REPORT ON EXAMINATION OF

PRE-PAID LEGAL SERVICES OF TENNESSEE, INC.

ADA, OKLAHOMA

AS OF

DECEMBER 31, 2006

THE DEPARTMENT OF COMMERCE AND INSURANCE

STATE OF TENNESSEE

NASHVILLE, TENNESSEE

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Ada, Oklahoma
May 21, 2008

Honorable Leslie A. Newman
Commissioner of Commerce
and Insurance
State of Tennessee
500 James Robertson Parkway
Nashville, Tennessee 37243

Dear Commissioner:

Pursuant to your instructions and in accordance with the Tennessee Insurance Laws, regulations, and resolutions adopted by the National Association of Insurance Commissioners (NAIC), a financial examination has been made concerning the condition and affairs of

PRE-PAID LEGAL SERVICES OF TENNESSEE, INC.
ONE PRE-PAID WAY
ADA, OKLAHOMA 74820

hereinafter generally referred to as the Company, and a report thereon is submitted as follows:

SCOPE OF EXAMINATION

This examination was called by the Commissioner of Commerce and Insurance of the State of Tennessee to commence on December 10, 2007. The examination field work started on December 12, 2007, and was conducted by examiners from the State of Tennessee Department of Commerce and Insurance (TDCI).

The examination was conducted at the Company's office in Ada, Oklahoma where all books and records are located. The period covered by this examination is from January 1, 2002, to the close of business on December 31, 2006, and includes any material transactions and/or events occurring subsequent to the examination date and noted during the course of the examination.

The examination of the financial condition of the Company was conducted in accordance with guidelines and procedures contained in the NAIC Financial Condition Examiners Handbook.

During the course of examination, assets were verified and valued, and liabilities were determined or estimated as of December 31, 2006. The Company's financial condition and its degree of solvency were thereby established. Test checks, covering selected periods, were made of income and disbursement items and a general review was made of the Company's operations, practices and compliance with statutes, to the extent hereinafter set forth.

All asset and liability items contained in the financial statement of this report were examined and verified with relative emphasis according to their amounts and potential impact on surplus. Additionally, an examination of the following items was made:

Company History	Charter and Bylaws	Management and Control
Corporate Records	Affiliated Companies	Fidelity Bond/Insurance
Employee Benefits	Territory	Plan of Operation
Loss Experience	Statutory Deposits	Commitments/Contingencies
Accounts and Records	Financial Statements	

Previous Examination:

The previous examination of the Company was made as of December 31, 2001, and resulted in a decrease of $427,410 to the Company's surplus account.

The Company was directed to comply with Tenn. Code Ann. § 56-43-107(a) by submitting any management agreement to TDCI prior to its entry by the Company and to file all such agreements with the TDCI that have not been previously filed or received approval. The Company submitted its Management Agreement to the TDCI on May 13, 2004 and is now in compliance with said directive.

The Company was directed to comply with Tenn. Comp. R. & Regs. ch. 0780-1-46, should it choose to hold its securities with a custodial bank by having such securities held pursuant to a qualified custodial agreement between the company and the custodial bank. The Company's custodial agreement was subsequently executed and submitted to the TDCI on May 13, 2004 to comply with said directive.

The Company was directed to comply with Tenn. Code Ann. § 56-1-501(g) by preparing its financial statements in accordance with the NAIC Accounting Practices and Procedures Manual, including, but not limited to SSAP No. 26, paragraph 4, as to recording bond purchases, and SSAP No. 10, or Issue Paper No. 83, paragraph 9, as to recording its deferred tax asset. The Company made the necessary changes in its subsequent financial statement to comply with said directive.

COMPANY HISTORY

The Company was incorporated on December 3, 1997, under the Tennessee Business Corporation Act as a for-profit legal insurance company. On April 20, 1998, the Company was issued a certificate of authority to transact the business of legal insurance pursuant to the Tennessee Code Annotated Title 56, Chapter 43.

There have been no regulatory activities since the prior examination was made as of December 31, 2001.

All operations are performed at the Company's home office in Ada, Oklahoma. The Company's development, since the previous examination, is depicted in the following table:

Date	Earned Premiums	Losses Incurred (Provider Attorney Per Capita Fees)	Admitted Assets	Liabilities	Capital & Surplus
12/31/02	$5,162,393	$2,004,868	$2,342,340	$341,814	$2,000,526
12/31/03	5,975,314	2,314,636	2,102,749	232,727	1,870,022
12/31/04	6,332,405	2,427,640	3,026,004	295,936	2,730,068
12/31/05	6,328,513	2,366,888	3,605,073	338,183	3,266,690
12/31/06	6,051,574	2,325,296	4,221,989	339,087	3,882,902

CHARTER AND BYLAWS

Charter:

Under the amended Charter approved April 15, 1998, the Company is a for profit corporation. The purpose for which the corporation is organized is to transact the business of legal insurance pursuant to Tenn. Code Ann. § 56-43-104(a) and to transact any other lawful business.

In addition to the preceding, the Charter recites other general and specific powers in detail. These are usual in nature and consistent with statute. The Charter was inspected and found to have been duly issued and properly recorded. There were no changes to the charter during the period under examination.

Bylaws:

The bylaws are such as are generally found in corporations of this type and contain no unusual provisions. The bylaws may be altered, amended, repealed or restated, or new bylaws may be adopted, at any meeting of the shareholders by the affirmative vote of a majority of the stock represented at such meeting, or by the affirmative vote of a majority of the Board of Directors who are present at any regular or special meeting of the Board. There were no changes to the bylaws during the period under examination.

MANAGEMENT AND CONTROL

Control:

At December 31, 2006, 100% of the outstanding shares of the Company were owned by Pre-Paid Legal Casualty, Inc. (PPLC), the Company's parent. There were no dividends paid by the Company during the examination period.

Board of Directors:

The business and affairs of the Company shall be managed by a Board of Directors. The Directors shall be elected at the annual meeting of the stockholders. The number of directors shall consist of no less than one and no more than ten. The Company's Board of Directors, at December 31, 2006, were as follows:

Name	Address	Occupation
Mark R. Harp	Ada, OK	COO, Pre-Paid Legal Services, Inc.
Kathleen S. Pinson	Ada, OK	VP Regulatory Compliance, Pre-Paid Legal Services, Inc.
Harland C. Stonecipher	Centrahoma, OK	CEO & President, Pre-Paid Legal Services, Inc.

Officers:

The officers of the Company consist of a President, a Secretary and such other officers as may be from time to time appointed by the Board of Directors. One person may simultaneously hold more than one office except the President may not simultaneously hold the office of Secretary. The Officers of the Company, at December 31, 2006, were as follows:

Name	Office Held
Mark R. Harp	President
Kathleen S. Pinson	Secretary/Treasurer

Conflict of Interests:

All directors and officers of the Company are required to complete an Annual Conflict of Interest Statement. The examiners reviewed the statements signed by the Company's directors and officers, for the period under examination, without exception.

Pecuniary Interest:

A check for compliance with Tenn. Code Ann. § 56-3-103 found that no director or officer of the Company had pecuniary interest in the investment or disposition of Company funds.

CORPORATE RECORDS

The minutes of the meetings of the Board of Directors and Stockholders were reviewed for the period under examination. They were found to be vague as to necessary detail and do not appear to adequately reflect the acts of the respective parties. The review of the minutes shows no indication that investment transactions were approved by the Board of Directors.

AFFILIATED COMPANIES

The Company is wholly-owned by PPLC. PPLC is an insurer domiciled in the State of Oklahoma, which in turn, is a wholly-owned subsidiary of Pre-Paid Legal Services, Inc. (PPLSI) the ultimate controlling entity. The Company is not subject to the Insurance Holding Company System Act of 1986 as defined in Tenn. Code Ann. § 56-11; however, holding company documents are sent to the TDCI annually. An organizational chart is attached to this report on page 23. The following agreements between the Company and PPLSI were in effect at December 31, 2006:

Management Agreement:

The Company entered into a Management Agreement with PPLSI effective January 1, 1998. Under the terms of the agreement, PPLSI agrees to provide to the Company certain record-keeping, accounting services and administrative assistance. Within 15 days after the end of each month, PPLSI shall calculate its monthly fees due for services provided. Such calculations of the monthly fees are based upon a formula contained within the agreement. Each monthly fee shall be payable by the Company at various times throughout the term of the agreement.

Tax Allocation Agreement:

A Tax Allocation Agreement, by and among PPLSI and its subsidiaries (Group), dated October 1, 2005, to be effective for the year ending December 31, 2005, and subsequent years was entered into. Under the provisions of the agreement, it is the intent of the parties to provide for sharing of ongoing consolidated tax liability. The tax liability shall be allocated to each member of the Group in accordance with the ratio of each member's statutory taxable income or loss to the total taxable income or loss of all members in the Group. Payments are due on or before ninety days following the end of the appropriate taxable year or appropriate quarterly tax estimate due date.

FIDELITY BOND AND OTHER INSURANCE

The Company is insured under the following coverages maintained by PPLSI at December 31, 2006:

Type or Class of Coverage	Limits
Commercial Property	$39,732,991 buildings $15,356,000 personal property
Commercial General Liability	$1,000,000 each occurrence $2,000,000 general aggregate $1,000,000 personal and advertising injury
Crime Coverage	$500,000 employee theft
Business Automobile	$1,000,000 liability $5,000 medical payments $1,000,000 uninsured motorists

Excess Liability – umbrella form	$5,000,000 each occurrence $5,000,000 aggregate
Workers' Compensation Employers Liability	Tennessee limit $1,000,000 each accident $1,000,000 disease – each employee $1,000,000 disease – policy limit
Employee Benefits Liability	$1,000,000 each claim $1,000,000 aggregate

On an organization-wide basis, the crime coverage is $500,000 less than the suggested minimum amount per the NAIC Financial Condition Examiners Handbook; however, on a Company-only basis, the coverage is $375,000 more than suggested. All of the above insurance policies are written by companies licensed to write in Tennessee.

RETIREMENT PLAN AND OTHER EMPLOYEE BENEFITS

The Company has no employees of its own. Personnel and services are provided by the Company's ultimate parent, PPLSI, in accordance with a Management Agreement as described in this report under the heading Affiliated Companies.

TERRITORY

The Company is licensed to transact business only in the State of Tennessee. The Certificate of Authority issued by the State of Tennessee was inspected and found to be in force both at the time of examination and inspection. During 2006, the Company wrote direct premiums of $6,132,488.

PLAN OF OPERATION

The Company markets a pre-paid legal services contract which allows a member access to a law firm for covered legal services under the contract. In exchange for a fixed monthly, quarterly, semi-annual or annual payment, a member will be entitled to specified legal services. Each contract is guaranteed renewable, except in the case of fraud or nonpayment of contract fees.

The basic legal service plan membership is sold as a package consisting of the following five separate benefit groups:

Preventive Legal Services
Motor Vehicle Legal Services
Trial Defense Services
IRS Audit Legal Services
Other Legal Services

When the member accesses the benefits of the contract, they call the provider attorney firm which is responsible for rendering the services under the contract. Any services beyond the covered services are subject to a retainer agreement between the attorney and the member. The Company is not a party to the additional agreements.

The agreement with the provider attorney firm calls for the Company to pay the attorney firm a monthly per capita fee in exchange for the firm rendering the legal services provided for in the membership contract. Payment is made each month to the provider attorney based on the number of active members.

LOSS EXPERIENCE

The loss experience of the Company, since the previous examination, as reported in its annual statements, is as follows:

Year	Premiums Earned	Losses Incurred	LAE Incurred	Loss Ratio	Other Underwriting Expenses	Combined Ratio
2002	$5,162,393	$2,004,868	$102,649	40.8%	$2,843,217	95.9%
2003	5,975,314	2,314,636	158,553	41.4%	3,698,663	103.3%
2004	6,332,405	2,427,640	180,859	41.2%	3,511,490	96.7%
2005	6,328,513	2,366,888	155,741	39.9%	3,211,566	90.6%
2006	6,051,574	2,325,296	166,026	41.1%	2,759,587	86.8%
Total	$29,850,199	$11,439,328	$763,828	40.9%	$16,024,523	94.6%

STATUTORY DEPOSITS

The Company maintained the following deposit at December 31, 2006, for the benefit of all policyholders, claimants and creditors of the Company.

Where Deposited and Description	Par Value	Statement Value	Market Value
Tennessee			
USTN, 4.25%, Due 8/15/13	$130,000	$132,365	$126,740

The above deposit was verified by direct correspondence with the regulating jurisdiction.

COMMITMENTS AND CONTINGENCIES

From the examination data made available, it appears that the only matters of law in which the Company was involved, during the period under review, were those arising out of the normal course of business and the outcome of such actions should not have a material effect on the financial position of the Company.

ACCOUNTS AND RECORDS

During the course of examination, such tests and audit procedures were made as were considered necessary, including substantial verification of postings, extensions and footings. General ledger trial balances were reconciled with copies of annual statements for the years 2002, 2003, 2004, 2005 and 2006.

Accounting records conform to generally accepted insurance accounting practices and appear to properly reflect the operations during the period under examination and the status of the Company at the date of examination.

The Company is audited annually by Grant Thornton LLP, Oklahoma City, Oklahoma. There is no violation as respects Tenn. Comp. R. & Reg., ch. 0780-1-65.07(3).

FINANCIAL STATEMENT

There follows a statement of assets, liabilities and statement of income at December 31, 2006, together with a reconciliation of surplus for the period under review, as established by this examination:

ASSETS

	Assets	Nonadmitted Assets	Net Admitted Assets
Bonds	$ 3,808,427	$ 0	$ 3,808,427
Cash, cash equivalents and short term investments	181,454	0	181,454
Subtotals, cash and invested assets	3,989,881	0	3,989,881
Investment income due and accrued	16,298	0	16,298
Premiums and considerations:			
Uncollected premiums and agents' balances in the course of collection	103,433	0	103,433
Current federal income tax recoverable	27,504	0	27,504
Net deferred tax asset	48,368	0	48,368
Receivables from parent, subsidiaries and affiliates	36,505	0	36,505
Total assets	$ 4,221,989	$ 0	$ 4,221,989

LIABILITIES, SURPLUS AND OTHER FUNDS

Commissions payable	$ 25,471
Taxes, licenses and fees	34,722
Unearned premiums	278,894
Total liabilities	339,087
Common capital stock	250,000
Gross paid in and contributed surplus	850,000
Unassigned funds	2,782,902
Surplus as regards policyholders	3,882,902
Totals	$ 4,221,989

STATEMENT OF INCOME

Underwriting Income	
Premiums earned	$ 6,051,574
Deductions:	
Losses incurred	2,325,298
Loss expenses incurred	166,026
Other underwriting expenses incurred	2,759,587
Total underwriting deductions	5,250,909
Net underwriting gain (loss)	800,665
Investment Income	
Net investment income earned	112,045
Net realized capital gains (losses)	(1,186)
Net investment gain (loss)	110,859
Net income before federal income taxes	911,524
Federal income taxes incurred	286,183
Net income	$ 625,341

RECONCILIATION OF SURPLUS
FOR THE PERIOD UNDER EXAMINATION

Surplus as regards policyholders, December 31, 2001	$ 1,785,259
Net income	205,787
Change in net deferred income tax	9,500
Change in surplus as regards policyholders for the year	215,267
Surplus as regards policyholders, December 31, 2002	$ 2,000,526
Net income	(83,700)
Change in net deferred income tax	(46,804)
Change in surplus as regards policyholders for the year	(130,504)
Surplus as regards policyholders, December 31, 2003	$ 1,870,022
Net income	254,292
Change in net deferred income tax	5,754
Paid in surplus	600,000
Change in surplus as regards policyholders for the year	860,046
Surplus as regards policyholders, December 31, 2004	$ 2,730,068
Net income	532,634
Change in net deferred income tax	4,188
Change in surplus as regards policyholders for the year	536,822
Surplus as regards policyholders, December 31, 2005	$ 3,266,890
Net income	625,341
Change in net deferred income tax	(9,329)
Change in surplus as regards policyholders for the year	616,012
Surplus as regards policyholders, December 31, 2006	$ 3,882,902

ANALYSIS OF CHANGES IN FINANCIAL STATEMENT AND COMMENTS RESULTING FROM EXAMINATION

Although minor differences were found in various items, none were considered to produce a material effect on surplus funds either singly or in the aggregate.

COMMENTS AND RECOMMENDATIONS

Comments:

None

Recommendations:

1. The following items were not in compliance with the Accounting Practices and Procedures Manual (AP&P) of the NAIC:

(a) The Company is reporting the wrong designation for two of the securities shown in its annual statement. A bond investment in General Motors shows a designation of 1; however, the correct designation is 3 according to the NAIC Valuation of Securities. Also, a bond investment in Weingarten Realty shows a designation of 1; however, the correct designation is 2 according to the NAIC Valuation of Securities. The value of these two securities is immaterial. The Company needs to follow the Purposes and Procedures Manual of the NAIC Securities Valuation Office as required by Statement of Statutory Accounting Principle (SSAP) No. 26, paragraph 7 of the NAIC AP&P.

(b) The Company is recording some acquisitions and sales of securities on the settlement date of the transaction; however, these transactions should be recorded on the trade date as required by SSAP No. 26, paragraph 4 of the NAIC AP&P.

Based on the above, it is recommended that the Company comply with Tennessee Code Annotated 56-1-501(g) to alleviate discrepancies.

2. A review of the minutes of the Board of Directors meetings during the period under examination was made. This review found no indication that investments

made by the Company were authorized, reviewed or approved by the Board of Directors.

Based on the above, it is recommended that the Company comply with Tenn. Code Ann. § 56-3-301(b)(1).

CONCLUSION

The customary insurance examination practices and procedures, as established by the NAIC, have been utilized in connection with the verification and valuation of assets and the determination of liabilities in the financial statement of this report.

In such manner, it was determined that, as of December 31, 2006, the Company had net admitted assets of $4,221,989 and liabilities, exclusive of capital, of $339,087. Thus, there existed for the additional protection of the policyholders, the amount of $3,882,902 in the form of paid-up capital, gross paid-in and contributed surplus and unassigned funds (surplus).

Respectfully submitted,

David R. White, CFE
Examiner-in-Charge
State of Tennessee
Southeastern Zone, NAIC

Donnie R. Nicholson
Examiner III
State of Tennessee
Southeastern Zone, NAIC

<u>AFFIDAVIT</u>

The undersigned deposes and says that he has duly executed the attached examination report of Pre-Paid Legal Services of Tennessee, Inc. dated May 21, 2008, and made as of December 31, 2006, on behalf of the TDCI. Deponent further says he is familiar with such instrument and the contents thereof, and that the facts therein set forth are true to the best of his knowledge, information and belief.

David R. White, CFE
Examiner-in Charge
State of Tennessee
Southeastern Zone, NAIC

Subscribed and sworn to before me this

21st day of May, 2008

Notary Helen W. Dorsey

County Davidson

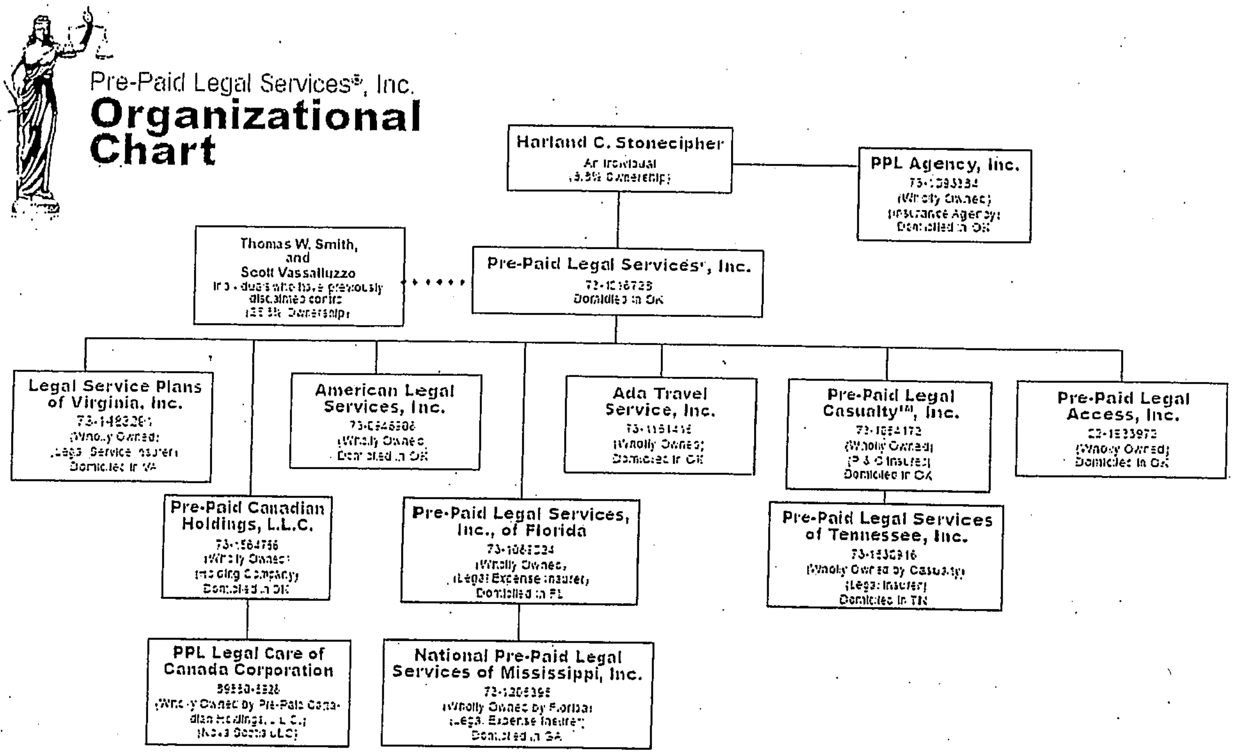
State Tennessee

Commission Expires 05/22/2010

HELEN W. DORSEY STATE OF TENNESSEE NOTARY PUBLIC DAVIDSON COUNTY, TENN.

My Commission Expires MAY 22, 2010

ORGANIZATIONAL CHART



PRE-PAID LEGAL SERVICES, INC.

"Justice For All"

Serving North American Families Since 1972

CORPORATE OFFICES: ONE PRE-PAID WAY • ADA, OKLAHOMA 74820 • (580) 436-1234 • WWW.PREPAIDLEGAL.COM

RECEIVED

JUN 11 2008

Dept. Of Commerce & Insurance
Company Examinations

June 3, 2008

State of Tennessee
Dept of Commerce & Insurance
Attn: Philip Blustein, CFE
500 James Robertson Parkway
Nashville, TN 37243

RE: Pre-Paid Legal Services of Tennessee, Inc.
Examination Report as of December 31, 2006

Dear Mr. Blustein:

Pre-Paid Legal Services of Tennessee, Inc. has received the Examination Report as of December 31, 2006. We have reviewed the report and acknowledge the Comments and Recommendations regarding our Accounts and Records as recorded on pages 19 and 20 of the report.

The Company has implemented the necessary procedures to comply with the recommendations.

Recommendation 1. (a), page 19
As required by SSAP No. 26, paragraph 7, we will report the current designations per the NAIC Valuation of Securities on future financial statements.

Recommendation 1. (b), page 19
As required by SSAP No. 26, paragraph 4, we will insure that all transactions are recorded on the trade date.

Recommendation 2., page 19, 20
As required by Tenn. Code Ann. § 56-3-301(b)(1), we will record minutes with specific authorization, review and approval of investments by the Board of Directors.

Thank you for your assistance with this Examination.

Sincerely,

Kathy Pinson

Kathy Pinson
Secretary

EXHIBIT
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Subsidiaries

Pre-Paid Legal Casualty™, Inc. • Pre-Paid Legal Services of Tennessee, Inc. • Pre-Paid Legal Services, Inc., of Florida • National Pre-Paid Legal Services of Mississippi, Inc.
Legal Service Plans of Virginia, Inc. • PPL Legal Care of Canada Corporation • Ohio Access to Justice, Inc., administered by Pre-Paid Legal Services, Inc.