



**COMMONWEALTH OF MASSACHUSETTS**  
**OFFICE OF CONSUMER AFFAIRS AND BUSINESS REGULATION**  
**DIVISION OF INSURANCE**

***REPORT OF EXAMINATION OF THE***  
**MASSACHUSETTS EDUCATION AND GOVERNMENT ASSOCIATION**  
**PROPERTY AND CASUALTY GROUP, INC.**

**Wakefield, Massachusetts**

**As of June 30, 2012**

**EMPLOYERS ID NO. 04-3287895**

**MASSACHUSETTS EDUCATION AND GOVERNMENT ASSOCIATION  
PROPERTY AND CASUALTY GROUP, INC.**

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**COMMONWEALTH OF MASSACHUSETTS**  
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**JOSEPH G. MURPHY**  
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January 17, 2014

Honorable Joseph G. Murphy  
Commissioner of Insurance  
Commonwealth of Massachusetts  
Division of Insurance  
1000 Washington Street, Suite 810  
Boston, MA 02118-6200

Honorable Commissioner:

Pursuant to your specific instructions and by authority of Section 6 of Chapter 40M of Massachusetts General Laws ("MGL"), an examination has been made of the financial condition and affairs of

**MASSACHUSETTS EDUCATION and GOVERNMENT ASSOCIATION**  
**PROPERTY and CASUALTY GROUP, INC.**

at its main administrative office located at 100 Quannapowitt Parkway, Wakefield, Massachusetts 01880. The following report thereon is respectfully submitted.

## **SCOPE OF EXAMINATION**

Massachusetts Education and Government Association Property and Casualty Group, Inc., hereinafter referred to as the ("Group") or ("MEGA"), was last examined by the Massachusetts Division of Insurance (the "Division") as of June 30, 2008. The examination covers the transactions of the Group from July 1, 2008, through June 30, 2012, including any material transactions and/or events occurring subsequent to the examination date and noted during the course of this examination.

During the examination, the transactions of the Group were reviewed and tested to the extent deemed necessary. Workpapers of the Group's independent certified public accountant and an actuarial report on unpaid loss and loss adjustment expense reserves prepared by the Group's independent consulting actuary were made available to the examiner and were utilized to the extent considered appropriate. The examination included a review of the general operations of the Group, treatment of its members and claimants, and the financial condition of the Group as of June 30, 2012. In addition, the corporate records were reviewed to ascertain compliance with Massachusetts General Laws. An independent actuarial consulting firm, PricewaterhouseCoopers LLP ("PwC") was retained by the Division to evaluate the adequacy of the Group's loss and loss adjustment expense reserves as of June 30, 2012.

The report of examination is written on the exception basis. Explanations of and details pertaining to various phases of the examination will be found herein. Unless it is specifically noted otherwise, all references to the Group's accounts, activities, and transactions are as of June 30, 2012.

### **Status of Findings from the Prior Examination**

The previous report of examination noted Property and Casualty underwriting files did not have all supporting premium detail and final premium rates within the files. This recommendation is no longer valid since the Group does not currently write Property and Casualty business.

The previous report of examination also recommended the Group review and amend their bylaws to reflect the current operating procedures of the Group. No evidence was in the Board of Directors' minutes indicating an application for membership or a vote of acceptance of a new member. The bylaws state that a prospective member must meet criteria for financial qualification and expected loss ratios. MEGA has not amended their bylaws during the current exam period and it is recommended the Group amend the bylaws to reflect the current operating procedures of the Group.

## **HISTORY**

The Massachusetts Education and Government Association Workers' Compensation Trust ("Trust") was approved for operation on June 30, 1990 by the Commissioner of Insurance and began operation on July 1, 1990 as a workers' compensation self-insurance group. The Trust was originally formed under the self-insurance provisions of MGL Chapter 152.

On October 4, 1995, the Trust was reorganized as a not-for-profit corporation known as Massachusetts Education and Government Association Workers' Compensation Group, Inc. The new corporation assumed all of the assets, liabilities, and obligations as successor-in-interest of the Trust. The Internal Revenue Service granted tax-exempt status to the Group.

On July 1, 2003, the workers' compensation group merged with the newly formed Massachusetts Education and Government Association Property & Casualty Group, Inc. This successor corporation was formed under MGL Chapter 40M, establishing a public entity property casualty group. This change allowed MEGA to offer multi-line insurance coverage in the property and liability area to public sector entities. In response to members demand, on July 1, 2007, MEGA began offering property and liability insurance. Effective July 1, 2011 the Group decided to exit the property and liability business to focus their efforts exclusively on workers compensation insurance.

## **MANAGEMENT**

According to the bylaws, the affairs of the Group shall be managed by the Board of Directors, who shall have and may exercise all the powers of the Group except those powers reserved to the members by law, the articles of organization or the bylaws. To assist in the management of the Group, the Board of Directors shall appoint an Administrator to perform and manage the day-to-day activities of the Group. The Board shall have the power to adopt and issue rules, regulations, policies and procedures which shall be binding upon the members and the Administrator.

### **Annual Meeting**

According to the bylaws as amended, the annual meeting of the members shall be held on the fourth Thursday in October of each year or, at such other time as determined by the Board of Directors.

### **Board of Directors**

The Board of Directors shall consist of not fewer than three or more than eleven directors with the number determined at each annual meeting by resolution of the members. The Board of Directors shall be divided as evenly as possible into three groups so that there will be staggered terms of office for each group of directors. Each director holds office for a term of three years. Upon expiration or resignation, his/her successor is elected at the next Annual Meeting.

MASSACHUSETTS EDUCATION AND GOVERNMENT ASSOCIATION  
PROPERTY AND CASUALTY GROUP, INC.

The members of the Board of Directors as of June 30, 2012 were as follows:

<u>Director</u>	<u>Professional Affiliation</u>
Sharon Andrew	Business Manager – Whitman-Hanson RSD
Melanie Hagman	Business Manager – Shawsheen Valley Regional VTSD
Kurtis Johnson	Director Business Operations – Blackstone Valley Vocational Technical RSD
Kirsteen Leveillee	Business Manager – South Middlesex Regional Vocational Technical School
William Ross	Town Manager – Town of Mansfield
Mark Webber	Town Administrator – Town of West Stockbridge
Martha White	Town Administrator – Town of Natick

The bylaws specify regular meetings of the Board of Directors shall be held not less than quarterly. At any meeting of the Board, not less than one-half of the Directors then in office shall constitute a quorum. The minutes indicated that a quorum was obtained at all meetings of the Board of Directors held during the examination period and the meetings were held quarterly. All Directors shall be individuals who are affiliated with (as employees, directors, trustees, or officers) members in good standing of the Group and shall be a resident of the Commonwealth.

Officers

Pursuant to the bylaws the officers of the Group shall be elected by the Board and there shall be a president, vice president, treasurer, clerk and such other officers, if any as the Board may from time to time designate. The officers shall be elected annually by the directors at their first meeting following the annual meeting of the members. The Group may also have such agents, if any, as the directors may appoint. The president must be a director.

The elected officers and their respective titles at June 30, 2012 follows:

<u>Name of Officer</u>	<u>Title</u>
Melanie Hagman	President
Mark Webber	Vice President
Kurtis Johnson	Treasurer
Tammy Smith	Clerk

Administrator

During the operating period under review, the Group by a written administrative service agreement engaged Cannon Cochran Management Services, Inc. (the "Administrator" or "CCMSI"), to perform and manage the day-to-day activities of the Group.

MASSACHUSETTS EDUCATION AND GOVERNMENT ASSOCIATION  
PROPERTY AND CASUALTY GROUP, INC.

Conflict of Interest Procedures

The Group has adopted a corporate business ethics policy for directors and officers pertaining to conflict of interest in accordance with Question 18 of the General Interrogatories of the Annual Statement. The Group has an established procedure for the disclosure to the Board of Trustees of any material interest or affiliation on the part of any officer or director which is in or is likely to conflict with his/her official duties.

**CORPORATE RECORDS**

Articles of Organization and Bylaws

The bylaws and articles of organization and amendments thereto were read. The minutes of the Board of Directors were reviewed for the period under examination. For that period, votes and authorizations were found to be in order and the records indicated that the group appeared to be conducting its affairs in compliance with its bylaws and the laws of the Commonwealth of Massachusetts.

Disaster Recovery and Business Continuity

The Administrator has a formal disaster plan for the continuity of the Group's business operations in the event of any disaster. The total recovery effort is governed by the Cannon Cochran Management Services, Inc. Disaster Recovery Plan. That plan was made available to the examiner for review and determined to have addressed adequately the process in which to resume certain critical business functions of the Group.

**GROWTH OF THE GROUP**

The following exhibit, compiled from financial statements of the Group for the years ended June 30, 2008 through June 30, 2012, are as follows:

Fund Year	Net Written Premium	Admitted Assets	Liabilities	Member's Surplus
2012	\$ 10,710,962	\$ 14,658,077	\$ 15,297,276	\$ (639,199)
2011	10,056,123	16,983,712	17,953,921	(970,209)
2010	11,061,735	20,870,167	16,382,200	4,487,967
2009	12,699,324	24,773,610	17,128,937	7,644,673
2008	16,307,843	28,538,508	17,439,400	11,099,108

### **TERRITORY AND PLAN OF OPERATION**

The Group is a self-insurance group permitted to transact business only in the Commonwealth of Massachusetts.

### **FIDELITY BONDS AND OTHER INSURANCE**

The Administrator has an Errors and Omissions policy with a limit of \$10 million per occurrence and \$10 million in the aggregate with an authorized Massachusetts insurer. The Group has coverage for Directors' and Officers' liability with a \$1 million limit.

### **REINSURANCE**

The Group maintains an excess workers compensation and employers liability insurance policy with an unaffiliated insurer. Under this policy, the Group's losses at June 30, 2012, in excess of \$1,000,000 for each individual accident or employee will be covered by the policy in accordance with statutory limits.

### **ACCOUNTS AND RECORDS**

The trial balance, general ledger and audited financial statements provided by the Group were reviewed for the fund year ending June 30, 2012. The Administrator received an Independent Service Auditor's Report for their third-party administration workers' compensation and property/casualty programs system for the period October 2, 2011 to September 30, 2012. The report's conclusion found CCMSI's claim systems are suitably designed to provide reasonable assurance that the specified control objectives would be achieved if the described controls were complied with satisfactorily.

General ledger account balances were reconciled and traced to amounts reported in the Annual Statement for the year ended June 30, 2012. All balance sheet accounts with a category class of statutory ledger, non ledger and non-admitted were summarized and traced to the appropriate asset exhibits and liability lines within the Annual Statement. Selected income and expense allocations and postings were sampled and verified for reasonableness. No material exceptions were noted.

The books and records of the Group are audited annually by Shores, Tagman, Butler & Company, P.A., independent certified public accountants, in accordance with 211 CMR 23.00.

MASSACHUSETTS EDUCATION AND GOVERNMENT ASSOCIATION  
PROPERTY AND CASUALTY GROUP, INC.

**FINANCIAL STATEMENTS**

The following financial statements are presented on the basis of accounting practices prescribed or permitted by the Division of Insurance of the Commonwealth of Massachusetts and by the National Association of Insurance Commissioners as of June 30, 2012:

Statement of Assets, Liabilities, Surplus and Other Funds as of June 30, 2012

Statement of Income for the year ended June 30, 2012

Statement of Capital and Surplus for the year ended June 30, 2012

Reconciliation of Capital and Surplus for the Four-Year Period ended June 30, 2012

**Massachusetts Education and Government Association Property and Casualty Group, Inc.**

Statement of Assets, Liabilities, Surplus and Other Funds

As of June 30, 2012

<b>Assets</b>	Per Company	Examination Changes	Per Examination	Notes
Bonds	\$11,663,570	\$ 0	\$11,663,570	
Common stocks	1,451,244		1,451,244	
Cash and short-term investments	1,121,939		1,121,939	
Receivable for securities	10,625		10,625	
Subtotals, cash and invested assets	14,247,378	\$ 0	14,247,378	
Investment income due and accrued	78,660		78,660	
Premiums and considerations:				
Deferred premiums	75		75	
Reinsurance: Amounts recoverable from reinsurers	332,797	(171,835)	160,962	( 1 )
Aggregate write-ins for invested assets:				
Other Receivables	(833)		(833)	
Total Assets	<u>\$14,658,077</u>	<u>\$ (171,835)</u>	<u>\$14,486,242</u>	
<b>Liabilities</b>				
Losses	\$14,146,772	\$ 5,659,342	\$19,806,114	( 2 )
Loss adjustment expenses	2,766,448		2,766,448	
Other expenses	16,725		16,725	
Advance premiums	610,928		610,928	
Aggregate write-ins for liabilities:				
Time Value of Money Discount	(2,243,597)	773,175	(1,470,422)	( 3 )
Total Liabilities	<u>15,297,276</u>	<u>6,432,517</u>	<u>21,729,793</u>	
Gross paid in and contributed surplus	573,835		573,835	
Unassigned funds (surplus)	(1,213,034)	(6,604,352)	(7,817,386)	
Surplus as regards policyholders	<u>(639,199)</u>	<u>(6,604,352)</u>	<u>(7,243,551)</u>	
Total Liabilities, Capital, and Surplus	<u>\$14,658,077</u>	<u>\$ (171,835)</u>	<u>\$14,486,242</u>	

**Massachusetts Education and Government Association Property and Casualty Group, Inc.**

Statement of Income

For the Year Ended June 30, 2012

	As Reported by the Company	Examination Changes	Per Statutory Examination	Notes
Premiums earned	\$ 10,710,962	\$ 0	\$ 10,710,962	
Deductions:				
Losses incurred	5,685,820	5,659,342	11,345,162	( 2 )
Loss expenses incurred	2,191,648		2,191,648	
Other underwriting expenses incurred	2,982,941		2,982,941	
Aggregate write-ins for underwriting deductions:				
Time Value of Money Discount	495,644	773,175	1,268,819	( 3 )
Total underwriting deductions	11,356,053	6,432,517	17,788,570	
Net underwriting gain (loss)	(645,091)	(6,432,517)	(7,077,608)	
Net investment income earned	279,374		279,374	
Net realized capital gains (losses)	69,836		69,836	
Net investment gain (loss)	349,210		349,210	
Net gain (loss) from agents' or premium balances charged off	(49,227)		(49,227)	
Total other income	(49,227)		(49,227)	
Net income before dividends to policyholders and before federal and foreign income taxes	(345,108)	(6,432,517)	(6,777,625)	
Dividends to policyholders				
Net income, after dividends to policyholders but before federal and foreign income taxes	(345,108)	(6,432,517)	(6,777,625)	
Federal and foreign income taxes incurred				
Net Income	\$ (345,108)	\$ (6,432,517)	\$ (6,777,625)	

**Massachusetts Education and Government Association Property and Casualty Group, Inc.**  
**Capital and Surplus**  
**For the Year Ended June 30, 2012**

	<u>As Reported by the Company</u>	<u>Examination Changes</u>	<u>Per Statutory Examination</u>	<u>Notes</u>
Surplus as regards policyholders, June 30, 2011	\$ (970,209)	\$ 0	\$ (970,209)	
Net income	(345,108)	\$ (6,432,517)	(6,777,625)	(2) & (3)
Change in net unrealized capital gains or (losses)	(28,356)		(28,356)	
Change in nonadmitted assets	130,639	(171,835)	(41,196)	(1)
Surplus adjustments: Paid in	<u>573,835</u>		<u>573,835</u>	
Change in surplus as regards policyholders for the year	<u>331,010</u>	<u>(6,604,352)</u>	<u>(6,273,342)</u>	
Surplus as regards policyholders, June 30, 2012	<u>\$ (639,199)</u>	<u>\$ (6,604,352)</u>	<u>\$ (7,243,551)</u>	

**Massachusetts Education and Government Association Property and Casualty Group, Inc.**

Reconciliation of Capital and Surplus  
For the Four-Year Period Ended June 30, 2012

	<u>2012</u>	<u>2011</u>	<u>2010</u>	<u>2009</u>
Surplus as regards policyholders,				
June 30, prior year	\$ (970,209)	\$ 4,487,967	\$ 7,644,673	\$11,099,108
Net income	(6,777,625)	(5,998,800)	(2,433,000)	(2,939,649)
Change in net unrealized capital gains or (losses)	(28,356)	460,919	190,078	(547,737)
Change in nonadmitted assets	(41,196)	79,705	(7,409)	32,951
Surplus adjustments: Paid in	573,835			
Aggregate write-ins for gains and losses in surplus			(906,375)	
Net change in capital and surplus for the year	<u>(6,273,342)</u>	<u>(5,458,176)</u>	<u>(3,156,706)</u>	<u>(3,454,435)</u>
Capital and surplus, June 30, current year (*)	<u><u>\$ (7,243,551)</u></u>	<u><u>\$ (970,209)</u></u>	<u><u>\$ 4,487,967</u></u>	<u><u>\$ 7,644,673</u></u>

\* - Reflects results of examination changes

## NOTES TO FINANCIAL STATEMENTS

### NOTE 1:

Amounts Recoverable from Reinsurers \$160,962

The receivable for reinsurance has been reduced by \$171,835 by the examination. Review of the receivables found balances overdue in excess of 90 days which requires the balances to be non-admitted for examination purposes. It is recommended that the Group properly age the reinsurance recoverable in accordance with Schedule F Part 4 of the Annual Statement.

### NOTE 2:

Losses \$ 19,806,114  
Loss Adjustment Expenses \$ 2,766,448

The Division engaged PricewaterhouseCoopers LLP to review the reasonableness of the Loss and Loss Adjustment Expense Reserves (the "Reserves") of MEGA as of June 30, 2012. The review was conducted in a manner consistent with the Code of Professional Conduct and the Qualification Standards of the American Academy of Actuaries and the Standards of Practice adopted by the Actuarial Standards Board.

MEGA held net loss and LAE reserves of \$16.9 million as of June 30, 2012. These reserves are net of anticipated salvage and subrogation and ceded reinsurance.

PwC's actuarial review utilized various actuarial methodologies to analyze MEGA's accident year paid and incurred loss data at annual valuations through June 30, 2012. PwC's actuarial central estimate of the net loss and LAE reserves is \$22.6 million. PwC also calculated a range of estimates that it considered reasonable and acceptable. The overall reasonable range of estimates extends from \$20.9 million to \$24.9 million.

The table below summarizes a comparison of PwC's range of reasonable estimates for Loss and LAE Reserves to the Company's net carried Loss and LAE Reserves as of June 30, 2012.

	Low Point of Range	Selected Estimate	High Point of Range
PricewaterhouseCoopers Estimate	\$20,867,722	\$22,572,562	\$24,879,678
Company Carried	16,913,220	16,913,220	16,913,220
Company Carried Over / (Under) PwC	(3,954,502)	(5,659,342)	(7,966,458)

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PwC updated their reserve analysis through the quarter ended March 31, 2013 to analyze more recent data. PwC's central estimate of reserves as of March 31, 2013, based upon a re-projection of ultimate losses and LAE and the associated reserves, was \$22.04 million, with a range of reasonability from \$20.39 million to \$24.44 million. MEGA's corresponding net held reserves at March 31, 2013 were \$15.51 million for losses and LAE. MEGA's held reserves were \$6.53 million below PwC's point estimate and \$4.88 million below the low end of PwC's range of reasonability.

NOTE 3:

Time Value of Money Discount	\$(1,470,422)
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MEGA used IRS discount factors to determine their discount of loss reserves. The exam discount was calculated using an assumed annual interest rate of 2.0% and payment patterns derived from MEGA's own historical payment history, resulting in a discount that is \$773,275 lower than MEGA's discount. We note that MEGA's investment income has continued to drop in response to further declines in interest rates.

**COMMENTS AND RECOMMENDATIONS**

It is recommended that MEGA properly age their Reinsurance Recoverable balances in accordance with Annual Statement instructions and properly complete the applicable parts of Schedule F of the Annual Statement.

MEGA instituted an assessment plan to recoup approximately \$4.70 million of its workers compensation losses for the three policy years that sustained the highest operating losses (policy years 7/03-04 through 7/05-06). For these years, MEGA's loss ratios, excluding the assessments were estimated to be between 95% and 120% as of March 31, 2011. Current loss ratios, including the impact of all planned assessments, are estimated to be 96%, 91% and 93% based on projections as of March 31, 2013.

MEGA should consider an assessment for Property/Casualty ("P&C") coverage that was written at a significant underwriting loss during the 2008 through 2011 policy years. MEGA earned \$3.4 million in net premium for the property casualty program during these years and has paid \$8.52 in losses through March 2013. PwC estimates that MEGA will pay an additional \$2.4 million in losses for this program to close the remaining open claims. MEGA's workers compensation program appears to be returning to a more stable financial position. Losses of \$7.5 million from the property casualty program have put a financial strain on the Group as a whole.

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PROPERTY AND CASUALTY GROUP, INC.

**ACKNOWLEDGEMENT**

Acknowledgement is made of the cooperation and courtesies extended by the officers and employees of the Company to all examiners during the examination.

A handwritten signature in cursive script, reading "Kenneth R. Plumb", is written over a horizontal line.

Kenneth R. Plumb, CPA, CFE  
Examiner-in-Charge  
Supervising Examiner  
Commonwealth of Massachusetts  
Division of Insurance