Report 19-16
September 2019

State Life Insurance Fund

Calendar Years 2018, 2017, and 2016

Office of the Commissioner of Insurance

State of Wisconsin

Legislative Audit Bureau

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Joe Chrisman
State Auditor

September 25, 2019

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee
State Capitol
Madison, Wisconsin 53702

Dear Senator Cowles and Representative Kerkman:

As required by s. 13.94 (1) (de), Wis. Stats., we have completed a financial audit of the Wisconsin State Life Insurance Fund (SLIF) for the years ended December 31, 2018, December 31, 2017, and December 31, 2016. SLIF provides low-cost life insurance policies to Wisconsin residents, is self-funded through premiums and investment earnings, and is administered by the Office of the Commissioner of Insurance (OCI). As of December 31, 2018, SLIF had 23,860 life insurance policies in effect and $185.1 million of life insurance in force. SLIF operates under specific statutory restrictions, including a prohibition on employing commissioned agents and a limitation on coverage of $10,000 for any insured individual.

SLIF prepares its financial statements on a regulatory basis in accordance with financial reporting requirements prescribed by the Wisconsin Commissioner of Insurance, but not in accordance with generally accepted accounting principles. We found SLIF's financial statements to be fairly presented in accordance with the financial reporting requirements it follows.

As required by s. 607.15, Wis. Stats., SLIF's net profits are distributed annually as policy dividends and the ratio of SLIF's surplus to its assets is to be between 7.0 percent and 10.0 percent, to the extent practicable. The surplus-to-assets ratio has been within the statutorily specified range since 2014 and was 7.6 percent as of December 31, 2018. The dividend scale was adjusted as of January 1, 2019, in an effort to maintain the surplus-to-assets ratio within the statutorily specified range.

We appreciate the courtesy and cooperation extended to us by OCI staff in completing our audit.

Respectfully submitted,

Joe Chrisman
State Auditor

JC/ES/ss

Introduction ■

The State Life Insurance Fund offers low-cost individual life insurance to Wisconsin residents.

The State Life Insurance Fund (SLIF), which was created in 1911 to provide low-cost individual life insurance to Wisconsin residents, is administered by the Office of the Commissioner of Insurance (OCI). SLIF is subject to the same regulatory requirements as any life insurance company licensed to operate in Wisconsin. Wisconsin is the only state that offers life insurance to its citizens. SLIF receives no subsidies from the State of Wisconsin.

SLIF offers a maximum of $10,000 in coverage for an individual through two types of life insurance policies: term life and whole life. Term life insurance provides coverage for a specific period of time, and death benefits are paid only if the insured individual dies within that time period. In contrast, whole life insurance offers lifetime insurance for the policyholder and accumulates a cash value that is returned if the policy is surrendered before the death of the insured individual. In addition, the whole life policyholder may borrow against the policy's cash value.

SLIF offers four different whole life insurance policy plans. Ordinary whole life insurance is the most popular and requires premiums to be paid each year during the insured individual's life. Other whole life policies require premiums to be paid up to the age of 65, for the first 20 years of the policy, or in a single payment at the start of coverage.

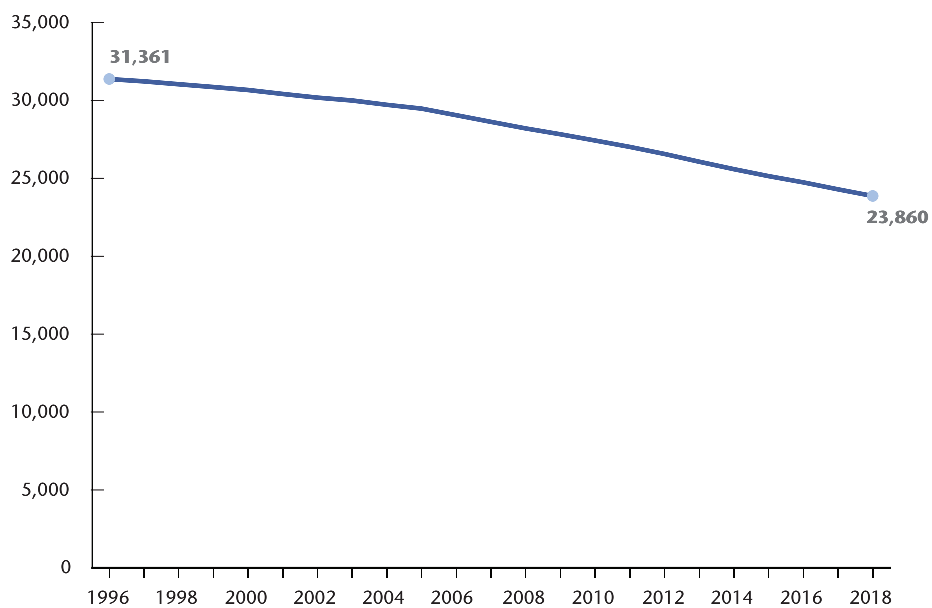
SLIF pays dividends on both term life insurance and whole life insurance policies. Policyholders may elect to accumulate dividends in their accounts, use the dividends to offset premium amounts they owe, apply the dividends to loan principal or interest, or have the dividends paid to them in cash.

The number of policies has continued to decline and was 23,860 as of December 31, 2018.

By statute, OCI is not allowed to advertise life insurance offered by SLIF, and SLIF is not permitted to use commissioned agents. As shown in Figure 1, the number of policies has been declining since December 31, 1996, when there were 31,361 policies. There were 23,860 policies as of December 31, 2018. The amount of insurance in force has also declined and was $185.1 million as of December 31, 2018. The number of new policies issued each year has been less than the total number of death claims and the number of policies surrendered for other reasons, such as failure to pay the annual premium. The continued decline is likely due to a combination of OCI's inability to advertise, the $10,000 limitation on coverage, and private sector competition.

Figure 1

State Life Insurance Fund
Number of Policies as of December 31



Surplus-to-Assets Ratio

The surplus balance of SLIF represents the difference between its assets, which are primarily investment holdings, and its liabilities, which are primarily actuarially determined reserves to pay future insurance benefits. The surplus balance increases when SLIF's revenues, including insurance premiums and investment earnings, are greater than its expenses, including benefit expenses and dividends paid to policyholders. It is important that SLIF have an adequate surplus balance in the event the actuarially determined reserves are not sufficient to pay benefits as they come due.

Statutes specify that, to the extent practicable, the ratio of SLIF's surplus to its assets is to be between 7.0 percent and 10.0 percent.

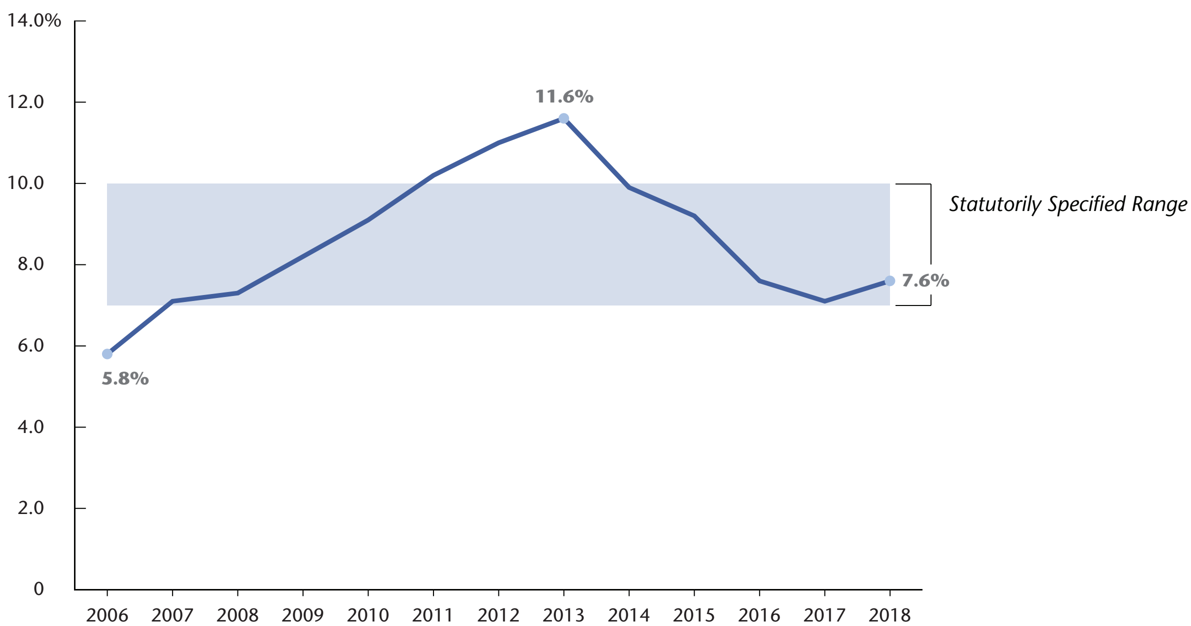
Section 607.15, Wis. Stats., provides that SLIF's net profits be distributed annually to policyholders in the form of dividends. However, statutes also specify that, to the extent practicable, the ratio of SLIF's surplus to its assets is to be between 7.0 percent and 10.0 percent. Some factors affecting the surplus-to-assets ratio, such as actuarially determined reserve balances, are not controllable by OCI staff. However, OCI can adjust the level of dividends paid to policyholders. Periodically, OCI staff will assess whether the dividend scale, which determines the dividends to pay to the various types of policyholders, needs to be adjusted to maintain a surplus-to-assets ratio within the statutorily specified range. If a dividend adjustment is necessary, OCI staff work with SLIF's actuary to review and adjust certain assumptions, such as anticipated investment earnings and mortality rates, which are used in the calculation of the dividend scale.

The surplus-to-assets ratio was 7.6 percent as of December 31, 2018.

As described in report 09-14, the dividend scale was adjusted in 2005 and 2006 in an effort to increase the surplus-to-assets ratio, which had declined below the statutorily specified minimum of 7.0 percent. As a result of these adjustments, the ratio was within the statutorily specified range as of December 31, 2007. However, as we described in report 13-16, the surplus-to-assets ratio continued to increase. As of December 31, 2011, the ratio exceeded the statutorily specified maximum of 10.0 percent and OCI adjusted the dividend scale in 2014 to reduce the surplus-to-assets ratio. As shown in Figure 2, the surplus-to-assets ratio has been within the statutorily specified range since December 31, 2014, and was 7.6 percent as of December 31, 2018. The dividend scale was adjusted as of January 1, 2019, in an effort to maintain the surplus-to-assets ratio within the statutorily specified range.

Figure 2

State Life Insurance Fund
Surplus-to-Assets Ratio as of December 31[1]



[1] Calculated based on amounts included in the audited financial statements.

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Audit Opinion ■

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Joe Chrisman
State Auditor

Independent Auditor's Report on the Financial Statements and Other Reporting Required by *Government Auditing Standards*

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Mr. Mark V. Afable, Commissioner
Office of the Commissioner of Insurance

Report on the Financial Statements

We have audited the accompanying financial statements and the related notes, which were prepared on a regulatory basis, of the Wisconsin State Life Insurance Fund (SLIF) as of and for the years ended December 31, 2018, December 31, 2017, and December 31, 2016, as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management of the SLIF is responsible for the preparation and fair presentation of these financial statements in accordance with financial reporting requirements prescribed by the State of Wisconsin Commissioner of Insurance, which are the statutory accounting principles established by the National Association of Insurance Commissioners, as described in Note 2A to the financial statements. Management is also responsible for the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from 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 audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, which is issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from 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 the 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 opinion on these financial statements.

Basis for Adverse Opinion—U.S. Generally Accepted Accounting Principles

As described in Note 2A to the financial statements, the financial statements are prepared by SLIF in accordance with the financial reporting requirements prescribed by the State of Wisconsin Commissioner of Insurance. This is a basis of accounting other than accounting principles generally accepted in the United States of America. Although not reasonably determinable, the effects on the financial statements of the variances between this regulatory basis of accounting and accounting principles generally accepted in the United States of America are presumed to be material.

Adverse Opinion—U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed above in "Basis for Adverse Opinion—U.S. Generally Accepted Accounting Principles," the financial statements referred to in the first paragraph do not present fairly, in accordance with accounting principles generally accepted in the United States of America, the financial position of SLIF as of December 31, 2018, December 31, 2017, and December 31, 2016, or changes in financial position or cash flows thereof for the years then ended.

Unmodified Opinion—Regulatory Basis of Accounting

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the regulatory basis financial position of SLIF as of December 31, 2018, December 31, 2017, and December 31, 2016, and the respective regulatory basis changes in its financial position and its regulatory basis cash flows thereof for the years then ended, in accordance with the financial reporting requirements prescribed by the State of Wisconsin Commissioner of Insurance as described in Note 2A to the financial statements.

Emphasis of Matter

As discussed in Note 2A to the financial statements, the financial statements referred to above present only SLIF and do not purport to, and do not, present fairly the financial position of the State of Wisconsin as of December 31, 2018, December 31, 2017, and December 31, 2016, the changes in its financial position, or where applicable, its cash flows for the years then ended, in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

Other Matter

Our audit was conducted for the purpose of forming an opinion on the regulatory basis financial statements of SLIF. The supplementary information included as Management's Discussion and Analysis on pages 13 through 19 is presented for purposes of additional analysis and is not a required part of the financial statements. Such information has not been subjected to the auditing procedures applied in the audit of the regulatory basis financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued a report dated September 23, 2019, on our consideration of SLIF's internal control over financial reporting; our tests of its compliance with certain provisions of laws, regulations, and contracts; and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of SLIF's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering SLIF's internal control over financial reporting and compliance.

LEGISLATIVE AUDIT BUREAU

Joe Chrisman
State Auditor

September 23, 2019

Management's Discussion and Analysis ▪

Prepared by the Wisconsin State Life Insurance Fund's Management

This section presents the Management's Discussion and Analysis of the financial performance of the Wisconsin State Life Insurance Fund during the calendar years ended December 31, 2018, December 31, 2017, and December 31, 2016. This discussion should be read in conjunction with the accompanying financial statements and notes. The financial statements, notes, and this discussion are the responsibility of the Office of the Commissioner of Insurance, which manages the Fund.

Overview of the Fund

The Fund was established in 1911 in response to a national scandal over the improper practices of some life insurance companies. The Fund is a state-sponsored life insurance program for the benefit of the residents of Wisconsin but receives no subsidies from the State of Wisconsin. It is not permitted to use commissioned agents, does not advertise, and is exempt from federal income tax. As a result, overhead expenses are minimal. Chapter 607, Wis. Stats., provides that the Fund is to provide low-cost life insurance for residents of Wisconsin. The maximum amount of coverage per individual is $10,000. The Fund offers five different policy plans, which all pay dividends.

The Fund operates on a calendar year basis. Administrative costs and operating costs, including claim payments, are funded through premiums collected from policyholders, policy loan interest, and investment earnings.

During the current audit period, the Fund's surplus-to-assets ratio was in compliance with s. 607.15, Wis. Stats., which requires, to the extent practicable, that the ratio of surplus to assets be between 7.0 percent and 10.0 percent.

Financial Statements

The Fund's financial statements have been prepared on a statutory basis of accounting, which is a type of regulatory basis of accounting, in accordance with accounting practices prescribed by the State of Wisconsin Commissioner of Insurance, which include practices recommended by the National Association of Insurance Commissioners (NAIC).

The Fund's financial statements comprise two components: 1) the financial statements, and 2) notes to the financial statements that explain in more detail some of the information in the financial statements.

Following this section are the financial statements and notes as they relate to the Fund. The financial statements include:

- the Balance Sheet—Statutory Basis, which provides information on the assets and the liabilities of the Fund, with the difference reported as fund surplus;

- the Statement of Operations and Changes in Fund Surplus—Statutory Basis, which presents the revenues earned and the expenses incurred during the year on an accrual basis, as well as the changes in fund surplus; and

- the Statement of Cash Flows—Statutory Basis, which presents information related to cash inflows and outflows summarized by operating, investing, and financing activities and helps measure the Fund's ability to meet financial obligations as they mature.

In this discussion and analysis, the reasons for the changes in financial activity for calendar years 2018, 2017, and 2016 are reviewed.

Assets

As shown in Table A, the largest portion of the Fund's assets, 93.8 percent as of December 31, 2018, is in the form of bonds invested through the State of Wisconsin Investment Board (SWIB). Fund investments are managed by SWIB pursuant to statutory requirements and in accordance with established investment guidelines. All bonds are carried at amortized cost using the scientific method to amortize any premiums and discounts.

Table A

Fund Assets
As of December 31

	2018	2017	2016	2015
Total Assets	$111,517,068	$111,892,508	$110,846,020	$101,418,666
Bonds	$104,628,532	$105,907,869	$104,559,098	$ 94,522,091
Percentage of Total Assets	93.8%	94.7%	94.3%	93.2%

Generally, the turnover in the portfolio is very low due to the long duration of the investments in the portfolio, which is the result of an effort to match the future maturities of investments with expected future payouts of benefits.

As recommended by NAIC accounting standards, the Fund's Statement of Operations and Changes in Fund Surplus reported $0 in net realized capital losses or gains on any bond sale. These realized gains and losses are accounted for in the interest maintenance reserve (IMR) and amortized into net investment income over the life of the bonds sold.

The Fund's remaining assets consisted of contract loans; receivables; and cash, cash equivalents, and short-term investments.

Liabilities

The largest area of the Fund's liabilities is the aggregate reserves for life insurance contracts, as shown in Table B.

Table B

Fund Liabilities
As of December 31

	2018	2017	2016	2015
Total Liabilities	$103,073,833	$103,978,128	$102,388,813	$92,107,784
Aggregate Reserves for Life Insurance Contracts	$66,316,735	$66,153,872	$65,811,636	$65,381,205
Percentage of Total Liabilities	64.3%	63.6%	64.3%	71.0%

The aggregate reserves for life insurance contracts are the amounts required by NAIC to be reported on the balance sheet to show the ability to pay all future claims on the Fund's insurance policies. Because the average age of policyholders is increasing, additional reserves are necessary to fund expected benefit payments upon death.

In addition to the policy reserves, liabilities consist of deposit accounts, also referred to as "deposit-type contracts," held by the Fund for the benefit of the policyholders. The liability for deposit-type contracts includes proceeds held on deposit, consisting of the value of matured policies and proceeds from death claims left in the Fund, and dividends left in the Fund to accumulate. As shown in Table C, the liability for deposit-type contracts increased in calendar years 2016 through 2018.

Table C

Deposit-type Contracts
As of December 31

	2018	2017	2016	2015
Liability for Deposit-type Contracts	$25,400,770	$24,295,487	$23,211,375	$22,011,082
Percentage Change from Prior Year	4.5%	4.7%	5.5%	6.0%

Annually, the Fund pays interest on the deposit-type contracts. As shown in Table D, interest credited to deposit-type contracts increased in both calendar years 2017 and 2018.

Table D

Interest Expense on Deposit-type Contracts
Calendar Year Ended December 31

	2018	2017	2016	2015
Interest Expense on Deposit-type Contracts	$778,225	$731,973	$667,742	$674,033
Percentage Change from Prior Year	6.3%	9.6%	(0.9)%	5.4%

Revenues

Revenue earned in the Fund is from investment income, premium income, and interest income on policy loans. There were 23,860 life insurance policies in effect as of December 31, 2018, a decrease of 1,272 policies, or 5.1 percent, from the policy count of 25,132 as of December 31, 2015.

As shown in Table E, the decrease in Fund revenue is due to the decline in insurance premium revenues resulting from fewer policies in effect and a decline in investment income.

Table E

Fund Revenue
Calendar Year Ended December 31

	2018	2017	2016	2015
Revenue	$6,411,801	$6,683,776	$6,589,286	$6,856,679
Percentage Change from Prior Year	(4.1)%	1.4%	(3.9)%	(1.0)%

Expenses

The Fund pays benefits to policyholders in the event of death, at maturity of the policy, upon surrender of the policy, or in the event the covered individual becomes disabled. The policy benefit claims experience of the Fund has been increasing due to the number of older policies maturing and the number of claims rising due to the aging of those insured by the Fund. Total policy benefits for each year are shown in Table F. The increase in 2017 and 2018 is due to an increase in death claims.

Table F

Policy Benefits
Calendar Year Ended December 31

	2018	2017	2016	2015
Policy Benefits	$2,283,722	$2,155,236	$1,894,350	$2,202,858
Percentage Change from Prior Year	6.0%	13.8%	(14.0)%	5.2%

General expenses include costs to support the administration of the Fund, such as actuarial services, and can fluctuate from year to year due to the timing of activity as shown in Table G. The Fund had an increase in general expenses in 2016 due to audit-related expenses of $91,300 incurred in calendar year 2016 that did not occur in the other years.

Table G

General Expenses
Calendar Year Ended December 31

	2018	2017	2016	2015
General Expenses	$605,699	$478,381	$694,337	$576,420
Percentage Change from Prior Year	26.6%	(31.1)%	20.5%	(7.5)%

Dividends and Surplus

Annually, the Fund pays dividends on all active policies. According to s. 607.15, Wis. Stats., "The net profits of the life fund shall be distributed annually among the policyholders, except that so far as is practicably possible, the ratio of surplus to assets shall be kept between 7 percent and 10 percent." Dividends paid over the last three years are reflected in Table H.

Table H

Dividends
Calendar Year Ended December 31

	2018	2017	2016	2015
Dividends	$2,087,217	$3,555,450	$3,554,540	$3,574,935
Percentage Change from Prior Year	(41.3)%	(0.0)%	(0.6)%	(24.1)%

As shown in Table I, the Fund's surplus-to-assets ratio has been within the statutorily specified range of 7.0 percent to 10.0 percent over that last three years. The dividend scale was adjusted as of January 1, 2019, in an effort to maintain the surplus-to-assets ratio within the statutorily specified range.

Table I

Surplus-to-Assets Ratio
Calendar Year Ended December 31

	2018	2017	2016	2015
Surplus	$8,443,235	$7,914,380	$8,457,207	$ 9,310,882
Total Assets	$111,517,068	$111,892,508	$110,846,020	$101,418,666
Surplus-to-Assets Ratio	7.6%	7.1%	7.6%	9.2%

Contacting the Fund's Financial Management

The financial report is designed to provide the Legislature, the executive branch of government, policyholders, the public, and other interested parties with an overview of the financial results of the Fund's activities and to show the Fund's financial position. If you have questions about this report, or need additional information, contact the Wisconsin State Life Insurance Fund manager at:

Office of the Commissioner of Insurance
125 South Webster Street, Post Office Box 7873
Madison, Wisconsin 53707-7873.

General information relating to the Fund can be found at the Fund's website, *https://oci.wi.gov/Pages/Funds/SLIFOverview.aspx.*

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Financial Statements ■

Balance Sheet—Statutory Basis
December 31, 2018, December 31, 2017, and December 31, 2016

	December 31, 2018	December 31, 2017	December 31, 2016
ASSETS			
Bonds (Note 3)	$ 104,628,532	$ 105,907,869	$ 104,559,098
Cash, Cash Equivalents, and Short-Term Investments (Note 3)	2,514,468	1,423,861	1,611,824
Contract Loans	3,024,870	3,176,751	3,286,620
Investment Income Receivable	1,294,587	1,324,678	1,328,474
Deferred Premiums and Uncollected Premiums (Note 9)	54,611	59,349	60,004
TOTAL ASSETS	$ 111,517,068	$ 111,892,508	$ 110,846,020
LIABILITIES AND FUND SURPLUS			
Aggregate Reserves for Life Insurance Contracts (Note 7)	$ 66,316,735	$ 66,153,872	$ 65,811,636
Liability for Deposit-type Contracts (Note 8)	25,400,770	24,295,487	23,211,375
Contract Claims (Note 2)	361,000	294,894	202,000
Dividends Due and Unpaid, Plus Those Payable in the Following Year (Note 5)	2,179,774	3,638,772	3,645,736
Premiums Received in Advance	47,172	19,869	24,106
Interest Maintenance Reserve (Note 2)	8,216,113	8,991,702	8,871,313
General Expenses Payable	88,138	95,029	181,148
Asset Valuation Reserve (Note 2)	351,740	355,777	333,754
Other Liabilities	112,391	132,726	107,745
Total Liabilities	103,073,833	103,978,128	102,388,813
Fund Surplus (Note 5)	8,443,235	7,914,380	8,457,207
TOTAL LIABILITIES AND FUND SURPLUS	$ 111,517,068	$ 111,892,508	$ 110,846,020

The accompanying notes are an integral part of this statement.

Statement of Operations and Changes in Fund Surplus—Statutory Basis for the Years Ended December 31, 2018, December 31, 2017, and December 31, 2016

	Year Ended December 31, 2018	Year Ended December 31, 2017	Year Ended December 31, 2016
REVENUES			
Premiums (Note 2)	$ 1,154,981	$ 1,232,500	$ 1,322,941
Net Investment Income (Note 4)	4,356,090	4,528,516	4,840,275
Amortization of Interest Maintenance Reserve	893,371	922,760	423,490
Miscellaneous Income	7,359	0	2,580
Total Revenues	**6,411,801**	**6,683,776**	**6,589,286**
OPERATING EXPENSES			
Benefits:			
Death Benefits	1,504,212	1,404,954	1,231,640
Matured Endowments	242,500	267,000	256,000
Surrender Benefits	530,370	475,204	398,537
Disability Benefits	6,640	8,078	8,173
Interest and Adjustments on Contract or Deposit-type Contract Funds	778,225	731,973	667,742
Increase in Aggregate Reserves for Life Insurance Contracts	162,863	342,236	430,431
Total Benefits	3,224,810	3,229,445	2,992,523
General Expenses	605,699	478,381	694,337
Total Operating Expenses	**3,830,509**	**3,707,826**	**3,686,860**
Net Income from Operations before Dividends and Net Realized Capital Gain (Loss)	**2,581,292**	**2,975,950**	**2,902,426**
Dividends to Policyholders (Note 5)	(2,087,217)	(3,555,450)	(3,554,540)
Net Realized Capital Gain (Loss)	0	0	0
NET INCOME (LOSS)	**$ 494,075**	**$ (579,500)**	**$ (652,114)**
CHANGES IN FUND SURPLUS			
Fund Surplus at Beginning of Period	$ 7,914,380	$ 8,457,207	$ 9,310,882
Net Income (Loss)	494,075	(579,500)	(652,114)
Change in Asset Valuation Reserve	4,037	(22,023)	(48,316)
Change in Net Unrealized Capital Gain (Loss)	30,743	58,696	(153,245)
NET CHANGE IN FUND SURPLUS	**528,855**	**(542,827)**	**(853,675)**
Fund Surplus at End of Period	$ 8,443,235	$ 7,914,380	$ 8,457,207

The accompanying notes are an integral part of this statement.

Statement of Cash Flows—Statutory Basis for the Years Ended December 31, 2018, December 31, 2017, and December 31, 2016

	Year Ended December 31, 2018	Year Ended December 31, 2017	Year Ended December 31, 2016
CASH FROM OPERATING ACTIVITIES			
Premiums Collected Net of Reinsurance	$ 1,187,058	$ 1,228,891	$ 1,327,941
Net Investment Income	4,395,350	4,345,971	4,910,753
Miscellaneous Income	7,359	0	2,580
Total Receipts	5,589,767	5,574,862	6,241,274
Benefit and Loss Related Payments	2,995,841	2,760,242	2,704,092
Expenses Paid and Aggregate Write-ins for Deductions	612,689	619,893	508,181
Dividends Paid to Policyholders	3,546,215	3,562,413	3,563,105
Total Benefits and Expenses	7,154,745	6,942,548	6,775,378
Net Cash Provided by Operating Activities	**(1,564,978)**	**(1,367,686)**	**(534,104)**
CASH FROM INVESTING ACTIVITIES			
Cash Received from Sale of Bonds	14,934,463	17,940,891	38,363,849
Cash Paid for Purchase of Bonds	(13,492,886)	(18,176,416)	(39,567,450)
Decrease (Increase) in Contract Loans	151,881	109,869	145,711
Net Cash Used in Investing Activities	**1,593,458**	**(125,656)**	**(1,057,890)**
CASH FROM FINANCING AND MISCELLANEOUS SOURCES			
Net Deposits on Deposit-type Contract and Other Insurance Liabilities	1,105,283	1,084,112	1,200,293
Other Cash Provided (Applied)	(43,156)	221,267	2,744
Net Cash Provided by Financing and Miscellaneous Sources	**1,062,127**	**1,305,379**	**1,203,037**
NET CHANGE IN CASH, CASH EQUIVALENTS, AND SHORT-TERM INVESTMENTS	**1,090,607**	**(187,963)**	**(388,957)**
Cash, Cash Equivalents, and Short-Term Investments at January 1	1,423,861	1,611,824	2,000,781
Cash, Cash Equivalents, and Short-Term Investments at December 31	$ 2,514,468	$ 1,423,861	$ 1,611,824

The accompanying notes are an integral part of this statement.

Notes to the Financial Statements ▪

1. DESCRIPTION OF THE FUND

The Wisconsin State Life Insurance Fund, which is part of the State of Wisconsin financial reporting entity and is reported as an enterprise fund in the State's basic financial statements, was created in 1911 to provide life insurance policies to Wisconsin residents at the lowest possible cost. The Fund is administered by the Office of the Commissioner of Insurance.

The Fund's operation is similar to that of a mutual life insurance company, and the Fund is subject to the same regulatory requirements as any life insurance company licensed to operate in Wisconsin. The Fund is also subject to unique statutory restrictions, such as a prohibition on employing agents and a maximum coverage of $10,000, which are designed to limit the competitive advantage the Fund may have over private insurance companies. The Fund offers two basic policies: whole life insurance and term life insurance. As of December 31, 2018, the Fund had 23,860 life insurance policies in effect, including 22,674 whole life insurance policies and 1,186 term life insurance policies. The total amount of insurance in force as of December 31, 2018, was $185,110,892.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Accounting Practices

The financial statements present the financial position and results of operations of only the activity of the State Life Insurance Fund and are not intended to present the financial activity for the State of Wisconsin as a whole. The Fund's financial statements are presented on a statutory basis of accounting, which is a type of regulatory basis of accounting, in accordance with accounting practices prescribed by the State of Wisconsin Commissioner of Insurance. The National Association of Insurance Commissioners' (NAIC) *Accounting Practices and Procedures Manual* (commonly referred to as the Codification) has been adopted by the State of Wisconsin Commissioner of Insurance as the prescribed practices for the Fund, as permitted by s. 623.02, Wis. Stats. The accounting practices and procedures prescribed by the State of Wisconsin Commissioner of Insurance vary in some respects from accounting principles generally accepted in the United States. The most significant differences between the statutory accounting standards and generally accepted accounting principles are as follows:

Financial Statement Area	Statutory Accounting Standards	Generally Accepted Accounting Principles
Bond Valuation	NAIC category 1 to 5 at amortized cost; NAIC category 6 at lower of amortized cost or fair value. A permanent impairment should be reported as a realized loss, with the cost basis written down to fair value.	Fair value.
Asset Valuation Reserve (AVR)	Formula-driven reserve balance. Established to mitigate potential credit-related investment losses. Year-to-year changes are charged or credited directly to surplus.	Not applicable.
Interest Maintenance Reserve (IMR)	Captures interest-related realized gains and losses on sale of investments and amortizes these to income over the remaining life of the investment sold.	Not applicable.
Realized Investment Gains (Losses)	Only non-IMR gains and losses are reported in income.	Reported as income.
Unrealized Investment Gains (Losses)	Recorded directly to surplus for assets recorded at fair value.	Reported as income.
Due and Deferred Premiums	Due premiums recorded as assets, except that certain balances over 90 days due would be nonadmitted; deferred premiums recorded as assets.	Due premiums reported as assets; deferred premiums offset against liabilities for future policy benefits.
Dividends	Provision made for dividends expected to be paid over the year subsequent to the date of the financial statements, whether or not declared or apportioned.	Provision made for accumulated earnings expected to be paid to policyholders, including pro rata portion of dividends incurred to valuation date; future dividends are accrued over the premium-paying period of the contract.

B. Use of Estimates

The preparation of the financial statements in conformity with statutory accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities. It also requires disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the period. Actual results could differ from those estimates.

C. Accounting Policies

Premiums—Premiums are reported as earned on the policy anniversary date.

Dividends—The amount of dividends to be paid to policyholders is determined annually by the contracted actuary and the Fund's management. The aggregate amount of policyholders' dividends is determined based on interest earnings, mortality, and expense experience for the Fund and judgment as to the appropriate level of statutory surplus to be retained by the Fund in order to be in accordance with s. 607.15, Wis. Stats., which requires that the ratio of surplus to assets is to be between 7.0 percent and 10.0 percent, insofar as is practicably possible.

Contract Loans—Policyholders may borrow from the Fund amounts up to the cash surrender value of their insurance policies. Such contract loans are reported at outstanding indebtedness to the Fund. Interest on contract loans is charged in arrears.

Bonds—In accordance with statutory accounting standards, the Fund reports bonds at amortized cost using the scientific method to amortize bond premiums and discounts, which recognizes the time-value of money and amortizes principal receipts on a pro rata basis, using the securities' current information as opposed to the initial amortized value. NAIC category 6 bonds are reported at the lower of amortized cost or fair value.

Interest Maintenance Reserve—The IMR accumulates interest-related realized gains and losses and amortizes them into income over the remaining life of the investments sold. The Fund uses the IMR method that amortizes groups of assets based on the average maturity dates using standard amortization tables developed by NAIC.

Contract Claims—The liability for unpaid claims includes reported claims that were not paid at year-end and estimates of claims that were incurred but not reported, based on claims reported in the following January.

3. CASH AND INVESTMENTS

All cash is deposited with the State of Wisconsin and is invested in the State Investment Fund, which is a short-term pool of state and local funds managed by the State of Wisconsin Investment Board (SWIB) with oversight by its Board of Trustees. The State Investment Fund is not registered with the Securities and Exchange Commission. Shares in the State Investment Fund are reported as cash equivalents and are carried at the cost of the participating shares, which is also the realizable value as of December 31. Interest income, gains, and losses of the State Investment Fund are allocated monthly.

The types of securities in which the State Investment Fund may invest are enumerated in ss. 25.17 (3) (b), (ba), (bd), and (dg), Wis. Stats., and include direct obligations of the United States or its agencies, corporations wholly owned by the United States or chartered by an act of Congress, securities guaranteed by the United States, unsecured notes of financial and industrial issuers, direct obligations of or guaranteed by the government of Canada, certificates of deposit issued by banks in the United States and solvent financial institutions in Wisconsin, and bankers acceptances. SWIB's trustees may specifically approve other prudent legal investments.

The Fund's investments, both long-term and short-term, are managed by SWIB with an investment objective to maintain a diversified portfolio of high-quality publicly issued fixed-income obligations that will preserve principal, maximize income while minimizing costs to policyholders, and approximate the expected life of the Fund's insurance contracts. The Fund's investments include public bonds that consist of U.S. government obligations and public utility, railroad, industrial, and miscellaneous corporate obligations. In addition, some privately placed fixed-income securities, purchased by the Fund under prior investment guidelines, continue to be held by the Fund.

The book and fair values of the Fund's investments as of December 31, 2018, are as follows:

	Book Value	Fair Value
Government Issuer Obligations	$ 47,467,500	$ 47,513,859
Industrials and Miscellaneous	57,161,032	60,677,083
Total	$104,628,532	$108,190,942

The book and fair values of the Fund's investments as of December 31, 2017, are as follows:

	Book Value	Fair Value
Government Issuer Obligations	$ 47,888,128	$ 49,501,324
Industrials and Miscellaneous	58,019,741	67,363,272
Total	$105,907,869	$116,864,596

The book and fair values of the Fund's investments as of December 31, 2016, are as follows:

	Book Value	Fair Value
Government Issuer Obligations	$ 46,881,502	$ 47,557,311
Industrials and Miscellaneous	57,677,596	65,083,560
Total	$104,559,098	$112,640,871

Book values represent the bonds' amortized costs using the method of amortization discussed in Note 2. Fair values were obtained from information provided by NAIC's Securities and Valuation Office and SWIB.

The book and fair values of bonds, by contractual maturity, at December 31, 2018, follows. Actual maturities may differ from contractual maturities because certain borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Book Value	Fair Value
Due in One Year or Less	$ 5,498,855	$ 5,462,515
Due after One Year through Five Years	23,400,226	24,231,929
Due after Five Years through Ten Years	10,694,069	11,209,565
Due after Ten Years	65,035,382	67,286,933
Total	$104,628,532	$108,190,942

Proceeds from the sales of securities were $14.9 million in 2018, $17.9 million in 2017, and $38.4 million in 2016. The sales resulted in gross realized gains of $235,255 in 2018, $1,043,150 in 2017, and $9,012,784 in 2016, and gross realized losses of $117,473 in 2018, $12,357 in 2017, and $16,337 in 2016. Realized investment gains and losses are determined by specific identification. Generally, realized gains and losses are credited or charged to the IMR and amortized into income over the remaining life of the investments sold. However, realized gains and losses related to bonds that had certain changes in their credit ratings are reported in the financial statements in the year that the bonds are sold.

Excluding investments in U.S. Treasury securities and other obligations of the federal government, the Fund is not exposed to any significant concentration of credit risk in its investments.

Further information about the investments in the State Investment Fund can be obtained from the separately issued State Investment Fund annual financial reports. These reports can be found at *https://www.swib.state.wi.us/publications.*

4. NET INVESTMENT INCOME

Net investment income for calendar years 2018, 2017, and 2016 was generated from the following sources:

	2018	2017	2016
Bonds and Private Placements	$4,269,957	$4,346,091	$4,467,015
Contract Loans	218,713	228,082	373,761
State Investment Fund	37,141	9,343	2,986
Subtotal	4,525,811	4,583,516	4,843,762
Less Investment Expenses	169,721	55,000	3,487
Net Investment Income	$4,356,090	$4,528,516	$4,840,275

Net investment income does not include reported net realized capital gains (losses), which are reported separately on the Statement of Operations and Changes in Fund Surplus.

5. SURPLUS AND POLICYHOLDERS' DIVIDEND RESTRICTIONS

The Fund pays dividends on all active policies. The estimated dividends payable in the following year are charged to current operations. Of the amounts reported on the balance sheet, the amounts paid out between January 1 and March 31 of the following year were $564,167 for 2018; $956,350 for 2017; and $950,380 for 2016.

Section 607.15, Wis. Stats., requires that the surplus be maintained at a level between 7.0 percent and 10.0 percent of assets, insofar as is practicably possible. The Fund's surplus-to-assets ratio was 7.6 percent as of December 31, 2018; 7.1 percent as of December 31, 2017; and 7.6 percent as of December 31, 2016.

6. REINSURANCE

The Fund currently has a contract with Optimum Reinsurance Company for insuring those applicants considered high risk by the Fund. This company is not affiliated, owned in excess of 10.0 percent, or controlled, either directly or indirectly, by the Fund or any representative of the Fund. In addition, no policies issued by the Fund have been reinsured with a company chartered in a country other than the United States (excluding U.S. branches of such companies) that is owned in excess of 10.0 percent or controlled directly or indirectly by an insured, a beneficiary, a creditor of an insured, or any other person not primarily engaged in the insurance business.

Under its reinsurance agreement, the Fund retains the reserves and related assets; pays the reinsurer premiums for the ceded business; and is reimbursed for benefits, unusual expenses, and adjustments to required reserves. The reinsurer has no obligation for the reimbursement of dividends related to the ceded business. The Fund does not have any reinsurance agreements in effect under which the reinsurer may unilaterally cancel any reinsurance for reasons other than for nonpayment of premium or other similar credits. Neither does the Fund have any reinsurance agreements in effect such that the amount of losses paid or accrued through the statement date may result in payment to the reinsurer of amounts that, in aggregate and allowing for offset of mutual credits from other reinsurance agreements with the same reinsurer, exceed the total direct premium collected under the reinsured policies.

The following table contains the total life insurance in force and the amount of reinsurance ceded as of the end of each calendar year:

As of:	Total Life Insurance in Force	Reinsurance Ceded
December 31, 2018	$185,110,892	$2,040,000
December 31, 2017	188,099,706	2,072,000
December 31, 2016	191,314,206	2,085,000

The Fund is contingently liable with respect to ceded insurance should the reinsurer be unable to meet its assumed obligations. Commencing in 2007, the Fund started applying a reserve credit based on the reinsurance ceded life insurance to its aggregate reserve calculation. The reinsurance credit was $23,096 for 2018; $22,330 for 2017; and $21,922 for 2016.

Payments to the reinsurer are treated as a reduction of premium income; claim payments received from the reinsurer are treated as a reduction of benefit expense. Reinsurance transactions reported in the Fund's operations are as follows:

	Premiums	Claims
2018	$41,382	$17,208
2017	36,726	11,440
2016	37,804	23,360

7. RESERVES FOR LIFE INSURANCE CONTRACTS

The aggregate reserve for life insurance contracts for policies issued prior to April 1977 is determined in accordance with the net level premium method, using the American Experience or 1958 Commissioners Standard Ordinary (CSO) mortality tables and an interest rate of 3.0 percent. Aggregate reserves for policies issued from April 1977 through March 1986 are based on the Commissioners Reserve Valuation Method, using the 1958 CSO mortality tables and an interest rate of 4.0 percent. Reserves for policies issued from April 1986 through December 1994 are based on a modified version of the Commissioners Reserve Valuation Method, using the 1980 CSO mortality tables and an interest rate of 5.0 percent. Reserves for policies issued from January 1, 1995, through December 31, 2008, are based on the Commissioners Reserve Valuation Method, using the 1980 CSO mortality tables and an interest rate of 4.0 percent. Reserves for policies issued from January 1, 2009, through December 31, 2012, are based on the Commissioners Reserve Valuation Method, using the 2001 CSO mortality tables and an interest rate of 4.0 percent. Reserves for policies issued since January 1, 2013, are based on the Commissioners Reserve Valuation Method, using the 2001 CSO tables and an interest rate of 3.5 percent.

The Fund waives deduction of deferred fractional premiums upon the death of the insured and returns any portion of the final premium beyond the date of death. Surrender values are not promised in excess of the legally computed reserves.

In addition to the gross premium for a rated age, extra premiums are charged for policies for individuals with high-risk factors issued after April 1, 1977. The Fund cedes 100.0 percent of the risk on substandard policies to its reinsurer. The Fund holds the standard reserve in its financial statements and did apply reserve credits related to reinsurance for this reporting period. Therefore, the actual reserve held by the Fund for substandard policies exceeds the minimum reserve that is required for such policies.

The Fund had the following amounts of insurance in force for which gross premiums were less than net premiums determined according to the standard valuation set by the State of Wisconsin, and the following amounts of reserves to cover this deficiency as of December 31, 2018, December 31, 2017, and December 31, 2016:

	Dec. 31, 2018	Dec. 31, 2017	Dec. 31, 2016
Insurance in Force for Which Gross Premiums Were Less than Net Premiums	$15,434,402	$16,262,723	$17,277,466
Portion of Aggregate Reserves to Cover Deficiency	65,673	71,844	78,566

Insurance-specific tabular interest, tabular less actual reserve released, and tabular cost have been determined by NAIC formulas. Tabular interest on funds not involving life contingencies is also determined by a separate NAIC formula.

8. LIABILITY FOR DEPOSIT-TYPE CONTRACTS

All of the deposit-type contracts of the Fund are subject to discretionary withdrawal without adjustment. They are reported at book value and are not affected by reinsurance. The liability accounts reported as of December 31, 2018, December 31, 2017, and December 31, 2016, include:

	Dec. 31, 2018	Dec. 31, 2017	Dec. 31, 2016
Supplementary Contracts without Life Contingencies	$ 2,410,166	$ 2,352,329	$ 2,325,182
Dividends Left to Accumulate	21,331,403	20,252,958	19,214,183
Accrued Deposits	1,659,201	1,690,200	1,672,010
Total Liability for Deposit-type Contracts	$25,400,770	$24,295,487	$23,211,375

9. DEFERRED PREMIUMS AND UNCOLLECTED PREMIUMS

As of December 31, deferred life insurance premiums and uncollected life insurance premiums, all of which were for ordinary life insurance, were:

	2018	2017	2016
Gross Premium:			
Ordinary New Business	$ 606	$ 582	$ 584
Ordinary Renewal	65,716	70,569	71,234
Total	$66,322	$71,151	$71,818
Net Premium:			
Ordinary New Business	$ 90	$ 214	$ 178
Ordinary Renewal	54,521	59,135	59,826
Total	$54,611	$59,349	$60,004

Gross premium is the premium charged to the policyholder. Net premium is the amount of premium used in the calculation of the statutory reserves and represents the amount needed to provide contract benefits based on statutory interest and mortality reserve assumptions. The difference between the gross and net premium represents the amount available for expenses.

10. EMPLOYEE RETIREMENT PLAN

Permanent employees of the Fund are participants in the Wisconsin Retirement System (WRS), which is administered by the Department of Employee Trust Funds (ETF), under the direction of the ETF Board. The WRS is a cost-sharing multiple-employer defined benefit pension plan administered through a trust. WRS benefits, required contributions, and other plan provisions are established by ch. 40, Wis. Stats. Eligible state and local government public employees are entitled to a retirement benefit based on the higher calculation of a formula benefit or a money purchase benefit. The formula benefit is calculated based on a formula factor, the employee's final average earnings, and creditable service. The money purchase benefit on the employee's contributions plus matching employer's contributions, with interest. The WRS recognized employer contributions from the Fund of $25,249 for 2018, $25,913 for 2017, and $21,750 for 2016.

Additional information about the WRS is included in the State of Wisconsin Comprehensive Annual Financial Report (CAFR). That report is publicly available at *https://doa.wi.gov/Pages/home.aspx.*

ETF also issues a standalone CAFR, which can be found at *http://etf.wi.gov/publications/cafr.htm*.

11. POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS

Other postemployment benefits (OPEB) are benefits other than pensions that state and local governments provide to their retired employees. Under ch. 40, Wis. Stats., ETF and the Group Insurance Board (GIB) have statutory authority for program administration and oversight of postemployment benefits. ETF administers postemployment benefit plans other than pension plans for State employees, which includes the Retiree Life Insurance program and the Retiree Health Insurance program (for retired state employees). Employees of the Fund are employees of the State. The Fund is required to report OPEB expenses. However, the Fund's financial statements do not include these expenses because they are immaterial to the Fund as a whole.

Additional Information about other postemployment benefits provided to State employees is included in the State of Wisconsin CAFR. That report is publicly available at *https://doa.wi.gov/Pages/home.aspx.*

ETF also issues a standalone CAFR, which can be found at *http://etf.wi.gov/publications/cafr.htm.*

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Auditor's Report

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Joe Chrisman
State Auditor

Report 19-16

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters

Senator Robert Cowles and
Representative Samantha Kerkman, Co-chairpersons
Joint Legislative Audit Committee

Mr. Mark V. Afable, Commissioner
Office of the Commissioner of Insurance

We have audited the financial statements and the related notes, which were prepared on a regulatory basis, of the Wisconsin State Life Insurance Fund (SLIF) as of and for the years ended December 31, 2018, December 31, 2017, and December 31, 2016, and have issued our report thereon dated September 23, 2019. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards,* which is issued by the Comptroller General of the United States. We provided an adverse opinion on SLIF's financial statements based on generally accepted accounting principles. We provided an unmodified opinion on SLIF's financial statements prepared on a regulatory basis in accordance with financial reporting requirements prescribed by the State of Wisconsin Commissioner of Insurance.

Internal Control over Financial Reporting

Management of SLIF is responsible for establishing and maintaining effective internal control over financial reporting (internal control). In planning and performing our audit of the financial statements, we considered SLIF's internal control to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of SLIF's internal control. Accordingly, we do not express an opinion on the effectiveness of SLIF's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent misstatements, or to detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or a combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of SLIF's financial statements will not be prevented, or that a material misstatement will not be detected and corrected on a timely basis. A *significant deficiency* is a deficiency or a combination of deficiencies in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether SLIF's financial statements are free from material misstatement, we performed tests of compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of This Report

This report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be used when considering SLIF's internal control and compliance. The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the result of that testing, and not to provide an opinion on the effectiveness of SLIF's internal control or on compliance. Accordingly, this report is not suitable for any other purpose.

LEGISLATIVE AUDIT BUREAU

Joe Chrisman
State Auditor

September 23, 2019