



SAIF CORPORATION

BOARD OF DIRECTORS AUDIT COMMITTEE

**Wednesday
September 14, 2011
8:39 a.m.**

**SAIF Corporation
400 High St SE
Salem, Oregon**

After determining a quorum was present, the meeting was called to order at 8:39 a.m.

Roll call:

John Endicott
Jim Ford

SAIF Corporation personnel present:

Brenda JP Rocklin, President and CEO
Casey Baumert, Corporate Internal Auditor
Ken Collins, Interim Vice President of Information Services
Jerry Dykes, Chief Financial Officer
Ryan Fleming, Human Resources Director
Brian Fowler, Premium Audit Manager
Kathy Gehring, Vice President of Claims
John Gilkey, Sr. Vice President of Policyholder Services and Programs
Michelle Graham, Vice President of Policyholder Services
Michael Hartman, Vice President of Policyholder Programs
Bruce Hoffman, Vice President of Underwriting Services
Ruth Koenig, Collection Manager
Gina Manley, Financial Reporting Manager
Theresa McHugh, Vice President of Financial Services
Mike Mueller, Sr. Vice President of Claims
Cathy Pollino, Chief Internal Auditor
Shannon Rickard, Legal Services Director
Colleen Sealock, Vice President of Operations and Human Resources
Pam Woods, Vice President of Claims
Shawn Wright, Chief Actuarial Officer
Sara Bayes, Executive Assistant

Other Attendees:

Julianne Kennedy, Secretary of State
Michelle Rock, Secretary of State
Scott Simpson, Moss Adams
Thor Yarbrough, Moss Adams

Approval of Audit Committee minutes

Motion Mr. Ford, second Mr. Endicott, to approve the minutes from the meeting of June 15, 2011. The vote was unanimous, and the motion was carried.

Internal Audit: Recording of Fraud and Third-Party Collection Transactions

Ms. Pollino reported that, during a prior audit, discrepancies on the amount of money owed to SAIF were noted between the Claims and Legal Collections systems for individual cases of injured worker fraud. Following that audit, it was determined that a similar situation might occur with third-party transactions.

The purpose of this audit was to review the recording of fraud and third-party collection transactions to ensure that all of the various program areas that use this information have up-to-date information regarding the current amount owed to SAIF. Ten fraud files and two third-party files were identified that had numbers that were mismatched in the two collection systems. Because the recovery of monies in these areas is fairly small, it was determined that it was not beneficial from a cost standpoint to update the systems so that the two programs could be linked. An alternative process has been put into place. When a recovery is received, notification is sent to a designated email group by the individual who receives or learns of the recovery, and a designated senior clerical specialist will be responsible for updating both collection systems. All files have now been reconciled on the two systems. Ruth Koenig reported that there are now very clear written procedures on how to proceed with the notification and recording of these collection transactions.

Internal Audit: Dividend Issuance Review

Ms. Pollino reported that this audit was to look at the processes to identify policies that did not qualify for a dividend, and the processes that identify policies that should be capped at 95 percent of premium paid. While there were a couple of errors identified during the audit, the audit was conducted while other quality control processes and management's final review were taking place. Ms. Pollino reports that internal audit is comfortable that the processes would have caught the errors and that no recommendations were warranted.

External financial audit

Scott Simpson reported that the Oregon Secretary of State Audits Division, following a bid process, selected Moss Adams to conduct the annual financial audit of SAIF. The Secretary of State Audits Division reviews the work performed by Moss Adams prior to issuance of their report.

Moss Adams performs two audits: an audit of SAIF's financial statements that are prepared in accordance with generally accepted accounting principles (GAAP), and an audit of the financial statements prepared in accordance with statutory accounting practices. In addition, Moss Adams issues a report on internal control over the financial reporting.

Mr. Simpson explained that there are required communications to those charged with governance, which is primarily intended for the board audit committee members. Management of SAIF is responsible for preparing the financial statements, and providing all records to Moss Adams in preparation for the audit. Moss Adams is responsible for auditing SAIF's financial statements, as well as communicating significant issues related to the audit that are relevant to overseeing the financial

reporting process. Mr. Simpson reported that there were no such issues identified during this financial audit.

The financial statement contains footnotes, which note some significant accounting policies. The financial statement also contains some estimates. Auditing procedures have been applied to those estimates and Moss Adams believes those estimates are appropriate.

No difficulties in dealing with management were encountered during the course of the audit, nor were there any disagreements with management. There were no corrected or uncorrected misstatements found during the audit. The required written representations from SAIF management were received, with no disagreements from Moss Adams. If Moss Adams becomes aware that a second CPA was contacted for a second opinion, they are required to report that to the SAIF board audit committee. No such consultations were found during the audit. Moss Adams found no relationships between the auditors and SAIF that would bear on their independence within the meaning of professional standards. Recommendations and other matters were communicated to management during the course of the audit.

Moss Adams had an unqualified and unmodified opinion on both the GAAP and statutory basis financial statements. The financial statements were presented fairly in all material respects. There were no material weaknesses or deficiencies found in the internal controls over financial reporting.

Thor Yarbrough reported that all activities were completed within the required timelines. SAIF personnel was prepared and well organized. The technology review and analysis of IT controls was performed in February 2011. Documentation by SAIF of key controls of critical audit areas was done well. Moss Adams held weekly meetings with Gina Manley, SAIF's financial reporting manager.

For the 2011 financial audit, Moss Adams will continue to update the audit preparation schedule. There will be additional testing of IT controls to reduce fieldwork. Interim fieldwork will begin in April 2012 and final fieldwork will begin in May 2012. Moss Adams would like to have a walk-through of the premiums and claims processes for their entire audit team. The audit team will remain essentially the same as for the 2010 audit.

In response to a question from Mr. Endicott, Theresa McHugh stated that the audit performed by Moss Adams is paid for by SAIF. The cost for the audit for year ending December 31, 2010 was approximately \$270,000.

Mr. Ford asked if Moss Adams read or tested the work of Oliver Wyman. Mr. Simpson stated that they do both. There is a procedure to review the work and to make certain that the methodology used is recognized by generally accepted accounting principles.

Mr. Ford asked if there was any issue from Moss Adams' perspective regarding Standard and Poor's downgrade. Mr. Simpson responded that, from an audit perspective, it was not an issue.

Shawn Wright reported that Oliver Wyman was engaged to report on an evaluation of the loss and loss adjustment expense reserves, an assessment of the future financial viability of SAIF, and an analysis of the differences between SAIF's current study and Oliver Wyman's current study.

Oliver Wyman found SAIF's loss adjustment expense reserves were reasonable, there is sufficient surplus to maintain SAIF's financial viability, and there were very minor differences in the two studies. The report notes that SAIF's reserves are at the high-end of Oliver Wyman's range. However, the gap between the carried reserves and the mean estimate has decreased.

The meeting was paused while the audit committee members met with the representatives of Moss Adams and the Oregon Secretary of State Audits Division without other SAIF employees present, followed by a meeting with Jerry Dykes, Gina Manley, and Shawn Wright without other SAIF employees present.

The audit committee meeting resumed at 9:35 a.m.

Internal Audit: Review of Business Decision System (BDS) Premium Data

The purpose of this audit was to ensure that the premium information stored in the BDS data warehouse matched the information from the various source systems.

Ms. Pollino reported there was only one set of data elements where a mismatch existed. It was determined that this error was caused by a table that was not properly aggregating all of the data elements. This aggregation table has since been fixed, and it was verified that all of the errors were corrected. The errors represented only .005 percent of the totals. There were no further recommendations.

Internal Audit: Premium Audit Program Quality Control Review Process

The purpose of this audit was to review the premium audit program's quality control review process to determine if changes could be made to make the process more efficient and effective, and whether this process added value to the program.

Ms. Pollino reported that approximately one of every four premium audits were reviewed by program staff based on established criteria. The system will flag for review any audit that added or deleted a job classification. This selection criterion created the most review tasks. It is recommended that there be a narrowing of the types of added classes reviewed to governing class changes, and/or those classes that have historically had classification problems, and to discontinue reviewing those that are only deleting a class.

A criterion exists that allows staff to enter certain classifications, so that when those classifications come in they are put into the review queue. This selection criterion is not currently being used. It is recommended that this criterion be used when management makes a significant decision on how classifications will be applied to help ensure consistent application.

Two selection criterion did not produce many review findings—audits with zero payroll and revised audits. It is recommended that these two selection criteria be considered for elimination.

It was determined that this process does provide value to the program. In approximately 13 percent of all reviews, significant changes to the audits were identified. Approximately 60 percent of audits returned could have been corrected by program staff, rather than sending them back to the auditors to correct.

Internal audit staff reviewed all of the 255 premium waivers that were approved between January 1, 2010 and May 11, 2011. In five cases, the required 60-day notice of additional premium was not given. In one case it was given when it was not required. In ten cases, the waiver dates entered into Business Online did not match the waiver approval form. In two cases there were miscellaneous errors. It is recommended that management reiterate to program staff the importance of providing the full 60-day notice and the need to enter the correct dates into the system.

Internal Audit: Claims Reserving Process

The purpose of this audit was to determine whether individual claim case reserves were being set within a reasonable range and whether the reserves were being updated at appropriate times.

Ms. Pollino reported that 200 claims with established reserves accepted during the first half of 2010 were reviewed. Internal audit staff rated 34 percent as excellent, 48 percent as good, 16.5 percent as fair, and 1.5 percent as poor. Eighty-nine percent of the reserves were found to be in the reasonable range, four percent were over reserved, and seven percent were under reserved. Incremental improvements can be made in the establishment of reserve amounts, the timing of initial reserves and updates to reserves, and the gathering of information prior to setting reserves.

Internal audit staff found that establishment of initial reserves and updating of subsequent reserves were timely 83.5 percent of time, 4.4 percent were reserved too soon, and 12 percent were reserved too late.

In the majority of cases, resources available to adjusters were used appropriately. Documentation of the rationale for reserving decisions was generally sufficient.

Audit Update Report

Three audits have been added to the list of internal audits in process—other states coverage, evidence handling, and third-party processes. Those three audits have been moved up in the queue, and planning and fieldwork are currently in process.

DCBS financial examination update

Jerry Dykes reported that the Department of Consumer and Business Services (DCBS) began a financial examination in June of 2010, three years after the last examination. DCBS indicated that it will likely finish its examination at the end of October. A report

of that examination will be issued sometime after that, and it may be available for the board at the December 2011 or January 2012 meeting.

Other business

The audit committee met with SAIF's internal audit staff without other SAIF employees present.

There being no further business, the meeting was adjourned at 9:39 a.m.

Stephanie Robinson, Assistant to the Board