



STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**OREGON DENTAL SERVICE
PORTLAND, OREGON**

NAIC COMPANY CODE 54941

AS OF

DECEMBER 31, 2009

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SALUTATION

October 8, 2010

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

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

Dear Commissioner and Director:

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

OREGON DENTAL SERVICE
601 SW Second Avenue
Portland, Oregon 97204

NAIC Company Code 54941

hereinafter referred to as the "Company." The following report is respectfully submitted.

SCOPE OF EXAMINATION

The full scope single-state examination of the Company was conducted as of December 31, 2009, 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.

We conducted our examination pursuant to ORS 731.300 and in accordance with the NAIC Financial Condition Examiners 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. An examination also includes 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 instruction when applicable to domestic state regulations.

All accounts and activities of the Company were considered in accordance with the risk focused examination process.

David Dillon, FSA, MAAA, of the firm Lewis & Ellis, participated in this examination by evaluating claims unpaid and unpaid claim adjustment expenses, as well as other items requiring actuarial expertise. The results of his analysis are found under the relevant section of this report.

Concurrent with this examination, two indirect insurance subsidiaries of the Company, ODS Health Plan, Inc., and Dentists Benefits Insurance Company, were also examined as of

December 31, 2009. There was a separate report of financial examination made for each company.

COMPANY HISTORY

The Company was incorporated in 1961 under the laws of the State of Oregon and under the sponsorship of the Oregon Dental Association (ODA) as the Oregon Dental Health Foundation, a nonprofit corporation. The Company received its Certificate of Authority as a domestic health care service contractor on July 23, 1962, under ORS Chapter 750. The Company adopted its current name on February 14, 1966.

The Articles of Incorporation provide for no capital stock and define the purpose of the Company as the promotion and improvement of dental health and dental hygiene in the State of Oregon without profit to the corporation. The Oregon Secretary of State Corporation Division registered the Company as a mutual benefit non-profit corporation.

On November 27, 2000, the Insurance Division approved a corporate reorganization in which the ODA, the ultimate controlling entity of the Company and sole shareholder of Health Services Group (HSG), donated all of its outstanding HSG stock to the Company. HSG owns ODS Health Plan, Inc., which in turn owns Dentists Benefits Insurance Company. As a result, HSG and all of its subsidiaries became a direct or indirect subsidiary of the Company.

CORPORATE RECORDS

Board Minutes

In general, the review of 2007 to 2009 Board meeting minutes of the Company, as well as the various committees authorized by the Board, 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. The Board maintained a quarterly meeting schedule.

The finance committee approved investments at each meeting and monitored the investment guidelines as needed, which was then approved by the Board as a whole, in accordance with ORS 733.730. The Board's compensation/governance committee approved officer salaries. The Company's Board then approved the committee's actions pursuant to ORS 732.320(3).

Articles of Incorporation

No changes were made during the period under examination. The Articles of Incorporation conformed to the Oregon Insurance code.

Bylaws

The Company's Bylaws were amended three times during the period under examination. First, on April 28, 2007, the Board added Article 1, section 1.4 authorizing the corporation to operate one or more educational institutions (ODS College of Dental Sciences). Second, on January 2, 2008, the Board amended Article 2, section 2.2 to establish the number of directors from sixteen (16) to any number between thirteen (13) and sixteen (16) and changing the number of directors in class (i) and class (ii) to correspond to the total number of directors; also, amended Article 2, section 2.2, subsection 2, to increase each directors' term from three years to four years, staggering the board from three groups into four groups. And third, on March 7, 2008, the Board amended Article 2, section 2.13, subsection 1, to change the way ODA may fill vacancies, including those created by increasing the size of the board. The Bylaws conformed to Oregon statutes.

Parent, Subsidiaries and Affiliated Companies

The Company filed an Insurance holding company registration statement on behalf of itself and its insurance subsidiaries in accordance with the provisions of ORS 732.552, ORS

732.554, and Oregon Administrative Rule (OAR) 836-027-0020. The holding company structure is comprised of the following entities:

Oregon Dental Association (ODA) is an Oregon nonprofit professional association formed in 1949. It is one of the five constituent dental societies that comprise the American Dental Association's Eleventh Trustee District. Members of the ODA are made up of licensed dentists in the State of Oregon. The Board of Trustees of the ODA appoints all but one director to the Company's Board of Directors, and would be considered the ultimate controlling entity.

Health Services Group (HSG) is an Oregon for-profit stock corporation owned 100% by the Company. It was formed in 1991 as a management company. It maintains all employees, facilities and operations used by the Company under a management agreement described below.

Dentists Management Corporation (DMC) is a wholly owned subsidiary of HSG whose primary function is to market a dental practice management system known as DAISY.

Dentists Benefits Corporation (DBC) is an insurance agency wholly owned by HSG. Its primary purpose is to market professional liability and other property and casualty coverages to Oregon dentists. DBC provides marketing services for DBIC and NORDIC.

Northwest Dentists Insurance Company (NORDIC) is a Washington domiciled property and casualty insurer owned 75% by HSG and 25% by the Washington State Dental Association. HSG purchased its ownership of NORDIC in February 2007. It writes property/general liability and professional liability coverages primarily in Washington and Idaho.

ODS Health Plan, Inc. (ODSHP) is a wholly owned subsidiary of HSG. ODSHP is a health care service contractor that received a Certificate of Authority from the Oregon Insurance Division in October 1999. This company provides group major medical and pharmacy insurance coverage in the States of Oregon and Alaska. ODSHP was created to handle the group medical business formerly written by the Company.

Dentists Benefits Insurance Company (DBIC) is a wholly owned subsidiary of ODSHP. DBIC was issued a Certificate of Authority from the Oregon Insurance Division as a property and casualty insurer. DBIC markets professional liability and commercial multi-peril coverages through DBC to dentists in eight states. DBIC commenced business in 1985.

ODS Plaza, Inc. is an Oregon business corporation wholly owned by ODSHP. This company was formed in 2005 to own and operate an office building located in Milwaukie, Oregon. This subsidiary was transferred to ODSHP from HSG on December 31, 2009.

BenefitHelp Solutions (fka BestChoice Administrators) is a third party administrator wholly owned by ODSHP. BestChoice Administrators was incorporated on January 24, 1994. The new name was adopted July 13, 2005.

ODS Community Health, Inc. (OCH) was incorporated in December 2003 for the purpose of handling business of the Oregon Health Plan, through the Division of Medical Assistance Programs (DMAP), and is a wholly owned subsidiary of ODS Health Plan, Inc.

ODS Bend Property LLC is an Oregon limited liability corporation wholly owned by ODSHP. This company was formed in 2007 to be a management company for an office building located in Bend, Oregon. The LLC owns approximately 74% of the office building. This subsidiary was transferred to ODSHP from HSG on December 31, 2009.

Statutory Deposit

At year-end 2009, the Company maintained two US T-Bills as deposits with the Oregon Insurance Division in the sum of \$369,000 (par value), for the benefit of all policyholders. These deposits were verified from the records of the Insurance Division.

MANAGEMENT AND CONTROL

Board of Directors

The Bylaws vest management and control of the Company in a Board of Directors of between 13 and 16 members, consisting of (i) not more than nine nor less than seven persons who are members in good standing of the ODA (ii) not more than six nor less than five persons, each of whom is neither an ODA member nor a practicing dentist, and (iii) the president of the Company. Directors serve terms of four years without limitation to the number of terms. All directors, with the exception of the president of the Company, are appointed by the ODA. A majority of the number of directors constitutes a quorum. The Board of Directors met all requirements of ORS 750.015.

Members of the Board of Directors, duly appointed and serving as of December 31, 2009, were:

<u>Name and Address</u>	<u>Principal Affiliation</u>	<u>Appointed</u>
Karen E. Anderegg Portland, OR 97225	Consultant	2000
Tracy S. Andrus Eagle, ID 83616	Consultant	2003
Wayne R. Barichello, DMD Oregon City, OR 97045	Dentist Barichello Family Dentistry	2005
Michael E. Biermann, DMD Portland, OR 97203	Pediatric Dentistry	2007
D. Jon Carnahan Salem, OR 97302	Consultant	1999

<u>Name and Address</u>	<u>Principal Affiliation</u>	<u>Appointed</u>
George J. Darke, DMD Vancouver, WA 98683	Retired Dentist	1998
Robert G. Gootee Portland, OR 97204	President & CEO Oregon Dental Service	1998
David W. Howerton, DMD** Salem, OR 97302	Associate Professor OHSU School of Dentistry	2004
Mark E. Jensen, DMD Bend, OR 97702	Dentist	2005
Jay C. Lamb, DMD* Eugene, OR 97401	Dentist	1991
Michael L. McKeel, DDS Gresham, OR 97030	Dentist	1996
Marta A. Monetti Portland, OR 97204	Sr. Vice President Edelman Public Relations	2007
Patrick M. Nearing, DMD La Grande, OR 97850	Dentist	2006
George J. Passadore Portland, OR 97225	President TriMet Board of Directors	2004
John C. Stevason Portland, OR 97204	Attorney Lane Powell PC	1999

*Chairman of the Board
**Vice Chairman of the Board

Officers

Operating management of the Company as of December 31, 2009, was under the direction of the following principal officers:

<u>Name</u>	<u>Office</u>
Robert G. Gootee	President and Chief Executive Officer
Thomas J. Bikales	Director of Legal and Regulatory Affairs and Secretary
Jonathan L. Jurevic	Senior Vice President, CFO and Treasurer
David W. Evans	Vice President, Controller and Asst. Secretary

Mr. Jurevic retired effective March 31, 2010, and was replaced by Steven Wynne. All other management functions are provided through a management agreement with HSG, as described below.

Intercompany Agreements

As of December 31, 2009, the Company was party to the following agreements with affiliates:

Management Agreement

The Company operates under a management agreement with HSG, dated January 1, 1995, and amended September 1, 2002. The management agreement states that HSG will provide all marketing, underwriting, claims, reinsurance, investment, financial and accounting, information systems and administrative functions to the Company. HSG will provide all equipment, computer software, furniture, fixtures and all tangible personal property used to transact business, as well as all employees and staff. Terms of the agreement include:

- the Company is to pay all costs and expenses that are directly attributable to its operations;
- indirect expenses are to be pooled and allocated using a fair and reasonable method; and
- those costs or expenses that inure to the sole benefit of HSG and do not benefit the Company shall be borne by HSG and shall not be subject to reimbursement.

It was noted the agreement did not specify a due date for payment, but stated HSG will invoice the Company from time to time (but not more frequently than monthly) and shall be paid by the Company within 15 business days of the date of the invoice. Sections 5.2 and 5.3 of the agreement allow HSG to hold all cash, by means of a sweep account, of the Company and all its indirect subsidiaries. The Company uses zero balance accounts, with the balances being swept into the HSG concentration account on a daily basis. At this point, the funds become the property of HSG, and an intercompany receivable or payable is established,

depending on the daily cash balance. Funds are swept back to the Company on an as needed basis, depending on its funding requirements. These funds are commingled and invested in investments held by HSG. All transactions are reconciled monthly, and balances held more than 90 days are paid interest equal to the 90-day US T-Bill rate as of the last business day of the month.

CONFLICT OF INTEREST

The Company has a conflict of interest policy that is stated in the ODS Code of Conduct. Board members, senior officers and key employees are required to annually sign a conflict of interest declaration. From a review of the completed conflict of interest questionnaires, it appeared that the affected personnel performed due diligence in completing the conflict of interest statements. No material conflicts of interest were noted.

FIDELITY BONDS AND OTHER INSURANCE

The examination of insurance coverages involved a review of the adequacy of limits and retentions, and the solvency of the insurers providing the coverages. The Company is insured for up to \$7,500,000 per occurrence, after a \$100,000 deductible, against losses from acts of dishonesty and fraud by its employees. It was noted that this fidelity bond coverage exceeded the minimum coverage recommended by the NAIC. The Company's office buildings and personal property are covered by a commercial package policy that includes earthquake and flood coverage. The property coverage appeared adequate based on the examination of the office values. All other insurance coverages in force at December 31, 2009, were as follows:

Commercial general liability	Business automobile
Umbrella liability	Managed care errors and omissions
Extortion	Mobile dental van
Workers' compensation	

The limits for the above coverages were found to be adequate as of December 31, 2009.

PENSION PLANS AND OTHER POST RETIREMENT BENEFITS

Employee Retirement Plans

The Company's wholly-owned subsidiary, HSG, offers a 401k pension plan covering substantially all of its employees, to which the Company reimburses HSG under the management agreement. Since the previous examination, the plan provided for HSG to contribute 8% of eligible employees' salaries and would match 2% of employees' contributions. Effective January 1, 2009, the plan was modified to make fixed contributions of 3% of eligible employees' salaries and match employee contributions up to 2%, 4% or 6% of their eligible earnings for years of service less than five years, between five and ten years, and more than ten years, respectively. The voluntary employee pre-tax contributions may range from 1% up to 70% of pay, not to exceed the following dollar amount:

<u>Year</u>	<u>Under Age 50</u>	<u>Age 50 or Over</u>
2007	\$15,500	\$20,500
2008	\$15,500	\$20,500
2009	\$16,500	\$22,000

Deferred Compensation Plans

The HSG deferred compensation plan is available to certain executives where they may defer a portion of their current income to be paid out upon retirement or other qualifying event. Participants in the plans have the position of unsecured creditors.

Also, HSG has adopted an annual bonus plan and a Supplemental Executive Retirement Account Plan (SERAP). The SERAP is a nonqualified defined benefit retirement plan to cover certain officers of HSG who have at least five or more years of service and meet certain other eligibility requirements. Benefits are based on years of service and the employee's final average pay, defined by the plan.

TERRITORY AND PLAN OF OPERATION

The Company is a member of the Delta Dental Plan Association, comprised of 39 independent plans operating in all 50 states, the District of Columbia and Puerto Rico to provide dental coverage to its subscribers. The Company writes business in Oregon, and began writing business in Alaska in 2009.

The Company's dental insurance business is comprised primarily of commercial plans, both in the small- and large-group employer markets. A large portion of the commercial business is written on a retention basis whereby the Company agrees to refund the excess, if any, of premium received over claims and administrative costs paid. The Company's fully insured dental business continues to decline, from 341,367 enrollees at December 31, 2006, to 165,420 enrollees at year-end 2009, with net premium income of \$128,798,007 and \$78,073,428, respectively.

In addition to insurance business, the Company offers two non-insurance dental plans to employer groups. An Administrative Service Contract (ASC) business for self-insured and partially insured groups provides for the collection of group's premiums and the processing of the group's claims, whereby the Company is paid a pre-determined management fee. The employer group retains all claim obligations, thus there is no insurance risk to the Company. A Minimum Premium Plan (MPP) is a product where the Company charges a group a minimum premium per person per month to cover the administrative costs of processing claims. The insured is responsible for the claim payments up to a maximum limit established by the contract. The Company covers claims incurred in excess of the maximum limit. During the examination period, the Company has seen considerable increase in ASC and MPP enrollment. Non-insurance enrollment increased from 320,201 lives in 2006 to 555,429 lives at the end of 2009.

GROWTH OF THE COMPANY

The growth of the Company over the last five years is reflected in the following schedule. The stated amounts were derived from the Company's filed annual statements, except in 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>Total Capital and Surplus</u>	<u>Net Income/ (Loss)</u>
2005	\$138,123,198	\$52,606,326	\$85,516,872	\$ 5,795,788
2006*	133,930,790	45,489,063	88,441,727	4,891,245
2007	136,180,239	46,046,174	90,134,065	3,805,715
2008	114,435,994	50,199,719	64,236,275	(4,676,305)
2009*	113,294,249	30,091,189	83,203,060	(5,855,091)

*Per examination

The significant drop in assets, surplus and net income during 2008 was primarily attributed to: 1) losses from operations (see below); 2) from realized capital losses of \$(1,725,024) and; 3) from unrealized capital losses of \$(20,782,787) related to the investment portfolio. During 2009, the Company divested itself of most of its non-affiliated common stocks.

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) Total Revenues</u>	<u>(2) Total Hospital and Medical</u>	<u>(3) CAE and General Expenses</u>	<u>(2)+(3)/(1) Combined Loss Ratio</u>
2005	\$130,409,866	\$112,781,863	\$14,896,276	97.9%
2006*	128,798,007	110,735,321	16,450,995	98.7%
2007	105,406,184	89,242,859	15,741,300	99.6%
2008	104,417,564	89,115,458	19,086,418	103.6%
2009*	78,073,428	70,679,593	11,351,020	105.1%

*Per examination

A combined loss incurred and expense to premium ratio of more than 100% indicates an underwriting loss, which this Company did report in 2008 and 2009. In addition, approximately 76% of the Company's premiums are in non-insurance Administrative Service Contracts (ASC) and Minimum Premium Plan (MPP) business, whereby the Company acts as a third-party administrator for self-insured and partially insured groups. The premiums and claims from this business are not included above, but the Company does collect a service fee which may offset a portion of the total expenses incurred on the insured business.

REINSURANCE

Assumed Business

Beginning January 1, 2005, the Company began assuming business from Delta Dental Insurance Corporation (DDIC) under a quota share reinsurance agreement. The business pertains to group dental service insurance contracts in the State of Alaska. Under a related Managing General Agency Agreement between the parties, effective the same date, the Company agreed to perform various marketing, underwriting, management and administrative activities and services on behalf of DDIC. All premiums and ASC payments were held, and used to pay claims and related expenses. The Company was paid a fee of 12% of gross written premiums on insured business and 99.5% of fees collected under ASC plans.

In 2008, DDIC agreed to move the business of the groups into the Company as the group policies renewed, so that effective December 1, 2009, all Alaska groups became direct ODS groups. The MGA Agreement was not renewed, and no further reinsurance business is being conducted.

Ceded Business

The Company does not currently cede any reinsurance on contracts in effect because the policy limits on dental insurance do not exceed \$1,500 per enrollee per year, which is a minimal exposure. The Company is in compliance with the provisions of ORS 731.504, which limits the risk on any one subject to 10% of surplus.

ACCOUNTS AND RECORDS

In general, the Company's records and source documentation supported the amounts presented in the Company's December 31, 2009, 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. The Company has a system in place to account for unclaimed funds, and has filed the reports on abandoned property pursuant to the provisions of ORS 98.352.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The Company has taken corrective action with respect to the three recommendations made in the 2006 report of examination. A follow-up report was prepared on September 25, 2009.

SUBSEQUENT EVENTS

There were no items subsequent to the examination date that would have a material impact on the information contained in this report.

FINANCIAL STATEMENTS

The following examination financial statements show the financial conditions of Oregon Dental Service as of December 31, 2009:

Statement of Assets
Statement of Liabilities, Capital and Surplus
Statement of Revenues and Expenses
Reconciliation of Surplus Since the Last Examination

**OREGON DENTAL SERVICE
STATEMENT OF ASSETS
As of December 31, 2009**

	Balance per Company	Exam Adjustment	Balance per Exam	Note
<u>ASSETS</u>				
Bonds	\$ 16,016,271	\$ -	\$ 16,016,271	1
Common stocks	83,957,347	-	83,957,347	1
Properties occupied by company	6,394,557	-	6,394,557	
Cash and short-term investments	(3,885,618)	-	(3,885,618)	1
Other invested assets	1,963,256	-	1,963,256	3
Aggregate write-ins for invested assets	<u>118,200</u>	<u>-</u>	<u>118,200</u>	4
Subtotal, cash and invested assets	<u>\$104,564,013</u>	<u>\$ -</u>	<u>\$104,564,013</u>	
Investment income due and accrued	108,615	-	108,615	
Premiums and considerations: Uncollected premiums and agent's balances in the course of collection	847,131	-	847,131	
Amounts receivable relating to uninsured plans	4,327,793	-	4,327,793	2
Electronic data processing equipment and software	1,434,893	-	1,434,893	
Receivables from parent, subsidiaries, and affiliates	1,589,393	-	1,589,393	
Aggregate write-ins for other than invested assets	<u>422,411</u>	<u>-</u>	<u>422,411</u>	
Total Assets	<u>\$113,294,249</u>	<u>\$ -</u>	<u>\$113,294,249</u>	

OREGON DENTAL SERVICE
STATEMENT OF LIABILITIES, CAPITAL AND SURPLUS
As of December 31, 2009

	Balance per Company	Exam Adjustment	Balance per Exam	Note
LIABILITIES, CAPITAL AND SURPLUS				
Claims unpaid	\$ 2,690,000	\$ -	\$ 2,690,000	2
Accrued medical incentive pool and bonuses	-	-	-	2
Unpaid claims adjustment expense	134,500	-	134,500	2
Aggregate health policy reserves	10,886,461	-	10,886,461	2
Premiums received in advance	1,351,558	-	1,351,558	
General expenses due or accrued	1,323,693	-	1,323,693	
Amounts withheld or retained for account of others	100,634	-	100,634	
Amounts due to parent, subsidiaries, and affiliates	5,033,048	-	5,033,048	
Payable for securities	3,037,032	-	3,037,032	
Liability for amount held under uninsured plans	4,989,260	-	4,989,260	2
Aggregate write-ins for liabilities	<u>545,003</u>	<u>-</u>	<u>545,003</u>	
Total Liabilities	<u>\$ 30,091,189</u>	<u>\$ -</u>	<u>\$ 30,091,189</u>	
Common capital stock	-	-	-	
Gross paid in and contributed surplus	20,747,852	-	20,747,852	
Unassigned funds (surplus)	<u>62,455,208</u>	<u>-</u>	<u>62,455,208</u>	
Total capital and surplus	<u>83,203,060</u>	<u>-</u>	<u>83,203,060</u>	
Total liabilities, capital and surplus	<u>\$ 113,294,249</u>	<u>\$ -</u>	<u>\$ 113,294,249</u>	

OREGON DENTAL SERVICE
STATEMENT OF REVENUE AND EXPENSES
For the Year Ended December 31, 2009

	Balance per Company	Exam Adjustment	Balance per Exam	Note
Net premium income	\$ 78,073,428	\$ -	\$ 78,073,428	
Aggregate write-ins	<u>-</u>	<u>-</u>	<u>-</u>	
Total Revenues	<u>78,073,428</u>	<u>-</u>	<u>78,073,428</u>	
Hospital and Medical:				
Hospital/medical benefits	-	-	-	
Other professional services	69,943,155	-	69,943,155	
Outside referrals	-	-	-	
Emergency room and out-of-area	-	-	-	
Prescription drugs	-	-	-	
Incentive pool, withhold adjustments and bonus amounts	<u>-</u>	<u>-</u>	<u>-</u>	
Subtotal:	69,943,155	-	69,943,155	
Less:				
Net reinsurance recoveries	<u>(736,438)</u>	<u>-</u>	<u>(736,438)</u>	
Total medical and hospital	70,679,593	-	70,679,593	
Non-health claims	-	-	-	
Claim adjustment expenses	4,793,181	-	4,793,181	
General administrative expenses	6,557,839	-	6,557,839	
Increase in reserves for life and accident and health contracts	<u>-</u>	<u>-</u>	<u>-</u>	
Total underwriting deductions	<u>82,030,613</u>	<u>-</u>	<u>82,030,613</u>	
Net underwriting gain or loss	<u>(3,957,185)</u>	<u>-</u>	<u>(3,957,185)</u>	
Net investment income earned	1,355,009	-	1,355,009	
Net realized capital gains or (losses)	<u>(3,092,492)</u>	<u>-</u>	<u>(3,092,492)</u>	
Net investment gains or (losses)	(1,737,483)	-	(1,737,483)	
Aggregate write-ins for other income or expense	<u>(160,423)</u>	<u>-</u>	<u>(160,423)</u>	
Net income or (loss) before federal income taxes	(5,855,091)	-	(5,855,091)	
Federal and foreign income taxes incurred	<u>-</u>	<u>-</u>	<u>-</u>	
Net Income (loss)	<u>\$ (5,855,091)</u>	<u>\$ -</u>	<u>\$ (5,855,091)</u>	

OREGON DENTAL SERVICE
RECONCILIATION OF SURPLUS SINCE THE LAST EXAMINATION
For the Year Ended December 31,

	2009	2008	2007
Capital and surplus, December 31, previous year	<u>\$64,236,275</u>	<u>\$90,134,065</u>	<u>\$88,441,727</u>
Net income	(5,855,091)	(4,676,305)	3,805,715
Change in net unrealized capital gains (losses)	24,334,938	(20,782,787)	(33,220)
Change in net deferred income tax	-	-	-
Change in nonadmitted assets	486,940	(438,698)	(2,080,157)
Change in unauthorized reinsurance	-	-	-
Change in surplus notes	-	-	-
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	-	-	-
Dividends to stockholders (cash)	-	-	-
Examination adjustment	-	-	-
Aggregate write-ins for gains and losses in surplus (1)	<u>(2)</u>	<u>-</u>	<u>-</u>
Change in surplus as regards policyholders for the year	<u>18,966,785</u>	<u>(25,897,790)</u>	<u>1,692,338</u>
Surplus as regards policyholders, December 31, current year	<u>\$83,203,060</u>	<u>\$64,236,275</u>	<u>\$90,134,065</u>
(1) Rounding error.			

NOTES TO THE FINANCIAL STATEMENTS

Note 1 - Investments

Most of the Company's long-term bond investments were in US government obligations, federal agency bonds, special revenue bonds, and corporate issues. The Company did not have a significant exposure to mortgaged-backed and asset-backed securities. All MBS/ABS issues were investment rated at year-end 2009, with a book carrying value of \$3.6 million, comprised over 22% of the total long-term bond portfolio. An additional \$4.9 million was invested in banks and financial institutions, equaling 31% of the bond portfolio.

Common stocks were comprised of investments in one wholly owned subsidiary and in six separate mutual funds, primarily invested in small cap stocks, international equities, and stock index portfolios. The Company's largest stock holding was its subsidiary, HSG, with a reported fair value of \$81,928,341, and was derived using modified GAAP statements under SSAP No. 97, paragraph 8(b)(i). The fair value of all common stocks, including subsidiaries, was \$83,957,347.

Cash and short-term deposits consisted of cash on deposit and investments in US Obligations, First American Prime Obligation funds and a repurchase agreement. Under the Company's cash management system, HSG holds all of the Company's cash, as described earlier in this report.

A comparison of the investments over the past five years is as follows:

<u>Year</u>	<u>A</u> <u>Bonds</u>	<u>B</u> <u>Common</u> <u>and</u> <u>Preferred</u> <u>Stocks</u>	<u>C</u> <u>Cash and</u> <u>Short-term</u>	<u>Ratio</u> <u>A/</u> <u>Total</u> <u>Assets</u>	<u>Ratio</u> <u>B/</u> <u>Total</u> <u>Assets</u>	<u>Ratio</u> <u>C/</u> <u>Total</u> <u>Assets</u>
2005	20,672,490	91,731,727	(526,276)	15.0%	66.4%	(0.4)%
2006*	20,046,031	90,391,341	(6,684,632)	15.0%	67.5%	(5.0)%
2007	20,539,841	90,489,108	(1,455,312)	15.1%	66.4%	(1.1)%
2008	25,216,559	68,942,451	1,256,087	22.0%	60.2%	1.1%
2009*	16,016,271	83,957,347	(3,885,618)	14.1%	74.1%	(3.4)%

Approval of investment transactions was performed by the finance committee of the Board of Directors, pursuant to ORS 733.740. As of December 31, 2009, invested assets of \$4,447,322, representing 4.3% 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 April 1, 2006, the Company entered into a custodial agreement with the US Bank, NA. The agreement contains all of the relevant protections described in OAR 836-027-0200(4)(a) through (l).

Note 2 – Claims Unpaid and Unpaid Claims Adjustment Expense Reserves

David Dillon, FSA, MAAA, of the firm Lewis & Ellis, Inc., reviewed the loss and loss adjustment expenses in the Company's filed financial statements as of December 31, 2009. The purpose of his review was to determine, in general, if the Company's actuarial items were reasonably stated. In his opinion, he concluded:

- 1) ODS's claims unpaid provision appeared inadequate by approximately 15%. Mr. Dillon noted that reserve adequacy has been consistently declining since 2005, and was inadequate in both 2008 and 2009.
- 2) Based on a recent pattern of declining adequacy in the claims unpaid liability provision, ODS should develop margin studies to help assess reserve methodologies.
- 3) Due to a billing practice, ODS did not establish unearned premium reserves. Mr. Dillon believes the impact was financially immaterial for 2009. However, the reserve provision should be established for future time periods.
- 4) Oregon Dental Services' terminal liability was backed out of amounts receivable and added as a paid claim.

To explain the last item, under partially insured plans, the Company will receive and pay claims from providers and then collect premiums and administrative income. The Company received premiums on certain contracts that were less than the claims paid to providers. Therefore, the Company recorded a recoverable for the deficit. If the contract is terminated prior to collection of this receivable, this would result in an accumulated deficit that the Company labeled a "terminal liability." At December 31, 2009, this terminal liability amounted to \$3.7 million. To comply with statutory accounting requirements of SSAP No. 47, paragraph 4, this terminal liability was backed out of receivables because the associated claims had already been paid. These claims were included as 2009 incurred claims and included in Line 1.1 of Part 2 of the Underwriting & Investment Exhibit.

The comparison of Mr. Dillon's findings to the 2009 Annual Statement is as follows:

	<u>Actuarial Report</u>	<u>Annual Statement</u>
Claims Unpaid	\$ 3,163,242	\$ 2,690,000
Accrued Medical Incentive Pool and Withhold Amounts	0	0
Unpaid Claim Adjustment Expense	134,500	134,500
Aggregate Health Policy Reserves	10,886,461	10,886,461
Unearned Premium Reserve	0	0
Premiums received in advance	1,351,558	1,351,558
Liability for amounts held under uninsured plans	4,989,260	4,989,260
Other Actuarial Liabilities	361,793	361,793
Amounts receivable relating to uninsured plans	4,327,793	4,327,793

As a result of Mr. Dillon's report, the unpaid claims reserve was found to be deficient by \$473,242. Due to the immaterial impact on surplus, the examiners will not propose an adjustment, however, **I recommend the Company develop formal margin studies to assess the reserve methodologies that meet moderately adverse conditions in its claims unpaid reserve.**

Note 3 – Other Invested Assets (Schedule BA)

The Company reported an investment in Aurora Offshore Fund Ltd II, domiciled in the Cayman Islands, which is a hedge fund managed by Harris Associates. Because hedge funds are not addressed in the Oregon Insurance Code, and likewise are not expressly prohibited, the Company was directed to limit its investment to no more than 7.5% of total admitted assets pursuant to the "prudent investor" standards of ORS 733.670(2). When we compared the total investment of \$2,268,538 to the total admitted assets as of the most recently filed statement (September 30, 2009), the hedge fund represented 1.9% of assets, and the Company was in compliance. At December 31, 2009, the book value of the investment represented 1.7% of total admitted assets.

Note 4 – Aggregate Write-in for Invested Assets

In 2001, the Company became a member of the Federal Home Loan Bank ("FHLB") upon the purchase of shares of capital stock in the FHLB of Seattle. This investment allows the Company to borrow on a line of credit to make residential mortgages. The Company borrowed no money under this arrangement during the period under examination.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

There was one comment or recommendation made as a result of this examination, as follows:

Page

- 25 I recommend the Company develop formal margin studies to assess the reserve methodologies that meet moderately adverse conditions in its claims unpaid reserve.

CONCLUSION

During the four-year period covered by this examination, the surplus of the Company has decreased from \$88,441,727, as presented in the December 31, 2006, report of examination to \$83,203,060, as shown in this report of examination. The comparative assets and liabilities are shown below:

	<u>2009</u>	December 31,	<u>2006</u>	<u>Change</u>
Assets	\$113,294,249		\$133,930,790	\$(20,636,541)
Liabilities	<u>30,091,189</u>		<u>45,489,063</u>	<u>(15,397,874)</u>
Surplus	<u>\$ 83,203,060</u>		<u>\$ 88,441,727</u>	<u>\$ (5,238,667)</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 Giffin, CFE, and Michael P. Phillips, CPA, CFE, AES, insurance examiners for the State of Oregon, Department of Consumer and Business Services, Insurance Division, participated in the examination.

Respectfully submitted,

Greg A. Lathrop, CFE
Supervising Financial 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 Oregon Dental Service.

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 Oregon Dental Service 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: _____