

# Public Education Employees' Health Insurance Fund

(A Component Unit of the State of Alabama)

## FINANCIAL STATEMENTS

For the Fiscal Year Ended September 30, 2018

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## **INDEPENDENT AUDITORS' REPORT**

To the Public Education Employees'  
Health Insurance Board of Control

### **Report on the Financial Statements**

We have audited the accompanying financial statements of the Public Education Employees' Health Insurance Fund (a component unit of the State of Alabama), as of and for the year ended September 30, 2018, and the related notes to the financial statements, which comprise the Public Education Employees' Health Insurance Fund's basic financial statements.

### **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.

### **Auditors' Responsibility**

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. 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 auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### **Opinion**

In our opinion, the financial statements referred to above present fairly, in all material respects, the net position of the Public Education Employees' Health Insurance Fund, as of September 30, 2018, and the changes in net position for the year then ended in accordance with accounting principles generally accepted in the United States of America.

## **Emphasis of Matter**

### *Adoption of New Accounting Pronouncement*

As described in Note 1 and Note 7 to the financial statements, during 2018 the Public Education Employees' Health Insurance Fund adopted Government Accounting Standards Board Statement No. 75, Accounting and Financial Reporting for Benefits Other than Pensions. Our opinion is not modified with respect to this matter.

## **Other Matters**

### *Prior-Year Comparative Information*

The financial statements include partial prior-year comparative information. Such information does not include all of the information required to constitute a presentation in conformity with accounting principles generally accepted in the United States of America. Accordingly, such information should be read in conjunction with the Public Education Employees' Health Insurance Fund's financial statements for the year ended September 30, 2017, from which such partial information was derived. We have previously audited the Public Education Employees' Health Insurance Fund's financial statements and we expressed an unmodified opinion on the respective financial statements in our report dated March 5, 2018. In our opinion, the summarized comparative information presented herein as of and for the year ended September 30, 2017, is consistent, in all material respects, with the audited financial statements from which it has been derived.

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, the schedule of proportionate share of the net pension liability, schedule of proportionate share of the net OPEB liability, the schedules of contributions and schedule of ten-year claims development information be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

*Cary Riggs & Ingram, L.L.C.*

Montgomery, Alabama  
February 15, 2019

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Management's Discussion and Analysis**  
**September 30, 2018**

The Public Education Employees' Health Insurance Fund (PEEHIF) is a health insurance plan for active and retired employees of state and local educational institutions. The contributions and benefit payments related to retirees that are processed through the PEEHIF are segregated from the PEEHIF and reported as part of the Alabama Retired Education Employees' Health Care Trust (Trust). The following discussion provides an overview of the financial position and results of operations for the PEEHIF as of and for the fiscal year ended September 30, 2018. For more detailed information, please refer to the financial statements, including the Notes to the Financial Statements and the Required Supplementary Information.

**Overview of the Financial Statements and Required Supplementary Information**

The financial statements include the Statement of Net Position, the Statement of Revenues, Expenses, and Changes in Fund Net Position, and the Statement of Cash Flows. The Notes to the Financial Statements are considered an integral part of the financial statements and should be read in conjunction with the financial statements. The financial statements are prepared under the accrual basis of accounting using the economic resources measurement focus. Revenues are recognized when earned and expenses are recognized when incurred, regardless of when cash is received or expended. Investments are reported at fair value.

The Statement of Net Position includes the assets, deferred outflows of resources, liabilities, and deferred inflows of resources of the PEEHIF and provides a snapshot of the financial position of the PEEHIF as of the end of the fiscal year. Assets primarily consist of cash, receivables, and short-term investments. Liabilities primarily consist of accounts payable and claims-related payables.

The Statement of Revenues, Expenses, and Changes in Fund Net Position includes the revenues and expenses of the PEEHIF for the fiscal year. Revenues primarily consist of premiums and interest income. Expenses primarily consist of claims.

The Statement of Cash Flows provides information about the cash receipts and payments of the PEEHIF during the fiscal year. The Statement of Cash Flows is divided into three sections – operating, investing, and non-capital financing activities. A reconciliation of operating income to net cash provided by operating activities is also presented. The PEEHIF had no activities related to non-capital or capital financing during the fiscal year. The PEEHIF's Statement of Cash Flows was prepared using the direct method, as required by GASB Statement No. 34. Under the direct method, major classes of receipts and payments are displayed. The net change in cash during the fiscal year plus the cash at the beginning of the fiscal year equals the cash at the end of the fiscal year.

The Notes to the Financial Statements include a description of the PEEHIF, a summary of significant accounting policies, a description of contract administrators and their respective fees, and other disclosures related to credit risks, concentrations of investments, unpaid claims liabilities, employee pension plans, and other postemployment benefits.

The Required Supplementary Information following the Notes to the Financial Statements provides a claims development table illustrating historical trend information on how the PEEHIF's earned revenues and interest income compare to the related costs of claims and other expenses assumed by the PEEHIF as of the end of the fiscal year. It also includes a Schedule of Proportionate Share of the Net Pension Liability and a Schedule of Contributions. Both schedules pertain to PEEHIF employees who participate in the Teachers' Retirement System of Alabama (TRS) pension plan.

With the implementation of GASB 75, the Required Supplementary Information includes new schedules: Schedule of Contributions and Schedule of Proportionate Share of the Net OPEB Liability. Both schedules pertain to employees of PEEHIF who participate in the State Employees' Health Insurance Plan (SEHIP)

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Management's Discussion and Analysis**  
**September 30, 2018**

**Comparative Financial Statements**

**Summary Comparative Statement of Net Position**  
**As of September 30, 2018 and 2017**  
(Amounts in Thousands)

	<u>2018</u>	<u>2017</u>	<u>Variance</u>	<u>% Increase/ (Decrease)</u>
<b><i>Assets and Deferred Outflows of Resources</i></b>				
Cash	\$ 2,121	\$ 4,508	\$ (2,387)	(52.95)
Receivables	8,570	19,104	(10,534)	(55.14)
Deposit with Claims-Paying Agent	3,334	1,559	1,775	113.86
Investments	291,762	192,792	98,970	51.34
Deferred Outflows of Resources	787	874	(87)	(9.95)
<b><i>Total Assets and Deferred Outflows of Resources</i></b>	<b><u>\$ 306,574</u></b>	<b><u>\$ 218,837</u></b>	<b><u>\$ 87,737</u></b>	<b><u>40.09</u></b>
<b><i>Liabilities and Deferred Inflows of Resources</i></b>				
Payables	\$ 37,289	\$ 34,133	\$ 3,156	9.25
Claims Incurred but Not Reported	56,463	54,917	1,546	2.82
Due to Teachers' Retirement System	24,700	-	24,700	100.00
Deferred Inflows of Resources	674	89	585	657.30
Total Liabilities and Deferred Inflows of Resources	119,126	89,139	29,987	33.64
Net Position - Restricted	119,134	67,689	51,445	43.18
Net Position - Unrestricted	68,314	62,009	6,305	10.17
Total Net Position	187,448	129,698	57,750	44.53
<b><i>Total Liabilities, Deferred Inflows of Resources, and Net Position</i></b>	<b><u>\$ 306,574</u></b>	<b><u>\$ 218,837</u></b>	<b><u>\$ 87,737</u></b>	<b><u>40.09</u></b>

**Summary Comparative Statement of Revenues, Expenses, and Changes in Fund Net Position**  
**For the Fiscal Years Ended September 30, 2018 and 2017**  
(Amounts in Thousands)

	<u>2018</u>	<u>2017</u>	<u>Variance</u>	<u>% Increase/ (Decrease)</u>
<b><i>Operating Revenues</i></b>				
Premiums	\$1,011,060	\$1,019,147	\$ (8,087)	(0.79)
Total Operating Revenues	1,011,060	1,019,147	(8,087)	(0.79)
<b><i>Operating Expenses</i></b>				
Claims	927,086	910,527	16,559	1.82
Fees and Assessments	354	445	(91)	(20.45)
Administrative	3,199	3,170	29	0.91
Total Operating Expenses	930,639	914,142	16,497	1.80
Operating Income/(Loss)	80,421	105,005	(24,584)	(23.41)
<b><i>Investment Revenues</i></b>				
Interest Income	4,464	1,416	3,048	215.25
Total Investment Revenues	4,464	1,416	3,048	215.25
Transfers	24,700	-	24,700	100.00
Change in Net Position	60,185	106,421	(46,236)	(43.45)
<b><i>Net Position</i></b>				
Beginning of Year	129,698	23,277	106,421	457.19
Adjustment for Application of GASB 75	(2,435)	-	(2,435)	100.00
End of Year	<b><u>\$ 187,448</u></b>	<b><u>\$ 129,698</u></b>	<b><u>\$ 57,750</u></b>	<b><u>44.53</u></b>

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Management's Discussion and Analysis**  
**September 30, 2018**

**Financial Highlights**

- Investments increased due to investment returns.
- Cash on hand at September 30, 2018, was primarily held for the payment of administrative expenses of the PEEHIF.
- The Alabama Legislature funded PEEHIF at \$800 per active member per month for employers. The prior year funding was \$800.
- Claims expenses remained relatively unchanged due to consistent enrollment and aggressive cost control measures.
- As of September 30, 2018, PEEHIP recorded a \$24.7 million transfer to Teachers' Retirement System in accordance with Act 2018-481 to fund a 2018 retiree lump sum payment. The transfer was made October 1, 2018.
- Interest income increased due to the increase in Investments from 2017 to 2018.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Statement of Net Position**

**September 30, 2018 with comparative amounts shown for 2017**

(Amounts in Thousands)

	<u>2018</u>	<u>2017</u>
<b>Assets</b>		
Current Assets:		
Cash (Note 1)	\$ 2,121	\$ 4,508
Premiums Receivable (Note 1)	2,121	1,144
Prescription Drug Plan Manufacturer Rebates Receivable	6,105	17,821
Interest Receivable	344	139
Deposit with Claims-Paying Agent	3,334	1,559
Total Current Assets	<u>14,025</u>	<u>25,171</u>
Noncurrent Assets:		
Investments, at Fair Value		
Investments, Restricted	119,134	67,689
Investments, Unrestricted	172,628	125,103
Total Investments, at Fair Value (Note 3)	<u>291,762</u>	<u>192,792</u>
Total Assets	<u>305,787</u>	<u>217,963</u>
Deferred Outflows of Resources		
Net Pension Liability	691	874
Net Other Post Employment Benefit (OPEB) Liability	96	-
Total Deferred Outflows of Resources	<u>787</u>	<u>874</u>
Total Assets and Deferred Outflows of Resources	<u>\$ 306,574</u>	<u>\$ 218,837</u>
<b>Liabilities</b>		
Current Liabilities:		
Accounts Payable	\$ 1,212	\$ 361
Due to Other Governments	350	335
Compensated Absences, Current (Note 1)	16	16
Reported Claims Payable (Note 4)	28,696	28,349
Due to Teachers' Retirement System (Note 1)	24,700	-
Claims Incurred but Not Reported (Note 4)	56,463	54,917
Total Current Liabilities	<u>111,437</u>	<u>83,978</u>
Noncurrent Liabilities:		
Compensated Absences (Note 1)	466	430
Net Pension Liability (Note 5)	3,112	3,450
Other Post-employment Benefits	-	1,192
Net OPEB Liability (Note 6)	3,437	-
Total Noncurrent Liabilities	<u>7,015</u>	<u>5,072</u>
Total Liabilities	<u>118,452</u>	<u>89,050</u>
Deferred Inflows of Resources		
Net Pension Liability	336	89
Net OPEB Liability	338	-
Total Deferred Inflows of Resources	<u>674</u>	<u>89</u>
Total Liabilities and Deferred Inflows of Resources	<u>119,126</u>	<u>89,139</u>
<b>Net Position</b>		
<b>Restricted</b>	119,134	67,689
<b>Unrestricted</b>	68,314	62,009
<b>Total Net Position (Note 1)</b>	<u>187,448</u>	<u>129,698</u>
<b>Total Liabilities, Deferred Inflows of Resources, and Net Position</b>	<u>\$ 306,574</u>	<u>\$ 218,837</u>

See accompanying Notes to the Financial Statements.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Statement of Revenues, Expenses and Changes in Fund Net Position**  
**For the Fiscal Year Ended September 30, 2018 with comparative amounts shown for 2017**

(Amounts in Thousands)

	2018	2017
<b><i>Operating Revenues</i></b>		
Premiums		
Unrestricted	\$ 961,046	\$ 951,717
Restricted	50,014	67,430
Total Premiums (Note 1)	1,011,060	1,019,147
 Total Operating Revenues	 1,011,060	 1,019,147
<b><i>Operating Expenses</i></b>		
Claims (Notes 2 and 4)	927,086	910,527
Fees and Assessments	354	445
Administrative	3,199	3,170
	930,639	914,142
 Total Operating Expenses	 930,639	 914,142
 Operating Income	 80,421	 105,005
<b><i>Investment Revenues</i></b>		
Interest Income		
Interest Income - Unrestricted	3,033	1,157
Interest Income - Restricted	1,431	259
Total Interest Income	4,464	1,416
 Total Investment Revenues	 4,464	 1,416
 Transfer to Teachers' Retirement System	 24,700	 -
 Change in Net Position	 60,185	 106,421
<b><i>Net Position</i></b>		
Beginning Net Position	129,698	23,277
Adjustment for Application of GASB 75 (Note 7)	(2,435)	
Beginning of Year - as adjusted	127,263	23,277
Ending Net Position		
Restricted	119,134	67,689
Unrestricted	68,314	62,009
Total Net Position	\$ 187,448	\$ 129,698

See accompanying Notes to the Financial Statements.



**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Statement of Cash Flows**

**For the Fiscal Year Ended September 30, 2018 with comparative amounts shown for 2017**

(Amounts in Thousands)

	<u>2018</u>	<u>2017</u>
<b><i>Cash Flows from Operating Activities</i></b>		
Receipts from Participants	\$ 1,010,083	\$ 1,019,136
Payments to Suppliers	(318)	(883)
Payments to Employees	(1,850)	(1,993)
Claims Paid	(915,252)	(930,287)
Fees and Assessments Paid	(339)	(6,028)
Net Cash Provided by Operating Activities	<u>92,324</u>	<u>79,945</u>
<b><i>Cash Flows from Investing Activities</i></b>		
Interest from Investments	4,259	1,298
Purchases of Investments	(2,708,755)	(3,287,851)
Sales and Maturities of Investments	2,609,785	3,206,883
Net Cash (Used for) Investing Activities	<u>(94,711)</u>	<u>(79,670)</u>
Net (Decrease)/Increase in Cash	(2,387)	275
Cash at Beginning of Year	4,508	4,233
<b><i>Cash at End of Year</i></b>	<u><u>\$ 2,121</u></u>	<u><u>\$ 4,508</u></u>
<b><i>Reconciliation of Operating Income to Net Cash Provided by Operating Activities</i></b>		
Operating Income	\$ 80,421	\$ 105,005
(Increase)/Decrease in Assets:		
Premiums Receivable	(977)	(11)
Rebates Receivable	11,716	(13,056)
Deposit with Claims-Paying Agent	(1,775)	670
Deferred Outflows of Resources	188	(91)
Increase/(Decrease) in Liabilities:		
Accounts Payable	851	(41)
Compensated Absences	36	9
Due to Other Governments	15	(5,583)
Other Post-employment Benefits (OPEB)	-	130
Net Pension Liability	(338)	217
Net OPEB Liability	(291)	-
Reported Claims Payable	347	(11,337)
Claims Incurred but Not Reported	1,546	1,545
Deferred Inflows of Resources	585	71
Net Cash Provided by Operating Activities	<u><u>\$ 92,324</u></u>	<u><u>\$ 77,528</u></u>
<b><i>Noncash Investing Activities</i></b>		
Increase in Interest Receivable	<u><u>\$ 205</u></u>	<u><u>\$ 119</u></u>

See accompanying Notes to the Financial Statements.

# **PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

## **Notes to the Financial Statements**

### **For the Fiscal Year Ended September 30, 2018**

#### **1) Organization and Summary of Significant Accounting Policies**

##### **A. General**

The Public Education Employees' Health Insurance Fund (PEEHIF) was established in 1983 pursuant to the *Code of Alabama 1975, Title 16, Chapter 25A* (Act 83-455 of the Alabama Legislature) to provide a uniform plan of health insurance for active and retired employees of state and local educational institutions which provide instruction at any combination of grades K-14 (collectively, eligible employees), and to provide a method for funding the benefits related to the plan. The four-year universities participate in the plan with respect to their retired employees, and are eligible and may elect to participate in the plan with respect to their active employees. At this time, only two universities have elected to participate in the plan with respect to their active employees. Responsibility for the establishment of the health insurance plan and its general administration and operations is vested in the Public Education Employees' Health Insurance Board (Board). The Board is a corporate body for purposes of management of the health insurance plan. All assets of the PEEHIF are held in trust for the payment of health insurance benefits. The Board has been appointed as the administrator of the PEEHIF. In accordance with the Governmental Accounting Standards Board (GASB), the PEEHIF is considered a component unit of the State of Alabama (State) and is included in the State's Comprehensive Annual Financial Report.

In order to comply with the reporting requirements set by GASB Statement No. 74, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, the contributions and benefit payments related to retirees that are processed through the PEEHIF are segregated from the PEEHIF and reported as part of the Alabama Retired Education Employees' Health Care Trust (Trust).

The Public Education Employees' Health Insurance Plan (PEEHIP) offers a basic hospital medical plan to active members and non-Medicare eligible retirees. Benefits include inpatient hospitalization for a maximum of 365 days without a dollar limit, inpatient rehabilitation, outpatient care, physician services, and prescription drugs.

Active employees and non-Medicare eligible retirees who do not have Medicare eligible dependents can enroll in a Medicare Advantage Prescription Drug Plan (MAPDP) in lieu of the basic hospital medical plan. The MAPDP includes hospital medical benefits, dental benefits, vision benefits, and an extensive formulary. However, participants in the MAPDP are required to receive care from a participating physician in the MAPDP plan.

The PEEHIP offers four optional plans (Hospital Indemnity, Cancer, Dental, and Vision) that may be selected in addition to or in lieu of the basic hospital medical plan or MAPDP. The Hospital Indemnity Plan provides a per-day benefit for hospital confinement, maternity, intensive care, cancer, and convalescent care. The Cancer Plan covers cancer disease only and benefits are provided regardless of other insurance. Coverage includes a per-day benefit for each hospital confinement related to cancer.

The Dental Plan covers diagnostic and preventive services, as well as basic and major dental services. Diagnostic and preventive services include oral examinations, teeth cleaning, x-rays, and emergency office visits. Basic and major services include fillings, general aesthetics, oral surgery not covered under a Group Medical Program, periodontics, endodontics, dentures, bridgework, and crowns. Dental services are subject to a maximum of \$1,250 per year for individual coverage and \$1,000 per person per year for family coverage. The Vision Plan covers annual eye examinations, eye glasses, and contact lens prescriptions.

PEEHIP members may opt to elect the PEEHIP Supplemental Plan for hospital medical coverage in lieu of the PEEHIP Hospital Medical Plan. The PEEHIP Supplemental Plan provides secondary benefits to the member's primary plan provided by another employer. Only active and non-Medicare retiree members and dependents are eligible for the PEEHIP Supplemental Plan. There is no premium required for this plan, and the plan covers most out-of-pocket expenses not covered by the primary plan. The plan cannot be used as a supplement to Medicare, the PEEHIP Hospital Medical Plan, or the State or Local Governmental Plans administered by the State Employees' Insurance Board (SEIB).

# **PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

## **Notes to the Financial Statements**

### **For the Fiscal Year Ended September 30, 2018**

#### **A. General, Continued**

The State Legislature specifies the monthly employer rate that participating school systems must contribute for each active employee. The monthly employer rate for fiscal year 2018 was \$800 per active participant. In accordance with the 2018 budget established by the Alabama Legislature, participating school systems paid the required monthly employer rate of \$800 on behalf of each active employee. Act 2003-473 requires universities who do not participate in the PEEHIP to pay the required monthly rate for each university retiree who participates in the plan. The required monthly employer rate for fiscal year 2018 was \$341 per university retiree. In addition to the employer payments each month, employees are required to pay certain premium amounts. Participants should refer to the PEEHIP member handbook for a more complete description of the PEEHIP's provisions.

#### **B. Basis of Accounting**

The PEEHIF is a proprietary fund that operates under the accrual basis of accounting using the economic resources measurement focus. The accompanying financial statements are prepared in accordance with the requirements of the Governmental Accounting Standards Board (GASB). Under these requirements, PEEHIF is considered component unit of the State of Alabama and is included in the State's Comprehensive Annual Financial Report. Premiums are recognized as revenues when earned, pursuant to plan requirements. Claims and assessments are recognized when due and payable in accordance with the terms of the plans provided. Expenses are recognized when the corresponding liability is incurred, regardless of when the payment is made. Subsequent events were evaluated by management through the date the financial statements were issued.

#### **C. Cash**

Cash consists of deposits held by the State Treasurer in the PEEHIF's name. Deposits are entirely insured by the Federal Deposit Insurance Corporation or protected under the Security for Alabama Funds Enhancement (SAFE) Program. The *Code of Alabama 1975*, as amended, requires all State organizations to participate in the SAFE Program. The SAFE Program is a multiple financial institution collateral pool. The SAFE Program requires all public funds to be deposited in a financial institution designated by the State Treasurer as a qualified public depository. Each qualified public depository is required to pledge collateral in accordance with the rules established by the SAFE Board of Directors. In the event that a qualified public depository defaults or becomes insolvent and the pledged collateral is insufficient to satisfy the claims of public depositors, the *Code of Alabama 1975, Section 41-14A-9(3)* authorizes the State Treasurer to make assessments against the other qualified public depositories in the pool so that there will be no loss of public funds. Cash designated for the payment of administrative expenses at September 30, 2018, was \$2,121,202.

#### **D. Expense Fund**

The Board designated \$2,400,000 of premiums received during the fiscal year ended September 30, 2018, to be used for the payment of administrative expenses. The administrative costs incurred directly for the operation of the PEEHIF are paid from the expense fund. Indirect costs are not allocated to the PEEHIF by the TRS.

#### **E. Investments**

The Board of Control of the PEEHIF has the responsibility and authority to invest and reinvest available funds, through the Secretary-Treasurer and Investment Committee, in bonds, mortgage-backed securities, mortgages, common and preferred stock, and other investment vehicles with the care, skill, prudence, and diligence under the circumstances then prevailing that a prudent person acting in a like capacity and familiar with such matters would use. All plan assets are carried at fair value except commercial paper and money market funds which are reported at cost, which approximates fair value. U.S. agency obligations and corporate bonds are reported at the last reported sales price.

# PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND

## Notes to the Financial Statements

### For the Fiscal Year Ended September 30, 2018

#### F. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts on the financial statements. Actual results may differ from these estimates.

#### G. Premiums

Premium revenue is recognized in the period in which the related coverage is provided. Premium payments that have not been received by the end of a coverage period are recorded as a receivable.

#### H. Fees and Assessments

The Patient Protection and Affordable Care Act (ACA) levies certain fees and assessments upon group health insurance plans. During fiscal year 2018, the PEEHIF was subject to the Patient-Centered Outcomes Research Institute Fee (PCORI Fee). The fee is calculated based on the number of covered lives under the plan. The expense for the PCORI fee is included in Fees and Assessments in the Statement of Revenues, Expenses, and Changes in Fund Net Position. The total fees due but not yet paid by the PEEHIF as of September 30, 2018, were recorded as Due to Other Governments in the Statement of Net Position and amounted to \$350,255.

#### I. Unpaid Claims Liabilities

Claims liabilities are established based on the actual cost of claims reported but not settled and estimates of claims that have been incurred but not reported. Actual claims costs ultimately incurred may vary from estimated claims liabilities should the nature and frequency of actual claims vary from historical claims experience on which the estimates are based. Adjustments to claims liabilities are charged or credited to expense in the periods in which they are made.

Unpaid claims liabilities are material estimates that are particularly susceptible to changes in the near term. Management believes the liabilities established for unpaid claims at September 30, 2018, are adequate to cover the ultimate net cost of claims, but the liabilities are necessarily based on estimates and accordingly, the amount ultimately paid will be more or less than such estimates.

#### J. Compensated Absences

The PEEHIF records a liability and a charge to expense for all compensated absences attributable to services already rendered that are not contingent on specific events outside the control of the employer or employee.

#### K. Net Position

The net position of the insurance and expense fund is allocated for the payment of insurance benefits and administrative expenses, respectively. As of September 30, 2018, the PEEHIF's unrestricted and restricted net position was allocated as follows:

	Net Position		
	(Amounts in Thousands)		
	Insurance Fund	Expense Fund	Total
Restricted	\$ 119,134	\$ -	\$ 119,134
Unrestricted	74,161	(5,847)	68,314
<b>Total Net Position</b>	<b>\$ 193,295</b>	<b>\$ (5,847)</b>	<b>\$ 187,448</b>

# **PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

## **Notes to the Financial Statements**

### **For the Fiscal Year Ended September 30, 2018**

#### **L. Comparative Statements**

The basic financial statements include the prior fiscal year Statement of Net Position, the Statement of Revenues, Expenses, and Changes in Fund Net Position, and the Statement of Cash Flows for comparative purposes only. Prior fiscal year note disclosures are not included. Therefore, the prior fiscal year basic financial statement presentation does not meet the minimum level of detail required for a presentation in conformity with generally accepted accounting principles. Accordingly, the prior fiscal year statements should be read in conjunction with the PEEHIP's prior fiscal year financial report from which the prior fiscal year statements were derived.

#### **M. Deferred Outflows & Inflows of Resources**

In addition to assets, the Statement of Net Position reports a separate section for deferred outflows of resources. This separate financial statement element, *Deferred Outflows of Resources*, represents a consumption of net position that applies to future periods and will not be recognized as an outflow of resources until that period. Deferred Outflows of Resources related to the employer's Net Pension Liability and Net OPEB Liability are reported as deferred outflows of resources.

In addition to liabilities, the Statement of Net Position reports a separate section for *Deferred Inflows of Resources*. This separate financial statement element represents an acquisition of net position that applies to future periods and will not be recognized until then. Deferred Inflows of Resources relate to Net Pension Liability and Net OPEB Liability.

#### **N. Commitments and Contingencies**

The president of the Alabama Education Association filed a lawsuit against members of the PEEHIP Board, claiming that an educational session on April 27, 2016 violated the provisions of the Alabama Open Meetings Act. On August 20, 2017, the trial court entered an order granting summary judgment in favor of the plaintiff. PEEHIP filed an appeal, and the Alabama Supreme Court heard oral arguments in the matter. The parties are currently awaiting the Supreme Court's decision. At September 30, 2018, \$119.1 million related to the amounts at issue in the litigation are held in a separate interest-bearing account in accordance with a September 23, 2016 order of the trial court.

#### **O. Due to Teachers' Retirement System**

Act 481 of the Legislature of 2018 authorized a one-time transfer from the Public Education Employees' Health Insurance Plan (PEEHIP) for \$24,700,000 (dollar amount not in thousands) to fund a one-time lump-sum bonus payment to retirees of the TRS during June 2018. The transfer was made October 1, 2018.

#### **P. New Accounting Pronouncements**

GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits other than Pensions* was implemented in fiscal year 2018. The statement objective is to improve accounting and financial reporting by state and local governments for post-employment benefits other than pensions (other postemployment benefits or OPEB). GASB No. 75 recognizes the net liability of OPEB, comprehensive measure of OPEB expense, and additional note disclosures and required supplementary information (RSI).

PEEHIP also implemented GASB Statement No. 85, Omnibus 2017, in fiscal year 2018. This statement addresses a variety of issues including issues related to blending component units, goodwill, fair value measurement and application, and postemployment benefits (pensions and other postemployment benefits) identified during implementation and application of certain GASB Statements.

# **PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

## **Notes to the Financial Statements**

### **For the Fiscal Year Ended September 30, 2018**

#### **2) Contract Administrators**

Blue Cross and Blue Shield of Alabama (BCBS), under contract with the Board, administered medical claims incurred in accordance with the plan. The BCBS administrative fee was \$15.35 per month per contract. The \$15.35 per member per month fee was charged to the PEEHIF.

BCBS, under contract with the Board, administered participant requests for reimbursement covered under flexible employee benefit plans. BCBS charged the PEEHIF an administrative fee of \$3.95 per month per contract.

MedImpact, under contract with the Board, administered claims under the prescription drug plan. The MedImpact administrative fee was \$1.05 per eligible member per month (PMPM). The \$1.05 PMPM fee was charged to the PEEHIF.

Southland Benefit Solutions, LLC (Southland), under contract with the Board, administered claims under the optional plans. The processing fees per month per contract were \$0.80 for Group Hospital Indemnity, \$0.66 for Group Cancer, \$1.12 for Group Vision, and \$1.49 for Group Dental.

Effective January 1, 2017, United Healthcare (UHC), under contract with the Board, provided a fully insured Medicare Advantage (MA) and Medicare Advantage Prescription Drug Plan (MAPDP) to Medicare eligible retirees and their eligible dependent.

VIVA Health, under contract with the Board, provided a fully insured Hospital Medical plan option for actives and non-Medicare eligible retirees who do not have Medicare eligible dependents.

#### **3) Investments**

##### **A. Investment Risks**

Investments are subject to certain types of risks, including interest rate risk, custodial credit risk, credit quality risk, and foreign currency risk. The following describes those risks and the PEEHIF's policies regarding those risks:

*Interest Rate Risk* – The fair value of fixed-maturity investments fluctuates in response to changes in market interest rates. The PEEHIF's investments are short term fixed rate commercial paper or fixed dollar value money market funds.

*Custodial Credit Risk* – Custodial credit risk is the risk that an entity will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party if the counterparty fails. The PEEHIF's safekeeping agent holds all investments of the PEEHIF in the PEEHIF's name.

*Credit Quality* – Nationally recognized statistical rating organizations provide ratings of debt securities' quality based on a variety of factors, such as the financial condition of the issuers, which provide investors with some idea of the issuer's ability to meet its obligations. Short-term investments may consist of commercial paper rated at least A-2 and/or P-2, repurchase agreements, short-term U.S. securities, and other money market investments.

*Concentration of Credit Risk* – The PEEHIF's investments at the fiscal year-end were all held in short-term investments, as they will be used to cover cash flow requirements in the short-term.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**A. Investment Risks, Continued**

The following table provides information concerning the fair value and the interest rate risk of the PEEHIF's investments as of September 30, 2018:

<b>INVESTMENTS</b>						
<b>Maturity in Years at Fair Value</b>						
<b>(Amounts in Thousands)</b>						
<b>Type of Investment</b>	<b>Less Than 1</b>	<b>1-5</b>	<b>6-10</b>	<b>More Than 10</b>	<b>Total Fair Value</b>	<b>Cost</b>
Money Market Funds	\$ 231,703	\$ -	\$ -	\$ -	\$ 231,703	\$ 231,703
Commercial Paper	60,059				\$ 60,059	\$ 60,059
<b>Total Investments</b>	<b>\$ 291,762</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ -</b>	<b>\$ 291,762</b>	<b>\$ 291,762</b>

The following table provides information concerning the credit risk of the PEEHIF's investments as of September 30, 2018:

<b>RATINGS OF FIXED MATURITIES</b>			
<b>(Amounts in Thousands)</b>			
<b>Moody's Ratings</b>	<b>Cost</b>	<b>Fair Value</b>	<b>Fair Value as a Percentage of Total</b>
P-1	\$ 9,995	\$ 9,995	3.43
P-2	50,064	50,064	17.16
NR	231,703	231,703	79.41
<b>Total Fixed Maturity</b>	<b>\$ 291,762</b>	<b>\$ 291,762</b>	<b>100.00</b>

  

<b>Standard &amp; Poor's Ratings</b>	<b>Cost</b>	<b>Fair Value</b>	<b>Fair Value as a Percentage of Total</b>
A-2	\$ 60,059	\$ 60,059	20.59
NR	231,703	231,703	79.41
<b>Total Fixed Maturity</b>	<b>\$ 291,762</b>	<b>\$ 291,762</b>	<b>100.00</b>

**B. Fair Value Measurement**

The PEEHIF categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy prioritizes the inputs to valuation used to measure the fair value of the asset, giving the highest priority to quoted prices in an active market for identical assets (Level 1 measurements) and the lowest priority to unobservable inputs (Level 3 measurements). The inputs to the three levels of the fair value hierarchy are described as follows:

- Level 1: Quoted (unadjusted) prices in an active market for identical assets or liabilities.
- Level 2: Significant other inputs which are observable either directly or indirectly, including quoted prices for similar assets or liabilities, quoted prices for identical or similar assets or liabilities in a less active market, or other market-corroborated inputs.
- Level 3: Valuations derived from valuation techniques using significant unobservable inputs for the asset or liabilities.

The categorization of investments within the hierarchy is based upon pricing transparency of the instrument and should not be perceived as the particular investment's risk.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Notes to the Financial Statements**  
**For the Fiscal Year Ended September 30, 2018**

**B. Fair Value Measurement, Continued**

Investments in equity securities classified as Level 1 are valued using quoted prices in an active market for those securities.

Investments in securities classified as Level 2 are valued using non-proprietary information that is readily available to market participants from multiple independent sources, which are known to be actively involved in the market. Pricing inputs may include market quotation, yields, maturities, call features, and ratings.

Investments in private equity, debt, and direct investments in real estate are classified as Level 3 due to lack of observable pricing inputs and are valued using annual appraisals based on a combination of market data and projected cash flows.

The following table provides information as of September 30, 2018, concerning fair value measurement:

	9/30/2018	Fair Value Measurements Using		
		(Amounts in Thousands)		
		Quoted Prices in Active Markets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
<i>Domestic Fixed Maturity</i>				
Money Market Funds	\$ 231,703	\$ -	\$ 231,703	\$ -
Commercial Paper	60,059	-	60,059	-
Total Domestic Fixed Maturity	291,762	-	291,762	-
<b>Total Investments</b>	<b>291,762</b>	<b>-</b>	<b>291,762</b>	<b>-</b>
<b>Total Fair Value</b>	<b>\$ 291,762</b>	<b>\$ -</b>	<b>\$ 291,762</b>	<b>\$ -</b>

**C. Concentration of Investments**

As of September 30, 2018, the PEEHIF did not own any investment securities that constituted more than 5% of the total fair value of investments.



**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**4) Unpaid Claims Liabilities**

As discussed in Note 1, the PEEHIF establishes a liability for both reported and unreported insured claims. This liability includes provisions for the future payment of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities for the PEEHIF during fiscal year 2018:

**UNPAID CLAIMS LIABILITIES**

(Amounts in Thousands)

Unpaid Claims and Claim Adjustment Expenses at Beginning of Year	<u>\$ 83,266</u>
Incurred Claims and Claim Adjustment Expenses:	
Provision for Insured Events of the Current Year	932,360
Decrease in Provision for Insured Events of Prior Years	<u>(5,274)</u>
Total Incurred Claims and Claim Adjustment Expenses	<u>\$ 927,086</u>
Payments:	
Claims and Claim Adjustment Expenses Attributable to Insured Events of the Current Year	\$ 847,201
Claims and Claim Adjustment Expenses Attributable to Insured Events of the Prior Years	<u>77,992</u>
Total Payments	<u>925,193</u>
Total Unpaid Claims and Claim Adjustment Expenses at the End of the Year	<u><u>\$ 85,159</u></u>

**5) Net Pension Liability**

The employees of the PEEHIF participate in the Teachers' Retirement System of Alabama (TRS). The TRS, a cost-sharing multiple-employer public employee retirement plan, was established as of September 15, 1939, pursuant to the *Code of Alabama 1975, Title 16, Chapter 25* (Act 419 of the Legislature of 1939) for the purpose of providing retirement allowances and other specified benefits for qualified persons employed by State-supported educational institutions. The responsibility for the general administration and operation of the TRS is vested in its Board of Control. The TRS Board of Control consists of 15 trustees as follows:

- 1) The State Superintendent of Education, ex officio.
- 2) The State Treasurer, ex officio.
- 3) The State Director of Finance, ex officio.
- 4) Twelve members of TRS who are elected by members from the same category of TRS for a term of three years as follows:
  - a. Teacher Place #1.
  - b. Teacher Place #2.
  - c. Teacher Place #3.
  - d. Educational Support Personnel Place #1.
  - e. Educational Support Personnel Place #2.
  - f. Retired Place #1.
  - g. Retired Place #2.
  - h. Superintendents' Place.
  - i. Principals' Place.
  - j. Postsecondary Place.
  - k. Higher Education Place #1.
  - l. Higher Education Place #2.

The Plan is administered by RSA and issues a Comprehensive Annual Financial Report each year. It is available at [www.rsa-al.gov](http://www.rsa-al.gov).

# **PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

## **Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

### **5) Net Pension Liability, Continued**

State law establishes retirement benefits as well as death and disability benefits and any ad hoc increase in postretirement benefits for the TRS. Benefits for TRS members vest after 10 years of creditable service. TRS members who retire after age 60 with 10 years or more of creditable service or with 25 years of service (regardless of age) are entitled to an annual retirement benefit, payable monthly for life. Service and disability retirement benefits are based on a guaranteed minimum or a formula method, with the member receiving payment under the method that yields the highest monthly benefit. Under the formula method, members of the TRS are allowed 2.0125% of their average final compensation (highest 3 of the last 10 years) for each year of service.

Act 377 of the Legislature of 2012 established a new tier of benefits (Tier 2) for members hired on or after January 1, 2013. Tier 2 TRS members are eligible for retirement after age 62 with 10 years or more of creditable service and are entitled to an annual retirement benefit, payable monthly for life. Service and disability retirement benefits are based on a guaranteed minimum or a formula method, with the member receiving payment under the method that yields the highest monthly benefit. Under the formula method, Tier 2 members of the TRS are allowed 1.65% of their average final compensation (highest 5 of the last 10 years) for each year of service. Members are eligible for disability retirement if they have 10 years of credible service, are currently in-service, and determined by the RSA Medical Board to be permanently incapacitated from further performance of duty. Preretirement death benefits are calculated and paid to the beneficiary based on the member's age, service credit, employment status, and eligibility for retirement.

Covered members of the TRS contributed 5% of earnable compensation to the TRS as required by statute until September 30, 2011. From October 1, 2011, to September 30, 2012, covered members of the TRS were required by statute to contribute 7.25% of earnable compensation. Effective October 1, 2012, covered members of the TRS are required by statute to contribute 7.50% of earnable compensation. Certified law enforcement, correctional officers, and firefighters of the TRS contributed 6% of earnable compensation as required by statute until September 30, 2011. From October 1, 2011, to September 30, 2012, certified law enforcement, correctional officers, and firefighters of the TRS were required by statute to contribute 8.25% of earnable compensation.

Effective October 1, 2012, certified law enforcement, correctional officers, and firefighters of the TRS are required by statute to contribute 8.50% of earnable compensation.

Tier 2 covered members of the TRS contribute 6% of earnable compensation to the TRS as required by statute. Tier 2 certified law enforcement, correctional officers, and firefighters of the TRS are required by statute to contribute 7% of earnable compensation.

Participating employers' contractually required contribution rate for the fiscal year ended September 30, 2018, was 12.24% of annual pay for Tier 1 members and 11.01% of annual pay for Tier 2 members. These required contribution rates are a percent of annual payroll, actuarially determined as an amount that, when combined with member contributions, is expected to finance the costs of benefits earned by members during the year, with an additional amount to finance any unfunded accrued liability. Total TRS employer contributions to the pension plan from the PEEHIF were \$276,266 for the fiscal year ended September 30, 2018.

At September 30, 2018, the PEEHIF reported a liability of \$3,112,000 for its proportionate share of the collective net pension liability. The collective net pension liability was measured as of September 30, 2017, and the total pension liability used to calculate the net pension liability was determined by an actuarial valuation as of September 30, 2016. The PEEHIF's proportion of the collective net pension liability was based on its share of contributions to the pension plan relative to the total employer contributions of all participating TRS employers. At September 30, 2017, the PEEHIF's proportion was 0.031667%, which was a decrease of 0.000201% from its proportion measured as of September 30, 2016.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**5) Net Pension Liability, Continued**

For the year ended September 30, 2018, the PEEHIF recognized pension expense of \$367,565. At September 30, 2018, the PEEHIF reported deferred outflows of resources and deferred inflows of resources related to pensions from the following sources:

	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Differences between Expected and Actual Experience	\$ -	\$ 133,000
Changes of Assumptions	186,000	-
Net Difference between Projected and Actual Earnings on Pension Plan Investments	-	186,000
Changes in Proportion and Differences between Employer Contributions and Proportionate Share of Contributions	229,000	17,000
Employer Contributions Subsequent to the Measurement Date	276,266	-
<b>Total</b>	<b><u>\$ 691,266</u></b>	<b><u>\$ 336,000</u></b>

The PEEHIF will recognize \$276,266 of reported deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date as a reduction of net pension liability in the fiscal year ended September 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to pensions will be recognized in pension expense as follows:

**Fiscal Year Ended  
September 30:**

2019	\$ 67,000
2020	\$ 113,000
2021	\$ (39,000)
2022	\$ (59,000)
2023	\$ (3,000)
Thereafter	\$ -

The total pension liability was determined by an actuarial valuation as of September 30, 2016, using the following actuarial assumptions, applied to all periods included in the measurement:

Inflation	2.75%
Projected Salary Increases	3.25% - 5.00%
Investment Rate of Return*	7.75%

\*Net of pension plan investment expense

The actuarial assumptions used in the actuarial valuation as of September 30, 2016, were based on the results of an investigation of the economic and demographic experience for the TRS based upon participant data as of September 30, 2015. The Teachers' Retirement System Board of Control accepted and approved these changes in September 2016, which became effective at the beginning of fiscal year 2016.

Mortality rates for TRS were based on the RP-2000 White Collar Mortality Table projected to 2020 using Scale BB with an adjustment of 115% for males and 112% for females age 78 and older. The disability mortality rates were based on the RP-2000 Disabled Mortality Table projected to 2020 using Scale BB with an adjustment of 105% for males and 120% for females.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**5) Net Pension Liability, Continued**

The long-term expected rate of return on pension plan investments was determined using a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target asset allocation and best estimates of geometric real rates of return for each major asset class are as follows:

	<b>Target Allocation</b>	<b>Long-Term Expected Rate of Return*</b>
Fixed Income	17.00%	4.40%
U.S. Large Stocks	32.00%	8.00%
U.S. Mid Stocks	9.00%	10.00%
U.S. Small Stocks	4.00%	11.00%
International Developed Market Stocks	12.00%	9.50%
International Emerging Market Stocks	3.00%	11.00%
Alternatives	10.00%	10.10%
Real Estate	10.00%	7.50%
Cash	3.00%	1.50%
<b>Total</b>	<b><u>100.00%</u></b>	

\*Includes assumed rate of inflation of 2.50%.

The discount rate used to measure the total pension liability was 7.75%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rate and that the employer contributions will be made at rates equal to the difference between actuarially determined contribution rates and the member rate. Based on those assumptions, components of the pension plan's fiduciary net position were projected to be available to make all projected future benefit payments of current plan members. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the total pension liability.

The following table presents the PEEHIF's proportionate share of the net pension liability calculated using the discount rate of 7.75%, as well as what its proportionate share of the net pension liability would be if it were calculated using a discount rate that is 1-percentage point lower (6.75%) or 1-percentage-point higher (8.75%) than the current rate:

	<b>1% Decrease (6.75%)</b>	<b>Current Discount Rate (7.75%)</b>	<b>1% Increase (8.75%)</b>
PEEHIF's Proportionate Share of Collective Net Pension Liability	\$4,293,000	\$ 3,112,000	\$2,114,000

Detailed information about the pension plan's fiduciary net position is available in the separately issued RSA Comprehensive Annual Financial Report for the fiscal year ended September 30, 2018. The supporting actuarial information is included in the GASB Statement No. 67 Report for the TRS prepared as of September 30, 2017. The auditor's report dated August 20, 2018, on the total pension liability, total deferred outflows of resources, total deferred inflows of resources, and total pension expense for the sum of all participating entities as of September 30, 2017, along with supporting schedules is also available. The additional financial and actuarial information is available at [www.rsa-al.gov](http://www.rsa-al.gov).

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**6) Net OPEB Liability**

The Alabama Retired State Employees' Health Care Trust (SEIF Retired - Trust) financial statements are prepared by using the economic resources measurement focus and accrual basis of accounting. This includes for purposes of measuring the net OPEB liability, deferred outflows of resources and deferred inflows of resources related to OPEB, and OPEB expense, information about the fiduciary net position of the SEIF Retired - Trust and additions to/deductions from its fiduciary net position. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions are recognized when due pursuant to plan requirements. Benefits are recognized when due and payable in accordance with the terms of the plan. Subsequent events were evaluated by management through the date the financial statements were issued.

The SEIF - Retired Trust is a single employer defined benefit health care plan, also known as other postemployment benefits (OPEB) trust, established in 2007 under the provisions of the Alabama Retiree Health Care Funding Act of 2007 (2007-16) as an irrevocable trust fund. Constitutional amendment 798 provides further legal authority to the SEIF - Retired Trust as an irrevocable trust fund. Active and retiree health insurance benefits are paid through the State Employees' Insurance Board (SEIB) pursuant to Act 833 of the Legislature of 1965. The assets of the SEIF - Retired Trust may not be used for any purpose other than to acquire permitted investments, pay administrative expenses, and provide postemployment health care benefits to or for retired employees and their dependents in accordance with the terms of the plan. Plan assets of SEIF - Retired Trust are legally protected from creditors. The legislature has no authority or power to appropriate the assets of the SEIF - Retired Trust. Responsibility for the general administration and operations of the SEIF - Retired Trust is vested in its trustees who consist of the State Employee's Insurance Board members. In accordance with GASB, the SEIF Retired - Trust is considered a component unit of the State of Alabama (State) and is included in the State's Comprehensive Annual Financial Report.

The SEIF plan (the Plan) provides basic medical coverage for up to 365 days of care during each hospital confinement, outpatient care, physicians' benefits, radiation therapy, and major medical benefits with no lifetime maximum. A group dental contract provides basic dental maintenance coverage with a maximum benefit amount of \$1,500 during each year for each eligible participant who elects coverage.

At September 30, 2017, the following employees were covered by the benefit terms:

Active Members	32,263
Inactive Members	<u>24,405</u>
Total	<u>56,668</u>

The Plan provides that the employers contribute monthly for the medical and dental insurance of participating employees. Coverage is also available to dependents of employees with their medical premiums typically being paid by the employee. Employee and dependent premium amounts are determined annually and are set at a rate necessary to provide sufficient funds to pay all claims and reasonable expenses of administering the plans.

At September 30, 2018, the PEEHIP reported a liability of \$3,437,196 for its proportionate share of the Net OPEB Liability. The Net OPEB Liability was measured as of September 30, 2017, and the Total OPEB Liability used to calculate the Net OPEB Liability was determined by an actuarial valuation as of September 30, 2016. The PEEHIP's proportion of the Net OPEB Liability was based on a projection of the PEEHIP's long-term share of contributions to the OPEB plan relative to the projected contributions of all participating employers, actuarially determined. At September 30, 2017, the PEEHIP's proportion was 0.010865999%, which was a decrease of 0.00007602% from its proportion measured as of September 30, 2016.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Notes to the Financial Statements**  
**For the Fiscal Year Ended September 30, 2018**

**6) Net OPEB Liability, Continued**

For the year ended September 30, 2018, the PEEHIP recognized OPEB expense of \$147,743. At September 30, 2018, the PEEHIP reported deferred outflows of resources and deferred inflows of resources related to OPEB from the following sources:

	<b>Deferred Outflows of Resources</b>	<b>Deferred Inflows of Resources</b>
Differences between Expected & Actual Experience	\$ -	\$ -
Changes of Assumptions	-	330,334
Net Difference between Projected & Actual		
Earnings on OPEB Plan Investments	-	5,746
Changes in Proportion & Differences between Employer		
Contributions & Proportionate Share of Contributions	-	2,122
Employer Contributions Subsequent to the Measurement Date	96,136	-
<b>Total</b>	<b>\$ 96,136</b>	<b>\$ 338,202</b>

The PEEHIP will recognize \$96,136 of reported deferred outflows of resources related to OPEB resulting from contributions subsequent to the measurement date as a reduction of Net OPEB Liability in the fiscal year ended September 30, 2019. Other amounts reported as deferred outflows of resources and deferred inflows of resources related to OPEB will be recognized in OPEB expense as follows:

<b>Fiscal Year Ended</b>	
<b>September 30:</b>	
2019	\$(77,513)
2020	\$(77,513)
2021	\$(77,513)
2022	\$(77,513)
2023	\$(28,151)
Thereafter	\$ -

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**6) Net OPEB Liability, Continued**

The Total Net OPEB Liability was determined by an actuarial valuation as of September 30, 2016, using the following actuarial assumptions, applied to all periods included in the measurement:

<b>Inflation</b>	2.75%
<b>Salary Increases*</b>	5.00-3.25% for State and Local Employees 4.50% for State Police 3.50-3.25% for Judges
<b>Long-Term Investment Rate of Return**</b>	7.50%
<b>Municipal Bond Index Rate at Measurement Date</b>	3.57%
<b>Municipal Bond Index Rate at Prior Measurement Date</b>	2.93%
<b>Projected Year for Fiduciary Net Position to be Depleted</b>	2021
<b>Single Equivalent Interest Rate at Measurement Date</b>	3.60%
<b>Single Equivalent Interest Rate at Prior Measurement Date</b>	2.96%
<b>Healthcare Cost Trend Rate</b>	
Pre-Medicare Eligible	7.75%
Medicare Eligible	5.00%
Ultimate Trend Rate	
Pre-Medicare Eligible	5.00%
Medicare Eligible	5.00%
Year of Ultimate Trend Rate	2021

\*Includes 3.00% wage inflation.

\*\*Compounded annually, net of investment expense, and includes inflation.

The rates of mortality for the period after service retirement are according to the sex distinct RP-2000 Blue Collar Mortality Table Projected with Scale BB to 2020 with an adjustment of 125% at all ages for males and 120% for females at ages on and after age 78. The rates of mortality for the period after disability retirement are according to the sex distinct RP-2000 Disabled Retiree Mortality Table Projected with Scale BB to 2020 with an adjustment of 130% at all ages for females.

The decremental assumptions and methods used in the valuation were selected based on the actuarial experience study prepared as of September 30, 2015, submitted to and adopted by the Teachers' Retirement System of Alabama.

The remaining actuarial assumptions (e.g., initial per capita costs, health care cost trends, rate of plan participation, rates of plan election, etc.) used in the September 30, 2016 valuation were based on a review of recent plan experience done concurrently with the September 30, 2016 valuation.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**6) Net OPEB Liability, Continued**

The long-term expected rate of return on OPEB plan investments was determined using a log-normal distribution analysis in which best-estimate ranges of expected future real rates of return (expected returns, net of OPEB plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. The target asset allocation and best estimates of geometric real rates of return for each major asset class are as follows:

	<u>Target Allocation</u>	<u>Long-Term Expected Rate of Return*</u>
Fixed Income	28.20%	4.40%
U.S.Domestic Stocks	55.20%	8.70%
International Developed Market Stocks	10.80%	9.80%
Cash	5.80%	1.50%
<b>Total</b>	<b><u>100.00%</u></b>	

\*Includes assumed rate of inflation of 2.50%.

The discount rate (also known as the Single Equivalent Interest Rate (SEIR), as described by GASB 74) used to measure the total OPEB liability at September 30, 2017 was 3.60%. The discount rate used to measure the total OPEB liability at the prior measurement date was 2.96%. The projection of cash flows used to determine the discount rate assumed that plan contributions will be made based on the average of the last five years of current contribution rates, indexed with inflation. The discount rate determination will use a municipal bond rate to the extent the trust is projected to run out of money before all benefits are paid. The rate used, if necessary, for this purpose is the monthly average of the Bond Buyers General Obligation 20-year Municipal Bond Index Rate (formerly published monthly by the Board of Governors of the Federal Reserve System). Projected future benefit payments for all current plan members were projected through 2115.

The following table presents the PEEHIP's proportionate shares of the Net OPEB liability of the Trust calculated using the current healthcare trend rate, as well as what the net OPEB liability would be if calculated using one percentage point lower or one percentage point higher than the current rate:

<b>1% Decrease (6.75% decreasing to 4% for pre-Medicare and 4% for Medicare Eligible)</b>	<b>Current Healthcare Trend Rate (7.75% decreasing to 5% for pre-Medicare and 5% for Medicare Eligible)</b>	<b>1% Increase (8.75% decreasing to 6% for pre-Medicare and 6% for Medicare Eligible)</b>
\$ 2,844,105	\$ 3,437,196	\$ 4,206,124

The following table presents the proportionate share of the Net OPEB liability for PEEHIP calculated using the discount rate of 3.60%, as well as what the net OPEB liability would be if calculated using one percentage point lower or one percentage point higher than the current rate:

<b>1% Decrease (2.60%)</b>	<b>Current Discount Rate (3.60%)</b>	<b>1% Increase (4.60%)</b>
\$ 4,100,154	\$ 3,437,196	\$ 2,911,791



**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**

**Notes to the Financial Statements**

**For the Fiscal Year Ended September 30, 2018**

**7) Change in Accounting Principle**

Net Position as of October 1, 2017, has been restated as follows for the implementation of GASB Statement No. 75, which replaces GASB Statement No. 45 and GASB Technical Bulletin 2006-1:

Net Position as previously reported at September 30, 2017	\$ 129,698,307
Prior Period Adjustment:	
Prior Year OPEB under GASB No. 45	1,192,203
October 1, 2017 Net OPEB Liability under GASB No. 75	(3,728,480)
Deferred Outflows:	
October 1, 2017 Contributions Subsequent to Measurement Date under GASB No. 75*	100,826
Total Prior Period Adjustment	<u>(2,435,451)</u>
<b>Net Position as Restated, October 1, 2017</b>	<b>Total <u><u>\$ 127,262,856</u></u></b>

\*Measurement date as of September 30, 2016

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Required Supplementary Information**  
**For the Fiscal Year Ended September 30, 2018**

**Ten-Year Claims Development Information**  
(Amounts in Thousands)

The following table illustrates how the PEEHIF's earned revenue and interest income compare to the related costs of claims and other expenses assumed by the PEEHIF as of the end of each of the past ten fiscal years. The lines of the table are defined as follows: (1) This line shows the total earned contribution and investment revenues for each fiscal year. (2) This line shows each fiscal year's other operating costs of the PEEHIF including overhead and claims expense not allocable to individual claims. (3) This line shows the PEEHIF's incurred claims and allocated claim adjustment expenses (both paid and accrued) as originally reported at the end of the first year in which the event that triggered coverage under the contract occurred (called policy year). (4) This line shows the cumulative amounts paid as of the end of successive years for each policy year. (5) This line shows how the incurred claims for each policy year increased or decreased as of the end of successive years. The annual re-estimated amount results from new information received on known claims, the re-evaluation of existing information on known claims as well as the emergence of previously unknown claims. (6) This line compares the latest re-estimated incurred claims amount to the amount originally established (line 3) and shows whether this latest estimate of claims cost is greater or less than originally thought. As data for each policy year matures, the correlation between original estimates and re-estimated amounts commonly is used to evaluate the accuracy of estimated incurred claims currently recognized.

	<b>Fiscal and Policy Year Ended</b>									
	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>	<b>2014</b>	<b>2013</b>	<b>2012</b>	<b>2011</b>	<b>2010</b>	<b>2009</b>
1) Net Earned Required Contribution & Investment Revenue	\$1,015,524	\$1,020,563	\$875,811	\$881,117	\$742,212	\$743,021	\$743,002	\$ 884,416	\$764,313	\$806,691
2) Unallocated Expenses	3,199	3,170	3,010	2,419	3,465	3,203	2,779	2,587	3,160	2,566
3) Estimated Incurred Claims & Expense at End of Policy Year	932,359	915,736	898,706	874,208	795,286	776,256	741,836	750,966	790,024	775,205
4) Paid (Cumulative) As Of:										
End of Policy Year	846,476	832,470	808,066	795,591	720,923	713,057	677,334	678,546	713,231	696,658
One Year Later			893,497	868,922	792,118	776,240	739,640	749,114	790,009	772,397
5) Reestimated Incurred Claims & Expense:										
End of Policy Year	932,359	915,736	898,706	874,208	795,286	776,256	741,836	750,966	790,024	775,205
One Year Later		910,462	893,497	868,922	792,118	776,240	739,640	749,114	790,009	772,397
6) Decrease in Estimated Incurred Claims & Expenses at End of Policy Year		(5,274)	(5,209)	(5,286)	(3,168)	(16)	(2,196)	(1,852)	(15)	(2,808)

**Note: 2007 was the first year that retirees were segregated from the active employees. As a result, 2007 includes the amounts only attributable to the active employees. This schedule is presented prospectively.**

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Required Supplementary Information**  
**For the Fiscal Year Ended September 30, 2018**

The following schedules pertain to PEEHIF employees who participate in the TRS pension plan.

**SCHEDULE OF PROPORTIONATE SHARE OF THE NET PENSION LIABILITY**

<b>Measurement Date</b>	<b>Fiscal Year</b>	<b>Proportion of the Net Pension Liability</b>	<b>Proportionate Share of the Net Pension Liability</b>	<b>Covered Payroll</b>	<b>Proportionate Share of the Net Pension Liability as a Percentage of Covered Payroll</b>	<b>Plan Fiduciary Net Position as a Percentage of the Total Pension Liability</b>
9/30/2017	9/30/2018	0.03%	\$ 3,112,000	\$2,176,417	142.99%	71.50%
9/30/2016	9/30/2017	0.03%	\$ 3,450,000	\$2,164,159	159.42%	67.93%
9/30/2015	9/30/2016	0.03%	\$ 3,233,000	\$2,079,345	155.48%	67.51%
9/30/2014	9/30/2015	0.03%	\$ 2,468,000	\$ 1,869,207	132.03%	71.01%

Schedule is intended to show information for 10 years.

Additional years will be displayed as they become available.

**SCHEDULE OF PENSIONS CONTRIBUTIONS**  
**For the Fiscal Years Ended September 30**

	<b>2018</b>	<b>2017</b>	<b>2016</b>	<b>2015</b>
Contractually Required Contribution	\$ 276,266	\$ 250,565	\$ 237,968	\$ 223,000
Contributions in relation to the Contractually Required Contribution	(276,266)	(250,565)	(237,968)	(223,000)
Contribution Deficiency/(Excess)	\$ -	\$ -	\$ -	\$ -
Covered Payroll	\$2,373,337	\$2,176,417	\$2,164,159	\$2,079,345
Contributions as a Percentage of Covered Payroll	11.64%	11.51%	11.00%	10.72%

Schedule is intended to show information for 10 years.

Additional years will be displayed as they become available.

*Changes to Benefit Terms*

- TRS's member contribution rates increased from 5% (6% for certified law enforcement, correctional officers, and firefighters) of earnable compensation to 7.25% (8.25%) of earnable compensation effective October 1, 2011, and to 7.50% (8.50%) of earnable compensation effective October 1, 2012.
- TRS members hired on or after January 1, 2013, are covered under a new benefit structure. TRS's member contribution rate is 6% (7% for certified law enforcement, correctional officers, and firefighters) of earnable compensation.

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Required Supplementary Information**  
**For the Fiscal Year Ended September 30, 2018**

*Changes to Assumptions*

In 2016, rates of withdrawal, retirement, disability, mortality, spouse coverage, and tobacco usage were adjusted to more closely reflect actual experience. In 2016, economic assumptions and the assumed rates of salary increase were adjusted to more closely reflect actual and anticipated experience. In 2016 and later, the expectation of retired life mortality was changed to the RP-2000 White Collar Mortality Table projected to 2020 using scale BB and adjusted 115% for all ages for males and 112% for ages 78 and over for females. The rates of disabled mortality were based on the RP-2000 Disabled Mortality Table projected to 2020 using scale BB and adjusted 105% for males and 120% for females.

The following schedules pertain to employees of PEEHIP who participate in the State Employees' Health Insurance Plan (SEHIP) which is administered by the State Employees' Insurance Board (SEIB).

**SCHEDULE OF PROPORTIONATE SHARE OF THE NET OPEB LIABILITY**  
**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE PLAN**

Measurement Date	Fiscal Year Ended	Proportion of the Net OPEB Liability (%)	Proportionate Share of the Net OPEB Liability	Covered Payroll	Proportionate Share of the Net OPEB Liability as a Percentage of Covered Payroll	Plan Fiduciary Net Position as a Percentage of the Total OPEB Liability
9/30/2017	9/30/2018	0.11	\$ 3,437,196	\$ 2,373,337	144.83	5.05

**SCHEDULE OF OPEB CONTRIBUTIONS**  
**For the Fiscal Years Ended September 30**

	<b>2018</b>
Contractually Required Contribution	\$ 96,136
Contributions in relation to the Contractually Required Contribution	(96,136)
Contribution Deficiency/(Excess)	<u>\$ -</u>
Covered Payroll	\$ 2,373,337
Contributions as a Percentage of Covered Payroll	4.05%

*Changes to Benefit Terms*

Effective January 1, 2017, Medicare eligible medical and prescription drug benefits are provided through a Medicare Advantage Prescription Drug Plan (MAPDP).

**PUBLIC EDUCATION EMPLOYEES' HEALTH INSURANCE FUND**  
**Required Supplementary Information**  
**For the Fiscal Year Ended September 30, 2018**

*Changes in Actuarial Assumptions*

In 2016, rates of withdrawal, retirement, disability, and mortality were adjusted to more closely reflect actual experience. In 2016, economic assumptions and the assumed rates of salary increase were adjusted to more closely reflect actual and anticipated experience

*Actuarial Assumptions*

The actuarially determined contribution rates in the schedule of employer contributions are calculated as of September 30, 2016, two years prior to the end of the fiscal year in which contributions are reported. The following actuarial methods and assumptions were used to determine the recent contribution rate reported in that schedule.

<b>Actuarial Cost Method</b>	Projected Unit Credit
<b>Amortization Method</b>	Level Percent of Pay, Open
<b>Remaining Amortization Period</b>	30 years
<b>Asset Valuation Method</b>	Market Value of Assets
<b>Inflation</b>	3.00%
<b>Healthcare Cost Trend Rate</b>	
<b>Pre-Medicare Eligible</b>	7.50%
<b>Medicare Eligible</b>	5.75%
<b>Ultimate Trend Rate</b>	
<b>Pre-Medicare Eligible</b>	5.00%
<b>Medicare Eligible</b>	5.00%
<b>Year of Ultimate Trend Rate</b>	2019
<b>Investment Rate of Return*</b>	5.00%

\* Includes 3.00% wage inflation