



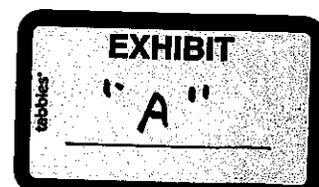
**STATE OF TENNESSEE**  
**DEPARTMENT OF COMMERCE AND INSURANCE**

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**REPORT ON EXAMINATION**  
**OF THE**  
**WORKERS' COMPENSATION SELF-INSURANCE GROUP FUND**  
**OF THE**  
**TENNESSEE AUTOMOTIVE ASSOCIATION SELF-INSURERS**  
**TRUST**  
**NASHVILLE, TENNESSEE**

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**AS OF**  
**DECEMBER 31, 2012**



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Nashville, Tennessee  
March 7, 2014

Honorable Julie Mix McPeak  
Commissioner  
State of Tennessee  
Department of Commerce and Insurance  
Nashville, Tennessee 37243

Dear Commissioner:

Pursuant to your instructions and in accordance with Tennessee Insurance Laws, regulations, and resolutions adopted by the National Association of Insurance Commissioners (NAIC), a financial examination and market conduct review was made of the condition and affairs of the

**WORKERS' COMPENSATION SELF-INSURANCE GROUP FUND  
of the  
TENNESSEE AUTOMOTIVE ASSOCIATION SELF-INSURERS TRUST**  
2521 White Avenue  
Nashville, Tennessee 37204

hereinafter and generally referred to as the "Fund" and "Trust" respectively, and a report thereon is submitted as follows:

**INTRODUCTION**

This examination was called by the Commissioner of Commerce and Insurance of the State of Tennessee on May 7, 2013, in accordance with Tenn. Code Ann. § 50-6-405 and Tenn. Comp. R. & Regs. ch. 0780-1-54-.20. On-site examination work commenced on September 12, 2013. The examination was performed by duly authorized representatives of the Department of Commerce and Insurance, State of Tennessee (TDCI).

With the Trust having authority to write business only in the State of Tennessee, the examination was not classified as an Association Examination under NAIC Guidelines.

## **SCOPE OF EXAMINATION**

This examination report covers the period from January 1, 2008, to the close of business on December 31, 2012, and includes any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

The examination of the Trust's financial condition was conducted in accordance with guidelines and procedures contained in the NAIC Financial Condition Examiners Handbook. In light of the NAIC Handbook requirements and applicable statutes and regulations, the examination was planned and procedures performed to evaluate the financial condition and to identify prospective risks of the Trust. This was accomplished by gathering information about the Trust, including controlling governance, identifying and assessing inherent risks within the Trust, and evaluating internal controls used to mitigate those risks. The examination also included assessing accounting principles used and significant estimates made by management as well as evaluating the overall financial statement presentation.

During the course of examination, assets were verified and valued, and liabilities were determined and estimated as of December 31, 2012. The financial condition of the Trust and its amount of solvency were thereby established. Test checks were made of income and disbursement items for selected periods, and a general review was made of the Trust's compliance with applicable statutes and regulations. All asset and liability items contained in the financial statement of this report were examined and verified with relative emphasis according to their amount and potential impact on solvency. The Trust's 2012 Audited Financial Statements was reconciled to corresponding general ledger account balances. The examination included a review of the year-end 2012 workpapers prepared by the Trust's auditor, Lattimore, Black, Morgan & Cain, PC (LBMC).

## **COMPLIANCE WITH PREVIOUS EXAMINATION FINDINGS**

The previous examination of the Trust was made as of December 31, 2007, by an examiner employed by the TDCI. The prior Report of Examination was dated October 16, 2009, and covered the period from January 1, 2003, through December 31, 2007. The Commissioner issued one (1) directive as set forth in the June 24, 2008, "Order Adopting Examination Report With Directive No. 09-094." A summary of the directive and the corrective action taken by the Trust is discussed below:

### Directive

The Trust was directed to comply with Tenn. Comp. R. & Regs. 0780-1-54.05 by ensuring that any amendments to the organizational documents or written contracts required to be provided to the Commissioner by Rule 0780-1-54-.04 are filed with the Commissioner no later than 30 days prior to the proposed effective date of the amendments, along with a non-refundable filing fee of \$90.00.

### Corrective Action

During the period of examination, the Trust entered into one (1) agreement that was required to be filed with the Commissioner no later than thirty (30) days prior to the proposed effective date. This agreement, a new third party administrator service agreement with Brentwood Services Administrators, Inc., was effective October 1, 2010, and was filed with the Commissioner on October 12, 2010. The Trust's submission of the agreement to the Commissioner did not meet the requirement of Tenn. Comp. R. & Regs. 0780-1-54.05. This issue is noted in the "Recommendations, Comments and Subsequent Events Sections" of this examination report.

## **COMPANY HISTORY**

The Tennessee Automotive Association (TAA) is a Tennessee nonprofit trade association of automobile and truck dealers which was incorporated in 1945. The TAA has been a viable, continuing entity since its inception. The Trust is an unincorporated association that was created by the TAA to act as a self-insurance group. The operation of the Trust is confined to Tennessee where it is licensed to transact the business of workers' compensation and employers' liability group self-insurance. Membership in the Trust is composed of qualifying members of the TAA that have pooled their liabilities under the Tennessee Workers' Compensation Law.

In accordance with Tenn. Comp. R. & Regs. 0780-1-54-.04, the Fund was created on December 17, 1990, with contributions from the initial members equal to 25% of their first year estimated annual net premium for workers' compensation coverage. The Trust continues to maintain the members' deposits, and new members in the Trust are also required to make a contribution equal to 25% of their first year estimated annual net premium.

The following exhibit depicts certain aspects of the growth and financial history of the Trust since the previous examination, according to audited financial statements filed with the TDCI:

<u>Calendar Year</u>	<u>Earned Premiums</u>	<u>Total Reserves for Losses &amp; LAE*</u>	<u>Admitted Assets</u>	<u>Liabilities</u>	<u>Equity or Surplus Funds</u>	<u>Distributions Due to Members**</u>
2008	\$8,452,136	\$6,581,360	\$17,427,677	\$17,427,677	\$0	\$8,404,990
2009	6,621,291	6,435,254	15,857,305	15,857,305	0	7,120,234
2010	6,731,253	6,887,676	16,523,422	16,523,422	0	7,265,966
2011	6,740,583	9,876,216	15,993,138	15,993,138	0	3,735,275
2012	7,565,403	9,766,865	16,733,519	16,733,519	0	4,343,895

\* This represents the total reserves for losses and loss adjustment expenses for all calendar years with open claims since inception.

\*\* The liability for "Distributions Due to Members" as disclosed in the Audited Financial Statements was viewed by the Trust as Surplus Funds.

### **TRUST AGREEMENT AND DECLARATION OF TRUST AND BYLAWS**

The Trust was created through the adoption of the Declaration of Trust and Bylaws (herein after referred to as the Bylaws) which was executed on December 17, 1990, and formally approved by the TDCI effective January 1, 1991. The Trust was formed to act as a workers compensation self-insurance group as defined by Tenn. Comp. R. & Regs. 0780-1-54-.02(17) and as authorized by Tenn. Code Ann. § 50-6-405. The Trust Agreement and Bylaws state the purpose of the Trust as follows:

"of holding and administering the Fund through which its members can meet and fulfill their obligations and liabilities 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 of its members; to provide the maximum allowable advance discounts or dividends on premium payments made by Members for workers' compensation coverage; and to minimize the cost of providing workers' compensation coverage by

developing and refining specialized claim services and a loss prevention program within TAA.”

The Trust was formed in accordance with Tenn. Code Ann. § 50-6-405(c) for the benefit of its member owners. Membership in the Trust consists of individuals, corporations and partnerships or other legal entities which are members in good standing of the TAA and which contribute to the Fund as a participating member in the Trust. The term member includes those individuals, corporations, and partnerships executing, or otherwise being bound by, the Indemnity Agreement and Power of Attorney.

### **INDEMNITY AGREEMENT AND POWER OF ATTORNEY**

In accordance with Tenn. Comp. R. & Regs. 0780-1-54-.04(2)(e)2., each member is required to execute and be bound by an indemnity agreement and power of attorney as a condition of membership in the Trust. Significant terms that each member agrees to include the following:

To assume, pay and discharge any liability of the self-insurance programs of the Group of any and all members, and each member agrees to pay contributions and such assessments as may be required. Without limiting any other rights of the Group, the TDCI shall have the right to enforce, on behalf of the Group, the joint and several liability of the members under this agreement and liability in the event of the Group's failure to enforce such obligations of the members. Provided, the Group's Board of Trustees shall use best efforts, in the event assessments require the performance of the members' joint and several obligations hereunder, to impose such assessments in an equitable manner against all members.

The members intend for this agreement to serve as a mutual covenant of assumption of joint and several liability, provided, however, the relationship of the members with each other and the Group shall not be deemed to form or operate as a partnership for any other purpose except that for which the Group is organized and operated.

The Board may admit as members of the Group only acceptable and financially sound entities. Except as otherwise provided by the Regulations, the Board shall, subject to the approval by the State Department of Commerce and Insurance, be the sole judge of whether an applying entity shall be admitted to membership and the eligibility of an entity to remain a member.

The Board will promulgate the rules and regulations for administering the Group, the expulsion of or suspension of members, and subject to the Regulations, the admission of members. Each member of the Group agrees to abide by such rules and regulations.

**REFUNDS OR DISTRIBUTIONS**

Pursuant to Tenn. Comp. R. & Regs. 0780-1-54.15, 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 with the written approval of the Commissioner. The Board of Trustees must declare the refund not less than eighteen (18) months after the end of the fund year, and if the refund is declared, ten percent (10%) of the refundable amount must be retained by the pool for an additional year to cover any obligations that may not yet have been reported.

The approval history of distributions, categorized by calendar year, since the previous examination report is as follows:

<u>Amount</u>	<u>Date of Approval by Board of Trustees</u>	<u>Date of Approval by TDCI</u>
\$1,358,032.53	May 18, 2008	May 23, 2008
1,359,999.18	May 15, 2009	August 7, 2009
499,999.95	May 7, 2010	June 4, 2010
652,245.08	May 6, 2011	May 31, 2011
200,000.00	May 18, 2012	May 31, 2012

As of December 31, 2012, the Trust had approved the distribution of a total of \$24,973,433 to its members since its inception.

**MANAGEMENT AND CONTROL**

The operation and administration of the Trust is the joint responsibility of a Board of Trustees consisting of not more than fifteen (15) or less than five (5) individuals. Pursuant to Tenn. Comp. R. & Regs. 0780-1-54-.06, all Trustees are required to be residents of the State of Tennessee or officers of corporations authorized to do business in the State of Tennessee. At least two-thirds of the Trustees are required to be employees, officers, or directors of members of the Trust. No affiliate of the administrator or the service agent shall serve as a Trustee. The Board of Trustees shall elect officers from among its members to serve for terms of one year. The officers of the Trust shall consist of a Chairman, a Vice-Chairman, and a Secretary.

As of December 31, 2012, the following persons were serving as members of the Board of Trustees:

<u>Name</u>	<u>Business/Occupation and Address</u>
Herb Adcox Chairman, Board of Trustees	Herb Adcox Chevrolet 5721 Lee Highway Chattanooga, TN 37421
Rick Hill Secretary	Rick Hill Imports P.O. Box 1787 Kingsport, TN 37662
Russell Gwatney Vice-Chairman	Gwatney Mazda of Germantown 7300 Winchester Memphis, TN 38125
Stan McNabb	Stan McNabb Chev-Cadillac-Buick- GMC P.O. Box 730 Manchester, TN 37388
John Murrey	Murrey Chevrolet, Inc. P.O. Box 574 Pulaski, TN 38478
Brent Smith (ex-officio member)	Ray Smith Chevrolet-Buick P.O. Box 487 Camden, TN 38320

The initial Board of Trustees was empowered by the Declaration of Trust and Bylaws and served until the first meeting of the members of the Trust. Thereafter, the Trustees shall be elected by the members of the Trust. Each Trustee shall serve for a term of five (5) years. A Trustee may resign and be fully discharged from all further duties or responsibilities by giving at least 30 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. If 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 to be subject to confirmation by the members at their next regularly scheduled meeting. Responsibilities of the Trustees as stated in the Bylaws include the following:

- The Trustees shall be responsible for all monies collected or disbursed by the 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 of the Trust and shall approve or disapprove such applications in accordance with rules promulgated by the Trustees.
- 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 established by the Trustees from time to time.
- The Trustees shall be responsible for and shall undertake the posting of such security deposits and/or security bonds as may be required to be posted with the TDCI.
- The Trustees shall be responsible for and shall cause to be filed with the TDCI 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 governmental regulations.
- The Trustees shall take all necessary precautions to safeguard the Fund and the other assets of the Trust including designating the administrator and the service agent of the Fund.

### **CONFLICTS OF INTEREST AND PECUNIARY INTERESTS**

Tenn. Comp. R. & Regs. 0780-1-54.07(6) and (7) state:

“No administrator or its employees or the pool’s board of trustees shall accept, or be the beneficiary of, either directly or remotely, any fee, brokerage, commission, gift or other consideration for or on account of any loan, deposit, sale payment, exchange, or reinsurance transaction made by or on behalf of such pool, or be pecuniarily interested in such purchase, sale, loan, either as borrower, principle, co-principle, agent or beneficiary, except that if a member, such person shall be entitled to all of the benefits accruing under the terms of the membership.”

“No administrator or its employees or the pool’s board of trustees shall take or receive for their own use any fee, brokerage, commission, gift or other consideration of the pool except for reasonable compensation for services performed or sales or purchases made to or for the pool in accordance with the terms of the administrator contract approved by the Commissioner. No administrator or its employees or the pool’s board of trustees shall collect a commission for the procurement of excess insurance for the pool.”

During the course of the examination, no instances of non-compliance with the Rule were found.

### **CORPORATE RECORDS**

The Trust's Bylaws state that the members of the Board of Trustees shall meet quarterly, or as often as required, at the principal office of the Trust, or at such other location as may be acceptable to the Trustees. Special meetings of the Trustees may be called at any time and may be by telephone conference calls or other methods of communication by which all Trustees participating may simultaneously hear each other. The members of the Trust shall meet annually on the first Tuesday in May of each year at the offices of the Trust or at such other place and time as may be determined by the Board of Trustees. During the period under examination, there were twenty-three (23) regular and special meetings of the Board of Trustees and five (5) meetings of the members of the Trust. The minutes of the meetings were reviewed and appear to reflect properly the acts of the respective bodies. Membership requirements, powers and duties of board members, and Trust members were verified to be in accordance with the Rules of the TDCI.

## **MANAGEMENT AGREEMENTS**

### **ADMINISTRATIVE AGREEMENT**

On December 17, 1990, the original "Administrative Agreement" was executed between Tennessee Automotive Association Service Company (TAASC) and the Trust. Thereafter, TAASC and the Trust entered into a revised "Administrative Agreement" effective January 5, 2006. The Board of Trustees of the Trust has engaged TAASC to act as the administrator of the Trust within the meaning of Tenn. Comp. R. & Regs. 0780-1-54-.02(1) and (2), to carry out the policies established by the Board of Trustees, and to provide day-to-day management of the Trust, to the extent such functions are not performed by the service agent. TAASC shall provide the following services for the Trust:

- Maintaining in effect the certificate of approval issued to the Trust by the Department of Commerce and Insurance
- Maintaining the accounting books and records
- Preparing all reports
- Providing all clerical, secretarial, and administrative support
- Receiving the premiums paid by the members

- Depositing the premiums in the claims fund account
- Administering and investing the claims fund and the administrative fund
- Preparing an annual budget and paying for reasonable expenses
- Negotiating on behalf of the Trust with the service company

The "Administrative Agreement" requires the administrator to be paid monthly by the Trust. This payment shall be based on a percent of the earned normal premium, defined as the gross premiums accrued by the Trust, plus or minus experience modifications. The amount charged by the administrator shall be approved by the Board of Trustees of the Trust.

TAASC is required to furnish to the Board of Trustees of the Trust audited financial statements on or before one hundred twenty (120) days after the end of the fiscal year and unaudited financial statements for each quarter on or before forty-five (45) days after the end of each fiscal quarter. These reports are required to include known claims and expenses, claims incurred but not reported, unearned premiums, and bad debts.

This agreement became effective on the date the Trust received a Certificate of Approval from the Commissioner and will continue in force until terminated as hereafter provided. The Trust may terminate the agreement without cause upon sixty (60) days written notice or with cause immediately upon written notice to the administrator. The administrator may terminate the Agreement without cause upon one hundred twenty (120) days written notice or with cause upon thirty (30) days written notice.

#### **CLAIMS PROCESSING AGREEMENT**

During the period of examination, and effective from October 1, 2007, through October 1, 2010, the Trust had an agreement with Brentwood Services Administrators, Inc. (BSA) that provided "Specified Third Party Administrator Services" in regards to claims processing and other related services.

The agreement with BSA in effect as of the date of this examination was effective October 1, 2010, to remain in effect until December 1, 2013. The agreement is automatically renewed for consecutive one (1) month terms at the ending date unless written notice of termination is provided by one party to the other party thirty (30) days prior to the ending date of the agreement or any one (1) month extension thereof, or a new agreement is entered into between the parties. Either party may terminate the agreement during its term by providing one hundred twenty (120) days prior written notice of termination to the other party.

The agreement stipulates that BSA will provide the following services:

- Providing claims services
- Providing loss control services
- Providing marketing and marketing assistance services
- Providing account management services
- Hosting and maintaining the Trust's website [www.taasit.com](http://www.taasit.com)

Examples of claims services to be provided are:

- Service, review, investigate, adjust, process and/or resist workers' compensation claims presented against the Trust
- Establish claim reserves and provide continuous review and update as necessary
- Prepare loss reports for Trust management no less than fifteen (15) days following the last day of the previous calendar month
- Prepare, maintain and file any and all records and reports that may be required by any state regulatory agencies in connection with BSA's handling of claims as instructed by the Trust

Examples of loss control services to be provided:

- Provide qualified loss control consultants to visit member employers
- Confer with management of member employers to review their current loss control program and assist in modification if needed
- Perform site surveys for hazard identification and assist members by providing information on third party contractors experienced in industrial hygiene and OSHA compliance

Examples of marketing and marketing assistance services to be provided:

- Develop and implement a marketing plan with the Trust's assistance to promote and present to prospective members

Examples of account management services to be provided:

- Develop underwriting rules for member employers to obtain workers' compensation coverage through the Trust in accordance with Trust rules and excess insurance carrier(s)'s rules and guidelines
- Prepare member packets including contribution/payroll self-reporting forms
- Develop appropriate contribution amounts for each member using classification codes, rates, modifiers, etc., consistent with appropriate law
- Prepare a seventeen (17) line unaudited loss report and risk intervention program report for each Board of Trustee's meeting

The Trust agrees to pay BSA a percent of earned normal premium on a monthly basis calculated in accordance with the formula exhibited in the Fee Schedule of the agreement. The Fee Schedule makes an allowance in the event that earned normal premium increases due to (a), the loss costs approved by the TDCI or (b), the value of any other component of the Tennessee premium calculation algorithm that is not a function of the Trust's loss cost multiplier or the experience of the participants of the Trust.

#### **MEDICAL BILL REVIEW SERVICES AGREEMENT**

Effective October 1, 2010, the Trust entered into an agreement with BSA for medical bill review. This agreement had the same renewal and termination terms as the above Claims Processing Agreement. BSA was paid a percentage of all savings derived from reductions to the medical provider's bill down to the fee schedule or usual and customary charges, as applicable, or resulting from the use of preferred provider organization savings.

The prior agreement with BSA for medical bill review was effective from October 1, 2007, through October 1, 2010.

#### **MEDICAL COST CONTAINMENT SERVICES AGREEMENT**

Effective October 1, 2010, the Trust entered into an agreement with BSA for medical cost containment services for larger medical expense claims or claims in which applicable law requires such services. This agreement had the same renewal and termination terms as the above Claims Processing Agreement and Medical Bill Review Services Agreement. BSA is paid a stated hourly rate depending on the service rendered. Examples of the services covered under this agreement range from physician review to on site case management.

The prior agreement with BSA for medical cost containment was effective from October 1, 2007, through October 1, 2010.

### **ROYALTY AGREEMENT**

Beginning January 1, 1992, and continuing through the period of examination, the Trust paid royalty fees to the TAA equal to a percentage of earned normal premium. Such fees were approved by the Board of Trustees to be paid to the Association for the use of the TAA trade name in the marketing efforts of the Trust.

### **CUSTODIAL AGREEMENT**

The Trust and its custodian, First Tennessee Bank National Association, completed a new custodian agreement during the period of examination. The new agreement signed by the custodian on February 18, 2009, and by the Trust on February 19, 2009, exhibited language compliant with Tenn. Comp. R. & Regs. 0780-1-46 (revised effective May 26, 2013).

### **INVESTMENT ADVISORY AGREEMENT**

The Trust was a party to an investment advisory agreement with Highland Capital Management, LLC (Highland) during the period of examination. The most recent agreement was executed and signed by the President of TAASC on behalf of the Trust on May 12, 2011.

This agreement gives Highland discretion to supervise and direct, on a continuing basis, as agent and attorney-in-fact on behalf of the Trust without prior consultation, the investment and reinvestment of all assets, subject to the limitations, needs and objectives imposed by the Trust. The agreement includes a schedule of compensation which was reviewed as part of the examination and was determined to be reasonable.

This agreement's schedule of compensation notes that fees are calculated quarterly, based upon market value of all assets under management in the account. Generally, one fourth of the annual fee will be billed in arrears each quarter.

## **FIDELITY BONDS AND OTHER INSURANCE**

Tenn. Comp. R. & Regs. 0780-1-54-.07(3)(b) requires an administrator applying for a license from the Commissioner of the TDCI to provide evidence of fidelity bond in the amount of \$200,000 written by a company licensed to transact business in this state.

The Trust's administrator, TAASC, maintains a Miscellaneous Professional Liability policy with Ironshore Specialty Insurance Company in the amount of \$1,000,000 each claim with a \$1,000,000 policy aggregate and a \$25,000 deductible.

Also, the Trust's administrator, TAASC, maintains a fidelity bond with Western Security Company for employee coverage in the amount of \$20,000. This policy became effective January 1, 1991, and was still in effect as of December 31, 2012.

The Trust maintains an Errors and Omissions policy with Navigators Specialty Insurance Company in the amount of \$1,000,000 each claim with a \$1,000,000 policy aggregate and a \$25,000 deductible. This policy's definition of insured would include the Trustees and members. The policy complies with Tenn. Comp. R. & Regs. 0780-1-54-.04(2)(b)(5) which requires each applicant for a certificate of authority to have in place an errors and omissions policy "for the board of trustees issued to protect the pool from damages, if any."

BSA maintains certain insurance coverage as required under its "Agreement to Provide Specified Third Party Services" dated October 1, 2010. These include general liability, auto liability, workers' compensation, contractual liability, and crime coverage. The following policies are issued by insurance companies within the Travelers umbrella of companies and Fidelity and Deposit Company of Maryland:

- The crime policy is issued by Fidelity and Deposit Company of Maryland and covers employee theft up to \$5,000,000 with a \$50,000 deductible.
- The workers compensation policy is issued by The Travelers Casualty and Surety Company with standard limits for both workers compensation and employers liability.
- The auto policy is issued by The Travelers Indemnity Company of Connecticut with a \$1,000,000 liability limit for one accident or loss, a \$2,000 limit for medical, and a standard limit for uninsured motorist. The policy provides for the lesser of actual cash value or cost of repair minus the deductible for auto physical damage.
- The commercial general liability policy is issued by Travelers Property Casualty Company of America with a \$2,000,000 general aggregate limit and a \$1,000,000 limit each occurrence with a \$1,000 deductible for business owners property coverage per occurrence and a \$250 deductible for building glass per occurrence.

- The commercial excess liability (umbrella) policy is issued by The Travelers Indemnity Company with a \$10,000,000 aggregate limit and a \$10,000 retained limit per occurrence.

All of the above insurance companies are licensed in the State of Tennessee with the exception of Ironshore Specialty Insurance Company and Navigators Specialty Insurance Company which operate as surplus lines carriers pursuant to Tennessee insurance statutes.

### **STATUTORY DEPOSITS**

In compliance with Tenn. Comp. R. & Regs. 0780-1-54-.04(3)(e), the Trust maintained the following deposit as of December 31, 2012:

<u>Description</u>	<u>Par Value</u>	<u>Statement Value</u>
Kingsport TN SCH GO 3.7%, due 5/01/2015	\$100,000	\$105,875

### **EXCESS OF LOSS INSURANCE**

In accordance with Tenn. Comp. R & Regs. 0780-1-54-.04(3)(c), the Trust had in effect, for the period January 1, 2012, to January 1, 2013, an excess of loss agreement for workers compensation and employers liability claims with Safety National Casualty Corporation. The agreement contains both specific and aggregate coverage.

Under the agreement's specific coverage, the excess insurer agrees to indemnify the Trust for the amount in excess of the Trust's \$450,000 specific retention for each accident or employee disease up to the statutory limit for workers' compensation and up to \$1,000,000 for employers' liability.

The aggregate portion of the agreement limits the Trust's obligation for losses and claim expenses incurred during 2012 to one hundred nine percent (109%) of earned premium which equates to a minimum retention of \$8,171,702. Under the agreement's aggregate coverage, the excess insurer agrees to indemnify the Trust for the sum of losses and claims expenses in excess of the Trust's limitation subject to a limit of indemnity of \$2,000,000.

The Trust's excess of loss policies have historically covered the one (1) year period of time commencing January 1 for each year since inception of the Trust. The contracts have been with different carriers and have had slightly different retentions and levels of

loss with the aggregate retention ranging from eighty percent (80%) to one hundred nine percent (109%) of earned premium.

A summarization by policy year for the period under examination is listed below:

<u>Policy Year</u>	<u>Specific Retention</u>	<u>Aggregate Indemnity</u>	<u>Aggregate Retention</u>	<u>Insurer</u>
1/1/08-09	\$400,000	\$2,000,000	\$9,561,640	Midwest Employers Casualty
1/1/09-10	400,000	2,000,000	7,591,740	Safety National Casualty
1/1/10-11	400,000	2,000,000	7,471,461	Safety National Casualty
1/1/11-12	400,000	2,000,000	7,495,832	Safety National Casualty
1/1/12-13	450,000	2,000,000	8,471,821	Safety National Casualty

The policies provide coverage for losses sustained by the 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. The policies have an aviation endorsement and provisions for the continuation of coverage in the event of plan insolvency. The policies were written by companies authorized to do business in the State of Tennessee.

Reliance National Indemnity Company provided the Trust specific and aggregate excess insurance coverage for fund years 1994 through 1999. During the year 2000, Reliance National Indemnity Company was merged into its parent company, Reliance Insurance Company. On October 3, 2001, Reliance Insurance Company was placed in liquidation by the Commonwealth Court of Pennsylvania and recoveries from the Reliance companies ceased.

The Trust's reserves reflect the insolvency of the Reliance companies and were increased to reflect the unlikely nature of any recoveries for the open excess claim incurred in the 1998 policy year. In addition, Trust's audited financial statements did not reflect any recovery amounts from Reliance as they were considered uncollectable by the Trust and its auditor.

## LOSS EXPERIENCE

<u>Year</u>	<u>Premiums Earned</u>	<u>Incurred Losses &amp; LAE</u>	<u>Underwriting Ratio</u>	<u>General &amp; Adm. Expense</u>	<u>Gen. &amp; Adm. Expense to Premium</u>	<u>Combined Ratio</u>
2008	\$8,452,136	\$3,098,884	36.7%	\$2,574,641	30.5%	67.1%
2009	6,621,291	5,328,162	80.5%	1,683,010	25.4%	105.9%
2010	6,731,253	4,920,040	73.1%	1,717,049	25.5%	98.6%
2011	6,740,583	8,357,884	123.9%	1,691,807	25.1%	149.1%
2012	7,565,403	5,179,063	68.5%	1,939,434	25.6%	94.1%

## ACCOUNTS AND RECORDS

### Financial Records

Tenn. Comp. R. & Regs. 0780-1-54-.09(2) requires the Trust to submit to the Commissioner a statement of financial condition audited by an independent certified public accountant on or before the last day of the sixth (6th) month following the end of the Trust's fiscal year. Tenn. Comp. R & Reg. 0780-1-54-.09(5) allows the Trust's audited financial statements to be prepared in accordance with Generally Accepted Accounting Principles (GAAP).

The Trust retained an independent accounting firm, LBMC, to issue the Trust's GAAP audited financial statements and to prepare their federal income tax and Tennessee Franchise and Excise tax returns.

During the period of examination, the Trust's accountant recorded all assets, liabilities, cash receipts, and disbursements, and produced a detailed General Ledger using QuickBooks. The Trust's auditor, LBMC, prepared all year-end adjusting entries and a trial balance as of year-end in conjunction with its annual audit of the Trust.

Claims accounting records were originally produced from cash disbursement source documents prepared by BSA. The Trust's auditor, LBMC, and actuarial firm, Casualty Actuarial Consultants, Inc. (CAC), rely upon BSA for individual case reserve estimate information for use in the Trust's audited financial statements and actuarial reports.

In conducting this examination, the TDCI did not retain the services of an independent actuary to review the reserves established by the Trust's actuary.

Member premium calculation and billing records originated from BSA's underwriting division including the calculation of loss experience modification factors. BSA relied upon final audited member payroll information from Tracz & Associates to calculate final audited premium.

The Trust was dependent upon its investment advisor, HCM, for the calculation of amortized cost of its bond investments shown on the balance sheet in the Trust's audited financial statements.

### **Information Systems**

The majority of the Trust's information systems and data requirements were provided by the Trust's administrator, TAASC, and the Trust's third party administrator, BSA, under the two (2) management agreements previously discussed.

TAASC used Tennessee Automotive Association (TAA) information technology equipment. TAA, in part, conducted business electronically using basic contemporary computing and networking methods. TAA had a domain server/client computing arrangement facilitated by a server. TAA employees worked from individual personal computer desktop workstations authenticating against a server file and print server. Users communicate internally and externally via electronic mail (e-mail). TAA's access control software consisted of a firewall and included data encryption technology. TAA used basic database management software and basic business accounting software.

The Trust's claims service provider and underwriter, BSA, utilized a hardware platform and operating system. BSA had operating system security software protection in place. BSA implemented a state of the art firewall system that prevented any outside access to BSA's information technology system or BSA's claims system. BSA had a local area network of connected desk top computers that ran on Windows operating systems. BSA used a software program for workers' compensation claim processing. BSA's underwriting division used underwriting software and software for premium computation and billing.

The Trust's administrator and claims service provider both have disaster recovery plans for their information technology systems that provide for offsite recovery of data. However, TAASC's disaster recovery plan is not formally documented in writing.

### **Examination of Accounts and Records**

The Examiner's assessment of the Trust's overall control environment found limited internal controls and limited segregation of duties by those engaged by the Trust to perform key activities. The Trust had no employees and was totally dependent upon

related parties or third parties for the performance of the day-to-day operations of the Trust.

In light of the Trust's limited segregation of duties and limited internal controls, the Examiner performed tests and audit procedures deemed necessary to verify the accuracy of the Trust's accounts and records as of year-end 2012, including substantial verification of supporting documentation. General ledger trial balances were reconciled with the financial statements, and all were reviewed for completeness of disclosure and conformity to GAAP as permitted by Tenn. Comp. R & Reg. 0780-1-54-.09(5).

During the course of the examination, it was noted that the reporting for premiums receivable, as prescribed by Tenn. Comp. R & Reg. 0780-1-54-.09(3)(a) was incorrect. This issue is further addressed in the "Analysis of Examination Changes" and the "Comments and Recommendations" sections of the report. Except as otherwise commented upon in this report, the accounts and records examined appear to properly reflect the operations of the Trust during the period under examination and the status of the Trust as of the date of examination.

Books and records of the Trust are kept at the home office location of TAA:

2521 White Avenue  
Nashville, Tennessee 37204

Claims and underwriting records are kept at the office of BSA located at:

104 Continental Place  
Suite 200  
Brentwood, Tennessee 37027

The Trust maintained cash and cash equivalents on deposit at banks in excess of federally insured amounts. No losses have been experienced in such accounts, and management believes the Trust is not exposed to any significant credit risk related to cash and cash equivalents.

#### **Correction of Fund Year Deficits**

The Trust, on May 23, 2012, notified the TDCI of a 2008 fund year deficit of \$359,626.40 and a 2011 fund year deficit of \$1,407,601. The Trust requested a \$1,210,348.76 transfer of surplus from the 2007 policy year and a \$556,878.64 transfer of surplus from the 2009 policy year to cover the combined 2008 and 2011 fund year deficits totaling \$1,767,227.40. The TDCI, via a letter dated May 31, 2012, approved

the surplus transfers from the 2007 & 2009 policy years to the 2008 & 2011 policy years pursuant to Tenn. Comp. R. & Regs. 0780-1-54.24(1)(b).

## **LITIGATION AND CONTINGENT LIABILITIES**

As of December 31, 2012, the Trust had committed no reserves to cover any contingent liability. Various lawsuits against the Trust have arisen in the normal course of business relating to workers' compensation claims' settlements. Contingent liabilities arising from litigation are not considered material in relation to the financial position of the Trust.

## **MARKET CONDUCT ACTIVITIES**

In conjunction with this examination, a market conduct review was made of the Trust as of December 31, 2012. The following areas were addressed:

### **UNDERWRITING**

#### **Underwriting - Membership Files**

Tenn. Comp. R. & Regs. 0780-1-54-.08 (1) (*Members of the Pool*), states:

"The board of trustees shall establish underwriting guidelines with respect to the addition of members to the pool as well as the renewal of its members. At a minimum, such underwriting guidelines shall set forth requirements for the members to be able to provide the pool evidence that the member is solvent. Each pool shall file such guidelines and any amendments thereto with the Commissioner no later than thirty (30) days prior to their proposed effective date."

During the period of examination, the Trust had published Underwriting Guidelines that were used in the acceptance and rejection of underwriting risk. The guidelines, which were filed with the TDCI on August 4, 2006, were found to be in compliance with the above rule requirements.

During the period of examination, the Trust conducted one hundred seven (107) member actions, including the following: twenty-three (23) new member files; thirty-five (35) member cancellations; thirty-two (32) member name changes; fifteen (15) name/location changes; and four (4) miscellaneous actions. All member actions were examined and found to be performed in accordance with Trust Underwriting Guidelines and in compliance with Tenn. Comp. R. & Regs. 0780-1-54-.08 (1).

### **Underwriting - Rate and Premium Contributions**

Trust underwriting rate and premium contributions were examined for compliance with Tenn. Comp. R. & Regs. 0780-01-54-.10 (Rates and Rate Reporting). In compliance with Section .10(4) of this rule, the Trust filed with the Commissioner of the TDCI its loss cost multiplier (LCM) and supporting documents for each year during the period of examination. The Trust's use of the LCM was further verified in the review of member underwriting files.

In the examination of member underwriting files, the examiners used ACL software to randomly select thirty (30) files from the Trust's total membership of two hundred fifty-three (253). The examination focused on the Trust's calculation of the members' 2012 estimated and audited premiums to include use of authorized rates, experience modifications, and discounts in determining member premium contributions. As a result of the examination, the following exceptions were noted:

- Two (2) members who had not annually renewed their Drug Free Workplace certification pursuant to Tenn. Comp. R. & Regs. 0800-02-12-.02(5), and therefore did not qualify for the credit, were given the Drug Free Workplace credit. One (1) member, who had recently purchased an additional dealership but had not applied for the Drug Free Workplace program for the new dealership, was extended the Drug Free Workplace credit on the new dealership. The above errors resulted in an underpayment of audited premium in the amount of \$6,244.
- One (1) member was charged an incorrect premium volume discount on their 2012 audited premium notice that resulted in the member's overpayment of audited premium in the amount of \$291.

### **ADVERTISING**

In the examination of Trust's advertising, items issued by the Trust were examined in accordance with Tenn. Code Ann. § 56-8-104 (1) (Misrepresentations and False Advertising of Insurance Policies) and Tenn. Code Ann. § 56-8-104 (2) (False Information and Advertising Generally). The Trust's print material, bulletins, and internet website was examined in accordance with the statute and found to be in compliance. The Trust was found to have strong controls in place for the production and use of all advertising materials approved by the Trust's administrator, TAASC.

### **CLAIMS REVIEW**

The Trust's processing of workers' compensation claims was examined for compliance with claims handling standards as required by the Department of Labor, Division of Workers' Compensation Tenn. Comp. R. & Regs. 0800-2-14.

The examiners used ACL to randomly select two samples from the claims population. One sample of thirty-nine (39) claims was selected from two hundred ninety (290) open claims as of December 31, 2012. A second sample of thirty-nine (39) claims was selected from one thousand, one hundred seventy-three (1,173) claims that were opened and closed during the examination period, January 1, 2008 to December 31, 2012. In total, a combined sample of seventy-eight (78) claim files was examined for compliance with Tenn. Comp. R. & Regs. 0800-2-14. As a result of the examination, the following exception findings are noted by rule section:

### **Reporting Requirements**

There were four (4) exceptions where the Trust was unable to provide the original claim file for examination. In place of the original file, the Trust provided files recreated from computer data and imaged records that did not contain a copy of the original C20 Form (First Report of Injury) with a stamped date of receipt. Without dated proof of insurer receipt of the C20 Form from the employer in these files, accurate calculation of the time taken to make initial contact with the claimant, employer, and physician (three (3) point contact) could not be determined.

Tenn. Comp. R. & Regs. 0800-2-14-.03 (1) requires employers to report accidents to their insurer within one working day of knowledge of injury. In the sample, there were twenty-two (22) exceptions found where employers failed to report an accident within one (1) working day of knowledge of the injury.

### **Investigation**

Tenn. Comp. R. & Regs. 0800-2-14-.04 (1) requires the insurer to make verbal or written contact with the claimant within two (2) working days of notice of accident to verify accident details. In the sample, there were seven (7) exceptions found where the Trust failed to contact the claimant within the required number of days.

Tenn. Comp. R. & Regs. 0800-2-14-.04 (2) requires the insurer to make personal or telephone contact with the employer within two (2) working days of notice of accident to verify details. In the sample, there were six (6) exceptions found where the Trust failed to contact the employer within the required number of days.

Tenn. Comp. R. & Regs. 0800-2-14-.04 (4) requires the insurer to make contact with physicians' who rendered medical services to claimants within seventy-two (72) hours of verbal or written notice to confirm injury and treatment to make a preliminary compensation determination. In the sample, there were six (6) exceptions found where the Trust failed to contact the treating physician within the required timeframe.

Tenn. Comp. R. & Regs. 0800-2-14-.04 (6) states, that when third party subrogation recovery is appropriate, the insurer shall develop a strategy to promptly obtain needed evidence. The TPA's internal control requires the possibility of subrogation be considered and documented on all claims. In the sample, there were eight (8) exceptions found where subrogation possibilities were not addressed or documented. Although subrogation was not documented in some files, no claim was found where the potential for subrogation was missed.

Tenn. Comp. R. & Regs. 0800-2-14-.04 (7) and (8) require that the decision on workers' compensation insurance coverage and compensability be made within fifteen (15) days of verbal or written notice of accident, and that claimants and employers be notified of the decision within the same timeframe. In the sample, there were two (2) exceptions found where the notification of compensability did not occur within the required timeframe.

### **Payment of Benefits**

Tenn. Comp. R. & Regs. 0800-2-14-.05 requires compensation payments for an injury be received by the claimant no later than fifteen (15) days after notice of injury, and that compensation benefits be issued timely to assure the injured employee receives the benefits before the date they are due. In the sample, there was one (1) exception found where the initial compensation payment was delayed; however, all follow-up payments were made when due. All other payments were made within the required timeframe.

### **Case Reserves**

The Trust established and maintained adequate reserves for, known claims and expenses, claims incurred but not reported (IBNR), and bad or uncollectible debt pursuant to Tenn. Comp. R. & Regs. 0780-01-54-.11(4).

In the examination of case reserves, the examiner considered the reserve established in each case and the overall reserve pattern present in the sample in determining if the Trust established and maintained adequate reserves. The examiner found no exceptions where the case reserve appeared to be inadequate. In general, during the period of examination, the Trust exercised a conservative reserve policy that resulted in establishment of an adequate reserve in compliance with rule requirements.

### **POLICYHOLDER COMPLAINTS**

Complaints for Workers Compensation Claims are handled through the TN Department of Labor and Workforce Development (TDOL). All information on how to request assistance is posted on the TDOL website: [www.tn.gov/labor-wfd/wcomp.shtml](http://www.tn.gov/labor-wfd/wcomp.shtml). The

website also provides information assistance related to the filing of a complaint and provides a C-40A form for submission of a request for assistance.

In the examination of claims in the claims review portion of the examination, the examiner reviewed several files that contained copies of requests for assistance submitted by claimants through the TDOL website. In each case, the examiner reviewed the request submitted by the claimant and the response provided by the Trust back to TDOL. In all cases, the Trust responded in compliance with TDOL requirements.

### **PRIVACY OF NON-PUBLIC PERSONAL INFORMATION**

The Trust's members (policyholders) are commercial businesses. Tenn. Comp. R. & Regs. 0780-1-72, (Privacy of Consumer Information Regulations), includes in the definition of "Scope" the following:

"These rules do not apply to information about companies or about individuals who obtain products or service for business, commercial, or agricultural purposes."

BSA processes the claims of the beneficiaries of the workers' compensation policies issued by the Trust to its members. In the agreement for "Specified Third Party Administrator Services" with the Trust, BSA includes confidentiality and protection language in an Addendum G. "Part 1" of the addendum states the parties hereto agree:

"all electronically stored information made accessible by Brentwood to TAASIT will not under any circumstance be revealed or released to any person or entity not directly in the decision making process of handling the claim to which the information refers;..."

The relationship of a beneficiary is addressed by Tenn. Comp. R. & Regs. 0780-1-72-.04(6)(b)5. A beneficiary in a workers' compensation plan is not solely considered a consumer of the licensee provided that the licensee does not disclose nonpublic information about the individual to a nonaffiliated third party other than as permitted under Rules 0780-1-72-.14, 0780-1-72-.15, and 0780-1-72-.16.

### **ANTI-FRAUD PLAN**

During the period of examination, the Trust formalized a written anti-fraud plan. Fraud detection procedures were in place, and the required fraud statement was exhibited on beneficiary claimant forms and applications as required by Tenn. Code Ann. § 56-47-112(b). The formalized anti-fraud plan was adopted February 20, 2009, and filed with

the TDCI on February 25, 2009. The "TAASIT Anti-Fraud Plan" language is in compliance with Tenn. Code Ann. § 56-47-112(a).

## **SUBSEQUENT EVENTS**

- (1) The Trust on May 17, 2013, notified the TDCI of a 2008 fund year deficit of \$134,588 and a 2011 fund year deficit of \$669,431. The Trust requested a \$514,338 transfer of surplus from the 2007 policy year and a \$289,682 transfer of surplus from the 2009 policy year to cover the combined 2008 and 2011 fund year deficits totaling \$804,019. The TDCI, via a letter dated May 24, 2013, approved the surplus transfers from the 2007 & 2009 policy years to the 2008 & 2011 policy years pursuant to Tenn. Comp. R. & Regs. 0780-1-54.24(1)(b).
- (2) At the June 18, 2013, Annual Meeting of the Trust's members, refunds of \$400,822 were distributed to the members. The request for this distribution was made to the TDCI on May 17, 2013, and subsequently approved by the TDCI on May 24, 2013.
- (3) The Tennessee Workers' Compensation Reform Act of 2013 became effective July 1, 2013, and is the most significant revision to the Tennessee workers' compensation law since the original 1919 act was passed. The 2013 Workers' Compensation Reform Act applies to injuries that occur on or after July 1, 2014.
- (4) The Trust and BSA entered into a new agreement to provide "Specified Third Party Administrator Services". The Trust met the filing requirement of Tenn. Comp. R. & Regs. 0780-1-54.05 by submitting this new agreement more than thirty (30) days prior to the effective date. The agreement was filed with the Commissioner on October 18, 2013, with an effective date of December 1, 2013.
- (5) On Thursday May 16, 2013, the Trustees voted to elect Russell Gwatney, Chairman of the Board of Trustees. Mr. Gwatney replaced the previous Chairman, Herb Adcox.
- (6) In November 2013, the Trust updated its signature cards for its administration and claims checking accounts in order to reflect representatives of the Trust that are currently authorized to issue checks.

## FINANCIAL STATEMENTS

There follows a balance sheet and a statement of operations and fund balance as of December 31, 2012, for the period under review, as established by this examination:

### BALANCE SHEET

#### Assets

Cash and cash equivalents	\$ 657,353
Investments	14,841,215
Premiums receivable (Note 1)	818,076
Other receivables	20,966
Accrued investment income	118,342
Reinsurance (excess insurance) receivable	73,437
Refundable income taxes	8,693
Restricted investments (State Deposit)	<u>105,875</u>
Total	<u>\$ 16,643,957</u>

#### Liabilities and Fund Balance

Loss and loss-adjustment expense reserve	\$ 9,766,865
Accounts payable to members	452,703
Accounts payable and accrued expenses	353,125
Distributions due to members (Notes 1 and 2)	4,254,333
Deferred revenue	440
Member deposits	<u>1,816,491</u>
Total Liabilities	16,643,957
Fund balance	<u>0</u>
Total	<u>\$ 16,643,957</u>

## STATEMENT OF OPERATIONS AND FUND BALANCE

### Revenues

Net premiums	\$7,565,403
Investment income	<u>377,317</u>
Total revenue	<u>7,942,720</u>

### Expenses

Loss and loss adjustment	5,179,063
Administrative fees	301,136
Bank charges	67,906
Payroll audit expense	53,675
Premium taxes	181,791
Professional fees	84,583
Reinsurance	459,859
Royalty fees	86,038
Service fees	692,385
Miscellaneous	<u>12,061</u>
Total expenses	<u>7,118,497</u>

Earnings before income taxes and distributions to members	824,223
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Income tax expense	<u>0</u>
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Earnings before distributions to members	824,223
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Examination adjustment to earnings before distributions to members. (Notes 1 and 2)	<u>(89,562)</u>
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Distributions due to (from) members	<u>734,661</u>
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Net earnings	<u><u>\$0</u></u>
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## ANALYSIS OF EXAMINATION CHANGES

### **NOTE 1 - PREMIUMS RECEIVABLE**

**\$818,076**

The above balance is \$89,562 less than the \$907,638 amount shown by the Trust on line three (3) of the Assets Section on the Balance Sheets page in its 2012 Audited Financial Statements as explained below.

The difference relates to: (1), Errors in the Trust's year-end 2012 Trial Balance totaling \$21,285 as compared to supporting documentation, and (2), the non-admittance of member premium receivable over ninety (90) days past due in excess of member deposits totaling \$68,278 pursuant to Tenn. Comp. R. & Regs. 0780-1-54.09(3)(a).

### **NOTE 2 - DISTRIBUTIONS DUE TO MEMBER**

**\$4,254,333**

The above balance is \$89,562 less than the \$4,343,895 amount shown by the Trust on line four (4) of the Liabilities Section on the Balance Sheets Page in its 2012 Audited Financial Statements as explained below.

The liability for "Distributions due to members" was composed of undistributed earnings and is considered by the TDCI and the Trust to be surplus funds in accordance with Tenn. Comp. R. & Regs. 0780-1-54-.11(1).

In order to reduce the non-admitted amount of premiums receivable by \$89,562 pursuant to Tenn. Comp. R. & Regs. 0780-1-54.09(3)(a), the liability for "Distributions due to members" reported on the Balance Sheets was reduced by \$89,562 and the "Distributions due to members" expense item disclosed on the Statements of Operations and Fund Balance was reduced by \$89,562.

Therefore, for purposes of this examination, the liability for "Distributions due to members" was \$4,254,333.

**SUMMARY SCHEDULE FOR "ANALYSIS OF EXAMINATION  
CHANGES"**

<u>Item</u>	<u>Members' Fund Balance</u>	
	<u>Increase</u>	<u>Decrease</u>
Premiums Receivable		\$89,562
Distributions Due to Members (Unassigned Funds)		<u>89,562</u>
Net Change to Fund Balance		<u>\$ 0</u>

## COMMENTS AND RECOMMENDATIONS

### Comments

- (1) Prior to the completion of this examination, the Trust entered into a third party administrator service agreement with BSA, effective December 1, 2013. This agreement was filed with the Commissioner on October 12, 2010, in compliance with the filing requirement of Tenn. Comp. R. & Regs. 0780-1-54.05 and is discussed in the report under the caption Subsequent Events.
- (2) The Trust, through the efforts of its outside counsel, received an excess insurance recovery in March 2012 from Reliance Insurance Company (in liquidation) in the amount of \$132,508. This payment was forty percent (40%) of the \$331,269 total recovery recognized by the liquidator of Reliance Insurance Company (Reliance).

This was the first excess insurance recovery the Trust received since Reliance was placed in liquidation on October 3, 2001, by the Commonwealth Court of Pennsylvania.

- (3) The Trust's audited financial statements prepared by the Trust's independent auditor, LBMC, and submitted to the TDCI on a GAAP basis have historically reported all earnings as "Distributions due to members." "Distributions due to members" were reported as a liability on the Trust's balance sheet since its inception.

Consequently, this accounting method produced a \$0.00 amount for "Net earnings" and a \$0.00 amount for "Fund balance" or members' surplus as of year-end. Historically, the liability for "Distributions due to members" was increased if revenue exceeded expenses for a policy year and was decreased upon the payment of distributions to members or if expenses exceeded revenue for a policy year.

The liability for "Distributions due to members" was composed of undistributed earnings and is considered by the TDCI and the Trust to be surplus funds in accordance with Tenn. Comp. R. & Regs. 0780-1-54-.11(1).

Beginning effective March 16, 2009, Tenn. Comp. R. & Regs. 0780-1-54-.11(1) required a pool or trust to establish and maintain an aggregate surplus equal to thirty percent (30%) of the unpaid claims liability of the pool or trust. The examination total for "Loss and loss adjustment expense reserves" was \$9,766,865 on a discounted

basis as of December 31, 2012. The Examiners determined that thirty percent (30%) of \$9,766,865 was \$2,930,060.

The \$4,254,333 examination total for "Distributions due to members" exceeded thirty percent (30%) of the discounted unpaid claims liability of the trust which equated to \$2,930,060. Therefore, the Trust was in compliance with the surplus requirements of Tenn. Comp. R. & Regs. 0780-1-54-.11(1) as of December 31, 2012.

The amount of undistributed earnings available to be returned to the Members by the Trust was limited by the surplus requirements of Tenn. Comp. R. & Regs. 0780-1-54-.11(1).

### **Recommendations**

- (1) It is recommended that the Trust implement controls in order to ensure compliance with the filing requirements of Tenn. Comp. R. & Regs. 0780-1-54.05. Any amendments to the organizational documents or written contracts required to be provided to the Commissioner, pursuant to Tenn. Comp. R. & Regs. 0780-1-54-.04, must be filed with the Commissioner no later than thirty (30) days prior to the proposed effective date of the contract.

A third party administrator service agreement with BSA, effective October 1, 2010, was filed with the Commissioner on October 12, 2010. The Trust's submission of the agreement to the Commissioner did not meet the filing requirement of Tenn. Comp. R. & Regs. 0780-1-54.05.

- (2) It is recommended that the Trust non-admit member premium receivable over ninety (90) days past due in excess of member deposits pursuant to Tenn. Comp. R. & Regs. 0780-1-54.09(3)(a) in future audited financial statements submitted to the TDCI.
- (3) It is recommended that the Trust, when calculating member premium, apply a Drug Free Workplace credit only to those members that have applied and received approval from the Tennessee Department of Labor, Division of Workers' Compensation, on an annual basis pursuant to Tenn. Comp. R. & Regs. 0800-02-12-.02(5).
- (4) It is recommended that the Trust refine its internal controls in order to more completely comply with the claim-handling requirements of Tenn. Comp. R. & Regs. 0800-2-14 – Claims-Handling Standards. These exceptions were disclosed in the

Claims Review subsection of the "Market Conduct Activities" section of this examination report.

- (5) It is recommended that the Trust's administrator, TAASC, obtain an Administrator License from the Commissioner, as required pursuant to Tenn. Comp. R. & Regs., Ch. 0780-1-54-.07.

## CONCLUSION

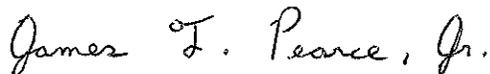
Insurance examination practices and procedures, as promulgated by the National Association of Insurance Commissioners, have been followed in connection with the verification and valuation of assets and the determination of liabilities of Tennessee Automotive Association Self-Insurers Trust of Nashville, Tennessee. Additionally, Tennessee Code Annotated and Tennessee Comprehensive Rules and Regulations have been followed in connection with the verification and valuation of assets and the determination of liabilities of the Trust.

In such manner, it was determined that, as of December 31, 2012, the Trust had assets of \$16,643,957 and liabilities, exclusive of distributions due to members, of \$12,389,624. Thus, there existed for the additional protection of the members of the Trust, the amount of \$4,254,333 in the form of distributions due to members (undistributed earnings).

The courteous cooperation extended by the Chairman of the Trust's Board of Trustees, the officers of the Tennessee Automotive Association Service Company, representatives of Brentwood Services Administrators, Inc., the representatives of Lattimore, Black, Morgan & Cain, P.C., and the President of Casualty Actuarial Consultants, Inc., during the course of the examination is hereby acknowledged.

In addition to the undersigned, Gregory Bronson, CIE, AMCM, ALMI, AIRC, Insurance Examiner, representing the State of Tennessee, participated in the work of this examination.

Respectfully submitted,



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James T. Pearce, Jr.  
Insurance Examiner  
State of Tennessee

**AFFIDAVIT**

The undersigned deposes and states that he has duly executed the attached examination report of Tennessee Automotive Association Self-Insurers Trust dated March 7, 2014, and made as of December 31, 2012, on behalf of the Department of Commerce and Insurance, State of Tennessee. Deponent further states 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.

James T. Pearce, Jr.

James T. Pearce, Jr.  
Insurance Examiner  
State of Tennessee

State Tennessee

County Davidson

Subscribed to and sworn before me

this 20<sup>th</sup> day of June, 2014

Notary Helen W. Dorsey

My Commission Expires: 11/06/2017





## TENNESSEE AUTOMOTIVE ASSOCIATION SELF INSURERS TRUST

TAA Building • 2521 White Avenue • Nashville, Tennessee 37204  
(615) 269-3433

### Board of Trustees

Russell Gwatney, *Chairman*  
Memphis

Rick Hill  
Kingsport

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Tullahoma

John Murrey  
Pulaski

Brent Smith  
Camden

Dave Kirk  
Crossville  
*ex-officio*

Yogi Vowell  
Fayetteville  
*ex-officio*

**Trust Administrator**  
Roberts V. Weaver, Jr.  
Nashville

June 26, 2014

E. Joy Little  
Director of Financial Examinations/Chief Examiner  
Tennessee Department of Commerce and Insurance  
500 James Robertson Parkway  
Nashville, TN 37243

RE: Tennessee Automotive Association Self Insurer's Trust – Report of Examination

Dear Ms. Little:

We hereby acknowledge receipt of the final Report of Examination for the Tennessee Automotive Association Self Insurer's Trust. By signing below, we indicate acceptance of the report, as transmitted, and without rebuttal.

Sincerely,

Roberts V. Weaver, Jr.  
President, Tennessee Automotive Association Service Company as Trust Administrator,  
Tennessee Automotive Association Self Insurer's Trust

