

Washington State Auditor's Office
Financial Statements Audit Report

Washington Counties Risk Pool
Thurston County

Audit Period
October 1, 2003 through September 30, 2004

Report No. 68485

Issue Date
May 6, 2005



Washington _____
State Auditor
_____ Brian Sonntag



**Washington State Auditor
Brian Sonntag**

May 6, 2005

Board of Directors
Washington Counties Risk Pool
Tumwater, Washington

Report on Financial Statements

Please find attached our report on the Washington Counties Risk Pool's financial statements.

We are issuing this report in order to provide information on the Pool's financial condition.

In addition to this work, we look at other areas of our audit clients' operations for compliance with state laws and regulations. The results of that audit will be included in a separately issued accountability report.

Sincerely,

BRIAN SONNTAG, CGFM
STATE AUDITOR

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Thurston County
October 1, 2003 through September 30, 2004**

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Independent Auditor's Report on Compliance and Internal Control over Financial Reporting in Accordance with Government Auditing Standards

Washington Counties Risk Pool Thurston County October 1, 2003 through September 30, 2004

Board of Directors
Washington Counties Risk Pool
Tumwater, Washington

We have audited the basic financial statements of the Washington Counties Risk Pool, Thurston County, Washington, as of and for the year ended September 30, 2004, and have issued our report thereon dated April 11, 2005. During the year ended September 30, 2004, the Pool has implemented Governmental Accounting Standards Board Statement 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, and its amendments.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to the financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

COMPLIANCE

As part of obtaining reasonable assurance about whether the Pool's financial statements are free of material misstatement, we performed tests of the Pool's compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, the objective of our audit of the financial statements was not to provide an opinion on overall compliance with these provisions. Accordingly, we do not express such an opinion.

The results of our tests disclosed no instances of material noncompliance that are required to be reported herein under *Government Auditing Standards*.

INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit, we considered the Pool's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting.

Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended for the information of management and the Board of Directors. However, this report is a matter of public record and its distribution is not limited. It also serves to disseminate information to the public as a reporting tool to help citizens assess government operations.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

BRIAN SONNTAG, CGFM
STATE AUDITOR

April 11, 2005

Independent Auditor's Report on Financial Statements

Washington Counties Risk Pool Thurston County October 1, 2003 through September 30, 2004

Board of Directors
Washington Counties Risk Pool
Tumwater, Washington

We have audited the accompanying basic financial statements of the Washington Counties Risk Pool, Thurston County, Washington, as of and for the year ended September 30 2004, as listed on page 5. These financial statements are the responsibility of the Pool's management. 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Washington Counties Risk Pool, as of September 30, 2004, and the changes in financial position and cash flows, where applicable, thereof, for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, during the year ended September 30, 2004, the Pool has implemented Governmental Accounting Standards Board Statement 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*, and its amendments.

In accordance with *Government Auditing Standards*, we have also issued our report on our consideration of the Pool's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management discussion and analysis on pages 6 through 8 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquires of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

The Claims Development Information is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods

of measurement and presentation of supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, appearing to read "Brian Sonntag". The signature is fluid and cursive, with the first name "Brian" and last name "Sonntag" clearly distinguishable.

BRIAN SONNTAG, CGFM
STATE AUDITOR

April 11, 2005

Financial Section

**Washington Counties Risk Pool
Thurston County
October 1, 2003 through September 30, 2004**

REQUIRED SUPPLEMENTAL INFORMATION

Management Discussion and Analysis – 2004

BASIC FINANCIAL STATEMENTS

Statement of Net Assets – 2004

Statement of Revenues, Expenses and Changes in Fund Net Assets – 2004

Statement of Cash Flows – 2004

Notes to Financial Statements – 2004

SUPPLEMENTAL INFORMATION

RSI – Ten Year Claims Development Information – 2004

WASHINGTON COUNTIES RISK POOL
MANAGEMENT DISCUSSION AND ANALYSIS
For the Fiscal Year October 1, 2003 through September 30, 2004

The management of the Washington Counties Risk Pool (“Pool”) offers the readers of the Pool’s financial statements this narrative as an overview and analysis of the Pool’s financial activities for its fiscal year that ended September 30, 2004, the first year for which GASB 34 statements were prepared. This discussion and analysis is intended to serve only as an introduction to the Washington Counties Risk Pool’s financial statements, which are comprised of two components: 1) the basic financial statements, and 2) the notes to the financial statements. To more fully understand the financial position of the Pool, this narrative must be viewed in context with information contained in the Pool’s financial statements and the accompanying notes.

The Pool’s function is to provide casualty (liability) insurance to its member counties. Its primary source of revenue is the fees/assessments paid by the Pool’s member counties. The major Pool expenses are payments of claims and judgments, including associated fees, and payments for coverage from reinsurance and excess insurance carriers.

The financial statements pertain solely to the Washington Counties Risk Pool which has no other component units for which it is financially accountable.

Financial Statements

The *Statement of Net Assets* presents information on all of the Pool’s assets and liabilities. The difference between the two is reported as *Net Assets*.

The *Statement of Revenues, Expenses and Changes in Net Assets* presents information concerning how the Pool’s net assets changed during the fiscal year. All changes in net assets are reported when the underlying event giving rise to the change actually occurs, regardless of the timing of related cash flows.

Notes to the Financial Statements

The *Notes to the Financial Statements* provide additional information essential to fully understanding the data provided in the Pool’s financial statements.

COMPARATIVE FINANCIAL INFORMATION – NET ASSETS:

	9/30/04	9/30/03
Current Assets	\$19,974,494	\$ 8,576,777
Non Current (Capital) Assets	558,386	593,395
Total Assets	\$20,532,880	\$ 9,170,172
Current Liabilities	\$21,782,813	\$10,924,174
Restricted Net Assets – Resolution 93-01	(\$ 1,249,933)	(\$ 1,754,002)
Total Liabilities and Net Assets	\$20,532,880	\$ 9,170,172

CHANGES IN THE POOL'S NET ASSETS:

	2004 ACTIVITES
<i>Operating Revenues</i>	
Member Assessments	\$ 9,544,842
Retro Assessments – Prior Years	2,100,000
Program Revenues	42
Total Operating Revenues	\$11,644,844
<i>Non Operating Revenues</i>	
Interest Income	74,129
Gain (Loss) on Capital Asset Disposition	2,700
Total Non-Operating Revenues	\$ 76,829
Total Revenues	\$11,721,673
<i>Operating Expenses</i>	
Claims Paid on Current Year Reserve	\$ 1,900,000
Adjustment to Prior Year's Claim Reserve	1,150,769
Unallocated Loss Adjustment Expense	93,552
Reinsurance Premiums	7,093,590
Claims Administration & Loss Control	621,658
General and Administrative	358,075
Total Operating Expenses	\$11,217,644
CHANGES IN NET ASSETS	\$ 504,069
Beginning Net Assets (October 1, 2003)	(\$1,754,002)
Ending Net Assets (September 30, 2004)	(\$1,249,933)

OVERALL FINANCIAL POSITION:

It is our opinion that the Pool's overall financial position improved during the fiscal year that began October 1, 2003 and ran through September 30, 2004. For example,

- Net assets increased by \$504,069;
- Operating income increased by \$427,240; and
- Operating revenues increased 13.5%, having risen from \$10.25 million (prior fiscal year) to \$11.64 million.

Moreover, two events that will significantly improve the Pool's financial position occurred subsequent to September 30, 2004 and thus were NOT reflected in the financial statements. They are:

- The actuarial reserve review was updated and lowered the reserve estimate \$122,000. Since the update was not presented until December 8, 2004, the reserve reduction will result in a corresponding \$122,000 increase in the Pool's net assets after the updated

review has been formally accepted by the Pool's directors when its board meets in April 2005.

- The Pool received \$2,000,000 December 23, 2004 as final settlement with an excess insurance carrier for that insurer's share of a class action judgment paid by the Pool in December 2002. The payment constitutes a substantial, but only partial recovery of the amounts written off as bad debt expenses for presentation of the Pool's 2002-03 financial statements. (NOTE: Negotiations with a reinsurance company for its share continue and are showing promise. This would result in full recovery of the earlier write off and negate the \$2.1 million retroactive assessment approved during the 2003-4 fiscal year.)

BUDGETARY VARIATIONS:

There were no significant variations from the budget adopted by the Pool's Board of Directors during the fiscal year ending September 30, 2004.

CAPITAL ASSET AND DEBT ACTIVITIES:

Capital Assets

The Pool's investment in capital assets as of September 30, 2004 was \$558,386 (net of accumulated depreciation) which includes real and personal property, i.e., office building with computers and office equipment and furniture, automobiles. One of the building's HVAC units was replaced during the 2003-4 fiscal year. Replacement of another unit is expected to occur in the 2005-6 fiscal year. For additional capital asset information, see Note 7 in the Notes to Financial Statements.

Long-Term Debt

The Washington Counties Risk Pool had no long-term debt as of September 30, 2004.

REQUEST FOR INFORMATION:

This financial report is designed to provide a general overview of the Washington Counties Risk Pool for all those with an interest in its finances. Questions concerning the information provided in this discussion and analysis and the Pool's financial report, or requests for additional information, should be addressed to:

WASHINGTON COUNTIES RISK POOL
205 Clark Place S.E.
Tumwater, WA 98501-4062
360/586-7447

**WASHINGTON COUNTIES RISK POOL
STATEMENT OF NET ASSETS
As of September 30, 2004**

ASSETS:

	2004
CURRENT ASSETS:	
Cash and Cash Equivalents	\$ 10,897,279
Investments	300,000
Prepaid Expenses	0
Member Deductible & Reinsurance Receivables	1,966,318
Member Assessment Receivable	2,460,710
Retro Assessment Premium Receivable	4,350,187
TOTAL CURRENT ASSETS	19,974,494
NONCURRENT ASSETS:	
Capital Assets (Net of Accumulated Depreciation)	558,386
TOTAL ASSETS	\$ 20,532,880

LIABILITIES:

CURRENT LIABILITIES:	
Claim Reserves	\$ 11,349,473
Unallocated Loss Adjustment Expenses Reserve	643,552
Accounts Payable	35,990
Accrued Liabilities	60,820
Unearned Revenue - Members Assessments	9,692,978
TOTAL CURRENT LIABILITIES	\$ 21,782,813
TOTAL RESTRICTED NET ASSETS - Resolution 93-01	(1,249,933)
TOTAL NET ASSETS AND LIABILITIES	\$ 20,532,880

The Accompanying Notes Are An Integral Part of This Statement.

**WASHINGTON COUNTIES RISK POOL
STATEMENT OF REVENUES AND EXPENSES
AND CHANGES IN FUND NET ASSETS
For the Fiscal Year Ended September 30, 2004**

OPERATING REVENUES:	<u>2004</u>
Member Assessments	\$ 9,544,842
Retro Assessment for Prior Years	2,100,000
Program Revenues	42
Total Operating Revenues	\$ 11,644,884
OPERATING EXPENSES:	
Claims Paid on Current Year Reserve	\$ 1,900,000
Adjustment fo Prior Year's Claims Reserves	1,150,769
Unallocated Loss Adjustment Expense	93,552
Reinsurance Premiums	7,093,590
Claims Administration & Loss Control	621,658
General and Administrative	<u>358,075</u>
Total Operating Expenses	\$ 11,217,644
Operating Income	<u>\$ 427,240</u>
NON OPERATING REVENUES (EXPENSES)	
Interest Income	\$ 74,129
Gains (Losses) on Capital Asset Disposition	2,700
Total Nonoperating Revenues (Expenses)	\$ 76,829
CHANGES IN NET ASSETS	\$ 504,069
TOTAL NET ASSETS, October 1, 2003	\$ <u>(1,754,002)</u>
TOTAL NET ASSETS, October 31, 2004	<u><u>\$ (1,249,933)</u></u>

The Accompanying Notes Are An Integral Part of This Statement

**WASHINGTON COUNTIES RISK POOL
STATEMENT OF CASH FLOW
For the Fiscal Year Ended September 30, 2004**

	<u>2004</u>
CASH FLOWS FROM OPERATING ACTIVITIES:	
Cash received from members	\$ 16,007,498
Cash payments for goods and services	(9,552,834)
Cash payments to employees for services	(417,483)
Net Cash Provided (Used) by Operating Activities	<u>\$ 6,037,181</u>
CASH FROM CAPITAL ACTIVITIES:	
Purchase of Office Equipment	\$ (29,274)
Sale of Equipment	2,700
Net Cash Provided (Used) by Capital Activities	<u>(26,574)</u>
CASH FLOW FROM INVESTING ACTIVITIES:	
Proceeds from sales of investments	\$ 500,000
Interest received	74,129
Net Cash Provided (Used) by Investing Activities	<u>\$ 574,129</u>
Increase (Decrease) in Cash and Cash Equivalents	\$ 6,584,736
Cash and Cash Equivalents - Beginning of the Year	4,312,543
Cash and Cash Equivalents - End of the Year	<u><u>10,897,279</u></u>

**RECONCILIATION OF OPERATING INCOME TO NET CASH
PROVIDED (USED) BY OPERATING ACTIVITIES**

Operating Income	427,240
Adjustments to reconcile net income to net cash:	
Cash provided by operating activities:	
Depreciation expense	64,282
Decrease (Increase) in Accounts Receivable	(5,330,364)
Decrease (Increase) in Prepaid Expenses	17,384
Increase (Decrease) in Claims Reserves	1,165,432
Increase (Decrease) in Unallocated Loss Adjustment Expen:	93,552
Increase (Decrease) in Unearned Revenue	9,692,978
Increase (Decrease) in Accounts Payable	(75,341)
Increase (Decrease) in Accrued Liabilities	(17,982)
Net Cash Provided for Operating Activities	<u>\$ 6,037,181</u>

The Accompanying Notes Are An Integral Part of This Statement.

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

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

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies of the Washington Counties Risk Pool conform to generally accepted accounting principles ("GAAP"). The following is a summary of the more significant policies:

a. Reporting Entity

The Washington Counties Risk Pool operates under the laws of the State of Washington applicable to joint self-insurance risk pools. It was formed by an Interlocal Agreement on August 18, 1988 pursuant to Chapters 48.62 and 39.34 RCW, and was organized to provide member counties with joint programs including joint self-insurance, joint purchasing of insurance, and joint contracting for hiring of personnel to provide administrative services, claims handling and risk management.

Joint self-insurance coverage is provided by the risk pool to member counties for bodily injury, personal injury, property damage, errors and omissions, and advertising injury. The risk pool provides its membership joint self-insurance coverage of \$10,000,000, subject to a member's individual deductible election, along with "following form" excess insurance coverage of \$10,000,000. Members elect a deductible amount of \$10,000, \$25,000, \$50,000, \$100,000, \$250,000 or \$500,000 per occurrence. There are no annual aggregate limits to the payments the risk pool can make for any one county member or all county members combined.

b. Basis of Accounting and Presentation

The accounting records of the risk pool are maintained in accordance with methods prescribed by the State Auditor's Office under the authority of Chapter 43.09 RCW. The risk pool also follows the accounting standards established by the Governmental Accounting Standards Board (GASB) Statement 10, *Accounting And Financial Reporting For Risk Financing And Related Insurance Issues*, as amended by GASB Statement 30, *Risk Financing Omnibus*, GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Funds*, and GASB Statement 33, *Accounting and Financial Reporting for Nonexchange Transactions*. In 1999 GASB issued Statement 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. The presented financial statements (including notes) reflect this and consecutive statements.

The risk pool uses the full-accrual basis of accounting where revenues are recognized when earned and expenses are recognized when incurred. Capital asset purchases are capitalized and long-term liabilities are accounted for within the financial statements.

The principal operating revenues of the pool are member assessments, while operating expenses include claims paid from current year reserves and adjustments to prior year's reserves, reinsurance premiums, and administrative expenses. Unbilled receivables are recorded at year end.

c. Cash and Cash Equivalents

For the purposes of the Statement of Cash Flows, the risk pool considers all highly liquid investments with maturity of three months or less when purchased to be cash equivalents.

d. Capital Assets and Depreciation

See Note 7

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

e. Receivables

Management decides if any accounts are deemed uncollectible. Uncollectible accounts are charged to expense in the period they are deemed uncollectible.

f. Investments

See Note 2.

g. Compensated Absences

Compensated absences are absences for which the employees will be paid, such as vacation and sick leave. The risk pool records unpaid leave for compensated absences as an expense and liability when incurred.

Vacation (Annual leave) may be accumulated up to 30 days and is payable upon resignation, retirement, or death. An employee with more than sixty days sick leave accrued may convert the days earned in the previous year (less any sick leave days used in the previous year) to annual leave days at the rate of four days of sick leave for one day of annual leave. Sick leave may accumulate up to 130 days. Sick leave does not vest until death or retirement, and the accrued liability is booked at ½ the amounts earned.

h. Unpaid Claim Liabilities

The risk pool establishes claim liabilities based on estimates of the ultimate cost of claims, including future claim adjustment expenses, for claims/lawsuits that have been reported but are not settled, and for claims that have been incurred but are not yet reported. The length of time for which such costs must be estimated varies depending on the coverage type involved. Estimated amounts of salvage and subrogation and reinsurance recoverable on unpaid claims are deducted from the liability for unpaid claims. Because actual claims costs depend on such complex factors as inflation, changes in doctrines of legal liability, and damage awards, the process used in computing claim liabilities does not necessarily result in an exact amount, particularly for coverages such as general liability. Claim liabilities are recomputed periodically using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claim liabilities are charged or credited to expense in the periods in which they are made.

i. Member Assessments and Unearned Member Assessments

Member assessments are collected in advance and recognized as revenue in the period for which insurance protection is provided. On the balance sheet, member assessments receivables were billed September 1st with up to the amount equivalent to 105% of the prior year's assessment being due by September 30th, and any remaining assessment due by January 31st. The assessments calculated are based on the members' worker hours and licensed vehicle counts.

j. Claim Reserves

Claims/Lawsuits are charged to income as incurred. Claim reserves represent the accumulation of estimates for reported, unpaid claims plus a provision for claims incurred but not reported (IBNR). These estimates are continually reviewed and updated, and any resulting adjustments are reflected in current earnings.

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

k. Unallocated Loss Adjustment Expense Reserve

The reserve for unallocated loss adjustment expenses (ULAE) represents the estimated cost to be incurred with respect to the settlement of both claims in process and those claims recognized as incurred but not reported (IBNR). Management estimates this liability at the end of each year based upon computations provided by the casualty actuary. The change in this liability each year is reflected in current earnings.

l. Exemption From Federal And State Taxes

Pursuant to revenue ruling number 90-74, income of municipal risk pools is excluded from gross income under IRC Section 115(1). Chapter 48.62 RCW exempts the risk pool from insurance premium taxes, and from business and occupation taxes imposed pursuant to Chapter 82.04 RCW.

NOTE 2 - DEPOSITS AND INVESTMENTS

a. Deposit

The risk pool's book values balances do not differ materially from the bank balance of deposits.

The risk pool's deposits and certificates of deposit are entirely covered by federal depository insurance (FDIC) or by collateral held in a multiple financial institution collateral pool administered by the Washington Public Deposit Protection Commission (PDPC).

b. Investments

As of September 30, 2004, the risk pool had the following investments:

	<u>Value</u>
U.S. Government and Agency Securities:	\$ 300,000
State Treasurer's Investment Pool:	\$ <u>10,006,662</u>
Total Investments:	\$ <u>10,306,662</u>

All temporary investments are stated at cost plus accrued interest approximating market. Other property and investments are shown on the balance sheet at cost, net of amortized premium or discount. Management intends to hold securities until maturity.

In accordance with GAAP applicable to regulated industries, reductions in market value are not reflected in the financial statements. Other gains or losses on investments sold or exchanged are recognized at the time the transactions are completed. In conformance with GAAP, the Pool's investments are recorded at market value, if material.

NOTE 3 - JOINT SELF-INSURED RETENTION

The risk pool retains responsibility for the payment of claims within specified self-insured retention limits prior to the application of coverage provided by its excess insurance contracts.

Historically, the risk pool and its member counties assumed liability for the first \$1 million of each occurrence, subject to the member county's elected deductible amount, for the two-month period ending November 30, 1988. Then with the purchase of excess insurance on December 1, 1988, the risk pool's assumed liability was reduced to \$500,000 per occurrence. And starting in fiscal year 1998, the risk pool's retention limit was lowered further to \$100,000 for liability claims.

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

Through prefunded member assessments collected at the beginning of each policy year, the risk pool committed assets for the years ended September 30, 2004 and 2003, of \$1,442,149 and \$1,617,411 respectively, specifically for the purpose of funding its self-insured retentions for those two years.

NOTE 4 - REINSURANCE CONTRACTS

The risk pool maintains both reinsurance and “following form” excess insurance contracts which provide coverage over the risk pool’s joint self-insured retention limits. The risk pool purchased reinsurance and excess insurance policies bring the total liability limit for the county members to \$20 million per occurrence. The limits provided are distributed as follows:

Member/Pool Self-Insured(*)	Reinsurance(*)	Excess	Total
\$100,000	\$9,900,000	\$10,000,000	\$20,000,000

* County members annually select deductible amounts of \$10,000, \$25,000, \$50,000, \$100,000, \$250,000 or \$500,000. The Risk Pool self-insures the balance between member deductibles and \$10,000,000 with reinsurance available to offset losses exceeding the greater of the member deductibles and \$100,000.

NOTE 5 - MEMBER'S SUPPLEMENTAL ASSESSMENTS AND CREDITS

RCW 48.62.141 and the Interlocal Agreement provide for the contingent liability of participants in the program if assets of the program are insufficient to cover the program's liabilities. Deficits of the risk pool are financed through retroactive assessments to member counties.

In 1999 the risk pool projected a funding shortfall of \$6.5 million for the 1993-1997 loss years. In order to cover this deficiency, the risk pool adopted a reassessment plan that was to require additional contributions from each member who participated in those years. The reassessment was to be billed to and collected from members over the course of ten years starting in October 1999. In addition, the plan required departing members to pay their reassessment for these years as if the county had remained a member of the risk pool. Annual reassessments were billed and collected in 1999, 2000, 2001 and 2002. Due to adverse claims development, the funding shortfall for the five policy years (1993-1998) increased to \$11.9 million by the end of 2002.

On the other hand, all claims and lawsuits from the first five years, 1988 through 1993, were concluded and closed by the end of 2002. The risk pool board voted to fix surplus earnings of \$4.3 million from the first five policy years as of October 1, 2002, calculate credits according to the proportionate amounts that qualifying counties paid into the risk pool loss fund for each of the separate policy years, and transfer them as credits to qualifying current members (those that did not have a subsequent break in risk pool membership) to partially fund the deficits of the next five years, 1993 through 1998.

In 2003 the risk pool board revised the residual reassessments to \$7.6 million (after the application of surplus credits), and approved the reassessment formula to be the proportionate amounts that a member county paid into the Pool loss fund, with each separate policy year calculated separately. The revised reassessments were to be collected in six equal annual installments, with the first collection billed in April 2003.

Members were offered an advance payment discount using a 2% compounded discount rate for each additional year paid. Thirteen members paid the full reassessment, as discounted, two members paid several annual installments with a partial discount, and ten members paid one annual installment. The twelve members with reassessment balances were billed and paid an additional installment during 2004. The deficiency balance remaining is approximately \$2.2 million.

And, to address the strain resulting from certain excess insurance and reinsurance companies having delayed reimbursement to the Risk Pool of their contractual shares of the Vicwood Meridian class action settlement, the Risk Pool board in July 2004 approved an additional retroactive assessment of \$2.1 million for the uncollected insurance

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

reimbursements and legal expenses. This reassessment will be billed in equal payments starting at a time and in amounts set by the Pool's Executive Committee if/when the Committee determines that funds are needed to address the Pool's near- or short-term financial obligations and/or after the Committee has determined that reasonable efforts to collect the amounts have been made without complete success. Any actual reassessment forthcoming will be distributed according to the proportional amounts paid by each participant county for the \$4.5 million excess of \$0.5 million layer of excess insurance and/or reinsurance for the applicable policy year(s).

NOTE 6 - UNPAID CLAIM LIABILITIES

As discussed in Note 2, the risk pool establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities for the risk pool during the past two years:

	<u>2004</u>	<u>2003</u>
Unpaid Claims and Claim Adjustment Expenses at Beginning of Year	\$10,184,042	\$12,380,643
Incurred Claims and Claim Adjustment Expenses:		
Provisions for Insured Events of the Current Year	1,442,149	1,617,411
Increase (Decrease) in Provision for Insured Events of Prior Years	1,608,619	41,164
Total Incurred Claims and Claim Adjustment Expenses	\$13,234,810	\$14,039,218
Payments:		
Claims and Claim Adjustment Expenses Attributable to Insured Events of the Current Year	\$ 68,432	\$ 5,092
Claims and Claim Adjustment Expenses Attributable to Insured Events of Prior Years	<u>1,816,904</u>	<u>3,850,084</u>
Total Payments	<u>\$ 1,885,336</u>	<u>\$ 3,855,176</u>
Total Unpaid Claims and Claim Adjustment Expenses at the End of Year	<u>\$ 11,349,474</u>	<u>\$10,184,042</u>

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

NOTE 7 – CAPITAL ASSETS

Capital assets are defined by the risk pool as assets with an initial, individual cost of \$2,500 and an estimated useful life in excess of one year. Capital assets are recorded at historical cost. Maintenance and repairs are expensed as incurred. When equipment is retired or otherwise disposed of, cost and accumulated depreciation are removed from the accounts, and any resulting gain or loss is reflected as other income. Depreciation is computed on the straight-line method over the estimated useful lives of the equipment (5 years) and building (30 years).

Capital assets activity for the year ended September 30, 2004 was as follows:

	Beginning Balance <u>9/30/03</u>	Increase (Decrease)	Ending Balance <u>9/30/04</u>
Capital Assets Not Being Depreciated:			
Land	\$ 99,404	\$	\$ 99,404
Capital Assets Being Depreciated:			
Building	460,000		460,000
Office Furnishings and Equipment	<u>325,212</u>	16,026	<u>341,238</u>
Total Capital Assets being Depreciated	785,212	16,026	801,238
Less Accumulated Depreciation for:			
Building	130,333	15,334	145,667
Office Furnishings and Equipment	<u>160,888</u>	35,701	<u>196,589</u>
Total Accumulated Depreciation	<u>291,221</u>	51,035	<u>342,256</u>
Total Capital Assets Being Depreciated (net)	<u>\$493,991</u>	\$35,009	<u>\$458,982</u>
TOTAL CAPITAL ASSETS NET	<u>\$593,395</u>	\$ 35,009	<u>\$558,386</u>

NOTE 8 - PENSION PLANS

a. Public Employees' Retirement System (PERS) Plans 1, 2, and 3

Substantially all Washington Counties Risk Pool full-time and qualifying part-time employees participate in one of the following statewide retirement systems administered by the Washington State Department of Retirement Systems, under cost-sharing multiple-employer public employee defined benefit and defined contribution retirement plans. The Department of Retirement Systems (DRS), a department within the primary government of the State of Washington, issues a publicly available comprehensive annual financial report (CAFR) that includes financial statements and required supplementary information for each plan. The DRS CAFR may be obtained by writing to: Department of Retirement Systems, Communications Unit, P.O. Box 48380, Olympia, WA 98504-8380. The following disclosures are made pursuant to GASB Statement No. 27, *Accounting for Pensions by State and Local Government Employers*.

Plan Description

PERS is a cost-sharing multiple-employer retirement system comprised of three separate plans for membership purposes: Plans 1 and 2 are defined benefit plans and Plan 3 is a combination defined benefit/defined contribution plan. Membership in the system includes: elected officials; state employees; employees of the Supreme, Appeals, and Superior courts (other than judges currently in a judicial retirement system); employees of legislative committees; community and technical colleges, college and university employees (not in national higher education retirement programs); judges of district and municipal courts; and employees of local governments. PERS participants who joined the system by September 30, 1977, are Plan 1 members. Those who joined on or after October 1, 1977 and by either, February 28, 2002 for state and higher education employees, or August 31, 2002 for local government employees, are Plan 2 members unless they exercise an option to transfer their membership to

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

Plan 3. PERS participants joining the system on or after March 1, 2002 for state and higher education employees, or September 1, 2002 for local government employees have the irrevocable option of choosing membership in either PERS Plan 2 or PERS Plan 3. The option must be exercised within 90 days of employment. An employee is reported in Plan 2 until a choice is made. Employees who fail to choose within 90 days default to PERS Plan 3. PERS defined benefit retirement benefits are financed from a combination of investment earnings and employer and employee contributions. PERS retirement benefit provisions are established in state statute and may be amended only by the State Legislature.

Plan 1 retirement benefits are vested after an employee completes five years of eligible service. Plan 1 members are eligible for retirement at any age after 30 years of service, or at the age of 60 with five years of service, or at the age of 55 with 25 years of service. The annual pension is 2 percent of the average final compensation per year of service, capped at 60 percent. The average final compensation is based on the greatest compensation during any 24 eligible consecutive compensation months. If qualified, after reaching the age of 66 a cost-of-living allowance is granted based on years of service credit and is capped at 3 percent annually.

Plan 2 retirement benefits are vested after an employee completes five years of eligible service. Plan 2 members may retire at the age of 65 with five years of service, or at the age of 55 with 20 years of service, with an allowance of 2 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 2 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and a cost-of-living allowance is granted (indexed to the Seattle Consumer Price Index), capped at 3 percent annually.

Plan 3 has a dual benefit structure. Employer contributions finance a defined benefit component, and member contributions finance a defined contribution component. The defined benefit portion provides a benefit calculated at 1 percent of the average final compensation per year of service. The average final compensation is based on the greatest compensation during any eligible consecutive 60-month period. Plan 3 members become eligible for retirement if they have: at least ten years of service; or five years including twelve months that were earned after age 54; or five service credit years earned in PERS Plan 2 prior to June 1, 2003. Plan 3 retirements prior to the age of 65 receive reduced benefits. If retirement is at age 55 or older with at least 30 years of service, a 3 percent per year reduction applies; otherwise an actuarial reduction will apply. There is no cap on years of service credit; and Plan 3 provides the same cost-of-living allowance as Plan 2. The defined contribution portion can be distributed in accordance with an option selected by the member, either as a lump sum or pursuant to other options authorized by the Employee Retirement Benefits Board.

There are 1,167 participating employers in PERS. Membership in PERS consisted of the following as of the latest actuarial valuation date for the plans of September 30, 2002:

Retirees and Beneficiaries Receiving Benefits	63,756
Terminated Plan Members Entitled to But Not Yet Receiving Benefits	19,152
Active Plan Members Vested	98,994
Active Plan Members Nonvested	55,191
Total	237,093

Funding Policy

Each biennium, the state Pension Funding Council adopts Plan 1 employer contribution rates, Plan 2 employer and employee contribution rates, and Plan 3 employer contribution rates. Employee contribution rates for Plan 1 are established by statute at 6 for state agencies and local government unit employees, and 7.5 percent for state government elected officials. The employer and employee contribution rates for Plan 2 and the employer contribution rate for Plan 3 are developed by the Office of the State Actuary to fully fund Plan 2 and the defined benefit portion of Plan 3. All employers are required to contribute at the level established by the Legislature. PERS Plan 3 defined contribution is a non-contributing plan for employers. Employees who participate in the defined contribution portion of PERS Plan 3 do not contribute to the defined benefit portion of PERS Plan 3. The Employee Retirement Benefits Board sets Plan 3 employee contribution rates. Six rate options are available ranging

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004**

from 5 to 15 percent; two of the options are graduated rates dependent on the employee's age. The methods used to determine the contribution requirements are established under state statute in accordance with chapters 41.40 and 41.45 RCW.

The required contribution rates expressed as a percentage of current-year covered payroll, as of September 30, 2004 were as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
Employer*	1.38%	1.38%	1.40%**
Employee	6.00%	1.18%	***

* The employer rates include the employer administrative expense fee currently set at 0.22%.

** Plan 3 defined benefit portion only.

*** Variable from 5.0% minimum to 15.0% maximum based on rate selected by the PERS 3 member.

Both the risk pool and the employees made the required contributions. The risk pool required contributions for the years ending September 30, 2004 were as follows:

	PERS Plan 1	PERS Plan 2	PERS Plan 3
2004	\$1,278	\$4,561	\$0
2003	\$1,195	\$4,153	\$0
2002	\$1,362	\$5,619	\$0

b. Qualified Pension Plan

The risk pool also participates in a qualified pension plan created in accordance with Internal Revenue Code Section 401(a). This plan is with the International City/County Management Association (ICMA). Employer contributions to the Qualified Pension Plan for the years ended September 30, 2004 and 2003 were \$25,884 and \$24,763, respectively.

NOTE 10 - DEFERRED COMPENSATION PLANS

The risk pool offers its employees a choice of two deferred compensation plans created in accordance with Section 457 of the Internal Revenue Code. The plans are with the International City/County Management Association (ICMA) and Nationwide Retirement Solutions (NRS). The plans, available to all eligible employees, permit them to defer a portion of their salary until future years. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

In 1998 NRS and ICMA Deferred Compensation Program plan assets were placed into trust for the exclusive benefit of participants and their beneficiaries. Pursuant to Governmental Accounting Standards Board (GASB) Statement 32 and since the risk pool is no longer the owner of these assets, the plan assets and liabilities are no longer reported in the risk pool's Financial Statements.

NOTE 11 – SUBSEQUENT EVENTS

In 2002, the risk pool paid a large settlement on behalf of a member county. The risk pool was reimbursed \$2,000,000 by one of its reinsurance companies to the full limit of its reinsurance contract but experienced difficulty in gaining full reimbursement from two other companies under their contracts. The risk pool negotiated a settlement in late 2004 with one company and plans to require the second reinsurance company to arbitrate under the terms of its reinsurance contract if a reasonable settlement does not result from negotiations presently taking place.

**WASHINGTON COUNTIES RISK POOL
NOTES TO FINANCIAL STATEMENTS
October 1, 2003 Thru September 30, 2004
REQUIRED SUPPLEMENTARY INFORMATION**

This required supplementary information is an integral part of the accompanying financial statements.

1. Ten-Year Claims Development Information

The table below illustrates how the risk pool's earned revenues and investment income compare to related costs of loss and other expenses assumed by the Risk Pool as of the end of each of the last ten years.

The rows of the table are defined as follows:

- (1) This line shows the total of each fiscal year's earned contribution revenues and investment revenues.
- (2) This line shows each fiscal year's other operating costs of the risk pool including overhead and claims expenses not allocable to individual claims.
- (3) This line shows the risk pool's incurred claims and allocated claims adjustment expense (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year).
- (4) This section of ten rows shows the cumulative amounts paid as of the end of successive years for each policy year.
- (5) This section of ten rows shows how each policy year's incurred claims increased or decreased as of the end of successive years. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known.
- (6) This line compares the latest reestimated incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for individual policy years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature policy years. The columns of the table show data for successive policy years.

**WASHINGTON COUNTIES RISK POOL
CLAIMS DEVELOPMENT
OCTOBER 1, 1995 THROUGH SEPTEMBER 30, 2004**

	<u>1995</u>	<u>1996</u>	<u>1997</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002</u>	<u>2003</u>	<u>2004</u>
1 Net earned required contributions and investment revenues	\$ 4,633	\$ 5,247	\$ 5,827	\$ 6,617	\$ 13,194	\$ 6,342	\$ 6,800	\$ 7,056	\$ 10,416	\$ 11,716
2 Unallocated expenses	\$ 1,682	\$ 1,826	\$ 1,997	\$ 1,753	\$ 3,765	\$ 3,734	\$ 4,216	\$ 4,531	\$ 5,635	\$ 8,071
3 Estimated incurred claims and expenses, end of policy year	\$ 2,272	\$ 3,625	\$ 3,093	\$ 4,200	\$ 1,900	\$ 2,000	\$ 2,249	\$ 1,860	\$ 1,615	\$ 1,900
4 Paid (cumulative) as of:										
End of Policy Year	\$ 52	\$ 84	\$ 49	\$ 5	\$ 10	\$ 18	\$ 3	\$ 36	\$ 51	\$ 68
One year later	\$ 200	\$ 1,017	\$ 399	\$ 362	\$ 77	\$ 205	\$ 204	\$ 160	\$ 240	
Two years later	\$ 1,049	\$ 2,237	\$ 1,643	\$ 1,366	\$ 258	\$ 365	\$ 389	\$ 282		
Three years later	\$ 1,756	\$ 3,197	\$ 2,893	\$ 2,474	\$ 424	\$ 680	\$ 695			
Four years later	\$ 4,021	\$ 3,977	\$ 3,738	\$ 3,705	\$ 636	747				
Five years later	\$ 4,895	\$ 5,381	\$ 5,409	\$ 3,985	904					
Six years later	\$ 5,147	\$ 5,439	\$ 6,871	\$ 4,687						
Seven years later	\$ 5,139	\$ 5,439	\$ 6,984							
Eight years later	\$ 5,956	\$ 5,463								
Nine years later	\$ 6,089									
5 Reestimate incurred claims and expense:										
End of Policy Year	\$ 2,272	\$ 3,625	\$ 3,093	\$ 4,200	\$ 1,900	\$ 2,000	\$ 2,249	\$ 1,860	\$ 1,615	\$ 1,900
One year later	\$ 3,150	\$ 3,625	\$ 4,650	\$ 4,700	\$ 1,725	\$ 1,985	\$ 1,800	\$ 1,685	\$ 1,890	
Two years later	\$ 3,105	\$ 5,350	\$ 5,550	\$ 5,100	\$ 1,650	\$ 1,580	\$ 1,730	\$ 1,380		
Three years later	\$ 4,600	\$ 5,850	\$ 5,775	\$ 5,675	\$ 1,220	\$ 1,460	\$ 1,350			
Four years later	\$ 4,975	\$ 5,575	\$ 6,320	\$ 5,416	\$ 1,115	\$ 1,370				
Five years later	\$ 5,100	\$ 5,717	\$ 7,388	\$ 5,961	\$ 1,142					
Six years later	\$ 5,276	\$ 5,806	\$ 8,528	\$ 6,943						
Seven years later	\$ 7,004	\$ 5,756	\$ 8,428							
Eight years later	\$ 6,419	\$ 5,956								
Nine years later	\$ 6,394									
6 Increase (decrease) in estimated incurred claims and expenses from end of policy year	\$ 4,122	\$ 2,331	\$ 5,335	\$ 2,743	(\$ 758)	(\$ 630)	(\$ 899)	(\$ 480)	\$ 275	-