FILED
NOV 0 7 2013
FRANKLIN CIRCUIT COURT
SALLY JUMP, CLERK

COMMONWEALTH OF KENTUCKY
FRANKLIN CIRCUIT COURT
DIVISION II
CIVIL ACTION NO. 13-CI-1296

SHARON P. CLARK, IN HER CAPACITY AS COMMISSIONER OF KENTUCKY DEPARTMENT OF INSURANCE

PETITIONER

V.

VERIFIED PETITION FOR REHABILITATION

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION SELF INSURANCE FUND

SERVE: John Stephen Kirby
Process Agent
KSBIT Workers' Compensation Fund
260 Democrat Drive
Frankfort, KY 40601

SERVE: D. E. Narramore, Jr,
Chair
KSBIT Workers' Compensation Fund
260 Democrat Drive
Frankfort, KY 40601

RESPONDENTS

AND

KENTUCKY EMPLOYERS' MUTUAL INSURANCE

SERVE: Jon E. Stewart
Process Agent
KEMI
250 West Main Street
Suite 900

Lexington, KY 40507-1724

AND

KENTUCKY LEAGUE OF CITIES INSURANCE SERVICES ASSOCIATION

SERVE: Susan Barto
President
KLC
100 East Vine Street
Suite 800
Lexington, KY 40507

SERVE: Temple Juett
Process Agent
KLC
100 East Vine Street
Suite 800
Lexington, KY 40507

*** *** ***

This action is instituted to appoint Sharon P. Clark, Commissioner of Insurance for the Commonwealth of Kentucky, as Rehabilitator of Kentucky School Boards Insurance Trust Workers' Compensation Fund; to obtain appropriate relief to protect policyholders, dependent injured workers, and the public; to approve an Assessment Plan; and, to approve the transfer of certain assets and liabilities of Kentucky School Boards Insurance Trust Workers' Compensation Fund to Kentucky Employers Mutual Insurance.

JURISDICTION, PARTIES, AND STATUTORY AUTHORITY

1. This Court has exclusive jurisdiction over this matter pursuant to KRS 304.33-040(3) and KRS 304.33-030(13).

2. The Commissioner states that she is the duly appointed and qualified Commissioner of Insurance of the Commonwealth of Kentucky.

3. Kentucky School Boards Insurance Trust ("KSBIT") was created in 1978 to provide coverage through nonprofit self-insurance funds authorized under Kentucky law. These self-insurance funds allowed school districts to combine their resources while sharing the risk. There are two separate self-insurance funds within KSBIT, both of which are in a deficit position. The two self-insurance funds are the Workers' Compensation Fund and the Property and Liability Pool. This action relates to the KSBIT Workers' Compensation Fund.

4. KSBIT Workers' Compensation Fund is a workers' compensation self-insured group authorized by KRS 342.350 and KRS 304.50-010 and defined in KRS 304.50-015.

5. Pursuant to KRS 342.803, Kentucky Employers' Mutual Insurance Authority ("KEMI") is a nonprofit, independent, self-supporting *de jure* municipal corporation and political subdivision of the Commonwealth. KEMI was created pursuant to KRS 342.803 to insure employers in the Commonwealth for workers' compensation. KEMI operates as a mutual insurance company owned by its policyholders and is the largest provider of workers' compensation insurance in Kentucky. KEMI has demonstrated sufficient financial capacity to accept the transfer of certain assets and liabilities of KSBIT Workers' Compensation Fund as described herein.

6. Pursuant to KRS 342.813(4), KEMI may reinsure any risk or part of any risk.

7. Pursuant to KRS 304.50-135(6), the Commissioner has the authority to approve bulk reinsurance or any other transfer of business if she determines it to be in the best interests of the KSBIT Workers' Compensation Fund's members and their employees.

8. KEMI is an indispensable party to this action because, as set forth herein, complete relief cannot be granted without it.

9. Kentucky League of Cities Insurance Services Association ("KLC") is an unincorporated association created by Interlocal Agreement dated 1987. KLC is an indispensable party to this action because there is an actual and justiciable controversy between it and the Petitioner and, as set forth herein, complete relief cannot be granted without it.

10. Pursuant to KRS 304.50-010, *et seq.*, the Commissioner and the Kentucky Department of Insurance have regulatory authority over workers' compensation self-insured groups such as KSBIT Workers' Compensation Fund.

11. Pursuant to KRS 304.33-140 and KRS 304.50-135, the Commissioner may apply by verified petition to the Court for an order directing the Commissioner to rehabilitate a domestic insurer domiciled in the Commonwealth when the Commissioner has reasonable cause to believe that the insurer is insolvent or that assets are endangered in an amount threatening the solvency of the insurer, and where the insurer is in such condition that the further transaction of business would be hazardous, financially or otherwise, to its policyholders, its creditors, or the public. KSBIT Workers' Compensation Fund is deemed an "insurer" pursuant to KRS 304.33-030(4) and KRS 304.33-020(11).

12. For the reasons set forth herein, the Commissioner respectfully submits that the entry of an Order of Rehabilitation against KSBIT Workers' Compensation Fund is both justified and necessary.

BACKGROUND

13. KSBIT Workers' Compensation Fund has been operating for several years in a deficit position.

14. Restating KSBIT Workers' Compensation Fund's audited financial statements using a "hindsight approach" demonstrates that KSBIT Workers' Compensation Fund entered into a deficit position, from which it never emerged, as of July 1, 1997.

15. The Kentucky League of Cities, Inc. ("KLC, Inc.") began administering the KSBIT Workers' Compensation Fund on January 1, 2010, which resulted in the transfer of responsibility for claims handling and loss control administration to KLC.

16. Pursuant to KRS 304.24-300, KLC loaned $5,500,000 in the form of a "Kentucky Surplus Note" to address the estimated deficit of KSBIT Workers' Compensation Fund. The Kentucky Surplus Note did not eliminate the deficit. The Kentucky Surplus Note simply addressed the deficit from a regulatory perspective.

17. Despite KLC, Inc.'s assistance, KSBIT Workers' Compensation Fund's financial condition did not improve.

18. According to the Independent Audit Report for years ended June 30, 2013 and 2012, prepared by Dean Dorton Allen Ford, PLLC, KSBIT Workers' Compensation Fund had a total net deficit of $37,089,129. KSBIT Workers' Compensation Fund's Statement of Net Deficit for those years as prepared by its independent auditor is attached as Exhibit A.

19. KSBIT Workers' Compensation Fund has taken a number of steps to address the fund's deficit. In addition to KLC, Inc.'s assistance, the fund cut operating costs, attempted to rebuild market share, shifted to a managed care model to reduce medical costs, and increased premium rates. However, the fund's deficits continued to grow. KSBIT Workers' Compensation Fund ceased accepting new or renewal business as of June 30, 2013.

20. In sum, despite years of work to eliminate KSBIT Workers' Compensation Fund's deficit, the deficit has significantly increased.

ORDER OF REHABILITATION

21. Based upon all information available, the Commissioner has concluded that KSBIT Workers' Compensation Fund's deficit is a severe threat to the solvency of the fund; that KSBIT Workers' Compensation Fund is in such condition that the further transaction of business would be hazardous, financially or otherwise, to its policyholders, dependent injured workers, and to the public; and, that the fund is in a hazardous financial condition.

22. Accordingly, and pursuant to KRS 304.33-150, the Commissioner requests that she and her successors be appointed as the Rehabilitator of KSBIT Workers' Compensation Fund.

23. The Commissioner further requests that she be bestowed with all authority and powers of a Rehabilitator as provided by KRS 304.33, including, but not limited to, confirmation that the Rehabilitator:

(a) has all the powers of the directors, officers, and managers of KSBIT Workers' Compensation Fund, whose authority shall be suspended, except as they are re-delegated by the Rehabilitator;

(b) may direct, manage, hire and discharge employees subject to any contract rights they may have;

(c) may deal with the property and business of the insurer;

(d) has the exclusive authority to prosecute any action that exists on behalf of members or policyholders of KSBIT Workers' Compensation Fund against any director or officer of KSBIT Workers' Compensation Fund or any other person or entity;

(e) shall take possession of the assets of KSBIT Workers' Compensation Fund as soon as possible and to administer them under the general supervision of this Court;

(f) may prepare a plan for the reorganization, consolidation, conversion, reinsurance, merger, or other transformation of KSBIT Workers' Compensation Fund;

(g) is authorized to employ and fix the compensation of any special deputy rehabilitators, counsel, clerks, and assistants, all of whom shall serve at the pleasure of the Rehabilitator;

(h) may pay all expenses of taking possession of KSBIT Workers' Compensation Fund and other costs and expenses of the administration of this proceeding; and,

(i) may pay such compensation and other costs and expenses of administration out of the funds or assets of KSBIT Workers' Compensation Fund.

24. Pursuant to her powers as Rehabilitator, the Commissioner requests and nominates as Special Deputy Rehabilitator, Joseph N. Pope, Jr.

25. Pursuant to KRS 304.33-160, the Rehabilitator is authorized and directed to take such action respecting pending litigation as she considers necessary in the interests of justice and for the protection of policyholders and the public, and to consider all litigation pending outside Kentucky and to petition the courts having jurisdiction over that litigation for stays whenever necessary to protect KSBIT Workers' Compensation Fund.

26. Pursuant to KRS 304.33-170, all courts in Kentucky before which any action or proceeding in which KSBIT Workers' Compensation Fund is a party or is obligated to defend a party is pending shall immediately stay that action for such time as is necessary for the Rehabilitator to obtain proper representation and prepare for further proceedings.

LOSS PORTFOLIO TRANSFER

27. The Commissioner has determined it to be in the best interests of KSBIT's policyholders, dependent injured worker claimants, and the public to identify a financially sound and capable insurer to whom certain of KSBIT Workers' Compensation Fund's assets and liabilities could be transferred. KRS 304.50-135(6).

28. KEMI is the largest provider of workers' compensation insurance in Kentucky, and is an insurer to many former members of KSBIT Workers' Compensation Fund for their workers' compensation coverage.

29. KEMI has agreed to enter into a loss portfolio transaction with the Rehabilitator, subject to certain terms and conditions. A Loss Portfolio Transfer Agreement ("LPT Agreement") is attached as Exhibit B.

30. A loss portfolio transfer is a transaction pursuant to which loss obligations are ceded to a reinsurer in return for a payment from and/or a transfer of assets of the ceding entity.

31. The LPT Agreement with KEMI was prepared in accordance with KRS 304.33-160(5), which authorizes plans for reorganization, conversion, consolidation, reinsurance, merger, or other transformation of an insurer.

32. Having conducted independent due diligence of the financial strength of KEMI, the Department of Insurance and the Commissioner have determined that the LPT Agreement with KEMI is the best option for the protection of KSBIT Workers' Compensation Fund's policyholders and dependent injured worker.

33. The Commissioner represents that KEMI has demonstrated through negotiations with the Department of Insurance its ability to address the difficult financial condition of KSBIT Workers' Compensation Fund.

34. The LPT Agreement with KEMI allows for a comprehensive and integrated plan of rehabilitation for KSBIT Workers' Compensation Fund. Additionally, the LPT Agreement provides full coverage of claims for KSBIT Workers' Compensation Fund's policyholders.

35. Under the LPT Agreement, the Commissioner, as Rehabilitator, will transfer to KEMI, *inter alia*:

(a) all binders, contracts, certificates, and other obligations of workers' compensation coverage issued by KSBIT Workers' Compensation Fund to its members prior to June 30, 2013, together with the liability to pay all losses covered by the contracts of coverage to all KSBIT Workers' Compensation Fund members;

(b) all rights, title, and interests of KSBIT and KSBIT Workers' Compensation Fund in all excess insurance policies and policies of reinsurance related to the KSBIT Workers' Compensation Fund; and,

(c) all accounting, actuarial and financial records, contract records, litigation files, claim files, correspondence, books, documents and information of KSBIT and KSBIT Workers' Compensation Fund related to contracts of coverage, transferred claims, and excess insurance policies.

36. In consideration for KEMI's acceptance of the contracts of coverage and the attendant liabilities, and pursuant to the terms and conditions of the LPT Agreement, the Rehabilitator will pay or transfer to KEMI the amount of $35,000,000 (the "Transfer Payment").

37. Pursuant to KSBIT Workers' Compensation Fund's Self-Insurance Agreement with its members, and pursuant to KRS 304.50-055, the Rehabilitator will assess KSBIT Workers' Compensation Fund members, in a manner that is fair and equitable and as approved by the Court, an aggregate amount necessary to pay the Transfer Payment to KEMI and such other liabilities and obligations of KSBIT Workers' Compensation Fund as the Rehabilitator deems appropriate.

38. To secure the payment of the Transfer Payment, the Rehabilitator, Kentucky Department of Education, and Kentucky Finance and Administration Cabinet would agree to a memorandum of understanding respecting the intercept of state funds to pay the assessments owed by any individual school board, all as discussed below, and the Rehabilitator would grant KEMI a first and prior security interest in lien in its assessments receivable, certain installment payment agreements to be entered by individual school boards not paying their assessment in full and the accounts into which the collected assessments are deposited

39. KEMI understands the financial pressures placed upon KSBIT Workers' Compensation Fund members and is working diligently with the Commissioner and the Department of Insurance to assist those members and the Commonwealth. Therefore, the amount to be paid or transferred to KEMI for its acceptance of KSBIT Workers' Compensation Fund's liabilities and obligations is to cover the believed value of those liabilities and obligations. In other words, the proposed assessment does not include a stated or intended profit to KEMI.

ASSESSMENT PLAN

40. The Rehabilitator must assess KSBIT Workers' Compensation Fund members to remedy the fund's deficit and to fund the LPT Agreement with KEMI. A copy of the assessment plan is attached hereto as Exhibit C.

41. The Rehabilitator intends to assess KSBIT Workers' Compensation Fund members as follows:

(a) Pursuant to KRS 304.50-015(11) and (12), a self-insured group deficit is defined to exist when "assets are insufficient to enable the group to discharge its legal liabilities."

(b) Restating KSBIT Workers' Compensation Fund's audited financial statements using a "hindsight approach" demonstrates that KSBIT Workers' Compensation Fund entered into a deficit position, from which it never emerged, as of July 1, 1997.

(c) Accordingly, only those members of KSBIT Workers' Compensation Fund from January 1, 1997 to June 30, 2013 are subject to the assessment.

42. Pursuant to the Rehabilitator's assessment plan, each assessed member may elect to pay its individual assessment in one of the following manners:

(a) A member may elect to pay its individual assessment in full within thirty (30) days of levying the individual assessment. Pursuant to KRS 304.50-055(9), a member may finance the payment of the assessment by issuing bonds, notes, or other obligations. Or,

(b) A member may elect to pay its individual assessment by payment of 25% of the amount of such assessment by a date certain and the balance in equal annual installments due on July 30 of each year over a period of two to six years, as the Member may elect, and a member's unpaid balance of its individual assessment may be prepaid at any time in full, without penalty.

43. Pursuant to the terms of the LPT Agreement, the Rehabilitator will diligently pursue the collection of all assessment payments. Accordingly, if any assessed member is more

than three (3) days past due on any installment payment, the Rehabilitator will commence collection of such past due installment payment pursuant to KRS 304.50-055 and KRS 160.160(5) by the intercept of any payment due to such member from the Commonwealth of Kentucky (the "Intercept").

44. Upon receipt of funds from such Intercept, the Rehabilitator will deposit the funds into the a deposit account established pursuant to the LPT Agreement, and thereafter remit such funds to KEMI with future payments of the Transfer Payment.

45. To secure the Premium and ensure the Intercept, the Rehabilitator and KEMI intend to enter with the Kentucky Department of Education and Kentucky Finance and Administration Cabinet a Memorandum of Understanding in the form attached to the LPT Agreement, and the Rehabilitator would grant KEMI a first and prior security interest in lien in its assessments receivable, certain installment payment agreements to be entered by individual school boards not paying their assessment in full and the accounts into which the collected assessments are deposited.

46. Pursuant to KRS 304.50-055(4), the assessment plan is fair and equitable and does not discriminate between members. The assessment plan funds the LPT Agreement with KEMI; ensures that KSBIT Workers' Compensation Fund's members' claims will be paid; and, alleviates risk to the public of having injured workers' claims transferred to the Commonwealth or to other carriers through additional assessments.

47. The assessment plan is a less expensive alternative to prior "novation" assessment options KSBIT Workers' Compensation Fund provided to its members.

48. The Commissioner thus respectfully submits that the LPT Agreement with KEMI, and the assessment necessary to fund that LPT Agreement, is in the best interests of KSBIT Workers' Compensation Fund, its members, dependent injured worker claimants, and the public.

SURPLUS NOTE WITH KLC DECLARATION OF RIGHTS

COUNT I

49. On January 6, 2010, and pursuant to KRS 304.24-300, KSBIT Workers' Compensation Fund and KLC entered into a $5,500,000 Kentucky Surplus Note pursuant to which KSBIT promised to repay KLC "solely out of the surplus of the Trust [KSBIT] in excess of $2,000,000 (the amount of which is referred to as the 'Minimum Surplus.')." A copy of the Surplus Note is attached hereto as Exhibit D.

50. Terms of the Surplus Note include the provision that, "The principal amount of this note shall not form a part of the Trust's [KSBIT's] statutory legal liabilities, except to the extent of its surplus in excess of the Minimum Surplus, or be the basis of any set-off."

51. Since the execution of the Surplus Note, KSBIT has not, and as a result of its discontinuation of writing new business as of July 1, 2013, never will have a surplus in excess of the Minimum Surplus.

52. Pursuant to the terms of the Surplus Note, the Commissioner's Assessment Plan does not include an amount to cover repayment of the Surplus Note.

53. KLC contends that the Surplus Note is evidence of a legal obligation presently payable by KSBIT and for which an assessment should be made.

COUNT II

54. At or about the time of the execution of the Surplus Note, KLC required that KSBIT enter into a Master Agreement (Exhibit E) whereby KLC required that it be allowed 9 of

19 seats on the KSBIT Board and also required that any matters involving the Surplus Notes be decided by a "Special Majority Vote" of at least 10 Trustees, 5 of whom must be KLC Trustees, effectively giving KLC control of the Board.

55. Despite the fact that no payment of interest was due on the Surplus Notes, the KSBIT Board, acting contrary to the interests of its membership, unlawfully caused interest to be paid on the note to KLC in the total sum of $888,853.

56. There is an actual and justiciable controversy between the Commissioner and KLC as to whether there is any obligation on the part of Commissioner to make an assessment and cause repayment of the Surplus Note, and there is a justiciable controversy as to the liability of KLC for repayment of the interest on the Surplus Notes, and these controversies form the basis of jurisdiction in this court for a declaratory judgment pursuant to Section 112(5) of the Kentucky Constitution, KRS 23A.010, and KRS 418.040.

PRAYER FOR RELIEF

1. The Commissioner requests that the Court *immediately* enter an order in the form attached hereto as Exhibit F which appoints the Commissioner and her successors in office as the Rehabilitator of KSBIT Workers' Compensation Fund, including bestowing upon the Commissioner all authority and powers of a Rehabilitator as provided by KRS 304.33, including, but not limited to, confirmation that the Rehabilitator:

(a) has all the powers of the directors, officers, and managers of KSBIT Workers' Compensation Fund, whose authority shall be suspended, except as they are re-delegated by the Rehabilitator;

(b) may direct, manage, hire and discharge employees subject to any contract rights they may have;

(c) may deal with the property and business of the insurer;

(d) has the exclusive authority to prosecute any action that exists on behalf of members or policyholders of Kentucky School Boards Insurance Trust Workers' Compensation Fund against any director or officers of Kentucky School Boards Insurance Trust Workers' Compensation Fund or any other person or entity;

(e) and, which

(i) directs the Rehabilitator to take possession of the assets of KSBIT Workers' Compensation Fund as soon as possible and to administer them under the general supervision of this Court;

(ii) directs the Rehabilitator to provide accountings to this Court at intervals as the Court may specify;

(iii) authorizes the Rehabilitator to employ and fix the compensation of any special deputy rehabilitators, counsel, clerks, and assistants, all of whom shall serve at the pleasure of the Rehabilitator; to pay all expenses of taking possession of KSBIT Workers' Compensation Fund and other costs and expenses of the administration of this proceeding; and, to pay such compensation and other costs and expenses of administration out of the funds or assets of KSBIT Workers' Compensation Fund;

(iv) authorizes the Rehabilitator to employ Joseph N. Pope as a Special Deputy Rehabilitator;

(v) authorizes and directs the Rehabilitator to take such action respecting pending litigation as she considers necessary in the interests of justice and for the protection of policyholders and the public, and to consider all litigation pending outside Kentucky and to petition the courts having jurisdiction over that litigation for stays whenever necessary to protect KSBIT Workers' Compensation Fund;

(vi) directs that any court or tribunal in Kentucky before which any action or proceeding in which KSBIT is a party or is obligated to defend a party is pending shall stay that action or proceeding for such time as is necessary for the Rehabilitator to obtain proper representation and prepare for further proceedings; and,

(f) provides that this Court retain jurisdiction for such other and related relief as is appropriate.

2. The Commissioner requests that the Court, following a properly noticed hearing, enter an order in the form attached hereto as G that:

(a) approves the LPT Agreement between the Rehabilitator and KEMI and the transactions contemplated thereby, including the Intercept and grant of the security interests and liens herein and in the LPT Agreement;

(b) approves the Assessment Plan as described herein.

3. For judgment declaring that the KSBIT Worker's Compensation Fund has no obligation to cause the payment of either principal or interest on the Surplus Note, and for money damages in the sum of $888,853, together with prejudgment interest thereon, for improper collection of interest on the Surplus Note: and

4. Any and all other appropriate relief to which Petitioner may be entitled.

Respectfully and jointly submitted,

Peter F. Ervin
La Tasha Buckner
PUBLIC PROTECTION CABINET
OFFICE OF LEGAL SERVICES
Capitol Tower Plaza
500 Mero Street, 5th Floor
Frankfort, Kentucky 40601
Telephone: (502) 564-7760

and

Shaun T. Orme
General Counsel
KENTUCKY DEPARTMENT OF INSURANCE
P.O. Box 517
Frankfort, Kentucky 40602-0517
Telephone: (502) 564-3630

Counsel for Sharon P. Clark, in Her Capacity as Commissioner of Kentucky Department of Insurance

VERIFICATION

I, Sharon P. Clark, Commissioner of the Kentucky Department of Insurance, affirm that the foregoing representations in the Verified Petition for Rehabilitation are true:

Sharon P. Clark

Sharon P. Clark
Commissioner
Kentucky Department of Insurance

COMMONWEALTH OF Kentucky)

)

COUNTY OF Franklin)

On this the 7th day of November, 2013, before me Deborah O. Stamper, the undersigned, **Sharon P. Clark**, did personally appear and acknowledged herself to be the Commissioner of the Kentucky Department of Insurance, and having been duly sworn executed and acknowledged this Verification.

In witness whereof I hereunto set my hand.

My Commission Expires: June 14, 2013

Deborah O. Stamper

Notary Public

CERTIFICATE OF SERVICE

I hereby certify that a copy of the foregoing **Verified Petition for Rehabilitation** was sent by first class mail to on this the 7th day of November, 2013 to the Kentucky School Boards Insurance Trust Property and Liability Fund members that are subject to the assessment.

I hereby further certify that a copy of the foregoing **Verified Petition for Rehabilitation** was sent by certified mail, return receipt requested, on this the 7th day of November, 2013 to:

Frank Papalia, Esq., Process Agent
New York Marine and General Insurance Company
412 Mt. Kemble Avenue, Ste 300C
Morristown, NJ 07960

CSC-Lawyers Incorporating Service Co., Process Agent
Liberty Mutual Insurance
421 West Main Street
Frankfort, KY 40601

CSC-Lawyers Incorporating Service Co., Process Agent
Selective Insurance Company of America
421 West Main Street
Frankfort, KY 40601

CT Corporation, Process Agent
Safety National Casualty Corporation
306 West Main Street, Ste. 512
Frankfort, KY 40601

Thomas E. Lentz, Esq., Process Agent
Midwest Employers Casualty Company
14755 North Outer Fourty Drive, Ste. 300
Chesterfield, MO 63017

President or Secretary, Process Agent
Westport Insurance Company
5200 Metcalf
Overland Park, KS 66202

CSC-Lawyers Incorporating Service Co., Process Agent
National Union Fire Insurance

421 West Main Street
Frankfort, KY 40601

CT Corporation, Process Agent
Aetna Insurance Company of Connecticut
306 West Main Street, Ste. 512
Frankfort, KY 40601

CT Corporation System, Process Agent
TIG Insurance Company
306 West Main Street, Ste. 512
Frankfort, KY 40601

Jonathan D. Kantor, Esq., Process Agent
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333 S. Wabash, 43S Avenue
Chicago, IL 60604

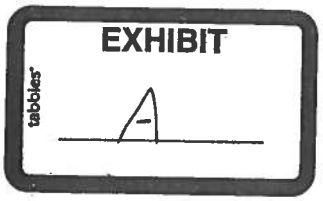
Roya L. Willis, Esq., Process Agent
MidStates Reinsurance Corporation
3495 Newmark Drive, Building 1
Miamisburg, OH 45342

Counsel for Petitioner

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND

Financial Statements and Supplementary Information

Years Ended June 30, 2013 and 2012
with Report of Independent Auditors



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DORTON

DEAN DORTON ALLEN FORD, PLLC

Report of Independent Auditors

Board of Trustees
Kentucky School Boards Insurance Trust Workers' Compensation Fund
Frankfort, Kentucky

Report on the Financial Statements

We have audited the accompanying financial statements of Kentucky School Boards Insurance Trust Workers' Compensation Fund (the Fund) which comprise the statements of net position as of June 30, 2013 and 2012, and the related statements of revenues, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kentucky School Boards Insurance Trust Workers' Compensation Fund as of June 30, 2013 and 2012, and the changes in its financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matters

Going Concern

The accompanying financial statements have been prepared assuming that the Fund will continue as a going concern. As discussed in Note 9 to the financial statements, the Commonwealth of Kentucky imposes certain asset requirements on insurance entities, including the Fund. As of June 30, 2013, the Fund's net deficit is at the Commonwealth's action level. As a result of this review, KSBIT took the following actions as part of a corrective action plan required by law:

- The KSBIT Pools ceased to accept new or renewal business after June 30, 2013 and entered into a runoff and wind up of business phase.

- KSBIT filed an assessment and wind up plan, to be approved by the Kentucky Department of Insurance, of current and past participating members to fund the deficit and the transfer of liability to a qualified insurer/reinsurer. Factors in the assessment methodology consisted of premiums paid, the projected cost claims in each pool by district, and the number of years of participation by each district in years generating a deficit.

- In early October 2013, the Department of Insurance indicated it was exploring other options for remedying the deficit and that in light of the other options, it would not approve the novation plan submitted by KSBIT. Accordingly, KSBIT withdrew its plan to transfer the obligations to a qualified reinsurer at the request of the Department. KSBIT is currently working with the Department on the other options.

Failure to meet the capital requirements and interim capital targets included in the Fund's plan would expose the Fund to regulatory sanctions that may include restrictions on operations, mandatory assessments, and placing the Fund under regulatory control. These matters raise substantial doubt about the Fund's ability to continue going as a concern. Management's plans in regard to these matters are described in Note 9. The financial statements do not include any adjustments that might result from the outcome of this uncertainty. Our opinion is not modified with respect to this matter.

Restatement

As discussed in Note 3 to the financial statements, the 2012 financial statements have been restated. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 5 - 7 be presented to supplement the basic financial statements. Such information, although not a required part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of the financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audits of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

The supplementary information on page 25 is presented for purposes of additional analysis and is not a required part of the financial statements but is supplementary information required by the Department of Insurance of the Commonwealth of Kentucky. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has not been subjected to the auditing procedures applied in the audits of the financial statements. Accordingly, it is inappropriate to and we do not express an opinion on the supplementary information referred to above.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated October 28, 2013 on our consideration of the the Fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the Fund's internal control over financial reporting and compliance.

Dean Dorton Allen Ford, PLLC

October 28, 2013
Lexington, Kentucky

Kentucky School Boards Insurance Trust Workers' Compensation Fund

Management's Discussion and Analysis (*Unaudited*)

Our discussion and analysis of the Kentucky School Boards Insurance Trust Workers' Compensation Fund (the Fund) provides an overview of the Fund's financial activity for the fiscal year ended June 30, 2013. It should be read in conjunction with the financial statements, which begin on page 7.

Using this Annual Report

This report consists of a series of financial statements, notes to the financial statements, and supplemental information.

Statements of Net Assets

The Kentucky League of Cities, Inc. (KLC) began administering the Kentucky School Board Insurance Trust (KSBIT) program on January 1, 2010, the middle of the July 2009 through June 2010 policy period. This resulted in the immediate transfer of responsibility for claims handling and loss control administration to KLC. The first underwriting and marketing responsibility for KLC relating to the KSBIT program begins with the July 2010 through June 2011 policy year. Effective January 1, 2010, The Trust, the Kentucky League of Cities Insurance Service Association (KLCIS), and the Department of Insurance agreed on a plan under which KLCIS would help KSBIT meet statutory surplus requirements for its Workers' Compensation Fund and Property and Liability Fund and KLCIS would administer the funds. On January 6, 2010, and pursuant to direction from the Department of Insurance, KSBIT and KLCIS entered into a Kentucky Surplus Note whereby KLCIS agreed to loan $5,500,000 to KSBIT's Workers' Compensation Fund and $2,500,000 to KSBIT's Property and Liability Fund, which promised to repay KLCIS out of surplus funds (see Note 8). Pursuant to direction by the Department of Insurance, the amount of each of the surplus notes was classified as net assets by the Trust under insurance law for purposes of calculating net worth and debt under GAAP accounting. In this agreement, KSBA agreed to endorse exclusively the KSBIT Workers' Compensation Fund and the Property and Liability Fund and to provide certain services to the Funds for a fee.

Table 1 shows all the assets and liabilities of the Fund and is presented on the accrual basis. The total net deficit increased $6,811,612 for the current fiscal year due to the following changes.

- The independent actuary's findings revealed $1,839,489 and $1,331,925 of prior year restatements of estimates of ultimate losses and loss adjustment expenses, respectively, due to some adverse trends and loss development.

- For the 2013 fiscal year, a reserve of $3,416,323 for unpaid loss adjustment expenses was recorded based on quotes received for third party administrative claims services in a runoff phase. The recording of this reserve in 2013 added $2,666,350 to the deficit, of which $1,331,925 relates to prior years.

- Also, the just expired 2013 policy year experienced losses that were greater than anticipated. The 2013 financial statements reflect an underwriting loss of $2,305,773 relating to adverse loss experience and legal and other professional fees associated with the proposed assessment, claims audits and expert actuarial reviews.

Table 1
Net Position

	2013	2012
Cash and investments	$ 12,412,066	$ 13,582,137
Capital and other assets	1,161,482	1,507,630
Total assets	13,573,548	15,089,767
Unpaid losses and loss adjustment expenses	42,272,642	37,352,564
Other liabilities	8,390,035	8,014,720
Total liabilities	50,662,677	45,367,284
Net position	$ (37,089,129)	$ (30,277,517)

Statement of Revenues, Expenses and Changes in Net Position

Table 2 shows the revenues and expenses of the Fund and is also presented on the accrual basis.

Table 2
Change in Net Position

Year ended June 30,	2013	2012
Net premiums earned	$ 7,365,823	$ 6,850,581
Investment and other gains (losses)	825	(156,686)
Total revenues	7,366,648	6,693,895
Losses and loss adjustment expenses	11,737,778	23,411,318
General administrative expenses	2,440,482	1,961,574
Total expenses	14,178,260	25,372,892
Change in net position	$ (6,811,612)	$ (18,678,997)

Description of Current and Expected Conditions

Despite years of work to eliminate deficits in the KSBIT pools, the latest financial statements indicated a significant increase in the deficits of both pools, which under the law requires corrective action. While KSBIT has taken a number of steps to address the pools' deficits including management and a loan by KLCIS in January 2010, cutting operating costs, attempting to rebuild market share, shifting to a managed care model to reduce medical costs, and increasing premium rates sharply, the deficits have grown as claims costs have escalated and a substantial number of districts have continued to leave the pools due to competitive pressures.

The Board of Trustees of KSBIT had claims and reserve reviews undertaken by independent outside firms to further confirm the Pools' deficits as a precedent to levying an assessment. As a result of these reviews and after consultation with the Kentucky Department of Insurance (Department), KSBIT took the following actions as part of a corrective action plan required by law:

- The KSBIT Pools ceased to accept new or renewal business after June 30, 2013 and entered into a runoff and wind up of business phase.

- KSBIT filed an assessment and wind up plan, to be approved by the Kentucky Department of Insurance, of current and past participating members to fund the deficit and the transfer of liability to a qualified insurer/reinsurer. Factors in the assessment methodology consisted of premiums paid, the projected cost claims in each pool by district, and the number of years of participation by each district in years generating a deficit.

- In early October 2013, the Department of Insurance indicated it was exploring other options for remedying the deficit and that in light of the other options, it would not approve the novation plan submitted by KSBIT. Accordingly, KSBIT withdrew its plan to transfer the obligations to a qualified reinsurer at the request of the Department. KSBIT is currently working with the Department on the other options.

- Even under the options being pursued by the Department of Insurance, it is KSBIT's understanding that a financing option negotiated by KSBA will give participating districts the choice of paying their portion of the assessment over a twenty-year period to help minimize the impact.

Contacting the Fund's Financial Management

This financial report is designed to provide a general overview of Kentucky School Boards Insurance Trust Workers' Compensation Fund's finances and to show the Fund's accountability to its members. If you have any questions about this report or need additional information, contact the Kentucky League of Cities office at 100 East Vine Street, Suite 800, Lexington, KY 40507.

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND

Statements of Net Position

June 30, 2013 and 2012

	2013	2012
Assets		
Investment securities, at fair value	$ 10,457,458	$ 9,063,482
Cash and cash equivalents	1,954,608	4,518,655
Premium receivable (net of allowance for doubtful accounts of $15,709 and $4,136 in 2013 and 2012, respectively)	141,385	160,777
Excess insurance receivable	920,100	1,124,036
Receivable from related entity	28,314	110,863
Accrued investment income	67,717	69,916
Property and equipment (net of accumulated depreciation of $8,381 and $5,911 for 2013 and 2012, respectively)	3,966	6,436
Prepaid expenses	-	35,602
Total assets	13,573,548	15,089,767
Liabilities		
Unpaid losses and loss adjustment expenses:		
Reported claims	22,367,313	23,131,510
Incurred but not reported claims	19,905,329	14,221,054
Total unpaid losses and loss adjustment expenses	42,272,642	37,352,564
Accounts payable	711,006	297,759
Surplus note payable (Note 3)	5,500,000	5,500,000
Payable to related entities (Note 3)	2,179,029	2,179,030
Advance premiums	-	37,931
Total liabilities	50,662,677	45,367,284
Net Position		
Net position (Note 3)	$ (37,089,129)	$ (30,277,517)

See accompanying notes.

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND

Statements of Revenues, Expenses and Changes in Net Position

Years ended June 30, 2013 and 2012

	2013	2012
Operating revenue:		
Net premiums earned	$ 7,365,823	$ 6,850,581
Operating expenses:		
Losses and loss adjustment expenses	11,737,778	23,411,318
Commission expense	550,405	516,159
Claims administration expense	716,127	729,302
Professional fees	574,160	170,876
Program administrative fees	510,868	492,281
Other expenses	88,922	52,956
Total operating expenses	14,178,260	25,372,892
Operating loss	(6,812,437)	(18,522,311)
Nonoperating revenue (loss):		
Interest and investment gains (losses), net	825	(156,686)
Change in net position	(6,811,612)	(18,678,997)
Net position at beginning of year, as previously reported		(3,919,490)
Restatement (Note 3)		(7,679,030)
Net position at beginning of year, as restated	(30,277,517)	(11,598,520)
Net deficit, end of year	$ (37,089,129)	$ (30,277,517)

See accompanying notes.

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND

Statements of Cash Flows

Years ended June 30, 2013 and 2012

	2013	2012
Cash flows from operating activities:		
Premiums collected	$ 7,335,712	$ 6,943,192
Losses and loss adjustment expenses paid	(6,817,701)	(6,988,392)
Underwriting expenses paid	(479,658)	(220,322)
Miscellaneous payments	(1,431,496)	(687,035)
Net cash used in operating activities	(1,393,143)	(952,557)
Cash flows from investing activities:		
Purchases of investments	(4,713,275)	(4,504,585)
Proceeds from sale and maturities of investments	3,180,783	7,176,106
Interest and dividends received	416,540	329,399
Net cash (used in) provided by investing activities	(1,115,952)	3,000,920
Cash flows from capital and financing activities:		
Change in receivable from related entity	82,548	1,607,477
Interest paid on surplus note	(137,500)	(275,000)
Net cash (used in) provided by capital and financing activities	(54,952)	1,332,477
Net (decrease) increase in cash and cash equivalents	(2,564,047)	3,380,840
Cash and cash equivalents, beginning of year	4,518,655	1,137,815
Cash and cash equivalents, end of year	$ 1,954,608	$ 4,518,655

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND

Statements of Cash Flows, continued

Years ended June 30, 2013 and 2012

	2013	2012
Reconciliation of operating loss to net cash used in operating activities:		
Operating loss	$ (6,812,437)	$ (18,522,311)
Adjustments:		
Depreciation	2,470	2,469
Allowance for doubtful accounts	11,573	5,864
Changes in assets and liabilities:		
Premium receivable	7,820	93,409
Excess insurance receivable	203,936	1,018,678
Prepaid expenses	35,602	(32,705)
Unpaid losses and loss adjustment expenses	4,920,078	16,422,926
Accounts payable	275,746	65,775
Advance premiums	(37,931)	(6,662)
Net cash used in operating activities	$ (1,393,143)	$ (952,557)

See accompanying notes.

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND

Notes to the Financial Statements

1. Nature of Organization and Operations

The Kentucky School Boards Insurance Trust (KSBIT, or the Trust) was organized by the Kentucky School Boards Association (KSBA, or the Association) effective July 7, 1978. The Trust established a Workers' Compensation Fund to provide group self-insurance coverage for Association members and their related agencies. All school districts, non-profit institutions of higher education, and other tax supported agencies of Kentucky who are members of the Association are eligible to participate.

Participating members make contributions to the Fund based upon premium rates determined by the Fund. Members may be subject to contribution assessments in the event of deficiencies in the Fund's net assets. The Fund's management considers anticipated investment income, among other things, in determining if a premium deficiency exists. Distributions of excess net assets to participants in the form of dividends may be declared by the Board of Trustees. However, under Kentucky Department of Insurance regulations, dividends may not be paid until thirty-six months after the expiration of the self-insurance term. Participation in the Fund included 80 and 89 members as of June 30, 2013 and 2012, respectively.

The Trust has also sponsored and organized a Property and Liability Insurance Fund and an Unemployment Compensation Fund.

Effective January 1, 2010, The Trust, the Kentucky League of Cities Insurance Service Association (KLCIS), and the Department of Insurance agreed on a plan under which KLCIS would help KSBIT meet statutory surplus requirements for its Workers' Compensation Fund and Property and Liability Fund and KLCIS would administer the funds. On January 6, 2010, and pursuant to direction from the Department of Insurance, KSBIT and KLCIS entered into a Kentucky Surplus Note whereby KLCIS agreed to loan $5,500,000 to KSBIT's Workers' Compensation Fund and $2,500,000 to KSBIT's Property and Liability Fund, which promised to repay KLCIS out of surplus funds (see Note 8). Pursuant to direction by the Department of Insurance, the amount of each of the surplus notes was classified as net assets by the Trust under insurance law for purposes of calculating net worth and debt under GAAP accounting. In this agreement, KSBA agreed to endorse exclusively the KSBIT Workers' Compensation Fund and the Property and Liability Fund and to provide certain services to the Funds at a fee equal to one and one-quarter percent (1.25%) of annual gross billed premiums of the Funds, but not to exceed $500,000 in any fiscal year.

Following is a description of the most significant risks facing workers' compensation insurers and how the Fund mitigates those risks:

Legal/Regulatory Risk

Legal/regulatory risk is the risk that changes in the legal or regulatory environment in which an insurer operates will occur and create additional losses or expenses not anticipated by the insurer in pricing its products. That is, regulatory initiatives designed to reduce insurer profits or new legal theories may create costs for the insurer beyond those currently recorded in the financial statements. The Fund is exposed to this risk by writing all of its business in Kentucky, thus increasing its exposure to a single jurisdiction. This risk is reduced by underwriting and loss adjusting practices that identify and minimize the adverse impact of this risk.

1. Nature of Organization and Operations, continued

Credit Risk

Credit risk is the risk that issuers of securities owned by an insurer will default or that other parties, including excess insurers that owe the insurer money will not pay. The Fund minimizes this risk by adhering to a conservative investment strategy, by utilizing financially sound excess insurers, by maintaining credit and collection policies, and by providing an allowance for any amounts deemed uncollectible.

Interest Rate Risk

Interest rate risk is the risk that interest rates will change and cause a decrease in the value of an insurer's investments. The Fund mitigates this risk by attempting to match the maturity schedule of its assets with the expected payouts of its liabilities. To the extent that liabilities come due more quickly than assets mature, an issuer would have to sell assets prior to maturity and recognize a gain or loss. The Fund uses the segmented time distribution method to measure interest rate risk.

2. Summary of Significant Accounting Policies

Basis of Accounting

The Fund uses the accrual basis of accounting. Under this method, revenues are recognized in the accounting period in which they are earned and expenses are recognized in the period incurred.

The Fund presents its financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. As a proprietary activity, the Fund has adopted GASB Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements.* Therefore, the Fund follows GASB pronouncements and all Financial Accounting Standards Board and predecessor boards' pronouncements except those that conflict with or contradict GASB pronouncements.

For 2013, the Fund implemented GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position.*

GASB Statement No. 63 identifies net position, rather than net assets, as the residual of all other elements presented in a statement of financial position. This change was incorporated in the Fund's 2013 financial statements; however, there was no effect on beginning net position/fund balance.

2. Summary of Significant Accounting Policies, continued

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and the accompanying notes. Actual results could differ from those estimates.

Material estimates that are particularly susceptible to significant change in the near-term relate to the determination of unpaid losses and loss adjustment expenses. In connection with the determination of unpaid losses and loss adjustment expenses, management uses the methodology described later in this note in "Unpaid Losses and Loss Adjustment Expenses".

Management believes that the liability for unpaid losses and loss adjustment expenses is adequate. While management uses available information to estimate unpaid losses and loss adjustment expenses, future changes to the liability may be necessary based on claims experience and changing claims frequency and severity conditions, as well as changes in doctrine of legal liability and damage awards in Kentucky. The future changes will be charged or credited to expenses when they occur.

Investment Securities

Investment securities consist of fixed maturity debt and equity securities that the Fund intends to use as part of its asset/liability management policy and securities that may be sold in response to unexpected liquidity needs.

Investment securities are stated at fair value based, generally, on quoted market prices. Changes in the fair value of investment securities are reported as revenue. The specific identification method is used to determine the cost of securities sold. Realized and unrealized gains and losses are included in non-operating revenue.

Cash and Cash Equivalents

Cash and cash equivalents consist principally of money market fund investments. For purposes of the statements of cash flows, the Fund considers all highly liquid investments with a maturity, at time of purchase, of three months or less to be cash equivalents.

Accounts Receivable

In accordance with accounting principles generally accepted in the insurance industry, the Fund records audit premiums as of the fiscal year-end in which they were earned. The allowance for doubtful accounts is an amount that management believes will be adequate to absorb possible uncollectible accounts based on prior experience. Amounts are charged against the allowance when management determines that collectability is doubtful.

2. Summary of Significant Accounting Policies, continued

Property and Equipment

Property and equipment consists of furniture and fixtures. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets. For the years ended June 30, 2013 and 2012, depreciation expense amounted to $2,470 and $2,469, respectively.

Premium Revenue

Premiums for contracts are recognized as earned on a pro rata basis over the contract period. Advance premiums relate to premiums paid by members for insurance coverage for the subsequent insurance period. Policy coverage is matched with revenue so as to result in recognition of profits over the life of the policies through establishment of reserves for incurred claims.

Unpaid Losses and Loss Adjustment Expenses

Unpaid losses and loss adjustment expenses are based on estimates of the ultimate cost of claims (including future claims adjustment expense) that have been reported but not settled, and of claims that have been incurred but not yet reported. The length of time for which such costs must be estimated varies depending on the coverage involved. Estimated amounts of subrogation and excess insurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Because actual claims cost depends on such complex factors as inflation, changes in doctrines of legal liability, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflects past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made.

Excess Insurance

Excess insurance premiums, losses, and loss adjustment expenses are accounted for on a basis consistent with those used in accounting for the original policies issued and the terms of the excess insurance contracts. Premiums, losses, and loss adjustment expenses are reported net of excess insured amounts. The Fund evaluates the financial condition of its excess insurers to minimize its exposure to significant losses from excess insurer insolvencies. The Fund holds funds and collateral as security under excess insurance agreements in the form of letters of credit for any excess insurers not subject to the regulation of the Kentucky Commissioner of Insurance. In the opinion of management, all amounts due from excess insurers at June 30, 2013 and 2012 are recoverable.

2. Summary of Significant Accounting Policies, continued

Net Position

The Fund's Board of Trustees may, at its discretion, refund to members the savings, if any, resulting from operations of the Fund in the form of dividends or reduced premiums. The amount of any future dividends or reductions in premiums is dependent on the Fund's ultimate liability for claims incurred and, accordingly, the amount may differ from the net position. No refunds were issued during 2013 or 2012.

In the event of adverse loss experience, the Fund can assess additional amounts to the members. An assessment would be computed and established by the Board of Trustees with each member's share being based on a portion of premiums and losses. There have been no assessments levied since the inception of the Fund. See Note 9 regarding a likely assessment as part of the Fund's corrective action plan.

Federal Income Taxes

The Internal Revenue Service has ruled that the income of the Fund is excludable from gross income, and therefore, exempt from taxation pursuant to Internal Revenue Code Section 115, which pertains to instrumentalities of state and local governments.

Subsequent Events

Management has evaluated subsequent events for accounting and disclosure requirements through October 28, 2013, the date that the financial statements were available to be issued. See Note 9 for management's corrective action plan and assessment of current and past participating members.

3. Restatement

During 2013, the Fund changed its accounting for $2,179,030 in funds it had previously received from related parties. During 2013, management of the Fund and related entities elected to classify the transfers as a loan. This change resulted in the net position of the Fund at July 1, 2011 being decreased by $2,179,030 via a payable to related entities of $2,179,030 being recorded. See Note 6 for additional information regarding this payable.

During 2013, the Fund changed its accounting treatment of the surplus note agreement. As directed by the Department of Insurance, management had previously recorded the surplus in net position, as opposed to a note payable. This change resulted in the net position at July 1, 2011 being reduced by $5,500,000 via a surplus note payable of $5,500,000 being recorded. See Note 8 for additional information regarding this note.

Neither of these changes in accounting had any effect on 2012's change in net position or cash flows.

4. Deposits and Investments

Deposits and investments held by the Fund as of June 30 are as follows:

	2013	2012
Deposits and investments classified as cash and cash equivalents:		
Cash and cash equivalents	$ 624,509	$ 380,763
Money market mutual funds	1,330,099	4,137,892
	1,954,608	4,518,655
Investments classified as investment securities:		
Certificate of deposit	2,257,497	2,197,167
Corporate bonds	1,570,894	1,566,579
Municipal bonds	3,912,559	2,703,912
U.S. government agency obligations	187,436	1,996,616
Common equity securities	822,136	290,459
Equity mutual funds	1,706,936	308,749
Investments classified as investment securities	10,457,458	9,063,482
Total deposits and investments	$ 12,412,066	$ 13,582,137

As of June 30, 2013, the Fund had the following investment maturities:

	Less than 1	1-5	6-10	More than 10
Certificate of deposit	$ 2,257,497	$ -	$ -	$ -
Corporate bonds	-	1,312,849	258,045	-
Municipal bonds	-	1,477,951	1,198,211	1,236,397
U.S. government agency obligations	-	-	-	187,436
Total maturities	$ 2,257,497	$ 2,790,800	$ 1,456,256	$ 1,423,833

Interest and investment gains (losses), net are comprised of the following for the years ended June 30:

	2013	2012
Interest and dividend income, net	$ 307,772	$ 329,399
Net realized and unrealized losses	(306,947)	(486,085)
	$ 825	$ (156,686)

4. Deposits and Investments, continued

Credit Risk

State law and the Fund investment guidelines assert that corporate bonds are allowable if issued, assumed, or guaranteed by a solvent institution created and existing under the laws of the United States of America. They also state that corporate bond investments shall not exceed 15% of the total market value of the portfolio at the time of purchase and that the bond has a minimum rating of A.

State law and the Fund investment guidelines assert that no individual equity holding shall comprise greater than 10% of the equity portion of the portfolio at the time of purchase. Both also state that an investment in an individual holding shall not represent at the time of purchase more than 5% of the market value of the holding. Furthermore, both state that investments in equities shall not exceed 20% of the total market value of the portfolio of the self-insurance group at the time of purchase. In addition, mutual funds that are registered investment advisors licensed by the Securities Exchange Commission and Commonwealth of Kentucky to perform investment services are allowable and shall not exceed 20% of the total market value of the portfolio at the time of purchase.

With respect to cash and statue defined bonds, both sets of guidelines state that, of the total investments held, no less than 75% of the total market value shall be held in cash, cash equivalents, and fixed income. Also, not less than 15% of the total investments shall be held in cash, cash equivalents or U.S. Treasuries and federal agency securities with a 1 year or less maturity. The Fund may also invest surplus funds or reserves not needed for current obligations in the following: U.S. government bonds, Treasury notes and T-bills or other direct obligations guaranteed by the full faith and credit of the United States of America, tax exempt obligations issued by Kentucky or its agencies with a minimum Standard and Poor (S&P) rating of A.

Furthermore, the Fund may also invest in obligations issued by a country, district, municipality or other legal authority within Kentucky with a minimum S&P rating of AA. Investments may also be made in investment share accounts in a savings and loan institution in Kentucky which is insured by the Federal Deposit Insurance Corporation. Finally, the Fund may also invest in certificates of deposit if issued by a duly chartered commercial bank in Kentucky.

As of June 30, 2013 and 2012, the Fund's management believes the Fund is in compliance with all applicable laws. As of June 30, 2013 and 2012, the Fund was invested in the following government agency bonds: Federal National Mortgage Association and Government National Mortgage Association. None of these bonds had S&P ratings. Additional investments include municipal bonds and money market accounts.

5. Excess Insurance Coverage

The Fund's Board of Trustees authorized the purchase of excess insurance coverage in order to reduce the ultimate loss exposure arising from large losses in the workers' compensation pool. The Fund purchases specific excess of loss insurance coverage for protection against losses in excess of specified amounts per occurrence. Excess insurance premiums are based upon a percentage of payrolls.

5. Excess Insurance Coverage, continued

For 2013 and 2012, the Fund purchased excess insurance coverage for the Workers' Compensation pool from New York Marine and General Insurance Company, an excess insurance carrier with a rating of "A" (Excellent) by A.M. Best and Company. The Fund purchased a buffer layer of excess insurance, defined as $1,000,000 in excess of $350,000, and $650,000 in excess of $350,000, in 2013 and 2012, respectively, as specific excess insurance coverage per occurrence.

Although the purchase of excess insurance coverage does not discharge the Fund from its primary liability to its members, the excess insurance company that assumes the coverage assumes the related liability, and it is the practice of organizations such as the Fund for accounting purposes to treat insured risks, to the extent of excess insurance coverage, as though they were risks for which the Fund is not liable. However, the Fund remains contingently liable in the event its excess insurers are unable to meet their contractual obligations.

Excess insurance premiums ceded were $1,033,552 and $1,099,301 for the years ended June 30, 2013 and 2012, respectively. Excess insurance recoveries on paid claims during 2013 and 2012 were $851,566 and $1,624,169, respectively.

6. Related Party Transactions

The following entities are the Fund's related entities:

Kentucky League of Cities (KLC)
Kentucky League of Cities Insurance Agency (KLCIA)
Kentucky League of Cities Premium Finance Company (KLCPFC)
Kentucky League of Cities Unemployment Compensation Reimbursement Trust (KLCUCRT)
Kentucky League of Cities Insurance Services Association (KLCIS)
Kentucky League of Cities Workers Compensation Trust (KLCWCT)
Kentucky School Boards Insurance Trust Property and Liability Fund (KSBITPLF)

Through December 31, 2009, the Fund occupied office space from and had an Administrative Agreement with Kentucky School Board Association (KSBA) to provide management and administrative services for the Fund. As of January 1, 2010, the KSBA agreed to endorse exclusively the Fund and to provide certain services to the Fund at a fee equal to one and one-quarter percent (1.25%) of annual gross billed premiums of the funds, but not to exceed $500,000 in any fiscal year. The amount paid to KSBA by the Fund was $98,214 and $78,206 for 2013 and 2012, respectively.

The Fund reports amounts as being due from or due to related parties. Related party receivables and payables included within the Fund's statements of net position consist of the following as of June 30:

	2013	2012
KSBIT liability fund receivable	$ 28,314	$ 110,863

6. Related Party Transactions, continued

The fund borrowed $2,179,030 from related parties in 2003. The amount is included in payable to related entities and was expected to be a temporary borrowing between the funds and is payable upon demand without interest.

7. Liability for Unpaid Losses and Loss Adjustment Expenses

Activity in the liability for unpaid losses and loss adjustment expenses for the years ended June 30, 2013 and 2012 is summarized as follows:

	2013	2012
Net unpaid losses and loss adjustment expenses, beginning of year	$ 37,352,564	$ 20,929,638
Incurred losses and loss adjustment expenses:		
Provision for insured events of the current year	8,566,364	7,260,139
Increase in provision for insured events of prior years	3,171,414	16,151,179
Total incurred losses and loss adjustment expenses	11,737,778	23,411,318
Payments:		
Losses and loss adjustment expenses attributable to insured events of the current year	1,571,103	1,829,029
Losses and loss adjustment expenses attributable to insured events of prior years	5,246,598	5,159,363
Total payments	6,817,701	6,988,392
Net unpaid losses and loss adjustment expenses, end of year	$ 42,272,641	$ 37,352,564

An increase (decrease) in the provision for insured events of prior years signifies that the Fund expects higher (lower) than anticipated ultimate losses in the final disposition of claims.

For the 2013 fiscal year, a reserve of $3,416,323 for unpaid loss adjustment expenses was recorded based on quotes received for third party administrative claims services in a runoff phase.

8. Surplus Note Agreement

On January 6, 2010, and pursuant to direction from the Department of Insurance, KSBIT and KLCIS entered into a Kentucky Surplus Note whereby KLCIS agreed to loan $5,500,000 to KSBIT's Workers' Compensation Fund and $2,500,000 to KSBIT's Property and Liability Fund, which promised to repay KLCIS out of surplus funds. Pursuant to direction by the Department of Insurance, the amount of each of the surplus notes was classified as net assets by the Trust under insurance law for purposes of calculating net worth and debt under GAAP accounting. Interest is due quarterly until each note is paid in full. Interest is calculated at a rate per annum which shall be equal to the sum of the year to date yield on the S&P Index weighted at 20% plus the year to date yield on the Bar Cap Index weighted at 80%. Provided, however, in no event shall the annual interest rate be less than 1% or greater than 5%. These notes have no fixed maturity date. KLCIS expects to recover the entire $8 million through the assessment process discussed in Note 9.

9. Going Concern Considerations and Management's Plans (*Unaudited*)

Description of Current and Expected Conditions

The Fund's financial statements are prepared on the going concern basis, which contemplates the realization of assets and the satisfaction of liabilities in the normal course of business. Due to deficits reflected in its June 30, 2011 financials and continuing to develop during 2012, the Fund determined that liabilities could not be satisfied in the ordinary course of business and that an assessment of members would be necessary to satisfy obligations and eliminate Fund deficits.

Thus, despite years of work to eliminate deficits in the KSBIT pools, the latest financial statements indicated a significant increase in the deficits of both pools, which under the law requires corrective action. While KSBIT has taken a number of steps to address the pools' deficits including management and a loan by KLCIS in January 2010, cutting operating costs, attempting to rebuild market share, shifting to a managed care model to reduce medical costs, and increasing premium rates sharply, the deficits have grown as claims costs have escalated and a substantial number of districts have continued to leave the pools due to competitive pressures.

The Board of Trustees of KSBIT had claims and reserve reviews undertaken by independent outside firms to further confirm the pools' deficits as a precedent to levying an assessment. As a result of these reviews and after consultation with the Kentucky Department of Insurance (Department), KSBIT took the following actions as part of a corrective action plan required by law:

- The KSBIT Pools ceased to accept new or renewal business after June 30, 2013 and entered into a runoff and wind up of business phase.

- KSBIT filed an assessment and wind up plan, to be approved by the Kentucky Department of Insurance, of current and past participating members to fund the deficit and the transfer of liability to a qualified insurer/reinsurer. Factors in the assessment methodology consisted of premiums paid, the projected cost claims in each pool by district, and the number of years of participation by each district in years generating a deficit.

9. Going Concern Considerations and Management's Plans (*Unaudited*), continued

Description of Current and Expected Conditions, continued

- In early October, 2013 the Department of Insurance indicated it was exploring other options for remedying the deficit and that in light of the other options, it would not approve the novation plan submitted by KSBIT. Accordingly, KSBIT withdrew its plan to transfer the obligations to a qualified reinsurer at the request of the Department. KSBIT is currently working with the Department on the other options.

- Even under the options being pursued by the Department of Insurance, it is KSBIT's understanding that a financing option negotiated by KSBA will give participating districts the choice of paying their portion of the assessment over a twenty-year period to help minimize the impact.

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DEAN DORTON ALLEN FORD, PLLC

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

Board of Trustees
Kentucky School Boards Insurance Trust Workers Compensation Fund
Frankfort, Kentucky

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Kentucky School Boards Insurance Trust Workers' Compensation Fund (the Fund) as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements, and have issued our report thereon dated October 28, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the Fund's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Dean Dorton Allen Ford, PLLC

October 28, 2013
Lexington, Kentucky

KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION FUND
Claims Development Information (*Unaudited*)
Years ended June 30, 2004 through 2013

The following table illustrates how the Association's earned premium revenue (net of excess insurance) and investment income compare to related costs of loss (net of loss assumed by excess insurers) and other expenses assumed by the Association as of the end of each of the last ten years. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's gross premium revenue and investment revenue, premium revenue ceded to excess insurers, and net earned premium revenue and reported investment revenue. (2) This line shows each fiscal year's other operating costs of the Association including overhead and claims expense not allocable to individual claims. (3) This line shows the Association's gross incurred claims and allocated claims adjustment expenses, claims assumed by excess insurers, and net incurred claims and allocated adjustment expenses (both paid and accrued) as originally reported as of the end of the first year in which the event that triggered coverage under the contract occurred (called policy year). (4) This section shows the cumulative net amounts paid as of the end of successive years for each policy year. (5) This line shows the latest reestimated amount of claims assumed by excess insurers as of the end of the current year for each accident year. (6) This section shows how each policy year's net incurred claims increased or decreased as of the end of successive years. (This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, and emergence of new claims not previously known.) (7) This line compares the latest reestimated net incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of net claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts commonly is used to evaluate the accuracy of net incurred claims currently recognized in less mature policy years. The columns of the table show data for successive policy years.

		Worker's Compensation Pool									
		Fiscal and Policy Year Ended									
		2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
(1)	Earned premium revenue and net investment income.	$ 9,962,643	$ 4,958,578	$ 9,020,633	$ 8,391,837	$ 7,251,756	$ 7,034,681	$ 6,170,242	$ 7,153,122	$ 6,968,894	$ 7,641,648
(2)	Unallocated expenses	736,210	616,882	1,443,560	1,380,326	1,488,346	1,482,629	1,752,663	2,269,011	2,236,571	2,715,482
(3)	Estimated incurred claims and expenses, end of policy year.	8,087,551	6,983,506	5,948,837	7,571,681	6,940,511	7,380,489	7,754,599	9,054,058	9,227,287	7,231,939
(4)	Net paid (cumulative) as of										
	End of policy year	2,052,257	1,099,844	1,561,970	1,997,667	1,605,821	1,677,731	1,713,699	2,270,791	1,829,029	1,571,103
	One year later	2,435,462	1,497,402	3,054,706	3,377,049	2,995,074	3,172,213	4,100,918	4,613,029	3,782,061	
	Two years later	4,027,167	2,066,701	3,842,688	4,305,647	3,723,496	4,494,415	4,772,232	5,498,790		
	Three years later	4,854,236	2,427,154	4,216,666	4,844,705	4,403,788	4,842,416				
	Four years later	5,370,366	2,570,146	4,564,526	5,067,522	4,516,733	5,116,353				
	Five years later	5,633,095	5,213,890	4,382,891	5,253,231	4,664,135					
	Six years later	6,207,942	5,713,726	4,430,544	5,422,845						
	Seven years later	6,410,585	5,807,476	4,498,163							
	Eight years later	6,546,455	5,850,497								
	Nine years later	6,692,652									
(5)	Reestimated ceded claims and expenses	-	-	-	-	-	-	-	-	-	-
(6)	Reestimated net incurred claims and expenses:										
	End of policy year	8,523,959	3,050,098	6,737,475	7,188,912	6,580,883	6,280,149	6,111,815	7,260,139	8,697,955	7,231,939
	One year later	8,531,642	3,336,863	6,415,393	6,823,373	5,672,366	6,413,224	6,131,030	9,282,038	9,227,287	
	Two years later	7,988,934	3,408,718	5,882,910	6,459,344	5,897,951	6,503,962	7,353,418	9,054,058		
	Three years later	7,944,695	3,450,446	5,787,434	6,882,232	6,154,515	7,454,983	7,754,599			
	Four years later	7,986,005	3,511,626	6,358,315	6,853,386	6,881,957	7,380,489				
	Five years later	7,979,903	6,949,924	5,820,017	7,535,658	6,940,511					
	Six years later	8,162,566	6,955,274	5,885,941	7,571,681						
	Seven years later	8,156,881	6,825,098	5,948,837							
	Eight years later	8,025,806	6,983,506								
	Nine years later	8,087,551									
(7)	Increase (decrease) in estimated net incurred claims and expenses from the end of the policy year	(436,408)	3,933,408	(788,638)	382,769	359,628	1,100,340	1,642,784	1,793,919	529,332	-

See report of independent auditors.

LOSS PORTFOLIO TRANSFER AGREEMENT

This Loss Portfolio Transfer Agreement (this "Agreement"), is dated as of _____ __, 2013, and by and between **SHARON P. CLARK, COMMISSIONER OF THE KENTUCKY DEPARTMENT OF INSURANCE, IN HER CAPACITY AS REHABILITATOR OF THE KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION SELF-INSURANCE FUND** (the "Rehabilitator") and **KENTUCKY EMPLOYERS' MUTUAL INSURANCE** ("KEMI"). The Rehabilitator and KEMI are, collectively, the "Parties" and each a "Party".

RECITALS

A. The Kentucky School Boards Insurance Trust Workers' Compensation Self-Insurance Fund (the "Fund"), is a fund pursuant to which participating members of the Kentucky School Boards Insurance Trust ("KSBIT") pooled their liabilities as a workers' compensation self-insured group under Kentucky Revised Statutes ("KRS") 304.50-005, *et. seq.*

B. As a result of a petition (the "Petition") filed with the Franklin Circuit Court, Commonwealth of Kentucky ("the "Court") on _____ ___, 2013, pursuant to KRS 304.33-140 and KRS 304.50-135, the Rehabilitator has sought, *inter alia*, (i) to be appointed rehabilitator of the Fund and (ii) an order of the Court approving entering this Agreement and consummating the transactions contemplated hereby.

C. KEMI is a nonprofit, independent, self-supporting *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky created pursuant to KRS 342.803, *et. seq.*, and, as such, has the authority to reinsure any risk.

D. Subject to the terms and conditions of this Agreement, including approval of the Court, the Rehabilitator and KEMI have agreed that the Rehabilitator will assess the Fund's members to fund the Fund's deficit and transfer certain liabilities of the Fund to KEMI and pay KEMI the premium contemplated herein.

NOW THEREFORE, in consideration of the mutual representations, warranties, covenants and agreements set forth herein, the receipt and sufficiency of which are hereby acknowledged, the Rehabilitator and KEMI agree as follows:

ARTICLE 1 - DEFINITIONS

1.1 Definitions. Capitalized terms used in this Agreement shall have the meanings set forth in Addendum "A" attached hereto.

1.2 Rules of Interpretation.

(a) The singular includes the plural and the plural includes the singular.

(b) The word "or" is not exclusive.

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(c) A reference to a Person includes its permitted successors and permitted assigns.

(d) The words "include," "includes" and "including" are not limiting.

(e) A reference in this Agreement to an Article, Section, Exhibit, Schedule, Annex or Appendix is to the Article, Section, Exhibit, Schedule, Annex or Appendix of this Agreement unless otherwise indicated. Exhibits, Schedules, Annexes or Appendices to this Agreement shall be deemed incorporated by reference into this Agreement and made a part hereof.

(f) The words "hereof," "herein" and "hereunder" and words of similar import when used in any document shall refer to such document as a whole and not to any particular provision of such document.

(g) The phrase "to the knowledge of" and similar phrases relating to knowledge of (i) the Fund or Rehabilitator as to a particular fact or other matter shall be deemed to exist if (A) any of those persons listed on Schedule 1.2(g) of the Fund Disclosure Schedule is actually aware of such fact or other matter or (B) a prudent individual in such listed person's position with the Fund or Rehabilitator, should reasonably be expected to be aware of such fact or other matter in the course of performing the duties of such position; and (ii) KEMI as to a particular fact or other matter shall be deemed to exist if (A) any of those persons listed on Schedule 1.2(g) of the KEMI Disclosure Schedule is actually aware of such fact or other matter or (B) a prudent individual in such listed person's position with KEMI should reasonably be expected to be aware of such fact or other matter in the course of performing the duties of such position.

ARTICLE 2 – TRANSFER OF PORTFOLIO; TRANSFER PAYMENT

2.1 Transfer of Portfolio; Assumption of Liabilities.

(a) Upon the terms and subject to the conditions contained in this Agreement and the Related Agreements, including the payment of the Transfer Payment and assignment of the Subrogation Rights and Excess Policies, at the Closing, the Rehabilitator shall sell, assign, transfer and convey to KEMI, and KEMI shall acquire, assume and accept from the Rehabilitator the following (the "Portfolio"):

(i) all binders, contracts, certificates and other obligations of the workers' compensation and employer's liability insurance coverage issued by the Fund to its Members prior to June 30, 2013 and identified on Schedule 2.1(a)(i) hereto (the "Contracts of Coverage"), together with the liability to pay all losses, including loss adjustment expenses, covered by the Contracts of Coverage to Members, including all existing and incurred but not reported ("IBNR") claims covered by the Contracts of Coverage and Ordinary Course Claims pending upon the Effective Date (collectively, the "Transferred Claims");

(ii) all rights of the Fund and KSBIT against any Person legally responsible for any loss paid by the Fund or KEMI, including, without limitation, all rights of subrogation,

contribution, payment of retention or deductibles or indemnification by a third party ("Subrogation Rights"), including, without limitation the Subrogation Rights identified on Schedule 2.1(a)(ii);

(iii) all right, title and interest of the Fund and KSBIT in all excess insurance policies and policies of reinsurance related to the Fund, including those identified on Schedule 2.1(a)(iii) hereto (the "Excess Policies");

(iv) all accounting, actuarial and financial records, contract records, litigation files, claim files, other files, images, data, correspondence, books, documents and information of KSBIT and the Fund related to the Contracts of Coverage, IBNR, Transferred Claims, Excess Policies, Subrogation Rights and the Fund (the "Records"), whether in paper, electronic media or other format; and

(v) all other property necessary to managing, enforcing or defending the Contracts of Coverage, Transferred Claims, Subrogation Rights and Excess Policies.

At the Closing, the assets that constitute the Portfolio will be delivered to KEMI free and clear of all Liens other than the obligations under the Contracts of Coverage from and after Closing.

(b) At the Closing KEMI will assume only the liabilities and obligation arising out of the Contracts of Coverage, together with the IBNR and Transferred Claims (the "Assumed Liabilities"), and no other liabilities of the Fund or KSBIT, whether known or unknown, liquidated or unliquidated, contingent or otherwise. All liabilities and obligations of the Fund and KSBIT other than the Assumed Liabilities (the "Retained Liabilities") shall be retained by and remain liabilities and obligations of the Fund and KSBIT. For avoidance of doubt, the Retained Liabilities shall include, and the Assumed Liabilities shall exclude, any and all liabilities arising out of any claim for bad faith, mishandling of claims, unlawful or unfair settlement practices, breach of any Contract of Coverage, violations of Law, any liabilities for borrowed money or that may be owed on surplus notes, any liability not specifically related to the workers' compensation obligations of the Fund, and any penalty, fine or assessment claimed by or owed to the Kentucky Department of Workers' Claims, Kentucky Department of Insurance or other Governmental Body, due to the actions or inactions of the Fund, KSBIT, the Kentucky League of Cities, any third party administrator or any other Person, including any fines, penalties or assessments under KRS 342.267, KRS 342.990 and 803 KAR 25:240.

(c) There is excluded from the Portfolio being transferred and the Fund shall retain, all rights to indemnification by the Members under the Self-Insurance Agreements, except to the extent constituting obligations to pay deductibles or retention which are being transferred as part of the Portfolio. The Fund's rights to indemnification by the Members under the Self-Insurance Agreements and otherwise shall remain in full force and effect.

2.2 Transfer Payment. In consideration for KEMI's acceptance of the Contracts of Coverage and attendant liabilities described above, the Rehabilitator shall pay to KEMI Thirty Five Million Dollars ($35,000,000) (the "Transfer Payment"), in accordance with the following terms and conditions:

(a) At the Closing, the Rehabilitator shall pay to KEMI by, wire transfer of immediately available funds an amount equal to the Initial Transfer Payment Installment, which in no event may be less than [_____Dollars ($_____)];

(b) Within thirty (45) days of the Closing the Rehabilitator shall pay to KEMI by wire transfer of immediately available funds to an account designed by KEMI, one hundred percent (100%) of the Assessment collected from Members since the Closing, less the Funding Commission Portion attributable to such collection;

(c) Thereafter, commencing on August 10, 2015 and on the 10th day of each August until August 10, 2020, the Rehabilitator shall pay to KEMI, by wire transfer of immediately available funds to an account designated by KEMI, the amount of the Individual Assessments collected by the Rehabilitator since the last payment of the Transfer Payment, except that the Rehabilitator shall pay over to KEMI within ten (10) days of receipt any Individual Assessments collected by the Rehabilitator (less the Funding Commission Portion attributable to such collection) that (i) are received more than ten (10) days before their due date or (ii) were past due when paid. If on or prior to August 10, 2020 KEMI has not been paid the Transfer Payment in full, the entire unpaid amount of the Transfer Payment shall be due and payable in full on such day.

2.3 Assessments.

(a) Levy of Assessment. Prior to the Closing, the Rehabilitator shall assess the Members pursuant to the Self-Insurance Agreements and applicable Law, an aggregate amount necessary to cure the asset deficiency of the Fund so that the Fund will, upon collection of all such assessments, be able to pay the Transfer Payment, the Funding Commission Assessment and the Retained Liabilities not being paid by other assessments and such other liabilities and obligations of the Fund as the Rehabilitator deems appropriate, in full (the "Assessment"). The Assessment shall be no less than Thirty-Five Million Dollars ($35,000,000). The Assessment shall be allocated among the Members (each Member's share of the Assessment is an "Individual Assessment") in a manner that is fair and equitable, as determined by the Rehabilitator and approved by the Court.

(b) Individual Assessment Payment Option. The Rehabilitator shall permit each Member to elect to pay its Individual Assessment in one of the following methods:

(i) A Member may elect to pay its Individual Assessment in full on or before the later of (1) the date that is thirty (30) days after the Court's entry of the Transfer Order or (2) July 31, 2014 (the "Due Date").

(ii) A Member may elect to pay its Individual Assessment in full on or before the Due Date from the proceeds from the issuance of bonds, notes or other obligations as provided in KRS 304.48-250 and 304.50-055 or as otherwise permitted by Law.

(iii) A Member may elect to pay its Individual Assessment over a period of two (2) to six (6) years (the "Installment Payment Method") as provided in the form of installment payment agreement attached as Exhibit "A" (the "Installment Payment Agreement"). To elect the Installment Payment Method, the Member

must on or before the Due Date (1) execute and deliver to the Rehabilitator a properly completed Installment Payment Agreement (including proper adoption by the applicable Board of Education) in the form of Exhibit "A" and (2) pay to the Rehabilitator 25% of the Individual Assessment. A Member's unpaid balance of its Individual Assessment under the Installment Payment Agreement may be prepaid at any time in full, without penalty.

If a Member has not on or prior to the Due Date either (x) paid the Individual Assessment in full by the Due Date as provided in Sections 2.3(b)(i) or 2.3(b)(ii) or (y) executed and delivered to the Rehabilitator a properly completed Installment Payment Agreement and paid in full the required initial installment on or before the Due Date as required by Section 2.3(b)(iii), the Member shall be deemed to have elected to pay the Individual Assessment in full pursuant to Section 2.3(b)(i) and if not paid by such Due Date the Member shall be deemed to be past due in paying the Individual Assessment and the Rehabilitator shall pursue the collection efforts under Section 2.3(c).

(c) Collection by Rehabilitator. The Rehabilitator will diligently pursue collection of all Individual Assessments, including payments due under the Installment Payment Agreements. If any Member is more than three (3) days past the date due to the Rehabilitator on any installment payment due under the Installment Payment Agreement, the Rehabilitator will immediately commence collection of such past due installment payment pursuant to KRS 304.50-055 and KRS 160.160(5) by the intercept of any payment due to such Member from the Commonwealth of Kentucky (the "Intercept") and, upon receipt of funds from such Intercept, deposit the same into the Account and thereafter remit such funds to KEMI with future payments of the Transfer Payment or, if earlier, within ten (10) days of receipt. To secure the Transfer Payment and ensure the Intercept, the Rehabilitator and KEMI shall enter with the Kentucky Department of Education and Kentucky Finance and Administration Cabinet the Memorandum of Understanding in the form attached hereto as Exhibit "B" (the "Memorandum of Understanding"). If any Member not party to an Installment Payment Agreement is past due on paying an Individual Assessment, the Rehabilitator will commence diligent collection efforts for the entire Individual Assessment of such Member, including effectuating an Intercept and bringing appropriate action before the Court and attaching assets, garnishing bank accounts held by the Member and other collection efforts a reasonably prudent judgment creditor would take.

(d) Collection by KEMI. The Rehabilitator shall on a monthly basis provide KEMI with an accounting of payments of the Individual Assessments made by the Members, which shall identify any Members who are past due in any payments of their Individual Assessments, including under any Installment Payment Agreements. During any period in which a high level of Individual Assessments are anticipated to be paid (for example the one-week period prior to the Due Date and the one-week period thereafter and the one-week period prior to and the one-week period after each July 31), the Rehabilitator shall keep KEMI apprised of, and provide information as to, collections of Individual Assessments on a more frequent basis as KEMI may request. If any Member is past due in any payment of Individual Assessments, including any payment due under any Installment Payment Agreement, within three (3) days of KEMI's written request the Rehabilitator shall inform KEMI in writing of whether the Intercept has been initiated for any past due payment, the status of the Intercept and any other collection efforts. If KEMI determines the Rehabilitator is not diligently pursuing collection of any Individual

Assessment, KEMI shall be entitled to initiate and pursue any and all collection efforts at the Fund's cost that the Rehabilitator may pursue, including initiating the Intercept under the Memorandum of Understanding.

(e) Depository. The Rehabilitator shall maintain a separate depository account for collection of the Individual Assessments (the "Account"), which shall be invested in a Treasury obligation money-market fund on funds in excess of the FDIC guaranteed amount. The financial institution shall be selected by the Rehabilitator with approval from KEMI (the "Depository"). All collections of Individual Assessments shall be deposited into the Account.

(f) Security. To secure the payment of the Transfer Payment and obligations to KEMI under this Agreement, the Rehabilitator shall grant KEMI a first and prior security interest and lien in the Assessment receivable and all future assessment receivables of the Fund, the Installment Payment Agreements, the Account and all proceeds thereof, pursuant to the form of security agreement attached hereto as Exhibit "C" (the "Security Agreement"). The Rehabilitator and KEMI will enter a control agreement with the Depository respecting such security interest in form mutually agreeable to the Rehabilitator, KEMI and the Depository (the "Control Agreement").

2.4 Funding Commission Assessment. The Rehabilitator shall be responsible for and pay the special fund assessment to the Kentucky Workers' Compensation Funding Commission respecting the Assessment (the "Funding Commission Assessment"). The Funding Commission Assessment will be collected and remitted by the Rehabilitator proportionately as the Assessment is collected in installments. The Rehabilitator and KEMI agree that while the Assessment as collected by the Fund is subject to the Funding Commission Assessment, the Transfer Payment paid to KEMI hereunder is not subject to a special funding assessment by the Kentucky Workers' Compensation Funding Commission.

ARTICLE 3 CLOSING AND DELIVERIES

3.1 Closing. The Parties shall hold a closing (the "Closing") on a date mutually agreeable to the Parties after which all the conditions to Closing set forth in Article 6 have been satisfied or waived and KEMI has the systems in place to accept transfer and management of the Portfolio and Transferred Claims. The date on which the Closing occurs shall be the "Closing Date". The Parties agree to endeavor for the Closing Date to be as soon as reasonably practicable.

3.2 Rehabilitator's Deliveries. The sale, transfer, assignment and delivery by the Rehabilitator of the Portfolio, as herein provided, shall be effected at the Closing by the Rehabilitator's execution, acknowledgement and delivery of the following, each in form satisfactory to the Rehabilitator and KEMI:

(a) an assignment and assumption agreement (the "Assignment") transferring to KEMI, all right, title and interest of the Fund and KSBIT in the Contracts of Coverage, including the IBNR and the Transferred Claims, the Excess Policies, the Subrogation Rights, the Records and all other rights and obligations under the Portfolio as contemplated by Section 2.1;

(b) a transition services agreement (the "Transition Services Agreement") in form mutually agreeable to KEMI and the Rehabilitator providing for support services from the Rehabilitator and any third party administrator of the Fund necessary in order to smoothly transition the management of the Portfolio, including Transferred Claims, to KEMI, including such services as are anticipated to be necessary to effectuate the requirements of Section 7.4;

(c) the Memorandum of Understanding;

(d) the Security Agreement and Control Agreement; and

(e) payment to KEMI of the Initial Transfer Payment Installment by wire transfer of immediately available funds to an account designated by KEMI in writing.

In addition, from and after the Closing the Rehabilitator will take such actions and execute and deliver such additional agreements and instruments of transfer as KEMI may reasonably request to deliver to and vest in KEMI the Portfolio.

3.3 KEMI's Deliveries. At the Closing, KEMI shall execute, acknowledge and deliver the following, each in form satisfactory to the Rehabilitator and KEMI:

(a) the Assignment;

(b) the Transition Services Agreement;

(c) the Memorandum of Understanding; and

(d) the Security Agreement and Control Agreement.

In addition, from and after the Closing KEMI will take such actions and execute and deliver such additional agreements and instruments of transfer as the Rehabilitator may reasonably request to assume the Portfolio and Assumed Liabilities.

ARTICLE 4 - REPRESENTATIONS AND WARRANTIES OF THE REHABILITATOR

In order to induce KEMI to enter into this Agreement, on behalf of the Fund, the Rehabilitator makes the representations and warranties set forth below which, except as set forth in the Fund Disclosure Schedule, are true, correct and complete on the date hereof and shall be true, correct and complete as of the Closing:

4.1 Fund. The Fund is a workers' compensation self-insured group under KRS 304.50-005, *et. seq.* and holds a valid certificate from the Kentucky Office of Insurance as required by KRS 304.50-005, *et. seq.* The Fund has all requisite power and authority to own its properties and assets. Pursuant to the Self-Insurance Agreements and applicable Law governing the Fund, the Members are jointly and severally liable for the liabilities of the Fund.

4.2 Rehabilitator. The Rehabilitator has filed a Petition with the Court pursuant to KRS 304.33-140 and KRS 304.50-135, seeking appointment as the rehabilitator of the Fund.

Upon appointment by the Court as rehabilitator of the Fund, the Rehabilitator will have all requisite power and authority as rehabilitator of the Fund under KRS Chapter 304, Subtitle 33.

4.3 Authorization and Validity. Subject to entry of the Transfer Order, Rehabilitator has all necessary authority to enter into and deliver this Agreement and the Related Agreements and to consummate the transactions contemplated hereby and thereby. Upon entry of the Transfer Order, the execution and delivery of this Agreement and the Related Agreements and the performance of the obligations hereunder and thereunder will have been duly and validly authorized, as applicable, by all necessary action by Rehabilitator. This Agreement and the Related Agreements have been, or will be at Closing, duly and validly executed and delivered by Rehabilitator and, subject to the Court's entry of the Transfer Order, constitute, or will constitute when executed or delivered, valid and binding obligations of the Fund and Rehabilitator, enforceable against the Fund and Rehabilitator in accordance with their terms. This Agreement, and once executed and delivered by the Rehabilitator, the Related Agreements, subject to the Court's entry of the Transfer Order, will constitute valid and binding obligations of KSBIT with respect to the rights and assets KSBIT holds or has held that are related to the Fund.

4.4 No Conflict or Violation. Subject to (a) the Court's entry of the Transfer Order, and (b) the receipt of the consents, waivers, authorizations and approvals set forth on Schedule 4.4 of the Fund Disclosure Schedule, the execution, delivery and performance by Rehabilitator and Fund of this Agreement and the Related Agreements (i) do not and will not violate or conflict with any provision of the trust agreement, bylaws and other governing documents of KSBIT with respect to the Fund or the Fund, (ii) do not and will not violate any provision of any Law or any Order applicable to Rehabilitator, KSBIT, the Fund or the Portfolio, (iii) do not and will not violate or result in a breach of or constitute (with due notice or lapse of time or both) a default under any Contract entered into by KSBIT related to the Fund, the Fund or to which the Fund's assets are subject, and (iv) will not result in the creation or imposition of any Lien on the Portfolio.

4.5 Consents and Approvals. Schedule 4.5 of the Fund Disclosure Schedule sets forth a true and complete list of each material consent, waiver, authorization or approval of any Governmental Body or of any other Person (other than the Court's entry of the Transfer Order), and each material declaration to or filing or registration with any such Governmental Body (other than pleadings in connection with seeking the Court's entry of the Transfer Order), that is required in connection with such Rehabilitator's execution, delivery and performance of this Agreement and the Related Agreements.

4.6 Compliance with Law. The Fund is not in violation, and has not violated, any Law, nor is the Fund in material default with respect to any Order, applicable to the Portfolio, except in either case for such violations or defaults that have been abated or which would not reasonably be expected to result in a Fund Material Adverse Effect.

4.7 Litigation.

(a) Except for the Rehabilitation Case and claims by employees and former employees of the Members covered by the Contracts of Coverage ("Ordinary Course Claims"), there are no Proceedings related to the Fund or Portfolio or the transactions contemplated hereby

pending or, to the Fund's knowledge, threatened, before any federal or state court or other Governmental Body by or against the Fund or KSBIT relating to the Fund.

(b) There is no Proceeding against the Fund, or KSBIT relating to the Fund, that has been brought by a Member of the Fund, nor, to the knowledge of the Fund, has any Member threatened to bring any Proceeding against the Fund, or KSBIT relating to the Fund.

(c) Other than facts or circumstances that might result in Ordinary Course Claims, there are no facts or circumstances known to the Fund that could reasonably be expected to give rise to any Claim or Proceeding that would be required to be disclosed pursuant to Section 4.7 (a) or (b) above.

(d) Except pursuant to the Rehabilitation Case and the Ordinary Course Claims, there are no material Orders outstanding against the Fund, KSBIT (with respect to or that affect the Fund) or the Rehabilitator.

(e) Schedule 4.7 to the Fund Disclosure Schedule sets forth each pending Proceeding that is an Ordinary Course Claim.

4.8 Ownership. At Closing, the Fund, or KSBIT as part of the Fund, will own and have transferable title to the assets that constitute part of the Portfolio and the Rehabilitator will have authority to transfer the Fund's and KSBIT's ownership and title to such assets to KEMI. Subject to entry of the Transfer Order, all of the Fund's, KSBIT's and Rehabilitator's right, title and interest in and to the Portfolio shall be transferred to KEMI at Closing, free and clear of all Liens.

4.9 Contracts. (a) Each of the Fund and KSBIT is in compliance with its obligations under the Contracts of Coverage and neither the Fund nor KSBIT, nor to the Fund's knowledge, any other party to any Contract of Coverage, is in default or violation under any Contract of Coverage.

(b) The Fund has paid in full all premiums due under each Excess Policy and the Fund and KSBIT are in compliance with their obligations under each Excess Policy and neither the Fund nor KSBIT, nor to the Fund's knowledge, any other party to any Excess Policy, is in default or violation under any Excess Policy.

(c) Each of the Subrogation Rights is in full force and effect and the Fund and KSBIT have not taken any action, or failed to take any action, that would waive or otherwise impair their ability or the ability of KEMI to fully collect the Subrogation Rights.

(d) Other than the Contracts of Coverage, the Excess Policies and the Subrogation Rights, there are no Contracts or rights under Contracts necessary to operate and manage the Fund.

4.10 Intellectual Property. Schedule 4.10 to the Fund Disclosure Schedule sets forth all Intellectual Property owned or used by the Fund (and KSBIT with respect to the Fund) to own, operate and manage the Portfolio. Each of KSBIT and the Fund has a right to own or use all such Intellectual Property through ownership or license as set forth on Schedule 4.10 to the

Fund Disclosure Schedule. No claim is pending, or to the Fund's knowledge has been threatened or asserted by any Person, challenging or questioning the use by KSBIT or the Fund of any such Intellectual Property or the validity or effectiveness of any of KSBIT's or the Fund's Intellectual Property used in connection with the Fund. The use of such Intellectual Property by KSBIT and the Fund does not infringe on the rights of any Person.

4.11 Financial Statements and Other Information. (a) Attached as Schedule 4.11 to the Fund Disclosure Schedule are true and complete copies of the Fund's unaudited statement of net deficits as of September 30, 2013, and the related unaudited statement of revenues, expenses and changes in net deficits and cash flows for the quarter then ended and the Fund's audited statements of net deficits as of June 30, 2103, 2012 and 2011, and the related audited statements of revenues, expenses and changes in net deficits and cash flows for the fiscal years then ended (collectively, the "Financial Statements"). The Financial Statements, which are attached to the Fund Disclosure Schedule at Schedule 4.11, were prepared in accordance with GAAP, consistently applied (except that the unaudited Financial Statements as of September 30, 2013 and for the quarter then ended are subject to normal year-end adjustments and will not include footnotes), and fairly present the financial condition and the results of operations of the Fund as of and for the fiscal periods therein specified, and were compiled from the books and records of the Fund regularly maintained by management and used to prepare the Financial Statements. Financial Statements of the Fund complied after September 30, 2013 (the "Subsequent Financial Statements") will be prepared in accordance with GAAP, consistently applied (except that the Subsequent Financial Statements for any interim period will be subject to normal year-end adjustments and will not include footnotes), and will fairly present the financial condition and the results of operations of the Fund as of and for the fiscal periods therein specified, and will be compiled from the books and records of the Fund regularly maintained by management and used to prepare the Financial Statements.

(b) The following information has been provided to KEMI and is accurate and complete and has not been altered, modified or updated since being provided to KEMI (the "Additional Information"):

(i) Additional Information prepared or provided by the Kentucky League of Cities on behalf of KSBIT:

(A) Detailed Fund Claim Data by School per Claimant

1. Paid loss, allocated loss adjustment expense, and attorney (legal) expense per claim;

2. Outstanding case reserves for each item listed in "(A)1" above;

3. Recoveries per claim;

4. Deductible per claim; and

5. Status (open/closed) per claim;

(B) Copies of certain available Excess Policies and cover notes respecting Excess Policies that are not available;

(C) Claim System made available to sample claim reserve adequacy;

(D) Claim Case Reserve Analysis Audit, 6/30/12, prepared by Marsh & McLennan, dated 11/26/2012;

(E) Reserve Review & Critique, 6/30/12, prepared by Milliman, dated 11/27/12;

(F) Analysis of Loss and Allocated Loss Adjustment Expense Reserves as of 6/30/12, prepared by Practical Actuarial Solutions, dated 9/13/12;

(G) Audited Financial Statement, prepared by Dean, Dorton, & Ford, dated 1/11/13;

(H) Reinsurance Schedules Detailing Excess & Aggregate Recoveries by Treaty as of 6/30/2012; and

(I) Statement of Actuarial Opinion as of 6/30/13, prepared by Practical Actuarial Solutions, dated 8/1/13.

(ii) Additional Information prepared by Taylor-Walker & Associates for or on behalf of the Kentucky Department of Insurance:

(1) KSBIT WC Fund Actuarial Examination as of 6/30/13, dated 8/20/13; and

(2) Summary of Discounted Net Loss and Net LAE Reserves as of 6/30/13.

The Rehabilitator acknowledges that, in addition to the Financial Statements, in entering into this Agreement and agreeing to the amount of the Transfer Payment, timing of the payment of the Transfer Payment and other transactions contemplated hereby, KEMI has relied upon the Additional Information and the accuracy thereof.

4.12 Financial Advisors. None of the Fund, KSBIT or Rehabilitator nor any other Person on the Fund's, KSBIT's or Rehabilitator's behalf has agreed to pay any brokerage fee, finder's fee or commission which could reasonably be expected to become the obligation of KEMI or the Fund with respect to the transactions contemplated by this Agreement.

4.13 Taxes. All required federal, state, local and other Tax Returns relating to the Fund, KSBIT and the Portfolio have been accurately prepared and duly and timely filed, and all Taxes required to be paid with respect to the periods covered by any such returns have been timely paid. No Tax deficiency or tax lien has been proposed or assessed against the Fund or Portfolio or any part thereof or against KSBIT or the Fund related to the Portfolio, and KSBIT has not executed any waiver of any statute of limitations on the assessment or collection of any Tax relating to the Fund or the Portfolio. No Tax audit, action, suit, proceeding, investigation or claim is now pending or, to the knowledge of the Fund, threatened against the Fund or KSBIT relating to the Fund or Portfolio.

ARTICLE 5 - REPRESENTATIONS AND WARRANTIES OF KEMI

In order to induce the Rehabilitator to enter into this Agreement, KEMI makes the representations and warranties set forth below, which are true, correct and complete on the date hereof and shall be true, correct and complete as of the Closing:

5.1 Organization. KEMI is a nonprofit, independent, self-supporting *de jure* municipal corporation and political subdivision of the Commonwealth of Kentucky created pursuant to KRS 342,803, *et. seq.*

5.2 Authorization and Validity. KEMI has all requisite power and authority to enter into this Agreement and the Related Agreements to which it is a party. The execution and delivery of this Agreement and the Related Agreements to which it is a party and the performance of the obligations hereunder and thereunder have been duly authorized by all necessary action by KEMI. This Agreement and the Related Agreements to which KEMI is a party have been, or will be, duly executed by KEMI and when executed and delivered constitute KEMI's valid and binding obligations, enforceable against KEMI in accordance with their terms.

5.3 Consents and Approvals. Except for entry of the Transfer Order and the matters set forth on Schedule 5.3 of the KEMI Disclosure Schedule, no consent, approval or action of, filing with or notice to, any Governmental Body or any other Person, on the part of KEMI is required in connection with the execution, delivery and performance of this Agreement or any of the Related Agreements to which KEMI is a party or the consummation of the transactions contemplated hereby or thereby.

5.4 Financial Advisors. Neither KEMI nor any Person on KEMI's behalf has agreed to pay any brokerage fee, finder's fee or commission which could reasonably be expected to become the obligation of the Rehabilitator or Fund with respect to the transactions contemplated by this Agreement.

ARTICLE 6 - CONDITIONS PRECEDENT TO PERFORMANCE BY PARTIES

6.1 Conditions to Each Party's Obligations. The respective obligations of each of the Rehabilitator and KEMI to consummate the transactions contemplated by this Agreement shall be subject to the fulfillment or waiver on or before the Closing of the following conditions:

(a) Court Approval. The entry of one or more final and non-appealable Orders by the Court, in the form acceptable to counsel to KEMI and Rehabilitator (collectively, the "Transfer Order"), which Orders in the aggregate: (i) approve the Petition for rehabilitation and appoint the Rehabilitator as rehabilitator of the Fund, (ii) approve and authorize the Assessment, Individual Assessments, form of Installment Payment Agreement, Intercept and Memorandum of Understanding and order the collection by the Rehabilitator of the Individual Assessments, (iii) find that the Intercept is a lawful and proper mechanism to ensure payment of the Assessment to the Rehabilitator and payment of the Transfer Payment to KEMI and order all Kentucky Governmental Bodies involved in payments due to Members to effect the Intercept, (iv) approve and authorize the entering of this Agreement by the Rehabilitator and performance by the

Rehabilitator, Fund and KSBIT of the obligations hereunder, including execution and delivery of the Memorandum of Understanding, Installment Payment Agreements and Security Agreement and payment of the Transfer Payment as contemplated by this Agreement, (v) approve and authorize the assignment and transfer of the Portfolio, free and clear of any Liens, as contemplated by this Agreement, including assignment and transfer of the Excess Policies to KEMI as contemplated by this Agreement, irrespective of any restrictions or limitations or requirements for endorsements contained in the Excess Policies respecting assignment or transfer thereof, (vi) find and order that KEMI will have, upon execution and delivery of the Security Agreement, filing of a financing statement with the Kentucky Secretary of State and entering the Control Agreement, a valid and enforceable first and prior security interest and lien under applicable Kentucky Law in the collateral identified in the Security Agreement, (vii) find and order that the Transfer Payment paid to KEMI hereunder is not subject to a special funding assessment by the Kentucky Workers' Compensation Funding Commission, (viii) order the Rehabilitator to make any Necessary Future Assessments, (ix) find and order that if the Fund is to enter a liquidation proceeding under Subtitle 33 of KRS Chapter 304, the Transfer Payment will be deemed an administrative expense of, and secured claim against, the Fund, and (ix) approve and authorize the consummation of all other transactions contemplated by this Agreement, subject to the terms and conditions of this Agreement. The Rehabilitator shall provide all Members of the Fund, creditors of the Fund, holders of Liens and Claims against the Fund and issuers of the Excess Policies, timely notice of the proposed entry of the Transfer Order and hearing for the same; copies and proof of service of the foregoing, together with a certified copy of the Transfer Order, shall be delivered to KEMI on or before the Closing.

(b) Injunctions. There shall not be outstanding any Order prohibiting the consummation of the transactions contemplated by this Agreement and no Proceeding shall have been commenced which could reasonably be expected to prohibit the consummation of the transactions contemplated hereby.

(c) No Change in Law. There shall not have been any action taken or any Law enacted by any Governmental Body which would render the Parties unable to consummate the transactions contemplated hereby or make the transactions contemplated hereby illegal or prohibit the consummation of the transactions contemplated hereby.

(d) Initial Transfer Payment Installment. The Rehabilitator shall have on behalf of the Fund collected sufficient funds to enable the Rehabilitator to pay the Initial Transfer Payment Installment at Closing.

6.2 Conditions Precedent to Performance by the Rehabilitator. The obligations of the Rehabilitator to consummate the transactions contemplated by this Agreement are subject to the fulfillment, at or before the Closing, of the following conditions, any one or more of which may be waived by the Rehabilitator in its sole discretion:

(a) Representations, Warranties and Obligations of KEMI. All representations and warranties made by KEMI in Article 5, shall be true and correct in all material respects on the date of this Agreement and on and as of the Closing Date (except to the extent that any such representation and warranty is made as of a specified date, in which case such representation and warranty shall continue to be made as of such specified date), and the covenants and agreements of KEMI to be performed on or before the Closing Date shall have

been duly performed in all material respects in accordance with this Agreement, and the Rehabilitator shall have received a certificate, dated the Closing Date and signed by an officer of KEMI, to that effect.

(b) Consents and Approvals. All consents, approvals and actions of, filings with and notices to any Governmental Body or other Person necessary to permit the Rehabilitator to perform its obligations under this Agreement and the Related Agreements and to consummate the transactions contemplated hereby and thereby (including transfer of the Portfolio) (i) shall have been duly obtained, made or given, (ii) shall be in form and substance reasonably satisfactory to the Rehabilitator, (iii) shall not be subject to the satisfaction of any condition that has not been satisfied or waived, and (iv) shall be in full force and effect, and all terminations or expirations of waiting periods imposed by any Governmental Body necessary for the consummation of the transactions contemplated by this Agreement and the Related Agreements shall have occurred.

6.3 Conditions Precedent to Performance by KEMI. The obligations of KEMI to consummate the transactions contemplated by this Agreement are subject to the fulfillment, at or before the Closing, of the following conditions, any one or more of which may be waived by KEMI in its sole discretion:

(a) Representations, Warranties and Obligations of the Rehabilitator. The representations and warranties made by the Rehabilitator in Article 4, individually and in the aggregate, shall be true and correct in all material respects on the date of this Agreement and on and as of the Closing Date (except to the extent that any such representation and warranty is made as of a specified date, in which case such representation and warranty shall continue to be made as of such specified date), and the covenants and agreements of the Rehabilitator to be performed on or before the Closing Date shall have been duly performed in all material respects in accordance with this Agreement, and KEMI shall have received a certificate, dated the Closing Date and signed by the Rehabilitator to that effect.

(b) Transfer Free of Liens. The Portfolio shall be transferred to KEMI free and clear of all Liens.

(c) No Fund Material Adverse Effect. Between the date of this Agreement and the Closing Date, there shall not have occurred any Fund Material Adverse Effect, or any event or development which, individually or together with such other events, could reasonably be expected to result in a Fund Material Adverse Effect.

(d) Consents and Approvals. All consents, approvals and actions of, filings with and notices to any Governmental Body or other Person necessary to permit KEMI and the Rehabilitator to perform their obligations under this Agreement and the Related Agreements and to consummate the transactions contemplated hereby and thereby (including transfer of the Portfolio), (i) shall have been duly obtained, made or given, (ii) be in form and substance satisfactory to KEMI, (iii) shall not be subject to the satisfaction of any condition that has not been satisfied or waived, and (iv) shall be in full force and effect, and all terminations or expirations of waiting periods imposed by any Governmental Body necessary for the consummation of the transactions contemplated by this Agreement and the Related Agreements shall have occurred.

(e) Order from Commissioner. KEMI shall have received a final and non-appealable Order from the Commissioner of the Department of Insurance that the receivable KEMI will book as a result of the Transfer Payment shall be a State Prescribed Difference from NAIC Statutory Accounting Principles and shall be reported as an admitted asset for purposes of statutory accounting and determination of solvency.

(f) Payment of Individual Assessments. Individual Assessments shall have been paid in full, or a properly completed Installment Payment Agreement (as contemplated by Section 2.3(b)(iii)) shall have been executed and delivered and the first installment payment required by Section 2.3(b)(iii) shall have been paid, by Members that in the aggregate (i) constitute 90% or more of the Members by number liable for the Assessment and (ii) owe at least 90% of the total Assessment by dollar amount.

ARTICLE 7 - COVENANTS

7.1 Covenants of the Rehabilitator. The Rehabilitator covenants as follows:

(a) Access to Properties and Records; Confidentiality. The Rehabilitator shall afford to KEMI, and to the accountants, counsel and representatives of KEMI, reasonable access during normal business hours throughout the period before the Closing (or the earlier termination of this Agreement pursuant to Article 8) to all books and records of the Fund and Rehabilitator relating to the Fund and the Portfolio.

(b) Further Assurances. At the request and the sole expense of KEMI, at any time after the Closing Date, the Rehabilitator shall execute and deliver such documents as KEMI or its counsel may reasonably request to effectuate the purposes of this Agreement or further vest ownership and title in the Portfolio in KEMI.

(c) Conduct of Operations. From the date hereof until the Closing, the Rehabilitator shall, except as otherwise permitted, required or contemplated by this Agreement or applicable Law, (i)(A) maintain and manage the Portfolio using prudent industry practices, and (B) comply, in all material respects, with all Contracts, Laws and Orders and promptly following receipt thereof, give KEMI copies of any notice received from any Governmental Body or other Person alleging any material violation of any such Contract, Law or Order; and (ii) the Rehabilitator shall not (A) permit the Fund to enter any new contracts of coverage or extend any new policies, (B) sell, transfer or lease any material properties or assets to any Person other than use of the assets in connection with management and payment of Ordinary Course Claims, or (C) engage in any transaction with any officer, director or Affiliate of the Fund.

(d) Rehabilitation Case. The Rehabilitator covenants and agrees to use commercially reasonable efforts in the Rehabilitation Case to prevail therein and in obtaining a Transfer Order in form and substance acceptable to the Rehabilitator and KEMI.

(e) No Release. The Rehabilitator and Fund will not release any Member from its liabilities and obligations to the Fund, including its joint and several liabilities and obligations with all Members.

(f) Subsequent Financial Statements. Commencing with the quarter ended December 31, 2013, the Rehabilitator shall cause to be prepared and delivered to KEMI within 45 days after the end of each quarter the unaudited statement of deficit and the related statements of revenues, expenses and changes in net deficit and cash flow for the quarter. In addition, the Rehabilitator shall provide KEMI with such other interim reports as KEMI may reasonably request that are prepared by the Rehabilitator in administering the Fund.

(g) Future Assessments. If the amount of the Assessment actually collected, or anticipated to be collected in a reasonable time, is insufficient to satisfy in full payment of the Transfer Payment, other obligations under this Agreement and other Retained Liabilities, including expenses to administer the rehabilitation of the Fund and any other existing Retained Liabilities or Retained Liabilities that arise in the future, then the Rehabilitator on behalf of the Fund shall levy additional assessments on the Members necessary to fully satisfy all such Retained Liabilities, including payment of the Transfer Payment and other obligations under this Agreement ("Necessary Future Assessments").

7.2 Covenants of KEMI. KEMI covenants as follows:

(a) Access to Books and Records. Following the Closing Date, KEMI agrees to give access to the Rehabilitator or its designees, as promptly as practicable, to such accounting, business, financial and Tax records and information (A) relating to the Portfolio that are in existence on the Closing Date and transferred to KEMI hereunder, or (B) coming into existence after the Closing Date that relate to the Portfolio before the Closing, as the Rehabilitator determines is reasonably necessary for any Tax, regulatory or business purpose of the Fund. Such access shall include, without limitation, access to any computerized information retrieval systems relating to the Portfolio. KEMI agrees that it will in accordance with its own record retention and destruction policies retain possession of and destroy accounting, business, financial and Tax records and information (A) relating to the Portfolio that are in existence on the Closing Date and transferred to KEMI hereunder, or (B) coming into existence after the Closing Date that relate to the Portfolio before the Closing.

(b) KEMI's Cooperation with the Rehabilitation Case. KEMI covenants and agrees to use commercially reasonable efforts to cooperate with the Rehabilitator in the Rehabilitation Case and in obtaining a Transfer Order in form and substance acceptable to the Rehabilitator and KEMI.

(c) Return of Excess Transfer Payment. KEMI agrees that after it has satisfied all the Assumed Liabilities, including Transferred Claims and other claims that may be brought in connection with the Assumed Liabilities, and determined in its discretion that there is no further potential liability arising from the Assumed Liabilities, including any potential future claims, that it will return to the Rehabilitator (for the use and benefit of the Members), the amount by which the Transfer Payment received by KEMI under this Agreement exceeds the Portfolio Costs and Expenses. The "Portfolio Costs and Expenses" means all amounts paid or expended in satisfying the Assumed Liabilities, including amounts paid on judgments, in settlement, and in administration of the Transferred Claims and other claims, and all other out-of-pocket expenses and costs incurred in connection with transfer and management of the Portfolio, all as determined by KEMI in its discretion.

7.3 Covenants of the Parties.

(a) Consents. The Parties shall promptly apply for and diligently prosecute all applications for, and shall use commercially reasonable efforts promptly to obtain, such consents, authorizations and approvals from such Governmental Bodies and third parties as shall be necessary or appropriate to permit the consummation of the transactions contemplated by this Agreement, and shall use commercially reasonable efforts to bring about the satisfaction as soon as practicable of all the conditions necessary to effect the consummation of the transactions contemplated by this Agreement. Each Party will also use all reasonable efforts to take or cause to be taken all actions necessary, proper or advisable to comply with all legal requirements that may be imposed on it with respect to this Agreement and the transactions contemplated hereby and, subject to the provisions hereof, to consummate the transactions contemplated by this Agreement as promptly as practicable.

(b) Publicity. KEMI and the Rehabilitator will consult with each other as to the timing, form and substance of any press release or other public disclosure materially related to this Agreement or the transactions contemplated hereby.

7.4 Covenants Related to Transition of Portfolio.

(a) Promptly following the Closing Date, the Rehabilitator shall deliver or cause the Fund to deliver to the named insureds under the Contracts of Coverage and the issuers of the Excess Policies a notice of transfer in form mutually agreeable to KEMI and the Rehabilitator.

(b) The Rehabilitator shall cooperate with and assist KEMI in KEMI becoming the successor party to the Rehabilitator respecting any Transferred Claims.

(c) The Rehabilitator and KEMI recognize that transfer of the management of the Portfolio, including the Transferred Claims, will require significant cooperation over an extended period of time. The Rehabilitator and KEMI agree to transition possession of the Records to KEMI sufficiently in advance of Closing so that as of Closing KEMI will be able to manage the Portfolio, including the Transferred Claims, in a reasonable manner and in compliance with Law. If the Records are transferred to KEMI and the Closing does not occur, KEMI shall immediately return all such Records to the Rehabilitator upon the Rehabilitator's demand and shall have no rights therein. The Rehabilitator shall cooperate with KEMI, and shall cause any third party administrator of the Fund to cooperate with KEMI at the Fund's expense, in transferring all Records from the Fund and its third party administrators to KEMI in a manner and format usable by KEMI for conversion to KEMI's software and management systems.

(d) Any payments received by or due to the Fund or KSBIT from any issuer of Excess Policies from and after the Closing shall be paid to KEMI upon receipt.

(e) Any payments received from any Person on account of Subrogation Rights from and after Closing transferred hereunder shall become the property of and be paid to KEMI.

(f) If any payment is received by the Fund or KSBIT which is to be credited to KEMI under or with respect to any of the Transferred Claims, the Rehabilitator will cause the Fund or KSBIT to immediately endorse and deliver to KEMI such checks, drafts, or money intended as such payment, and until delivery of such items to KEMI, the Fund and KSBIT will treat any such checks, drafts, or money as the property of KEMI held for the account of and in trust for KEMI.

(g) (i) From and after the Closing Date, KEMI will be solely liable for the payment of Transferred Claims, including, without limitation, the defense, adjustment, settlement, and payment of all losses and expenses arising under or relating to the Transferred Claims. However, until the Closing Date, the Rehabilitator shall continue to administer and be liable for the defense, adjustment, settlement, and payment of all losses and expenses arising under or relating to the Transferred Claims.

(ii) The Rehabilitator will cause all information and notices regarding the Transferred Claims actually received by the Fund after the Closing Date to be promptly reported to KEMI. The Rehabilitator also will undertake any reasonable arrangements deemed necessary by KEMI to ensure that all notices received by the Fund after the Closing Date in connection with the Transferred Claims are promptly delivered to KEMI. The Rehabilitator shall be responsible for, and shall indemnify KEMI against, any fines, penalties, assessments, damages and other losses, including reasonable expenses and costs of defense (including attorneys' fees), claimed by or owed to any Person resulting from delay in or the failure of Rehabilitator to forward information and notices to KEMI as required above.

ARTICLE 8 - TERMINATION

8.1 Termination. This Agreement may be terminated prior to the Closing (but not after Closing):

(a) By mutual consent of KEMI and the Rehabilitator;

(b) By either the Rehabilitator or KEMI after September 30, 2014 (as such date may be extended by the Parties by mutual written agreement), if the Closing has not occurred by such date; provided, however, that as of such date the Party terminating this Agreement is not in default under this Agreement;

(c) Provided the terminating Party is not otherwise in default or breach of this Agreement, and has not failed or refused to close without justification hereunder, by either KEMI or the Rehabilitator, without prejudice to other rights and remedies which the terminating Party may have, if the other Party shall (i) have materially failed to perform its covenants or agreements contained herein required to be performed on or prior to the Closing Date, or (ii) have materially breached any of its representations or warranties contained herein; provided, however, that in the case of clause (i) or (ii), the defaulting Party shall have a period of thirty (30) days following written notice from the non-defaulting Party to cure any breach of this Agreement, if such breach is curable;

(d) By KEMI, upon the Rehabilitator or Fund entering into a definitive agreement for any transaction (or series of transactions) involving a material portion of the Portfolio to a Person other than KEMI or effecting any other transaction the consummation of which would be substantially inconsistent with the transactions herein contemplated, including without limitation proposing a plan of reorganization that would be so inconsistent;

(e) By either the Rehabilitator or KEMI if (A) any court of competent jurisdiction (other than the Court) or other competent Governmental Body (other than the Court) has issued an order which has become final and non-appealable or (B) any Law is in effect, in either case, restricting, restraining or altering in a material manner or enjoining or otherwise prohibiting or making illegal the effectuation of the transactions contemplated by this Agreement or the effect hereof;

(f) By either the Rehabilitator or KEMI if the Court has issued an order which has become final and non-appealable restricting or restraining in a material manner or denying or enjoining or otherwise prohibiting or making illegal the effectuation of any of the transactions contemplated by this Agreement; or

(g) By either the Rehabilitator or KEMI if the Court confirms a plan of rehabilitation for the Fund in the Rehabilitation Case that does not contemplate the transactions contemplated by this Agreement or the Fund enters liquidation proceedings.

8.2 Effect of Termination; Remedies. In the event of termination of this Agreement pursuant to this Article 8, (i) all rights and obligations of the Parties shall terminate, except the obligations of the Parties pursuant to Article 8 and Article 10, and (ii) no Party shall be entitled to any damages from the other Party, except (A) if this Agreement is terminated by a Party due to the willful breach by the other Party, the non-breaching Party shall be entitled to all damages at law or in equity and (B) if this Agreement is terminated by KEMI under Section 8.2(d) or by KEMI or Rehabilitator under Section 8.2 (e), (f) or (g) and the Rehabilitator supported or did not object to the Order or confirmation on which the termination is based, then Rehabilitator shall reimburse KEMI from the Fund for all actual costs and expenses of KEMI, including attorneys' and other professional fees incurred by KEMI in preparing and entering this Agreement and participating and assisting in the Rehabilitation Case.

ARTICLE 9 INDEMNIFICATION

9.1 Survival. The representations and warranties of the Parties under this Agreement shall survive the execution and delivery of this Agreement and the Closing of the transactions contemplated hereby for a period of six years. The covenants and agreement of the Parties under this Agreement shall survive the execution and delivery of this Agreement and the Closing of the transactions contemplated hereby indefinitely.

9.2 Indemnification of KEMI by the Rehabilitator. The Rehabilitator, on behalf of the Fund, agrees the Fund shall indemnify and hold KEMI, its directors, managers, officers employees and agents (collectively, the "KEMI Indemnitees") harmless from any and all liabilities, obligations, claims, contingencies, damages, costs and expenses, including all court costs and reasonable

attorneys' fees (collectively, "Losses"), that KEMI may suffer or incur as a result of or relating to:

(a) the breach of any representation or warranty made by the Rehabilitator in this Agreement or the Related Agreements;

(b) the breach of any covenant or agreement of the Rehabilitator under this Agreement; and

(c) the Retained Liabilities.

9.3 Indemnification of the Rehabilitator. KEMI shall indemnify and hold the Rehabilitator and Fund, and each of the Rehabilitator's and Fund's officers, directors, employees, and agents (collectively, the "Fund Indemnitees") harmless from any and all Losses that any Fund Indemnitee may suffer or incur as a result of or relating to:

(a) the breach of any representation or warranty made by KEMI in this Agreement or the Related Agreements;

(b) the breach of any covenant or agreement of KEMI under this Agreement; and

(c) the Assumed Liabilities.

9.4 Procedures.

(a) Any KEMI Indemnitee or Fund Indemnitee desiring indemnification under this Article 9 and entitled thereto (an "Indemnified Party") shall, within the relevant limitation period provided for in Section 9.1, promptly upon becoming aware thereof, give written notice thereof to the Party obligated to indemnify such Indemnified Party (such notified Party, the "Responsible Party"); provided that the failure to so notify shall not relieve the Responsible Party of its obligations hereunder, except to the extent that the Responsible Party is actually prejudiced thereby. Such notice by such Indemnified Party shall state the amount of the claim, if known, and the method of computation thereof, the nature of such claim and a reference to the provision of this Agreement upon which such claim is based, all with reasonable particularity.

(b) If a claim, action, suit or proceeding by a Person other than a Party hereto or its respective Affiliates (a "Third Party Claim") is made against any Indemnified Party, and if such Indemnified Party intends to seek indemnification with respect thereto under this Article 9, such Indemnified Party shall promptly notify the Responsible Party of such claims; provided that the failure to so notify shall not relieve the Responsible Party of its obligations hereunder, except to the extent that the Responsible Party is actually prejudiced thereby.

(c) With respect to any Third Party Claim, the Responsible Party shall have thirty (30) days after receipt of such notice to assume the conduct and control, at the expense of the Responsible Party, of the settlement or defense thereof, and the Indemnified Party shall cooperate with it in connection therewith; provided that the Responsible Party shall permit the

Indemnified Party to participate in such settlement or defense through counsel chosen by such Indemnified Party and the fees and expenses of such counsel shall be borne by the Indemnified Party. Notwithstanding the foregoing, the Responsible Party shall not be entitled to assume control of the defense as to any matter, and if subject to indemnification under this Article 9, shall pay the reasonable fees and expenses of counsel selected and retained by the Indemnified Party, if: (i) the Responsible Party does not undertake the defense of such Third Party Claim within thirty (30) days after the receipt of the Indemnified Party's notice of a claim for indemnification hereunder; (ii) the claim for indemnification relates to or arises in connection with any criminal proceeding, action, indictment, allegations or investigation against the Indemnified Party; or (iii) the Indemnified Party reasonably shall have concluded (upon written advice of its counsel) that, with respect to such claims, the Indemnified Party and the Responsible Party may have conflicting interests (collectively, the "Litigation Control Conditions"). If the Indemnified Party assumes the control of the defense of such claim because the claim meets one or more of the Litigation Control Conditions, the Indemnified Party shall have the right to assume control of the defense of the claim but shall not thereby waive any right to indemnification therefor pursuant to this Agreement; provided, however, that the Indemnified Party shall not consent to an entry of judgment or settle such claim without the prior written consent of the Responsible Party, which shall not be unreasonably withheld. The Responsible Party shall, if it agrees to pay the full amount thereof, be permitted independently to consent to an entry of judgment or settle any Third Party Claim, provided that in the event such judgment or settlement includes any obligation being imposed on the Indemnified Party other than the payment of cash, then such judgment or settlement shall not be entered into without the prior written consent of the Indemnified Party.

(d) Any Indemnified Party shall cooperate in all reasonable respects with the Responsible Party and its attorneys in the investigation, trial and defense of any Third Party Claim and any appeal arising therefrom.

10 MISCELLANEOUS

10.1 Expenses. Subject to the provisions of Section 8.2(ii)(B), whether or not the transactions contemplated hereby are consummated, the Rehabilitator and Fund, on the one hand, and KEMI, on the other hand, shall bear their own respective costs and expenses, including, without limitation, fees, disbursements and other costs of any brokers, finders, investment bankers, attorneys, accountants and other advisors, in connection with this Agreement and the transactions contemplated hereby.

10.2 Notices. All notices under this Agreement shall be given to the Parties at the following addresses (i) by personal delivery; (ii) by certified mail, postage prepaid, return receipt requested; and (iii) by nationally recognized overnight or other express courier services:

If to KEMI:

Kentucky Employers' Mutual Insurance
250 West Main Street, Suite 900
Lexington, Kentucky 40507
Attn: Michelle Landers, General Counsel
Facsimile: _____

With a copy to:

Stoll Keenon Ogden PLLC
300 West Vine Street, Suite 2100
Lexington, Kentucky 40507
Attn: J. David Smith, Jr.
Facsimile: (859) 246-3662

If to the Rehabilitator:

With a copy to:

All notices shall be effective and shall be deemed delivered (i) if by personal delivery, on the date of delivery if delivered during normal business hours of the recipient, and if not delivered during such normal business hours, on the next Business Day following delivery; (ii) if by courier service, on the next Business Day after dispatch thereof; and (iii) if by mail, on the third (3rd) Business Day after dispatch thereof. Any Party hereto may change its address by notice to all Parties hereto delivered in accordance with this Section 10.2.

10.3 Amendments. No supplement, modification or waiver of this Agreement shall be binding unless in writing and executed by each Party hereto.

10.4 Waiver. At any time prior to the Closing, KEMI or the Rehabilitator may (a) extend the time for the performance of any of the obligations or other acts of the other Party hereto, (b) waive any inaccuracies in the representations and warranties of the other Party contained herein or in any document delivered pursuant hereto, and (c) waive compliance with any of the obligations of the other Party or any of the conditions to its own obligations contained herein to the extent permitted by law. Any agreement on the part of KEMI, on the one hand, and the Rehabilitator, on the other hand, to any such extension or waiver shall be valid only if set

forth in an instrument in writing signed on behalf of KEMI and the Rehabilitator. The failure of a Party to exercise any right or remedy shall not be deemed or constitute a waiver of such right or remedy in the future. No waiver of any of the provisions of this Agreement shall be deemed or shall constitute a waiver of any other similar or dissimilar provision hereof, nor shall any such waiver constitute a continuing waiver unless otherwise expressly provided.

10.5 Headings. The headings contained in this Agreement are for reference purposes only and shall not affect in any way the meaning or interpretation of this Agreement.

10.6 Assignment. Neither this Agreement nor any of the rights, interests or obligations hereunder shall be assigned by any of the Parties hereto (whether by operation of law or otherwise) to any Person without the prior written consent of the other Parties. Notwithstanding the foregoing, the rights, interests and obligations of the Rehabilitator shall automatically be assigned to any successor rehabilitator of the Fund.

10.7 Parties in Interest. This Agreement shall be binding upon and inure solely to the benefit of the Parties hereto and their successors (by way of successors in office, successors as rehabilitator of the Fund, merger, conversion or otherwise) and permitted assigns, and nothing in this Agreement, expressed or implied, is intended to confer upon any other Person any rights or remedies of any nature under or by reason of this Agreement.

10.8 Counterparts. This Agreement may be executed in two or more counterparts, each of which shall be deemed to constitute an original, but all of which shall constitute one and the same instrument, and shall become effective when one or more counterparts have been signed by each of the Parties hereto.

10.9 Severability. If any term, provision, covenant or restriction of this Agreement is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remainder of the terms, provisions, covenants and restrictions of this Agreement shall remain in full force and effect and shall in no way be affected, impaired or invalidated. It is hereby stipulated and declared to be the intention of the Parties that they would have executed the remaining terms, provisions, covenants and restrictions without including any of such which may be hereafter declared invalid, void or unenforceable. In such case, the Parties hereto shall promptly meet and negotiate substitute provisions for those rendered or declared illegal or unenforceable so as to preserve as nearly as possible the contemplated economic effects of the transactions contemplated hereby.

10.10 Entire Agreement. This Agreement and the exhibits, schedules and addenda hereto and the Related Agreements constitute the entire agreement among the Parties hereto and supersede all prior agreements and understandings oral or written, among the Parties hereto with respect to the subject matter hereof and thereof. There are no warranties, representations or other agreements between the Parties in connection with the subject matter hereof except as set forth specifically herein or in the Related Agreements or contemplated hereby or thereby.

10.11 Governing Law. This Agreement shall be governed by and construed according to the laws of the Commonwealth of Kentucky, without regard to or application of its conflict of laws principles. The Parties to this Agreement agree that the Court shall have exclusive jurisdiction, and the Parties hereby submit to such jurisdiction, of any dispute arising under or

related to this Agreement. **THE PARTIES HEREBY WAIVE ANY RIGHT TO A TRIAL BY JURY RESPECTING ANY CLAIM BROUGHT AGAINST THE OTHER PARTY ARISING OUT OF THIS AGREEMENT.**

10.12 Not Construed Against Any One Party. This Agreement is the result of negotiations among, and has been reviewed by, the Parties hereto. Accordingly, this Agreement shall be deemed to be the product of all Parties, and no ambiguity shall be construed in favor of or against any Party.

10.13 Enforcement. KEMI may either at law or in equity, by suit, action, mandamus or other Proceedings, enforce and compel performance by the Rehabilitator, the Fund and KSBIT (with respect to the Fund and rights and assets KSBIT holds or has held for the Fund), and their officers and agents of all duties imposed or required by Law or by this Agreement.

10.14 Rehabilitator's Liability Limited to the Fund. The obligations of Rehabilitator hereunder are as Rehabilitator of the Fund and the obligations of Rehabilitator hereunder shall be limited to the assets of the Fund, provided Rehabilitator shall be required to levy appropriate assessments against the Members of the fund to fund the Rehabilitator's and Fund's liabilities and obligations hereunder. Rehabilitator agrees not to withdraw as rehabilitator of the Fund, or seek or support any motion to withdraw as rehabilitator of the Fund, until such time as the Transfer Payment is paid in full. At any time after the Rehabilitator ceases to be Rehabilitator of the Fund, this Agreement shall be binding on the Fund.

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IN WITNESS WHEREOF, this Agreement has been duly executed and delivered by the duly authorized representatives of KEMI and the Rehabilitator on the date first above written.

REHABILITATOR:

_____

SHARON P. CLARK, COMMISSIONER OF THE KENTUCKY DEPARTMENT OF INSURANCE, IN HER CAPACITY AS REHABILITATOR OF THE KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION SELF-INSURANCE FUND

KEMI:

KENTUCKY EMPLOYERS' MUTUAL INSURANCE

By: _____

Jon E. Stewart, President and Chief Executive Officer

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ADDENDUM "A"

TO LOSS PORTFOLIO TRANSFER AGREEMENT

When used in the Loss Portfolio Transfer Agreement of which this Addendum "A" is a part, the following terms shall have the following meaning.

"Account" has the meaning assigned to it in Section 2.3.

"Additional Information" has the meaning assigned to it in Section 4.11.

"Affiliate" means, as applied to a specific Person, any Person that directly, or indirectly through one or more intermediaries, controls or is controlled by or is under common control with the Person specified. For purposes of this definition, "control" (including the terms "controlling," "controlled by" and "under common control with") shall mean the possession, directly or indirectly, of the power to direct or cause the direction of the management and policies of a Person, whether through the ownership of voting securities or by Contract or otherwise.

"Assessment" has the meaning assigned to it in Section 2.3.

"Agreement" means that certain Loss Portfolio Transfer Agreement of which this Addendum "A" forms a part.

"Assignment" has the meaning assigned to it in Section 3.2.

"Assumed Liabilities" has the meaning assigned to it in Section 2.1.

"Business Day" means any day other than a Saturday, Sunday or other day on which national or state banking associations are required or permitted by law to be closed in Kentucky.

"Claim" means any written action, suit, Proceeding, hearing, investigation, litigation, charge, complaint, claim or demand.

"Closing" has the meaning assigned to it in Section 3.1.

"Closing Date" has the meaning assigned to it in Section 3.1.

"Contracts" means shall mean with respect to a Person any legally binding written or oral agreement, arrangement, authorization, commitment, contract, indenture, instrument, lease (except for the Leases), obligation, plan, practice, restriction, order, permit, understanding or undertaking of any kind or character, or other document to which that Person is a party or that is binding on that Person or its equity capital, assets or business.

"Contracts of Coverage" has the meaning assigned to it in Section 2.1.

"Control Agreement" has the meaning assigned to it in Section 2.3.

"Court" has the meaning assigned to it in the Recitals to the Agreement.

"Depository" has the meaning assigned to it in Section 2.3.

"Due Date" has the meaning assigned to it in Section 2.3.

"Excess Policies" has the meaning assigned to it in Section 2.1.

"Fund" has the meaning assigned to it in the Recitals to the Agreement.

"Fund Disclosure Schedule" means that certain disclosure schedule delivered to KEMI by the Rehabilitator simultaneously with entering this Agreement.

"Fund Indemnitees" has the meaning assigned to it in Section 9.3.

"Fund Material Adverse Effect" means (a) an adverse effect on the validity or enforceability of this Agreement or any of the Related Agreements in any material respect, (b) an adverse effect on the condition (financial or other) of the Fund or assets or liabilities of the Portfolio, taken as a whole, in any material respect, or (c) an impairment of the ability of the Rehabilitator or Fund to fulfill its respective obligations under this Agreement or any of the Related Agreements in any material respect.

"Funding Commission Assessment" has the meaning assigned to it in Section 2.4.

"Funding Commission Portion" means each Member's share of the Funding Commission Assessment as provided in the assessment plan approved by the Rehabilitator and the Court.

"GAAP" means generally accepted accounting principles in the United States, consistently applied.

"Governmental Body" means any: (a) nation, state, county, city, town, village, district or other jurisdiction of any nature; (b) federal, state, local, municipal, foreign or other government; (c) governmental or quasi-Governmental Body of any nature (including any self-regulatory organization, governmental agency, branch, department, official or entity and any court or other tribunal); (d) multi-national organization or body; or (e) body exercising, or entitled to exercise, any administrative, executive, judicial, legislative, police, regulatory or taxing authority or power of any nature.

"IBNR" has the meaning assigned to it in Section 2.1.

"Indebtedness" of any Person means any obligations of such Person, whether or not contingent, (a) for borrowed money, (b) evidenced by notes, bonds, indentures or similar instruments, (c) for the deferred purchase price of goods and services, other than trade payables incurred in the ordinary course of business, (d) under capital leases, (e) that would be shown as debt on a balance sheet of such Person prepared in accordance with GAAP, and (f) in the nature of direct or indirect guarantees of the obligations described in clauses (a) through (e) above of any other Person.

"Indemnified Party" has the meaning assigned to it in Section 9.4.

"Individual Assessment" has the meaning assigned to it in Section 2.3.

"Initial Transfer Payment Installment" means the sum of (i) all of the cash, cash equivalents and securities held by the Fund as of Closing, less a reasonable reserve determined by the Rehabilitator for the cash needs of the Fund to pay obligations (other than the Transfer Payment) as they come due, including costs of administration of the rehabilitation, and after taking into account anticipated timing of receipt of the Assessment from the Members, and (ii) an amount equal to the entire Assessment collected as of Closing (less the Funding Commission Portion), but in no event shall the Initial Transfer Payment Installment be less than [$_____].

"Intellectual Property" means domestic patents and patent rights, trademarks and trademark rights, trade names and trade name rights, service marks and service mark rights, service name and service name rights, brand names, inventions, processes, formulae, copyrights, business and product names, logos, slogans, trade secrets, industrial models, designs, computer programs, business telephones, facsimile and e-mail addresses, websites and technology, and software (including all source codes) and related documentation, drawings, know-how, methods, processes, technology, engineering specifications, procedures, bills of material, trade secrets, all pending applications for and registrations of patents, trademarks, service marks and copyrights and any other intangible property, including all rights to any such property which is owned by and licensed from others and any goodwill associated with any of the above.

"Intercept" has the meaning assigned to it in Section 2.3.

"Installment Payment Agreement" has the meaning assigned to it in Section 2.3.

"Installment Payment Method" has the meaning assigned to it in Section 2.3.

"KEMI" has the meaning assigned to it in the first literary paragraph of the Agreement.

"KEMI Disclosure Schedule" means that certain disclosure schedule delivered to the Rehabilitator by KEMI simultaneously with entering this Agreement.

"KEMI Indemnitees" has the meaning assigned to it in Section 9.2

"KEMI Material Adverse Effect" means a material adverse effect on the ability of the Buyer to fulfill its obligations under this Agreement or any of the Related Agreements.

"KRS" has the meaning assigned to it in the Recitals to this Agreement.

"KSBIT" has the meaning assigned to it in the recitals to the Agreement.

"Laws" means all laws, statutes, rules, regulations, ordinances, judicial decisions, and other pronouncements having the effect of law of the United States, any foreign country or any domestic or foreign state, county, city or other political subdivision or of any Governmental Body.

"Liens" means any mortgage, pledge, assessment, security interest, lease, judgment lien, tax lien, mechanic's lien, materialman's lien, other lien, adverse claim, levy, option, right of first refusal, charge, debenture, indenture, deed of trust, right-of-way, restriction, encroachment, license, lease, security agreement, or other encumbrance of any kind, and other restrictions or limitations on the use or ownership of real or personal property or irregularities in title thereto or any conditional sale contract, title retention contract or other Contract to give any of the foregoing.

"Losses" has the meaning assigned to it in Section 9.2.

"Members" means all Persons who are or were members of the Fund (including any and all successors of Persons who were members of the Fund) at any time.

"Memorandum of Understanding" has the meaning assigned to it in Section 2.3.

"Necessary Future Assessments" has the meaning assigned to it in Section 7.1.

"Order" means any writ, judgment, decree, injunction, or similar order of any Governmental Body, in each such case whether preliminary or final.

"Ordinary Course Claim" has the meaning assigned to it in Section 4.7.

"Parties" and "Party" has the meaning assigned to it in the first literary paragraph of this Agreement.

"Petition" has the meaning assigned to it in the Recitals to the Agreement.

"Person" means any natural person, corporation, limited liability company, general partnership, limited partnership, proprietorship, other business organization, entity, trust, union, association or Governmental Body.

"Portfolio" has the meaning assigned to it in Section 2.1.

"Portfolio Costs and Expenses" has the meaning assigned to it in Section 7.2.

"Transfer Payment" has the meaning assigned to it in Section 2.2.

"Proceeding" means any action, suit, proceeding, arbitration, investigation or audit, whether or not by any Governmental Body.

"Records" has the meaning assigned to it in Section 2.1.

"Rehabilitation Case" means the Proceeding brought by the Rehabilitator before the Court pursuant to the Petition to rehabilitate the Fund pursuant to KRS Chapter 344, Subtitle 33.

"Rehabilitator" has the meaning assigned to it in the first literary paragraph of the Agreement, and includes the successors in office of the Commissioner of the Office of Insurance of the Commonwealth of Kentucky, and any other successor rehabilitator of the Fund.

"Related Agreements" means (a) the Assignment, (b) the Transition Services Agreement, (c) the Security Agreement, (d) the Control Agreement, (e) the Memorandum of Understanding, (f) the Installment Payment Agreements, and (g) any other agreement, certificate or similar document to be executed by any Party hereto in connection with this Agreement.

"Responsible Party" has the meaning assigned to it in Section 9.4.

"Retained Liabilities" has the meaning assigned to it in Section 2.1.

"Security Agreement" has the meaning assigned to it in Section 2.3.

"Self-Insurance Agreements" means the agreements entered into by the Members with the Fund or KSBIT providing for indemnity of the Fund and/or agreeing to be liable for liabilities of the Fund.

"Subrogation Rights" has the meaning assigned to it in Section 2.1.

"Subsequent Financial Statements" has the meaning assigned to it in Section 7.1.

"Third Party Claim" has the meaning assigned to it in Section 9.4.

"Transfer Payment" has the meaning assigned to it in Section 2.2.

"Transfer Order" has the meaning assigned to it in Section 6.1.

"Transition Services Agreement" has the meaning assigned to it in Section 3.2.

"Taxes" means any and all taxes, fees, levies, duties, tariffs, import, assessments and other charges, imposed by any taxing authority, together with any related interest, penalties or other additions to tax, or additional amounts imposed by any taxing authority, and without limiting the generality of the foregoing, shall include net income alternative or add-on minimum tax, gross income, gross receipts, sales, use, ad valorem, value added, franchise, profits, license, transfer, the Funding Commission Assessment, recording, escheat, withholding, payroll, employment, excise, severance, stamp, occupation, premium, property, windfall profit, environmental, custom duty, or other tax, governmental fee or other like assessment or charge of any kind whatsoever.

"Tax Returns" means all federal, state, local, provincial and foreign returns, declarations, claims for refunds, forms, statements, reports, schedules, and information returns or statements, and any amendments thereof (including, without limitation, any related or supporting information or Schedule attached thereto) required to be filed with any Taxing authority in connection with any Tax or Taxes.

"Transition Services Agreement" has the meaning assigned to it in Section 3.2.

"Transfer Order" has the meaning assigned to it in Section 6.1.

"Transferred Claims" has the meaning assigned to it in Section 2.1.

EXHIBIT "A"

Form of Installment Payment Agreement

INSTALLMENT PAYMENT AGREEMENT

THIS INSTALLMENT PAYMENT AGREEMENT (this "Agreement"), is by and between the board of education for the Kentucky school district identified below (the "Board of Education") and Sharon P. Clark, Commissioner of the Kentucky Department of Insurance (the "Rehabilitator"), in her capacity as Rehabilitator of the Kentucky School Boards Insurance Trust Workers Compensation Self-Insurance Fund (the "Fund").

RECITALS:

1. The Fund is a fund pursuant to which participating members, including the Board of Education, pooled their liabilities as a workers' compensation self-insured group under KRS 304.50-005, *et. seq.*

2. Due to a substantial deficit, the Fund was placed into rehabilitation (the "Rehabilitation") before the Franklin Circuit Court (the "Court"), pursuant to KRS Chapter 304, Subtitle 33, wherein the Rehabilitator was appointed rehabilitator of the Fund.

3. In connection with the Rehabilitation and pursuant to a Loss Portfolio Transfer Agreement ("LPT Agreement"), between the Rehabilitator and Kentucky Employers' Mutual Insurance ("KEMI") , which LPT Agreement has been approved by the Court, KEMI agreed to accept transfer of certain workers' compensation insurance obligations of the Fund in exchange for a transfer payment of Thirty-Five Million Dollars ($35,000,000) (the "Transfer Payment").

4. The members of the Fund, including the Board of Education, are jointly and severally liable for the Fund's liabilities and the Fund has insufficient assets to pay the Transfer Payment. The Rehabilitator on behalf of the Fund has assessed the members of the Fund an aggregate assessment of $_____ (the "Aggregate Assessment") to fund, *inter alia*, the payment of the Transfer Payment to KEMI and the payment of the special fund assessment to the Kentucky Workers' Compensation Funding Commission. The Aggregate Assessment was approved by the Court.

5. The Aggregate Assessment was allocated among the members liable therefor in a manner determined by the Rehabilitator to be fair and equitable, which allocation has been approved by the Court, and the allocation of the Aggregate Assessment to the Board of Education is as set forth below (the "Assessment").

6. As permitted by KRS 304.50-055(9) and approved by the Court, the Rehabilitator and KEMI have agreed that conditioned upon entering this Agreement, the Board of Education may pay its Assessment over a period of years, not to exceed six (6) years, and the Board of Education has elected to pay the Assessment as set forth below.

NOW THEREFORE, in consideration of the mutual covenants and promises herein contained, the Board of Education and the Rehabilitator, in its capacity as Rehabilitator of the Fund and for and on behalf of the Fund, agree as follows:

1. Basic Terms.[to be completed by Board of Education]:

(a) *Name of Board of Education.* The Board of Education is the board of education for: _____ [insert name of school district].

(b) *Approval.* The Board of Education approved this Agreement and the installment payments set forth herein at [complete and select one]:

_____ at a regular meeting held on _____[insert date] , pursuant to the duly adopted regular meeting schedule of the Board of Education that has been made available to the public; or

_____ at a special meeting of the Board of Education held on _____ insert date [date], pursuant to written notice duly given at least 24 hours in advance of the meeting to all Board of Education members and to local news media that have requested to be so notified, and posted at a conspicuous place at the offices of the Board of Education;

all in compliance with the applicable provisions of KRS 61.820 through 61.850.

(c) *Assessment Amount.* The Assessment upon the Board of Education is $_____ [insert amount].

(d) *Financing.* Unless indicated to the contrary below, the Board of Education will pay the Assessment in multiple installments, the first installment in an amount equal to 25% of the Assessment due and payable on or prior to [July 31, 2014] ("Initial Installment Date") and the balance paid as follows [select one]:

_____ in two additional annual installment payments each equal to 37.5% of the Assessment, the first of such additional installment payments due on July 31, 2015 and the remaining installment payments due on each July 31, 2016. On July 31, 2016, the entire unpaid balance of the Assessment is due and payable in full.

_____ in three additional annual installment payments each equal to 25% of the Assessment, the first of such additional installment payments due on July 31, 2015, and the remaining installment payments due on each July 31 thereafter until the Assessment is paid in full. On July 31, 2017, the entire unpaid balance of the Assessment is due and payable in full.

_____ in four additional annual installment payments each equal to 18.75% of the Assessment, the first of such additional installment payments due on July 31, 2015, and the remaining installment payments due on each July 31 thereafter until the Assessment is paid in full. On July 31, 2018, the entire unpaid balance of the Assessment is due and payable in full.

_____ in five additional annual installment payments each equal to 15% of the Assessment, the first of such additional installment payments due on July 31, 2015, and the remaining installment payments due on each July 31 thereafter until the Assessment is paid in full. On July 31, 2019, the entire unpaid balance of the Assessment is due and payable in full.

_____ in six additional annual installment payments each equal to 12.5% of the Assessment, the first of such additional installment payments due on July 31, 2015, and the remaining installment

payments due on each July 31 thereafter until the Assessment is paid in full. On July 31, 2020, the entire unpaid balance of the Assessment is due and payable in full.

_____ the Board of Education elects to pay the entire Assessment in full on or before the Initial Installment Date.

If any payment is due on a day other than a business day, the payment shall be due the last business day preceding such due date. If the Board of Education does not elect an installment payment option set forth above and approve this Agreement and cause its execution and delivery to the Rehabilitator at _____, on or before the Initial Installment Date, the Board of Education shall be required to pay the entire Assessment in full on the Initial Installment Date, unless the Rehabilitator and KEMI agree in writing to the contrary upon request by the Board of Education.

2. Payment. The Board of Education agrees to pay the Assessment in accordance with Section 1 of this Agreement. Such payments shall be due and payable without any right of set-off or deduction. The Assessment may be prepaid in whole or part at any time without penalty or premium. If at any time any payment is not paid when due, the past due payment shall accrue interest at a rate of twelve percent (12%) per annum until paid (or the highest rate permitted by law, if less).

3. Intercept. The Board of Education acknowledges and agrees that if it does not timely pay the Rehabilitator any payment when due hereunder, the Rehabilitator or KEMI may notify the Kentucky Department of Education ("DOE"), as assisted as necessary by the Kentucky Finance and Administration Cabinet ("FAC"), to withhold or intercept appropriations from the Commonwealth of Kentucky otherwise due to the Board of Education (the "Appropriations") to the extent of the payment then due. If at any time the Memorandum of Understanding by and among the DOE, FAC, the Rehabilitator and KEMI is canceled or terminated by any of the DOE, FAC or Rehabilitator, the entire Assessment, including all installment payments not yet paid, shall become immediately due and payable without any further action and, if such Assessment is not then paid in full immediately, the Rehabilitator and KEMI shall each have the right to cause the DOE to withhold or intercept the Appropriations to the extent of the Assessment then due. The Board of Education hereby releases and indemnifies the DOE, FAC, Rehabilitator and KEMI for effectuating any withholding or intercept of Appropriations.

4. Events of Default. The occurrence of any of the following events shall be deemed an "Event of Default": (i) the Board of Education fails to make any payment when due under this Agreement; (ii) the Board of Education breaches any other obligation under this Agreement; (iii) the Board of Education shall commence any case, proceeding or other action under any law relating to bankruptcy, insolvency, reorganization or relief of debtors, seeking to have an order for relief entered or seeking to adjudicate it as a bankrupt or insolvent, or seeking reorganization, arrangement, adjustment, winding-up, liquidation, dissolution, composition or other relief with respect to it or its debts, or seeking appointment of a receiver, trustee, custodian or other similar official for it or for all or any substantial part its assets or it shall make a general assignment for the benefit of their creditors; (iv) there shall be commenced against the Board of Education any case, proceeding or other action seeking issuance of a warrant of attachment, execution, distraint or similar process against all or any substantial part of its assets which continues undismissed and unstayed for a period of thirty (30) days or which results in the entry of an order for any such relief; (v) the Board of Education shall breach or default, beyond any period of grace with respect thereto, in any of the terms or conditions of any agreement covering any debt owing to any person or entity in excess of One Million Dollars ($1,000,000.00); or (vi) entry of a judgment in the amount of One Million Dollars ($1,000,000.00) or greater against the Board of Education, which remains unsatisfied or undischarged and in effect for thirty (30) days after such entry without a stay of enforcement or execution.

5. Remedies. Upon the occurrence of any Event of Default described in the foregoing Section 4, upon the election of Rehabilitator, the entire Assessment, including all installment payments not yet paid, shall be immediately due and payable (except where such Event of Default is under clause (iii) or (iv) of Section 4, in which event the entire Assessment, including all installment payments not yet paid, shall automatically become immediately due and payable without any election by or action of the Rehabilitator), and the Rehabilitator may exercise all rights and remedies under this Agreement and applicable law. The rights provided for in this Agreement are cumulative and not exclusive of any other rights, powers, privileges or remedies provided by law or in equity. Upon the occurrence of any Event of Default, the Rehabilitator may either at law or in equity, by suit, action, mandamus or other proceedings, enforce and compel performance by the Board of Education and its officers and agents of all duties imposed or required by law or by this Agreement.

6. General.

(a) *KEMI.* KEMI is relying on this Agreement and the obligations of the Board of Education in permitting the Board of Education to pay the Assessment in installments rather than as a lump-sum payment. As a result thereof, the Rehabilitator and Board of Education agree that KEMI is and shall be a third-party beneficiary of this Agreement and. the Board of Education and Rehabilitator agree not to modify or terminate this Agreement without the prior written consent of KEMI.

(b) *No Waiver.* Any waiver, forbearance, failure or delay by the Rehabilitator in exercising any right, power or remedy under this Agreement will not be deemed to be a waiver of such right, power or remedy, and any single or partial exercise of any right, power or remedy under this Agreement will not preclude the further exercise thereof; and every right, power and remedy of the Rehabilitator will continue in full force and effect until such right, power or remedy is specifically waived by an instrument in writing executed by the waiving party.

(c) *Submission to Venue and Jurisdiction and Waiver of Jury Trial.* The undersigned agree that any action or proceeding arising, directly, indirectly, or otherwise, in connection with, out of, or from this Agreement, any breach hereof, or any transaction covered hereby shall be resolved in, and the parties consent and submit to the sole and exclusive jurisdiction and venue of, the Franklin Circuit Court, Commonwealth of Kentucky. Notwithstanding the foregoing, if the enforcement of the Rehabilitator's or KEMI's rights or remedies herein requires pursuing an action or proceeding in an alternative or other court, such action or proceeding shall not be subject to the foregoing jurisdictional and venue exclusivity provision, and the Rehabilitator or KEMI may so pursue any such action or proceeding against the Board of Education in any court of competent jurisdiction. **THE PARTIES HEREBY WAIVE ANY RIGHT TO A TRIAL BY JURY RESPECTING ANY CLAIM BROUGHT AGAINST THE OTHER PARTY ARISING OUT OF THIS AGREEMENT.**

(d) *Governing Law.* The laws of the Commonwealth of Kentucky will govern the construction of this Agreement and the rights, remedies and duties of the parties hereto, without regard to principles of conflicts of laws.

(e) *Time of Essence.* Time will be of the essence in the performance of the Board of Education's obligations under this Agreement.

(f) *Heirs, Successors and Assigns Bound.* This Agreement will bind and inure to the benefit of the successors and assigns of the Board of Education, Rehabilitator and the Fund, and will bind the Board of Education, Rehabilitator and the Fund, and all successors and permitted assigns of any of them.

(g) *Assignment.* The Board of Education may not assign this Agreement without the prior

written consent of the Rehabilitator. The Rehabilitator may assign its rights and interests herein to any person, including KEMI.

(h) *Severability of Provisions*. A judicial decree, order or judgment holding any provision herein invalid or unenforceable will not in any way impair or preclude enforcement of the remaining provisions herein, and will not in any way impair or preclude enforcement of rights or remedies of the Rehabilitator under applicable law or their right to collect the Assessment.

(i) *Counterpart Execution*. This Agreement may be executed in several counterparts, any of which will be treated for all purposes as an original, and all of which will be treated as one and the same Agreement.

(j) *Notices*. All notices under this Agreement shall be given to the parties at the following addresses (i) by personal delivery; (ii) by certified mail, postage prepaid, return receipt requested; and (iii) by nationally recognized overnight or other express courier services:

If to the Rehabilitator:

[insert]

If to the Board of Education, to the attention of the Superintendent at the Board of Education's principal office address.

All notices shall be effective and shall be deemed delivered (i) if by personal delivery, on the date of delivery if delivered during normal business hours of the recipient, and if not delivered during such normal business hours, on the next business day following delivery; (ii) if by courier service, on the next business day after dispatch thereof; and (iii) if by mail, on the third (3rd) business day after dispatch thereof. Any party hereto may change its address by notice to all parties hereto delivered in accordance with this Section 6(j).

(k) *Headings*. Section headings used in this Agreement are for convenience only and are not part of this Agreement.

(l) *Joint and Several Liability*. The Board of Education acknowledges that this Agreement and its performance hereunder in no way limits or reduces its joint and several liability with the other members of the Fund for the liabilities and obligations of the Fund.

(m) *Integration and Modification*. This Agreement comprises the entire agreement between the Board of Education and Rehabilitator concerning its subject matter. Any modification to this Agreement must be made in writing and signed by the party against whom the modification is sought to be enforced.

IN WITNESS WHEREOF, the undersigned have executed this Agreement as of the date first above written.

Board of Education for the School District of

_____
(print school district name)

By: _____

Name: _____

Title: _____

_____
Sharon P. Clark, Commissioner of the Kentucky Department of Insurance, in her capacity as Rehabilitator of the Kentucky School Boards Insurance Trust Workers Compensation Self-Insurance Fund

EXHIBIT "B"

Memorandum of Understanding

Memorandum of Understanding
Commonwealth of Kentucky
Between
Kentucky Department of Education
Kentucky Department of Insurance
The Finance and Administration Cabinet
And
Kentucky Employers' Mutual Insurance

THIS MEMORANDUM OF UNDERSTANDING (**MOU**) is made and entered into the ____ day of _____, 20___ by and between the Commonwealth of Kentucky, Kentucky Department of Education, hereinafter known as "**KDOE**," the Kentucky Department of Insurance, hereinafter known as "**KDOI**" or "**Rehabilitator,**" the Finance and Administration Cabinet, hereinafter known as "**FAC,**" and Kentucky Employers' Mutual Insurance, hereinafter known as "**KEMI**."

W I T N E S S E T H:

WHEREAS, the Kentucky School Boards Insurance Trust (KSBIT) self-insured workers' compensation fund has become insolvent and subject to the rehabilitation authority of the Kentucky Commissioner of Insurance; and

WHEREAS, it is the intention of the Kentucky Commissioner of Insurance to exercise her authority under KRS 304.33-010 et seq. and file a petition for the rehabilitation of the KSBIT workers compensation fund and implement a plan of assessment for the recoupment of the accrued deficit of said fund; and

WHEREAS, it is the intention of the Kentucky Commissioner of Insurance to cause a guarantee of payment of the assessment for the benefit of KEMI, as loss portfolio transferee of the KSBIT workers' compensation fund and liabilities pursuant to that certain Loss Portfolio Transfer Agreement filed with the Franklin Circuit Court, as it may be amended ("LPT Agreement"); and

WHEREAS, KDOE has the statutory authority and duty under KRS 160.160 and KRS 304.50-055 to intercept and pay funds otherwise due to an individual school district

in satisfaction of any default by that school district in the payment of financing for its liability under the assessment;

NOW THEREFORE, the parties agree as follows:

In order to ensure payment of the assessment by individual school districts, the Support Education Excellence in Kentucky funds and other appropriations to a local school district will be intercepted by KDOE, with any necessary assistance from the state FAC, when a local school district does not make a timely payment of funds in accordance with its installment payment agreement, all as provided in KRS 160.160, KRS 304.48-250 and KRS 304.50-055. KDOE will initiate such intercept upon written certification by KDOI or KEMI that any school district has not made timely payment of funds in accordance with its installment payment agreement. Upon receipt of such written certification, KDOE shall immediately withhold or intercept any payment due to such local school district from the Commonwealth of Kentucky (to the extent of the amount of the required payment) and remit such payment to the Rehabilitator for deposit into the Account (as defined in the LPT Agreement) and the Rehabilitator will remit such funds to KEMI when due under the LPT Agreement. Withholding or interception shall occur from any General Fund amounts which are allotments to the local school district in the current budget biennium.

This MOU will apply to allotments to the local school district in future budget bills.

The KDOE and the state FAC also agree that, they shall take all reasonable steps necessary and within their respective statutory authority, in order to address a default by a school district in paying its assessment when due.

Access to Records:

KEMI agrees that the Finance and Administration Cabinet, the Auditor of Public Accounts, and the Legislative Research Commission, or their duly authorized representatives, shall have access to any books, documents, papers, records, or other evidence, which are directly pertinent to this contract for the purpose of financial audit or program review. KEMI recognizes that any books, documents, papers, records, or

other evidence, received during a financial audit or program review shall be subject to the Kentucky Open Records Act, KRS 61.870 to 61.884.

Choice of Law and Forum:

The laws of the Commonwealth of Kentucky shall govern all questions as to the execution, validity, interpretation, construction, and performance of this agreement or any of its terms. Any suit, action or other proceeding regarding the execution, validity, interpretation, construction, or performance of this MOU shall be filed in the Franklin Circuit Court of the Commonwealth of Kentucky.

General:

This MOU shall be binding upon and inure solely to the benefit of the parties hereto and their successors and assigns. This MOU, together with the LPT Agreement once fully executed, constitutes the entire agreement among the parties hereto with respect to the subject matter hereof and thereof.

No supplement, modification or waiver of this MOU shall be binding unless in writing and executed by each party hereto. No waiver of any of the provisions of this MOU shall be deemed or shall constitute a waiver of any other similar or dissimilar provision hereof, nor shall any such waiver constitute a continuing waiver unless otherwise expressly provided.

If any term, provision, covenant or restriction of this MOU is held by a court of competent jurisdiction to be invalid, void or unenforceable, the remainder of the terms, provisions, covenants and restrictions of this MOU shall remain in full force and effect and shall in no way be affected, impaired or invalidated. It is hereby stipulated and declared to be the intention of the parties that they would have executed the remaining terms, provisions, covenants and restrictions without including any of such which may be hereafter declared invalid, void or unenforceable. In such case, the parties hereto shall promptly meet and negotiate substitute provisions for those rendered or declared illegal or unenforceable so as to preserve as nearly as possible the contemplated economic effects of the transactions contemplated hereby.

The execution and delivery of this MOU by the parties hereto is a condition precedent to KEMI's obligations under the LPT Agreement. Consequently, the parties recognize KEMI is relying on this MOU and the terms hereof and would not consummate the transactions contemplated by the LPT Agreement without this MOU.

The Rehabilitator, KEMI or both of them may either at law or in equity, by suit, action, mandamus or other proceedings, enforce and compel performance by the KDOE, FAC, KDOI and their officers and agents of all duties imposed or required by law or by this MOU.

Approvals:

This Memorandum of Understanding is subject to the terms and conditions as stated. By affixing signatures below, the parties agree that electronic approvals may serve as electronic signatures. This MOU may be executed in two or more counterparts, each of which shall be deemed to constitute an original, but all of which shall constitute one and the same instrument, and shall become effective when one or more counterparts have been signed by each of the parties hereto. In addition, the parties verify that they are authorized to bind this agreement between parties and that they accept the terms of the agreement.

_____ _____

Terry Holliday, Commissioner
Kentucky Department of Education

Date

_____ _____

Lori Hudson Flanery, Secretary
Kentucky Finance & Administration Cabinet

Date

_____ _____

Sharon Clark, Commissioner
Kentucky Department of Insurance,
in her capacity as Commissioner and Rehabilitator

Date

KEMI:

KENTUCKY EMPLOYERS' MUTUAL INSURANCE

By: _____ _____
Jon E. Stewart, President and Chief Executive Officer — Date

Approved as to form and legality:

_____ _____
Attorney — Date
Kentucky Department of Education

_____ _____
Attorney — Date
Kentucky Finance & Administration Cabinet

_____ _____
Attorney — Date
Kentucky Department of Insurance
Public Protection Cabinet

_____ _____
Attorney — Date
Kentucky Employers' Mutual Insurance

EXHIBIT "C"

Security Agreement

SECURITY AGREEMENT

THIS SECURITY AGREEMENT (this "Agreement") is made and entered into as of _____ ____, 20__, by and between **SHARON P. CLARK, COMMISSIONER OF THE KENTUCKY DEPARTMENT OF INSURANCE, IN HER CAPACITY AS REHABILITATOR OF THE KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION SELF-INSURANCE FUND** ("Debtor") and **KENTUCKY EMPLOYERS' MUTUAL INSURANCE** ("Secured Party"). Reference is made to that certain Loss Portfolio Transfer Agreement, dated _____ ____, 2013 (the "LPT Agreement"), by and between Debtor and Secured Party. Capitalized terms used in this Agreement and not otherwise defined shall have the meanings assigned to them in the LPT Agreement.

WITNESSETH:

Secured Party and Debtor, in her capacity as Rehabilitator of the Fund and for and on behalf of the Fund, agree as follows:

1. **Grant of Security Interest by Debtor to Secured Party**. For good and valuable consideration, the receipt and sufficiency of which is acknowledged by Debtor, Debtor does hereby grant unto Secured Party a first and prior security interest and lien in and to, and pledges, all the "Collateral" as defined and described in numerical paragraph two (2) hereof to secure all of the "Indebtedness" as defined and described in numerical paragraph three (3) hereof.

2. **Collateral**. The Collateral covered by this Agreement is all property described in Schedule "A" attached hereto and incorporated herein by reference, and any supplemental exhibits or schedules thereto, and all proceeds and products thereof (all of which collateral is herein collectively referred to as the "Collateral").

3. **Indebtedness Secured**. This Agreement is made as collateral security for the payment and performance of all of the following obligations (the "Indebtedness"):

(a) **Transfer Payment and LPT Agreement**. Debtor's obligation to pay Secured Party the $35,000,000 Transfer Payment due under the LPT Agreement and all other obligations of the Rehabilitator or Fund to KEMI under the LPT Agreement, whether now existing or hereafter arising; and

(b) **Expenditures for Collateral**. The repayment of any amounts that Secured Party may advance or spend for the care, maintenance or preservation of the Collateral, and any other expenditures that Secured Party may make under the provisions of this Agreement or for the benefit of the Debtor.

4. Perfection of Security Interest.

(a) **Filing of Financing Statements**.

(i) Debtor hereby authorizes Secured Party to file financing statements (the "Financing Statements"), in such places as Secured Party deems appropriate, describing the Collateral (including a description as all assets of Debtor). Debtor, at the request of Secured Party, will execute such Financing Statements.

(ii) Debtor authorizes Secured Party to file such Financing Statements describing any agricultural liens or other liens held by Secured Party.

(b) **Possession**.

(i) Debtor will have possession of the Collateral, except where expressly otherwise provided in this Agreement, or where following an "Event of Default" (as defined below) and during any continuance thereof Secured Party elects to take possession of the Collateral.

(ii) Where Collateral is in the possession of a third party, Debtor will join with Secured Party in notifying the third party of Secured Party's security interest and obtaining an acknowledgment from the third party that it is holding the Collateral for the benefit of Secured Party.

(c) **Control**. Debtor will cooperate with Secured Party in obtaining control with respect to any Collateral consisting of deposit accounts, investment property, letters of credit rights and electronic chattel paper.

(d) **Marking of Chattel Paper**. Debtor will not create any chattel paper without placing a legend on the chattel paper acceptable to Secured Party indicating that Secured Party has a security interest in the chattel paper.

5. Representations and Warranties of Debtors.

(a) **Organization and Existence**. The Fund is a workers' compensation self-insured group under KRS 304.50-005, *et. seq.* and holds a valid certificate from the Kentucky Office of Insurance as required by KRS 304.50-005, *et. seq.* The Rehabilitator has been appointed rehabilitator of the Fund pursuant to KRS Chapter 304, Subtitle 33 and has all requisite power and authority as rehabilitator of the Fund under KRS Chapter 304, Subtitle 33. Debtor has all necessary authority, powers and qualifications to carry on the business now conducted by it and to be conducted by it and to enter into the transactions described herein.

(b) **Authorization and Enforceability**. The execution, delivery and performance of this Agreement by Debtor has been duly authorized by all necessary action by Debtor, and this Agreement has been duly executed and delivered by Debtor and constitutes the legal, valid and binding obligations of Debtor and is enforceable in accordance with its terms.

(c) **Ownership of Collateral**.

(i) Debtor is the absolute owner of the legal and beneficial title to all of the Collateral, (exclusive of hereafter acquired, replaced or created items), and is in full possession thereof.

(ii) The Collateral is free and clear of all liens, encumbrances and adverse claims whatsoever, except for the security interest created in favor of Secured Party by this Agreement.

6. Covenants of Debtors.

(a) **Payment and Performance of Indebtedness**. The Indebtedness will be paid and performed by Debtor to Secured Party in accordance with the terms of the LPT Agreement.

(b) **Payment and Performance of Other Obligations**. Debtor will comply in all respects with any and all agreements between Debtor and Secured Party.

(c) **Use of Collateral**. All the Collateral is used or will be used for business purposes only.

(d) **Defense of Claims Against Collateral**. Debtor will defend the Collateral against the claims and demands of all persons.

(e) **Cooperation of Debtor in Perfection of Security Interest**.

(i) Debtor will execute and deliver to Secured Party upon request new UCC-1 Financing Statements describing the Collateral specified herein for recordation where necessary in Secured Party's sole discretion to perfect Secured Party's security interest in the Collateral, and Debtor will pay all filing and recording fees and filing and recording taxes in connection with the filing and/or recordation of such Financing Statements, and, if paid by the Secured Party, Debtor will reimburse Secured Party therefor upon demand of Secured Party.

(ii) This Agreement may, in the sole discretion of Secured Party, be filed as a financing statement and Debtor agrees to also execute any additional financing statements with respect hereto which may be requested by Secured Party.

(iii) Secured Party may, in its sole discretion, deliver this Agreement or

any other document executed pursuant hereto or in connection herewith with any person or organization which registers, sells or is in any manner involved with any or all of the Collateral. Secured Party will be entitled to notify the person in possession of the Collateral, or any other person Secured Party deems appropriate of the security interest herein granted and to notify such person or entity to forward all documents with respect to the Collateral to Secured Party and otherwise as Secured Party deems appropriate. Secured Party may post, in a conspicuous place at any and all locations where the Collateral may be located, a notice stating Secured Party's interest in the Collateral.

(f) **Prohibition of Additional Security Interests or Liens**. Debtor will not:

(i) permit any loan or security interest (other than Secured Party's security interest granted herein) to attach to any of the Collateral;

(ii) permit any of the Collateral to be levied upon under any legal process; or

(iii) dispose of or enter or agree to enter into any sale of any of the Collateral, without prior written consent of Secured Party.

(g) **Inspection of Collateral and Debtor's Records**. Debtor will permit Secured Party and/or its agents to inspect and appraise the Collateral and inspect the books and records of Debtor at all reasonable times and from time to time.

(h) **Change in State of Organization, Name or Reorganization**. Debtor will not change the type of entity the Fund now is, nor incorporate nor organize the Fund in another state or foreign jurisdiction nor permit the Fund to conduct business under any other name than "The Kentucky School Boards Insurance Trust Workers' Compensation Self-Insurance Fund" nor change or reorganize the type of business entity under which it does business except upon prior written approval of Secured Party. If such approval is given, Debtor agrees that all documents, instruments and agreements demanded by Secured Party will be prepared and filed at Debtor's expense before such change of name or business entity occurs.

(i) **Notification Requirements of Debtor**. Debtor will notify Secured Party in writing of any proposed change in any of Debtor's state of organization, principal office or place of business, or mailing address, at least thirty (30) days prior thereto.

7. Limited Power of Attorney to Secured Party.

(a) Debtor hereby irrevocably appoints Secured Party as Debtor's attorney-in-fact to do all acts and things which Secured Party may deem necessary or appropriate to perfect and continue perfected the security interest created by this Agreement and to protect and, in case of an Event of Default hereunder, sell the Collateral, including, but not limited to, the execution in Debtor's name as Debtor's irrevocable attorney-in-fact:

(i) notifications and agreements to sell where sale is permitted;

(ii) any documents or papers necessary or helpful to comply with the terms of any agreements relative to any of the Collateral; and

(iii) UCC-1 (and other) Financing Statements covering the Collateral and filing and recordation of same wherever Secured Party deems appropriate, with Debtor to reimburse Secured Party for all filing and recording fees, taxes and other expenses in connection therewith upon demand of Secured Party.

(b) Provided, however, the power of attorney granted hereby will survive the disability of the principal, but when all the Indebtedness is fully paid and performed, this power of attorney will become null and void upon Secured Party's receipt of written notification from Debtor to such effect.

8. **Events of Default**. An "Event of Default" under this Agreement will occur upon any default in, or breach of, any covenant (including without limitation any promise to pay money) agreement, representation or warranty by Debtor under the provisions of: (i) the LPT Agreement (subject to any applicable grace or cure periods), (ii) any other agreement regarding any of the Indebtedness (subject to applicable grace and cure periods), and (iii) this Agreement (provided Debtor shall have fifteen (15) days after written notice of any non-monetary default or breach hereunder to cure the same).

9. **Remedies Upon Event of Default**.

(a) Upon the occurrence of any "Event of Default," Secured Party will have all rights and remedies in and against the Collateral and otherwise of a secured party under Chapter 355 of the Kentucky Revised Statutes (the "UCC") and the other applicable law of Kentucky (and all such other states where any part of the Collateral may be located, if applicable) and all other applicable laws and all rights provided herein, in all other documents evidencing, securing or related to any of the Indebtedness (including without limitation the LPT Agreement), or in any other applicable agreement, all of which rights and remedies will, to the full extent permitted by law, be cumulative.

(b) In addition, upon the occurrence and during the continuance of any "Event of Default", Secured Party will have the right, to collect and receive directly from third parties payments due with respect to the Collateral and the right to sell the Collateral at public or private sale. If Secured Party realizes upon Collateral by receiving payments due with respect to Collateral from a Person other than Debtor (including Members of the Fund or the Depository), Secured Party will notify Debtor of such receipt of payment from such third party. The requirement of reasonable notice of the time and place of disposition of Collateral by Secured Party will be conclusively deemed to have been met if such notice is mailed, postage prepaid, to Debtor's address specified above at least ten (l0) days before the time of the sale or disposition. Secured Party may bid upon and purchase any or all of the Collateral at any public sale thereof. Secured Party may dispose of all or any part of the Collateral at one or more times and from time

to time and in one or more lots or parcels, and upon such terms and conditions, including a credit sale, as Secured Party determines in its sole discretion.

(c) Secured Party will apply the net proceeds of any such disposition of the Collateral (after deducting therefrom all costs incurred in connection therewith, or incidental to the holding, preparing for sale, in whole or in part, of the Collateral, including Secured Party's attorneys' fees and court costs) to the Indebtedness and any other obligations of Debtor to Secured Party in the order elected by Secured Party in its sole discretion, and any remaining proceeds will be paid to the Debtor or such other party as is entitled thereto.

(d) Secured Party may exercise its right of set off with respect to the Indebtedness in the same manner as if the Indebtedness were unsecured.

(e) Debtor agrees to pay to Secured Party, as part of the Indebtedness, all amounts paid by Secured Party, including, but not limited to:

(i) Secured Party's attorneys' fees, to the extent not prohibited by applicable law, in connection with the enforcement of any of Debtor's obligations hereunder or contained in the documents evidencing the Indebtedness, with interest thereon at the highest rate provided for in any of the Indebtedness,

(ii) for taxes, levies and prior liens and insurance on, repairs to, maintenance of, or transporting or otherwise caring for, the Collateral, and

(iii) in collecting, taking possession of or preserving the Collateral.

10. Supplemental and Miscellaneous Provisions.

(a) **Continuing Agreement with Respect to Credit Agreement**. This is a continuing security agreement with respect to the LPT Agreement and Transfer Payment due thereunder and all the rights, powers and remedies hereunder will apply to any and all extensions, renewals, amendments or modifications of the LPT Agreement and Transfer Payment due thereunder.

(b) **Rights and Remedies of Secured Party are Cumulative**. The rights, powers and remedies given to Secured Party by this Agreement will be in addition to all rights, powers and remedies given to the Secured Party by virtue of any other agreement now existing or subsequently entered into by and between the parties hereto and any statute or rule of law.

(c) **No Waiver by Secured Party**. Any waiver, forbearance, failure or delay by Secured Party in exercising any right, power or remedy hereunder will not be deemed to be a waiver of such right, power or remedy, and any single or partial exercise of any right, power or remedy hereunder will not preclude the further exercise thereof; and every right, power and remedy of Secured Party will continue in full force and effect until such right, power or remedy is specifically waived by an instrument in writing executed by Secured Party.

(d) **Submission to Venue, Jurisdiction and Service of Process; Waiver of Jury Trial**. The undersigned agree that any action or proceeding arising, directly, indirectly, or otherwise, in connection with, out of, or from this Agreement, any breach hereof, or any transaction covered hereby shall be resolved in, and the parties consent and submit to the sole and exclusive jurisdiction and venue of, the Franklin Circuit Court, Commonwealth of Kentucky. Notwithstanding the foregoing, if the enforcement of the Secured Party's rights or remedies herein requires pursuing an action or proceeding in an alternative or other court, such action or proceeding shall not be subject to the foregoing jurisdictional and venue exclusivity provision, and Secured Party may so pursue any such action or proceeding against Debtor in any court of competent jurisdiction. **THE PARTIES HEREBY WAIVE ANY RIGHT TO A TRIAL BY JURY RESPECTING ANY CLAIM BROUGHT AGAINST THE OTHER PARTY ARISING OUT OF THIS AGREEMENT.**

(e) **Governing Law**. The laws of the Commonwealth of Kentucky will govern the construction of this Agreement and the rights, remedies and duties of the parties hereto, unless the laws of the state where the Collateral or part thereof is situated dictate that the laws of such other state will govern with respect thereto.

(f) **Time of Essence**. Time will be of the essence in the performance of Debtor's obligations under this Agreement.

(g) **Heirs, Successors and Assigns Bound**. This Agreement will bind and inure to the benefit of the successors and assigns of Secured Party and will bind the Fund and Rehabilitator, and all successors and assigns of either, and all persons who become bound as a debtor under this Agreement. Secured Party does not consent to any assignment by Debtor except as expressly provided in this Agreement.

(h) **Assignment**. Secured Party may assign its rights and interests under this Agreement to any permitted assignee of the LPT Agreement in connection with assignment of the LPT Agreement. Debtor may not assign this Agreement without the prior written consent of Secured Party. If an assignment is made, Debtor will render performance under this Agreement to the assignee. Debtor waives and will not assert against any assignee any claims, defenses, or setoffs which Debtor could assert against Secured Party except defenses which cannot be waived.

(i) **Severability of Provisions**. A judicial decree, order or judgment holding any provision herein invalid or unenforceable will not in any way impair or preclude enforcement of the remaining provisions herein, and will not in any way impair or preclude enforcement of rights or remedies of Secured Party under the UCC, or other applicable law.

(j) **Counterpart Execution**. This Agreement may be executed in several counterparts, any of which will be treated for all purposes as an original, and all of which will be treated as one and the same Agreement.

(k) **Notices**. Any notices required by this Agreement or under the UCC must be sent and will be deemed delivered by and to Secured Party and Debtor in accordance with the terms of the LPT Agreement.

(l) **Headings**. Section headings used in this Agreement are for convenience only and are not part of this agreement.

(m) **Integration and Modification**. This Agreement, the LPT Agreement and any other agreements executed in connection herewith and therewith comprise the entire agreement between the Debtor and Secured Party concerning the subject matter hereof. Any modification to this Agreement must be made in writing an signed by the party against whom the modification is sought to be enforced.

IN TESTIMONY WHEREOF, witness the signature of the parties hereto.

SHARON P. CLARK, COMMISSIONER OF THE KENTUCKY DEPARTMENT OF INSURANCE, IN HER CAPACITY AS REHABILITATOR OF THE KENTUCKY SCHOOL BOARDS INSURANCE TRUST WORKERS' COMPENSATION SELF-INSURANCE FUND

"DEBTOR"

KENTUCKY EMPLOYERS' MUTUAL INSURANCE

By: _____
Jon E. Stewart,
President and Chief Executive Officer

"SECURED PARTY"

SCHEDULE "A"

The property covered by this Agreement includes all of Debtor's right, title and interest in, to and under the following described property, whether now owned or hereafter acquired by Debtor, and whether now existing or hereafter created, arising, accruing, incurred or entered into (all of which is hereinafter collectively called the "Collateral"):

1. All of Debtor's rights to payment of assessments against the members (the "Members") of The Kentucky School Boards Insurance Trust Workers' Compensation Self-Insurance Fund (the "Fund"), whether now in existence or arising from time to time hereafter, including, without limitation, rights under those certain Installment Payment Agreements between Debtor and each Member that joins in such an Installment Payment Agreement (collectively, the "Assessment Receivable").

2. Each and every Installment Payment Agreement between Debtor and any Member and all sums of money due and to become due thereunder, as the same may be modified, supplemented or amended from time to time in accordance with its terms.

3. That certain **[describe Account(s)]** held by **[Depository]** and all other deposit and other accounts into which any payments of the Assessment Receivable is deposited.

4. All "Proceeds", as such term is defined in the Uniform Commercial Code of the Commonwealth of Kentucky, as in effect from time to time, of the foregoing.