Report on Examination

of the

Associated Builders & Contractors of Tennessee Workers' Compensation Self-Insurance Fund

Memphis, Tennessee

as of

March 31, 2004

Department of Commerce and Insurance

State of Tennessee

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Company Examinations

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Nashville, Tennessee

August 21, 2006

Honorable Paula A. Flowers
Commissioner of Commerce and Insurance
State of Tennessee
500 James Robertson Parkway
Nashville, Tennessee 37243

Commissioner:

Under authority delegated by you and in compliance with your instructions, a financial examination and market conduct review has been made of the condition and affairs of the

Associated Builders & Contractors of Tennessee
Workers' Compensation Self-Insurance Fund
1408 Ridgeway Road
Memphis, Tennessee 38119

(Hereinafter referred to as the "Fund") as of March 31, 2004, and a report thereon is respectfully submitted as follows:

Introduction

This examination was arranged by the Commissioner of the Tennessee Department of Commerce and Insurance, in accordance with Tenn. Code Ann. § 50-6-405 and Tenn. Comp. R. & Regs., 0780-1-54-.06. It was commenced on May 4, 2005, by examiners employed with the Tennessee Department of Commerce and Insurance. This is the first examination of the Fund.

Scope of Examination

The period covered hereunder is from January 1, 1999, to the close of business on March 31, 2004, the date of this examination. In addition, since this is the first examination conducted of the Fund, information is also provided in select areas from the Fund's inception in 1994 through the examination as listed above. The examination was conducted at the office of the Fund's service company, Alternative Services Concepts, L.L.C, located at 1101 Kermit Drive, Suite 800, Nashville, Tennessee. The Fund maintains its records at three (3) locations. The Fund's Trust Agreement and Bylaws, Indemnity Agreement and Power of Attorney, Third-Party Agreements, and Board of Trustees and member meeting minutes are maintained by the Fund Administrator who is located at 1408 Ridgeway Road, Memphis, Tennessee. All accounting and claim files are located at the office of Fund's service company, Alternative Services Concepts, L.L.C , in Nashville, Tennessee. All records associated with Fund membership, underwriting, marketing, excess insurance and liability insurance coverage is located at the office of Willis Pooling, Nashville, Tennessee.

During the course of the examination, the assets of the Fund were verified, and liabilities were determined or estimated as of March 31, 2004, in accordance with procedures as prescribed by Tenn. Code Ann. and Tenn. Comp. R. & Regs., of the State of Tennessee, the National Association of Insurance Commissioners (NAIC), the National Council on Compensation Insurance (NCCI) and Generally Accepted Accounting Principles (GAAP) where applicable. The Fund's financial solvency and degree thereof was thus established. Test checks covering selected periods were made of income and disbursement items, and a general review was made of the Fund's operations, practices and compliance with Tenn. Code Ann. and Tenn. Comp. R. & Regs., to the extent hereinafter set forth. In order to reduce duplication of examination procedures and to contribute to the efficiency of this examination, the examiners relied upon the work papers of the Fund's independent accountants, to the extent deemed necessary.

An examination of all asset and liability items contained in the financial statement of this report was made and individual items were verified with relative emphasis according to

their amount and significance. An examination was also made into the following matters:

History and Organization
Trust Agreement and Bylaws
Indemnity Agreement
Management and Control
Corporate Records
Management Agreements
Premium Refunds
Fidelity Bonds
Statutory Deposit
Market Conduct Activities
Excess Insurance Coverage
Loss Experience
Accounts and Records
Litigation, Contingent Liabilities and Subsequent Events
Subsequent Events
Financial Statement

They are discussed in detail as follows:

History and Organization

The Tennessee Chapter, Associated Builders and Contractors, Inc. (ABC) is a Tennessee non profit trade association of licensed builders, suppliers, and service companies associated with the building industry which was organized in the State of Tennessee in 1971. The Chapter was initially incorporated as the Middle Tennessee Chapter, ABC and the charter was later amended in 1973 changing the name to the Tennessee Chapter, ABC. ABC is made up of three (3) regional Chapters, the West, Middle and East Tennessee Chapters.

On September 12, 1994, the Fund was created by members of ABC to act as a self-insured workers' compensation pool in accordance with Tenn. Code Ann. § 50-6-405(c)(1). A certificate of approval was issued to the Fund by the Tennessee Department of Commerce and Insurance on January 4, 1995, with an effective date of January 1, 1995, authorizing the Fund to conduct operations as a self-insured workers' compensation pool. The operation of the Fund is confined to the State of Tennessee where it is licensed to transact the business of workers' compensation and employers' liability insurance.

Membership in the Fund is composed of qualifying members of ABC that have pooled their liabilities in accordance with the Tennessee Workers' Compensation Act. The Fund at March 31, 2004, included eighty-two (82) members.

The Fund was developed with the objective of bringing ABC membership a benefit package consisting of fair pricing, availability to qualifying members, superior service and an opportunity to share in the profits of the Fund. The Fund lists the following as its Mission Statement:

> Providing more control over the influence of insurance cost by giving commercial contractors and suppliers in the State of Tennessee a workers' compensation self-insurance pool that is:
>
> - A viable alternative to the commercial insurance market
> - Designed to provide long term financial stability
> - Less susceptible to the pricing fluctuations of the commercial insurance market
> - A partnership between participating members and claims administration in hands on claims management
> - Supportive of safety with industry specific loss control methods and solutions.

The following table reflects the growth and financial history of the Fund, since its organization, as shown by its financial statements filed with the Tennessee Department of Commerce and Insurance:

*Year	Members	**Total Revenue	Total Expenses	Assets	Equity
December 31, 1995	47	$2,310,386	$2,502,739	$1,907,867	$(192,353)
December 31, 1996	66	4,152,748	3,803,663	4,426,592	96,732
December 31, 1997	63	4,148,899	4,025,179	5,129,458	230,452
December 31, 1998	58	3,490,734	3,480,614	4,342,282	279,572
March 31, 2000 (15 Months)	59	3,871,304	3,860,899	4,385,973	289,977
March 31, 2001	58	3,167,622	3,157,424	4,014,797	300,175
March 31, 2002	55	3,322,551	3.300,232	4,175,388	322,494
March 31, 2003	66	4,532,193	4,275,777	5,918,609	578,910
March 31, 2004	82	5,769,898	5,571,786	6,798,491	751,022

* The Group changed its fiscal year end from December 31 to March 31 during calendar year 2000; therefore, no financial statement was published for 1999, and the 2000 financial statement is for 15 months.

** Total Revenue = Premium Revenue + Interest Income.

Fund and Trust Agreement and Bylaws

The Fund was created through the adoption of the "Fund and Trust Agreement and Bylaws" which was executed on September 12, 1994. The Fund was formed to act as a workers' compensation self-insurance pool as defined by Tenn. Comp. R. & Regs., 0780-1-54-.02 and as authorized by Tenn. Code Ann. § 50-6-405. The Fund and Trust Agreement and Bylaws state that the Fund is being established as a collective fund to provide monies for payment of claims filed against the members under the Tennessee Workers' Compensation Law.

The Fund is an association which is owned by its members. Membership in the Fund is limited to the Tennessee Chapter, ABC and its members in good standing, associate members, and independent contractors affiliated with such members. The term "members" includes those individuals, corporations and partnerships executing, or otherwise being bound by, the Indemnity Agreement.

There have been two (2) recorded amendments to the Fund's bylaws since their adoption in 1994. On March 8, 2000, the Fund year was changed to commence at 12:01 a.m. on the 1st day of April each year, and ending at 12:01 a.m. on the 1st day of April of the following year. Previous fund years had coincided with the calendar year. On May 27, 1988, provisions for resignation and termination of, and reapplication for membership were added to the Fund's bylaws.

Indemnity Agreement

In accordance with Tenn. Comp. R. & Regs., 0780-1-54-.04(2)(e), each member is required to execute and be bound by an Indemnity Agreement as a condition of membership in the Fund. The Fund's Indemnity Agreement was reviewed, and listed below is a summary of the significant terms agreed to:

- The Fund and each member will, jointly and severally, assume and discharge by

payment any final, non-appealable, awards entered in the Courts of the State of Tennessee against any member of the Fund, or the Fund itself, for workers' compensations benefits for employees or their dependents and that the agreement is a mutual covenant of assumption and not a partnership.

- The Board of Trustees will set up, operate and enforce the administrative rules, regulations and bylaws of the Fund and the Fund may admit as members of the Fund only those who meet the criteria for membership established by the Board of Trustees.

- The members ratify and confirm the appointment of the Fund's Service Agent(s), and that each member hereby appoints the Service Agent(s) as its agent and attorney-in-fact.

- Each member shall initiate and maintain a safety program to provide its employees safe and sanitary working conditions and that each member will allow representatives of the Fund and the Service Agent(s) access to all work sites for the purpose of determining whether the member's safety program and practices meet the Fund's criteria for membership in the Fund.

- Each member shall pay promptly all contributions and assessments by the Fund and that this requirement is also extended to former members who were such during any part of the year(s) for which contributions or assessments are due.

- Each member shall allow their books, vouchers, contracts, documents and records of any and every kind while such person is a member and within two (2) years after final termination of membership which show or tend to show or verify the contribution which is payable under the terms of the agreement.

- The Fund will defend, in the name of the member and on behalf, any suits or other proceedings which may at any time be instituted against such member on account of injuries or death within the purview of the Tennessee Workers' Compensation Act.

- The Fund will provide each prospective member at the time of application for membership a written description of any refund plan then in effect.

- Members, joint and severally, agree that there will be no disbursements to members out of assets of the Fund in the form of dividends or distributions of accumulated reserves until provisions have been made for the Fund's obligations under the Workers' Compensation Law and then only at the discretion of the Board of Trustees.

Management and Control

The operation and administration of the Fund is the joint responsibility of a Board of Trustees consisting of not less than five (5) nor more than nine (9) members. The Fund's bylaws state that all Trustees must be the designated representative of a member in good standing with ABC, that the original Trustees are elected to an indefinite term, and that all other Trustees are elected to three (3) year terms and may serve an indefinite number of terms if so elected. The bylaws further state that the Board of Trustees shall include equal representation from each region with the position of Chairman rotated annually among the regions. In addition, Tenn. Comp. R. & Regs., 0780-1-54-.07 requires:

- That Trustees must be residents of the State of Tennessee or officers of corporations authorized to do business in the State of Tennessee;
- That at least two-thirds of the Trustees shall be employees, officers, or directors of members of the Fund;
- Affiliates of the administrator or the service agent shall not serve as a Trustee.

Examination procedures included verification of the Fund's compliance with Tennessee Rules and Regulations. As of March 31, 2004, the following persons were serving as members of the Board of Trustees:

Board of Trustees	Employment Information
Dale L. Denny, Chairman	Chief Financial Officer and General Counsel, John Bouchard & Sons Company, Nashville, Tennessee
Mike Webb, Vice Chairman	President, Webb & Sons Construction Company Inc., Athens, Tennessee
Mike Hankins	President, Acoustics & Specialties Inc., Memphis, Tennessee
Ralph Harnes	Secretary/Controller, Joseph Construction Company Inc., Knoxville, Tennessee
R.E. Linkous	President, Linkous Construction Company Inc., Memphis, Tennessee
Charles Dennis	President, Dennis Electric, Inc., Memphis, Tennessee
Jerry L. Barrix	President, Wade Electric, Jackson, Tennessee
Jim Pedigo	Chief Financial Officer, J. E. Crain & Son, Nashville, Tennessee
Jim Wakefield	President, Wakefield Corporation, Knoxville, Tennessee

Election of Trustees is made by the members of the Fund in good standing during the opening of the Fund's annual meeting. The Board of Trustees, from their own members and by majority vote, elects a Chairman and a Vice Chairman. The Chairman and Vice-Chairman serve one (1) year terms and the Vice-Chairman may serve successive terms. Trustees may elect other officers as desirable who serve at the pleasure of the Board of Trustees. Trustees receive reimbursement for their actual, reasonable expenses incurred in the performance of their duties as members of the Board of Trustees.

In the event the office of any Trustee becomes vacant, the remaining Trustees may by majority vote appoint a successor Trustee to serve the remainder of the unexpired term and until his successor is elected. The Board of Trustees has the right at any time by majority vote to remove a Trustee for cause. The successor Trustee is elected by majority vote and will hold office until the next annual election of the Board of Trustees. Powers and Duties of the Board of Trustees as stated in the bylaws include the following:

- The Board of Trustees shall have the power to invest the monies in the Fund Account, and may engage a Fund Account Fiduciary for that purpose. Investments are limited to those approved under the laws of the State of Tennessee and the Regulations of the Tennessee Department of Commerce and Insurance. Loans from the Fund Account to any member, or any organization affiliated with the Fund, are not permitted.

- The Board of Trustees shall have the power to make, execute, acknowledge and deliver any and all documents required to be made in connection with the settlement and defense of any claim.

- The Board of Trustees shall have the power to settle, compromise, or submit to arbitration any claims, debts or damages due or owing to or from the Fund; to commerce or defend suits or legal or administrative proceedings, and to represent the Fund, the Administrator and the members in all suits and Legal proceedings.

- The Board of Trustees shall have the power to employ an Administrator, Service Agent, Fund Actuary, Fund Accountant and other suitable agents and pay their reasonable expenses and compensation.

- The Board of Trustees shall have the power to assess rates, premiums, contributions and penalties; accept or reject any application for membership; declare dividends and terminate membership.

- The Board of Trustees shall have the duty to take all reasonable precautions to protect the members from losses and shall enter into any suitable excess insurance contracts to fully and adequately protect members against excess losses.

Corporate Records

The Fund's bylaws state that the Board of Trustees shall hold quarterly meetings with the date of such meeting to be set by the Chairman. No notice is required for regular meetings of the Board of Trustees, and special meetings of the Board of Trustees may be called at any time by the Chairman or any two (2) Trustees. Notice of any special meeting shall be given in writing or personally, by mail, phone or facsimile not less than three (3) days before such meeting; however, by unanimous consent of the Trustees, special meetings may be held without notice at any time and place. Attendance of Trustees at duly called meetings is mandatory and absence by any Trustee from two (2) consecutive meetings shall result in the office of such Trustee being automatically declared vacant. If

the Trustee shows good cause for the absence, by majority vote of the Board of Trustees, such absence may be excused if the absent Trustee has voted by proxy.

During the period under examination (January 1999 to March 2004) there were forty-two (42) regular meetings, twenty-two (22) telephone conference meetings and four (4) special meetings of the Board of Trustees. There were four (4) annual meetings of the Fund's membership. The Fund experienced high attendance by Trustees at all meetings with the Fund always obtaining a quorum for the transaction of business. The minutes of the meetings were reviewed and appear deficient in the recording of Trustee elections. It was not apparent from review of the minutes that election of the Chairman and Vice Chairman occurred in accordance with the Fund's bylaws. This issue is further addressed in the "Comments" section of this report.

Management Agreements and Policies

Administrator Agreement

The Board of Trustees has engaged an administrator within the meaning of Tenn. Comp. R. and Regs., 0780-1-54-.02(1), to carry out policies established by the Board of Trustees and provide for the daily management of the Fund, to the extent such functions are not performed by the service company. Beginning with the inception of the Fund, Walter Parr was the Board of Trustees appointed administrator, and on January 1, 1997, he was replaced when the Fund entered into an "Administration Agreement" with Sally Alston. As of the date of this report, Ms. Alston is serving as the Fund's administrator and under the current contract, is responsible for providing the following services:

- Maintaining in effect the certificate of approval issued to the Fund by the Tennessee Department of Commerce and Insurance.
- Maintaining the accounting books and records, preparing the financial statement and arranging for an annual audit of the Fund by independent certified public accountants by working through the appointed service company.
- Preparing all reports furnished to the members through the appointed service company.

- Soliciting applications for membership in the Fund if licensed as a property and casualty agent (Administrator is not licensed and does not solicit applications).
- Providing all clerical, secretarial and administrative support required by the Fund and the Board of Trustees, including keeping minutes of all Board of Trustees and membership meetings, as recorded by an individual appointed by the service company.
- Overseeing the service company's duties of receiving premium payments from the members, depositing funds in the claims account to pay claims expenses and excess insurance, and depositing the balance in the administrative account established by the Fund.
- Administering and investing, in accordance with the criteria established by the Board of Trustees, funds not needed for current obligations as is handled by the Fund's investment firm.
- Negotiating and executing with the approval of the Fund, agreements with service companies.
- Directing the daily operations of the Fund in cooperation with the Service Agent to ensure operations are conducted in a sound business like manner.

The Administrator's compensation is set by the Board of Trustees and is based on a percentage of the Fund's premiums earned (i.e. the annual amount paid by the members of the Fund). The fee paid is based on invoiced earned premiums and is subject to adjustment upon completion of the payroll audits of the members of the Fund and the annual audit of the Fund's financial statement. Any overpayment or underpayment of compensation is promptly settled.

The agreement automatically renews for successive one (1) year terms, unless terminated. It can be terminated for cause in the event of a breach of the agreement by either party, or can be terminated without cause by either party within ninety (90) days written notice to the other party.

The agreement directs the Administrator to furnish on or before one hundred twenty (120) days after the end of each fiscal year an audited financial statement and on or before forty-five (45) days after the end of each fiscal quarter unaudited financial statements. These reports shall be in a form approved by the Commissioner of the Tennessee Department of Commerce and Insurance and shall include known claims and expenses,

claims incurred but not reported, unearned premiums, and bad debts.

The Administrative Agreement empowers the Administrator to execute agreements on behalf of the Fund with accountants, attorneys, custodians, brokers, investment advisors and other consultants and agents. The agreement gives special emphasis on empowerment of the Administrator to place any part of the assets of the Fund in a custodial account or accounts with a financial institution with the authority to invest and reinvest such assets in accordance with policies and criteria approved by the Board of Trustees.

Claims Service Agreement (Alternative Service Concepts)

The Fund enters into a service agreement each year for the provision of claims and other administrative services. Contracts are executed at the beginning of each fiscal year with a starting date of April 1st and an ending date of March 31st of the following year. Beginning with the Fund's inception, these services were provided by Willis Administrative Services Corporation (WASC) a subsidiary of Willis Corroon Corporation. On May 1, 2002, WASC was sold by Willis Corroon Corporation to a group of investors who changed WASC's name to Alternative Service Concepts, LLC (ASC). On April 1, 2003, and each year thereafter, ASC has provided these services to the Fund. Listed below is a summary of the major provisions in the current contract with ASC:

ASC Agrees:

- To review all claim and/or loss reports with claim and/or loss dates incurred and reported during the term of Contract which involve Workers' Compensation claims against the Fund.
- To investigate, adjust, settle or resist all such losses and/or claims within the discretionary settlement authority limit of thirty thousand dollars ($30,000); and for cases in excess of the discretionary settlement authority limit, only with specific prior approval of the Fund.
- To furnish claims forms necessary for proper claims administration.

- To establish claims and/or loss files for each reported claim and/or loss. All files shall be exclusive property of the Fund and shall be available for review by the Fund at any reasonable time, with notice.

- To furnish the Fund a monthly Claim Activity Report.

- To provide financial statements to include the preparation and distribution of monthly Balance Sheets and Income Statements based on data provided by the underwriters and/or administrators; and reconcile the claims payment account.

- To assist independent auditors in their preparation of annual financial statements.

- To maintain adequate General Liability, Automobile Liability, Workers' Compensation, Fidelity Bond and Errors and Omissions Insurance Coverage.

- To indemnify, defend and hold harmless the Fund with respect to any claims asserted as a result of any errors, omissions, torts, intentional torts or other negligence on the part of ASC and/or its employees, unless they complained of actions of ASC were taken at the specific direction of the Fund.

The Fund Agrees:

- To make funds available for ASC to draw from for claim and/or loss payments and for associated allocated expense within the discretionary settlement authority limit of thirty thousand dollars ($30,000).

- To pay all allocated loss expenses (i.e. attorney fees, expert fees, independent medical examinations, etc.) in addition to the claims service fee.

- To relinquish authority to ASC in all matters relating to claims service within the discretionary settlement authority limit.

- If ASC acting at the specific direction of the Fund becomes liable to any third party, the Fund agrees to indemnify, defend and hold ASC and/or its employees harmless.

- If ASC or any of its employees are named as defendant in any action where the plaintiffs case involves a claim and there are no allegations of errors, omissions, torts, intentional torts or other negligence on the part of ASC, the Fund will assume defense of the action on behalf of ASC and indemnify and hold ASC harmless from any judgment rendered as a result of the action.

ASC and the Fund mutually agree:

- The contract shall be construed and interpreted in accordance with the laws of the State of Tennessee.
- The contract covers claim service for the Fund in the United States of America; and any gross receipt tax or assessments in those where levied will be in addition to the service fee.
- The contract represents the entire understanding of ASC and the Fund and supersedes all prior oral and written communications between the parties as to the subject matter; and neither this contract, nor any provisions of it may be amended, modified or waived except in writing signed by a duly authorized representative of ASC and the Fund.
- To not employ a person who has been employed by the other party at any time during the term of the contract, unless the person to be employed has not been employed by the other party during the immediate preceding six (6) months or unless the hiring party has obtained the other party's prior written consent.
- During the terms of the contract ASC will store at its expense, closed files for a period of three (3) years. After this period, files will either be returned to the Fund or stored by ASC at the Fund's expense.

The claim service fee for the contract in effect during the examination and the subsequent period is based on a percentage of the Fund's earned premiums. In the event that there is any material change to the method of premium calculation that causes the earned premium for the same members to decrease or increase greater than ten percent (10%), ASC reserves the right to renegotiate their fees accordingly for the remainder of the contract period. At the end of the annual policy period, adjustments are made based on the actual discounted standard premium as developed by actual audit of member's payroll for that period.

Administrative Service Agreement (Willis Pooling)

On September 1, 1994, the Fund entered in a service company agreement with Public Entities National Company (PENCO), an east Tennessee corporation and subsidiary of Willis Corroon Corporation with its principal office in Nashville, Tennessee. The contract term was for an initial three (3) years period with an automatic extension for future one (1)

year terms, unless ninety (90) days prior written notice is given by either party to terminate the contract. On January 9, 2001, the Tennessee Department of Commerce and Insurance received notification from PENCO that as a result of a corporate sell off of the PENCO name, PENCO would be changing its name to Willis Pooling. As of the date of this report, the above contract is still in effect with Willis Pooling. The current contract is effective until April 1, 2007, with a provision for an automatic extension for future one (1) year terms. Listed below is a summary of the contract's provisions:

Services to Provide:

- Administrative and data services, including collection of all premiums due from the members of the Fund; the preparation of various monthly, quarterly, and annual reports as required by the members, the Board of Trustees, reinsurance carriers, or the Tennessee Department of Commerce and Insurance;
- Loss control services;
- Marketing of the Fund to prospective members;
- Assist the Fund in obtaining reinsurance

Other key provisions:

- The Fund agrees to not appoint or recognize any other service company or broker for the program and/or for any insurance coverage provided for in the contract during the term of the contract.
- The Fund agrees to pay the service company compensation based on a percentage of the Fund's premiums earned.
- The service company shall retain the entire commissions accruing from placement of any primary or excess insurance coverage written for the Fund.
- The service company has the right to assign this agreement, or any portion thereof, to any other subsidiary or affiliate of Willis Corroon Corporation which is qualified to do business in the State of Tennessee.
- The contract lists provisions for non-renewal of insurance coverage and gives the service company as much as one hundred eighty (180) days beyond expiration of any insurance coverage to present an alternate proposal or proposals. During the 180 day period the agreement remains in full force. If the proposal is accepted by

the Fund, the agreement will continue in full force unless otherwise sooner terminated.

Addendums to the Contract:

Services to be provided are the same as listed in previous contracts with the addition of a new requirement to provide administrative and data services as required by NCCI.

A hold harmless paragraph is added which states in summary that the service company will hold the Fund harmless from loss, cost, or expense incurred as a result of Service Company's negligence unless the negligent act or wrong is committed by a Fund employee or a contractor other than the service company.

Administrative Subcontractor Agreement (Fortier Loss Control)

On April 1, 2000, the Fund entered into a "Subcontractor Agreement" with Fortier Loss Control Consultants, Inc. of Nashville, Tennessee, to provide loss control services. The initial contract was for a one (1) year period ending March 31, 2000. A new contract was executed at the start of each fiscal year, and as of the date of this report, the contract is still in effect. Listed below is a summary of the contract's key provisions:

Services to Provide:

- Field safety inspection and consultative services to members of the Fund.
- Written inspection reports to members inspected with a copy furnished to the Administrator of the Fund.

Other Key Provisions:

- Fortier Loss Control agrees that all letters, reports, and correspondence regarding the service is the property of the Fund and shall be returned to the Fund upon termination of the agreement.
- Fortier Loss Control will perform services as an independent contractor; not as an agent or employee of the Fund; and shall have no authority to negotiate any contract on behalf of the Fund.
- Fortier Loss Control will hold in a fiduciary capacity for the benefit of the Fund, all secret or confidential information, knowledge, or data relating to the Fund or the Fund members. Fortier Loss Control will not, without prior written consent of the

Fund, communicate or divulge any information, knowledge, or data to anyone other than the Fund and those designated by it.

- The Fund agrees to pay Fortier Loss Control compensation in an amount equal to a percentage of the Fund's premiums earned.

- The Fund may terminate the agreement immediately upon the occurrence of "cause". Cause includes deliberate refusal to perform material services, negligence in performing material services, breach of material provisions, or acts of willful or gross misconduct.

- Fortier Loss Control may terminate the agreement with thirty (30) days written notice.

- The agreement can not be assigned by Fortier Loss Control without prior written consent of the Fund.

- The agreement shall be governed by and construed in accordance with the laws of the State of Tennessee, and each party agrees to submit to the jurisdiction of the courts of the State of Tennessee.

- Fortier Loss Control shall indemnify and hold harmless the Fund, from and against any and all claims, damages, losses and expenses arising out of or resulting from performance of Fortier Loss Control's work under the contract, provided that any claim, damage, loss and expense is attributable to bodily injury, sickness, disease, or death, or injury to or destruction of tangible property, but only to the extent caused by proven or alleged negligent acts or omissions of Fortier Loss Control or its employees.

- The Fund shall indemnify, defend and hold harmless Fortier Loss Control from any and all costs, demands, lawsuits, liabilities, damages, fines, penalties and attorney's fees suffered by or incurred by Fortier Loss Control resulting from or arising out of any breach of the agreement by the Fund or the negligence or willful misconduct of the Fund.

- Fortier Loss Control shall maintain errors and omissions and/or professional liability insurance policies providing protection to the Fund to cover loss by reason of negligence on the part of Fortier Loss Control providing services pursuant to the agreement. Fortier Loss Control shall name the Fund as an additional insured on the policy which shall be evidenced on the certificate of insurance to be delivered to the Fund.

Royalty Agreement

During the period of examination, the Fund had no royalty agreement in effect with ABC; however, as a gesture of goodwill, the Fund makes an annual voluntary contribution to ABC with the amount determined each year by the Fund's Board of Trustees. Past annual contributions have ranged from thirty thousand dollars ($30,000) to fifty thousand dollars ($50,000).

Investment Policy

Tenn. Code Ann. § 50-6-405(c)(2) states:

> Notwithstanding any other law or rule to the contrary, funds not needed for current obligations may be invested by the Board of Trustees in "Tennessee securities" as defined in § 56-4-210(b). The Board of Trustees of each workers' compensation pool shall adopt an investment policy. Such policy shall address credit, quality of investments, maximum maturity of investments and such other matters as the Board of Trustees deems appropriate

During the course of examination, it was determined that the Fund has an informal investment policy that accomplishes the Fund's investment objectives, but has not adopted a formal written investment policy that addresses the criteria described above. Minutes from Board of Trustees meetings show that the status of the Fund's investment and bank accounts are routinely discussed, and that the Fund would on occasion invite the Bank Investment Manager to address the Board of Trustees concerning investments. All of the Fund's investments are in "Tennessee Securities" as defined by Tenn. Code Ann. § 56-4-210(b). Fund investments are of high quality with well distributed maturity dates.

Investment/Custodial Agreement

During the period of examination, the Fund's investments were managed by First Tennessee Bank from January 1999 through December 2003, and later by National Bank of Commerce (NBC) from December 2003 through the date of examination. A copy of the Fund's investment management/custodial agreement on the closed account with First

Tennessee Bank was requested but none could be found.

Although as of the date of this examination the Fund was party to an investment/custodial agreement with NBC, the agreement has since as a result of merger been transferred to the SunTrust Bank. As of the date of this examination report the custodial agreement with SunTrust Bank remains in effect. This agreement appoints NBC (now SunTrust Bank) as the investment management agent, custodian, and attorney-in-fact to hold and manage the money, securities, other property and interest in property which the Fund delivers to its investment management account at the bank. The agreement directs the bank to buy, sell, execute, accept, hold, manage in accordance with mutually agreed upon investment objectives, and deliver assets for the account.

Investment Management Agreement

The Fund executed an investment advisory agreement with Commerce Capital Management, Inc. on November 25, 2003. The agreement gives Commerce Capital Management, Inc., discretion to supervise and direct, on a continuing basis, as agent and attorney-in-fact on behalf of the Fund without prior consultation, the investment of all assets, subject to the limitations the Fund may impose by written notice and according to the Fund's investment policy. The agreement names the Fund's Investment Policy as an attached exhibit, however no policy was found to be attached.

NCCI Affiliation Agreement

On January 1, 2003, the Fund entered into an "Affiliation Agreement" with NCCI for a term of five (5) years. The Agreement, which is signed by the Fund Administrator, provides the Fund a license to use various NCCI filed rating systems and plans, including loss costs/rates and other products and services. The Agreement also includes a third-party administration/servicing company agreement signed by a representative of Willis Pooling granting the service company authority to act through, in concert with, or for the

benefit of the Fund in undertaking and performing certain functions required under the Agreement.

Premium Refunds

Pursuant to Tenn. Comp. R. & Regs., 0780-1-54-.16(1) , self-insured workers' compensation pools are allowed to provide refunds to the members of the pool when there is an excess amount of premium above what is necessary to fund all obligations for that fund year. The Board of Trustees must declare the refund not less than twelve (12) months after the end of the fund year; and if the refund is declared, ten percent (10%) of the refundable amount must be retained by the pool for an additional one (1) year period in order to cover any claims obligations that may not yet have been reported or developed. The following table is a summary of the refunds declared since inception of the Fund through the date of this examination along with the corresponding date of prior approval by the Tennessee Department of Commerce and Insurance:

Fund Year(s)	Date of Board of Trustees Approval	Refund Amount	Date of Approval by the Tennessee Department of Commerce and Insurance
1995,1996	03/05/97	$1,000,000	03/14/97
1996	02/25/98	500,000	03/04/98
1997	04/29/98	500,000	07/02/98
1997	11/19/98	500,000	12/02/98
1998	02/23/00	300,000	03/08/00
1996,1998	02/16/01	200,000	03/09/01
1995,1996,1998	02/18/02	200,000	03/13/02
1995, 1996,1998	03/07/03	250,000	03/19/03
1996,1998,2002	02/25/04	300,000	03/03/04
	Total	$3,750,000	

The above premium refunds in general were distributed to members who participated in the fund years as a credit on their next premium due with the Fund paying all premium

taxes due on the credit return. If the refund was due a member who was no longer with the Fund, a cash payment was made to the recipient.

Fidelity Bonds

Tenn. Comp. R. & Regs., 0780-1-54-.04(2)(f) and (2)(g) require the administrator and service company to maintain a fidelity bond in a form and amount acceptable to the Commissioner of the Tennessee Department of Commerce and Insurance. During the period of examination and the period subsequent to the examination, the following fidelity bond coverages were confirmed:

Service Company	Insurer Affording Coverage	Type Coverage/ Aggregate Limit
ASC	-Atlantic Mutual Insurance Company -National Union Fire Insurance Company	General Liability/$2,000,000 Automobile Liability/$1,000,000 Excess Umbrella Liability/$10,000,000 Workers' Comp/$1,000,000 Directors&Officers/$5,000,000 Errors &Omissions/$10,000,000 Crime Coverage/$5,000,000
Willis Pooling	-Illinois National Insurance Company	General Liability/$1,000,000
	-Lloyds of London, XL Europe Ltd, AIG, and Others	Errors & Omissions/ $5,000,000
Fortier Loss Control	-The Hartford -Gresham & Associates	General Liability/$2,000,000 Automobile Liability/$1,000,000 Workers'Comp/$500,000 Professional Liability/$1,000,000

The Fund maintained directors and officers insurance covering each Trustee and the Fund's Administrator. During the examination period this insurance was maintained through Royal Indemnity Company with a liability aggregate limit of one million dollars ($1,000,000), and a deductible of fifteen thousand dollars ($15,000) per each loss. During the period subsequent to the examination, the above insurance was maintained through Landmark American Insurance Company with a liability aggregate limit of one million

dollars ($1,000,000), and a fifteen thousand dollar ($15,000) deductible. In addition, the Fund maintains commercial crime insurance covering the Fund's Board of Trustees and Administrator. This coverage, which is maintained through Travelers Casualty and Surety Company, has an aggregate limit of one hundred thousand dollars ($100,000) with a one thousand dollar ($1,000) deductible. All companies providing coverage are licensed to do business in the State of Tennessee or are approved foreign surplus lines companies in Tennessee.

Statutory Deposit

Pursuant to Tenn. Comp. R. & Regs., 0780-1-54-.04(2)(b), workers' compensation pools are required to maintain either a security deposit, a surety bond, or a financial security endorsement on file with the Tennessee Department of Commerce and Insurance in an amount approved by the Commissioner of the Tennessee Department of Commerce and Insurance. This security which is required for a workers' compensation pool to obtain and maintain self-insured status is for the sole purpose of paying workers' compensation claims and associated expenses, if the Fund fails to pay the benefits in which it is legally obligated to pay. The amount of the security is prescribed by the Commissioner and is based on factors such as size, years in existence, types of employment, and other relevant factors. Based on the above, the Fund was directed by the Commissioner to maintain a bond in the amount of five hundred thousand dollars ($500,000). To satisfy this requirement, the Fund obtained on January 1, 1995, a surety bond in the amount of five hundred thousand dollars ($500,000) with Frontier Insurance Company. This surety bond remained in force until it was cancelled by the insurer on March 31, 2001. On March 31, 2001, the Fund entered into a depository agreement with the Tennessee Department of Commerce and Insurance maintaining a five hundred thousand dollar ($500,000) security deposit in the form of bonds backed by the full faith and credit of the State of Tennessee. These bonds are maintained in an escrow account managed by NBC, (now the SunTrust Bank) with individual securities, which are replaced by new securities of the same value and backing as they mature. The custodianship of the securities in this account is covered

by a State of Tennessee Self-Insurer Form B Custodian Affidavit and Depository Agreement.

Market Conduct Activities

Marketing

The Fund's primary emphasis with marketing is to the membership of ABC. The Fund maintains contact with the membership by attending and making presentations at chapter meetings in the three (3) ABC regions (East, Middle, & West). As a result of this effort, current members have assisted the Fund in identifying and approaching new prospects for membership who share the Fund's goals and objectives.

The Fund also uses several other marketing sources:

- The Fund conducts marketing and self promotion through the Fund's website: www.abcsif.com. Within this website is adequate information about the Fund's origination history and business purpose, management structure, member guidelines, claims handling process, loss control services, rate information and current participant listing. Also included are links to printable documents for applications and brochures.

- The Fund makes use of brochures and business postcards that are sent to prospective member companies. The items list the Fund's origination, history, business purpose, and member requirements. In addition, it outlines details of how the Fund will benefit prospective members and provides pertinent contact information on how to learn more about the Fund. The business postcard lists growth and premium increase percentages as well as reasons for selecting the Fund.

- The Fund also utilizes the services of independent agents to market the Fund to the ABC membership. Agents are paid on new and renewal premiums using a sliding scale with agents receiving a commission of seven and a half percent (7.5%) on new members during the first year; a commission of five percent (5%) during the second year; and a commission that increases by one quarter percent (0.25%) per year thereafter to a maximum of seven and a half percent (7.5%). The commissions are paid out on a quarterly basis.

Underwriting

The Fund utilizes the services of Willis Pooling to assist with establishment of premium underwriting guidelines and development of actuarial projections used by the Fund. The following requirements and guidelines which were established by the Fund's Board of Trustees must be met in order to become a member of the Fund:

- Be a member in good standing of ABC.
- Have annual premium of twenty thousand dollars ($20,000) or more. Minimum premium is twenty thousand dollars ($20,000).
- Have been in business as a commercial contractor or equipment dealer for at least three years.
- Have an average loss ratio for the last four (4) years in the range of sixty five percent (65%) or less.
- NCCI Modification of one and a quarter (1.25) or less.
- Be approved for membership by the Fund's Board of Trustees, the Tennessee Department of Commerce and Insurance, and Midwest Employee Casualty Company or excess carrier, if applicable.
- Must provide a completed Association for Cooperative Operations Research and Development (ACORD) Applicant Information Section and ACORD Workers Compensation Application.
- Must provide clear copies of current and prior year experience modification worksheets, the most recent expired year's payroll audit (optional) and a clear copy of the current policy declarations sheet showing payrolls by class (optional).
- Must provide most current audited or reviewed financial statements. If not available, provide a clear and complete copy of the Franchise and Excise Tax Returns.
- Must provide currently valued loss runs for the current and four (4) prior years.
- Must provide supplemental workers compensation application.
- Must not be prohibited in any category.
- Must agree, as part of the application process, to comply with all loss control/safety requirements, claims consultation requirements, restrictions, etc. as determined by the Board of Trustees.
- Must provide an approved safety, workers' compensation and loss prevention program.

- Facility and/or job site inspections on all initial members are required within thirty (30) days of binding. Prospects not surveyed prior to binding will be bound subject to favorable loss control.

Once all above requirements and underwriting guidelines are met and approval is granted by the Board of Trustees, the new member must provide payment of twenty-five (25%) of the annual premium before the membership becomes effective. The Tennessee Department of Commerce and Insurance will then confirm or deny membership in the pool.

Rating

Tenn. Comp. R. & Regs., 0780-1-54-.15 requires the Fund to adhere to a uniform classification system, uniform experience rating plan, and manual rules approved by the Commissioner of the Tennessee Department of Commerce and Insurance. Pursuant to Tenn. Code Ann. § 56-5-320, the Commissioner has prescribed that the uniform classification system to be used by self-insured trusts is to be in accordance with the rating procedures published by NCCI. The Fund is also required to file with the Commissioner a multiplier and supporting information which shall apply to the most recently approved, currently effective advisory prospective loss costs. All multipliers are required by Tenn. Code Ann. § 56-5-306 to be actuarially justified and shall be certified by a member in good standing of the Casualty Actuarial Society.

Examination procedures included verification of the Fund's use of approved rating procedures and manuals during the period of examination. Per NCCI procedures, self-insured trusts are required to apply its approved multiplier to advisory loss costs to develop the manual rates for specific class codes. Manual rates for each class code are then multiplied by the basis of premium (audited payroll per one hundred dollars) for each class code to calculate manual premium. Based on eligibility requirements, a drug free workplace discount of five percent (5%) can then be applied to total manual premium for all class codes to calculate subject premium. An experience modification factor is applied to each member's subject premium to calculate modified premium. Scheduled credits and debits are applied to subject premium to determine standard premium. A premium volume

discount is then applied in order to determine final premium. Premiums are billed by requiring a down payment of twenty-five percent (25%) of the estimated annual premium with the balance paid in nine (9) additional consecutive monthly payments. The Fund's method and setting of rates during the period of this examination was found to be in compliance with the above except as noted in the "Recommendations" section of this report.

Forms

A signed completed application, Board of Trustees approval letter and Indemnity Agreement are provided to the Tennessee Department of Commerce and Insurance for approval before entry into the Fund and for evidence of membership and coverage. Examination procedures included verification of the Fund's use and proper execution of approved forms for each of its members.

Upon approved entry into the Fund, new members receive a certificate of insurance, premium rating calculation form and premium invoice from Willis Pooling, and claim filing information from ASC. Agents who assist the Fund in membership retention are provided an operations manual that outlines Fund benefits and procedures. Agents are kept abreast of Fund operations by the Fund Administrator and the service companies and are encouraged to express their concerns and ideas on marketing of the Fund.

Claims

The Fund's practices pertaining to the handling of loss settlements were reviewed by the examiners by sampling both open and closed claim files. The sample consisted of claims paid, unpaid claims and those in litigation. The review disclosed that the Fund in general settled its claims properly after receipt of the necessary documents, however there were some instances identified where the Fund appears to be in non-compliance with policy provisions and Rules (see the claims comment in "Recommendations" section of this report on page 46 of this report).

Policyholder Complaints

The Fund does not have any formal written complaint procedures nor does it maintain a formal complaint register. Inquiries made to the Consumer Insurance Services section of the Tennessee Department of Commerce and Insurance indicated there were no regulatory concerns with the Fund during the period under examination. Disputed claims or questions concerning workers' compensation benefits can be addressed to a Workers' Compensation Specialist with the Tennessee Department of Labor and Workforce Development.

Anti-Fraud Plan

As of January 1, 1997, the Fund had in place an anti-fraud plan that complied with the Tennessee Workers' Compensation Reform Act of 1996. Each year in accordance with Tenn. Code Ann. § 56-47-112, the Fund submitted an anti–fraud summary report to the Tennessee Department of Commerce and Insurance summarizing the Fund's anti-fraud activities.

Excess of Loss Insurance

In accordance with Tenn. Comp. R. & Regs., 0780-1-54-.04(2)(c), the Fund has from its inception through the date of this report entered into a number of agreements with insurance carriers that provide excess of loss insurance. The policies were underwritten by companies authorized to do business in Tennessee and the policy forms in use were verified to have been filed with and approved by the Tennessee Department of Commerce and Insurance.

On March 31, 2004, the Fund had excess of loss insurance with Midwest Employers Casualty Company (MWECC). This MWECC policy sets the insurance carrier's specific limit for workers' compensation liability to the statutory maximum per accident, and sets the maximum limit the carrier will pay for the employer's liability (i.e. Fund liability) at one million dollars ($1,000,000) per accident (or each employee for disease). The policy sets

the specific retention (i.e. self-insured retention) at five hundred thousand dollars ($500,000) per accident (or each employee for disease) with an additional one (1) time corridor deductible of two hundred fifty thousand dollars ($250,000). These limits in effect make the Fund initially responsible for the first five hundred thousand dollars ($500,000) of each accident plus some or the entire two hundred fifty thousand dollars ($250,000) corridor deductible until the corridor deductible is exhausted. The policy sets the Funds minimum aggregate retention at 4.832 per one hundred dollars ($100) of payroll (which is approximately ninety-three percent (93%) of premium for the current policy period). The carrier's maximum aggregate limit is set at five million dollars ($5,000,000). The policy also provides for the continuation of coverage in the event the Fund becomes insolvent during the policy period.

The examination of excess of loss insurance policies in effect subsequent to the examination period show that the Fund continues to have coverage provided by MWECC; however in the current policy with MWECC, the Fund agreed to significant changes in the coverage. The Fund's policy with an effective date of April 1, 2005, and an expiration date of April 1, 2006, increased the self-insured retention to seven hundred fifty thousand dollars ($750,000) per accident with a one time corridor deductible of two hundred fifty thousand dollars ($250,000); increased the Fund's minimum aggregate retention to 5.4076 per one hundred dollars ($100) of payroll; and decreased the carrier's maximum aggregate limit to three million dollars $3,000,000. These new limits have exposed the Fund to payment on the first excess claim to one million dollars ($1,000,000) before coverage begins on the specific excess loss policy. In addition, the raising of the minimum aggregate retention and the lowering of the carrier's maximum aggregate limit has further narrowed the Fund's aggregate excess loss coverage. The above changes in insurance coverage which have increased the amount the Fund is at risk were approved by the Fund's Board of Trustees.

Based on a report prepared by the Fund's actuary, the Fund experienced six (6) claims during the period 1998 through 2001 in which paid losses exceeded the specific retention of the respective excess policies. The Fund's specific retention was two hundred

fifty thousand dollars ($250,000) for the years 1998 through 2000, and increased to three hundred thousand dollars ($300,000) in 2001. From 2002 through 2005, the specific retention increased from three hundred thousand dollars ($300,000) to seven hundred fifty thousand dollars ($750,000) and included the addition of a corridor deductible that ranged from one hundred fifty thousand dollars ($150,000) to the current amount of two hundred fifty thousand dollars ($250,000). During this period, the Fund has not experienced any claims in which paid losses exceed the specific retention; however, the Fund does anticipate that incurred losses on a 2003 fund year claim will exceed the specific retention. The Fund exceeded its minimum aggregate retention in fund year 2000. The minimum aggregate retention for fund year 2000 which is 3.066 per one hundred dollars ($100) of payroll was calculated to be two million one hundred eighty-four thousand five hundred dollars ($2,184,500) and the Fund recorded losses incurred in the same year of two million three hundred thirteen thousand four hundred thirty-four dollars ($2,313,434).

Loss Experience

The following table depicts the ratio of incurred losses valued as of June 3, 2004, to earned premium revenue for the periods indicated below:

*Fiscal Year	Premiums Earned	Losses & ALAE	Und. Ratio	Sell, Gen. & Admin. Exp.	S,G, & A Exp. To Premium	Investment & Other Income	Combined Loss Ratio
1995	$ 2,587,732	$ (1,924,014)	74.4%	$ (578,725)	22.4%	$ 45,738	94.9%
1996	4,745,567	(1,779,306)	37.5%	(1,024,357)	21.6%	139,606	56.1%
1997	3,964,112	(2,147,532)	54.2%	(1,377,647)	34.8%	184,787	84.3%
1998	3,307,161	(1,219,596)	36.9%	(1,261,018)	38.1%	183,573	69.5%
2000	3,665,271	(2,412,589)	65.8%	(1,148,310)	31.3%	206,033	91.5%
2001	2,997,369	(2,001,553)	66.8%	(955,871)	31.9%	170,253	93.0%
2002	3,139,914	(2,067,489)	65.8%	(1,032,743)	32.9%	182,637	92.9%
2003	4,330,430	(2,455,642)	56.7%	(1,570,135)	36.3%	201,763	88.3%
2004	5,620,330	(3,215,825)	57.2%	(2,055,961)	36.6%	149,568	91.1%

(*) Note: The Fund changed its fiscal year ending from December 31 to March 31 during calendar year 2000; therefore, no financial statements were produced for December 31,1999, and the 2000 financial statements are for 15 months.

The updated analysis as presented in the March 31, 2005, actuarial report indicates the

estimated ultimate incurred losses illustrated above have decreased and will ultimately have a positive effect on the Fund's financial position.

Accounts and Records

Financial records and reports are maintained and produced primarily by ASC, the Fund's service company. The Fund contracts with an independent actuarial firm to periodically perform an evaluation of loss and loss expense reserves. The Fund retains an independent accounting firm to prepare and perform an audit of the Fund's financial statements and to prepare the Fund's federal income tax return.

During the course of this examination, such tests and audit procedures were performed as were deemed necessary to verify the accuracy of the Fund's accounts and records for the period under examination. General ledger trial balances were reconciled with the financial statements and all were reviewed for completeness of disclosure and conformity to GAAP as currently permitted by the Tennessee Department of Commerce and Insurance.

The accounts and records examined conform to the above requirements and in general appear to reflect properly the operations of the period under examination and the status of the Fund as of the date of this report.

Litigation, Contingent Liabilities and Subsequent Events

The Fund is named as defendant in various legal actions arising from workers' compensation claims. The Fund upon estimating the reserves for losses and loss adjustment expenses provides for these in their financial statements. From the data made available during the course of this examination, it would appear that the Fund had no matters of pending litigation which would adversely affect its financial condition at March 31, 2004, other than these which arose out of the ordinary course of business. The Fund reported that it had no other agreements or pending matters of contingent nature that would materially affect its financial position or operating results at March 31, 2004.

Subsequent Events

Premium Refund Plan

On July 11, 2005, the Tennessee Department of Commerce and Insurance approved a distribution of premium refunds to members from the 2002 fund year in the amount of two hundred fifty thousand dollars ($250,000). The Fund's Board of Trustees had approved the distribution on February 23, 2005. The terms of the distribution are as follows:

- Forty percent (40%) is based on premium size - a pro-rata amount based on the percentage the member paid in premiums for the policy year under consideration as it bears to the total premiums paid by all eligible Fund members for the same year.
- Forty percent (40%) is based on underwriting profits – a distribution to members who qualify by having a loss ratio for the policy year under consideration that equals 40% or less. The pro-rata distribution is based on the percentage the member paid in premiums for the policy year under consideration as it bears to the total premiums paid by all eligible Fund members for the same year.
- Twenty percent (20%) is based on longevity – a pro-rata amount based on the total number of months each member has participated in the Fund from the member's initial joining date through the policy year under consideration.
- Member's eligible for the above distributions are Fund members who were insured for any length of time during the year under consideration for the premium return.

Custodian Agreement

The Fund's custodial agreement in effect as of the examination date stated that NBC (now SunTrust Bank) held investments on behalf of ABC. Subsequent to the date of examination, the Fund executed an addendum to the custodial agreement that now reflects the account holder as ABC Workers' Compensation Self-Insurance Fund. This addendum was signed on September 20, 2005, between the Fund and SunTrust Bank.

Member Premium "Loss Credit"

On September 12, 2005, the Fund submitted a request to the Tennessee Department of Commerce and Insurance requesting approval to deviate from NCCI guidelines in the Fund's use of a debit/credit policy in the calculation of member premiums. As of the date of this report the request was pending.

Financial Statement

There follows a balance sheet and a statement of operations as of March 31, 2004, together with a reconciliation of members' equity, as established by this examination.

Balance Sheet

Assets:		
Cash and cash equivalents	$	343,669
Marketable debt securities		4,970,933
Marketable debt securities held in trust		509,794
Premiums receivable		434,517
Interest receivable		87,212
Retention receivable		312,593
Prepaid expenses		1,773
Deferred income taxes		138,000
Total assets	$	6,798,491
Liabilities:		
Unpaid losses and loss adjustment expenses	$	4,400,000
Premium refunds payable		686,439
Accrued expenses and fees		278,831
Unearned premiums		682,199
Total liabilities		6,047,469
Members' Equity:		
Policyholder' surplus (deficit)		751,022
Total liabilities and members' equity	$	6,798,491

Statements of Operations, Comprehensive Income and Members' Equity

Revenues:	
Premiums earned	$ 5,620,330
Interest income and other	149,568
Total revenues	5,769,898
Expenses:	
Losses and loss adjustment expenses	3,215,825
Excess insurance premiums	539,738
Commission expense	390,435
Administration fees –ASC	352,393
Return of premiums (Dividends)	300,000
General and administrative	224,854
Management fees – Affinity (Willis Pooling)	281,011
Premium tax expense	134,892
Loss control fees – Fortier	132,638
Total expenses	5,571,786
Income before income taxes	198,112
Income tax expense	26,000
Net Income	172,112
Members' equity at beginning of year	578,910
Members' Equity At End Of Year	$ 751,022

Reconciliation of Members' Equity

(Fund Balance)

	March 31, 2000	March 31, 2001	March 31, 2002	March 31, 2003	March 31, 2004
Members' Equity at Beginning of Year	$ 279,572	$ 289,977	$ 300,175	$ 322,494	$ 578,910
Net Income (Loss) after taxes, but before distributions to members	310,405	210,198	222,319	506,416	472,112
Distributions from or (return of premiums to) members during the year.	(300,000)	(200,000)	(200,000)	(250,000)	(300,000)
Total members' equity	$ 289,977	$ 300,175	$ 322,494	$ 578,910	$ 751,022

Comments

Premium Refunds

Pursuant to Tenn. Comp. R. & Regs., 0780-1-54-.16, self-insured workers' compensation pools are allowed to provide refunds to the members of the pool when there is an excess amount of premium above what is necessary to fund all obligations for that fund year, but payment of a refund based on a previous fund year shall not be contingent on continued membership in the group after that fund year. During the period under examination the Fund made multiple refunds which were contingent on continued membership in the Fund. They were as follows:

Paid for Fund Year	BOT approval	Amount	Dept. approval
1996	02/25/98	500,000	03/04/98
1997	04/29/98	500,000	07/02/98
1997	11/19/98	500,000	12/02/98
1998	02/23/00	300,000	03/08/00
1996,1998	02/16/01	200,000	03/09/01
1995,1996,1998	02/18/02	200,000	03/13/02
1995, 1996,1998	03/07/03	250,000	03/19/03
	Total	$2,450,000	

The Fund's membership that participated in these refunds was limited by the following criteria:

- Member's eligible for the distributions are those active Fund members with no breaks in service between the year under consideration and the year the refund is issued.
- A break in membership will result in a new anniversary date and all time prior to the new anniversary date will not be considered.

The criteria for these payments was in violation of Tenn. Comp. R. & Regs., 0780-1-54-.16(2) because eligibility was limited to former members who had not withdrawn from the Fund at time of payment of the refund. The Fund sought prior approval, and the Tennessee Department of Commerce and Insurance did approve the methodology for

these refunds prior to their payment by the Fund. These methodologies should not have been approved by the Tennessee Department of Commerce and Insurance as they were in violation of Tenn. Comp. R. & Regs., 0780-1-54-.16.

Establishment of a Line of Credit

The Fund in conjunction with its investment manager/account custodian established a set of procedures for the management of the Fund's investment accounts that are aimed at satisfying short term cash requirements by preventing the premature liquidation of bonds. An element of this strategy was the establishment of a line of credit to be used as a third layer of liquidity before the Fund would need to liquidate bonds. Although the Fund's business decision was a legitimate effort to prevent premature liquidation of assets, the Fund should be aware that no monies can be borrowed in the Fund's name without obtaining prior approval from the Commissioner of Tennessee Department of Commerce and Insurance. Tenn. Comp. R. & Regs., 0780-1-54-.07(2)(b) specifies that the Board of Trustees shall not borrow any monies in the name of the Fund except in the ordinary course of business without first advising the Commissioner of the nature and purpose of the loan and obtaining prior approval from the Commissioner. Conformation was provided by SunTrust Bank that, during the period of examination and as of the date of this examination report, the Fund had not borrowed any money against this line of credit.

Recommendations

Indemnity Agreement

The Fund's Indemnity Agreement states that the Fund shall operate on a fiscal year from 12.01 a.m., January 1 to midnight of December 31 of each year. This statement is incorrect since the Fund changed its fiscal year to 12.01 a.m. April 1 to midnight March 31 as of approval by the Board of Trustees on February 23, 2000. The Indemnity Agreements signed by the members do not list the Fund's correct fiscal year. It is recommended that the Fund amend its indemnity agreement to list the correct fiscal year and that the amended agreement be submitted to the Tennessee Department of Commerce and

Insurance in accordance with Tenn. Comp. R. & Regs., 0780-1-54-.04(3). It is also recommended that all current and former members of the Fund be notified of the correction.

Membership Files

Tenn. Comp. R. & Regs., 0780-1-54-.08 specifies that the application for membership and its approval shall be maintained as permanent records of the Board of Trustees. The review of a sample of membership files revealed several of the applications for membership did not contain the Chairman's signature as proof of Board of Trustee approval. In addition, the Indemnity Agreement in five (5) member files [approximately nineteen percent (19%) of the sample] had not been signed by the Fund's Chairman. It is recommended that the Fund conduct a comprehensive review of all files and has the Chairman sign any unsigned Indemnity Agreements and Membership Applications. The Fund should also take actions to ensure all required documents for membership in the Fund are properly completed before membership in the Fund is granted by the Board of Trustees.

Election of Officers

The Fund's bylaws state that the Board of Trustees from their own members and by majority vote shall elect a Chairman and a Vice Chairman to serve one (1) year terms, and the Vice-Chairman may serve successive terms. A review of the minutes from Board of Trustees meetings from 1994 through 2004 revealed there was no documentation therein that indicated the above elections were held. It is recommended that elections of Fund's officers be conducted in accordance with the bylaws, and that all elections are properly recorded in the minutes of the Board of Trustees meetings.

Additionally, on March 24, 2004, the Board of Trustees voted to change the term of the Chairman of the Board of Trustees to two (2) years; however there is no evidence that this amendment which changed the bylaws on file with the Tennessee Department of Commerce and Insurance was ever submitted to the Tennessee Department of Commerce and Insurance in accordance with Tenn. Comp. R. & Regs., 0780-1-54-.04(3). It is recommended that any amendments to the Fund's bylaws be submitted to the Tennessee

Department of Commerce and Insurance in accordance with Tenn. Comp. R. & Regs., 0780-1-54-.04(3).

Investment Policy

Tenn. Code Ann. § 50-6-405(c)(2) specifies that the Board of Trustees of each workers' compensation pool shall adopt an investment policy and that the policy shall address credit, quality of investments, maximum maturity of investments and such other matters as the Board of Trustees deems appropriate. During the examination it was determined that the Fund had not adopted a formal investment policy as described by the above statute and it is therefore recommended that the Fund develop an investment policy in accordance with Tenn. Code Ann. § 50-6-405(c)(2).

Underwriting and Rating

Examination procedures included a review of the Fund's rating procedures for a sample of twenty-seven (27) of its members for the 2003 – 2004 policy years. Premium recalculations were performed and the Fund's adherence to approved rating procedures was verified. The following are comments about exceptions that were noted as a result of this examination:

Drug Free Workplace Premium Credit

Tenn. Code Ann. § 50-9-104 specifies the eligibility requirements for a five percent (5%) drug free workplace premium credit for an employer who has certified to the Tennessee Department of Labor and Workforce Development that a qualifying drug free workplace program has been established. The premium credit shall be applied to the policy pro rata as of the date of certification by the Tennessee Department of Labor and Workforce Development. The examiners noted four (4) exceptions to this statute. For the 2003-2004 policy years, the Fund allowed two (2) members (R.G. Anderson and Massey Construction) who were eligible to receive only partial credit to receive the full drug free workplace credit. Also, two (2) other members (Vic Davis Construction and Rouse Construction) were eligible to receive partial credit but were denied any credit by the Fund.

The Board of Trustees adopted a guideline whereby any member that has not been

certified seven (7) months out of the twelve (12) month policy period would not be eligible for any credit, and any member so certified would be entitled to the entire five percent (5%) credit. This policy is different from the statutes which provide for pro rata application regardless of the period the member is certified. It is recommended that the Fund revise their policy on drug free workplace premium credits in order to comply with Tenn. Code Ann. § 50-9-104, and make adjustments to these members' premium billings.

Premium Loss Credit

As noted earlier in this report, the Fund applies schedule-rating factors to members' premium which is done as follows:

> The loss ratio for each member shall be annually calculated using four (4) years of experience. These years shall not include the most recent policy year, but shall be years two (2), three (3), four (4) and five (5) ago. If a member has not been in the Fund long enough to have five (5) years experience with the Fund, the pre-Fund experience information gathered for the quote shall be used to calculate a ratio using years two (2), three (3), four (4) and five (5) ago. If a member's loss ratio using this method is less than thirty percent (30%), then the member qualifies for a ten percent (10%) premium credit. If a member's loss ratio is one hundred percent (100%) to one hundred fifty percent (150%), then an annual premium debit of ten percent (10%) shall be applied until the ratio drops to lower than one hundred percent (100%). If a member's loss ratio is one hundred fifty-one percent (151%) or higher, then the premium debit shall be twenty-five percent (25%) until it drops as described above. The debit policy only applies to renewals and not new business. The Board of Trustees of the Fund has the discretion to eliminate the debit based upon extenuating circumstances.

It is the opinion of examiners that based on our review, the Fund is consistent in the application of its schedule rating policy. However, there was one (1) isolated instance noted where a member that should have received a ten percent (10%) debit under the guidelines received no adjustment, and the file lacked supporting documentation to determine the reason. Additionally, the Board of Trustees acted within their discretion and granted approval for one (1) of the Fund members with a high loss ratio due to one (1) large claim to have their debit reduced from twenty-five percent (25%) to ten percent (10%). This Fund member was also serving as a member of the Fund's Board of Trustees

at that time and appeared to have a conflict of interest; however the member abstained when the Board of Trustees voted for this decrease in their premium.

Although it is the opinion of the examiners that the above described rating procedure in use by the Fund is used consistently for its membership, it is considered inconsistent with rating procedures approved by the Tennessee Department of Commerce and Insurance. Pursuant to Tenn. Comp. R. & Regs., 0780-1-54-.15(1), the Fund is required to adhere to the rating procedures promulgated by the NCCI. Per the NCCI Experience Rating Plan Manual, the premium for a risk is allowed to be modified in accordance with a schedule rating table to reflect such characteristics of the risk that are not reflected in its experience. The schedule rating adjustments in use by the Fund are dependent solely on members' past experience and therefore do not comply with NCCI schedule rating guidelines. It is therefore recommended that the Fund adhere to established NCCI procedures in application of its schedule rating premium adjustments.

Per Bulletin issued by the Tennessee Department of Commerce and Insurance, self insured trusts that use manual rules dealing with schedule rating that are different than those of the NCCI must file and receive approval from the Commissioner of the Tennessee Department of Commerce and Insurance prior to their use. The Fund did not have Tennessee Department of Commerce and Insurance approval for the above procedure. It should be noted that subsequent to the date of examination, the Fund submitted a request to the Tennessee Department of Commerce and Insurance for approval of their rating plan.

Waiver of Subrogation Endorsement

The Fund included a waiver of subrogation endorsement for twenty (20) of the twenty-seven (27) members that were reviewed for the 2003 – 2004 policy years. The Fund charged two hundred fifty dollars ($250) per policy for this endorsement. Effective April 22, 2004, the Tennessee Department of Commerce and Insurance by Bulletin to all workers' compensation insurance carriers writing business in Tennessee, stated that a waiver of subrogation endorsement is permitted, but insurers may not apply a fee or charge in connection with the waiver. Subsequent to the date of the Bulletin, the Fund continued

to offer the endorsement but no longer charges a fee for it in accordance with Tennessee Department of Commerce and Insurance policy and NCCI procedures.

Small Deductible Policy

The Fund has a procedures manual for underwriting guidelines that includes a statement indicating small deductible policies are available to its members subject to vote by the Board of Trustees. Based on the examiners review, it appears that the Fund has not issued policies with small deductibles to its members. NCCI procedures state that small deductible plans are allowed but must be filed with the Tennessee Department of Commerce and Insurance for approval prior to their use, and the Fund has never filed such a request with the Tennessee Department of Commerce and Insurance. It is recommended that the Fund either remove this as an available policy to be written, or request the required approval from the Tennessee Department of Commerce and Insurance if they ever chose to issue policies of this type in the future.

Claims Payments

Examination procedures included a review of a sample of the Fund's claimant files and corresponding claims payments for losses and loss adjustment expenses for the period under examination. The Fund's adherence to Tennessee Statutes and Rules and Regulations was verified and exceptions that were noted are as follows:

Court Ordered Settlements

Included in the review of claims disbursements was a review of forty-two (42) claimants' files. Several of the claims reviewed by the examiners were settled in court or through the Tennessee Department of Labor and Workforce Development Mediated Settlements. It was noted by the examiners that a number of the court ordered judgments against the Fund incorrectly listed the judgment as being against someone other than the Fund. There were five (5) court ordered settlements which named a local government workers' compensation fund as the insurer and not the Group. Although the names were incorrectly listed in the legal documents, the Fund honored all obligations of its insured membership.

Late Payment of Medical Cost

Tenn. Comp. R. & Regs., 0800-2-14-.07, requires all medical costs owed under the Tennessee Worker's Compensation Law be paid within forty-five (45) days of receipt of bill or invoice. Examination procedures included a review of a random sample of sixty (60) medical payments made by the Fund in 2004 to determine compliance with this Regulation. Based on the results of our sample, twenty-two percent (22%) of the Fund's payments for medical costs exceed the forty-five (45) day requirement [thirteen (13) out of sixty (60) disbursements] and the Fund is in non-compliance with this Rule. It is therefore recommended that action be taken by the Fund to ensure payment of medical costs occur within forty-five (45) days in accordance with Tenn. Comp. R. & Regs., 0800-1-14-.07.

Medical Bill Review Fees

It has been the Fund's practice to have claims payments for medical bills reviewed by an independent third party for reduction to agreed upon network charges prior to their payment. Bills are typically paid at a discounted rate after their review and the Fund pays a fee for this service based on the amount of reduction.

The Fund used the services of three (3) different medical bill review companies during the period of our examination, all of which were arranged for by ASC, the Fund's claims service company. Beginning in February of 2000, services were provided by National Healthcare Resources, Inc. (NHRI). In May of 2002, services were provided by Concentra Integrated Services Inc. (CISI) which had merged with NHRI. In July 2003, the medical review service company was changed to Diversified Healthcare Services Inc. (DHSI) which was acquired by Fair Isaac (FI) in September 2003.

During the period of time the Fund utilized the services of NHRI/CISI, the Fund paid a fee equal to thirty-three percent (33%) of the savings realized through the discount process directly to NHRI/CISI, but there was never an agreement for these services. However, the Fund's service company did have an agreement with NHRI/CISI for a lesser amount of fees equal to five dollars ($5.00) per bill, twenty percent (20%) of the PPO savings and a ninety cents ($0.90) line and header charge to be billed to ASC for NHRI/CISI's services. When the Fund began using the services of DHSI, fees continued to

be paid at a rate of thirty-three percent (33%) of savings, but were instead paid directly to ASC, the Fund's service company. The Fund still had no contract for these services but ASC in turn paid DHSI/FI at their lower contract rate of twenty-two percent (22%) of savings and ninety cents ($0.90) a line and header charge.

The examiners reviewed twenty-four (24) medical bill review fees from our claims sample that were paid by the Fund to ASC for DHSI's services during the examination period. The bills that were discounted by DHSI [which totaled six thousand two hundred forty dollars and thirty-seven cents ($6,240.37)] were reduced by twenty and eight tenths percent (20.8%) [or one thousand two hundred ninety-eight dollars and forty cents ($1,298.40)] prior to payment by the Fund. Fees for this service which were paid by the Fund to ASC were equal to thirty-three percent (33%) of the savings, or four hundred twenty-eight dollars and forty-eight cents ($428.48). ASC was obligated to pay DHSI one hundred ninety-one dollars and sixty-one cents ($191.61) per the terms of their contract. Therefore, based on the items in our review, the Fund's service company, ASC, retained approximately fifty-five percent (55%) of the fees for medical bill review paid by the Fund. Subsequent to the date of examination on March 2, 2005, ASC by e-mail informed the Fund that they were lowering the Fund's medical bill review fees. The new fees reflected the actual cost charged by DHSI to ASC.

The examiners also noted that the Fund was not getting refunds from DHSI for medical bill review reconsiderations. When a medical bill that had previously been paid at a discounted amount was again submitted by the medical provider to be reconsidered, and the medical bill was subsequently approved by DHSI to be paid at a greater amount (additional payment to the provider), the Fund's review fee was still based on the original and inflated discount amount. This problem began when the Fund's service company, ASC, switched claims servicing software in 2003 and changed the medical bill review provider. It was assumed the new software would handle this transaction and that refunds were being netted out of monthly bills as they had in the past. When this problem was noticed, management of ASC began working to resolve this problem by manually adjusting medical bill review statements and updating claims software. ASC provided the examiners with a list generated by DHSI for reconsideration refunds owed to the Fund for the time

period from July 1, 2003, through December 31, 2004. The examiners compared this to ten (10) claimant files from the examination sample for claims and noted that only approximately fifty-one percent (51%) of the reconsideration refunds were identified by DHSI [three thousand two hundred fifty dollars ($3,250) out of six thousand three hundred eighty-three dollars and fifty-one cents ($6,383.51)]. It is recommended that the Fund continue to work with ASC and DHSI to ensure the Fund receives all refunds to which it is entitled and that procedures are created to prevent this problem in the future.

There has never been an agreement between the Fund and its service company or medical bill review company for services and related fees. The only evidence of such that was provided to the examiners was an e-mail dated March 2, 2005, notifying the Fund of the reduction in review service fees to reflect the actual charges by DHSI which was briefly discussed at one (1) of the Fund's Board of Trustees meetings. It is recommended that the Group and ASC execute a formal agreement for the provision of medical bill review services.

Premium Refund Plan

Tenn. Comp. R. & Regs., 0780-1-54-.16(2) requires all members be given a written description of the refund plan at the time of application for membership. Applications for membership in the Fund are taken by independent agents. The Fund provides the agents information on the premium refund plan, however it could not be confirmed from examination of member files that a copy of the Fund's premium refund plan is given to new members at the time of application. It is recommended that the Fund develop membership procedures that will allow for verification that members have been given written descriptions of the Fund's refund plan in accordance with Tenn. Comp. R. & Regs., 0780-1-54.16(2).

Fund Bylaws

Article X, Section 5 of the Fund's bylaws states that members may resign only upon written notice to the Board of Trustees at least sixty (60) days before the end of the current Fund Year, and that the resignation will become effective sixty (60) days after notice is

given. However, Tenn. Comp. R. & Regs., 0780-1-54-.08 provides that individual members in a self insurance pool may elect to terminate their participation in the pool at any time.

Article X, Section 5 of the Fund's bylaws also states that a resigning member will forfeit any and all rights to dividends in the Fund unless otherwise directed by the Tennessee Department of Commerce and Insurance. However, Tenn. Comp. R. & Regs., 0780-1-54-.08 further require that refund payment based on a previous fund year shall not be contingent on continued membership in the group.

Article X, Section 6 of the Fund's bylaws establishes grounds for termination of member's rights and privileges in the Fund by the Board of Trustees, which would be effective as of the date of the official cancellation notice to the Tennessee Department of Commerce and Insurance. It also states that no liability will accrue to the Fund or its remaining members from actions of terminated members occurring after the date of official cancellation notice. However, Tenn. Comp. R. & Regs., 0780-1-54-.08 (2) require the Fund to maintain coverage of each cancelled or terminated member for a period of thirty (30) days after such notice unless the pool is notified sooner by the Commissioner of Labor and Workforce Development that the cancelled or terminated member has procured workers' compensation insurance through an insurer, has become a licensed self-insurer, or has become a member of another pool.

It is recommended that the fund revise the bylaws discussed above to comply with Tennessee Rules and Regulations.

Unclaimed Property

The Fund has not submitted any unclaimed property reports to the State of Tennessee Treasury Department since its inception in 1995, and is holding funds which should have been remitted to the State of Tennessee in accordance with Tenn. Code Ann. § Title 66, Chapter 29. The Fund has not implemented formal policies and procedures for maintaining and reporting unclaimed property, and the absence of any policies has prevented the Fund's compliance with the statute. It is recommended that the Fund identify any escheatable amounts that should have already been remitted to the State of Tennessee and do so beginning with the next reporting period. It should be noted that the

Fund's management is already aware of this obligation and has taken steps to identify and report funds for purposes of compliance with Tenn. Code Ann. § Title 66, Chapter 29.

Reporting of Work-Related Injuries

During the period of examination, the Fund received numerous reports of injuries from employer members that were submitted as "Report Only" claim files. These were turned in by members as information only claims and no medical costs were incurred by the Fund. The Fund's practice is to retain these files for approximately two (2) years in case the injury does develop into a compensable claim.

The examiners reviewed a sample of "Report Only" claims files submitted from April 1, 2003, through March 31, 2005 and noted that many indicated medical treatment had been provided to the injured employee. However, no medical expenses were paid by the Fund; they all appeared to have been paid by the employer member without a request for reimbursement from the Fund. As a result, these claims were never reported to the Tennessee Department of Labor and Workforce Development nor were the related costs submitted to the NCCI for inclusion in the calculation of the employer's experience mod.

This is a violation of Tennessee Statutes which require notification to the Tennessee Department of Labor and Workforce Development of each and every accident resulting in a work-related death or personal injury. It is therefore recommended that whenever the Fund receives "Report Only Claim Files" that indicate medical expenses have been paid, enough information should be requested from the member employer to ensure the claim is properly reported to the Tennessee Department of Labor and Workforce Development and the NCCI.

Subsequent Events

Subsequent to this examination, revisions were published to Tenn. Comp. R. & Regs., 0780-1-54 (Self-Insured Workers' Compensation Pools) by the Tennessee Department of Commerce and Insurance with an effective date of November 14, 2005. In addition, Tenn. Comp. R. & Regs., 0780-1-81 (Administration of Self Insurance Workers' Compensation Programs by Single Employers or Pools) was published by the Tennessee

Department of Commerce and Insurance with an effective date of November 26, 2005. Although the new Comp. R. & Regs. do not apply to the period under examination, they do contain a number of new requirements with which the Fund is required to come into compliance. Listed below are new requirements of the revised rules along with the status of the Fund's efforts to come into compliance with the new requirements.

Licensing of the Fund Administrator

Revised Tenn. Comp. R. & Regs., 0780-1-54-.07 states that no person shall act as an administrator for a pool without a license issued by the Commissioner of the Tennessee Department of Commerce and Insurance. The revised Rules give persons acting as an administrator for an existing pool as of January 1, 2005, twelve (12) months from the effective date of the revised Rules to obtain such license. The Fund's administrator should submit an application to be licensed in accordance with revised Tenn. Comp. R. & Regs., 0780-1-54-.07.

Custodial Agreement

Revised Tenn. Comp. R. & Regs., 0780-1-54-.013 (4) now requires pools to maintain investments and deposits pursuant to Tenn. Comp. R. & Regs., 0780-1-46 "Permissible Method of Holding Securities." The revised Rules are specific as to requirements for a custodial agreement, and provide detailed information on the language of the custodial agreement. During the examination period, the Fund's investment agreement with Suntrust Bank was not subject to the requirement of the revised Rules; however, effective November 14, 2005, the Fund must comply with the new requirement. The Fund's current investment agreement with Suntrust Bank does not contain the safeguards required by Tenn. Comp. R. & Regs., 0780-1-46 and should be revised. As of the date of this report, the Fund has not executed a custodial agreement that complies with revised Tenn. Comp. R. & Regs., 0780-1-54-.013 (4) and Tenn. Comp. R. & Regs., 0780-1-46.

Royalty Agreement

During the period covered by this examination, the Fund routinely made annual

contributions to ABC. The Fund was not obligated by contract to make payments but did so at the discretion of its Board of Trustees. Any future payments the Fund wishes to make to ABC for royalty fees will be subject to revised Tenn. Comp. R. & Regs., 0780-1-54-.016 (2) which states that "a sponsoring association may require a pool to pay to the sponsoring association a royalty fee or fee for using its name or other services which may be provided by the sponsoring association to the pool." The Rule further states that "all fees paid to the sponsoring association are required to be approved by Commissioner of the Tennessee Department of Commerce and Insurance no later than thirty (30) days prior to the execution of any contract setting such fees between the pool and the sponsoring association." If it is the Fund's intent to continue to make contributions to ABC without a written contract, the Fund must request approval from the Commissioner of the Tennessee Department of Commerce and Insurance prior to any fee being paid to ABC. Otherwise, the Fund and ABC should execute a contract for royalty fee payments in accordance with revised Tenn. Comp. R. & Regs., 0780-1-54-.016 (2) and the Fund should request approval from the Commissioner of the Tennessee Department of Commerce and Insurance prior to making future payments.

Third Party Administrator (TPA) Certificate of Authority

Tenn. Comp. R. & Regs., 0780-1-81-.09 (9) requires a TPA obtain a certificate of authority or license from the Commissioner of the Tennessee Department of Commerce and Insurance prior to performing any TPA functions in the State of Tennessee. The Chapter further states that any TPA that holds a license as a service company at the time of the effective date of the Chapter has until January 1, 2006, to obtain a certificate of authority. The Fund's TPA's (ASC and Willis Pooling) should submit an application for a certificate of authority in accordance with Tenn. Comp. R. & Regs., 0780-1-81-.09.

TPA Disclosure of Charges and Fees

Tenn. Comp. R. & Regs. 0780-1-81-.08 states that TPA's shall disclose to the employer or pool all affiliates of the TPA providing services to the employer or pool and any fees in addition to those paid to the TPA for such services. In the Group's administrative service agreement with its TPA, Willis Pooling, a key provision is for the TPA to retain the

entire commission accruing from placement of any primary or excess insurance coverage written for the Fund. In accordance with Tenn. Comp. R. & Regs. 0780-1-81-.08, the TPA should disclose to the Group the amount of all commissions retained from the placement of the above insurance coverage.

Member's Equity

Subsequent to the date of examination, the Fund provided the Department with financial records which summarized its members' equity on a policy year basis for all eleven years the Fund has been in existence. Although the Fund reported an overall net worth per examination at March 31, 2004, of seven hundred fifty-one thousand twenty-two dollars ($751,022), the Fund reported net losses and deficiencies in the four (4) policy years ending December 31, 1997, March 31, 2000, March 31, 2001 and March 31, 2004. These deficiencies will be addressed pursuant to Tenn. Comp. R. & Regs. 0780-1-54.

Conclusion

The work papers and audited financial statements used in connection with the examination of the Fund were prepared using generally accepted accounting principles (GAAP) and National Association of Insurance Commissioners (NAIC) procedures, where applicable. These work papers were used to verify and value the assets and determine the liabilities of the Associated Builders & Contractors of Tennessee Workers' Compensation Self-Insurance Fund as of March 31, 2004. In addition, Tennessee Code Annotated and Tennessee Comprehensive Rules and Regulations of the Tennessee Department of Commerce and Insurance were utilized to determine compliance of the issues addressed in this report on examination.

In such manner, it was found that as of March 31, 2004, the Fund had assets of six million seven hundred ninety-eight thousand four hundred ninety-one dollars ($6,798,491) and liabilities, exclusive of surplus, of six million forty-seven thousand four hundred sixty-nine dollars ($6,047,469). Thus, there existed for the additional protection of the policyholders, the amount of seven hundred fifty-one thousand twenty-two dollars ($751,022) in the form of premiums refundable to members (Members' Equity).

The courteous cooperation extended during the course of the examination by the Fund Administrator, and the officers and employees of the companies providing services to the Fund is hereby acknowledged. In addition to the undersigned, Mr. Lacy Smith, Insurance Examiner II, with the State of Tennessee Department of Commerce and Insurance, participated in the work of this examination.

Respectfully submitted,

Gregory Bronson
Examiner-in-Charge
Insurance Examiner III
State of Tennessee

Kurt Polasko
Insurance Examiner III
State of Tennessee

Examination Affidavit

The undersigned deposes and says that he has duly executed the attached examination report of Associated Builders & Contractors of Tennessee Workers' Compensation Self-Insurance Fund dated August 21, 2006, and made as of March 31, 2004, on behalf of the Tennessee Department of Commerce and Insurance. Deponent further says he is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of his knowledge, information and belief.

Gregory Bronson
Examiner-in-Charge
Insurance Examiner III
Department of Commerce and Insurance
State of Tennessee

County Davidson
State Tennessee

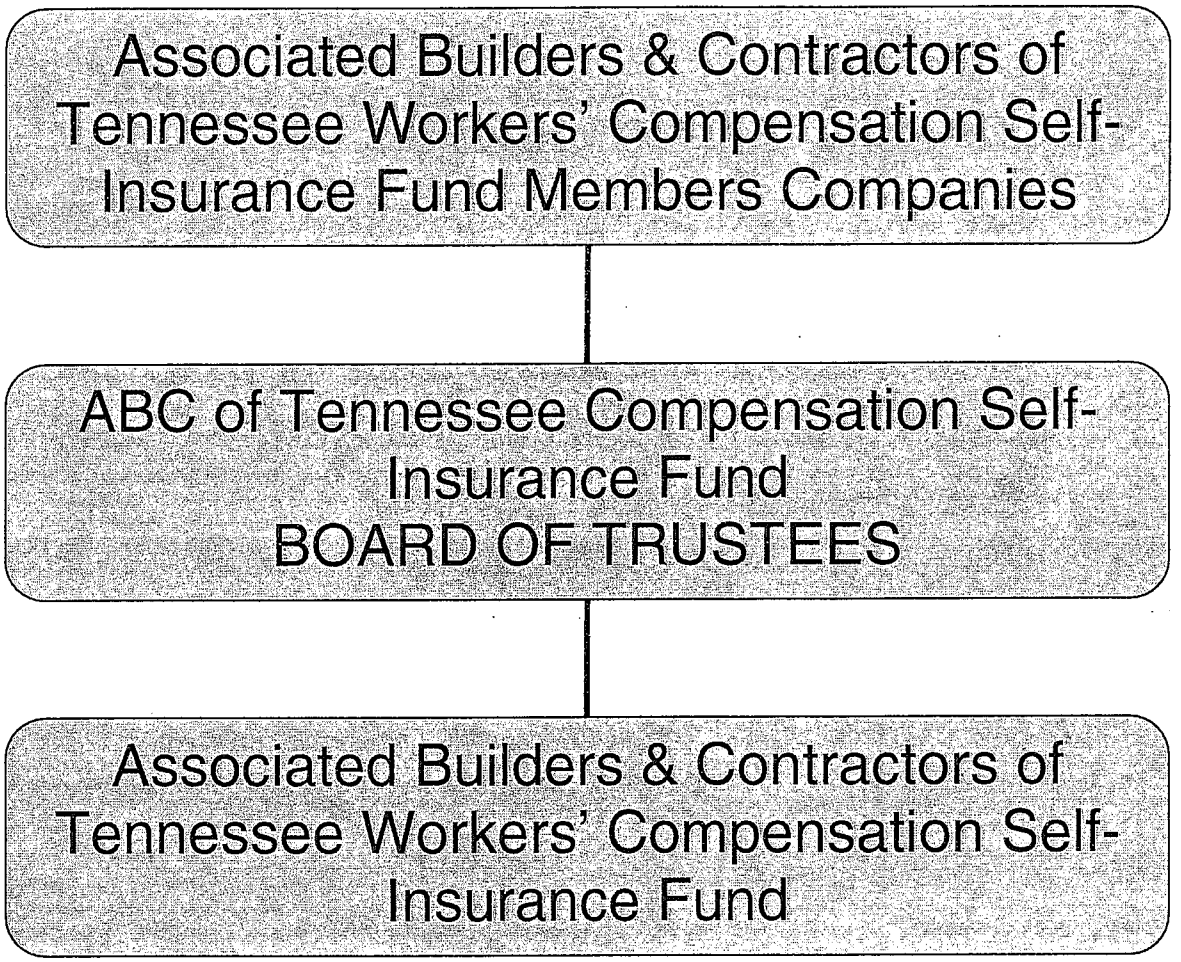
Subscribed and sworn to before me
this 21st day of
August, 2006.

Helen W. Dorsey
(Notary)

My Commission Expires:
05/22/2010

HELEN W. DORSEY
STATE OF TENNESSEE NOTARY PUBLIC
DAVIDSON COUNTY, TENN.
My Commission Expires MAY 22, 2010

ORGANIZATIONAL CHART # 1



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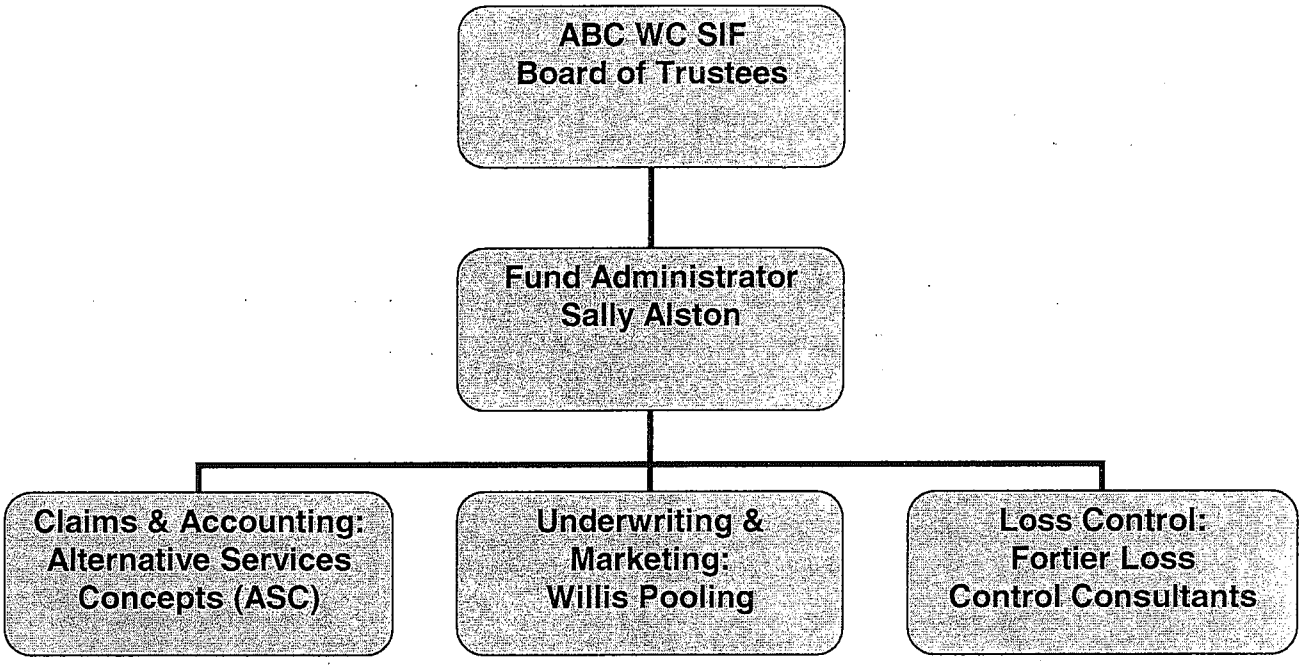
Associated Builders & Contractors of Tennessee Workers' Compensation Self-Insurance Fund