

# FINANCIAL AUDIT

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Commonwealth of Pennsylvania  
Department of Labor and Industry  
State Workers' Insurance Fund  
Harrisburg, Pennsylvania  
For the Years Ended December 31, 2019  
and December 31, 2018

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December 2020



Commonwealth of Pennsylvania  
Department of the Auditor General

Eugene A. DePasquale • Auditor General

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**DEPARTMENT OF LABOR AND INDUSTRY  
STATE WORKERS' INSURANCE FUND  
DECEMBER 31, 2019 and 2018**

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**TABLE OF CONTENTS**

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Background .....	1
Independent Auditor's Report.....	2
SWIF Management's Discussion and Analysis .....	5
Statements of Operations and Changes in Surplus (Statutory Basis) .....	8
Statements of Operations and Changes in Surplus (Statutory Basis) .....	9
Statements of Cash Flows (Statutory Basis).....	10
Notes to Financial Statements.....	11
Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With <i>Government Auditing Standards</i> .....	28
Distribution List .....	30

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**DEPARTMENT OF LABOR AND INDUSTRY  
STATE WORKERS' INSURANCE FUND  
DECEMBER 31, 2019 and 2018**

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**BACKGROUND**

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The State Workers' Insurance Fund (SWIF) is a self-sustaining fund operating within the Pennsylvania Department of Labor and Industry for the purpose of providing workers' compensation insurance to employers, including those refused policies by private insurance firms. SWIF is subject to underwriting rules, classifications, and rates promulgated by rating bureaus authorized by the State Insurance Commissioner. A board consisting of the Secretary of Labor and Industry, the State Treasurer, and the Insurance Commissioner oversees operations of the fund.



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AUDITOR GENERAL

### **Independent Auditor's Report**

The Honorable Tom Wolf  
Governor  
Commonwealth of Pennsylvania  
Harrisburg, PA 17120

#### **Report on the Financial Statements**

We have audited the accompanying Statements of Admitted Assets, Liabilities and Surplus-statutory basis of the State Workers' Insurance Fund (SWIF) as of December 31, 2019, and December 31, 2018, and the related Statements of Operations and Changes in Surplus-statutory basis and the Statements of Cash Flows-statutory basis for the years then ended, and the related notes to the financial statements.

#### ***Management's Responsibility for the Financial Statements***

Management is responsible for the preparation and fair presentation of these financial statements in accordance with statutory accounting practices as prescribed or permitted by the Insurance Department of Pennsylvania. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

#### ***Auditor's Responsibility***

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

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the admitted assets, liabilities, and surplus of SWIF as of December 31, 2019, and December 31, 2018, and the results of its operations and its cash flows for the years then ended in accordance with statutory accounting practices as prescribed or permitted by the Insurance Department of Pennsylvania as described in Note A.

### ***Basis of Accounting***

We draw attention to Note A of the financial statements, which describes the basis of accounting. As described in Note A to the financial statements, the financial statements are prepared by SWIF in accordance with statutory accounting practices as prescribed or permitted by the Insurance Department of Pennsylvania, which is a basis of accounting other than accounting principles generally accepted in the United States of America, to meet the requirements of the Insurance Department of Pennsylvania. The effects on the financial statements of the variances between these regulatory accounting practices and accounting principles generally accepted in the United States of America, although not reasonably determinable, are presumed to be material. Our opinion is not modified with respect to this matter.

### ***Emphasis of Matter***

As discussed in Note E, the insurance loss liability of SWIF is based on actuarial analysis of historical experience adjusted to estimate the impact of Act 44 of 1993 and Act 57 of 1996 and changes in claims management practices adopted by SWIF management. Because of the length of time required for the actual insurance loss liability to be determined and the uncertainty regarding whether the adjusted data will be supported by future claim payments, the actual liability may vary significantly from the estimated amount provided for in the Statements of Admitted Assets, Liabilities and Surplus-statutory basis.

## ***Other Matters***

### *Supplementary Information*

Our audit was conducted for the purpose of forming an opinion on the statutory financial statements as a whole. The management's discussion and analysis is presented for purposes of additional analysis and is not a required part of the statutory financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the statutory financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

### *Other Information*

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

## **Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated December 1, 2020, on our consideration of SWIF'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 SWIF's internal control over financial reporting and compliance.

## ***Restriction on Use***

Our report is intended solely for the information and use of the board of directors and management of SWIF, others within the entity, and for filing with the Insurance Department of Pennsylvania, and is not intended to be and should not be used by anyone other than those specified parties.

December 1, 2020



Eugene A. DePasquale  
Auditor General

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**DEPARTMENT OF LABOR AND INDUSTRY  
STATE WORKERS' INSURANCE FUND  
DECEMBER 31, 2019 and 2018**

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**SWIF MANAGEMENT'S DISCUSSION AND ANALYSIS**

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**Assets and Liabilities**

The State Workers' Insurance Fund (SWIF) disclosed total admitted assets of \$1.434 billion as of December 31, 2019. This was an increase of \$1 million or 0.07% from 2018. Total investments increased from \$1.372 billion in 2018 to \$1.389 billion in 2019 or a \$17 million increase. This increase was offset by a decrease of \$15.4 million in receivables.

SWIF's total liabilities decreased to \$1.403 billion, a decrease of \$105 million or 6.96% from the prior year. Net unpaid losses decreased as of year-end 2019 to \$1.089 billion from \$1.190 billion in the prior year, a decrease of \$101 million or 8.48%. This decrease was due to an actuarial adjustment to SWIF's incurred but not reported and bulk reserves. Unpaid loss adjustment expenses increased by \$12.5 million, due to an increase in the loss adjustment expense ratio. All other liabilities decreased \$16.5 million mainly due to an \$18 million decrease in unearned premiums.

**Surplus**

Surplus as regards policyholders was \$30.78 million, a decrease in the deficit of \$106 million or 142% for 2019 as compared to the reported deficit of (\$74.9) million in 2018. SWIF's net income before other changes in surplus for 2019 was \$81.7 million versus a net income in 2018 of \$66.9 million. The improvement to SWIF's deficit was largely due to the net income of \$81.7 million and the change in unrealized capital gains of \$26 million.

SWIF continues to discount its loss reserves at a discount rate of 2%.

SWIF now has a surplus due to a change in an actuarial estimate. We have implemented several initiatives to keep the surplus positive, as outlined below in the section titled Future Initiatives.

**Operational Results**

SWIF recorded net income before other changes in surplus of \$81.7 million for 2019. This is an increase of \$14.8 million as compared to the 2018 net income of \$66.9 million. The earned premiums decreased by \$33.2 million or 20.7% to \$127.1 million in 2019, from \$160.3 million in 2018. This decline in earned premium was offset by a decrease in underwriting expense of \$24 million. This led to a decrease in underwriting gain of \$9 million. The decrease in underwriting gain was offset by a \$25 million increase in net investment income.

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**DEPARTMENT OF LABOR AND INDUSTRY  
STATE WORKERS' INSURANCE FUND  
DECEMBER 31, 2019 and 2018**

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**SWIF MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

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Net investment income increased 50.3% or \$24.7 million to \$73.8 million. During 2019, SWIF had an increase in its investment portfolio performance as total yield increased to 11.7% from (0.8%) in 2018. The 2019 yield of SWIF's fixed income portfolio was 10.2% and equity yield was 30.4%.

During 2019, SWIF also had a \$9.8 million net loss in charged off premium that reduced SWIF's overall net income. This premium was ruled uncollectible and charged off through the Pennsylvania Attorney General's Office.

**Future Initiatives**

SWIF'S Compromise and Release Initiative continues to produce savings in future reserves. During 2019, 609 claims were settled that resulted in loss reserve savings of \$46.6 million.

SWIF continues to closely monitor staffing levels as a means of controlling personnel expense. As of year-end 2019, the SWIF staffing level increased slightly from 209 employees to 211.

SWIF contracted with Hoover Rehabilitation Inc. in May 2013 for the Medical Bill Repricing, Preferred Provider Organization, Pharmacy Benefit Management, and Durable Medical Equipment. During 2019, SWIF realized net savings below medical bill fee schedule of 10.39% for medical bill payment savings of \$7.5 million.

During 2019, SWIF's Customer Service Unit handled 61,945 of the 70,489 calls received or 87.9% of all calls. This unit eliminates the need to transfer calls to the Underwriting Claims, Auditing, and Accounting Divisions. This unit also handled 3,439 first report of injury calls.

SWIF is currently engaged in a project to update its information technology platform. The current operating system, PowerComp, is being replaced by Guidewire, an industry leading property casualty tool. This installation is being performed by Deloitte in conjunction with the Employment, Banking, and Revenue Delivery Center in the Pennsylvania Office of Administration, Office for Information Technology, and the SWIF staff. The new platform, along with an organizational transformation effort, will bring SWIF more in line with the best practices of the workers' compensation insurance market. As part of this upgrade, SWIF will offer an interactive customer portal that will allow for enhanced customer services to both claimants and policyholders.

As of April 2019, SWIF's Commercial Loss Cost Multiplier (LCM) remained at 3.187 and Coal LCM at 1.904.

In 2017, SWIF began to transition its investment portfolio to the Pennsylvania Treasury Department, which should lead to savings in SWIF's future investment expense. The equity portion of the portfolio was transitioned in 2018 and the fixed portion was completed in June 2019.



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**DEPARTMENT OF LABOR AND INDUSTRY  
STATE WORKERS' INSURANCE FUND  
DECEMBER 31, 2019 and 2018**

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**SWIF MANAGEMENT'S DISCUSSION AND ANALYSIS (Continued)**

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SWIF is the third-party administrator for the Commonwealth's Uninsured Employers Guarantee Fund and the Self-Insurance Guarantee Fund which resulted in annual revenue of \$624,598 for 2019.

In July 2019, SWIF raised its minimum premium from \$564 to \$612.

SWIF collected \$1,186,168 in past due premium during 2019 through its credit card program titled SWIFPay. This includes dollars from the SWIFPhone program that was launched in May of 2019.

**STATE WORKERS' INSURANCE FUND**  
**DECEMBER 31, 2019 and 2018**

**STATEMENTS OF ADMITTED ASSETS, LIABILITIES AND SURPLUS (statutory basis)**

<u>ADMITTED ASSETS</u>	(Expressed in Thousands)	
<u>Investments</u>	<u>2019</u>	<u>2018</u>
Bonds	\$ 1,210,441	\$ 1,226,817
Stocks	124,194	95,541
Short-term investments	54,428	49,768
Total Investments – Note B	\$ 1,389,063	\$ 1,372,126
 <u>Cash</u>		
On deposit in Treasury Department	\$ 2,052	\$ 2,640
 <u>Receivables</u>		
Uncollected premiums in course of collection	\$ 4,791	\$ 5,355
Premiums, agents' balances, and installments booked but deferred and not yet due	28,338	40,993
Reinsurance recoverable on loss payments	309	2,234
Interest due and accrued on investments	9,104	9,722
Funds held by or deposited with reinsurance companies	14	14
Other amounts receivable under reinsurance contracts	305	0
Accrued retrospective premiums	162	152
Total receivables	\$ 43,023	\$ 58,470
<b>Total Admitted Assets</b>	<b>\$ 1,434,138</b>	<b>\$ 1,433,236</b>
 <u>LIABILITIES AND SURPLUS</u>		
 <u>Liabilities</u>		
Net unpaid losses – Notes C and E	\$ 1,089,194	\$ 1,190,090
Unpaid loss adjustment expenses	246,153	233,618
Reinsurance payable	26	22
Premium deficiency reserve	631	0
Accrued administrative expenses	6,907	9,251
Unearned premiums	38,418	56,303
Ceded reinsurance premiums payable	0	3
Policyholders' premium credit balances	9,815	10,783
Restricted account – Commonwealth Self Insurance	2,430	2,460
Policyholder deposits	1,425	1,910
Net payable for securities	5,238	106
Other liabilities	3,121	3,637
Total liabilities	\$ 1,403,358	\$ 1,508,183
 <u>Surplus</u>		
Unassigned surplus (deficit) – Note F	30,780	(74,947)
Total surplus (deficit) as regards policyholders	\$ 30,780	\$ (74,947)
<b>Total Liabilities and Surplus</b>	<b>\$ 1,434,138</b>	<b>\$ 1,433,236</b>

~ The notes to the financial statements are an integral part of these statements. ~

**STATE WORKERS' INSURANCE FUND  
FOR THE YEARS ENDED DECEMBER 31, 2019 and 2018**

**STATEMENTS OF OPERATIONS AND CHANGES IN SURPLUS (statutory basis)**

(Expressed in Thousands)

	<u>2019</u>	<u>2018</u>
<b><u>Underwriting Income</u></b>		
Premiums earned	\$ 127,186	\$ 160,309
<b><u>Underwriting Expenses</u></b>		
Losses incurred	\$ 44,554	\$ 100,695
Loss adjustment expenses	47,364	14,058
Other	17,534	18,945
Change in premium deficiency reserve	631	0
Total underwriting expenses	<u>\$ 110,083</u>	<u>\$ 133,698</u>
<b>Net Underwriting Gain (Loss)</b>	<u>\$ 17,103</u>	<u>\$ 26,611</u>
<b><u>Investment Income</u></b>		
Investment income earned	\$ 44,084	\$ 46,437
Net realized capital gains (losses)	31,426	5,150
Total investment income	<u>\$ 75,510</u>	<u>\$ 51,587</u>
<b><u>Investment Expenses</u></b>	<u>\$ 1,698</u>	<u>\$ 2,439</u>
<b>Net Investment Income</b>	<u>\$ 73,812</u>	<u>\$ 49,148</u>
<b><u>Other Income/Expenses</u></b>		
Other income (expenses)	\$ 586	\$ 630
Net loss from premium balances charged off	(9,808)	(9,483)
Total other income/expenses	<u>\$ (9,222)</u>	<u>\$ (8,853)</u>
<b><u>Net Income (Loss) Before Other Changes in Surplus</u></b>	<u>\$ 81,693</u>	<u>\$ 66,906</u>
<b><u>Other Changes in Surplus</u></b>		
Change in net unrealized capital gain (loss)	\$ 26,097	\$ (32,261)
Change in nonadmitted assets	(1,984)	1,823
Prior period adjustment	(79)	0
Total other changes in surplus	<u>\$ 24,034</u>	<u>\$ (30,438)</u>
<b>Net change in surplus (deficit) during the year</b>	<u>\$ 105,727</u>	<u>\$ 36,468</u>
<b>Surplus (deficit) at beginning of year</b>	<u>\$ (74,947)</u>	<u>\$ (111,415)</u>
<b>Surplus (deficit) at end of year</b>	<u><u>\$ 30,780</u></u>	<u><u>\$ (74,947)</u></u>

~ The notes to the financial statements are an integral part of these statements. ~

**STATE WORKERS' INSURANCE FUND  
FOR THE YEARS ENDED DECEMBER 31, 2019 and 2018**

**STATEMENTS OF CASH FLOWS (statutory basis)**

(Expressed in Thousands)

	<u>2019</u>	<u>2018</u>
<b>Cash flows from operating activities:</b>		
Premiums collected net of reinsurance	\$ 119,310	\$ 161,485
Benefit and loss related payments	(143,825)	(154,494)
Commissions, expenses paid, and aggregate write-ins	(56,149)	(51,037)
Investment income (net of investment expenses)	46,288	42,722
Miscellaneous income (uses)	(9,222)	(8,853)
Net cash from operating activities	<u>\$ (43,598)</u>	<u>\$ (10,177)</u>
<b>Cash flows from investing activities:</b>		
Proceeds from sale of bonds	\$ 1,502,431	\$ 925,721
Proceeds from sale of stocks	253	140,960
Payments for purchase of bonds	(1,457,101)	(949,960)
Payments for purchase of stocks	(2,806)	(107,323)
Miscellaneous proceeds (applications)	5,132	(2,939)
Net cash from investing activities	<u>\$ 47,909</u>	<u>\$ 6,459</u>
<b>Cash flows from miscellaneous sources:</b>		
Other cash provided (applied)	<u>\$ (239)</u>	<u>\$ (1,749)</u>
<b>Net change in cash and short-term investments</b>	<u>\$ 4,072</u>	<u>\$ (5,467)</u>
<b>Cash and short-term investments at beginning of year</b>	<u>\$ 52,408</u>	<u>\$ 57,875</u>
<b>Cash and short-term investments at end of year</b>	<u><u>\$ 56,480</u></u>	<u><u>\$ 52,408</u></u>

~ The notes to the financial statements are an integral part of these statements. ~

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**STATE WORKERS' INSURANCE FUND  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2019 and 2018**

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**NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

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The State Workers' Insurance Fund (SWIF) prepares its statutory financial statements in accordance with statutory accounting practices as prescribed or permitted by rules and regulations promulgated by the Insurance Department of Pennsylvania. These statutory practices are primarily designed to demonstrate solvency and differ from generally accepted accounting principles (GAAP) in certain significant areas:

- Certain assets, designated as nonadmitted, are not permitted to be reported in the statutory financial statements and are charged directly to surplus. Major nonadmitted assets include premiums due in excess of statutory limitations (three months); expenses for furniture, fixtures, and supplies; and unrealized gains or losses on investments. Under GAAP, these items would be treated as assets net of the related contra accounts of allowance for doubtful accounts, depreciation, and valuation allowances for investments.
- Certain disclosures required under GAAP are not required under SWIF's statutory accounting practices as follows:
  - Securities lending transactions involving the receipt of cash collateral (or securities that may be pledged or sold without default) with an asset and a liability related to the receipt of the collateral reported on SWIF's Balance Sheet.
  - A Statement of Cash Flows which includes a reconciliation of operating income to net cash provided by (used for) operating activities and which excludes short-term investments.
  - Reporting certain investments at fair value in the Balance Sheet with the current year change in fair value recognized as an element of investment income in the Operating Statement.
  - Reporting the net pension liability and related deferred outflows of resources and deferred inflows of resources.
  - Reporting the net other postemployment benefits liability and related deferred outflows of resources and deferred inflows of resources.

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**STATE WORKERS' INSURANCE FUND  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2019 and 2018**

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**NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**

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Investments

Investments are stated on the basis adopted by the National Association of Insurance Commissioners (NAIC) and are recorded based on trade date. The book/adjusted carrying value of bonds is stated at amortized cost. The book/adjusted carrying value of common stock is reported at market value with market value rates taken from the custodian statement. Preferred stock is reported at cost/amortized cost. Realized investment gains or losses are included in the Statement of Operations and Changes in Surplus. Unrealized investment gains or losses from revaluation of investments (i.e., stocks) are charged directly to surplus. Short-term investments are recorded at cost which approximates fair value.

Premium and Revenue Recognition

Premiums earned and assessments billed to policyholders are recorded as income. Unearned premiums and assessments are recorded as a liability and earned as the policy term expires. Premiums and assessments are booked as written on the effective date of the policy. Assessments paid are classified as expenses.

Loss and Loss Adjustment Expense Reserves

The liability for unpaid losses is based upon individual case estimates adjusted for incurred but not reported losses based on past experience, a probable loss reserve, and statutory minimum requirements as determined by SWIF's Actuarial Committee and independent review by outside actuaries. Loss reserves ceded by the National Workers' Compensation Reinsurance Pool and the Pennsylvania Workers' Compensation Reinsurance Pool and assumed by SWIF are included in loss reserves. The liability for loss adjustment expense is determined by SWIF's Actuarial Committee as a percentage of loss reserves based on past experience.

Use of Estimates

The preparation of the accompanying Statements of Admitted Assets, Liabilities and Surplus-statutory basis requires management to make estimates and assumptions that affect the reported amounts of admitted assets, liabilities, surplus, and disclosure of contingent liabilities at the date of this statutory financial statement. Actual results could differ from those estimates.

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**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

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**NOTE B – INVESTMENTS**

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GAAP (per Governmental Accounting Standards Board Statement No. 40) requires certain disclosures regarding policies and practices with respect to investments and the risks associated with them. Although these disclosures are not required for the statutory financial statements of SWIF, similar informative disclosures have been provided as follows:

SWIF categorizes investments according to the level of investment risk assumed by the Commonwealth. SWIF has formally adopted a written investment policy. Provisions of the written investment policy and current management of the investments consider custodial credit risk, concentration of credit risk, credit risk, interest rate risk, and foreign currency risk. The identified risks are discussed in detail below.

*Custodial Credit Risk* – Custodial credit risk for investments is the risk that, in the event of the failure of the counterparty to a transaction, SWIF would not be able to recover the value of investment or collateral securities that are in the possession of an outside party. In accordance with a contractual relationship between SWIF and its custodial agents, substantially all investments, where securities are used as evidence of the investment, are held by the custodians in book entry form in the name of the Commonwealth or the custodian. These investments are defined as insured or registered investments for which the securities are held by SWIF or its agent.

*Concentration of Credit Risk* – Concentration of credit risk is the risk of loss attributed to the magnitude of the government's investment in a single issuer. SWIF's investment policy does not place a limit on the concentration of investments in any one issuer.

*Credit Risk* – Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The credit risk of a debt instrument is measured by nationally-recognized statistical rating agencies such as Moody's Investors Services (Moody's). SWIF requires fund assets to be invested in investment grade bonds rated BBB/Baa (or equivalent) or better except that investment managers may invest up to 10 percent of the total fixed income portfolio in non-investment grade bonds. The investments rated NR (Not Rated) and WR (Withdrawn Rating) are approximately 2 percent of the fixed income portfolio at December 31, 2019. This excludes share balances of \$48 million in the Treasury Department's unrated short-term investment pools.

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

The following tables disclose aggregate fair value, by major Moody's credit quality rating category at December 31, 2019 and 2018 (amounts in thousands):

**December 31, 2019**

<u>Investment Type</u>	<u>Amount</u>	<u>Moody's Rating</u>	<u>% Portfolio</u>
US Agency	\$ 1,066	A1	0.08%
US Agency	1,113	A2	0.08%
US Agency	454	Aa1	0.03%
US Agency	1,302	Aa2	0.09%
US Agency	2,102	Aaa	0.15%
US Agency	702	Baa1	0.05%
US Agency	736	Baa2	0.05%
US Agency	221	Baa3	0.02%
<b>Total US Agency Securities</b>	<b>\$ 7,696</b>		
US Government Securities	\$ 252,769	Aaa	17.85%
<b>Total US Government Securities</b>	<b>\$ 252,769</b>		
Mortgage-Backed Securities	\$ 253,523	Aaa	17.90%
Mortgage-Backed Securities	177	Ba1	0.01%
Mortgage-Backed Securities	4,082	NR	0.29%
<b>Total Mortgage-Backed Securities</b>	<b>\$ 257,782</b>		
Asset Backed Securities	\$ 702	A2	0.05%
Asset Backed Securities	1,822	A3	0.13%
Asset Backed Securities	365	Aa2	0.03%
Asset Backed Securities	977	Aa3	0.07%
Asset Backed Securities	771	Aaa	0.05%
Asset Backed Securities	427	Ba1	0.03%
Asset Backed Securities	463	Baa1	0.03%
Asset Backed Securities	2,467	Baa2	0.17%
Asset Backed Securities	2,997	NR	0.21%
<b>Total Asset Backed Securities</b>	<b>\$ 10,991</b>		
Corporate Obligations	\$ 61,372	A1	4.33%
Corporate Obligations	85,849	A2	6.06%
Corporate Obligations	100,398	A3	7.09%
Corporate Obligations	13,528	Aa1	0.96%
Corporate Obligations	20,943	Aa2	1.48%
Corporate Obligations	24,423	Aa3	1.72%



**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

<u>Investment Type</u>	<u>Amount</u>	<u>Moody's Rating</u>	<u>% Portfolio</u>
Corporate Obligations	\$ 6,259	Aaa	0.44%
Corporate Obligations	9,138	B1	0.65%
Corporate Obligations	329	B2	0.02%
Corporate Obligations	45,697	Ba1	3.23%
Corporate Obligations	23,899	Ba2	1.69%
Corporate Obligations	24,044	Ba3	1.70%
Corporate Obligations	86,482	Baa1	6.11%
Corporate Obligations	95,776	Baa2	6.76%
Corporate Obligations	98,322	Baa3	6.94%
Corporate Obligations	17,630	NR	1.24%
Corporate Obligations	713	WR	0.05%
<b>Total Corporate Obligations</b>	<b>\$ 714,802</b>		
<b>Treasury Investment Program</b>	<b>\$ 48,007</b>	NR	3.39%
<b>Total Fixed Income Securities</b>	<b>\$ 1,292,047</b>		
<b>Equity Securities</b>	<b>\$ 124,194</b>	NR	8.77%
<b>Total Portfolio at December 31, 2019</b>	<b>\$ 1,416,241</b>		<b>100.00%</b>

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

**December 31, 2018**

<u>Investment Type</u>	<u>Amount</u>	<u>Moody's Rating</u>	<u>% Portfolio</u>
US Agency	\$ 8,470	A1	0.63%
US Agency	2,728	A2	0.20%
US Agency	3,427	Aa1	0.25%
US Agency	3,811	Aa2	0.28%
US Agency	3,878	Aa3	0.29%
US Agency	29,588	Aaa	2.19%
US Agency	286	Baa2	0.02%
US Agency	174	Baa3	0.01%
US Agency	9,184	NR	0.68%
<b>Total US Agency Securities</b>	<b>\$ 61,546</b>		
US Government Securities	\$ 227,623	Aaa	16.85%
<b>Total US Government Securities</b>	<b>\$ 227,623</b>		
Mortgage-Backed Securities	\$ 339	A1	0.03%
Mortgage-Backed Securities	128	A3	0.01%
Mortgage-Backed Securities	100	Aa3	0.01%
Mortgage-Backed Securities	196,317	Aaa	14.53%
Mortgage-Backed Securities	266	Ba1	0.02%
Mortgage-Backed Securities	251	Ba2	0.02%
Mortgage-Backed Securities	71	Ba3	0.01%
Mortgage-Backed Securities	306	Baa1	0.02%
Mortgage-Backed Securities	841	Baa3	0.06%
Mortgage-Backed Securities	608	WR	0.04%
Mortgage-Backed Securities	8,235	NR	0.61%
<b>Total Mortgage-Backed Securities</b>	<b>\$ 207,462</b>		
Asset Backed Securities	\$ 678	A1	0.05%
Asset Backed Securities	1,133	A2	0.08%
Asset Backed Securities	3,992	A3	0.30%
Asset Backed Securities	484	Aa1	0.04%
Asset Backed Securities	841	Aa2	0.06%
Asset Backed Securities	2,966	Aa3	0.22%
Asset Backed Securities	31,821	Aaa	2.35%
Asset Backed Securities	1,314	Baa1	0.10%
Asset Backed Securities	998	Baa2	0.07%
Asset Backed Securities	16,682	NR	1.23%
<b>Total Asset Backed Securities</b>	<b>\$ 60,909</b>		

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

<u>Investment Type</u>	<u>Amount</u>	<u>Moody's Rating</u>	<u>% Portfolio</u>
Corporate Obligations	\$ 68,167	A1	5.04%
Corporate Obligations	79,013	A2	5.85%
Corporate Obligations	115,631	A3	8.56%
Corporate Obligations	8,582	Aa1	0.64%
Corporate Obligations	26,168	Aa2	1.94%
Corporate Obligations	23,985	Aa3	1.77%
Corporate Obligations	12,962	Aaa	0.96%
Corporate Obligations	868	B1	0.06%
Corporate Obligations	347	B2	0.03%
Corporate Obligations	20,855	Ba1	1.54%
Corporate Obligations	4,653	Ba2	0.34%
Corporate Obligations	5,419	Ba3	0.40%
Corporate Obligations	119,596	Baa1	8.85%
Corporate Obligations	88,860	Baa2	6.58%
Corporate Obligations	64,510	Baa3	4.77%
Corporate Obligations	14,898	NR	1.10%
Corporate Obligations	1,040	WR	0.08%
<b>Total Corporate Obligations</b>	<b>\$ 655,554</b>		
<b>Treasury Investment Program</b>	<b>\$ 42,647</b>	NR	3.16%
<b>Total Fixed Income Securities</b>	<b>\$ 1,255,741</b>		
<b>Equity Securities</b>	<b>\$ 95,291</b>	NR	7.05%
<b>Preferred Securities</b>	<b>\$ 249</b>	NR	0.02%
<b>Total Portfolio at December 31, 2018</b>	<b>\$ 1,351,281</b>		<b>100.00%</b>

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

*Interest Rate Risk* – Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. SWIF measures interest rate risk using duration. As means for limiting SWIF's exposure to fair value losses arising from rising interest rates, SWIF requires investments to have maturities consistent with SWIF's liabilities. SWIF's long-term asset allocation diversifies its fixed income core segment between intermediate duration and longer duration strategies. Duration is a measure of an investment's sensitivity to changes in interest rates. The higher the duration, the greater the changes in fair value when interest rates change. For reporting purposes, SWIF elects to use option-adjusted duration, which takes into account embedded options affecting cash flows. At December 31, 2019 and 2018, SWIF's fixed income portfolio had the following option-adjusted durations by fixed income sector:

<u>December 31, 2019</u> <u>Investment Type</u>	<u>Amount</u>	<u>Duration</u> <u>(in years)</u>
US Agency Securities	\$ 7,696	10.84
US Government Securities	252,769	9.69
Mortgage Backed Securities	257,782	3.34
Asset Backed Securities	10,991	5.24
Corporate Obligations	714,802	4.81
Treasury Investment Program	48,007	N/A
<b>Total Fixed Income Securities</b>	<b><u>\$ 1,292,047</u></b>	
Equity Securities	<u>124,194</u>	N/A
<b>Total Portfolio Securities</b>	<b><u>\$ 1,416,241</u></b>	

N/A – Indicates duration is not applicable to investment.

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

<u>December 31, 2018</u> <u>Investment Type</u>	<u>Amount</u>	<u>Duration</u> <u>(in years)</u>
US Agency Securities	\$ 61,546	5.35
US Government Securities	227,623	9.08
Mortgage Backed Securities	207,462	3.72
Asset Backed Securities	60,909	2.78
Corporate Obligations	655,554	6.51
Treasury Investment Program	42,647	N/A
<b>Total Fixed Income Securities</b>	<b>\$ 1,255,741</b>	
Equity Securities	95,291	N/A
Preferred Securities	249	N/A
<b>Total Portfolio Securities</b>	<b>\$ 1,351,281</b>	

N/A – Indicates duration is not applicable to investment.

**Foreign Currency Risk** – Foreign currency risk is the risk that changes in exchange rates will adversely affect the fair value of an investment. All SWIF investments are denominated in US dollars, issued under US laws and regulations, designed for US investors, and traded in US markets.

Securities Lending Program

The Fiscal Code provides the Treasury Department with numerous custodial responsibilities; the securities lending program (SLP) is an integral part of the custodial function. A contract between the Treasury Department and its custodian, acting as lending agent, provides that the custodian lends securities owned by SWIF to independent brokers, dealers and banks, acting as borrowers.

Lending agreements between the custodian and the borrowers require that the custodian receives collateral from the borrowers in exchange for the securities lent. For collateral received which is not denominated in United States dollars or whose primary trading market is located outside the United States, the fair value of the collateral received must be at least 105 percent of the fair value of the securities lent. The fair value of all other collateral received must be at least 102 percent of the fair value of the securities lent. Securities lent consist of both domestic and foreign equity securities and United States Treasury and foreign debt obligations. Almost all collateral received consists of cash; a very small portion of collateral received consists of letters of credit, United States Treasury, corporate, and/or foreign debt obligations. Collateral is priced to market daily.

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**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

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**NOTE B – INVESTMENTS (Continued)**

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Additional collateral from borrowers is required if the fair value of the collateral received declines below lending agreement requirements. The lending agent cannot pledge or sell collateral securities received unless the borrower defaults. Accordingly, neither collateral securities received from borrowers nor the related obligations to borrowers are reported.

To the extent collateral received consists of cash, the lending agency may use or invest the cash in accordance with reinvestment guidelines approved by the Treasury Department. Either the participant or the borrower may terminate lending agreements on demand. Lending agreements are typically of very short duration, usually overnight. Therefore, the duration of lending agreements does not generally match the maturities of the investments made with cash collateral. The resulting interest rate risk is mitigated by the lending agent's ability to reallocate lending agreements among SLP participants.

The SLP requires that the lending agent indemnify the Treasury Department for all claims, liabilities, and costs resulting from the lending agent's negligence or intentional misconduct. During the fiscal year ended December 31, 2019, there were no failures by any borrower to return securities lent or pay distributions thereon. Also, there were no losses resulting from a lending agent or borrower default, and there were no Treasury Department restrictions on the amount of loans that could be made.

At December 31, 2019 and 2018 there was no credit risk to the borrowers because the fair value of collateral received was greater than the fair value of the securities lent, consistent with the lending agreements outstanding. The carrying amount and fair value (in thousands) of the securities lent was \$16,976 and \$22,957, respectively.

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

SWIF's investment securities owned at December 31, 2019 and 2018, were as follows (amounts in thousands):

<u>December 31, 2019</u>	<u>Book/Adjusted Carrying Value</u>	<u>Market Value</u>
<b><u>Bonds</u></b>		
Government	\$ 317,912	\$ 320,429
States, Territories, and Possessions	3,921	4,088
Political Subdivisions of States, Territories, and Possessions	2,796	3,308
Residential Mortgage Backed Securities	167,106	168,348
Commercial Mortgage Backed Securities	8,495	8,677
Industrial and Miscellaneous	710,211	732,769
<b><u>Total Bonds</u></b>	<b>\$ 1,210,441</b>	<b>\$ 1,237,619</b>
<b><u>Common Stocks</u></b>	<b>\$ 124,194</b>	<b>\$ 124,194</b>
<b><u>Short-Term Investments</u></b>	<b>\$ 54,428</b>	<b>\$ 54,428</b>
<u>December 31, 2018</u>	<u>Book/Adjusted Carrying Value</u>	<u>Market Value</u>
<b><u>Bonds</u></b>		
Government	\$ 296,082	\$ 292,187
States, Territories, and Possessions	17,963	18,076
Political Subdivisions of States, Territories, and Possessions	7,555	8,292
Revenue and Special Obligations	29,193	29,342
Residential Mortgage Backed Securities	145,022	141,496
Commercial Mortgage Backed Securities	12,668	12,668
Industrial and Miscellaneous	718,334	703,912
<b><u>Total Bonds</u></b>	<b>\$ 1,226,817</b>	<b>\$ 1,205,973</b>
<b><u>Common Stocks</u></b>	<b>\$ 95,291</b>	<b>\$ 95,291</b>
<b><u>Preferred Stocks</u></b>	<b>\$ 250</b>	<b>\$ 249</b>
<b><u>Short-Term Investments</u></b>	<b>\$ 49,768</b>	<b>\$ 49,768</b>

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE B – INVESTMENTS (Continued)**

In accordance with the Fiscal Code, cash balances of most Commonwealth funds, including SWIF, are pooled by the Treasury Department. SWIF's short-term investments were also pooled for the calendar years ended December 31, 2019 and 2018. Pertaining to marketable equity securities, December 31, 2019 showed a net unrealized capital gain of \$15,107 (in thousands), and December 31, 2018 showed a net unrealized capital loss of (\$10,991) (in thousands).

**NOTE C – COMPOSITION OF LOSS RESERVES AND INCURRED BUT NOT REPORTED (IBNR) LOSSES**

	<u>December 31, 2019</u> <u>(Amounts in Thousands)</u>		
	<u>Coal</u>	<u>Commercial</u>	<u>Total</u>
<b><u>Loss Reserves</u></b>			
Indemnity	\$ 14,123	\$ 233,300	\$ 247,423
Medical	3,223	103,927	107,150
Bulk	11,991	907,821	919,812
<b>Total Loss Reserves</b>	<u>\$ 29,337</u>	<u>\$ 1,245,048</u>	<u>\$ 1,274,385</u>
<b><u>IBNR Loss Reserves</u></b>	<u>\$ 289</u>	<u>\$ 49,806</u>	<u>\$ 50,095</u>
<b><u>Net Losses</u></b>			\$ 1,324,480
Add:			
Assumed Outstanding Loss Reserves (Including IBNR)			741
Less:			
Discount of Reserves			(232,735)
Recoverable Reinsurance (Including IBNR)			<u>(3,292)</u>
<b><u>Net Unpaid Losses</u></b>			<u>\$ 1,089,194</u>



**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE C – COMPOSITION OF LOSS RESERVES AND INCURRED BUT NOT REPORTED (IBNR) LOSSES**

	<u>December 31, 2018</u> (Amounts in Thousands)		
	<u>Coal</u>	<u>Commercial</u>	<u>Total</u>
<b><u>Loss Reserves</u></b>			
Indemnity	\$ 14,874	\$ 283,293	\$ 298,167
Medical	3,505	125,901	129,406
Bulk	13,054	939,133	952,187
<b>Total Loss Reserves</b>	<u>\$ 31,433</u>	<u>\$ 1,348,327</u>	<u>\$ 1,379,760</u>
<b><u>IBNR Loss Reserves</u></b>	<u>\$ 573</u>	<u>\$ 68,891</u>	<u>\$ 69,464</u>
<b><u>Net Losses</u></b>			\$ 1,449,224
Add:			
Assumed Outstanding Loss Reserves (Including IBNR)			975
Less:			
Discount of Reserves			(253,799)
Recoverable Reinsurance (Including IBNR)			<u>(6,310)</u>
<b><u>Net Unpaid Losses</u></b>			<u>\$ 1,190,090</u>

**NOTE D – PENSION AND OTHER POSTEMPLOYMENT BENEFITS**

**Pension**

**Plan Description:** To provide pension benefits for employees of state government and certain other organizations, the State Employees' Retirement System (SERS) administers a cost-sharing multiple-employer defined benefit retirement plan.

**Retirement Benefits:** Under the plan, for most employees hired prior to January 1, 2011, retirement benefits vest after 5 years of credited service. Generally, employees who retire at age 60 with three years of service, or with 35 years of service if under the age of 60, are entitled to a normal (unreduced) annual retirement benefit. The general annual benefit is 2 percent of a Class A member's highest three-year average salary multiplied by years of service. This annual benefit is 2.5 percent for Class AA members.

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**STATE WORKERS' INSURANCE FUND  
NOTES TO FINANCIAL STATEMENTS  
DECEMBER 31, 2019 and 2018**

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**NOTE D – PENSION AND OTHER POSTEMPLOYMENT BENEFITS (Continued)**

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Act 2010-120 (Act 120), which preserved all benefits in place for members, mandated a number of benefit reductions for new members effective January 1, 2011. The benefit reduction included a new class of membership that accrues benefits at 2 percent of their final average salary instead of the previous 2.5 percent. The new vesting period changed from five to ten years of credited service, and the option to withdraw lump sum accumulated employee contributions was eliminated. The new normal retirement age is 65 for most employees. Act 120 created a new A-3 class of service and an optional A-4 class for most employees that entered SERS membership for the first time on or after January 1, 2011. The general annual benefit for Class A-3 members is 2 percent of the member's highest three-year average salary times years of service while the Class A-4 benefit accrual rate is 2.5 percent.

**Contribution Requirements:** All member contribution rates are determined by Commonwealth law. The active plan member contribution rate is 6.25 percent of covered payroll for employees in Class AA; for Class A members, the contribution rate is 5 percent. The general membership contribution rate under Act 120 for A-3 and A-4 members is 6.25 percent and 9.3 percent of salary, respectively. The SERS Board has the authority to establish or amend periodic employer contributions at actuarially determined rates, expressed as a percentage of annual covered payroll.

Act 120 imposed annual rate increase collars on employer contributions until no longer needed. The fiscal year ended June 30, 2018, marked the first year the actuarially required employer contribution increase was lower than the collar established for the year of 4.5 percent. As a result, the rate caps are no longer in effect.

**Summary of Significant Accounting Policies:** The SERS financial statements are prepared on the accrual basis of accounting, whereby expenses are recorded when the liability is incurred, revenues are recorded in the accounting period in which they are earned and become measurable, and investment purchases and sales are recorded as of the related trade date. Member and employer contributions are recognized in the period in which contributions are due, and the employer has a legal requirement to provide contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

SERS issues stand-alone financial statements which are available at [www.sers.pa.gov](http://www.sers.pa.gov). Written requests for financial statements should be directed to the following address:

State Employees' Retirement System  
30 North Third Street, Suite 150  
Harrisburg, PA 17101-1716

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE D – PENSION AND OTHER POSTEMPLOYMENT BENEFITS (Continued)**

The SWIF's contributions (in thousands) for the fiscal years ended December 31, 2019 and 2018 in relation to the contractually required contributions are as follows:

<b>Year Ended December 31</b>	<b>Contractually Required Contributions</b>	<b>Actual Contributions</b>
2019	\$4,128	\$4,128
2018	\$4,300	\$4,300

Additional pertinent information regarding SERS, outside the scope of SWIF reporting, is published each year as part of the Commonwealth of Pennsylvania's Basic Financial Statements included in the Comprehensive Annual Financial Report.

**Other Postemployment Benefits**

**Plan Description:** The Commonwealth established and sponsors a Retired Employees Health Program (REHP) plan which provides postemployment benefits other than pensions (OPEB). This plan is administered by the Pennsylvania Employee Benefits Trust Fund (PEBTF), which acts as a third-party administrator and administers the REHP under an administrative agreement with the Commonwealth. The plan is a single employer defined benefit OPEB plan. The SWIF participates in the REHP, which provides a variety of healthcare benefits to eligible retirees. The REHP is provided as part of collective bargaining agreements with most Commonwealth labor unions. All policy decisions and types and levels of benefits for the REHP fall under the purview of the Commonwealth's Executive Board and Secretary of Administration. REHP does not have a governing board. The REHP plan does not issue a stand-alone financial report, nor is it included in the financial statements of a public employee retirement system.

**Benefits Provided:** Benefit provisions included in the REHP plans are established and may be amended by the establishing sponsor. The REHP plan provides postemployment healthcare benefits to eligible employees. Employees who retire from the Commonwealth and meet one of the following eligibility criteria are eligible to receive REHP benefits:

- 25 or more years of service;
- 20 or more years of service and superannuation age – age 50 for Park Rangers, Capitol Police, and certain enforcement officers, or age 60 for all other employees (age 55 or 65 for employees subject to Act 120 of 2010);
- Disability retirement – requires five years of service (no service requirements for enforcement officers).

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE D – PENSION AND OTHER POSTEMPLOYMENT BENEFITS (Continued)**

*Contribution Requirements:* REHP contribution requirements are contractually required and established by the Commonwealth's Office of Administration and the Office of the Budget. The contribution rates are established as a set amount per current active REHP eligible employee per biweekly pay in order to fund the REHP plan. During the period January 1, 2019 to June 30, 2019, SWIF contributed \$300 for each active employee paid and reported as part of biweekly payroll expenses for its employees. During the period July 1, 2019 to December 31, 2019, SWIF contributed \$230 for each active employee paid and reported as part of biweekly payroll expenses for its employees.

The SWIF's contributions (in thousands) for the fiscal years ended December 31, 2019 and 2018 in relation to the contractually required contributions are as follows:

<b>Year Ended December 31</b>	<b>Contractually Required Contributions</b>	<b>Actual Contributions</b>
2019	\$1,591	\$1,591
2018	\$1,578	\$1,578

Additional pertinent information on the REHP, outside the scope of SWIF reporting, including overall actuarial liabilities and assumptions related to the Commonwealth, is published each year as part of the Commonwealth of Pennsylvania's Basic Financial Statements included in the Comprehensive Annual Financial Report.

**NOTE E – INSURANCE LOSS LIABILITY**

The reported insurance loss liability is primarily based on historical claims experience. One of the assumptions used to determine the reported liability amount includes using a discount rate of 2.00 percent at December 31, 2019 and December 31, 2018. There is uncertainty as to whether the reported liability will be supported by future claims experience, including payments; this uncertainty must be considered when evaluating the reported insurance loss liability. Like other private insurance carriers authorized to transact and provide workers' compensation insurance in the Commonwealth, SWIF is required to pay assessments into the Pennsylvania Workers' Compensation Security Fund, a separate special revenue fund established by the Pennsylvania Department of Insurance to authorize and account for the payment of workers' compensation claims to individuals who are insured by insurance carriers that become insolvent.

**STATE WORKERS' INSURANCE FUND**  
**NOTES TO FINANCIAL STATEMENTS**  
**DECEMBER 31, 2019 and 2018**

**NOTE E – INSURANCE LOSS LIABILITY (Continued)**

For the two calendar years ended December 31, 2019 and 2018, the following summary provides information on prior year reported insurance loss liability, incurred claims and payments, and current year reported insurance loss liability (amounts in thousands). In 2019, there was an adjustment made to the prior year liability. The prior year liability was increased by \$79,280 due to an error discovered in some payments made on claims which were coded as chargeable (decreasing the reserve), and should have been coded as non-chargeable (increasing the loss adjustment expense).

<u>Year Ended December 31</u>	<u>Prior Year Liability</u>	<u>Incurred Claims</u>		<u>Payments</u>		<u>Current Year Liability</u>
		<u>Current</u>	<u>Prior</u>	<u>Current</u>	<u>Prior</u>	
2019	\$1,423,809	\$152,707	(60,785)	\$33,497	\$146,861	\$1,335,373
2018	\$1,497,470	\$191,500	(76,754)	\$35,579	\$152,907	\$1,423,730

**NOTE F – SURPLUS AS REGARDS POLICYHOLDERS**

By statute, the State Workers' Insurance Board is required to set aside a percentage of premiums to sufficiently maintain the surplus to cover the catastrophe hazard of all the subscribers in the fund and to guarantee the solvency of the fund. The statute also provides that the board shall have the power to reinsure any risk which they may deem necessary. Accordingly, with the assistance of JLT Re Inc., SWIF entered into contracts with several reinsurers to provide catastrophe coverage to its policyholders. The reinsurance is intended to protect and enhance SWIF's capital base.

As a result of this reinsurance program, SWIF's catastrophe reserve is not required as a set aside of the fund's unassigned surplus.



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EUGENE A. DePASQUALE  
AUDITOR GENERAL

**Report on Internal Control Over Financial Reporting and on Compliance and Other  
Matters Based on an Audit of Financial Statements Performed in Accordance with  
*Government Auditing Standards***

**Independent Auditor's Report**

The Honorable Tom Wolf  
Governor  
Commonwealth of Pennsylvania  
Harrisburg, PA 17120

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the Statements of Admitted Assets, Liabilities and Surplus-statutory basis of the State Workers' Insurance Fund (SWIF), the related Statements of Operations and Changes in Surplus-statutory basis and the Statements of Cash Flows-statutory basis as of and for the years ended December 31, 2019, and December 31, 2018, and the related notes to the financial statements, and have issued our report thereon dated December 1, 2020.

**Internal Control Over Financial Reporting**

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

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

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

### **Compliance and Other Matters**

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

### **Purpose of this Report**

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

December 1, 2020



Eugene A. DePasquale  
Auditor General

**COMMONWEALTH OF PENNSYLVANIA  
DEPARTMENT OF LABOR AND INDUSTRY  
STATE WORKERS' INSURANCE FUND  
DISTRIBUTION LIST  
DECEMBER 31, 2019 AND 2018**

This report was initially distributed to the following:

Commonwealth of Pennsylvania

**The Honorable Tom Wolf**  
Governor

**The Honorable Joseph Torsella**  
State Treasurer

**The Honorable Jen Swails**  
Secretary of the Budget

**The Honorable Lucas Miller**  
Inspector General

**The Honorable Jessica Altman**  
Insurance Commissioner

**The Honorable W. Gerard Oleksiak**  
Secretary  
Department of Labor and Industry

**Mr. Scott Weiant**  
Deputy Secretary for Compensation  
and Insurance  
Department of Labor and Industry

**Mr. Andrew Thomas**  
Director  
State Workers' Insurance Fund

**Mr. Joseph Dorbad**  
Assistant Director  
State Workers' Insurance Fund

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