



BASIC FINANCIAL STATEMENTS, REQUIRED  
SUPPLEMENTARY INFORMATION, AND  
OTHER FINANCIAL INFORMATION

West Virginia Public Employees Insurance Agency  
Years Ended June 30, 2009 and 2008  
With Report of Independent Auditors

Ernst & Young LLP

West Virginia Public Employees Insurance Agency

Basic Financial Statements, Required Supplementary Information,  
and Other Financial Information

Years Ended June 30, 2009 and 2008

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## Report of Independent Auditors

The Finance Board  
West Virginia Public Employees Insurance Agency

We have audited the accompanying basic financial statements of the West Virginia Public Employees Insurance Agency (PEIA), an enterprise fund of the State of West Virginia, as of June 30, 2009 and 2008, and for the years then ended, as listed in the table of contents. These financial statements are the responsibility of PEIA's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We were not engaged to perform an audit of PEIA's internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of PEIA's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinions.

As discussed in Note 1, the financial statements of PEIA are intended to present the financial position, the changes in financial position, and the cash flows of only that portion of the business-type activities of the State of West Virginia that is attributable to the transactions of PEIA. They do not purport to, and do not, present fairly the financial position of the State of West Virginia as of June 30, 2009 and 2008, the changes in its financial position, or, where applicable, its cash flows for the years then ended, in conformity with accounting principles generally accepted in the United States.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of PEIA, an enterprise fund of the State of West Virginia, as of June 30, 2009 and 2008, and the changes in its financial position and its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

As more fully described in Notes 6 and 9 to the financial statements, in fiscal year 2008, PEIA adopted Governmental Accounting Standards Board (GASB) Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, which changed the methodology for capitalization of computer software costs, and GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (GASB 45), which changed the accounting and reporting for postemployment benefits.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 4, 2010, on our consideration of PEIA's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our 2009 audit.

Management's discussion and analysis on pages 3 through 8 and the supplemental schedule of Ten-Year Claims Development Information on page 40 are not a required part of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures to management's discussion and analysis on pages 3 through 8 and the Ten-Year Claims Development Information on page 40, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit of the basic financial statements was performed for the purpose of forming an opinion on the basic financial statements of PEIA, taken as a whole. Other financial information listed in the table of contents is presented for purposes of additional analysis and is not a required part of the basic financial statements of PEIA. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

A handwritten signature in cursive script that reads 'Ernst & Young LLP'.

February 4, 2010

# West Virginia Public Employees Insurance Agency

## Management's Discussion and Analysis

Year Ended June 30, 2009

This section of the annual financial report of the West Virginia Public Employees Insurance Agency (PEIA) presents a discussion and analysis of the financial performance of PEIA for the year ended June 30, 2009. Please read it in conjunction with the basic financial statements, which follow this section.

### **OVERVIEW OF THE FINANCIAL STATEMENTS**

PEIA's basic financial statements are prepared in accordance with U.S. generally accepted accounting principles for governmental entities. The primary purpose of PEIA is to provide group health and prescription drug insurance for the employees of state agencies, colleges and universities, county school boards, and other governmental units as set forth in the West Virginia Public Employees Insurance Act of 1971 as amended. PEIA operates in a manner similar to any other insurance company. PEIA is an enterprise fund of the State of West Virginia and is combined with other similar funds to comprise the enterprise funds of the State of West Virginia. The basic financial statements are presented on the accrual basis of accounting. The three basic financial statements presented within the financial statements are as follows:

*Statement of Net Assets* – This statement presents information reflecting PEIA's assets, liabilities, and net assets. Net assets represent the amount of total assets less total liabilities. The statement of net assets is categorized as to current and noncurrent assets and liabilities. For purposes of the basic financial statements, current assets and liabilities are those assets and liabilities with immediate liquidity or which are collectible or become due within 12 months of the statement date.

*Statement of Revenues, Expenses, and Changes in Net Assets* – This statement reflects PEIA's operating revenues and expenses, as well as nonoperating revenues during the fiscal year. The major source of operating revenues is premium income, while major expense areas include medical and prescription drug claims costs. The change in net assets for an enterprise fund is similar to net profit or loss for any other insurance company.

*Statement of Cash Flows* – The statement of cash flows is presented on the direct method of reporting which reflects cash flows from operating, capital, and investing activities. Cash collections and payments are reflected in this statement to arrive at net increase or decrease in cash for the fiscal year.

# West Virginia Public Employees Insurance Agency

## Management's Discussion and Analysis (continued)

### FINANCIAL HIGHLIGHTS

The following tables summarize the financial position and the changes in financial position as of and for the years ended June 30:

				Change 2009 – 2008		Change 2008 – 2007	
	2009	2008	2007	Amount	Percent	Amount	Percent
Cash and cash equivalents	\$ 2,700,245	\$ 15,425,536	\$ 18,657,241	\$ (12,725,291)	(82.5)%	\$ (3,231,705)	(17.3)%
Equity position in internal investment pool	33,294,218	40,382,507	141,259,154	(7,088,289)	(17.6)	(100,876,647)	(71.4)
Premium receivable	26,466,755	14,355,794	13,564,676	12,110,961	84.4	791,118	5.8
Other current assets	6,682,408	13,730,357	7,296,181	(7,047,949)	(51.3)	6,434,176	88.2
Total current assets	69,143,626	83,894,194	180,777,252	(14,750,568)	(17.6)	(96,883,058)	(53.6)
Equity position in internal investment pools	115,072,492	122,360,685	169,996,583	(7,288,193)	(6.0)	(47,635,898)	(28.0)
Equity position in internal investment pool – restricted	7,738,658	7,738,658	3,942,911	–	–	3,795,747	96.3
Capital assets, net	6,495,407	5,153,924	568,064	1,341,483	26.0	4,585,860	807.3
Total assets	198,450,183	219,147,461	355,284,810	(20,697,278)	(9.4)	(136,137,349)	(38.3)
Claims payable	56,461,892	51,276,816	52,999,509	5,185,076	10.1	(1,722,692)	(3.3)
Other current liabilities	25,017,598	56,827,048	124,267,822	(31,809,450)	(56.0)	(67,440,774)	(54.3)
Total current liabilities	81,479,490	108,103,864	177,267,331	(26,624,374)	(24.6)	(69,163,466)	(39.0)
Noncurrent liabilities:							
Premium stabilization fund	7,738,658	7,738,658	3,942,911	–	–	3,795,747	96.3
Total liabilities	89,218,148	115,842,522	181,210,242	(26,624,374)	(23.0)	(65,367,720)	(36.1)
Net assets-invested in capital assets	6,495,407	5,153,924	568,064	1,341,483	26.0	4,585,860	807.3
Net assets-unrestricted	102,736,628	98,151,015	173,506,504	4,585,613	4.7	(75,355,490)	(43.4)
Total net assets	\$ 109,232,035	\$ 103,304,939	\$ 174,074,568	\$ 5,927,096	5.7%	\$ (70,769,630)	(40.7)%
Premium revenue	\$ 464,263,863	\$ 416,040,777	\$ 466,232,421	\$ 48,223,086	11.6%	\$ (50,191,644)	(10.8)%
Less: Payments to managed care organizations and life reinsurance premiums	(60,186,506)	(60,595,834)	(59,228,061)	409,328	0.7	(1,367,773)	(2.3)
Net premium revenue	404,077,357	355,444,943	407,004,360	48,632,414	13.7	(51,559,417)	(12.7)
Administrative fees, net	4,693,824	4,487,011	4,450,017	206,813	4.6	36,994	0.8
Total operating revenues	408,771,181	359,931,954	411,454,377	48,839,227	13.6	(51,522,423)	(12.5)
Claims expense, net	371,015,676	419,370,075	359,512,303	(48,354,399)	(11.5)	59,857,772	16.6
Administrative service fees	14,810,235	12,820,798	12,723,779	1,989,437	15.5	97,019	0.8
Other expenses	10,107,845	6,764,371	7,435,296	3,343,474	49.4	(670,925)	(9.0)
Total operating expenses	395,933,756	438,955,244	379,671,378	(43,021,488)	(9.8)	59,283,866	15.6
Operating income (loss)	12,837,425	(79,023,290)	31,782,999	91,860,715	116.2	(110,806,289)	(348.6)
Supplemental appropriation	–	–	6,700,000	–	–	(6,700,000)	(100.0)
Litigation settlement, net	–	–	3,085,000	–	–	(3,085,000)	(100.0)
Transfer out	(7,320)	–	(80,487,422)	(7,320)	(100.0)	80,487,422	100.0
Net investment (loss) income	(6,903,009)	7,978,307	22,126,245	(14,881,316)	(186.5)	(14,147,938)	(63.9)
Total nonoperating (loss) income	(6,910,329)	7,978,307	(48,576,177)	(14,888,636)	(186.6)	56,554,484	116.4
Change in net assets	5,927,096	(71,044,983)	(16,793,178)	76,972,079	108.3	(54,251,805)	(323.1)
Net assets, beginning of year	103,304,939	174,074,569	190,867,747	(70,769,630)	(40.7)	(16,793,178)	(8.8)
Change in accounting principle for other postemployment benefits	–	275,353	–	(275,353)	(100.0)	275,353	100.0
Net assets, end of year	\$ 109,232,035	\$ 103,304,939	\$ 174,074,569	\$ 5,927,096	5.7%	\$ (70,769,630)	(40.7)%

## West Virginia Public Employees Insurance Agency

### Management's Discussion and Analysis (continued)

The current portion of equity position in internal investment pool and cash and cash equivalents decreased \$19.8 million as the result of \$26.1 million used in operations. \$6.9 million was used to cover investment losses, and \$7.3 million was provided from liquidation of investments related to equity position in internal investment pool. \$2.8 million of cash and cash equivalents was used for the purchase of capital assets, and \$8.7 million was advanced to the Retiree Health Benefit Trust (RHBT).

In the previous year, the decrease of cash and cash equivalents and the current portion of equity position in internal investment pool is a result of \$33.3 million used in operations. \$10.3 million came from investment returns net of reinvestments, \$61.9 million was provided from liquidation of investments, and \$16.6 million used for purchase of investments in the equity position in internal investment pool. \$5.0 million of cash and cash equivalents was used for the purchase of capital assets, \$108.2 million was transferred to RHBT, \$10.8 million was advanced to RHBT, \$1.4 million was collected from the prior year appropriation, and \$3.8 million was transferred to noncurrent accounts.

Premium receivable at June 30, 2009, was \$12.1 million more than the prior year because several large employers did not remit their premium until after year-end. Premiums receivable at June 30, 2008, was \$.8 million more than the prior year which is an insignificant increase.

At the current year-end, other current assets were down \$7.0 million because the \$7.2 million advance to RHBT in the prior year had been collected, prescription rebates receivable were up \$.5 million and provided refunds receivable were down \$.3 million. At year-end 2008, other current assets were up \$6.4 million due to an increase in advances to RHBT for \$7.2 million and prescription rebates receivable of \$.8 million less the collection of prior year appropriations of \$1.4 million.

Claims payable increased \$5.2 million due to increased enrollment and medical cost inflation. For fiscal year 2008, the liability decreased approximately \$1.7 million due to a large pay down of the claims inventory.

Other current liabilities decreased \$31.8 million mainly resulting from a reduction of premium deficiency reserve for the new year by \$27.7 million, \$4.7 million decrease in accounts payable, \$1.9 million reduction of accrued liabilities, less an advance from RHBT of \$1.5 million and \$1.0 million increase in unearned revenue.

## West Virginia Public Employees Insurance Agency

### Management's Discussion and Analysis (continued)

In the prior year, other current liabilities decreased \$67.4 million resulting from the transfer of \$48.2 million prior year excess reserves to RHBT, increased by the accrual of \$43.3 million premium deficiency reserve, \$5.3 million increase in accounts payable less a \$2.8 million reduction of unearned revenue, \$3.6 million reduction of the amount due to RHBT, and \$1.5 million reduction of accrued liabilities.

In 2009, the increase in net assets resulted primarily from an increase in premium revenues of \$48.2 million over prior year and lower claims costs, less investment losses. The previous year decline resulted from the recognition of a premium deficiency reserve of \$43.3 million, higher than anticipated claims expenses, and lower investment earnings.

Net premiums increased \$48.6 million as a result of a reduction in the passthrough of postemployment benefit funding to RHBT, a \$6.8 million decrease in provision for uncollectible accounts, and changes in policy holder counts. In 2008, the premium decrease of \$51.6 million was primarily due to accrued actuarial liability funding of approximately \$39.0 million taken from PEIA premiums to RHBT for the first time in 2008.

Medical and prescription drug claims were 94% of total plan operating expenses for the three-year period. In the current year, claims expense was reduced by \$27.7 million to adjust the year-end 2009 premium deficiency reserve. Additionally, claims experience indicates a 5.8% increase in medical claims and a 6.8% increase in drug claims, net of premium deficiency. Fiscal year 2008 claims expense includes a \$43.3 million premium deficiency charge. Claims experience indicated a 10.2% increase in medical claims and a 11.0% decrease in drug claims for a combined 4.6% increase.

Administrative service fees and other expenses have averaged approximately 5% to 6% of plan operating expenses for the three-year period. Administrative service fees expense increased 15.5% due to replacement of old contracts with new higher fee contracts, while other expenses increased 49.4% primarily due to a \$0.9 million increase in wellness spending and a \$1.1 million increase in depreciation relating to a new computer system. In the prior year, administrative service fees expense was level, while other expenses decreased 9.0% primarily due to 2008 professional service fees being capitalized as software costs.

There were no supplemental appropriations from the State in 2009 or 2008. Supplemental appropriations granted by the State Code in 2007 were \$6.7 million.

There were no litigation settlements in 2009 and 2008. A settlement of \$3.0 million was reached in 2007 between PEIA and its former Prescription Benefit Manager.



## West Virginia Public Employees Insurance Agency

### Management's Discussion and Analysis (continued)

As a result of fiscal year 2007 earnings, PEIA's reserve levels were increased beyond the level allowed by State Code requiring a transfer which was \$52.8 million larger than the prior year amount. In 2009 and 2008, the PEIA reserve levels did not reach the threshold requiring such a transfer.

PEIA sustained a net investment loss in fiscal year 2009, due to market value declines, resulting in a \$14.9 million reduction in revenue from the prior year. Net investment income decreased \$14.1 million in fiscal year 2008 due to lower average investible balances and the economic downturn which negatively impacted the rate of return on investments.

Net assets increased \$5.9 million in fiscal year 2009. The 2009 increase resulted primarily from a reduction of claims expense of \$27.7 million to adjust the year end premium deficiency reserve, lower than expected claims expenses, while partially offset by investment losses. When the reduction of the premium deficiency is excluded, current year net asset change becomes negative \$21.8 million. Premium rate increases totaling \$6.0 million were adopted for the current year. The Financial Plan for 2009 indicated a decrease in total net assets of \$46.8 million. However, it did not include the \$27.7 million reduction of expense related to the premium deficiency reserve. Total claims costs for current year were \$18.4 million less, investment loss was \$6.9 million more, and non-claims expenses were \$0.8 million more than plan.

Net assets decreased approximately \$71.0 million in the previous year. The 2008 decrease resulted primarily from the recognition of a premium deficiency reserve of \$43.3 million, higher than anticipated claims expense, and lower investment earnings. When the premium deficiency reserve is excluded, the loss becomes \$27.5 million. No premium rate increases were adopted for the 2008 year. The Financial Plan indicated a decrease in total net assets of \$20.9 million. The Plan did not include the \$43.3 million premium deficiency reserve. Total claims costs were \$4.3 million less, investment income was \$4.8 million less, and non-claims expenses were \$3.4 million less than planned.

### **ECONOMIC CONDITIONS**

After allowing for the contribution to help fund retiree health care costs which is included in the active policyholder premium amount, PEIA's average active employee family monthly premium cost is \$742.32 compared to the national average cost of \$1,143.25. It should also be noted that PEIA incurred a reduction of plan assets of \$21.8 million, excluding the effect of recording current premium deficiency reserve.

## West Virginia Public Employees Insurance Agency

### Management's Discussion and Analysis (continued)

The rate of health care premium inflation is directly driven by new and more expensive medical technology including medical equipment and prescription drugs, direct to the consumer advertising, and the reluctance of employers and policyholders to limit their financial exposure. Another concern that arises is supported by medical academia. They have concluded that current scientific data does not support a reasonable cost/risk/quality of life/benefit ratio for a large number of the most expensive medical procedures performed today.

In 2009, health insurance cost rose 5.0% nationally. During the same period, the overall inflation rate decreased 0.7% and wage gains were limited to 1.8%. Such disparity reduces disposable incomes of policyholders as they are asked to bear a larger share of health care cost and stresses the operations of their employers.

Premium increases totaling \$45.8 million were placed into effect for the year that began July 1, 2009.

#### **CAPITAL ASSET AND LONG-TERM DEBT ACTIVITY**

During fiscal year 2008, PEIA adopted Governmental Accounting Standards Board Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, in conjunction with our implementation of new computer software. Following the provisions of Statement No. 51, we capitalized computer software costs of \$2.7 million and \$4.5 million in fiscal years ended 2009 and 2008, respectively. These additions are expected to result in additional annual depreciation over the next five years of approximately \$540,000 and \$900,000, respectively. See Note 6 for further details.

PEIA has no long-term debt.

#### **REQUESTS FOR INFORMATION**

This financial report is designed to provide PEIA's customers, governing officials, legislators, citizens, and taxpayers with a general overview of PEIA's accountability for the money it receives. If you have any questions about this report or need additional information, contact the Chief Financial Officer at (304) 558-7850.

# West Virginia Public Employees Insurance Agency

## Statements of Net Assets

	June 30	
	2009	2008
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 2,700,245	\$ 15,425,536
Equity position in internal investment pool	33,294,218	40,382,507
Premiums receivable:		
Due from State of West Virginia	2,324,756	1,155,303
Other, less allowance for doubtful accounts of \$4,971,000 and \$6,262,000, respectively	24,141,999	13,200,491
Accounts receivable:		
Provider refunds, less allowance for doubtful accounts of \$452,000 and \$389,000, respectively	469,046	792,014
Prescription rebates	5,960,234	5,537,230
Due from RHBT	–	7,178,893
Other	253,128	222,220
Total current assets	69,143,626	83,894,194
Noncurrent assets:		
Equity position in internal investment pools	115,072,492	122,360,685
Equity position in internal investment pool – restricted	7,738,658	7,738,658
Capital assets, net of accumulated depreciation of \$2,393,849 and \$974,092, respectively	6,495,407	5,153,924
Total noncurrent assets	129,306,557	135,253,267
Total assets	198,450,183	219,147,461
<b>Liabilities</b>		
Current liabilities:		
Claims payable	56,461,892	51,276,816
Premium deficiency reserve	15,588,245	43,301,816
Accounts payable	3,078,470	7,760,535
Unearned revenue	1,329,780	357,244
Other accrued liabilities	3,483,904	5,407,453
Due to RHBT	1,537,199	–
Total current liabilities	81,479,490	108,103,864
Noncurrent liabilities:		
Other accrued liabilities: Premium stabilization fund	7,738,658	7,738,658
Total liabilities	89,218,148	115,842,522
<b>Net assets</b>		
Invested in capital assets	6,495,407	5,153,924
Unrestricted	102,736,628	98,151,015
Total net assets	\$ 109,232,035	\$ 103,304,939

*See accompanying notes.*

# West Virginia Public Employees Insurance Agency

## Statements of Revenues, Expenses, and Changes in Net Assets

	<b>Year Ended June 30</b>	
	<b>2009</b>	<b>2008</b>
Operating revenues:		
Premiums net of provisions for bad debts of \$(1,291,000) and \$5,453,000, respectively	<b>\$ 464,263,863</b>	\$ 416,040,777
Less:		
Payments to managed care organizations	(54,666,461)	(55,127,294)
Life insurance premiums ceded	(5,520,045)	(5,468,540)
Net premium revenue	<b>404,077,357</b>	355,444,943
Administrative fees, net of refunds	4,693,824	4,487,011
Total operating revenues	<b>408,771,181</b>	359,931,954
Operating expenses:		
Claims expense, net	371,015,676	419,370,075
Administrative service fees	14,810,235	12,820,798
Other expenses	10,107,845	6,764,371
Total operating expenses	<b>395,933,756</b>	438,955,244
Operating income (loss)	<b>12,837,425</b>	(79,023,290)
Nonoperating revenues (expenses):		
Investment (loss) income, net of fees	(6,903,009)	7,934,895
On behalf of contributions	-	43,412
Transfer out	(7,320)	-
Total nonoperating (loss) income	<b>(6,910,329)</b>	7,978,307
Change in net assets	<b>5,927,096</b>	(71,044,983)
Total net assets, beginning of year	<b>103,304,939</b>	174,074,569
Change in accounting principle for other postemployment benefits	-	275,353
Total net assets, beginning of year adjusted	<b>103,304,939</b>	174,349,922
Total net assets, end of year	<b>\$ 109,232,035</b>	\$ 103,304,939

*See accompanying notes.*

# West Virginia Public Employees Insurance Agency

## Statements of Cash Flows

	<b>Year Ended June 30</b>	
	<b>2009</b>	<b>2008</b>
<b>Operating activities</b>		
Cash received from participants	\$ 396,466,817	\$ 358,481,169
Cash received from pharmacy rebates	13,632,097	11,842,611
Cash paid to employees	(1,564,977)	(1,609,354)
Cash paid to suppliers and others	(27,503,967)	(12,445,580)
Cash paid for claims	(407,176,268)	(389,633,562)
Net cash used in operating activities	(26,146,298)	(33,364,716)
<b>Noncapital financing activities</b>		
Advances from (to) RHBT	8,716,092	(10,802,314)
Payment of prior years excess reserves to RHBT	-	(108,167,017)
Transfers	(7,320)	1,404,382
Net cash provided by (used in) noncapital financing activities	8,708,772	(117,564,949)
<b>Capital and related financing activities</b>		
Purchases of capital assets	(2,761,240)	(4,953,733)
Net cash used in capital and related financing activities	(2,761,240)	(4,953,733)
<b>Investing activities</b>		
Purchases of investments	(89,145,903)	(16,629,926)
Sale of investments	81,735,951	61,885,203
Investment earnings	7,795,138	10,315,516
Net cash provided by investing activities	385,186	55,570,793
Net decrease in cash and cash equivalents	(19,813,580)	(100,312,605)
Cash and cash equivalents at beginning of year	63,546,701	163,859,306
Cash and cash equivalents at end of year	\$ 43,733,121	\$ 63,546,701
Cash and cash equivalents consist of:		
Cash and cash equivalents	\$ 2,700,245	\$ 15,425,536
Equity position in internal investment pool – current	33,294,218	40,382,507
Equity position in internal investment pool – restricted	7,738,658	7,738,658
	\$ 43,733,121	\$ 63,546,701
<b>Reconciliation of operating (loss) income to net cash used in operating activities</b>		
Operating income (loss)	\$ 12,837,425	\$ (79,023,290)
<b>Adjustments</b>		
Depreciation	1,419,757	367,873
Provision for uncollectible accounts	(1,291,000)	2,602,000
Decrease (increase) in operating assets:		
Premiums receivable	(9,650,508)	(4,484,826)
Due from State of West Virginia	(1,169,453)	1,091,708
Provider refunds receivable	322,968	(189,600)
Prescription refunds receivable	(423,004)	(749,611)
Other	(30,908)	279,546
Increase (decrease) in operating liabilities:		
Claims payable	5,185,076	(1,722,692)
Accounts payable	(4,682,065)	5,372,542
Premium deficiency	(27,713,571)	43,301,816
Unearned revenue	972,536	(2,835,950)
Other accrued liabilities	(1,923,551)	2,625,768
Total adjustments	(38,983,723)	45,658,574
Net cash used in operating activities	\$ (26,146,298)	\$ (33,364,716)
<b>Noncash activities</b>		
Decrease in fair value of investments	\$ (14,698,145)	\$ (2,380,621)
On behalf of contributions	\$ -	\$ 43,412

See accompanying notes.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements

June 30, 2009

### **1. Reporting Entity**

The State of West Virginia Public Employees Insurance Agency (PEIA) was established under the Public Employees Insurance Act of 1971 (Act). PEIA is an agency of the State of West Virginia and, accordingly, is reported as an enterprise fund of the primary government in the State's Comprehensive Annual Financial Report (CAFR).

PEIA provides the following basic employee benefit coverage to all participants: hospital, surgical, group major medical, basic group life, accidental death, and prescription drug coverage for active employees of the State of West Virginia (State) and various related State and non-State agencies. Additionally, all participants may elect to purchase additional life insurance under the optional life insurance policy. All premium rates are established based upon projected coverage costs as reviewed and approved by the Finance Board of PEIA. See "Budgetary Requirements" for further discussion of this process. PEIA's enrollment consists of approximately 75,000 health and basic life insurance policyholders, and 13,000 policyholders with life insurance only. PEIA insures approximately 179,000 individuals, including participants and dependents.

During the 2006 Regular Session of the West Virginia Legislature, House Bill 4654 was enacted creating the West Virginia Retiree Health Benefit Trust (RHBT) Fund for the purpose of providing for and administering retiree postemployment health care benefits, and the respective revenues and costs of those benefits as a cost-sharing multiple employer plan. As a consequence of the legislation, health insurance policies covering approximately 34,000 retirees and their dependents, along with the related revenues, claims costs, and expenses were transferred to RHBT effective July 1, 2006. RHBT and PEIA jointly share administrative duties relating to the other postemployment benefit (OPEB) operations. Both entities are housed in the same office space and share expenses. Expenses directly attributable to the OPEB plan are charged to RHBT. Other operating expenses, except personnel, are allocated based on policyholder count between PEIA and RHBT. Personnel expenses attributable to three dedicated employees are charged in full to RHBT; while the balance of the combined expense is allocated between the two entities based on estimated time requirements.

The basic financial statements of PEIA are intended to present the financial position, changes in financial position, and cash flows of only that portion of the business-type activities of the State of West Virginia that is attributable to the transactions of PEIA. They do not purport to, and do not, present fairly the financial position of the State of West Virginia as of June 30, 2009 and 2008, and the changes in its financial position or, where applicable, its cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **2. Summary of Significant Accounting Policies**

#### **Basis of Reporting**

PEIA operates as an enterprise fund. Accordingly, the financial statements of PEIA have been prepared on the accrual basis in conformity with U.S. generally accepted accounting principles for governmental entities as prescribed or permitted by the Governmental Accounting Standards Board (GASB). Revenues mainly are derived from premiums earned net of related reinsurance premiums, plus administrative fees billed. Expenses consist primarily of claims, administrative service fees, and various general and administrative costs.

In September 1993, GASB issued Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*. As permitted by the Statement, PEIA has elected not to adopt Financial Accounting Standards Board (FASB) statements and interpretations issued after November 30, 1989, unless GASB specifically adopts such FASB statements or interpretations.

#### **Use of Estimates**

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make certain estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from management's estimates.

#### **Annual Financial Plan**

The Act requires the Finance Board of PEIA to prepare a proposed annual financial plan. The plan must be designed to generate sufficient revenues to meet all expected expenses, including insurance, administrative expenses, and incurred but not reported claims (IBNR) of PEIA. An independent professional actuary must review the plan and give an opinion stating that the plan may be reasonably expected to generate sufficient revenue to meet estimated insurance claims and administrative expenses. The financial plan must be presented to the governor and the legislature no later than January 1, prior to the beginning of the new plan year.

PEIA Finance Board establishes PEIA premiums based upon its approved annual financial plan. The financial plan projects the anticipated costs of the program for each fiscal year and the premium levels necessary to meet these costs. Any variances between projected and incurred

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **2. Summary of Significant Accounting Policies (continued)**

costs are incorporated into subsequent financial plans and subsequent premiums are adjusted accordingly on a prospective basis. Premiums assessed by PEIA are not subject to retroactive adjustment based upon actual costs incurred.

#### **Cash and Cash Equivalents**

Cash and cash equivalents include short-term investments with original maturities of 90 days or less. Cash and cash equivalents principally consist of amounts on deposit with the West Virginia State Treasurer's office, outside financial institutions, and amounts deposited in an internal investment pool managed by the West Virginia Board of Treasury Investments (BTI) that is reported as part of equity position in internal investment pool – current-unrestricted and noncurrent-restricted, respectively.

#### **Premiums Receivable**

All premiums receivable are reported at their gross premium value due from employers and individual subscribers. The gross value is then reduced by the estimated portion that is expected to be uncollectible based upon management's review of the payment status of the underlying accounts and other economic factors that are deemed necessary in the circumstances.

#### **Accounts Receivable**

Accounts receivable include overpayments made by third-party administrators which are due to PEIA and estimated prescription refunds and rebates that are due PEIA from third-party administrators and other drug companies. The estimated prescription refunds/rebate receivable is based upon estimated prescription claim count and historical average rebate per claim. These receivables have been reduced by the estimated portion that is expected to be uncollectible based upon management's review of the payment status of the underlying accounts and other economic factors that are deemed necessary in the circumstances.

#### **Equity Position in Internal Investment Pools**

PEIA owns equity positions in state government investment pools managed by the West Virginia Investment Management Board (WVIMB) and the Board of Treasury Investments (BTI). Some investment pool funds are subject to market risk because of changes in interest rates, bond prices, and stock prices. Investment earnings and losses are allocated to PEIA based on the balance of



# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **2. Summary of Significant Accounting Policies (continued)**

PEIA's investments maintained in relation to the total investments of all state agencies participating in the pool. The Equity Position in Internal Investment Pools is reported at fair value and changes in fair value are included in investment income.

A thirteen-member Board of Trustees governs the WVIMB. Three members of the Board serve by virtue of their office: the Governor, the Auditor, and the Treasurer. The other ten are appointed by the Governor and confirmed by the Senate. All appointees must have experience in pension management, institutional management or financial markets. In addition, one must be an attorney experienced in finance and investment matters and another must be a Certified Public Accountant. Only six of the ten appointed Trustees may be from the same political party. The Governor serves as Chairman of the Board. A Vice-Chairman is elected by the Trustees. A Secretary, who need not be a member of the Board, is also elected by the Trustees to keep a record of the proceedings of the Board. Details regarding these investment pools and a copy of the WVIMB financial report can be obtained by contacting West Virginia Investment Management Board, 500 Virginia Street, East, Suite 200, Charleston, WV 25301 or by calling 304-645-5939.

A five-member Board of Directors governs the BTI. The Governor, Treasurer, and Auditor serve as ex-officio members of the Board. The Governor appoints the two remaining members subject to the advice and consent of the State Senate. Of the two members appointed by the Governor, one shall be a certified public accountant and one shall be an attorney, and both shall have experience in finance, investing, and management. The State Treasurer is Chairman of the Board. The BTI prepares separately issued financial statements covering the pooled fund, which can be obtained from its website or a published copy from the West Virginia Board of Treasury Investments, 1900 Kanawha Boulevard, East, Building 1, Room E-122, Charleston, West Virginia 25305.

### **Capital Assets**

Capital assets with an initial cost of \$1,000 or greater are recorded at cost. PEIA has assigned a useful life of three to five years for capital assets. Depreciation expense computed using the straight-line method was \$1,419,757 and \$367,873 for the years ended June 30, 2009 and 2008, respectively.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **2. Summary of Significant Accounting Policies (continued)**

#### **Claims Payable and Expense**

The liability for unpaid claims and claims processing costs is based on an actuarial estimate of the ultimate cost of settling such claims incurred as of the statement of net assets date (including claims reported and in process of settlement, claims reported but not yet processed for settlement, and claims incurred but not yet reported or processed for settlement). The estimated actuarial liability reflects certain assumptions, which include such factors as enrollment, utilization, inflation, and other societal and economic factors. Adjustments to the estimated actuarial liability for the final settlement of claims will be reflected in the year that the actual results of the settlement of the claims are made and are known. The estimated liability is adjusted annually based on the most current claim incurrence and claim settlement history (see Note 7). Claims relating to participants in managed care organizations (MCOs) as well as claims relating to participants covered under the optional life insurance plan are not considered in the liability as PEIA has no liability for the participants who elect such coverage. Additionally, the estimated liability for unpaid claims and claims processing costs is recorded net of amounts ceded to reinsurers for basic life benefits as management believes these reinsured risks are fully recoverable. However, in the event a reinsurer is unable financially to satisfy an obligation, PEIA is responsible for such liability. Claims expense is reported net of pharmacy rebate income of \$14,055,101 and \$12,592,222 for the years ended June 30, 2009 and 2008, respectively.

#### **Premium Deficiency Reserve**

Premium deficiency is required when policies in force as of the financial statement date are expected to produce a loss when claims cost (including IBNR), plus expected claims adjustment expenses, are expected to exceed related premiums. Management has recorded a premium deficiency reserve of \$15,588,245 and \$43,031,816 as of June 30, 2009 and 2008, respectively. Furthermore, in January 2009, the Finance Board approved the premium rates for fiscal year 2010. In making this determination, management took into consideration anticipated premium revenue and claims costs. PEIA did not include anticipated investment income in determining whether a premium deficiency exists. Adjustments to the estimated premium deficiency liability are reflected as a change in estimate in the year the actual results are known.

PEIA participants are not subject to supplemental assessment in the event of a premium deficiency. At the time of premium payment, the risk of loss due to incurred benefit costs is transferred from the participant to PEIA. If the assets of PEIA were to be exhausted, participants would not be responsible for the liabilities.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **2. Summary of Significant Accounting Policies (continued)**

#### **Unearned Revenue**

Unearned revenue includes premium revenues collected for future contract periods. These revenues will be recognized in the operating periods in which they are earned.

#### **Insurance Programs and Related Premium Revenues**

PEIA offers the following types of coverage to its participants: health coverage through a self-insured preferred provider benefit (PPB) plan, health coverage through external MCOs, and life and accidental death and dismemberment (AD&D) insurance benefits under basic and optional plans. PEIA collects premiums for participants in the PPB plan and uses these premiums in the administration of the plan. Additionally, PEIA has the statutory authority to raise additional revenues in the form of premiums without the need for external (legislative) action.

For participants who elect coverage through MCOs, PEIA collects premiums from employers and remits a capitation fee to an MCO carrier. The capitation fees paid by PEIA to each MCO are in accordance with their respective contracts. Benefits are the responsibility of each MCO carrier. The premiums earned by PEIA have been included in gross premium revenue while the capitation fees submitted to each MCO carrier are reflected as payments to MCOs on the financial statements.

As of the June 2009 coverage month, PEIA provided health coverage to 119 State agency divisions with approximately 22,000 primary participants (not including dependents), 55 county school boards with approximately 32,000 primary participants, 539 local government entities with approximately 11,000 primary participants, and 23 college and university entities with approximately 10,000 primary participants. Approximately 91,000 dependents participated in PEIA health plans as well.

As of the June 2008 coverage month, PEIA provided health coverage to 119 State agency divisions with approximately 21,000 primary participants (not including dependents), 55 county school boards with approximately 32,000 primary participants, 524 local government entities with approximately 10,000 primary participants, and 23 college and university entities with approximately 10,000 primary participants. Approximately 88,000 dependents participated in PEIA health plans as well.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **2. Summary of Significant Accounting Policies (continued)**

Employees covered through PEIA are eligible to obtain life insurance coverage under basic and optional life insurance plans. Basic life benefits and AD&D benefits of \$10,000 are provided to active State employees under the age of 65 at no cost to the employee. Coverage amounts decrease with age. No AD&D benefits are available to retirees. Basic life benefits are available to retirees with coverage ranging from \$2,500 to \$5,000 depending on age. For these basic life benefits, PEIA collects premiums and submits them to the insurance carrier. PEIA has reinsured 100% of these basic benefits; however, PEIA remains contingently liable in the event the insurer does not honor its obligation. The premiums earned for basic life insurance are reflected in gross premiums and the related amounts ceded to the reinsurer are reflected as life reinsurance premiums on the financial statements.

Active employees may elect to obtain additional optional coverage for both life and AD&D with coverage from \$5,000 to \$500,000 that decreases with age. Active employees may also elect dependent optional life coverage and AD&D at a level up to \$20,000 per spouse and \$10,000 per child. Retirees may obtain optional life insurance coverage from \$5,000 to \$150,000 depending on age; however, optional AD&D insurance is not available to retirees. Retirees may also elect dependent optional life coverage at levels up to \$20,000 for spouse and \$10,000 per child. Amounts collected by PEIA from employees for optional coverage totaled \$13,417,453 and \$10,324,716 during the fiscal years ended June 30, 2009 and 2008, respectively, and were remitted directly to the carrier. In this instance, PEIA functions as an agent and, accordingly, neither these premiums nor the related costs are reflected in the financial statements.

Revenues include an administrative fee that PEIA charges to all participating entities in the plan. The fee is based on the participating entities' number of employees enrolled in the plan.

#### **Administrative Service Fees**

PEIA contracts with and pays administrative service fees to two third-party administrators. Services include processing of insurance claims, precertification reviews, utilization reviews, and various other duties. The majority of related fees are assessed each month based upon the number of covered participants or claims processed at predetermined rates without regard to the period in which a claim is incurred, processed, or settled.

#### **Supplemental Appropriations**

Supplemental appropriations represent legally authorized appropriations under West Virginia State Code by the West Virginia Legislature. The purpose of the transfers was to reduce state employee health care insurance premium rate increases.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### 2. Summary of Significant Accounting Policies (continued)

#### Compensated Absences, Including Postretirement Benefits

Employees fully vest in all earned but unused annual leave and PEIA accrues for obligations that may arise in connection with compensated absences for vacation at the current rate of employee pay. In accordance with State personnel policies, employees vest in any remaining unused sick leave only upon retirement, at which time any unused compensated absence time can be converted into employer paid premiums for postretirement health care coverage through RHBT, or be converted into a greater retirement benefit under the State's Public Employees' Retirement System.

#### Operating Revenues and Expenses

Balances classified as operating revenues and expenses are those that comprise PEIA's ongoing operations. Principal operating revenues include health insurance premiums, life insurance premiums, and insurance administration fees, less amounts paid to managed care organizations and life insurance reinsurers. Operating expenses include the cost of medical claims, drug claims, claims adjudication, administration, and depreciation of capital assets. Other revenues and expenses are classified as nonoperating in the financial statements.

#### Net Assets

As required by GASB Statement 34, PEIA displays net assets in three components, if applicable: invested in capital assets, net of related debt; restricted; and unrestricted.

*Invested in Capital Assets, Net of Related Debt* – This component of net assets consists of capital assets, net of accumulated depreciation and reduced by the outstanding balances of any bonds, mortgages, notes, or other borrowings that are attributable to the acquisition, construction, or improvement of those assets.

*Unrestricted Net Assets* – Unrestricted net assets consist of net assets that do not meet the definition of "restricted" or "invested in capital assets, net of related debt." In the governmental environment, net assets are often *designated* to indicate that management does not consider them to be available for general operations. These types of constraints on resources are internal and management can remove or modify them. Such internal designations are not reported on the face of the statement of net assets.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### 2. Summary of Significant Accounting Policies (continued)

West Virginia Code Section 5-16-25 requires the Finance Board of PEIA to maintain a reserve of 10% of projected plan costs for general operation purposes and provide future plan stability. As of June 30, 2009 and 2008, PEIA has sufficient net assets to comply with this code section. In the event the reserve fund exceeds 15% of the actuarial recommended reserve of 20% to 25% of total projected costs, the excess was to be remitted to the State of West Virginia Department of Administration. Accordingly, excess reserves of \$80,487,422 and \$27,679,595 were due to be transferred for years ended 2009 and 2008, respectively. Senate Bill 129, which became effective July 1, 2007, amended 5-16-25 indicating that the excess reserve funds shall be transferred to the West Virginia Retiree Health Benefit Trust Fund beginning in fiscal 2008. Accordingly, the monies were transferred to RHBT in fiscal year 2008. There were no excess reserves to be transferred for the year ended June 30, 2009.

### Reclassifications

Certain 2008 amounts in the accompanying financial statements have been reclassified to conform to the 2009 presentation. Such reclassifications did not impact the previously reported change in net assets.

### 3. Cash and Cash Equivalents

Following is a summary of PEIA's cash and cash equivalents as of June 30:

	<u>2009</u>	<u>2008</u>
Cash and cash equivalents on deposit with State Treasurer	\$ 1,399,113	\$ 14,417,841
Deposits with outside financial institutions	<u>1,301,132</u>	<u>1,007,695</u>
Cash and cash equivalents reported on statement of net assets	<b>2,700,245</b>	15,425,536
Equity position in internal investment pool with BTI – current-unrestricted	<b>33,294,218</b>	40,382,507
Equity position in internal investment pool with BTI – noncurrent-restricted	<b>7,738,658</b>	7,738,658
Total cash and cash equivalents	<u><b>\$ 43,733,121</b></u>	<u>\$ 63,546,701</u>

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **4. Deposit and Investment Risk Disclosures**

#### **Deposits with Outside Financial Institutions**

##### *Custodial Credit Risk*

Custodial credit risk is the risk that, in the event of a bank failure, PEIA's deposits might not be recovered. PEIA has no deposit policy for custodial credit risk.

As of June 30, 2009 and 2008, the carrying amount of PEIA's bank deposits was \$1,301,132 and \$1,007,695, respectively, and the respective bank balances totaled \$1,511,042 and \$1,256,580. Of the total bank balance, \$1,510,741 and \$1,256,580, respectively, were uninsured and collateralized with government-sponsored enterprise securities held by financial institutions. These securities are held in the name of the financial institution and not that of PEIA.

#### **West Virginia Money Market Pool (*Formerly Cash Liquidity Pool*) – Equity Position in Internal Investment Pool – Current – Managed by BTI**

##### *Credit Risk*

The BTI administers the pool and limits exposure to credit risk by requiring all corporate bonds held by their West Virginia Money Market Pool to be rated AA- by Standard & Poor's (or its equivalent) or higher. Commercial paper must be rated at least A-1 by Standard & Poor's and P1 by Moody's. Additionally, the pool must have at least 15% of its assets in United States Treasury issues.

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

The following table provides information on the credit ratings of the WV Money Market Pool's investments (in thousands).

Security Type	June 30, 2009		Carrying Value	Percent of Pool Assets
	Credit Rating			
	Moody's	S&P		
Commercial paper	P1	A-1	\$ 592,479	23.05%
Corporate bonds and notes	Aaa	AAA	10,000	0.39
	Aa1	AA	7,000	0.27
	Aa2	AA	10,000	0.39
	Aa3	AA	15,503	0.60
	A1	AA	19,309	0.75
	A1	A	12,000	0.47
Total corporate bonds and notes			73,812	2.87
U.S. agency bonds	Aaa	AAA	294,019	11.44
U.S. Treasury bills*	Aaa	AAA	483,714	18.82
Negotiable certificates of deposit	P1	A-1	128,402	5.00
U.S. agency discount notes	P1	A-1	635,602	24.73
Money market funds	Aaa	AAA	150,223	5.84
Repurchase agreements (underlying securities):				
U.S. Treasury notes*	Aaa	AAA	165,110	6.43
U.S. agency notes	Aaa	AAA	46,900	1.82
Total repurchase agreements			212,010	8.25%
Total investments			\$ 2,570,261	100.00%

\* U.S. Treasury issues are explicitly guaranteed by the United States government and are not subject to credit risk.

*Custodial Credit Risk*

Repurchase agreements included in BTI's investment portfolio are collateralized by at least 102% of their value and the collateral is held in the name of the BTI. Securities lending collateral is invested in the lending agent's money market fund in BTI's name.



West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

*Interest Rate Risk*

The weighted-average maturity of the investments of the WV Money Market Pool cannot exceed 60 days. The maturity of individual securities cannot exceed 397 days from the date of purchase. The following table provides the weighted-average maturities (WAM) for the various asset types in the WV Money Market Pool at June 30, 2009.

<b>Security Type</b>	<b>Carrying Value</b>	<b>WAM (Days)</b>
	<i>(In Thousands)</i>	
Repurchase agreements	\$ 212,010	1
U.S. Treasury bills	483,714	69
Commercial paper	592,479	32
Negotiable certificates of deposit	128,402	56
U.S. agency discount notes	635,602	57
Corporate bonds and notes	73,812	38
U.S. agency bonds/notes	294,019	70
Money market funds	150,223	1
Total investments	<u>\$ 2,570,261</u>	<u>47</u>

PEIA's investment in the BTI WV Money Market Pool of \$41,040,389 at June 30, 2009, represents approximately 1.6% of total investments in this pool.

**Equity Position in Internal Investment Pools – Noncurrent-Unrestricted Managed by WVIMB**

**Public Employees Insurance Agency Fund**

This investment fund was specifically designed for PEIA by WVIMB based on PEIA's unique cash flow needs. PEIA is the only State agency participating in this fund and owns 100% of the total assets. The fund invests in various pools managed by WVIMB.

West Virginia statute mandates that the Public Employees Insurance Agency Fund shall be managed by WVIMB, a public corporation.

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

**Investment Objectives**

This fund's investment objective is to achieve a total rate of return of at least 5.4% per annum, net of fees.

**Asset Allocation**

Based upon the WVIMB's determination of the appropriate risk tolerance for the fund, the WVIMB has adopted the following broad asset allocation guidelines for the assets managed for the Public Employees Insurance Agency Fund. (Policy targets have been established on a market value basis.) The asset values of the pools below are reported in equity position in internal investment pools – noncurrent-unrestricted on the statement of net assets.

<b>Asset Class</b>	<b>Policy Target</b>	
	<b>2009</b>	<b>2008</b>
Large cap domestic equity	7.5%	7.5%
Non-large cap domestic equity	–	–
International equity	7.5	7.5
Total equity	<b>15.0%</b>	15.0%
Fixed income	<b>85.0%</b>	65.0%
Hedge fund	–	20.0
	<b>Asset Value at June 30</b>	
	<b>2009</b>	<b>2008</b>
	<i>(In Thousands)</i>	
<b>Asset allocation (actual)</b>		
Large cap domestic equity pool	\$ 7,324	\$ 7,648
Non-large cap domestic equity pool	1,313	1,559
International nonqualified pool	3,054	2,305
International equity pool	6,258	5,795
Short-term fixed income pool	1	27
Total return fixed income/fixed income pool	53,033	62,803
Core fixed income	21,406	–
Hedge fund	22,683	(1)
Fixed income nonqualified pool	–	42,225
Total	<b>\$ 115,072</b>	<b>\$ 122,361</b>

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **4. Deposit and Investment Risk Disclosures (continued)**

#### **Asset Class Risk Disclosures**

##### *Large Cap Domestic Equity Pool*

This pool holds equity securities of U.S. companies and money market funds with the highest credit rating. PEIA's amount invested in the Large Cap Domestic Equity Pool of \$7,324,000 and \$7,648,000 at June 30, 2009 and 2008, respectively, represents approximately 0.4% and 0.4% of total investments in this pool.

##### *Non-Large Cap Domestic Equity Pool*

This pool holds equity securities of U.S. companies and money market funds with the highest credit rating. PEIA's amount invested in the Non-Large Cap Domestic Equity Pool of \$1,313,000 at June 30, 2009 and \$1,559,000 at June 30, 2008, represents approximately 0.4% and 0.2% of total investments in this pool.

##### *International Nonqualified Pool*

This pool holds an institutional mutual fund that invests in equities denominated in foreign currencies. West Virginia statute limits the amount of international securities to no more than 30% of the total assets managed by the WVIMB. The value of this investment was \$101,246,000 and \$57,888,000 at June 30, 2009 and 2008, respectively. This investment, although denominated in U.S. dollars, is exposed to foreign currency risk through underlying investments. The specific currencies of the underlying investments were not available. West Virginia statute limits the amount of international securities to no more than 30% of the total assets managed by the WVIMB. PEIA's amount invested in the International Nonqualified Pool of \$3,054,000 at June 30, 2009 and \$2,305,000 at June 30, 2008, represents approximately 3.02% and 3.98% of total investments in this pool.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### 4. Deposit and Investment Risk Disclosures (continued)

#### *International Equity Pool*

This pool has both equity securities and cash that are denominated in foreign currencies and are exposed to foreign currency risk. West Virginia statute limits the amount of international securities to no more than 30% of the total assets managed by the WVIMB. PEIA's amount invested in the International Equity Pool of \$6,258,000 at June 30, 2009 and \$5,795,000 at June 30, 2008, represents approximately 0.42% and 0.35% of total investments in this pool. The amounts (in U.S. dollars) of the securities and cash denominated in foreign currencies as of June 30 are as follows:

Currency	2009		
	Equity Securities	Cash	Total
Australian Dollar	\$ 45,295,313	\$ 187,926	\$ 45,483,239
Brazil Cruzeiros Real	76,243,266	1,318,077	77,561,343
British Pound	175,318,942	1,551,666	176,870,608
Canadian Dollar	43,761,183	109,535	43,870,718
Czech Koruna	7,234,731	135	7,234,866
Danish Krone	10,935,831	33,982	10,969,813
Euro	266,768,796	6,226,567	272,995,363
Hong Kong Dollar	115,552,388	304,416	115,856,804
Hungarian Forint	11,566,434	781	11,567,215
Indonesian Rupiah	2,474,340	-	2,474,340
Israeli Shekel	13,692,033	81	13,692,114
Japanese Yen	214,493,385	2,000,670	216,494,055
Malaysian Ringitt	8,765,540	25,190	8,790,730
Mexican New Peso	20,204,832	54,161	20,258,993
New Taiwan Dollar	44,242,681	29,702	44,272,383
New Zealand Dollar	1,750,119	404,401	2,154,520
Norwegian Krone	9,140,372	127,263	9,267,635
Pakistani Rupee	1,371,114	-	1,371,114
Philippine Peso	4,738,490	-	4,738,490
Polish Zloty	4,768,257	39	4,768,296
Singapore Dollar	31,364,188	238,905	31,603,093
South African Rand	20,492,344	55,109	20,547,453
South Korean Won	75,285,153	527,742	75,812,895
Swedish Krona	19,034,030	75,507	19,109,537
Swiss Franc	58,766,408	928,122	59,694,530
Thailand Baht	-	2,202	2,202
Turkish Lira	30,584,716	42,029	30,626,745
Total	<u>\$ 1,313,844,886</u>	<u>\$ 14,244,208</u>	<u>\$ 1,328,089,094</u>

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

This table excludes cash and securities held by the pool that are denominated in U.S. dollars. The fair value of the U.S. dollar denominated cash and securities is \$181,239,129.

*Short-Term Fixed Income Pool*

*Credit Risk*

The WVIMB limits the exposure to credit risk in the Short-Term Fixed Income Pool by requiring all corporate bonds to be rated AA or higher. Commercial paper must be rated A1 by Standard & Poor's and P1 by Moody's. Additionally, the pool must have at least 15% of its assets in United States Treasury issues.

The following table provides information on the weighted-average credit ratings of the Short-Term Fixed Income Pool's investments as of June 30, 2009.

Security Type	Moody's	S&P	2009	
			Carrying Value	Percent
Agency discount notes	P1	A-1	\$ 88,452,922	33.3%
U.S. Treasury note	Aaa	AAA	92,585,804	34.9
Commercial paper	P1	A-1	12,999,680	4.9
U.S. Treasury bills	Aaa	AAA	43,996,249	16.6
Agency bonds	Aaa	AAA	27,496,451	10.3
Money market fund	Aaa	AAA	131	0.0
Total rated investments			<u>\$ 265,531,237</u>	<u>100.0%</u>

This table includes securities received as collateral for repurchase agreements valued at \$92,585,804 in 2009.

*Custodial Credit Risk*

Repurchase agreements are collateralized at 102% and the collateral is held in the name of the WVIMB.

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

*Interest Rate Risk*

The weighted-average maturity of the investments of the Short-Term Fixed Income Pool is not to exceed 60 days. The maturity of floating rate notes is assumed to be the next interest rate reset date. The following table provides the weighted-average maturities (WAM) for the various asset types in the Short-Term Fixed Income Pool as of June 30, 2009.

Security Type	2009	
	Carrying Value	WAM (days)
Repurchase agreements	\$ 91,593,000	1
U.S. Treasury bills	43,996,249	23
Commercial paper	12,999,680	5
Agency discount notes	88,452,922	54
Agency bond	27,496,451	52
Money market fund	131	1
Total assets	<u>\$ 264,538,433</u>	<u>28</u>

PEIA's amount invested in the Short-Term Fixed Income Pool at June 30, 2009 and 2008, was nominal.

## West Virginia Public Employees Insurance Agency

### Notes to Financial Statements (continued)

#### 4. Deposit and Investment Risk Disclosures (continued)

##### *Total Return Fixed Income Pool (Previously Named Fixed Income Pool)*

##### *Credit Risk*

The WVIMB limits the exposure to credit risk in the Total Return Fixed Income Pool by maintaining at least an average rating of investment grade as defined by the Nationally Recognized Statistical Rating Organizations. The following table provides the weighted-average credit ratings of the asset types in the fixed income pool as of June 30, 2009.

<u>Security Type</u>	<u>Moody's</u>	<u>S&amp;P</u>	<u>2009</u>	
			<u>Fair Value</u>	<u>Percent of Assets</u>
Agency mortgage-backed securities	Aaa	AAA	\$ 531,284,382	20.2%
Money market funds	Aaa	AAA	472,292,326	17.9
Corporate bonds and notes	Baa	BBB	466,052,257	17.7
Corporate collateralized mortgage obligations	Baa	AA	91,081,767	3.5
U.S. Treasury inflation protection bonds	Aaa	AAA	74,631,563	2.8
Agency notes	Aa	AA	3,866,877	0.1
U.S. Treasury bonds and notes	Aaa	AAA	1,678,244	0.1
Corporate preferred securities	C	C	965,455	0.0
Corporate asset-backed securities	Aa	AA	622,399	0.0
Agency collateralized mortgage obligations	Aaa	AAA	465,532	0.0
Total rated investments			<u>\$ 1,642,940,802</u>	<u>62.3%</u>

Unrated securities include commingled investment pools valued at \$987,106,348, swaps, options, and swaptions valued at \$(10,205,602), future contracts valued at \$6,356,507, foreign currency forward contracts valued at \$(610,756), and cash of \$16,705,447 pledged to brokers as collateral. These unrated securities represent 37.7% of the fair value of the pool's investments.

##### *Custodial Credit Risk*

At June 30, 2009, the Total Return Fixed Income Pool held no securities that were subject to custodial credit risk. Repurchase agreements, when held, are collateralized at 102% and the collateral is held in the name of the WVIMB. Investments in commingled funds are held in an account in the name of the WVIMB. All remaining securities are held by the WVIMB's custodian in the name of the WVIMB. Securities lending collateral is invested in the lending agent's money market fund.

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

*Interest Rate Risk*

The WVIMB monitors interest rate risk of the Total Return Fixed Income Pool by evaluating the modified duration of the investments in the pool. The following table provides the weighted-average modified duration for the various asset types in the Total Return Fixed Income Pool as of June 30, 2009.

<b>Security Type</b>	<b>Fair Value</b>	<b>Modified Duration (Years)</b>
Commingled investment pools	\$ 987,105,348	2.5
Agency mortgage-backed securities	531,284,382	9.6
Money market fund	472,292,326	0.0
Corporate notes and bonds	466,052,257	5.7
Corporate collateralized mortgage obligations	91,081,767	5.1
U.S. Treasury inflation protection bonds	74,631,563	13.1
Agency bonds	3,866,877	2.8
U. S. Treasury notes and bonds	1,678,244	16.4
Corporate asset-backed securities	622,399	2.5
Agency collateralized mortgage obligations	465,532	1.0
Total assets	<u>\$ 2,629,080,695</u>	<u>5.4</u>

The Total Return Fixed Income Pool invests in commercial and residential mortgage-backed and asset-backed securities. The cash flows from these securities are based on the payment of the underlying collateral. The modified duration and yield to maturity of these securities are dependent on estimated prepayment assumptions that consider historical experience, market conditions, and other criteria. Actual prepayments may vary with changes in interest rates. Rising interest rates often result in a slower rate of prepayments while declining rates tend to lead to faster prepayments. As a result, the fair values of these securities are highly sensitive to interest rate changes. The Total Return Fixed Income Pool held \$623,449,368 and \$372,154,404 of these securities at June 30, 2009 and 2008, respectively, which represented approximately 24% and 13%, respectively, of the value of the Total Return Fixed Income Pool.



West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

PEIA's amount invested in the Total Return Fixed Income Pool of \$53,033,000 and \$62,803,000 at June 30, 2009 and 2008, respectively, represented approximately 2.0% and 2.3% of total investments in the pool.

*Core Fixed Income Pool*

*Credit Risk*

The WVIMB limits the exposure to credit risk in the Core Fixed Income Pool by maintaining at least an average rating of investment grade as defined by the Nationally Recognized Statistical Rating Organizations. The following table provides the weighted-average credit ratings of the rated assets in the Core Fixed Income Pool as of June 30, 2009.

Security Type	Moody's	S&P	Fair Value	Percent of Assets
Agency collateralized mortgage obligations	Aaa	AAA	\$ 134,378,380	33.1%
Agency mortgage-backed securities	Aaa	AAA	117,952,526	29.1
U.S. Treasury bonds and notes	Aaa	AAA	69,633,643	17.2
Corporate bonds and notes	A	A	41,035,802	10.1
Corporate collateralized mortgage obligations	Baa	AA	25,367,921	6.3
Money market funds	Aaa	AAA	15,209,068	3.7
Corporate asset-backed securities	Aaa	AAA	2,191,003	0.5
Total rated investments			\$ 405,768,343	100.0%

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**4. Deposit and Investment Risk Disclosures (continued)**

*Interest Rate Risk*

The WVIMB monitors interest rate risk of the Core Fixed Income Pool by evaluating the modified duration of the investments in the pool. The following table provides the weighted-average modified duration for the various asset types in the Core Fixed Income Pool as of June 30, 2009.

Security Type	Fair Value	Modified Duration (Years)
Agency collateralized mortgage obligations	\$ 134,378,380	3.4
Agency mortgage-backed securities	117,952,526	8.9
U.S. Treasury bonds and notes	69,633,643	6.4
Corporate bonds and notes	41,035,802	5.0
Corporate collateralized mortgage obligations	25,367,921	4.1
Money market funds	15,209,068	0.0
Corporate asset-backed securities	2,191,003	1.9
Total assets	<u>\$ 405,768,343</u>	<u>5.4</u>

The Core Fixed Income Pool invests in commercial and residential mortgage-backed securities, asset-backed securities, and collateralized mortgage obligations. The cash flows from these securities are based on the payment of the underlying collateral. The modified duration and yield to maturity of these securities are dependent on estimated prepayment assumptions that consider historical experience, market conditions, and other criteria. Actual prepayments may vary with changes in interest rates. Rising interest rates often result in a slower rate of prepayments while declining rates tend to lead to faster prepayments. As a result, the fair values of these securities are highly sensitive to interest rate changes. At June 30, 2009, the Core Fixed Income Pool held \$279,883,830 of these securities. This represents approximately 69% of the value of the pool's securities.

PEIA's amount invested in the Core Fixed Income Pool of \$21,406,000 at June 30, 2009, represented approximately 5.28% of total investments in this pool. At June 30, 2008, PEIA had no investment in this pool.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### **4. Deposit and Investment Risk Disclosures (continued)**

#### *Hedge Fund Pool*

The Hedge Fund Pool holds shares in various commingled institutional funds and shares of a money market fund with the highest credit rating. The commingled institutional funds are not rated by any of the nationally recognized statistical rating agencies and thus any credit risk cannot be accurately reported. The pool is indirectly exposed to foreign currency risk as certain of the funds have investments denominated in foreign currencies. West Virginia statute limits the amount of international securities to no more than 30% of the total assets managed by the WVIMB. At June 30, 2009, approximately \$456,938,000 or 41.00%, of the market value of the funds were held in foreign currencies. PEIA's amount invested in the Hedge Fund Pool of \$22,683,000 at June 30, 2009, represented approximately 2.04% of total investments in this pool. PEIA had a nominal investment in this pool at June 30, 2008.

#### *Fixed Income Nonqualified Pool*

During the fiscal year the WVIMB liquidated the Fixed Income Nonqualified Pool. This pool held positions in institutional mutual funds with a combined value of \$474,561,035 at June 30, 2008, that invested in mortgage-backed securities and corporate bonds. The mutual funds were unrated. The weighted-average modified duration of the underlying securities was 5.6 years. PEIA's amount invested in the Fixed Income Nonqualified Pool of \$42,225,000 at June 30, 2008, represented approximately 8.9% of total investments in this pool. As of June 30, 2009, PEIA had no investment in the Fixed Income Nonqualified Pool.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### 5. Equity Position in Internal Investment Pool – Restricted (Premium Stabilization Fund) Managed by BTI

Optional life insurance premiums are funded entirely by program participants. The premium stabilization fund consists of accumulated dividends and interest on the participant optional life insurance policies. The premium stabilization fund is invested in the BTI Money Market Pool. See pages 21 and 23 for investment risk disclosures related to this pool. To the extent that these policyholder premiums are refunded to PEIA in the form of dividends and interest by the life insurance company, the funds are refunded to the related optional life policyholders by way of reductions in future premium increases. This account is utilized to track the accumulated balance due to optional life policyholders. Cash and cash equivalents include \$7,738,658 as of June 30, 2009 and 2008, restricted to meet this obligation.

The following table represents changes in the premium stabilization fund for the years ended June 30:

	<u>2009</u>	<u>2008</u>
Premium stabilization fund – beginning of the year	\$ 7,738,658	\$ 3,942,911
Life insurance dividends and interest refunds received	–	3,795,747
Premium stabilization fund – end of year	<u>\$ 7,738,658</u>	<u>\$ 7,738,658</u>

### 6. Capital Assets

During fiscal year 2008, PEIA adopted Governmental Accounting Standards Board Statement No. 51, *Accounting and Financial Reporting for Intangible Assets*, in conjunction with the implementation of new computer software. Following the provisions of Statement No. 51, computer software costs of \$2,655,890 and \$4,503,244 were capitalized in 2009 and 2008, respectively, which is expected to result in an increase in depreciation/amortization expense of approximately \$540,000 over the next five years.

West Virginia Public Employees Insurance Agency

Notes to Financial Statements (continued)

**6. Capital Assets (continued)**

Capital asset activity for the years ended June 30, 2009 and 2008 was as follows:

	<b>June 30 2008</b>	<b>Additions</b>	<b>Disposals</b>	<b>June 30 2009</b>
	<i>(In Thousands)</i>			
Intangible assets	\$ 5,014	\$ 2,656	\$ –	\$ 7,670
Equipment	1,114	105	–	1,219
Total capital assets	6,128	2,761	–	8,889
Accumulated depreciation	(974)	(1,420)	–	(2,394)
Total capital assets, net	<u>\$ 5,154</u>	<u>\$ 1,341</u>	<u>\$ –</u>	<u>\$ 6,495</u>
	<b>June 30 2007</b>	<b>Additions</b>	<b>Disposals</b>	<b>June 30 2008</b>
Intangible assets	\$ 511	\$ 4,503	\$ –	\$ 5,014
Equipment	663	451	–	1,114
Total capital assets	1,174	4,954	–	6,128
Accumulated depreciation	(606)	(368)	–	(974)
Total capital assets, net	<u>\$ 568</u>	<u>\$ 4,586</u>	<u>\$ –</u>	<u>\$ 5,154</u>

## West Virginia Public Employees Insurance Agency

### Notes to Financial Statements (continued)

#### 7. Unpaid Claims Liabilities

As discussed in Note 2, PEIA establishes a liability for both reported and unreported insured events, which includes an estimate of future payments of losses. The following represents changes in those aggregate liabilities for PEIA for the years ended June 30:

	<b>2009</b>	<b>2008</b>	<b>2007</b>
	<i>(In Thousands)</i>		
Claims payable, beginning of year	\$ 51,277	\$ 52,999	\$ 60,122
Incurred claims expenses:			
Provision for insured events of the current year	<b>400,289</b>	377,099	359,842
Decrease in provision for insured events of prior years	<b>(1,560)</b>	(1,030)	(330)
Total incurred claims expense	<b>398,729</b>	376,069	359,512
Payments:			
Claim payments attributable to insured events of:			
Current year	<b>354,773</b>	335,380	320,480
Prior years	<b>38,771</b>	42,411	46,155
Total payments	<b>393,544</b>	377,791	366,635
Claims payable, end of year	<b>\$ 56,462</b>	\$ 51,277	\$ 52,999

The above payments are net of pharmacy rebates of \$13,632,097, \$11,842,611, and \$13,771,022 for the years ended June 30, 2009, 2008, and 2007, respectively.

#### 8. Employee Benefit Plans

All full-time PEIA employees are eligible to participate in the State of West Virginia Public Employees Retirement System (PERS), a cost-sharing, multiple-employer, public employee retirement system. Employees who retire at or after age 60 with 5 or more years of contributory service or who retire at or after age 55 and have completed 25 years of credited service are eligible for retirement benefits as established by State statute. Retirement benefits are payable monthly for life, in the form of a straight-line annuity equal to 2% of the employee's final average salary, multiplied by the number of years of the employee's credited service at the time of retirement. PERS also provides deferred retirement, early retirement, and death and disability benefits, and issues an annual report which can be obtained by contacting PERS.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### 8. Employee Benefit Plans (continued)

Covered employees are required to contribute 4.5% of their salary to PERS. PEIA is required to contribute 10.5% of covered employees' salaries to PERS. The required employee and employer contribution percentages are determined by actuarial advisement within ranges set by statute. PEIA and employee contributions, both the statutorily required and actual contributions made, for the three years ended June 30 are as follows:

	<u>2009</u>	<u>2008</u>	<u>2007</u>
Employer contributions (10.5%)	\$ 163,469	\$ 167,079	\$ 136,720
Employee contributions (4.5%)	70,058	71,605	58,594
Total contributions	<u>\$ 233,527</u>	<u>\$ 238,684</u>	<u>\$ 195,314</u>

PEIA's contributions to the retirement plan for each of the years indicated above were equal to its required contributions. The contributions are included in other operating expenses in the basic financial statements.

The Consolidated Public Retirement Board (CPRB) administers the State's retirement systems. CPRB prepares separately issued financial statements covering the State's retirement systems, including PERS, which can be obtained from the Consolidated Public Retirement Board, 4101 MacCorkle Avenue, S.E., Charleston, West Virginia 25304-1636.

### 9. Postemployment Benefits Other Than Pension Benefits

#### Other Postemployment Benefits

PEIA participates in a cost-sharing, multiemployer, defined benefit other postemployment benefit plan that covers the retirees of State agencies, colleges and universities, county boards of education, and other government entities as set forth in the West Virginia Code. Financial activities of the OPEB plan are accounted for in the RHBT. The plan provides the following retiree group insurance coverage to participants: medical and prescription drug coverage through a self-insured plan and through external managed care organizations, basic group life, accidental death, and prescription drug coverage for retired employees of the State and various related State and non-State agencies and their dependents. Details regarding this plan and a copy of the RHBT financial report can be obtained by contacting Public Employees Insurance Agency, 601 57<sup>th</sup> Street Southeast, Suite 2, Charleston, West Virginia 25304-2345 or by calling 1-888-680-7342.

# West Virginia Public Employees Insurance Agency

## Notes to Financial Statements (continued)

### 9. Postemployment Benefits Other Than Pension Benefits (continued)

Upon retirement, an employee may apply unused sick leave and/or annual leave to reduce their future insurance premiums paid to RHBT. Substantially all employees hired prior to July 1, 2001, may become eligible for these benefits if they reach normal retirement age while working for PEIA. According to West Virginia State Code, employees hired prior to June 30, 1988, can receive health care credit against 100% of their health care coverage. Employees hired between June 30, 1988 and June 30, 2001, can receive health care credit against 50% of their health care cost. Employees hired July 1, 2001, or later, may not convert sick leave into a health care benefit.

Beginning July 1, 2007, PEIA adopted GASB Statement No. 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions* (GASB 45) which provides guidance on all aspects of other postemployment benefit reporting by employers. This Statement establishes standards for the measurement, recognition, and display of OPEBs (including health care and life insurance) expense/expenditures and related liabilities (assets), note disclosures, and, if applicable, required supplementary information (RSI) in the financial reports of state and local governmental employers. The GASB statement is based on the premise that the “costs” of employee services should be reported during the periods when the services are rendered. For “employer” OPEB reporting, the State and PEIA report “expense” on an accrual basis in the amount of the “annual required contribution” and a “liability” for the amount of the “annual required contribution” that was not actually paid.

Historically, PEIA recorded compensated absences under the provisions of GASB Statement No. 16, *Accounting for Compensated Absences*, and recorded a liability for the conversion of sick leave into OPEB health care benefits, which was included as part of the compensated absences liability. Under GASB 45, the conversion of sick leave into OPEB health care benefits is now required to be accounted for as part of the OPEB obligation. In conjunction with the adoption of GASB 45, which was adopted prospectively, PEIA adjusted the net asset balance as of July 1, 2007, to account for the effect of this change in accounting principle by reducing the OPEB portion of the compensated absences liability recorded under the old methodology to zero (in thousands).

Net assets balance as reported June 30, 2007	\$ 174,074
Cumulative effect of change in accounting principle for other postemployment benefits	275
Net asset balance as adjusted July 1, 2007	<u>\$ 174,349</u>



## West Virginia Public Employees Insurance Agency

### Notes to Financial Statements (continued)

#### **9. Postemployment Benefits Other Than Pension Benefits (continued)**

Legislation requires RHBT to determine through an actuarial study, the contractually required contribution (CRC) which shall be sufficient to maintain the RHBT in an actuarially sound manner. The CRC is allocated to respective cost-sharing employers, including PEIA, who are required by law to fund at least the minimum annual premium component of the CRC. Revenues collected by RHBT shall be used to fund current OPEB health care claims and administrative expenses with residual funds held in trust for future OPEB costs. Based on the actuarial studies completed, the contractually required contribution rates were determined for the fiscal year ended June 30, 2009 and 2008. PEIA's contributions to the RHBT were \$63,800 and \$81,900 for fiscal years 2009 and 2008, respectively, which represent 48.5% and 49.4% of the contractually required contributions. The cumulative unpaid of \$98,000 and \$30,000 for fiscal year 2009 and 2008, respectively, is recorded in other accrued liabilities in the statements of net assets. The State on PEIA's behalf has paid \$43,000 towards the annual required contribution for fiscal years 2008.

The Code provides that contribution requirements of the members and the participating employers are established and may be amended by the RHBT Finance Board. A non-Medicare plan member or beneficiaries receiving benefits contributes monthly premiums ranging from \$208 to \$919 per month for retiree only coverage, and from \$421 to \$2,184 per month for retiree and spouse coverage. Medicare covered retirees are charged premiums ranging from \$68 to \$453 per month for retiree only coverage, and from \$113 to \$945 per month for retiree and spouse coverage. Monthly premiums vary based on years of service and choice of coverage.

#### **10. Litigation**

PEIA is engaged in various legal actions that it deems to be in the ordinary course of business. PEIA believes that it has adequately provided for probable costs of current litigation. As these legal actions are resolved, however, PEIA could realize positive and/or negative impact to its financial performance in the period in which these legal actions are ultimately decided.

# Required Supplementary Information

# West Virginia Public Employees Insurance Agency

## Ten-Year Claims Development Information (Unaudited)

The table below illustrates how PEIA's earned premiums (net of reinsurance) and investment income compare to related costs of loss (net of loss assumed by reinsurers) and other expenses assumed by PEIA as of the end of each of the years presented. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's earned and ceded premiums, administrative fees, other operating, and investment revenues. (2) This line shows each fiscal year's other operating costs of PEIA including overhead and unallocated claims expense not allocable to individual claims. (3) This line shows PEIA's incurred and ceded claims and allocated claims adjustment expense (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage occurred (called accident year). (4) These lines show the cumulative amounts paid as of the end of successive years for each accident year. (5) This line shows the most current estimate of losses assumed by reinsurers for each accident year. (6) These lines show how each accident year's incurred claims increased or decreased as of the end of successive years. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (7) This line compares the latest reestimated net incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of net claims cost is greater or less than originally thought. As data for individual accident years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature accident years. The columns of the table show data for successive accident years.

	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
<i>(In Thousands)</i>										
1) Premiums, investment, and other revenues										
Earned	\$ 388,179	\$ 417,673	\$ 432,220	\$ 501,170	\$ 575,420	\$ 591,470	\$ 657,858	\$ 502,666	\$ 433,959	\$ 460,756
Ceded	75,298	76,656	51,962	56,730	61,833	55,846	62,467	59,228	60,596	60,187
Net earned	312,881	341,017	380,258	444,440	513,587	535,624	595,391	443,438	373,363	400,569
2) Unallocated expenses	14,564	16,754	16,531	21,195	23,347	23,579	26,036	20,321	25,038	23,627
3) Estimated incurred claims and allocated claims adjustment expense, end of accident year:										
Incurred	334,802	388,645	431,544	450,592	493,230	542,512	580,561	419,070	437,694	460,476
Ceded	75,298	76,656	51,962	56,730	61,833	55,846	62,467	59,228	60,596	60,187
Net incurred	259,504	311,989	379,582	393,862	431,397	486,666	518,094	359,842	377,098	400,289
4) Paid (cumulative) claims and allocated claims adjustment expense as of:										
End of accident year	217,771	262,116	327,451	343,939	379,101	426,562	460,973	320,480	335,380	354,773
One year later	254,001	310,090	374,269	390,420	428,176	487,303	507,194	362,605	373,609	
Two years later	254,852	310,047	374,685	388,999	428,218	487,237	507,479	363,147		
Three years later	254,887	309,981	374,465	388,911	428,218	487,237	507,479			
Four years later	254,887	309,981	374,465	388,911	428,218	487,237				
Five years later	254,887	309,981	374,465	388,911	428,218					
Six years later	254,887	309,981	374,465	388,911						
Seven years later	254,887	309,981	374,465							
Eight years later	254,887	309,981								
Nine years later	254,887									
5) Reestimated ceded claims and expenses	75,298	76,656	51,962	56,730	61,833	55,846	62,467	59,228	60,596	-
6) Reestimated net incurred claims and allocated claims adjustment expense:										
End of accident year	259,504	311,989	379,582	393,862	431,397	486,666	518,094	359,842	377,099	400,289
One year later	256,492	319,539	375,350	389,662	428,567	487,656	517,884	358,832	374,948	
Two years later	255,440	319,306	375,050	389,162	428,687	487,536	517,854	359,112		
Three years later	255,355	319,076	374,920	389,352	428,687	487,556	518,154			
Four years later	255,270	319,076	374,920	389,352	428,687	487,556				
Five years later	255,270	319,076	374,920	389,352	428,687					
Six years later	255,270	319,076	374,920	389,352						
Seven years later	255,270	319,076	374,920							
Eight years later	255,270	319,076								
Nine years later	255,270									
7) Increase (decrease) in estimated net incurred claims and allocated claims adjustment expense from end of accident year	(4,234)	7,087	(4,662)	(4,510)	(2,710)	890	60	(730)	(2,150)	-

Note: The above financial data is summarized for individual contract periods. Subsequent premium and related expense adjustments and reserve developments are recorded in the year incurred for fiscal year financial reporting but are included in the applicable contract year for purposes of the above schedule. Accordingly, components of change in net assets as determined on contract-year basis will differ from that included in PEIA's fiscal year financial statements

## Other Financial Information

West Virginia Public Employees Insurance Agency

Deposits Disclosure

Form 7

June 30, 2009  
(In Thousands)

	<b><u>Carrying Amount</u></b>
Cash with Treasurer	\$ 1,399,113
Deposit in transit	–
Cash in outside bank accounts	<u>1,301,132</u>
Total carrying amount of deposits	2,700,245
Cash equivalents (with BTI)	<u>41,032,876</u>
Total cash	<u><u>\$ 43,733,121</u></u> (1)

(1) Agrees to audited statement of net assets as follows:

Cash and cash equivalents	\$ 2,700,245
Equity position in internal investment pool – current	33,294,218
Equity position in internal investment pool – noncurrent and restricted	<u>7,738,658</u>
Total cash equivalents	<u><u>\$ 43,733,121</u></u> (2)

(2) Agrees to audited statement of cash flows. \$ 43,733,121

# West Virginia Public Employees Insurance Agency

## Investments Disclosure

### Form 8

June 30, 2009

*(In Thousands)*

<b>Investment Pool</b>	<b>Amount Unrestricted</b>	<b>Amount Restricted</b>	<b>Amount Reported</b>	<b>Fair Value</b>
West Virginia Board of Treasury				
Investments (BTI):				
WV Money Market Pool	\$ 33,294,218	\$ 7,738,658	\$ 41,032,876	\$ 41,032,876
Total equity position in internal investment pool with BTI	<u>\$ 33,294,218</u> (1)	<u>\$ 7,738,658</u> (1)	<u>\$ 41,032,876</u>	<u>\$ 41,032,876</u>
West Virginia Investment Management				
Board (IMB) Investment Pools:				
Short-term fixed income	\$ 729	\$ -	\$ 729	729
Total return fixed income	53,033,279	-	53,033,279	53,033,279
Core fixed income	21,406,991	-	21,406,991	21,406,991
Fixed income nonqualified	-	-	-	-
Large cap domestic	7,324,285	-	7,324,285	7,324,285
Non-large cap domestic	1,313,442	-	1,313,442	1,313,442
International nonqualified	3,053,587	-	3,053,587	3,053,587
Hedge fund	22,682,651	-	22,682,651	22,682,651
International equity	6,257,528	-	6,257,528	6,257,528
Total equity position in internal investment pools with IMB	<u>\$ 115,072,492</u>	<u>\$ -</u>	<u>\$ 115,072,492</u>	<u>\$ 115,072,492</u> (1)

(1) Agrees to audited statement of net assets as follows:

Equity position in internal investment pool - current	\$ 33,294,218
Equity position in internal investment pools - noncurrent	115,072,492
Equity position in internal investment pool - noncurrent and restricted	<u>7,738,658</u>
Total equity position in internal investment pools	<u>\$ 156,105,368</u>

West Virginia Public Employees Insurance Agency

Deposits and Investments Disclosure

Form 8-A

June 30, 2009  
(In Thousands)

Reconciliation of cash and cash equivalents and investments as reported in the financial statements to the amounts disclosed in the footnotes:

Cash and cash equivalents as reported \$ 2,700,245 (1)

Equity position in internal investment pools as reported \$ 156,105,368 (2)

(1) Agrees to audited statement of net assets.

(2) Agrees to Form 8.

# West Virginia Public Employees Insurance Agency

## Accounts Receivable

### Form 9

June 30, 2009  
(In Thousands)

Total accounts receivable	\$ 38,571,773 (1)
Less allowance for doubtful accounts	<u>(5,422,610) (1)</u>
Net receivable	<u><u>\$ 33,149,163</u></u>

(1) Agrees to audited statement of net assets as follows:

Premium receivable:	
Due from State of West Virginia	\$ 2,324,756 (2)
Other, net	24,141,999 (2)
Add allowance for doubtful accounts	4,971,023 (2)

Accounts receivable:	
Provider refunds, net	469,046 (2)
Add allowance for doubtful accounts	451,587 (2)
Prescription rebates	5,960,234 (2)
Other	<u>253,128 (2)</u>
Total accounts receivable	<u><u>\$ 38,571,773</u></u>

Allowance for doubtful accounts:	
Premium receivable – other	\$ 4,971,023 (2)
Provider refunds	<u>451,587 (2)</u>
	<u><u>\$ 5,422,610</u></u>

(2) Agrees to the audited statement of net assets.



West Virginia Public Employees Insurance Agency

Due (To) From Primary Government

Form 10

June 30, 2009  
(In Thousands)

<b>Agency</b>	<b>Total</b>
West Virginia Lottery Commission	\$ -
Workforce WV/Payroll-05303	5
Workers Compensation Commission	155
	<u>160</u>
West Virginia Retiree Health Benefit Trust Fund	-
WV Public Employees Retirement Board	164
WV Public Employees Retirement Board	(144)
WV Teachers Retirement Board	(355)
Consolidated Retirement Bd/Judges Ret.	(7)
Deputy Sheriffs Retirement	(120)
Public Safety/Con.Pub.Emp.Ret.Bd.	(14)
	<u>(476)</u>
Senate	4
House of Delegates	(10)
Joint Comm on Govt and Finance	8
Supreme Court / Judicial	(37)
Governors Office	(2)
Homeland Security - Emergency Management	-
Auditors Office	3
Treasurer of State's Office	-
Tax Department	101
Tax Division	-
Tax Department – Budget Office	2
Tax Department – Office of Appeals	-
Attorney General	11
Secretary of State	6
Department of Education	209
WV Secondary Schools Activities Comm	6
Division of Forestry	30
WV School for the Deaf and Blind	3
Library Commission	9

West Virginia Public Employees Insurance Agency

Due (To) From Primary Government

Form 10 (continued)

(In Thousands)

<b>Agency</b>	<b>Total</b>
Culture and History	(15)
Department of Corrections	(22)
Anthony Correctional Center	(9)
Huttonsville Correctional Center	286
Pruntytown Correctional Center	6
Northern Correctional Facility	22
Mt Olive Correctional Facility	95
Department of Corrections/St. Marys Corr	75
Department of Corrections/Denmar Facility	(3)
WV Division of Juvenile Services	84
Ohio County Correctional Center	(9)
Health Department	865
Veterans Affairs	59
Pinecrest Hospital	34
Welch Emergency Hospital	6
William R Sharpe Jr Hospital	13
Mildred Mitchell-Bateman Hospital	234
Lakin State Hospital	14
Lakin Correctional Facility	2
John Manchin Sr. Health Care	35
Hopemont State Hospital	(3)
Division of Rehabilitation Services	176
Department of Labor	-
Office of Miners Health, Safety and Training	9
Division of Environmental Protection	12
WV Division of Energy	5
Agriculture	(2)
Geological Survey	1
Department of Education and Arts	(10)
Military Affairs and Public Safety	2
Division of Protective Services	(9)
Department of Transportation	-
WV Board of Chiropractic Examiners	-

West Virginia Public Employees Insurance Agency

Due (To) From Primary Government

Form 10 (continued)

(In Thousands)

<b>Agency</b>	<b>Total</b>
Environmental Quality Board	(3)
Public Safety	(16)
Adjutant General	(12)
WV Board of Optometry	-
Human Rights Commission	11
Fire Commission	(1)
Department of Highways	37
Public Port Authority	(1)
Aeronautics Commission	-
Motor Vehicles	6
Coal Heritage Highway Authority	-
Bureau of Senior Services	(3)
Criminal Justice/Highway Safety	(2)
Public Transit	-
Real Estate Commission	2
Insurance Commission	(99)
WV Radiologic Technology	1
Oil and Gas Conservation	-
WV Board of Accountancy	(2)
WV Board of Dental Examiners	(1)
WV Board of Professional	-
WV Board of Pharmacy	-
WV State Bd of Examiners For LPNs	-
WV Engineers Registration Board	1
WV Board of Osteopathy	-
WV Bd of Examiners/Registered Nurses	4
WV Board of Veterinary Medicine	-
WV Massage Therapy Licensure Bd	-
Board of Funeral Service Examiners	-
Department of Administration	(3)
WV Barbers and Beauticians Commission	6
Public Service Commission	-
WV Economic Development Authority	-

West Virginia Public Employees Insurance Agency

Due (To) From Primary Government

Form 10 (continued)

(In Thousands)

<b>Agency</b>	<b>Total</b>
Natural Resources	(30)
Municipal Bond Commission	(3)
Board of Examiners In Counseling	(2)
WV Board of Social Worker Examiners	3
ABC Commission	2
Board of Exam Speech	-
Board of Examiners of Psychologists	-
Board of Respiratory Care	(1)
Department of Human Services	345
Division of Tourism	11
Health Care Authority	-
House of Delegates	9
Martinsburg Correctional Center	16
Senate	3
WV Armory Board	8
WV Board of Occupational Therapy	-
WV Board of Physical Therapy	-
WV Center For Nursing	-
WV Division of Banking	(7)
WV Military Authority	(7)
WV Real Estate Appraiser/Lic Cert Bd	(1)
	<u>2,567</u>
Total Primary Government	2,251
Total Component Units	73
	<u><u>\$ 2,324</u></u>

West Virginia Public Employees Insurance Agency

Component Unit – A/R Balances

Form 11

June 30, 2009  
(In Thousands)

<b>Unit</b>	<b>Amount</b>
Higher Education	\$ (150)
Parkways, EDA, and Tourism	(6)
Regional Jail and Correction Facility Authority	166
Public Defender Corporation	45
WV EDA	(11)
Educational Broadcasting	12
School Building Authority	(5)
Railroad Maintenance Authority	1
Racing Commission	20
WV Jobs Investment Trust	–
Housing Development Corporation	2
Water Development Authority	–
SWMB	(1)
WSWP - TV	(1)
	1
	<u>\$ 73</u>

STATE OF WEST VIRGINIA  
 DEPARTMENT OF ADMINISTRATION - FINANCE DIVISION  
 FINANCIAL ACCOUNTING AND REPORTING SECTION

**FORM 15**

GAAP REPORTING FORM - TRANSFERS IN/OUT

Audited Agency **Public Employees Insurance Agency**

Indicate amounts transferred from/to your agency as of June 30, 2009.

<b>WVFIMS Doc. ID</b>	<b>Agency Transferring From</b>	<b>WVFIMS FUND</b>	<b>Agency Transferring To</b>	<b>WVFIMS FUND</b>	<b>Amount</b>
<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>5</b>	<b>6</b>
D1463003	PEIA	2180	Insurance Commission	7160	\$ 7,320
<b>Total</b>					<b>\$ 7,320</b>

\*Do not include IGTs, Reimbursements or Expense to Expense transactions.

Explain Transfers In/Out amounts greater than or equal to \$1,000,000. PEIA statutory transfer per SB 125.

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## 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*

The Finance Board  
West Virginia Public Employees Insurance Agency

We have audited the financial statements of the West Virginia Public Employees Insurance Agency (PEIA) as of and for the year ended June 30, 2009, and have issued our report thereon dated February 4, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

### **Internal Control Over Financial Reporting**

In planning and performing our audit, we considered PEIA's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of PEIA's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of PEIA's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2009-01, 2009-02, and 2009-03 to be material weaknesses.

## Compliance and Other Matters

As part of obtaining reasonable assurance about whether PEIA's financial statements are free of 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*.

PEIA's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit PEIA's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, the Finance Board, and others within the entity, and is not intended to be, and should not be, used by anyone other than these specified parties.

*Ernst + Young LLP*

February 4, 2010



**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS**

**State Agency**

Public Employees Insurance Agency (PEIA)

- Criteria:** Management is responsible for establishing and maintaining adequate controls over changes to and processes to maintain its information systems.
- Condition:** The following IT general controls findings related to the BAS and Great Plains applications were noted:
- **Manage Changes – Authorization, Testing, and Approval**

During our review of the Great Plains and BAS application change management process, management indicated that the change requests were to be authorized via the weekly task lists; however, we were unable to obtain any documentation surrounding the process. Additionally, no documentation was available to support that the changes/upgrades had been effectively tested and that the change/upgrade obtained final approval for migration to the production environment.
  - **Manage Changes – OS and DB Upgrades/Patches**

The process for applying operating system and database upgrades and/or patches (for the Great Plains application) is informal, and no documentation is maintained to support the operating system or database upgrades/patches were authorized, tested, and approved prior to production migration.
  - **Logical Access – Password Settings**

The Great Plains application password settings, due to functionality limitations, are not configured to 1) be a minimum number of characters in length, 2) force password expirations after a set number of days, 3) lock out user accounts after a defined number of invalid login attempts, and 4) prevent users from reusing their previously used passwords.
  - **Logical Access – Administrator Access**

Access to the PROGRAMMER function (which grants users the ability to perform user administration for the BAS application) is not restricted to authorized individuals. This function is granted to three authorized administrators and four programmers.
  - **Logical Access – New User Access Authorization**

New user access is not consistently documented via e-mails or SATT forms for user access to Great Plains or BAS. Documentation is either not retained or does not include the system whereby access is required, or the type of access to be granted.
- Context:** The information systems conditions noted above could affect the accuracy of processing PEIA and RHBT financial information, including premiums/contributions.
- Cause:** During the time of our review, management is still in the process of defining and implementing their controls related to program change management and logical access processes. Additionally, management is working with the West Virginia Office of Technology to determine where controls are the responsibility of the agency versus the hosting facility.

**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS  
(continued)**

**State Agency**  
Public Employees Insurance Agency (PEIA)

**Effect:**

- **Manage Changes – Authorization, Testing, and Approval**  
Lack of formal written policies and procedures for application changes and upgrades does not contribute to an effective environment and could lead to inconsistencies in protocol or documentation. Without proper documentation of authorization, user acceptance testing, and migration approval, implemented changes to the production environment may not be operating as intended.
- **Manage Changes – OS and DB Upgrades/Patches**  
Lack of formal written policies and procedures for patches and upgrades does not contribute to an effective environment and could lead to inconsistencies in protocol or documentation. Without proper documentation of authorization, user acceptance testing, migration approval, and implemented changes to the production environment may not be operating as intended.
- **Logical Access – Password Settings**  
The current password settings could lead to unauthorized access to sensitive and/or confidential information.
- **Logical Access – Administrator Access**  
Improper administrator access could lead to inappropriate or excessive user access rights being granted to existing users.
- **Logical Access – New User Access Authorization**  
The lack of controls surrounding the authorization and approval of system access could lead to inappropriate or excessive user access rights being granted to existing users.

**Recommendation:** Based on the findings noted, outlined below are the recommendations:

- **Manage Changes – Authorization, Testing, and Approval**  
Management should implement formal (written) policies and procedures surrounding Great Plains and BAS program changes (modifications or upgrades) to include documentation of authorization, testing, and approval.
- **Manage Changes – OS and DB Upgrades/Patches**  
Management should implement formal (written) policies and procedures surrounding the upgrades and/or patches applied to the operating system and database upgrades supporting the Great Plains application.
- **Logical Access – Password Settings**  
Management should work with the application vendor to enhance password security. The following are considered leading industry practice.
  - Require passwords to be six to eight characters in length.
  - Force passwords to expire every 60 to 90 days.

**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS  
(continued)**

**State Agency**

Public Employees Insurance Agency (PEIA)

- Automatically lock user accounts after three to five unsuccessful logon attempts.
- Prevent users from reusing previously used passwords by maintaining a password history file.
- Logical Access – Administrator Access  
Management should restrict access to the privileged roles within the BAS application and limit them to a select number of IT personnel who require such access.  
If preventive measures cannot be taken, due to system limitations, management should consider performing a periodic review of all changes to user security for the BAS application to determine if the changes were performed by authorized individuals. Management should confirm that adequate documentation is maintained to provide evidence (sign-offs, hard-copy reports, etc.) of the review.
- Logical Access – New User Access Authorization  
Management should enhance the current application access administration processes to verify that all user access is consistently documented with access details (access needed per system) and management approval is granted prior to gaining access to the systems. Management should verify that adequate documentation is maintained to provide evidence (sign-offs, e-mails, SATT forms, etc.) of the authorization and approval.

**Views of  
Responsible  
Officials and  
Planned Corrective  
Actions:**

We are in the process of rolling out a new change control system (PITS). This will allow the PEIA staff to make formal request to the IT staff and will track the request within this system. The system is in production at this point and is being used by the PEIA Finance Group and the PEIA Eligibility Group. The complete rollout is scheduled to be complete by April 1, 2010.

A formal procedure was developed in April 2008. However, PEIA will need to work closer with WVOT to make sure that all patches are documented according to the procedure.

When attempting to log on in GP a call is made to SQL Server to verify the userid and password. SQL Server is under the constraints to only allow four attempts. The current version of GP (9.0) uses all four attempts to verify one attempt in GP. Therefore if the restrictions were turned on in GP there would be no room for error. Because the SQL Server is maintained by WVOT and is a statewide process, the attempts cannot be increased through SQL Server. Therefore PEIA's only option is to move to GP version 10 or 11. These versions are equipped to handle this issue. PEIA plans to move to one of these versions before the end of FY 2010.

**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS  
(continued)**

**State Agency**

Public Employees Insurance Agency (PEIA)

In the original design of BAS there was an admin role, which was intended for the PEIA IT personnel to be able to add, term, or modify a user's role in BAS. This role had no other function within the system. After a consolidation of IT staff to WVOT, it became necessary for the programming staff to take on the Admin role of BAS, and therefore the programmer role was changed to have admin rights. A new role is now being created that would allow only Admin Authorized programmers to have Admin rights in the system. This programming will be completed by November 30, 2009.

We will be moving the access role into the PITS system and eliminating SATT. This will allow the PEIA staff to request access to various systems, and the system will track the approval process as well as the actual process of giving the access. This will be completed in spring of 2010.

**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-2 YEAR-END FINANCIAL STATEMENT CLOSING PROCESS**

**State Agency**

Public Employees Insurance Agency (PEIA)

**Criteria:** A critical element of an entity's internal control over financial reporting is its ability to record, process, and to summarize accounting transactions in a timely manner and to prepare financial statements that give a true and accurate assessment of the entity's financial status. Timely and accurate financial statements are crucial to effective decision-making by management.

Further, a fundamental concept of effective internal control over financial reporting is supervision and review of general ledger activities, including journal entries.

**Condition:** During fiscal year 2008, PEIA management implemented a new information system that is utilized in accounting and financial reporting for PEIA and RHBT. Prior year system implementation issues continued to impact current year financial reporting. Issues are noted as follows:

- Significant delays in being able to produce reliable PEIA financial statements. Accounting personnel did not fully implement the system in developing year-end financial statements. Rather, many closing entries were posted to the trial balance on Excel-based spreadsheets.
- Several accounts, including cash and investments, were not properly reconciled in a timely manner, resulting in significant adjustments upon completion of the reconciliations at year-end.
- Significant issues were noted in the premium billing and collection process as participating agencies and PEIA personnel went through the learning curve of understanding the complexity of the system. At the beginning of the current fiscal year due to held check issues, significant PEIA staff time was spent reconciling employer account balances, including the split between PEIA and RHBT amounts due.
- Delays were noted in accurately reporting the due to/from RHBT balance. For example, we noted one instance in which a reimbursement paid by RHBT to PEIA was recorded through an expense account.
- Further, we noted that the BAS relies significantly on systematic batched transactions, and there was not a systematic control to verify the batch transactions were balancing prior to posting in GP during the fiscal year. We are not aware of a formal reconciliation process in place to ensure these transactions were properly reported in GP. In addition, controllers and the Premium Accounts Division create and post journal entries in the general ledger without supervisory review and approval of entries.

**Context:** Management was not able to produce accurate and complete financial statements for PEIA until late January 2010.

**Cause:** Management indicated that problems related to the prior year system implementation lasted longer than they expected.

The current procedures do not require journal entries to be reviewed and approved.

**Effect:** Management was unable to provide financial statements to executive management and the Finance Board in a timely manner.

Without proper review and approval of journal entries, errors or irregularities could occur and not be detected.

**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-2 YEAR-END FINANCIAL STATEMENT CLOSING PROCESS  
(continued)**

**State Agency**  
Public Employees Insurance Agency (PEIA)

**Recommendation:** Management has spent a significant amount of time to date in fiscal year 2010 focused on refining fiscal year 2009 and 2010 financial information. Consequently, sufficient resources should be devoted to refining the fiscal year 2010 information to date and in the future to ensure that accurate and timely financial statements are produced. As part of this process, all accounts should be reconciled in a timely manner. Furthermore, management should evaluate the root cause of the system issues encountered and determine the necessary corrective action to prevent their reoccurrence (e.g., additional training, hiring additional staff, new policies and procedures). For instance, procedures should be established requiring the reconciliation of the online portal information with the GP national account level information. Management should also implement their procedures to follow up on and resolve participant credit balances in a timely manner.

With the new system, management has the ability to generate premiums/contributions aging reports and collection history. Accordingly, we recommend that management challenge the methodology for estimating the allowance for doubtful accounts and begin using actual collection history by aging category based on hindsight analysis to determine the allowance percentage by aging category.

Policies and procedures should be developed requiring limiting the individuals that have the ability to create and post journal entries in the general ledger. In particular, IT personnel should not have the ability to make journal entries. Additionally, the policies and procedures should require that journal entries be reviewed and approved by supervisory personnel and documentation be maintained supporting the entries.

**Views of  
Responsible  
Officials and  
Planned Corrective  
Actions:**

PEIA agrees with this issue in that the timeliness and accurate reporting of financial information is imperative. PEIA will be requiring all transactions to be accounted for in the financial system for FY 2010 and instituting more controls on the journal entry process. Moreover, the main cause of un-timely reporting was the cash reconciliation. This issue has already seen substantial improvement during FY 2010 as the frequency of reconciling items has reduced due to previously implemented controls.

PEIA will be reviewing the implementation process for additional controls to provide assurance that all batch postings are accurate before posting.

Beyond the held checks from the beginning of fiscal year 2009, there are no further issues with holding checks and the issues associated.

**STATE OF WEST VIRGINIA  
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-03 ACCOUNTS PAYABLE CUTOFF**

**State Agency**  
Public Employees Insurance Agency (PEIA)

- Criteria:** In accordance with U.S. generally accepted accounting principles, accounts payable reported in the financial statements should include all expenditures incurred and unpaid by the government as of the balance sheet date. Further, a fundamental concept of effective internal control over financial reporting is supervision and review of general ledger activities, including journal entries.
- Condition:** We reviewed the accounts payable detail and noted that several paid invoices remained in the balance at year-end. The payments had been posted but had not been applied to the invoices, which remained open. One invoice has already been voided but remained open in the general ledger. In addition, miscellaneous accounts payable represented services or goods received before year-end that had not been invoiced and were misclassified within the accounts payable balance instead of the other accrued liabilities balance.
- Context:** Accounts payable was overstated by \$667,000. Miscellaneous accounts payable was overstated by \$192,000 and was misclassified as part of accounts payable on the statement of net assets presentation.
- Cause:** Proper training was not provided to accounting staff to understand the accounts payable process.
- Effect:** The initial draft of the financial statements did not fairly state or classify accounts payable and accrued liabilities as of June 30, 2009.
- Recommendation:** Management should establish procedures to ensure that all personnel are properly trained in the accounts payable process and are properly supervised. An accounting manual should be compiled in order to guide new employees who are involved in the accounts payable process.
- Views of Responsible Officials and Planned Corrective Actions:** PEIA concurs and will implement the necessary steps to prevent this issue from occurring again. Weekly reviews of the aging report in conjunction with FIMS payments will occur to identify any dated or paid invoices immediately.

**Ernst & Young LLP**

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