

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

(CONTINUED)

18. Risk Management/Reinsurance (Continued)

The Insurance Reserve Fund purchases insurance and reinsurance and separately reports the related reinsurance premium and premium expenses. Insurance is purchased to cover risks where the Insurance Reserve Fund has limited expertise (aircraft insurance and ocean marine insurance). Reinsurance is purchased to limit the Insurance Reserve Fund's liability for catastrophic loss (property reinsurance and medical professional liability reinsurance), to obtain specialized engineering services (boiler and machinery reinsurance), or to obtain services for which the Insurance Reserve Fund is not adequately staffed (automobile liability reinsurance).

The Office of Insurance Services, Health, Life, and Disability Insurance Reserve Fund self-insures health and dental insurance for all participating governmental employees, including those of the Office. Additionally, effective January 1, 1999, the HLDIRF began offering a self-insured HMO point of service plan to certain employees of MUSC. The HLDIRF purchases coverage for basic group life, dependent life, optional supplemental life, group optional life and basic disability from commercial carriers. The State Life and Long-Term Disability program is also self-insured.

The Office of Insurance Services, Insurance Reserve Fund self insures Tort Liability Insurance, Automobile Physical Damage Insurance, and the self insured retention for Property, Medical Professional Liability, and Boiler and Machinery Insurance.

Reinsurance for catastrophic losses is purchased for losses above the following loss levels:

Property-\$2,000,000 per location/\$10,000,000 per occurrence
Medical malpractice-\$250,000

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19. Restatement

Retained earnings for fiscal year 2000 was understated due to an overstatement of depreciation expense of \$139,576. Beginning retained earning and accumulated depreciation have been restated. Adjustments to the previously presented 2000 amounts are as follows:

	<u>As Previously Reported</u>	<u>Increase (Decrease)</u>	<u>As Restated</u>
Balance Sheet			
Assets:			
Furniture and equipment, net of accumulated deposition	\$ 719,248	\$ 139,576	\$ 858,824
Fund equity:			
Retained earnings	85,992,760	139,576	86,132,336
Statement of Revenue, Expenditures and Changes in Fund Balance			
Operating Expenses:			
Professional and administrative fees	34,461,944	(139,576)	34,322,368
Statement of Cash Flows:			
Operating income (loss)	(87,186,043)	139,576	(87,046,467)
Adjustments to reconcile operating income (loss) to net cash provided by (used in) operating activities			
Depreciation expense	290,790	(139,576)	151,214

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20. Discussion of Fund Deficit in FY 2000-2001

During 2000/2001, the Health, Life and Disability Insurance Reserve Fund reported a net income of \$9,594,574. This income, along with losses in recent years, has resulted in a retained deficit of \$72,303,889 for the Fund at June 30, 2001. Additionally, Section 1-11-710(A)(4) of the South Carolina Code of Laws, 1976, as amended, stipulates that “a reserve equal to not less than an average of one and one-half months’ claims must be maintained in the accounts and all funds in excess of the reserve must be used to reduce premium rates or expand benefits as funding permits.” Under Proviso 63B.9 the reserve requirement was changed. The Proviso reads “Notwithstanding any other provision of law, the State Health Plan is only required to seek a twenty-two day reserve fund by the end of calendar year 2001.” As of June 30, 2001, the HLDIRF does not have a twenty-two day reserve fund. Management of the HLDIRF has reviewed the above situations and offers their analysis below. Although certain changes in the funding and coverages have taken place, there is no guarantee that the HLDIRF will return to a surplus position or that cash will be adequate to cover claims and administrative costs. Additional funding sources, such as further rate increases, State appropriations, etc. may be necessary to provide for the costs of the continued existence of the Plan.

Management’s analysis:

The State Health Plan continues to experience unprecedented claims expenditure growth. This is a result of continued dramatic increases in service volume and prescription drug costs. As was anticipated during calendar year 2000, State Health Plan expenditures exceeded income. Effective January 2001, a combination of increased funding and benefit payment reductions were enacted in an effort to improve the Plan's financial condition and restore Plan reserves. However, those measures were not sufficient to garner financial stability of the Plan. Further measures have been deemed necessary and additional funding increases and cost sharing initiatives have been enacted with an effective date of January 2002. These measures include a \$12 per month employee increase and an approximate average 9.5% increase in employer funding. In addition to increased funding, several cost sharing initiatives are slated for implementation. They include a \$100 deductible for Emergency Room services (waived if admitted), a \$50 deductible for Outpatient services (waived for oncology, physical therapy and Emergency Room), a \$2 copayment increase for prescription drugs, a “pay the difference” generic substitution policy and a \$100/person increase in the out-of-pocket prescription drug maximum.

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20. Discussion of Fund Deficit in FY 2000-2001 (Continued)

Additionally, beginning in 2002, the State Health Plan will be operating under a new Administrative Services Only contract with BCBSSC. This contract will allow for further cost savings initiatives for the Plan. Most notably, a nationwide network of hospitals and physicians, for which discounts will be made available to the Plan for members receiving services outside of South Carolina.

Management is and will be continually monitoring the financial condition of the State Health Plan, as well as keeping the Board and other interested parties updated as to the Plan's financial status.

21. Subsequent Event

In February 2001, the South Carolina Budget and Control Board reorganized the Office of Insurance Services. This reorganization, however, did not become effective from an accounting and budgetary basis until July 1, 2001.

The Insurance Reserve Fund was transferred to the Office of General Services. The Health, Life, and Disability Insurance Reserve Fund was transferred to the new Employee Benefits Division in the South Carolina Retirement System. The new name of the Health, Life, and Disability Insurance Reserve fund is the Employee Insurance Program.

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22. Reconciliation of Claims Liabilities by Fund

The schedule below presents the changes in claims liabilities for the past two years for the Office's two internal service funds.

	Insurance Reserve Fund		Health, Life, and Disability Insurance Reserve Fund	
	2001	2000	2001	2000
	(In thousands)		(In thousands)	
Unpaid claims and claim adjustment expenses at beginning of the fiscal year	\$ 151,149	\$ 138,899	\$ 157,439	\$ 128,806
Incurred claims and claim adjustment expenses:				
Provision for insured events of the current fiscal year	37,430	36,860	629,985	666,644
Increases (decreases) in provision for insured events of prior fiscal years	15,083	2,984	146,672	75,238
Total incurred claims and claim adjustment expenses	52,513	39,844	776,657	741,882
Payments:				
Claims and claim adjustment expenses attributable to insured events of the current fiscal year	8,659	7,422	554,842	566,987
Claims and claim adjustment expenses attributable to insured events of prior fiscal years	26,760	20,172	238,225	146,262
Total payments	35,419	27,594	793,067	713,249
Total unpaid claims and claim adjustment expenses at end of the fiscal year	<u>\$ 168,243</u>	<u>\$ 151,149</u>	<u>\$ 141,029</u>	<u>\$ 157,439</u>
The above totals are comprised of the following:				
Claims payable	\$ 106,986	\$ 89,916	\$ 44,185	\$ 39,039
Claims incurred but not reported	61,257	61,233	96,844	118,400
Total	<u>\$ 168,243</u>	<u>\$ 151,149</u>	<u>\$ 141,029</u>	<u>\$ 157,439</u>

The HMO self-insured managed care plan liability at June 30, 2001 was \$1,368,267 and is included in the claims liability of HLDIRF listed above.