

**SOUTH CAROLINA SECOND INJURY FUND
COLUMBIA, SOUTH CAROLINA**

FINANCIAL STATEMENTS

June 30, 2008

State of South Carolina



Office of the State Auditor

1401 MAIN STREET, SUITE 1200
COLUMBIA, S.C. 29201

RICHARD H. GILBERT, JR., CPA
DEPUTY STATE AUDITOR

(803) 253-4160
FAX (803) 343-0723

October 16, 2008

The Honorable Mark Sanford, Governor
and
Mr. William E. Gunn, Director
South Carolina Second Injury Fund
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Second Injury Fund for the fiscal year ended June 30, 2008, was issued by McDowell-Pearman, LLC, Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

If you have any questions regarding this report, please let us know.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Richard H. Gilbert Jr.", written in a cursive style.

Richard H. Gilbert, Jr., CPA
Deputy State Auditor

RHGjr/trb

SOUTH CAROLINA SECOND INJURY FUND
COLUMBIA, SOUTH CAROLINA

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McDOWELL ♦ PEARMAN, LLC
CERTIFIED PUBLIC ACCOUNTANTS

W. M. McDowell, Jr. CPA
Ben J. Pearman, CPA
Cheryl H. Thigpen, CPA
• • • •

Charles M. Ayers, CPA
Lisa N. Smith, CPA

INDEPENDENT AUDITORS' REPORT

Mr. Richard H. Gilbert, Jr.
Interim State Auditor
South Carolina Office of the State Auditor
Columbia, South Carolina

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the South Carolina Second Injury Fund as of and for the year ended June 30, 2008, which collectively comprise the Fund's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

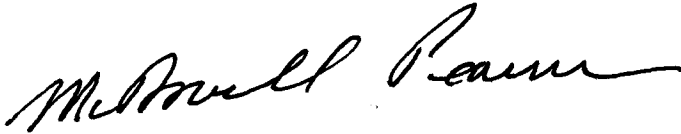
As described in Note 1, the financial statements of the South Carolina Second Injury Fund are intended to present the financial position, result of operations, and the cash flows of only that portion of the Funds of the State of South Carolina that is attributable to the transactions of the South Carolina Second Injury Fund. These financial statements do not purport to, and do not, present fairly the financial position of the State of South Carolina primary government or financial reporting entity as of June 30, 2008, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, and each major fund of the South Carolina Second Injury Fund as of June 30, 2008, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Mr. Richard H. Gilbert, Jr.
Interim State Auditor
South Carolina Office of the State Auditor
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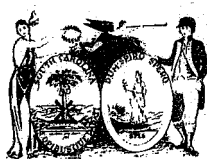
In accordance with *Government Auditing Standards*, we have also issued our report dated September 23, 2008, on our consideration of the South Carolina Second Injury Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, and other matters. The purpose of that report is 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 internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The Management's Discussion and Analysis is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

A handwritten signature in black ink, appearing to read "McDowell Baum". The signature is fluid and cursive, with a long horizontal stroke at the end.

September 23, 2008

The South Carolina Second Injury Fund



WILLIAM E. GUNN
INTERIM DIRECTOR

WINTHROP BUILDING, SUITE 119
220 EXECUTIVE CENTER DRIVE
COLUMBIA, S.C. 29210
www.scsif.sc.gov

(803) 798-2722
FAX: (803)798-5290

Management's Discussion and Analysis

Overview of the Financial Statements and Financial Analysis

This report is prepared in accordance with Governmental Accounting Standards Board Statement 34, *Basic Financial Statements-and Management's Discussion and Analysis for State and Local Governments*. There are five financial statements presented: Statement of Net Assets; Statement of Activities; Statement of Revenues and Changes in Fund Balance – Governmental Fund Type; Statement of Revenues, Expenses, and Changes in Net Assets – Proprietary Fund Type; and Statement of Cash Flows. This discussion and analysis of the Second Injury Fund's (the Fund) financial statements provides an overview of its financial activities for the year.

Statement of Net Assets

The Statement of Net Assets presents the assets, liabilities, and net assets of the Fund as of the end of the fiscal year. The Statement of Net Assets presents end-of-year data concerning assets (current and noncurrent), liabilities (current and noncurrent), and net assets (assets minus liabilities). Current assets are those which are reasonably expected to be realized in cash or sold or consumed within one year. Current liabilities are obligations whose liquidation is expected to require the use of current assets.

Condensed Statement of Net Assets:

	FY 2008	FY 2007	VARIANCE
Assets:			
Current assets	\$ 51,383,820	\$ 53,445,581	\$ (2,061,761)
Capital assets, net of depreciation	6,823	11,492	(4,669)
Total Assets	\$ 51,390,643	53,457,073	(2,066,430)

	FY 2008	FY 2007	VARIANCE
Liabilities:			
Current liabilities	\$ 61,245,752	\$ 61,674,818	\$ 429,066
Non-current liabilities	18,161,459	11,481,196	(6,680,263)
Total Liabilities	<u>\$ 79,407,211</u>	<u>\$ 73,156,014</u>	<u>\$ (6,251,197)</u>
Net Assets (Deficit):			
Invested in capital assets	\$ 6,823	\$ 11,492	\$ (4,669)
Deficit	(28,023,391)	(19,710,433)	(8,312,958)
Total Net Assets (Deficit)	<u>\$ (28,016,568)</u>	<u>\$ (19,698,941)</u>	<u>\$ (8,317,627)</u>

Statement of Activities

Changes in total net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Activities. The purpose of the statement is to present the revenues received by the Fund, both operating and nonoperating, and the expenses paid by the Fund, operating and nonoperating, and any other revenue, expenses, gains, and losses received or spent by the Fund. Nonoperating revenues, are revenues received for which goods and services are not provided.

The Statement of Activities is prepared on the accrual basis of accounting. Accrual accounting attempts to record the financial effects of transactions on an entity in the period in which those transactions occur rather than in the period in which cash is received or paid. Revenues are recognized when services or goods are provided. Expenses are recognized when resources are utilized in order to produce goods or services.

Condensed Statement of Activities:

	FY 2008	FY 2007	VARIANCE
Operating Revenues	\$ 1,671,725	\$ 1,548,314	\$ 123,411
Operating Expenses	(18,989,352)	(15,377,836)	(3,611,516)
Operating Loss	(17,317,627)	(13,829,522)	(3,488,105)
Transfers	9,000,000	7,400,000	1,600,000
Decrease in net Assets	(8,317,627)	(6,429,522)	(1,888,105)
Net Assets - (Deficit) - Beginning of Year	<u>(19,698,941)</u>	<u>(13,269,419)</u>	<u>(6,429,522)</u>
Net Assets - (Deficit) - End of Year	<u>\$ (28,016,568)</u>	<u>\$ (19,698,941)</u>	<u>\$ (8,317,627)</u>

Individual Fund Statements

The Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Fund Type is presented on the modified accrual basis of accounting with reconciliation to the Statement of Activities. The Statement of Revenues Expenditures, Expenses and Changes in Net Assets – Proprietary Fund Type is a more detailed statement than presented on the Statement of Activities, and is presented on the accrual basis of accounting.

The final statement presented by Second Injury Fund is the Statement of Cash Flows. The Statement of Cash Flows presents detailed information about the cash activity of the Proprietary Fund Type during the year. The statement is divided into three parts. The first part deals with operating cash flows and shows the net cash used by the operating activities of the Fund. The second section reflects cash flows from investing activities and shows the interest received from investing activities. The third section reconciles the net cash used to the operating income or loss displayed on the Statement of Revenues, Expenses, and Changes in Net Assets for the Second Injury Fund.

Condensed Statement of Cash Flows:

	<u>FY 2008</u>	<u>FY 2007</u>	<u>VARIANCE</u>
Cash Provided (used) by:			
Operating activities	\$ (5,310,967)	\$ (25,822,218)	\$ 20,511,251
Investing activities	<u>3,316,182</u>	<u>3,985,304</u>	<u>(669,122)</u>
Net Change in Cash	(1,994,785)	(21,836,914)	19,842,129
Cash and Cash Equivalents –			
Beginning of Year	<u>51,993,789</u>	<u>73,830,703</u>	<u>(21,836,914)</u>
Cash and Cash Equivalents –			
End of Year	<u>\$ 49,999,004</u>	<u>\$ 51,993,789</u>	<u>\$ (1,994,785)</u>

Economic Outlook

The Workers' Compensation Uninsured Employers' Fund shows an overall deficit due to the fact that it records the actuarial liability for unpaid claims. The fund is basically on a pay as you go basis and receives transfers from two other state entities when monies are needed to pay claims.

We feel both the Second Injury Fund's and Workers' Compensation Uninsured Employers' Fund's overall financial positions are sound. Amendments, effective June 25, 2003, to Sections 42-7-310 and 42-9-400 of the South Carolina Code of Laws have reduced the number of Second Injury Fund claims accepted for reimbursement by 61% from FY 2004 to FY 2008. There has been a 32%

reduction in dollars reimbursed from a high of \$166.9 million in FY2005 to \$113.2 million in FY2008. We should see continuations of this downward trend as the full effect of the changes to the amendments are realized. This will cause the continued reduction of reimbursements and the lowering of the annual assessment. Legislation was enacted in FY2007 that put the Fund in runoff and ultimately terminates the Fund on July 1, 2013 with any remaining liabilities and residual activity being transferred to the South Carolina Budget and Control Board.

FINANCIAL STATEMENTS

SOUTH CAROLINA SECOND INJURY FUND

STATEMENT OF NET ASSETS

JUNE 30, 2008

	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
<u>ASSETS</u>			
Current Assets:			
Cash and Cash Equivalents	\$ 813,230	\$ 198,466	\$ 1,011,696
Cash and Cash Equivalents - Restricted	-	49,800,538	49,800,538
Receivable - Restricted	-	71,250	71,250
Interest Receivable	4,885	-	4,885
Interest Receivable - Restricted	-	495,451	495,451
Total Current Assets	818,115	50,565,705	51,383,820
Equipment, Net of Accumulated Depreciation of \$43,621	-	6,823	6,823
Total Assets	818,115	50,572,528	51,390,643
<u>LIABILITIES</u>			
Current Liabilities:			
Accounts Payable	-	1,563	1,563
Claims Payable From Restricted Assets	-	50,367,239	50,367,239
Accrued Payroll	-	96,444	96,444
Accrued Compensated Absences	-	87,000	87,000
Claims and Awards	10,000,000	-	10,000,000
Funds held for others	693,506	-	693,506
Total Current Liabilities	10,693,506	50,552,246	61,245,752
Noncurrent Liabilities:			
Claims and Awards	18,148,000	-	18,148,000
Accrued Compensated Absences	-	13,459	13,459
Total Noncurrent Liabilities	18,148,000	13,459	18,161,459
Total Liabilities	28,841,506	50,565,705	79,407,211
<u>NET ASSETS</u>			
Net Assets (Deficit):			
Invested in capital assets	-	6,823	6,823
Deficit	(28,023,391)	-	(28,023,391)
Total Net Assets (Deficit)	\$ (28,023,391)	\$ 6,823	\$ (28,016,568)

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2008

	Expenses	Charges for Services	Total Governmental Activity	Total Business-Type Activity	Total
Governmental Activity:					
Workers compensation claims, net \$	17,312,958	\$ -	\$ (17,312,958)	\$ -	(17,312,958)
Business Type Activity:					
Workers compensation claims	1,676,394	1,671,725	-	(4,669)	(4,669)
Total	<u>\$ 18,989,352</u>	<u>\$ 1,671,725</u>	<u>(17,312,958)</u>	<u>(4,669)</u>	<u>(17,317,627)</u>
Transfers			9,000,000		9,000,000
Change in Net Assets			(8,312,958)	(4,669)	(8,317,627)
Net Assets (Deficit) - July 1			<u>(19,710,433)</u>	11,492	<u>(19,698,941)</u>
Net Assets (Deficit) - June 30			<u>\$ (28,023,391)</u>	<u>\$ 6,823</u>	<u>\$ (28,016,568)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND
WORKERS' COMPENSATION UNINSURED EMPLOYERS' FUND
GOVERNMENTAL FUND
BALANCE SHEET
FOR THE YEAR ENDED JUNE 30, 2008

ASSETS

Cash	\$ 813,230
Interest Receivable	<u>4,885</u>
Total Assets	<u>\$ 818,115</u>

LIABILITIES AND FUND EQUITY

Funds Held for Others	<u>\$ 693,506</u>
Total Liabilities	<u>693,506</u>
Fund Balance – Reserved for workers' compensation claims	<u>124,609</u>
Total Liabilities and Fund Balance	<u>\$ 818,115</u>

RECONCILIATION TO STATEMENT OF NET ASSETS

Fund Balance Above	\$ 124,609
Recognition of liability for claims and awards on statement of net assets	<u>(28,148,000)</u>
Deficit on Statement of Net Assets	<u>\$ (28,023,391)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**WORKERS' COMPENSATION UNINSURED EMPLOYERS' FUND
GOVERNMENTAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE
FOR THE YEAR ENDED JUNE 30, 2008**

Expenditures:

Workers' Compensation Uninsured	
Employers' Fund claims and awards, net of recoupments of \$684,304	\$ 8,206,376
Claims adjustment expenditures	<u>925,582</u>
Total Expenditures	<u>9,131,958</u>

Transfer from Workers' Compensation Commission	1,017,900
Transfer from South Carolina Department of Insurance	<u>7,982,100</u>
Total Transfers	<u>9,000,000</u>

Net Change in Fund Balance	(131,958)
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Fund Balance - July 1	<u>256,567</u>
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Fund Balance - June 30	<u>\$ 124,609</u>
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RECONCILIATION TO STATEMENT OF ACTIVITIES

Net Change in Fund Balance above	\$ (131,958)
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Recognition of change in claims liability	<u>(8,181,000)</u>
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Change in net assets on statement of activities	<u>\$ (8,312,958)</u>
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THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**SECOND INJURY FUND
ENTERPRISE FUND
STATEMENT OF NET ASSETS**
JUNE 30, 2008

ASSETS

Current Assets:

Cash and Cash Equivalents	\$ 198,466
Cash and Cash Equivalents - Restricted	49,800,538
Receivable – Restricted	71,250
Interest Receivable - Restricted	<u>495,451</u>
Total Current Assets	<u>50,565,705</u>

Equipment, Net of Accumulated

Depreciation of \$43,621	<u>6,823</u>
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Total Assets	<u>50,572,528</u>
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LIABILITIES

Current Liabilities:

Accounts Payable	1,563
Claims Payable From Restricted Assets	50,367,239
Accrued Payroll	96,444
Accrued Compensated Absences	<u>87,000</u>
Total Current Liabilities	<u>50,552,246</u>

Noncurrent Liabilities:

Accrued Compensated Absences - Noncurrent	<u>13,459</u>
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Total Noncurrent Liabilities	<u>13,459</u>
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Total Liabilities	<u>50,565,705</u>
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NET ASSETS

Invested in capital assets	<u>6,823</u>
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Total Net Assets	<u>\$ 6,823</u>
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THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

SECOND INJURY FUND

ENTERPRISE FUND

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS

FOR THE YEAR ENDED JUNE 30, 2008

Operating Revenue:

Assessments	\$ 1,671,725
Total Revenue	<u>1,671,725</u>

Operating Expenses:

Administration:

Personal services	1,041,521
Employer contributions	298,624
Contractual services	164,905
Fixed charges and contributions	105,492
Supplies	35,666
Travel	21,808
Minor uncapitalized equipment	3,709
Depreciation	<u>4,669</u>

Total Operating Expenses	<u>1,676,394</u>
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Net Income (Loss)	(4,669)
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Net Assets - July 1	<u>11,492</u>
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Net Assets - June 30	<u>\$ 6,823</u>
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THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**SECOND INJURY FUND
ENTERPRISE FUND
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2008**

Cash Flows From Operating Activities:	
Assessments and other income received	\$ 111,090,057
Claims paid	(114,719,108)
Administrative expenses paid	<u>(1,681,916)</u>
Net Cash Provided (Used) by Operating Activities	<u>(5,310,967)</u>
Cash Flows From Investing Activities:	
Interest income received restricted for payment of claims	<u>3,316,182</u>
Net Cash Provided by Investing Activities	<u>3,316,182</u>
Net Increase (Decrease) in Cash and Cash Equivalents	(1,994,785)
Cash and Cash Equivalents, Beginning of Year	<u>51,993,789</u>
Cash and Cash Equivalents, End of Year	<u>\$ 49,999,004</u>
Reconciliation of Operating Income (Loss) to Net Cash Provided (Used) by Operating Activities:	
Operating income (loss)	\$ (4,669)
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	4,669
Assessments and other income received:	
Restricted for payment of claims	109,418,332
Claims paid	(114,719,108)
Increase (Decrease) in Liabilities:	
Accounts payable	(205)
Accrued payroll	(10,250)
Accrued compensated absences	<u>264</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ (5,310,967)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008**

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The core of the financial reporting entity is the primary government which has a separately elected governing body. As required by generally accepted accounting principles, the financial reporting entity includes both the primary government and all its component units. Component units are legally separate organizations for which the elected officials or the primary government are financially accountable. In turn, component units may have component units.

An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. That organization is identified herein as a primary entity.

The primary entity is financially accountable if it appoints a voting majority of the organization's governing body including situations in which the voting majority consists of the primary entity's officials serving as required by law (e.g., employees who serve in an ex officio capacity on the component unit's board are considered appointments by the primary entity) and (1) it is able to impose its will on that organization or (2) there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary entity. The primary entity also may be financially accountable if an organization is fiscally dependent on it even if it does not appoint a voting majority of the board. An organization is fiscally dependent on the primary entity that holds one or more of the following powers:

- (1) Determine its budget without another government's having the authority to approve and modify that budget.
- (2) Levy taxes or set rates or charges without approval by another government.
- (3) Issue bonded debt without approval by another government.

Based on the application of the above criteria, no component units are included in the reporting entity.

Prior to July 1, 1993, the Second Injury Fund ("the Fund") was considered to be a component unit of the State of South Carolina. Effective July 1, 1993, the Fund was considered part of the State of South Carolina's primary government and is included in the State of South Carolina's Comprehensive Annual Financial Report as such. This is based on guidance provided by GASB Statement 14 *The Financial Reporting Entity*. The South Carolina Second Injury Fund was established by Section 42-7-310 of the Code of Laws of South Carolina. The funds of the Fund are included in the Comprehensive Annual Financial Report of the State of South Carolina.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

The Fund is administered by a Director appointed by the State Budget and Control Board. The reporting entity is part of the State primary government unit. The accompanying financial statements present the financial position, results of operations and cash flows solely of the South Carolina Second Injury Fund and do not include any other funds of the State of South Carolina. The Second Injury Fund does not have any component units.

The Second Injury Fund, per Code of Laws Section 42-7-310, established the guidelines by which to pay compensation claims in those cases where an individual having an existing permanent physical impairment incurs a subsequent disability from injury by accident arising out of and in the course of employment. Funding for payment of compensation awards and for Fund operating costs is provided by equitable assessments upon all workman's compensation insurance carriers, self-insurers, and the South Carolina State Accident Fund (approximately 360 entities). Participation is mandatory as required by State law. Participants of the fund are responsible for the fund's liabilities. Payments of claims and awards are made directly to the carriers and self-insurers. The State of South Carolina will not be responsible for any expense or liabilities of the fund, except the State Accident Fund, who is a participant in the fund.

Per Code of Laws Section 42-7-200(a), as amended, the Second Injury Fund is responsible for administering the Workers' Compensation Uninsured Employers' Fund. The Fund issues payment of awards of workers' compensation benefits, which are unpaid because of employers' who fail to acquire necessary coverage for employees. Funding for payment of awards is provided from collections of the tax on insurance carriers and self-insured persons in an amount sufficient to maintain the fund. The monies are transferred from the South Carolina Department of Insurance and the South Carolina Workers' Compensation Commission.

Basis of Presentation - Fund Accounting

The government uses funds to report its financial position, results of operations and cash flows. Fund accounting is designed to demonstrate legal compliance and to aid financial management by segregating transactions related to certain government functions or activities.

A fund is a separate fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with related liabilities and residual equities or balances and changes therein which are segregated to carry on specific activities or attain certain objectives in accordance with applicable regulations, restrictions, or limitations. Separate accounts are maintained for each fund. Funds are classified into three categories: governmental, proprietary, and fiduciary. Each category, in turn, is divided into separate "fund types."

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

Governmental funds include the Workers' Compensation Uninsured Employers' Fund, a special revenue fund. Proprietary funds include the Second Injury Fund, an enterprise fund.

Since June 30, 1999, the Fund agreed to disburse the remaining funds of several self-insured workers compensation funds of a bankrupt companys. The Fund handles those funds in a fiduciary/agency capacity and the activities are reported in Note 11.

Basis of Accounting

Government-wide Financial Statements

In the government-wide Statement of Net Assets and Statements of Activities, both governmental and business-like activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used.

Fund Financial Statements

The Workers' Compensation Uninsured Employers' Fund a special revenue fund uses the modified accrual basis of accounting. The revenues are recognized when they become available and measurable. Available means those amounts that will be received within one year of the date of the financial statements. The transfers from the South Carolina Insurance Commission and the South Carolina Workers' Compensation Commission are recorded when received in cash because they are not considered available until the Fund requests the transfer of funds. The request from the Fund is the event that is considered necessary to trigger the recognition of transfer.

Expenditures of this fund are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred. Expenditure recognition is limited to exclude amounts represented by noncurrent liabilities since they do not affect net current assets. Because this basis of accounting differs from the manner in which the government-wide financial statements are prepared the fund financial statements include a reconciliation with brief explanations to better identify the relationship between the government-wide financial statements and the individual fund financial statements.

The Second Injury Fund an enterprise fund is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. These operating statements present increases and decreases in total assets.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

The revenues and expenses are recognized on the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

The Second Injury Fund individual financial statements are prepared on the same basis of accounting as the government-wide financial statements; therefore there is no reconciliation between the fund and government-wide statements.

The Government Accounting Standards Board (GASB) is the recognized standard setting body for generally accepted accounting principles applicable to governmental proprietary activities in the United States of America. The Fund applies all applicable Government Accounting Standards Board (GASB) pronouncements and all applicable Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989 when not in conflict with (GASB) pronouncements. In accordance with GASB Statement 20, the Fund has elected not to implement FASB Statements 103 and after.

Budget Policy

The South Carolina Second Injury Fund is granted an annual appropriation for administrative operating purposes by the General Assembly to be funded from the Second Injury Fund's participant's assessments. The appropriation as enacted becomes the legal operating budget for the Fund for its budgeted activities. The Appropriation Act authorizes expenditures from funds appropriated from the General Fund of the State and authorizes expenditures of total funds. The Total Funds column in the Appropriations Act for each individual budgetary unit authorizes expenditures from all budgeted resources. A revenue budget is not adopted for individual budgetary units. The agency receives no State General Funds Appropriations. The General Assembly enacts the budget through passage of line-item appropriations by program within budgetary unit within budgetary fund category, State General Fund or other budgeted funds. Budgetary control is maintained at the line item level of the budgetary entity. Agencies may process disbursement vouchers in the State's budgetary accounting system only if enough cash and appropriation authorization exist.

Transfers of funds may be approved by the State Budget and Control Board under its authority or by the agency as set forth in the 2008 Appropriation Act Proviso 72.10 as follows: Agencies are authorized to transfer appropriations within programs and within the agency with notification to the Division of Budget and Analyses and the State Comptroller General. No such transfer may exceed twenty percent of the program budget. Transfers from personal services accounts or from other operating accounts may be restricted to any level set by the Board.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

During the fiscal year-end closeout period in July, agencies may continue to charge vendor, interagency, and interfund payments for the fiscal year to that fiscal year's appropriation. For the Fund, any unexpended funds as of June 30, automatically carry over to the ensuing fiscal year. State law does not require the use of encumbrance accounting.

State law does not precisely define the budgetary basis of accounting. The current Appropriation Act states that the General Assembly intends to appropriate all State funds and to authorize and/or appropriate the use of all other monies to operate State government for the current fiscal year. The State's annual budget is prepared primarily on the modified accrual basis of accounting with several exceptions, principally the cash disbursements basis for payroll expenditures.

The budget and actual comparison in Note 2 presents actual expenditures on the budgetary basis of accounting compared to the legally adopted and modified budget on a line-item expenditure basis for the Fund's administrative costs. The level of legal control for each agency is reported in a publication of the State Comptroller General's Office titled *A Detailed Report of Appropriations and Expenditures* for each fiscal year.

Capital Assets

Equipment acquisitions require the use of enterprise fund financial resources and are capitalized at cost in the fund upon acquisition. Purchases of equipment in excess of \$5,000 are capitalized. Depreciation of equipment is charged as an expense against operations, and accumulated depreciation is reported on the Funds' balance sheet. Depreciation has been provided over the estimated useful lives of five to ten years using the straight-line method of depreciation.

Compensated Absences

Generally all permanent full-time State employees and certain part-time employees scheduled to work at least one-half of the agency's workweek are entitled to accrue and carry forward at calendar year-end a maximum of 180 days sick leave and 45 days annual vacation leave. Upon termination of State employment, employees are entitled to be paid for accumulated unused annual vacation leave up to the maximum of 45 days, but are not entitled to any payment for unused sick leave. The South Carolina Second Injury Fund calculates the gross compensated absences liability based on recorded balances of unused leave. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary-related benefit payments is recorded as a current liability. The net change in the liability is recorded in the current year in the applicable administrative expense categories.

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008(Continued)

Cash and Cash Equivalents

The amounts shown in the financial statements as "*cash and cash equivalents*" represent cash on deposit with the State Treasurer and cash invested in various investments by the State Treasurer as part of the State's internal cash management pool.

Because the State's internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The pool includes some long-term investments such as obligations of the United States and certain agencies of the of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. Most State agencies participate in the State's internal cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of funds. For those accounts, cash equivalents included investments in short-term, highly liquid securities having an original maturity of three months or less.

The State's internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each agency's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. Agencies record and report their deposits in the general deposit account at cost. However, agencies report their deposits in the special deposit accounts at fair value. Investments in the pool are recorded at fair value. Interest earned by the agency's special deposit accounts is posted to the agency's account at the end of each month and is retained by the agency. Interest earnings are allocated based on the percentage of an agency's accumulated daily interest receivable to the total undistributed interest received by the pool. Reported interest income includes interest earnings, realized gains/losses and unrealized gains/losses on investments in the pool arising from changes in fair value. The South Carolina Second Injury Fund only has special deposit accounts. Realized gains and losses are allocated daily and are included in the accumulated income receivable. Unrealized gains and losses are allocated at year-end based on the agency's percentage of ownership in the pool.

Although the State's internal cash management pool includes some long-term investments, it operates as a demand deposit account; therefore, for credit risk information pertaining to the internal cash management pool, see the deposits disclosures in Note 3.

Statement of Cash Flows

For purposes of this statement the South Carolina Second Injury Fund considers investments with the State of South Carolina's internal cash management pool to be cash equivalents because they are readily convertible to cash with an insignificant risk of loss in value.

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

Unpaid Claims Liabilities

It has been determined that the Second Injury Fund did not fall within GASB 10's definition of a public entity risk pool (PERP), because there is no actual transfer of risk to the Fund, and also the majority of the entities serviced by the fund are not governmental entities. Assessments for the current year are recognized only to the extent actually assessed to the participants. The assessments are recognized as revenues only to the extent they are used to cover the funds administrative expenses and capital outlay. Claims are recognized as a liability only to the extent that assets are available to liquidate these liabilities. Based on the fund operations and prior actuarial studies, it was determined that the liabilities far exceed the available assets, however since the participants are ultimately responsible for paying these liabilities and there is no transfer of risk, a liability is recognized only to the availability of assets to pay claims. Therefore the balance sheet does not include any additional claims reported to the Second Injury Fund as a claims service or an estimate of IBNR claims which are the responsibility of the participants. The payments of claims are not considered an operating expense of the fund. These are only shown on the statement of cash flows.

Prior to July 1, 1995, the Workers' Compensation Uninsured Employers' Fund was determined to be covered by GASB Statement 10 as an activity other than a public entity risk pool (PERP) which, however, does involve risk financing activities. The primary difference between a PERP and a non-PERP entity is that in a non-PERP entity the government does not transfer or pool its risks. Effective July 1, 1995, it has been determined that the Fund is a state benefit program that should follow GASB 10's guidance for measurement and recognition of claims liabilities. However, the Fund is not required to present additional disclosures, such as the claims reconciliation table required by GASB 10. GASB 10 allows the selection of fund type based upon characteristics of the fund. This activity is classified as a special revenue fund. The Fund actuarially establishes claims liabilities based on estimates of the ultimate cost of claims (including future claim adjustment expenses) that have been reported but not settled, and of claims that have been incurred but not reported. The length of time for which such costs must be estimated varies depending on the coverage involved. Because actual claims costs depend on such complex factors as medical technology, changes in doctrines of legal liability, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed annually using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflects past inflation and on other factors that are considered to be appropriate modifiers of past experience. Also included in the calculation is an estimate of future recoupments by the fund from the uninsured employers. In August 2008, an actuarial study was done for the year ended June 30, 2008.

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

Assessment Revenues

Second Injury Fund assessments are recognized as enterprise fund revenues only to the extent which they are needed for administrative expenses and capital outlay of the fund, less depreciation and gain on disposal of assets recorded by the Fund.

Restricted Assets and Claims Payable from Restricted Assets

Cash which is not required to pay administrative liabilities is restricted for payment of claims. The sources of funds to pay restricted claims are assessments, interest earned on deposits and other income. Also interest receivable is restricted for payment of claims. As explained in Note 1 under Unpaid Claims Liabilities, a payable of claims is recorded only to the extent of the assets available to pay claims.

Administration Expenses

The Second Injury Fund does not allocate any administrative expenses to the Uninsured Employers Fund because by State law the Uninsured Employers' Fund cannot pay administrative expenses. The fund only pays claims and those direct costs associated with payment of the claims. See Note 11 regarding administrative expenses and the Bankruptcy Claim Fund special revenue fund. All administration expenses are reported in the enterprise fund.

Estimates

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

NOTE 2 - BUDGET COMPARISON TO ACTUAL

The Administration expenses of the enterprise fund shown in the statement of revenue, expenses, and changes in retained earnings are reported on the accrual basis of accounting, which differs from the legally enacted budgetary basis for the year ended June 30, 2008. Adjustments of the GAAP basis of accounting to the budgetary basis consist of reversals of payroll and compensated absences accruals and the related fringe benefits, and of reflecting equipment acquisitions as expenses.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

Administration expenses per statement	\$ 1,676,394
Adjustments to Budgetary Basis:	
Depreciation	(4,669)
Net Accruals:	
Personal services	8,259
Employer contributions	<u>1,727</u>
Total Actual on Budgetary Basis	<u>\$ 1,681,711</u>

The Administration expenditures shown below are presented on the budgetary basis compared to the legally adopted and modified budget by object code category.

<u>Fiscal Year 2008</u>	<u>Legal Basis Budget</u>	<u>Actual on Budgetary Basis</u>	<u>Variance Favorable (Unfavorable)</u>
Personal Services	\$ 1,051,776	\$ 1,049,779	\$ 1,997
Employer Contributions	300,377	300,352	25
Other Operating Expenses	<u>378,249</u>	<u>331,580</u>	<u>46,669</u>
Total	<u>\$ 1,730,402</u>	<u>\$ 1,681,711</u>	<u>\$ 48,691</u>

The special revenue fund does not budget and is not allocated any administrative costs. Claims and claims adjustment expenses of neither fund are a budgeted expenditure.

NOTE 3 - DEPOSITS AND INVESTMENTS

All deposits of South Carolina Second Injury Fund are under the control of the State Treasurer who, by law, has sole authority for investing State Funds.

State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days. At June 30, 2008, all State Treasurer bank balances were fully insured or collateralized with securities held by the State or by its agents in the State's name.

With respect to investments in the State's internal cash management pool, all of the State Treasurer's investments are insured or registered or are investments for which the securities are held by the State or its agent in the State's name. Information pertaining to the reported amounts, fair values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

NOTE 4 - EQUIPMENT

Equipment is stated at original cost. A summary of the changes in equipment and accumulated depreciation is as follows:

<u>Equipment</u>			
<u>Balance</u> <u>7/01/07</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>6/30/08</u>
\$ 50,443	\$ -	\$ -	\$ 50,443

<u>Accumulated Depreciation</u>			
<u>Balance</u> <u>7/1/07</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>6/30/08</u>
\$ 38,951	\$ 4,669	\$ -	\$ 43,620

NOTE 5 - LONG-TERM LIABILITIES

The following is a summary of changes in long-term liabilities of the Fund:

	<u>July 1, 2007</u>	<u>Increase</u>	<u>Decrease</u>	<u>June 30, 2008</u>	<u>Due Within</u> <u>One Year</u>
Governmental Activity:					
Claims and Awards	\$ 19,967,000	\$ 17,324,855	\$ 9,143,855	\$ 28,148,000	\$ 10,000,000
Business-Type Activity:					
Compensated Absences	100,196	86,636	86,373	100,459	87,000
Total	<u>\$ 20,067,196</u>	<u>\$ 17,411,491</u>	<u>\$ 9,230,228</u>	<u>\$ 28,248,459</u>	<u>\$ 10,087,000</u>

NOTE 6 - PENSION PLAN AND OTHER EMPLOYEE BENEFITS

The Retirement Division of the State Budget and Control Board maintains four independent defined benefit plans and issues its own publicly available Comprehensive Annual Financial Report (CAFR), which includes financial statements and required supplementary information. A copy of the separately issued CAFR may be obtained by writing to the Retirement Division, 202 Arbor Lake Drive, Columbia, South Carolina, 29223. Furthermore, the Division and the four pension plans are included in the CAFR of the State of South Carolina.

Substantially all employees of the South Carolina Second Injury Fund are covered by a pension plan through the South Carolina Retirement System (SCRS), a

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

cost-sharing multiple-employer defined benefit pension plan administered by the Retirement Division, a public employee retirement system. Generally all State employees are required to participate in and contribute to the SCRS as a condition of employment unless exempted by law as provided in Section 9-1-480 of the South Carolina Code of Laws. This plan provides retirement annuity benefits as well as disability, cost of living adjustment, death, and group-life insurance benefits to eligible employees and retirees.

Under SCRS, employees are eligible for a full service retirement annuity upon reaching age 65 or completion of 28 years credited service regardless of age. The benefit formula for full benefits effective since July 1, 1989, for the SCRS is 1.82 percent of an employee's average final compensation multiplied by the number of years of credited service. Early retirement options with reduced benefits are available as early as age 55. Employees are vested for a deferred annuity after five years service and qualify for a survivor's benefit upon completion of 15 years credited service. Disability annuity benefits are payable to employees totally and permanently disabled provided they have a minimum of five years credited service (this requirement does not apply if the disability is the result of a job related injury). A group-life insurance benefit equal to an employee's annual rate of compensation is payable upon the death of an active employee with a minimum of one year of credited service.

Effective January 1, 2001, Section 9-1-2210 of the South Carolina Code of Laws allows employees eligible for service retirement to participate in the Teacher and Employee Retention Incentive (TERI) Program. TERI participants may retire and begin accumulating retirement benefits on a deferred basis without terminating employment for up to five years. Upon termination of employment or at the end of the TERI period, whichever is earlier, participants will begin receiving monthly service retirement benefits which will include any cost of living adjustments granted during the TERI period. Because participants are considered retired during the TERI period, they do not earn service credit, and are ineligible to receive group life insurance benefits or disability retirement benefits.

Effective July 1, 2006 employees participating in the SCRS were required to contribute 6.5 percent of all compensation. Effective July 1, 2007, the employer contribution rate was 12.48 percent which included a 3.42 percent surcharge to fund retiree health and dental insurance coverage. The Fund's actual contributions to the SCRS for the fiscal year ended June 30, 2008 were \$95,110, and equaled the required contributions of 9.06 percent (excluding the surcharge) for the year. Employer contributions for fiscal year 2007 were \$77,662 and for fiscal year 2006 were \$68,028. Also, the Fund paid employer group-life insurance contributions of \$1,664 in the current fiscal year at the rate of .15 percent of compensation.

The amounts paid by the South Carolina Second Injury Fund for pension and group-life benefits are reported as employer contributions. Article X, Section 16, of the South Carolina Constitution requires that all State operated retirement systems be

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008(Continued)

funded on a sound actuarial basis. Title 9 of the South Carolina Code of Laws of 1976, as amended, prescribes requirements relating to membership, benefits, and employee/employer contributions for each pension plan. Employee and employer contribution rates to SCRS are actuarially determined. The surcharges to fund retiree health and dental insurance are not part of the actuarially established rates. Annual benefits, payable monthly for life, are based on length of service and on average final compensation (an annualized average of the employee's highest 12 consecutive quarters of compensation).

The System does not make separate measurements of assets and pension liabilities for individual employers. Under Title 9 of the South Carolina Code of Laws, the Fund's liability under the plan is limited to the amounts of contributions (stated as a percentage of covered payroll) established by the State Budget and Control Board. Therefore, the Fund's liability under the pension plan is limited to the contribution requirements for the applicable year from amounts appropriated therefore in the South Carolina Appropriation Act and amounts from other applicable revenue sources. Accordingly, the Fund recognizes no contingent liability for unfunded costs associated with participation in the plan.

At retirement, employees participating in the SCRS receive additional service credit (at a rate of 20 days equals one month of service) for up to 90 days for accumulated unused sick leave.

Post-Employment and Other Employee Benefits**a. Plan Description**

In accordance with the South Carolina Code of Laws and the annual Appropriations Act, the State provides post-employment health and dental and long-term disability benefits to retired State and school district employees and their covered dependents. South Carolina Second Injury Fund contributes to the Retiree Medical Plan (RMP) and the Long-term Disability Plan (LTDP), cost-sharing multiple-employer defined benefit postemployment healthcare and long-term disability plans administered by the Employee Insurance Program (EIP), a part of the State Budget and Control Board (SBCB). Generally, retirees are eligible for the health and dental benefits if they have established at least ten years of retirement service credit. For new hires May 2, 2008 and after, retirees are eligible for benefits if they have established twenty-five years of service for 100% employer funding and fifteen through twenty-four years of service for 50% employer funding. Benefits become effective when the former employee retires under a State retirement system. Basic long-term disability (BLTD) benefits are provided to active state, public school district and participating local government employees approved for disability.

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008(Continued)

b. Funding Policies

Section 1-11-710 and 1-11-720 of the South Carolina Code of Laws of 1976, as amended, requires these postemployment healthcare and long-term disability benefits be funded through annual appropriations by the General Assembly for active employees to the EIP and participating retirees to the SBCB except the portion funded through the pension surcharge and provided from other applicable sources of the EIP for its active employees who are not funded by State General Fund appropriations. Employers participating in the RMP are mandated by State statute to contribute at a rate assessed each year by the Office of the State Budget, 3.42% of annual covered payroll for 2008. The EIP sets the employer contribution rate based on a pay-as-you-go basis. The South Carolina Second Injury Fund paid approximately \$35,902 applicable to the surcharge included with the employer contribution for retirement benefits for the fiscal year ended June 30, 2008. BLTD benefits are funded through a per person premium charged to State agencies, public school districts, and other participating local governments. The monthly premium per active employee paid to EIP was \$3.23 for the fiscal year ended June 30, 2008.

Effective May 1, 2008 the State established two trust funds through Act 195 for the purpose of funding and accounting for the employer costs of retiree health and dental insurance benefits and long-term disability insurance benefits. The South Carolina Retiree Health Insurance Trust Fund is primarily funded through the payroll surcharge. Other sources of funding include additional State appropriated dollars, accumulated EIP reserves, and income generated from investments. The Long Term Disability Insurance Trust Fund is primarily funded through investment income and employer contributions.

One may obtain complete financial statements for the benefit plans and the trust funds from Employee Insurance Program, 1201 Main Street, Suite 360, Columbia, SC 29201

Deferred Compensation Plans

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of the agency have elected to participate. The multiple-employer plans, created under Internal revenue code sections 457, 401(k), and 403(b) are administered by third parties and are not included in the Comprehensive Annual Financial Report of the State of South Carolina. Compensation deferred under the plans is placed in trust for the contributing employee. Employees may withdraw the current value of their contributions when they terminate State employment. Employees may also withdraw the current value of their contributions prior to termination if they meet requirements specified by the applicable plan. The State has no liability for losses under the plans.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

NOTE 7 - OPERATING LEASE

The Second Injury Fund paid \$95,304 in fiscal year 2008 for rental of office space from a party outside of state government, under an operating lease. The current lease will expire in October, 2009.

The Fund is obligated under this lease as follows:

<u>Year Ending</u> <u>June 30</u>	<u>Amounts</u>
2009	96,006
2010	32,338
Total Minimum Payments Required	<u>\$ 128,344</u>

NOTE 8 - TRANSACTIONS WITH STATE ENTITIES

The Fund has significant transactions with the State of South Carolina and various State agencies.

Services received at no cost from State agencies include maintenance of certain accounting records and payroll and disbursement processing from the Comptroller General and check preparation, banking and investment functions from the State Treasurer.

Other services received at no cost from the various divisions of the State Budget and Control Board include retirement and health plan administration, personnel management, assistance in the preparation of the State Budget, review and approval of certain budget amendments, procurement services and other centralized functions.

The Fund had financial transactions with various State agencies during the fiscal year. Significant payments were made to divisions of the State Budget and Control Board for retirement and insurance plans contributions, information technology support, insurance coverage, office supplies, printing, telephone, and interagency mail. Significant payments were also made for unemployment and workers' compensation coverage for employees. The amounts of 2008 expenses applicable to transactions with State entities are not readily available. As a self-insurer, the State Accident Fund ("SAF") pays assessments to the Fund and is also reimbursed by the Fund for claims it has paid. The Fund collected assessments from the State Accident Fund (SAF) in the amount of \$7,492,737 and reimbursed claims to the SAF in the amount of \$12,245,450 for workers compensation claims the SAF had paid. The Fund provided no services free of charge to other state agencies during the fiscal year.

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008(Continued)

NOTE 9 - ASSESSMENTS

The Second Injury Fund assesses all insurance carriers and self-insurers (including the State Accident Fund). Each carrier, under regulation prescribed by the Workers' Compensation Commission, shall make payments to the Fund in an amount equal to that proportion of one hundred thirty-five percent of the total disbursement made from the Fund during the preceding fiscal year less the amount of net assets in the Fund as of June thirtieth of the preceding fiscal year which the total normalized premiums of such carrier bore to the total normalized premiums of all carriers for the preceding calendar year. An employer who has ceased to be a self-insurer shall continue to be liable for any assessments into the Fund on account of any benefits paid by him during such calendar year. Any assessment levied or established in accordance with this section constitutes a personal debt of every employer or insurance carrier so assessed and is due and payable to the Second Injury Fund when payment is called for by the Fund. Assessments are done in September of each year. Assessments on carriers and self-insurers in the current fiscal year were \$110,981,619. Overall collections of assessments was \$110,987,814, which included some amounts from prior years.

NOTE 10 - RISK MANAGEMENT

The Fund is exposed to various risks of loss and maintains State or commercial insurance coverage for certain risks. The only risks known to the Fund's management that is not insured are for policy deductibles. Management believes such coverage is sufficient to preclude any significant uninsured losses to the Fund. The Fund has not had any claims in the past three years. There were no significant reductions in insurance coverage from coverage in the prior year. The Fund pays insurance premiums to certain other State agencies and commercial insurers to cover risk that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered premium losses sustained during the policy period in accord with the insurance policy and benefit program limits. Several State funds accumulate assets and the State itself assumes substantially all risks for the following:

1. Claims of covered employees for health and dental insurance benefits (Office of Insurance Services); and
2. Claims of covered public employees for long-term disability and group-life insurance benefits (Office of Insurance Service).
3. Claims of covered public employees for workers' compensation insurance benefits (State Accident Fund).
4. Claims of covered public employees for unemployment compensation insurance benefits (Employment Security Commission).

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

The Fund and other entities pay premiums to the states Insurance Reserve Fund (IRF) which issues policies, accumulate assets to cover the risks of loss and pays claims incurred for covered losses related to the following Fund assets, activities, and/or events.

1. Personal property and equipment - Eighty percent of each loss is covered by the IRF. Losses are subject to a \$250 deductible.
2. Data processing equipment - Coverage is up to \$300,000 per loss with a \$250 deductible.
3. Torts - General tort liability up to \$1,000,000 per occurrence.

The IRF is a self-insurer and purchases reinsurance to obtain certain services and specialized coverage and to limit losses in the areas of property, boiler and machinery, and automobile liability. The IRF's rates are determined actuarially.

State agencies are the primary participants in the State's Health and Disability Insurance Fund and in the IRF.

The Fund purchases insurance through a private carrier for employee fidelity bond insurance coverage for all employees to cover losses of up to \$50,000 arising from theft or misappropriations. Management believes based on exposure and likelihood of loss that this coverage is sufficient.

The Fund has not recorded an estimated claims expense related to insurance policy deductibles and policy limits because there is no evidence of asset impairment or other information to indicate a loss should be recorded as of June 30, 2008.

NOTE 11 - BANKRUPTCY CLAIM FUND - SPECIAL REVENUE FUND

In the fiscal year 1999 the Fund assumed the claims payment function for a bankrupt company's self-insured workers compensation fund. During fiscal year 2004, the Fund assumed the claims payment function for two other bankrupt companys. During the year the Fund received \$28,774 of interest earned on the cash deposits. Also interest receivable on these deposits at June 30, 2008 totaled \$4,885. Workers compensation claims and related expenses amounting to \$19,847 were paid by the Fund and \$108,000 of court ordered funds were received by the Fund in the fiscal year ended June 30, 2008. At June 30, 2008, \$688,621 of cash and \$4,885 of interest receivable was available for payment of claims. More funding may be made available through the bankruptcy court or recovery of third party liens, of which the amount recoverable is unknown at this time. After all monies available for payment of these claims are collected and disbursed, the Fund has no further liability for payment of the bankrupt companys' claims.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2008

(Continued)

Any reimbursement for administrative expense of the Fund would only be made from any remaining funds after all claims have been satisfied but it is not expected that there will be any remaining funds to reimburse such expenses.

NOTE 12 - GASB 31 ADJUSTMENTS

Effective January 1, 1998, the Division adopted Governmental Accounting Standards Board (GASB) Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. This statement requires that most investments of governmental entities be stated at fair value rather than at cost. For internal (and external) investment pools, this statement requires the equity position of each fund that sponsors the pool to be reported as assets in those funds. The unrealized gains included in cash and cash equivalents of the proprietary fund at June 30, 2008 were \$53,624.

NOTE 13 - TERMINATION OF SECOND INJURY FUND

In 2007 the Worker's Compensation Reform Act (S. 332) was ratified and signed by the Governor in FY 2007. The major affect of the Act is that the fund was put in "run-off" and will be terminated effective July 1, 2013. Certain effective dates are set out in the Act to permit an orderly termination of the Fund. Some of the significant dates are as follows:

Effective July 1, 2007 the factor used in the assessment calculation is reduced from 175% to 135%.

Effective July 1, 2008 no claims will be accepted with a date of injury of July 1, 2008 or after.

Effective January 1, 2011 no notice of new claims will be accepted.

Effective July 1, 2013 the Uninsured Employers' Fund will be transferred to the State Accident Fund.

Effective July 1, 2013 the Second Injury Fund will be terminated and all remaining obligations and assets will be transferred to the Budget and Control Board.

McDOWELL ♦ PEARMAN, LLC
CERTIFIED PUBLIC ACCOUNTANTS

W. M. McDowell, Jr. CPA
Ben J. Pearman, CPA
Cheryl H. Thigpen, CPA
• • • •

Charles M. Ayers, CPA
Lisa N. Smith, CPA

**INDEPENDENT AUDITOR'S 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**

Mr. Richard H. Gilbert, Jr.
Interim State Auditor
South Carolina Office of the State Auditor
Columbia, South Carolina

We have audited the financial statements of the South Carolina Second Injury Fund, as of and for the year ended June 30, 2008 and have issued our report thereon dated September 23, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the South Carolina Second Injury Fund's internal control over financial reporting as a basis for designing our auditing procedures 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 Fund's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency 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 misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the organization's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles, such that there is more than a remote likelihood that a misstatement of the

South Carolina Second Injury Fund's financial statements that is more than inconsequential will not be prevented or detected by the organization's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the South Carolina Second Injury Fund's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the South Carolina Second Injury Fund's financial statements are free of 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 determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information and use of those charged with governance, management, others within the organization, and is not intended to be or should not be used by anyone other than these specified parties.

A handwritten signature in black ink, appearing to read "M. Paul Rean". The signature is fluid and cursive, with the first name "M. Paul" and last name "Rean" clearly distinguishable.

September 23, 2008