Texas Association of School Boards Risk Management Fund

Financial Statements as of and for the Years Ended
August 31, 2017 and 2016
Independent Auditors' Report

TEXAS ASSOCIATION OF SCHOOL BOARDS
RISK MANAGEMENT FUND

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Report of Independent Auditors

The Board of Trustees
Texas Association of School Boards Risk Management Fund:

Report on the Financial Statements

We have audited the accompanying financial statements of the Texas Association of School Boards Risk Management Fund as of and for the years ended August 31, 2017 and 2016, and the related notes to the financial statements, which collectively comprise the basic financial statements listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in conformity with U.S. generally accepted accounting principles; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free of material misstatement, whether due to fraud or error.

Auditor's Responsibility

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

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

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Texas Association of School Boards Risk Management Fund at August 31, 2017 and 2016, and the changes in its financial position and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

Required Supplementary Information

U.S. generally accepted accounting principles require that the Management's discussion and analysis on pages 3 to 8 and the ten year claims development information and reconciliation of unpaid claims and claim adjustment expense liability by type of contract schedules on pages 24 to 28 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Ernst & Young LLP

November 3, 2017

MANAGEMENT'S DISCUSSION AND ANALYSIS
Texas Association of School Boards Risk Management Fund
Years Ended August 31, 2017 (Unaudited)
(See Independent Auditors' Report)

The Texas Association of School Boards Risk Management Fund (the "Fund") herein sets forth a narrative overview and analysis of its financial activities for the fiscal year ended August 31, 2017.

Overview of the Financial Statements

The Texas Association of School Board Risk Management Fund's financial statements consist of three components: 1) financial statements, 2) notes to the financial statements, and 3) required supplementary information. The financial statements present the results of operations from the following Fund programs: Workers' Compensation, Auto, Property, Liability and Unemployment Compensation.

Financial Highlights

Assets exceeded Fund liabilities at August 31, 2017, by $203.4 million and no amounts were designated as restricted as of the end of the year.

The statement of net position presents the Fund's net assets (total assets – total liabilities) as Net Position (Members' Equity). The Fund's governing Board of Trustees called for the use of Members' Equity to support operations for the year. Net position decreased by $9.4 million during the 2016-2017 fiscal year. The decrease to $203.4 million was primarily due to exceptionally high property claims during the year.

The Fund's investment portfolio continues to generate a steady source of income on which the Fund relies to support its operations. This financial strength helped in weathering the storms of the past year, as severe weather pummeled member properties. Despite these challenges, the Fund's investment portfolio is well-diversified to withstand the volatility in the financial marketplace and the Fund will continue to be a steady partner for its members.

Fund Accounting and Financial Statements

The Fund is a public entity risk pool created under the Texas Interlocal Cooperation Act and all of the Fund's programs are accounted for as an enterprise fund within the Governmental Accounting Standards Board (GASB) framework.

The Fund carries reserves for each program except Unemployment Compensation. The Fund's reserves include case-based reserves, incurred but not reported (IBNR) claims and unallocated loss adjustment expenses (ULAE). The Fund also carries reserves for certain claims where the Fund provided a layer of stop-loss coverage to self-funded workers' compensation members from September 1, 1988 to August 31, 1992. Reserves are established by management in consultation with the Fund's independent consulting actuary.

The Statement of Net Position presents information regarding all of the Fund's assets and liabilities, with the difference between the two being reported as Net Position. Over time, increases or decreases in Net Position may provide a useful indicator regarding how the Fund is meeting the needs and expectations of its members.

The Statement of Revenues, Expenses and Changes in Net Position presents the financial results of the Fund. This statement presents information showing how the Fund's Net Position changed during the most recent fiscal year. The Fund utilizes enterprise fund accounting and thus uses the accrual method of accounting. All changes in Net Position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenue and expenses are reported in this statement for some items that will result in cash flows in future fiscal periods (e.g. loss and loss adjustment expenses, accrued investment income and reinsurance premiums payable).

The Statement of Cash Flows presents the sources and uses of cash from operating activities, financing activities, and investing activities. This statement ends with the cash in the statements of net position. A reconciliation of operating income to cash provided by the operating activities is also presented. The basic financial statements begin on page 9.

Notes to the Financial Statements

The notes provide additional information that is integral to a full understanding of the financial information presented in the financial statements. The notes to the financial statements begin on page 12.

Financial Analysis for the Fund

The Statements of Net Position *– As of August 31, 2017, 2016, 2015*

Comparative Condensed Statements of Net Position
As of August 31, 2017, 2016, and 2015

	2017	2016	2015
Assets:			
Cash and investments	$ 324,666,752	$ 329,402,809	$ 337,707,807
Other current assets	12,644,053	15,364,545	9,526,905
Long-term assets	362,068	462,068	562,068
Total Assets	$ 337,672,873	$ 345,229,422	$ 347,796,780
Liabilities and equity:			
Current liabilities	$ 71,654,544	$ 68,949,328	$ 58,508,698
Long-term liabilities	62,649,194	63,543,868	65,170,874
Total Liabilities	134,303,738	132,493,196	123,679,572
Net Position:			
Members' Equity (Unrestricted)	203,369,135	212,736,226	224,117,208
Total liabilities and net position	$ 337,672,873	$ 345,229,422	$ 347,796,780

Cash and Investments

The Fund carried cash, cash equivalents and investments of $324.7 million at August 31, 2017, $329.4 million at August, 31, 2016, and $337.7 million at August 31, 2015. The Fund’s investments are made in accordance with the Fund’s Investment Policy, which is reviewed and approved annually by the Fund’s Board of Trustees. The Fund’s investments consist primarily of corporate and government bonds, mortgage backed securities, international debt and equity mutual funds.

Reserves

Reserves for losses and loss adjustment expenses were approximately $106.6 million at August 31, 2017, $105.6 million at August 31, 2016, and $100.2 million at August 31, 2015. Actuarial projected reserves increased by approximately $1.0 million during 2017. The majority of this increase is directly related to the developing loss experience in the Fund’s Property program.

The Fund discounts its workers' compensation reserves to reflect an estimate of anticipated investment earnings on accumulated contributions during the payout period of the reserves. The Fund discounts reserves due to the relatively low variability in the amount and timing of future loss payments. Accordingly, reserves are presented at net present value using a discount rate of 4% as of August 31 of each year. The reserve discount as of August 31, 2017, 2016, and 2015, was $13.6 million, $16.4 million, and $15.5 million.

Net Position – Members' Equity

Net Position (Members' Equity) decreased by approximately $9.4 million during 2016-2017, $11.4 million during 2015-2016, and $31.2 million during 2014-2015.The decrease during 2016-2017 was primarily due to exceptionally high property claims during the year.

As of August 31, 2017, there were no amounts of Net Position that the Fund's Board of Trustees had declared restricted as all such funds were determined necessary for operations of the Fund. At the end of the current fiscal year, Net Position totaled $203.4 million.

The Statement of Revenue, Expenses and Changes in Net Position *– Fiscal years ended August 31, 2017, 2016, and 2015*

Comparative Condensed Statements of
Revenues, Expenses and Changes in Net Position
For the Years Ended August 31, 2017, 2016, and 2015

	2017	2016	2015
Operating revenues:			
Gross contributions earned	$90,984,306	$ 82,597,057	$ 83,743,408
Other revenue	437,495	424,289	374,750
Stop-loss and reinsurance premiums	(14,136,491)	(15,083,249)	(14,349,010)
Total operating revenues	77,285,310	67,938,097	69,769,148
Non-operating revenues (expenses):			
Investment income – net of expenses	10,966,495	11,320,872	13,133,418
Realized and change in unrealized gains (losses) from investments	6,554,166	7,572,990	(12,295,126)
Total non-operating revenue	17,520,661	18,893,862	838,292
Total revenues	94,805,971	86,831,959	70,607,440
Operating expenses:			
Net incurred losses	65,825,464	60,211,549	66,309,268
Administrative and other expenses	38,347,598	38,001,392	35,482,290
Total operating expenses	104,173,062	98,212,941	101,791,558
Change in net position	(9,367,091)	(11,380,982)	(31,184,118)
Members' Equity -- Beginning of the year	212,736,226	224,117,208	255,301,326
Members' Equity -- End of year	$203,369,135	$ 212,736,226	$ 224,117,208

Contributions

Member contributions are the Fund’s main source of revenue and are recorded upon execution of the Interlocal Participation Agreement (IPA) and recognized as earned. These documents between the Fund and its members set forth the coverage terms, agreement period, required contribution, and the obligations of the parties.

For the fiscal years ended August 31, 2017, 2016, and 2015, the Fund reported earned contributions and Administrative-Services-Only (ASO) fees of $91.0 million, $82.6 million, and $83.7 million. Contributions increased for all program lines primarily due to increases in contribution rates.

Net operating revenue is calculated using program revenue, other revenue, and stop loss premiums expensed during the fiscal year. For the fiscal years ended August 31, 2017, 2016, and 2015, the Fund reported net operating revenue of $77.3 million, $67.9 million, and $69.8 million. Net operating revenue increased in 2017 primarily due to the increase of contributions for all program lines.

The Fund continues to operate in a very competitive market where participants offer generally flat rates. Though contributions increased, various factors will offset these increases to a certain degree. Growth in the workforce will result in larger contributions for the Workers' Compensation line of business, but healthcare expenses are also anticipated to increase. Contributions for the Auto and Property lines of business are expected to rise slightly due to changes in exposure, but such increases will be offset by lower rates due to an excess capacity in the insurance market place and also an increase in claim expenses due to rises in construction and repair costs and frequency of accidents.

Investment Income, realized and change in unrealized gains (losses) from investments

Investment income continues to contribute significantly to the Fund's overall financial strategy. Interest and dividend earnings on fixed investment securities compose a large part of investment income. The Fund marks to market all investments on a monthly basis. The Fund reports realized and unrealized gains or losses from investments as a component of the results from operations. The Fund earned $11.0 million in investment income (net of fees) for the year ended August 31, 2017, compared to $11.3 million for the year ended August 31, 2016, and $13.1 million for the year ended August 31, 2015. Total non-operating revenue includes the change in unrealized gains or losses, realized gains or losses, and interest and dividend earnings net of fees.

Program Expenses

As of August 31, 2017, 2016, and 2015, total expenses were $104.2 million, $98.2 million, and $101.8 million respectively. During the 2016-2017 fiscal year, the increase in expenses resulted from an increase in incurred losses for the Property, Liability and Automobile programs.

The Fund has no staff. Instead, it contracts with TASB for administration and management of its programs and it reports this expense as Program Administrative Fees. TASB performs marketing, underwriting, claims administration, loss prevention, financial operations, and other administrative and operational activities on behalf of the Fund. The Fund has a Service Agreement with TASB and pays TASB an administrative fee for TASB's responsibilities as outlined in the Service Agreement. The administrative fee is approved annually by the Fund's Board of Trustees and reimburses TASB's actual costs incurred for administration of the Fund's programs. The Fund incurred TASB administrative fees of $26.9 million, $26.1 million, and $24.0 million as of August 31, 2017, 2016, and 2015, respectively.

In addition to the Service Agreement for administration of the Fund's program, the Fund and TASB have entered into an Affinity and License Agreement. The Agreement recognizes the role that TASB played in creation of the Fund, and allows the Fund to use TASB's name and logo. The sponsorship and license fee was $1.8 million as of August 31, 2017, 2016, and 2015, and is reported as sponsorship fees.

TEXAS ASSOCIATION OF SCHOOL BOARDS
RISK MANAGEMENT FUND

STATEMENTS OF NET POSITION
AS OF AUGUST 31, 2017 AND 2016

	2017	2016
ASSETS		
Current assets:		
Cash and cash equivalents	$ 13,469,331	$ 16,842,543
Mutual funds	73,318,175	90,891,001
Fixed income securities	10,685,215	2,042,392
Contributions receivable	7,183,523	5,551,395
Stop loss coverage receivable	2,517,406	7,086,734
Accrued interest receivable	2,025,381	2,067,427
Investment Securities Sold	485,000	356,880
Prepaid expenses and other assets	432,744	302,109
Total current assets	110,116,775	125,140,481
Non-current assets:		
Fixed income securities	227,194,030	219,626,873
Other assets	362,068	462,068
Total non-current assets	227,556,098	220,088,941
TOTAL ASSETS	$ 337,672,873	$ 345,229,422
LIABILITIES AND NET POSITION		
Current liabilities:		
Reserve for losses and LAE at estimated net present value	$ 43,923,056	$ 42,278,393
Unemployment compensation claims payable	1,293,334	1,463,180
Unearned contributions - net of prepaid stop loss premiums	15,871,804	13,459,297
Checks payable on losses	2,781,637	2,851,496
Accrued expenses and other liabilities	7,784,713	8,896,962
Total current liabilities	71,654,544	68,949,328
Non-current liabilities:		
Reserve for losses and LAE at estimated net present value	62,649,194	63,293,868
Deposits from members	-	250,000
Total non-current liabilities	62,649,194	63,543,868
Total liabilities	134,303,738	132,493,196
Net Position:		
Members' Equity (Unrestricted)	203,369,135	212,736,226
TOTAL LIABILITIES AND NET POSITION	$ 337,672,873	$ 345,229,422

See notes to financial statements.

TEXAS ASSOCIATION OF SCHOOL BOARDS
RISK MANAGEMENT FUND

STATEMENTS OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEARS ENDED AUGUST 31, 2017 AND 2016

	2017	2016
OPERATING REVENUES:		
Member contributions	$ 88,071,035	$ 79,970,586
Administrative-service-only fees	2,913,271	2,626,471
Other revenue	437,495	424,289
Stop-loss and reinsurance premiums	(14,136,491)	(15,083,249)
Net operating revenue	77,285,310	67,938,097
OPERATING EXPENSES:		
Claims expense	70,422,392	91,457,378
Reinsurance recoveries	(4,596,928)	(31,245,829)
Net incurred losses	65,825,464	60,211,549
Unemployment compensation claim reimbursements	6,617,941	6,203,260
Program administrative fees	26,859,841	26,078,491
General and administrative	2,825,401	3,023,251
Contract service fees	112,443	775,687
Sponsorship and royalties	1,931,971	1,920,704
Total operating expenses	104,173,062	98,212,941
OPERATING (LOSS) INCOME	(26,887,752)	(30,274,844)
NON-OPERATING REVENUES:		
Investment Income — Net of expenses	10,966,495	11,320,872
Realized and change in unrealized gains (losses) from investments	6,554,166	7,572,990
NON-OPERATING REVENUE, NET	17,520,661	18,893,862
CHANGE IN NET POSITION	(9,367,091)	(11,380,982)
NET POSITION:		
Members' Equity (Unrestricted) Beginning of year	212,736,226	224,117,208
Members' Equity (Unrestricted) End of year	$ 203,369,135	$ 212,736,226

See notes to financial statements.

TEXAS ASSOCIATION OF SCHOOL BOARDS
RISK MANAGEMENT FUND

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED AUGUST 31, 2017 AND 2016

	2017	2016
CASH FLOWS FROM OPERATING ACTIVITIES:		
Cash from members	$ 91,514,685	$ 83,923,078
Cash from reinsurers	16,767,420	12,085,939
Claims paid, including unemployment compensation claims	(83,881,213)	(78,520,381)
Cash paid to reinsurers	(14,167,126)	(15,177,237)
Cash paid to vendors and TASB	(29,797,685)	(29,877,428)
Cash paid in royalties	(1,931,971)	(1,920,704)
Other uses of cash	(674,754)	2,380,146
Net cash used in operating activities	(22,170,645)	(27,106,588)
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of investments	(75,902,187)	(40,120,888)
Proceeds from sales and maturities of investments	83,691,078	65,663,339
Investment income	11,008,542	11,320,872
Net cash provided by investing activities	18,797,433	36,863,323
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(3,373,212)	9,756,735
CASH AND CASH EQUIVALENTS:		
Beginning of year	16,842,543	7,085,808
End of year	13,469,331	16,842,543
RECONCILIATION OF OPERATING (LOSS) INCOME TO NET CASH USED IN OPERATING ACTIVITIES:		
Operating (loss) income	(26,887,751)	(30,274,844)
Adjustments to reconcile net excess of revenues over expenses to net cash used in operating activities:		
(Increase) decrease in contributions receivable	(1,632,128)	363,485
(Increase) decrease in stop-loss coverage receivable	4,569,328	(5,914,864)
(Increase) decrease in prepaid expenses and other assets	(30,635)	(93,988)
(Decrease) increase in deposits from members	(250,000)	-
(Decrease) increase in unearned contributions, net of stop-loss premiums	2,412,507	962,536
(Decrease) increase in checks payable on losses	(69,859)	399,224
(Decrease) increase in reserve for losses and loss adjustment expenses at estimated net present value	999,989	5,366,160
(Decrease) increase in unemployment compensation claims payable	(169,847)	129,847
(Decrease) increase in accrued expenses and other liabilities	(1,112,249)	1,955,857
NET CASH USED IN OPERATING ACTIVITIES	$ (22,170,645)	$ (27,106,588)
NONCASH ACTIVITIES		
Change in unrealized gains (losses) from investments	$ 6,766,190	$ 7,599,965

1. GENERAL STATEMENT

The Texas Association of School Boards Risk Management Fund (the "Fund") is as a public entity risk-sharing pool composed of five separate fund programs, which were established by members of the Texas Association of School Boards, Inc. (TASB). The workers' compensation and unemployment compensation programs were created in 1974 and 1977, respectively. The auto, property, and liability programs were created in 1981. These individual programs were merged in April 1997 with the TASB Workers' Compensation Self-Insurance Fund and renamed the Fund. Each program was created in accordance with the Interlocal Cooperation Act, Chapter 791 of the Texas Government Code, and operates in accordance with the appropriate rules, regulations, and laws of the state of Texas.

The general objective of all programs include (a) formulating, developing, and administering services for its membership; (b) obtaining lower costs for workers' compensation, auto, property, and liability coverage; and (c) developing a comprehensive safety and loss control program. Members of the Fund participate in the Fund through Interlocal Participation Agreements (IPA). The Fund operates as a risk-sharing pool by Members choosing to share their risk exposures with other members of the Fund or, in the case of the workers' compensation or unemployment compensation programs, participate as administrative-services-only (ASO) members whereby they fund their own claims and pay the Fund for administrative and loss control services. Approximately 1,050 school districts, education service centers, cooperatives, and community colleges participate in one or more of the Fund's programs.

The Fund is composed of five programs: Workers' Compensation, Auto, Liability, Property and Unemployment Compensation programs, which have been combined in the accompanying financial statements.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of Accounting and Presentation — The Fund prepares its financial statements using the accrual basis of accounting. The Fund is subject to the pronouncements of the Governmental Accounting Standards Board (GASB) and accounts for its activities as an enterprise fund. This enterprise fund is a single reporting entity and does not have component units; therefore, no separate component unit financial statements are presented.

Income Taxes — The Fund is exempt from federal income tax under Section 115 of the Internal Revenue Code. Accordingly, the accompanying financial statements do not include a provision or a liability for federal income taxes.

Member Contributions — Contributions receivable are established as of the coverage date for the full annual contribution, net of deductible credits. Such contributions are earned on a pro-rata basis over a 12-month period.

The Fund's contributions are developed annually with assistance from the Fund's actuary and are based on projected claims and expense costs. The funding methodology utilized by the Fund is approved annually by the Fund's Board of Trustees.

Contribution Deficiency — A contribution deficiency should be recognized when the sum of expected claim costs, including incurred but not reported claims, and all expected claim adjustment expenses exceeds related unearned contributions. When determining the existence or absence of a contribution deficiency, the Fund does not consider anticipated investment income. At August 31, 2017 and 2016, a contribution deficiency for the Fund did not exist.

Cash and Cash Equivalents — For purposes of financial statement presentation, the Fund considers cash, money market mutual funds, and debt securities with original maturities of less than 90 days at date of purchase as cash and cash equivalents.

Investments — Investments are carried at fair value. All investment income and changes in the fair value of investments are reported as non-operating revenue in the statements of revenues, expenses and changes in net position. Changes in the fair value of investments include both realized and unrealized gains and losses on investments.

Unemployment Compensation Claims Payable and Checks Payable on Losses — The unemployment compensation claims payable is reported separately on the statement of net position from checks payable on losses. Checks payable on losses correspond to claim checks outstanding from the workers' compensation, auto, liability, and property programs. Unemployment compensation claims payable represent the July and August claims liability due to the Texas Workforce Commission (TWC) on behalf of unemployment program members.

Unemployment compensation claim reimbursements are expensed as incurred for the unemployment compensation program. These expenses are shown separately from losses paid in other programs on the statements of revenues, expenses and changes in net position. However, revenue is included in member contributions and administrative-services-only fees and totaled $10,531,106 and $10,197,932 for the years ended August 31, 2017 and 2016, respectively.

Revenues and Expenses — The Fund distinguishes operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services in connection with the Fund's principal ongoing operations. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses. Sponsorship and royalties represent fees paid to TASB for the use of its name and other intellectual property. Royalties are also paid to the Texas Association of School Administrators (TASA) for its endorsement.

Other Revenue — Other revenue for fiscal year 2016–17 consists primarily of revenue from the Texas Municipal League Intergovernmental Risk Pool (TML-IRP) for preauthorization and medical review services provided by the Fund.

Net Position — Net Position (Members' Equity) consists entirely of retained earnings, none of which is restricted. The Fund refers to this balance internally as Members' Equity.

Reserve for Losses and Loss Adjustment Expenses — Reserve for losses and loss adjustment expenses is a total of case estimates for losses on claims reported, estimates of losses incurred but not reported at year-end, and an estimate of unallocated loss adjustment expense (ULAE), less amounts expected to be ceded to reinsurers.

The Fund discounts reserves for only the workers' compensation program. Total undiscounted reserves (i.e., case-basis reserves plus incurred but not reported (IBNR) reserves) for all lines of business were $120,154,969 and $122,019,777 at August 31, 2017 and 2016, respectively. Total net discounted reserves (i.e., case-basis reserves plus IBNR reserves) at August 31, 2017 and 2016, totaled $106,572,250 and $105,572,261, respectively.

The estimates of reserves are also subject to the effects of the nature of the risks underwritten, the inherent difficulty in estimating the ultimate costs of fully developed claims and trends in loss severity and frequency. Specifically, workers’ compensation reserves are subject to state legislation and medical inflation. For these reasons, the ultimate amount of losses and related loss adjustment expenses may vary significantly from the estimated reserves recorded in the financial statements. Although considerable variability is inherent in such estimates, management records the reserves based on actuarial valuations and believes that the reserve for losses and loss adjustment expenses is adequate. The estimates are continually reviewed and adjusted as necessary as experience develops or new information becomes known; such adjustments are included in current operations.

Stop Loss (Reinsurance) – Prospective reinsurance premiums, losses, and loss adjustment expenses are accounted for on a basis consistent with those used in accounting for the original policies issued and the terms of the reinsurance contracts.

3. CASH, CASH EQUIVALENTS, AND INVESTMENTS

Under provisions of the Fund’s investment policy and guidelines, the Fund may invest in the following types of instruments:

a. Obligations of the U.S. government or its agencies and instrumentalities

b. Dollar-denominated fixed-income securities of U.S. and foreign issuers

c. Mortgage pass-through and collateralized mortgage obligations

d. Asset-backed securities

e. Global and international bond funds

f. Equity funds

g. Dollar-denominated money market instruments including, but not limited to, certificates of deposit, commercial paper, bankers’ acceptances, time deposits, repurchase and reverse-repurchase agreements, floating-rate instruments, U.S. money market funds, and short-term bank investment funds, and

h. Public funds investment pools

The investment portfolio is diversified to reduce the risk of loss of investment income from over-concentration of assets. Pursuant to the Fund’s Investment Policy, the Fund strives to maintain a portfolio mix consisting of 65% investment-grade fixed income securities, 10% high-yield securities, 10% foreign securities, and 15% equity funds. The Fund does not intend to hold securities until maturity. Securities are reported on the statement of net position at fair value, and temporary changes in the fair value of the securities are recognized as unrealized gains and losses and reported as a component of non-operating revenue. Recorded fair values are based upon quoted prices in actively traded markets. For the years ended August 31, 2017 and 2016, the Fund recognized an unrealized net gain of $6,766,190 and $7,599,965, respectively, on the investment portfolio.

The original cost and estimated fair values, based on published market rates and dealer quotes, of instruments in the Fund's investment portfolio are reflected below:

	Original Cost	Gross Unrealized Gain	Gross Unrealized Loss	Estimated Fair Value
August 31, 2017:				
U.S. government obligations	$ 4,925,244	$ 73,806	$ -	$ 4,999,050
U.S. government agency obligations	17,167,087	361,541	(206,913)	17,321,715
International obligations	977,925	-	(155,267)	822,658
Corporate debt securities	137,713,061	3,735,782	(2,283,416)	139,165,427
Mortgage-backed securities	75,768,433	571,843	(769,880)	75,570,396
Global bond fund	16,108,871	-	(1,014,683)	15,094,188
Stock index fund	42,074,631	16,149,356	-	58,223,987
	$ 294,735,252	$ 20,892,328	$ (4,430,159)	$ 311,197,420
August 31, 2016:				
U.S. government obligations	$ 2,970,948	$ 76,272	$ -	$ 3,047,220
U.S. government agency obligations	17,167,087	568,344	(122,130)	17,613,301
International obligations	977,925	-	(117,897)	860,028
Corporate debt securities	141,246,154	4,554,779	(2,317,309)	143,483,624
Mortgage-backed securities	56,674,212	647,089	(656,209)	56,665,092
Global bond fund	37,390,893	-	(4,658,672)	32,732,221
Stock index fund	46,339,690	12,632,002	(812,912)	58,158,780
	$ 302,766,909	$ 18,478,487	$ (8,685,129)	$ 312,560,266

Deposits — Demand deposits at August 31, 2017 and 2016 are $198,308 and $564,539, respectively. At August 31, 2017 and 2016, $13,271,023 and $16,278,004, respectively, is held in money market mutual funds, invested with Dreyfus or held by Wells Fargo, the Fund's investment custodian, to invest by Conning, Inc., the Fund's investment manager.

Investment Risk Factors –There are many factors that can affect the value of investments. The Fund is exposed to the following risks: custodial credit risk, interest rate risk, credit risk, concentration of credit risk, and foreign currency risk.

Custodial Credit Risk — Deposits are exposed to custodial credit risk if they are not covered by depository insurance and the deposits are uncollateralized, collateralized with securities held by the pledging financial institution, or collateralized with securities held by the pledging financial institution's trust department or agent, but not in the depositor-government's name.

The balance of $198,308 in demand deposits as of August 31, 2017, is insured by the financial institution. The Fund is not subject to the Public Funds Investment Act or the Public Funds Collateral Act and is therefore not eligible to receive collateralization of money in depository institutions.

Investments are exposed to custodial credit risk if the securities are uninsured or not registered in the name of the Fund, and are held by either the counterparty, or the counterparty's trust department or agent but not in the Fund's name. The Fund utilizes the services of external investment portfolio managers. All of the Fund's investments are registered and held in the Fund's name at August 31, 2017 and 2016, and are not, therefore, exposed to custodial credit risk.

Interest Rate Risk – Interest rate risk is the risk that the value of fixed income securities will decline because of rising interest rates.

The fair value of investments at August 31, 2017 and 2016 is shown below by contractual maturity using the segmented time distribution method. Expected maturities may differ from contractual maturities because borrowers may have the right to prepay obligations without call or prepayment penalties.

	Estimated Fair Value	
	August 31, 2017	**August 31, 2016**
Due in one year or less:		
Corporate debt securities	$ 7,857,632	$ 2,042,392
International obligations	822,658	-
U.S. government agency obligations	2,004,925	-
Total due in one year or less	10,685,215	2,042,392
Due after one year through five years:		
U.S. government obligations	4,999,050	3,047,220
U.S. government agency obligations	9,377,763	10,494,434
International obligations	-	860,028
Mortgage-backed securities	6,557,508	5,472,189
Corporate debt securities	60,508,117	69,120,839
Total due after one year through five years	81,442,438	88,994,710
Due after five years:		
U.S. government agency obligations	5,939,026	7,118,867
Mortgage-backed securities	69,012,888	51,192,903
Corporate debt securities	70,799,679	72,320,393
Total due after five years	145,751,593	130,632,163
Total fixed income securities	237,879,246	221,669,265
Mutual funds -- global	15,094,188	32,732,221
Stock index fund	58,223,987	58,158,780
Total due after five years	73,318,175	90,891,001
Total fixed income securities and mutual funds	$ 311,197,421	$ 312,560,266

Credit Risk —Fixed income securities are subject to credit risk, which is the chance that a bond issuer will fail to pay interest or principal in a timely manner, or that negative perceptions of the issuer's ability to make these payments will cause security prices to decline. The circumstances may arise due to a variety of factors such as financial weakness, bankruptcy, litigation and/or adverse political developments. Credit risk is measured by a nationally recognized credit rating agency. US government or obligations explicitly guaranteed by the US government are not considered to have credit risk and do not require disclosure of credit quality. The following table shows the credit ratings as of August 31, 2017 and 2016, for each investment type.

	August 31, 2017			August 31, 2016		
		Fair Value	S&P Rating		Fair Value	S&P Rating
U.S. government obligations	$	4,999,050	NA	$	3,047,220	NA
U.S. government agency obligations		14,228,104	AAA - A-		16,244,427	AAA - A-
U.S. government agency obligations		1,748,638	BBB+			
U.S. government agency obligations		1,344,973	NR		1,368,874	NR
International obligations		822,658	BB		860,028	BB+
Corporate debt securities		40,174,173	AA+ - A-		44,740,370	AA+ - A-
Corporate debt securities		93,140,429	BBB+ - B-		96,799,654	BBB+ - B-
Corporate debt securities		5,850,825	NA		1,943,600	NA
Mortgage-backed securities		16,238,340	AAA - A-		17,214,979	AAA
Mortgage-backed securities		59,332,056	NA		39,450,113	NA
Global bond fund		15,094,188	NA		32,732,221	NA
Stock index fund		58,223,987	NR		58,158,780	NR
	$	311,197,421		$	312,560,266	

Concentration of Credit Risk – Concentration of credit risk is the risk associated with a lack of diversification, or having too much invested in a few individual issuers, thereby exposing the organization to greater risks resulting from adverse economic, regulatory, geographic, or credit developments.

As of August 31, 2017 and 2016, there were no investments in issuers, excluding mutual funds and U.S. government obligations that represent 5% or more of the total investments.

Foreign Currency Risk — Foreign currency risk is the risk that fluctuations in the exchange rate will adversely affect the value of investments denominated in a currency other that the U.S. dollar. At August 31, 2017 and 2016, the Fund had $15,094,189 and $32,732,221, respectively in a global bond mutual fund invested with Templeton Global that was denominated in various currencies. According to the Fund's Investment Policy, the Fund seeks to have investments of 10% of its total portfolio in a global bond mutual fund denominated in foreign currencies, but can have as much as 15% of the total portfolio invested in non-dollar denominated currencies at any time.

Fair Value Measurements –

The Fund categorizes its fair value measurements within the fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value into broad levels as follows:

Level 1 – Valuation is based upon quoted prices in active markets for identical securities

Level 2 – Inputs to the valuation methodology include:

- Quoted prices for similar assets in active markets;
- Quoted prices for identical or similar assets in inactive markets;
- Inputs other than quoted prices that are observable for the asset;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means

Level 3 – Valuation is based upon significant unobservable inputs (including the Fund's own assumptions determining the fair value of investments).

The fair values of investments are measured using quoted market prices or dealer quotations, when available. When quoted market prices are not available, fair value is measured using quoted market prices for similar securities. The asset's classification within the fair value hierarchy is based on using the lowest level of input that is significant to the fair value measurement. The valuation techniques used by the Fund maximize the use of observable inputs and minimize the use of unobservable inputs.

The following table sets forth by level, within the fair value hierarchy, the Fund's investments at fair value as of August 31, 2017 and 2016:

	Quoted Prices in Active Markets (Level 1)	Significant Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Totals
August 31, 2017:				
U.S. government obligations	$ 4,999,050	$ -	$ -	$ 4,999,050
U.S. government agency obligations	-	17,321,715	-	17,321,715
International obligations	-	822,658	-	822,658
Corporate debt securities	-	139,165,427	-	139,165,427
Mortgage-backed securities	-	75,570,396	-	75,570,396
Global bond fund	15,094,188	-	-	15,094,188
Stock index fund	58,223,987	-	-	58,223,987
	$ 78,317,225	$ 232,880,196	$ -	$ 311,197,421
August 31, 2016:				
U.S. government obligations	$ 3,047,220	$ -	-	$ 3,047,220
U.S. government agency obligations	-	17,613,301	-	17,613,301
International obligations	-	860,028	-	860,028
Corporate debt securities	-	143,483,624	-	143,483,624
Mortgage-backed securities	-	56,665,092	-	56,665,092
Global bond fund	32,732,221	-	-	32,732,221
Stock index fund	58,158,780	-	-	58,158,780
	$ 93,938,221	$ 218,622,045	$ -	$ 312,560,266

Investments in U.S. Treasury securities or mutual fund investments were recorded using Level 1 fair values based on observable quoted market prices from national security exchanges.

Prices for government agency, municipal, corporate, mortgage backed, and asset backed securities of the Fund are based on observable market data for the same or similar securities, including quoted prices in markets that are not active, or matrix pricing or other similar techniques that use observable market inputs, and, consequently, are classified as Level 2.

4. STOP-LOSS AGREEMENTS

The Fund has entered into stop loss and/or reinsurance agreements to reduce its exposure to catastrophic or higher than expected claim costs. Each of the Fund’s programs, except unemployment compensation, has its own stop-loss agreement in place with various terms, conditions, and levels of retention. The

Fund's Interlocal Participation Agreements state that the Fund is not responsible for any payment or any obligations to the program participant from any reinsurer, stop-loss carrier, or excess coverage provider. Based on its assessment of the creditworthiness of its reinsurers, management believes that such events are not likely to occur.

At August 31, 2017 and 2016, stop loss recoverable of $15,712,818 and $23,523,957, respectively, have been deducted from the reserve for losses and loss adjustment expenses. As of August 31, 2017 and 2016, the Fund has also recorded stop-loss reimbursements receivable of $2,517,406 and $7,086,734, respectively, on claims paid by the Fund.

5. ADMINISTRATIVE-SERVICES-ONLY MEMBERS

The Fund provides claims, loss control, and risk management services for certain self-insured members in exchange for an administrative fee. Some former ASO members in the workers' compensation program maintain deposits with the Fund to cover anticipated claim payments. At August 31, 2017 and 2016, the Fund held deposits of $0 and $250,000, respectively.

The Fund assumed a layer of stop-loss coverage for certain workers' compensation ASO districts from September 1, 1988 to August 31, 1992. Reserves as of August 31, 2017 and 2016, include estimated ultimate ASO losses of $1,763,641 and $1,846,494, respectively.

6. RELATED-PARTY TRANSACTIONS

The Fund has entered into the following agreements with TASB, whereby TASB provides services related to the administration of the Fund. As administrator of the Fund, TASB significantly influences its management and operating practices and is a related party to the Fund.

· TASB provides administration and management services of the Fund's programs. Services include, but are not limited to, overall program management, claims administration, marketing, billing and collecting contributions, cash management, planning, underwriting, and loss control. An administrative service agreement with TASB was entered into effective September 1, 2016, and remains in effect for a period of 60 months. Either party may terminate the agreement with notice of 180 days.

  The Fund paid TASB approximately $26,859,841 and $26,078,491 for such services for each of the years ended August 31, 2017 and 2016, respectively. As of August 31, 2017, the amount paid is net of a receivable for $140,159 for overpayment of the TASB administrative fee for the 2016-2017 fiscal year. This receivable, which is reported in Prepaid Expenses and Other Assets, was paid in full in October 2017.

· The Fund and TASB have a sponsorship and royalty agreement which gives the Fund use of certain intellectual assets, i.e., TASB's name and logo. The Fund incurred $1,800,000 in these fees to TASB for the years ended August 31, 2017 and 2016.

7. RESERVE FOR LOSSES AND LOSS ADJUSTMENT EXPENSES

Management establishes a liability for losses based primarily upon consultation with its independent actuary. These loss reserves are based upon the accumulation of (i) case base estimates for losses and expenses on claims reported and in process of settlement, (ii) estimates of additional reserves for reported claims based on statistical analyses, and (iii) estimates of losses and expenses incurred but not reported based upon past experience. These reserves have been reduced by amounts anticipated to be recovered from stop-loss agreements, deductibles, and a discount to reflect the present value of the estimated reserve for the workers' compensation program. The estimates represent the ultimate cost of settling claims, including the effects of inflation and other societal and economic factors. Adjustments to these estimates are charged or credited to operations in the period they become known. Due to the nature of risks underwritten, such estimates of reserves could be more or less than the amount ultimately paid upon settlement of the claims.

The Fund records its workers' compensation reserves for losses and loss adjustment expenses at estimated net present value (discounted basis). The Fund's accounting policy is to consider future investment income when the earning asset base is equal to or greater than the anticipated ultimate unpaid claims liability at estimated net present value. Reserves are discounted using interest rates that are reasonable considering the Fund's historical investment earnings. For 2017 and 2016, a discount rate of 4.0% has been used in the calculation, resulting in discounts for the workers' compensation program of $13,582,719 and $16,447,516, respectively.

The schedule on the following page represents changes in reserves for losses during the years ended August 31, 2017 and 2016. This schedule indicates that overall, during the 2016-17 and 2015-16 fiscal years, the Fund experienced favorable development on prior-year estimated total losses and loss adjustment expenses, net of stop-loss recoverable. This resulted from payments and development for prior years being less than previously projected.

	Changes in Reserve	
	Year Ended August 31, 2017	Year Ended August 31, 2016
Reserve for losses and LAE - beginning of fiscal year	$ 105,572,261	$ 100,206,101
Net incurred claims and claim adjustment expenses:		
Provision for covered events of the current fiscal year	79,923,464	77,803,666
Decrease in provision for covered events of prior fiscal years	(16,962,795)	(16,612,513)
Change in estimated future investment income	2,864,796	(979,604)
Net incurred claims and claim adjustment expenses	65,825,465	60,211,549
Net payments:		
Claims and claim adjustment expenses attributable to covered events of current fiscal year	31,966,093	27,179,252
Claims and claim adjustment expenses attributable to covered events of prior fiscal years	32,859,383	27,666,137
Net payments	64,825,476	54,845,389
Reserve for losses and LAE - end of fiscal year	$ 106,572,250	$ 105,572,261

8. OTHER ASSETS – LONG-TERM

This item represents an equity contribution to the Fund's reinsurer Government Entities Mutual (GEM). Related to the equity contribution, GEM started providing liability coverage to the Fund effective December 2003. The Fund is eligible to recover its equity after 5 years and based on the sole discretion of GEM's Board of Directors. The fund accounts for this equity contribution under the cost method. During 2015, the Fund requested return of its contributed capital of $500,000, which was approved by GEM's board of directors and will be returned on a ratable basis of $100,000 per year which started in December 2015.

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