ATTACHMENT B

STATE OF COLORADO

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Date: September 14, 2010

To: Members of the Legislative Audit Committee

From: Sally Symanski, CPA SJS
State Auditor

Subject: Pinnacol Assurance Status Report and Related Information

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The following documents have been provided by Pinnacol Assurance:

Exhibit 1. Status Report: Summary and Detail of Implementation Status

Exhibit 2. Executive Performance Plan Target Setting Methodology **(Recommendation No. 1)**

Exhibit 3. Amended and Restated Executive Performance Plan (Approved by Board on August 4, 2010) **(Recommendation No. 2)**

Exhibit 4. Executive Discretionary Bonus Program **(Recommendation No. 3)**

Exhibit 5. Information Provided at August 17, 2010, Legislative Audit Committee hearing **("Information Only")**

The following documents have been compiled by the Office of the State Auditor (OSA):

Exhibit 6. Stipulation for Entry of Final Agency Order, Division of Insurance, with Summary prepared by the OSA

AUDIT RECOMMENDATION STATUS REPORT

AUDIT NAME: Pinnacol Assurance Performance Audit
AUDIT NUMBER: 2042
DEPARTMENT/AGENCY/ENTITY: Pinnacol Assurance
DATE: June 2010

SUMMARY INFORMATION

Please complete the table below with summary information for all audit recommendations. ***For multi-part recommendations, list each part of the recommendation SEPARATELY.*** *(For example, if Recommendation 1 has three parts, list each part separately in the table.)*

Recommendation Number *(e.g., 1a, 1b, 2, etc.)*	**Pinnacol's Response** *(i.e., agree, partially agree, disagree)*	**Original Implementation Date** *(as listed in the audit report)*	**Implementation Status** *(Implemented, Partially Implemented, or Not Implemented)* ** A recommendation that is in progress should be denoted as "partially implemented."*	**Revised Implementation Date** *(Complete only if Pinnacol is revising the original implementation date.)*
1a	Agree	December 2010	Implemented	September 1, 2010
1b	Agree	December 2010	Implemented	September 1, 2010
1c	Agree	December 2010	Implemented	September 1, 2010
2a	Agree	December 2010	Implemented	September 1, 2010
2b	Agree	December 2010	Implemented	September 1, 2010
2c	Agree	December 2010	Implemented	September 1, 2010
3a	Agree	December 2010	Implemented	September 1, 2010
3b	Agree	December 2010	Implemented	September 1, 2010
3c	Agree	December 2010	Implemented	September 1, 2010
3d	Agree	December 2010	Implemented	September 1, 2010
3e	Agree	December 2010	Implemented	September 1, 2010
4a	Agree	December 2010	Partially implemented	
4b	Agree	December 2010	Partially implemented	
5	Partially Agree	December 2010	Implemented	September 1, 2010

Recommendation Number *(e.g., 1a, 1b, 2, etc.)*	**Pinnacol's Response** *(i.e., agree, partially agree, disagree)*	**Original Implementation Date** *(as listed in the audit report)*	**Implementation Status** *(Implemented, Partially Implemented, or Not Implemented)* ** A recommendation that is in progress should be denoted as "partially implemented."*	**Revised Implementation Date** *(Complete only if Pinnacol is revising the original implementation date.)*
6a	Agree	December 2010	Partially implemented	
6b	Agree	December 2010	Implemented	September 1, 2010
7a	Agree	December 2010	Partially implemented	
7b	Agree	December 2010	Partially implemented	
8a	Partially Agree	December 2010	Partially implemented	
8b	Partially Agree	December 2010	Partially implemented	
8c	Partially Agree	December 2010	Partially implemented	
9	Agree	Implemented and Ongoing	Implemented	
10	Agree	Implemented and Ongoing	Implemented	
11	Agree	December 2010	Not implemented	December 31, 2011
12a	Agree	December 2010	Partially implemented	December 1, 2010
12b	Agree	December 2010	Partially implemented	December 1, 2010
13	Agree	December 2010	Partially implemented	December 1, 2010
14	Agree	December 2010	Partially implemented	

DETAIL OF IMPLEMENTATION STATUS

Recommendation No. 1: The Board of Directors should work with Pinnacol Assurance management to ensure the Executive Performance Plan is structured to promote and reward superior performance by:

a. Fully documenting the methodology for setting all targets, the rationales for the methodology, and how it should be applied. The documentation should clearly reflect how the Board has defined superior performance and how the target-setting methodology supports that definition.

b. Developing and documenting a standardized evaluation mechanism that includes reviewing the targets against actual results annually. The evaluation should be used to determine the extent to which the program's intent of rewarding superior performance is being accomplished and to modify the program's structure and goals as needed.

c. Obtaining professional expertise regarding the development and application of a methodology for setting performance targets as appropriate.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

a. The Board establishes Executive Performance Plan targets. Prior to 2009, Plan targets were set by reviewing the company's annual business plan goals and utilizing the probability theory recommended by compensation consultants. In 2009, the Board changed its methodology for setting Plan targets to an established formula that also factors in past performance. The 2009 Plan maximum net income target was set at 230 percent of the 2009 business plan goal. The Board Compensation Committee documented this methodology for setting Plan targets in 2009 and used the same methodology for establishing 2010 Plan targets. The Board will expand its documentation to define how the target-setting methodology supports superior performance.

b. A standardized evaluation process, developed and implemented in 2009, is already in place. The Board Compensation Committee evaluated the process used in 2009 at the February 17, 2010 Compensation Committee meeting and recommended the same methodology for 2010 which was approved at the March 10, 2010 Board meeting. The Board Compensation Committee will document this annual evaluation in meeting minutes.

c. This process is already in place. For the past several years, the Board has retained the Hay Group to provide professional executive compensation expertise.

Pinnacol's Comments on Implementation Status of Recommendation:

a. The Board has expanded its documentation to define how the target-setting methodology supports superior performance. The documentation includes the Executive Performance plan document and target setting methodology document.

b. Annually there will be a separate agenda item for the Board Compensation Committee to evaluate the prior year's EPP against intent to reward for superior performance and document the discussion in meeting minutes. In addition, the Compensation Committee will review three year net income and combined ratio projections relative to proposed EPP targets to evaluate intent to reward future performance.

c. We addressed this in our initial response.

Recommendation No. 2: The Board of Directors should work with Pinnacol Assurance management to improve Pinnacol's controls over awards paid under the Executive Performance Plan by developing and implementing written policies and procedures that:

a. Describe the sources of data and methods for determining net income and combined ratio results for the Plan as well as for calculating bonuses.

b. Require a thorough, standardized, and documented review of all data and calculations related to determining bonuses prior to payment.

c. Establish a mechanism for recovering any bonus payments made in error.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

a. The methodology used to calculate net income and combined ratio was documented by the Controller in 2010 for the 2009 bonuses. This methodology was provided to the Compensation Committee and the Board for their review. In the future, Pinnacol will use a consistent methodology to calculate net income and combined ratio and will continue to report the methodology to the Board and Compensation Committee. Bonus calculations have been documented for many years.

b. The Controller already reviews all data and calculations performed by Human Resources prior to payment. For the 2009 bonuses, this review was documented. This recommendation has already been implemented.

c. Though no overpayments have been made in the past, the Board and Pinnacol Assurance agree to investigate the possibility of implementing a mechanism for recovering any bonus payments made in error.

Pinnacol's Comments on Implementation Status of Recommendation:

a. The source of data for determining net income and combined ratio results is the financial statement which will be included in the documentation for 2010 bonuses. The Controller has already documented the methodology used to calculate net income and combined ratio results for 2009 and will use this same methodology in 2010. Results will be reviewed by the Board Compensation Committee, approved by the Board and documented in Board minutes.

b. A memo will be prepared to document the components of the CEO's review process and approval of awards for individual/business unit goals. A memo will be prepared to document the components of the Controller's review of the accuracy of the award calculations. Compensation Committee minutes will document their review and approval of corporate net income, combined ratio and customer satisfaction results. To ensure we have a dual audit system in place, internal auditors, independent of Pinnacol, will review documentation and accuracy of award payouts.

c. The Executive Performance Plan document has been amended and restated to include a clawback provision.

Recommendation No. 3: The Pinnacol Board of Directors should reevaluate whether the discretionary bonus program is in the best interests of Pinnacol Assurance and its policyholders. If the Board chooses to retain the program, it should work with Pinnacol Assurance management to strengthen the discretionary bonus program by creating a written policy that:

a. Clearly indicates the program's purpose and how it is distinct from the purpose of the Executive Performance Plan.

b. Includes criteria that define "extraordinary" performance and "special projects" in such a way that they are distinct from the achievements the Plan rewards and do not include normally assigned duties.

c. Coordinates the timing of Executive Performance Plan bonuses and discretionary bonuses to prevent duplication.

d. Includes the requirement that the CEO report all discretionary bonuses to the Board for review before the bonuses are paid.

e. Documents the dollar limits the Board has established for the program.

<u>Pinnacol's Written Response in Audit Report</u>:

Agree. Implementation date: December 31, 2010.

a. The Board agrees to provide additional documentation as described in the recommendation.

b. The Board agrees to provide additional documentation as described in the recommendation.

c. The Board agrees to review the timing of discretionary bonuses.

d. In 2009, the Board formally made it a requirement for the CEO to report all discretionary bonuses to the Board for review prior to bonuses being paid. This recommendation has already been implemented.

e. Dollar limits were set with the inception of the plan and have remained unchanged. This recommendation has already been implemented.

<u>Pinnacol's Comments on Implementation Status of Recommendation</u>:

a. A plan document has been formalized by the Board and the program's purpose is included in the plan document.

b. Criteria has been established and is documented in the plan document.

c. The plan document states that a discretionary bonus must be awarded in the same calendar year as the year the performance generating the bonus occurred. The CEO, Vice Presidents and Associate Vice Presidents are eligible to receive a discretionary bonus unless they are already being compensated or rewarded for the performance or effort with another form of recognition or payment.

d. The plan document requires the CEO to inform the full Board of his/her proposed discretionary bonus recommendations.

e. The dollar limits the Board has established for this program have been documented in the plan document.

Recommendation No. 4: Pinnacol Assurance should strengthen the gainsharing program by:

a. Evaluating its target-setting process to ensure the program is meeting its philosophy of paying bonuses only for extraordinary performance.

b. Documenting clear and reasonable objectives and rationales for the program, including all critical elements.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

Pinnacol agrees with the recommendations.

Pinnacol's Comments on Implementation Status of Recommendation:

a. The Gainsharing Task Force is evaluating the target-setting process to ensure the program is meeting its philosophy of paying bonuses only for extraordinary performance. The evaluation will be completed by December 31, 2010.

b. The Gainsharing Task Force is working on documenting clear and reasonable objectives and rationales for the program, including all critical elements.

Recommendation No. 5: The Board of Directors should work with Pinnacol Assurance management to further research and refine the methods used to select the loss cost multipliers. The Board and Pinnacol should select and apply loss cost multipliers that are based on indicated differences in expected losses and expenses among tiers, giving full consideration to all other anticipated rating adjustments.

Pinnacol's Written Response in Audit Report:

Partially agree. Implementation date: December 31, 2010.

Pinnacol and the Board of Directors will continue to evaluate and exercise prudent consideration in the selection of each individual tier change based on indications for the determination of our ultimate loss cost multipliers. This process includes but is not limited to: maintaining our intent of complying with Colorado Insurance Law, utilizing allowable judgment, properly acknowledging Colorado Division of Insurance oversight and loss cost rate orders, our past and prospective loss experience, Colorado marketplace conditions, valid rating adjustments, potential changes to our underwriting model, and expense provisions. Hence, our goal of striving to ensure that our rates are not excessive, inadequate, or unfairly discriminatory is unchanged.

Pinnacol does not believe that this audit process validated any Colorado Insurance Law concerns with our rating process that were material or that would have ultimately had an impact on our "filed" rates.

Pinnacol's Comments on Implementation Status of Recommendation:

In response to an inquiry from the Colorado Division of Insurance (DOI), we engaged an independent, qualified actuary to review our current LCM structure. The content of the analysis was shared with the DOI. On 9/8/2010, the DOI "Filed" and accepted our loss cost multipliers that were effective on 1/1/2010. This submission was originally provided to the DOI on 12/28/2009. The loss cost multipliers were accepted as they were originally submitted from Pinnacol Assurance, without any changes from the DOI. The Attorney General and Pinnacol Assurance have concurred that this actuarial analysis is "confidential" and not for public dissemination.

Recommendation No. 6: The Board of Directors and Pinnacol Assurance should improve the method used to determine the indicated tier LCMs by:

a. Implementing a comprehensive review process for all data, calculations, and material assumptions used in the process for accuracy, consistency, and reasonableness.

b. Considering the use of a qualified actuary to assist in setting rates.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

a. Pinnacol and the Board will conduct research and develop a viable review process. Such review process will determine if any changes are needed.

b. Pinnacol management will continue to evaluate the merits of using a qualified actuary to assist in setting rates and implement any needed changes.

Pinnacol's Comments on Implementation Status of Recommendation:

a. Under the direction of the Director of Corporate Compliance, Pinnacol is researching and developing an enhanced internal LCM review process which may include on-going assistance of a qualified actuary.

b. Pinnacol management engaged a qualified actuary to review our current LCM's.

Recommendation No. 7: The Pinnacol Board should work with Pinnacol Assurance management to ensure that the method used to determine eligibility for the Schedule Rating Plan is in compliance with all applicable statutes by:

a. Reevaluating the use of the Standard tier LCM to determine whether policies are eligible for Schedule Rating adjustments and the effect of the methodology on employer premiums.

b. Filing all rating information with the Division of Insurance before using the information to determine premiums.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

a. Pinnacol management will continue our on-going regulatory dialogue with the Colorado Division of Insurance to determine an appropriate outcome to this issue by ensuring our method used to determine eligibility for the Schedule Rating Plan remains compliant with Colorado Insurance Law and does not adversely impact our policyholders. The result(s) of such dialogue will be communicated to the Board for its consideration. This audit has validated that our consistent process has increased schedule rating eligibility by approximately 2 percent of our policyholders over a four-year period (January 1, 2005 – December 31, 2008) resulting in schedule rating net premium reductions equaling $475,994. As such, we will continue to research this issue and implement any needed changes.

b. Pinnacol management will review our process of filing all rating information with the Division of Insurance with the intention of ensuring we are in compliance with all statutes and our filings are complete and accurate. The results of this review will be communicated to the Board.

Pinnacol's Comments on Implementation Status of Recommendation:

This item was settled on August 24, 2010.

a. Pinnacol and the DOI have agreed that Pinnacol will modify the use of standard tier LCM's for all eligible policies effective January 1, 2011.

b. Pinnacol and the DOI have agreed to modify some of the factors used in the schedule-rating plan for all eligible policies effective January 1, 2011. The revised schedule-rating plan will be resubmitted to the DOI prior to January 1, 2011. In addition, Pinnacol now has a Director of Corporate Compliance who reviews rate filings to ensure that all filings are complete and accurate.

Recommendation No. 8: Pinnacol Assurance should improve its rate filings submitted to the Division of Insurance by:

a. Reevaluating its Schedule Rating Plan to eliminate factors that duplicate the employer's experience rating.

b. Ensuring it files any changes to its Schedule Rating Plan before applying the changes.

c. Ensuring it submits filings that are complete and accurate.

Pinnacol's Written Response in Audit Report:

Partially agree. Implementation date: December 31, 2010.

a. Pinnacol management will continue our on-going regulatory dialogue with the Colorado Division of Insurance to determine an appropriate outcome to this issue by ensuring our Schedule Rating Plan factors remain compliant with Colorado Insurance Law while not adversely impacting our policyholders. At this point, Pinnacol does not believe that this audit process validated that our schedule rating factors duplicate the employer's experience rating.

b. As previously stated in our response to Recommendation No. 7b, Pinnacol will review our process of filing all rating information (including changes to the Schedule Rating Plan) with the Division of Insurance with the intention of ensuring we are in compliance with all statutes and our filings are complete and accurate.

c. As previously stated in our response to Recommendation Nos. 7b and 8b, Pinnacol will review our process of filing all rating information with the Division of Insurance with the intention of ensuring we are in compliance with all statutes and our filings are complete and accurate.

Pinnacol's Comments on Implementation Status of Recommendation:

This item was settled on August 24, 2010.

a. Pinnacol and the DOI have agreed that Pinnacol will modify the Schedule Rating Plan for all eligible policies effective January 1, 2011.

b. Pinnacol and the DOI have agreed to modify some of the factors used in the schedule-rating plan for all eligible policies effective January 1, 2011. The revised schedule-rating plan will be resubmitted to the DOI prior to January 1, 2011.

c. Pinnacol has implemented some internal changes and continues to research and develop an enhanced internal review process that may include on-going assistance of a qualified actuary to assure completeness and accuracy of our filings. Pinnacol is collaborating with an independent actuary to assist, in some manner, with future loss cost multiplier filings. In addition, we have assigned a Director of Corporate Compliance to oversee our DOI filing process.

Recommendation No. 9: The Board of Directors should continue to work with Pinnacol Assurance management to apply the surplus policy, including annually evaluating the surplus collar, adjusting the collar as appropriate, and managing rates and dividends to bring the surplus to a level within the collar.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: Implemented and ongoing.

The Board and Pinnacol management will continue to apply the surplus policy, including evaluating and adjusting the surplus collar and managing rates and dividends on a multi-year timeframe, to bring the surplus to a level indicated by the collar.

Pinnacol's Comments on Implementation Status of Recommendation:

On August 19, the Investment Committee completed its annual review of the surplus policy and made a recommendation to the Board to approve the policy. The Board approved the surplus policy at the September 1 meeting.

Recommendation No. 10: Pinnacol Assurance should continue its training and other efforts to ensure that staff are handling claims appropriately and to reduce errors and violations in processing claims.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: Implemented and ongoing.

Pinnacol agrees with Recommendation No. 10 and remains committed to continuing training and other efforts to handle claims appropriately. The compliance results from the Division of Workers' Compensation Claims audits clearly demonstrate that Pinnacol's results improved in each category from 2007 to 2009.

Pinnacol's Comments on Implementation Status of Recommendation:

Pinnacol continues to provide training and other efforts to handle claims appropriately. A list of training classes that claim staff might attend is available for review.

Recommendation No. 11: Pinnacol Assurance should consider expanding the use of the injured worker surveys by setting targets and including the results as a component of the Executive Performance Plan and gainsharing programs.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

The Board and Pinnacol agree to evaluate the injured worker survey process and internal uses. Neither the Board nor Pinnacol can commit to include survey results in the Executive Performance Plan and gainsharing metrics until an analysis is completed. In addition, Senate Bill 10-13 and Division of Workers' Compensation Rules of Procedure Rule 5, 5-14 regarding surveys will impact the survey process. At the time of the response, Senate Bill 13 has not been signed into law and Rule 5-14 is only proposed. Pinnacol will study the issue.

Pinnacol's Comments on Implementation Status of Recommendation:

Senate Bill 13 and Rule 5-14 were just finalized in July 2010. The injured worker survey was distributed for the first time in August 2010 and results are pending. We require more time to evaluate the injured worker survey results, establish benchmarks to be evaluated by the Compensation Committee, and determine their applicability as a performance measure for gainsharing and executive performance plan purposes. We will complete our evaluation of the survey process and determine if there is an appropriate internal use of these results in the Executive Performance Plan or gainsharing program during 2011.

Recommendation No. 12: Pinnacol Assurance and the Board of Directors should adhere to established policies over employee and Board travel and entertainment expenses and improve policies where necessary by:

a. Establishing a meaningful review process that enforces all policy requirements such as those for proper receipts, documentation, prior approval and justification, and allowable expense provisions. Managers that do not uphold policies should be subject to disciplinary action.

b. Establishing and implementing a policy that requires an independent review of Board member and CEO travel and entertainment expenses, such as by requiring the Board or a designated Board member to review for approval the expenses of the CEO and requiring the Board Chair to review for approval the expenses of Board members.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

a. Pinnacol will review and revise the travel and entertainment expense policy to make sure that it accurately reflects all of the requirements for reimbursement. After the revised policy is issued and communicated to employees, all managers will be responsible for fully enforcing the policy.

b. The Board will evaluate a policy designating the Board member(s) responsible for reviewing the expenses of the CEO and of Board members.

Pinnacol's Comments on Implementation Status of Recommendation:

a. A draft policy that accurately reflects all of the requirements for reimbursement was distributed for review by management on September 7, 2010. The final policy will be issued in the fourth quarter of 2010. Staff will be trained immediately and the new policy will be effective on December 1, 2010.

b. Independent Board review of the expenses of the CEO and of other Board members is included in the policy referenced in 12a.

Recommendation No. 13: Pinnacol Assurance should strengthen its controls over lodging and non-business meal expenses by establishing clear "not to exceed" spending guidelines on these expenses in its expense policies and requiring employees and Board members to follow the guidelines.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

As part of the travel and expense policy review mentioned in the response to Recommendation No. 12, Pinnacol will evaluate enhancing the guidelines on lodging and meal spending. Any decisions made will be incorporated into the revised policy.

Pinnacol's Comments on Implementation Status of Recommendation:

The policy referenced in 12a contains clear spending guidelines on lodging and meal expenses.

Recommendation No. 14: Pinnacol Assurance and the Board of Directors should strengthen employee and Board Business Ethics and Conflict of Interest policies by defining the type and dollar value of gifts, benefits, or expenses paid by Pinnacol's business partners, that employees and Board members must disclose.

Pinnacol's Written Response in Audit Report:

Agree. Implementation date: December 31, 2010.

Pinnacol and the Board will research possible policy enhancements and implement changes.

Pinnacol's Comments on Implementation Status of Recommendation:

A new gift policy has been approved by Pinnacol management and will be effective October 1, 2010. The Board of Directors is evaluating a gift policy to be implemented by January 1, 2011.

Executive Performance Plan Target Setting Methodology

With the 2009 changes the Board has already made to the Executive Performance Plan (EPP), the Board feels the Plan is designed to reward Executives appropriately when superior performance has been achieved.

In 2009, the Board addressed the need to establish more rigor in the financial planning process and in setting EPP targets. An ad-hoc committee comprised of Board members and Pinnacol management oversee the development of the financial plan that is approved annually by the Board. The financial plan provides the Board with annual net income and combined ratio plan targets which along with customer satisfaction are key performance drivers in the insurance industry. These performance drivers are included in the EPP and achieving a minimum net income threshold is required to trigger an award payout under the EPP.

In setting EPP targets, the Board feels that it is their fiscal responsibility to set stretch goals that have a longer- term focus. Setting targets requires an understanding of the volatility of the business which will constantly be impacted by changes in payroll as a result of economic expansion/recession, premium rates (that have been dropping significantly over the past several years), investment income and reserves that are constantly being recalibrated based on the risk associated with the book of business. These factors are considered in setting annual financial plan goals and EPP targets.

Along with the current year financial projections, the Board Compensation Committee developed a formula in 2009 for establishing net income and combined ratio EPP targets that acknowledges past performance and provides participants with a clear understanding of how targets are set and awards calculated. Acknowledging past performance recognizes that there is uncertainty in the financial planning process and considers that there is momentum (the human element) that needs to be taken into account to set EPP targets. Prior to 2009, only the business plan and Milliman projections based on probabilities were used to set EPP targets.

The same formulas used in 2009 to set net income and combined ratio targets have been used to set 2010 net income targets. Details are as follows:

2010 Net Income Targets

To establish the maximum 2010 EPP net income target - the 3-year rolling average percent difference between plan and actual net income is 200%. 200% of the 2010 business plan of $47.4M = $94.8M which is used to set the Maximum EPP target. The threshold EPP target is set at 57.7% of the maximum 200% of plan = $54.51M. Commendable = $74.66M which is the midpoint between threshold and maximum.

Note, that past performance (3-year rolling average percent difference between plan and actual net income performance) is used to set the maximum EPP target. The Board feels that setting the maximum EPP target at 200% of the 2010 business plan is a stretch and reflects superior performance.

The Board wanted to ensure that the threshold target would be set higher than the financial plan and there would be an appropriate spread between threshold and maximum. In 2009, the Board Compensation Committee modeled several scenarios to arrive at threshold being 57.7% of maximum. The 2009 EPP maximum was set at 230% of plan based on the 3-year rolling average calculation and a 100% spread between threshold and maximum was determined to be reasonable which represented 57.7% of maximum. To maintain a consistent methodology, 57.7% of maximum was used in 2010 to establish the 2010 threshold EPP target.

EPP Net Income Formula:				
	2007	2008*	2009	2010
Net Income Plan	$ 80,400,000	$ 50,500,000	$ 63,600,000	$ 47,400,000
Actual Net Income	$ 169,900,000	$ 122,300,000	$ 93,019,836	
% of Plan	211%	242%	146%	
3 yr. Average			200%	
Maximum Payout Goal				200%
				$ 94,800,000
Midpoint				157.5%
				$ 74,655,000
Threshold Payout				115%
				$ 54,510,000

2010 Combined Ratio Targets

To establish the maximum 2010 EPP combined ratio target - the 3-year rolling average percent difference between plan and actual is 87%. 87% of the 2010 plan of 114.5% = 99.6% Maximum EPP target. Threshold is set at 110% of the maximum 99.6% which = 109.6%. Commendable = 95.7% which is the midpoint between threshold and maximum.

The same methodology to set net income is used to set combined ratio targets. Past performance (3-year rolling average percent difference between plan and actual combined ratio performance) is used to set the maximum EPP target. The Board feels that setting the maximum EPP target at 87% of the 2010 business plan is a stretch and reflects superior performance.

The Board wanted to ensure that the combined ratio threshold target would be more of a stretch than the financial plan and that there would be an appropriate spread between threshold and maximum. In 2009, the Board Compensation Committee modeled several scenarios to arrive at threshold being 110% of maximum to achieve its goal of being more difficult to attain than the financial plan and maintain a spread in the targets between threshold and maximum. To maintain a consistent methodology, 110% of maximum was used in 2010 to establish the 2010 threshold EPP target.

EPP Combined Ratio Formula:					
	2006	2007	2008	2009	2010
Plan Combined Ratio	102.6	102.9	109.4	108.8	114.5
Actual Combined Ratio	87.4	89.8	89.6	100.3	
% of Plan	85%	87%	82%	92%	
3 yr. Average			85%	87%	
Maximum Payout Goal					87%
					99.6
Midpoint					91.4%
					104.6
Threshold Payout					95.7%
					109.6

2010 Customer Satisfaction Targets

The customer satisfaction goals are established after reviewing customer satisfaction surveys over time and company performance over time. In general, EPP goals for the customer service quality survey are set in the same way other EPP goals are set: to achieve a stretch level of performance. For several years prior to 2007, goals for customer service were increased as results increased. In the last few years, however, EPP goals for customer service have remained flat because Pinnacol's customer service scores have been outstanding. Maintaining that same outstanding level of performance is considered a stretch.

Consider, for example, this statement from independent consultant K.L. Berry, given to the board in early 2007: "Pinnacol Assurance continues to score significantly above the 8.2 insurance industry benchmark for customer satisfaction established by the American Customer Satisfaction Index." Other surveys, like the J.D. Power study of auto insurers in 2009 (in which only one company, USAA, scored better than 870 on a 1000-point scale), seem to confirm that Pinnacol's performance puts it in elite company. This is backed up by feedback received regularly by Pinnacol's agents, many of whom believe Pinnacol is the best in the industry when it comes to customer service.

Because of the above, we have a very tight range of "threshold, commendable and maximum" for EPP targets. Threshold = 8.6, Commendable = 8.7, and Maximum = 8.8.

Future Changes

Changes in the methodology and formulas used for establishing Executive Performance Plan targets may be required to address prospective business changes (i.e. net income projections continue to decline and the current formula no longer incentivizes for exceeding plan). Any potential changes will be reviewed by the Board Compensation Committee. The Board Compensation Committee will submit changes to the full Board for their review and approval.

Pinnacol Assurance reserves the right to add, change, end, or suspend the Executive Performance Plan (EPP) at any time, with or without notice. The Executive Performance Plan shall not be construed as a contract of employment, nor does it restrict the right of Pinnacol Assurance to discharge the employee or the right of the employee to terminate his or her employment at any time.

PINNACOL ASSURANCE
AMENDED AND RESTATED EXECUTIVE PERFORMANCE PLAN

SUMMARY

This Executive Performance Plan ("Performance Plan") is amended and restated effective for Plan Years commencing on or after January 1, 2010 and amends and restates the Executive Performance Plan previously adopted by the Board of Directors of Pinnacol Assurance ("Board") on September 2, 2009. The Performance Plan is intended to recognize both the achievement of major company objectives and key individual and business unit objectives, measured on an annual basis. The company must achieve its annual net income objective in order for any awards to be paid.

This program appropriately emphasizes individual and group accountability for making specific contributions to Pinnacol Assurance's overall business results. Based on Board approval, the Performance Plan will be finalized and communicated to Executive Staff. A relatively short decision-result cycle should be attainable (first quarter of the following year) to determine award payout following Board approval.

PLAN DESCRIPTION

Plan Year – The Plan Year shall be a calendar year.

Performance Measures – No awards under this Performance Plan will be made or paid unless Pinnacol Assurance meets or exceeds the annual net income objective for the Plan Year, as set forth by the Board.

Eligibility – This Performance Plan will only apply to the following positions which will be considered Eligible Employees: President & CEO, Vice Presidents and Associate Vice Presidents (excluding the Vice President of Underwriting and Chief Marketing Officer and the Associate Vice President of Marketing). An Eligible Employee's participation will be based on a pro-rata calculation of the number of months of service worked in the Plan Year if that Eligible Employee has been employed at Pinnacol for less than the twelve calendar months of the Plan Year and was hired prior to October 1 of the Plan Year. An Eligible Employee who is hired on or after October 1 of a Plan Year is not eligible to participate in the Performance Plan for the year of hire.

Incentive Award Plans – Eligible Employees will have incentive award plans based on meeting major company objectives and individual and business unit objectives related to Pinnacol Assurance's annual business plan. For Vice Presidents and Associate Vice Presidents, the amount of an award under this Performance Plan, if any, is subject to the approval of the President & CEO and then ultimately the Board. For the President & CEO, the amount of an award under this Performance Plan, if any, is subject to the approval of the Board.

Determination of Payment

1. Eligible Employees Other Than the President & CEO

   The President & CEO shall make a determination as soon as practicable after the end of the Plan Year as to whether each Eligible Employee (other than the President & CEO) has met his or her individual and business unit objectives, and whether the company objectives have been met. The President & CEO shall make an initial determination as to the award that each such Eligible Employee is eligible for under this Performance Plan for the Plan Year. The Board shall then approve the amount of all awards (the date of such approval being the "Initial Determination Date" with respect to such Eligible Employees). The determination of an award by the Board as well as the decision as to whether to make any award, shall be in the sole discretion of the Board.

2. President & CEO

   The Compensation Committee of the Board shall make a determination as soon as practicable after the end of the Plan Year as to whether the President & CEO has met his individual and business unit objectives, and whether the company objectives have been met. The Board Compensation Committee shall make an initial determination as to the award that the President & CEO is eligible for under this Performance Plan for the Plan Year. The Board shall then approve the amount of the final award (the date of such approval being the "Initial Determination Date" with respect to the President & CEO). The determination of an award by the Board as well as the decision as to whether to make any such award shall be in the sole discretion of the Board.

3. Subsequent Adjustment

   The Board may increase or decrease the amount of an award subsequent to an Initial Determination Date (a "Subsequent Adjustment"), provided, however, that a Subsequent Adjustment shall only be made because of a mathematical error, an adjustment to net income as described below under "**Award Payout Calculation** - Net income calculation - **Adjustments to Net Income,**" or upon the determination of the Board that a metric or criterion used to compute an award had been determined in error. The date on which the Board approves a Subsequent Adjustment shall be a Subsequent Determination Date with respect to such Subsequent Adjustment.

4. The Initial Determination Date with respect to a Plan Year shall be on or after January 1 of the calendar year immediately following the Plan Year but no later than the May 31 of the calendar year immediately following such Plan Year. Any Subsequent Determination Date with respect to a Plan Year shall be no later than the September 30 of the calendar year immediately following such Plan Year.

Payment – Payment of an award, or of a Subsequent Adjustment that increases an award, shall be made within 2-1/2 months of the Initial Determination Date (with respect to the award) or within 2-1/2 months of the Subsequent Determination Date (with respect to the Subsequent Adjustment).

In the event that a Subsequent Adjustment reduces an award that has already been paid, Pinnacol Assurance may recoup such Subsequent Adjustment from the recipient of an award by reducing the compensation otherwise payable to such recipient within sixty (60) days of the

Subsequent Determination Date (including, but not limited to, regular compensation, bonuses, commissions, or severance pay and any amount of such Subsequent Adjustment that Pinnacol Assurance has not recouped from such compensation shall be paid by the recipient to Pinnacol Assurance on the sixtieth (60th) day following the Subsequent Determination Date. This paragraph applies whether or not such recipient has remained an Eligible Employee.

Vesting – An Eligible Employee who is not employed by Pinnacol Assurance on a Determination Date (whether an Initial or Subsequent Determination Date) forfeits all rights to an award (or an increase in an award in the case of a Subsequent Adjustment) for the Plan Year to which such Determination Date relates. An Eligible Employee who is employed by Pinnacol Assurance on an Initial or Subsequent Determination Date is fully vested in the award (or an increase in an award, in the case of a Subsequent Adjustment) granted on such date.

Allocation of Award Under Each Plan - Incentive awards will be earned as follows once the Board has determined that an Eligible Employee has met the criteria for an individual award:

	Company Objectives	Business Unit/Individual Objectives
President & CEO	80%	20%
Vice Presidents	50%	50%
Associate Vice Presidents	40%	60%

Eligible Employee's Plan Award Range (% of Base Salary)

	Threshold	Commendable	Maximum
Associate Vice Presidents	17.5%	27.5%	37.5%
Vice Presidents	20.0%	32.5%	45.0%
President & CEO	22.5%	37.5%	52.5%

Award Payout Calculation

Individual worksheets will be prepared for each Eligible Employee. Pinnacol will use the following factors in determining the amount of the award once the threshold criteria are met:

1. Company Objectives

   Annual net income, combined ratio and policyholder customer satisfaction targets will be established by the Board. Projected as well as past performance will be factored into the formula for establishing company objectives.

   A. Net income calculation
      Proposed adjustments will be documented and presented by the President & CEO to the Board Compensation Committee at the beginning of each Plan Year. The net income calculation will be based on the company's financial statements. Net income for purposes of this plan will exclude capital gains or losses from equity in the investment portfolio. Any proposed adjustments will be reviewed by the Board Compensation Committee and approved by the Board before a final award is calculated.

      Adjustments to Net Income – The final amount of net income achieved may be adjusted by unforeseen and uncontrollable items subject to Board approval as recommended by the Board Compensation Committee. These adjustments will be made to assure that net income for purposes of this Performance Plan is a fair reflection of the business performance of Pinnacol Assurance. Other unforeseen items that could impact the performance would be issues such as adverse court rulings, imposed regulatory costs and/or revenue reductions, and Board approved budget adjustments. Said items are mentioned as examples and are not intended to be exclusive, or limiting in any manner.

B. Combined Ratio will be based on the combined ratio results for insurance operations excluding structured settlements, as determined by the company's financial statements.

C. Policyholder Customer Satisfaction will be based on the "Overall Policyholder Service Quality Score" results and will not include renewal likelihood.

2. <u>Business Unit/Individual Objectives</u>

The President & CEO will establish annual business unit and individual objectives for Eligible Vice Presidents and Associate Vice Presidents. The Board will establish individual objectives for the President & CEO and Company objectives for all Eligible Employees.

3. <u>Calculation of the award incentive amount</u>

A. If the actual result is between two measurements (i.e., threshold and commendable and commendable and maximum) then the award will be linearly interpolated to match the actual result not to exceed the maximum award for that performance measure.

B. The President & CEO shall make the determination as to individual objective attainment when the attainment of such individual is dependent upon another part of Pinnacol. This will be documented and approved with the President's signature prior to an award payout. The President shall have the opportunity to present the case to the Board Compensation Committee for approval if there is a vested interest concern.

C. The President & CEO may review any additional issues or concerns regarding any award with the Board Compensation Committee prior to final award approval by the full Board.

<u>Section 409A</u>

This Performance Plan is intended to comply with Section 409A of the Internal Revenue Code of 1986, as amended, the Treasury Regulations promulgated thereunder, and any administrative guidance or judicial decisions with respect thereto ("Section 409A") and shall be construed accordingly. It is the intention of Pinnacol Assurance that payments under this Performance Plan not be subject to the additional tax or interest imposed pursuant to Section 409A. To the extent such potential payments or benefits are or could become subject to Section 409A, Pinnacol Assurance may amend this Performance Plan with the goal of giving Eligible Employees the economic benefits described herein in a manner that does not result in such tax or interest being imposed. Notwithstanding anything in this Performance Plan to the contrary, no payment to be made under this Performance Plan shall be made at a time earlier than that provided for in this Performance Plan unless such payment is (i) an acceleration of payment permitted to be made under Treasury Regulation Section 1.409A-3(j)(4) or (ii) otherwise not be subject to additional taxes and interest under Section 409A. All payments contemplated by this Performance Plan are intended to qualify as "short-term deferrals" as such term is defined in Treasury Regulation Section 1.409A-1(b)(4) and this Performance Plan shall be construed accordingly. It is the intention of Pinnacol Assurance that no person shall be considered to have a legally binding right to any award under this Performance Plan at any time prior to an Initial Determination Date that relates to an award, or, in the case of a Subsequent Determination that provides for an increase to an award, prior to such Subsequent Determination Date. Each payment described in this Performance Plan shall be a separate payment and a separately identifiable payment to the maximum extent permitted by Section 409A.

Pinnacol Assurance reserves the right to add, change, end, or suspend this Performance Plan at any time, with or without notice. This document shall not be construed as a contract of employment, nor does it restrict the right of Pinnacol Assurance to discharge the employee or the right of the employee to terminate his or her employment at any time.

Board Approved 8/4/10

Pinnacol Assurance
Executive Discretionary Bonus Program

Program Purpose:
A discretionary bonus program will provide the Board and CEO with a tool to recognize executives for extraordinary efforts (superior performance) on projects, unforeseen market conditions, etc. outside of the Executive Performance Program.

Eligibility:
The CEO, Vice Presidents and Associate Vice Presidents are eligible to receive a discretionary bonus unless they are already being compensated or rewarded for the performance or effort with another form of recognition or payment.

Maximum Annual Award Amount
- An annual pool of $180,000 is available for all bonuses paid under the Executive Discretionary Bonus Program. The total of all bonuses awarded each year shall not exceed $180,000.
- Appropriate withholding taxes and 401(k) deferrals (if executive is participating in the 401(k) program) will be deducted from the bonus amount
- The discretionary bonus is not PERA includable compensation

Guidelines for Awarding Cash Bonuses:
- An executive's actions must demonstrate an exceptional contribution towards achieving Pinnacol's strategic goals, must clearly exceed the expectations of assigned responsibilities and must fall outside the expectations of any other form of bonus plan.
- Justification must be provided explaining why the executive should be considered for a bonus award based on the impact of their actions from a time, money, resource or customer standpoint.
- Discretionary bonus must be awarded in the same calendar year as the year the performance generating the bonus occurred.

Process
- Executive must present a written justification for the bonus request to the Board or CEO. The Executive Discretionary Bonus Request form is included below.
- The CEO will inform the full Board via e-mail of his/her proposed discretionary bonus recommendations. No approval is required from the Board.
- Board members requiring additional information or who disagree with the CEO's recommendation must notify the CEO and copy the full board
- Justifications should be submitted to the Human Resources Compensation Manager or Human Resources VP to trigger the processing of the bonus.
- Bonus information should not be communicated to the employee prior to the check being processed.

Budget
There is no formal budget for this program as the dollar impact is minimal.

Executive Discretionary Bonus Request

Employee Name ____

Bonus Amount Requested $______________ **(after tax)**

Describe Reason for Award (Describe the extraordinary performance, the tie to Pinnacol's strategic goals and the impact or ROI) :

Requested By____ **Date**__________________

Date Check Needed: __________________________

PINNACOL
ASSURANCE

7501 E. Lowry Blvd
Denver, CO 80230-7006
www.pinnacol.com

July 20, 2010

Legislative Audit Committee
200 East 14th Avenue
Denver, CO 80203-2211

RE: Pinnacol Assurance LAC Follow-up Questions

To the Legislative Audit Committee:

At the June 7, 2010 Legislative Audit Committee hearing, there were four questions by the Committee Members. Pinnacol has provided responses to these questions, as follows:

1) Information on the gainsharing payouts made to claims personnel vs. other employees.

   Response: This is our best estimate based on manual calculations.
   Gainsharing Request: Claims Staff vs. All Employees

2008

	Avg Headcount	Total Gainsharing
Claims Staff	110	$950,380
All Employees	609	$5,876,311

2009

	Avg Headcount	Total Gainsharing
Claims Staff	106	$870,496
All Employees	618	$5,558,619

2) How many current employees are PERA-vested (i.e. more than 5 years of service)?

   Response: 383 out of 605 (63.3%) employees have five or more years of service.

3) What percentage of claims are denied in the first 20 days by the automated system vs. by a claim rep?

   Response: The automated system does not deny claims. 100% of claim denials are done by claims representatives. Pinnacol received about 48,539 claims in 2009. Of those, 2,559 were denied. Almost 37,000 claims were paid and no admission was required. Pinnacol admitted on 4,168 claims. This activity was within the first 20 days. These numbers can change after 20 days.

4) What other state funds have Change in Control Agreements?

<u>Response</u>: Within the American Association of State Compensation Insurance Funds (AASCIF), there are eighteen non-state agency funds that operate in a competitive environment similar to Pinnacol Assurance. Among these workers' compensation organizations, over 40% of them have executive severance agreements to compensate executives when a termination occurs that is without cause or for good reason to accommodate situations beyond the employer/employee's control. Within the context of executive severance agreements, Pinnacol Assurance and at least one other AASCIF fund have also addressed a potential sale of company or hostile takeover with the addition of change in control agreements. Based on recent attempts to propose legislation to either sell Pinnacol outright or dramatically alter the structure of the company by usurping surplus, Pinnacol's Board has approved executive change in control agreements so that if a change in control occurs, the Company's ability to serve its policyholders and injured workers will not be adversely impacted. Both a change in control and termination without cause or for good reason must occur for executives to receive this type of payment.

Please let us know if you have any additional questions. We look forward to hearing from you regarding the September Legislative Audit Committee hearing.

Sincerely,

Kathy Kranz, CPA
Controller

Summary of Stipulation Issued by the Division of Insurance

In the *Pinnacol Assurance Performance Audit, May 2010*, the Office of the State Auditor (OSA) reported findings regarding the rate setting practices used by Pinnacol Assurance (Pinnacol) and Pinnacol's filing of rating information with the Colorado Division of Insurance (Division) as required by statute and rule. These findings cited concerns about whether Pinnacol's rate-setting processes resulted in rates that were fair, adequate, and not excessive. Chapter 3 of the audit report included four recommendations for Pinnacol to improve its rate-setting processes and its filings with the Division.

On August 24, 2010, the Division and Pinnacol entered into a Stipulation for Entry of Final Agency Order, which is attached here, that addressed rating issues that were still outstanding as of that date. The Stipulation and Order included the following agreements:

1. Pinnacol will discontinue the practice of using the Standard tier Loss Cost Multiplier to determine a policy's eligibility for Schedule Ratings. Instead, Pinnacol will file a new process with the Division, effective January 1, 2011, to use the Loss Cost Multiplier of the tier in which the policy is issued to determine Schedule Rating eligibility. *This change implements Recommendation No. 7 of our audit report, effective 1/1/2011.*

2. Pinnacol will discontinue the use of the loss history and financial history factors in its Schedule Rating plan and will file this change with the Division effective January 1, 2011. *This change addresses Recommendation No. 8 of our audit report, effective 1/1/2011.*

3. Pinnacol will pay $15 million from its surplus finds to policyholders as credits against future premiums due to the use of unfiled Schedule Rating factors between 2002 and 2009. In addition, Pinnacol will pay $80,000 in civil penalties related to this issue. *Both Recommendation Nos. 7 and 8 of our audit cited problems regarding Pinnacol's filing of rating information with the Division.*

BEFORE THE DIVISION OF INSURANCE, STATE OF COLORADO

Division File Nos. 247459 & 247654
Final Agency Order No. O-11-035

STIPULATION FOR ENTRY OF FINAL AGENCY ORDER

IN THE MATTER OF PINNACOL ASSURANCE WORKER'S COMPENSATION RATE FILING OF DECMBER 21, 2009, SERFF #12627785 AND PINNACOL ASSURANCE WORKER'S COMPENSATION RATE FILING OF DECEMBER 28, 2009, SERFF #126433053 AND RATE HEARING SET FOR AUGUST 25, 2010

THE State of Colorado Division of Insurance ("Division") and Pinnacol Assurance ("Pinnacol"), hereby enter into this Stipulation for Entry of Final Agency Order ("Stipulation") to resolve the matters at issue in Division File Nos. 247459 and 247654, the above referenced rate filings, and the hearing set for August 25, 2010 regarding rate matters, and do hereby stipulate and agree as follows:

1. Pinnacol is a quasi-government agency with a primary purpose of providing workers compensation insurance to workers and employers in Colorado.

2. The Colorado Commissioner of Insurance ("Commissioner") and the Division have jurisdiction over Pinnacol and the subject matter herein pursuant to Title 10, C.R.S., including Article 4 of Title 10, C.R.S., and § 8-45-117, C.R.S.

3. The Division sent correspondence to Pinnacol, dated May 7, 2010, raising several issues regarding Pinnacol rate filings or unfiled rate matters. Additional issues were set forth in correspondence the Division sent Pinnacol dated July 2, 2010.

4. As of August 10, 2010 certain issues remained unresolved and, as a result, the Division filed a Notice of Hearing pursuant to §§ 10-4-418 and 24-4-105, C.R.S. setting a hearing for August 25, 2010 to address the unresolved issues. The Notice of Hearing is incorporated herein by reference as **Exhibit 1.**

5. In order to avoid the uncertainty and cost of litigation, the Division and Pinnacol have worked cooperatively to resolve all matters at issue regarding the August 25, 2010 hearing, The Division and Pinnacol hereby agree to the following:

a. **With respect to Issue #1 as set out in the Notice of Hearing,** the Division and Pinnacol agree that Pinnacol will be permitted to maintain $10,000.00 as the minimum premium for an insured to qualify for scheduled rating.

b. **With respect to Issue #2 as set out in the Notice of Hearing,** the Division and Pinnacol agree that Pinnacol will change its current practice of using the standard tier loss cost multiplier for all policy classifications in determining scheduled rating eligibility. The Division and Pinnacol agree that Pinnacol will use the loss cost multiplier applicable to each policy classification in determining scheduled rating eligibility on a prospective basis, in a manner that remains revenue neutral to the schedule rating plan. Pinnacol will file this change with the Division with an effective date of January 1, 2011.

c. **With respect to Issue #3 as set out in the Notice of Hearing,** the Division and Pinnacol agree that Pinnacol will discontinue using loss history and financial history as schedule rating factors in its scheduled rating plan. Pinnacol will file this change with the Division with an effective date of January 1, 2011.

d. **With respect to Issue #4 as set out in the Notice of Hearing,** Pinnacol used unfiled rating factors in its scheduled rating plan for the years 2002 to 2009. Therefore, Pinnacol agrees to pay fifteen million dollars ($15,000,000.00) from its surplus funds to policy holders as a credit, over a period of one year, commencing January 1, 2011. The fifteen million dollars ($15,000,000.00) shall be credited pro rata to each Pinnacol policy holder, who is schedule rated, in that policy holder's next policy period occurring after January 1, 2011. The fifteen million dollars ($15,000,000.00) credit shall be applied to each policyholder's calculated premium and shall be based on a ratio of the total credit to the total expected premium for 2011. The parties acknowledge that the credit may exceed fifteen million dollars ($15,000,000.00) but under no circumstances will it be less than fifteen million dollars ($15,000,000.00).

e. **With respect to Issue #4 as set out in the Notice of Hearing,** Pinnacol also agrees to pay an eighty thousand dollar ($80,000.00) civil penalty within thirty (30) days of the date of issuance of the Final Agency Order accepting this Stipulation. Pinnacol shall be assessed a 10% surcharge on the civil penalty, which surcharge will be due and paid to the Division by Pinnacol at the time the civil penalty is paid by Pinnacol to the Division. The surcharge is assessed pursuant to § 24-34-108, C.R.S. and will be used to fund the development, implementation and maintenance of consumer outreach and education.

f. Pinnacol agrees that when any monies are paid to policy holders as a credit pursuant to paragraph 4(d) above, an invoice or other document identifying the credit shall be sent to the policy holders, advising the policyholders that the credit is being paid as a result of the settlement with the Division regarding a rate filing matter.

g. Pinnacol waives its rights to a hearing regarding the Notice of Hearing and all rights it may have to appeal the Final Agency Order approving this Stipulation.

h. Pinnacol agrees to withdraw its August 13, 2010 open records request.

i. The public hearing scheduled for August 25, 2010 shall be vacated.

6. By entering into this Stipulation, Pinnacol knowingly and voluntarily waives its rights pursuant to §§ 10-4-418, and 24-4-104, 105 and 106, C.R.S., including but not limited to, a hearing in this matter; the right to be represented at such hearing by counsel chosen and retained by Pinnacol; the right to present a defense, oral and documentary evidence, and cross-examine witnesses at such hearing; and the right to seek judicial review of this Stipulation and the Final Agency Order approving this Stipulation.

7. The Division and Pinnacol agree that this Stipulation is a full and final settlement of the issues raised in the Notice of Hearing or that could have been raised at the August 25, 2010 hearing.

8. Neither this Stipulation or the Final Agency Order approving this Stipulation shall be deemed in any manner to prevent the Division from commencing any other agency action relating to any other conduct of Pinnacol not settled herein, and without regard to whether such conduct occurred prior to the date of this Stipulation or the Final Agency Order approving this Stipulation.

9. Pinnacol understands and acknowledges the Division may take such lawful steps as may be required or appropriate to investigate and determine whether Pinnacol is in compliance with the Stipulation and the Final Agency Order approving this Stipulation, and take any action it deems appropriate to enforce compliance with the terms of the Stipulation and Final Agency Order.

10. In the event the Division takes action relating to alleged violations of this Stipulation or Final Agency Order approving this Stipulation, said Stipulation and Final Agency Order shall be admissible in full in that proceeding for any purpose.

11. Respondent enters into this Stipulation freely and voluntarily, after having the opportunity to consult with counsel of its choice, and with full understanding and acceptance of the legal consequences of this Stipulation and the Final Agency Order approving this Stipulation.

12. Pinnacol understands that this Stipulation and the Final Agency Order approving this Stipulation shall be reported to the National Association of Insurance Commissioners pursuant to §§ 10-2-416(5)(e) and 10-2-803(2), C.R.S.

13. Invalidation of any provision of this Stipulation or the Final Agency Order approving this Stipulation by a court of competent jurisdiction will in no way affect any other provisions, which shall remain in full force and effect.

14. This Stipulation and Final Agency Order embodies the entire agreement between Pinnacol and the Division, and there are no agreements, understandings, representations or warranties that are not expressly set forth herein.

15. Upon the Commissioner's entry of the Final Agency Order approving this Stipulation, this Stipulation and Final Agency Order shall be a public record in the custody of the Division under the Colorado Public Records Act, § § 24-72-101, *et seq.*, C.R.S.

16. This Stipulation is subject to approval by the Commissioner or her designee, and shall become binding upon the parties hereto upon such approval. In the event the Commissioner does not approve this Stipulation, the parties shall retain all claims and defenses available to them had this Stipulation not been entered into by the parties.

PINNACOL ASSURANCE

Ken Ross

BY: Kenneth Ross

TITLE: Pres./CEO

8/24/2010

DATE

Subscribed and sworn to before me in the County of Denver, State of CO, this 24th day of August, 2010, by Johawna H. Robbins

Johawna H Robbins

NOTARY PUBLIC

My commission expires: 6/26/2014

FOR THE COLORADO DIVISION OF INSURANCE

Peggy A. B

PEGGY A. BROWN, ESQ.
Deputy Commissioner of Consumer Affairs

8/24/2010

DATE

JOHAWNA H. ROBBINS NOTARY PUBLIC STATE OF COLORADO

APPROVED AS TO FORM

SNELL & WILMER, LLP

____
TIMOTHY G. O'NEILL, # 17311
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1200 17th Street
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Denver, Colorado 80202

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BEFORE THE DIVISION OF INSURANCE, STATE OF COLORADO

Division File Nos. 247459 & 247654
Final Agency Order No. O-11-035

FINAL AGENCY ORDER

IN THE MATTER OF PINNACOL ASSURANCE WORKER'S COMPENSATION RATE FILING OF DECMBER 21, 2009, SERFF #12627785 AND PINNACOL ASSURANCE WORKER'S COMPENSATION RATE FILING OF DECEMBER 28, 2009, SERFF #126433053 AND RATE HEARING SET FOR AUGUST 25, 2010

THIS MATTER comes before Marcy Morrison, Commissioner of Insurance for the State of Colorado ("Commissioner"), upon the Stipulation for Entry of Final Agency Order between the Colorado Division of Insurance ("Division") and Pinnacol Assurance ("Pinnacol"). After reviewing the Stipulation, the Commissioner makes the following Findings and enters the following Order:

FINDINGS

1. The Commissioner has jurisdiction over Pinnacol and this matter pursuant to Title 10, C.R.S., including Article 4 of Title 10, C.R.S., and § 8-45-117, C.R.S.

2. By entering into the Stipulation, Pinnacol has waived its right to a hearing pursuant to §§ 10-4-418, and 24-4-104, 105, and 106, C.R.S.; the right to be represented at such hearing by counsel chosen and retained by Pinnacol; the right to present a defense, oral and documentary evidence, and cross-examine witnesses at such hearing; and the right to seek judicial review of this Final Agency Order.

ORDER

Based upon the foregoing and the terms of the Stipulation between the Division and Pinnacol, it is hereby ORDERED as follows:

1. Pinnacol shall pay an eighty thousand dollar ($80,000.00) civil penalty regarding Issue #4 as set out in the Notice of Hearing within thirty (30) of the date of this Final Agency Order.

2. Pinnacol shall pay a 10% surcharge on the eighty thousand dollar ($80,000.00) civil penalty, which surcharge will be due and paid to the Division by Pinnacol at the time the civil penalty is paid by Pinnacol to the Division. The surcharge is assessed pursuant to § 24-34-108, C.R.S. and

will be used to fund the development, implementation and maintenance of consumer outreach and education.

3. When any monies are paid to policy holders as a credit pursuant to paragraph 4(d) of the Stipulation, an invoice or other document identifying the credit shall be sent to the policy holders, advising the policyholders that the credit is being paid as a result of the settlement with the Division regarding a rate filing matter.

4. Pinnacol shall comply with the other requirements set out in the Stipulation.

5. In the event the Division commences an action against Pinnacol for an alleged violation of this Final Agency Order, this Final Agency Order, Stipulation, and the factual basis of this proceeding shall be admissible in any such action.

6. Pinnacol shall comply with the other requirements set out in the Stipulation.

7. The Stipulation is incorporated by reference and all its conditions, terms, and agreements are specifically made a part of this Order as though fully set forth herein.

DONE AND ORDERED this 27th day of August 2010.

Marcy Morrison

MARCY MORRISON
COLORADO INSURANCE COMMISSIONER

CERTIFICATE OF SERVICE

This is to certify that I have duly served the within STIPULATION FOR ENTRY OF FINAL AGENCY ORDER and FINAL AGENCY ORDER upon all parties herein by depositing copies of same in the United States mail, first-class postage prepaid, at Denver, Colorado, this 24th day of August 2010 addressed as follows:

Via Inter-Agency Mail:

Timothy O'neill
Snell And Wilmer, LLP
1200 Seventeenth Street, Suite 1900
Denver, Co. 80202

Todd S. Larson
Senior Assistant Attorney General
Judy L. LaBuda
Assistant Attorney General
Office of the Colorado Attorney General
1525 Sherman Street, 7th Floor
Denver, Colorado 80203

Paula

PAULA SISNEROS
Dir. of Compliance and Investigations