



Financial Statements
June 30, 2016 and 2015

Workforce Safety & Insurance

WORKFORCE SAFETY & INSURANCE

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Independent Auditor's Report

To the Board of Directors
Workforce Safety & Insurance
Bismarck, North Dakota

Report on the Financial Statements

We have audited the accompanying financial statements of the business-type activities of Workforce Safety & Insurance, a department of the State of North Dakota, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise Workforce Safety & Insurance's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the business-type activities of Workforce Safety & Insurance, as of June 30, 2016 and 2015, and the changes in financial position and cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of Matter

As discussed in Note 1, the financial statements of Workforce Safety & Insurance, an agency of the State of North Dakota are intended to present the financial position, the changes in financial position and cash flows of only that portion of the business-type activities of the State of North Dakota that is attributable to the transactions of Workforce Safety & Insurance. They do not purport to, and do not, present fairly the financial position of the State of North Dakota as of June 30, 2016 and 2015, the changes in its financial position, or its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matters

Required Supplementary Information

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

Other Information

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise Workforce Safety & Insurance's financial statements. The loss development information and schedule of attorney fees and costs are presented for purposes of additional analysis and are not a required part of the financial statements.

The loss development information and schedule of attorney fees and costs are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic 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 basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 11, 2016 on our consideration of Workforce Safety & Insurance's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering Workforce Safety & Insurance's internal control over financial reporting and compliance.

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

Fargo, North Dakota
October 11, 2016

WORKFORCE SAFETY & INSURANCE

MANAGEMENT'S DISCUSSION AND ANALYSIS

YEARS ENDED JUNE 30, 2016 AND 2015

Workforce Safety & Insurance (WSI) was established in 1919 with the purpose of providing workers compensation insurance for employers, state agencies and other governmental units working in North Dakota. WSI operates in a manner similar to any other insurance company, but is also an agency of the State of North Dakota. As management of WSI, we offer readers of these financial statements a narrative overview and analysis of WSI's financial activities for the fiscal years ended June 30, 2016, 2015, and 2014. We encourage readers to consider the information presented here in conjunction with the entire financial statement package and the notes to those statements, which follow this section.

WSI is a proprietary fund and uses the accrual basis of accounting. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. WSI, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. WSI is a special government reporting unit for the State of North Dakota and is combined with other similar funds to comprise the enterprise funds of the State of North Dakota.

Overview of Financial Statements

WSI's basic financial statements include the 1) balance sheet, 2) statement of revenues, expenses and changes in fund net position, 3) statement of cash flows, and 4) statement of appropriations. The balance sheet provides readers the assets, deferred outflows of resources, liabilities and deferred inflows of resources of the fund, with the difference between the two considered net position. It also provides the basis for determining the overall financial strength and solvency of the workers compensation fund. The statement of revenues, expenses and changes in fund net position shows the operating performance of WSI for the fiscal year. The statement of cash flows identifies cash flows from operating activities, non-capital financing activities, capital and related financing activities, and investing activities. The statement of cash flows answers questions such as where did the cash come from, what was cash used for, and what was the change in the cash balance during the fiscal year. The statement of appropriations shows WSI's expenditures in relationship to the biennial appropriation approved by the 2015 Legislative Assembly.

WSI's notes to the financial statements provide readers additional information that is essential to a full understanding of data provided in the fund financial statements. The notes can be found on pages 16-40 of this report. In addition to the basic financial statements and accompanying notes, this report also presents required supplemental pension liability and contribution schedules on page 41. Other supplementary information concerning WSI's loss development and WSI's legal costs can be found on page 42-43.

WSI implemented the new GASB Statement No. 68, Accounting and Financial Reporting for Pensions, which requires governmental agencies to report their proportionate share of pension expense and liabilities. This statement was implemented into the fiscal year 2015 financial statement. Prior year financial reports were not restated, as detailed information is not available for the prior years. Due to this change, the financial report for fiscal year 2014 will not tie out to the fiscal year 2015 report in all areas. Areas of difference will be noted on each report.

Financial Highlights

Reduced activity in the energy and other related industries are reflected in WSI's book of business. Fiscal year 2016 shows reductions in earned premiums and incurred losses, relating to both a decreased number of policyholders and filed claims.

MANAGEMENT'S DISCUSSION AND ANALYSIS

At June 30, 2016, June 30, 2015, and June 30, 2014 coverage extended to the following employers:

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Annual premium \$250 - \$5,000	17,835	18,297	18,798
Annual premium \$5,001 - \$50,000	5,654	6,067	5,562
Annual premium \$50,001 - \$100,000	572	588	533
Annual premium over \$100,000	517	568	496
	<u>24,578</u>	<u>25,520</u>	<u>25,389</u>
Total policyholders	<u>24,578</u>	<u>25,520</u>	<u>25,389</u>

North Dakota's active policyholder count decreased by 942 policies in fiscal year 2016, ending with a total of 24,578 policies. Fiscal year 2015's total of 25,520 reflects an increase of 131 policyholders over the fiscal year 2014 total of 25,389. The decline in policies is due to the weaker economic conditions in the State.

Condensed Statements of Revenue & Expenses

	<u>2016</u>	<u>2015</u>	<u>2014</u>
REVENUE			
OPERATING REVENUE			
Premium-net of discount and reinsurance premium	\$ 291,244,452	\$ 329,690,311	\$ 313,164,770
Subrogation, penalties and finance charges	11,531,180	9,013,590	4,843,628
Building rental revenue	851,446	753,022	742,222
Other revenue (Note 24)	5,055,698	349,773	29,215
	<u>308,682,776</u>	<u>339,806,696</u>	<u>318,779,835</u>
NONOPERATING REVENUE			
Earnings on investments	69,501,734	60,172,170	184,144,392
Total revenues	<u>378,184,510</u>	<u>399,978,866</u>	<u>502,924,227</u>
EXPENSES			
OPERATING EXPENSES			
Incurred losses and loss adjustment expenses	197,467,710	248,084,909	292,047,713
Payroll and employee benefits	23,533,739	21,509,627	20,935,411
Other administrative expenses	1,165,833	1,865,241	1,697,116
Pension expenses	581,854	619,152	-
Bad debt expenses	1,977,037	3,120,914	3,126,998
Depreciation expenses	398,680	372,402	1,003,191
	<u>225,124,853</u>	<u>275,572,245</u>	<u>318,810,429</u>
NONOPERATING EXPENSE			
Investment and other expenses	4,724,205	4,409,843	4,187,034
Dividend expenses	136,968,985	97,925,896	95,557,186
	<u>141,693,190</u>	<u>102,335,739</u>	<u>99,744,220</u>
Total expenses	<u>366,818,043</u>	<u>377,907,984</u>	<u>418,554,649</u>
Change in net position	<u>\$ 11,366,467</u>	<u>\$ 22,070,882</u>	<u>\$ 84,369,578</u>

(continued on next page)

MANAGEMENT'S DISCUSSION AND ANALYSIS

WSI's financial position remains stable. Earned premium net of discounts and reinsurance totaled \$291 million, \$330 million, and \$313 million for fiscal years 2016, 2015, and 2014, respectively.

Written premium for fiscal year 2016 totals \$310.3 million, a 17% decrease from 2015's total of \$372.6 million. Fiscal year 2015's total written premium was 6% higher than fiscal year 2014's amount of \$350.2 million.

In fiscal year 2016, WSI's investment portfolio yielded a year to date return of 3.58% (net of fees), with a gain of \$69.5 million before expenses. The year-to-date return for fiscal years 2015 and 2014 was 3.27% and 11.71%, respectively. WSI's average investment return for the five year period ending June 30, 2016 is 6.56% and the average ten year rate of return is 5.66%. WSI's estimated reserve liabilities are currently discounted at 5.0%.

WSI re-entered the Securities Lending arena in fiscal year 2016. Total income for the year was \$213,849 with related expense of \$42,729.

In fiscal year 2016, the WSI Board of Directors recommended issuing a 50% dividend credit in accordance with North Dakota Century Code (NDCC) 65-04-02. The Governor of North Dakota approved this recommendation. This dividend credit is estimated to be \$150 million and will be applied to renewing policyholders in good standing in accordance with NDCC 65-04-02. This is comparable to the 30% dividend credit declared in fiscal year 2015, and the 39% dividend credit declared in fiscal year 2014, which were estimated at \$100 million and \$115 million, respectively. WSI issued dividend credits in eleven of the past twelve years, totaling approximately \$1.08 billion.

WSI's premium billings are estimated annually based upon the employer's prior year's estimated payroll. At the end of each year, payroll reports are submitted and reviewed for accuracy. The billing is then adjusted to reconcile with actual prior year payroll reports. As estimates are reconciled to actual amounts and premiums are adjusted, dividend estimates that were derived from estimated premium are also adjusted.

The estimated dividend credit declared in June of 2016 was \$150 million dollars. The actual dividend expense booked in fiscal year 2016 was decreased by \$13.1 million, due to decreases in the estimated residual amount from the dividend credit estimates from fiscal year 2015 and 2014. The fiscal year 2015 dividend credit estimate was reduced by \$9 million and the fiscal year 2014 dividend credit estimate was reduced by \$4 million. The bulk of this residual was due to lower premiums as economic conditions slowed.

Incurred loss and LAE were \$197 million in fiscal year 2016, a decrease of 20% or \$50.6 million less than the \$248 million reported in fiscal year 2015. Incurred losses in fiscal year 2015 were \$44 million or 15% less than the incurred loss amount of \$292 million in fiscal year 2014. These decreases are a result of both the economic slowdown of oil production activity in the state and WSI's continued efforts to promote safety education.

The number of total claims filed in fiscal year 2016 was also less than in fiscal year 2015 and 2014. Total claims filed in fiscal year 2016 totaled 21,250. This is 3,548 or 14% less than the 24,798 total claims filed in fiscal year 2015. The total number of claims filed in fiscal year 2015 was previously reported as 24,767. This amount was adjusted as it increased by 31 claims, likely due to some claims being delayed in the registration process for various reasons. Fiscal year 2015 claims decreased by 1,597 claims or 6% less than the total claims filed in fiscal year 2014 of 26,395. WSI contributes these decreases to both the reduced activity in the energy industry, and WSI's continued commitment to safety education and injury prevention programs.

As oil production activity has slowed and some companies have left the state, new challenges have arisen in debt collection. WSI is contracting with a third party collection agency to address these challenges. Actual premium bad debt expense was \$1.7 million for fiscal year 2016, \$1.4 million for fiscal year 2015, and \$638 thousand for fiscal year 2014.

MANAGEMENT'S DISCUSSION AND ANALYSIS

WSI contracted with a collection agency, Access Receivables, in March 2015, to assist with delinquent premium account collection. During the earlier part of fiscal year 2015 and fiscal year 2014, WSI had contracted with The Affiliated Group, another collection agency, to assist with collections on delinquent accounts. The ratio of total delinquent accounts to in-force premium ranges from 2.7% to 3.7% over the past three fiscal years, with the current year being the largest.

Total accounts not making payments has increased to \$10.4 million in fiscal year 2016. This is a 21% increase or \$1.8 million more than the fiscal year 2015 total of \$8.6 million. The \$8.6 million in fiscal year 2015 was an increase of 30% over the fiscal year 2014 total of \$6.6 million.

Delinquent premium in active collections increased to \$12.9 million in fiscal year 2016, an increase of \$1.6 million or 14% over the fiscal year 2015 total of \$11.3 million. The fiscal year 2015 total of \$11.3 million was 31% or \$2.7 million higher than the fiscal year 2014 total of \$8.6 million. No change was made to the allocation for premium bad debt expense in fiscal year 2016. This allocation was increased from \$6 million to \$7.5 million in fiscal year 2015, and from \$4 million to \$6 million in fiscal year 2014.

The allocation for other bad debt expense remained at \$2,000,000, based on an analysis of the total amount outstanding. Actual other bad debt expense for fiscal year 2016 totaled \$273 thousand, compared to \$203 thousand in fiscal year 2015 and \$489 thousand in fiscal year 2014.

The net position as of June 30, 2016 equaled \$466 million compared to \$455 million on June 30, 2015 and \$439 million on June 30, 2014. The net position as of June 30, 2016 represents approximately 40.3% of the actuarial discounted reserve liability of \$1.112 billion, compared to the net position as of June 30, 2015, which stood at approximately 41.5% of the actuarial discounted reserve liability of \$ 1.096 billion and the net position on June 30, 2014, which totaled 41.7% of the actuarial discounted reserve liability of \$1.053 billion.

Condensed Statements of Change in Net Position

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Beginning net position, as restated	\$ 454,782,551	\$ 432,711,669	\$ 354,758,275
Change in net position	<u>11,366,467</u>	<u>22,070,882</u>	<u>84,369,578</u>
Ending net position	<u>\$ 466,149,018</u>	<u>\$ 454,782,551</u> **	<u>\$ 439,127,853</u>

** The ending net position in fiscal year 2014 of \$439.1 million is \$6.4 million more than the beginning net position in fiscal year 2015. This variance is due to the implementation of GASB 68 as discussed on page 4 in the "Overview of the Financial Statements" and Note 16. This \$ 6.4 million is the agency's estimated, pro-rated share of outstanding pension liability that has accrued over the years. This amount is being recorded in fiscal year 2015.

MANAGEMENT'S DISCUSSION AND ANALYSIS

	Condensed Balance Sheets		
	2016	2015	2014
ASSETS			
CURRENT ASSETS			
Cash and cash equivalents	\$ 2,009,802	\$ 2,448,255	\$ 3,082,594
Investments	1,822,483,705	1,753,102,799	1,692,463,156
Invested securities lending collateral	17,214,543	-	-
Premium receivables, net	40,153,603	47,304,062	49,319,201
Other accounts receivable, net	6,127,150	4,739,646	5,287,596
Investment interest receivable	9,667,915	9,591,339	11,574,574
Prepaid expenses	316,513	536,921	357,509
Total current assets	<u>1,897,973,231</u>	<u>1,817,723,022</u>	<u>1,762,084,630</u>
NON-CURRENT ASSETS			
Premises, furniture and equipment	<u>11,888,286</u>	<u>10,355,807</u>	<u>10,648,689</u>
Total assets	<u>1,909,861,517</u>	<u>1,828,078,829</u>	<u>1,772,733,319</u>
DEFERRED OUTFLOWS OF RESOURCES			
Deferred outflow pension	<u>892,196</u>	<u>822,588</u>	<u>-</u>
TOTAL ASSETS AND DEFERRED OUTFLOWS	<u><u>\$ 1,910,753,713</u></u>	<u><u>\$ 1,828,901,417</u></u>	<u><u>\$ 1,772,733,319</u></u>
LIABILITIES			
CURRENT LIABILITIES			
Accounts payable	6,944,404	6,729,959	5,911,293
Unearned premium	144,577,275	160,329,226	152,954,059
Dividend payable	156,837,761	103,055,204	121,733,101
Securities lending collateral	17,214,543	-	-
Unpaid loss and LAE	<u>133,408,574</u>	<u>131,600,880</u>	<u>126,336,720</u>
Total current liabilities	458,982,557	401,715,269	406,935,173
NONCURRENT LIABILITIES			
Compensated absences, net	215,619	202,162	201,013
Pension liability	6,282,403	5,953,413	-
Unpaid Loss & LAE, discounted 5%	<u>978,329,541</u>	<u>965,073,120</u>	<u>926,469,280</u>
Total non-current liabilities	984,827,563	971,228,695	926,670,293
Total Liabilities	1,443,810,120	1,372,943,964	1,333,605,466
DEFERRED INFLOWS OF RESOURCES			
Deferred Inflow Pension	794,575	1,174,902	-
NET POSITION			
Invested in capital assets	11,888,286	10,355,807	10,648,689
Designated/Unrestricted	<u>454,260,732</u>	<u>444,426,744</u> **	<u>428,479,164</u>
Total net position	<u>466,149,018</u>	<u>454,782,551</u>	<u>439,127,853</u>
TOTAL LIABILITIES, DEFERRED INFLOWS AND NET POSITION	<u><u>\$ 1,910,753,713</u></u>	<u><u>\$ 1,828,901,417</u></u>	<u><u>\$ 1,772,733,319</u></u>

* Reader should note the beginning net position for fiscal year 2015 was reduced by approximately \$6.4 million from the \$439.1 million stated as fiscal year 2014's ending net position. This adjustment was made to implement GASB Statement No. 68. See Note 16.

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MANAGEMENT'S DISCUSSION AND ANALYSIS

WSI's total assets and deferred outflows of resources as of June 30, 2016 totaled \$1.91 billion. This is an increase of 4.5% or \$81.8 million. Total assets on June 30, 2015 of \$1.83 billion increased \$60 million or 3.4% over total assets on June 30, 2014 of \$1.77 billion. Variances in total assets year over year are due to investment market fluctuations, reduced premium based on economic changes, premium rate modifications, changes in incurred losses, and the issuance of premium dividend credits. The difference between assets and liabilities is reported on the balance sheet as net position, which is commonly referred to as fund surplus.

Changes in net position are the result of two separate activities or major program revenues: underwriting and investing. Underwriting activities measure annual premium revenues against claims costs and administrative expenses; while investing activities measure interest, dividends and changes in the fair value of WSI's investments. WSI's investing activities are designed to support its underwriting results and so, to the extent that investments appreciate in value, WSI can operate with an underwriting loss and still maintain its financial strength.

Fiscal year 2016 activities resulted in underwriting revenue of \$69 million, an increase of approximately \$15 million over fiscal year 2015. The fiscal year 2015 underwriting activity resulted in a gain of \$54.1 million which was \$59.8 million more than the underwriting loss of \$5.6 million stated in fiscal year 2014.

The change in net position in fiscal year 2016 of \$11.4 million is 48% lower than the \$22.1 million gain in fiscal year 2015. A dividend credit of 50% was declared in fiscal year 2016, vs. a 30% credit in fiscal year 2015. Net earned premium decreased by \$38 million, almost 12%. The uptick in investment return of \$13.5 million in fiscal year 2016 was helpful in maintaining a positive change in net position. In fiscal year 2014, the strong investment return helped contribute to the change in net position of \$84.4 million.

Condensed Underwriting and Investment Analysis

	<u>2016</u>	<u>2015</u>	<u>2014</u>
Net premium earned	\$ 291,244,452	\$ 329,690,311	\$ 313,164,770
Incurring losses	179,428,887	230,705,448	276,448,829
Allocated loss adjustment expenses	6,711,210	6,898,127	5,377,918
Unallocated loss adjustment expenses	11,327,613	10,481,334	10,220,966
General and administrative expenses	24,187,960	26,868,184	26,762,717
Pension expenses	<u>581,854</u>	<u>619,152</u>	<u>-</u>
Total losses and expenses	222,237,524	275,572,245	318,810,430
Underwriting income (loss)	69,006,928	54,118,066	(5,645,660)
Investment and other income	79,328,524	65,878,712	185,572,423
Dividend expenses	<u>(136,968,985)</u>	<u>(97,925,896)</u>	<u>(95,557,186)</u>
Change in net position	<u>\$ 11,366,467</u>	<u>\$ 22,070,882</u>	<u>\$ 84,369,577</u>

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MANAGEMENT'S DISCUSSION AND ANALYSIS

Capital Assets

WSI's non-current assets include land, the Century Center office building, furniture, and equipment. A statement of changes in capital assets for fiscal year 2016, 2015, and 2014 can be found under Note 5 – Capital Assets.

Economic Factors and Next Year's Budget and Rates

WSI is a proprietary enterprise fund and does not receive any general fund dollars. Workers compensation premium and investment returns are the main sources of revenue. To ensure solvency of the fund, premium rates are actuarially established on an annual basis by external actuarial consultants. For policy year 2016, WSI anticipates average statewide premium levels to decrease by approximately 2.5%. This compares to the policy year 2015 increase of 4.8% and policy year 2014 increase of 1.3%.

Available Fund Surplus

The 2009 Legislative Assembly revised the language regarding fund surplus requirements outlined in NDCC 65-04-02, adding clarifying parameters for determining the amount of net position, or surplus, to be considered available for dividend declaration. This language allows the net position to be reduced by special project funding which has been legislatively approved, to arrive at available surplus. Following these guidelines, the available surplus as of June 30, 2016 was \$442.8 million or 39.8% of the actuarial discounted reserve liability of \$1.112 billion. As of June 30, 2015 and June 30, 2014, the available surplus was 38.9% and 39.2%, respectively.

WORKFORCE SAFETY & INSURANCE
BALANCE SHEETS
YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 2,009,802	\$ 2,448,255
Investments	1,822,483,705	1,753,102,799
Invested securities lending collateral	17,214,543	-
Premium receivable, net	40,153,603	47,304,062
Due from other funds	-	13
Other accounts receivable, net	6,127,150	4,739,633
Investment interest receivable	9,667,915	9,591,339
Prepaid expenses	316,513	536,921
Total current assets	<u>1,897,973,231</u>	<u>1,817,723,022</u>
NONCURRENT ASSETS		
Land	901,974	901,974
Capital assets, net	10,393,691	9,453,833
Construction in progress	592,621	-
Total assets	<u>1,909,861,517</u>	<u>1,828,078,829</u>
DEFERRED OUTFLOWS OF RESOURCES		
Deferred Outflow Pension	892,196	822,588
TOTAL ASSETS AND DEFERRED OUTFLOWS OF RESOURCES	<u><u>\$ 1,910,753,713</u></u>	<u><u>\$ 1,828,901,417</u></u>
LIABILITIES		
CURRENT LIABILITIES		
Accounts payable	\$ 4,400,732	\$ 3,966,827
Due to other state agencies	198,631	202,604
Unearned premium	144,577,275	160,329,226
Dividend payable	156,837,761	103,055,204
Compensated absences payable	1,324,517	1,241,855
Investment accounts payable	1,020,524	1,318,673
Securities lending collateral	17,214,543	-
Unpaid loss and LAE	133,408,574	131,600,880
Total current liabilities	<u>458,982,557</u>	<u>401,715,269</u>
NONCURRENT LIABILITIES		
Compensated absences payable, net of current	215,619	202,162
Pension Liability	6,282,403	5,953,413
Unpaid loss and LAE, discounted at 5%	978,329,541	965,073,120
Total non-current liabilities	<u>984,827,563</u>	<u>971,228,695</u>
Total liabilities	<u>1,443,810,120</u>	<u>1,372,943,964</u>
DEFERRED INFLOWS OF RESOURCES		
Deferred inflow pension	794,575	1,174,902
NET POSITION		
Invested in capital assets, net of related debt	11,888,286	10,355,807
Designated/Unrestricted	454,260,732	444,426,744
Total net position	<u>466,149,018</u>	<u>454,782,551</u>
Total liabilities and net position	<u>1,909,959,138</u>	<u>1,827,726,515</u>
TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION	<u><u>\$ 1,910,753,713</u></u>	<u><u>\$ 1,828,901,417</u></u>

WORKFORCE SAFETY & INSURANCE
STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN FUND NET
POSITION YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
OPERATING REVENUES		
Net premiums earned	\$ 291,244,452	\$ 329,690,311
Penalties and finance charges	3,997,490	3,874,619
Third party subrogation recoveries	7,533,690	5,138,971
Rental operations	851,446	753,022
Other Revenue (Note 24)	<u>5,055,698</u>	<u>349,773</u>
Total operating revenues	<u>308,682,776</u>	<u>339,806,696</u>
OPERATING EXPENSES		
Incurred losses and loss adjustment expenses	197,467,710	248,084,909
Payroll and benefits	23,533,739	21,509,627
Pension expenses	581,854	619,152
Other administrative expenses	1,165,833	1,865,241
Bad debt expense	1,977,037	3,120,914
Depreciation expense	<u>398,680</u>	<u>372,402</u>
Total operating expenses	<u>225,124,853</u>	<u>275,572,245</u>
OPERATING INCOME (LOSS)	<u>83,557,923</u>	<u>64,234,451</u>
NONOPERATING REVENUES (EXPENSES)		
Interest and investment revenue	50,381,724	63,530,966
Investment expenses	(4,681,476)	(4,409,843)
Securities lending investment revenue	213,849	-
Securities lending expenses	(42,729)	-
Net (decrease) increase in fair value of investments	18,906,161	(3,358,796)
Dividend credit expenses	<u>(136,968,985)</u>	<u>(97,925,896)</u>
Net non-operating revenues (expenses)	(72,191,456)	(42,163,569)
CHANGE IN NET POSITION	11,366,467	22,070,882
TOTAL NET POSITION, BEGINNING OF YEAR	<u>454,782,551</u> **	<u>432,711,669</u>
TOTAL NET POSITION, END OF YEAR	<u>\$ 466,149,018</u>	<u>\$ 454,782,551</u>

** Note the beginning Net Position for fiscal year 2015 was reduced by approximately \$6.4 million, due to the implementation of GASB Statement No. 68, Pension Liability Reporting, as explained in Note 1.

WORKFORCE SAFETY & INSURANCE
STATEMENTS OF CASH FLOWS
YEARS ENDED JUNE 30, 2016 AND 2015

	<u>2016</u>	<u>2015</u>
CASH FLOWS FROM OPERATING ACTIVITIES		
Receipts from employers	\$ 226,808,140	\$ 240,092,178
Receipts from other funds	2,518,866	3,201,301
Receipts from others	14,838,995	6,923,205
Payments to medical providers	(97,821,360)	(116,691,224)
Payments to injured workers	(80,138,512)	(82,369,496)
Payments to employers	(17,335,307)	(8,874,966)
Payments to employees	(23,505,057)	(22,142,738)
Payments to other funds	(3,481,929)	(2,870,142)
Payments to others	(15,397,133)	(15,325,793)
	<u>6,486,703</u>	<u>1,942,325</u>
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Acquisition and construction of capital assets	<u>(1,931,159)</u>	<u>(79,520)</u>
	<u>(1,931,159)</u>	<u>(79,520)</u>
CASH FLOWS FROM INVESTING ACTIVITIES		
Contributions to pooled investments	(27,993,997)	(25,497,144)
Withdrawals from pooled investments	<u>23,000,000</u>	<u>23,000,000</u>
	<u>(4,993,997)</u>	<u>(2,497,144)</u>
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(438,453)	(634,339)
CASH AND CASH EQUIVALENTS, BEGINNING OF YEAR	<u>2,448,255</u>	<u>3,082,594</u>
CASH AND CASH EQUIVALENTS, END OF YEAR	<u>\$ 2,009,802</u>	<u>\$ 2,448,255</u>
SCHEDULE OF OTHER NONCASH ACTIVITIES		
Net (decrease) increase in fair value of investments	\$ 19,403,106	\$ (139,658,810)
Changes in securities lending collateral	17,214,543	-
Investment revenue	46,245,738	56,679,528
Dividends credited to premium billings	83,186,428	116,603,792
Account receivable premium reductions	(83,186,428)	(116,603,792)

STATEMENTS OF CASH FLOWS (continued)

	<u>2016</u>	<u>2015</u>
RECONCILIATION OF OPERATING REVENUE TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES		
Operating income	\$ 83,557,923	\$ 64,234,451
Adjustments to reconcile operating revenue to net cash provided (used) by operating activities		
Deferred outflows Retirement & Investment office (RIO)	10,431	-
Deferred inflows Retirement & Investment office (RIO)	3,281	-
Decrease in due to other state agencies (RIO)	1,245	-
Depreciation/amortization expense	398,680	372,402
Dividend credits applied to receivables	(136,968,985)	(97,925,896)
Change in assets and liabilities		
Decrease in premium receivable	7,150,458	2,004,253
Decrease in retrospective premium receivable	-	10,886
(Increase) decrease in other accounts receivable	(1,387,504)	547,949
Increase (decrease) in prepaid expenses	220,408	(179,412)
Increase in accounts payable	436,089	313,470
(Decrease) increase in due to other state agencies	(5,217)	36,933
(Decrease) increase to pension liability	328,990	(46,192)
Increase (decrease) in dividend payables	53,782,557	(18,677,897)
(Decrease) increase in unearned premium	(15,751,951)	7,375,167
Increase in compensated absences payable	96,119	8,211
Increase in unpaid loss and loss adjustment expenses	15,064,115	43,868,000
Increase in deferred outflows	(69,609)	-
Decrease in deferred inflows	(380,327)	-
Net cash provided by operating activities	<u>\$ 6,486,703</u>	<u>\$ 1,942,325</u>

WORKFORCE SAFETY & INSURANCE
STATEMENTS OF APPROPRIATIONS
YEAR ENDED JUNE 30, 2016

	Approved 2015-17 Biennial Appropriation	Expenditures 2016	Expenditures 2017	Unexpended Appropriation
APPROPRIATED EXPENDITURES	\$ 68,865,170	\$ 32,393,004	\$ -	\$ 36,472,166
CONTINUING APPROPRIATIONS				
Collection agency fees	-	127,261	-	-
Vocational rehabilitation grant	-	94,186	-	-
Employer fraud & field investigation	-	50,617	-	-
Litigation fees & costs	-	205,349	-	-
Provider fraud	-	54	-	-
Performance Evaluation	-	-	-	-
Other states coverage	-	600,000	-	-
Building operations	-	803,380	-	-
Safety programs	-	4,176,823	-	-
Reinsurance	-	7,127,375	-	-
Total*	<u>\$ 68,865,170</u>	<u>\$ 45,578,049</u>	<u>\$ -</u>	<u>\$ 36,472,166</u>

*This total represents WSI's expenditures through the State Treasurer's Office using the State's PeopleSoft system. WSI has received an authorization from the State Treasurer's Office to also issue payments directly from the Bank of North Dakota; these payments include policyholder refunds, indemnity benefits, medical benefits, allocated loss adjustment expenses, and the educational revolving loan fund transactions.

WORKFORCE SAFETY & INSURANCE
NOTES TO FINANCIAL STATEMENTS
YEARS ENDED JUNE 30, 2016 AND 2015

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Statements and Reporting Entity

Workforce Safety & Insurance (WSI) is an agency of the State of North Dakota, operating through the legislative authority of Title 65 of the North Dakota Century Code.

WSI was established in 1919 for the administration of the Workers Compensation Act and other designated acts. As a state agency, WSI is a department of the State of North Dakota and is included in the State's Comprehensive Annual Financial Report as an enterprise fund. The director of WSI is appointed by the Governor. Workforce Safety & Insurance provides no-fault medical and disability insurance to North Dakota employers. The state of North Dakota is a "monopolistic" state where WSI is the sole provider of workers compensation insurance. WSI is financed by premiums charged to employers doing business in North Dakota. The premiums are available primarily for the payment of claims to employees injured in the course of employment.

The accompanying financial statements of Workforce Safety & Insurance follow the pronouncements of the Governmental Accounting Standards Board (GASB), which is the nationally accepted standard-setting body for establishing accounting principles generally accepted in the United States of America for governmental entities.

For financial reporting purposes, WSI has included all funds and has considered all potential component units for which WSI is financially accountable, and other organizations for which the nature and significance of their relationship with WSI are such that exclusion would cause WSI's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. This criterion includes appointing a voting majority of an organization's governing body and (1) the ability of WSI to impose its will on that organization or (2) the potential for the organization to provide specific financial benefits to, or impose specific financial burden on WSI.

Based upon these criteria, there are no component units to be included within WSI as a reporting entity and WSI is an agency within the State of North Dakota as a reporting entity.

Fund Financial Statements

WSI uses a fund to report financial position and operational results. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities. A fund is a separate accounting entity with a self-balancing set of accounts.

The financial activities of WSI reported in the accompanying statements are classified into one fund category, the proprietary fund. The proprietary fund includes the Enterprise Fund, which is used to account for the operations of the workers compensation insurance program for North Dakota employers and employees.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of WSI are premiums charged to policyholders for workers compensation insurance. WSI also recognizes as operating revenues, penalties and interest billed for delinquent premium, third party liability subrogation recoveries, student loan interest and rental revenue from building tenants.

NOTES TO FINANCIAL STATEMENTS

Measurement Focus, Basis of Accounting and Financial Statement Presentation

Operating expenses for the enterprise fund include the incurred losses, payroll and benefits, other administrative expenses, bad debt expense, depreciation on capital assets and building expense. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus. Proprietary funds are accounted for on a flow of economic resources measurement focus. This measurement focus includes all assets and liabilities associated with the operations of these funds on the balance sheet.

Proprietary funds are accounted for using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when they are earned and expenses are recognized when the related liability is incurred.

Budgetary Policies and Procedures

WSI operates through a biennial appropriation provided by the State Legislature. WSI prepares a biennial budget for administrative expenses which is included in the Governor's budget and is presented to the General Assembly at the beginning of each legislative session. The General Assembly enacts the budgets of the various state departments through passage of specific appropriation bills. Before signing the appropriation bills, the Governor may veto any specific appropriation, subject to legislative override. Once passed and signed, the appropriation becomes WSI's administrative budget for the next two years. Any changes to the budget appropriation require Emergency Commission authorization. The Legislative Assembly approved a single-line appropriation for WSI beginning with the 2001-2003 biennium.

The Emergency Commission can authorize receipt of federal or other moneys not appropriated by the Assembly if the Assembly did not indicate any intent to reject the money. The Emergency Commission may authorize pass-through federal funds from one state agency to another. Unexpended appropriations lapse at the end of each biennium.

The State of North Dakota does not formally budget revenues, thus, a Statement of Revenues, Expenditures, and Changes in Fund Net Position - Budget and Actual cannot be prepared as required by accounting principles generally accepted in the United States of America. In its place a Statement of Appropriations has been presented. The Statement of Appropriations has been prepared using the modified accrual basis.

Cash and Investments

Cash and cash equivalents for reporting purposes, includes cash and short-term, highly liquid investments that are readily convertible to known amounts of cash and so near their maturity that they present insignificant risk of changes in value because of changes in interest rates. This includes investments with original maturity of three months or less. Investments are stated at fair value. GASB Statement 72 defines fair value as, "*the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.*" Fair value was determined by reference to published market data for publicly traded securities or through the use of independent valuation services and appraisers for other investments.

Net appreciation (depreciation) is determined by calculating the change in the fair value of investments between the end of the year and the beginning of the year, less any purchases of investments at cost, plus sales of investments at fair value. Investment expense consists of those administrative expenses directly related to the Retirement and Investment Office investment operations.

NOTES TO FINANCIAL STATEMENTS

WSI's investment policy allows investment managers to use derivative securities. Managers are specifically permitted to use Treasury futures and options, S & P 500 index futures and options, and currency forwards and futures to hedge portfolio risk, but not to speculate or to leverage the portfolio. Managers may use their discretion to use other derivatives to enhance returns, reduce risk, or facilitate the management of index funds. WSI's policy with respect to these derivatives is that their use may not increase the credit, market or legal risk level associated with a fully invested portfolio of common stocks or fixed income obligations, depending on the manager's designated role.

As the master custodian for the Retirement and Investment Office, Northern Trust is the Agent of Record for WSI's portfolio.

Premium Receivable

Premium receivables are stated net of allowance for doubtful accounts in the amount of \$7.5 million at June 30, 2016 and June 30, 2015. Premium receivables also include an estimate of premiums that have yet to be billed at year-end, but will be billed in subsequent periods.

Through 2005, several WSI policyholders participated in the Retrospective Rating Program whereby annual adjustments were made to reflect the insured's annual loss experience. Per the terms of the retrospective rating contract, these adjustments were required to be made over a 10 year period, effectively closing out the program June 30, 2015.

Other Accounts Receivable

Other accounts receivable consists of medical assessments, deductibles, reinsurance receivable on loss payments, receivables resulting from overpayments on claims, and other miscellaneous receivables. These receivables are stated net of allowance for doubtful accounts in the amount of \$2 million at June 30, 2016 and June 30, 2015.

Prepaid Expenses

Payments made to vendors which exceed \$12,000 per year, for services that will benefit periods beyond June 30, 2016 and 2015 are recorded as prepaid expenses.

Capital Assets and Depreciation

All capital assets are recorded in the accompanying financial statements at cost. WSI capitalizes equipment and software costing over \$5,000 in accordance with section 54-27-21 of the NDCC.

WSI's capital assets are being depreciated on a straight-line basis over estimated useful lives ranging from 3 to 50 years.

Due to Other Funds

During the course of operations, numerous transactions occur between other state agencies for goods provided or services rendered. These payables are classified "Due to other funds" on the statement of net position in the period for which the liability applies.

NOTES TO FINANCIAL STATEMENTS

Compensated Absences Payable

Annual Leave: WSI employees accrue vested annual leave at a variable rate based on years of service. The amount of annual leave earned ranges between 1 and 2 days per month, and is fixed by the employing unit per section 54 -06-14 of the North Dakota Century Code. Accrued annual leave cannot exceed 30 days at April 30 of each year. Employees are paid for unused annual leave upon termination or retirement.

Sick Leave: WSI employees accrue sick leave at the rate of one working day per month of employment without limitation on the amount that can be accumulated. Per North Dakota Century Code section 54-06-14, employees vest at 10 years of continuous service at which time the State is liable for 10% of the employee's accumulated unused sick leave.

WSI's liability for accumulated unpaid annual leave and sick leave is reported in the enterprise fund, and will be funded by WSI's appropriation when the liability is to be liquidated. The net change in the liability is recorded as an adjustment to other administrative expenses within the enterprise fund.

Deferred Outflows and Inflows of Resources

In addition to assets, the statement of financial position reports a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until then.

In addition to liabilities, the statement of financial position reports a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources*, represent an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

Unearned Premium

Premiums are billed to the employer at the beginning of the employer's policy year. The billed premium is recognized as revenue on a straight-line basis over the applicable year. Unearned premiums consist of the unamortized portion of premiums at WSI's fiscal year-end.

Unpaid Loss and Loss Adjustment Expenses (LAE)

The liability for unpaid loss and loss adjustment expense (LAE) is estimated by WSI's actuary, taking into consideration past experience of WSI in paying claims and the general conditions of the environment in which WSI operates. This liability is based on the estimated ultimate costs to settle both reported and incurred but not reported (IBNR) losses and LAE, and includes the effects of inflation and other societal and economic factors. The actuarial computations also include a 5% discount to report this liability at its estimated present value.

Management believes the estimated liability for unpaid loss and LAE is sufficient to cover the ultimate net costs of incurred losses, but such loss reserves are necessarily based on estimates and the ultimate liability may be greater or less than the amounts estimated. Any adjustments to this estimated liability are reflected as part of current operations.

NOTES TO FINANCIAL STATEMENTS

Pensions

For purposes of measuring the net pension liability, deferred outflows/inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the North Dakota Public Employee Retirement System (NDPERS) and additions to/deductions from NDPERS's fiduciary net position have been determined on the same basis as they are reported by the NDPERS. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value.

Reinsurance

In accordance with NDCC Sections 65-02-13 and 65-02-13.1, WSI obtained reinsurance coverage with Munich Re America, formerly American Re-Insurance Company. The contracts for reinsurance were in effect for all losses incurred on or after December 1, 1999 through November 30, 2002. Under the reinsurance contract, Munich Re America agrees to reimburse WSI on an excess of loss basis. In 2002, global influences such as the 9-11 attacks hardened the reinsurance market and pushed the price of reinsurance to an inefficient level. As a result, WSI withdrew from the reinsurance market.

When the insurance market softened in 2008, WSI again sought reinsurance coverage. Working through a reinsurance intermediary, Guy Carpenter, WSI obtained catastrophic coverage beginning in calendar year 2010 and has continued to purchase excess of loss coverage through calendar year 2016. WSI deems this protection essential due to the types of industries which have entered and expanded within the state. Terms, limits, and pricing are re-evaluated annually.

Restatement – GASB Statement No. 68

As of July 1, 2014, WSI adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions and GASB Statement No. 71 Pension Transition for Contributions Made Subsequent to the Measurement Date*. The implementation of these standards requires governments calculate and report the costs and obligations associated with pensions in their basic financial statements. Employers are required to recognize pension amounts for all benefits provided through the plan which include the net pension liability, deferred outflows of resources, deferred inflows of resources, and pension expense. See additional information in Note 11.

Net Position

Net position represents the difference between (a) assets and deferred outflows of resources and (b) liabilities and deferred inflows of resources in the financial statements. Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any long-term debt attributable to the acquisition, construction, or improvement of those assets. Restricted net position consists of restricted assets reduced by liabilities and deferred inflows of resources related to those assets. Unrestricted net position is the net amount of assets, liabilities, and deferred inflows of resources that are not included in the determination of net investment in capital assets or the restricted component of net position.

NOTES TO FINANCIAL STATEMENTS

NOTE 2 - RECONCILIATION FROM APPROPRIATIONS TO GAAP REPORTING

Because accounting principles applied for purposes of developing data on an appropriations basis differ from those used to present financial statements in conformity with GAAP, a reconciliation of the expenses on an appropriations basis to the expenses on a GAAP basis for Enterprise Fund administrative expenses for the years ended June 30, 2016 and 2015 are presented below:

	<u>2016</u>	<u>2015</u>
Administrative expenses on an appropriations basis	\$ 45,578,049	\$ 41,726,798
Reconciling adjustments		
Fixed asset additions	(1,931,159)	(79,519)
Payroll and benefits	(23,533,739)	(22,174,971)
Unallocated loss adjustment expense	(11,327,613)	(10,481,334)
Increase in compensated absences payable	96,119	8,211
Increase in pension payable	328,990	-
Increase (decrease) in administrative payable	(1,171,346)	281,730
Decrease (increase) in prepaid expenses	220,408	(179,412)
Refund of prior biennium expenses	(124,316)	-
Increase in deferred outflows	(69,609)	-
Increase in deferred inflows	(380,327)	-
Revolving loan fees	1,345	1,636
Ceded reinsurance premium	(6,520,969)	(7,237,898)
Administrative expenses on a GAAP basis	<u>\$ 1,165,833</u>	<u>\$ 1,865,241</u>

NOTE 3 - CASH DEPOSITS AND INVESTMENT SECURITIES

Deposits

Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, WSI will not be able to recover deposits that are in the possession of an outside party. WSI does not have a formal policy that limits custodial credit risk for deposits. All of WSI's cash deposits are uncollateralized. The carrying amount of WSI's cash deposits were \$2,009,802 on June 30, 2016, and \$2,448,255 on June 30, 2015. Bank balances for June 30, 2016 and June 30, 2015 were \$6,844,554 and \$6,374,789, respectively. These monies are deposited in the Bank of North Dakota and are guaranteed by the State of North Dakota under NDCC 6-09-10.

WSI is required to have all funds deposited at the Bank of North Dakota in accordance with North Dakota Century Code 6-09-07.

Investments

WSI is required to use the North Dakota State Investment Board (SIB) for its investing activities. The State Investment Board directs the activities of the North Dakota Retirement and Investment Office (RIO) in order to manage the day to day operations of the fund. The SIB and RIO exercise the prudent investor rules as described in NDCC 21-10-07.

NOTES TO FINANCIAL STATEMENTS

The SIB administers the portfolio according to WSI's investment allocation policy. The SIB selects money managers and monitors performance on a continual basis. WSI contracted with Callan & Associates in September 2013 to conduct an asset allocation study. Based on the results of that study, WSI modified its investment allocation policy in April 2014. The modification includes a portfolio mix with 16% in domestic equity, 9% in international equity, 53% in domestic fixed income, 15% in diversified real assets, 6% in real estate, and 1% in cash equivalents. The former allocation mix contained 13% in domestic equity, 7% in international equity, 51% in domestic fixed income, 22% in inflation protected assets, 6% in real estate, and 1% in cash equivalents.

WSI's investment policy does not address credit risk, custodial credit risk, concentration of credit risk, interest rate risk, or foreign currency risk.

Credit Risk

WSI is invested in an external investment pool managed by the North Dakota State Investment Board. The pool is not rated.

Interest Risk

The SIB has chosen to use the Segmented Time Distribution disclosure method. A table detailing WSI's portion of the investment pool as of June 30, 2016 is reported below. Readers may refer to the RIO financial statements regarding highly sensitive securities that are disclosed at the SIB level.

	Market Value	Less Than 1 Year	Duration			Not Determined
			1-6 Years	6-10 Years	Over 10 Years	
Segmented Time Distribution						
Asset backed securities	\$ 30,430	\$ -	\$ 2,491	\$ 8,552	\$ 19,387	\$ -
Bank loans	3,013	-	2,220	793	-	-
Commercial mortgage-backed	36,184	1	-	1,466	34,717	-
Corporate bonds	385,871	10,468	92,212	146,020	137,171	-
Government agencies	12,722	396	6,223	2,280	3,823	-
Government bonds	91,847	202	16,562	32,461	42,621	-
Government mortgage & commercial backed	50,625	228	950	2,595	46,853	-
Index linked government bonds	12,483	2,402	-	2,306	7,774	-
Municipal/provincial bonds	11,607	71	2,557	1,387	7,592	-
Nongovernmental backed CMO's	14,224	-	2,687	38	11,499	-
Other fixed income	1,013	166	847	-	-	-
Short term bills and notes	435	435	-	-	-	-
Pooled investments	441,917	63,681	130,289	137,065	110,882	-
Total debt securities	\$ 1,092,371	\$ 78,050	\$ 257,038	\$ 334,963	\$ 422,319	\$ -

Securities Lending

GASB Pronouncements for "Accounting and Financial Reporting for Securities Lending Transactions," establishes accounting and financial reporting standards for securities lending transactions. The standard requires governmental entities to report securities lent as assets in their balance sheets. Cash received as collateral and investments made with that cash must also be reported as assets. The statement also requires the costs of the securities lending transactions to be reported as expenses separately from income received. In addition, the statement requires disclosures about the transactions and collateral related to them.

NOTES TO FINANCIAL STATEMENTS

State statutes permit and the SIB has authorized the use of securities lending – loans of securities to broker-dealers and other entities for collateral with a simultaneous agreement to return the collateral for the same securities in the future. Northern Trust is the securities lending agent for the SIB. Securities are loaned versus collateral that may include cash, U.S. government securities and irrevocable letters of credit. U.S. securities are loaned versus collateral valued at 102% of the market value of the securities plus any accrued interest. Non-U.S. securities are loaned versus collateral valued at 105% of the market value of the securities plus any accrued interest.

Non-cash collateral cannot be pledged or sold unless the borrower defaults. All securities loans can be terminated on demand by either the lender or the borrower, although the average term of SIB loans was approximately 69 days as of June 30, 2016. Cash open collateral is invested in a short term investment pool, which had an interest sensitivity of 1 day as of this statement date. There were no violations of legal or contractual provisions, no borrower or lending agent default losses known to the securities lending agent. There are no dividends or coupon payments owing on the securities lent. Securities lending earnings are credited to participating clients on approximately the fifteenth day of the following month.

Indemnification deals with the situation in which a client's securities are not returned due to the insolvency of a borrower and Northern Trust has failed to live up to its contractual responsibilities relating to the lending of those securities. Northern Trust's responsibilities include performing appropriate borrower and collateral investment credit analyses, demanding adequate types and levels of collateral, and complying with applicable Department of Labor and Federal Financial Institutions Examination Council regulations concerning securities lending.

For securities loaned at fiscal year end, the SIB has no credit risk exposure to borrowers because the amount the SIB owes the borrowers exceeds the amounts the borrowers owe the SIB.

As of June 30, 2016, the total amount of cash collateral related to these lent securities was \$17,214,543. WSI has not had securities lending in its portfolio since fiscal year 2010.

NOTES TO FINANCIAL STATEMENTS

Foreign Currency Risk

WSI is invested in an external investment pool managed by the SIB. A table detailing WSI's exposure to foreign currency through their share of the investment pool as of June 30, 2016 is reported below.

Foreign Currencies (in thousands)	<u>Short Term</u>	<u>Debt</u>	<u>Equity</u>	<u>Total</u>
Australian dollar	\$ 5	\$ -	\$ 5,201	\$ 5,206
British pound sterling	(340)	397	20,692	20,749
Canadian dollar	2	-	1,521	1,523
Israeli shekel	7	-	700	707
Danish krone	8	-	1,628	1,636
Euro	(2,343)	2,372	29,669	29,698
Hong Kong dollar	44	-	6,564	6,608
Hungarian forint	3	-	-	3
Japanese yen	1,827	123	24,878	26,828
Mexican peso	2	-	933	935
New Zealand dollar	5	-	561	566
Norwegian krone	93	-	1,664	1,757
Singapore dollar	15	-	780	795
South African rand	19	-	1,001	1,020
South Korean won	-	-	848	848
Swedish krona	4	-	3,528	3,532
Swiss franc	28	-	8,745	8,773
International commingled funds (various currencies)	-	-	32,381	32,381
	<u> </u>	<u> </u>	<u> </u>	<u> </u>
Total securities subject to foreign currency risk	<u>\$ (621)</u>	<u>\$ 2,892</u>	<u>\$ 141,294</u>	<u>\$ 143,565</u>

NOTE 4 - SIGNIFICANT CONCENTRATIONS OF CREDIT RISK

WSI extends short-term credit to its customers, most of whom are located within the state of North Dakota. With this credit risk, WSI has established an estimate of allowance for doubtful accounts.

NOTES TO FINANCIAL STATEMENTS

NOTE 5 - CAPITAL ASSETS

A statement of changes in capital assets for the year ended June 30, 2016 is as follows:

	Balance July 1, 2015	Additions	Deletions	Balance June 30, 2016
Capital assets, not being depreciated				
Land	\$ 901,974	\$ -	\$ -	\$ 901,974
Construction in Progress	-	592,621	-	592,621
Total capital assets, not being depreciated	<u>\$ 901,974</u>	<u>\$ 592,621</u>	<u>\$ -</u>	<u>\$ 1,494,595</u>
Capital assets, being depreciated				
Building	\$ 11,474,168	\$ -	\$ -	\$ 11,474,168
Furniture and equipment	409,539	5,189	-	414,728
Intangibles				
Software	2,836,354	1,333,349	-	4,169,703
Total capital assets, being depreciated	14,720,061	1,338,538	-	16,058,599
Less accumulated depreciation for				
Building	(2,668,608)	(229,483)	-	(2,898,091)
Furniture and equipment	(293,967)	(39,437)	-	(333,404)
Intangibles				
Software	(2,303,653)	(129,760)	-	(2,433,413)
Accumulated depreciation and amortization	(5,266,228)	(398,680)	-	(5,664,908)
Total capital assets, net	<u>\$ 10,355,807</u>	<u>\$ 1,532,479</u>	<u>\$ -</u>	<u>\$ 11,888,286</u>

A statement of changes in capital assets for the year ended June 30, 2015 is as follows:

	Balance July 1, 2014	Additions	Deletions	Balance June 30, 2015
Capital assets, not being depreciated				
Land	\$ 901,974	\$ -	\$ -	\$ 901,974
Total capital assets, not being depreciated	<u>\$ 901,974</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 901,974</u>
Capital assets, being depreciated				
Building	\$ 11,474,168	\$ -	\$ -	\$ 11,474,168
Furniture and equipment	583,771	79,520	(253,752)	409,539
Intangibles				
Software	2,836,354	-	-	2,836,354
Total capital assets, being depreciated	14,894,293	79,520	(253,752)	14,720,061
Less accumulated depreciation for				
Building	(2,439,125)	(229,483)	-	(2,668,608)
Furniture and equipment	(506,290)	(41,429)	253,752	(293,967)
Intangibles				
Software	(2,202,163)	(101,490)	-	(2,303,653)
Accumulated depreciation and amortization	(5,147,578)	(372,402)	253,752	(5,266,228)
Total capital assets, net	<u>\$ 10,648,689</u>	<u>\$ (292,882)</u>	<u>\$ -</u>	<u>\$ 10,355,807</u>

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NOTES TO FINANCIAL STATEMENTS

NOTE 6 - DUE FROM (TO) OTHER STATE AGENCIES

The following is a detail of amounts due to and from other State of North Dakota agencies at June 30, 2016 and June 30, 2015.

DUE TO	2016	2015
Central Services / Office Management & Budget	\$ 6,522	\$ 8,478
Dept. of Transportation	10,856	11,425
Information Technology	170,024	177,749
Office of Administrative Hearing	3,844	3,053
Office of the Attorney General	1,985	1,899
Bismarck State College	5,400	-
	<u>\$ 198,631</u>	<u>\$ 202,604</u>
DUE FROM	2016	2015
Surplus Property	\$ -	\$ 13
	<u>\$ -</u>	<u>\$ 13</u>

NOTE 7 - UNPAID LOSS AND LOSS ADJUSTMENT EXPENSES (LAE)

An independent actuarial review of WSI's liability for unpaid loss and loss adjustment expenses was conducted for the years ended June 30, 2016 and 2015. The actuarial computations for unpaid loss and LAE include a 5% discount to report this liability at its estimated present value.

For the year ended June 30, 2016 and June 30, 2015, the consulting actuaries presented an estimate in the form of a range to emphasize the uncertainty which is typical for a "long-tailed" liability insurer such as workers' compensation. Amounts stated are net of reinsurance. Ranges are displayed in thousands.

FY 2016	(In Thousands)		
	Low	Central Value	High
Full value basis, undiscounted	\$ 1,716,741	\$ 1,842,107	\$ 1,941,869
Present value basis, discounted at 5%	1,035,636	1,111,738	1,177,260

WSI management recorded the consulting actuary's central estimate of the ultimate cost for unpaid loss and LAE of \$1,111,738,115.

FY 2015	(In Thousands)		
	Low	Central Value	High
Full value basis, undiscounted	\$ 1,630,595	\$ 1,824,275	\$ 1,960,103
Present value basis, discounted at 5%	985,267	1,096,674	1,182,176

WSI management recorded the consulting actuary's central estimate of the ultimate cost for unpaid loss and LAE of \$1,096,674,000.

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NOTES TO FINANCIAL STATEMENTS

WSI establishes a liability for both reported and incurred but not reported (IBNR) losses, which includes estimates of both future payments of losses and the related loss adjustment expenses, both allocated and unallocated. A reconciliation of the changes in unpaid loss and LAE during the past two years is shown as follows:

	(In Thousands)	
	2016	2015
Unpaid claims and claim adjustment expenses at beginning of fiscal year	\$ 1,096,674	\$ 1,052,806
Discount	727,601	690,199
Undiscounted reserves	1,824,275	1,743,005
Incurred claims and claims adjustment expenses:		
Provision for insured events of the current year	228,620	314,612
Change in provision for prior fiscal years	(37,759)	(35,405)
Change in LAE and other claim recoveries	9,375	6,280
Total incurred losses and loss adjustment expenses	200,236	285,487
Claims and claim adjustment payments attributable:		
To events of the current year	(40,871)	(60,697)
To insured events of prior years	(141,533)	(143,520)
Total paid	(182,404)	(204,217)
Provision for liability discount	(730,369)	(727,601)
Total unpaid claims and claim adjustment expenses at fiscal year end	\$ 1,111,738	\$ 1,096,674

NOTE 8 - ALL STATES COVERAGE

WSI is the sole provider of workers' compensation coverage in North Dakota and insures employers for work related injuries. A North Dakota employer that operates outside of the state may be at risk for claims filed in another jurisdiction. As a solution, in September 2004, WSI contracted with the Accident Fund of America to provide "temporary and incidental" coverage for North Dakota employers who operate outside the state on an incidental basis. Effective July 1, 2010, the program was expanded to include all North Dakota policyholders at no charge to the individual policyholder.

NOTE 9 - OPERATING LEASES

WSI has entered into various operating leases for office space and equipment. Leases contain a clause allowing for termination with a 90-120 day notice and a clause stating that renewal is dependent on appropriation funding by the State Legislature. Expenditures for operating leases were \$299,476 for fiscal year 2016 and \$277,192 for fiscal year 2015. Postage meter leases for Bismarck and Fargo offices each had minor changes in both fiscal years.

NOTES TO FINANCIAL STATEMENTS

The following is a schedule of future minimum lease payments required under the operating leases. Any future renewal or termination options that are available, are not included in the totals below.

<u>Year Ending June 30,</u>	
2017	\$ 301,849
2018	63,866
2019	5,408
	<u>\$ 371,123</u>

NOTE 10 - LONG-TERM LIABILITIES

Compensated Absences Payable

WSI employees can earn annual leave at a variable rate based on years of service. The amount of annual leave earned ranges between 1 and 2 days per month and accrued annual leave cannot exceed 30 days as of April 30th of each year. WSI employees earn sick leave at the rate of one working day per month of employment without limitation on the amount that can be accumulated. At 10 years of continuous service, the State is liable for 10 percent of the employee's accumulated unused sick leave.

The reported liabilities for compensated absences were \$1,540,136 and \$1,444,017 on June 30, 2016, and June 30, 2015 respectively. This balance includes the employer's share of FICA taxes.

	<u>FY 2016 Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>FY 2016 Ending Balance</u>	<u>Amount Due Within One Year</u>
Other long-term liabilities					
Compensated absences	<u>\$ 1,444,017</u>	<u>\$ 1,303,732</u>	<u>\$ 1,207,613</u>	<u>\$ 1,540,136</u>	<u>\$ 1,324,517</u>
	<u>FY 2015 Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>FY 2015 Ending Balance</u>	<u>Amount Due Within One Year</u>
Other long-term liabilities					
Compensated absences	<u>\$ 1,435,806</u>	<u>\$ 1,192,209</u>	<u>\$ 1,183,998</u>	<u>\$ 1,444,017</u>	<u>\$ 1,241,855</u>

WSI's employee turnover rate for fiscal year 2016 and 2015 were 5.17% and 9.3%, respectively.

NOTE 11 - PENSION PLANS

WSI participates in the North Dakota Public Employees Retirement System (NDPERS) administered by the State of North Dakota. NDPERS is an agency of the State of North Dakota financial reporting entity and is included in the State of North Dakota's Comprehensive Annual Financial Report. The following is a brief description of the plans, for general information only. Participants should refer to NDCC Chapter 54-52 for more complete information.

NOTES TO FINANCIAL STATEMENTS

Defined Benefit Pension Plan

NDPERS is a cost -sharing multiple-employer defined benefit pension plan that covers most of the classified employees of WSI. The plan provides pension, disability and death benefits. The cost to administer the plan is financed through the contributions and investment earnings of the plan. Responsibility for administration of the NDPERS defined benefit pension plan is assigned to a Board comprised of seven members. The Board consists of a Chairman, who is appointed by the Governor, one member appointed by the Attorney General; one member appointed by the State Health Officer; three members elected by the active membership of the NDPERS system; and one member elected by the retired public employees. Effective July 1, 2015, the Board was expanded to include two members of the legislative assembly appointed by the Chairman of Legislative Management.

Pension Benefits

Benefits are set by statute. NDPERS has no provisions or policies with respect to automatic and ad hoc post-retirement benefit increases. Member of the Main System are entitled to unreduced monthly pension benefits beginning when the sum of age and years of credited service equal or exceed 85 (Rule of 85), or at normal retirement age (65). For members hired on or after January 1, 2016 the Rule of 85 will be replaced with the Rule of 90 with a minimum age of 60. The monthly pension benefit is equal to 2.00% of their average monthly salary, using the highest 36 months out of the last 180 months of service, for each year of service. The plan permits early retirement at ages 55-64 with three or more years of service.

Members may elect to receive the pension benefits in the form of a single life, joint and survivor, term-certain annuity, or partial lump sum with ongoing annuity. Members may elect to receive the value of their accumulated contributions, plus interest, as a lump sum distribution upon retirement or termination, or they may elect to receive their benefits in the form of an annuity. For each member electing an annuity, total payment will not be less than the members' accumulated contributions plus interest.

Death and Disability Benefits

Death and disability benefits are set by statute. If an active member dies with less than three years of service for the Main System, a death benefit equal to the value of the member's accumulated contributions, plus interest, is paid to the member's beneficiary. If the member has earned more than three years of credited service for the Main System, the surviving spouse will be entitled to a single payment refund, life-time monthly payments in an amount equal to 50% of the member's accrued normal retirement benefit, or monthly payments in an amount equal to the member's accrued 100% Joint and Survivor retirement benefit if the member had reached normal retirement age prior to date of death. If the surviving spouse dies before the member's accumulated pension benefits are paid, the balance will be payable to the surviving spouse's designated beneficiary.

This state statute requires contributions be made to the plan by either the employee or the employer under a "salary reduction" agreement. WSI has implemented a salary reduction agreement and is currently contributing the employees' shares. The required contributions are determined using an entry age normal actuarial funding method. The North Dakota Retirement Board was created by the State Legislature and is the governing authority of PERS. WSI's required and actual contributions to PERS defined benefit pension plan for fiscal years ending June 30, 2016, 2015, and 2014, totaled \$685,886, \$619,152, and \$536,103, respectively.

Eligible members, who become totally disabled after a minimum of 180 days of service, receive monthly disability benefits equal to 25% of their final average salary with a minimum benefit of \$100. To qualify under this section, the member has to become disabled during the period of eligible employment and apply for benefits within one year of termination. The definition for disabled is set by the System in the North Dakota Administrative Code.

NOTES TO FINANCIAL STATEMENTS

Refunds of Member Account Balance

Upon termination, if a member is not vested (is not 65 or does not have three years of service credited for the NDPERS) they will receive the accumulated member contributions and vested employer contributions, plus interest, or may elect to receive this amount at a later date. If a member has vested, they have the option of applying for a refund or can remain as a terminated vested participant. If a member terminated and withdrew their accumulated member contribution and is subsequently reemployed, they have the option of repurchasing their previous service.

Member and Employer Contributions

Member and employer contributions paid to NDPERS are set by statute and are established as a percent of salaries and wages. Member contribution rates are 7% and employer contribution rates are 7.12% of covered compensation.

The member's account balance includes the vested employer contributions equal to the member's contributions to an eligible deferred compensation plan. The minimum member contribution is \$25 and the maximum may not exceed the following:

- 1 to 12 months of service – Greater of one percent of monthly salary or \$25
- 13 to 24 months of service – Greater of two percent of monthly salary or \$25
- 25 to 36 months of service – Greater of three percent of monthly salary or \$25
- Longer than 36 months of service – Greater of four percent of monthly salary or \$25

Pension Liabilities, Pension Expense, and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

At June 30, 2016, the Employer reported a liability of \$6,282,403 for its proportionate share of the net pension liability. The net pension liability was measured as of June 30, 2015, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date. This compares to the proportionate liability of \$5,953,413 reported on June 30, 2015, which was measured as of June 30, 2014; and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of that date.

The Employer's proportion of the net pension liability was based on the Employer's share of covered payroll in the Main System pension plan relative to the covered payroll of all participating Main System employers. At June 30, 2015, the Employer's proportion was 0.923906 percent, which was a decrease of 0.014051 from its proportion of 0.937957 percent measured as of June 30, 2014.

NOTES TO FINANCIAL STATEMENTS

For the year ended June 30, 2016, WSI recognized pension expense of \$581,854. At June 30, 2016, WSI reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Difference between expected and actual experiences	\$ 182,261	\$ -
Change in assumptions	-	(559,733)
Net differences between projected and actual earnings on pension plan investments	-	(132,621)
Changes in proportion and differences between employer contributions and proportionate share of contributions	-	(92,730)
Employer contributions subsequent to the measurement date	<u>685,886</u>	<u>-</u>
WSI Total	<u>868,147</u>	<u>(785,084)</u>
Allocation from Retirement Investment Office	<u>24,049</u>	<u>(9,491)</u>
Total	<u>\$ 892,196</u>	<u>\$ (794,575)</u>

In the year ended, June 30, 2016, \$685,886 was reported as deferred outflows of resources related to pensions resulting from Employer contributions subsequent to the measurement date. This will be recognized as a reduction of the net pension liability in the year ended June 30, 2017.

In the year ended, June 30, 2015, \$619,152 was reported as deferred outflows of resources related to pensions resulting from Employer contributions subsequent to the measurement date. This was recognized as a reduction of the net pension liability in the year ended June 30, 2016.

Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

<u>Year Ending June 30,</u>	
2017	\$ (188,721)
2018	(188,721)
2019	(188,721)
2020	85,323
2021	(122,009)

NOTES TO FINANCIAL STATEMENTS

For the year ended June 30, 2015, WSI recognized pension expense of \$619,152. At June 30, 2015, WSI reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	Deferred Outflows of Resources	Deferred Inflows of Resources
Difference between expected and actual experiences	\$ 203,436	\$ -
Change in assumptions	-	-
Net differences between projected and actual earnings on pension plan investments	-	(1,174,902)
Changes in proportion and differences between employer contributions and proportionate share of contributions	-	-
Employer contributions subsequent to the measurement date	<u>619,152</u>	<u>-</u>
Total	<u>\$ 822,588</u>	<u>\$ (1,174,902)</u>

Actuarial assumptions

The total North Dakota PERS pension liability in the July 1, 2015 actuarial valuation was determined using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	3.50%
Salary increase (Payroll Growth)	4.50% per annum
Investment Rate of Return	8.00%, net of investment expenses
Cost of Living Adjustment	None

For active members, inactive members and healthy retirees, mortality rates were based on the RP-2000 Combined Healthy Mortality Table set back two years for males and three years for females, projected generationally using the SSA 2014 Intermediate Cost scale from 2014. For disabled retirees, mortality rates were based on the RP-2000 Disabled Mortality Table with ages set back one year for males (not set back for females) multiplied by 125%.

The actuarial assumptions used were based on the results of an actuarial experience study completed in 2015. They are the same as the assumptions used in the July 1, 2015, funding actuarial valuation for NDPERS.

As a result of the 2015 actuarial experience study, the NDPERS Board adopted several changes to the actuarial assumptions effective July 1, 2015. This includes changes to the mortality tables, disability incidence rates, retirement rates, administrative expenses, salary scale, and percent married assumption.

The long-term expected rate of return on pension plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target allocation and projected arithmetic real rates of return, after deducting inflation, but before investment expenses, used in the derivation of the long-term expected investment rate of return assumptions for each major asset class are summarized in the following table:

NOTES TO FINANCIAL STATEMENTS

Asset Class	Target Allocation	Long-Term Expected Real Rate of Return
Domestic Equity	31%	6.90%
International Equity	21%	7.55%
Private Equity	5%	11.30%
Domestic Fixed Income	17%	1.52%
International Fixed Income	5%	0.45%
Global Real Assets	20%	5.38%
Cash Equivalents	1%	0.00%

Discount rate. The discount rate used to measure the total pension liability was 8 percent as of June 30, 2015. The projection of cash flows used to determine the discount rate assumes that member and employer contributions will be made at rates equal to those based on the July 1, 2015, Actuarial Valuation Report. For this purpose, only employer contributions that are intended to fund benefits of current plan members and their beneficiaries are included. Projected employer contributions that are intended to fund the service costs of future plan members and their beneficiaries, as well as projected contributions from future plan members, are not included. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments for current plan members as of June 30, 2015. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability as of June 30, 2015.

Sensitivity of the Employer's proportionate share of the net pension liability to changes in the discount rate. The following presents the Employer's proportionate share of the net pension liability calculated using the discount rate of 8 percent, as well as what the Employer's proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage-point lower (7 percent) or 1-percentage-point higher (9 percent) than the current rate:

	<u>1% Decrease (7%)</u>	<u>Current Discount Rate (8%)</u>	<u>1% Increase (9%)</u>
Employer's proportionate share of the net pension liability	\$ 9,633,751	\$ 6,282,403	\$ 3,540,395

Pension plan fiduciary net position. Detailed information about the pension plan's fiduciary net position is available in the separately issued NDPERS financial report. This report may be obtained by writing to: North Dakota Public Employees Retirement System; 400 East Broadway, Suite 505; PO Box 1657, Bismarck, ND 58502-1657.

Changes of assumptions. Amounts reported in 2016 reflect actuarial assumption changes effective July 1, 2015 based on the results of an actuarial experience study completed in 2015. This includes changes to the mortality tables, disability incidence rates, retirement rates, administrative expenses, salary scale, and percent married assumption.

Defined Contribution Retirement Plan

The North Dakota Defined Contribution Retirement Plan (Plan) is administered by the North Dakota Public Employees Retirement System Board. The Plan was established on January 1, 2000, and is administered in accordance with Chapter 54-52.6 of the NDCC. The Plan covers state employees who are in positions not classified by the State of North Dakota Human Resource Management Services Division. Employees of the judicial branch or the Board of Higher Education and State Institutions under the jurisdiction of the Board of Higher Education are not eligible to participate in the Plan.

NOTES TO FINANCIAL STATEMENTS

Member contributions to the Plan are vested immediately and employer contributions to the Plan made on behalf of the member are 100% vested after four years of service. Contribution rates for the Plan are set by statute. In January 2013, member contributions were established at 6% and employer contribution were established at 6.12%. Employees were contributing 2% and WSI was paying the remaining portion of the member contribution.

In January 2014, both the member and employer contributions increased by 1% to 7% and 7.12% respectively. At this time, employees contributed 3% with WSI paying the remainder of the member contribution.

Contributions made to the Plan, by the members and WSI, for fiscal years ending June 30, 2016, 2015, and 2014, totaled \$478,825, \$851,022, and \$807,107, respectively. Contributions decreased significantly in fiscal year 2016 as a large number of WSI employees transferred from the defined contribution plan to the defined benefit plan.

Pension plan fiduciary net position

Detailed information about the pension plan's fiduciary net position is available in the separately issued NDPERS financial report. This report may be obtained by writing to: North Dakota Public Employees Retirement System; 400 East Broadway, Suite 505; PO Box 1657, Bismarck, ND 58502-1657.

NOTE 12 - POSTRETIREMENT BENEFITS

Former WSI employees receiving retirement benefits under the Retirement Plan are eligible to participate in the Retiree Health Benefits Fund, a cost-sharing multiple -employer plan, as administered by the Public Employees Retirement Board. During each month of employment, WSI contributes a percentage based upon each employee's salary into the Retiree Health Benefits Fund.

Total contributions for the fiscal years ending June 30, 2016, 2015, and 2014 were \$180,404, \$167,842, and \$162,372, respectively. The 61st Legislative Assembly increased the contribution percentage from 1.00% to 1.14%, effective August 1, 2009.

NOTE 13 - EMPLOYEE DEFERRED COMPENSATION PLAN

Employees of WSI may participate in an employee deferred compensation plan in accordance with Internal Revenue Service Code Section 457. The plan allows participating employees to defer a portion of their salary until future years. The deferred compensation is not available to the participants until termination, retirement, death, or unforeseeable emergency. The plan is administered by the State of North Dakota Retirement Board. All compensation deferred under the plans, all property and rights purchased with those amounts, and all income attributable to those amounts, property or rights are held in trust for the exclusive use of the employee or their beneficiary. Since the investments are not held by WSI, the investments and the related obligation to employees is not included in WSI's statement of net position.

NOTE 14 - RISK MANAGEMENT

WSI is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. The following are funds/pools established by the State for risk management issues.

WSI is insured by the State Fire & Tornado Fund as well as the State Bonding Fund. WSI pays an annual premium to the Fire & Tornado Fund for 90% replacement cost of its personal property. Replacement cost is estimated on the office building and all furniture and equipment in consultation with the Fire & Tornado Fund.

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NOTES TO FINANCIAL STATEMENTS

The State Bonding Fund currently provides WSI with blanket fidelity bond coverage in the amount of \$2,000,000 for its employees. The State Bonding Fund does not currently charge any premium for this coverage.

WSI is insured through the OMB Risk Management Division for workers compensation insurance as well as tort liability. WSI pays an annual premium to the OMB Risk Management Division for both of these exposures. The Risk Management Division manages all workers compensation claims for all state agencies.

NOTE 15 - REINSURANCE

WSI currently contracts with reinsurance intermediary, Guy Carpenter, for placement of catastrophic claim insurance. WSI has four coverage levels, with retention limits of \$3 million, \$5 million, \$10 million and \$20 million dollars. WSI deems this protection essential to protect the fund against catastrophic losses. Terms, limits, and pricing are re-evaluated annually. For the year ended June 30, 2016 and 2015 WSI recorded ceded losses of \$11,102,810 and \$5,348,696 and ceded premiums of \$6,520,756 and \$7,237,898, respectively.

NOTE 16 - RESTATEMENT OF NET POSITION

As of July 1, 2014, WSI adopted GASB Statement No. 68, *Accounting and Financial Reporting for Pensions and GASB Statement No. 71 Pension Transition for Contributions Made Subsequent to the Measurement Date*.

This implementation required the addition of four new accounts; Pension Expense, Pension Liability, Deferred Outflows and Deferred Inflows to the fiscal year 2015 financials. The additional disclosures required by these standards are included in Note 11.

Net Position - June 30, 2014, as previously reported	\$ 439,127,853
Restatement due to implementation of GASB 68, effect on net position	<u>(6,416,184)</u>
Net Position - July 01, 2014, as restated	<u>\$ 432,711,669</u>

** In accordance with GASB Statement No. 68, the 2014 financial statements were not restated as the appropriate actuarial valuations for the prior periods were not available.

NOTE 17 - SIGNIFICANT LEGISLATIVE CHANGES

Fiscal year 2016 was a non- legislative year.

NOTE 18 - RELATED PARTIES

As stated in Note 1 of these financial statements, WSI is an agency of the state of North Dakota; as such, the other state agencies and political subdivisions are related parties.

NOTE 19 - TENANT LEASES

WSI leases six suites to five tenants in their main office building at 1600 East Century Avenue, Bismarck, ND. The Department of Human Services has two suites, one for Child Support and one for Provider Audit. These tenants, identified below, began leasing space at WSI's Century Center on July 1, 2003. All tenants had an increase in their lease rates on July 1, 2007, July 1, 2011, and again on July 1, 2015.

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NOTES TO FINANCIAL STATEMENTS

All tenants have renewed their leases with a term of July 1, 2015 through June 30, 2017 as provided below:

	<u>Monthly Rent</u>	<u>Annual Rent</u>
ND Council on the Arts	\$ 1,764	\$ 21,171
ND Department of Commerce	21,083	252,993
ND Human Services Child Support	10,392	124,701
ND Human Services Provider Audit	2,107	25,280
ND OMB Risk Management	2,057	24,690
ND Parks & Recreation	7,551	90,611
	<u>\$ 44,954</u>	<u>\$ 539,446</u>
Total	<u>\$ 44,954</u>	<u>\$ 539,446</u>

NOTE 20 - FINANCIAL RESERVES AND SURPLUS

NDCC 65-04-02 requires WSI to maintain adequate financial reserves plus surplus of at least 120% to a maximum of 140% of the actuarial established discounted reserve. Should WSI's available surplus be outside of these levels, statute allows WSI two years to come into compliance. However, statute restricts WSI from granting a dividend credit of greater than 50% of the prior year's premium.

The 2009 Legislative Assembly modified this statute via 2009 HB1035. The legislation defined "available surplus" as net position excluding funds designated or obligated to specific programs or projects pursuant to a directive or specific approval by the legislative assembly. This legislation also set parameters on when a dividend declaration should and should not be considered.

WSI's available surplus of \$442.8 million plus discounted reserves on June 30, 2016 equals 139.8% of the estimated actuarial discounted reserve liability of \$1.112 billion. This compares to the available surplus of \$427.1 million plus estimated discounted reserve liabilities on June 30, 2015, which equaled 138.9% of the estimated actuarial discounted reserve liabilities of \$1.097 billion. The available surplus of \$412.4 million plus estimated discounted reserve liabilities on June 30, 2014, equaled 139.2% of the estimated actuarial discounted reserve liabilities of \$1.053 billion. WSI granted a 50%, 30% and 39% dividend credit in fiscal year 2016, 2015 and 2014, respectively.

Ratio of Available Surplus to Discounted Reserves

	Actual June 2014	Actual June 2015	Actual June 2016
Estimated Discounted Financial Reserves	\$ 1,052,806,000	\$ 1,096,674,000	\$ 1,111,738,115
NET POSITION or "SURPLUS"	\$ 439,127,853	\$ 454,782,551	\$ 466,149,018
2009 HB 1035 Allowable Deductions from Net Assets (Surplus)			
Safety & Education Grants	11,885,767	12,881,858	8,705,035
Revolving School Loan Fund	14,806,047	14,797,047	14,637,495
Total Exclusions from Net Position(Surplus)	26,691,814	27,678,905	23,342,530
Available Fund Surplus	\$ 412,436,039	\$ 427,103,646	\$ 442,806,488
	39.2%	38.9%	39.8%

NOTES TO FINANCIAL STATEMENTS

NOTE 21 - COMMITMENT - CAPS (CLAIMS AND POLICY SYSTEM)

WSI is working closely with ITD and several outside companies to enhance and develop its current Claims and Policy software system. This program, titled CAPS, completed the planning stage in June 2015. CAPS will replace core business applications by consolidating the current databases and adding new functionality. This program is being completed in phases, with each phase having several releases, using an evolutionary implementation. As each release is completed, the development is put into production for immediate usage.

This program is expected to extend out to June 2023. The Policy system replacement is estimated to be complete at the end of CY 2019, followed with the replacement of the Claims system. To date, two releases are nearly complete, both ahead of schedule and within budget.

NOTE 22 - CONTINUING APPROPRIATIONS

The following information discloses WSI's continuing appropriation authority of funding from the workers' compensation fund. WSI does not receive any general fund dollars.

NDCC 54-06-29 Collection Agency Fees - WSI maintains an internal collections unit to manage its premium receivable. From time to time, after all collection efforts have been exhausted, account balances may be written off as uncollectible. Some of these account balances may be turned over to external collection agencies.

This continuing appropriation is addressed in OMB Fiscal and Administrative Policy 212. The dollars reported are the fees paid to collection agencies for amounts recovered.

NDCC 65-01-13 Information Fund - This fund was established to recapture costs of providing publications and statistical information to private citizens, businesses, associations, corporations and limited liability companies. Direct costs of operating this fund are expensed as incurred, such as publication printing costs and file storage and retrieval fees. Indirect costs, such as employee wages, are not specifically allocated to this fund. Fees collected for publications and other information requests are deposited into this fund.

NDCC 65-02-05.1 Building Operations – Workforce Safety & Insurance manages the day-to-day operations and maintenance of the building, such as utilities, janitorial service and grounds keeping.

NDCC 65-02-06.1 Allocated Loss Adjustment Expenses – WSI's allocated loss adjustment expenses are charged directly to specific claims and authorized as a continuing appropriation, just like indemnity and medical benefits for injured workers. These expenses include legal fees, and cost containment expenses for return to work case management, fraud investigation services, and the costs of other services required as part of the claims adjudication process.

NDCC 65-02-06.2 Litigation Expense – The 2009 Legislative Assembly authorized a continuing appropriation for expenses associated with litigating employer-related issues and for payment of organization expenses associated with litigating medical provider related issues as identified under sections 65-02-23 and 65-02-20.

NDCC 65-02-13.1 Other States Coverage – An amount necessary to allow the organization to establish a program of reinsurance and a program of extraterritorial coverage and other states' insurance is to be appropriated out of the Workforce Safety & Insurance Fund, as a continuing appropriation. The organization may execute a contract for reinsurance and a contract for extraterritorial coverage and other states' insurance binding on the organization and the contracting party.

NOTES TO FINANCIAL STATEMENTS

NDCC 65-02-13.1 Reinsurance – This statute authorizes the organization to reinsure any risk or any part thereof and may enter into agreements of reinsurance. Costs of reinsurance are to be appropriated from the Workforce Safety and Insurance fund, as a continuing appropriation. The annual financial audit report must report on any contracts executed pursuant to this statute.

NDCC 65-02-23 Insurance Fraud – This statute authorizes a continuing appropriation for "costs associated with identifying, preventing and investigating employer and provider fraud." Injured worker fraud investigative expenses are charged directly to the claim. WSI's special investigations unit (SIU) works to investigate and prevent insurance fraud by employers, medical providers and injured workers.

NDCC 65-02-13.1 Reinsurance – This statute authorizes the organization to reinsure any risk or any part thereof and may enter into agreements of reinsurance. Costs of reinsurance are to be appropriated from the Workforce Safety and Insurance fund, as a continuing appropriation. The annual financial audit report must report on any contracts executed pursuant to this statute.

NDCC 65-02-23 Insurance Fraud – This statute authorizes a continuing appropriation for "costs associated with identifying, preventing and investigating employer and provider fraud." Injured worker fraud investigative expenses are charged directly to the claim. WSI's special investigations unit (SIU) works to investigate and prevent insurance fraud by employers, medical providers and injured workers.

NDCC 65-02-30 Performance Evaluation – This statute requires a performance evaluation be conducted on WSI operations every other biennium through the coordination of the State Auditor's Office. Funding is provided through a continuing appropriation.

NDCC 65-03-04 Safety Programs – This statute provides a continuing appropriation for promoting safety through education, training, consultation, grants and other incentives. WSI's loss control employees and their related administrative expenses are not included as part of this continuing appropriation.

NDCC 65-05.1-08 Educational Revolving Loan Fund – The 2005 Legislative Assembly established a revolving loan fund to provide low interest loans to individuals that have suffered compensable work injuries. The loans must be used to pursue an education at an accredited institution of higher education or an institution of technical education. The loan program is administered by the Bank of North Dakota. In June 2005, WSI's board of directors earmarked \$15 million for the educational revolving loan fund. WSI began marketing the loan program in August 2005.

NDCC 65-05-36 Preferred Worker Program – WSI established a program for injured workers who, while employable, are unable to return to the employer at the time of their injury. The preferred worker program offers benefits to North Dakota employers for hiring people under this program. This continuing appropriation funds any employment-related expenses such as equipment purchases and work-site modifications for the preferred worker.

NOTES TO FINANCIAL STATEMENTS

NOTE 23 - FAIR VALUE MEASUREMENT

Recurring fair value measurements are those that Governmental Accounting Standards Board (GASB) Statements require or permit in the statement of net position at the end of each reporting period. Fair value measurements are categorized based on the valuation inputs used to measure an asset's fair value: Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs. Investments' fair value measurements are as follows at June 30, 2016:

Investments	Fair Value	Fair Value Measurements Using		
		Level 1 Inputs	Level 2 Inputs	Level 3 Inputs
Investments held with RIO	\$ 1,839,698,248	\$ -	\$ -	\$ 1,839,698,248

Investments held with RIO are categorized as level 3 and are valued by RIO.

NOTE 24 - CONTINGENCY

During fiscal year 2016, there was activity on two lawsuits as noted below:

AON

WSI has recently resolved a lawsuit following a dispute with Aon eSolutions, Inc., formerly known as Valley Oak Systems, Inc. In the resolution, WSI received a settlement and the payment is recorded as other revenue in the statements of revenue, expenses and changes in fund net position for the year ended June 30, 2016. This lawsuit related to a contract entered into in June 2007, whereby Aon agreed to provide software to WSI to replace WSI's existing workers' compensation policy and claims management software systems. After more than five years of work on the project and approximately \$17,000,000 in expenditures to both Aon and others, Aon was unable to deliver the software and WSI terminated its relationship with Aon effective December 31, 2012.

On March 27, 2014, WSI commenced a lawsuit against Aon in Burleigh County District Court. Aon asserted a counterclaim against WSI for work Aon asserts it performed under the contract but for which it never received payment. Aon asserts it is owed an amount of at least \$400,000.00. In December, 2015, this lawsuit was settled outside of court by mutual agreement, to the mutual satisfaction of both parties.

Valley Med Flight

Valley Med Flight v. Terry Dwelle, in his capacity as State Health Officer, and Bryan Klipfel, in his capacity as Executive Director of WSI

Valley Med Flight is an emergency air ambulance service provider in North Dakota. In June 2015, Valley Med Flight commenced an action in United States District Court to declare invalid and to stop the enforcement of 2015 North Dakota House Bill No. 1255, enacted as North Dakota Century Code section 23-27-04.10. This law pertains to air ambulance services in North Dakota and is primarily administered by the North Dakota Department of Health.

NOTES TO FINANCIAL STATEMENTS

Also part of this lawsuit is Valley Med Flight's attempt to declare invalid and to stop the enforcement of WSI's medical fee schedule and laws that pertain to air ambulance services in workers' compensation cases. Valley Med Flight asserts WSI's fee schedule for air ambulance services is preempted by federal law, namely, the Airline Deregulation Act of 1978. The Office of the Attorney General represents WSI's interests in this matter. In March, 2016, the Court ruled in Valley Med Flight's favor, precluding WSI from applying its medical fee schedule to medical air ambulance bills. WSI did not appeal the Court's decision.

Indirect Litigation

WSI is indirectly connected to two class actions involving holdings in investment account overseen by the State Investment Board (SIB). The SIB has been named as a defendant in two cases, arising out of the Tribune and General Motors bankruptcy proceedings, relating to securities that were purchased by external investment managers in one or more portfolios held by the SIB on behalf of its investment client funds. Outside counsel has been retained for both cases, in addition to assistance received from the ND Office of Attorney General. As of June 30, 2016, no liability has been recorded as it is too early in the litigation process to reasonably determine whether any payments will be required.

Requests for information

This financial report is designed to provide a general overview of WSI's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Director of Finance, Workforce Safety & Insurance, 1600 East Century Avenue, Suite 1, Bismarck, ND 58503

WORKFORCE SAFETY & INSURANCE
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF EMPLOYER PENSION LIABILITY AND CONTRIBUTIONS
JUNE 30, 2016 AND JUNE 30, 2015

Schedules of Required Supplementary Information
Schedule of WSI's Share of Net Pension Liability
ND Public Employees Retirement System
Last 10 Fiscal Years*

	<u>2016</u>	<u>2015</u>
WSI's portion of NDPERS net pension liability (asset)	0.923906%	0.937957%
WSI's proportionate share of NDPERS net pension liability (asset)	\$ 6,282,403	\$ 5,953,414
WSI's covered employee payroll (measurement date as of 06/2015)	\$ 8,230,866	\$ 8,087,854
WSI's proportionate share of NDPERS net pension liability (asset) as a percentage of its covered employee payroll	76.0%	73.6%
NDPERS Plan fiduciary net position as a percentage of the total pension liability	77.2%	77.7%

* Amounts presented have a measurement date of the previous fiscal year end.

Changes of assumptions. Amounts reported in 2016 reflect actuarial assumption changes effective July 1, 2015 based on the results of an actuarial experience study completed in 2015. This includes changes to the mortality tables, disability incidence rates, retirement rates, administrative expenses, salary scale, and percent married assumption.

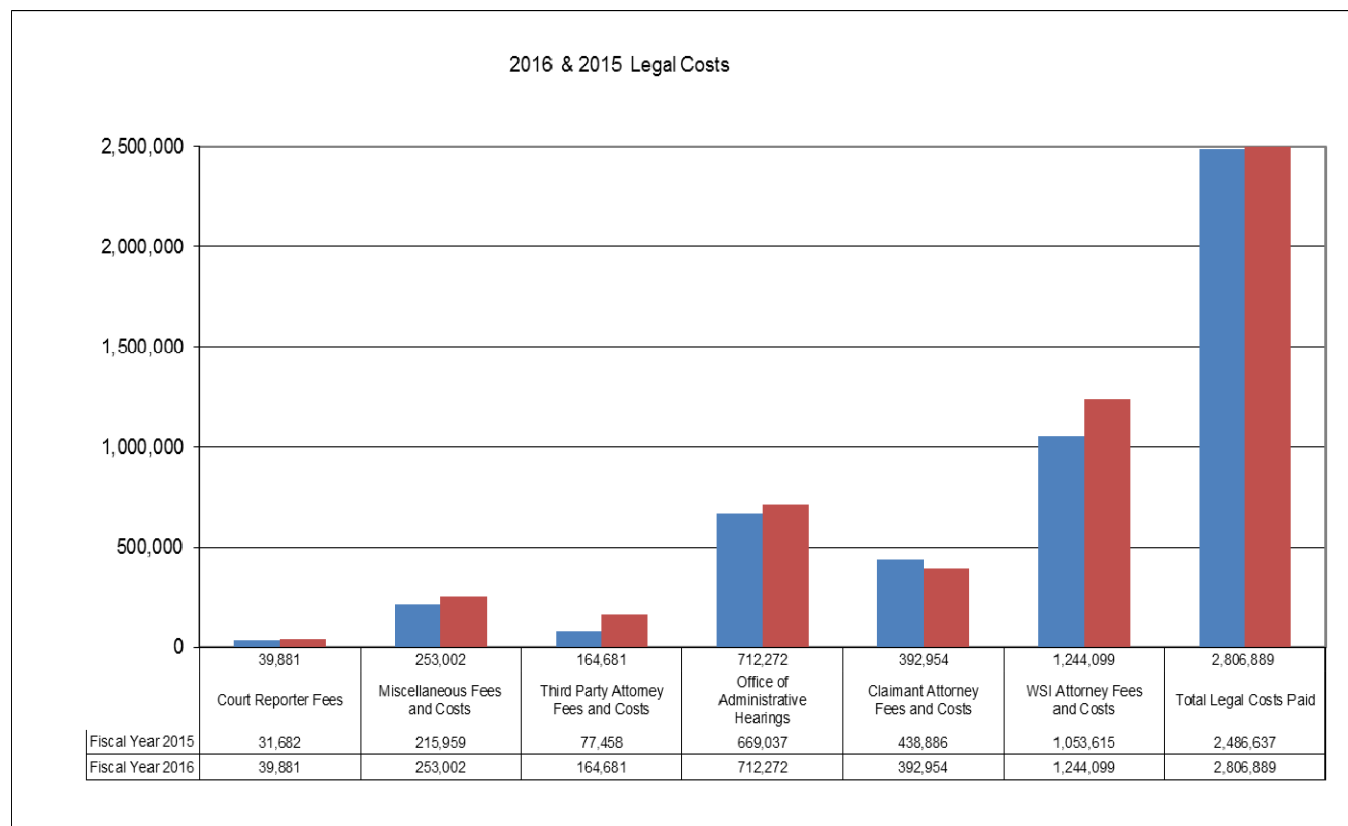
Schedules of Required Supplementary Information
Schedule of WSI's Contributions
ND Public Employees Retirement System
Last 10 Fiscal Years**

	<u>2016</u>	<u>2015</u>
Statutorily required contribution	\$ 625,201	\$ 619,152
Contributions in relation to the actuarially determined contribution	(617,554)	(619,152)
Contribution deficiency (excess)	7,647	-
Covered employee payroll	\$ 8,230,866	\$ 8,695,955
Contributions as a percentage of covered employee payroll	7.60%	7.12%

**Complete data for these schedules is not available prior to 2015.

WORKFORCE SAFETY & INSURANCE
SUPPLEMENTARY INFORMATION
SCHEDULE OF ATTORNEY FEES AND COSTS
JUNE 30, 2016 AND JUNE 30, 2015

Pursuant to Section 65-02-06.1 of the NDCC, the following chart shows the breakdown of allocated loss adjustment expenses (ALAE) for legal fees and costs paid to attorneys representing both the injured workers and WSI, amounts paid for administrative law judges through the Office of Administrative Hearings, court reporter fees, and other miscellaneous legal fees. Legal fees and costs paid in fiscal years 2016 and 2015 were \$2,806,889 and \$2,486,637, respectively. These costs are included as a portion of incurred losses within the “Statements of Revenues, Expenses and Changes in Fund Net Position” of this report.



WORKFORCE SAFETY & INSURANCE
SUPPLEMENTARY INFORMATION
LOSS DEVELOPMENT INFORMATION
JUNE 30, 2016

The table below illustrates how the Fund's earned revenues and investment income compare to related costs of loss and other expenses assumed by the Fund as of the end of each of the last ten years. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's other operation costs of the Fund including overhead and claims expense not allocable to individual claims, as well as investment expenses. (3) This line shows the Fund's incurred losses and allocated loss adjustment expenses, both paid and accrued, as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (referred to as policy year). (4) This section of 10 rows shows the cumulative amounts paid at the end of successive years for each policy year. (5) This section of 10 rows shows how each policy years' estimated incurred losses increased or decreased at the end of each successive year. This annual re-estimation is the result of new information received regarding unknown claims, re-evaluation of existing information on known claims, as well as the emergence of new claims not previously known. (6) This line compares the latest re-estimated incurred losses amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than the original. As data for individual policy years mature, the correlation between original estimates and re-estimated amounts is commonly used to evaluate the accuracy of incurred losses currently recognized in less mature policy years. The columns of the table show data for successive policy years. All data is shown in thousands.

	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
1. Net earned required contribution and investment revenues	\$ 220,949	\$ 165,637	\$ 48,033	\$ 288,949	\$ 357,172	\$ 340,730	\$ 442,995	\$ 502,371	\$ 407,949	\$ 377,414
2. Unallocated expenses	40,011	40,662	30,944	32,709	29,997	33,321	51,881	40,617	41,275	42,938
3. Estimated incurred claims and expense, end of policy year	120,109	131,380	168,964	160,265	191,795	230,158	299,882	337,537	314,612	228,620
4. Paid (cumulative) as of										
End of policy year	20,982	26,584	32,054	30,861	38,596	44,224	52,886	64,846	60,697	40,871
One year later	37,151	46,708	54,795	52,410	65,249	86,783	99,078	111,166	101,990	
Two years later	43,292	53,511	63,358	59,515	76,420	102,133	117,108	127,873		
Three years later	47,083	57,571	69,606	65,216	84,638	110,896	127,508			
Four years later	50,343	60,452	74,643	69,289	90,072	115,555				
Five years later	52,435	63,168	79,073	73,010	93,588					
Six years later	54,678	65,611	82,500	75,495						
Seven years later	56,699	67,694	84,423							
Eight years later	58,374	69,439								
Nine years later	59,703									
5. Reestimated incurred claims and expense										
End of policy year	120,109	131,380	168,964	160,265	191,795	230,158	299,882	337,537	314,612	228,620
One year later	119,100	140,328	157,106	151,411	192,257	257,806	293,069	321,494	283,404	
Two years later	120,358	132,931	153,098	147,853	193,114	243,814	287,797	299,221		
Three years later	110,135	128,652	149,683	146,418	187,355	240,505	272,390			
Four years later	107,711	126,087	148,228	142,001	184,329	227,887				
Five years later	105,446	123,301	147,800	138,874	180,677					
Six years later	103,787	120,429	150,100	136,675						
Seven years later	101,810	119,692	146,641							
Eight years later	100,570	119,161								
Nine years later	102,043									
6. Change in estimated incurred claims and expense from end of policy year	\$ (18,066)	\$ (12,219)	\$ (22,323)	\$ (23,590)	# \$ (11,118)	\$ (2,271)	\$ (27,492)	\$ (38,316)	\$ (31,208)	\$ -

(continued on next page)

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

Board of Directors
Workforce Safety & Insurance
Fargo, North Dakota

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, the financial statements of the business-type activities of Workforce Safety & Insurance, a department of the State of North Dakota, as of and for the years ended June 30, 2016 and 2015, and the related notes to the financial statements, which collectively comprise the Workforce Safety & Insurance's basic financial statements, and have issued our report thereon dated October 11, 2016.

Internal Control over Financial Reporting

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

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

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

Compliance and Other Matters

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

Purpose of this Report

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

A handwritten signature in cursive script that reads "Eide Bailly LLP".

Fargo, North Dakota
October 11, 2016

**Workforce Safety & Insurance
Independent Auditor's Specific Comments Requested by the
North Dakota Legislative Audit and Fiscal Review Committee
Year Ended June 30, 2016**

Board of Directors
Workforce Safety & Insurance
Bismarck, North Dakota

The Legislative Audit and Fiscal Review Committee require that certain items be addressed by independent certified public accountants performing audits of State agencies. The items and our responses regarding the June 30, 2016 audit of the Authority are as follows:

Audit Report Communications:

1. What type of opinion was issued on the financial statements?

Unmodified.

2. Was there compliance with statutes, laws, rules and regulations under which the Authority was created and is functioning?

Yes.

3. Was internal control adequate and functioning effectively?

In planning and performing our audit of the financial statements, we considered Workforce Safety & Insurance's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of Workforce Safety & Insurance's internal control. With that in mind, we did not have any internal control findings.

4. Were there any indications of lack of efficiency in financial operations and management of the Authority?

No.

5. Was action taken on prior audit findings and recommendations?

NA – There was no prior audit findings.

6. Was a management letter issued? If so, provide a summary below, including any recommendations and the management responses.

No.

Audit Committee Communications:

- 1. Identify any significant changes in accounting policies, any management conflicts of interest, any contingent liabilities, or any significant unusual transactions.**

Nothing noted in the current year.

- 2. Identify any significant accounting estimates, the process used by management to formulate the accounting estimates, and the basis for the auditor's conclusions regarding the reasonableness of those estimates.**

One of the most sensitive estimates is the liability for unpaid losses and loss adjustment expenses (LAE). The liability for unpaid losses and LAE is estimated by WSI's actuary, taking into consideration past experience of WSI in paying claims and the general conditions of the environment in which WSI operates. This liability is based on the estimated ultimate costs to settle both reported and incurred but not reported (IBNR) losses and LAE, and includes the effects of inflation and other societal and economic factors. The actuarial computation also includes a 5% discount to report this liability as its estimated present value. We, as auditors of WSI, have a third party actuary review the estimate as provided by WSI's actuary to ensure the estimate is reasonable.

Management's estimate of the net pension liability is based on an actuary's calculation in accordance with the employment contracts. We evaluated the key factors and assumptions used to develop the net pension liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Another significant estimate to the financial statements is the dividend expense and related liability. The dividend expense and liability is calculated using the policyholder's prior year premium less any safety discounts awarded. This premium is an estimate based upon the previous year's actual payroll, and is subject to change once the current year's actual payroll is known. As that becomes known, and the premiums are adjusted, so too will the dividend liability and expense be adjusted. We have reviewed the assumptions and calculation used in determining the estimate to ensure the estimate is reasonable.

- 3. Identify any significant audit adjustments.**

None.

- 4. Identify any disagreements with management, whether or not resolved to the auditor's satisfaction, relating to a financial accounting, reporting, or auditing matter that could be significant to the financial statements.**

None.

- 5. Identify any serious difficulties encountered in performing the audit.**

None.

- 6. Identify any major issues discussed with management prior to retention.**

None.

7. Identify any management consultations with other accountants about auditing and accounting matters.

None.

8. Identify any high-risk technology systems critical to operations based on the auditor's overall assessment of the importance of the system to the agency and its mission, or whether any exceptions identified in the six report questions to be addressed by auditors are directly related to the operations of an information technology system.

The Claims Management System (CMS) and Policy Holder Services (PICS) have been identified as the most high-risk systems at Workforce Safety Insurance. There were no exceptions identified that were directly related to this application.

This report is intended solely for the information and use of the Board of Directors, Legislative Audit and Fiscal Review Committee, and management, and is not intended to be and should not be used by anyone other than these specified parties

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

Fargo, North Dakota
October 11, 2016

To the Audit Committee
Workforce Safety & Insurance
City, State

We have audited the financial statements of the business-type activities of Workforce Safety & Insurance for the years ended June 30, 2016 and 2015. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards*, as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated April 7, 2016. Professional standards also require that we communicate to you the following information related to our audit.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by Workforce Safety & Insurance are described in Note 1 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2016. We noted no transactions entered into by Workforce Safety & Insurance during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimates affecting the financial statements were:

One of the most sensitive estimates is the liability for unpaid losses and loss adjustment expenses (LAE). The liability for unpaid losses and LAE is estimated by WSI's actuary, taking into consideration past experience of WSI in paying claims and the general conditions of the environment in which WSI operates. This liability is based on the estimated ultimate costs to settle both reported and incurred but not reported (IBNR) losses and LAE, and includes the effects of inflation and other societal and economic factors. The actuarial computation also includes a 5% discount to report this liability at its estimated present value. We evaluated the key factors and actuarial assumptions used to develop these reserves and projections in determining that it is reasonable in relation to the financial statements taken as a whole.

Another significant estimate to the financial statements is the dividend expense and related liability. The dividend expense and liability is calculated using the policyholder's prior year premium less any safety discounts awarded. This premium is an estimate based upon the previous year's actual payroll, and is subject to change once the current year's actual payroll is known. As that becomes known, and the premiums are adjusted, so too will the dividend liability and expense be adjusted. We have reviewed the assumptions and calculation used in determining the estimate to ensure the estimate is reasonable.

Also management's estimate of the net pension liability is based on an actuary's calculation in accordance with the employment contracts. We evaluated the key factors and assumptions used to develop the net pension liability in determining that it is reasonable in relation to the financial statements taken as a whole.

Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The most sensitive disclosures affecting the financial statements were:

The disclosure of investments, unpaid losses and loss adjustment expenses reserve, net pension liability information, and fair value measurement in Notes 3, 7, 11 and 23 respectively, to the financial statements. Investment disclosures consisted of fair market value, concentration of credit and custodial risk, interest rate risk and foreign currency risk. Unpaid losses and loss adjustment expenses reserves and net pension liability consist of actuarial estimates of future obligations and the development of prior estimates and the effect on the current financial information.

The financial statement disclosures are neutral, consistent, and clear.

Difficulties Encountered in Performing the Audit

We encountered no significant difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. No corrected or uncorrected financial statement adjustments were noted during the course of the audit.

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 11, 2016.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a “second opinion” on certain situations. If a consultation involves application of an accounting principle to the governmental unit’s financial statements or a determination of the type of auditor’s opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as Workforce Safety & Insurance auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Other Matters

We applied certain limited procedures to Management’s Discussion and Analysis, Schedule of Employer’s Share of Net Pension Liability and Schedule of Employer’s Contributions, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management’s responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on Loss Development Information and Schedule of Attorney Fees and Costs, which accompany the financial statements but are not RSI. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of the Audit Committee, Legislative Audit and Fiscal Review Committee, management, and other state officials, and is not intended to be, and should not be, used by anyone other than these specified parties.

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

Fargo, North Dakota
October 11, 2016