

SOUTH CAROLINA STATE ACCIDENT FUND

COLUMBIA, SOUTH CAROLINA

**FINANCIAL STATEMENTS,
REQUIRED SUPPLEMENTARY INFORMATION,
AND INDEPENDENT AUDITORS' REPORT**

YEAR ENDED JUNE 30, 1999



Office of the State Auditor

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December 16, 1999

The Honorable James H. Hodges, Governor
and
Mr. Irvin D. Parker, 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, 1999, was issued by Cherry, Bekaert, & Holland, LLP, Certified Public Accountants, under contract with the South Carolina Office of the State Auditor.

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

Respectfully submitted,


Thomas L. Wagner, Jr., CPA
State Auditor

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Independent Auditors' Report

Office of the State Auditor
Columbia, South Carolina

We have audited the accompanying balance sheet of the South Carolina State Accident Fund (the Fund) as of June 30, 1999 and the related statements of revenues, expenses, and changes in retained earnings, and cash flows for the year then ended. These financial statements are the responsibility of the Fund's management. Our responsibility is to express an opinion on these financial statements based on our audit. The financial statements of the South Carolina State Accident Fund as of and for the year ended June 30, 1998 were audited by other auditors whose report dated September 11, 1998, expressed an unqualified opinion on those statements.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

As discussed in Notes 1 and 2 the financial statements present only the South Carolina State Accident Fund, an internal service fund, and are not intended to present fairly the financial position of the State of South Carolina primary government or financial reporting entity and the results of its operations and cash flows of its proprietary fund types in conformity with generally accepted accounting principles.

In our opinion, the financial statements referred to in the first paragraph present fairly, in all material respects, the financial position of the South Carolina State Accident Fund as of June 30, 1999 and the results of its operations and cash flows for the year then ended, in conformity with generally accepted accounting principles.

The Year 2000 Issues on pages 21 and 22 is not a required part of the financial statements but is supplementary information required by the Governmental Accounting Standards Board, and we did not audit the information and do not express an opinion on such information. Further we were unable to apply to the information certain procedures prescribed by professional standards because of the unprecedented nature of the year 2000 issue, its effects, the fact that authoritative measurement criteria regarding the status of remediation efforts have not been established, and the success of remediation efforts will not be fully determinable until the year 2000 and after and because insufficient evidence exists to support disclosures. In addition, we do not provide assurance that the South Carolina State Accident Fund is or will become Year 2000 compliant or that the Fund's remediation efforts will be successful in whole or in part, or that parties with which the South Carolina State Accident Fund does business are or will become Year 2000 compliant.

Florence, South Carolina
October 15, 1999

FINANCIAL STATEMENTS

SOUTH CAROLINA STATE ACCIDENT FUND

BALANCE SHEETS, JUNE 30, 1999 AND 1998

ASSETS

	<u>1999</u>	<u>1998</u>
Current Assets:		
Cash and cash equivalents	\$38,815,838	\$50,349,109
Premiums receivable, net of allowance for uncollectible accounts of \$381,703 in 1999 and \$379,945 in 1998	16,700,299	20,277,766
Claims recoveries and reimbursement receivables	678,450	206,978
Recoverable under reinsurance annuity contract	159,616	-
Accrued interest receivable	<u>304,594</u>	<u>458,743</u>
Total current assets	<u>56,658,797</u>	<u>71,292,596</u>
Property and Equipment:		
Computer and technical equipment	9,839,098	9,259,191
Office furniture and equipment	<u>348,576</u>	<u>347,400</u>
Total	10,187,674	9,606,591
Less: Accumulated depreciation	<u>2,160,979</u>	<u>1,176,467</u>
Net property and equipment	<u>8,026,695</u>	<u>8,430,124</u>
Other Assets:		
Investment in reinsurance annuity contract	1,282,294	-
Less: Accumulated amortization	<u>37,679</u>	<u>-</u>
Other assets net of accumulated amortization	<u>1,244,615</u>	<u>-</u>
Total assets	<u>\$65,930,107</u>	<u>\$79,722,720</u>

LIABILITIES AND FUND EQUITY

Current Liabilities:		
Accounts payable	\$ 568,479	\$ 1,678,953
Accrued compensated absences and related benefits	340,698	305,496
Accrued payroll and related liabilities	290,278	277,530
Accrued refundable premiums	522,228	125,109
Deferred premium revenue	12,761,613	17,761,533
Funds held in escrow	768,244	545,015
Unpaid claims liability and claims adjustment expenses payable within one year - net	24,090,000	25,178,000
Less: Amounts recoverable from the State of South Carolina	<u>(572,200)</u>	<u>(399,000)</u>
Total current liabilities	<u>38,769,340</u>	<u>45,472,636</u>
Noncurrent Liabilities:		
Unpaid claims liability and claims adjustment expenses payable beyond one year - net	27,099,000	26,148,000
Less: Amounts recoverable from the State of South Carolina	<u>(10,800)</u>	<u>(18,000)</u>
Total noncurrent liabilities	<u>27,088,200</u>	<u>26,130,000</u>
Total liabilities	65,857,540	71,602,636
Fund Equity:		
Retained earnings	<u>72,567</u>	<u>8,120,084</u>
Total liabilities and fund equity	<u>\$65,930,107</u>	<u>\$79,722,720</u>

SOUTH CAROLINA STATE ACCIDENT FUND

STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN RETAINED EARNINGS

FOR THE YEARS ENDED JUNE 30, 1999 AND 1998

	1999	1998
OPERATING REVENUES		
Premiums	\$35,090,236	\$39,282,056
Interest income	2,415,599	3,257,321
Registration fees	-	920
Total operating revenues	<u>37,505,835</u>	<u>42,540,297</u>
OPERATING EXPENSES:		
Claims expense	<u>30,670,183</u>	<u>26,061,651</u>
Administrative expenses:		
Second Injury Fund assessment	5,586,494	5,794,617
Personal services and employee benefits	3,511,693	3,310,715
Contractual services	980,425	1,082,175
Rent and insurance	342,848	366,305
Supplies and materials	255,491	180,477
Bad debts	57,828	366,578
Depreciation	1,008,985	638,156
Travel	83,926	-
Actuarial audit fee	30,000	-
Other	-	116,039
Total administrative expenses	<u>11,857,690</u>	<u>11,855,062</u>
Total operating expenses	<u>42,527,873</u>	<u>37,916,713</u>
OPERATING INCOME (LOSS)	<u>(5,022,038)</u>	<u>4,623,584</u>
NONOPERATING REVENUES (EXPENSES)		
Amortization expense – reinsurance annuity contract premium	(37,679)	-
Gain (loss) on sale of property and equipment	<u>12,200</u>	<u>(20,466)</u>
Total nonoperating revenues (expenses)	<u>(25,479)</u>	<u>(20,466)</u>
INCOME (LOSS) BEFORE TRANSFER	(5,047,517)	4,603,118
TRANSFER TO PRIMARY GOVERNMENT	<u>(3,000,000)</u>	-
NET INCOME (LOSS)	(8,047,517)	4,603,118
RETAINED EARNINGS AT BEGINNING OF YEAR	<u>8,120,084</u>	<u>3,516,966</u>
RETAINED EARNINGS AT END OF YEAR	<u>\$ 72,567</u>	<u>\$ 8,120,084</u>

SOUTH CAROLINA STATE ACCIDENT FUND

STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 1999 AND 1998

	<u>1999</u>	<u>1998</u>
CASH FLOWS FROM OPERATING ACTIVITIES:		
Operating income (loss)	\$ (5,022,038)	\$ 4,623,584
Adjustment to reconcile operating income (loss) to net cash used by operating activities:		
Depreciation expense	1,008,985	638,156
Provision for bad debts	1,758	147,990
Acquisition of reinsurance annuity contract	(1,282,294)	-
Changes in assets and liabilities:		
Decrease in premiums receivable	3,575,709	16,025,145
(Increase) decrease in claims recoveries and reimbursement receivable	(501,562)	955,611
(Increase) decrease in recoverable under reinsurance annuity contract	(159,616)	-
Reclassification of interest income to investing activities	(2,415,599)	(3,257,321)
Increase (decrease) in accounts payable	(1,110,474)	70,053
Increase in accrued compensated absences and related benefits	35,202	39,623
Increase in accrued payroll and related benefits	12,748	22,876
Increase (decrease) in accrued refundable premiums	397,119	(1,173,832)
Increase (decrease) in deferred premium revenue	(4,999,920)	(16,578,591)
Increase in funds held in escrow	223,229	315,689
(Decrease) in estimate of unpaid claims liability, net of amounts recoverable from the State of South Carolina	<u>(303,000)</u>	<u>(6,634,000)</u>
Total adjustments	<u>(5,517,715)</u>	<u>(9,428,601)</u>
Net cash (used) by operating activities	<u>(10,539,753)</u>	<u>(4,805,017)</u>
CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES		
Transfers to primary government	<u>(3,000,000)</u>	-
Net cash (used) by non-capital financing activities	<u>(3,000,000)</u>	-
CASH FLOW FROM CAPITAL AND RELATED FINANCING ACTIVITIES		
Proceeds from sale of property and equipment	12,200	3,225
Acquisition of capital assets	<u>(605,556)</u>	<u>(4,519,526)</u>
Net cash used by capital and related financing activities	<u>(593,356)</u>	<u>(4,516,301)</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds received under reinsurance annuity contract	30,090	
Interest received on deposits	<u>2,569,748</u>	<u>3,491,050</u>
Net cash provided by investing activities	<u>2,599,838</u>	<u>3,491,050</u>
Net (decrease) in cash and cash equivalents	(11,533,271)	(5,830,268)
Cash and cash equivalents at beginning of year	<u>50,349,109</u>	<u>56,179,377</u>
Cash and cash equivalents at end of year	<u>\$38,815,838</u>	<u>\$50,349,109</u>

Supplemental Disclosure:

Noncash capital and related financing activities:

The cost of equipment disposed of was \$24,474 in 1999 and \$48,166 in 1998 and accumulated depreciation on this equipment was \$24,474 in 1999 and \$24,475 in 1998.

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 1 – Reporting Entity

The South Carolina State Accident Fund (the 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 Commission 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 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 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.

Note 2 – Summary of Significant Accounting Policies

Fund Accounting – The South Carolina state government uses funds and account groups 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 entities 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 by one department or agency of a governmental unit to others on a cost reimbursement basis.

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 as well as all applicable FASB pronouncements issued on or before November 30, 1989 not in conflict with GASB standards.

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 2 – Summary of Significant Accounting Policies (continued)

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.

Because the internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements, certain corporate bonds.

The State’s internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each fund’s equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. 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 has a general deposit account and two special deposit accounts. 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 income receivable of the pool. Reported interest income includes interest earnings, realized gains/losses and unrealized gains/losses on investments in the pool arising from changes in fair value. Realized gains and losses are allocated daily and are included in the accumulated income receivable. Unrealized gains and losses are allocated at year-end based on the percentage ownership in the pool.

Although the cash management pool includes some long-term investments, it operates as a demand deposit account, therefore, for credit risk information pertaining to the cash management pool, see the deposits disclosures in Note 4.

Allowance For Uncollectible Accounts – The allowance for uncollectible accounts is estimated by management as 2% of year-end premium receivables from municipalities and counties as well as specific identification of certain accounts. No allowance is recorded for billed premiums for future years not yet earned.

Property and Equipment – Property and equipment are recorded at cost. As a general rule, items with a cost in excess of \$400 and a useful life of at least two years are capitalized. Cost of assets acquired under long-term contracts are capitalized as incurred. Depreciation is provided using the straight-line method over the useful lives of the related assets and begins at the time the asset is placed in service.

Major classifications of property and equipment and related useful lives are summarized as follows:

Computer and technical equipment	2-10 years
Office furniture and equipment	2-20 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 but not administrative 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

SOUTH CAROLINA STATE ACCIDENT FUND
Notes to Financial Statements
June 30, 1999 and 1998

Note 2 – Summary of Significant Accounting Policies (continued)

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 DOT claims prior to January 1, 1994, are not included in the State Accident Fund's claims liability. See below and Note 5 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 periodically 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.

Prior to July 1, 1998 the Fund acted as a claims servicer with respect to claims incurred by the Department of Transportation prior to January 1, 1994 and the Department of Public Safety prior to August 1, 1993. For the year ended June 30, 1999 the General Assembly required the State Accident Fund to purchase an annuity for the purpose of funding the future obligation for workers compensation claims filed prior to restructuring by Department of Highways and Public Transportation employees. As stated above prior to July 1, 1999 the Fund acted as a claims servicer with respect to claims incurred by the Department of Transportation prior to January 1, 1994 and the Department of Public Safety prior to August 1, 1993. Risk of loss for those periods was retained by the Department of Transportation. The Fund received full reimbursement of claims paid, including an amount for administrative costs. The Fund paid \$334,365 in claims during the year ended June 30, 1999 for claims incurred prior to June 30, 1998. After June 30, 1998 workers compensation claims from these agencies are be paid from funds received from the annuity purchased. Risk of loss on these claims became the responsibility of the State Accident Fund. The Fund's administrative costs are no longer reimbursed under the annuity. See Note 14 for additional information.

Reinsurance – The Fund has obtained reinsurance coverage to reduce its exposure to catastrophic losses on insured events. Losses from an insured event are covered up to \$45 million, with the Fund retaining the risk for the first \$5 million of loss. Coverage is limited to \$2 million per individual. Reinsurance permits recovery of portion of losses from reinsures, 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. There were no amounts due from reinsurers at June 30, 1999 or 1998. The reinsurance contract covers a three year period with the premiums paid annually. The coverage period runs from July 1 to June 30.

Funds Held in Escrow – The Fund has established an escrow account to maintain accountability for funds received in settlement of third party reimbursable claims until final disposition of the case has been determined. The funds are deposited in this account upon receipt and recorded as a liability. Upon disposition of the case, the funds are transferred to the trust deposit account and recorded as a reduction of claims expense.

Recognition of Premium 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

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 2 – Summary of Significant Accounting Policies (continued)

determined based on actual payrolls for the policy period which are in excess of estimated premiums billed which were based on estimated payroll costs.

A receivable is recorded at the time a premium is billed. 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 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 General Assembly enacts the budget through passage of specific line-item appropriations by program within budgetary unit, within budgetary fund category, State 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 authority or by the agency as set forth in the 1999 Appropriations Act proviso 72.14 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. Agencies may charge vendor, interagency, and interfund payments for fiscal year 1999 to 1999 appropriations in July. 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 current Appropriations Act states that the General Assembly intends to appropriate all monies to operate State government for the current fiscal year. 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 generally accepted accounting principles applicable to proprietary fund types, 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 State's internal cash management 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

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 2 – Summary of Significant Accounting Policies (continued)

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 applicable personal services and employee benefits expense category.

Use of Estimates – The preparation of financial statements in conformity with generally accepted accounting principles 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.

Investment in Reinsurance Annuity Contract – As more fully explained in Note 5 under the 1993 Restructuring Act, the Department of Transportation and the Department of Public Safety were created and were charged with responsibilities of the former Department of Highways and Public Transportation effective July 1, 1993. Section 44.4 of the 1998-1999 Appropriation Act passed by the General Assembly required the State Accident 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. This annuity is being amortized over the life of the contract in proportion to annuity proceeds received.

Note 3 – 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. There were no significant reductions in insurance coverage from prior years. The cost of settled claims and claim losses have not exceeded this coverage in any of the past four 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 Employment Security Commission;
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 Office of Insurance Services; and
4. Claims of covered public employees for long-term disability and group-life insurance benefits. This type of claim is handled through the Office of Insurance Services.

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

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 3 – Risk Management (continued)

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 obtains coverage through a commercial insurer for employee fidelity bond insurance for all employees for losses arising from theft or misappropriation.

The Fund has not transferred the portion of the risk of loss related to insurance policy deductibles for its property contents, general torts, and fidelity bond coverage’s to a State or commercial insurer. There were no expenses incurred for the years ended June 30, 1999 and 1998 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, 1999, 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, 1999, 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 4 – Deposits

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, certain funds used to pay claims are on deposit with financial institutions.

The following schedule reconciles deposits within the footnotes to the balance sheet amounts:

<u>Balance Sheet</u>		<u>Footnotes</u>	
Cash and cash equivalents	\$38,815,838	Deposits Held by State Treasurer	\$38,915,534
	_____	Other deposits (overdraft)	____(99,696)
	<u>\$38,815,838</u>		<u>\$38,815,838</u>

At June 30, 1999 the bank balance was \$404,566 and the amount reported in the financial statements is \$(99,696). The entire amount was either covered by insurance or collateralized with securities held by the Fund, or by its agent in the Fund’s name.

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 4 – Deposits (continued)

State law requires full collateralization of all State Treasurer's bank balances. The State Treasurer must correct any deficiencies in collateral within seven days. At June 30, 1999 and 1998, all of the State Treasurer bank balances were fully insured or collateralized with securities held by the State or by its agents in the State's name. At June 30, 1999 all of the State Accident Fund's bank balances were fully insured or collateralized with securities held by the Fund or by its agents in the Fund's name. With respect to investments in the State's cash management pool, all of the State Treasurer's investments are insured or registered or are investments for which the securities are held by the State or its agents in the State's name. Information pertaining to the carrying amounts, market values, and credit risk of the State Treasurer's investments is disclosed in the Comprehensive Annual Financial Report of the State of South Carolina.

Note 5 – Investment in Reinsurance Annuity Contract

Under the 1993 Restructuring Act, the Department of Transportation and the Department of Public Safety were created and were charged with responsibilities of the former Department of Highways and Public Transportation effective July 1, 1993. Section 44.4 of the 1998-1999 Appropriation Act passed by the General Assembly required the State Accident 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.

At July 1, 1998 estimated liability for these claims was \$2,048,000. The estimated liability at June 30, 1999 was \$1,988,000. While the State believes the annuity will provide funding adequate to cover this liability, the Fund has ultimate responsibility to pay these claim should the annuity funding be inadequate. On March 11, 1999 the State Accident 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, 1999 the Fund paid \$189,708 of Department of Transportation claims covered by this annuity. They received reimbursement of \$30,091 under this contract for the year ended June 30, 1999. The amount \$159,616, shown on the balance sheet as recoverable under reinsurance annuity contract, represents amount due under the annuity that will be collected in the year ending June 30, 2000. 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 liability for these claims is not reported by either the State Accident Fund or the Department of Transportation because the State of South Carolina 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, 1999 was \$37,679 and is included as amortization expense in the nonoperating section of the statement of revenues, expenses, and changes in retained earnings. The Department of Transportation no longer reimburses the Fund for administrative costs.

Note 6 – Premiums Receivable

Premium receivable consist of amounts receivable from/for the following:

	<u>1999</u>	<u>1998</u>
County governments and agencies	\$ 1,516,343	\$ 1,251,838
Municipal governments and agencies	<u>417,380</u>	<u>410,681</u>
Total	1,933,723	1,662,519
Less, allowance for uncollectible accounts	<u>(381,703)</u>	<u>(379,945)</u>
Total	1,552,020	1,282,574
State agencies	2,966,584	2,812,644
Billed premiums for future periods not yet earned	<u>12,181,695</u>	<u>16,182,548</u>
Total	<u>\$16,700,299</u>	<u>\$20,277,766</u>

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 6 – Premiums Receivable (continued)

Included in premium receivable and premium revenue is \$1,072,947 and \$844,694 receivable from policyholders for premium adjustments at June 30, 1999 and 1998, respectively (see Note 7). Of these amounts, \$881,561 and \$402,741 was due from state agencies at June 30, 1999 and 1998, respectively.

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 amounts the Fund owed policyholders for estimated premiums in excess of actual adjusted premiums at June 30, 1999 and 1998 were \$522,228 and \$125,109 respectively, for those county and municipal policyholders who elected to receive a refund check. In addition, for State agencies whose estimated premiums exceed the actual adjusted premiums, credits of \$371,589 and \$43,060 at June 30, 1999 and 1998 were applied to premiums receivable to reduce future billings. Premium adjustments for additional amounts due from policyholders for actual premiums in excess of the estimated billings are reported as a component of premium receivables and disclosed in Note 6. Each county and municipal policyholder chooses to either receive a check from the Fund or to have the credit adjustment reduce their next premium bill. For amounts due to policyholders who elect to reduce premiums, such amounts were applied against those respective premiums receivable. Amounts due to policyholders at year end represent policyholders with net credit balances or those who elect to receive a refund. Adjustments owed to state agencies are used to reduce future payments. The account title was changed from the prior year to better reflect the liability nature of the account.

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 of South Carolina when the claims are paid. Estimated amounts recoverable from subrogation have been deducted from the claims liability. The amount accrued for unpaid claims liability and claims adjustment expenses is as follows:

	<u>1999</u>	<u>1998</u>
Unpaid claims liability and claim adjustment expenses at beginning of year	\$ <u>50,909,000</u>	\$ <u>57,543,000</u>
Incurring claims and claims adjustment expense:		
Provision for insured events – current year	33,495,000	32,278,651
Changes in provision for insured events – prior years	<u>(2,824,817)</u>	<u>(6,634,000)</u>
Total incurred claims and claims adjustment expenses	<u>30,670,183</u>	<u>25,644,651</u>
Claims paid or payable:		
Claims and claims adjustment expenses attributable to insured events of the current year	(8,056,000)	(9,294,000)
Claims and claims adjustment expenses attributable to insured events of the prior years	<u>(22,917,183)</u>	<u>(22,984,651)</u>
Total claims paid or payable	<u>(30,973,183)</u>	<u>(32,278,651)</u>
Total unpaid claims liability and claim adjustment expenses at end of year	50,606,000	50,909,000
Less: Short-term portion	<u>(23,517,800)</u>	<u>(24,779,000)</u>
Long-term portion	<u>\$ 27,088,200</u>	<u>\$ 26,130,000</u>

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 8 – Unpaid Claims Liability and Claims Adjustment Expenses (continued)

This claim liability is further categorized as follows:

Claims reported and/or payable:		
State agencies	\$ 25,300,000	\$ 15,669,000
Counties and municipalities	<u>6,315,000</u>	<u>5,178,000</u>
Total	<u>31,615,000</u>	<u>20,847,000</u>
Claims incurred but not reported:		
State agencies	15,488,000	23,332,000
Counties and municipalities	<u>3,503,000</u>	<u>6,730,000</u>
Total	<u>18,991,000</u>	<u>30,062,000</u>
Total claims liability	<u>\$ 50,606,000</u>	<u>\$ 50,909,000</u>
Claims reported and/or payable:		
Short-term	\$ 15,586,000	\$ 10,147,000
Long-term	<u>16,029,000</u>	<u>10,708,000</u>
Total	<u>31,615,000</u>	<u>20,847,000</u>
Claims incurred but not reported:		
Short-term	9,628,000	14,632,000
Long-term	<u>9,363,000</u>	<u>15,430,000</u>
Total	<u>18,991,000</u>	<u>30,062,000</u>
Total unpaid claims liability and claims adjustment expense	<u>\$ 50,606,000</u>	<u>\$ 50,909,000</u>

Note 9 – Second Injury Fund Assessment

The Fund is required to pay an annual assessment to the Second Injury Fund of the State of South Carolina. 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 years 1999 and 1998 was \$5,586,494 and \$5,794,617 respectively.

Note 10 – Pension Plan

The South Carolina Retirement Division maintains four independent defined benefit plans and issues its own publicly available Comprehensive Annual Financial Report (CAFR) which includes financial statements and required supplementary information. A copy of the separately issued CAFR may be obtained by writing to the South Carolina Retirement System, 202 Arbor Lake Drive, Columbia, South Carolina, 29223. Furthermore, The Retirement System and the four pension plans are included in the CAFR of the State of South Carolina.

SOUTH CAROLINA STATE ACCIDENT FUND
Notes to Financial Statements
June 30, 1999 and 1998

Note 10 – Pension Plan (continued)

Substantially all employees of the Fund are covered by a pension plan through the South Carolina Retirement System (SCRS), a cost sharing multiple-employer defined benefit pension plan administered by the Retirement Division of the State Budget and Control Board, a public employee retirement system (PERS). Generally, all State employees are required to participate in and contribute to the System as a condition of employment unless exempted by law as provided in Section 9-1-480 of the South Carolina Code of Laws. This plan provides annuity benefits as well as disability, cost of living adjustment, death and group-life insurance benefits to eligible employees and retirees.

Under the SCRS, employees are eligible for a full service retirement annuity upon reaching age sixty-five or completion of thirty years service regardless of age. The benefit formula for full benefits effective since July 1, 1989, for the System is 1.82% of an employees average final compensation multiplied by the number of years of credited service. Early retirement options with reduced benefits are available as early as age fifty five. Employees are vested for a deferred annuity after five years credited service. Disability annuity benefits are payable to employees totally and permanently disabled provided they have a minimum of five years credited service. A group-life insurance benefit equal to an employee's annual rate of compensation is payable upon the death of an active employee with a minimum of one year credited service.

Since July 1, 1988, employees participating in the SCRS have been required to contribute six percent of all compensation. Effective July 1, 1997, the employer contribution rate became 9.466% which included a 1.916% surcharge to fund retiree health and dental insurance coverage. Effective July 1, 1998, the employer contribution rate became 9.580%, which includes a 2.030% surcharge to fund retiree and dental insurance coverage. The Fund's actual contributions to the SCRS for the years ended June 30, 1999, 1998, and 1997 were \$265,894, \$242,754, and \$193,447 respectfully, and equaled the required contributions of 7.55% (excluding the surcharge) for each year. Also, the Fund paid employer group life insurance contributions of \$4,163 and \$3,847 for the years ended June 30, 1999 and 1998, respectfully, at the rate of .15% of compensation.

The amounts paid by the Fund for pension, group-life, and post-retirement benefits are included as personal services expenses.

Article X, Section 16, of the South Carolina Constitution requires that all State-operated retirement systems be fund on a sound actuarial basis. Title Nine of the South Carolina Code of Laws of 1976, as amended, prescribes requirements relating to membership, benefits, and employee/employer contributions for each pension plan. 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. Annual benefits, payable monthly for life, are based on length of service and an average final compensation (an annualized average of the employee's highest twelve consecutive quarters of compensation).

The System does not make separate measurements of assets and pension benefit obligations for individual employers. Under Title Nine of the South Carolina Code of Laws, the Fund's liability under the plan is limited to the amount of contributions (stated as a percentage of covered payroll) established by the State Budget and Control Board. Therefore, the Fund's liability under the pension plan is limited to the contribution requirements for the applicable year from amounts appropriated therefor in the South Carolina Appropriations Act and amounts from other applicable revenue sources. Accordingly, the Fund recognizes no contingent liability for unfunded costs associated with participation in the plan. All required contributions due to the plan were met.

At retirement, employees participating in the SCRS receive additional service credit (at a rate of twenty days equals one month of service) for up to ninety days of accumulated unused sick leave.

SOUTH CAROLINA STATE ACCIDENT FUND
Notes to Financial Statements
June 30, 1999 and 1998

Note 11 – Post-Employment and Other Employee Benefits:

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

These benefits are provided through annual appropriations, by the General Assembly, to the Fund for its active employees and to the State Budget and Control Board for all participating State retirees except the portions funded through the pension surcharge and provided from other applicable revenue sources of the Fund for its active employees who are not funded by State General Fund appropriations. The State finances health and dental plan benefits on a pay-as-you-go basis. Currently, approximately 19,170 State retirees meet these eligibility requirements.

The Fund recorded employer contributions expenses applicable to these benefits for active employees in the amount of \$180,238 and \$172,107 for the years ended June 30, 1999 and 1998 respectively, included with the employer contributions for retirement benefits. These amounts were remitted to the South Carolina Retirement Systems for distribution to the Division of Insurance Services for health and dental insurance benefits.

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

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

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 the Internal Revenue Code Sections 457, 401(k), and 403(b) are administered by third parties and are not included in the Comprehensive Annual Financial Report of the State of South Carolina. Compensation deferred under the plans is placed in trust for the contributing employee. 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.

On August 20, 1996 the provisions of Internal Revenue Code Section 457 were amended by adding subsection (g). That subsection provides that new plans will not be considered eligible plans unless all assets and income of the plans are held in trust for the exclusive benefit of the participants and their beneficiaries. Existing plans also had to comply with this requirement by January 1, 1999. South Carolina's plan adopted this change effective July 27, 1998.

SOUTH CAROLINA STATE ACCIDENT FUND
Notes to Financial Statements
June 30, 1999 and 1998

Note 13 – Operating Leases:

The Fund's noncancelable operating leases having remaining terms of more than one year expire in fiscal year ending June 30, 2002. The Fund is obligated under an operating lease for the rental of office space. The lease contains a renewal option for one year at the same terms and conditions, except that the rental rate shall be negotiated. 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. Minimum future rental obligations under this non-cancelable lease are as follows:

Fiscal Year Ended June 30,	Amount
2000	\$ 262,452
2001	262,452
2002	<u>262,452</u>
Total minimum obligations	\$ <u>787,356</u>

The Fund is not obligated under any non-cancelable operating leases for the rental of office equipment that have remaining terms in excess of one year from June 30, 1999.

Operating lease expenses for the fiscal years ended June 30, 1999 and 1998, were \$258,361 and \$277,370, respectively, for office space and \$13,820 and \$19,770, respectively, for office equipment and vehicles. The Fund reports these costs in the applicable functional expense categories.

Note 14 – 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 years ended June 30, 1999 and 1998. 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 Employment Security Commission. The amounts of 1999 and 1998 expenditures applicable to these transactions are not readily determinable.

The Fund provided no services free of charge to other State Agencies during the years ended June 30, 1999 and 1998; however, the Fund provided worker's compensation coverage to all State Agencies for a fee. Premium revenue from State Agencies during the years ended June 30 1999 and 1998 was \$25,052,235 and \$30,570,166, respectively.

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 14 – Transactions With State Entities: (continued)

As discussed in Notes 2, 5 and 6 the Fund acts as a claims servicer for certain agencies prior to their participation in the Fund and receives recoveries from the State for State Agency claims prior to July 1, 1986, when the claims are paid. The recoveries due from the State are recorded net of any third party or Second Injury Fund recoveries and, therefore, may result in an amount due to the State of South Carolina. These amounts are netted on the balance sheet. Amounts receivable or payable at June 30 for reimbursement of and recoveries for claims paid are as follows:

	<u>1999</u>	<u>1998</u>
Due from the State of South Carolina	\$ 24,975	\$ 19,033
Due from the Department of Transportation	\$ -	\$ 38,162

Claims paid during the years ended June 30, 1999 and 1998 for which reimbursement or recoveries were due from various State Agencies are as follows:

	<u>1999</u>	<u>1998</u>
Due from the State of South Carolina	\$ 62,840	\$ 65,187
Due from the Department of Transportation	\$334,365	\$ 50,672

As disclosed in Note 5 the Fund purchased an annuity for the purpose of funding future obligations for workers compensation claims filed prior to restructuring of the Department of Transportation employees. During the year ended June 30, 1999 the Department of Transportation paid \$334,365 to the Fund for claims payments. The amounts paid or payable from the Department of Transportation include an assessment of 7.8% for the unallocated expenses for the year ended June 30, 1998.

Note 15 – Operating Loss

The State Accident Fund's net loss was caused in part by a one time transfer of \$ 3,000,000 in investment income to the State of South Carolina's general Fund as required by Proviso 44.5 of the 1999 Appropriation Act. The proviso required the State Accident Fund to transfer to the State General Fund interest earned or accruing on monies in the State Accident Fund. The statement of revenues, expenses, and changes in retained earnings shows a net loss in excess of \$ 8,000,000 and an operating loss in excess of \$5,000,000 for the year ended June 30, 1999. The transfer of money to the general fund will not be required for the year ending June 30, 2000. Management reviews rates during November and December. If a rate increase is determined to be necessary it would take effect January 1st. Management felt it could not raise rate on January 1, 1999 because the National Council on Compensation Insurance had filed for a five percent rate decrease. For the year ending June 30, 2000 management reviewed rates with the Fund actuary in order to determine if a rate increase was necessary. Based on this review the Fund has realigned rates by rate class. In some classes rates were increased and in others they were decreased. The Fund further automated its claims processing procedures. While this caused an increase in expenses for the year ended June 30, 1999, the Fund feels expenses will be reduced in future years as employees retire or leave the Fund. Some of the employees will not be replaced.

SOUTH CAROLINA STATE ACCIDENT FUND

Notes to Financial Statements

June 30, 1999 and 1998

Note 16 – 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 17 – Reclassification of 1998 Amounts

During fiscal year 1999 the Fund reclassified certain 1998 balances, where appropriate, to correspond with the 1999 financial statement presentation. Below is a summary of the effects of the changes as of and for the year ended June 30, 1998.

Recognition of Interest Income as Operating Revenue – For the year ended June 30, 1998 \$3,257,321 was reported in the financial statements as nonoperating revenue. This has been reclassified in the operating revenue section of the Statements of Revenues, Expenses and Changes in Retained Earnings to better reflect the nature of the transactions.

Recognition of Loss on Sale of Property and Equipment - For the year ended June 30, 1998 \$20,466 was reported in the financial statements as an operating expense. This has been reclassified in the nonoperating revenue (expense) section of the Statements of Revenues, Expenses and Changes in Retained Earnings to better reflect the nature of the transactions.

Change in Premium Receivables – For the year ended June 30, 1998 the change in premium receivable and bad debts were reported using net amounts. The amounts have been reclassified and reported at gross amounts.

Statement of Revenues, Expenses and Changes in Retained Earnings

	<u>As Previously Reported</u>	<u>Reclassification</u>	<u>As Reclassified</u>
Operating Revenue	\$39,282,976	\$3,257,321	\$42,540,297
Administrative Expenses	37,937,179	(20,466)	37,916,713
Operating Income	1,345,797	3,277,787	4,623,584
Nonoperating revenues (expenses)	3,257,321	(3,277,787)	(20,466)

Statement of Cash Flows

Operating Income	1,345,797	3,277,787	4,623,584
Provision for bad debts	366,578	(218,588)	147,990
Loss on disposal of capital assets	20,466	(20,466)	-
Decrease in premium receivables	15,806,557	218,588	16,025,145
Reclassify interest income to investing activities	-	(3,257,321)	(3,257,321)

Required Supplementary Information

**SOUTH CAROLINA STATE ACCIDENT FUND
REQUIRED SUPPLEMENTARY INFORMATION
YEAR 2000 ISSUES
JUNE 30, 1999**

The year 2000 issue arises because most computer software programs allocate two digits to the *Year* date field on the assumption that the first two digits will always be *19*. Without reprogramming, such programs will interpret, for example, the year 2000 as the year 1900. Also, some programs may be unable to recognize that the year 2000 is a leap year.

The year 2000 issue may affect electronic equipment containing computer chips that have date recognition features – such as environmental systems, elevators, and vehicles – as well as computer software programs. In addition, the year 2000 issue affects not only computer applications and equipment under the South Carolina State Accident Fund's direct control but also the systems of other entities with which the South Carolina State Accident Fund transacts business. Some of the South Carolina State Accident Fund's systems/equipment affected by the year 2000 issue are critical to the continued and uninterrupted operations of the South Carolina State Accident Fund.

The computer systems identified as most crucial to the South Carolina State Accident Fund's operations are its Claims Management System (CMS), Lawson Accounting System and its Policyholders System (PHS). The Fund also relies on other State agencies for mission critical functions such as payroll processing. Important but not mission critical systems include most personal computers.

Because of the unprecedented nature of the year 2000 issue, its effects and the success of related remediation efforts will not be fully determinable until the year 2000 and thereafter. Management cannot assure that the South Carolina Accident Fund is or will be year 2000 compliant, the South Carolina State Accident Fund's remediation efforts will be successful in whole or in part, or that parties with whom the South Carolina State Accident Fund does business will be year 2000 compliant.

The South Carolina State Accident Fund has purchased and installed upgrades of its mission critical software. These systems have been tested by the software vendor in all critical areas. The costs of these upgrades and their installation costs have been absorbed by the South Carolina State Accident Fund as part of its routine software systems operating budget. At June 30, 1999 the South Carolina State Accident Fund had no outstanding commitments related to its efforts to address Year 2000 issues in computer systems and other electronic equipment.

Work to address the year 2000 issue with respect to each system critical to conducting operations falls predominantly within one of the following stages of work:

1. Awareness stage – Establishing a budget and project plan for dealing with the year 2000 issue.
2. Assessment stage – Identifying the systems and components for which year 2000 work is needed.
3. Remediation stage – Making changes to systems and equipment.
4. Validation/testing stage – Validating and testing changes that were made during the remediation stage.

**SOUTH CAROLINA STATE ACCIDENT FUND
 REQUIRED SUPPLEMENTARY INFORMATION
 YEAR 2000 ISSUES
 JUNE 30, 1999**

The State Accident Fund's year 2000 remediation work for its mission-critical systems and electronic equipment are in the following stages of work. C means complete, P means in process, A means still needs to be addressed.

	Awareness	Assessment	Remediation	Validation/ Testing
Claims Management Software	C	C	C	C
Policy Holders Software	C	C	C	C
Lawson Accounting Software	C	C	C	C
RS 6000 Computer System	C	C	C	C
UPS IBM BP3011	C	C	C	C
Voice mail system	C	C	C	C
Telephone system	C	C	C	C

For other important, but not mission critical, equipment and systems and personal computers, the State Accident Fund has completed the Awareness, Assessment, and Remediation stages. The validation and testing stage is in process on these non-mission critical systems.

The South Carolina State Accident Fund has made contingency plans for the possible failure of computer systems and embedded devices and also for possible interruptions to the Fund's business.