REPORT ON EXAMINATION

of the

TENNESSEE FORESTRY ASSOCIATION SELECTIVE WORKERS' COMPENSATION GROUP

2605 ELM HILL PIKE, SUITE G
NASHVILLE, TENNESSEE

as of

DECEMBER 31, 2009

DEPARTMENT OF COMMERCE AND INSURANCE

STATE OF TENNESSEE

NASHVILLE, TENNESSEE
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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 TENNESSEE FORESTRY ASSOCIATION SELECTIVE WORKERS' COMPENSATION GROUP

2605 ELM HILL PIKE, SUITE G
NASHVILLE, TENNESSEE 37214

hereinafter and generally referred to as the "Group," 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 January 25, 2010 in accordance with Tenn. Code Ann. § 50-6-405 and Tenn. Comp. R. & Regs. § 0780-01-54-.20. On-site examination work commenced on July 6, 2010. The examination was performed by duly authorized representatives of the Department of Commerce and Insurance, state of Tennessee ("TDCI").

With the Fund 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, 2005 to the close of business on December 31, 2009, 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 financial condition was conducted in accordance with guidelines
and procedures contained in the NAIC Financial Condition Examiners Handbook. During the course of examination, assets were verified and valued and liabilities were determined and estimated as of December 31, 2009. The financial condition of the Group and its degree 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 Group’s operations, practices, and 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.

In addition, the following topics were reviewed:

- History and Organization
- Trust Agreement and Declaration of Trust and Bylaws
- Indemnity Agreement
- Management and Control
- Corporate Records
- Management Agreements
- Related Party Services
- Fidelity Bonds and Other Insurance
- Statutory Deposits
- Market Conduct Activities
- Excess of Loss Insurance
- Retirement Plan and Other Employee Benefits
- Loss Experience
- Accounts and Records
- Pecuniary Interest
- Refunds or Distributions
- Litigation and Contingent Liabilities
- Subsequent Events
- Financial Statement

The previous examination was conducted as of December 31, 2004 by authorized representatives of the TDCI. The last previous examination report included various recommendations which were incorporated into Commissioner's Order No. 08-060 as “Directives”. These “Directives are stated as follows:

1. The Group is DIRECTED to comply with Tenn. Code Ann. § 56-5-313 by making written application to the Commissioner for approval of any deductible plans prior to making them available to members.

   Corrective Action: The deductible plans now used by the Group are filed with the TDCI and conform to standard to NCCI procedures and practices.

2. The Group is DIRECTED to comply with Tenn. Code Ann. § 56-47-112 by implementing and maintaining an anti-fraud plan and submitting an annual anti-
fraud report to the TDCI summarizing the Group's anti-fraud activities.

Corrective Action: The Group has an anti-fraud plan which was filed with the TDCI and stamped June 19, 2008.

3. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.06 by not extending credit to individual members for the payment of premium, except pursuant to plans that have been granted prior written approval by the Commissioner.

Corrective Action: The Group is not extending credit to individual members. In some cases, the audit premium is paid within two or three months with the member paying a portion in each month due to the current economic environment. Tenn. Comp. R. & Regs. § 0780-01-54-.08(9) does include language which states: "A pool shall cancel a member that is more than 120 days late in making a premium payment." The Group abides by this guideline.

Some members have asked for additional review and re-audit when questioning the NCCI occupational code which was used for the premium calculation. The sample tested during the examination indicates that audit premiums are paid.

4. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.08 by ensuring that member application and indemnity agreements are properly executed and maintained as permanent records.

Corrective Action: The Group maintains the application and indemnity agreement in the member file on site at the office of the Tennessee Forestry Association.

5. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.08 for the cancellation of members that fail to make timely premium payments in accordance with the cancellation policies established in the Group's bylaws.

Corrective Action: The Group now issues prompt notice of cancellation to a member for non-payment of premium.

6. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.10 by adhering to the uniform classification system, uniform rating plan, and the rules of the rate service organization designated by the Commissioner. No variance from these standards is permitted unless written permission is granted by the Commissioner.

Corrective Action: The Group currently complies with designated practices of NCCI.

7. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-
by filing any waiver of subrogation endorsements as required by Tenn. Code Ann. § 56-5-306.

Corrective Action: The Group filed a copy of its waiver with the TDCI.

8. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.11 by filing premium payment plans with the Commissioner for approval prior to their use and offering only those plans which have been approved by the Commissioner.

Corrective Action: The Group files its premium payment plans with the TDCI as part of its annual Premium Analysis prepared by the Group's actuary.

9. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.12 by applying the Tenn. Code Ann. § 56-4-210 investment credit to gross premiums only, in accordance with Tenn. Code Ann. § 56-4-206. The Group is further directed to provide appropriate documentation for any employers claiming an exemption from the TOSHA surcharge, as provided for in Tenn. Code Ann. § 56-4-206.

Corrective Action: Review of the Group's premium tax return indicates compliance with proper investment credit calculation and documentation of exemption from the TOSHA surcharge.

10. The Group is DIRECTED to ensure that the Group's investment policy is in compliance with Tenn. Comp. R. & Regs. § 0780-01-54-.13.

Corrective Action: The Group currently has an investment policy which complies with the regulation.

11. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.15 which states that "any monies for a fund year in excess of the amount necessary to fund all obligations for that fund year may be declared refundable by the board of trustees not less than eighteen (18) months after the end of the fund year, after written approval is granted to the pool by the Commissioner to disburse such funds."

Corrective Action: The Group made the following statement of position on refunds in relation to the "Directive."

"In order to maximize the assets of the Trust, we have designated the excess monies earned by the Trust as Distributions payable. This in no means should indicate that we intend to distribute these monies to the membership in the near future. Along with the requirement of approval of the Department, we will monitor the development of that surplus to ensure that the Trust will maintain adequate reserves to cover any future or past liabilities."
This designation is to ensure that those monies earned by the members of the Trust are not unduly taxed and thus reducing those earned monies and adding stability to the fund. This has been reviewed by our Accountant and deemed appropriate within acceptable accounting practices."

No distributions have been paid to members during the period of examination. Further discussion is included under the caption, "Refunds or Distributions."

12. The Group is DIRECTED to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.24 for the reporting of fund year deficiencies to the Commissioner and obtaining written approval from the Commissioner before using surplus funds from previous years to make up any fund year deficiencies.

Corrective Action: The Group currently requests approval before transferring surplus funds from previous years to make up any fund year deficiencies. The analysis is prepared by the Group's outside auditor.


Corrective Action: The Group re-audited the items which appeared to be unclaimed property following the prior examination. It was determined that the checks had been reissued and this process cleared the exceptions.

The current examination reviewed the items to determine compliance with the time line in the statues. The Group is currently in the process of putting in place a policy for the filing of the annual report even though there are no funds to be remitted to the state of Tennessee.

**HISTORY AND ORGANIZATION**

The Tennessee Forestry Association ("TFA") is a Tennessee non-profit trade association of saw millers, landowners, pulp and paper companies, loggers, manufacturers, foresters and business people which was organized in 1951. The TFA has been a viable, continuing entity since its inception, and currently includes more than 2,000 members in Tennessee.

On April 15, 1993, the Group was created by members of TFA to act as a self-insured workers' compensation pool in accordance with Tenn. Code Ann. § 56-6-405. Funding was provided by contributions of the initial members equal to 25% of their first year estimated annual premiums in accordance with Tenn. Comp. R. & Regs. § 0780-01-54-.04. The operation of the Group is confined to the state of Tennessee where it is licensed to transact the business of workers' compensation and employers' liability group self-insurance. Membership in the Group continues to be composed of qualifying members of TFA that have pooled their liabilities in accordance with the Tennessee
Workers' Compensation Act. New members in the Group are also required to make a contribution equal to 25% of their first year estimated annual net premium.

At December 31, 2009, the Group was licensed in one state, Tennessee.

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

<table>
<thead>
<tr>
<th>Fund Year</th>
<th>Members</th>
<th>Net Premium Revenue</th>
<th>Total Expenses</th>
<th>Assets</th>
<th>*Equity</th>
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<tr>
<td>2005</td>
<td>163</td>
<td>$8,269,343</td>
<td>$9,602,191</td>
<td>$9,084,689</td>
<td>$890,859</td>
</tr>
<tr>
<td>2006</td>
<td>153</td>
<td>6,786,222</td>
<td>5,530,982</td>
<td>9,142,081</td>
<td>1,945,530</td>
</tr>
<tr>
<td>2007</td>
<td>143</td>
<td>6,510,501</td>
<td>7,709,903</td>
<td>8,890,222</td>
<td>1,087,545</td>
</tr>
<tr>
<td>2008</td>
<td>127</td>
<td>5,055,723</td>
<td>4,433,214</td>
<td>8,432,394</td>
<td>2,501,767</td>
</tr>
<tr>
<td>2009</td>
<td>114</td>
<td>3,769,343</td>
<td>2,999,523</td>
<td>8,128,641</td>
<td>3,864,068</td>
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*Includes member distribution payable (undistributed earnings). Distributions are only paid with the express written approval of the Commissioner of Commerce and Insurance.

The above schedule does not exhibit investment income which is taken into account in determining the net income or loss of the Group for its years of operation. Net income or loss is exhibited on page 31 of this report under the caption, "Statement of Changes in Members' Equity."

The equity as of December 31, 2009 was adjusted based upon findings during this examination to $3,707,958. This is the result of after the fact premium audit adjustments which are discussed under the caption, "Analysis of Changes in Financial Statement and Comments Resulting from Examination."

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

The Group was created through the adoption of the Declaration of Trust and Bylaws which was executed on April 15, 1993. The Group was formed to act as a workers compensation self-insurance group in accordance with Tenn. Comp. R. & Regs. Chapter 0780-01-54 as authorized by Tenn. Code Ann. § 50-6-405. The Trust Agreement and Bylaws state the purpose of the Trust as follows:

- "This Trust is executed for the purpose 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 the 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 by developing and refining specialized claims services and loss prevention programs with the TFA."

The Trust is an association which is owned by its Members. Membership in the Trust consists of individuals, corporations, partnerships or other legal entities which are members in good standing of the TFA and which contribute to the Fund as a participating member in the Trust. The term Members includes those individuals, corporations, partnerships or other legal entities executing, or otherwise being bound by the Indemnity Agreement.

The principal office of the Trust is established as follows:

2605 Elm Hill Pike, Suite G
Nashville, Tennessee 37229

The above location is also the office of the TFA.

**INDEMNITY AGREEMENT**

In accordance with Tenn. Comp. R. & Regs. § 0780-01-54-.04(2)(e)2, each member is required to execute and be bound by an indemnity agreement as a condition of membership in the Group. Significant terms that each member agrees to include the following:

Each and all members jointly and severally agree 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 assessment 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 the Act or this agreement and liability of any member for unpaid contributions and assessments in the event of the Group's failure to enforce such of the member or members.

The Group's Board of Trustees shall use best efforts, in the event assessments require the performance of the members' joint and several obligations, to impose such assessments in an equitable manner against all members.

The members intend this agreement as a mutual covenant of assumption of joint and several liabilities 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 of Trustees may admit as members of the Group only acceptable and financially sound entities. Except as otherwise provided by the Regulation, the Board of Trustees shall 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 member shall provide in a form acceptable to the TDCI, a current financial statement. The Group shall file with the Commissioner on or before the day it is required to file its audited financial statement a copy of the said financial statement as required by Tenn. Comp. R. and Regs. § 0780-01-54-.08(12).

A member is not relieved of its workers' compensation liabilities incurred during the period of membership except through payment by the Group or the member of required workers' compensation benefits.

Each member agrees to initiate and maintain a safety program to give its employees safe and sanitary working conditions and agrees to follow the general recommendations of the Group, the Administrators, and Service Company to promote the general welfare of its employees.

The Board and the members have designated and appointed Employers Risk Services, Inc. as the Third Party Administrator or such substitute or replacement as shall be appointed by the Board subject to approval as a Third Party Administrator by the TDCI.

The Group may procure excess insurance to protect its members against excess losses as deemed necessary by the Board or as required by the Regulations.

**MANAGEMENT AND CONTROL**

The operation and administration of the Fund is the joint responsibility of a Board of Trustees consisting of not more than 15 or less than five (5) individuals. 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 in accordance with Tenn. Comp. R. & Regs. § 0780-01-54-.06. Trustees are elected for a term of five (5) years by the members of the Group and at least one (1) Trustee shall be a member of the Board of Directors of the TFA: but all Trustees need not be members of the Group.

The officers of the Group shall consist of a Chairman, Vice-Chairman and Treasurer. The Trustees may elect other officers as to them appear desirable. Officers shall hold Office until the first meeting of the Board of Trustees following the annual meeting or until their successor is chosen.
At December 31, 2009 the following persons were serving as members of the Board of Trustees:

Name and Address

Steve Collie
Manager
Hassell & Hughes Lumber Co., Inc.
608 Hwy 13 South
Collinwood, TN 38450

Bill Ring
President
TIKA Energies Co., Inc.
1014 Dallas Road, #101
Chattanooga, TN 37405

Bobby Cunningham, Jr.
Retired (Treasurer)
White County Lumber Co., Inc.
2920 Sullivan Knowles Road
Sparta, TN 38583

Phil Averitt
President
J. V. Averitt Lumber Co., Inc.
288 Clay Wright Road
Erin, TN 37061

Mike Barnes
LLC Member (Owner)
The Sawmill, LLC
295 Wildcat Hollow Road
Hohenwald, TN 38462

Don Miller
Retired (President)
Cleveland Wood Products
557 Sipes Road SW
Cleveland, TN 37311

Key responsibilities of the Trustees summarized from the Bylaws include the following:

- The Trustees may, at their discretion, invest, or direct to be invested any monies in excess of current obligation in accordance with applicable state and federal statutes.
• The Trustees will share with the members all of the Group's assets in excess of those amounts needed to cover losses and expenses, subject to the approval of the TDCI.

• The Trustees shall adopt a set of rules, regulations and guidelines which shall be entitled Tennessee Forestry Association Selective Workers’ Compensation Group Manual which shall at all time be followed by members.

• The Trustees may from time to time, establish a reasonable amount of compensation for attendance at regular or special meetings of the Board, annual meetings of Group membership, or for performance of the duties of a Trustee.

Certain services are purchased from outside contractors if needed. Such services include actuarial analysis and independent audit.

Actuarial Services: Casualty Actuarial Consultants, Inc.
7101 Executive Center Drive, Suite 225
Brentwood, TN 37027

Auditing Services: Shores, Tagman, Butler & Company, P.A.
17 South Magnolia Avenue
Orlando, FL 32801

Accounting and Bookkeeping Services: Donna M. Swann, CPA
3354 Highway 41 South
Springfield, TN 37172

Claims Processing Services: ERS, Inc.
(formerly known as Employers Risk Services, Inc.)
Post Office Box 628
1240 Fair Way Street
Bowling Green, KY 42102

Tennessee Location
109 International Drive, Suite 101
Franklin, TN 37067

Premium Audit: Overland Solutions, Inc.
P. O. Box 413866
Kansas City, MO 64141

Loss Control: ERS, Inc.
Post Office Box 628
1240 Fair Way Street
Bowling Green, KY 2102
CORPORATE RECORDS

The members of the Board of Trustees shall meet quarterly or as often as required, the exact date and place of said meeting to be furnished to the Board members by the Chairman or Secretary. Special meetings may be called at any time by the Chairman or any two members of the Board. Notice of regular and special meetings shall be given by mail, cable telegram, telephone or personal delivery.

The Members of the Group shall meet annually in conjunction with the Tennessee Forestry Association Annual Meeting.

During the period under examination there were 21 regular and special meetings of the Board of Trustees and 5 meetings of the members of the Group. The minutes of the board meetings and the membership meeting/notification documents were reviewed and appear to reflect properly the acts of the respective bodies. Membership requirements, powers and duties of board members and Group members were verified to be in accordance with the Rules of the TDCI.

MANAGEMENT AGREEMENTS

Administrative Agreement

The Group has used two administrators during the period of examination. Mr. George Colley served from October 10, 2003 until February of 2009. Mr. Mike Whitley acted as interim administrator up until March 17, 2010 when the Group and Mr. Whitley entered into the formal administration agreement. The Group filed the document with the TDCI while the examination was ongoing. The TDCI had previously been informed by letter that Mr. Whitley was acting as interim administrator.

The Administrator shall carry out the policies established by the Board of Trustees of the Group, and shall provide daily management of the Group, and shall conduct such other activities as required by applicable laws and regulations. Without limiting the foregoing, the Administrator’s delineated areas of authority, and duties and obligations, include the following:

- the purchase and selection of excess insurance;
- the purchase and selection of errors and omissions coverage for the Board of Trustees;
• the purchase and selection of necessary and prudent surety/fidelity bonds;
• the implementation of marketing policies approved by the Board of Trustees;
• underwriting authority to the extent such authority is not retained by the Board of Trustees by law or practice (as required by Tenn. Comp. R. & Regs. § 0780-1-54-.06(2)(c), the Board of Trustees retains the sole and undelegable authority to approve an application for membership into the pool and the initial premium of a new member);
• the payment of vendors and other expenses;
• the hiring and firing of the staff of the Administrator;
• the hiring and firing of a third party administrator, accountant, actuary, and other vendors deemed necessary or prudent to service the Group.

The Administrator's compensation is set by the Board of Trustees, and per the agreement, is set at a flat fee. This compensation is in accordance with Tenn. Comp. R. & Regs. § 0780-01-54-.07(5).

The Agreement shall continue in force and effect until terminated in accordance with its provisions, or by mutual agreement of the parties. It can be terminated by either party at any time upon not less than 30 days prior written notice.

Mr. Whitley filed the formal license application, "Application to Serve as Administrator of Group Self-Insurance Pool" while the examination was ongoing which was accepted by the TDCI. Mr. Whitley had worked for the Group for several years previously acting in the capacity of underwriter. He also holds a license as a property casualty insurance agent.

Mr. Whitley continues to act as Administrator, as defined within the meaning of Tenn. Comp. R. & Regs. § 0780-01-54-.02(1).

Claims Administration and Loss Control Agreement

The claims service/loss control contract with ERS, Inc. ("ERS") in effect the date of this examination was effective January 1, 2009 to remain in effect through December 31, 2011. This contract may be terminated with cause by either party by providing 60 days prior written notice or without cause by either party by providing 90 days prior written notice. ERS is currently licensed as a third party administrator with the TDCI. A summary of major provisions follows:

Claims Adjusting Authority and Responsibilities:

• ERS has the authority and responsibility to provide claims adjusting services for
the Group in connection with claims relating to occurrences under the workers' compensation insurance program subject to all terms and conditions of the Claims Administration and Loss Control Agreement.

- ERS shall receive and examine, on behalf of the Group, all reports of industrial injury to or disease of employees of the Group members reported to ERS and initiate procedures for the proper processing of each claim in accordance with applicable statutory and administrative regulations.

- ERS shall investigate each reported claim or loss, and adjust, settle or deny all claims in accordance with the Tennessee Workers' Compensation Law and subject to the ultimate authority of the Group.

- ERS shall establish and adequately reserve a claim file for each claim for which there is injury and/or anticipated liability and/or formal claim has been made.

- ERS shall furnish all claim forms necessary for proper claims administration.

- ERS shall furnish the Group with a monthly claim activity report.

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

- ERS shall maintain in force such insurances as are customary or required by law to protect itself and its clients. These include General Liability, Workers' Compensation, Fidelity Bond and Errors and Omissions Insurance Coverage.

Claim Settlement Authority:

- ERS shall have discretionary settlement authority of $100,000.

- The Group shall make funds available for ERS to draw from for claim and/or loss payments and for associated allocated expense.

- Loss payments exceeding $100,000 in the aggregate shall require the prior approval of the Group.

Loss Control Responsibilities:

- ERS shall provide consultation for the orientation of employees of the Group's members who are directly involved in the processing of claims and losses. ERS shall also employ and retain a loss control representative according to guidelines stated in the agreement.
- ERS shall provide on-site surveys for hazard identification and work practices evaluations for each member at least twice yearly.

- ERS shall provide written reports with appropriate summary of activities, listing of hazards and loss problems, and recommendations for improvement.

- For accidents reported to ERS, ERS shall provide accident analysis and investigation at the workplaces of the members to identify trends and problem areas for loss control focus.

- ERS shall provide consultation for safety and health training seminars for members as requested and mutually agreed.

- ERS shall provide on-site surveys for hazard identification and work practices evaluations for prospective members as determined by the Group.

The Group agrees to pay to ERS a service fee equal to a percent of the Group's earned Workers' Compensation premium for claims administration. At the end of the annual policy period, adjustments are made based on the actual audit of member's payroll for that period.

The Group agrees to pay ERS an additional annual fee equal to a percent of the Group's earned Workers' Compensation premium for loss control services.

Medical bill review for claims adjudicated is also provided by ERS for a fee of 22% of the amount saved. There shall be no fee for this service for any bills processed which do not generate a savings to the Group.

The old claims service agreement was on file for record with the TDCI; however, the current agreement had not been officially filed. When this was brought to management's attention, a filing was completed during the course of this examination. The Fund had mistakenly interpreted filing to only be required if there was a material change in a contract.

Tenn. Comp. R. & Regs. § 0780-01-54.05 requires:

"Any amendments to the organizational documents or written contracts required to be provided to the Commissioner by Rule 0780-1-54-.04 shall be filed with the Commissioner with a non-refundable filing fee of ninety dollars ($90.00) no later than thirty (30) days prior to the proposed effective date of the amendments."

Further discussion is included under the caption, "Comments and Recommendations."

The Agreement and the services provided are in accordance with Tenn. Comp. R. & Regs. § 0780-1-81.
Debt Collection Agreement

The Group is party to an agreement with Franklin Collection Service, Inc. ("Agency") of Tupelo, Mississippi for the collection of bad debts. The agreement has been effective since November 20, 2003, with termination with or without cause by either party requiring a 60 day written notice. Major provisions are as follows:

- The Agency is authorized to act as attorney in fact related to checks, drafts, etc received during the collection of accounts submitted by the Group.

- The Agency is authorized at its option to place accounts with Attorneys for collection through court action.

- The Agency will not accept for collection any account exceeding three (3) years old or less than ten dollars ($10.)

- The Agency’s fees are based on a percentage of the amounts collected from delinquent account and vary based on the age of the account.

- When filing suit in an effort to collect money, the Agency shall indemnify and hold harmless the Group for any claim brought by or against the Agency resulting in loss or damage including court cost and attorney’s fees.

Related Party Services/Royalty Agreement

Article VII, Section four (4) of the Group’s Bylaws state that the Group shall pay the TFA an annual royalty fee for the use of the Association’s name and logo. The Bylaws further state that the payment shall be made from the Group in an amount as determined by the Group’s Board of Trustees. During the period of examination, the Group provided annual royalty payments to TFA equal to one (1) percent of earned premium with no adjustment made for end of year member audited premiums. This arrangement is accordance with Tenn. Comp. R. & Regs. § 0780-1-54.

FIDELITY BOND AND OTHER INSURANCE

The Group maintains a financial institution bond with National Union Fire Insurance Company of Pittsburgh, Pa. with a limit of $200,000 per each claim and with a $200,000 aggregate limit, including $1,000 retention per claim. The policy covers losses resulting directly from dishonest or fraudulent acts committed by an "Employee" acting alone or in collusion with others. The Administrator is considered an "Employee" under this policy.

The Group maintains a directors’ and officers’ liability policy with National Union Fire Insurance Company of Pittsburg, Pa. with a $1,000,000 limit. The Group maintains a separate professional liability policy with the same insurer with a $2,000,000 limit which includes errors and omissions. The professional liability 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."

The Group has added the Administrator as an insured to their professional liability policy in order to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.07(3)(b) and (c) which exhibit the following requirements under the heading, Administrators:

- "Evidence that the applicant has obtained a fidelity bond in the amount of $200,000 written by a company licensed to transact business in this state, which may be obtained either by the administrator or the pool on the administrators’ behalf;"

- Evidence that the applicant has obtained an errors and omissions insurance policy for the protection of the pool in the amount of $200,000 written by company licensed to transact business in this state, unless waived by the Commissioner upon a showing of proof that the applicant is unable to obtain such coverage;"

The Group maintains an automobile policy which is issued by The Cincinnati Insurance Company with a $1,000,000 liability limit for one accident or loss and standard limits for medical and uninsured motorist.

The above insurance companies listed are licensed in the state of Tennessee.

Employers Risk Services, Inc. maintains certain insurance coverage as required under its "Claims Administration and Loss Control Services Contract" dated September 15, 2005. These include general liability, auto liability, workers’ compensation, crime and errors and omission coverage. The various coverage types are issued by various companies under one certificate as follows:

- The general liability policy is issued by Acuity, a mutual insurance company with a $2,000,000 general aggregate and $1,000,000 each occurrence limit.

- The auto liability policy is issued by Acuity with a $1,000,000 combined limit.

- The workers compensation policy is issued by Accident Fund Insurance Company of America with standard limits for both workers compensation and employers liability.

- The excess/umbrella policy is issued by Acuity with a $5,000,000 aggregate limit and a $10,000 retained limit per occurrence.

- The crime policy is issued by Acuity with a $500,000 limit subject to a $500 deductible per occurrence.
The errors and omissions policy is issued by Great American Excess and Surplus Insurance Company with a $6,000,000 aggregate limit.

The above insurance companies listed are licensed in the state of Tennessee.

**STATUTORY DEPOSITS**

In compliance with Tenn. Comp. R. & Regs. § 0780-1-54-04(e), the Group maintained the following deposit at December 31, 2009.

<table>
<thead>
<tr>
<th>Where Deposited and Description</th>
<th>Par Value</th>
<th>Statement Value</th>
<th>Market Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Tennessee</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>U. S. Treasury @ 3.875% due 10/31/2012</td>
<td>$500,000</td>
<td>$500,000</td>
<td>$500,000</td>
</tr>
<tr>
<td>Total</td>
<td>$500,000</td>
<td>$500,000</td>
<td>$500,000</td>
</tr>
</tbody>
</table>

**MARKET CONDUCT ACTIVITIES**

A market conduct review was made of the Group as of December 31, 2009, in conjunction with this examination. The following items were addressed:

**Policy (Certificate of Coverage) Forms and Underwriting Practices:**

A review was made of the Group's filed indemnity agreement and underwriting policies.

Formal application requirements for the trust were reviewed.

Regulatory Rate Exhibits which exhibit the "loss cost multiplier" are filed yearly with the TDCI in compliance with Tenn. Comp. R. & Regs. § 0780-01-54-.10(4).

No unusual findings were noted.

The Group offers deductibles for those members who wish to retain a small portion of their loss exposure. These plans and the corresponding premium analysis are filed with TDCI.

**Deductibles Offered**

- $250
- 500
- 1,000
- 1,500
- 2,500
The Group’s payment plans available to its members:

- Annual
- Two (2) equal installments
- Three (3) equal installments
- Four (4) equal installments
- Five (5) equal installments
- Six (6) equal installments
- Seven (7) equal installments
- Eight (8) equal installments
- Nine (9) equal installments
- Ten (10) equal installments
- 12.5% down and nine (9) equal payments
- 15% down and nine (9) equal payments
- 25% down and nine (9) equal payments

Advertising:

The Fund markets on a direct basis to the members of the Tennessee Forestry Association. The coverage is written by independent agents licensed in the state of Tennessee. The Administrator/Executive Director of the Group is also a licensed agent in Tennessee for property and casualty lines of insurance. The Administrator receives no commission from the production or renewal of business.

Tenn. Comp. R. & Regs. § 0780-01-54-.17 requires that “any person soliciting membership in a pool must be appropriately licensed as an insurance producer authorized to sell property and casualty lines of insurance.”


The advertising material reviewed appears to be in compliance with applicable statutes and regulations.

Claims Review:

A sample of paid and open claim files reviewed during the examination indicated that claims were being paid in accordance with policy (certificate of coverage) provisions and settlements were made properly upon receipt of proper evidence of the Group’s liability.

Tenn. Comp. R. & Regs. § 0800-02-14.07(1) requires: “All medical costs owed under the Tennessee Workers’ Compensation Law shall be paid within forty-five (45) days of receipt of bill or invoice.” The examiners tested a sample of the Trust’s claim payments and noted that the payments for medical costs were made within the required time.
Tenn. Comp. R. & Regs. § 0800-02-14.05(1) requires: “Compensation payments for an injury shall be received by the claimant no later that fifteen (15) days after notice of injury.” The examiners tested a sample of the Trust’s claim payments and noted that the payments for the indemnity portion of the claims sampled were made within the required time frame with the exception of one claim. The claim was reported 30 days after the injury by the employee and was initially denied due to findings of the initial treating physician. The initial treatment report indicated that the problem was not a direct result of the on the job injury. A second treating physician reversed the result and the employee requested a benefit review by the Department of Labor with the assistance of legal counsel which resulted in a favorable ruling for the employee. The Group paid the full 24 weeks of Temporary Total Disability and then settled the Permanent Disability through court proceedings. This does not appear to present a systemic problem based on the unusual circumstances of this claim.

If a claim is considered by a member to be relatively minor, the member sends the claim as “information only” to the Group’s third party administrator. Some of the members choose to pay up to the first $250 in “medical” expenses on small claims. If the bills exceed this small amount, the claim office (ERS) assumes handling of the claim which is then classified as active with a reserve worksheet being prepared.

The Group has an anti-fraud plan on file with the TDCI pursuant to Tenn. Code Ann. § 56-47-112(a).

**Policyholder Complaints:**

Inquiries made to the various sections within the Division of Insurance indicated no specific regulatory concerns with the Company during the period under examination. No unusual practices, transactions or items warranting significant concern with regard to the Group were noted.

**Privacy of Non-Public Personal Information**

The Fund’s members (policyholders) are commercial businesses. Tenn. Comp. R. & Regs. § 0780-01-72, “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.”

Employers Risk Services, Inc. processes the claims of the beneficiaries of the workers’ compensation policies issued by the Group to its members. The “Claims Service Contract” with the Group includes the following language:
"Each party will hold the Protected Information of the other in confidence using procedures no less stringent than those used with respect to its own confidential and proprietary information of a similar nature subject to the terms of this agreement."

The relationship of a beneficiary is addressed by Tenn. Comp. R. & Regs. § 0780-01-72-.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.

**EXCESS OF LOSS INSURANCE**

The Group had in effect for the period January 1, 2009 to December 31, 2009 an excess of loss agreement for workers compensation and employers liability claims with Midwest Employers Casualty Company in accordance with Tenn. Comp. R & Regs. § 0780-01-54-.04(3)(c). The agreement contains both specific and aggregate coverage.

Under the agreement's specific coverage, the excess insurer agrees to indemnify the Group for the amount in excess of the Group's $500,000 specific retention subject to a corridor deductible of $250,000 for losses over $500,000 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 Group's obligation for losses and claim expenses incurred during 2009 to a formula of (Payroll/100)*7.0571 which equates to a minimum retention of $6,810,398. Under the agreement's aggregate coverage, the excess insurer agrees to indemnify the Group for the sum of losses and claims expenses in excess of the Fund's limitation subject to a limit of indemnity of $2,000,000.

The Trust's excess of loss polices have historically covered the one (1) year period of time commencing January 1 for each year since 1995. The contracts have been with the same carrier with the exception of the 1997, 1998 and 1999 fund years and have had different retentions and levels of loss with the aggregate retention.
A summary of all companies providing coverage during the history of the Group follows:

<table>
<thead>
<tr>
<th>Fund Year</th>
<th>Specific Retention</th>
<th>Aggregate Retention</th>
<th>Basis for Aggregate</th>
<th>Insurer</th>
</tr>
</thead>
<tbody>
<tr>
<td>4/15/93-94</td>
<td>$250,000</td>
<td>$1,080,400</td>
<td>103% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>4/15/94-</td>
<td>250,000</td>
<td>1,848,300</td>
<td>105% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>12/31/94</td>
<td>250,000</td>
<td>2,689,700</td>
<td>105% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/95-96</td>
<td>250,000</td>
<td>3,925,900</td>
<td>110% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/96-97</td>
<td>250,000</td>
<td>3,772,079</td>
<td>93% of normal premium</td>
<td>Safety National</td>
</tr>
<tr>
<td>1/1/97-98</td>
<td>250,000</td>
<td>3,865,533</td>
<td>93% of normal premium</td>
<td>Safety National</td>
</tr>
<tr>
<td>1/1/98-99</td>
<td>250,000</td>
<td>3,721,500</td>
<td>82.284% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/00-01</td>
<td>350,000</td>
<td>3,961,200</td>
<td>88.9% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/01-02</td>
<td>500,000</td>
<td>5,430,500</td>
<td>96.5% of normal premium</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/02-03</td>
<td>500,000</td>
<td>6,454,000</td>
<td>(Payroll/100)*5.4771</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/03-04</td>
<td>500,000</td>
<td>7,162,088</td>
<td>(Payroll/100)*6.0555</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/04-05</td>
<td>500,000</td>
<td>7,829,918</td>
<td>(Payroll/100)*6.6709</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/05-06</td>
<td>500,000</td>
<td>8,723,036</td>
<td>(Payroll/100)*7.8931</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/06-07</td>
<td>500,000</td>
<td>10,720,000</td>
<td>(Payroll/100)*7.0260</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/07-08</td>
<td>500,000</td>
<td>9,542,355</td>
<td>(Payroll/100)*7.0571</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/08-09</td>
<td>500,000</td>
<td>8,820,398</td>
<td>(Payroll/100)*5.4771</td>
<td>Midwest Employers</td>
</tr>
</tbody>
</table>

*ALAE pro rata from 4/15/93 through 12/31/95. ALAE included in the Specific Retention from 1/1/96 to present. The specific maximum is set by statute.

**Corridor deductible of $250,000 for losses over $500,000 for policy periods 1/1/05 forward.
<table>
<thead>
<tr>
<th>Policy Year</th>
<th>Aggregate Limit</th>
<th>Insurer</th>
</tr>
</thead>
<tbody>
<tr>
<td>4/15/93-94</td>
<td>$2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>4/15/94-</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>12/31/94</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/95-96</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/96-97</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/97-98</td>
<td>2,000,000</td>
<td>Safety National</td>
</tr>
<tr>
<td>1/1/98-99</td>
<td>2,000,000</td>
<td>Safety National</td>
</tr>
<tr>
<td>1/1/99-00</td>
<td>2,000,000</td>
<td>Safety National</td>
</tr>
<tr>
<td>1/1/00-01</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/01-02</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/02-03</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/03-04</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/04-05</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/05-06</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/06-07</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/07-08</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/08-09</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
<tr>
<td>1/1/09-09</td>
<td>2,000,000</td>
<td>Midwest Employers</td>
</tr>
</tbody>
</table>

The policies provide coverage for losses sustained by the Group 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 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.

**RETIREMENT PLAN AND OTHER EMPLOYEE BENEFITS**

**SEP Plan**

The Group offers a Simplified Employee Pension Plan under section 408(k) of the Internal Revenue Code for eligible employees. Employees are covered after completing one year of employment. The maximum amount that an employer can contribute is determined by federal law.

Contributions are made to an Individual Retirement Account which is owned by the employee and administered by the Vanguard Group. Contributions are made at the discretion of the Board of Trustees on a yearly basis determined by the profitability and overall operation of the Group. No contributions were made for the 2009 year.

**Medical Insurance**

The Company offered medical insurance for the Administrator on a contributory basis through BlueCross BlueShield of Tennessee for the years 2005 through 2009. The
Administrator is additionally offered the opportunity of electing coverage for his or her spouse and/or dependents. BlueCross BlueShield is licensed in Tennessee as a “Tennessee Nonprofit Hospital and Medical Association.”

During 2010, the Group changed the provider for medical coverage to UnitedHealthcare Plan of the River Valley, Inc. The provider is licensed in Tennessee as a “Health Maintenance Organization.”

**LOSS EXPERIENCE**

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>2005</td>
<td>$8,269,343</td>
<td>$7,125,856</td>
<td>86.2%</td>
<td>2,476,335</td>
<td>29.9%</td>
<td>116.1%</td>
</tr>
<tr>
<td>2006</td>
<td>6,786,222</td>
<td>3,180,014</td>
<td>46.9%</td>
<td>2,350,968</td>
<td>34.6%</td>
<td>81.5%</td>
</tr>
<tr>
<td>2007</td>
<td>6,510,501</td>
<td>5,476,250</td>
<td>84.1%</td>
<td>2,233,653</td>
<td>34.3%</td>
<td>118.4%</td>
</tr>
<tr>
<td>2008</td>
<td>5,055,723</td>
<td>2,158,093</td>
<td>42.7%</td>
<td>2,275,121</td>
<td>45%</td>
<td>87.7%</td>
</tr>
<tr>
<td>2009</td>
<td>3,769,343</td>
<td>1,425,529</td>
<td>37.8%</td>
<td>1,573,994</td>
<td>41.8%</td>
<td>79.6%</td>
</tr>
</tbody>
</table>

The above comparison is based upon the numbers exhibited in the audited statement for each given year filed with the TDCI.

General and administrative expenses as stated above includes safety and loss control expense, and excess insurance premium.

General and administrative expenses do not include Return of Premium expensed in any given year.

**ACCOUNTS AND RECORDS**

During the course of examination, such tests and audit procedures were made as were considered necessary, including substantial verification of postings, extensions and footings and reconciliation of subsidiary ledgers to control accounts where necessary. General ledger trial balances were reconciled with copies of the Independent Auditors’ Financial Statements for the years 2005, 2006, 2007, 2008 and 2009 in order to verify the reasonableness of the financial presentation for the years since the prior examination.

Accounting records conform to generally accepted insurance accounting practices and appear to properly reflect the operations during the period under examination and the status of the Group at the date of examination.
An annual audit of the Group is performed by an independent accounting firm, Shores, Tagman, Butler & Company, P.A.

Books and records such as "Declaration of Trust and Bylaws," board minutes, membership files, accounting records and general correspondence of the Group are kept at the office location of the administrator which is also the office of the TFA:

2605 Elm Hill Pike, Suite G
Nashville, TN 37214

Claims records are kept at the office of Employers Risk Services, Inc. (Third Party Administrator) located at:

Post Office Box 628
1240 Fair Way Street
Bowling Green, KY 42102

Tennessee Location
109 Shingle Way, Suite 101
Franklin, TN 37067

The Group 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 Group is not exposed to any significant credit risk related to cash and cash equivalents.

**PECUNIARY INTEREST**

Tenn. Comp. R. & Regs. § 0780-01-54.07(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 interest in such purchase, sale, loan, either as borrower, principle, coprinciple, 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."
The Administrator certifies and documents that to the best of his knowledge and belief that the Group is in compliance with the rule.

**REFUNDS OR DISTRIBUTIONS**

Pursuant to Tenn. Comp. R. & Regs. § 0780-01-54.15, any monies in excess of the amount necessary to fund all obligations for that fund year may be declared to be refundable by the board of trustees not less than 18 months after the end of the fund year with the written approval of the Commissioner. If a refund is declared and approved by the Commissioner, 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 following table is a summary of the refunds approved by the TDCI and distributed by the Group categorized by fund year:

<table>
<thead>
<tr>
<th>Fund Year</th>
<th>Amount of Refund</th>
</tr>
</thead>
<tbody>
<tr>
<td>1995</td>
<td>$725,086</td>
</tr>
<tr>
<td>1996</td>
<td>673,158</td>
</tr>
<tr>
<td>1997</td>
<td>121,426</td>
</tr>
<tr>
<td>1998</td>
<td>46,360</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>$1,566,030</strong></td>
</tr>
</tbody>
</table>

No refunds have been approved or paid since the prior examination.

The approval history for the last refund which was the only refund during the previous examination period of December 31, 1999 to December 31, 2001 is categorized by calendar year as follows:

<table>
<thead>
<tr>
<th>Amount</th>
<th>Date of Approval by TDCI</th>
<th>Fund Years ending</th>
</tr>
</thead>
</table>

Disbursals are only made pursuant to the prior written approval granted by the TDCI. When the Board votes to approve a refund, it is always contingent upon the approval of the TDCI.

From April 8, 1986 up until the Rule was amended to become effective November 14, 2005, the time frame was not less than “12 months after the end of the fund year.”

The Group stated the following policy as a formal reply to the prior examination which addresses their blanket approval to declare all earnings of the Group as distributions/return of premiums back to the members of the Group.

“In order to maximize the assets of the Trust, we have designated the excess
monies earned by the Trust as Distributions payable. This in no means should
indicate that we intend to distribute these monies to the membership in the near
future. Along with the requirement of approval of the Department, we will monitor
the development of that surplus to ensure that the Trust will maintain adequate
reserves to cover any future or past liabilities.

This designation is to ensure that those monies earned by the members of the
Trust are not unduly taxed and thus reducing those earned monies and adding
stability to the fund. This has been reviewed by our Accountant and deemed
appropriate within acceptable accounting practices.

There was no formal declaration of a dividend noted in the minutes of the Board of
Trustees meetings during 2009. The last formal declaration was on March 2, 2005.

LITIGATION AND CONTINGENT LIABILITIES

As of December 31, 2009, the Group has committed no reserves to cover any
contingent liability. Various lawsuits against the Group have arisen in the normal course
of business relating to workers’ compensation claims’ settlements. Contingent liabilities
arising from such litigations which are known to exist are not considered to have a
material adverse affect on its financial examination as of the examination date.

SUBSEQUENT EVENTS

The Group and its custodian, PNC Bank, National Association, completed a new
custodian agreement during the course of the examination to ensure compliance with
the technical requirements of Tenn. Comp. R. & Regs. § 0780-01-46-.03(2)(a), which
became effective on July 12, 2005. The rule states:

"The custodial agreement required by this rule shall contain the following:

1. A provision stating that the standard of responsibility on the part of the custodian
   shall not be less than that of the responsibility of a bailee for hire or a fiduciary
   under statutory or case law of Tennessee;

2. A provision stating that the securities held by the custodian are subject to
   instructions of the insurance company;

3. A provision stating that the securities may be withdrawn immediately upon
   demand of the insurance company; and

4. A provision stating that the agreement is between the custodian and the
   insurance company, and not the parent or affiliate of the insurance company."
The new agreement signed by PNC Bank on October 5, 2010 and by the Group on October 4, 2010 exhibited language compliant with Tenn. Comp. R. & Regs. § 0780-01-46-03(2)(a).

As previously stated under the caption, Fidelity Bond and Other Insurance, The Group has added the Administrator as an insured to their professional liability policy in order to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.07(3)(b) and (c).

The Group made a filing with the TDCI dated November 2, 2010 of its current Application to Serve As Administrator of a Group Self Insurance Pool, Administrator Agreement, Excess Insurance Policy and amended Claims Administration and Loss Control Service Agreement pursuant to Tenn. Comp. R. & Regs. § 0780-1-54.05.
FINANCIAL STATEMENT

There follows a balance sheet and a statement of operations and fund balance as of December 31, 2009, together with a reconciliation of member deposits and distributions due to members for the period under review, as established by this examination:

**BALANCE SHEET**

<table>
<thead>
<tr>
<th>Assets</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Cash and cash equivalents</td>
<td>$523,561</td>
</tr>
<tr>
<td>Marketable debt securities (Munic. Bonds)</td>
<td>5,961,271</td>
</tr>
<tr>
<td>Premiums receivable (audit premium) net of allowance for uncollectible amounts of $83,094</td>
<td>140,189</td>
</tr>
<tr>
<td>Accrued interest receivable</td>
<td>62,316</td>
</tr>
<tr>
<td>Excess insurance recoverable on paid losses</td>
<td>25,316</td>
</tr>
<tr>
<td>Excess insurance recoverable on unpaid losses</td>
<td>442,950</td>
</tr>
<tr>
<td>Prepaid excess insurance premiums</td>
<td>38,474</td>
</tr>
<tr>
<td>Claims service fee payable/refund ERS</td>
<td>6,466</td>
</tr>
<tr>
<td>Loss control payable/refund ERS</td>
<td>18,744</td>
</tr>
<tr>
<td>Royalty fee payable/refund</td>
<td>10,361</td>
</tr>
<tr>
<td>Other assets (see detail below)</td>
<td>42,283</td>
</tr>
<tr>
<td>Deferred tax asset</td>
<td>799,178</td>
</tr>
<tr>
<td></td>
<td><strong>$8,071,109</strong></td>
</tr>
</tbody>
</table>

*Other assets detail*

| Property and equipment --at cost- net of accumulated depreciation of $74,148.49 | $3,977 |
| Prepaid Trustee liability insurance          | 12,956 |
| Deductibles receivable                       | 23,718 |
| Commissions payable or refundable            | 1,632  |
| Total other assets                           | **$42,283** |

The Group has invoiced ERS for the refundable amount resulting from the claims service fee and the loss control fee which are based upon premium volume.

The Group has invoiced Tennessee Forestry Association for the refundable amount for the royalty fee which is based upon premium volume.
**Liabilities and Members’ Surplus**  

<table>
<thead>
<tr>
<th>Liabilities</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loss and loss adjustment reserves</td>
<td>$3,630,504</td>
</tr>
<tr>
<td>Member distribution payable</td>
<td>3,331,295</td>
</tr>
<tr>
<td>Member overpayments</td>
<td>630,389</td>
</tr>
<tr>
<td>Accounts payable and other accrued liabilities (see detail below)</td>
<td>102,258</td>
</tr>
</tbody>
</table>

**Total liabilities**  
7,694,446

<table>
<thead>
<tr>
<th>Surplus/Members’ Surplus</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member equity (surplus)</td>
</tr>
<tr>
<td>Statutory surplus</td>
</tr>
</tbody>
</table>

**Total surplus**  
376,663

**Accounts payable and accrued liabilities**

<table>
<thead>
<tr>
<th></th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Premium tax payable</td>
<td>(93,966)</td>
</tr>
<tr>
<td>Accounts payable</td>
<td>(7,840)</td>
</tr>
<tr>
<td>Accounts payable claims</td>
<td>(452)</td>
</tr>
</tbody>
</table>

**Total accounts payable and accrued expenses (liability)**  
($102,258)
# STATEMENT OF INCOME

**Revenues**

- Premiums earned: $3,769,343
- Investment income: 205,778

**Total revenues**: 3,975,121

**Expenses**

- Losses and loss adjustment: 1,425,529
- Excess insurance premiums: 346,262
- Salary and payroll taxes: 135,772
- Commissions: 283,862
- Claims service fees (ERS): 263,476
- Royal fee expense: 37,639
- Premium taxes: 91,556
- Safety and loss control: 93,475
- Professional fees: 76,611
- Other administrative expenses: 245,341

**Total expenses**: 2,999,523

**Income before member distribution**: 975,598

**Member distribution**: (1,286,809)

**Deferred income tax benefit**: 311,211

**Net income**: $0
## STATEMENT OF CHANGES IN MEMBERS'S EQUITY

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total members' equity prior year</td>
<td>$2,049,238</td>
<td>$890,859</td>
<td>$1,945,530</td>
<td>$1,101,158</td>
<td>$2,501,767</td>
</tr>
<tr>
<td>Net income before taxes and return of premium to members</td>
<td>(1,088,452)</td>
<td>1,471,428</td>
<td>(909,021)</td>
<td>868,185</td>
<td>975,598</td>
</tr>
<tr>
<td>Return of premium paid to members</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Income tax benefit (expense)</td>
<td>52,571</td>
<td>(435,542)</td>
<td>0</td>
<td>487,967</td>
<td>311,211</td>
</tr>
<tr>
<td>Reduction in accrual of excess income as distributable to members</td>
<td>(122,498)</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Addition in accrual of excess income as distributable to members</td>
<td></td>
<td>18,785</td>
<td>64,649</td>
<td>44,457</td>
<td>75,492</td>
</tr>
<tr>
<td>(Reduction) in previously accrued member distribution resulting from examination</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>(156,110)</td>
</tr>
<tr>
<td>Total members equity, December 31</td>
<td>$890,859</td>
<td>$1,945,530</td>
<td>$1,101,158</td>
<td>$2,501,767</td>
<td>$3,707,958</td>
</tr>
</tbody>
</table>

### Detail by Year of Member Equity

<table>
<thead>
<tr>
<th></th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
</tr>
</thead>
<tbody>
<tr>
<td>Member distribution payable by year</td>
<td>$877,246</td>
<td>$1,931,917</td>
<td>$1,087,545</td>
<td>$2,488,154</td>
<td>$3,331,295</td>
</tr>
<tr>
<td>Member equity (surplus)</td>
<td>13,613</td>
<td>13,613</td>
<td>13,613</td>
<td>13,613</td>
<td>13,613</td>
</tr>
<tr>
<td>Statutory surplus</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>363,050</td>
</tr>
<tr>
<td>Total members equity, December 31</td>
<td>$890,859</td>
<td>$1,945,530</td>
<td>$1,101,158</td>
<td>$2,501,767</td>
<td>$3,707,958</td>
</tr>
</tbody>
</table>

The above reconciliation is prepared using the audited financial statements filed with the TDCI. Unrealized losses and unrealized gains to the bond portfolio as well as adjustments to loss reserves influence the addition in accrual to excess income as distributable to members.

The adjustments for the 2009 year relate to premium audits which were unavailable at
the time of preparation of the audited statement as well as the establishment of a statutory surplus as required by Tenn. Comp. R. & Regs. § 0780-1-54.11 which became effective March 16, 2009.

After the 2007 year which exhibited a net loss before taxes and return of premium to members, the Group did submit with the assistance of its CPA firm a plan to allocate profits from previous fund years. The TDCI then requested an allocation by member for each fund year be prepared. The Group has still not provided this requested information to the TDCI as of the date of this examination in the requested format. Both the CPA firm and actuary are continuing in the process of calculating this allocation. The Group has been profitable for the years following 2007.
ANALYSIS OF CHANGES IN FINANCIAL STATEMENT AND COMMENTS RESULTING FROM EXAMINATION

Item                                      Amount

Premiums receivable  
(audit premium) net of allowance for uncollectible amounts of $83,094  $ 140,189

The above amount reflects a reduction to the amount stated in the Audited Financial Statement, December 31, 2009 for this asset in the amount of $93,103.

For a self-insured workers' compensation pool, the premiums receivable are audit premiums after final payrolls are calculated. Some members may ask for a review of their audit after the cutoff date for the CPA Audit which in some cases may result in changes to the amount initially calculated. Testing consisted of reviewing the subsequent collection of the audit premiums through the end of May, 2010 which indicated collection of $140,189.

The adjustment is reasonable in part due to one member declaring bankruptcy which forgoes the collection of $36,808.60 in premium receivable. Another member asked for re-audit and it was determined that $67,978 in audit premium was not owed. These adjustments only became apparent after completion of the annual CPA audit.

Member overpayments  $ 630,389

The above amount reflects an increase to the amount stated in the Audited Financial Statement for this liability in the amount of $63,007.

Review and subsequent testing of the current member reimbursement run (seriatim by member) validates the amount currently calculated for the 2009 fund year in the amount of $630,389. The adjustments were the result of re-audits which were completed after the cutoff date of the CPA audit.

Statutory surplus  $ 363,050

The Group's Surplus is presented in the Audited Financial Statement under Member Distribution Payable. Tenn. Comp. R. & Regs. § 0780-1-54.11(1) requires:

"(1) A pool shall establish and maintain an aggregate surplus equal to:

(a) thirty percent (30%) of the unpaid claims liability of the pool. The pool may accumulate the surplus at a rate of ten percent (10%) per fund year over the next three (3) years. However, each pool shall have an aggregate surplus of thirty percent (30%) of the unpaid claims liability three (3) years from the effective date of this Chapter."
The required surplus for the Group is $363,050; therefore, the Group complies with the Rule.

The Group presents member distributions payable declared as operating expenses and deduct from total income prior to the calculation of net income or net loss for federal income tax purposes. The intent of this treatment is to designate the excess monies earned by the Fund as distributions payable back to its members.

The Member Distribution Payable to Members as represented on the GAAP financial statements of the Group represents retained earnings which have not been approved for payment to the members by the TDCI; however, these earnings are being treated as declared for payment under the accounting treatment approved by the Board of Trustees and recorded as a liability.

**Member distribution payable**

$3,331,295

The above amount is reflects a decrease of $519,160 from the amount stated in the Audited Financial Statement and results from the summation of the three (3) changes mentioned previously.

**SUMMARY SCHEDULE FOR “ANALYSIS OF CHANGES IN FINANCIAL STATEMENT AND COMMENTS RESULTING FROM EXAMINATION” AS THEY AFFECT MEMBER EQUITY (SURPLUS)**

<table>
<thead>
<tr>
<th>Item</th>
<th>Member Equity</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Increase</td>
</tr>
<tr>
<td>Premiums receivable</td>
<td>$93,103</td>
</tr>
<tr>
<td>Member overpayments</td>
<td></td>
</tr>
<tr>
<td>Statutory surplus</td>
<td></td>
</tr>
<tr>
<td>Member distribution payable</td>
<td>0</td>
</tr>
<tr>
<td>Totals</td>
<td>$363,050</td>
</tr>
<tr>
<td>Net change in member equity</td>
<td></td>
</tr>
</tbody>
</table>
COMMENTS AND RECOMMENDATIONS

Comments:

• The Trust effected a new custodial agreement with PNC Bank, National Association during the course of the examination to clarify some technical language pursuant to Tennessee Regulations. The agreement was discussed previously in the report under the caption “Subsequent Events.”

Recommendations:

• It is recommended that the Group put in place controls in order to monitor compliance with Tenn. Comp. R. & Regs. § 0780-01-54.05 pertaining to the filing of amendments to agreements and written contracts. This recommendation includes working with the TDCI in order to determine if a copy of the unsigned agreement can be filed no later than 30 days prior in order to meet the time line for effective date. Documents including amendments to the Claims Servicing Agreements were filed with the TDCI; however, the filing was not within the required time line.

Tenn. Comp. R. & Regs. § 0780-01-54.05 requires:

“Any amendments to the organizational documents or written contracts required to be provided to the Commissioner by Rule 0780-01-54-.04 shall be filed with the Commissioner with a non-refundable filing fee of ninety dollars ($90.00) no later than thirty (30) days prior to the proposed effective date of the amendments.”

• It is recommended that the Group comply with Tenn. Code Ann. §§ 66-29-113 and 66-29-115 in its handling of unclaimed property.

The Group is currently working on the filing of its annual report. There are no funds to be remitted at this time.

• It is recommended that the Group continue its efforts to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.15 which states that “any monies for a fund year in excess of the amount necessary to fund all obligations for that fund year may be declared refundable by the board of trustees not less that eighteen (18) months after the end of the fund year, after written approval is granted to the pool by the Commissioner to disburse such funds.”
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 Forestry Association Selective Workers' Compensation Group.

In such manner, it was determined that, as of December 31, 2009, the Group had assets of $8,071,109 and liabilities exclusive of member distribution payable of $4,363,151. Thus, there existed for the additional protection of the members of the Group/policyholders, the amount of $3,707,958 in the form of member distribution payable (retained earnings), member equity (surplus) and statutory surplus.

The courteous cooperation of the officers and employees of the Group extended during the course of the examination is hereby acknowledged.

Respectfully submitted,

Keith M. Patterson
Insurance Examiner
State of Tennessee
Southeastern Zone, N.A.I.C.
AFFIDAVIT

The undersigned deposes and says that he has duly executed the attached examination report of Tennessee Forestry Association Selective Workers' Compensation Group dated June 27, 2011, and made as of December 31, 2009, on behalf of the Department of Commerce and Insurance, state of Tennessee. 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.

Keith M. Patterson
Insurance Examiner
State of Tennessee
Southeastern Zone, N.A.I.C.

Subscribed and sworn to before me
this 27th day of
June, 2011

Notary
County
State
Commission Expires 8/20/2011
July 14, 2011

Dear Mr. Gaddis,

As the Executive Director of the Tennessee Forestry Association Selective Workers' Compensation Group, I would like to submit the following comments regarding the recommendations of the examination that was conducted for the years 2004-2009.

Before I address the recommendations included in the examination results, I would like to express my gratitude to you and Keith Patterson for the excellent management of the exam. During the audit Mr. Patterson was professional, knowledgeable, and respectful of our daily operations. I am very pleased that this examination went more efficiently than prior audits. The decorum afforded to our staff and me was a very positive reflection of the Tennessee Department of Commerce and Insurance.

Comments on Recommendations

From Page 35 of the Examination Report
(I will add my comments in blue)

- It is recommended that the Group put in place controls in order to monitor compliance with Tenn. Comp. R. & Regs. § 0780-01-54.05 pertaining to the filing of amendments to agreements and written contracts. This recommendation includes working with the
TDCI in order to determine if a copy of the unsigned agreement can be filed no later than 30 days prior in order to meet the time line for effective date. Documents including amendments to the Claims Servicing Agreements were filed with the TDCI; however, the filing was not within the required time line.

Tenn. Comp. R. & Regs. § 0780-01-54.05 requires:

"Any amendments to the organizational documents or written contracts required to be provided to the Commissioner by Rule 0780-01-54-.04 shall be filed with the Commissioner with a non-refundable filing fee of ninety dollars ($90.00) no later than thirty (30) days prior to the proposed effective date of the amendments."

- While I understand the intent of the rule, I must offer that it is difficult to provide details of agreements or service contracts to the Department thirty (30) days prior to the effective date. Having met difficulties with compliance to the rule in the past, we will endeavor to comply with the rule as written.

- It is recommended that the Group comply with Tenn. Code Ann. §§ 66-29-113 and 66-29-115 in its handling of unclaimed property.

  The Group is currently working on the filing of its annual report. There are no funds to be remitted at this time.

- With the assistance of our internal Accountant (Donna Swann, CPA) we are working diligently to identify any funds that will need to be reported to the State of Tennessee. While we do not have any unclaimed property to report at this time, it is possible that there are funds that are not yet due to be escheated to the State of Tennessee. We understand that we are required to file an unclaimed property report annually even if there are no funds that will be returned to the State. We will submit an annual report in order to comply with the rule as recommended.

- It is recommended that the Group continue its efforts to comply with Tenn. Comp. R. & Regs. § 0780-01-54-.15 which states that "any monies for a fund year in excess of the amount necessary to fund all obligations for that fund year may be declared refundable by the board of trustees not less that eighteen (18) months after the end of the fund year, after written approval is granted to the pool by the Commissioner to disburse such funds."
• We will work with Shores, Tagman, Butler, and Company, P.A. in order to continue our current efforts to comply with the rule as recommended.

Please do not hesitate to contact me should you have any questions or concerns, you may reach me at (615)883-3832.

Respectfully,

[Signature]

Mike Whitley
Executive Director
Tennessee Forestry Association
Selective Workers' Compensation Group