

SOUTH CAROLINA STATE BUDGET AND CONTROL BOARD
OFFICE OF INSURANCE SERVICES

NOTES TO COMBINED FINANCIAL STATEMENTS

JUNE 30, 2001 AND 2000

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.

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

Reporting Entity (Continued)

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.

The South Carolina State Budget and Control Board, Office of Insurance Services, Insurance Reserve Fund; Health, Life, and Disability Insurance Reserve Fund and Seniors' Prescription Drug Program 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). All of the divisions of the Board reporting entity are under the control of the Executive Director of the State Budget and Control 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.

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NOTES TO COMBINED FINANCIAL STATEMENTS

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

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 financial statements of the Special Revenue Fund include the Balance Sheet; Statement of Revenue, Expenditures, and Changes in Fund Balances; and Statement of Expenditures -Budget and Actual-All Budgeted Funds.

The Internal Service Funds presented include:

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

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 (A)(4) (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.

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

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.

The Special Revenue Fund presented include:

- The South Carolina Seniors' Prescription Drug Program
(also known as Silver Card/Silver Card Plus Program)

The South Carolina Seniors' Prescription Drug Program is authorized in Section 44-130-30 and 44-130-40 of the South Carolina Code of Laws of 1976, as amended.

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.

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 both Governmental and Proprietary Fund types.

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(CONTINUED)

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

Description of Funds

Government Funds-Governmental funds use the current financial resources measurement focus. Only current assets and current liabilities are generally included on their balance sheets. Their operating statements present sources and uses of available resources during a given period. The following fund is reported as a governmental fund:

South Carolina Seniors' Prescription Drug Program (Special Revenue Fund)-Beginning January 1, 2001, the South Carolina Seniors' Prescription Drug Program (the "Program") was created by the South Carolina Seniors' Prescription Drug Program Act passed by the General Assembly.

This program is administered by the State Budget and Control Board through its Office of Insurance Services. The purpose of the program is to provide financial assistance for purchasing prescription drugs to senior citizens who are ineligible for or do not have insurance coverage or other assistance through federal, state, or private programs for these purchases. To be eligible to participate in this program a person must:

- (1) be a South Carolina resident who has attained the age of sixty-five years;
- (2) have resided in South Carolina at least six consecutive months before participation in the program;
- (3) be ineligible for Medicaid prescription benefits;
- (4) not have any pharmacy benefits or coverage from any governmental or private insurance program providing such benefits;
- (5) have an annual income that does not exceed one hundred fifty percent of the federal poverty level. Priority must be given to applicants without Medicare supplements or other third party benefits or coverage during the six months before application.

The program is funded from proceeds received by the State in the settlement agreement and related documents, between the State and leading United States tobacco manufacturers dated November 23, 1998.

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

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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:

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

- (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 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.

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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. In addition, effective January 1, 1999, the Office began offering a managed care pilot program limited to Medical University of South Carolina's (MUSC) employees living in Charleston, Dorchester or Berkeley counties. The "MUSC managed care program" is a self-insured HMO point of service plan. Premiums are paid through payroll deductions. 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 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 6*) 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, basic life and basic long-term disability coverages.

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

Basis of Accounting

The modified accrual basis of accounting is used by all governmental fund types. Under the modified accrual basis of accounting, revenues are recognized when susceptible to accrual (i.e., when they become both measurable and available). “Measurable” means the amount of the transaction can be determined and “available” means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current period. Expenditures are recorded when the related fund liability is incurred.

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.