

WHAT A
DIFFERENCE
A DECADE
MAKES



THE BEACON MUTUAL INSURANCE COMPANY

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President & Chief Executive Officer

The Beacon Mutual Insurance Company

Mr. Joseph A. Solomon

President & Chief Executive Officer

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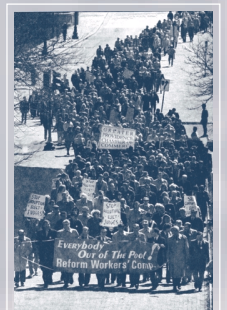
Vice President Claims

Mr. Paul W. Redman

Vice President Information Systems

Cover Photo: Historic march on the State House, organized by the Greater Providence Chamber of Commerce. Over 2,000 business leaders joined together to protest rising workers' compensation premiums.

March 29, 1990



Providence Journal Photo

MESSAGE FROM THE PRESIDENT AND CHAIRMAN

This year's annual report focuses on the strides that have been made in improving the workers' compensation system in Rhode Island over the past ten years. This remarkable story was made possible due to a concerted effort that took our system from the brink of disaster to a national model of success. With the support of our legislators, the Workers' Compensation Court, the medical and agent community and of course the joint effort of business and labor, the employers of Rhode Island are reaping the benefits of a system that is functioning properly. In fact, during the past 11 years there has not been a single rate increase in Rhode Island, a statement few states, if any, can claim.

The Beacon is proud to have played a part in the overall stabilization and proper functioning of the workers' compensation system. Our story is equally remarkable in what we have accomplished and the successes we have achieved.

During the past ten years, Rhode Island employers insured with The Beacon have saved over \$775 million in premium payments relative to premiums paid in 1993, the first year we started writing business in the state. These savings have resulted from rate decreases, dividends, shared earnings, scheduled credits and safety group reimbursements. The average premium of \$2.10 per \$100 in payroll paid by our policyholders in 2003 was 46.5% less than the \$3.93 that was paid in 1993. In addition, over the past ten years, The Beacon has paid over \$60 million in assessments to the Administrative Fund that supports the workers' compensation system in Rhode Island.

This past year marked another successful chapter for The Beacon. The Company's net written premiums grew from \$134.7 to \$149.8 million, an 11% increase. We implemented our new underwriting and claims software program, PowerComp, which will improve our company's efficiency, service and data analysis abilities. We also launched our PRIDE initiative that defines our values of Professionalism, Respect, Integrity, Dedication and Excellence. Our employees have been the foundation of our success and our PRIDE initiative encompasses those values that will make our vision a reality.

Our commitment to providing unparalleled service remains our major objective. In this regard, we have devoted much effort into developing a Loss Prevention staff with expertise that is unmatched in the industry. Their efforts, combined with the efforts of Rhode Island employers and employees in recognizing the importance of safety, are making our workplaces safer. Similar efforts have been made in our Claims Department in order to ensure that injured workers receive timely and proper treatment to facilitate their recovery and return to gainful employment. Our underwriting staff continues to develop products and programs to meet the needs of our policyholders.

Much has happened during the past decade and, although the story has been one of success, the story is not over. We believe that there are more goals to be achieved and more benefits to be realized. We want to continue to improve and maintain our position as the workers' compensation insurer of choice in Rhode Island.



Mr. Joseph A. Solomon,
President and Chief Executive Officer



Mr. Sheldon S. Sollosy,
Chairman of the Board

In the early 1990's, the workers' compensation system was in shambles. Then Governor Bruce Sundlun, the General Assembly, the Workers' Compensation Court, business leaders, the medical and agent community, and organized labor joined forces to devise a multi-tier plan to return stability to the state's workers' compensation system.

Thus creating The Beacon Mutual Insurance Company.



1993

WHAT A
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MAKES

2003



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The Beacon is critical to the Rhode Island economy based on the services it offers to Rhode Island businesses, the jobs it creates, the expenditures it makes, the tax revenue it provides to state and local authorities, the investments it makes in the economy and the savings in premiums to Rhode Island businesses.

”

Edward M. Mazze, PH.D
Dean of the College of Business Administration
University of Rhode Island



At The Beacon Mutual Insurance Company, an essential element of our company vision is to remain “the workers’ compensation insurer of choice in Rhode Island.” With currently 70% of the market share for workers’ compensation insurance, we are proud of the growth and success we have earned since our humble beginnings as a competitive mutual insurance company.

Workers’ comp:
IT’S A MONSTER
Providence Journal, Jan. 13, 1991

In 1988, the incurred losses in workers’ compensation claims were in excess of \$56.2 million. Peter Burton, then-director of the National Council on Compensation Insurance (NCCI), declared “the Rhode Island workers’ compensation program is probably the most out-of-balance system in the United States” (Workers’ Compensation, Terry Thomason, Timothy P. Schmidle and John Burton 2001). With a 32% rate increase approved by the Department of Business Regulation, and a proposed 123% rate hike by the NCCI, Rhode Island’s workers’ compensation system was in dire need of a major overhaul. Insurance companies were losing money rapidly and many were forced to cease the writing of new policies. In addition, local employers claimed that rising premiums were devastating their business – forcing them to leave the state or go out of business entirely. Highly publicized stories of companies leaving Rhode Island were prevalent. A 90-year old truck body manufacturer left Rhode Island for Pennsylvania, expecting to save over \$500,000 in workers’ compensation costs, with many more companies tempted to do the same.

123% workers comp rate hike debated
Attorney general’s office calls it ‘outrageous’; petitioner says it’s vital
Providence Journal, Feb. 8, 1991

The culmination of a community outraged by a system that was failing at all levels, came in the form of a protest rally at the State House. Over 2,000 small business leaders joined with the Greater Providence Chamber of Commerce on March 29, 1990, to protest rising insurance premiums. Many carried banners that read “Everyone out of the (assigned-risk) pool,” in response to the more than 90% of Rhode Island employers that were forced into the state-assigned risk pool.

Workers’ comp ‘clearly isn’t working’
Buffeted by spiraling costs, lawsuits and competing interests
Providence Journal, April 21, 1991

With the system in shambles, the Governor, the General Assembly, the Workers’ Compensation Court, business leaders, the medical and agent community, and organized labor joined forces to devise a multi-tier plan to return stability to the state’s workers’ compensation system. In 1991, legislation was enacted for the creation of the State Compensation Insurance Fund (SCIF), “an independent public corporation for the purpose of insuring employers against liability for personal injuries for which their employees may be entitled to benefits.” In addition, the Workers’ Compensation Advisory Council, a coalition of business, labor, and legislative stakeholders, was created to advise the Governor and the General Assembly on the administration of the workers’ compensation system. To make certain that injured workers received the highest quality medical treatment, the Medical Advisory Board was created under the direction of the Chief Judge of the Workers’ Compensation Court. The Workers’ Compensation Court has also contributed to the success of the system through the timely disposition of disputed cases. Historically, the court was plagued by a backlog of cases which has now been eliminated.

Workers’ compensation costs out of control – claims filed in excess of \$56.2 million

2,000 businessmen and women join together for protest march on State House

SCIF officially renamed The Beacon Mutual Insurance Company - write first policy to Potter Clothing Company of Newport



1988
Many employers forced to leave Rhode Island due to skyrocketing premiums

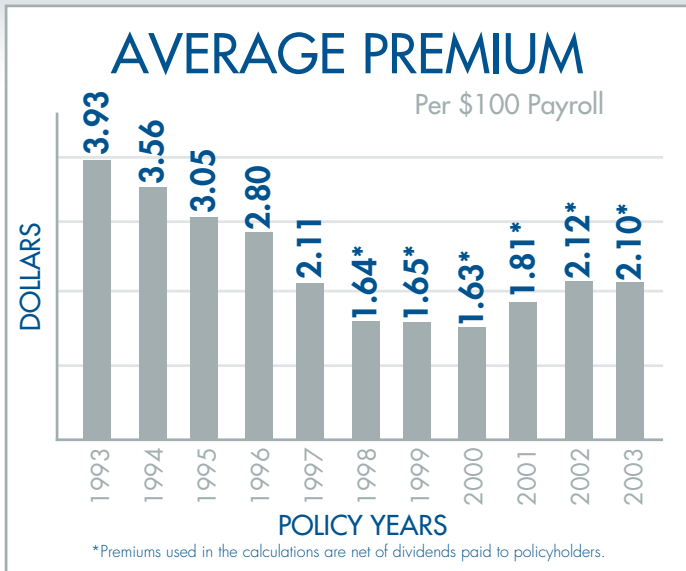
1989
Largest insurer stops writing new policies for workers’ compensation

1990
The Governor and General Assembly implement major reforms, including creation of State Compensation Insurance Fund (SCIF)

1991

1992

1993



The SCIF was officially renamed The Beacon Mutual Insurance Company in July 1992, writing our first policy to Potter Clothing in August of that year. Gradually, Rhode Island began to see improvements in the workers' compensation system. By 1994, improved market conditions allowed The Beacon to begin providing discounts to manual premium rates paid by deserving employers.

Workers' compensation: A report
 Sundlun says Reform Act has brought big improvement
Providence Journal, Jan. 16, 1994

The Beacon introduced or reintroduced premium saving programs to the Rhode Island workers' compensation system. Such programs included: retrospective rating plans, merit rating loss-free credit program, safety groups, CompAlliance, tail coverage and shared earnings plans. The programs were implemented to reward employers for their commitment to making their facilities as safe as possible. As a result, the average cost of workers' compensation has dropped from 3.93% of employer payroll in 1993 to 2.1% of total payroll in 2003.

Workers' comp insurer lowers rates

Providence Journal, Nov. 20, 1996

As the market continued to improve, historic rate decreases were offered to policyholders, beginning with a 6.0% decrease in 1994; 17.5% decrease in 1996; and a 7.8% decrease in 1998. With Rhode Island's workers' compensation costs at or below the national average, we began to research additional avenues to reduce costs even further. The first step was to improve and enhance our loss prevention efforts. In an attempt to offer Rhode Island employers the most timely information concerning the prevention of workplace injuries, The Beacon joined forces with Industrial Health Strategies. As ergonomic-related injuries slowly emerged as a silent contributor to more than one-third of all workers' compensation claims, The Beacon began to assemble one of the most experienced staff of loss prevention specialists in the country.

By 1998, The Beacon Mutual Insurance Company had emerged as the premier provider of workers' compensation insurance in the state. For the first time, Beacon policyholders received dividend checks. To further assist the families who are directly affected by workers' compensation accidents, Beacon established 'The Beacon Brighter Tomorrow Fund,' a scholarship fund to benefit spouses and/or dependents of workers that are fatally or severely injured as a result workplace accidents.

Beacon joins with Industrial Health Strategies to give employers and employees a better understanding of how to prevent ergonomic-related injuries in the workplace

Beacon issues first dividend checks to policyholders

'Beacon Brighter Tomorrow Fund' scholarship established

Beacon implements major loss prevention programs to ensure the safety and health of all RI employees

1994	1995	1996	1997	1998	1999
Improved market conditions allow for first-ever rate discounts to employers		Historic 17.5% rate decrease		Agents' Advisory Council formed to assist with the improvement of policies and product enhancements to insureds	

Workers' comp insurance is back on track

Providence Journal, Jan. 15, 1998

A study conducted in 1999 by the National Academy of Social Insurance concluded that Rhode Island was beginning to "see a decline (in worker's compensation costs) that exceeds national rates and standards." Chief Judge Robert F. Arrigan and Associate Judge George E. Healy of the state's Workers' Compensation Court, in an article published in the 'Quarterly Law Review' portion of the Providence Business News, commented that Beacon has "set the standard for quality underwriting and claims-handling practices." They also went on to conclude, "Beacon's commitment to excellence has assisted in the reduction of the cost of compensation."

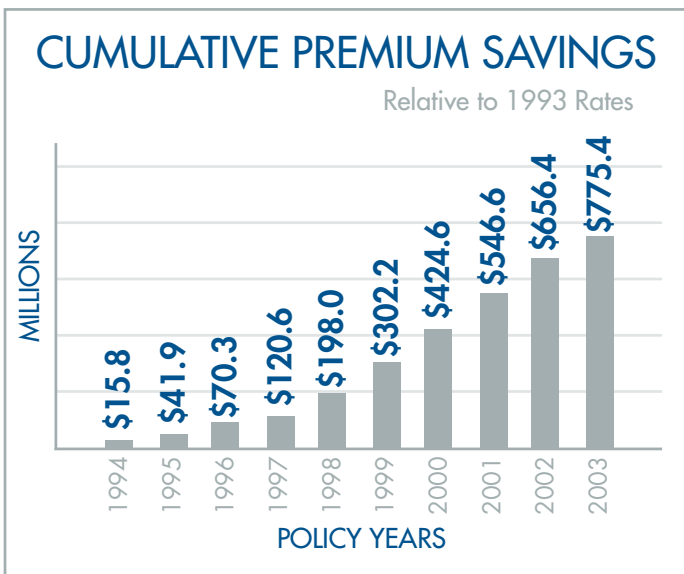
economy since its founding in 1990. The findings were that "The Beacon is critical to the Rhode Island economy based on the services it offers to Rhode Island businesses, the jobs it creates, the expenditures it makes, the tax revenue it provides to state and local authorities, the investments it makes in the economy and the savings in premiums to Rhode Island businesses." The economic benefits of the Beacon, which totaled more than \$411 million with investments in 2001, does not include the more than \$775 million saved in premiums by Rhode Island employers from 1993 through 2003 as a result of the reduced premiums. The Beacon also serves as a model corporate citizen, through charitable giving and the volunteer efforts of many company employees.

R.I.'s workers' compensation system in good health

Providence Business News, Aug. 18-24, 2003

To conclude the study Mazze stated, "The Beacon has been able to lower its premiums because of management efficiencies, education and training programs to make the workplace safer . . . lower workers' compensation insurance premiums make Rhode Island a more attractive place to do business for companies located in Rhode Island and for companies interested in moving to Rhode Island."

Through an exceptional collaboration of business, labor, medical, judicial and legislative leaders, the Rhode Island workers' compensation system has emerged as a model for other states to follow. From our tumultuous beginnings - to our success today, it is truly remarkable to see what a difference a decade can make. We believe that our experienced claim management staff, coupled with a team of dedicated underwriting and loss prevention specialists, helps to maintain our position as the workers' compensation insurer of choice in Rhode Island.



In an attempt to measure the contribution of The Beacon to the State of Rhode Island, Dean of the College of Business Administration at the University of Rhode Island, Edward M. Mazze, PH.D, completed an economic impact study in 2001. The study focused on The Beacon's operations and its contributions to the Rhode Island

Beacon has 10th consecutive year of no rate increases



Average Rhode Island workers' compensation costs see decline that exceeds national rates

Beacon has paid into the State's Administrative Fund, over \$60 million from 1993 to 2003



FINANCIAL

December 31, 2003 and 2002

A full set of audited financial statements, including footnotes, is available upon request.



Statutory Statements of Admitted Assets, Liabilities, and Policyholders' Surplus
December 31, 2003 and 2002

<i>Admitted Assets</i>	<i>2003</i>	<i>2002</i>
Investments:		
Bonds and debt securities	\$ 325,497,032	\$ 304,135,524
Preferred stocks	19,774,726	6,075,400
Common stocks	31,608,786	16,322,798
Real estate	14,760,980	14,943,402
Short-term investments	12,365,934	35,337,239
Other invested assets	188,132	409,280
Total investments	404,195,590	377,223,643
Cash (overdraft)	(2,432,792)	(7,233,968)
Agents' and premium balances receivable	44,288,623	36,716,433
Accrued retrospective premiums	589,606	787,677
Interest and dividends receivable	4,908,916	5,204,280
Reinsurance recoverable on paid losses	81,989	114,207
Equipment, net	616,470	727,462
Other assets	1,217,964	2,124,293
Total admitted assets	\$ 453,466,366	\$ 415,664,027

Liabilities and Policyholders' Surplus

Liabilities:		
Loss and loss adjustment expense reserves:		
Loss reserves	\$ 215,362,296	\$ 205,659,332
Loss adjustment expense reserves	38,915,625	33,096,737
Loss and loss adjustment expense reserves	254,277,921	238,756,069
Unearned premiums	63,407,460	54,314,271
Premiums received in advance	1,730,313	915,133
Policyholder dividends	683,733	500,912
Taxes, licenses, and fees	11,157,426	9,507,559
Other liabilities	12,223,495	14,623,184
Total liabilities	343,480,348	318,617,128
Policyholders' surplus:		
Capital assessment	20,758,685	20,758,685
Unassigned surplus	89,227,333	76,288,214
Total policyholders' surplus	109,986,018	97,046,899
Total liabilities and policyholders' surplus	\$ 453,466,366	\$ 415,664,027



Statutory Statements of Operations
Years ended December 31, 2003 and 2002

	2003	2002
Underwriting income:		
Premiums written, net	\$ 149,821,901	\$ 134,790,677
Increase in unearned premiums	(10,223,148)	(8,399,057)
Premiums earned	139,598,753	126,391,620
Losses incurred	82,316,550	70,484,908
Loss adjustment expenses incurred	25,893,740	16,570,784
Other underwriting expenses incurred	41,963,490	43,005,506
Underwriting loss	(10,575,027)	(3,669,578)
Net investment income	15,428,123	18,469,331
Net realized capital gains (losses)	5,281,396	(1,769,597)
Other income (expense), net	(65,838)	(1,214,457)
Net income before dividends to policyholders	10,068,654	11,815,699
Dividends to policyholders	2,953,983	2,050,327
Net income	\$ 7,114,671	\$ 9,765,372

Statutory Statements of Changes in Policyholders' Surplus
Years ended December 31, 2003 and 2002

	2003	2002
Balance at beginning of year	\$ 97,046,899	\$ 92,867,115
Net income	7,114,671	9,765,372
Net change in unrealized capital gains (losses)	5,913,153	(2,809,542)
Decrease in non-admitted assets	(1,040,730)	(2,776,046)
Cumulative effect - changes in accounting principles	952,025	—
Balance at end of year	\$ 109,986,018	\$ 97,046,899



Statutory Statements of Cash Flow
Years ended December 31, 2003 and 2002

	2003	2002
Cash from operations:		
Premiums collected, net of reinsurance	\$ 143,561,872	\$ 128,635,331
Loss and loss adjustment expenses paid	(93,653,284)	(90,312,052)
Underwriting expenses paid	(42,723,422)	(37,365,663)
Cash from underwriting	7,185,166	957,616
Net investment income	18,533,377	19,332,473
Other income (expense)	(65,838)	(1,214,457)
Dividends to policyholders	(2,771,161)	(6,112,637)
Net cash from operations	22,881,544	12,962,995
Cash from investments:		
Proceeds from investments sold, matured or repaid:		
Bonds	197,997,688	196,376,966
Stocks	21,453,286	7,314,489
Miscellaneous proceeds	—	(1,716)
Total investment proceeds	219,450,974	203,689,739
Cost of investments acquired:		
Bonds	215,968,824	201,297,834
Stocks	44,944,882	12,031,460
Real estate	151,550	253,141
Other invested assets	50,000	—
Total investments acquired	261,115,256	213,582,435
Net cash from (used by) investments	(41,664,282)	(9,892,696)
Cash from financing and miscellaneous sources:		
Other cash provided	1,243,418	2,639,445
Net transfers from affiliates	1,209,749	(1,177,271)
Other applications	(1,840,558)	(3,558,108)
Net cash from (used by) financing and miscellaneous sources	612,609	(2,095,934)
Net change in cash and short-term investments	(18,170,129)	974,365
Cash and short-term investments – beginning of year	28,103,271	27,128,906
Cash and short-term investments – end of year	\$ 9,933,142	\$ 28,103,271



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