





Risk Management Division

Mission Statement

Preserve Minnesota's governmental assets by managing customer risk.

Goals/Strategies

Reduce risk by using proactive risk management techniques

Maintain financial stability

Deliver comprehensive, cost-effective, insurance services

Vision

Our vision is to be a leader in providing high quality risk and insurance management products and services to our customers and to be recognized as a leader in the state and insurance community.

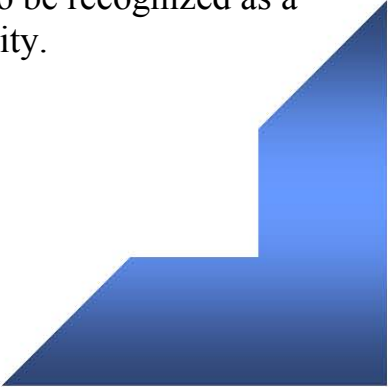


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Commissioner's Statement



Risk management is about bringing order to change in an unpredictable world. Accomplishing it requires vigilance, anticipation, knowledge and commitment to customer needs.

The Risk Management Division continues to grow and develop new and innovative products for the changing needs of its customers. For example, with computers now as ubiquitous as the telephone in business and government, Risk Management Division in 2006 added cyber-property and cyber-liability insurance to its customers' coverage, at no additional charge. The year also brought about additional loss control measures through inspections and appraisals at numerous state owned properties and through the implementation of Fleet Safety Management Standards.

In spite of the best efforts toward minimizing risk, losses occur. But advance planning in anticipation of an incident and quick action at the time of an accident can limit losses. Such was the case in October 2005, when a high-pressure water main burst and caused extensive flooding on two floors of the Centennial Office Building in St. Paul. Early notification of the event resulted in a quick response by specialty disaster-restoration contractors. Irreplaceable documents from Military Affairs and veterans' organizations were freeze-dried and saved for future generations. A quick dry-out prevented mold development and the building was swiftly restored and remodeled.

Beyond dealing with accidents and destruction, the mission of the Risk Management Division – in fact, of the entire Department of Administration – is to help our customers succeed so that they may better fulfill their missions. On the lighter side, we are fortunate to have customers for which rest, relaxation, entertainment and enlightenment are the objectives of their work. With that in mind, the focus of this Annual Report is on FUN.

From the Great Minnesota Get Together to the Minnesota Lottery, from the Zoo to skiing and golfing at Giant's Ridge, from historic preservation at Ironworld Discovery Center to fishing, hunting and all other outdoor activities supported by the Department of Natural Resources, to the arts and culture, Risk Management Division has interesting, important and, most of all, many customers whose business is fun. It is certainly our pleasure working with them.

A handwritten signature in black ink that reads "Dana B. Badgerow".

Dana B. Badgerow, Commissioner
Department of Administration

Director's Message



This year's annual report objective is to lighten up a bit and, to do that, we are emphasizing the "fun" agencies that we insure. These are the agencies that specialize in entertaining the masses and include the Minnesota Zoo, Minnesota State Fair, Giant's Ridge, Ironworld, Minnesota State Lottery, Perpich Center for Arts Education, the Minnesota Amateur Sports Commission, as well as others.

Fiscal Year 2006 was indeed a fun year from many aspects:

- The Risk Management **Fund** (RMF) was financially stable;
 - The results per line of business were positive, with the exception of auto liability, and we are working on that;
 - Dividend payouts to policyholders were maintained;
 - Interest income was up; and,
- Most importantly, we had a veteran staff with no turnover in the last two years.

So, is there any reason not to be in high spirits and emphasize the fun side of risk management?

In this annual report, there are more pictures and fewer figures than usual. The depiction of our fun agencies also adds a more interesting aspect to reporting on the year just past. Our customers continue to do a great job of managing their properties and liabilities.

The concept of insurance is that "the premiums of many pay the losses of a few." This concept has been in place for over three centuries when insurance was first transacted in coffee houses in England. The most famous of all the coffee houses was the one owned by Edward Lloyd in the City of London, now referred to as *Lloyd's of London*. Perhaps you have heard of it. It is significant to continue the tradition of insurance and risk management in some small way and I believe that is what is taking place with the Minnesota risk management endeavor. This insurance concept is alive in the Risk Management Division (RMD).

We look forward to serving our customers in the future, just as we have in the past. It is no platitude to say that we enjoy providing the best insurance environment we can for our customers and we are pleased to take this year to recognize our agencies that help entertain and educate the general public.

Next year, we will be looking at our 20th anniversary. It is gratifying to know that the RMD will continue to provide professional insurance services to our customers. The RMF is built on a solid foundation that started with that first auto liability policy issued by the RMF on January 1, 1987. It is the pleasure of today's RMD staff to carry on the tradition.

I would like to conclude by saying a special thank you to all for making this year such a success.

A handwritten signature in cursive script that reads "Phillip E. Blue".

Phillip Blue
Director

Risk Management Fund Advisory Committee

Frank Ahrens
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Fiscal & Administrative Services

Mary Lou Houde
Department of Commerce
Registration & Insurance

John King
Department of Corrections

Peggy Lexau
Department of Finance

Sheila Reger
Deputy Commissioner
Department of Administration

Peter Young
University of St. Thomas

Sieglinde Bier
Minnesota State Colleges
and Universities

Bill Hoyt
Metropolitan Airports
Commission

Terry Lahti
Department of Natural
Resources

Tim Morse
Department of Administration
Travel Management Division

John Scharffbillig
Department of Transportation

Phillip Blue
Department of Administration
Risk Management Division

Tom Hugdahl
3M Insurance Department
(Retired)

Jan Larson
Department of Administration
Financial Mgmt and Reporting

Mary Pittelko
State Agricultural Society
(State Fair)

Gary Westman
Department of Employee
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Split Rock Lighthouse
Photo courtesy of Minnesota Historical Society



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Customer Agencies and Political Subdivisions



Administrative Hearings, Office of	Military Affairs, Department of
Agriculture, Department of	Minnesota Historical Society
Amateur Sports Commission	Minnesota State Academies
Anoka County	MN Legislature – Office of the Revisor of Statutes
Attorney General	MN State Lottery
Barbers & Cosmetologist Examiners, Board of	MN State Colleges and Universities - all facilities
Behavioral Health & Therapy, Board of	MN Technology
Center for Criminal Justice & Law Enforcement	Natural Resources, Department of
Chicano Latino Affairs Council	Nursing, Board of
Chiropractic Examiners, Board of	Nursing Home Examiners BENHA, Board of
Commissioner's Office	Office Supply Connection
Communications Media	Ombudsman for Mental Health & Mental Retardation
Central Mail	Optometry, Board of
DocuComm	Pennington County
ReComm	Perpich Center for Arts Education
Corrections, Department of	Pharmacy (ASU), Board of
Dakota County	Physical Therapy, Board of
Dentistry, Board of	Plant Management
Development Disabilities Council	Podiatric Medicine, Board of
Dietetics & Nutrition Practice, Board of	Pollution Control Agency
Education, Department of	Port Authority of the City of St Paul
Emergency Medical Services Regulatory Board	Psychology, Board of
Employee Relations, Department of	Public Defense, Board of
Employment and Economic Development, Department of	Public Employees Retirement Association
Enterprise Technology, Office of	Public Safety, Department of
Explore Minnesota Tourism	Public Service, Weights & Measures
Financial Management & Reporting	Revenue, Department of
Gambling Control Board	Risk Management
Governor's Office	Secretary of State
Health, Department of	Social Work, Board of
Health Professional Services Program	STAR Program
Higher Education Facilities Authority	State Agricultural Society (State Fair)
Higher Education Services Office	State Architect's Office
Housing Finance Agency	State Armory Building Commission
Human Rights, Department of	State Arts Board
Human Services, Department of	State Auditor
Indian Affairs Council	Supreme Court – State Court Administration
Information Policy Analysis Division	Supreme Court – State Court Admin/Law Library/Court of Appeals
Insurance Fraud Prevention, Division of	Supreme Court – Board of Law Examiners
Investment Board	Surplus Services
Iron Range Resources	Teachers Retirement Association
Judicial Standards, Board of	Transportation, Department of
Labor & Industry, Department of	Travel Management
Lawyers Professional Responsibility Board	Veterans Affairs
Management Analysis	Veterans Homes Board – all locations
Marriage & Family Therapy, Board of	Veterinary Medicine, Board of
Medical Practice, Board of	Zoological Board
Metropolitan Airports Commission	
Metropolitan Council	

Fiscal Year 2006 Highlights

Property renewal rates were reduced an average of 21 percent, or a little over \$1.1 million in premium, from the previous year's rates. This was possible due to lower reinsurance costs brought on by improved loss experience. The improvement in loss experience was due, in part, to increased loss control efforts by agencies and Risk Management.

The Risk Management Advisory Committee approved payment of more than \$1.3 million in dividends to eligible policyholders.



Risk Management retained the Minnesota State Colleges and Universities system (MnSCU) property insurance program. Customer service was vital to retention of the program since MnSCU considers the Risk Management Division their "risk management arm."

Centennial Student Union –
Minnesota State University, Mankato

For the second straight year, staff renewed 100 percent of self-insurance policies in the first quarter. This is a tremendous achievement from a processing and cash flow standpoint. It took the equivalent of two FTEs working diligently to accomplish this task.

An Auto Fleet Management Task Force, comprised of the state's major (85 percent) auto agencies – Minnesota Department of Transportation (MnDOT), Public Safety, Travel Management, MnSCU, and Department of Natural Resources (DNR) – was initiated to put together a standardized policy for certain elements of auto fleet management, such as driver obligations, accident reporting, van selection, towing regulations, etc., with the intent of reducing accidents and auto insurance costs statewide. The statewide policy developed by the Task Force was adopted by the Risk Management Advisory Committee. Involvement continues as the Task Force reviews exceptions to the Model Fleet Safety Management Standards and meets with agencies one-on-one to discuss the Standards.



Staff met with Munich Re America, our excess casualty carrier, in order to gain a better understanding of what could be expected for the FY07 excess casualty renewal. They were informed about RMD's proactive steps taken since a large May 17, 2005 auto loss in Michigan. Those steps taken will serve to improve both auto liability and auto physical damage loss experience, increasing the likelihood that Munich will continue to provide excess casualty coverage for our clients at a fair premium.

Major water damage, the result of a water main break, occurred in the Centennial Office Building on October 3, 2005. The result of the loss was a learning experience for the various players in reporting, quick action, and clarification of individual roles.

Spring Seminars were conducted at four statewide locations. Evaluation returns that included learning experiences and recommendations were compiled and noted.

Certificate of Insurance issuance capability was added to Risk360°, RMD's policy processing software. Automation of Certificate issuance is more time efficient.



"From a claims perspective . . ."



Underwriting staff visited the MnDOT Camp Ripley Snow Plow Operator Training Program. Staff gained a better understanding of the effectiveness of the program and how it can positively impact the RMF auto loss experience.

During the Hurricane Katrina disaster and aftermath, state agencies involved in the relief efforts were kept apprised of insurance issues as they arose.

“Do you think you’re ready for the road test?”

Request for Proposals (RFP) for broker services – The broker places our reinsurance and facilitates placement of purchased insurance, thereby allowing the RMF to meet clients’ demands for coverages and limits of liability. Two brokers were selected – Alliant Insurance Services for the property program and incumbent Marsh USA for the casualty program.

The RFP process for claims administration services was implemented. Allied Adjusters, the preceding five-year incumbent, was selected from a number of proposers.

Twenty-five new policies were written by the RMF in FY06 for a total premium of approximately \$37,000. Some policies represented additional coverages for our existing clients; whereas, others were for new clients. Explore Minnesota Tourism - Governor’s Snowmobile Ride; a joint venture between Pennington County, DNR, and MnDOT; and additional coverages for MnSCU and Public Safety are examples.

The RMF purchased \$5 million additional excess casualty coverage that provided additional protection for the Auto Liability and General Liability lines from extra-territorial and federal claims.



FY06 was the first time that the RMF insured the Governor’s Snowmobile Ride, which is sponsored by Explore Minnesota Tourism.



Safety Programs

The RMD safety initiatives include several loss prevention programs. These efforts were initiated following a major fire loss in 2001. RMD establishes an annual budget for loss prevention and divides the expenditures between property loss conservation surveys, infrared electrical systems surveys, and real estate appraisals. In FY06 a greater emphasis was placed on the area of automobile fleet safety.

Fleet Safety

The importance of a comprehensive fleet safety program came to the forefront following a tragic van accident that resulted in the death of several college students during a campus trip to another state. A task force comprised of representatives from five state agencies was formed in July of 2005. The purpose of the task force was to develop a set of standards that each state agency would be asked to address in their fleet safety program. The agencies participating on the task force represented 85 percent of the state's automobile fleet. The Model Fleet Safety Management Standards were presented to the Risk Management Advisory Committee for their approval. The task force has remained in place to assist state agencies with the development and implementation of their fleet safety program.

COPE

COPE is an insurance acronym referring to the **C**onstruction, **O**ccupancy, **P**rotection, and **E**xposure for a particular building. A COPE visit is a property loss conservation survey of a state facility. These surveys are conducted by an outside property loss control consultant and/or a RMD staff member. These COPE surveys help to assure that the state properties insured in the RMF are in compliance with fire and life safety codes. During FY06, COPE surveys were conducted on three MnSCU campuses and at two correctional facilities. Going forward, RMD will be scheduling COPE surveys on a once every three year cycle.

Infrared Electrical Systems Surveys



During FY06, we continued to conduct Infrared Electrical Systems Surveys on state properties that are insured in the RMF. We started using this innovative loss prevention technique in FY05. The emphasis in FY06 was to survey the MnSCU campuses. Working with Infrared Consulting Services, we conducted infrared surveys on 33 MnSCU campuses. The MnSCU project will be completed in FY07. We plan to continue to conduct infrared surveys of other insured state properties.

Infrared scan at Minnesota State College - Southeast Technical, Winona

Appraisals

We work with each of our insured customers to establish and maintain an adequate amount of insurance for each item on their property schedule. It is very important for property managers to regularly review and update their property coverage limits. In the event of a fire or other loss, an inadequate amount of coverage could result in the insured not being fully reimbursed for their damage. The RMD works with several nationally recognized commercial property valuation firms to establish an annual adjustment that reflects inflation and current construction costs.

During FY06, RMD conducted on-site property appraisals at four MnSCU campuses and one building in the Capitol complex.

Glossary of Insurance Terms

Translation: Insurance Fun Facts from A to Z

Accident: An incident resulting in injury or damage to a person or property which has or could become a loss.

Translation: Oops!

Aggregate Limit: A limit in an insurance policy stipulating the most it will pay for all covered losses sustained during a specified period of time, usually one year. Aggregate limits are commonly included in liability policies.

Translation: The insurance company will pay up to this amount and no more in any given year.



You don't want this to happen!

Automobile Liability Insurance: Auto liability provides coverage for injuries to others and/or damage to their property (bodily injury and property damage liability) arising out of an insured's ownership or use of motor vehicles.

Translation: Covers injuries to others and damage to their vehicle, all because you were distracted or weren't watching where you were going.

Automobile Physical Damage Insurance: Auto physical damage provides coverage for damage to owned vehicles. Two basic types of physical damage coverage are generally provided for owned vehicles – collision and comprehensive. Collision coverage insures against damage from collision with another vehicle or object, as well as from overturning. Comprehensive coverage provides protection against damage from other perils such as hail, fire, vandalism, and flood.

Translation: Covers damage to the vehicle you are driving.

Boiler & Machinery Insurance: Although it is called Boiler and Machinery Insurance, businesses with no boilers on premises have a significant exposure. What is referred to as “boiler insurance” provides important coverage for machinery as well; e.g., building maintenance equipment, like air conditioners, furnaces, and production machinery. Equipment breakdowns and electrical damage losses are relatively commonplace occurrences. They are not covered under property insurance policies; rather, they are covered under boiler and machinery. Coverage includes loss sustained by the boilers or the machinery itself, damage to other property, and business interruption (use and occupancy) losses.

Translation: Covers loss to boilers and other machinery, loss to property that is damaged because of boilers and other machinery, and lost profits and extra expenses that result because of the loss.

Business Income Insurance: Coverage designed to provide protection against losses resulting from a temporary shutdown because of fire or other insured peril. The insurance provides reimbursement for lost net profits and necessary continuing expenses.

Translation: It pays for lost profits and the bills you incur for extra expenses because of a shutdown.

Claim: Demand or obligation for payment as a result of a loss.

Translation: When you say to your insurer, “Pay up; I’ve had a loss.”

Combined Loss & Expense Ratio: Basically, a measure of the relationship between dollars spent for claims and expenses and premium dollars taken in. A ratio above 100 means that for every premium dollar taken in, more than a dollar went for losses and expenses.

Translation: A measure of what’s left over after the insurance company pays its bills and claims.

Coverage: The scope of protection provided under a contract of insurance; any of several risks covered by a policy.

Translation: The wide range of things that can happen to trigger your insurance coverage.

Crime Insurance: Employee dishonesty coverage insures against loss to the agency as a result of employee dishonesty or fraud. Money and securities coverage provides protection for losses occurring inside the insured's premises, or while outside the insured's premises, if the money and securities are in the care and custody of an employee. In addition, coverage applies over and above the limits purchased by an armored car service for loss in transporting the insured's money or securities. Coverage does not extend to any property other than money and securities. (The RMF provides coverage for both employee dishonesty and money and securities losses.)

Translation: Insurance protection from theft by an employee, and burglary and robbery of money and securities by non-employees.

Deductible: An amount that a policyholder agrees to pay, per claim or per accident, toward the total amount of an insured loss.

Translation: You owe this amount every time you have a loss.

Dividend: A return of part of the premium on participating insurance to reflect the difference between the premium charged and the combination of expense and investment experience.

Translation: You get part of what's left over after we pay our bills and your claims. What happens to the other part? We keep it for a rainy day. If it doesn't rain, you get it back too.

Exclusions: Specific conditions or circumstances listed in the policy for which the policy will not provide benefit payments.

Translation: The events that the policy does not cover (it's a short list).

Exposure: A situation, practice, or condition that might lead to loss.

Translation: The thing that caused the loss in the first place; e.g., fire or water.

First party claim: A demand for payment under an insurance policy made by a policyholder reporting an insured event directly to his carrier.

Translation: Best explained by an example: Agency (policyholder) files a claim with the RMF (insurer).

Frequency and Severity: Frequency is the number of times an incident occurs; severity is the monetary impact of a loss.

Translation: Losses that occur often (frequency); losses that may not occur often but are r-e-a-l-l-y expensive when they do occur (severity).

General Liability Insurance: General liability protects the insured against a claim alleging bodily injury or property damage. The coverage includes defense costs, awards, or settlements associated with lawsuits brought by third parties who are injured or sustain property damage as a result of the insured's operations or while on the insured's premises.

Translation: Covers aches and pains that you cause to others and damage to their property because of your inattention.

Insurance: An arrangement under which individuals, businesses, and other organizations or entities, in exchange for payment of a premium, are guaranteed compensation for losses resulting from certain perils under specified conditions.

Translation: It's a trade – you pay premium to the insurer and they pay your losses.

Loss: A reduction in value.

Translation: You have less than what you started out with unless adequately insured.

Loss Control: Any conscious action (or decision not to act) intended to reduce the frequency, severity, or unpredictability of accidental losses.

Translation: What you do to reduce accidents or to eliminate them.

Occurrence: An accident, including continuous or repeated exposure to substantially the same general, harmful conditions, that results in bodily injury or property damage during the period of an insurance policy.

Translation: A happening or an event.

Peril: A “cause” of loss; e.g., fire, vandalism, terrorism.

Translation: Something that made the loss occur.

Premium: The sum paid by a policyholder to keep an insurance policy in force.

Translation: It's what your insurance costs you.



Contact us for a premium quote!

Property Insurance: Property insurance is first-party coverage, as opposed to liability insurance, which is described as third-party coverage. [The RMF provides coverage for damage to the insured's (first-party) property caused by an insured peril. The coverage is written on an “all risk” of direct physical loss basis – coverage for all perils not specifically excluded by the policy. Examples of covered perils include, but are not limited to, damage caused by fire, windstorm, hail, collapse, theft, vandalism, flood, earthquake, business interruption, and other unforeseen causes of loss. The RMF property program also provides builder's risk coverage.]

Translation: Covers loss or damage to the property owned by your agency and property that your agency is legally responsible for that is owned by others.

Reinsurance: The acceptance by one or more insurers, called reinsurers, of a portion of the risk accepted by another insurer who has contracted for the entire coverage.

Translation: Insurance companies buy insurance too.

Risk Management: The practice of protecting an organization from financial harm by identifying, analyzing, and controlling risk at the lowest possible cost.

Translation: All the things that can be done to reduce or eliminate losses, such as improving housekeeping and transferring the liability by contract.

Risk: (1) The chance of loss; (2) The insured or property covered by a policy or application.

Translation: (1) The likelihood that a loss will occur; (2) the thing that is covered.

Self-Insured: Having a sound funding mechanism in place for loss settlements.

Translation: See definition of Uninsured.

Third Party: The claimant under a liability policy. So called because the person making the claim is not one of the two parties – insured and insurer – to the insurance contract.

Translation: We couldn't have said it better.

Tort: A civil wrong, as opposed to a criminal wrong, that is recognized by law as grounds for a lawsuit.

Translation: Example – a negligent act causing damage.

Uninsured: A party that is not insured.

Translation: Best explained by an example: You have no insurance so losses must be paid out of your agency's budget.



A Beautiful Dance
Perpich Center for Arts Education
Photo courtesy of the Perpich Center for Arts Education

Minnesota Zoo – learning adventures with the Zoomobile
Minnesota Zoological Garden
Photos courtesy of the Minnesota Zoological Garden

Perpich Center for Arts Education
“Sculpting” students for careers in
The Arts
Photo courtesy of Perpich Center
for Arts Education

MnDOT
“Watch out for the wet paint!”

“Fore!”
Bear Paw at Giant's Ridge



MnDOT . . . preparing for your winter fun.



DNR Fire Tower
Minnesota State Fairgrounds
Climbing your way to fun!



A greeting from Paul ~ Welcome Center
Baxter, Minnesota



Minnesota State Fair ~ a true “Classic”



Minnesota State Fair
Progress in Learning ~ The New Birthing Center



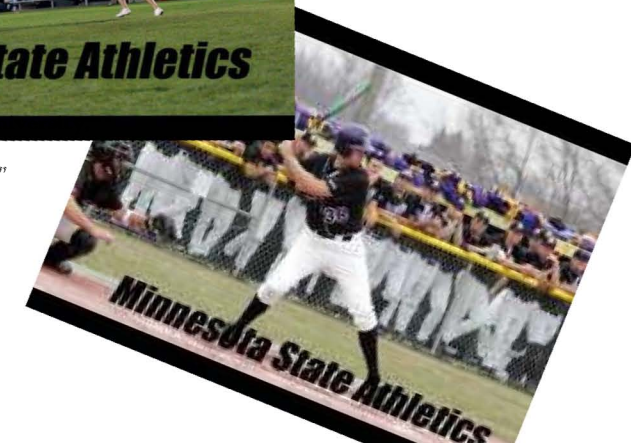
Visit the Veterans Memorial at
Ironworld Discovery Center; Chisholm, Minnesota



To Our Risk Management Fund Customers
“Thank You! Thank You Very Much!”



Mankato
“Go Team!”



Minnesota State Athletics

Involvement in Outside Public Projects

Not only does Risk Management have fun with its day-to-day operations, it also has the privilege of being involved with large public projects. Following is a list of those projects, their status, and how Risk Management is involved.



Hiawatha Light Rail in city of Minneapolis
Photo courtesy of Metro Transit

Hiawatha Light Rail

This project has been operating very successfully for over a year, but insurance issues that came up during construction still need to be monitored. At the end of this fiscal year, there were only a couple of workers' compensation claims still open and a builder's risk issue. At this time, the Hiawatha Risk Management Advisory Committee, made up primarily of Risk Managers affected by this project, such as Minneapolis, Bloomington, Metropolitan Airports Commission, and Met Council, continue to monitor activities and will do so until all claims and outstanding items are resolved.

Northstar Commuter Rail – Minneapolis to Big Lake

What is 40 miles long, travels at a speed of 79 mph, and is expected to come to towns near you in 2009? *Northstar Commuter Rail!* The Northstar Corridor is slated to run along Highway 10 from the Big Lake area to downtown Minneapolis. In FY06, the Minnesota Legislature approved \$60 million in bonding for this project and Northstar entered the final design phase. Pending 2007 approval of federal matching funds, Northstar is expected to be fully operational by 2009.

Since the state is the grantee for the project, the RMD is a member of the Northstar Risk Management Advisory Committee, which was established to address the varied exposures to loss during construction and operation of the commuter rail. In cooperation with MnDOT, the Met Council, the Northstar Corridor Development Authority, and other interested parties, the RMD evaluates and makes recommendations on how to best control potential exposures to loss. In most instances, risk transfer (insurance and contracts), risk retention (deductibles), and risk mitigation (loss control) are the principle options.

Since safety is a core value, a loss control professional will join the Advisory Committee in early 2007, ensuring that the proper emphasis is placed on project safety.

Republican National Convention Risk Management Advisory Committee

It won't take place until September of 2008, but an insurance committee made up of cities, counties, the Metropolitan Airports Commission, the Met Council, and the State have been busy working on establishing plans for insurance to cover this short, but highly visible, extravaganza. It takes a lot of planning to cover the insurance and other issues that develop from such a massive event. It is the stated mission that the Risk Management Advisory Committee for the Republican National Convention will support the Host Committee with the mutual objective of having a well-planned professional event held in Minnesota as the world looks on. It should be fun!

Minnesota Twins Ballpark

Last year, the Minnesota Legislature created the Minnesota Ballpark Authority which includes the Minnesota Twins and Hennepin County. As with other public projects, this project requires a Risk Management Advisory Committee (RMAC). The RMAC members include Hennepin County, the City of Minneapolis, the Met Council, the State of Minnesota, and the Executive Director of the Ballpark Authority. This project is just starting, but, when the 2010 baseball season starts, they will be yelling "play ball"! This project also has ties with the commuter rails since there will be Northstar and light rail stations. The Hiawatha Light Rail line is being extended to the ballpark. Construction of these stations will be under the auspices of the Minnesota Twins ballpark project.

Division Summary of Operations

In FY06, the RMD continued to provide four major areas of service to state departments, boards, bureaus, commissions, and component units of the state of Minnesota, as well as political subdivisions. Those services include:

- ◆ Managing the RMF which operates as the state's internal insurance company. The RMF provides property and casualty insurance coverages tailored to meet our customers' needs.
- ◆ Purchasing commercial insurance to meet customers' needs when the placement of insurance coverage in the RMF may not be appropriate or cost effective.
- ◆ Providing risk management consulting and training services on a wide variety of issues.
- ◆ Providing internal underwriting, loss control, and claims expertise that are dedicated to the unique needs of our customers.

The RMD annually develops a business plan for each line of insurance underwritten by the RMF. Each line of insurance is evaluated for the development of losses, adjusting expenses, reinsurance expenses, and administrative expenses.

An objective of the RMD is to maintain operating expenses well below the industry average for comparable insurance companies (as reported by A.M. Best in its annual publication *Aggregates and Averages*). The five-year performance of the RMF, compared to industry averages, as demonstrated in Exhibit 1, indicates that we have met our objective in each of the past five years, with all five years better than 40 percent lower than the industry. FY06's operating expense ratio, at 15.9 percent, is up slightly from last year; however, the RMF continues to experience a very stable expense ratio, resulting in a five-year savings of nearly \$4.5 million.

Exhibit 1 **Summary of Operations**

	FY02	FY03	FY04	FY05	FY06
Net Premium Written	\$5,585,401	\$5,911,569	\$6,309,145	\$6,996,519	\$6,453,114
Industry average operation expense ratio	30.5%	29.9%	29.5%	30.3%	30.0%
Projected industry average operation expense based on RMD's actual premium	\$1,703,547	\$1,767,559	\$1,861,198	\$2,119,945	\$1,935,934
Actual RMD operating expenses	\$ 950,542	\$1,029,334	\$ 941,969	\$ 968,275	\$1,025,712
RMD operating expense ratio	17.0%	17.4%	14.9%	13.8%	15.9%
Savings to clients	\$ 753,005	\$ 738,225	\$ 919,229	\$1,151,670	\$ 910,222
Five year total savings	\$4,472,351				

Exhibit 2

Self-Insurance Property and Casualty Underwriting Results

Premiums Earned by Line

	<u>FY03</u>	<u>FY04</u>	<u>FY05</u>	<u>FY06</u>
Auto Insurance				
Auto Liability	\$2,075,124	\$2,040,527	\$2,102,050	\$2,503,659
Auto Physical Damage	842,214	806,788	780,091	961,667
Garagekeeper's Legal Liability	34,456	33,743	33,500	30,668
Standard Commercial Insurance				
Property	\$4,187,342	\$4,437,164	\$4,696,156	\$3,822,477
Boiler & Machinery	152,662	154,573	167,778	88,577
General Liability	1,412,839	1,307,708	1,336,936	1,383,029
Crime	68,359	70,387	76,690	84,032
Other*	309,263	320,632	360,638	369,625
Total Premiums Earned	<u>\$9,082,859</u>	<u>\$9,171,522</u>	<u>\$9,553,839</u>	<u>\$9,243,734</u>
Less Reinsurance Ceded	\$3,206,085	\$2,903,662	\$2,605,036	\$2,845,774
Total Net Premiums Earned	5,876,774	6,267,860	6,948,803	6,397,960
Plus Unearned Premium	34,795	41,285	47,716	55,154
Total Net Premiums Written	<u>\$5,911,569</u>	<u>\$6,309,145</u>	<u>\$6,996,519</u>	<u>\$6,453,114</u>

Combined Loss and Expense Ratio (Before Dividends and IBNR)

	<u>FY03</u>	<u>FY04</u>	<u>FY05</u>	<u>FY06</u>
Auto Insurance				
Auto Liability	88%	71%	391%	74%
Auto Physical Damage	70%	70%	87%	79%
Garagekeeper's Legal Liability	42%	10%	14%	18%
Standard Commercial Insurance				
Property	16%	20%	11%	41%
General Liability	71%	35%	31%	14%
Boiler & Machinery	7%	102%	9%	10%
Crime	51%	10%	40%	40%
Other*	<u>53%</u>	<u>63%</u>	<u>52%</u>	<u>55%</u>
Combined Loss Ratio Before Reinsurance	48%	41%	105%	50%
Combined Loss Ratio After Reinsurance	74%	58%	77%	72%

* Other includes Inland Marine and Vendor Warranty

Financial Position Discussion

Exhibit 2 reflects that, in FY06, overall premiums earned decreased \$310K, which was the result of a very favorable 21 percent rate decrease in the property line. Earned premium for the property line decreased \$874K and premiums earned for other lines increased \$564K, resulting in a net decrease of \$310K.

Reinsurance costs have remained relatively stable over the last four years, with a high in FY03 of \$3,206K and a low in FY05 of \$2,605K. The reinsurance programs, as they are currently structured, have served their intended purpose of reducing the year-to-year volatility in the RMF's retained results.

In FY06, the increase in reinsurance cost of \$241K, and the decrease in the earned premium base of \$280K, largely accounted for the current year contribution to the \$544K reduction in Net Premiums Written from \$6,997K in FY05 to \$6,453K in FY06.

The gross combined loss and expense results for FY06 were very good, with a 50 percent first year development factor. Auto liability settled down from a poor FY05 of 391 percent gross combined ratio to a more realistic 74 percent in the current year. This was primarily due to the absence of the catastrophic losses that occurred in FY05. There is still a need to focus on the auto liability line loss control initiatives to realize better results and ultimately lower customer premium.

The results, after reinsurance, are indicative of the balancing impact a good reinsurance program has on the net numbers. The last four years have produced excellent net combined ratios that range from a high of 77 percent in FY05 to a low of 58 percent in FY04.

Exhibit 3 measures four important aspects of the RMF's operation. The net premium and loss results have been excellent. Dividends were not paid in FY03 due to adverse property results, but have been reinstated over the last three years. To date, more than \$12 million of dividends have been returned to our customers. Policyholder's surplus, the amount of dollars to pay future expenses and maintain the status of a viable fund, is at \$6.6 million after a 16.8 percent increase in FY06, primarily due to more favorable loss development.

The Net Premiums Written to Policyholder's surplus is at a very conservative .98:1. That is, for every 98 cents of Net Premiums Written, there is \$1 in Surplus to back it up. The insurance industry benchmark for this ratio is typically 2:1.

The performance of the RMF over the last four years has been exactly along the lines that were envisioned when it was originally set up. The RMF provides the State of Minnesota with an economically beneficial approach to effectively insuring the state's exposures at a very competitive cost.



Minnesota State University, Mankato - Ostrander-Student Memorial Bell Tower

Exhibit 3

RMF Performance by Fiscal Year

\$8,000,000					
\$7,000,000					
\$6,000,000					
\$5,000,000					Net Premium Written
\$4,000,000					Net Losses & Expenses
\$3,000,000					Policyholders' Surplus
\$2,000,000					Dividends Paid
\$1,000,000					
\$0					
	FY03	FY04	FY05	FY06	
	FY03	FY04	FY05	FY06	
Net Premium Written (NPW)	\$5,911,569	\$6,309,145	\$6,996,519	\$6,453,114	
Net Losses & Expenses	3,599,563	3,694,938	5,405,373	4,612,193	
Policyholders' Surplus	5,491,210	6,258,717	5,664,417	6,616,058	
Dividends Paid	0	1,668,215	1,729,215	1,361,289	
NPW to PH Surplus Ratio	1.08:1	1.01:1	1.24:1	.98:1	

Dividends

Good news for customers of the RMF! The FY06 dividend of \$1,036,430 was calculated as of June 30, 2006, and declared and paid in FY07. This brings the total dividends declared to \$12,432,923. FY06 dividends and total dividends from inception of the program, by line of insurance, are as follows:

	Calculated in FY06	Total Dividends
Auto Liability	\$ 375,589	\$6,658,364
General Liability	660,841	3,749,618
Property Insurance	0	2,024,941
	\$1,036,430	\$12,432,923



Dividends – Just like winning the Lottery

**State of Minnesota
Risk Management Fund
Statement of Net Assets
June 30, 2006**

ASSETS

	FY06	FY05
CURRENT ASSETS		
Cash	16,354,700.32	15,824,570.51
Accounts Receivable	26,087.00	17,966.81
Prepaid Expenses	800.00	0.00
Prepaid Reinsurance	0.00	0.00
Prepaid Billback Insurance	109,801.10	237,935.45
Reinsurance Recoverable	200,000.00	200,000.00
Due from Others – Nonoperating (Note 3)	17,517.37	0.00
Total Current Assets	<u>16,708,905.79</u>	<u>16,280,472.77</u>
NONCURRENT ASSETS		
Capital Assets (Note 3)	14,180.72	14,180.72
Less: Accumulated Depreciation	(13,002.00)	(8,274.00)
Due from Others – Nonoperating (Note 3)	17,918.57	0.00
Total Noncurrent Assets	<u>19,097.29</u>	<u>5,906.72</u>
TOTAL ASSETS	<u>16,728,003.08</u>	<u>16,286,379.49</u>

LIABILITIES

CURRENT LIABILITIES		
Accounts Payable	74,713.66	56,898.38
Salaries Payable	42,440.68	35,768.00
Claims Payable	4,938,151.02	5,405,209.00
Claims Payable – IBNR (Note 1)	4,728,727.00	4,668,362.00
Due to Other Funds (Note 6)	0.00	80,995.04
Due to Other Funds – Nonoperating (Note 6)	49,002.04	0.00
Dividend Payable	0.00	0.00
Unearned Premium – Self Insurance	55,154.00	47,716.00
Unearned Premium – Billback	144,631.00	266,997.00
Compensated Absences Payable (Note 5)	6,148.45	7,513.01
Total Current Liabilities	<u>10,038,967.85</u>	<u>10,569,458.43</u>
NONCURRENT LIABILITIES		
Due to Other Funds – Nonoperating (Note 6)	1,574.35	0.00
Compensated Absences Payable (Note 5)	71,402.51	52,503.71
Total Noncurrent Liabilities	<u>72,976.86</u>	<u>52,503.71</u>
TOTAL LIABILITIES	<u>10,111,944.71</u>	<u>10,621,962.14</u>
NET ASSETS (Note 7)		
Invested in Capital Assets, Net of Related Debt	1,178.72	5,906.72
Unrestricted Net Assets	6,614,879.65	5,658,510.63
TOTAL NET ASSETS	<u>6,616,058.37</u>	<u>5,664,417.35</u>

**State of Minnesota
Risk Management Fund
Statement of Revenues, Expenses & Changes in Net Assets
For Period Ended June 30, 2006**

	FY06 YTD	FY05 YTD
OPERATING REVENUES		
Insurance Premiums – Self Insurance	9,243,734.00	9,553,839.00
Insurance Premiums – Worker's Compensation	0.00	0.00
Insurance Premiums – Billback	1,149,247.00	1,127,097.00
Non-Insured Tort Claims	113,488.00	30,157.00
Consulting Services	1,750.00	1,838.00
Total Operating Revenues	<u>10,508,219.00</u>	<u>10,712,931.00</u>
OPERATING EXPENSES (Note 1)		
Claims – Self Insurance	3,583,167.41	4,754,608.41
Claims – IBNR	60,365.00	271,643.00
Salaries & Benefits	853,821.91	727,996.15
Rent	35,458.80	33,084.40
Advertising	0.00	1,449.88
Repairs	2,612.69	133.76
Insurance	1,134.00	366.00
Insurance Premium – Billback	1,149,247.00	1,127,097.00
Insurance Premium – Self Insurance	2,845,773.94	2,605,036.00
Printing	4,655.96	5,146.08
Professional Services – Adjuster	228,642.99	193,539.87
Professional Services – Broker	0.00	18,000.00
Professional Services – Legal and Other	5,249.29	51,262.22
Computer Services	66,737.12	5,577.49
Communications	38,136.01	48,464.45
Travel	8,329.35	4,413.63
Other Operating Costs	11,963.70	4,080.54
Memberships and Employee Development	1,476.00	2,880.00
Supplies	24,748.86	25,116.13
Depreciation	4,728.00	4,728.00
Indirect Costs	39,827.00	46,076.00
Total Operating Expenses	<u>8,966,075.03</u>	<u>9,930,699.01</u>
OPERATING INCOME (LOSS)	<u>1,542,143.97</u>	<u>782,231.99</u>
NONOPERATING REVENUES (EXPENSES)		
Interest Earnings	721,887.04	352,683.83
Policyholder Dividend Expense	(1,361,289.00)	(1,729,214.99)
Crisis Management Grant	0.00	0.00
Nonoperating Revenues (Note 3)	48,899.01	0.00
Total Non-Operating Revenues (Expenses)	<u>(590,502.95)</u>	<u>(1,376,531.16)</u>
CHANGE IN NET ASSETS	951,641.02	(594,299.17)
NET ASSETS, BEGINNING	5,664,417.35	6,258,716.52
Adjustment to Net Assets	<u>0.00</u>	<u>0.00</u>
NET ASSETS, ENDING	<u>6,616,058.37</u>	<u>5,664,417.35</u>

**State of Minnesota
Risk Management Fund 410
Footnotes to Financial Statements
For Period Ended June 30, 2006**

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Risk Management Internal Service Fund utilizes full accrual accounting, pursuant to M.S. § 16A.055.

The Fund provides automobile liability, general liability, automobile physical damage, property, boiler and machinery insurance on real and personal property, business interruption, and other insurance coverage to state agencies. Insurance coverage generally coincides with the fiscal year, and revenue is recognized over the period of coverage. Coverage was first issued beginning January 1, 1987. The Fund also purchases reinsurance from reinsurance companies to protect itself from catastrophic losses and the aggregation of losses. The Fund also purchases commercial insurance at the request of state agencies and bills those agencies at cost; these revenues and expenses are referred to as "Billbacks" and are pro-rated over the lives of the various policies; those revenues and expenses are identified separately.

Expenses are based on data received from the MAPS accounting system, and from subsidiary records.

An estimated liability has been included for claims incurred but not reported (IBNR).

This financial statement includes claims information known as of June 30, 2006 for claims incurred prior to July 1, 2006.

2. LEGISLATION AND AUTHORITY

The Risk Management Internal Services Fund was created by Minnesota Laws 1986, Chapter 455, Section 3.

3. DUE FROM OTHERS

In FY06, a settlement agreement was filed by the New York Attorney and an Amended Citation issued by the New York State Superintendent of Insurance to compensate eligible policyholder clients. The total compensation is \$53,607.36: Risk Management \$48,899.01, other state agencies and political subdivisions \$4,708.35. Risk Management has received \$16,576.42 to date and will receive additional payments of \$17,517.37 in FY07, \$8,959.29 in FY08, and \$8,959.28 in FY09 totaling \$35,435.94 as outstanding from the settlement.

4. CAPITAL ASSETS

	Acquisition Cost	Accrued Depreciation
Balances as of 07/01/05	14,180.72	(8,274.00)
Additions		
Deletions		
Write-offs		
Current Depreciation		<u>(4,728.00)</u>
Balances as of 06/30/06	<u>14,180.72</u>	<u>(13,002.00)</u>

5. COMPENSATED ABSENCES

State employees accrue vacation leave, sick leave, and compensatory leave at various rates within limits specified in their collective bargaining agreements. This leave is liquidated in cash only at the time of separation from state employment. The accumulated leave is shown as a liability.

	Short Term	Long Term
Compensated Absences, Beginning Balance	7,513.01	52,503.71
Increases in Compensated Absences	(1,364.56)	18,898.80
Decreases in Compensated Absences		
Compensated Absences, Ending Balance	<u>6,148.45</u>	<u>71,402.51</u>

6. DUE TO OTHER FUNDS

In FY03, the Department of Administration became a participant in a new Worker's Compensation plan. The previous Worker's Comp plan for the Department of Administration, administered by Risk Management, had a surplus balance. Funds are returned to the appropriate divisions based on the status of outstanding claims.

In FY05, the total Due To Other Funds of \$80,995.04 is the summation of the following:

\$10,315.26 to health and safety committee to purchase supplies and/or memberships
\$70,679.78 to PrintComm

In FY06, the total Due To Other Funds of \$50,576.39 is the summation of the following:

\$10,315.26 to health and safety committee to purchase supplies and/or memberships
\$37,147.78 to Comm.Media
\$ 3,113.35 to other state agencies and political subdivisions as a settlement agreement, filed by New York Attorney General & New York State Superintendent of Insurance for overcharges of brokerage fees. This amount will be returned as received from the settlement as follows: \$1,539.00 in FY07, \$787.68 in FY08, and \$786.67 in FY09.

7. NET ASSETS

During FY02, the State of Minnesota implemented new accounting standards, as prescribed by the Governmental Accounting Standards Board (GASB). The standards include revised statement formats which resulted in the change from retained earnings to net asset reporting. For historical cost comparison, the total net assets and the retained earnings have been reconciled as shown below.

Invested in Capital Assets, Net of Related Debt	1,178.72			
Unrestricted Net Assets	<u>6,614,879.65</u>			
Total Net Assets	<u>6,616,058.37</u>			
Schedule of Retained Earnings				
	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr
Beginning Retained Earnings	5,664,417.35	4,647,086.58	4,678,396.95	5,136,073.40
Prior Period Adjustment	0.00	0.00	0.00	0.00
Quarterly Net Income (Loss)	<u>(1,017,330.77)</u>	<u>31,310.37</u>	<u>457,676.45</u>	<u>1,479,984.97</u>
Ending Retained Earnings	4,647,086.58	4,678,396.95	5,136,073.40	6,616,058.37
Add: Capital Contributions	0.00	0.00	0.00	0.00
Reconciliation to Total Net Assets	<u>4,647,086.58</u>	<u>4,678,396.95</u>	<u>5,136,073.40</u>	<u>6,616,058.37</u>

**STATEMENT OF ACTUARIAL OPINION
REGARDING THE STATE OF MINNESOTA
ASSUMED AUTOMOBILE AND LIABILITY OTHER THAN AUTO RETAINED LIABILITIES
AS OF MARCH 31, 2006**

My name is Todd A. Gruenhagen and I am the Consultant and Managing Director of Green Hills Consulting, Inc., a Minnesota Corporation. Green Hills Consulting, Inc. is a worldwide actuarial & risk management consulting firm specializing in statistical solutions to actuarial analyses. I am an Associate of the Casualty Actuarial Society and a Member of the American Academy of Actuaries. I meet the qualification standards of the American Academy of Actuaries for rendering an actuarial opinion on property and casualty loss and loss adjustment expense reserves.

Green Hills Consulting, Inc. has been retained by the State of Minnesota as their consulting actuary. One of the services we provide to the State of Minnesota is the evaluation of liabilities assumed under Minnesota Statutes, Chapter 3, Section 376, Subdivision 4, for automobile liability and liability other than auto exposures.

All loss data utilized in this analysis was provided to me via the State of Minnesota, Risk Management Division. I relied on the accuracy and completeness of the loss data without audit or independent verification. Exposure information was provided via the State of Minnesota, Risk Management Division. If the data is inaccurate or incomplete, these estimates may need to be revised.

The State of Minnesota's retained automobile liability for accident periods July 1, 1994 through March 31, 2006, listed by accident period as of March 31, 2006 are as follows:

		(1)	(2)	(3)	(4) =(3)-(2)	(5) =(1)-(3)	(6) =(4)+(5)
Accident Period		Ultimates	Paid	Incurred	Case O/S	IBNR	Total
Beginning:	Ending:	@3/31/2006	Losses @3/31/2006	Losses @3/31/2006	Reserves @3/31/2006	Reserves @3/31/2006	Reserves @3/31/2006
7/1/1994	6/30/1995	1,888,553	1,888,553	1,888,553	-	-	-
7/1/1995	6/30/1996	914,374	914,374	914,374	-	-	-
7/1/1996	6/30/1997	1,671,600	1,670,316	1,670,316	-	1,284	1,284
7/1/1997	6/30/1998	1,722,500	1,718,662	1,718,662	-	3,838	3,838
7/1/1998	6/30/1999	907,200	902,872	902,872	-	4,328	4,328
7/1/1999	6/30/2000	1,363,700	1,285,854	1,359,755	73,900	3,945	77,846
7/1/2000	6/30/2001	1,483,000	1,402,842	1,451,744	48,903	31,256	80,158
7/1/2001	6/30/2002	1,141,000	950,389	1,114,923	164,534	26,077	190,611
7/1/2002	6/30/2003	1,423,200	987,765	1,324,142	336,377	99,058	435,435
7/1/2003	6/30/2004	1,367,600	773,204	1,077,229	304,025	290,371	594,396
7/1/2004	3/31/2005	3,698,800	1,137,548	3,238,334	2,100,786	460,466	2,561,252
7/1/2005	3/31/2006	1,646,325	293,306	1,159,779	866,473	486,546	1,353,019
Totals:		19,227,852	13,925,685	17,820,682	3,894,998	1,407,170	5,302,168

The State of Minnesota's retained liability, other than auto liability for accident periods July 1, 1994 through March 31, 2006, listed by accident period as of March 31, 2006, are as follows:

		(1)	(2)	(3)	(4)	(5)	(6)
					= (3)-(2)	= (1)-(3)	= (4)+(5)
Accident Period		Ultimates	Paid	Incurred	Case O/S	IBNR	Total
Beginning:	Ending:	@3/31/2006	Losses	Losses	Reserves	Reserves	Reserves
		@3/31/2006	@3/31/2006	@3/31/2006	@3/31/2006	@3/31/2006	@3/31/2006
7/1/1994	6/30/1995	56,902	56,902	56,902	-	-	-
7/1/1995	6/30/1996	150,753	150,753	150,753	-	-	-
7/1/1996	6/30/1997	242,445	242,445	242,445	-	-	-
7/1/1997	6/30/1998	210,722	210,722	210,722	-	-	-
7/1/1998	6/30/1999	205,200	185,845	203,344	17,500	1,856	19,355
7/1/1999	6/30/2000	104,800	102,050	102,050	-	2,750	2,750
7/1/2000	6/30/2001	554,400	526,668	545,889	19,222	8,511	27,732
7/1/2001	6/30/2002	653,800	604,814	608,560	3,746	45,240	48,986
7/1/2002	6/30/2003	877,800	612,581	844,792	232,211	33,008	265,219
7/1/2003	6/30/2004	502,400	131,697	422,077	290,380	80,323	370,703
7/1/2004	6/30/2005	591,000	46,739	223,712	176,972	367,288	544,261
7/1/2005	3/31/2006	603,675	15,336	42,702	27,365	560,973	588,339
Totals:		4,753,896	2,886,551	3,653,947	767,396	1,099,949	1,867,345

It is my opinion that the above estimated liabilities:

1. Are computed in accordance with commonly accepted actuarial loss reserving standards and methods and are fairly stated in accordance with sound actuarial principles.
2. Make a reasonable provision for all unpaid loss and allocated loss adjustment expense liabilities that the State of Minnesota assumes under Minnesota Statute 3.736, Subdivision 4 for automobile and liability other than auto exposures.
3. Are based on factors and data relevant to the State of Minnesota.

I believe that these reserves make a good and sufficient provision, in the aggregate, for all unpaid loss and allocated loss adjustment expense obligations of the State of Minnesota with respect to its retained liability exposures for the accident period July 1, 1994 through March 31, 2006. This opinion is based upon my best estimate of the ultimate loss and allocated loss adjustment expenses to be paid by the State of Minnesota and is based upon data available as of March 31, 2006.

Note that this estimate is based upon actuarial assumptions as to future contingencies deemed to be reasonable and appropriate under the circumstances. The reader of this Statement must realize that these projections involve estimates of future events and, as such, are subject to economic and statistical variations from the expected values. For these reasons, no absolute assurance can be given that the emergence of actual losses will correspond to the projections reflected in this report. However, I have not anticipated any extraordinary changes to the legal, social, or economic environment that might affect the reserve values. In today's environment, all entities are subject to the terrorist attack exposure. RMF's terrorist attack exposure cannot be reasonably estimated. Thus, only reserves excluding terrorist attacks are determined.

This opinion is provided to the State of Minnesota solely for the purpose of meeting its internal reporting obligations. Any other use is prohibited.

13 April, 2006
Date

/s/ Todd A. Gruenhagen
Todd A. Gruenhagen, ACAS MAAA
Green Hills Consulting, Inc.
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St. Paul, MN 55155-1401
Return service requested



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