 2005, the Company requested permission from the Director to make an extraordinary distribution to its direct parent. Upon securing a favorable opinion from the Attorneys General's Office, the Insurance Division approved a distribution as follows:

| <u>Declared date</u> | <u>Paid date</u> | <u>Amount</u> | <u>Description</u> |
|----------------------|------------------|---------------|--------------------|
| 11/26/2008           | 12/31/2008       | \$ 41,600,000 | Extraordinary      |

The \$41.6 million cash distribution was approved by the Oregon Insurance Division on December 12, 2008, pursuant to ORS 732.576(6).

**Surplus Notes**

The Company had issued surplus notes to Regence Bluecross Blueshield of Oregon (RBCBSO) in exchange for cash on the following dates:

| <u>Issue Date</u> | <u>Interest Rate</u> | <u>Par Value</u>    | <u>Carrying Value</u> |
|-------------------|----------------------|---------------------|-----------------------|
| June 1997         | 6.0%                 | \$21,000,000        | \$21,000,000          |
| September 1998    | 6.0%                 | 19,000,000          | 19,000,000            |
| March 1999        | 6.0%                 | <u>20,000,000</u>   | <u>20,000,000</u>     |
| Total             |                      | <u>\$60,000,000</u> | <u>\$60,000,000</u>   |

The original surplus note issued in June 1997 was for \$36,000,000. In December 2002, the Company repaid \$15 million principal and \$5 million interest on its surplus notes to RCBBSO, after receiving approval from DCBS.

Under the terms of the surplus notes, the repayment of principal or interest requires the permission of the director of the Department of Consumer and Business Services. On March 21, 2007, Company management submitted a request to the director for approval to pay all its outstanding surplus notes and related accumulated interest in four quarterly payments. The request was approved by the director, and the Company made the surplus note repayment and interest payments as follows:

| <u>Date of payment</u> | <u>Principal</u> | <u>Interest</u> | <u>Date approved</u> |
|------------------------|------------------|-----------------|----------------------|
| 3/31/2007              | \$15,000,000     | \$8,000,000     | 3/26/2007            |
| 6/30/2007              | 15,000,000       | 8,000,000       | 6/12/2007            |
| 9/30/2007              | 15,000,000       | 8,000,000       | 9/18/2007            |
| 12/31/2007             | 15,000,000       | 9,040,247       | 12/17/2007           |

No surplus notes were outstanding at December 31, 2008.

## CORPORATE RECORDS

### Board Minutes

In general, the review of 2006 to 2009 Board meeting minutes of the Company and of TRG, as well as the various committees authorized by TRG, indicated that the minutes support the transactions of the Company and clearly describe the actions taken by its directors and

officers. A quorum, as defined by ORS 731.302, met at all of the meetings held during the period under review. Regular Board meetings are held quarterly.

TRG's Investment Committee approved investments and monitored the investment guidelines for TRG and each of its subsidiaries. Minutes of their meetings were approved by the Company's Board of Directors in accordance with ORS 733.730. TRG's Personnel and Compensation Committee approved officer salaries. The Company's Board approved the TRG Personnel and Compensation Committee's actions pursuant to ORS 732.320(3).

### **Articles of Incorporation**

The Company's Articles of Incorporation were not amended during the period under examination. The Articles of Incorporation conformed to Oregon statutes.

### **Bylaws**

The Company amended its corporate Bylaws twice during the period under examination; on June 6, 2006 to reflect the reduction in the number of directors, and April 12, 2008, to establish two classes of directors, to change the term of office from one year to three years, and to set a mandatory retirement age at 70. The Company shares a common Board of Directors with its upstream parent, RBCBSO.

The Bylaws conformed to Oregon statutes.

### **Holding Company Registration Statement**

An insurance holding company registration statement was filed by the Company in accordance with the provisions of ORS 732.552, ORS 732.554, and Oregon Administrative Rule (OAR) 836-027-0020(1).

## MANAGEMENT AND CONTROL

### Board of Directors

Article II, section 2, of the Company's Amended Bylaws state that the number of directors shall not be more than seven (7) or less than five (5). In addition, the Bylaws specify that there be two classes of directors, outside and inside. Outside directors shall be a person who is not an employee of an affiliate or of the corporation. Inside directors shall be a person who is an employee of the corporation. Only the CEO of TRG and the corporate president may be an inside director. Generally, directors shall serve one or more terms of three years, staggered so that approximately 1/3 are elected each year. A majority of the number of directors constitutes a quorum. The Board of Directors met all requirements of ORS 750.015.

As of December 31, 2008, the Company's Board of Directors was as follows:

| <u>Name and Address</u>                       | <u>Principal Occupation</u>   | <u>Member Since</u> |
|---|---|---------------------|
| William L. Chenevich<br>Portland, Oregon      | Vice Chairman<br>US Bancorp   | 2004                |
| Peggy Y. Fowler<br>Tigard, Oregon             | CEO<br>Portland General Electric  | 2005                |
| Mark B. Ganz<br>Portland, Oregon              | CEO<br>The Regence Group  | 2004                |
| William R. Lee, MD<br>Portland, Oregon        | Physician   | 1995                |
| Luis Machuca<br>Hillsboro, Oregon             | President and CEO<br>Kryptiq Corporation  | 2008                |
| J. Bart McMullan Jr. M.D.<br>Portland, Oregon | President<br>Regence BlueCross BlueShield of OR<br>Regence Health Maintenance of OR<br>Regence HMO Oregon | 2004                |
| John W. Morgan<br>Portland, Oregon            | President and CEO<br>HemCon Medical Technologies, Inc.  | 2008                |

Dr. McMullan announced his retirement in September 2009, and was replaced by Jared L. Short.

Article IV of the Amended Bylaws state the board shall have no standing committees. Instead, TRG authorized five different committees to assist in the management of all its subsidiaries. The committees are: 1) Organizational & Governance Committee; 2) Investment Committee; 3) Audit & Compliance Committee; 4) Personnel & Compensation Committee; and 5) Health Care Services Committee. The various committees provide direction to the Group within the area/field in which they are assigned. The committees' actions are summarized and reported to TRG's board of directors during their regular meetings. The actions and minutes of each of the committees are approved during the Company's board of director meetings.

### **Officers**

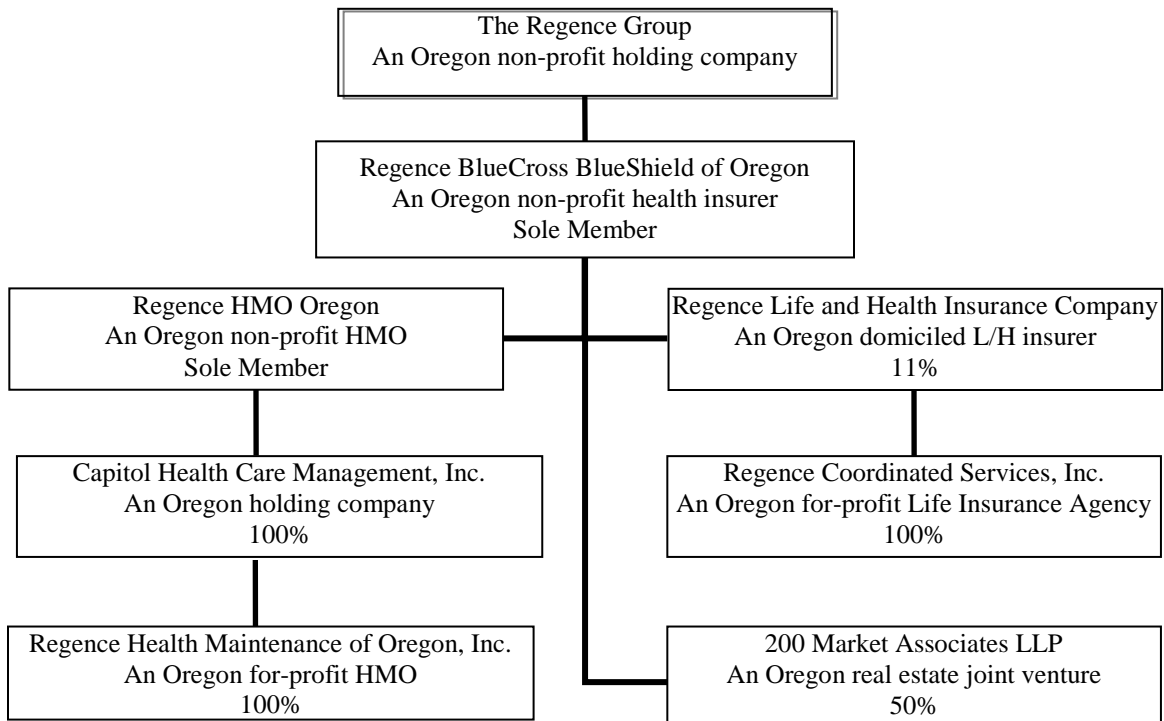
Operating management of the Company as of December 31, 2008, was under the direction of the following principal officers:

| <b><u>Officer</u></b>   | <b><u>Office</u></b>               |
|-------------------------|------------------------------------|
| John B. McMullan Jr. MD | President                          |
| Steven L. Hooker        | Treasurer                          |
| Kerry E. Barnett        | Secretary                          |
| Stephanie C. Dreyfuss   | Vice President – Provider Services |
| Dorane L. Wintermeyer   | Vice President – Sales             |
| Michael T. Mudrow       | Assistant Secretary                |

Dr. McMullan retired in September 2009, and was replaced by Jared L. Short. Steven Hooker announced his retirement in December 2009. He was replaced by Andreas B. Ellis. Dorane Wintermeyer is no longer with Regence and has not yet been replaced.

**Affiliated Companies**

The Company is part of a holding company system in which TRG is the ultimate parent. TRG is a nonprofit Oregon Corporation governed by an 11-member board of directors and is the sole member of RBCBSO, Regence BlueShield (RBS), and Regence BlueCross BlueShield of Utah (RBCBSU). In addition, TRG manages the operations of Regence BlueShield of Idaho (RBSI) under the terms of a long-term management services agreement. The following organization chart depicts the relationship of Oregon affiliates within the Regence group.



The following is a description of the parent, affiliates and subsidiaries:

Regence BlueCross BlueShield of Oregon (RBCBSO) is authorized to conduct business as a health care service contractor in the states of Oregon and Washington. Also, RBCBSO is licensed as a foreign corporation by the Secretary of State of Idaho. The company operates as a Blue Cross and Blue Shield plan subject to operational and performance standards

established by the national Blue Cross and Blue Shield Association. RBCBSO is the sole member of the Company and would be considered to be the direct parent.

Capitol Health Care Management, Inc. (CHCM) is an Oregon for-profit business corporation which functions as a down stream holding company to own all the stock of RHO subsidiaries and to consolidate the income tax results of the for-profit subsidiaries of RHO. CHCM owns 100% of the RHMO's common stock.

Regence Health Maintenance of Oregon, Inc. (RHMO) is a for-profit Oregon health care service contractor federally qualified as a health maintenance organization. RHO ceased writing business in 2005.

Regence Life and Health Insurance Company (RLH) is an Oregon domiciled for-profit insurer licensed to conduct the business of life and accident and health insurance in Alaska, Idaho, Montana, Oregon, Utah, and Washington.

Regence Coordinated Services, Inc. (RCS) is a for-profit life and health insurance agency owned by RLH, and formed by the four TRG regional plans, which merged four regional insurance agency subsidiaries into RCS. In consideration of this transaction, each of the affiliated plans received shares of RLH stock (RBS – 75%, RBCBSU – 12%, RBCBSO – 11%, and RBSI – 2%).

200 Market Associates LP is a limited partnership formed by RBCBSO and Russell Development Company, each with a 50% ownership, to own and operate an office building located at 200 SW Market Street, Portland, Oregon.

## **INTERCOMPANY AGREEMENTS**

### **Regence Administrative Services Agreement**

Effective December 28, 2007, TRG entered into a cost-sharing agreement with each of the Regence Plans in Idaho, Oregon, Utah and Washington, including their subsidiary companies. Under the terms of the agreement, TRG will provide all operational, administrative, and management services reasonably necessary to transact business. These services include managerial, legal, financial, actuarial, underwriting, accounting, human resources, billing, membership, claims adjudication, customer service, reporting, regulatory compliance, and all applicable technical, clerical and communication support, as well as all necessary equipment, materials, office space and general supplies. Reimbursement will be made using a cost allocation method described in the contract, and it is the intent that TRG receive full compensation for the cost of its services and general overhead and taxes, and that no profit be derived from the agreement. This complies with the provisions of ORS 732.215. Reconciliations will be performed monthly, and settlement of expenses shall be made 90 days after the month end. The agreement will automatically renew each year, unless cancelled by any party upon 30 days written notice. The Insurance Division approved the agreement on February 13, 2008, in accordance with ORS 732.574(2)(d).

### **Management Agreement with RCBBSO**

RCBBSO performs certain functions for the Company under a management agreement entered into and effective January 1, 1999, including the use of RCBBSO's employees for performing the operations of the Company. Some of the functions that RCBBSO performs under the management agreement include: accounting, data processing, marketing, financial reporting, budgeting, provider contracting and policy services. In return for these services, the Company agrees to pay all costs and expenses that are directly attributable to its operations. Indirect expenses are charged to the Company using a written cost allocation

plan. The allocation method appeared to be reasonable and therefore meets the provisions of ORS 732.574(1)(b).

### **Insolvency Agreement**

Effective August 1, 1991, the Company entered into an agreement with RBCBSO whereby RBCBSO agrees, in the event of insolvency of the Company, to make payments to policyholders for covered services.

### **CONFLICT OF INTEREST**

The Company's Code of Business Conduct provides for conflict of interest disclosure in the form of a questionnaire that is completed annually by the Company's Board of Directors, officers, and employees. All personnel performed due diligence in completing the questionnaire. From a review of the questionnaires of board members and senior management, there were no material conflicts of interest reported.

### **FIDELITY BOND AND OTHER INSURANCE**

A review of the adequacy of limits, retentions, and the solvency of the insurers providing the insurance was considered during the examination of the Company's insurance coverage. TRG purchased insurance covering itself and all its subsidiaries. A fidelity bond covered losses up to \$15,000,000 per occurrence, net of a \$50,000 deductible, caused by employees' dishonesty and fraud. This coverage exceeded the minimum coverage recommended by the NAIC *Financial Condition Examiners Handbook*. Executive liability risks and D&O risks are covered up to \$50,000,000 per loss occurrence net of a \$250,000 deductible. Other insurance coverages in force at December 31, 2008, included property, commercial general and excess liability, automobile liability, umbrella liability, fiduciary liability, computer crime liability, and workers' compensation. All insurance limits and deductibles appeared adequate as of December 31, 2008.

## **PENSION PLANS AND OTHER EMPLOYEE BENEFITS**

The Company does not have its own employees, but does contribute to the pension and other employee benefits assessed for employees performing work for it.

### **Employee Retirement Plan**

The Company participates in a defined-benefit pension plan sponsored by TRG that covers substantially all regular employees having one or more years of service. Benefits are based upon years of service and the employee's final average compensation. The Company also participates in a supplemental executive retirement plan sponsored by TRG to cover key employees meeting specific eligibility requirements. The Company's practice is to reimburse TRG for employee retirement plan obligations and to record such amounts as employment related expenses. The Company has no legal obligation for benefits under these plans; the obligation is carried by TRG. As sponsor of the plan, however, TRG is legally required to fund the plans regardless of amounts paid to TRG by the Company. The Company's share of net expenses for the retirement plans was \$0 and \$1,000 in 2008 and 2007, respectively.

Effective December 31, 2009, the defined-benefit pension plan was frozen. Subsequent to the freeze date, there will be no new participants enrolled in the plan and no pension benefits will be earned after that date. Benefits-eligible employees who have not yet met plan eligibility criteria were immediately eligible and non-vested plan participants became fully vested.

### **Employee 401(k) Plan**

The Company participates in an employee savings plan sponsored by TRG in which the Company will match employee contributions up to 50 percent of the first 6% of salary for each pay period in which the employee makes a contribution. Beginning January 1, 2010, this employee match will increase up to 100% of the first 6% of salary for each pay period in

which the employee makes a contribution. In addition, a discretionary contribution of up to 5% of eligible earnings for eligible employees will be added, subject to annual review and board approval. Expense is allocated to the Company based on the portion of the employees' functional activities that relate to the Company. The Company has no legal obligation for benefits under this plan; the obligation is carried by TRG. As sponsor of the plan, however, TRG is legally required to fund the plan regardless of amounts paid to TRG by the Company. The Company contributed no net expenses for the savings plan during the period under examination.

### **Post-retirement Benefits Plan**

The Company participates in a post-retirement health and welfare plan sponsored by TRG for retired employees, subject to certain eligibility rules based on age and years of service at retirement date. Employees hired after January 1, 2004, are not eligible for benefits. Expenses are allocated to the Company monthly, based on relative employee count. The Company has no legal obligation for benefits under this plan; the obligation is carried by TRG. As sponsor of the plan, however, TRG is legally required to fund the plan regardless of amounts paid to TRG by the Company. The Company contributed no net expenses for the benefits plan during the period under examination.

Coverage for eligible participants who retire on or after January 2, 2010, will terminate the date the participant or beneficiary attains Medicare eligibility on the basis of age or disability, regardless of whether the participant or beneficiary becomes entitled to Medicare.

Eligible participants who retire on or after January 2, 2010, and already are eligible for Medicare on the basis of age or disability will not be eligible to enroll in the plan. Retirees must be enrolled as a participant in the active employee health and welfare plan immediately

prior to retirement in order to be eligible to enroll in the plan, except for those individuals retiring between October 1, 2009, and January 1, 2010.

### **TERRITORY AND PLAN OF OPERATION**

The Company ceased writing business in 2005.

### **GROWTH OF THE COMPANY**

Growth of the Company over the past five years is reflected in the following schedule. Amounts were derived from Company's filed annual statements, except in those years where a report of examination was published by the Oregon Insurance Division.

| <b><u>Year</u></b> | <b><u>Assets</u></b> | <b><u>Liabilities</u></b> | <b><u>Capital and Surplus</u></b> | <b><u>Net Income (Loss)</u></b> |
|--------------------|----------------------|---------------------------|-----------------------------------|---------------------------------|
| 2004               | \$131,435,380        | \$11,665,267              | \$119,770,112                     | \$10,921,711                    |
| 2005*              | 125,594,466          | 1,260,702                 | 124,333,766                       | 3,998,735                       |
| 2006               | 108,747,021          | 2,969,766                 | 105,777,255                       | 2,367,731                       |
| 2007               | 47,874,256           | 460,564                   | 47,413,692                        | 4,253,270                       |
| 2008*              | 7,511,331            | 1,208,978                 | 6,302,353                         | 460,577                         |

\*Per examination

The Company ceased writing business in 2005. As noted earlier in this report of examination, the Company repaid \$60,000,000 in surplus notes in 2007 and paid a \$41,600,000 cash distribution to its immediate parent in 2008.

### **LOSS EXPERIENCE**

The following exhibit reflects the annual underwriting results of the Company over the last five years. The amounts were compiled from copies of the Company's filed annual statements and, where indicated, from the examination reports.

| <u>Year</u> | <u>(1)<br/>Total Revenues</u> | <u>(2)<br/>Total Hospital<br/>and Medical</u> | <u>(3)<br/>CAE and General<br/>Expenses</u> | <u>(2)+(3)/(1)<br/>Combined<br/>Loss Ratio</u> |
|-------------|-------------------------------|---|---|--|
| 2004        | \$84,980,398                  | \$74,481,827                                  | \$9,734,600                                 | 99.1%  |
| 2005*       | (193,346)                     | 205,986                                       | 1,057,500                                   | (653.5)%                                       |
| 2006        | 0                             | (45,168)                                      | 1,237,765                                   | 0.0%   |
| 2007        | 0                             | 12,243  | 438,512                                     | 0.0%   |
| 2008*       | 0                             | 0   | 1,051,559                                   | 0.0%   |

\*Per examination

The Company ceased writing business during 2005.

### **REINSURANCE**

The Company has an excess of loss agreement with RBCBSO whereby the Company cedes 100% of its losses related to commercial institutional fund benefits above \$200,000. In accordance with the terms of the agreement, the Company agrees to pay RBCBSO a premium on a per-member per-month basis for this reinsurance coverage.

The reinsurance agreement contained a proper insolvency clause in accordance with ORS 731.508(3) as required to take reserve credits for reinsurance ceded. In addition, the Company does not retain risk on any one subject of insurance in an amount exceeding 10% of its surplus pursuant to the provisions of ORS 731.504.

### **ACCOUNTS AND RECORDS**

In general, the Company's records and source documentation supported the amounts presented in the Company's December 31, 2008 annual statement and were maintained in a manner by which the financial condition was readily verifiable pursuant to the provisions of ORS 733.170. From a review of the Company's disaster recovery plan, it was determined that the current information system possessed the physical and internal controls as prescribed by the NAIC.

## **COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS**

No recommendations were made in the 2005 examination report.

## **FINANCIAL STATEMENTS**

The following examination financial statements show the financial conditions of Regence Health Maintenance of Oregon, Inc., as of December 31, 2008:

Statutory Balance Sheet  
Statement of Revenues and Expenses  
Reconciliation of Surplus Since the last Examination

**REGENCE HMO OREGON  
BALANCE SHEET  
AS OF DECEMBER 31, 2008**

|   | BALANCE<br>PER COMPANY     | EXAM<br>ADJUSTMENT | BALANCE<br>PER EXAM        | NOTE |
|---|----------------------------|--------------------|----------------------------|------|
| <b>Assets</b>   |                            |                    |                            |      |
| Bonds   | \$ 3,135,848               | -                  | \$ 3,135,848               | 1    |
| Properties occupied by company                        | 2,709,995                  | -                  | 2,709,995                  |      |
| Cash and short-term investments                       | 1,032,866                  |                    | 1,032,866                  |      |
| Receivables for securities                            | 232                        | -                  | 232                        | 1    |
| Aggregate write-ins for invested assets               | -                          | -                  | -                          |      |
| Subtotal, cash and invested assets                    | <u>\$ 6,878,941</u>        | <u>\$ -</u>        | <u>\$ 6,878,941</u>        |      |
| Investment income due and accrued                     | 9,840                      | -                  | 9,840                      |      |
| Current FIT recoverable                               | 519,495                    | -                  | 519,495                    |      |
| Receivables from parent, subsidiaries, and affiliates | 58,527                     | -                  | 58,527                     |      |
| Aggregate write-ins for other than invested assets    | 44,528                     | -                  | 44,528                     |      |
| Total Assets  | <u><u>\$ 7,511,331</u></u> | <u><u>\$ -</u></u> | <u><u>\$ 7,511,331</u></u> |      |
| <b>Liabilities, Capital and Surplus</b>               |                            |                    |                            |      |
| Claims unpaid   | -                          | -                  | -                          | 2    |
| Unpaid claims adjustment expense                      | -                          | -                  | -                          | 2    |
| General expenses due or accrued                       | 48,162                     | -                  | 48,162                     |      |
| Current FIT payable                                   | 1,022,656                  | -                  | 1,022,656                  |      |
| Net deferred tax liabilities                          | 82                         | -                  | 82                         |      |
| Amounts due to parent, subsidiaries, and affiliates   | 100,000                    | -                  | 100,000                    |      |
| Payable for securities                                | 37,115                     | -                  | 37,115                     |      |
| Aggregate write-ins for liabilities                   | 963                        | -                  | 963                        |      |
| Total Liabilities                                     | <u>\$ 1,208,978</u>        | <u>\$ -</u>        | <u>\$ 1,208,978</u>        |      |
| Common capital stock                                  | -                          |                    | -                          |      |
| Gross paid in and contributed surplus                 | 1,620,928                  | -                  | 1,620,928                  |      |
| Unassigned funds (surplus)                            | 4,681,425                  | -                  | 4,681,425                  |      |
| Total capital and surplus                             | <u>6,302,353</u>           | <u>-</u>           | <u>6,302,353</u>           |      |
| Total liabilities, capital and surplus                | <u><u>\$ 7,511,331</u></u> | <u><u>\$ -</u></u> | <u><u>\$ 7,511,331</u></u> |      |

**REGENCE HMO OREGON  
STATEMENT OF REVENUE AND EXPENSES  
FOR THE YEAR ENDED DECEMBER 31, 2008**

|   | BALANCE<br>PER COMPANY | EXAMINATION<br>ADJUSTMENT | BALANCE<br>PER EXAM | NOTE |
|---|------------------------|---------------------------|---------------------|------|
| Net premium income  | \$ -                   | \$ -                      | \$ -                |      |
| Fee-for-service   | -                      | -                         | -                   |      |
| Aggregate write-ins for other non-health care related revenue   | -                      | -                         | -                   |      |
| <b>Total Revenues</b>   | <b>-</b>               | <b>-</b>                  | <b>-</b>            |      |
| <b>Hospital and Medical:</b>                                    |                        |                           |                     |      |
| Hospital/medical benefits                                       | -                      | -                         | -                   |      |
| Other professional services                                     | -                      | -                         | -                   |      |
| Outside referrals   | -                      | -                         | -                   |      |
| Emergency room and out-of-area                                  | -                      | -                         | -                   |      |
| Prescription drugs  | -                      | -                         | -                   |      |
| Incentive pool, withhold adjustments and bonus amounts          | -                      | -                         | -                   |      |
| <b>Subtotal:</b>  | <b>-</b>               | <b>-</b>                  | <b>-</b>            |      |
| <b>Less:</b>  |                        |                           |                     |      |
| Net reinsurance recoveries                                      | -                      | -                         | -                   |      |
| <b>Total medical and hospital</b>                               | <b>-</b>               | <b>-</b>                  | <b>-</b>            |      |
| Non-health claims   | -                      | -                         | -                   |      |
| Claim adjustment expenses                                       | -                      | -                         | -                   |      |
| General administrative expenses                                 | 1,051,559              | -                         | 1,051,559           |      |
| Increase in reserves for life and accident and health contracts | -                      | -                         | -                   |      |
| <b>Total underwriting deductions</b>                            | <b>1,051,559</b>       | <b>-</b>                  | <b>1,051,559</b>    |      |
| <b>Net underwriting gain or loss</b>                            | <b>(1,051,559)</b>     | <b>-</b>                  | <b>(1,051,559)</b>  |      |
| Net investment income earned                                    | 3,072,163              | -                         | 3,072,163           |      |
| Net realized capital gains or (losses)                          | (965,127)              | -                         | (965,127)           |      |
| Net investment gains or (losses)                                | 2,107,036              | -                         | 2,107,036           |      |
| Aggregate write-ins for other income or expense                 | -                      | -                         | -                   |      |
| <b>Net income or (loss) before federal income taxes</b>         | <b>1,055,477</b>       | <b>-</b>                  | <b>1,055,477</b>    |      |
| Federal and foreign income taxes incurred                       | 594,900                | -                         | 594,900             |      |
| <b>Net Income (loss)</b>  | <b>\$ 460,577</b>      | <b>\$ -</b>               | <b>\$ 460,577</b>   |      |

**REGENCE HMO OREGON**  
**RECONCILIATION OF SURPLUS SINCE THE LAST EXAMINATION**  
**FOR THE YEAR ENDED DECEMBER 31**

|   | 2008                | 2007                 | 2006                  |
|---|---------------------|----------------------|-----------------------|
| Capital and surplus, December 31, previous                  | \$ 47,413,698       | \$ 105,777,260       | \$ 124,333,771        |
| Net income  | 460,577             | 4,253,270            | 2,367,731             |
| Change in net unrealized capital gains (losses)             | 118,460             | (21,817,529)         | 2,788,380             |
| Change in net deferred income tax                           | 28,085              | (115,906)            | 125,155               |
| Change in nonadmitted assets                                | (118,460)           | 19,316,603           | (23,837,777)          |
| Change in unauthorized reinsurance                          | -                   | -                    | -                     |
| Change in surplus notes                                     | -                   | (60,000,000)         | -                     |
| Cumulative effects of changes in accounting principles      | -                   | -                    | -                     |
| Capital changes:  | -                   | -                    | -                     |
| Paid in   | -                   | -                    | -                     |
| Transferred from surplus (Stock Dividend)                   | -                   | -                    | -                     |
| Transferred to surplus                                      | -                   | -                    | -                     |
| Surplus adjustments:  | -                   | -                    | -                     |
| Paid in   | -                   | -                    | -                     |
| Transferred to capital (Stock Dividend)                     | -                   | -                    | -                     |
| Transferred from capital                                    | (41,600,000)        | -                    | -                     |
| Dividends to stockholders (cash)                            | -                   | -                    | -                     |
| Examination adjustment (1)                                  | (7)                 | -                    | -                     |
| Aggregate write-ins for gains and losses in surplus         | -                   | -                    | -                     |
| Change in surplus as regards policyholders for the year     | <u>(41,111,345)</u> | <u>(58,363,562)</u>  | <u>(18,556,511)</u>   |
| Surplus as regards policyholders, December 31, current year | <u>\$ 6,302,353</u> | <u>\$ 47,413,698</u> | <u>\$ 105,777,260</u> |

(1) Rounding error

## NOTES TO FINANCIAL STATEMENTS

### Note 1 – Invested Assets

At year-end 2008, all of the Company's long-term bond investments were in US government obligations. The Company did not have any exposure to mortgaged-backed or asset-backed securities. Cash and short-term deposits consisted of cash on deposit and a short-term treasury money market fund. A comparison of the investments over the past five years is as follows:

| <u>Year</u> | <u>A</u><br><u>Bonds</u> | <u>B</u><br><u>Common</u><br><u>Stock</u> | <u>C</u><br><u>Cash and</u><br><u>Short-term</u> | <u>Ratio</u><br><u>A/</u><br><u>Total Assets</u> | <u>Ratio</u><br><u>B/</u><br><u>Total Assets</u> | <u>Ratio</u><br><u>C/</u><br><u>Total Assets</u> |
|-------------|--------------------------|---|--|--|--|--|
| 2004        | \$54,134,242             | \$44,148,047                              | \$23,451,503                                     | 41.2%  | 33.6%  | 17.8%  |
| 2005*       | 61,293,955               | 44,344,491                                | 12,774,250                                       | 48.8%  | 35.3%  | 10.2%  |
| 2006        | 63,964,057               | 24,489,075                                | 15,208,148                                       | 58.8%  | 22.5%  | 14.0%  |
| 2007        | 19,830,468               | 0   | 12,566,393                                       | 41.4%  | 0.0%   | 26.2%  |
| 2008*       | 3,135,848                | 0   | 1,032,866  | 41.7%  | 0.0%   | 13.8%  |

\*Per examination

The minutes indicated that the Board reviews and approves investments in accordance with the provisions of ORS 733.730 and ORS 733.740. As of December 31, 2008 invested assets with a reported book value of \$3,235,848, representing 47% 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.

Effective December 29, 2005, the Company entered into an amended and restated custodial agreement with Mellon Bank, NA. The agreement appears to contain all of the relevant protections described in OAR 836-027-0200(4)(a) through (l).

### Note 2 - Claims Unpaid and Claims Adjustment Expenses

Scott L. Fitzpatrick, FSA, MAAA, life and health actuary for the Oregon Insurance Division, reviewed the loss and loss adjustment expenses in the Company's filed financial statements as of December 31, 2008. The purpose of his review was to determine, in general, if the Company's liabilities were reasonably stated. In his opinion, he concluded:

|                                     | My Estimate | Company Estimate |
|-------------------------------------|-------------|------------------|
| Claims Unpaid                       | \$0         | \$0              |
| Accrued Med. Incentive Pool & Bonus | \$0         | \$0              |
| Unpaid Claims Adjustment Expenses   | \$0         | \$0              |
| Aggregate Health Policy Reserves    | \$0         | \$0              |
| Aggregate Health Claim Reserves     | \$0         | \$0              |
| Experience Rated Refunds            | \$0         | \$0              |
| Any Other Actuarial Liabilities     | \$0         | \$0              |

My total estimate for actuarial liabilities exactly matches the company's estimate, since the company is dormant and no actuarial liabilities currently exist. Therefore, the statement of the actuarial liabilities at year-end for the annual statement was appropriate and adequate.

### **SUMMARY OF COMMENTS AND RECOMMENDATIONS**

There were no comments or recommendations as a result of this report of examination, and no adjustments to surplus were made.

### **CONCLUSION**

During the period covered by this examination, the capital and surplus of the Company has decreased from \$124,333,766 as presented in the December 31, 2005 report of examination to \$6,302,353 as shown in this report of examination. The comparative assets and liabilities are shown below:

|             | <b><u>2008</u></b>  | <b><u>December 31,</u></b> | <b><u>2005</u></b>   | <b><u>Change</u></b>   |
|-------------|---------------------|----------------------------|----------------------|------------------------|
| Assets      | \$ 7,511,331        |                            | \$125,594,468        | \$(118,083,137)        |
| Liabilities | <u>1,208,978</u>    |                            | <u>1,260,702</u>     | <u>(51,724)</u>        |
| Surplus     | <u>\$ 6,302,353</u> |                            | <u>\$124,333,766</u> | <u>\$(118,031,413)</u> |

## ACKNOWLEDGMENT

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

In addition to the undersigned, Raymond W. Anderson, CFE, Mark A. Giffin, CFE, and Ellen Quale, CPA, AFE, insurance examiners, and Scott Fitzpatrick, FSA, MAAA, Life and Health Actuary, for the State of Oregon, Department of Consumer and Business Services, Insurance Division, participated in the examination. David L. Daulton, CFE, of the firm Huff, Thomas and Company, and Aaron Phillips, examiner for the Utah Department of Insurance, also participated in this examination, both representing the State of Utah.

Respectfully submitted,

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Greg A. Lathrop, CFE  
Supervising Insurance Examiner  
Insurance Division  
Department of Consumer and Business Services  
State of Oregon

**AFFIDAVIT**

STATE OF OREGON            )  
  )  ss  
County of Marion            )

Greg A. Lathrop, CFE, being duly sworn, states as follows:

1.     I have authority to represent the state of Oregon in the examination of Regence HMO Oregon.
  
2.     The Insurance Division of the Department of Consumer and Business Services of the state of Oregon is accredited under the National Association of Insurance Commissioners Financial Regulation Standards and Accreditation.
  
3.     I have reviewed the examination work papers and examination report, and the examination of Regence HMO Oregon was performed in a manner consistent with the standards and procedures required by the Oregon Insurance Code.

The affiant says nothing further.

\_\_\_\_\_  
Greg A. Lathrop, CFE  
Supervising Financial Examiner  
Department of Consumer and Business Services  
State of Oregon

Subscribed and sworn to me this \_\_\_\_\_ day of \_\_\_\_\_, 2010.

\_\_\_\_\_  
Notary Public for the State of Oregon

My Commission Expires: \_\_\_\_\_