



October 25, 2011

Mr. Laurence F. Koll
The Minnesota Self-Insurers' Security Fund
West 1430 First National Bank Building
332 Minnesota Street
St. Paul, MN 55101

Dear Mr. Koll:

In accordance with your request, we are attaching the accompanying PDF file, which contains an electronic final version of the financial statements of The Minnesota Self-Insurers' Security Fund as of June 30, 2011 and 2010. We understand that your request for the electronic copy has been made as a matter of convenience. You understand that electronic transmissions are not entirely secure and that it is possible for confidential financial information to be intercepted by others.

These financial statements and our report(s) on them are not to be modified in any manner. This final version supersedes all prior drafts. Any preliminary draft version of the financial statements previously provided to you in an electronic format should be deleted from your computer, and all printed copies of any superseded preliminary draft versions should likewise be destroyed.

Professional standards and our firm policies require that we perform certain additional procedures whenever our reports are included, or we are named as accountants, auditors or "experts," in a document used in a public or private offering of equity or debt securities. Accordingly, as provided for and agreed to in the terms of our arrangement letter, The Minnesota Self-Insurers' Security Fund will not include our reports, or otherwise make reference to us, in any public or private securities offering without first obtaining our consent. Any request to consent is also a matter for which separate arrangements will be necessary. After obtaining our consent, The Minnesota Self-Insurers' Security Fund also agrees to provide us with printer's proofs or masters of such offering documents for our review and approval before printing, and with a copy of the final reproduced material for our approval before it is distributed. In the event our auditor/client relationship has been terminated when The Minnesota Self-Insurers' Security Fund seeks such consent, we will be under no obligation to grant such consent or approval.

Thank you for the opportunity to serve you.

Sincerely,

A handwritten signature in black ink that reads "Dan Vandenberghe". The signature is fluid and cursive, with the first name "Dan" being particularly prominent.

Daniel A. Vandenberghe, Partner
612.376.9267

wpd
Attachment

The Minnesota Self-Insurers' Security Fund

Financial Report
June 30, 2011



McGladrey & Pullen, LLP
Certified Public Accountants

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Independent Auditor's Report

To the Board of Trustees
The Minnesota Self-Insurers' Security Fund

We have audited the accompanying balance sheets of The Minnesota Self-Insurers' Security Fund (the Fund) as of June 30, 2011 and 2010, and the related statements of revenues and expenses, members' equity (deficit) and cash flows for the years then ended. These financial statements are the responsibility of the Fund's management. 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. 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 audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of The Minnesota Self-Insurers' Security Fund as of June 30, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

McGladrey & Pullen, LLP

Minneapolis, Minnesota
October 21, 2011

The Minnesota Self-Insurers' Security Fund

Balance Sheets
June 30, 2011 and 2010

Assets	2011	2010
Cash and cash equivalents	\$ 1,644,647	\$ 1,996,339
Security deposit receivable (Note 3)	534,754	566,349
Reinsurance and other receivables (Note 2)	9,634,891	11,950,565
Membership assessment receivable	4,651	-
Prepaid expenses	3,883	2,237
Total assets	\$ 11,822,826	\$ 14,515,490
Liabilities and Members' Equity (Deficit)		
Liabilities		
Accounts payable	\$ 73,093	\$ 89,755
Deferred revenue	323,488	306,149
Estimated liability for incurred, incurred but unreported, and incomplete claims (Note 2)	18,375,420	21,712,971
Security deposit held pursuant to Kmart bankruptcy proceeding (Note 2)	985,304	1,175,769
Total liabilities	19,757,305	23,284,644
Contingency (Note 2)		
Members' Equity (Deficit) (Note 4)	(7,934,479)	(8,769,154)
Total liabilities and members' equity (deficit)	\$ 11,822,826	\$ 14,515,490

See Notes to Financial Statements.

The Minnesota Self-Insurers' Security Fund

**Statements of Revenues and Expenses
Years Ended June 30, 2011 and 2010**

	2011	2010
Revenues:		
General membership assessment	\$ 966,293	\$ -
Terminated member assessments	213,436	-
Investment income	2,872	4,382
Total revenues	1,182,601	4,382
Expenses:		
Claims incurred, net of recoveries and change in estimated liabilities (Note 2)	(227,255)	(978,433)
Professional fees attributed to bankruptcies	41,091	37,737
Claims administration fees	105,061	63,884
Professional and administrative	429,029	371,018
Total expenses, including change in estimated liabilities	347,926	(505,794)
Excess of revenues over expenses	\$ 834,675	\$ 510,176

**Statements of Members' Equity (Deficit)
Years Ended June 30, 2011 and 2010**

	2011	2010
Balance (deficit), beginning	\$ (8,769,154)	\$ (9,279,330)
Excess of revenues over expenses	834,675	510,176
Balance (deficit), ending	\$ (7,934,479)	\$ (8,769,154)

See Notes to Financial Statements.

The Minnesota Self-Insurers' Security Fund

**Statements of Cash Flows
Years Ended June 30, 2011 and 2010**

	2011	2010
Cash Flows From Operating Activities		
Excess of revenues over expenses	\$ 834,675	\$ 510,176
Adjustments to reconcile excess of revenues over expenses to net cash used in operating activities:		
Changes in assets and liabilities:		
Security deposit receivable	31,595	32,840
Reinsurance and other receivables	2,311,023	1,347,284
Prepaid expenses	(1,646)	22,250
Accounts payable	(16,662)	47,058
Deferred revenue	17,339	102,445
Estimated liability for incurred, incurred but unreported, and incomplete claims	(3,337,551)	(3,267,982)
Net cash used in operating activities	(161,227)	(1,205,929)
Cash Flows From Financing Activities		
Security deposit held pursuant to bankruptcy proceeding	(190,465)	(241,467)
Net cash used in financing activities	(190,465)	(241,467)
Decrease in cash and cash equivalents	(351,692)	(1,447,396)
Cash and Cash Equivalents		
Balance, beginning	1,996,339	3,443,735
Balance, ending	<u>\$ 1,644,647</u>	<u>\$ 1,996,339</u>

See Notes to Financial Statements.

The Minnesota Self-Insurers' Security Fund

Notes to Financial Statements

Note 1. Nature of Operations and Significant Accounting Policies

Nature of operations: The Minnesota Self-Insurers' Security Fund (the Fund) was incorporated under the Minnesota Non-Profit Act on September 9, 1988, and certain rights and obligations were enacted by law as of September 29, 1988. A 10-member Board of Trustees governs the Fund. The purpose of the Fund is to fulfill the obligations placed upon it by *Minnesota Statutes*, Chapter 79A, as summarized below.

Employers who are private self-insurers of workers' compensation benefits on or after July 1, 1988, in the state of Minnesota (as identified by the Commissioner of the Minnesota Department of Commerce) are required to be members of this Fund. The Commissioner makes the initial determination of which employers are qualified to be self-insured. The Commissioner also has the authority to revoke the employers' certificate to self-insure.

The Fund is liable for the administration and payment of workers' compensation benefits when a self-insured member declares bankruptcy or becomes insolvent and the Commissioner of Commerce issues a certificate of default. The Fund has the right to obtain reimbursement from the bankrupt or insolvent member, is entitled to any subrogation or reinsurance that the member was entitled to, and also has the right to receive the security deposit that the member has provided to the Commissioner of the Minnesota Department of Commerce. *Minnesota Statutes*, Chapter 79A, states that the security deposit is to be equal to 110 percent of the member's estimated future workers' compensation liability as determined by an actuary. The security deposit may be in the form of a bond, letter of credit, or cash deposit; is held and regulated by the Commissioner; and is not within the control of the Fund. If the assumed liabilities of the bankrupt or insolvent member exceed these sources of revenues, the Fund may assess its members a pro rata share (subject to annual limitation) of the funding necessary to carry out the Fund's remaining claim payment obligations and to cover the reasonable costs of administering the Fund.

The Fund has a service agreement with Berkley Risk Administrators Company (Berkley) to provide administration of claims that the Fund is responsible for. There is an annual administration fee and a fee per claim charged by Berkley. The agreement is effective through December 31, 2012.

A summary of the Fund's significant accounting policies follows:

Management estimates: The preparation of financial statements requires the trustees to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the estimated liability for incurred, incurred but unreported, and incomplete claims.

Assessments: Member assessments are recognized as revenue in the period in which the assessment is made by the Fund. Assessments are based on the members' workers' compensation indemnity benefits paid during the previous calendar year. Assessments by the Fund cannot exceed 10 percent of the indemnity benefits paid by the members during the calendar year. A 2 percent assessment was made in the year ended June 30, 2011. There was no assessment for the year ended June 30, 2010.

The Fund has the authority to assess employers who have terminated their self-insurance status. Departing members after April 1, 1998, are assessed a final amount based upon an actuarially determined discounted indemnity liability of the member on the date of departure. On August 1, 2010, the statutory exit assessment formula was changed so that members who exit must pay their proportionate share of the Fund's current liability.

The Minnesota Self-Insurers' Security Fund

Notes to Financial Statements

Note 1. Nature of Operations and Significant Accounting Policies (Continued)

Cash and cash equivalents: For purposes of reporting the statement of cash flows, the Fund considers all savings accounts, money market mutual funds, and all highly liquid debt instruments purchased with a maturity of three months or less to be cash equivalents.

The Fund maintains its cash in bank deposit, checking and money market accounts, which generally exceed federally insured limits. The Fund maintains daily sweep accounts that invest in commercial paper and repurchase agreements, which are not covered by federal insurance. At June 30, 2011, approximately \$1,699,000 was invested in these sweep accounts. The Fund has not experienced any losses in such accounts. At June 30, 2011 and 2010, cash and cash equivalents are recorded at cost, which approximates fair value because of the short-term nature of these instruments.

Estimated liability for incurred, incurred but unreported, and incomplete claims: The liabilities assumed from the bankrupt or insolvent members for incurred but not reported and incomplete claims and claim administration expenses are estimated by an independent actuary based on loss reserves, paid claims, industry data and general conditions of the environment associated with these claims. These liabilities are necessarily based on estimates, and the ultimate liability may be in excess of or less than the amounts stated. The variability of the liability is increased where there is a lack of historical data available and because the claims may be in connection with employers that are no longer in operation.

The unpaid claims and claim adjustment expense estimates are continually reviewed and, as adjustments to the estimated liabilities become necessary, such adjustments will be reflected in the year they are determined.

Reinsurance: When the Fund becomes legally liable for the claim liabilities of a bankrupt or insolvent member, it is entitled to receive any reinsurance that the member was entitled to. Under state law, all Minnesota self-insurers are required to be members of the Minnesota Workers' Compensation Reinsurance Association (WCRA). The Fund has applied for, and continues to receive, recoveries from reinsurance for certain paid claims in excess of the WCRA retention limits. The Fund has also pursued subrogation from various third parties and continues to receive recoveries. The Fund received reinsurance during 2011 and 2010 from Erieview Insurance Company, Ltd. (Erieview), a captive insurance company that reinsured the National Steel Corporation and its subsidiary, National Steel Pellet Company (National Steel) (see Note 2). Total reinsurance and subrogation recoveries on paid claims were approximately \$473,000 and \$393,000, respectively, in 2011 and 2010.

The Fund also estimates the future recoveries it expects to receive from the WCRA, Erieview and Gen Re as they relate to the estimated liability for incurred, incurred but unreported, and incomplete claims and records the expected recoveries as reinsurance receivable. The estimated amount recoverable from these reinsurers was approximately \$9,635,000 and \$11,951,000 at June 30, 2011 and 2010, respectively. Expected recoveries are netted against claims expense on the statements of revenues and expenses.

Subsequent events: The Fund has considered subsequent events through October 21, 2011, the date that the financial statements were available to be issued, in preparing the financial statements and notes thereto.

Tax status: The Fund is exempt from federal and state taxation.

The Minnesota Self-Insurers' Security Fund

Notes to Financial Statements

Note 2. Member Liabilities Assumed

The Fund, since its inception, has assumed the liabilities for the payment of workers' compensation benefits and the costs of settling these claims from 13 former members who have declared bankruptcy or are insolvent. No new member obligations were assumed in fiscal year 2011 or 2010. The Fund receives the proceeds of the bankrupt or insolvent members' security deposits and recognizes these deposits as revenue at the lesser of the deposit received or the Fund's estimate of the claim liability assumed (see Note 3). Amounts received in excess of the claims liability assumed are reported as deferred revenue.

In 2002, the Fund recorded estimated liabilities of approximately \$9,408,000 it assumed as a result of the Kmart Corporation (Kmart) bankruptcy. The Fund received a security deposit of approximately \$7,154,000. As the result of a claim in bankruptcy by the Fund, the bankruptcy court determined during 2003 that Kmart was responsible for the claims. As a result, the claim liability is not the responsibility of the Fund and it is not recorded on its balance sheet. The Fund continues to pay workers' compensation claims and claims administration fees for Kmart using the security deposit it holds until the security deposit is exhausted. Claims paid for Kmart are not included in the Fund's expenses for 2011 and 2010. The remaining security deposit held related to Kmart is reported as cash and cash equivalents on the Fund's balance sheet. A liability equal to the amount of the remaining security deposit (approximately \$985,000 at June 30, 2011) is reported on the Fund's balance sheet as security deposit held pursuant to bankruptcy proceeding. At June 30, 2011, the Fund estimates that the remaining undiscounted claims liability, net of reinsurance recoveries, exceeds the remaining security deposit by approximately \$2,701,000.

In June 2003, the Fund assumed the workers' compensation liabilities for National Steel, a former member of the Fund. Shortly after the Fund assumed these liabilities, it began pursuing reinsurance reimbursement from a National Steel-affiliated captive insurance company on several National Steel workers' compensation claims that were ceded to Erieview over multiple years. During fiscal years 2011 and 2010, claims for reinsurance were made to Erieview, and payments of approximately \$81,000 and \$70,000, respectively, have been received on these claims. Reinsurance receivable from Erieview is estimated at \$582,000 and \$849,000 at June 30, 2011 and 2010, respectively.

At June 30, 2011 and 2010, the estimated gross claim liability for National Steel recorded by the Fund is \$13,282,000 and \$16,910,000, respectively.

The Minnesota Self-Insurers' Security Fund

Notes to Financial Statements

Note 2. Member Liabilities Assumed (Continued)

Activity in the estimated liability for incurred, incurred but not reported, and incomplete claims for the years ended June 30, 2011 and 2010, is summarized as follows:

	2011	2010
Balance, beginning	\$ 21,713,000	\$ 24,981,000
Less reinsurance receivable at July 1	(11,692,000)	(13,172,000)
	<u>10,021,000</u>	<u>11,809,000</u>
Increase (decrease) in actuarial estimates over prior-year estimates	(227,000)	(978,000)
Claims paid (net of reinsurance and subrogation proceeds of \$473,000 and \$393,000 in 2011 and 2010) related to member bankruptcies	(608,000)	(810,000)
	<u>9,186,000</u>	<u>10,021,000</u>
Plus reinsurance receivable at June 30	9,189,000	11,692,000
Balance, ending	<u>\$ 18,375,000</u>	<u>\$ 21,713,000</u>

At June 30, 2011, the Fund has recorded the actuary's estimate of the liabilities it has assumed from its bankrupt or insolvent members at the undiscounted amount of \$18,375,000. If the liabilities were discounted using a 4 percent rate, the liabilities would approximate \$14,370,000.

During 2009, a member filed for bankruptcy protection. As of the date of this report, this member has not defaulted on its workers' compensation liability. The Fund and the Department of Commerce are monitoring the situation, and the Fund has retained special bankruptcy counsel. No liability was recorded as of June 30, 2011, as the Department of Commerce has not determined at this time that the Fund will be responsible for these workers' compensation claims. As of June 30, 2011, the Fund has not been notified of any members that had defaulted on their workers' compensation liability or filed for bankruptcy.

It is possible that other members may become bankrupt or insolvent in the future. The number and amount of such future liabilities that the Fund may be required to assume, if any, cannot be estimated and, accordingly, no provision for such liabilities, if any, has been made in the financial statements.

Note 3. Security Deposits Receivable and Revenue

When the Fund assumes the workers' compensation liabilities for a bankrupt or insolvent member, it receives the posted security deposit that the Commissioner is holding. The Fund recognizes the security deposit as revenue when the Commissioner notifies the Fund that the member has defaulted on its workers' compensation claims and orders the Fund to pay the member's claims. Security deposits received in excess of the actuarially determined claims liability assumed are recorded as a liability on the balance sheet. When excess security deposits are received, subsequent changes in the estimate of claims liability assumed may cause increases or decreases in revenue.

The Minnesota Self-Insurers' Security Fund

Notes to Financial Statements

Note 3. Security Deposits Receivable and Revenue (Continued)

In connection with the RisComp Industries, Inc. (RisComp) bankruptcy that occurred in 2002, RisComp posted a surety bond of \$2,996,000. The surety company exercised its option under Minnesota Statutes to administer and pay RisComp's workers' compensation benefits. In 2002, the Fund recorded the estimated liability assumed from RisComp and recognized the full amount of the surety bond as a receivable and as revenue. As the claims are paid, the liability and receivable are decreased. At June 30, 2011 and 2010, respectively, the receivable was approximately \$535,000 and \$566,000, and the estimated remaining claim liability, net of reinsurance recoveries, was approximately \$845,000 and \$873,000. No other security deposits receivable or revenue were recorded as of and for the years ended June 30, 2011 and 2010.

The receivable from the surety company is subject to the risk that the surety company may be unable or unwilling to pay claims in the future.

Note 4. Funding Policy and Subsequent Event

The Fund's primary source of revenue with which to pay liabilities that it has assumed from its bankrupt or insolvent members is the security, which has been posted with the Minnesota Department of Commerce. The Fund also receives revenue from a terminating member assessment that is levied on any member when they no longer self-insure. In the event that revenue is inadequate to pay claims, the Fund may assess all members to make up the deficiency. The Fund recognizes the revenue from the bankrupt or insolvent member's security when it is notified by the Commissioner and records the estimated liabilities that it has assumed from its bankrupt or insolvent members (see Note 2) when those liabilities are known. The Fund does not recognize the revenue that will be received from future members' assessments, which will be used to retire any excess liabilities, until the assessments are actually made to the members. The Fund's policy is to assess its members (within limits provided by state of Minnesota statutes) only when an amount is necessary to meet the annual cash flow requirements of the Fund if other sources of revenue are inadequate to pay claims and operating expenses for that year. A history of member assessments may be obtained on the Internet at www.mnsisf.org.

In July 2011, the Fund made a 2 percent assessment to the members for approximately \$929,000.