

EXAMINATION REPORT
of
VIRGINIA FORESTRY SAFETY
GROUP SELF-INSURANCE ASSOCIATION
RICHMOND, VIRGINIA
as of
DECEMBER 31, 2010

COMMONWEALTH OF VIRGINIA

JACQUELINE K. CUNNINGHAM
COMMISSIONER OF INSURANCE
STATE CORPORATION COMMISSION
BUREAU OF INSURANCE



P.O. BOX 1157
RICHMOND, VIRGINIA 23218
TELEPHONE: (804) 371-9741
TDD/VOICE: (804) 371-9206
<http://www.scc.virginia.gov/division/boi>

I, Jacqueline K. Cunningham, Commissioner of Insurance of the Commonwealth of Virginia, do hereby certify that the annexed copy of the Examination Report of Virginia Forestry Safety Group Self-Insurance Association as of December 31, 2010, 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 23rd day of March, 2012

A handwritten signature in cursive script that reads 'Jacqueline K. Cunningham'.

Jacqueline K. Cunningham
Commissioner of Insurance

(SEAL)

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Richmond, Virginia
January 6, 2012

Honorable Jacqueline K. Cunningham
Commissioner of Insurance
Richmond, Virginia

Dear Madam:

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 FORESTRY SAFETY
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, 2007. This examination covers the period from January 1, 2008 through December 31, 2010.

HISTORY

The Association was licensed by the Bureau effective January 1, 1995. According to its indemnity agreement, the Association was formed to allow members to self-insure and to pool their separate liabilities arising pursuant to the terms of the Virginia Workers' Compensation Act and for certain other types of employers' liabilities.

MANAGEMENT AND CONTROL

Control of the Association is vested in a Members' Supervisory Board (the "Board") elected by the members of the Association. The by-laws provide for no less than three nor more than eleven board members, three-fourths of whom shall be officers of members in good standing of the Association. Board members serve until their successors are elected.

The Board and officers were as follows at December 31, 2010:

<u>Representative</u>	<u>Member</u>
Kerry L. Clary	Aubrey L. Clary, Inc. Gasburg, Virginia
Sigmund R. Jones	S. R. Jones, Jr. and Sons, Inc. Gasburg, Virginia
Franklin B. Myers	M. M. Wright, Inc. Gasburg, Virginia
Jerry D. Rose	Jerry D. Rose, Inc. Courtland, Virginia
Ronald E. Wright	Ronald E. Wright Logging, Inc. Ebony, Virginia

Officers

Chairman	Jerry D. Rose
Vice Chairman	Franklin B. Myers
Secretary / Treasurer	Ronald E. Wright

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 employers engaged in a similar type of business, upon the approval of the Board and the Commission.

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 members' liabilities under the Virginia Workers' Compensation Act. No formal insurance policy is issued to the members.

An administrator is responsible for assisting the board in managing the affairs of the Association. Claims are processed and paid by a service agent under a contractual agreement with the Association. The Association's operations are conducted on a calendar year basis.

ADMINISTRATIVE AGREEMENT

Effective January 1, 1996, the Association entered into an administrative agreement with Self-Insurance Services, LLC, ("SIS"). The original term of this agreement was for a period of 12 months and the agreement continued thereafter subject to termination by either party by 90 days advance written notice.

According to the agreement, SIS shall administer the financial affairs of the Association as established and adopted by the Board, maintain necessary records of accounts, advise the Board on policy matters, contract for claims handling, pay all items of expense to the extent funds are available, direct the solicitation and enrollment of new members, file necessary reports, and conduct other managerial duties.

As compensation for its services, SIS shall receive the sum of 13% of all members' contributions paid to the Association, adjusted for final payroll audits. In addition, SIS retains 100% of the commission received for placement of excess insurance coverage. The Association incurred \$175,521 in fees relating to this agreement in calendar year 2010.

CLAIMS SERVICE AGREEMENT

Effective January 1, 2000, the Association entered into a claims service agreement with PMA Management Corporation ("PMA"). The original term of this agreement was for a period of 12 months and the agreement shall remain in full force and effect unless otherwise amended or terminated.

Under the terms of the agreement, the services provided by PMA include full claims handling and adjusting for all claims incurred during the period of the agreement until their conclusion, unless otherwise transferred; assisting the Association in the selection of outside vendors when necessary to professionally defend a claim; and notifying excess insurers of all qualified claims which may exceed the Association's retention.

Effective with an amendment dated January 1, 2010, PMA shall receive an annual fee of \$26,000, payable in quarterly installments, as compensation for its claims services. For managed care services, PMA receives \$95 per hour for medical case management services and for disability management coordinators. For cost containment services, the Association pays \$8.25 per bill reviewed and PMA receives 35% of the savings generated. For risk control services at the Association's request, PMA receives \$125 per hour.

In addition, the Association pays PMA an annual administrative service fee of \$4,500 to cover the costs of basic administrative services and fees, which may include, but not limited to, account setup, account maintenance, incurred banking fees, monthly loss analysis and monthly claim reconciliation. Finally, the Association pays an annual fee of \$3,500 to access PMA's Internet-based claims information system. The Association incurred \$42,503 in fees relating to this agreement in calendar year 2010.

DIVIDENDS TO MEMBERS

Any surplus assets accumulated within a plan 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:

DIVIDENDS TO MEMBERS

Any surplus assets accumulated within a plan 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

<u>Fiscal Year</u>	<u>September 16, 2008</u>	<u>October 2, 2009</u>	<u>October 8, 2010</u>
1995	\$ 3,584		
1996	11,839	\$ 3,407	
1997	10,000	20,000	\$ 36,832
1998	10,000	10,000	41,494
2000	25,000	25,000	30,000
2001	50,000	100,000	75,000
2002	100,000	100,000	50,000
2003	50,000	50,000	10,000
2004	100,000	100,000	50,000
2005	100,000	200,000	200,000
2006	50,000	50,000	100,000
2007			100,000
2008		<u>100,000</u>	<u>200,000</u>
Totals	<u>\$ 510,423</u>	<u>\$ 758,407</u>	<u>\$ 893,326</u>

FIDELITY BOND COVERAGE

At December 31, 2010, the Association was listed as a named insured on a fidelity bond with a \$100,000 limit of liability, subject to a \$5,000 deductible, to insure against losses arising from dishonest acts of its administrator and employees.

SPECIAL RESERVES AND DEPOSITS

At December 31, 2010, the Association had United States Treasury Notes with a par value of \$300,000 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, 2010, with the following limits:

	<u>Association's Retention</u>	<u>Excess Insurer's Limits</u>
Specific Excess	\$500,000 maximum for each accident and each employee for disease	Workers' Compensation Statutory Employers' Liability \$1,000,000
Aggregate Excess	100% of billed premium subject to a minimum retention of \$1,310,461	\$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. The examination covers the period January 1, 2008 through December 31, 2010. Assets were verified and liabilities were established at December 31, 2010. 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 Agreement
Claims Service 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, 2010, a statement of income for the year ended December 31, 2010, 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, 2010

ASSETS

Bonds, long term	\$3,957,682
Other invested assets	145,519
Cash on deposit	83,127
Deposit with service agent	71,746
Premiums receivable	113,456
Interest due and accrued	37,206
Amounts recoverable on paid losses	16,124
Income taxes receivable	606,329
Prepaid administrative fees	1,508
Prepaid excess insurance premiums	3,290
Prepaid bond	566
	<hr/>
Total assets	<u><u>\$5,036,553</u></u>

LIABILITIES AND MEMBERS' EQUITY

Losses unpaid	\$3,539,113
Loss adjustment expenses unpaid	73,977
Contingency reserve	678,701
Unearned premiums	490,136
Premium refunds payable	115,808
Taxes, licenses and fees payable	51,971
Dividends payable	657,297
Professional fees payable	14,000
Investment fees payable	1,300
Payroll audit fees payable	5,160
	<hr/>
Total liabilities	\$5,627,463
Restricted members' equity	308,601
Unrestricted members' equity	(899,511)
	<hr/>
Total liabilities and members' equity	<u><u>\$5,036,553</u></u>

STATEMENT OF INCOME
FOR YEAR ENDED DECEMBER 31, 2010

UNDERWRITING INCOME

Premiums earned	<u>\$1,004,803</u>
Deductions:	
Losses incurred	\$61,240
Loss expenses incurred	51,466
Other underwriting expenses incurred	276,418
Contingency reserve	<u>35,461</u>
Total underwriting deductions	<u>\$424,585</u>
Net underwriting gain	<u>\$580,218</u>

INVESTMENT INCOME

Net investment income earned	\$156,186
Net realized capital (losses)	<u>(4,506)</u>
Net investment gain	<u>\$151,680</u>
Net gain before federal income taxes	\$731,898
Federal income taxes incurred	<u>(27,757)</u>
Net income	<u><u>\$759,655</u></u>

RECONCILIATION OF MEMBERS' EQUITY
FOR THE YEAR ENDED DECEMBER 31, 2010

	<u>2008</u>	<u>2009</u>	<u>2010</u>
Members' equity, previous year before undistributed dividends	*		
	\$31,939	\$52,076	\$57,665
Adjustment for previous examination changes	85,280		
Net income	433,136	520,294	759,655
Net unrealized capital gain or (loss)	(78,464)	113,968	(3,467)
Dividends paid to members	<u>(419,815)</u>	<u>(628,673)</u>	<u>(747,466)</u>
Restricted and unrestricted members' equity, end of year	\$52,076	\$57,665	\$66,387
Less: Restricted members' equity, end of year	<u>279,276</u>	<u>318,117</u>	<u>308,601</u>
Unrestricted members' equity, end of year before undistributed dividends	(\$227,200)	(\$260,452)	(\$242,214)
Less: Dividends declared but unpaid	<u>381,703</u>	<u>511,437</u>	<u>657,297</u>
Unrestricted members' equity, end of year	<u><u>(\$608,903)</u></u>	<u><u>(\$771,889)</u></u>	<u><u>(\$899,511)</u></u>

* Adjusted members' equity from previous examination.

Members' Account By Fiscal Year Inception to Date December 31, 2010

	All Other Fiscal Years Preceding 1995-2006	Third Fiscal Year Preceding 2007	Second Fiscal Year Preceding 2008	First Fiscal Year Preceding 2009	Current Calendar Year 2010	Total Inception to Date (1995-2010)
<u>Income Received</u>						
Premiums written	\$16,979,679	\$1,924,483	\$1,681,888	\$1,437,643	\$1,842,649	\$23,866,342
Less: Excess insurance	1,923,924	281,574	245,701	231,428	182,499	2,865,126
Net premiums written	\$15,055,755	\$1,642,909	\$1,436,187	\$1,206,215	\$1,660,150	\$21,001,216
Investment income	1,672,075	104,683	69,167	20,671	174,658	2,041,254
Allocation between years	74,023	16,571	25,381	37,046	(153,021)	0
Other	154,716	0	0	0	83,506	238,222
Total income collected	\$16,956,569	\$1,764,163	\$1,530,735	\$1,263,932	\$1,765,293	\$23,280,692
<u>Less: Expenses Paid</u>						
Losses paid	\$6,766,113	\$920,561	\$281,123	\$317,473	\$332,302	\$8,617,572
Allocated loss adjustment expenses paid	410,022	59,839	37,286	25,181	31,282	563,610
Administrative fees	2,211,855	250,183	218,645	180,124	177,029	3,037,836
Service agent's fees	349,121	43,007	39,681	40,560	42,503	514,872
Taxes, licenses, and fees	421,831	46,187	57,154	72,510	0	597,682
Federal income tax	514,454	579	16,833	0	606,329	1,138,195
Other expenses	196,464	18,480	18,504	18,921	4,717	257,086
Total expenses	\$10,869,860	\$1,338,836	\$669,226	\$654,769	\$1,194,162	\$14,726,853
Net cash income	\$6,086,709	\$425,327	\$861,509	\$609,163	\$571,131	\$8,553,839
<u>Add: Receivables</u>						
Premiums receivable	\$0	\$0	\$0	\$0	\$113,456	\$113,456
Interest due and accrued	15,371	3,595	5,507	8,038	4,695	37,206
Recoverable on paid losses	277	15,847	0	0	0	16,124
Other	0	0	0	0	611,693	611,693
Total	\$15,648	\$19,442	\$5,507	\$8,038	\$729,844	\$778,479
<u>Deduct: Liabilities</u>						
Losses unpaid	\$222,645	\$300,000	\$750,000	\$1,317,866	\$948,602	\$3,539,113
Loss adjustment expenses	5,395	0	1,202	31,390	35,990	73,977
Contingency reserve	486,934	57,735	50,457	43,129	40,446	678,701
Unearned premiums	0	0	0	0	490,136	490,136
Premium refunds payable	0	0	0	0	115,808	115,808
Taxes, licenses and fees payable	0	0	0	0	51,971	51,971
Other expenses payable	0	0	0	0	20,460	20,460
Total	\$714,974	\$357,735	\$801,659	\$1,392,385	\$1,703,413	\$4,970,166

Members' Account By Fiscal Year Inception to Date December 31, 2010

	All Other Fiscal Years Preceding 1995-2006	Third Fiscal Year Preceding 2007	Second Fiscal Year Preceding 2008	First Fiscal Year Preceding 2009	Current Calendar Year 2010	Total Inception to Date (1995-2010)
Restricted and Unrestricted Members' Equity to date by fiscal year before dividends	\$5,387,383	\$87,034	\$65,357	(\$775,184)	(\$402,438)	\$4,362,152
Less: Dividends paid inception to date by fiscal year	3,936,726	85,477	273,562	0	0	4,295,765
Less: Restricted Members' Equity by fiscal year	<u>61,720</u>	<u>61,720</u>	<u>61,720</u>	<u>61,720</u>	<u>61,721</u>	<u>308,601</u>
Unrestricted Members' Equity undistributed by fiscal year	\$1,388,937	(\$60,163)	(\$269,925)	(\$836,904)	(\$464,159)	(\$242,214)
Less: Dividends declared but unpaid	<u>616,336</u>	<u>14,523</u>	<u>26,438</u>	<u>0</u>	<u>0</u>	<u>657,297</u>
Unrestricted Members' Equity 12/31/10	<u>\$772,601</u> *	<u>(\$74,686)</u>	<u>(\$296,363)</u>	<u>(\$836,904)</u>	<u>(\$464,159)</u>	<u>(\$899,511)</u>

* Although the cumulative unrestricted members' equity for the fiscal years 1995-2006 at December 31, 2010 was \$772,601, the 1999 fiscal year had members' equity deficit of \$15,040.

STATEMENT OF EXAMINERS' CHANGES IN MEMBERS' EQUITY
DECEMBER 31, 2010

	<u>Amount Per Association</u>	<u>Amount Per Examiner</u>	<u>Increase (Decrease) Members' Equity</u>
<u>Assets:</u>			
Premiums receivable	\$0	\$113,456	\$113,456
Prepaid administrative fees	1,766	1,508	(258)
Prepaid excess insurance premiums	0	3,290	3,290
<u>Liabilities:</u>			
Premium refunds payable	\$4,337	\$115,808	(\$111,471)
Administrative fees payable	6,770	0	6,770
Taxes, licenses and fees payable	57,000	51,971	5,029
Payroll audit fees payable	0	5,160	<u>(5,160)</u>
Examiners changes in members' equity			<u><u>\$11,656</u></u>
Restricted and unrestricted members' equity per Association			(\$602,566)
Restricted and unrestricted members' equity per Examiners			<u>(590,910)</u>
Increase in restricted and unrestricted members' equity			<u><u>\$11,656</u></u>

RECOMMENDATIONS FOR CORRECTIVE ACTION

Management and Control

1. The results of this examination reflect an unrestricted members' equity deficit for the 1999, 2007, 2008, 2009 and 2010 fiscal years of \$15,040, \$74,686, \$296,363, \$836,904, and \$464,159, 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. <u>Premiums receivable</u> | <u>\$113,456</u> |
| <u>Premium refunds payable</u> | <u>\$115,808</u> |

The above amounts have been increased \$113,456 and \$111,471, respectively. The Examiners' amounts are based on a review of the subsequent 2010 fiscal year member payroll audits and reflect differences between audited contributions and contributions paid at December 31, 2010.

- | | |
|---------------------------------------|----------------|
| 3. <u>Prepaid administrative fees</u> | <u>\$1,508</u> |
|---------------------------------------|----------------|

The above asset is \$258 less than the amount reported by the Association in its 2010 Annual Statement. The Examiners' amount is based on a review of subsequent 2010 fiscal year member payroll audits and reflects the difference between the actual fees paid compared to the fees required by the administrative agreement for fiscal year 2010 at December 31, 2010.

- | | |
|---|----------------|
| 4. <u>Prepaid excess insurance premiums</u> | <u>\$3,290</u> |
|---|----------------|

The above asset has been established by the Examiners. The Examiners' amount is attributed to a decrease in the normal premium, as defined by the excess insurer and developed from subsequent 2010 member payroll audits, which is the basis for computing excess insurance premiums.

5. Administrative fees payable \$0

The above liability is \$6,770 less than the amount reported by the Association in its 2010 Annual Statement. The Examiners' amount is based on a review of the subsequent 2009 fiscal year member payroll audits and reflects the difference between the fees owed and the amounts actually paid for fiscal year 2009 at December 31, 2010.

6. Taxes, licenses, and fees payable \$51,971

The above liability is \$5,029 less than the amount reported by the Association in its 2010 Annual Statement. The Examiners' amount is based on a review of invoices paid in 2011 for taxes and services pertaining to or provided in 2010.

7. Payroll audit fees payable \$5,160

The above liability has been established by the Examiners. The Examiners' amount is based on a review of invoices paid in 2011 for payroll auditing services pertaining to or provided in 2010.

SUBSEQUENT EVENT

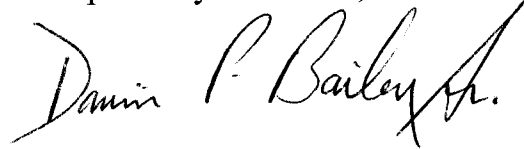
On November 4, 2011, the Bureau approved dividends for the Association totaling \$621,872.

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 and Milton Parker, Jr. participated in the work of the examination.

Respectfully submitted,

A handwritten signature in cursive script that reads "Darrin P. Bailey, Sr." The signature is written in black ink and is positioned to the right of the typed name.

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

VIRGINIA FORESTRY SAFETY GROUP SELF INSURANCE ASSOCIATION

Administered By
SELF INSURANCE SERVICES, LLC STATE CORP. COMMISSION
COST CONTROL THROUGH SERVICE BUREAU OF INSURANCE

12 MAR 19 AM 10:24

March 14, 2012

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:

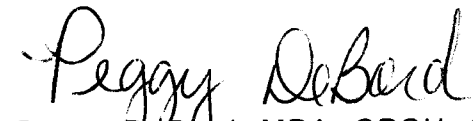
Enclosed are the responses to your recommendations for corrective action for Virginia Forestry Safety Group Self Insurance Association during the examination period January 1, 2008 through December 31, 2010.

Please let me know if you have any questions concerning our responses.

Sincerely,



Jerry D. Rose
Chairman
Members' Supervisory Board
Virginia Forestry Safety Group
Self Insurance Association



Peggy DeBord, MBA, CPCU, CIC
Administrator
Virginia Forestry Safety Group
Self Insurance Association

Enclosures

Virginia Forestry Safety Group Self Insurance Association

Responses to Recommendations for Corrective Action

Management and Control

1. The Association is aware of and will make every effort to assure that the Association is financially sound and able to fulfill its obligations under the Virginia Workers' Compensation Act.

Accounts and Records

2. The Association agrees with this adjustment. The adjustment was made with the benefit of subsequent payroll audit information not available at the time the financial statement was filed.
3. The Association agrees with this adjustment. The adjustment was made with the benefit of subsequent payroll audit information not available at the time the financial statement was filed.
4. The Association agrees with this adjustment. The adjustment was made with the benefit of subsequent payroll audit information not available at the time the financial statement was filed.
5. The Association agrees with this adjustment. The adjustment was made with the benefit of subsequent payroll audit information not available at the time the financial statement was filed.
6. The Association agrees with this adjustment. The adjustment was made with the benefit of subsequent invoice information not available at the time the financial statement was filed.
7. The Association agrees with this adjustment. The adjustment was made with the benefit of subsequent invoice information not available at the time the financial statement was filed.