



STATE OF OREGON

DEPARTMENT OF CONSUMER AND BUSINESS SERVICES

INSURANCE DIVISION

REPORT OF FINANCIAL EXAMINATION

OF

**PACIFICARE OF OREGON, INC.
LAKE OSWEGO, OREGON**

NAIC COMPANY CODE 95893

AS OF

December 31, 2006

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May 18, 2007

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, Room 440
Salem, Oregon 97301-3883

Dear Director:

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

PACIFICARE OF OREGON, INC.
Five Centerpointe Drive, Suite 600
Lake Oswego, Oregon 97035

NAIC Company Code 95893

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

SCOPE OF EXAMINATION

This regularly scheduled examination of the Plan was conducted as of December 31, 2006, covering the four-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 the provisions of ORS 731.300 and in accordance with procedures and guidelines prescribed by the National Association of Insurance Commissioners (NAIC) for the purpose of determining the Plan's financial condition, ability to fulfill 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. The record testing included, but was not limited to, assets, liabilities, income and expense related items. A review was also made of the corrective actions taken by the Plan with respect to comments and/or recommendations in the previous report of examination as of December 31, 2002.

Scott Fitzpatrick, FSA, MAAA, and David Ball, FSA, MAAA, actuaries for the State of Oregon, Department of Consumer and Business Services, Insurance Division, participated in this examination by evaluating unpaid claims and unpaid claims adjustment expenses. The results of their analyses are found under the relevant section of this report.

COMPANY HISTORY

The Plan was incorporated under the laws of the State of Oregon on August 28, 1985, as a for-profit organization under the name of PacifiCare of Oregon II. The Plan received its Certificate of Authority on January 30, 1987, and was authorized to transact the business of accepting prepayment of health care services under the provisions of ORS 750.055 and ORS 731.354. Effective February 4, 1987, the Plan purchased the assets of PacifiCare of Oregon, a non-profit health maintenance organization incorporated in Oregon on June 1, 1984. Concurrently, the nonprofit company was dissolved and the Plan commenced business under its current name, PacifiCare of Oregon, Inc.

The Plan became a federally qualified health maintenance organization on March 26, 1987.

Effective December 20, 2005, the Plan was acquired as part of the acquisition of PacifiCare Health Systems, Inc., by UnitedHealth Group, Inc.

MANAGEMENT AND CONTROL

Board of Directors

Amended and Restated Bylaws as of March 16, 2006, vest management and control of the Plan in a Board of Directors. Article 3.2 of the Bylaws states the number of directors of the corporation shall be four. The number of directors may be increased from time to time by amendment to these Bylaws, but such number shall never be less than three. The directors serving at December 31, 2006, were as follows:

<u>Name and Address</u>	<u>Affiliation</u>	<u>Director Since</u>
Robert J. Sheehy 5901 Lincoln Drive Edina, MN 55436	Chief Executive Officer United HealthCare, Inc.	March, 2006
Steven A. Schmidt Five Centerpointe Drive Lake Oswego, OR 97035	CEO, Northwest Region PacifiCare of Oregon, Inc.	March, 2006
James A. Frey, II * 5995 Plaza Drive Cypress, CA 90630	Senior Vice President Western Markets PacifiCare Health Systems, LLC	March, 2006
Susan A. Brickey 5029 S.E. Reedway Portland, OR 97206	Health Care Consultant Brickey Enterprises, LLC	February, 2007

*Chairman of the Board

Mr. Schmidt was removed from the Board in February 2007. His replacement had not been elected to the Board as of the date of completion of the fieldwork.

The Board of Directors did not meet the requirements of ORS 750.015, as only one of the four directors meets the definition of representative of the public. **I recommend the Plan replace a current director with an individual that would qualify as a representative of the public, or consider amending its Bylaws to add an additional board member that would qualify as a representative of the public in compliance with ORS 750.015 and the Plan's Bylaws.**

Officers

Principal officers elected and serving the Plan at December 31, 2006, were as follows:

<u>Name</u>	<u>Office</u>
Steven A. Schmidt	President and CEO
Susan L. Berkel	Vice President and CFO
Forrest G. Burke	Secretary
Robert W. Oberrender	Treasurer
Juanita V. Bolland Luis	Assistant Secretary
Donald A. Powers	VP – Finance and Assistant Treasurer

Mr. Schmidt was replaced by David Hansen in February 2007.

Parent, Subsidiary and Affiliated Companies

The Plan is a member of an insurance company holding system, which includes a number of affiliated entities, 67 of which are insurance companies. The ultimate parent is UnitedHealth Group, Inc. (NYSE: UNH), a Minnesota corporation located in Minnetonka, Minnesota. UNH provides individuals with access to health care services and resources through more than 500,000 physicians and other care providers and 4,600 hospitals across the United States. UNH owns 100% of PacifiCare Health Systems, LLC, which in turn owns 100% of PacifiCare Health Plan Administrators, Inc. (PHPA), a California corporation. As of December 31, 2006, PHPA owned 500,000 of the 1,000,000 authorized shares of the Plan's no par common stock. The 500,000 shares represent 100% of the Plan's issued and outstanding shares of common stock.

INTERCOMPANY AGREEMENTS

A significant portion of the Plan's operations is performed by its direct parent and by affiliated companies. The following is a description of the agreements under which the Plan operated as of December 31, 2006:

Management and Administrative Services Agreement – This agreement was entered into on January 1, 1999, between the Plan and PHPA, whereby PHPA will provide management and administrative services for the Plan, including personnel, planning and development, legal services, insurance/reinsurance services, licenses and permits, state and federal regulatory compliance, health service agreements, membership accounting, customer service, claims administration, provider information management, financial reporting and analysis, treasury services, internal audit, tax services, provider contract analysis, facility leases, facility maintenance, personnel management, payroll services, actuarial and pricing services, underwriting services, provider contracting, credentialing, provider relations, quality improvement, utilization management, medical management, health improvement/wellness programs, grievance and appeals, marketing administration, product development, sales and distribution, information services, and office services. Compensation for these services is equal to a percentage of Total Gross Revenues, defined as all collected premiums less any retroactive refunds and adjustments.

Behavior Health Services Agreement – This agreement became effective October 1, 1996, between the Plan and an affiliate, PacifiCare Behavioral Health, Inc. (PBHI), to provide expertise and a provider network for the delivery of chemical dependency and mental health services. The Plan pays a monthly capitation fee of a predetermined PMPM amount that varies depending on the plan code.

Pharmaceutical Services Agreement – Effective October 1, 1998, the Plan and its affiliate, PacifiCare Pharmacy Centers, Inc. (now known as Rx Solutions, Inc.), entered into an agreement to provide pharmacy services and benefit plans. Under Section 5.01 of the agreement, rebates are collected by Rx Solutions, Inc., and sent to the Plan on a quarterly

basis. The administrator charges the Plan a claims processing fee of a predetermined amount per retail claim and per mail claim, plus additional fees for other services.

Master License Agreement – Effective October 1, 1998, the Plan and its affiliate, PacifiCare Life and Health Insurance Company entered into an agreement for the nonexclusive and nontransferable license of service marks, trademarks, trade names, logos, slogans, tag lines or other intellectual properties. The Plan agrees to pay a royalty fee equal to a percentage of total gross revenues, as defined above. Effective January 1, 2007, this royalty fee was reduced to a lower percentage of total gross revenues.

First Restated Tax Sharing Agreement – The Plan was added to the existing consolidated tax agreement between and among all subsidiaries of UnitedHealth Group, Inc., effective January 1, 2006. Computation of tax liability is calculated on a “stand alone” basis and the Plan agrees to remit any estimated tax liability payment on a quarterly basis. Upon filing of the federal consolidated tax return with the IRS, the Plan and UNH will have sixty days to settle any overpayment/underpayment.

Reinsurance Agreement – The Plan entered into an HMO stop-loss reinsurance agreement with an affiliate, PacifiCare Life Assurance Company. This agreement, originally entered into on January 1, 2003, is for a term of one year and is amended annually. See Reinsurance below for further description.

CONFLICT OF INTEREST

The Plan has a conflict of interest policy that requires officers and directors to report conflicts of interest to the Plan. A completed conflict of interest and business ethics questionnaire statement was prepared by all officers and directors. A review of the signed statements did not reveal any conflicts.

CORPORATE RECORDS

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

Articles of Incorporation

The Articles of Incorporation conformed with Oregon statutes. No amendments were made to the Articles of Incorporation during the period under review.

Bylaws

The Bylaws conformed with Oregon statutes. Effective March 15, 2006, the Bylaws were amended to increase the number of directors of the Plan from three to four.

Board of Director Minutes

A review of the Board of Director minutes indicated the Board performed its designated duties in managing the affairs of the Plan as specified in the Bylaws. The review of the 2003 through 2006 Board minutes indicated that the Board approved investments in accordance with the provisions of ORS 733.730 and ORS 733.740. In addition, the Board appoints the chief executive officer, to whom is delegated the authority to approve officer salaries in accordance with the provisions of ORS 732.320(3). Minutes supported the transactions of the Plan and actions taken by its officers.

A quorum met at all meetings, however, a review of the Board minutes disclosed that during two of the four annual meetings held during the period under review, the individual representative of the public did not participate or attend.

FIDELITY BONDS AND OTHER INSURANCE

The examination of insurance coverages involved a review of adequacy of limits and retentions, and the solvency of the insurers providing the coverages. UNH purchased insurance covering itself and its subsidiaries, including the Plan. Fidelity coverage insures against employee dishonesty, counterfeiting, forgery or computer crimes committed by an employee. This coverage is up to an aggregate loss limit of \$25 million after a retention of \$500,000 per loss. Fidelity bond coverage was found to exceed the minimum coverage recommended by the NAIC. In addition, the Plan is covered against directors and officers liability in aggregate for \$10,000,000. Other insurance coverages in force at December 31, 2006, were as follows:

Commercial general liability	Errors and omissions
Professional liability	Workers' compensation

The above coverages were found to be adequate as of December 31, 2006.

PENSION PLANS AND OTHER POST RETIREMENT BENEFITS

The Plan has no employees and therefore, no direct liability for employee benefits. All management and administrative functions are performed under an agreement with PHPA. The ultimate controlling entity, UNH, maintains a pension plan covering all employees of its various subsidiaries.

Defined Contribution Retirement Plans

UNH sponsors a defined contribution retirement plan intended to qualify under Section 401(a) and 401(k) of the Internal Revenue Code of 1986, as amended (the “Code”). Participation in the plan is available to substantially all employees who meet certain eligibility requirements and elect to participate. Employees may contribute up to the maximum limits allowed by Sections 401(k) and 415 of the Code, with UNH matching contributions at 50% of the contribution level, up to a maximum of 3%. Vesting of employee contributions is immediate, and employer matching funds vest after two years.

TERRITORY AND PLAN OF OPERATION

The Plan offers prepaid and point of service (POS) health care services and provides services to its members through contracts with hospitals and physician groups. The physician groups are compensated either through a fixed monthly capitated fee or a fee for service arrangement. For the capitation fee, the primary care physician is responsible for the payment of referral physicians and specialists, while the POS plan pays negotiated fees to physicians for services rendered. Hospitals that contract with the Plan provide inpatient, outpatient, in-area emergency service, and various services to employer groups for a negotiated fee.

A substantial number of enrollees in the Plan’s business include employer groups and individuals covered under the Centers for Medicare and Medicaid Services (CMS) Medicare Advantage program. The product name for these enrollees is known as “Secure Horizons.” Hospitals that provide services in conjunction with this program are paid primarily on negotiated terms.

In addition to Oregon, the Plan has a Certificate of Authority to write insurance in the State of Washington (issued June 30, 1994). However, it wrote business only in Oregon during the period under examination.

In annual statements filed with the Oregon Insurance Division, the Plan reported total enrolled members as follows:

<u>Line of Business</u>	<u>2006</u>	<u>2005</u>	<u>2004</u>	<u>2003</u>
Individual hospital & medical	851	1,615	1,872	2,316
Group hospital & medical	16,751	21,702	33,422	48,599
Federal Employee HBP	4,859	5,183	5,966	7,265
Medicare	<u>23,657</u>	<u>23,025</u>	<u>22,682</u>	<u>23,992</u>
Total enrollment	<u>46,162</u>	<u>51,515</u>	<u>63,942</u>	<u>82,172</u>

GROWTH OF THE COMPANY

The growth of the Plan since the last financial examination is reflected in the following schedule. The stated amounts were derived from the Plan's filed annual statements and where indicated, from an examination report.

<u>Year</u>	<u>Assets</u>	<u>Liabilities</u>	<u>Surplus as Regards Policyholders</u>	<u>Net Income</u>
2002*	\$ 95,257,080	\$48,666,705	\$46,590,375	\$ 7,608,569
2003	99,227,466	56,009,006	43,218,460	(3,244,691)
2004	74,596,024	34,973,922	39,622,103	10,353,639
2005	78,455,313	33,613,961	44,841,352	7,558,703
2006*	103,658,828	52,739,987	50,918,841	13,439,456

*Per examination

LOSS EXPERIENCE

The following exhibit reflects the annual underwriting results of the Plan since 2002. The amounts were compiled from copies of the Plan's filed annual statements and where indicated, from an examination report.

Income Statement - Loss Ratios on a Calendar Year Basis

<u>Year</u>	(1) <u>Net Premium Income</u>	(2) <u>Loss and Loss Adjustment Expenses (LAE) Incurred</u>	(2/1) <u>Ratio</u>
2002*	\$373,381,367	\$326,807,220	87.53%
2003	358,088,945	329,477,506	92.01%
2004	327,240,035	277,891,644	84.92%
2005	310,629,648	263,628,768	84.87%
2006*	319,210,553	261,159,160	81.81%

*Per examination

HOLDING COMPANY REGISTRATION

Timely and complete holding company registration statements were filed by the Plan in accordance with the provisions of ORS 732.552, ORS 732.554, ORS 732.564 and Oregon Administrative Rule (OAR) 836-27-020(1).

During the period examined, the Plan paid dividends to its parent, as follows:

<u>Year</u>	<u>Cash Dividend</u>
2003	\$ 0
2004	15,000,000
2005	5,000,000
2006*	7,300,000

*Per examination

The Plan made the proper disclosure of these dividends to the director of the Department of Consumer and Business Services in accordance with the reporting requirements established by ORS 732.554. The Plan did not pay extraordinary dividends during the period examined.

REINSURANCE

Stop-Loss Agreement

For 2006, the Plan's reinsurance program was comprised of an HMO Stop-Loss Agreement with an affiliate, PacifiCare Life Assurance Company (NAIC #84506). Under terms of the agreement, the reinsurer reimburses the Plan for losses per member up to \$2,000,000 after retention of \$400,000 plus 20% of all hospital and medical services in excess of the specific

retention. Lifetime benefit per member is \$2,000,000. It was determined the Plan's reinsurance agreement clearly specified the risk taken by the reinsurer, with no unusual provisions reducing the reinsurer's risk.

Insolvency Clause

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

Risk Retention

The Plan's reinsurance agreement requires the Plan to retain \$400,000 per person and 20% of hospital and medical losses. In view of the Plan's surplus of \$50,918,841 at December 31, 2006, the Plan does not retain risk on any one subject of insurance in excess of 10% of its surplus to policyholders pursuant to the maximum risk retention set by ORS 731.504.

STATUTORY DEPOSIT

To satisfy the statutory deposit requirements in Oregon for a health care service contractor, the Plan has on deposit a surety bond in the amount of \$250,000 with the Department of Consumer and Business Services, Insurance Division. Bond #6120713 was placed on September 5, 2001 to be effective October 15, 2001, with Safeco Insurance Company of America and is still in place as of the date of this examination.

In addition, the Plan reported \$390,846 in short-term investments held in a custody account with the State of Washington Department of the Insurance Commissioner. This was properly disclosed on Schedule E – Part 3 in the 2006 annual statement.

ACCOUNTS AND RECORDS

Most of the records are maintained at the corporate offices of UNH, in Minnetonka, Minnesota. Some of the accounting records and the corporate documents were shipped to the Plan's Lake Oswego, Oregon, offices. New procedures enacted by the Oregon Insurance Division now allow examiners to travel to where the records are maintained. The Plan is therefore in compliance with ORS 732.245, which requires every domestic insurer to keep its records in Oregon. In general, the Plan's records and source documentation supported the amounts presented in the Plan's December 31, 2006 annual statement, with the following exceptions:

Intercompany Settlements

The Plan's current intercompany process uses consolidated settlements between the various subsidiaries of UNH. In order to minimize wire transfer activity and make the intercompany process more efficient, consolidated settlements are made to a "settlement business unit." All applicable entities consolidate the items to be settled and transfer cash with this "settlement business unit." All wire transfers for a particular settlement are done on the same day. Because the entities all have cash move on the same day, the effect is the same as if the entities all transferred money between each other. The net effect of the "settlement business unit" is zero.

The Plan provided general ledger details to verify settlements of sampled items from the intercompany payable detail. However, the settlements did not indicate which entity was being settled with or give any further explanation or detail. Further, the examiner requested January bank statements as independent settlement documentation of the sampled items. The bank statement settlement amounts did not match the amounts in the sample for any of the items. Upon further request, the Plan failed to provide an explanation or reconciliation from

the bank statement to the sampled amounts. One sampled item matched to a wire transfer settlement, however, the settlement date on the wire transfer was September 14, 2006. As a result, the amount should not have been an outstanding intercompany payable at December 31, 2006. Again, the Plan failed to explain why the amount remained outstanding. Finally, the Plan did not provide any supporting or settlement detail for two tax related sampled items.

I recommend the Plan maintain records with sufficient detail to verify subsequent settlements of year-end intercompany receivable/payable balances, pursuant to ORS 731.308(2). This will allow the examiners to determine reasonableness and consistency of the year-end balances, to verify collectability, and to determine if the year-end intercompany amounts are adequately stated, in accordance with the examination requirements of the NAIC Examiners Handbook.

Advance Premium

The detail of premiums received in advance only comprised \$33,837 out of a total reported balance of \$3,197,579. As a result, the detail could not be agreed to the general ledger or to the filed annual statement. In addition, the Plan did not provide Employer Group agreements and related contract face sheets detailing group/plan/year rates and contract period for the advance premium sample. The examiner could not confirm that the Plan was in compliance with the provisions of SSAP No. 54 based on the detail provided for testing of premiums received in advance because related contracts were not provided for the sampled amounts. As a result, the policy effective date could not be verified.

I recommend the Plan perform regular reconciliations of the advance premium account and include payment date and policy coverage dates to verify that the premium amount was paid in advance of the coverage date. In addition, the Plan shall maintain all contracts related to advance premium so the examiner can determine compliance with SSAP No. 54.

COMPLIANCE WITH PRIOR EXAMINATION RECOMMENDATIONS

The Plan has complied with most of the recommendations in the report of financial examination made as of December 31, 2002. The following exception was noted:

I recommend the Company ensure at least one-third of the members of the Board of Directors be representatives of the public to comply with the provisions of ORS 750.015.

As was noted earlier in this report, the representative of the public was not present at two of the four meetings held during the period under review. In August 2006, the Plan elected Susan A. Brickey to the Board as the representative of the public, however, effective March, 2006, the Plan had expanded the number of board members to four, which places the Plan out of compliance with the statute and with their own Bylaws.

PACIFICARE OF OREGON, INC.
ASSETS
DECEMBER 31, 2006

	<u>ANNUAL</u> <u>STATEMENT</u>	<u>EXAMINATION</u> <u>ADJUSTMENTS</u>	<u>EXAMINATION</u> <u>BALANCE</u>	<u>NOTE</u>
Assets				
Bonds	\$59,797,942		\$59,797,942	1
Cash and short-term investments	30,609,454		30,609,454	1
Aggregate write-ins for invested assets	-	-	-	
Subtotal, cash and invested assets	\$90,407,396	\$0	\$90,407,396	
Investment income due and accrued	707,068	-	707,068	
Premiums and considerations:				
Uncollected premiums and agent's balances in the course of collection	5,072,621	-	5,072,621	
Deferred premiums, agents' balances and installments booked but deferred and not yet due.	-	-	-	
Accrued retrospective premiums	-	-	-	
Net deferred tax asset	2,997,246	-	2,997,246	
Receivables from parent, subsidiaries, and affiliates	2,656,469	-	2,656,469	
Health Care and other amounts receivable Aggregate write-ins for other than invested assets	1,818,028	-	1,818,028	
	-	-	-	
Total Assets	<u>\$103,658,828</u>	<u>\$0</u>	<u>\$103,658,828</u>	

PACIFICARE OF OREGON, INC.
LIABILITIES, CAPITAL AND SURPLUS
DECEMBER 31, 2006

Liabilities, Capital and Surplus			
Claims unpaid	\$22,378,509	\$22,378,509	2
Accrued medical incentive pool and bonus arrangements	1,133,026	1,133,026	2
Unpaid claims adjustment expense	588,544	588,544	2
Aggregate health policy reserves	12,804,695	12,804,695	2
Aggregate health claim reserves	186,335	186,335	2
Premiums received in advance	3,197,579	3,197,579	
General expenses due or accrued	960,218	960,218	
Current Federal and foreign income tax payable and interest thereon	3,545,140	3,545,140	
Amounts withheld or retained for account of others	9,270	9,270	
Amounts due to parent, subsidiaries, and affiliates	4,887,951	4,887,951	
Liability for amounts held under uninsured accident and health plans	3,048,720	3,048,720	
Aggregate write-ins for liabilities	-	-	
Total Liabilities	<u>\$52,739,987</u>	<u>\$0</u>	
Common capital stock	500,000	500,000	
Gross paid in and contributed surplus	11,500,000	11,500,000	
Aggregate write-ins for other than special surplus funds	500,000	500,000	
Unassigned funds (surplus)	38,418,841	-	38,418,841
Total Capital and Surplus	<u>50,918,841</u>	<u>-</u>	<u>50,918,841</u>
Total Liabilities, Capital and Surplus	<u>\$103,658,828</u>	<u>\$0</u>	<u>\$103,658,828</u>

PACIFICARE OF OREGON, INC.
STATEMENT OF REVENUE AND EXPENSES
DECEMBER 31, 2006

	<u>BALANCE</u> <u>PER COMPANY</u>	<u>EXAM</u> <u>ADJ</u>	<u>BALANCE</u> <u>PER EXAM</u>	<u>NOTE</u>
Member months	<u>572,907</u>	-	<u>572,907</u>	
Net premium income	\$324,687,649	\$0	\$324,687,649	
Change in unearned premium reserves and reserve for rate credits	(5,477,096)	-	(5,477,096)	
Aggregate write-ins for other non-health care related revenue	<u>-</u>	<u>-</u>	<u>-</u>	
Total Revenues	<u>\$319,210,553</u>	<u>\$0</u>	<u>\$319,210,553</u>	
Hospital and Medical:				
Hospital/medical benefits	230,141,022	-	230,141,022	
Other professional services	2,727,134	-	2,727,134	
Outside referrals	-	-	-	
Emergency room and out-of-area	-	-	-	
Prescription Drugs	22,354,348	-	22,354,348	
Incentive pool and withhold adjustments	<u>231,817</u>	<u>-</u>	<u>231,817</u>	
Subtotal:	\$ 255,454,321	\$ -	255,454,321	
Less:				
Net reinsurance recoveries	<u>95,334</u>	<u>-</u>	<u>95,334</u>	
Total medical and hospital	255,358,987	-	255,358,987	
Non-health claims	-	-	-	
Claim adjustment expenses	5,800,173	-	5,800,173	
General administrative expenses	38,285,417	-	38,285,417	
Increase in reserves for life and accident and health contracts	<u>-</u>	<u>-</u>	<u>-</u>	
Total underwriting deductions	<u>299,444,577</u>	<u>-</u>	<u>299,444,577</u>	
Net underwriting gain or loss	<u>19,765,976</u>	<u>-</u>	<u>19,765,976</u>	
Net investment income earned	3,677,332	-	3,677,332	
Net realized capital gains or (losses)	<u>(339,734)</u>	<u>-</u>	<u>(339,734)</u>	
Net investment gains or (losses)	<u>3,337,598</u>	<u>-</u>	<u>3,337,598</u>	
Net income or (loss) before federal income taxes	23,103,574	-	23,103,574	
Federal and foreign income taxes incurred	<u>9,664,118</u>	<u>-</u>	<u>9,664,118</u>	
Net Income (loss)	<u>\$13,439,456</u>	<u>\$0</u>	<u>\$13,439,456</u>	

PACIFICARE OF OREGON, INC.
RECONCILIATION OF SURPLUS SINCE THE LAST EXAMINATION
FOR THE YEARS ENDED DECEMBER 31, 2006

	2006	2005	2004	2003
Capital and surplus, December 31, previous year	<u>\$44,841,352</u>	<u>\$39,622,103</u>	<u>\$43,218,460</u>	<u>\$46,590,375</u>
Net income	13,439,456	7,558,703	10,353,639	(3,244,691)
Net unrealized capital gains or (losses)	-	-	-	-
Change in net unrealized foreign exchange capital gain (loss)	-	-	-	-
Change in net deferred income tax	(15,649)	3,114,502	1,025,086	(420,890)
Change in nonadmitted assets	(46,318)	(453,956)	24,917	293,666
Change in provision for 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 from surplus (Stock Dividend)	-	-	-	-
Transferred to surplus	-	-	-	-
Net remittances from or (to) Home Office	-	-	-	-
Dividends to stockholders (cash)	(7,300,000)	(5,000,000)	(15,000,000)	-
Change in treasury stock	-	-	-	-
Aggregate write-ins for gains and losses in surplus	-	-	-	-
Examination adjustment	-	-	-	-
Cumulative effects of changes in accounting principles	-	-	-	-
Aggregate write-ins for gains and losses in surplus	-	-	-	-
Change in surplus as regards policyholders for the year	<u>6,077,489</u>	<u>5,219,249</u>	<u>(3,596,358)</u>	<u>(3,371,915)</u>
Surplus as regards policyholders, December 31, current year	<u>\$ 50,918,841</u>	<u>\$ 44,841,352</u>	<u>\$ 39,622,102</u>	<u>\$ 43,218,460</u>

NOTES TO THE FINANCIAL STATEMENTS

Note 1 - Investments

Most of the Plan's long-term bond investments were in US Treasury obligations, federal agency bonds, municipal obligations, and corporate issues. The Plan did have some exposure to mortgaged-backed and asset-backed securities, but all issues were investment rated. Cash and short-term deposits consisted of US Treasury Bills and various money market funds. 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>Cash and</u> <u>Short-term</u>	<u>Ratio</u> <u>A/</u> <u>Total Assets</u>	<u>Ratio</u> <u>B/</u> <u>Total Assets</u>
2002	\$64,015,551	\$20,622,257	67%	22%
2003	67,890,694	25,508,909	68%	26%
2004	67,126,746	(5,051)	90%	0%
2005	65,037,955	1,929,427	83%	3%
2006	59,797,942	30,609,454	58%	29%

The Board of Directors approved the investment transactions, pursuant to ORS 733.740. As of December 31, 2006, invested assets of \$41,785,328, representing 46% 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.

Note 2 – Claims Unpaid and Unpaid Claims Adjustment Expenses

The DCBS actuaries, Scott Fitzpatrick, FSA, MAAA and David Ball, FSA, MAAA, performed a review of the Plan's unpaid claims liability as of December 31, 2006. Based on the Plan's claims runoff data, they concluded that the December 31, 2006, liability for unpaid claims was adequate. The underlying data supporting the review was examined by DCBS insurance examiners. No exceptions were noted during the examination of the Plan's claims data.

SUMMARY OF COMMENTS AND RECOMMENDATIONS

Following is a summary of the comments and recommendations made as a result of this examination.

Page

- 6 I recommend the Plan replace a current director with an individual that would qualify as a representative of the public, or consider amending its Bylaws to add an additional board member that would qualify as a representative of the public in compliance with ORS 750.015 and the Plan's Bylaws.
- 17 I recommend the Plan maintain records with sufficient detail to verify subsequent settlements of year-end intercompany receivable/payable balances, pursuant to ORS 731.308(2). This will allow the examiners to determine reasonableness and consistency of the year-end balances, to verify collectability, and to determine if the year-end intercompany amounts are adequately stated, in accordance with the examination requirements of the NAIC Examiners Handbook.
- 18 I recommend the Plan perform regular reconciliations of the advance premium account, and include payment date and policy coverage dates to verify that the premium amount was paid in advance of the coverage date. In addition, the Plan shall maintain all contracts related to advance premium so the examiner can determine compliance with SSAP No. 54.

Within 21 days of the publication of this report, the Plan must submit a Plan of Action to identify the steps to be taken to satisfy each of the above recommendations. Within three months of the publication of this report, or as soon thereafter as practical, the Insurance Division will conduct a follow-up examination to ensure appropriate steps have been taken by the Plan to satisfy each recommendation.

CONCLUSION

During the four-year period covered by this examination, the surplus of the Plan has increased from \$46,590,375, as presented in the December 31, 2002, report of examination, to \$50,918,841, as shown in this report of examination. The comparative assets, liabilities, and surplus are shown below:

	December 31,		
	<u>2006</u>	<u>2002</u>	<u>Change</u>
Assets	\$103,658,828	\$95,257,080	\$8,401,748
Liabilities	<u>52,739,987</u>	<u>48,666,705</u>	<u>4,073,282</u>
Surplus	<u>\$ 50,918,841</u>	<u>\$46,590,375</u>	<u>\$4,328,466</u>

SUBSEQUENT EVENTS

Effective January 1, 2007, the Plan entered into an Administrative Services Agreement with an affiliate, ACN Group, Inc., for delivery of chiropractic services and alternative medicines. ACN Group agrees to provide all administrative and support services as described in the agreement in exchange for a predetermined PMPM amount. This agreement was reviewed by the Oregon Insurance Division and a “no objection” letter was issued September 22, 2006.

ACKNOWLEDGMENT

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

In addition to the undersigned, Mark Giffin, CFE, and Raymond W. Anderson, AFE, insurance examiners, and Scott Fitzpatrick, FCAS, MAAA, actuary 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 PacifiCare of Oregon, Inc.
2. 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. The examination of PacifiCare of Oregon, Inc., 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 _____, 2007.

Notary Public for the State of Oregon

My Commission Expires: _____