

October 8, 1998

The Honorable David M. Beasley, Governor  
and  
Members of the South Carolina State Budget and Control Board  
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina State Budget and Control Board Office of Insurance Services for the fiscal year ended June 30, 1998, was issued by Milhous, DeLoach & Williamson, L.L.P., 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,

Thomas L. Wagner, Jr., CPA  
State Auditor

TLWjr/jap

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

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AUDITED FINANCIAL STATEMENTS  
AND OTHER FINANCIAL INFORMATION

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YEARS ENDED JUNE 30, 1998 AND 1997

WITH  
REPORT OF INDEPENDENT AUDITORS

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

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AUDITED FINANCIAL STATEMENTS  
AND OTHER FINANCIAL INFORMATION

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YEARS ENDED JUNE 30, 1998 AND 1997

WITH

REPORT OF INDEPENDENT AUDITORS

**CONTENTS**

Report of Independent Auditors .....	1
<b>Combined Financial Statements</b>	
Combined Balance Sheets .....	3
Combined Statements of Revenues, Expenses, and Changes in Retained Earnings .....	4
Combined Statements of Cash Flows .....	5
Notes to Combined Financial Statements (An Integral Part of the Financial Statements) .....	6
<b>Other Financial Information</b>	
Combining Balance Sheet - All Internal Service Funds .....	38
Combining Statement of Revenues, Expenses, and Changes in Retained Earnings - All Internal Service Funds .....	39
Combining Statement of Cash Flows - All Internal Service Funds.....	40

## **REPORT OF INDEPENDENT AUDITORS**

Mr. Thomas L. Wagner, Jr., CPA  
State Auditor  
State of South Carolina  
Columbia, South Carolina

We have audited the accompanying combined financial statements of the South Carolina State Budget and Control Board, Office of Insurance Services (the “Office”) as of and for the years ended June 30, 1998 and 1997, as listed in the table of contents. These financial statements are the responsibility of the management of the South Carolina State Budget and Control Board, Office of Insurance Services. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. 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 audits provide a reasonable basis for our opinion.

As discussed in *Note 1*, the accompanying financial statements of the South Carolina State Budget and Control Board, Office of Insurance Services are intended to present the financial position and results of operations and cash flows of its proprietary fund type of only that portion of the funds of the State of South Carolina that is attributable to the transactions of the funds of the South Carolina State Budget and Control Board, Office of Insurance Services.

As also discussed in *Note 1*, the Office changed its method of accounting for investments by implementing Governmental Accounting Standards Board Statement Number 31, “Accounting and Financial Reporting for certain Investments and for External Investment Pools.”

In our opinion, the combined financial statements referred to above present fairly, in all material respects, the financial position of the funds of the South Carolina State Budget and Control Board, Office of Insurance Services, as of June 30, 1998 and 1997, and the results of operations and cash flows of its proprietary fund type for the years then ended in conformity with generally accepted accounting principles.

Our audit was made for the purpose of forming an opinion on the combined financial statements taken as a whole. The other financial information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the combined financial statements. Such information has been subjected to the auditing procedures applied in the audits of the combined financial statements and, in our opinion, is fairly stated in all material respects in relation to the combined financial statements taken as a whole.

September 4, 1998

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED BALANCE SHEETS

JUNE 30, 1998

	<b>Proprietary Fund Type</b>	
	<b>Internal Service</b>	
	<b>1998</b>	<b>1997 (as restated)</b>
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 236,861,448	\$ 215,517,128
Premiums receivable	14,560,540	16,063,835
Reinsurance recovery receivable	1,670,771	1,272,083
Prescription Drug Rebate receivable	398,446	1,015,242
Current portion of notes receivable	3,679,888	5,462,122
Accrued interest	5,680,055	6,862,424
Due from South Carolina Retirement Division	13,815,183	13,039,359
Prepaid insurance	2,210,550	2,450,700
Other assets	185,669	420,409
Total current assets	279,062,550	262,103,302
Non-current assets:		
Investments	199,003,321	218,646,944
Long-term notes receivable	30,836,296	34,385,175
Furniture and equipment, net of accumulated depreciation	1,012,047	1,317,785
Total non-current assets	230,851,664	254,349,904
Total assets	<u>\$ 509,914,214</u>	<u>\$ 516,453,206</u>
<b>Liabilities and Fund Equity</b>		
Current liabilities:		
Accounts payable	\$ 233,335	\$ 548,555
Accrued payroll	493,664	404,821
Claims payable	118,798,784	125,689,758
Deferred premium revenue	40,679,428	34,120,069
Claims incurred but not reported	129,623,258	129,176,314
Accrued compensated absences	499,166	522,725
Total current liabilities	290,327,635	290,462,242
Contingencies ( <i>Note 13</i> )	—	—
Fund equity:		
Contributed capital	45,974	6,539
Retained earnings:		
Reserved for:		
Installment Purchase Program	35,000,000	35,000,000
Savannah Valley Development Loans	20,000,000	20,000,000
Unreserved	164,540,605	170,984,425
Total fund equity	<u>219,586,579</u>	<u>225,990,964</u>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED BALANCE SHEETS

JUNE 30, 1998

Total liabilities and fund equity

\$ 509,914,214

\$ 516,453,206

*See accompanying notes.*

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED STATEMENTS OF REVENUES, EXPENSES,  
AND CHANGES IN RETAINED EARNINGS

YEAR ENDED JUNE 30, 1998 AND 1997

	Proprietary Fund Type	
	Internal Service	
	1998	1997 (as restated)
<b>Operating Revenues</b>		
Insurance premiums:		
Tort liability	\$ 23,305,157	\$ 19,737,418
Auto liability	15,068,783	13,783,021
Professional liability	6,434,220	7,099,310
Comprehensive and collision	2,125,930	2,038,344
School bus liability	3,523,205	3,527,141
Fire	7,174,898	7,330,789
Extended coverage	3,608,125	3,702,452
Inland Marine	2,555,601	2,394,696
Active employees:		
Health	435,871,959	419,358,006
Dental	36,991,502	33,973,039
Life	3,022,466	1,327,661
Long term disability	9,935,026	9,112,323
Dependent/optional life	17,263,346	15,474,574
Retirees:		
Health	28,660,684	27,540,528
Dental	2,061,828	1,867,163
Retiree surcharge	86,311,816	84,664,255
Other premium revenues	3,289,072	3,275,851
Prescription drug rebates	3,648,135	4,032,117
Income from deposits and investments	35,119,197	39,159,276
Notes receivable interest	2,556,722	2,535,312
Other	274,557	70,870
Total operating revenues	728,802,229	702,004,146
<b>Operating Expenses</b>		
Reinsurance premiums	23,584,010	27,553,445
Premiums	96,272,711	90,425,550
Claims:		
Tort liability	6,439,420	15,259,763
School bus liability	4,707,494	3,663,618
Fire	2,729,166	3,129,257
Extended coverage	2,010,253	4,793,224
Health	505,167,625	461,283,045
Dental	40,119,284	39,735,265
Life	1,228,007	845,851
Long term disability	7,050,511	11,342,365
Hospitals and physicians	5,338,828	7,118,073
Auto and Inland Marine	2,643,351	2,665,603
Other	102,603	156,699
Professional and administrative fees	26,781,325	31,583,972
Administrative and planning	773,224	1,436,542
Insurance Benefits Administration	5,868,436	4,895,994
Insurance Reserve Administration	4,327,577	4,213,383
Total operating expenses	735,143,825	710,101,649
Operating loss	(6,341,596)	(8,097,503)
Loss on disposal of assets	(102,224)	(65,196)
Net loss	(6,443,820)	(8,162,699)
Retained earnings, beginning of year, as restated ( <i>Note 16</i> )	225,984,425	227,566,644
Residual equity transfer from South Carolina Retirement Division ( <i>Note 13</i> )	—	6,580,480



SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED STATEMENTS OF REVENUES, EXPENSES,  
AND CHANGES IN RETAINED EARNINGS

YEAR ENDED JUNE 30, 1998 AND 1997

Retained earnings at end of year, as restated

\$ 219,540,605

\$ 225,984,425

*See accompanying notes.*

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED STATEMENTS OF CASH FLOWS

YEARS ENDED JUNE 30, 1998 AND 1997

	<b>Proprietary Fund Type</b>	
	<b>Internal Service</b>	
	<b>1998</b>	<b>1997 (as restated)</b>
<b>Cash Flows from Operating Activities</b>		
Operating loss	\$ (6,341,596)	\$ (8,097,503)
Reclassify investment income included in operating loss to investing activity	(37,675,919)	(41,694,588)
Transfer of cash and cash equivalents from South Carolina Retirement Division	—	8,953,076
Adjustments to reconcile operating loss to net cash used in operating activities:		
Depreciation expense	268,294	287,371
Change in assets-(increase) decrease:		
Premiums receivable	1,503,295	1,155,948
Reinsurance recovery receivable	(398,688)	(135,513)
Due from South Carolina Retirement Division	(775,824)	838,754
Prepaid insurance, preventive drug rebate receivable and other assets	1,091,687	(1,124,310)
Change in liabilities-increase (decrease):		
Accounts payable, accrued payroll and compensated absences	(249,937)	(1,622,129)
Deferred premium revenue	6,559,359	1,525,177
Claims payable and incurred but not reported	(6,126,882)	13,388,743
Total adjustments	1,871,304	14,314,041
Net cash used in operating activities	(42,146,211)	(26,524,974)
<b>Cash Flows from Capital and Related Financing Activities</b>		
Purchase of fixed assets	(76,067)	(543,944)
Net cash used in capital and related financing activities	(76,067)	(543,944)
<b>Cash Flows from Investing Activities:</b>		
Principal payments received on notes receivable	6,470,183	5,786,062
Funds disbursed as notes receivable	(1,139,070)	(5,833,771)
Purchases of investments	(52,243,870)	(89,278,748)
Proceeds from sales and maturity of investments	75,434,211	53,869,760
Interest received-deposits and investments	32,204,160	31,818,117
Premiums amortized and discounts accreted	284,262	—
Interest received-notes receivable	2,556,722	2,743,709
Net cash provided by (used in) investing activities	63,566,598	(894,871)
Net increase (decrease) in cash and cash equivalents	21,344,320	(27,963,789)
Cash and cash equivalents, beginning of year	215,517,128	243,480,917
Cash and cash equivalents, end of year	<u>\$ 236,861,448</u>	<u>\$ 215,517,128</u>
<b>Supplemental Information</b>		
Noncash capital and related financing activities:		
Receipt of contributed capital fixed assets	\$ 39,435	\$ —
Disposal of other fixed assets	(50,721)	(69,826)
Noncash investing activities:		
Receipt of investments (through residual equity transfer- <i>Note 13</i> )	—	15,907,305
Receipt of accrued interest receivable (through residual equity transfer- <i>Note 13</i> )	—	267,119
Noncash operating activities:		
Assumption of accounts payable and accrued expenses (through residual equity-transfer <i>Note 13</i> )	—	5,844
Assumption of incurred but unpaid claims (through residual equity transfer- <i>Note 13</i> )	—	18,541,176

*See accompanying notes.*

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED STATEMENT OF CASH FLOWS - PROPRIETARY FUND TYPE

- CONTINUED -

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

JUNE 30, 1998 AND 1997

**1. Basis of Presentation and Summary of Significant Accounting Policies**

The financial statements of all funds of the South Carolina State Budget and Control Board, Office of Insurance Services (the "Office") were prepared in conformity with generally accepted accounting principles (GAAP) as applied to governmental entities. The Government Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the Office's accounting policies are described below.

**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 of its component units. Component units are legally separate organizations for which the elected officials of 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 government or 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 bond debt without approval by another government.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

JUNE 30, 1998 AND 1997

Based on these criteria, the Office has determined that it has no component units. This financial reporting entity only includes the Office, a primary entity.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Reporting Entity (Continued)

The South Carolina State Budget and Control Board, Office of Insurance Services, Insurance Reserve Fund and Health, Life, and Disability Insurance Reserve Fund are funds of the South Carolina State Budget and Control Board, which is a part of the State of South Carolina primary government. All funds of the Office of Insurance Services are included in this report and no other Offices or funds of the South Carolina State Budget and Control Board or any other part of the State of South Carolina primary government are included. Effective July 1, 1994, the Office of Insurance Services is one of four offices under control of the Division of Operations of the South Carolina State Budget and Control Board (the Board). The Board is composed of the Governor; the State Treasurer; the Comptroller General; the Chairman of the Senate Finance Committee; and the Chairman of the House Ways and Means Committee; all of whom serve in an ex-officio capacity.

The South Carolina State Budget and Control Board, formerly the Budget Commission, was established and created by Reorganization Plan No. 2 adopted by the General Assembly in 1950 pursuant to the terms and provisions of Act 621, Acts of 1948. Under the Act, ten state agencies were abolished as separate entities and their functions and duties were brought under the supervision of the Budget and Control Board. The funds and account groups of the Budget and Control Board are included in the Comprehensive Annual Financial Report of the State of South Carolina.

The Office operates as a unit under the Budget and Control Board and its Executive Director. The laws of the State and the policies and procedures specified by the State for State agencies are applicable to the Office's activities. The accompanying financial statements present the financial position and results of operations solely of the Office and do not include any other agencies or any component units of the State of South Carolina.

Basis of Presentation

The financial statements present all funds of the South Carolina State Budget and Control Board, Office of Insurance Services. The financial statements of the Internal Service Funds include the Balance Sheet; Statement of Revenues, Expenses, and Changes in Retained Earnings; and the Statement of Cash Flows.

The Internal Service Funds presented include:

- Insurance Reserve Fund (IRF)

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

- Health, Life, and Disability Insurance Reserve Fund (HLDIRF)

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Basis of Presentation (Continued)

The Office of Insurance Services was created by the Budget and Control Board on June 5, 1989 to manage insurance programs provided by the State for its employees, retirees, agencies, institutions, and political subdivisions. The Office was formed with the Insurance Reserve Fund section from the Office of General Services and the Insurance Benefits section from the South Carolina Retirement Division. The Administration and Planning section was added to these two sections to complete the Office. Additionally, effective July 1, 1996, the State Life and Long-Term Disability program was transferred to the Office from the South Carolina Retirement Division. This program is accounted for in the Health, Life, and Disability Insurance Reserve Fund.

Programs managed by the Office's Insurance Reserve Fund section are authorized in the following sections of the South Carolina Code of Laws, 1976, as amended: Section 1-11-140 (tort liability, medical professional liability for individuals and entities and risk management section); Section 1-11-710 (risk management section); Regulation 19-612 (automobile liability); Section 10-7-10 et. seq. (property); Section 59-67-710 (school bus liability); and Section 59-67-790 (school bus pupil injury). Section 15-78-10 et. seq. (the S.C. Tort Claims Act) further defines parameters of coverage provided by the Insurance Reserve Fund.

The group health, dental, life, accidental death and dismemberment and disability programs managed by the Office's HLDIRF are authorized in Sections 1-11-710 and 1-11-720 of the South Carolina Code of Laws of 1976, as amended. The long-term care program managed by the Office is authorized in Section 1-11-740 of the South Carolina Code of Laws of 1976, as amended.

The Office also has an administrative and planning staff responsible for overseeing the operations of the Office. Cost of operations for the administrative and planning staff are allocated equally to the IRF and the HLDIRF.

Fund Accounting

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



SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Fund Accounting (Continued)

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; however, in the accompanying financial statements, funds that have similar characteristics have been combined into fund types. Accordingly, all financial transactions in the combined statements have been reported by fund type.

Funds are classified into three categories: governmental, proprietary and fiduciary. Each category, in turn, is divided into separate “fund types”. The Office of Insurance Services of the South Carolina State Budget and Control Board uses the Proprietary Fund Type.

Description of Funds

**Proprietary Funds**-Proprietary funds are used to account for activities similar to those found in the private sector, where the determination of net income is necessary or useful for sound financial administration. Goods or services from such activities can be provided either to outside parties (enterprise funds) or to other departments or agencies primarily within the government (internal service funds). The following funds are reported as proprietary funds:

- (1) **Insurance Reserve Fund (internal service fund)**-The Insurance Reserve Fund insures state agencies, school districts, special purpose political subdivisions, county governments and municipal governments in South Carolina. The Insurance Reserve Fund provides property insurance on governmentally owned buildings, the contents of such buildings, equipment and automobiles. The Insurance Reserve Fund provides automobile liability insurance on governmentally owned vehicles and school buses, tort liability insurance for government premises and operations, and medical professional liability for hospitals. The Insurance Reserve Fund is a self-insurer and purchases reinsurance to limit losses in the areas of property insurance, boiler and machinery insurance, automobile liability insurance, and medical professional liability insurance. The Insurance Reserve Fund collects premiums from participating entities, issues policies, and pays claims incurred under the policies from accumulated premiums and earnings on investments and notes receivable. The premium rates are determined actuarially and approved by the South Carolina Budget and Control Board. The

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

Insurance Reserve Fund allocates the costs of providing claims servicing and claims payments by charging each participant a premium. Interest income is considered in the premium rate setting process.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

- (2) **Health, Life, and Disability Insurance Reserve Fund (internal service fund)**-The Health, Life, and Disability Insurance Reserve Fund provides health insurance to eligible employees and retirees of State agencies and school districts who elect coverage through either a health maintenance organization or through the State's self-insured health plan. The State Life and Long-Term Disability Plan is a self insured group life and long-term disability plan available to eligible active state and public school employees enrolled in a State health plan. All dental coverage is through the State's self-insured plan which is available to eligible State and public school employees and retirees. Health and dental premiums are paid from State funds and through payroll deductions for eligible State and public school employees. Premiums for the State Life and Long-Term Disability Plan are paid through payroll deductions. Premiums for participating retirees are paid by the Agencies and the School Districts through the retirement system (employer share) and directly from the employee (employee share). State agencies and the local school districts pay the premiums for the following insured plans which are available to eligible full-time employees enrolled in a State health plan: (1) basic group life, and (2) basic long-term disability plan. The dependent/optional life program is available to eligible State and public school employees. Premiums for the dependent/optional life program are paid through payroll deduction. Premiums and the retiree surcharge (see *Note 4*) for the self-insured health and dental plans are actuarially determined and approved by the South Carolina State Budget and Control Board. Long-term care insurance is also available to eligible State and public school employees. Premiums for long-term care insurance are paid through payroll deductions. The long-term care plan is fully insured. Details on eligibility requirements and coverage for all plans are contained in the *Insurance Benefits Guide*. Premium rates for all plans are reviewed on a calendar year basis annually and adjusted as considered necessary after actuarial calculation. Interest income is considered in the premium rate setting process. The State as the predominant participant, retains the risk of loss for the self-insured health, dental, supplemental group-life and supplemental long-term disability coverages.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Basis of Accounting

The accounting and financial reporting treatment applied to a fund is determined by its measurement focus.

All proprietary funds are accounted for using the economic resources accounting measurement focus which is upon determination of net income, financial position, and cash flows. Under this method, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. Fund equity (i.e., net total assets) is segregated into contributed capital and retained earnings components. Proprietary fund-type operating statements present increases (e.g., revenues) and decreases (e.g., expenses) in net total assets.

All proprietary funds use 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 Insurance Reserve Fund reports claims liabilities when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated. The Health, Life, and Disability Insurance Reserve Fund establishes claims liabilities when the information available prior to the issuance of the financial statements indicates it is probable a liability has been incurred by the date of the financial statements and the amount can be reasonably estimated.

The Governmental Accounting Standards Board (GASB) is the recognized standard-setting body for generally accepted accounting principles for all State governmental entities. The accounting policies of the Office conform to generally accepted accounting principles applicable to governmental proprietary activities as prescribed by GASB. Accordingly, the Office applies all applicable GASB pronouncements and has elected to apply only those applicable standards issued by the Financial Accounting Standards Board on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

Change in Accounting Principal

During the year ended June 30, 1998, the Office was required to implement Governmental Accounting Standards Board (GASB) statement Number 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools" (GASB #31). GASB #31 requires that investments be reported at fair value.

Cash and Cash Equivalents

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

The amounts shown in the financial statements as “cash and cash equivalents” represent cash on deposit with the State Treasurer and amounts invested in various short-term instruments by the State Treasurer and held in separate agency accounts, as part of the State’s cash management pool.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Office considers all highly liquid securities purchased with a maturity of three months or less to be cash equivalents. Because the 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 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 cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of funds.

The State's cash management pool consists of a general deposit account and several special deposit accounts. The State records each fund's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. Investments in the pool are recorded at cost. 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. Amortization of premiums and discounts is allocated and reported as interest income. 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.

Although the cash management pool includes some long-term investments, it operates as a demand deposit account; therefore, for credit risk information pertaining to the cash management pool, see the deposits disclosures in *Note 2*.

Investments

Investments, in accordance with GASB #31, are valued at fair value.

The Office amortizes bond premiums and accretes bond discounts using the effective interest method from the date of purchase to maturity. Unrealized gains and losses in investments are recognized as investment income in the period of occurrence. Interest income consists of interest earned during the year, amortization of premiums and accretion of discounts, and recognized gains/losses on securities. Earnings are posted to the agency's account at the end of each month.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

Securities and securities transactions are reflected in the financial statements on a trade-date basis.

Premium Revenue-Insurance Reserve Fund

Premiums billed to agencies (premiums receivable) for insurance coverage are deferred and amortized into income over the term of the insurance policy.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Premium Revenue-Health, Life, and Disability Insurance Reserve Fund

Premiums billed to employers, employees and retirees (premiums receivable) for insurance coverage are recorded as revenue when earned on a monthly basis. The retiree surcharge on employees is recognized as the liability is incurred by the various State agencies and school districts.

Deferred Premium Revenue

Premiums billed in advance of coverage, payments received in advance of coverage, or in excess of amounts billed and premiums collected but unearned are recorded as deferred premium revenue in the Insurance Reserve Fund and the Health, Life, and Disability Insurance Reserve Fund.

Reinsurance Recovery Receivable

Reinsurance Recovery Receivable represents claims that have been paid by the Insurance Reserve Fund which are recoverable from reinsurers. Reinsurance permits partial recovery of losses from reinsurance; however, the Insurance Reserve Fund, as direct insurers remains primarily liable. Amounts deemed recoverable from reinsurance are deducted from claims expenses.

Prepaid Insurance Premiums

Payments made to insurers and reinsurers for services that will benefit future periods are recorded as Prepaid expenses and other assets. The related expense is recognized prorata over the policy periods.

Fixed Assets

Fixed assets held in proprietary funds are capitalized at cost if purchased. Fixed assets contributed by other State agencies or funds are recorded at the State's original acquisition cost less accumulated depreciation from the purchase date. Assets donated by other parties are valued at fair market value at the date of gift. The Office has one class of fixed asset, equipment, which is depreciated on a straight-line basis over the estimated useful lives of 5-10 years.



SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Claims Liabilities Including Claims Incurred but not Reported (IBNR)

Losses are recorded at estimated amounts at the time they are reported and include a provision for expenses associated with claim settlements. Insurance claims are expensed as incurred over the period of coverage. The Office establishes an unpaid claim liability for claims in the process of review, and for IBNR claims. The liability for IBNR claims is actuarially estimated based on the most current historical claims experience of previous payments, changes in number of members and participants, inflation, award trends, and estimates of health care trend (cost, utilization and intensity of services) changes. Estimates of liabilities for incurred claims are continually reviewed and revised as changes in these factors occur and revisions are reflected in the current year's operating statement in the applicable claims expense. The liability is reported net of estimated receivables for salvage subrogation and reinsurance for the Insurance Reserve Fund. Claims payable and the related expense have been reduced by reinsurance recoveries receivable for claims paid and for estimated receivables for claims to be paid of approximately \$5,000,000 and \$4,700,000 as of June 30, 1998 and 1997, respectively. Amounts for allocated and unallocated claims adjustment expenses have been included in the calculation of IBNR.

Claim costs for basic group life and long-term disability coverages are actuarially calculated using the one-year term cost method; the cost of coverage is the present value of all benefit payments that will be made on expected claims incurred during the year following the valuation date. Claim liabilities are equal to the present value, as of the valuation date, of all future payments to be made for disabilities and deaths up to that date. Actuarial assumptions include an interest rate of 5.50% for 1998 and 1997, compounded annually.

Claims Payable-Insurance Reserve Fund

Claims payable represents claims resulting from losses that have been incurred and not paid at June 30. The claims payable balance is based on actual losses incurred and settled and estimated losses for claims in the final stages of review and settlement.

Claims Payable-Health, Life, and Disability Insurance Reserve Fund

Claims payable in the Health, Life, and Disability Insurance Reserve Fund represents claims related to health claims, dental claims, and State Life and Long-Term Disability claims payable at June 30. The claims payable balance is based on claims that have been paid by the third party administrators on behalf of the Health, Life, and Disability Insurance Reserve Fund.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**1. Basis of Presentation and Summary of Significant Accounting Policies (Continued)**

Compensated Absence

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 maximums of 180 days sick leave and of 45 days annual vacation leave, except that faculty members do not accrue annual leave. Upon termination of State employment, employees are entitled to be paid for accumulated unused annual vacation leave up to the maximum, but are not entitled to any payment for unused sick leave. The compensated absences liability includes accrued annual leave earned for which the employees are entitled to paid time off or payment at termination. The leave liability also includes an estimate for unused sick leave and leave from the agency's leave transfer pool for employees who have been approved as leave recipients under personal emergency circumstances which commenced on or before June 30, 1998. The Office 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 in each applicable internal service fund. The net change in the liability is recorded in the current year in the applicable funds.

Fund Equity

Contributed capital is recorded in proprietary funds that have received contributions of property or other assets from other funds and other agencies. Reserves represent those portions of fund equity legally segregated for a specific future use. Retained earnings is recorded in proprietary funds to reflect the net accumulated earnings of the fund.

Budget

The General Assembly enacts a budget for the Office within the Division of Operations budgetary unit of the State Budget and Control Board which includes only administrative activities and provides specific line-item appropriations by program within the budgetary unit. A statement of budgeted versus actual expenditures by line-item is not required for internal service funds and therefore is not presented.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**2. Investments and Deposits**

As prescribed by Statute, the State Treasurer is the custodian and investment manager of all investments and deposits of the Office.

The following table presents the amortized cost and market values of the long-term investments of the Office at June 30, 1998 and 1997.

	<b>Amortized Cost</b>		<b>Market</b>	
	<b>1998</b>	<b>1997</b>	<b>1998</b>	<b>1997</b>
U.S. Treasury obligations	\$ 22,984,517	\$ 22,662,505	\$ 31,073,106	\$ 29,912,748
U.S. Government agencies and government-insured securities	87,628,024	133,320,160	88,999,080	134,288,922
Corporate bonds	19,935,970	49,760,589	21,395,171	49,905,890
Financial and other	56,322,238	4,584,262	57,535,964	4,539,384
<b>Total</b>	<b>\$ 186,870,749</b>	<b>\$ 210,327,516</b>	<b>\$ 199,003,321</b>	<b>\$ 218,646,944</b>

At June 30, 1998, the amortized cost of the above investments was comprised of the following:

	<b>Par Value</b>	<b>Unamortized Premiums</b>	<b>Unaccrued Discounts</b>	<b>Amortized Cost</b>
U.S. Treasury obligations	\$ 23,285,000	\$ 11,204	\$ (311,687)	\$ 22,984,517
U.S. Government agencies and government-insured securities	87,814,179	2,719	(188,874)	87,628,024
Corporate Bonds	20,430,000	86,747	(580,777)	19,935,970
Financial and other	56,080,000	629,652	(387,414)	56,322,238
<b>Total</b>	<b>\$ 187,609,179</b>	<b>\$ 730,322</b>	<b>\$ (1,468,752)</b>	<b>\$ 186,870,749</b>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**2. Investments and Deposits (Continued)**

The accounts classified as investments in the financial statements comprise investments held for the Office and the State of South Carolina which are legally restricted and earnings thereon become revenue of the specific fund from which the investment was made. These investments are specific, identifiable investment securities, some of which may be included in one of the State Treasurer's investment pools.

The investment types listed above include all investment types in which monies were held throughout the fiscal year. For all investment classifications reported above, the balances therein fluctuated minimally in excess of the year-end balances throughout the year ended June 30, 1998. As discussed in *Note 1*, GASB #31 required investments reported at fair value. Therefore, gains and losses recognized due to market fluctuations are recognized as income on deposits and investments.

In accordance with State Law, the IRF and the HLDIRF may invest in a variety of instruments including obligations of the United States and its agencies and securities fully guaranteed by the United States, certain corporate obligations, certain shares of Federal savings and loan associations and State chartered savings and loan associations, and collateralized repurchase agreements. All investments are required to be insured or registered, or held by the State or its agent in the name of the State Treasurer as custodian.

The Office's investments are categorized to give an indication of the level of risk assumed by the entity at year-end. The credit risk categories are concerned with custodial credit risk, which is the risk that a government will not be able to recover the value of investment or collateral securities that are in the possession of an outside party if the counterparty to the investment transaction fails. There are three categories of credit risk.

- (1) Insured or registered, or securities held by the government or its agent in the government's name.
- (2) Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the government's name.
- (3) Uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the government's name.

At June 30, 1998 and 1997, all of the Office's investments were in Category (1).

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**2. Investments and Deposits (Continued)**

All deposits with financial institutions are required to be insured or collateralized with securities held by the State or its agent in the State Treasurer's name as custodian. At June 30, 1998 and 1997, 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 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 agents in the State's name. Information pertaining to the carrying amounts, market values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

During 1998 and 1997, the following amounts (which apply to all investments) were included in interest income:

	<u>1998</u>	<u>1997</u>
Discount accretion	\$ 405,658	\$ 148,522
Premium amortization	(121,395)	(34,759)
Net accretion/amortization included in interest income	<u>\$ 284,263</u>	<u>\$ 113,763</u>

Cash and cash equivalents whose cost approximates market value at June 30, 1998 and 1997, were composed of the following:

	<u>June 30, 1998</u>			
	<u>Cash</u>	<u>Short-Term Investments</u>	<u>Repurchase Agreements</u>	<u>Total</u>
IRF	\$ 8,655,852	\$ 29,655,322	\$ 50,740,000	\$ 89,051,174
HLDIRF	144,875,274	—	2,935,000	147,810,274
	<u>\$ 153,531,126</u>	<u>\$ 29,655,322</u>	<u>\$ 53,675,000</u>	<u>\$ 236,861,448</u>
	<u>June 30, 1997</u>			
	<u>Cash</u>	<u>Short-Term Investments</u>	<u>Repurchase Agreements</u>	<u>Total</u>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

IRF	\$ 119,688	\$ 20,000,000	\$ 18,005,000	\$ 38,124,688
HLDIRF	<u>174,362,440</u>	<u>—</u>	<u>3,030,000</u>	<u>177,392,440</u>
	<u>\$ 174,482,128</u>	<u>\$ 20,000,000</u>	<u>\$ 21,035,000</u>	<u>\$ 215,517,128</u>

**2. Investments and Deposits (Continued)**

At June 30, 1998 and 1997, the IRF bank balances totaled \$4,917,653 and \$206,881, respectively and the HLDIRF bank balances totaled \$144,502,247 and \$175,059,464, respectively. All of these amounts were on deposit with the South Carolina State Treasurer's Office.

The short-term instruments consists of U.S. Government agency and government-insured securities whose cost approximates market at June 30, 1998. The short-term investments and repurchase agreements are considered Category (1) in the risk classifications as defined previously. As of June 30, 1998 and 1997, there were no unamortized premiums or unaccreted discounts pertaining to the short-term investments and repurchase agreements disclosed above.

The investment types listed above include all investment types in which monies were held throughout the year ended June 30, 1998. Due to higher cash flows at certain times during the year, the Office's investment in repurchase agreements and short-term investments fluctuated significantly. The maximum amounts held in these classifications during the year ended June 30, 1998 and 1997, were as follows:

	<u>1998</u>	<u>1997</u>
Short-term investments	<u>\$ 30,000,000</u>	<u>\$ 20,000,000</u>
Repurchase agreements	<u>\$ 60,000,000</u>	<u>\$ 55,465,624</u>

A summary of total investments is as follows:

	<u>1998</u>		<u>1997</u>	
	<u>Amortized Cost</u>	<u>Market Value</u>	<u>Amortized Cost</u>	<u>Market Value</u>
Long-term investments	\$ 186,870,749	\$ 199,003,321	\$ 210,327,516	\$ 218,646,945
Short-term investments	29,655,322	29,655,322	20,000,000	20,000,000
Repurchase agreements	53,675,000	53,675,000	21,035,000	21,035,000

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

<u>\$ 270,201,071</u>	<u>\$ 282,333,643</u>	<u>\$ 251,362,516</u>	<u>\$ 259,681,945</u>
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SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**3. Premiums Receivable**

Premiums receivable at June 30, 1998 and 1997, consist of the following:

**June 30, 1998:**

<b>Due From:</b>	<b>Due to:</b>		
	<b>Insurance Reserve Fund</b>	<b>Health, Life, and Disability Insurance Reserve Fund</b>	<b>Total</b>
Local government	\$ 7,090,208	\$ 1,115	\$ 7,091,323
State government	7,065,507	200,414	7,265,921
Other	189,462	13,834	203,296
	<u>\$ 14,345,177</u>	<u>\$ 215,363</u>	<u>\$ 14,560,540</u>

**June 30, 1997:**

<b>Due From:</b>	<b>Due to:</b>		
	<b>Insurance Reserve Fund</b>	<b>Health, Life, and Disability Insurance Reserve Fund</b>	<b>Total</b>
Local government	\$ 8,732,857	\$ 9,945	\$ 8,742,802
State government	7,053,227	123,847	7,177,074
Other	76,181	67,778	143,959
	<u>\$ 15,862,265</u>	<u>\$ 201,570</u>	<u>\$ 16,063,835</u>

Premiums receivable and deferred premium revenue include approximately \$11,900,000 and \$12,800,000 attributable to premiums billed in advance of coverage as of June 30, 1998 and 1997, respectively.

**4. Due from South Carolina Retirement Division**

\$13,815,183 and \$13,039,359 (\$13,346,173 and \$12,576,576 from South Carolina Retirement System and \$469,010 and \$462,783 from Police Officers Retirement System) due from the South Carolina Retirement Systems at June 30, 1998 and 1997, respectively, represent revenues recognized on behalf of Health, Life, and Disability Insurance Reserve

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

Fund of 1.985% and 2.047% of covered compensation from all State agencies and public school systems during fiscal years 1998 and 1997 to be used for health and dental insurance benefits of State retirees. In accordance with provisions of the Appropriations Act for each year, an additional employer contribution surcharge on covered payroll was added to the contribution rate applicable to entities covered by the State Health Insurance Plan.

**5. Notes Receivable**

Amounts due from notes receivable in the Insurance Reserve Fund at June 30, 1998 and 1997, consist of the following:

	<u>1998</u>	<u>1997</u>
<b>Due from State Agencies</b>		
Sixteen and twenty-four notes respectively, due under the I.P.P. program in monthly/annual installments, including interest at 6.5%; collateralized by the assignment of notes issued by the Office of General Services for the Installment Purchase Program; range of maturity 1998 to 2006.	\$ 17,270,646	\$ 21,988,525
<b>Due from Engineering Services Section of the Office of General Services</b>		
Four and five notes, respectively, due in annual installments, including interest from 5% to 8%; range of maturity 1998 to 2005.	2,929,834	3,547,138
<b>Due from South Carolina Forestry Commission</b>		
One note due in annual installments of \$118,099, including interest at 8.75%; matures 2000; original amount \$400,000. The balance on this note was prepaid in full during 1998.	—	75,000
<b>Due from Savannah Valley Development Division of the Department of Commerce</b>		

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

One note in the principal amount of \$3,306,893 with interest at 8%; maturity date is January 31, 2021.	1,576,893	2,136,893
One note in the principal amount of \$2,500,000 with interest at 8%; maturity date is January 31, 2022.	2,500,000	2,500,000
One note in the principal amount of \$121,239 with interest at 8%; maturity date is January 31, 2022.	121,239	121,239

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**5. Notes Receivable (Continued)**

	<u>1998</u>	<u>1997</u>
<b>Due from Savannah Valley Development Division of the Department of Commerce (Continued)</b>		
One note in the principal amount of \$1,227,733 with interest at 8%; maturity date is January 31, 2023.	1,227,733	1,227,733
One note in the principal amount of \$2,690,812 with interest at 8%; maturity date is January 31, 2024.	2,690,812	2,690,812
One note in the principal amount of \$1,260,186 with interest at 8%; maturity date is January 31, 2024.	1,260,186	1,260,186
One note in the principal amount of \$1,569,410 with interest at 8%; maturity date is January 31, 2024.	1,569,410	1,569,410
One note in the principal amount of \$1,730,361 with interest at 8%; maturity date is January 31, 2027.	1,730,361	1,730,361
One note in the principal amount of \$1,139,070 with interest at 8%; maturity date is January 31, 2028.	1,139,070	—
<b>Due from the State of South Carolina</b>		
One note in the principal amount of \$2,500,000 with interest at 4.5%; maturity date is July 15, 1998.	500,000	1,000,000
Total	34,516,184	39,847,297
Less current portion	(3,679,888)	(5,462,122)
Total	<u>\$ 30,836,296</u>	<u>\$ 34,385,175</u>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**6. Fixed Assets and Contributed Capital**

The following are summaries of changes in fixed assets of the Internal Service Funds for each year.

	<b>Balance, July 1, 1997</b>	<b>Additions</b>	<b>Deletions</b>	<b>Balance June 30, 1998</b>
Furniture and Equipment	<u>\$ 2,348,293</u>	<u>\$ 115,504</u>	<u>\$ 465,988</u>	<u>\$ 1,997,809</u>

	<b>Balance, July 1, 1996</b>	<b>Additions</b>	<b>Deletions</b>	<b>Balance June 30, 1997</b>
Furniture and Equipment	<u>\$ 1,874,175</u>	<u>\$ 543,944</u>	<u>\$ 69,826</u>	<u>\$ 2,348,293</u>

A summary of fixed assets by fund at June 30, 1998 and 1997, is as follows:

<b>June 30, 1998</b>	<b>Furniture and Equipment</b>	<b>Accumulated Depreciation</b>	<b>Net Book Value</b>
Insurance Reserve Fund	\$ 865,033	\$ 440,965	\$ 424,068
Health, Life and Disability Insurance Reserve Fund	<u>1,132,776</u>	<u>544,797</u>	<u>587,979</u>
Total	<u>\$ 1,997,809</u>	<u>\$ 985,762</u>	<u>\$ 1,012,047</u>

<b>June 30, 1997</b>	<b>Furniture and Equipment</b>	<b>Accumulated Depreciation</b>	<b>Net Book Value</b>
Insurance Reserve Fund	\$ 1,084,160	\$ 460,590	\$ 623,570

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

Health, Life and Disability Insurance Reserve Fund	<u>1,264,133</u>	<u>569,918</u>	<u>694,215</u>
Total	<u>\$ 2,348,293</u>	<u>\$ 1,030,508</u>	<u>\$ 1,317,785</u>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**6. Fixed Assets and Contributed Capital (Continued)**

Depreciation expense for the years ended June 30, 1998 and 1997, was \$268,294 and \$287,731, respectively.

The following is a schedule of changes in contributed capital for the years ended June 30, 1998 and 1997.

	<b>Health, Life, and Disability Insurance Reserve Fund</b>
Balance, June 30, 1996, and June 30, 1997	\$ 6,539
Donated assets-year ended June 30, 1998	39,435
Disposal of assets-year ended June 30, 1998	—
Balance, June 30, 1998	<u>\$ 45,974</u>

**7. Lease Obligations**

The Office leases office space accounted for as an operating lease. The office space lease was amended effective May 1, 1997, and now expires June 30, 2002. Rental expense under this lease for the years ended June 30, 1998 and 1997, was \$652,493 and \$499,491. The lease payments are fixed for the remaining life of the lease which expires on June 30, 2002. The lease contains a renewal option which expires June 30, 2001.

The following schedule summarizes the Office's obligations under operating leases having remaining terms in excess of one year as of June 30, 1998:

<b><u>Fiscal Year Ending June 30,</u></b>	<b><u>Total</u></b>
1999	\$ 652,493
2000	652,493
2001	652,493
2002	652,493
Total	<u>\$ 2,609,972</u>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**7. Lease Obligations (Continued)**

The Office has also entered into a number of operating leases which expire in various years from 1997 through 2001 for office equipment which contain cancellation provisions and are subject to annual appropriation. In the normal course of business, operating leases are generally renewed or replaced by other leases. Operating leases are generally payable on a monthly basis. For the years ended June 30, 1998 and 1997, expenses under these leases were approximately \$28,000 a year.

**8. Retained Earnings-Reserved**

**Installment Purchase Program**-The Insurance Reserve Fund "Installment Purchase Program" consists of notes issued by State agencies and institutions to the Division of General Services to finance the purchase of office, telecommunications, medical, and data processing equipment. The program is authorized under South Carolina State Code 1-1-1020. The program is funded through loans from the Insurance Reserve Fund to the Office of General Services. Effective July 1, 1994, this program is administered by the State Treasurer's Office. At June 30, 1998 and 1997, \$35,000,000 of the retained earnings of the Insurance Reserve Fund was reserved for support of the program. The total balance outstanding at June 30, 1998 and 1997, was \$17,270,646 and \$21,988,525, respectively.

**Savannah Valley Development Program**-At June 30, 1998 and 1997, \$20,000,000 of the Insurance Reserve Fund retained earnings has been reserved for loans to the Savannah Valley Development Division of the Department of Commerce, as authorized under South Carolina State Code 13-9-10, formerly the Clark's Hill-Russell Authority (a Joint Resolution; R-22, H2516; of the State, approved March 12, 1987, and R-755, H2680; of the State, approved June 20, 1988). As of June 30, 1998 and 1997, \$13,815,705 and \$13,236,634, respectively, was outstanding.

**9. Pension Plans**

The majority of employees of the Office are covered by a retirement plan through the South Carolina Retirement System (SCRS), a cost-sharing multiple-employer defined benefit pension plan administered by the Retirement Division of the State Budget and Control Board, 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



SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

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.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**9. Pension Plans (Continued)**

The Retirement Division 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 South Carolina Retirement Division, Post Office Box 11960, Columbia, South Carolina 29211-1960. Furthermore, the Division and the four pension plans are included in the CAFR of the State of South Carolina.

Under the SCRS, employees are eligible for a full service retirement annuity upon reaching age 65 or completion of 30 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. 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.

Since July 1, 1988, employees participating in the SCRS have been required to contribute 6 percent of all compensation. For the years ended June 30, 1998, 1997 and 1996 the employer contribution rate was 7.55 percent (before a surcharge to fund retiree health and dental insurance coverage). The Office's actual contributions to the SCRS for those years were approximately \$398,000, \$307,000 and \$287,000, respectively, and equaled the required contributions of 7.55 percent (excluding the surcharge) for each year. Also, the Office paid employer group-life insurance contributions at the rate of .15 percent of compensation for the years ended June 30, 1998, 1997, and 1996.

The amounts paid by the Office for pension and group-life benefits are reported as employer contribution expenditures within the applicable administrative expenditure categories to which the related salaries are charged.

Article X, Section 16 of the South Carolina Constitution requires that all State-operated retirement systems be funded on a sound actuarial basis. Title 9 of the South Carolina Code of Laws of 1976, as amended, prescribes requirements relating to membership, benefit and employee/employer contributions for each retirement system. Employee and

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

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).

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**9. Pension Plans (Continued)**

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

**10. Post-Employment and Other Employee Benefits**

In accordance with the South Carolina Code of Laws and the annual Appropriation Act, the State of South Carolina provides certain health care, dental, and life insurance benefits to certain active and retired State employees and certain surviving dependents of retirees. All permanent full-time and certain permanent part-time employees of the Office are eligible to receive these benefits. The State provides post employment health and dental benefits to employees who retire from State service or who terminated with at least 20 years of State service who meet one or more of the eligibility requirements, such as age, length of service, and hire date. Generally those who retire must have at least 10 years of retirement service credit to qualify for State-funded benefits. Benefits are effective at date of retirement when the employee is eligible for retirement benefits.

These benefits are provided through annual appropriations by the General Assembly to the Office for its active employees and to the State Budget and Control Board for all participating State retirees except the portion funded through the pension surcharge and provided from other applicable sources of the Office for its active employees who are not funded by State General Fund appropriations. The State finances health and dental plan benefits on a pay-as-you-go basis.

The Office recorded employer contributions expenditures within the applicable administrative expenditure categories for these insurance benefits for active employees of approximately \$267,000 and \$264,000 for the years ended June 30, 1998 and 1997, respectively. As discussed in *Note 9*, the Office paid approximately \$81,200 and \$81,000 for the years ended June 30, 1998 and 1997, respectively, applicable to the surcharge

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

included with the employer contributions for retirement benefits (1.916% for 1998 and 1.985% for 1997).

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**10. Post-Employment and Other Employee Benefits (Continued)**

Information regarding the cost of insurance benefits applicable to Office retirees is not available. By State law, the Office has no liability for retirement benefits. Accordingly, the cost of providing these benefits for retirees is not included in the accompanying financial statements.

In addition, the State General Assembly periodically directs the Retirement Systems to pay supplemental (cost of living) increases to retirees. Such increases are primarily funded from Systems' earnings; however, a portion of the required amount is appropriated from the State General Fund annually for the SCRS benefits.

**11. Deferred Compensation Plans**

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of the Office have elected to participate. The multiple-employer plans, created under Internal Revenue Code Sections 457, 401 (k), and 403 (b), are accounted for as agency funds of the State and included in the Comprehensive Annual Financial Report of the State of South Carolina. Employees may withdraw the current value of their contributions when they terminate State employment. Employees may also withdraw contributions prior to termination if they meet requirements specified by the applicable plan.

Compensation deferred under the Section 401 (k) and 403 (b) plans is placed in trust for the contributing employee. The State has no liability for losses under the plans. Under the Section 457 plan, all deferred compensation plan amounts and earnings remain assets of the employer (the State) subject to the claims of the employer's general creditors, one of whom is the employee participant. It is unlikely, however, that the State would ever use plan assets to satisfy claims of the State's general creditors. The portion of assets of the Section 457 plan to which the State has access is disclosed in its annual financial report.

**12. Related Party Transactions**

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

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

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

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**12. Related Party Transactions (Continued)**

The following services are provided for a fee to various State agencies and within the South Carolina State Budget and Control Board. The fees are recorded as revenues in the financial statements for the Insurance Reserve Fund and the Health, Life, and Disability Insurance Reserve Fund. Total amounts of premiums received from other state agencies is not readily available.

Health, Life, and Disability Insurance Fund:

Health, dental, basic group-life and disability, and State Life and Long-Term Disability insurance coverage for state agencies and local governments

Insurance Reserve Fund:

Property coverage for state and local governments

A significant portion of the Office's total insurance premium revenue is for insurance premiums charged to other state agencies and divisions of the South Carolina State Budget and Control Board. Premiums owed from these entities were \$7,265,921 and \$7,177,074 at June 30, 1998 and 1997, respectively.

The following details the insurance premiums charged by the Office to other state agencies and divisions of the South Carolina State Budget and Control Board during the year ended June 30, 1998:

Tort liability	\$ 13,613,683
Auto liability	5,196,295
Professional liability	5,322,410
Comprehensive and collision	217,280
School bus liability	3,082,961
Fire	2,844,808
Extended coverage	1,430,602
Inland Marine	799,232
Active employees:	
Health	190,615,387
Dental	16,152,150
Life	1,481,829
LTD	4,370,246
Dependent/optional life	8,711,042
Retirees:	



SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

Health	13,328,247
Dental	974,343
Retiree surcharge	35,296,879
Other premium revenues	1,555,949
	<hr/> <u>\$ 304,993,343</u>

**12. Related Party Transactions (Continued)**

The Office had financial transactions with various State agencies during the fiscal year. Significant payments were made to Divisions (Offices) of the State Budget and Control Board for retirement and insurance plans contributions, vehicle rental, surplus property disposal fees, office supplies, printing, and telephone, interagency mail, data processing services, purchasing, record maintenance, internal audit and personnel services. Significant payments were also made for unemployment and workers' compensation coverage for employees to other agencies. The amounts of 1998 and 1997 expenditures applicable to related party transactions are not readily available.

The following services are received from other Divisions (Offices) of the South Carolina State Budget and Control Board at no charge:

- Division of Operations
  - Record storage
- Retirement Division
  - Collection of health and dental premiums from retirees
  - Retirement plan administration
  - Collection of retiree insurance surcharge from employers

During the year ended June 30, 1998 and 1997, the State Life and Long-Term Disability program paid \$1,717,616 and \$590,822, respectively to the South Carolina Retirement Division for administrative expenses.

Additionally, refer to *Note 4* for a description of the amounts due from South Carolina Retirement Division.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**13. Residual Equity Transfer**

Effective July 1, 1996, the South Carolina Retirement Division transferred the State life and Long-Term Disability program to the Office. The net assets of the program (which was accounted for as an internal service fund at the South Carolina Retirement Division) amounted to \$6,580,480 as of the date of the transfer. For financial reporting purposes, this transaction has been accounted for as a residual equity transfer into the Health, Life, and Disability Insurance reserve Fund on the Books of the Office.

The assets, liabilities and fund equity of the State Life and Long-Term Disability program at the date of the transfer were as follows (amounts in thousands):

Assets:

Cash and cash equivalents	\$ 8,953
Accrued interest receivable	267
Investments (at amortized cost)	<u>15,907</u>
	<u><u>\$ 25,127</u></u>

Liabilities and Fund Equity:

Accounts payable and accrued expenses	\$ 6
Incurred but unpaid claims	<u>18,541</u>
	<u>18,547</u>

Fund Equity:

Retained earnings	<u>6,580</u>
Total liabilities and fund equity	<u><u>\$ 25,127</u></u>

During 1996 (prior to the transfer from the South Carolina Retirement Division to the Office), the State Life and Long-Term Disability program reported the following revenues, expenses and transfers (amounts in thousands):

Operating revenues	\$ 8,472
Operating expenses	<u>(6,816)</u>
Operating income	1,656
Operating transfers out for administrative expenses	(534)

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

Net income

---

\$ 1,122

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SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**13. Residual Equity Transfer (Continued)**

Additionally, the following changes in the liabilities for claims were reported (amounts in thousands):

Balance, July 1, 1995	\$ 16,669
Current year claims and changes in estimates	6,816
Claims payments	<u>(4,944)</u>
Balance, June 30, 1996	<u><u>\$ 18,541</u></u>

**14. Contingencies**

By the nature of its operations and responsibilities as an insurer, the Office has been named in a number of lawsuits, many of which are pending. A provision has been made in the financial statements for the payment of routine claims. Management is not aware of any other claims that, in their opinion, would have a material effect on the financial statements and, therefore, no liability has been recorded.

**15. Risk Management/Reinsurance**

The Office is exposed to various risks of loss and maintains State or commercial insurance coverage for each of those risks except for business interruption insurance. Management believes such coverage is sufficient to preclude any significant uninsured losses for the covered risks. There were no significant reductions in insurance coverage from coverage in the prior year. Settled claims have not exceeded this coverage in any of the past three years.

The Office pays insurance premiums to itself, certain other State agencies and commercial insurers to cover risks that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered economic losses sustained during the policy period in accord with insurance policy and benefit program limits.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**15. Risk Management/Reinsurance (Continued)**

State management believes it is more economical to manage certain risks internally and set aside assets for claim settlement. Several State funds accumulate assets and the State itself assumes substantially all risks for the following:

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

Employees elect health coverage through either a health maintenance organization or through the State's self-insured plan. All of the other coverages listed above are through the applicable State self-insured plan except dependent and optional life premiums are remitted to commercial carriers.

The Office and other entities pay premiums to the Insurance Reserve Fund which issues policies, accumulates assets to cover the risks of loss, and pays claims incurred for covered losses related to the following Office assets, activities, and/or events:

1. Theft of, damage to, or destruction of assets;
2. Auto liability for non-state owned vehicles; and
3. General torts.

State agencies and other entities are the primary participants in the HLDIRF and in IRF.

The Office obtains coverage of up to \$750,000 per loss through a commercial carrier for employee fidelity bond insurance for all employees for losses arising from theft or misappropriation.

The Office has recorded insurance premium expense regarding its internal operations in the applicable administrative expense categories.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**15. Risk Management/Reinsurance (Continued)**

The Office has not transferred the portion of the risk of loss related to insurance policy deductibles and limits. The Office has not reported an estimated claims loss expense, and the related liability at June 30, 1998 or 1997, based on the requirements of GASB 10 because information at June 30 did not indicate that an asset had been impaired or a liability had been incurred. GASB 10 states that a liability for claims must be reported only if information prior to issuance of the financial statements indicates that it is probable that an asset has been impaired or a liability has been incurred on or before June 30 and the amount of loss is reasonably estimable.

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. It 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

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**16. Restatement**

As discussed in *Note 1*, the office implemented a change in accounting principle. As prescribed in GASB #31, implementation is retroactively applied by restatement of prior year retained earnings to recognize unrealized gains or losses on investments.

	<b>As Previously Reported</b>	<b>Restatement</b>	<b>As restated</b>
	<hr/>	<hr/>	<hr/>
<u>Balance Sheet:</u>			
Investments	\$210,327,516	\$ 8,319,428	\$218,646,944
Unreserved retained earnings	162,664,997	8,319,428	170,984,425
 <u>Statement of Revenues, Expenses, and Changes in Retained Earnings:</u>			
Income from deposits and investments	30,839,848	8,319,428	39,159,276
Net loss	(16,482,127)	8,319,428	(8,162,699)
 <u>Statement of Cash Flows:</u>			
Operating loss	(16,416,931)	8,319,428	(8,097,503)
Reclassify investment income	(33,375,160)	(8,319,428)	(41,694,588)

**17. Net Loss**

During 1998, the Health, Life, and Disability Insurance Reserve Fund reported a net loss of \$34,161,014.

The net loss for the year ended June 30, 1998, is attributable to the State Health Plan maintaining constant contribution levels and spending down retained earnings to pay claims. Section 1-11-710 of the S.C. Code of Laws requires the Plan to have a cash reserve balance equivalent to no less than 1 1/2 months of claims payments. In recent years, the cash balance exceeded this benchmark by a substantial amount. By allowing the HLDIRF retained earnings to fall to near the statutory requirement, the State Health Plan has been

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

able to keep employee and employer contributions constant over the past seven and five years, respectively.

Because of a continuing increase in health claims costs and depletion of reserves, the State Health Plan instituted an 18% employer rate increase effective January 1999. This increase will allow the State Health Plan to maintain its current level of benefits, keep employee contributions constant for another year, and maintain reserves at statutory levels.



SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

**18. 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 funds.

	<b>Insurance Reserve Fund</b>		<b>Health, Life, and Disability Insurance Reserve Fund</b>	
	<b>1998</b>	<b>1997</b>	<b>1998</b>	<b>1997</b>
	<b>(In thousands)</b>		<b>(In thousands)</b>	
Unpaid claims and claim adjustment expenses at beginning of the fiscal year	\$ 157,306	\$ 153,040	\$ 97,560	\$ 69,896
Incurred claims and claim adjustment expenses:				
Provision for insured events of the current fiscal year	39,855	12,742	451,263	505,931
Increases (decreases) in provision for insured events of prior fiscal years	(15,885)	38,628	102,303	7,276
Total incurred claims and claim adjustment expenses	23,970	51,370	553,566	513,207
Payments:				
Claims and claim adjustment expenses attributable to insured events of the current fiscal year	10,182	9,075	400,259	459,947
Claims and claim adjustment expenses attributable to insured events of prior fiscal years	24,316	38,029	149,223	44,137
Total payments	34,498	47,104	549,482	504,084
Other changes:				
Transfer of State Life and LTD program from Retirement Division	—	—	—	18,541
Total unpaid claims and claim adjustment expenses at end of the fiscal year	\$ 146,778	\$ 157,306	\$ 101,644	\$ 97,560

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

— CONTINUED —

The above totals are comprised of the following:

Claims payable	\$ 93,544	\$ 94,810	\$ 25,255	\$ 30,880
Claims incurred but not reported	<u>53,234</u>	<u>62,496</u>	<u>76,389</u>	<u>66,680</u>
Total	<u>\$ 146,778</u>	<u>\$ 157,306</u>	<u>\$ 101,644</u>	<u>\$ 97,560</u>

**19. Year 2000**

The office has begun to identify and update its systems for year 2000 (Y2K) compliance. As of June 30, 1998, the office has made substantial changes and upgrades to its systems, however, the office is not yet fully Y2K compliant. No significant commitments exist for planned changes and upgrades at June 30, 1998.

**20. Reclassifications**

Certain amounts from 1997 have been reclassified to conform to the 1998 presentation. Specifically, certain revenue and expense line items on the Combined Statement of Revenue, expenses, and Changes in Retained Earnings have been updated to the 1998 presentations requiring further detail on the 1997 amounts.

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED STATEMENTS OF CASH FLOWS

YEARS ENDED JUNE 30, 1998 AND 1997

OTHER FINANCIAL INFORMATION

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINING BALANCE SHEET - ALL INTERNAL SERVICE FUNDS

JUNE 30, 1998  
(With comparative totals for June 30, 1997)

	1998			1997
	Insurance Reserve Fund	Health, Life, and Disability Insurance Reserve Fund	Totals	Restated Totals
<b>Assets</b>				
Current assets:				
Cash and cash equivalents	\$ 89,051,174	\$ 147,810,274	\$ 236,861,448	\$ 215,517,128
Premiums receivable	14,345,177	215,363	14,560,540	16,063,835
Reinsurance recovery receivable	1,670,771	—	1,670,771	1,272,083
Current portion of notes receivable	3,679,888	—	3,679,888	5,462,122
Due from South Carolina Retirement Division	—	13,815,183	13,815,183	13,039,359
Preventative Drug Rebate Receivable	—	398,446	398,446	1,015,242
Accrued interest	3,728,578	1,951,477	5,680,055	6,862,424
Prepaid insurance	2,210,550	—	2,210,550	2,450,700
Other assets	183,776	1,893	185,669	420,409
Total current assets	<u>114,869,914</u>	<u>164,192,636</u>	<u>279,062,550</u>	<u>262,103,302</u>
Non-current assets:				
Investments	176,141,748	22,861,573	199,003,321	218,646,944
Long-term notes receivable	30,836,296	—	30,836,296	34,385,175
Furniture and equipment, net of accumulated depreciation	424,068	587,979	1,012,047	1,317,785
Total non-current assets	<u>207,402,112</u>	<u>23,449,552</u>	<u>230,851,664</u>	<u>254,349,904</u>
Total assets	<u>\$ 322,272,026</u>	<u>\$ 187,642,188</u>	<u>\$ 509,914,214</u>	<u>\$ 516,453,206</u>
<b>Liabilities and Fund Equity</b>				
Current liabilities:				
Accounts payable	\$ 233,335	\$ —	\$ 233,335	\$ 548,555
Accrued payroll	177,460	316,204	493,664	404,821
Claims payable	93,544,181	25,254,603	118,798,784	125,689,758
Deferred premium revenue	38,494,338	2,185,090	40,679,428	34,120,069
Claims incurred but not reported	53,233,449	76,389,809	129,623,258	129,176,314
Accrued compensated absences	248,088	251,078	499,166	522,725
Total current liabilities	<u>185,930,851</u>	<u>104,396,784</u>	<u>290,327,635</u>	<u>290,462,242</u>
Fund equity:				
Contributed capital	—	45,974	45,974	6,539
Retained earnings:				
Reserved for:				
Installment purchase program				
Savannah Valley Development	35,000,000	—	35,000,000	35,000,000
Loans	20,000,000	—	20,000,000	20,000,000
Unreserved	81,341,175	83,199,430	164,540,605	170,984,425
Total fund equity	<u>136,341,175</u>	<u>83,245,404</u>	<u>219,586,579</u>	<u>225,990,964</u>
Total liabilities and fund equity	<u>\$ 322,272,026</u>	<u>\$ 187,642,188</u>	<u>\$ 509,914,214</u>	<u>\$ 516,453,206</u>

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINING STATEMENT OF REVENUES, EXPENSES,  
AND CHANGES IN RETAINED EARNINGS - ALL INTERNAL SERVICE FUNDS

YEAR ENDED JUNE 30, 1998  
(With comparative totals for the year ended June 30, 1997)

	1998			1997
	Insurance Reserve Fund	Health , Life, and Disability Insurance Reserve Fund	Totals	Restated Totals
<b>Operating Revenues</b>				
Insurance premiums:				
Tort liability	\$ 23,305,157	\$ —	\$ 23,305,157	\$ 19,737,418
Auto liability	15,068,783	—	15,068,783	13,783,021
Professional liability	6,434,220	—	6,434,220	7,099,310
Comprehensive and collision	2,125,930	—	2,125,930	2,038,344
School bus liability	3,523,205	—	3,523,205	3,527,141
Fire	7,174,898	—	7,174,898	7,330,789
Extended coverage	3,608,125	—	3,608,125	3,702,452
Inland Marine	2,555,601	—	2,555,601	2,394,696
Active employees:				
Health	—	435,871,959	435,871,959	419,358,006
Dental	—	36,991,502	36,991,502	33,973,039
Life	—	3,022,466	3,022,466	1,327,661
Long term disability	—	9,935,026	9,935,026	9,112,323
Dependent/optional life	—	17,263,346	17,263,346	15,474,574
Retirees:				
Health	—	28,660,684	28,660,684	27,540,528
Dental	—	2,061,828	2,061,828	1,867,163
Retiree surcharge	—	86,311,816	86,311,816	84,664,255
Other premium revenues	2,701,432	587,640	3,289,072	3,275,851
Prescription drug rebates	—	3,648,135	3,648,135	4,032,117
Income from deposits and investments	20,332,753	14,786,444	35,119,197	39,159,276
Notes receivable interest	2,556,722	—	2,556,722	2,535,312
Other	1,032	273,525	274,557	70,870
Total operating revenues	89,387,858	639,414,371	728,802,229	702,004,146
<b>Operating Expenses</b>				
Reinsurance premiums	23,584,010	—	23,584,010	27,553,445
Premiums	1,341,267	94,931,444	96,272,711	90,425,550
Claims:				
Tort liability	6,439,420	—	6,439,420	15,259,763
School bus liability	4,707,494	—	4,707,494	3,663,618
Fire	2,729,166	—	2,729,166	3,129,257
Extended coverage	2,010,253	—	2,010,253	4,793,224
Health	—	505,167,625	505,167,625	461,283,045
Dental	—	40,119,284	40,119,284	39,735,265
Life	—	1,228,007	1,228,007	845,851
Long term disability	—	7,050,511	7,050,511	11,342,365
Hospitals and physicians	5,338,828	—	5,338,828	7,118,073
Auto and Inland Marine	2,643,351	—	2,643,351	2,665,603
Other	102,603	—	102,603	156,699
Professional and administrative fees	8,021,542	18,759,783	26,781,325	31,583,972
Administrative and planning	386,612	386,612	773,224	1,436,542
Insurance Benefits Administration	—	5,868,436	5,868,436	4,895,994
Insurance Reserve Administration	4,327,577	—	4,327,577	4,213,383
Total operating expenses	61,632,123	673,511,702	735,143,825	710,101,649
Operating income (loss)	27,755,735	(34,097,331)	(6,341,596)	(8,097,503)
Loss on disposal of assets	(38,541)	(63,683)	(102,224)	(65,196)
Net income (loss)	27,717,194	(34,161,014)	(6,443,820)	(8,162,699)
Retained earnings, beginning of year	108,623,981	117,360,444	225,984,425	227,566,644
Residual equity transfer from South Carolina Retirement Division	—	—	—	6,580,480
Retained earnings at end of year	\$ 136,341,175	\$ 83,199,430	\$ 219,540,605	\$ 225,984,425

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINING STATEMENT OF CASH FLOWS

YEAR ENDED JUNE 30, 1998

(With comparative totals for the year ended June 30, 1997)

	1998			1997
	Insurance Reserve Fund	Health, Life, and Disability Insurance Reserve Fund	Totals	Restated Totals
<b>Cash Flows from Operating Activities</b>				
Operating income (loss)	\$ 27,755,735	\$ (34,097,331)	\$ (6,341,596)	\$ (8,097,503)
Reclassify investment and note interest income included in operating income (loss) to investing activity	(22,889,475)	(14,786,444)	(37,675,919)	(41,694,588)
Transfer of cash and cash equivalents from South Carolina Retirement Division	—	—	—	8,953,076
Adjustments to reconcile operating income (loss) to net cash used in operating activities:				
Depreciation expense	147,329	120,965	268,294	287,371
Change in operating assets-(increase) decrease:				
Premiums receivable	1,517,088	(13,793)	1,503,295	1,155,948
Reinsurance recovery receivable	(398,688)	—	(398,688)	(135,513)
Due from South Carolina Retirement Division	—	(775,824)	(775,824)	838,754
Prepaid insurance, preventative drug rebate receivable and other assets	474,891	616,796	1,091,687	(1,124,310)
Change in operating liabilities-increase (decrease):				
Accounts payable, accrued payroll and compensated absences	11,230	(261,167)	(249,937)	(1,622,129)
Deferred premium revenue	4,992,469	1,566,890	6,559,359	1,525,177
Claims payable and incurred but not reported	(10,211,120)	4,084,238	(6,126,882)	13,388,743
Total adjustments	(3,466,801)	5,338,105	1,871,304	14,314,041
Net cash used in operating activities	1,399,459	(43,545,670)	(42,146,211)	(26,524,974)
<b>Cash Flows from Capital and Related Financing Activities</b>				
Purchase of fixed assets	(28,430)	(47,637)	(76,067)	(543,944)
Net cash used in capital and related financing activities	(28,430)	(47,637)	(76,067)	(543,944)
<b>Cash Flows from Investing Activities:</b>				
Principal payments received on notes receivable	6,470,183	—	6,470,183	5,786,062
Funds disbursed as notes receivable	(1,139,070)	—	(1,139,070)	(5,833,771)
Purchase of investments	(51,642,220)	(601,650)	(52,243,870)	(89,278,748)
Proceeds from sales and maturity of investments	75,119,260	314,951	75,434,211	53,869,760
Interest received-deposits and investments	17,915,497	14,288,663	32,204,160	31,818,117
Premiums amortized and discounts accreted	275,085	9,177	284,262	—
Interest received-notes receivable	2,556,722	—	2,556,722	2,743,709
Net cash provided by (used in) investing activities	49,555,457	14,011,141	63,566,598	(894,871)
Net increase (decrease) in cash and cash equivalents	50,926,486	(29,582,166)	21,344,320	(27,963,789)
Cash and cash equivalents, beginning of year	38,124,688	177,392,440	215,517,128	243,480,917
Cash and cash equivalents, end of year	<u>\$ 89,051,174</u>	<u>\$147,810,274</u>	<u>\$236,861,448</u>	<u>\$215,517,128</u>
<b>Supplemental Information</b>				
Noncash capital and related financing activities:				
Receipt of contributed capital assets	\$ —	\$ —	\$ 39,435	\$ —
Disposal of other fixed assets	(42,062)	(8,659)	(50,721)	(69,826)
Noncash investing activities:				
Receipt of investments (through residual equity transfer)	—	—	—	15,907,305
Receipt of accrued interest receivable (through residual equity transfer)	—	—	—	267,119
Noncash operating activities:				
Assumption of accounts payable and accrued expenses (through residual equity transfer)	—	—	—	5,844

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD  
OFFICE OF INSURANCE SERVICES

COMBINED STATEMENT OF CASH FLOWS - PROPRIETARY FUND TYPE

- CONTINUED -

Assumption of incurred but unpaid claims (through residual equity transfer)	—	—	—	18,541,176
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