



**STATE OF NEW JERSEY
INDIVIDUAL HEALTH COVERAGE PROGRAM**

Financial Statements

June 30, 2010

With Independent Auditors' Report

**State of New Jersey
Individual Health Coverage Program
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June 30, 2010**

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Independent Auditors' Report

To the Board of Directors,
State of New Jersey Individual Health Coverage Program

We have audited the accompanying statement of net assets of the State of New Jersey Individual Health Coverage Program (the "Program"), which includes the General Fund and the Agency Fund, as of June 30, 2010, and the related statement of changes in net assets, and changes in assets and liabilities-loss assessment (Agency) fund for the year then ended. These financial statements are the responsibility of the Program's management. 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 of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Program's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides 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 Program as of June 30, 2010, and the changes in its net assets and the changes in its assets and liabilities-loss assessment (Agency) fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

The management's discussion and analysis as listed in the table of contents is not a required part of the basic financial statements but is supplemental information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation. However, we did not audit the information and express no opinion on it.

WithumSmith+Brown, PC

November 17, 2010

**State of New Jersey
Individual Health Coverage Program
Management's Discussion and Analysis
June 30, 2010**

The following narrative provides an overview and analysis concerning the New Jersey Individual Health Coverage Program's ("Program") financial performance of its activities for the fiscal year ended June 30, 2010.

General Information

In fiscal year 2010 the Program assessed for the 2007/2008 loss assessment and the fiscal year 2010 and 2011 administrative assessment. Only one carrier reported losses for the 2007/2008 calculation period in the amount of \$438,389. The administrative assessment was based on the budget for fiscal years ending June 30, 2010 and 2011 in the amount of \$329,300 and \$331,700, respectively.

The administrative audit for the fiscal year ended June 30, 2009 was completed.

Financial Highlights

The Program's assets totaled \$30,603,954, a decrease of \$581,799 from the prior fiscal year due primarily to a decrease in cash. Cash decreased by \$525,326 due to payment of loss reimbursements to a carrier for losses for the 2001/2002, 2003/2004 and 2005/2006 calculation periods and payment of operating expenditures, offset by return of funds advanced toward losses, cash received for the 2007/2008 loss and 2010/2011 administrative assessments and interest earned on the funds held in Treasury.

Total other liabilities increased \$272,456 due primarily to collection of funds for the 2011 fiscal year budgeted expenditures of \$331,700 which is recorded as deferred income.

Restricted cash and restricted net assets increased by \$724,370. The accounts relate to monies received from a carrier refunding the Board for cash advances and assessment credits made against the reported net reimbursable losses. The funds are in a separate interest bearing account held in Treasury and have earned interest of \$14,575 in this fiscal year.

Overview of the Financial Statements

The Program has a General Fund and an Agency Fund. The General Fund uses the cash received from assessments to pay for operating expenditures. The fund is reported using the accrual basis of accounting. The Agency Fund is used to record the liability due to the carriers who incurred net paid losses.

The Program has no capital assets.

There is no balance for Unrestricted Net Assets for revenues are equal to actual expenditures. The difference in an assessment billed to the carriers and the revenue is recorded as a receivable from or payable to the members. In fiscal year 2010, carriers were billed the budgeted amount for fiscal year 2010 administrative expenditures of \$329,300, which exceeded the actual expenditures of \$262,316.

The Notes to the Financial Statements provide additional background information to assist the reader in understanding the data provided in the financial statements.

Financial Analysis

	<u>2010</u>	<u>2009</u>
Total Assets	\$30,603,954	\$31,185,753
Liabilities:		
Due to Carriers for Losses	\$11,392,069	\$12,970,694
Other Liabilities	\$15,841,711	\$15,569,255
 Total Revenues & Expenditures	 \$ 262,316	 \$ 310,242
 Total Budgeted Expenditures	 \$ 329,300	 \$ 508,600

**State of New Jersey
Individual Health Coverage Program
Management's Discussion and Analysis
June 30, 2010**

Total expenditures decreased by \$47,926 as compared to fiscal year 2009. This was the result of no costs for audits of reimbursable losses and less than expected salaries and fringe. Costs for audits of reimbursable losses are accrued in the fiscal year the losses are reported. No audit costs related to reimbursable losses were recorded in fiscal year 2010, because the costs were accrued in fiscal year 2009 for the final period in which loss reimbursements were provided.

Expenditures were favorable as compared to budget due primarily to less than expected salaries, benefits and legal fees.

For the fiscal year ended June 30, 2010, salaries and fringe accounted for 81.3% of total expenditures and legal fees accounted for 9.4%, as compared to 71.1% and 4.5%, respectively, for the fiscal year ended June 30, 2009.

Contacting the Program Board

This financial report is designed to provide the Individual Health Coverage Program Board and the member carriers with a general overview of the Program's finances and to demonstrate the Board's accountability for the administrative assessment funds received. If there are any questions about this report or need additional information, contact the State of New Jersey Individual Health Coverage Program at 20 West State Street, 11th floor, PO Box 325, Trenton, New Jersey 08625-0325.

State of New Jersey
Individual Health Coverage Program
Statement of Net Assets
June 30, 2010

Assets	General Fund	Loss Assessment Fund (Agency Fund)	Total (Memorandum Only)
Cash and cash equivalents	\$ 27,228,507	\$ --	\$ 27,228,507
Restricted cash - treasury	<u>3,370,174</u>	<u>--</u>	<u>3,370,174</u>
Total cash and cash equivalents	30,598,681	--	30,598,681
Accounts receivable			
Accounts receivable - members (billed)	5,273	--	5,273
Due from general fund	<u>--</u>	<u>11,392,069</u>	<u>11,392,069</u>
Total accounts receivable	<u>5,273</u>	<u>11,392,069</u>	<u>11,397,342</u>
	<u>\$ 30,603,954</u>	<u>\$ 11,392,069</u>	<u>\$ 41,996,023</u>
Liabilities and Net Assets			
Due to loss assessment fund	\$ 11,392,069	\$ --	\$ 11,392,069
Interest payable - members	6,472,280	--	6,472,280
Accounts payable - members	8,371,257	--	8,371,257
Accounts payable	9,856	--	9,856
Accrued expenses	614,871	--	614,871
Due to SEH program	41,747	--	41,747
Deferred income	331,700	--	331,700
Net paid loss reimbursement due - members	<u>--</u>	<u>11,392,069</u>	<u>11,392,069</u>
Total liabilities	27,233,780	11,392,069	38,625,849
Net Assets			
Restricted	3,370,174	--	3,370,174
Unrestricted	<u>--</u>	<u>--</u>	<u>--</u>
	<u>3,370,174</u>	<u>--</u>	<u>3,370,174</u>
	<u>\$ 30,603,954</u>	<u>\$ 11,392,069</u>	<u>\$ 41,996,023</u>

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

State of New Jersey
Individual Health Coverage Program
Statement of Changes in Net Assets
For the Year Ended June 30, 2010

Revenues		
Administrative assessment		\$ 262,316
Expenditures		
Current operations		
Audit fees - program	20,000	
Salaries and fringe benefits	213,156	
Legal fees	24,690	
Other administrative expenses	2,798	
Printing expenses	490	
Professional services	1,204	
		<u>262,338</u>
Total expenditures from current operations		<u>262,338</u>
Other Income and Expenditures		
Late fees		<u>22</u>
Total other income and expenditures		<u>22</u>
Changes in net assets- unrestricted		--
Net assets- unrestricted at the beginning of the year		<u>--</u>
Net assets- unrestricted at the end of the year		<u>\$ --</u>

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

**State of New Jersey Individual Health Coverage Program
 Statement of Changes in Assets and Liabilities -
 Loss Assessment (Agency) Fund
 For the Year Ended June 30, 2010**

	Beginning Balance	Additions	Deductions	Ending Balance
Due from general fund	\$ <u>12,970,694</u>	\$ <u>470,464</u>	\$ <u>2,049,089</u>	\$ <u>11,392,069</u>
Net paid loss reimbursement due - members	\$ <u>12,970,694</u>	\$ <u>470,464</u>	\$ <u>2,049,089</u>	\$ <u>11,392,069</u>

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

**State of New Jersey
Individual Health Coverage Program
Notes to Financial Statements
June 30, 2010**

1. Organization and Purpose

The State of New Jersey Individual Health Coverage Program (the "Program") was created pursuant to N.J.S.A. 17B:27A-2 to 16, amended by L.1993, c.164, L. 1994, c.102, L. 1995, c.291, L. 1997, c.146, L. 2001, c.368 and L. 2008, c.38. It has as its members all insurance companies, health service corporations, hospital service corporations, medical service corporations, and health maintenance organizations that issue or have in force health benefits plans in New Jersey. The purpose of the Program is to assure the availability of standardized individual health benefits plans and basic and essential plans in New Jersey on an open enrollment, community-rated or modified community-rated basis, and to reimburse certain losses of member companies for the calendar year ended December 31, 1992 pursuant to N.J.S.A. 17B:27A-13, for each calendar year ended December 31, 1993 through December 31, 1996, and for each two-year calculation period through 2007/2008 pursuant to N.J.S.A. 17B:27A-12, as amended. Pursuant to L. 2008, c.38 carriers cannot seek reimbursement for losses after the 2007/2008 calculation period. Assessments to carriers subsequent to the 2007/2008 calculation period will be solely to fund administrative expenses. The Program is tax-exempt.

2. Basis of Presentation and Accounting Policies

The Program's financial statements are prepared in accordance with accounting principles generally accepted in the United States of America as prescribed by the Governmental Accounting Standards Board ("GASB"). The Program follows the pronouncements of all applicable Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions and Accounting Research Bulletins on Accounting Procedures issued on or before November 30, 1989, unless they conflict with or contradict GASB pronouncements. In addition all financial records are kept in accordance with the State of New Jersey's prescribed policies and procedures.

General Fund and Loss Assessment (Agency) Fund

The IHC Program is made up of two funds, the General Fund and the Loss Assessment (Agency) Fund. The IHC Program Agency Fund was established to separate operating costs from member company loss reimbursements that are based on formula driven by the established regulatory authority. The Agency Fund houses the liability for the net paid loss reimbursement due to member companies with the corresponding debit being Due from the General Fund where all the cash balances and administrative activities are maintained.

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 of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Several prior year loss audits were completed during the fiscal year ended June 30, 2010, resulting in the reversal of the accruals which were based on estimated audit costs. The estimates were accrued in the fiscal year when the losses were reported. The estimates exceeded the actual costs for the loss calculation periods as follows:

2001/2002	
2003/2004	\$183,290
2005/2006	\$134,202
	\$136,732

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Notes to Financial Statements
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These amounts represent the reversal of both the member's and the Program's share of the audit costs. Pursuant to N.J.A.C.11:20-8.8(b) the members and the Program share the costs equally. The amounts for the member's share are included as deductions in the Statement of Changes in Assets and Liabilities – Loss Assessment (Agency) Fund because the member's share of the actual audit costs reduces the amount of the loss reimbursement. The Program's share of the costs has been reclassified from Accrued Expenses to the Accounts Payable – Members account and will be refunded to the carriers for those periods when the final reconciliation is prepared.

Cash and Cash Equivalents

Cash and cash equivalents include cash held in banks, and cash held by the State of New Jersey. The Program's total cash and cash equivalents were \$30,598,681 at June 30, 2010. The Program's bank balances were \$163,920 at June 30, 2010, all of which was insured by the Federal Deposit Insurance Corporation held in the Program's name by the Program's financial institutions or agents.

The interest income earned was recorded as a payable to member companies. As of June 30, 2010, the amount of interest income held by the Program is \$6,472,280. The amount of interest earned shall be distributed to member carriers in accordance with N.J.A.C. 11:20-2.7(c)2 upon completion of the loss and administrative audits, issuance of final reconciliations, and settlement of outstanding litigation.

Cash held by the State of New Jersey Department of Banking and Insurance (DOBI) include funds used for payment of Program expenses, such as staff salaries, fringe benefits, and other miscellaneous expenses that are provided through State sources. The State of New Jersey also holds restricted cash funds that are related to litigation over disputed assessment amounts. As of June 30, 2010, the restricted cash balance was \$3,370,174.

Cash and cash equivalents consist of:

Commercial Checking	\$ 899
Money Market	163,021
NJ State - IHC DOBI - Admin	26,288
Cash Held In Treasury	27,038,299
Restricted Cash - Treasury	<u>3,370,174</u>
Total Cash and Cash Equivalents	<u>\$ 30,598,681</u>

Accounts Receivable - Billed

Accounts receivable consists of amounts receivable from member carriers that were billed a loss assessment to fund reimbursement to those carriers offering individual health coverage in the State of New Jersey that incurred reimbursable losses. Member carriers are also billed an administrative assessment to fund the budgeted amount for Program expenses. No allowance for doubtful accounts was recorded, since any uncollectible amounts, should they occur, would be reallocated to other member carriers in accordance with N.J.S.A. 17B:27A-11 and 12.

Accounts Payable – Members

The balance represents amounts to be refunded to the members as a result of differences in the assessment to all member carriers of reported losses versus audited losses, budgeted administrative expenses assessed versus audited administrative expenses, and appeals of assessments billed resulting from Exhibit K revisions. The amounts will be refunded to the carriers following the final reconciliation of the reimbursable losses and the Program expenses for those calculation periods.

Net Paid Loss Reimbursements Due to Members

Net paid loss reimbursements due to members represents amounts due to member carriers who have incurred reimbursable losses as a result of offering individual health coverage in the State, in accordance with N.J.A.C. 11:20-8.5. The liability is recorded in the year the paid losses are reported by the members.

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As of June 30, 2010, approximately \$11 million was due to fifteen carriers for the losses incurred for the 1993-2008 calculation periods.

Pursuant to N.J.A.C. 11:20-8.8, audits are performed for carriers with reported net paid reimbursable losses, for each calculation period. Due to the timing of the audits, any adjustments are recorded in the year the audit is completed. No provision has been made in the accompanying financial statements to reflect the possible results of on-going loss audits.

Revenues and Operating Expenditures

Revenues and expenditures are related to the operation of the Program. Revenues are based on an administrative assessment to the member carriers pursuant to N.J.A.C. 11:20-2.12 of a budgeted amount approved by the IHC Program Board. Revenues are recorded when earned. Expenditures are recorded when incurred.

There is no balance for the unrestricted fund balance of the Program pursuant to N.J.A.C. 11:20-2.12(a). A final reconciliation of the assessment for administrative expenses shall be made upon approval of the final audited statement of the Program's financial statements. The member's share shall be calculated based on the audited amount of the expenses and credited for any money advanced against the previous assessment.

Related Party Transactions

Although the Program and Small Employer Health Benefits Program ("SEH Program") are distinct state agencies and have separate Boards of Directors and regulations, the programs share the staff, thus salaries, fringe benefits and other miscellaneous expenses incurred through the Department of Banking and Insurance are recorded equally by each program. In 2010 charges to and from the SEH Program amounted to \$1,990 and \$213,156, respectively. As of June 30, 2010 the Program owed the SEH Program \$41,747.

Pensions

The staff of the Program is covered under the State Health Benefits Plan, which includes health, dental, and prescription coverage.

The State offers seven defined benefit pension funds: Public Employees' Retirement System ("PERS"), Teachers' Pension and Annuity Fund ("TPAF"), Police and Firemen's Retirement System ("PFRS"), State Police Retirement System ("SPRS"), Judicial Retirement System ("JRS"), Consolidated Police and Firemen's Pension Fund ("CPFPPF"), and the Prison Officers' Pension Fund ("POPF"). The staff of the Small Employer Health Benefits Program are members of the PERS.

The PERS was established in 1955 by New Jersey Statute and can be found in the New Jersey Statutes annotated, Title 43, Chapter 15A. Changes in the law can only be made by an act of the State legislature. Rules governing the operation and administration of the system may be found in Title 17, Chapters 1 and 2 of the New Jersey Administrative Code. The system was established to provide retirement, death and disability benefits, including post-retirement health care, to all full-time employees of the State and any county, municipality, school district, or public agency provided the employee is not a member of any other state-administered retirement system. Membership is mandatory for such employees.

Vesting occurs after 8 to 10 years of service for pension benefits and 25 years for post-retirement health care coverage. Members are always fully vested in their own contributions and, after three years of service credit, become vested for 2% of the related interest earned on the contributions.

The PERS is a defined benefit plan administered by the New Jersey Division of Pensions and Benefits. Administrative expenses are paid by the PERS to the State of New Jersey, Department of Treasury. Contributions include funding for basic retirement allowances, cost-of-living adjustments, noncontributory death benefits, and cost of medical premiums after retirement for qualified retirees.

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The full normal employee contribution rate is 5.5% of base salary. The rate for members who are eligible for the Prosecutors Part of the PERS (Chapter 366, P.L. 2001) is 8.5% of base salary.

Employers are required to contribute at an actuarially determined rate. The annual employer contributions include funding for basic retirement allowances, cost-of-living adjustments, and noncontributory death benefits.

In accordance with the provisions of N.J.S.A. 43:15A, the contribution policy requires State-related employers and the State of New Jersey to contribute at an actuarially determined rate. The actuarial cost method is projected unit credit. The actuarial assumptions were: investment rate of return 8.25%, salary range 5.45%, cost-of-living adjustments of 60% of the average consumer price index for the calendar year. The asset valuation method is the five year average of market value.

Contributions during the fiscal year 2009 for the PERS amounted to approximately \$1.5 billion. The State of New Jersey's annual required contribution and actual contributions were \$622,123,112 and \$79,296,935, respectively.

The PERS had an actuarial accrued liability of \$17,072,702,680 as of June 30, 2008. The actuarial value of assets of \$11,200,668,671, at June 30, 2008, was less than PERS liabilities, resulting in a funding ratio of 65.6%, or \$5,872,034,009 in funding deficit. Covered payroll for employees under the PERS amounted to \$4,609,019,779, which translates into a funding deficit of 127.4% of covered payroll.

Retirement benefits for age and service are available at age 60. Employees who retire at the age of 60 are entitled to a retirement benefit determined to be 1/55th of the final average salary for each year of service credit. Final average salary equals the average salary for the final three years of service prior to retirement (or the highest three years compensation if other than the final three years). Members may seek early retirement after achieving 25 years of service credit or they may elect deferred retirement after achieving eight to ten years of service credit, in which case, benefits would begin the first day of the month after the member attains normal retirement age.

Financial statements for the State of New Jersey Public Employees' Retirement System are available by contacting the Division of Pensions and Benefits, P.O. Box 295, Trenton, NJ 08625-0295.

The information contained herein for the pension footnote is taken from the PERS report for the fiscal year ended June 30, 2009, because the report for the fiscal year ended June 30, 2010 is not available at the time of issuance of this audit report and the information contained in the note is not reflected in the financial statements for the Program for the fiscal year ended June 30, 2010.

3. Fair Value Measurements

Effective July 1, 2008, the Program adopted the accounting pronouncement for Fair Value Measurements. The pronouncement defines fair value, establishes a framework for measuring fair value under generally accepted accounting principles and enhances disclosure about fair value measurements. Fair value is defined under the pronouncement as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participations on the measurement date. Valuation techniques used to measure fair value under the pronouncement must maximize the use of observable inputs and minimize the use of unobservable inputs. The standard describes a fair value hierarchy based on three levels of inputs, of which the first two are considered observable and the third unobservable, that may be used to measure fair value are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities.

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- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the asset or liabilities.
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liabilities.

In accordance with accounting standards, the following tables represent the Program's fair value hierarchy for its financial assets (cash and cash equivalents) measured at fair value on a recurring basis as of June 30, 2010:

	<u>Level 1</u>	<u>Level 2</u>	<u>Level 3</u>
Cash and cash equivalents	<u>\$ 30,598,681</u>	<u>\$ --</u>	<u>\$ --</u>

4. Litigation

The Program is currently party to one legal action, which involves a challenge to the nature and extent of documentation to support the independent audit of the reimbursable losses. In the opinion of management, the ultimate resolution of this matter will not have an effect on the Program's financial statements because any losses incurred will be reallocated to the member insurance carriers.

5. Subsequent Events

The Program has evaluated subsequent events occurring after the statement of net assets through the date of November 17, 2010. Based on this evaluation, the Program has determined that the following subsequent events require disclosure. In fiscal year 2011, the Program has selected a bid submitted by Navigant and will be entering into a contract to engage in research and analysis regarding a methodology and/or pricing system for reimbursement of claims by carriers for health care services rendered on a non-network or out-of-network basis for a cost of \$400,000. Member companies will be assessed in fiscal year 2011 for the additional administrative assessment to cover the expense of this agreement.