

STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**PHYSICIANS ASSOCIATION OF CLACKAMAS COUNTY  
HEALTH PLANS, INC.  
CLACKAMAS, OREGON**

**NAIC COMPANY CODE 47260**

AS OF

DECEMBER 31, 1994

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September 28, 1995

Honorable Kerry Barnett  
Director of Consumer and Business Services  
State of Oregon  
350 Winter Street NE, Room 440-4  
Salem, Oregon 97310

Dear Director:

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

**PACC Health Plans, Inc.  
12901 SE 97th Avenue  
Clackamas, Oregon 97015**

**NAIC Company Code 47260**

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

## **SCOPE OF EXAMINATION**

The examination of the Plan was conducted as of December 31, 1994, 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 procedures and guidelines prescribed by the National Association of Insurance Commissioners (NAIC) for the purpose of determining the Plan's financial condition, ability to fulfill and the manner of fulfillment of 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 Plan. A review was also made of the corrective actions taken by the Plan with respect to comments and/or recommendations in the previous financial report of examination as of December 31, 1991.

In addition to the above, the examiner reviewed work papers prepared by the Plan's CPA auditors in their examination of the Plan's accounts for the year ended December 31, 1994. A portion of the CPA's work papers have been incorporated into the work papers of the examiner, and have been utilized in determining the scope and areas of emphasis in conducting the examination.

In addition to those items specifically commented upon in this report, other phases of the Plan's operations were reviewed, including the following areas that require no further comment:

Officer, employee, and agent welfare and pension plans

## **PLAN HISTORY**

The Plan was incorporated under the laws of the State of Oregon on September 6, 1977, as a nonprofit organization under the name Clackamas Health Services, Inc. The Plan received its Certificate of Authority on July 1, 1983, and was authorized to transact business as a healthcare service contractor. Additionally, the Plan became licensed as a healthcare service contractor in the State of Washington on September 23, 1991. Effective October 1, 1990, the Plan changed its name to PACC Health Plans, Inc.

## **GROWTH OF THE PLAN**

The growth of the Plan is reflected in the following schedule. The statistics were derived from Plan filed annual statements except in those years where a triennial report of examination has been filed with the Oregon Insurance Division.

<b><u>Year</u></b>	<b><u>Admitted Assets</u></b>	<b><u>Liabilities</u></b>	<b><u>Reserves</u></b>	<b><u>Net Income</u></b>
1991*	\$14,173,255	\$ 7,840,902	\$ 6,332,353	\$ 1,496,723
1992	17,417,846	8,166,705	9,251,141	2,688,457
1993	26,184,509	9,318,983	16,865,526	6,491,740
1994*	33,395,843	11,127,435	22,268,408	5,697,609

\*Per examination

## **LOSS EXPERIENCE**

The following exhibit reflects the annual underwriting results of the Plan since the last examination. The amounts were compiled from copies of the Plan's filed annual statements.

<b><u>Year</u></b>	<b><u>Premiums Earned</u></b>	<b><u>Claims and Claims Expenses</u></b>	<b><u>Ratio</u></b>
1991*	\$43,882,686	\$37,774,092	86.1%
1992	51,124,154	42,649,580	83.4%
1993	53,999,626	41,011,795	75.9%
1994*	61,372,831	47,910,671	78.1%

\*Per examination

## **MANAGEMENT AND CONTROL**

### **Board of Directors**

The Bylaws vest management and control of the Plan in a Board of Directors consisting of 15 members, eight of whom shall be physicians and seven of whom shall be nonphysicians. At least five of the directors shall be representatives of the public. Directors serve terms of four years and may serve for a maximum of three terms. A majority of the number of directors constitutes a quorum. The Board of Directors meet all requirements of ORS 750.015.

Members of the Board of Directors, duly elected and serving as of December 31, 1994 were:

<b><u>Director/Address</u></b>	<b><u>Business Affiliation</u></b>	<b><u>Director Since</u></b>
Curtis L. Bender* 4800 Mill St. West Linn, OR 97068	Simpson Paper Company Area supervisor	1993
James T. Brouillette* 19600 S. Molalla Oregon City, OR 97045	Clackamas Community College - Director Public Service	1984
David A. Durfee, MD 10818 SE Oak St. Milwaukie, OR 97222	Ophthalmologist	1986
George I. Hansen, JD* 11515 SW Pacific Hwy. Portland, OR 97223	Attorney At Law	1989
Daniel B. Herr, MD 1105 NE 78th Avenue Portland, OR 97213	Anesthesiologist	1992
Jonathan H. Hoppert, MD 19250 SW 65th, Ste. 100 Tualatin, OR 97062	Orthopedist	1987
Daniel L. Hughson, MD 1185 South Elm Canby, OR 97013	Internal Medicine	1990
Kenneth Lien* 3710 NW 166th Dr. Beaverton, OR 97006	Retired	1989
Richard M. Page* 6727 SW 13th Avenue Portland, OR 97219	Retired	1994

David A. Pass, MD 1105 NE 78th Avenue Portland, OR 97213	Anesthesiologist	1991
Robert A. Perry, MD 1500 Division St. Oregon City, OR 97045	Radiologist	1989
Beverly E. Phillipson, MD 5050 NE Hoyt St., Ste. 354 Portland, OR 97213	Endocrinologist	1994
Lyle A. Reese* 10898 SW 111th Tigard, OR 97223	Clackamas Community College - Retired Dean of Instruction	1994
Donald E. Reger* 6936 SW 11th Drive Portland, OR 97219	Insurance Agent - Retired	1992
C. Edward Skeeters, MD 6464 SW Borland Rd. #A-1 Tualatin, OR 97062	Urologist	1985

\*Represents public director position as required by ORS 750.015.

### **Officers**

Operating management of the Plan as of December 31, 1994, was under the direction of the following principal officers:

<b><u>Name</u></b>	<b><u>Office</u></b>
Martin A Preizler	President and Chief Executive Officer
David Pass, MD	Secretary
H. M. Dolan	Senior Vice President and Chief Administrative Officer
Theodore C. Falk	Vice President and General Counsel
Julie A. Ferguson	Vice President - Health Systems and Quality
Jerry J. Jarosz	Vice President - Information Systems and Technology
Frank W. Kleinheinz	Vice President - Sales
Kevin L. McCartin	Vice President - Sales, Product, and Pricing
Ron D. Morgan	Vice President - Corporate Development and Community Affairs
Lori L. Mueller	Vice President and Chief Financial Officer
Louise J. Walczak	Vice President - Human Resources
Sharon Bryant	Director of Claims

In view of the Plan's favorable unassigned funds, reliable state of records, and substantial compliance with the Oregon Insurance Code, it appears that overall, the Board of Directors and officers possess the insurance experience to manage the affairs of the Plan as required for the Plan to hold a certificate of authority under the provisions of ORS 731.386.

**Affiliate**

Physicians Association of Clackamas County (PACC) - PACC was incorporated as a nonprofit corporation, on March 4, 1954. PACC operates as a Federally qualified Health Maintenance Organization and is licensed in Oregon and Washington.

The Plan, as an insurance holding company system, has made timely annual holding company registration filings in accordance with ORS 732.551 and OAR 836-27-020(1). PACC's control of the Plan derives from the fact that the Board of Trustees of PACC elect the Plan's Board of Directors.

**Management Agreements**

The Plan's affiliate, PACC, makes all disbursements for claims and administrative expenses for the Plan under the terms of an administrative services agreement entered into on August 16, 1989. Under the terms of agreement, PACC provides the necessary administrative services required to fulfill PACCHP's contractual obligations. In consideration for these services, PACC receives a variable fee that is based on individual lines of business member months and service units.

As of December 31, 1994, the Plan did not have any management or exclusive agency contracts in effect that were contrary to the provisions of ORS 732.215 and ORS 732.220, respectively.

**MANAGEMENT AFFIRMATION**

## **CONFLICT OF INTEREST**

It was noted in the corporate minutes, for the period under examination, the board addresses conflict of interest issues. However, during 1994, the Plan did not require officers and directors to disclose conflict of interest on a signed conflict of interest statement.

I recommend that all persons that hold director and officer positions with the Plan, annually sign a conflict of interest statement in order to make known any conflicts that would affect the fulfillment of their fiduciary responsibilities to the Plan. This recommendation is supported by the NAIC Examiners Handbook, page 2J-8 and ORS 733.210.

### **Subsequent Event**

It was noted the Plan is in the process of adopting a conflict of interest policy called "Conflict of Interest Standards and Procedures." In addition, based on a discussion with the Plan's general counsel, the Plan will institute conflict of interest statements that will be signed annually by the Board and other key employees.

## **INSURANCE**

The examination of insurance coverages involved a review of adequacy of limits and retentions, and the solvency of the insurers providing the coverages.

The Plan has a directors and officers policy that indemnifies directors and officers for aggregate losses up to \$10,000,000 and a financial institutions bond insuring loss from employee dishonesty for up to \$1,000,000. The fidelity bond coverage met the minimum limits required by the NAIC.

Other types of coverages provided the Plan include:

Workers' compensation  
Professional liability  
General liability  
Casualty

Fire  
Fiduciary liability  
Automobile liability

The Plan's insurance coverages were determined to be adequate as of December 31, 1994.

## **CORPORATE RECORDS**

### **Board Minutes**

The Plan Bylaws state the Board of Directors shall meet at least annually and from time to time as designated by the Board. The minutes of the Plan are recorded in sufficient detail to determine the actions taken by the Board. A quorum was achieved at all board meetings held during the period under examination.

The Board of Directors approves investments in accordance with the requirements of ORS 733.730 and records of investments were maintained in accordance with the provisions of ORS 733.740.

### **Articles of Incorporation**

The Articles of Incorporation were amended at a meeting of the Board of Directors on March 15, 1993. The amended article now reads as follows:

Article IV, Designation. The Corporation is a mutual benefit corporation as defined in the Oregon Nonprofit Corporation Act.

### **Bylaws**

At a meeting of the Board of Directors on November 22, 1994, the following articles and sections of the Bylaws were amended to read:

2.2 Number. The Board of Directors shall consist of 15 Directors, eight of whom shall be physicians and seven of whom shall be nonphysicians. No fewer than five of the seven nonphysicians shall be representatives of the public who are not practicing health care providers or employees or directors of a participant hospital ("Public Representative"). No reduction of the number of Directors shall give the effect of removing any Director prior to the expiration of his or her term of office. In addition, the President and Chief Executive Officer shall be an ex officio, nonvoting member of the Board of Directors and shall be entitled to notice of, and to attend, all meetings of the Board of Directors with the exception of that portion of any meeting where the board is to evaluate the performance of or set the salary for the President and Chief Executive Officer.

2.4 Appointment of Directors. The Directors shall be appointed by the Board of Trustees of PACC, an Oregon nonprofit corporation, following the election of new PACC Trustees.

2.10 Quorum, Procedures and Vote (b) The Board shall from time to time adopt procedures for the efficient and effective conduct of its meetings. The Board shall adopt conflict of interest policies for Directors in compliance with legal requirements. The board shall from time to time adopt pricing policies and compensation procedures in compliance with prevailing law. No physician Director shall act upon decisions regarding the size, composition or method of compensating the Corporation's provider panel.

(c) The action of a majority of the Directors present at any meeting shall be the act of the Board of Directors if there is a quorum present at the time of the action, unless a greater number is required by law, the Articles of Incorporation or these Bylaws.

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

The Plan arranges for the provision of comprehensive healthcare services to its subscribers through contracts with hospitals and physicians. The physicians are compensated predominantly through a Plan approved schedule of "usual, customary and reasonable fees" that is incorporated into the individual participating provider agreement. In addition, the Plan covers services provided by a nonparticipating provider based on usual and customary fees. Amounts above this are billed to the subscriber.

Hospitals that contract with the Plan, provide inpatient, outpatient, and in area emergency, and various other services to subscribers for a negotiated fee.

The Plan's service area includes Oregon and Washington.

## **REINSURANCE**

The Plan entered into an excess of loss reinsurance contract (the same contract covers its affiliate - PACC) on January 1, 1994, that indemnifies the Plan against eligible hospital expenses with the following coverages and limits:

### **Coverage**

Eligible hospital expenses and out of area emergency services provided by per diem hospital approved by the reinsurer.

### **Limits**

90% of \$900,000/per member in excess of \$100,000/per member

Eligible hospital expenses and out of area emergency services provided by non per diem hospital.

80% of \$900,000/per member in excess of \$100,000/per member.

The contract limits eligible hospital services to a maximum average of \$3,000 per day over the entire length of stay or stays in the hospital.

### **Insolvency Clause**

The insolvency clause of the reinsurance agreement did not specify that payments will be made to a statutory successor without diminution in the event of an insolvency. In addition, there was an endorsement (Endorsement F) that reduced the amount the reinsurer will pay in the event of the Plan's insolvency by limiting hospital stays to 365 days. Due to the ability of the reinsurer to diminish payments in the event of the Plan's insolvency, the Plan was not permitted to take reinsurance credits under this agreement as specified by ORS 731.508(3). No adjustment was made to the annual statement balance of reinsurance recoverables of \$24,778, at December 31, 1994, due to the immaterial nature of this amount.

The Plan does not retain risk on any one subject in excess of ten percent (10%) of its surplus to policyholders as required by ORS 731.504.

### **Subsequent Event**

During the course of the examination, The Plan amended the insolvency clause and Endorsement F to eliminate the possibility of payment with diminution in the event of insolvency. As a result, no further comment or recommendation is deemed necessary.

## **CONTINGENCY RESERVE AND CAPITAL STABILIZATION FUND**

### **Contingency Reserves**

The Plan participates in a contingency reserve, established in 1963 by its affiliate, for the purpose of protecting the Plan against the effects of catastrophes and seasonal fluctuations in business. The reserve was funded by mandatory withholds from physician's compensation. Withdrawals from the reserve may be made by physicians upon the Board of Directors approval and the following:

1. Physician retires at age of 65.
2. Physician retires at age 55 after at least ten years of service with the Plan.
3. Physician ceases practice in Clackamas County.
4. Death of Physician
5. Physician terminates practice due to permanent disability.
6. Dissolution of the Plan.

The description of the contingency reserve states no benefits can be paid, during any year, which exceeds 5% of the contingency reserves at the beginning of the year or which reduces said reserves to less than \$50,000. Should the Plan dissolve, all Plan liabilities and obligations must be satisfied prior to any distribution to the providers under this arrangement.

### **Capital Stabilization Fund**

On June 30, 1988, the Plan stopped contributions to the contingency reserves and established a capital stabilization fund with the same purpose and funding arrangement except the withhold requirement was expanded to include all member physicians and reserve amounts are allocated to separate provider accounts. At the end of every fiscal accounting year, the Plan calculates a contribution cap for each provider. At the beginning of each fiscal accounting year, amounts in excess of the applicable contribution caps for the preceding year may be refunded to the providers. This distribution is subject to the approval of the Trustees.

Like the contingency reserve, provider payments are subordinate to all other Plan liabilities and obligations. The Plan's accounting system segregates the assets of the contingency reserve and the stabilization fund from the Plan's general assets. As of December 31, 1994, the market value of cash and invested assets for the contingency reserve and stabilization fund was \$625,309 and \$2,081,865, respectively.

In 1994, the Board of Directors made a decision to liquidate the contingency reserve and stabilization fund subject to the financial condition of the corporation and with the Board's annual approval of the total withdrawals for each year.

During the examination, it was noted the Plan does not maintain documentation whereby physicians agree to accept amounts withheld from compensation for the purpose of funding contingency reserves and stabilization funds. In the absence of signed physician statements acknowledging the acceptance of the stipulated withholds, the contingency reserve and stabilization fund appear to be a liability. Further, it was determined the contingency reserve and stabilization fund did not meet the Oregon Insurance Division's criteria for reporting these balances as surplus. The Division's

position is based on the NAIC Accounting Practices and Procedures for HMOs, page 9-1, which sets forth provisions on reporting subordinated indebtedness as net worth as follows:

This item represents a surplus account derived from the subordination of HMO debts to owners, medical providers, or other creditors. Statutes generally allow this account as a surplus item because it has been subordinated to all other liabilities and cannot be repaid without the consent of the regulatory agency.

Although the contingency reserve and stabilization fund are subordinate to other Plan liabilities and obligations, they do not require the Plan to seek regulatory approval for distribution of principal or interest. As a result, I recommend the Plan submit the contingency reserve and stabilization fund to the Oregon Insurance Division for regulatory approval to reflect these amounts as equity rather than as a liability and develop a supplement to the provider agreement that requires the member provider to sign an agreement showing acceptance of a subordinate position in the withheld compensation. This recommendation is supported by the NAIC Accounting Practices and Procedures Manual for HMOs, page 9-1 and ORS 733.210(2).

Until the Plan complies with the preceding recommendation, a reclassification of the entire combined contingency reserve and stabilization fund balances in the book value amount of \$2,529,123 has been made from aggregate write-ins for reserves to aggregate write-ins for other liabilities pursuant to the provisions of ORS 733.030(5). The resultant reclassification reduces reserves and unassigned funds to \$18,911,029.

### **Subsequent Event**

Please see the subsequent event section at the end of this report.

## **ACCOUNTS AND RECORDS**

In general, the Plan's records and source documentation supported the amounts presented in the Plan's December 31, 1994, annual statement and were maintained in a manner by which the financial condition was readily verifiable as required by ORS 733.170. However, attention is directed to the following issues as a result of this examination.

### **Claims Unpaid**

The Oregon Insurance Division's consulting actuary determined the Plan's reserves to be understated by an estimated \$724,000 for the period examined, and noted the following:

In general, the company's reserves and liabilities appear to be calculated accurately and consistently, but with very little margin. The run-off claims experienced during the first quarter of 1995 were higher than expected, but not higher than would have been covered by a 15% margin over best estimate claim reserves. The above adjustment [\$724,000] increases unpaid claims at 12/94 by 12%, to an amount sufficient to cover actual three month run-off plus residual reserve estimates.

In view of these comments, I recommend the Plan set future claims unpaid reserves at a level which includes a margin over a best estimate number. The DCBS consulting actuary's adjustment was not made due to its immaterial effect relative to the Plan's December 31, 1994, reserves and unassigned funds.

### **Custodial Agreement**

The Plan maintains its statutory deposit at U.S. Bank as required by the Oregon Insurance Division. It was noted the Plan did not have a safekeeping agreement with U.S. Bank. In regards to custodial accounts, the NAIC suggest insurers maintain a safekeeping agreement with the following minimum language:

In the event that there is a loss of securities for which the bank is obligated to indemnify the Company, the securities shall be promptly replaced or the value of the securities and the value of any loss of rights resulting from such a loss shall be promptly replaced.

I recommend the Plan enter into an agreement with U.S. Bank and that such agreement contain the clauses described above. This recommendation is facilitated by the NAIC Examiners Handbook, page 2G-8 and ORS 731.302.

**Miscellaneous Accounts Receivable**

The Plan reported unsecured receivables over 90 days as admitted assets. The NAIC Accounting Practices and Procedures Manual, page 9-1, considers receivables, where collectability is uncertain, to be nonadmitted assets. I recommend the Plan consider unsecured receivables to be nonadmitted assets and exclude such amounts from the balance reported on the annual statement. This recommendation is supported by ORS 733.210 and ORS 733.010(8).

**Disaster Recovery Plan**

Although the Plan has a written disaster recovery program, it was determined the Plan did not provide for an alternative computer facility in the event of disaster. I recommend the Plan make formal arrangements for the use of an alternative computer facility in the event of a disaster in accordance with the NAIC Examiners Handbook, page I-54 and pursuant to the provisions of ORS 731.302.

As of December 31, 1994, all disbursements in excess of \$100 were supported by signed vouchers or related documents as required by ORS 732.320.

The Plan is in compliance with the required capitalization provisions of ORS 750.045.

The Plan reports unclaimed property to the State in accordance with the ORS 98.302 to 98.436.

**COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS**

The Plan has complied with all recommendations made in the 1991 report with the following exception:

"We recommend the Company require all key employees and officers to sign conflict of interest statements annually." (1991)

As discussed above, the Plan did not require directors and key employees to sign annual conflict of interest statements.

**PACC HEALTH PLANS, INC.**  
**STATEMENT OF ASSETS, LIABILITIES, RESERVES & OTHER FUNDS**  
**AS OF DECEMBER 31, 1994**

<b><u>ASSETS</u></b>	<b><u>Ledger</u></b> <b><u>Assets</u></b>	<b><u>Nonadmitted</u></b> <b><u>Assets</u></b>	<b><u>Net Admitted</u></b> <b><u>Assets</u></b>
Bonds (Note 2)	\$21,240,714		\$21,240,714
Common Stocks	929,603		929,603
Mortgage Loans	1,700,931		1,700,931
Cash on Hand and Deposit (Note 4)	1,771,913		1,771,913
Short-term Investments (Note 3)	6,289,379		6,289,379
Uncollected Premiums	587,038		587,038
Reinsurance Recoverable	24,778		24,778
Interest and Investment Income Due and Accrued	365,432		365,432
EDP Equipment	306,298		306,298
Furniture and Equipment	834,289	834,289	0
Aggregate Write-ins Other Than Investments	<u>573,002</u>	<u>393,245</u>	<u>179,757</u>
Total Assets	<u>\$34,623,377</u>	<u>\$ 1,227,534</u>	<u>\$33,395,843</u>

**LIABILITIES, RESERVES & OTHER FUNDS**

Claims Unpaid	\$ 6,068,523
Unpaid Claims Adjustment Expenses	235,109
Unearned Premiums	1,937,596
Other Expenses Due or Accrued	201,535
Aggregate Write-ins for Other Liabilities	<u>2,684,672</u>
Total Liabilities	<u>11,127,435</u>
Statutory Reserves	500,000
Aggregate Write-ins for Reserves	2,783,047
Unassigned Funds	<u>18,985,361</u>
Total Reserves and Unassigned Funds	<u>22,268,408</u>
Total Liabilities, Reserves & Unassigned Funds	<u>\$33,395,843</u>

**PACC HEALTH PLANS, INC.  
 UNDERWRITING AND INVESTMENT EXHIBIT  
 FOR THE YEAR ENDED DECEMBER 31, 1994**

**UNDERWRITING INCOME**

Premiums Earned	\$61,372,831
<u>Deductions</u>	
Claims Incurred	45,912,803
Claims Adjustment Expenses Incurred	1,997,868
Administrative Expenses Incurred	4,957,273
Soliciting Expenses Incurred	4,067,819
Reinsurance Allowances - Expense and Experience Refund	<u>438,940</u>
Total Underwriting Deductions	<u>57,374,703</u>
Net Underwriting Gain	3,998,128

**INVESTMENT INCOME**

Net Investment Income Earned	1,646,470
Net Realized Capital Gains	<u>54,330</u>
Net Investment Gain	1,700,800
Aggregate Write-ins for Other Income	(1,319)
Federal Income Taxes	<u>0</u>
Net Gain	<u>\$ 5,697,609</u>

**RESERVES AND UNASSIGNED FUNDS  
 AS OF DECEMBER 31, 1994**

Reserves and Unassigned Funds December 31, 1993:	\$16,865,526
Net Gain	5,697,609
Net Unrealized Capital Gains	(1,344,901)
Change in Nonadmitted Assets	1,318,759
Aggregate Write-ins for changes to reserves	<u>(268,585)</u>
Change in Reserves for 1994	<u>5,402,882</u>
Reserves and Unassigned Funds December 31, 1994	<u>\$22,268,408</u>





Per annual statement	\$1,607,137
Per examination	<u>6,289,379</u>
Difference	<u>(\$4,682,242)</u>

The difference represents a reclassification of commercial paper from cash to short-term investments. This reclassification conforms with the HMDI annual statement instructions which classify short-term investments as those which had maturities of one year or less at the time of acquisition. There is no effect on unassigned funds as a result of this reclassification.

**Note 4 - Cash**

Per annual statement	\$6,454,155
Per examination	<u>1,771,913</u>
Difference	<u>\$4,682,242</u>

The difference represents a reclassification of commercial paper from cash to short-term investments. See Note 3.

**SUMMARY OF COMMENTS AND RECOMMENDATIONS**

Page

- 10 I recommend that all persons that hold director and officer positions with the Plan annually sign a conflict of interest statement in order to make known any conflicts that would affect the fulfillment of their fiduciary responsibilities to the Plan. This recommendation is supported by the NAIC Examiners Handbook, page 2J-8, and ORS 733.302.
- 16 I recommend the Plan submit the contingency reserve and stabilization fund to the Oregon Insurance Division for regulatory approval to reflect these amounts as equity rather than as a liability and develop a supplement to the provider agreement that requires the member provider to sign an agreement showing acceptance of a subordinate position in the withheld compensation. (Please see the subsequent event section of this report.)
- 17 I recommend the Plan set future claims unpaid reserves at a level which includes a margin over a best estimate number.
- 18 I recommend the Plan enter into a safekeeping agreement with U.S. Bank. The agreement should contain an indemnification clause regarding the replacement of securities in the event of custodian negligence. This recommendation is facilitated by the NAIC Examiners Handbook, page 2G-8, and ORS 731.302.

Page

- 18 I recommend the Plan consider unsecured receivables to be nonadmitted assets and exclude such amounts from the balance reported on the annual statement. This recommendation is supported by ORS 733.210 and ORS 733.010(8).
- 18 I recommend the Plan make formal arrangements for the use of an alternative computer facility in the event of a disaster in accordance with the NAIC Examiners Handbook, page I-54 and pursuant to the provisions of ORS 731.302.

**CONCLUSION**

During the three year period covered by this examination, the reserves and unassigned funds of the Plan has increased from \$6,332,353 as presented in the December 31, 1991, report of examination, to \$22,268,408 as shown in this report of examination.

The comparative assets and liabilities are shown below:

	<b>December 31,</b>		
	<b><u>1994</u></b>	<b><u>1991</u></b>	<b><u>Change</u></b>
Assets	\$33,395,843	\$14,173,255	\$19,222,588
Liabilities	<u>11,127,435</u>	<u>7,840,902</u>	<u>\$ 3,286,533</u>
Reserves & Unassigned Funds	<u>\$22,268,408</u>	<u>\$ 6,332,353</u>	<u>\$15,936,055</u>

### **SUBSEQUENT EVENT**

Subsequent to the date of this examination, on April 9, 1997, the Plan together with its affiliate PACC, entered into an Agreement and Plan of Reorganization (Agreement) with Qual-Med Oregon Health Plan, Inc. (Qual-Med). The Agreement was approved by DCBS on October 20, 1997, the transaction described in the Agreement closed on October 22, 1997.

The purpose of the Agreement was to merge the operations of the Plan and PACC into the operations of Qual-Med. The facts of this merger are contained in the "Proposed Plan of Acquisition of Control and Merger Case No. INS 97-10-007" on file with DCBS.

In accordance with the Agreement and DCBS's Order approving the Agreement, the participating physicians were paid their respective interests in the Contingency Reserves and Capital Stabilization Fund (CRCSF), either directly or through transfer of the CRCSF to Clackamas County Medical Society as successor sponsor. As a result of the merger the subsequent payment of the Plan's CRCSF obligations, the examination recommendation and proposed adjustment of \$2,529,123 are not considered necessary for purposes of this examination.

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

In addition to the undersigned, Timothy R. Hurley, CFE, Michael P. Phillips, CFE, CPA, and Janice A. Leith, insurance examiners for the State of Oregon, Department of Consumer and Business Services, Insurance Division, and Catherine R. Turner, FSA, MAAA, consulting actuary, participated in the examination.

Respectfully submitted,

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D. Patrick Huth, CFE  
Supervising Insurance Examiner  
Insurance Division  
Department of Consumer and Business Services  
State of Oregon

**AFFIDAVIT**

STATE OF OREGON            )  
  )  ss  
County of Marion            )

D. Patrick Huth, CFE, being duly sworn, deposes and says the preceding report of financial examination as of December 31, 1994, of PACC Health Plans, Inc., Clackamas, Oregon, subscribed by him is true and correct to the best of his knowledge and belief.

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D. Patrick Huth, CFE  
Supervising Insurance Examiner  
Insurance Division  
Department of Consumer and Business Services  
State of Oregon

Subscribed and sworn to before me this \_\_\_\_\_ day of \_\_\_\_\_, 1998.

\_\_\_\_\_  
NOTARY PUBLIC for the State of Oregon  
My Commission Expires:\_\_\_\_\_