

**STATE WORKERS' INSURANCE FUND:
FINANCIAL INTEGRITY AND STABILITY**

**REPORT OF THE
SELECT COMMITTEE TO STUDY SWIF**

General Assembly of the Commonwealth of Pennsylvania
JOINT STATE GOVERNMENT COMMISSION
November 1996

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108 Finance Building
Harrisburg, Pennsylvania 17120
November 1996

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The Joint State Government Commission was created by act of July 1, 1937 (P.L.2460, No.459) as amended, as a continuing agency for the development of facts and recommendations on all phases of government for the use of the General Assembly.

JOINT STATE GOVERNMENT COMMISSION, 1996

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TO THE MEMBERS OF THE GENERAL ASSEMBLY:

Pursuant to Act 10 of 1996, the Joint State Government Commission submits the report of the Select Committee to Study the Financial Integrity and Stability of the State Workers' Insurance Fund as of December 31, 1995. The recommendations adopted and herein presented by the select committee are the culmination of efforts on the part of the committee, the Commission, and Coopers & Lybrand L.L.P. (C&L), the accounting firm contracted by the Commission on behalf of the select committee. Senator Gibson E. Armstrong served as chairman of the select committee.

Respectfully submitted,

Roger A. Madigan
Chairman

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EXECUTIVE SUMMARY

This report is the latest in a series of studies of the financial health of the State Workers' Insurance Fund (SWIF). SWIF is the governmental fund that provides workers' compensation insurance to the residual market; as such it occupies a position similar to the assigned risk plan in automobile insurance by providing legally mandatory coverage to those who cannot obtain coverage in the voluntary market. Because residual carriers collect the worst risks, they face problems in maintaining solvency while keeping premium rates affordable to their subscribers.

The present study differs from previous audits of SWIF in that it inquires into whether the claims records kept by SWIF were consistent with its stated position as set forth on its balance sheet. The actuarial and accounting work was performed by Coopers & Lybrand L.L.P. (C&L), a firm named by the select committee upon review of competitive proposals.

The reports submitted by C&L came to two conclusions that deserve the attention of the General Assembly. The first is that the incompleteness of SWIF's insureds' claims records makes it impossible at present to perform an audit in accordance with generally accepted auditing standards and thus

only a disclaimer of opinion was issued by C&L. To perform a complete audit will require a reconstruction of the claims data, which may or may not be adequate to allow an unqualified opinion to be rendered. Alternatively, by keeping proper annually audited books, a set of records that will support an unqualified audit will gradually emerge.

The second conclusion is that SWIF has a reserve deficiency of \$326 million, which after taking a surplus of \$260 million into account, indicates a net shortfall over time of \$66 million; if SWIF were financially healthy, it would show a net surplus of about \$400 million. The financial weakness of SWIF is due in part to the Commonwealth's withdrawal from the fund of \$340 million from 1988 through 1992, compounding the inherent difficulty in maintaining a residual carrier in the workers' compensation insurance market. The deficiency does not indicate imminent insolvency, but does indicate that measures need to be taken to avoid further financial deterioration. It is also possible that the stated financial position of SWIF could change once the incompleteness of the claims records is rectified. Furthermore, SWIF's finances could be more favorable if it is earning more than the assumed 4 percent on its investments.

SELECT COMMITTEE RECOMMENDATIONS

The select committee adopts the following recommendations:

- (1) Establish continued legislative oversight of SWIF, pending the certification by a qualified accountant that SWIF has adequate reserves and that its records can support a standard audit. (Legislation required.)
- (2) Take appropriate steps to put the financial records in such a condition that an unqualified audit can be performed.
- (3) Suspend payments from the Fund, other than settlements of claims and ordinary expenses, until the shortfall has been eliminated. In particular, surplus should not be distributed and payments in lieu of taxes should not be made until the Fund is financially sound. (Legislation required.)
- (4) If the Commonwealth's fiscal standing permits, appropriate a partial or complete repayment over time of amounts previously distributed to other funds from SWIF. (Legislation required.)
- (5) Remove the Insurance Commissioner from the State Workers' Insurance Board and give the Insurance Department authority to regulate SWIF as if it were a private carrier. (Legislation required.)
- (6) Remove the State Treasurer from the State Workers' Insurance Board to relieve this official from potential conflicts of interest. (Legislation required.)

INTRODUCTION

The present study was done pursuant to the act of February 23, 1996 (P.L.27, No.10).¹ Under this legislation the Joint State Government Commission was directed to “establish a joint select committee to investigate the financial integrity and stability of the State Workers’ Insurance Fund (SWIF),” and to that end to evaluate the adequacy of SWIF’s reserves and surpluses “as measured against qualifying standards in benchmark tests of financial stability and performance tests of financial sufficiency against which workers’ compensation carriers are generally measured” and also to evaluate SWIF’s investment portfolio and investment practices. As part of this investigation, the committee was empowered to commission an independent actuarial study of SWIF. After evaluating proposals, the committee selected Coopers & Lybrand to perform the financial audit and actuarial study. The select committee was chaired by Senator Gibson E. Armstrong, chairman of the Senate Labor and Industry Committee.

¹This act added section 2211.1 to the act of April 9, 1929 (P.L.177, No.175), known as The Administrative Code of 1929. The study was originally to have concluded by June 30, 1996, but the termination date was extended to November 30, 1996 by the act of June 12, 1996 (P.L.337, No.53), when the section expires.

SWIF and its supervising agency, the State Workers' Insurance Board (SWIB), were established by the act of June 2, 1915 (P.L.762, No.340) (SWIF Act); 77 P.S. § 201 et seq., concurrently with the establishment of the workers' compensation program in this Commonwealth.² SWIF was created as a self-funding mechanism for providing workers' compensation coverage, which is mandatory for all employers, for those who wished to avail themselves of its services. Such state-constituted insurers have been established in many states to afford coverage to the "residual market," that is, those employers who are unable to obtain coverage in the voluntary insurance market.³ As insurer of last resort, SWIF occupies a position similar to the assigned risk plan in automobile insurance; at the same time, SWIF insures many businesses that could obtain voluntary coverage.⁴ The residual market can easily become unstable if rates are not set at the correct level.⁵ For many years SWIF was protected from the vagaries of the residual market because it covered the large pool of

²Workers' compensation is provided pursuant to the act of June 2, 1915 (P.L.736, No.338), known as the Workers' Compensation Law.

³National Association of Insurance Commissioners, "Market Conditions in Workers' Compensation Insurance," (NAIC Report) Interim Report Presented to the NAIC Workers' Compensation (D) Task Force (1993), 17.

⁴Legislative Budget and Finance Committee (LB&FC) Performance Audit State Workmen's Insurance Board (August 1993) (1993 LB&FC Performance Audit), 3, 4.

⁵NAIC Report, 52-55.

Commonwealth employees. However, since 1983 the Commonwealth has obtained other coverage for these employees.⁶

The 1915 act originally made no provision for outside audits of SWIF. However, a 1923 supplement to the 1915 act⁷ required the Auditor General to make an annual examination and audit of SWIF and to review its disbursements for salaries and expenses. Since 1957, the Auditor General has had the responsibility to audit SWIF annually under section 402 of The Fiscal Code within the Auditor General's power to audit the affairs of the executive branch of Commonwealth government.⁸ A supplement enacted in 1933 required the Insurance Department to perform a "complete examination and audit" of SWIF annually in order "to ascertain its financial condition and its ability to meet its obligations, whether [SWIB] in managing the fund has complied with the provisions of law relating to the fund, and the equity of the board's plans and dealings with its policyholders."⁹ In 1961 the Insurance Department's oversight was redesignated as a "complete inspection and examination," to be done every three years or more often if deemed necessary; the scope of this examination included any "facts relating to its

⁶1993 LB&FC Performance Audit, 70.

⁷Act of June 13, 1923 (P.L.698, No.291).

⁸Section 402 of the act of April 9, 1929 (P.L.343, No.176), known as The Fiscal Code. The act of May 31, 1957 (P.L.237, No.115), removed an exception for SWIF, thereby making the Auditor General responsible for auditing SWIF.

⁹Act of May 1, 1933 (P.L.102, No.68), § 1.

business methods and management” as well as the areas included in the 1933 supplement.¹⁰ In 1975 Attorney General Opinion No. 75-44 concluded that the Insurance Commissioner cannot properly audit SWIF because of the Commissioner’s role in administering the Fund as a member of SWIB. As a result, the Insurance Department does not conduct financial or regulatory audits of SWIB.¹¹ The Insurance Department is authorized to increase the liability or compensation loss reserves of SWIF if these are inadequate under statutory standards.¹²

The SWIF Act was amended thirteen times prior to its repeal and incorporation into the Workers’ Compensation Act.¹³ The act of July 1, 1990 (P.L.298, No.68), the most extensive of these amendments, made substantial changes to the treatment of surpluses. The original act had provided that the safely distributable surplus “be distributed among the subscribers in proportion to the premiums paid by them” in the form of credits to all subscribers except those that terminated coverage under the Fund.¹⁴ Despite this provision, \$205 million was paid from SWIF to the General Fund, the Sunny Day Fund and the Tax Stabilization Reserve Fund in

¹⁰Act of July 26, 1961 (P.L.902, No.387).

¹¹1993 LB&FC Performance Audit, 13.

¹²Act of June 19, 1919 (P.L.437, No.216), § 3; 77 P.S. §§ 393 and 394.

¹³This count does not include the Commonwealth Court Act (1969 Act 185, P.L.434), the Appellate Court Jurisdiction Act (1970 Act 223, P.L.673) or the Judiciary Act Repealer Act (1978 Act 53, P.L.202), all of which incidentally affected the SWIF Act.

¹⁴Act of June 2, 1915 (P.L.762, No.340), § 11.

calendar years 1988 and 1989.¹⁵ The 1990 amendments authorized payments of safely distributable surplus to be split between the subscribers and the Sunny Day Fund and the Tax Stabilization Reserve Fund.¹⁶ The Advisory Council to SWIB was established with the duty to recommend what amount, if any, constitutes the safely distributable surplus; to commission independent actuarial studies of SWIF no more than once a year; and to review the annual independent actuarial study of SWIF that the legislation required SWIB to conduct through a certified actuary. Furthermore, the 1990 amendments required SWIF to make payments in lieu of taxes to the General Fund and appropriated \$125 million from SWIF to the General Fund representing such “taxes” accrued from January 1, 1985 through June 30, 1990. Since then, payments in lieu of taxes have been measured by the amount which would have been paid in Federal income and Pennsylvania premium taxes had SWIF been subject to such taxes. Finally, the 1990 amendments repealed the 1933 supplement, thereby relieving the Insurance

¹⁵Office of the Auditor General, Audit Report for the Years Ended December 31, 1992 and 1991 (SWIF), 13.

¹⁶The Sunny Day Fund and the Tax Stabilization Reserve Fund are to be reimbursed for any downward deviations granted to subscribers as compared to otherwise applicable rates. After this adjustment, at least one-half of the surplus is available for appropriation for ratable credits or rebates to the subscribers. Whatever remains may be transferred to those funds by appropriation. These provisions were inserted as a result of a stipulation settling a lawsuit brought by the Pennsylvania Chamber of Commerce. 1990 House Legislative Journal, 1301-1306. The provisions, formerly in §11 of the SWIF Act, have been reenacted without substantive change by 1996 Act No. 57 as § 1511(c) of the Workers’ Compensation Act.

Department of its responsibilities regarding oversight of SWIF, except those pertaining to loss reserves.

A comprehensive reform of the Workers' Compensation Act was instituted by the act of July 2, 1993 (P.L.190, No.44). The act, among other changes, included extensive provisions relating to setting of premium rates that give SWIF and other insurers greater flexibility. More competitive rates could induce the more profitable policyholders to shift from SWIF to other carriers, although SWIF could also benefit from greater flexibility.¹⁷

In August 1993, the Legislative Budget and Finance Committee released a performance audit of SWIF in response to three bills proposing to review SWIF under Sunset.¹⁸ This study relied on an actuarial study of SWIF by Ernst & Young that concluded that as of December 31, 1992, SWIF had adequate reserves but no safely distributable surplus.¹⁹ The act also included provisions tightening medical benefits, which were expected to exert downward pressure on premium rates.

The SWIF Act was repealed by the act of June 24, 1996 (P.L.350, No.57), which reenacted its provisions without relevant substantive changes as Article XV of the Workers' Compensation Act.

¹⁷1993 LB&FC Performance Audit, 8.

¹⁸ibid., 1.

¹⁹ibid., 18-26.

FINANCIAL AUDIT AND ACTUARIAL ANALYSIS

Over the past fifteen years, various efforts have been made to audit the financial and actuarial standing of SWIF. The major concern that seemed to arise in recent years was that the primary financial data of SWIF had not been audited by any of the analyses. Rather, the baseline data was provided by SWIF to the auditors, who assumed it to be complete and accurate. The lack of a complete audit, from the most primary data available through a complete actuarial analysis, prompted the General Assembly to commission this study. Coopers & Lybrand approached the project focusing its efforts on two separate but linked analyses. First, the statutory balance sheet was audited and substantiated; then an actuarial analysis was performed on the financial data thus verified.

Financial Audit

The basis of a financial audit is the reconciliation of the figures on the balance sheet with the transactions that the balance sheet reflects. In the case of this particular balance sheet audit, C&L attempted to map the year's transactions to the summaries of admitted assets, liabilities and

surplus that were reported by SWIF as of December 31, 1995. The financial audit decreased assets by \$5.3 million and liabilities were decreased by \$15.4 million, resulting in a net increase in the surplus account of \$10.1 million.²⁰ The auditor, having been satisfied that sufficient evidence substantiated the reported figures on the balance sheet, then passed the data on to the actuary.

Actuarial Analysis

An actuarial analysis provides an indication of the ability of an insurance company to honor the current and future claims to which it is obligated, thereby forecasting the health of the insurance fund. The history of the insurance fund is examined in order to make projections about the future situations that the fund may face. Data gathered and analyzed include the type of claim, the claimant's medical history, the payment schedule and the costs of administering each claim. Additionally, the

²⁰C&L, "Report of Independent Accountants on Statutory Statement of Admitted Assets, Liabilities and Surplus as of December 31, 1995" (Report on Statutory Statement), 15. The entries for premiums in the course of collection and accrued investment income were reported by SWIF to be \$42.4 million and \$25.1 million, respectively. C&L found discrepancies in the accounting of these amounts, and made changes to the financial statement. Premiums in the course of collection was changed to \$40.1 million and accrued investment income was changed to \$22 million, for a net decrease in the assets category of \$5.3 million.

Liabilities were also adjusted. Unearned premium reserve was reported as \$82.5 million and changed to \$65.5 million. Accrued taxes, licenses and fees was changed from \$8.0 million to \$9.6 million. The net affect to liabilities was a decrease of \$15.4 million. The changes to assets and liabilities led to C&L to adjust the surplus from \$139 million to \$149 million.

actuary studies the income of the fund, including premiums and investment income. The ability of the fund to meet its obligations depends on the income it receives as it is making payments on claims. The claims and income predictions are aggregated, from which an overall indication of the present and future health of the fund can be determined.

The claims master file is the primary record of compensation claims. Most relevant data regarding specific claims are held in this file. Therefore, the claims master file is a source of the substantiating data for the loss reserves and loss adjustment expenses; those two accounts represent the payment obligations of SWIF on the balance sheet.

C&L discovered during its audit procedures that the detailed claims master file did not exist at SWIF in a manner suitable for audit. Although SWIF maintained summary data regarding the filed claims, the original documents supporting those data have not been retained. Several attempts were made to locate sufficient records, but none were successful. By C&L's reporting, neither SWIF, the Auditor General, the Insurance Department, the Pennsylvania Compensation Rating Bureau (PCRB)²¹ nor any of the private accounting firms that C&L contacted had records that could substantiate the summaries calculated by SWIF.

²¹The PCRB is the privately created rating organization designated by the Insurance Department to set the rates for workers' compensation in this Commonwealth, subject to the approval of the department.

To overcome the obstacle of the missing data, C&L, with the agreement of SWIF management, contacted the Joint State Government Commission with a request to extend the original engagement contract for additional financing to fund its attempt to build a claims master file data base.²² SWIF computer personnel were able to create computer tapes reflecting approximately ten million transactions spanning the last eight years. The sorting and analyzing of these transactions proved too burdensome to be completed in time for C&L's final report to be submitted to the select committee. As a result, the financial figures that C&L used for its actuarial analysis were predominantly unaudited. For this reason, C&L was not able to offer an unqualified opinion on the state of SWIF.

Reserves and Surpluses

The actuarial report indicates that there is a potential for reserves to be inadequate and that surplus is currently unable to cover such an inadequacy. Reserve adequacy is shown in three scenarios presented in the analysis: undiscounted liabilities, liabilities discounted at 4 percent, and liabilities discounted at 6 percent.²³ Discounted liabilities refer to the use of

²²Letter from Mark Glessner, C&L, to Conrad C. M. Arensberg, Commission, dated August 14, 1996.

²³Coopers & Lybrand, "State Workmen's Insurance Fund Estimates of Reserves for Losses and Reserves for Loss Adjustment Expenses as of December 31, 1995" (Estimate of Reserves), October 1996, 4.

present-value calculations in determining reserve adequacy. Because the reserve money held by SWIF is expected to earn interest and thereby grow over time, SWIF need not hold current reserves covering all of the future payments that it will be making. To reflect these earnings, the reserve is discounted using an interest rate that reflects the expected rate of return on investments. It is generally assumed in the insurance industry that at least 4 percent will be earned on investments, and present reserves are held to reflect that rate.

When SWIF assumed a 4 percent discount, it represented its reserves to be \$1.267 billion. C&L, using SWIF's data, arrived at a significantly different amount. C&L considered three possibilities for what the needed level of reserves may be: an expected, a reasonable high and a reasonable low. The expected reserves, at a discount of 4 percent, are \$1.593 billion. This amount is greater than SWIF's calculated reserves by \$326 million, and indicates that SWIF has underfunded its reserves by that amount. The reasonable high estimate of needed reserves is \$1.708 billion and the reasonable low estimate is \$1.465 billion. Thus, the range of needed reserves, as calculated by C&L, is \$198 million to \$441 million more than SWIF can accommodate with its present reserves.²⁴

²⁴C&L, Estimate of Reserves, 4, 17 and 18.

The difference of \$326 million between C&L's expected level of reserves and SWIF's indicated reserves can be explained. Through the years up to and including 1994, there has been a range of differences between SWIF's and C&L's calculations of reserves. The total of these differences is \$235 million. Part of the reason for the differences is that SWIF calculated the reserves for each year based on the data it had for each particular year. With the benefit of hindsight, C&L could make more accurate calculations of payout, because the payouts for those years had already been made. It is also possible that C&L made different assumptions from those made by SWIF in interpreting loss development statistics, in assessing the impact of legislative reform on Pennsylvania's workers' compensation loss costs or in weighting the various actuarial methods used to develop a reserve estimate. The remaining difference²⁵ between SWIF's and C&L's calculations is accounted for by C&L's adjustment of adverse claims development by \$34 million and loss adjustment expenses by \$57 million.²⁶

SWIF reported a surplus of \$260 million for the period ended December 31, 1995. If reserves cannot cover losses, the surplus is applied

²⁵I.e., \$326 million - \$235 million = \$91 million.

²⁶C&L, Estimate of Reserves, 18.

to the shortfall. If the surplus were used against this shortfall, the fund would remain short by approximately \$66 million (i.e., \$326 million - \$260 million).

C&L also calculated the reserves necessary assuming a 6 percent rate of return on SWIF's investments. The shortfall possibilities under a 6 percent discounting scenario range from \$42 million to \$258 million, with the expected reserve shortfall amounting to \$155 million.

SWIF is lagging the rest of the industry in terms of its reserve and surplus adequacy. C&L identified other states' funds and their reserve and surplus adequacies. When compared to these funds, SWIF should be maintaining a surplus in the range of \$400 million to \$500 million.²⁷

Other Findings

SWIF's investment portfolio was analyzed by C&L to address certain areas of SWIF's investment practices.²⁸ C&L found that SWIF is operating without a formal investment policy to direct its investment managers. The undefined investment policy has resulted in some practices that may not be optimizing SWIF's portfolio. For example, C&L determined that the turnover rate of SWIF's portfolio is faster than it should be. In some instances, SWIF's investment practices are not in accordance with generally accepted

²⁷Ibid., 168.

²⁸The maturity spread of SWIF's investments is presented in C&L, State Workmen's Insurance Fund, Observations and Findings, 14.

accounting principles, but it appears that these deviations have not had a material impact on the balance sheet.²⁹ SWIF management has agreed to consider implementing the recommendations made by C&L.

C&L took into consideration that SWIF operates somewhat differently from other insurance providers in the workers' compensation sector. SWIF relies on the Department of Labor & Industry and other State agencies for providing various services that private insurers would provide for themselves.³⁰

Several other findings that C&L highlighted during the course of its review seem unique to SWIF among other workers' compensation insurance providers but are unrelated to its position as a public agency. For instance, no one person has complete oversight of the financial operations, increasing the potential for inefficiencies.

Another problem is in the area of reinsurance. It is common in the industry for insurance companies to buy insurance against their own potential losses. The option has always been available to SWIF.³¹ SWIF is not currently participating in a reinsurance program with respect to open

²⁹Ibid., 13-21.

³⁰For example, SWIF relies on the Department of General Services for office space, building maintenance and procurement services. The Department of Labor & Industry negotiates service and legal contracts on behalf of SWIF. The State Treasury processes checks and invests SWIF's short-term investments and cash. C&L, Report on Statutory Statement, 14.

³¹Section 1514 of the Workers' Compensation Act, formerly § 14 of the SWIF Act.

claims, although it continues to be a party to reinsurance contracts that expired in the mid-1980's.³² Rather than rely on reinsurance, SWIF maintains a catastrophe reserve account funded by a percentage of premiums. As of December 31, 1995, this account stood at \$110 million. This amount is held in the surplus account, and has been considered by C&L in its analysis of the reserve and surplus adequacy.³³

From 1988 through 1992, the Legislature appropriated from SWIF \$340 million into the General and other funds.³⁴ Had they been retained in SWIF, these funds would have raised the current surplus of \$260 million to a level of \$600 million, not counting interest or transfers to reserves. The result would be that although not facing a difficult financial situation, SWIF's surplus would be about \$126 million below its recommended level relative to its peers in the industry after the reserve inadequacies are considered.³⁵

Coopers & Lybrand's Recommendations

C&L has made observations beyond the adjustments to the balance sheet and the recommendations to improve the standing of the reserves and

³²C&L, Observations and Findings, 39-41.

³³C&L, Report on Statutory Statement, 14. The catastrophe reserve account is provided for by § 1509 of the Workers' Compensation Act, formerly § 9 of the SWIF Act.

³⁴1993 LB&FC Performance Audit, 22. As the appropriation of the funds occurred prior to the period being audited, C&L did not formally evaluate its effect.

³⁵The \$340 million would potentially raise surplus from \$260 million to \$600 million. It is expected that reserves would be about \$326 million short of meeting SWIF's obligations. The shortfall would be funded by surplus, leaving that account at \$274 million. C&L determined that SWIF's healthy level of surplus is at least \$400 million.

surplus.³⁶ There are forty-six recommendations made by C&L to address the managerial and operations problems faced by SWIF and to conform its practices with generally accepted accounting principles. These range from automating certain manual operations by purchasing a spreadsheet program, to evaluating SWIF's compliance with the regulations of the Insurance Department.

Nearly all of the recommendations that have been made are agreed to by SWIF management. In a few instances, SWIF management claims that certain recommendations may not be feasible or appropriate under its current environment. Management's agreement and attempts to follow through on C&L's recommendations represents the commitment of SWIF to regain its financial standing.

³⁶C&L, Observations and Findings.

SELECT COMMITTEE RECOMMENDATIONS EXPLAINED

The Select Committee recommends the following measures for consideration by the General Assembly:

1. *Establish continued legislative oversight of SWIF, pending the certification by a qualified accountant that SWIF has adequate reserves and that its records can support a standard audit.* Given the recent history of SWIF and the difficulties inherent in maintaining a viable carrier of last resort, only continuous legislative oversight will assure that the Fund is continuing to improve its position and that future problems will receive the immediate attention of the General Assembly. Legislation will be needed in order to establish an appropriate oversight mechanism.

2. *Take appropriate steps to put the financial records in such a condition that an unqualified audit can be performed.* It is likely but not certain that by further analysis of the computer records of claims, an accurate data base can be reconstructed. The second alternative--and the only alternative if the first strategy fails--is to do a series of audited statements that will gradually formulate an accurate financial picture.

3. *Suspend payments from the Fund, other than settlements of claims and ordinary expenses, until the shortfall has been eliminated. In particular, surplus should not be distributed and payments in lieu of taxes should not be made until the Fund is financially sound.* The law permits SWIF to make distributions of “safely distributable surplus” to the Commonwealth, but only if such distributions will not impair the actuarial soundness of the Fund. With the Fund facing a shortfall of \$326 million, such a surplus does not presently exist. While in other circumstances it might be appropriate for payments in lieu of taxes to be made in order to put the Fund on a competitive basis with other carriers, it seems unwise to continue requiring such payments when the Fund is in a weak financial state. Legislation would be needed to suspend payments in lieu of taxes.

4. *If the Commonwealth’s fiscal standing permits, appropriate a partial or complete repayment over time of amounts previously distributed to other funds from SWIF.* It is likely that SWIF owes its position in part to the removal of \$340 million from the Fund from 1988-92. The Fund’s return to full financial health will be facilitated by an infusion of appropriated funds.

5. *Remove the Insurance Commissioner from the State Workers’ Insurance Board and give the Insurance Department the authority to regulate SWIF as if it were a private carrier.* In 1975 the Attorney General determined that the Insurance Commissioner could not simultaneously serve on SWIB

and audit SWIF as an illegal conflict of interest existed. The Insurance Commissioner remains a member of SWIB under current legislation. Since the Insurance Department possesses the expertise to supervise the financial affairs of private workers' compensation carriers, it may be preferable to resolve the conflict by enacting legislation that gives the Insurance Commissioner supervisory rather than board functions with regard to SWIF.

6. Remove the State Treasurer from the State Workers' Insurance Board to relieve this official from potential conflicts of interest. The State Treasurer is also a member of the State Workers' Insurance Board. This duty may raise a conflict of interest when considered in light of the responsibility under Article III of The Fiscal Code to direct the investment of the moneys of the Commonwealth.