

SOUTH CAROLINA STATE ACCIDENT FUND

COLUMBIA, SOUTH CAROLINA

FINANCIAL STATEMENTS

YEAR ENDED JUNE 30, 2013

State of South Carolina



Office of the State Auditor

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November 5, 2013

The Honorable Nikki R. Haley, Governor
and
Mr. Harry B. Gregory, Jr., Director
South Carolina State Accident Fund
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina State Accident Fund for the fiscal year ended June 30, 2013 was issued by Rogers Laban, PA, Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

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

Respectfully submitted,

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

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

RHGjr/trb

SOUTH CAROLINA STATE ACCIDENT FUND

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INDEPENDENT AUDITOR'S REPORT

Mr. Richard H. Gilbert, Jr., CPA
Deputy State Auditor
State of South Carolina
Columbia, South Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of the South Carolina State Accident Fund ("the Fund") as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of significant estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the Fund as of June 30, 2013, and the respective changes in financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Reporting Entity

As described in Note 1, the Financial Statements of the State Accident Fund reporting entity are intended to present the financial position and results of operations of only that portion of the financial reporting entity of the State of South Carolina that is attributable to the transactions that comprise the South Carolina State Accident Fund reporting entity. They do not purport to and do not present the financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America, and do not include any other agencies, divisions, or component units of the State of South Carolina.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Reporting Required by Government Auditing Standards

In accordance with Government Auditing Standards, we have also issued our report dated October 7, 2013, on our consideration of the Fund's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the Fund's internal control over financial reporting and compliance.

Rogers Lalan, PA

October 7, 2013

STATE ACCIDENT FUND

MANAGEMENT'S DISCUSSION AND ANALYSIS

The South Carolina State Accident Fund ("Fund") presents a management's discussion and analysis of its financial statements for fiscal year 2013. The discussion includes an overview of the financial activity for the year. This report is prepared in accordance with Governmental Accounting Standards Board Statement 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*. This discussion should be read in conjunction with the Fund's financial statements and accompanying notes.

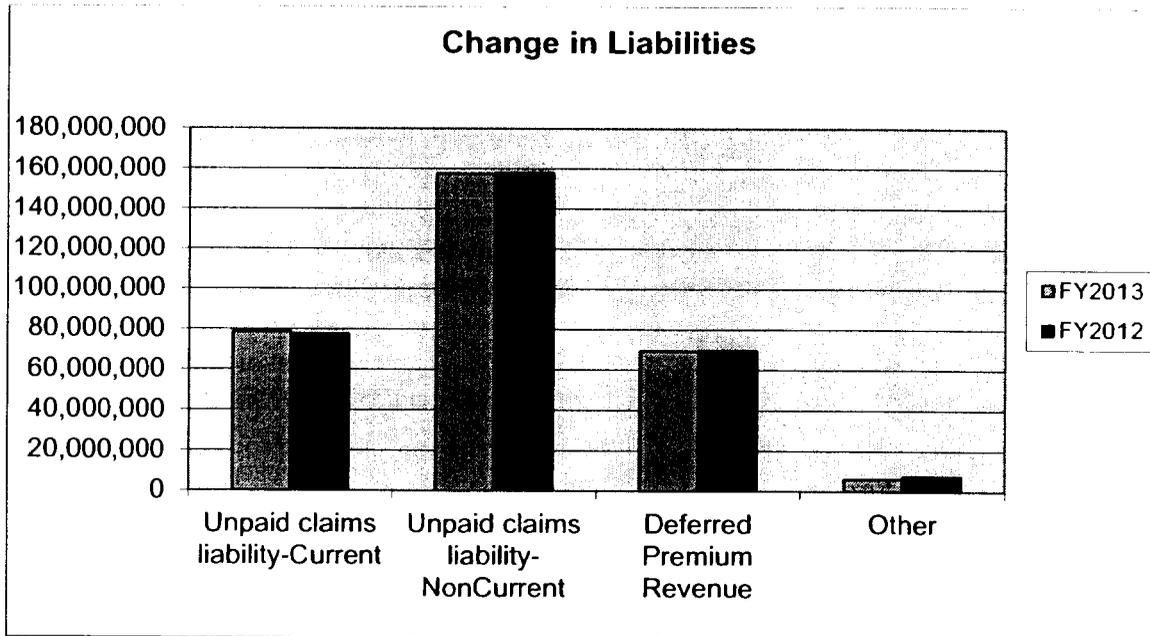
Overview of the Financial Statements and Financial Analysis

The Statement of Net Position presents information reflecting the Fund's assets, liabilities, and net position. This statement provides the reader with a snapshot view at a point in time. Net position represents the amount of total assets less liabilities. Assets and liabilities are shown as current and noncurrent. Current assets and liabilities are those with immediate liquidity or which are collectible or due within twelve months of the statement date. The Statement of Net Position indicates the funds available for the Fund's operation along with the liabilities that will come due during the next fiscal year. Total assets increased by \$9 million over the prior fiscal year.

Unpaid claims liabilities are a large part of the Fund's liabilities and have been separated into current (to be paid within one year) and noncurrent (to be paid after one year). Current estimated unpaid claim liabilities increased slightly and non-current decreased compared to the prior year. The change in the current and noncurrent was due to the actuarial assessment of reserves. (See Change in Liabilities chart below.) The current liabilities decreased by \$820 thousand as a result of the decrease in deferred premium revenue and accrued refundable premium. (See Statement of Net Position chart below.) This reduction of deferred premium being primarily attributable to an overall payroll decrease brought about by current economic conditions. Deferred premium revenue represents the amount of premium billed, but not yet earned, for the future period. The decrease in accrued refundable premium is the result of efforts made to more accurately estimate premium billing. The Fund had no increase in base rates effective January 1, 2013.

**State Accident Fund
Condensed Statements of Net Position
June 30, 2013**

	FY2013	FY2012
ASSETS		
Current assets	\$ 281,504,972	\$ 272,439,791
Capital assets, net of accumulated depreciation	120,780	76,123
Other noncurrent assets	368,829	436,796
Total assets	<u>281,994,581</u>	<u>272,952,710</u>
LIABILITIES		
Current liabilities	153,867,584	154,687,669
Noncurrent liabilities	157,521,083	158,002,720
Total liabilities	<u>311,388,667</u>	<u>312,690,389</u>
Net Position		
Invested in capital assets	120,780	76,123
Unrestricted	(29,514,866)	(39,813,802)
Total net position	<u>\$ (29,394,086)</u>	<u>\$ (39,737,679)</u>



The chart above shows the breakdown of liabilities and the change compared to the previous fiscal year.

Statements of Revenues, Expenses, and Changes in Net Position

This statement represents operating revenues and expenses, as well as the non-operating revenues and expenses during the operating year. The purpose of this statement is to present the reader with information relating to monies received and expenses paid during the year. The Fund's revenue comes primarily from premium income for workers' compensation insurance coverage provided to state agencies and political subdivisions. The major expenses are from incurred claim liabilities, which include medical costs and lost wages paid to injured workers, and the change in anticipated future payments. The Fund is a quasi-governmental organization whose normal operation is similar to that of other property and casualty insurance companies. The Fund receives no state appropriations.

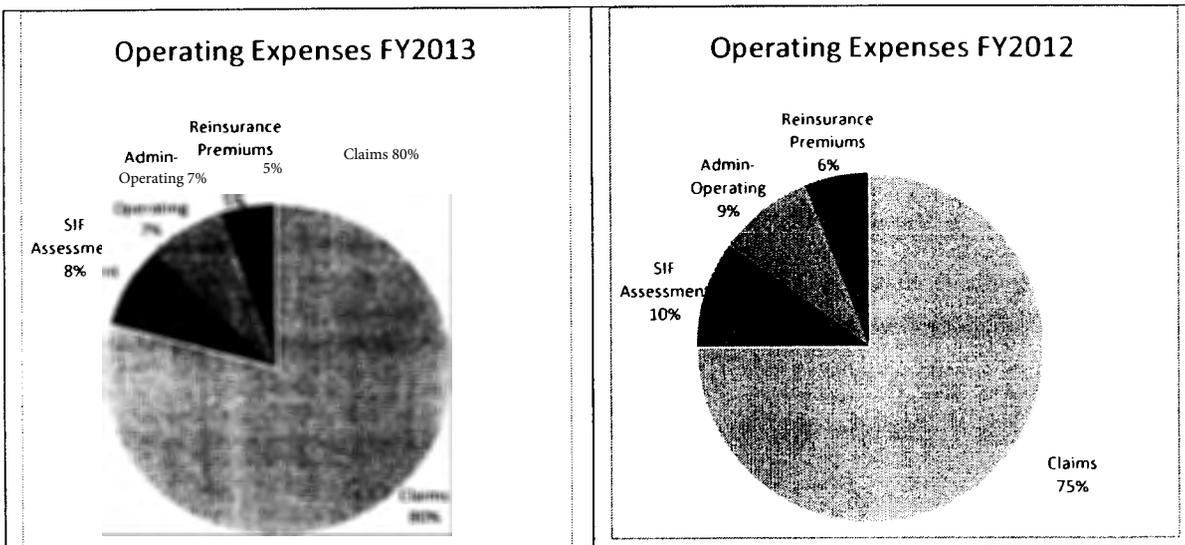
The Fund is a proprietary fund entity; therefore, the Statement of Revenues, Expenses, and Changes in Net Position has been prepared on the accrual basis. Statements prepared using the accrual basis recognize revenues when earned and expenses when incurred.

The operating revenue in this statement includes primarily premium billed based on policyholder payroll but also effected by their experience modifier. The experience modifier can either increase or decrease the policyholder's premium. As a result of new policies electing to purchase their coverage from the Fund, operating revenue increased by \$1.5 million in fiscal year 2013. The non-operating revenues decreased due to low interest rates received on investments with the State Treasurer's Office.

The operating expenses in this statement include administrative expenses, claims paid, and claims incurred during the year. Operating expenses increased by \$6.1 million compared to the prior fiscal year. This increase was mostly due to the reduction in Second Injury Fund recoveries which offsets the claims cost. Fiscal year 2013 had a change in reserves of \$335 thousand (which increased the claims incurred). The administrative cost ratio, the amount of premium dollars used to operate the Fund, during fiscal year 2013 remained below 7.5%. The South Carolina State Accident Fund continues to have one of the lowest administrative cost ratios in the workers' compensation industry.

	2013	2012
Operating revenues	\$ 75,596,185	\$ 74,133,752
Operating expenses	<u>67,070,597</u>	<u>60,945,582</u>
Operating gain (loss)	8,525,588	13,188,170
Nonoperating revenues	<u>1,818,005</u>	<u>3,962,473</u>
Change in Net Position	10,343,593	17,150,643
Net position (deficit) - beginning of year	<u>(39,737,679)</u>	<u>(56,888,322)</u>
Net position (deficit) - at end of year	<u>\$ (29,394,086)</u>	<u>\$ (39,737,679)</u>

The charts below show that during the past two fiscal years 75-80% of expenses have been paid directly to injured workers or to medical providers on behalf of the injured worker.



Capital Asset and Debt Activity

Capital assets increased by \$83,855 for the purchase of a new backup system, the replacement of a server, two net switch and a disk drive for additional capacity. Servers are used to connect users to the agency network. These purchases enabled the Fund to maintain and improve its operations, data storage, and enhance communication. There were no other significant additions to capital assets and no capital asset retirements during the fiscal year. The Fund had no changes in credit rating or debt limitations that may affect future financing.

Economic Outlook

The past several years have been a challenging financial period for South Carolina and the nation as businesses and government adjusted to a historic economic downturn resulting in job reductions, stagnant or declining payroll, reduced capital, and an overall tentative business environment. In no way was the South Carolina State Accident Fund immune to the effects of the Great Recession. The overall reduction in payroll among policyholders severely and adversely impacted the premium revenue that provides the operational income for the Fund. Nevertheless, as a result of management initiatives implemented in 2005, years before the current economic crisis, the Fund has positioned itself to meet financial challenges through focused efforts to promote operational efficiency, quality case management, and effective premium pricing. Those efforts have paid off as Fiscal Year 2013 marks the eighth consecutive year of performance success for the South Carolina State Accident Fund which concluded the year with a net operating income of \$10,343,593.

Understanding that the economic climate is still precarious, the Fund will continue to explore and develop new and innovative methods of decreasing operating expenses while maintaining low claim costs, stable premium pricing, and high customer satisfaction. Working with our actuaries and reinsurers, we will continue the ongoing efforts to improve our overall financial standing while at the same time establishing and maintaining adequate reserves to ensure the long-term financial viability of the Fund. Mindful that the effects of the recession are not unique to the State Accident Fund, we are also keenly aware that our policyholders have been adversely impacted. It is our goal to understand the challenges and needs of our policyholders and assist them in meaningful ways to reduce their overall workers' compensation costs. By maximizing efficiency without sacrificing quality customer service, we believe we accomplished this goal with resulting rate stabilization and reductions to base premiums.

As South Carolina and the nation begin to recover from the recent economic challenges, the State Accident Fund remains committed to providing stable, long-term workers' compensation coverage to state, county, and local governments as cost-effectively as possible. Our emphasis on higher efficiencies, lower costs, and improved delivery of services will help us remain well-positioned to keep our promises to our policyholders and their employees long into the future. In that way, the State Accident Fund will continue to operate in a financially stable manner while fulfilling its mission. As the economy improves, that is good news for South Carolina employers and workers.

SOUTH CAROLINA STATE ACCIDENT FUND

STATEMENT OF NET POSITION

JUNE 30, 2013

ASSETS

Current Assets:

Cash and cash equivalents	\$	214,198,947
Premiums receivable		64,881,011
Claims recoveries and reimbursement receivables, net of allowance for doubtful accounts of \$706,688		1,890,360
Recoverable under reinsurance annuity contract		36,809
Accrued interest receivable		484,860
Prepaid expenses		12,985
Total current assets		281,504,972

Noncurrent Assets:

Capital assets, net of accumulated depreciation		120,780
Investment in reinsurance annuity contract, net of accumulated amortization of \$913,465		368,829
Total noncurrent assets		489,609
Total assets	\$	281,994,581

LIABILITIES AND NET POSITION

Current Liabilities:

Accounts payable	\$	2,064,924
Accrued compensated absences and related benefits		251,641
Accrued payroll and related liabilities		262,859
Accrued refundable premiums		3,548,170
Deferred premium revenue		69,215,596
Unpaid claims liability and claims adjustment expenses payable within one year - net		78,524,394
Total current liabilities		153,867,584

Noncurrent Liabilities:

Accrued compensated absences and related benefits		45,477
Unpaid claims liability and claims adjustment expenses payable beyond one year - net		157,475,606
Total noncurrent liabilities		157,521,083

Total liabilities		311,388,667
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Net Position (Deficit):

Invested in capital assets		120,780
Unrestricted deficit		(29,514,866)
Total net position (deficit)		(29,394,086)
Total liabilities and net position	\$	281,994,581

See accompanying Notes to Financial Statements.

SOUTH CAROLINA STATE ACCIDENT FUND

**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN FUND NET POSITION
YEAR ENDED JUNE 30, 2013**

OPERATING REVENUES	
Premiums	<u>\$ 75,596,185</u>
OPERATING EXPENSES	
Claims	53,271,226
Second Injury Fund assessment	5,518,221
Administrative:	
Personal services and employee benefits	3,596,779
Contractual services	548,295
Rent and insurance	342,121
Supplies and materials	66,931
Depreciation	39,198
Amortization expense - reinsurance annuity contract premium	37,620
Reinsurance premiums	3,544,920
Bad debts	34,511
Other expenses	45,775
Actuarial fee	25,000
Total administrative expenses	<u>8,281,150</u>
Total operating expenses	<u>67,070,597</u>
OPERATING INCOME	8,525,588
NONOPERATING REVENUES	
Interest/investment income	<u>1,818,005</u>
CHANGE IN NET POSITION	10,343,593
NET POSITION (DEFICIT), AT BEGINNING OF YEAR	<u>(39,737,679)</u>
NET POSITION (DEFICIT), AT END OF YEAR	<u><u>\$ (29,394,086)</u></u>

See accompanying Notes to Financial Statements.

SOUTH CAROLINA STATE ACCIDENT FUND

**STATEMENT OF CASH FLOWS
YEAR ENDED JUNE 30, 2013**

CASH FLOWS FROM OPERATING ACTIVITIES:

Cash received for premiums from state agencies	\$ 52,068,243
Cash received for premiums from other entities	17,153,512
Cash received for reimbursements of claims expense from state agencies	6,058,283
Cash received for reimbursements of claims expense from other entities	1,738,640
Payments for claims	(60,344,164)
Refunds of premiums to state agencies	(7,494)
Refunds of premiums to other entities	(93,308)
Refunds of claims expense to state agencies	(98,053)
Refunds of claims expense to other entities	(39,486)
Payments for salaries and related benefits	(3,650,127)
Payment of second injury fund assessment to other state agency	(3,862,755)
Payments for other administrative expenses to other state agencies	(296,070)
Payments for other administrative expenses to other entities	(4,145,197)
Net cash provided by operating activities	4,482,024

CASH FLOWS FROM NON-CAPITAL AND RELATED FINANCING ACTIVITIES:

Repayment of cash overdraft	(417,418)
Net cash used by non-capital and related financing activities	(417,418)

CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES:

Acquisition of capital assets	(83,855)
Net cash used by capital and related financing activities	(83,855)

CASH FLOWS FROM INVESTING ACTIVITIES:

Interest/investment income received	2,168,279
Net cash provided by investing activities	2,168,279

NET INCREASE IN CASH AND CASH EQUIVALENTS

6,149,030

CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR

208,049,917

CASH AND CASH EQUIVALENTS AT END OF YEAR

\$ 214,198,947

**Reconciliation of net operating revenues
to net cash provided by operating activities:**

Operating income	\$ 8,525,588
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation and amortization	76,818
Changes in assets and liabilities:	
(Increase) decrease in premiums receivable	(3,269,806)
(Increase) decrease in claims recoveries and reimbursement receivables	820
(Increase) decrease in prepaid expenses	(2,718)
(Increase) decrease in recoverable under reinsurance annuity contract	35,626
Increase (decrease) in accounts payable	1,824,470
Increase (decrease) in accrued compensated absences and related benefits	(57,340)
Increase (decrease) in accrued payroll and related liabilities	3,992
Increase (decrease) in accrued refundable premiums	(2,750,196)
Increase (decrease) in deferred premium revenue	(455,230)
Increase (decrease) in estimate of unpaid claims liability	550,000
Total adjustments	(4,043,564)
Net cash provided by operating activities	\$ 4,482,024

See accompanying Notes to Financial Statements.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The financial statements of South Carolina State Accident Fund (the Fund) were prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to governmental entities. The Government Accounting Standards Board (GASB) is the accepted standard-setting body in the United States of America for establishing governmental accounting and financial reporting principles. The more significant of the Fund's accounting policies are described below.

Reporting Entity

The South Carolina State Accident Fund, a primary entity, is part of the primary government of the State of South Carolina and is included in the Comprehensive Annual Financial Report of the State of South Carolina. The Fund was established by Section 42-7-10 of the Code of Laws of South Carolina, as amended, to provide worker's compensation insurance coverage to State entities. Although the State of South Carolina is the Fund's predominant participant, counties, municipalities, and other political subdivisions of the State may elect to participate. The State assumes the full risk for the covered claims. The Fund is responsible for investigating, adjusting and paying worker's compensation claims as awarded by the Worker's Compensation Fund for job related accidental injury, disease, or death to employees of participants.

The Fund is administered by a director, appointed by the Governor, with the advice and consent of the Senate, for a term of six years. The accompanying financial statements present the financial position, results of operations, and cash flows solely of the Fund and do not include any other departments, institutions, component units, etc. of the State of South Carolina.

The core of the financial reporting entity is the primary government which has a separately elected governing body. As required by accounting principles generally accepted in the United States of America ("GAAP"), 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.

A 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 government or entity that holds one or more of the following powers:

- (1) Determines its budget without another government's having the Fund to approve and modify that budget.
- (2) Levies taxes or set rates or charges without approval by another government.
- (3) Issues bonded debt without approval by another government.

An organization can also be a component unit of another entity if the exclusion of that organization would be misleading to the users of the primary entity's financial statements. The organization is fiscally independent if it holds all three of those powers. Based on the criteria, the Fund has determined it is not a component of another entity and it has no component units.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

The budget, personnel, procurement, and other laws of the State and the policies and procedures for State agencies are applicable to the activities of the Fund.

Fund Accounting

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

A fund is a separate fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with related liabilities and residual equities or balances and changes therein which are segregated to carry on specific activities or attain certain objectives in accordance with applicable regulations, restrictions, or limitations.

The South Carolina State Accident Fund is an internal service fund of the proprietary fund types of the State of South Carolina. Such funds account for the financing of goods and services that are used primarily by the State.

Basis of Accounting

The accounting policies of the Fund conform to generally accepted accounting principles (GAAP) applicable to proprietary activities as prescribed by the Governmental Accounting Standards Board (GASB), the recognized standard-setting body for GAAP for all state governmental entities. Proprietary fund entities use the accrual basis of accounting. If measurable, revenues are recognized when earned and expenses when incurred. In accordance with GASB Statement 20, the Fund has elected to apply all applicable GASB pronouncements and not to apply FASB pronouncements and interpretations issued after November 30, 1989.

Cash and Cash Equivalents

The amount shown in the financial statements as "cash and cash equivalents" represents cash on deposit with the State's Treasurer, cash in banks, and cash invested in various instruments by the State Treasurer as part of the State's internal cash management pool (the "Pool") and short-term investments not held by the State Treasurer's Office and having a maturity at purchase of three months or less.

Because the 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.

The 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 held by the Pool are carried at fair value. Interest earned on the agency's special deposit account is posted to the agency's account at the end of each month and is retained by the agency. The Fund records and reports its deposits in the general deposit account at cost. The Fund reports its deposits in the special deposit accounts at fair value. Interest earnings are allocated based on the percentage of the Fund's accumulated daily income receivable to the total interest receivable of the Pool. Reported investment 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.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Unrealized gains and losses are allocated at year-end based on the percentage ownership in the Pool.

Although the Pool includes some long-term investments, it operates as a demand deposit account, therefore, for credit and other risk information pertaining to the Pool, see the Comprehensive Annual Financial Report ("CAFR") of the State.

Capital Assets

Capital assets are recorded at cost at the date of acquisition. The Fund follows capitalization guidelines established by the State of South Carolina. All land is capitalized, regardless of cost. The Fund capitalizes movable personal property with a unit value in excess of \$5,000 and a useful life in excess of two years and intangible assets including software costing in excess of \$100,000. Routine repairs and maintenance are charged to operating expenses in the year in which the expense was incurred.

Depreciation is computed using the straight-line method over the estimated useful lives of the assets, generally 3 to 10 years.

Unpaid Claims Liability

The Fund establishes unpaid claims liabilities based on estimates of the ultimate cost of claims that have been reported but not settled, and of claims that have been incurred but not reported. The amount accrued includes estimated specific incremental claims adjustment expenses. Estimated amounts of salvage and subrogation and reinsurance recoverable, if any, on both settled and unsettled claims have been deducted from the liability for unpaid claims to the extent reasonably estimable. In addition, to the extent reasonably estimable, the liability for unpaid claims has been adjusted for amounts to be recovered or reimbursed from participants who retain the risk of loss for specific periods. This includes amounts recoverable from the State of South Carolina for state agency claims prior to July 1, 1986. See Note 8 for further explanation. Claims liabilities for claims of the South Carolina Department of Transportation ("DOT") prior to January 1, 1994, are not included in the State Accident Fund's claims liability. See below and Note 4 for further information. Because actual claims costs depend on such complex factors as inflation, changes in doctrine of legal liability, and damage awards, the process used in computing claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed annually as of fiscal year end using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. While management believes that the amount is adequate, the ultimate liability may be in excess of or less than the amounts provided.

The methods for making such estimates and for establishing the resulting liability are continually reviewed, and any adjustments are reflected in current earnings. A provision for inflation in the calculation of estimated future claims costs is implicit in the calculation because reliance is placed both on actual historical data that reflect past inflation and on other factors that are considered to be appropriate modifiers of past experience. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made.

DOT and the South Carolina Department of Public Safety ("DPS") managed their own workers' compensation claims prior to the State's restructuring in 1993. When they became policyholders, the Fund agreed to provide claim services for their claims with a date of injury prior to January 1, 1994 for DOT and August 1, 1993 for DPS. Because the Fund was not the insurer and had not collected premiums to cover these losses, the agencies reimbursed the Fund for the cost of these claims.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

In the 1998-1999 Appropriations Bill 700, Proviso 44.4 stated, "(SAF: Workers' Compensation Claims) from the funds in the Workers' Compensation Trust Fund, the Fund shall purchase an annuity for the purpose of funding the future obligation for workers' compensation claims filed prior to restructuring by South Carolina Department of Highways and Public Transportation employees." After June 30, 1998 the Fund was no longer reimbursed, as originally agreed upon. Instead, it used the funds received from the annuity purchased under the proviso to pay these claims. This annuity is being amortized over the life of the contract in proportion to annuity proceeds received. See Note 4 for further discussion.

Reinsurance

The Fund has obtained reinsurance coverage to reduce its exposure to losses on insured events. Losses in excess of \$1,000,000 from an insured event are covered up to limits based on the type of injury as set by the worker's compensation statutes of the South Carolina Code of Laws, with the Fund retaining the risk for the first \$1,000,000 of loss. Reinsurance permits recovery of a portion of losses from reinsurers, although it does not discharge the primary liability of the Fund as direct insurer of the risks reinsured. The Fund does not report reinsured risks as liabilities, unless it is probable that those risks will not be covered by reinsurers. The reinsurance coverage also reduces its exposure to losses on insured events related to State owned aircrafts in excess of \$1,000,000 per occurrence up to the limit of \$9,000,000.

Recognition of Premium Revenue, Receivables and Deferred Revenue

Premiums are recognized as revenue on a pro rata basis over the policy term. Policies are billed and issued on both the fiscal year and calendar year basis. Premiums are based on an actuarial method and are currently adjusted so that over a reasonable period of time expected revenues, including investment income, and anticipated expenses will be approximately equal. In addition, premium revenue includes accrued premium adjustments for additional premiums owed by policyholders as determined based on actual payrolls for the policy period which are in excess of estimated premiums billed. This premium revenue was based on estimated payroll costs. Revenue is reduced for refunds payable. Estimated premiums receivables and refund payables are recorded as of year-end for future anticipated premium adjustments for the policy years which end within the Fund's fiscal year. A receivable is recorded at the time the annual estimated premium is billed even though some/all of the amounts may not be currently due. Deferred revenue is recognized to the extent that the premiums billed and not yet received are for future periods. In addition, deferred revenue is recognized for unearned premiums received.

Budget Policy

The Fund is granted an annual appropriation for operating purposes by the South Carolina General Assembly (the "General Assembly") to be funded by workers' compensation premiums and interest earned thereon. The Appropriation, as enacted, becomes the legal operating budget for the Fund. The Appropriations Act authorizes expenditures from the General Fund of the State and authorizes expenditures of total funds. The General Assembly enacts the budget through passage of specific line-item appropriations by program within budgetary unit, within budgetary fund category, the General Fund or other budgeted funds. Budgetary control is maintained at the line-item level of the entity. Agencies may process disbursement vouchers in the State's budgetary accounting system only if enough cash and appropriation authorization exist. Transfers of funds may be approved by the State Budget and Control Board under its Fund or by the agency as set forth in the 2013 Appropriations Act proviso 89.9 as follows: Agencies are authorized to transfer appropriations within programs and within the agency with notification to the Division of Budget and Analyses and the State Comptroller General. No such transfer may exceed twenty percent of the program budget. Transfers from personal services accounts or from other operating accounts may be restricted to any level set by the Board.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

Current legislation states that the General Assembly intends to appropriate all monies to operate State government for the current fiscal year. Any unexpended appropriations as of June 30 automatically lapse on July 31 unless authorization is received from the General Assembly to carry over the funds to the ensuing fiscal year. State law does not precisely define the budgetary basis of accounting. For each fiscal year, the level of legal control for each agency is reported in a publication by the State Comptroller General. The State's annual budget is prepared primarily on the modified accrual basis of accounting with several exceptions, principally the cash basis for payroll expenses and certain non-State appropriations revenue.

The Fund's budget includes administrative expenses and specifically excludes claims expense and the Second Injury Fund assessment. Amounts to be expended for capital assets are also budgeted. Expenses prepared on the accrual basis do not vary significantly from the budgetary basis. In accordance with GAAP applicable to business-type activities, a comparison of actual revenues and expenses to the budgeted amounts has not been presented.

Statement of Cash Flows

For purposes of cash flows, the Fund considers all highly liquid investments with a maturity of three months or less when purchased to be cash equivalents. The Pool is included in this definition of cash equivalents.

Compensated Absences

Generally, all permanent full-time State employees and certain part-time employees scheduled to work at least one-half of the Fund'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 and compensatory holiday and overtime leave earned for which the employees are entitled to paid time off or payment at termination. The Fund calculates the compensated absences liability based on recorded balances of unused leave for which the employer expects to compensate employees through paid time off or cash payments at termination. That liability is determined by using fiscal year-end current salary costs and the cost of the salary-related benefit payments. The net change in the liability is recorded in the current year in the personal services and employee benefits expense category.

Operating and Nonoperating Revenues and Expenses

The Fund distinguishes operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and delivering goods in connection with a proprietary fund's principal ongoing operations. The Fund's primary operating revenues are from premium revenues. Operating expenses include the cost of services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses. Nonoperating revenues include interest/investment income and other revenues.

Net Position

The Fund reports under the provisions of GASB Statement No. 34 of the GASB, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments* ("GASB 34").

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED):

GASB 34 established standards for external financial reporting for all state and local governmental entities, which includes a statement of net position, with classification of net position into three components. These components are categorized as follows:

Invested in capital assets: This represents the Fund's total investment in capital assets, net of outstanding debt obligations, if any, related to those capital assets. To the extent debt has been incurred but not yet expended for capital assets, such amounts are not included as a component of invested in capital assets, net of related debt.

Unrestricted net position: Unrestricted net position (deficit) represents the remainder of the Fund's liabilities in excess of assets excluding the net position reported in other categories.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Such estimates include the unpaid claims liability.

Change in Accounting Principle

For 2013, the Fund implemented Governmental Accounting Standard Board (GASB) Statement No. 63, "Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position". GASB Statement No. 63 identifies net position, rather than net assets, as the residual of all other elements presented in a statement of financial position. This change was incorporated in the Fund's 2013 financial statements; however, there was no effect on beginning net position/fund balance.

NOTE 2 RISK MANAGEMENT:

Insurance Coverage

The Fund, an administrative agency, is exposed to various risks of loss and maintains State or commercial insurance coverage for each of those risks. Management believes such coverage is sufficient to preclude any significant uninsured losses for the covered risks. The cost of settled claims and claim losses has not exceeded this coverage in any of the past three years. The Fund pays insurance premiums to itself and certain other State agencies 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 accordance with insurance policy and benefit program limits. 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 type of claims:

1. Claims of State employees for unemployment compensation benefits. This type of claim is handled through the South Carolina Department of Employment and Workforce.
2. Claims of covered employees for workers' compensation benefits for job-related illnesses or injuries. This type of claim is handled by the State Accident Fund.
3. Claims of covered public employees for health and dental insurance benefits. This type of claim is handled by the Public Employee Benefit Authority – Insurance Benefits.
4. Claims of covered public employees for long-term disability and group-life insurance benefits. This type of claim is handled through the Public Employee Benefit Authority – Insurance Benefits.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 2 RISK MANAGEMENT (CONTINUED):

Employees elect health coverage through either a health maintenance organization or through the State's self-insured plan. All of the other coverages previously listed are through the applicable State self-insured plan except dependent and optional life premiums are remitted to commercial carriers. The Fund and other entities pay premiums to the State's Insurance Reserve Fund (IRF) which issues policies, accumulates assets to cover the risks of loss, and pays claims incurred for covered losses related to the following assets, activities, and/or events:

1. Theft of, damage to, or destruction of assets – building contents;
2. General tort claims; and
3. Data processing equipment.

The IRF is a self-insurer and purchases reinsurance to obtain certain services and specialized coverage and to limit losses in the areas of property insurance. Also, the IRF purchases reinsurance for catastrophic property insurance. Reinsurance permits partial recovery of losses from reinsurers, but the IRF remains primarily liable. The IRF's rates are determined actuarially. State agencies and other entities are the primary participants in the State's Health and Disability Insurance Fund and in the IRF.

The Fund has not transferred the portion of the risk of loss related to insurance policy deductibles for its property contents or general torts to a State or commercial insurer, and does not carry fidelity bond coverage on its employees. There were no expenses incurred for the year ended June 30, 2013 for actual claim payments related to such retained risk of loss.

The Fund has not reported an estimated claims loss expense and the related liability at June 30, 2013, based on the requirements of GASB Statements No. 10 and No. 30, which state 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, 2013, and the amount of loss is reasonably estimable. In management's opinion, claims losses in excess of insurance coverage, if any, are unlikely and, if incurred, would be insignificant to the Fund's financial position. Furthermore, there is no evidence of asset impairment or other information to indicate that a loss should be recorded. Therefore, no loss accrual has been recorded.

NOTE 3 DEPOSITS AND INVESTMENTS:

Cash and cash equivalents consist of deposits under the control of the State Treasurer, who by law, has sole authority for investing State funds and deposits under the control of the State Accident Fund. However, as authorized by the State Treasurer's office, certain funds used to pay claims are deposited with financial institutions.

Deposits

State law requires full collateralization of all State Treasurer's bank balances. The State Treasurer must correct any deficiencies in collateral within seven days. With respect to investments in the State's 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, credit and other risks as required by GASB Statement No. 40, *Deposit and Investment Risk Disclosures*, of the State Treasurer's investments is disclosed in the CAFR of the State. Copies of this report may be obtained from the South Carolina Office of the Comptroller General, 1200 Senate Street, 305 Wade Hampton Office Building, Columbia, South Carolina 29201 or by visiting the Comptroller General's website at <http://www.cg.sc.gov>.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2013

NOTE 3 DEPOSITS AND INVESTMENTS (CONTINUED):

At June 30, 2013, cash and cash equivalents was \$212,177,767 which was in accounts with the State Treasurer and the Treasurer's balance was \$213,677,767. At June 30, 2013, the bank balance in financial institutions was \$1,554,208 and the amount reported in the financial statements was \$2,021,180. The entire bank balance was covered by insurance and collateralized with securities held by the Fund, or by its agent in the Fund's name.

Investments

Investments meet the State's investment guidelines and consist of overnight repurchase agreements which are fully collateralized by U.S. Treasury securities. Because of the relatively small amount of the investments in overnight repurchase agreements, management does not believe that there is any concentration of credit risk associated with its investments. Fair value of investments approximates cost because of the short maturity of these investments. All of the Fund's investments are stated at fair value except those meeting certain specific requirements. Purchases and sales are accounted for on the trade date. Unrealized gains and losses on investments have been recorded on the accrual basis. Earnings are recorded on the accrual basis. The Fund had investment in reinsurance annuity contract of \$368,829 at June 30, 2013. Further details of this investment are found in Note 4.

NOTE 4 INVESTMENT IN REINSURANCE ANNUITY CONTRACT:

Under the 1993 Restructuring Act, the DOT and the DPS were created and were charged with responsibilities of the former Department of Highways and Public Transportation effective July 1, 1993. Proviso 44.4 of the 1998-1999 Appropriation Act passed by the General Assembly required the Fund to purchase an annuity for the purpose of funding the future obligation for workers' compensation claims filed prior to restructuring by the Department of Highways and Public Transportation employees using funds from the Workers' Compensation Trust Fund. While the State believes the annuity will provide funding adequate to cover this liability, the Fund has ultimate responsibility to pay these claims should the annuity funding be inadequate. On March 11, 1999 the Fund purchased a Type One annuity that will pay a fixed amount quarterly for a period of forty years. The annuity was effective as of January 1, 1999. The Fund received its first quarterly annuity payment on April 5, 1999. For the year ended June 30, 2013, the Fund paid approximately \$24,000 of the DOT claims covered by this annuity. They received reimbursement of \$60,088 under this contract for the year ended June 30, 2013. For the year ended June 30, 2013, the amount of \$36,809 shown on the statement of net position as recoverable under reinsurance annuity contract, represents amounts due under the annuity that will be collected in the future for cumulative claims payments in excess of cumulative annuity receipts. The estimated future claims for DOT is \$320,000, which is not included in the unpaid claims liability and claims adjustment expenses payable on the statement of net position.

Under the terms of the annuity the Fund will receive 160 quarterly payments. For the first forty payments the Fund will receive \$30,091 per quarter, the next forty payments will be for \$15,022, the next forty payments will be for \$3,726, and the last forty will be for \$2,364. Total amount to be received under the annuity will be \$2,048,120.

The total price of the annuity was \$1,282,294 and was paid in a single premium. The amount of the annuity to purchase was determined actuarially. The amount remaining to be received by the Fund at June 30, 2013 was \$589,106.

The liability for these claims is not reported by either the Fund or the DOT because the State feels that the proceeds from the annuity contract will provide adequate funding to pay these claims and the risk of loss is remote. The annuity is being amortized over the life of the annuity in proportion to annuity proceeds received. The amount of amortization charged for the year ended June 30, 2013

SOUTH CAROLINA STATE ACCIDENT FUND

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013**

was \$37,620, and is included as amortization expense in the Statement of Revenues, Expenses and Changes in Fund Net Position.

NOTE 5 PREMIUMS RECEIVABLE:

Premiums receivable consist of amounts receivable from the following:

County and Municipal Governments and Agencies	\$ 5,477,518
State Agencies	<u>59,403,493</u>
	<u><u>\$ 64,881,011</u></u>

The majority of premiums receivable represent billings for future periods which have not been earned as of fiscal year-end.

NOTE 6 CAPITAL ASSETS:

Capital assets activity for the year ended June 30, 2013 is summarized as follows:

	Beginning Balance July 1, 2012	Increases	Decreases	Ending Balance June 30, 2013
Equipment and furniture	\$ 991,137	\$ 83,855	\$ -	\$ 1,074,992
Software	<u>8,152,000</u>	<u>-</u>	<u>-</u>	<u>8,152,000</u>
Total capital assets at historical cost	<u>9,143,137</u>	<u>83,855</u>	<u>-</u>	<u>9,226,992</u>
Less accumulated depreciation for:				
Equipment and furniture	(915,014)	(39,198)	-	(954,212)
Software	<u>(8,152,000)</u>	<u>-</u>	<u>-</u>	<u>(8,152,000)</u>
Total accumulated depreciation	<u>(9,067,014)</u>	<u>(39,198)</u>	<u>-</u>	<u>(9,106,212)</u>
Capital assets, net of accumulated depreciation	<u>\$ 76,123</u>	<u>\$ 44,657</u>	<u>\$ -</u>	<u>\$ 120,780</u>

Depreciation expense was \$39,198 for the year ended June 30, 2013.

NOTE 7 ACCRUED REFUNDABLE PREMIUMS:

Policyholders are billed annually for estimated premiums based on the policyholder's estimated payroll. After the policy period ends, policyholders submit the details of the actual salaries paid, and the Fund adjusts the premium based on the actual payroll and a rating modifier based on claims experience. The amount the Fund owed policyholders for estimated premiums in excess of actual adjusted premiums at June 30, 2013 was \$890,276 for those county and municipal policyholders. An additional \$2,657,894 was due to State agencies.

NOTE 8 UNPAID CLAIMS LIABILITY AND CLAIMS ADJUSTMENT EXPENSES:

The amount accrued for unpaid claims liability and claims adjustment expenses is an actuarially determined amount, based on the Fund's historical claims expenses adjusted for current factors, for the estimated ultimate cost of settling claims for events which occurred on or before year-end but were unpaid at the end of the year. To the extent claims were incurred on behalf of state agencies prior to July 1, 1986, reimbursement will be due from the State when the claims are paid. Estimated amounts recoverable from subrogation have been deducted from the claims liability.

SOUTH CAROLINA STATE ACCIDENT FUND

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 8 UNPAID CLAIMS LIABILITY AND CLAIMS ADJUSTMENT EXPENSES (CONTINUED):

The estimated reimbursement due from the State for claims prior to July 1, 1986, which is included in unpaid claims liability and claims liability adjustment expense, is as follows:

Due within one year	\$ 115,000
Due after one year	<u>510,000</u>
Total	<u><u>\$ 625,000</u></u>

The amounts accrued for unpaid claims liability and claims adjustment expenses, net of amounts recoverable from the State, for the past two years are as follows:

	2013	2012
Unpaid claims liability and claim adjustment expenses at beginning of year	\$ 235,450,000	\$ 237,790,000
Current year claims and changes in estimates	53,271,226	45,688,483
Claims payments	<u>(52,721,226)</u>	<u>(48,028,483)</u>
Total unpaid claims liability and claim adjustment expenses at the end of year	<u><u>\$ 236,000,000</u></u>	<u><u>\$ 235,450,000</u></u>

This claims liability is further categorized as follows:

State Agencies	\$ 181,249,000	\$ 177,509,000
Counties and Municipalities	54,751,000	57,941,000
Total	<u><u>\$ 236,000,000</u></u>	<u><u>\$ 235,450,000</u></u>

NOTE 9 SECOND INJURY FUND ASSESSMENT:

The Fund is required to pay an annual assessment to the Second Injury Fund of the State. The assessment is usually billed in the first quarter of the fiscal year and is based on a specified percentage of total claims paid by the Second Injury Fund during the previous calendar year. The Second Injury Fund handles claims for workers who have permanent physical impairments and incur subsequent disability from injury by accidents arising out of and in the course of employment. The assessment for fiscal year 2013 was \$5,518,221, of which \$1,655,466 was paid subsequent to June 30, 2013 and is included in accounts payable. The Fund receives reimbursements of claims expense from the Second Injury Fund. The total amount recovered during fiscal year 2013 was \$5,961,891 which is reported as a reduction of claims expense.

NOTE 10 PENSION PLAN:

All employees of the Fund are eligible to participate in 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 South Carolina Public Employee Benefit Authority (PEBA), a public employee retirement system. Generally, all full-time or part-time equivalent State employees in a permanent position are required to participate in and contribute to the SCRS as a condition of employment unless exempted by law as provided in Section 9-1-480 of the South Carolina Code of Laws, as amended, or are eligible and elect to participate in the State Optional Retirement Program (ORP). The SCRS plan provides a life-time monthly retirement annuity benefits to members as well as disability, survivor options, annual benefit adjustments, death benefits, and incidental benefits to eligible employees and retired members.

The Retirement Division maintains five independent defined benefit plans and issues its own publicly available Comprehensive Annual Financial Report (CAFR) which includes financial statements and required supplementary information.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2013

NOTE 10 PENSION PLAN (CONTINUED):

A copy of the separately issued CAFR may be obtained by writing to the South Carolina Public Employee Benefit Authority, P.O. Box 11960, Columbia, South Carolina 29211-1960. Furthermore, the Division and the five pension plans are included in the State of South Carolina's CAFR.

Under the SCRS, Class II members are eligible for a full service retirement annuity upon reaching age 65 or completion of 28 years of credited service regardless of age. Employees who first became members of the System after June 30, 2012 are considered Class III members and are eligible for a full service retirement annuity upon reaching age 65 or upon meeting the rule of 90 requirement (i.e., the members age plus the years of service add up to a total of at least 90).

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 (AFC) multiplied by the number of years of credited service. For Class II members, AFC is the average annual earnable compensation during 12 consecutive quarters and includes an amount for up to 45 days termination pay at retirement for unused annual leave. For Class III members, AFC is the average annual earnable compensation during 20 consecutive quarters and termination pay for unused annual leave at retirement is not included. Early retirement options with reduced benefits are available as early as age 55 for Class II members and age 60 for Class III members. Class II members are vested for a deferred annuity after five years of earned service. Class III members are vested for a deferred annuity after eight years of earned service. Members qualify for a survivor's benefit upon completion of 15 years of credited service (five years effective January 1, 2002).

Disability annuity benefits are payable to Class II members if they have permanent incapacity to perform regular duties of the member's job and they have at least 5 years of earned service (this requirement does not apply if the disability is a result of a job related injury). Class III members qualify for disability annuity benefits provided they have a minimum of eight years of credited service. An incidental death 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 or to a working retired contributing member. There is no service requirement for death resulting from actual performance of duties for an active member. For eligible retired members, a lump-sum payment is made to the retiree's beneficiary of up to \$6,000 based on years of service at retirement. TERI participants and retired contributing members are eligible for the increased death benefit equal to their annual salary in lieu of the standard retired member benefit.

Effective January 1, 2001, Section 9-1-2210 of the South Carolina Code of Laws allows employees eligible for service retirement to participate in the Teacher and Employee Retention Incentive (TERI) Program. TERI participants may retire and begin accumulating retirement benefits on a deferred basis without terminating employment for up to five years. Upon termination of employment or at the end of the TERI period, whichever is earlier, participants will begin receiving monthly service retirement benefits which will include any cost of living adjustments granted during the TERI period. Because participants are considered retired during the TERI period, they do not earn service credit, and are ineligible to receive group life insurance benefits or disability retirement benefits. The TERI program will end effective June 30, 2018.

Effective July 1, 2012, employees participating in the SCRS were required to contribute 7.00% of all earnable compensation. The employer contribution rate for SCRS was 15.15%. Included in the total SCRS employer contribution rate is a base retirement contribution of 10.45%, .15% for the incidental death program and a 4.55% surcharge that will fund retiree health and dental insurance coverage. Employer contributions for State ORP include a 5.45% employer retirement contribution, 4.55% retiree insurance surcharge and .15% incidental death benefit. The Fund's actual contributions to the SCRS for the years ended June 30, 2013, 2012, and 2011 were approximately \$257,000, \$237,000, and \$233,000, respectively, and equaled the base required retirement contribution rate, excluding surcharge, of 10.45% for 2013, 9.385% for 2012 and 9.24% for 2011.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 10 PENSION PLAN (CONTINUED):

Also, the Fund paid employer incidental death program contributions of approximately \$3,700, \$3,800, and \$3,900, at the rate of .15% of compensation for the current fiscal years ended June 30, 2013, 2012, and 2011 respectively.

As an alternative to membership to SCRS, newly hired State and school district employees may elect to participate in the State Optional Retirement Program (ORP), a defined contribution plan. The ORP was established in 1987 under Title 9, Chapter 20, of the South Carolina Code of Laws. State ORP participants direct the investment of their funds into a plan administered by one of four investment providers. The State assumes no liability for State ORP plan other than for payment of contributions to designated companies. To elect participation in the ORP, eligible employees must elect membership within their first 30 days of employment. Under State law, contributions to the ORP are required at the same rates as for the SCRS, 10.60% plus the retiree surcharge of 4.55% from the employer in fiscal year 2013. Of the 10.60% employer retirement contribution rate, the employer remits 5.00% directly to the participant's ORP account and the remaining 5.45% and .15% incidental death program contribution amounts are remitted to SCRS. For fiscal year 2013, total contributions requirements to the ORP were approximately \$28,000 (excluding the surcharge) from the Fund as employer and approximately \$18,000 from its employees as plan members.

The amounts paid by the Fund for pension, incidental death program, and accidental death program contributions are reported as employer contribution expenditures within the applicable functional 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 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.

For the current fiscal year, SCRS does not make separate measurements of assets and pension benefit obligations for individual employers within the cost-sharing plan. Under Title 9 of the South Carolina Code of Laws, the Fund's liability under the plans is limited to the amount of required employer contributions (stated as a percentage of covered payroll) as established by the South Carolina Public Employee Benefit Authority and as appropriated in the South Carolina Appropriation Act and from other applicable revenue sources. Accordingly, the Fund recognizes no contingent liability for unfunded costs associated with participation in the plan.

NOTE 11 POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS:

Plan Description

In accordance with the South Carolina Code of Laws and the annual Appropriations Act, the State provides post-employment health and dental and long-term disability benefits to retired State and school district employees and their covered dependents. The Fund contributes to the South Carolina Retiree Health Insurance Trust Fund (SCRHITF) and the South Carolina Long-Term Disability Insurance Trust Fund (SCLTDITF), cost-sharing multiple employer defined benefit postemployment healthcare, and long-term disability plans administered by the Insurance Benefits Division (IB), a part of the South Carolina Public Employee Benefit Authority (PEBA). Generally, retirees are eligible for the health and dental benefits if they have established at least ten years of retirement service credit. For new hires beginning employment May 2, 2008 and after, retirees are eligible for benefits if they have established 25 years of service for 100% employer funding and 15 through 24 years of service for 50% employer funding. Benefits become effective when the former employee retires under a State retirement system.

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 11 POSTEMPLOYMENT BENEFITS OTHER THAN PENSIONS (CONTINUED):

Basic Long-Term Disability (BLTD) benefits are provided to active state, public school district, and participating local government employees approved for disability.

Funding Policies

Section 1-11-710 of the South Carolina Code of Laws of 1976, as amended, requires these postemployment and long-term disability benefits be funded through annual appropriations by the General Assembly for active employees to the IB and participating retirees to the PEBA, except for the portion funded through the pension surcharge and provided from the other applicable sources of the IB, for its active employees who are not funded by State General Fund appropriations. Employers participating in the RMP are mandated by State statute to contribute at a rate assessed each year by the Office of the State Budget, 4.55% of annual covered payroll for 2013 and 4.30% of annual covered payroll for 2012. The IB sets the employer contribution rate based on a pay-as-you-go basis.

The Fund paid approximately \$124,000 and \$119,000 applicable to the surcharge included with the employer contribution for retirement benefits for the fiscal years ended June 30, 2013 and 2012, respectively. BLTD benefits are funded through a person's premium charged to State agencies, public school districts, and other participating local governments. The monthly premium per active employee paid to IB was \$3.22 for the fiscal years ended June 30, 2013 and 2012.

Effective May 1, 2008 the State established two trust funds through Act 195 for the purpose of funding and accounting for the employer costs of retiree health and dental insurance benefits and long-term disability insurance benefits. The SCRHITF is primarily funded through the payroll surcharge. Other sources of funding include additional State appropriated dollars, accumulated IB reserves, and income generated from investments. The SCLTDITF is primarily funded through investment income and employer contributions.

One may obtain complete financial statements for the benefit plans and the trust funds from PEBA Retirement Benefits and Insurance Benefits, 202 Arbor Lake Drive, Suite 360, Columbia, SC 29223.

NOTE 12 DEFERRED COMPENSATION PLANS:

Several optional deferred compensation plans are available to State employees and employers of its political subdivisions. Certain employees of the Fund have elected to participate. The multiple-employer plans, created under Internal Revenue Code Sections 457, 401 (k), and 403 (b), are administered by third parties and are not included in the CAFR of the State. Compensation deferred under the plans is placed in trust for the contributing employees. The State has no liability for losses under the plans. 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.

NOTE 13 OPERATING LEASES:

The Fund leases its office space and computers from an external party. The lease for the rental of office space expires on June 30, 2014 and the rental rate is \$23,876 per month. The two leases for computers expire on January 18, 2014 and February 8, 2014, and the rental rates are \$833 and \$2,168 per month, respectively. It also leases office equipment and vehicles under short-term and/or cancelable operating leases. 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. There were no minimum future rental obligations under noncancelable leases with a remaining term in excess of one year.

SOUTH CAROLINA STATE ACCIDENT FUND

**NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2013**

NOTE 13 OPERATING LEASES (CONTINUED):

Operating lease expenses for the fiscal year ended June 30, 2013 was approximately \$332,000.

NOTE 14 LONG-TERM LIABILITIES:

Long-term liability activity for the year ended June 30, 2013 was as follows:

	June 30, 2012	Additions	Reductions	June 30, 2013	Due within One year
Accrued compensated absences and related benefits	\$ 354,458	\$ 194,301	\$ (251,641)	\$ 297,118	\$ 251,641
Unpaid claims liability and claims adjustment expense payable	\$ 235,450,000	\$ 53,271,226	\$ (52,721,226)	\$ 236,000,000	\$ 78,524,394

NOTE 15 TRANSACTIONS WITH STATE ENTITIES:

The Fund has significant transactions with the State of South Carolina and various State agencies. Services received at no cost from State Agencies include maintenance of certain accounting records and payroll and disbursement processing from the Comptroller General's office; check preparation, banking, and investment functions from the State Treasurer; legal services from the Attorney General's office; and record storage for the Department of Archives and History. Other services received at no cost from the various divisions of the State Budget and Control Board include pension plan administration, insurance plans administration, audit services, personnel management, assistance in the preparation of the State Budget, property management and record keeping, review and approval of certain budget amendments, procurement services, and other centralized functions.

The Fund had financial transactions with various State Agencies during the year ended June 30, 2013. Significant payments were made to divisions of the State Budget and Control Board for pension and insurance plan contributions, vehicle rental, insurance coverage, office supplies, printing, telephone, interagency mail, and data processing services. Payments were also made for unemployment coverage for employees to the Department of Employment and Workforce. The amount of expenses applicable to these transactions is not readily determinable. The Fund provided no services free of charge to other State Agencies during the year ended June 30, 2013.

Total revenues from other State agencies based on the agency classification chart prepared by the South Carolina Comptroller General's Office are as follows:

General Government	\$ 2,554,480
Administration of Justice	15,763,202
Education	4,917,428
External	1,139,940
Higher Education	13,607,446
Health and Environment	10,102,690
Housing Authority	56,855
Resource and Economic Development	1,324,743
Social Services	1,678,686
Transportation	7,939,085
Unemployment Compensation	260,431
Other business Types	82,119
	<u>\$ 59,427,105</u>

SOUTH CAROLINA STATE ACCIDENT FUND

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2013

NOTE 15 TRANSACTIONS WITH STATE ENTITIES (CONTINUED):

During the fiscal year, the Fund received \$36,622 for reimbursements of claims expense from the State of South Carolina for claims prior to 1986. An additional \$14,369 was billed subsequent to June 30, 2013 for the last of fiscal year 2013 and is included in the claims recoveries and reimbursement receivables account on the balance sheet.

NOTE 16 NET LOSS/NET POSITION DEFICIT:

The Fund has a retained earnings deficit of approximately \$29,400,000. The deficit includes lost interest earnings through 1995. Prior to 1990, all investment income earnings of the Fund were credited to the General Fund of the State. For fiscal years 1991 and 1992, the Fund received one-third and two-thirds of the investment income. Section 42-7-75 of the South Carolina Code of Laws require the State Treasurer to deposit in the Fund's trust account monthly sufficient funds to pay expenses and claims required by law to be paid with the amount limited to the amount of investment income which the Fund would have earned since its inception if all investment earnings had been credited to the Fund. Estimates prepared by management in 1995 estimated that limit to be approximately \$12,300,000 assuming an interest rate of 4% to approximately \$20,600,000 using an interest rate of 6%.

NOTE 17 CONCENTRATIONS OF CREDIT RISK AND OTHER CONCENTRATIONS:

The Fund has reinsurance contracts with providers which share or limit the Fund's exposure to losses. However, should the reinsurance providers be unable to meet their obligations settlement of these amounts will ultimately be the responsibility of the South Carolina State Accident Fund. The Fund provides services to South Carolina governmental entities. The limited make-up of the membership group, as well as the limited geographic region in which the Fund operates, increases the Fund's exposure to business concentrations.

NOTE 18 SUBSEQUENT EVENTS

In accordance with SC Code of Laws Section 42-7-200, effective July 1, 2013, all functions within the Second Injury Fund related to the Uninsured Employers' Fund, including all allied, advisory, affiliated, or related entities, as well as the employees, funds, property, and all contractual rights and obligations associated with the Uninsured Employers' Fund, were transferred to the South Carolina Workers' Compensation Uninsured Employers' Fund, and all powers, duties, obligations, and responsibilities of the Second Injury Fund that relate to the Uninsured Employers' Fund were devolved upon the South Carolina Workers' Compensation Uninsured Employers' Fund in accordance with the State Budget and Control Board's plan for the closure of the Second Injury Fund. Effective July 1, 2013, the South Carolina Workers' Compensation Uninsured Employers' Fund was established within the office of the State Accident Fund. As of June 30, 2013, the Uninsured Employers' Fund had assets of approximately \$400,000, liabilities of approximately \$95,900,000, and a deficit net position of approximately \$95,500,000.

**INDEPENDENT AUDITOR'S REPORT ON INTERNAL CONTROL OVER FINANCIAL
REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT
OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH
GOVERNMENT AUDITING STANDARDS**

Mr. Richard H. Gilbert, Jr., CPA
Deputy State Auditor
State of South Carolina
Columbia, South Carolina

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards issued by the Comptroller General of the United States, the financial statements of the South Carolina State Accident Fund ("the Fund") as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements and have issued our report thereon dated October 7, 2013.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Fund's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of the Fund's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies, and therefore, material weaknesses or significant deficiencies may exist that were not identified. However, as described in the accompanying schedule of findings, we identified a certain deficiency in internal control that we consider to be a material weakness.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings as item 2013-1 to be a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Fund's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under Government Auditing Standards.

The Fund's Response to Findings

The Fund's response to the findings identified in our audit is described in Appendix A. The Fund's response was not subjected to the auditing procedures applied in the audit of the financial statements and, accordingly, we express no opinion on it.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with Government Auditing Standards in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Rogers Lalan, PA

October 7, 2013

SOUTH CAROLINA STATE ACCIDENT FUND

SCHEDULE OF FINDINGS

JUNE 30, 2013

2013-1 Deficiencies Noted in Financial Records and Statements

Condition: Our audit disclosed deficiencies in the preparation of the financial statements and the recording of transactions in the books of the Fund. The deficiencies are described as follows:

1. The workpaper prepared by the Fund to estimate the adjustments related to premium audits not performed as of year-end was incorrect. The Fund did not use the correct amounts to calculate the estimated adjustments causing an overstatement of revenues of approximately \$1,100,000, an understatement of receivables of approximately \$125,000, and an understatement of liabilities of approximately \$1,225,000.
2. The Fund did not reconcile the operating cash recorded on their books to the South Carolina Enterprise Information System (SCEIS) and to the State Treasurer's Office cash balances. As a result, cash was overstated by approximately \$7,000, accounts payable was overstated by approximately \$3,000, and expenses were understated by approximately \$4,000.

Cause: There was no separate review by someone other than the preparer for the figures used to calculate the adjustments related to premium audits not performed as of year-end. Fund personnel did not reconcile the operating cash account to SCEIS and the State Treasurer's Office cash balances.

Effect: Procedures in place by the Fund did not detect items that caused the financial records to be inaccurate.

Criteria: Generally accepted accounting principles require that all transactions be properly recorded and good internal control procedures require procedures to be in place to detect errors.

Recommendation: The Fund should implement procedures to ensure that all information used to prepare the financial statements is accurate and that documentation exists to support the estimated adjustments related to premium audits not performed as of year-end. The Fund should ensure that all information reported in the financial statements including the notes is accurately stated in accordance with generally accepted accounting principles.

SOUTH CAROLINA STATE ACCIDENT FUND

STATUS OF PRIOR FINDINGS

JUNE 30, 2013

During our current audit, we reviewed the status of action taken on the findings we reported on our report on the financial statements of the Fund dated October 12, 2012 resulting from the audit of the financial statements for the year ended June 30, 2012. The following findings were reported:

2012-1 Deficiencies Noted in Financial Records and Statements

2012-2 Error in Calculation of Claims Payments

Note that the finding listed above as 2012-2 was corrected. The finding listed above as 2012-1 was repeated in the current year.

MANAGEMENT'S RESPONSE

APPENDIX A

State Accident Fund's Response to Findings

2013 – 1 Deficiencies Noted in Financial Records and Statements

1. The workpaper as initially prepared should have been presented as a “draft”. The Fund continued work on the workpaper making revisions and corrections as it was reviewed to ensure accuracy until the final correct report was presented to the audit team.
2. As a state agency, the Fund must utilize reports from SCEIS. The “finding” references an inaccurate report received from SCEIS. In the future, the Fund will attempt to work more closely with SCEIS to ensure that its reports are accurate. The report of the State Treasurer's Office referenced in the “finding” is not, however, provided to the Fund, thereby, making the suggested reconciliation an unlikely solution.