

MINNESOTA WORKERS' COMPENSATION  
ASSIGNED RISK PLAN

FINANCIAL STATEMENTS  
TOGETHER WITH  
INDEPENDENT AUDITORS' REPORT

DECEMBER 31, 2005

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

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**INDEPENDENT AUDITORS' REPORT**

Plan Administrator and the Commerce Department  
of the State of Minnesota  
Minnesota Workers' Compensation Assigned Risk Plan  
Minneapolis, Minnesota

We have audited the balance sheet of the Minnesota Workers' Compensation Assigned Risk Plan (the Plan) as of December 31, 2005, and the related statements of operations and comprehensive income (loss), changes in policyholders' surplus, and cash flows for the year then ended. These financial statements are the responsibility of the Plan Administrator. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the Plan as of and for the year ended December 31, 2004, were audited by other auditors whose report dated July 29, 2005, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2005 financial statements referred to above present fairly, in all material respects, the financial position of the Minnesota Workers' Compensation Assigned Risk Plan as of December 31, 2005, and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

June 15, 2006

*Olsen Thielen & Co., Ltd.*

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## BALANCE SHEET DECEMBER 31, 2005 AND 2004

ASSETS		
	2005	2004
INVESTMENTS:		
Fixed Maturities - At Fair Value	\$ 243,210,271	\$ 203,888,919
Equity Securities - At Fair Value		
(Cost: 2005 - \$58,626,599; 2004 - \$53,414,631)	67,831,724	66,429,385
Short-Term Investments	6,518,385	23,987,926
Total Investments	317,560,380	294,306,230
Cash	1,898,361	4,240,995
Accrued Interest and Dividends	2,170,744	1,401,202
Premiums Receivable	19,698,461	26,555,598
Reinsurance Recoverable on Unpaid Losses	360,000,000	354,000,000
Reinsurance Recoverable on Paid Losses	10,290,156	8,920,847
Deferred Service Carrier Fees	5,693,239	7,759,601
Deferred Policy Acquisition Costs	1,729,313	2,076,376
Due From Broker for Security Sales	7,193	54,746
Reinsurance Premium Receivable	5,654	-
Miscellaneous Assets	640,751	43,369
 TOTAL ASSETS	 \$ 719,694,252	 \$ 699,358,964
LIABILITIES AND POLICYHOLDERS' SURPLUS		
LIABILITIES:		
Reserve for Losses	\$ 604,000,000	\$ 574,000,000
Reserve for Loss Adjustment Expenses	22,000,000	22,000,000
Unearned Premiums	42,446,167	50,609,734
Special Compensation Fund Assessment Payable	7,227,240	7,917,862
Servicing Carrier Administration Fee Payable	2,910,883	4,502,237
Accounts Payable and Accrued Expenses	433,756	367,653
Drafts Outstanding	169,048	294,009
Due to Broker for Pending Purchases	861	477,001
Commissions and Other	701,252	1,091,161
Reinsurance Premium Payable	-	680,368
Total Liabilities	679,889,207	661,940,025
POLICYHOLDERS' SURPLUS:		
Unassigned Surplus - Terrorism Coverage	1,900,999	1,402,708
Unassigned Surplus - All Other Coverages	31,168,124	20,919,208
Accumulated Other Comprehensive Income	6,735,922	15,097,023
Total Policyholders' Surplus	39,805,045	37,418,939
 TOTAL LIABILITIES AND POLICYHOLDERS' SURPLUS	 \$ 719,694,252	 \$ 699,358,964

*The accompanying notes are an integral part of the financial statements.*

**MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN**  
**STATEMENT OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)**  
**YEARS ENDED DECEMBER 31, 2005 AND 2004**

	<b>2005</b>	<b>2004</b>
REVENUES:		
Net Earned Premiums	<b>\$ 94,092,321</b>	\$ 102,491,010
Net Investment Income	<b>11,631,441</b>	9,150,501
Net Realized Capital Gains	<b>4,598,748</b>	2,611,029
Other	<b>—</b>	2,050,363
Total Revenues	<b><u>110,322,510</u></b>	<u>116,302,903</u>
LOSSES AND EXPENSES INCURRED:		
Losses and Loss Adjustment Expenses	<b>73,532,621</b>	90,578,661
Servicing Carrier Fees	<b>11,944,034</b>	18,211,505
Special Compensation Fund Assessments	<b>3,729,361</b>	4,932,790
Other Underwriting Expenses	<b>10,369,287</b>	8,328,688
Total Losses and Expenses Incurred	<b><u>99,575,303</u></b>	<u>122,051,644</u>
NET INCOME (LOSS)	<b><u>10,747,207</u></b>	<u>(5,748,741)</u>
OTHER COMPREHENSIVE INCOME (LOSS):		
Change in Unrealized Appreciation of Investments	<b><u>(8,361,101)</u></b>	<u>286,356</u>
Other Comprehensive Income (Loss)	<b><u>(8,361,101)</u></b>	<u>286,356</u>
COMPREHENSIVE INCOME (LOSS)	<b><u>\$ 2,386,106</u></b>	<b><u>\$ (5,462,385)</u></b>

*The accompanying notes are an integral part of the financial statements.*

## MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

### STATEMENT OF CHANGES IN POLICYHOLDERS' SURPLUS YEARS ENDED DECEMBER 31, 2005 AND 2004

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	<u>2005</u>	<u>2004</u>
UNASSIGNED SURPLUS:		
Beginning Balance	\$ 22,321,916	\$ 28,070,657
Net Income (Loss)	<u>10,747,207</u>	<u>(5,748,741)</u>
Total Unassigned Surplus	<u>33,069,123</u>	<u>22,321,916</u>
ACCUMULATED OTHER COMPREHENSIVE INCOME:		
Beginning of Year	15,097,023	14,810,667
Change in Unrealized Appreciation on Securities	<u>(8,361,101)</u>	<u>286,356</u>
End of Year	<u>6,735,922</u>	<u>15,097,023</u>
POLICYHOLDERS' SURPLUS	<u>\$ 39,805,045</u>	<u>\$ 37,418,939</u>

*The accompanying notes are an integral part of the financial statements.*

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## STATEMENT OF CASH FLOWS YEARS ENDED DECEMBER 31, 2005 AND 2004

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	<u>2005</u>	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Premiums Collected, Net of Reinsurance	\$ 92,785,891	\$ 105,545,995
Investment Income Received	11,193,390	9,920,667
Loss and Loss Adjustment Expenses Paid	(50,901,930)	(46,313,938)
Special Compensation Fund Assessments Paid	(3,038,739)	(4,256,361)
Underwriting and Other Expenses Paid	(25,033,252)	(31,250,359)
Net Cash Provided By Operating Activities	<u>25,005,360</u>	<u>33,646,004</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of Fixed Maturities	(275,992,940)	(147,095,434)
Purchases of Equity Securities	(27,316,662)	(17,590,250)
Proceeds From Sales and Maturities of Fixed Maturities	232,192,990	121,341,440
Proceeds From Sales of Equity Securities	26,727,664	19,840,055
Due to/Due From Broker for Security Purchases and Sales	(428,587)	487,637
Net Change in Short-Term Investments	17,469,541	(13,919,534)
Net Cash Used In Investing Activities	<u>(27,347,994)</u>	<u>(36,936,086)</u>
NET DECREASE IN CASH	(2,342,634)	(3,290,082)
CASH at Beginning of Year	<u>4,240,995</u>	<u>7,531,077</u>
CASH at End of Year	<u>\$ 1,898,361</u>	<u>\$ 4,240,995</u>

*The accompanying notes are an integral part of the financial statements.*

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

### NOTE 1 - DESCRIPTION OF PLAN

The Minnesota Workers' Compensation Assigned Risk Plan (the Plan) is the source of workers' compensation and employers' liability coverage for Minnesota employers who have been unable to obtain an insurance policy through the voluntary market. Coverage provided through the Plan is substantially the same as coverage available from licensed workers' compensation insurance companies.

The Plan was established in 1982 and contracts with servicing contractors who review applications, issue policies, collect premiums, pay claims, and perform other administrative duties for the Plan per contractual requirements. To the extent that the assets of the Plan are inadequate to meet its obligations, the Commissioner of the Minnesota Department of Commerce shall assess all licensed workers' compensation insurance companies doing business in the state of Minnesota an amount sufficient to fully fund the obligations of the Plan. The assessment of each insurer shall be in a proportion equal to the proportion that the amount of workers' compensation insurance written by that insurer in Minnesota during the calendar year preceding the assessment bears to the total workers' compensation insurance written in Minnesota during the same calendar year by all licensed insurers. No assessments were made in either 2005 or 2004. The servicing contractors bear no share of the Plan's liabilities.

Since inception, the Plan has contracted with six servicing contractors to administer the program. These contractors are as follows:

- Berkley Risk Administrators Company, LLC (BRAC);
- RTW, Inc. (RTW);
- Employers Insurance of Wausau, a Mutual Company (EIW);
- Occupational Healthcare Management Services (OHMS);
- Deferred Compensation Administrators, Inc. (DCA); and
- St. Paul Risk Services, Inc. (SPRS).

Policies are allocated to servicing carriers according to each carrier's contractual percentage participation in the program. The percentage participations have varied over time, as outlined in the following chart:

Policy Inception Period	Percentage Participation					
	BRAC	RTW	EIW	OHMS	DCA	SPRS
Inception - 6/30/83	7.0%	–%	30.0%	–%	3.0%	60.0%
7/1/83 - 12/31/86	18.0	–	67.0	–	15.0	–
1/1/87 - 3/31/89	50.0	–	33.0	–	17.0	–
4/1/89 - 3/31/92	65.0	–	35.0	–	–	–
4/1/92 - 3/31/94	50.0	–	50.0	–	–	–
4/1/94 - 3/31/97	50.0	–	25.0	25.0	–	–
4/1/97 - 7/1/00	50.0	–	50.0	–	–	–
7/1/00 - 7/1/04	100.0	–	–	–	–	–
7/1/04 - 12/31/05	75.0	25.0	–	–	–	–



# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES

#### **Basis of Presentation**

The Plan's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America (GAAP).

#### **Risks and Uncertainties**

Certain risks and uncertainties are inherent in the Plan's day-to-day operations and in the process of preparing its financial statements. The more significant of those risks and uncertainties, as well as the Plan's methods for mitigating, quantifying, and minimizing such risks, are presented below and throughout the notes to the financial statements.

#### **Financial Statements Risk**

The preparation of financial statements requires the Plan Administrator to make estimates and assumptions that affect the reported financial statement balances, as well as the disclosure of contingent assets and liabilities. The most significant of these amounts is the liability for loss and loss adjustment expense (LAE) reserves. While the Plan Administrator believes the reserve for losses and LAE makes a reasonable provision to cover the ultimate liability, it is reasonably possible that the actual ultimate loss and LAE costs may vary from amounts provided, and the variance could be material to the financial statements.

#### **Investments Risk**

The Plan is exposed to risks that issuers of securities owned by the Plan will default or that interest rates will change and cause a decrease in the value of its investments. The Plan mitigates these risks by investing in high-grade securities and by matching maturities of its investments with the anticipated payouts of its liabilities.

#### **Premiums Receivable Risk**

Premiums receivable represent amounts to be received from insureds. Premiums are calculated based upon information provided by the insured. Audits are performed on the information provided after the policy expiration date. These audits may result in an additional premium billing or a premium refund. Any difference between the initial premium and the audit premium is reflected in current operations when the audit premium is billed or premium refund is remitted.

#### **Investments**

The Plan's entire fixed maturity and equity investment portfolios are classified as available-for-sale as defined by Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debt and Equity Securities*. Accordingly, the Plan carries these investments on the balance sheet at estimated fair value.

Short-term investments include investments maturing within one year and money market instruments and are carried at cost, which approximates fair value.

Realized gains and losses from sales of investments are reflected in earnings based on the average cost of the investments sold. The difference between the cost and estimated fair value of investments is monitored. If any investments experience a decline in value that the Plan believes is other than temporary, the asset is written down for the decline and a realized loss is reflected in earnings. Changes in unrealized appreciation or depreciation resulting from changes in the fair value of investments are reflected directly in policyholders' surplus as accumulated other comprehensive income.

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### Deferred Costs and Fees

Policy acquisition costs, such as commissions and premium taxes which vary with and are primarily related to the production of business, are deferred and amortized over the effective period of the related insurance policies. If deferred policy acquisition costs were to exceed the sum of unearned premiums and related anticipated investment income less related losses and loss adjustment expenses, the excess costs would be expensed immediately.

Service carrier fees, which are primarily related to the production and maintenance of business, are deferred and amortized over the effective period of the related insurance policies.

#### Unearned Premiums

Premiums are earned ratably over the terms of the policies. Unearned premiums are calculated on the daily pro-rata method and represent the unexpired portion of premiums written.

#### Losses and LAE

The reserves for losses and LAE represent an estimate of the ultimate net cost of all claims that have occurred and are unpaid. The reserves are based on loss factors determined by independent consulting actuaries, using statistical analyses and projections and the historical loss experience of the Plan, and give effect to estimates of trends in claim severity and frequency. As claim settlements occur that differ from reserves estimates, these differences are included in current operations.

For policies with inception dates prior to April 1, 1992, the servicing contractors were responsible for all allocated and unallocated LAE incurred in the settlement of losses. Allocated loss adjustment expenses (ALAE) include legal fees and related expenses (expert testimony, investigations, etc.), medical examinations, and other costs paid to third parties associated with the defense and settlement of particular claims. Unallocated loss adjustment expenses (ULAE) include that portion of the cost of settling claims that cannot be attributed to a specific claim and are more in the nature of an overhead expense (servicing contractors' claim adjuster salaries, rent, etc.).

For policies with inception dates after April 1, 1992, the Plan is responsible for legal and related expenses incurred in the settlement of losses and, accordingly, a liability for these amounts has been established. All other ALAE and all ULAE continue to be the responsibility of the servicing contractors.

#### Special Compensation Fund Assessments

The Minnesota Department of Labor and Industry currently assesses all insurers writing workers' compensation insurance in Minnesota. The assessment pays for the operation of the Special Compensation Fund (SCF). The SCF pays the cost of administration by the State of Minnesota of the workers' compensation laws; reimburses supplementary benefits paid to claimants; reimburses certain benefits paid to claimants with qualifying, prior registered conditions; and pays claims of injured employees of uninsured employers.

In March 2002, legislation was passed by the Minnesota state legislature and signed into law to change the method of assessing insured employers from a loss-based assessment to a premium-based assessment. This change was effective beginning in 2003, from which point the obligating event for assessment liability became the writing of, or becoming obligated to write or renew, the premiums on which the future assessments are to be based. According to MN Senate File 3136, the premium-based method of assessment was to be collected through a policyholder surcharge.

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

### NOTE 2 - SIGNIFICANT ACCOUNTING POLICIES (Continued)

#### Special Compensation Fund Assessments (Continued)

The special compensation fund assessment payable represents those assessments currently due based on pure premiums and the estimated liabilities for future SCF assessments based on SCF surcharges collected on policies with an effective date on or after January 1, 2003.

#### Income Taxes

The Plan is exempt from paying income taxes under Section 501 of the Internal Revenue Code. Accordingly, no provision for income taxes is included in the accompanying financial statements.

### NOTE 3 - CASH PROVIDED BY OPERATING ACTIVITIES

A reconciliation of cash provided by operating activities to the amount reflected in the statement of cash flows is as follows:

	2005	2004
Net Cash Flow From Operating Activities:		
Net Income (Loss)	\$ 10,747,207	\$ (5,748,741)
Adjustments to Reconcile Net Income (Loss) to Net Cash Provided By Operating Activities:		
Net Realized Capital Gains	(4,598,748)	(2,611,029)
Amortization and Accretion	331,491	748,735
Changes in Operating Assets and Liabilities:		
Reserve for Losses and Loss Adjustment Expenses	30,000,000	136,000,000
Reinsurance Recoverable on Paid Losses	(1,369,309)	(1,735,277)
Reinsurance Recoverable on Unpaid Losses	(6,000,000)	(90,000,000)
Unearned Premiums	(8,163,567)	502,392
Premiums Receivable	6,857,137	3,110,073
Due From Broker for Security Sales	47,553	19,707
Deferred Service Carrier Fees	2,066,362	458,003
Deferred Policy Acquisition Costs	347,063	108,304
Special Compensation Fund Assessment Payable	(690,622)	676,429
Service Carrier Administration Fee Payable	(1,591,354)	145,272
Commissions and Other	(389,909)	(2,868,883)
Accounts Payable and Accrued Expenses	66,103	(2,242,838)
Drafts Outstanding	(124,961)	294,009
Due to Broker for Pending Purchases	(476,140)	467,930
Reinsurance Premiums Payable or Receivable	(686,022)	(557,480)
Accrued Interest And Dividends	(769,542)	21,431
Other Assets	(597,382)	(3,142,033)
Net Cash Provided By Operating Activities	\$ 25,005,360	\$ 33,646,004

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

### NOTE 4 - REINSURANCE

The Plan is reinsured by the Minnesota Workers' Compensation Reinsurance Association (WCRA). There is not, nor has there ever been, any other applicable reinsurance. The following table lists the selected per-occurrence retentions by accident year for the past eleven years:

<u>Accident Year</u>	<u>Loss only Per-Occurrence Retention</u>
1995	\$ 250,000
1996	260,000
1997	270,000
1998	280,000
1999	290,000
2000	310,000
2001	330,000
2002	350,000
2003	360,000
2004	360,000
2005	380,000

A contingent liability exists with respect to reinsurance ceded to the extent that the reinsurer is unable to meet its obligation assumed under the reinsurance agreements.

The effect of ceded reinsurance on premiums written, premiums earned, and losses and LAE is reflected in the following table:

	<u>2005</u>	<u>2004</u>
Premium Written:		
Direct	\$ 89,426,687	\$ 103,430,016
Ceded	<u>(3,535,163)</u>	<u>(3,675,865)</u>
Net Premiums Written	<u>\$ 85,891,524</u>	<u>\$ 99,754,151</u>
Premiums Earned:		
Direct	\$ 97,627,484	\$ 106,166,875
Ceded	<u>(3,535,163)</u>	<u>(3,675,865)</u>
Net Premiums Earned	<u>\$ 94,092,321</u>	<u>\$ 102,491,010</u>
Losses and Loss Adjustment Expenses:		
Direct	\$ 92,521,185	\$ 192,690,354
Ceded	<u>(18,988,564)</u>	<u>(102,111,693)</u>
Net Losses and Loss Adjustment Expenses	<u>\$ 73,532,621</u>	<u>\$ 90,578,661</u>

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

### NOTE 5 - INVESTMENTS

The amortized cost, gross unrealized appreciation and depreciation, and the estimated fair values of investments in fixed maturities are as follows:

	<u>2005</u>			
	<u>Amortized Cost</u>	<u>Gross Unrealized Appreciation</u>	<u>Gross Unrealized Depreciation</u>	<u>Estimated Fair Value</u>
U.S. Treasury Securities and Obligations	\$ 191,398,257	\$ 429,148	\$ (2,417,034)	\$ 189,410,371
Mortgage-Backed Securities	<u>54,281,217</u>	<u>275,163</u>	<u>(756,480)</u>	<u>53,799,900</u>
Total Fixed Maturities	<u>\$ 245,679,474</u>	<u>\$ 704,311</u>	<u>\$ (3,173,514)</u>	<u>\$ 243,210,271</u>

  

	<u>2004</u>			
	<u>Amortized Cost</u>	<u>Gross Unrealized Appreciation</u>	<u>Gross Unrealized Depreciation</u>	<u>Estimated Fair Value</u>
U.S. Treasury Securities and Obligations	\$ 121,136,782	\$ 1,123,678	\$ (589,594)	\$ 121,670,866
Mortgage-Backed Securities	<u>80,669,866</u>	<u>1,782,330</u>	<u>(234,143)</u>	<u>82,218,053</u>
Total Fixed Maturities	<u>\$ 201,806,648</u>	<u>\$ 2,906,008</u>	<u>\$ (823,737)</u>	<u>\$ 203,888,919</u>

The amortized cost and estimated fair value of investments in fixed maturities at December 31, 2005 by contractual maturity are shown below. Expected maturities will likely differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	<u>Amortized Cost</u>	<u>Estimated Fair Value</u>
Due in One Year or Less	\$ 15,524,486	\$ 15,403,686
Due After One Year Through Five Years	80,572,971	79,876,343
Due After Five Years Through Ten Years	49,769,171	49,081,029
Due in More Than Ten Years	45,531,629	45,049,313
Mortgage-Backed Securities	<u>54,281,217</u>	<u>53,799,900</u>
	<u>\$ 245,679,474</u>	<u>\$ 243,210,271</u>

The gross unrealized appreciation and depreciation on equity securities are as follows:

	<u>2005</u>	<u>2004</u>
Unrealized Appreciation	\$ 10,840,969	\$ 13,784,073
Unrealized Depreciation	<u>(1,635,844)</u>	<u>(769,319)</u>
Net Unrealized Gains on Equity Securities	<u>\$ 9,205,125</u>	<u>\$ 13,014,754</u>

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

### NOTE 5 - INVESTMENTS (Continued)

Net investment income for 2005 and 2004 is summarized as follows (fixed maturities include interest on short-term investments):

	<u>2005</u>	<u>2004</u>
Fixed Maturities	\$ 10,989,387	\$ 8,386,519
Equity Services	1,131,300	1,225,478
Total	<u>12,120,687</u>	<u>9,611,997</u>
Investment Expenses	<u>(489,246)</u>	<u>(461,496)</u>
Net Investment Income	<u>\$ 11,631,441</u>	<u>\$ 9,150,501</u>

Cash proceeds received from sales of investments in fixed maturities during 2005 and 2004 were \$214,091,789 and \$101,844,310, respectively. In 2005 and 2004, gross gains of \$2,339,091 and \$918,851 and gross losses of \$2,363,311 and \$896,402, respectively, were realized on those sales.

Gross gains of \$5,511,755 and \$3,067,140 and gross losses of \$888,786 and \$478,560 were realized on sales of equity securities in 2005 and 2004, respectively.

### NOTE 6 - LIABILITY FOR LOSSES AND LOSS ADJUSTMENT EXPENSES

A reconciliation of beginning and end of year balances in the liability for unpaid losses and loss adjustment expenses (LAE), net of reinsurance recoverable for the years ended December 31, 2005 and 2004, is as follows:

	<u>2005</u>	<u>2004</u>
Liability for Losses and LAE at Beginning of Year	\$ 596,000,000	\$ 460,000,000
Reinsurance Recoverable on Unpaid Losses - Beginning of Year	(354,000,000)	(264,000,000)
Net Liability for Losses and LAE at Beginning of Year	<u>242,000,000</u>	<u>196,000,000</u>
Provision for Losses and LAE for Claims Incurred:		
Current Year	47,626,707	78,478,000
Prior Year	25,905,914	12,100,661
Total Incurred	<u>73,532,621</u>	<u>90,578,661</u>
Losses and LAE Payments for Claims Incurred:		
Current Year	10,078,762	12,216,000
Prior Year	39,453,859	32,362,661
Total Paid	<u>49,532,621</u>	<u>44,578,661</u>
Net Liability for Losses and LAE at End of Year	<u>266,000,000</u>	<u>242,000,000</u>
Reinsurance Recoverable on Unpaid Losses - End of Year	<u>360,000,000</u>	<u>354,000,000</u>
Liability for Losses and LAE at End of Year	<u>\$ 626,000,000</u>	<u>\$ 596,000,000</u>

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

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### **NOTE 6 - LIABILITY FOR LOSSES AND LOSS ADJUSTMENT EXPENSES (Continued)**

As a result of changes in estimates of insured events in prior years, the losses and LAE incurred (net of reinsurance) increased by \$25,905,914 in 2005 and \$12,100,661 in 2004. The increase in 2005 and 2004 prior year losses was due primarily to worsening of claim experience incurred from original estimates established and severity of covered claims. Loss and LAE reserves were booked near the high end of the actuarial range in both 2005 and 2004 due to continued adverse development and industry deterioration for workers' compensation business.

### **NOTE 7 - STRUCTURED SETTLEMENTS**

The Plan, through EIW, has purchased annuities to settle certain claims with the claimant as payee but for which the Plan remains contingently liable. The Plan eliminated its loss reserves for these claims at the time the annuities were purchased. A contingent liability exists to the extent that the issuer of the annuity contracts becomes unable to fulfill its contractual obligations. The issuer, Employers Life Insurance Company of Wausau, is an affiliate of EIW. The present value of all annuity contracts still in force at December 31, 2005 and 2004 was approximately \$3.9 million and \$4.2 million, respectively.

### **NOTE 8 - CONTINGENCIES**

Since inception, the Plan has contracted with six servicing contractors to provide policy issuance, premium accounting, and claim settlement services in exchange for a service fee based upon standard written premium. Contingent liabilities exist with respect to the performance of the above services to the extent that the servicing carriers are unable to meet their obligations under terms of the general services agreement.

At present, the Plan is not engaged in any litigation known to the Plan that will have a material adverse effect on its business. As is common with other insurance providers, the Plan is regularly engaged in the defense of claims arising out of the conduct of the insurance business.

# MINNESOTA WORKERS' COMPENSATION ASSIGNED RISK PLAN

## NOTES TO FINANCIAL STATEMENTS

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### NOTE 9 - OTHER COMPREHENSIVE INCOME (LOSS)

Comprehensive income (loss) is defined as any change in policyholders' surplus originating from non-owner transactions. The Plan had identified those changes as being comprised of net income and change in unrealized appreciation on securities. The components of comprehensive income, other than net income, are as follows:

	<u>2005</u>	<u>2004</u>
Unrealized Appreciation (Depreciation) Arising During the Period	<b>\$ (3,762,353)</b>	\$ 2,897,385
Less Reclassification Adjustment for Realized Capital Gains Included in Net Income or Loss	<u><b>(4,598,748)</b></u>	<u>(2,611,029)</u>
Total Other Comprehensive Income (Loss)	<u><b>\$ (8,361,101)</b></u>	<u>\$ 286,356</u>

### NOTE 10 - POLICYHOLDERS' SURPLUS

In 2002, a Minnesota law was enacted that required the Plan to transfer its "excess surplus" (as defined in statute) to the general fund of the state of Minnesota. Based on the criteria for "excess surplus", there are no available funds for transfer to the general fund at December 31, 2005.