WCRA®

2011 ANNUAL REPORT

Workers'
Compensation
Reinsurance
Association®

To Our Members

The WCRA's financial recovery continued in 2011. The Association's 2010 year-end deficit of $59 million was reduced to $8 million as of December 31, 2011. Over the last three years, we have reduced our balance sheet deficit by $416 million. Three factors have contributed to our financial improvement: excellent investment returns, assessments, and reductions in loss reserves.

Investments: While the Association's investment portfolio earned a disappointing 1 percent return in 2011, the annualized return for the last three years has been 14 percent. Our discount rate and annual assumed rate of return is 7 percent, so investment returns above that percentage improve the Association's capital position. Since the cataclysmic market declines of 2008, our superior investment returns have contributed $169 million toward the reduction of our balance sheet deficit.

Assessments: The Surplus Distribution Recovery Program (Program) of assessments was approved in 2009 for the specific purpose of eliminating the Association's deficit and rebuilding our capital base. It is doing so by recovering a portion of the $1.2 billion the WCRA previously distributed to members and workers' compensation policyholders. Since the Program was approved, assessments have contributed $137 million toward reducing our deficit.

Loss Reserve Reductions: Our actuaries are charged with projecting what our long-term claim liabilities will be decades into the future. Based on careful economic analysis and the recommendations of the WCRA Actuarial Committee, the Board of Directors establishes parameters for the work of the actuaries by regularly reviewing and adopting economic assumptions. For example, the discount rate is set at 7 percent; the general inflation rate assumption is 2.8 percent; and the medical escalation rate is 7.5 percent. Variations from these assumptions can have a significant impact on our loss reserve requirements, which in turn can substantially affect our capital position. In recent years, medical costs have trended lower than our 7.5 percent medical escalation rate assumption, which has in turn reduced our reserve requirements. As a result, over the last three years, the Board has approved a reduction of $122 million in loss reserves, which produced a corresponding reduction in our deficit.

Looking ahead, the Board of Directors has approved the continuation of the Program in 2012, which is expected to add $54 million to capital for the year. The Board will decide whether to continue the Program in 2013 and 2014 based on the Association's future financial condition. Any investment returns that exceed the 7 percent assumed rate will also add to capital. Further, if reserve requirements continue to trend lower, any additional reserve reductions approved by the Board would also improve the WCRA's capital position.

During the process of considering the Program in 2009, our members, as well as the Commissioner of Commerce, clearly indicated that the WCRA should build a strong enough capital base to withstand future financial shocks and avoid future assessments. The Board of Directors agrees and will continue to focus on strengthening the Association's financial position.

In addition, the annual premiums members will have to pay for the WCRA's statutory unfunded liabilities are expected to dramatically accelerate in the coming years. If our capital position permits, the Association intends to explore with its members, regulators, and the Legislature the possible elimination of the prefunded limit. Such an action would likely result in significant long-term benefit for WCRA members.

During 2012, the Association will continue the process of upgrading its information systems. More tools will be developed to better enable WCRA members to manage their WCRA claims and premium transactions. For self-insurer members, new reference materials and tools will be developed to assist them with basic exposure-related reporting requirements. In addition, a new, more user-friendly website with increased content is expected to be in place by midyear.

We look forward to working with all of our members into the future, and encourage you to contact us with any suggestions you have as to how we can better serve you.

Carl W. Cummins III
President and CEO

Stuart C. Henderson
Board Chair

Overview

The WCRA experienced a third consecutive year of financial improvement in 2011. At December 31, 2011, the balance sheet deficit was $8 million, an improvement of $51 million from the December 31, 2010 deficit of $59 million. This continued financial improvement was due to a reduction in prior accident year funded loss reserves and the continuation of the Surplus Distribution Recovery Program of assessments approved in 2009. Prior accident year funded loss reserves were reduced by $100 million due primarily to favorable development on case reserves. In addition, the WCRA recorded a contribution to capital of $54 million from the assessment program.

The WCRA's cash flow from operating activities was $5 million in 2011, up from $4 million in 2010. This increase was due mainly to an increase in dividends from investments. The WCRA continues to have substantial liquidity and met all of its financial obligations on a timely basis in 2011.

Operating Results and Comprehensive (Loss) Income

PREMIUMS AND LOSSES

The WCRA earned $49 million in funded premiums in 2011, down from $50 million in 2010. This decrease was due to a reduction in exposure base.

Funded losses and loss expenses incurred for 2011 were $59 million, down significantly from $133 million in 2010. This decrease was due to actuarial adjustments of prior accident year losses. Prior accident year loss reserves were reduced by $100 million in 2011 compared to a reduction of $20 million in 2010. The reduction in prior accident year reserves in 2011 was due primarily to favorable development on case reserves which resulted in lower projected ultimate losses.

The components of discounted funded losses and loss expenses are shown below.

($ millions)	2011	2010
Prior accident years:		
Present value update	**$108**	**$103**
Actuarial adjustments	**(100)**	**(20)**
Total prior accident years	**8**	**83**
Current accident year	**51**	**50**
Total funded losses and loss expenses incurred	**$ 59**	**$133**

INVESTMENT PERFORMANCE

For the year ended December 31, 2011, the investment portfolio returned 1 percent compared to a return of 13 percent in 2010. In both 2011 and 2010, the WCRA's assumed rate of investment return was 7 percent. The decrease in 2011 investment return was due primarily to poor performance in the international and domestic equity markets. In 2011, the WCRA's international equities lost 13 percent and US equities returned only 1 percent. In 2010, the WCRA's international equities returned 11 percent and domestic equities returned 17 percent.

The components of investment results are shown below.

($ millions)	2011	2010
Investment income, net of related expenses	$ 30	$ 27
Net realized investment gains	7	102
Change in unrealized (losses) gains on securities	(28)	49
Total investment results	$ 9	$178

In 2011 and 2010, the WCRA Investment Policy included asset allocation targets of 40 percent for domestic equities, 20 percent for international equities, and 40 percent for fixed income investments.

COMPREHENSIVE (LOSS) INCOME

The WCRA recorded a comprehensive loss of $3 million in 2011, compared to comprehensive income of $92 million in 2010. Comprehensive income consists of net income and the change in unrealized gains (losses) on investments, the impact of foreign currency translation adjustments on securities denominated in a currency other than U.S. dollars, and the change in the funded status of the defined benefit pension plan. In 2011, the comprehensive loss was due primarily to unrealized losses on investments. In 2010, the comprehensive income was due mainly to strong investment performance, including realized investment gains of $102 million.

Balance Sheet

ASSETS AND LIABILITIES

Total assets were $1,854 million at December 31, 2011 compared with $1,923 million at the end of 2010. The decrease in total assets was due primarily to a decrease in invested assets.

Total liabilities were $1,862 million at December 31, 2011 compared with liabilities of $1,982 million at December 31, 2010. The decrease in liabilities was due mainly to a decrease in the amount due to securities brokers for unsettled securities transactions and a decrease in the liabilities for losses and loss expenses.

The WCRA's largest liability is the reserve for funded losses and loss expenses. This liability totaled $1,554 million at December 31, 2011 compared with $1,571 million at December 31, 2010. This liability represents the present value, discounted at 7 percent, of the total estimated obligation for losses and loss expenses for unpaid amounts up to the prefunded limit. Because this liability involves claims that will be paid out over a period of many years, judgments as to the ultimate exposure are an important component of the loss reserving process. Reserves are reviewed on a regular basis using a variety of actuarial techniques. They are adjusted based on loss experience and as new information becomes available.

Changes in the discounted liability for funded losses and loss expenses are shown below.

($ millions)	2011	2010
Funded reserves as of January 1	**$1,571**	**$1,512**
Losses and loss expenses incurred:		
Prior accident years	**$ 8**	**$ 83**
Current accident year	**51**	**50**
Total incurred	**59**	**133**
Losses and loss expenses paid	**(76)**	**(74)**
Funded reserves as of December 31	**$1,554**	**$1,571**

The components of prior accident year incurred losses and loss expenses are discussed above under "Operating Results and Comprehensive (Loss) Income."

The liability for unfunded losses and loss expenses totaled $167 million at December 31, 2011 compared to $195 million at December 31, 2010. This liability represents the present value, discounted at 7 percent, of the total estimated obligation for losses and loss expenses for unpaid amounts in excess of the prefunded limit. The $28 million decrease in this liability in 2011 was due to a $42 million reduction in prior accident year loss reserves. This prior-year impact was due to favorable case reserve development. In 2010, the increase in this liability was driven by the present value update and reserves for the current accident year. Unfunded deferred premium revenue of negative $26 million was recognized in 2011, concurrent with incurred unfunded losses and loss expenses of negative $26 million. Loss payments in excess of prefunded limits totaled $1.8 million and $1.6 million in 2011 and 2010, respectively.

DEFICIT

At December 31, 2011, the WCRA had an accumulated balance sheet deficit of $8 million, an improvement of $51 million from the December 31, 2010 deficit of $59 million. This improvement was primarily due to a reduction in prior accident year funded loss reserves and the continuation of the assessment program. Prior accident year funded loss reserves were reduced by $100 million due primarily to favorable development on case reserves. In addition, the WCRA recorded a contribution to capital of $54 million from the assessment program.

In 2009, the Board of Directors adopted the Surplus Distribution Recovery Program, which declared deficient premium assessments of $178 million to members and deficiency assessments of $90 million to self-insurer members and workers' compensation policyholders. The deficient premium assessments are payable in five equal annual installments. In both 2011 and 2010, the WCRA recorded an installment of $36 million of the deficient premium assessments as a contribution to capital. The deficient premium assessments are being recorded on an installment basis due to reasonable uncertainty regarding continuation of the assessments over the full five years. The deficiency assessments are prospective in nature, and are being determined on a year-to-year basis over the five-year period, 2010 through 2014. Deficiency assessments of $18 million and $12 million were recorded as a contribution to capital in 2011 and 2010, respectively.

Cash Flow and Liquidity

The WCRA's cash flow from operating activities was $5 million in 2011, up from $4 million in 2010. This increase was due primarily to an increase in dividends from investments. The WCRA continues to have substantial liquidity and met all of its financial obligations on a timely basis in 2011. In addition, the WCRA has a marketable investment portfolio that can provide significant liquidity. Management believes the WCRA has the liquidity necessary to continue to meet its financial obligations on a timely basis for the foreseeable future.

OUR MISSION

The WCRA ensures the availability of long-term reinsurance protection for serious Minnesota workers' compensation claims. Our staff of innovative professionals is dedicated to achieving the highest standard of excellence through stable and reasonable rates, expert claims administration, and informational services.

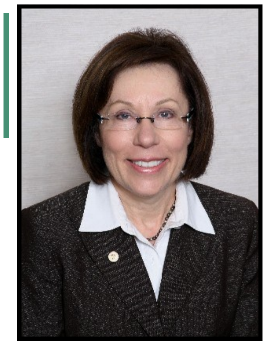
OUR VISION

The WCRA will provide reinsurance services that are considered superior by its members and other participants in the workers' compensation system.

Board of Directors

Chair

Stuart Henderson
Western National Insurance Group



Sharyle Knutson
Minnesota AFL-CIO

Brian Melas
Liberty Mutual Insurance Group

Vice Chair

Robert Lund
SFM

Gary Nelson
Medtronic, Inc.

Edward Reynoso
Teamsters Joint Council 32 DRIVE

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Minnesota State Board of Investment

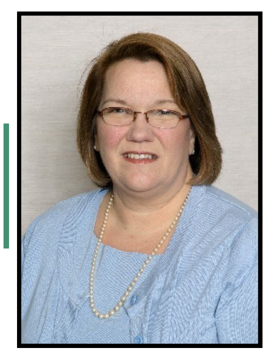
Wayne Simoneau
Public Representative

Kristin Hanson
Minnesota Management and Budget

Michele Spencer
Ecumen

Michael Thoma
The Travelers Companies, Inc.

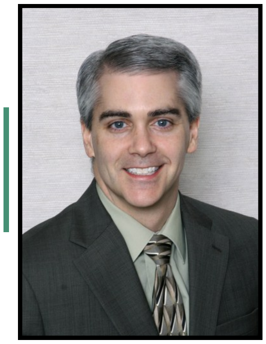
David Hennes
The Toro Company



Allison Waggoner
DCI, Inc.

Senior Management

Carl (Buzz) Cummins
President and CEO



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Actuarial Vice President

Elisabeth Skoglund
Vice President
Claims and Information Systems

Treasurer

Donald Swanson
Vice President
Finance and Investments

Cynthia Smith
Vice President
Operations

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Tony Tio, Actuary

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Mary Fraser, Administrative Assistant
Dawn Gagnelius, Reinsurance Claims Examiner
Natalie Haefner, Catastrophic Nurse Consultant
Thor Haugen, Reinsurance Claims Specialist
Gregory Jeans, Claims Account Manager
Julie Olson, Claims Account Manager
Sherry Staffa, Reinsurance Claims Specialist

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Lori Thompson, Corporate Controller

OPERATIONS

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Jeanne Mann, Administrative Assistant
Dorraine Sullivan, Administrative Assistant

INFORMATION SYSTEMS

Christian King, Manager – Information Systems
Thomas Reynen, Programmer
Annie Whitney, Network Administrator

PREMIUM AUDIT

David Jerden, Premium Field Auditor
Karen Newcom, Administrative Assistant
James Sanem, Senior Premium Audit Specialist

Workers' Compensation Reinsurance Association

Financial Statements
December 31, 2011 and 2010

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Report of Independent Auditors

To the Board of Directors and Members of
Workers' Compensation Reinsurance Association

In our opinion, the accompanying balance sheets and the related statements of operations, comprehensive income and accumulated deficit and of cash flows present fairly, in all material respects, the financial position of the Workers' Compensation Reinsurance Association (the "Association") at December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Association's management. Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits of these statements in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

February 29, 2012

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Workers’ Compensation Reinsurance Association
Balance Sheets
December 31, 2011 and 2010

(in thousands of dollars)	2011	2010
Assets		
Investments, at fair value		
Cash and cash equivalents	**$ 21,638**	$ 59,884
Short-term	**4,300**	46,841
Common and preferred stock	**918,503**	978,250
Bonds	**672,390**	581,350
Total investments	**1,616,831**	1,666,325
Uncollected reinsurance premiums		
Deferred for unfunded losses	**168,229**	194,726
Total uncollected reinsurance premiums	**168,229**	194,726
Assessments receivable	**10,694**	11,874
Accrued investment income	**5,689**	4,598
Due from securities brokers	**51,688**	45,326
Prepaid expenses and other assets	**365**	421
Property and equipment, less accumulated depreciation of $607 and $708 at December 31, 2011 and 2010, respectively	**271**	116
Total assets	**$ 1,853,767**	$ 1,923,386
Liabilities and Accumulated Deficit		
Liabilities		
Losses and loss expenses		
Funded	**$ 1,553,694**	$ 1,571,289
Unfunded	**167,334**	195,350
Total losses and loss expenses	**1,721,028**	1,766,639
Deferred assessments	**46,411**	67,004
Due to securities brokers	**92,155**	147,297
Accounts payable and other liabilities	**2,569**	1,528
Total liabilities	**1,862,163**	1,982,468
Accumulated deficit from operations	**(178,298)**	(257,443)
Accumulated other comprehensive income	**169,902**	198,361
Designated accumulated deficit	**(8,396)**	(59,082)
Total liabilities and accumulated deficit	**$ 1,853,767**	$ 1,923,386

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

Workers' Compensation Reinsurance Association
Statements of Operations, Comprehensive (Loss) Income and Accumulated Deficit
Years Ended December 31, 2011 and 2010

(in thousands of dollars)	2011	2010
Revenues		
Reinsurance premiums		
Funded earned	**$ 49,125**	$ 49,709
Unfunded deferred	**(26,205)**	16,973
Investment income, net of related expenses	**30,343**	26,508
Realized investment gains (losses)		
Net realized investment gains	**26,650**	106,162
Net realized impairment (losses)	**(19,964)**	(4,596)
Total revenues	**59,949**	194,756
Expenses		
Losses and loss expenses		
Funded	**58,559**	133,302
Unfunded	**(26,205)**	16,973
Losses and loss expenses incurred	**32,354**	150,275
Operating and administrative expenses	**2,058**	1,978
Total expenses	**34,412**	152,253
Net income	**25,537**	42,503
Other comprehensive (loss) income		
Change in net unrealized (losses) gains on securities and foreign currency translation adjustment	**(28,459)**	49,441
Comprehensive (loss) income	**(2,922)**	91,944
Assessments	**53,608**	47,552
Accumulated deficit, beginning of year	**(59,082)**	(198,578)
Accumulated deficit, end of year	**$ (8,396)**	$ (59,082)

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

Workers' Compensation Reinsurance Association
Statements of Cash Flows
Years Ended December 31, 2011 and 2010

(in thousands of dollars)	2011	2010
Cash flows from operating activities		
Net premiums collected	**$ 49,416**	$ 51,597
Interest and dividends received, net of related expenses	**35,161**	29,781
Losses and loss expenses paid	**(77,965)**	(75,497)
Operating and administrative expenses paid	**(1,753)**	(1,953)
Net cash provided by operating activities	**4,859**	3,928
Cash flows from investing activities		
Sale and maturities of investments		
Short-term, net	**42,541**	-
Common and preferred stocks	**557,576**	1,126,658
Bonds	**3,335,116**	2,327,111
Purchase of investments		
Short-term, net	**-**	(45,184)
Common and preferred stocks	**(548,119)**	(1,168,990)
Bonds	**(3,459,396)**	(2,285,737)
Purchase of equipment	**(231)**	(77)
Net cash used in investing activities	**(72,513)**	(46,219)
Cash flows from financing activities		
Assessments	**29,408**	46,214
Net cash provided by financing activities	**29,408**	46,214
Net (decrease) increase in cash and cash equivalents	**(38,246)**	3,923
Cash and cash equivalents		
Beginning of year	**59,884**	55,961
End of year	**$ 21,638**	$ 59,884

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

1. General Information

Description of Association

In 1979, the Minnesota Legislature created the Workers' Compensation Reinsurance Association (the "Association"), a nonprofit, unincorporated association, to provide reinsurance protection for serious workers' compensation losses to all primary workers' compensation insurance providers and self-insured employers in the state of Minnesota. The Association provides full indemnification to its members for workers' compensation losses paid in accordance with Minnesota Statutes Chapter 176 that exceed a member's retention limit.

Operating procedures are prescribed by Minnesota Statutes Section 79.34-79.40, as amended (the "Enabling Act"), and the Association's Plan of Operation (the "Plan"). Amendments to the Plan must be approved by the Board of Directors of the Association (the "Board") and the Minnesota Commissioner of Labor and Industry.

Membership

All insurance carriers authorized to underwrite workers' compensation risks in Minnesota and all employers, including political sub-divisions, authorized to self-insure their workers' compensation liabilities in Minnesota are required to be members of the Association.

Retention Limits

For 2011 and 2010, members selected one of three maximum per-loss occurrence retention limits, which were $450,000, $900,000 or $1,800,000. Retention limits are determined annually based on a formula prescribed in the Enabling Act. Minnesota workers' compensation losses incurred by members in excess of the retention limit selected are reinsured by the Association.

Premiums

The estimated aggregate annual reinsurance premium billed by the Association to members in each calendar year is calculated to cover the following estimated costs:

- The present value of the estimated ultimate liability for members' incurred losses above the selected retention limit up to and including the prefunded limit of $9.0 million per occurrence for 2011 and 2010, for funded losses reinsured by the Association.

- Loss payments expected to be made to members for claim amounts in excess of prefunded limits (unfunded losses).

- Operating and administrative expenses of the Association, and loss expenses incurred by the Association. (Loss expenses incurred by members on reinsured claims are not recoverable from the Association.)

- Charges for the current year or a prior year, as determined by the Board, for any reinsurance coverage purchased by the Association.

- Adjustments due to excess or deficient funded premiums, if any, for prior years as determined by the Board.

Estimated reinsurance premiums for each year are billed to the individual members based on: (1) the funded rate for the member's selected retention limit; (2) the rate for expected unfunded payments; and (3) the member's most recent actual exposure base available at the beginning of the annual billing cycle, adjusted for a factor which represents the estimated difference between the member's most recent actual exposure base and the actuarially projected exposure base. In the following year, reinsurance premium adjustments to bring the estimated premiums to actual are calculated and billed or credited to members.

For insurer members, the exposure base is the earned premium at the WCRA standard earned premium reporting level reported in the WCRA Annual Financial Call multiplied by 1.20. Experience rating modifications of the insurers' individual insured are reflected in the Annual Call data.

For self-insurer members, the exposure base is calculated from Minnesota's covered payroll, multiplied by pure premium base rates as published by the MWCIA, multiplied by 1.20, multiplied by an experience rating modification factor.

2. Summary of Significant Accounting Policies

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual results could differ from those estimates.

Risks and Uncertainties

The Association invests in stocks and bonds of U.S. and foreign companies, U.S. government securities, and mortgage-backed securities. The investment viability and return of funds is dependent on, among other factors, the financial results of the underlying issuers. Due to the level of risk associated with certain investments, it is reasonably possible that changes in the values will occur in the near term and that such changes could materially affect future financial statements.

The process of estimating the liability for losses and loss expenses, by its very nature, involves substantial uncertainty. The level of uncertainty is influenced by factors such as the economic assumptions associated with workers' compensation reinsurance. Ultimate actual payments for losses and loss expenses could be significantly different from the estimates.

The Association holds cash on deposit balances throughout the fiscal year that exceed the FDIC insurable limits for banking institutions.

Comprehensive Income

The Association follows the reporting concept of "Comprehensive Income" which requires the reporting of comprehensive income in addition to net income from operations. Comprehensive income is a more inclusive financial reporting methodology that includes disclosure of certain financial information that historically has not been recognized in the calculation of net income. Comprehensive income for the Association includes net income and other comprehensive income, which includes unrealized gains and losses on available-for-sale securities, the impact of foreign currency translation adjustments on securities denominated in a currency other than U.S. dollars, and the change in the funded status of the defined benefit pension plan.

Cash Equivalents
Cash on deposit, shares in money market funds, and short-term debt securities with original maturities of three months or less are classified as cash equivalents.

Short-Term
Debt securities with original maturities greater than three months and less than one year are classified as short term. Amortized cost approximates market value.

Investments
The Association has classified its investments as "available for sale" and carries such securities at fair value. Accordingly, the net unrealized gains or losses are included in other comprehensive income as a separate component of capital. In determining the realized gain or loss on sales of investments, cost is based on the average cost method. Interest income is recognized when earned. Dividend income is recognized on the ex-dividend date.

Purchased premiums and discounts are amortized or accreted using the effective interest rate method over the terms of the respective issues.

When a decline in value of an investment is determined to be other-than-temporary, the specific investment is carried at estimated fair value, and its original book value is reduced to reflect this impairment. Such reductions in book value are recognized in the period in which they were written down as either realized investment losses or as a component of other comprehensive income. See also "New Accounting Pronouncements" in Note 2.

Effective January 1, 2008, the Association adopted Accounting Standards Codification ("ASC") 820. This Standard defines fair value, establishes a framework for measuring fair value, and expands disclosures about fair value measurements. It describes three levels of inputs that may be used to measure fair value:

Level 1: Quoted prices in active markets for identical assets or liabilities that the reporting entity has the ability to access at the measurement date.

Level 2: Observable inputs other than quoted prices included within Level 1 that are observable for the asset or liability either directly or indirectly.

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Property and Equipment
Property and equipment are stated at cost. Depreciation on property and equipment is calculated on the straight-line method over the estimated useful lives of the assets. Upon sale or retirement of property and equipment, the cost and related accumulated depreciation are removed from the accounts and any resulting gain or loss is credited or charged to operations.

Determination of Required Capital

After the close of each fiscal year or at such other times that it deems appropriate, the Board reports whether capital or a deficit exists based on the annual audited year-end financial statements. In determining whether or not to declare an excess surplus distribution or a deficiency assessment, the Board evaluates the capital or deficit relative to the reserves for discounted funded losses and loss expenses. The Board has determined that up to 60% of the liability for funded losses and loss expenses should be retained and reflected on the balance sheet as required capital. Required capital is needed to maintain sufficient assets to provide for variations between expected and actual investment returns, variations between expected and actual claims experience, and other unexpected financial developments. The Board may consider a deficiency assessment if the designated accumulated deficit exceeds 10% of the liability for funded losses and loss expenses.

The Board may declare an excess surplus distribution or an assessment if no such distribution or assessment has been declared in the preceding four years, provided that distributions or assessments may be declared more or less frequently than every five years if the Board, at its sole discretion, determines that it is necessary and prudent to do so. Excess surplus distributions or assessments may be declared by the Board and distributed to or collected from members or policyholders pursuant to the provisions of The Enabling Act and applicable provisions of the Plan. In 2009, the Board declared deficient premium assessments and deficiency assessments. See also Note 9.

Reinsurance Premiums

Funded earned reinsurance premiums are for the calendar year coverage period for funded losses (losses up to and including the prefunded limit). These premiums are billed in the current period. The reinsurance premiums for the calendar year may also include a credit or charge to equitably distribute excess or deficient premiums for previous periods, including any excess or deficient premiums resulting from a retroactive change in the prefunded limit.

Unfunded deferred reinsurance premiums are to be billed in future years for unfunded losses (loss amounts in excess of the prefunded limit) incurred during the calendar year coverage period and are recognized as earned revenue concurrent with the related unfunded losses and loss expenses. Reinsurance premiums for unfunded losses are billed to the members of the Association in the calendar year when payments in excess of prefunded limits are expected to be reimbursed by the Association. The Association began billing for losses in the unfunded layer in 2003. Premiums of $0.3 million and $1.9 million were billed in 2011 and 2010, respectively.

Losses and Loss Expenses

The liability for funded losses and loss expenses represents the present value, discounted using 7% (this is the Association's expected long term return on investments), of the estimated liability for losses and loss expenses of the Association for unpaid amounts up to and including the prefunded limit, as determined by actuarial projections using historical pricing model simulations and the payment and case reserve experience of the Association.

The liability for unfunded losses and loss expenses represents the present value, discounted using 7%, of the estimated liability for losses and loss expenses of the Association for unpaid amounts in excess of the prefunded limit, as determined by actuarial projections of the Association.

The selection of the discount rate is based on a very long-term investment horizon, corresponding to the nature of the Association's funded and unfunded losses and loss expenses liabilities.

Subsequent Events
The Association has evaluated events that have occurred subsequent to December 31, 2011, through February 29, 2012.

New Accounting Pronouncements
Effective January 1, 2010, the Association adopted FASB amended guidance on "Fair Value Measurements and Disclosures" which was intended to improve disclosures about fair value measurements by increasing transparency in financial reporting. The guidance provides for a greater level of disaggregated information and expanded disclosures of valuation techniques and inputs to fair value measurements. The adoption of this guidance had no impact on our financial condition and results of operations but resulted in additional disclosures.

In June 2011, the FASB issued ASU No. 2011-05, "Comprehensive Income (Topic 220): Presentation of Comprehensive Income." ASU No. 2011-05 eliminates the option to present the components of other comprehensive income as part of the statement of accumulated deficit. It requires an entity to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements.

Regardless of whether one or two statements are presented, an entity is required to show reclassification adjustments on the face of the financial statements for items that are reclassified from other comprehensive income to net income. ASU No. 2011-05 is to be applied retrospectively and is effective for fiscal years, beginning after December 15, 2011. The WCRA will adopt this pronouncement in 2012.

3. Investments

The cost of common and preferred stocks, amortized cost of bonds, and estimated fair values at December 31, 2011 and 2010, are as follows:

	2011			
(in thousands of dollars)	**Cost/ Amortized Cost**	**Gross Unrealized Gains**	**Gross Unrealized Losses**	**Estimated Fair Value**
Cash and Cash Equivalents	$ 21,638	$ -	$ -	$ 21,638
Short-term	4,300	-	-	4,300
Common stocks	$ 772,735	$ 151,071	$ (11,805)	$ 912,001
Preferred stocks	4,989	1,514	(1)	6,502
Total stocks	$ 777,724	$ 152,585	$ (11,806)	$ 918,503
U.S. Treasury securities and obligations of U.S. government and agencies	$ 274,376	$ 18,768	$ (121)	$ 293,023
Corporate debt securities	225,705	11,920	(3,752)	233,873
Mortgage-backed securities	141,075	4,542	(123)	145,494
Total bonds	$ 641,156	$ 35,230	$ (3,996)	$ 672,390

(in thousands of dollars)	2010 Cost/ Amortized Cost			Gross Unrealized Gains		Gross Unrealized Losses		Estimated Fair Value
Cash and Cash Equivalents	$	59,875	$	9		-	$	59,884
Short-term		46,838		3	$	-		46,841
Common stocks	$	785,788	$	191,489	$	(6,521)	$	970,756
Preferred stocks		5,763		1,731		-		7,494
Total stocks	$	791,551	$	193,220	$	(6,521)	$	978,250
U.S. Treasury securities and obligations of U.S. government and agencies	$	177,590	$	2,094	$	(3,054)	$	176,630
Corporate debt securities		215,831		13,977		(2,073)		227,735
Mortgage-backed securities		175,036		2,671		(722)		176,985
Total bonds	$	568,457	$	18,742	$	(5,849)	$	581,350

Total unrealized losses were $15.8 million and $12.4 million at December 31, 2011 and 2010, respectively. The following tables provide a breakdown of unrealized losses at December 31, 2011 and 2010. The Association has reviewed the components and duration of these unrealized losses and concluded that the losses are temporary in nature. The unrealized losses are primarily on common stocks. The unrealized losses as of December 31, 2011 and 2010 are as follows:

	Unrealized Holding Losses as of December 31, 2011											
	Less than 12 months				12 months or more				Total			
(in thousands of dollars)	Estimated Fair Value		Unrealized Losses		Estimated Fair Value		Unrealized Losses		Estimated Fair Value		Unrealized Losses	
Short-term	$	-	$	-	$	-	$	-	$	-	$	-
Common stocks	$	94,666	$	(11,327)	$	4,196	$	(478)	$	98,862	$	(11,805)
Preferred stocks		491		(1)		-		-		491		(1)
Total stocks	$	95,157	$	(11,328)	$	4,196	$	(478)	$	99,353	$	(11,806)
U.S. Treasury securities and obligations of U.S. government and agencies	$	21,909	$	(109)	$	904	$	(5)	$	22,813	$	(114)
Corporate debt securities		87,789		(2,856)		12,135		(903)		99,924		(3,759)
Mortgage-backed securities		(21,069)		(123)		-		-		(21,069)		(123)
Total bonds	$	88,629	$	(3,088)	$	13,039	$	(908)	$	101,668	$	(3,996)

	Unrealized Holding Losses as of December 31, 2010											
	Less than 12 months				12 months or more				Total			
(in thousands of dollars)	Estimated Fair Value		Unrealized Losses		Estimated Fair Value		Unrealized Losses		Estimated Fair Value		Unrealized Losses	
Short-term	$	-	$	-	$	-	$	-	$	-	$	-
Common stocks	$	69,508	$	(4,501)	$	16,677	$	(2,020)	$	86,185	$	(6,521)
Preferred stocks		-		-		-		-		-		-
Total stocks	$	69,508	$	(4,501)	$	16,677	$	(2,020)	$	86,185	$	(6,521)
U.S. Treasury securities and obligations of U.S. government and agencies	$	103,541	$	(3,054)	$	-	$	-	$	103,541	$	(3,054)
Corporate debt securities		68,591		(1,361)		10,354		(712)		78,945		(2,073)
Mortgage-backed securities		61,501		(691)		2,833		(31)		64,334		(722)
Total bonds	$	233,633	$	(5,106)	$	13,187	$	(743)	$	246,820	$	(5,849)

The amortized cost and estimated fair value of debt securities at December 31, 2011, by contractual maturity, are shown below:

(in thousands of dollars)		Amortized Cost		Estimated Fair Value
Due in one year or less	$	16,440	$	16,887
Due after one year through five years		123,392		124,432
Due after five years through ten years		185,533		196,107
Due after ten years		315,791		334,964
	$	641,156	$	672,390

Expected maturities will differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

The Association evaluates its investment securities for other-than-temporary impairment on an annual basis. Factors considered in determining whether an impairment is other-than-temporary include: 1) the length of time and the extent to which fair value is less than cost, 2) the financial condition, industry, and near-term prospects of the issuer, 3) adverse changes or events impacting the issuer, and 4) for equity securities, the ability and intent of the Association to hold these investments until recovery.

During 2011, the Association made a determination that the decline in the fair value of certain of its investments was other-than-temporary. As a result of this determination, the cost bases of the individual securities were written down to fair value as the new cost bases. For debt securities, the Association further determined that the decline in fair value that was other-than-temporary was entirely credit loss. In 2011, the total write-down for all investments was $19.9 million and this entire amount was recorded in earnings as a realized loss. The Association also wrote down $4.6 million of individual securities to fair value in 2010.

In 2011, net realized gains consisted of gains on securities of approximately $7.0 million and foreign currency translation loss of $0.3 million. In 2010, net realized gains consisted of gains on securities of approximately $101.7 million and foreign currency translation loss of $0.1 million.

Gross gains of $92.4 million and $182.5 million, and gross losses of $65.8 million and $76.3 million, were realized on sales of investments during 2011 and 2010, respectively. Additional realized losses of $19.9 million and $4.6 million were recognized due to other-than-temporary impairment of securities during 2011 and 2010, respectively. Net investment income and net realized investment gains (losses) during the years ended December 31, 2011 and 2010 are summarized below:

	Net Investment Income		Net Realized Gains (Losses)	
(in thousands of dollars)	**2011**	**2010**	**2011**	**2010**
Cash and cash equivalents	**$ 218**	$ 141	**$ -**	$ -
Common and preferred stocks	**16,859**	14,314	**(4,459)**	49,002
Bonds	**21,028**	21,495	**11,145**	52,564
Securities lending	**15**	1,164	**-**	-
Miscellaneous	**1,236**	-	**-**	-
	39,356	37,114	**$ 6,686**	$ 101,566
Investment expenses	**(4,226)**	(4,551)		
Interest expense on prepaid assessments	**(4,787)**	(6,055)		
	$ 30,343	$ 26,508		

Other comprehensive income in 2011 and 2010 is comprised of the change in unrealized (losses) gains on available-for-sale securities arising during the year, the impact of foreign currency translation adjustments on securities denominated in currency other than U.S. dollars and the change in the funded status of the defined benefit pension plan as follows:

(in thousands of dollars)	**2011**	**2010**
Change in net unrealized (losses) gains on securities	**$ (41,744)**	$ 42,135
Adjustment of losses included in net income	**19,964**	4,596
Foreign currency net translation (loss) gain	**(5,811)**	3,070
Pension benefit obligation	**(868)**	(360)
Total other comprehensive (loss) income	**$ (28,459)**	$ 49,441

(in thousands of dollars)	**2011**	**2010**
Accumulated other comprehensive income consists of		
Net unrealized gains on securities	**$ 170,831**	$ 192,756
Foreign currency translation gain	**1,182**	6,848
Pension benefit obligation	**(2,111)**	(1,243)
Total accumulated other comprehensive income	**$ 169,902**	$ 198,361

The Association has entered into interest-rate future, stock index future, interest-rate options, and interest rate swap contracts. These derivatives are used for several purposes including the management of yield curve and duration on fixed income investments, and for the overlay of cash balances to maintain equity and fixed income exposure in accordance with asset allocation policy. Hedge accounting is not used for any derivative contracts. The primary risks of these derivative instruments are interest rate, credit, and equity market risk. By using certain derivative instruments, the Association is exposed to the counterparty's credit risk i.e. the risk that derivative counterparties may not perform in accordance with the contractual provisions. The Association's exposure to counterparty credit risk is limited to the unrealized gains on such transactions. As of December 31, 2011 and December 31, 2010, the total net liability of derivative instruments was $0.1 million and $0.3 million, respectively. In 2011, net realized losses and the change in net unrealized gains on derivatives totaled $(2.8) million and less than $0.1 million, respectively. The net realized losses from derivatives were primarily from interest-rate and stock-index futures. In 2010, net realized gains and the change in net unrealized losses on derivatives totaled $4.0 million and $(0.2) million, respectively. The majority of this income from derivatives was net realized gains on interest-rate and stock-index futures.

4. Fair Value Measurements

Accounting Standards Codification 820 defines fair value as the exit price that would be received for an asset in the principal or most advantageous market for the asset. See Note 2 for the three levels of inputs that may be used in measuring fair value. We do not have any assets or liabilities measured at fair value on a nonrecurring basis at December 31, 2011 or December 31, 2010. There were no securities as of December 31, 2011 and 2010, respectively, where the fair value was determined using Level 3 inputs, i.e. unobservable inputs supported by little or no market activity.

Assets measured at fair value on a recurring basis are summarized below:

(in thousands of dollars)	Fair Value Measurement Using			
As of December 31, 2011	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Short-term	$ 21,638	$ 4,300	$ -	$ 25,938
Common stocks	$ 912,001	$ -	$ -	$ 912,001
Preferred stocks	-	6,502	-	6,502
Total stocks	$ 912,001	$ 6,502	$ -	$ 918,503
U.S. Treasury securities and obligations of U.S. government and agencies	$ 285,906	$ 7,117	$ -	$ 293,023
Corporate debt securities	-	233,873	-	233,873
Mortgage-backed securities	-	145,494	-	145,494
Total bonds	$ 285,906	$ 386,484	$ -	$ 672,390

(in thousands of dollars)	Fair Value Measurement Using			
As of December 31, 2010	**Level 1**	**Level 2**	**Level 3**	**Total Fair Value**
Short-term	$ 45,220	$ 1,621	$ -	$ 46,841
Common stocks	$ 970,756	$ -	$ -	$ 970,756
Preferred stocks	-	7,494	-	7,494
Total stocks	$ 970,756	$ 7,494	$ -	$ 978,250
U.S. Treasury securities and obligations of U.S. government and agencies	$ 164,583	$ 12,047	$ -	$ 176,630
Corporate debt securities	-	227,735	-	227,735
Mortgage-backed securities	-	176,985	-	176,985
Total bonds	$ 164,583	$ 416,767	$ -	$ 581,350

5. Liabilities for Losses and Loss Expenses

The liability for losses and loss expenses at December 31, 2011 and 2010, is summarized as follows:

(in thousands of dollars)	**2011**	**2010**
Funded, undiscounted	**$ 6,894,306**	$ 6,940,273
Discount	**(5,340,612)**	(5,368,984)
Funded, discounted	**1,553,694**	1,571,289
Unfunded, undiscounted	**1,472,256**	1,737,537
Discount	**(1,304,922)**	(1,542,187)
Unfunded, discounted	**167,334**	195,350
Total, discounted	**$ 1,721,028**	$ 1,766,639

Funded Liabilities

Activity in the funded liability for losses and loss expenses is summarized as follows:

(in thousands of dollars)	**2011**	2010
Balance at January 1		
Funded, undiscounted	**$ 6,940,273**	$ 6,409,177
Incurred related to		
Current year	**395,388**	396,017
Prior years	**(365,202)**	208,963
Total incurred	**30,186**	604,980
Paid related to		
Current year	**56**	32
Prior years	**76,097**	73,852
Total paid	**76,153**	73,884
Balance at December 31		
Funded, undiscounted	**6,894,306**	6,940,273
Discount	**(5,340,612)**	(5,368,984)
Funded, discounted	**$ 1,553,694**	$ 1,571,289

Reserves are reviewed periodically and updated based on current claims experience, trends, and economic outlook.

The following table compares the present value of the Association's funded reserve changes during 2011 with those of 2010.

	2011	**2010**
Discount rate at year end	**7.0%**	7.0%

(in thousands of dollars)	**2011**	**2010**
Funded reserves as of prior year end	**$ 1,571,289**	$ 1,511,871
Prior accident year impact of actuarial adjustments	**(100,000)**	(20,266)
Payments on prior accident years	**(76,097)**	(73,852)
Present value update	**107,327**	103,246
Reserves for current accident year	**51,176**	50,290
Total calendar year funded reserve changes	**(17,595)**	59,418
Funded reserves as of year end	**$ 1,553,694**	$ 1,571,289

In both 2011 and 2010, the reduction in prior year loss reserves was due primarily to favorable development on case-incurred losses, which resulted in lower projected ultimate losses.

Unfunded Liabilities

Payments on prior accident years in excess of prefunded limits totaled $1.8 million and $1.6 million in 2011 and 2010, respectively. Anticipated payments in excess of prefunded limits are billed as premiums for the unfunded layer.

The unfunded reserve methodology follows the funded analysis. Discount rates for unfunded reserves are the same as the funded reserves. The table below compares the present value unfunded reserve changes during 2011 with those of 2010.

(in thousands of dollars)		**2011**		**2010**
Unfunded reserves as of prior year end	**$**	**195,350**	$	179,990
Prior year changes				
Prior accident year impact of actuarial adjustments		**(42,096)**		-
Payments on prior accident years		**(1,812)**		(1,613)
Present value update		**13,611**		12,543
Reserves for the current accident year		**2,280**		4,430
Total calendar year unfunded reserve changes		**(28,016)**		15,360
Unfunded reserves as of year end	**$**	**167,334**	$	195,350

Reserve changes for the unfunded layer do not have an impact on accumulated deficit because on the statement of operations, unfunded losses incurred (which include reserve changes) are offset by an unfunded deferred premium.

In 2011, the reduction in prior year loss reserves was due primarily to favorable development on case-incurred losses, which resulted in lower projected ultimate losses.

6. Employee Benefit Plans

Defined Benefit Pension Plan

The Association has a noncontributory defined benefit pension plan that covers employees who meet eligibility and entry date requirements. The Association uses a December 31 measurement date. As of December 31, 2011, the plan's investment mix was 60% equities and 40% debt securities. The determination of the long-term rate of return on plan assets was based on historical rates of return and future estimated returns for the individual assets classes. Based on the target allocation, the overall expected long-term rate of return for the plan is 7.25%.

Benefits paid in 2011 and 2010 were $32,048 and $23,950, respectively. The estimated benefit payments for 2012 are $41,219.

(in thousands of dollars)	**2011**	**2010**
Benefit obligation, end of year	**$ 4,734**	$ 3,529
Plan assets at fair value, end of year	**2,756**	2,543
Funded status (recognized as a component of accrued liabilities and accumulated comprehensive income)	**$ (1,978)**	$ (986)

(in thousands of dollars)	**2011**	**2010**
Employer contributions	**$ 190**	$ 186
Discount rate	**4.09%**	5.06%
Expected return on plan assets	**7.25%**	8.00%
Rate of compensation increase	**4.00%**	4.00%

The fair value of the plan's assets was determined in accordance with ASC 820, Fair Value Measurements, using the three levels of inputs described in Note 2.

The fair value of plan equities of $1.7 million was determined using Level 1 inputs consisting of quoted prices for identical securities in active markets. The fair value of plan debt securities of $1.1 million was determined using Level 2 inputs consisting of quoted prices for similar securities in active markets. There were no securities where the fair value was determined using Level 3 inputs, i.e. unobservable inputs supported by little or no market activity.

Defined Contribution Plan

The Association sponsors a defined contribution plan, which covers employees who meet the plan's eligibility requirements and have completed the service requirements, under Section 401(k) of the Internal Revenue Code. Participants can contribute a certain percentage of their compensation (subject to annual contribution limits) to the plan. In 2011 and 2010, the Association matched a maximum 4.0% of participant eligible compensation. The Association's matching contribution to the plan was $0.1 million in both 2011 and 2010.

7. Income Tax Status

In 1996, the Association was granted an exemption from federal income taxes under Section 501(c)(27)(a) of the Internal Revenue Code. The Association received a tax-exempt determination letter from the Internal Revenue Service dated February 7, 1997. Therefore, no provision for income taxes is included in the Association's financial statements.

8. Cash Flows

A reconciliation of net income to net cash provided by operating activities for the years ended December 31, 2011 and 2010 is as follows:

(in thousands of dollars)	**2011**	**2010**
Net income	**$ 25,537**	$ 42,503
Adjustments to reconcile net loss to net cash provided by operating activities		
Net realized investment gains	**(6,686)**	(101,566)
Decrease in funded uncollected reinsurance premiums, net of accrued premium adjustments	**2**	1,403
(Decrease) increase in liability for funded losses and loss expenses	**(17,595)**	59,418
Other, net	**3,601**	2,170
Total adjustments	**(20,678)**	(38,575)
Net cash provided by operating activities	**$ 4,859**	$ 3,928

9. Assessments

On May 19, 2009 the Board declared deficient premium assessments to members of $178 million and deficiency assessments to self-insurer members and workers' compensation policyholders of $90 million.

Deficient Premium Assessments
The deficient premium assessments are retrospective in nature, and are based on members' historic WCRA exposures and selected coverage layers from 1979 to 2008. All insurers and self-insurers who were members of the WCRA on December 31, 2008, are obligated to pay deficient premium assessments.

The deficient premium assessments are payable in five equal annual installments, with the first installment due on July 15, 2010, and subsequent installments due on each February 1, 2011 through 2014. Members were given the options of prepaying their entire five-year deficient premium assessment on December 1, 2009, July 15, 2010, February 1, 2011, 2012 or 2013, and having the assessment obligation discounted at an annual rate of 7%.

The Association recorded installments of $35.6 million and $35.8 million of the deficient premium assessments as a contribution to capital in 2011 and 2010, respectively. The deficient premium assessments are being recorded on an installment basis due to reasonable uncertainty regarding continuation of the assessments over the full five years. The Board Resolution declaring the assessments provides that annually the Board will determine whether additional capital produced by earlier assessments, improved investment performance, and/or adjustments in loss reserve requirements warrant continuation of the assessments.

As of December 31, 2011 and 2010, members had prepaid discounted assessments totaling $106.3 million and $105.9 million, respectively. In 2011 and 2010, installments of the total undiscounted amount of the prepaid assessments were recorded as a contribution to capital. As of December 31, 2011 and 2010, the respective remaining portions of the prepaid assessments were recorded as deferred premium assessments. The prepayment discount is being amortized at an annual rate of 7%. Amortization of $4.8 million and $6.1 million was recorded as an offset to investment income in 2011 and 2010, respectively. As of December 31, 2011 and 2010, a deficient premium receivable was recorded for the respective portions of the 2011 and 2010 installments of the deficient premium assessments that were not prepaid.

Deficiency Assessments

The deficiency assessments are prospective in nature, and are being determined on a year-to-year basis over the five year period, 2010 through 2014. The exposure base for these deficiency assessments will be calculated in accordance with the policy year accumulated standard earned premium at Designated Statistical Reporting (DSR) level methodology as defined by the Minnesota Workers' Compensation Insurers Association. For each year of the deficiency assessments, self-insurers and policyholders will pay deficiency assessments based on their estimated DSR premium for the year, subject to subsequent true-up audit adjustments. Deficiency assessments of $18.0 million and $11.8 million were recorded as a contribution to capital in 2011 and 2010, respectively.

10. Contingencies

In October 2008, the Association, along with three other Minnesota nonprofit organizations, filed a lawsuit against Wells Fargo Bank, N.A., relating to its securities lending program. The lawsuit was filed in Minnesota District Court in Ramsey County (court). The trial was concluded in June 2010. The jury found that Wells Fargo Bank had breached its fiduciary duty to the plaintiffs and violated the Minnesota Consumer Fraud statute. Based on the jury verdict, the court entered judgment for the Association in the amount of $12 million. Subsequently, in a judgment entered in June 2011, the court found that the WCRA and the other plaintiffs are also entitled to an award of attorney's fees, litigation costs, forfeiture of certain fees by Wells Fargo, and pre-judgment interest. Wells Fargo has appealed the case to the Minnesota Court of Appeals (appeals court). Final briefs were filed with the appeals court in November 2011 and oral arguments were presented to the appeals court in February 2012. Because the legal proceedings are not concluded, the Association did not record a benefit from the lawsuit in either the 2011 or the 2010 financial statements.

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