

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)

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.

Cash and Cash Equivalents

For purposes of the statements of cash flows, the Office considers all highly liquid securities with a maturity of three months or less at the time of purchase to be cash equivalents. Because the State's internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The State Treasurer administers the cash management pool. 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 internal cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of funds.

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

Cash and Cash Equivalents (Continued)

Most State agencies including the Office participate in the State's internal cash management pool. Because the cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The State Treasurer administers the cash management pool. 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. For credit risk information pertaining to the internal cash management pool, see the deposits disclosures in *Note 4*.

The State's internal 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. Deposits in the general deposit account are recorded and reported at cost. However, the Office reports its deposits in the special deposit accounts at fair value. Investments in the pool are recorded and reported at fair value. Interest earned by the agency's special deposit accounts is posted to the agency's account at the end of each month and is retained by the agency. Interest earnings are allocated based on the percentage of an agency's accumulated daily interest receivable to the total income receivable of the pool. Reported interest income includes interest earnings, realized gains/losses, and unrealized gains/losses on investments in the pool arising from changes in fair value. Realized gains and losses are allocated daily and are included in the accumulated income receivable. Unrealized gains and losses are allocated at year-end based on the Office's percentage ownership in the pool.

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

Investments

Investments, in accordance with Governmental Accounting Standards Board (GASB) Statement Number 31, "Accounting and Financial Reporting for Certain Investments and for External Investment Pools", are reported at fair value. Securities traded on a national exchange are valued at the last reported sales price.

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

Investments (Continued)

Investment income consists of interest earned during the year, amortization of premiums and accretion of discounts, realized gains/losses on securities, and unrealized gains and losses resulting from changes in fair value. Earnings are posted to the agency's account at the end of each month. 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.

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

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.

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

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.

Depreciation expense (for both purchased and contributed assets) is recorded in the applicable fund's administration account. The capitalization dollar threshold limit for fixed assets is \$1,000.

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 \$4,200,000 and \$6,100,000 as of June 30, 2001 and 2000, 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 5.75% and 5.50% for 2001 and 2000, compounded annually.

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

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.

Compensated Absences

Generally all permanent full-time State employees and certain part-time employees scheduled to work at least one-half of the agency's workweek are entitled to accrue and carry forward at calendar year-end maximums of 180 days sick leave and of 45 days annual vacation leave. Upon termination of State employment, employees are entitled to be paid for accumulated unused annual vacation leave up to the maximum, 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, 2001. 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 fund's administration account.

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

Fund Equity

Contributed capital is recorded in proprietary funds that have received contributions of property or other assets from other funds and other agencies. Reservations of retained earnings are limited to outside third-party restrictions. Retained earnings are recorded in proprietary funds to reflect the net accumulated earnings of the fund. Reservations of fund balances of governmental funds are created to either (1) satisfy legal covenants that require that a portion of the balance be segregated for a specific future use or (2) identify the portion of the fund balance that is not appropriable for future discretionary expenditures. The unreserved component of fund equity is computed as total fund equity less reserved amounts.

Budget Policy

The General Assembly enacts a budget for the Office within the Division of Operations budgetary unit of the State Budget and Control. The Appropriation Act authorizes expenditures from funds appropriated from the General Fund of the State and authorizes expenditures of total funds. The Total Funds column includes all budgeted resources, including the State General Fund as well as most federal fund and department-generated sources. A revenue budget is not adopted for individual budgetary units.

The accompanying financial statements include a Combined Statement of Expenditures-Budget and Actual-All Budgeted Funds. The Budgetary General Fund category on that statement corresponds to the General Funds column in the Appropriation Act and Other Budgeted Funds category represents the difference between Total Funds and General Funds columns in the Appropriations Act.

The current Appropriations Act states that the General Assembly intends to appropriate all monies to operate state government for the current fiscal year. Any unexpended state General Fund appropriations lapse to the General Fund of the State on July 31 unless specific authorization is given to carryover the funds to the ensuing fiscal year. Appropriations carried forward for a specific purpose are reported as reserved fund balance. Proviso 63B.10 of the 2001/2002 Appropriations Act authorizes the South Carolina Seniors' Prescription Drug Program to carry forward unspent State General Fund appropriations.

During the fiscal year close-out period through July, departments and agencies may continue to charge vendor, interagency, and interfund payments applicable to the current year to this fiscal year's appropriation.

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