



FINANCIAL STATEMENTS AND REQUIRED
SUPPLEMENTARY INFORMATION

West Virginia Retiree Health Benefit Trust Fund
Years Ended June 30, 2009 and 2008
With Report of Independent Auditors

Ernst & Young LLP

 **ERNST & YOUNG**

West Virginia Retiree Health Benefit Trust Fund
Financial Statements and Required Supplementary Information

Years Ended June 30, 2009 and 2008

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Report of Independent Auditors

The Finance Board
West Virginia Retiree Health Benefit Trust Fund

We have audited the accompanying statements of plan net assets of the West Virginia Retiree Health Benefit Trust Fund (RHBT), a fiduciary fund of the State of West Virginia, as of June 30, 2009 and 2008, and the related statements of changes in plan net assets for the years then ended. These financial statements are the responsibility of RHBT's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States 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. We were not engaged to perform an audit of RHBT's internal control over financial reporting. Our audits included 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 RHBT'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, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

As discussed in Note 1, the financial statements of RHBT are intended to present the plan net assets and the changes in plan net assets of only that portion of the activities of the State that is attributable to the transactions of the RHBT. They do not purport to, and do not, present fairly the financial position of the State as of June 30, 2009 and 2008, the changes in its financial position or, where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

In our opinion, the financial statements referred to above present fairly, in all material respects, the plan net assets of RHBT, a fiduciary fund of the State of West Virginia, at June 30, 2009 and 2008, and the changes in its plan net assets for the years then ended in conformity with accounting principles generally accepted in the United States.

In accordance with *Government Auditing Standards*, we have also issued our report dated February 4, 2010 on our consideration of RHBT's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is 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.

The management's discussion and analysis on pages 3 through 14 and the supplemental schedules of funding progress and employer contributions on pages 40 and 41 are not a required part of the basic financial statements but are supplementary information required by the Governmental Accounting Standards Board. 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.

Ernst + Young LLP

February 4, 2010

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis

Year Ended June 30, 2009

The June 30, 2009 Annual Financial Report of the West Virginia Retiree Health Benefit Trust Fund (RHBT) presents the following management discussion and analysis as supplementary information to the basic financial statements.

FUND OVERVIEW

RHBT is a fiduciary fund of the State of West Virginia (State), established July 1, 2006, as an irrevocable trust (Code section 5-16D-2). Fund revenues pay costs of the defined benefit, cost-sharing, multiemployer Other Postemployment Benefit (OPEB) plan (the Plan). The Plan provides medical, prescription drug, and life insurance for retirees of State agencies, colleges and universities, county boards of education, and other government entities as set forth in the West Virginia Code (Employers) and has approximately 35,000 policyholders and 51,000 covered lives.

The medical and prescription drug insurance is provided through two options:

- Self Insured Preferred Provider Benefit Plan – primarily for non-Medicare eligible retirees and spouses
- External Managed Care Organizations – primarily for Medicare eligible retirees and spouses

RHBT Medicare eligible members receive medical and prescription drug coverage from a Medicare Advantage Prescription Drug (MAPD) plan administered by Coventry Health Care. RHBT and Medicare make capitation payments to fund the MAPD claims costs. The MAPD plan assumes all risk and liability for Medicare policyholders.

Life insurance is provided through Minnesota Life Insurance Company and is fully funded by member contributions.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

MAJOR DEVELOPMENTS

- The conversion and implementation of financial accounting and premium billing software was completed.
- PEIA/RHBT offices were relocated from the state capitol complex to the Department of Environmental Protection building in Kanawha City.
- Customer Resource Management software began beta testing – with a FY 2010 implementation.
- County Boards of Education initiated legal action seeking relief – from recognizing the OPEB liability in their financial statements.
- Teachers unions initiated legal action seeking to overturn the Finance Board decision to stop subsidizing OPEB premium contributions for employees hired after June 30, 2010.

OVERVIEW OF THE FINANCIAL STATEMENTS

The two basic financial statements (described below) are presented on the accrual basis of accounting:

Statement of Plan Net Assets—Presents information reflecting assets, liabilities, and plan net assets. Plan net assets represent the amount of total assets less total liabilities. The statement of plan net assets is categorized as to current and noncurrent assets and liabilities. For purposes of the basic financial statements, current assets and liabilities are those assets and liabilities with immediate liquidity or which are collectible or become due within 12 months of the statement date. The Statement of Plan Net Assets is the government version of a for-profit balance sheet.

Statement of Changes in Plan Net Assets—Presents contributions and deductions to the Plan during the fiscal year. The primary source of contributions is premium income. The primary sources of deductions are medical and prescription drug claims costs. The Statement of Changes in Plan Net Assets is the government version of a for-profit income statement.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

FINANCIAL HIGHLIGHTS

The following tables summarize the plan net assets and changes in plan net assets as of and for the years ended June 30:

Statement of Net Plan Assets (\$000's)	2009	2008	Change 2009 – 2008	
			Amount	Percent
Assets				
Cash and cash equivalents	\$ 31,410	\$ 9,197	\$ 22,213	242%
Equity position in internal investment pools	359,933	248,611	111,322	45
Due from PEIA	1,537	–	1,537	100
Contribution receivable	12,129	11,195	934	8
Other receivables	974	1,012	(38)	(4)
Total assets	405,983	270,015	135,968	50
Liabilities				
Claims payable	7,660	7,060	600	8
Due to PEIA	–	7,179	(7,179)	(100)
Other liabilities	909	958	(49)	(5)
Total liabilities	8,569	15,197	(6,628)	(44)
Net assets held in trust for OPEB	\$ 397,414	\$ 254,818	\$ 142,596	56%

Comparative year-to-year major variance explanations (2009 vs. 2008) for the Statement of Net Plan Assets are:

Cash and cash equivalents (\$22.2M increase)

- \$22.2M generated from operations

Equity in internal investment pools (\$111.3M increase)

- \$91.0M additional funding transfer from State
- \$20.3M generated from operations and investment earnings

Due to/from West Virginia Public Employees Insurance Agency (PEIA) (\$5.7M decrease)

- \$5.7M decrease is the change in the net result of payments to PEIA for allocated services – and receipts from PEIA for monies collected on behalf of RHBT.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

Contributions receivable (\$0.9M increase)

- \$1.2M increase is attributable to a reduction in allowance for bad debts
- \$0.3M decrease due to timing

Claims payable (\$0.6M increase)

- \$0.6M increase in claims incurred but not yet paid.

Statement of Net Plan Assets (\$000's)

	2008	2007	Change 2008 – 2007	
			Amount	Percent
Assets				
Cash and cash equivalents	\$ 9,197	\$ 1	\$ 9,196	9,196%
Equity position in internal investment pools	248,611	6,247	242,364	3,880
Due from PEIA	–	3,623	(3,623)	(100)
Contribution receivable	11,195	4,384	6,811	155
Other receivables	1,012	5,338	(4,326)	(81)
Total assets	270,015	19,593	250,422	1,278
Liabilities				
Claims payable	7,060	16,400	(9,340)	(57)
Due to PEIA	7,179	–	7,179	100
Other liabilities	958	26	932	3,585
Total liabilities	15,197	16,426	(1,229)	(7)
Net assets held in trust for OPEB	\$ 254,818	\$ 3,167	\$ 251,651	7,946%

Comparative year-to-year major variance explanations (2008 vs. 2007) for the Statement of Net Plan Assets are:

Cash and cash equivalents (\$9.2M increase)

- \$9.2M generated from operations

Equity in internal investment pools (\$242.4M increase)

- \$153.7M additional funding transfer from State
- \$88.7M generated from operations and investment earnings

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

Due to/from West Virginia Public Employees Insurance Agency (PEIA) (\$3.6M increase)

- \$3.6M increase is the net result of the changes in payments to PEIA for allocated services and receipts from PEIA for monies collected on behalf of RHBT.

Contributions receivable (\$6.8M increase)

- \$6.8M increase is attributable to an increase in premium rates and some slowdown in payments due to the adoption of a new remittance procedure.

Other receivables (\$4.3M decrease)

- \$4.3M decrease results from collecting prior year Medicare Drug Subsidy.

Claims payable (\$9.3M decrease)

- \$9.3M decrease is because Medicare covered member's claims liabilities were transferred to the MAPD.

Other liabilities (\$0.9M increase)

- \$0.9M increase is because of certain unpaid capitation payments due to the MAPD.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

Statement of Changes in Net Plan Assets (\$000's)

			Change 2009 – 2008	
	2009	2008	Amount	Percent
Additions				
Employers	\$ 235,137	\$ 324,098	\$ (88,961)	(27)%
Plan members	63,655	60,872	2,783	5
Total contributions	298,792	384,970	(86,178)	(22)
Retiree drug subsidy	1,267	437	830	190
Interest and dividend income	5,456	3,046	2,410	79
Net depreciation in fair value of investments	(2,324)	(2,462)	138	6
Total additions	303,191	385,991	(82,800)	(21)
Deductions				
Managed Care Org. – payments	75,947	57,996	17,951	31
Claims expense, net	81,335	70,215	11,120	16
Administrative service fees	1,384	1,762	(378)	(21)
Other expenses	1,929	4,367	(2,438)	(56)
Total deductions	160,595	134,340	26,255	20
Net increase	142,596	251,651	(109,055)	(43)
Net assets held in trust for OPEB:				
Beginning of period	254,818	3,167	251,651	7,946
End of period	\$ 397,414	\$ 254,818	\$ 142,596	56%

Comparative year-to-year variance explanations (2009 vs. 2008) for the Statement of Changes in Net Plan Assets are:

Employer contributions (\$89.0M decrease)

- \$62.6M decrease in fund transfers from PEIA and the State of West Virginia.
- \$1.4M increase in Annual Required Contribution payments.
- \$11.2M increase in premium contributions because of 10% Pay Go premium rate increase.
- \$39.0M decrease in premium contribution because of one-year passthrough of postemployment accrued actuarial liability fund from PEIA to RHBT.

West Virginia Retiree Health Benefit Trust Fund
Management's Discussion and Analysis (continued)

Plan member contributions (\$2.8M increase)

- \$2.8M increase is the result of a 10% Pay Go premium rate increase.

Retiree drug subsidy (\$0.8M increase)

- \$0.8M increase is the result of additional revenues received for the fiscal year 2008 but recorded in fiscal year 2009 due to prior year underestimate of retiree drug subsidy receivable.

Interest and dividend income (\$2.4M increase)

- \$2.4M increase is because of the growth in funds held for investment as a result of the increase in the trust fund net assets.

Net depreciation in fair value of investments

- Insignificant variance

Managed Care Organization – payments (\$18.0M increase)

- \$18.0M increase results from a 32% increase in the MAPD Plan capitation rates.

Claims expense (\$11.1M increase)

- \$11.1M increase results from inflationary cost increases of 7% for health and 12% for prescription drug claims.

Administrative service fees (\$0.4M decrease)

- \$0.4M decrease is a result of a reduction in precertification fees. The risk for MAPD retirees was transferred and the indemnity plan no longer needed to precertify the services.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

Other expenses (\$2.4M decrease)

- \$4.2M decrease in bad debt expense from improved collections.
- \$0.6M increase in professional fees for miscellaneous software installation and support costs.
- \$0.4M increase in information systems processing cost from increased volume.
- \$0.4M increase in capital asset lease and building rental costs from PEIA due to office relocation and software usage.
- \$0.4M increase in other general and administrative costs from increased volume.

Statement of Changes in Net Plan Assets (\$000's)

	2008	2007	Change 2008 – 2007	
			Amount	Percent
Additions				
Contributions				
Employers	\$ 324,098	\$ 125,146	\$ 198,952	159%
Plan members	60,872	63,591	(2,719)	(4)
Total contributions	384,970	188,737	196,233	104
Retiree drug subsidy	437	19,370	(18,933)	(98)
Interest and dividend income	3,046	75	2,971	3,961
Net depreciation in fair value of investments	(2,462)	–	(2,462)	(100)
Total additions	385,991	208,182	177,809	85
Deductions				
Managed Care Org. – payments	57,996	4,700	53,296	1,134
Claims expense, net	70,215	191,571	(121,356)	(63)
Administrative service fees	1,762	4,518	(2,756)	(61)
Other expenses	4,367	4,226	141	3
Total deductions	134,340	205,015	(70,675)	(34)
Net increase	251,651	3,167	248,484	(7,846)
Net assets held in trust for OPEB:				
Beginning of period	3,167	–	3,167	100
End of period	\$ 254,818	\$ 3,167	\$ 251,651	7,946%

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

Comparative year-to-year variance explanations (2008 vs. 2007) for the Statement of Changes in Net Plan Assets are:

Employer contributions (\$199.0M increase)

- \$153.7M increase in fund transfers from PEIA and the State of West Virginia.
- \$45.3M increase in premium rates and changes in enrollment costs.

Plan member contributions (\$2.7M decrease)

- \$2.7M decrease is the result of reduced member premium contributions resulting from transferring Medicare retirees to the MAPD.

Retiree drug subsidy (\$18.9M decrease)

- \$18.9M decrease is the result of transferring Medicare retiree drug coverage to the MAPD.

Interest and dividend income (\$3.0M increase)

- \$3M increase is because of the growth in funds held for investment as a result of monies transferred from PEIA and the State of West Virginia.

Net depreciation in fair value of investments (\$2.5M decrease)

- \$2.5M decrease is because of the decline in fair value of funds held for investment-related to the global economic recession.

Managed Care Organization – payments (\$53.3M increase)

- \$53.3M increase is the result of transferring Medicare retirees to the MAPD plan.

Claims expense (\$121.4M decrease)

- \$121.4M decrease is the result of transferring Medicare retirees to the MAPD plan.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

Administrative service fees (\$2.8M decrease)

- \$2.8M decrease results from lower third-party administrative fees for processing medical and drug claims as retirees move to the MAPD Plan.

Other expenses (\$0.1M increase)

- \$0.1M inflationary cost increases.

ECONOMIC CONDITIONS

Health care cost inflation continued to significantly exceed general economic inflationary costs. The primary factors contributing to rising health care costs are:

- Medical equipment technology
- New drug therapies
- Consumer-driven advertising for health care services
- Aging population – Baby boomers reaching prime years of health care utilization
- Health insurance premium increases by insurance companies because of reduced investment earnings

OPEB LIABILITY

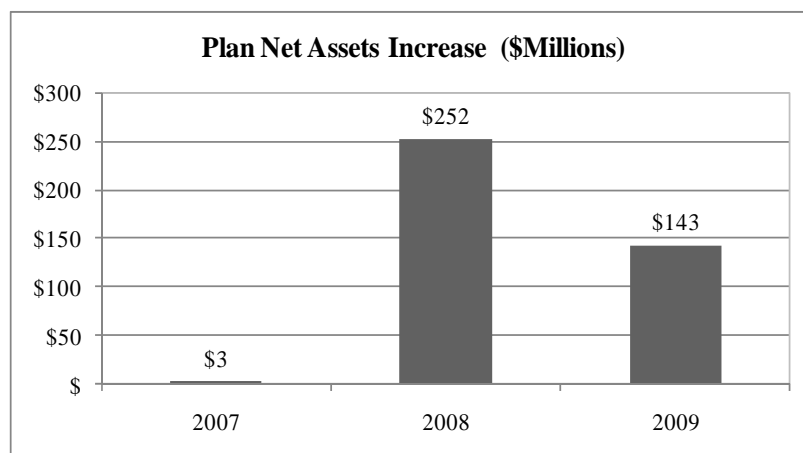
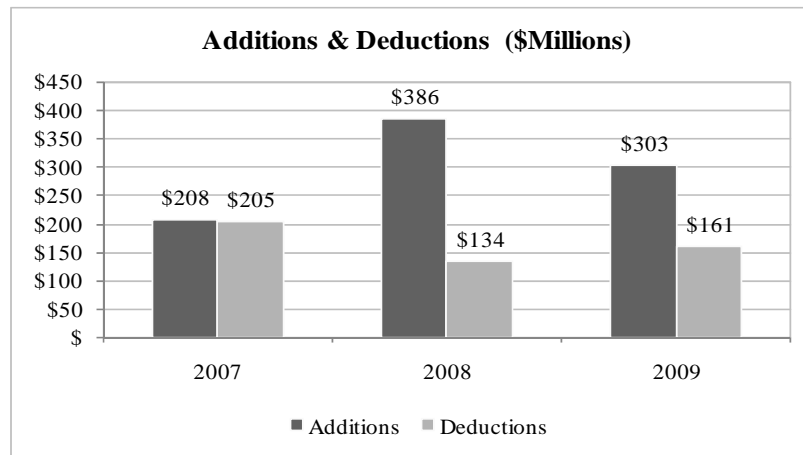
The OPEB liability, Actuarial Accrued Liability (AAL), at June 30, 2009, is \$7.1 billion based on calculations as prescribed in Governmental Accounting Standards Board (GASB) Statement No. 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*. The \$7.1 billion is a substantial unfunded liability for the Employers. The Employers are evaluating options to address this unfunded obligation and fulfill commitments made to current and retired employees and to attract and retain quality governmental employees in the future. The State has demonstrated its intent to deal with the substantial unfunded liability by the passage of Senate Bill 129, which became effective July 1, 2007. This bill amended West Virginia Code (the Code) Section 5-16-25, indicating that the PEIA excess reserve funds shall be transferred to RHBT. Funds totaling \$108.2 million were transferred to the Plan in fiscal year 2008 related to this provision in the Code. In fiscal year 2009, the State transferred \$91 million to pay for general funded employers' portion of the AAL.

West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)

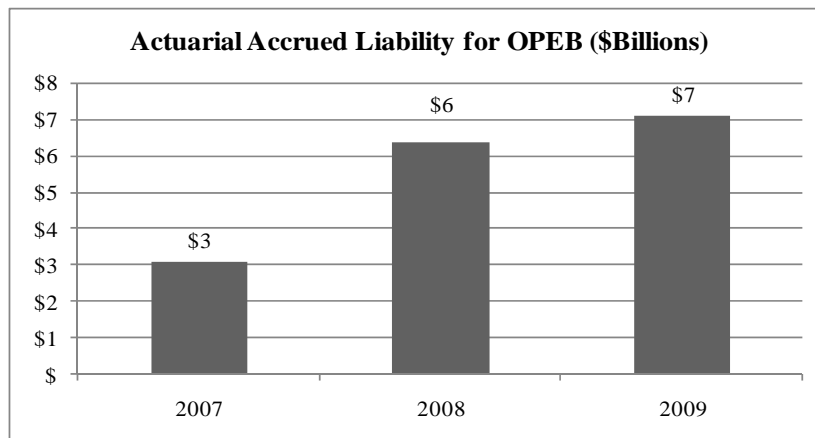
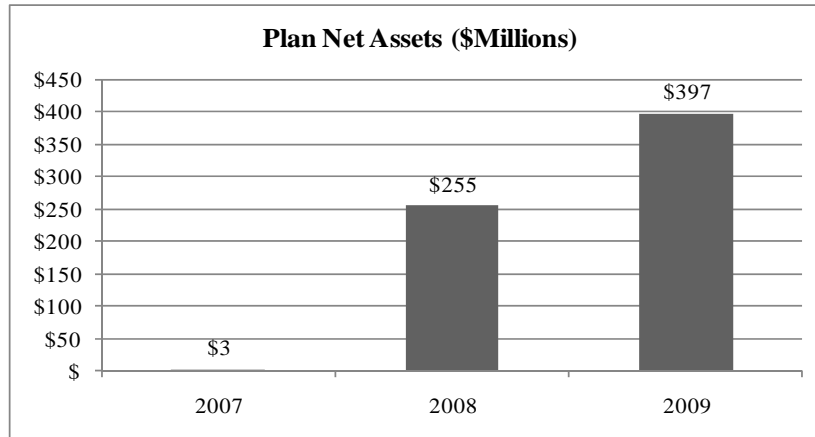
REQUESTS FOR INFORMATION

This financial report is designed to provide RHBT's participants, governing officials, legislators, citizens, and taxpayers with a general overview of RHBT's accountability for the money it receives. If you have any questions about this report or need additional information, contact the Chief Financial Officer at (304) 558-7850, ext. 52642.



West Virginia Retiree Health Benefit Trust Fund

Management's Discussion and Analysis (continued)



West Virginia Retiree Health Benefit Trust Fund

Statement of Plan Net Assets

	June 30	
	2009	2008
	<i>(In Thousands)</i>	
Cash and cash equivalents	\$ 31,410	\$ 9,197
Equity position in internal investment pools	359,933	248,611
Due from PEIA	1,537	–
Contributions receivable – net of allowance for doubtful accounts of \$3,000 and \$4,200, respectively	12,129	11,195
Other receivables	974	1,012
Total assets	405,983	270,015
Claims payable	7,660	7,060
Other liabilities	909	958
Due to PEIA	–	7,179
Total liabilities	8,569	15,197
Net assets held in trust for other postemployment benefits	\$ 397,414	\$ 254,818

See accompanying notes.

West Virginia Retiree Health Benefit Trust Fund

Statements of Changes in Plan Net Assets

	Year Ended June 30	
	2009	2008
	<i>(In Thousands)</i>	
Additions:		
Employers	\$ 235,137	\$ 324,098
Plan members	63,655	60,872
Total contributions	298,792	384,970
Other additions:		
Retiree drug subsidy	1,267	437
Interest and dividend income	5,456	3,046
Net depreciation in fair value of investments	(2,324)	(2,462)
Total additions	303,191	385,991
Deductions:		
Payments to managed care organizations	75,947	57,996
Claims expense, net	81,335	70,215
Administrative service fees	1,384	1,762
Other expenses	1,929	4,367
Total deductions	160,595	134,340
Change in net assets	142,596	251,651
Net assets held in trust for other postemployment benefits:		
Beginning of period	254,818	3,167
End of period	\$ 397,414	\$ 254,818

See accompanying notes.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements

June 30, 2009

1. Reporting Entity

The West Virginia Retiree Health Benefit Trust Fund (RHBT) is a fiduciary fund of the State of West Virginia (State), established July 1, 2006, as an irrevocable trust (Code section 5-16D-2). RHBT's financial results are included in the State's Comprehensive Annual Financial Report (CAFR).

RHBT's basic financial statements present the plan net assets and the changes in plan net assets for the State's activities attributable only to the transactions of RHBT. RHBT's basic financial statements do not purport to, and do not, present fairly the financial position of the State as of June 30, 2009 and 2008, the changes in its financial position or, where applicable, its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

2. Plan Description and Contribution Information

The Plan is a cost-sharing, multiemployer, defined benefit other postemployment benefit plan and covers the retirees of State agencies, colleges and universities, county boards of education, and other government entities as set forth in the West Virginia Code (the Code). Financial activities of the Plan are accounted for in the RHBT. The Plan is administered by a combination of the West Virginia Public Employees Insurance Agency (PEIA) and the RHBT staff. Plan benefits are established and revised by PEIA and RHBT management with the approval of their Finance Boards.

The Plan provides the following benefits:

- Medical and Prescription Drug Insurance
- Life & Accidental Death Insurance

The Plan Medical and Prescription Drug benefits are provided through two options:

- Self Insured Preferred Provider Benefit Plan – primarily for non-Medicare eligible retirees and spouses
- External Managed Care Organizations – primarily for Medicare eligible retirees and spouses

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

2. Plan Description and Contribution Information (continued)

RHBT Medicare eligible members receive medical and prescription drug coverage from a Medicare Advantage Prescription Drug (MAPD) plan administered by Coventry Health Care. RHBT and Medicare make capitation payments to fund the MAPD claims costs. The MAPD plan assumes all risk and liability for Medicare policyholders.

RHBT collects employer contributions for Managed Care Organization (MCO) participants and remits capitation payments to the MCO. Medical and prescription drug benefits paid by the MCO are not reflected in RHBT's financial statements. Contributions earned by RHBT are included in employer and plan member contributions. MCO capitation fee payments are recorded as a deduction on the financial statements.

Survivors of retirees have the option of purchasing the medical and prescription drug coverage.

Life insurance is provided through Minnesota Life Insurance Company – fully funded by member contributions.

The Plan has the following characteristics:

- Other postemployment benefit plan
- Cost-sharing
- Multiemployer
- Defined benefit

Eligible participants of the Plan are retirees of:

- State government agencies
- State colleges and universities
- County boards of education
- Other government entities (towns, county commissions, etc.)

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

2. Plan Description and Contribution Information (continued)

Eligible participants hired after June 30, 2010, will be required to fully fund premium contributions upon retirement.

Plan administration is provided by:

- Claims adjudication – Wells Fargo (third-party administrator)
- The staff of PEIA and RHBT
- Finance Board comprised of nine members

Finance Board members are appointed by the governor, serve a term of four years, and are eligible for reappointment. The State Department of Administration cabinet secretary serves as chairman of the board. Four members represent labor, education, public employees, and public retirees, respectively. The four remaining members represent the public-at-large.

Members may obtain optional life insurance coverage from \$2,500 to \$150,000 depending on age; however, optional AD&D insurance is not available. Members may also elect dependent optional life coverage at levels up to \$20,000 for spouse and \$10,000 per child. Amounts collected by RHBT from members for optional coverage totaled \$9.9M during the fiscal year ended June 30, 2009, and were remitted directly to the carrier. RHBT functions as an agent for these optional benefits and, accordingly, neither these premiums nor the related costs are reflected in the financial statements.

Membership consists of the following as of June 30, 2009:

	<u>Policyholders</u>	<u>Covered Lives</u>
Retirees and beneficiaries	34,602	50,887
Active members	74,533	165,109
Totals	<u>109,135</u>	<u>215,996</u>
Number of participating employers		657

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

2. Plan Description and Contribution Information (continued)

A non-Medicare plan member or beneficiaries receiving benefits contributes monthly health care premiums ranging from \$208 to \$744 per month for retiree-only coverage, and from \$416 to \$1,772 per month for retiree and spouse coverage. Medicare covered retirees are charged health care premiums ranging from \$46 to \$339 per month for retiree-only coverage, and from \$69 to \$1,156 per month for retiree and spouse coverage. Monthly premiums vary based on years of service and choice of coverage.

West Virginia Code section 5-16D-6 also assigns to the PEIA and RHBT Finance Boards the authority to establish and amend contribution requirements of the plan members and the participating employers. Participating employers are required by statute to contribute at a rate assessed each year by RHBT. The annual contractually required rate is the same for all participating employers. However, the annual contractually required rate for State general revenue funded agencies was lower because of additional transfers made by the State. The annual contractually required rate for State general revenue funded agencies was set at \$236.91 and \$272.96 per active employee per month effective June 30, 2009 and 2008, respectively. The annual contractually required rate for State non-general funded agencies and other participating employers was \$388.21 and \$340.47 per active policyholder per month effective June 30, 2009 and 2008, respectively.

West Virginia Code section 5-16-25 requires the Finance Board of PEIA to maintain a reserve of 10% of projected plan costs for general operation purposes and to provide future plan stability. In the event the reserve fund exceeds certain parameters specified in the Code, the excess is to be remitted to RHBT in accordance with Senate Bill 129, which became effective July 1, 2007. Funds totaling \$108.2 million were transferred to the Plan in fiscal year 2008 related to this provision in the Code. In fiscal year 2009, the State transferred \$91 million to pay for general funded employers' portion of the AAL.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

3. Summary of Significant Accounting Policies

Basis of Reporting

RHBT is accounted for as a fiduciary fund. Accordingly, the basic financial statements are prepared using the accrual basis of accounting in conformity with accounting principles generally accepted in the United States of America for governmental entities as prescribed or permitted by the Governmental Accounting Standards Board (GASB). RHBT implemented GASB 43, *Financial Reporting for Postemployment Benefit Plans Other Than Pension Plans*, in 2007 as part of its initial basic financial statement presentation. The primary sources of revenue are plan members and employer contributions. Members' contributions are recognized in the period in which the contributions are due. Employer contributions and related receivables to the Trust are recognized pursuant to a formal commitment from the employer or statutory contractual requirement, when there is a reasonable expectation of collection. Benefits and refunds are recognized when due and payable.

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 certain estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from management's estimates.

Budgetary Requirements

The Code requires the RHBT Finance Board (the Board) to set the annual required contribution sufficient to maintain the fund in an actuarially sound manner. The Board shall annually allocate to the respective employers the employers' portion of the annual required contribution.

Cash and Cash Equivalents

Cash and cash equivalents are monies deposited on account with the West Virginia State Treasurer and used primarily to fund operating expenses.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

3. Summary of Significant Accounting Policies (continued)

Equity Position in Internal Investment Pools

RHBT owns equity positions in state government investment pools managed by the West Virginia Investment Management Board (WVIMB) and the Board of Treasury Investments (BTI). Some investment pool funds are subject to market risk because of changes in interest rates, bond prices, and stock prices. Investment earnings and losses are allocated to RHBT based on the balance of RHBT's investments maintained in relation to the total investments of all state agencies participating in the pool. The Equity Position in Internal Investment Pools is reported at fair value and changes in fair value are included in investment income.

A thirteen-member Board of Trustees governs the WVIMB. Three members of the Board serve by virtue of their office: the Governor, the Auditor, and the Treasurer. The other ten are appointed by the Governor and confirmed by the Senate. All appointees must have experience in pension management, institutional management or financial markets. In addition, one must be an attorney experienced in finance and investment matters and another must be a Certified Public Accountant. Only six of the ten appointed Trustees may be from the same political party. The Governor serves as Chairman of the Board. A Vice-Chairman is elected by the Trustees. A Secretary, who need not be a member of the Board, is also elected by the Trustees to keep a record of the proceedings of the Board. Details regarding these investment pools and a copy of the WVIMB financial report can be obtained by contacting West Virginia Investment Management Board, 500 Virginia Street, East, Suite 200, Charleston, WV 25301 or by calling 304-645-5939.

A five-member Board of Directors governs the BTI. The Governor, Treasurer, and Auditor serve as ex-officio members of the Board. The Governor appoints the two remaining members subject to the advice and consent of the State Senate. Of the two members appointed by the Governor, one shall be a certified public accountant and one shall be an attorney, and both shall have experience in finance, investing, and management. The State Treasurer is Chairman of the Board. The BTI prepares separately issued financial statements covering the pooled fund, which can be obtained from its website or a published copy from the West Virginia Board of Treasury Investments, 1900 Kanawha Boulevard, East, Building 1, Room E-122, Charleston, West Virginia 25305.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

3. Summary of Significant Accounting Policies (continued)

Due To/From PEIA

This balance represents the deficiency or excess of RHBT contributions collected by PEIA over expenses paid by PEIA for RHBT.

Contributions Receivable

Contributions receivable are reported net of an allowance for amounts estimated to be uncollectible based on management's review of the payment status of the underlying accounts and other economic factors that are deemed necessary in the circumstances.

Prescription Drug Rebates

Through arrangements with its Prescription Benefit Manager (PBM), RHBT collects rebates from prescription drug manufacturers. The estimated prescription rebates receivable is based on prescription claims counts and historical average rebate per claim. The receivable has been reduced by the estimated portion that is expected to be uncollectible based on management's review of the payment status of the underlying accounts and other factors that are deemed necessary in the circumstances.

Retiree Drug Subsidy

RHBT recorded retiree drug subsidy (RDS) revenue from the federal government under the provisions of Medicare Part D (primarily for fiscal year 2008). The MAPD provider, Coventry Health Care, assumed ownership of the Retiree Drug Subsidy Revenue when Medicare Retirees were transferred to the MAPD plan. The RDS revenue has been accounted for as voluntary non-exchange transactions in accordance with GASB technical bulletin 2006-1. Accordingly, RDS estimated revenue is recognized as RHBT incurs Medicare-eligible retiree prescription drug expenditures.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

3. Summary of Significant Accounting Policies (continued)

Claims Payable and Expense

The liability for unpaid claims and claims processing costs is based on an actuarial estimate of the ultimate cost of settling such claims due and payable as of the statement of net assets date (including claims reported and in process of settlement, claims reported but not yet processed for settlement, and claims incurred for services provided but not yet reported or processed for settlement). The estimated actuarial liability reflects certain assumptions, which include such factors as enrollment and utilization. Adjustments to the estimated actuarial liability for the final settlement of claims will be reflected in the year that actual results of the settlement of the claims are made and are known. The estimated liability is adjusted periodically based on the most current claim incurrence and claim settlement history.

Claims relating to participants in MCOs, as well as claims relating to participants covered under the optional life insurance plan, are not considered in the liability as RHBT has no liability for the participants who elect such coverage. Additionally, the estimated liability for unpaid claims and claims processing costs is recorded net of amounts ceded to reinsurers for basic life benefits as management believes these reinsured risks are fully recoverable. However, in the event a reinsurer is unable financially to satisfy an obligation, RHBT is responsible for such liability.

Administrative Service Fees

RHBT contracts with two external third-party administrators (TPA) for claims adjudication precertification reviews, utilization reviews, and various other duties. TPA fees are assessed monthly based upon the number of covered members without regard to the period in which a claim is incurred. TPA contracts are either on an annual or biannual basis.

Other Operating Expenses

Other operating expenses are comprised primarily of:

- Professional fees
- Personnel costs
- Lease costs from PEIA

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

3. Summary of Significant Accounting Policies (continued)

RHBT and PEIA share:

- Office space
- Personnel
- Computer systems
- Third-party administrators

Expenses directly attributable to the OPEB plan are charged to RHBT. Shared expenses with PEIA are allocated based on membership count between PEIA and RHBT. Personnel expenses attributable to RHBT full-time dedicated employees are charged in full to RHBT; while the balance of the combined personnel expense is allocated between the two entities based on estimated time requirements.

Reclassifications

Certain 2008 amounts in accompanying financial statements have been reclassified to conform to 2009 presentation. Such reclassifications did not impact the previously reported change in net assets.

4. Deposit and Investment Risk Disclosures

Equity Position in Internal Investment Pool Managed by BTI

WV Money Market Pool (*Formerly Cash Liquidity Pool*)

RHBT's investment in the BTI WV Money Market pool of \$159,395,000 and \$50,114,089 at June 30, 2009 and 2008, respectively, represents approximately 6% and 2%, respectively, of total investments in this pool and is reported as part of equity position in internal investment pools on the statement of plan net assets.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Credit Risk

The BTI limits exposure to credit risk by requiring all corporate bonds held by their WV Money Market Pool to be rated AA- by Standard & Poor's (or its equivalent) or higher. Commercial paper must be rated at least A-1 by Standard & Poor's and P1 by Moody's. Additionally, the pool must have at least 15% of its assets in U.S. Treasury issues.

The following table provides information on the credit ratings of the WV Money Market Pool's investments at June 30, 2009 (in thousands).

Security Type	Credit Rating		Carrying	Percent of
	Moody's	S&P	Value	Pool Assets
Commercial paper	P1	A-1	\$ 592,479	23.05%
Corporate bonds and notes	Aaa	AAA	10,000	0.39
	Aa1	AA	7,000	0.27
	Aa2	AA	10,000	0.39
	Aa3	AA	15,503	0.60
	A1	AA	19,309	0.75
	A1	A	12,000	0.47
Total corporate bonds and notes			73,812	2.87
U.S. agency bonds	Aaa	AAA	294,019	11.44
U.S. Treasury bills*	Aaa	AAA	483,714	18.82
Negotiable certificates of deposit	P1	A-1	128,402	5.00
U.S. agency discount notes	P1	A-1	635,602	24.73
Money market funds	Aaa	AAA	150,223	5.84
Repurchase agreements (underlying securities):				
U.S. Treasury notes*	Aaa	AAA	165,110	6.43
U.S. agency notes	Aaa	AAA	46,900	1.82
Total repurchase agreements			212,010	8.25
Total investments			\$ 2,570,261	100.00%

* U.S. Treasury issues are explicitly guaranteed by the United States government and are not subject to credit risk.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Custodial Credit Risk

Repurchase agreements included in BTI's investment portfolio are collateralized by at least 102% of their value and the collateral is held in the name of the BTI. Securities lending collateral is invested in the lending agent's money market fund in BTI's name.

Interest Rate Risk

The weighted-average maturity of the investments of the WV Money Market Pool cannot exceed 60 days. The maturity of individual securities cannot exceed 397 days from the date of purchase. The following table provides the weighted-average maturities (WAM) for the various asset types in the WV Money Market Pool at June 30, 2009.

Security Type	Carrying Value	WAM (Days)
	<i>(In Thousands)</i>	
Repurchase agreements	\$ 212,010	1
U.S. Treasury bills	483,714	69
Commercial paper	592,479	32
Certificates of deposit	128,402	56
U.S. agency discount notes	635,602	57
Corporate bonds and notes	73,812	38
U.S. agency bonds/notes	294,019	70
Money market funds	150,223	1
Total investments	<u>\$ 2,570,261</u>	<u>47</u>

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Equity Position in Internal Investment Pools Managed by WVIMB

RHBT's investments in the following pools are managed by the WVIMB. Such investments, which are stated at fair value (actual asset allocation), are reported as part of equity position in internal investment pools on the statement of net assets.

	June 30	
	2009	2008
	<i>(In Thousands)</i>	
Large cap domestic equity pool	\$ 4,254	\$ 5,430
Non-large cap domestic equity pool	762	757
International equity pool	3,687	2,374
International nonqualified pool	1,729	–
Total return fixed income pool	134,757	118,132
Fixed income nonqualified	–	71,611
Core fixed income	55,347	–
Short-term fixed income pool	2	193
	\$ 200,538	\$ 198,497

Liquidity Needs and Investment Objectives

The RHBT is expected to have minimal liquidity needs until fiscal year 2011, upon which time annual liquidity needs are expected to increase. The investment objective is to provide for stable, long-term growth of assets, while seeking to minimize risk of loss. There is no specifically identified rate of return target.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Asset Allocation

Based upon the WVIMB's determination of the appropriate risk tolerance for the fund, the WVIMB adopted the following broad asset allocation guidelines for the assets managed for RHBT. (Policy targets are established on a market value basis.)

Asset Class	Policy Target	
	2009	2008
Domestic equity	2.5%	2.5%
International equity	2.5	2.5
Total equity	5.0%	5.0%
Fixed income	95.0%	95.0%
Cash (included in fixed income above)	*	*

* Cash levels to be reviewed as needed, at least annually, collaboratively with management staff from PEIA.

Asset Class Risk Disclosures

Large Cap Domestic Equity Pool

This pool holds equity securities of U.S. companies and money market funds with the highest credit rating. RHBT's amount invested in the large cap domestic pool of \$4,254,000 and \$5,430,000 at June 30, 2009 and 2008, respectively, represents approximately 0.2% and 0.3%, respectively, of total investments in this pool.

Non-Large Cap Domestic Equity Pool

This pool holds equity securities of U.S. companies and money market funds with the highest credit rating. RHBT's amount invested in the Non-Large Cap Domestic Pool of \$762,000 and \$757,000 at June 30, 2009 and 2008, respectively, represents approximately 0.2% and 0.1%, respectively, of total investments in this pool.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

International Equity Pool

This pool has both equity securities and cash that are denominated in foreign currencies and are exposed to foreign currency risks. West Virginia statutes limit the amount of international securities to no more than 30% of total assets managed by the WVIMB. The amounts (in U.S. dollars) of the securities and cash denominated in foreign currencies are as follows:

Currency	2009		
	Equity Securities	Cash	Total
Australian Dollar	\$ 45,295,313	\$ 187,926	\$ 45,483,239
Brazil Cruzeiros Real	76,243,266	1,318,077	77,561,343
British Pound	175,318,942	1,551,666	176,870,608
Canadian Dollar	43,761,183	109,535	43,870,718
Czech Koruna	7,234,731	135	7,234,866
Danish Krone	10,935,831	33,982	10,969,813
Euro	266,768,796	6,226,567	272,995,363
Hong Kong Dollar	115,552,388	304,416	115,856,804
Hungarian Forint	11,566,434	781	11,567,215
Indonesian Rupiah	2,474,340	–	2,474,340
Israeli Shekel	13,692,033	81	13,692,114
Japanese Yen	214,493,385	2,000,670	216,494,055
Malaysian Ringitt	8,765,540	25,190	8,790,730
Mexican New Peso	20,204,832	54,161	20,258,993
New Taiwan Dollar	44,242,681	29,702	44,272,383
New Zealand Dollar	1,750,119	404,401	2,154,520
Norwegian Krone	9,140,372	127,263	9,267,635
Pakistani Rupee	1,371,114	–	1,371,114
Philippine Peso	4,738,490	–	4,738,490
Polish Zloty	4,768,257	39	4,768,296
Singapore Dollar	31,364,188	238,905	31,603,093
South African Rand	20,492,344	55,109	20,547,453
South Korean Won	75,285,153	527,742	75,812,895
Swedish Krona	19,034,030	75,507	19,109,537
Swiss Franc	58,766,408	928,122	59,694,530
Thailand Baht	–	2,202	2,202
Turkish Lira	30,584,716	42,029	30,626,745
Total	\$ 1,313,844,886	\$ 14,244,208	\$ 1,328,089,094

This table excludes cash and securities held by the pool that are denominated in U.S. dollars. The fair value of the U.S. dollar denominated cash and securities is \$181,239,129.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

International Nonqualified Pool

The pool holds an institutional mutual fund that invests in equities denominated in foreign currencies. The value of this investment at June 30, 2009, was \$101,245,849. This investment, although denominated in U.S. dollars, is exposed to foreign currency risk through the underlying investments. The specific currencies of the underlying investments were not available.

Funds are invested in Silchester International Investors' Value Equity Trust. The pool is expected to produce investment returns that exceed the Morgan Stanley Capital International's EAFE index by 200 basis points on an annualized basis over three- to five-year periods, net of external investment management fees. The pool exists for participants who are not "qualified" (as defined by the *Internal Revenue Code*).

West Virginia statute limits the amount of international securities to no more than 30% of the total assets managed by the WVIMB. At June 30, 2009, the WVIMB was in compliance with this limitation. RHB'T's amount invested in the International Nonqualified Pool of \$1,729,000 at June 30, 2009, represents approximately 1.7% of total investments in this pool.

Fixed Income Nonqualified Pool

During the fiscal year the WVIMB liquidated this pool. This pool held positions of institutional mutual funds with a combined value of \$474,561,035 at June 30, 2008. The mutual funds invested in mortgage-backed securities and corporate bonds.

RHB'T's total investment in the Fixed Income Nonqualified Pool of \$71,611,000 at June 30, 2008, represented approximately 15.0% of total investments in the pool.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Total Return Fixed Income Pool (*Previously Named Fixed Income Pool*)

Credit Risk

The WVIMB limits the exposure to credit risk in the Total Return Fixed Income Pool by maintaining at least an average rating of investment grade as defined by the Nationally Recognized Statistical Rating Organizations. The following table provides the weighted-average credit ratings of the asset types in the fixed income pool as of June 30, 2009.

Security Type	Moody's	S&P	2009	
			Fair Value	Percent of Assets
Agency mortgage backed-securities	Aaa	AAA	\$ 531,284,382	20.2%
Money market funds	Aaa	AAA	472,292,326	17.9
Corporate bonds and notes	Baa	BBB	466,052,257	17.7
Corporate collateralized mortgage obligations	Baa	AA	91,081,767	3.5
U.S. Treasury inflation protection bonds	Aaa	AAA	74,631,563	2.8
Agency notes	Aa	AA	3,866,877	0.1
U.S. Treasury bonds and notes	Aaa	AAA	1,678,244	0.1
Corporate preferred securities	C	C	965,455	0.0
Corporate asset-backed securities	Aa	AA	622,399	0.0
Agency collateralized mortgage obligations	Aaa	AAA	465,532	0.0
Total rated investments			\$ 1,642,940,802	62.3%

Unrated securities include commingled investment pools valued at \$987,106,348 and swap options valued at \$(10,205,602), future contracts valued at \$6,356,507, foreign currency forward contracts valued at \$(610,756), and cash of \$16,705,447 pledged to brokers as collateral. These unrated securities represent 37.7% of the fair value of the pool's investments.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Interest Rate Risk

The WVIMB monitors interest rate risk of the Total Return Fixed Income Pool by evaluating the modified duration of the investments in the pool. The following table provides the weighted average modified duration for the various asset types in the Total Return Fixed Income Pool as of June 30, 2009.

Security Type	2009	
	Fair Value	Modified Duration (Years)
Commingled investment pools	\$ 987,105,348	2.5
Agency mortgage-backed securities	531,284,382	9.6
Money market fund	472,292,326	0.0
Corporate notes and bonds	466,052,257	5.7
Corporate collateralized mortgage obligations	91,081,767	5.1
U.S. Treasury inflation protection bonds	74,631,563	13.1
Agency bonds	3,866,877	2.8
U.S. Treasury notes and bonds	1,678,244	16.4
Corporate asset-backed securities	622,399	2.5
Agency collateralized mortgage obligations	465,532	1.0
Total assets	<u>\$ 2,629,080,695</u>	<u>5.4</u>

The Total Return Fixed Income Pool invests in commercial and residential mortgage-backed, asset-backed securities, and collateralized mortgage obligations. The cash flows from these securities are based on the payment of the underlying collateral. The modified duration and yield to maturity of these securities are dependent on estimated prepayment assumptions that consider historical experience, market conditions, and other criteria. Actual prepayments may vary with changes in interest rates. Rising interest rates often result in a slower rate of prepayments while declining rates tend to lead to faster prepayments. As a result, the fair values of these securities are highly sensitive to interest rate changes. At June 30, 2009, the Total Return Fixed Income Pool held \$623,449,368 of these securities – representing approximately 24% of the value of the pool's securities.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

RHBT's amount invested in the Total Return Fixed Income Pool of \$134,757,000 and \$118,132,000 at June 30, 2009 and 2008, respectively, represented approximately 5.0% and 4.3%, respectively, of total investments in the pool.

Core Fixed Income Pool

Credit Risk

The WVIMB limits the exposure to credit risk in the Core Fixed Income Pool by maintaining at least an average rating of investment grade as defined by the Nationally Recognized Statistical Rating Organizations. The following table provides the weighted-average credit ratings of the rated assets in the Core Fixed Income Pool as of June 30, 2009.

Security Type	Moody's	S&P	Fair Value	Percent of Assets
Agency collateralized mortgage obligations	Aaa	AAA	\$ 134,378,380	33.1%
Agency mortgage-backed securities	Aaa	AAA	117,952,526	29.1%
U.S. Treasury bonds and notes	Aaa	AAA	69,633,643	17.2%
Corporate bonds and notes	A	A	41,035,802	10.1%
Corporate collateralized mortgage obligations	Baa	AA	25,367,921	6.3%
Money market funds	Aaa	AAA	15,209,068	3.7%
Corporate asset-backed securities	Aaa	AAA	2,191,003	0.5%
Total rated investments			\$ 405,768,343	100.0%

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Interest Rate Risk

The WVIMB monitors interest rate risk of the Core Fixed Income Pool by evaluating the modified duration of the investments in the pool. The following table provides the weighted-average modified duration for the various asset types in the Core Fixed Income Pool as of June 30, 2009.

Security Type	Fair Value	Modified Duration (years)
Agency collateralized mortgage obligations	\$ 134,378,380	3.4
Agency mortgage-backed securities	117,952,526	8.9
U.S. Treasury bonds and notes	69,633,643	6.4
Corporate bonds and notes	41,035,802	5.0
Corporate collateralized mortgage obligations	25,367,921	4.1
Money market funds	15,209,068	0.0
Corporate asset-backed securities	2,191,003	1.9
Total assets	<u>\$ 405,768,343</u>	<u>5.4</u>

The Core Fixed Income Pool invests in commercial and residential mortgage-backed securities, asset-backed securities, and collateralized mortgage obligations. The cash flows from these securities are based on the payment of the underlying collateral. The modified duration and yield to maturity of these securities are dependent on estimated prepayment assumptions that consider historical experience, market conditions, and other criteria. Actual prepayments may vary with changes in interest rates. Rising interest rates often result in a slower rate of prepayments while declining rates tend to lead to faster prepayments. As a result, the fair values of these securities are highly sensitive to interest rate changes. At June 30, 2009, the Core Fixed Income Pool held \$279,883,830 of these securities. This represents approximately 69% of the value of the pool's securities.

RHBT's amount invested in the Core Fixed Income Pool of \$55,347,000 at June 30, 2009, represents approximately 13.6% of total investments in this pool.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Short-Term Fixed Income Pool

Credit Risk

WVIMB limits the exposure to credit risk in the Short-Term Fixed Income Pool by requiring all corporate bonds to be rated AA or higher. Commercial paper must be rated A1 by Standard & Poor's and P1 by Moody's. Additionally, the pool must have at least 15% of its assets in United States Treasury issues.

The following table provides information on the weighted-average credit ratings of the Short-Term Fixed Income Pool's investments as of June 30, 2009.

Security Type	Moody's	S&P	2009	
			Carrying Value	Percent
Agency discount notes	P1	A-1	\$ 88,452,922	33.3%
U.S. Treasury note	Aaa	AAA	92,585,804	34.9%
Commercial paper	P1	A-1	12,999,680	4.9%
U.S. Treasury bills	Aaa	AAA	43,996,249	16.6%
Agency bonds	Aaa	AAA	27,496,451	10.3%
Money market fund	Aaa	AAA	131	0.0%
Total rated investments			\$ 265,531,237	100.0%

This table includes securities received as collateral for repurchase agreements with a fair value of \$92,585,804 as compared to the amortized cost of the repurchase agreements of \$91,593,000.

Custodial Credit Risk

Repurchase agreements are collateralized at 102% and the collateral is held in the name of the WVIMB. All remaining securities are held by the WVIMB's custodian in the name of the WVIMB.

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

4. Deposit and Investment Risk Disclosures (continued)

Interest Rate Risk

The weighted-average maturity of the investments of the short-term fixed income pool is not to exceed 60 days. The maturity of floating rate notes is assumed to be the next interest rate reset date. The following table provides the weighted-average maturities (WAM) for the various asset types in the Short-Term Fixed Income Pool as of June 30, 2009.

Security Type	2009	
	Carrying Value	WAM (days)
Repurchase agreements	\$ 91,593,000	1
U.S. Treasury bills	43,996,249	23
Commercial paper	12,999,680	5
Agency discount notes	88,452,922	54
Agency bond	27,496,451	52
Money market fund	131	1
Total assets	<u>\$ 264,538,433</u>	<u>28</u>

RHBT's amount invested in the Short-Term Fixed Income Pool at June 30, 2009 and 2008, was nominal.

5. Funded Status and Funding Progress

The funded status of the Plan as of the most recent actuarial valuation is as follows (in thousands):

Actuarial Valuation Date	Actuarial Value of Assets (A)	Actuarial Liability (AAL) – Entry Age (B)	Unfunded AAL (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll (C)	UAAL as a Percentage of Covered Payroll [(B-A)/C]
June 30, 2009	\$ 397,414	\$ 7,079,763	\$ 6,682,349	5.600%	\$ 3,437,271	194.41%

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

5. Funded Status and Funding Progress (continued)

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 health care 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 estimated actuarial accrued liability reflected above is based on the substantive plan in place at the time of the latest actuarial valuation. Accordingly, it reflects the impact of transferring Medicare covered participants to the MAPD plan. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents trend information about whether the actuarial values of plan assets are increasing or decreasing over time relative to the actuarial accrued liabilities for benefits. The purpose of the disclosure is to provide information that approximates the funding progress of the plan.

The accompanying schedule of employer contributions, also presented as required supplementary information, presents trend information about the amounts contributed to the plan by employers in comparison to the amount that is actuarially determined in accordance with the parameters of GASB Statement No. 43 (the ARC). 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 30 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 projection of benefits for financial reporting purposes does not explicitly incorporate the potential effects of legal or contractual funding limitations on the pattern of cost-sharing between the employer and plan members in the future. 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. However, the preparation of any estimate of future postretirement costs requires consideration of a broad array of complex social and economic events. Future changes in the Medicare Advantage Prescription Drug program, changes in reimbursement methodology, the emergence of new and expensive medical procedures and prescription drugs option, changes in the investment rate of return, and other matters increase the level of uncertainty of such estimates. As such, the estimate of

West Virginia Retiree Health Benefit Trust Fund

Notes to Financial Statements (continued)

5. Funded Status and Funding Progress (continued)

postretirement program costs contains considerable uncertainty and variability and actual experience may vary significantly by the current estimated obligation. Additional information for the latest actuarial valuations follows:

	<u>Valuation Date – June 30, 2009</u>
Actuarial cost method	Entry age
Amortization method	Level percentage of projected payroll, closed
Remaining amortization period	27 years
Asset valuation method	Fair value
Actuarial assumptions:	
Investment rate of return	3.72% blended rate reflecting long-term expected returns on RHBT and State investments held by BTI
Health care cost trend rate	9.2% initial; 6.0% ultimate

Required Supplementary Information

West Virginia Retiree Health Benefit Trust Fund

Schedule of Funding Progress

(In Thousands)

Actuarial Valuation Date	Actuarial Value of Assets (A)	Actuarial Accrued Liability (AAL) – Entry Age (B)	Unfunded AAL (UAAL) (B-A)	Funded Ratio (A/B)	Covered Payroll (C)	UAAL as a Percentage of Covered Payroll [(B-A)/C]
June 30, 2009	\$ 397,414	\$ 7,079,763	\$ 6,682,349	5.600%	\$ 3,437,271	194.41%
June 30, 2008	\$ 254,818	\$ 6,362,640	\$ 6,107,822	4.00%	\$ 3,298,252	185.18%
June 30, 2007	\$ 3,167	\$ 3,079,933	\$ 3,076,766	0.10%	\$ 3,312,102	92.89%

The estimated actuarial accrued liability reflected above is based on the substantive plan in place at the time of the latest actuarial valuation. Accordingly, it reflects the impact of transferring Medicare-covered participants to a Medicare Advantage Prescription Drug plan. The total population covered by the RHBT was approximately 109,135 and 106,578 at June 30, 2009 and 2008, respectively.

The investment rate of return changed from 5.22% as of June 2007 to 3.72% as of June 30, 2008 due to the change in long term expected returns on RHBT and State investments held by BTI.

West Virginia Retiree Health Benefit Trust Fund

Schedule of Employer Contributions

(In Thousands)

Year Ended June 30	Annual Required Contribution	Percentage Contributed
2009	\$ 341,565	69%
2008	397,975	81
2007	649,426 (1)	19

(1) The annual required contribution for the year ended June 30, 2007, does not reflect the impact of transferring Medicare plan participants to a MAPD and other substantive plan changes that were made subsequent to the 2007 annual required contribution calculation.

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*

The Finance Board
West Virginia Retiree Health Benefit Trust Fund

We have audited the financial statements of the West Virginia Retiree Health Benefit Trust Fund (RHBT) as of and for the year ended June 30, 2009, and have issued our report thereon dated February 4, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States 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 RHBT's internal control over financial reporting 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 RHBT's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of RHBT's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses and therefore, there can be no assurance that all deficiencies, significant deficiencies, or material weaknesses have been identified. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be material weaknesses.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis.

A material weakness is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. We consider the deficiencies described in the accompanying schedule of findings and responses as items 2009-01 and 2009-02 to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether RHBT's 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*.

RHBT's responses to the findings identified in our audit are described in the accompanying schedule of findings and responses. We did not audit the RHBT's responses and, accordingly, we express no opinion on them.

This report is intended solely for the information and use of management, the Finance Board, and others within the entity, and is not intended to be, and should not be, used by anyone other than these specified parties.

Ernst + Young LLP

February 4, 2010

**STATE OF WEST VIRGINIA
SCHEDULE OF FINDINGS AND RESPONSES**

2009-1 INFORMATION SYSTEM CONTROLS

State Agency

Retiree Health Benefit Trust (RHBT)

- Criteria:** Management is responsible for establishing and maintaining adequate controls over changes to and processes to maintain its information systems.
- Condition:** The following IT general controls findings related to the BAS and Great Plains applications were noted:
- **Manage Changes – Authorization, Testing, and Approval**

During our review of the Great Plains and BAS application change management process, management indicated that the change requests were to be authorized via the weekly task lists; however, we were unable to obtain any documentation surrounding the process. Additionally, no documentation was available to support that the changes/upgrades had been effectively tested and that the change/upgrade obtained final approval for migration to the production environment.
 - **Manage Changes – OS and DB Upgrades/Patches**

The process for applying operating system and database upgrades and/or patches (for the Great Plains application) is informal and no documentation is maintained to support the operating system or database upgrades/patches were authorized, tested, and approved prior to production migration.
 - **Logical Access – Password Settings**

The Great Plains application password settings, due to functionality limitations, are not configured to 1) be a minimum number of characters in length, 2) force password expirations after a set number of days, 3) lock out user accounts after a defined number of invalid login attempts, and 4) prevent users from reusing their previously used passwords.
 - **Logical Access – Administrator Access**

Access to the PROGRAMMER function (which grants users the ability to perform user administration for the BAS application) is not restricted to authorized individuals. This function is granted to three authorized administrators and four programmers.
 - **Logical Access – New User Access Authorization**

New user access is not consistently documented via emails or SATT forms for user access to Great Plains or BAS. Documentation is either not retained or does not include the system whereby access is required, or the type of access to be granted.
- Context:** The information systems conditions noted above could affect the accuracy of processing RHBT financial information, including premiums/contributions.
- Cause:** During the time of our review, management is still in the process of defining and implementing their controls related to program change management and logical access processes. Additionally, management is working with the West Virginia Office of Technology to determine where controls are the responsibility of the agency versus the hosting facility.

**STATE OF WEST VIRGINIA
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS
(continued)**

State Agency
Retiree Health Benefit Trust (RHBT)

Effect:

- Manage Changes – Authorization, Testing, and Approval

Lack of formal written policies and procedures for application changes and upgrades does not contribute to an effective environment and could lead to inconsistencies in protocol or documentation. Without proper documentation of authorization, user acceptance testing, and migration approval, implemented changes to the production environment may not be operating as intended.
- Manage Changes – OS and DB Upgrades/Patches

Lack of formal written policies and procedures for patches and upgrades does not contribute to an effective environment and could lead to inconsistencies in protocol or documentation. Without proper documentation of authorization, user acceptance testing, migration approval, and implemented changes to the production environment may not be operating as intended.
- Logical Access – Password Settings

The current password settings could lead to unauthorized access to sensitive and/or confidential information.
- Logical Access – Administrator Access

This could lead to inappropriate or excessive user access rights being granted to existing users.
- Logical Access – New User Access Authorization

The lack of controls surrounding the authorization and approval of system access could lead to inappropriate or excessive user access rights being granted to existing users.

Recommendation: Based on the findings noted, outlined below are the recommendations:

- Manage Changes – Authorization, Testing, and Approval

Management should implement formal (written) policies and procedures surrounding Great Plains and BAS program changes (modifications or upgrades) to include documentation of authorization, testing, and approval.
- Manage Changes – OS and DB Upgrades/Patches

Management should implement formal (written) policies and procedures surrounding the upgrades and/or patches applied to the operating system and database upgrades supporting the Great Plains application.
- Logical Access – Password Settings

Management should work with the application vendor to enhance password security. The following are considered leading industry practice.

 - Require passwords to be six to eight characters in length.
 - Force passwords to expire every 60 to 90 days.

**STATE OF WEST VIRGINIA
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS
(continued)**

State Agency

Retiree Health Benefit Trust (RHBT)

- Automatically lock user accounts after three to five unsuccessful logon attempts.
- Prevent users from reusing previously used passwords by maintaining a password history file.
- Logical Access – Administrator Access

Management should restrict access to the privileged roles within the BAS application and limit them to a select number of IT personnel who require such access.

If preventive measures cannot be taken, due to system limitations, management should consider performing a periodic review of all changes to user security for the BAS application to determine if the changes were performed by authorized individuals. Management should confirm that adequate documentation is maintained to provide evidence (sign-offs, hard-copy reports, etc.) of the review.

- Logical Access – New User Access Authorization

Management should enhance the current application access administration processes to verify that all user access is consistently documented with access details (access needed per system) and management approval is granted prior to gaining access to the systems. Management should verify that adequate documentation is maintained to provide evidence (sign-offs, e-mails, SATT forms, etc.) of the authorization and approval.

**Views of
Responsible
Officials and
Planned Corrective
Actions:**

We are in the process of rolling out a new change control system (PITS). This will allow the staff to make formal request to the IT staff and will track the request within this system. The system is in production at this point and is being used by the Finance Group and the Eligibility Group. The complete rollout is scheduled to be complete by April 1, 2010.

A formal procedure was developed in April 2008. However, RHBT will need to work closer with WVOT to make sure that all patches are documented according to the procedure.

When attempting to log on in GP, a call is made to SQL Server to verify the userid and password. SQL Server is under the constraints to only allow four attempts. The current version of GP (9.0) uses all four attempts to verify one attempt in GP. Therefore if the restrictions were turned on in GP, there would be no room for error. Because the SQL Server is maintained by WVOT and is a statewide process, the attempts cannot be increased through SQL Server. Therefore RHBT's only option is to move to GP version 10 or 11. These versions are equipped to handle this issue. RHBT plans to move to one of these versions before the end of FY 2010.

**STATE OF WEST VIRGINIA
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-1 INFORMATION SYSTEM CONTROLS
(continued)**

**State Agency
Retiree Health Benefit Trust (RHBT)**

In the original design of BAS there was an admin role, which was intended for the RHBT IT personnel to be able to add, term, or modify a user's role in BAS. This role had no other function within the system. After a consolidation of IT staff to WVOT, it became necessary for the programming staff to take on the Admin role of BAS, and therefore the programmer role was changed to have admin rights. A new role is now being created that would allow only Admin Authorized programmers to have Admin rights in the system. This programming will be completed by November 30, 2009.

We will be moving the access role into the PITS system and eliminating SATT. This will allow the staff to request access to various systems and the system will track the approval process as well as the actual process of giving the access. This will be completed in spring of 2010.

**STATE OF WEST VIRGINIA
SCHEDULE OF FINDINGS AND RESPONSES**

2009-2 YEAR-END FINANCIAL STATEMENT CLOSING PROCESS

State Agency

Retiree Health Benefit Trust (RHBT)

- Criteria:** A critical element of an entity's internal control is its ability to record, process, and to summarize accounting transactions in a timely manner and to prepare financial statements that give a true and accurate assessment of the entity's financial status. Timely and accurate financial statements are crucial to effective decision-making by management.
- Further, a fundamental concept of effective internal control is supervision and review of general ledger activities, including journal entries.
- Condition:** During fiscal year 2008, PEIA management implemented a new information system that is utilized in accounting and financial reporting for RHBT. Prior year system implementation issues continued to impact current year financial reporting. Issues are noted as follows:
- Significant delays in being able to produce reliable RHBT financial statements. Accounting personnel did not fully implement the system in developing year-end financial statements. Rather, many closing entries were posted to the trial balance on Excel-based spreadsheets.
 - Several accounts, including cash and investments, were not properly reconciled in a timely manner, resulting in significant adjustments upon completion of the reconciliations at year-end.
 - Significant issues were noted in the premium billing and collection process as participating agencies and personnel went through the learning curve of understanding the complexity of the system. In addition, the RHBT year-end annual required contribution aging report was provided with errors. At the beginning of the current fiscal year due to held check issues, significant staff time was spent reconciling employer account balances, including the split between PEIA and RHBT amounts due.
 - Delays in accurately reporting the due to/from PEIA balance. For example, we noted one instance in which a reimbursement paid by RHBT to PEIA was recorded through an expense account.
 - Further, we noted that the BAS relies significantly on systematic batched transactions, and there was not a systematic control to verify the batch transactions were balancing prior to posting in GP during the fiscal year. We are not aware of a formal reconciliation process in place to ensure these transactions were properly reported in GP. In addition, controllers and the Premium Accounts Division create and post journal entries in the general ledger without supervisory review and approval of entries.
- Context:** Management was not able to produce accurate and complete financial statements for RHBT until late January 2010.
- Cause:** Management indicated that problems related to the prior year system implementation lasted longer than they expected.
- The current procedures do not require journal entries to be reviewed and approved.

**STATE OF WEST VIRGINIA
SCHEDULE OF FINDINGS AND RESPONSES**

**2009-2 IMPACT OF PRIOR YEAR SYSTEM IMPLEMENTATION AND OTHER MATTERS
(continued)**

State Agency
Retiree Health Benefit Trust (RHBT)

Effect: Management was unable to provide financial statements to executive management and the Finance Board in a timely manner.

Without proper review and approval of journal entries, errors or irregularities could occur and not be detected.

Recommendation: Management has spent a significant amount of time to date in fiscal year 2010 focused on refining fiscal year 2009 and 2010 financial information. Consequently, sufficient resources should be devoted to refining the fiscal year 2010 information to date and in the future to ensure that accurate and timely financial statements are produced prospectively. As part of this process, all accounts should be reconciled in a timely manner. Furthermore, management should evaluate the root cause of the system issues encountered and determine the necessary corrective action to prevent their reoccurrence (e.g., additional training, hiring additional staff, new policies, and procedures). For instance, procedures should be established requiring the reconciliation of the online portal information with the GP national account level information. Management should also implement their procedures to follow up on and resolve participant credit balances in a timely manner.

With the new system, management has the ability to generate premiums/contributions aging reports and collection history. Accordingly, we recommend that management challenge the methodology for estimating the allowance for doubtful accounts and begin using actual collection history by aging category based on hindsight analysis to determine the allowance percentage by aging category.

Policies and procedures should be developed requiring limiting the individuals that have the ability to create and post journal entries in the general ledger. In particular, IT personnel should not have the ability to make journal entries. Additionally, the policies and procedures should require that journal entries be reviewed and approved by supervisory personnel and documentation be maintained supporting the entries.

Views of Responsible Officials and Planned Corrective Actions: PEIA agrees with this issue in that the timeliness and accurate reporting of financial information is imperative. PEIA will be requiring all transactions to be accounted for in the financial system for FY 2010 and instituting more controls on the journal entry process. Moreover, the main cause of un-timely reporting was the cash reconciliation. This issue has already seen substantial improvement during FY 2010 as the frequency of reconciling items has reduced due to previously implemented controls.

PEIA will be reviewing the implementation process for additional controls to provide assurance that all batch postings are accurate before posting.

Beyond the held checks from the beginning of fiscal year 2009, there are no further issues with holding checks and the issues associated.

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