Washington State Department of
Labor & Industries

State of Washington Industrial Insurance Fund Statutory Financial Information Report

For the Fiscal Years Ended June 30, 2013 and 2012

State of Washington Industrial Insurance Fund
Statutory Financial Information Report
For the Fiscal Years Ended June 30, 2013 and 2012

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Washington State Office of Financial Management
Washington State Investment Board

Washington State Department of
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Keep Washington Safe and Working

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Washington State Department of
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STATE OF WASHINGTON
DEPARTMENT OF LABOR AND INDUSTRIES
P.O. Box 44000 • Olympia Washington 98504-4000

December 4, 2013

The Honorable Jay Inslee, Governor
Honorable Members of the Legislature
Director of Office of Financial Management
Washington State Citizens
Olympia, Washington 98504

RE: Statutory Financial Information Report (SSAP)

The Revised Code of Washington 51.44.115 requires the Department of Labor & Industries (L&I) to publish a Statutory Financial Information Report for the Industrial Insurance Fund (State Fund) in conformity with statutory accounting practices and principles promulgated by the National Association of Insurance Commissioners within six months of the close of each fiscal year. This report is published to fulfill that requirement for the fiscal year ended June 30, 2013.

L&I is fully responsible for the completeness and reliability of the information contained in this report, based upon a comprehensive framework of internal controls established for this purpose. Because the cost of internal controls should not exceed anticipated benefits, the objective is to provide reasonable, rather than absolute, assurance that the financial statements are free of any material misstatements.

The independent certified public accounting firm, Eide Bailly, LLP, has issued an unmodified ("clean") opinion on the Statutory Financial Information Report for the fiscal years ended June 30, 2013 and 2012. The independent auditor's report is located at the front of the financial section of this report.

Management's Discussion and Analysis (MD&A) immediately follows the independent auditor's report and provides a narrative introduction, overview, and analysis of the consolidated statutory financial statements. The MD&A complements the information provided in this letter of transmittal and should be read together with it.

Following the MD&A are the consolidated financial statements and notes to the financial statements. The required schedules and an independent actuarial opinion complete the Statutory Financial Information Report.

PROFILE OF THE STATE FUND

The workers' compensation system has existed in Washington State for 102 years. Washington was one of the first states to enact workers' compensation laws. Our state's Workmen's Compensation Act, established on July 28, 1911, was designed to protect workers and employers from injustice and financial hardship arising from work-related injuries in extremely hazardous work. In 1923, Washington became one of only two states where workers pay a portion of the insurance premiums.

The Industrial Insurance Fund covers 168,000 employers and approximately 2.5 million workers statewide. Total premiums assessed in Fiscal Year 2013, including both the employer and worker portions, in the State Fund were $1.74 billion. Over 84,000 claims were accepted in Fiscal Year 2013; about 80 percent of the accepted claims were for medical benefits only and received no compensation for time off work or disability-related benefits. Approximately 39,000 claims are active in any given month, of which about 19,000 are receiving time-loss benefits, many of which involve long-term disability and complex medical issues. In the same year, retraining plans were completed by 583 injured workers who were not able to return to their occupations after injury.

The Industrial Insurance Fund is part of the Workers' Compensation Program and is made up of the Accident, Medical Aid, and Pension Reserve Accounts. The activities within the Industrial Insurance Fund are financed and operated in a manner similar to private business entities. Premiums collected from employers and workers and investment earnings finance the cost of providing medical coverage, time-loss payments, disability benefits to qualifying individuals, Stay at Work reimbursements, and structured settlements. L&I prepares a Statutory Financial Information Report for the Washington State Industrial Insurance Fund of the Workers' Compensation Program annually, based on a fiscal year beginning July 1 and ending June 30.

During the 2011 Legislative Session, the Legislature passed historic workers' compensation reforms to improve outcomes for injured workers, reduce disability and cut costs for the state's workers' compensation program. Included in these reforms were the Stay at Work and Structured Settlement Programs, which were implemented by L&I during Fiscal Year 2012. Fiscal Year 2013 was the first full year that the programs were in place. Additional programs included in the 2011 reforms were established during Fiscal Year 2013, including the Medical Provider Network and the expansion of the Centers of Occupational Health and Education (COHEs). These new programs have the potential to impact the choices for injured workers and the rates paid by employers.

L&I is a leader in state government for using Lean process improvement techniques. Lean is helping L&I create and deliver the most value from the customer's perspective while consuming the fewest resources. As of June 30, 2013, L&I has completed 20 Lean projects and 27 others are underway. One large-scale Lean project has cut 70 days out of the process to complete vocational assessments for injured workers. The Department refers over 7,000 workers for these assessments each year. Lean is an investment for the future, leading to fundamental changes in business processes that reduce delays, improve quality and lower costs. This holds down claims costs for L&I and required premiums for employers and workers.

ACKNOWLEDGEMENTS

As in the work and service we provide every day, this Statutory Financial Information Report represents our commitment to maintain excellence in financial reporting, and the financial statements are in conformance with the highest standards of financial accountability.

The preparation of this report could not have been accomplished without the professionalism and dedication demonstrated by the financial and management personnel of L&I, the Washington State Office of Financial Management, and the Washington State Investment Board.

Sincerely,

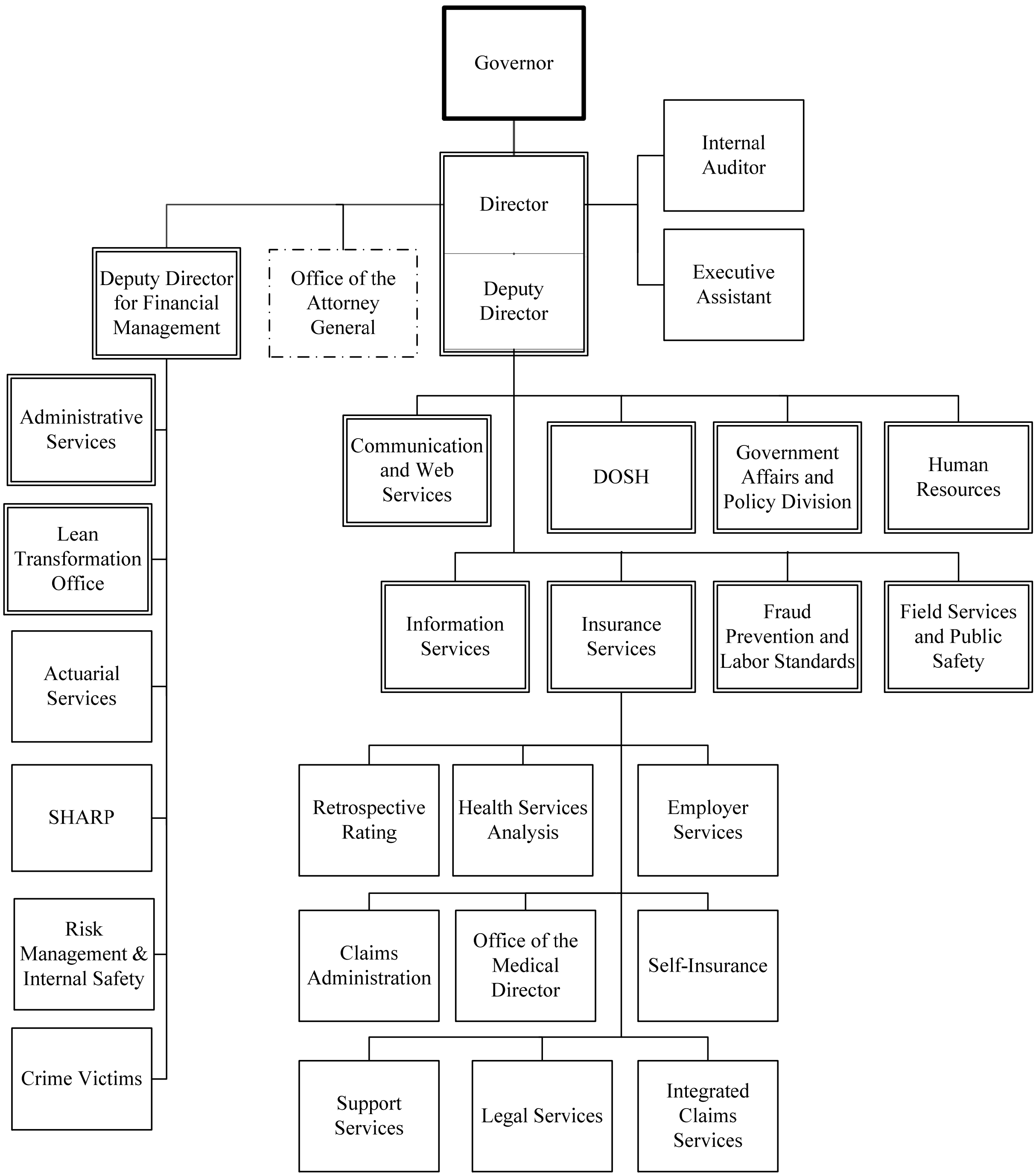
Joel Sacks
Director

Randi Warick
Deputy Director for
Financial Management

Vickie Kennedy
Assistant Director,
Insurance Services

Washington State Department of Labor & Industries

Organization Chart
June 30, 2013



Financial Section

Washington State Department of
Labor & Industries

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CPAs & BUSINESS ADVISORS

Independent Auditor's Report

Mr. Joel Sacks Director
Washington State Department of Labor and Industries
Industrial Insurance Fund
P.O. Box 44001
Olympia, WA 98504-4001

Report on the Financial Statements

We have audited the accompanying consolidated statutory financial statements (referred to as the financial statements) of Washington State Department of Labor and Industries Industrial Insurance Fund (Fund), which comprise the consolidated statutory statement of admitted assets, liabilities, and surplus as of June 30, 2013 and 2012, and the related consolidated statutory statements of income and changes in contingency reserve, and consolidated statutory cash flows for the year then ended, and the related notes to the consolidated statutory financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated statutory financial statements in accordance with the accounting practices prescribed or permitted by the Insurance Department of the State of Washington. Management is also responsible for 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 consolidated statutory financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated statutory financial statements are free from 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 consolidated statutory 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 consolidated statutory 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 consolidated statutory financial statements.

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

Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles

As described in Note 1 to the consolidated statutory financial statements, the consolidated statutory financial statements are prepared using accounting practices prescribed or permitted by the Insurance Department of the State of Washington, which is a basis of accounting other than accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between the statutory basis of accounting described in Note 1 and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter described in the Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles paragraph, the consolidated statutory financial statements referred to above do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of the Fund as of June 30, 2013 and 2012, or the results of its operations or its cash flows for the year then ended.

Opinion on Regulatory Basis of Accounting

In our opinion, the consolidated statutory financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, and surplus of the Fund as of June 30, 2013 and 2012, and the results of its operations and its cash flows for the year then ended, on the basis of accounting described in Note 1.

Change in Accounting Principle

As discussed in Note 2 to the consolidated statutory financial statements, a specific net other postemployment benefits (OPEB) calculation was made during 2013 resulting in overstatement of amounts previously reported for OPEB as of June 30, 2012 and is accounted for as a change in accounting principle under the accounting practices prescribed or permitted by the Insurance Department of the State of Washington. Accordingly, the amounts reported for OPEB liabilities have been restated in the 2012 statutory financial statements now presented, and a cumulative adjustment has been made to the contingency reserve as of June 30, 2012, to reflect the change in accounting principle. Our opinion is not modified with respect to that matter.

Report on Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the consolidated statutory financial statements taken as a whole. The accompanying supplementary information included in the *Schedule of Claims Development Information Basic Plan*, and the *Schedule of Funding Progress for Other Postemployment Benefits* on pages 80 through 81 are not required part of the basic consolidated statutory-basis financial statements. The accompanying supplementary information included in the *Supplemental Schedule of Investment Risk Interrogatories* and the *Summary Investment Schedule* on pages 82 through 85 are required to be presented to comply with the National Association of Insurance Commissioners' Annual Statement Instructions and the National Association of Insurance Commissioners' Accounting Practices and Procedures Manual and are not a required part of the basic statutory-basis consolidated financial statements. Such information included in the schedules referred to above is the responsibility of management, is presented for purposes of additional analysis and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other procedures in accordance with the auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the consolidated statutory financial statements taken as a whole.

Our audit was conducted for the purpose of forming an opinion on the consolidated statutory financial statements taken as a whole. The information contained in the *Introductory Section, Management Discussion and Analysis and the Statement of Actuarial Opinion sections*, as listed in the accompanying table of contents, which is the responsibility of management, is presented for purposes of additional analysis and are not a required part of the basic statutory financial statements. Such information has not been subject to the auditing procedures applied in the audit of the consolidated statutory financial statements, and, accordingly, we do not express an opinion or provide any assurance on it.

Eide Bailly LLP

Fargo, North Dakota
December 4, 2013

Washington State Department of
Labor & Industries

Keep Washington Safe and Working

Management's Discussion and Analysis

The state of Washington's Department of Labor & Industries (L&I) administers the state Workers' Compensation Program, including the Industrial Insurance Fund.

This section of the state of Washington Industrial Insurance Fund's Statutory Financial Information Report presents management's discussion and analysis of the financial performance of the Industrial Insurance Fund for the fiscal years ended June 30, 2013 and 2012. This discussion should be read in conjunction with the accompanying consolidated statutory financial statements and notes to the consolidated statutory financial statements. The consolidated statutory financial statements, notes to the consolidated statutory financial statements, and this discussion are the responsibility of the Industrial Insurance Fund's management.

History and Information that Makes the State of Washington's Industrial Insurance Fund Unique

The state of Washington's Workmen's Compensation Act established the industrial insurance system in 1911, covering only extremely hazardous work. Washington's workers' compensation insurance was provided solely through the Industrial Insurance Fund until 1971, when the system underwent a major overhaul. In 1971, the Legislature expanded the scope of coverage to virtually all workers and created an option for qualified employers to self-insure, thus paying the cost of claims for their injured workers from their own funds and also assuming responsibility for their own claims administration.

Washington State, through Title 51 of the Revised Code of Washington (RCW), requires all employers, unless exempted, to secure coverage for job-related injuries and illnesses either by paying insurance premiums to the Industrial Insurance Fund or by self-insuring. Direct private insurance is not authorized, although self-insurers are permitted to reinsure up to 80 percent of their obligations.

Under statute RCW 51.16.035, L&I is required to have the lowest possible rates while maintaining solvency of the system. L&I is also required to limit rate fluctuations, follow recognized insurance principles, and stimulate and encourage accident prevention.

In Washington, premiums are based on the workers' exposure to risk (hours on the job), which employers and workers agreed to in the 1930s. Also, Washington requires both the employers and workers to contribute to the cost of premiums.

Workplace Injuries

Washington's workers' compensation system provides insurance for about 2.5 million employees working for 168,000 employers. Men accounted for 67 percent of injured workers, and 46 percent of all injuries were to workers from 30 to 50 years of age. The most common injuries were traumatic injuries to muscles, tendons, ligaments, and back joints, including spine and spinal cord. Forty-four fatal pensions were awarded in Fiscal Year 2013. Below is a comparison of select Industrial Insurance Fund statistics.

Statistics at a Glance				
	Fiscal Year 2013		Fiscal Year 2012	
Employers insured		168,000		166,000
Workers covered		2,487,000		2,420,000
Hours reported		3,270,000,000		3,183,000,000
Premiums assessed (employers' portion)	$	1,429,000,000	$	1,358,000,000
Premiums assessed (workers' portion)	$	313,000,000	$	290,000,000
Benefits incurred expense	$	2,162,748,000	$	1,957,245,000
Number of claims filed		103,328		101,524
Total days paid for lost work		7,521,311		7,850,982

Note: The data above are a snapshot as of the first week of October.

Using the Statutory Financial Statements

The accompanying consolidated statutory financial statements include the Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve; Consolidated Statutory Statement of Operations and Changes in Contingency Reserve; and Consolidated Statutory Statement of Cash Flows. These financial statements have been prepared in conformity with the Statements of Statutory Accounting Principles (SSAP), as promulgated by the National Association of Insurance Commissioners, whereby the main purpose of SSAP-based information is to determine solvency. Solvency is defined as the availability of the Industrial Insurance Fund’s admitted assets to satisfy its obligations to injured workers and beneficiaries. The notes to the consolidated statutory financial statements provide additional information that is essential to a full understanding of the data provided in the consolidated statutory financial statements.

The accompanying consolidated statutory financial statements report the financial position and results of operations for three of the seven Workers’ Compensation Program accounts: the Accident, Medical Aid, and Pension Reserve Accounts. These three accounts represent the Workers’ Compensation Program Basic Plan, also known as the Industrial Insurance Fund. The Industrial Insurance Fund is accounted for as an enterprise fund of the state of Washington and reports business activities under the accrual basis of accounting, much like a private business enterprise.

Overview of the Financial Statements

This discussion and analysis serves as an introduction to the Industrial Insurance Fund’s financial statements, which consist of the following components:

The Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve provides information about the Fund’s admitted assets and liabilities and reflects the contingency reserve as of June 30, 2013 and 2012. The Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve can be found on page 27 of this report.

The Consolidated Statutory Statement of Operations and Changes in Contingency Reserve reflects revenues and expenses for Fiscal Years 2013 and 2012. The Consolidated Statutory Statement of Operations and Changes in Contingency Reserve can be found on page 28 of this report.

The Consolidated Statutory Statement of Cash Flows reflects cash collections and cash payments to arrive at the net increase or decrease in cash during Fiscal Years 2013 and 2012. The Consolidated Statutory Statement of Cash Flows can be found on page 29 of this report.

The Notes to the Consolidated Statutory Financial Statements are an integral part of the financial statements and are essential to a full understanding of the Industrial Insurance Fund's financial position and results of operations presented in the financial statements. The Notes to the Consolidated Statutory Financial Statements can be found on page 31 of this report.

Elimination for Consolidated Financial Statements

It is important to the readers of the Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve that we include details of each account, report the true contingency reserve balance, and show compliance with the statutory Pension Reserve Account transfer requirement. Each year, the Pension Reserve Account's assets and liabilities are evaluated, and a transfer is made between the Accident, Pension Reserve, and Second Injury Accounts, as required by law. In order to arrive at an accurate consolidated Industrial Insurance Fund balance, the receivable and the accrued liability of $8,064,000 resulting from the transfer between the Pension Reserve Account and the Accident Account was eliminated in Fiscal Year 2013.

Financial Highlights

Condensed Financial Snapshot
(in millions)

	As of and For the Fiscal Year Ended June 30, 2013	Restated As of and For the Fiscal Year Ended June 30, 2012	$ Change	% Change
Total Admitted Assets	$ 13,183	$ 12,512	$ 671	5.36%
Total Liabilities	12,564	11,922	642	5.39%
Total Revenues Earned	2,255	2,647	(392)	(14.81%)
Total Expenses Incurred	2,466	2,283	183	8.02%
Total Contingency Reserve	620	590	30	5.08%

Financial Position

The Industrial Insurance Fund's financial position at June 30, 2013 and 2012 was as follows:

Summary of Financial Position
As of June 30, 2013 and 2012
(in thousands)

	June 30, 2013	Restated June 30, 2012
Admitted Assets		
Fixed income investments	$ 9,020,076	$ 8,625,928
Treasury inflation-protected securities	1,589,964	1,619,787
Equities investments	1,730,470	1,580,216
Short-term investments	208,683	82,211
Unsettled trade receivables	1,694	7
Total Investments	12,550,887	11,908,149
Securities lending collateral	27,469	-
Interest receivable	107,081	109,617
Cash and cash equivalents	7,670	6,970
Premiums receivable, net	445,540	432,484
Other assets	44,588	54,566
Total Admitted Assets	$ 13,183,235	$ 12,511,786
Liabilities and Contingency Reserve		
Benefit liabilities	$ 11,806,072	$ 11,202,955
Claims administration liabilities	529,165	535,975
Retrospective rating adjustments	125,616	121,690
OPEB liabilities	25,763	19,237
Other liabilities	49,588	41,790
Collateral from securities lending activities	27,469	-
Total Liabilities	12,563,673	11,921,647
Contingency reserve	619,562	590,139
Total Liabilities and Contingency Reserve	$ 13,183,235	$ 12,511,786

Total admitted assets of $13,183.2 million increased by $671.5 million, or 5.4 percent, as compared to the end of Fiscal Year 2012, primarily due to increases in total investments of $642.7 million and securities lending collateral of $27.5 million. Total investments grew by $642.7 million compared to the prior year-end due to investment income and a strong stock market. The most significant changes in the investment balances are from increases of $520.6 million in fixed income and short-term investments and $150.3 million in equities, offset by a $29.8 million decline in treasury inflation-protected securities (TIPS). Fixed income investments increased, because bonds were purchased using investment income and due to contributions to the asset class. Specifically, equities and TIPS were sold to bring the investment allocations back in line with longer-term targets. The proceeds from these sales were mainly invested in fixed income.

Both assets and liabilities from securities lending activities increased by $27.5 million as compared to the June 30, 2012, year-end. At the end of Fiscal Year 2012, the Washington State Investment Board (WSIB) changed the custodian bank acting as agent in securities lending transactions from JPMorgan to State Street and recalled all securities on loan. Thus, there were no assets on loan and no collateral held related to securities lending transactions at June 30, 2012. During Fiscal Year 2013, WSIB began securities lending activities with the new custodian bank and had $26.4 million cash collateral held and reinvested as of June 30, 2013. Additional information on securities lending collateral is included in Note 9, Sale, Transfer and Servicing of Financial Assets and Extinguishments of Liabilities, of this report.

Total benefit liabilities increased $603.1 million, or 5.4 percent, to $11,806.1 million during Fiscal Year 2013, as shown by the following table.

Benefit Liabilities
(in thousands)

	Fiscal Year 2013	Fiscal Year 2012
Benefit liabilities, beginning	$ 11,202,955	$ 10,793,048
New liabilities incurred, current year	1,490,113	1,388,204
Development on prior years		
Discount accretion	352,898	379,617
Other development on prior liabilities *	254,184	108,077
Change in discount rate *	65,553	81,346
Claim payments	(1,559,631)	(1,547,337)
Change in benefit liabilities	603,117	409,907
Benefit liabilities, ending	$ 11,806,072	$ 11,202,955

* Unexpected changes.

New liabilities incurred for the current accident year, discount accretion, and claim payments are normal activities that occur every year. The remaining $295.8 million of the benefit liability increase resulted from new information on previously estimated liabilities. Explanations for the unexpected changes follow:

• Reduction in the number of future expected total permanent disability pensions granted for recent accident years.	($261.0)	million
• A 75 percent reduction in the savings assumptions regarding future structured settlements.	$238.0	million
• Increase in the expected number of future claims receiving medical payments for older accident years.	$132.0	million
• Difference between actual pensioner mortality and expected mortality.	$ 32.2	million
• Other accident and medical benefit liability development.	$ 89.0	million
• Decrease in the non-pension discount rate from 2.0 to 1.5 percent.	$ 65.6	million
Total unexpected changes:	$295.8	million

Detailed changes in the benefit liabilities are explained in Note 10, Changes in Benefit and Claims Administration Liabilities, of this report.

During Fiscal Year 2013, total liabilities, other than benefit liabilities and securities lending collateral, increased $11.4 million, or 1.6 percent, mainly due to increases in other accrued liabilities, retrospective rating adjustments, and other post-employment benefits, offset by decreases in claims administration. Retrospective rating adjustments increased largely due to the observed recent improvement in the relative performance of retro-participating firms compared to non-participating firms. Other postemployment benefit (OPEB) liabilities increased mainly due to a prior period adjustment to bring the State Fund's Net OPEB obligation in agreement with the amount calculated by the Washington State Office of the State Actuary. For additional details on the OPEB prior period adjustment, please refer to Note 2, Accounting and Reporting Changes, and for additional details on OPEB accruals, please refer to Note 6.D, Other Postemployment Benefits, of this report.

Results of Operations

Industrial Insurance Fund operating results and certain key financial ratios are presented in the following table:

Summary of Operations and Changes in Contingency Reserve
For the Fiscal Years Ended June 30, 2013 and 2012
(in thousands)

	Fiscal Year 2013	Restated Fiscal Year 2012
Net premiums earned	$ 1,584,213	$ 1,463,393
Net investment income earned	465,868	481,892
Net investment realized gains	87,405	547,771
Self-insured reimbursements	68,795	103,579
Other income	48,898	50,330
Total Revenue Earned	2,255,179	2,646,965
Net benefits (losses) incurred	2,162,748	1,957,245
Claims administration expenses (LAE) incurred	149,818	184,878
Premium administration expenses incurred	36,234	33,980
Other administration expenses incurred	40,352	37,182
Self-insured administration expenses incurred	25,319	24,175
Non-insurance administration expenses incurred	51,822	46,034
Total Administration Expenses Incurred	303,545	326,249
Total Expenses Incurred	2,466,293	2,283,494
Net Transfers In (Out)	-	-
Net Income (Loss)	(211,114)	363,471
Other changes in contingency reserve	240,537	(562,470)
Changes in contingency reserve, net	29,423	(198,999)
Beginning contingency reserve, July 1	590,139	789,138
Ending Contingency Reserve, June 30	$ 619,562	$ 590,139
Loss ratio	136.5%	133.7%
Loss adjustment expense (LAE) ratio	9.5%	12.6%
Loss and LAE Ratio	146.0%	146.3%
Underwriting and other expense ratio	4.8%	4.9%
Combined Ratio	150.8%	151.2%
Less: Net investment income ratio	29.4%	32.9%
Operating Ratio	121.4%	118.3%

The Industrial Insurance Fund's contingency reserve increased by $29.4 million during Fiscal Year 2013, ending with a balance of $619.6 million. The change in the contingency reserve is largely due to equity unrealized gains from a strong stock market, offset by adverse development in prior liabilities and changes in non-tabular account discount rates, as discussed above.

Net premiums earned of $1,584.2 million during Fiscal Year 2013 increased by $120.8 million, or 8.3 percent, from Fiscal Year 2012. This increase is primarily due to an increase in the number of hours reported by employers. In Fiscal Year 2012, employers reported 3,183 million hours worked; this figure has increased to 3,270 million hours for Fiscal Year 2013.

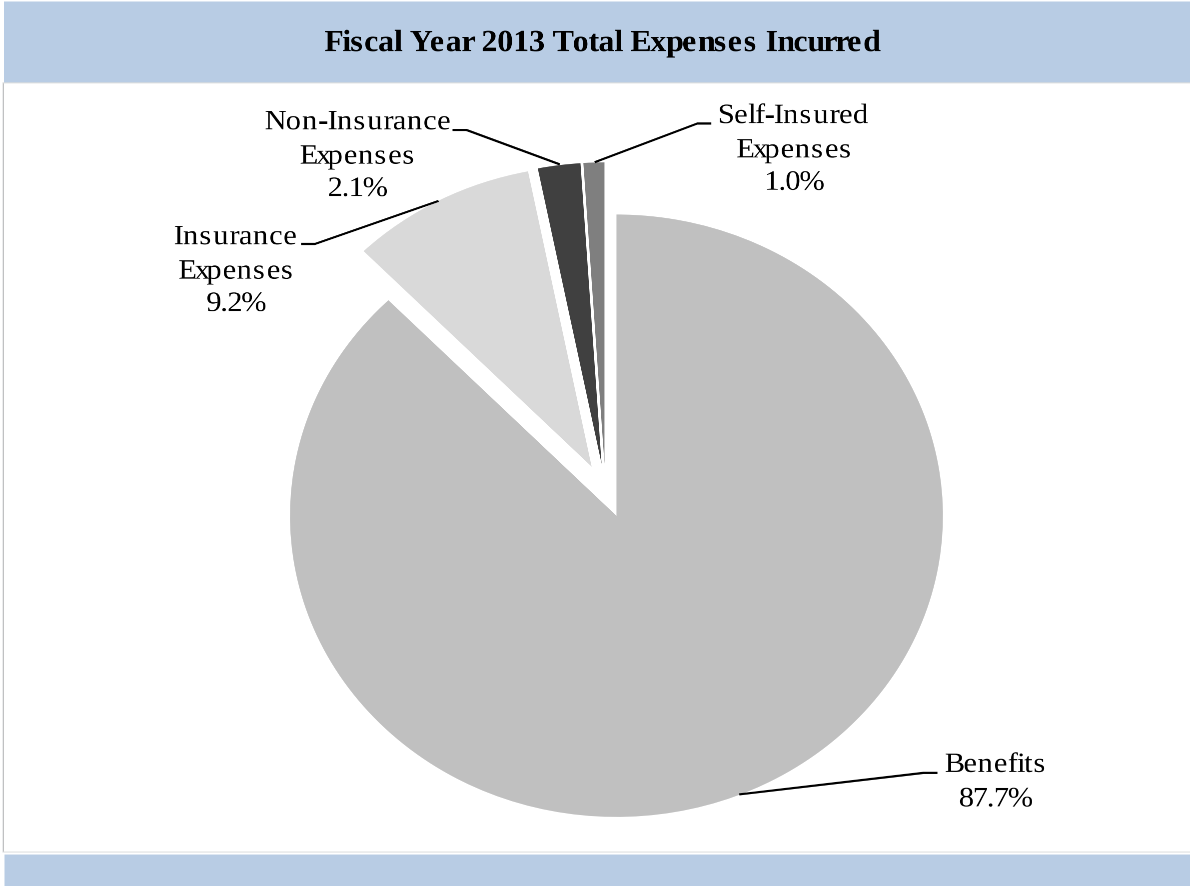
Net investment income earned decreased $16.0 million during Fiscal Year 2013 when compared to the prior year, mostly as a result of lower interest and dividends received. As fixed income securities mature, they are being replaced with bonds yielding a lower interest rate, which resulted in a decrease of $10.1 million in interest income on fixed-income securities. A change in the dividend distribution policy of commingled trust funds resulted in $5.9 million less in dividends. The new policy states that State Street Global Advisors will forgo the distribution of net income to unit holders of Common Trust Funds. All income generated by the portfolio of investments of a given strategy will accumulate in the fund and increase the net asset value of the fund.

Realized gains decreased $460.4 million during Fiscal Year 2013 mainly due to the unusually high Fiscal Year 2012 realized gain of $547.8 million. During Fiscal Year 2012, equities were sold by the WSIB to align with the new passive benchmark which was changed from the Dow Jones US Total Stock Market Index (DJUSTSMI) to MSCI US IMI benchmark.

Benefits incurred during Fiscal Year 2013 totaled $2,162.8 million, an increase of $205.5 million, or 10.5 percent, from Fiscal Year 2012. Benefits incurred is made up of net benefits paid plus the change in benefit liabilities. Benefits paid increased by $12.3 million, as discussed below. Changes in benefit liabilities between Fiscal Year 2013 and Fiscal Year 2012 increased $193.2 million. In Fiscal Year 2012, the change in benefit liabilities increased $409.9 million, primarily due to development on prior accident year liabilities and a change in the discount rate. In Fiscal Year 2013, the change in benefit liabilities increased $603.1 million, as discussed above.

Total administration expenses incurred decreased $22.7 million from Fiscal Year 2012, mainly as a result of decreases in claims administration expenses incurred, offset by an increase in other administration expenses incurred. The decrease in claims administration expenses is primarily due to the change in claims administration liabilities.

The following chart shows the ratio of benefit expense, insurance, non-insurance, and self-insured administration expenses incurred for Fiscal Year 2013:



The following ratios are recognized industry measures used to compare one insurance company to another. The ratios are expressed as a percentage of total net premiums earned.

- The benefit (loss) and loss adjustment expense (LAE) ratio represents the total costs for processing claims and benefits as a percentage of total net premiums earned. Although our LAE ratio is consistently lower than the industry average, our loss ratio is higher than the industry average. There are many factors that impact loss and LAE ratios, including Legislative decisions, claim frequency, severity, and exposure. These ratios were impacted this year by the one-time reduction to the structured settlements savings estimate, continued slow economic recovery, and the change in the benefit liabilities discount rates.

- The combined ratio expresses total insurance costs, including incurred expenses for benefits and administration as a percentage of total net premiums earned. When the total insurance costs exceed net premium revenues, the combined ratio exceeds 100 percent. This is expected, because income earned on investments supplements premium revenues to cover costs, so premium rates are set accordingly to arrive at anticipated breakeven.

- The operating ratio reflects the combined ratio less the net investment income ratio and is another industry measure of overall financial performance. Ratios above 100 percent indicate that expenses are greater than premiums and net investment income earned. Insurance companies are motivated to make profits and, therefore, work towards an operating ratio below 100 percent; however, the Industrial Insurance Fund is operated as a part of state government, and its goal is to break even. An operating ratio greater than 100 percent decreases the contingency reserve balance.

- The combined ratio decreased from 151.2 percent in Fiscal Year 2012 to 150.8 percent in Fiscal Year 2013. The operating ratio increased from 118.3 percent in Fiscal Year 2012 to 121.4 percent in Fiscal Year 2013. Increased benefit costs offset by decreased LAE and lower interest and dividend income impacted these ratios. The Underwriting and Other Expense Ratio of 4.8 percent remains consistently low compared to the industry average.

Cash Flows and Liquidity

Cash Flows - The primary sources of cash were from premiums collected and investment income. The primary uses of cash were for payment of benefits, administration expenses, and purchases of investments.

Cash flows of the Industrial Insurance Fund are summarized as follows:

Cash Flow Summary
For the Fiscal Years Ended June 30, 2013 and 2012
(in thousands)

	Fiscal Year 2013	Fiscal Year 2012
Operations		
Net premiums collected	$ 1,575,083	$ 1,474,455
Other reimbursements and income	108,092	110,932
Net benefits paid	(1,559,631)	(1,547,338)
Insurance administration expenses paid	(227,785)	(213,508)
Self-insured administration expenses paid	(24,582)	(23,319)
Non-insurance administration expenses paid	(49,556)	(44,138)
Cash used in operations	(178,379)	(242,916)
Investment Activities		
Investment income	466,403	484,865
Net realized gains	87,405	547,771
Purchases, net	(370,871)	(786,782)
Investment management expenses	(3,858)	(3,824)
Cash provided by investment activities	179,079	242,030
Change in Cash		
Net increase (decrease) in cash	$ 700	$ (886)

Net premiums collected increased mostly as a result of the Accident Account and Medical Aid Account standard premiums collected increasing by $60.2 million and $40.4 million, respectively, during Fiscal Year 2013 due to an increase in reported hours.

The benefits paid increased $12.3 million, or 0.8 percent, when compared to the prior year. Benefits paid in the Medical Aid and Pension Reserve Accounts increased by $14.3 million and $15.0 million, respectively, but were partially offset by a decrease in the Accident Account of $17.0 million. The net increase of $12.3 million is explained by the following:

- The Accident Account's benefits paid decrease resulted from lower time-loss payments because of fewer active time-loss claims being paid for fewer days and because there were fewer claims receiving permanent partial disability awards.

- The Medical Aid Account's benefits paid increase is due to more medical payments to health care providers and more Stay at Work benefit payments. Health care benefits paid increased because more claimants received benefits, offset by slightly lower average payments. The Stay at Work benefits paid increased due to more employees receiving benefits.

- The pension benefits paid increase is mainly because of higher numbers of pensioners receiving benefits, together with higher average monthly benefits.

Administrative expenses paid increased $21.0 million over the prior year primarily due to administering new reform programs passed during the 2011 Legislative Session, such as the Medical Provider Network, Stay at Work, Structured Settlements, and expansion of Centers for Occupational Health and Education. L&I implemented these new programs half-way through Fiscal Year 2012, and thus, administrative expenses were lower than in Fiscal Year 2013 when these new programs operated for the full year.

The decrease in net investment income collected and realized gain of $478.8 million is comprised of decreases of $12.5 million in bond investment income, $460.4 million in equity and bond investment realized gains, and $5.9 million in dividend income, compared to the prior year. These changes were discussed in the results of operations section above.

There was a net decrease of $415.9 million in the purchase and sale of investments as compared to the prior year due to investment activities and market conditions.

Liquidity - The Industrial Insurance Fund's operations require sufficient liquidity to meet both short-term and long-term requirements. Resources to ensure short-term liquidity come from two basic elements:

- L&I may increase rates in order to increase its contingency reserve, resulting in positive cash flow.

- Premiums are paid to L&I every three months.

The Industrial Insurance Fund has generally met its operating requirements by maintaining appropriate levels of liquidity in its investment portfolio and through utilization of positive cash flow. The Industrial Insurance Fund is able to match projected cash inflows from premiums and investment income from this portfolio with projected cash outflows for payment of benefits.

Future Plan

Workers' compensation rates can have a major impact on businesses in Washington. In an effort to avoid significant, unpredictable rate fluctuations, the Department's long term goals include steadily rebuilding the workers' compensation contingency reserve balance to protect against unexpected changes and gradually decreasing the discount rate used to discount pension liabilities. The Department's nine-year plan that began in 2013 is designed to increase the contingency reserve balance from 13 to 15 percent of total liabilities (less securities lending obligations) and reduce the pension discount rate from 6.5 to 4.5 percent. By the end of Calendar Year 2014, the Department estimates it will increase the contingency reserve balance from $620 million up to $902 million. Currently, the benefit liabilities for pensions are discounted at 6.5 percent, and by the end of Calendar Year 2014, the Department's goal is to reduce the discount rate to 6.3 percent.

Requests for Information

This report is designed to provide a general overview of the Industrial Insurance Fund and to illustrate the Fund's financial position and results of operations to interested parties. If you have any questions about this report or need additional financial information, please contact the Chief Accounting Officer at the Department of Labor & Industries, P.O. Box 44833, Olympia, Washington 98504-4833.

In accordance with the Revised Code of Washington (RCW) 51.44.115, L&I also publishes a Comprehensive Annual Financial Report (CAFR) for the Workers' Compensation Program. This report is prepared in compliance with generally accepted accounting principles (GAAP).

The Industrial Insurance Fund Statutory Financial Information Report and the Workers' Compensation Program CAFR are available at L&I's website at:
http://www.lni.wa.gov/ClaimsIns/Insurance/Learn/StateFund/Reports.

Washington State Department of
Labor & Industries

Keep Washington Safe and Working

Consolidated Statutory Financial Statements

Washington State Department of
Labor & Industries

Keep Washington Safe and Working

Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve

As of June 30, 2013 and 2012

(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Elimination for Consolidated Statements	Total June 30, 2013	Restated Total June 30, 2012
Admitted Assets						
Cash and Investments						
Investments, net						
Fixed income	$ 3,413,167,000	$ 2,760,334,000	$ 2,846,575,000	$ -	$ 9,020,076,000	$ 8,625,928,000
Treasury inflation-protected securities	472,102,000	792,472,000	325,390,000	-	1,589,964,000	1,619,787,000
Equities	535,549,000	766,433,000	428,488,000	-	1,730,470,000	1,580,216,000
Short term	69,929,000	29,306,000	109,448,000	-	208,683,000	82,211,000
Unsettled trade receivables	577,000	565,000	552,000	-	1,694,000	7,000
Total Investments	4,491,324,000	4,349,110,000	3,710,453,000	-	12,550,887,000	11,908,149,000
Securities lending collateral	25,371,000	1,088,000	1,010,000	-	27,469,000	-
Interest receivable	41,396,000	33,092,000	32,593,000	-	107,081,000	109,617,000
Cash and cash equivalents	4,307,000	2,337,000	1,026,000	-	7,670,000	6,970,000
Total Cash and Investments	4,562,398,000	4,385,627,000	3,745,082,000	-	12,693,107,000	12,024,736,000
Other Assets						
Premiums receivable, net, incl. earned but unbilled	285,189,000	160,351,000	-	-	445,540,000	432,484,000
Real estate and improvements						
(less $11,475,000 encumbrances)	14,912,000	14,912,000	-	-	29,824,000	27,798,000
Self-insurance receivables, net	3,516,000	3,452,000	3,789,000	-	10,757,000	12,092,000
Miscellaneous receivables, net	9,015,000	953,000	2,103,000	(8,064,000)	4,007,000	14,676,000
Total Other Assets	312,632,000	179,668,000	5,892,000	(8,064,000)	490,128,000	487,050,000
Total Admitted Assets	$ 4,875,030,000	$ 4,565,295,000	$ 3,750,974,000	$ (8,064,000)	$ 13,183,235,000	$ 12,511,786,000
Liabilities and Contingency Reserve						
Liabilities						
Benefits	$ 4,291,331,000	$ 3,775,655,000	$ 3,739,086,000	$ -	$ 11,806,072,000	$ 11,202,955,000
Other Liabilities						
Claims administration	191,912,000	337,253,000	-	-	529,165,000	535,975,000
Retrospective rating adjustments	125,616,000	-	-	-	125,616,000	121,690,000
Accrued liabilities						
OPEB claim administration	6,529,000	8,042,000	-	-	14,571,000	11,185,000
OPEB other administration	6,693,000	4,499,000	-	-	11,192,000	8,052,000
Other accrued liabilities	24,627,000	21,989,000	10,878,000	(8,064,000)	49,430,000	41,417,000
Deferred revenue	110,000	48,000	-	-	158,000	373,000
Collateral from securities lending activities	25,371,000	1,088,000	1,010,000	-	27,469,000	-
Total Other Liabilities	380,858,000	372,919,000	11,888,000	(8,064,000)	757,601,000	718,692,000
Total Liabilities	4,672,189,000	4,148,574,000	3,750,974,000	(8,064,000)	12,563,673,000	11,921,647,000
Contingency Reserve	202,841,000	416,721,000	-	-	619,562,000	590,139,000
Total Liabilities and Contingency Reserve	$ 4,875,030,000	$ 4,565,295,000	$ 3,750,974,000	$ (8,064,000)	$ 13,183,235,000	$ 12,511,786,000

The Notes to the Consolidated Statutory Financial Statements are an integral part of this statement.

The source of this financial information is the Washington State Agency Financial Reporting System with adjustments for statutory basis of accounting.

Consolidated Statutory Statement of Operations and Changes in Contingency Reserve

For the Fiscal Years Ended June 30, 2013 and 2012

(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Total Fiscal Year 2013	Restated Total Fiscal Year 2012
Revenues					
Net standard premiums earned	$ 1,097,145,000	$ 623,797,000	$ -	$ 1,720,942,000	$ 1,634,266,000
Less net retrospective rating adjustments	(136,729,000)	-	-	(136,729,000)	(170,873,000)
Net premiums earned	960,416,000	623,797,000	-	1,584,213,000	1,463,393,000
Net investment income earned	181,990,000	142,806,000	141,072,000	465,868,000	481,892,000
Net fixed income investment realized gains	15,268,000	19,945,000	38,847,000	74,060,000	31,741,000
Net equity investment realized gains	4,301,000	6,093,000	2,951,000	13,345,000	516,030,000
Self-insured administrative expense assessments	13,708,000	13,171,000	-	26,879,000	25,463,000
Self-insured second injury pension reserve assessments	-	-	26,086,000	26,086,000	56,600,000
Self-insured cash funded & bonded pension reimbursements	-	-	15,830,000	15,830,000	21,516,000
Fines, penalties, and interest	36,882,000	2,381,000	69,000	39,332,000	40,674,000
Other income	7,531,000	2,035,000	-	9,566,000	9,656,000
Total Revenues Earned	1,220,096,000	810,228,000	224,855,000	2,255,179,000	2,646,965,000
Expenses					
Benefits incurred	651,380,000	896,426,000	614,942,000	2,162,748,000	1,957,245,000
Administration expenses incurred:					
Insurance expenses incurred:					
Claims administration expenses incurred	49,148,000	100,670,000	-	149,818,000	184,878,000
Premium administration expenses incurred	17,733,000	18,501,000	-	36,234,000	33,980,000
General insurance administration expenses incurred	13,277,000	6,871,000	-	20,148,000	19,158,000
Other agencies insurance expenses incurred	10,184,000	10,020,000	-	20,204,000	18,024,000
Total insurance expenses incurred	90,342,000	136,062,000	-	226,404,000	256,040,000
Self-insured administration expenses incurred	13,580,000	11,739,000	-	25,319,000	24,175,000
Non-insurance expenses incurred	34,765,000	17,057,000	-	51,822,000	46,034,000
Total Expenses Incurred	790,067,000	1,061,284,000	614,942,000	2,466,293,000	2,283,494,000
Net Income (Loss) Before Transfers	430,029,000	(251,056,000)	(390,087,000)	(211,114,000)	363,471,000
Transfers In (Out)					
Pension funding transfers	(328,325,000)	-	328,325,000	-	-
Net Transfers In (Out)	(328,325,000)	-	328,325,000	-	-
Net Income (Loss)	101,704,000	(251,056,000)	(61,762,000)	(211,114,000)	363,471,000
Other Changes in Contingency Reserve					
Equities unrealized gains (losses)	82,010,000	124,740,000	65,695,000	272,445,000	(583,099,000)
Treasury inflation-protected securities unrealized gains (losses)	538,000	(2,374,000)	(4,480,000)	(6,316,000)	36,671,000
Bonds unrealized gains (losses)	(1,076,000)	427,000	561,000	(88,000)	-
Change in nonadmitted assets	(19,895,000)	(5,595,000)	(14,000)	(25,504,000)	(16,042,000)
Change in Contingency Reserve, Net	163,281,000	(133,858,000)	-	29,423,000	(198,999,000)
Beginning contingency reserve, July 1	39,560,000	550,579,000	-	590,139,000	789,138,000
Ending Contingency Reserve, June 30	$ 202,841,000	$ 416,721,000	$ -	$ 619,562,000	$ 590,139,000

The Notes to the Consolidated Statutory Financial Statements are an integral part of this statement.

The source of this financial information is the Washington State Agency Financial Reporting System with adjustments for statutory basis of accounting.

Consolidated Statutory Statement of Cash Flows
For the Fiscal Years Ended June 30, 2013 and 2012
(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Total Fiscal Year 2013	Total Fiscal Year 2012
Standard premiums collected	$ 1,089,169,000	$ 618,717,000	$ -	$ 1,707,886,000	$ 1,614,797,000
Less retrospective rating adjustments	(132,803,000)	-	-	(132,803,000)	(140,342,000)
Net premiums collected	956,366,000	618,717,000	-	1,575,083,000	1,474,455,000
Self-insured administration expense reimbursements	13,479,000	12,950,000	-	26,429,000	24,530,000
Self-insured second injury pension reserve reimbursements	-	-	35,593,000	35,593,000	38,640,000
Self-insured cash funded and bonded pension reimbursements	-	-	17,490,000	17,490,000	18,746,000
Fines, penalties, and interest	21,295,000	2,124,000	-	23,419,000	23,243,000
Other income (expenses)	7,151,000	(1,044,000)	(946,000)	5,161,000	5,773,000
Fund transfers in (out)	(379,108,000)	-	379,108,000	-	-
Operating Cash Flow In	619,183,000	632,747,000	431,245,000	1,683,175,000	1,585,387,000
Benefits paid	605,744,000	579,604,000	374,283,000	1,559,631,000	1,547,338,000
Administration expenses:					
Insurance expenses:					
Claims administration expenses	60,002,000	93,240,000	-	153,242,000	141,242,000
Premium administration expenses	17,227,000	17,974,000	-	35,201,000	35,055,000
General insurance administration expenses	12,991,000	6,701,000	-	19,692,000	19,298,000
Other agencies insurance expenses	9,942,000	9,708,000	-	19,650,000	17,913,000
Total insurance expenses	100,162,000	127,623,000	-	227,785,000	213,508,000
Self-insured administration expenses	13,215,000	11,367,000	-	24,582,000	23,319,000
Non-insurance expenses	33,469,000	16,087,000	-	49,556,000	44,138,000
Total Administration Expenses Paid	146,846,000	155,077,000	-	301,923,000	280,965,000
Operating Cash Flow Out	752,590,000	734,681,000	374,283,000	1,861,554,000	1,828,303,000
Net Operating Cash Flow In (Out)	(133,407,000)	(101,934,000)	56,962,000	(178,379,000)	(242,916,000)
Investment income - bonds	181,571,000	143,143,000	140,763,000	465,477,000	478,022,000
Investment income - equities	292,000	404,000	230,000	926,000	6,843,000
Net realized gains on investments	19,569,000	26,038,000	41,798,000	87,405,000	547,771,000
Net (purchases) sales of investments	(65,825,000)	(66,089,000)	(238,957,000)	(370,871,000)	(786,782,000)
Investment expenses	(1,427,000)	(1,353,000)	(1,078,000)	(3,858,000)	(3,824,000)
Total Investment Cash Flow In (Out)	134,180,000	102,143,000	(57,244,000)	179,079,000	242,030,000
Net Cash Flow In (Out)	773,000	209,000	(282,000)	700,000	(886,000)
Beginning Cash, July 1	3,534,000	2,128,000	1,308,000	6,970,000	7,856,000
Ending Cash, June 30	$ 4,307,000	$ 2,337,000	$ 1,026,000	$ 7,670,000	$ 6,970,000

The Notes to the Consolidated Statutory Financial Statements are an integral part of this statement.
The source of this financial information is Washington State's Agency Financial Reporting System (AFRS) with adjustments for statutory basis of accounting.

Washington State Department of
Labor & Industries

Keep Washington Safe and Working

Notes to the Consolidated Statutory Financial Statements

For the Fiscal Years Ended June 30, 2013 and 2012

Index

Note 1 - Summary of Significant Accounting Policies

1.A. Nature of Operations

The state of Washington's Department of Labor & Industries (L&I) administers the state's Workers' Compensation Program. Through Title 51 of the Revised Code of Washington (RCW), Washington State requires all employers, unless exempt, to secure coverage for job-related injuries and illnesses either by paying insurance premiums to the Industrial Insurance Fund or by self-insuring. The agency is the exclusive writer of workers' compensation insurance in the state of Washington for all businesses except the self-insured. Direct private insurance is not authorized, although self-insurers are permitted to reinsure up to 80 percent of their obligations.

Chapter 51.44 RCW provides six benefit accounts: the Accident Account, Medical Aid Account, Pension Reserve Account, Supplemental Pension Account, Second Injury Account, and the Self-Insured Employer Overpayment Reimbursement Account, primarily to make compensation payments to injured workers or to medical providers for rehabilitation services to injured workers. A seventh account, called the Industrial Insurance Rainy Day Fund Account, was created during the 2011 Legislative Session. The purpose of the account is to receive transfers of funds from the Accident and Medical Aid Accounts when assets for those accounts combined are between 10 and 30 percent in excess of their funded liabilities. The funds are then set aside to reduce a rate increase or aid businesses during or recovering from economic recessions. The Industrial Insurance Rainy Day Fund Account did not have any activity during or balance at the end of Fiscal Year 2013. These seven accounts are known collectively as the Workers' Compensation Program.

The Accident, Medical Aid, and Pension Reserve Accounts are referred to as the Industrial Insurance Fund and are the focus of this report. The Supplemental Pension, Second Injury, Self-Insured Employer Overpayment Reimbursement, and Industrial Insurance Rainy Day Fund Accounts are not part of the Industrial Insurance Fund and are not included in this report.

The Industrial Insurance Fund is self-sustaining through the ability to assess the appropriate rates of insurance premiums and prudent investment management. The three accounts are maintained on an actuarially solvent basis, except that a cash-flow basis is used for the components of the Pension Reserve Account when self-insured employers guarantee related benefits with a surety bond. The accompanying consolidated statutory statements report on the financial position and results of operations of the Industrial Insurance Fund.

1.A.1. Description of the Industrial Insurance Fund

The Accident Account pays compensation directly to injured workers for lost wages during temporary disability and permanent partial disability awards. It also pays costs for vocational retraining and for structured settlements. The Structured Settlement Program was created by House Bill 2123 during the 2011 Legislative Session and is a voluntary program in which those who are eligible can negotiate an agreement for the non-medical portion of a claim and receive settlement payment(s).

Pursuant to RCW 51.44.070, funds from the Accident Account are to be transferred to the Pension Reserve Account for the present value of pensions awarded to survivors of fatally injured workers and to workers who have a permanent total disability.

Revenues for this account are from employer-paid premiums based on individual employers' reported payroll hours and are reported net of refunds. Employers may elect to have their premiums retrospectively rated with an annual adjustment for actual benefits incurred. The retrospective adjustment calculation considers both the Accident and Medical Aid Accounts' experience and premiums together and may result in either a rebate of premiums paid or an assessment of additional premiums due. All retrospective premium adjustments are financed entirely through the Accident Account.

On behalf of injured workers, the Medical Aid Account pays for the cost of medical, vocational rehabilitation services, and Stay at Work reimbursements. The Stay at Work Program was also created by House Bill 2123 during the 2011 Legislative Session and is a financial incentive program that encourages employers to bring employees recovering from on-the-job injuries back to light-duty or transitional work.

Equal contributions from employers and employees fund this account. It is the employer's responsibility to collect the employee portion of the medical aid premium and submit the employee and employer contributions to Labor & Industries quarterly.

The Pension Reserve Account pays benefits to all permanently disabled pensioners (including disabled employees of self-insured employers), their dependents, and surviving dependents of fatalities.

Funding for pension payments is generated by transfers from the Accident and Second Injury Accounts and cash funded or bonded pension payments from self-insured employers. Funding required to cover estimated present cash value of monthly pension payments is calculated upon the basis of an annuity; such annuity values are based upon L&I's experience as to rates of mortality, disability, remarriage, and interest, according to RCW 51.44.070.

1.B. Accounting Practices and Basis of Presentation

The Industrial Insurance Fund follows the Statements of Statutory Accounting Principles (SSAP) as promulgated by the National Association of Insurance Commissioners (NAIC), as directed by RCW 51.44.115. The SSAP are very conservative in nature and are designed to protect injured workers to ensure that, in the event of liquidation, sufficient amounts have been set aside to provide for outstanding claims. This accounting basis is used to present solvency and the adequacy of premium rates.

SSAP standards are required to be used by property and casualty insurance enterprises in the United States when reporting their financial position to state insurance regulators, subject to any differences prescribed or permitted by each state's law. The NAIC defines prescribed accounting practices as "… those practices that are incorporated directly or by reference by state laws, regulations and general administrative rules applicable to all insurance enterprises domiciled in a particular state. The NAIC Accounting Practices and Procedures Manual (AP&P) is not intended to preempt states' legislative and regulatory authority."[1] Washington's (WA) prescribed differences from the NAIC are addressed in RCW 48.13.071, which provides limits on investments. The NAIC defines permitted practices as "…practices specifically requested by an insurer that depart from SSAP and state-prescribed accounting practices, and have received approval from the insurer's domiciliary state regulatory authority."[1]

In accordance with Title 51 RCW and Title 296 of the Washington Administrative Code (WAC), the Industrial Insurance Fund is administered by L&I. Pursuant to Title 48 RCW and Title 284 WAC, L&I is not required to file annual statements with the Washington State Office of the Insurance Commissioner (WSOIC). The Industrial Insurance Fund is not required to report to the WSOIC or complete an annual statement in accordance with the NAIC annual statement filing instructions. Since the Industrial Insurance Fund is not subject to oversight by the WSOIC, there is no requirement that the Industrial Insurance Fund request approval from WSOIC for departures from the SSAP. Thus, we have no such permitted practices.

While there are no prescribed or permitted practices followed by the Industrial Insurance Fund that differ from SSAP, a long-established practice of discounting on a non-tabular basis exists that departs from SSAP No. 65, which allows discounting fixed and reasonably determinable payments on a tabular only basis. Non-tabular discounting is only permitted in certain instances in which states have prescribed or permitted practices to allow it. (See Note 1.C.3 and Note 12.B for additional information on discounting methodology and non-tabular discounting.)

In addition, the Industrial Insurance Fund recognizes a liability for the net Other Postemployment Benefit (OPEB) obligation based on Governmental Accounting Standards Board (GASB) Statement No. 45 – Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions. The net OPEB obligation includes the unfunded actuarial accrued liability amortized over thirty years. This practice departs from SSAP No. 92. The Industrial Insurance Fund participates in a multiemployer OPEB plan. SSAP No. 92 states that employers with multiemployer plans are not required to recognize the unfunded status of the OPEB plan, but are only required to recognize the required contribution to the plan for the period reported.

[1] NAIC AP&P Manual as of March 2012, Section: Permitted Practices Advance Notification Requirement, Implementation Questions and Answers, Question 2.

The following table shows the Industrial Insurance Fund's net income and contingency reserve as reported on the accompanying financial statements and what they would have been if there were no departures from NAIC SSAP requirements.

Effect of Practices that Depart from SSAP

	As of and for the Fiscal Year Ended June 30, 2013	Restated As of and for the Fiscal Year Ended June 30, 2012
Net Income, WA basis	**$ (211,114,000)**	**$ 363,471,000**
Effect of WA prescribed practices	-	-
Effect of WA permitted practices	-	-
Effect of practices that depart from SSAP:		
Non-tabular discounting	394,392,000	379,588,000
OPEB administration liability	6,526,000	5,675,000
Net Income, NAIC SSAP basis	**$ 189,804,000**	**$ 748,734,000**
Contingency Reserve, WA Basis	**$ 619,562,000**	**$ 590,139,000**
Effect of WA prescribed practices	-	-
Effect of WA permitted practices	-	-
Effect of practices that depart from SSAP:		
Non-tabular discounting	(1,519,111,000)	(1,913,503,000)
OPEB administration liability	25,763,000	19,237,000
Contingency Reserve, NAIC SSAP basis	**$ (873,786,000)**	**$ (1,304,127,000)**

The financial statement layout and terminology were selected based on the terminology and formatting customary to governmental insurance funds. The Industrial Insurance Fund refers to losses as "benefits" and loss adjustment expenses as "claims administration expenses." Any surplus remaining in the Fund is referred to as "contingency reserve."

1.B.1. Use of Estimates

The preparation of financial information in conformity with the SSAP requires management to make estimates and assumptions that affect the reported amounts of admitted assets, liabilities, and contingency reserve at the date of the financial information and the reported amounts of revenues and expenses during the reporting period. Material estimates that are susceptible to significant changes include benefit and claims administration liabilities, premium receivables, self-insurance receivables, retrospective rating adjustment liabilities, and accrued liabilities for other postemployment benefits. Actual results could differ materially from those estimates.

Management's estimates are based on its knowledge of and experience about past and current events and circumstances and its assumptions about conditions it expects will exist in the future. The most significant estimates made in these statutory financial statements are the benefit and claims administration liabilities at the date of the financial information. Factors relevant to the estimation of these liabilities include the estimation of the ultimate frequency and severity of losses, the level of inflation of future medical costs over long periods of time, the future legal environment, and the amount of future expenses required to investigate and settle claims. Management's estimates are reviewed after the fiscal year-end by a nationally recognized, qualified consulting actuarial firm. The independent actuarial firm's opinion is included at the end of this report.

1.B.2. Differences between SSAP and GAAP

The SSAP followed by the Industrial Insurance Fund vary in some respects from Generally Accepted Accounting Principles (GAAP) as promulgated by the Financial and Governmental Accounting Standards Boards. Some of the most significant differences between the SSAP and GAAP are as follows:

- Investments in bonds are reported for SSAP at amortized cost or market value based on their NAIC rating; for GAAP, such fixed maturity investments would be designated at purchase as held-to-maturity, trading, or available-for-sale. Held-to-maturity fixed investments would be reported at amortized cost. The remaining fixed maturity investments would be reported at fair value with unrealized holding gains and losses reported in operations for those designated as trading and as a separate component of capital and surplus for those designated as available-for-sale.

- For SSAP, all loan-backed securities are adjusted for the effects of changes in prepayment assumptions using the prospective method, which equates the carrying amount of the investment to the present value of the anticipated future cash flows using a recalculated effective yield. The recalculated yield is then used to accrue income on the investment balance for subsequent accounting periods. If it is determined that a decline in fair value is other-than-temporary, the cost basis of the security is written down to the undiscounted estimated future cash flows. Under GAAP, all securities other than high-credit quality securities are adjusted using the prospective method when there is a change in estimated future cash flows. If it is determined that a decline in fair value is other-than-temporary, the cost basis of the security is written down to the discounted fair value. If high-credit quality securities are adjusted, the retrospective method is used, which equates the present value of the actual and anticipated cash flows with the original cost of the investment. The current balance is then increased or decreased to the amount that would have resulted had the revised yield been applied since inception, and the investment income is decreased or increased.

- SSAP assets designated as "nonadmitted assets" are excluded from total admitted assets and defined as assets having economic value other than those which can be used to fulfill policyholder obligations and assets unavailable due to encumbrances or third party interests. These assets consist primarily of premiums in collection that have been outstanding for over ninety days, office furniture, equipment, and prepaid expenses. Nonadmitted assets are charged against the contingency reserve unless otherwise specifically addressed within the NAIC's Accounting Practices and Procedures Manual. Under GAAP, premium receivables are presented net of allowance for doubtful accounts;

furniture and equipment are presented net of accumulated depreciation; and prepaid expenses are presented at full cost.

- SSAP limits the aggregate amount of admitted electronic data processing equipment and operating system software, net of accumulated depreciation, to 3 percent of the reporting entity's capital and surplus. Under GAAP, computer equipment and software purchases meeting the state's capitalization criteria are recorded as assets, net of accumulated depreciation, with no limitations.

- The focus of SSAP accounting is solvency; therefore, it is concerned with assets that can be used immediately to cover benefit liabilities. GAAP accounting is focused on "going concern," which assumes that an entity has the ability to survive, and therefore, assets and liabilities are presented in the order of liquidity and classified as current and non-current.

- The Consolidated Statutory Statement of Operations and Changes in Contingency Reserve presents premiums earned and investment income as the primary revenue sources, and expenses are presented as activities. GAAP presentations separate operating income from investment income, since investment activity is not normally a primary revenue source. GAAP also presents expenses by character rather than by the purpose of the item purchased or service obtained and the net effect of revenues and expenses as a change in net position.

- Both SSAP and GAAP require the statement of cash flows to be prepared using the direct method. However, the statutory statement of cash flows differs in certain aspects from the presentation required by GAAP. On the SSAP Consolidated Statement of Cash Flows, Cash Flows In includes operating transfers and other income. Cash Flows Out is categorized by benefits paid and administration expenses. The GAAP statement of cash flows includes a reconciliation between operating income from the statement of operations and cash flows from operating activities.

1.C. Significant Accounting Policies

1.C.1. Recognition of Premiums

Premiums are based on individual employers' reported payroll hours and insurance rates based on each employer's risk classification(s) and past experience. In addition to its regular premium plans, the Industrial Insurance Fund offers a retrospective premium rating plan under which an employer's premiums are adjusted annually for up to three years following the plan year, based on the employer's actual loss experience.

Employers' workers' compensation insurance premiums are due within 30 days following each calendar quarter in which payroll hours are reported. Net premiums receivable reported in the financial statement is an actuarial estimate of the two most recent quarters' uncollected premium balances, based on past collection statistics, growth projection, observed development of premiums reported, statistical analysis, and other factors, including actuarial judgment. This amount represents the estimated premiums that will ultimately be collected. All premium receivables exceeding 90 days in age are adjusted as nonadmitted assets in the current period and are not included in the net premiums receivable amount. For premium receivables over 90 days in age, collection efforts are continued until the premiums are collected or all legal means are exhausted.

According to SSAP No. 60, a premium deficiency reserve is recognized "…when anticipated losses, loss adjustment expenses, and maintenance costs exceed the recorded unearned premium reserve and contingency reserve." Because the Industrial Insurance Fund has no unearned premium reserves or installment premium contracts, no premium deficiency reserve is recorded.

1.C.2. Benefit and Claims Administration Liabilities

The Industrial Insurance Fund establishes benefit and claims administration liabilities arising from its workers' compensation coverage based on estimates of the ultimate cost of benefits that have been reported but not resolved and claims that have been incurred but not reported. The length of time for which such costs must be estimated varies depending on the type of benefit involved. Since actual claim costs depend on complex factors such as inflation, changes in doctrines of legal liabilities, claim adjudication, and judgments, the actual ultimate claim costs may differ from the estimates.

Benefit and claims administration liabilities are recomputed quarterly using a variety of actuarial and statistical techniques. These techniques are used to produce current estimates that reflect recent settlements, claim frequency, expected inflation, and other economic, legal, and social factors. A provision for inflation in the calculation of estimated future benefits 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.

Future premium income is not offset against benefit liabilities, because benefit liabilities come from coverage periods for which premiums have, in general, already been fully earned. The obligation to pay benefit and claims administration liabilities is not contingent upon any future premiums for future coverage periods.

Adjustments to benefit and claims administration liabilities are charged or credited to benefit and claims administration expense in the periods in which they are made. Unpaid benefits and claims administration expenses include amounts based on past experience for claims development on reported claims and benefits incurred but not reported. Such liabilities are necessarily based on assumptions and estimates, and while management believes the amount is adequate, the ultimate liability may be in excess of or less than the amount provided. The methods for making such estimates and for establishing the resulting liabilities are continually reviewed, and any adjustments are reflected in the period affected.

1.C.3. Discounting Methodology

The Industrial Insurance Fund discounts benefit and claims administration expense reserves to reflect the time value of money. The Industrial Insurance Fund uses both tabular and non-tabular discounting. Non-tabular discounting is an accounting practice that departs from SSAP No. 65 as disclosed in 1.B of this note. The bullets below discuss the discount method and rate applied to each discounted liability category.

- The benefit liabilities in the Pension Reserve Account are discounted on a tabular basis at 6.5 percent.

- Liabilities in the Accident Account for pensions incurred but not yet awarded are discounted on both a tabular and non-tabular basis. For each future pension award, the estimated future pension payments are discounted from the anticipated payment dates back to the anticipated date of the pension award on a tabular basis at 6.5 percent. The payments are then discounted from the anticipated date of the pension award back to June 30, 2013, on a non-tabular basis at 1.5 percent.

- All other Accident and Medical Aid Account benefit and claims administration liabilities are discounted on a non-tabular basis at 1.5 percent.

The Industrial Insurance Fund's non-tabular discount rate is set 2 percentage points less than the 5-year average of the 20-year U.S. Treasury yield, rounded to the nearest one-half percent. Since interest rates have decreased and have remained low, the non-tabular discount rate dropped from 2.0 percent to 1.5 percent during Fiscal Year 2013. As a result of this non-tabular discount rate change, benefit and claims administration expense liabilities increased.

In the reserving process, the long-term inflation rate assumption is set equal to the non-tabular discount rate, and this long-term inflation rate is the basis for the medical inflation assumptions. This decrease in the long-term inflation rate lowered the medical inflation assumptions, which reduced the Medical Aid Account benefit and claims administration expense liabilities. In the Medical Aid Account, the effect of the reduction in the medical inflation assumptions largely offsets the effect of the lower discount rate on these expenses.

The net effects of reducing both the non-tabular discount rate and the long-term inflation rate assumptions from 2.0 percent to 1.5 percent were an increase of $83.4 million in benefit liabilities and a decrease of the same amount in contingency reserve, as shown in the table below.

Effects of Non-Pension Discount Rate Change on Benefit and Claims Administration Expense
June 30, 2013
(in thousands)

	Long-Term Inflation Rate & Non-Pension Discount Rate @ 2.0%	Effect of Reducing Non-Pension Discount Rate to 1.5%	Effect of Reducing Long-Term Inflation Rate to 1.5%	Long-Term Inflation Rate & Non-Pension Discount Rate @ 1.5%	Net Effect of Changing Long Term Inflation Rate and Non-Pension Discount Rate: Dollars	Percent
Accident Account	$ 4,407,027	$ 76,216	$ -	$ 4,483,243	$ 76,216	1.7%
Medical Aid Account	4,105,731	297,671	(290,495)	4,112,908	7,177	0.2%
Total	$ 8,512,758	$ 373,887	$ (290,495)	$ 8,596,151	$ 83,393	1.0%

1.C.4. Cash and Cash Equivalents

Cash includes cash in banks, cash on deposit with the Office of the State Treasurer (OST), and cash on hand. It also consists of cash equivalents invested by the OST which are short-term, highly liquid investments that are readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of interest rates. Under RCW 43.08.015, the OST has the statutory responsibility to ensure the effective cash management of state public funds. RCW 43.84.080 authorizes the Treasurer to invest available cash and includes a list of eligible investments.

The beginning and ending cash and cash equivalent amounts on the Consolidated Statutory Statement of Cash Flows do not include short-term investments. It is not practical to include short-term investments because of the volume of transactions and complexity involved in reporting, as they are managed by the Washington State Investment Board (WSIB), a separate Washington State agency.

The U.S. Department of Energy has contracted with L&I to pay benefits to the Industrial Insurance Fund for workers injured on the job at the Hanford nuclear production complex. The Industrial Insurance Fund has received amounts, including trust cash and trust investments, in advance from the U.S. Department of Energy to cover the pension liability for these injured workers. These amounts are not reported in the financial statements.

As of June 30, 2013, trust cash amounted to $510,031 and is available to reimburse the Industrial Insurance Fund for monthly pension payments. In addition, trust investments totaling $3,007,396 were invested in U.S. Treasury Notes and are also available to reimburse the Industrial Insurance Fund for future expenses.

1.C.5. Investments

The Industrial Insurance Fund uses the following accounting policies to value investments:

- Investment grade bonds are stated at amortized cost using the scientific interest method. Non-investment grade bonds with NAIC designations of 3-6 are stated at the lower of amortized cost or fair value. Fair values are reported using pricing sources approved by the NAIC. The Industrial Insurance Fund holds only investment grade securities, as defined by Lehman Barclays Capital Global Family of Fixed Income Indices.

- Short-term investments are stated at amortized cost using the scientific interest method. Per SSAP No. 2, accounting for short-term investments should follow guidance for similar long-term investments (see discussion above on investment grade bonds). Therefore, any short-term bond premiums and discounts are amortized using the scientific interest method.

- Common stocks are stated at fair value.

- Investment grade loan-backed securities are stated at amortized cost. Non-investment grade loan-backed securities with NAIC designations of 3-6 are stated at the lower of amortized cost or fair value. Fair values are reported using pricing sources approved by the NAIC. The Industrial Insurance Fund holds only investment grade securities, as defined by Lehman Barclays Capital Global Family of Fixed Income Indices. In compliance with SSAP No. 43R, changes in currently estimated cash flows are reviewed quarterly using the Bloomberg investment valuation model for prepayment assumptions in valuing mortgage backed securities. These securities are revalued using the prospective adjustment method. See Note 2.G. for other-than-temporary impairment analysis of mortgage-backed securities.

- Treasury Inflation-Protected Securities (TIPS) are indexed and presented net at par and include a consideration of unrealized gains on the change in par, in accordance with SSAP Interpretation 01-25. Changes in fair value are not considered until traded.

- Securities Lending Collateral - Cash received as collateral on securities lending transactions and investments made with that cash are reported as assets. Securities received as collateral are reported as assets if the Industrial Insurance Fund has the ability to pledge or sell them without a borrower default. Liabilities resulting from these transactions are also reported in the balance sheet. Securities lending transactions collateralized by securities that the Industrial Insurance Fund does not have the ability to pledge or sell unless the borrower defaults are not reported as assets or liabilities.

1.C.6. Capital Assets

In accordance with the Washington State Office of Financial Management’s policy, it is the Industrial Insurance Fund’s policy to capitalize:

- All land

- Buildings, building improvements, and leasehold improvements with a cost of $100,000 or greater

- All capital assets with a unit cost of $5,000 or greater, unless otherwise noted

- Infrastructure with a cost of $100,000 or greater

- Intangible assets either purchased or internally developed, with a cost of $1,000,000 or greater, that are “identifiable” by meeting either of the following conditions:

    - The asset is capable of being separated or divided and sold, transferred, licensed, rented, or exchanged; or

    - The asset arises from contractual or other legal rights, regardless of whether those rights are transferable or separable

- All capital assets acquired with a Certificate of Participation

Capital assets are recorded at cost. Capital asset costs include the purchase price plus those costs necessary to place the asset in its intended location and condition for use. Normal maintenance and repair costs that do not materially add to the value or extend the life of capital assets are not capitalized. The cost and related accumulated depreciation of disposed capital assets are removed from the accounting records.

The value of assets constructed for use in the Industrial Insurance Fund includes all direct construction costs and indirect costs that are related to the construction. Net interest costs incurred during the period of construction, if material, are capitalized.

Depreciation and amortization expenses are calculated using the straight-line method over the estimated useful lives of the assets. Total depreciation and amortization expense for capital assets was $8.4 million for the fiscal year ended June 30, 2013, and $6.6 million for the fiscal year ended June 30, 2012.

Generally, estimated useful lives are as follows:

- Buildings and building components 5 to 50 years
- Furnishings, equipment, and collections 3 to 50 years
- Other improvements 3 to 50 years
- Infrastructure 20 to 50 years
- Intangible assets with definite useful lives 3 to 50 years

In accordance with the SSAP, not all capitalized assets are admitted for reporting purposes. Common examples of nonadmitted capital assets are equipment, furniture, and supplies. These nonadmitted assets are adjusted from the respective account's contingency reserve, and current purchases are immediately expensed. SSAP No. 16 allows electronic data processing equipment (EDP) and operating system software to be admitted, up to 3 percent of the contingency reserve; however, the Industrial Insurance Fund takes a more conservative approach and does not admit any EDP equipment or operating system software.

1.C.7. Risk Management

The state of Washington operates a self-insurance liability program pursuant to RCW 4.92.130. The state's policy is generally not to purchase commercial insurance for the risk of losses to which it is exposed. Instead, the state's management believes it is more economical to manage its risks internally and set aside assets for claims settlement in the Risk Management Fund, an internal service fund. A limited amount of commercial insurance is purchased for certain liabilities and to limit the exposure to catastrophic losses. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past eleven fiscal years. Otherwise, the self-insurance liability program services all claims against the state for injuries and property damage to third parties.

The Workers' Compensation Program participates in the state's self-insurance liability program, in proportion to its anticipated exposure to liability losses, to manage its various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; and natural disasters.

Note 2 - Accounting and Reporting Changes

The Washington State Office of Financial Management (OFM) records the Net OPEB Obligation (NOO) for the Industrial Insurance Fund. Prior to Fiscal Year 2013, OFM estimated the Industrial Insurance Fund's portion of the state's NOO based on the current year's employee benefit expense. In Fiscal Year 2013, OFM adopted the specific NOO for the Industrial Insurance Fund calculated by the Washington State Office of the State Actuary (OSA) to record the Industrial Insurance Fund's NOO. An entry for the difference of $9,769,132 was made to bring the Industrial Insurance Fund's NOO in agreement with the amount calculated by OSA. See Note 6.D. Other Postemployment Benefits for more details.

The difference between the amount calculated by OSA as of July 1, 2011, and the amount actually reported in the prior year financial statements is treated as a change in accounting principle, in accordance with SSAP No. 3 *Accounting Changes and Correction of Errors*. The cumulative effect of this change was a $9,769,132 increase in contingency reserve as of July 1, 2012 and 2011, as shown in the table below. The total liabilities at July 1, 2012, also decreased by the same amount. This change has no impact on net income and total admitted assets in the two fiscal years.

Other Postemployment Benefits

	June 30, 2013	Restated June 30, 2012
Contingency reserve at June 30, 2012 and 2011, as previously reported	$ 580,370,000	$ 779,369,000
Cumulative effect of changes in accounting principles - Net OPEB Obligation	9,769,000	9,769,000
Contingency reserve at July 1, 2012 and 2011	$ 590,139,000	$ 789,138,000
Total liabilities at June 30, 2013 and 2012, as previously reported	$ 12,563,673,000	$ 11,931,416,000
Cumulative effect of changes in accounting principles - Net OPEB Obligation	-	(9,769,000)
Total liabilities at June 30, 2013 and 2012	$ 12,563,673,000	$ 11,921,647,000

Note 3 - Investments

3.A. Summary of Investment Policies

Under RCW 43.33A.030, trusteeship over the Industrial Insurance Fund's investments is vested in the voting members of the WSIB. The Legislature established a standard of care for investment of these funds in RCW 43.33A.140. Additionally, the WSIB and its staff must

comply with other state laws, such as the Ethics in Public Service Act chapter 42.52 RCW, as it makes investment decisions and seeks to meet its investment objectives.
In accordance with RCW 43.33A.110, Industrial Insurance Fund investments are to be managed to limit fluctuations in the industrial insurance premiums and, subject to this purpose, achieve a maximum return at a prudent level of risk. Based on this requirement, the strategic objectives are to:

- Maintain the solvency of the accounts
- Maintain premium rate stability
- Ensure sufficient assets are available to fund the expected liability payments
- Subject to the objectives above, achieve a maximum return at a prudent level of risk

Performance objectives are intended to provide the WSIB and the Industrial Insurance Fund with a way to measure the success of this investment policy, the overall asset allocation strategy, and the implementation of that strategy over time. First and foremost, the performance of the investment portfolios shall be judged relative to the strategic objectives. With the first three criteria met, the actual rates of return of the portfolios will be compared to the Comparable Market Index (CMI) for each account. The CMI’s are developed and calculated with the goal to construct a hypothetical passive portfolio with the duration, asset allocation, and appropriate mix of fixed income sectors based on the individual targets for each Industrial Insurance Fund account. The return for each account’s portfolio should not be significantly different from that of its CMI over the long-term.

Eligible Investments - Eligible investments are securities and deposits that are in accordance with the Industrial Insurance Fund’s investment policy and RCW 43.33A.110. Eligible investments include:

- U.S. equities
- International equities
- Treasury inflation protection securities (TIPS)
- U.S. treasuries and government agencies
- Credit bonds
- Mortgage-backed securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices
- Asset-backed securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices

- Commercial mortgage-backed securities rated investment grade, as defined by Barclays Capital Global Family of Fixed Income Indices

- Investment grade non-U.S. dollar bonds

Investment Restrictions - To meet stated objectives, investments of the Industrial Insurance Fund are subject to the following constraints:

- All assets under the management of the WSIB are to be invested to maximize return at a prudent level of risk in accordance with RCW 43.33A.110 and RCW 43.33A.140.

- Asset allocation will be reviewed every three to four years, or sooner if there are significant changes in funding levels or the liability durations.

- Assets will be rebalanced across asset classes when the fair value of the assets falls outside the policy ranges. The timing of any rebalancing will be based on market opportunities, cash flows, and the consideration of transaction costs; therefore, they need not occur immediately.

- Sector allocation for U.S. equities should be within a range of 55 to 65 percent. Allocation for international equities should be within a range of 35 to 45 percent.

- No corporate fixed income issue cost shall exceed 3 percent of the Fund's fair value at the time of purchase, nor shall its fair value exceed 6 percent of the Fund's fair value at any time. This rule applies to any specific corporate bond relative to all of the Fund's assets in aggregate, across all accounts and all their asset class holdings.

- The benchmark and structure for U.S. equities will be the broad U.S. stock market as defined by the Morgan Stanley Capital International (MSCI) US Investable Market Index (IMI) passive mandate. The benchmark and structure for international equities will be the MSCI All Country World Ex U.S. IMI (MSCI ACW Ex U.S. IMI). Both portfolios will be 100 percent passively managed in commingled index funds. The commingled funds may use futures for hedging or establishing a long position.

- The fixed income portfolios' structures vary, depending upon the required duration target. The duration targets will be reviewed every three years, or sooner if there are significant changes in the funding levels or the liability durations.

- The Treasury Inflation-Protected Securities (TIPS) will be managed to plus or minus 20 percent of the duration of the Barclays Capital U.S. TIPS Index.

- Sector allocation of fixed income investments must be managed within the following prescribed ranges:

  - U.S. Treasuries and government agencies — 5 to 25 percent

  - Credit bonds — 20 to 70 percent

- Asset-backed securities 0 to 10 percent
- Commercial mortgage-backed securities 0 to 10 percent
- Mortgage-backed securities 0 to 25 percent

These targets are long-term in nature. Deviations may occur in the short-term as a result of interim market conditions; however, if a range is exceeded, the portfolios must be rebalanced as soon as it is practical to the target allocations.

- Total market value of below-investment-grade credit bonds, as defined by Barclays Capital Global Family of Fixed Income Indices, shall not exceed 5 percent of the total market value of the funds. Although below-investment-grade mortgage-backed, asset-backed, and commercial mortgage-backed securities may not be purchased, portfolio holdings that are downgraded to those levels or are no longer rated may continue to be held.

- Total holdings of below-investment-grade credit bonds, as defined by Barclays Capital Global Family of Fixed Income Indices, should not exceed 5 percent of total fixed income holdings.

3.B. Interest Rate Risk

Interest rate risk is the risk that changes in interest rates over time will adversely affect the fair value of an investment. The risk is managed within the portfolios using effective duration, which is the measure of a debt investment's exposure to fair value changes arising from changes in interest rates. Increases in prevailing interest rates generally translate into decreases in fair values of those investments. The Industrial Insurance Fund does not have a formal policy specifically for interest rate risk.

As of June 30, 2013, the Industrial Insurance Fund's portfolio was within the duration targets below:

- Accident Account – within plus or minus 20 percent of an effective duration target of 7 years

- Medical Aid Account – within plus or minus 20 percent of an effective duration target of 6 years

- Pension Reserve Account – within plus or minus 20 percent of an effective duration target of 7 years

It is the goal of the fixed income portfolios to match the target durations. Although there may be differences from the targets due to market conditions, over any extended period of time, those differences should not be material.

3.C. Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The Industrial Insurance Fund's investment policies limit the fixed income securities to investment-grade or higher at the time of purchase. Investment-grade securities are those fixed income securities with a Moody's rating of Aaa to Baa or a Standard and Poor's rating of AAA to BBB. The rated debt investments of the Industrial Insurance Fund as of June 30, 2013, were rated by Moody's and/or an equivalent national rating organization.

Concentration of Credit Risk - Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The Industrial Insurance Fund's policy states that corporate fixed income issues cost shall not exceed 3 percent of the Fund's fair value at the time of purchase, not shall its fair value exceed 6 percent of the Fund's fair value at any time. There was no concentration of credit risk as of June 30, 2013.

Custodial Credit Risk - Custodial credit risk is the risk that in the event a depository institution or counterparty fails, the Industrial Insurance Fund will not be able to recover the value of its deposits, investments, or collateral securities. As of June 30, 2013, investment securities (excluding cash, cash equivalents and repurchase agreements held as securities lending collateral) are registered and held in the name of the WSIB for the benefit of the Industrial Insurance Fund, and are not exposed to custodial credit risk.

3.D. Foreign Currency Risk

Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment or a deposit. The Industrial Insurance Fund does not have a formal policy to limit foreign currency risk. The Industrial Insurance Fund had $668.2 million and $628.8 million invested in an international commingled equity index fund at June 30, 2013 and 2012, respectively. As such, no currency denomination risk is present at June 30, 2013.

3.E. Derivatives

The Industrial Insurance Fund is authorized to utilize various derivative financial instruments, including collateralized mortgage obligations, financial futures, forward contracts, interest rate and equity swaps, and options to manage its exposure to fluctuations in interest and currency rates while increasing portfolio returns.

Derivative transactions involve, to varying degrees, market and credit risk. The Industrial Insurance Fund mitigates market risks arising from derivative transactions by requiring collateral in cash and investments to be maintained equal to the securities positions outstanding, and thereby prohibiting the use of leverage or speculation. Credit risks arising from derivative transactions are mitigated by selecting and monitoring creditworthy counterparties and collateral issuers.

Domestic and foreign passive equity index fund managers may also utilize various derivative securities to manage exposure to risk and increase portfolio returns. Information on the extent of use and holdings of derivative securities by passive equity index fund managers is unavailable. The only derivative securities held directly by the Industrial Insurance Fund were collateralized mortgage obligations (CMOs) of $1.6 billion and $1.7 billion at June 30, 2013 and 2012, respectively.

3.F. Reverse Repurchase Agreements

State law permits the Industrial Insurance Fund to enter into reverse repurchase agreements; i.e., a sale of securities with a simultaneous agreement to repurchase them in the future at the same price plus a contract rate of interest. The fair value of the securities underlying reverse repurchase agreements normally exceeds the cash received, providing the dealers a margin against a decline in fair value of the securities. If the dealers default on their obligations to resell these securities to the state or provide securities or cash of equal value, the Industrial Insurance Fund would suffer an economic loss equal to the difference between the fair value, plus accrued interest, of the underlying securities and the agreement obligation, including accrued interest.

There were no reverse repurchase agreements during Fiscal Years 2013 and 2012, and there were no liabilities outstanding as of June 30, 2013 and 2012.

3.G. Wash Sales Transactions

In accordance with SSAP No. 103, paragraph 28l, disclosure is required to be made in the annual statement for wash sales transactions involving unrated securities or those with NAIC designations of 3 or below. Wash sales are any transfers when an asset is sold and the proceeds are reinvested within 30 days in the same or substantially the same security. There were no wash sale transactions in the Industrial Insurance Fund during Fiscal Year 2013 or Fiscal Year 2012.

3.H. Bonds

At June 30, 2013 and 2012, bonds were comprised of U.S. Government, other governments, corporate, and mortgage-backed securities with an aggregate book adjusted carrying value (BACV) of $10,610,040,000 and $10,245,715,000 and fair value of $11,329,577,000 and $11,373,029,000, respectively, as shown in the following tables:

Book Adjusted Carrying Values and Fair Values
June 30, 2013
(in thousands)

	Book Adjusted Carrying Value	Fair Value Excess over BACV	BACV Excess over Fair Value	Fair Value
U.S. Government obligations - excluding mortgage-backed securities	$ 2,683,872	$ 146,619	$ (52,751)	$ 2,777,740
All other government obligations	1,145,913	69,507	(17,737)	1,197,683
Mortgage-backed securities	1,770,201	194,039	(4,303)	1,959,937
Industrial and miscellaneous - excluding mortgage-backed securities	5,010,054	443,872	(59,709)	5,394,217
Total	$ 10,610,040	$ 854,037	$ (134,500)	$ 11,329,577

Book Adjusted Carrying Values and Fair Values
June 30, 2012
(in thousands)

	Book Adjusted Carrying Value	Fair Value Excess over BACV	BACV Excess over Fair Value	Fair Value
U.S. Government obligations - excluding mortgage-backed securities	$ 2,361,181	$ 112,116	$ (50,853)	$ 2,422,444
All other government obligations	89,670	12,636	-	102,306
Public utilities - unaffiliated	1,033,583	191,469	-	1,225,052
Mortgage-backed securities	1,891,874	281,977	-	2,173,851
Industrial and miscellaneous - excluding mortgage-backed securities	4,869,407	583,505	(3,536)	5,449,376
Total	$ 10,245,715	$ 1,181,703	$ (54,389)	$ 11,373,029

The following tables present the Industrial Insurance Fund's bond investments by type and by stated contractual maturity in years, and provide the BACV and fair value of bonds as of June 30, 2013 and 2012. Expected maturities may differ from contractual maturities, because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

Schedule of Maturities
June 30, 2013
(in thousands)

			Maturity			
Investment Type	**Fair Value**	**Book Adjusted Carrying Value**	**1 year or less**	**Over 1 year through 5 years**	**Over 5 years through 10 years**	**Over 10 years**
U. S. Government obligations - excluding mortgage-backed securities	$ 2,777,740	$ 2,683,872	$ 189,909	$ 1,168,036	$ 687,472	$ 638,455
All other government obligations	1,197,683	1,145,913	-	554,336	327,551	264,026
Mortgage-backed securities	1,959,937	1,770,201	-	54,195	57,420	1,658,586
Industrial and miscellaneous - excluding mortgage-backed securities	5,394,217	5,010,054	100,984	1,149,250	1,804,885	1,954,935
Total	$ 11,329,577	$ 10,610,040	$ 290,893	$ 2,925,817	$ 2,877,328	$ 4,516,002

Schedule of Maturities
June 30, 2012
(in thousands)

			Maturity			
Investment Type	**Fair Value**	**Book Adjusted Carrying Value**	**1 year or less**	**Over 1 year through 5 years**	**Over 5 years through 10 years**	**Over 10 years**
U. S. Government obligations - excluding mortgage-backed securities	$ 2,422,444	$ 2,361,181	$ 144,920	$ 1,125,271	$ 566,660	$ 524,330
All other government obligations	102,306	89,670	19,988	64,944	-	4,738
Mortgage-backed securities	2,173,851	1,891,874	30,000	99,934	98,517	1,663,423
Industrial and miscellaneous - excluding mortgage-backed securities	6,674,428	5,902,990	524,832	1,311,743	1,907,493	2,158,922
Total	$ 11,373,029	$ 10,245,715	$ 719,740	$ 2,601,892	$ 2,572,670	$ 4,351,413

The following additional tables are included to summarize the different classes of investments held by the Industrial Insurance Fund as they are rated by the National Association of Insurance Commissioners (NAIC). There were not any securities with an NAIC rating higher than four at the fiscal years ended June 30, 2013 and 2012.

Fair Value of Securities by NAIC Designation
June 30, 2013
(in thousands)

	NAIC Designation 1	2	3	4	Total
U.S. Government obligations-excluding mortgage-backed securities	$ 2,777,740	$ -	$ -	$ -	$ 2,777,740
All other government obligations	804,911	316,447	76,325	-	1,197,683
Commercial mortgage-backed securities	388,249	-	-	-	388,249
Residential mortgage-backed securities	1,571,688	-	-	-	1,571,688
Industrial and miscellaneous-excluding mortgage-backed securities	2,222,226	2,972,255	184,899	14,837	5,394,217
Total	$ 7,764,814	$ 3,288,702	$ 261,224	$ 14,837	$ 11,329,577

Fair Value of Securities by NAIC Designation
June 30, 2012
(in thousands)

	NAIC Designation 1	2	3	Total
U.S. Government obligations-excluding mortgage-backed securities	$ 2,422,444	$ -	$ -	$ 2,422,444
All other government obligations	102,306	-	-	102,306
Public utilities (unaffiliated)	644,922	569,193	10,937	1,225,052
Commercial mortgage-backed securities	430,064	-	-	430,064
Residential mortgage-backed securities	1,743,787	-	-	1,743,787
Industrial and miscellaneous-excluding mortgage-backed securities	2,550,437	2,589,175	309,764	5,449,376
Total	$ 7,893,960	$ 3,158,368	$ 320,701	$ 11,373,029

Gross unrealized losses on bonds, the fair value of the related bonds aggregated by investment category, and length of time that individual bonds have been in a continuous unrealized loss position, at June 30, 2013 and 2012, were as follows:

Bonds with Unrealized Losses
June 30, 2013
(in thousands)

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. Government obligations-excluding mortgage-backed securities	$ 825,870	$ (51,437)	$ -	$ -	$ 825,870	$ (51,437)
All other government obligations	334,410	(18,511)	-	-	334,410	(18,511)
Mortgage-backed securities	148,715	(4,303)	-	-	148,715	(4,303)
Industrial and miscellaneous-excluding mortgage-backed securities	1,099,241	(63,079)	10,120	(574)	1,109,361	(63,653)
Total	$ 2,408,236	$ (137,330)	$ 10,120	$ (574)	$ 2,418,356	$ (137,904)

Bonds with Unrealized Losses
June 30, 2012
(in thousands)

	Less than 12 Months		12 Months or Longer		Total	
	Fair Value	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**	**Fair Value**	**Unrealized Losses**
U.S. Government obligations-excluding mortgage-backed securities	$ 173,686	$ (1,119)	$ 463,394	$ (49,734)	$ 637,080	$ (50,853)
All other government obligations	-	-	-	-	-	-
Public utilities (unaffiliated)	-	-	-	-	-	-
Mortgage-backed securities	-	-	-	-	-	-
Industrial and miscellaneous-excluding mortgage-backed securities	139,042	(2,210)	23,070	(1,326)	162,112	(3,536)
Total	$ 312,728	$ (3,329)	$ 486,464	$ (51,060)	$ 799,192	$ (54,389)

In compliance with SSAP No. 26, management has looked at all bonds in an unrealized loss position and used several categories of information to determine whether any impairment is other-than-temporary. The information considered included general market conditions, industry or company financial prospects, an issuer's fundamental credit difficulties, and the length of time and the extent to which the fair value had been below cost. Management has no intention to sell these securities and does not believe these impairments are other-than-temporary.

Similarly, in compliance with SSAP No. 43R, management has looked at mortgage-backed securities with unrealized losses and has used several categories of information to determine whether any impairment is other-than-temporary. State Street Corporation's investment valuation model for prepayment assumptions and determining currently estimated cash flows in valuing mortgage-backed securities was used. The factors that are considered include discounted cash flow on an investment, the length of time and amount of impairment, forecasts, market data, and financial condition of the issuer(s). As of June 30, 2013, no mortgage-backed securities have been determined to be other-than-temporarily impaired.

The following tables summarize realized gains or losses of bonds that were sold during Fiscal Years 2013 and 2012:

Bonds Redeemed or Sold
June 30, 2013
(in thousands)

	Sales Proceeds	Realized Gains	Realized Losses	Net Realized Gains (Losses)
U.S. Government obligations-excluding mortgage-backed securities	$ 577,665	$ 48,344	$ -	$ 48,344
All other government obligations	90,210	-	-	-
Mortgage-backed securities	172,839	-	-	-
Industrial and miscellaneous-excluding mortgage-backed securities	737,021	26,522	(806)	- 25,716
Total	$ 1,577,735	$ 74,866	$ (806)	$ 74,060

Bonds Redeemed or Sold
June 30, 2012
(in thousands)

	Sales Proceeds	Realized Gains	Realized Losses	Net Realized Gains (Losses)
U.S. Government obligations-excluding mortgage-backed securities	$ 542,504	$ 449	$ -	$ 449
All other government obligations	-	2,415	-	2,415
Public utilities (unaffiliated)	19,007	703	(227)	476
Mortgage-backed securities	100,331	-	-	-
Industrial and miscellaneous-excluding mortgage-backed securities	572,857	29,080	(679)	28,401
Total	$ 1,234,699	$ 32,647	$ (906)	$ 31,741

3.I. Fair Value Measurements

The Industrial Insurance Fund has categorized its investments that are reported on the Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve at fair value into a three-level hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The three-level hierarchy is based on the degree of subjectivity inherent in the valuation method by which fair value was determined. The three levels are defined as follows:

- Level 1 - Quoted prices in active markets for identical assets or liabilities.
- Level 2 - Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that can be corroborated by observable market data for substantially the full term of the assets or liabilities.

- Level 3 - Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The asset's or liability's fair value measurement level within the hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs.

Following is a description of the valuation methodologies used for assets measured at fair value:

- Industrial & miscellaneous bonds - value is based on market values approved by the NAIC.

- Equities – value is based on the underlying equity.

- Other invested assets – value is based on the underlying equity.

The preceding methods described may produce a fair value calculation that may not be indicative of net realizable value or reflective of the future fair values. The Industrial Insurance Fund has determined that its valuation methods are appropriate and consistent with other market participants; however, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date.

The following tables present the financial instruments related to the Fund's assets carried at fair value as of June 30, 2013 and 2012, by the SSAP 100 valuation hierarchy.

Investment Assets Carried at Fair Value
June 30, 2013
(in thousands)

	Level 1	Level 2	Level 3	Total
Industrial and miscellaneous bonds	$ -	$ 61,398	$ -	$ 61,398
Equities	-	1,730,470	-	1,730,470
Total Assets at Fair Value	$ -	$ 1,791,868	$ -	$ 1,791,868

Investment Assets Carried at Fair Value
June 30, 2012
(in thousands)

	Level 1	Level 2	Level 3	Total
Industrial and miscellaneous bonds	$ -	$ 178,945	$ -	$ 178,945
Equities	-	1,580,216	-	1,580,216
Total Assets at Fair Value	$ -	$ 1,759,161	$ -	$ 1,759,161

Only bonds with an NAIC rating of 3-6 and a fair value lower than the book adjusted value are carried at fair value on the financial statements. On June 30, 2013, there were seven bonds in this category, with fair values totaling $61,398,000. On June 30, 2012, there were eleven bonds in this category, with fair values totaling $178,945,000.

At the end of each reporting period, the Industrial Insurance Fund evaluates whether or not any event as occurred or circumstances have changed that would cause an instrument to be transferred between Levels 1 and 2. This policy also applies to transfers into or out of Level 3. During the current year, no transfers into or out of Levels 1, 2 or 3 were required.

The fair value of bonds categorized as Level 2 were valued using a market approach. These valuations were determined to be Level 2 valuations, as quoted markets prices for similar instruments in an active market were utilized. This was accomplished by the use of matrix pricing. Matrix pricing takes quoted prices of bonds with similar features and applies analytic methods to determine the fair value of bonds held.

The following tables reflect the fair values and admitted values of all admitted assets and liabilities. The fair values are also categorized into the three-level fair value hierarchy as described above.

Investment Assets at Fair Value
June 30, 2013
(in thousands)

	Fair Value	Admitted Value	Level 1	Level 2	Level 3	Total
Bonds	$ 11,329,577	$ 10,610,040	$ -	$ 11,329,577	$ -	$ 11,329,577
Equities	1,730,470	1,730,470	-	1,730,470	-	1,730,470
Other invested assets	208,773	208,683	-	208,773	-	208,773
Total Assets at Fair Value	$ 13,268,820	$ 12,549,193	$ -	$ 13,268,820	$ -	$ 13,268,820

Investment Assets at Fair Value
June 30, 2012
(in thousands)

	Fair Value	Admitted Value	Level 1	Level 2	Level 3	Total
Bonds	$ 11,373,029	$ 10,245,715	$ -	$ 11,373,029	$ -	$ 11,373,029
Equities	1,580,216	1,580,216	-	1,580,216	-	1,580,216
Other invested assets	82,211	82,211	-	82,211	-	82,211
Total Assets at Fair Value	$ 13,035,456	$ 11,908,142	$ -	$ 13,035,456	$ -	$ 13,035,456

Note 4 - Real Estate and Improvements

At June 30, 2013 and 2012, the Accident and Medical Aid Accounts admitted only land, buildings, and improvements, net of accumulated depreciation and encumbrances.

SSAP No. 40 requires that buildings more than 50 percent occupied by the reporting entity be categorized as a real estate investment and that depreciation and interest expenses be classified as investment expenses. The building occupied by the Industrial Insurance Fund's employees is financed through general obligation bonds of the state of Washington. The remaining balance due on the bonds as of June 30, 2013, was $11.5 million. Due to indirect ownership by the state of Washington, the land, building, and improvements are not shown as a real estate investment of the Industrial Insurance Fund. The related depreciation and interest expenses are allocated between administrative and non-insurance expenses based on percentage of use by employees.

Real Estate and Improvements
(in thousands)

	June 30, 2013	June 30, 2012
Land	$ 3,204	$ 3,204
Building occupied by Industrial Insurance Fund	65,134	65,134
Improvements, other than buildings	1,020	1,020
Encumbrances	(11,475)	(14,875)
Accumulated depreciation - building	(27,641)	(26,288)
Accumulated depreciation - improvements	(418)	(397)
Total	$ 29,824	$ 27,798

Note 5 - Investment Income

The Industrial Insurance Fund does not admit investment income due and accrued if amounts are over 90 days past due. As of June 30, 2013 and 2012, all investment income due and accrued was admitted, with balances accrued by security type, as summarized in the following table.

Admitted Interest Income Due and Accrued
(in thousands)

	June 30, 2013	June 30, 2012
U.S. government obligations, excluding mortgage-backed securities	$ 13,067	$ 13,831
All other government obligations	14,139	486
Public utilities (unaffiliated)	-	16,209
Mortgage-backed securities	7,851	8,563
Industrial and miscellaneous, excluding mortgage-backed securities	71,950	70,500
Other interest	74	28
Total	$ 107,081	$ 109,617

The following table provides details for net investment income by security type for the fiscal years ended June 30, 2013 and 2012.

Net Investment Income Earned (in thousands)	Fiscal Year 2013	Fiscal Year 2012
U.S. government obligations, excluding mortgage-backed securities	$ 32,124	$ 33,005
All other government obligations	41,697	4,354
Public utilities (unaffiliated)	-	58,690
Mortgage-backed securities	98,465	103,300
Industrial and miscellaneous, excluding mortgage-backed securities	290,847	273,400
Total Bond Interest	463,133	472,749
Equities dividends	926	6,843
Net securities lending income	910	5,120
Other interest and litigation income	577	907
Amortization	4,145	139
Gross investment income	469,691	485,758
Investment expenses	(3,823)	(3,866)
Total Net Investment Income Earned	$ 465,868	$ 481,892

Note 6 - Retirement Plans, Compensated Absences, Deferred Compensation Plan, and Other Postemployment Benefits

6.A. Retirement Plans

Industrial Insurance Fund employees participate in the Washington State Public Employees' Retirement System (PERS), administered by the Department of Retirement Systems. The PERS is a multiemployer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans, and Plan 3 is a combination defined benefit/defined contribution plan. PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977, and by February 28, 2002, are Plan 2 members, unless they exercised an option to transfer their membership to Plan 3. PERS participants joining the system on or after March 1, 2002, have the irrevocable option of choosing membership in either Plan 2 or Plan 3.

Under the PERS, the employee and employer contribute a percentage of the employee's compensation. The employer contribution rates for the Workers' Compensation Program at June 30, 2013 and 2012 for each of Plans 1, 2, and 3 were 7.21 and 7.08 percent of the employee's annual covered salary, respectively. The Industrial Insurance Fund contributed $10,147,452 and $9,858,778 to the PERS during the fiscal years ended June 30, 2013 and 2012, respectively.

An actuarial valuation of the PERS plan for the Industrial Insurance Fund as a stand-alone entity is not available. Pension note disclosures for the PERS are included in the Comprehensive

Annual Financial Report for the state of Washington. A copy of this report may be obtained by contacting the Accounting Division of the Office of Financial Management at P.O. Box 43113, Olympia, Washington 98504-3113 or online at http://www.ofm.wa.gov/cafr.

6.B. Compensated Absences

Industrial Insurance Fund employees accrue vested annual leave at a variable rate based on years of service. In general, accrued annual leave cannot exceed 240 hours at the employee's anniversary date.

Employees accrue sick leave at the rate of one day per month without limitation on the amount that can be accumulated. Sick leave is not vested; i.e., the Industrial Insurance Fund does not pay employees for unused sick leave upon termination except upon employee death or retirement, when the Industrial Insurance Fund is liable for 25 percent of the employee's accumulated sick leave. In addition, the Industrial Insurance Fund has a "sick leave buyout option" in which, each January, employees who have accumulated sick leave in excess of 480 hours may redeem sick leave earned but not taken during the previous year at the rate of one day's pay in exchange for each four days of sick leave.

It is the Industrial Insurance Fund's policy to liquidate unpaid compensated absence balances outstanding at June 30 with future resources, rather than advance funding it with currently available expendable financial resources.

The Industrial Insurance Fund recognizes the expense and accrues a liability for annual leave and estimated sick leave buyout, including related payroll taxes and benefits as applicable, as the leave is earned. The annual leave and sick leave accrued liability was $14,661,965 and $13,527,582 at June 30, 2013 and 2012, respectively.

6.C. Deferred Compensation Plan

Industrial Insurance Fund employees have the option to participate in the state of Washington's Deferred Compensation Plan (DCP). There are no contributions made on behalf of employees to the Deferred Compensation Plan by the Industrial Insurance Fund. The Department of Retirement Systems administers the DCP and contracts with a third party (currently Great-West Retirement Services) for recordkeeping and other administrative services. The Washington State Investment Board selects and monitors DCP's investment options based on advice and recommendations provided by the Employee Retirement Benefits Board.

6.D. Other Postemployment Benefits

The Industrial Insurance Fund participates fully in the Other Postemployment Benefit (OPEB) plan administered by the Washington State Health Care Authority (HCA) under the auspices of the Public Employees Benefits Board (PEBB).

The following table shows components of the Industrial Insurance Fund's OPEB costs for Fiscal Year 2013 and 2012, the amount actually contributed to the plan, and changes in the Industrial Insurance Fund's Net OPEB Obligation (NOO):

Net OPEB Obligation (NOO)				
		Fiscal Year 2013		Restated Fiscal Year 2012
NOO, July 1[1]	$	19,237,000	$	13,562,000
Annual OPEB costs		8,451,000		7,796,000
Contributions made		(1,925,000)		(2,121,000)
NOO, June 30	$	25,763,000	$	19,237,000

[1]The NOO Balance of $23,331,132 at July 1, 2011, as previously reported, was reduced by a prior period adjustment of $9,769,132, and was restated to $13,562,000. See Note 2 – Accounting and Reporting Changes for the explanation of the prior period adjustment.

The above information was provided by the Washington State Office of Financial Management. The Industrial Insurance Fund's OPEB plan represents 1.60 percent and 1.50 percent of the state of Washington's OPEB plan as of June 30, 2013 and 2012, respectively.

The information below fully discloses the state of Washington's information with regard to funding policy, annual OPEB costs and contributions made, the funded status and funding progress of the employer individual plan, as well as actuarial methods and assumptions used. As the Industrial Insurance Fund participates in this multiemployer plan, as defined by SSAP No. 92, no stand-alone information for the Industrial Insurance Fund is available. The state of Washington's OPEB plan does not issue a financial report.

Plan Description and Funding Policy

The state of Washington, through the HCA, administers a multiemployer OPEB plan per RCW 41.05.065. The HCA is authorized to design benefits and determine the terms and conditions of employee and retired employee participation and coverage, including establishment of eligibility criteria for both active and retired employees. PEBB programs include medical, dental, life, and long-term disability insurance.

Employers participating in the PEBB plan include the state (which includes general government agencies and higher education institutions), 54 of the state's K-12 schools and educational service districts (ESDs) and 207 political subdivisions and tribal governments. Additionally, the PEBB plan is available to the retirees of the remaining 243 K-12 schools and ESDs.

As of June 30, 2013 and 2012, membership in the PEBB plan consisted of the following:

PEBB Plan Membership by Fiscal Year

	Active Employees		Retirees[1]		Total	
	2013	2012	2013	2012	2013	2012
State	107,003	106,255	28,633	27,807	135,636	134,062
K-12 schools and ESDs[2]	1,838	1,800	30,354	29,245	32,192	31,045
Political subdivisions	11,840	11,375	1,392	1,261	13,232	12,636
Total	120,681	119,430	60,379	58,313	181,060	177,743

[1]Retirees include retired employees, surviving spouses, and terminated members entitled to a benefit.
[2]In Fiscal Year 2013, there were 101,189 full-time equivalent active employees in the 243 K-12 schools and ESDs that elected to limit participation in PEBB only to their retirees. In Fiscal Year 2012, there were 98,349 full-time equivalent active employees in the 246 K-12 schools and ESDs that elected to limit participation in PEBB only to their retirees.

For Fiscal Years 2013 and 2012, the estimated monthly cost for PEBB benefits for active employees (averaged across all plans and tiers) was as follows:

Estimated Montly Cost of PEBB Benefits by Fiscal Year

	2013	2012
Required Premium[1]		
Medical	$ 913	$ 880
Dental	82	83
Life	4	5
Long-term disability	2	2
Total	$ 1,001	$ 970
Employer contribution	$ 865	$ 852
Employee contribution	136	118
Total	$ 1,001	$ 970

[1] Per Index Rate Model 7.2 for Fiscal Year 2013 and 3.60 for Fiscal Year 2012

The relationship between the PEBB OPEB plan and its member employers and their employees and retirees is not formalized in a contract or plan document. Rather, the benefits are provided in accordance with a substantive plan. A substantive plan is one in which the plan terms are understood by the employers and plan members. This understanding is based on communications between the HCA, employers and plan members, and the historical pattern of practice with regard to the sharing of benefit costs.

The PEBB retiree OPEB plan is available to employees who elect to continue coverage and pay the administratively established premiums at the time they retire under the provisions of the retirement system to which they belong. Retirees' access to PEBB plans depends on the retirement eligibility of their respective retirement system. PEBB members are covered in the following retirement systems: Public Employees' Retirement System, Public Safety Employees' Retirement System, Teachers' Retirement System, School Employees' Retirement System, Washington State Patrol Retirement System, and Higher Education.

Per RCW 41.05.022, retirees who are not yet eligible for Medicare benefits may continue participation in the state's non-Medicare community-rated health insurance risk pool on a self-pay basis. Retirees in the non-Medicare risk pool receive an implicit subsidy. The implicit subsidy exists because retired members pay a premium based on a claims experience for active employees and other non-Medicare retirees. The subsidy is valued using the difference between the age-based claim costs and the premium. In Calendar Year 2012, the average weighted implicit subsidy was valued at $330 per month per member, and in Calendar Year 2013, the average weighted implicit subsidy is projected to be $294 per month per member.

Retirees who are enrolled in both Parts A and B of Medicare may participate in the state's Medicare community-rated health insurance risk pool. Medicare retirees receive an explicit subsidy in the form of reduced premiums. Annually, the HCA administrator recommends an amount for the next calendar year's explicit subsidy for inclusion in the Governor's budget. In Calendar Year 2012, the explicit subsidy was $150 per month per member, and it remained $150 per month per member in Calendar Year 2013.

Administrative costs, as well as implicit and explicit subsidies, are funded by required contributions from participating employers. The subsidies provide monetary assistance for medical and life insurance benefits.

Contributions are set each biennium as part of the budget process. In Fiscal Years 2013 and 2012, the costs of the subsidies were approximately 6.0 percent and 6.5 percent of the cost of benefits for active employees, respectively. The benefits are funded on a pay-as-you-go basis.

The PEBB OPEB plan is accounted for as an agency fund on an accrual basis. The plan has no investments or other assets. The PEBB OPEB plan does not issue a publicly available financial report.

For information on the results of an actuarial valuation of the employer-provided subsidies associated with the PEBB plan, refer to:
http://osa.leg.wa.gov/Actuarial_services/OPEB/OPEB.htm.

Annual OPEB Cost and Net OPEB Obligation

The state's (general government agencies and higher education institutions) annual OPEB cost (expense) is calculated based on the annual required contribution (ARC) of the state as the employer, an amount actuarially determined.

The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover the normal costs each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed 30 years.

The following table shows the components of the state's annual OPEB cost for Fiscal Year 2013 and 2012, the amount actually contributed to the plan, and changes in the state's Net OPEB Obligation (NOO):

OPEB Cost Components
(in thousands)

	Fiscal Year 2013	Fiscal Year 2012
Annual required contribution	$ 342,283	$ 320,991
Interest on NOO	53,434	46,250
Amortization of NOO	(48,684)	(36,954)
Annual OPEB cost	347,033	330,287
2012 Adjustment[1]	56,476	-
Contributions made	(69,115)	(78,673)
Increase in NOO	334,394	251,614
NOO, July 1	1,279,381	1,027,767
NOO, June 30	$ 1,613,775	$ 1,279,381

[1]An actuarial valuation of the OPEB plan was not prepared in Fiscal Year 2012. The Fiscal Year 2012 estimated contributions and OPEB cost were refined during the actuarial valuation prepared as of January 1, 2013. These revised estimates resulted in an increase in the Net OPEB Obligation reported as of June 30, 2012.

The state's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation was as follows:

OPEB History
(in thousands)

Fiscal Year Ended June 30,	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
2013	$ 347,033	19.9%	$ 1,613,775
2012	$ 330,287	23.8%	$ 1,279,381
2011	$ 328,568	23.9%	$ 1,027,767

Funded Status and Funding Progress

Actuarial valuations are performed on a two-year basis. The funded status of the plan as of June 30, 2013 and 2011 are based on the latest actuarial valuation dates available, January 1, 2013 and 2011, respectively, was as follows:

OPEB Funded Status
(in thousands)

	June 30, 2013	June 30, 2011
Actuarial accrued liability (AAL)	$ 3,706,856	$ 3,491,970
Actuarial value of plan assets	-	-
Unfunded actuarial accrued liability (UAAL)	$ 3,706,856	$ 3,491,970
Funded ratio (actuarial value of plan assets/AAL)	0.00%	0.00%
Covered payroll (active plan members)	$ 5,786,960	$ 5,937,061
UAAL as a percentage of covered payroll	64.06%	58.82%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trends. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress, following the notes to the consolidated statutory financial statements, presents multiyear trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the terms of the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

Significant methods and assumptions were as follows:

Significant Methods and Assumptions		
	June 30, 2013	**June 30, 2011**
Actuarial valuation date	January 1, 2013	January 1, 2011
Actuarial cost method	Projected Unit Credit (PUC)	Projected Unit Credit (PUC)
Amortization method	Closed, level percentage of projected payroll amortization method	Closed, level percentage of projected payroll amortization method
Remaining amortization period	30 years	30 years
Asset valuation method	N/A - No Assets	N/A - No Assets
Actuarial assumptions:		
Investment rate of return	4.0%	4.5%
Projected salary increases	3.75%	4.0%
Health-care inflation rate	8.0% initial rate, 5% ultimate rate in 2093	7.0% initial rate, 5% ultimate rate in 2083
Inflation rate	3.0%	3.5%

Note 7 - Commitments and Contingencies

7.A. Commitments

Effective July 1, 1992, the Washington State Legislature required the Industrial Insurance Fund, under RCW 48.22.070, to participate in an assigned risk pool providing workers' compensation coverage under the United States Longshoreman and Harbor Workers' Act. The Industrial Insurance Fund is obligated to participate 50 percent in the underwriting losses or surpluses of the assigned risk pool. This participation is scheduled to continue indefinitely due to amending legislation passed in 1997. However, the Industrial Insurance Fund has not made any payments to this risk pool since enactment of this indefinite commitment.

7.B. Contingencies

The Industrial Insurance Fund is party to numerous routine legal proceedings that normally occur in operations. At any given point, there may be numerous lawsuits that could financially impact the Fund. Although the outcome of these lawsuits is not currently determinable, the resolution of these matters, is not likely to have a material impact on the Industrial Insurance Fund's financial position, revenues or expenses.

7.C. Exposure

The lack of diversity of exposure by line of business and by state could be a risk factor for benefit liability and claims administration expense (CAE) reserves. By statute, the Fund's direct exposure is limited to one line of business (workers' compensation) in one state (Washington). Therefore, any adverse trends affecting this line of business and/or state could have a material effect on the Fund's benefit liability and CAE reserves. Such trends would include legislative benefit level changes that may have an effect on all open workers' compensation claims.

Note 8 - Leases

The Industrial Insurance Fund leases land, office facilities, office and computer equipment, and other assets under a variety of operating lease agreements. Although lease terms vary, most leases are subject to appropriation from the State Legislature to continue the obligation. Since the possibility of not receiving funding from the Legislature is remote, leases are considered non-cancelable for financial reporting purposes. Certain operating leases are renewable for specified periods. Management expects the leases to be renewed or replaced by other leases.

The total operating lease rental expenses for Fiscal Years 2013 and 2012 were $10,467,386 and $10,075,203, respectively. There are no contingent rental payments or unusual renewal options, escalation clauses or restrictions, and there have been no early terminations of existing leases. Certain rental commitments have renewal options extending through the year 2018. Some of these renewals are subject to adjustments in future periods.

The following table presents future minimum payments for operating leases as of June 30, 2013:

Future Minimum Payments
June 30, 2013

Operating Leases (by Fiscal Year)	Accident Account	Medical Aid Account	Total
2014	$ 3,787,526	$ 3,638,765	$ 7,426,291
2015	3,456,018	3,324,764	6,780,782
2016	2,920,018	2,811,273	5,731,291
2017	2,243,742	2,149,609	4,393,351
2018	534,082	510,242	1,044,324
Total Future Minimum Lease Payments	$ 12,941,386	$ 12,434,653	$ 25,376,039

Note 9 - Sale, Transfer and Servicing of Financial Assets and Extinguishments of Liabilities

Securities Lending

The Industrial Insurance Fund participates in securities lending programs with the Washington State Investment Board (WSIB) and the Office of the State Treasurer (OST) to increase investment income. At June 30, 2013, the Industrial Insurance Fund had $26,381,220 of cash collateral received through the WSIB in the Accident and the Pension Reserve Accounts. There was $1,088,426 of cash collateral received in the Medical Aid Account invested through the OST.

Securities Lending - WSIB

Washington State law and WSIB policy permit the Industrial Insurance Fund to participate in securities lending programs to augment investment income. The WSIB has entered into an agreement with State Street Corporation to act as agent for the WSIB in securities lending transactions. As State Street Corporation is the custodian bank for the WSIB, it is counterparty to securities lending transactions.

Fixed income securities were loaned and collateralized by the Industrial Insurance Fund's agent with cash, U.S. Government or U.S. Agency Securities (exclusive of mortgage-backed securities and letters of credit). When the loaned securities had collateral denominated in the same currency, the collateral requirement was 102 percent of the fair value, including accrued interest of the securities loaned. All other securities were required to be collateralized at 105 percent of the fair value, including accrued interest of the loaned securities.

During Fiscal Years 2013 and 2012, securities lending transactions could be terminated on demand by either the Industrial Insurance Fund or the borrower. The weighted average maturity of loans for Fiscal Year 2012 was 1.5 days. As of June 30, 2013, the collateral held had an average duration of 22.42 days and an average weighted maturity of 57.44 days. Because the securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash collateral. No more than 20 percent of the total on loan value can be held by a specific borrower. Collateral investment guidelines specifically prohibit European domiciled holdings. There are no restrictions on the amount of securities that can be lent.

Since the securities lending agreements were terminable at will, the maturity dates of the liabilities for collateral to be returned did not generally match the investments made with the cash collateral. To provide liquidity to manage those mismatches, State Street Corporation is required to re-invest no less than the targeted 20 percent of the cash collateral received in the overnight maturities to ensure sufficient liquidity available for the return of collateral to borrowers within the ordinary course of business. In the event that loans are returned beyond what is expected in the ordinary course of business, State Street Corporation would be allowed to sell investments at its discretion and in accordance with the investment guidelines of the cash collateral account.

Securities were lent with the agreement that they would be returned in the future for exchange of the collateral. State Street Corporation indemnified the Industrial Insurance Fund by agreeing to purchase replacement securities or return the cash collateral in the event a borrower failed to return the loaned securities or pay distributions thereon. State Street Corporation's responsibilities included performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable federal regulations concerning securities lending.

During Fiscal Years 2013 and 2012, there were no significant violations of legal or contractual provisions, no failures by any borrowers to return loaned securities or to pay distributions thereon. Further, the Industrial Insurance Fund incurred no losses during Fiscal Years 2013 or 2012 resulting from a default by either the borrowers or the securities lending agents.

WSIB changed the custodian bank from JPMorgan to State Street, effective July 1, 2012, and all the securities on loan were recalled so they could be transferred. As a result, there were no collateral held or securities on loan at June 30, 2012. WSIB and State Street resumed securities lending activities in Fiscal Year 2013. At June 30, 2013, total collateral held and fair value of securities on loan were $26,381,220 and $26,200,506, respectively.

The market value of cash collateral assets at June 30, 2013, was $26,381,220, and the following table provides information regarding cash collateral assets:

Cash Collateral Held Under Securities Lending
June 30, 2013
(in thousands)

	NAIC Rating	Book Adjusted Carrying Value	Level 2 Fair Value	Maturity Date: Under 30 days	30 - 59 days	60 - 89 days	90 - 119 days	120 - 179 days	180 days - less than 1 year	1 year - 2 years
Cash and cash equivalents	1	$ 6,062	$ 6,063	$ 1,274	$ 880	$ 1,529	$ 304	$ 729	$ 1,145	$ 202
Commercial paper	1	4,791	4,792	304	1,214	1,300	607	810	557	-
Repurchase agreements	2	2,206	2,206	2,206	-	-	-	-	-	-
Repurchase agreements	Not rated	12,570	12,570	12,570	-	-	-	-	-	-
Bank and promissory notes	1	749	750	-	-	345	-	-	-	405
Total Collateral Held		$ 26,378	$ 26,381	$ 16,354	$ 2,094	$ 3,174	$ 911	$ 1,539	$ 1,702	$ 607

Non-cash collateral cannot be pledged or sold absent borrower default. There was no non-cash collateral held under securities lending at June 30, 2013 or 2012. Net earnings received through the securities lending program were $910,453 for Fiscal Year 2013 and $5,119,692 for Fiscal Year 2012.

Securities Lending – OST

State statutes permit the OST's to lend its securities to broker-dealers and other entities with a simultaneous agreement to return the collateral for the same securities in the future. The OST, which has contracted with Citibank as a lending agent to lend securities, receives earnings for this activity.

The OST lending agent lends U.S. government and U.S. agency securities and receives collateral, which can be in the form of cash or other securities. The collateral, which must be valued at 102 percent of the fair value of the loaned securities, is priced daily and, if necessary, action is taken to maintain the collateralization level at 102 percent.

The cash is invested by the lending agent in accordance with investment guidelines approved by the OST. The securities held as collateral and the securities underlying the cash collateral are held by the custodian. One option available to the lending agent is to invest cash collateral into an OST account in the Local Government Investment Pool (LGIP). The LGIP portfolio is invested in a manner generally consistent with a Rule 2a-7 money market fund recognized by the Securities and Exchange Commission (17CFR.270.2a-7). Rule 2a-7 funds are limited to high-quality obligations with limited maximum and average maturities, the effect of which is to minimize both market and credit risk. At June 30, 2013, the Industrial Insurance Fund's cash collateral totaled $1,088,426, all of which was invested in the LGIP. At June 30, 2012, there was no cash collateral held.

The contract with the lending agent requires them to indemnify the OST if the borrowers fail to return the securities (and if the collateral is inadequate to replace the securities lent) or if the borrower fails to pay the OST for income distribution by the securities' issuers while the securities are on loan. The OST cannot pledge or sell collateral securities received unless the borrower defaults. At June 30, 2013, the fair value of securities on loan for the Industrial Insurance Fund totaled $1,065,797. At June 30, 2012, there were no securities on loan.

The OST's investment policy requires that any securities on loan be made available by the lending agent for next day liquidity at the option of the OST. During Fiscal Year 2013, the OST had no credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed the OST.

There were no violations of legal or contractual provisions or any losses resulting from a default of a borrower or lending agent during the fiscal year.

Note 10 - Changes in Benefit and Claims Administration Liabilities

An increase of $677.9 million in the provision for insured events of prior years in benefit and claims administration liabilities in Fiscal Year 2013 is comprised of $362.6 million of discount accretion, $67.8 million of change in the non-tabular discount rate, and $247.5 million of adverse development on prior years. The non-tabular discount rate was changed in Fiscal Year 2013 from 2.0 percent to 1.5 percent. For more information on discounting, see Note 1.C.3. New liabilities for the current year increased $106.4 million from the prior year because of an increase in claim severity and exposure, partially offset by a decrease in claim frequency. The exposure growth was due to an increase in reported hours and employment growth in businesses in higher-risk classes.

The following schedule presents the changes in benefit and claims administration liabilities for the fiscal years ended June 30, 2013 and 2012, for the Industrial Insurance Fund:

Changes in Benefit and Claims Administration Liabilities
(in thousands)

	Fiscal Year 2013	Fiscal Year 2012
Unpaid benefit and claims administration liabilities, July 1	$ 11,738,930	$ 11,288,310
Incurred benefit and claims administration liabilities:		
Provision for insured events of the current year	1,631,274	1,524,878
Increase in provision for insured events of prior years	677,906	614,321
Total incurred benefit and claims administration liabilities	2,309,180	2,139,199
Payments:		
Benefit and claims administration liabilities attributable to:		
Insured events of the current year	296,347	283,763
Insured events of prior years	1,416,526	1,404,816
Total payments	1,712,873	1,688,579
Total unpaid benefit and claims administration liabilities, June 30	$ 12,335,237	$ 11,738,930
Current portion	$ 1,411,259	$ 1,330,942
Long-term portion	$ 10,923,978	$ 10,407,988

At June 30, 2013 and 2012, $20.0 billion and $20.1 billion of unpaid benefit and claims administration liabilities are shown at their net present and settlement value of $12.3 billion and $11.7 billion, respectively. In the Accident Account, the incurred but not-yet-awarded pensions are discounted from the anticipated payment dates back to the anticipated time of award at a rate of 6.5 percent, and from the anticipated time of award to the present at 1.5 percent. All other Accident and Medical Aid Account benefits and claims administration liabilities are discounted at 1.5 percent. The benefit liabilities in the Pension Reserve Account are discounted at 6.5 percent.

2013 Benefit Liability Development by Program
(in thousands)

Program/ Category	Undiscounted Liabilities	Discount Rate	Benefit Liabilities
Accident	$ 7,133,436	1.5% & 6.5%	$ 4,291,331
Medical Aid	4,990,475	1.5%	3,775,655
Pensions	7,318,128	6.5%	3,739,086
Total Benefit Liability	19,442,039		11,806,072
Claim Administration Expense (CAE)	581,726	1.5%	529,165
Total Benefit and CAE Liabilities	$ 20,023,765		$ 12,335,237

2012 Benefit Liability Development by Program (in thousands)					
Program/ Category		**Undiscounted Liabilities**	**Discount Rate**		**Benefit Liabilities**
Accident	$	7,637,283	2.0% & 6.5%	$	4,245,695
Medical Aid		4,955,417	2.0%		3,458,833
Pensions		6,879,102	6.5%		3,498,427
Total Benefit Liability		19,471,802			11,202,955
Claim Administration Expense (CAE)		611,844	2.0%		535,975
Total Benefit and CAE Liabilities	$	20,083,646		$	11,738,930

Note 11 - Retrospectively-Rated Contracts and Contracts Subject to Redetermination

11.A. Method Used to Estimate

The Industrial Insurance Fund estimates accrued retrospective premium annual adjustments for unadjusted enrollment periods by reviewing historical participation and return patterns. The historical averages are used to arrive at an estimate of net retrospective return premiums for unadjusted periods. Cumulative return premiums for periods from first annual adjustment through third annual adjustment are system-generated, and the accruals are the difference between the cumulative returns and the amount already returned. The third annual retrospective adjustment is final.

11.B. Method Used to Record

Retrospective return premiums due to employers are netted with additional premiums due from employers and recorded as a liability.

11.C. Amount and Percent of Net Retrospective Premiums

Net premiums for the fiscal years ended June 30, 2013 and 2012, on retrospectively-rated workers' compensation policies were $713.9 million, or 42 percent, and $690.1 million, or 42 percent, of total workers' compensation net premiums, respectively.

11.D. Calculation of Nonadmitted Retrospective Premiums

Retrospective additional premiums 90 days past due after the third annual retrospective adjustment are nonadmitted.

Note 12 - Discounting of Liabilities for Unpaid Benefits or Unpaid Claims Administration Expenses

The case reserves shown in this exhibit are the reserves for pensions awarded through June 30, 2013, only. The State Fund estimates case reserves on certain other individual claims solely for the purpose of classification rating, retrospective rating, and experience rating. Such case reserves are not maintained on claims that do not enter the rating calculations, so they are not meaningful for claims less than approximately 18 months old or more than approximately seven years old.

12.A. Tabular Discounts

The mortality table is based upon 1980 census data. The liabilities are discounted at 6.5 percent per annum. The June 30, 2013, liabilities include $6,270,858,000 of such reserves, net of tabular discounts. The amount of the tabular discount for case reserves is $3,579,042,000 and $2,590,374,000 for Incurred But Not Reported (IBNR) reserves at June 30, 2013.

At June 30, 2012, the liabilities, net of tabular discounts, amounted to $6,099,659,000. The amount of the tabular discount for case reserves was $3,380,675,000 and $3,050,538,000 for IBNR reserves.

Liabilities Discounted on a Tabular Basis
June 30, 2013
(in thousands)

Fiscal Accident Year	Benefit Liabilities Gross of Tabular Discount	Tabular Discounts		Benefit Liabilities Net of Tabular Discount
		Case	IBNR	
2003 & Prior	$ 5,686,198	$ 2,374,643	$ 351,385	$ 2,960,170
2004	601,164	210,620	95,995	294,549
2005	632,979	204,084	121,959	306,936
2006	692,519	201,845	154,223	336,451
2007	781,524	192,711	207,988	380,825
2008	839,248	155,913	271,399	411,936
2009	779,174	108,480	284,103	386,591
2010	665,882	72,429	264,077	329,376
2011	604,846	35,014	268,133	301,699
2012	572,683	14,773	275,834	282,076
2013	584,057	8,530	295,278	280,249
Total	$ 12,440,274	$ 3,579,042	$ 2,590,374	$ 6,270,858

12.B. Non-Tabular Discounts

The non-tabular discount rate is based upon the 5-year average of the 20-year treasury yield rounded to the nearest one-half percent, less 2 percentage points. As of June 30, 2013, the rounded 5-year average was 3.5 percent, and the indicated non-tabular discount rate was 1.5 percent. The non-tabular discount is calculated using the selected non-tabular discount rate and the anticipated payout of the liabilities. This discount rate was changed in Fiscal Year 2013 from 2.0 percent to 1.5 percent.

Excluding liabilities related to fiscal accident year 2013, the June 30, 2013, liabilities include $7,267,856,000 of discounted loss and loss adjustment expense liabilities discounted on a non-tabular basis at 1.5 percent. These discounted loss and loss adjustment expense liabilities would total $7,200,034,000 at the previous non-tabular discount rate of 2.0 percent. The reduction in the non-tabular discount rate increased the discounted liabilities at June 30, 2013, by $83,393,000.

The June 30, 2013, liabilities included $8,066,986,000 of reserves for benefits and $529,165,000 of reserves for claims administration expenses, net of tabular and non-tabular discounts. The amount of the non-tabular discounts for IBNR reserves was $1,466,550,000; the reserve for defense and cost-containment expense was $35,193,000; and the reserve for adjusting and other expense was $17,368,000.

At June 30, 2012, liabilities included $7,704,528,000 of reserves for benefits and $535,975,000 of reserves for claims administration expenses, net of tabular and non-tabular discounts. The amount of the non-tabular discounts for IBNR reserves was $1,837,634,000; the reserve for defense and cost-containment expense was $46,515,000; and the reserve for adjusting and other expense was $29,354,000.

Liabilities Discounted on a Non-Tabular Basis
June 30, 2013
(in thousands)

Fiscal Accident Year	Benefit & CAE Liabilities Net of Tabular and Gross of Non-Tabular Discount	Non-Tabular Discounts: Case	Non-Tabular Discounts: IBNR	Non-Tabular Discounts: DCC	Non-Tabular Discounts: AO	Benefit & CAE Liabilities Net of Tabular and Non-Tabular Discount
2003 & Prior	$ 2,282,609	$ -	$ 465,430	$ 9,865	$ 1,386	$ 1,805,928
2004	310,910	-	51,759	1,155	448	257,548
2005	398,919	-	65,049	1,460	607	331,803
2006	482,629	-	73,814	1,691	821	406,303
2007	594,828	-	83,013	1,950	1,153	508,712
2008	749,576	-	97,420	2,345	1,584	648,227
2009	812,994	-	103,120	2,488	1,765	705,621
2010	851,885	-	107,658	2,663	1,839	739,725
2011	988,139	-	121,703	3,106	2,158	861,172
2012	1,144,877	-	135,913	3,651	2,496	1,002,817
2013	1,497,896	-	161,671	4,819	3,111	1,328,295
Total	$ 10,115,262	$ -	$1,466,550	$ 35,193	$ 17,368	$ 8,596,151

Note 13 - Related Party Transactions

The Industrial Insurance Fund transfers expenditures and cash within the Accident, Medical Aid, and Pension Reserve Accounts, as well as the Supplemental Pension and Second Injury Accounts from the Workers' Compensation Program.

Certain goods and services are provided to L&I by other Washington State agencies. The OST and the WSIB are the Industrial Insurance Fund's agents for managing its cash and investments. Fees related to the management of the Industrial Insurance Fund's investments are deducted from investment income.

The tables below summarize payments made and expenditures reported for goods and services provided by other Washington State agencies for Fiscal Years 2013 and 2012. Payments made may be more or less than reported expenditures due to accruals.

Related Party Transactions
Payments Made for Goods and Services

	Fiscal Year 2013	Fiscal Year 2012
Office of the Attorney General	$ 18,257,444	$ 14,815,648
Department of Enterprise Services[1]	15,090,049	14,862,567
Consolidated Technology Services	9,751,753	5,242,693
Washington State Patrol	592,354	385,067
Office of the State Auditor	494,119	444,367
Office of Financial Management[1]	368,071	113,180
Office of the Secretary of State	335,441	335,380
Office of Administrative Hearings	259,738	101,738
Employment Security Department	48,467	48,116
Department of Revenue	17,181	-
Department of Transportation	14,094	14,498
Office of Administrator for the Courts	6,188	8,094
Department of Licensing	5,390	4,870
Department of Corrections	2,145	3,146
Office of the State Treasurer	1,988	1,088
Total	$ 45,244,420	$ 36,380,451

[1]During Fiscal Year 2012, the Department of Information Services, Department of General Administration, Department of Printing, Department of Personnel, and a portion of the Office of Financial Management were consolidated into the Department of Enterprise Services.

Related Party Transactions Expenditures Reported for Goods and Services		
	Fiscal Year 2013	Fiscal Year 2012
Office of the Attorney General	$ 18,328,204	$ 17,837,938
Department of Enterprise Services[1]	14,518,919	16,622,057
Consolidated Technology Services	8,920,652	6,800,790
Washington State Patrol	600,170	481,257
Office of the State Auditor	511,441	457,429
Office of the Secretary of State	354,951	351,866
Office of Financial Management[1]	334,602	146,649
Office of Administrative Hearings	206,747	155,538
Employment Security Department	47,000	56,475
Department of Revenue	17,181	1,074
Department of Transportation	16,319	14,749
Office of Administrator for the Courts	6,045	8,597
Department of Licensing	3,164	7,386
Office of the State Treasurer	2,078	1,276
Department of Corrections	1,681	3,677
Washington State University	275	-
Department of Social and Health Services	50	-
Total	$ 43,869,479	$ 42,946,758

[1]During Fiscal Year 2012, the Department of Information Services, Department of General Administration, Department of Printing, Department of Personnel, and a portion of the Office of Financial Management were consolidated into the Department of Enterprise Services.

The following amounts were due from other Washington State agencies at the end of the fiscal year:

Totals Due from Related Parties		
	June 30, 2013	June 30, 2012
Office of the Attorney General	$ 9,071	$ 14,591
Washington State Patrol	4,003	-
Department of Corrections	791	-
Department of Enterprise Services	-	5,457
Total	$ 13,865	$ 20,048

The following amounts were due to other Washington State agencies at the end of the fiscal year:

Totals Due to Related Parties		
	June 30, 2013	June 30, 2012
Department of Enterprise Services[1]	$ 2,376,065	$ 2,252,080
Office of the Attorney General	1,570,225	3,022,290
Consolidated Technology Services	726,996	1,558,097
Washington State Patrol	107,109	96,700
Department of Corrections	77,665	18,662
Office of the Secretary of State	47,228	30,378
Employment Security Department	41,752	75,523
Department of Social and Health Services	41,451	-
Office of the State Auditor	30,384	13,062
Department of Transportation	23,658	2,458
Washington State University	6,303	-
Department of Licensing	5,652	104
Department of Natural Resources	1,630	-
Evergreen State College	1,463	-
Department of Revenue	1,074	1,074
Office of Administrative Hearings	809	53,800
Office of the State Treasurer	466	377
Office of Administrator for the Courts	360	504
Office of Financial Management[1]	-	33,469
Total	$ 5,060,292	$ 7,158,578

[1]During Fiscal Year 2012, the Department of Information Services, Department of General Administration, Department of Printing, Department of Personnel, and a portion of the Office of Financial Management were consolidated into the Department of Enterprise Services.

The Washington State Legislature and the Governor provide appropriation authority from the Industrial Insurance Fund for the use by the following Washington State agencies:

- **Board of Industrial Insurance Appeals** hears appeals of decisions made by the Department of Labor & Industries.

- **University of Washington** aims to promote health and minimize occupational disease or injury through teaching, research, and service.

- **Department of Health** completes surveys and on-site investigations of farm worker housing.

- **Health Care Authority** assists with reviews to develop preferred prescription drug lists.

- **Joint Legislative Audit and Review Committee** was contracted to perform a performance audit of the workers' compensation claim management system.

The operating expenses incurred by these agencies are summarized in the following table and are included in the Industrial Insurance Fund's financial information report totals.

Related Party Operating Expenses	Fiscal Year 2013	Fiscal Year 2012
Board of Industrial Insurance Appeals	$ 19,026,860	$ 17,334,549
University of Washington	6,677,865	6,047,145
Department of Health	168,992	174,370
Health Care Authority	93,391	268,727
Joint Legislative Audit and Review Committee	81,028	-
Total	$ 26,048,136	$ 23,824,791

Note 14 - Income Taxes

The Industrial Insurance Fund is exempt from federal income tax under the Internal Revenue Service Code sections 115 and 501(c) (27).

Note 15 - Capital and Contingency Reserve

15.A. Capital

The Industrial Insurance Fund has no shares of stock authorized or outstanding.

15.B. Contingency Reserve

The contingency reserve represents net admitted assets available for financing ongoing operations and uncertainties not otherwise reserved. Changes in the contingency reserve are made up of investment and insurance operating results.

For Fiscal Years 2013 and 2012, changes in the contingency reserve resulted from the following:

Explanation of State Fund Operating and Investment Results
(in millions)

	Fiscal Year 2013	Restated Fiscal Year 2012
Contingency Reserve, July 1	$ 590	$ 789
Unexpected Investment Results:		
Actual Unrealized and Realized Gains (Losses):		
Equities: Unrealized gains (losses)	273	(583)
TIPS: Unrealized gains	(6)	36
Equities: Realized gains	13	516
Fixed Income: Realized gains	74	32
Total Actual Unrealized and Realized Gains	354	1
Less Expected Gains	(110)	(110)
Total Unexpected Investment Results	244	(109)
Insurance Operation Results:		
Prior year loss favorable (unfavorable)	(254)	(35)
Reduction of non-pension discount rate	(66)	(81)
Prior year retro (unfavorable)	-	(54)
Premium adequacy	106	81
Total Insurance Operating Results	(214)	(90)
Change to contingency reserve	30	(199)
Contingency Reserve, June 30	$ 620	$ 590

The contingency reserve balances by fund for Fiscal Years 2013 and 2012 were:

Contingency Reserve Balances by Fund
(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Total
Contingency Reserve, June 30, 2013	$ 202,841,000	$ 416,721,000	$ -	$ 619,562,000
Contingency Reserve, June 30, 2012, as restated	$ 39,560,000	$ 550,579,000	$ -	$ 590,139,000

Note 16 - Asbestos and Environmental Reserves

Claims related to asbestos and hazardous chemicals or waste arise mainly as a result of the claimants' exposure at work and are covered by the Industrial Insurance Fund. There is not a large exposure, and it is not fundamentally different from any other injury due to exposure to hazardous materials in normal industrial activity. Case and IBNR (Incurred But Not Reported) reserves related to asbestos or environmental exposure claims are not specially reserved. IBNR and CAE (Claims Administration Expense) reserves related to asbestos claims are included as part of benefit and CAE liabilities.

The table below shows a gross basis for the case reserves related to asbestos. L&I does not currently hold any reinsurance agreements.

Workers' Compensation
Asbestos Claims

	Fiscal Year 2013	Fiscal Year 2012	Fiscal Year 2011
Beginning case reserve related to asbestos	$ 49,298,040	$ 49,973,965	$ 51,098,510
Benefits incurred	8,452,858	5,788,998	8,812,306
Payments made	(7,004,638)	(6,464,923)	(9,936,851)
Ending case reserve related to asbestos	$ 50,746,260	$ 49,298,040	$ 49,973,965

Note: Amounts are case reserves and do not include IBNR or CAE reserves.

Note 17 - Subsequent Events

For the annual Statutory Financial Information Report as of June 30, 2013, an analysis of subsequent events has been evaluated through the report issue date of December 31, 2013. The event described below existed after June 30, 2013.

17.A. Proposed Rate Announcement

Each year, the Director of the Department of Labor & Industries adopts new workers' compensation insurance premium rates for the next calendar year. On September 16, 2013, the Director announced a proposed 2.7 percent increase in the average premium rate for 2014. The following four principles were used to guide the rate-setting process:

1. Set steady and predictable rate increases to help businesses plan ahead.
2. Benchmark rates against wage inflation (this happens automatically in other states).
3. Slowly rebuild the reserves to protect against unexpected changes.
4. Lower costs while focusing on better outcomes for injured workers.

The final rates will be adopted in early December 2013 and go into effect on January 1, 2014.

Washington State Department of
Labor & Industries

Keep Washington Safe and Working

Supplementary Information

State of Washington Workers' Compensation Program - Basic Plan
Schedule of Claims Development Information
Fiscal Years 2003 through 2012
(in millions)

The table below illustrates how the Workers' Compensation Program Basic Plan's earned revenues (net of reinsurance) and investment revenues compare to the related costs of losses (net of loss assumed by reinsurers) and other expenses assumed by the program as of the end of each of the last ten fiscal years. The Workers' Compensation Program has not purchased reinsurance since September 30, 2002, and has never had a qualifying event that generated a recovery.

The rows of the table are defined as follows:

1. This line shows each fiscal year's earned contribution revenues and investment revenues.
2. This line shows the Basic Plan's incurred claims (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called fiscal accident year).
3. This section shows the cumulative amounts paid as of the end of successive years for each fiscal accident year.
4. This section shows how each fiscal accident year's incurred claims increased or decreased as of the end of successive years. Annual re-estimation results from new information received on known claims, re-evaluation of existing information on known claims, and emergence of new claims not previously known.
5. This line compares the latest re-estimated incurred claims amount to the amount originally established (line 2) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and re-estimates is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature fiscal accident years.

The columns of the table show data for successive fiscal years.

	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013
1. Net earned required contribution and investment revenues	$ 1,337	$ 2,452	$ 1,392	$ 2,406	$ 1,697	$ 1,692	$ 2,797	$ 2,525	$ 2,581	$ 1,928
2. Estimated incurred claims and accident year	2,505	2,308	2,141	2,196	2,256	2,363	2,312	2,254	2,086	2,105
3. Paid (cumulative) as of:										
End of fiscal accident year	244	260	278	295	310	322	298	289	284	296
One year later	528	556	589	625	679	667	604	584	580	
Two years later	681	715	754	817	890	863	773	747		
Three years later	784	821	873	953	1,042	1,000	890			
Four years later	860	906	964	1,059	1,162	1,107				
Five years later	925	977	1,038	1,144	1,258					
Six years later	982	1,039	1,103	1,216						
Seven years later	1,031	1,094	1,159							
Eight years later	1,076	1,142								
Nine years later	1,118									
4. Re-estimated incurred claims and expenses:										
End of fiscal accident year	2,505	2,308	2,141	2,196	2,256	2,363	2,312	2,254	2,086	2,105
One year later	2,203	1,989	2,053	2,234	2,559	2,535	2,271	2,139	2,026	
Two years later	1,971	1,939	2,055	2,390	2,647	2,538	2,261	2,066		
Three years later	1,864	1,954	2,151	2,441	2,724	2,485	2,137			
Four years later	1,886	2,025	2,196	2,526	2,662	2,411				
Five years later	1,941	2,067	2,244	2,445	2,576					
Six years later	1,966	2,111	2,198	2,388						
Seven years later	2,016	2,056	2,186							
Eight years later	1,965	2,058								
Nine years later	1,941									
5. Increase (decrease) in estimated incurred claims and expenses from end of policy year	(564)	(250)	45	192	320	48	(175)	(188)	(60)	

Source: Washington State Department of Labor & Industries Actuarial Services

State of Washington Schedule of Funding Progress for Other Postemployment Benefits

This schedule presents the results of the OPEB valuation for Fiscal Years 2013, 2011, and 2009:

Schedule of Funding Progress
Other Postemployment Benefits
Valuation Years 2013, 2011, and 2009
(in millions)

	2013	2011	2009
Actuarial valuation date	1/1/2013	1/1/2011	1/1/2009
Actuarial value of plan assets	$ -	$ -	$ -
Actuarial accrued liability (AAL)*	$ 3,706	$ 3,492	$ 3,787
Unfunded actuarial accrued liability (UAAL)	$ 3,706	$ 3,492	$ 3,787
Funded ratio	0%	0%	0%
Covered payroll	$ 5,787	$ 5,937	$ 5,678
UAAL as a percentage of covered payroll	64%	59%	67%

* Based on projected unit credit actuarial cost method.

Source: Schedule provided by the Washington State Office of Financial Management with data from the Washington State Office of the State Actuary

Supplemental Investment Risk Interrogatories
June 30, 2013

1. The Industrial Insurance Fund's total admitted assets as reported on page 27 of this annual Statutory Financial Information Report were $13,183,235,000 at June 30, 2013.

2. Following are the Industrial Insurance Fund's ten largest exposures to a single issuer/borrower/investment by investment category, excluding: (i) U.S. government, U.S. government agency securities, and those U.S. government money market funds listed in the Appendix to the SVO's *Practices and Procedures Manual* as exempt, (ii) property occupied by the Industrial Insurance Fund, and (iii) policy loans:

	Amount	Percentage of Total Admitted Assets
Bond - Freddie Mac	$ 346,086,000	2.63%
Bond - Fannie Mae	150,677,000	1.14%
Bond - Norfolk Southern Corp	105,402,000	0.80%
Bond - Burlington Northern Santa Fe	91,869,000	0.70%
Bond - Citigroup Commercial Mortgage	89,726,000	0.68%
Bond - British Columbia Prov of	87,988,000	0.67%
Bond - Southern Cal Edison	81,851,000	0.62%
Bond - Petrobras Intl Fin Co	80,368,000	0.61%
Bond - Vale Overseas Limited	78,902,000	0.60%
Bond - JPMorgan Chase & Co	74,983,000	0.57%

3. The Industrial Insurance Fund's total admitted assets held in bonds and preferred stocks, by NAIC rating, including bonds classified as short term investments at June 30, 2013, were:

	Amount	Percentage of Total Admitted Assets
Bonds with an NAIC rating of 1	$ 7,238,995,000	54.91%
Bonds with an NAIC rating of 2	3,133,154,000	23.77%
Bonds with an NAIC rating of 3	250,877,000	1.90%
Bonds with an NAIC rating of 4	14,788,000	0.11%

4. Assets held in foreign investments:

   Assets held in foreign investments exceeded 2.5 percent of the Industrial Insurance Fund's total admitted assets.

Supplemental Investment Risk Interrogatories
June 30, 2013

Total admitted assets held in foreign investments at June 30, 2013:

Asset Type	Amount	Percentage of Total Admitted Assets
Bonds	$ 2,568,785,000	19.49%
Equities	668,182,000	5.07%

Total admitted assets held in foreign investments in bonds by NAIC rating at June 30, 2013:

NAIC Rating	Amount	Percentage of Total Admitted Assets
Countries rated NAIC – 1	$ 980,371,000	7.44%
Countries rated NAIC – 2	1,365,178,000	10.36%
Countries rated NAIC – 3	208,448,000	1.58%
Countries rated NAIC – 4	14,788,000	0.11%

Ten largest non-sovereign (i.e. non-governmental) investments held in foreign issues at June 30, 2013:

Issuer	NAIC Rating	Amount	Percentage of Total Admitted Assets
Vale Overseas Limited	2	$ 78,902,000	0.60%
Siemens Financieringsmat	1	59,917,000	0.45%
Oderbrecht Finance Ltd	2	53,774,000	0.41%
Southern Copper Corp	2	53,450,000	0.41%
DBS Bank Ltd/Singapore	1	49,995,000	0.38%
National Australia Bank Ltd	1	44,921,000	0.34%
Aust & NZ Banking Group	1	39,962,000	0.30%
BRF - Brasil Foods SA	2	39,848,000	0.30%
Woodside Finance Ltd	2	39,837,000	0.30%
Hutchinson Wham Int 03/33	1	34,931,000	0.26%

	Amount	Percentage of Total Admitted Assets
5. Total admitted assets held in Canadian investments	$1,019,776,000	7.74%

6. The Industrial Insurance Fund had no investments with contractual sales restrictions, which are defined as investments having restrictions that prevent investments from being sold within 90 days.

Supplemental Investment Risk Interrogatories
June 30, 2013

7. The Industrial Insurance Fund's admitted assets held in equity interests (including investments in the shares of mutual funds, preferred stocks, publicly traded equity securities, and other equity securities, including Schedule BA equity interests, and excluding money market and bond mutual funds listed in the Appendix to the SVO's *Practices and Procedures Manual*, as exempt, or Class 1) were:

Fund	Amount	Percentage of Total Admitted Assets
Blackrock MSCI U.S. IMI Index	$ 1,062,288,000	8.06%
MSCI EAFE Index SL CTF	415,272,000	3.15%
MSCI Emerging Markets Free IND	129,492,000	0.98%
MSCI Small Cap Index (Provisio)	55,510,000	0.42%
Canada MSCI CTF	42,527,000	0.32%
MSCI Equity Index Fund	18,347,000	0.14%
MSCI Canada Small Cap	7,034,000	0.05%

Assets held in equity interest exceeded 2.5 percent of the Industrial Insurance Fund's total admitted assets.

8. The Industrial Insurance Fund did not hold any nonaffiliated, privately-placed equities under Securities Exchange Commission (SEC) Rule 144a or SEC Rule 144 without volume restrictions.

9. The Industrial Insurance Fund did not hold general partnership interests.

10. The Industrial Insurance Fund did not own any mortgage loans.

11. The Industrial Insurance Fund did not have any individual parcels or groups of contiguous parcels of real estate.

12. The Industrial Insurance Fund held no investments in mezzanine real estate loans.

13. The Industrial Insurance Fund did not have admitted assets subject to repurchase agreements, reverse repurchase agreements, dollar repurchase agreements or dollar reverse repurchase agreements at June 30, 2013.

14. The Industrial Insurance Fund did not own any warrants not attached to other financial instruments, options, caps, and floors at June 30, 2013.

15. The Industrial Insurance Fund did not have any exposure for collars, swaps, and forwards during Fiscal Year 2013.

16. The Industrial Insurance Fund did not have any potential exposure for futures contracts during Fiscal Year 2013.

Summary Investment Schedule
June 30, 2013

The Industrial Insurance Fund held cash and invested assets as of June 30, 2013, consisting of the following:

	Gross investment holding		Admitted assets as reported in the annual statement			
	Amount	Percentage	Amount	Securities Lending Reinvested Collateral Amount	Total Amount	Percentage
Bonds:						
U.S. Treasury securities	$ 2,683,872,000	21.14%	$ 2,683,872,000	$ -	$ 2,683,872,000	21.14%
Foreign government (including Canada, excluding mortgage-backed securities)	1,145,913,000	9.03%	1,145,913,000	-	1,145,913,000	9.03%
Mortgage-backed securities (includes residential and commercial mortgage-backed securities)						
Issued or guaranteed by GNMA	93,994,000	0.74%	93,994,000	-	93,994,000	0.74%
Issued or guaranteed by FNMA, FHLMC	1,318,098,000	10.38%	1,318,098,000	-	1,318,098,000	10.38%
Issued or guaranteed by all other	358,109,000	2.82%	358,109,000	-	358,109,000	2.82%
Other fixed income securities (excluding short-term)						
Unaffiliated domestic securities	2,616,967,000	20.62%	2,616,967,000	-	2,616,967,000	20.62%
Unaffiliated foreign securities	2,393,087,000	18.85%	2,393,087,000	-	2,393,087,000	18.85%
Equity interests:						
Commingled index funds - domestic	1,062,288,000	8.37%	1,062,288,000	-	1,062,288,000	8.37%
Commingled index funds - foreign	668,182,000	5.26%	668,182,000	-	668,182,000	5.26%
Receivables for securities and interest	108,775,000	0.86%	108,775,000	-	108,775,000	0.86%
Cash and cash equivalents	7,670,000	0.06%	7,670,000	22,710,000	30,380,000	0.24%
Securities lending collateral	27,469,000.00	0.22%	-	-	-	0.00%
Short-term investments	208,683,000	1.65%	208,683,000	4,759,000	213,442,000	1.69%
Total	$ 12,693,107,000	100.00%	$ 12,665,638,000	$ 27,469,000	$ 12,693,107,000	100.00%

Washington State Department of
Labor & Industries

Keep Washington Safe and Working

Independent Actuarial Opinion

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October 5, 2013

Statement of Actuarial Opinion

State of Washington – Industrial Insurance Fund

Identification

I, Rod Morris, am a Specialist Leader with the firm of Deloitte Consulting LLP. I am a Member of the American Academy of Actuaries and meet its qualification standards for rendering this Statement of Actuarial Opinion, and I am a Fellow of the Casualty Actuarial Society. I was appointed by the Washington State Auditors' Office to provide a Statement of Actuarial Opinion regarding the reasonableness of the State of Washington Industrial Insurance Fund's ("the Fund") carried loss and loss adjustment expense ("LAE") reserves as of June 30, 2013.

The Fund is comprised of three Workers' Compensation Program Accounts: the Accident Account, the Medical Aid Account, and the Pension Reserve Account. The Fund is currently administered by the State of Washington Department of Labor & Industries ("the Department").

Scope

I have examined the reserves listed in Exhibit A: Scope, as shown in the Fund's Statutory Financial Information Report, as of June 30, 2013. The loss and loss adjustment expense reserves specified in Exhibit A, on which I am expressing an opinion, reflect the Loss Reserve Disclosure items (8 thru 10) listed in Exhibit B.

In forming my opinion on the loss and loss adjustment expense reserves, I relied upon data provided by Mr. William Vasek, the Department's Chief Actuary, his actuarial staff, and Sharon Elias, the Department's Financial Services Program Manager. I evaluated that data for reasonableness and consistency. My examination included the use of such actuarial assumptions and methods and such tests of the calculations as I considered necessary.

My review was limited to items listed in Exhibit A, and did not include an analysis of any other balance sheet items. I have not examined the Fund's assets and I have formed no opinion as to the validity or value of these assets.

Opinion

In my opinion, the amounts carried in Exhibit A on account of the items identified:

(A) meet the requirements of the insurance laws of the State of Washington.

(B) are consistent with reserves computed in accordance with accepted loss reserving standards and principles.

(C) make a reasonable provision for all unpaid loss and loss expense obligations of the Fund under the terms of its contracts and agreements.

Relevant Comments

A. Risk of Material Adverse Deviation

I have identified the major risk factors for the Fund as the lack of diversity of exposure by line of business and by state, future medical trend, the discounting of the reserves, reserve leverage, future cost of living adjustments and the impact of the 2011 Reforms. The potential impact of these risk factors is described in the following paragraphs. The absence of other risk factors from this listing does not imply that additional factors will not be identified in the future as having been a significant influence on the Fund's reserves.

By statute, the Fund's direct exposure is limited to one line of business (workers' compensation) in one state (Washington). Therefore, any adverse trends affecting this line of business and/or state could have a material effect on the Fund's loss and loss adjustment expense reserves. Such trends would include legislative benefit level changes and adverse decisions or interpretations of law that may have an effect on all open workers' compensation claims.

A major assumption in the analysis of the medical component of the workers' compensation reserves is the selection of a long-term medical trend factor to apply to future calendar year medical payments. Estimating medical trend has become increasingly difficult in recent years because it has been highly variable. In my opinion, there is a higher than normal degree of variability associated with the Fund's medical loss reserves due to the uncertainty surrounding future medical trends and the expected length of medical payments.

The Department discounts the loss and loss adjustment expense reserves to reflect the time value of money using an average annual interest rate of 3.71%. Changes to the interest rate used for discounting could result in material changes to the reserves.

The Fund defines its "Contingency Reserve" as the difference between its assets and liabilities. Other insurance companies typically refer to this Contingency Reserve as Statutory Surplus. Due to the size of the Fund's Contingency Reserve, $619.6 million, relative to the size of its loss and loss adjustment expense reserve, $12.3 billion, any small changes in reserves will have a material impact on the Contingency Reserve. The current reserve leverage ratio (reserve / contingency reserve) is significantly higher than the majority of workers' compensation carriers in the industry and workers' compensation funds in other states.

An implicit assumption in the Department's actuarial review is that the State of Washington cost of living adjustments will be similar to cost of living adjustments approved by the Federal Government for Social Security retirement benefits. Future State of Washington cost of living adjustments that vary significantly from those approved by the Federal Government for Social Security retirement benefits could result in a material change in future costs and the adequacy of the reserves, especially for the Pension Reserve Account.

During 2011, the State of Washington passed two bills (SSB 5801 and EHB 2123) that promote getting workers back on the job faster and made other changes that impact costs. These changes are expected to reduce the system's overall costs in the future and also have an impact on past claims. These reforms are considered in the Department's unpaid claim liability as of June 30, 2013. Key changes included in the reforms are:

- Claim Resolution Structured Settlement Agreements
- Deductions for Prior PPD Awards from TPD Benefits
- Elimination of Interest on Unpaid PPD Award Schedules
- One-Year Freeze in COLA, Delay in First COLAs
- Washington Stay-At-Work Program
- Statewide Provider Network
- COHE Expansion

There is uncertainty related to the impact of these changes on the unpaid claim liability. The amount of net savings contemplated in the unpaid claim liability as of June 30, 2013 totals $293.5 million on a discounted basis. The contemplated savings related to the reforms has been significantly reduced this year. Specifically, the contemplated savings related to the structured settlement agreements has been reduced by 75%. The number of structure settlements agreed to and approved has been much less than expected. Therefore, the savings related to this provision of the reforms was reduced accordingly.

With respect to this Statement of Actuarial Opinion, the amount of adverse deviation that I consider to be material is $123.9 million. My basis for determining this amount is 20% of the Contingency Reserve, which is an amount that would represent a reasonable upward fluctuation in loss and loss adjustment expense reserves from those carried by the Fund that would be material to the Contingency Reserve. At this time, my assessment is that the Fund does have a significant risk of a material adverse deviation.

My materiality standard was selected based on the context in which this opinion letter will be used. It is prepared solely to assess the reasonableness of the Fund's loss and loss adjustment expense reserves. Other measures of materiality might be used for reserves that are being evaluated in a different context.

B. Other Disclosures in Exhibit B

Underwriting Pools or Associations

The Fund participates in the Washington United States Longshore and Harbor Workers' Compensation Act Assigned Risk Plan ("WARP") which was established to provide USL&H workers' compensation insurance coverage for employers unable to purchase it through the normal private insurance market. The Fund pays assessments to WARP and participates in any underwriting losses or surpluses incurred by WARP. Based on discussions with the Department, we understand that WARP is not currently in a deficit position. Therefore, the Fund has not booked a reserve to account for any unpaid claim liability related to WARP.

We understand that the Fund does not participate in any other voluntary or involuntary pools.

Asbestos Exposures and Environmental Exposures

I have reviewed the Fund's exposure to asbestos and environmental claims. In my opinion, the chance of material liability related to asbestos and environmental claims is remote. The Fund has not provided coverage that could reasonably be expected to produce material levels of asbestos and/or environmental liability claims activity.

Disclosure of Unearned Premium Reserves for Long Duration Contracts

The Fund does not write single or fixed premium policies with coverage periods of thirteen months or greater which are non-cancelable and not subject to premium increase.

Reinsurance

The Fund has no ceded or assumed reinsurance. Based on discussions with the Department's management and their description of the Fund's ceded (and/or assumed) reinsurance, I am not aware of any reinsurance contract that either has been or should have been accounted for as retroactive reinsurance or financial reinsurance.

Discounting

The Department discounts the loss and loss adjustment expense reserves to reflect the time value of money. The amount of discount is based on an actuarially derived projected payment pattern and two selected annual interest rates.

- For the Medical Aid Account, the Department's selected interest rate is 1.5%.
- For the Pension Reserve Account, the Department's selected interest rate is 6.5%.
- For the Accident Account, a combination of the two interest rates is used to discount the reserves. The future total permanent disability and fatal transfers made to the Pension Account assume interest discounts based on an annual rate of 6.5%. The actual transfer payments and all other payments are discounted using a Department selected rate of 1.5%.

The average combined interest rate for the Fund is approximately 3.71% with a total discount amount of $7.7 billion. The interest rates were selected by the Department, and I make no opinion regarding the appropriateness of the selected rates. The interest rate used to discount the Accident Account future total permanent disability and fatal transfers made to the Pension Account remained the same this year at 6.5%. The interest rate used for all other future payments was reduced this year from 2.0% to 1.5%. The effect of reducing this interest rate was an increase in the discounted unpaid claim liability of $373.9 million including the current fiscal accident year.

Major Assumption Changes

The Department lowered its long term inflation rate assumption this year from 2.0% to 1.5% to reflect more recent lower inflation rates. The effect of reducing the inflation rate was a decrease in the discounted unpaid claim liability of $290.5 million including the current fiscal accident year.

Over the past year, the Department has reduced its estimate of the number of total permanent disability claims for accident periods prior to June 30, 2012 by 1,051 claims. The reduction was the result of the closing of more of the active time loss claims than was expected over the past year. The effect of reducing this estimate was a decrease in the discounted unpaid claim liability of approximately $220.0 million.

C. General Uncertainty

In evaluating whether the reserves make a reasonable provision for unpaid losses and loss adjustment expense, it is necessary to project future loss and loss adjustment expense payments. It is certain that actual future losses and loss adjustment expenses will not develop exactly as projected and may, in fact, vary significantly from the projections. No warranty is expressed or implied that such variance will not occur.

Further, my projections make no provision for the broadening of coverage by legislative action or judicial interpretation or for extraordinary future emergence of new classes of losses or types of losses not sufficiently represented in the Fund's historical data base or which are not yet quantifiable.

Actuarial Report

An actuarial report and underlying actuarial workpapers supporting the findings expressed in this Statement of Actuarial Opinion will be provided to the Department to be retained for a period of seven years in its administrative offices and available for regulatory examination.

This Statement of Opinion is solely for the use of assessing the reasonableness of the loss and LAE reserves and is only to be relied upon by the Fund and the State.

Rod Morris

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October 5, 2013

Statement of Actuarial Opinion – Year Ended June 30, 2013

State of Washington Industrial Insurance Fund

Exhibit A: SCOPE

Loss Reserves:	**Amount**
A. Net of Reinsurance Reserve for Unpaid Losses	$11,806,072,000
B. Net of Reinsurance Reserve for Unpaid Loss Adjustment Expenses	$ 529,165,000
Total Net Loss and Loss Adjustment Expenses Reserves	$12,335,237,000
C. Reserve of Unpaid Losses – Direct and Assumed	$11,806,072,000
D. Reserve for Unpaid Loss Adjustment Expenses – Direct and Assumed	$ 529,165,000
Total Gross Loss and Loss Adjustment Expense Reserves	$12,335,237,000
E. Retroactive Reinsurance Reserve Assumed	$0
F. Other Loss Reserve items on which the Appointed Actuary is expressing an Opinion	$0
Premium Reserves:	
G. Reserve for Direct and Assumed Unearned Premiums for Long Duration Contracts	$0
H. Reserve for Net Unearned Premiums for Long Duration Contracts	$0
I. Other Premium Reserve items on which the Appointed Actuary is expressing an Opinion	$0

Statement of Actuarial Opinion – Year Ended June 30, 2013

State of Washington Industrial Insurance Fund

Exhibit B: DISCLOSURES

Item:	**Column 1**	**Column 2**	**Column 3**	**Column 4**
1. **Name of Appointed Actuary**		**Last** Morris	**First** Rodney	**Middle** Scott
2. **The Appointed Actuary's Relationship to the Company.** Enter E or C based upon the following: E if an Employee, C if a Consultant			**C**	
3. **The Appointed Actuary is a Qualified Actuary based upon what qualification?** Enter F, A, M, or O based upon the following: **F** if a Fellow of the Casualty Actuarial Society (FCAS) **A** if an Associate of the Casualty Actuarial Society (ACAS) **M** if not a member of the Casualty Actuarial Society, but a Member of the American Academy of Actuaries approved by the Casualty Practice Council, as documented with the attached approval letter. **O** for Other			**F**	
4. **Type of Opinion, as identified in the OPINION** paragraph. Enter R, I, E, Q, or N based upon the following: **R** if reasonable **I** if Inadequate or Deficient Provision **E** if Excessive or Redundant Provision **Q** if Qualified. Use Q when part of the OPINION is Qualified. **N** if No Opinion			**R**	
5. **Materiality Standard expressed in $US** (Used to answer Question #6.)	$123,912,400			
6. Is there a Significant Risk of Material Adverse Deviation? YES or NO				YES [X] NO [ ]
7. **Statutory Surplus (Contingency Reserve)**	$619,562,000			

State of Washington Industrial Insurance Fund

Exhibit B: DISCLOSURES

Item:	Column 1	Column 2	Column 3	Column 4
8. Discount included as a reduction to loss reserves and loss expense reserves as reported in Schedule P				
8.1 Non-tabular Discount	$1,519,112,000			
8.2 Tabular Discount	$6,169,416,000			
9. The net reserves for losses and expenses for the Company's share of voluntary and involuntary underwriting pools' and associations' unpaid losses and expenses that are included in reserves shown on the Liabilities, Surplus and Other Funds page, Losses and Loss Adjustment Expenses lines.	n/a			
9. The total claims made extended loss and expense reserve (Schedule P Interrogatories)				
9.1 Amount reported as loss reserves	n/a			
9.2 Amount reported as unearned premium reserves	n/a			
10. Other items on which the Appointed Actuary is providing Relevant Comments	n/a			

State of Washington Industrial Insurance Fund
Statutory Financial Information Report

Other formats for persons with disabilities are available on request.
Call 1-800-547-8367. TDD users, call 360-902-5797.
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