



PINNACOL ASSURANCE

Statutory-Basis Financial Statements and
Supplemental Schedules of Investment and Reinsurance Information

December 31, 2021 and 2020

(With Independent Auditors' Report Thereon)

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PINNACOL ASSURANCE

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PINNACOL ASSURANCE

Report Summary

Authority and Purpose/Scope of the Audit

This audit is conducted under the authority of Section 8-45-121(2) of the Colorado Revised Statutes (C.R.S.), which authorizes the State Auditor to conduct an annual financial audit of Pinnacol Assurance (Pinnacol or the Company) and contract with an auditor or firm of auditors, having the specialized knowledge and experience. The primary purpose of our engagement is to audit the statutory-basis financial statements of Pinnacol as of and for the year ended December 31, 2021, 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* issued by the Comptroller General of the United States, and to express an opinion on those statutory-basis financial statements and the supplemental schedules of investment information. The objective of an audit conducted in accordance with such standards is to obtain reasonable, but not absolute, assurance about whether the statutory-basis financial statements are free of material misstatement.

The financial statements of Pinnacol are prepared in accordance with statutory accounting principles prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado (hereinafter referred to as statutory-basis financial statements, or financial statements in accordance with statutory accounting principles). Accordingly, they are not designed to present, and do not present, the financial position or results of operations in accordance with U.S. generally accepted accounting principles.

In the course of our audit, we examined, on a test basis, evidence supporting the amounts and disclosures in Pinnacol's statutory-basis financial statements as of and for the year ended December 31, 2021.

Audit Opinion and Report

As we are issuing an opinion on the statutory-basis financial statements in conformity with accounting principles prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado, we have modified our financial statement opinion to include an adverse opinion on accounting principles generally accepted in the United States of America (GAAP).

We issued a report on Pinnacol's compliance and internal control over financial reporting based on an audit of the financial statements performed in accordance with *Government Auditing Standards*. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be deficiencies, significant deficiencies, or material weaknesses. A deficiency in internal control over financial reporting 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, or detect and correct, misstatements on a timely basis. A significant deficiency is a deficiency, or combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis.

We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

Summary of Current Year Findings and Recommendations

There were no reported findings and recommendations resulting from the audit for fiscal year 2021.

Summary of Prior Year Findings and Recommendations

There were no reported findings and recommendations resulting from the audit for fiscal year 2020.

PINNACOL ASSURANCE

Description of Pinnacol Assurance

December 31, 2021

Pinnacol Assurance (Pinnacol or the Company) was established as a political subdivision of the State of Colorado (the State) under provisions of the Workers' Compensation Act of Colorado (Title 8, Article 45 of the Colorado Revised Statutes, as amended) to operate as a domestic mutual insurance company for the benefit of injured employees and dependents of deceased employees in Colorado. As required under state law, Pinnacol provides an assured source of workers' compensation insurance to Colorado employers. Pinnacol shall not refuse to insure any Colorado employer or cancel any insurance policy due to the risk of loss or amount of premium, except as otherwise provided in Title 8, Article 45, C.R.S., as amended.

Pinnacol is controlled by a nine-member board of directors, which is appointed by the Governor with the consent of the Colorado Senate. The board of directors has control over all moneys of Pinnacol and is restricted to use such moneys only for the purposes provided in Title 8, Article 45, C.R.S., as amended. The board of directors appoints a chief executive officer who is vested with full power and jurisdiction over the administration of Pinnacol. Pinnacol is not an agency of state government. The State retains no liability on the part of Pinnacol and no State moneys are used for Pinnacol operations. All revenue, moneys, and assets of Pinnacol belong solely to Pinnacol. The State of Colorado has no claim to, nor any interest in, such revenue, moneys, and assets and shall not borrow, appropriate, or direct payments from such revenue, moneys, and assets for any purpose.

Cake Insure, Inc. (Cake) was incorporated on September 20, 2017. Cake is a wholly owned subsidiary of Pinnacol and helps small businesses quote and purchase a workers' compensation insurance policy from Pinnacol. Cake is a digital platform designed to market, underwrite, and service small policyholders that are not considered high risk. With the launch of Cake, Pinnacol became subject to Title 10, Article 3, Part 8 of the C.R.S., Insurance Holding Company Systems, which requires additional report filings with the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado. Pinnacol holds 100% of the voting shares ownership in Cake. An "Insurance Holding Company System" is two or more affiliated persons, one or more of which is an insurer.

Policyholders' Surplus

Pinnacol had policyholders' surplus of \$1,628,060,000 and \$1,557,810,000 as of December 31, 2021 and 2020, respectively. The increase in surplus is primarily related to current year net income.



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Denver, CO 80202-5598

Independent Auditors' Report

The Members of the Legislative Audit Committee and
Pinnacol Assurance Board of Directors:

Report on the Audit of the Financial Statements

Opinions

We have audited the financial statements of Pinnacol Assurance (the Company), which comprise the statutory-basis statements of admitted assets, liabilities, and policyholders' surplus as of December 31, 2021 and 2020, and the related statutory-basis statements of operations and changes in policyholders' surplus, and cash flow for the years then ended, and the related notes to the financial statements.

Unmodified Opinion on Statutory Basis of Accounting

In our opinion, the accompanying financial statements present fairly, in all material respects, the admitted assets, liabilities, and policyholders' surplus of the Company as of December 31, 2021 and 2020, and the results of its operations and its cash flow for the years then ended in accordance with accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado described in Note 1.

Adverse Opinion on U.S. Generally Accepted Accounting Principles

In our opinion, because of the significance of the matter discussed in the Basis for Adverse Opinion on U.S. Generally Accepted Accounting Principles section of our report, the financial statements do not present fairly, in accordance with U.S. generally accepted accounting principles, the financial position of the Company as of December 31, 2021 and 2020, or the results of its operations or its cash flows for the years then ended.

Basis for Opinions

We conducted our audits in accordance with auditing standards generally accepted in the United States of America (GAAS) and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Our responsibilities under those standards are further described in the Auditors' Responsibilities for the Audit of the Financial Statements section of our report. We are required to be independent of the Company and to meet our other ethical responsibilities, in accordance with the relevant ethical requirements relating to our audits. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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

As described in Note 1 to the financial statements, the financial statements are prepared by the Company using accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado, which is a basis of accounting other than U.S. generally accepted accounting principles. Accordingly, the financial statements are not intended to be presented in accordance with U.S. generally accepted accounting principles. The effects on the financial statements of the variances between the statutory accounting practices described in Note 1 and U.S. generally accepted accounting principles, although not reasonably determinable, are presumed to be material and pervasive.



Responsibilities of Management for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado. 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.

In preparing the financial statements, management is required to evaluate whether there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for one year after the date that the financial statements are issued.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion. Reasonable assurance is a high level of assurance but is not absolute assurance and therefore is not a guarantee that an audit conducted in accordance with GAAS and *Government Auditing Standards* will always detect a material misstatement when it exists. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control. Misstatements are considered material if there is a substantial likelihood that, individually or in the aggregate, they would influence the judgment made by a reasonable user based on the financial statements.

In performing an audit in accordance with GAAS and *Government Auditing Standards*, we:

- Exercise professional judgment and maintain professional skepticism throughout the audit.
- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, and design and perform audit procedures responsive to those risks. Such procedures include examining, on a test basis, evidence regarding the amounts and disclosures in the financial statements.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control. Accordingly, no such opinion is expressed.
- Evaluate the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluate the overall presentation of the financial statements.
- Conclude whether, in our judgment, there are conditions or events, considered in the aggregate, that raise substantial doubt about the Company's ability to continue as a going concern for a reasonable period of time.

We are required to communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit, significant audit findings, and certain internal control related matters that we identified during the audit.

Supplementary Information

Our audits were conducted for the purpose of forming an opinion on the financial statements as a whole. The supplementary information included in the investment risks interrogatories, summary investment schedule and reinsurance interrogatories is presented for purposes of additional analysis and is not a required part of the financial statements but is supplementary information required by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audits of the financial



statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with GAAS. In our opinion, the information is fairly stated in all material respects in relation to the financial statements as a whole.

Report on Other Legal and Regulatory Requirements

In accordance with *Government Auditing Standards*, we have also issued our report dated May 18, 2022 on our consideration of Pinnacol Assurance's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements 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 Pinnacol Assurance'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* in considering Pinnacol Assurance's internal control over financial reporting and compliance.

KPMG LLP

Denver, Colorado
May 18, 2022

PINNACOL ASSURANCE

Statutory-Basis Statements of Admitted Assets, Liabilities, and
Policyholders' Surplus

December 31, 2021 and 2020

(In thousands)

Admitted Assets	2021	2020
	<u> </u>	<u> </u>
Cash and invested assets:		
Bonds at adjusted carrying value, fair value of \$2,450,971 in 2021 and \$2,471,087 in 2020 (note 4)	\$ 2,322,842	2,251,470
Preferred stock at adjusted carrying value, fair value of \$754 in 2021 and \$713 in 2020 (note 4)	752	660
Common stock at fair value, actual cost of \$331,772 in 2021 and \$368,440 in 2020. (note 4)	456,309	473,148
Mortgage loans on real estate (note 4)	68,554	45,066
Real estate at cost – net of accumulated depreciation of \$21,178 in 2021 and \$19,865 in 2020	12,847	14,024
Cash, cash equivalents, and short-term investments	53,272	70,331
Other invested assets (notes 4 and 9)	156,972	128,262
Receivables for securities sold	26	69
Total cash and invested assets	<u>3,071,574</u>	<u>2,983,030</u>
Uncollected premiums	28,559	28,822
Earned but unbilled premiums	15,575	—
Funds held by or deposited with reinsurers	4,491	4,582
Electronic data processing equipment – at cost – net of accumulated depreciation of \$2,677 in 2021 and \$3,182 in 2020	570	790
Receivables from subsidiaries and affiliates	74	168
Accrued investment income	18,595	18,466
Total admitted assets	<u>\$ 3,139,438</u>	<u>3,035,858</u>
Liabilities and Policyholders' Surplus		
Reserve for unpaid losses and loss adjustment expenses:		
Reserve for unpaid losses (note 2)	\$ 802,573	805,576
Reserve for unpaid loss adjustment expenses (note 2)	105,898	104,373
Total reserve for unpaid losses and loss adjustment expenses	<u>908,471</u>	<u>909,949</u>
Unearned premiums	69,787	70,501
Advance premiums	9,628	10,501
Dividends payable to policyholders	70,878	31,660
Commissions payable	30,396	29,258
Structured settlement liability (note 3)	381,815	383,881
Payable to subsidiaries and affiliates	64	75
Credit balances due policyholders	9,111	8,699
Payable for securities purchased	341	4,549
Other liabilities	30,887	28,975
Total liabilities	<u>1,511,378</u>	<u>1,478,048</u>
Surplus notes (note 7)	92,000	100,000
Special surplus fund for unfunded pension benefits (notes 1 and 7)	192,211	181,930
Unassigned policyholders' surplus (note 7)	1,343,849	1,275,880
Total liabilities and policyholders' surplus	<u>\$ 3,139,438</u>	<u>3,035,858</u>

See accompanying notes to the statutory-basis financial statements.

PINNACOL ASSURANCE

Statutory-Basis Statements of Operations and Changes in
Policyholders' Surplus

Years ended December 31, 2021 and 2020

(In thousands)

	<u>2021</u>	<u>2020</u>
Underwriting income:		
Premiums earned	\$ 548,807	528,291
Deductions:		
Losses incurred (note 2)	306,712	309,363
Loss adjustment expenses incurred (note 2)	80,358	77,513
Other underwriting expenses incurred	155,531	150,180
Total underwriting deductions	<u>542,601</u>	<u>537,056</u>
Net underwriting gain (loss)	<u>6,206</u>	<u>(8,765)</u>
Investment income:		
Net investment income earned (note 4)	91,173	82,512
Net realized capital gain (note 4)	49,417	58,218
Total investment income	<u>140,590</u>	<u>140,730</u>
Other income (loss):		
Provision for uncollectible premiums	(2,397)	(3,639)
Structured settlement expense (note 3)	(2,286)	(3,042)
Software impairment	(6,142)	—
Other income	599	652
Dividends to policyholders	(90,919)	(12,188)
Less federal income taxes incurred	(564)	—
Net income	<u>45,087</u>	<u>113,748</u>
Change in net unrealized gains on investments	73,682	(12,650)
Change in nonadmitted assets	(40,519)	(4,883)
Change in surplus note	(8,000)	
Policyholders' surplus – beginning of year	<u>1,557,810</u>	<u>1,461,595</u>
Policyholders' surplus – end of year	<u>\$ 1,628,060</u>	<u>1,557,810</u>

See accompanying notes to the statutory-basis financial statements.

PINNACOL ASSURANCE

Statutory-Basis Statements of Cash Flow

Years ended December 31, 2021 and 2020

(In thousands)

	<u>2021</u>	<u>2020</u>
Cash flow from operations:		
Premiums collected – net of reinsurance	\$ 530,646	547,439
Losses and loss adjustment expenses paid – net of reinsurance and deductibles	(388,548)	(379,049)
Other underwriting expenses paid	(153,694)	(157,616)
Dividends paid to policyholders	(51,701)	(73,358)
Federal and foreign income taxes paid (recovered)	(405)	—
Investment income received, net of investment expenses paid	96,039	88,480
Miscellaneous proceeds (expenses)	<u>(5,543)</u>	<u>652</u>
Net cash provided by operations	<u>26,794</u>	<u>26,548</u>
Cash flow from investments:		
Proceeds from sale, maturity, or redemption of investments:		
Bonds	486,129	473,168
Stocks	90,776	250,576
Mortgage loans on real estate	11,935	4,455
Other invested assets	8,112	7,723
Miscellaneous proceeds	<u>45</u>	<u>104,310</u>
Total proceeds from sale or redemption of investments	<u>596,997</u>	<u>840,232</u>
Cost of investments acquired:		
Bonds	(551,823)	(610,263)
Stocks	(14,567)	(240,896)
Mortgage loans on real estate	(35,423)	(25,707)
Other invested assets	(28,317)	(29,819)
Miscellaneous proceeds (applications)	<u>(4,346)</u>	<u>(2,655)</u>
Total investments acquired	<u>(634,476)</u>	<u>(909,340)</u>
Net cash used in investments	<u>(37,479)</u>	<u>(69,108)</u>
Cash flow provided by (used in) financing and miscellaneous sources:		
Cash from repurchase of surplus notes	(8,000)	—
Cash provided by (used in) other miscellaneous sources	<u>1,626</u>	<u>(102,739)</u>
Net cash used in financing and miscellaneous sources	<u>(6,374)</u>	<u>(102,739)</u>
Net decrease in cash, cash equivalents, and short-term investments	(17,059)	(145,299)
Cash, cash equivalents, and short-term investments – beginning of year	<u>70,331</u>	<u>215,630</u>
Cash, cash equivalents, and short-term investments – end of year	\$ <u><u>53,272</u></u>	\$ <u><u>70,331</u></u>

See accompanying notes to the statutory-basis financial statements.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

(1) Nature of Operations and Significant Accounting Policies

(a) Organization

Pinnacol Assurance (Pinnacol or the Company) was established under provisions of the Workers' Compensation Act of Colorado (Title 8, Article 45 of the C.R.S., as amended), as a political subdivision of the State of Colorado (the State), to operate as a domestic mutual insurance company for the benefit of injured employees and dependents of deceased employees. Pinnacol offers insurance to employers operating within the State.

Pinnacol is controlled by a nine-member board of directors, which is appointed by the Governor with the consent of the Senate. In accordance with the applicable statutes of the State, the administration of Pinnacol is under the direction of a chief executive officer, appointed by the board of directors. Pinnacol is not an agency of the State and the State retains no liability on behalf of Pinnacol and no State moneys are used for Pinnacol operations.

Cake Insure, Inc. (Cake) was incorporated on September 20, 2017. Cake is a wholly owned subsidiary of Pinnacol and helps small businesses obtain quotes and purchase a workers' compensation insurance policy from Pinnacol. Cake created a digital platform designed to market, underwrite, and service small policyholders that are not considered high risk. Pinnacol is leveraging the innovations of Cake and continues to scale those innovations across both companies.

(b) Basis of Presentation

The accompanying statutory-basis financial statements of Pinnacol have been prepared in accordance with accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado (the Division). Prescribed statutory accounting practices (SAP) are those practices that are incorporated directly or by reference to state laws, regulations, and general administrative rules applicable to all insurance enterprises domiciled in a particular state. Colorado has adopted the National Association of Insurance Commissioners' (NAIC) SAP, which are codified in the NAIC's *Accounting Practices and Procedures Manual* (the Manual). Therefore, compliance with the Manual is a prescribed accounting practice. In the preparation of the accompanying statutory-basis financial statements, the Company has followed NAIC guidelines and has not utilized any practices considered to be permitted practices.

Statutory accounting practices contained in the Manual vary in some respects from accounting principles generally accepted in the United States of America (GAAP). The more significant differences between NAIC SAP and GAAP are as follows:

- Policy acquisition costs, such as commissions, premium surcharges, and other expenses directly related to the cost of acquiring new business are expensed as incurred, while under GAAP, they are deferred and amortized over the policy term to provide for proper matching of revenue and expense.
- Investments in debt securities are generally carried at amortized value, while under GAAP, they would be carried at fair value. For GAAP, changes in fair value in bonds go through net investment income.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

- Pinnacol’s investment in preferred stock of Cake, a subsidiary, is reported at the lower of cost or fair value. Under GAAP, it would be included in the consolidated financial statements and all significant intercompany balances and transactions would be eliminated in consolidation.
- Short-term investments, which include investments with maturities at the time of acquisition of one year or less, are included with cash and cash equivalents in the accompanying statutory-basis financial statements, while under GAAP, only investments with maturities at the time of acquisition of three months or less are included with cash and cash equivalents.
- Assets are reported under NAIC SAP at “admitted asset” value and “nonadmitted” assets, or those items not meeting the definition of an asset, are excluded through a charge against policyholders’ surplus, while under GAAP, all assets are reported on the balance sheet, net of any required valuation allowance. Nonadmitted assets at December 31, 2021 and 2020 comprised the following (in thousands):

	2021	2020
Other invested assets	\$ 45,772	—
Receivables	15,089	16,098
Fixed assets	360	5,978
Prepays	4,575	3,201
Total nonadmitted assets	\$ 65,796	25,277

- The reserve for losses and loss adjustment expenses (LAE) is reported net of reinsurance, while under GAAP, the balance sheet reports reinsurance recoverable, including amounts related to losses incurred but not reported, as assets.
- The surplus note is reported as a component of surplus, increasing policyholders’ surplus under NAIC SAP. Under GAAP, the surplus note is recorded as long-term debt. The related interest expense may not be accrued under NAIC SAP until approved for payment by the commissioner of the state of domicile while under GAAP, the interest expense is recorded as incurred.
- Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions*, requires employers that are part of a cost-sharing multiple-employer pension fund to record their portion of the unfunded liability, while under NAIC SAP, the employer must only record the cost of the contribution and any liability for any contributions due and unpaid.
- GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*, requires employers that are part of a cost-sharing multiple-employer Other Postemployment Benefit (OPEB) plan to record their portion of the net OPEB liability, while under NAIC SAP, the employer must only record the cost of the contribution and any liability for any contributions due and unpaid.

The effect of the differences between statutory basis of accounting and generally accepted accounting principles, although not reasonably determinable, is presumed to be material. Pinnacol is a political subdivision of the State and as such would follow all applicable GASB pronouncements.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

(c) Use of Estimates

The preparation of statutory-basis financial statements in accordance with accounting practices prescribed by the Division 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 statutory-basis financial statements and the reported amounts of revenue and expenses during the reporting period. Significant estimates include the internal structured settlement liability, the reserves for unpaid losses and loss adjustment expenses, the earned but unbilled premiums asset, estimated fair value of investments, as well as the contingency for uncollectible premiums, among others. Actual results could differ from those estimates and such differences could be significant.

(d) Investments

Investments are recorded on the trade date. Bonds and preferred stocks are stated at amortized value or fair value, based on their NAIC designation, and are adjusted for other than temporary declines in fair value. Mortgage loans on real estate are carried at the outstanding principal balance, less any allowances for credit losses. Common stocks, mutual funds, and common trust funds are carried at fair value. Other invested assets, including partnerships, are recorded at the underlying audited equity value. Due to Colorado Revised Statutes limitations, the balance of other invested assets may not exceed 5% of admitted assets. Any amount exceeding that threshold is treated as a nonadmitted asset. For those investments in which the audited financial statements are not available in a timely manner, the unaudited equity value is used. Unrealized capital gains on common stocks, preferred stocks, mutual funds, and common trust funds are reported as a direct adjustment to policyholders' surplus. Common stocks and preferred stocks in an unrealized loss position for both years are recorded as other-than-temporary impairments (OTTI) and are recorded as a realized loss in the statutory-basis statement of operations in the period in which they occur.

Bond premium or discount is recognized using the effective-interest method taking into consideration specified interest and principal provisions over the life of the bond. Bonds containing call provisions are amortized to the call or maturity value or date that produces the lowest asset value.

Gains and losses on investments sold are realized in operations and are computed using the specific-identification method.

Prepayment assumptions for purposes of recognition of income and valuing of loan-backed bonds and structured securities were obtained from widely accepted models with inputs from major third-party data providers. Model assumptions are specific to asset class and collateral type and are regularly evaluated and adjusted where appropriate. The prospective-adjustment method is used to value all loan-backed securities.

Real estate includes land, the building on the land, and capitalized building improvements used in conducting the Company's business. Land is carried at cost. Building and capitalized building improvements are carried at cost less accumulated depreciation. The cost of the building and capitalized improvements is depreciated over an estimated useful life of 30 years using the straight-line method. Depreciation expense was approximately \$1,313,000 and \$1,324,000 for the years ended December 31, 2021 and 2020, respectively, and is included in net investment income earned in the statutory-basis statements of operations and changes in policyholders' surplus.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

(e) Investment in Subsidiary

Cake was incorporated on September 20, 2017 as a subsidiary of Pinnacol. Pinnacol purchased 2,000,000 voting shares of preferred stock in Cake on September 28, 2017. Pinnacol's ownership percentage in Cake is 100%.

As disclosed in note 1(b), Pinnacol does not consolidate its financial results with Cake. Pinnacol and Cake issue stand-alone financial statements.

Perpetual preferred stock of Cake is reported at the lower of book value or fair value. Cake preferred shares are not publicly priced. As of December 31, 2021 and 2020, Pinnacol recorded \$0 for the carrying value of its investment.

(f) Cash, Cash Equivalents, and Short-Term Investments

For purposes of the statement of cash flow, cash, cash equivalents, and short-term investments include cash on deposit, money market funds, and other investments with maturities of one year or less at the date of acquisition.

As of December 31, 2021, cash, cash equivalents, and short-term investments of approximately \$53,272,000 include (\$7,992,000) of book overdrafts, \$61,264,000 of cash equivalents, and \$0 of short-term investments. As of December 31, 2020, cash, cash equivalents, and short-term investments of approximately \$70,331,000 include (\$4,791,000) of book overdrafts, \$74,819,000 of cash equivalents, and \$303,000 of short-term investments.

(g) Receivables for Securities Sold

As of December 31, 2021, and 2020, receivables for securities sold were approximately \$26,000 and \$69,000, respectively. Receivables for securities arise when sales of securities are recorded as of the trade date. A receivable due from the custodian is established when a security has been sold, but the proceeds from the sale have not yet been received. Receivables for securities not received within 15 days from the stated settlement date are nonadmitted. There were no nonadmitted receivables for securities sold in 2021 or 2020.

(h) Uncollected Premiums

Uncollected premiums are reported net of loss contingencies for uncollectible and nonadmitted balances. Certain receivables are not admissible for statutory accounting purposes.

All receivables for canceled policies and billed receivables that relate to balances outstanding for a period exceeding 90 days are not admissible according to the Manual.

Pinnacol independently estimates the realizable amounts of premiums receivable and records a loss contingency for any uncollectible balances that were not already nonadmitted. During 2021 and 2020, Pinnacol recorded a provision of approximately \$2,397,000 and \$3,639,000, respectively, for premiums receivable due to the unlikelihood of ultimate collection thereof. These amounts are reflected as provision for uncollectible premiums in the accompanying statutory-basis statements of operations and changes in policyholders' surplus.

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A significant portion of Pinnacol's premium receivable balances at December 31, 2021 and 2020 were from companies operating in the construction and services industries in Colorado. The construction industry represents approximately 38% of premiums earned as of December 31, 2021 and 2020. The services industry represents approximately 38% of active policy premiums as of December 31, 2021 and 37% as of December 31, 2020, with all other individual industries constituting the remainder of premiums receivable balances.

(i) Earned but Unbilled Premiums

Earned but unbilled premiums represent a receivable or liability for changes in earned premium and audit premiums, which are amounts due from or to policyholders after the respective policy period has expired based on payroll audits performed by Pinnacol. Such amounts are estimated by Pinnacol based upon internal calculations using historical premium data. There was less uncertainty in 2021, relative to 2020, around payroll impacts associated with the Coronavirus (COVID-19) pandemic. Pinnacol recorded a net estimated earned but unbilled premium receivable in 2021 and 2020 of approximately \$15,575,000 and \$0, respectively.

(j) Credit Balances Due Policyholders

Credit balances due policyholders represent excess premiums or are amounts due to policyholders. Generally, credit balances due policyholders are applied to future premium obligations of policyholders. For 2021 and 2020, such amounts are approximately \$9,111,000 and \$8,699,000, respectively.

(k) Electronic Data Processing Equipment and Software

Electronic data processing (EDP) equipment is recorded at cost, less accumulated depreciation, and depreciated on a straight-line basis over an estimated useful life of three years. Net book value of electronic data processing equipment at December 31, 2021 and 2020 was approximately \$570,000 and \$790,000, respectively. Operating software is recorded at cost, less accumulated depreciation, and depreciated on a straight-line basis over an estimated useful life of three years. Nonoperating software is recorded at cost, less accumulated depreciation, and depreciated on a straight-line basis over an estimated useful life of five years and nonadmitted. Net book value of EDP and software at December 31, 2021 and 2020 was approximately \$190,001 and \$5,773,000, respectively. Internal-use software implementation costs have been impaired and written down from \$6,142,000 to \$0 in 2021, based on a significant change in the manner and timeframe in which the software is expected to be used. The software was previously recorded as a nonadmitted asset in 2020 and, thus, had no impact on surplus in 2021. The software impairment was recorded in the other income (loss) section of the statutory-basis statements of operations and changes in policyholders' surplus. Related depreciation expense of approximately \$517,000 and \$499,000 was incurred during 2021 and 2020, respectively, and is included in LAE and other underwriting expenses incurred in the statutory-basis statements of operations and changes in policyholders' surplus.

(l) Office Equipment, Furniture, Art, and Leasehold Improvements

Office equipment, furniture, art, and leasehold improvements are recorded at cost and depreciated on a straight-line basis. Office equipment, furniture, art, and automobiles are depreciated over an estimated useful life of five years. Leasehold improvements are depreciated over the shorter of the term of the lease or the useful life. In accordance with the Manual, these are nonadmitted assets. The net book value of these assets at December 31, 2021 and 2020 was approximately \$170,000 and \$205,000,

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respectively. Related depreciation expense of approximately \$95,000 and \$99,000 was incurred in 2021 and 2020, respectively, and is included in LAE and other underwriting expenses incurred in the statutory-basis statements of operations and changes in policyholders' surplus.

(m) Safety Group Dividend Program

Pinnacol has a safety group program whereby policyholders who are members of the program are entitled to a dividend based on established criteria. Pinnacol paid out safety group dividends of \$1,507,000 in 2021 and \$2,296,000 in 2020. As of December 31, 2021, and 2020, safety group dividends payable of \$2,072,000 and \$2,613,000, respectively, are included in dividends payable to policyholders. These dividends are not declared from surplus nor are they recorded as a direct reduction to policyholders' surplus. The dividends are recorded as dividends to policyholders in the statutory-basis statements of operations and changes in policyholders' surplus.

(n) Individual Loss Control Dividend Program

Pinnacol has an individual loss control dividend (ILCD) program that is designed for policyholders who are committed to effective loss control in their business operations. If the policyholder meets the minimum premium requirements and pays an additional 5% premium charge as a buy in to the plan, the policyholder may receive a reduction of premium based on the policy premium and the loss ratio. Pinnacol paid out ILCDs of \$18,962,000 in 2021 and \$21,382,000 in 2020. As of December 31, 2021 and 2020, ILCDs payable of \$28,196,000 and \$28,709,000, respectively, are included as dividends payable to policyholders in the statutory-basis statements of operations and changes in policyholders' surplus.

(o) General Policyholder Dividends

The board of directors, at its discretion, determines the amount of general policyholder dividends to be declared, based on Pinnacol's overall experience and financial condition. Pinnacol has declared or accrued policyholder dividends to its policyholders in good standing of approximately \$89,953,000 in 2021 and \$10,009,000 in 2020. This is included in dividends payable to policyholders. General policyholder dividends are accrued when declared by the board of directors. On November 4, 2020, the board of directors chose not to declare a general policyholder dividend, delaying the final decision and the subsequent accrual of the general policyholder dividend until year-end 2020 financial results were available. On February 24, 2021, the board of directors determined the final amount of the general policyholder dividend to be paid in March 2021 to be \$50,000,000. On November 3, 2021, the board of directors declared a general policyholder dividend to be paid in March 2022 of approximately \$40,000,000 with the final amount to be set in February 2022 based on year-end 2021 financial results. On February 23, 2022, the board of directors determined the final amount of the general policyholder dividend to be paid in March 2022 to be \$50,000,000.

(p) Reserve for Unpaid Losses and Loss Adjustment Expenses and Structured Settlement Liability

The reserve for unpaid losses and loss adjustment expenses represents management's best estimate of ultimate net cost of all reported and unreported losses incurred through December 31, 2021 and 2020. The reserve for unpaid losses and loss adjustment expenses is estimated by management, which uses an independent third-party actuary to provide estimates based on individual case basis valuations and statistical analyses. Those estimates are subject to the effects of trends in loss severity and frequency. Although considerable variability is inherent in such estimates, management believes

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the reserve for unpaid losses and loss adjustment expenses is adequate. These estimates are continually reviewed and adjusted, as necessary, as experience develops, or new information becomes known. Such adjustments are included in losses incurred or loss adjustment expenses incurred within the statutory-basis statements of operations and changes in policyholders' surplus in the period such information becomes known. Subrogation claims (claims against third parties) are recognized as a reduction of losses incurred when collections are received.

Internal structured settlement liabilities represent obligations to claimants and dependents on cases that have been closed by contract. The discounted reserve for internal structured settlements is estimated by management, which uses an independent third-party actuary to provide estimates based on these obligations.

(q) Revenue Recognition and Unearned Premiums

For certain policies, earned premium is recorded on an installment basis to match the billing frequency stated in the policyholder contract with a provision for amounts earned but unbilled. Earned premium for all other contracts is recognized using the daily pro rata method over the period the policy is effective.

Unearned premiums represent amounts either collected or billed and due from policyholders at December 31, 2021 and 2020 but unearned at that date as they pertain to subsequent policy periods. Unearned premiums billed, which relate to policy effective dates subsequent to December 31, 2021 are not included in the unearned premiums balance but are included as advance premium if the related cash is collected. Unearned premiums are computed on a daily pro rata basis over the effective period of the policies.

(r) Premium Deficiency Reserve

A premium deficiency reserve is recognized by recording an additional liability for the deficiency, which results when anticipated future loss, loss adjustment expense, commissions, other acquisition costs, and maintenance costs exceed the recorded unearned premium reserve, any future installment premiums on existing policies, and anticipated investment income. The change in this reserve is recorded as a component of other underwriting deductions.

Pinnacol recorded a premium deficiency reserve of \$0 at December 31, 2021 and 2020. Pinnacol considered anticipated investment income at 2.5% when evaluating the premium deficiency reserve for 2021.

(s) Multiemployer Pension Plans and Other Postretirement Benefits

Pinnacol participates in the State Division Trust Fund (SDTF), a cost-sharing multiple-employer defined-benefit pension and healthcare trust fund plan administered by the Public Employees' Retirement Association (PERA). SDTF provides retirement, disability, and survivor benefits. All employees of Pinnacol are members of the SDTF.

Pinnacol participates in the Health Care Trust Fund (HCTF), a cost-sharing multiple-employer defined-benefit OPEB plan administered by PERA. The HCTF provides a healthcare premium subsidy to eligible participating PERA benefit recipients and retirees who choose to enroll in one of the PERA

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healthcare plans; however, the subsidy is not available if only enrolled in the dental and/or vision plan(s).

As a participant in a multiple-employer pension plan and HCTF, Pinnacol recognizes as net pension cost and net postretirement benefit cost the required contribution for the period and as a liability any contributions due and unpaid.

(t) Reinsurance

Ceded reinsurance transactions are accounted for based on estimates of their ultimate cost. Losses incurred, loss adjustment expenses incurred, and the reserve for loss adjustment expenses are reported net of reinsured amounts in accordance with the Manual. Premiums earned are reported net of reinsurance (note 5).

(u) Taxes

As a political subdivision of the State of Colorado, Pinnacol is generally not subject to federal or state income taxes under a specific exemption granted under Section 501(c) of the Internal Revenue Code; nor is Pinnacol subject to property tax or sales and use taxes. However, Pinnacol is subject to income taxes on any net income that is derived from a trade or business regularly carried on and not in furtherance of the purposes for which it was granted exemption.

In 2021, Pinnacol incurred \$564,000 of federal tax expense that is attributable to investment income that is considered unrelated business income. No federal tax expense was recognized in 2020. Pinnacol recorded an estimated federal tax liability at December 31, 2021 of approximately \$159,000. Pinnacol is not aware of any uncertain tax positions.

Pinnacol is not subject to a premium tax pursuant to Section 8-45-117(3), C.R.S. However, Pinnacol is subject to a surcharge on premiums pursuant to Section 8-44-112(1)(a), C.R.S. The surcharge is based on a rate established by the Colorado Department of Labor and Employment Division of Workers' Compensation annually, approximately 1.45% at December 31, 2021 and 2020. Such amounts are included in other underwriting expenses incurred.

(v) Surplus Note

Pinnacol issued a \$100,000,000 surplus note on June 25, 2014. Before issuing this debt, the Company obtained approval from the Commissioner of the Division for the transaction and approval to classify the debt as a component of policyholders' surplus. Upon obtaining approval from the Commissioner of the Division on October 21, 2021, Pinnacol repurchased \$8,000,000 of its outstanding \$100,000,000 surplus note on October 28, 2021, by paying the noteholder cash consideration equal to 131% of the principal repurchased plus accrued interest.

(w) Special Surplus Fund for Unfunded Pension Benefits

Pinnacol participates in a cost-sharing multiple-employer defined-benefit pension plan administered by PERA. PERA has a net pension liability, which represents the unfunded pension benefits. Statutory accounting does not allow Pinnacol's portion of the net pension liability to be recorded as a liability, but allows a company to establish a special surplus fund to provide for contingencies. PERA provides Pinnacol with the audited schedule of employers' allocations and net pension liability. The total pension

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liability used to calculate the net pension liability is determined by an actuarial valuation as of December 31, 2019. PERA uses standard update procedures to roll forward the total pension liability to December 31, 2020. A discount rate of 7.25% is being used. PERA also provides the employer allocation percentage for purposes of calculating Pinnacol's proportionate share of the collective net pension liability.

Pinnacol participates in the Health Care Trust Fund (HCTF), a cost-sharing multiple-employer defined-benefit Other Postemployment Benefit (OPEB) plan administered by PERA. Although not required under statutory accounting to record its share of the liability, the Company has identified its portion of the HCTF liability in a special surplus fund in the same manner as the PERA net pension liability obligation.

(x) Application of Recent Statutory Accounting Pronouncements

During 2021, there were no substantive revisions to statutory accounting that were applicable to Pinnacol, and therefore, there were no substantive revisions adopted by the Company.

(y) COVID-19 Impacts

On March 10, 2020, Colorado declared a state of emergency in response to the spread of the COVID-19 pandemic. Pinnacol has been adversely affected by the COVID-19 pandemic primarily due to a reduction in payroll by policyholders that reduced premiums. Pinnacol continues to experience some impacts from the COVID-19 pandemic. While COVID-19-related claims continue, they are significantly off the peaks experienced in late 2020. Pinnacol is unable to project the full extent of the impact of COVID-19.

(2) Unpaid Losses and Loss Adjustment Expenses

Unpaid losses and loss adjustment expenses (both allocated and unallocated) represent management's best estimate of the ultimate medical and indemnity net cost of all losses and loss adjustment expenses that are incurred but unpaid at year-end. Such estimates are based on individual case estimates for reported claims and actuarial estimates for losses that have been incurred but not reported. Any change in probable ultimate liabilities is reflected in losses incurred or loss adjustment expenses incurred within the statutory-basis statements of operations and changes in policyholders' surplus in the period such determination is made.

The estimated ultimate cost of losses is based on historical patterns and the expected impact of current socioeconomic trends. The ultimate settlement of claims will not be known in many cases for years after the time a policy expires. Court decisions and federal and state legislation between the time a policy is written, and the time associated claims are ultimately settled, among other factors, may dramatically impact the ultimate cost. Due to these factors, among others, the process to estimate loss and loss adjustment reserves at a point in time cannot provide an exact forecast of future payments. Rather, it produces a best estimate of liability as of a certain date. Management believes the currently estimated reserves to be adequate. While the ultimate liability may differ from the current estimate, management does not believe the difference will have a material effect, either adverse or favorable, on Pinnacol's financial position or results of operations.

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Unpaid Losses and Loss Adjustment Expenses

Activity in the liability for unpaid losses and loss adjustment expenses in 2021 and 2020 is summarized as follows (in thousands):

	Unpaid losses and loss adjustment expenses	
	2021	2020
Balance at January 1	\$ 909,949	902,122
Additional amounts incurred related to:		
Current year	433,373	420,721
Prior years	<u>(46,303)</u>	<u>(33,845)</u>
Total incurred	<u>387,070</u>	<u>386,876</u>
Reductions relating to payments for:		
Current year	133,658	130,227
Prior years	<u>254,890</u>	<u>248,822</u>
Total paid	<u>388,548</u>	<u>379,049</u>
Balance at December 31	<u>\$ 908,471</u>	<u>909,949</u>

During the year ended December 31, 2021, the provision for unpaid losses and loss adjustment expenses for insured events of prior years was reduced by \$301,193,000 to \$608,756,000. This reduction includes payments for unpaid losses and loss adjustment expenses of approximately \$254,890,000 and a \$46,303,000 reduction in reserves for prior year unpaid losses and loss adjustment expense. This decrease is generally the result of ongoing analysis of recent loss development trends and better than expected development. Pinnacol's claims continue the trend of favorable development that has been evident for a number of calendar years. When the actual selected ultimate cost of an accident year's claims is less than the original estimate, favorable development is recorded. This favorable development resulted from initiatives to improve claims handling practices and reduce claims handling expenses when prudent and a reduction of ultimate claim frequency in Colorado. Pinnacol management continually evaluates the estimated ultimate cost of all accident years and on a calendar year basis adjusts to the best estimate available, favorable or unfavorable, in the current period. The amount of reserve credit recorded for high deductibles on unpaid losses was \$6,011,000 and \$4,867,000 as of December 31, 2021 and 2020, respectively. Such reduction is collateralized generally with letters of credit for the benefit of Pinnacol. Pinnacol received \$6,907,000 and \$8,765,000 in subrogation as of December 31, 2021 and 2020, respectively. There were no significant changes in methodologies or assumptions used in calculating the reserves.

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(3) Internal Structured Settlements

Pinnacol has an internal structured settlement program in which it retains the liability for settlements to claimants rather than purchasing annuities from third parties. This liability has mortality risk and is discounted using a market rate. The internal structured settlement liability is actuarially valued. The internal structured settlement liability is reported as a financing liability separate from unpaid losses and loss adjustment expenses on the statutory-basis statements of admitted assets, liabilities, and policyholders' surplus.

Activity in the liability for internal structured settlements in 2021 and 2020 is summarized as follows (in thousands):

	<u>2021</u>	<u>2020</u>
Beginning balance	\$ 383,881	387,750
Amounts incurred:		
Change in valuation	2,286	3,042
Amounts paid	(27,597)	(27,451)
New internal structured settlements	<u>23,245</u>	<u>20,540</u>
Ending balance	<u>\$ 381,815</u>	<u>383,881</u>

Pinnacol uses an annuity quote that is based upon an estimated discount rate as a basis for the paid claim amount. As such, the liability should be discounted at a market rate. The discount rate applied to internal structured settlement liabilities is 2.5% at December 31, 2021 and 2020.

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The amount of the discount for unpaid internal structured settlements as of December 31, 2021 and 2020 is approximately \$136,364,000 and \$141,279,000, respectively. The discount amounts for internal structured settlement reserves at December 31, 2021 and 2020 are distributed over the years in which the losses were incurred as follows (in thousands):

2021		2020	
Loss year	Discount	Loss year	Discount
Prior	\$ 99,072	Prior	\$ 102,728
2011	5,152	2010	4,433
2012	3,383	2011	5,547
2013	5,185	2012	3,502
2014	6,906	2013	5,440
2015	4,919	2014	6,257
2016	2,892	2015	5,308
2017	2,789	2016	2,979
2018	3,900	2017	2,770
2019	1,249	2018	1,435
2020	560	2019	834
2021	357	2020	46
Total	\$ <u>136,364</u>	Total	\$ <u>141,279</u>

(4) Investments

Estimated fair value of investments in bonds and equities is based on quotations provided by widely accepted third-party data providers. In 2021 and 2020, Reuters (Refinitiv), Interactive Data Corporation (IDC), and Markit Partners were used to obtain fair market values. Additionally, in 2021 and 2020, the fair value of certain common trust funds was primarily determined by net asset value and common stock warrants were primarily determined by a widely accepted third-party vendor, followed by a hierarchy using broker/dealer quotes, including Bloomberg, Yield Book analytic model, and a benchmark to index model. Prior month price is used only when information is limited or unavailable.

(a) Bonds

The NAIC's Securities Valuation Office (SVO) assigns designations of bonds from 1 to 6. Bonds with designations of 1–2 are stated at amortized value using the interest method. Bonds with designations of 3–6 require the bond to be carried at the lower of amortized value or fair value, with any related unrealized loss reported in policyholders' surplus.

During 2021 and 2020, Pinnacol had investments in long-term bonds, which the NAIC's SVO assigned a 3 or higher designation. Carrying values are equal to the lower of amortized value or fair value for these bonds.

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The carrying value and the fair value of investments in long-term bonds in 2021 and 2020 are summarized as follows (in thousands). The carrying value includes investment grade bonds that are reported at amortized value and low rated bonds that are reported at the lower of cost or fair value:

	2021			
	Carrying value	Gross unrealized gains	Gross unrealized losses	Fair value
Government obligations:				
Nonloan-backed bonds	\$ 190,336	9,025	(427)	198,934
Loan-backed bonds	1,145	159	—	1,304
U.S. political subdivisions:				
Nonloan-backed bonds	16,412	1,186	(43)	17,555
Loan-backed bonds	—	—	—	—
U.S. special revenue:				
Nonloan-backed bonds	63,980	7,892	(116)	71,756
Loan-backed bonds	365,412	7,002	(4,140)	368,274
Industrial and miscellaneous:				
Nonloan-backed bonds	1,290,923	106,652	(3,645)	1,393,930
Loan-backed bonds	388,645	5,942	(1,947)	392,640
Hybrid securities:				
Nonloan-backed bonds	5,989	589	—	6,578
Loan-backed bonds	—	—	—	—
	<u>\$ 2,322,842</u>	<u>138,447</u>	<u>(10,318)</u>	<u>2,450,971</u>

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2020				
	Carrying value	Gross unrealized gains	Gross unrealized losses	Fair value
Government obligations:				
Nonloan-backed bonds	\$ 200,731	18,972	—	219,703
Loan-backed bonds	1,565	217	—	1,782
U.S. political subdivisions:				
Nonloan-backed bonds	14,705	1,874	—	16,579
Loan-backed bonds	—	—	—	—
U.S. special revenue:				
Nonloan-backed bonds	67,594	8,658	(59)	76,193
Loan-backed bonds	381,346	13,492	(183)	394,655
Industrial and miscellaneous:				
Nonloan-backed bonds	1,277,052	167,895	(742)	1,444,205
Loan-backed bonds	300,981	10,083	(1,502)	309,562
Hybrid securities:				
Nonloan-backed bonds	7,496	915	(3)	8,408
Loan-backed bonds	—	—	—	—
	<u>\$ 2,251,470</u>	<u>222,106</u>	<u>(2,489)</u>	<u>2,471,087</u>

The book/adjusted carrying value and estimated fair value of investments in long-term bonds at December 31, 2021, by contractual maturity, are shown in the following table (in thousands). Contractual maturities for investments such as mortgage-backed securities may differ from actual maturities because the borrower may have the right to call or prepay obligations with or without call or prepayment penalties.

2021		
	Book/adjusted carrying value	Fair value
Due in one year or less	\$ 30,167	30,533
Due after one year through five years	552,344	581,352
Due after five years through ten years	514,148	542,438
Due after ten years	470,981	534,430
Loan-backed and/or structured securities	755,202	762,218
	<u>\$ 2,322,842</u>	<u>2,450,971</u>

Proceeds from sales of investments in long-term bonds during 2021 and 2020 were approximately \$176,071,000 and \$233,171,000, respectively. Realized gains on long-term bonds of approximately \$11,677,000 and \$13,884,000 and realized losses of approximately (\$941,000) and (\$2,253,000) were recognized during 2021 and 2020, respectively.

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The following table provides the length of impairment for those investments in long-term bonds with an unrealized loss as of December 31, 2021 (in thousands):

Description of securities	Less than 12 months		12 months or greater		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Government obligations	\$ 8,077	(427)	—	—	8,077	(427)
U.S. political subdivisions	2,007	(43)	—	—	2,007	(43)
U.S. special revenue	207,780	(4,257)	—	—	207,780	(4,257)
Industrial and miscellaneous	326,284	(5,236)	36,715	(1,084)	362,999	(6,320)
Hybrid securities	198	(2)	—	—	198	(2)
Total	\$ 544,346	(9,965)	36,715	(1,084)	581,061	(11,049)

The following table provides the length of impairment for those investments in long-term bonds with an unrealized loss as of December 31, 2020 (in thousands):

Description of securities	Less than 12 months		12 months or greater		Total	
	Fair value	Unrealized losses	Fair value	Unrealized losses	Fair value	Unrealized losses
Government obligations	\$ —	—	—	—	—	—
U.S. political subdivisions	—	—	—	—	—	—
U.S. special revenue	34,479	(241)	—	—	34,479	(241)
Industrial and miscellaneous	122,654	(1,924)	32,627	(587)	155,281	(2,511)
Hybrid securities	388	(12)	—	—	388	(12)
Total	\$ 157,521	(2,177)	32,627	(587)	190,148	(2,764)

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(b) Loan-Backed and Structured Securities

Loan-backed securities are stated at amortized value or fair value based on their NAIC designation. The prospective method is used to value mortgage-backed securities. Prepayment assumptions for single class and multiclass mortgage-backed/asset-backed securities were obtained from widely accepted models with inputs from major third-party data providers. Any loan-backed and structured securities in an unrealized loss position were reviewed to determine whether an other-than-temporary impairment (OTTI) should be recognized at year-end. At December 31, 2021 and 2020, Pinnacol recognized approximately \$0 and \$3,073,000 in OTTI on loan-backed securities. Loan-backed and structured securities in an unrealized loss position as of year-end, stratified based on length of time continuously in these unrealized loss positions, are as follows (in thousands):

	2021	
	Aggregate amount of unrealized loss	Aggregate fair value of securities with unrealized loss
Less than 12 months	\$ (6,087)	389,468
12 months or longer	(60)	11,193
	<u>\$ (6,147)</u>	<u>400,661</u>

(c) Equities

Unrealized gains on investments in common stocks, mutual funds, and common trust funds are reported as a component of policyholders' surplus. For any decline in the fair value of equities, which is determined to be other than temporary, the resulting OTTI loss is recognized in the statement of operations. OTTI of common stocks, mutual funds, and common trust funds result in the establishment of a new, adjusted cost basis for such investments. The original cost, adjusted cost, net unrealized gains (measured against adjusted cost), and fair value of common stocks, mutual funds, and common trust funds are summarized as follows (in thousands):

	Original cost	Adjusted cost	Net unrealized gains	Fair value
December 31, 2021	\$ 337,664	331,772	124,537	456,309
December 31, 2020	378,175	368,440	104,708	473,148

The Company is a member of the Federal Home Loan Bank (FHLB) of Topeka. Through its membership, the Company may borrow an amount, which is dependent on the market value and risk related to investments that are held at FHLB. The Company has not conducted any borrowings with the FHLB as of December 31, 2021. As a requirement of the membership, Pinnacol owns FHLB Class A and Class B Capital Stock. In 2021, these assets totaled \$500,000 and \$30,500, respectively.

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(d) Mortgage Loans on Real Estate

The Company held approximately \$68,554,000 and \$45,066,000 of commercial mortgage loans at December 31, 2021 and 2020, respectively. Mortgage loans on real estate consist entirely of domestic commercial collateralized loans and are carried at their unpaid principal balances adjusted for any unamortized premiums or discounts, origination fees, provision allowances, and foreign currency translations. Interest income is accrued on the unpaid principal balance for all loans, except for loans on nonaccrual status. Premiums, discounts, and origination fees are amortized to net investment income using the effective-interest method.

A third-party manager actively manages the Company's mortgage loan portfolio by completing ongoing comprehensive analysis of factors, such as debt service coverage ratios, loan-to-value ratios, payment status, default or legal status, collateral property evaluations, and general market conditions. On a quarterly basis, the Company reviews any provided credit quality risk indicators in its internal assessment of loan impairment and credit loss.

Management's periodic evaluation and assessment for mortgage impairments is based on delinquency status, internally derived fair value, as well as credit concern status based on known and inherent risks in the portfolio, adverse situations that may affect the borrower's ability to repay, the fair value of the underlying collateral, composition of the loan portfolio, current economic conditions, loss experience, and other relevant factors. Risk is mitigated primarily through first lien collateralization, guarantees, loan covenants, and borrower reporting requirements. Since the Company does not hold uncollateralized mortgages, loans are generally deemed to be collectible. Any remaining unrecoverable amounts are written off during the final stage of the foreclosure process.

Loan balances are considered delinquent when payment has not been received based on contractually agreed-upon terms. The accrual of interest is discontinued when concerns exist regarding the realization of loan principal or interest. The Company resumes interest accrual on loans when a loan returns to current status or under new terms when loans are restructured or modified.

At December 31, 2021, the Company did not have any troubled, impaired, or delinquent mortgage loans, or any reason to believe payments would be uncollectible on any existing loans.

(e) Securities Lending Transactions

The Company participated in a securities lending program, whereby the Company lent securities, which were included in bonds and common stocks, to financial institutions (counterparties) in short-term arrangements. On March 13, 2020, the Company directed its agent bank to suspend securities lending activity in light of uncertain market conditions. Accordingly, all loaned securities were returned, and all repurchase agreements were terminated as of March 25, 2020. On November 12, 2020, the agreement with the agent bank was terminated, along with the third-party securities lending agreement on November 13, 2020.

(f) Other Invested Assets

Investments in partnerships are stated at the underlying audited equity value. For those investments in which the audited financial statements were not available by the March 1, 2021 statutory annual statement filing deadline, the unaudited equity value was used. Other invested assets total approximately \$202,744,000 and \$128,262,000 in 2021 and 2020, respectively, with \$199,224,000 and

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\$128,239,000 relating to investments in partnerships. Due to Colorado Revised Statutes limitations, the balance of other invested assets may not exceed 5% of admitted assets. At December 31, 2021, approximately \$45,772,000 was nonadmitted due to this requirement. The balance at December 31, 2020 did not exceed 5% of admitted assets. The Company has contributed \$139,522,000 in net capital (capital contributions, less capital distributions) since investing in partnerships and is responsible for up to an additional \$64,692,000.

(g) Impairment of Investments

The Company writes securities down to fair value that it deems to be OTTI in the period the securities are deemed to be so impaired. The Company records write-downs as realized capital losses and adjusts the cost basis of the securities, accordingly. The Company does not adjust the revised cost basis for subsequent recoveries in value.

The assessment of whether an OTTI occurred is based upon management's case-by-case evaluation of the underlying reasons for the decline in fair value. Management considers a wide range of factors, as described below, regarding the security issuer and uses its best judgment in evaluating the cause of the decline in its estimated fair value and in assessing the prospects for near term recovery. Inherent in management's evaluation of the security are assumptions and estimates about the operations and future earnings potential of the issuer.

Considerations used by the Company in the impairment evaluation process include, but are not limited to, the following:

- Fair value is significantly below cost.
- The decline in fair value is attributable to specific adverse conditions affecting a particular instrument, its issuer, an industry, or geographic area.
- The decline in fair value has existed for an extended period of time.
- A debt security has been downgraded by a credit rating agency.
- The financial condition of the issuer has deteriorated.
- A change in future expected cash flow has occurred.
- Dividends have been reduced or eliminated or scheduled interest payments have not been made.
- The ability and intent to hold investments until recovery, including consideration of the investment manager's discretion to sell securities.
- The present value of projected cash flows expected to be collected is less than amortized value of loan-backed and structured securities.

While all available information is taken into account, it is difficult to predict the ultimate recoverable amount from a distressed or impaired security.

At December 31, 2021 and 2020, 5.19% and 5.11% of long-term bonds held by the Company were rated noninvestment grade, respectively. At December 31, 2021 and 2020, the Company had approximately \$11,049,000 and \$2,765,000, respectively, of unrealized losses related to its long-term

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bonds. The unrealized losses on securities are primarily attributable to fluctuations in market interest rates and changes in credit spreads since the securities were acquired.

(h) *Other-Than-Temporary Impairment*

During 2021 and 2020, the Company recognized approximately \$902,000 and \$10,244,000, respectively, in OTTI on long-term bonds, and \$10,000 and \$8,517,000, respectively, in OTTI on common stocks, mutual funds, and common trust funds.

(i) *Fair Value Measurements*

The Company has categorized its assets and liabilities that are reported on the statutory-basis statements of admitted assets, liabilities, and policyholders' surplus at fair value into the three-level fair value hierarchy. The three-level fair value hierarchy is based on the degree of subjectivity inherent in the valuation method by which fair value was determined. The three levels are defined as follows.

- Level 1 – Quoted prices in active markets for identical assets and liabilities: This category, for items measured at fair value on a recurring basis includes common stocks, preferred stocks, and money market mutual funds. The estimated fair value of the equity securities within this category are based on quoted prices in active markets and are thus classified as Level 1.
- Level 2 – Significant other observable inputs: This category for items measured at fair value on a recurring basis includes bonds and common stocks, which are not exchange traded. The estimated fair values of some of these items were determined by independent pricing services using observable inputs. Others were based on quotes from markets, which were not considered actively traded.
- Level 3 – Significant unobservable inputs: This category for items measured at fair value includes common stocks, common stock warrants, preferred stocks, and bonds. The estimated fair value of common stock warrants and bonds was determined by internal ratings in the absence of observable inputs.

The following table represents (in thousands) information about the Company's financial assets measured at fair value in Level 3 as of December 31, 2021.

<u>Assets</u>	<u>Fair value measurements – Level 3</u>						
	<u>Beginning balance, January 1, 2021</u>	<u>Amortization accretion</u>	<u>Current realized net income (loss)</u>	<u>Change in unrealized surplus</u>	<u>Purchases/ transfers into Level 3</u>	<u>Sales/ settlements/ transfers out of Level 3</u>	<u>Ending balance, December 31, 2021</u>
Bonds – private placements \$	—	—	25	(386)	2,297	(1,936)	—
All other bonds	1,217	—	3	33	—	(1,253)	—
Common stocks – industrial and miscellaneous	650	—	9	28	100	(16)	771
Total assets \$	<u>1,867</u>	<u>—</u>	<u>37</u>	<u>(325)</u>	<u>2,397</u>	<u>(3,205)</u>	<u>771</u>

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The following table represents (in thousands) information about the Company's financial assets measured at fair value in Level 3 as of December 31, 2020.

Fair value measurements – Level 3 December 31, 2020							
Assets	Beginning balance January 1, 2020	Amortization accretion	Current realized net income (loss)	Change in unrealized surplus	Purchases/ transfers into Level 3	Sales/ settlements/ transfers out of Level 3	Ending balance December 31, 2020
Bonds – bank loans	\$ 94	1	(49)	7	19	(72)	—
All other bonds	—	—	75	605	11,978	(11,441)	1,217
Common stocks – industrial and miscellaneous	132	—	58	29	538	(107)	650
Total assets	\$ 226	1	84	641	12,535	(11,620)	1,867

The following tables present (in thousands) information about the Company's financial assets measured at fair value on a recurring basis for accounting purposes as of December 31, 2021 and 2020, respectively, and indicates the fair value hierarchy of the valuation techniques utilized by the Company to determine such fair value:

Fair value measurements – recurring basis December 31, 2021				
Assets	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Common stocks:				
Industrial and miscellaneous	\$ 525	—	772	1,297
Common trust funds	—	124,396	—	124,396
Mutual funds	257,694	72,922	—	330,616
Total common stocks	258,219	197,318	772	456,309
Perpetual preferred stocks	652	—	—	652
Redeemable preferred stocks	—	—	—	—
Money market mutual funds	19,975	—	—	19,975
Total assets	\$ 278,846	197,318	772	476,936

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Fair value measurements – recurring basis				
December 31, 2020				
Assets	Quoted prices in active markets for identical assets (Level 1)	Significant other observable inputs (Level 2)	Significant unobservable inputs (Level 3)	Total
Common stocks:				
Industrial and miscellaneous	\$ 363	—	650	1,013
Common trust funds	—	127,968	—	127,968
Mutual funds	276,731	67,436	—	344,167
Total common stocks	277,094	195,404	650	473,148
Perpetual preferred stocks	187	—	—	187
Redeemable preferred stocks	—	—	—	—
Money market mutual funds	30,849	—	—	30,849
Total assets	\$ 308,130	195,404	650	504,184

Certain assets are measured at fair value on a nonrecurring basis quarterly or more frequently if events dictate that the carrying value of the asset may not be recovered. These assets include bonds held at fair value with an NAIC designation of 3–6 and redeemable preferred stocks held at fair value with an NAIC designation of RP3–RP6. There were bonds with these designations where the fair value was less than amortized value, which resulted in an unrealized loss of \$730,000 at December 31, 2021 and \$277,000 at December 31, 2020.

The following tables reflect (in thousands) the fair values and admitted values of all admitted assets and liabilities that are financial instruments, excluding those accounted for under the equity method as

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of December 31, 2021 and 2020, respectively. The fair values are also categorized into the three-level fair value hierarchy as described above.

December 31, 2021					
Type of financial instrument	Fair value	Admitted value	Level 1	Level 2	Level 3
Financial instruments – assets:					
Long-term bonds:					
CDOs/CBOs/CLOs	\$ 191,937	190,055	—	191,937	—
Private placements	138,948	134,476	—	—	138,948
All other bonds	2,120,086	1,998,311	—	2,039,648	80,438
Total long-term bonds	<u>2,450,971</u>	<u>2,322,842</u>	<u>—</u>	<u>2,231,585</u>	<u>219,386</u>
Preferred stocks:					
Perpetual preferred	754	752	754	—	—
Redeemable preferred	—	—	—	—	—
Total preferred stocks	<u>754</u>	<u>752</u>	<u>754</u>	<u>—</u>	<u>—</u>
Common stocks:					
Industrial and miscellaneous	1,297	1,297	525	—	771
Common trust funds	124,396	124,396	—	124,396	—
Mutual funds	330,616	330,616	257,695	72,922	—
Total common stocks	<u>456,309</u>	<u>456,309</u>	<u>258,220</u>	<u>197,318</u>	<u>771</u>
Mortgage loans	68,511	68,554	—	—	68,511
Cash, cash equivalents, and short-term investments	53,273	53,272	53,273	—	—
Total assets	<u>\$ 3,029,818</u>	<u>2,901,729</u>	<u>312,247</u>	<u>2,428,903</u>	<u>288,668</u>

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Type of financial instrument	December 31, 2020				
	Fair value	Admitted value	Level 1	Level 2	Level 3
Financial instruments – assets:					
Long-term bonds:					
CDOs/CBOs/CLOs	\$ 192,519	190,268	—	192,519	—
Private placements	101,549	93,790	—	—	101,549
All other bonds	2,177,019	1,967,412	—	2,122,357	54,662
Total long-term bonds	2,471,087	2,251,470	—	2,314,876	156,211
Preferred stocks:					
Perpetual preferred	709	657	709	—	—
Redeemable preferred	4	3	4	—	—
Total preferred stocks	713	660	713	—	—
Common stocks:					
Industrial and miscellaneous	1,013	1,013	363	—	650
Common trust funds	127,968	127,968	—	127,968	—
Mutual funds	344,167	344,167	276,731	67,436	—
Total common stocks	473,148	473,148	277,094	195,404	650
Mortgage loans	44,922	45,066	—	—	44,922
Cash, cash equivalents, and short-term investments	70,334	70,331	70,027	307	—
Total assets	\$ 3,060,204	2,840,675	347,834	2,510,587	201,783

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(j) *Investment Income*

Major categories of net investment income (expense) for the years ended December 31, 2021 and 2020 are summarized as follows (in thousands):

	2021	2020
Investment income (expense):		
Corporate and miscellaneous bonds	\$ 73,119	71,888
U.S. government bonds	4,147	4,578
Cash and other investments	12	882
Real estate	5,646	5,656
Other invested assets	11,031	5,556
Mortgage loans	2,526	1,753
Equity securities	13,400	9,094
Securities lending income	—	49
Surplus note interest expense	(11,101)	(8,625)
Investment expenses	(7,607)	(8,319)
Net investment income earned	91,173	82,512
Net realized capital gain (loss):		
Corporate and miscellaneous bonds	9,834	1,261
U.S. government bonds	—	126
Equity securities	39,583	56,810
Cash and other investments	—	21
Net realized capital gains	49,417	58,218
Net investment income	\$ 140,590	140,730

(5) **Reinsurance**

Ceded Reinsurance – Pinnacol purchases excess of loss reinsurance with two layers and terrorism coverage. The reinsurance coverage for individual workers' compensation accidents was as follows:

- Layer 1 – Limit of \$20,000,000 in excess of retention of \$20,000,000 per occurrence
- Layer 2 – Limit of \$40,000,000 in excess of retention of \$40,000,000 per occurrence
- Terrorism Only – Limit of \$50,000,000 in excess of retention of \$80,000,000 per occurrence

Management is not aware of any loss nor did the Company record any loss great enough to attach to these layers during any of the prior policy periods.

Reinsurance contracts do not relieve Pinnacol of its obligations, and a failure of the reinsurer to honor its obligations could result in losses unreimbursed to Pinnacol. Pinnacol evaluates and monitors the financial

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condition of its reinsurers to minimize its exposure to loss from reinsurer insolvency. Management of Pinnacol believes its reinsurers are financially sound and will continue to meet their contractual obligations.

Pinnacol uses Lloyd's Syndicates as part of its ceded reinsurer program. The Syndicates are generally not rated by AM Best. The remaining reinsurers had the following AM Best ratings at December 31, 2021:

<u>Reinsurer</u>	<u>AM Best rating</u>
Allied World Assurance Company, Limited	A
Arch Reinsurance Company	A+
Endurance Specialty Insurance Limited	A+
Convex Insurance UK Limited	A-
Lloyd's Syndicate 3000 (Markel Syndicate Management Limited)	A

Assumed Reinsurance – Pinnacol has entered into assumed reinsurance contracts that allow the Company to provide insurance coverage under the workers' compensation provisions of other states for the employees of Colorado companies who work outside of Colorado (Other States Coverage). Effective March 1, 2004, Pinnacol executed a reinsurance contract with Argonaut Insurance Company for Other States Coverage. The contract was canceled in 2010; however, Pinnacol will continue to pay existing claims in accordance with this reinsurance agreement until these claims are closed or these risks are transferred. As the Company entered into a reinsurance agreement in 2010 with Zurich American Insurance Company, there were no gaps in coverage. This agreement was still in effect as of December 31, 2021. The Other States Coverage contracts are designed as 100% quota share arrangements with Pinnacol acting as the assuming company. Premium revenue is recognized pro rata over the period the policy is effective.

Funds have been placed on deposit as collateral with Argonaut Insurance Company and Zurich American Insurance Company in the amount of \$4,491,000 and \$4,582,000 in 2021 and 2020, respectively.

A Letter of Credit has been posted to Argonaut Insurance Company in the amount of \$4,715,000 and \$5,368,000 in 2021 and 2020, respectively.

Assets have been pledged in a trust to Zurich American Insurance Company in the amount of \$20,755,000 and \$20,898,000 in 2021 and 2020, respectively.

Pinnacol held unearned premium reserves related to assumed business of \$884,000 and \$762,000 for the years ended December 31, 2021 and 2020, respectively. Pinnacol had loss and loss adjustment expense reserves related to assumed business of \$19,645,000 and \$17,970,000 for the years ended December 31, 2021 and 2020, respectively.

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The following reinsurance activity has been recorded in the accompanying statutory-basis financial statements (in thousands):

	2021	2020
Direct premiums written	\$ 539,424	512,025
Premiums ceded	(1,427)	(1,256)
Premiums assumed	10,096	9,639
Net premiums written	\$ 548,092	520,408
Direct premiums earned	\$ 540,261	519,589
Premiums ceded	(1,427)	(1,256)
Premiums assumed	9,973	9,957
Net premiums earned	\$ 548,807	528,291
Direct losses incurred	\$ 300,175	305,396
Losses ceded	—	—
Losses assumed	6,538	3,967
Net losses incurred	\$ 306,712	309,363
Direct loss adjustment expenses incurred	\$ 79,193	76,354
Loss adjustment expenses ceded	—	—
Loss adjustment expenses assumed	1,165	1,160
Net loss adjustment expenses incurred	\$ 80,358	77,513

(6) Employee Benefits

(a) *Defined-Benefit Pension Plan through the State of Colorado*

Pensions – Pinnacol participates in the State Division Trust Fund (SDTF), a cost-sharing multiple-employer defined-benefit pension fund administered by the Public Employees' Retirement Association of Colorado (PERA). The net pension liability, deferred outflows of resources, and deferred inflows of resources related to pensions, pension expense, information about the fiduciary net position, and additions to/deductions from the fiduciary net position of the SDTF have been determined using the economic resources measurement focus and the accrual basis of accounting. For this purpose, benefit payments (including refunds of employee contributions) are recognized when due and payable in accordance with the benefit terms. Investments held by the SDTF are reported at fair value.

The Colorado General Assembly passed significant pension reform through Senate Bill (SB) 18-200: *Concerning Modifications to the Public Employees' Retirement Association Hybrid Defined Benefit Plan Necessary to Eliminate with a High Probability the Unfunded Liability of the Plan Within the Next Thirty Years*. The bill was signed into law by Governor Hickenlooper on June 4, 2018. SB 18-200 makes changes to certain benefit provisions. Most of these changes were in effect as of December 31, 2021.

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Plan description – All Pinnacol employees are provided with pensions through the SDTF – a cost-sharing multiple-employer defined-benefit pension plan administered by PERA. Plan benefits are specified in Title 24, Article 51 of the Colorado Revised Statutes (C.R.S.), administrative rules set forth at 8 C.C.R. 1502 1, and applicable provisions of the federal Internal Revenue Code. Colorado State law provisions may be amended from time to time by the Colorado General Assembly. PERA issues a publicly available comprehensive annual financial report (Annual Report) that can be obtained at <https://www.copera.org/investments/pera-financial-reports>.

Benefits provided – PERA provides retirement, disability, and survivor benefits. Retirement benefits are determined by the amount of service credit earned and/or purchased, highest average salary, the benefit structure(s) under which the member retires, the benefit option selected at retirement, and age at retirement. Retirement eligibility is specified in tables set forth at C.R.S. § 24-51-602, 604, 1713, and 1714.

The lifetime retirement benefit for all eligible retiring employees under the PERA benefit structure is the greater of the:

- Highest average salary multiplied by 2.5% and then multiplied by years of service credit.
- Value of the retiring employee's member contribution account plus a 100% match on eligible amounts as of the retirement date. This amount is then annuitized into a monthly benefit based on life expectancy and other actuarial factors.

In all cases, the service retirement benefit is limited to 100% of highest average salary and also cannot exceed the maximum benefit allowed by federal Internal Revenue Code.

Members may elect to withdraw their member contribution accounts upon termination of employment with all PERA employers; waiving rights to any lifetime retirement benefits earned. If eligible, the member may receive a match of either 50% or 100% on eligible amounts depending on when contributions were remitted to PERA, the date employment was terminated, whether five years of service credit has been obtained, and the benefit structure under which contributions were made.

Benefit recipients who elect to receive a lifetime retirement benefit are generally eligible to receive postretirement cost-of-living adjustments (COLAs), referred to as annual increases in the C.R.S., once certain criteria are met. Pursuant to SB 18-200, eligible benefit recipients under the PERA benefit structure who began membership before January 1, 2007, will receive an annual increase of 1.25% unless adjusted by the automatic adjustment provision (AAP) pursuant C.R.S. § 24-51-413. Eligible benefit recipients under the PERA benefit structure who began membership on or after January 1, 2007, will receive the lesser of an annual increase of 1.25% or the average of the Consumer Price Index for Urban Wage Earners and Clerical Workers for the prior calendar year, not to exceed 10% of PERA's Annual Increase Reserve (AIR) for the SDTF. The AAP may raise or lower the aforementioned annual increase by up to 0.25% based on the parameters specified in C.R.S. § 24-51-413.

Disability benefits are available for eligible employees once they reach five or more years of earned service credit and are determined to meet the definition of disability. The disability benefit amount is based on the retirement benefit formula(s) shown above considering a minimum 20 years of service credit, if deemed disabled.

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Survivor benefits are determined by several factors, which include the amount of earned service credit, highest average salary of the deceased, the benefit structure(s) under which service credit was obtained, and the qualified survivor(s) who will receive the benefits.

Contributions – Eligible employees of Pinnacol and the State are required to contribute to the SDTF at a rate set by Colorado statute. The contribution requirements are established under C.R.S. § 24-51-401, *et seq* and C.R.S. § 24-51-413. Eligible employees were required to contribute 10.00% of their PERA-includable salary until June 30, 2021; thereafter, the contribution increased to 10.50% of PERA-includable salary. The employer contribution requirements for Pinnacol are summarized in the table below:

	For the year ended December 31		
	2021	2020	2019
Employer contribution rate (includes 1.02% allocation to the Health Care Trust Fund – see note 6c) ¹	10.90 %	10.90 %	10.40 %
Amortization equalization Disbursement (AED) as specified in C.R.S. §24-51-411 ¹	5.00	5.00	5.00
Supplemental amortization Equalization disbursement (SAED) as specified in C.R.S., §24-51-411 ¹	5.00	5.00	5.00
Defined Contribution Supplement as specified in C.R.S. §24-51-415	0.05	—	—
Total employer contribution rate ¹	20.95 %	20.90 %	20.40 %

¹ Contribution rates are expressed as a percentage of salary as defined in C.R.S. § 24-51-101(42).

As specified in C.R.S. § 24-51-414, the State is required to contribute \$225,000,000 each year to PERA starting on July 1, 2018. A portion of the direct distribution payment is allocated to the SDTF based on the proportionate amount of annual payroll of the SDTF to the total annual payroll of the SDTF, School Division Trust Fund, Judicial Division Trust Fund, and Denver Public Schools (DPS) Division Trust Fund. House Bill (HB) 20-1379 suspended the \$225,000,000 direct distribution payable on July 1, 2020 for the state's 2020-21 fiscal year.

Employer contributions are recognized by the SDTF in the period in which the compensation becomes payable to the member and Pinnacol is statutorily committed to pay the contributions to the SDTF. Employer contributions recognized by the SDTF from Pinnacol were \$13,590,000 and \$13,249,000, for the years ended December 31, 2021 and 2020, respectively. These contributions met the contribution requirement for each year.

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(b) Voluntary Tax Deferred Retirement Plans

Plan description – Employees of Pinnacol that are also members of the SDTF may voluntarily contribute to the Voluntary Investment Program, an Internal Revenue Code Section 401(k) defined-contribution plan administered by PERA. Title 24, Article 51, Part 14 of the C.R.S., as amended, assigns the authority to establish the Plan provisions to the PERA Board of Trustees. PERA issues a publicly available Annual Report, which includes additional information on the Voluntary Investment Program. That report can be obtained at <https://www.copera.org/investments/pera-financial-reports>.

Funding policy – The Voluntary Investment Program is funded by voluntary member contributions up to the maximum limits set by the Internal Revenue Service, as established under Title 24, Article 51, Section 1402 of the C.R.S., as amended. In addition, Pinnacol has agreed to match employee's elective contributions into the PERA 401(k) Plan at 50% up to the first 6% of employees' elected deferrals. Employees are immediately vested in their own contributions, employer contributions, and investment earnings. For the years ended December 31, 2021 and 2020, Pinnacol contributed approximately \$1,564,000 and \$1,569,000, respectively, in matching contributions to the PERA 401(k) Plan. Pinnacol also offers a 457 deferred compensation plan.

(c) Defined-Benefit Other Postemployment Benefit (OPEB) Plan

OPEB plan – Pinnacol participates in the Health Care Trust Fund (HCTF), a cost-sharing multiple-employer defined-benefit OPEB plan administered by PERA.

Plan description – The HCTF is established under Title 24, Article 51, Part 12 of the C.R.S., as amended. Colorado State law provisions may be amended from time to time by the Colorado General Assembly. Title 24, Article 51, Part 12 of the C.R.S., as amended, sets forth a framework that grants authority to the PERA Board to contract, self-insure, and authorize disbursements necessary in order to carry out the purposes of the PERACare program, including the administration of the premium subsidies. Colorado State law provisions may be amended from time to time by the Colorado General Assembly. PERA issues a publicly available comprehensive annual financial report (Annual Report) that can be obtained at <https://www.copera.org/investments/pera-financial-reports>.

Benefits provided – The HCTF provides a healthcare premium subsidy to eligible participating PERA benefit recipients and retirees who choose to enroll in one of the PERA healthcare plans; however, the subsidy is not available if only enrolled in the dental and/or vision plan(s). The healthcare premium subsidy is based upon the benefit structure under which the member retires and the member's years of service credit. The basis for the amount of the premium subsidy funded by each trust fund is the percentage of the member contribution account balance from each division, as it relates to the total member contribution account balance from which the retirement benefit is paid.

C.R.S. § 24-51-1202 *et seq.* specifies the eligibility for enrollment in the healthcare plans offered by PERA and the amount of the premium subsidy. The law governing a benefit recipient's eligibility for the subsidy and the amount of the subsidy differs slightly depending under which benefit structure the benefits are calculated. All benefit recipients under the PERA benefit structure are eligible for a premium subsidy, if enrolled in a healthcare plan under PERACare.

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Enrollment in the PERACare is voluntary and is available to benefit recipients and their eligible dependents, certain surviving spouses, and divorced spouses and guardians, among others. Eligible benefit recipients may enroll into the program upon retirement, upon the occurrence of certain life events, or on an annual basis during an open enrollment period.

PERA benefit structure – The maximum service-based premium subsidy is \$230 per month for benefit recipients who are under 65 years of age and who are not entitled to Medicare; the maximum service-based subsidy is \$115 per month for benefit recipients who are 65 years of age or older or who are under 65 years of age and entitled to Medicare. The maximum service-based subsidy, in each case, is for benefit recipients with retirement benefits based on 20 or more years of service credit. There is a 5% reduction in the subsidy for each year less than 20. The benefit recipient pays the remaining portion of the premium to the extent the subsidy does not cover the entire amount.

For retirees who have not participated in Social Security and who are not otherwise eligible for premium-free Medicare Part A for hospital-related services, C.R.S. § 24-51-1206(4) provides an additional subsidy. According to the statute, PERA cannot charge premiums to benefit recipients without Medicare Part A that are greater than premiums charged to benefit recipients with Part A for the same plan option, coverage level, and service credit. Currently, for each individual PERACare enrollee, the total premium for Medicare coverage is determined assuming plan participants have both Medicare Part A and Part B and the difference in premium cost is paid by the HCTF on behalf of benefit recipients not covered by Medicare Part A.

Contributions – Pursuant to Title 24, Article 51, Section 208(1) (f) of the C.R.S., as amended, certain contributions are apportioned to the HCTF. PERA-affiliated employers are required to contribute at a rate of 1.02% of PERA-includable salary into the HCTF. Pinnacol's contribution is included in the contribution rate of 20.95% in note 6(a). No member contributions are required to the HCTF. The contribution requirements for Pinnacol are established under Title 24, Article 51, Part 4 of the C.R.S., as amended. For the years ended December 31, 2021 and 2020, Pinnacol contributions to the HCTF were approximately \$662,000 and \$655,000, respectively, equal to the required contributions for each year.

(d) Other

Health and Welfare Trust – Effective January 1, 2010, Pinnacol entered into certain self-funded benefit programs with its vendors for healthcare, dental care, and vision care and established a separate legal trust for administrative purposes. In 2019, Pinnacol also entered into a guaranteed cost program with one of its two healthcare vendors. Pinnacol withholds monthly premium from its employee participants' payroll checks and uses these premiums and the employer contribution amounts to fund the trust account. These premiums are used to reimburse medical claims paid by the third-party vendors for the self-funded programs or pay premiums to the healthcare vendor for the guaranteed cost program. Employer contributions in 2021 and 2020 were \$7,182,000 and \$7,019,000, respectively.

Accrued Paid Leave – Pinnacol employees may accrue paid time off based on their length of service subject to certain limitations on the amount that will be paid upon termination or taken in future periods. Paid time off is recorded as an expense and a liability at the time the paid time off is earned. The estimated liability for cumulative accrued paid time off of approximately \$4,262,000 and \$4,391,000 at December 31, 2021 and 2020, respectively, is included in other liabilities in the statutory-basis statements of admitted assets, liabilities, and policyholders' surplus.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

(7) Policyholders' Surplus

The board of directors declared general policyholder dividends in 2021 of \$90,000,000 and 2020 of \$10,000,000. In March 2021, Pinnacol paid general policyholder dividends in the amount of \$50,000,000 to policyholders in good standing. On November 3, 2021, the Board of Directors declared a general policyholder dividend to be paid in March 2022 of approximately \$40,000,000. On February 23, 2022, the Board of Directors determined the final amount of the general policyholder dividend paid in March 2022 to be \$50,000,000 based on year-end 2021 financial results.

The Division monitors a company's "risk-based capital" in assessing the financial strength of an insurance company. Pinnacol's level of surplus exceeds the "company action level" of risk-based capital, which is approximately \$204,818,000 for 2021.

A surplus note in the amount of \$100,000,000 was issued on June 25, 2014, to an unaffiliated third party in exchange for cash. Each payment of principal and interest on the surplus note may be made only with the prior approval of the Division and only to the extent Pinnacol has sufficient policyholders' surplus to make such payment. The interest on the unpaid principal amount of this note will be paid in semiannual installments at the rate of 8.625% per annum. Upon obtaining approval from the Commissioner of the Division on October 21, 2021, Pinnacol repurchased \$8,000,000 of its outstanding \$100,000,000 surplus note on October 28, 2021, by paying the noteholder cash consideration equal to 131% of the principal repurchased plus accrued interest. In 2021, \$11,101,000 of interest was paid on the note and recorded as investment expense. The note, which is subordinate to the prior payment of all other liabilities of the Company, will be due and payable twenty years from the issuance date, with an optional prepayment date in whole or part in fifteen years with no penalty. The surplus note was issued to partially cover Pinnacol's estimated proportionate share of PERA's unfunded liability for vested service of Pinnacol employees and retirees. This liability is not required to be recorded in the statutory-basis financial statements as of December 31, 2021, but it reduces the capital adequacy assessments of outside rating agencies, such as A.M. Best. In accordance with the note agreement, Pinnacol may apply the proceeds for general corporate purposes.

The surplus note agreement contains customary affirmative and negative covenants and requires that Pinnacol maintain certain specified ratios and thresholds. Among others, these covenants include maintaining a maximum writing ratio, debt to capitalization ratio, and interest coverage ratio. Management believes that Pinnacol is in compliance with such covenants, ratios, and thresholds at December 31, 2021.

As discussed in note 1(w), the Company participates in a cost-sharing multiple-employer defined-benefit pension plan administered by PERA. The funded portion of PERA's total pension liability as of December 31, 2020 is 59.1%. The Company has a special surplus fund to identify its portion of the unfunded pension benefits. The discount rate is 7.25%. Based on information provided by PERA as of July 2021, the Company's special surplus fund for the unfunded pension benefits has increased by \$11,671,000 from \$173,941,000 in 2020 to a new balance of \$185,611,000 for 2021. There are no limitations for using the special surplus fund for policyholders, injured workers, or other creditors.

As discussed in note 1(w), the Company participates in the Health Care Trust Fund (HCTF) administered by PERA. The Company has identified its portion of the HCTF liability in a special surplus fund in the same manner as the PERA net pension liability obligation. The HCTF liability has decreased by \$1,389,000 from \$7,989,000 in 2020 to a new balance of \$6,600,000 for 2021.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

(8) Commitments and Contingencies

Pinnacol has made the following commitments:

<u>Total Contingent Liabilities</u>	<u>2021</u>
Pinnacol has committed to fund partnerships investments	\$ 64,692,000
Pinnacol has committed to rated note investments	11,682,000
Pinnacol has committed to mortgage loan investments	<u>6,708,000</u>
Total	<u>\$ 83,082,000</u>

Lawsuits arise against the Company in the normal course of business. Contingent liabilities arising from litigation and other matters are not considered material in relation to the financial position of the Company.

At December 31, 2021 and 2020, Pinnacol had a letter of credit for the benefit of Argonaut Insurance Company under an assumed reinsurance agreement for approximately \$4,715,000 and \$5,368,000, respectively. This reinsurance agreement allows Argonaut Insurance Company to draw upon the letter of credit, which is 100% collateralized, at any time to secure any of Pinnacol's obligations under the agreement. Included in long-term bonds and money market securities are amounts held as collateral for the letter of credit of approximately \$10,085,000 and \$10,096,000, compared to a requirement of \$4,715,000 and \$5,368,000, as of December 31, 2021 and 2020, respectively.

At December 31, 2021 and 2020, Pinnacol had a trust for the benefit of Zurich American Insurance Company under an assumed reinsurance agreement. This reinsurance agreement allows Zurich American Insurance Company, the beneficiary, to claim the trust assets at any time to secure any of Pinnacol's obligations under the agreement. Included in long-term bonds are amounts held in the trust of approximately \$20,755,000 and \$20,898,000 as of December 31, 2021 and 2020. These bonds had a total market value of approximately \$21,833,000 and \$22,941,000 as of December 31, 2021 and 2020, which Zurich American Insurance Company deemed sufficient to secure Pinnacol's obligations under the agreement.

Pinnacol is contingently liable for approximately \$33,380,000 of claims closed by the purchase of annuities from life insurers for structured settlements. Pinnacol has not purchased annuities from life insurers under which the Company is payee, and therefore, no balances are due from such annuity insurers.

Pinnacol is aware of an unfunded net pension liability. If Pinnacol were to partially or fully leave the PERA program, the unfunded net pension liability for the vested service of Pinnacol employees and retirees would become immediately due to PERA. Title 24, Article 51, Section 316 of the C.R.S. requires a company to calculate the reserve transfer necessary when an employer disaffiliates from PERA. The formula to calculate the termination liability differs significantly from the formula used to calculate Pinnacol's share of the unfunded pension obligation under GASB 68. Therefore, the amount of a possible future termination liability is unknown but is expected to exceed \$200,000,000. Currently, the possibility of the Company partially or fully leaving the PERA program is remote and would require legislative action.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

(9) Related-Party Transactions

There was a loan agreement between Pinnacol and Cake that was deemed uncollectible. The full balance of the loan was accordingly reported as a realized loss as of December 31, 2019. Due to the uncollectibility of the loan and accrued interest, the loan agreement was terminated in 2020.

As of December 31, 2021, the value of Pinnacol's investment in Cake is \$0, which was a result of Cake's negative equity position at the time of impairment. Currently, Pinnacol's share of losses exceeds its investment. However, Pinnacol does not have any obligation or guarantee related to this investment. The losses are summarized in the table below:

Entity	Pinnacol's share of net income (loss)	Accumulated share of net income (losses)	Pinnacol's share of equity, including negative equity	Guaranteed obligation commitment for financial support (yes/no)	Reported value
Cake Insure, Inc.	\$ (9,915,000)	(9,915,000)	1,980,000	No	—

Under a program administrator agreement approved by the Division, Cake writes policies for Pinnacol through its digital platform that potential policyholders can utilize to receive a quote and bind a policy. Pinnacol pays Cake program administration fees on premium that Cake generates organically or through a referral program with Pinnacol and makes payments to Cake monthly as policies are generated. During 2021, Pinnacol incurred \$888,000 in program administrator fees.

PINNACOL ASSURANCE

Notes to Statutory-Basis Financial Statements

December 31, 2021 and 2020

Pinnacol is currently leveraging Cake's research and software development to transform Pinnacol's business and reimagine enterprise-wide systems. The use of this technology will allow Pinnacol to operate a digital platform for multiple distribution channels while continuing to build digital capabilities for all policies.

Under a management service agreement approved by the Division, Pinnacol provides certain personnel services to its subsidiary for a variable monthly fee and receives reimbursement for costs Cake incurred. During 2021, Pinnacol received \$523,000 in management fees and reimbursed costs from its subsidiary. The management fees offset various expenses in the income statement.

At December 31, 2021, Pinnacol reported \$64,000 due to subsidiary for commissions due to Cake as an agent. Pinnacol also reported \$74,000 due from subsidiary for management fees and reimbursable expenses under the management service agreement.

There were no transactions with affiliates in amounts that exceeded 0.5% of the total admitted assets of Pinnacol.

(10) Subsequent Events

The board of directors declared general policyholder dividends on November 3, 2021 in an amount to be approximately \$40,000,000. The final dividend amount of \$50,000,000 was confirmed by the Board in February 2022 and subsequently paid in March 2022.

Subsequent events have been evaluated through May 18, 2022, the date these statutory-basis financial statements were available to be issued.

**SUPPLEMENTAL SCHEDULES OF INVESTMENT AND
REINSURANCE INFORMATION**
(See Independent Auditors' Report)

PINNACOL ASSURANCE
Supplemental Schedule of Investment Information
Investment Risks Interrogatories
Year ended December 31, 2021
(In thousands)

1. Pinnacol's total admitted assets as reported on page 2 of its annual statement are: \$ 3,139,438
2. The following are the ten largest exposures to a single issuer/borrower/investment by investment category, excluding: (i) U.S. government securities, U.S. government agency securities, and those U.S. government money market funds listed in the Appendix to the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* as exempt, (ii) property occupied by Pinnacol, (iii) policy loans, and (iv) all SEC and foreign registered funds (open-end, closed-end, UIT and ETFs) and common trust funds that are diversified within the meaning of the Investment Company Act of 1940 (Section 5(b) (1)).

Issuer	Description of exposure	Amount	Percentage of total admitted assets
2.01 Federal National Mortgage Association	MBS	\$ 246,484	7.851%
2.02 Federal Home Loan Mortgage Corporation	CMO, MBS	118,928	3.788
2.03 NB Pinnacol Assurance Fund LP	Sch BA-Joint Venture	93,604	2.982
2.04 Deerpath Newbury Partners LLC	Bonds, Sch BA-Joint Venture	25,225	0.803
2.05 Lending Ark Asia Secured Private Debt Fund I, LP	Bonds, Sch BA-Joint Venture	22,160	0.706
2.06 First Eagle DIV-A Funding LLC	Bonds, Sch BA-Joint Venture	16,903	0.538
2.07 Blue Ocean Income Fund LP	Bonds, Sch BA-Joint Venture	15,144	0.482
2.08 GCM Grosvenor Special Opportunities Fund, Ltd.	Sch BA-Joint Venture	14,685	0.468
2.09 Alphabet Inc	Bonds, Equities	14,107	0.449
2.10 GCM Grosvenor Opportunistic Credit Fund V, Ltd.	Sch BA-Joint Venture	13,856	0.441

3. Pinnacol's total admitted assets held in bonds and preferred stocks by NAIC designation are:

NAIC Designation	Amount	Percentage of total admitted assets
Bonds:		
NAIC-1	\$ 1,607,146	51.192%
NAIC-2	595,208	18.959
NAIC-3	54,602	1.739
NAIC-4	44,868	1.429
NAIC-5	17,768	0.566
NAIC-6	3,250	0.104
Preferred stocks:		
P/RP-1	0	—
P/RP-2	183	0.006
P/RP-3	385	0.012
P/RP-4	100	0.003
P/RP-5	84	0.003
P/RP-6	0	—
	<u>\$ 2,323,594</u>	

4. Assets held in foreign investments are \$377,492 and assets held in foreign-currency-denominated investments are \$0, which is approximately 12.02% and 0% of Pinnacol's total admitted assets, respectively.

5. The following represents aggregate foreign investment exposure categorized by NAIC sovereign designation:

Foreign investment assets		Amount	Percentage of total admitted assets
NAIC Designation			
Countries designated NAIC-1		\$ 343,280	10.934%
Countries designated NAIC-2		27,788	0.885
Countries designated NAIC-3 or below		6,425	0.205
		<u>\$ 377,493</u>	

PINNACOL ASSURANCE
Supplemental Schedule of Investment Information
Investment Risks Interrogatories
Year ended December 31, 2021
(In thousands)

6. The following represents the largest foreign investment exposures by country, categorized by the country's NAIC sovereign designation:

Foreign investment assets			
NAIC Designation	Country	Amount	Percentage of total admitted assets
Countries designated NAIC-1:			
Country 1:	Cayman Islands	\$ 177,836	5,665%
Country 2:	United Kingdom	33,432	1,065
Countries designated NAIC-2:			
Country 1:	Mexico	16,394	0,522
Country 2:	Panama	6,031	0,192
Countries designated NAIC-3 or below:			
Country 1:	Virgin Islands, British	4,484	0,143
Country 2:	Aruba	1,800	0,057
		<u>\$ 239,977</u>	

7. Aggregate unhedged foreign currency exposure is \$0, which is approximately 0% of Pinnacol's total admitted assets.

8. The following represents aggregate unhedged foreign currency exposure categorized by NAIC sovereign designation:

Foreign-currency-denominated investment assets			Percentage of total admitted assets
NAIC Designation	Amount		
Countries designated NAIC-1	\$ 0	—%	
Countries designated NAIC-2	0	—	
Countries designated NAIC-3 or below	0	—	
	<u>\$ 0</u>		

9. The following represents the largest unhedged foreign currency exposures by country, categorized by the country's NAIC sovereign designation:

Foreign-currency-denominated investment assets			
NAIC Designation	Country	Amount	Percentage of total admitted assets
Countries designated NAIC-1:			
Country 1:		\$ 0	—%
Country 2:		0	—
Countries designated NAIC-2:			
Country 1:		0	—
Country 2:		0	—
Countries designated NAIC-3 or below:			
Country 1:		0	—
Country 2:		0	—
		<u>\$ 0</u>	

10. The following represents the ten largest nonsovereign (i.e., nongovernmental) foreign issues:

Issuer	NAIC Designation	Amount	Percentage of total admitted assets
10.01 Lending Ark Asia Secured Private Debt	1PL, Sch BA-Joint Venture	\$ 22,160	0,706%
10.02 Macquarie Group Limited	1FE	8,500	0,271
10.03 Credit Suisse Group AG	2FE	8,006	0,255
10.04 HSBC Holdings plc	1FE	7,008	0,223
10.05 Petronas Capital Limited	1FE	6,975	0,222
10.06 Fomento Económico Mexicano, S.A.B. de C.V.	1FE	5,148	0,164
10.07 Aptiv PLC	2FE	5,109	0,163
10.08 Shell International Finance B.V.	1FE	5,083	0,162
10.09 Arch Capital Group Ltd.	2FE	5,063	0,161
10.10 BP Capital Markets p.l.c.	1FE	5,031	0,160

PINNACOL ASSURANCE
Supplemental Schedule of Investment Information
Investment Risks Interrogatories
Year ended December 31, 2021
(In thousands)

11. Assets held in Canadian investments are less than 2.5% of Pinnacol's total admitted assets.
12. Amounts and percentages of the reporting entity's total admitted assets held in investments with contractual sales restrictions:
- 12.01 Are assets held in investments with contractual sales restrictions less than 2.5% of the reporting entity's total admitted assets? Yes [] No [X]
- 12.02 Aggregate statement value of investments held in investments with contractual sales restrictions \$ 203,212 6.473%
- Largest three investments held in investments with contractual sales restrictions:
- 12.03 NB Pinnacol Assurance Fund LP \$ 93,604 2.982%
- 12.04 Lending Ark Asia Secured Private Debt Fund I, LP 22,160 0.706
- 12.05 First Eagle DI V-A Funding LLC 16,903 0.538
13. The following are the ten largest equity interests (including investments in the shares of mutual funds, preferred stocks, publicly traded equity securities, and other equity securities and excluding money market and bond mutual funds listed in the *Purposes and Procedures Manual of the NAIC Investment Analysis Office* as exempt or NAIC Class 1):

Issuer	Amount	Percentage of total admitted assets	
13.02 Blackrock Equity Index Fund B	\$ 124,396	3.962%	
13.03 NB Pinnacol Assurance Fund LP	93,604	2.982	
13.04 T. Rowe Price U.S. Equity Research Fund	80,284	2,557	
13.05 GQG Partners International Equity Fund	50,031	1,594	
13.06 Vanguard Total International Stock ETF	44,013	1,402	
13.07 T. Rowe Price Institutional Small-Cap Stock	39,058	1,244	
13.08 First Eagle Overseas Fund	28,650	0,913	
13.09 Dodge & Cox International Stock Fund	24,645	0,785	
13.10 Franklin International Growth Fund	24,111	0,768	
13.11 GQG Partners Emerging Markets Equity Fund	22,891	0,729	
14. Amounts and percentages of the reporting entity's total admitted assets held in nonaffiliated, privately placed equities:			
14.01 Are assets held in nonaffiliated, privately placed equities less than 2.5% of the reporting entity's total admitted assets?	Yes []	No [X]	
14.02 Aggregate statement value of investments held in nonaffiliated, privately placed equities	197,318	6.285%	
Largest three investments held in nonaffiliated, privately placed equities:			
14.03 BLACKROCK EQUITY INDEX FUND B	124,396	3.962%	
14.04 GQG Partners International Equity Fund	50,031	1,594	
14.05 GQG Partners Emerging Markets Equity Fund	22,891	0,729	
<u>Ten Largest Fund Managers</u>			
14.06 BLACKROCK EQUITY INDEX FUND B	124,693	—	124,693
14.07 T. ROWE PRICE FUNDS	119,342	119,342	—
14.08 GQG PARTNERS FUNDS	72,922	—	72,922
14.09 VANGUARD FUNDS	49,824	49,824	—
14.10 WELLS FARGO FUNDS TRUST – TREASURY PLUS MONEY MARKET FUND	41,799	41,799	—
14.11 FIRST EAGLE OVERSEAS FUND	28,650	28,650	—
14.12 DODGE & COX INTERNATIONAL STOCK FUND	24,645	24,645	—
14.13 FRANKLIN INTERNATIONAL GROWTH FUND	24,111	24,111	—
14.14 STATE STREET INSTITUTIONAL INVESTMENT TRUST – INTERNATIONAL TREASURY PLUS MONEY MARKET FUND	19,464	19,464	—
14.15 MORGAN STANLEY INSTITUTIONAL FUND, INC.	11,121	11,121	—

Items 15 through 19 are not applicable.

See accompanying independent auditors' report.

PINNACOL ASSURANCE

Supplemental Schedule of Investment Information
Summary Investment Schedule

December 31, 2021

(In thousands)

Investment categories	Gross investment holdings*		Admitted assets as reported in the annual statement	
	Amount	Percentage of gross investment holdings	Amount	Percentage of total admitted assets
Long-term bonds:				
U.S. governments	\$ 169,695	5.4 %	\$ 169,695	5.4 %
All other governments	21,786	0.7	21,786	0.7
U.S. states, territories and possessions	1,001	—	1,001	—
U.S. political subdivisions of states, territories, and possessions	15,411	0.5	15,411	0.5
U.S. special revenue and special assessment obligations	429,392	13.8	429,392	14.0
Industrial and miscellaneous	1,679,568	53.9	1,679,568	54.7
Hybrid securities	5,989	0.2	5,989	0.2
Parent, subsidiaries, and affiliates	—	—	—	—
SVO identified funds	—	—	—	—
Unaffiliated bank loans	—	—	—	—
Preferred stocks:				
Industrial and miscellaneous (unaffiliated)	752	—	752	—
Parent, subsidiaries, and affiliates	—	—	—	—
Common stocks:				
Industrial and miscellaneous publicly traded (unaffiliated)	684	—	684	—
Industrial and miscellaneous other (unaffiliated)	573	—	573	—
Parent, subsidiaries, and affiliates publicly traded	—	—	—	—
Parent, subsidiaries, and affiliates other	—	—	—	—
Mutual funds	455,012	14.6	455,012	14.6
Unit investment trusts	—	—	—	—
Closed-end funds	40	—	40	—

PINNACOL ASSURANCE

Supplemental Schedule of Investment Information
Summary Investment Schedule

December 31, 2021

(In thousands)

Investment categories	Gross investment holdings*		Admitted assets as reported in the annual statement	
	Amount	Percentage of gross investment holdings	Amount	Percentage of total admitted assets
Mortgage loans:				
Farm mortgages	\$ —	— %	\$ —	— %
Residential mortgages	—	—	—	—
Commercial mortgages	68,554	2.2	68,554	2.2
Mezzanine real estate loans	—	—	—	—
Real estate:				
Property occupied by Company	12,847	0.4	12,847	0.4
Property held for production of income	—	—	—	—
Property held for sale	—	—	—	—
Cash, cash equivalents, and short-term investments:				
Cash	(7,992)	(0.3)	(7,992)	(0.3)
Cash equivalents	61,264	2.0	61,264	2.0
Short-term investments	—	—	—	—
Contract loans	—	—	—	—
Derivatives	—	—	—	—
Other invested assets (Schedule BA)	202,744	6.5	156,972	5.1
Receivables for securities	26	—	26	—
Securities lending	—	—	—	—
Other invested assets	—	—	—	—
Total invested assets	\$ 3,117,346	100 %	\$ 3,071,574	100 %

* Gross investment holdings as valued in compliance with NAIC *Accounting Practices and Procedures Manual*.

Note: Reinsurance Interrogatories are excluded as they are not applicable.

See accompanying independent auditors' report.

PINNACOL ASSURANCE

Reinsurance Interrogatories

December 31, 2021

1. Has the reporting entity ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates) for which during the period covered by the statement: (i) it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders; (ii) it accounted for that contract as reinsurance and not as deposit; and (iii) the contract(s) contain one or more of the following features or other features that would have similar results:
- (a) A contract term longer than two years and the contract is noncancelable by the reporting entity during the contract term;
- (b) A limited or conditional cancellation provision under which cancellation triggers an obligation by the reporting entity, or an affiliate of the reporting entity, to enter into a new reinsurance contract with the reinsurer, or an affiliate of the reinsurer;
- (c) Aggregate stoploss reinsurance coverage;
- (d) A unilateral right by either party (or both parties) to commute the reinsurance contract, whether conditional or not, except for such provisions, which are only triggered by a decline in the credit status of the other party;
- (e) A provision permitting reporting of losses, or payment of losses, less frequently than on a quarterly basis (unless there is no activity during the period); or
- (f) Payment schedule, accumulating retentions from multiple years, or any features inherently designed to delay timing of the reimbursement to the ceding entity?
2. Has the reporting entity during the period covered by the statement ceded any risk under any reinsurance contract (or under multiple contracts with the same reinsurer or its affiliates), for which it recorded a positive or negative underwriting result greater than 5% of prior year-end surplus as regards policyholders or it reported calendar year written premium ceded or year-end loss and loss expense reserves ceded greater than 5% of prior year-end surplus as regards policyholders. This disclosure is limited to reinsurance contracts with written premium cessions or loss and loss expense reserve cessions described in paragraph 116 of SSAP No. 62R, *Property and Casualty Reinsurance*. This disclosure excludes cessions to approved pooling arrangements or to captive insurance companies that are directly or indirectly controlling, controlled by, or under control with (i) one or more unaffiliated policyholders of the reporting entity, or (ii) an association of which one or more unaffiliated policyholders of the reporting entity is a member.
- (a) The written premium ceded to the reinsurer by the reporting entity or its affiliates represents fifty percent (50%) or more of the entire direct and assumed premium written by the reinsurer based on its most recently available financial statement; or
- (b) Twenty-five percent (25%) or more of the written premium ceded to the reinsurer has been retroceded back to the reporting entity or its affiliates in a separate reinsurance contract?
3. If yes to 1 or 2, please provide the following information in the Reinsurance Summary Supplemental Filing:
- (a) The aggregate financial statement impact gross of all such ceded reinsurance contracts on the balance sheet and statement of income;
- (b) A summary of the reinsurance contract terms and indicate whether it applies to the contracts meeting the criteria in 1 or 2; and
- (c) A brief discussion of management's principle objectives in entering into the reinsurance contract, including the economic purpose to be achieved.
4. Except for transactions meeting the requirements of paragraph 31 of SSAP No. 62R, *Property and Casualty Reinsurance*, has the reporting entity ceded any risk under any reinsurance contract (or multiple contracts with the same reinsurer or its affiliates) during the period covered by the financial statement, and either:
- (a) Accounted for that contract as reinsurance (either prospective or retroactive) under statutory accounting principles (SAP) and as a deposit under generally accepted accounting principles (GAAP); or
- (b) Accounted for that contract as reinsurance under GAAP and as a deposit under SAP?
5. If yes to 4, explain in the Reinsurance Summary Supplemental Filing why the contract(s) is treated differently for GAAP and SAP.
6. Does the reporting entity have any risks reinsured under a quota share reinsurance contract with any other entity that includes a provision that would limit the reinsurer's losses below the stated quota share percentage?

See accompanying independent auditors' report.



KPMG LLP
Suite 800
1225 17th Street
Denver, CO 80202-5598

Independent Auditors' Report on Internal Control Over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance With Government Auditing Standards

The Members of the Legislative Audit Committee and
Pinnacol Assurance Board of Directors:

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of Pinnacol Assurance, which comprise the statutory-basis statements of admitted assets, liabilities, and policyholders' surplus as of December 31, 2021, and the related statutory-basis statements of operations and changes in policyholders' surplus, and cash flow for the year then ended, and the related notes to the financial statements, and have issued our report thereon dated May 18, 2022. Our report on the financial statements includes an adverse opinion on U.S. generally accepted accounting principles because the financial statements are prepared using statutory accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado, which is a basis of accounting other than U.S. generally accepted accounting principles. Our report on the financial statements also includes an unmodified opinion on the financial statements in accordance with statutory accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado, which is a basis of accounting other than U.S. generally accepted accounting principles.

Report on Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered Pinnacol Assurance's internal control over financial reporting (internal control) as a basis for designing 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 Pinnacol Assurance's internal control. Accordingly, we do not express an opinion on the effectiveness of Pinnacol Assurance'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, or 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 the entity's financial statements will not be prevented, or 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 or significant deficiencies may exist that were not identified.

Report on Compliance and Other Matters

As part of obtaining reasonable assurance about whether Pinnacol Assurance's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the



financial statements. 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

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

KPMG LLP

Denver, Colorado
May 18, 2022



KPMG LLP
Suite 800
1225 17th Street
Denver, CO 80202-5598

May 18, 2022

The Members of the Legislative Audit Committee and
Pinnacol Assurance Board of Directors
Denver, Colorado

Ladies and Gentlemen:

We have audited the financial statements of Pinnacol Assurance (the Company), prepared in accordance with accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado, as of December 31, 2021 and 2020 and for each of the years then ended, and issued our report thereon under date of May 18, 2022. Under our professional standards, we are providing you with the accompanying information related to the conduct of our audits.

Our Responsibility Under Professional Standards

We are responsible for forming and expressing an opinion about whether the financial statements, that have been prepared by management with the oversight of the Pinnacol Assurance Risk and Audit Committee of the Board of Directors (Pinnacol Risk and Audit Committee), are presented fairly, in all material respects, in conformity with accounting practices prescribed or permitted by the Division of Insurance of the Department of Regulatory Agencies of the State of Colorado, which practices differ from the U.S. generally accepted accounting principles. We have a responsibility to perform our audit of the financial statements in accordance with auditing standards generally accepted in the United States of America (AICPA) and the standards applicable to financial statement audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. In carrying out this responsibility, we planned and performed the audit to obtain reasonable assurance about whether the financial statements as a whole are free of material misstatement, whether caused by error or fraud. Because of the nature of audit evidence and the characteristics of fraud, we are to obtain reasonable, not absolute, assurance that material misstatements are detected. We have no responsibility to plan and perform the audit to obtain reasonable assurance that misstatements, whether caused by error or fraud, that are not material to the financial statements are detected. Our audits do not relieve management or the Pinnacol Risk and Audit Committee of their responsibilities.

In addition, in planning and performing our audit of the financial statements, we considered internal control over financial reporting (internal control) as a basis for designing 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 the Company's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Company's internal control. We also have a responsibility to communicate significant matters related to the financial statement audit that are, in our professional judgment, relevant to the responsibilities of the Pinnacol Risk and Audit Committee in overseeing the financial reporting process. We are not required to design procedures for the purpose of identifying other matters to communicate to you.

Significant Unusual Transactions

In connection with our audit of the Company's financial statements, no significant unusual transactions were identified.



The Members of the Legislative Audit Committee and
Pinnacol Assurance Board of Directors
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Uncorrected and Corrected Misstatements

Uncorrected Misstatements and Financial Statement Presentation and Disclosure Omissions

In connection with our audit of the Company's financial statements, no uncorrected financial statement misstatements in the Company's books and records or significant financial statement presentation and disclosure omissions were identified as of and for the year ended December 31, 2021. We have communicated this to management.

Corrected Misstatements

In connection with our audit of the Company's financial statements, no corrected financial statement misstatements in the Company's books and records were identified as of and for the year ended December 31, 2021.

Significant Accounting Policies and Practices

In connection with our audit of the Company's financial statements, no new, or changes in, significant accounting policies and practices were identified.

Qualitative Aspects of Accounting Practices

We have discussed with the Pinnacol Assurance Risk and Audit Committee and management our judgments about the quality, not just the acceptability, of the Company's accounting policies as applied in its financial reporting. The discussions generally included such matters as the consistency of the Company's accounting policies and their application and the understandability and completeness of the Company's financial statements, which include related disclosures.

Significant Accounting Estimates and Significant Financial Statement Disclosures

The preparation of the financial statements requires management of the Company to make a number of estimates and assumptions relating to the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. Significant accounting estimates reflected in the Company's 2021 statutory-basis financial statements included the following:

Reserve for Unpaid Losses and Loss Adjustment Expenses is based on an analysis of historical paid and incurred claims. To assist management in estimating the liability for unpaid losses and loss adjustment expenses, the Company retains the assistance of an actuarial consulting firm. We evaluated the key factors and assumptions used to develop the reserve for unpaid losses and loss adjustment expenses, including possible management bias in developing the estimate, in determining that the reserve for unpaid losses and loss adjustment expenses is reasonable in relation to the financial statements as a whole.

Internal Structured Settlement Liability is based on mortality risk and discounted using a market rate. The Company discounts internal structured settlement liabilities on a tabular basis using a discount rate of 2.5% for 2021. The discount rate is based on an estimate of expected investment yield and considers the risk of adverse deviation in the future from such yield. To assist management in estimating the internal structured settlement liability, the Company retains the assistance of an actuarial consulting firm. We evaluated key factors and assumptions used to develop the structured settlement liability, including possible management bias in developing the estimate, in determining that the structured settlement liability is reasonable in relation to the financial statements as a whole.



Other Information in Documents Containing Audited Financial Statements

Our responsibility for other information in documents containing the Company's financial statements and our auditors' report thereon does not extend beyond the financial information identified in our auditors' report, and we have no obligation to perform any procedures to corroborate other information contained in these documents.

Significant Difficulties Encountered During the Audit

We encountered no significant difficulties in dealing with management in performing our audit.

Significant Issues Discussed, or Subject to Correspondence, with Management

We generally discuss a variety of matters, including the application of accounting principles and auditing standards with the Pinnacol Risk and Audit Committee and management each year prior to our retention by the Legislative Audit Committee as the Company's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Management's Consultation with Other Accountants

To the best of our knowledge, management has not consulted with other accountants during the year ended December 31, 2021.

Difficult or Contentious Matters for Which We Consulted

In connection with our audit of the Company's financial statements, we did not consult outside of the engagement team for any difficult or contentious matters.

Disagreements with Management

There were no disagreements with management on financial accounting and reporting matters that individually or in the aggregate could be significant to the Company's financial statements, or our report.

Written Communications

The following written communications between management and us have been provided:

1. Internal legal letter
2. Management representation letter

Independence

We are not aware of any additional circumstances or relationships between our firm and the Company and persons in a financial reporting oversight role at the Company that may reasonably be thought to bear on independence.

Affirmation of Independence

We hereby affirm that as of May 18, 2022, we are independent accountants with respect to the Company under all relevant professional and regulatory standards.

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The Members of the Legislative Audit Committee and
Pinnacol Assurance Board of Directors
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This letter to the Legislative Audit Committee and Pinnacol Risk and Audit Committee is intended solely for the information and use of Legislative Audit Committee and Pinnacol Risk and Audit Committee, management, and the Office of the State Auditor and is not intended to be and should not be used by anyone other than these specified parties. However, upon release by the Legislative Audit Committee, the report is a public document.

Very truly yours,

KPMG LLP