



Washington State Department of
Labor & Industries



State of Washington Industrial Insurance Fund Statutory Financial Information Report

For the Fiscal Years Ended June 30, 2015 and 2014



***State of Washington Industrial Insurance Fund
Statutory Financial Information Report***
For the Fiscal Years Ended June 30, 2015 and 2014



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Department of Labor and Industries

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Washington State Office of Financial Management

Washington State Investment Board



Keep Washington Safe and Working

State of Washington Industrial Insurance Fund
Statutory Financial Information Report
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Table of Contents

	<u>Page</u>
INTRODUCTORY SECTION	
Letter of Transmittal	3
Organization Chart	7
FINANCIAL SECTION	
Independent Auditor’s Report	11
Management’s Discussion and Analysis	15
Consolidated Statutory Financial Statements	
Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve	29
Consolidated Statutory Statement of Operations and Changes in Contingency Reserve	30
Consolidated Statutory Statement of Cash Flows.....	31
Notes to the Consolidated Statutory Financial Statements	33
Supplementary Information	
Schedule of Undiscounted Claims Development Information	79
Supplemental Investment Risk Interrogatories.....	80
Summary Investment Schedule.....	84
INDEPENDENT ACTUARIAL OPINION	
Statement of Actuarial Opinion	85



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Introductory Section



Keep Washington Safe and Working



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

December 4, 2015

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

The Revised Code of Washington 51.44.115 requires the Department of Labor and 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, 2015.

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, 2015 and 2014. 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.

PROFILE OF THE INDUSTRIAL INSURANCE FUND

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, 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 ended June 30.

L&I, an agency of Washington State, is responsible for managing the state's workers' compensation system; enforcing the Washington Industrial Safety and Health Act; providing safety and health consultations and information; enforcing wage and hour, child labor and family leave requirements; managing the state's Crime Victims' Compensation Program; registering contractors and apprentices; inspecting electrical work, elevators, boilers and factory-assembled structures; and issuing licenses for certain skilled trades.

L&I headquarters is located at 7273 Linderson Way SW in Tumwater, Washington. There are 18 additional L&I field offices across Washington State that enable us to respond to specific needs in different localities.

The workers' compensation system has existed in Washington State for 104 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.

Washington's workers' compensation insurance was provided solely through the State 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 the Self-Insurance Program, which allows an option for qualified employers with sufficient financial resources to self-insure. Self-insured employers pay the cost of claims for their injured workers from their own funds and also assume significant responsibility for their own claims administration. The workers of self-insured employers are entitled to the same rights and benefits as those workers insured by the State Fund managed by L&I. There are approximately 355 employers who are self-insured, covering approximately one-quarter of all workers in Washington.

During the 2011 legislative session, the Legislature passed another historic workers' compensation reform designed to improve outcomes for injured workers, reduce disability and cut costs for the state's Workers' Compensation Program. Included in this reform were the creation of the Stay at Work and Structured Settlement Programs and the Medical Provider Network, and the expansion of the Centers of Occupational Health and Education (COHEs).

The State Fund also has an optional financial incentive program, called Retrospective Rating, to help qualifying employers reduce their industrial insurance costs through safety and return-to-work efforts. Employers who join the Retrospective Rating Program receive partial refunds if their claim costs are lower than expected, but must pay additional premiums if their claim costs are higher than expected.

The Industrial Insurance Fund covers approximately 174,000 employers and 2.69 million workers statewide. Total premiums assessed during fiscal year 2015, including both the employer and worker portions, were \$2.01 billion. Over 82,000 claims were accepted in fiscal

year 2015; about 80 percent of the accepted claims were for medical treatment only and received no compensation for time off work or disability-related benefits. Approximately 38,500 claims are active in any given month, of which about 17,700 are receiving time-loss benefits, many of which involve long-term disability and complex medical issues. In fiscal year 2015, retraining plans were completed by 474 injured workers who were not able to return to any type of work at the employer of injury.

MAJOR INITIATIVES

Governor Jay Inslee has directed state agencies to measure performance, improvements, innovation, engagement, transparency and accountability in state government. In response, L&I is focused on five goal areas:

- Make workplaces safe.
- Help injured workers heal and return to work.
- Make it easy to do business with L&I.
- Help honest workers and businesses by cracking down on the dishonest ones.
- Ensure L&I is an employer of choice.

L&I's efforts to make workplaces safe involve reducing the rate of injury and fostering a culture of safety in the workplace. Data shows that the agency is making a difference. A 10-year L&I study that began in 1999 shows that an agency safety inspection or consultation results in reductions in compensable workers' compensation claims ranging from 6.4 to 12.9 percent, depending on the type of business. Subsequent surveys conducted from 2012 to 2013 show that those earlier numbers continue to hold up.

L&I is helping injured workers heal and return to work by creating a culture where employers, workers, medical providers, vocational experts, and L&I staff are all focused on maintaining the workers' connection to the workforce, along with their motivation to return to work. Using data to identify the most at-risk injured workers allows L&I's Early Return to Work staff in the field to quickly reach out to the workers and their employers to develop light-duty work options. We are working closely with private sector vocational professionals to identify services most likely to result in a return to work when opportunities with the worker's employer of injury appear to be exhausted. In addition, the agency has partnered with the Employment Security Department to work together to provide services to injured workers motivated to return to work, and to make sure the hand-off from workers' compensation to unemployment insurance is quick and simple.

In an effort to make it easier to do business with L&I, informational materials have become clearer, processes have been improved based on customer expectations, and new computer applications now allow employers to pay workers' compensation quarterly premiums and businesses to purchase licenses online. In addition, L&I has worked hard to ensure that Washington's businesses aren't faced with the challenge of wildly fluctuating workers' compensation rates. The agency has been able to do that, in part, thanks to efficiencies within the organization. L&I pledged to help rebuild reserves by saving up to \$70 million through administrative efficiencies, and the agency exceeded that goal in fiscal year 2015 by actually saving \$515 million – and this work continues.

L&I is cracking down on unscrupulous business practices by improving methods for identifying illegal activities. L&I created an Underground Economy Advisory Committee to develop strategies for improving the effectiveness of combatting the underground economy. The agency is also stepping up its efforts to publicize the state's prosecution of fraudulent workers, providers and employers. During plea bargain negotiations, some of the plaintiffs have actually indicated they would rather pay a higher fine than have a press release sent out about their business. The agency refuses to negotiate away the public's right to know about criminal proceedings, but the offer demonstrates that such publicity can be a powerful prevention tool.

In order to ensure that L&I is an employer of choice, L&I continues to encourage and promote safety, well-being, and a culture of trust, as well as to provide employees with opportunities to grow and learn. L&I is continuing to use Lean to empower employees to make decisions that affect their work. Employee-led Lean projects have reduced time for claim processing, improved relationships with customers, streamlined our collections process, and reduced burden on staff.

L&I has recently launched a multi-year enterprise initiative - *Business Transformation*. The objective of the initiative is to engage staff to transform our business processes, culture, and technology so that we can successfully achieve our mission and continue to meet customer expectations in the future. We are currently in the first phase of the initiative, which will establish the 10-year vision and develop a roadmap to help us achieve this vision.

ACKNOWLEDGEMENTS

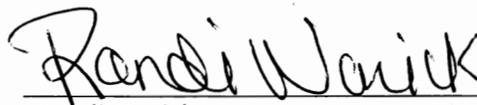
As in the work and service we provide every day, this Statutory Financial Information Report represents our commitment to maintain excellence in financial reporting, and the financial statements are in conformance with the highest standards of financial accountability.

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



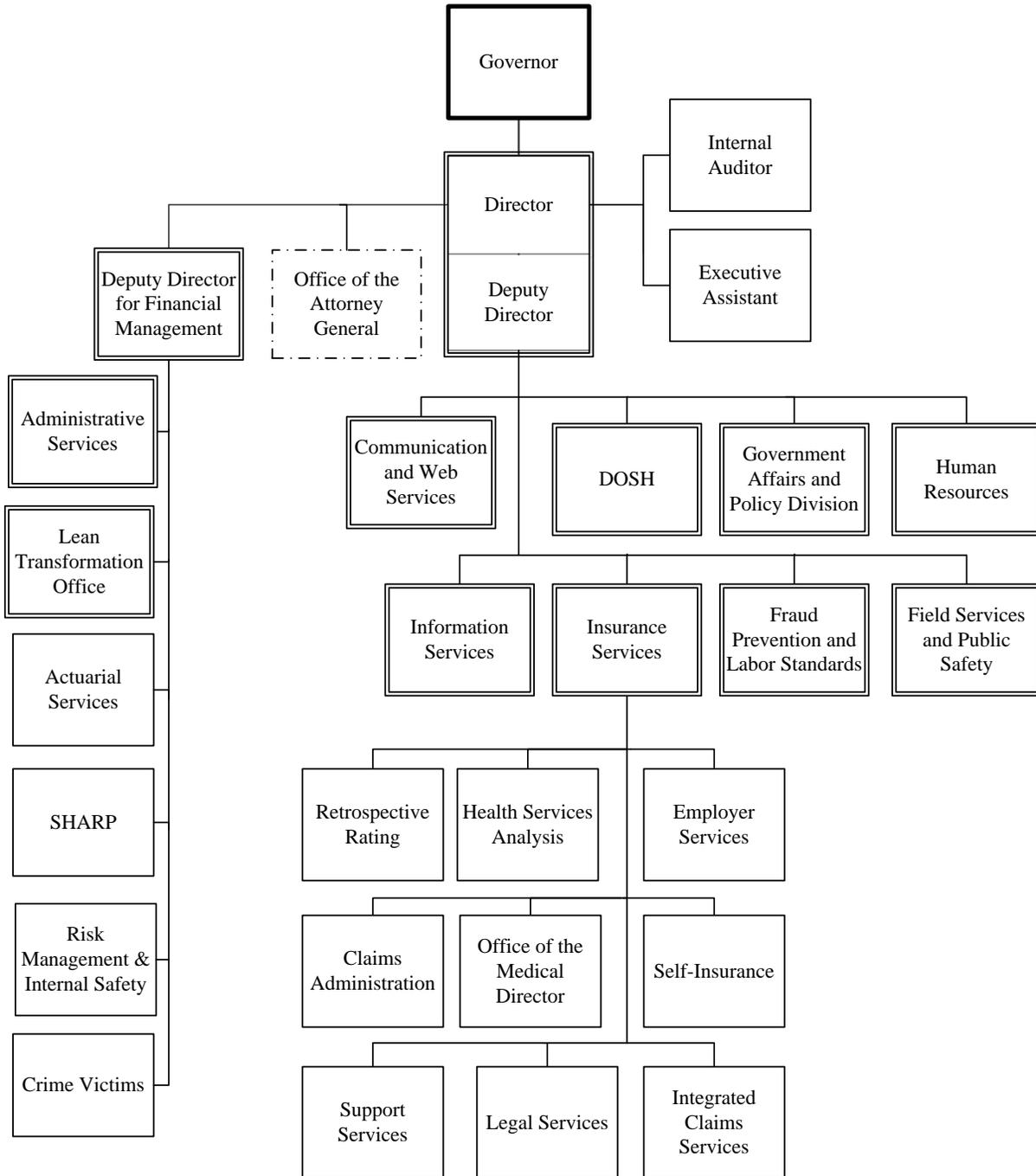
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**Organization Chart
June 30, 2015**





Keep Washington Safe and Working

Financial Section



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Independent Auditor's Report

Mr. Joel Sacks Director
Washington State Department of Labor and Industries
Industrial Insurance Fund
Olympia, Washington

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 contingency reserve as of June 30, 2015 and 2014, and the related consolidated statutory statements of operations and changes in contingency reserve, and consolidated statutory cash flows for the years 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 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 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 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 financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

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

As described in Note 1 to the financial statements, the 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 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, 2015 and 2014, 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 financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, and contingency reserve of the Fund as of June 30, 2015 and 2014, and the results of its operations and its cash flows for the year then ended, on the basis of accounting described in Note 1.

Other Matters

Required Supplementary Information

Our audit was conducted for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying supplementary information included in the *Supplemental Schedule of Investment Risk Interrogatories* and the *Summary Investment Schedule* on pages 80 through 84 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 financial statements taken as a whole.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements. The *Introductory Section, Management Discussion and Analysis, the Statement of Actuarial Opinion Section, and Schedule of Claims Development Information - Basic Plan* are presented for purposes of additional analysis and are not a required part of the financial statements.

The *Schedule of Claims Development Information – Basic Plan* is the responsibility of management and was derived from and relate directly to the underlying accounting and other records used to prepare the financial statements. Such 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 additional procedures in accordance with 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 financial statements taken as a whole.

The information contained in the *Introductory Section, Management Discussion and Analysis and the Statement of Actuarial Opinion sections* have not been subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

A handwritten signature in black ink that reads "Eide Bailly LLP". The signature is written in a cursive, flowing style.

Fargo, North Dakota
December 2, 2015



Keep Washington Safe and Working

Management's Discussion and Analysis

Our management's discussion and analysis of the state of Washington Industrial Insurance Fund's (State Fund) Statutory Financial Information Report provides an overview of the Industrial Insurance Fund's financial performance for the fiscal years ended June 30, 2015 and 2014. The information included here should be considered along with the transmittal letter, which can be found on pages 3-6 of this report, and the accompanying Consolidated Statutory Financial Statements and notes to the Consolidated Statutory Financial Statements, which follow this narrative.

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

Washington was one of the first states to enact workers' compensation laws. 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 State Fund until 1971, when the system underwent a major overhaul. It was then that 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. The state of Washington's Department of Labor and Industries (L&I) operates as an exclusive workers' compensation fund, one of only four remaining in the United States.

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

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.

Size and Scope of Washington's Industrial Insurance Fund

The following information provides some context on the size and scope of the Industrial Insurance Fund and how it changed between fiscal year 2014 and 2015.

Statistics at a Glance		
	Fiscal Year 2015	Fiscal Year 2014
Employers insured*	174,000	169,000
Workers covered*	2,690,000	2,580,000
Hours reported**	3,538,000,000	3,388,000,000
Premiums assessed (employers' portion)**	\$ 1,624,000,000	\$ 1,514,000,000
Premiums assessed (workers' portion)**	\$ 386,000,000	\$ 343,000,000
Benefits incurred expense*	\$ 1,880,432,000	\$ 2,131,342,000
Number of claims filed	109,359	106,903
Total days paid for lost work	6,841,091	7,054,849

Note: The data above is a snapshot as of September following the fiscal year-end.

* Rounded to the nearest thousand

** Rounded to the nearest million

In fiscal year 2015, Washington's workers' compensation system provided insurance for about 2.69 million employees working for 174,000 employers. There were 109,359 claims filed and 82,707 claims accepted. Among the accepted claims, 66,411 of them were medical-only claims. There were 61 fatal pensions awarded in fiscal year 2015. Total premiums assessed from both employers and workers during the current year were approximately \$2,010 million. The business or industry group that filed the greatest number of claims was restaurants and taverns. The most common injuries were traumatic injuries to muscles, tendons, ligaments, and back joints, including the spine and spinal cord.

Overview of the 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.

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, 2015 and 2014. The Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve can be found on page 29 of this report.

The Consolidated Statutory Statement of Operations and Changes in Contingency Reserve shows how the Fund's contingency reserve changed during the fiscal year. It presents revenues and expenses for fiscal years 2015 and 2014. The Consolidated Statutory Statement of Operations and Changes in Contingency Reserve can be found on page 30 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 and cash equivalents during fiscal years 2015 and 2014. The Consolidated Statutory Statement of Cash Flows can be found on page 31 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 pages 33-75 of this report.

These financial statements have been prepared in conformity with the Statutory Accounting Principles (SAP), as promulgated by the National Association of Insurance Commissioners. The main purpose of SAP-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.

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 fiscal year 2015, the receivable and the accrued liability of \$133,956,000 resulting from the transfer from the Accident Account to the Pension Reserve Account was eliminated in order to arrive at an accurate consolidated Industrial Insurance Fund balance.

State of Washington Industrial Insurance Fund

Financial Position

The Industrial Insurance Fund's financial position at June 30, 2015 and 2014 was as follows:

Summary of Financial Position As of June 30, 2015 and 2014 (dollars in thousands)				
	June 30, 2015	June 30, 2014	\$ Change	% Change
Admitted Assets				
Fixed income investments	\$ 12,008,655	\$ 11,377,374	\$ 631,281	5.5%
Equities investments	1,895,746	1,886,836	8,910	0.5%
Short-term investments	108,857	264,598	(155,741)	(58.9%)
Receivable for securities	5	41,222	(41,217)	(100.0%)
Total Investments	14,013,263	13,570,030	443,233	3.3%
Securities lending collateral	68,406	4,354	64,052	1471.1%
Interest receivable	112,021	106,653	5,368	5.0%
Cash and cash equivalents	11,385	10,300	1,085	10.5%
Premiums receivable, net	531,231	493,440	37,791	7.7%
Other assets	83,796	48,345	35,451	73.3%
Total Admitted Assets	\$ 14,820,102	\$ 14,233,122	\$ 586,980	4.1%
Liabilities and Contingency Reserve				
Benefit liabilities	\$ 12,660,158	\$ 12,372,673	\$ 287,485	2.3%
Claims administration liabilities	580,764	539,864	40,900	7.6%
Retrospective rating adjustments	184,980	141,598	43,382	30.6%
OPEB liabilities	42,573	32,299	10,274	31.8%
Other liabilities	58,079	192,813	(134,734)	(69.9%)
Collateral from securities lending activities	68,406	4,354	64,052	1471.1%
Total Liabilities	13,594,960	13,283,601	311,359	2.3%
Contingency Reserve	1,225,142	949,521	275,621	29.0%
Total Liabilities and Contingency Reserve	\$ 14,820,102	\$ 14,233,122	\$ 586,980	4.1%

Total admitted assets of \$14,820 million increased by \$587 million, or 4.1 percent, as compared to the end of fiscal year 2014, primarily due to increases of \$443 million in total investments, \$64 million in securities lending collateral, \$38 million in premiums receivable, and \$35 million in other assets.

The most significant changes in the investment balances are from increases of \$631 million in fixed income investments. This increase was partially offset by decreases of \$156 million in short-term investments and \$41 million in the receivable for securities.

- Additional fixed income investments were purchased with the proceeds from rebalancing the short-term and equity portfolios. Also, cash collected from operations and net investment income received was reinvested within the fixed income portfolio.
- Decreases in short-term investments and the receivable for securities for fiscal year 2015 are mainly due to timing of investment activities.

State of Washington Industrial Insurance Fund

Both assets and liabilities from securities lending activities increased by \$64 million as compared to June 30, 2014, due to an increased demand for borrowing securities. The June 30, 2015, balance of cash collateral held for securities lending transactions was \$68 million. Additional information on securities lending collateral is included in Note 8 - Sale, Transfer and Servicing of Financial Assets and Extinguishments of Liabilities of this report.

Most of the premiums receivable balance represents the estimated premiums due for the quarter ended June 30, 2015. The estimated receivables have increased by \$38 million as compared to June 30, 2014, mostly as a result of an increase in the number of hours reported by employers, more hours reported by businesses in higher-rated classes, and a premium rate increase in the Medical Aid Account.

The change in the other assets balance mostly consists of a receivable in the Pension Reserve Account for \$34 million that is due from the Second Injury Account. As previously discussed, 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 fiscal year 2015, a transfer was required from the Second Injury Account to the Pension Reserve Account.

Total benefit liabilities increased \$287 million, or 2.3 percent, to \$12,660 million during fiscal year 2015, as shown by the following table:

Benefit Liabilities		
(in thousands)		
	Fiscal Year 2015	Fiscal Year 2014
Benefit liabilities, beginning	\$ 12,372,673	\$ 11,806,072
New liabilities incurred, current year	1,662,520	1,548,682
Development on prior years		
Change in reserve discount	236,214	333,167
Other development on prior liabilities	(55,220)	249,493
Change in discount rate	36,918	-
Claim payments	(1,592,947)	(1,564,741)
Change in benefit liabilities	287,485	566,601
Benefit liabilities, ending	\$ 12,660,158	\$ 12,372,673

It is expected that benefit liabilities will change every year due to normal activities, such as adding the current accident year liabilities, discounting existing liabilities, and paying claims. In addition, benefit liabilities also changed due to management's decision to refine our actuarial estimates and favorable development on prior liabilities. This fiscal year, benefit liabilities increased as a result of the following managerial decisions that have no direct relationship to the claim operations:

- L&I has a plan to reduce the pension discount rate from 6.5 to 4.5 percent by 2023. During fiscal year 2015, the pension discount rate was reduced from 6.5 to 6.4 percent, which increased liabilities by \$37 million.
- The mortality assumptions underlying the calculation of pension liabilities were developed by the Office of the Insurance Commissioner and have been used since 1987, but these assumptions do not consider the gender of the recipient. L&I implemented updated mortality tables on April 1, 2015, that include separate tables by gender, which increased benefit liabilities by \$165 million.
- When the Legislature passed the Workers' Compensation reforms in 2011, L&I estimated the potential savings from the reforms and recognized the savings by reducing liabilities. Now that the reforms are operational and the savings are reflected in claims data, the benefit liabilities were increased by \$83 million for the last adjustment to avoid double-counting the 2011 reform savings.

The increases in benefit liabilities explained above were partially offset by favorable development from new information on previously-estimated liabilities. Medical claims are closing faster, and there were significantly fewer active medical claims than expected, resulting in a \$444 million decrease in liabilities.

Detailed changes in the benefit liabilities are explained in Note 9 - Changes in Benefit and Claims Administration Liabilities of this report.

The Retrospective Rating Program is a voluntary financial incentive program offered by L&I to reduce workplace injuries and costs associated with workers' compensation claims. The program provides an economic incentive to employers by refunding a portion of their workers' compensation premiums if injury claims are below estimates during three annual evaluations. If employer claims are above estimates, an additional premium is assessed to the employer's account. The Retrospective Rating Adjustments liability includes the estimated return of earned premiums, net any additional premiums expected to be assessed through the final adjustment for all current participants. This liability increased \$43 million as compared to June 30, 2014, due to an increase in standard premiums reported by retrospective rating participants and improved retrospective rating participant performance relative to the Industrial Insurance Fund, which increased average refund percentages and projected refunds.

Other liabilities decreased \$135 million, mainly due to a decrease of \$137 million in the payable for securities. The payable for securities had a balance of \$147 million as of June 30, 2014, and only a \$10 million balance as of June 30, 2015. The payable for securities represents the amount owed for the purchase of investment securities as of the end of the fiscal year that will not be paid until July of the following fiscal year.

The contingency reserve increased by \$276 million due to greater premiums collected than current accident year incurred benefits, investment income, and prior year benefit liabilities increased less than expected.

State of Washington Industrial Insurance Fund

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, 2015 and 2014				
(dollars in thousands)				
	Fiscal Year	Fiscal Year		
	2015	2014	\$ Change	% Change
Net premiums earned	\$ 1,808,152	\$ 1,673,242	\$ 134,910	8.1%
Net investment income earned	493,408	479,774	13,634	2.8%
Net investment realized gains	58,660	303,184	(244,524)	(80.7%)
Self-insured reimbursements	117,987	75,562	42,425	56.1%
Other income	54,853	54,814	39	0.1%
Total Revenue Earned	2,533,060	2,586,576	(53,516)	(2.1%)
Net benefits (losses) incurred	1,880,432	2,131,342	(250,910)	(11.8%)
Claims administration expenses (LAE) incurred	205,310	166,031	39,279	23.7%
Premium administration expenses incurred	42,349	36,487	5,862	16.1%
Other administration expenses incurred	42,474	42,067	407	1.0%
Self-insured administration expenses incurred	27,901	25,982	1,919	7.4%
Non-insurance administration expenses incurred	56,433	49,378	7,055	14.3%
Total Administration Expenses Incurred	374,467	319,945	54,522	17.0%
Total Expenses Incurred	2,254,899	2,451,287	(196,388)	(8.0%)
Net Income	278,161	135,289	142,872	105.6%
Other changes in contingency reserve	(2,540)	194,670	(197,210)	(101.3%)
Changes in contingency reserve, net	275,621	329,959	(54,338)	(16.5%)
Beginning contingency reserve, July 1	949,521	619,562	329,959	53.3%
Ending Contingency Reserve, June 30	\$ 1,225,142	\$ 949,521	\$ 275,621	29.0%

Net premiums earned for the current period is the sum of net premiums collected and the changes in premiums receivable and retrospective rating adjustments liability between June 30, 2014 and June 30, 2015. Net premiums earned increased \$135 million, mainly due to an increase in the number of hours reported by employers, more hours reported by businesses in higher-rated classes, and premium rate increases in the Medical Aid Account. In fiscal year 2015, employers reported 3,538 million hours worked; this figure increased from 3,388 million hours for fiscal year 2014. There has been a steady growth of quarterly standard premiums for 18 quarters since December 31, 2010.

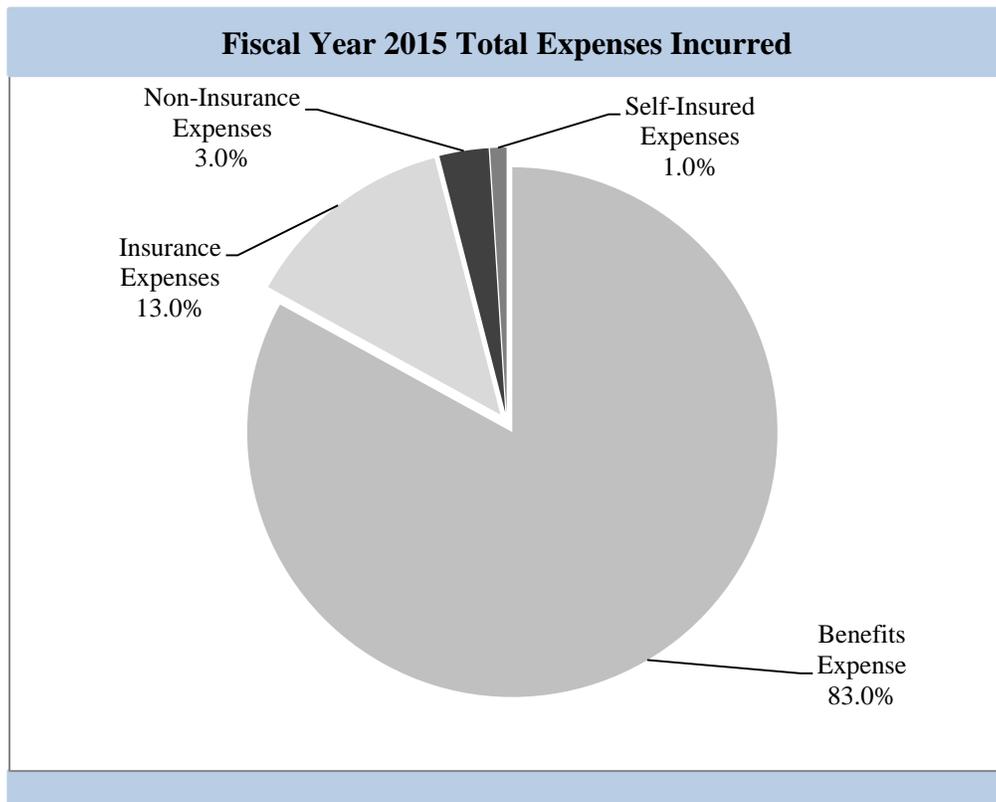
Net investment income earned of \$493 million was \$14 million higher during fiscal year 2015 when compared to fiscal year 2014. Despite continued low interest rates, interest income from bonds increased, because there were more fixed income investments, as previously discussed.

Net realized capital gains from the sale of fixed income and equity investments added \$59 million to net income in fiscal year 2015. Realized capital gains from the sale of fixed income investments due to normal portfolio activity added \$41 million to net income. There was an additional \$18 million realized gain from the sale of \$40 million in equities to rebalance the portfolio. Realized gains decreased \$245 million when compared to fiscal year 2014 due to the sale of TIPS and equities. During fiscal year 2014, TIPS were sold because of a change in the asset allocation policy, and equities were sold to rebalance the portfolio.

In fiscal year 2015, benefits incurred decreased \$251 million from the prior year to \$1,880 million. Benefits incurred includes \$1,593 million in benefits paid and a \$287 million increase in benefit liabilities. The decrease in net benefits incurred mainly resulted from the decrease in the change in benefit liabilities between fiscal year 2015 and fiscal year 2014.

Claims administration expenses incurred is made up of claims administration expenses paid plus the change in claims administration liabilities during the reporting period. The change in claims administration expenses of \$39 million between fiscal year 2015 and 2014 resulted primarily from the change in claims administration liabilities estimated by the actuaries and the claims portion of the Other Postemployment Benefit (OPEB) liabilities. Estimated claims administration liabilities increased mainly as a result of benefit liabilities increasing and an actuarial methodology change and correction.

The following chart provides detail on total expenses incurred in fiscal year 2015:



State of Washington Industrial Insurance Fund

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

Key Financial Ratios

	Fiscal Year 2015	Fiscal Year 2014	Fiscal Year 2015 Excluding One- time Adjustments
Loss ratio	104.0%	127.4%	88.2%
Loss adjustment expense (LAE) ratio	11.4%	9.9%	11.4%
Loss and LAE Ratio	115.4%	137.3%	99.6%
Underwriting and other expense ratio	4.7%	4.7%	4.7%
Combined Ratio	120.1%	142.0%	104.3%
Less: Net investment income ratio	27.3%	28.7%	27.3%
Operating Ratio	92.8%	113.3%	77.0%

- 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. There are many factors that impact loss and LAE ratios, including legislative decisions and claim frequency, severity, and exposure.
- The combined ratio expresses total insurance costs, including benefits and administration expenses incurred as a percentage of total net premiums earned. When the total insurance costs exceed net premium revenues, the combined ratio is above 100 percent. The Industrial Insurance Fund's rates are set based on the anticipated breakeven rate. Income earned on investments supplements premium revenues to cover expenses so that the lowest possible rates can be set. As a result, it is expected that the Industrial Insurance Fund's combined ratio will exceed 100 percent.
- 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 the sum of premiums and net investment income earned. The operating ratio does not include realized or unrealized investment gains. Insurance companies are motivated to make profits and, therefore, work toward an operating ratio below 100 percent. Unlike other insurance companies, the Industrial Insurance Fund is operated as a part of state government, and in most years, its goal is to break even rather than make a profit. However, the Industrial Insurance Fund has a 10-year plan to increase the contingency reserve to 14 percent of liabilities. The contingency reserve was 9 percent of liabilities as of June 30, 2015. The 10-year plan is discussed more later.
- In fiscal year 2015, benefit liabilities increased \$285 million as a result of managerial decisions that have no direct relationship to claim operations as discussed above. If these

State of Washington Industrial Insurance Fund

one-time adjustments had not been made, the loss ratio would have been 88.2 percent and the operating ratio would have been 77.0 percent.

The combined ratio decreased from 142.0 percent in fiscal year 2014 to 120.1 percent in fiscal year 2015. The combined ratio decreased due to an increase in premiums earned and a decrease in benefits incurred.

The operating ratio decreased from 113.3 percent in fiscal year 2014 to 92.8 percent in fiscal year 2015 as a result of the decrease in the combined ratio for the reasons stated above.

The LAE ratio and the underwriting and other expense ratios remain consistently lower when compared to the workers' compensation insurance industry.

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 benefit payments, 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, 2015 and 2014					
(dollars in thousands)					
	Fiscal Year	Fiscal Year			
	2015	2014	\$ Change	% Change	
Operations					
Net premiums collected	\$ 1,813,743	\$ 1,641,324	\$ 172,419	10.5%	
Other reimbursements and income	108,949	116,908	(7,959)	(6.8%)	
Net benefits paid	(1,592,947)	(1,564,741)	(28,206)	1.8%	
Insurance administration expenses paid	(241,079)	(229,603)	(11,476)	5.0%	
Self-insured administration expenses paid	(26,480)	(25,608)	(872)	3.4%	
Non-insurance administration expenses paid	(51,532)	(47,209)	(4,323)	9.2%	
Operating Cash Flow In (Out)	10,654	(108,929)	119,583	109.8%	
Investment Activities					
Investment income	487,010	480,418	6,592	1.4%	
Net realized gains	58,660	303,184	(244,524)	(80.7%)	
Purchases, net	(550,922)	(667,810)	116,888	(17.5%)	
Investment management expenses	(4,317)	(4,233)	(84)	2.0%	
Investment Cash Flow In (Out)	(9,569)	111,559	(121,128)	(108.6%)	
Net increase in cash	\$ 1,085	\$ 2,630	\$ (1,545)	(58.7%)	

Net premiums collected increased \$81 million in the Accident Account and \$91 million in the Medical Aid Account over the prior year, for a total increase of \$172 million. This increase was mainly due to a higher number of hours reported by employers, more hours reported by businesses in higher-rated classes, and premium rate increases in the Medical Aid Account.

Other reimbursements and income collected decreased \$8 million, mainly due to a one-time self-insured employer surety receipt of about \$5 million remitted to L&I as a result of the Hostess bankruptcy in fiscal year 2014. A self-insured employer is required to provide a surety bond as insurance in case it ever defaults on its obligation to its injured workers. In case of default, the surety proceeds are paid from either a bond company or a bank and are used to provide future benefits to the injured workers of that employer.

Net benefits paid increased \$28 million when compared to the prior year, as explained below.

- The Accident Account's \$3 million increase in net benefits paid resulted from increasing exposure as a result of the increase in the number of hours worked and increased average payments per claim, partially offset by a decrease in the number of active claims.
- The Medical Aid Account's \$4 million increase in net benefits paid was due to increasing exposure as a result of the increase in the number of hours worked and an increase in medical inflation, which is the average medical costs per claim, offset by fewer active claims that are more than 13 years old.
- The Pension Account's net benefits paid increased \$21 million, mainly because of higher numbers of pensioners receiving benefits, together with higher average monthly benefits.

Administration expenses paid have increased \$17 million, or 5.5 percent, primarily due to the increase in expenses for one-time information technology projects, including the Business Transformation Project, the Electronic Benefit Payment System, and the Occupational Health Management System for the Centers of Occupational Health & Education (COHEs), and an increase in grants awarded by the Safety & Health Investment Program.

The increase of \$7 million in net investment income collected was mainly due to an increase in bond investment income, because there were additional fixed income securities in fiscal year 2015.

There was \$59 million in net realized gains in fiscal year 2015, a decrease of \$245 million from the previous year. The decrease is due to the sale of TIPS and equities in fiscal year 2014 as discussed above.

Investment purchases exceeded sales by \$551 million, mainly due to reinvesting short-term securities, investment income, and net income.

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 factors:

- 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 reinvesting positive cash flow. The Industrial Insurance Fund is able to match projected cash inflows from premiums and investment income from its portfolio with projected cash outflows for payment of benefits.

Future Plan

In 2012, L&I adopted a 10-year plan to increase the contingency reserve to a level between 13 and 15 percent of liabilities, while reducing the rate used to discount pension liabilities from 6.5 to 4.5 percent by 2023. L&I took the first step to reduce the pension discount rate in April of 2015, moving from 6.5 to 6.4 percent. A rate increase of 0.8 percent for workers' compensation premiums was implemented in January 2015 to offset the increase in liabilities from the discount rate adjustment, to protect against wage inflation, and to help build the contingency reserve.

L&I's goal for fiscal year 2016 is to increase the contingency reserve balance from \$1,225 million to \$1,293 million by increasing premium rates and reducing costs by \$35 to \$70 million. By the end of calendar year 2016, L&I plans to reduce the discount rate from 6.4 percent to a range between 6.25 and 6.4 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>.

Consolidated Statutory Financial Statements



Keep Washington Safe and Working

State of Washington Industrial Insurance Fund

Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve
As of June 30, 2015 and 2014
(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Elimination for Consolidated Statements	Total June 30, 2015	Total June 30, 2014
Admitted Assets						
Cash and Investments						
Investments, Net						
Fixed income	\$ 4,525,075,000	\$ 3,997,967,000	\$ 3,485,613,000	\$ -	\$ 12,008,655,000	\$11,377,374,000
Equities	589,999,000	854,887,000	450,860,000	-	1,895,746,000	1,886,836,000
Short-term	29,814,000	34,738,000	44,305,000	-	108,857,000	264,598,000
Receivable for securities	2,000	2,000	1,000	-	5,000	41,222,000
Total Investments	5,144,890,000	4,887,594,000	3,980,779,000	-	14,013,263,000	13,570,030,000
Securities lending collateral	26,176,000	255,000	41,975,000	-	68,406,000	4,354,000
Interest receivable	44,479,000	34,460,000	33,082,000	-	112,021,000	106,653,000
Cash and cash equivalents	7,308,000	2,599,000	1,478,000	-	11,385,000	10,300,000
Total Cash and Investments	5,222,853,000	4,924,908,000	4,057,314,000	-	14,205,075,000	13,691,337,000
Other Assets						
Premiums receivable, net, incl. earned but unbilled	324,954,000	206,277,000	-	-	531,231,000	493,440,000
Real estate and improvements (less \$4,050,000 encumbrances)	17,251,000	17,250,000	-	-	34,501,000	32,055,000
Self-insurance receivables, net	3,108,000	3,055,000	8,137,000	-	14,300,000	10,047,000
Miscellaneous receivables, net	863,000	633,000	167,455,000	(133,956,000)	34,995,000	6,243,000
Total Other Assets	346,176,000	227,215,000	175,592,000	(133,956,000)	615,027,000	541,785,000
Total Admitted Assets	\$ 5,569,029,000	\$ 5,152,123,000	\$ 4,232,906,000	\$ (133,956,000)	\$ 14,820,102,000	\$14,233,122,000
Liabilities and Contingency Reserve						
Liabilities						
Benefits	\$ 4,688,010,000	\$ 3,794,398,000	\$ 4,177,750,000	\$ -	\$ 12,660,158,000	\$12,372,673,000
Other Liabilities						
Claims administration	207,858,000	372,906,000	-	-	580,764,000	539,864,000
Retrospective rating adjustments	184,980,000	-	-	-	184,980,000	141,598,000
Accrued liabilities						
OPEB claim administration	9,847,000	12,991,000	-	-	22,838,000	17,934,000
OPEB other administration	11,854,000	7,881,000	-	-	19,735,000	14,365,000
Other accrued liabilities	159,527,000	18,834,000	3,220,000	(133,956,000)	47,625,000	45,607,000
Deferred revenue	305,000	188,000	-	-	493,000	134,000
Payable for securities	-	-	9,961,000	-	9,961,000	147,072,000
Collateral from securities lending activities	26,176,000	255,000	41,975,000	-	68,406,000	4,354,000
Total Other Liabilities	600,547,000	413,055,000	55,156,000	(133,956,000)	934,802,000	910,928,000
Total Liabilities	5,288,557,000	4,207,453,000	4,232,906,000	(133,956,000)	13,594,960,000	13,283,601,000
Contingency Reserve	280,472,000	944,670,000	-	-	1,225,142,000	949,521,000
Total Liabilities and Contingency Reserve	\$ 5,569,029,000	\$ 5,152,123,000	\$ 4,232,906,000	\$ (133,956,000)	\$ 14,820,102,000	\$14,233,122,000

The Notes to the 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.

State of Washington Industrial Insurance Fund

Consolidated Statutory Statement of Operations and Changes in Contingency Reserve
For the Fiscal Years Ended June 30, 2015 and 2014
(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Total Fiscal Year 2015	Total Fiscal Year 2014
Revenues					
Net standard premiums earned	\$ 1,222,838,000	\$ 772,921,000	\$ -	\$ 1,995,759,000	\$ 1,849,218,000
Less net retrospective rating adjustments	(187,607,000)	-	-	(187,607,000)	(175,976,000)
Net premiums earned	1,035,231,000	772,921,000	-	1,808,152,000	1,673,242,000
Net investment income earned	195,056,000	153,317,000	145,035,000	493,408,000	479,774,000
Net fixed income investment realized gains	16,037,000	8,365,000	16,171,000	40,573,000	261,971,000
Net equity investment realized gains	489,000	651,000	16,947,000	18,087,000	41,213,000
Self-insured administrative expense assessments	12,208,000	11,729,000	-	23,937,000	23,963,000
Self-insured second injury pension reserve assessments	-	-	72,169,000	72,169,000	36,096,000
Self-insured cash funded & bonded pension reimbursements	-	-	21,881,000	21,881,000	15,503,000
Fines, penalties, and interest	43,388,000	3,193,000	64,000	46,645,000	45,504,000
Other income	6,531,000	1,677,000	-	8,208,000	9,310,000
Total Revenues Earned	1,308,940,000	951,853,000	272,267,000	2,533,060,000	2,586,576,000
Expenses					
Benefits incurred	718,497,000	487,767,000	674,168,000	1,880,432,000	2,131,342,000
Administration expenses incurred:					
Insurance expenses incurred					
Claims administration expenses incurred	77,576,000	127,734,000	-	205,310,000	166,031,000
Premium administration expenses incurred	20,630,000	21,719,000	-	42,349,000	36,487,000
General insurance administration expenses incurred	13,787,000	7,107,000	-	20,894,000	22,214,000
Other agencies insurance expenses incurred	10,478,000	11,102,000	-	21,580,000	19,853,000
Total insurance expenses incurred	122,471,000	167,662,000	-	290,133,000	244,585,000
Self-insured administration expenses incurred	14,370,000	13,531,000	-	27,901,000	25,982,000
Non-insurance administration expenses incurred	37,716,000	18,717,000	-	56,433,000	49,378,000
Total administration expenses incurred	174,557,000	199,910,000	-	374,467,000	319,945,000
Total Expenses Incurred	893,054,000	687,677,000	674,168,000	2,254,899,000	2,451,287,000
Net Income (Loss) Before Transfers	415,886,000	264,176,000	(401,901,000)	278,161,000	135,289,000
Transfers In (Out)					
Pension funding transfers	(406,794,000)	-	406,794,000	-	-
Net Transfers In (Out)	(406,794,000)	-	406,794,000	-	-
Net Income	9,092,000	264,176,000	4,893,000	278,161,000	135,289,000
Other Changes in Contingency Reserve					
Fixed income unrealized (losses)	(4,046,000)	(1,086,000)	-	(5,132,000)	3,022,000
Equities unrealized gains (losses)	13,270,000	20,535,000	(4,982,000)	28,823,000	333,602,000
Treasury Inflation-Protected Securities unrealized (losses)	-	-	-	-	(136,291,000)
Other accounting adjustments	(21,323,000)	(4,997,000)	89,000	(26,231,000)	(5,663,000)
Change in Contingency Reserve, Net	(3,007,000)	278,628,000	-	275,621,000	329,959,000
Beginning contingency reserve, July 1	283,479,000	666,042,000	-	949,521,000	619,562,000
Ending Contingency Reserve, June 30	\$ 280,472,000	\$ 944,670,000	\$ -	\$ 1,225,142,000	\$ 949,521,000

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.

State of Washington Industrial Insurance Fund

Consolidated Statutory Statement of Cash Flows
For the Fiscal Years Ended June 30, 2015 and 2014
(rounded to the nearest thousand)

	Accident Account	Medical Aid Account	Pension Reserve Account	Total Fiscal Year 2015	Total Fiscal Year 2014
Standard premiums collected	\$ 1,203,585,000	\$ 754,383,000	\$ -	\$ 1,957,968,000	\$ 1,801,318,000
Less retrospective rating adjustments	(144,225,000)	-	-	(144,225,000)	(159,994,000)
Net premiums collected	1,059,360,000	754,383,000	-	1,813,743,000	1,641,324,000
Self-insured administration expense reimbursements	12,306,000	11,823,000	-	24,129,000	24,574,000
Self-insured second injury pension reserve reimbursements	-	-	42,258,000	42,258,000	34,357,000
Self-insured cash funded and bonded pension reimbursements	-	-	15,065,000	15,065,000	18,449,000
Fines, penalties, and interest	25,197,000	1,425,000	-	26,622,000	26,405,000
Other income (expenses)	3,838,000	(2,910,000)	(53,000)	875,000	13,123,000
Fund transfers in (out)	(265,921,000)	-	265,921,000	-	-
Operating Cash Flow In	834,780,000	764,721,000	323,191,000	1,922,692,000	1,758,232,000
Benefits paid	595,576,000	575,654,000	421,717,000	1,592,947,000	1,564,741,000
Administration expenses					
Insurance expenses					
Claims administration expenses	59,796,000	99,710,000	-	159,506,000	151,969,000
Premium administration expenses	19,863,000	20,590,000	-	40,453,000	35,984,000
General insurance administration expenses	13,435,000	6,835,000	-	20,270,000	21,663,000
Other agencies insurance expenses	10,121,000	10,729,000	-	20,850,000	19,987,000
Total insurance expenses	103,215,000	137,864,000	-	241,079,000	229,603,000
Self-insured administration expenses	13,721,000	12,759,000	-	26,480,000	25,608,000
Non-insurance administration expenses	35,269,000	16,263,000	-	51,532,000	47,209,000
Total Administration Expenses Paid	152,205,000	166,886,000	-	319,091,000	302,420,000
Operating Cash Flow Out	747,781,000	742,540,000	421,717,000	1,912,038,000	1,867,161,000
Net Operating Cash Flow In (Out)	86,999,000	22,181,000	(98,526,000)	10,654,000	(108,929,000)
Investment income - fixed income	192,601,000	148,060,000	144,080,000	484,741,000	479,136,000
Investment income - equities	692,000	1,006,000	571,000	2,269,000	1,282,000
Net realized gains on investments	16,526,000	9,016,000	33,118,000	58,660,000	303,184,000
Net (purchases) sales of investments	(294,728,000)	(178,443,000)	(77,751,000)	(550,922,000)	(667,810,000)
Investment expenses	(1,603,000)	(1,480,000)	(1,234,000)	(4,317,000)	(4,233,000)
Total Investment Cash Flow In (Out)	(86,512,000)	(21,841,000)	98,784,000	(9,569,000)	111,559,000
Net Cash Flow In (Out)	487,000	340,000	258,000	1,085,000	2,630,000
Beginning Cash, July 1	6,821,000	2,259,000	1,220,000	10,300,000	7,670,000
Ending Cash, June 30	\$ 7,308,000	\$ 2,599,000	\$ 1,478,000	\$ 11,385,000	\$ 10,300,000

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.



Keep Washington Safe and Working

Notes to the Consolidated Statutory Financial Statements

For the Fiscal Years Ended June 30, 2015 and 2014

Index

	<u>Page</u>
Note 1 - Summary of Significant Accounting Policies	34
Note 2 - Investments.....	44
Note 3 - Real Estate and Improvements	57
Note 4 - Investment Income	58
Note 5 - Retirement Plans, Compensated Absences, Deferred Compensation Plan, and Other Postemployment Benefits.....	59
Note 6 - Commitments and Contingencies.....	64
Note 7 - Leases	64
Note 8 - Sale, Transfer and Servicing of Financial Assets and Extinguishments of Liabilities.....	65
Note 9 - Changes in Benefit and Claims Administration Liabilities	68
Note 10 - Retrospectively-Rated Contracts and Contracts Subject to Redetermination	70
Note 11 - Discounting of Liabilities for Unpaid Benefits or Unpaid Claims Administration Expenses.....	70
Note 12 - Related Party Transactions	72
Note 13 - Income Taxes	73
Note 14 - Capital and Contingency Reserve	73
Note 15 - Asbestos and Environmental Reserves.....	74
Note 16 - Subsequent Events.....	75

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 excluded or 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, Medical Aid, Pension Reserve, Supplemental Pension, Second Injury, and the Self-Insured Employer Overpayment Reimbursement Accounts, 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 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 fiscal year 2015 or balance on June 30, 2015. 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 in which 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

There are three accounts making up the Industrial Insurance Fund: the Accident, Medical Aid, and Pension Reserve Accounts.

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. 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 come 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. 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 L&I quarterly.

The Pension Reserve Account pays benefits to the surviving spouse or dependent of fatally injured workers and to all permanently and totally disabled workers or their surviving spouse or dependents. This includes benefits for pensions awarded to employees of self-insured employers.

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 the estimated present cash value of monthly pension payments is calculated on 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 Statutory Accounting Principles (SAP), which includes 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 SAP 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.

The SAP are required to be used by property and casualty insurance enterprises in the United States (U.S.) 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 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

¹ NAIC AP&P Manual as of March 2015, Section: Preamble Questions and Answers, Question 2, page P-13.

from NAIC SAP and state prescribed accounting practices, and have received approval from the insurer's domiciliary state regulatory authority."²

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 (OIC). The Industrial Insurance Fund is not required to report to the OIC 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 OIC, there is no requirement that the Industrial Insurance Fund request approval from OIC for departures from SAP. Thus, we have no such permitted practices.

While there are no prescribed or permitted practices followed by the Industrial Insurance Fund that differ from SAP, 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 11.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.

² NAIC AP&P Manual as of March 2015, Section: Preamble Questions and Answers, Question 2, page P-13.

State of Washington Industrial Insurance Fund

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 SAP requirements:

Effect of Practices that Depart from SAP		
(rounded to the nearest thousand)		
	As of and For the Fiscal Year Ended June 30, 2015	As of and For the Fiscal Year Ended June 30, 2014
Net Income, WA Basis	\$ 278,161,000	\$ 135,289,000
Effect of practices that depart from SAP		
Non-tabular discounting	46,125,000	(212,890,000)
OPEB administration liability	10,274,000	6,536,000
Net Income, NAIC SAP Basis	\$ 334,560,000	\$ (71,065,000)
Contingency Reserve, WA Basis	\$ 1,225,142,000	\$ 949,521,000
Effect of practices that depart from SAP		
Non-tabular discounting	(1,685,876,000)	(1,732,001,000)
OPEB administration liability	42,573,000	32,299,000
Contingency Reserve, NAIC SAP Basis	\$ (418,161,000)	\$ (750,181,000)

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 SAP 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 with 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 SAP and GAAP

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

- Investments in bonds are reported for SAP at amortized cost or market value based on their NAIC designation; for GAAP, investments in bonds are reported at fair value.
- For SAP, all mortgage-backed and other loan-backed securities are adjusted for the effects of changes in prepayment assumptions using the retrospective 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 amortize 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 mortgage-backed and other loan-backed securities are reported at fair value.
- SAP assets designated as *nonadmitted assets* are 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” and are excluded from total admitted assets. These assets consist primarily of premium receivables 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 AP&P 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.
- SAP 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 SAP 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 SAP 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 SAP 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

Workers’ compensation insurance premiums are determined by 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.

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. 53, a premium deficiency reserve is recognized “...when the anticipated losses, loss adjustment expenses, and maintenance costs exceed the recorded unearned premium reserve and any future installment premiums on existing policies.” Because the Industrial Insurance Fund has sufficient anticipated investment income and 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 6.4 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 from 4.5 to 6.4 percent. The payments are then discounted from the anticipated date of the pension award back to the evaluation date 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 discount rate is typically carried at long-term yield rates for risk-free assets, and the investment term is set equal to the average duration of the benefit and claims administration expense payments. Per L&I policy, the non-pension discount rate is equal to the Benchmark Rate less the Risk Adjustment, rounded to the nearest half a percentage point. The Benchmark Rate is

the five-year moving average of the U.S. 20-Year Treasury yield. The Risk Adjustment equals two percentage points until the Benchmark Rate reaches 4.0 percent. Below 4.0 percent, the Risk Adjustment is half the Benchmark Rate.

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 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 due to interest rate fluctuations. Under RCW 43.08.015, 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.

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.
- 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 mortgage-backed and other loan-backed securities are stated at amortized cost. Non-investment grade mortgage-backed and other 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. In compliance with SSAP No. 43R, changes in currently-estimated cash flows are reviewed quarterly using the State Street Corporation's investment valuation model for prepayment assumptions in valuing mortgage-backed and other loan-backed securities. These securities are revalued using the retrospective adjustment method. See Note 2.H. for other-than-temporary impairment analysis of mortgage-backed and other loan-backed securities.

State of Washington Industrial Insurance Fund

- 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 Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve. 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. Unusual Items and Restricted Assets

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, 2015, trust cash amounted to \$202,942 and is available to reimburse the Industrial Insurance Fund for monthly pension payments. In addition, trust investments totaling \$2,473,560 were invested in U.S. Treasury Notes and are also available to reimburse the Industrial Insurance Fund for future expenses. At June 30, 2014, trust cash and trust investment balances were \$194,012 and \$2,477,155, respectively.

The following tables summarize restricted assets at June 30, 2015 and 2014:

Restricted Assets June 30, 2014 (dollars in thousands)									
Restricted Asset Category	Total General Account (G/A)	Restricted G/A Assets Supporting	Total Separate Account (S/A)	Restricted S/A Assets Supporting	Total		% Restricted to	Total	% Restricted to
	Restricted Assets	S/A Activity	Restricted Assets	G/A Activity	Restricted	Total Assets	Total Assets	Admitted Assets	Total Admitted Assets
Collateral held under security lending agreements	\$ 68,406	\$ -	\$ -	\$ -	\$ 68,406	\$ 68,406	100.00%	\$ 14,820,102	0.46%

Restricted Assets June 30, 2014 (dollars in thousands)									
Restricted Asset Category	Total General Account (G/A)	Restricted G/A Assets Supporting	Total Separate Account (S/A)	Restricted S/A Assets Supporting	Total		% Restricted to	Total	% Restricted to
	Restricted Assets	S/A Activity	Restricted Assets	G/A Activity	Restricted	Total Assets	Total Assets	Admitted Assets	Total Admitted Assets
Collateral held under security lending agreements	\$ 4,354	\$ -	\$ -	\$ -	\$ 4,354	\$ 4,354	100.00%	\$ 14,233,122	0.03%

- 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 SAP, 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 (EDP) equipment and operating system software to be admitted, up to three 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.8. 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 ten fiscal years. Otherwise, the self-insurance liability program services all claims against the state for injuries and property damage to third parties.

The Industrial Insurance Fund 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 - Investments

2.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 CMIs 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 chapter 43.33A RCW. Eligible investments include:

- U.S. equities.
- International equities.
- 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.

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 to the target allocations as soon as it is practical.

- 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 market value of below investment grade mortgage-backed, asset-backed and commercial mortgage-backed securities shall not exceed 5 percent of total market value of the funds.

2.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 fixed income investments. The Industrial Insurance Fund does not have a formal policy specifically for interest rate risk.

As of June 30, 2015, 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 seven years
- Medical Aid Account – within plus or minus 20 percent of an effective duration target of six years
- Pension Reserve Account – within plus or minus 20 percent of an effective duration target of seven 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.

2.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, 2015, 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, nor 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, 2015.

Custodial Credit Risk - Custodial credit risk is the risk that in the event a depository institution or counterparty fails, the Industrial Insurance Fund would not be able to recover the value of its deposits, investments, or collateral securities. As of June 30, 2015, 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. There are no general policies relating to custodial credit risk.

2.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 \$695.0 million and \$682.4 million invested in an international commingled equity index fund at June 30, 2015 and 2014, respectively. As such, no currency denomination risk is present at June 30, 2015.

2.E. Derivatives

To manage its exposure to fluctuations in interest and currency rates while increasing portfolio returns, 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.

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 \$1.30 billion and \$1.47 billion at June 30, 2015 and 2014, respectively.

2.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 2015 or 2014, and there were no liabilities outstanding as of June 30, 2015 or 2014.

2.G. Wash Sales Transactions

Wash sales are any transfers that occur when an asset is sold and the proceeds are reinvested within 30 days in the same or substantially the same security. These transactions involve unrated securities or those with NAIC designations of 3 or below. There were no wash sale transactions in the Industrial Insurance Fund during fiscal year 2015 or 2014.

2.H. Bonds

At June 30, 2015 and 2014, bonds were comprised of U.S. government, other governments, corporate, mortgage-backed, and other loan-backed securities, with an aggregate book adjusted carrying value (BACV) of \$12,008,655,000 and \$11,377,374,000 and fair value of \$12,502,439,000 and \$12,232,300,000, respectively, as shown in the following tables:

Book Adjusted Carrying Values and Fair Values				
June 30, 2015				
(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	\$ 1,165,527	\$ 5,116	\$ (11,937)	\$ 1,158,705
All other government obligations	1,300,556	59,458	(14,762)	1,345,252
Mortgage-backed and other loan-backed securities	1,800,133	127,225	(3,424)	1,923,934
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	7,637,471	432,925	(103,362)	7,967,035
Hybrid securities	104,968	3,036	(491)	107,513
Total	\$ 12,008,655	\$ 627,760	\$ (133,976)	\$ 12,502,439

State of Washington Industrial Insurance Fund

Book Adjusted Carrying Values and Fair Values				
June 30, 2014				
(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	\$ 1,055,063	\$ 2,993	\$ (12,734)	\$ 1,045,322
All other government obligations	1,346,981	81,828	(8,521)	1,420,288
Mortgage-backed and other loan-backed securities	1,916,467	154,793	(4,372)	2,066,888
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	6,943,856	648,336	(10,774)	7,581,418
Hybrid securities	115,007	3,457	(80)	118,384
Total	\$ 11,377,374	\$ 891,407	\$ (36,481)	\$ 12,232,300

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, 2015 and 2014. 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, 2015						
(in thousands)						
Investment Type	Fair Value	Book Adjusted Carrying Value	Maturity			
			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	\$ 1,158,705	\$ 1,165,527	\$ -	\$ 818,655	\$ 54,933	\$ 291,939
All other government obligations	1,345,252	1,300,556	163,932	510,500	357,645	268,478
Mortgage-backed and other loan-backed securities	1,923,934	1,800,133	20,953	189,619	83,253	1,506,308
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	7,967,035	7,637,471	306,456	2,519,104	1,944,262	2,867,649
Hybrid securities	107,513	104,968	-	4,988	99,981	-
Total	\$ 12,502,439	\$ 12,008,655	\$ 491,342	\$ 4,042,866	\$ 2,540,073	\$ 4,934,374

State of Washington Industrial Insurance Fund

Schedule of Maturities						
June 30, 2014						
(in thousands)						
Investment Type	Fair Value	Book Adjusted Carrying Value	Maturity			
			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	\$ 1,045,322	\$ 1,055,063	\$ 49,965	\$ 701,984	\$ 303,114	\$ -
All other government obligations	1,420,288	1,346,981	101,980	605,281	380,619	259,101
Mortgage-backed and other loan-backed securities	2,066,888	1,916,467	-	186,258	132,085	1,598,124
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	7,581,418	6,943,856	206,943	2,384,979	1,740,925	2,611,009
Hybrid securities	118,384	115,007	-	-	115,007	-
Total	\$ 12,232,300	\$ 11,377,374	\$ 358,888	\$ 3,878,502	\$ 2,671,750	\$ 4,468,234

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 NAIC. There were no securities with an NAIC designation higher than 5 at the fiscal years ended June 30, 2015 and 2014.

Fair Value of Securities by NAIC Designation						
June 30, 2015						
(in thousands)						
	NAIC Designation					Total
	1	2	3	4	5	
U.S. government obligations - excluding mortgage-backed securities	\$ 1,158,705	\$ -	\$ -	\$ -	\$ -	\$ 1,158,705
All other government obligations	1,111,220	225,644	8,388	-	-	1,345,252
Mortgage-backed and other loan-backed securities	1,923,934	-	-	-	-	1,923,934
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	4,627,784	3,256,155	83,096	-	-	7,967,035
Hybrid securities	20,304	82,304	4,905	-	-	107,513
Total	\$ 8,841,947	\$ 3,564,103	\$ 96,389	\$ -	\$ -	\$ 12,502,439

Fair Value of Securities by NAIC Designation						
June 30, 2014						
(in thousands)						
	NAIC Designation					Total
	1	2	3	4	5	
U.S. government obligations - excluding mortgage-backed securities	\$ 1,045,322	\$ -	\$ -	\$ -	\$ -	\$ 1,045,322
All other government obligations	1,078,670	268,776	72,842	-	-	1,420,288
Mortgage-backed and other loan-backed securities	2,066,331	-	-	-	557	2,066,888
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	4,085,593	3,297,875	197,950	-	-	7,581,418
Hybrid securities	30,201	83,046	5,137	-	-	118,384
Total	\$ 8,306,117	\$ 3,649,697	\$ 275,929	\$ -	\$ 557	\$ 12,232,300

State of Washington Industrial Insurance Fund

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, 2015 and 2014, were as follows:

Bonds with Unrealized Losses						
June 30, 2015						
(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	\$ 246,216	\$ (7,187)	\$ 488,603	\$ (4,914)	\$ 734,819	\$ (12,101)
All other government obligations	91,710	(3,693)	131,960	(12,522)	223,670	(16,215)
Mortgage-backed and other loan-backed securities	120,453	(831)	68,442	(2,117)	188,895	(2,948)
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	2,213,231	(86,207)	331,914	(24,494)	2,545,145	(110,701)
Hybrid securities	24,426	(537)	-	-	24,426	(537)
Total	\$ 2,696,036	\$ (98,455)	\$ 1,020,919	\$ (44,047)	\$ 3,716,955	\$ (142,502)

Bonds with Unrealized Losses						
June 30, 2014						
(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	\$ 150,344	\$ (67)	\$ 650,563	\$ (12,667)	\$ 800,907	\$ (12,734)
All other government obligations	33,966	(220)	144,648	(9,268)	178,614	(9,488)
Mortgage-backed and other loan-backed securities	94,762	(311)	114,492	(4,076)	209,254	(4,387)
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	337,239	(1,461)	412,437	(10,675)	749,676	(12,136)
Hybrid securities	19,920	(80)	-	-	19,920	(80)
Total	\$ 636,231	\$ (2,139)	\$ 1,322,140	\$ (36,686)	\$ 1,958,371	\$ (38,825)

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 of selling 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 and other loan-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 and other loan-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

State of Washington Industrial Insurance Fund

issuer(s). As of June 30, 2015, no mortgage-backed or other loan-backed securities have been determined to be other-than-temporarily impaired.

The following tables summarize realized gains or losses of bonds that were redeemed or sold during fiscal years 2015 and 2014:

Bonds Redeemed or Sold June 30, 2015 (in thousands)				
	Sales			Net Realized
	Proceeds	Realized Gains	Realized Losses	Gains (Losses)
U.S. government obligations - excluding mortgage-backed securities	\$ 333,494	\$ 2,238	\$ (71)	\$ 2,167
All other government obligations	229,635	8,743	-	8,743
Mortgage-backed securities	223,574	-	-	-
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	541,775	29,831	(168)	29,663
Hybrid securities	-	-	-	-
Total	\$ 1,328,478	\$ 40,812	\$ (239)	\$ 40,573

Bonds Redeemed or Sold June 30, 2014 (in thousands)				
	Sales			Net Realized
	Proceeds	Realized Gains	Realized Losses	Gains (Losses)
U.S. government obligations - excluding mortgage-backed securities	\$ 2,144,351	\$ 279,503	\$ (34,345)	\$ 245,158
All other government obligations	42,535	859	-	859
Mortgage-backed securities	179,324	-	-	-
Industrial and miscellaneous - excluding mortgage-backed and other loan-backed securities	527,401	19,165	(3,211)	15,954
Hybrid securities	-	-	-	-
Total	\$ 2,893,611	\$ 299,527	\$ (37,556)	\$ 261,971

State of Washington Industrial Insurance Fund

In compliance with SSAP No. 26, paragraph 20.1, the following table shows the details of the structured notes held by the Industrial Insurance Fund at June 30, 2015 and 2014.

Structured Notes					
June 30, 2015					
(in thousands)					
CUSIP Identification	Actual Cost	Fair Value	Book/Adjusted Carry Value	Mortgage-Referenced Security (Y/N)	
064159CR5	\$ 20,000	\$ 20,076	\$ 20,000		N
136069FV8	25,000	25,088	25,000		N
172967GV7	20,000	20,057	20,000		N
63254AAH1	10,000	10,049	10,000		N
045167CL5	25,000	24,996	25,000		N
Total	\$ 100,000	\$ 100,266	\$ 100,000		

Structured Notes					
June 30, 2014					
(in thousands)					
CUSIP Identification	Actual Cost	Fair Value	Book/Adjusted Carry Value	Mortgage-Referenced Security (Y/N)	
064159CR5	\$ 20,000	\$ 20,110	\$ 20,000		N
136069FV8	25,000	25,148	25,000		N
172967GV7	20,000	20,218	20,000		N
63254AAH1	10,000	10,062	10,000		N
045167CL5	25,000	24,991	25,000		N
Total	\$ 100,000	\$ 100,529	\$ 100,000		

2.I. Common Stocks

The gross unrealized losses on common stocks, fair value of the common stocks, and length of time that individual common stocks have been in a continuous unrealized loss position, at June 30, 2015 and 2014, were as follows:

Common Stocks with Unrealized Losses						
June 30, 2015						
(in thousands)						
	Less than 12 Months		12 Months or Longer		Total	
	Fair value	Unrealized Losses	Fair value	Unrealized Losses	Fair value	Unrealized Losses
Commingled index funds	\$ 145,009	\$ (6,219)	\$ 36,059	\$ (5,651)	\$ 181,068	\$ (11,870)
Total	\$ 145,009	\$ (6,219)	\$ 36,059	\$ (5,651)	\$ 181,068	\$ (11,870)

State of Washington Industrial Insurance Fund

Common Stocks with Unrealized Losses						
June 30, 2014						
(in thousands)						
	Less than 12 Months		12 Months or Longer		Total	
	Fair value	Unrealized Losses	Fair value	Unrealized Losses	Fair value	Unrealized Losses
Commingled index funds	\$ -	\$ -	\$ 41,339	\$ (3,659)	\$ 41,339	\$ (3,659)
Total	\$ -	\$ -	\$ 41,339	\$ (3,659)	\$ 41,339	\$ (3,659)

In compliance with SSAP No. 30, management has looked at all commingled index funds in an unrealized loss position and used several categories of information to determine whether any impairment is other-than-temporary. The information considered for broad equity funds included general market conditions and prospects for the economy as a whole in the short term. Management has no intention of selling these commingled index funds and does not believe these impairments are other-than-temporary.

2.J. 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. The 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

State of Washington Industrial Insurance Fund

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, 2015 and 2014, by the SSAP No. 100 valuation hierarchy:

Investment Assets Carried at Fair Value				
June 30, 2015				
(in thousands)				
	Level 1	Level 2	Level 3	Total
Fixed income	\$ -	\$ 95,696	\$ -	\$ 95,696
Equities	-	1,895,746	-	1,895,746
Total	\$ -	\$ 1,991,442	\$ -	\$ 1,991,442

Investment Assets Carried at Fair Value				
June 30, 2014				
(in thousands)				
	Level 1	Level 2	Level 3	Total
Fixed income	\$ -	\$ 47,876	\$ -	\$ 47,876
Equities	-	1,886,836	-	1,886,836
Total	\$ -	\$ 1,934,712	\$ -	\$ 1,934,712

Only bonds with an NAIC designation 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, 2015, there were nine bonds in this category, with fair values totaling \$95,696,266. On June 30, 2014, there were four bonds in this category, with fair values totaling \$47,875,840.

At the end of each reporting period, the Industrial Insurance Fund evaluates whether or not any event has 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 values 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.

State of Washington Industrial Insurance Fund

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, 2015						
(in thousands)						
	Fair Value	Admitted Value	Level 1	Level 2	Level 3	Total
Fixed income	\$ 12,502,439	\$ 12,008,655	\$ -	\$ 12,502,439	\$ -	\$ 12,502,439
Equities	1,895,746	1,895,746	-	1,895,746	-	1,895,746
Short-term investments	108,857	108,857	-	108,857	-	108,857
Total	\$ 14,507,042	\$ 14,013,258	\$ -	\$ 14,507,042	\$ -	\$ 14,507,042

Investment Assets at Fair Value						
June 30, 2014						
(in thousands)						
	Fair Value	Admitted Value	Level 1	Level 2	Level 3	Total
Fixed income	\$ 12,232,300	\$ 11,377,374	\$ -	\$ 12,232,300	\$ -	\$ 12,232,300
Equities	1,886,836	1,886,836	-	1,886,836	-	1,886,836
Short-term investments	264,598	264,598	-	264,598	-	264,598
Total	\$ 14,383,734	\$ 13,528,808	\$ -	\$ 14,383,734	\$ -	\$ 14,383,734

Note 3 - Real Estate and Improvements

At June 30, 2015 and 2014, the Accident and Medical Aid Accounts admitted only land, buildings, and improvements, net of accumulated depreciation and encumbrances.

SSAP No. 40R requires that buildings more than 50 percent occupied by the reporting entity be categorized as a real estate investment and that depreciation and interest expense 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, 2015, was \$4.1 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, 2015		June 30, 2014	
Land	\$	3,204	\$	3,204
Building occupied by Industrial Insurance Fund		65,134		65,134
Improvements, other than buildings		1,020		1,020
Encumbrances		(4,050)		(7,870)
Accumulated depreciation - building		(30,348)		(28,995)
Accumulated depreciation - improvements		(459)		(438)
Total	\$	34,501	\$	32,055

State of Washington Industrial Insurance Fund

Note 4 - 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, 2015 and 2014, all investment income due and accrued was admitted, with balances accrued by security type, as summarized in the following table:

Interest Income Admitted Due and Accrued			
(in thousands)			
	June 30, 2015		June 30, 2014
U.S. Government obligations - excluding			
mortgage-backed securities	\$ 4,133	\$	1,894
All other government obligations	13,461		14,653
Mortgage-backed and other loan-backed securities	8,066		7,904
Industrial and miscellaneous - excluding			
mortgage-backed and other loan-backed securities	84,641		80,467
Hybrid securities	1,719		1,733
Other interest	1		2
Total	\$ 112,021	\$	106,653

The following table provides details for net investment income by security type for the fiscal years ended June 30, 2015 and 2014:

Net Investment Income Earned			
(in thousands)			
	Fiscal Year 2015		Fiscal Year 2014
U.S. Government obligations - excluding			
mortgage-backed securities	\$ 15,634	\$	27,304
All other government obligations	46,238		47,767
Mortgage-backed and other loan-backed securities	83,036		90,326
Industrial and miscellaneous - excluding			
mortgage-backed and other loan-backed securities	339,098		296,113
Hybrid securities	5,502		5,515
Total Bond Interest	489,508		467,025
Equities dividends	2,269		1,283
Net securities lending income	(182)		355
Other interest and litigation income	571		9,486
Amortization	5,461		5,876
Gross investment income	497,627		484,025
Investment expenses	(4,219)		(4,251)
Total Net Investment Income Earned	\$ 493,408	\$	479,774

Note 5 - Retirement Plans, Compensated Absences, Deferred Compensation Plan, and Other Postemployment Benefits

5.A. Retirement Plans

The Industrial Insurance Fund is administered by L&I, an agency of the state of Washington and part of the primary government. Industrial Insurance Fund employees participate in the Washington State Public Employees' Retirement System (PERS), administered by the Washington State Department of Retirement Systems (DRS).

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.

PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. Under the PERS, the employee and employer contribute a percentage of the employee's compensation.

Each biennium, the state Pension Funding Council adopts Plan 1 employer contributions rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Contribution requirements are established and amended by state statute. All employers are required to contribute at the level established by the Legislature. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

The employer contribution rates for the Industrial Insurance Fund for fiscal years ended June 30, 2015 and 2014, for each of Plans 1, 2, and 3 was 9.21 percent of the employee's annual covered salary. The Industrial Insurance Fund contributed \$13,991,371 and \$13,528,925 to the PERS during the fiscal years ended June 30, 2015 and 2014, respectively. The Industrial Insurance Fund's contribution was 1.5 percent of total employer contributions to the plans in fiscal years ended June 30, 2015 and 2014. The employer contribution rate from July 1, 2015, through June 30, 2016, has already been established by the legislature to be 11.18 percent for each of Plans 1, 2, and 3.

Employee contribution rates for Plan 1 are established by statute at 6 percent for state agencies employees. Contributions for Plan 2 members are determined by the aggregate method and may vary over time. The contribution rate for Plan 2 state agency employees for fiscal years ended June 30, 2015 and 2014 was 4.92 percent of the employee's annual covered salary. Under Plan 3, employer contributions finance the defined benefit portion of the plan, and member contributions finance the defined contribution portion. The Director of the DRS sets Plan 3 employee contribution rate options. Members can choose from six rate options ranging from 5 to 15 percent. Two of the options are graduated rates dependent on the employee's age.

Beginning in fiscal year 2015, the Industrial Insurance Fund's net pension liability was calculated based on GASB Statement No. 68 *Accounting and Financial Reporting for Pensions*. The Industrial Insurance Fund's proportionate share of the collective pension liability for fiscal year ended June 30, 2015 was \$131,010,803 for the plans in which its employees participate. The proportion is based on the Industrial Insurance Fund's contributions relative to the contributions of all participating employers.

Additional information regarding PERS may be obtained from the stand-alone financial report prepared by DRS. A copy of the report may be obtained by contacting the Washington State Department of Retirement Systems, P.O. Box 48380, Olympia, WA 98504-8380 or online at <http://www.drs.wa.gov/administration/annual-report>.

5.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, at which time 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 \$13,690,150 and \$13,945,050 at June 30, 2015 and 2014, respectively.

5.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 DCP by the Industrial Insurance Fund. The DRS administers the DCP and contracts with a third party (currently Great-West) for recordkeeping and other administrative services. The WSIB selects and monitors DCP's investment options based on advice and recommendations provided by the Employee Retirement Benefits Board.

5.D. Other Postemployment Benefits

Employees of the Industrial Insurance Fund are eligible to participate in the state of Washington's defined benefit Other Postemployment Benefit (OPEB) plan, a multiemployer plan, as administered by the state through the Washington State Health Care Authority (HCA).

Plan Description and Funding Policy

Per RCW 41.05.065, the Public Employees Benefits Board (PEBB), created within 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.

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 systems. 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 2014, the average weighted implicit subsidy was valued at \$291 per member per month, and in calendar year 2015, the average weighted implicit subsidy is projected to be \$308 per member per month.

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 2014, the explicit subsidy was up to \$150 per month per member, and it remained at up to \$150 per month per member in calendar year 2015.

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

Contributions are set by the legislature each biennium as part of the budget process. In calendar year 2015, the cost of the subsidies was approximately 6.0 percent of the cost of benefits for active employees. The benefits are funded on a pay-as-you-go basis.

The plan has no investments or other assets. Accordingly, the PEBB OPEB plan is not reported in the financial statements of the state, nor is a separate financial report publicly available.

For information on the results of the most recent actuarial valuation for the OPEB, 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 in accordance with the parameters of GASB Statement No. 45. 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 annual OPEB cost recorded for the Industrial Insurance Fund represents an allocation of the total ARC of the state of Washington, adjusted for interest and amortization. The Industrial Insurance Fund's annual OPEB cost is calculated by the Washington State Office of the State Actuary (OSA) and is recorded by OFM. The allocation is primarily based on L&I's number of active and retired employees in relation to the total number of active and retired employees of the state.

State of Washington Industrial Insurance Fund

The following table shows components of the Industrial Insurance Fund's allocated annual OPEB costs and changes in the Industrial Insurance Fund's Net OPEB Obligation (NOO) for fiscal years 2015 and 2014. All contributions required by the funding method were paid.

Components of Allocated Annual OPEB Cost		
	Fiscal Year 2015	Fiscal Year 2014
Annual required contribution	\$ 12,446,000	\$ 8,625,000
Allocated interest on Net OPEB Obligation	1,292,000	1,031,000
Allocated amortization of Net OPEB Obligation	<u>(1,180,000)</u>	<u>(924,000)</u>
Allocated annual OPEB cost	12,558,000	8,732,000
Allocated contributions made	<u>(2,284,000)</u>	<u>(2,196,000)</u>
Increase in Net OPEB Obligation	10,274,000	6,536,000
Net OPEB Obligation, beginning of year	<u>32,299,000</u>	<u>25,763,000</u>
Net OPEB Obligation, end of year	<u><u>\$ 42,573,000</u></u>	<u><u>\$ 32,299,000</u></u>

The Industrial Insurance Fund's NOO represents 1.8 percent and 1.7 percent of the state of Washington's NOO as of June 30, 2015 and 2014, respectively. The Industrial Insurance Fund's contribution was 1.5 percent and 1.4 percent of total employer contributions to the plan in fiscal years ended June 30, 2015 and 2014, respectively.

The Industrial Insurance Fund's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the NOO for fiscal years 2015, 2014, and 2013 were as follows:

Net OPEB Obligation			
by Fiscal Year			
	2015	2014	2013
Allocated annual OPEB cost	\$ 12,558,000	\$ 8,732,000	\$ 8,451,000
Percentage of annual OPEB cost contributed	18.2%	25.1%	22.8%
Net OPEB Obligation	\$ 42,573,000	\$ 32,299,000	\$ 25,763,000

A complete description of the funded status and actuarial assumptions of the state of Washington's OPEB plan is 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 43127, Olympia, Washington 98504-3127, or online at <http://www.ofm.wa.gov/cafr>.

Note 6 - Commitments and Contingencies

6.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.

6.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.

6.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 7 - Leases

The Industrial Insurance Fund leases 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 2015 and 2014 were \$10,748,463 and \$10,368,992, 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 2020. Some of these renewals are subject to adjustments in future periods.

State of Washington Industrial Insurance Fund

The following table presents future minimum payments for operating leases as of June 30, 2015:

Future Minimum Payments					
June 30, 2015					
Operating Leases (by Fiscal Year)	Accident Account		Medical Aid Account		Total
2016	\$	4,378,534	\$	4,176,227	\$ 8,554,761
2017		3,543,580		3,349,291	6,892,871
2018		2,211,686		2,046,859	4,258,545
2019		1,442,780		1,283,464	2,726,244
2020		1,183,957		1,028,293	2,212,250
Total Future Minimum Lease Payments	\$	12,760,537	\$	11,884,134	\$ 24,644,671

Note 8 - Sale, Transfer and Servicing of Financial Assets and Extinguishments of Liabilities

Securities Lending

The Industrial Insurance Fund participates in securities lending programs with the WSIB and the OST to increase investment income. At June 30, 2015, the Industrial Insurance Fund had \$68,151,292 of cash collateral received through the WSIB in the Accident and Pension Reserve Accounts. There was \$255,396 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.

Debt securities were loaned and collateralized by the Industrial Insurance Fund’s agent with cash, U.S. government or U.S. agency securities, including U.S. agency mortgage-backed securities (exclusive of 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 2015 and 2014, securities lending transactions could be terminated on demand by either the Industrial Insurance Fund or the borrower. At June 30, 2015 and 2014, the cash collateral held had an average duration of 22.5 days and an average weighted final maturity of 79.7 days and 82.2 days, respectively. Because securities lending agreements were terminable at will, their duration did not generally match the duration of the investments made with the cash

State of Washington Industrial Insurance Fund

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.

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. 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 2015 and 2014, 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 2015 or 2014 resulting from a default by either the borrowers or the securities lending agents.

At June 30, 2015 and 2014, total collateral held was \$106,455,879 and \$70,982,464 and fair value of securities on loan were \$102,621,078 and \$69,443,310, respectively.

The market value of cash collateral assets at June 30, 2015 and 2014, was \$68,151,292 and \$4,115,764, respectively. The following tables provide information regarding cash collateral assets:

Cash Collateral Held Under Securities Lending										
June 30, 2015										
(in thousands)										
	NAIC Designation	Book Adjusted		Level 2	Maturity Date					
		Carrying Value	Fair Value	Under 30 days	30 - 59 days	60 - 89 days	90 - 119 days	120 - 179 days	180 days - less than 1 year	1 - 2 years
Cash and cash equivalents	1	\$ 12,220	\$ 12,220	\$ 3,298	\$ 666	\$ 1,332	\$ 2,663	\$ 1,331	\$ 2,930	\$ -
Commercial paper	1	7,057	7,057	1,531	1,331	1,498	533	832	1,332	-
Repurchase agreements	2	1,665	1,665	1,665	-	-	-	-	-	-
Repurchase agreements	Not Rated	22,038	22,038	22,038	-	-	-	-	-	-
U.S. Treasuries	1	4,994	4,994	1,864	866	-	-	333	1,931	-
Yankee CDs	1	15,880	15,880	4,394	666	3,995	666	3,329	2,830	-
Corporate	1	4,295	4,297	666	-	466	-	1,166	666	1,333
Total Cash Collateral Held		\$ 68,149	\$ 68,151	\$ 35,456	\$ 3,529	\$ 7,291	\$ 3,862	\$ 6,991	\$ 9,689	\$ 1,333

State of Washington Industrial Insurance Fund

Cash Collateral Held Under Securities Lending										
June 30, 2014										
(in thousands)										
	NAIC Designation	Book Adjusted	Level 2	Maturity Date						
		Carrying Value	Fair Value	Under 30 days	30 - 59 days	60 - 89 days	90 - 119 days	120 - 179 days	180 days - less than 1 year	1 - 2 years
Commercial paper	1	\$ 484	\$ 484	\$ -	\$ 68	\$ 137	\$ 48	\$ 127	\$ 104	\$ -
Yankee CDs	1	758	758	99	172	154	34	158	141	-
Certificate & time deposits	1	485	485	152	34	69	-	69	161	-
Cash	1	515	515	515	-	-	-	-	-	-
Cash	2	429	429	429	-	-	-	-	-	-
Cash	Not Rated	1,149	1,149	1,149	-	-	-	-	-	-
Corporate	1	226	227	-	-	-	-	-	69	158
Bank note	1	69	69	-	-	-	-	-	-	69
Total Cash Collateral Held		\$ 4,115	\$ 4,116	\$ 2,344	\$ 274	\$ 360	\$ 82	\$ 354	\$ 475	\$ 227

Non-cash collateral cannot be pledged or sold absent borrower default. Accordingly, non-cash collateral held under securities lending contracts with a value of \$38,304,587 at June 30, 2015, and \$66,866,700 at June 30, 2014, has not been included in the Consolidated Statutory Statement of Admitted Assets, Liabilities, and Contingency Reserve. Net earnings received through the securities lending program were -\$182,063 for fiscal year 2015 and \$354,723 for fiscal year 2014.

Securities Lending – OST

State statutes permit the OST 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 has contracted with Citibank, N.A. as a lending agent and receives a share of income from this activity. The lending agent lends 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 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, as currently 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, 2015 and 2014, the Industrial Insurance Fund's cash collateral totaled \$255,396 and \$237,929, respectively, all of which was invested in the LGIP.

Contracts require the lending agent to indemnify the OST if the borrowers fail to return 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,

State of Washington Industrial Insurance Fund

2015, the fair value of securities on loan for the Industrial Insurance Fund totaled \$249,293. At June 30, 2014, the fair value of securities on loan was \$232,283.

The OST 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 years 2015 and 2014, the OST had no credit risk exposure to borrowers because the amounts owed to the borrowers exceeded the amounts the borrowers owed to 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 9 - Changes in Benefit and Claims Administration Liabilities

The following schedule presents the changes in benefit and claims administration liabilities for the fiscal years ended June 30, 2015 and 2014, for the Industrial Insurance Fund:

Changes in Benefit and Claims Administration Liabilities		
(in thousands)		
	Fiscal Year 2015	Fiscal Year 2014
Unpaid benefit and claims administration liabilities, July 1	\$ 12,912,537	\$ 12,335,237
Incurred benefit and claims administration liabilities		
Provision for insured events of the current year	1,818,597	1,643,940
Increase in provision for insured events of prior years	262,240	650,069
Total incurred benefit and claims administration liabilities	2,080,837	2,294,009
Less Payments		
Benefit and claims administration liabilities attributable to		
Insured events of the current year	(300,862)	(296,885)
Insured events of prior years	(1,451,590)	(1,419,824)
Total payments	(1,752,452)	(1,716,709)
Unpaid benefit and claims administration liabilities, June 30	\$ 13,240,922	\$ 12,912,537
Current portion	\$ 1,475,918	\$ 1,458,437
Long-term portion	\$ 11,765,004	\$ 11,454,100

An increase of \$262.2 million in the provision for insured events of prior years in benefit and claims administration liabilities in fiscal year 2015 is comprised of a \$241.8 million change in the reserve discount and \$20.4 million of adverse development on prior years. The main reasons for the adverse development are listed below.

- The pension discount rate was reduced from 6.5 to 6.4 percent.
- L&I implemented updated mortality tables, which include separate tables by gender.
- The final adjustment was made to avoid double counting 2011 reform savings.

State of Washington Industrial Insurance Fund

The adverse development was offset by favorable development due to medical claims closing faster and having significantly fewer active medical claims than expected.

At June 30, 2015 and 2014, \$20,902 million and \$20,366 million of unpaid benefit and claims administration liabilities are shown at their net present and settlement value of \$13,241 million and \$12,912 million, respectively. In the Accident Account, liabilities 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 from 4.5 to 6.4 percent. The payments are then discounted from the anticipated date of the pension award back to the evaluation date, on a non-tabular basis, at 1.5 percent. For more information on discounting, see Note 1.C.3.

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 6.4 percent.

Benefit Liability Development by Program			
June 30, 2015			
(dollars in thousands)			
Program/ Category	Undiscounted Liabilities	Discount Rate	Benefit Liabilities
Accident	\$ 7,130,705	1.5%, 4.5%-6.4%	\$ 4,688,010
Medical Aid	5,043,322	1.5%	3,794,398
Pensions	<u>8,085,993</u>	6.4%	<u>4,177,750</u>
Total Benefit Liability	20,260,020		12,660,158
Claim Administration Expense (CAE)	<u>641,493</u>	1.5%	<u>580,764</u>
Total Benefit and CAE Liabilities	<u><u>\$ 20,901,513</u></u>		<u><u>\$ 13,240,922</u></u>

Benefit Liability Development by Program			
June 30, 2014			
(dollars in thousands)			
Program/ Category	Undiscounted Liabilities	Discount Rate	Benefit Liabilities
Accident	\$ 6,950,589	1.5%, 4.5%-6.5%	\$ 4,565,089
Medical Aid	5,183,269	1.5%	3,882,285
Pensions	<u>7,636,040</u>	6.5%	<u>3,925,299</u>
Total Benefit Liability	19,769,898		12,372,673
Claim Administration Expense (CAE)	<u>596,557</u>	1.5%	<u>539,864</u>
Total Benefit and CAE Liabilities	<u><u>\$ 20,366,455</u></u>		<u><u>\$ 12,912,537</u></u>

Note 10 - Retrospectively-Rated Contracts and Contracts Subject to Redetermination

10.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 the first annual adjustment through the 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.

10.B. Method Used to Record

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

10.C. Amount and Percent of Net Retrospective Premiums

Net premiums for the fiscal year ended June 30, 2015, on retrospectively-rated workers' compensation policies were \$820.2 million, which were 41 percent of total workers' compensation net standard premiums earned. The net premiums for fiscal year ended June 30, 2014, on retrospectively-rated workers' compensation policies were \$750.3 million, which were 41 percent of total workers' compensation net standard premiums earned for that year.

10.D. Calculation of Nonadmitted Retrospective Premiums

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

Note 11 - 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, 2015, only. The Industrial Insurance 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.

11.A. Tabular Discounts

The mortality tables are based on a 2014 study of Industrial Insurance Fund claimant data and the 2000 U.S. Census data. The liabilities for pensions already granted are discounted at 6.4 percent per annum. The liabilities for pensions incurred but not yet granted are discounted at rates from 4.5 to 6.4 percent, reflecting the pension discount rates anticipated to be in effect

State of Washington Industrial Insurance Fund

when the pensions are granted. The June 30, 2015, liabilities include \$6,720,156,000 of such reserves, net of tabular discounts. The amount of the tabular discount for case reserves (i.e. pensions already granted) is \$3,908,243,000 and is \$2,066,472,000 for Incurred But Not Reported (IBNR) reserves at June 30, 2015.

At June 30, 2014, the liabilities, net of tabular discounts, amounted to \$6,471,644,000. The amount of the tabular discount for case reserves was \$3,710,741,000 and is \$2,011,176,000 for IBNR reserves.

Liabilities Discounted on a Tabular Basis*					
June 30, 2015					
(in thousands)					
Fiscal Accident Year	Undiscounted Benefit Liabilities Gross of Tabular Discount	Tabular Discounts		Benefit Liabilities Net of Tabular Discount	
		Case	IBNR		
2005 & Prior	\$ 6,326,100	\$ 2,684,249	\$ 269,827	\$ 3,372,024	
2006	630,371	228,951	82,239	319,181	
2007	727,776	245,839	115,411	366,526	
2008	780,153	225,309	158,203	396,641	
2009	715,689	181,028	168,283	366,378	
2010	625,919	134,250	168,837	322,832	
2011	563,176	98,535	170,122	294,519	
2012	512,029	59,908	179,414	272,707	
2013	563,648	24,890	229,190	309,568	
2014	596,828	13,659	250,652	332,517	
2015	653,182	11,625	274,294	367,263	
Total	\$ 12,694,871	\$ 3,908,243	\$ 2,066,472	\$ 6,720,156	

*Includes liabilities for pensions already granted and pensions incurred but not yet granted.

11.B. Non-Tabular Discounts

The non-tabular discount rate is made up of a benchmark rate less a risk adjustment rate, rounded to the nearest one-half percentage point. The benchmark rate is the five-year moving average of the U.S. 20-Year Treasury yield. The risk adjustment equals two percentage points until the benchmark rate reaches 4.0 percent. Below 4.0 percent, the risk adjustment is half the benchmark rate. As of June 30, 2015, the benchmark rate was 3.09 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.

The June 30, 2015, liabilities included \$8,482,409,000 of reserves for benefits and \$580,764,000 of reserves for claims administration expenses, net of tabular and non-tabular discounts. The amount of the non-tabular discounts for IBNR reserves was \$1,625,147,000, the amount for defense and cost containment (DCC) expense reserves was \$38,765,000, and the amount for adjusting and other (AO) expense reserves was \$21,964,000.

State of Washington Industrial Insurance Fund

The June 30, 2014, liabilities included \$8,447,374,000 of reserves for benefits and \$539,864,000 of reserves for claims administration expenses, net of tabular and non-tabular discounts. The amount of the non-tabular discounts for IBNR reserves was \$1,675,308,000, the amount of non-tabular discount for DCC expense reserves was \$37,267,000, and the non-tabular discount for AO expense reserves was \$19,426,000.

Liabilities Discounted on a Non-Tabular Basis*						
June 30, 2015						
(in thousands)						
Fiscal Accident Year	Benefit & CAE Liabilities Net of Tabular and Gross of Non-Tabular Discount	Non-Tabular Discounts				Benefit & CAE Liabilities Net of Tabular and Non- Tabular Discount
		Case	IBNR	DCC	AO	
2005 & Prior	\$ 2,511,000		\$ 505,200	\$ 10,666	\$ 2,638	\$ 1,992,496
2006	373,865		64,629	1,474	685	307,077
2007	488,746		80,296	1,837	976	405,637
2008	624,616		97,693	2,233	1,351	523,339
2009	660,474		101,319	2,333	1,467	555,355
2010	658,672		97,547	2,305	1,528	557,292
2011	687,857		98,448	2,389	1,646	585,374
2012	745,598		101,050	2,491	1,857	640,200
2013	1,002,845		129,016	3,264	2,553	868,012
2014	1,285,994		160,098	4,218	3,196	1,118,482
2015	1,709,382		189,851	5,555	4,067	1,509,909
Totals	\$ 10,749,049	\$ -	\$1,625,147	\$ 38,765	\$ 21,964	\$ 9,063,173

*Excludes liabilities for pensions already granted, but includes liabilities for pensions incurred but not yet granted.

Note 12 - Related Party Transactions

L&I administers the state's Workers' Compensation Program, including the Industrial Insurance Fund. It is an agency of the state of Washington; therefore, other Washington State agencies are related parties. Certain goods and services, such as attorney general legal services, information technology services, facilities management, building security, and cash and investment management services, are provided to L&I by other state agencies.

Total expenses incurred for goods and services provided by other Washington State agencies were \$49,196,899 in fiscal year 2015 and \$47,362,442 in fiscal year 2014. During fiscal years 2015 and 2014, 88.6 percent and 88.8 percent, respectively, of the total related party expenses were to the Attorney General's Office, the Department of Enterprise Services, and Consolidated Technology Services. Total amounts due to other state agencies were \$6,107,739 and \$6,218,924 at June 30, 2015 and 2014, respectively.

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

- **Board of Industrial Insurance Appeals** - hears appeals of decisions made by L&I
- **University of Washington** - promotes health and minimizes 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** - performs a performance audit of the workers' compensation claims management system

Total operating expenses incurred by these agencies in the Industrial Insurance Fund were \$26,784,019 and \$25,740,586 in fiscal years 2015 and 2014, respectively.

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

Note 13 - 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 14 - Capital and Contingency Reserve

14.A. Capital

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

14.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.

State of Washington Industrial Insurance Fund

For fiscal years 2015 and 2014, changes in the contingency reserve resulted from the following:

Explanation of Industrial Insurance Fund Operating and Investment Results		
(in thousands)		
	Fiscal Year 2015	Fiscal Year 2014
Contingency Reserve, July 1	\$ 949,521	\$ 619,562
Unexpected Investment Results		
Actual unrealized and realized gains (losses)		
Fixed income: unrealized gains (losses)	(5,132)	3,022
Equities: unrealized gains	28,823	333,602
TIPS: unrealized (losses)	-	(136,291)
Fixed income: realized gains	40,573	261,971
Equities: realized gains	18,087	41,213
Total actual unrealized and realized gains	82,351	503,517
Less expected gains	(76,230)	(95,800)
Total Unexpected Investment Results	6,121	407,717
Unexpected Insurance Operation Results		
Development of prior years' Loss and CAE liability	273,441	(266,985)
Development of prior years' Retro refund liability	(26,310)	(42,926)
Premium adequacy	22,369	232,153
Total Unexpected Insurance Operation Results	269,500	(77,758)
Change in contingency reserve	275,621	329,959
Contingency Reserve, June 30	\$ 1,225,142	\$ 949,521

The contingency reserve balances by account for fiscal years 2015 and 2014 were:

Contingency Reserve Balances				
by Account				
(in thousands)				
	Accident Account	Medical Aid Account	Pension Reserve Account	Total
Contingency Reserve, June 30, 2015	\$ 280,472	\$ 944,670	\$ -	\$ 1,225,142
Contingency Reserve, June 30, 2014	\$ 283,479	\$ 666,042	\$ -	\$ 949,521

Note 15 - 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 reserves related to asbestos or

environmental exposure claims are not specially reserved. IBNR and CAE 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.

Asbestos Claims		
	Fiscal Year 2015	Fiscal Year 2014
Beginning case reserve related to asbestos	\$ 50,539,979	\$ 50,746,260
Benefits incurred	547,171	6,831,078
Payments made	(6,671,997)	(7,037,359)
Ending case reserve related to asbestos	\$ 44,415,153	\$ 50,539,979

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

Note 16 - Subsequent Events

For the annual Statutory Financial Information Report as of June 30, 2015, an analysis of subsequent events has been evaluated through the report issuance date of December 31, 2015. The event described below existed after June 30, 2015.

16.A. Proposed Rate Announcement

Each year, the Director of L&I adopts new workers' compensation insurance premium rates for the next calendar year. On September 23, 2015, the Director announced a proposed 2 percent increase in the average premium rate for 2016. 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 2015 and go into effect on January 1, 2016.



Keep Washington Safe and Working

Supplementary Information



Keep Washington Safe and Working

State of Washington Industrial Insurance Fund

State of Washington Industrial Insurance Fund Schedule of Undiscounted Claims Development Information Fiscal Years 2006 through 2015 (in millions)

The table below illustrates how the Industrial Insurance Fund's earned revenues (net of reinsurance) and investment revenue 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 Industrial Insurance Fund has not purchased reinsurance since September 30, 2002, and has never had a qualifying event that generated a recovery.

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

	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015
Net earned required contribution and investment revenues	\$ 1,392	\$ 2,406	\$ 1,697	\$ 1,692	\$ 2,797	\$ 2,525	\$ 2,581	\$ 1,928	\$ 2,888	\$ 2,113
Estimated incurred claims and expenses, end of fiscal accident year	2,141	2,196	2,256	2,363	2,312	2,254	2,086	2,105	2,061	2,304
Paid (cumulative) as of:										
End of fiscal accident year	278	295	310	322	298	289	284	296	297	301
One year later	589	625	679	667	604	584	580	593	613	
Two years later	754	817	890	863	773	747	734	755		
Three years later	873	953	1,042	1,000	890	857	840			
Four years later	964	1,059	1,162	1,107	981	940				
Five years later	1,038	1,144	1,258	1,192	1,054					
Six years later	1,103	1,216	1,337	1,262						
Seven years later	1,159	1,281	1,406							
Eight years later	1,210	1,340								
Nine years later	1,256									
Re-estimated incurred claims and expenses: *										
End of fiscal accident year	2,141	2,196	2,256	2,363	2,312	2,254	2,086	2,105	2,061	2,304
One year later	2,053	2,234	2,559	2,535	2,271	2,139	2,026	2,001	2,175	
Two years later	2,055	2,390	2,647	2,538	2,261	2,066	1,967	2,036		
Three years later	2,151	2,441	2,724	2,485	2,137	2,012	1,878			
Four years later	2,196	2,526	2,662	2,411	2,147	1,986				
Five years later	2,244	2,445	2,576	2,439	2,137					
Six years later	2,198	2,388	2,621	2,439						
Seven years later	2,186	2,419	2,625							
Eight years later	2,183	2,421								
Nine years later	2,163									
Increase (decrease) in estimated incurred claims and expenses from end of policy year **	22	225	369	76	(175)	(268)	(208)	(69)	114	
Percentage change in estimated incurred claims and expenses	1%	10%	16%	3%	-8%	-12%	-10%	-3%	6%	

Source: Washington State Department of Labor & Industries Actuarial Services

* Re-estimated claims and expenses result from new information received on known claims, re-evaluation of existing information on known claims, and emergence of new claims not previously known.

** This line compares the latest re-estimated incurred claims amount to the amount originally established 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 more recent fiscal accident years.

**Supplemental Investment Risk Interrogatories
June 30, 2015**

1. The Industrial Insurance Fund's total admitted assets as reported on page 29 of this annual Statutory Financial Information Report were \$14,820,102,000 at June 30, 2015.
2. The 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 as exempt in the Appendix to the SVO's *Practices and Procedures Manual* (ii) property occupied by the Industrial Insurance Fund, and (iii) policy loans:

	Amount	Percentage of Total Admitted Assets
Bonds - Freddie Mac	\$ 708,333,000	4.78%
Bonds - Fannie Mae	437,734,000	2.95%
Bonds - Citibank Credit Card Issuance	152,954,000	1.03%
Bonds - Asian Development Bank	145,912,000	0.98%
Bonds - JPMorgan Chase & Co	114,975,000	0.78%
Bonds - Citigroup Inc	113,942,000	0.77%
Bonds - Burlington Northern Santa Fe	110,813,000	0.75%
Bonds - Citigroup Commercial Mortgage	107,498,000	0.73%
Bonds - Trans-Canada Pipelines	106,656,000	0.72%
Bonds - Norfolk Southern Corp	105,385,000	0.71%

3. The Industrial Insurance Fund's total admitted assets held in bonds and preferred stocks, by NAIC designation, including bonds classified as short-term investments at June 30, 2015, were:

	Amount	Percentage of Total Admitted Assets
Bonds with an NAIC designation of 1	\$ 8,553,914,000	57.72%
Bonds with an NAIC designation of 2	3,467,901,000	23.40%
Bonds with an NAIC designation of 3	95,696,000	0.65%

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, 2015**

Total admitted assets held in foreign investments at June 30, 2015:

<u>Asset Type</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
Bonds	\$ 3,403,038,000	22.96%
Equities	695,000,000	4.69%

Total admitted assets held in foreign investments in bonds by NAIC rating at June 30, 2015:

<u>NAIC Designation</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
Countries designated NAIC – 1	\$ 2,058,164,000	13.89%
Countries designated NAIC – 2	773,639,000	5.22%
Countries designated NAIC – 3	571,234,000	3.85%

Two countries with the largest foreign investment exposure in each NAIC designation at June 30, 2015:

<u>Issuer</u>	<u>NAIC Designation</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
Australia	1	\$ 457,656,000	3.09%
Cayman Islands	1	441,110,000	2.98%
Brazil	2	229,413,000	1.55%
Indonesia	2	144,888,000	0.98%
SupraNational	3 or below	380,399,000	2.57%
Korea (South)	3 or below	182,448,000	1.23%

**Supplemental Investment Risk Interrogatories
June 30, 2015**

Ten largest non-sovereign (i.e., non-governmental) investments held in foreign issues at June 30, 2015:

<u>Issuer</u>	<u>NAIC Designation</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
Vale Overseas Limited	2	\$ 83,758,000	0.57%
National Australia Bank	1	64,994,000	0.44%
Alibaba Group Holding Ltd	1	64,726,000	0.44%
Petroleos Mexicanos	2	63,883,000	0.43%
Siemens Financieringsmat	1	59,935,000	0.40%
Petronas Capital Ltd	1	59,264,000	0.40%
National Australia Bank Ltd	1	54,983,000	0.37%
State Grid Overseas Inv	1	54,332,000	0.37%
Aust & NZ Banking Group	1	53,991,000	0.36%
DBS Bank Ltd/Singapore	1	49,998,000	0.34%

- | | <u>Amount</u> | <u>Percentage of Total
Admitted Assets</u> |
|--|-----------------|--|
| 5. Total admitted assets held in Canadian investments | \$1,252,763,000 | 8.45% |
| 6. The Industrial Insurance Fund had no investments with <i>contractual sales restrictions</i> , which are defined as “investments having restrictions that prevent investments from being sold within 90 days.” | | |
| 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 <i>Practices and Procedures Manual</i> , as exempt, or Class 1, were: | | |

<u>Fund</u>	<u>Amount</u>	<u>Percentage of Total Admitted Assets</u>
Blackrock MSCI U.S. IMI Index	\$ 1,182,983,000	7.98%
MSCI EAFE Index SL CTF	440,763,000	2.97%
MSCI Emerging Markets Free IND	135,222,000	0.91%
MSCI Small Cap Index (Provisio)	66,920,000	0.45%
Canada MSCI CTF	41,658,000	0.28%
MSCI Equity Index Fund	21,570,000	0.15%
MSCI Canada Small Cap	6,629,000	0.04%

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

Supplemental Investment Risk Interrogatories
June 30, 2015

8. The Industrial Insurance Fund did not hold any non-affiliated, 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, 2015.
14. The Industrial Insurance Fund did not own any warrants not attached to other financial instruments, options, caps, or floors at June 30, 2015.
15. The Industrial Insurance Fund did not have any exposure for collars, swaps, or forwards during fiscal year 2015.
16. The Industrial Insurance Fund did not have any potential exposure for futures contracts during fiscal year 2015.

State of Washington Industrial Insurance Fund

Summary Investment Schedule June 30, 2015

The Industrial Insurance Fund held cash and invested assets as of June 30, 2015, consisting of the following:

	Gross investment holding		Admitted assets as reported in the annual statement			
	Amount	Percentage	Securities Lending Reinvested			
			Amount	Collateral Amount	Total Amount	Percentage
Bonds:						
U.S. Treasury securities	\$ 1,165,527,000	8.21%	\$ 1,165,527,000	\$ -	\$ 1,165,527,000	8.21%
U.S. Government agency and corporate obligations (excluding mortgage-backed securities)	-	0.00%	-		-	0.00%
Foreign government (including Canada, excluding mortgage-backed securities)	1,300,556,000	9.16%	1,300,556,000	-	1,300,556,000	9.16%
Mortgage-backed securities (includes residential and commercial mortgage-backed securities)						
Issued or guaranteed by GNMA	56,234,000	0.40%	56,234,000	-	56,234,000	0.40%
Issued or guaranteed by FNMA, FHLMC	1,146,066,000	8.07%	1,146,066,000	-	1,146,066,000	8.07%
Issued or guaranteed by all other	396,493,000	2.79%	396,493,000	-	396,493,000	2.79%
Other fixed income securities (excluding short-term):						
Unaffiliated domestic securities	4,579,529,000	32.24%	4,579,529,000	-	4,579,529,000	32.24%
Unaffiliated foreign securities	3,364,250,000	23.68%	3,364,250,000	-	3,364,250,000	23.68%
Equity interests:						
Commingled index funds - domestic	1,182,983,000	8.33%	1,182,983,000	-	1,182,983,000	8.33%
Commingled index funds - foreign	712,763,000	5.02%	712,763,000	-	712,763,000	5.02%
Real estate investments:						
Property occupied by company	-	0.00%	-	-	-	0.00%
Property held for production of income	-	0.00%	-	-	-	0.00%
Receivables for securities and interest	112,026,000	0.79%	112,026,000	-	112,026,000	0.79%
Cash and cash equivalents	11,385,000	0.08%	11,385,000	46,531,000	57,916,000	0.41%
Securities lending collateral	68,406,000	0.48%	-	-	-	0.00%
Short-term investments	108,857,000	0.77%	108,857,000	21,875,000	130,732,000	0.92%
Total	\$14,205,075,000	100.00%	\$14,136,669,000	\$ 68,406,000	\$ 14,205,075,000	100.00%

Independent Actuarial Opinion



Keep Washington Safe and Working

October 2, 2015

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 reserves as of June 30, 2015.

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, 2015. 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 adjustment expense obligations of the Fund under the terms of its contracts and agreements.

Relevant Comments

A. Risk of Material Adverse Deviation

With respect to this Statement of Actuarial Opinion, the amount of adverse deviation that I consider to be material is \$245.0 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. 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.

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, and future cost of living adjustments. 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 3.46%. 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, \$1.23 billion, relative to the size of its loss and loss adjustment expense reserve, \$13.24 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, although the Fund’s leverage ratio has been declining in recent years.

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.

The Fund is exposed to the uncertainty of variability of the reserves which could result in material adverse deviation. At this time, my assessment is that the Fund has a significant risk of a material adverse deviation.

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 selected annual interest rates as follows.

- 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 6.4%.
- For the Accident Account, combinations of interest rates are 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 6.4% for the remaining months of calendar year 2015. This rate is reduced to 6.25% for calendar year 2016 and then is gradually reduced each additional calendar year by 0.25% for the following seven calendar years until settling on a long term annual rate of 4.5%. 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 3.46% 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 Pension Reserve Account changed from 6.5% last year to 6.4% this year. The interest rate used to discount the Accident Account future fatal transfers made to the Pension Account changed from 6.5% last year to the interest rates that gradually decrease to 4.5% discussed above. The effect of reducing these interest rate assumptions this year was an increase in the discounted unpaid claim liability of \$36.9 million.

We note that the interest rate used to discount the Accident Account future total permanent disability transfers made to the Pension Account remains unchanged this year. Although, the rate at which the interest rates gradually decrease to 4.5% changed this year causing the discounted unpaid claim liability to decrease \$18.5 million. The interest rate used for all other future payments remained the same this year at 1.5%.

The net effect of all the interest rate assumption changes combined this year was an increase in the discounted unpaid claim liability of \$18.4 million including the current fiscal accident year.

Major Assumption Changes

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, 2014. The reduction was the result of the closing of more of the active time loss claims than was expected over the past year and using more recent averages in the selection of claim development factors to reflect more recent history. The effect of reducing this estimate was a decrease in the discounted unpaid claim liability of approximately \$135.3 million. We note that this decrease only accounts for the change in estimate of the number of total permanent disability claims for accident periods prior to June 30, 2014.

This year, the Department changed mortality assumptions used to estimate the unpaid claim liabilities. In the prior year mortality assumptions relied on annuity factors, developed in 1987, based on the 1980 decennial mortality tables published by the US census. In 2014, the Department performed a study to update the mortality tables and annuity factors. Deloitte Consulting performed a review of these new mortality assumptions and concluded that they were reasonable in a June 10, 2014 report provided to the State Auditor's Office. These updated mortality assumptions are used in the current year estimate of the unpaid claim liabilities. The updated mortality tables and annuity factors caused the discounted reserves to increase as follows:

Effect of change in Mortality Tables and Annuity Factors:

Accident Account:	\$ 48.0 million
Medical Aid Account:	\$ 47.1 million
<u>Pension Reserve Account:</u>	<u>\$ 70.2 million</u>
Total:	\$165.3 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 loss adjustment expense reserves and is only to be relied upon by the Fund and the State.



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October 2, 2015

Statement of Actuarial Opinion – Year Ended June 30, 2015

State of Washington Industrial Insurance Fund

Exhibit A: SCOPE

<u>Loss Reserves:</u>	<u>Amount</u>
A. Net of Reinsurance Reserve for Unpaid Losses	\$12,660,158,000
B. Net of Reinsurance Reserve for Unpaid Loss Adjustment Expenses	<u>\$ 580,764,000</u>
Total Net Loss and Loss Adjustment Expenses Reserves	\$13,240,922,000
C. Reserve of Unpaid Losses – Direct and Assumed	\$12,660,158,000
D. Reserve for Unpaid Loss Adjustment Expenses – Direct and Assumed	<u>\$ 580,764,000</u>
Total Gross Loss and Loss Adjustment Expense Reserves	\$13,240,922,000
E. Retroactive Reinsurance Reserve Assumed	\$0
F. Other Loss Reserve items on which the Appointed Actuary is expressing an Opinion	\$0
<u>Premium Reserves:</u>	
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, 2015

State of Washington Industrial Insurance Fund

Exhibit B: DISCLOSURES

<u>Item:</u>	<u>Column 1</u>	<u>Column 2</u>	<u>Column 3</u>	<u>Column 4</u>
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.)	\$245,041,400			
6. Is there a Significant Risk of Material Adverse Deviation? YES or NO				YES [X] NO []
7. Statutory Surplus (Contingency Reserve)	\$1,225,207,000			

Statement of Actuarial Opinion – Year Ended June 30, 2015

State of Washington Industrial Insurance Fund

Exhibit B: DISCLOSURES

<u>Item:</u>	<u>Column 1</u>	<u>Column 2</u>	<u>Column 3</u>	<u>Column 4</u>
8. Discount included as a reduction to loss reserves and loss expense reserves as reported in Schedule P				
8.1 Non-tabular Discount	\$1,685,876,000			
8.2 Tabular Discount	\$5,974,714,000			
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			



Keep Washington Safe and Working

***State of Washington Industrial Insurance Fund
Statutory Financial Information Report***

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