EXHIBIT

A

Report on Examination

of the

Workers' Compensation Self-Insurance Group Fund

of the

Tennessee Association of Business Company Owners' Managed Program

d/b/a

"TABCOMP Trust"

750 Old Hickory Boulevard
Building 2, Suite 100
Brentwood, TN 37027

as of

December 31, 2003

Department of Commerce and Insurance

State of Tennessee

Nashville

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Dept. Of Commerce & Insurance
Company Examinations

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Nashville, TN
May 4, 2005

Honorable Paula A. Flowers
Commissioner of Commerce & Insurance
State of Tennessee
Nashville, TN

Commissioner:

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

Workers' Compensation Self-Insurance Group Fund

of the

Tennessee Association of Business Company Owners' Managed Program

d/b/a

TABCOMP Trust

Brentwood, Tennessee

## Introduction

This examination was arranged by the Financial Affairs Section of the Department of Commerce and Insurance, State of Tennessee in accordance with Tenn. Code Ann. § 50-6-405 and Tenn. Comp. R & Regs. 0780-1-54-.06. It was commenced on July 1, 2004, by examiners of the State of Tennessee, Department of Commerce and Insurance. This is the first such examination of the Tennessee Association of Business Company Owners' Managed Program ("TABCOMP Trust").

## Scope of Examination

The period covered hereunder is from July 1, 2001, the effective date of formation of TABCOMP Trust, to the close of business on December 31, 2003, the date of this examination. During the course of examination, the assets of the TABCOMP Trust were verified, and liabilities were determined or estimated as of December 31, 2003, in accordance with Tenn. Code Ann. and Tenn. Comp. R & Regs. and Generally

Accepted Accounting Principles. TABCOMP Trust'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 TABCOMP Trust's operations, practices and compliance with statutes, to the extent hereinafter set forth.

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 Declaration of Trust and Bylaws
Indemnity Agreement and Power of Attorney
Management and Control
Corporate Records
Management Agreements
Statutory Deposit
Fidelity Bonds and Other Insurance
Market Conduct Activities
Excess Insurance Coverage
Loss Experience
Accounts and Records
Litigation, Contingent Liabilities and Subsequent Events
Financial Statement

They are discussed in detail as follows:

## History and Organization

In accordance with Tenn. Code Ann. § 50-6-405(c)(1), TABCOMP Trust affiliated with the Tennessee Chamber of Commerce & Industry ("TCCI") upon its formation. The TCCI is the state chamber of commerce and the state manufacturers' association. It is involved in federal and state legislation and regulations, human resources, taxation, the environment, health care and other issues that affect the state's business community.

The TCCI was founded in 1912 as the state affiliate of the National Association of Manufacturers. In 1985, it merged with the Tennessee Taxpayers Association and became affiliated with the U.S. Chamber of Commerce. In 1987, the then Tennessee Manufacturers and Taxpayers Association was renamed the Tennessee Association of Business ("TAB"). In November 2002, TAB was renamed TCCI. Currently, the organization has over 1,000 members across Tennessee from all facets of business and industry.

TABCOMP Trust was created by members of the TCCI to act as a self-insurance group to provide workers' compensation and employers' liability coverage for Tennessee employees. Membership in the TABCOMP Trust is composed of qualifying members of the TCCI that have pooled their liabilities under the Tennessee Workers' Compensation Law.

The original trust was created as the Tennessee Association of Business Selective Self Insurers Trust ("TABSSIT") effective December 31, 1991. An initial group of ten members made contributions equal to 25% of their first year estimated annual net premium for workers' compensation coverage (in accordance with Tenn. Comp. R & Regs. 0780-1-54-.04). The formation of TABSSIT was accomplished by the members with the assistance of the then president of the TAB, Mr. Carter Witt, and Alexsis, Inc., TABSSIT's third party administrator.

Effective December 31, 1998, the Board of Trustees and TABSSIT's Members voted to cease operations, and all of its Members withdrew from TABSSIT and secured workers' compensation coverage primarily through the voluntary market. TABSSIT executed a loss portfolio transfer with Safety National Casualty Corporation ("Safety"), their excess insurance carrier, whereby Safety assumed 100% of the liabilities and obligations of TABSSIT for all of its specific and aggregate liability for losses, including unpaid losses and loss adjustment expenses from the time period January 1, 1992 through December 31, 1998. TABSSIT accumulated a positive Members' equity of approximately $3.4M as a result of its operations from 1992 through 1998, and returned approximately $2.7M in excess reserve funds to its former Members after funding the loss portfolio transfer (refer to "Payment of Refunds" on page 33 for a more thorough description of the distribution of TABSSIT refunds).

On July 1, 2001, a new Trust was formed under the name of Tennessee Association of Business Company Owners' Managed Program, d/b/a TABCOMP Trust. It began accepting new Members and underwriting future risks effective this same date. Although TABCOMP Trust was created as a new trust, the operations are identical to TABSSIT, and membership and management is common between both. This examination only covers the period of TABCOMP Trust's operations subsequent to its formation on July 1, 2001.

The following table summarizes the growth and financial history of both TABSSIT and TABCOMP Trust since their organization:

| TABSSIT | Members | Revenues | Expenses | Income (loss) | Assets | Members' Balance | |
|---|---|---|---|---|---|---|---|
| 1992 | 31 | 2,104,828 | (1,994,840) | 109,988 | 1,245,741 | 109,988 | |
| 1993 | 79 | 4,354,422 | (4,061,502) | 292,920 | 3,001,277 | 403,343 | |
| 1994 | 136 | 7,656,945 | (7,975,832) | (318,887) | 5,092,272 | 84,020 | |
| 1995 | 186 | 11,079,360 | (11,074,727) | 4,633 | 8,663,919 | 88,654 | |
| 1996 | 205 | 10,559,468 | (10,539,610) | 19,858 | 9,898,598 | 79,129 | |
| 1997 | 128 | 6,575,665 | (3,991,465) | 2,584,200 | 10,041,405 | 2,714,872 | |
| 1998 | 117 | 4,542,927 | (3,891,444) | 651,483 | 11,579,238 | 3,369,261 | |
| **TABCOMP Trust** | | | | | | | |
| 2001 | 8 | 174,846 | (212,483) | (37,637) | 911,478 | 735,306 | * |
| 2002 | 79 | 4,257,885 | (3,742,112) | 515,773 | 3,314,560 | 1,291,356 | * |
| 2003 | 88 | 5,900,305 | (5,598,762) | 301,543 | 5,398,072 | 1,608,505 | * |

* included in these amounts is approximately $735K, $770K and $850K of TABSSIT reserve funds held by TABCOMP Trust in 2001, 2002 & 2003 respectively

The above amounts were taken from audited financial statements of TABSSIT and TABCOMP Trust which were filed with the Department of Commerce and Insurance. Only the operations of TABCOMP Trust were subject to examination by the Department of Commerce and Insurance, and TABCOMP Trust's December 31, 2003 financial statement is included at the end of this examination report.

## Trust Agreement and Declaration of Trust and Bylaws

When TABCOMP Trust was formed, a "Declaration of Trust and Bylaws" was executed by the Board of Trustees of the new membership and approved by the Department of Commerce and Insurance to be effective July 1, 2001. TABCOMP Trust was formed to act as a workers' compensation self-insurance group as defined by Tenn. Comp. R & Regs. 0780-1-54-.02 and as authorized by Tenn. Code Ann. § 50-6-405. TABCOMP Trust Agreement and Bylaws state the purpose of the Trust as follows:

> to hold and administer the Fund through which its Members can fulfill their responsibilities under the Tennessee Workers' Compensation Act; to form a workers' compensation self-insurance group pursuant to the Act to provide for workers' compensation coverage and for benefits to employees and dependents of its Members; to provide the maximum

allowable advance discounts or dividends on contributions made by Members for workers' compensation coverage; and to contain the cost of providing workers' compensation coverage by developing and refining specialized claim techniques and a loss prevention program

TABCOMP Trust is an association which is owned by its Members. Membership in TABCOMP Trust consists of persons, partnerships, corporations or other legal business entities, who are employers, are members in good standing of the TCCI, and who contribute to the Workers' Compensation Self-Insurance Group Fund ("Fund") as a participant in the Trust.

Indemnity Agreement and Power of Attorney

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 and power of attorney as a condition of membership in TABCOMP Trust. Significant terms that each Member agrees to in accordance with the Indemnity Agreement include the following:

- The Members, jointly and severally, will pay any final award based upon a claim against any of them under the workers' compensation laws of the State of Tennessee; and the Trust will pay any assessments lawfully levied against it by the State of Tennessee.
- The Agreement is a mutual covenant of assumption of joint and several liability and not a partnership.
- The Board of Trustees will set up, operate and enforce the administrative rules, regulations and by-laws of the Trust and the Fund
- The Board of Trustees may admit as Members only those who meet the criteria for membership established by the Board of Trustees. The Board of Trustees shall be the sole judge of whether or not an applicant shall be admitted to membership.
- Each Member shall pay promptly all contributions and assessments required by TABCOMP Trust. This requirement shall also extend to former Members who were such during any part of the year(s) for which the contribution or assessment is due. The amount of such contributions will be determined by applying applicable experience modification to the rates for the exposure to risk. The required contribution may be reduced by any discount allowed by the Board of Trustees. In the event of a loss fund deficit, the Board of Trustees may adopt any plan it deems equitable for the elimination of such deficit.
- Each Member hereby appoints the designated claims service agent as its agent and attorney-in-fact, to act in its behalf and to execute in its name all such contracts, reports, waivers, agreements and excess insurance contracts as the Claims Service Agent may deem necessary or desirable; and to make or arrange for payment of claims, medical expenses and all other things required or necessary, insofar as they

affect its workers' compensation liability under Tennessee law and are covered by the terms of TABCOMP Trust and the rules and regulations an now provided or as hereafter promulgated by the Board of Trustees.

- Each Member shall give TABCOMP Trust, the Claims Service Agent, and any of their agents, servants, employees or attorneys, permission and access at all reasonable time to examine the member's work place, plant work, machinery and appliances covered by this Agreement, and shall permit such persons at all reasonable times while such person is a Member and within two years after the final termination of membership to examine the Member's books, vouchers, contracts, documents and records of any and every kind which show or tend to show or verify the contribution which is payable under the terms hereof.
- After all obligations for workers compensation benefits and related expenses have been provided for, the remaining funds of TABCOMP Trust shall be distributed to Members in such manner as the Trustees shall deem equitable. This includes (i) limiting distribution to Members with a loss ratio not in excess of a level designated by the Board of Trustees, and/or (ii) providing that any Member may share in prorata distribution of dividends regardless of when such dividends are declared so long as such member participated during the year for which distribution is made.
- TABCOMP Trust will provide each prospective Member at the time of application for membership a written description of any refund plan then in effect.

Examination procedures included a review to determine that every member of TABCOMP Trust executed the above described "Indemnity Agreement." There were no exceptions to our tests noted.

## Management and Control

The operation and administration of TABCOMP Trust is the joint responsibility of a Board of Trustees consisting of not more than fifteen nor less than five persons. Tenn. Comp. R & Regs. and the Trust's Bylaws require all Trustees to be residents of the State of Tennessee or officers of corporations authorized to do business in Tennessee. At least two-thirds of the Trustees are required by Tenn. Comp. R & Regs. and Bylaws to be employees, officers or directors of Members of TABCOMP Trust. No affiliate of the Administrator or the Service Company shall serve as a Trustee. The officers of the Board of Trustees shall be, at a minimum, a Chairman, a Vice-Chairman and a Secretary.

The initial Board of Trustees was empowered with the creation of TABCOMP Trust through the execution of the "Declaration of Trust and Bylaws" effective July 1, 2001. Seven persons were named therein to be Trustees to serve until the first meeting

of the Members of TABCOMP Trust. Thereafter, the Bylaws and the Rules provide that the Board of Trustees shall be elected by the Members of TABCOMP Trust. Each subsequently elected Trustee shall serve for a term of five years.

A Trustee may resign and be fully discharged from all further duties or responsibilities by giving at least thirty days prior written notice to the Chairman of the Board of Trustees. A Trustee may be removed, with or without cause, by a majority vote of all Trustees. When a Trustee dies, becomes incapacitated, refuses to act, resigns or is removed, his successor shall be appointed by the remaining Trustees to fill the unexpired term of office. Such appointment shall be subject to confirmation by the Members at their next regularly scheduled meeting.

At December 31, 2003 the following persons were serving as members of the Board of Trustees:

| Trustee | Member Affiliation |
|---|---|
| Jim Dyer, Chairman | Metal Products |
| Deck Sachse, Vice Chairman | Conwood Co. |
| Ian Smith, Secretary | WYKO |
| Ray Butler, Jr. | Steelcraft Corp. |
| Clayton Chambers | Toyoda Automotive N. America |
| Rick Francis | Tennessee Apparel |
| Mike Griffin | International Playing Cards |
| Bill Ring | Kingsport Foundry |
| Daryl Smith | Hail & Cotton |

Responsibilities of the Trustees as stated in the Bylaws include the following:

- The Trustees shall have the power, authority and responsibility for the general supervision and operation of TABCOMP Trust, including the administration of the Fund, and shall conduct the business activities of TABCOMP Trust in accordance with the bylaws, applicable federal and/or state statutes, and applicable governmental rules and regulations.
- The Trustees shall be responsible for all monies collected or disbursed by TABCOMP Trust and for the segregation of all monies into the Claims Fund Account and the Administrative Fund Account.
- The Trustees shall receive applications for membership from prospective new members and shall approve or disapprove such applications in accordance with rules promulgated by the Trustees. The Trustees may delegate the ministerial

authority for membership approval to the Administrator or such other person as they select.

- The Trustees shall be responsible for establishing such trusts, loss funds, or other funds as may be required from time to time by the Rules or as may be determined by the Trustees.
- The Trustees shall be responsible for posting such security deposits and/or security bonds as may be required by the Department of Commerce and Insurance.
- The Trustees shall be responsible for and shall cause to be filed with the Department of Commerce and Insurance and elsewhere such annual or other periodic audits, reports and disclosures as may be required from time to time by applicable federal or state statutes or Tenn. Comp. R & Regs.. The Trustees shall take all necessary precautions to safeguard the Fund and the other assets of TABCOMP Trust including the following:

  Designate an administrator as its agent to administer the Fund and the day to day operations of the Trust. In order to accomplish such, the administrator is authorized to select and supervise a service agent. Such administrator shall not be an owner, officer, or employee of the service agent. The Board of Trustees shall delineate in the written minutes of its meetings the other areas of authority delegated to the Administrator.

  Retain control of all monies collected or disbursed for the Trust; all loss funds or funds of any type shall remain in the custody of the Trustees or the administrator; provided, however, that a revolving fund for payment of compensation benefits due and other related expenses may be established for the use of the service agent.

## Corporate Meetings & Records

### Board of Trustees Meetings

The Bylaws provide that the Trustees shall meet at least quarterly at the principal office of TABCOMP Trust or at some other location as may be acceptable to the Trustees. The Chairman shall set the date, time and location of each meeting and notice thereof shall be furnished to each Trustee by the Secretary not less than ten days prior to the date of such meeting. The notice shall specify the purpose of the meeting and any action proposed to be taken.

Special meetings may be called at any time by the Chairman, and shall be called by the Chairman upon request of at least three Trustees. Special meetings may be held by telephone conference calls or other methods of communication in which all Trustees participating may simultaneously hear each other. For the purpose of any meetings of

the Trustees, a quorum shall consist of at least a majority of the Board of Trustees. All actions by and decisions of the Board of Trustees shall be by the vote of a simple majority of those participating in a duly called meeting at which a quorum is present.

The Secretary, Acting Secretary, or his designee shall keep minutes of all meetings, proceedings and acts of the Board of Trustees. Copies of all minutes of the meeting of the Board of Trustees shall be sent by the Secretary, Acting Secretary or a designee to all Trustees and shall be made available to the Department of Commerce and Insurance.

During the period under examination, there were ten regular meetings of the Board of Trustees. Membership requirements and powers and duties of Board Members was verified to be in accordance with Tenn. Comp. R & Regs., except as otherwise commented on in this exam report.

Members' Meetings

The Bylaws of TABCOMP Trust require the Members of the Trust to meet annually at the offices of TABCOMP Trust on the first Tuesday in October of each year or at such other place and time as may be determined by the Trustees. Special meetings of the Members may be called at any time by the Trustees and shall be called upon the written request of not less than 20% of the Members. Written notice of all meetings of the Members shall be delivered not less than ten days or more than thirty days prior to the meeting, either in person or by mail. Each Member shall have one vote and may vote either in person or by written proxy. All actions by, and decisions of, the Members shall be by the vote of a simple majority of those attending a duly called meeting at which a quorum is present.

An annual report on the activities and the status of the fund shall be presented by the Trustees at such meeting, and new Trustees will be elected. The Members shall also confirm any compensation established by the Board of Trustees for attendance at meetings of the Board of Trustees and the performance of the normal duties of Trustees.

During the two and one half year period under examination, there were two regular meetings of the Members of the Trust. Subsequent to the date of examination, TABCOMP Trust continued to hold regular meetings of its membership as required by its bylaws and Tenn. Comp. R & Regs. Membership requirements and powers and

duties of TABCOMP Trust Members were verified to be in accordance with Tenn. Comp. R & Regs.

## Management Agreements

### Administrative Services Agreements

On July 1, 2001, with the formation of TABCOMP Trust, the Board of Trustees voted to designate Carter Witt as Administrator of TABCOMP Trust within the meaning of Tenn. Comp. R & Regs. 0780-1-54-.02. The Administrator is to carry out the policies established by the Board of Trustees and provide day-to-day management of TABCOMP Trust. An "Administration Agreement" between TABCOMP Trust and Carter Witt does not appear to have been entered into at that time. An agreement subsequently became effective June 6, 2002, and continued in effect through December 31, 2003, the date of this examination.

### Services Agreements

A "Service Agreement" between TABCOMP Trust and TAB Service Corporation became effective July 1, 2001 with the formation of TABCOMP Trust, and it continued in effect until cancelled on January 1, 2003. TAB Service Corporation is wholly owned by the TCCI, the not-for-profit sponsoring association of TABCOMP Trust. TAB Service Corporation provided the following services to TABCOMP Trust under the terms of the agreements:

a. Review all incidents and claims arising under the Tennessee Workers Compensation Act against TABCOMP Trust; conduct appropriate investigations of such claims; secure necessary claims-related services on behalf of TABCOMP Trust; adjust claims; and provide to TABCOMP Trust reports on claims transactions.

b. Establish a Claims Fund to be used by TAB Service Corporation for the receipt of premium and payment of claims.

c. Collect, receive process and report to TABCOMP Trust loss data organized to provide risk management information.

d. Appoint agents and assist them with presenting insurance benefits to potential TABCOMP Trust members. TAB Service Corporation will prepare pamphlets, booklets, advertising material and other promotional materials for use in soliciting business both directly and through independent agents.

e. Facilitate the underwriting of TABCOMP Trust members.

f. Provide, either directly or by use of a loss control subcontractor, on-site surveys for hazard identification and work practices evaluation a minimum of one time per year

per member. Provide accident analysis and investigation to identify trends and problem areas for loss control focus. Provide assistance with safety and health training seminars. Provide TABCOMP Trust with written reports on loss control.

g. Supervise, direct and implement the production, underwriting, premium collection, payroll audit, accounting, statistical and other work necessary or incidental to the insurance business written under this agreement. Set up and maintain such books and records in the manner as may be mutually agreed to record the transactions pursuant to agreement. Furnish, render and provide on behalf of TABCOMP Trust all services and facilities for the business it transacts, as are customarily furnished, rendered and provided by insurance companies for the business written. Cancel certificates for cause as approved by TABCOMP Trust. Provide TABCOMP Trust with an independent financial examination in a form acceptable to TABCOMP Trust in the event any state insurance department requires the provision of such examination.

On January 1, 2003, TABCOMP Trust and TAB Service Corporation entered into a Service Agreement that replaced the original agreement. The terms of the replacement agreement were identical to the terms in the original agreement effective July 1, 2001, except "Addendum A", Article I (1.1), the initial discretionary settlement authority limit granted to TAB Service Corporation for final settlement increased from $20,000 to $50,000. The Service Agreements with TAB Service Corporation, in effect during the entire period under examination from July 1, 2001 through December 31, 2003, provided that TAB Service Corporation shall be paid total annual service fees, billed monthly, equal to 13% of premium, broken down as follows:

| | |
|---|---|
| Claims Administration | 5% of Premium |
| Loss Control | 2% of Premium |
| Underwriting | 1% of Premium |
| Marketing and Administration | 5% of Premium |

TAB Service Corporation was paid agents' commissions during the period of examination from Safety for the placement of TABCOMP Trust's excess insurance coverage. They were also paid agents' commissions by TABCOMP Trust for members that joined without an independent insurance agent. Amounts paid to TAB Service Corporation for all services during the period of examination were approximately as follows:

| | |
|---|---|
| Service Company fees | $ 1,343,000 |
| Excess insurance commissions | 127,000 |
| Independent agents' commissions | 179,000 |
| Total | $ 1,649,000 |

Loss Control Agreement

Loss control services were provided under the Service Agreement between TABCOMP Trust and TAB Service Corporation for the period from inception of TABCOMP Trust until July 15, 2002, when a "Loss Control Agreement" between TABCOMP Trust and Fortier Loss Control Consultants Inc. ("Fortier") became effective. The term of the agreement was for a period of one year and provided compensation to Fortier of 2% of earned premium on a monthly basis to be adjusted after audit to reflect final premium. Under the agreement, Fortier shall:

1. Conduct risk evaluation surveys of prospective members as requested and provide written reports to TABCOMP Trust.
2. Conduct semi-annual visits to members to evaluate loss control programs.
3. Provide technical support to members to assist them with their loss control programs.
4. Track hours of service available to members of TABCOMP Trust based on 2% of their premium divided by Fortier's hourly rate ($90/hr). Members with substantial premiums will be informed of the hours available and offered the opportunity to develop a plan to utilize these hours to assist their loss control program.
5. Members with high losses will be provided additional services as needed to address their loss control problems. These services may exceed 2% of their premium, but total services provided to TABCOMP Trust will not exceed 2% of the total earned premium.
6. Fortier will provide reports to the Board of Trustees as requested.

Upon expiration of the agreement, a new "Loss Control Agreement" between TAB Service Corporation and Fortier was entered into and became effective July 15, 2003, for one year unless renewed and provided for substantially the same services and compensation. The fees to Fortier under the new agreement were paid by TABCOMP Trust through TAB Service Corporation until June 2004. Loss control services were subsequently included in the responsibilities of Cannon Cochran Management Services, Inc. ("CCMSI") under the Administrator Agreement entered into with TABCOMP Trust effective November 1, 2004 which is discussed more fully under the "Litigation, Contingent Liabilities and Subsequent Events" section of this examination report.

Statutory Deposit

Pursuant to Tenn. Comp. R & Regs. 0780-1-54.04(2)(b), self insured workers' compensation groups are required to maintain either a security deposit, a surety bond,

or a financial security endorsement on file with the Department of Commerce and Insurance in an amount approved by the Commissioner. The amount of the bond is prescribed by the Commissioner and is based on factors such as size, years in existence, and types of employment risk.

The Trust satisfied this requirement effective June 14, 2001, by obtaining a surety bond with Safety, a corporate surety company incorporated in Missouri and authorized to transact business in the State of Tennessee. The bond provided $500,000 in coverage which is to be used by the State for the sole purpose of paying workers' compensation claims and associated expenses if the pool fails to pay the benefits which it is legally obligated to pay. TABCOMP Trust maintains a deposit with Safety in the amount of $300,000 as security for their bond. The surety bond contains a provision of prior notification to the Department of Commerce and Insurance in the event of revocation or cancellation. Examination procedures included verification of renewal of the bond subsequent to the date of examination.

Fidelity Bond and Other Insurance

Tenn. Comp. R & Regs. § 0780-1-54-.04(2)(f-g) requires the Administrator and the Service Company to maintain, at all times, a fidelity bond in a form and amount prescribed by the Commissioner. Such fidelity bonds shall be written by bonding companies licensed to do business in the State of Tennessee, and provide coverage in amounts satisfactory to the Commissioner. During the period of examination, the Administrator maintained a commercial crime policy with Travelers Casualty and Surety Company of America (Travelers") with a $100,000 limit and a $5,000 deductible. Travelers was verified to be licensed to do business in the State of Tennessee. Subsequent to the date of examination, coverage was bound by State Auto Insurance Company, insuring a new Administrator, Will Hord, in the same amount of coverage. Examination procedures included verification of renewal of coverage upon the expiration of the policy in effect as of the date of this examination.

TABCOMP Trust's Service Company, TAB Service Corporation, maintained a fidelity bond for the period of March 17, 2001 through the date of examination with American International Specialty Lines Insurance Company, a surplus lines carrier

authorized to conduct business in Tennessee. Coverage was provided in the aggregate amount of $2,500,000.

During the period of examination, TABCOMP Trust maintained a policy providing at least $1,000,000 of errors and omissions coverage with a deductible of $25,000. The coverage was provided by Royal Surplus Lines Insurance Company of Charlotte, North Carolina, a surplus lines carrier authorized to conduct business in the State of Tennessee.

## Market Conduct Activities

### Marketing

TABCOMP Trust has advertised its services in the Insurors of Tennessee magazine and maintained a small yellow page advertisement. TAB Service Corporation, has maintained a website www.tabservicecorp.com that provides information about the program. Marketing efforts have been directed at members of the sponsoring association, TCCI (formerly TAB) and at non-member manufacturing companies and agents. TABCOMP Trust representatives and informational literature has historically been made available at annual meetings of the membership of the sponsoring association. TABCOMP Trust's Administrator and marketing staff visit independent agents and prospective members throughout the State and provide them with literature about TABCOMP Trust and its underwriting guidelines. TABCOMP Trust pays commissions on new and renewal premium to independent agents that market the TABCOMP Trust's policies through a tiered program that ranges from a minimum of 7% on premiums below $500,000 to a maximum of 9% on premiums of $1,000,000 or more.

### Underwriting

TABCOMP Trust applies the following underwriting and rating procedures approved by the Board of Trustees to all new applicants to TABCOMP Trust:

1. Agree to join the TCCI (formerly TAB), if not already a member, and have operations engaged primarily in the business of manufacturing.
2. Meet a minimum annual premium requirement of $10,000 (final premium).
3. Have been in business at least three years with workers' compensation coverage. Exceptions may be considered if it can be demonstrated that the business' management has successfully operated a similar business prior to establishment of applicant firm.

4. Provide a fully completed Acord Workers' Compensation form accompanied by currently valued loss runs and payrolls for the current year and three preceding years.
5. Provide the latest available experience modification factor from the NCCI or other approved rating company.
6. Have a cumulative loss ratio not exceeding 60% for the most recent four years of coverage.
7. Have a net worth equal to or greater than four times the annual premium in order to qualify.

These guidelines are applied only to initial applications for new business and not to renewals. Also, the guidelines have not been applied to business written under the TABSSIT or written directly by Safety prior to the formation of TABCOMP Trust in July, 2001. Initial approval of membership is the responsibility of TAB Service Corporation. New members falling within all underwriting guidelines are brought by TAB Service Corporation to the first subsequent Board of Trustees meeting for formal approval. Any prospective new member falling outside any guideline, but recommended for coverage due to special circumstances, must be voted on by the Board of Trustees before they can be accepted. Applications for new business that contain quotes that result in an estimated premium amount below the "amount needed for approval" by the excess carrier are submitted to the excess carrier for underwriting approval before being submitted to the Board of Trustees for membership approval. Renewal quotes are not required to be individually approved by the excess carrier.

Rating Procedures

Tenn. Comp. R & Regs. 0780-1-54-.15 requires TABCOMP Trust to adhere to a uniform classification system, uniform experience rating plan, and manual rules approved by the Commissioner. 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 the National Council on Compensation Insurance ("NCCI"). TABCOMP Trust 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.

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 / $100) for each class code to calculate manual premium. Based on eligibility requirements, a drug free workplace discount of 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.

Premium is billed using one of two payment plans currently being offered by TABCOMP Trust. The standard plan requires a down payment of 25% of the estimated annual premium with the balance paid in eight additional consecutive monthly payments. The optional plan allows payment of the estimated annual premium in twelve substantially equal monthly payments. The optional plan, according to TABCOMP Trust personnel, is usually limited to members that have higher annual premium amounts and have requested the plan in order to ease cash flow.

The objective of TABCOMP Trust's rating procedures is to quote and write coverage to an expected loss ratio of between 60% and 65%. The premium amount needed to arrive at the target loss ratio range is calculated using a "loss pick" worksheet. The underwriter also calculates a target premium amount based on the excess carrier expected loss ratio of 65%, which is calculated using the average losses over the past four years with development at an anticipated rate of 20%. This calculated premium amount is indicated as the excess carrier's "amount needed for approval". The underwriter adjusts premium calculated based on NCCI procedures by applying "schedule debits or credits" in such a manner as to make the final premium amount fit within the target loss ratio premium range. In some cases, the underwriter uses the maximum permitted debit amount of 25% and the indicated premium amount is still below the amount needed to reach the target loss ratio. Applications for new business that contain quotes that result in an estimated premium amount below the

"amount needed for approval" by the excess carrier are then submitted to the excess carrier for rating approval before being submitted to the board for membership approval. Renewal quotes are not required to be individually approved by the excess carrier.

Examination procedures included a review of the rating calculations performed during the period of examination. Comments about the results of our review are included on page 35 of this examination report.

Forms

Tenn. Comp. R & Regs. 0780-1-54-.08 requires an employer joining a workers' compensation group to submit an application for membership to the Board of Trustees or its Administrator and enter into the indemnity agreement. Membership takes effect no earlier than each Member's date of approval. The application for membership and its approval shall be maintained as permanent records of the Board of Trustees. Examination procedures included a review of these documents for each member with no exceptions noted.

Policy forms for evidence of membership and coverage, the Indemnity Agreement, Power of Attorney and State approved application for membership are also required to be filed with the Department of Commerce and Insurance. Examination procedures included a review of TABCOMP Trust's use and filing of approved forms for each of its Members and no exceptions were noted.

Claims

TABCOMP Trust's practices pertaining to the handling of loss settlements were reviewed by sampling both open and closed claim files. The sample consisted of claims paid, claims denied and those in litigation for claims incurred during the period of this examination. The review disclosed that TABCOMP Trust settled its claims promptly after receipt of the necessary documents and in accordance with policy provisions. Examination procedures included verification of proper use and filing of required claims reporting forms with the Tennessee Department of Labor.

## Excess of Loss Insurance

In accordance with Tenn. Comp. R & Regs. 0780-1-54-.04(2)(c), an excess of loss agreement with Safety was entered into effective July 1, 2001, to limit the liability of TABCOMP Trust for workers' compensation and employers' liability claims. Under the

agreement, the excess insurer agreed to indemnify TABCOMP Trust against individual losses in excess of the specific retention, and for the sum of all losses and claims expenses in excess of the aggregate retention subject to an annual aggregate indemnity. During the period of examination, TABCOMP Trust maintained excess of loss coverage and each policy period had different retentions and levels of loss share. Below is a summarization of TABCOMP Trust's liability with respect to workers compensation losses under the original and renewal excess of loss agreements:

| Excess Ins. Policy Year | Specific Retention | Aggregate Indemnity | Aggregate Retention | Insurer |
|---|---|---|---|---|
| 7/01-12/02 | $250,000 | $3,000,000 | 80% of man. prem. | Safety National Casualty Corp. |
| 1/03-12/03 | $300,000 | $3,000,000 | 85% of man. prem. | Safety National Casualty Corp. |
| 1/04-12/04 | $300,000 | $3,000,000 | 85% of man. prem. | Safety National Casualty Corp. |

The policies provide coverage for losses sustained by TABCOMP Trust as a result of injury by accident occurring during the policy period or by disease caused or aggravated by exposure to conditions causing the disease occurring during the policy period. During the period of examination, TABCOMP Trust has had no claims to reach the specific attachment point of the excess coverage on either a paid or incurred basis, and the attachment point of the aggregate coverage is not expected to be penetrated for any period covered by this examination.

The excess policies have provisions for the continuation of coverage in the event of plan insolvency. The agreements do not relieve TABCOMP Trust from its obligations to its members and the failure of the excess insurer to honor its obligations would result in additional losses to TABCOMP Trust. The policies were written by Safety, a company authorized to do business in Tennessee. Examination procedures included verification that TABCOMP Trust renewed coverage with Safety subsequent to the examination date.

## Loss Experience

The following table depicts the ratio of losses and loss expenses and general and administrative expenses to premium revenue for TABCOMP Trust and its predecessor, TABSSIT:

| TABSSIT | Premiums Earned | Losses & ALAE | Und. Ratio | Sell., Gen. & Admin. Exp. | S,G, & A Exp. To Premium | Investment & Other Income | Combined Loss Ratio |
|---|---|---|---|---|---|---|---|
| 1992 | 2,072,936 | (1,263,858) | 61.0% | (751,817) | 36.3% | 22,052 | 96.2% |
| 1993 | 4,227,045 | (3,059,510) | 72.4% | (1,471,220) | 34.8% | 73,916 | 105.3% |
| 1994 | 7,524,406 | (5,939,569) | 78.9% | (2,263,870) | 30.1% | 192,917 | 106.3% |
| 1995 | 10,587,305 | (6,776,069) | 64.0% | (2,963,198) | 28.0% | 434,023 | 88.4% |
| 1996 | 9,955,839 | (6,382,499) | 64.1% | (2,849,822) | 28.6% | 563,339 | 87.8% |
| 1997 | 6,147,409 | (3,750,000) | 61.0% | (1,947,632) | 31.7% | 434,909 | 86.6% |
| 1998 | 4,085,301 | (2,710,000) | 66.3% | (1,443,460) | 35.3% | 408,114 | 92.4% |
| | 44,600,241 | (29,881,505) | 67.0% | (13,691,019) | 30.7% | 2,129,270 | 93.2% |
| **TABCOMP Trust** | | | | | | | |
| 2001 | 174,846 | (150,220) | 85.9% | (56,837) | 32.5% | 0 | 118.4% |
| 2002 | 4,313,195 | (2,316,050) | 53.7% | (1,387,900) | 32.2% | 24,669 | 85.4% |
| 2003 | 5,847,963 | (3,805,008) | 65.1% | (1,998,036) | 34.2% | 63,520 | 98.2% |
| | 10,336,004 | (6,271,278) | 60.7% | (3,442,773) | 33.3% | 88,189 | 93.2% |

The above table was derived from amounts included in the audited financial statements and actuarial reports filed with the Department of Commerce and Insurance for the years indicated. Only the operations of TABCOMP Trust were subject to examination by the Department of Commerce and Insurance, and TABCOMP Trust's December 31, 2003 financial statement is included at the end of this examination report.

## Accounts and Records

During the course of examination, such tests and examination procedures were made as were considered necessary, including substantial verification of postings, extensions and footings, and reconciliation of subsidiary ledgers to control accounts. General ledger trial balances were reconciled with corresponding copies of financial statements filed for the period under examination and financial statements filed for the years under examination were reviewed for completeness of disclosure. This review revealed no material omissions.

Financial statements conform to Generally Accepted Accounting Principles as permitted by the Department of Commerce and Insurance. Said statements appear to reflect properly the operations during the period under examination and the status of the Fund at the date of examination except as commented upon elsewhere in this exam report.

Financial records and reports are maintained and produced by TABCOMP Trust and by TAB Service Corporation. TABCOMP Trust contracts with a local actuarial firm to periodically perform an evaluation of loss and loss expense reserves. TABCOMP Trust retains an independent accounting firm to compile the financial statements, perform an annual audit on the financial statements and to prepare its federal income tax return.

## Litigation, Contingent Liabilities and Subsequent Events

Just prior to year end 2003, a dispute arose between TABCOMP Trust, its sponsoring association (TCCI), and its service organization (TAB Service Corporation). Efforts to resolve the dispute included application to the Department of Commerce and Insurance to form a new trust (which was later rescinded) and settlement of a related lawsuit. TABCOMP Trust and TCCI also reached an agreement for TABCOMP Trust to begin making royalty fee payments to TCCI based on 1% of TABCOMP Trust's premiums.

On January 1, 2004, TABCOMP Trust appointed Will Hord as its Administrator, and on May 25, 2004, Mr. Hord was replaced by George Davis as Administrator. Effective May 27, 2004, the Board of Trustees canceled the Service Agreement in effect with TAB Service Corporation. All of the management and administrative services previously provided under the TAB Service Corporation agreement continued to be performed by the same employees which became employees of TABCOMP Trust and worked under the direction and supervision of Mr. Davis, who also became a direct employee of TABCOMP Trust. Mikhel Lindsley, Controller for TABCOMP Trust, was named interim Administrator on August 1, 2004.

Pursuant to an agreement between TABCOMP Trust and TCCI, TABCOMP Trust and CCMSI entered into an Administrator Agreement on October 25, 2004, which became effective on November 1, 2004, for a term of thirty-eight months. It provides that CCMSI is responsible for the daily management and administration of TABCOMP Trust. Compensation for CCMSI is equal to an agreed percentage of collected member contribution subject to a specified minimum audited premium amount. The payment of fees less reimbursement for office lease expenses, furniture and equipment and software is to be monthly. Almost all employees of TABCOMP Trust, which were

formerly employees of TAB Service Corporation, became employees of CCMSI on or about November 1, 2004, the effective date of the Administrator Agreement.

## 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. TABCOMP Trust's Board, on November 7, 2003, approved the distribution of a "dividend totaling $300,000" which was paid in January 2004. The dividend payment was a return of surplus from the 2002 policy year operations and was approved by the Department of Commerce and Insurance prior to payment. Every Member from the 2002 policy year participated in the refund proportionately to their annual premium without any restrictions or qualifications in accordance with Tenn. Comp. R & Regs. 0780-1-54-.16(2).

TABCOMP Trust, in limited situations, places a risk in their "loss sensitive program." This is a plan that allows select Members to have some portion of their premium returned to them if certain predetermined levels of loss ratios are achieved. For example, if a participating Member's loss ratio for the policy year is 40% or less, they would be entitled to a "refund" equal to 20% of their annual premium. The refunds are considered "discounts" and paid to the member approximately six months after the end of the fund year. There were no members placed in the loss sensitive program in the 2001 policy year. TABCOMP Trust had five members participate in the program in the 2002 policy year, four of which received "refunds" in 2003 totaling $179,112. TABCOMP Trust had six members participate in the program in the 2003 policy year, three of which received "refunds" in 2004 totaling $226,828 (refer to Underwriting & Rating comment number "4" on page 36 for a more thorough description of TABCOMP Trust's use of this program).

The following table is a summary of the (a)surplus distributions and (b)loss sensitive premium refunds distributed by TABCOMP Trust during and subsequent to the period of examination:

| | Payments for Fund Years Ending December 31, | | |
|---|---|---|---|
| Year Paid | 2002 | 2003 | Total |
| 2003 | (b) 179,112 | | $ 179,112 |
| 2004 | (a) 300,000 | (b) 226,828 | 526,828 |
| Total | $ 479,112 | $ 226,828 | $ 705,940 |

## Financial Statement

There follows a Balance Sheet and a Statement of Operations as of December 31, 2003, together with a Reconciliation of Members' Equity for the period under review, as established by this examination. For purposes of this examination, Members Distributions Payable is being included in the Members' Equity section of these financial statements to more clearly summarize the members' financial interest in and responsibility to the Trust. The Trust reported this amount as a liability in its financial statements filed with the Department of Commerce and Insurance.

# TENNESSEE ASSOCIATION OF BUSINESS COMPANY OWNERS' MANAGED PROGRAM
## STATEMENT OF FINANCIAL POSITION
## DECEMBER 31, 2003

### ASSETS

| | Balance per Trust | Examination Adjustments | Balance per Examination |
|---|---|---|---|
| Cash and cash equivalents | $1,080,806 | | $1,080,806 |
| Investments in debt securities available-for-sale | 3,503,518 | | 3,503,518 |
| Deposit with bonding company | 300,000 | | 300,000 |
| Premiums receivable | 352,898 | | 352,898 |
| Accrued interest receivable | 33,458 | | 33,458 |
| Prepaid expenses | 11,265 | | 11,265 |
| Refundable income taxes | 9,971 | | 9,971 |
| Deferred federal income taxes | 106,156 | | 106,156 |
| Total assets | 5,398,072 | | 5,398,072 |

### LIABILITIES AND MEMBERS' EQUITY

| | | | |
|---|---|---|---|
| Liabilities | | | |
| Unpaid losses & loss adjustment expenses | 3,338,538 | | 3,338,538 |
| Member distribution payable | 755,666 | $755,666 | |
| TABSSIT members' surplus | | (890,476) | 890,476 |
| Overpayments by members | 269,505 | | 269,505 |
| Accounts payable and other accrued expenses | 181,524 | | 181,524 |
| Reserve for loss sensitive premium refunds | | (226,828) | 226,828 |
| Loss contingency for dispute with TCCI | | (185,000) | 185,000 |
| Total Liabilities | 4,545,233 | (546,638) | 5,091,871 |
| Members' Equity | | | |
| Policyholders' surplus before accumulated other comprehensive earnings | 852,839 | 852,839 | |
| Member distribution payable | | (261,476) | 261,476 |
| Restricted fund balance | | (44,725) | 44,725 |
| Total Members' Equity | 852,839 | 546,638 | 306,201 |
| Total Liabilities & Members' Equity | $5,398,072 | | $5,398,072 |

# TENNESSEE ASSOCIATION OF BUSINESS COMPANY OWNERS' MANAGED PROGRAM
## STATEMENT OF INCOME & COMPREHENSIVE EARNINGS
## FOR THE YEAR ENDED DECEMBER 31, 2003

| | | |
|---|---|---|
| Revenues | | |
| Premiums | $ 5,621,135 | |
| Investment income | 52,342 | |
| Total revenues | | $ 5,673,477 |
| Expenses | | |
| Claims and claim adjustments | 3,604,728 | |
| Excess insurance | 481,006 | |
| Agents' commissions | 407,955 | |
| Administrative service fee | 380,878 | |
| Claims adjusting fee | 292,398 | |
| State assessments | 140,351 | |
| Loss control | 116,959 | |
| Administrator fee | 100,000 | |
| Loss contingency | 185,000 | |
| Other expenses | 74,487 | |
| Total expenses | | 5,783,762 |
| Net income before member distribution and provision for income taxes | | (110,285) |
| Member distribution | | 27,811 |
| Provision for income taxes | | |
| Current income tax benefit | 30,522 | |
| Deferred income tax benefit | 51,952 | 82,474 |
| Net Income | | 0 |
| Other comprehensive earnings, net of tax | | |
| Unrealized holding gain arising during the period, net of deferred taxes of $10,638 | (5,291) | |
| Add: decrease in accrual of unrealized gain as distributable to members | 5,291 | 0 |
| Comprehensive earnings | | $0 |

TENNESSEE ASSOCIATION OF BUSINESS
COMPANY OWNERS' MANAGED PROGRAM
STATEMENT OF CHANGES IN POLICYHOLDERS' SURPLUS
FOR THE YEAR ENDED DECEMBER 31, 2003

| | 2001 | 2002 | 2003 |
|---|---|---|---|
| Member Distribution Payable | | | |
| Balance at December 31 prior year | $0 | $0 | $556,052 |
| Change from results of operations | | 530,110 | (27,811) |
| Increase for unrealized gain on securities | | 25,942 | (5,291) |
| Dividends paid to Members | | | (179,112) |
| Reclass to "Policyholders' Surplus (TABSSIT)" | | | (37,637) |
| Reclass to "Restricted Fund Balance" | | | (44,725) |
| Balance at December 31 | 0 | 556,052 | 261,476 |
| Restricted Fund Balance | | | |
| Balance at December 31 prior year | 0 | 0 | 0 |
| Reclass from "Distributions Due Members" | | | 44,725 |
| Balance at December 31 | 0 | 0 | 44,725 |
| Total members equity, December 31 | $0 | $556,052 | $306,201 |

## Analysis of Changes in Financial Statement

TABSSIT Members' surplus held by TABCOMP Trust ..... $ 890,476

The above account is a newly designated account and the amount per examination is the total of the amount actually belonging to former Members of TABSSIT, the previous trust. The balance includes $852,839 previously reported as "Policyholders' Surplus" and $37,637 reclassified from "Members Distributions Payable" attributable to the Trust's treatment of the 2001 operating loss which was improperly taken from surplus funds belonging to members of TABSSIT. (See "Payment of Refunds" on page 33 of this examination report for a more thorough explanation and a recommendation for corrective action.)

Policyholders' surplus before accumulated other comprehensive earnings ..... $ 0

The above amount is $852,839 less than reported by TABCOMP Trust in its December 31, 2003 financial statement. As noted above, the balance which was reported as equity has been reclassified as a liability owed to the former Members of TABSSIT, the Trust's predecessor.

Accrual for subsequent event: settlement of dispute with TCCI ..... $ 185,000

The above account is a newly designated account established per this examination. The 2003 audited financial statements submitted by TABCOMP Trust to the Department of Commerce and Insurance disclosed that a dispute over sponsorship fees between TABCOMP Trust and TCCI had arisen which raised substantial doubt about TABCOMP Trust's ability to continue as a going concern, but that the financial statements did not include any adjustments that might result from the outcome of this uncertainty.

Subsequent efforts to settle the dispute and a related lawsuit caused TABCOMP Trust to incur additional non-recurring expenses of approximately $185,000. These additional expenses which represent the amount TABCOMP Trust subsequently paid in 2004 are being recognized in the financial statements of this examination report to keep the statements from being misleading.

Reserve for loss sensitive premium refunds ..... $ 226,828

The above account is a newly designated account established per this examination. As noted earlier in this report, TABCOMP Trust's "loss sensitive program" allows them to return some portion of premium as a "discount" to select Members subsequent to the policy year end if certain predetermined levels of loss ratios are achieved. For the 2003 policy year, TABCOMP Trust refunded premium totaling $226,824 to three Members which were in this program. TABCOMP Trust did not account for these refunds in their financial statements submitted to the Department of Commerce and Insurance however they are being recognized as a liability in the financial statements of this examination report.

Restricted fund balance ..... $ 44,725

The above amount was established as a result of this examination. It represents the "surplus" from the 2002 and 2003 fund years which was declared by the Board of Trustees as payable to the Members, but is not yet allowed by Tenn. Comp. R & Regs. to be declared as "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. However, the Board of Trustees must declare the refund not less than twelve months after the end of the fund year and if the refund is declared, 10% of the refundable amount must be retained by the pool to cover any obligations that may not yet have been reported. TABCOMP Trust declared and reported dividends for 2002 and 2003 approximately fourteen months prior to their date of eligibility per Tenn. Comp. R. & Regs. See "Declaration of Refunds" on page 32 of this examination report for a more thorough description and a recommendation for corrective action.

Member Distributions Payable ..... $ 261,476

The above amount as established per examination is $494,190 less than reported by TABCOMP Trust in its December 31, 2003 financial statements. The difference is the result of the examination adjustments noted above and summarized as follows:

| | |
|---|---|
| Member Distribution Payable, balance reported by TABCOMP Trust | $755,666 |
| Examination Adjustments: | |
| Premium discounts for "loss sensitive" policies | (226,828) |
| Expenses to settle dispute with TCCI | (185,000) |
| Net loss for 2001 charged against TABSSIT surplus | (37,637) |
| Regulatory refund restrictions | (44,725) |
| Member Distribution Payable, balance per examination | $261,476 |

## Comments

1. Formation of "TABCOMP" Trust

Tenn. Code Ann. § 50-6-405(c)(1) requires an initial group of at least ten employer members to qualify as self insurers. Tenn. Comp. R & Regs. 0780-1-54-.04(i) requires proof of payment to the group by each member of not less than 25% of that member's first year estimated annual net premium as of the effective date of formation of the Trust. TABCOMP Trust misrepresented to the Department of Commerce and Insurance that it satisfied the eligibility requirements to form a trust in accordance with Tenn. Comp. R & Regs.. It neither had the requisite number of members upon their formation, nor did the members they had pay the required amount of premium to TABCOMP Trust with their application. TABCOMP Trust filed Indemnity Agreements and Member's Applications for Membership with the Department of Commerce and Insurance indicating that they had only seven Members effective July 1, 2001. However, many of these did not become premium paying Members of TABCOMP Trust until January 1, 2002. When TABCOMP Trust began operations on July 1, 2001, it actually had only one Member who was essentially acting as a single self insured employer.

Will Hord, Chairman of the Board of Trustees, signed the "Employers' Application for Group Coverage" submitted to the Department of Commerce and Insurance on May 30, 2001 requesting approval for a certificate of authority effective July 1, 2001. Six other members of the Board of Trustees were designated in the "Declaration of Trust and Bylaws" which was submitted with the application. None of the members of the Board of Trustees were Members of TABCOMP Trust on its effective date of formation which was in violation of Tenn. Comp. R & Regs. and the Trust's Bylaws, both of which require at least two-thirds of the Board to be Members of the Trust. One Trustee joined TABCOMP Trust effective September 15, 2001 and the remaining Trustees did not become Members of TABCOMP Trust until January 1, 2002.

2. Administrator

Beginning with the formation of TABCOMP Trust effective July 1, 2001, Carter Witt was TABCOMP Trust's designated Administrator and TAB Service Corporation the designated Service Company. Mr. Witt was president of TAB Service Corporation while

he served as Administrator for TABCOMP Trust. This relationship was in violation of Tenn. Comp. R & Regs. 0780-1-54-.09 which state: "no administrator or its employees, officers or directors shall be an employee, officer or director of, or have either a direct or indirect financial interest in, a service company." Mr. Witt received compensation from TAB Service Corporation as an employee while serving as Administrator for TABCOMP Trust, but received no additional compensation from TABCOMP Trust for his contracted "administrative" duties. Beginning in October 2002, Mr. Witt was no longer affiliated with TAB Service Corporation but continued to serve as Administrator for TABCOMP Trust through December 31, 2003, the date of this examination. The Trust paid fees to the Administrator of $100,000 per year during this period; however almost all services required of the Administrator continued to be provided by TAB Service Corporation.

Will Hord, a former chairman of the Board of Trustees, was appointed Administrator effective January 1, 2004, and administrative duties continued to be provided primarily by TAB Service Corporation. Contractual responsibilities of the Administrator and of TAB Service Corporation did not change with the change in Administrator, but the fee was reduced from $100,000 per year to $12,000 per year. Mr. Hord resigned as Administrator effective May 28, 2004, and although he was no longer affiliated with TABCOMP Trust, Mr. Hord was compensated for administrative fees for seven months after his departure.

George Davis was appointed Administrator effective May 25, 2004, and served as such until his resignation effective July 31, 2004. Effective August 1, 2004, Mikhel Lindsley was appointed Interim Administrator. Both had been employees of TAB Service Corporation since inception of TABCOMP Trust, and had provided or overseen the provision of most of the administrative services during Mr. Witt's and Mr. Hord's tenures as Administrators. Both also became employees of TABCOMP Trust after the contract with TAB Service Corporation was cancelled on April 27, 2004 effective May 27, 2004.

The Trust's current Administrator is CCMSI and their appointment was effective November 1, 2004. CCMSI is paid a percentage of premiums for their services which include (1) general administrative duties (regulatory and account management functions), (2) claims administration, (3) risk management services, (4) loss control

services, and (5) managed care services. Within their application to be Administrator, which was filed with the Department of Commerce and Insurance , they agree that they will not be pecuniarily interested in any sale, purchase, exchange, reinsurance or other similar transaction or property of the Pool, or take or receive for his or their own use any fee, brokerage, commission, gift or other consideration of the Pool except in accordance with Tenn. Code Ann. Title 50, Chapter 6, or for reasonable compensation for services performed or sales or purchases made to or for the Pool in accordance with the terms of a contract approved by the Commissioner.

CCMSI is the broker of record for TABCOMP Trust's excess insurance policy, and TABCOMP Trust's agent for both their surety bond and directors and officers liability policy, receiving commissions for each. Their Administration Agreement also specifies that they will provide TABCOMP Trust with managed care services upon mutual agreement of the parties, and there is a schedule of managed care services and fees attached to the agreement. Receiving compensation in addition to administrative fees for these services contradicts the pecuniary interest terms of their application to serve as Administrator they filed with the Department of Commerce and Insurance.

3. Unclaimed Property

TABCOMP Trust's predecessor, TABSSIT, did not submit any unclaimed property reports to the State of Tennessee ("State") during the period of its operations which were prior to this examination. As a result, TABCOMP Trust is holding these funds which should have already been remitted to the State in accordance with Tenn. Code Ann. Title 66, Chapter 29. TABCOMP Trust is in the process of identifying these escheatable funds for purposes of remitting them to the State on behalf of TABSSIT beginning with the next reporting period. TABCOMP Trust does not yet have an unclaimed property reporting obligation because it has been in existence for less than five years.

## Recommendations

1. Corporate Records

The original Board of Trustees was empowered by the "Declaration of Trust and Bylaws." Thereafter, Tenn. Comp. R & Regs. provide that Board Members are to be elected by the Members of the Trust. The following are exceptions to Tenn. Comp. R & Regs. which were noted through the examiners review of minutes to Board of Trustees and Members meetings.

1. At a meeting held on January 25, 2002, the Board of Trustees elected Mike Griffin.
2. At a meeting held on January 25, 2002, Rick Francis was listed as a Board of Trustee member. The examiners could find no evidence in TABCOMP Trust's corporate records of his election to the Board of Trustees.
3. At a meeting held on October 8, 2004, the Board of Trustees accepted Lynn Johnson and Chris Karbowiak as Board of Trustee members.

The manner of election of the above Board of Trustee members is inconsistent with the Bylaws and Tenn. Comp. R & Regs.. Pursuant to Tenn. Comp. R & Regs. 0780-1-54-.07 and TABCOMP Trust's Bylaws, it is recommended that TABCOMP Trust's Board of Trustee members be elected by TABCOMP Trust membership.

2. Declaration of Refunds

TABCOMP Trust's Board of Trustees voted on October 25, 2002 to "declare as payable to the Members any and all surplus that exists as of December 31, 2002" but that "the exact amount of this dividend is currently unknown as the year-end accounting is not complete." The Board of Trustee's intent is "that all surplus funds be returned to the members therefore the surplus funds that arose during the year should be recorded as an expense on the income statement with the unpaid portion of these amounts added to the liabilities on the balance sheet...and that the Fund will never retain any surplus." The Board' of Trustee's declaration of these amounts as dividends was made fourteen months prior to their eligibility pursuant to Tenn. Comp. R & Regs. 0780-1-54.16 which specifies dividends may not be declared less than twelve months after the end of the fund year. TABCOMP Trust accounted for the surplus attributed to the 2003 policy year similarly in its financial statements, but there is no evidence recorded in the

minutes to the meetings of TABCOMP Trust's Board of Trustees that they ever declared these amounts payable to the Members.

It is the opinion of the examiners that TABCOMP Trust's practice of treating the surplus attributable to its current year of operations as dividends immediately payable to its members is being done prior to the date of eligibility per Tenn. Comp. R & Regs., and that these restricted funds are being misreported as "Distributions Due Members" in TABCOMP Trust's financial statements. It is recommended that, in the future, TABCOMP Trust comply with Tenn. Comp. R & Regs. in declaration of refunds payable to its Members.

3. Payment of Refunds

TABCOMP Trust's predecessor, TABSSIT, ceased operations effective December 31, 1998. Although TABSSIT has not been active since this date, its certificate of approval was never terminated and remains in effect in accordance with Tenn. Comp. R & Regs. 0780-1-54-.05. Management represented to the examiners that there are no plans for TABSSIT's reactivation, therefore it is recommended that management take the necessary steps to terminate the certificate of authority of TABSSIT in accordance with Tenn. Comp. R. & Regs., and that any remaining surplus funds be returned to its former members in accordance with TABSSIT's Bylaws and the "Indemnity Agreement and Power of Attorney" binding on each former Member. These surplus funds were previously declared as refunds payable to its former Members by TABSSIT's Board of Trustees and presented as such in financial statements submitted to the Department of Commerce and Insurance.

TABSSIT executed a loss portfolio contract with their excess insurance carrier, Safety, when operations ceased December 31, 1998. However, TABSSIT's administrator, TAB Service Corporation, continued to service all transferred claims for Safety under a "TPA Service Agreement." They also made efforts to keep the TABSSIT membership together by putting together a program whereby replacement workers compensation coverage was provided to TABSSIT Members through the voluntary market directly by Safety. TAB Service Corporation continued to administer this program by serving as the manager for Safety and provided production, loss control,

premium collection, claims administration and accounting services under an "Operating Agreement."

According to TABSSIT's audited financial statements that were filed with the Department of Commerce and Insurance, it accumulated approximately $3.4 million in surplus as a result of its operations from 1992 through December 31, 1998. Beginning in 1999, the majority of these TABSSIT reserve funds were returned to TABSSIT's former members by TAB Service Corporation in the form of refunds. Authority for refunds is contained in Tenn. Comp. R. & Regs. 0780-1-54-.16 which provides that any monies for a fund year in excess of the amount necessary to fund all obligations for that fund year may be refunded to the members. TAB Service Corporation distributed the TABSSIT refunds as follows:

| Date Paid | Amount |
|---|---|
| 1999 | $ 906,290 |
| 2000 | 1,169,821 |
| 2001 | 605,901 |
| Total | $ 2,682,012 |

Beginning in 1999, TAB Service Corporation and the former Board of Trustees of TABSSIT implemented a refund policy whereby Trust members that did not transition into the Safety program would be ineligible to participate in the premium refunds. This action by the administrator and TAB Service Corporation created a conflict of interest because refund eligibility was contingent on TABSSIT Members purchasing replacement coverage from Safety's program which was being managed by TAB Service Corporation. It is the opinion of the examiners that this action was also in violation of Tenn. Comp. R. & Regs. 0780-1-54-.16 (2) which states payment of a refund based on a previous fund year shall not be contingent on continued membership in the group after that fund year. As such, many former TABSSIT members that did not purchase coverage from Safety did not receive the dividend distributions to which they were entitled.

TABCOMP Trust is currently holding approximately $900,000 of TABSSIT surplus funds according to audited financial statements filed with the Department of

Commerce and Insurance. It is therefore recommended that this be distributed to former TABSSIT members after TABSSIT's dissolution, and that priority should be given to those Members who were not allowed to participate in the first three dividend distributions to the extent that they receive their share of distributions which were previously and improperly withheld.

Tenn. Comp. R. & Regs. 0780-1-54-.16 requires each member to be given a written description of the Trust's refund plan at the time of their application for membership. TABCOMP Trust's Indemnity Agreement and Power of Attorney agreed to and signed by each member provides only a general description of TABCOMP Trust's refund policy by stating "remaining funds of the Trust shall be distributed to Members in such manner as the Trust shall deem equitable which includes limiting distribution to Members with a loss ratio not in excess of a level designated by the Board, and/or providing that any Member may share in prorate distribution of dividends regardless of when such dividends are declared so long as such Member participated during the year for which the distribution is made." The examiners could not find any evidence that TABCOMP Trust has ever provided its members with a clear description of its refund plan and it is recommended that this be done by management in conjunction with each new and renewal policy application. It is also recommended that TABCOMP Trust refrain from implementing refund plans with restrictive terms prior to their effective date.

4. Underwriting and Rating

TABCOMP Trust had 8, 79 and 88 Members participate in the Fund during the 2001, 2002 and 2003 policy years which were covered by this examination. The examiners' review of a sample of the Members' rating calculations made by TABCOMP Trust during this period revealed the following exceptions:

1. Tenn. Code Ann. § 50-9-104 specifies the eligibility requirements for a 5% drug free workplace premium credit. The examiners conducted an extensive review of TABCOMP Trust's premium and rating procedures and noted only one exception to this policy. In 2002, TABCOMP Trust allowed an ineligible Member, Quad Industries, to receive the full drug free workplace credit. It is recommended that, due to the unauthorized discount, an adjustment be made to this Member's premium billing.

2. As noted earlier in this report, TABCOMP Trust applies schedule-rating factors to Members' premium in such a manner as to adjust the estimated premium to make the expected loss ratio fit within an established target range. This method was applied fairly and consistently to all members during the period of examination; however TABCOMP Trust's adjustments are dependent solely on members' past experience. The procedure does not appear to comply with NCCI schedule rating guidelines, has not been approved by the Department of Commerce and Insurance and does not appear to have been formally approved by TABCOMP Trust's Board of Trustees. Per Tenn. Comp. R. & Regs. 0780-1-54-.15, it is recommended that TABCOMP Trust adhere to established NCCI procedures in application of its schedule rating adjustments to premium.

3. Recalculations of five members audited premium amounts resulted in differences in the amount of Stock Discount (Premium Volume Discount) applied. All five members received discounts slightly above the amount they were entitled to per NCCI procedures, and all policies were for terms of less than a full year. The estimated premiums were annualized for application of all credits and debits, including stock discounts, and then prorated to the actual term of the policy. The calculation of the stock discount was consistent for all members that had partial year policies. These differences occurred in the 2001 and 2002 policy years and the total amount of difference amounted to $2,078 and $2,753 respectively. It is recommended that, in the future, TABCOMP Trust adhere to NCCI procedures by applying premium volume discounts to actual premium amounts instead of annualized amounts.

4. As noted earlier in this report, TABCOMP Trust makes a "loss sensitive" program available to some of its Members. Decisions to place or keep members in the program are not based on any established procedures and some are more a factor of market/competitive forces. Amounts returned are considered "underwriting discounts" and paid from funds labeled "Members Distributions Payable," which is comprised of surplus funds declared by the board as payable to Members. It is the opinion of the examiners that this loss sensitive program is essentially a form of "retrospective rating" as defined in the NCCI rating manuals. The NCCI procedures for retrospective rating are very detailed and the simplistic manner in which TABCOMP Trust administers its loss sensitive program is not consistent with these procedures. In addition, the practice of applying "stock discounts" to members in the loss sensitive program is inconsistent with NCCI procedures which specify that premium subject to retrospective rating is not eligible for discounts.

   It is the opinion of the examiners that it is inappropriate for TABCOMP Trust to use retrospective rating. Self insured trusts operate with the purpose of eventually returning all profits to its members; however retrospective rating gives specific members priority in receipt of refunds. The use of retrospective rating also creates the possibility that TABCOMP Trust could be obligated to return premium to participating members in a policy year in which TABCOMP Trust was not profitable, which would require an assessment of the non-participating membership. Furthermore, TABCOMP Trust's application of its loss sensitive

program was not considered by their independent actuaries in the determination of their loss cost multiplier. It is recommended that TABCOMP Trust's administrator obtain approval from the Department of Commerce and Insurance and its Board of Trustees for any future application of its loss sensitive program. It is also recommended that the loss sensitive refunds previously returned by TABCOMP Trust which were accounted for as Members' Distributions should instead be accounted for as a reduction to premium with corresponding offsets to expenses which are a function of written premium.

5. Policy Issuance

The following problems were noted as a result of a review of TABCOMP Trust's 2005 policy year issues and renewals:

1. TABCOMP Trust renewed coverage for Texas Boot in January 2005, but the required down payment of premium was never made. Based on the language of TABCOMP Trust's policies and Tenn. Comp. R. & Regs., coverage was not able to be canceled until 30 days after their cancellation notice was mailed on March 15, although no premium was ever paid by the Member.
2. TABCOMP Trust's Board of Trustees allowed coverage to be bound for Elite Trailer prior to the receipt of the required complete Member's application package (which includes member financial statements). Without these documents, it was impossible for TABCOMP Trust to apply required underwriting procedures to this account prior to policy issuance. This action was in violation of the Trust's Bylaws, NCCI Procedures and Tenn. Comp. R. & Regs. 0780-1-54-.08(1) which provide an employer joining a workers' compensation self-insurance group shall: (a) submit an application for membership to the board of trustees or its administrator and (b) enter into the indemnity agreement required by the Rules. Membership takes effect no earlier than each member's date of approval. The application for membership and its approval shall be maintained as permanent records of the Board of Trustees.

It is recommended that TABCOMP Trust's Board implement procedures that prevent its obligation to provide coverage to non premium paying Members, and refrain from issuing policies to Members prior to their required application, review and approval processes are complete.

6. Termination of Service Company Agreement

The service company agreement between TABCOMP Trust and TAB Service Corporation specifies that claims covered by TABCOMP Trust during the term of the agreement will be handled for twenty-four months after cancellation or expiration of the agreement. If the agreement expires or is terminated, all applicable books, records and

files of TABCOMP Trust shall promptly be, at the choice of TABCOMP Trust, transferred to TABCOMP Trust or a designated third party, or will be retained for continued service by TAB Service Corporation for a period of time not to exceed twenty four months. The service agreement was cancelled effective May 27, 2004, but TABCOMP Trust released TAB Service Corporation from this provision in their contract. The employees of TAB Service Corporation became employees of TABCOMP Trust and all services previously provided by TAB Service Corporation were performed directly by TABCOMP Trust employees.

The provision for incurred losses in TABCOMP Trust's financial statements includes an estimate for losses and allocated loss adjustment expenses ("ALAE") only. ALAE are those expenses, such as litigation costs, which can be directly attributed to a specific claim. Unallocated loss adjustment expenses ("ULAE") that cannot be directly associated with a particular claim such as administrative expenses, consulting fees and claims handling fees are not included in the estimates. Since TABCOMP Trust released TAB Service Corporation from its contractual obligation to perform these services upon the termination of its service contract, it is recommended that TABCOMP Trust establish a provision for ULAE in its reserve liability equal to the expected cost of settling all open claims.

## Conclusion

The customary insurance examination practices and procedures, as promulgated by the National Association of Insurance Commissioners, have been followed in connection with the verification and valuation of assets and the determination of the liabilities of the Fund of TABCOMP Trust.

In such manner, it was found that as of December 31, 2003, TABCOMP Trust had assets of $5,398,072 and liabilities, exclusive of member's equity, of $5,091,871. Thus, there existed a surplus of $306,201 in the form of restricted funds and Member Distributions Payable. As noted earlier in this examination report under the section "Refunds," TABCOMP Trust made a $300,000 distribution to its Members in January 2004 subsequent to the date of this examination. The effect of this transaction without regard to TABCOMP Trust's other operations was to leave it with remaining surplus of $6,201.

The courteous cooperation of the officers and employees of TABCOMP Trust's administrator, its independent accountants and its actuarial consulting firm extended during the course of examination is hereby acknowledged.

In addition to the undersigned, Mr. Michael Lamb, AIE, Insurance Examiner II and Ms. Amy Elliott, Insurance Examiner II, with the State of Tennessee Department of Commerce and Insurance, participated in the work of this examination.

Respectfully submitted,

Mark E. Jaquish, CFE, CPA
Insurance Examiner
State of Tennessee

Examination Affidavit

The undersigned deposes and says that he has duly executed the attached examination report of TABCOMP Trust dated May 4, 2005, and made as of December 31, 2003, on behalf of the 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.

Mark Jaquish, CFE, CPA
Insurance Examiner
State of Tennessee

County Davidson
State Tennessee

Subscribed and sworn to before me
this 16th day of
June, 2005.

Helen H. Dorsey
(Notary)

TABCOMP TRUST
Workers' Compensation Self Insured Fund

Sponsored by Tennessee Chamber of Commerce

750 Old Hickory Blvd.
Building 2, Suite 100
Brentwood, TN 37027
Phone: 615.370.5964
Toll Free: 866.295.6689
Fax: 615.377.0946

EXHIBIT
B

July 5, 2005

RECEIVED
JUL 06 2005
Dept. Of Commerce & Insurance
Company Examinations

Don Spann
State of Tennessee
Department of Commerce & Insurance
500 James Robertson Parkway – 4th Floor
Nashville, TN 37243-1135

Re: Comments related to state audit recommendations

Dear Mr. Spann:

Thank you for providing us with a final copy of the state audit dated June 16, 2005. The following are comments of compliance, correction and rebuttal to the final audit's recommendations. Per your instructions, we have quoted the state examination, with page numbers, followed by our response.

**Comment 1 concerning Litigation, Contingent Liabilities, and Subsequent Events (p20) and Accrual for subsequent event: settlement of dispute with TCCI (p26):**

Litigation, Contingent Liabilities and Subsequent Events (p20)

Just prior to year end 2003, a dispute arose between TABCOMP Trust, its sponsoring association (TCCI), and its service organization (TAB Service Corporation).

Accrual for subsequent event: settlement of dispute with TCCI (p26)..... $ 185,000

The above account is a newly designated account established per this examination. The 2003 audited financial statements submitted by TABCOMP Trust to the Department of Commerce and Insurance disclosed that a dispute over sponsorship fees between TABCOMP Trust and TCCI had arisen which raised substantial doubt about TABCOMP Trust's ability to continue as a going concern, but that the financial statements did not include any adjustments that might result from the outcome of this uncertainty.

Subsequent efforts to settle the dispute and a related lawsuit caused TABCOMP Trust to incur additional non-recurring expenses of approximately $185,000. These additional expenses which represent the amount TABCOMP Trust subsequently paid in 2004 are being recognized in the financial statements of this examination report to keep the statements from being misleading.

**TABCOMP Trust was not involved in a dispute with either its sponsoring association (TCCI) or its service organization (TAB Service Corporation) in 2003.**

**The audited financial statements for the year ended December 31, 2003, are dated June 9, 2004. As of the completion of the audited financial statements, there**

was no lawsuit filed against TABCOMP Trust, nor even a threat of a lawsuit filed against TABCOMP Trust. At best, any potential litigation was a contingent liability, at best. In order for a contingent liability to be accrued, there are two tests set forth in the *Standards of Financial Accounting Statements No. 5.* These include the following:

1) Payment of the liability must be probable.
2) A liability must be able to be reasonably estimated.

Considering the fact that there was not even a lawsuit, or a threat of a lawsuit, as of the date of the financial statements (June 9, 2004), there is no way that TABCOMP had the requirement for an accrual of a liability as of December 31, 2003. There is nothing in generally accepted accounting principles that require restatement of a financial statement for something of this nature.

It must be completely understood that the going concern language in the opinion letter does not deal with the threat of litigation. Per our discussion with the auditors and as was stated in the policyholders' meetings, which the auditors attended, their concerns were the possible things that could cause the fund to close down such as:

1) The excess insurers could cancel the excess insurance policy prior to expiration.

2) The Board could vote to close the fund down.

3) Policyholders could get fed up with the uncertainty of the situation and leave in mass.

The going concern language has nothing whatsoever to do with litigation. Furthermore, review of note fourteen does not contain anything related to litigation whatsoever.

Finally, we have asked our auditors as to whether or not they would express an unqualified opinion on the December 31, 2003 statements were this amount accrued. The auditors' answers were that no, they could not express an unqualified opinion, as this accrual did not meet the definition of accrual under *Statement of Financial Accounting Standards No. 5.* At the earliest this expense should appear in the 2004 financial statements. TABCOMP Trust's 2004 financial statements correctly reflect the $185,000 as expenses generated and paid for in 2004.

Comment 2 concerning Recommendation for Corporate Records (p32):

1. Corporate Records (p32)

The original Board of Trustees was empowered by the "Declaration of Trust and Bylaws." Thereafter, Tenn. Comp. R & Regs. provide that Board Members are to be elected by the Members of the Trust. The following are

exceptions to Tenn. Comp. R & Regs. which were noted through the examiners review of minutes to Board of Trustees and Members meetings.

1. At a meeting held on January 25, 2002, the Board of Trustees elected Mike Griffin.
2. At a meeting held on January 25, 2002, Rick Francis was listed as a Board of Trustee member. The examiners could find no evidence in TABCOMP Trust's corporate records of his election to the Board of Trustees.
3. At a meeting held on October 8, 2004, the Board of Trustees accepted Lynn Johnson and Chris Karbowiak as Board of Trustee members.

The manner of election of the above Board of Trustee members is inconsistent with the Bylaws and Tenn. Comp. R & Regs.. Pursuant to Tenn. Comp. R & Regs. 0780-1-54-.07 and TABCOMP Trust's Bylaws, it is recommended that TABCOMP Trust's Board of Trustee members be elected by TABCOMP Trust membership.

**The approved minutes for the November 6, 2001 meeting (Appendix A) list Rick Francis as a board member. Furthermore, the annual membership meeting on May 10, 2002 (Appendix B) shows the membership present voting unanimously for all board members, including Rick Francis and Mike Griffin. However, only seven members were represented at this meeting.**

**The agenda for the August 5, 2005 annual membership meeting includes electing and voting for board members for the upcoming year. To comply with TABCOMP Trust's Bylaws and Tenn. Comp. R & Regs., the following are included on the ballot: Mike Griffin, Rick Francis, Lynn Johnson, Chris Karbowiak, and Joe Internicola.**

**Comment 3 concerning Restricted Fund Balance (p27) and Declaration of Refunds (p32):**

Restricted fund balance (p27) ..... $ 44,725

The above amount was established as a result of this examination. It represents the "surplus" from the 2002 and 2003 fund years which was declared by the Board of Trustees as payable to the Members, but is not yet allowed by Tenn. Comp. R & Regs. to be declared as "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. However, the Board of Trustees must declare the refund not less than twelve months after the end of the fund year and if the refund is declared, 10% of the refundable amount must be retained by the pool to cover any obligations that may not yet have been reported. TABCOMP Trust declared and reported dividends for 2002 and 2003 approximately fourteen months prior to their date of eligibility per Tenn. Comp. R. & Regs. See "Declaration of Refunds" on page 32

of this examination report for a more thorough description and a recommendation for corrective action.

2. Declaration of Refunds (p32)

TABCOMP Trust's Board of Trustees voted on October 25, 2002 to "declare as payable to the Members any and all surplus that exists as of December 31, 2002" but that "the exact amount of this dividend is currently unknown as the year-end accounting is not complete." The Board of Trustee's intent is "that all surplus funds be returned to the members therefore the surplus funds that arose during the year should be recorded as an expense on the income statement with the unpaid portion of these amounts added to the liabilities on the balance sheet...and that the Fund will never retain any surplus." The Board' of Trustee's declaration of these amounts as dividends was made fourteen months prior to their eligibility pursuant to Tenn. Comp. R & Regs. 0780-1-54.16 which specifies dividends may not be declared less than twelve months after the end of the fund year. TABCOMP Trust accounted for the surplus attributed to the 2003 policy year similarly in its financial statements, but there is no evidence recorded in the minutes to the meetings of TABCOMP Trust's Board of Trustees that they ever declared these amounts payable to the Members.

It is the opinion of the examiners that TABCOMP Trust's practice of treating the surplus attributable to its current year of operations as dividends immediately payable to its members is being done prior to the date of eligibility per Tenn. Comp. R & Regs., and that these restricted funds are being misreported as "Distributions Due Members" in TABCOMP Trust's financial statements. It is recommended that, in the future, TABCOMP Trust comply with Tenn. Comp. R & Regs. in declaration of refunds payable to its Members.

**The financial statements of TABCOMP were prepared in accordance with generally accepted accounting principles as required by applicable law. They are not statutory financial statements. Generally accepted accounting principles for property and casualty insurance enterprises are set forth in *Statement of Financial and Accounting Standards No. 60.* amongst other places. *Statement of Financial and Accounting Standards No. 60* requires a policyholder's dividends shall be accrued based upon the estimate of the amount to be paid. The governing documents of the fund and intent of the Board of Trustees are reasonably clear. All surplus funds will ultimately be returned to the policyholders. As such, TABCOMP has made an accrual of the ultimate amounts anticipated to be refunded to the policyholders as of the end of each year. Whether or not the trustees made a declaration of a dividend has no bearing on this accrual. Generally accepted accounting principles requires this accrual under the facts and circumstances that exist with respect to TABCOMP. Further, it is our interpretation of the rules that the dividend declaration they are referring to is the declaration preceding an actual payment. The trustees have not made a payment prematurely. They have always made any dividend payments in accordance with the requirements of applicable laws, rules, and regulations. All the so called declarations that have been made are doing**

**nothing more than restate what is in the Fund's governing documents. This declaration in the minutes has been done largely for federal income tax purposes.**

**This recommendation of the audit is not something the Board can agree with. In the event that the Fund were to adopt this procedure, it would cost the trust fund hundreds of thousands of dollars, if not millions of dollars, ultimately. The only way that the Fund can obtain a tax deduction for the amounts that have been deducted on the tax return as accrued but unpaid policyholder dividends is to have the "declaration" in the minutes. These amounts would have to be accounted for in the financial statements the way they have been treated. In the event that this was not done, it is our auditor's estimate that there would be additional federal income taxes of approximately $260,000. To put this in another context, to make the changes that have been recommended means that there's $260,000 of funds that would not be available to either pay claimants in the State of Tennessee or to return to employers in the State of Tennessee. Either way the State of Tennessee loses. Once this amount is gone to the Internal Revenue Service, in the form of a payment of federal income taxes, it is gone forever. It will not be coming back to Tennessee. The substantial cost to the trust fund is an unnecessary cost and puts the trust fund in a more precarious position financially.**

**Comment 4 concerning TABSSIT Members' surplus held by TABCOMP Trust (p26), Policyholders' surplus before accumulated other comprehensive earnings (p26) and Payment of Refunds (p33):**

TABSSIT Members' surplus held by TABCOMP Trust (p26) ..... $ 890,476

The above account is a newly designated account and the amount per examination is the total of the amount actually belonging to former Members of TABSSIT, the previous trust. The balance includes $852,839 previously reported as "Policyholders' Surplus" and $37,637 reclassified from "Members Distributions Payable" attributable to the Trust's treatment of the 2001 operating loss which was improperly taken from surplus funds belonging to members of TABSSIT. (See "Payment of Refunds" on page 33 of this examination report for a more thorough explanation and a recommendation for corrective action.)

Policyholders' surplus before accumulated other comprehensive earnings (p26)..... $ 0

The above amount is $852,839 less than reported by TABCOMP Trust in its December 31, 2003 financial statement. As noted above, the balance which was reported as equity has been reclassified as a liability owed to the former Members of TABSSIT, the Trust's predecessor.

3. Payment of Refunds (p33)

TABCOMP Trust's predecessor, TABSSIT, ceased operations effective December 31, 1998. Although TABSSIT has not been active since this date, its certificate of approval was never terminated and remains in effect in accordance with Tenn. Comp. R & Regs. 0780-1-54-.05. Management represented to the

examiners that there are no plans for TABSSIT's reactivation, therefore it is recommended that management take the necessary steps to terminate the certificate of authority of TABSSIT in accordance with Tenn. Comp. R. & Regs., and that any remaining surplus funds be returned to its former members in accordance with TABSSIT's Bylaws and the "Indemnity Agreement and Power of Attorney" binding on each former Member. These surplus funds were previously declared as refunds payable to its former Members by TABSSIT's Board of Trustees and presented as such in financial statements submitted to the Department of Commerce and Insurance.

TABSSIT executed a loss portfolio contract with their excess insurance carrier, Safety, when operations ceased December 31, 1998. However, TABSSIT's administrator, TAB Service Corporation, continued to service all transferred claims for Safety under a "TPA Service Agreement." They also made efforts to keep the TABSSIT membership together by putting together a program whereby replacement workers compensation coverage was provided to TABSSIT Members through the voluntary market directly by Safety. TAB Service Corporation continued to administer this program by serving as the manager for Safety and provided production, loss control, premium collection, claims administration and accounting services under an "Operating Agreement."

According to TABSSIT's audited financial statements that were filed with the Department of Commerce and Insurance, it accumulated approximately $3.4 million in surplus as a result of its operations from 1992 through December 31, 1998. Beginning in 1999, the majority of these TABSSIT reserve funds were returned to TABSSIT's former members by TAB Service Corporation in the form of refunds. Authority for refunds is contained in Tenn. Comp. R. & Regs. 0780-1-54-.16 which provides that any monies for a fund year in excess of the amount necessary to fund all obligations for that fund year may be refunded to the members. TAB Service Corporation distributed the TABSSIT refunds as follows:

| Date Paid | Amount |
|---|---|
| 1999 | $ 906,290 |
| 2000 | 1,169,821 |
| 2001 | 605,901 |
| Total | $ 2,682,012 |

Beginning in 1999, TAB Service Corporation and the former Board of Trustees of TABSSIT implemented a refund policy whereby Trust members that did not transition into the Safety program would be ineligible to participate in the premium refunds. This action by the administrator and TAB Service Corporation created a conflict of interest because refund eligibility was contingent on TABSSIT Members purchasing replacement coverage from Safety's program which was being managed by TAB Service Corporation. It is the opinion of the examiners that this action was also in violation of Tenn. Comp. R. & Regs. 0780-1-54-.16 (2) which states payment of a refund based on a previous fund year shall not be contingent on continued membership in the group after that fund

year. As such, many former TABSSIT members that did not purchase coverage from Safety did not receive the dividend distributions to which they were entitled.

TABCOMP Trust is currently holding approximately $900,000 of TABSSIT surplus funds according to audited financial statements filed with the Department of Commerce and Insurance. It is therefore recommended that this be distributed to former TABSSIT members after TABSSIT's dissolution, and that priority should be given to those Members who were not allowed to participate in the first three dividend distributions to the extent that they receive their share of distributions which were previously and improperly withheld.

Tenn. Comp. R. & Regs. 0780-1-54-.16 requires each member to be given a written description of the Trust's refund plan at the time of their application for membership. TABCOMP Trust's Indemnity Agreement and Power of Attorney agreed to and signed by each member provides only a general description of TABCOMP Trust's refund policy by stating "remaining funds of the Trust shall be distributed to Members in such manner as the Trust shall deem equitable which includes limiting distribution to Members with a loss ratio not in excess of a level designated by the Board, and/or providing that any Member may share in prorate distribution of dividends regardless of when such dividends are declared so long as such Member participated during the year for which the distribution is made." The examiners could not find any evidence that TABCOMP Trust has ever provided its members with a clear description of its refund plan and it is recommended that this be done by management in conjunction with each new and renewal policy application. It is also recommended that TABCOMP Trust refrain from implementing refund plans with restrictive terms prior to their effective date.

**We are in agreement that the financial statements of TABCOMP Trust reflect approximately $850,000 of money that came from the balance after the loss portfolio transfer in the previous TABSSIT program. The Board did not undertake this action without considering regulatory concerns or seeking permission from regulators as to this transaction. At the end of 1998, George Davis, Vice President of TAB Service Corporation, sought this permission from Neil Nevins, Assistant Commissioner. In a letter dated December 31, 1998 (Appendix C), Mr. Nevins approved the loss portfolio transfer to Safety National Casualty Corporation. He further stated that all future activities of TABSSIT should be carried out in accordance with its bylaws. We further sought clarification of this and further permission for this treatment from Mark Brothers, Director of Self Insurance, in our board meeting June 7, 2001 (Appendix D). Having had several informal discussions with the regulator and receiving permission from the regulator for this treatment in writing, we believe that we have a reasonable basis for accounting for these items in this fashion. Considering the sensitivity of the Department to this issue, the Board realizes it must take some action on this. The action in consideration will be that no amount of this surplus will be refunded to any member who was not a policyholder of TABSSIT. We believe these amounts have previously been accounted for properly and were treated as such with the complete understanding and approval of the regulatory authorities.**

**As of today, 63% of TABCOMP Trust's 2005 active policyholders were members in the original TABSSIT program. These forty-two members represent $2,884,500.00 in premium or 63% of the total 2005 fund year premium.**

**The agenda for the board meeting on August 5, 2005 will include a discussion concerning a clear description of TABCOMP Trust's dividend/refund plan. Once this plan has been finalized, we will distribute a copy to our members.**

**Comment 5 concerning Underwriting and Rating (p35):**

4. Underwriting and Rating (p35)

TABCOMP Trust had 8, 79 and 88 Members participate in the Fund during the 2001, 2002 and 2003 policy years which were covered by this examination. The examiners' review of a sample of the Members' rating calculations made by TABCOMP Trust during this period revealed the following exceptions:

1. Tenn. Code Ann. § 50-9-104 specifies the eligibility requirements for a 5% drug free workplace premium credit. The examiners conducted an extensive review of TABCOMP Trust's premium and rating procedures and noted only one exception to this policy. In 2002, TABCOMP Trust allowed an ineligible Member, Quad Industries, to receive the full drug free workplace credit. It is recommended that, due to the unauthorized discount, an adjustment be made to this Member's premium billing.

**The extension of the drug free work place credit to Quad Industries for the 2002 year was a simple, clerical oversight and an isolated incident. This resulted in a discount given of $1,017.00. Since the error benefited the member, we respectfully request that the additional premium for the 2002 fund year for Quad Industries be waived. We now have measures in place to verify that drug free work place credits are only given according to the period of eligibility.**

2. As noted earlier in this report, TABCOMP Trust applies schedule-rating factors to Members' premium in such a manner as to adjust the estimated premium to make the expected loss ratio fit within an established target range. This method was applied fairly and consistently to all members during the period of examination; however TABCOMP Trust's adjustments are dependent solely on members' past experience. The procedure does not appear to comply with NCCI schedule rating guidelines, has not been approved by the Department of Commerce and Insurance and does not appear to have been formally approved by TABCOMP Trust's Board of Trustees. Per Tenn. Comp. R. & Regs. 0780-1-54-.15, it is recommended that TABCOMP Trust adhere to established NCCI procedures in application of its schedule rating adjustments to premium. (p36)

**Effective January 1, 2005, TABCOMP Trust began adherence to established NCCI procedures in application of scheduled rating adjustments to all membership premium funding.**

3. Recalculations of five members audited premium amounts resulted in differences in the amount of Stock Discount (Premium Volume Discount) applied. All five members received discounts slightly above the amount they were entitled to per NCCI procedures, and all policies were for terms of less than a full year. The estimated premiums were annualized for application of all credits and debits, including stock discounts, and then prorated to the actual term of the policy. The calculation of the stock discount was consistent for all members that had partial year policies. These differences occurred in the 2001 and 2002 policy years and the total amount of difference amounted to $2,078 and $2,753 respectively. It is recommended that, in the future, TABCOMP Trust adhere to NCCI procedures by applying premium volume discounts to actual premium amounts instead of annualized amounts. (p36)

**Effective 2004, TABCOMP Trust began adherence to NCCI procedures on application of premium volume discounts to actual premium amounts instead of annualized amounts upon the examiners' notification of the oversight.**

4. As noted earlier in this report, TABCOMP Trust makes a "loss sensitive" program available to some of its Members. Decisions to place or keep members in the program are not based on any established procedures and some are more a factor of market/competitive forces. Amounts returned are considered "underwriting discounts" and paid from funds labeled "Members Distributions Payable," which is comprised of surplus funds declared by the board as payable to Members. It is the opinion of the examiners that this loss sensitive program is essentially a form of "retrospective rating" as defined in the NCCI rating manuals. The NCCI procedures for retrospective rating are very detailed and the simplistic manner in which TABCOMP Trust administers its loss sensitive program is not consistent with these procedures. In addition, the practice of applying "stock discounts" to members in the loss sensitive program is inconsistent with NCCI procedures which specify that premium subject to retrospective rating is not eligible for discounts.

   It is the opinion of the examiners that it is inappropriate for TABCOMP Trust to use retrospective rating. Self insured trusts operate with the purpose of eventually returning all profits to its members; however retrospective rating gives specific members priority in receipt of refunds. The use of retrospective rating also creates the possibility that TABCOMP Trust could be obligated to return premium to participating members in a policy year in which TABCOMP Trust was not profitable, which would require an assessment of the non-participating membership. Furthermore, TABCOMP Trust's application of its loss sensitive program was not considered by their independent actuaries in the determination of their

loss cost multiplier. It is recommended that TABCOMP Trust's administrator obtain approval from the Department of Commerce and Insurance and its Board of Trustees for any future application of its loss sensitive program. It is also recommended that the loss sensitive refunds previously returned by TABCOMP Trust which were accounted for as Members' Distributions should instead be accounted for as a reduction to premium with corresponding offsets to expenses which are a function of written premium. (p36)

**The member distribution payable numbers that were accrued on the financial statements are inclusive of amounts due to the loss sensitive members. This appears to simply be a reclassification of an amount that has already been recorded. It does not change the financial position of TABCOMP. We elected to reflect this in the member distribution payable and not break it out separately.**

**Further, if we were to break this out separately, there is some chance that this would be considered to be unearned premium reserves for purposes of federal income tax filing. We would only be entitled to deduct 80% of these amounts rather than the full amounts. This would cost the Trust Fund a significant amount of money.**

**The 2004 audited financials of TABCOMP Trust reflect the potential loss sensitive payouts for the 2004 fund year. Furthermore, effective January 1, 2005 TABCOMP Trust permanently discontinued use of loss sensitive plans.**

**Comment 6 concerning Policy Issuance (p37):**

5. Policy Issuance (p37)

The following problems were noted as a result of a review of TABCOMP Trust's 2005 policy year issues and renewals:

1. TABCOMP Trust renewed coverage for Texas Boot in January 2005, but the required down payment of premium was never made. Based on the language of TABCOMP Trust's policies and Tenn. Comp. R. & Regs., coverage was not able to be canceled until 30 days after their cancellation notice was mailed on March 15, although no premium was ever paid by the Member.

**On February 15, 2005, TABCOMP Trust issued a ten day cancellation notice to Texas Boot (Appendix E) for non-payment of premium forty-five days after the due date of the installment, January 1, 2005, according to TABCOMP Trust's Indemnity Agreement. This same Indemnity Agreement received approval from the Department as part of TABCOMP Trust's application to operate as an approved group self insurer effective July 1, 2001. Once payment was not received within the ten day period, a thirty day cancellation notice was mailed March 1, 2005. Furthermore, the credit produced from Texas Boot's 2004 audit was applied to the balance of the 2005 fund year resulting in no outstanding balance.**

**TABCOMP Trust understands the importance of collecting all premium installments, especially the initial fund year deposit. The Board is meeting August**

**5, 2005 and will discuss revising the Indemnity Agreement to prevent TABCOMP Trust's obligation to provide coverage to members who do not make their initial fund year deposit.**

2. TABCOMP Trust's Board of Trustees allowed coverage to be bound for Elite Trailer prior to the receipt of the required complete Member's application package (which includes member financial statements). Without these documents, it was impossible for TABCOMP Trust to apply required underwriting procedures to this account prior to policy issuance. This action was in violation of the Trust's Bylaws, NCCI Procedures and Tenn. Comp. R. & Regs. 0780-1-54-.08(1) which provide an employer joining a workers' compensation self-insurance group shall: (a) submit an application for membership to the board of trustees or its administrator and (b) enter into the indemnity agreement required by the Rules. Membership takes effect no earlier than each member's date of approval. The application for membership and its approval shall be maintained as permanent records of the Board of Trustees.

It is recommended that TABCOMP Trust's Board implement procedures that prevent its obligation to provide coverage to non premium paying Members, and refrain from issuing policies to Members prior to their required application, review and approval processes are complete. (p37)

**Coverage for Elite Trailer was bound prior to receipt of its' financial statements as a result of a miscommunication. TABCOMP Trust's Board was provided a guideline regarding binding procedures on April 22, 2005 (Appendix F) to ensure the avoidance of this type of problem in the future.**

**Comment 7 concerning Termination of Service Company Contract (p37-38):**

6. Termination of Service Company Contract (p37-38)

The service company agreement between TABCOMP Trust and TAB Service Corporation specifies that claims covered by TABCOMP Trust during the term of the agreement will be handled for twenty-four months after cancellation or expiration of the agreement. If the agreement expires or is terminated, all applicable books, records and files of TABCOMP Trust shall promptly be, at the choice of TABCOMP Trust, transferred to TABCOMP Trust or a designated third party, or will be retained for continued service by TAB Service Corporation for a period of time not to exceed twenty four months. The service agreement was cancelled effective May 27, 2004, but TABCOMP Trust released TAB Service Corporation from this provision in their contract. The employees of TAB Service Corporation became employees of TABCOMP Trust and all services previously

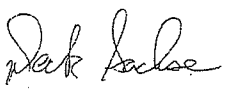
provided by TAB Service Corporation were performed directly by TABCOMP Trust employees.

The provision for incurred losses in TABCOMP Trust's financial statements includes an estimate for losses and allocated loss adjustment expenses ("ALAE") only. ALAE are those expenses, such as litigation costs, which can be directly attributed to a specific claim. Unallocated loss adjustment expenses ("ULAE") that cannot be directly associated with a particular claim such as administrative expenses, consulting fees and claims handling fees are not included in the estimates. Since TABCOMP Trust released TAB Service Corporation from its contractual obligation to perform these services upon the termination of its service contract, it is recommended that TABCOMP Trust establish a provision for ULAE in its reserve liability equal to the expected cost of settling all open claims.

**Following the termination of the TAB Service Corporation contract, TABCOMP Trust established a provision for unallocated loss adjustment expenses. As of December 31, 2004, this expense of $62,169.00, as calculated by TABCOMP Trust's actuary, Casualty Actuarial Consultants, Inc. (Appendix G), is reported as a reserve liability on the financial statements.**

TABCOMP Trust is committed to complying with the rules and regulations of the Department of Commerce & Insurance while providing sound coverage to our members. Immediate steps were taken to correct certain disparities found within TABCOMP Trust's operations. Policies and procedures are in review to further protect our members' interests. In as much, we respectfully request a hearing to bring additional clarification of TABCOMP Trust's position in these matters. As we look forward to resolving these issues, please contact me at 901/248-1742 with available dates.

Sincerely,



Deck Sachse
Chairman

Acknowledged by: William Shores, CPA

# TABCOMP
## Board of Trustees
## Tuesday, November 6, 2001

The Board of Trustees of the TABCOMP Trust met in Nashville at the Marriott Courtyard on Tuesday, November 6, 2001. Board members and others in attendance were:

Doug Gentry, Genco Stamping
Will Hord, Steelcraft, Inc.
Deck Sachse, Conwood Co.
Jim Dyer, Metal Products
Bill Ring, Kingsport Foundry
Ian Smith, WYKO
Rick Francis, TN Apparel

Carter Witt, Trust Administrator

Attending TAB Service Corporation Staff: George Davis, Vice-President, Mikhel Lindsley, Controller, Robert McDougal, Underwriter, and Tom Walker, Director of Marketing.

Will Hord called the meeting to order at 8:15.

George Davis opened by giving a history the TABSSIT and Safety National programs. An overview of beginning the new Trust, TABCOMP. On overhead he showed the organizational chart of TABCOMP. Here he listed the Board of Directors for TAB Comp. (See attachment).

Mr. Davis explained Lisa Dennison will be the actuary, Ms. Dennison was formally with Costner Group who was the actuary for TABSSIT.

Shores & Company will be the firm that will handle the TABCOMP Audit.

The excess carrier will be Safety National. Safety National is an A rated company and has been in association with TAB since 1992.

Mr. Davis gave a brief history of TABSSIT and the loss cost system from 1992. The combined ratio graph showed how insurance companies, nationally, were charging less premium than expenses.

Mr. Davis stated the State requires a $500,000 bond for all Trust.

Mr. Witt proposed a commission tiered program for agencies.

Any premium under $499,999 the commission is 7%
From $500,000 to $999,999 the commission is 8%
For premiums of $1,000,000 and greater the commission increases to 9%.

Reasons for this proposal: By raising the commission TABCOMP may be able to hold business.

Some agencies move blocks of business in order to take advantage of such programs.

Mr. Francis asked if members had to have agents?
Mr. Witt: No
A unanimous vote taken to install the tiered commission program.

Mr. Dyer asked what is our average premium?
Mr. McDougal: $60K

Mr. McDougal presented the underwriting report:

- ✓ 52 members are in the Safety National Program, - We are in the progress of rolling those companies into TABCOMP.
- ✓ He estimates the premium from the rollover companies at $3.4 million
- ✓ TABCOMP is rating the business at a 60% loss ratio.
- ✓ He is currently working eleven submissions that represent $1.9million in premium.
- ✓ A list of requirements for a company to be apart of TABCOMP was presented.

Mr. Francis expressed concern that the minimum annual premium is $5,000. Mr. McDougal explained that guideline was from the Safety National program and TABCOMP simply adopted it.

Mr. McDougal explained Safety National analyzes each submission for losses and projected losses. Ms. Lindsley reviews the financial statements for stability.

Mr. Walker presented the marketing campaign that started in August to promote and inform the TAB membership and former participants of the workers' compensation program. The staff agreed to set a goal of an increase of $2.5 million in premium. A series of letters have been mailed to companies that renew their coverage on January 1. Letters have been mailed to agents letting them know TAB has an "A" rated claims department and competitive rates. On October 31st a letter was mailed to 900 members of the TAB Membership. Starting the week of October 26th the TAB Service staff started calling these members and personally talking about the TABCOMP program and letting them know how to get a quote.

As of Monday, Nov. 5th 130 calls had been made and 30 companies expressed interest in receiving a quote.

Next meeting: January 25th

Adjourn 9:25 am.

# TABCOMP
# Annual Membership Meeting
# Friday, May 10, 2002

The first Annual Membership Meeting of TABCOMP Trust met in Nashville at the Hilton Suites on Friday, May 10, 2002. Board members and others in attendance were:

Will Hord, Steelcraft, Inc.
Deck Sachse, Conwood Co.
Jim Dyer, Metal Products
Doug Gentry, Genco Stamping
Mike Griffin, IPC&L
Rick Francis, TN Apparel
Eli Bennett, Bennett Tool & Die
Bill Ring, Kingsport Foundry

Carter Witt, Trust Administrator

Attending TAB Service Corporation Staff: George Davis, Vice-President, Mikhel Lindsley, Controller, Robert McDougal, Underwriter, and Tom Walker, Director of Marketing, Michelle Radford, Claims Manager.

Members attending: Tracy Austin and John Weakly both from Genco

Will Hord called the meeting to order at 9:40

Mr. Hord welcomed everyone and gave a brief history explaining that a decade ago TABSSIT was started and has since changed into TABCOMP.
Mr. Davis gave a presentation on the workers' compensation market. With a graph he explained the rates that have been filed with the state. See Attached report.

Mr. Davis covers areas of concern in the workers compensation arena. See attached

Mr. Hord on behalf of the membership and board thanked Mr. Davis and Mr. Witt and the Service Corp. staff for a job well done.

Mr. Witt gave an overview of the financial status of TABCOMP. He stated that the claims were currently coming in less than 65%. Mr. Witt explained AmSouth is handling the investment account.

Rick Francis presented the nominations for the Board and their terms.
The nominations are as follow:

| | | | |
|---|---|---|---|
| Will Hord, | Chairman | West | 1 year |
| Jim Dyer | Vice Chair | Middle | 3 years |
| Deck Sachse, | Secretary | West | 2 years |

| | | |
|---|---|---|
| Eli Bennett | Middle | 1 year |
| Doug Gentry | Middle | 1 year |
| Ian Smith, | East | 2 years |
| Bill Ring | East | 2 years |
| Rick Francis | Middle | 3 years |
| Mike Griffin | East | 3 years |

A unanimous vote was taken to approve the trustees and their terms.

Then meeting was adjourned at 10:15

STATE OF TENNESSEE
DEPARTMENT OF COMMERCE AND INSURANCE
Insurance Division
500 James Robertson Parkway
Nashville, TN 37243
615-741-2176

December 30, 1998

George Davis
TAB Service Corporation
611 Commerce Street, Suite 3023
Nashville, TN 37203-3742

RE: Tennessee Association of Business Select Self-Insured Trust
Proposed Loss Portfolio Transfer

Dear Mr. Davis:

This Department has carefully reviewed the proposed Loss Portfolio Transfer of The Tennessee Association of Business Select Self-Insured Trust to Safety National Casualty Corporation.

Approval of this transaction is hereby granted based on the representations made that all known, re-opened and IBNR claims occurring between January 1, 1992 through December 31, 1998 will be transferred to Safety National Casualty Corporation. In addition, all future activities should be carried out in accordance with the bylaws of the Trust.

I trust you will find this information of assistance; however, should you require additional information, please contact me at 615-741-2176.

Sincerely,

C. Neil Nevins
Assistant Commissioner

CNN/lg

TAB Comp

June 7, 2001

The Board of Trustees of the TABCOMP Trust met in Nashville at the Holiday Inn Vanderbilt on Thursday, June 7, 2001. Board members and others in attendance were:

Doug Gentry, Genco Stamping
Will Hord, Steelcraft, Inc.
Deck Sachse, Conwood Co.
Jim Dyer, Metal Products.
Eli Bennett, Bennett Tool & Die

Carter Witt, Trust Administrator

Attending TAB Service Corporation Staff: George Davis, Vice-President, Mikhel Lindsley, Controller, Robert McDougal, Underwriter, and Tom Walker, Claims Administrative Supervisor.

Will Hord called the meeting to order at 8:00.

George Davis opened by giving an overview of beginning a new Trust, TABCOMP. On overhead he showed the organizational chart of TABCOMP. Here he listed the Board of Directors for TAB Comp. (See attachment).

Mr. Davis explained Lisa Dennison will be the actuary, Ms. Dennison was formally with Costner Group who was the actuary for TABSSIT.

No decision has been made regarding the firm that will handle the TABCOMP Audit.

The excess carrier will be Safety National. Safety National is an A rated company and has been in association with TAB since 1992.

Mr. Davis gave a brief history of TABSSIT and the loss cost system from 1992. The combined ratio graph showed how insurance companies, nationally, are charging less premium than expenses.

Mr. Sachse asked why the 1998-year showed a loss ratio greater than 100%. Mr. Davis explained that one claim with Crescent Hosiery Mills cost over 1.1 million dollars and that show on the calculation. In actuality TABCOMP paid out $250,000 and the rest was covered under the excess insurance policy. Factoring in a loss of $250,000 dropped the loss ratio down to around 70%.

Jim Dyer asked if we could reactivate TABSSIT. Mr. Davis explained the State requested we start a new one.

Mr. Davis gave a review of TABCOMP since 1999 when TABSSIT was converted to a fully insured program through Safety National. In 1999 Safety National made a profit of $169k and in 2000 they had a loss of $637k. In 2001 Safety National tried to kick out (not renew their coverage) three members one of which ended up staying. As of 1-1-02 Safety National is getting out of first dollar coverage.

The graph showing TABCOMP has the money to cover the potential gap – at this level of premium we have no chance of an assessment.

Mr. Hord asked if the gap increased as the premium increased. Mr. Davis answered Yes.

Mr. Sachse inquired if TABCOMP has authority to move the money from TABSSIT to TAB COMP and cover the gap. Mr. Davis and Mr. Brothers both agreed this was acceptable. The law states the money can be moved as long as the money is used to further the interest of the members.

Mr. Gentry asked if we have to invest in Tennessee funds. Mr. Witt answered Yes; they must be government secured fund.

Mr. McDougal presented the underwriting guidelines and requirements for being a member of TABCOMP. See attachment

Mr. Bennett wanted the asset/premium ratio raised from 2/1 to 4/1. This was agreed on and a vote take to make the change. If a company falls below this 4/1 ratio the board can vote and allow that member to stay in program.

Mr. Witt proposed Will Hord as Chairman,
Jim Dyer as Vice Chairman
Deck Sachse as Secretary

A unanimous vote was take to approve the officers.

Issues to discuss at next meeting:
Term Limits if needed on officers.

Next meeting in October.

Adjourn 9:10 am.

# TABCOMP TRUST

February 15, 2005

Mr. Don Taylor
Texas Boot Company
P.O. Box 17307
Nashville, TN 37217

VIA CERTIFIED MAIL

RE: Notice of Cancellation for
Non-Payment of Premium Due 1/1/05

Dear Mr. Taylor:

This letter will serve as appropriate, written notification that Texas Boot Company's workers compensation coverage through the TABCOMP Trust is in jeopardy of being cancelled, if overdue premiums in the amount of $47,512.28 are not received in TABCOMP's office by the close of business on February 25, 2005. Should payment in full of the amount indicated above not be received by the due date, a 30 day cancellation notice will be issued, and Texas Boot's coverage will be cancelled effective March 28, 2005. Reinstatement of coverage will not be made without good cause.

We regret that we must take this course of action, however these measures are necessary to protect the interests of the TABCOMP membership and are prescribed in the indemnity agreement you signed upon Texas Boot's joining the TABCOMP Trust. We appreciate your prompt payment to avoid this cancellation.

Sincerely,

Mikhel Lindsley
CFO

CC: Frank Caruso, Arthur J. Gallager & Co.
Tennessee Department of Commerce and Insurance

Appendix E

750 Old Hickory Blvd. • Building 2, Suite 100 • Brentwood, TN 37027 • Phone 615-370-5964 • Fax: 615-377-0946

## TABCOMP/CCMSI
## Claims Quoting Procedure

- Review submission to determine class eligibility and minimum premium requirements—decline if eligibility or premium level unacceptable.
- Request all information needed to consider for quoting.
- Once all requested information is received, reviewed and approved, forward submission to Safety National for approval to add to the excess policy.
- Once Safety National approves, contact TCCI to determine membership status. If prospect is not already a member, request an invoice for dues.
- Once TCCI invoice is received, issue quote on condition of receipt and approval of financials, receipt of down payment check, receipt of TCCI dues payment and receipt of signed indemnity agreement/group application prior to binding coverage.
- Issue a binder of coverage only upon receipt and approval of financials, receipt of down payment check, receipt of TCCI dues payment, and receipt of signed indemnity agreement/group application.


TABCOMPTRUST
Workers' Compensation Self Insured Fund
Sponsored by Tennessee Chamber of Commerce and Industry

Appendix B, Exhibit IV

*TENNESSEE ASSOCIATION OF BUSINESS COMPANY OWNERS' MANAGED PROGRAM*

WORKERS COMPENSATION

ESTIMATED ULAE RESERVES AS OF 12/31/04
(Includes Claims Closed Without Cost)

E. ESTIMATED ULAE FOR MED-ONLY CLAIMS

| Policy Period | Estimated ULAE for Med-Only Claims Open During:** 2005 | 2006 | 2007 | 2008 | 2009 | Total |
|---|---|---|---|---|---|---|
| 7/1-12/31/01 | $ 0 | | | | | $ 0 |
| 1/1/02-03 | 0 | | | | | 0 |
| 1/1/03-04 | 0 | | | | | 0 |
| 1/1/04-05 | 100 | | | | | 100 |
| Total | $100 | $0 | $0 | $0 | $0 | $100 |

F. TOTAL ESTIMATED ULAE

| Policy Period | Estimated ULAE for Claims Open During: 2005 | 2006 | 2007 | 2008 | 2009 | Total |
|---|---|---|---|---|---|---|
| 7/1-12/31/01 | $ 0 | | | | | $ 0 |
| 1/1/02-03 | 2,700 | $ 1,200 | | | | 3,900 |
| 1/1/03-04 | 8,700 | 4,200 | $2,100 | | | 15,000 |
| 1/1/04-05 | 30,700 | 7,800 | 3,900 | $2,100 | | 44,500 |
| Total | $42,100 | $13,200 | $6,000 | $2,100 | $0 | $63,400 |

G. TOTAL ESTIMATED ULAE-DISCOUNTED AT 2%

| Policy Period | Discounted Estimated ULAE for Claims Open During: 2005 | 2006 | 2007 | 2008 | 2009 | Total |
|---|---|---|---|---|---|---|
| 7/1-12/31/01 | $ 0 | | | | | $ 0 |
| 1/1/02-03 | 2,673 | $ 1,165 | | | | 3,838 |
| 1/1/03-04 | 8,614 | 4,077 | $1,999 | | | 14,690 |
| 1/1/04-05 | 30,398 | 7,572 | 3,712 | $1,959 | | 43,641 |
| Total | $41,685 | $12,814 | $5,711 | $1,959 | $0 | $62,169 |

** Based on estimated ULAE of $100 per open med-only claim