STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES
TEACHER HEALTH INSURANCE SECURITY FUND

FINANCIAL AUDIT
For the Year Ended June 30, 2007

AGENCY OFFICIALS

Director	Barry S. Maram
Assistant Director	Vacant
General Counsel	Nancy Shalowitz (7/1/06-12/28/07) Kyong Lee (Acting) (12/31/07 – Current)
Inspector General	John C. Allen
State Purchasing Officer	Thomas Meirink
Division of Finance, Administrator	Michael Moss
Office of Fiscal Management, Chief	Jack Dodds

Department of Healthcare and Family Services offices are located at:

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STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES
TEACHER HEALTH INSURANCE SECURITY FUND
FINANCIAL AUDIT
For the Year Ended June 30, 2007

FINANCIAL STATEMENT REPORT

SUMMARY

The audit of the accompanying financial statements of the Illinois Department of Healthcare and Family Services' Teacher Health Insurance Security Fund was performed by the Office of the Auditor General.

Based on their audit, the auditors expressed an unqualified opinion on the Teacher Health Insurance Security Fund's financial statements.

SUMMARY OF FINDINGS

The auditors identified matters involving the Department's internal control over financial reporting that they considered to be a significant deficiency. The significant deficiency is described in the accompanying Schedule of Findings on pages 17-18 of this report as finding 07-1, financial statements not timely.

EXIT CONFERENCE

The finding and recommendation appearing in this report was discussed with Department personnel at an exit conference on May 22, 2008. Attending were:

Department of Healthcare and Family Services
Elvin Lay, Fiscal Chief
Gary Casper, Fiscal Manager
Peggy Edwards, External Audit Liaison
Chris Butkauskas, Administrative Assistant

Office of the Auditor General
Georgine Stephens, Assistance Director
Teresa Davis, Audit Manager
Paula Sorensen, Audit Supervisor

The response to the recommendation was provided by Peggy Edwards on June 5, 2008.

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OFFICE OF THE AUDITOR GENERAL
WILLIAM G. HOLLAND

INDEPENDENT AUDITORS' REPORT

Honorable William G. Holland
Auditor General
State of Illinois

We have audited the accompanying financial statements of the Teacher Health Insurance Security Fund of the State of Illinois, Department of Healthcare and Family Services, as of and for the year ended June 30, 2007, as listed in the table of contents. These financial statements are the responsibility of the State of Illinois, Department of Healthcare and Family Services' 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 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 the 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 Teacher Health Insurance Security Fund of the State of Illinois, Department of Healthcare and Family Services, as of June 30, 2007, and the changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated June 12, 2008 on our consideration of the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting of the Teacher Health Insurance Security Fund and on our tests of the State of Illinois, Department of Healthcare and Family Services' compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

INTERNET ADDRESS: AUDITOR@MAIL.STATE.IL.US

The Schedule of Funding Progress for the Year Ended June 30, 2007 and the Schedule of Contributions from Employers and Other Contributing Entities for the Year Ended June 30, 2007 on pages 13-14 are not a required part of the financial statements of the Teacher Health Insurance Security Fund but is supplementary 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 of the required supplementary information. However, we did not audit the information and express no opinion on it.

The State of Illinois, Department of Healthcare and Family Services has not presented a management's discussion and analysis for the Teacher Health Insurance Security Fund that accounting principles generally accepted in the United States of America has determined is necessary to supplement, although not required to be part of, the financial statements.

Bruce L. Bullard

Bruce L. Bullard, CPA
Director of Financial and Compliance Audits

June 12, 2008

STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES
TEACHER HEALTH INSURANCE SECURITY FUND

STATEMENT OF PLAN NET ASSETS

June 30, 2007

(amounts expressed in thousands)

Assets	
Cash and short-term investments	$ 85,913
Receivables	
Employer	2,641
Employee	3,521
Federal government	5,479
Interest	271
Other receivables	5,539
Total receivables	17,451
Total assets	103,364
Liabilities	
Accounts payable and other	37,454
Intergovernmental payables	1
Due to other funds	57
Short-term compensated absences	1
Total current liabilities	37,513
Long-term compensated absences	61
Total liabilities	37,574
Net assets held in trust for other postemployment benefits	$ 65,790

The accompanying notes to the financial statements are an integral part of this statement.

STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES
TEACHER HEALTH INSURANCE SECURITY FUND
STATEMENT OF CHANGES IN PLAN NET ASSETS
June 30, 2007

(amounts expressed in thousands)

Additions	
Contributions	
Employer	$ 58,191
State	75,839
Plan member:	
Actives	77,377
Retirees	128,580
Consolidated Omnibus Budget Reconciliation Act	189
Total contributions	340,176
Interest income	3,454
Federal government Medicare Part D	17,026
Total additions	360,656
Deductions	
Benefit payments	356,212
Administrative expense	3,253
Total deductions	359,465
Net increase/(decrease)	1,191
Net assets held in trust for other postemployment benefits	
Beginning of year	64,599
End of year	$ 65,790

The accompanying notes to the financial statements are an integral part of this statement.

The Teacher Health Insurance Security Fund (also known as The Teacher Retirement Insurance Program, "TRIP") is a non-appropriated trust fund held outside the State Treasury, with the State Treasurer as custodian. Revenues deposited into the Trust are for the sole purpose of providing the health benefits to retirees, as established under the plan, and associated administrative costs. TRIP is a cost-sharing multiple-employer defined benefit post-employment healthcare plan that covers retired employees of participating school districts throughout the State of Illinois, excluding the Chicago Public School System. TRIP health coverage includes provisions for medical, prescription, and behavioral health benefits, but does not provide vision, dental, or life insurance benefits. Annuitants may participate in the State administered Preferred Provider Organization plan or choose from several managed care options. The State Employees Group Insurance Act of 1971 (5 ILCS 375/6.5) establishes the eligibility and benefit provisions for the plan. The Illinois Departments of Healthcare and Family Services (HFS) and Central Management Services (CMS) administer the plan with the cooperation of the Teachers Retirement System (TRS).

In order to be eligible, retirees of public schools must have been certified educators or administrators during their time of employment. Non-certified educational support personnel are not eligible, but they can participate in the Illinois Municipal Retirement System. Eligibility to participate in the plan is currently limited to former full-time employees and their dependents.

A. Summary of Significant Accounting Principles

Basis of Accounting: TRIP's financial statements are prepared using the accrual basis of accounting. Plan member contributions are recognized in the period in which the contributions are due. Employer contributions to the plan are recognized when due and the employer has made a formal commitment to provide the contributions. Benefits and refunds are recognized when due and payable in accordance with the terms of the plan.

Cash and Cash Equivalents: Cash and cash equivalents include cash on hand and cash in banks for locally held funds. Cash equivalents are defined as short-term, highly liquid investments readily convertible to cash.

Investments/Deposits: Investments are in money market funds. Investments are reported at fair value.

Compensated Absences: The liability for compensated absences reported in the statement of plan net assets consists of unpaid, accumulated vacation and sick leave balances for Department employees. The liability has been calculated using the vesting method, in which leave amounts for both employees who currently are eligible to receive termination payments and other employees who are expected to become eligible in the future to receive such payments upon termination are included. The liability has been calculated based on the employees' current salary level and includes salary related costs (e.g., Social Security and Medicare tax).

Legislation that became effective January 1, 1998, capped the paid sick leave for all State Employees' Retirement System members at December 31, 1997. Employees continue to accrue twelve sick days per year, but will not receive monetary compensation for any additional time earned after December 31, 1997. Sick days earned between 1984 and December 31, 1997, (with a 50% cash value) would only be used after all days with no cash value are depleted. Any sick days earned and unused after December 31, 1997, will be converted to service time for purposes of calculating employee pension benefits.

Use of Estimates: The preparation of financial statements in conformity with Generally Accepted Accounting Principles (GAAP) requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and to disclose 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.

New Accounting Standards: For the year ended June 30, 2007, the Department implemented Governmental Accounting Standards Board (GASB) Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans* which establishes financial reporting standards for postemployment benefit plans other than pensions.

B. Contribution Information

Membership of the plan consisted of the following at June 30, 2007, the date of the latest actuarial valuation:

Retirees and beneficiaries receiving benefits	61,260
Waived retirees who may elect healthcare coverage in the future	19,260
Terminated plan members entitled to but not yet receiving benefits	14,188
Active plan members	129,322
Total	224,030
Number of participating employers	1,007

The State Employees Group Insurance Act of 1971 (5 ILCS 375/6.6) requires that all active contributors of the Teachers' Retirement System (TRS), who are not employees of a department, make contributions to the plan at a rate of .8% of salary and for every employer of a teacher to contribute an amount equal to .6% of each teacher's salary. Beginning July 1, 2007, HFS will determine, by rule, the percentage required, which each year shall not exceed 105% of the percentage of salary actually required to be paid in the previous fiscal year. The State Pension Funds Continuing Appropriation Act (40 ILCS 15/1.3) requires the State to make a $13 million appropriation and an annual appropriation to the fund in an amount certified by the TRS Board of Trustees. Administrative costs are paid by the fund.

The State Employees Group Insurance Act of 1971 (5 ILCS 375/6.5) requires that the HFS Director determine the rates and premiums for annuitants and dependent beneficiaries and establish the cost-sharing parameters, as well as funding. Member premiums are set by this statute, which provides for a subsidy of either 50% or 75%, depending upon member benefit choices. Dependents are eligible for coverage, at a rate of 100% of the cost of coverage.

For the year ended June 30, 2007, member annuitants (including their dependent beneficiaries) contributed $128.6 million, or approximately 39.33% of total premiums, through their required contributions. Member required contributions ranged from $62.86 to $163.66, per month per retiree, and from $291.51 to $490.99, per month per retiree and spouse (assuming Medicare eligibility). For non-Medicare eligible members, required contributions ranged from $51.22 to $561.11, per month per retiree, and from $256.11 to $1,692.32, per month per retiree plus dependents. The State Employees Group Insurance Act of 1971 (5 ILCS 375/6.6) requires active teachers contribute .8% of salaries; they contributed $77.4 million, or approximately 23.67% of total premiums. The State Employees Group Insurance Act of 1971 (5 ILCS 375/6.6) also requires participating school districts contribute .6% of salaries; they contributed $58.2 million, or approximately 17.80% of total premiums. In addition, the State Employees Group Insurance Act of 1971 (5 ILCS 375/6.6) requires the State contribute .8% of salaries; they contributed $62.8 million, or approximately 19.20% of total premiums. The State also contributed an additional $13 million in fiscal year 2007, which the State Pension Funds Continuing Appropriation Act (40 ILCS 15/1.3) required. The fund received $17.0 million in Medicare Part D subsidy payments from the federal government.

C. Deposits and Investments

Deposits

The State Treasurer is the custodian of the State's cash and cash equivalents for funds maintained in the State Treasury. Deposits in the custody of the State Treasurer are pooled and invested with other State funds in accordance with the Deposit of State Moneys Act of the Illinois Compiled Statutes (15 ILCS 520/11). Funds held by the State Treasurer have not been categorized as to credit risk because the Department does not own individual securities.

Detail on the nature of these deposits and investments are available within the State of Illinois' Comprehensive Annual Financial Report.

Cash on deposit with the State Treasurer totaled $77,007 thousand at June 30, 2007.

Investments

As of June 30, 2007, the Department had the following investments outside of the State Treasury:

	Fair Value (Thousands)	Book Value (Thousands)	Weighted Average Maturity (Years)
Money market mutual funds	$ 8,906	$ 8,906	0.090
Total fixed income investments	$ 8,906	$ 8,906	

Interest Rate Risk: The Department does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk: The Department does not have a formal investment policy that limits investment choices. The Money Market Mutual Funds and the Illinois Public Treasurers' Investment Pool were rated AAAm by Standard & Poor's.

D. Status and Funding Progress—OPEB Plans

The funded status of the plan, as of the most recent actuarial valuation date, is as follows (amounts expressed in thousands):

Actuarial Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL)-- Projected Unit (b)	Unfunded AAL (UAAL) (b-a)	Funded Ratio (a/b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ([b-a]/c)
6/30/07	$65,790	$14,284,678	$14,218,888	.46%	$7,785,458	182.63%

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Actuarially determined amounts are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The Schedule of Funding Progress, presented as required supplementary information following the notes to the financial statements, present multi-year trend information about whether the actuarial values of plan assets are increasing or decreasing over time, relative to the actuarial accrued liabilities for benefits. Current year presentation does not reflect trend information, as this is the first year of implementation of GASB Statement 43.

The accompanying Schedule of Contributions from Employers and Other Contributing Entities presents trend information about the amounts contributed to the plan by employers in comparison to the Annual Required Contribution (ARC), an amount that is actuarially determined in accordance with the parameters of GASB Statement 43. Current year presentation does not reflect trend information, as this is the first year of implementation of GASB Statement 43. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost for each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years.

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations. Additional information as of the latest actuarial valuation follows:

Valuation Date	6/30/07
Actuarial Cost Methods	Projected Unit Credit
Amortization Method	Level Percentage of Pay
Remaining Amortization Period	30 years
Asset Valuation Method	Market Value
Actuarial Assumptions	
Inflation Rate	3.5%
Amortization Period	Open
Investment rate of return*	4.5%*
Healthcare Cost Trend Rate	9% Initial
	5% Ultimate

* Determined as a blended rate of the expected long-term investment returns on plan assets based upon the funded level of the plan as of the valuation date.

E. Long-Term Obligations

Changes in long-term obligations (amounts expressed in thousands) for the year ended June 30, 2007, were as follows:

	Balance July 1, 2006	Additions	Deletions	Balance June 30, 2007	Amounts Due Within One Year
Compensated Absences	$ 59	$ 45	$ 42	$ 62	$ 1
Total	$ 59	$ 45	$ 42	$ 62	$ 1

F. Commitments and Contingencies

The Department is a party to numerous other legal proceedings, many of which normally occur in the course of operations. These proceedings are not, in the opinion of the Department's legal counsel, likely to have a material adverse impact on the Department's financial position. In the event a material action is settled against the Department, such amounts would be paid from future appropriations or by another State agency. Accordingly, no amounts have been provided in the accompanying financial statements related to outstanding litigation.

STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES
TEACHER HEALTH INSURANCE SECURITY FUND
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF FUNDING PROGRESS
(amounts expressed in thousands)

Actuarial Valuation Date	**Actuarial Value of Assets (a)**	**Actuarial Accrued Liability (AAL)-- Projected Unit (b)**	**Unfunded AAL (UAAL) (b-a)**	**Funded Ratio (a/b)**	**Covered Payroll (c)**	**UAAL as a Percentage of Covered Payroll ([b-a]/c)**
6/30/2007	$ 65,790	$ 14,284,678	$ 14,218,888	0.46%	$ 7,785,458	182.63%

STATE OF ILLINOIS
DEPARTMENT OF HEALTHCARE AND FAMILY SERVICES
TEACHER HEALTH INSURANCE SECURITY FUND
REQUIRED SUPPLEMENTARY INFORMATION
SCHEDULE OF CONTRIBUTIONS FROM EMPLOYERS
AND OTHER CONTRIBUTING ENTITIES
(amounts expressed in thousands)

Year Ended June 30	Annual Required Contribution	State Percentage Contributed	Employers Percentage Contributed	Medicare Part D Percentage Contributed
2007	$ 1,013,794	7.48%	5.74%	1.68%

This actuarial valuation as of June 30, 2007, is the first actuarial valuation of the Teacher Health Insurance Security Fund. This and future valuations will set the Annual Required Contribution (ARC) on a prospective basis, meaning each valuation will set the ARC for the following fiscal year. Because this is the first valuation, the ARC calculated from this valuation will set the ARC for two fiscal years, FY2007 and FY2008. The ARC for FY2007 was determined by applying the Employer ARC determined in this valuation as a percentage of payroll (13.31%) to FY2007 payroll ($7.6 billion).

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OFFICE OF THE AUDITOR GENERAL
WILLIAM G. HOLLAND

INDEPENDENT ACCOUNTANTS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS*

Honorable William G. Holland
Auditor General
State of Illinois

We have audited the Teacher Health Insurance Security Fund of the State of Illinois, Department of Healthcare and Family Services, as of and for the year ended June 30, 2007, and have issued our report thereon dated June 12, 2008. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting of the Teacher Health Insurance Security Fund as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the State of Illinois, Department of Healthcare and Family Services' internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of the entity's financial statements that is more than inconsequential will not be prevented or detected by the entity's internal control. We consider the deficiency in the accompanying schedule of findings to be a significant deficiency in internal control over financial reporting as item 07-1.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by the entity's internal control.

Compliance and Other Matters

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

Bruce L. Bullard

Bruce L. Bullard, CPA
Director of Financial and Compliance Audits

June 12, 2008

SCHEDULE OF FINDINGS

For the Year Ended June 30, 2007

07-1. **FINDING** (Financial statements not timely)

The Illinois Department of Healthcare and Family Services (Department) did not provide the auditors with timely financial statements for the Teacher Health Insurance Security Fund.

The Department did not provide complete financial statements for the year ended June 30, 2007 to the auditors until March 3, 2008. Financial statements were received nine months after the year end.

Concepts Statement of Governmental Accounting Standards Board (GASBCS 1, paragraph 66) states "if financial reports are to be useful, they must be issued soon enough after the reported events to affect decisions. Timeliness alone does not make information useful, but the passage of time usually diminishes the usefulness that the information otherwise would have had."

The Department's management has the ultimate responsibility for the Department's internal control system to ensure that the financial statements are timely.

Department management stated that the delay in completing the financial statements was attributed to the implementation of Statement No. 43 of the Governmental Accounting Standards Board, *Financial Reporting for Postemployment Benefit Plans Other than Pension Plans (GASB43)*. As part of the implementation, an actuary firm was acquired through the bid process and significant collaboration was necessary between the Department, the Governor's Office of Management and Budget and the Teachers Retirement System, causing an overall delay in the reporting process.

The late submission of the financial statements causes delays in the audit process and impacts State-wide reporting. (Finding Code No. 07-1)

RECOMMENDATION

We recommend the Department review its current process for the preparation of the Teacher Health Insurance Security Fund's financial statements and allocate the resources necessary to ensure the financial statements are completed on a timely basis.

DEPARTMENT RESPONSE

The Department agrees with the finding. When a new standard is implemented it is critical that due care be given to ensure proper implementation. The implementation of this standard required that an actuarial valuation be performed. Once received, this valuation had to be reviewed by management within the Department and the Governor's Office of Management and Budget (GOMB) to ensure that the information was accurate. Once the review was final, the financial statements were completed and supplied to the Auditor General's Office. The extended timeframe necessary for completion of the report was four months following the initial due date of the statements. Although the Department recognizes the importance of providing timely financial information, we also realize the need for accurate data. As the initial implementation has now been completed, the Department does not anticipate delays in FY' 08.