

**Teacher Group Insurance Fund**

**For the Year Ended  
June 30, 1997**

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STATE OF TENNESSEE  
**COMPTROLLER OF THE TREASURY**

State Capitol  
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William R. Snodgrass  
Comptroller

August 10, 1998

The Honorable Don Sundquist, Governor  
and

Members of the General Assembly  
State Capitol  
Nashville, Tennessee 37243

and

The Honorable John Ferguson, Chairman  
Local Education Insurance Committee  
State Capitol  
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the Teacher Group Insurance Fund for the year ended June 30, 1997. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance disclosed certain deficiencies, which are detailed in the Observations and Comments section of this report. The Department of Finance and Administration's management has responded to the audit findings. The Division of State Audit will follow up the audit to examine the application of the procedures instituted because of the audit findings.

Very truly yours,

W.R. Snodgrass  
Comptroller of the Treasury

WRS/rm  
98/045

State of Tennessee

# Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit  
**Teacher Group Insurance Fund**  
For the Year Ended June 30, 1997

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## AUDIT OBJECTIVES

The objectives of the audit were to consider the fund's internal control over financial reporting; to determine compliance with certain provisions of laws, regulations, and contracts; to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

## AUDIT FINDINGS

The audit report contains no findings; however, two findings regarding weak computer controls over the Tennessee Insurance System (TIS) were included in the 1997 audit report on the Department of Finance and Administration. The department maintains on TIS participant information such as coverage type and status, eligible dependents, premiums due, and payment history for the Teacher Group Insurance Fund.

## OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

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"Audit Highlights" is a summary of the audit report. To obtain the complete audit report which contains all findings, recommendations, and management comments, please contact

Comptroller of the Treasury, Division of State Audit  
1500 James K. Polk Building, Nashville, TN 37243-0264  
(615) 741-3697

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**Audit Report  
Teacher Group Insurance Fund  
For the Year Ended June 30, 1997**

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# **Teacher Group Insurance Fund For the Year Ended June 30, 1997**

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## **INTRODUCTION**

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### **POST-AUDIT AUTHORITY**

This is a report on the financial and compliance audit of the Teacher Group Insurance Fund. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

### **LEGISLATIVE HISTORY**

The Local Education Insurance Committee was created in 1986 by an act of the General Assembly, codified as Title 8, Chapter 27, Section 301, *Tennessee Code Annotated*. The purpose of the committee is to provide access to health insurance coverage to teachers in political subdivisions of the State of Tennessee.

### **ORGANIZATION**

The Local Education Insurance Committee oversees the administration of the Teacher Group Insurance Fund. The committee is composed of the Governor, who may designate the Commissioner of Education to attend in his place as a full voting member, a representative of local school boards to be selected by the Tennessee School Boards Association, the State Treasurer, the Commissioner of Commerce and Insurance, the Comptroller of the Treasury, the Commissioner of Finance and Administration, and three teachers elected to represent the three grand divisions under the procedures contained in Title 8, Chapter 34, Section 302, *Tennessee Code Annotated*.

The Department of Finance and Administration, Division of Insurance Administration, is responsible for processing all payments and cash receipts of the fund through the state’s accounting system.

The contractor, Blue Cross and Blue Shield of Tennessee, Inc., processes all participant claims, makes all claim payments, provides access to a preferred provider organization, and carries out utilization management function.

An organization chart for the fund's administration is on the following page.

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## AUDIT SCOPE

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The audit was limited to the period July 1, 1996, through June 30, 1997, and was conducted in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Financial statements are presented for the year ended June 30, 1997, and for comparative purposes, the year ended June 30, 1996. The Teacher Group Insurance Fund forms an integral part of the state government and as such has been included as an enterprise fund in the *Tennessee Comprehensive Annual Financial Report*.

The audit covered fund 56 of the State of Tennessee Accounting and Reporting System.

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## OBJECTIVES OF THE AUDIT

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The objectives of the audit were

1. to consider the fund's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements;
2. to determine compliance with certain provisions of laws, regulations, and contracts;
3. to determine the fairness of the presentation of the financial statements; and
4. to recommend appropriate actions to correct any deficiencies.

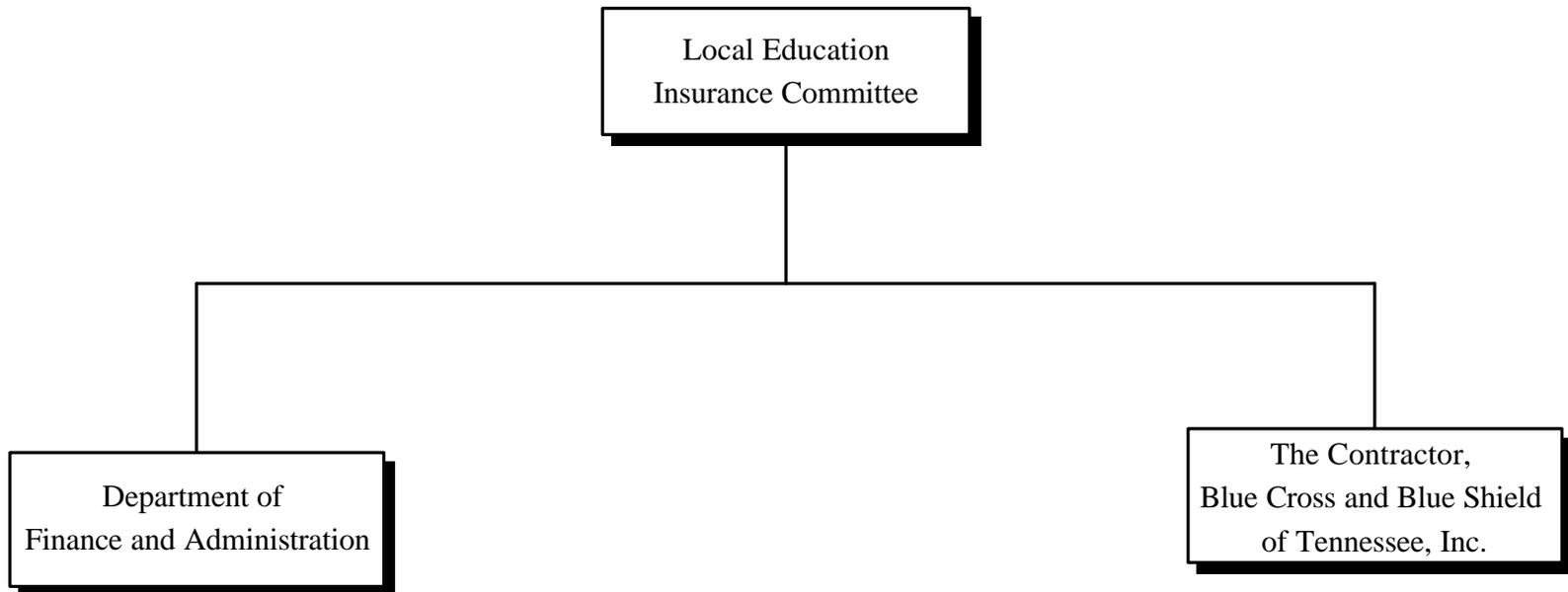
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## PRIOR AUDIT FINDINGS

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There were no findings in the prior audit report; however, the report did refer to a finding in the 1996 Department of Finance and Administration audit report concerning weak controls over the Tennessee Insurance System. This finding has not been resolved and is repeated in the 1997 Department of Finance and Administration audit report.

**TEACHER GROUP INSURANCE FUND  
ADMINISTRATION  
ORGANIZATION CHART**



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## OBSERVATIONS AND COMMENTS

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The Division of Insurance Administration maintains participant information such as coverage type and status, eligible dependents, employment status, premiums due, and payment history for the Teacher Group Insurance Fund on the Tennessee Insurance System (TIS). Two findings regarding computer controls over TIS were included in the 1997 audit report on the Department of Finance and Administration.

1. The Tennessee Insurance System has not been designed, implemented, and maintained in a manner which allows it to function efficiently and effectively. As a result, the system is not producing the desired results and changes are being made directly to the TIS database through the Application Development Facility (ADF). Because these changes are not made to the insurance accounting on the State of Tennessee Accounting and Reporting System (STARS), TIS and STARS do not reconcile. Management concurred with this finding and stated that the department has restructured to focus resources on implementing corrective action.
2. Too many employees have access to security maintenance screens, and security authorization forms identifying approved access to the system were not maintained. Management concurred with this finding, stating that they have taken corrective action.

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## RESULTS OF THE AUDIT

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### AUDIT CONCLUSIONS

#### Internal Control

As part of the audit of the Teacher Group Insurance Fund's financial statements for the year ended June 30, 1997, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Reportable conditions are detailed in the Observations and Comments Section of the report. Consideration of internal control disclosed no material weaknesses.

#### Compliance

The results of our audit tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered an unqualified opinion on the financial statements of the Teacher Group Insurance Fund.



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**Report on Compliance and on Internal Control Over Financial Reporting  
Based on an Audit of Financial Statements  
Performed in Accordance With *Government Auditing Standards***

December 17, 1997

The Honorable W. R. Snodgrass  
Comptroller of the Treasury  
State Capitol  
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have audited the financial statements of the Teacher Group Insurance Fund, as of and for the year ended June 30, 1997, and have issued our report thereon dated December 17, 1997. We conducted our audit in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

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

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the fund's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing

The Honorable W. R. Snodgrass  
December 17, 1997  
Page Two

our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the fund's ability to record, process, summarize, and report financial data consistent with management's assertions in the financial statements.

The following reportable conditions were noted:

- The Tennessee Insurance System (TIS) has significant problems which have caused TIS and the State of Tennessee Accounting and Reporting System not to reconcile.
- Controls over security for the Tennessee Insurance System should be improved.

These conditions are described in the Observations and Comments section of this report.

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe none of the reportable conditions described above are material weaknesses.

We also noted other matters involving the internal control over financial reporting that we have reported to the fund's management in a separate letter.

This report is intended for the information of the General Assembly of the State of Tennessee and management. However, this report is a matter of public record, and its distribution is not limited.

Sincerely,



Arthur A. Hayes, Jr., CPA, Director  
Division of State Audit

AAH/rm



**STATE OF TENNESSEE  
COMPTROLLER OF THE TREASURY  
DEPARTMENT OF AUDIT  
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**Independent Auditor's Report**

December 17, 1997

The Honorable W. R. Snodgrass  
Comptroller of the Treasury  
State Capitol  
Nashville, Tennessee 37243

Dear Mr. Snodgrass:

We have audited the accompanying balance sheets of the Teacher Group Insurance Fund, as of June 30, 1997, and June 30, 1996, and the related statements of revenues, expenses, and changes in retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the fund's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

We conducted our audits in accordance with generally accepted auditing standards and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Teacher Group Insurance Fund, as of June 30, 1997, and June 30, 1996, and the results of its operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

The Honorable W. R. Snodgrass  
December 17, 1997  
Page Two

In accordance with *Government Auditing Standards*, we have also issued our report dated December 17, 1997, on our consideration of the fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grants.

Sincerely,

A handwritten signature in black ink that reads "Arthur A. Hayes, Jr." with a stylized flourish at the end.

Arthur A. Hayes, Jr., CPA, Director  
Division of State Audit

AAH/rm

TEACHER GROUP INSURANCE FUND  
COMPARTIVE BALANCE SHEETS  
JUNE 30, 1997, AND JUNE 30, 1996

(Expressed in Thousands)

	<u>June 30,1997</u>	<u>June 30,1996</u>
<u>ASSETS</u>		
Current assets:		
Cash (Notes 1 and 2)	\$ 18,855	\$ 26,386
Accounts receivable	<u>1,371</u>	<u>1,157</u>
 Total assets	 \$ <u><u>20,226</u></u>	 \$ <u><u>27,543</u></u>
 <u>LIABILITIES AND EQUITY</u>		
Liabilities:		
Current liabilities:		
Warrants payable	\$ 3,444	\$ 1,795
Accounts payable and accruals	15,114	14,424
Deferred revenue	<u>229</u>	<u>214</u>
 Total liabilities	 <u>18,787</u>	 <u>16,433</u>
Equity:		
Retained earnings, unreserved	<u>1,439</u>	<u>11,110</u>
 Total equity	 <u>1,439</u>	 <u>11,110</u>
 Total liabilities and equity	 \$ <u><u>20,226</u></u>	 \$ <u><u>27,543</u></u>

The Notes to the Financial Statements are an integral part of this statement.

TEACHER GROUP INSURANCE FUND  
 COMPARATIVE STATEMENTS OF REVENUES, EXPENSES, AND  
 CHANGES IN RETAINED EARNINGS  
 FOR THE YEARS ENDED JUNE 30, 1997, AND JUNE 30, 1996

(Expressed in Thousands)

	<u>Year Ended June 30, 1997</u>	<u>Year Ended June 30, 1996</u>
<u>OPERATING REVENUES</u>		
Premiums	\$ <u>94,056</u>	\$ <u>81,773</u>
Total operating revenues	<u>94,056</u>	<u>81,773</u>
<u>OPERATING EXPENSES</u>		
Contractual services	3,017	2,072
Rentals and insurance	15,236	5,624
Benefits	85,852	77,606
Other	<u>751</u>	<u>1,650</u>
Total operating expenses	<u>104,856</u>	<u>86,952</u>
Operating loss	<u>(10,800)</u>	<u>(5,179)</u>
<u>NONOPERATING REVENUES</u>		
Interest income	<u>1,129</u>	<u>1,567</u>
Net loss	<u>(9,671)</u>	<u>(3,612)</u>
Retained earnings, July 1	<u>11,110</u>	<u>14,722</u>
Retained earnings, June 30	<u>\$ <u>1,439</u></u>	<u>\$ <u>11,110</u></u>

The Notes to the Financial Statements are an integral part of this statement.

TEACHER GROUP INSURANCE FUND  
COMPARATIVE STATEMENTS OF CASH FLOWS  
FOR THE YEARS ENDED JUNE 30, 1997, AND JUNE 30, 1996

(Expressed in Thousands)

	<u>June 30, 1997</u>	<u>June 30, 1996</u>
Cash flows from operating activities:		
Operating loss	\$ <u>(10,800)</u>	\$ <u>(5,179)</u>
Adjustments to reconcile operating (loss) to net cash provided by operating activities:		
Changes in assets and liabilities:		
Increase in accounts receivable	(214)	(219)
Increase (decrease) in warrants payable	1,649	(132)
Increase in accounts payable	690	1,323
Increase (decrease) in deferred revenue	<u>15</u>	<u>(38)</u>
 Total adjustments	 <u>2,140</u>	 <u>934</u>
 Net cash used for operating activities	 <u>(8,660)</u>	 <u>(4,245)</u>
 Cash flows from investing activities:		
Interest received	<u>1,129</u>	<u>1,567</u>
 Net cash provided by investing activities	 <u>1,129</u>	 <u>1,567</u>
 Net decrease in cash	 (7,531)	 (2,678)
Cash, July 1	<u>26,386</u>	<u>29,064</u>
 Cash, June 30	 <u>\$ 18,855</u>	 <u>\$ 26,386</u>

The Notes to the Financial Statements are an integral part of this statement.

**Teacher Group Insurance Fund**  
**Notes to the Financial Statements**  
**June 30, 1997, and June 30, 1996**

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**NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**A. Reporting Entity**

The Teacher Group Insurance Fund is used to account for revenues received and claims paid on behalf of teachers in political subdivisions of the state who have elected coverage under a group medical plan similar to that offered to state employees. The fund has been included as an enterprise fund in the *Tennessee Comprehensive Annual Financial Report*.

**B. Basis of Presentation**

The accompany financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The Teacher Group Insurance Fund follows all applicable GASB pronouncements as well as applicable private-sector pronouncements issued on or before November 30, 1989.

**C. Measurement Focus and Basis of Accounting**

The accompany financial statements have been prepared using the accrual basis of accounting and the flow of economic resources measurement focus. Under this basis, revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred.

**D. Cash**

Cash is defined as cash on hand, demand deposits such as the pooled investment fund, and investments with three months or less to maturity when purchased.

**NOTE 2. DEPOSITS**

The Teacher Group Insurance Fund had \$18,854,583 in the State Treasurer's pooled investment fund at June 30, 1997, and \$26,385,730 at June 30, 1996.

**Teacher Group Insurance Fund**  
**Notes to the Financial Statements (Cont.)**  
**June 30, 1997, and June 30, 1996**

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The pooled investment fund administered by the State Treasurer is authorized by statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The current resolution of that board gives the Treasurer approval to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, various U.S. Treasury and agency obligations, limited money market mutual funds, and obligations of the State of Tennessee pursuant to *Tennessee Code Annotated*, Section 9-4-602 (b). The pooled investment fund is also authorized to enter into securities lending agreements in which U.S. government securities may be loaned to brokers for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The pool's custodial credit risk is presented in the *Tennessee Comprehensive Annual Financial Report* for the year ended June 30, 1997.

**NOTE 3. RISK MANAGEMENT**

The Teacher Group Insurance Fund, a public entity risk pool, was established in January 1986 to provide a program of health insurance coverage for the teachers in the political subdivisions of the state. In accordance with *Tennessee Code Annotated*, Section 8-27-302, all local education agencies are eligible to participate. Fund members at June 30, 1997, included 106 local education agencies, two cooperatives with 29,842 teachers and support staff, and 1,448 retirees insured in the basic plan or a health maintenance organization. The state does not retain any risk for losses by this fund.

The Teacher Group Insurance Fund assumes responsibility for determining plan benefits and eligibility, establishing premiums sufficient to fund plan obligations, recording and reporting financial transactions accurately, reporting enrollment to vendors, processing claims submitted for services provided to plan participants, communicating with plan participants, and complying with appropriate state and federal laws and regulations. Plan participants are required to pay premiums on time, file claims for services received, report changes in eligibility of themselves or their dependents, and ensure that only eligible expenses are paid by the plan. Individuals who cancel coverage may be required to demonstrate insurability to rejoin the plan. Employers must wait 24 months before rejoining the plan if the employer elects to withdraw from the plan. In the case of the individuals or groups rejoining the plan, a preexisting condition exclusion currently applies.

**Teacher Group Insurance Fund**  
**Notes to the Financial Statements (Cont.)**  
**June 30, 1997, and June 30, 1996**

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The Teacher Group Insurance Fund establishes claims liabilities based on estimates of the ultimate cost of claims that have been reported but not settled and of claims that have been incurred but not reported. Teachers and providers have 13 months to file medical claims. The process used to compute claims liabilities does not necessarily result in an exact amount. Claims liabilities are recomputed periodically using actuarial and statistical techniques to produce current estimates, which are 16.5 percent of the prior 12 months' claims. Adjustments to claims liabilities are charged or credited to expense in the period in which they are made. The Teacher Group Insurance Fund does not consider investment income in determining if a premium deficiency exists.

As discussed above, the Teacher Group Insurance Fund establishes a liability for both reported and unreported insured events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represents changes in those aggregate liabilities during the past two years (expressed in thousands):

	<u>1997</u>	<u>1996</u>
Unpaid claims at beginning of year	\$ 14,001	\$ 13,099
Incurred claims, provision for insured events of the current year	<u>86,086</u>	<u>78,678</u>
Total incurred claims expenses	100,087	91,777
Payments	<u>85,070</u>	<u>77,776</u>
Total unpaid claims at end of year	\$ <u>15,017</u>	\$ <u>14,001</u>

STATE OF TENNESSEE  
TEACHER GROUP INSURANCE FUND  
REQUIRED SUPPLEMENTARY INFORMATION  
TEN-YEAR CLAIMS DEVELOPMENT INFORMATION

(Expressed in Thousands)

The table below illustrates how the Teacher Group Insurance Fund's earned revenues and investment income compare to related costs of loss and other expenses assumed by the Teacher Group Insurance Fund as of the end of each of the last ten years. The rows of the table are defined as follows: (1) This line shows the total of each fiscal year's earned contribution revenues and investment revenues. (2) This line shows each fiscal year's other operating costs of the fund, including overhead. (3) This line shows the fund'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. (4) This section shows the cumulative amounts paid as of the end of successive years for each fiscal year; these amounts are unavailable. (5) This section shows how each fiscal year's incurred claims increased or decreased as of the end of successive years, these amounts are unavailable for prior years. This annual reestimation results from new information received on known claims, reevaluation of existing information on known claims, as well as emergence of new claims not previously known. (6) This line compares the latest reestimated 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 individual fiscal years mature, the correlation between original estimates and reestimated amounts is commonly used to evaluate the accuracy of incurred claims currently recognized in less mature fiscal years. The columns of the table show data for successive fiscal years.

	Fiscal Year Ended June 30									
	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>
(1) Net earned required contribution and investment revenues	\$17,889	\$26,855	\$35,939	\$43,308	\$51,804	\$63,291	\$75,715	\$79,410	\$83,340	\$95,185
(2) Unallocated expenses	507	579	730	931	991	1,234	2,224	1,794	3,722	3,768
(3) Estimated incurred claims and expenses, end of fiscal year	18,797	28,362	39,038	45,439	51,605	58,521	69,157	73,741	78,678	86,086
(4) Paid (cumulative) as of:										
End of fiscal year	*	*	*	*	*	*	*	*	*	*
One year later	*	*	*	*	*	*	*	*	*	
Two years later	*	*	*	*	*	*	*	*		
Three years later	*	*	*	*	*	*	*			
Four years later	*	*	*	*	*	*				
Five years later	*	*	*	*	*					
Six years later	*	*	*	*						
Seven years later	*	*	*							
Eight years later	*	*								
Nine years later	*									

(continued on next page)

Fiscal Year Ended June 30 (Cont.)

	<u>1988</u>	<u>1989</u>	<u>1990</u>	<u>1991</u>	<u>1992</u>	<u>1993</u>	<u>1994</u>	<u>1995</u>	<u>1996</u>	<u>1997</u>
(5) Reestimated incurred claims and expenses:										
End of fiscal year	*	*	*	45,439	51,605	58,521	69,157	73,741	78,678	86,086
One year later	*	*	*	*	*	*	*	*	*	*
Two years later	*	*	*	*	*	*	*	*	*	*
Three years later	*	*	*	*	*	*	*	*	*	*
Four years later	*	*	*	*	*	*	*	*	*	*
Five years later	*	*	*	*	*	*	*	*	*	*
Six years later	*	*	*	*	*	*	*	*	*	*
Seven years later	*	*	*	*	*	*	*	*	*	*
Eight years later	*	*	*	*	*	*	*	*	*	*
Nine years later	*	*	*	*	*	*	*	*	*	*
(6) Increase (decrease) in estimated incurred claims and expense from end of fiscal year	*	*	*	*	*	*	*	*	*	*

\* Data not available