EXAMINATION REPORT
of
VIRGINIA COMMERCE GROUP SELF-INSURANCE ASSOCIATION
RICHMOND, VIRGINIA
as of
DECEMBER 31, 2008

COMMONWEALTH OF VIRGINIA
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE

COMMONWEALTH OF VIRGINIA

ALFRED W. GROSS
COMMISSIONER OF INSURANCE
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE

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I, Alfred W. Gross, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Virginia Commerce Group Self-Insurance Association as of December 31, 2008, is a true copy of the original report on file with this Bureau.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed to the original the seal of the Bureau at the City of Richmond, Virginia this 8th day of October, 2009

Alfred W. Gross

Alfred W. Gross
Commissioner of Insurance

(SEAL)

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Richmond, Virginia
July 9, 2009

Honorable Alfred W. Gross
Commissioner of Insurance
Richmond, Virginia

Dear Sir:

Pursuant to your instructions and by authority of Section 38.2-1317 of the Code of Virginia, an examination of the records and affairs of:

VIRGINIA COMMERCE
GROUP SELF-INSURANCE ASSOCIATION

Richmond, Virginia

hereinafter referred to as the Association, has been completed. The report is hereby submitted for your consideration.

DESCRIPTION

The Association is a group self-insurance association licensed to provide workers' compensation coverage and employers' liability coverage to its members pursuant to Section 65.2-802 of the Code of Virginia and 14 VAC 5-370-10 et seq. (Rules Governing Group Self-Insurers of Liability Under the Virginia Workers' Compensation Act) promulgated by the State Corporation Commission (the "Commission").

The Association was last examined by representatives of the Commission's Bureau of Insurance (the "Bureau") as of December 31, 2005. This examination covers the period from January 1, 2006 through December 31, 2008.

HISTORY

The Virginia Retail Merchants Group Self-Insurance Association was licensed by the Bureau on January 1, 1982. In 1989, the Virginia Retail Merchants Group Self-Insurance Association changed its name to the Virginia Commerce Group Self-Insurance Association. On July 1, 1990, the Bureau revised the Association's license to authorize employers' liability coverage. According to the members indemnity agreement, the Association was formed to allow members to join together to provide for joint and cooperative action to self-insure and to pool their separate liabilities arising pursuant to the terms of the Virginia Workers' Compensation Act.

MANAGEMENT AND CONTROL

Control of the Association is vested in a Members' Supervisory Board (the "Board") elected by the members of the Association. The bylaws provide for no less than three nor more than nine Board members, all of whom shall be members of the Association in good standing. Each Board member shall serve a term of three years or until the members elect a successor.

The Board and officers were as follows at December 31, 2008:

Representative	Member
James A. Branscome	Freeman Beverage Company, Inc. Falmouth, Virginia
Robert E. Burgess, Jr.	Callao Supermarket Callao, Virginia
Angelo F. Castanes	Sonny Merryman Richmond, Virginia
Jonathan E. Phares	The Commonwealth Club Richmond, Virginia
Steven G. Sodikoff	Steven Toyota Norfolk, Virginia
Robert W. N. Smith	Owen Printing Company Petersburg, Virginia

Officers

Robert W. N. Smith	Chairman
Jonathan E. Phares	Vice Chairman
Robert E. Burgess, Jr.	Secretary/Treasurer

TERRITORY AND PLAN OF OPERATION

The operation of the Association is confined to Virginia where it is licensed to transact the business of workers' compensation and employers' liability group self-insurance. Membership in the Association is available to applicants engaged in a similar type of business upon the approval of the Board, the Bureau and the Safety National Casualty Corporation, the Association's excess insurance carrier.

All members are required to enter into an indemnity agreement in which each member jointly and severally agrees to assume and discharge members' employers' liabilities and any and all members' liabilities covered under the Virginia Workers' Compensation Act. No formal insurance policy is issued to the members.

The Association has a contractual agreement with an administrator who shall administer and manage the affairs of the Association in accordance with the policies adopted and established by the Board. The administrator also functions as the claims service agent. The Association's operations are conducted on a calendar year basis.

ADMINISTRATIVE AND OTHER SERVICES AGREEMENT

Effective January 1, 2002, the Association entered into an administrative and other services agreement with Landin, Inc. ("Landin"). This agreement is effective for a period of one year and will automatically renew for additional one-year terms. Either party may elect to non-renew or renegotiate any portion of this agreement with 60 days prior written notice. According to the agreement, Landin is responsible for, but not limited to, the following:

- Advising the Board on policy matters and insuring that the provisions of the Board's contracts for services are met;
- Establishing and maintaining a set of books;
- Billing and collecting all sums due the Association;
- Contracting for the annual member payroll audits;
- Paying all items of expense in accordance with the policies of the Board;
- Investing the Association's fund surpluses as directed by the Board and properly accounting for all funds of the Association to the Board;

- Providing complete loss control services, which shall include conducting loss control evaluations of members, preparing and monitoring computer loss runs and furnishing complete claims handling services and administration for all workers' compensation claims and employers' liability claims to their conclusion.

As compensation for its services, Landin shall receive 10% of the net audited premiums collected. Total administrative and other service fees incurred for fiscal year 2008 were $613,409. Additionally, Landin coordinates with Genex Services Inc., ("Genex") an outside claims review service company, for the review and completion of inpatient bill audits, the inpatient utilization review process and identifying any reductions from the application of any provider contracted allowances, fee schedules and negotiations generated from the cost containment program. Genex shall receive up to 25% of the savings generated by performing this service and such payments are made directly to Genex from the Association.

MARKETING AGREEMENT

Effective February 28, 2001, the Association entered into a marketing agreement with Landin. The agreement was amended effective January 1, 2007 and gives Landin the exclusive right to solicit participation and membership in the Association, including the right to subcontract with other licensed insurance agents and/or firms for a term of ten years. The agreement is thereafter renewable every five years. The agreement reflects the following commission schedule:

Premium Volume	Commission
$0 to $100,000	11% of all net audited premium
$100,001 to $250,000	12% of all net audited premium
$250,001 and above	13% of all net audited premium

As a production incentive, the Association shall also pay Landin a 2% commission for new business of $50,000 or more for the year that the new business is produced. The production incentive will be based on audited annualized premium and paid on net audited premium for that year.

Either party may terminate this agreement by providing 90 days written notice prior to the effective date of termination. Total marketing costs incurred for fiscal year 2008 were $725,442.

DIVIDENDS TO MEMBERS

Any surplus assets accumulated within a fiscal year may be declared refundable by the Board. Payment of this surplus in the form of dividends, however, may not be made until the Association has received approval from the Bureau. During the examination period, the Bureau approved the following dividends:

	Approval Dates		
Fiscal Year	September 8, 2006	September 19, 2007	September 10, 2008
1985	$108		
1987		$3,249	
1990	11,000	9,081	$2,846
1991	14,000	19,497	5,438
1992		26,483	8,957
1993	31,000	48,010	6,443
1994	36,000	50,000	3,798
1995	50,000	88,529	37,239
1996	66,000	60,000	80,000
1997	46,000		
1998	68,000	40,000	40,000
1999	88,000	60,000	30,000
2001	140,000	170,000	160,000
2003			13,464
2004	100,000	130,000	140,000
2005		130,000	140,000
2006		200,000	400,000
2007			70,000
Totals	$650,108*	$1,034,849**	$1,138,185***

*The dividend was subject to the condition that $150,108 of the approved amount be used to offset the 2002 fiscal year deficit and $500,000 be disbursed to the membership.

**The dividend was subject to the condition that $534,849 of the approved amount be used to offset the 2002 fiscal year deficit and $500,000 be disbursed to the membership.

***The dividend was subject to the condition that $138,185 of the approved amount be used to offset the 2002 fiscal year deficit and funding of the Board Discretionary Fund and $1,000,000 be disbursed to the membership.

FIDELITY BOND COVERAGE

At December 31, 2008, the Association was listed as a named insured on a fidelity bond with a $250,000 limit of liability, to insure against losses arising from dishonest acts of its administrator and employees.

SPECIAL RESERVES AND DEPOSITS

At December 31, 2008, the Association had a United States Treasury Note with a par value of $250,000 on deposit with the Treasurer of Virginia as required by 14 VAC 5-370-60 A.

EXCESS INSURANCE COVERAGE

The Association had both specific excess and aggregate excess insurance agreements in force at December 31, 2008, with the following limits:

	Association's Retention	Excess Insurer's Limits
Specific Excess	$500,000	Workers' Compensation Statutory Employers' Liability $1,000,000
Aggregate Excess	100% of total standard premium, subject to a minimum retention of $5,879,363	$5,000,000

SCOPE

This is a full scope financial condition examination initiated and conducted under the provisions of Article 4, Chapter 13 of Title 38.2 of the Code of Virginia. It covers the period January 1, 2006 through December 31, 2008. Assets were verified and liabilities were established at December 31, 2008. A review of income and disbursements for the period was made to the extent deemed necessary.

The items comprising the Balance Sheet had a medium or low risk assessment as determined from the principles of the risk-based examination approach contained in the NAIC Financial Condition Examiners Handbook. Analytical review procedures were applied to non-material items.

In addition, the following matters were reviewed, several of which are discussed separately under their respective captions in the report:

History
Management and Control
Territory and Plan of Operation
Administrative and Other Services Agreement
Marketing Agreement
Dividends to Members
Fidelity Bond Coverage
Special Reserves and Deposits
Excess Insurance Coverage
Financial Statements

FINANCIAL STATEMENTS

There follows a statement reflecting the financial condition of the Association at December 31, 2008, a statement of income for the year ended December 31, 2008, a reconciliation of members' equity for the period under review, a statement of members' account by fiscal year inception to date and a statement of Examiners' changes in members' equity.

BALANCE SHEET
DECEMBER 31, 2008

ASSETS

Bonds, short-term	$1,203,255
Bonds, long-term	9,614,964
Other invested assets	1,060,693
Cash on deposit	90,447
Premiums receivable	413,582
Interest due and accrued	112,232
Amounts recoverable on paid losses	95,928
Income tax receivable	958,144
Prepaid marketing fees	115,705
Prepaid service agent's fees	50,788
Prepaid administrative fees	41,566
Excess insurance premium receivable	10,246
Total assets	$13,767,550

LIABILITIES AND MEMBERS' EQUITY

Losses unpaid	$7,040,341
Loss adjustment expenses unpaid	307,830
Contingency reserve	1,145,611
Unearned premiums	1,120,247
Premium refunds payable	352,002
Taxes, licenses and fees payable	173,988
Other expenses payable	611
Professional fees payable	55,000
Investment fees payable	1,650
Marketing fees payable	8,072
Total liabilities	$10,205,352
Restricted members' equity	302,469
Unrestricted members' equity	3,259,729
Total liabilities and members' equity	$13,767,550

STATEMENT OF INCOME
FOR YEAR ENDED DECEMBER 31, 2008

UNDERWRITING INCOME

Premiums earned	$5,731,848
Deductions:	
Losses incurred	$4,629,414
Loss expenses incurred	141,494
Other underwriting expenses incurred	1,614,287
Contingency reserve	25,735
Total underwriting deductions	$6,410,930
Net underwriting loss	($679,082)

INVESTMENT INCOME

Net investment income earned	$601,380
Net realized capital gains	234,805
Net investment gain	$836,185

OTHER INCOME

Late fees	$7,100
Dividends applied to deficit fund years and board discretionary fund	138,185
Total other income	$145,285
Net income before federal income taxes incurred	$302,388
Federal income taxes incurred	(201,825)
Net income	$504,213

RECONCILIATION OF MEMBERS' EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2008

		2006	2007	2008
Members' equity, previous year	*	$1,866,158	$3,300,012	$4,679,536
Adjustment for previous examination changes		(115,347)		
Net income		2,059,449	2,148,081	504,213
Net unrealized capital gains or (losses)		139,860	266,292	(483,366)
Dividends paid to members		(650,108)	(1,034,849)	(1,138,185)
Restricted and unrestricted members' equity, end of year		$3,300,012	$4,679,536	$3,562,198
Less: Restricted members' equity, end of year		260,016	271,421	302,469
Unrestricted members' equity, end of year		$3,039,996	$4,408,115	$3,259,729

* Adjusted members' equity from previous examination.

Members' Account By Fiscal Year Inception to Date December 31, 2008

	All Other Fiscal Years Preceding 1982-2004	Third Fiscal Year Preceding 2005	Second Fiscal Year Preceding 2006	First Fiscal Year Preceding 2007	Current Fiscal Year 2008	Total Inception to Date (1982-2008)
Income Received						
Premiums written	$75,818,272	$7,466,595	$7,988,026	$7,276,913	$7,192,323	$105,742,129
Less: Excess insurance	5,788,988	552,536	594,094	507,830	473,541	7,916,989
Net premiums written	$70,029,284	$6,914,059	$7,393,932	$6,769,083	$6,718,782	$97,825,140
Investment income	6,753,489	259,457	288,847	131,261	846,140	8,279,194
Allocation between years	189,758	99,251	174,888	254,131	(718,028)	0
Other	869,346	16,406	18,531	13,631	(201,981)	715,933
Total income collected	$77,841,877	$7,289,173	$7,876,198	$7,168,106	$6,644,913	$106,820,267
Less: Expenses Paid						
Losses paid	$40,127,138	$3,366,829	$2,473,089	$2,458,869	$1,180,632	$49,606,557
Allocated loss adjustment expenses paid	1,335,356	217,640	177,807	143,704	35,025	1,909,532
Administrative fees	3,060,885	335,997	359,461	327,461	317,600	4,401,404
Service agent's fees	4,491,573	410,663	439,341	400,230	388,179	6,129,986
Taxes, licenses, and fees	1,130,876	104,213	149,122	143,374	360	1,527,945
Federal income tax	1,528,418	97,195	312,373	209,113	756,319	2,903,418
Other expenses	9,930,607	985,151	1,051,732	977,296	871,180	13,815,966
Total expenses	$61,604,853	$5,517,688	$4,962,925	$4,660,047	$3,549,295	$80,294,808
Net cash income	$16,237,024	$1,771,485	$2,913,273	$2,508,059	$3,095,618	$26,525,459
Add: Receivables						
Premiums receivable	$0	$0	$0	$0	$413,582	$413,582
Interest due and accrued	25,038	13,185	23,232	33,759	17,018	112,232
Amounts recoverable on paid losses	95,928	0	0	0	0	95,928
Other	0	568	84,269	116,988	974,624	1,176,449
Total	$120,966	$13,753	$107,501	$150,747	$1,405,224	$1,798,191
Deduct: Liabilities						
Losses unpaid	$911,813	$644,663	$746,588	$1,687,925	$3,049,352	$7,040,341
Loss adjustment expenses	41,507	15,860	40,832	89,347	120,284	307,830
Contingency reserve	279,643	223,997	239,641	218,307	184,023	1,145,611
Unearned premiums	0	0	0	0	1,120,247	1,120,247
Premium refunds payable	0	0	0	0	352,002	352,002
Taxes, licenses and fees payable	0	0	0	0	173,988	173,988
Other expenses payable	0	0	0	0	65,333	65,333
Total	$1,232,963	$884,520	$1,027,061	$1,995,579	$5,065,229	$10,205,352

Members' Account By Fiscal Year Inception to Date December 31, 2008

	All Other Fiscal Years Preceding 1982-2004	Third Fiscal Year Preceding 2005	Second Fiscal Year Preceding 2006	First Fiscal Year Preceding 2007	Current Fiscal Year 2008	Total Inception to Date (1982-2008)
Restricted and Unrestricted Members' Equity to date by fiscal year before dividends	$15,125,027	$900,718	$1,993,713	$663,227	($564,387)	$18,118,298
Less: Dividends paid inception to date by fiscal year	13,616,100	270,000	600,000	70,000	0	14,556,100
Less: Restricted Members' Equity by fiscal year	55,915	55,915	55,915	55,916	55,915	279,576
Less: Board Discretionary Fund	0	7,631	7,631	7,631	0	22,893
Unrestricted Members' Equity 12/31/08	$1,453,012	$567,172	$1,330,167	$529,680	($620,302)	$3,259,729

STATEMENT OF EXAMINERS' CHANGES IN MEMBERS' EQUITY
DECEMBER 31, 2008

	Amount Per Association	Amount Per Examiner	Increase (Decrease) Members' Equity
Assets:			
Premiums receivable	$1,685	$413,582	$411,897
Prepaid service agent's fees	54,122	50,788	(3,334)
Prepaid administrative fees	44,281	41,566	(2,715)
Excess insurance premium receivable	14,771	10,246	(4,525)
Liabilities:			
Loss adjustment expenses unpaid	$237,383	$307,830	($70,447)
Contingency reserve	1,143,801	1,145,611	(1,810)
Premium refunds payable	0	352,002	(352,002)
Taxes, licenses and fees payable	142,061	173,988	(31,927)
Marketing fees payable	132	8,072	(7,940)
Examiners' changes in members' equity			($62,803)
Restricted and unrestricted members' equity per Association			$3,625,001
Restricted and unrestricted members' equity per Examiners			3,562,198
Decrease in unrestricted members' equity			($62,803)

RECOMMENDATIONS FOR CORRECTIVE ACTION

Management and Control

1. The results of this examination reflect an unrestricted members' equity deficit for the 1989, 1994, 1997 and 2008 fiscal years of $25,054, $17,701, $12,279 and $620,302, respectively.

The Board is reminded of its responsibility to assure that the Association is financially sound and able to fulfill its obligations under the Virginia Workers' Compensation Act. The Board must recognize the Association's financial condition and take necessary steps, which may include assessments, to eliminate all deficits.

Accounts and Records

2. Premiums receivable	$413,582
Premium refunds payable	$352,002

The above amounts have been increased $411,897 and $352,002, respectively. The Examiners' amounts are based on a review of the subsequent 2008 payroll audits and reflect differences between audited contributions and contributions paid at December 31, 2008.

3. Prepaid administrative fees	$41,566
Prepaid service agent's fees	$50,788

The above amounts are $2,715 and $3,334 less, respectively, than reported by the Association in its 2008 Annual Statement. The decreases are attributed to higher earned premiums developed from subsequent 2008 payroll audits, which are the basis for computing fees due to the Association's administrator/service agent.

4. Excess insurance premium receivable	$10,246

The above asset is $4,525 less than the amount reported by the Association in its 2008 Annual Statement. The Examiners' amount reflects the difference between the Association's excess insurance premiums paid in 2008 and premiums owed developed from subsequent 2008 payroll audits, which is the basis for computing excess insurance premiums.

5. Loss adjustment expenses unpaid $307,830

The above liability is $70,447 more than the amount reported by the Association in its 2008 Annual Statement. The increase in Loss adjustment expenses unpaid by fiscal year is as follows:

Fiscal Year	Association	Examiners	Increase
2003	$ 0	$ 10,999	$ 10,999
2005	7,171	15,860	8,689
2006	12,441	40,832	28,391
2007	66,979	89,347	22,368
Total change			$ 70,447

The Examiner's increase results from a development of loss adjustment expenses paid and reserve changes occurring during the period January 1 through June 30, 2009, on claims incurred December 31, 2008 and prior. The Association should review its methodologies to ensure sufficient loss adjustment expense reserves are established in all future filings with the Bureau.

6. Contingency reserve $1,145,611

The above liability is $1,810 more than the amount reported by the Association in its 2008 Annual Statement. The Examiners' change is a result of an increase in earned premium based on a review of subsequent 2008 payroll audits, which is the basis for the calculation of the contingency reserve.

7. Taxes, licenses, and fees payable $173,988

The above liability is $31,927 more than the amount reported by the Association in its 2008 Annual Statement. The Examiners' amount was based on a review of invoices paid in 2009 for taxes pertaining to 2008.

8. Marketing fees payable $8,072

The above liability is $7,940 more than the amount reported by the Association in its 2008 Annual Statement. The Examiners' change is a result of an increase in earned premium based on a review of subsequent 2008 payroll audits, which is the basis for the calculation of marketing fees.

CONCLUSION

The courteous cooperation extended by the Association's administrator and service agent during the course of the examination is gratefully acknowledged.

In addition to the undersigned, George E. Morgan, CFE participated in the work of the examination.

Respectfully submitted,

Darrin P. Bailey, Sr., CFE, MHP
Senior Insurance Examiner

VCGSIA
VIRGINIA COMMERCE GROUP
SELF-INSURANCE ASSOCIATION

STATE CORP COMMISSION
BUREAU OF INSURANCE
09 OCT -5 AM 9:15

September 24, 2009

Mr. David H. Smith, CFE, CPA, CPCU
Chief Examiner
State Corporation Commission
Bureau of Insurance
P. O. Box 1157
Richmond, VA 23218

Dear Mr. Smith:

This is in response to your September 4, 2009, letter regarding the Virginia Commerce Group Self-Insurance Association's Examination Report as of December 31, 2008. We take no issue with any matter contained in the examination report. Regarding the recommendations for corrective action, we respond as follows:

Management and Control

1. As mentioned in our August 7, 2009, letter to Janis Bunce, we have requested permission to apply the excess contingency reserve to the 1989, 1994, and 1997 fund years to eliminate the deficits in those years. In a letter dated September 17, 2009, Janis Bunce indicated there was $219,558 in excess contingency reserves available that could be applied to these fund year deficits.

   We will continue to monitor the 2008 fund year deficit and reevaluate upon the filing of the 2009 annual statement due to the following:

   - Investment earnings in 2009 and future years will be allocated based on the allocation formula. Thus, 2008 will continue to earn investment income during 2009 and beyond.

   - The deficit includes IBNR, contingency reserve and restricted equity of over $2.3 million, which taken together exceed the deficit in the 2008 fund year.

   Based on the above, we believe the deficit is manageable and does not jeopardize the long-term financial integrity of the VCGSIA.

2. Premiums Receivable and Premium Refunds Payable – The increase in premiums receivable and premium refunds payable are due to differences between audited premiums and premiums received as of December 31, 2008.

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Administrator and Service Company · The Landin Companies · info@landininc.com

3. Prepaid Administrative Fees and Prepaid Service Agent's Fees – The differences can be attributed to higher earned premiums developed from subsequent payroll audits, which are the basis for computing fees due to the Administrator and Service Agent.

4. Excess Insurance Premium Receivable – The change can be attributed to the difference between premiums paid in 2008 and premiums owed developed from subsequent 2008 payroll audits, which is the basis for computing excess insurance premiums.

5. Loss Adjustment Expenses Unpaid – All open VCGSIA claims are reviewed on a regular basis by Management. The timeframe for the management review is 30 to 120 days depending on the issues involved in each claim. Reserve adequacy is included in this review process. Landin strives to have its best estimate of a reserve on claims before they are six months old.

   Regarding the loss adjustment expense noted in the examination report, the changes are the result of new litigation stemming from claims in which Landin is questioning the causation of current treatment/injuries to the original claim. This has necessitated either a file reopening or re-assessment of the expense cost of the claim.

6. Contingency Reserve – The difference can be attributed to an increase in earned premiums developed from subsequent payroll audits, which is the basis for the calculation of the contingency reserve.

7. Taxes, Licenses, and Fees Payable – The difference can be attributed to an increase in the liability for taxes pertaining to 2008, which is a result of the workers' compensation payroll tax assessment that was paid in 2009.

8. Marketing Fees Payable – The difference can be attributed to higher earned premiums developed from subsequent payroll audits, which is the basis for computing marketing fees.

I hope our responses are satisfactory. Should you have any questions or need any additional information, please do not hesitate in contacting us. Please provide 15 copies of the report. Thank you.

Sincerely,

J Phares

Jonathan Phares, Chairman
Members' Supervisory Board