# STATE INSURANCE DEPARTMENT

## Annual Financial Report

**June 30, 2018**

LEGISLATIVE JOINT AUDITING COMMITTEE

# STATE INSURANCE DEPARTMENT
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# FOR THE YEAR ENDED JUNE 30, 2018



## FINANCIAL STATEMENTS



## OTHER INFORMATION (Unaudited)

Arkansas

Sen. Jason Rapert
Senate Chair
Sen. Eddie Cheatham
Senate Vice Chair

Rep. Richard Womack
House Chair
Rep. DeAnn Vaught
House Vice Chair

Roger A. Norman, JD, CPA, CFE, CFF
Legislative Auditor

LEGISLATIVE JOINT AUDITING COMMITTEE
ARKANSAS LEGISLATIVE AUDIT

## INDEPENDENT AUDITOR'S REPORT

State Insurance Department
Legislative Joint Auditing Committee

***Report on the Financial Statements***

We have audited the accompanying financial statements of the major fund and the aggregate remaining fund information of the State Insurance Department, a department of Arkansas state government, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the State Insurance Department's departmental financial statements as listed in the table of contents.

***Management's Responsibility for the Financial Statements***

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

***Auditor's Responsibility***

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

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

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

***Opinions***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the major fund, and the aggregate remaining fund information of the State Insurance Department as of June 30, 2018, changes in financial position thereof, and the budgetary comparison for the general fund for the year then ended, in accordance with accounting principles generally accepted in the United States of America.

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***Emphasis of Matter***

As indicated above, the financial statements of the State Insurance Department are intended to present the financial position, the changes in financial position, budgetary comparisons of only that portion of the major fund, and the aggregate remaining fund information of the State that is attributable to the transactions of the State Insurance Department. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2018, the changes in its financial position, and budgetary comparisons for the year then ended in accordance with accounting principles generally accepted in the United States of America. Our opinion is not modified with respect to this matter.

***Other Matters***

*Required Supplementary Information*

The Governmental Accounting Standards Board requires that a Management's Discussion and Analysis be presented to supplement government-wide financial statements. However, as discussed in the "Emphasis of Matter" paragraph above, the financial statements of the State Insurance Department are only for the specific transactions and activity of the Agency and not for the State as a whole. Therefore, the Management's Discussion and Analysis is not required to be presented for the State Insurance Department individually. Our opinions on the departmental financial statements is not affected by the omission of this information.

*Other Information*

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the State Insurance Department's departmental financial statements. The Schedule of Selected Information and Other General Information are presented for purposes of additional analysis and are not a required part of the departmental financial statements.

The Schedule of Selected Information and Other General Information have not been subjected to the auditing procedures applied in the audit of the departmental financial statements, and accordingly, we do not express an opinion or provide any assurance on this information.

***Other Reporting Required by Government Auditing Standards***

In accordance with *Government Auditing Standards,* we have also issued our report dated October 16, 2019 on our consideration of the State Insurance Department's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is solely to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the State Insurance Department's internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the State Insurance Department's internal control over financial reporting and compliance.

ARKANSAS LEGISLATIVE AUDIT

Roger A. Norman

Roger A. Norman, JD, CPA, CFE, CFF
Legislative Auditor

Little Rock, Arkansas
October 16, 2019
SA1042518

Arkansas

Sen. Jason Rapert
Senate Chair
Sen. Eddie Cheatham
Senate Vice Chair

Rep. Richard Womack
House Chair
Rep. DeAnn Vaught
House Vice Chair

Roger A. Norman, JD, CPA, CFE, CFF
Legislative Auditor

LEGISLATIVE JOINT AUDITING COMMITTEE
ARKANSAS LEGISLATIVE AUDIT

**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***

**INDEPENDENT AUDITOR'S REPORT**

State Insurance Department
Legislative Joint Auditing Committee

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the major fund and the aggregate remaining fund information of the State Insurance Department (the "Agency"), a department of Arkansas state government, as of and for the year ended June 30, 2018, and the related notes to the financial statements, which collectively comprise the State Insurance Department's departmental financial statements, and have issued our report thereon dated October 16, 2019.

***Internal Control Over Financial Reporting***

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

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and therefore, material weaknesses or significant deficiencies may exist that have not been identified. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. We did identify certain deficiencies in internal control, described in the accompanying Schedule of Findings and Responses as items *2018-1 and 2018-2* that we consider to be significant deficiencies.

***Compliance and Other Matters***

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

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## SCHEDULE OF FINDINGS AND RESPONSES

2018-1 The Agency failed to retire timely four assets totaling $2,987. Additionally, two assets totaling $1,581 could not be located for observation.

We recommend the Agency perform an annual inventory of capital assets and update the capital asset master list in AASIS.

***Management personnel responded:*** *The Arkansas Insurance Department (AID) has divided asset responsibility between two divisions; IT for IT-related equipment and Accounting for all other items. The Accounting division recently conducted a comprehensive inventory of all non-IT assets throughout the Department, reconciled to AASIS, and submitted a request in June to retire a number of assets that could not be located. AID does not believe that any theft occurred, but instead old, low value assets had been discarded due to no longer functioning. The IT division was in the process of conducting this same exercise and has reviewed their procedures and added additional steps to ensure better inventory controls. Additions include performing annual physical inventory of all computer equipment, reconciling asset information with AASIS, and ensuring the removal of equipment from AASIS is performed by designated staff who has knowledge of asset removal.*

2018-2 Review of receipting procedures revealed the Public Employee Claims Division (PECD) failed to receipt six checks totaling $58,742 when received. Additionally, the Liquidation Division failed to deposit timely three checks totaling $6,612.

We recommend the Agency establish controls to ensure all monies are receipted and deposited timely.

***Management personnel responded:*** *The payments received into the Public Employee Claims Division were not listed on an internally kept Excel spreadsheet, but were listed in AASIS as they were deposited. This issue was remedied on July 1, 2019, by moving PECD onto the Cash Receipting System (CRS) tool that the rest of the Insurance Department uses. This requires verifying that the amounts entered in the detail tie out to the amount deposited, eliminating the chance that deposits do not tie to the checks received detail. Regarding the Liquidation Division, two situations led to the finding. One deposit of $105 was received on July 14, 2017, but not deposited until July 24, 2017, due to the Director being on vacation and a backup was not assigned for that time. Subsequently in May of 2018, a similar situation occurred; however, the checks were deposited into the Life and Health account instead of the Property and Casualty account. These were discovered during the bank reconciliation in early June and then corrected on June 13, 2018. In order to correct and prevent future issues, the Liquidation Division is also going to move all receipts to the CRS system, which requires that any receipts entered for deposit are verified by a second person. In addition, the Division Director will assign a backup for making deposits in the case of extended absences.*

### *Agency's Response to Findings*

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

### *Purpose of this Report*

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose. However, pursuant to Ark. Code Ann. § 10-4-417, all reports presented to the Legislative Joint Auditing Committee are matters of public record, and distribution is not limited.

ARKANSAS LEGISLATIVE AUDIT

Tom Bullington, CPA
Deputy Legislative Auditor

Little Rock, Arkansas
October 16, 2019

STATE INSURANCE DEPARTMENT
BALANCE SHEET – GOVERNMENTAL FUND
JUNE 30, 2018

Exhibit A

| | General Fund |
|---|---|
| ASSETS | |
| Cash and cash equivalents | $ 94,242,646 |
| Receivable, net: | |
| Loss recoveries | 1,716,977 |
| Interest | 98,124 |
| Due from fiduciary fund | 2,570,496 |
| Due from other state agencies | 414,085 |
| Prepaid items | 123,314 |
| TOTAL ASSETS | $ 99,165,642 |
| LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE | |
| Liabilities: | |
| Accounts payable - vendors | $ 24,869 |
| Accrued and other current liabilities | 402,788 |
| Unearned insurance premiums | 654,476 |
| Claims payable | 4,827,983 |
| Due to other governments | 14 |
| Due to other state agencies | 553,575 |
| Total Liabilities | 6,463,705 |
| Deferred inflows of resources: | |
| Related to revenues | 4,274,523 |
| Fund balance: | |
| Nonspendable - prepaid items | 123,314 |
| Restricted | 14,144,495 |
| Committed | 67,648,414 |
| Assigned | 6,699,928 |
| Unassigned | (188,737) |
| Total Fund Balance | 88,427,414 |
| TOTAL LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND FUND BALANCE | $ 99,165,642 |

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

STATE INSURANCE DEPARTMENT | Exhibit B

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE –
GOVERNMENTAL FUND
FOR THE YEAR ENDED JUNE 30, 2018

| | General Fund |
|---|---|
| REVENUES | |
| Federal grants and reimbursements | $ 1,249,841 |
| Insurance assessments and premiums | 20,598,043 |
| Insurance fraud fees per Act 337 of 1997 | 920,700 |
| Administrative and financial regulations | 30,223,549 |
| Bond premiums per Act 728 of 1997 | 799,971 |
| Fidelity bond recoveries | 87,296 |
| Examiners' travel expense reimbursements | 33,565 |
| Investment earnings | 281,504 |
| Other sales, refunds, and reimbursements | 7,412,445 |
| TOTAL REVENUES | 61,606,914 |
| Less: State Treasury service charge | 452,552 |
| NET REVENUES | 61,154,362 |
| EXPENDITURES | |
| Salary and benefits | 11,182,846 |
| Communication and transportation of commodities | 264,638 |
| Printing and advertising | 6,065 |
| Repairing and servicing | 210,598 |
| Utilities and rent | 1,345,188 |
| Travel and subsistence | 341,783 |
| Professional services | 2,004,813 |
| Insurance and bonds | 10,711,466 |
| Other expenses and services | 366,433 |
| Commodities, materials, and supplies | 217,957 |
| Refunds, taxes, and claims | 32,293,861 |
| Capital outlay | 309,973 |
| TOTAL EXPENDITURES | 59,255,621 |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | 1,898,741 |

STATE INSURANCE DEPARTMENT Exhibit B

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE –
GOVERNMENTAL FUND
FOR THE YEAR ENDED JUNE 30, 2018

| | General Fund |
|---|---|
| OTHER FINANCING SOURCES (USES) | |
| Interagency transfers: | |
| Claims funding | $ 13,040,902 |
| Other, net | (59,378) |
| Workers compensation administrative cost reimbursement | 1,681,923 |
| Prior-year warrants outlawed and cancelled | 3,025 |
| TOTAL OTHER FINANCING SOURCES (USES) | 14,666,472 |
| NET CHANGE IN FUND BALANCE | 16,565,213 |
| FUND BALANCE - JULY 1 | 71,862,201 |
| FUND BALANCE - JUNE 30 | $ 88,427,414 |

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

STATE INSURANCE DEPARTMENT

Exhibit C

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE –
BUDGET AND ACTUAL - GENERAL FUND
FOR THE YEAR ENDED JUNE 30, 2018

| | General Fund | | | |
|---|---|---|---|---|
| | Budgeted Amount | | | Variance With Final Budget Positive |
| | Original | Final | Actual | (Negative) |
| REVENUES | | | | |
| Federal grants and reimbursements | $ 6,832,693 | $ 6,832,693 | $ 1,249,841 | $ (5,582,852) |
| Insurance assessments and premiums | 42,074,443 | 42,074,443 | 20,598,043 | (21,476,400) |
| Insurance fraud fees per Act 337 of 1997 | | | 920,700 | 920,700 |
| Administrative and financial regulation fees | 15,834,437 | 15,834,437 | 30,223,549 | 14,389,112 |
| Bond premiums per Act 728 of 1997 | | | 799,971 | |
| Fidelity bond recoveries | 4,104,855 | 4,104,855 | 87,296 | (4,017,559) |
| Examiners' travel expense reimbursements | 100,000 | 100,000 | 33,565 | (66,435) |
| Investment earnings | | | 281,504 | 281,504 |
| Other sales, refunds, and reimbursements | | | 7,412,445 | 7,412,445 |
| TOTAL REVENUES | 68,946,428 | 68,946,428 | 61,606,914 | (8,139,485) |
| Less: State Treasury service charge | | | 452,552 | (452,552) |
| NET REVENUES | 68,946,428 | 68,946,428 | 61,154,362 | (7,792,066) |
| EXPENDITURES | | | | |
| Regular salaries | 9,258,336 | 9,322,597 | 8,305,741 | 1,016,856 |
| Extra help | 140,000 | 140,000 | 69,931 | 70,069 |
| Operating expenses | 5,275,558 | 23,219,499 | 13,464,671 | 9,754,828 |
| Personal services matching | 3,055,494 | 3,072,199 | 2,805,903 | 266,296 |
| Overtime | 35,000 | 35,000 | 13 | 34,987 |
| Conference fees and travel | 493,416 | 340,121 | 274,622 | 65,499 |
| Professional fees and services | 5,934,489 | 2,212,276 | 1,730,906 | 481,370 |
| Capital outlay | 155,000 | 345,551 | 309,973 | 35,578 |
| Investments | 760,637 | | | |
| Refunds/Reimbursements | 11,150,000 | 11,150,000 | 11,015,342 | 134,658 |
| Claims | 64,589,218 | 42,712,400 | 21,278,519 | 21,433,881 |
| Special maintenance | 50,000 | 40,000 | | 40,000 |
| TOTAL EXPENDITURES | 100,897,148 | 92,589,643 | 59,255,621 | 33,334,022 |
| EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES | (31,950,720) | (23,643,215) | 1,898,741 | 25,541,956 |

STATE INSURANCE DEPARTMENT Exhibit C

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE – BUDGET AND ACTUAL - GENERAL FUND

FOR THE YEAR ENDED JUNE 30, 2018

| | General Fund | | | |
|---|---|---|---|---|
| | Budgeted Amount | | | Variance With Final Budget Positive |
| | Original | Final | Actual | (Negative) |
| OTHER FINANCING SOURCES (USES) | | | | |
| Interagency transfers: | | | | |
| Claims funding | $ 28,750,000 | $ 28,750,000 | $ 13,040,902 | $ (15,709,098) |
| Other, net | | | (59,378) | (59,378) |
| Workers compensation administrative cost reimbursement | | | 1,681,923 | 1,681,923 |
| Prior-year warrants outlawed and cancelled | | | 3,025 | 3,025 |
| TOTAL OTHER FINANCING SOURCES (USES) | 28,750,000 | 28,750,000 | 14,666,472 | (14,083,528) |
| NET CHANGE IN FUND BALANCE | (3,200,720) | 5,106,785 | 16,565,213 | 11,458,428 |
| FUND BALANCE - JULY 1 | 71,862,201 | 71,862,201 | 71,862,201 | |
| FUND BALANCE - JUNE 30 | $ 68,661,481 | $ 76,968,986 | $ 88,427,414 | $ 11,458,428 |

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

STATE INSURANCE DEPARTMENT
STATEMENT OF FIDUCIARY NET POSITION –
FIDUCIARY FUNDS - AGENCY
FOR THE YEAR ENDED JUNE 30, 2018

Exhibit D

| | Total |
|---|---|
| ASSETS | |
| Cash and cash equivalents | $ 5,669,301 |
| Financial assurance instruments | 226,210,347 |
| TOTAL ASSETS | $ 231,879,648 |
| LIABILITIES | |
| Due to general fund | $ 2,570,496 |
| Due to life and health guaranty fund | 2,084,632 |
| Due to insurance companies | 227,224,520 |
| TOTAL LIABILITIES | $ 231,879,648 |

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

NOTE 1: Summary of Significant Accounting Policies

A. Reporting Entity/History

Act 148 of 1959, as amended, established the present Arkansas Insurance Code; the Arkansas Insurance Department, as a department of Arkansas state government; and the Arkansas Insurance Commissioner. The Insurance Department generally regulates all insurance companies and their agents doing business in the State of Arkansas. Its activities include granting or withholding charters, certificates of authority, and licenses; approving policies, proxies, and advertising material; conducting hearings on matters affecting the regulation of the insurance industry; administering and collecting premium taxes due from domestic and foreign insurance companies and all worker's compensation insurance written in the State; receiving and examining, at least annually, reports and financial statements from all insurance companies authorized to do business in the State; and preparing an annual report of the Insurance Commissioner.

Act 809 of 1979 created a Public Employee Workmen's Compensation Claims Section within the State Commerce Department – Insurance Division and provided for the administration and management of the section.

Act 728 of 1987 established the Governmental Bonding Board for the purpose of developing and administering the self-insured Fidelity Bond Program for all public employees. The Board shall have five members as follows: the President of the Association of Arkansas Counties, the President of the Arkansas Municipal League, the Director of the Arkansas Department of Education – General Education Division, the Director of the Department of Finance and Administration, and the Arkansas Insurance Commissioner, who serves as Chair. The presidents of the Association of Arkansas Counties and the Arkansas Municipal League, when attending to official business of the Board, shall be entitled to a per diem equal the rate received by members of the General Assembly for attending joint interim committee meetings and mileage equal to the rate for state employees.

Act 78 of the 2003 Second Extraordinary Session moved the State School Insurance Program from the Department of Education to the State Insurance Department.

Act 684 of 2007 abolished the Arkansas Title Insurance Agents' Licensing Board and transferred all of its powers and duties to the State Insurance Department.

Act 788 of 2017 abolished the State Board of Embalmers and Funeral Directors, the Burial Association Board, and the Arkansas Cemetery Board and transferred all of their powers and duties to the State Board of Embalmers, Funeral Directors, Cemeteries, and Burial Services within the State Insurance Department.

B. Basis of Presentation – Fund Accounting

The accounting system is organized and operated on a fund basis. A *fund* is defined as a fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances and changes therein, which are segregated for purposes of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. The following types of funds, if applicable to this Agency, are recognized in the accompanying financial statements.

Governmental Funds

General Fund – General Fund is the general operating fund and is used to report all financial resources, except those required to be accounted for in another fund.

NOTE 1: Summary of Significant Accounting Policies (Continued)

B. Basis of Presentation – Fund Accounting

Fiduciary Funds

Trust and Agency Funds –Trust and Agency Funds are used to report resources held by the Agency in a trustee capacity or as an agent for individuals, other governmental units, and other funds. These include Pension Trust Funds, Employee Health Trust Funds, Investment Trust Funds, Private-Purpose Trust Funds, and Agency Funds. The specific activity accounted for at this Agency includes the following:

Agency funds account for assets held by the Agency as a custodial agent for insurance companies that are required to have a security deposit on hand in the State, as set out in Ark. Code Ann. § 23-63-205, and for insolvent insurance companies who are in receivership.

C. Basis of Accounting

Basis of accounting refers to when revenues and expenditures or expenses are recognized and reported in the financial statements. Financial statements for governmental funds are presented using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized when they become both measurable and available. "Available" means collectible within the current period or soon enough thereafter to pay current liabilities (i.e., 45 days). Expenditures are generally recognized under the modified accrual basis when the related fund liability is incurred. Revenues from federal grants and federal reimbursements are recognized when all applicable eligibility requirements and the availability criteria of 45 days have been met. The economic resources measurement focus and accrual basis of accounting are used in all Proprietary and Fiduciary Fund financial statements. Under the accrual basis, revenues are recognized when earned, and expenses are recorded when incurred.

D. Cash and Cash Equivalents

Cash and cash equivalents include demand accounts, imprest accounts, cash on hand, cash in State Treasury, all certificates of deposit with maturities at purchase of 90 days or less, and all short-term instruments with maturities at purchase of 90 days or less. All short-term investments are stated at fair value.

E. Deposits and Investments

State Board of Finance Policies

Ark. Code Ann. § 19-4-805 requires that agencies holding monies not deposited in the State Treasury, other than the institutions of higher learning, abide by the recommendations of the State Board of Finance. The State Board of Finance promulgated cash management, collateralization, and investments policies and procedures, effective July 14, 2012, as referenced in the Financial Management Guide issued by the Department of Finance and Administration for use by all state agencies.

The stated goal of state cash management is the protection of principal, while maximizing investment income and minimizing non-interest earning balances. Deposits are to be made within the borders of the State of Arkansas and must qualify for Federal Deposit Insurance Corporation (FDIC) deposit insurance coverage. Policy requires a minimum of four bids to be sought on interest-bearing deposits in order to obtain the highest rate possible.

Policy states that funds are to be in transactional and non-transactional accounts as defined in the Financial Management Guide. Funds in excess of immediate expenditure requirements (excluding minimum balances) should not remain in non-interest bearing accounts.

NOTE 1: Summary of Significant Accounting Policies (Continued)

E. Deposits and Investments (Continued)

State Board of Finance Policies (Continued)

State Board of Finance policy states that cash funds may only be invested in accounts and investments authorized under Ark. Code Ann. §§ 19-3-510, -518. All noncash investments must be held in safekeeping by a bank or financial institution. In addition, all cash funds on deposit with a bank or financial institution that exceed FDIC deposit insurance coverage must be collateralized. Collateral pledged must be held by an unaffiliated third-party custodian in an amount at least equal to 105% of the cash funds on deposit.

Deposits

Deposits are carried at cost and consist of cash in bank, cash in State Treasury, and certificates of deposit totaling $19,221,604, $59,065,089, and $19,540,000, respectively. State Treasury Management Law governs the management of funds held in the State Treasury, and the Treasurer of State is responsible for ensuring these funds are adequately insured and collateralized.

Custodial Credit Risk – Custodial credit risk for deposits is the risk that, in the event of the failure of a depository institution, the Agency will not be able to recover deposits or will not be able to recover collateral securities that are in the possession of an outside party. The Agency has adopted the State Board of Finance Policy requiring the use of depository insurance and collateralization procedures to manage the risk that deposits may not be returned. As of June 30, 2018, none of the Agency's bank balance of $19,320,355 was exposed to custodial credit risk.

F. Interfund Balances and Transfers

Interfund receivables and payables arise from interfund transactions and are recorded by all funds affected in the period in which transactions are executed. Details of interfund transfers are disclosed in the financial statements.

G. Prepaid Expenses

Prepaid expenses generally represent the cost of consumable supplies on hand or unexpired services at year-end. The cost of these items is included with expenditures at the time of purchase. Prepaid expenses, as reported in the general fund financial statements, are also recorded as a nonspendable component of fund balance indicating that they do not constitute "available, spendable financial resources."

H. Deferred Outflows of Resources and Deferred Inflows of Resources

Deferred outflows of resources represent a decrease of net position that applies to future periods. Thus, these items will not be recognized as an outflow of resources (an expense or expenditure) until a future period.

Deferred inflows of resources represent an increase of net position that applies to future periods. These items will not be recognized as an inflow of resources (revenue) until a future period.

I. Fund Equity

Fund Balance

In the financial statements, fund balance is reported in one of five classifications, where applicable, based on the constraints imposed on the use of the resources.

The nonspendable fund balance includes amounts that cannot be spent because they are either (a) not in spendable form (e.g., prepaid items, inventories, long-term amount of loans and notes receivables, etc.) or (b) legally or contractually required to be maintained intact.

NOTE 1: Summary of Significant Accounting Policies (Continued)

I. Fund Equity (Continued)

Fund Balance (Continued)

The spendable portion of fund balance, where applicable, comprises the remaining four classifications: restricted, committed, assigned, and unassigned.

*Restricted fund balance.* This classification reflects constraints imposed on resources either (a) externally by creditors, grantors, contributors, or laws or regulations of other governments or (b) by law through constitutional provisions or enabling legislation.

*Committed fund balance.* These amounts can only be used for specific purposes according to constraints imposed by legislation of the General Assembly, the government's highest level of decision-making authority. Committed amounts cannot be used for any other purpose unless the General Assembly removes or changes the constraint by the same action that imposed the constraint.

*Assigned fund balance.* This classification reflects amounts constrained by the State's "intent" to be used for specific purposes but are neither restricted nor committed. The General Assembly has the authority to assign amounts to be used for specific purposes by legislation or approved methods of financing.

*Unassigned fund balance.* This amount is the residual classification for the general fund.

When more than one spendable classification is available for use, it is the State's policy to use the resources in this order: restricted, committed, assigned, and unassigned.

A summary of the nature and purpose of each of these fund balance classifications as of June 30, 2018, is as follows:

| | Nonspendable | Spendable Fund Balance | | |
|---|---|---|---|---|
| | Fund Balance | Restricted | Committed | Assigned |
| Prepaid expenses | $ 123,314 | | | |
| Program requirements | | $ (7,699) | | |
| Other | | 14,152,194 | $ 67,648,414 | $ 6,699,928 |
| Total | $ 123,314 | $ 14,144,495 | $ 67,648,414 | $ 6,699,928 |

J. Budgetary Data

The State utilizes an annual budgeting process with budget amounts initially derived from the previous fiscal year's funded allocation. In accordance with the appropriations and funding provided by the Legislature, individual state agencies have been charged with the responsibility of administering and managing their programs as authorized by the Legislature. Agencies are also charged with the responsibility of preparing an annual operations plan as a part of the budgetary process for the operation of each of their assigned programs. State law provides for the establishment of a comprehensive financial management system that includes adequate controls over receipts, expenditures, and balances of Agency funds. It is mandated that this system include a modified accrual system, conform with generally accepted governmental accounting principles, and provide a reporting system whereby actual expenditures are compared to expenditures projected in the Agency's annual operation plan.

NOTE 2: Financial Assurance Instruments

Ark. Code Ann. § 23-63-206 requires all insurers authorized to transact business in the State to make and maintain deposits of securities. Ark. Code Ann. § 23-63-903 specifies that these deposits shall consist of certified checks, certificates of deposit, or any combination of securities, the market value of which is readily ascertainable. These funds are held by the Agency as a custodial agent in various commercial banks and amounted to $226,210,347 at June 30, 2018.

Schedule 1

# STATE INSURANCE DEPARTMENT
## SCHEDULE OF SELECTED INFORMATION
## FOR THE FIVE-YEAR PERIOD ENDED JUNE 30, 2018
## (UNAUDITED)

| | For the Year Ended June 30, | | | | |
|---|---|---|---|---|---|
| | 2018 | 2017 | 2016 | 2015 | 2014 |
| **General Fund** | | | | | |
| Total Assets | $ 99,165,642 | $ 80,545,914 | $ 98,850,076 | $ 79,763,344 | $119,436,232 |
| Total Liabilities | 6,463,705 | 4,681,148 | 4,870,615 | 4,823,359 | 5,209,980 |
| Total Deferred Inflows of Resources | 4,274,523 | 4,002,565 | 3,942,991 | 4,015,639 | 3,749,918 |
| Total Fund Equity | 88,427,414 | 71,862,201 | 87,036,470 | 70,924,346 | 110,476,334 |
| Net Revenues | 61,154,362 | 58,578,634 | 60,624,226 | 55,365,285 | 76,201,230 |
| Total Expenditures | 59,255,621 | 56,166,363 | 59,518,918 | 59,712,207 | 78,241,109 |
| Total Other Financing Sources (Uses) | 14,666,472 | (17,586,540) | 15,006,816 | (35,205,066) | 13,503,817 |
| **Aggregate Remaining Fund Information** | | | | | |
| Total Assets | 231,879,648 | 238,816,180 | 256,297,965 | 256,823,642 | 264,394,886 |
| Total Liabilities | 231,879,648 | 238,816,180 | 256,297,965 | 256,823,642 | 264,394,886 |

STATE INSURANCE DEPARTMENT
OTHER GENERAL INFORMATION
JUNE 30, 2018
(UNAUDITED)

A. Capital Assets

Capital assets purchased and in the custody of this Agency were recorded as expenditures at the time of purchase. Assets with costs exceeding $5,000 and an estimated useful life exceeding one year are reported at historical cost, including ancillary costs (such as professional fees and costs, freight costs, preparation or setup costs, and installation costs). Infrastructure or public domain fixed assets (such as roads, bridges, tunnels, curbs and gutters, streets and sidewalks, drainage systems, and lighting systems) are also capitalized. Gifts or contributions are generally recorded in the accounts at acquisition value at the time received. Acquisition value is the market value if the Agency would have purchased the item. In accordance with current accounting principles generally accepted in the United States of America, general capital assets and depreciation are reported in the State's "Government-Wide" financial statements but are not reported in the governmental fund financial statements. Depreciation is reported for proprietary fund capital assets based on a straight-line method, with no salvage value. Estimated useful lives generally assigned are as follows:

| Assets: | Years |
|---|---|
| Equipment | 5-20 |
| Buildings and building improvements | 20-50 |
| Infrastructure | 10-40 |
| Land improvements | 10-100 |
| Intangibles | 4-95 |
| Other capital assets | 10-15 |

Capital assets activity for the year ended June 30, 2018, was as follows:

| | Beginning Balance | Additions | Retirements | Ending Balance |
|---|---|---|---|---|
| Governmental activities: | | | | |
| Equipment | $ 2,591,215 | $ 107,573 | $ 212,220 | $ 2,486,568 |
| Improvements | 44,714 | 2,400 | | 47,114 |
| Construction in progress | 100,000 | 200,000 | | 300,000 |
| Total governmental activities | $ 2,735,929 | $ 309,973 | $ 212,220 | $ 2,833,682 |

B. Pension Plan

Arkansas Public Employees Retirement System (APERS)

Plan Description – The Agency contributes to APERS, a cost-sharing, multiple-employer defined benefit pension plan administered by the APERS Board of Trustees. APERS provides retirement and disability benefits, annual redetermination of benefit adjustments, and survivor benefits to plan members and beneficiaries. The Constitution of Arkansas, Article 5, vests with the General Assembly the legislative power to enact and amend benefit provisions of APERS as published in Chapters 2, 3, and 4 of Title 24 of the Arkansas Code Annotated. APERS issues a publicly available financial report that includes financial statements and required supplementary information. This report may be obtained by writing to Arkansas Public Employees Retirement System, One Union National Plaza, 124 West Capitol, Little Rock, Arkansas, 72201 or by calling 1-501-682-7855.

Funding Policy – Contributory plan members are required to contribute 5% of their annual covered salary. The Agency is required to contribute for all covered state employees at the rate of 14.50% of annual covered payroll. The contribution requirements of plan members are established and may be amended by the Arkansas General Assembly. The contribution requirements of the Agency are established and may be amended by the APERS Board of Trustees. The Agency's contributions to APERS for the years ended June 30, 2018, 2017, and 2016, were $1,215,070, $1,235,238, and $1,275,461, respectively, equal to the required contributions for each year.

C. Postemployment Benefits Other Than Pensions (OPEB)

Arkansas State Employee Health Insurance Plan (Plan)

Plan Description – The Department of Finance and Administration – Employee Benefits Division (DFA-EBD) provides medical and prescription drug benefits for eligible state employees and retirees. Policies for DFA-EBD related to medical and prescription drug plans are established by the State and Public School Life and Health Insurance Board (Board) and may include ad hoc benefit changes or annual cost redeterminations. For the current year, no ad hoc or cost redetermination changes occurred. The Constitution of Arkansas, Article 5, vests the General Assembly with legislative power to enact and amend duties of and benefit provisions of the Board and DFA-EBD, respectively, as published in Subchapter 4, Chapter 5 of Title 21 of the Arkansas Code Annotated. DFA-EBD is included in the State of Arkansas's Comprehensive Annual Financial Report (CAFR), which includes all applicable financial information, notes, and required supplementary information. That report may be obtained by writing to Department of Finance and Administration, 1509 West Seventh Street, Suite 403, Little Rock, Arkansas 72201 or by calling 501-682-1675.

The Agency contributes to the Plan, a single employer defined benefit OPEB plan administered by DFA-EBD, on a monthly basis. The Board establishes medical and prescription drug benefits for three classes of covered individuals: active employees, terminated employees with accumulated benefits, and retires and beneficiaries. The Plan is established on the basis of a pay-as-you-go financing requirement, and no assets are accumulated in a trust, as defined by Governmental Accounting Standards Board (GASB) Statement No. 75. The State's annual OPEB cost for the Plan is based on an actuarially-determined calculated amount made in accordance with GASB Statement No. 75.

Funding Policy – Employer contributions to the Plan are established by Ark. Code Ann. § 21-5-414 and may not exceed $450 per budgeted position. Employees, retirees, and beneficiaries contribute varying amounts based on the type of coverage and inclusion of family members. Benefits for Medicare-eligible retirees are coordinated with Medicare Parts A and B, and the Plan is the secondary payer.

D. Compensated Absences – Employee Leave

Annual leave is earned by all full-time employees. Upon termination, employees are entitled to receive compensation for their unused accrued annual leave up to 30 days. Liabilities for compensated absences are determined at the end of the year based on current salary rates.

Sick leave is earned by all full-time employees and may be accrued up to 120 days. Compensation up to a maximum of $7,500 for unused sick leave is payable to employees upon retirement.

Compensated absences are reported in the State's "Government-Wide" financial statements but are not reported as liabilities or expenditures in the governmental funds. However, the compensated absences payable attributable to this Agency's employee annual and sick leave as of June 30, 2018 and 2017, amounted to $781,788 and $838,546, respectively. The net changes to compensated absences payable during the year ended June 30, 2018, amounted to $(56,758).

E. Taxes and Fees

The Agency collects various taxes and fees that are deposited into the State's general and special revenue funds. The Agency does not disburse these funds, and they are not included in the departmental financial statements. Deposits to the State Treasury of these receipts were as follows:

| Receipts Deposited | Year Ended June 30, 2018 |
|---|---|
| Insurance premium taxes | $ 223,361,620 |
| Agents' license and filing fees | 16,061,684 |
| Total | $ 239,423,304 |