

**SOUTH CAROLINA STATE FISCAL
ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

(An internal service fund of the State of South Carolina)

FINANCIAL REPORT

**FOR THE FISCAL YEAR ENDED
JUNE 30, 2019**



September 23, 2019

Members of the State Fiscal Accountability Authority
Columbia, South Carolina

This report on the audit of the financial statements of the State Fiscal Accountability Authority – Insurance Reserve Fund for the fiscal year ended June 30, 2019, was issued by Mauldin & Jenkins, 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,

George L. Kennedy, III, CPA
State Auditor

GLKIII/sag

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**FINANCIAL REPORT
FOR THE FISCAL YEAR ENDED JUNE 30, 2019**

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INDEPENDENT AUDITOR'S REPORT

To Mr. George L. Kennedy, III, CPA
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 **South Carolina State Fiscal Accountability Authority Insurance Reserve Fund** (the "Fund"), a fund of the State Fiscal Accountability Authority, as of and for the fiscal year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

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

Auditor's Responsibility

Our responsibility is to express 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.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the South Carolina State Fiscal Accountability Authority Insurance Reserve Fund as of June 30, 2019, and the changes in financial position and cash flows for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Emphasis of a Matter

As discussed in Note 1, the financial statements present only the Insurance Reserve Fund of the South Carolina State Fiscal Accountability Authority and do not purport to, and do not, present fairly the financial position of the South Carolina State Fiscal Accountability Authority, which is a part of the State of South Carolina primary government, as of June 30, 2019, and the changes in financial position and cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to the matter.

Other Matters

Required Supplementary Information - Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis (on pages 4 through 11), the Schedule of Fund's Proportionate Share of the Net Pension Liability (on page 53), the Schedule of Fund Pension Contributions (on page 54), the Schedule of Fund's Proportionate Share of the Net OPEB Liability (on page 55), and the Schedule of Fund OPEB Contributions (on page 56), 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 September 23, 2019, on our consideration of the South Carolina State Fiscal Accountability Authority Insurance Reserve 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 solely 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 effectiveness of the Fund's 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.

Mauldin & Jenkins, LLC

Columbia, South Carolina
September 23, 2019

SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY INSURANCE RESERVE FUND

MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis (MD&A) of the South Carolina State Fiscal Accountability Authority Insurance Reserve Fund (the "Fund") provides an overview of the major financial activities affecting the operations of the Fund. This overview encompasses the financial performance and financial statements of the Fund for the fiscal year ended June 30, 2019. The information contained in this MD&A is prepared by management and should be considered in conjunction with the information contained in the Independent Auditor's Report and notes to the financial statements. Following this MD&A are the basic financial statements of the Fund, together with the notes, which are essential to a full understanding of the data contained in the financial statements.

Financial Highlights

Key financial highlights for fiscal year 2019 are as follows:

- The fund's net position decreased by \$5,751,320 or 3.87 percent;
- The assets and deferred outflows of resources of Fund exceeded its liabilities and deferred inflows of resources at June 30, 2019, by \$142,718,054.
- The Fund experienced an operating loss of \$30,494,478 compared with a loss of \$25,400,176 in the prior year.
- The Fund recognized investment income of \$24,699,495 for the fiscal year ended June 30, 2019, as compared to \$4,045,031 in the prior year.

Overview of the Financial Statements

This discussion and analysis is intended to serve as an introduction to the Fund's basic financial statements. The notes to the financial statements contain more detail on some of the information presented in the financial statements. The financial statements of the Fund report information about the Fund using accounting methods similar to those used by private sector companies. These statements offer short and long-term financial information about its activities. The Statement of Net Position presents information on all of the Fund's assets and deferred outflows of resources and liabilities and deferred inflows of resources, with the difference between these items reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the Fund is improving or deteriorating. The Statement of Net Position can be found on page 12 of this report.

The Statement of Revenues, Expenses and Changes in Net Position presents information showing how the Fund's net position changed during the fiscal year ended June 30, 2019. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus revenues and expenses are recorded in this statement for some items that will only result in cash flows in future fiscal periods (for example, earned but unused vacation leave). The Statement of Revenues, Expenses, and Changes in Net Position can be found on page 13 of this report.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Overview of the Financial Statements (Continued)

The Statement of Cash Flows presents information regarding the net changes in cash and cash equivalents resulting from (1) operations, (2) non-capital and related financing activities, and (3) investing activities.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided within the financial statements. The notes to the financial statements can be found on pages 15 through 52 of this report.

Financial Statements

Net Position: The following table presents condensed Statements of Net Position as of June 30, 2019 and 2018.

	<u>2019</u>	<u>2018</u>
Current assets	\$ 80,135,290	\$ 71,551,623
Non-current assets	<u>479,858,664</u>	<u>455,833,444</u>
Total assets	<u>559,993,954</u>	<u>527,385,067</u>
Deferred outflows of resources	<u>2,034,017</u>	<u>4,170,450</u>
Current liabilities	409,943,540	371,765,900
Long-term liabilities	<u>9,010,138</u>	<u>10,945,829</u>
Total liabilities	<u>418,953,678</u>	<u>382,711,729</u>
Deferred inflows of resources	<u>356,239</u>	<u>374,414</u>
Net position:		
Unrestricted	<u>142,718,054</u>	<u>148,469,374</u>
Total net position	<u>\$ 142,718,054</u>	<u>\$ 148,469,374</u>

The Fund's total current assets increased by \$8,583,667 during the fiscal year ended June 30, 2019. Elements to consider related to these changes include:

- The Fund's cash and cash equivalents increased approximately \$418 thousand during the fiscal year ended June 30, 2019.
- The Fund's accounts receivable increased approximately \$5.10 million during the fiscal year ended June 30, 2019.
- The Fund's prepaid expenses increased by approximately \$2.88 million during the fiscal year ended June 30, 2019.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Statements (Continued)

The Fund's investments increased by approximately \$24.02 million during the fiscal year ended June 30, 2019. Elements to consider related to these changes include:

- For the fiscal year ended June 30, 2019, the South Carolina State Treasurer's Office purchased investments on behalf of the fund in the amount of \$102,838,358 while sales and maturities of investments totaled \$91,371,381, which was the primary cause of the net increase in investments.

The Fund's current liabilities increased by approximately \$38.18 million during the fiscal year ended June 30, 2019. Elements to consider related to these changes include:

- The Fund's unearned revenues increased by \$9.68 million during the year ended June 30, 2019.
- The Fund's claims payable and claims incurred but not reported increased by \$17.77 million and \$10.82 million, respectively.

The Fund's long-term liabilities decreased by approximately \$1.94 million during the current year as a result of an overall decrease in the net pension liability of \$1.96 million, partially offset by an increase in the net OPEB liability approximately \$78,000.

The Fund's net position decreased by \$5,751,320 during the fiscal year ended June 30, 2019. These changes are attributed to an operating loss for the year of \$30,494,478 partially offset by investment income of \$24,699,495.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Statements (Continued)

Revenues, Expenses and Changes in Net Position: The following table summarizes the revenues, expenses and changes in net position for the fiscal years ended June 30, 2019 and 2018.

	2019	2018
Operating revenues:		
Insurance premiums	\$ 137,017,693	\$ 125,461,794
Operating revenues	137,017,693	125,461,794
Operating expenses:		
Claims	121,459,901	106,365,084
Reinsurance premiums	40,258,587	37,346,369
Administrative	5,793,683	7,150,517
Operating expenses	167,512,171	150,861,970
Operating loss	(30,494,478)	(25,400,176)
Nonoperating revenues		
Investment income	24,699,495	4,045,031
Other non-operating revenues	43,663	62,751
Nonoperating revenue	24,743,158	4,107,782
Change in net position	(5,751,320)	(21,292,394)
Net position, beginning of year, as previously reported	148,469,374	173,875,250
Restatement for change in accounting principle	-	(4,113,482)
Net position, beginning of year, as restated	148,469,374	169,761,768
Net position, end of year	\$ 142,718,054	\$ 148,469,374

For the fiscal year ended June 30, 2019, operating expenses increased \$16,650,201, or 11.0% to \$167,512,171. The majority of the current year increase in expenses is the result of increased claims and claims related expenses of \$15,094,817.

For the fiscal year ended June 30, 2019, non-operating revenues of the Fund totaled \$24,743,158, which was approximately \$20.63 million higher than the fiscal year ended June 30, 2018. This increase is primarily attributable to an increase in investment income of approximately \$20.65 million.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Financial Statements (Continued)

Statement of Cash Flows: The following table summarizes the cash flows for the fiscal years ended June 30, 2019 and 2018.

	<u>2019</u>	<u>2018</u>
Net cash used in operating activities	\$ (114,901)	\$ (4,444,065)
Net cash provided by non-capital financing activities	43,663	62,751
Net cash provided by investing activities	<u>489,519</u>	<u>626,722</u>
Net increase (decrease) in cash and cash equivalents	418,281	(3,754,592)
Cash and cash equivalents, beginning of year	<u>6,868,980</u>	<u>10,623,572</u>
Cash and cash equivalents, end of year	<u>\$ 7,287,261</u>	<u>\$ 6,868,980</u>

For the fiscal year ended June 30, 2019, cash used in operating activities resulted in a decrease in cash and cash equivalents of \$114,901. This is a decrease from the amount of cash used in operating activities in fiscal year 2018 of \$4,444,065. The majority of the decrease in cash used in operating activities is the result of increased receipts from insurance premiums and decreased payments for claims and claims related expenses in fiscal year 2019 as compared to fiscal year 2018.

As noted previously, cash and cash equivalents increased by approximately \$418 thousand during fiscal year 2019. This is an increase from fiscal year 2018 where a net decrease in cash and cash equivalents of \$3,754,592 was reported.

Overview of the Fund

The Insurance Reserve Fund is a self-insurance mechanism operated by the State of South Carolina. In many respects, the Fund functions in the same way as an insurance company. The Fund issues policies, collects premiums, pays losses, and purchases reinsurance against swings in experience or catastrophic losses. As an insurance operation, the Fund files a National Association of Insurance Commissioners Annual Statement each year with and is subject to periodic audits by the South Carolina Department of Insurance. The Fund does not market its services or pay marketing costs. Also, the Fund does not pay taxes or participate in any Guaranty Fund or Pool. As a self-insurance mechanism, the Fund is responsible for funding fortuitous losses experienced by governmental entities in South Carolina and offers very broad and, in some cases, unique coverage for its insureds.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Economic Factors

The Fund has maintained adequate reinsurance. Based on the modeling for a 100-year storm event, the Fund purchased \$600 million of coverage subject to a maximum self-insured retention of \$10 million per occurrence and \$15 million in the annual aggregate with a \$1 million trailing per occurrence for subsequent claims. As a result of the series of catastrophic weather events of the last few years, the property reinsurance market has changed significantly. In 2018, the fund's property reinsurance program saw an increase in cost of over 8% (\$1.9 million). In 2019 the Fund's property reinsurance program saw an increase in cost of nearly 12% (\$3.5 million) and the markets are continuing to contract. It is expected that the markets will continue this pattern and the Fund will be forced to pay more for its property reinsurance over the next several years.

For the fourth consecutive year the Fund dealt with natural catastrophes. Hurricanes Florence and Michael are the latest events. Comparatively, the natural catastrophes are as follows:

- Historic Flood of 2015 - \$13.1 million, 160 Claims, 1,094 Segments – all claims are closed
- Hurricane Matthew in 2016 - \$25.4 million, 268 Claims, 3,483 Segments – all claims are closed
- Hurricane Irma in 2017 - \$4.3 million, 79 Claims, 348 Segments – all claims are closed
- Hurricane Florence in 2018 - estimated \$11.3 million, 73 Claims, 1,054 Segments – 5 claims remain
- Hurricane Michael in 2018 - estimated \$395,893, 16 Claims, 30 Segments – 1 claim remains

Even though the Fund received some reimbursement from the reinsurance markets for the Flood of 2015 and Hurricane Matthew, the self-insured retention of \$10 million per occurrence was borne entirely by the Fund. Because the self-insured retention was not met for Hurricanes Irma and Michael, the approximate \$4.8 million in losses associated with these storms has been borne solely by the Fund. Hurricane Florence may generate a small reimbursement after all claims have been closed, but will still represent an additional \$10 million in storm generated losses over a short span of time.

In addition to suffering four catastrophic losses in four years, the Fund experienced other significant property losses including the Town of Cottageville \$1.5 million fire loss; the Spartanburg Community College Tornado loss approximately \$1 million, a fire at the DMH Bull St. property of \$468,000 and the Clemson YMCA at \$770,000. There have also been several significant water damage claims that collectively cost in excess of \$1 million.

The effect of paying the Self Insured Retention of \$10 million for three of the last four years not only impacts the policyholder equity and financial position of the Fund, but combined with the additional major losses reduces assets available for investment which effects investment income.

In fiscal year 2019, liability experience in the tort liability and medical professional liability lines continued to deteriorate significantly. This has caused significant changes in Tort claim reserves and puts additional pressure on the need for rate increases.

By statute, the Fund's assets are invested and managed by the South Carolina Office of the State Treasurer. The Fund's investments increased by \$24,025,220 in fair market value for the fiscal year. Investment income, increased by \$20,654,464 in fiscal year 2019 to \$24,699,495. This is a significant change from the investment income of \$4,045,031 of the prior year.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The \$20.7 million increase in investment income is a considerable factor in helping to reduce the loss in Net Position.

Effective July 1, 2017, the Fund implemented a rate increase in the property line only of 30% affecting properties in seacoast and beach territories. At the time the rates were approved, the increase in property rates was projected to be equivalent to a 5% premium increase (approximately \$5,200,000/year) across the Fund's portfolio and all lines of coverage.

Beginning July 1, 2018, the Fund implemented additional rate changes on a statewide basis in multiple lines of insurance as follows:

- Building and Personal Property, Builders' Risk, Business Income, and Data Processing rates increased 12%.
- Inland Marine (all coverage forms) increased 15%
- Automobile Physical Damage (Comprehensive and Collision) increased 10%
- Tort rates increased 15%

At the time the rates were approved, the increase in property rates was projected to be equivalent to an 8% premium increase (approximately \$10,200,000/year) across the Fund's portfolio and all lines of coverage. The resulting net increase in premiums from these changes will not fully impact the Fund's financials until the increase in premium is fully earned, which will take 24 months from the date of implementation due to the various policy renewal dates for the Fund's insureds.

Economic Outlook

Beginning July 1, 2019, the Fund implemented additional rate changes on a statewide basis in multiple lines of insurance as follows:

- Building and Personal Property, Builders' Risk, Business Income, and Data Processing rates increased 15% for inland property, and 23% for all property located in either Beach or Seacoast areas.
- Inland Marine (all coverage forms) increased 15%
- Automobile Liability rates increased 16%
- Automobile Physical Damage (Comprehensive and Collision) increased 25%
- Tort rates increased 25%
- Professional Liability rates increased 30% for State entities and 25% for Non-State entities

At the time the rates were approved, the increase in property rates was projected to be equivalent to an 18% premium increase (projected \$ 24,400,000/year) across the Fund's portfolio and all lines of coverage.

The resulting net increase in premiums from these changes will not fully impact the Fund's financials until the increase in premium is fully earned, which will take 24 months from the date of implementation due to the various policy renewal dates for the Fund's insureds.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Requests for Information

This financial overview is designed to provide readers with a general overview of the Fund's finances, and to show accountability. If you have questions or would like further information about this financial report, you may contact Mable Prioleau, Accounting Fiscal Manager, (803) 737-0260.

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**STATEMENT OF NET POSITION
JUNE 30, 2019**

ASSETS AND DEFERRED OUTFLOWS OF RESOURCES

Current assets:

Cash and cash equivalents	\$	7,287,261
Receivables:		
Premiums receivable, net of allowance		48,049,548
Accrued interest		3,450,207
Prepaid reinsurance		21,348,274
Total current assets		80,135,290

Non-current assets:

Investments		479,858,664
Total non-current assets		479,858,664
Total assets		559,993,954

Deferred outflows of resources:

Pension		1,784,987
Other postemployment benefits		249,030
Total deferred outflows of resources		2,034,017

**LIABILITIES, DEFERRED INFLOWS OF RESOURCES,
AND NET POSITION**

Current liabilities:

Accounts payable		98,730
Accrued salaries and related expenses		255,611
Accrued compensated absences		157,984
Unearned premium revenue		88,790,531
Claims payable		207,946,840
Claims incurred but not reported		112,693,844
Total current liabilities		409,943,540

Non-current liabilities:

Accrued compensated absences, net of current portion		30,584
Net pension liability		4,982,507
Net other postemployment benefits liability		3,997,047
Total non-current liabilities		9,010,138
Total liabilities		418,953,678

Deferred inflows of resources:

Pension		29,321
Other postemployment benefits		326,918
Total deferred inflows of resources		356,239

Net position:

Unrestricted		142,718,054
Total net position		\$ 142,718,054

The accompanying notes are an integral part of these financial statements.

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
FOR THE FISCAL YEAR ENDED JUNE 30, 2019**

Operating revenues:	
Insurance premiums	\$ 137,017,693
Total operating revenues	137,017,693
Operating expenses:	
Claims	88,853,477
Claims related expenses	32,606,424
Reinsurance premiums	40,258,587
Professional services	199,504
Salaries and benefits	3,397,100
Other services	709,876
Authority allocation	1,399,522
Other operating expenses	87,681
Total operating expenses	167,512,171
Operating loss	(30,494,478)
Non-operating revenues:	
Investment income	24,699,495
Other non-operating revenues	43,663
Total non-operating revenues	24,743,158
Change in net position	(5,751,320)
Net position, beginning of year	148,469,374
Net position, end of year	\$ 142,718,054

The accompanying notes are an integral part of these financial statements.

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**STATEMENT OF CASH FLOWS
FOR THE FISCAL YEAR ENDED JUNE 30, 2019**

CASH FLOWS FROM OPERATING ACTIVITIES

Receipts from insurance premiums	\$ 141,595,721
Payments for claims and claims related expenses	(92,869,206)
Payments for reinsurance premiums	(43,138,167)
Payments for professional services	(199,504)
Payments to suppliers	(2,197,079)
Payments for salaries and benefits	(3,306,666)
Net cash used in operating activities	(114,901)

CASH FLOWS FROM NON-CAPITAL FINANCING ACTIVITIES

Other non-operating receipts	43,663
Net cash provided by non-capital financing activities	43,663

CASH FLOWS FROM INVESTING ACTIVITIES

Purchase of investments	(102,838,358)
Proceeds from the sale of investments	91,371,381
Income from investments	11,956,496
Net cash provided by investing activities	489,519

Increase in cash and cash equivalents	418,281
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Cash and cash equivalents:

Beginning of year	6,868,980
End of year	\$ 7,287,261

Reconciliation of operating loss to net cash used in operating activities:

Operating loss	\$ (30,494,478)
Adjustments to reconcile operating loss to net cash used in operating activities:	
(Increase) decrease in:	
Premiums receivable	(5,101,050)
Prepaid insurance	(2,879,580)
Deferred outflows of resources - pension	2,265,774
Deferred outflows of resources - other postemployment benefits	(129,341)
Increase (decrease) in:	
Accrued salaries and related expenses	(97,078)
Accrued compensated absences	(43,309)
Unearned premium revenue	9,679,078
Claims payable	17,771,238
Claims incurred but not reported	10,819,457
Deferred inflows of resources - pension	25,471
Deferred inflows of resources - other postemployment benefits	(43,646)
Net pension liability	(1,964,983)
Net other postemployment benefits liability	77,546
Net cash used in operating activities	\$ (114,901)

Supplementary Schedule of Non-Cash Investing, Capital and Financing Activities:

Increase in fair value of investments	\$ 12,558,243
Net non-cash investing, capital and financing activities	\$ 12,558,243

The accompanying notes are an integral part of these financial statements.

SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY INSURANCE RESERVE FUND

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The State Fiscal Accountability Authority Insurance Reserve Fund is a fund of the State Fiscal Accountability Authority, which is a part of the State of South Carolina (the “*State*”) primary government. This report contains only the Fund and no other offices or funds of the State Fiscal Accountability Authority or any other part of the State of South Carolina primary government are included. The Insurance Reserve Fund (the “*Fund*”) is under the control of the State Fiscal Accountability Authority (the “*SFAA*”).

The SFAA was established and created by the South Carolina Restructuring Act of 2014, Act 121. The funds of the SFAA are included in the Comprehensive Annual Financial Report of the State of South Carolina.

All of the divisions of the SFAA reporting entity are under the control of its Executive Director. SFAA is governed by a five-member Authority, consisting of the Governor, the State Treasurer, the Comptroller General, the Chairman of the Senate Finance Committee, and the Chairman of the House Ways and Means Committee, all of whom serve in an ex-officio capacity.

Programs managed by the Fund are authorized in the following sections of the South Carolina Code of Laws, 1976, as amended: Section 1-11-140 (tort liability, medical professional liability for individuals and entities and risk management section); Section 1-11-710 (A) (4) (risk management section); Regulation 19-612 (automobile liability); Section 10-7-10 et. seq. (property); Section 59-67-710 (school bus liability); and Section 59-67-790 (school bus pupil injury). Section 15-78-10 et. seq. (the S.C. Tort Claims Act) further defines parameters of coverage provided by the Fund.

The Fund insures state agencies, school districts, special purpose political subdivisions, county governments and municipal governments in South Carolina. The Fund provides property insurance on governmentally owned buildings, the contents of such buildings, equipment and automobiles. The Fund provides automobile liability insurance on governmentally owned vehicles and school buses, tort liability insurance for government premises and operations, and medical professional liability for hospitals. The Fund is a self-insurer and purchases reinsurance to limit losses in the areas of property insurance, boiler and machinery insurance, and automobile liability insurance.

The Fund collects premiums from participating entities, issues policies, and pays claims incurred under the policies from accumulated premiums and earnings on investments and notes receivable. The premium rates are determined in consultation with the actuary and the SFAA. The Fund allocates the costs of providing claims servicing and claims payments by charging each participant a premium. Interest income is considered in the premium rate setting process.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Measurement Focus, Basis of Accounting and Basis of Presentation

The Fund is an internal service fund within the State Fiscal Accountability Authority as the State's managers have determined that the State is the predominant participant in the Fund.

The financial statement presentation for the Fund meets the requirements of Governmental Accounting Standards Board ("GASB") Statement No. 34, *Basic Financial Statements and Management's Discussion and Analysis for State and Local Governments*. As an internal service fund, the Fund in its stand-alone financial statements is considered a proprietary fund under the guidance of GASB Statement No. 34. However, the guidance requires internal service funds included in the basic financial statements of the primary government to be reported as part of the governmental activity. Therefore, presentation in the Comprehensive Annual Financial Report of the State of South Carolina will include this fund as a governmental activity.

The Fund's financial statements have been presented using the economic resources measurement focus which is based upon a determination of net income, financial position, and cash flows. Under this method, all assets and liabilities associated with the operation of the Fund are included on the statement of net position. Net position is segregated into net investment in capital assets, restricted, and unrestricted net position components.

The Fund uses the accrual basis of accounting. Revenue is recognized in the accounting period in which they are earned and become measurable; expenses are recognized in the period incurred, if measurable. The Fund reports claims liabilities when it is probable that a loss has occurred and the amount of the loss can be reasonably estimated.

In accounting and reporting for its operations, the Fund applies all Governmental Accounting Standards Board (GASB) pronouncements. The Fund's financial statements include the provisions of GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*; GASB Statement No. 37, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments: Omnibus*; and, Interpretation No. 6, *Recognition and Measurement of Certain Liabilities and Expenditures in Governmental Fund Financial Statements*. The financial statements include a Management's Discussion and Analysis (MD&A) section providing an analysis of the Fund's overall financial position and results of operations.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents and Investments

Cash and Cash Equivalents - For purposes of the statement of cash flows, the Fund considers all highly liquid securities with a maturity of three months or less at the time of purchase to be cash equivalents. Most State agencies, including the Fund, 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. Because the State's internal cash management pool operates as a demand deposit account, amounts invested in the pool are classified as cash and cash equivalents.

The State Treasurer administers the cash management pool. The pool includes some long-term investments such as obligations of the United States and certain agencies of the United States, obligations of the State of South Carolina and certain of its political subdivisions, certificates of deposit, collateralized repurchase agreements, and certain corporate bonds. For credit risk information pertaining to the internal cash management pool, see the Deposits and Investments disclosures in Note 2.

The State's internal cash management pool consists of a general deposit account and several special deposit accounts. The State records each fund's equity interest in the general deposit account; however, all earnings on that account are credited to the General Fund of the State. Deposits in the general deposit account are recorded and reported at cost. However, the Fund reports its deposits in the special deposit accounts at fair value. Interest earned by the agency's special deposit accounts is posted to the agency's account at the end of each month and is retained by the agency. Interest earnings are allocated based on the percentage of an agency's accumulated daily interest receivable to the total income receivable of the pool.

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

Investments - Deposits and investments for the Fund are governed by the South Carolina Code of Laws, Section 11-9-660, "Investment of Funds". The Fund accounts for its investments at fair value in accordance with GASB Statement No. 72, *Fair Value Measurement and Application*. Changes in unrealized gain or loss on the carrying value of investments are reported as a component of investment income in the statement of revenues, expenses, and changes in net position.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and Cash Equivalents and Investments (Continued)

Investment income consists of interest earned during the year, amortization of premiums and accretion of discounts, realized gains/losses on securities, and unrealized gains/losses resulting from changes in fair value. Earnings are posted to the Fund's account at the end of each month. Securities and securities transactions are reflected in the financial statements on a trade-date basis.

The Fund has a number of financial instruments, none of which are held for trading purposes. Except for nonparticipating investment contracts, investments are reported at fair value which is based on quoted market prices. Nonparticipating investment contracts, such as nonnegotiable certificates of deposits and repurchase agreements, are reported at amortized cost which approximates fair value. See Note 2 for additional information.

Receivables

Premiums receivable consist of receivables from insurance coverage policies. Allowances for doubtful accounts are maintained based on an estimate of collections for those balances aged over 90 days.

Reinsurance Recoverable

The Fund purchases reinsurance for catastrophic losses above certain thresholds on a per occurrence, in the aggregate, and trailing after both occurrence and in the aggregate basis. Amounts to be repaid to the Fund through its purchase of such reinsurance policies are reported in the Statement of Net Position as reinsurance recoverable.

Prepaid Expenses

Payments made to insurers and reinsurers for services that will benefit future periods are recorded as prepaid expenses. The related expense is recognized pro-rata over the policy periods.

Management Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 period. Actual results could differ from those estimates.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Compensated Absences

Generally, all permanent full-time State employees and certain part-time employees scheduled to work at least half of the days in the month are entitled to accrue and carry forward at calendar year-end maximums 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, but are not entitled to any payment for unused sick leave. The compensated absences liability includes accrued annual leave earned for which the employees are entitled to paid time off or payment at termination. The 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 in the Fund.

Unearned Premium Revenue

Premiums billed in advance of coverage, payments received in advance of coverage, or in excess of amounts billed and premiums collected but unearned are recorded as unearned premium revenue.

Claims Payable

Claims payable represents claims resulting from losses that have been incurred but not paid at June 30. The claims payable balance is based on actual losses incurred and settled and estimated losses for claims in the final stages of review and settlement.

Claims Incurred but Not Reported (IBNR)

Losses are recorded at estimated amounts at the time they are reported and include a provision for expenses associated with claim settlements. Insurance claims are expensed as incurred over the period of coverage. The Fund establishes an unpaid claim liability for claims in the process of review, and for IBNR claims. The liability for IBNR claims is actuarially estimated based on the most current historical claims experience of previous payments, changes in number of members and participants, inflation, and award trends. Estimates of liabilities for incurred claims are continually reviewed and revised as changes in these factors occur and revisions are reflected in the current year's operating statement in the applicable claims expense. The liability is reported net of estimated receivables for salvage, subrogation, and reinsurance. Amounts for allocated and unallocated claims adjustment expenses have been included in the calculation of IBNR.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred Outflows/Inflows of Resources

In addition to assets, the Statement of Net Position reports a separate section for *deferred outflows of resources*. This separate financial statement element represents a consumption of net position that applies to future period(s) and so will not be recognized as an outflow of resources (expense) until then. Five items relating to the Fund's Pension Plan and four items relating to the Fund's Other Postemployment Benefit Plan (OPEB) qualify for reporting in this category and are combined in the Statement of Net Position under the headings "Pension" and "Other Postemployment Benefits", respectively. The first item, experience losses, results from periodic studies by the actuary of the Pension Plan and OPEB Plan, which adjust the net pension and net OPEB liabilities for actual experience for certain trend information that was previously assumed, for example the assumed dates of retirement of plan members. These experience losses are recorded as deferred outflows of resources and are amortized into pension and OPEB expense over the expected remaining service lives of the plan members. The second item, differences between projected investment return on pension and OPEB investments and actual return on those investments, is deferred and amortized against pension and OPEB expense over a four-year period for pensions and a five-year period for OPEB, resulting in recognition as a deferred outflow of resources. The third item results from changes in the proportionate share and differences between employer contributions and the proportionate share of total plan employer contributions relative to both the pension and OPEB plans. These changes are reported as deferred outflows of resources and will be recognized as a reduction of the net pension and OPEB liabilities in future years. The fourth item, changes in the actuarial assumptions, adjust the net pension liability, and are amortized into pension expense over the expected remaining service lives of plan members. Additionally, any contributions made by the Fund to the pension plan and OPEB plan, respectively, before year-end but subsequent to the measurement date of the Fund's net pension liability and net OPEB liability are reported as deferred outflows of resources and will be recognized as a reduction of the respective net pension liability and net OPEB liability during the fiscal year ended June 30, 2020.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Deferred Outflows/Inflows of Resources (Continued)

In addition to liabilities, the Statement of Net Position reports a separate section for *deferred inflows of resources*. This separate financial statement element represents an acquisition of net position that applies to future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. One item relating to the Fund's pension plan and three items relating to the Fund's OPEB plan qualify for reporting in this category and are combined in the Statement of Net Position under the heading "Pension" and "Other Postemployment Benefits", respectively. The first item, experience gains relating to the Fund's pension plan and OPEB plan qualify for reporting in this category and is recorded in the Statement of Net Position under the heading "Pension" and "Other Postemployment Benefits", respectively. Experience gains result from periodic studies by the actuaries of the pension plan and OPEB plan, which adjust the net pension and the net OPEB liabilities for actual experience for certain trend information that was previously assumed. These gains are recorded as deferred inflows of resources and are amortized into pension and OPEB expense over the expected remaining lives of the plan members. The second item results from changes in the proportionate share and differences between employer contributions and the proportionate share of total plan employer contributions relating the Fund's OPEB plan. These changes are reported as deferred inflows of resources and will be recognized as OPEB expense in future years. The third item, changes in the actuarial assumptions, adjust the net OPEB liability and are amortized into OPEB expense, respectively, over the expected remaining service lives of plan members.

Net Position Classification

Net position is classified and displayed in three components within the Statement of Net Position. These three classifications are as follows:

- a) Net investment in capital assets consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowing used for the acquisition, construction, or improvement of those assets.
- b) Restricted net position consists of net position with constraints placed on the use either by (1) external groups such as creditors, grantors, contributors, or laws and regulations of other governments; or (2) law through constitutional provisions or enabling legislation.
- c) Unrestricted net position consists of all other net position that does not meet the definition of "restricted".

As of June 30, 2019, the Fund reported only unrestricted net position. Additionally, when both restricted and unrestricted resources are available to finance expenses, it is the Fund's policy to apply restricted resources first.

NOTES TO FINANCIAL STATEMENTS

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Operating and Non-operating Revenues and Expenses

Operating revenues and expenses in the financial statements are those that result from providing services and producing and delivering goods and/or services. Also included are all revenues and expenses not related to capital and related financing, non-capital financing, or investing activities. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

NOTE 2. DEPOSITS AND INVESTMENTS

Total deposits as of June 30, 2019, are summarized as follows:

As reported in the *Statements of Net Position*:

Cash and cash equivalents	\$	7,287,261
Investments		479,858,664
	\$	<u>487,145,925</u>

Cash deposited with the South Carolina State Treasurer's Office	\$	7,239,870
Cash held by third party administrator		47,391
U.S. Government and agency bonds		295,408,774
Corporate bonds and commercial paper		184,449,890
	\$	<u>487,145,925</u>

Custodial Credit Risk – Deposits and Investments. Custodial credit risk for deposits is the risk that, in the event of the failure of a depository financial institution, a government will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. For an investment, this is the risk that, in the event of the failure of the counterparty, the Fund will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. State statutes require all deposits and investments (other than federal or state government instruments) to be collateralized by depository insurance, obligations of the U.S. government, or bonds of public authorities, counties, or municipalities. As of June 30, 2019, all of the Fund's deposits and investments held by the South Carolina State Treasurer's Office were covered under federal depository insurance and/or collateralized with securities held by the pledging financial institution's trust department or agent.

NOTES TO FINANCIAL STATEMENTS

NOTE 2. DEPOSITS AND INVESTMENTS (CONTINUED)

Interest Rate Risk. Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. Investments held for longer periods are subject to increased risk of adverse interest rate changes. The South Carolina State Treasurer's Office has adopted a formal investment policy that limits liquid investment to cash, repurchase agreements, United States Treasury of federal agency discount notes, and commercial paper. Additionally, the State Treasurer further preserves principal by investing mostly in the highest investment grade securities. In order to diversify investment holdings, asset allocation policies are utilized for investments having more than one year to maturity. For further information regarding the State of South Carolina's interest rate risk policies, refer to the State's publicly available comprehensive annual financial report. Overall credit exposure is managed by asset allocation policies and by additional constraints controlling risk exposure to individual corporate issuers.

Credit Risk. Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. The South Carolina State Treasurer's Office has adopted a formal investment policy in accordance with state statutes, which authorize the types of permitted investments. Information regarding the State of South Carolina's credit rate risk policies can be found in the State's publicly available comprehensive annual financial report.

NOTES TO FINANCIAL STATEMENTS

NOTE 2. DEPOSITS AND INVESTMENTS (CONTINUED)

As of June 30, 2019, the Fund's exposure to interest rate risk and credit risk regarding its investments is as follows:

Investment	Fair Value	Credit Rating	Weighted Average Maturity (Years)
U.S. government and agency bonds:			
U.S. treasury bonds	\$ 194,528,638	Aaa	3.73
Collateralized mortgage obligations, mortgage and asset backed securities	33,470,479	Aa1	31.72
Collateralized mortgage obligations, mortgage and asset backed securities	67,409,657	Not rated	18.32
Corporate bonds and commercial paper	997,560	Aaa	3.72
Corporate bonds and commercial paper	201,704	Aa1	0.94
Corporate bonds and commercial paper	5,689,659	Aa2	2.86
Corporate bonds and commercial paper	4,528,332	Aa3	4.60
Corporate bonds and commercial paper	11,772,920	A1	3.20
Corporate bonds and commercial paper	20,891,242	A2	4.74
Corporate bonds and commercial paper	28,488,197	A3	4.65
Corporate bonds and commercial paper	42,258,149	Baa1	4.43
Corporate bonds and commercial paper	45,354,632	Baa2	4.09
Corporate bonds and commercial paper	17,813,128	Baa3	4.26
Corporate bonds and commercial paper	1,263,097	B2	2.24
Corporate bonds and commercial paper	5,191,270	Not rated	2.47
	<u>\$ 479,858,664</u>		

Fair Value Measurements. The Fund categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; and Level 3 inputs are significant unobservable inputs.

NOTES TO FINANCIAL STATEMENTS

NOTE 2. DEPOSITS AND INVESTMENTS (CONTINUED)

The Fund has the following recurring fair value measurements as of June 30, 2019:

Investment	Level 1	Level 2	Level 3	Fair Value
Debt securities:				
U.S. Treasury bonds	\$ 194,528,638	\$ -	\$ -	\$ 194,528,638
Collateralized mortgage obligations and asset backed securities	-	100,880,136	-	100,880,136
Corporate bonds and commercial paper	-	184,449,890	-	184,449,890
Total investments measured at fair value	<u>\$ 194,528,638</u>	<u>\$ 285,330,026</u>	<u>\$ -</u>	
Total investments				<u>\$ 479,858,664</u>

The U.S. treasury bonds, collateralized mortgage obligations and asset backed securities, and the Corporate bonds and commercial paper classified in Level 1 of the fair value hierarchy are valued using prices quoted in active markets for those investments.

The collateralized mortgage obligations and asset backed securities and the corporate bonds and commercial paper investments classified in Level 2 of the fair value hierarchy are valued using a pricing matrix technique. Matrix pricing is used to value securities based on the securities' relationship to benchmark quoted prices. The Fund has no investments classified in Level 3 of the fair value hierarchy.

The repurchase agreements are measured at amortized cost as a practical expedient due to the absence of a readily determinable fair value associated with such investments. As a result, these investments are not categorized according to the fair value hierarchy.

NOTE 3. RECEIVABLES

Premiums receivable including the allowances for uncollectible accounts consisted of the following at June 30, 2019:

Premiums receivable:	
State government	\$ 28,624,096
Local governments	15,158,860
Other	4,507,122
	<u>(240,530)</u>
Less: Allowance for uncollectible accounts	
Total premiums receivable, net	<u>\$ 48,049,548</u>

NOTES TO FINANCIAL STATEMENTS

NOTE 4. LONG-TERM LIABILITIES

The following is a summary of long-term liability activity for the Fund for the fiscal year ended June 30, 2019:

	Balance June 30, 2018	Additions	Reductions	Balance June 30, 2019	Due Within One Year
Compensated absences	\$ 231,877	\$ 114,673	\$ (157,982)	\$ 188,568	\$ 157,984
Net pension liability	6,947,490	451,234	(2,416,217)	4,982,507	-
Net OPEB liability	3,919,501	245,901	(168,355)	3,997,047	-
	<u>\$ 11,098,868</u>	<u>\$ 811,808</u>	<u>\$ (2,742,554)</u>	<u>\$ 9,168,122</u>	<u>\$ 157,984</u>

Compensated absences payable: As discussed in Note 1, this obligation represents accumulated annual leave and compensatory time benefits which are accrued when incurred.

Net Pension Liability: See Note 5 for additional information.

Net OPEB Liability: See Note 6 for additional information.

NOTE 5. PENSION PLANS

Overview

The South Carolina Public Employee Benefit Authority (PEBA), which was created July 1, 2012, administers the various retirement systems and retirement programs managed by its Retirement Division. PEBA has an 11-member Board of Directors, appointed by the Governor and General Assembly leadership, which serves as co-trustee and co-fiduciary of the systems and the trust funds. By law, the State Fiscal Accountability Authority (SFAA), which consists of five elected officials, also reviews certain PEBA Board decisions regarding the funding of the systems and serves as a co-trustee of the systems in conducting that review. Effective July 1, 2017, the Retirement System Funding and Administration Act of 2017 assigned the PEBA Board of Directors as the Custodian of the Retirement Trust Funds and assigned SC PEBA and the Retirement Systems Investment Commission (RSIC) as co-trustees of the Retirement Trust Funds. For purposes of measuring the net pension liability, deferred outflows and inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the Systems and additions to/deductions from the Systems fiduciary net position have been determined on the accrual basis of accounting as they are reported by the Systems in accordance with generally accepted accounting principles (GAAP). For this purpose, revenues are recognized when earned and expenses are recognized when incurred. Benefit and refund expenses are recognized when due and payable in accordance with the terms of the plan. Investments are reported at fair value.

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Overview (Continued)

PEBA issues a Comprehensive Annual Financial Report (CAFR) containing financial statements and required supplementary information for the South Carolina Retirement System's Pension Trust Funds. The CAFR is publically available through the Retirement Benefits' link on PEBA's website at www.peba.sc.gov, or a copy may be obtained by submitting a request to PEBA, 202 Arbor Lake Drive, Columbia, SC 29223. PEBA is considered a division of the primary government of the state of South Carolina and therefore, retirement trust fund financial information is also included in the comprehensive annual financial report of the state.

Plan Description

The South Carolina Retirement System (SCRS), a cost-sharing multiple-employer defined benefit pension plan, was established effective July 1, 1945, pursuant to the provisions of Section 9-1-20 of the South Carolina Code of Laws for the purpose of providing retirement allowances and other benefits for employees of the state, its public school districts, and political subdivisions.

The State Optional Retirement Program (State ORP) is a defined contribution plan that is offered as an alternative to SCRS to certain newly hired employees of state agencies, institutions of higher education, public school districts and individuals first elected to the General Assembly at or after the general election in November 2012. State ORP participants direct the investment of their funds into an account administered by one of four third party record keepers.

Membership

Membership requirements are prescribed in Title 9 of the South Carolina Code of Laws. A brief summary of the requirements the system is described below.

South Carolina Retirement System – Generally, all employees of covered employers are required to participate in and contribute to the SCRS as a condition of employment. This plan covers general employees, teachers and individuals newly elected to the South Carolina General Assembly beginning with the November 2012 general election. An employee member of the system with an effective date of membership prior to July 1, 2012, is a Class Two member. An employee member of the system with an effective date of membership on or after July 1, 2012, is a Class Three member.

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Membership (Continued)

State ORP – As an alternative to membership in SCRS, newly hired state, public school, and higher education employees and individuals newly elected to the S.C. General Assembly beginning with the November 2012 general election have the option to participate in the State Optional Retirement Program (State ORP), which is a defined contribution plan. State ORP participants direct the investment of their funds into a plan administered by one of four investment providers. PEBA assumes no liability for State ORP benefits. Rather, the benefits are the liability of the investment providers. For this reason, State ORP assets are not part of the retirement systems' trust funds for financial statement purposes. Contributions to the State ORP are at the same rates as SCRS. A direct remittance is required from the employers to the member's account with the investment providers for the employee contribution and a portion of the employer contribution (5 percent). A direct remittance is also required to SCRS for the remaining portion of the employer contribution and an incidental death benefit contribution, if applicable, which is retained by SCRS.

Benefits

Benefit terms are prescribed in Title 9 of the South Carolina Code of Laws. PEBA does not have the authority to establish or amend benefit terms without a legislative change in the code of laws. Key elements of the benefit calculation include the benefit multiplier, years of service, and average final compensation. A brief summary of the benefit terms is presented below.

South Carolina Retirement System – A Class Two member who has separated from service with at least five or more years of earned service is eligible for a monthly pension at age 65 or with 28 years credited service regardless of age. A member may elect early retirement with reduced pension benefits payable at age 55 with 25 years of service credit. A Class Three member who has separated from service with at least eight or more years of earned service is eligible for a monthly pension upon satisfying the Rule of 90 requirement that the total of the member's age and the member's creditable service equals at least 90 years. Both Class Two and Class Three members are eligible to receive a reduced deferred annuity at age 60 if they satisfy the five- or eight-year earned service requirement, respectively. An incidental death benefit is also available to beneficiaries of active or retired members of employees who participate in the death benefit program.

The annual retirement allowance of eligible retirees or their surviving annuitants is increased by the lesser of 1% or \$500 every July 1. Only those annuitants in receipt of a benefit on July 1 of the preceding year are eligible to receive the increase. Members who retire under the early retirement provisions at age 55 with 25 years of service are not eligible for the benefit adjustment until the second July 1 after reaching age 60 or the second July 1 after the date they would have had 28 years of service credit had they not retired.

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Contributions

Contributions are prescribed in Title 9 of the South Carolina Code of Laws. If the scheduled employee and employer contributions provided in statute, or the rates last adopted by the board, are insufficient to maintain the amortization period set in statute, the board shall increase employer contribution rates as necessary.

After June 30, 2027, if the most recent annual actuarial valuation of the Systems for funding purposes shows a ratio of the actuarial value of system assets to the actuarial accrued liability of the system (the funded ratio) that is equal to or greater than eighty-five percent, then the board, effective on the following July first, may decrease the then current contribution rates upon making a finding that the decrease will not result in a funded ratio of less than eighty-five percent. If contribution rates are decreased pursuant to this provision, and the most recent annual actuarial valuation of the system shows a funded ratio of less than eighty-five percent, then effective on the following July first, and annually thereafter as necessary, the board shall increase the then current contribution rates until a subsequent annual actuarial valuation of the system shows a funded ratio that is equal to or greater than eighty-five percent.

The Retirement System Funding and Administration Act establishes a ceiling on employee contribution rates at 9 percent for SCRS. The employer contribution rates will continue to increase annually by 1 percent through July 1, 2022. The legislation's ultimate scheduled employer rate is 18.56 percent for SCRS. The amortization period is scheduled to be reduced one year for each of the next 10 years to a twenty year amortization period.

Required employee contribution rates for the fiscal year ended June 30, 2019, for the SCRS and State ORP plans, are as follows:

South Carolina Retirement System	
Employee class two	9.00%
Employee class three	9.00%
State ORP	
Employee	9.00%

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Contributions (Continued)

Required employer contribution rates for the fiscal years ended June 30, 2019, for the SCRS and State ORP plans, are as follows:

South Carolina Retirement System	
Employer class two	14.41%
Employer class three	14.41%
Employer incidental death benefit	0.15%
State ORP	
Employer*	14.41%
Employer incidental death benefit	0.15%

(*) Of this employer contribution, 5% of earnable compensation must be remitted by the employer directly to the ORP vendor to be allocated to the member's account with the remainder of the employer contribution remitted to the SCRS.

For the fiscal year ended June 30, 2019, the Fund's contributions to the SCRS plan amounted to \$286,802.

For the fiscal year ended June 30, 2019, Fund and Fund employees' contributions to the State ORP plan were as follows:

State ORP		
Employee required contribution	\$	44,275
Employer required contribution	\$	71,627
Percent contributed		100%

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Actuarial Assumptions and Methods

Actuarial valuations of the plan involve estimates of the reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and future salary increases. Amounts determined regarding the net pension liability are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. South Carolina state statute requires that an actuarial experience study be completed at least once in each five-year period. An experience report on the Systems was most recently issued for the period ending June 30, 2015.

The June 30, 2018, total pension liability (TPL), net pension liability (NPL), and sensitivity information shown in this report were determined by our consulting actuary, Gabriel, Roeder, Smith and Company (GRS) and are based on an actuarial valuation performed as of July 1, 2017. The total pension liability was rolled-forward from the valuation date to the plans' fiscal year end, June 30, 2018, using generally accepted actuarial principles.

Assumptions and methods used in the July 1, 2017, valuation for the System are as follows:

	SCRS
Actuarial cost method	Entry Age
Actuarial assumptions:	
Investment rate of return	7.25%
Projected salary increases	3.0% to 12.5% (varies by service)
Includes inflation at	2.25%
Benefit adjustments	lesser of 1% or \$500

The post-retiree mortality assumption is dependent upon the member's job category and gender. The base mortality assumptions, the 2016 Public Retirees of South Carolina Mortality table (2016 PRSC), was developed using the Systems' mortality experience. These base rates are adjusted for future improvement in mortality using published Scale AA projected from the year 2016.

Former Job Class	Males	Females
General Employees and Members of the General Assembly	2016 PRSC Males multiplied by 100%	2016 PRSC Females multiplied by 111%

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Actuarial Assumptions and Methods (Continued)

The long-term expected rate of return on pension plan investments is based upon 30 year capital market assumptions. The long-term expected rate of returns represent assumptions developed using an arithmetic building block approach primarily based on consensus expectations and market based inputs. Expected returns are net of investment fees. The expected returns, along with the expected inflation rate, form the basis for the target asset allocation adopted at the beginning of the 2018 fiscal year.

The long-term expected rate of return is produced by weighting the expected future real rates of return by the target allocation percentage and adding expected inflation and is summarized in the table on the following page. For actuarial purposes, the 7.25 percent assumed annual investment rate of return used in the calculation of the TPL includes a 5.00 percent real rate of return and a 2.25 percent inflation component.

The target allocation and best estimates of arithmetic real rates of return for each major asset class are summarized in the table on the following page.

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Actuarial Assumptions and Methods (Continued)

Asset Class	Target Asset Allocation	Expected Arithmetic Real Rate of Return	Long-Term Expected Portfolio Real Rate of Return
Global equity	47.0%		
Global public equity	33.0%	6.99%	2.31%
Private equity	9.0%	8.73%	0.79%
Equity options strategies	5.0%	5.52%	0.28%
Real assets	10.0%		
Real estate (private)	6.0%	3.54%	0.21%
Real estate (REITs)	2.0%	5.46%	0.11%
Infrastructure	2.0%	5.09%	0.10%
Opportunistic	13.0%		
GTAA/Risk parity	8.0%	3.75%	0.30%
Hedge funds (non-PA)	2.0%	3.45%	0.07%
Other opportunistic strategies	3.0%	3.75%	0.11%
Diversified credit	18.0%		
Mixed credit	6.0%	3.05%	0.18%
Emerging markets debt	5.0%	3.94%	0.20%
Private debt	7.0%	3.89%	0.27%
Conservative fixed income	12.0%		
Core fixed income	10.0%	0.94%	0.09%
Cash and short duration (net)	2.0%	0.34%	0.01%
	100%		
		Total expected real return	5.03%
		Inflation for actuarial purposes	2.25%
		Total expected nominal return	7.28%

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Net Pension Liability (Continued)

The total pension liability is calculated by the Systems' actuary, and each plan's fiduciary net position is reported in the Systems' financial statements. The net pension liability is disclosed in accordance with the requirements of GASB 67 in the Systems' notes to the financial statements and required supplementary information. Liability calculations performed by the Systems' actuary for the purpose of satisfying the requirements of GASB Nos. 67 and 68 are not applicable for other purposes, such as determining the plans' funding requirements.

Pension Expense

For the fiscal year ended June 30, 2019, the Fund recognized its proportionate share of collective pension expense of \$485,039 and recognition of deferred amounts from changes in proportionate share and differences between employer contributions and the proportionate share of total plan employer contributions of \$1,005,990 for a total of \$1,491,029 for the SCRS plan.

Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions

As of June 30, 2019, the Fund reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

South Carolina Retirement System	Deferred Outflows of Resources	Deferred Inflows of Resources
Differences between expected and actual experience	\$ 8,994	\$ 29,321
Changes of assumptions	197,678	-
Net difference between projected and actual earnings on pension plan investments	79,147	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	1,212,366	-
Employer contributions subsequent to the measurement date	286,802	-
Total	<u>\$ 1,784,987</u>	<u>\$ 29,321</u>

Fund contributions subsequent to the measurement date of \$286,802 for the SCRS plan are reported as deferred outflows of resources and will be recognized as a reduction of the net pension liability in the year ended June 30, 2020.

NOTES TO FINANCIAL STATEMENTS

NOTE 5. PENSION PLANS (CONTINUED)

Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions (Continued)

As of June 30, 2019, other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

South Carolina Retirement System

Year ended June 30:	
2020	\$ 1,200,855
2021	306,337
2022	(31,680)
2023	(6,648)

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS

Overview

The South Carolina Public Employee Benefit Authority (PEBA) was created by the South Carolina General Assembly as part of Act No. 278 effective July 1, 2012. PEBA is a state agency responsible for the administration and management of the state's employee insurance programs, other post-employment benefits trusts and retirement systems and is part of the State of South Carolina primary government.

The governing board of PEBA is a board of 11 members. The membership composition is three members appointed by the Governor, two members appointed by the President Pro Tempore of the Senate, two members appointed by the Chairman of the Senate Finance Committee, two members appointed by the Speaker of the House of Representatives and two members appointed by the Chairman of the House Ways and Means Committee. Individuals appointed to the PEBA board must possess certain qualifications. Members of the PEBA board serve for terms of two years and until their successors are appointed and qualify. Terms commence on July first of even numbered years. The PEBA board appoints the Executive Director. The laws of the State and the policies and procedures specified by the State for State agencies are applicable to all activities of PEBA. By law, the State Fiscal Accountability Authority (SFAA), which consists of five elected officials, also reviews certain PEBA Board decisions in administering the State Health Plan and other post-employment benefits (OPEB).

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Plan Description

The Other Post-Employment Benefits Trust Fund (OPEB Trust), refers to the South Carolina Retiree Health Insurance Trust Fund (SCRHITF), was established by the State of South Carolina as Act 195, which became effective on May 2008. The SCRHITF was created to fund and account for the employer costs of the State's retiree health and dental plans.

In accordance with Act 195, the SCRHITF is administered by the PEBA, Insurance Benefits and the State Treasurer is the custodian of the funds held in trust. The Board of Directors of PEBA has been designated as the Trustee.

The SCRHITF is a cost-sharing multiple-employer defined benefit plans. Article 5 of the State Code of Laws defines the plan and authorizes the Trustee to at any time adjust the plan, including its benefits and contributions, as necessary to insure the fiscal stability of the plan. In accordance with the South Carolina Code of Laws and the annual Appropriations Act, the State provides post-employment health and dental benefits to retired State and school district employees and their covered dependents.

Benefits

The SCRHITF is a healthcare plan that covers retired employees of the State of South Carolina, including all agencies, and public school districts. The SCRHITF provides health and dental insurance benefits to eligible retirees. 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 15-24 years of service for 50% employer funding.

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Contributions and Funding Policies

Section 1-11-710 of the South Carolina Code of Laws of 1976, as amended, requires the postemployment and long-term disability benefits to be funded through non-employer and employer contributions for active employees and retirees to the PEBA – Insurance Benefits. Non-employer contributions consist of an annual appropriation by the General Assembly and the statutorily required transfer from PEBA – Insurance Benefits reserves.

The SCRHITF is funded through participating employers that are mandated by State statute to contribute at a rate assessed each year by the Department of Administration Executive Budget Office on active employee covered payroll. The covered payroll surcharge for the year ended June 30, 2019, was 5.50 percent. The South Carolina Retirement System collects the monthly covered payroll surcharge for all participating employers and remits it directly to the SCRHITF. Other sources of funding for the SCRHITF also include the implicit subsidy, or age-related subsidy inherent in the healthcare premiums structure. The implicit subsidy represents a portion of the health care expenditures paid on behalf of the employer's active employees. For purposes of GASB Statement No. 75, this expenditure on behalf of the active employee is reclassified as a retiree health care expenditure so that the employer's contributions towards the plan reflect the underlying age-adjusted, retiree benefit costs. Non-employer contributions include the mandatory transfer of accumulated PEBA – Insurance Benefits' reserves and the annual appropriation budgeted by the General Assembly. It is also funded through investment income. For the fiscal year ended June 30, 2019, the Fund's contributions to the SCRHIT plan amounted to \$122,915.

GASB Statement No. 75 requires participating employers to recognize revenue in an amount equal to the employer's proportionate share of the change in the collective net OPEB liability arising from contributions to the OPEB plan during the measurement period from non-employer contributing entities for purposes other than the separate financing of specific liabilities to the OPEB plan. Therefore, employers should classify this revenue in the same manner as it classifies grants from other entities. For the fiscal year ended June 30, 2019, the Fund recognized \$30,167 as a non-operating revenue from contributions from non-employer contributing entities.

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Contributions and Funding Policies (Continued)

For purposes of measuring the net OPEB liability, deferred outflows and inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the SCRHITF, and additions to and deductions from the SCRHITF fiduciary net position have been determined on the same basis as they were reported by the SCRHITF. For this purpose, revenues are recognized when earned and expenses are recognized when incurred. Therefore, benefit and administrative expenses are recognized when due and payable. Investments are reported at fair value.

PEBA, Insurance Benefits issues audited financial statements and required supplementary information for the OPEB Trust Funds. This information is publicly available through the Insurance Benefits' link on PEBA's website at www.peba.sc.gov or a copy may be obtained by submitting a request to PEBA – Insurance Benefits, 202 Arbor Lake Drive, Columbia, SC 29223. PEBA is considered a division of the primary government of the state of South Carolina and therefore, OPEB Trust fund financial information is also included in the comprehensive annual financial report of the state.

Actuarial Assumptions and Methods

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future.

Projections of benefits for financial reporting purposes are based on the substantive plans (as understood by the employer and plan participants) and include the types of benefits provided at the time the valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point.

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Actuarial Assumptions and Methods (Continued)

Additional information as of the latest actuarial valuation for SCRHITF:

Valuation Date:	June 30, 2017
Actuarial Cost Method:	Entry Age Normal
Inflation:	2.25%
Investment Rate of Return:	4.00, net of OPEB Plan investment expense; including inflation.
Single Discount Rate:	3.62% as of June 30, 2018
Demographic Assumptions:	Based on the experience study performed for the South Carolina Retirement Systems for the 5-year period ending June 30, 2015.
Mortality:	For healthy retirees, the 2016 Public Retirees of South Carolina Mortality Table for Males and the 2016 Public Retirees of South Carolina Mortality Table for Females are used with fully generational mortality projections based on Scale AA from the year 2016. Multipliers are applied to the base tables based on gender and employment type.
Health Care Trend Rate:	Initial trend starting at 6.75% and gradually decreasing to an ultimate trend rate of 4.15% over a period of 14 years.
Retiree Participation:	79% for retirees who are eligible for funded premiums. 59% participation for retirees who are eligible for partial funded premiums. 20% participation for retirees who are eligible for non-funded premiums.
Notes:	There were no benefit changes during the year; the discount rate changed from 3.59% as of June 30, 2017, to 3.62% as of June 30, 2018.

Roll Forward Disclosure

The actuarial valuation was performed as of June 30, 2017. Update procedures were used to roll forward the total OPEB liability to June 30, 2018 (measurement date used for the Fund's reporting as of June 30, 2019).

Net OPEB Liability

The Net OPEB Liability (NOL) is calculated separately for each OPEB Trust Fund and represents that particular Trust's Total OPEB Liability (TOL) determined in accordance with GASB No. 74 less that Trust's fiduciary net position. The allocation of each employer's proportionate share of the collective Net OPEB Liability and collective OPEB Expense was determined using the employer's payroll-related contributions over the measurement period. This method is expected to be reflective of the employer's long-term contribution effort as well as be transparent to individual employers and their external auditors.

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Net OPEB Liability (Continued)

The following table represents the components of the net OPEB liability as of June 30, 2019:

	2019
Total OPEB liability	\$ 4,340,189
Plan fiduciary net position	343,142
Employer's net OPEB liability	\$ 3,997,047
Plan fiduciary net position as a percentage of the total OPEB liability	7.91%
Fund's proportionate share of the collective net OPEB liability	0.028207%

The TOL is calculated by the Trust's actuary, and each Trust's fiduciary net position is reported in the Trust's financial statements. The NOL is disclosed in accordance with the requirements of GASB No. 74 in the Trust's notes to the financial statements and required supplementary information. Liability calculations performed by the Trust's actuary for the purpose of satisfying the requirements of GASB Nos. 74 and 75 and are not applicable for other purposes, such as determining the Trust's funding requirements.

Single Discount Rate

The Single Discount Rate of 3.62% was used to measure the total OPEB liability for the SCRHITF. The accounting policy for this plan is to set the Single Discount Rate equal to the prevailing municipal bond rate. Due to the plan's investment and funding policies, the difference between a blended discount rate and the municipal bond rate would be less than several basis points (several hundredths of one percent).

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Long-term Expected Rate of Return

The long-term expected rate of returns represent assumptions developed using an arithmetic building block approach primarily based on consensus expectations and market based inputs. The expected returns, along with the expected inflation rate, form the basis for the target asset allocation adopted at the beginning of the 2017 fiscal year. The long-term expected rate of return is produced by weighting the expected future real rates of return by the target allocation percentage and adding expected inflation. This information is summarized in the following table:

Asset Class	Target Asset Allocation	Expected Arithmetic Real Rate of Return	Weighted Long- Term Expected Real Rate of Return
U.S. Domestic Fixed Income	80.00%	2.09%	1.67%
Cash	20.00%	0.84%	0.17%
Total	100.00%		1.84%
		Total expected weighted real return	1.84%
		Inflation for actuarial purposes	2.25%
		Total expected nominal return	4.09%
		Investment return assumption	4.00%

Sensitivity Analysis

The following table presents the SCRHITF's net OPEB liability calculated using a Single Discount Rate of 3.56%, as well as what the plan's net OPEB liability would be if it were calculated using a Single Discount Rate that is one percent lower or one percent higher:

<u>South Carolina Retiree Health Insurance Plan</u>		
<u>Sensitivity of the Net OPEB Liability to Changes in the Discount Rate</u>		
1% Decrease (2.62%)	Current Discount Rate (3.62%)	1% Increase (4.62%)
\$ 4,708,905	\$ 3,997,047	\$ 3,423,233

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Sensitivity Analysis (Continued)

Regarding the sensitivity of the SCRHITF's net OPEB liability to changes in the healthcare cost trend rates, the following table presents the plan's net OPEB liability, calculated using the assumed trend rates as well as what the plan's net OPEB liability would be if were calculated using a trend rate that is one percent lower or one percent higher:

<u>South Carolina Retiree Health Insurance Plan</u>		
<u>Sensitivity of the Net OPEB Liability to Changes in the Healthcare Cost Trend Rate</u>		
	Current Healthcare Cost Trend Rates	
1% Decrease (5.75% decreasing to 3.15%)	(6.75% decreasing to 4.15%)	1% Increase (7.75% decreasing to 5.15%)
\$ 3,288,924	\$ 3,997,047	\$ 4,912,518

OPEB Expense

For the fiscal year ended June 30, 2019, the Fund recognized its proportionate share of collective OPEB expense of \$485,039 and recognition of deferred amounts from changes in proportionate share and differences between employer contributions and the proportionate share of total plan employer contributions of \$223,366 for a total of \$7,839 for the SCRHITF plan.

NOTES TO FINANCIAL STATEMENTS

NOTE 6. OTHER POSTEMPLOYMENT BENEFITS (CONTINUED)

Deferred Outflows of Resources and Deferred Inflows of Resources

At June 30, 2019, the Fund reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

South Carolina Retiree Health Insurance Plan	Deferred Outflows of Resources	Deferred Inflows of Resources
	<u> </u>	<u> </u>
Differences between expected and actual experience	\$ 59,878	\$ 1,393
Changes of assumptions	-	325,480
Net difference between projected and actual earnings on OPEB plan investments	15,326	-
Changes in proportion and differences between employer contributions and proportionate share of contributions	50,911	45
Employer contributions subsequent to the measurement date	122,915	-
Total	<u><u>\$ 249,030</u></u>	<u><u>\$ 326,918</u></u>

Fund contributions subsequent to the measurement date of \$122,915 for the SCRHITF plan are reported as deferred outflows of resources and will be recognized as a reduction of the net OPEB liability in the year ended June 30, 2020.

As of June 30, 2019, other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

<u>South Carolina Retiree Health Insurance Plan</u>	
Year ended June 30:	
2020	\$ (39,523)
2021	(39,523)
2022	(39,523)
2023	(41,164)
2024	(43,765)
Thereafter	2,695

NOTES TO FINANCIAL STATEMENTS

NOTE 7. OPERATING LEASES

The Fund leases office space from a party outside of State government and this lease is accounted for as an operating lease. Rental expense under this lease for the year ended June 30, 2019, was \$254,337.

The future minimum lease payments due under this lease are as follows for the year ended June 30:

Year Ending June 30,	<u>Total Minimum Lease Payments</u>
2020	\$ 255,024
2021	264,224
2022	264,224
2023	264,224
2024	264,224
2025	264,224
	<u>\$ 1,576,144</u>

NOTE 8. RELATED PARTY TRANSACTIONS

The Fund has significant transactions with the State of South Carolina and various state agencies. Property and liability coverage is provided for a fee to various State agencies and within the State Fiscal Accountability Authority. The fees are recorded as revenues in the financial statements for the Fund. The tables on the following pages detail the insurance premiums received by the Fund from other state agencies and divisions of the State Fiscal Accountability Authority during the year ended June 30, 2019.

NOTES TO FINANCIAL STATEMENTS

NOTE 8. RELATED PARTY TRANSACTIONS (CONTINUED)

State Entity	Amount	State Entity	Amount
Adjutant General of South Carolina	\$ 258,212	Comptroller General	\$ 12,314
Admn. Agency Support Services	65,746	Confederate Relic Room	20,557
Administrative Law Court	2,723	Court of Appeal - Finance	82,528
Admn. Administration - OEPP	65,562	DDSN - Midlands Center	39,837
Admn. Division of General Services	477,959	DDSN - Pee Dee Center	45,102
Admn. Division of Technology Operations	196,669	DDSN - Whitten Village	56,134
Admn. Executive Budget Office	4,203	Department of Commerce	31,639
Admn. GS Facilities Management	500	Department of Corrections	2,537,476
Admn. GS State Fleet Management & IMS	1,424,087	Department of Education	5,197,044
Admn. Hunley Commission	4,011	Department of Juvenile Justice	602,844
Admn. Office of Human Resources	5,201	Department of Natural Resources	1,125,760
Admn. Office of the Executive Director	63,048	Department on Aging	18,563
Aeronautics Division	25,476	Department of Mental Health	1,916,905
Agriculture Department S.C.	101,548	Department of Motor Vehicles	167,898
Aiken Community Health	775	Department of Social Services	630,982
Alcohol & Other Drug Abuse Services	8,806	Department of Transportation	13,234,688
Anderson-Oconee Pickens	6,598	DHEC	1,454,698
Appellate Defense Commission	21,524	Disabilities & Special Needs	56,694
Archives & History Department	19,306	Disabilities & Special Needs Depts.	285,082
Arts Commission	15,049	Education Oversight Comm.	8,227
Attorney General Office	51,996	Election Commission	13,732
Berkeley County Mental Health	1,830	ETV/SDN	360,862
Blind Commission	25,075	Financial Institutions State Board	74
Charleston Dorchester Community	4,795	Financial Institute State Board - Finance	16,370
The Citadel	803,781	Forestry Commission	262,800
Clemson University	3,923,114	Francis Marion University	451,938
Coastal Carolina University	1,677,650	Governor's Office	13,837
Coastal Empire Mental Health Center	2,975	Governor's School for Science	81,652
College of Charleston	1,440,630	Greenville Mental Health	5,595
Columbia Area Mental Health Center	1,601	Health and Human Services Finance	174,692
Commission for Minority Affairs	7,250	Higher Education Tuition	1,699
Commission on Higher Education	25,944	Horry County Higher Education Comm.	9,392
Commission on Prosecution Coord.	19,565	House of Representatives	151,725

NOTES TO FINANCIAL STATEMENTS

NOTE 8. RELATED PARTY TRANSACTIONS (CONTINUED)

State Entity (continued)	Amount	State Entity	Amount
Human Affairs Comm.	\$ 11,887	S.C. First Steps	\$ 74,161
John De La Howe School	106,887	S.C. Gov. School for Arts and Humanities	62,296
Lander University	363,533	S.C. Malpractice Patients Comp. Fund	8,679
Legislative Audit Council	5,734	S.C. Office of Inspector General	5,048
Legislative Council	3,252	S.C. Rural Infrastructure Authority	8,617
Legislative Services Agency	19,474	S.C. School for the Deaf and Blind	194,094
Lexington County Community Mental Health	1,116	S.C. State Accident Fund	9,252
Lieutenant Governor's Office	20,570	S.C. State Senate	34,974
LLR - Architectural Exam Bd.	229,725	S.C. State University	363,490
Medical University Hospital Authority	3,951,496	S.C. Transportation Infrastructure Bank	4,988
Medical University of S.C.	2,164,178	S.C. Worker's Compensation Comm.	16,396
MUSC	7,019,077	Sea Grant Consortium, S.C.	4,143
Office of Regulatory Staff	36,784	Secretary of State	13,095
Orangeburg Area Mental Health	2,094	SFAA Administration	29,684
Parks Recreation & Tourism	727,932	SFAA Procurement Services Office	20,031
Patriots Point Development Authority	120,464	SLED	490,378
Pee Dee Mental Health	4,030	South Carolina Conservation Bank	7,544
Piedmont Mental Health Center	4,320	South Carolina Jobs	5,181
Probation, Parole & Pardon Services	288,398	South Carolina Public Service	346,171
Procurement Review Panel	7,093	Spartanburg Area Mental Health	2,002
Public Employee Benefits Authority	68,287	State Auditor's Office	6,920
Public Safety Department	1,042,283	State Board of Financial Institutions	258
Public Service Commission	18,287	State Ethics Commission	11,749
Retirement System Investment Comm.	20,753	State Housing Finance & Dev. Auth	31,821
Revenue and Fiscal Affairs Office	35,004	State Library	13,998
Revenue and Taxation Department	134,660	State Museum Commission	25,165
Santee Wateree Mental Health	1,775	State Treasurer's Office	20,481
S.C. Criminal Justice Academy	88,065	Technology & Comp Edy. St. Bd.	76,534
S.C. Dept. of Consumer Affairs	17,886	Tobacco Settlement Revenue Management	2,865
S.C. Dept. of Employment and Workforce	235,755	Tri-County Community Mental Health	3,556
S.C. Dept. of Insurance	13,330	University of S.C. - Aiken	185,914

NOTES TO FINANCIAL STATEMENTS

NOTE 8. RELATED PARTY TRANSACTIONS (CONTINUED)

State Entity (continued)	Amount	State Entity	Amount
University of South Carolina	\$ 4,442,344	Wil Lou Gray Opportunity School	\$ 49,938
USC - Beaufort Campus	104,780	Winthrop University	620,817
USC - Lancaster Campus	39,548		
USC - Salkehatchie	64,601		
USC - School of Medicine	886,693		
USC - School of Medicine Greenville	17,406		
USC - Spartanburg	215,031		
USC - Sumter Campus	42,156		
Vocational Rehabilitation Dept	467,195		
Waccamaw Mental Health Center	2,050		
		Total premiums received from other state entities	<u>\$ 65,618,722</u>

Amounts recorded as premiums receivable in the financial statements of the Fund due from the state and other state entities as of June 30, 2019, are as follows:

State Entity	Amount	State Entity	Amount
Adjutant General	\$ 335,060	Public Employee Benefit Authority	\$ 82,470
Arts Commission	17,004	Public Safety Department	1,232,205
The Citadel	31	Revenue & Taxation Dept.	178,773
Clarendon Memorial Hospital	401	S.C. Malpractice Patients Comp. Fund	10,806
Clemson University	4,656,136	S.C. Criminal Justice Academy	113,055
Coastal Carolina University	2,007,793	S.C. School for the Deaf and Blind	15
College of Charleston	1,643,887	S.C. State Constables Association	4,925
Court of Appeal - Finance	99,574	S.C. State University	437,563
Department of Education	5,439,697	Sea Grant Consortium, S.C.	5,463
Department of Juvenile Justice	680,685	SLED	596,134
Department of Mental Health	2,241,874	South Carolina Public Service	11,243
Department of Motor Vehicle	239,367	State Auditor's Office	8,628
Department of Transportation	53	State Ethics Commission	14,538
Disabilities & Special Needs	67,434	State Library	17,028
Florence Darlington Technical College	277,336	State Museum Commission	34,205
Greenville Technical College	145	Technical College of the Low Country	132,563
Francis Marion University	5,169	Trident Technical College	591,179
Health and Human Services Finance	208,533	University of S.C. - Aiken	208,972
Horry - Georgetown Technical College	268,267	University of South Carolina	5,172,768
Lander University	451,660	USC - Spartanburg	241,756
Medical University Hospital Authority	745	Vocational Rehabilitation Department	539,139
Midlands Tech College	14,693	Winthrop University	184
Office of Regulatory Staff	24,975	York Technical College	172,198
Patriots Point Dev. Authority	137,767		
		Premiums due from other state entities, net	<u>\$ 28,624,096</u>

NOTES TO FINANCIAL STATEMENTS

NOTE 8. RELATED PARTY TRANSACTIONS (CONTINUED)

The Fund has financial transactions with various State agencies during the fiscal year. Significant payments were made to SFAA and the Department of Administration (DOA) for printing, telephone, interagency mail, data processing services, purchasing, record maintenance, internal audit and personnel services and to the South Carolina Public Employee Benefit Authority for retirement and insurance plan contributions.

NOTE 9. COMMITMENTS AND CONTINGENCIES

By the nature of its operations and responsibilities as an insurer, the Fund has been named in a number of lawsuits, many of which are pending. A provision has been made in the financial statements for the payment of routine claims. Management is not aware of any other claims that, in their opinion, would have a material effect on the financial statements and, therefore, no liability has been recorded.

As a result of the 2004-2005 Appropriations Act Proviso 63.47, the Fund is to provide funds to cover legal defense costs of the State associated with the Abbeville School Funding litigation case. During the year ended June 30, 2019, the Fund did not incur any legal defense costs associated with this Proviso. However, the ultimate amount of this liability is not known as of the date of our report.

As a result of the 2006-2007 Appropriations Act Proviso 63.33, the Fund is to provide funds to cover legal defense costs of the State associated with the Prison Mental Health Care litigation case. During the year ended June 30, 2019, the Fund did not incur any legal defense costs associated with the case. However, the ultimate amount of this liability is not known as of the date of our report.

As a result of the 2015-2016 Appropriations Act Proviso 59.9, the Fund is to provide up to \$50,000 of opposing attorney fees and court costs as ordered by the court in those cases in which the Attorney General defends one or more public officers in their official capacities. During the year ended June 30, 2019, the Fund did not incur any legal defense costs associated with the case. However, the ultimate amount of this liability is not known as of the date of our report.

NOTE 10. RISK MANAGEMENT

The Fund is exposed to various risks of loss and maintains State or commercial insurance coverage for each of those risks except for certain types of risks for which it is self-insured (these risks are further described herein). 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 coverage in the prior year.

NOTES TO FINANCIAL STATEMENTS

NOTE 10. RISK MANAGEMENT (CONTINUED)

The Fund pays insurance premiums to itself, certain other State agencies and commercial insurers to cover risks that may occur in normal operations. The insurers promise to pay to or on behalf of the insured for covered 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:

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

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

The Fund acts as an insurance company in that it issues policies, accumulates 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. Theft of, damage to, or destruction of assets;
2. Auto liability for state and non-state owned vehicles; and
3. General torts.

State agencies and other entities are the primary participants in the Fund.

The Fund has recorded insurance premium expense regarding its internal operations in the applicable administrative expense categories. The Fund has not transferred the portion of the risk of loss related to insurance policy deductibles and limits.

NOTES TO FINANCIAL STATEMENTS

NOTE 10. RISK MANAGEMENT (CONTINUED)

The Fund purchases insurance and reinsurance and separately reports the related reinsurance premium and premium expenses. Insurance is purchased to cover risks where the Fund has limited expertise (aircraft insurance and ocean marine insurance). Reinsurance is purchased to limit the Fund's liability for catastrophic loss (property reinsurance), to obtain specialized engineering services (boiler and machinery reinsurance), or to obtain services for which the Fund is not adequately staffed (automobile liability reinsurance). The Fund self-insures Tort Liability Insurance, Automobile Physical Damage Insurance, Medical Professional Liability and the self-insured retention for Property, Inland Marine, and Boiler and Machinery Insurance.

Property reinsurance for catastrophic losses is purchased for losses above the following loss levels:

- \$10,000,000 per occurrence; \$15,000,000 in the aggregate; \$1,000,000 trailing after both occurrence and aggregate

Reinsurance permits partial recovery of losses from reinsurers; however, the Fund, as the direct insurer of the risks, remains primarily liable. As of June 30, 2019, there have been no catastrophe claims in excess of the limit of reinsurance purchased.

NOTE 11. RECONCILIATION OF CLAIMS LIABILITY

The Fund reports liabilities when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. Amounts for allocated and unallocated claims adjustment expenses have been included in the calculation of the unpaid claims liability. The liability is reported net of receivables for salvage, subrogation, and reinsurance. The unpaid policy claims liability includes a provision for reported claims and claims incurred but not reported. The liability for claims incurred but not reported is an actuarial estimate based on the most current historical claims experience. This estimate does not necessarily result in an exact amount. The Fund continually reviews estimates of liabilities for incurred claims and revises those estimates as changes occur.

NOTES TO FINANCIAL STATEMENTS

NOTE 11. RECONCILIATION OF CLAIMS LIABILITY (CONTINUED)

Changes in the balances of claims liabilities during the past two fiscal years were as follows:

	2019	2018
	<u>(in thousands)</u>	<u>(in thousands)</u>
Unpaid claims and claims adjustment expenses at the beginning of the year	\$ 292,050	\$ 282,735
Incurring claims and claim adjustment expenses:		
Provision for insured events of the current year	29,322	45,565
Increase in provision for insured events of prior years	92,238	61,274
Total incurred claims and claim adjustment expenses	<u>121,560</u>	<u>106,839</u>
Payments:		
Claims and claim adjustment expenses attributable to insured events of the current year	22,425	41,593
Claims and claim adjustment expenses attributable to insured events of prior years	70,544	55,931
Total payments	<u>92,969</u>	<u>97,524</u>
Total unpaid claims and claim adjustment expenses at the end of the year	<u>320,641</u>	<u>292,050</u>
The above totals are comprised of the following:		
Claims payable	207,947	190,176
Claims incurred but not reported	112,694	101,874
Total claims payable	<u>\$ 320,641</u>	<u>\$ 292,050</u>

REQUIRED SUPPLEMENTARY INFORMATION

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUND'S PROPORTIONATE
SHARE OF THE NET PENSION LIABILITY
FOR THE PLAN YEAR ENDED JUNE 30,**

South Carolina Retirement System

Plan Year Ended June 30,	Fund's proportion of the net pension liability	Fund's proportionate share of the net pension liability	Fund's covered payroll	Fund's share of the net pension liability as a percentage of its covered payroll	Plan fiduciary net position as a percentage of the total pension liability
2018	0.022237%	\$ 4,982,507	\$ 2,946,642	169.1%	54.1%
2017	0.030862%	6,947,490	2,513,166	276.4%	53.3%
2016	0.027126%	5,794,070	2,211,011	262.1%	52.9%
2015	0.024571%	4,660,099	2,035,873	228.9%	57.0%
2014	0.024011%	4,133,937	1,981,230	208.7%	59.9%
2013	0.024011%	4,306,757	2,576,340	167.2%	56.4%

Notes to the Schedule:

The schedule will present 10 years of information once it is accumulated.

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUND PENSION CONTRIBUTIONS
FOR THE FISCAL YEAR ENDED JUNE 30,**

South Carolina Retirement System

Fiscal Year Ended June 30,	Statutorily required contribution	Contributions in relation to the statutorily required contribution	Contribution deficiency (excess)	Fund's covered payroll	Contributions as a percentage of covered payroll
2019	\$ 286,802	\$ 286,802	-	\$ 1,969,793	14.56%
2018	399,561	399,561	-	2,946,642	13.56%
2017	290,522	290,522	-	2,513,166	11.56%
2016	241,000	241,000	-	2,211,011	10.90%
2015	221,910	221,910	-	2,035,873	10.90%
2014	210,010	210,010	-	1,981,230	10.60%

Notes to the Schedule:

The schedule will present 10 years of information once it is accumulated.

Actuarial assumptions used in determining the statutorily required contribution are as follows:

System	SCRS
Calculation date	July 1, 2016
Actuarial cost method	Entry Age Normal
Asset valuation method	5-year Smoothed
Amortization method	Level % of pay
Amortization period	30 years variable, but not to exceed 30 years
Investment return	7.50%
Inflation	2.25%
Salary increases	3.00% plus step-rate increases for members with less than 21 years of service
Mortality	2016 Public Retirees of South Carolina Mortality Tables for Males and Females, both projected at Scale AA from the year 2016. Male rates are multiplied by 100% for non-educators and 92% for educators. Female rates multiplied by 111% for non-educators and 98% for educators.

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUND'S PROPORTIONATE
SHARE OF THE NET OPEB LIABILITY
FOR THE PLAN YEAR ENDED JUNE 30,**

South Carolina Retiree Health Plan

Plan Year Ended June 30,	Fund's proportion of the net OPEB liability	Fund's proportionate share of the net OPEB liability	Fund's covered payroll	Fund's share of the net OPEB liability as a percentage of its covered payroll	Plan fiduciary net position as a percentage of the total OPEB liability
2018	0.028207%	\$ 3,997,047	\$ 2,119,212	188.6%	7.91%
2017	0.028939%	3,919,501	2,259,625	173.5%	7.60%
2016	0.029264%	4,233,920	2,381,426	177.8%	6.62%

Notes to the Schedule:

The schedule will present 10 years of information once it is accumulated.

The discount rate changed from 3.59% as of June 30, 2017 to 3.62% as of June 30, 2018.

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUND OPEB CONTRIBUTIONS
FOR THE FISCAL YEAR ENDED JUNE 30,**

South Carolina Retiree Health Plan

Fiscal Year Ended June 30,	Statutorily required contribution	Contributions in relation to the statutorily required contribution	Contribution deficiency (excess)	Fund's covered payroll	Contributions as a percentage of covered payroll
2019	\$ 122,915	\$ 122,915	\$ -	\$ 2,234,819	5.50%
2018	112,954	112,954	-	2,119,212	5.33%
2017	120,438	120,438	-	2,259,625	5.33%

Notes to the Schedule:

The schedule will present 10 years of information once it is accumulated.

The actuarial assumption used in determining the statutorily required contribution are disclosed in Note 6 of the notes to the financial statements.

COMPLIANCE SECTION



**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***

**To Mr. George L. Kennedy, III, CPA
State Auditor
South Carolina Office of the State Auditor
Columbia, South Carolina**

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the **South Carolina State Fiscal Accountability Authority Insurance Reserve Fund** (the "Fund"), a fund of the South Carolina State Fiscal Accountability Authority, as of and for the year ended June 30, 2019, and the related notes to the financial statements, which collectively comprise the Fund's basic financial statements, and have issued our report thereon dated September 23, 2019.

Internal Control Over Financial Reporting

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

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. 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 internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

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

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.

A handwritten signature in black ink that reads "Mauldin & Jenkins, LLC". The signature is written in a cursive, flowing style.

Columbia, South Carolina
September 23, 2019

**SOUTH CAROLINA STATE FISCAL ACCOUNTABILITY AUTHORITY
INSURANCE RESERVE FUND**

**SCHEDULE OF FINDINGS AND RESPONSES
FOR THE FISCAL YEAR ENDED JUNE 30, 2019**

**SECTION I
SUMMARY OF AUDIT RESULTS**

Financial Statements

Type of auditor's report issued

Unmodified

Internal control over financial reporting:

Material weaknesses identified?

Yes No

Significant deficiencies identified not considered
to be material weaknesses?

Yes None Reported

Noncompliance material to financial statements noted?

Yes No

**SECTION II
FINANCIAL STATEMENT FINDINGS AND RESPONSES**

None reported

**SECTION III
STATUS OF PRIOR YEAR AUDIT FINDINGS**

None reported