

SAIF Corporation

(A Component Unit of the State of Oregon)

*Financial Statements and Supplementary
Schedules as of and for the Years
Ended December 31, 2015 and 2014, and
Report of Independent Auditors*

SAIF CORPORATION

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OVERVIEW OF SAIF CORPORATION FINANCIAL REPORTING

SAIF Corporation (SAIF) has prepared the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America. As a discrete component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board (GASB). Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as a special purpose government engaged solely in business-type activities. Accordingly, SAIF follows the accrual basis of accounting. Revenues are recognized when earned, regardless of when received, and expenses are recognized when incurred, regardless of when paid.

SAIF also prepares financial statements in conformity with statutory accounting practices, which are prescribed for use in reporting accounting transactions for insurance companies. These practices arise from state laws and from rules adopted by the State Insurance Commissioner and, for Oregon, are the practices promulgated by the National Association of Insurance Commissioners (NAIC). Statutory accounting practices are conservative in nature and are designed to protect policyholders and claimants to ensure that, in the event of liquidation, sufficient amounts will have been set aside to provide for the outstanding claims of injured workers and their dependents, whereas generally accepted accounting principles (GAAP) are based on the going-concern concept and recognize revenues when earned and expenses when incurred.

There are significant differences between the statutory statements that SAIF prepares for regulatory and management purposes and the accompanying financial statements. They include:

- Statutory accounting requires the majority of invested assets to be recorded at amortized cost, whereas investments are stated at fair value in the accompanying statements with the corresponding change in the fair value for the year recorded as investment income.
- Statutory accounting does not allow the accrual of policyholder dividends until declared by the Board of Directors. GAAP requires the accrual of estimated policyholder dividends.
- Statutory accounting requires that certain assets not readily available for the payment of claims be "nonadmitted" and removed from the statement of net position. Those assets, such as property and equipment, are included on the GAAP financial statements.

REPORT OF INDEPENDENT AUDITORS

The Board of Directors of
SAIF Corporation

The Secretary of State Audits Division of
The State of Oregon

Report on the Financial Statements

We have audited the accompanying financial statements of SAIF Corporation ("SAIF"), a component unit of the State of Oregon, as of and for the years ended December 31, 2015 and 2014, and the related notes to the financial statements, which collectively comprise SAIF'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 opinions 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 SAIF's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

Opinions

In our opinion, the financial statements referred to previously present fairly, in all material respects, the respective financial position of SAIF Corporation as of December 31, 2015 and 2014, and the respective changes in financial position, and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

REPORT OF INDEPENDENT AUDITORS (continued)

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 4 through 12 and postemployment healthcare benefit plan schedule of funding progress and employer contributions and defined benefit pension plan schedule of proportionate share of the net pension liability (asset) and employer contributions on pages 40 through 41 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 opinions on the financial statements that collectively comprise SAIF's basic financial statements. The introductory section titled, Overview of SAIF Corporation Financial Reporting, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The Overview of SAIF Corporation Financial Reporting has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated July 28, 2016 on our consideration of SAIF Corporation'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 SAIF Corporation's internal control over financial reporting and compliance.

Moss Adams LLP

Portland, Oregon
July 28, 2016

SAIF CORPORATION
Management's Discussion and Analysis
December 31, 2015 and 2014

Management of SAIF Corporation (SAIF) prepares Management's Discussion and Analysis for readers of SAIF's financial statements. This narrative overview and analysis of the financial activities of SAIF is as of and for the years ended December 31, 2015 and 2014. Readers are encouraged to consider this information in conjunction with SAIF's financial statements and notes that follow.

Financial Statements

This discussion and analysis is intended to serve as an introduction to SAIF's financial statements: the Statements of Net Position; the Statements of Revenues, Expenses, and Changes in Net Position; and the Statements of Cash Flows. The financial statements are designed to provide the readers with an overview of SAIF's financial position and activities.

The Statements of Net Position present information on SAIF's assets, deferred outflows of resources, liabilities, and deferred inflows of resources, with the difference reported as net position. Assets and liabilities are classified as either current or noncurrent.

The Statements of Revenues, Expenses, and Changes in Net Position are SAIF's income statements. Revenues earned and expenses incurred during the year are classified as either operating or nonoperating.

The Statements of Cash Flows present the changes in SAIF's cash and cash equivalents during the year. These statements are prepared using the direct method of cash flows. The statements break out the sources and uses of SAIF's cash and cash equivalents into the following categories: operating activities, investing activities, and capital and related financing activities.

**Condensed Financial Information
(In thousands)**

Condensed Statements of Net Position Information

| | <u>2015</u> | <u>December 31, 2014</u> | <u>2013</u> | <u>2014 to 2015 Increase (Decrease)</u> | <u>2013 to 2014 Increase (Decrease)</u> |
|---|---------------------|------------------------------|---------------------|---|---|
| ASSETS | | | | | |
| CURRENT ASSETS: | | | | | |
| Cash and cash equivalents | \$ 40,778 | \$ 42,199 | \$ 58,376 | \$ (1,421) | \$ (16,177) |
| Investments | 4,409,271 | 4,512,514 | 4,323,985 | (103,243) | 188,529 |
| Securities lending cash collateral | 52,272 | 146,178 | 172,668 | (93,906) | (26,490) |
| Accounts and interest receivable, net | 404,161 | 395,337 | 385,546 | 8,824 | 9,791 |
| Other assets | <u>246</u> | <u>813</u> | <u>148</u> | <u>(567)</u> | <u>665</u> |
| Total current assets | <u>4,906,728</u> | <u>5,097,041</u> | <u>4,940,723</u> | <u>(190,313)</u> | <u>156,318</u> |
| NONCURRENT ASSETS—Capital assets, net | <u>15,267</u> | <u>14,311</u> | <u>15,075</u> | <u>956</u> | <u>(764)</u> |
| Total assets | <u>4,921,995</u> | <u>5,111,352</u> | <u>4,955,798</u> | <u>(189,357)</u> | <u>155,554</u> |
| DEFERRED OUTFLOWS OF RESOURCES | | | | | |
| Related to pensions | <u>5,604</u> | <u>-</u> | <u>-</u> | <u>5,604</u> | <u>-</u> |
| Total deferred outflows of resources | <u>5,604</u> | <u>-</u> | <u>-</u> | <u>5,604</u> | <u>-</u> |
| LIABILITIES | | | | | |
| CURRENT LIABILITIES: | | | | | |
| Reserve for losses and loss adjustment expenses | 261,404 | 255,309 | 251,185 | 6,095 | 4,124 |
| Unearned premiums | 226,901 | 223,501 | 217,434 | 3,400 | 6,067 |
| Accounts payable | 88,626 | 84,707 | 74,720 | 3,919 | 9,987 |
| Obligations under securities lending | 52,284 | 146,180 | 172,633 | (93,896) | (26,453) |
| Other liabilities and deposits | <u>73,487</u> | <u>60,312</u> | <u>53,385</u> | <u>13,175</u> | <u>6,927</u> |
| Total current liabilities | <u>702,702</u> | <u>770,009</u> | <u>769,357</u> | <u>(67,307)</u> | <u>652</u> |
| NONCURRENT LIABILITIES: | | | | | |
| Reserve for losses and loss adjustment expenses | 2,647,214 | 2,706,754 | 2,790,190 | (59,540) | (83,436) |
| Other postemployment benefits obligation | 4,427 | 3,993 | 3,029 | 434 | 964 |
| Pension related payable | 10,205 | - | - | 10,205 | - |
| Net pension liability | <u>34,187</u> | <u>-</u> | <u>-</u> | <u>34,187</u> | <u>-</u> |
| Total noncurrent liabilities | <u>2,696,033</u> | <u>2,710,747</u> | <u>2,793,219</u> | <u>(14,714)</u> | <u>(82,472)</u> |
| Total liabilities | <u>3,398,735</u> | <u>3,480,756</u> | <u>3,562,576</u> | <u>(82,021)</u> | <u>(81,820)</u> |
| DEFERRED INFLOWS OF RESOURCES | | | | | |
| Related to pensions | <u>7,894</u> | <u>-</u> | <u>-</u> | <u>7,894</u> | <u>-</u> |
| Total deferred inflows of resources | <u>7,894</u> | <u>-</u> | <u>-</u> | <u>7,894</u> | <u>-</u> |
| NET POSITION: | | | | | |
| Net investment in capital assets | 15,267 | 14,311 | 15,075 | 956 | (764) |
| Unrestricted | <u>1,505,703</u> | <u>1,616,285</u> | <u>1,378,147</u> | <u>(110,582)</u> | <u>238,138</u> |
| Total net position | <u>\$ 1,520,970</u> | <u>\$ 1,630,596</u> | <u>\$ 1,393,222</u> | <u>\$ (109,626)</u> | <u>\$ 237,374</u> |

**Condensed Revenues, Expenses,
and Changes in Net Position Information**

| | Years Ended December 31, | | | 2014 to 2015 | 2013 to 2014 |
|---|--------------------------|---------------------|---------------------|------------------------|------------------------|
| | 2015 | 2014 | 2013 | Increase (Decrease) | Increase (Decrease) |
| OPERATING REVENUES: | | | | | |
| Net premiums earned | \$ 491,229 | \$ 474,355 | \$ 435,671 | \$ 16,874 | \$ 38,684 |
| Other income | <u>29,980</u> | <u>28,540</u> | <u>27,210</u> | <u>1,440</u> | <u>1,330</u> |
| Total operating revenues | <u>521,209</u> | <u>502,895</u> | <u>462,881</u> | <u>18,314</u> | <u>40,014</u> |
| OPERATING EXPENSES: | | | | | |
| Net losses and loss adjustment expenses incurred | 325,679 | 270,861 | 316,818 | 54,818 | (45,957) |
| Policyholders' dividends | 119,993 | 164,950 | 129,145 | (44,957) | 35,805 |
| Underwriting expenses | 141,016 | 120,304 | 112,157 | 20,712 | 8,147 |
| Bad debt provision | <u>1,119</u> | <u>1,480</u> | <u>925</u> | <u>(361)</u> | <u>555</u> |
| Total operating expenses | <u>587,807</u> | <u>557,595</u> | <u>559,045</u> | <u>30,212</u> | <u>(1,450)</u> |
| OPERATING LOSS | <u>(66,598)</u> | <u>(54,700)</u> | <u>(96,164)</u> | <u>(11,898)</u> | <u>41,464</u> |
| NONOPERATING REVENUES: | | | | | |
| Net investment income (loss) | <u>(22,939)</u> | <u>292,074</u> | <u>85,801</u> | <u>(315,013)</u> | <u>206,273</u> |
| INCREASE (DECREASE) IN NET POSITION | <u>(89,537)</u> | <u>237,374</u> | <u>(10,363)</u> | <u>(326,911)</u> | <u>247,737</u> |
| NET POSITION—Beginning of year | 1,630,596 | 1,393,222 | 1,403,585 | 237,374 | (10,363) |
| Prior period adjustments (see note 2) | (11,071) | - | - | (11,071) | - |
| Cumulative effect of change in accounting principles (see note 2) | <u>(9,018)</u> | <u>-</u> | <u>-</u> | <u>(9,018)</u> | <u>-</u> |
| RESTATEMENT—Beginning net position | <u>1,610,507</u> | <u>1,393,222</u> | <u>1,403,585</u> | <u>217,285</u> | <u>(10,363)</u> |
| NET POSITION—End of year | <u>\$ 1,520,970</u> | <u>\$ 1,630,596</u> | <u>\$ 1,393,222</u> | <u>\$ (109,626)</u> | <u>\$ 237,374</u> |

Financial position as of December 31, 2015

At the end of 2015, total assets decreased \$189.4 million from the prior year, and deferred outflows of resources increased \$5.6 million. Total liabilities decreased \$82.0 million for the year, deferred inflows of resources increased \$7.9 million, and net position decreased \$109.6 million (as restated). The restatement of net position includes a prior period adjustment to record a pension related payable (see note 10), which decreased net position by \$11.1 million. In addition, the cumulative effect of change in accounting principles due to GASB 68 implementation decreased net position by \$9.0 million. See note 2 new accounting pronouncements for additional information on the amounts restated due to GASB 68 implementation.

Significant changes include:

Cash and cash equivalents—The majority of SAIF's cash accounts consist of short-term investments and money market funds utilized by external investment managers. Cash and cash equivalents decreased \$1.4 million from December 31, 2014 to December 31, 2015. A \$3.9 million decrease in cash was offset by a \$2.5 million increase in money market fund balances held by the fixed income managers.

Investments—At the end of 2015, investments were \$103.2 million or 2.3 percent lower than at the end of 2014. SAIF's asset allocation was in compliance with the asset allocation policy as of December 31, 2015. Investment holdings (principal and cost) increased \$76.8 million for bonds and decreased \$0.1 million for equities. Bond holdings increased due to the reinvestment of investment income offset somewhat by the withdrawal of bond principal to fund the policyholder dividend payment. Market values decreased \$171.7 million for bonds and decreased \$8.2 million for equities. The BlackRock MSCI ACWI fund had a negative return of 1.85 percent for 2015.

Securities lending cash collateral—This line item can fluctuate significantly from period to period depending on the amount of investment securities on loan. The amount of securities on loan will vary depending on market conditions and the demand for certain securities in SAIF's portfolio. During 2015, these balances have decreased significantly, as lending costs have increased due to regulation changes.

Accounts and interest receivable—The balance in this line is comprised of investment income receivable, net premiums receivable, accrued retrospective premiums receivable, and other accounts receivable. This balance increased \$8.8 million or 2.2 percent from December 31, 2014 to December 31, 2015.

Accrued investment income decreased \$0.8 million or 2.1 percent from December 31, 2014 to December 31, 2015.

Premiums receivable increased \$10.1 million or 3.3 percent in 2015, due to the growth in premiums. Net written premiums increased 2.7 percent from 2014 to 2015.

Accrued retrospective premiums receivable decreased \$0.7 million or 3.1 percent due to favorable loss reserve development.

Other accounts receivable increased \$0.2 million or 0.8 percent in 2015, primarily due to an increase in premium assessment receivables.

Other assets—This line had no significant change from 2014 to 2015.

Deferred outflows of resources—The \$5.6 million balance in this line is related to pensions due to GASB Statement No. 68 implementation at December 31, 2015 (see note 10).

Reserve for losses and loss adjustment expenses—The total (current and noncurrent) reserve for losses and loss adjustment expenses (LAE) decreased \$53.4 million or 1.8 percent from the prior year. Loss reserves decreased \$60.7 million or 2.4 percent and LAE reserves increased \$7.3 million or 1.7 percent during 2015. Loss reserves for the 2015 accident year were offset by favorable loss reserve development in prior accident years. The favorable loss reserve development was attributed primarily to permanent total and permanent partial disability medical loss reserves. The key drivers were a decrease in ultimate counts and the continuing downward trend in medical severity. The observed medical escalation rate for 2015 was well below the assumption. Indemnity loss reserves experienced favorable development driven by actual costs for permanent total disability being lower than expected for recent accident years and the reduction in ultimate projected counts for fatal. LAE reserves for the 2015 accident year were offset by favorable loss reserve development in prior accident years. The favorable LAE reserve development was largely attributable to the overall reduction in reserves.

Unearned premiums—The amount of unearned premium for 2015 increased \$3.4 million or 1.5 percent due to the increase in premium.

Accounts payable—The balance in this line is comprised of commissions payable, reinsurance payable, accrued premium assessment, and other accounts payable. This line increased \$3.9 million from 2014 to 2015. The \$0.2 million increase in commission payable and the \$2.2 million increase in premium assessment payable are due to the growth in premium. Reinsurance payable increased \$1.6 million due to an increase in the balance due to the assigned risk pool. Other accounts payable decreased \$0.1 million from 2014 to 2015.

Obligations under securities lending—This line item can fluctuate significantly from period to period depending on the amount of investment securities on loan. The amount of securities on loan will vary depending on market conditions and the demand for certain securities in SAIF's portfolio. During 2015, these balances have decreased significantly, as lending costs have increased due to regulation changes.

Other liabilities and deposits—The balance in this line is comprised of accrued retrospective premiums payable, premium deposits, amounts due to brokers for security purchases, amounts due to other governments, and compensated absences payable. This balance increased \$13.2 million or 21.8 percent from the prior year, primarily due to an \$11.7 million increase in the estimated amount of return premium payable on retrospectively rated policies, a \$1.1 million increase in premium deposits, and the recording of a \$0.4 million current portion of the pension related payable.

Pension related payable—Prior to the formation of the PERS State and Local Government Rate Pool (SLGRP), the State and community colleges were pooled together in the State and Community College Pool (SCCP), while local government employers participated in the Local Government Rate Pool (LGRP). The unfunded actuarial liability (UAL) attributable to the SCCP at the time the SLGRP was formed is maintained separately from the SLGRP and is reduced by contributions and increased for interest charges at the assumed interest rate, which was 7.75 percent in fiscal year 2015. The \$10.2 million increase in this line is the noncurrent portion of the pre-SLGRP pooled liability attributable to SAIF, which is being amortized over the period ending December 31, 2027.

Net pension liability—The \$34.2 million increase in this line is SAIF’s portion of the net pension liability allocated by the State of Oregon due to GASB Statement No. 68 implementation at December 31, 2015 (see note 10).

Deferred inflows of resources—The \$7.9 million balance in this line is related to pensions due to GASB Statement No. 68 implementation at December 31, 2015 (see note 10).

Operations - year ended December 31, 2015

Significant changes in revenues and expenses include:

Net premiums earned—In 2015, net premiums earned increased \$16.9 million or 3.6 percent. The increase was due to new sales and higher reported payrolls by policyholders and was tempered by a 5.3 percent decrease to pure premium rates effective January 1, 2015.

Other income—This line increased \$1.4 million or 5.0 percent in 2015, due to an increase in premium assessment income as a result of the growth in premium.

Net losses and loss adjustment expenses incurred—Net losses incurred for the current year increased \$38.3 million from 2014, while net LAE incurred increased \$16.5 million for a total net increase of \$54.8 million. Net paid losses for 2015 were \$9.6 million higher than the prior year, and the change in loss reserves was \$28.7 million more than the prior year. The favorable loss reserve development for 2015 was attributed primarily to permanent total and permanent partial disability medical loss reserves. The key drivers were a decrease in ultimate counts and the continuing downward trend in medical severity. The observed medical escalation rate for 2015 was well below the assumption. Indemnity loss reserves experienced favorable development driven by actual costs for permanent total disability being lower than expected for recent accident years and the reduction in ultimate projected counts for fatal. LAE incurred increased as reserves for the 2015 accident year were offset by favorable loss reserve development in prior accident years. The favorable LAE development was largely attributable to the overall reduction in loss reserves.

Policyholders’ dividends—Substantially all of SAIF’s business is written under various participating plans wherein a dividend may be returned to the policyholder. Dividends may be paid to the extent that a surplus is accumulated from premiums, investment gains, and/or loss reserve reductions. In 2015, policyholder dividends of \$120.0 million were incurred and paid to qualifying policyholders. In 2014, policyholder dividends of \$165.0 million were incurred and paid to qualifying policyholders.

Underwriting expense—This line increased \$20.7 million or 17.2 percent in 2015, due to an increase in premium and the implementation of GASB 68.

Net investment income—Net investment income for 2015 was \$315.0 million lower than the amount recorded for 2014, primarily due to a significant decrease in bond market values. The change in fair value of investments recorded for 2015 was a negative \$179.9 million compared to a positive \$97.4 million for 2014. Net realized investment gains were \$8.0 million for 2015, compared to net realized gains of \$46.9 million for 2014. For 2015, net realized gains from bonds were \$7.9 million, while net realized gains on equity sales were \$0.1 million. In addition, the payment of policyholder dividends during the past six years has reduced the opportunity for investment income.

Economic outlook

It is anticipated that the economy and unemployment rates will continue to improve during 2016, although at a slower rate than recent years. The 5.3 percent pure premium rate reduction approved for 2016 may off-set premium growth due to new sales and increased payrolls during 2016.

The 2016 capital budget includes \$29.9 million and the operating budget includes \$2.4 million in funds to support a home office renovation project. During 2016, the predesign and schematic design development phases of the project will be completed and construction will begin. As of December 31, 2015, SAIF has total future commitments of \$5.5 million for expenditures related to the project through contracts currently in place.

The 2016 budget also includes \$3.9 million for a policy and billing system replacement project. During 2016, consultants will be hired for system development and staff augmentation.

Financial position as of December 31, 2014

At the end of 2014, total assets increased \$155.6 million from the prior year. Total liabilities decreased \$81.8 million for the year, and net position increased \$237.4 million.

Significant changes include:

Cash and cash equivalents—The majority of SAIF's cash accounts consist of short-term investments and money market funds utilized by external investment managers. Cash and cash equivalents decreased \$16.2 million from December 31, 2013 to December 31, 2014, primarily due to a decrease in the money market fund balances held by the fixed income managers.

Investments—At the end of 2014, investments were \$188.5 million or 4.4 percent higher than at the end of 2013. SAIF's asset allocation was in compliance with the asset allocation policy as of December 31, 2014. Investment holdings (principal and cost) increased \$131.0 million for bonds and decreased \$40.0 million for equities. Bond holdings increased due to the reinvestment of investment income offset somewhat by the withdrawal of bond principal to fund the policyholder dividend payment. The decrease in equities was due to withdrawals to fund the policyholder dividend. Market values increased \$99.0 million for bonds and decreased \$1.5 million for equities. The BlackRock MSCI ACWI fund had a positive return of 4.2 percent for 2014.

Securities lending cash collateral—This line item can fluctuate significantly from period to period depending on the amount of investment securities on loan. The amount of securities on loan will vary depending on market conditions and the demand for certain securities in SAIF's portfolio.

Accounts and interest receivable—The balance in this line is comprised of investment income receivable, net premiums receivable, accrued retrospective premiums receivable, and other accounts receivable. This balance increased \$9.8 million or 2.5 percent from December 31, 2013 to December 31, 2014.

Accrued investment income increased \$633 thousand or 1.7 percent from December 31, 2013 to December 31, 2014.

Premiums receivable increased \$11.3 million or 3.8 percent in 2014, due to the growth in premiums. Net written premiums increased 5.7 percent from 2013 to 2014.

Accrued retrospective premiums receivable decreased \$6.8 million or 23.3 percent due to favorable loss reserve development, primarily for the State of Oregon's retrospectively rated policies.

Other accounts receivable increased \$4.7 million or 20.2 percent in 2014. Receivables due from the assigned risk pool increased \$5.0 million due to a change to gross up receivables and payables related to the pool, and reinsurance recoverable decreased \$0.3 million.

Other assets—This line had no significant change from 2013 to 2014.

Reserve for losses and loss adjustment expenses—The total (current and noncurrent) reserve for losses and loss adjustment expenses (LAE) decreased \$79.3 million or 2.6 percent from the prior year. Loss reserves decreased \$89.8 million or 3.4 percent and LAE reserves increased \$10.5 million or 2.6 percent during 2014. Loss reserves for the 2014 accident year were offset by favorable loss reserve development in prior accident years. The favorable loss reserve development was attributed primarily to permanent total and permanent partial disability medical loss reserves. The key drivers were a decrease in the tail factor and the continuing downward trend in medical severity. The observed medical escalation rate for 2014 was well below the assumption. Indemnity loss reserves experienced unfavorable development as indemnity costs for recent accident years were higher than expected. LAE reserves for the 2014 accident year were offset by favorable loss reserve development in prior accident years. The favorable LAE development was largely attributable to the overall reduction in reserves.

Unearned premiums—The amount of unearned premium for 2014 increased \$6.1 million or 2.8 percent due to the increase in premium.

Accounts payable—The balance in this line is comprised of commissions payable, reinsurance payable, accrued premium assessment, and other accounts payable. This line increased \$10.0 million from 2013 to 2014. The \$0.7 million increase in commission payable and the \$1.8 million increase in premium assessment payable are due to the growth in premium. Reinsurance payable increased \$3.9 million due to a change to gross up receivables and payables related to the assigned risk pool. Other accounts payable increased \$3.6 million from 2013 to 2014, primarily due to a \$2.8 million increase in policyholder credits.

Obligations under securities lending—This line item can fluctuate significantly from period to period depending on the amount of investment securities on loan. The amount of securities on loan will vary depending on market conditions and the demand for certain securities in SAIF's portfolio.

Other liabilities and deposits—The balance in this line is comprised of accrued retrospective premiums payable, premium deposits, amounts due to brokers for security purchases, amounts due to other governments, and compensated absences payable. This balance increased \$6.9 million or 13.0 percent from the prior year, primarily due to a \$5.6 million increase in the estimated amount of return premium payable on retrospectively rated policies, and a \$1.6 million increase in premium deposits.

Operations - year ended December 31, 2014

Significant changes in revenues and expenses include:

Net premiums earned—In 2014, net premiums earned increased \$38.7 million or 8.9 percent. The increase was due to new sales and higher reported payrolls by policyholders and tempered by a 7.6 percent decrease to pure premium rates effective January 1, 2014.

Other income—This line increased \$1.3 million or 4.9 percent in 2014, due to an increase in premium assessment income as a result of the growth in premium.

Net losses and loss adjustment expenses incurred—Net losses incurred for 2014 decreased by \$43.3 million from 2013, while net LAE incurred decreased \$2.7 million for a total net decrease of \$46.0 million. The favorable loss reserve development was attributed primarily to permanent total and permanent partial disability medical loss reserves. The key drivers were a decrease in the tail factor and the continuing downward trend in medical severity. The observed medical escalation rate for 2014 was well below the assumption. Indemnity loss reserves experienced unfavorable development driven by higher than expected actual counts for fatal claims and an increase in severity for permanent total disability claims. LAE incurred decreased as reserves for the 2014 accident year were offset by favorable loss reserve development in prior accident years. The favorable LAE development was largely attributable to the overall reduction in reserves.

Policyholders' dividends—Substantially all of SAIF's business is written under various participating plans wherein a dividend may be returned to the policyholder. Dividends may be paid to the extent that a surplus is accumulated from premiums, investment gains, and/or loss reserve reductions. In 2014, policyholder dividends of \$165.0 million were incurred and paid to qualifying policyholders. In 2013, policyholder dividends of \$129.1 million and \$129.2 million were incurred and paid, respectively, to qualifying policyholders.

Underwriting expense—This line increased \$8.1 million or 7.3 percent in 2014, due to an increase in premium.

Net investment income—Net investment income for 2014 was \$206.3 million higher than the amount recorded for 2013, primarily due to a significant increase in bond market values. The change in fair value of investments recorded for 2014 was a positive \$97.4 million compared to a negative \$111.9 million for 2013. Net realized investment gains were \$46.9 million for 2014, compared to net realized gains of \$51.3 million for 2013. For 2014, net realized gains from bonds were \$26.7 million, while net realized gains on equity sales were \$20.2 million. Investment income increased \$1.8 million from 2013 to 2014, and has been adversely affected by relatively low yields on high quality securities as bonds that were sold or matured with higher yields were replaced with lower yield securities. In addition, the payment of policyholder dividends during the past several years has reduced the opportunity for investment income.

SAIF CORPORATION

**STATEMENTS OF NET POSITION
AS OF DECEMBER 31, 2015 AND 2014
(In thousands)**

| | <u>2015</u> | <u>2014</u> |
|---|---------------------|---------------------|
| ASSETS | | |
| CURRENT ASSETS: | | |
| Cash and cash equivalents | \$ 40,778 | \$ 42,199 |
| Investments | 4,409,271 | 4,512,514 |
| Securities lending cash collateral | 52,272 | 146,178 |
| Investment income receivable | 36,200 | 36,984 |
| Premiums receivable, net | 318,364 | 308,284 |
| Accrued retrospective premiums receivable | 21,693 | 22,382 |
| Accounts receivable | 27,904 | 27,687 |
| Other assets | <u>246</u> | <u>813</u> |
| Total current assets | <u>4,906,728</u> | <u>5,097,041</u> |
| NONCURRENT ASSETS—Capital assets, net | <u>15,267</u> | <u>14,311</u> |
| Total assets | <u>4,921,995</u> | <u>5,111,352</u> |
| DEFERRED OUTFLOWS OF RESOURCES | | |
| Related to pensions | <u>5,604</u> | <u>-</u> |
| Total deferred outflows of resources | <u>5,604</u> | <u>-</u> |
| LIABILITIES | | |
| CURRENT LIABILITIES: | | |
| Reserve for losses and loss adjustment expenses | 261,404 | 255,309 |
| Unearned premiums | 226,901 | 223,501 |
| Accrued retrospective premiums payable | 52,012 | 40,303 |
| Commissions payable | 13,487 | 13,242 |
| Reinsurance payable | 12,936 | 11,342 |
| Accrued premium assessment payable | 28,873 | 26,649 |
| Premium deposits | 15,295 | 14,154 |
| Accounts payable | 33,330 | 33,473 |
| Obligations under securities lending | 52,284 | 146,180 |
| Pension related payable | 433 | - |
| Other liabilities | <u>5,747</u> | <u>5,856</u> |
| Total current liabilities | <u>702,702</u> | <u>770,009</u> |
| NONCURRENT LIABILITIES: | | |
| Reserve for losses and loss adjustment expenses | 2,647,214 | 2,706,754 |
| Other postemployment benefits obligation | 4,427 | 3,993 |
| Pension related payable | 10,205 | - |
| Net Pension Liability | <u>34,187</u> | <u>-</u> |
| Total noncurrent liabilities | <u>2,696,033</u> | <u>2,710,747</u> |
| Total liabilities | <u>3,398,735</u> | <u>3,480,756</u> |
| DEFERRED INFLOWS OF RESOURCES | | |
| Related to pensions | <u>7,894</u> | <u>-</u> |
| Total deferred inflows of resources | <u>7,894</u> | <u>-</u> |
| NET POSITION: | | |
| Net investment in capital assets | 15,267 | 14,311 |
| Unrestricted | <u>1,505,703</u> | <u>1,616,285</u> |
| Total net position | <u>\$ 1,520,970</u> | <u>\$ 1,630,596</u> |

See notes to financial statements.

SAIF CORPORATION

**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014
(In thousands)**

| | <u>2015</u> | <u>2014</u> |
|--|---------------------|---------------------|
| OPERATING REVENUES: | | |
| Net premiums earned | \$ 491,229 | \$ 474,355 |
| Other income | <u>29,980</u> | <u>28,540</u> |
| Total operating revenues | <u>521,209</u> | <u>502,895</u> |
| OPERATING EXPENSES: | | |
| Net losses and loss adjustment expenses incurred | 325,679 | 270,861 |
| Policyholders' dividends | 119,993 | 164,950 |
| Underwriting expenses | 141,016 | 120,304 |
| Bad debt provision | <u>1,119</u> | <u>1,480</u> |
| Total operating expenses | <u>587,807</u> | <u>557,595</u> |
| OPERATING LOSS | <u>(66,598)</u> | <u>(54,700)</u> |
| NONOPERATING REVENUES: | | |
| Investment income | (16,187) | 298,714 |
| Investment expenses | <u>(6,752)</u> | <u>(6,640)</u> |
| Net investment income (loss) | <u>(22,939)</u> | <u>292,074</u> |
| INCREASE (DECREASE) IN NET POSITION | <u>(89,537)</u> | <u>237,374</u> |
| NET POSITION—Beginning of year | 1,630,596 | 1,393,222 |
| Prior period adjustments | (11,071) | - |
| Cumulative effect of change in accounting principles | <u>(9,018)</u> | <u>-</u> |
| RESTATEMENT--Beginning net position | <u>1,610,507</u> | <u>1,393,222</u> |
| NET POSITION—End of year | <u>\$ 1,520,970</u> | <u>\$ 1,630,596</u> |

See notes to financial statements.

SAIF CORPORATION

**STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014
(In thousands)**

| | <u>2015</u> | <u>2014</u> |
|--|------------------|------------------|
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Premiums collected, net of reinsurance | \$ 499,683 | \$ 487,004 |
| Loss and loss adjustment expenses paid | (379,124) | (350,173) |
| Underwriting expenses paid | (141,016) | (120,304) |
| Policyholder dividends paid | (119,993) | (164,950) |
| Other receipts | <u>59,227</u> | <u>30,395</u> |
| Net cash used in operating activities | <u>(81,223)</u> | <u>(118,028)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of investments | (1,230,677) | (1,093,519) |
| Proceeds from sales and maturities of investments | 1,145,755 | 1,037,175 |
| Interest received on investments and cash balances | 166,161 | 158,333 |
| Interest received from securities lending | 601 | 411 |
| Interest paid for securities lending | <u>(181)</u> | <u>(93)</u> |
| Net cash provided by investing activities | <u>81,659</u> | <u>102,307</u> |
| CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES: | | |
| Acquisition of capital assets | (1,918) | (482) |
| Proceeds from disposition of capital assets | <u>61</u> | <u>26</u> |
| Net cash used in capital and related financing activities | <u>(1,857)</u> | <u>(456)</u> |
| NET DECREASE IN CASH AND CASH EQUIVALENTS | (1,421) | (16,177) |
| CASH AND CASH EQUIVALENTS—Beginning of year | <u>42,199</u> | <u>58,376</u> |
| CASH AND CASH EQUIVALENTS—End of year | <u>\$ 40,778</u> | <u>\$ 42,199</u> |

(Continued)

SAIF CORPORATION

**STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014
(In thousands)**

| | <u>2015</u> | <u>2014</u> |
|---|--------------------|---------------------|
| RECONCILIATION OF OPERATING LOSS TO NET CASH PROVIDED BY OPERATING ACTIVITIES: | | |
| Operating loss | \$ (66,598) | \$ (54,700) |
| Adjustments to reconcile operating loss to net cash provided by | | |
| Operating activities: | | |
| Depreciation and amortization | 1,124 | 1,192 |
| Bad debt provision | 1,118 | 1,480 |
| Net changes in assets and liabilities: | | |
| Premiums receivable, net | (11,198) | (12,778) |
| Accrued retrospective premiums receivable | 689 | 6,799 |
| Accounts receivable | (216) | (4,659) |
| Other assets | 6 | 5 |
| Reserve for losses and loss adjustment expenses | (53,445) | (79,312) |
| Unearned premiums | 3,400 | 6,067 |
| Accrued retrospective premiums payable | 11,709 | 5,583 |
| Commissions payable | 245 | 638 |
| Reinsurance payable | 1,594 | 3,918 |
| Accrued premium assessment payable | 2,224 | 1,816 |
| Premium deposits | 1,142 | 1,581 |
| Accounts payable | (367) | 3,615 |
| Other liabilities | (110) | (236) |
| Net pension liability | 46,538 | - |
| Pension related payable | (433) | - |
| Other postemployment benefits obligation | 434 | 963 |
| (Increase)/decrease in deferred outflows of resources: | | |
| Related to pensions | (3,140) | - |
| Increase/(decrease) in deferred inflows of resources: | | |
| Related to pensions | <u>(15,939)</u> | <u>-</u> |
| Total adjustments | <u>(14,625)</u> | <u>(63,328)</u> |
| NET CASH USED IN OPERATING ACTIVITIES | <u>\$ (81,223)</u> | <u>\$ (118,028)</u> |
| SUPPLEMENTAL SCHEDULE OF NONCASH INVESTING ACTIVITIES: Investments acquired and sold through conversions and tax free exchange transactions | <u>\$ 63,121</u> | <u>\$ 37,645</u> |

See notes to financial statements.

SAIF CORPORATION

NOTES TO FINANCIAL STATEMENTS

AS OF AND FOR THE YEARS ENDED DECEMBER 31, 2015 AND 2014

1. DESCRIPTION OF BUSINESS & REGULATORY ENVIRONMENT

SAIF Corporation (SAIF) is a public corporation created by an act of the Oregon Legislature. It traces its origins to 1914 when its predecessor organization commenced business.

SAIF is an insurance company authorized to write workers' compensation coverage in Oregon and is a servicing carrier for accounts in the assigned risk pool. SAIF also provides coverage governed by the Longshore and Harbor Workers' Compensation Act, Jones Act, and Federal Employers Liability Law. SAIF has partnered with Zurich American Insurance Company and United States Insurance Services to provide other states coverage effective February 1, 2011. SAIF's Board of Directors is appointed by the governor of the State of Oregon and consists of Oregon business and community leaders not otherwise in the employ of SAIF. Certain members of SAIF's Board of Directors are SAIF policyholders or are employed by SAIF policyholders. The transactions between SAIF and these policyholders were within SAIF's standard terms and conditions.

SAIF writes business on a direct basis as well as through agents. Premiums written on a direct basis were 20.0 percent and 22.7 percent of standard premium during 2015 and 2014, respectively. SAIF issues workers' compensation insurance policies to individual Oregon employers including state agencies.

The Oregon Department of Consumer and Business Services (DCBS) enforces workers' compensation laws under the Oregon Revised Statutes (ORS). Under the reporting requirements of the DCBS, Insurance Division, SAIF is subject to Risk Based Capital (RBC) requirements of the National Association of Insurance Commissioners (NAIC), which establishes that certain amounts of capital and surplus be maintained. SAIF's RBC calculated minimum capital and surplus amount on the statutory basis of accounting was \$285.2 million and \$289.5 million at December 31, 2015 and 2014, respectively. At December 31, 2015 and 2014, the statutory capital and surplus of SAIF exceeded the minimum RBC requirements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of accounting—SAIF has prepared the accompanying financial statements in accordance with accounting principles generally accepted in the United States of America for governmental entities. As a discretely presented component unit of the State of Oregon, SAIF is subject to the pronouncements of the Governmental Accounting Standards Board (GASB). Under accounting principles generally accepted in the United States of America as applied to governmental entities, SAIF accounts for its activities as a special purpose government engaged solely in business-type activities. Accordingly, SAIF follows the economic resources measurement focus and the accrual basis of accounting. Revenues are recognized when earned, regardless of when received, and expenses are recognized when incurred, regardless of when paid.

Investments—SAIF reports investments at fair value on the statement of net position and recognizes the corresponding change in the fair value of investments in the year in which the change occurs as investment income. The fair value of debt and equity securities is determined using recognized pricing services or prices quoted by one or more independent broker. Equity securities traded on a national exchange are valued at the last reported sales price. Debt securities are valued using evaluated bid prices at December 31, 2015 and 2014.

Cash and cash equivalents—Cash and cash equivalents include investments in highly liquid debt instruments with an original maturity of three months or less. SAIF places its temporary cash investments with the Oregon Short-Term Fund (OSTF), an external cash and investment pool. SAIF's participation in this fund is involuntary. This fund is not registered with the Securities and Exchange Commission and is not rated. The OSTF is a cash and investment pool that operates as a demand deposit account. As a result, SAIF's investment is not impacted by changes in the market value of the OSTF. By statute, the OSTF may hold securities with maturities no greater than three years. Audited financial statements and monthly compliance summaries, which include information about the OSTF's maturity distribution and credit quality, may be obtained at the Oregon State Treasury's web site: [http://www.oregon.gov/treasury/Divisions/Investment/Pages/Oregon-Short-Term-Fund-\(OSTF\).aspx](http://www.oregon.gov/treasury/Divisions/Investment/Pages/Oregon-Short-Term-Fund-(OSTF).aspx). As of December 31, 2015 and 2014, SAIF's balance in the OSTF was \$28.3 million and \$33.9 million, respectively.

Oregon's State Treasurer employs the services of two external investment managers to manage SAIF's fixed income portfolios. The cash balances of the fixed income managers are invested in the SSgA Prime Money Market Fund which had a fund credit quality rating of AAAM. This fund's stated objectives are to maximize current income while maintaining a stable \$1.00 unit value by investing in high quality, short maturity securities. The average maturity of the SSgA Prime Money Market Fund as of December 31, 2015 and 2014, was 27 days and 34 days, respectively.

Concentrations of credit risk—Financial instruments, which potentially subject SAIF to concentrations of credit risk, consist principally of temporary cash investments and debt securities. SAIF places its investment securities with financial institutions approved by the State of Oregon and limits the amount of credit exposure to any one financial institution. Concentrations of credit risk with respect to investments in debt securities are limited due to the large number of such investments and their distribution among many different industries and geographic regions.

Capital assets—Capital assets are stated at historical cost, less accumulated depreciation. Maintenance, repairs, and minor renovations are charged to expense as costs are incurred. Upon retirement or sale, any resulting gain or loss is recorded as other income.

Internal and external costs incurred to develop internal-use computer software and web sites during the application development stage are capitalized; costs incurred during the preliminary project stage and post-implementation/operation stage are expensed as incurred.

Capital assets are capitalized and depreciated using the straight-line method over the estimated useful lives of the assets as follows:

| | <u>Capitalization Threshold</u> | <u>Useful Life</u> |
|---------------------------------------|-------------------------------------|------------------------|
| Buildings and improvements | All | 30–40 years |
| Furniture, equipment, and automobiles | \$0–\$5,000 | 3–7 years |
| Data processing software | \$500,000 | 3 years |

Capital assets activity for the years ended December 31, 2015 and 2014, was as follows (dollars in thousands):

| | 2015 | | | |
|---------------------------------------|------------------------------|------------------|------------------|---------------------------|
| | Beginning Balance | Additions | Disposals | Ending Balance |
| Nondepreciable capital assets - land | \$ 3,029 | \$ - | \$ - | \$ 3,029 |
| Buildings and improvements | 26,419 | 949 | - | 27,368 |
| Furniture, equipment, and automobiles | 6,100 | 1,193 | (655) | 6,638 |
| Data processing software | <u>9,043</u> | <u>-</u> | <u>-</u> | <u>9,043</u> |
| Total depreciable capital assets | <u>41,562</u> | <u>2,142</u> | <u>(655)</u> | <u>43,049</u> |
| Total | <u>44,591</u> | <u>2,142</u> | <u>(655)</u> | <u>46,078</u> |
| Less accumulated depreciation for: | | | | |
| Buildings and improvements | (16,536) | (539) | - | (17,075) |
| Furniture, equipment, and automobiles | (4,701) | (585) | 593 | (4,693) |
| Data processing software | <u>(9,043)</u> | <u>-</u> | <u>-</u> | <u>(9,043)</u> |
| Total accumulated depreciation | <u>(30,280)</u> | <u>(1,124)</u> | <u>593</u> | <u>(30,811)</u> |
| Capital assets—net | <u>\$ 14,311</u> | <u>\$ 1,018</u> | <u>\$ (62)</u> | <u>\$ 15,267</u> |
| | | | | |
| | 2014 | | | |
| | Beginning Balance | Additions | Disposals | Ending Balance |
| Nondepreciable capital assets - land | \$ 3,029 | \$ - | \$ - | \$ 3,029 |
| Buildings and improvements | 26,419 | - | - | 26,419 |
| Furniture, equipment, and automobiles | 5,975 | 482 | (357) | 6,100 |
| Data processing software | <u>9,043</u> | <u>-</u> | <u>-</u> | <u>9,043</u> |
| Total depreciable capital assets | <u>41,437</u> | <u>482</u> | <u>(357)</u> | <u>41,562</u> |
| Total | <u>44,466</u> | <u>482</u> | <u>(357)</u> | <u>44,591</u> |
| Less accumulated depreciation for: | | | | |
| Buildings and improvements | (15,802) | (734) | - | (16,536) |
| Furniture, equipment, and automobiles | (4,546) | (486) | 331 | (4,701) |
| Data processing software | <u>(9,043)</u> | <u>-</u> | <u>-</u> | <u>(9,043)</u> |
| Total accumulated depreciation | <u>(29,391)</u> | <u>(1,220)</u> | <u>331</u> | <u>(30,280)</u> |
| Capital assets—net | <u>\$ 15,075</u> | <u>\$ (738)</u> | <u>\$ (26)</u> | <u>\$ 14,311</u> |

Premiums—Premiums are based on individual employers' reported payroll using predetermined, DCBS-approved insurance rates based on employee risk classifications and are recognized as income on a pro rata basis over the coverage period, which is generally one year. Ceded premiums are recognized consistent with the underlying policies. The portion of premiums that will be earned in the future are deferred and reported as unearned premiums.

Policyholders' premiums due to SAIF are recorded as premiums receivable, net of the allowance for uncollectible accounts of \$785 thousand and \$840 thousand, at December 31, 2015 and 2014, respectively. Premiums receivable consists of both billed amounts and unbilled amounts. Unbilled premiums receivable primarily represent premiums recorded as written at

the policy inception date and not yet billed, as well as an estimate of the difference between amounts earned ratably on installment-billed policies and the amount billed on the policy. Unbilled premiums receivable also include estimated billings on payroll reporting policies that were earned but not billed prior to year-end. SAIF uses its historical experience to estimate earned but unbilled amounts, which are recorded as premiums receivable. These unbilled amounts are estimates, and while SAIF believes such amounts are reasonable, there can be no assurance the amounts ultimately received will equal the recorded unbilled amounts. The ultimate collectability of the unbilled premiums receivable can be affected by general changes in the economy and the regulatory environment due to the increased time required to determine the billable amount. SAIF considers these factors when estimating the premium receivable for unbilled premiums. Unbilled premiums receivable at December 31, 2015 and 2014 were \$312.2 million and \$301.9 million, respectively, including unearned premiums of \$172.3 million and \$170.5 million, respectively, and are included in premiums receivable, net.

Certain policyholders are required to remit deposits which represent premium expected to be payable to SAIF at the end of the month following the reporting period (monthly and quarterly), plus one additional month. Deposits are generally in the form of cash and are recorded as policyholders' premium deposits. However, policyholders may pledge surety bonds and securities, as well as letters of credit, in lieu of cash deposits. Premium deposits at December 31, 2015 and 2014, were \$15.3 and \$14.2 million, respectively.

In addition to its regular premium plans, SAIF offers employers retrospective premium rating plans under which premiums are adjusted annually for up to 10½ years following the plan year based on policyholders' loss experience. Adjustments to the original premiums are paid to or collected from the policyholders six months following the expiration of the policy and annually thereafter for up to 10½ years. The estimate of the net accrued premiums receivable for retrospective rating plans as of December 31, 2015 and 2014, is as follows (dollars in thousands):

| | <u>2015</u> | <u>2014</u> |
|---|--------------------|--------------------|
| Accrued retrospective premiums receivable | \$ 21,693 | \$ 22,382 |
| Accrued retrospective premiums payable | <u>(52,012)</u> | <u>(40,303)</u> |
| Net | <u>\$ (30,319)</u> | <u>\$ (17,921)</u> |

SAIF estimates accrued retrospective premiums receivable and payable by reviewing historical loss and premium development patterns at various stages of maturity and using these historical patterns to arrive at the best estimate of return and additional retrospective premiums on all open retrospectively rated policies. Premiums written on retrospective workers' compensation policies for 2015 and 2014 were \$93.1 million and \$90.8 million, respectively, or 18.9 percent of net premiums written for each year.

Reserve for losses and loss adjustment expenses—The reserve for losses and LAE is generally based on past experience. The liability includes provisions for reported claims, claims incurred but not reported, and claims that are currently closed but which experience indicates will be reopened.

Management believes that the reserve for incurred but unpaid losses and LAE at December 31, 2015 and 2014, is a reasonable estimate of the ultimate net costs of settling claims and claim expenses incurred. Annually, the Board of Directors reviews the actuarial assumptions utilized in determining the liability for such losses. Actual claim costs depend upon such factors as duration of worker disability, medical cost trends, occupational disease, inflation, and other societal and economic factors. As a result, the process used in computing the ultimate cost of settling claims and expense for administering claims is necessarily based on estimates. The amount ultimately paid may be more or less than such estimates. Adjustments resulting from

changes in estimates of these liabilities are charged or credited to operations in the period in which they occur (see note 4).

Premium deficiency—Premium deficiency is based upon an estimate of the amount by which the sum of anticipated claims costs, claims adjustment expenses, and maintenance expenses exceeds expected premium income and earnings on investments. At December 31, 2015 and 2014, no reserve for premium deficiency was required to be recorded.

Policyholders' dividends—Substantially all of SAIF's business is written under various participating plans wherein a dividend may be returned to the policyholder. Dividends may be paid to the extent that a surplus is accumulated from premiums, investment gains, and/or loss reserve reductions. In 2015, policyholder dividends of \$120.0 million were incurred and paid to qualifying policyholders. In 2014, policyholder dividends of \$165.0 million were incurred and paid to qualifying policyholders.

Taxes and assessments—The Oregon Department of Justice has determined that SAIF is exempt from federal and state taxes, because it is an integral part of the State of Oregon and, alternatively, exempt under either or both Sections 501(c)(27)(B) and 115(1) of the Internal Revenue Code.

SAIF is subject to levies by the Oregon Workers' Compensation Division of the DCBS. Such assessments constitute an in-lieu-of-tax relative to premiums. Premium assessments were \$28.5 million and \$27.2 million, including \$28.9 million and \$26.6 million of accrued premium assessments, for the years ended December 31, 2015 and 2014, respectively.

Use of estimates—The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the reported amounts of revenues and expenses during the reporting period, and disclosures of contingent assets and liabilities at the date of the financial statements. Actual results could differ from those estimates.

Deferred outflows of resources and deferred inflows of resources—Deferred outflows of resources represent a consumption of net position that applies to a future period and so will not be recognized as an outflow of resources (expense) until then. Deferred inflows of resources represent an acquisition of net position that applies to a future period and will not be recognized as an inflow of resources (revenue) until that time.

New accounting pronouncements—In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of GASB Statement No. 27*. This statement replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*, as well as the requirements of Statement No. 50, *Pension Disclosures*, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements (hereafter jointly referred to as trusts) that meet certain criteria. This statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit pensions, this statement identifies the methods and assumptions that should be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about pensions also are addressed. SAIF implemented this statement for the fiscal year ended December 31, 2015. See note 10 for additional information. The impact of this statement on SAIF's financials resulted in a restatement of net position. The 2015 beginning net position was restated as follows:

| | <u>January 1, 2015</u> |
|--|----------------------------|
| Net position, as previously stated | \$ 1,630,596 |
| Prior period adjustment (Pension related payable) | (11,071) |
| Cumulative effect of change in accounting principle due to GASB 68 implementation | <u>(9,018)</u> |
| Net position, as restated | <u><u>\$ 1,610,507</u></u> |

In November 2013, the GASB issued Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date—An Amendment of GASB Statement No. 68*. This statement amends paragraph 137 of Statement 68 to require that, at transition, a government should recognize a beginning deferred outflow of resources for its pension contributions, if any, made subsequent to the measurement date of the beginning net pension liability. The provisions of this statement are required to be applied simultaneously with the provisions of Statement 68. SAIF implemented this statement for the fiscal year ended December 31, 2015. See note 10 for additional information.

In February 2015, the GASB issued Statement No. 72, *Fair Value Measurement and Application*. This statement addresses accounting and financial reporting issues related to fair value measurements. This statement requires a government to use valuation techniques that are appropriate under the circumstances and for which sufficient data are available to measure fair value. This statement establishes a hierarchy of inputs to valuation techniques used to measure fair value. This statement also provides guidance for applying fair value to certain investments and disclosures related to all fair value investments. The requirements of this statement are effective for SAIF's 2016 financial statements. SAIF is currently evaluating the impact of this standard on the financial statements.

In June 2015, the GASB issued Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This statement replaces the requirements of Statements No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*, as amended, and No. 57, *OPEB Measurements by Agent Employers and Agent Multiple-Employer Plans*. This Statement establishes standards for recognizing and measuring liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. For defined benefit OPEB, this Statement identifies the methods and assumptions that are required to be used to project benefit payments, discount projected benefit payments to their actuarial present value, and attribute that present value to periods of employee service. Note disclosure and required supplementary information requirements about defined benefit OPEB also are addressed. In addition, this Statement details the recognition and disclosure requirements for employers with payables to defined benefit OPEB plans that are administered through trusts that meet the specified criteria and for employers whose employees are provided with defined contribution OPEB. The requirements of this statement are effective for SAIF's 2018 financial statements. SAIF is currently evaluating the impact of this standard on the financial statements.

In June 2015, the GASB issued Statement No. 76, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. This Statement establishes the hierarchy of GAAP for state and local governments. The requirements of this Statement apply to all state and local governmental entities. This Statement supersedes Statement No. 55, *The Hierarchy of Generally Accepted Accounting Principles for State and Local Governments*. It also amends Statement No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*, paragraphs 64, 74, and 82. The requirements of this statement are effective for SAIF's 2016 financial statements. SAIF is currently evaluating the impact of this standard on the financial statements.

In December 2015, the GASB issued Statement No. 79, *Certain External Investment Pools and Pool Participants*. This Statement establishes accounting and financial reporting standards for qualifying external investment pools that elect to measure for financial reporting purposes all of their investments at amortized cost. This Statement also establishes accounting and financial reporting standards for state and local governments that participate in a qualifying external investment pool that measures for financial reporting purposes all of its investments at amortized cost. This Statement applies to all state and local governments. The requirements of this statement are effective for SAIF's 2016 financial statements. SAIF is currently evaluating the impact of this standard on the financial statements.

In March 2016, the GASB issued Statement No. 82, *Pension Issues—An Amendment of GASB Statements No. 67, No. 68, and No. 73*. This Statement amends Statements 67 and 68 to instead require the presentation of covered payroll, defined as the payroll on which contributions to a pension plan are based, and ratios that use that measure. This Statement clarifies that a deviation, as the term is used in Actuarial Standards of practice issued by the Actuarial Standards Board, from the guidance in an Actuarial Standard of Practice is not considered to be in conformity with the requirements of Statement 67, Statement 68, or Statement 73 for the selection of assumptions used in determining the total pension liability and related measures. This Statement clarifies that payments that are made by an employer to satisfy contribution requirements that are identified by the pension plan terms as plan member contribution requirements should be classified as plan member contributions for purposes of Statement 67 and as employee contributions for purposes of Statement 68. It also requires that an employer's expense and expenditures for those amounts be recognized in the period for which the contribution is assessed and classified in the same manner as the employer classifies similar compensation other than pensions (for example, as salaries and wages or as fringe benefits). The requirements of this statement are effective for SAIF's 2017 financial statements. SAIF is currently evaluating the impact of this standard on the financial statements.

Reclassifications—Certain reclassifications have been made to prior year amounts in order to conform with current year presentation.

3. CASH, CASH EQUIVALENTS, AND INVESTMENTS

Cash and cash equivalents—SAIF's cash is held in demand accounts with the State Treasurer, State Street Bank and Trust Company, and U.S. Bank. The cash held by the State Treasurer is invested in the OSTF, a cash and investment pool that is available for use by all state funds and eligible local governments. Cash equivalents held by State Street Bank and Trust Company consist of \$5.3 million in the SSgA Prime Money Market fund.

SAIF's cash and cash equivalents totaled \$40.8 million and \$42.2 million as of December 31, 2015 and 2014, respectively, and are composed of the following (dollars in thousands):

| | <u>2015</u> | <u>2014</u> |
|--|------------------|------------------|
| Cash balances | | |
| Oregon Short-Term Fund | \$ 28,328 | \$ 33,900 |
| State Street Bank and Trust Company | 1,451 | - |
| U.S. Bank | <u>5,727</u> | <u>5,506</u> |
| | 35,506 | 39,406 |
| Cash equivalents | | |
| State Street Bank (SSgA prime money market fund) | <u>5,272</u> | <u>2,793</u> |
| | 5,272 | 2,793 |
| Total cash and cash equivalents | <u>\$ 40,778</u> | <u>\$ 42,199</u> |

Custodial credit risk for cash and cash equivalents (deposits)—Custodial credit risk for deposits is the risk that in the event of a bank failure, SAIF will not be able to recover the value of its deposits or collateral securities that are in possession of an outside party. State Treasury demand deposit accounts and investments of the OSTF held in state banks are insured up to the Federal Deposit Insurance (FDIC) amount of \$250 thousand. Where balances exceed the FDIC amount, the balances are covered by collateral held in a multiple financial institution collateral pool administered by the Oregon State Treasury in the Public Funds Collateralization Program. As of December 31, 2015, the cash held by both State Street Bank and Trust Company (State Street) and U.S. Bank is in noninterest bearing accounts, is FDIC insured up to \$250 thousand, and is uninsured for any balances exceeding that amount.

Investments—SAIF's investment policies are governed by statute and the Oregon Investment Council (Council). The State Treasurer (Treasurer) is the investment officer for the Council and is responsible for the funds on deposit in the State Treasury. In accordance with ORS 293.726, the investment funds are required to be invested, and the investments of those funds managed, as a prudent investor would do, exercising reasonable care, skill, and caution. While the Treasurer is authorized to use demand deposit accounts and fixed-income investments, equity investment transactions must be directed by external investment managers that are under contract with the Council. Equity investments are limited to not more than 50 percent of the monies contributed to the Industrial Accident Fund (SAIF Corporation). However, SAIF's adopted investment policy as approved by the Council limits equity holdings to a range of 7 to 13 percent of the market value of invested assets with a target allocation of 10 percent.

Bond, mortgage-backed, asset-backed, and equity security transactions are recorded on a trade-date basis, generally three business days prior to the settlement date. However, the number of days between trade and settlement dates for mortgage-backed securities can be up to 30 days or longer, depending on the security. Due from brokers for security sales at December 31, 2015 and 2014, were \$176 thousand and \$738 thousand, respectively. Due to brokers for security purchases at December 31, 2015 and 2014, were \$4 thousand and \$3 thousand, respectively.

Interest rate risk—Interest rate risk is the risk that changes in interest rates of debt investments will adversely affect the fair value of an investment. SAIF's policy for fixed income investments provides that a duration target be used to manage interest rate risk. The policy calls for the portfolio duration to be within 20 percent of the benchmark duration. The benchmark duration as of December 31, 2015, was 5.74 years, with an acceptable range of 4.59 to 6.89 years. As of that date, the fixed income portfolio's duration was 5.83 years.

The following 2015 maturity distribution schedule includes \$1.3 billion in interest-rate sensitive securities. As of December 31, 2015, SAIF held \$461.4 million of U.S. Federal Agency mortgage-backed securities and \$433.9 million of collateralized mortgage obligations (CMOs). These securities are based on cash flows from principal and interest payments on underlying mortgages. Therefore, they are sensitive to prepayments by mortgagees, which may result from a decline in interest rates. As of December 31, 2015, SAIF held \$420.3 million of asset-backed securities which consisted primarily of automobile, student loans, and collateralized loan obligations (CLOs). The value of these securities can be volatile as interest rates fluctuate. Additional risk inherent with these securities is the unpredictability of default on loans that are the collateral for the debt.

The following schedule represents the fixed income investments by maturity date as of December 31, 2015 and 2014, using the segmented time distribution method. Expected maturities will differ from contractual maturities, because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties (dollars in thousands):

| 2015 | Less Than 1 Year | 1–5 Years | 6–10 Years | More Than 10 Years | Fair Value |
|---|-----------------------------|----------------------|-----------------------|-----------------------------------|-----------------------|
| Bonds: | | | | | |
| U.S. Treasury obligations | \$ 31,516 | \$ 54,293 | \$ - | \$ 29,502 | \$ 115,311 |
| U.S. federal agency mortgage securities | 63,939 | 165,041 | 108,225 | 124,206 | 461,411 |
| U.S. federal agency debt | - | 3,019 | - | 1,605 | 4,624 |
| Corporate bonds | 54,220 | 536,430 | 685,028 | 707,792 | 1,983,470 |
| Municipal bonds | 1,347 | 13,276 | 18,213 | 55,803 | 88,639 |
| Collateralized mortgage obligations | 113,717 | 107,457 | 183,551 | 29,155 | 433,880 |
| Asset-backed securities | 42,785 | 155,561 | 79,694 | 142,252 | 420,292 |
| International debt securities | <u>15,462</u> | <u>101,348</u> | <u>148,212</u> | <u>200,678</u> | <u>465,700</u> |
| Total bonds | <u>\$ 322,986</u> | <u>\$1,136,425</u> | <u>\$1,222,923</u> | <u>\$1,290,993</u> | <u>\$3,973,327</u> |
| Equity securities: | | | | | |
| BlackRock MSCI ACWI IMI index fund | | | | | \$ 435,944 |
| Total equity securities | | | | | <u>435,944</u> |
| Total investments | | | | | <u>\$4,409,271</u> |

| 2014 | Less Than 1 Year | 1–5 Years | 6–10 Years | More Than 10 Years | Fair Value |
|---|-----------------------------|----------------------|-----------------------|-----------------------------------|-----------------------|
| Bonds: | | | | | |
| U.S. Treasury obligations | \$ 21,999 | \$ 118,365 | \$ - | \$ 12,712 | \$ 153,076 |
| U.S. federal agency mortgage securities | 62,710 | 166,698 | 114,618 | 152,737 | 496,763 |
| U.S. federal agency debt | 7,800 | 3,159 | - | 1,699 | 12,658 |
| Corporate bonds | 30,103 | 569,711 | 620,072 | 808,112 | 2,027,998 |
| Municipal bonds | 16,297 | 10,877 | 13,325 | 64,004 | 104,503 |
| Collateralized mortgage obligations | 76,081 | 166,745 | 61,770 | 34,862 | 339,458 |
| Asset-backed securities | 122,351 | 175,043 | 135,835 | 40,505 | 473,734 |
| International debt securities | <u>19,376</u> | <u>106,381</u> | <u>176,903</u> | <u>157,413</u> | <u>460,073</u> |
| Total bonds | <u>\$ 356,717</u> | <u>\$1,316,979</u> | <u>\$1,122,523</u> | <u>\$1,272,044</u> | <u>\$4,068,263</u> |
| Equity securities: | | | | | |
| BlackRock MSCI ACWI IMI index fund | | | | | \$ 444,251 |
| Total equity securities | | | | | <u>444,251</u> |
| Total investments | | | | | <u>\$4,512,514</u> |

Credit risk—Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. SAIF's credit risk policy is to maintain a well-diversified investment portfolio. Fixed income holdings shall be the largest component of the portfolio. The policy seeks to maintain an overall fixed income portfolio quality of at least "A" or higher.

The majority of SAIF's debt securities as of December 31, 2015 and 2014, were rated by Moody's and Standard & Poor's, which are credit rating providers. The following schedule represents the ratings of debt securities by investment type as of December 31, 2015 and 2014, using either Moody's or Standard & Poor's rating scale (dollars in thousands):

2015

Quality Ratings

| | AAA | AA | A | BBB | BB | B | CCC | CC | C | D | Unrated | Fair Value |
|---|------------|------------|------------|--------------|------------|-----------|----------|------|------|----------|-----------|--------------|
| Bonds: | | | | | | | | | | | | |
| U.S. Treasury obligations | \$ 112,312 | - | - | - | - | - | - | - | - | - | 2,999 | \$ 115,311 |
| U.S. federal agency mortgage securities | - | 461,411 | - | - | - | - | - | - | - | - | - | 461,411 |
| U.S. federal agency debt | 3,019 | 1,605 | - | - | - | - | - | - | - | - | - | 4,624 |
| Corporate bonds | 19,856 | 129,489 | 523,048 | 1,099,429 | 189,790 | 15,110 | 950 | - | - | - | 5,798 | 1,983,470 |
| Municipal bonds | - | 53,326 | 18,370 | 11,863 | 5,080 | - | - | - | - | - | - | 88,639 |
| Collateralized mortgage obligations | 196,387 | 139,505 | 52,372 | 166 | 1,089 | 2,090 | 5,384 | - | - | 6,549 | 30,338 | 433,880 |
| Asset-backed securities | 350,311 | 58,790 | 8,167 | 2,771 | - | - | - | - | - | 253 | - | 420,292 |
| International debt securities | - | 52,825 | 69,956 | 285,390 | 48,522 | 9,007 | - | - | - | - | - | 465,700 |
| Total bonds | \$ 681,885 | \$ 896,951 | \$ 671,913 | \$ 1,399,619 | \$ 244,481 | \$ 26,207 | \$ 6,334 | \$ - | \$ - | \$ 6,802 | \$ 39,135 | \$ 3,973,327 |

2014

Quality Ratings

| | AAA | AA | A | BBB | BB | B | CCC | CC | C | D | Unrated | Fair Value |
|---|------------|--------------|------------|--------------|------------|-----------|----------|------|------|----------|------------|--------------|
| Bonds: | | | | | | | | | | | | |
| U.S. Treasury obligations | \$ - | 153,076 | - | - | - | - | - | - | - | - | - | \$ 153,076 |
| U.S. federal agency mortgage securities | - | 496,763 | - | - | - | - | - | - | - | - | - | 496,763 |
| U.S. federal agency debt | - | 4,858 | 7,800 | - | - | - | - | - | - | - | - | 12,658 |
| Corporate bonds | 20,344 | 171,865 | 634,390 | 950,335 | 183,394 | 36,724 | 2,404 | - | - | - | 28,542 | 2,027,998 |
| Municipal bonds | - | 52,620 | 43,382 | 4,068 | - | - | - | - | - | - | 4,433 | 104,503 |
| Collateralized mortgage obligations | 86,421 | 105,476 | 78,824 | 6,304 | 439 | 1,167 | - | - | - | 7,767 | 53,060 | 339,458 |
| Asset-backed securities | 224,546 | 86,711 | 7,931 | - | - | - | - | - | - | 332 | 154,214 | 473,734 |
| International debt securities | - | 4,674 | 110,286 | 275,391 | 44,975 | 14,711 | 6,003 | - | - | - | 4,033 | 460,073 |
| Total bonds | \$ 331,311 | \$ 1,076,043 | \$ 882,613 | \$ 1,236,098 | \$ 228,808 | \$ 52,602 | \$ 8,407 | \$ - | \$ - | \$ 8,099 | \$ 244,282 | \$ 4,068,263 |

Concentration of credit risk—Concentration of credit risk is the risk of loss attributed to the magnitude of an entity's investment in a single issuer. SAIF's investment policy places limitations on the amount that may be invested in any one issuer. The following specific limitations reflect, in part, the Oregon Investment Council's current investment philosophy regarding diversification.

- No fixed income investment in any one issue shall be in excess of 5 percent of the outstanding fixed income obligations of the issuer.
- Issuer level restrictions shall not apply to U.S. government and agency obligations, including agency-backed mortgages (no limit) and private mortgage-backed and asset-backed securities, which shall be limited to 10 percent per issuer.
- Obligations of other national governments are limited to 10 percent per issuer.

As of December 31, 2015 and 2014, SAIF did not have a concentration of credit risk in any one issuer that exceeded the policy outlined above.

Securities on deposit—U.S. Treasury obligations with a fair value of \$8.2 million and \$8.3 million were on deposit with the Federal Reserve as required by the U.S. Department of Labor under the Longshore and Harbor Workers' Compensation Act as of December 31, 2015 and 2014, respectively. In addition, certificates of deposit with a fair value of \$480 thousand and \$372 thousand were on deposit at U.S. Bank as required by the DCBS at December 31, 2015 and 2014, respectively.

Securities lending—In accordance with state investment policies, SAIF participates in securities lending transactions. The Oregon State Treasury has, through a Securities Lending Agreement, authorized State Street to lend SAIF's securities to broker-dealers and banks pursuant to a form of loan agreement. Both SAIF and the borrowers maintain the right to terminate all securities lending transactions on demand. There have been no significant violations of the provisions of securities lending agreements.

During 2015 and 2014, State Street loaned SAIF's fixed income securities and received cash and noncash collateral denominated in U.S. dollars. Borrowers were required to deliver collateral for each loan equal to at least 102 percent of the fair value of the loaned security. SAIF did not impose any restrictions on the amount of the loans State Street made on its behalf. Securities received as collateral may not be sold or pledged by SAIF, except in the event of borrower default. SAIF was fully indemnified by State Street against losses due to borrower default, and there were no losses during the year from the failure of borrowers to return loaned securities.

Cash collateral received for securities loaned is invested in the State Street Bank and Trust Company Oregon Short-Term Investment Fund (the Fund), an "external investment pool" for purposes of GASB Statement No. 31. SAIF's participation in this fund is voluntary. The fair value of investments held by this fund is based upon valuations provided by a recognized pricing service. This fund is not registered with the Securities and Exchange Commission, but the custodial agent is subject to the oversight of the Federal Reserve Board and the Massachusetts Commissioner of Banks. No income from the Fund was assigned to another fund by the custodial agent during 2015 and 2014. At December 31, 2015 and 2014, the Fund had an average life-final maturity of 139 days and 109 days, respectively.

The cash collateral held at December 31, 2015 and 2014, was \$52.3 million and \$146.2 million, respectively. At December 31, 2015 and 2014, securities received as collateral were \$25.1 million and \$31.7 million, respectively. At December 31, 2015 and 2014, the fair value, including accrued investment income related to the securities on loan, was \$76.0 million and

\$174.3 million, respectively. For 2015 and 2014, securities lending income was \$601 thousand and \$407 thousand and securities lending expense was \$181 thousand and \$93 thousand, respectively.

4. RESERVE FOR LOSSES AND LOSS ADJUSTMENT EXPENSES

SAIF has established a reserve for both reported and unreported insured events, which includes estimates of future payments of losses and related LAE. In estimating the reserve for losses and LAE, SAIF considers prior experience, industry information, currently recognized trends affecting data specific to SAIF, and other factors relating to workers' compensation insurance underwritten by SAIF.

The following table provides a reconciliation of the beginning and ending reserve for losses and LAE at December 31, 2015 and 2014 (dollars in thousands):

| | <u>2015</u> | <u>2014</u> |
|---|---------------------------|---------------------------|
| Gross reserve for losses and loss adjustment expenses—beginning of year | \$3,086,962 | \$3,176,312 |
| Less reinsurance recoverable—beginning of year | <u>(124,899)</u> | <u>(134,937)</u> |
| Net reserve for losses and loss adjustment expenses—beginning of year | <u>2,962,063</u> | <u>3,041,375</u> |
| Incurred losses and loss adjustment expenses: | | |
| Provision for insured events of the current year | 558,627 | 527,601 |
| Provision for insured events of prior years | <u>(232,948)</u> | <u>(256,740)</u> |
| Total incurred losses | <u>325,679</u> | <u>270,861</u> |
| Loss and loss adjustment expense payments attributable to: | | |
| Insured events of the current year | 124,081 | 131,671 |
| Insured events of prior years | <u>255,043</u> | <u>218,502</u> |
| Total payments | <u>379,124</u> | <u>350,173</u> |
| Net reserve for losses and loss adjustment expenses—end of year | 2,908,618 | 2,962,063 |
| Plus reinsurance recoverable—end of year | <u>113,133</u> | <u>124,899</u> |
| Gross reserve for losses and loss adjustment expenses—end of year | <u><u>\$3,021,751</u></u> | <u><u>\$3,086,962</u></u> |

The reserve for losses and LAE decreased \$53.4 million in 2015, which was net of favorable development of \$232.9 million. Loss reserves decreased \$60.7 million as compared to the prior year. Loss reserves for the 2015 accident year were offset by favorable loss reserve development in prior accident years. The favorable loss reserve development was attributed primarily to permanent total and permanent partial disability medical loss reserves. The key drivers were a decrease in ultimate counts and the continuing downward trend in medical severity. The observed medical escalation rate for 2015 was well below the assumption. Indemnity loss reserves experienced favorable development driven by actual costs for permanent total disability being lower than expected for recent accident years and the reduction in ultimate projected counts for fatal.

LAE reserves increased \$7.3 million. LAE reserves for the 2015 accident year were offset by favorable loss reserve development in prior accident years. The favorable LAE development was largely attributable to the overall reduction in reserves.

The reserve for losses and LAE decreased \$79.3 million in 2014, which was net of favorable development of \$256.7 million. Loss reserves decreased \$89.8 million as compared to the prior year. Loss reserves for the 2014 accident year were offset by favorable loss reserve development in prior accident years. The favorable loss reserve development was attributed primarily to permanent total and permanent partial disability medical loss reserves. The key drivers were a decrease in the tail factor and the continuing downward trend in medical severity. The observed medical escalation rate for 2014 was well below the assumption. Indemnity loss reserves experienced unfavorable development as indemnity costs for recent accident years were higher than expected. LAE reserves increased \$10.5 million. LAE reserves for the 2014 accident year were offset by favorable loss reserve development in prior accident years. The favorable LAE development was largely attributable to the overall reduction in reserves.

SAIF discounts the indemnity reserve for known unpaid fatal and permanent total disability losses on a tabular basis using the 2007 United States Life Tables, the 1997 United States of America Railroad Retirement Board Remarriage Table, and a discount rate of 3.5 percent. SAIF does not discount any incurred but not reported reserves, medical unpaid losses, or unpaid LAE. Gross reserves subject to tabular discounting were \$263.9 million and \$269.1 million for 2015 and 2014, respectively. The discounts were \$94.0 million and \$95.1 million as of December 31, 2015 and 2014, respectively.

Anticipated salvage and subrogation of \$35.7 million and \$33.2 million was included as a reduction of the reserve for losses and LAE at December 31, 2015 and 2014, respectively.

SAIF's exposure to asbestos claims arose from the sale of workers' compensation policies. Reserves of \$19.1 million and \$20.6 million for losses and LAE are related to asbestos claims as of December 31, 2015 and 2014, respectively. Amounts paid for asbestos-related claims were \$999 thousand and \$776 thousand at December 31, 2015 and 2014, respectively.

5. REINSURANCE

In the ordinary course of business, SAIF cedes premiums for purposes of risk diversification and limiting maximum loss exposure from catastrophic events through contractual agreements with reinsurers. If such assuming reinsurers are unable to meet the obligations assumed under these reinsurance agreements, SAIF would be liable to pay the obligation. To minimize its exposure to significant losses from reinsurer insolvencies, SAIF evaluates the financial condition of its reinsurers and monitors concentration of credit risk.

SAIF maintains reinsurance protection providing limits of \$160 million excess of \$35 million per occurrence with a \$10 million maximum on any one life. This reinsurance protection excludes coverage for nuclear, biological, chemical, or radiological events in some or all instances. During 2015, SAIF had reinsurance protection for 85 percent of losses in excess of 20 percent of 2014 direct written premium for acts of foreign and domestic terrorism through the Terrorism Risk Insurance Program Reauthorization Act.

The following amounts have been deducted in the accompanying financial statements as a result of reinsurance ceded for 2015 and 2014 (dollars in thousands):

| | <u>2015</u> | <u>2014</u> |
|---|-------------|-------------|
| Reserve for losses and loss adjustment expenses | \$ 37,053 | \$ 44,131 |
| Premiums earned | 1,187 | 682 |
| Losses and loss adjustment expenses incurred | (6,335) | (5,780) |

Of the \$37.1 and \$44.1 million recoverable, SAIF had a reinsurance recoverable from an individual reinsurer of \$21.6 million and \$24.4 million, respectively as of December 31, 2015 and 2014.

In 2015, SAIF performed a commutation with Coliseum Reinsurance Corporation extinguishing Coliseum Reinsurance Corporation's 12.5 percent participation in SAIF's 1992 and 1993 \$4 million in excess of \$1 million per claim reinsurance treaty. SAIF recognized the amounts received from the reinsurer as a reduction of losses and loss adjustment expenses paid (thereby reducing losses and loss adjustment expenses incurred) in the current year. SAIF also increased its loss and loss adjustment expense reserves (thereby increasing losses and loss adjustment expenses incurred) to recognize the effect of releasing the reinsurer from its obligations under the treaty. The net effect of the commutation was a decrease in underwriting income of \$661 thousand. This amount is shown below by statement of income classification and by reinsurer.

| <u>Statement of Income Account</u> | <u>Amount</u> |
|------------------------------------|---------------|
| Losses incurred | \$ 661 |
| Loss adjustment expenses incurred | - |
| Premium earned | - |
| Other | - |
| Total | <u>\$ 661</u> |

| <u>Reinsurer</u> | <u>Amount</u> |
|----------------------------------|---------------|
| Coliseum Reinsurance Corporation | \$ 661 |

In 2014, SAIF performed a commutation with Excalibur Reinsurance Corporation extinguishing Excalibur Reinsurance Corporation's 25 percent participation in SAIF's 1992 and 1993 \$4 million in excess of \$1 million per claim reinsurance treaty. SAIF recognized the amounts received from the reinsurer as a reduction of losses and loss adjustment expenses paid (thereby reducing losses and loss adjustment expenses incurred) in the current year. SAIF also increased its loss and loss adjustment expense reserves (thereby increasing losses and loss adjustment expenses incurred) to recognize the effect of releasing the reinsurer from its obligations under the treaty. The net effect of the commutation was a decrease in underwriting income of \$2.7 million. This amount is shown below by statement of income classification and by reinsurer.

| <u>Statement of Income Account</u> | <u>Amount</u> |
|---|----------------------|
| Losses incurred | \$ 2,969 |
| Loss adjustment expenses incurred | - |
| Premium earned | (266) |
| Other | - |
| Total | <u>\$ 2,703</u> |

| <u>Reinsurer</u> | <u>Amount</u> |
|-----------------------------------|----------------------|
| Excalibur Reinsurance Corporation | \$ 2,703 |

In November 2010, SAIF received formal approval from the DCBS for implementation of its Other States Coverage program. Beginning February 1, 2011, SAIF partnered with Zurich American Insurance Company and United States Insurance Services (USIS) to provide other states coverage. Zurich issues policies covering the non-Oregon operation of SAIF's customers and manages claims arising from those policies. SAIF reinsures those policies in full. USIS, a broker licensed in all fifty states, provides marketing and administrative services.

The following amounts are included in the accompanying financial statements as a result of participation in other states coverage in 2015 and 2014 (dollars in thousands):

| <u>Other States Coverage</u> | <u>2015</u> | <u>2014</u> |
|---|--------------------|--------------------|
| Assumed: | | |
| Reserve for losses and loss adjustment expenses | \$ 13,509 | \$ 9,474 |
| Unearned premiums | 5,855 | 6,311 |
| Premiums written | 13,224 | 13,769 |
| Premiums earned | 13,680 | 13,412 |
| Losses and loss adjustment expenses incurred | 9,519 | 8,135 |
| Commission expense | 2,110 | 1,948 |

SAIF is authorized to write business on behalf of the Oregon Workers' Compensation Insurance Plan (the Plan), administered by the National Council on Compensation Insurance through the National Workers' Compensation Reinsurance Pool (NWCRP). The Plan provides a guaranteed source of workers' compensation insurance for employers unable to obtain coverage because of unstable financial conditions, poor loss experience, or the inherently dangerous nature of the work. SAIF cedes such business to the Plan. In addition, SAIF is required to assume its share of premiums and losses from the Plan based on SAIF's voluntary market share.

The following amounts are included in the accompanying financial statements as a result of participation in the Plan in 2015 and 2014 (dollars in thousands):

| NWCRP | 2015 | 2014 |
|---|-------------|-------------|
| Assumed: | | |
| Reserve for losses and loss adjustment expenses | \$ 75,357 | \$ 70,183 |
| Unearned premiums | 5,432 | 5,126 |
| Premiums written | 31,331 | 32,289 |
| Premiums earned | 31,026 | 31,614 |
| Losses and loss adjustment expenses incurred | 20,960 | 13,843 |
| Commission expense | 11,408 | 11,151 |
| Ceded: | | |
| Reserve for losses and loss adjustment expenses | \$ 76,080 | \$ 80,768 |
| Unearned premiums | 6,791 | 6,555 |
| Premiums written | 19,313 | 17,287 |
| Premiums earned | 19,077 | 17,209 |
| Losses and loss adjustment expenses incurred | 2,843 | 3,217 |
| Commission expense | 7,260 | 6,725 |

6. LEASE COMMITMENTS

SAIF leases office space in several locations under noncancelable operating leases expiring during various years through 2021. Lease expense was \$1.7 million and \$1.3 million as of December 31, 2015 and 2014, respectively.

SAIF's future minimum lease payments under operating leases at December 31, 2015, are as follows (dollars in thousands):

| | |
|------------------------|-----------------|
| 2016 | \$ 2,342 |
| 2017 | 2,671 |
| 2018 | 1,534 |
| 2019 | 429 |
| 2020 | <u>164</u> |
| Total minimum payments | <u>\$ 7,140</u> |

Certain rental commitments have renewal options extending through the year 2031. Some of these renewals are subject to adjustments in future periods. Total minimum lease payments have not been reduced by minimum sublease rentals of approximately \$95 thousand on leases due in the future under noncancelable subleases as of December 31, 2015.

7. RISK MANAGEMENT

The State of Oregon administers property and casualty insurance programs covering state government agencies through its Insurance Fund, an internal service fund. The Insurance Fund services claims for: direct physical loss or damage to state property; tort liability claims brought against the state, its officers, employees, or agents; workers' compensation; and employees, elected officials, and members of commissions and boards for faithful performance. The Insurance Fund is backed by a commercial excess property policy with limits of \$400 million and a blanket commercial excess bond with limits of \$4.5 million.

SAIF participates in the Insurance Fund. The cost of servicing insurance claims and payments is covered by charging an assessment to each participating state entity based on its share of services provided in a prior period. The total statewide assessment of each type of coverage is based on independent biennial actuarial forecasts and administrative expenses, less any

available fund balance of the Insurance Fund from the prior biennium. SAIF's assessment was \$1.6 million and \$0.2 million as of December 31, 2015 and 2014, respectively.

SAIF's employees do not participate in the State of Oregon's health insurance plans.

8. CONTINGENCIES

SAIF has entered into structured settlements wherein SAIF has purchased annuities for which the claimant is payee, but for which SAIF is contingently liable. The amount of the contingent liability is the amount of the liability due to the various claimants that has been offset by the purchase of the annuity. Contingent liabilities arising from these settlements were \$3.0 million and \$3.3 million at December 31, 2015 and 2014, respectively.

In 1998, in response to the flood that occurred in 1996, SAIF installed an observation well to mitigate future flood risk. In the process of drilling the well, petroleum contamination was discovered in the soil under the High Street building. Once this contamination was discovered, SAIF worked with the State of Oregon Department of Environmental Quality ("DEQ") to determine if action was required. Based on the DEQ's review and acceptance of the Remedial Action Plan for the petroleum contamination, SAIF will install remediation systems consisting of a plume interceptor/containment system and remediation/monitoring wells.

The total estimated remediation costs have increased from the recorded \$200,000, at December 31, 2015, to a range of \$270,800 to \$350,000, at issuance date. SAIF believes the difference between the recorded estimate and the present estimated range is insignificant to the financial statements both quantitatively and qualitatively. Therefore, no adjustment will be made to change the estimate recorded.

During the normal course of business, SAIF becomes involved in litigation arising out of matters incident to the conduct of its insurance operations. SAIF is represented in these actions by the Oregon Department of Justice. Some of these potential liabilities become actual liabilities when one or more future events occur or fail to occur. To the extent that the future event is likely to occur or fail to occur, and a reasonable estimate of the loss can be made, an estimated liability would be recorded on SAIF's financial statements. Management believes that these matters do not materially impact the financial statements.

9. DEFERRED COMPENSATION PLAN

SAIF provides a deferred compensation plan, authorized under and consistent with Internal Revenue Code Section 457(b), as a benefit available to all its employees. The plan authorizes the employee to execute an individual agreement with the plan's record keeper, Empower Retirement Services, whereby the employee defers a portion of his or her current income until future years, as a retirement savings vehicle in which funds are sheltered from federal and state taxation until withdrawal. Participants cannot receive the funds until certain circumstances are met. Funds withheld from employee compensation and remitted to the plan are invested by the employee in a variety of mutual funds and other offerings selected by SAIF's investment committee. Plan assets are held in a trust account with Wells Fargo, and administered by Empower Retirement Services for the exclusive benefit of the participant or his or her beneficiary. Participants' rights under the plan are equal to the fair market value of the deferred account for each participant. SAIF has no rights to participant funds, and does not perform the investing function for the participant. SAIF's fiduciary accountability for the plan extends only to selection of the investment options that are made available to the participants. Thus, plan assets and any related liability to plan participants have been excluded from the financial statements.

10. RETIREMENT PLAN

Plan descriptions—SAIF's employees hired prior to August 29, 2003, participate in the Oregon Public Employees' Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan. The PERS Board of Trustees under the guidelines of ORS Chapter 238 administers PERS. The PERS retirement allowance, payable monthly for life, may be selected from multiple retirement benefit options. Options include survivorship benefits and lump-sum refunds. The basic benefit formula is 1.67 percent of a member's final average salary multiplied by the member's number of years of service. Benefits may also be calculated under either a money match or an annuity-plus-pension computation if a greater benefit results. PERS also provides death and disability benefits. A copy of the Oregon Public Employees' Retirement System annual financial report may be obtained by writing to PERS, Fiscal Services Division, PO Box 23700, Tigard, Oregon 97281-3700. The report may also be accessed online at: http://oregon.gov/PERS/pages/section/financial_reports/financials.aspx.

Beginning January 1, 2004, all covered employees are required by state statute to contribute 6.00 percent of their salary to the Individual Account Program (IAP), a defined contribution plan. Current law permits employers to pay employees' contributions to PERS, which SAIF has elected to do. Additionally, SAIF is required by statute to contribute a percentage of each covered employee's salary to fund the PERS program. For the year ended December 31, 2015, SAIF's contribution rate of each covered employee's salary was 13.28 percent. This contribution is the minimum contribution required for future periods. Rates are subject to change as a result of subsequent actuarial valuations.

SAIF employees hired on or after August 29, 2003, participate in the Oregon Public Service Retirement Plan (OPSRP) after completing six months of service. OPSRP is a hybrid pension plan (cost sharing multiple-employer plan) administered by the PERS Board of Trustees under the guidelines of ORS Chapter 238A with two components: the Pension Program (defined benefit) and the IAP (defined contribution). SAIF currently contributes 7.31 percent of each covered employee's salary to the Pension Program and 6.00 percent to the IAP. This contribution is the minimum contribution required for future periods. Rates are subject to change as a result of subsequent actuarial valuations.

SAIF participates, along with other State of Oregon agencies, in paying the debt service for State of Oregon general obligation bonds issued in October 2003 to reduce an unfunded PERS liability. The bonds are scheduled to mature 25 years after the date of issuance. Currently, the repayment rate is 6.00 percent of payroll each month. The payment rate is recalculated periodically, as needed.

The total amount contributed by SAIF for all plans for the years ended December 31, 2015, 2014, and 2013, consist of the following (dollars in thousands):

| | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|--------------------------------------|-----------------|-----------------|-----------------|
| Employer contributions: | | | |
| Debt service | \$ 4,354 | \$ 4,195 | \$ 3,823 |
| PERS-Pension Program | 4,394 | 3,902 | 3,938 |
| OPSRP-Pension Program | <u>2,147</u> | <u>1,877</u> | <u>1,561</u> |
| Total employer contributions | <u>10,895</u> | <u>9,974</u> | <u>9,322</u> |
| Employee contributions paid by SAIF: | | | |
| PERS-IAP | 2,298 | 2,373 | 2,435 |
| OPSRP-IAP | <u>1,670</u> | <u>1,383</u> | <u>1,157</u> |
| Total employee contributions | <u>3,968</u> | <u>3,756</u> | <u>3,592</u> |
| Total contributions | <u>\$14,863</u> | <u>\$13,730</u> | <u>\$12,914</u> |

For the years ended December 31, 2015, 2014, and 2013, SAIF's employer contributions were equal to the annual required contributions.

Net pension liability—At December 31, 2015, SAIF reported a liability of \$34.2 million 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 December 31, 2013. At December 31, 2015, SAIF's proportionate share was .60 percent of the statewide pension plan, and 2.34 percent of employer state agencies.

For the year ended December 31, 2015, SAIF recorded pension expense of \$27.5 million. At December 31, 2015, SAIF reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources (in thousands):

| | <u>Deferred Outflows of Resources</u> | <u>Deferred Inflows of Resources</u> |
|--|---|--|
| Differences between expected and actual experience | \$ 1,844 | \$ - |
| Net difference between projected and actual earnings on investments | - | 7,166 |
| Changes in proportion and differences between fund contributions and proportionate share of contributions | <u>875</u> | <u>727</u> |
| Total (prior to post-measurement date contributions) | <u>2,719</u> | <u>7,894</u> |
| Net deferred outflows/(inflows) of resources before contributions subsequent to the measurement date | - | (5,175) |
| Contributions subsequent to the measurement date | <u>2,885</u> | - |
| Net deferred outflows/(inflows) of resources | | <u>\$ (2,290)</u> |

The \$2.9 million reported as deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ended December 31, 2016. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expenses as follows (in thousands):

| Fiscal Year | Deferred Outflows/(Inflows) of Resources (Prior to Post-Measurement Date Contributions) | |
|--------------------|--|---------|
| 2016 | \$ | (2,958) |
| 2017 | | (2,958) |
| 2018 | | (2,958) |
| 2019 | | 3,534 |
| 2020 | | 165 |
| Total | \$ | (5,175) |

Actuarial methods and assumptions—The following methods and assumptions were used in the development of the total pension liability:

| | |
|-----------------------------------|---|
| Valuation date | December 31, 2013 |
| Measurement date | June 30, 2015 |
| Experience study | 2014, published September 2015 |
| Actuarial cost method | Entry age normal |
| Actuarial assumptions: | |
| Inflation rate | 2.75 percent |
| Long-term expected rate of return | 7.75 percent |
| Discount rate | 7.75 percent |
| Projected salary increases | 3.75 percent |
| Cost of living adjustments (COLA) | Blend of 2.00 percent COLA and graded COLA (1.25 percent/0.15 percent) in accordance with <i>Moro</i> decision; blend based on service. |
| Mortality | <p>Healthy retirees and beneficiaries: RP-2000 sex-distinct, generational per Scale AA, with collar adjustments and set-backs as described in the valuation.</p> <p>Active members: Mortality rates are a percentage of healthy retiree rates that vary by group, as described in the valuation.</p> <p>Disabled retirees: Mortality rates are a percentage (65 percent for males, 90 percent for females) of the RP-2000 static combined disabled mortality sex-distinct table.</p> |

Long-term expected rate of return—To develop an analytical basis for the selection of the long-term expected rate of return assumptions, in July 2013 the PERS Board reviewed long-term assumptions developed by both Milliman’s capital market assumptions team and the Oregon Investment Council’s (OIC) investment advisors. The following table shows Milliman’s assumptions for each of the asset classes in which the plan was invested at that time based on the OIC long-term target asset allocation:

| <u>Asset Class</u> | <u>Target Allocation</u> | <u>Compound Annual (Geometric) Return</u> |
|-----------------------------|--------------------------|---|
| Core fixed income | 7.20% | 4.50% |
| Short-term bonds | 8.00% | 3.70% |
| Intermediate-term bonds | 3.00% | 4.10% |
| High yield bonds | 1.80% | 6.66% |
| Large cap US equities | 11.65% | 7.20% |
| Mid cap US equities | 3.88% | 7.30% |
| Small cap US equities | 2.27% | 7.45% |
| Developed foreign equities | 14.21% | 6.90% |
| Emerging market equities | 5.49% | 7.40% |
| Private equity | 20.00% | 8.26% |
| Hedge funds/absolute return | 5.00% | 6.01% |
| Real estate (property) | 13.75% | 6.51% |
| Real estate (REITS) | 2.50% | 6.76% |
| Commodities | 1.25% | 6.07% |
| Total | 100.00% | |
| Assumed inflation - mean | | 2.75% |

The OIC's description of each asset class was used to map the target allocation to the asset classes. Each asset class assumption is based on a consistent set of underlying assumptions, and includes adjustment for the inflation assumption. These assumptions are not based on historical returns, but instead are based on a forward-looking capital market economic model.

Discount rate—The discount rate used to measure the total pension liability was 7.75 percent for the Defined Benefit Pension Plan. The projection of cash flows used to determine the discount rate assumed that the contributions from plan members and those of the contributing employers are made at the contractually required rates, as actuarially determined. Based on those assumptions, the pension plan's fiduciary net position was projected to be available to make all projected future benefit payments of the current plan members. Therefore, the long-term expected rate of return on pension plan investments for the Defined Benefit Pension Plan was applied to all periods of projected benefit payments to determine the total pension liability.

The following table presents the net pension liability (asset) calculated using the discount rate of 7.75 percent, as well as what the net pension liability (asset) would be if it were calculated using a discount rate that is one percent lower (6.75 percent) or one percent higher (8.75 percent) than the current rate (in millions):

| <u>Net Pension Liability (Asset)</u> | <u>1% Decrease (6.75%)</u> | <u>Discount Rate (7.75%)</u> | <u>1% Increase (8.75%)</u> |
|--------------------------------------|--------------------------------|----------------------------------|--------------------------------|
| Defined Benefit Pension Plan | \$ 82.5 | \$ 34.2 | \$ (6.5) |

Pension plan fiduciary net position—Detailed information about the pension plan's fiduciary net position is available in the separately issued PERS financial report.

Pension related payable—Prior to the formation of the PERS State and Local Government Rate Pool (SLGRP), the State and community colleges were pooled together in the State and Community College Pool (SCCP), while local government employers participated in the Local Government Rate Pool (LGRP). These two pools combined to form the SLGRP, effective

January 1, 2002. The unfunded actuarial liability (UAL) attributable to the SCCP at the time the SLGRP was formed is maintained separately from the SLGRP and is reduced by contributions and increased for interest charges at the assumed interest rate, which was 7.75 percent in fiscal year 2015. The pre-SLGRP pooled liability attributable to SAIF is being amortized over the period ending December 31, 2027. SAIF is being assessed an employer contribution rate of 1.85 percent of covered payroll for payment of this liability. The outstanding pre-SLGRP pooled liability as of December 31, 2015 for SAIF is \$10.6 million, of which \$0.4 million is recorded as the current portion, and is reported in the accompanying financial statements as pension related payable.

11. OTHER POSTEMPLOYMENT BENEFIT PLAN

Plan description—SAIF administers a single-employer defined benefit healthcare plan. SAIF employees retiring under Oregon PERS are eligible to receive medical coverage for self and eligible dependents until age 65. Retirees must pay the premium for the coverage elected. Premiums for coverage are identical for active and retired employees, except to the extent that SAIF pays all or a portion of its active employees' premiums. Participating retirees pay their own monthly premiums based on a blended premium rate since retirees are pooled together with active employees for insurance rating purposes. Benefit provisions are established by SAIF.

Funding policy—SAIF's funding policy provides for contributions at amounts sufficient to fund benefits on a pay-as-you-go basis. For the years ended December 31, 2015 and 2014, respectively, retired plan members contributed \$644 thousand and \$718 thousand through their required contributions, and the required contribution rate per retired member was an average of \$778 and \$893 per month.

Annual OPEB cost and net OPEB obligation—SAIF's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution (ARC) of the employer, an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

The following table shows the components of SAIF's annual OPEB cost for the years ended December 31, 2015, 2014, and 2013, the amount actually contributed, and changes in SAIF's net OPEB obligation to the plan (dollars in thousands):

| | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|---|-----------------|-----------------|-----------------|
| Annual required contribution | \$ 1,265 | \$ 1,909 | \$ 1,832 |
| Interest on net OPEB obligation | 200 | 151 | 101 |
| Adjustment to ARC | <u>(517)</u> | <u>(392)</u> | <u>(262)</u> |
| Annual OPEB cost (expense) | 948 | 1,668 | 1,671 |
| Contributions made | <u>514</u> | <u>704</u> | <u>666</u> |
| Increase in net OPEB obligation | 434 | 964 | 1,005 |
| Net OPEB obligation - beginning of year | <u>3,993</u> | <u>3,029</u> | <u>2,024</u> |
| Net OPEB obligation - end of year | <u>\$ 4,427</u> | <u>\$ 3,993</u> | <u>\$ 3,029</u> |
| Percent of annual OPEB cost contributed | 54.2% | 42.2% | 39.9% |

Actuarial methods and assumptions—Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events far into the future. Actuarially determined amounts are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The schedule of funding progress shown as required supplementary information presents multi-year trend

information about whether the actuarial value of assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits. Calculations are based on the types of benefits provided under the terms of the substantive plan at the time of each valuation and on the pattern of sharing of costs between the employer and participating members to that point. Actuarial calculations reflect a long-term perspective and include techniques that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

The postemployment healthcare benefit obligation was determined as part of the actuarial valuation prepared by a consulting actuary as of January 1, 2015, using the projected unit credit cost method. Significant assumptions used in the actuarial valuation include a 5.00 percent investment rate of return. A 6.25 percent health care cost trend rate was used for 2016, 6.00 percent for 2017, 5.25 percent for 2018 through 2019, 5.50 percent for 2020 through 2029, 6.00 percent for 2030, 6.75 percent for 2031 through 2032, 6.50 percent for 2033 through 2037, 6.25 percent for 2038 through 2040, 6.00 percent for 2041 through 2047, 5.75 percent for 2048 through 2060, 5.50 percent for 2061 through 2063, 5.25 percent for 2064 through 2066, 5.00 percent for 2067 through 2069, and a 4.75 percent ultimate trend rate thereafter. The unfunded actuarial accrued liability (UAAL) is being amortized as a level dollar amount over an open period of 10 years. As GASB Statement No. 45 was implemented prospectively, there was no net OPEB liability at transition on January 1, 2007.

Funding progress information—The funded status as of the most recent actuarial valuation date is as follows (dollars in thousands):

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (b) | Unfunded Actuarial Accrued Liability (UAAL) (b-a) | Funded Ratio (a/b) | Annual Covered Payroll (c) | UAAL as a Percentage of Annual Covered Payroll ((b-a)/c) |
|--------------------------|-------------------------------|---------------------------------|---|--------------------|----------------------------|--|
| 01/01/2011 | \$0 | \$6,980 | \$6,980 | 0.0% | \$56,948 | 12.3% |
| 01/01/2013 | \$0 | \$10,150 | \$10,150 | 0.0% | \$61,712 | 16.4% |
| 01/01/2015 | \$0 | \$7,201 | \$7,201 | 0.0% | \$68,447 | 10.5% |

(Unaudited)
REQUIRED SUPPLEMENTARY INFORMATION
POSTEMPLOYMENT HEALTHCARE BENEFIT PLAN
SCHEDULE OF FUNDING PROGRESS AND EMPLOYER CONTRIBUTIONS
For the years ended December 31, 2015 and 2014
(In thousands)

The Schedule of Funding Progress and the Schedule of Employer Contributions present multi-year trend information comparing the actuarial value of plan assets to the actuarial accrued liability, and the actual contributions to the annual required contributions.

Schedule of Funding Progress

| Actuarial Valuation Date | Actuarial Value of Assets (a) | Actuarial Accrued Liability (b) | Unfunded Actuarial Accrued Liability (UAAL) (b-a) | Funded Ratio (a/b) | Annual Covered Payroll (c) | UAAL as a Percentage of Annual Covered Payroll ((b-a)/c) |
|--------------------------|-------------------------------|---------------------------------|---|--------------------|----------------------------|--|
| 01/01/2011 | \$0 | \$6,980 | \$6,980 | 0.0% | \$56,948 | 12.3% |
| 01/01/2013 | \$0 | \$10,150 | \$10,150 | 0.0% | \$61,712 | 16.4% |
| 01/01/2015 | \$0 | \$7,201 | \$7,201 | 0.0% | \$68,447 | 10.5% |

Schedule of Employer Contributions

| | <u>2015</u> | <u>2014</u> | <u>2013</u> |
|---|-----------------|-----------------|-----------------|
| Annual required contribution | \$ 1,265 | \$ 1,909 | \$ 1,832 |
| Interest on net OPEB obligation | 200 | 151 | 101 |
| Adjustment to ARC | <u>(517)</u> | <u>(392)</u> | <u>(262)</u> |
| Annual OPEB cost (expense) | 948 | 1,668 | 1,671 |
| Contributions made | <u>514</u> | <u>704</u> | <u>666</u> |
| Increase in net OPEB obligation | 434 | 964 | 1,005 |
| Net OPEB obligation - beginning of year | <u>3,993</u> | <u>3,029</u> | <u>2,024</u> |
| Net OPEB obligation - end of year | <u>\$ 4,427</u> | <u>\$ 3,993</u> | <u>\$ 3,029</u> |
| Percent of annual OPEB cost contributed | 54.2% | 42.2% | 39.9% |

Summary of Key Actuarial Methods and Assumptions

| | |
|-----------------------------|--|
| Actuarial valuation date | As of January 1, 2015 |
| Actuarial cost method | Projected Unit Credit Cost Method |
| Amortization | 10 years |
| Discount rate | 5.00% |
| Health care cost trend rate | A 6.25 percent health care cost trend rate was used for 2016, 6.00 percent for 2017, 5.25 percent for 2018 through 2019, 5.50 percent for 2020 through 2029, 6.00 percent for 2030, 6.75 percent for 2031 through 2032, 6.50 percent for 2033 through 2037, 6.25 percent for 2038 through 2040, 6.00 percent for 2041 through 2047, 5.75 percent for 2048 through 2060, 5.50 percent for 2061 through 2063, 5.25 percent for 2064 through 2066, 5.00 percent for 2067 through 2069, and a 4.75 percent ultimate trend rate thereafter. |

(Unaudited)
REQUIRED SUPPLEMENTARY INFORMATION
DEFINED BENEFIT PENSION PLAN
SCHEDULE OF PROPORTIONATE SHARE OF THE NET PENSION LIABILITY (ASSET)
AND EMPLOYER CONTRIBUTIONS
For the years ended December 31, 2015 and 2014
(In thousands)

The Schedule of the Proportionate Share of the Net Pension Liability (Asset) and the Schedule of Employer Contributions present multi-year trend information comparing the proportionate share of the net pension liability (asset) to covered-employee payroll, and the actual contributions to the contractually required contributions.

Schedule of the Proportionate Share of the Net Pension Liability (Asset)

| | <u>2015</u> | <u>2014</u> |
|--|-------------|-------------|
| Proportion of the net pension liability (asset) | 0.60% | (0.54%) |
| Proportionate share of the net pension liability (asset) | \$ 34,187 | \$ (12,351) |
| Covered-employee payroll | \$ 68,447 | \$ 65,145 |
| Employer net pension liability (asset) as a percentage of covered-employee payroll | 49.9% | (18.9%) |
| Plan fiduciary net position as a percentage of the total pension liability | 91.9% | 103.6% |

Schedule of Employer Contributions

| | <u>2015</u> | <u>2014</u> |
|---|----------------|----------------|
| Contractually required contributions | \$ 6,541 | \$ 5,778 |
| Contributions in relation to the contractually required contributions | <u>(6,541)</u> | <u>(5,778)</u> |
| Contribution deficiency (excess) | <u>\$ -</u> | <u>\$ -</u> |
| Covered-employee payroll | \$ 68,447 | \$ 65,145 |
| Contributions as a percentage of covered-employee payroll | 9.6% | 8.9% |

10-year trend information specific to SAIF Corporation is not available prior to the year ended December 31, 2014.

