

**SOUTH CAROLINA SECOND INJURY FUND
COLUMBIA, SOUTH CAROLINA**

AUDITED FINANCIAL STATEMENTS

June 30, 2013

with

INDEPENDENT AUDITORS REPORT

State of South Carolina



Office of the State Auditor

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November 1, 2013

The Honorable Nikki R. Haley, Governor
and
Members of the South Carolina State Budget and Control Board
Columbia, South Carolina

This report on the audit of the financial statements of the South Carolina Second Injury Fund for the fiscal year ended June 30, 2013, was issued by McDowell-Pearman, LLC, 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 SECOND INJURY FUND
COLUMBIA, SOUTH CAROLINA

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McDOWELL ♦ PEARMAN, LLC
CERTIFIED PUBLIC ACCOUNTANTS

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INDEPENDENT AUDITORS REPORT

Mr. Richard H. Gilbert, Jr.
Interim State Auditor
South Carolina Office of the State Auditor
Columbia, South Carolina

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, and each major fund of the South Carolina Second Injury 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

South Carolina Second Injury Fund's 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 an opinion 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 from 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 policies used and the reasonableness of significant accounting 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 on the financial statements.

Opinion on the Financial Statements

In our opinion, the financial statements referred to above present fairly, in all material respects the respective financial position of the governmental activities, the business-type activities, and each major fund of the South Carolina Second Injury Fund as of June 30, 2013, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Emphasis of Other Matter

As discussed in Note 1, the financial statements of the South Carolina Second Injury Fund are intended to present the financial position, result of operations, and the cash flows of only that portion of the Funds of the State of South Carolina that is attributable to the transactions of the South Carolina Second Injury Fund. These financial statements do not purport to, and do not, present fairly the financial position of the State of South Carolina primary government or financial reporting entity as of June 30, 2013, and the changes in its financial position and its cash flows, where applicable, for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Other Matters

Accounting principles generally accepted in the United States of America require that management's discussion and analysis on pages 3 through 6 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 30, 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, and 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.



October 30, 2013

NIKKI R. HALLY, CHAIR
GOVERNOR
CURTIS M. LOFTIS, JR.
STATE TREASURER
RICHARD ECKSTROM, CPA
COMPTROLLER GENERAL



SC BUDGET AND CONTROL BOARD

**INSURANCE RESERVE FUND
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W. BRIAN WHITE
CHAIRMAN, HOUSE WAYS AND MEANS
MARCIA ADAMS
EXECUTIVE DIRECTOR

Management's Discussion and Analysis

Overview of the Financial Statements and Financial Analysis

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*. There are five financial statements presented: Statement of Net Position; Statement of Activities; Statement of Revenues and Changes in Fund Balance – Governmental Fund Type; Statement of Revenues, Expenses, and Changes in Net Position – Proprietary Fund Type; and Statement of Cash Flows. This discussion and analysis of the Second Injury Fund's (the Fund) financial statements provides an overview of its financial activities for the year.

Statement of Net Position

The Statement of Net Position presents the assets, liabilities, and net assets of the Fund as of the end of the fiscal year. The Statement of Net Position presents end-of-year data concerning assets (current and noncurrent), liabilities (current and noncurrent), and net position (assets minus liabilities). Current assets are those which are reasonably expected to be realized in cash or sold or consumed within one year. Current liabilities are obligations whose liquidation is expected to require the use of current assets.

Condensed Statement of Net Position

<u>Assets</u>	<u>FY 2013</u>	<u>FY 2012</u>	<u>VARIANCE</u>
Current Assets	87,472,501	41,945,425	45,527,076
Capital assets, net of accumulated depreciation	1,446	4,337	(2,891)
Total Assets	\$87,473,947	\$41,949,762	\$45,524,185

<u>Liabilities</u>	<u>FY 2013</u>	<u>FY 2012</u>	<u>VARIANCE</u>
Current Liabilities	96,072,256	49,356,048	46,716,208
Non-current Liabilities	86,885,000	35,157,839	51,727,161
Total Liabilities	\$ 182,957,256	\$ 84,513,887	\$ 98,443,369

Net Position (Deficit)			
Invested in capital assets	1,446	4,337	(2,891)
Deficit	(95,484,755)	(42,568,462)	(52,916,293)
Total Net Position (Deficit)	\$ (95,483,309)	\$ (42,564,125)	\$ (52,919,184)

Statement of Activities

Changes in total net position as presented on the Statement of Net Position are based on the activity presented in the Statement of Activities. The purpose of the statement is to present the revenues received by the Fund, and the expenses paid by the Fund, and transfers to the Fund, which reconciles to the change in net position (deficit) for the year.

The Statement of Activities is prepared on the accrual basis of accounting. Accrual accounting attempts to record the financial effects of transactions on an entity in the period in which those transactions occur rather than in the period in which cash is received or paid. Revenues are recognized when services or goods are provided. Expenses are recognized when resources are utilized in order to produce goods or services.

Condensed Statement of Activities

	<u>FY 2013</u>	<u>FY 2012</u>	<u>VARIANCE</u>
Operating revenues	1,520,018	1,559,634	(39,616)
Operating expenses	(62,239,202)	(16,067,974)	(46,171,228)
Operating loss	(60,719,184)	(14,508,340)	(46,210,844)
Transfers	7,800,000	7,400,000	400,000
Decrease net position	(52,919,184)	(7,108,340)	(45,810,844)
Net position (deficit) – beg. of year	(42,564,125)	(35,455,785)	(7,108,340)
Net position (deficit) at end of year	\$ (95,483,309)	\$ (42,564,125)	\$ (52,919,184)

Individual Fund Statements

The Statement of Revenues, Expenditures and Changes in Fund Balance – Governmental Fund Type is presented on the modified accrual basis of accounting with reconciliation to the Statement of Activities. The Statement of Revenues Expenditures, Expenses and Changes in Net Position – Proprietary Fund Type is a more detailed statement than presented on the Statement of Activities, and is presented on the accrual basis of accounting.

The final statement presented by Second Injury Fund is the Statement of Cash Flows. The Statement of Cash Flows presents detailed information about the cash activity of the Proprietary Fund Type during the year. The statement is divided into three parts. The first part deals with operating cash flows and shows the net cash used by the operating activities of the Fund. The second section shows the interest received from investing activities. The third section reconciles the net cash provided or (used) to the cash and equivalent displayed on the Statement of Net Position.

Condensed Statement of Cash Flows

	<u>FY 2013</u>	<u>FY 2012</u>	<u>VARIANCE</u>
Cash provided (used) by:			
Operating activities	44,072,904	92,079	43,780,825
Investing activities	1,707,287	946,227	761,060
Net change in cash	45,780,191	1,238,306	44,541,885
Cash & cash equivalents – beg. of year	41,091,634	39,853,328	1,238,306
Cash & cash equivalents – end of year	<u>\$ 86,871,825</u>	<u>\$ 41,091,634</u>	<u>\$ 45,780,191</u>

Economic Outlook

The Workers' Compensation Uninsured Employers' Fund shows an overall deficit due to the fact that it records the actuarial liability for unpaid claims. The fund is basically on a pay as you go basis and receives transfers from two other state entities when monies are needed to pay claims.

We feel both the Second Injury Fund's and Workers' Compensation Uninsured Employers' Fund's overall financial positions are fairly stated. Amendments, effective June 25, 2003, to Sections 42-7-310 and 42-9-400 of the South Carolina Code of Laws provided for a termination of the Second Injury Fund programs and appropriations and a transfer of the winding down of affairs of the Second Injury Fund to the Budget and Control Board. The transfer to the Budget and Control Board was completed on July 1, 2013 and the Second Injury Fund terminated at that time. Effective July 1, 2013, the UEF transferred to the State Accident Fund.

The amendments further provided that no claims shall be accepted for Second Injury Fund reimbursement after December 31, 2011. This eliminates any new Second Injury Fund claims. Accordingly, we anticipate a downward trend of payments as the Second Injury Fund liabilities wind down. In addition, under the terms of the Closure Plan adopted, the Assessment has been set for \$60 million annually for five years.

The liabilities of the Uninsured Employers' Fund increased based on the actuarial report of liabilities. In the future these will be reported by the State Accident Fund.

FINANCIAL STATEMENTS

SOUTH CAROLINA SECOND INJURY FUND

STATEMENT OF NET POSITION
JUNE 30, 2013

	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS-TYPE ACTIVITIES</u>	<u>TOTAL</u>
<u>ASSETS</u>			
Current Assets:			
Cash and Cash Equivalents	\$ 400,245	\$ 158,627	\$ 558,872
Cash and Cash Equivalents - Restricted	-	86,713,198	86,713,198
Interest Receivable - Restricted	<u>-</u>	<u>200,431</u>	<u>200,431</u>
Total Current Assets	<u>400,245</u>	<u>87,072,256</u>	<u>87,472,501</u>
Equipment, Net of Accumulated Depreciation of \$46,525	<u>-</u>	<u>1,446</u>	<u>1,446</u>
Total Assets	<u>400,245</u>	<u>87,073,702</u>	<u>87,473,947</u>
<u>LIABILITIES</u>			
Current Liabilities:			
Accounts Payable	-	12,419	12,419
Claims Payable from Restricted Assets	-	86,913,629	86,913,629
Accrued Payroll	-	77,288	77,288
Accrued Compensated Absences	-	68,920	68,920
Claims and Awards	<u>9,000,000</u>	<u>-</u>	<u>9,000,000</u>
Total Current Liabilities	<u>9,000,000</u>	<u>87,072,256</u>	<u>96,072,256</u>
Noncurrent Liabilities:			
Claims and Awards	<u>86,885,000</u>	<u>-</u>	<u>86,885,000</u>
Total Noncurrent Liabilities	<u>86,885,000</u>	<u>-</u>	<u>86,885,000</u>
Total Liabilities	<u>95,885,000</u>	<u>87,072,256</u>	<u>182,957,256</u>
<u>NET POSITION</u>			
Net Position (Deficit):			
Invested in capital assets	-	1,446	1,446
Deficit	<u>(95,484,755)</u>	<u>-</u>	<u>(95,484,755)</u>
Total Net Position (Deficit)	<u>\$ (95,484,755)</u>	<u>\$ 1,446</u>	<u>\$ (95,483,309)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**STATEMENT OF ACTIVITIES
FOR THE YEAR ENDED JUNE 30, 2013**

	<u>Expenses</u>	<u>Charges for Services</u>	<u>Total Governmental Activity</u>	<u>Total Business-Type Activity</u>	<u>Total</u>
Governmental Activity:					
Workers compensation claims, net	\$ 60,716,293	\$ -	\$ (60,716,293)	\$ -	\$ (60,716,293)
Business Type Activity:					
Workers compensation claims	<u>1,522,909</u>	<u>1,520,018</u>	<u>-</u>	<u>(2,891)</u>	<u>(2,891)</u>
Total	<u>\$ 62,239,202</u>	<u>\$ 1,520,018</u>	<u>(60,716,293)</u>	<u>(2,891)</u>	<u>(60,719,184)</u>
 Transfers			<u>7,800,000</u>	<u>-</u>	<u>7,800,000</u>
 Change in Net Position			(52,916,293)	(2,891)	(52,919,184)
Net Position (Deficit) – July 1			<u>(42,568,462)</u>	<u>4,337</u>	<u>(42,564,125)</u>
Net Position (Deficit) – June 30			<u>\$ (95,484,755)</u>	<u>\$ 1,446</u>	<u>\$ (95,483,309)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND
WORKERS' COMPENSATION UNINSURED EMPLOYERS' FUND
GOVERNMENTAL FUND
BALANCE SHEET
FOR THE YEAR ENDED JUNE 30, 2013

ASSETS

Cash	\$ <u>400,245</u>
Total Assets	\$ <u>400,245</u>

FUND EQUITY

Fund Balance – Reserved for workers' compensation claims	\$ <u>400,245</u>
Total Fund Balance	\$ <u>400,245</u>

RECONCILIATION TO STATEMENT OF NET POSITION

Fund Balance Above	\$ 400,245
Recognition of liability for claims and awards on statement of net position	<u>(95,885,000)</u>
Deficit on Statement of Net Position	<u>\$ (95,484,755)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**WORKERS' COMPENSATION UNINSURED EMPLOYERS' FUND
GOVERNMENTAL FUND
STATEMENT OF REVENUES, EXPENDITURES AND
CHANGES IN FUND BALANCE
FOR THE YEAR ENDED JUNE 30, 2013**

Expenditures:

Workers' Compensation Uninsured Employers' Fund claims and awards, net of recoupments of \$732,289	\$ 7,681,495
Claims adjustment expenditures	<u>373,798</u>
Total Expenditures	<u>8,055,293</u>
Transfer from Workers' Compensation Commission	882,180
Transfer from South Carolina Department of Insurance	<u>6,917,820</u>
Total Transfers	<u>7,800,000</u>
Net Change in Fund Balance	(255,293)
Fund Balance - July 1	<u>655,538</u>
Fund Balance - June 30	<u>\$ 400,245</u>

RECONCILIATION TO STATEMENT OF ACTIVITIES

Net Change in Fund Balance above	\$ (255,293)
Recognition of change in claims liability	<u>(52,661,000)</u>
Change in net position on statement of activities	<u>\$ (52,916,293)</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

SECOND INJURY FUND
ENTERPRISE FUND
STATEMENT OF NET POSITION
JUNE 30, 2013

ASSETS

Current Assets:	
Cash and Cash Equivalents	\$ 158,627
Cash and Cash Equivalents - Restricted	86,713,198
Interest Receivable - Restricted	<u>200,431</u>
Total Current Assets	<u>87,072,256</u>
Equipment, Net of Accumulated Depreciation of \$46,525	<u>1,446</u>
Total Assets	<u>87,073,702</u>

LIABILITIES

Current Liabilities:	
Accounts Payable	12,419
Claims Payable from Restricted Assets	86,913,629
Accrued Payroll	77,288
Accrued Compensated Absences	<u>68,920</u>
Total Current Liabilities	<u>87,072,256</u>
Total Liabilities	<u>87,072,256</u>

NET POSITION

Invested in capital assets	<u>1,446</u>
Total Net Position	<u>\$ 1,446</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

SECOND INJURY FUND
ENTERPRISE FUND
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
FOR THE YEAR ENDED JUNE 30, 2013

Operating Revenue:	
Assessments	\$ <u>1,520,018</u>
Total Revenue	<u>1,520,018</u>
Operating Expenses:	
Administration:	
Personal services	832,124
Employer contributions	287,685
Contractual services	226,029
Fixed charges and contributions	142,160
Supplies	18,426
Travel	13,594
Depreciation	<u>2,891</u>
Total Operating Expenses	<u>1,522,909</u>
Net Income (Loss)	(2,891)
Net Position - July 1	<u>4,337</u>
Net Position - June 30	<u>\$ 1,446</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

**SECOND INJURY FUND
ENTERPRISE FUND
STATEMENT OF CASH FLOWS
FOR THE YEAR ENDED JUNE 30, 2013**

Cash Flows from Operating Activities:	
Assessments and other income received	\$ 98,196,298
Claim refunds	352,997
Claims paid	(52,914,262)
Administrative expenses paid	<u>(1,562,129)</u>
Net Cash Provided (Used) by Operating Activities	<u>44,072,904</u>
Cash Flows from Investing Activities:	
Interest income received restricted for payment of claims	<u>1,707,287</u>
Net Cash Provided by Investing Activities	<u>1,707,287</u>
Net Increase (Decrease) in Cash and Cash Equivalents	45,780,191
Cash and Cash Equivalents, Beginning of Year	<u>41,091,634</u>
Cash and Cash Equivalents, End of Year	<u>\$ 86,871,825</u>
Reconciliation of Operating Income (Loss) to Net Cash	
Provided (Used) by Operating Activities:	
Operating income (loss)	\$ (2,891)
Adjustments to reconcile operating income to net cash provided by operating activities:	
Depreciation	2,891
Assessments and other income received:	
Restricted for payment of claims	96,679,751
Claims paid (net of refunds)	(52,561,265)
Increase (Decrease) in liabilities:	
Accounts payable	12,317
Accrued payroll	(12,981)
Accrued compensated absences	<u>(44,918)</u>
Net Cash Provided (Used) by Operating Activities	<u>\$ 44,072,904</u>

THE ACCOMPANYING NOTES ARE AN
INTEGRAL PART OF THIS FINANCIAL STATEMENT

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The core of the financial reporting entity is the primary government which has a separately elected governing body. As required by generally accepted accounting principles, the financial reporting entity includes both the primary government and all its component units. Component units are legally separate organizations for which the elected officials or the primary government are financially accountable. In turn, component units may have component units.

An organization other than a primary government may serve as a nucleus for a reporting entity when it issues separate financial statements. That organization is identified herein as a primary entity.

The primary entity is financially accountable if it appoints a voting majority of the organization's governing body including situations in which the voting majority consists of the primary entity's officials serving as required by law (e.g., employees who serve in an ex officio capacity on the component unit's board are considered appointments by the primary entity) and (1) it is able to impose its will on that organization or (2) there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the primary entity. The primary entity also may be financially accountable if an organization is fiscally dependent on it even if it does not appoint a voting majority of the board. An organization is fiscally dependent on the primary entity that holds one or more of the following powers:

- (1) Determine its budget without another government's having the authority to approve and modify that budget.
- (2) Levy taxes or set rates or charges without approval by another government.
- (3) Issue bonded debt without approval by another government.

Based on the application of the above criteria, no component units are included in the reporting entity.

Prior to July 1, 1993, the Second Injury Fund ("the Fund") was considered to be a component unit of the State of South Carolina. Effective July 1, 1993, the Fund was considered part of the State of South Carolina's primary government and is included in the State of South Carolina's Comprehensive Annual Financial Report as such. This is based on guidance provided by GASB Statement 14, *The Financial Reporting Entity*. The South Carolina Second Injury Fund was established by Section 42-7-310 of the Code of Laws of South Carolina. The funds of the Fund are included in the Comprehensive Annual Financial Report of the State of South Carolina.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2013

(Continued)

The Fund is administered by a Director appointed by the State Budget and Control Board. The reporting entity is part of the State primary government unit. The accompanying financial statements present the financial position, results of operations and cash flows solely of the South Carolina Second Injury Fund and do not include any other funds of the State of South Carolina. The Second Injury Fund does not have any component units.

The Second Injury Fund, per Code of Laws Section 42-7-310, established the guidelines by which to pay compensation claims in those cases where an individual having an existing permanent physical impairment incurs a subsequent disability from injury by accident arising out of and in the course of employment. Funding for payment of compensation awards and for Fund operating costs is provided by equitable assessments upon all workmen's compensation insurance carriers, self-insurers, and the South Carolina State Accident Fund (approximately 360 entities). Participation is mandatory as required by State law. Participants of the fund are responsible for the fund's liabilities. Payments of claims and awards are made directly to the carriers and self-insurers. The State of South Carolina will not be responsible for any expense or liabilities of the fund, except the State Accident Fund, who is a participant in the fund.

Per Code of Laws Section 42-7-200(a), as amended, the Second Injury Fund is responsible for administering the Workers' Compensation Uninsured Employers' Fund. The Fund issues payment of awards of workers' compensation benefits, which are unpaid because of employers' who fail to acquire necessary coverage for employees. Funding for payment of awards is provided from collections of the tax on insurance carriers and self-insured persons in an amount sufficient to maintain the fund. The monies are transferred from the South Carolina Department of Insurance and the South Carolina Workers' Compensation Commission.

Basis of Presentation - Fund Accounting

The government uses funds to report its financial position, results of operations and cash flows. 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. Separate accounts are maintained for each fund. Funds are classified into two categories: governmental and proprietary. Each category, in turn, is divided into separate "fund types."

Governmental funds include the Workers' Compensation Uninsured Employers' Fund, a special revenue fund. Proprietary funds include the Second Injury Fund, an enterprise fund.

Deferred Outflows/Inflows of Resources

The Governmental Accounting Standards Board issued Statement No. 63 *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. The objective of this statement is to improve financial reporting by standardizing the presentation of deferred outflows of resources and deferred inflows of resources and their effects on a government's net position. The requirements of the statement are effective for periods beginning after December 15, 2011. The Fund implemented provisions of this statement during the year ended June 30, 2013.

In accordance with GASB 63 the term net assets, effective in the current year, is defined as net position. Net position includes deferred outflows and inflows as explained below.

In addition to assets, the statement of net position will sometimes report a separate section for deferred outflows of resources, which represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense/expenditure) until that time.

Also in addition to liabilities the statement of net position will sometimes report a separate section for deferred inflows of resources, which represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time.

The Fund does not have any items that qualify for reporting as deferred outflows or inflows.

Basis of Accounting

Government-wide Financial Statements

In the government-wide Statement of Net Position and Statements of Activities, both governmental and business-like activities are presented using the accrual basis of accounting. Under the accrual basis of accounting, revenues are recognized when earned and expenses are recorded when the liability is incurred or economic asset used.

Fund Financial Statements

The Workers' Compensation Uninsured Employers' Fund a special revenue fund uses the modified accrual basis of accounting. The revenues are recognized when they become available and measurable. Available means those amounts that will be received within one year of the date of the financial statements. The transfers from the South Carolina Insurance Commission and

SOUTH CAROLINA SECOND INJURY FUND

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the South Carolina Workers' Compensation Commission are recorded when received in cash because they are not considered available until the Fund requests the transfer of funds. The request from the Fund is the event that is considered necessary to trigger the recognition of transfer.

Expenditures of this fund are generally recognized under the modified accrual basis of accounting when the related fund liability is incurred. Expenditure recognition is limited to exclude amounts represented by noncurrent liabilities since they do not affect net current assets. Because this basis of accounting differs from the manner in which the government-wide financial statements are prepared the fund financial statements include a reconciliation with brief explanations to better identify the relationship between the government-wide financial statements and the individual fund financial statements.

The Second Injury Fund an enterprise fund is accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the balance sheet. These operating statements present increases and decreases in total assets.

The revenues and expenses are recognized on the accrual basis of accounting. Revenues are recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable.

The Second Injury Fund individual financial statements are prepared on the same basis of accounting as the government-wide financial statements; therefore there is no reconciliation between the fund and government-wide statements.

The Government Accounting Standards Board (GASB) is the recognized standard setting body for generally accepted accounting principles applicable to governmental proprietary activities in the United States of America. The Fund applies all applicable Government Accounting Standards Board (GASB) pronouncements and all applicable Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989 when not in conflict with (GASB) pronouncements. In accordance with GASB Statement 20, the Fund has elected not to implement FASB Statements 103 and after.

Budget Policy

The South Carolina Second Injury Fund is granted an annual appropriation for administrative operating purposes by the General Assembly to be funded from the Second Injury Fund's participant's assessments. The appropriation as enacted becomes the legal operating budget for the Fund for its budgeted activities. The

SOUTH CAROLINA SECOND INJURY FUND

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Appropriation Act authorizes expenditures from funds appropriated from the General Fund of the State and authorizes expenditures of total funds. The Total Funds column in the Appropriations Act for each individual budgetary unit authorizes expenditures from all budgeted resources. A revenue budget is not adopted for individual budgetary units. The agency receives no State General Funds Appropriations. The General Assembly enacts the budget through passage of 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 budgetary 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 2013 Appropriation 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 Comptroller General. No such transfer may exceed twenty percent of the program budget. Upon request, such transfers may be provided to members of the General Assembly on an agency by agency basis. Transfers from personal services accounts to other operating accounts or from other operating accounts may be restricted to any established standard level set by the Budget and Control Board upon formal approval by a majority of the members of the Budget and Control Board.

During the fiscal year-end closeout period in July, agencies may continue to charge vendor, interagency, and interfund payments for the fiscal year to that fiscal year's appropriation. For the Fund, any unexpended funds as of June 30, automatically carry over to the ensuing fiscal year. State law does not require the use of encumbrance accounting.

State law does not precisely define the budgetary basis of accounting. The current Appropriation Act states that the General Assembly intends to appropriate all State funds and to authorize and/or appropriate the use of all other 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 disbursements basis for payroll expenditures.

The budget and actual comparison in Note 2 presents actual expenditures on the budgetary basis of accounting compared to the legally adopted and modified budget on a line-item expenditure basis for the Fund's administrative costs. The level of legal control for each agency is reported in a publication of the State Comptroller General's Office titled *A Detailed Report of Appropriations and Expenditures* for each fiscal year.

Capital Assets

Equipment acquisitions require the use of enterprise fund financial resources and are capitalized at cost in the fund upon acquisition. Purchases of equipment in excess of \$5,000 are capitalized. Depreciation of equipment is charged as an expense against operations, and accumulated depreciation is reported on the Funds' balance sheet. Depreciation has been provided over the estimated useful lives of five to ten years using the straight-line method of depreciation.

Accrued Compensated Absences

Generally all permanent full-time State employees and certain part-time employees scheduled to work at least one-half of the agency's workweek are entitled to accrue and carry forward at calendar year-end a maximum of 180 days sick leave and 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 of 45 days, but are not entitled to any payment for unused sick leave. The South Carolina Second Injury Fund calculates the gross compensated absences liability based on recorded balances of unused leave. The entire unpaid liability for which the employer expects to compensate employees through paid time off or cash payments, inventoried at fiscal year-end current salary costs and the cost of the salary-related benefit payments is recorded as a current liability. The net change in the liability is recorded in the current year in the applicable administrative expense categories.

Cash and Cash Equivalents

The amounts shown in the financial statements as "*cash and cash equivalents*" represent cash on deposit with the State Treasurer and cash invested in various investments by the State Treasurer as part of the State's internal cash management pool.

Because the State's internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents. The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. Most State agencies participate in the State's internal cash management pool; however, some agency accounts are not included in the pool because of restrictions on the use of funds. For those accounts, cash equivalents included investments in short-term, highly liquid securities having an original maturity of three months or less.

The State's internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each agency's equity interest in the general deposit account; however, all earnings on that account are credited to

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS FOR THE YEAR ENDED JUNE 30, 2013

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the General Fund of the State. Agencies record and report their deposits in the general deposit account at cost. However, agencies report their deposits in the special deposit accounts at fair value. Investments in the pool are recorded at fair value. Interest earned by the agency's special deposit accounts is posted to the agency's account at the end of each month and is retained by the agency. Interest earnings are allocated based on the percentage of an agency's accumulated daily interest receivable to the total undistributed interest received by 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. The South Carolina Second Injury Fund only has special deposit accounts. 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 agency's percentage of ownership in the pool.

Although the State's internal cash management pool includes some long-term investments, it operates as a demand deposit account; therefore, for credit risk information pertaining to the internal cash management pool see the deposits disclosures in Note 3.

Statement of Cash Flows

For purposes of this statement the South Carolina Second Injury Fund considers investments with the State of South Carolina's internal cash management pool to be cash equivalents because they are readily convertible to cash with an insignificant risk of loss in value.

Unpaid Claims Liabilities

It has been determined that the Second Injury Fund did not fall within GASB 10's definition of a public entity risk pool (PERP), because there is no actual transfer of risk to the Fund, and also the majority of the entities serviced by the fund are not governmental entities. Assessments for the current year are recognized only to the extent actually assessed to the participants. The assessments are recognized as revenues only to the extent they are used to cover the funds administrative expenses and capital outlay. Claims are recognized as a liability only to the extent that assets are available to liquidate these liabilities. Based on the fund operations and prior actuarial studies, it was determined that the liabilities far exceed the available assets, however since the participants are ultimately responsible for paying these liabilities and there is no transfer of risk, a liability is recognized only to the availability of assets to pay claims. Therefore the balance sheet does not include any additional claims reported to the Second Injury Fund as a claims service or an estimate of IBNR claims which are the responsibility of the participants. The payments of claims are not considered an operating expense of the fund. These are only shown on the statement of cash flows.

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Prior to July 1, 1995, the Workers' Compensation Uninsured Employers' Fund was determined to be covered by GASB Statement 10 as an activity other than a public entity risk pool (PERP) which, however, does involve risk financing activities. The primary difference between a PERP and a non-PERP entity is that in a non-PERP entity the government does not transfer or pool its risks. Effective July 1, 1995, it has been determined that the Fund is a state benefit program that should follow GASB 10's guidance for measurement and recognition of claims liabilities. However, the Fund is not required to present additional disclosures, such as the claims reconciliation table required by GASB 10. GASB 10 allows the selection of fund type based upon characteristics of the fund. This activity is classified as a special revenue fund. The Fund actuarially establishes claims liabilities based on estimates of the ultimate cost of claims (including future claim adjustment expenses) that have been reported but not settled, and of claims that have been incurred but not reported. The length of time for which such costs must be estimated varies depending on the coverage involved. Because actual claims costs depend on such complex factors as medical technology, changes in doctrines 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 using a variety of actuarial and statistical techniques to produce current estimates that reflect recent settlements, claim frequency, and other economic and social factors. 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 reflects past inflation and on other factors that are considered to be appropriate modifiers of past experience. Also included in the calculation is an estimate of future recoupments by the fund from the uninsured employers. In June 2013, an actuarial study was done for the year ended June 30, 2013.

Assessment Revenues

Second Injury Fund assessments are recognized as enterprise fund revenues only to the extent which they are needed for administrative expenses and capital outlay of the fund, less depreciation and gain on disposal of assets recorded by the Fund.

Restricted Assets and Claims Payable from Restricted Assets

Cash which is not required to pay administrative liabilities is restricted for payment of claims. The sources of funds to pay restricted claims are assessments, interest earned on deposits and other income. Also interest receivable is restricted for payment of claims. As explained in Note 1 under Unpaid Claims Liabilities, a payable of claims is recorded only to the extent of the assets available to pay claims.

Administration Expenses

The Second Injury Fund does not allocate any administrative expenses to the Uninsured Employers Fund because by State law the Uninsured Employers' Fund

SOUTH CAROLINA SECOND INJURY FUND

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(Continued)

cannot pay administrative expenses. The fund only pays claims and those direct costs associated with payment of the claims. All administration expenses are reported in the enterprise fund.

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.

Subsequent Events

In preparing these financial statements, the Second Injury Fund has evaluated events and transactions for potential recognition or disclosure through xxxxxxxx, 2013, the date the financial statement was available to be issued.

NOTE 2 - BUDGET COMPARISON TO ACTUAL

The Administration expenses of the enterprise fund shown in the statement of revenue, expenses, and changes in retained earnings are reported on the accrual basis of accounting, which differs from the legally enacted budgetary basis for the year ended June 30, 2013. Adjustments of the GAAP basis of accounting to the budgetary basis consist of reversals of payroll and compensated absences accruals and the related fringe benefits, and of reflecting equipment acquisitions as expenses.

Administration expenses per statement	\$	1,522,909
Adjustments to Budgetary Basis:		
Depreciation		(2,891)
Net Accruals:		
Personal services		47,707
Employer contributions		<u>10,192</u>
Total Actual on Budgetary Basis	\$	<u>1,577,917</u>

The Administration expenditures shown below are presented on the budgetary basis compared to the legally adopted and modified budget by object code category.

<u>Fiscal Year 2013</u>	<u>Legal Basis Budget</u>	<u>Actual on Budgetary Basis</u>	<u>Variance Favorable (Unfavorable)</u>
Personal Services	\$ 984,591	\$ 879,831	\$ 104,760
Employer Contributions	351,951	297,877	54,074
Other Operating Expenses	<u>459,932</u>	<u>400,209</u>	<u>59,723</u>
Total	<u>\$ 1,796,474</u>	<u>\$ 1,577,917</u>	<u>\$ 218,557</u>

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
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(Continued)

The special revenue fund does not budget and is not allocated any administrative costs. Claims and claims adjustment expenses of neither fund are a budgeted expenditure.

NOTE 3 - DEPOSITS AND INVESTMENTS

All deposits of South Carolina Second Injury Fund are under the control of the State Treasurer who, by law, has sole authority for investing State Funds.

State law requires full collateralization of all State Treasurer bank balances. The State Treasurer must correct any deficiencies in collateral within seven days. At June 30, 2013, all State Treasurer bank balances were fully insured or collateralized with securities held by the State or by its agents in the State's name.

With respect to investments in the State's internal 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 agent in the State's name. Information pertaining to the reported amounts, fair 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 4 - EQUIPMENT

Equipment is stated at original cost. A summary of the changes in equipment and accumulated depreciation is as follows:

<u>Equipment</u>			
<u>Balance</u> <u>7/01/12</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>6/30/13</u>
\$ 47,971	\$ -	\$ -	\$ 47,971
<u>Accumulated Depreciation</u>			
<u>Balance</u> <u>7/1/12</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>6/30/13</u>
\$ 43,634	\$ 2,891	\$ -	\$ 46,525

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
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NOTE 5 - LONG-TERM LIABILITIES

The following is a summary of changes in long-term liabilities of the Fund:

	<u>July 1, 2012</u>	<u>Increase</u>	<u>Decrease</u>	<u>June 30, 2013</u>	<u>Due Within One Year</u>
Governmental Activity:					
Claims and Awards	\$ 43,224,000	\$ 60,716,293	\$ 8,055,293	\$ 95,885,000	\$ 9,000,000
Business-Type Activity:					
Compensated Absences	113,839	90,000	134,919	68,920	68,920
Total	\$ 43,337,839	\$ 60,806,293	\$ 8,190,212	\$ 95,953,920	\$ 9,068,920

NOTE 6 - PENSION PLAN

The majority of employees of the Fund are covered by a retirement plan through the South Carolina Retirement System (SCRS), a cost-sharing multiple-employer defined benefit pension plan administered by the Retirement Division of the 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 lifetime monthly retirement annuity benefits to members as well as disability, survivor options, annual benefit adjustments, death benefits, and incidental death 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. 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 Fund and the five pension plans are included in the statewide CAFR of the State of South Carolina.

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

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(Continued)

compensation during 12 consecutive quarters and includes an amount for up to 45 days of 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 be closed and end for all participants effective June 30, 2018.

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 of 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 incidental death amounts are remitted to SCRS.

SOUTH CAROLINA SECOND INJURY FUND

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Effective July 1, 2012, the member contribution was increased from 6.5% to 7%.

The effective employer rates by year for SCRS and the State ORP are as follows:

SCRS and State ORP					
<u>Effective Date</u>	<u>Base Employer Rate</u>	<u>Insurance Surcharge</u>	<u>Total Employer Rate</u>	<u>Optional Incidental Death Benefit</u>	<u>Optional Accidental Death Prog.</u>
07/01/12	10.450%	4.55%	15.000%	0.15%	N/A
07/01/11	9.385%	4.30%	13.685%	0.15%	N/A
07/01/10	9.240%	3.90%	13.140%	0.15%	N/A

Five percent of the earnable compensation contributed as part of the State ORP employer contribution is remitted directly to the ORP vendor to be allocated to the member's account.

The Fund's actual contributions to the SCRS and State ORP for the years ended June 30, 2013, 2012 and 2011 were \$ 92,382, \$ 86,282, and \$94,100, respectively, and equaled the base required retirement contribution rate as shown in the above table. Also, the Fund paid employer incidental death contributions of, \$1,320, \$1,379, and \$1,527, at the rate of .15% of compensation for the fiscal years ended June 30, 2013, 2012, and 2011 respectively.

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 is actuarially determined.

The surcharges to fund retiree health and dental insurance are not part of the actuarially established rates. For the current fiscal year the 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 plans.

NOTE 7 - POST-EMPLOYMENT 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 Division 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. 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, and which are included in the tables in Note 10. The IB sets the employer contribution rate based on a pay-as-you-go basis. The Fund paid \$39,592 and \$39,532 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

SOUTH CAROLINA SECOND INJURY FUND

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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 a copy of the 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 8 - OPERATING LEASE

The Second Injury Fund paid \$133,832 in fiscal year 2013 for rental of office space from a party outside of state government, under an operating lease. The current lease dated November 21, 2008 expired in June, 2013.

NOTE 9 - 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 and check preparation, banking and investment functions from the State Treasurer.

Other services received at no cost from the various divisions of the State Budget and Control Board include retirement and health plan administration, personnel management, assistance in the preparation of the State Budget, review and approval of certain budget amendments, procurement services and other centralized functions.

The Fund had financial transactions with various State agencies during the fiscal year. Significant payments were made to divisions of the State Budget and Control Board for retirement and insurance plans contributions, information technology support, insurance coverage, office supplies, printing, telephone, and interagency mail. Significant payments were also made for unemployment and workers' compensation coverage for employees. The amounts of 2013 expenses applicable to transactions with State entities are not readily available. As a self-insurer, the State Accident Fund ("SAF") pays assessments to the Fund and is also reimbursed by the Fund for claims it has paid. The Fund collected assessments from the State Accident Fund (SAF) in the amount of \$5,518,221 and reimbursed claims to the SAF in the amount of \$6,069,281 for workers compensation claims the SAF had paid. The Fund provided no services free of charge to other state agencies during the fiscal year.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
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NOTE 10 - ASSESSMENTS

The Second Injury Fund assesses all insurance carriers and self-insurers (including the State Accident Fund). Each carrier, under regulation prescribed by the Workers' Compensation Commission, shall make payments to the Fund in an amount equal to that proportion of one hundred thirty-five percent of the total disbursement made from the Fund during the preceding fiscal year less the amount of available cash in the Fund as of June thirtieth of the preceding fiscal year which the total normalized premiums of such carrier bore to the total normalized premiums of all carriers for the preceding calendar year. An employer who has ceased to be a self-insurer shall continue to be liable for any assessments into the Fund on account of any benefits paid by him during such calendar year. Any assessment levied or established in accordance with this section constitutes a personal debt of every employer or insurance carrier so assessed and is due and payable to the Second Injury Fund when payment is called for by the Fund. Assessments are done in September of each year. Assessments on carriers and self-insurers in the current fiscal year were \$98,350,533. Overall collections of assessments was \$98,295,407, which can include some amounts from prior years, adjustments based on incorrect data and amounts not being collected due to carrier bankruptcy.

NOTE 11 - RISK MANAGEMENT

The Fund is exposed to various risks of loss and maintains State or commercial insurance coverage for certain risks. The only risks known to the Fund's management that is not insured are for policy deductibles. Management believes such coverage is sufficient to preclude any significant uninsured losses to the Fund. The Fund has not had any claims in the past three years. There were no significant reductions in insurance coverage from coverage in the prior year. The Fund pays insurance premiums to certain other State agencies and commercial insurers to cover risk that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered premium losses sustained during the policy period in accord with the insurance policy and benefit program limits. Several State funds accumulate assets and the State itself assumes substantially all risks for the following:

1. Claims of covered employees for health and dental insurance benefits (Public Employee Benefit Authority); and
2. Claims of covered public employees for long-term disability and group-life insurance benefits (Public Employee Benefit Authority).
3. Claims of covered public employees for workers' compensation insurance benefits (State Accident Fund).
4. Claims of covered public employees for unemployment compensation insurance benefits (Department of Employment and Workforce).

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NOTES TO FINANCIAL STATEMENTS
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The Fund and other entities pay premiums to the states Insurance Reserve Fund (IRF) which issues policies, accumulate assets to cover the risks of loss and pays claims incurred for covered losses related to the following Fund assets, activities, and/or events.

1. Personal property and equipment - Eighty percent of each loss is covered by the IRF. Losses are subject to a \$250 deductible.
2. Data processing equipment - Coverage is up to \$300,000 per loss with a \$250 deductible.
3. Torts - General tort liability up to \$1,000,000 per occurrence.

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, boiler and machinery, and automobile liability. The IRF's rates are determined actuarially.

State agencies are the primary participants in the State's Health and Disability Insurance Fund and in the IRF.

The Fund purchases insurance through a private carrier for employee fidelity bond insurance coverage for all employees to cover losses of up to \$50,000 arising from theft or misappropriations. Management believes based on exposure and likelihood of loss that this coverage is sufficient.

The Fund has not recorded an estimated claims expense related to insurance policy deductibles and policy limits because there is no evidence of asset impairment or other information to indicate a loss should be recorded as of June 30, 2013.

NOTE 12 - GASB 31 ADJUSTMENTS

Effective January 1, 1998, the Division adopted Governmental Accounting Standards Board (GASB) Statement No. 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*. This statement requires that most investments of governmental entities be stated at fair value rather than at cost. For internal (and external) investment pools, this statement requires the equity position of each fund that sponsors the pool to be reported as assets in those funds. The unrealized gains included in cash and cash equivalents of the proprietary fund at June 30, 2013 were \$1,636,080.

SOUTH CAROLINA SECOND INJURY FUND

NOTES TO FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2013

(Continued)

NOTE 13 – TERMINATION OF SECOND INJURY FUND

The Worker' Compensation Reform Act (S. 332) was ratified and signed by the Governor in FY 2007. The major affect of the Act is that the fund was put in "run-off" and will be terminated effective July 1, 2013. Certain effective dates are set out in the Act to permit an orderly termination of the Fund. Some of the significant dates are as follows:

Effective July 1, 2007 the factor used in the assessment calculation is reduced from 175% to 135%.

Effective July 1, 2008 no claims will be accepted with a date of injury of July 1, 2008 or after.

Effective January 1, 2011 no notice of new claims will be accepted.

Effective July 1, 2013 the Uninsured Employers' Fund will be transferred to the State Accident Fund.

Effective July 1, 2013 the Second Injury Fund will be terminated and all remaining obligations and assets will be transferred to the Budget and Control Board.

NOTE 14 – CONTINGENCY

The Fund in prior years was a victim of fraud by an outside party. This party presenting forged credentials had the Fund replace certain outstanding checks. The checks were made to the original payees however the outside party was able to deposit the checks into his own account. The checks were issued by the State Treasurer's Office based on the Fund's vouchers. The outside party was convicted in March of 2009 of forgery in the amount of \$592,509. He was also ordered to make restitution. The Fund received \$15,417 in restitution payment in FY 2013. A total of \$42,667 of restitution payments has been made. Currently the Fund has not determined to what extent that they are liable to replace the stolen funds or who should receive the restitution payments. One check in the amount of \$62,479 has been covered by the bank. As of June 30, 2013 no liability has been recorded for the Fund for replacement of these checks or repayment of restitution payments received.

McDOWELL ♦ PEARMAN, LLC
CERTIFIED PUBLIC ACCOUNTANTS

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**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.
Interim State Auditor
South Carolina Office of the State Auditor
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 as of and for the year ended June 30, 2013, and the related notes to the financial statements, which collectively comprise the South Carolina Second Injury Fund's basic financial statements, and have issued our report thereon dated October 30, 2013.

Internal Control over Financial Reporting

In planning and performing our audit of the financial statements, we considered the South Carolina Second Injury 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 South Carolina Second Injury Fund's internal control. Accordingly, we do not express an opinion on the effectiveness of South Carolina Second Injury Fund's internal control.

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 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. *A significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be material deficiencies or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that were not identified. Given these limitations, during our audit we did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses or significant deficiencies. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the South Carolina Second Injury Fund's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, and contracts, 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*.

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.



October 30, 2013